

Do South African Small Businesses Prefer Conservative Tax Advice To Aggressive Tax Advice?

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ABSTRACT

Taxpayers' relationship with tax practitioners may influence tax compliance behaviour. International research has been inconclusive on whether taxpayers prefer conservative tax approaches or more aggressive approaches. There has been only limited research on taxpayers' preferences in South Africa. Several tax relief measures are available to South African small businesses as growing enterprises, but such entities may lack skilled tax staff and they therefore rely on tax practitioners. The first objective of this study is to determine whether such taxpayers prefer conservative or aggressive tax advice from practitioners. The second objective is to determine whether small business taxpayers would continue to use their tax practitioners' services if they disagree with a suggested tax approach. Questionnaires were sent to 50 small businesses in a rural South African town. The data showed that most participating small business taxpayers prefer conservative advice but will agree with the tax practitioner, irrespective of the type of tax advice offered. As long as the advice does not involve tax evasion, they prefer to retain a tax practitioner's services irrespective of the type of advice and their (dis)agreeing with it.

Keywords: Small Businesses Prefer Conservative to Aggressive Tax Advice; South African Small Business Taxes; Tax Practitioner & Small Business Relationship

1 INTRODUCTION

Taxation can be highly complex – even the famous physicist Albert Einstein admitted that income tax was one of the hardest things to understand (Proverbial.net, n.d.). Taxpayers – individuals or businesses – therefore engage tax practitioners in order to file accurate returns (Collins, Milliron & Toy, 1990, p. 15; Tan, 1999, p. 445) and to minimise their tax liabilities (Sakurai & Braithwaite, 2001, p. 14-15). Taxpayers' needs can be met by tax practitioners who can either apply tax law aggressively, or, more conservatively, exploit possible grey areas contained in the various Acts.

Some prior research indicates that taxpayers tend to favour conservative tax reporting by their tax practitioners (Hite & McGill, 1992, p. 398; Tan, 1999, p. 445), but other research indicates that some taxpayers insist on aggressive tax reporting (Schisler, 1994, p. 124-142). Stephenson (2007, p. 418) found that tax practitioners tended to be more aggressive than their clients would prefer, but a 2004 study conducted by Mason and Garrett-Levy (cited in Stephenson, 2006, p. 15) revealed degrees of aggressiveness lower than expected among tax practitioners. The extent to which taxpayers themselves, as opposed to tax practitioners, contribute to tax non-compliance is still unclear. The South African Revenue Service ("SARS") (n.d.(a)) has indicated that tax practitioners play a critical role in shaping taxpayers' attitudes and behaviours, and in defining their actual levels of tax compliance. It can therefore be assumed that the greater the engagement with tax practitioners, the greater the impact of this tax-compliance relationship.

Internationally, taxpayers make extensive use of tax practitioners' services. The Australian Taxation Office indicated that, during 2002, 77% of the Australian population used the services of a tax practitioner or a tax agent to

submit their tax returns (Sakurai & Braithwaite, 2001, p. 9). In South Africa, SARS (n.d.(a)) has noted that the use of tax practitioners has increased significantly. According to SARS, during 2004, approximately 95% of South African small businesses outsourced some of their tax functions to tax practitioners (Killian, Karlinsky, Payne & Arendse, 2007, p. 32-33).

According to the Department of Trade and Industry (“DTI”), South African small businesses as growing enterprises have become the primary focus of the South African government since the start of South Africa’s new democratic era in 1994 (DTI, n.d. p. 3). Various tax relief measures have been introduced to benefit these entities, but such small businesses do not necessarily have skilled tax staff to attend to their tax affairs and therefore often use tax practitioners’ services (Venter & De Clercq, 2007, p. 146). Studies on the relationship between taxpayers and tax practitioners are thus relevant in order to expand on the existing knowledge of taxpayer compliance behaviour. However, only limited research on this relationship has been conducted in the South African context.

Hence, focusing on the above-mentioned information, the main purpose of this article is to report on exploratory research conducted on whether taxpayers in the small business sector in a rural town in South Africa (the name of which cannot be disclosed for the sake of confidentiality) prefer to receive conservative or aggressive advice from their tax practitioners. The specific research objectives were to determine whether small business taxpayers

- prefer to receive conservative or aggressive advice from their tax practitioners; and
- would continue to make use of the services of their tax practitioners if these taxpayers disagreed with the tax approach proposed to them.

The rest of the article is structured as follows: first it reviews the existing literature on taxpayer compliance. The literature review is followed by a description of the research design and methods used. The results of the study are then presented. Finally, the implications and limitations of the findings and directions for further research are discussed.

2 LITERATURE REVIEW

In this section the compliance behaviour of taxpayers is first explained by means of various theoretical frameworks drawn from the literature. A discussion on tax practitioners follows. Finally, small businesses as examples of taxpayers are explored in more depth, because these entities formed the target population of this exploratory study.

2.1 Taxpayer compliance behaviour and its importance

Taxpayer compliance is crucial to the government of any country, because taxation is an important source of revenue for the government. In South Africa, the National Treasury (2009) reported that the budget revenue figure for 2007/2008 of R559 773.8 million was exceeded – the actual revenue received was R572 814.6 million. The budget revenue figure of R559 773.8 million was arrived at after adding non-tax revenue of R11 671.7 million and deducting payments in terms of Customs Union agreements of R24 712.6 million. A revenue budget aids the government with its fiscal aims, such as economic, educational, welfare and other social security services. Non-compliance may have a detrimental impact on the achievement of government objectives by creating budget deficiencies.

Extensive research has been conducted on the numerous factors that may influence taxpayers to engage in tax non-compliance. Various theoretical frameworks have been developed, ranging from economic to social-psychological explanations. These are briefly discussed below.

2.1.1 Economic frameworks

The first economic model to be considered is the classical model posited by Allingham and Sandmo (1972, p. 323-338), which assumes that people are rational, immoral taxpayers who wish to maximise value. This model

regards the tax rate as a factor which determines the benefits of engaging in tax evasion, and the possibility of detection and legal punishment as factors that determine the costs associated with evasion (Webley, Robben, Elffers & Hessing, 1991, p. 8). Taxpayers weigh up the benefits and costs against each other in order to maximise value.

A further development of the classical model is the deterrence theory framework, which is based on the notion that taxpayers' compliance behaviour is shaped by their perceptions of the possibility of detection and legal punishment – this implies that the theory predicts that taxpayers will break the law by practising tax evasion, unless the expected legal penalties are greater than the additional savings from tax evasion (Murphy, 2004, p. 308). The deterrence theory is the main theoretical framework which has been applied to explain taxpayers' compliance behaviour (Smith & Kinsey, 1987, p. 641). Further additions have been made to the deterrence theory framework. One of these additions is the interactive (game-playing) framework by Corchon (cited in Webley *et al.*, 1991:10). Another development in the deterrence theory framework is the prospect theory framework of Kahneman and Tversky (1979, p. 263-291).

2.1.2 Social-psychological frameworks

Apart from the economic frameworks, Lewis (1982, p. 37-120, 215) proposes two frameworks for compliance behaviour in which psychology and economics are combined. One framework combines the interests of the individual and the authorities, while the other framework concentrates on the relationship between tax mindsets and tax behaviour (Webley *et al.*, 1991:14).

In addition to the two frameworks suggested by Lewis, another framework that explains compliance behaviour using a social viewpoint and prospect theory is Smith and Kinsey's (1987, p. 642-657) framework, which distinguishes between the process and content of decisions regarding compliance behaviour.

As the study reported in this article explored taxpayers' preference for the type of advice given by tax practitioners, it is also important to note the regulation theory framework, which deals with the type of advice to be expected from a regulated or an unregulated tax practitioner, and which assumes that taxpayers tend to rely on aggressive tax advice.

2.1.3 The regulation theory framework

Tax practitioners play a critical role in shaping taxpayers' attitudes and behaviour, and in defining their actual levels of tax compliance (SARS, n.d.(a)). Schmidt (2001, p. 170) argues that taxpayers rely more on advice received from professional tax practitioners belonging to a highly regulated institution than from those who do not belong to such an institution, for instance the South African Institute of Chartered Accountants ("SAICA"). Regulated tax practitioners are theoretically considered to be able to offer a greater variety of client services and to negotiate with the taxation authorities (Schmidt, 2001, p. 161). Because of their supposedly greater credibility they may tend to be more aggressive than unregulated tax practitioners in ambiguous tax situations.

2.2 Tax practitioners

The theoretical frameworks indicated that the tax practitioner can influence the taxpayer's tax behaviour and illuminated the reasons for taxpayers to utilise the services of tax practitioners.

2.2.1 The demand for and role of tax practitioners

It has already been indicated in the introduction that taxpayers engage extensively with tax practitioners. According to a briefing note on the revised draft Regulation of Tax Practitioners Bill issued in June 2008 (SARS, n.d.(a)), nearly 23 000 tax practitioners are registered with SARS. It is thus evident that clients rely heavily on their tax practitioners and trust them with their tax affairs. The most important role tax practitioners can play for taxpayers is to provide assurance that their tax affairs are under control and that their tax-related actions are lawful (Sakurai & Braithwaite, 2001, p. 20).

Tax practitioners give their clients advice to assist them with minimising their tax liability, in some cases opting for choices that incur the risk that the return might be challenged. Klepper, Mazur and Nagin (1991, p. 168) indicate that a tax practitioner's advice can take two forms. With the tax practitioner's specialised knowledge and experience, the practitioner could merely indicate any reporting positions to the client which are likely to be challenged by tax authorities. The tax practitioner could also advise the client on how to take advantage of any ambiguity in the tax law which may affect the client's reporting position; in other words, aggressive tax advice from the tax practitioner.

Sakurai and Braithwaite (2001, p. 12) found that honesty and risk-aversion were the two most important characteristics that taxpayers require of tax practitioners, while the least popular are creativity and aggressiveness. Other desired characteristics in tax practitioners include their ability to interpret tax ambiguities, skills in tax minimisation, and the ability to warn clients against illegal tax-planning schemes (Sakurai & Braithwaite, 2001, p. 14-15).

A number of studies suggest that the main reason that taxpayers engage with tax practitioners is to file an accurate tax return. Tan (1999, p. 439) has found that taxpayers engage with tax practitioners mainly in order to file an accurate tax return and to avoid serious tax penalties. In a study conducted by Collins, Milliron and Toy (1990, p. 15), 70% of the participants confirmed that they preferred accuracy, while only 25% preferred tax minimisation. These choices suggest that taxpayers prefer conservative advice, which is also indicated in the studies by Tan (1999, p. 445) and Hite and McGill (1992, p. 398).

It appears that many taxpayers do not feel sufficiently competent to file an accurate tax return on their own. Sakurai and Braithwaite, who conducted a study on Australian citizens, found that only 12% of the participants felt capable of completing their own tax returns without any external assistance (2001, p. 11-12). Of these respondents, 36% did not feel at all competent to complete their own tax returns. In another study, Rupert and Fischer (1995, p. 51) reported that taxpayers who engaged with tax practitioners were less familiar with the marginal tax rate applicable to them than those who prepared their own tax returns.

Similar findings were reported in a South African study that found that most South African small businesses outsource their tax functions. The researchers found that these small businesses largely outsourced their tax responsibilities because of a lack of skilled tax personnel and insufficient time required to manage tax functions. Compared to the first two reasons, cost saving was not regarded as a significant motivation for outsourcing tax responsibilities (Venter & De Clercq, 2007, p. 131-146). It became clear, therefore, that the needs of the taxpayer had to be matched with those of the tax practitioners.

2.2.2 Matching the needs of taxpayers and tax practitioners

Sakurai and Braithwaite (2001, p. 20) found that taxpayers prefer tax minimisation with conflict avoidance to tax minimisation involving creative accounting and aggressive tax planning. This indicates that taxpayers are cautious about the extent of the risk they wish to engage in (Sakurai & Braithwaite, 2001, p. 20). Although taxpayers are considered able to differentiate between low- and high-risk tax minimisation, there is still a possibility that they could engage with tax practitioners that share their preferences and that the two parties could, in some instances, influence each other towards tax evasion (Sakurai & Braithwaite, 2001, p. 21) – taxpayers tend to look for tax practitioners who match their needs (Sakurai & Braithwaite, 2001, p. 18). However, there is a risk that tax practitioners and taxpayers could misinterpret each other's messages as to what precisely a low- or a high-risk tax minimiser entails. This could ultimately result in their failing to meet each other's expectations (Sakurai & Braithwaite, 2001, p. 22).

In addition, Schmidt (2001, p. 170) observes that tax practitioners should be mindful of communicating information accurately to their clients as such information could influence their clients' behaviour. Schmidt (2001, p. 170) reports, that when a tax practitioner communicated to a client that the probability of an audit or a penalty was low, most taxpayers overestimated this low probability. According to Christensen (1992, p. 78), the greatest mismatch between client and tax practitioner tends to occur when a tax practitioner greatly underestimates a client's preference for conservative tax advice. Stephenson (2007, p. 418) also found that tax practitioners were more

aggressive than their clients wanted them to be. It is interesting to note that a study conducted by Mason and Garrett-Levy in 2004 (cited in Stephenson, 2006, p. 15) delivered results to the contrary, which revealed lower than expected degrees of aggressiveness among tax practitioners.

Studies by Tan (1999, p. 431-447) and Hite and McGill (1992, p. 389-403) also found that taxpayers preferred conservative advice. In these studies they presented an ambiguous tax situation to a sample of taxpayers in which the taxpayers had to indicate their preference for the type of tax advice they would like. The scenario technique was used to address the first objective of the current study, namely to determine whether small business taxpayers, within a South African environment, prefer to receive conservative or aggressive advice from their tax practitioners.

The scenarios sketched in the current exploratory study to test the taxpayers' preference for the type of advice consisted mainly of ambiguous tax situations involving an ambiguous tax inclusion and an ambiguous deduction. Christensen and Hite (1997, p. 8-9) found that taxpayers believed that there was a greater likelihood that an audit would detect an understatement of income than an overstatement of deductions. Hence, logically, taxpayers would rather deduct an ambiguous expense than exclude an ambiguous income item from their tax returns (Christensen & Hite, 1997, p. 14). This finding is borne out by the findings of an American study by Hite and Hasseldine (2003, p. 7) on tax audits by the Internal Revenue Service ("IRS") office from October 1997 to July 1998. The authors found that there were more adjustments relating to incorrect tax deductions (59%) than for taxable income (22%). This indicates a preference for aggressive reporting in the case of tax ambiguity on deductions (Hite & Hasseldine, 2003, p. 5).

In studies by Tan (1999, p. 431-447) and Hite and McGill (1992, p. 389-403), taxpayers were also asked whether they would disengage from their tax practitioner on the basis of the advice they received. If taxpayers disagreed with aggressive advice, it strengthened the hypothesis that taxpayers prefer conservative advice. In the study by Hite and McGill (1992, p. 398), the taxpayers claimed that they wanted to terminate the services of their tax practitioners when they disagreed with aggressive advice received. However, Tan (1999, p. 443) found no significant evidence to indicate that taxpayers who preferred conservative advice would in fact go so far as to disengage from their tax practitioners if they were given aggressive advice. These results did not support the findings by Hite and McGill (1992, p. 389-403) who found that those participants who agreed with the advice wanted to continue making use of the tax practitioner's services, while those who disagreed claimed that they wanted to disengage from the practitioner. Tan (1999, p. 441) also showed that there was a greater willingness to continue engaging with a tax practitioner when conservative advice was provided. This addresses the second research objective of this study, namely whether the taxpayer would continue to make use of the services of their tax practitioners if these taxpayers disagreed with the tax approach proposed to them.

The finding by Tan (1999, p. 443) that there was no significant evidence to indicate that taxpayers would disengage from their tax practitioners, even if they received aggressive advice with which they disagreed, emphasises the importance of client trust in tax practitioners. It is clear that tax practitioners have a very important role to fulfil.

2.2.3 The regulation of tax practitioners in South Africa

The process of regulating South African tax practitioners is still underway. The process involves two phases, as explained in a briefing note by SARS (n.d. (a)).

The first phase requires the registration of tax practitioners with SARS. This was achieved with the introduction of section 67A into the Income Tax Act by the Second Revenue Laws Amendment Act, Act 34 of 2004 (South Africa), promulgated on 24 January 2005. This section prescribes that on 30 June 2005 or otherwise 30 days after a natural person starts to render tax practitioner services, as discussed in this section, such a person should register as a tax practitioner with SARS.

The second phase involves the creation of an independent regulatory board for tax practitioners. This board will be regulated by its own law and Acts (SARS, n.d.(b)). This phase with regard to the creation of an independent

regulatory board is still in progress, with only a revised draft Regulation of Tax Practitioners Bill currently available. The revised version of the draft Regulation of Tax Practitioners Bill was issued in June 2008 (SARS, 2008). Until the Regulation of Tax Practitioners Act has been finalised and effectively brought into operation, conditions may exist which could create the opportunity for tax practitioners to follow more aggressive tax approaches. An example of this may be the case of tax practitioners who do not belong to any statutory body and who are therefore not controlled by any code of professional conduct or subject to that body's disciplinary procedures.

In the final section of the literature review, small businesses are discussed in more detail. Despite the fact that there are many taxpayers in South Africa, this exploratory study focused only on small businesses as taxpayers.

2.3 Small business

Within the South African context, a variety of taxpayer types exist. The following subsections explain the reasoning behind choosing small business taxpayers as the unit of analysis.

2.3.1 Definition of a small business

There are various definitions of a small business in the South African context, ranging from economic to taxation perspectives. It was decided to look at this concept from a tax perspective.

From a taxation perspective, section 12E(4)(a) of the Income Tax Act (South Africa, 1962) provides a definition of a small business corporation. This section lists all the requirements that should be met in order for an entity to qualify as a small business corporation and to qualify for some taxation relief. One of the requirements is that the gross income (similar to turnover for taxation purposes) of such a concern for a given tax year should not be greater than R14 million. For the purposes of this study, the taxation perspective, and particularly the requirement of a turnover of R14 million or less, was used for the target population.

2.3.2 The importance of small businesses in South Africa

According to the DTI (n.d., p. 3), small business development became a primary focus for the government at the start of South Africa's new democratic era in 1994. In March 1995, the first comprehensive policy and strategy on small business development was prepared when the government published its *White Paper on the national strategy for the development and promotion of small businesses in South Africa*. The policy and strategy included the measures to stimulate the creation and growth of small businesses, for example, streamlining regulatory conditions, creating access to information, finance, providing training and introducing differential taxation. The DTI (2005) stressed that these businesses are important because small businesses stimulate economic growth and play a significant role in black economic empowerment. Small businesses also provide a way by which to achieve wealth distribution and more equitable growth. They also play a crucial role in technical and other innovations. Finally, small businesses could possibly address the increase in the unemployment rate. Small businesses contribute 36.1% to South Africa's gross domestic product ("GDP") and contribute to 68.2% of employment in the private sector. In the agriculture, construction and retail sectors, more than 80% of the total workforce is employed by small businesses (Killian *et al.*, 2007, p. 17).

Ahmed and Braithwaite (2005, p. 554) found that small business taxpayers are generally law-abiding and that they take their tax responsibilities seriously. However, in an American study conducted by Hite, Stock and Cloyd (1992, p. 26), it was found that approximately one fifth of small businesses either understate their taxable income or overstate their tax deductions.

2.3.3 Small businesses and tax practitioners

In South Africa, a study conducted by Venter and De Clercq (2007, p. 146) showed that small businesses tend to outsource their tax functions because these businesses lack skills and time. During 2004, SARS determined that about 95% of small businesses needed to outsource some of their tax functions to tax practitioners (Killian *et al.*, 2007, p. 32-33). The increase in the use of tax practitioners in South Africa may therefore also be a result of the

need for small businesses to outsource their tax functions. Taking the above findings into account, it was considered both interesting and valuable to explore the preferences of small businesses for either conservative or aggressive advice.

3 RESEARCH METHODOLOGY

This section of the article describes the research methodology utilised in obtaining the research reported in this article.

3.1 Sampling

The target population consisted of small businesses in a rural town in South Africa (not named for reasons for confidentiality) from July 2009 to September 2009. The target population was selected with convenience and cost in mind. The medium-sized town has a population of approximately 250 000 people. The differentiated economy of the town includes nearly 600 commercial businesses, agricultural and industrial activities and industries. An alphabetical list was obtained from the chairperson of the town's business association. The list contained the contact details for 788 names, of either businesses or their owners. According to the chairperson, the list comprised the local businesses as listed in the 2007/2008 telephone directory. This was also the most recent list available at the time of sampling. These businesses were regarded to be members of the business association. It is important to emphasise that this was an exploratory study that attempted to highlight areas for future research. A sample size of 50 participants was considered to be appropriate for this study.

The sampling design consisted of systematic sampling, using a predetermined sequence (Leedy & Ormrod, 2005, p. 203). A sample of 50 businesses from the list of 788 businesses was mathematically selected by way of division, so that every 16th business on the list was selected. A computer-simulated random number was obtained, namely 11. From that number on, every 16th business was selected. The sampling method used was considered to be the most logical and feasible manner to identify the target population and units of analysis for this study. The list was checked for completeness regarding the numerical sequence of the businesses. It was important to obtain 50 completed questionnaires by means of the sampling design to ensure a 100% response rate.

3.2 Data collection

In this study, Questionnaires were used to collect the data. In order to determine whether participants would experience any problems in answering the questionnaire and make appropriate adjustments, a pilot study was conducted as recommended by Saunders, Lewis and Thornhill (2007, p. 386). The questionnaire was pre-tested by two academic colleagues and three acquaintances of the researchers who were qualifying small business owners. All comments received were taken into account and the questionnaire was amended accordingly before use on the sample.

The owners or financial representatives of the businesses were contacted telephonically to enquire whether they would participate in the study by completing the questionnaire. If a business did not meet the two main criteria, namely having a turnover of less than R14 million per year and using the services of a tax practitioner, the next business on the list was selected as part of the sample. The participants were asked whether they would prefer to schedule an appointment to complete the questionnaire in the presence of the researcher or whether they would rather complete the questionnaire in their own time. The questionnaires were designed to be self-administered and were delivered by hand in a sealed blank envelope to either the participants themselves or to their administrative officer. Only the owners of the businesses or financial supervisors could receive and complete the questionnaire. A follow-up telephone call was made to participants who had indicated that they preferred to complete the questionnaire in their own time but did not respond within a week. The questionnaires were collected by hand after completion.

3.3 Questionnaire design

This study was based on Tan's study (1999, p. 431-447) which was conducted on businesses in general, not specifically on small businesses, in the Manawatu region of New Zealand. The research reported in this article is not an exact replication of Tan's study or questionnaire, as it was specifically tested on small businesses, and it was also tested in a different geographical area, namely a rural town in South Africa. The questionnaire was designed taking cognisance of previous research, as discussed in the literature review.

3.4 Data analysis

Numerical codes were assigned to all the questions. The completed questionnaires were collected and the numerical codes were entered in the coding boxes on the questionnaires. The analysis was carried out by the Department of Statistics at the University of Pretoria. The coded responses were then captured and analysed by means of the Statistical Analysis Software (SAS) package Version 9.2.

Ethical clearance was obtained from the Faculty of Economic and Management Sciences' Research Ethics Committee. Research ethics applied in this study, including informed consent from the participants, voluntary participation and a guarantee of the anonymity of participants and confidentiality of the data.

3.5 Delimitations

The following delimitations applied to this exploratory study:

- The target population was comprised of small businesses in a rural town in South Africa, the name of which cannot be disclosed for ethical reasons. Different results might be obtained from another target population.
- Franchises or branches whose head offices dealt with their financial affairs and whose head offices were located elsewhere were excluded from the sample in this study, as they were presumed to have a total turnover exceeding R14 million.
- The scenarios sketched in the questionnaires were kept straightforward. In reality, various factors would be considered and effectively communicated by tax practitioners to their clients before a decision was made on a tax-ambiguous situation. Taxpayers would also consider more eventualities before deciding to disengage from their tax practitioners.
- Other variables, such as the preference of different South African population groups, past experiences with tax practitioners, SARS audits and/or tax penalties, may have an impact on taxpayers' preference for the type of advice they receive. The effects of these variables were, however, not tested in this study.
- Survey-based research was chosen for this study, which was limited by potential participant bias where self-reporting was used (Saunders *et al.*, 2007, p. 386).
- The scope of the study was limited, because it focused only on small businesses in a rural town in South Africa. Thus the purpose was not to generalise conclusions to all small businesses in South Africa, and the results should be interpreted with caution.

4 RESULTS

Within this section the results obtained through conducting the research are discussed.

4.1 Conservative or aggressive advice

The study aimed to determine whether small-business taxpayers prefer conservative or aggressive advice from their tax practitioners.

Figure 1 indicates the participants' responses as to why they engaged with a tax practitioner.

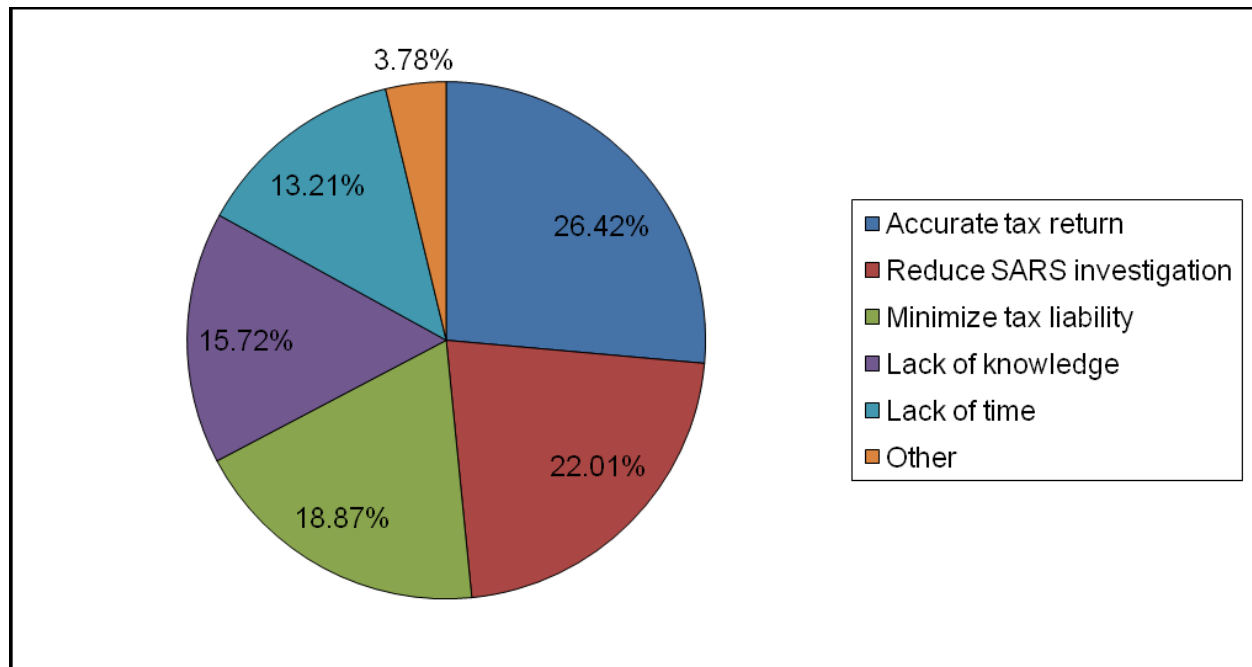


Figure 1: Reasons for engaging with a tax practitioner

It is evident from the data obtained that the main reason for the participants (26.42%) to engage with a tax practitioner was to file an accurate tax return. This finding is in line with the findings of previous studies, such as those by Tan (1999, p. 445) and Collins *et al.* (1990, p. 15), as indicated in the literature review. The second main reason was to reduce the risk of being investigated by SARS (22.01%). These two main reasons are regarded as indicative of a preference for conservative advice.

However, the third main reason was to limit the tax liability to a minimum (18.87%), which is clearly indicative of a preference for aggressive advice. Only 15.72% of the respondents indicated a lack of own knowledge and/or skilled personnel as a reason and 13.21% indicated their lack of time as a reason. A small percentage of 3.78% of participants chose other reasons for using the services of a tax practitioner.

The second question requested the participants to indicate whether, in general, they preferred to receive conservative or aggressive tax advice from a tax practitioner. The information gathered shows that the majority (62%) of the participants indicated that they preferred conservative advice, while 38% indicated that they preferred aggressive advice.

In view of the above findings it appears that the participants preferred conservative advice.

The participants were prompted to give reasons for their preference for a certain type of advice. The majority indicated that their preference for conservative advice was prompted by their desire to do the correct thing and not take chances. Other reasons given were that they wanted a good relationship with SARS, that they did not want to waste time and money on addressing queries from SARS, and that they did not want to pay tax penalties and interest. Most of those who preferred aggressive advice argued that they regarded the Act as open to challenge and that they wanted to benefit their concerns by limiting their tax liability to a minimum. These findings addressed the first research question.

4.2 Relationship with tax practitioner

The second research objective was to determine whether small business taxpayers would continue to use the services of their tax practitioners if they disagreed with the tax approach proposed to them. The study attempted to address this research objective with the following question: “Should you in any situation disagree with the advice of a tax practitioner due to ethical or technical reasons, would you continue to use him or her?”

The participants expressed strong feelings about the fact that they would discontinue their use of a tax practitioner’s services if they disagreed on ethical or technical grounds. This was confirmed by 52% of all the participants. If the participants who were uncertain (24%) were excluded from the results, it would indicate that approximately 68% would disengage from the practitioner and only 32% would still continue to use the services of a particular tax advisor with whom they disagreed. In support of their claim, the majority indicated that they felt strongly about being honest and ethical. The participants did not want to be associated with tax evasion.

4.3 Replication of scenarios tested by Tan

Finally, the study aimed to support the abovementioned findings by testing a number of different scenarios replicated from the study performed by Tan (1999, p . 431-447). The participants had to assume that there was no clear authority in the Act or any interpretation of the tax treatment of a certain income and expense. In order to substantiate the first objective, the participants had to indicate their response to each type of advice received by the tax practitioner in different scenarios. The different scenarios, together with the responses of the participants regarding their preferences for the type of tax advice, are set out in Table 1.

Table 1: Responses regarding taxpayers’ preferences for a particular type of tax advice

Tax advice with regard to the tax treatment of an ambiguous item on the tax return	Percentage of participants who would definitely agree with the advice	Percentage of participants who might agree with the advice	Percentage of participants who might disagree with the advice	Percentage of participants who would definitely disagree with the advice
Include an ambiguous income	58%	18%	14%	10%
Exclude an ambiguous income	24%	24%	16%	36%
Do not deduct an ambiguous expense	34%	20%	22%	24%
Deduct an ambiguous expense	40%	26%	8%	26%

The results show that when a tax practitioner provided conservative advice on an ambiguous income item, 76% of the participants preferred conservative advice. The 76% was comprised of participants who would either definitely agree (58%) or who might agree (18%) with the conservative advice. It appears that when the advice was asked in the negative form, in other words, excluding the ambiguous income item, the participants’ preference for conservative advice was not as strongly supported. Only 52% would disagree, either definitely (36%) or maybe (16%), with the aggressive advice. Similarly, when an ambiguous expense was in question, the participants did not indicate a significant preference for conservative advice when the tax practitioner advised against deducting the expense. Only 54% would agree with the advice, either definitely (34%) or maybe (20%). However, when the tax practitioner provided aggressive advice on an ambiguous expense, the majority – 66% of the respondents – preferred aggressive advice, either definitely (40%) or maybe (26%). This is in line with findings by Hite and Hasseldine (2003, p. 7) and Christensen and Hite (1997, p. 14). Overall, it appears that the participants preferred conservative advice, although not to a significant level. However, the participants tended to be more aggressive when the deduction of an ambiguous expense was in issue.

The next scenario aimed to address the second research objective: “Will you continue to make use of his services as a result of the abovementioned advice?” Each of the scenarios in which tax advice was provided, together with the responses of the participants as to whether they would continue to make use of the tax practitioner’s services, is presented in Table 2.

Table 2: Responses regarding the retention of the tax practitioner based on the type of tax advice received

Tax advice on the tax treatment of an ambiguous item on the tax return	Percentage of participants who would definitely continue to engage with the practitioner	Percentage of participants who might continue to engage with the practitioner	Percentage of participants who might disengage from the practitioner	Percentage of participants who would definitely disengage from the practitioner
Include an ambiguous income	86%	8%	2%	4%
Exclude an ambiguous income	54%	14%	10%	22%
Do not deduct an ambiguous expense	70%	8%	14%	8%
Deduct an ambiguous expense	70%	18%	0%	12%

The results indicate that, irrespective of the type of advice provided, the majority of the taxpayers would still continue to use the services of the tax practitioner. This was evident in all four scenarios. When the tax practitioner advised including or excluding the said income, 94% in the case of the advice to include the income and 68% in the case of the advice to exclude the income would either definitely continue to use the practitioner’s services, or would maybe do so. When the tax practitioner in the scenario advised not to deduct the expense, 78% indicated that they would either definitely or maybe continue to use the services and if the tax practitioner advised deducting the expense, 88% would either definitely or maybe continue to use the services. This finding is similar to that by Tan (1999, p. 443), who reported that there was no sizeable correlation between the type of tax advice received and whether or not the services of a tax practitioner would be retained.

However, it was evident that, when conservative advice was given on an income item, there was a greater willingness (94%) to continue engaging with the tax practitioner than when aggressive tax advice was provided. Where the tax practitioner advised excluding the income item, 68% would continue to engage with him or her. However, when aggressive tax advice on an expense was given, there was a greater willingness (88%) to retain the practitioner’s services than when conservative advice was given, in which case 78% indicated they would continue to engage with him or her. This is different in some ways from the finding by Tan (1999, p. 441), who reported a greater willingness to continue using the services of a tax practitioner when conservative advice was provided, particularly with reference to the deduction of an expense. This finding, however, correlates with the findings on the participants’ preference for the type of advice given on income and expense.

Table 3 below contains a summary of the participants’ responses regarding their preferences for the type of tax advice given in each scenario and whether they would continue to make use of the tax practitioner’s services in each case. Significant relationships existed – these are considered in the discussion after Table 3. Participants’ responses indicating that they definitely or maybe agreed are grouped together, and those stating that they definitely or maybe disagreed are also grouped together for the purposes of this table.

Fisher’s exact test was done to test for significant relationships between the types of tax advice and whether taxpayers would retain a tax practitioner’s services.

Table 3: Summary of responses (frequency and row percentage) regarding taxpayers' agreement with the tax advice relating to the different scenarios and retention of the tax practitioner

	Scenario 1		Scenario 2		Scenario 3		Scenario 4	
	Agree to include the said income	Disagree on including the said income	Agree to exclude the said income	Disagree on excluding the said income	Agree not to deduct the said expense	Disagree on deducting the said expense	Agree to deduct the said expense	Disagree on deducting the said expense
Continue to engage	38 (100%)	9 (75%)	24 (100%)	10 (38.46%)	26 (96.30%)	13 (56.52%)	32 (96.97%)	12 (70.59%)
Discontinue engaging	0 (0%)	3 (25%)	0 (0%)	16 (61.54%)	1 (3.70%)	10 (43.48%)	1 (3.03%)	5 (29.41%)
TOTAL	38 (100%)	12 (100%)	24 (100%)	26 (100%)	27 (100%)	23 (100%)	33 (100%)	17 (100%)
Fischer's p-values	0.0112	0.0112	0.0001	0.0001	0.0012	0.0012	0.0136	0.0136

Instances at a 5% level are statistically significant. All the instances show that there is a significant relationship between taxpayers' engagement with their tax practitioner and their agreement with the advice offered.

In the first scenario, all the participants who agreed with the advice indicated that they would continue to engage with the tax practitioner, while some of the participants (25%) would disengage from the tax practitioner if they disagreed with his or her advice. From a qualitative viewpoint, there is a connection between a taxpayer's continuing to engage with a tax practitioner when conservative tax advice was provided, and the fact that they would do so even if they disagreed with the advice. As already indicated, all the participants who would mainly agree to include the ambiguous income item would mainly continue to do so. Of the participants who indicated that they would mainly disagree with this advice, 75% would still mainly continue to use the practitioner.

In the second scenario, all the participants who agreed with the advice would continue to engage with the tax practitioner, but the majority of the participants (61.54%) indicated that they would disengage from the tax practitioner if they disagreed. Based on a qualitative review, there is some relationship between the fact that taxpayers would continue to engage with a tax practitioner when aggressive tax advice was given, even if they disagreed with that advice. As stated, all of the participants would continue to engage with the tax practitioner when they agreed with the advice to exclude the ambiguous income item. An aggregate of only 38% of the participants who indicated that they would disagree would still continue to engage with the practitioner, while the majority (62%) would disengage from the tax practitioner if they disagreed.

In the third scenario, an aggregate of 96% of the participants who agreed with the advice would continue to engage with the tax practitioner, whereas an aggregate of 43% of the participants indicated that they would disengage if they disagreed with the advice. From a qualitative perspective, it should be noted that taxpayers would continue to engage with a tax practitioner when conservative tax advice was given, even if they disagreed with that advice. As already shown, an aggregate of 96% of those who said they would agree not to deduct the ambiguous expense would continue to engage with the practitioner. An aggregate of 57% who said they would disagree with the advice would continue to engage with the practitioner.

In the last scenario, an aggregate of 97% of the participants who agreed with the advice given by the practitioner would continue to engage with the tax practitioner, whereas an aggregate of 29% indicated that they would disengage from their tax practitioner if they disagreed with the advice. However, from a qualitative perspective, there is a link between taxpayers' continuing to engage with a tax practitioner when aggressive tax advice was provided and their disagreeing with the advice. Of the participants who indicated that they would agree with the advice to deduct the ambiguous expense, 97% would continue to engage with the practitioner. Of the participants who indicated that they would disagree, 71% would continue to engage with the practitioner.

Despite the statistical evidence, and based on a interpretive review, in all the abovementioned instances except when the participants disagreed with the advice to exclude the income item, participants would continue to engage with their tax practitioners, even when they disagreed with their advice. These findings, therefore, did not support the findings by Tan (1999, p. 441) and Hite and McGill (1992, p. 396).

Based on a qualitative review, the outcome of the second research objective is, therefore, that taxpayers would generally continue to engage with a tax practitioner if they disagreed with the advice given, as there was no relation between agreement with advice and termination of services. The difference in findings could be ascribed to the fact that Tan (1999, p. 437) conducted his study on businesses in general and not specifically on small businesses, and the geographic region was also different. (Tan's study was done in the Manawatu region of New Zealand.)

The final section of the article summarises the findings and draws conclusions from the research objectives. A summary of contributions, limitations and suggestions for future research are also offered.

5 CONCLUSION

The main purpose of this exploratory research was to examine the preferences of taxpayers in the small business sector relating to the type of advice offered by their tax practitioners. This was done by means of addressing the following research objectives: firstly to determine whether small business taxpayers prefer to be given conservative or aggressive advice by their tax practitioners; and secondly to determine whether small business taxpayers would continue to use the services of their tax practitioners if these taxpayers disagreed with the proposed tax approach.

Three main findings on the preferences of small business taxpayers regarding the types of tax advice offered by practitioners emerged from this study: Firstly, when asked directly which type of advice they preferred, the majority of participants indicated that they preferred receiving conservative tax advice from their tax practitioners, as they wanted to do what was right and not take chances. This was corroborated by the fact that they were concerned mainly with filing an accurate tax return and avoiding investigation by SARS.

Secondly, when ambiguous scenarios were presented to the participants, it appeared that they preferred aggressive advice when an ambiguous expense was in question.

Finally, the results also showed that participants tended to agree with the tax practitioner, irrespective of the type of tax advice. This may particularly have been the case if they were not knowledgeable about a tax issue and relied on their tax practitioners for guidance.

In support of their reliance on and trust in their tax practitioners, the participants indicated that they would, in most cases, retain the services of their tax practitioner, irrespective of the type of advice given, even if they disagreed with the advice, as long as the advice did not involve tax evasion. It follows logically that tax practitioners can play a vital role in the compliance behaviour of taxpayers.

The findings of this study showed that participants would prefer conservative tax advice from their tax practitioners. The validity of this conclusion is, however, questionable, given the tendency to favour more aggressive advice when the deduction of an expense was in question, or when the significance of a tax issue was not understood. In such a case, they would merely follow the advice given to them by their tax practitioner. Moreover, it was clear that taxpayers in the small business sector would, for the most part, continue to engage with their tax practitioner even if they disagreed with the tax approach proposed to them. These findings, therefore, do not support the findings by Tan (1999, p. 441) and by Hite and McGill (1992, p. 396). There is also a indication that the participants in the current study rely heavily on their tax practitioners. Together with the conclusions on the research objectives and the problem statement, these findings have practical implications.

The findings of this study, which indicate to some extent that small business taxpayers would prefer conservative tax advice, are in line with Tan's conclusions (1999, p. 445) and with those of Hite and McGill (1992,

p. 398). The findings by Sakurai and Braithwaite (2001, p. 20), Tan (1999, p. 439), Hite and McGill (1992, p. 21) and Collins *et al.* (1990, p. 15) are corroborated, in that the most important reason for taxpayers to engage with tax practitioners is to file an accurate tax return. However, the taxpayers did indicate that, when an ambiguous expense was in question, they would prefer aggressive advice. This concurs with the findings by Hite and Hasseldine (2003, p. 7) and Christensen and Hite (1997, p. 14).

With regard to the retention of a tax practitioner's services, it is evident that small business taxpayers tend to remain loyal to their tax practitioners irrespective of the type of advice they are given or even if they disagree with it, except in the case of tax evasion. However, this finding contradicts the findings of previous research by Tan (1999, p. 441) and by Hite and McGill (1992, p. 96). In these earlier studies, taxpayers indicated that they would disengage from their tax practitioner if they disagreed with the advice they were given. However, Tan (1999, p. 443) showed that there was no significant connection between the type of tax advice received and the retention of a tax practitioner, which was also evident in this study. The fact that small business taxpayers in this study are very clear about the fact that they do not want to be associated with tax evasion corroborates the findings by Ahmed and Braithwaite (2005, p. 554).

As indicated above, taxpayers rely on their tax practitioners for guidance and trust them with their tax affairs. This finding corroborates conclusions in studies such as those by Sakurai and Braithwaite (2001, p. 19) and Tan (1999, p. 445), who stressed the importance of tax practitioners' roles in taxpayers' compliance behaviour. It follows that it is necessary for South African tax practitioners to be strictly regulated. This supports the rationale for the Regulation of Tax Practitioners Act, which will become effective in South Africa in the very near future. It is crucial that the relevant statutory body carrying out the regulation of tax practitioners is both efficient and stringent in enforcing the relevant code of conduct. In order for this to be possible, the necessary disciplinary procedures need to be put in place and adequate knowledge and expertise on the part of all South African tax practitioners must be monitored. This will not only benefit the taxpayer by reducing penalties and audit exposure, but will also aid the government in improving its revenue income.

This study can be extended to include other geographical areas and types of taxpayers (i.e. individuals and medium to large businesses). Additional variables, such as the likelihood of penalties or audit exposure, which were used in Tan's study (1999, p. 437), could also be introduced into the questionnaire to test how these variables would influence taxpayers' decisions relating to their preference for the type of advice offered.

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