Factors Influencing Voluntary Compliance by Small Businesses: Preliminary Survey Results

IRS Research Conference

June 20, 2013

Why survey small businesses?

- Unreported income by small businesses represents the largest portion of the tax gap
- Sole proprietor income is generally not subject to information reporting
- Relatively inexpensive measures, such as document matching and correspondence examinations, cannot reliably detect such income
- A survey could measure the influence of various factors affecting voluntary compliance
- A survey could measure the types of noncompliance (*i.e.* the noncompliance typology posed by the literature)

Which factors?

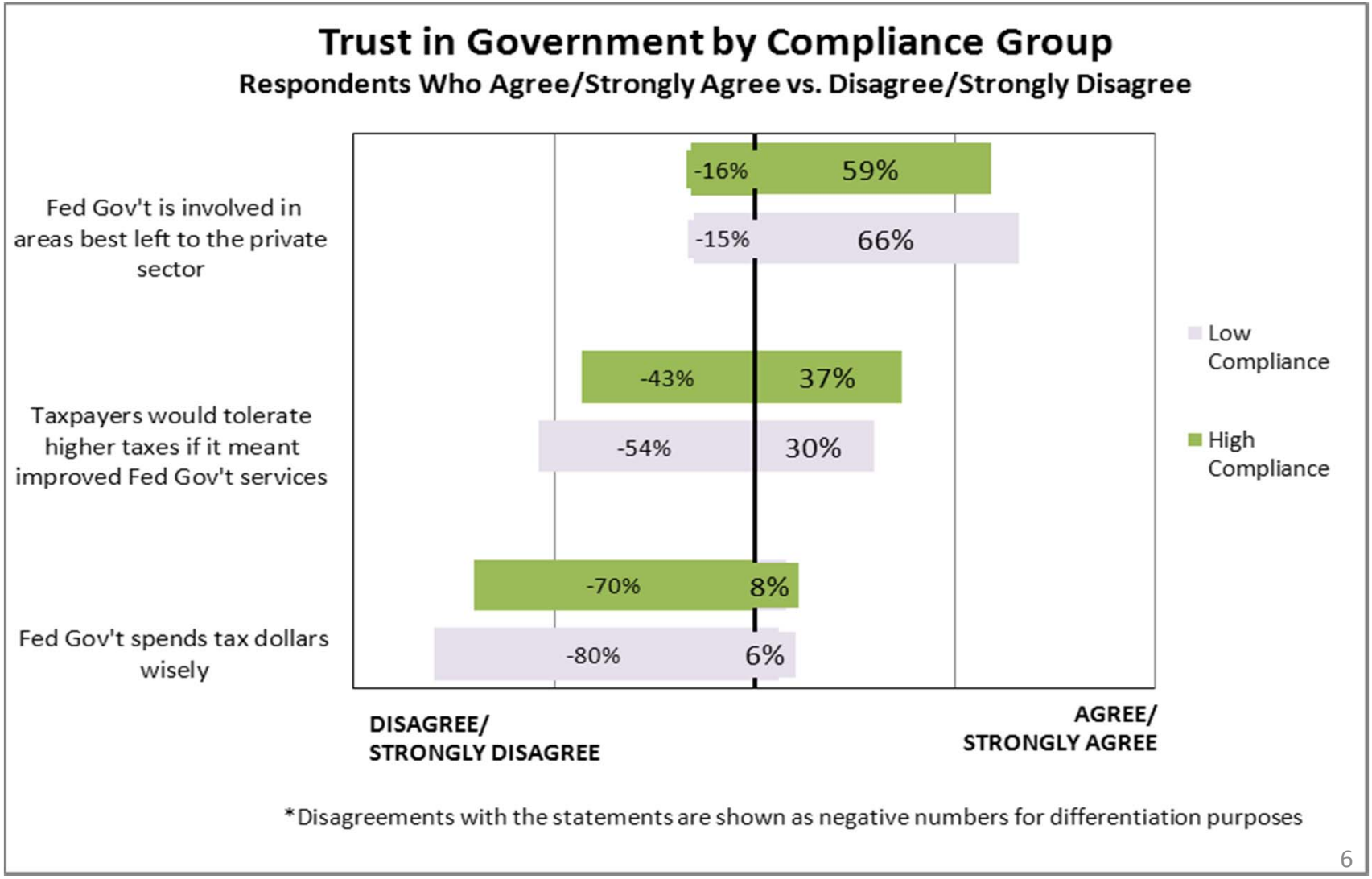
- Deterrence
- Norms
- Tax morale
- Trust
- Complexity and convenience of complying
- The influence of preparers

What did we do?

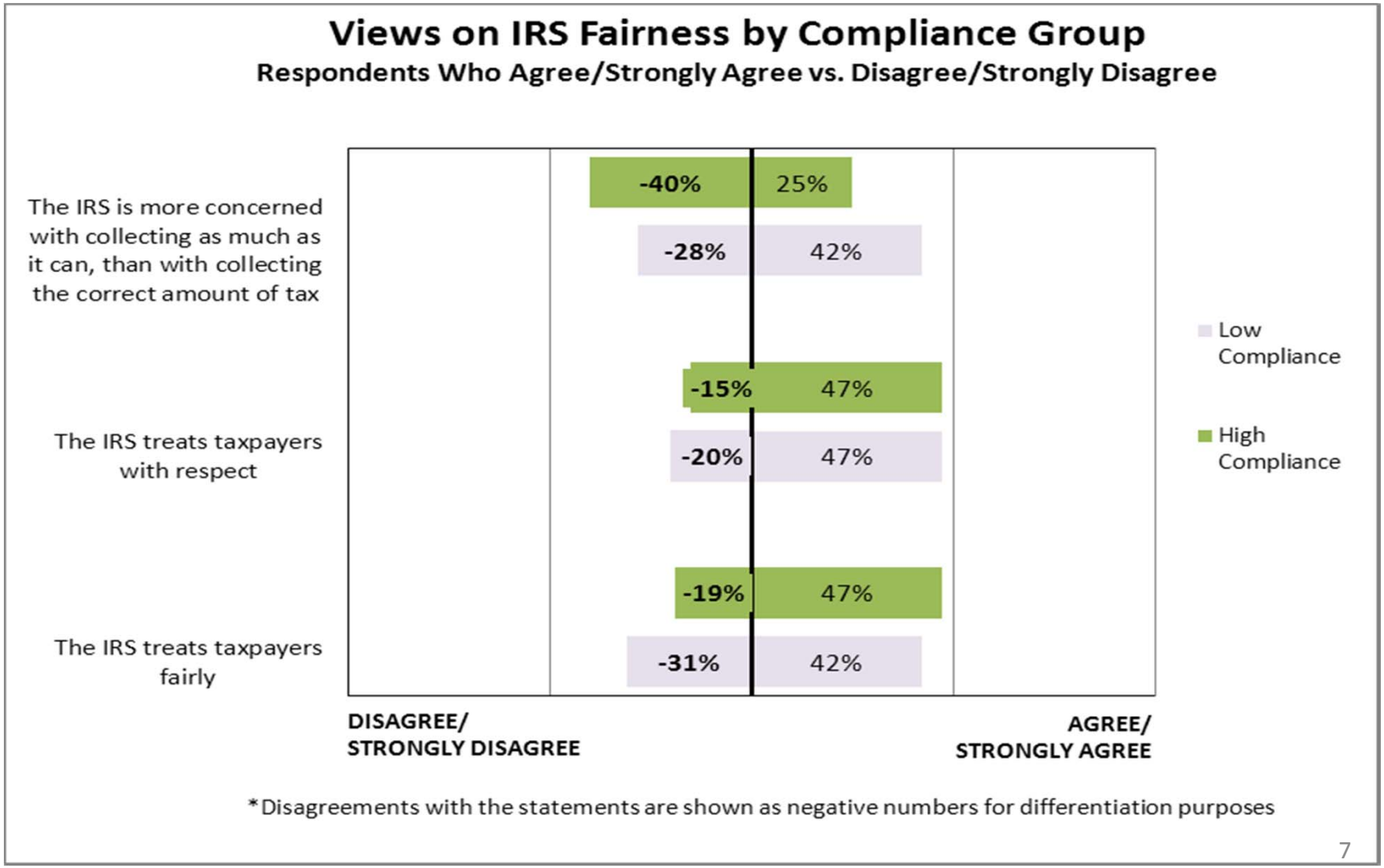
- Two telephone surveys
  - Nationally representative sample of small businesses with high, medium, and low levels of estimated reporting compliance
    - Stratified sample by Examination Activity Code (EAC) – a measure of income
    - Used IRS estimates that an audit would produce an adjustment (Discriminant Index Function, DIF) as a proxy for reporting compliance
  - Community survey of small businesses in selected sites with median DIF scores in top and bottom third
    - Found few high-compliance communities
- Achieved a good response rate
  - 56% for the national sample
  - 54% for the community sample

What did the National Survey reveal?

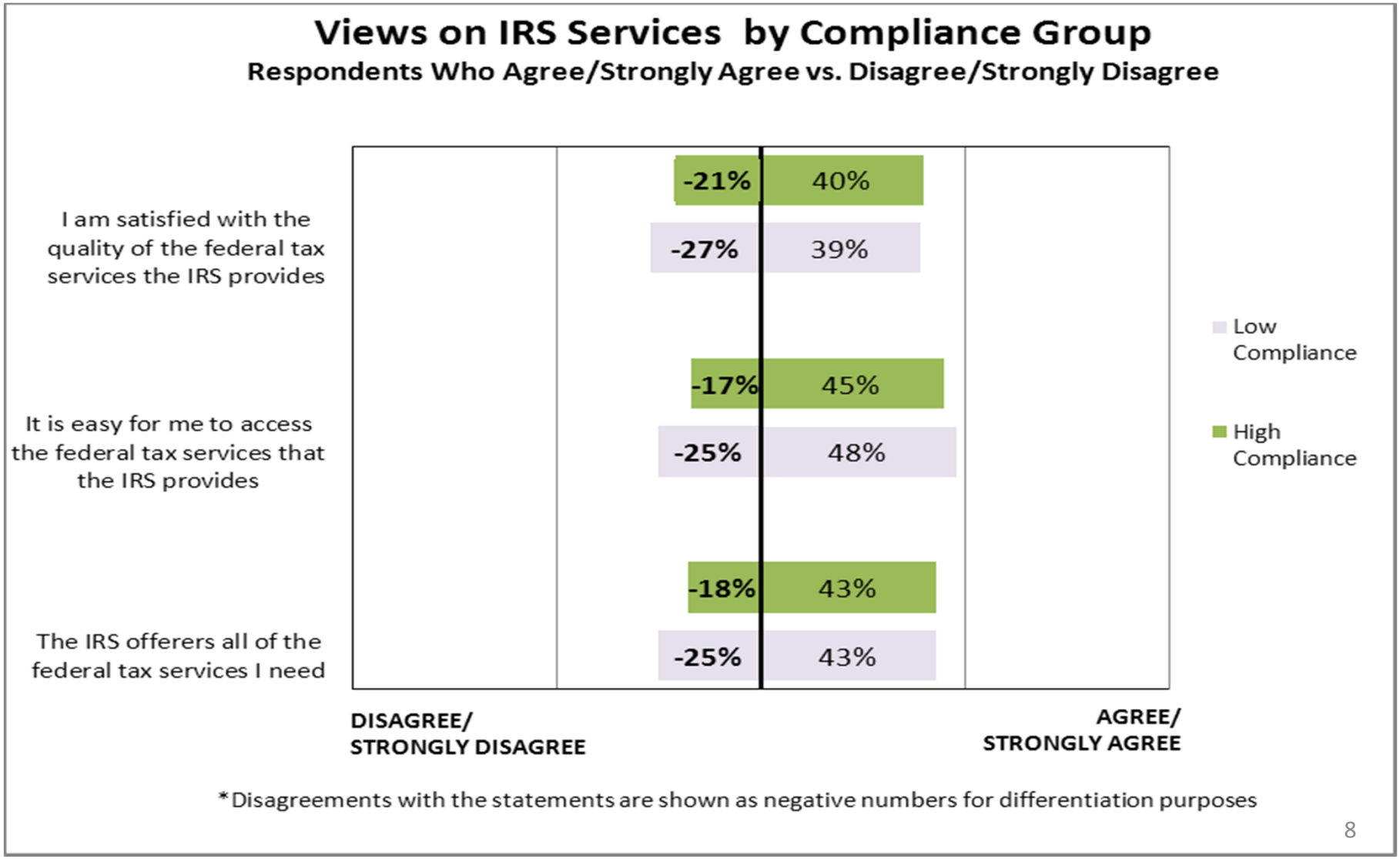
The low-compliance group expressed less trust in government



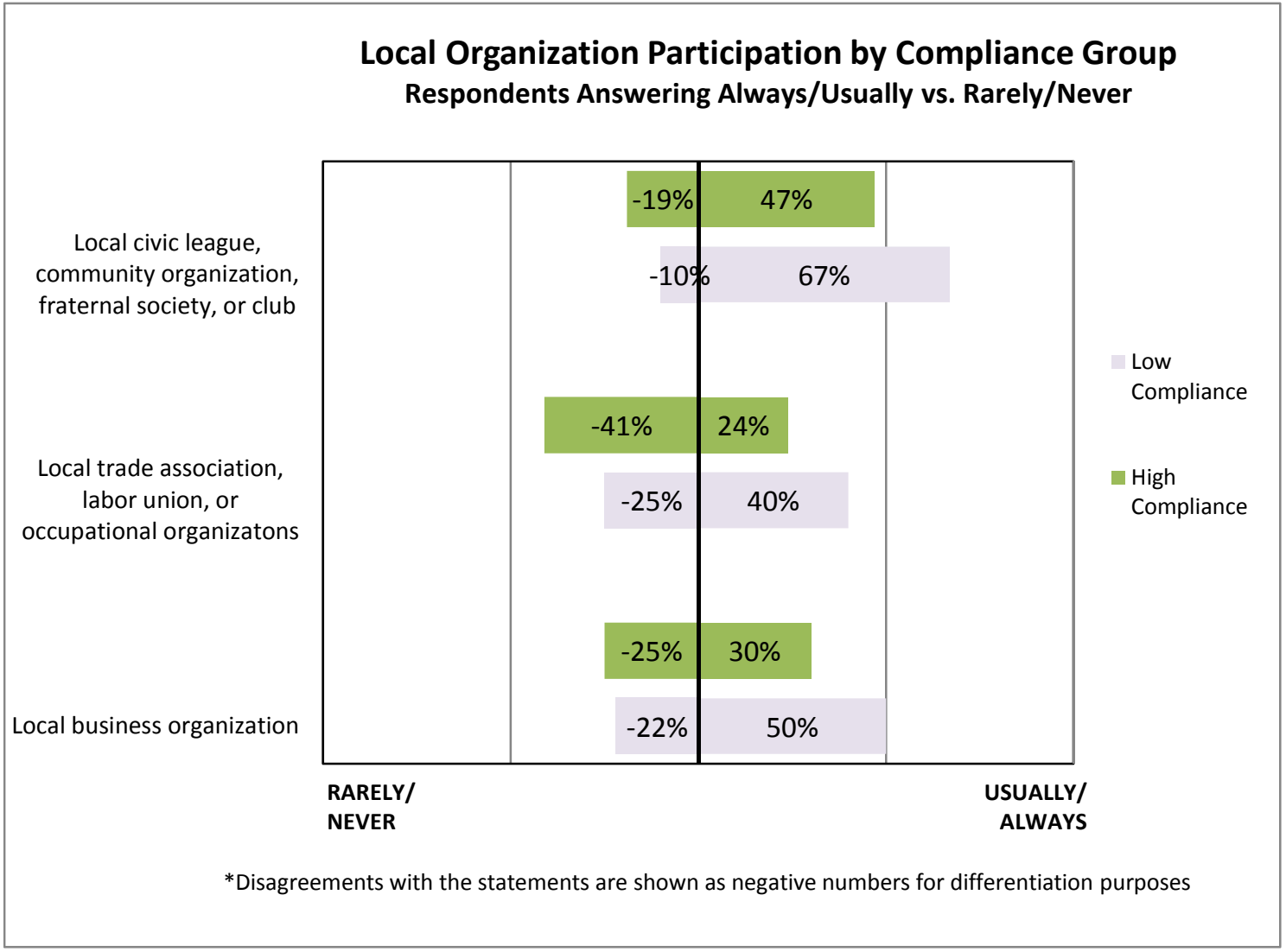
The low-compliance group expressed less faith in the IRS



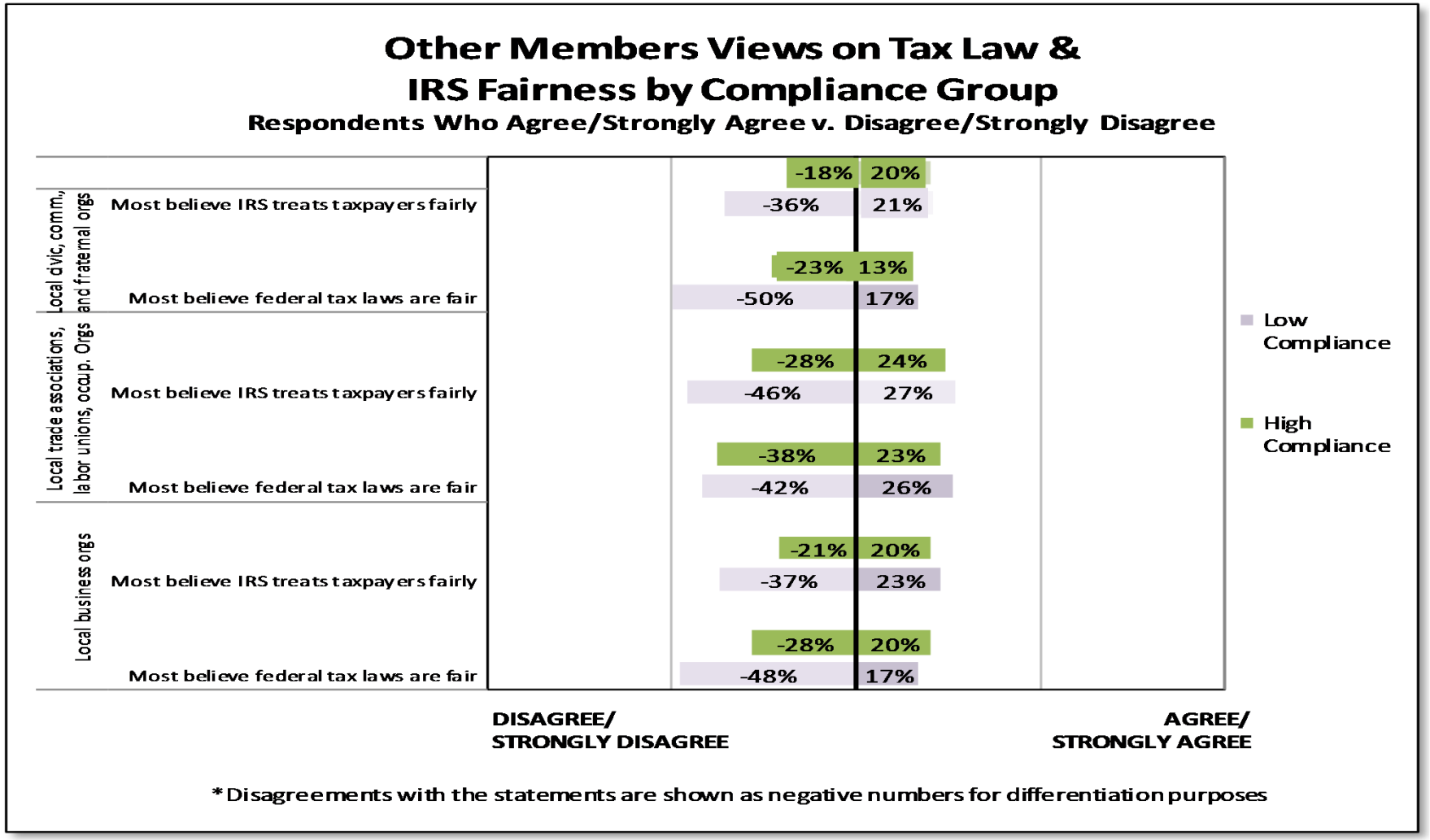
The low-compliance group expressed less satisfaction with IRS services



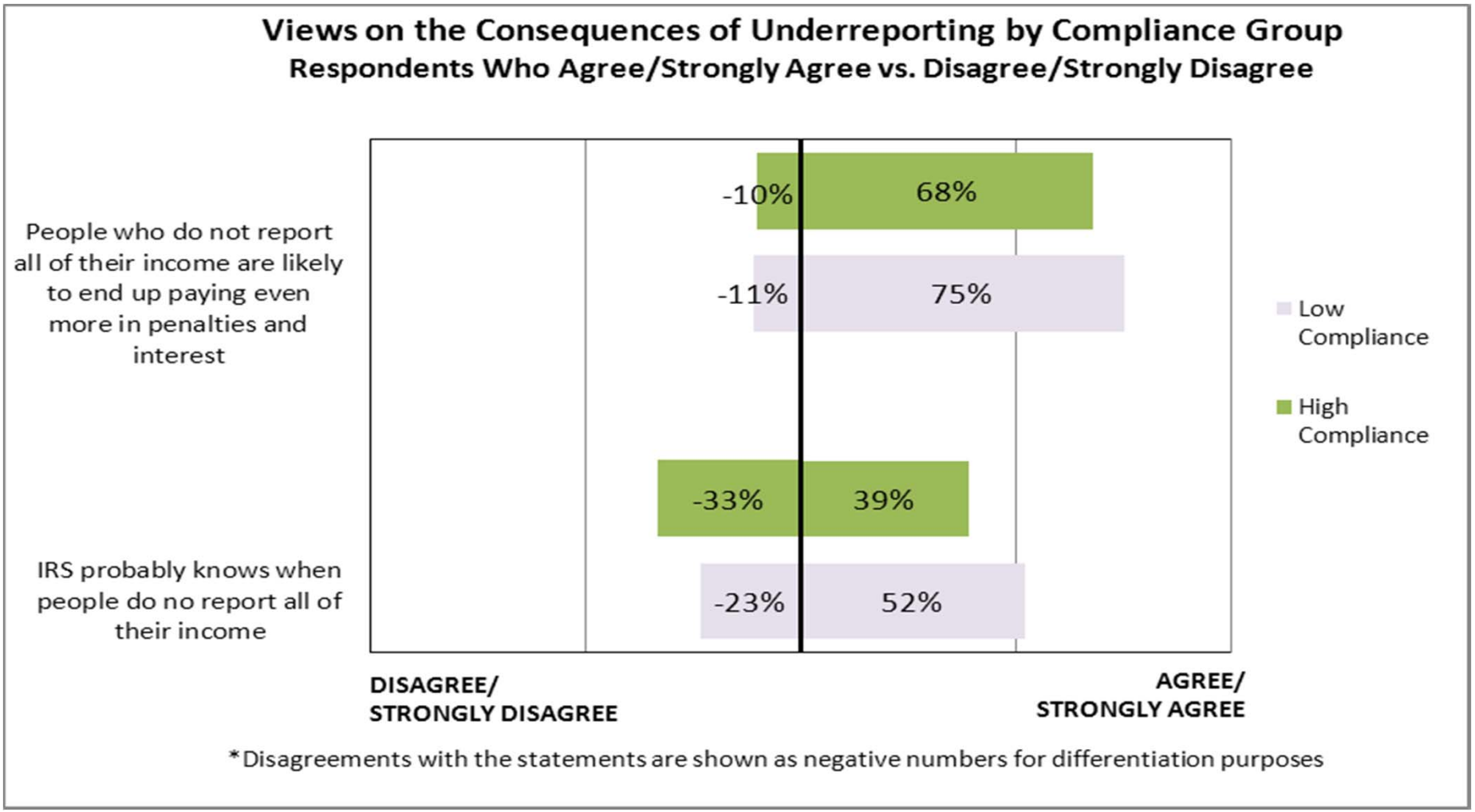
The low-compliance group was more likely to participate in local organizations



The low-compliance group was more likely to report other members of local organizations view the IRS and the tax law negatively

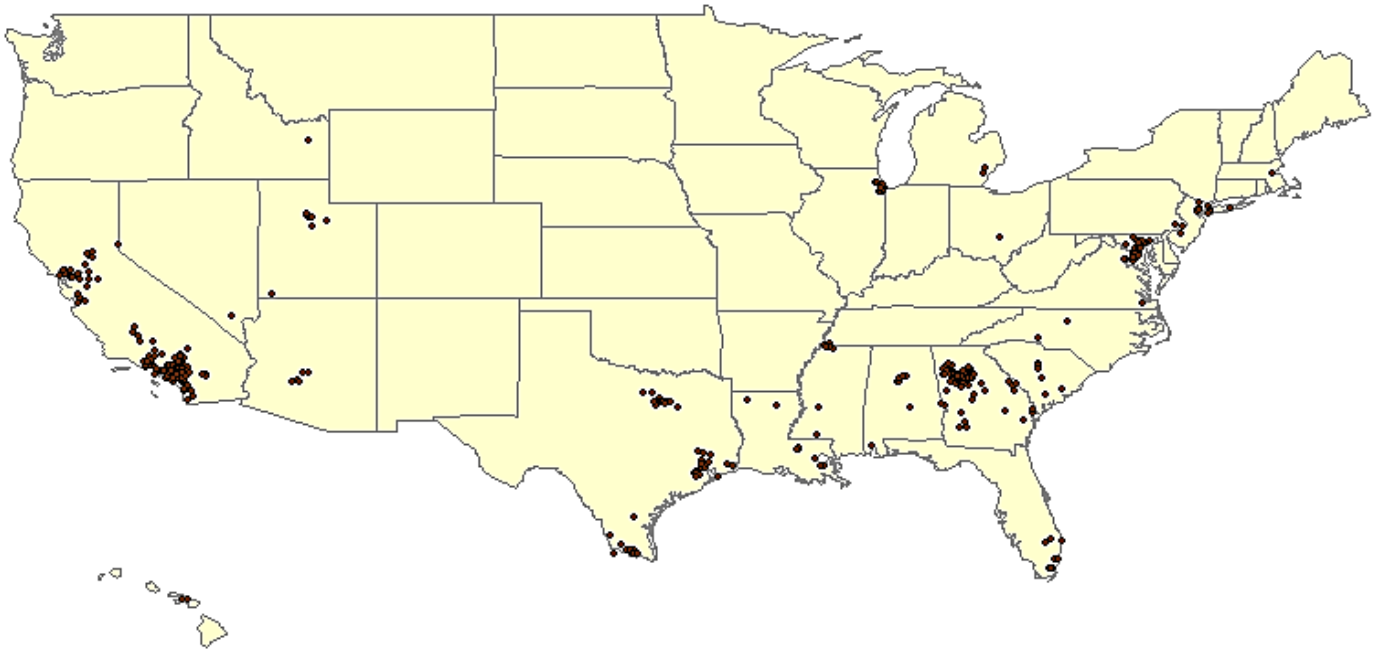


The low-compliance group was less likely to report that it pays to cheat

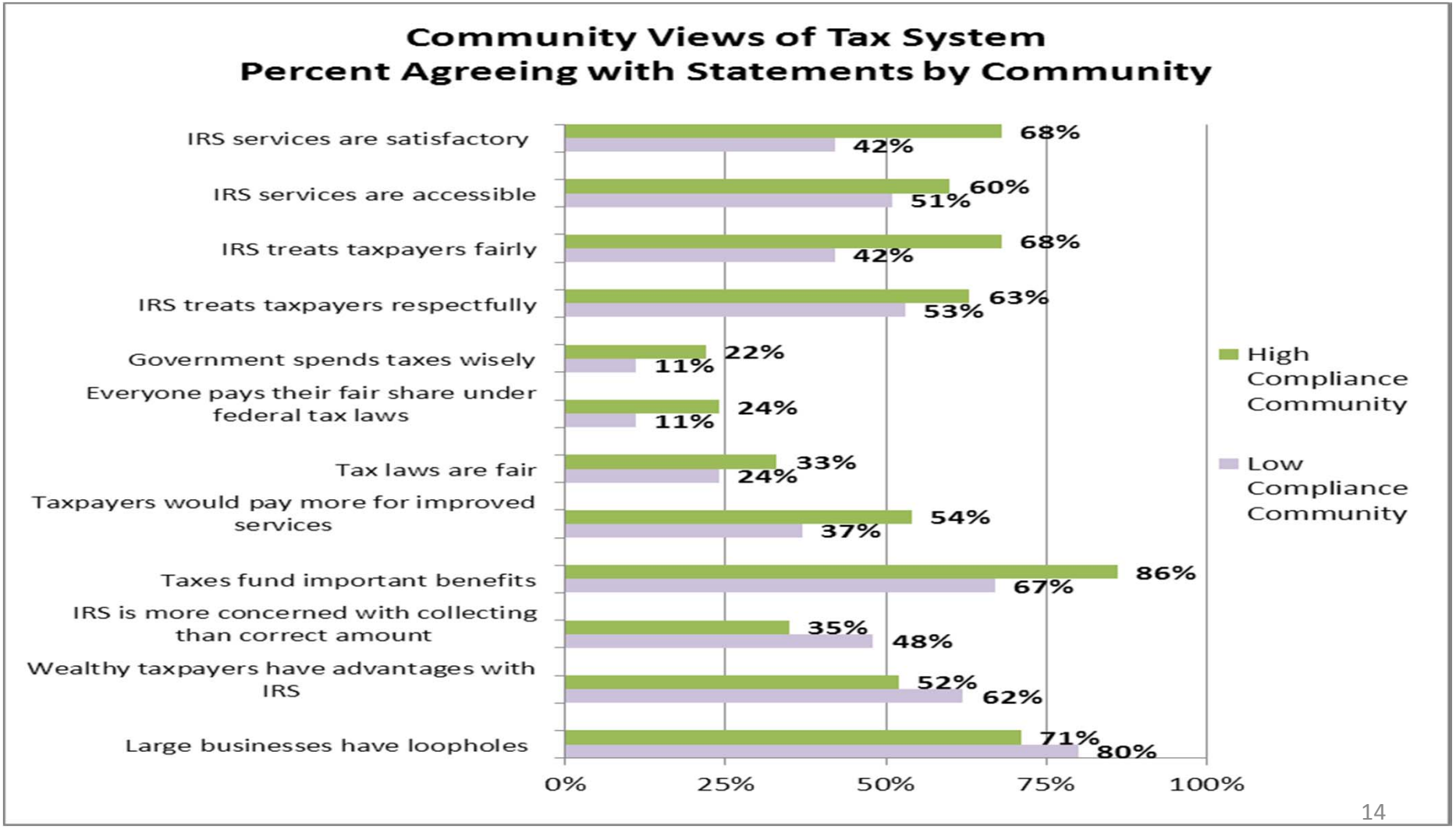


What did the Community Survey reveal?

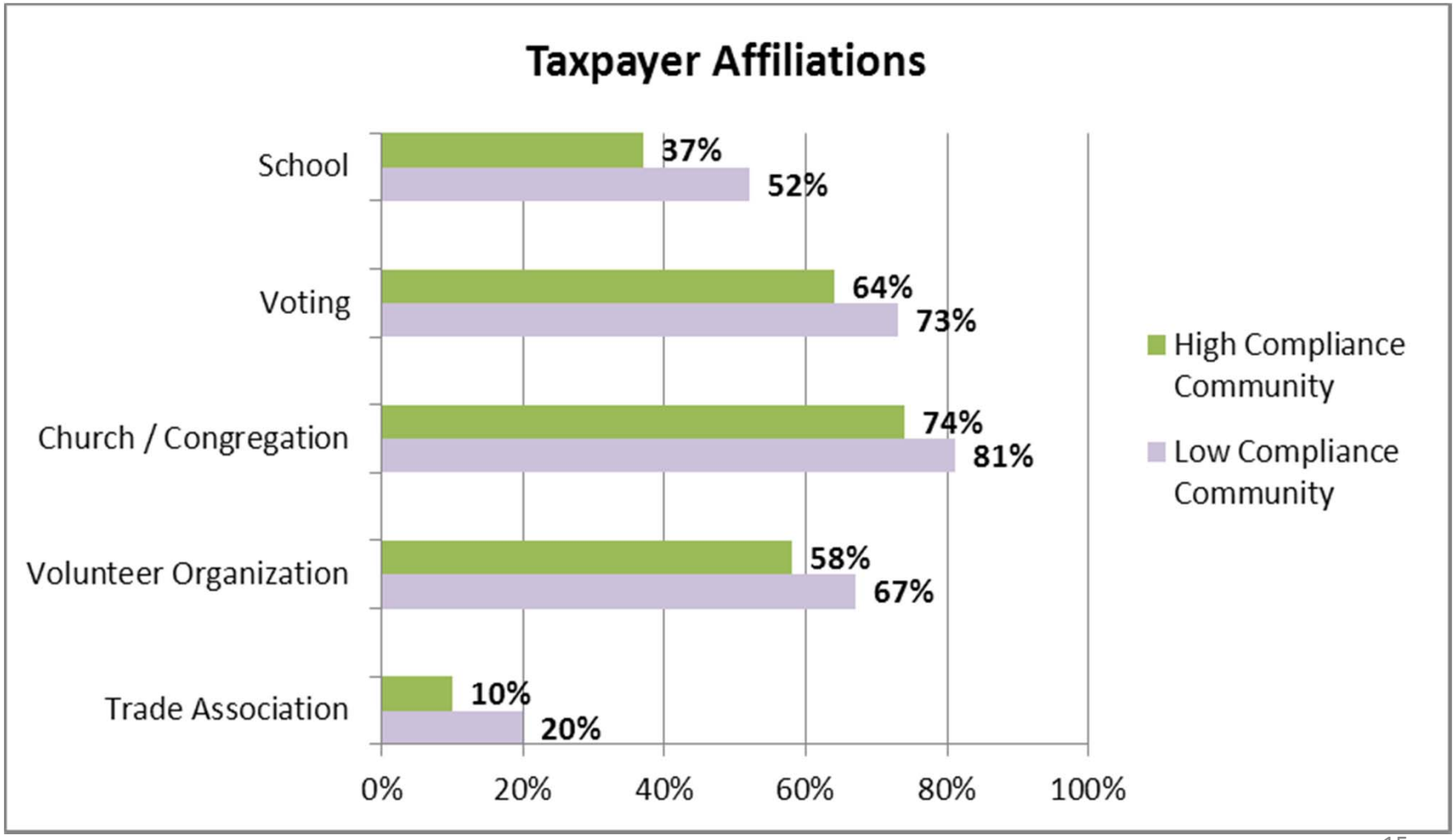
Low-compliance sites



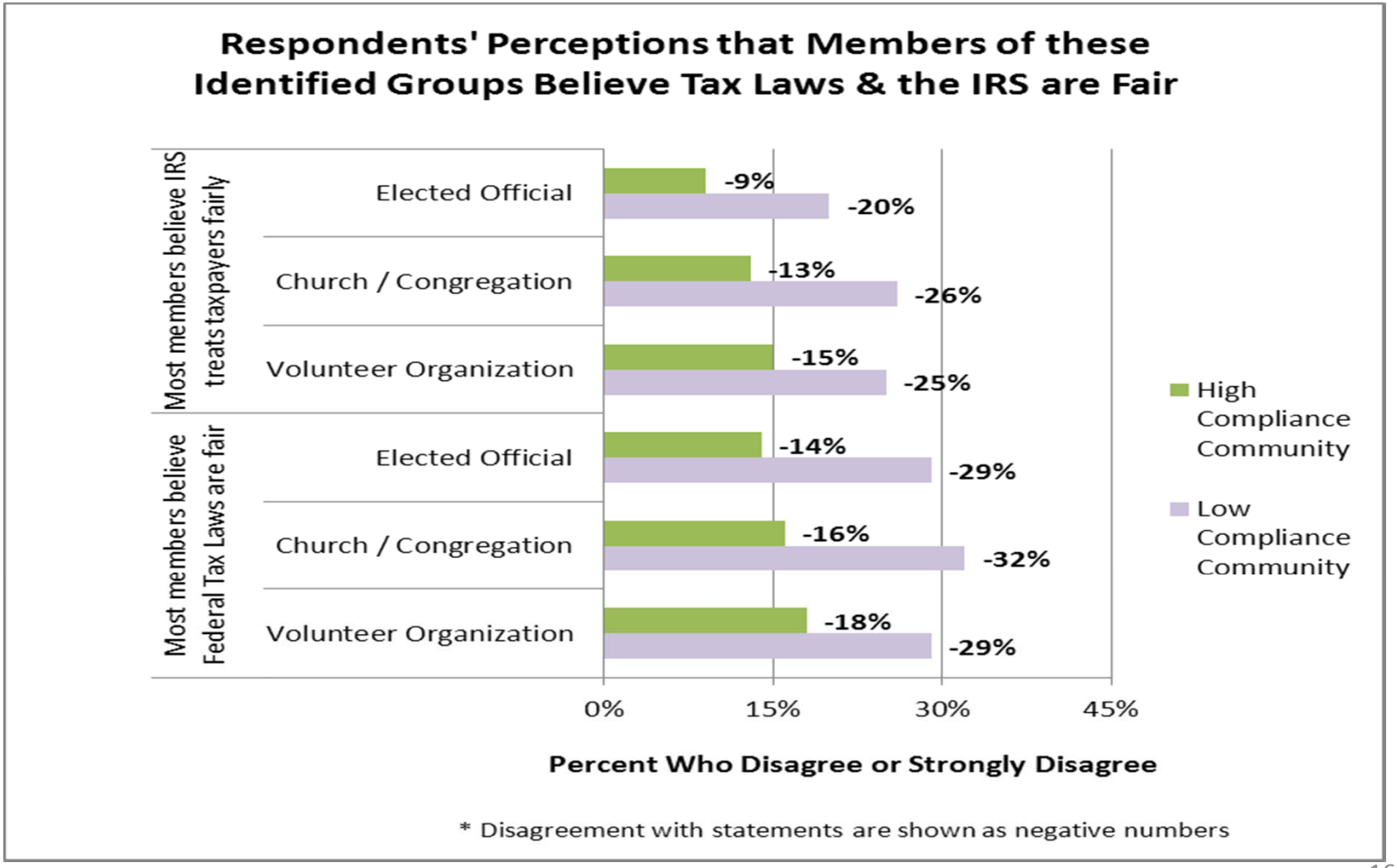
Low-compliance sites viewed taxation more negatively



Low-compliance sites had more civic participation



Low-compliance sites more strongly perceived that their associates believe taxation is unfair



Observations

- Attitudes toward government, law, and IRS may promote
  - noncompliance in the case of norms and distrust
  - compliance in the case of tax morale and trust.
- Low-compliance respondents were more likely to
  - participate in local organizations
  - believe that organization members held negative views about government, law, and IRS.

Implications

- Survey did not reveal much effect of deterrence or complexity on compliance.
- Primary types of noncompliance were social and symbolic, which could be addressed by promotion of trust in government, law, and IRS.