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Responsive Regulation and the Uncertainty of Tax Law – Time to Reconsider the Commissioner’s Model of Cooperative Compliance?

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Abstract

Over the last decade the Australian Taxation Office has adapted the model of ‘responsive regulation’ in developing its cooperative compliance model. This model seeks to promote voluntary compliance with Australia’s taxation laws by tailoring the administrative treatment of taxpayers in accordance with the individual taxpayer’s tax compliance posture. The fulcrum of this model of tax administration is the proposition that taxation law is determinate, such that ‘complying’ and ‘non-complying’ taxpayers may be segregated and treated accordingly. This paper argues that this dichotomous model is problematic in at least some tax contexts, and considers the implications of legal indeterminacy for the cooperative compliance model.

1. INTRODUCTION

At the time of its emergence in the 1990s, ‘responsive regulation’ promised a neat resolution of several challenges confronting regulators. In the taxation domain, these challenges included:

- the dramatic expansion of the reach of government regulation - extending across the wider community and into hitherto unregulated domains. This expansion had been prompted by the growth in the taxpayer base during and after the second world war, and also by the expansion of the substantive tax base during the 1980’s and 1990’s. In this context, the command and control concept of ‘chasing down every last cent’, although mythical,¹ was openly acknowledged to be an impossibility given the numbers of taxpayers under a mass taxation system;²

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¹ For discussion of the revenue maximizing culture of the Australian Taxation Office of the 1980’s, which saw ‘small’ taxpayers with relatively simple taxation breaches prosecuted in preference to ‘big’ taxpayers with complicated tax arrangements, see Peter Grabosky and John Braithwaite, *Of Manners Gentle*, Oxford University Press, Melbourne, 1986, 161ff. Grabosky and Braithwaite cite R Redlich, *Annual Report of the Special Prosecutor 1983-4*, AGPS, Canberra, 1984: ‘The Taxation Office too often elected not to unravel the corporate structure which a criminal employed to hide his assets because Tax officers could spend that time dealing with straightforward returns of other taxpayers and thereby recover the same or greater revenue.’ (at 131).

² Trevor Boucher, ‘Risk Management on a Market Segmented Basis’ in Peter Grabosky and John Braithwaite (eds), *Business Regulation and Australia’s Future*, Australian Institute of Criminology, Canberra, 1993, 231 at 232. For academic discussion of this point see: Peter Grabosky and John Braithwaite, *Of Manners Gentle*, Oxford University Press, Melbourne, 1986.

- the expansion of the public scrutiny of government, arising from the open government reforms of the 1980s, including freedom of information laws and the creation of additional avenues for public sector review;³
- the impact of neoliberal ideology, which brought to the fore the ‘business’ of government – the public were now ‘clients’;⁴ performance appraisals of objectively defined outcomes became routine⁵ and public servants were incentivised with remuneration ‘at risk’. The discipline of defining performance outcomes meant that the doctrine of strict enforcement of the law was expressly rather than implicitly overlooked in favour of a managerial discretion as to the best deployment of limited resources;⁶ and
- the neoliberal wave of small government thinking⁷ saw governments disguising the amount and nature of ‘public’ intervention in ‘private’ affairs by promoting self-regulation, as with the introduction of a self assessment tax system. Such self-regulation saw state power diffused throughout the community as taxpayers assumed greater responsibility for tax compliance. A command and control conception of state power was inapt in describing this new era of governmentality.⁸

Public sector agencies were therefore squeezed by small government rhetoric at a time when, paradoxically, more was being demanded of them. In this context ‘responsive regulation’ promised a regulator’s nirvana – retention of existing substantive policy, greater accountability, enhanced compliance with the law *and* public sector efficiency dividends. This optimal regulatory outcome could be achieved, it was argued, by creating regulatory partnerships between regulators and regulatees which would leave the community largely to regulate itself,⁹ with the regulatory ‘big sticks’ wielded by the regulator for those few who demonstrated the most egregious of non-compliant behaviour.

There is a wealth of literature regarding the nature, implementation and operation of responsive regulation programs, yet some of the fundamental concepts upon which responsive regulation is constructed remain ill-defined. One critical aspect of the responsive regulation literature is that it assumes that the law is determinate. This assumption is critical to the concept of responsive regulation because responsive regulation is constructed upon a dualistic paradigm of compliance and non-

³ For discussion of which see: J Goldring, ‘The Accountability of Public Administration and the Rule of Law in Australia’ (1981) 1 *Lawasia* (NS) 326; J Goldring, ‘The Foundations of the “New Administrative Law” in Australia’ (1981) 40 *Australian Journal of Public Administration* 79.

⁴ For discussion of this see Mark Redmond, ‘Is the Taxpayer Really Revenue’s Customer?’ *The Sunday Business Post*, 29 May 2005; John Prebble, ‘Customers, branding, mottoes and the New Zealand inland revenue department’ in Michael Walpole and Chris Evans (eds), *Tax Administration in the 21st Century*, Prospect, Sydney, 2001.

⁵ Anuphan Kitnitchiva, ‘Accountability and Fairness in Tax Administrations – A Case Study of the Thailand Revenue Department’ (2006) *Asia Pacific Tax Bulletin* (Mar/Apr) 76.

⁶ Now incorporated in the Financial Management and Accountability Act 1997. For discussion of the approach to risk management adopted by the Australian Taxation Office in the early 1990’s see: Trevor Boucher, ‘Risk Management on a Market Segmented Basis’ in Peter Grabosky and John Braithwaite (eds), *Business Regulation and Australia’s Future*, Australian Institute of Criminology, Canberra, 1993, 231.

⁷ See, for example, Milton Friedman and Rose Friedman, *Free to Choose*, Penguin Books, Harmondsworth, 1980.

⁸ Mitchell Dean, *Governmentality: power and rule in modern society*, Sage, London, 1999.

⁹ T Boucher, above n 2.

compliance. Regulators need to be able to identify non-compliance so that they can adopt an appropriate regulatory response. However, even when proponents of responsive regulation acknowledge that the law is indeterminate, they do not consider the implications of legal indeterminacy for the responsive regulation paradigm. If the law is indeterminate, and in section 3 I argue that there are good reasons for accepting that at least some tax law is of indeterminate meaning, then the operation of the responsive regulation model in the domain of taxation law is open to question. If a significant challenge confronting tax administrators is the ‘management’ of taxpayer behaviour under indeterminate law, as at least one former Commissioner candidly acknowledged,¹⁰ the dualistic compliance paradigm of responsive regulation must be reconsidered. Framing the relationship between regulator and regulatee in terms of a partnership in an indeterminate legal domain is problematic for a number of reasons. The identity of the partners, the relative bargaining power of the partners, the capacity of the regulator to resist regulatory capture or enrapture, and the preservation/enhancement of the legitimacy of the taxation system in the secretive and hence opaque domain of taxation law are all issues which, it will be argued below, have not been adequately addressed in the cooperative compliance literature.

It is possible that failure to address such issues means that the cooperative compliance model has not generated the desired regulatory nirvana that was promised and the failure to address these issues may be counterproductive. For example, the public may perceive ‘partnerships’ with demographic taxpaying groups such as large corporate taxpayers as yet another example of ‘the rich not paying their fair share’.¹¹ If so, Australia might yet again revisit the dark days of the 1970’s in which the legitimacy of the taxation system was threatened.¹² Further, even if the cooperative compliance paradigm does engender a stronger awareness of an obligation to pay a ‘fair share’ of the nation’s tax, it is not clear whether this attitudinal shift translates into the behaviour of taxpayers who adopt ‘less aggressive’ tax compliance postures when they encounter indeterminate law. This is because there is not necessarily any consistency between general attitudes towards the tax system or the tax administration and specific behaviours in particular contexts.¹³ If Braithwaite is right in suggesting that context-specific attitudes must be linked to context specific-behaviours,¹⁴ there is clearly a need to consider the effectiveness of the cooperative compliance model in altering taxpayer behaviour in specific contexts. Without such analysis, it is possible that taxpayers will cherry-pick tax administration advantages proffered by the ATO in its efforts to build community partnerships, while ‘playing for the grey’ in other contexts. After all, the existence of any positive effect of the cooperative compliance

¹⁰ Id.

¹¹ Valerie Braithwaite, *Perceptions of Who's Not Paying Their Fair Share*, Working Paper No 54, Centre for Tax System Integrity, Canberra, 2004.

¹² Margaret Levi, *Of Rule and Revenue*, Uni of California Press, Berkeley, 1988.

¹³ DS Massey, ‘A Brief History of Human Society: The Origin and Role of Emotion in Social Life’ (2002) 67 *American Sociological Review* 1; cited in Valerie Braithwaite, ‘Dancing with Tax Authorities’, in Valerie Braithwaite (ed), *Taxing Democracy*, Ashgate Publishing, Ashenden, 2003, 17.

¹⁴ Valerie Braithwaite (ed), above n 13, 17; citing M Fishbein and I Ajzen, ‘Attitudes Toward Objects as Predictors of Single and Multiple Behavioural Criteria’ (1974) 81 *Psychological Review* 59; S Epstein, ‘Aggregation and Beyond: Some Basic Issues on the Prediction of Behavior’ (1983) 51 *Journal of Personality* 360.

model, in terms of tax administration efficiency, is open to question given that the cost of raising each \$100 of tax revenue has increased over the past decade.¹⁵

One purpose of this paper is to explore the implications for the responsive regulation paradigm if one accepts, as I argue we must, that at least some tax law is of indeterminate meaning. The second purpose of this paper is to suggest future directions for quantitative and qualitative research with a view to quantifying the significance of these implications for the cooperative compliance model in its day to day operation.

2. WHAT IS RESPONSIVE REGULATION?

2.1 A definition

The concept of ‘responsive regulation’ entails administration of determinate law by officials who tailor their regulatory behaviour according to the compliance posture adopted by individuals subjected to the relevant law.¹⁶ The hallmark of responsive regulation is the pursuit of cooperation by the regulatee with the regulator:

Regulatory pyramids offer the advantage of handing tax officers a set of tools that can be applied without having to have a detailed understanding of why non-compliance has occurred. One starts with the expectation of co-operation; escalation on the pyramid occurs only when one sees the other defaulting and becoming non-co-operative.¹⁷

The compliance pyramid depicted by the Commissioner in his *Compliance Strategy*¹⁸ reflects his interpretation of responsive regulation in the taxation domain.¹⁹ For taxpayers who adopt a posture of ‘voluntary compliance’,²⁰ responsive regulation entails the provision of assistance in enabling taxpayers to understand and comply with the law. However, for taxpayers who adopt a posture of ‘resistance’, the tax administrator will consider deploying an escalating range of enforcement measures in achieving compliance. As taxpayers exhibit increasing resistance to ‘cooperation’, under the ‘tit for tat’ principle²¹ the Commissioner responds with escalating enforcement powers.

2.2 Voluntary Compliance and Legitimacy

Promoting voluntary compliance generates public sector efficiency gains because the governed become voluntarily complying self-governors, thereby enabling the

¹⁵ Commonwealth of Australia, *The Commissioner of Taxation Annual Report 2004-05*, Australian Taxation Office, Canberra, 2006, 11 (Fig 1.9). Of course, there is an infinite array of variables which might produce this outcome and mask the fact that the cooperative compliance model is reaping efficiency dividends.

¹⁶ N Gunningham and P Grabosky, *Smart Regulation: Designing Environmental Policy*, Clarendon, Oxford, 1998; J Braithwaite, *Restorative Justice and Responsive Regulation*, Oxford University Press, New York, 2002.

¹⁷ V Braithwaite and J Braithwaite, ‘Managing taxation compliance: the evolution of the Australian Taxation Office compliance model’ in M Walpole and C Evans (eds), *Tax Administration in the 21st Century*, Prospect, Sydney, 2001 at 218.

¹⁸ Commonwealth of Australia, *2006-07 Compliance Program*, Australian Taxation Office, Canberra, 2006, 3.

¹⁹ For discussion of the history of the adoption of the concept of responsive regulation in the taxation domain, see: V Braithwaite and J Braithwaite, above n 17.

²⁰ For consideration of the nature of ‘voluntary compliance’ see section 3.2 below.

²¹ Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate*, Oxford University Press, New York, 1992, 26-7.

regulatory agency to devote its limited enforcement resources to those exhibiting resistant postures. Tyler’s work suggests that voluntary compliance is enhanced by legitimacy, and in turn that legitimacy is enhanced if procedural fairness is adopted by regulatory agencies.²²

There are various factors which might induce compliance with the law: the perceived risk of sanctions, peer/social pressure to comply, normative motivation founded upon a sense of obligation to comply with laws which accord with a person’s sense of morality and/or a belief that the law/government is legitimate such that the law must be obeyed.²³ Tyler notes that reliance upon sanctions alone will be ineffective in achieving effective and efficient regulation of compliance. Further, Tyler notes that moral norms offer an unreliable basis for governments seeking to achieve compliance with the law – moral heterogeneity within any community makes it virtually impossible that most will agree with the morality of all law. Similarly, peer/social pressure are unreliable. By contrast, Tyler argues that legitimacy offers governments the promise of discretionary authority – people will obey the law, even if they disagree with the law, simply because they believe that the law must be obeyed.²⁴

Accepting that individuals continue their membership of social groups for self-interested reasons, Tyler observes that individuals use their perceptions of procedural fairness as a proxy for substantive fairness:

The model that has been developed rests on an assumption that people ultimately care about issues of self-interest. In the context of organizational membership, simple short-term self-interest extends across a number of issues and over time. People want to feel that they will generally benefit from membership in the group. They judge whether they will by examining the procedures according to which allocations are made and disputes resolved. If the procedures are fair, people think they will receive positive outcomes.²⁵

Tyler speculates that legitimation of government is socialized from an early age,²⁶ and argues that regulators should perceive their interactions with the public as opportunities to nurture that sense of legal obligation, legitimacy, amongst adults.

In the context of taxation law there is discretionary power on both ‘sides’ – taxpayers may choose their compliance posture while the Commissioner may choose his regulatory response from a suite of administrative powers. According to the responsive regulation literature, building cooperative compliance within this domain of discretion entails creating a regulatory relationship based upon trust.²⁷ Trust is defined as ‘a relationship where the other player can be taken at his or her word, where there is a commitment to honest communication, to understand the needs of the other, to agreed rules of fair play and a preference for cooperation.’²⁸ By exhibiting trust, for example, the tax administration would encourage taxpayers to self-identify

²² Tom Tyler, *Why People Obey Law*, Yale University Press, New Haven, 1990.

²³ For discussion of these motivators for compliance see Tyler, above n 22, 22ff.

²⁴ Id, 25-6.

²⁵ Id, 172-3.

²⁶ Id, ch 12, 176ff.

²⁷ T Makkai and J Braithwaite, ‘Procedural justice and regulatory compliance’ (1996) 20 *Law and Human Behaviour* 83.

²⁸ Ayres and Braithwaite, above n 21, 86.

areas of tax compliance risk. Trusting the tax administration not to impose penalties arbitrarily, such taxpayers would seek the assistance of the administration in resolving these issues. Thus, the Commissioner has a broad discretion to remit administrative penalties²⁹ and has stated that remission of penalties generally is appropriate where the taxpayer has a good compliance record and has made an honest mistake.³⁰

Signalling trust of a particular individual while indicating preparedness to exercise escalating powers of enforcement would seem contradictory, but legitimisation of the tax system is enhanced by indicating to individual taxpayers that the Commissioner’s enforcement powers will ensure that others will be compelled to comply with the law.³¹ Thus, in addition to the definition of trust adopted by Ayres and Braithwaite, it seems that the nature of responsive regulation implies that trust also entails public confidence in the uniform application of the law across all taxpayers.

2.3 Partnership and responsive regulation

This foundation of trust underpins the discourse of deliberative democracy embodied within the responsive regulation paradigm. One of the innovative aspects of responsive regulation was that it purported to bring the discourse of deliberative democracy into the regulatory domain. This discourse holds that individuals with competing interests can be drawn to a consensus if preconditions to engagement in rational discussion are met.³² This discourse of partnership entails tax administrators and taxpayers joining in ‘regulatory conversations’³³ regarding the implementation of ‘the law’.³⁴ Thus the discourse of tax administration incorporates the rhetoric of ‘partnership’ in preference to the discourse of distrust, confrontation and dispute characteristic of command and control regulation:

In short, the philosophy is one of a community based tax system where the ATO works in partnership with the community. It behoves the community to be involved in the tax system’s development, in its compliance and in its administration.³⁵

The Taxpayers’ Charter reflects an attempt to frame the mutual obligations of the partners in this enterprise.

²⁹ *Taxation Administration Act 1953* (Cth) Sch 1 s 298-20.

³⁰ See for example Practice Statement PS LA 2004/5.

³¹ Braithwaite and Braithwaite, above n 17, (2001, in Evans and Walpole), at 218.

³² See, for example: Cass Sunstein, ‘Beyond the Republican Revival’ (1988) 97 *Yale Law Journal* 1713; James Fishkin, *Democracy and Deliberation: new directions for democratic reform*, Yale Uni Press, New Haven, Conn, 1991.

³³ John Braithwaite, ‘Rules and Principles – A Theory of Legal Certainty’ (2002) 27 *Australian Journal of Legal Philosophy* 47 at 71, citing Julia Black, ‘Talking about Regulation’ (1998) *Spring Public Law* 77.

³⁴ John Braithwaite, *Markets in Vice Markets in Virtue*, The Federation Press, Sydney, 2005, 150.

³⁵ Michael D’Ascenzo, ‘Tax Administration into the 21st century’ in Michael Walpole and Chris Evans, *Tax administration in the 21st century*, Prospect, 2001, 1 at 9. Australian Tax Office, *Improving Tax Compliance in the Cash Economy*, Australian Tax Office, Canberra, 1998; Michael Carmody, ‘Revitalising the tax administration system: the Australian experience’, Address delivered at Tax Administration Advisory Board Meeting, 11-12 January 2005, Phoenix, Arizona; Michael D’Ascenzo, ‘A new relationship with the tax profession’, Paper delivered at the 21st National Convention of the Taxation Institute of Australia, 6 April 2006; Michael D’Ascenzo, ‘Living our Values’, Address delivered at 7th International Tax Administration Conference, 20 April, 2006, Sydney; Michael D’Ascenzo, ‘Relationships between tax administrators and tax agents/taxpayers’, Address delivered at the Asia-Oceania Consultants Association general meeting, 11 November 2005, Manila.

2.4 Community oversight of the partnership – passing the regulatory buck to public interest groups?

Recognising that the wider community has an interest in regulatory integrity and the potential for ‘partnership’ to be code for regulatory capture in some contexts, Ayres and Braithwaite proposed the institution of tripartism as the mechanism by which regulatory capture might be averted within a cooperative regulatory framework:

Tripartism is defined as a regulatory policy that fosters the participation of PIGs [public interest groups] in the regulatory process in three ways. First, it grants the PIG and all its members access to all the information that is available to the regulator. Second, it gives the PIG a seat at the negotiating table with the firm and the agency when deals are done. Third, the policy grants the PIG the same standing to sue or prosecute under the regulatory [58] statute as the regulator. Tripartism means both unlocking to PIGs the smoke-filled rooms where the real business of regulation is transacted and allowing the PIG to operate as a private attorney general.³⁶

According to this model, one public interest group³⁷ would be appointed by the state or by a peak council of ‘public interest groups’ to sit at the regulatory table during negotiations between regulator and regulatee.³⁸ The appointment of just one public interest group representative is apparently justified upon the assumption that regulatory decision making is apolitical.³⁹ The extent of the resources required for adequate prosecution of this task is barely mentioned.⁴⁰ However, if considered a ‘weaker party’, the public interest group would be provided with resources ‘so that they can hire technically competent consultants to help them use that power effectively.’⁴¹

Under this tripartite model, Ayres and Braithwaite suggest, the regulatee could be expected to propose a low ball regulatory outcome while the public interest advocate would be expected (for reasons which are not apparent) to propose a high ball regulatory outcome which exceeded the will of the legislature expressed in the legislation. In such circumstances, the regulator would perform the ‘good cop/bad cop’ routine and oversee resolution of this dispute by brokering an agreement with the regulatee at the mid-point ‘closer to the democratic will embodied in the law.’⁴² Cooperation between the regulator and the regulatee could therefore flourish, because the nasty confrontational work was being performed by a public interest representative

³⁶ Ayres and Braithwaite, above n 21, 57-8.

³⁷ It is not clear what definition of ‘public interest group’ would be adopted. It is clear that a public interest group is one which represents ‘the community interest’, but it is not clear whether this would exclude business lobby groups, for example.

³⁸ Ayres and Braithwaite, above n 21, 58.

³⁹ Ayres and Braithwaite note that tripartism could be adopted in the legislative branch of government, but accept that ‘simple tripartism’ would ‘provide too narrow a basis for PIG participation’: Ayres and Braithwaite, above n 21, 58.

⁴⁰ ‘Activism by salaried PIG [public interest group] lawyers is probably needed.’: Ayres and Braithwaite, id, 84.

⁴¹ Id, 59.

⁴² Id, 82.

who, apparently routinely, would argue for an untenable interpretation of the relevant law.⁴³

3. WHAT IS COMPLIANCE? LIBERAL LEGALISM, INDETERMINATE LAW AND THE CONCEPT OF COOPERATE COMPLIANCE

3.1 What is “compliance” for the purpose of the cooperative compliance model?

In section 2.1 above it was noted that responsive regulation is depicted as a pyramid of increasingly uncooperative taxpayer postures and corresponding regulatory responses. The object of responsive regulation is to induce regulatees to gravitate to the base of the regulatory pyramid, where there is a cooperative, trusting partnership of regulatees and regulator. Although there is occasional and fleeting reference to legal ambiguity,⁴⁴ underpinning this model is the assumption that law is determinate.⁴⁵ Thus, government makes what Valerie Braithwaite describes as ‘direct requests’, and the regulatee can be said to have ‘complied’ if they act in accordance with that request.⁴⁶ Escalation up the compliance pyramid will be considered when a taxpayer exhibits ‘uncooperative behaviour’ - action not in accordance with the direct request - irrespective of the motivation of that behaviour.⁴⁷ The determinacy of the law means that escalation up the enforcement pyramid for ‘uncooperative’ taxpayers is legitimated by the mutual recognition of what the law requires.

There are different forms of compliance. Taxpayers at the base of the compliance pyramid are said to ‘voluntarily’ comply because they submit to or even adopt the compliance culture of the tax administration,⁴⁸ while those at the pinnacle of the pyramid are subject to enforced compliance.

3.2 Cooperative compliance and liberal political theory – the keystone of determinate law

Emphasising cooperation in defining compliance raises the possibility that ‘compliance’ will be confused with submission to a dominant will.⁴⁹ From the perspective of liberal political theory, which is ever alert to the possibility of illegitimate state intervention in the private domain, the concept of ‘cooperative compliance’ is fraught with risk.⁵⁰ Liberals believe that, as much as possible, individuals should be allowed to pursue their respective concepts of the good life with minimal interference from others, including the state.⁵¹ Thus, liberal political theory

⁴³ At this point it is worth observing that Ayres and Braithwaite have duplicated the existing system of dispute resolution in which the regulator is conceived of as an impartial umpire – much the same as a judge who ‘finds’ the right meaning of the law under the ‘fairytale’ view of liberal legalism.

⁴⁴ Valerie Braithwaite, ‘Dancing with Tax Authorities: Motivational Postures and Non-compliant Actions’ in Valerie Braithwaite (ed), above n 13, 15 at 17.

⁴⁵ For discussion of this see section 3.2 below.

⁴⁶ Valerie Braithwaite, ‘Tax System Integrity and Compliance’ in Valerie Braithwaite (ed), above n 13.

⁴⁷ Braithwaite and Braithwaite, above n 17, 218.

⁴⁸ See the extract accompanying n 96 below.

⁴⁹ For early discussion of the concept of regulatory capture see: George Stigler, ‘The theory of economic regulation’ (1971) 2 *Bell Journal of Economics and Management Science* 3; Sam Peltzman, ‘The growth of government’ (1980) 23 *Journal of Law and Economics* 209. For further discussion of regulatory capture see section 4.4 below.

⁵⁰ G de Q Walker, *The Tax Wilderness: How to restore the rule of law*, Centre for Independent Studies, Melbourne, 2004; see also Geoffrey de Q Walker, *The Rule of Law: Foundation of Constitutional Democracy*, Melbourne University Press, Melbourne, 1988.

⁵¹ Isaiah Berlin, ‘Two Concepts of Liberty’ in Isaiah Berlin, *Four Essays on Liberty*, Oxford University Press, Oxford, 1969; Ronald Dworkin, ‘Liberalism’ in Stuart Hampshire (ed), *Public and Private*

holds that the state must be neutral as to competing conceptions of the good life, because favouring one conception over another would be oppressive and hence be an illegitimate exercise of state power.⁵² There are competing understandings of how this principle of state neutrality should be adopted in practice, with some accepting it entails state compliance with formal procedures laid down in a ‘rule of recognition’,⁵³ while others hold that state legitimacy hinges upon compliance with some substantive principle of neutrality (ie promoting efficient private markets). Nevertheless, it is clear that the norm of state neutrality dictates that ‘the law’ is applied uniformly across all legal subjects because the imperfect administration of a ‘neutral’ law is as evil as a non-neutral law.

This requirement that the law be administered neutrally means that a community must be able to define compliance by reference to an objective standard which is independent of the behaviour of the participants in the process. That is, the meaning of the law must be clear such that state oppression through wrongful exercise of state power is as readily ascertainable as a state’s failure to impose the law upon all subjects (as arises in the case of regulatory capture). Mindful that ‘responsive regulation’ might be interpreted as code for arbitrary regulation, Ayres and Braithwaite accept that the thesis of determinate law, which underpins the rule of law, is an integral feature of responsive regulation:

Although we have seen the virtues of giving regulatory agencies big guns, it is crucial that the state set limits on the maximum sanctions that can be imposed and on the offenses for which they can be applied. Obviously, the rule of law is needed as protection against the excesses that we have seen from regulators with the backing of the ruling party in countries such as China, excesses that have included execution and arrest without trial. The rule of law is not only essential to a republican regulatory order, it is definitional of it (Braithwaite and Pettit, 1990: 54-136).⁵⁴

However, it is clear that there is no consensus within the responsive regulation literature upon how the one determinate legal meaning is to be ascertained, and nor is there universal acceptance of the fact that the determinate, objective legal meaning need be exogenous of the regulatory agency. Nevertheless, there is a consensus upon the proposition that ‘there is one legal meaning’ such that regulatees know whether they are complying or not. Thus, at different points in the literature associated with cooperative compliance:

- it is said that non compliance occurs where there is a departure from ‘what the ATO regards as the policy purposes of the parliament’s tax laws’;⁵⁵

Morality, Cambridge Uni Press, Cambridge, 1978; Robert Nozick, *Anarchy, State and Utopia*, Basic Books, 1974.

⁵² For discussion of this aspect of liberalism see: R Bruce Douglas, Gerald M Mara and Henry S. Richardson, *Liberalism and the Good*, Routledge, New York, 1990; Bobby Jindal, ‘Relativism, Neutrality and Transcendentalism: Beyond Autonomy’ (1997) 57 *Louisiana Law Review* 1253.

⁵³ See, for example, discussion of this in HLA Hart, *The Concept of Law*, Clarendon, Oxford, 1961, ch vi.

⁵⁴ Ayres and Braithwaite, above n 21, 53.

⁵⁵ John Braithwaite, op cit n 56, 179; see also Valerie Braithwaite, ‘Tax System Integrity and Compliance: The Democratic Management of the Tax System’ in Valerie Braithwaite, above n 13, ch 13 at 276ff, esp 278 (‘or if the regulatee gives the request meaning that undermines the intent of the regulator (e.g., playing for the grey in tax law)’); Doreen McBarnet, ‘When Compliance is not the Solution but the Problem’, in Valerie Braithwaite (ed), above n 13, 229 at 234 ‘...override claims to

- the definition of compliance suggested by James and Alley is adopted. This definition holds that compliance entails ‘the willingness of individuals and other taxable entities to act ... within the spirit as well as the letter of tax law and administration, without the application of enforcement activity’;⁵⁶
- the Australian Taxation Office adopted what John Braithwaite labeled a literalist approach⁵⁷ to defining compliance, quite possibly drawing upon the definition adopted by Roth, Scholz and Witte;⁵⁸
- on occasion the Australian Taxation Office adopts a ‘purposive’ approach to the interpretation of taxation law;⁵⁹
- the Australian Taxation Office appears to adopt a theory of legislative meaning which incorporates both pragmatic and purposive elements;⁶⁰ and
- the Commissioner of Taxation appears to acknowledge multiple paths to identifying statutory meaning and suggests that the ‘purpose’ of the legislation should prevail without acknowledging that the legislative purpose may be indistinct.⁶¹

Clearly the concept of the rule of law, and in particular the determinacy of law, is definitional of responsive regulation because responsive regulation depends upon everyone knowing who the ‘cheats’⁶² are, who the ‘socially responsible’⁶³ regulatees are and how ‘gaps’ in the letter of the law ought be resolved,⁶⁴ such that escalation up the compliance pyramid for recalcitrants will be legitimate.⁶⁵

Within this literature the possibility of different interpretations of the law is acknowledged occasionally. However, it seems to be accepted that in such cases the regulatee’s interpretation generally will be acknowledged to be wrong because it is inconsistent with the regulator’s ‘right’ interpretation.⁶⁶ At this point it should be

compliance based on the letter of the law, rather than on what those producing or enforcing the law see as its spirit’.

⁵⁶ Ayres and Braithwaite, above n 21, 26-7, 60; Valerie Braithwaite, above n 13, 24; John Braithwaite, ‘Large Business and the Compliance Model’ in Valerie Braithwaite, above n 13, 177-8; Doreen McBarnet, ‘When Compliance is not the solution but the problem: From Changes in Law to Changes in Attitudes’ in the same volume, 229-30; see also Commonwealth of Australia, *The Australian Taxation Office’s Management of Aggressive Tax Planning*, Australian National Audit Office Report No 23 2003/2004, AGPS, Canberra, 2004, 24. For discussion of the concept of practical compliance see: Michael Carmody, ‘The Art of Tax Administration: Two Years On’ in Rodney Fisher and Michael Walpole, *Global Challenges in Tax Administration*, Fiscal Publications, Bath, 2005, 5 at 7.

⁵⁷ John Braithwaite, ‘Large Business and the Compliance Model’ in Valerie Braithwaite (ed), above n 13, 177 at 177.

⁵⁸ ‘Compliance with reporting requirements means that the taxpayer files all required tax returns at the proper time and that the returns accurately report tax liability in accordance with the Internal Revenue Code, regulations, and court decisions applicable at the time the return is filed.’ J Roth, J Scholz and A Witte, *Taxpayer Compliance*, (vol 1) Uni of Pennsylvania Press, Philadelphia, 1989, 21.

⁵⁹ Commonwealth of Australia, *2006-07 Compliance Program*, Australian Taxation Office, 2006, Foreword (referring to ‘the objectives’ of the taxation system).

⁶⁰ Australian Taxation Office, *Integrity Framework*, Australian Taxation Office, Canberra, 2006, 8

⁶¹ Michael D’Ascenzo, ‘Along the Road to Damascus: A Framework for Interpreting the Tax Law’ (2000) 3 *Journal of Australian Taxation* 384 cf Mark Burton, ‘Democratic Tax Administration’ in Margaret McKerchar and Michael Walpole, *More Global Challenges in Tax Administration*, Fiscal Publications, Bath, 2006 (forthcoming).

⁶² Ayres and Braithwaite, above n 21, 26-7.

⁶³ Id

⁶⁴ Id, 27.

⁶⁵ For a discussion of the concept of legitimacy see: Tyler, above n 22, ch 1.

⁶⁶ As is most clearly seen in the first dot point in the preceding list.

noted that if the ‘right’ interpretation is governed by the regulator’s interpretation of the law, it is difficult to see how the rule of law is definitional of responsive regulation, because this would make regulators judges in their own cause and lay the way for autocratic power, which Ayres and Braithwaite expressly disavow.⁶⁷

However, for present purposes it is clear that determinate meaning of authorized legislative texts, as determined by one means or another, is central to the operation of responsive regulation. There is little point in revisiting the substantial literature regarding the limitations of this liberal legalism.⁶⁸ However there are two salient aspects of liberal legalism which are particularly relevant to the ensuing discussion of responsive regulation:

1. a central aspect of liberal legalism is the proposition that a legislative text, created in accordance with the appropriate ‘rule of recognition’, constitutes law and is the focus of any interpretive inquiry. The interpretation of the text is not an open-ended inquiry into what is ‘right’ – it is the quest for the one ‘right’ legislative meaning. Finding the one right meaning of the text means that the consideration of the moral aspects of competing interpretations is just as irrelevant as perceptions of the various pragmatic consequences of differing interpretations.

Under the paradigm of responsive regulation, then, a person is not a ‘cheat’ if they ‘buy’ a legislated tax favour through ‘lobbying’ and/or clandestine political deals.⁶⁹ From this perspective, such legislated deals are legitimate because they are ‘the law’ and are therefore apparently assumed to express the ‘democratic will’.⁷⁰ The opacity of the legislative process and the myopia of ‘the people’ are ignored.⁷¹ By contrast, a person who does not procure such legislative favours is a ‘cheat’ if they do not ‘cooperate’ with what they perceive to be a defective law which has emerged from a defective process driven by the machinations of powerful interest groups.

Liberal legalism therefore dictates that we ignore the prospect that people might be cynical about the origins of a law and hence be cynical about the justice and fairness of a law. By adopting this legal formalism, Tyler and others within the responsive regulation fold have focused our attention upon the legitimization of the tax administration, rather than upon the legitimacy of the government’s taxation institutions and the substantive law more generally.⁷² However, if the law is indeterminate, it is possible that taxpayers look beyond administrative procedural fairness; and

2. legal formalism lends itself to a top-down, command and control theory of state power. Under this paradigm, state power is concentrated in state institutions

⁶⁷ Ayres and Braithwaite, above n 21, 53.

⁶⁸ For discussion of the concept of legal formalism, and its limitations, see Duncan Kennedy, ‘Legal Formality’ (1976) *Journal of Legal Studies* 351; J. Shklar, *Legalism*, Cambridge Mass 1964.

⁶⁹ Dan Roberts, ‘GE surges as tax breaks cut in’, *The Australian*, 24 January 2005, 28.

⁷⁰ Ayres and Braithwaite, above n 21, 82.

⁷¹ The limitations of the legislative process in Australia were considered, albeit in the limited context of small business tax concessions, in: Mark Burton, ‘The Australian small business tax concessions – public choice, public interest or public folly’ (2006) 21 *Australian Tax Forum* 91. See also Mark Burton, ‘Chaos, Rhetoric and the Legitimation of ‘Democratic’ Government – A Critical Review of the Australian Tax Legislative Process’ (2007) *Sydney Law Review* (forthcoming).

⁷² Tom Tyler, *Why People Obey the Law*, Princeton University Press, Princeton, 2006, 262.

because the source of the power is the clear meaning of the legislative texts and the state determines how that power is exercised. The exercise of power under legislation might be delegated to others who are traditionally considered to fall outside of ‘the state’, as under the concept of meta-risk management,⁷³ but such delegations of power can be revoked. Always, in the background, lies the omnipotent state, overseeing the exercise of ‘its’ power legitimated by the community’s understanding of legislative meaning.

However, if the meaning of legislation is indeterminate and hence contestable (and often contested), the state is engaged in a process by which its power is contingent, in which its power is defined according to the specific context. Thus, in regulating indeterminate taxation law, different taxpayers might exert more or less influence vis a vis the tax administration in interpretive contests.

4. THE INDETERMINACY OF LAW

The concept of responsive regulation therefore hinges upon the existence of determinate legislative meaning. However, there are three reasons to question whether such determinate legal meaning exists.

4.1 Variability of interpretive method

The first is the fact that there are various means of identifying the ‘true meaning’ of a legal text. As Wittgenstein noted,⁷⁴ words do not have a finite meaning independent of their context. Instead, words assume a meaning within a particular context. In light of this insight, different interpretive methods have been developed which define the relevant context differently. There are, for example, multiple definitions of what a ‘literalist’ approach to statutory interpretation entails, each one adopting a different rule as to the nature of the context which should be considered in pursuing a literalist interpretation. Similarly, there are various understandings of what a purposive approach entails.⁷⁵

Recognition of the existence of multiple interpretive paths indicates that compliance cannot be objectively determined in many cases – this is not a case of all interpretive roads leading to Rome. McBarnet’s concept of ‘creative compliance’,⁷⁶ for example, acknowledges that different interpretive paths produce different plausible meanings. Similarly, the vagaries of the compliance concept have been acknowledged by various proponents of cooperative compliance, including the Commissioner of Taxation (albeit rarely),⁷⁷ Valerie Braithwaite⁷⁸ and John Braithwaite.⁷⁹

⁷³ Christine Parker, *The open corporation: effective self-regulation and democracy*, Oxford University Press, Melbourne, 2002; For discussion of the application of Parker’s work in the context of taxation law see: John Braithwaite, ‘Meta Risk Management and Responsive Regulation for Tax System Integrity’ (2003) 25 *Law & Policy* 1.

⁷⁴ Ludwig Wittgenstein, *Philosophical Investigations*, trans G.E.M. Anscombe, Basil Blackwell, Oxford, 1968 (3rd edn).

⁷⁵ Mark Burton, ‘The Rhetoric of tax interpretation – where talking the talk is not walking the walk’ (2005) 3(1) *Journal of the Australasian Tax Teachers Association* 1.

⁷⁶ Doreen McBarnet, ‘When Compliance is not the Solution but the Problem: From Changes in Law to Changes in Attitude’ in Valerie Braithwaite, *Taxing Democracy*, 229 at 230.

⁷⁷ See, for example: Commonwealth of Australia, *Cooperative Compliance: Working with Large Business in the New Tax System*, Australian Taxation Office, Canberra, 2000, 6; Commonwealth of Australia, *Large Business and Tax Compliance*, Australian Taxation Office, Canberra, 2006, 10.

⁷⁸ Braithwaite, above n 13, 4.

⁷⁹ John Braithwaite, above n 34, ch 10 (acknowledgement that tax law needs to be made more certain).

Apparently in recognition of this threat to responsive regulation, John Braithwaite has argued that the tax law can be made ‘more certain’ by adopting a combination of legislative principles and legislative rules. This legislative framework, Braithwaite suggests, would promote a purposive approach to legislation.⁸⁰ Under this approach, legislation would comprise core principles (such as ‘safe driving in light of road conditions’)⁸¹ and specific elaborations of these principles (‘rules’ – such as ‘you cannot exceed 80 kilometres per hour in a speed zone marked as such’). In the event of conflict, principles would trump rules. According to Braithwaite, a driver would know that they would not face regulatory action while driving under the prescribed speed in an 80km/h speed zone ‘in normal circumstances’⁸² or provided that there were no ‘unusually dangerous conditions’.⁸³ However, in ‘abnormal circumstances’ the driver would know that they must comply with the principle.

There are two aspects of this proposal which indicate that it may not provide a smooth road to legislative certainty:

1. Braithwaite appears to assume that a principle has a determinate meaning, when this is not necessarily the case. Whether one talks of ‘principles’ or ‘rules’, both must be expressed in language which is, as I have suggested above, of indeterminate meaning. The meaning of a principle can be just as elusive as the meaning of a rule. Thus, for example, Braithwaite suggests that a general anti-avoidance rule is an example of a ‘principle’ which should be adopted under his model. However, the difficulty of identifying the meaning of this ‘principle’ is illustrated by the case law. For example, the recent High Court decision in *FCT v Hart*⁸⁴ left unresolved the meaning of the definition of ‘scheme’ in ITAA36 s 177A(1).⁸⁵

Taking Braithwaite’s example of traffic regulation, in the absence of an exhaustive definition of what constitutes ‘normal circumstances’ and/or ‘unusually dangerous conditions’, a driver would be well advised to seek compliance with the principle and ignore the rule. But the vagaries of applying such a principle as ‘drive carefully’ in specific contexts mean that reasonable people will reasonably disagree about what the principle means in any one context. After all, there is a very real possibility that different people will adopt different interpretive standpoints when interpreting the principle, a prospect which I address in section 4.2 below; and

2. the interaction of rules and principles under Braithwaite’s model can be expected to create uncertainty, rather than resolve it. Giving principles such as ‘safe driving’ priority over rules (‘drive within the stated speed limit’) leaves the way open for drivers who exceed the speed limit to argue that they were complying with the principle. The driver of a car with high performance brakes, collision detection and evasion technology and so forth might quite reasonably argue that they were driving ‘safely’. They might quite plausibly argue that they were driving more safely than the person in the adjacent lane whose reflexes are slowed because she/he has consumed some alcohol (but is within the legal limit)

⁸⁰ Id.

⁸¹ Id, 144.

⁸² Id, 145.

⁸³ Id, 145.

⁸⁴ *FCT v Hart* (2004) 217 CLR 216.

⁸⁵ Justin Dabner and Mark Burton, ‘Hart – the death of tax planning?’ (2004) *CCH Tax Week* 373.

and who is driving a fully laden old car which has outmoded brakes and suspension. It is possible Braithwaite’s interpretive model means that the law is no more certain than under any of the existing interpretive approaches adopted by the courts.

4.2 No consensus regarding interpretive standpoint

The second source of legal indeterminacy is that there is no consensus regarding the appropriate interpretive standpoint.

In view of the various approaches to defining the context of legislation for the purposes of ascertaining its meaning, it would be possible for a community to (somehow) agree that ambiguity should be resolved by recourse to one interpretive standpoint such as ‘adopt the meaning which is most efficient in an economic sense’. Thus, Ayres and Braithwaite describe their concept of ‘regulatory republicanism’ in which an ‘enlightened’ private sector and an informed public sector engage constructively in deliberative dialogue.⁸⁶ This draws upon the communicative theories of Habermas⁸⁷ and Sunstein⁸⁸ which posit that rational conversations will tend to produce determinate meaning. However, there is good reason to question whether consensus can be reached when the participants in a shared conversation hold incommensurable standpoints.⁸⁹ Ayres and Braithwaite seem to acknowledge this issue, without adequately addressing it, when they express a preference for small group decision making upon the basis that it would ‘maximise the prospects of genuine dialogue around the table leading to a discovery of win-win solutions, instead of a babble of many conflicting voices talking past each other.’⁹⁰

Such standpoint incommensurability may be seen in the literature regarding taxation law. Within this literature there are diametrically opposed standpoints regarding the interaction of the concept of private property with the nature of taxation:

- for those who adopt a communitarian perspective, all property belongs to the state and so ‘tax’ is not an imposition upon individuals but merely the portion of the state’s property which the state does not forego to private ownership.⁹¹ To those who adopt this standpoint, the onus is upon the taxpayer to show why the government should not withhold its property from the taxpayer. Further, under this

⁸⁶ John Braithwaite, above n 34, 150.

⁸⁷ Jurgen Habermas, *Theory of Communicative Action* (vol 1), Thomas McCarthy (trans), Beacon Press, Boston, 1984; Jurgen Habermas, *Between Facts and Norms: Contributions to a Discourse Theory of Law and Democracy*, William Rehg (trans), Polity Press, Cambridge, 1996.

⁸⁸ Cass R Sunstein, ‘The Republican Civic Tradition: Beyond the Republican Revival’ (1988) 97 *Yale LJ* 1539.

⁸⁹ Chantal Mouffe, ‘Democracy and Pluralism: A Critique of the Rationalist Approach’ (1995) 16 *Cardozo Law Review* 1533.

⁹⁰ Ayres and Braithwaite, above n 21, 58. This comment appears to conflict with the earlier endorsement of Sunstein’s four principles of deliberative decision making (at 18), and so may not be intended as a rejection of such principles. However, in discussing the problem of regulatory capture, Braithwaite and Ayres posit the regulator as an umpire sitting between the opposing interests of the regulatee and a public interest group representative: Ayres and Braithwaite above n 21, 81ff, esp 86.

⁹¹ Liam Murphy and Thomas Nagel, *The Myth of Ownership: Taxes and Justice*, Oxford Uni Press, Oxford, 2000.

view, it is appropriate to interpret legislation in favour of the revenue, as the courts have done from time to time;⁹²

- for many liberals, private property preexists any claim of the state and so a tax is an imposition upon individuals. This imposition might be cast in terms of an exchange contract – ‘taxes are what you pay for civilized society.’⁹³ Or it might be conceived in terms of a compulsory exaction which does not necessarily purchase public services – theft.⁹⁴ Under this view, the onus is upon the state to show why it should receive some of the taxpayer’s private property. Thus tax legislation is to be read restrictively because the government is compulsorily acquiring private property and has ample resources to accurately define the extent to which it will exact tax from its subjects.

The significance of these incommensurable standpoints is evident in the discussion of what constitutes ‘voluntary compliance’, a subject candidly considered in an Australian Taxation Office review of its Large Case Audit Program in 1992.⁹⁵ Although the extract below is long, it acknowledges that the concept of ‘voluntary compliance’ is contestable owing to the existence of incommensurable standpoints, and particularly where the law is accepted to be ‘grey’:

Large corporate taxpayers and the ATO define voluntary compliance, and thus tax due, differently. Most corporations desire and make substantial efforts to comply with the taxation law, while at the same time practising varying degrees of active tax planning in their goal to maximise returns to shareholders. The ATO’s view of compliance, on the other hand, is influenced by a conservative view of the law and the need to protect the tax base. With many grey areas of the taxation law, different perceptions of tax due on the part of corporations and the ATO are inevitable. In fact, these grey areas account for more than half of all debits collected by the program, while the remainder is mostly attributable to legitimate disputes of fact or errors where the law is not in question.

Given these different perceptions, the term ‘voluntary compliance’ for this taxpayer group may be somewhat misleading. For other taxpayer segments, ‘voluntary compliance’ describes the readiness of the taxpayers to do the right thing – to accurately report their income and expenses and pay the tax due. On this definition, the largest corporations (the top 100) can be said to be highly compliant, as this taxpayer base, with rare exceptions, is not intending to evade tax. In fact, only one instance of tax evasion has been prosecuted for the LCP. Nonetheless, corporations still have a large motivation to minimize tax, which occurs most fruitfully in areas where the law is unclear. In this taxpayer group, the degree of ‘non-compliance’ is more a function of a lack of clarity in the tax law than inappropriate taxpayer behaviour. The key, therefore, to increased voluntary compliance by the

⁹² See, for example, M Burton, ‘Reconciling the Rhetoric of Rights with the Pro-Revenue Construction of Tax Legislation in Eighteenth Century Britain’ (2003) 7 *Canberra Law Review* 27.

⁹³ *FCT v Spotless Services Ltd* 96 ATC 5201, 5206.

⁹⁴ See, for example, Eric Mack, ‘Self Ownership, Taxation, and Democracy: A Philosophical-Constitutional Perspective’ in Donald P. Racheter and Richard E. Wagner, *Limiting Leviathan*, Edward Elgar, Cheltenham, 1999, ch 2; for discussion of this discourse see: Marc Linder, ‘Eisenhower-Era Marxist Confiscatory Taxation: Requiem for the Rhetoric of Rate Reduction for the Rich’ (1996) 70 *Tulane L Rev* 905.

⁹⁵ Cited in Boucher above n 2, 237.

ATO definition is to narrow the gap between the ATO’s and corporate taxpayers’ interpretations of the law.⁹⁶

According to the Australian Taxation Office, the concept of ‘voluntary compliance’ entails adoption of the Australian Taxation Office’s interpretation of the law in cases of legal ambiguity. In a more recent (albeit brief) discussion of the concept of ‘legal ambiguity,’ the Commissioner accepts that there may be differing plausible interpretations of the law which are consistent with the policy intent (apparently assuming that the policy intent is discernible and sufficiently finite as to guide the construction of textual meaning).⁹⁷ In such circumstances the Commissioner states that he adopts that interpretation which produces the lower compliance costs. What this more recent statement overlooks is the fact that the policy intent may not be clearly discernible and, even if it is discernible, it may be so general as to be of limited use in elaborating the meaning of statutory terms. The policy of ITAA97 Div 152, for example, offers little assistance in gleaning the meaning of ‘in connection with your retirement’ in section 152-105.⁹⁸ In such circumstances the resolution of statutory meaning by the Commissioner will be influenced by the perspective adopted. Often, but not always,⁹⁹ this will mean that a taxpayer will be obliged to adopt a communitarian perspective when interpreting the law. From this perspective, a taxpayer is obliged to pay as much tax as might possibly be payable under relevant taxation laws. That is, a taxpayer/tax agent who interprets ambiguous law in favour of the taxpayer is considered to have adopted an ‘aggressive’ tax position, while a taxpayer who interprets ambiguous law in favour of the revenue is considered to be an exemplary cooperator.

This approach to labeling taxpayers who adopt an individualist stance as ‘aggressive’ is also found in the academic literature. Thus, for example, Richardson and Sawyer adopt the definition of Roth and Scholz,¹⁰⁰ noting that:

Although this definition allows for both intentional and unintentional compliance, it does not clarify whether the taking of an aggressive tax position on an ambiguous issue represents non-compliance if the revenue authority or courts fail to accept the treatment at a later date.¹⁰¹

Note here that there is no necessary connection between the aggressivity of the position adopted and any subsequent reversal of that position by a court – implicit within the statement is acknowledgement of the possibility that an aggressive position might be approved by subsequent court decision. Asserting a favourable position on an issue of legal ambiguity is labelled ‘aggressive’ because it contravenes the

⁹⁶ Id.

⁹⁷ Commonwealth of Australia, Large Business and Tax Compliance, above n 77.

⁹⁸ See, for example: Commonwealth of Australia, *A Post-implementation Review of the Quality and Effectiveness of the Small Business Capital Gains Concessions in Division 152 of the Income Tax Assessment Act 1997*, The Board of Taxation, Canberra, 2005, 4.

⁹⁹ See the discussion in section 5.5 below.

¹⁰⁰ See above n 58.

¹⁰¹ Maryann Richardson and AJ Sawyer, ‘A Taxonomy of the Tax Compliance Literature: Further Findings, Problems and Prospects’ (2001) 16 *Australian Tax Forum* 137 at 142. Adopting a favourable interpretation of ambiguous law and constructing a set of circumstances with a view to minimizing taxation, McBarnett’s ‘creative compliance,’ are quite different cases. Creative compliance might more readily be accepted to be ‘aggressive’ under both the communitarian and the contractarian view of taxation.

communitarian norm of paying as much tax as is possible which is, presumably, the ‘spirit of the law’.

The competing standpoints of communitarianism and private property mean that there are often competing interpretations of taxation law and, indeed, competing interpretations of the concept of ‘voluntary compliance’. Although there may be arguments for adopting communitarianism as a normative interpretive rule, such arguments have not received universal agreement. Indeed, given the cynical manipulation of substantive taxation law to the advantage of particular groups of taxpayers noted below,¹⁰² it is doubtful that a communitarian ethic truly is the will of the people.

4.2.1 Tripartism – basis for compromising incommensurable standpoints?

Ayres and Braithwaite implicitly suggest that their model of tripartism will resolve this problem of incommensurable standpoints. As noted in section 2.4 above, tripartism entails tripartite negotiation of regulatory outcomes in an environment of trust, which is defined to include a preference for cooperation.¹⁰³ Sitting between regulatee and public interest group representative, who respectively advocate opposing regulatory outcomes which are inconsistent with the law, it is envisaged that the regulator would broker a resolution which approximates ‘the democratic will’.

There are a number of theoretical and practical difficulties with this tripartite model:

- the most significant is that tripartism and the rule of law are mutually inconsistent. As noted above,¹⁰⁴ Ayres and Braithwaite indicated that the rule of law is definitional of responsive regulation. If so, there is no room for compromise regarding substantive regulatory outcomes. There may be room for compromise regarding how those outcomes are achieved, the imposition of penalties for non-compliance with determinate law (providing that such discretion is allowed under the relevant legislation) and such-like,¹⁰⁵ but the rule of law means compliance with determinate legal outcomes, not the brokering of deals;
- it may be that the commitment to ‘cooperation’ entails a commitment to striking a compromise, but it is not clear why an independent party would agree to ‘cooperate’ in this way if they genuinely believe that the law does not require such compromise. This problem is all the more salient because of the incommensurable standpoints which may underpin the discourse of regulator and regulatee.¹⁰⁶ In the absence of the protective shroud of the rule of law, tripartism could all too easily become state oppression of minorities and/or a cloak for regulatory capture. The failure to acknowledge the depth of the incommensurability challenge is also evident in the cursory suggestion that a compromise approximating ‘the democratic will’ will emerge.¹⁰⁷ Perhaps acknowledging the limitations of this

¹⁰² See the discussion in section 4.3 below.

¹⁰³ See text accompanying n 28.

¹⁰⁴ See section 3.2.

¹⁰⁵ To some, such legislatively authorized discretions are anathema to the rule of law: de Q Walker, above n 50.

¹⁰⁶ Ayres and Braithwaite refer to this problem of incommensurability, but seem to suggest that deliberative dialogue will ‘orient our practical and political lives’ (citing Bernstein): Ayres and Braithwaite, above n 21, 97. They do not deal with the problem of deliberation being undertaken under duress and nor do they deal with the problem that some might not agree with deliberative dialogue.

¹⁰⁷ Ayres and Braithwaite, above n 21, 82.

suggestion, Ayres and Braithwaite suggest that the two parties might ‘take turns’ at losing.¹⁰⁸ Again, it is not clear why a party who genuinely believes that their interpretation of the law is right would agree to take their turn at losing; and

- other shortcomings of this tripartite model include doubts about how trust, defined to include a preference for cooperation, could survive if regulatee and PIG routinely adopt ambit claims which are beyond what all acknowledge to be ‘the democratic will’, whether public interest groups would have sufficient resources to prosecute their claims, whether there is any need for a tripartite regulatory domain given that the law is assumed to be determinate and how tripartism could operate in a mass taxation context.

Perhaps with these shortcomings in mind, it seems that Braithwaite has resiled somewhat from the original conception of tripartism. In his *Markets in Vice Markets in Virtue*¹⁰⁹ he suggests that tripartism was incorporated into the Australian Taxation Office’s cooperative compliance model by the reference to ‘building community partnerships’.¹¹⁰ However, the discussion of building *bipartite* community partnerships in the Compliance Model is a far cry from the tripartism outlined by Ayres and Braithwaite, and so it is doubtful that ‘community partnerships’ embody tripartism. In any case, Braithwaite observes that tripartism has not been implemented as there has been no engagement with the community on a broad base.¹¹¹ Braithwaite therefore calls for an ‘assertive social movement politics’ which would, apparently, focus upon the tax profile of large corporations.¹¹² There is no discussion of what institutional changes would be necessary to engender such broad community oversight and in any case, it seems that tripartism is no closer to resolving the incommensurability of standpoints which its tripartite compromise of competing viewpoints promised.

4.3 Ad hoc legislation and the “spirit of the law”

As noted in section 3.2 above, some rely upon the spirit of the law¹¹³ or the ‘logic and policy’¹¹⁴ of the law as the basis upon which textual indeterminacy might be resolved. However, the third significant source of legislative indeterminacy is the fact that the tax legislation is riddled with myriad arbitrary rules and lacunae which defy identification of any logic, underlying purpose or ‘spirit’ of the law.¹¹⁵ The widespread exploitation of tax loopholes during the 1970’s¹¹⁶ prompted the introduction of the general anti-avoidance rules within Part IVA of the ITAA 1936. These rules purportedly protect the underlying purpose of the income tax law,¹¹⁷ but arbitrary

¹⁰⁸ Id, 85.

¹⁰⁹ John Braithwaite, above n 34.

¹¹⁰ Id, 73.

¹¹¹ Id, 73-4.

¹¹² Id, 207-8.

¹¹³ Although tax advisors generally express some mystification as to what the ‘spirit of the law’ actually is: Roman Tomasic and Brendon Pentony, ‘Tax Compliance and the Rule of Law: From Legalism to Administrative Procedure?’ (1991) 8 *Australian Tax Forum* 85.

¹¹⁴ Michael D’Ascenzo, ‘Along the Road to Damascus: A Framework for interpreting the tax law’ (2000) 2 *Journal of Australian Taxation* 384 at 389.

¹¹⁵ For a critique of the policy failures of successive governments see Richard Krever, ‘Taming Tax Complexity’ (2003) 25 *Sydney Law Review* 367. For an earlier expression of a similar view see; Rick Krever, ‘Avoidance, Evasion and Reform: Who Dismantled and Who’s Rebuilding the Australian Income Tax System?’ (1987) 10 *UNSW Law Journal* 215.

¹¹⁶ Margaret Levi, above n 12.

¹¹⁷ Michael D’Ascenzo, above n 114.

rules, poorly framed tax concessions and tax loopholes continue to cloud any putative purpose, if one exists at all.

The Commissioner compounds the problematic identification of the underlying purpose of the law by sanctioning some arrangements which appear, at least to many tax practitioners, to have all of the hallmarks of ‘aggressive tax avoidance’. For example, in his Media Release¹¹⁸ regarding superannuation recontribution arrangements the Commissioner indicated that the general anti-avoidance rules in Part IVA will not apply to common superannuation recontribution strategies. In essence, these strategies entail a taxpayer taking an eligible termination payment from a superannuation fund (which is subject to concessional taxation treatment)¹¹⁹ and recontributing that payment to the superannuation fund as the ‘purchase price’ of a superannuation pension. The effect of this arrangement is that the assessable amount of the superannuation pension will be less by comparison to the case of a similar taxpayer who merely rolled over their superannuation entitlement within the fund (ie without taking the benefit as an eligible termination payment and then recontributing it). By entering into a superannuation recontribution arrangement, then, the taxpayer is arbitraging the (low) immediate tax liability against the present value of the future taxation savings.

Such planning opportunities arise because of departures from the core taxing principles. In this case, the taxpayer is only taxed upon a fraction of their economic income by virtue of section 27C. The substance of the alternative means of obtaining a pension is essentially identical – in both cases the taxpayer uses their superannuation entitlement to ‘purchase’ a retirement pension. However, the form is different – taking money out of the fund renders it liable to (low) taxation as an eligible termination payment,¹²⁰ and the after-tax amount of the ETP is immediately reinvested into the same superannuation fund. The alternative form simply entails the money being retained by the superannuation fund and applied to the payment of a pension to the member.

The Commissioner’s acceptance of formalist ‘tax planning’ evidenced in his approach towards superannuation recontribution arrangements appears to be contrary to the Commissioner’s general approach to the application of Part IVA. In Practice Statement 2001/15 the Commissioner observes that ‘aggressive tax planning’ exhibits any or all of a range of indicia, including arrangements which are contrived or artificial in their execution, have little or no real underlying business purpose and arrangements that use tax exempt entities to ‘wash’ income.¹²¹ A superannuation recontribution arrangement appears to satisfy these indicia – the round robin payment, artificiality, and absence of non-tax justification for the arrangement and ‘washing’ income through a low tax entity are core aspects of the Commissioner’s definition of aggressive tax planning. It is therefore arguable that the Commissioner’s decision that Part IVA does not apply to at least some superannuation recontribution arrangements is inconsistent with the law which the Commissioner purports to uphold.

¹¹⁸ Commissioner of Taxation, Media Release Nat 04/058, 4 August 2004. The Commissioner indicates that a public ruling on such recontribution strategies will be released in the near future.

¹¹⁹ *Income Tax Assessment Act 1936* s 27C.

¹²⁰ *Income Tax Assessment Act 1936* s 27C.

¹²¹ Commissioner of Taxation, ‘Law Administration’, Practice Statement 2001/15.

The favourable treatment of superannuation by the Commissioner may be explicable on public policy grounds, but this favourable treatment has no clear legislative basis. By sanctioning a formalist approach in the case of superannuation recontribution arrangements, the Commissioner is signaling that, in circumstances of his choosing, he will vary his usual approach to the general anti-avoidance rules. This apparently arbitrary application of the general anti-avoidance rules may foster cynicism among tax advisors. Indeed, anecdotal evidence indicates that at least some tax advisors had advised clients against superannuation recontribution arrangements before the Commissioner’s press release upon the basis that such arrangements were too aggressive. One point which the research literature does not explore is whether such arbitrary administration of the taxation law causes tax advisors to lose confidence in the integrity of the taxation system and/or whether they take courage to explore other opportunities for minimizing tax on behalf of their clients.

5. PARTNERSHIP OR STRATEGIC ALLIANCE? LEGAL INDETERMINACY AND WHAT IT MEANS TO BE “COOPERATIVE” UNDER THE COOPERATIVE COMPLIANCE MODEL

The preceding discussion has outlined why the thesis that the law is determinate is fundamental to the cooperative compliance model. Further, the preceding discussion has indicated that there are good reasons for accepting that the law will often be indeterminate. There is clearly a need to consider the implications of legal indeterminacy for the cooperative compliance model.

5.1 Partnership, determinacy and legitimacy

The cooperative compliance literature repeatedly refers to the need to build a partnership with ‘the community’ and also with specific segments of the community such as small business, large business and also specific industry groups such as the building industry.¹²² Despite the significance of the concept of ‘partnership’ to the responsive regulation approach to tax compliance, the Australian Taxation Office has not published a comprehensive statement regarding the nature and operation of the partnership concept,¹²³ and nor is there a considered discussion of the partnership concept in the theoretical literature. Various aspects of the cooperative compliance model are considered in various ATO publications, however there is no comprehensive public document which details the nature of the model, strengths of the model, weaknesses of the model and institutional structures and strategies to counteract those weaknesses. Thus, for example, the Commissioner’s compliance strategy details the operation of the compliance model,¹²⁴ the Large Business compliance document offers a brief and limited consideration of the problematic concept of compliance in the context of indeterminate law¹²⁵ and the Annual Report offers some discussion of integrity assurance and transparency measures designed to

¹²² Commonwealth of Australia, *Improving Tax Compliance in the Cash Economy*, Australian Taxation Office, Canberra, 1998, 11; Commonwealth of Australia, *Cooperative Compliance- Working with Large Business in the New Tax System*, Australian Taxation Office, Canberra, 2000.

¹²³ The closest that the Australian Taxation Office has come to producing such a document is *Cooperative Compliance – Working with Large Business in the New Tax System* (above n 122). However, this document is restricted to providing operational guidance of the cooperative compliance model in a specific context, and so it does not offer a detailed elaboration of the core concepts upon which it is based.

¹²⁴ Commonwealth of Australia, above n 18, 3-4.

¹²⁵ Commonwealth of Australia, *Large Business and Tax Compliance*, above n 77.

assure community confidence in the operation of the cooperative compliance model.¹²⁶ There is no comprehensive, critical consideration of the cooperative compliance model. Such a document, if produced, would form the backbone of the Commissioner’s administrative strategy. A central aspect of such a document would elaborate upon the nature of the ‘partnership’ with the community to which the Commissioner refers.

A partnership connotes collective endeavour to achieve a mutual goal. The assumption of determinate law is integral to the limited mutual goal of the tax compliance partnership – *compliance* with ‘the law’. This integration of the determinacy thesis into the definition of the partnership means that the partnership need not reach a consensus upon the meaning of the law because this is a given. The sole purpose of the partnership is to develop ‘solutions’ for best implementing what is presumed to be determinate law.¹²⁷ Given this limited mutual goal, the responsive regulation literature implies that there is limited scope for the incommensurable standpoints described in section 4.2 above to threaten the mutuality of the partnership. Indeed, as noted in section 2.2 above, one function of responsive regulation is to generate discretionary authority in the state by shifting the population’s gaze, when considering whether to comply with a law, from questions regarding the morality of law to questions regarding the procedural fairness with which the law is administered. However, if legislative meaning is indeterminate, this exclusion of standpoint incommensurability from the regulatory domain must be reconsidered.

The issues to be addressed in undertaking this reconsideration of the compliance partnership include:

1. the identity of the partners;
2. the nature of the ‘partnership’, and in particular the implications for the existence of such a partnership if one accepts that the law is indeterminate. One key question here is whether the relationship is a partnership or a series of strategic alliances;
3. identification of the ‘partners’ and their respective roles, and in particular the significance of external stakeholders (ie government) to the partnership, the role of tax agents as partners in the context of a self assessment regime and their influence upon the nature of any partnership; and
4. whether there is one partnership with ‘the community’ or whether there are multiple partnerships with different segments of the community, and if the latter, how the confidence of the wider community in tax system integrity is maintained.

Given that it is now some ten years since the commencement of implementing responsive regulation in the taxation domain, it is timely that such issues be addressed.

5.2 Partnership with whom – Australian Taxation Office or government as a whole?

As noted in section 2.2 above, Tyler’s study of public perceptions of a small number of criminal laws suggested a link between legitimacy, procedural fairness and

¹²⁶ Commissioner of Taxation, *Annual Report 2005-06*, Australian Taxation Office, Canberra, 2006, 201ff.

¹²⁷ Commonwealth of Australia, above n 18, Commissioner’s Foreword (‘in accordance with law’).

voluntary compliance. This link is fundamental to the cooperative compliance model. However, it is possible that Tyler’s findings are inapplicable in the context of taxation law because of differing public perceptions of criminal law and taxation law respectively. Although Tyler noted the limitations of his study, and in particular the absence of literature demonstrating the applicability of his findings in other legal contexts,¹²⁸ little has been done to address this shortcoming with specific reference to taxation law.

An integral aspect of Tyler’s study was the accuracy with which it was assumed that survey participants would self-report their compliance with the laws in question.¹²⁹ Tyler perhaps too readily accepts that the public are in a position to judge whether they have complied with such rules. Nevertheless, it might be that these rules of criminal law have assumed a relatively determinate meaning in Tyler’s subject population. However, there is reason to doubt the relevance of Tyler’s work to taxation law, given that 52% of the respondents in one recent survey agreed that they felt ‘very confused about taxation matters’.¹³⁰ Further, the relevance of Tyler’s study to ‘voluntary compliance’ of indeterminate taxation law must be open to question because taxpayers confronted with indeterminate law may well not experience the same sense of obligation to comply with ‘the law’. Where taxpayers acknowledge that the law is indeterminate, they may well not confer upon the Australian Taxation Office the ‘discretionary authority’ to resolve such ambiguity as it sees fit.

There is clearly a need for further research in this domain in order to ascertain whether Tyler’s findings are applicable with respect to indeterminate taxation law. For example, it is possible that Tyler’s subjects viewed the criminal laws examined in his study more favourably than the Australian public perceives some or all of its taxation law. The criminal laws considered by Tyler had relatively obvious justifications in terms of members of a community co-existing in relative harmony – preventing those in control of vehicles on public thoroughfares from speeding, preventing drink driving, not disturbing neighbours with excessive noise, ensuring that people park their vehicles legally and preventing theft. It would be reasonable to expect wide public support for such rules. Of course such rules reflect political compromises regarding individual rights, the power of the liquor industry to prevent an outright ban on driving with any alcohol in one’s blood, etc. However, these laws are quite possibly perceived to be less politicized than, for example, taxation law. A meaningful comparison of perceptions of such laws has not been undertaken, and in any case it is doubtful that such a study would reveal propositions of general application. Nevertheless, one study indicates that the Australian public express considerable cynicism regarding Australia’s taxation institutions more generally,¹³¹ reflecting the fact that they accept that taxation law is highly politicized. In this context, it would be reasonable to speculate that there is a much lower store of legitimacy upon which the government might call in promoting voluntary tax compliance.

¹²⁸ Tyler, above n 22, 168.

¹²⁹ Id, 40.

¹³⁰ Commonwealth of Australia, *Community Perceptions Survey 2005*, Australian Taxation Office, Canberra, 2005.

¹³¹ Valerie Braithwaite, *Perceptions of Who’s Not Paying Their Fair Share*, Working Paper No 54, Centre for Tax System Integrity, Canberra, 2004.

Given that many Australians seem to view taxation law differently to the way in which Tyler’s subjects viewed criminal law, with whom should the partnership be constructed under the cooperative compliance model? If the public is cynical about the origin and fairness of taxation law, seeking to construct a partnership between the tax administration and the wider community might have minimal impact upon the legitimacy of taxation law because the public do not accept that procedural fairness is an appropriate proxy for substantive fairness in the taxation context. If so, the government will need to widen its agenda by seeking to construct a partnership between the wider community and the government’s taxation institutions as a whole. This would necessitate the adoption of tax system legitimization strategies, rather than merely the extant tax administration legitimization strategies.

5.3 Partnership or adversarialism

The indeterminacy of taxation law suggests that Tyler’s proposition, that voluntary compliance is enhanced by legitimacy and that legitimacy is enhanced by citizen perceptions of procedural fairness,¹³² must be reconsidered. Tyler’s study focused upon relatively ‘objective’ criminal acts, or at least, offences of a type which the general public would profess some understanding.¹³³ As it is founded upon the assumption of determinate law, Tyler’s study therefore does not necessarily offer guidance as to how taxpayer’s would behave in the context of indeterminate law. In particular, Tyler assumed that ‘voluntary compliance’ entailed action in accordance with relatively objective, determinate laws such as not exceeding a specified speed limit. There was no question of the relevant regulator seeking to redefine ‘voluntary compliance’ in terms of ‘compliance with the regulator’s interpretation of the law’. It is possible that taxpayers who encounter indeterminate law will be less influenced by perceptions of legitimacy and more influenced by self interest. If they do adopt a standpoint of self-interest, it is quite likely that they will adopt an understanding of ‘voluntary compliance’ which is at odds with that adopted by the regulator. The extract accompanying note 96 above indicates that this is the case. Further, as discussed below,¹³⁴ it seems that tax advisors adopt a more ‘aggressive’ advisory persona when advising upon uncertain law.

One ramification for the tax administration arising from the indeterminacy of law is that the meaning assigned to a taxation rule will depend upon a range of contextual factors, including the interpretive stance adopted by the particular tax official on a particular day and the tax official’s characterization of the circumstances of a particular case.¹³⁵ One such contextual factor is the Commissioner of Taxation’s statutory obligation to apply his available resources in order to achieve ‘proper use’ of available resources.¹³⁶ In the context of indeterminate law, it is reasonable to expect that the Commissioner will at least occasionally interpret his managerial obligation in such a way that he will ‘play for the grey’ in seeking to maximise the revenue, rather

¹³² Tyler, above n 22, 172.

¹³³ The offences about which the survey subjects were questioned were exceeding the speed limit, parking offences, making sufficient noise as to disturb neighbours, drink driving and theft.

¹³⁴ See section 5.5.2 below.

¹³⁵ Owing to the fact that the concept of a fractured self, as opposed to a unified, coherent self, is the basis of modern psychology and sociology. For acknowledgement of this point in the context of responsive regulation see: Valerie Braithwaite, above n 13, 21.

¹³⁶ *Financial Management and Accountability Act 1997* (Cth) s 44(1). Subsection 44(2) defines ‘proper use’ as ‘efficient, effective and ethical use’, without defining those terms.

than conceding that legal indeterminacy means that interpretive discretion should be exercised in favour of the taxpayer. Thus:

- the Commissioner’s compliance strategy makes no mention of identifying areas of overcompliance, despite the fact that there is some evidence that a substantial number of tax returns might result in overpayment of tax;¹³⁷
- the Commissioner might adopt unduly favourable interpretations of case decisions. For example, by focusing upon the joint judgment of two of five High Court justices in the High Court decision of *Hart*,¹³⁸ the Commissioner ignores the substantial uncertainty regarding the meaning of ‘scheme’.¹³⁹ It is difficult to believe that this partial reading of the High Court’s decision is anything but a deliberate attempt to portray the decision in the most favourable (for the revenue) light possible;
- the Commissioner appears to have adopted a selective approach to funding litigation under his test case program, apparently with the view to maximizing the likelihood of obtaining favourable outcomes;¹⁴⁰
- the recent Burges report¹⁴¹ illustrated that large business taxpayers believe that the Commissioner routinely adopts ambit positions which are not necessarily supported by the law. It might also be noted that the manner in which the Burges inquiry was undertaken reflects the sense of distrust between the Commissioner and members of this group of taxpayers which is undesirable in a partnership; and
- the adoption of ‘aggressive’ litigation strategies,¹⁴² notwithstanding the Commissioner’s suggestion to the contrary.¹⁴³

These factors indicate that, at least in some contexts, the Commissioner has responded to legal indeterminacy by adopting an adversarial, revenue maximizing stance. Of course, it is reasonable to expect that at least some taxpayers will also adapt to the indeterminate domain of tax law by adopting adversarial, self-interested positions. Further, as discussed in sections 4.3 and 5.5, the Commissioner will tolerate or accept such self-interested stances for a variety of reasons. The point is that such adversarialism is founded upon incommensurate standpoints, rather than mutual interest, and is therefore destructive of efforts to create a partnership.

¹³⁷ Roth, Scholz and Witte, above n 58, vol 1, 51-54. Most recently, see Republic of Ireland, *Interim Report on Under-claiming of Tax Credits, Allowances and Relief*, Joint Committee on Finance and the Public Service, Eighth Report, Dublin, 2007.

¹³⁸ *FCT v Hart* (2004) 217 CLR 216.

¹³⁹ See the discussion of the *Hart* decision in Law Administration Practice Statement PS/LA 2005/24 para 54ff; cf Justin Dabner and Mark Burton, ‘Hart – the death of tax planning?’ (2004) *CCH Tax Week* 373.

¹⁴⁰ Commonwealth of Australia, *Review of Tax Office Management of Part IVC Litigation*, Report of the Inspector-General of Taxation, Inspector General of Taxation, Sydney, 2006, Ch 6, esp para 6.186.

¹⁴¹ Kevin Burges, *Report on the concerns of a number of the largest companies in the Large Business Segment, with ATO audit, investigation and advice procedures*, Australian Taxation Office, Canberra, 2005.

¹⁴² *FCT v Indoороopilly Children Services (Qld) Pty Ltd* 2007 ATC 4236; discussed in Elizabeth Kazi, “ATO drops aggressive legal tactics” and “Ruling may go beyond the fringe” (6 March 2007) *Australian Financial Review* 1 and 6 respectively.

¹⁴³ The Commissioner maintains that the Australian Taxation Office upholds the model litigant policy of the Commonwealth government: Michael D’Ascenzo, Do professionals have an ethical compass and does it matter? Speech delivered to the Victorian Tax Bar Association, Melbourne, 30 March 2007.

5.4 Partnership and the problem of incommensurability

The indeterminacy of law also problematises the implementation of the compliance pyramid because of the fact that the Commissioner and taxpayers might have quite different understandings of what it means to comply with the tax law in specific contexts. By contrast to the adversarialism discussed in the preceding paragraph, such conflicting interpretations might be genuinely held in the sense that both parties genuinely believe that they have arrived at the 'correct' amount of tax to pay. This was acknowledged, for example, by the Senate Economics References Committee in its consideration of the mass marketed tax minimization arrangements of the 1990's.¹⁴⁴

If 'cooperation' with the Commissioner is central to the concept of compliance, taxpayers who are not in a financial position to challenge the Commissioner's interpretation will feel coerced into complying with what they consider to be an incorrect interpretation of the law. Here, the Commissioner's adherence to the proposition of determinate law can cause real damage to the perceived legitimacy of the tax system at an individual level because the Commissioner fails to acknowledge that incommensurable interpretive standpoints may lead to different, plausible interpretations. By enforcing what he considers to be the correct interpretation of the law, it is possible that taxpayers will submit to the Commissioner's coercive power but move to a different compliance posture in the future. Again, such an outcome would be destructive of any partnership with the taxpayer.

5.5 Indeterminacy and the diffusion of social power – the genesis of strategic alliances

The third implication of legal indeterminacy for the concept of partnership is that officers within the Australian Taxation Office might be less secure about what compliance means in a particular case. Meaning will be contingent upon the interpretive stance adopted by the particular tax officer in the specific case and having regard to other contextual factors. Thus the neat dichotomous categorization of taxpayers depicted in the compliance pyramid, between compliers and non-compliers, will be problematic. Instead of black and white, there will be many shades of grey. As different tax officials interpret the law and taxpayers' circumstances differently, there is the possibility that the Australian Tax Office will speak with multiple dissonant voices as its officers grapple with the indeterminacy of the rules they are meant to enforce.¹⁴⁵

5.5.1 Strategic alliances and diffuse social power

If there is no mutual understanding upon which a partnership between the taxation office and the wider community can be grounded, social power is far more diffuse than portrayed under the top-down paradigm of responsive regulation.¹⁴⁶ Without the clear authority of the law underpinning his administration of the tax system, the Commissioner is not the omnipotent regulator depicted in command and control regulatory models, or for that matter in the responsive regulation model. Instead, the Commissioner must choose his targets carefully, hoping that he survives the rigours of public challenge and judicial scrutiny relatively unscathed. If the Commissioner is

¹⁴⁴ Commonwealth of Australia, *Inquiry into Mass Marketed Tax Effective Schemes and Investor Protection*, Interim Report of the Senate Economic Reference Committee, Canberra, 2001, 26ff.

¹⁴⁵ See, for example, the examples of inconsistent administrative response in: TNS Research, *Review of the Taxpayers' Charter 2005*, TNS Research, Perth, 2006, 53.

¹⁴⁶ Mitchell Dean, above n 8.

perceived to be compelling taxpayers to adopt a communitarian outlook, he risks fuelling counterproductive public perceptions of oppressive conduct¹⁴⁷ which could all too easily fuel widespread tax protest¹⁴⁸ and a legitimacy crisis. Doubtless, well resourced taxpayers could exert considerable pressure upon the Commissioner through such ‘public information’ and lobbying efforts.¹⁴⁹ The Australian Taxation Office will be reluctant to pursue dubious cases for fear that unfavourable decisions will undermine their projection of concentrated state power reflected in the compliance pyramid.¹⁵⁰

In this context of diffuse social power, the best that the Commissioner can hope for is a series of strategic alliances with different segments of the community. A strategic alliance entails otherwise independent parties pursuing their respective objectives by means which happen to coincide. Rather than appealing to what is often portrayed as the communitarian spirit of the law, the existence of strategic alliances is founded upon self interest:

An important element of the building and construction project is the establishment of good relationships with industry bodies and the unions. For example, meetings have already been held with the HIA and MBA. They are supportive of the ATO approach to achieve a level playing field so that cash operators are not able to gain a competitive advantage over compliant businesses.¹⁵¹

Here the building industry lobbyists were prepared to engage with the ATO in order to advance the interests of their members by neutralizing the competitive advantage of non-compliant builders. However, extrapolating from this standpoint of self-interest, it would be reasonable to expect that this relationship would cease if the ATO proposed a program which was disadvantageous to HIA and MBA members but advantageous to the broader community.

To similar effect, Braithwaite proposes that special deals be negotiated with specific groups of self-interested taxpayers:

A dilemma of business-industry partnership is that business norms are not pro-tax, but anti-tax ... A risk of partnership, therefore, is that the tax office will be captured by an anti-taxpaying culture. One idea for a paradigm of community partnership to respond to this change (sic) of capture would, we suspect, be premature until some of the other strategies in this chapter were given more time to work. This is the idea of the government negotiating with the business community a *compliance-tax-rate-spiral*. The reason that it may be a bad idea at this time is that there are too many corporations presently

¹⁴⁷ Commonwealth of Australia, *Inquiry into Mass Marketed Tax Effective Schemes and Investor Protection*, Final Report of the Senate Economics References Committee, Parliament of Australia, Canberra, 2002, 22ff.

¹⁴⁸ Marjorie Kornhauser, ‘Legitimacy and the Right of Revolution: The Role of Tax Protests and Anti-Tax Rhetoric in America’ (2002) 50 *Buffalo L Rev* 819.

¹⁴⁹ Michael Carmody, ‘Administering Australia’s Tax System’ Monash University, Law School Foundation Lecture, 30 July 1998; see also George Megalogenis, ‘Cheats lobbying politicians to pressure the ATO’ *The Australian*, 31 July 1998, 5.

¹⁵⁰ Braithwaite acknowledges this shortcoming of the general anti-avoidance rules: J Braithwaite, above n 34, 63.

¹⁵¹ Australian Taxation Office, *Improving Tax Compliance in the Cash Economy*, Australian Taxation Office, Canberra, 1998, 12.

paying no tax who therefore have no interest in trading off higher compliance for lower company tax rates. However, floating the possibility of a *compliance-tax-rate-spiral* as something that might work in future could encourage public-regarding business taxpayers to see that in the long run there is much that Australian business could gain from a more cooperative compliance culture.¹⁵²

Presumably public regarding businesses are already voluntarily complying with the law, so it is not clear how this compliance tax rate spiral would induce non-taxpaying taxpayers to pay tax. It is possible that lower tax rates will induce non-taxpayers to pay some tax because the perceived costs of minimizing tax are greater than complying. But this shift in behaviour would be based upon calculations of self interest, a prospect which Braithwaite acknowledges. The danger for Braithwaite’s model is that once it has embarked upon this cycle of self interest, the government may never be in a position to break out into a cycle of ‘public regarding’ compliance. In any case, there are a number of other problems with this proposal, given that the integrity of the taxation administration is crucial to winning the wider community over to the model of cooperative compliance.¹⁵³ For example, if such special arrangements are entered into on a one-to-one basis, the Commissioner’s secrecy obligations mean that such arrangements cannot be transparent. Further, whether or not such arrangements were transparent, it might reasonably be expected that such favourable deals will be viewed cynically by others in the community, who might see such arrangements as yet another instance of regulatory agencies being too close to big business.¹⁵⁴ After all, the message that such an arrangement would send is that tax avoiders can broker a special deal simply by being especially successful at tax avoidance. Accordingly, other taxpayers might understandably be more inclined to hold back from embracing the communitarian ethic in order to minimize their tax and/or broker their own special deal:

Go too far in reducing penalties and interest and it may be difficult to justify the result to the community generally and to those who face penalties and interest for debts unrelated to any participation in tax avoidance schemes in particular.¹⁵⁵

With this descending spiral of special deals brokered by self-interested taxpayers, the communitarian ethic would quite possibly recede ever more into the distance, leaving cynicism to prevail.

5.5.2 Strategic alliances and the role of tax advisors

The preceding discussion suggests that the indeterminacy of taxation law problematises the creation of a partnership between the Taxation Office and the community, because it may not be possible to identify a mutual ‘enterprise’. In the

¹⁵² John Braithwaite, ‘Large Business and the Compliance Model’, in Valerie Braithwaite (ed), above n 13, 177 at 188-9. It is not clear how inducing ‘public regarding’ corporations (which, presumably, are less deeply imbued with an ‘anti-taxpaying culture’ in the first place) will lead non-public regarding corporations to embrace a cooperative compliance culture. Moreover, it is not clear how negotiating a *compliance-tax-rate-spiral* will counteract regulatory capture on the part of tax administrators who are seeking a partnership with members of the community who adopt an ‘anti-taxpaying’ stance.

¹⁵³ Braithwaite and Braithwaite, above n 17, 218.

¹⁵⁴ Braithwaite, above n 11, Item 4.1.7.

¹⁵⁵ Michael D’Ascenzo, ‘In Defence of the Rule of Law’, Speech delivered to Law Council of Australian Taxation Law Workshop, Aitken Hill, Victoria, 26-28 October 2001.

absence of determinate law which grounds a mutual understanding of compliance, interpretive differences between the Taxation Office and taxpayers can only be resolved by an exercise of power. It is possible that such an exercise of interpretive discretion is perceived as benign. Equally, the Commissioner can be perceived to be as unreasonable in ‘chasing down every last cent’ which might possibly be justified under the legislation as taxpayers can be unreasonable in avoiding paying every last cent of tax on the basis of a diametrically opposed interpretation.

As intermediaries between taxpayers and tax administrator, ‘tax advisors’¹⁵⁶ can be expected to play a pivotal role in shaping the nature of the relationship between the two parties.¹⁵⁷ This might be negative for the Tax Office, given that tax advisors as a group are more critical of the Australian Taxation Office with respect to specific performance indicators than other segments of the community.¹⁵⁸ Much of the literature dealing with the influence of advisors upon taxpayer compliance adopts a definition of compliance which assumes that the taxation law is determinate¹⁵⁹ – very little of this literature has considered the role of tax advisors where the law is ambiguous.¹⁶⁰ Nevertheless, the literature indicates that tax advisors assume different persona in different contexts. In performing routine ‘tax compliance’ work, such as lodging administrative forms and applying settled law to straightforward cases (ie deductibility of usual and appropriate business expenses), it seems that tax advisors adopt a ‘compliance’ outlook and therefore assume a ‘tax administration’ persona. However, where the law is ambiguous, it seems advisors adopt an ‘aggressive’ stance in assisting their clients to minimize their tax.¹⁶¹ Thus, although the data indicates that

¹⁵⁶ It should be noted that ‘tax advisors’ is used broadly here, and so is not restricted to registered tax agents and lawyers giving tax advice. Financial planners also play a prominent role in giving advice which affects the tax paid by taxpayers.

¹⁵⁷ Commonwealth of Australia, *The Australian Taxation Office’s Management of its Relationship with Tax Practitioners*, Performance Audit Report No 19 2002-03, Australian National Audit Office, 2003, 38-40; Maryann Richardson and AJ Sawyer, above n 101, 210.

¹⁵⁸ TNS Research, above n 145; Interestingly, Tyler observes that the more highly educated a person is the lower their perception of state legitimacy: Tyler, above n 22, 47. Tyler states that this is consistent with the earlier work of Sarat: A Sarat, ‘Support for the legal system’ (1975) 3 *American Politics Quarterly* 3.

¹⁵⁹ Thus, for example, tax compliance has been defined as ‘reporting all income and paying all taxes in accordance with the applicable laws, regulations and court decisions’: J Alm, B Jackson and M McKee, ‘Alternative Government Approaches for Increasing Tax Compliance’ (1992) 90 *TNT* 260; see also the definition of compliance adopted by Richardson and Sawyer: above n 101.

¹⁶⁰ Note that Richardson and Sawyer observe that their definition of ‘compliance’ would mean that aggressive tax planning is ‘compliant’ behaviour; id, 210. Note, however, that where general anti-avoidance provisions apply to such ‘aggressive tax planning’, clearly the behaviour would be non-compliant.

¹⁶¹ In this regard an influential study was that of Steven Klepper, Mark Mazur and Daniel Nagin, ‘Expert intermediaries and legal compliance: the case of tax preparers’ (1991) 34 *Journal of Law and Economics* 205 (arguing that tax preparers assumed the dual role of tax code enforcer when the law was ‘unambiguous’ and tax loophole exploiter where the law was ambiguous). For other studies indicating a correlation between tax preparer use and ‘non-compliance’ see: PA Hite, ‘The effect of peer reporting behaviour on taxpayer compliance’ (1988) 9 *Journal of the American Taxation Association* 47; B Erard, ‘Taxation with representation: an analysis of the role of tax practitioners in tax compliance’ (1993) 52 *Journal of Public Economics* 163; JC Young, ‘Factors associated with noncompliance: evidence from the Michigan tax amnesty program’ (1994) 16 *Journal of the American Taxation Association* 82.

clients prefer low risk tax returns, it may be that in the context of ambiguous law advisors and clients have differing understandings of the meaning of ‘low risk.’¹⁶²

Therefore a number of questions are worthy of further investigation:

1. in selecting a tax advisor and seeking advice, do taxpayers clearly express their tax risk preference, such that the significance of tax advisors’ influence is diminished? This is important because the personal opinions of tax advisors regarding the tax system might be outweighed by market forces – tax advisors would have to meet the tax advice market rather than tax advisors shaping that market;
2. whether the Commissioner’s cooperative compliance program has induced a communitarian ethic on the part of tax advisors, such that ambiguous law is interpreted less ‘aggressively’. Alternatively, have tax advisors adopted/maintained a self-interest ethic, under which they selectively negotiate strategic alliances with the ATO when in their clients’ respective interests, while adopting ‘aggressive’ stances when this is perceived to be in their clients’ respective interests; and
3. if such an ethical shift has arisen, what were the drivers and inhibitors of this shift and if such an ethical shift has not arisen, what might prompt such a shift? In particular, what is the significance of Taxation Office actions such as the publication of more information regarding the exercise of the Commissioner’s general administrative discretion, playing a pro-active role in shaping the way that tax advisors interact with the ATO and so forth?

5.5.3 Demand driven cooperative compliance?

Whether taxpayers’ risk preferences dictate the outcome of tax advice was recently considered in Australia by Braithwaite and Sakurai.¹⁶³ After analyzing survey data Sakurai and Braithwaite contend that a majority of taxpayers are relatively conservative in their attitude towards selecting a tax advisor. The majority of taxpayers, the authors suggest, state that their ideal tax advisor is one in whom they can trust to adopt a ‘minimum fuss’ approach to tax compliance. This would suggest that clients’ preferences within the financial services market would act as a significant brake upon the deployment of creative compliance strategies. However, three observations should be noted with respect to this finding.

First, the nature of the survey relied upon by Braithwaite did not enable the respondents to elaborate upon what they understood to be a ‘minimum fuss’ approach to tax compliance.¹⁶⁴ Presumably, ‘minimum fuss’ is synonymous with ‘compliance’.

¹⁶² Peggy A Hite and Gary A McGill, ‘An Examination of Taxpayer Preference for Aggressive Tax Advice’ (1992) 45 *National Tax Journal* 389.

¹⁶³ Yuka Sakurai and Valerie Braithwaite, ‘Taxpayers’ perceptions of practitioners: Finding one who is effective and does the right thing?’ accessed at <http://ctsi.anu.edu.au/publications/taxpubs/Sakurai.VB.pdf>; cf A Christensen, ‘Evaluation of Tax Services: A Client and Preparer Perspective’ (1992) *The Journal of the American Taxation Association* 160.

¹⁶⁴ Question 11.11 merely asked ‘What priority would you place on the following qualities if you were to choose a tax agent or advisor?’ Respondents were offered a range of alternative descriptions, one being ‘someone who will do it honestly and with minimum fuss’. It might be noted that ‘minimum fuss’ is ambiguous – does it mean ‘avoiding confrontation with the ATO’ or does it mean ‘not fussing with the client about dotting every I and crossing every t’?

However, given the preceding discussion regarding the indeterminacy of the compliance concept, it is clear that there are shades of grey which the survey data does not tease out. After all, it should be remembered that many of those who participated in 'aggressive tax minimization arrangements' claimed to have taken appropriate steps in ensuring that their arrangements were 'within the law' and were not 'aggressive'.¹⁶⁵ The Senate Economics Committee final report even acknowledged that the ATO appeared to lend some credence to this view by its ambivalent response to such schemes.¹⁶⁶ Further, the prominent role of financial advisors¹⁶⁷ in promoting so-called 'aggressive tax minimization arrangements'¹⁶⁸ indicates that they wield considerable influence with clients who generally have low financial literacy¹⁶⁹ and who, as a group, purportedly prided themselves upon their good tax compliance record.¹⁷⁰ The recurrent theme of testimony given by taxpayers embroiled in these schemes was that their professional advisor considered that the relevant scheme was 'within the law'.¹⁷¹

The nature of this problem may be illustrated by reference to the Tax Commissioner's statement regarding superannuation retribution arrangements.¹⁷² Clearly an arrangement which appears to fall within the somewhat vague description of such arrangements provided by the Commissioner is a 'minimum fuss' arrangement, but what of a similar arrangement which is not within this administratively defined safe harbour? A tax advisor, for example, might provide a client with some illustrations of the types of express loopholes under the taxation law by way of illustrating the arbitrary nature of the existing taxation law. The tax advisor might then recommend a particular arrangement to a client, perhaps a variation of an 'authorised' superannuation retribution arrangement, which the advisor considers to be legitimate. The advisor might suggest that the taxpayer enter into such an arrangement, noting that other taxpayers are 'playing a similar game' but benefiting from the Commissioner's favourable treatment of some tax minimization arrangements. The point is that financial advisors do not provide advice with respect to a tax system which is founded upon the dichotomy of compliance/non-compliance. Advisors are not necessarily 'playing for the grey' but, rather, are swimming in a sea of grey.

Second, it is not clear how clients with a preference for 'minimum fuss' advice will accurately identify providers of such advice. That taxpayers seek advice in order to

¹⁶⁵ Commonwealth of Australia, *Inquiry into Mass Marketed Tax Effective Schemes and Investor Protection*, Interim Report of the Senate Economic Reference Committee, Canberra, 2001, 26ff; see also Commonwealth of Australia, *Inquiry into Mass Marketed Tax Effective Schemes and Investor Protection*, Final Report of the Senate Economics References Committee, 2002, 20ff.

¹⁶⁶ Cf Michael D'Ascenzo, 'In Defence of the Rule of Law', Speech delivered to Law Council of Australian Taxation Law Workshop, Aitken Hill, Victoria, 26-28 October 2001.

¹⁶⁷ According to then Second Commissioner Michael D'Ascenzo, some 97% of the 35,000 taxpayers involved in mass marketed tax minimisation arrangements were advised by a tax advisor: Michael D'Ascenzo, above n 166.

¹⁶⁸ A nomenclature which seems to imply that 'non-aggressive', but nevertheless deliberate, tax minimising, arrangements are somehow different.

¹⁶⁹ Chant Link and Associates, *A Report for ASIC on Consumer Decision Making at Retirement*, Report No 2514, Sydney, 2004, 52ff.

¹⁷⁰ Commonwealth of Australia, of Australia, *Inquiry into Mass Marketed Tax Minimisation Schemes and Investor Protection*, Interim Report of the Senate Economics Committee, AGPS, Canberra, 2001, ch 3.

¹⁷¹ Commonwealth of Australia, *Inquiry into Mass Marketed Tax Minimisation Schemes and Investor Protection*, Interim Report of the Senate Economics Committee, AGPS, Canberra, 2001, ch 4.

¹⁷² Commissioner of Taxation, op cit n 118.

obtain assurance that they are within the law has been supported by a number of studies in several jurisdictions.¹⁷³ However, the literature in this field indicates that clients and tax advisors often talk at cross purposes when discussing relative levels of audit risk with respect to particular items on a tax return.¹⁷⁴

Third, the Braithwaite/Sakurai study does not indicate whether taxpayers would adopt a ‘minimum fuss’ approach where to do so created a higher perceived tax burden than would apply if some tax minimizing advice were followed. As Braithwaite notes, survey responses are context dependent.¹⁷⁵ With this in mind, it would be useful to know whether those who opted for a ‘minimum fuss’ approach would have responded similarly if told that this approach would effectively cost them \$10,000 by comparison to a ‘legitimate’ restructuring of their affairs akin to the formalism of a superannuation retribution arrangement. Braithwaite’s conclusions as to taxpayer attitudes to compliance must be read cautiously, owing to the significant prospect that taxpayer attitudes towards compliance may vary with the context in which those attitudes are formed.

5.5.4 Cooperative compliance and tax advisors – the need for further research

Assuming that tax agents do play a significant role in shaping their client’s risk profiles, responsive regulation posits that tax agents will adopt the cooperative, communitarian ethic of the responsive regulator and induce their clients to gravitate to the base of the compliance pyramid. Unfortunately, there is insufficient data to assess whether this effect is identifiable. In a recent survey undertaken by TNS Consulting, it seemed that tax agents as a group are more negative regarding Australian Taxation Office performance against its Charter, but it also seems that tax agent opinion of the ATO has improved over recent years.¹⁷⁶

This research does not answer the question of whether the cooperative compliance model is engendering a new approach to ‘voluntary compliance’ on the part of tax advisors. Further research needs to be undertaken in order to ascertain whether the apparent improvement in tax advisor perceptions of the ATO has translated into less ‘aggressive’ stances being recommended to clients in areas of ambiguity/creative compliance.

5.6 Partnership or regulatory capture?

If the relationship between the tax administration and at least some taxpayers in some circumstances is best conceived in terms of a strategic alliance, and a strategic alliance in an indeterminate legal domain, one critical question is whether there are sufficient safeguards in place to ensure that the Commissioner is not captured by powerful interest groups. Indeed, one reason given for the adoption of responsive regulation was that a command and control approach to regulation predisposed regulators to being ‘captured’ by regulatees because regulators were reluctant to use the big sticks available to them in a one dimensional regulatory response.

¹⁷³ LM Tan, ‘Taxpayers’ Preference for Type of Advice from Tax Practitioner: A Preliminary Examination’ (1999) 20 *Journal of Economic Psychology* 431 (New Zealand); PA Hite and G McGill, ‘An Examination of Taxpayers’ Preference for Aggressive Tax Advice’ (1992) 45 *National Tax Journal* 389 (USA); Pauline Niemirowski and Alexander Wearing, ‘Taxation Agents and Taxpayer Compliance’ (2003) 6 *Journal of Australian Taxation* 166 at 196 (Australia).

¹⁷⁴ Hite and McGill, above n 173, 390-1.

¹⁷⁵ Braithwaite, above n 13, 16-17.

¹⁷⁶ TNS Research, *Review of the Taxpayers’ Charter 2005*, TNS Research, Perth, 2006, 16-17.

The concept of regulatory capture is open to various definitions, ranging from corrupt conduct to subtle indications regarding the regulator’s future career path to even more subtle influencing of the regulator’s outlook which affects the application of law in the grey zone.¹⁷⁷ Thus, for example, when considering the possible application of Part IVA, a regulator might be influenced by the neoliberal discourses of regulatory compliance costs, efficiency/risk assessment and international business competitiveness, discourses which they encounter on a daily basis in their dealings with large business taxpayers. Such discourses often lead to a different conclusion than that arrived at from some other deontological standpoint such as ‘it is right to pay tax’.

Clearly, in talking of building partnerships with ‘stakeholders’ such as large business taxpayers, there is a real risk of some form of regulatory capture occurring. Unfortunately, to date the literature regarding responsive regulation in the taxation domain does not grapple with this issue adequately.

In the recent past there are sufficient indications of a failure of overt institutional integrity assurance as to raise concerns about the prospect of regulatory capture or, at best, regulatory failure. For example:

- as discussed by Grbich¹⁷⁸ and Braithwaite,¹⁷⁹ the ‘Petrolias affair’ is cause for concern regarding the extent to which the tax administration has allowed a neoliberal ‘risk management culture’ to diminish the legitimacy of the tax administration because of the use of ‘strategic alliances’ to advance the interests of some taxpayers at the expense of others;
- the membership and terms of reference of the Commissioner’s ad hoc advisory committees are less than inclusive of the wider community, and moreover the nature of the Australian Taxation Office response to matters raised by such committees is not clear;¹⁸⁰
- the recent management of small business tax debt¹⁸¹ raises the same query regarding the integrity of the tax administration; and
- the Commissioner’s integrity assurance mechanisms are themselves not transparent.¹⁸²

It may be that the statutory secrecy obligations of the Commissioner with respect to taxation information have had their day. Conceived in an era where command and control regulators were assumed to impartially enforce the ‘democratic will’, secrecy of tax information was justified upon the basis that executive government could be trusted to do its job. In the new era of discretionary administration of indeterminate law, there is at least a case for enhancing the transparency of tax administration by

¹⁷⁷ See the material cited at n 49 above.

¹⁷⁸ Yuri Grbich, ‘After Bellinz and Ralph: a new focus for decision-making in the Australian tax system’ in Michael Walpole and Chris Evans, *Tax Administration in the 21st Century*, Prospect, Sydney, 2001, 11.

¹⁷⁹ Braithwaite, above n 34, 41, 61, 73.

¹⁸⁰ Burton, above n 61; Braithwaite, above n 34, 73.

¹⁸¹ Inspector-General of Taxation, *Review into the Tax Office’s Small Business Debt Collection Practices*, Commonwealth of Australia, Canberra, 2005. Fleur Anderson, ‘Direct calls to small business pay off for Tax Office’ *Australian Financial Review*, 23 August 2006, 11.

¹⁸² For discussion of this see: Burton, above n 61.

lifting the veil of secrecy. Indeed, Braithwaite speculates that such action may be appropriate in the case of large corporate taxpayers,¹⁸³ although he does not explain why restricting tax system transparency to this demographic group would be appropriate. The most obvious benefit of such an approach would be that the Commissioner would not need to devote as many resources to integrity assurance measures designed to promote community confidence in the tax administration. Further research needs to be undertaken with a view to identifying the relative merits of a relaxation of the Commissioner's secrecy obligations.

6. CONCLUSION

There can be little doubt that the cooperative compliance model represents a quantum shift in the taxpayer/tax administration relationship, and it is doubtful that many would argue for a return to the adversarial approach of the past. Nevertheless, the cooperative compliance model is still under development. The purpose of this paper was to identify the weaknesses of the cooperative compliance model, not with the object of rejecting the model but rather with a view to identifying those areas which require further theoretical/empirical research.

The rhetorical strength of the responsive regulation paradigm rests upon the rule of law because the proposition of determinate law is central to the success of the responsive regulation paradigm. Knowing who is complying and who is not complying, who are the 'cheats' and who are 'socially irresponsible', makes it easy to legitimize responsive regulation. Under this regulatory model, encouraging taxpayers to comply with 'the law' and deploying enforcement powers against those who resist seems a sensible approach to managing a mass tax system with limited resources. Within this paradigm it is accepted that the Commissioner cannot be expected to achieve perfect neutrality in the sense of 'chasing down every last cent'. However, the legitimacy of administrative action rests upon the belief that the Commissioner is amoral in his administration of 'the law' – that the Commissioner is merely implementing 'the democratic will' and so is not adversarial but fair, he is not partisan but impartial. The exercise of state power is neutral and efficient. Offering such a reassuring depiction of tax administration, it is little wonder that the troubling ambiguity of taxation law receives fleeting attention within the responsive regulation literature.

Paradoxically, however, adherence to the determinacy thesis is the Achilles heel of responsive regulation. At least some significant aspects of the taxation law are indeterminate. As the Commissioner acknowledged in 1992, such ambiguity goes to the heart of the concept of compliance for those with the resources to explore such ambiguity.¹⁸⁴ Why, then, does the Commissioner persevere with the discourse of partnership? In part, adherence to the belief in determinate law is testimony to the rhetorical power of the rule of law. It may be that, living in what purports to be a liberal democracy, contemplating a world in which the law is not determinate is simply too horrific for many to accept that our noble liberal dream is in fact a nightmare of unfettered executive and/or judicial discretion. In any case, there are good strategic reasons for the Commissioner to adhere to this position, even if he at times implicitly seems to recognize that the tax law is not determinate. Most

¹⁸³ Braithwaite, above n 34, 160-1.

¹⁸⁴ Boucher, above n 2.

importantly, adherence to the legal determinacy thesis enables the Commissioner to adopt a 'don't shoot the messenger' discourse – 'I am only applying the law' – when confronted with allegations of partial tax administration or when subjected to political pressure.¹⁸⁵ More cynically, endorsing the proposition that 'the law is the law' means that the Commissioner is able to promote his interpretation of law, which he most probably knows to be contingent, as the 'right' interpretation. By doing so, he maintains the faith in impartial administration while in fact adopting contingent interpretations of ambiguous law. Further, by adopting this message, the Commissioner hopes to reassure the general public that all really are equal before the tax law, despite the evidence of regulatory capture which suggests the contrary.

Significant parts of the tax law are indeterminate and the implications of this indeterminacy for the cooperative compliance model must be the subject of further quantitative and qualitative research. In the absence of such research, it is possible that responsive regulation is not fulfilling its promise. It is possible, for example, that tax administration does not entail a partnership. Instead, Commissioner and taxpayer alike might pursue their respective interests as they best see them in specific contexts. In specific contexts, the interests of taxpayer(s) and tax Commissioner might overlap and so a strategic alliance will be formed. In other contexts, the interests of taxpayer(s) and Commissioner might diverge and any former strategic alliance will dissolve. It is possible, therefore, that effective tax administration is undermined by the failure to acknowledge the significance of law's indeterminacy for the cooperative compliance model. The limited evidence available suggests that these possibilities cannot be discounted. It is time to reconsider this model by undertaking further research.

¹⁸⁵ Michael Carmody, 'Administering Australia's Tax System' Monash University, Law School Foundation Lecture, 30 July 1998; see also George Megalogenis, 'Cheats lobbying politicians to pressure the ATO' *The Australian*, 31 July 1998, 5.