

Antecedents of Interpersonal Trust in Tax Audits

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ABSTRACT

Using a survey of 154 tax auditors (civil servants) we study the development of interpersonal trust between tax auditors and taxpayers during the course of a tax audit. Although the concepts of mutual trust, understanding and transparency are centrepieces of so-called enhanced relationship tax-compliance programs that have recently been developed worldwide the issue of interpersonal trust between the involved parties has been neglected by prior research. Drawing on insights from financial auditing research we investigate auditors' individual trait characteristics, auditee's behaviour during the conduct of the audit, and the level of conflict. We find that interpersonal trust develops independently from auditor's professional scepticism, while auditor's professional identification even promotes interpersonal trust. Further, it shows that also in a tax audit environment auditor's trust increases with the information quality and less opportunistic behaviour of the auditee, and in a low-conflict relationship. In addition to the theoretical contributions, the findings have practical implications for tax auditors and auditees.

Keywords: Trust, Tax Audit, Tax Administration, Tax Avoidance.

JEL Classification: H26, H25, K34

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1. Introduction

This study investigates the antecedents of an interpersonal trust relationship between tax auditors and an auditee representative. The concepts of “mutual trust, understanding and transparency” are centrepieces of so-called “enhanced relationship” tax-compliance programs that have recently developed worldwide and which are continuously growing in number and size. The OECD suggested the establishment of enhanced relationship programs (OECD 2008) to improve relationships between taxpayers and revenue bodies based on co-operation and mutual trust in order to avoid aggressive tax planning. According to that OECD study, such an enhanced relationship is assumed to increase taxpayers’ levels of compliance, reduce the taxpayers demand for aggressive tax planning and give revenue bodies better information about aggressive tax planning and therefore the opportunity to devise more effective responses. During the audit process, such an enhanced relationship should result in more effective audit procedures and higher audit quality.

So far, it is unclear if and under which conditions an interpersonal trust relationship can evolve during a tax audit. Prior research primarily focused on the taxpayer’s institutional trust. However, the mutuality of the concept “trust” calls for studying both sides of the trust relationship. Also the transferability of results from financial auditing is highly questionable since in contrast to the tax audit environment the financial audit environment incentivizes the auditor to engage in an interpersonal trust relationship. By focusing on the individual relationship between the civil servant performing the tax audit and the taxpayer representative, we provide insights from the “other side” of the mutual interpersonal trust relationship that is seen critical by the literature for promoting voluntary compliance and we therefore shed light onto an existing significant research gap in tax research.

Notwithstanding the highest levels of governmental confidentiality obligations we were granted permission to conduct a survey among 154 tax auditors (civil servants) from the *Large Businesses Assessment and Audit Unit* of the Austrian Ministry of Finance regarding their work experience. Our study investigates the effect of auditor’s demographic factors (age, gender and professional experience), auditor’s trait characteristics, such as professional identification (Bamber and Bamber 2009; Bamber

and Iyer 2007) and auditor trait scepticism (Hurt 2010), auditor's perception of the auditee representative's behaviour in the form of information quality and opportunistic behaviour, and on the relationship level, the level of conflict, on auditor's trust in the auditee representative during the tax audit. We employ the widespread approach of conceptualising and operationalising trust through perceived trustworthiness, as proposed by Mayer et al. (1995). Mayer et al. (1995) identify the trustor's perception of the trustee's *ability*, *benevolence*, and *integrity* as the three dimensions of trust.

Our results show that even in the highly antagonistic environment of a tax audit interpersonal trust relationships between tax auditor and the taxpayer (or the taxpayer's representative) emerges. The development of mutual trust is highly situation specific and predominantly shaped by the behaviour of the taxpayer's representative. The willingness to communicate openly and the quality of shared information by the taxpayer's representative facilitates, while opportunistic behaviour discourages the development of mutual trust. The tax auditor's professional scepticism does not inhibit the level of trust and a high level of professional identification of the tax auditor even enhances an interpersonal trust relationship. This shows that a professional attitude is not creating a barrier against interpersonal trust. Professional identification is even promoting trust of the tax auditor in the auditee, which might be due to the fact that the auditor's integrity is an important basis for trust.

Our findings have several implications for research and practice: This paper introduces an elaborated conceptualisation and operationalisation of interpersonal trust and related concepts into tax research. Further, due to the unique possibility of surveying civil servants that are otherwise bound by highly restrictive confidentiality obligations, the paper provides an empirical evidence on the emergence of interpersonal trust in tax audits for the first time. Further, our findings that professional scepticism and professional identification are not creating barriers for interpersonal trust emphasize the importance of selecting the right people as tax auditors who are both obeying to the profession's principles and able to build up a trust relationship. For taxpayers our results show that trust attracting behaviour also works in an environment, where the auditor has little incentives to engage in a trust relationship. Since a trustful relationship is seen by the literature as being more efficient and could lead to less time consuming and

less costly audit procedures taxpayers would benefit from establishing trustful relationships with “their” tax auditors.

The remainder of this paper proceeds as follows. Section 2 provides background regarding the role of trust in enhancing tax compliance and the importance of trust in interpersonal relationship and section 3 discusses related literature and develops our hypotheses. We present our research method and the results of our survey in section 4. Section 5 provides a discussion of the results and concludes.

2. Theoretical background to tax audits and trust

The importance of trust in interpersonal relationships is broadly recognized. Although trust is an important concept in many fields of research, there is no commonly used definition of trust (for a general review, see Nooteboom 2002). However the literature in general agrees on defining trust as the willingness of a party to take a risk (Lewis and Weigert 1985; Rotter 1967; Bhattacharya et al. 1998; Larzelere and Huston 1980; Fukuyama 1995; Möllering 2001, 2006) and “*to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to monitor or control that other party*” (Mayer et al. 1995 at p. 712). The main advantages of interpersonal trust include positive effects on information sharing, negotiations, and conflict resolution (Dyer and Chu 2003), its flexibility (Gulati 1995), and its robustness to changes in circumstances (Doz 1996). Further positive effects are the reduction of agency problems (Ring and van de Ven 1992), the cutback of transaction costs (e.g. Macaulay (1963)), reduced monitoring and control necessities (e.g. Zand (1972)), decreased use of legal actions (Sitkin and Roth 1993), increase in cooperation (e.g. Doz (1996)) and support of decision making in situations where information is scarce (e.g. Luhmann (2000)).

Trust has also been identified by the psychological tax literature as an important non-economic factor that drives and sustains taxpayers’ willingness to comply with the law (Braithwaite 2003; Murphy 2003, 2004; Kirchler et al. 2006; Tyler 2001, 2006; Pommerehne and Frey 1992; Torgler 2005; Wenzel

2002; Kastlunger et al. 2011; Kirchler et al. 2014). Based on the findings of the psychological tax literature the OECD in its *Study on the Role of Tax Intermediaries* (OECD 2008) recommends tax authorities to establish an environment in which trust and co-operation can develop so that “enhanced relationships” between taxpayers and revenue bodies can exist. Such a culture of mutual trust is seen as a significant facilitator of transparency, it can lead to more familiarity and better communication (OECD 2008; Cummins et al. 1996). In 2005, The Netherlands were the first to introduce an enhanced relationship program called “Horizontal Monitoring” whose key elements are “*mutual trust, understanding, and transparency.*” Around the same time, the IRS launched a similar program similar called Compliance Assurance Process (CAP) based on “*transparent and cooperative interaction between taxpayers and the IRS*”. Other countries such as Australia, Singapore, South Korea, New Zealand or the United Kingdom established similar programs based on mutual trust to facilitate interaction and cooperation between taxpayers and administrations (OECD 2013).

Enhanced relationship programs have received only little attention in the accounting literature so far. De Simone et al. (2013), based on a significant line of accounting literature using analytical models to research the relationship between taxpayer and tax authority (Graetz et al. 1986; Reinganum and Wilde 1986; Beck and Jung 1989a, 1989b; Beck et al. 1996; Reinganum and Wilde 1988; Sansing 1993), model the interaction between taxpayers and tax administration as a strategic game. They model the behaviours of taxpayer and tax authority inside and outside of an enhanced relationship program and specify conditions under which entering the program is beneficial to both parties. They find that, despite the counterintuitive nature of a cooperative program in the context of an inherently adversarial relationship, the program is mutually beneficial in many cases. The empirical study by Beck and Lisowsky (2014) examines participants in the U.S. CAP program. They find that voluntary participants in this U.S. enhanced relationship program report larger uncertain tax benefits (UTB) on their financial statements prior to entering the program than non-participants and a decrease in the magnitude of reported UTB after entering the program. Both papers focus on either the reporting behaviour of the taxpayer when (not) participating in the enhanced relationship program or on assessing financial

statement effects of voluntary participation in such a program whereas our paper focuses on the development of interpersonal trust, whose establishment is promoted by the various enhanced relationship programs, during a tax audit procedure. While both papers focus mostly on the behaviour of the taxpayer our paper in contrast puts the focus on the tax auditors' perceptions.

Similarly to the accounting literature, the psychological tax literature cited above focuses mostly on the taxpayers' perspective, studies the effect of the taxpayer's trust in the tax authority and highlights the importance of perceived trustworthiness of tax authorities. While the OECD (2008) and the implementation documents of the various enhanced relationship programs regularly point at the importance of mutual trust, the tax auditors' perspective of "mutual trust" has been neglected by prior empirical studies. This is a significant gap in prior accounting research and psychological tax research as the mutuality of the concept "trust" calls for studying both sides of the trust relationship. We therefore focus on the individual relationship between tax auditor and taxpayer but in contrast to the existing literature we study the tax auditor's perspective. With this change of perspective we contribute to the existing accounting literature as we provide insights from the "other side" of the mutual interpersonal trust relationship that is seen critical by the literature for promoting voluntary compliance.

3. Hypothesis development

As prior research indicates the importance of interpersonal trust in a (financial) audit environment this study investigates the antecedents of interpersonal trust against the backdrop of tax audits. In this study we look at behaviours by a taxpayer (or its representative) and on personal attitudes of the tax auditor that have been identified in the trust literature as potentially influencing interpersonal trust. We focus on two auditor dispositional factors, *professional trait scepticism* and *professional identification*, and characteristics of the actual relationship between the auditor and the taxpayer that are influenced by the taxpayer's behaviour ("trust attracting behaviour" see Rennie et al, 2010): *information quality*, *opportunistic behaviour*, *level of conflict*). As prior research has not focused on the interpersonal

relationship between the two parties involved in a tax audit it is rather unclear if and how interpersonal trust relationships evolve between tax auditors and the taxpayer or its representative (table 1 gives an overview of the factors potentially affecting the level of trust).

TABLE 1 about here

Professional Scepticism.

Auditors are obliged to be independent in mind, thus they have to approach the client with professional scepticism. Professional scepticism means that the provision of the auditors' opinion must not be affected by influences that compromise independent judgment (Hurt 2010). Financial auditing research mainly assumes a negative relation between professional scepticism and trust (Shaub 1996; Rose 2007; Kerler and Killough 2009; Quadackers et al. 2014). According to Knechel (2013) auditors who exercise higher levels of professional scepticism are more likely to confront a client or perform additional procedures when high-risk irregularities arise. They are more likely to detect fraud, exhibit high-quality assessments of evidence, are less trusting of a client and more likely to invest in high levels of audit effort. The assumption of this negative relation is also implicit to the familiarity threat hypothesis that expects the behavioural bond between auditor and auditee to replace auditor's necessary professional scepticism (Latham et al. 1998). Thus, a high level of professional scepticism might also forestall a trust relationship within the tax auditing context. Therefore, we set up our first hypotheses as follows:

H1: Professional Scepticism will be negatively associated with tax auditor's trust in the taxpayer's representative.

Professional Identification.

Social identity theory (Tajfel and Turner 1979) implies that individuals self-categorize into several social identities and follow their respective principles. A social identity is the individual's cognitive consensus with a group's norms and values. According to (Shropshire 2010), identity is a powerful mechanism for understanding individuals' behaviour. The social identity leads to a differentiation from those whose social identity is perceived as being different, while supportive behaviour can be expected to those with the same norms and values (Kane 2010). However, social identity theorists have also revealed that the effect on actual behaviour depends on its relevance in the respective setting (Ashforth and Mael 1989; Foreman and Whetten 2002; Golden-Biddle and Rao 1997). In a financial auditing context previous literature has shown that auditors have a high professional identification, higher than their identification with clients (Bamber and Iyer 2007), which leads to a reduced likelihood of acquiescing with the client's preferred position (Bamber and Iyer 2007). In a tax audit context auditors might therefore also be less willing to build up a trust relationship when they have strong mental ties with their audit profession (professional identification). Therefore, we set up our second hypotheses as follows:

H2: Professional Identification will be negatively associated with tax auditor's trust in the taxpayer's representative.

Information Quality

Prior research has shown that the openness of communication or the quality of the shared information respectively (Rennie et al. 2010) is positively associated with interpersonal trust in financial auditing environments. Both openness of communication and high information quality have been identified in the trust literature as potential antecedents to interpersonal trust (see Williams (2001); McAllister (1995)) and have been discussed and empirically tested by Whitener et al. (1998), Krosgaard et al. (2002) and Rennie et al. (2010) in a manager-employee context as well as a financial auditing context. They find that when an auditee shows high levels of openness of communication and provides high information quality the financial auditor feels greater trust towards this individual. Conversely, an

auditee representative who is not able to communicate openly and provide information at a high quality may not generate an improved feeling of trust by the auditor and may even create distrust. Drawing on the findings of financial auditing research allows us to formulate the following hypothesis:

H3: The quality of information shared by the taxpayer's representative with the tax auditor will be positively associated with tax auditor's trust in the taxpayer's representative.

Opportunistic Behaviour

Opportunistic behaviour has been described as the behaviour of a party that endangers a relationship for the purpose of taking advantage of a new opportunity and to seek a short term gain. Opportunistic behaviour may cause a relationship between partners to become unstable (De Ruyter and Wetzels 1999). De Ruyter and Wetzels (1999) show that the less an auditee experiences the relationship with the auditor as enjoyable the more they will be inclined to exhibit opportunistic behaviour. Conversely, the more the auditor exhibits a client-oriented attitude the less the auditee will be inclined to react on the basis of short term advantages and gains. De Ruyter and Wetzels (1999) find that client orientation has a significant negative effect on opportunistic behaviour. Transposing these findings from the financial auditing literature to a tax audit environment allows us to establish the following hypothesis:

H4: Opportunistic behaviour of the taxpayer's representative will be negatively associated with tax auditor's trust in the taxpayer's representative.

Level of Conflict

A further aspect that influences the interpersonal relationship between auditor and auditee is the intensity and frequency of disagreement between the two during the course of an audit (*level of conflict*). The frequency and intensity of disagreements and their negative effects on interpersonal trust relationships have been discussed by Anderson and Narus (1990); Morgan and Hunt (1994) and Rennie et al. (2010). Drawing on their findings we predict that the level of conflict would tend to have a negative relation with the trust that a tax auditor feels for the taxpayer's representative. The more frequently and

intensively the auditor and the taxpayer's representative have disagreements, the lower the auditor's trust of this individual would be. The rationale behind this is that frequent and intense disagreements may be indicative of a taxpayer's representative who tends to push the limits of the tax code or who attempts to influence the audit process. It should also be noted that prior research, yet outside of the auditing context, demonstrates that cooperation between the parties to a relationship is positively associated with interpersonal trust (Anderson and Narus 1990; Morgan and Hunt 1994). We thus hypothesize as follows:

H5: The level of conflict between the taxpayer's representative and the tax auditor will be negatively associated with tax auditor's trust in the taxpayer's representative.

4. Empirical Study

4.1. Institutional Setting

Our study is based among a survey of tax auditors from the *Large Businesses Assessment and Audit Unit* from Austria. In Austria a strict regulatory environment for tax audit and tax auditors exists. First, a relevant university degree for tax auditors of the *Large Businesses Assessment and Audit Unit* is mandatory. They further undergo a rigorous training program and continuing professional education safeguards high expertise. Second, there is an internal review system. A board of around twenty experts constantly peer reviews the audits/auditors and also gives advice in difficult issues. These evaluations of the internal reviewers are also relevant for promotions. Tax auditors are thus highly incentivised to generate high audit quality. Third, a rotation system of the lead auditor after each audit ensures high independence from the auditee. Regarding the audit process itself, tax auditors are assigned to regional teams. They regularly conduct the audit in a group consisting of three auditors. An average duration of an audit is three to six month with around 30 audit days per firm (for large businesses: 50 audit days on average). The selection of the audited taxpayer follows three rationales: one third of auditees is selected by a risk analysis based on irregularities in the tax return, another third is selected by a time (random)

selection, and the last third is selected due to special events and reports. For large businesses a full coverage is intended, meaning that a large business is basically audited every three years covering a period of the previous three years.

It has to be noted that the regulatory environment of a tax audit is different from the regulatory environment of a financial audit. While the financial auditor is appointed and remunerated by the audited company the individual civil servant performing the tax audit is assigned to the taxpayer by the revenue body. There is no application or bidding process preceding the audit and there are no direct economic dependencies between the auditor and the taxpayer. Financial auditors are to some extent economically dependent on the auditee, which leads to different incentives also in regard of the trust relationship. Their aim of keeping the audit mandate for future periods could influence the audit process and the audit's outcome. In contrast, the civil servant performing the tax audit is economically independent from the auditee which regularly prevents any future contingencies to affect the audit process. The absence of any direct economic dependencies between tax auditor and taxpayer diminishes any economic incentives for the tax auditor to build up any sort of goodwill-based trust relationships with the auditee to streamline the audit process. Rather by virtue of their legal obligations and their promotion incentives the civil servants might perform the tax audit without any personal dependencies and incentives contingent on the well-being of the auditee and the auditee's experience and recollections of the audit process.

4.2. Data and Methodology

In this study we followed the traditional test logic based on the ideas of critical rationalism. Our starting point was the research model that emerged from previous literature (e.g. Rennie et al. (2010)). To build up a broad empirical basis for the hypothesis tests, we conducted a questionnaire study surveying 154 tax auditors from the *Large Businesses Assessment and Audit Unit* of the Austrian Ministry of Finance. Even though the tax auditors as civil servants are bound to the highest levels of governmental confidentiality obligations, which are especially strict with respect to secrecy in tax matters, we were granted permission to conduct the survey in 2012 and 2013 during an educational

training. From a total population of 509 tax auditors in Austria, 154 tax auditors participated in our survey. The participation was on a voluntary basis and nearly all participants of the educational training (154 of 155) responded to the survey. Table 2 below provides demographic information on the participants of the study.

TABLE 2 about here

Since the possibility to survey tax auditors is rare, we approached the survey participants with a bundle of research instruments. By guaranteeing full anonymity, the participants were granted maximum freedom to express their opinions. In order to avoid any recall bias to our results, we asked the tax auditors to report their experience with their current tax audit appointment. In case of multiple current audit appointments the participants were instructed to choose the one taxpayer whose initials were first in alphabetic order. Due to confidentiality obligations the name of the specific taxpayer could not be disclosed to us and was not reported on the questionnaire.

The hypotheses were tested by relying on the 154 observations of the auditor auditee relationship. We regressed auditor's professional scepticism, auditor's professional identification, information quality, auditee's opportunistic behaviour, level of conflict and some controls, against the auditor's perception of trust in the auditee's representative. Wherever possible we used (or adapted) measures that had been used in other published research for the operationalisation of the latent construct (Rennie et al. 2010; De Ruyter and Wetzels 1999). Each item of the questionnaire was critically evaluated and pre-tested. In line with previous research, the regressions were estimated using ordinary least squares (OLS).

Auditor's trust

Perceived trustworthiness is the perception that the interaction partner is willing and able to stick to the formal and informal rules of social exchange. It depends on the auditors' perception of their clients'

benevolence, integrity, and ability. Integrity refers to “the trustor’s perception that the trustee adheres to a set of principles that the trustor finds acceptable” (Mayer et al., 1995: 719). Benevolence covers “the extent to which a trustee is believed to want to do good to the trustor, aside from an egocentric profit motive” (Mayer et al., 1995: 718). Ability refers to skills and competencies that are critical for realizing the expected performance: “Ability is that group of skills, competencies, and characteristics that enable a party to have influence within some specific domain” (Mayer et al., 1995: 717). High level of perceived ability makes the auditor confident that the interaction partner will perform as expected. Perceived integrity, perceived benevolence, and perceived ability result in a feeling of *trust* towards an interaction partner. To measure trust, we employ the scales proposed by Mayer and Davis (1999) consisting of the following 9 items: “*My contact person in the audited firm is very successful in his/her job.*”, “*My contact person in the audited firm is competent.*”, “*My contact person in the audited firm understands the accounting standards.*”, “*My contact person in the audited firm has a strong sense of justice.*”, “*I have never had to wonder whether my contact person in the audited firm will stick to his/her word.*”, “*My contact person in the audited firm always tries to be fair.*”, “*Our needs and desires are very important to my contact person in the audited firm.*”, “*My contact person in the audited firm contributes to the audit more than required.*”, “*My contact person in the audited firm would not knowingly act against our interests.*”. The auditors were asked to evaluate the individual items on a seven-point Likert scale ranging from ‘totally disagree’ (1) to ‘totally agree’ (7). The items were factorized in one construct defined *auditor trust*.

Professional Scepticism

Professional scepticism is one of the central concepts in auditing. According to the concept advanced by Hurtt (2010), professional scepticism is an individual’s propensity to defer drawing conclusions until the evidence provides sufficient support for one alternative/explanation over others. It comprises six auditor traits: (i) a questioning mind, (ii) suspension of judgment, (iii) the search for knowledge, (iv) interpersonal understanding, (v) autonomy, and (vi) self-esteem. For the operationalisation of professional scepticism, a condensed version of Hurtt’s (2010) scepticism scale

was used. As the construct is reflective, the scale was condensed to reflect the item for each dimension that showed the highest loadings (Chin 1998). The scale comprises the following items: “*I take my time when making decisions.*”, “*I tend to immediately accept what other people tell me.*”, “*I like to understand the reason for other people's behaviour.*”, “*I think that learning is exciting.*”, “*I have confidence in myself.*”, “*I frequently question things that I see or hear.*”. The auditors were asked to evaluate the individual items on a seven-point Likert scale ranging from ‘totally disagree’ (1) to ‘totally agree’ (7). The items were factorized in one construct defined *professional scepticism*.

Professional Identification

Professional identification means the identification of the auditor with the profession’s norms and values. For the construct professional identification, the scale of Bamber and Iyer (2007) was used. The scale comprises the following items: “*When someone criticizes my profession, it feels like a personal insult.*”, “*When I talk about my profession, I usually say ‘We’ rather than ‘They.’*”, “*I am very interested in what others think about my profession.*”, “*My profession’s successes are my successes.*”, “*When someone praises my profession, it feels like a personal compliment.*”. The auditors were asked to evaluate the individual items on a seven-point Likert scale ranging from ‘totally disagree’ (1) to ‘totally agree’ (7). The items were factorized in one construct defined *professional identification*.

Information Quality

Information quality is a measure of the value the information provides to the auditor. To assess information quality, the scale by Moro et al. (2014) was adopted. The scale comprises the following items: “*The information I get is always accurate.*”, “*I am often provided with information that is irrelevant for the audit.*”, “*I was always provided with full information.*”, “*Only when I request the information I need for the audit, it is provided to me.*”, “*The auditee responds quickly to my inquiries.*”. The auditors were asked to evaluate the individual items on a seven-point Likert scale ranging from ‘totally disagree’ (1) to ‘totally agree’ (7). The items were factorized in one construct defined *information quality*.

Opportunistic Behaviour

Opportunistic behaviour means the attempt to take advantage at the expense of the auditor in order to further own interests. To measure opportunistic behaviour we applied a scale that comprises the following items: “*I experience social pressure during the audit process.*”, “*There is a risk, that the auditee tries to influence the audit through his/her professional and personal network.*”. The auditors were asked to evaluate the individual items on a seven-point Likert scale ranging from ‘totally disagree’ (1) to ‘totally agree’ (7). The items were factorized in one construct defined *opportunistic behaviour*.

Audit conflict

For measuring “*Audit Conflict*” we employ a direct question measured by the reverse coded item “*Problems are discussed and resolved at an early stage*” (Beattie et al. 2000). The auditors were asked to evaluate the individual item on a seven-point Likert scale ranging from ‘totally disagree’ (1) to ‘totally agree’ (7). The reverse coded item was defined as *audit conflict*.

Controls

As control variables we include age of the tax auditor, gender of the tax auditor (dummy variable with “1” being female and “0” being male), and the years of tax audit experience.

4.3. Test of Hypotheses

To test the hypotheses, we employ an OLS regression analysis. We regress the (latent) variables for the tax auditors’ trait characteristics, professional scepticism and professional identification, the auditor’s perception of the auditee behaviour in form of information quality and opportunistic behaviour, the level of conflict, and the control variables that consist of the tax auditors’ demographic characteristics (age, gender and professional experience) against the dependent variable auditor trust. Our model is highly significant ($p = .000$) and has a relatively high explanatory power with $R^2 = .514$. Table 3 below reports the results of the OLS regression.

TABLE 3 about here

With respect to the tax auditors individual characteristics the trait *professional identification* shows a significant positive association with auditor trust ($p = .078$) while *professional scepticism* has no significant influence on the interpersonal trust level ($p = .454$). Since we assumed a negative association for H1 and H2, we have to reject both hypotheses.

The variables for trust attracting behaviours of the taxpayer all show significant relations to the level of interpersonal trust. As hypothesized *information quality* is highly significant ($p = .000$) positively associated and has the strongest influence on auditors' trust. This result confirms H3. *Opportunistic behaviour* and the *level of conflict* are both significantly negatively related with the level of interpersonal trust (opportunistic behaviour: $p = .013$; level of conflict: $p = .096$), which confirms H4 and H5.

The control variables that consist of the tax auditors' demographic characteristics (age, gender and professional experience) are only significant with respect to gender ($p = .081$) providing evidence that female tax auditors are more likely to establish interpersonal trust relationships with the representative of the audited taxpayer. The variables age and professional experience show no significant association with auditor trust.

5. Discussion and Conclusion

Scientific research on tax compliance and taxpayer behaviour assumes that (interpersonal) trust is an important driver for tax compliance. However, the interpersonal relationship between tax auditor and taxpayer established during tax audits has received only little attention so far. In an attempt to shed light on the emergence of tax auditor's trust in the taxpayer (or its representative), we investigate auditor's trait characteristics, auditor's perception of the auditee behaviour, and the level of conflict.

One of the main results of our survey of 154 tax auditors from the *Large Businesses Assessment and Audit Unit* of the Austrian Ministry of Finance shows that tax auditor's dispositional factors have a slightly different impact as previously assumed in the financial auditing literature. While the earlier financial auditing literature (King 2002; Shaub 1996) argued that a professionally sceptical auditor would not build up trust in the auditee, we find that the auditor's professional trait scepticism does not constrain the formation of a trust relationship. Our result is in line with recent findings from empirical financial auditing research that documented also an insignificant relation between trust and professional scepticism (Kerler and Killough 2009) and further coincides with general trust research that has theorized that trust and distrust are not bi-polar opposites but two different dimensions (Lewicki et al. 2006). Second, while we assumed a negative relation between professional identification and trust, our results indicate the opposite. One explanation for this might be that professional identification and trust have a common ground in a maxim and value based behaviour. An auditor with a strong ethical posture might also be highly trustworthy, which leads to a positive relation between professional identification and interpersonal trust.

Furthermore, the results of our study provide evidence for the importance of situational factors on tax auditor's trust. It is shown that not only in a financial audit environment, which is characterized by greater incentives for the auditor to build up a trust relationship with their auditee, but also in a tax audit environment the auditor develops interpersonal trust according to principles that have been already well documented in other fields. Our findings indicate that the better the information quality is and the less the taxpayer (representative) behaves opportunistically, the more trust the auditor perceives in the taxpayer (representative).

As predicted, the level of conflict has a significant negative association with the level of trust that the tax auditor develops towards the taxpayer (representative). The intensity and frequency of disagreement between the two during the course of a tax audit influences the interpersonal trust relationship negatively. The findings are in line with results of previous research of various types of interpersonal relationships. Based on the results we can conclude that the more frequently and

intensively the auditor and the taxpayer's representative have disagreements, the lower is the auditor's trust in their counterpart.

With respect to the tax auditors' individual demographical variables only gender has a significant impact on the level of trust. Our findings indicate that female auditors perceive a higher level of trust than their male colleagues. This finding might be due to the fact that women tend to be more communicative and socially competent and therefore more likely to build up a trust relationship (Breesch and Branson 2009; Chung and Monroe 2001). Another explanation might be that this is a result of a different self-construction between women and men due to social norms (Breesch and Branson 2009; Chung and Monroe 2001). For male auditors it might be less acceptable to show a high level of trust which introduces a gender bias that drives our result with regards to the gender control variable.

The findings of our study have several implications for further research and for practice. For tax research, concepts from other fields have been introduced and empirically tested for the first time. The better understanding of the role of interpersonal relationships in tax audits sheds light on an under researched area of tax research that is highly relevant and provides a valuable starting point for fruitful follow-up research. Future studies in this topical field should concentrate on the identification of further factors that determine the level of trust. Such studies could also put a stronger focus on the personal characteristics of the taxpayers or their representatives. Furthermore, future studies might focus on the (positive) impact that trust exerts within the auditor taxpayer relationship. However our study does not only provide value for tax research, but it might also inform financial audit research and practice. Since the tax audit environment is characterized by environmental factors, such as state control and higher independence that are also demanded for financial audits, the findings that trust also evolves in a tax audit environment under conditions that have been discussed as inhibiting trust, can be expected to enrich also the discussion in financial auditing.

For practice our results show that the development of trust is not prevented by auditors, who are highly sceptical or strongly identify with their profession. Instead a high level of professional identification might even build up the ethical foundation for an auditor to enter in a trust relationship. In

this respect, our findings could alleviate the concern of regulators that they can have only either sceptical auditors or auditors that build up a trust relationship. Since it is assumed by the existing literature that a trust relationship can lead to a more efficient audit procedure our findings emphasize the importance of selecting the right people as tax auditors and as taxpayer representatives: as tax auditors individuals who have a high level of professional scepticism and professional identification, since they are also able to build up trust relationships, while keeping their professional ethics. For taxpayers our results highlight that it is beneficial to communicate openly and to behave correctly in order to build up an interpersonal trust relationship with “their” tax auditor.

As with all research, the limitations of our study must be considered by interpreting our results. A limitation of this study is that we rely on the recall of incidents by participants. This reliance brings with it the risk that the events were recalled inaccurately or in a biased manner. Moreover, the respondents recalled unique incidents which varied in recentness. Counterbalancing this issue is that anchoring recall on a particular incident (*a concrete audit assignment*) enhances recall relative to situations where no anchor is used (Rennie et al. 2010; Levin et al. 2006). A second major type of limitation is that this study examines a limited number of potentially important variables that may affect auditor trust. As a result, this is an exploratory study. We do not mean to suggest that other variables may not be important. Finally, the usual limitations of field studies based on self-reporting and cross sectional data also apply to this study, and so results should be interpreted with this in mind.

Table 1: Factors potentially affecting tax auditor's trust of a taxpayer representative

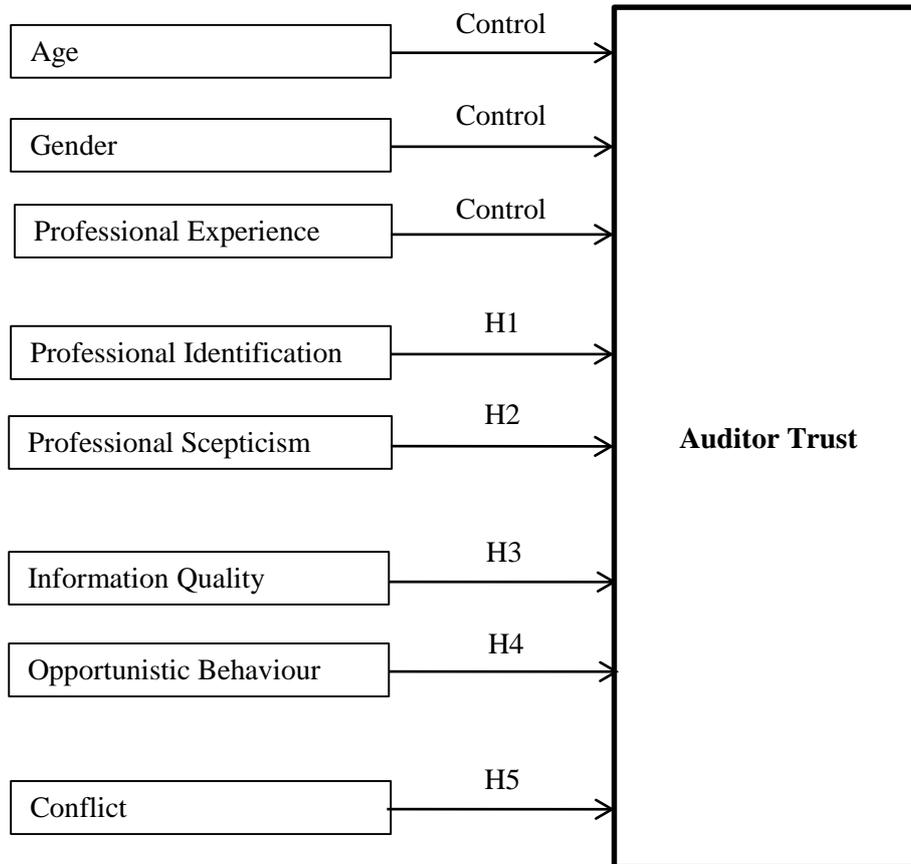


Table 2: Descriptive statistics

		Tax Auditors			
	Description	mean	std.dev.	Min	max
1	Auditor Gender	.316	.466	0	1
2	Auditor Age	44.856	6.119	23	56
3	Professional Experience	18.471	6.845	2	30
4	Trait Professional Scepticism	5.691	.578	4.17	6.83
5	Professional Identification	3.806	1.246	1	6.40
6	Information Quality	4.067	1.398	1.2	6.80
7	Opportunistic Behaviour	2.891	1.560	1	7
8	Audit Conflict	3.042	1.326	1	7
9	Trust	4.030	1.435	1	6.67

Table 3: Regression model, dependent variable: Auditor Trust

		Number of obs	154		
		Sig.	0.000		
		R-squared	0.514		
Variable Description	Coef.	Std. Err.	p	VIF	
Auditor Age	-.010	.014	.475	1.343	
Auditor Gender	.298	.170	.081	1.219	
Professional Experience	.008	.012	.502	1.411	
Professional Scepticism	.099	.132	.454	1.127	
Professional Identification	.106	.059	.078	1.064	
Information Quality	.542	.057	.000	1.225	
Auditee Opportunistic Behaviour	-.128	.051	.013	1.226	
Conflict	-.086	.051	.096	1.130	
_cons	20.750	26.948	.443		

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