THE EFFECTS OF DIFFERENT LETTER STYLES ON REPORTED RENTAL INCOME AND RENTAL DEDUCTIONS: AN EXPERIMENTAL APPROACH

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Abstract

This paper reports on an experimental study, conducted in collaboration with the Australian Taxation Office (Tax Office), investigating the effects of different letter styles on the rental income reported and rental deductions claimed by 6803 taxpayers with rental property. In June 2000, letters were sent out through the Tax Office to a number of rental property owners. The letters varied in tone (either a 'soft' and cooperative tone or a 'hard' and threatening tone was used) and in content (being informed about completing rental information in the tax return correctly, being sent a *Rental Property Schedule* (a schedule) to complete and return, being sent a schedule to complete and return, together with an information booklet, or being sent a schedule that did not have to be returned to the Tax Office). The letters were sent to two samples of taxpayers: those who had been sent a schedule to complete in previous years (touched sample); and those who had not previously been sent a schedule (untouched sample). It was found that being sent a schedule and having to return it to the Tax Office was paramount in reducing the amount of deductions claimed for rental property compared with a control group, for both those previously touched and previously untouched. Further, for those previously touched, a hard tone resulted in fewer rental deduction claims than did a soft tone when the schedule had to be returned. This pattern, however, was reversed when the schedule did not have to be returned. A hard tone resulted in more rental deduction claims than did a soft tone. It is argued that reactance may have been aroused when taxpayers felt illegitimately threatened, producing an increase in rental deductions claimed when they were not under surveillance. A further study (beginning June 2001) will investigate further the relationship between illegitimate threat and deduction claims relating to rental property.

The effects of different letter styles on reported rental income and rental deductions: An experimental approach

Natalie Taylor and Michael Wenzel[1]

Introduction

Australian residents who own rental property must declare in their annual tax return all the rental income they obtain in a financial year from these properties. Similarly, they can claim deductions for expenses legitimately associated with their rental properties. These deductions comprise expenses for advertising for tenants, repairs and maintenance, gardening and lawn mowing, cleaning, pest control, stationery, telephone and postage, and travel, body corporate fees and charges, council rates, depreciation on plant, insurance interest on loans, land tax, legal fees, property agent fees and commissions, special building write-off, water charges, and borrowing and sundry rental expenses.

In 1998 the Australian Taxation Office (Tax Office) identified potential risk characteristics of certain groups of taxpayers whose compliance with the tax laws in terms of rental income could be questionable (for example, they did not have rental income but claimed rental deductions). It then actively targeted these 'high risk' taxpayers the following year. Before the 1999 lodgment period, the Tax Office sent a *Rental Property Schedule* (a schedule) and instructions, as well as a booklet with detailed information on tax issues relating to rental properties, to these 'risk' taxpayers. The schedule comprised a double-sided form to be completed by taxpayers. The front page required taxpayers to provide their tax file number, name, date of birth, address of rental property, date the property first earned rental income, number of weeks the property was rented in the current financial year, and a signed declaration. The second page required specific details about rental income and expenses (as listed above) to be provided. That is, the figure entered for net rent was to be justified explicitly in the schedule (something not required in ordinary tax returns). The schedule, instructions and information booklet were sent to approximately 20,000 rental property owners who lodged a paper tax return. Electronic lodgments were excluded because (a) they automatically involve filling out schedules and hence the effect of completing schedules for those who had done it before would have been lessened and (b) those who had previously

[1] In collaboration with Tony Goddard, Geoff Whyte, Daniel Heavey, Leanne Bleakley, Fiona Zani and Daryll D'Mello of the Australian Taxation Office.

lodged electronically would probably do so again, in which case they would be completing a schedule anyway.

Effects of completing a rental schedule

While having to complete a schedule was found to improve compliance for these ‘risk’ taxpayers, it is unclear (a) whether there is a cheaper and more efficient way to increase compliance and (b) what the effects of the schedules are due to. That is, is it necessary to send out information booklets as well as schedules to taxpayers with rental income, or will receiving schedules with brief instructions, or even receiving only an informal letter, be just as effective in improving compliance? Hence one goal of the present study was to investigate how much, if any, information is necessary to improve compliance in reporting rental income and claiming associated deductions once the Tax Office has initiated contact. If it were found that simply filling in a schedule led to similar or greater levels of compliance than when issued with instructions and booklets, then one possible outcome to improve compliance (at minimal cost to the Tax Office) could be to include rental schedules in *TaxPack*.[2]

Secondly, if the schedules are effective, is it because they raise awareness that the Tax Office has those taxpayers under surveillance (deterrence effect), or because simply filling out the schedules helps taxpayers track their income and expenses? If the effect is due to surveillance, then requiring schedules to be returned to the Tax Office would be necessary to improve compliance. If the effect is due to better record-keeping or more information, then sending out schedules to taxpayers for their own record-keeping, without requiring them to be returned to the Tax Office, should result in increased rental income compliance.

Determining whether surveillance or better record-keeping or knowledge is responsible for the effect of a schedule would benefit the Tax Office. If surveillance is not responsible, this would greatly reduce the costs involved in obtaining greater compliance and would suggest that including the schedule in *TaxPack* would be useful and productive. Hence, a second goal of the present study was to investigate whether the effect of the schedules is due to surveillance or better record-keeping.

[2] *TaxPack* is an annual magazine style booklet of taxation forms and instructions compiled by the Tax Office for the benefit of individual taxpayers. *TaxPack* is posted to taxpayers’ home addresses and distributed through newsagents.

High risk versus low risk groups

While the schedules were found to improve rental income compliance for those classified as high risk, it is unclear what effect they might have on those (a) who are not classified as belonging to a risk group, and (b) 'risk' taxpayers who have previously been required by the Tax Office to complete a schedule (that is, repeated targeting). If the schedules were to be included in *TaxPack* (and hence completed by all rental property owners), it needs to be determined whether the schedules are likely to improve compliance for all types of rental property owner. In the present study, then, samples were drawn from two populations of rental property owners: 'risk' taxpayers who have previously been required to complete and return schedules (referred to in this study as 'previously touched'); and non-risk taxpayers who have not been required to complete schedules before (referred to in this study as 'previously untouched').

Taking a hard or soft approach

Traditionally, the belief that paying tax is not popular (and that taxpayers are self-interested and need monitoring) has encouraged the use of a 'hard line' approach. The need for such an approach becomes stronger with taxpayers who are classified as 'high risk' or are in other ways resistant to paying or declaring the correct amount of taxes. The assumption is that taking a hard approach will improve tax compliance through fear of audit or sanction. While research supports the view that deterrence measures can affect tax behaviour (for example, Allingham & Sandmo, 1972), other research suggests that the effects of threat/audit/sanction can sometimes be counterproductive (for example, Blumenthal, Christian & Slemrod, 1998; Schwartz & Orleans, 1967). Indeed, research into reactance (Brehm & Brehm, 1981) has shown that the use of threat and coercion, particularly when perceived as illegitimate, can produce the opposite behaviour from that advocated. The present study attempted to investigate this by sending rental property owners a letter with either a 'soft' (cooperative, informative) or a 'hard' (emphasising threat/sanctions) tone. This allowed the opportunity to explore how each strategy might affect the different groups of taxpayers.

Method

Participants

Nine thousand taxpayers who were recorded as owning rental property were randomly selected by the Tax Office for the study. All taxpayers included in the study lodged paper (rather than electronic) tax returns. While the majority of those who lodged their returns were self-preparers, some tax agent returns were also included.[3] Samples were drawn randomly from two distinct populations of rental property owners: those previously untouched by the Tax Office and those previously touched by the Tax Office. Those who were defined as 'previously untouched' had not previously been sent schedules to complete. Those who were defined as 'previously touched' had been sent schedules to complete and return to the Tax Office in previous years and, on the basis that the Tax Office had sent out schedules only to taxpayers with certain risk characteristics, those taxpayers in the previously touched population belonged to a 'risk' group. These risk groups comprised any of the following: taxpayers who claimed rental deductions and

1. Those whose gross rental income was $0.
2. Those whose gross rental income was more than $35,000.
3. Those whose net rental income was less than $8000 and whose taxable income was more than $5400.
4. Those whose gross rental income was between $5000 and $35,000, and whose taxable income was more than $20,700.

For the untouched sample, participants were between 17 and 71 years of age (median age of 48), with 48% female and 52% male. For the touched sample, participants were between 22 and 71 years of age (median age of 49), with 39% female and 61% male.

Design

Five hundred taxpayers from each of the touched and untouched samples were randomly allocated to eight experimental conditions which comprised a mixture of tone of letter (soft or hard) and letter content (information only, schedule only, schedule and booklet, no return

[3] Only paper returns lodged by agents were included. The data consisted of 942 returns lodged by agents for the touched sample, and 1200 for the untouched sample.

of schedule). The letters for the eight experimental conditions are provided in the appendix. The experimental conditions comprised the following:

1. information only with soft tone
2. information only with hard tone
3. schedule only with soft tone
4. schedule only with hard tone
5. schedule and booklet with soft tone
6. schedule and booklet with hard tone
7. no return of schedule with soft tone
8. no return of schedule with hard tone.

Those allocated to the untouched and touched control groups received no letter or intervention of any kind. This yielded 18 conditions in total.

Independent variables

Tone of letters. The ‘soft’ letters began with the sentence ‘At the Australian Taxation Office (ATO) we are committed to helping taxpayers to correctly prepare their income tax returns’. The emphasis in these letters was on the role of the Tax Office as being informative and helpful. There was no mention of penalties or audit action. The ‘hard’ letters began with ‘Over the past few years the Australian Taxation Office (ATO) has conducted an extensive review program which has enabled us to collect and analyse rental property income and deductions data. The program has resulted in a substantial number of adjustments to rental property claims.’ These letters emphasised that taxpayers could be selected for audit action, and that penalties for non-compliance could be imposed.

Letter content. The ‘information only’ condition consisted of bringing to the attention of taxpayers the need to complete their tax returns correctly in relation to rental property, and how to obtain further information about tax requirements concerning rental property. No schedule was included within this condition. The ‘schedule only’ condition consisted of brief instructions within the letter on how to complete the enclosed schedule and when and where to return them. The ‘schedule and booklet’ condition consisted of a schedule plus a booklet of instructions on how to complete it, as well as a booklet detailing tax issues related to rental property. The letter advised when and where to return the schedule. The ‘no return of schedule' condition consisted of brief instructions contained within the letter on how to complete the enclosed schedule (the schedule sent in this condition did not ask for personal details to be completed, only rental income and deduction information relating to each property). However, it was emphasised that the schedule was for the benefit of the taxpayer, that it should be kept with their taxation records, and that it was *not* to be returned to the Tax Office.

Procedure

The letters and schedules were mailed out to taxpayers by the Tax Office in June 2000, just before the end of the 1999–2000 financial year. For the conditions where schedules were required to be returned to the Tax Office, the letters specified that the schedules were to be returned at the same time as tax returns (however, the schedules and tax returns were to be returned to different addresses). At the top of each letter was an identifier number to indicate which condition the letter belonged to.

Monitoring phone calls (reverse work flow)

Each letter specified a phone number for taxpayers to ring if they had any queries or concerns. This number was a dedicated number for phone calls relating specifically to the letters. As an indicator of the potential workflow stemming from the letters, incoming phone calls from taxpayers receiving the letters were recorded against their respective letter condition. For each phone call the Tax Office employee taking the call was required to indicate, on a proforma sheet of paper, the letter condition and the main concern raised by the caller. The Tax Office employee was also required to indicate whether the following issues were raised by the caller and, if so, to circle on a scale from 1 (very satisfied) to 7 (very dissatisfied) the satisfaction of the caller in relation to the issue. The categories of issues listed were: the style/tone of the letter, complexity of the letter, whether justification was requested for the letter, problems with schedule, instructions, help/confusion due to schedule, threat or fear of audit, feelings of insult, selection (why me?), costs of the letter, general criticism or praise, tax technical issues, or other (please specify). Ratings of the overall tone of the call were also given as to how aggressive, indignant, polite and grateful the caller was (on a scale from 1 = not at all to 7 = very much).

Data extraction and de-identification

In January 2001 (approximately two months after the official deadline for lodging individual tax returns) the Tax Office provided the authors with de-identified anonymous data on the following variables for each taxpayer included in the sample: age, sex, lodgment week in 1999 and in 2000, whether a schedule had been lodged, whether a tax return for 2000 had been lodged, letter condition for each taxpayer, total income for 2000 and 1999 (excluding net rent), total deductions for 2000 and 1999 (excluding rental deductions), gross rental income for 2000 and 1999, net rent for 2000 and 1999, and rental deductions claimed in 2000 and 1999. At the time of accessing and analysing the data, 1435 taxpayers had not lodged a tax return.[4]

Data screening

Of the 9000 taxpayers randomly selected by the Tax Office, 2197 were excluded from analysis on the following grounds:

- Those who reported that net rental income = \$0 and total rental deductions = \$0 were excluded on the basis that they did not have rental income for 1999–2000 and should not be included in the analysis (n = 719).
- 1435 did not lodge a tax return and hence did not yield rental and/or correlational data. Those who did not lodge a tax return were evenly spread across the four experimental letter conditions and control conditions, $\chi^2(4) = 4.210$, $\underline{p} < .38$, ns. This indicated that non-lodgment was not associated with one type of condition, and ensured that excluding these cases from analysis (n = 1435) would not bias the results.
- Due to the huge variability in gross rental income reported (minimum = \$0, maximum = \$296,057) and the heavily positively skewed distribution (mean = \$10,033, median = \$7318, mode = \$7800), a square root transformation was applied to try and normalise the distribution. Those cases with square root transformed gross rental income greater than 5 standard deviations from the mean were excluded from analysis on the basis that they were outliers and potentially too influential on the distribution (n = 20). This changed the distribution (maximum = \$90,080, mean = \$9610, median = \$7280, mode = \$7000).

[4] It is possible that those who had not lodged an individual tax return by this time had switched to having their return prepared by a tax agent. Returns lodged by tax agents can be lodged as late as May of the following year.

- Due to the huge variability in total income reported (minimum = –\$57,799, maximum = \$1,230,785) and the heavily positively skewed distribution (mean = \$47,248, median = \$39,497, mode = \$0), a square root transformation was applied to try and normalise the distribution. Those cases with a square root total income greater than 5 standard deviations from the mean were excluded from the analysis on the basis that they were outliers and potentially too influential on the distribution (n = 23). This changed the distribution (maximum = \$343,086, mean = \$45,257, median = \$39,369, mode = \$0).

After these criteria were applied to the data, there were 6803 cases available for analysis.

Results

Taxpayer phone calls to the Tax Office

A total of 119 phone calls were received (3% of all those who received a letter). The frequency of calls as a function of letter condition is given in Table 1. It can be seen that the majority of incoming calls were from taxpayers who received a schedule only to be returned (57%), followed by those taxpayers who received both a schedule and booklet (28%). Only 6% of all phone calls were from those in the information only condition, while only 9% of all phone calls were from those in the no return of schedule condition. Hence the vast majority of calls were from taxpayers who were required to return a schedule, and the number of calls in the schedule only condition was twice that in the schedule and booklet condition, $\chi^2(1) = 12.13$, $p < .001$, indicating that the booklet did provide some extra information not available to those in the schedule only condition.

Table 1: Frequency of phone calls as a function of letter type

Letter type	Frequency	Percentage
Soft information only (n = 752)	3	2.5
Soft schedule only (n = 782)	31	26.1
Soft schedule and booklet (n = 744)	13	10.9
Soft no return of schedule (n = 734)	4	3.4
Hard information only (n = 771)	4	3.4
Hard schedule only (n = 734)	37	31.1
Hard schedule and booklet (n = 753)	20	16.8
Hard no return of schedule (n = 770)	7	5.9

Note: A total of 119 phone calls were received.

This is further supported by the finding (see Table 2) that requests for extra information dominated the reasons for phone calls and were located primarily in the schedule only condition.

Table 2: Frequency of issues raised as a function of letter condition

Issue raised	Information only	Schedule only	Schedule and booklet	No return of schedule
Sent schedules in previous years – why again?	0	14	6	2
Property sold	2	21	5	4
Am I a suspect?	3	2	0	0
Extra information required	2	20	10	5
Angry at being sent letter	0	2	1	0
Letter was hostile	0	0	1	0
Submitting electronically	0	2	1	0
Requesting more schedules	0	4	3	0
Miscellaneous	0	2	6	0

Note: A total of 119 phone calls were received.

It can be seen that hostile reactions were very infrequent and that the average tone of the phone calls was not aggressive (M = 1.71, SD = 1.53), not indignant (M = 1.88, SD = 1.70), reasonably polite (M = 6.19, SD = 1.52) and reasonably grateful (M = 5.32, SD = 1.77). Due to the small number of total phone calls received (n = 119) and the differing number of phone calls per condition, it was not possible to investigate reliably whether reactions differed according to condition.

Normality of distribution of variables

All variables (both dependent and covariate) to be included in the analyses were assessed for normality of distribution. Gross rental income 2000, gross rental income 1999, total rental deductions 2000, total rental deductions 1999 and income 2000 (excluding net rent) were all positively skewed. A square root transformation was applied to these variables, resulting in much better distributions. Net rent 2000 and net rent 1999 were reasonably distributed and remained in raw form. While transformed variables can improve the statistical qualities of data analysis (indeed, it is for this reason that transformations are applied), results in terms of dependent variables can be difficult to interpret. This is particularly so if one wishes to frame the results in terms of dollar savings, as is the case here. In the present results, then, all statistical analyses will use the transformed variable, while tables and figures (for purposes of illustration) will refer to dollars based on raw data unless the transformed variable produces a different pattern of results. Covariates in all analyses will use the transformed variable.

Touched versus untouched samples

Rather than include the two types of taxpayer as a separate independent variable, separate analyses were conducted on all dependent variables for those previously untouched and those previously touched. This was because the touched sample comprised a combination of high risk groups who had been sent a schedule to complete before. In fact, some of those in this sample were receiving a schedule for the third time. The variation in selection criteria for the high risk groups meant that the variance in the touched sample was particularly high. Further, average gross rental income ($5968 vs. $12,879), rental deductions ($6240 vs. $12,206) and net rent (–$254 vs. $686) were substantially lower for the untouched group than they were for the touched group.

Effects of letter content and soft or hard tone

The three main dependent variables being investigated were gross rental income, rental deductions and net rent reported in 2000. To investigate the effects of letter content and tone on each of these outcome measures, separate analyses of covariance were conducted for both the untouched and touched samples, controlling for age, sex, lodgment week, income 2000 and whether a schedule had been lodged. The latter was included as a covariate because, although two of the conditions (and the control condition) did not require a schedule to be returned, 14% (269) of those in the information only condition, 14% (265) of those in the no return of schedule condition, and 14% (126) of those in the control condition lodged schedules.[5] Hence it was necessary to take into account whether a schedule had been lodged in case this differentially affected results. Rental income declared and rental deductions claimed in the previous year were also used as covariates for each respective analysis.

Gross rental income

Untouched sample

A 4 (type of letter: information only, schedule only, schedule and booklet, no return of schedule) x 2 (tone: soft or hard) ANCOVA with gross rental income 2000 (transformed) as the dependent variable revealed age, lodgment week, total income, gross rental income declared in 1999 and rental deductions in 2000 to be significant covariates (see Table 3, left-hand side). Younger taxpayers tended to report less gross rental income than did older taxpayers, those who lodged their return earlier rather than later in the year declared less rental income, those with higher incomes declared less gross rental income than those with lower incomes, those with higher gross rental income in 1999 had higher gross rental income in 2000, and higher rental deductions in 2000 were associated with higher gross rental income. Further, the amount of gross rental income declared did not depend on whether a schedule had been lodged, $F\ (1, 2860) = 1.66$, $p = .20$, and was not affected by letter condition, $F(3, 2860) < 1$, ns, tone of letter, $F(1, 2860) = 1.52$, $p = .22$, or their interaction, $F(3, 2860) < 1$, ns, (see Table 3, left-hand side).

[5] Although taxpayers were selected in the sample on the basis they had lodged a paper return in 1999, a number of taxpayers chose to lodge their returns electronically. Returns lodged electronically required a schedule to be completed. It was determined that 125 taxpayers in the control conditions lodged electronically, and 253 taxpayers in the information only conditions lodged electronically. It is expected that those who returned a schedule in the no return condition would have comprised a mixture of those who lodged electronically and those who returned their schedules even though they were not required to.

Table 3: Analyses of covariance (ANCOVA) on gross rental income 2000 (transformed variable) for untouched and touched samples

	Untouched sample			Touched sample		
Source	**df**	**F**	**p**	**df**	**F**	**p**
Covariates						
Age	1	29.69	.000	1	56.51	.000
Sex	1	1.32	.251	1	4.07	.044
Lodgment week 2000	1	17.00	.000	1	5.84	.016
Income 2000	1	59.93	.000	1	30.13	.000
Schedule lodged?	1	1.66	.198	1	0.22	.642
Gross rent 1999	1	1526.71	.000	1	4555.54	.000
Rental deductions 2000	1	2045.28	.000	1	919.68	.000
Tone (soft or hard)	1	1.52	.219	1	0.94	.331
Letter type	3	.29	.835	3	0.14	.938
Tone x letter type	3	.16	.922	3	0.90	.439
Error	2860			3150		

Touched sample

A 4 (type of letter: information only, schedule only, schedule and booklet, no return of schedule) x 2 (tone: soft or hard) ANCOVA with gross rental income 2000 (transformed) as the dependent variable revealed precisely the same pattern as for the untouched sample. Again, age, lodgment week, total income, gross rental income declared in 1999 and rental deductions in 2000 were significant covariates (in the same directions as for the untouched sample), while the effects of letter condition, tone of letter and the interaction between the two were insignificant, Fs < 1, (see Table 3, right-hand side).

Rental deductions

Untouched sample

Given the emphasis in the schedules on itemising deductions, it would make sense if the effect of the schedules occurred in relation to deductions, that is, deductions claimed should differ between taxpayers who received a schedule and those who did not. A 4 (type of letter: information only, schedule only, schedule and booklet, no return of schedule) x 2 (tone: soft or hard) ANCOVA with total rental deductions claimed (transformed) as the dependent variable revealed age, lodgment week, total income, total rental deductions claimed in 1999 and gross rental income in 2000 to be significant covariates (see Table 4, left-hand side).

Table 4: Analyses of covariance (ANCOVA) on rental deductions 2000 (transformed variable) for untouched and touched samples

	Untouched sample			**Touched sample**		
<u>Source</u>	**df**	**F**	**p**	**df**	**F**	**p**
Covariates						
Age	1	154.16	.000	1	86.50	.000
Sex	1	0.17	.684	1	1.08	.300
Lodgment week 2000	1	33.05	.000	1	25.28	.000
Income 2000	1	109.02	.000	1	58.32	.000
Schedule lodged	1	6.32	.012	1	12.84	.000
Gross rent 2000	1	1377.39	.000	1	857.69	.000
Rental deductions 1999	1	2222.83	.000	1	4838.76	.000
Tone	1	0.59	.442	1	1.85	.174
Letter	3	4.81	.002	3	4.11	.006
Tone x letter	3	0.53	.664	3	2.05	.105
Error	2860			3150		

Again, younger taxpayers claimed more rental deductions than older taxpayers, later lodgers claimed less rental deductions than earlier lodgers, higher income earners claimed more rental deductions than lower income earners, the higher the rental deductions claimed in 1999 the higher the rental deductions claimed in 2000, and those with higher gross rental income claimed more rental deductions than those with lower gross rental income. Further, a main effect for letter type was found, F (3, 2860) = 4.81, p=.002. Pairwise comparisons, taking covariates into account, revealed the schedule only condition (M transformed = 68.13, M raw data = $5781) to yield significantly less rental deductions than the information only condition (M transformed = 71.63, M raw data = $6551), p = .005, and the no return of schedule condition (M transformed = 71.65, M raw data = $6550), p = .004. The schedule and booklet condition (M transformed = 70.04, M raw data = $6167) did not differ from the other conditions. There was no effect for tone and no interaction.

Touched sample

The pattern of results for the touched sample was very similar to that of the untouched sample. A 4 (type of letter: information only, schedule only, schedule and booklet, no return of schedule) x 2 (tone: soft or hard) ANCOVA with total rental deductions claimed (transformed) as the dependent variable revealed age, lodgment week, lodgment of schedule, total income, total rental deductions claimed in 1999 and gross rental income 2000 to be significant covariates, in the same directions as in the previous analysis (see Table 4, right-hand side). A main effect for letter type was found, F (3, 3150) = 4.11, p = .006. Again, pairwise comparisons revealed the schedule only condition (M transformed = 97.60, M raw data = $11,536) to yield significantly less rental deductions than the information only condition (M transformed = 101.08, M raw data = $12,365), p = .012, and the no return of schedule condition (M transformed = 101.29, M raw data = $12,519), p = .007. The schedule and booklet condition (M transformed = 99.00, M raw data = $11,907) did not differ from the other conditions. Again, there was no effect for tone and no interaction between tone and letter type.

Given that tone did not appear to affect gross rental income declared or rental deductions claimed, tone was dropped as a separate factor from the following analyses. Letter type was collapsed across tone to allow comparison between the experimental letter conditions and the control conditions for each of gross rental income, rental deductions and net rent.

Effectiveness of letters

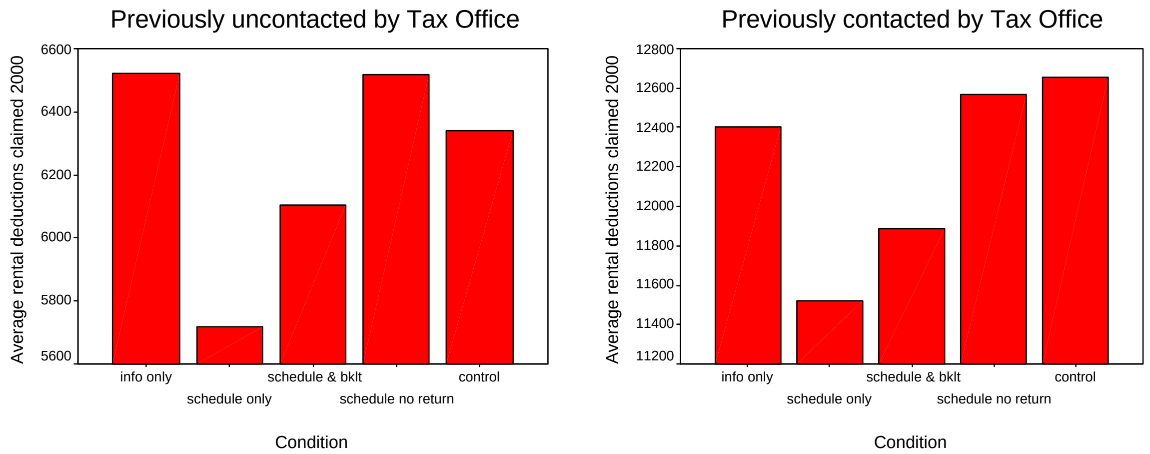
Differences between experimental and control conditions

While it was shown above that gross rental income did not differ between the experimental conditions, it remains to be seen whether any of the experimental conditions differed from the control conditions. To determine whether *gross rental income 2000* (transformed) differed between experimental and control conditions, a one-way ANCOVA, controlling for the relevant covariates (as above), was conducted for both the untouched and touched samples. No differences were found in gross rental income declared between any of the experimental and control conditions for either the untouched sample, $\underline{F}$ (4, 3221) = 1.64, $\underline{p}$ = .162, or the touched sample, $\underline{F}$ (4, 3558) < 1, ns. Clearly, reported gross rental income was not affected by the experimental manipulations. Table 5 details the average gross rental income reported as a function of condition for both the untouched and touched samples.

Table 5: Average gross rental income declared in 2000 ($) and average rental deductions claimed in 2000 ($) after controlling for covariates, as a function of condition

	Information only	**Schedule only**	**Schedule and booklet**	**No return of schedule**	**Control**
Untouched	**n = 710**	**n = 719**	**n = 732**	**n = 714**	**n = 358**
Average gross rent 2000 (with covariates)	6208	5919	5957	6054	5700
Average rental deductions 2000 (with covariates)	6523	5718	6103	6517	6340
Touched	**n = 813**	**n = 797**	**n = 765**	**n = 790**	**n = 405**
Average gross rent 2000 (with covariates)	12,907	12,868	12,962	12,911	12,745
Average rental deductions 2000 (with covariates)	12,404	11,518	11,887	12,564	12,658

As *rental deductions 2000* were found to differ between letter type conditions, simple comparisons were conducted between experimental and control conditions to ascertain if significant differences existed. Average rental deductions claimed in 2000 (raw data), after controlling for relevant covariates, are shown in Figure 1a for the untouched sample and in Figure 1b for the touched sample.



(a) (b)

Figure 1: Mean rental deductions claimed in 2000 ($) by (a) those previously uncontacted and (b) those previously contacted by the Tax Office as a function of condition, after controlling for age, sex, whether a rental schedule had been lodged, lodgment week, 2000 total income, rental deductions claimed in 1999 and gross rental income 2000.

It can be seen that the patterns for both samples are very similar – only the general level of rental deductions claimed was different (that is, higher levels of deductions for the touched sample). Simple comparisons (controlling for covariates) revealed the schedule only condition (M = $5781) to be the only experimental condition that differed significantly from the control condition (M = $6340), p = .011 for the untouched sample. On average, the schedule only condition reduced rental deduction claims by approximately $622 per person. For the touched sample, both the schedule only condition (M = $11,518) and the schedule and booklet condition (M = $11,887) differed significantly from the control condition (M = $12,658), ps = .001 and .031 respectively. On average, the schedule only condition reduced rental deduction claims by approximately $1139 per person while the schedule and booklet condition reduced rental deduction claims by approximately $770 per person. Table 5 details the average rental deductions claimed as a function of condition for both the untouched and touched samples. It would appear that receiving and having to return a schedule to the Tax Office was paramount in reducing the amount of rental deductions claimed.

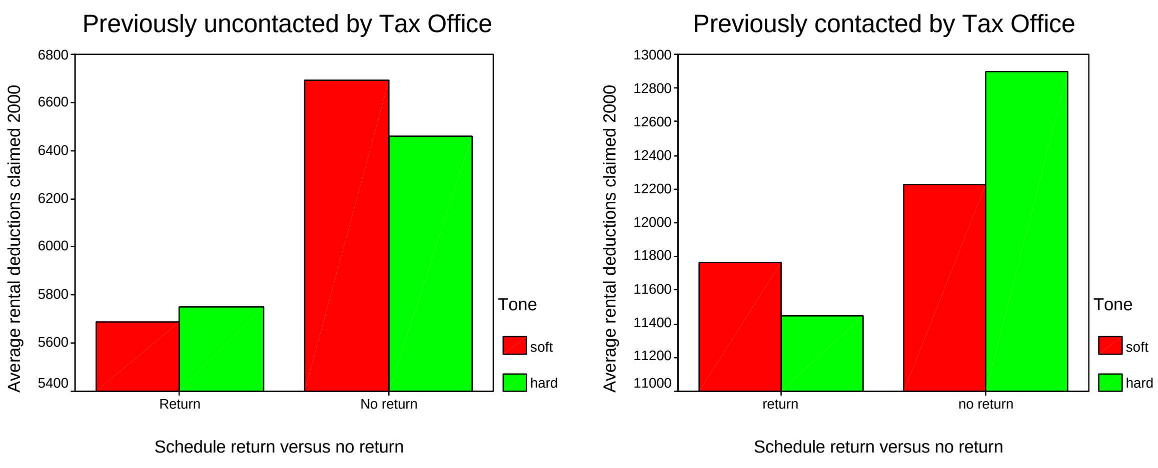
Difference between schedule only and no return of schedule conditions

The no return of schedule condition was included to investigate whether any increase in rental income declared or decrease in rental deductions claimed when a schedule was returned was due to being accountable to the Tax Office (surveillance), or due to the information contained in the schedule per se. That is, simply following the guidelines in the schedule may have led to a decrease in rental deductions claimed through increasing knowledge about what was required. To investigate the role of the schedule, these two conditions were compared for deductions claimed in 2000 in an ANCOVA, controlling for relevant covariates. Further, to test for the possibility of reactance being raised through a hard tone of letter, tone (hard or soft) was included as a separate factor in the analysis. Table 6 gives the results of this analysis.

It can be seen from Table 6 that, after controlling for other variables, a main effect for condition was found for both those previously untouched, $F(1, 1422) = 12.73$, $p=.000$, and those previously touched, $F(1, 1576) = 10.43$, $p=.001$, reflecting higher deductions claimed by those who received a schedule but did not have to return it (M = $6578 for untouched and M = $12,561 for touched) than those who had to return it (M = $5719 for untouched and M = $11,605). In addition, however, a marginally significant interaction was found between tone and condition for those previously touched by the Tax Office, $F(1, 1576) = 3.37$, $p = .067$. The interaction between tone and condition for those previously contacted by the Tax Office and those not contacted by the Tax Office are depicted graphically in Figure 2.

Table 6: Analyses of covariance (ANCOVA) on rental deductions 2000 (transformed variable), as a function of receiving and returning a schedule and tone, for untouched and touched samples

	Untouched sample			Touched sample		
Source	**df**	**F**	**p**	**df**	**F**	**p**
Covariates						
Age	1	63.97	.000	1	48.72	.000
Sex	1	0.57	.565	1	0.22	.642
Lodgment week 2000	1	18.65	.000	1	8.12	.004
Income 2000	1	49.27	.000	1	51.20	.000
Schedule lodged	1	6.55	.011	1	9.65	.002
Gross rent 2000	1	656.48	.000	1	444.38	.000
Rental deductions 1999	1	1119.72	.000	1	2536.04	.000
Tone	1	1.65	.200	1	0.11	.744
Letter	1	12.73	.000	1	10.43	.001
Tone x letter	1	0.62	.432	1	3.37	.067
Error	1422			1576		



(a) (b)

Figure 2: Mean rental deductions claimed in 2000 for (a) those previously uncontacted and (b) those previously contacted by the Tax Office as a function of tone and whether the schedule had to be returned.

It can be seen that while not having to return the schedule resulted in greater rental deductions being claimed for both those previously touched and not touched, a hard tone of letter resulted in less rental deductions being claimed than did a soft tone for those previously touched when the schedule had to be returned. This pattern, however, was reversed when the schedule did not have to be returned. A hard tone of letter resulted in more rental deductions being claimed than did a soft tone.

Net rent

While net rent was not reported in these results as a separate variable (net rent is the result of gross rental income minus rental deductions), it is a within-subjects variable and for this reason will be reported briefly. Separate ANCOVAs for net rent revealed precisely the same pattern as that found for rental deductions. For the untouched sample, the schedule only condition (M = \$61) was the only condition to result in significantly greater net rent than the control condition (M = –\$457), p = .005. For the touched sample, the schedule only condition (M = \$1128) and the schedule and booklet condition (M = \$915) resulted in significantly greater net rent than did the control condition (M = \$244), ps = .005 and .035, respectively. In terms of value to the Tax Office, this means that, on average, the schedule only condition resulted in approximately \$518 more in net rent per person than did the control condition for the untouched sample, and approximately \$884 more in net rent per person for the touched sample.

Discussion

Effect of letter type

It would appear that being required to return a schedule to the Tax Office is important in producing less rental deduction claims and greater net rent than in the control conditions. While the schedule only condition was the only condition to differ significantly from the control group for those previously untouched ‘non-risk’ rental property owners, both the schedule only condition and the schedule and booklet condition differed significantly from the control group in the previously touched ‘risk’ sample. It seems that the requirement to return a schedule is paramount in reducing rental deduction claims. One possible reason why including the booklet had an effect for previously touched rental property owners but not for the previously untouched sample may be due to the fact that those with higher rental income find the booklet useful while those with lower rental income do not. Given that average gross rental income was substantially lower for the previously untouched sample than for the touched sample, it is possible that those in the touched sample generally own more properties and may be more familiar with, or interested in obtaining further information about, rental property issues. Those in the untouched sample, however, may own less rental property and may find the information contained in the booklet too complex or unnecessary.

Further, although the question of which condition was most effective in producing the greatest declaration of rental income was answered (schedule only), implying that the booklet and information sheets are unnecessary, it must be remembered that this was also the condition in which most phone calls were received. The majority of these calls related to requests for extra information, and were double that received for the schedule and booklet condition. This implies that there may have been an information deficit in the schedule only condition, and it is possible that these taxpayers may have erred on the side of caution in declaring rental income and claiming rental deductions. This possibility will be investigated in the next phase of this study (beginning June 2001) in which, based on the issues raised in the phone calls received, more information will be provided in the letter accompanying the schedules. It should be remembered also, however, that the number of calls overall was small (only 3% of those in the study rang in).

Returning the schedule versus not returning the schedule

Receiving the schedule without having to return it was included in the design to investigate whether the effect of the schedule was due to surveillance by the Tax Office or improved record keeping/informational value. The results revealed that receiving the schedule alone without having to return it resulted in higher rental deduction claims than when the schedule had to be returned, and did not differ from the control group. While this result suggests that it is surveillance by the Tax Office that drives the effect of the schedules, it is possible that taxpayers in the no return condition simply discarded the schedule without looking at it once they realised they did not need to return it. If this were so, then a clear comparison between the two conditions could not be made. This possibility means that the informational/better record-keeping possibility cannot be dismissed out of hand. To address this issue, the next phase of this study will attempt to focus taxpayers who receive a schedule but do not have to return it on looking at and completing the schedule.

Hard or soft tone letters

Although the effects of tone were not strong and did not differentiate behaviour in general, it is possible that the distinction between soft and hard tone was not as clear as it could have been. To ensure that the letters are perceived by taxpayers in the intended way (that is, that a hard letter is indeed perceived as hard), the next phase of this study will pretest the letters on a convenience sample of taxpayers before the letters are sent out with the schedules. Pretesting the letters will provide a greater degree of confidence that the tone of the letters can be differentiated in the intended manner.

Despite the overall lack of an effect of tone in the present study, an interaction effect was found for the touched sample on whether or not the schedule had to be returned. That is, a hard tone produced less rental deduction claims than did a soft tone when the schedule had to be returned, but a soft tone produced less rental deductions than did a hard tone when the schedule did not have to be returned. Two possibilities present themselves here. Firstly, it is possible that a consistency effect may have been at work. For example, when a schedule has to be returned to the Tax Office, a hard tone is more consistent with such an approach. When a schedule does not have to be returned, a softer more cooperative tone is consistent.

A second and related explanation centres around the concept of reactance (Brehm & Brehm, 1981). When one is under surveillance (and hence can be punished for non-compliance), greater compliance results when threatened. However, to receive a threatening letter when one is not being asked to return the schedule may seem strange and needlessly aggressive, particularly if one has received and been asked to return a schedule in the past (which taxpayers in the touched sample had). That is, not only were they receiving a schedule from the Tax Office (for at least the second time), which they were not required to return, but some were also getting a harder than warranted letter accompanying it. This illegitimate threat could have raised reactance, which may then have been expressed in claiming more rental deductions when they were not under surveillance, resulting in more rental deductions being claimed when a hard rather than soft tone was used.

The explanation of reactance is also consistent with the finding that the interaction occurred only for those previously contacted, as these were the taxpayers most likely to perceive greatest illegitimacy. Although previously untouched non-risk taxpayers may have felt annoyed by having to complete a schedule (why me?), the fact that this was the first time they had been asked to complete a schedule may have provided sufficient justification to prevent reactance occurring. Those who were being sent schedules for the second or third time may have found it more difficult to justify (I am being unfairly victimised), increasing the potential for perceptions that being sent a schedule (again) was an illegitimate behaviour. To investigate further the hypothesis that reactance may explain the behaviour of the previously touched sample, the design for the next phase of the study will focus on taxpayers being sent a schedule, with short instructions included in the accompanying letter, which they will be required to either return or to keep. The letter accompanying the schedule will either emphasise penalties and sanctions (hard tone) or contain an appeal message (pretested), but the focus will be on manipulating perceptions of legitimacy of receiving the schedule. Both previously untouched and touched taxpayers will be sampled again. This time, however, the touched sample will comprise those previously classified as untouched from the present study and who were required to return schedules. This means that the touched sample in the next phase will not be from risk groups, and will have been requested to complete a schedule only once before. This manipulation will (a) assist in reducing extraneous variance (recall that the variance in the touched sample from the present study was particularly large because taxpayers were from a variety of different risk groups), and (b) provide the potential for perceptions of greater illegitimacy of being sent schedules. If reactance is being aroused as a result of being illegitimately threatened, the effect of sending threatening letters could result in counterproductive outcomes for the Tax Office. For this reason, investigating this possibility experimentally (as is proposed for the next phase of this study) would provide valuable information for the Tax Office.

Including the schedules in **TaxPack**

As will be recalled, it was suggested that if the schedules alone, with brief instructions, improved compliance over and above that of control groups and other conditions, they could potentially be included in *TaxPack* as an effective and cheap means of achieving greater compliance. Although the schedules alone were found in this study to result in significantly less rental deductions being claimed than in the control and other conditions, an important question still remains to be answered. If surveillance is responsible for the effect of the schedules (this point was not clarified in the present study), this would raise the question of whether it is personalised surveillance (I have been sent this schedule specially so the Tax Office is watching me) or general surveillance (Everyone is filling in this schedule so the Tax Office is watching everyone). If it were the latter, including the schedule in *TaxPack* would prove more beneficial than if it were the former. This is because once the schedule goes into *TaxPack*, it is no longer associated with personalised surveillance. Hence to find a reduction in the amount of rental deductions being claimed if the schedule was included in *TaxPack* would suggest that personal surveillance was not responsible for the effect of the schedules.

A first step toward investigating this issue is currently being undertaken, through comparing rental income and rental deduction statements of those who lodged their returns electronically in 1999–2000 with those of the paper preparers included in this study. Those who lodge electronically are automatically required to complete a schedule as part of the normal course of completing their tax return. Hence a comparison between electronic lodgers (non-personalised) and those paper preparers who were sent a schedule by the Tax Office to complete and return (personalised) should provide some insight into whether or not the effect of the schedules is to do with personal surveillance.

Conclusions

It is clear that the effect of the schedules is on the amount of rental deductions claimed (and hence net rent), not on gross rental income declared. Significantly less rental deductions were claimed in the present study when a schedule, accompanied by brief instructions, had to be completed and returned to the Tax Office. This result was consistent across both those taxpayers who had been asked to complete rental schedules before (and were classified as belonging to risk groups), and those who had not. In terms of value to the Tax Office, this resulted in approximately $518 more in net rent per person than in the control condition for the untouched sample, and approximately $884 more in net rent per person for the touched sample.

Further, for those who have been sent schedules to complete in previous years (classified as belonging to risk groups), the tone of the letter appears to be important, depending upon whether or not the schedule has to be returned. Taking a hard line appears to result in less rental deductions being claimed when the schedule has to be returned (and the taxpayer is under surveillance), but results in higher rental deductions being claimed when the schedule does not have to be returned (taxpayer not under surveillance). This implies that taking one approach to all taxpayers is inadequate and can be counterproductive (one hat does not fit all). It is also very interesting to note that simply being contacted by the Tax Office (that is, being individually sent a letter of any description by the Tax Office) does not result in reduced rental deduction claims. Contact alone seems to be insufficient to produce behavioural change.

Although the present study was not able to answer completely all the questions it set out to investigate (for example, whether the effect of schedules is due to surveillance or information), it was consistently found that having to return the schedules resulted in the least rental deductions being claimed. The questions that remain unanswered will be, and can only be, addressed through further experimental investigation. Indeed, the value of the experimental approach is that it allows a more controlled investigation of particular questions and hypotheses, while often raising questions or problems that could not have been previously foreseen. Such unforeseen issues or unresolved questions then provide a solid direction to pursue in further research. In this way, the answers to the questions become more and more refined and reliable. This is what the next phase of the rental project (beginning June 2001) is aiming for. Identifying experimentally which approach is best suited to which taxpayer will prove beneficial in obtaining the best outcome in terms of rental income and, in a broader context, obtaining better outcomes across different areas of tax revenue. Such an approach is clearly of value to the Tax Office.

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APPENDIX

SOFT INFORMATION ONLY CONDITION

Dear

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

At the Australian Taxation Office (ATO) we are committed to helping taxpayers to correctly prepare their income tax returns.

Based on the data that we have collected from our rental property audit activities, we have identified a number of errors that rental property owners commonly make.

We are writing to some rental property owners, such as yourself, to draw your attention to areas where mistakes are regularly made. By alerting you to these areas, we hope to make the process of preparing a correct return easier for you.

The areas where mistakes are often made include:

- non-commercial rental arrangements
- availability of the property for rental
- repairs
- depreciation
- special building write-off
- interest
- travel expenses

If you prepare your own income tax return, please read the instructions for question 17 of *TaxPack 2000 supplement* before completing that question. If you would like further information regarding the taxation implications of rental property ownership, please refer to the ATO publication, *Rental Properties*. To obtain a copy of this booklet, please call our distribution service on 1300 720 092 and they will make arrangements to send you a copy. Alternatively, you may wish to visit your local branch of the ATO to obtain a copy.

If you choose to prepare your own tax return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *TaxPack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Please remember that you are responsible for the accuracy of your tax return, even if it is prepared by a registered tax agent.

If you have any further enquiries regarding the above, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J Granger
DEPUTY COMMISSIONER OF TAXATION

SOFT SCHEDULE ONLY TO BE RETURNED CONDITION
Dear

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

At the Australian Taxation Office (ATO) we are committed to helping taxpayers to correctly prepare their income tax returns.

To help us identify areas of misunderstanding, we are asking selected taxpayers to provide additional rental information by completing a rental property schedule. As part of this process, we have selected you to assist us with our review this year.

Enclosed are four *Rental Property Schedules*. Please work through the instructions outlined in this letter and complete a schedule for each rental property that you own, or have an interest in.

If you require more than 4 schedules, please contact Public Assistance in your local ATO branch on 132 861. They will arrange to mail additional copies to you.

How to complete the schedule
Please complete your personal details and the property details on the front page of the schedule.

You need to provide details of your rental property income and expenses you incurred against that income on page two of the schedule. Please put the amount of your expenses at the relevant labels, and deduct your total expenses from the gross rent figure, to determine net rent. If you have a net loss, please place an 'L' in the box to the right of the net rent figure.

If you have expenses that cannot be allocated to any of the listed labels, please include them in the sundry rental expenses at label 'V'.

If you own more than one rental property, you must prepare a separate schedule for each property.

If you are a part owner of a property, divide all gross assessable rental income and rental expenses in the same proportion as your share in the property – for example 50/50.

Joint tenants who are not carrying on a business of property rental must divide the rental income and expenses equally, as each tenant holds an equal interest in the property.

Tenants in common may hold different interests in the property. If they are not carrying on a business of property rental, they must divide the rental income and expenses in accordance with their legal interest in the property.

For further assistance regarding the taxation implications of rental property ownership, please refer to the booklet *Rental Properties*. To obtain a copy of this booklet, please call our distribution service on 1300 720 092 and they will make arrangements to send you a copy. Alternatively, you may wish to visit your local branch of the ATO to obtain a copy.

Who is required to complete a Rental Property Schedule?
Please note that not all property owners will be required to complete a rental property schedule for the 1999-2000 income year. Only a recipient of a letter such as this needs to complete a rental property schedule. It is possible that other owners of a property in which you held an interest will not have been requested to complete a rental property schedule. Please note that you only need to disclose income and expenses from a rental property(s) located in Australia.

Problem areas
Based on the data that we have collected from our rental property audit activities, we have identified a number of errors that rental property owners commonly make. By alerting you to the areas where the errors are made, we hope to make the process of preparing a correct return easier for you. These areas are:

- non-commercial rental arrangements
- availability of the property for rental
- repairs
- depreciation
- special building write-off
- interest

- travel expenses

<u>Lodgment of the Schedule</u>
The schedule is to be forwarded to the ATO in the envelope provided. The address on this envelope is:

Rental Property Schedule
Corporate Data Capture
PO Box 1200
Albury NSW 2640

You must return the schedule to the ATO on the same day as you lodge your tax return. Please note that this is not the address for lodgment of your tax return. See page 130 of *TaxPack 2000* to find out where to lodge your tax return.

TaxPack
This package is being sent to you separately from *TaxPack 2000* and *TaxPack 2000 supplement*. You should receive your copy of these publications in the next 2-3 weeks, if you have not already received them. Otherwise, they will be available from 1 July to 31 October 2000 from newsagents, or throughout the year from the ATO.

If you choose to prepare your own return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *Tax Pack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Please remember that you are responsible for the accuracy of your tax return, even if it is prepared by a registered tax agent.

If you have any further enquiries about the Rental Property Schedule, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J Granger
DEPUTY COMMISSIONER OF TAXATION

SOFT SCHEDULE AND BOOKLET CONDITION

Dear Name

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

At the Australian Taxation Office (ATO) we are committed to helping taxpayers to correctly prepare their income tax returns.

To help us identify areas of misunderstanding, we are asking selected taxpayers to provide additional rental information by completing a rental property schedule. As part of this process, we have selected you to assist us with our review this year.

Information Package

The enclosed information package consists of a copy of *Rental property instructions and schedule* and the booklet *Rental Properties*. Please work through the instructions and booklet to calculate the net income or loss from your rental property(s). You will need to complete a separate schedule for each rental property that you own or hold an interest in.

At the back of the *Rental property instructions and schedule* are 6 rental property schedules. If you require more, please contact Public Assistance in your local ATO branch on 132 861. They will arrange to mail additional copies to you.

Who is required to complete a Rental Property Schedule?

Please note that not all property owners will be required to complete a rental property schedule for the 1999-2000 income year. Only a recipient of a letter such as this needs to complete a rental property schedule. It is possible that other owners of a property in which you held an interest will not have been requested to complete a rental property schedule. Please note that you only need to disclose income and expenses from a rental property(s) located in Australia.

Problem areas

Based on the data that we have collected from our rental property audit activities, we have identified a number of errors that rental property owners commonly make. By alerting you to the areas where the errors are made, we hope to make the process of preparing a correct return easier for you. These areas are:

- non-commercial rental arrangements
- availability of the property for rental
- repairs
- depreciation
- special building write-off
- interest
- travel expenses

Each of these topics is covered in the enclosed booklet, *Rental Properties*.

Lodgment of the Schedule

The schedule is to be forwarded to the ATO in the envelope provided. The address on this envelope is:

Rental Property Schedule
Corporate Data Capture
PO Box 1200
Albury NSW 2640

You must return the schedule to the ATO on the same day as you lodge your tax return. Please note that this is not the address for lodgment of your tax return. See page 130 of *TaxPack 2000* to find out where to lodge your tax return.

TaxPack

This package is being sent to you separately from *TaxPack 2000* and *TaxPack 2000 supplement*. You should receive your copy of these publications in the next 2-3 weeks, if you have not already received them. Otherwise, they will be available from 1 July to 31 October 2000 from newsagents, or throughout the year from the ATO.

If you choose to prepare your own tax return and you make an honest mistake, you will not be charged a penalty provided you have properly used *TaxPack 2000* and *TaxPack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Please remember that you are responsible for the accuracy of your tax return, even if it is prepared by a registered tax agent.

If you have any further enquiries about the Rental Property Schedule, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J Granger
DEPUTY COMMISSIONER OF TAXATION

SOFT NO RETURN OF SCHEDULE CONDITION

Dear Name

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

At the Australian Taxation Office (ATO) we are committed to helping taxpayers to correctly prepare their income tax returns.

Based on the data that we have collected from our rental property audit activities, we have identified a number of errors that rental property owners commonly make.

We are writing to some rental property owners, such as yourself, to draw your attention to areas where mistakes are regularly made. By alerting you to these areas, we hope to make the process of preparing a correct return easier for you.

The areas where mistakes are often made include:

- non-commercial rental arrangements
- availability of the property for rental
- repairs
- depreciation
- special building write-off
- interest
- travel expenses

If you prepare your own income tax return, please read the instructions for question 17 of *TaxPack 2000 supplement* before completing the question.

For your information, we have also included a schedule which you can use to assist in determining the net rent that you have earned on your rental property(s).

This schedule has been included for your information only. You are not obliged to use it, however we recommend that you do, and you should keep it with your taxation records. **Please do not send the completed schedule back to the ATO.**

How to complete the schedule

To complete this schedule you need to place the address of property at the top of the form (please make copies of the schedule if you own or have an interest in more than three properties). Place the amount of your expenses at the relevant labels, and deduct your total expenses from the gross rent figure, to determine net rent. If your expenses are greater than your gross rent, you have made a rental loss.

If you have expenses that cannot be allocated to any of the listed labels, please include them in the sundry rental expenses at label 'V'.

If you are a part owner of a property, divide all gross assessable rental income and rental expenses in the same proportion as your share in the property – for example 50/50.

Joint tenants who are not carrying on a business of property rental must divide the rental expenses and income equally, as each tenant holds an equal interest in the property.

Tenants in common may hold different interests in the property. If they are not carrying on a business of property rental, they must divide the rental income and expenses in accordance with their legal interest in the property.

If you would like further information regarding the taxation implications of rental property ownership, please refer to the ATO publication, *Rental Properties*. To obtain a copy of this booklet, please call our distribution service on 1300 720 092 and they will make arrangements to send you a copy. Alternatively, you may wish to visit your local branch of the ATO to obtain a copy.

If you choose to prepare your own tax return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *TaxPack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Please remember that you are responsible for the accuracy of your tax return, even if it is prepared by a registered tax agent.

If you have any further enquiries about the Rental Property Schedule, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J Granger
DEPUTY COMMISSIONER OF TAXATION

HARD INFORMATION ONLY CONDITION
Dear Name

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

Over the past few years the Australian Taxation Office (ATO) has conducted an extensive review program which has enabled us to collect and analyse rental property income and deductions data. The program has resulted in a substantial number of adjustments to rental property claims.

Our review has enabled us to identify certain broad groups of taxpayers with similar income and deduction patterns. In order for us to refine our approach we are randomly selecting a sample of rental property owners to verify, or provide other data, on our findings.

You may be selected as part of our sample for audit action, so when you lodge your income tax return this year, take particular care to ensure you have correctly accounted for all your rental income and associated deductions. You should also ensure that you keep all necessary supporting documentation.

Audit Action

As part of an overall verification process, we will be reviewing the income tax returns of those taxpayers that we believe require further scrutiny. A number of those taxpayers will be contacted and asked to submit their records and details of their claims for specific review.

If you are selected for a specific review we will write to you and let you know what information and documentation we require. If we ask you to send us records or other information – but you do not – we may adjust your return and impose a penalty. This is why it is important that you maintain accurate records and that you provide us with the information, if requested.

Wherever possible, reviews will be commenced in the current year.

Penalties

Under self assessment, we generally process income tax returns based on the information supplied by taxpayers. However, you are responsible for the accuracy of your income tax return, even if it is prepared by a registered tax agent. Penalties may apply if your income tax return is found to be incorrect.

If you choose to prepare your own return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *Tax Pack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Assistance

If you have any further enquiries regarding the above, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J. Granger
DEPUTY COMMISSIONER OF TAXATION

HARD SCHEDULE ONLY TO BE RETURNED CONDITION

Dear Name

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

Over the past few years the Australian Taxation Office (ATO) has conducted an extensive review program which has enabled us to collect and analyse rental property income and deductions data. The program has resulted in a substantial number of adjustments to rental property claims.

Our review has enabled us to identify certain broad groups of taxpayers with similar income and deduction patterns. In order for us to refine our approach we are randomly selecting a sample of rental property owners to verify, or provide other data on our findings.

You have been selected to complete the attached Rental Property Schedule for this purpose. You may also be selected as part of our sample for audit action, so you should take particular care to ensure you have correctly accounted for all your rental income and associated deductions. You should also ensure that you keep all the necessary supporting documentation.

Rental Property Schedules

We are sending you four Rental Property Schedules. You must complete a schedule for each property you own or have an interest in.

How to complete the schedule

Please complete your personal details and the property details on the front page of the schedule.

You need to provide details of your rental property income and expenses you incurred against that income on page two of the schedule. Please put the amount of your expenses at the relevant labels, and deduct your total expenses from the gross rent figure, to determine net rent. If you have a net loss, please place an 'L' in the box to the right of the net rent figure.

If you have expenses that cannot be allocated to any of the listed labels, please include them in the sundry rental expenses at label 'V'.

If you own more than one rental property, you must prepare a separate schedule for each property.

If you are a part owner of a property, divide all gross assessable rental income and rental expenses in the same proportion as your share in the property – for example 50/50.

Joint tenants who are not carrying on a business of property rental must divide the rental income and expenses equally, as each tenant holds an equal interest in the property.

Tenants in common may hold different interests in the property. If they are not carrying on a business of property rental, they must divide the rental income and expenses in accordance with their legal interest in the property.

It is possible that other owners of a property in which you hold an interest will not have been requested to complete a rental property schedule.

Lodgment of the Schedule
The schedule is to be forwarded to the ATO in the envelope provided. The address on this envelope is:

Rental Property Schedule
Corporate Data Capture
PO Box 1200
Albury NSW 2640

You must return the schedule to the ATO on the same day as you lodge your tax return. Please note that this is not the address for lodgment of your tax return. See page 130 of *TaxPack 2000* to find out where to lodge your tax return.

Audit Action

As part of an overall verification process, we will be reviewing the income tax returns of those taxpayers that we believe require further scrutiny. A number of those taxpayers will be contacted and asked to submit their records and details of their claims for specific review.

If you are selected for a specific review we will write to you and let you know what information and documentation we require. If we ask you to send us records or other information – but you do not – we may adjust your return and impose a penalty. This is why it is important that you maintain accurate records and that you provide us with the information, if requested.

Wherever possible, reviews will be commenced in the current year.

Penalties

Under self assessment, we generally process income tax returns based on the information supplied by taxpayers. However, you are responsible for the accuracy of your income tax return, even if it is prepared by a registered tax agent. Penalties may apply if your income tax return is found to be incorrect.

If you choose to prepare your own return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *Tax Pack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Assistance

If you have any further enquiries about the Rental Property Schedule, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J. Granger
DEPUTY COMMISSIONER OF TAXATION

HARD SCHEDULE AND BOOKLET CONDITION

Dear Name

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Our review has enabled us to identify certain broad groups of taxpayers with similar income and deduction patterns. In order for us to refine our approach we are randomly selecting a sample of rental property owners to verify, or provide data on our findings.

You have been selected to complete the attached Rental Property Schedule for this purpose. You may also be selected as part of our sample for audit action, so you should take particular care to ensure you have correctly accounted for all your rental income and associated deductions. You should also ensure that you keep all the necessary supporting documentation.

Rental Property Schedule

We are sending you a R*ental Property Instructions and Schedule* booklet which has six rental property schedules attached to it. You must complete a separate schedule for each property you own or have an interest in. By working through the instructions and schedule, we are confident that you will correctly calculate the net income or loss from your property(s).

Lodgment of the Schedule

The schedule is to be forwarded to the ATO in the envelope provided. The address on this envelope is:

Rental Property Schedule
Corporate Data Capture
PO Box 1200
Albury NSW 2640

You must return the schedule to the ATO on the same day as you lodge your tax return. Please note that this is not the address for lodgment of your tax return. See page 130 of *TaxPack 2000* to find out where to lodge your tax return.

Rental Booklet

To assist you in completing your rental property claims we have also enclosed a copy of the *Rental Properties* booklet.

Audit Action

As part of an overall verification process, we will be reviewing the income tax returns of those taxpayers that we believe require further scrutiny. A number of those taxpayers will be contacted and asked to submit their records and details of their claims for specific review.

If you are selected for a specific review we will write to you and let you know what information and documentation we require. If we ask you to send us records or other information – but you do not – we may adjust your return and impose a penalty. This is why it is important that you maintain accurate records and that you provide us with the information, if requested.

Wherever possible, reviews will be commenced in the current year.

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Under self assessment, we generally process income tax returns based on the information supplied by taxpayers. However, you are responsible for the accuracy of your income tax return, even if it is prepared by a registered tax agent. Penalties may apply if your income tax return is found to be incorrect.

If you choose to prepare your own return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *Tax Pack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

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Yours faithfully

J. Granger
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HARD NO RETURN OF SCHEDULE CONDITION

Dear Name

2000 TAX RETURN : INFORMATION ABOUT YOUR RENTAL PROPERTY OR PROPERTIES

Over the past few years the Australian Taxation Office (ATO) has conducted an extensive review program which has enabled us to collect and analyse rental property income and deductions data. The program has resulted in a substantial number of adjustments to rental property claims.

In order to improve the accuracy of rental property claims, the ATO is randomly selecting a sample of rental property owners who will be sent a Rental Property Schedule to assist them in completing their tax returns. It is possible that some rental property owners included in this year's sample may have been sent schedules last year as well. This schedule asks for details of all income and deductions associated with each rental property owned, which you can use to assist in determining the net rent that you have earned on your rental property(s).

This schedule has been included for your information only. You are not obliged to use it, however in your own interests we recommend that you do, and you should keep it with your taxation records. **Do not send the completed schedule back to the ATO – it should be kept with your taxation records.**.

You may be selected as part of our sample for audit action, so when you lodge your income tax return this year, take particular care to ensure you have correctly accounted for all your rental income and associated deductions. You should also ensure that you keep all necessary supporting documentation.

How to complete the schedule
To complete this schedule you need to place the address of the property at the top of the form (please make copies of the schedule if you own or have an interest in more than three properties).

You need to provide details of your rental property income and expenses you incurred against that income on page two of the schedule. Rental income (A) is the full amount of all rent paid by your tenants, and is not to be reduced by agent commissions or other deductions. Other rental related income (B) includes compensation for lost rent, retained rental bond money, letting fees, and expenditure adjustments such as reimbursements and recoupments. Please put the amount of your expenses at the relevant labels, and deduct your total expenses from the gross rent figure, to determine net rent. If you have a net loss, please place an 'L' in the box to the right of the net rent figure.

If you have expenses that cannot be allocated to any of the listed labels, they should be included in the sundry rental expenses at label 'V'.

If you are a part owner of a property, divide all gross assessable rental income and rental expenses in the same proportion as your share in the property–for example 50/50.

Joint tenants who are not carrying on a business of property rental must divide the rental expenses and income equally, as each tenant holds an equal interest in the property.

Tenants in common may hold different interests in the property. If they are not carrying on a business of property rental, they must divide the rental income and expenses in accordance with their legal interest in the property.

Audit Action
As part of an overall verification process, we will be reviewing the income tax returns of those taxpayers that we believe require further scrutiny. A number of those taxpayers will be contacted and asked to submit their records and details of their claims for specific review.

If you are selected for a specific review we will write to you and let you know what information and documentations we require. If we ask you to send us records or other information – but you do not – we may adjust your return and impose a penalty. This means it is in your interests to maintain accurate records and to provide us with the information, if requested. Wherever possible, audit of tax returns will be commenced in the current year.

Penalties
Under self assessment, we generally process income tax returns based on the information supplied by taxpayers. However, you are responsible for the accuracy of your income tax return, even if it is prepared by a

registered tax agent. Penalties may apply if your income tax return is found to be incorrect, and penalties will be imposed if deliberately false or misleading claims are made.

If you choose to prepare your own return and you make an honest mistake, you will not be charged a penalty, provided you have properly used *TaxPack 2000* and *Tax Pack 2000 supplement* in preparing your tax return. See the *Commissioner's guarantee* on the inside front cover of *TaxPack 2000* for more details.

Further information
In you have any further enquiries about the Rental Property Schedule, please telephone (08) 9268 5794, or for the cost of a local call, telephone the ATO Public Assistance helpline on 132 861 and ask to be connected to extension 85794.

Yours faithfully

J Granger
DEPUTY COMMISSIONER OF TAXATION

THE CENTRE FOR TAX SYSTEM INTEGRITY
WORKING PAPERS

No. 1. Braithwaite, V. & Reinhart, M. *The Taxpayers' Charter: Does the Australian Taxation Office comply and who benefits?* Dec. 2000.

No. 2. Braithwaite, V. *The Community Hopes, Fears and Actions Survey: Goals and Measures.* March 2001.

No. 3. Braithwaite, V., Reinhart, M., Mearns, M. & Graham, R. *Preliminary findings from the Community Hopes, Fears and Actions Survey*. April 2001.

No. 4. Mearns, M. & Braithwaite, V. *The Community Hopes, Fears and Actions Survey: Survey method, sample representativeness and data quality*. April 2001.

No. 5. Sakurai, Y. & Braithwaite, V. *Taxpayers' perceptions of the ideal tax adviser: Playing safe or saving dollars?* May 2001.

No. 6. Wenzel, M. *The impact of outcome orientation and justice concerns on tax compliance: The role of taxpayers' identity.* June 2001.

No. 7. Wenzel, M. *Misperceptions of social norms about tax compliance (1): A prestudy.* June 2001.

No. 8. Wenzel, M. *Misperceptions of social norms about tax compliance (2): A field-experiment.* June 2001.

No. 9. Taylor, N. *Taxpayers who complain about paying tax: What differentiates those who complain from those who don't?* June 2001.

No. 10. Wenzel, M. *Principles of procedural fairness in reminder letters and awareness of entitlements: A prestudy*. June 2001.

No. 11. Taylor, N. & Wenzel, M. *The effects of different letter styles on reported rental income and rental deductions: An experimental approach.* July 2001.