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# Linking Ethics and Risk Management in Taxation: Evidence from an Exploratory Study in Ireland and the UK

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ABSTRACT. Ethical dilemmas involving tax issues were identified by members of the American Institute of Certified Public Accountants as posing the most difficult ethical problem for them (Finn et al., *Journal of Business Ethics* **7**(8), pp. 607–609, 1988). The KPMG tax shelter fraud case proves that the tax profession has not gone untainted in the age of numerous accounting and corporate scandals, such as the Enron débâcle (Sikka and Hampton, *Accounting Forum* **29**(3), 325–343, 2005). High-profile scandals serve to highlight the problems caused by differences in ethical judgement among accountants and tax practitioners and the issue of ethics has been brought publicly to the forefront of the profession. Nevertheless, the nature and dimension of ethical issues in tax practice have been largely unexplored (Erard, *Journal of Public Economics* **52**(2), 163–197, 1993; Marshall et al., *Journal of Business Ethics* **17**(12), 1265–1279, 1998; Frecknall Hughes, Unpublished PhD Thesis, The University of Leeds, 2002). This research aims to contribute to the debate on ethics in tax practice by reporting interview data on tax practitioners' perceptions of ethics in the jurisdictions of Ireland and the United Kingdom and exploring the link or equation of ethics with risk management.

KEY WORDS: ethics, perceptions of ethics, risk management, tax practice, tax practitioners

## Introduction

Tax, once the remit of the 'general practitioner' accountant and considered an offshoot of accounting, has grown in complexity and importance and has become a distinct and highly specialised profession in itself. Accounting practices of all sizes often have dedicated tax departments to handle tax compliance and tax planning activities. The combination of self-assessment systems, complex tax codes, increased penalties for non-compliance with tax legislation and higher levels of cross border activity has resulted in an increased reliance on tax practitioners' advice as taxpayers grapple with complying with the tax code in their domestic jurisdiction as well as foreign jurisdictions. The impact on worldwide exchequer revenue of non-compliance with tax legislation is considerable. As significant players in the tax compliance game, tax practitioners are in a position to influence the level of tax that their clients pay through their reporting recommendations, making them worthy of focused research.

The accounting profession in general has undergone severe criticism in the aftermath of numerous accounting scandals and we have witnessed the fall of one of the biggest international accounting practices as a result of the Enron débâcle. The KPMG tax shelter fraud case in particular proves that the tax profession has not gone untainted in the age of accounting and corporate scandals (Sikka and Hampton, 2005). These high profile scandals have served to highlight the problems caused by differences in ethical judgement among accountants and tax practitioners and the issue of ethics has been brought publicly to the forefront of the profession. While many studies in recent years have focused on ethics in accounting, very little work has been done on ethics in tax practice. This is despite the fact that ethical dilemmas involving tax issues were identified by members of the American Institute of Certified Public Accountants as posing the most difficult ethical problem for them (Finn et al., 1988, pp. 607–609). At the core of the ethical debate is the question of how much a person or company is 'obligated' to pay, and what exactly the tax professional should be

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prepared to do or advise to reduce the tax bill. The debate is not over 'to pay or not to pay', but, rather, about the ethical standard to be applied to determine what should be paid. In the context of ethical dilemmas, this could be framed along deontological principles (following an imperative to act inherently ethically) or consequentialist ones (whereby an assessment of overall effects determines an action's ethicality).

Tax practitioners' work within a profession which is highly fragmented. In practice, we find tax advice being given by a broad range of business professionals including accountants, auditors, lawyers, barristers, former and current members of the Irish and UK revenue authorities, tax experts working within industry,[1] as well as those officially designated as Chartered Tax Advisers and Taxation Technicians as a result of their membership of tax dedicated professional bodies. The term 'tax practitioner' attempts to cover this diverse range of individuals. Some work as sole practitioners or in accounting, legal or tax specialist partnerships and will provide various types of tax advice to their clients. Tax experts working in industry are more typically employees of a firm (by which we mean typically a company or group of companies) and will identify with and serve only that company's interests as heads or members of an in-house/internal tax department. Usually companies/groups of companies will be of considerable size before an internal department of this nature is warranted. This fragmentation of the tax profession means that some professionals operating within the profession are subject to government regulation relating to aspects of their work other than tax (external auditors, solicitors and barristers), some are subject to the independent regulation of their own professional institutes (members of the various accountancy and taxation bodies), while others may not be subject to regulation of any sort. Fragmented professional regulation may give rise to ethical dilemmas when tax practitioners comply with differing levels of ethical standards as dictated by a range of professional bodies – or, indeed, none at all. In the UK and Ireland, anyone can set up in business as a tax adviser. It is very much a case of '*caveat emptor*', which further complicates any attempt at establishing a common ethical standard for the profession.

This research aims to contribute to the debate on ethics in tax practice by reporting interview data on tax practitioners' perceptions of ethics in the jurisdictions of Ireland and the United Kingdom and by exploring the process and links by which ethics seems to be increasingly equated with risk management. It is not our aim at this stage to test the moral reasoning processes of tax professionals, as such work would require a very different focus. Here 'tax professionals' are a sample of professionals working principally in advisory firms and in-house tax departments. The increased understanding of how ethics are perceived may facilitate policy makers, professional bodies and educators to respond appropriately in encouraging ethics in tax practice.

The remainder of this article is laid out as follows. Section "Linking ethics and risk management" establishes a link between ethics and risk management; section "Ethics and risk issues in tax: review of the literature" reviews the literature on the factors that make tax practice particularly susceptible to ethical dilemmas and also examines the concept of risk management in a tax practice context; section "Research method and sample selection" describes the research method, while section "Analysis of interview data" sets out the findings from interviews carried out with tax practitioners to examine their perceptions of ethics. Section "Discussion and conclusion" concludes.

## Linking ethics and risk management

The issue of ethics in the area of taxation is complicated. First of all, it is common in this context to find the word used without any definition, and it is frequently used interchangeably with 'morality' without distinction of meaning. 'Ethics' originally as a concept did not inherently carry any overtones of anything good or bad, but simply referred to customs, practices or usages, derived from the Greek word *ἔθος* or *ἦθος*. The Latin word 'mores', from which 'morality' is derived, means much the same thing. It is possible to draw distinctions between ethics and morality:

> 'Morality' suggests a stern set of duties that require us to subordinate our natural desires ... in order to obey the moral law .... Very often, morality is assumed to have a religious basis. These connotations of 'morality' are features of a particular conception of ethics, one linked to the Jewish and Christian traditions, rather

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than an inherent feature of any ethical system. Singer (1994, p. 7)

There is generally some debate over the differentiation of the terms, though academic literature and our interviewees often use them interchangeably. For this article, however, we shall use the terms 'ethics' and 'ethical'. By 'acting ethically' we will mean doing something that, for example, society as a whole or specific groups within would perceive as 'good', and 'acting unethically', the converse.

In the context of taxation, however, 'ethics' is a term most commonly used to mean a set of values or principles which should be of universal application – in other words 'normative ethics', which define what we ought to do or should do. However, taxation is also discussed, debated and reflected upon outside practice in ways that help clarify those values or principles. Thus, what is normative can be subject to development and change, and it depends on the extent to which changes have been successfully implemented as to whether values and principles may also change. One can easily see this by looking at the issue of smoking (following Frecknall Hughes, 2002).

Today, the general opinions about the harmful effects of smoking are well known: it may cause lung or other cancers in the smoker and/or in passive smokers, it pollutes the environment – and so on. There is now an established feeling, that, whatever the pleasure derived from the activity by the smoker, overall the disadvantages outweigh these, such that smoking is not perceived as a 'good' thing, despite the revenues it brings into government coffers from tobacco duty. Opinion has developed such that the legislative ban on smoking in enclosed public places in effect from 29 March 2004 in Ireland and 1 July 2007 in the UK has been accepted without undue resistance. Many institutions, such as hospitals, universities, etc., had non-smoking policies in place many years ahead of the legal ban. Hospitals, as providers of care for smoking-related illness, would be keen to discourage the practice which caused it. One may contrast with this a view of the same subject in the early years of the century. In the following quotation, an advertising scheme is under discussion, whereby the manufacturers of a certain brand of cigarettes are proposing to give vouchers in the packets, which may be collected and used for travel, holidays and other leisure activities.

> '"This scheme should carry a strong appeal to women. 'Give your children that seaside holiday by smoking Whifflets'. That sort of thing. We want to get women down to serious smoking. Too many of them play about with it. Take them off scented stuff and put them on to the straightforward Virginia cigarette … you can smoke a lot more of them in the day without killing yourself."' (This 'killing' was in the context, humorously, of getting nicotine poisoning, which is rare in respect of smoking) Sayers (1933, p. 229)

Here it is portrayed as beneficial to smoke, because of the rewards the vouchers can bring. There is no suggestion that smoking can do any real harm or is in any way unacceptable. In itself it reveals a change of attitude towards women smoking: this was unacceptable in the Victorian era, when women who smoked were regarded as degraded. This is a revealing quotation. It is embedded in a contemporary novel and is indicative of opinion at the time. (One may also deduce much, incidentally, about the ethics of advertisers.)

Arguably, the vast majority of individuals, including – and, perhaps, especially – those running businesses and companies, do not consciously seek to act outside the boundaries of practices established in accordance with widely accepted values and principles. Again, for the majority, such values and principles are those set down in statute. However, at the same time there is a need to cope with changes in values, and as the smoking example shows, a legislative body can take a very long time to amend law to take account of changes. It is arguable that much the same is happening in the area of taxation, given impetus by the clear-cut changes in attitude noted on the advent of the Labour government in the UK in 1997, evidenced in comments made by Peter Wyman, then Head of Tax at Coopers & Lybrand.

> Customs & Excise appears now to use the term 'legitimate avoidance' to distinguish between what they clearly believe to be 'illegitimate' avoidance and 'the legitimate desire to organise affairs in a tax efficient way'. These deliberate attempts to confer an aura of illegality to a legitimate activity are dangerous, and should not be allowed to continue unchallenged. Wyman (1997, p. 3)

This has spread to all aspects of taxation, and is observed as including the former Inland Revenue following the merger of that body with Customs &

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Excise in the UK on 18 April 2005. There has been substantial academic debate (see for example, Freedman, 2004; Simpson, 2004; Tiley, 2004). That debate continues. Reed (2007, p. 4) reports in *Accountancy Age* that:

> [a]dvisers have accused the taxman of acting more aggressively following the merger of the Inland Revenue and Customs.

This represents a sea-change in attitude when compared with that shown in tax case judgements earlier in the twentieth century. The earliest case often cited is the 1929 case of *Ayrshire Pullman Services and D.M. Ritchie v CIR*, and Lord Clyde's comments:

> No man in this country is under the smallest obligation, moral or other, so to arrange his legal relations to his business or to his property so as to enable the Inland Revenue to put the largest possible shovel into his stores. 14 TC 754 at 764

While this has a quite explicit ethical tone to it, it is clear the taxpayer may use whatever legal means are available to him to reduce one's tax liability. This did not really change until the 1960s when Lord Denning, often a controversial judge, commented in 1969 in *Re Weston's Settlements:*

> The avoidance of tax may be lawful, but it is not yet a virtue. [1969] 1 Ch 223 at 225.

Such a comment draws a distinction between lawful activity and virtuous (or ethical) activity in the way that earlier cases do not and is identifiably the beginning of a trend of examination and re-assessment of avoidance which continued with a large number of very high profile cases[2] and which remains a focus of attention, though, as the above comments by Wyman indicate, the angle is different and more deliberate.

There is a difference between tax avoidance so extreme that it stretches the law and its legality has to be decided in Court, and sensible tax planning, such as making sure certain action is taken by a specified date to obtain a relief. Commentators, however, often explicitly state that all avoidance is unethical (see, for example, Christensen and Murphy, 2004; Reed, 2007). The position is not made clearer by the Revenue authorities. Rather than attempting to define tax avoidance, whether 'acceptable' or 'unacceptable', they refer to it using intangible terms.

> … like the elephant, we'll know unacceptable tax planning when we see it: it will depend on degrees of concealment, artificiality, and 'aggressiveness' in the overall context of the intention of the Oireachtas[3] when the tax laws were enacted. O'Grady[4] (2003, p. 2)

While in Ireland and the UK various anti-avoidance measures have been enacted (e.g. s.811, *Taxes Consolidation Act 1997*[5] is the Irish general anti-avoidance provision; s.144, *Finance Act 2000*[6] in the UK on fraudulent income tax evasion) the continuing dominant debate about avoidance creates an environment in which businesses and practitioners are uncertain whether their tax practices will attract attention from the Revenue authorities, and thus, detrimental media coverage and criticism. Consequently they themselves are likely to assess very carefully the potential effect(s) of what they do in all areas related to tax, so that it does not redound to their discredit and create an unwelcome reputation. Such uncertainty and ways of dealing with it lie at the heart of what is now termed 'risk management' (Power, 2004).

Francis and Armstrong (2003, p. 376), consider that

> … managing risk is about the application of policies and procedures to the tasks of identifying, analysing and assessing risks, determining the degree of exposure to risk that organisations can accommodate and taking appropriate steps to avoid litigation, loss of reputation or injury.

In terms of the development of this concept in taxation, it would not be too extreme to suggest that ethical behaviour is not now just a matter of acting in a manner permitted by law, but necessitates building on to that a risk assessment of potential challenge by the Revenue authorities and of adverse judgement by other interested parties and stakeholders. Firms themselves (see later) tend to assess their actions using the rhetoric of risk management. It becomes a question not only of 'Are we acting as we should?', but also of 'Are we acting as we should and is anything going to come back later and bite us on the leg?'. This goes beyond compliance with the law and in extreme cases might result in taxpayers actually not obtaining full tax benefit from application of the law.

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Power (2004) expresses grave concern that this current focus on risk management has resulted in experts who are being made increasingly accountable for what they do, becoming more preoccupied with managing their own risks and defending themselves than concentrating on their expert judgement itself. Secondary risks to reputation are becoming as significant as the primary risks for which experts have knowledge and training. He argues that this trend is resulting in a dangerous flight from judgement and is cultivating an environment of defensiveness. Reputation has emerged as a new management object for private and public sector organisations, resulting in a high degree of anxiety where there is any threat to organisational identity and economic survival.

> … [T]here is an intensification of strategies to avoid blame when things go wrong… The result is a potentially catastrophic downward spiral in which expert judgement shrinks to an empty form of defendable compliance. Power (2004, p. 42)

## Ethics and risk issues in tax: review of the literature

Prior literature (which we review below) supports the contention that tax practitioners operate in an environment characterised by factors that give rise to numerous ethical pressures. Earlier research focuses on the professional tax practitioner, working in a firm of advisers, or on individual taxpayers, but corporate taxpayers are rarely mentioned. However, while ethics has been identified as a significant variable influencing tax practitioners (Milliron, 1988) and some studies have identified the particular ethical issues they face (see in particular Marshall et al., 1998 in Australia and; Yetmar et al., 1998 in the United States), to date very little work has been done to investigate the manner in which tax practitioners perceive ethics on a daily basis. The nature and dimension of ethical issues in tax have been largely unexplored (Erard, 1993; Frecknall Hughes, 2002; Marshall et al., 1998). However, from the limited research that has been done, we can identify some of the factors that make the tax environment particularly problematic from an ethical and, on our reading, a risk management perspective.

### *Ambiguity in the tax law*

Tax legislation must often be applied to complex business or personal transactions. In many cases the legislation does not state in a clear and concise manner specifically how the transaction in question should be dealt with, leaving a range of choices from which to select. Dilemmas may arise when faced with this ambiguity in the legislation (Hume et al., 1999).

### *Multiple stakeholders*

In carrying out their professional duties, tax practitioners have responsibilities towards a number of parties. If they are advisers, these will be their clients, the tax system as represented by the taxing authority, other business advisers, other colleagues within the firm, the professional body with which they are associated and possibly others as well. Firms (companies/groups of companies) owe duty to a range of interested stakeholders, such as shareholders, employees, customers, suppliers, regulatory authorities, including the Government in respect of tax payable, trade unions, etc. Ethical issues may arise because of the perceived need to satisfy simultaneously all of these constituents who may not always have compatible expectations (Yetmar et al., 1998; Yetmar and Eastman, 2000).

> Today's tax practitioner must be an agile tightrope walker, able to balance a host of divergent demands. Maintaining one's equilibrium is indeed difficult as a clamour of voices shout conflicting commands… In light of this obstacle-laden course, contemporary tax practitioners are bound to encounter ethical dilemmas as they attempt to cross this often obscure pathway. (Dox, 1992, p. 71)

### *Pressure*

Extant literature (e.g. Kaplan and Reckers, 1985; Westat, 1980) highlights that taxpayers themselves can often have very unethical attitudes to tax compliance and may be willing to play the 'investigation lottery' by adopting aggressive tax reporting positions in the knowledge that the prospect of an audit by the taxing authority is unlikely. In respect of tax

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advisers, Cruz et al. (2000, p. 223) identify client pressure to adopt overly aggressive reporting positions as one of the most difficult issues facing tax practitioners. Tax advisers must temper the compliance behaviour of their client should the latter stray into territory that is deemed too tax aggressive. It is, however, not always very clear at what point the adviser should insist on less aggressive reporting (Cruz et al., 2000).

*Tax practitioner aggressiveness*

Carnes et al. (1996) define tax aggressiveness in a relative fashion: being more likely than other tax professionals to take pro-taxpayer positions for the same situation. The literature has linked tax aggressiveness with the ethical attitude of the practitioner (Milliron, 1988). It is widely accepted in tax compliance literature that taxpayers' ethical beliefs about tax evasion correlate highly with tax compliance (Carroll, 1987; Etzioni, 1988; Roth et al., 1989; Smith, 1990) and this correlation may also extend to tax practitioners, although it is unclear which variable is the driver. Does tax aggression in a practitioner lead to a lowering of ethical standards or does tax aggression stem from a particular ethical attitude?

*Business managers*

As well as the specific duties involved in the daily work of tax advisers, it is worth remembering that they are also business managers, often with junior staff reporting to them and client portfolios to manage, who are required to deal with the dilemmas involved in managing or working in any business (Yetmar et al., 1998). Lewis (1985), citing a number of studies that have dealt with business ethics, concludes that pressure to compromise personal ethical standards is felt most keenly at the middle and lower management levels.

*Reputational issues*

The various accounting scandals that have dogged the taxation profession in America (e.g. the KPMG tax shelter fraud case in the US[7]) have resulted in media criticism of the profession's ethical profile. The profession needs to cleanse this tarnished reputation by concentrating on improving the ethical behaviour and attitudes of individual members. It is essential in this context that there is a clear understanding of how individual practitioners perceive ethics.

*Competition*

It has long been recognised that competition can cause individuals to ignore ethical considerations (Lewis, 1985). Tax advisers operate in a highly competitive environment where they are constantly striving to attract new clients. This kind of environment may foster a reduction in the level of ethical behaviour as advisers strive to obtain and retain clients. Fisher (1994), finds that tax-related malpractice suits against certified public accountants are the primary cause of legal action against accountants in the United States (see also Bandy, 1996; Schaefer and Zimmer, 1998; Yancey, 1996). He argues that the increased incidence of litigation aimed at tax practitioners may force them to question their role in the context of the ethical standards set by their firm, their profession and themselves (Yetmar and Eastman, 2000). Yetmar et al. (1998), venture as far as to suggest that when competition is strong, practitioners may be tempted to misrepresent their capabilities and take on work where they lack the knowledge or skills to perform their duties.

*Stress*

The sums of money involved in the transactions that tax practitioners advise on are often very significant, bringing additional pressure to bear on the practitioner. This factor, as well as the many already discussed above, and numerous others, combine to make tax practice a stressful profession. Yetmar and Eastman (2000, p. 276) cite the work of Weick (1983), which finds that stress is a major issue in accounting practices. Weick states that *dis*tress (which he defines as an abundance of stress that causes performance to decrease from its peak) in accounting work situations is evidenced by certain suboptimal behaviours. These behaviours include: a reduction in the amount of time given by the accountant to each

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task; the blocking out of new information; the appearance of giving up or only being superficially involved; and a negative or cynical attitude towards clients. Weick suggests that all of these behaviours may lead to decreased ethical behaviour. Yetmar and Eastman (2000) examine these suboptimal behaviours in the context of the tax practitioner. They suggest that the tax practitioner under excess stress may exhibit reduced ethical behaviour by not taking the time to investigate and defend properly an ambiguous tax issue, by arriving at a tax decision and subsequently ignoring compelling evidence that would overturn the original decision, and/or by reducing the care and advocacy shown the client by failing legally to minimise the client's tax liability (Yetmar and Eastman, 2000, p. 276).

Tax practitioners at work in tax departments of companies may find themselves under stress, but for different reasons. They appreciate tax in terms of effect on their own business(es), and pressure might be brought to bear by senior management to reduce tax bills or to devise ways of implementing plans that minimise tax or reduce the organisation's effective rate of tax. They may work independently or in conjunction with external tax advisers. There is no examination in the literature of issues which affect them.

*Public expectation*

As professionals (of whatever category), there is a public expectation that tax practitioners not only have a high degree of technical competence, but also adhere to the very highest ethical standards (Yetmar et al., 1998).

*The privilege of self-regulation*

As members of various professional accountancy and tax bodies, each of which will have their own codes of ethics, tax practitioners are largely afforded the privilege of self-regulation in the UK and Ireland. However, in recent years some regulation has been introduced in the United States (including tax preparer penalties). If it is perceived that the self-governance system is not functioning as it should in the UK, there may be public pressure on policy makers to re-assess the independent status of the accounting and tax professions.

*Risk management*

The environment in which tax professionals operate today is markedly different from even a decade ago. The proliferation of negligence claims against all kinds of business advisers in Ireland and the UK in the recent past, and the associated financial and reputational damage that accompanies these claims, has resulted in a sharp focus on ways in which the threat of litigation against accountants, auditors and tax professionals can be reduced. The plethora of information highways available today means that clients of professional advisers are much more informed as to their legal rights and the remedies available to them should they suffer loss as a result of the actions or omissions of advisers leading to an increasingly litigious culture (Doyle, 2001).

Tax in particular is a complex and difficult area for advisers, involving as it does an abundance of increasingly complex legislation, case law, guidance notes and so on, that change on a regular basis and are often ambiguous. Each time there is a Government Budget, new legislation or a significant judgement in a tax case, new risks of wrongly interpreting tax law arise for a tax adviser (Eckstein, 2004). Tax authorities are more conscious of the existence of abusive tax saving or avoidance strategies and in seeking to increase compliance, are scrutinising tax professionals, contributing to an expansion of risks associated with tax practice (Beasley et al., 2006). While the risk of advising a client incorrectly presents an obvious danger, it is suggested that tax advisers are just as likely to find a claim taken against them for more fundamental errors, e.g. for missing a deadline, failing to implement properly all the steps of a transaction, or not being clear on who exactly may rely on the tax advice given (Eckstein, 2004). Indeed, all of the factors discussed above in the context of making tax practice an environment which presents the tax practitioner with ethical dilemmas, also serve to make tax practice a risky environment in which to work. However, many of these risks can be significantly reduced by the implementation of risk management controls and the adequate supervision of these controls

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(Doyle, 2002). Firms of all sizes are increasingly devoting considerable resources to designing and enhancing policies and procedures that are designed to reduce the risk of claims being taken against them.

In the US, most Certified Public Accountant (CPA) firms are very aware of the importance of managing the risks of financial statement audits in an environment characterised by heightened litigation, but they are now becoming increasingly cognisant of tax engagement[8] risks (Beasley et al., 2006). Yancey (1996, p. 12), observes that while audit failures have been well-publicised in the media and are very costly to settle, tax claims occur more frequently and tax engagements give rise to approximately half of all malpractice claims against CPA firms (see also Bandy, 1996). Schaefer and Zimmer (1998) report that during the 1987 to 1993 period, 48 per cent of the new malpractice claims received by the American Institute of Certified Public Accountants (AICPA) Professional Liability Insurance plan were from tax engagements.

Malpractice suits not only cost enormous amounts of money, but also as a consequence of a lawsuit, a tax practice may also lose clients and suffer severe damage to its reputation. For overall financial and general health reasons, therefore, it is clear that the management of risk should be given high priority in the running of every tax practice (Doyle, 2002). As well as the obvious benefits for the protection of the tax practice from litigation, Graham Ward (former president of the Institute of Chartered Accountants in England and Wales) argues that effective risk management is also in the public interest, leading to clarity in the expectations of clients, closer meeting of those expectations and higher quality advice (Hart, 2000, p. v).

Andrew Scott (Hart, 2000, p. vii), in the preface of a book called 'Risk Management for Accountants', sums up risk management for the accountancy profession, as the delivery of a quality product, provided on a timely basis, at a reasonable cost. Above all, it involves the accountant providing appropriate information or advice. However, he suggests that although quality is fundamental, it is not everything. Risks can arise through taking on the wrong client or the wrong assignment; through responding inappropriately to requests for assistance from people who are not clients; through creating or preserving material that is unnecessary or unhelpful; or by failing to observe basic principles or independence or confidentiality (Hart, 2000, p. vii).

Doyle (2001) echoes this view in the context of tax by describing risk management in tax practice as the careful identification and assessment of risks before committing a firm to provide particular tax services. He suggests that it is a basic principle for any professional adviser to decline assignments to advise on complex issues where the level of specialist expertise is simply not adequate to advise on particular issues. Risk management also involves contracting and organising assignments that are accepted in a way that controls and minimises the associated risks, consistent with rewards and commercial objectives.

Yet despite the focus on risk management in accounting and tax practices, a thorough search for academic literature in the area of risk management in tax practice has yielded very few empirical studies.[9] There is clearly a gap in the academic research into risk management in tax practice and especially on any link between risk management and ethics.

Perhaps one of the interesting issues to emerge in the context of risk management over the past decade has been the rising importance of reputational risk. Damage to reputation emerged as the most frequently cited risk concern by large businesses surveyed in a forthcoming Global Risk Management Survey by Aon. Ruth Joplin, Chicago-based managing director of Aon Global Risk Consulting and project leader of the survey is cited by Hofmann (2007, p. 4) as observing that

> [w]hereas senior management and risk managers have traditionally been concerned with operational and financial risk, they now have to deal with issues as diverse, complex and esoteric as reputation crises, sustainability, labour unrest, pandemics and the impact of new regulation all around the world … [T]hey depend on reputation to a greater degree than organisations may have in the past because there's been a shift in the paradigm of business.

Organisations are ''less reliant on bricks and mortar resources'' than on their ability to grow based on reputation. ''They depend on their reputation more than anything else to secure favour with creditors, people, customers and business partners'' (cited by Hofmann, 2007, p. 4).

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*Summary*

As we have seen, the literature supports the contention that tax practitioners operate in an environment characterised by factors that give rise to numerous ethical pressures and risk. However, while ethics have been identified as a significant variable influencing tax practitioners (Milliron, 1988) and some studies have identified the particular ethical issues they face (see in particular Marshall et al., 1998 in Australia and; Yetmar et al., 1998 in the United States), no work has investigated the perception of ethics among tax practitioners and there appears to be no research into the ethical environment and ethical issues facing practitioners in jurisdictions outside the United States and Australia. The day-to-day working environment experienced by a tax practitioner working in Ireland and the UK may be quite different from that of the American or Australian practitioner. This article endeavours to fill in some of the gaps by investigating the perception of ethics within the tax profession in Ireland and the UK by reporting semi-structured interviews with a number of tax practitioners working in different job contexts. In particular it sets out findings that show the developing link between ethics and risk management, which is new. The research method and findings are discussed in the next sections.

## Research method and sample selection

As this is an exploratory study, we decided that face-to-face interviews with tax professionals would best provide rich and detailed analysis. The research was carried out in Ireland and the UK, as described below. The regulatory frameworks governing the tax professions in the UK and Ireland are comparable and the issues that emerged from the interviews would be relevant in both the UK and Irish contexts.

*Ireland*

Using a cross between purposive and convenience sampling, potential interviewees were identified by prior personal knowledge, professional contact or recommendation. According to Patton (1990, p. 169):

> The logic and power of purposeful sampling lies in selecting information-rich cases for study in depth. Information-rich cases are those from which one can learn a great deal about issues of central importance to the purpose of the research, thus the term purposeful sampling.

Erlandson et al. (1993, pp. 83–84) note that an aspect of purposeful sampling is sample size.

> The basic rule is, 'There are no rules for sample size.' In qualitative research one is looking more for quality than quantity, more for information richness than information volume.

Tax partners were particularly targeted for interview on the basis that their range of experience was likely to yield richer data than tax practitioners at more junior levels, and they were more likely to have encountered ethical dilemmas. It was also important to gather views from tax practitioners working in different contexts so that the views expressed were generalisable to the tax practitioner community at large. Consequently, ten potential interviewees deemed to represent practitioners from a wide range of firm categories, were contacted by e-mail, given information on the broad nature of the research, assured as to the confidentiality of names and firms, and asked if they would contribute their time on a voluntary basis. All ten agreed to be interviewed.

The ten Irish interviewees comprised practitioners from Big 4 firms ($n$ = 4), a middle tier firm ($n$ = 1), a small accounting practice ($n$ = 1), a legal practice ($n$ = 1), a large multinational company ($n$ = 1), a sole practitioner ($n$ = 1) and a director within a relevant professional institute ($n$ = 1). Interviewee title, firm or company profile, region and how they are referred to in this article are set out in Table I.

The personal interview schedule was developed from research questions arising from reviewing the prior literature. Open-ended questions and probes were used to elicit each participant's views. However, the interviews were semi-structured following a predetermined pattern across the topic area of research. All ten interviews were carried out in Dublin and Limerick during November and December 2006 and January 2007 by one of the authors. Most were carried out at the interviewees' place of work with three being conducted more informally in

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TABLE I

Profiles of Irish interviewees[a]

| Title | Firm/company profile | Region | Reference in paper |
|---|---|---|---|
| Tax Partner | Big Four (firm 1) | Dublin | Tax Partner 1 |
| Tax Partner | Big Four (firm 4) | Dublin | Tax Partner 2 |
| Tax Partner | Big Four (firm 4) | Limerick | Tax Partner 3 |
| Risk Management Partner | Big Four (firm 3) | Dublin | Risk Management Partner |
| Tax Partner | Large practice (firm 1) | Limerick | Tax Partner 4 |
| Managing Partner | Small accounting practice | Limerick | Managing Partner |
| Tax Consultant | Sole Practitioner | Dublin | Sole Practitioner 1 |
| Law Partner | Small Solicitors practice | Wexford | Legal Partner |
| Senior Staff Official | Relevant Professional Institute | Dublin | Institute Official |
| Tax Director | Multinational Company | Dublin | Tax Director |

Tax practices are categorised according to size as set out below:
*Big Four*: Tax practices within the accounting firms; PricewaterhouseCoopers, KPMG, Deloitte and Ernst & Young.
*Large*: Tax practice sections of large international accounting firms other than the Big Four.
*Medium*: Tax practices in national accounting firms.
*Small*: Tax practices in large local and regional firms.
*Sole Practitioner*: One tax practitioner operating alone.

social settings. The interviews lasted between 45 and 90 minutes. All participants consented to interviews being tape-recorded and interviews were transcribed verbatim at a later date by the researcher who had conducted the interviews. These procedures are consistent with recommendations in the research methods literature for conducting this type of research (see, for example, Robson, 2002; Saunders et al., 2007).

### The UK

In order to obtain the interview data, a search was carried out on a number of the FTSE top 100 companies, across different industry sectors, to determine appropriate organisations, i.e. those involved in overseas transactions. Again, this was a cross between purposive and convenience sampling. It was felt that interviewing firms with international involvement would provide richer data because of their necessary wider involvement in complex tax issues. As a determinant of international involvement, we examined the most recent financial statements and other information to establish if the organisation owned overseas subsidiary companies, and if so, how many and where they were located. A short list was made of 18 UK-based public limited companies. A letter requesting an interview and briefly outlining the nature of the project was sent to either the named Finance Directors or Company Secretaries of the companies. We asked that our request be forwarded to senior tax personnel if this was more appropriate. This approach to obtain interviews was adopted on the grounds of pragmatism, to establish primarily if there were public limited companies willing to discuss issues likely to be considered very confidential in nature.

Managers from seven companies agreed to interviews, which were undertaken in the period September to December 2004 with one of the authors. We felt that seven organisations were a number sufficient to provide the range of case study data we were seeking. In approaching companies we emphasised that we were aware of the sensitive nature of the topic and gave assurances of anonymity and confidentiality.

An open-ended, semi-structured questionnaire was used for the interviews, covering ethics as well as other areas. Issues for discussion were derived primarily from the literature reviewed above. Interview questionnaires were sent in advance of the interviews to six of the seven interviewees at their request. Interviews were undertaken in the respondents' offices, lasted from 60 to 90 minutes, were tape recorded (with the interviewees' permission) and

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subsequently professionally transcribed verbatim. The transcriptions were sent to the interviewees to ensure that the transcribed version reflected accurately their comments. Some changes to transcriptions were requested and made. These were chiefly for the sake of clarity and to maintain confidentiality.

The characteristics of the interview sample firms are shown in Table II.

In total the number of interviews undertaken was 17. Given the inherently sensitive nature of taxation, which practitioners are often reluctant to discuss, this represents a significant number of interviews.

## Analysis of interview data

The narrative data (audiotapes) were converted into partially processed data (verbatim transcripts, as detailed above) before coding and analysis. The themes of analysis were established *a priori* as a result of the way in which interviews were carried out. The semi-structured nature of the interviews facilitated coding during the analysis stage of the study. The transcripts of the interviews were read and re-read in order to develop a full understanding of the responses. Data were coded using typical content analysis procedures (Lincoln and Guba, 1985; Taylor and Bogdan, 1984). The authors independently coded the interviews. Discrepancies were resolved through consensus among the researchers. Interpretation errors are a potential validity threat (Kirk and Miller, 1986). We have attempted to limit this possible hazard by the use of multiple coders. Although the themes of analysis were established *a priori*, it transpired that many other themes were evident also in the data, which are evidenced below. In what follows, we include extensive quotes from our interviewees *"to allow the reader to hear the interviewees' voices…[and to]…allow the richness of the data to shine through"* (O'Dwyer, 2004, p. 403).

### *The terminology and the place of ethics in tax practice*

As will be clear from some of the quotes set out in this section, there was confusion among interviewees about the role of ethics in tax, if any. Many of the interviewees boldly stated that ethics have no place in tax practice – or, indeed, business, e.g.:

TABLE II

Characteristics of interview respondent firms

| | Firm A | Firm B | Firm C | Firm D | Firm E | Firm F | Firm G |
|---|---|---|---|---|---|---|---|
| Size of tax department | 50 | 7 | 29 | 30 | 50 | 10 | 200 worldwide; 6 in head office |
| Use external tax advisers | Yes | Yes | Yes | Yes | Yes | Yes | Yes |
| International presence | Operates in over 80 countries | Subsidiaries in about 30 countries | Worldwide operations: 40% Europe, 40% US, 20% Asia | Most European countries and the USA | 1000 companies worldwide | The majority of the business is in the US | Operates in 76 countries |

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> I suppose the question that you are asking is to what extent does ethics or morals come into it when you are making a decision and I would say probably not that much to be honest – Tax Partner 2

> To a certain extent there is really no ethics in tax. There is no ethical dimension to taxation. I don't think that many tax people would feel that if I save my clients tax, patients die in hospital or anything like that. I think they don't think in those terms at all. I think they will always resist the view that kind of relationship between the common good and what they do. – Tax Partner 2

> It is not immediately apparent…I'll be perfectly honest with you, that ethics and tax would go hand in hand… – Tax Partner 4

> Most of them [tax decisions] are just, just perhaps one side or the other, of almost of a moral line, and that's not very easy, not very easy at all because is there any such thing as morality in business, should there be any such thing as morality in business and which way do you go? – Firm C

> I think morality in companies is very difficult because companies' directors, employees, have fiduciary duties towards their shareholders, and that's the law, and they have a duty to maximise returns. So on a simple basis, no, there is no morality in business other than to operate within the law. As far as individuals and tax avoidance, that's slightly more difficult because they have no higher fiduciary duty to anybody other than themselves. – Firm C

However, adviser interviewees invariably contradicted this initial view as interviews progressed and they began to speak about specific ethical scenarios.

*The letter of the law*

At the initial stages of all interviews, adviser interviewees were keen to express the distinction between tax planning and tax evasion. They were unanimous in their view that any tax advice given to a client that complies with the letter of the law is considered ethical and that advice breaching any rule of law is considered unethical. There was agreement that individual practitioners may bend the law to varying degrees where the legislation is ambiguous, depending on their personal risk profile and the culture of the firm for which they work. They see the servicing of the client as being the primary duty of a tax practitioner.

> If you follow the law then you shouldn't get into a debate as to whether something is good, bad or indifferent because that is not for you or for your client to judge. All you can advise on is the legal position in terms of your scenarios. – Institute official

> You've got a set of rules here and there are a lot of guys like me that will feel that everything is ok so long as you stay within the rules. – Tax Partner 4

Beyond this basic framework, however, there was initially no clear sense that ethics play any role in tax practice. Firm interviewees also confirmed this.

> It's for the Government to set the tax rates and the policies and the legislation… so you've got a framework to work within it – and I think if you say 'Well, this is the framework but actually there's a morality issue here', I think that just completely muddies the water and nobody knows where they stand – so I don't think you can say that you should act differently to what the legal framework says, because otherwise I don't know where you draw the line. – Firm B

> I think that the general view you would find amongst my peers is that the law's the law and you follow the law, and if the law's unclear you argue about it. – Firm E

> What is law? Surely the law is the codification of what society believes is the moral position on anything, and therefore if you follow the law, then how can you not have followed what the general consensus of moral view is?… And I think if you then start to actually look at what is the moral code you're meant to substitute instead of the law, you end up in a very great dilemma. – Firm F

The clear distinction made by tax practitioners between what is within the parameters of the law, and therefore, ethical, and what is illegal, and therefore, unethical, is somewhat at odds with the Revenue authorities' view, expressed by Michael O'Grady (Irish Revenue Commissioner) as follows:

> … socially responsible attitudes to tax planning should be influenced to a much greater extent by the policy behind the law – assuming that policy is clearly stated

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> or is self-evident – instead of seeing tax law just as something to be tweaked and tailored to clients' interests, regardless of the underlying policy – O'Grady (2003, p. 1)

In fact Mr O'Grady goes so far as to say:

> In our view, 'technical' compliance with tax law, which completely outflanks the policy behind the law, can be just as corrosive as evasion in terms of the overall impact on voluntary compliance. – O'Grady (2003, p. 3)

There is also a sense among practitioners, that utilising the law can have one of two effects. It can become standard practice – 'what everyone does', such that if one does not go to Court, one is out of line with peers or standard practice.

> It's just become routine, it's standard. So you get to the point where now, it's almost like now if we want to litigate on a VAT matter, we don't even bother telling anyone because it's just routine: everyone does it all the time. There are thousands of these cases going through. Every major corporate you can think of, I think, has had a big VAT case, usually more than one … It's sort of like denatured it … And I think the same is true even if we litigated on a pure corporate tax issue: people don't seem to pay much attention to it anymore. – Firm A

> A good case in point would be the Debenhams transaction. If I was a retailer, as far as I know, only one major retailer is outside of that and that's Morrisons who's not done it. Everyone else has done it, and if I was in that industry I would be there too because you couldn't not be. Not because I think it particularly should work: I just think you would be disadvantaging your shareholders if it ended up working. It's a bit like the group litigation orders with the ECJ cases. Do I want to be involved in that? I don't want to have anything to do with any of them, but I have to attach myself to them because if they do go through and if some ridiculous result does come out, then you actually have disadvantaged your shareholders who haven't been involved in them so, yes, we'll get to that extent but we don't tend to push those sorts of things. I'm not interested in breaking any new ECJ law but I do have to join in when the things are going on. – Firm G

Secondly, if use is, perhaps, difficult to understand, but not contentious, then the ground needs to be thoroughly prepared.

> [B]ut there are times when if you think you're allowed to do something within the rules that apply, that you do it and you just try and explain why you've done it – Firm E

*Reputation*

All interviewees considered that their personal reputation with both clients and with the Revenue authorities was vitally important. The two primary reasons for this were the ability to sleep at night knowing that one's conscience was clear (this reason was couched in terms of being comfortable that no issue was going to come back to the practitioner, rather than being happy in the knowledge that one had 'done the right thing') and because having a bad reputation with the Revenue authorities result in them targeting one's clients for Revenue audit. The legal partner in particular stressed that the business was entirely dependent on one's good name.

> When it comes to legal work, there is not even a question of not being 100 per cent ethical because the business we are in is entirely dependent on one's good name. – Legal Partner

Some interviewees expressed the view that when it comes to tax practice, it is the Revenue authorities that are guilty of not behaving in an ethical manner. They are increasingly introducing legislation, which pushes more responsibility for policing the tax system back on tax practitioners (e.g. procedures under 'Whistle Blowing' and Money Laundering legislation). They have been undertaking investigations that have sometimes resulted in undue hardship for innocent parties, without mitigating that hardship (e.g. widows inheriting life policies which had been kept off-shore by their late husbands to avoid Irish tax).[10] Even when taxpayers operate within the strict letter of the law, the Revenue authorities may attack business structures on the basis of the general anti-avoidance legislation contained in s.811 *The Taxes Consolidation Act 1997*[11] in Ireland or under various specific provisions in the UK, or on the basis of prior case law.

> … you'll go in and see the Revenue and say 'Here's a cost that you in Government have told us to incur if

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we want to do this in business but you won't give us a tax deduction for it'. Where is the morality of that? You're prepared to tax, you want to tax profits, but you don't want to tax real profits because you're constructing a tax system that doesn't give you deductions for all the costs that you need to incur to legally realise those profits, so I think the whole issue of morality is…I find very difficult – Firm E

There is also some suggestion that Revenue authorities themselves play an active role in creating scandals which damage reputation. In the UK:

… there's a little bit of a concern that 'naming and shaming' is going to become a tactic… – Firm A

… and it's one of the lines that David Varney is coming up with, the new Chairman of Customs and Revenue, saying things like, 'Is it good business for your name to be all over the front page of the FT or the News of the World for that matter as doing dicey things that might well be within the law but are exploiting child labour in Indonesia, for instance?. Or doing ridiculously artificial schemes that are making use of Bermuda and the Caicos Islands and giving money, keeping it for yourself instead of giving it to the UK government where it clearly belongs.' – Firm C

Interestingly, Marshall et al. (1998) identified the failure to acknowledge a public responsibility to contribute to the improvement of the tax laws and their administration, e.g. reporting blatant tax avoidance arrangements, as one of the ethical issues facing tax practitioners. However, their study found that this item was ranked among the bottom four out of 25 by the tax practitioners themselves.

Other issues in respect of reputation concern the perception of stakeholders about a good name. One Irish interviewee did report withdrawing from a case where a multinational client wished to eliminate its Irish tax liability completely. The client was entirely within the letter of the law but had no commercial rationale for the structure that they wanted implemented, other than to eliminate Irish tax. The interviewee, however, immediately admitted that his reason for withdrawing from the case was to preserve his reputation in the event that the structure was attacked by the Revenue authority as having no commercial basis, rather than for ethical reasons or any sense of responsibility to society at large. This attitude towards reputation appears to reflect a fear of reputational risk rather than a desire to maintain a high ethical standard.

Interviewees in general did not want to be the focus of media interest for being associated with transactions perceived as 'scandalous', as this is damaging to their reputation.

… if this gets written up, what does it look like? – Firm A

I think we, like I suspect most large companies, would prefer not to appear on the front page of the FT or whatever the equivalent is around the world, with 'Nasty multinational thinks up ways to save vast amounts of tax'. – Firm E

However, there is a perception that how and where an issue is reported does make a difference.

Being in the FT for doing planning, well, my personal view is, that's not necessarily so bad because who reads the FT? And people who understand, well, not understand, that's perhaps wrong, people who have a certain view of the role of corporates in the economy, i.e. to deliver returns to shareholder, so it might be that some people reading the FT would be delighted and would say, 'I must invest in that company, it's going to deliver me a better post-tax return than a competitor'. – Firm D

However, there is an acceptance that only certain types of transaction are likely to attract media interest. They have to be transactions that are relatively easily understood and not overly technical.

Someone has interpreted 'this' to be meaning 'that'. It's difficult to write terribly sexy copy out of that sort of stuff. Some of the stuff is just so technical, detailed… basically, that it almost doesn't matter. There could be lots of money attached to it but it's just not something that's going to get the press excited. You do a sort of PAYE saving scheme for one director or something and they can get terribly excited. – Firm A

There is also a cost to preserve reputation which stakeholders must bear.

I think everyone thinks there must be some value in a good reputation. You don't want your name in the newspapers. You want to have a good relationship with your tax authorities because one day you might need a clearance for a real commercial transaction. You might make a mistake and want them to look

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leniently on it. There is benefit but how to quantify it is difficult. – Firm D

*Risk management procedures*

Once adviser interviewees progressed from talking specifically about tax work and focused on client relationship issues, they admitted that thorny problems can sometimes arise in this sphere of the work. However, in addressing client relationship dilemmas, it is risk management principles and procedures that they evoke, rather than considering these problems as ethical dilemmas.

> I don't think that people think about ethics unless they have a specific ethical dilemma, it's not something that would occur to them as a general issue. It is only when they come up against a problem that they would start thinking in ethical terms without even realising that they are. For example if they come up with a tricky client situation they will automatically start thinking, 'what is the risk here? Are there company guidelines about this, best practice guidelines?' Even I am struggling to answer the question as to where ethics comes into tax practice – Institute official

Risk management was identified as crucial by all interviewees, but how risk management interacts with ethics is unclear to them. Some see ethics and risk management as separate concepts and others regard them as amounting to the same thing.

> If I was to talk to a client, I wouldn't use the words – 'ethically you have to pay tax'. I would be putting it to him, the risk he puts himself and his business and his family and his employees, by not being tax compliant. If you start talking to a client about ethics, he thinks you are God and you have a Revenue Commissioners' stamp at the back of your head. Talk to them about risk and you are giving them good advice for which they will thank you. – Managing Partner

Interviewees linked the emergence of very tight risk management procedures in accounting firms with the Enron débâcle, the KPMG tax shelter fraud case, and various other accounting scandals that have emerged in recent years. The introduction of regulations under the *Sarbanes Oxley Act 2002* in the US has had a huge impact on firms with multinational clients and restricted the types of non-audit services that can be offered to these clients. Firms are now subject to rules laid down, not only in domestic law, but also by various regulators (e.g. The Irish Financial Services Regulatory Authority and The Securities and Exchange Commission in the United States) and are influenced by best practice guidelines as laid down by professional institutes. In the aftermath of Enron, most firms have undertaken programmes of self-regulation to reduce the risk of litigation. The bigger firms (Big Four and Large Practices as defined) have partners, and even whole departments, dedicated solely to the issue of risk management. The terminology varies and perhaps accounts for some of the confusion over the link between risk and ethics. One of the Big Four firms has a 'Risk Management and Reputation Department'; another has a dedicated 'Ethics and Values Partner'. Most professional firms of any significant size have their own code of conduct (also known as an ethical code, ethical guidelines, risk management code or referred to by other similar names). Most in-house interviewees also referred to having a risk management or 'brand' committee.[12]

> Ethics in tax practice has become a far more overt topic since Enron and SOX[13] and things like that. We are more inclined to think about it because of Enron but I don't think tax people think of it in terms of ethics. They think of it in terms of aggressive or less aggressive. Risk management also has a lot to do with it actually. – Tax Partner 2

As mentioned above, all interviewees were unanimous in considering risk management as a crucial issue in tax practice and were very comfortable discussing risk procedures for themselves, their firm and their clients. There was no question of not being extremely well versed in risk management principles. Whereas the concept of ethics is nebulous, risk management is tangible and actionable. It is also often considered in terms of the effect on reputation.

> In today's world the most important thing is that you cover your a**e to be perfectly honest. – Tax Partner 4

> I think that my primary responsibility to myself is to make sure I am covered, but what I would do is, I would say 'I will advise you based on what you tell me'… even if there was a suggestion that it was different, if somebody represents something to me and

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shows it to me and I don't 100 per cent know that it isn't the case, then I will feel absolutely ok advising them on that. – Tax Partner 4

We identify what the risks are against the potential rewards and one of the risks is going to be reputational risk, or relationship with the Revenue or whatever, and we do look at them and it is balancing it up. – Firm B

The most important thing to us is the reputational risk on a transaction. If we think it'll damage the reputation of the corporation, we just wouldn't touch it and that's obviously very judgemental, and we do turn down a lot of stuff because it fits into that category…and if it's some artificial tax scam it just doesn't get past go. – Firm G

… we particularly think about 'What happens if we were to do this kind of transaction? How does that affect risks?'… [I]f you are going to be doing things that are, to put it in the extreme, shovelling bits of paper around and getting a tax saving from that. That puts you at a high risk profile – Firm D

There are perceived advantages, however, of implementing stringent internal risk controls and management procedures in terms of treatment by the Revenue authorities.

… it's very easy to view all tax planning on the basis of initiatives, but it is part of the risk management process also, because one of the primary responsibilities of an internal tax department is to manage risk, and basically to give very little surprises to senior management so that they can get on and operate the business, and therefore you've got to be included within the planning operation in order to manage and mitigate the taxes, but also there's part of that risk management function. – Firm F

I know our organisation does not want to be seen to do the aggressive end of the spectrum, and we make a virtue out of that. If you were able to ask the Revenue, I think we would be seen as at the good guy end of the spectrum rather than the bad guy end of the spectrum in terms of complying with the Revenue, in terms of not getting into a lot of these sorts of schemes and that actually pays off because they come and talk to us a lot more and ask us…when they're going to make changes they'll listen to us more than they'll listen to someone who's at the bad guy end of the spectrum…I'm sure we get a lighter touch than some of the others do because we've been properly risk-assessed. That's why the risk assessment is actually quite a good tool for us, because they come in, they look at us, they know what we do and when they risk-assess us they say, 'It's not worth spending a whole load of time on these guys: we'll go after somebody else' – Firm G

These observations highlight the tangible benefits to the firms of implementing stringent risk management processes, perhaps hinting that risk management 'tools' are used for strategic reasons rather than to ensure that the firm operates to a high ethical standard. They also reveal that tax authorities operate on a principle of risk management, if they are 'risk-assessing' or 'risk-profiling' taxpayers as suggested. From a Revenue perspective, this would not be risk management in the sense of internal ethical practice for the Revenue authority as an organisation. It is externally focused and is the risk that taxpayers would be implementing procedures/schemes, etc., such that there would be a risk of tax leakage and Government tax take being reduced. In a sense, risk management from a Revenue authority's perspective is the policing of risk management implemented by taxpayers. This risk-based approach by tax authorities is seen by some as a counterpart to tax practitioner focus on corporate responsibility, and, for the UK at least, a Code of Conduct has been proposed as a basis for compliance by taxpayers, tax practitioners and HMRC, whereby taxpayers would be open, accountable and transparent, Government would "create purposive law backed by a general anti-avoidance principle, and a reporting structure that ensures everything is 'on the record'", and tax practitioners would assist disclosure and "match tax planning to the economic reality of the transactions on which they comment" (Murphy, 2007, p. 15).

*Actual risk management procedures*

All interviewees commented on the vast amounts of resources that are being expended on risk management in terms of money, time and documentation. Risk management procedures vary immensely depending on the size of the firm and the profile of the firm's client base. However, the Big Four and Large Practices have very similar processes. Before clients are taken on, the firm undertakes client acceptance procedures involving background

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checks, conflict tests and risk profiling. The firm must be seen to make a definitive judgement as to whether the entity is suitable to be taken on as a client. The use of client acceptance letters (also known as engagement letters) is routine. Having learnt the lessons from accounting and tax scandals over the past 10 years, practitioners are anxious to ensure that their firm's name is not associated with anything unethical (despite the fact that they are unclear about what this means) and to root out potentially problematic individuals or companies before they are ever accepted as clients. This is seen as a key defence and justification mechanism.

> I would say that if you look at the history, this firm has suffered tribunals where the individual involved did not realise that [information] was not complete but have suffered since then. If there is any doubt at all, we will walk away because we don't want the firm's name associated with anything. Individuals are very clear that they don't want to be associated because long-term, they know that if they do something wrong or something goes wrong, it will come back and haunt, not only the firm, but also the individual. – Risk Management Partner

There is a clearly identified hierarchical system in place for dealing with any ambiguous issues. Staff will typically report to a line manager who in turn reports to the tax partner for the engagement. The tax partner may consult other partners and the Risk Management partner or department, if one exists. Staff may also discuss an issue directly with the risk management partner if they are uncomfortable bringing their concerns to the line manager or the partner responsible for the engagement. It is recognised that with all the risk management procedures that have been introduced, there is less chance of a scenario arising that necessitates a tax practitioner having to make a personal choice in terms of what action to take.

> Trying to understand balance between regulation and ethics so if you follow the rules and as the rules become tighter and tighter and stricter and stricter, that drives activity and the way we work so then consequently, I suppose we work ethically because those rules are designed to apply ethics at a certain level. – Tax Partner 3

While risk management was seen as crucial across the spectrum of interviewees, the extent of the risk management procedures varies depending on the size of the tax practice or range of business activities. Smaller firms and sole practitioners have less onerous procedures as a result of the reduced numbers of personnel involved in dealing with a client, the reduced focus on self-regulation and the profile of their clients as compared with the bigger firms (e.g. indigenous owner managers which may even be exempt from audit versus large multinational companies which may be governed by *Sarbanes Oxley* regulations).

*The impact of a risk management culture*

There was an acceptance among interviewees that having such rigid risk management procedures in place to cover every eventuality may desensitise the ethical antennae of tax practitioners. Risk management kicks in and directs behaviour before an ethical decision is taken.

> I would prefer if people's moral compasses were activated early on because I would much prefer people responding the right way from an intuitive or instinctive reason rather than 'chapter two of the risk management manual tells me I must do the following'. So could we end up with a situation where there are people coming up through the system that are never exposed to the moral dilemma? Yes. Do I worry then that there may be a fall in ethical standards? No, because I think the risk management boundaries are tighter. But do I think it is a good thing? No, because as I say I would prefer practitioners to have an inner intuitive understanding as to what is right and wrong rather than a mechanical regurgitation of a factual situation. – Tax Partner 1

This quotation highlights the need for research into the '*intuitive or instinctive reasoning*' of tax practitioners.

One interviewee made the observation that the risk management procedures have pushed tax practitioners towards acting within very narrowly defined parameters so that they never get as far as having to address ethical dilemmas using their own judgement.

> So if you take it that the morality boundaries are out there but the risk management boundaries have moved in even closer so you never get near the moral

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> boundaries because you hit the risk management boundaries first. – Tax Partner 1

One interviewee pointed out that although risk management is a significant area of professional concern, promotion criteria are still largely profits based (e.g. chargeable hours, fee recovery, securing new work and new clients). Therefore, there is a sense that as long as all the boxes can be successfully ticked to close off the risk management procedures, it is all about profit and that is what is ultimately rewarded.

> … the biggest burden on us now is actually making sure that we have all these pieces of paper to justify our position rather than actually being right. Being right, there's no premium in being right any more, you've got to prove you're right, and that's the big burden on us today. And that's where we're spending a lot of time and effort. – Firm G

### *The role of ethics: beyond risk management*

It was only when the Irish interviewer finally made reference to some specific examples of ethical dilemmas that can arise in the relationship between the client and the practitioner, that interviewees began to look beyond both the tax code and the risk management procedures and agree that ethical dilemmas do present themselves in tax practice on occasion and that acting ethically may not be as simple as merely complying with the law and with the firm's risk management procedures.

> That is where we run into rocky ground and we don't have the comfort of relying on a particular rule or regulation. Very few of the things we do are determined finally by a personal choice. We are so regulated but where it does come down to personal choice, that is, where it is very hard to make a judgement as to what is right and wrong. – Tax Partner 3

> It is not immediately apparent … I'll be perfectly honest with you … But you can always sense that there is, without knowing the definition of it, there is an ethical thing within tax. There has to be. There are a number of circumstances where you come across without sitting down and thinking – ah jeez that involves as much about ethics as anything else. – Tax Partner 4

The apparent confusion as to whether ethics have a role in tax practice leads us to question whether tax practitioners' ethical sensitivity is deficient. According to Rest (1983), an individual may fail to behave ethically if he or she fails to recognise that there is an ethical issue to be resolved in the first instance. In terms of taxation, risk management procedures may actually prevent proper consideration by practitioners of the type of dilemma the procedures are designed to address, in that application of the procedures becomes an automatic part of the day-to-day job. It may be that only when existing procedures fail to detect, or do not extend to, a particular issue that the issue is then perceived as an ethical dilemma. In this sense risk management procedures would stultify ethical appreciation.

## Discussion and conclusion

Interviews carried out with tax practitioners in Ireland and the UK provided a rich source of information about how ethics are perceived in tax practice. There is no prior in-depth study of this, and no prior empirical or theoretical model which might provide any suggestion as to how ethics in this area are operationalised as risk management. This latter is the major contribution which this article makes to the literature. The apparent confusion as to the role of ethics is interesting given that there is such an emphasis being placed on ethics in the larger firms, with the establishment of firm-specific ethical codes of conduct and the creation of roles and even departments the remit of which appears to be centred around ethics and values. One is led to question whether the focus on increasing ethical profile is simply a public relations exercise and an attempt to manage risk to prevent litigation rather than motivated by a genuine will to increase ethical standards among practitioners.

The increased move to integrate risk management procedures into the day-to-day work of tax practitioners emerged as a very significant issue for tax practice. There appears to be a dearth of research into the impact of this relatively new phenomenon and it certainly merits further investigation.

The analyses of interviewees' perceptions of ethics in tax practice, when considered in the context of their views on risk management, leads to the

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conclusion that in most cases risk management seems to have replaced the role of ethics in tax practice. The central tenet of risk management identified by the interviewees was avoidance of expensive litigation and the preservation of their reputations and the reputation of the firm, often in the context of uncertainty as to how transactions would be perceived.

> The reason I stay within the law is because I'll get punished if I don't. Absolutely no question about that. – Tax Partner 4

> I don't want to be associated with this because if this ever does come home to roost, that's my reputation. So in fact, if I am honest, it's more a reputational issue than a moral issue. – Tax Partner 1

> … if your reputation with the regulator is damaged, you get in trouble. – Tax Partner 3

> When I see, sometimes, an Inland Revenue announcement that they've just moved against such and such avoidance scheme, and I've never even heard of the scheme, and you can't help but think, 'Ah well, there's another one that's passed me by'. But on the other hand if it's the sort of thing that the Inland Revenue have decided to outlaw the minute they see it, that's probably the sort of thing I wouldn't want to have been doing in the first place. – Firm C

It is suggested that the existence of tight risk management policies in tax practice may be serving to desensitise the ethical antennae of tax practitioners. The more positive conclusion put forward is that risk management procedures are an attempt by firms to operationalise broad ethical principles. In other words, the underlying theoretical construct is that of ethics, but risk management is its linguistic expression and operational form.

The recognition in the literature that reputational risk has increased in importance was also strongly confirmed in interviews with practitioners. The results are very much in line with Power's (2004) expressed concern about a risk management approach that is heavily focused on organisational processes. He argues that an intensified concern for organisational process may incubate risks of its own, not least the failure to see, imagine or act on the 'bigger picture'. The example he uses of an auditor uncovering a major fraud illustrates this point well. The auditor noticed that a purchase invoice had not been folded, indicating that it had not been in an envelope (and sent by post), and thus, had been fraudulently produced by the auditee company. Audit procedures did not allow for this observation to be taken into account, and had the auditor been concerned solely with official process, he/she would not have seen the purchase invoice in this macro fashion: a vignette for how risk management processes can be risky in circumstances where the is over-reliance on process.

## Notes

[1] Tax experts working in industry may, or course, originate from any of the aforementioned groups, or those mentioned subsequently.

[2] See, notably, Ramsay (WT) Ltd v CIR [1981] 1 All ER 865; Furniss v Dawson [1984] AC 474; Fitzwilliam (Countess) and Others v CIR [1993] 3 All ER 184; and Barclays Mercantile Business Finance Ltd v Mawson HL 2004.

[3] The Oireachtas is the Irish National Parliament.

[4] Michael O'Grady is an Irish Revenue Commissioner

[5] *Taxes Consolidation Act (Ireland) 1997, Number 39 of 1997, Direct Tax Acts, Finance 2007 version, Irish Taxation Institute.*

[6] Great Britain. *Finance Act 2000: Elizabeth II. Chapter 17.* (2000) London: The Stationery Office.

[7] See Sikka and Hampton (2005).

[8] A tax engagement is a contract, either written or oral, to carry out tax work. The work may be the preparation of an annual tax return, which is typically recurrent work, or may relate to a specific non-recurrent project.

[9] See Hackenbrack and Nelson (1996). The authors investigated the impact of engagement risk on how aggressive or conservative auditors were in their reporting recommendations to clients. Kadous and Magro examined client-based risk factors but focused on tax professionals in Kadous and Magro (2001).

[10] This issue was the subject of controversy in Ireland in 2006. The Irish Revenue Commissioners instigated a special investigation into the use of off-shore accounts by Irish taxpayers in order to identify taxpayers who had failed to pay Irish income tax on the interest earned on money deposited off-shore (i.e. outside of Ireland). Many of these accounts were opened by taxpayers on advise from their bank managers, with assurances that it

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was common practice to have an off-shore account in order to avoid tax on deposit interest. The penalties and interest levied on some of the non-compliant taxpayers exceeded the amount of money on deposit off shore. Representations were made to the Irish Revenue Commissioners by the Irish Taxation Institute on behalf of widows who were being subjected to enormous interest and penalties on deposit interest earned on accounts opened off-shore by their late husbands, to ask for the circumstances of the cases to be considered before interest and penalties were levied. The Irish Revenue Commissioners refused to reconsider their original stance, which was to subject all non-compliant taxpayers to the same penalties and interest regardless of the circumstances of the case. This resulted in many hardship cases where the entire life savings of widows (who may not have even known that an off-shore account existed) had to be utilised to discharge the tax liabilities of their late husbands.

[11] *Taxes Consolidation Act (Ireland) 1997, Number 39 of 1997, Direct Tax Acts, Finance 2007 version, Irish Taxation Institute.*

[12] These are not specifically named here as the committee names would identify the respondents' firms.

[13] *The Sarbanes-Oxley Act of 2002*, Pub. L. No. 107–204, 116 Stat. 745 (July 30, 2002), is a United States federal law also known as the *Public Company Accounting Reform and Investor Protection Act of 2002*.

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