



*Research report*

# Motivating SME compliance

Achieving better voluntary compliance  
amongst small businesses: research findings

Business Customer & Strategy

**May 2010**

---

## Motivating SME Compliance

### *About Business Customer and Strategy (BC&S)*

Business Customer and Strategy is part of Business Tax. The goal of BC&S is to maximise Business Customer compliance for HMRC at best cost for both HMRC and the customer. This is done by developing business tax strategies through customer understanding, working with teams in HMRC and across government departments.

### *Contents*

Motivating SME compliance	3
Research requirement	3
Method, Data and Tools used, Sample	5
Ideas tested	6
Executive summary of main findings	13

© Crown Copyright 2013 Published by Her Majesty's Revenue and Customs.

Disclaimer: The views in this report are the authors' own and do not necessarily reflect those of HM Revenue & Customs.

---

## Motivating SME Compliance

# Motivating SME compliance

## *Research requirement*

### Background and objectives

This project was commissioned in two separate stages. The following section aims to outline the background and objectives for both pieces of work and indicate how the two played together. Ultimately whilst there is a clear trajectory throughout these two pieces, for clarity, this report will retain the terminology of ‘stage one’ and ‘stage two’ in order to signpost the way in which themes and concepts have been developed over the course of the work.

#### a. Background

In the wake of global recession and with the recognition of a significant budget deficit in the UK economy the importance of plugging the ‘tax gap’ (the estimated difference between the amount actually received by HMRC and the amount which it should receive) has perhaps never been greater. However, with substantial budget cuts and belt tightening to reduce the deficit anticipated across the public sector for the foreseeable future, it is more important than ever for HMRC to explore more innovative and more cost-effective approaches for closing the tax gap.

Stage one of this project was initially commissioned in November 2008 and aimed specifically at increasing voluntary compliance amongst small business owners (SMEs). The objectives for the project were specifically rooted in the desire to investigate alternative avenues through which HMRC might seek to encourage greater compliance, by complementing rather than replacing existing strategies. Whilst it was recognised that HMRC had in place a number of strategic initiatives to support compliance amongst SMEs – including more investment up-front and upstream (including agents), a greater focus on evaders, and better support for voluntarily compliant businesses - the ‘tax gap’ remained significant.

This project, therefore, was undertaken on the rationale that the continued ‘tax gap’ amongst SMEs indicates that there may be an audience that is either not currently being reached by existing strategies or may be more (cost) effectively targeted through alternative methods. That by tapping into prevalent motivations in the wider business and personal worlds of those who are unwilling, unable, or for other reasons do not end up paying sufficient tax, the department may begin to widen the field for alternative approaches.

This working hypothesis is not unique to this project. Over recent years a number of studies both inside and outside the public sector have debated similar issues. A notable example of this is found in ‘Mindspace’ a study which was published by The Cabinet Office in March 2010 (after the completion of stage one of this project) which states:

*Tools such as incentives and information are intended to change behaviour by “changing minds”. If we provide the carrots and sticks, alongside accurate information, people will weigh up the revised costs and benefits of their actions and respond accordingly. Unfortunately, evidence suggests that people do not always respond in this “perfectly rational” way.*

*In contrast, approaches based on “changing contexts” - the environment within which we make decisions and respond to cues - have the potential to bring about significant changes in behaviour at relatively low cost. Shaping policy more closely around our inbuilt responses to the world offers a potentially powerful way to improve individual wellbeing and social welfare.<sup>1</sup>*

---

<sup>1</sup> Mindspace Report; Cabinet Office & Institute for Government

---

## Motivating SME Compliance

Thus in the same way as 'MindSpace' presents the potential for tapping into inbuilt responses this project sought first to establish what these inbuilt responses or 'motivations' were in the context for small business and how these relate to attitudes and behaviours surrounding tax (stage one). Stage two looked at means, in the form of ideas for products and services that would best leverage these attitudes and behaviours to encourage greater compliance.

It is important to note that this project was not at any stage an evaluation of the ultimate cost to HMRC in delivering a particular strategy. It worked instead from the SME perspective by establishing what motivated, and therefore had an intrinsic value, to SMEs. With that said, the project has been conscious at every stage of the need for any recommendations to be both practical and ultimately actionable, albeit with further development required, and therefore pains have been taken throughout the process to ensure a 'common sense' approach.

### b. Objectives

As the project was commissioned in two stages, the objectives built on each other accordingly. In broad terms, stage one can be seen as a more exploratory piece of work, seeking to develop a comprehensive view of small business owners' motivations and attitudes toward tax. Stage two objectives were more directed, seeking to develop the notional territories established in stage one to a point where they could be practically translated to a set of robust ideas and tested with SME customers.

At stage one the project looked to:

- Explore the deterrents and motivators that drive compliance, both voluntary and otherwise
- Explore the emotional or otherwise non rational dynamics of compliance
- Identify methods by which HMRC can influence businesses to improve voluntary compliance
- Understand why, and to what degree, different types of business customers are motivated as individuals i.e. emotionally/ non rationally, rather than in a more professional manner

Stage one produced an understanding of motivational territories, which were presented as six 'levers' which had the potential to generate voluntary compliance.

Stage two sought to build on these motivational territories developed in stage one by generating a range of ideas for products and services for SMEs that HMRC could use to drive compliance, alongside a set of directive design principles that would assist any future SME innovation within the department.

In detail the stage two objectives were to:

- Propose, test and finalise a set of design principles based on the territories from stage one to guide innovation and design of motivational tools to drive voluntary compliance amongst SMEs
- Generate original and realistic ideas for positive motivational tools (not marcomms) based on the territories from stage one
- Test the most promising of those ideas, plus a set of existing ideas around issuing certificates
- Refine ideas as necessary and recommend ideas to take forward

The ideas for motivational tools were designed, therefore, to fulfil two objectives through the research. On the first level they have been assessed as discreet propositions that HMRC may or may not choose to take forward for further development. Perhaps more crucially these ideas provided a practical method by which the levers established in stage one could be re-examined. The ideas provided SMEs with a practical context around which to frame conversations and allowed us to gain more minute, practical detail around the levers and their impact in 'reality', albeit a simulated environment. This exploration has provided us with some significant nuance which has been reflected in the discussion of levers in this report.

---

## Motivating SME Compliance

### c. Target audience

Participants in this research were all key influencers in the tax affairs of a small business. The vast majority of participants were small business owner-managers but a small number of pre-start up businesses (those who had not yet officially registered their business and agents) were used in order to gain perspectives from the widest breadth of the SME community. A full breakdown of the sample is included in the appendices.

Whilst the current HMRC SME segmentation had not yet been developed when stage one was commissioned, the range of SME postures on compliance were recognised in the design of the stage one research. SMEs who exhibit some avoidance or evasion behaviours, which we would now recognise as the rule breaker and potential rule breaker segments, were a clear target for the research. Likewise SMEs with low levels of knowledge, confidence and ability (that is, unaware and willing but needs help segments) were also part of the research, for the potential to provide wider insight into barriers to voluntary compliance. In addition, more compliant small business owners, those that we would now recognise as willing and able, were included in the research, presenting a clear opportunity to identify and unpick positive motivators alongside negative ones.

Even after the development of the SME segmentation, the findings from stage one - which we will explore in more detail in section 5 of this document - in fact uncovered strong potential for the work to continue to take a broad segment perspective. Whilst the different segments clearly presented differing attitudes towards certain aspects of taxation, there were some areas where there was more consensus and actions hinged around more fundamental human behavioural theory, which were unlikely to have a significantly different impact across segments. Certain levers identified could be used for action *across* segments. 'Social proof' a key lever from stage one is a good example of this, where utilising this lever would require a weight of public influence across compliant segments to drive social pressure on those who currently do not comply.

It was also recognised as imperative that the application of any lever would not foster a negative impact in any of the currently compliant segments. Thus measuring impact of the ideas across all segments was essential.

That said, however, SMEs from the 'rule breaker' segment were excluded in the final round of testing in stage two. This decision was taken on the basis that the customer strategy in relation to this segment is to increase the likelihood and consequences of being caught; not to encourage voluntary compliance. Furthermore, all the ideas to be tested in stage two were, on face value at least, centred on support from HMRC which it was thought would be unlikely to have a significant impact on rule breakers in direct research (i.e. focus groups). Crucially our conclusion is still that there can be an opportunity to target rule breakers and improve compliance through levers such as social proof but, as we will discuss later in the report, our view is that this cannot be tested through traditional research methods and therefore the influence of the levers and ideas on rule breakers cannot be conclusively assessed here.

It should be noted that throughout the report when we refer to 'willing' SMEs we are referring to the group of SMEs comprised of three segments: willing and able, payment deferrers and potential payment deferrers. These three segments were grouped together in stage two, as it was not practical within the confines of the budget available to sample them separately.

## *Method, Data and Tools used, Sample*

### Detailed methodology

In order to reach our conclusions, a thorough and highly developed methodology was used that included a mixture of innovation exercises and traditional research methods. Despite being separate projects, both are

## Motivating SME Compliance

strongly linked and there is a clear continuation from the first project into the second.

Stage 1 Project		
1	<b>Project Planning and grounding</b>	The project started with a great deal of background reading, desk research and a workshop with HMRC staff in order to help us understand the scope of the project
2	<b>15x full day Ethnographies</b>	We then conducted a series of SME focused ethnographies to explore and understand both their attitudes around tax and wider motivations
3	<b>Hypothesis testing - Focus groups</b>	Using our analysis from the ethnographies, we conducted 16x two hour focus groups with a range of business sizes & segments to test our early motivational hypothesis
4	<b>Analysis and Conclusions</b>	After evaluating the feedback, we then concluded the first stage by presenting our final hypothesis of potentially fertile motivational territory for SMEs
Stage 2 Project		
1	<b>Project Planning and reviewing territories</b>	We began by working closely with HMRC to outline which of the stage 1 territories would follow into the second stage for further exploration
2	<b>Desk research and stimulus harvesting</b>	We then carried out a substantial amount of desk research to search, filter and deploy new ideas and used them as stimulus for the first workshop
3	<b>Co-creation #1 – Ideas generation</b>	The two-day workshop was held with both innovation experts and HMRC staff and enabled us to translate the territories into a series of tangible propositions
4	<b>Testing #1 – Evaluate</b>	Having built a library of propositions, we then presented many of them to 8x two hour SME focus groups for discussion. A range of segments and business sizes were tested.
5	<b>Co-creation #2 – Ideas refinement</b>	The rich feedback we received from the groups was analysed and used as stimulus for a second two-day workshop aimed at refining and further developing the propositions
6	<b>Testing #2 – Evaluate</b>	Narrowing our focus to several rounded propositions, we retested them with new SME focus groups (8x two hours) to measure their success
7	<b>Refine, decide and develop business case</b>	Having collected all of the data, we evaluated the reactions of each segment and developed a set of design principles and recommendations for future proposition design

### *Ideas tested*

The ideas presented in stage two were the outputs of two creative workshops held with both HMRC staff and innovation experts familiar with small business management. Each of the following ideas for tools, resources and services were designed to link to the motivational levers developed in stage one. Having explored the more wide reaching insight from investigating these ideas in the main body of this report, the following section is an examination of the potential they may present as discreet propositions. Where appropriate

---

## Motivating SME Compliance

recommendations are also made here for modifications and refinements, however, it is important to consider that these ideas were not fully developed and 'ready to market' (the necessary input for this was beyond the scope of this project, requiring a full analysis of cost and feasibility). The research instead sought to take ideas to the point where they could be easily understood 'at a glance' for a notional read on appeal, thus for each idea that follows we have presented the 'idea outline' in the manner in which they were presented to SMEs.

### a. The online account

#### IDEA OUTLINE

- The SME would receive a letter including details of how to access the businesses' online account via a secure link on the HMRC website
- The first time the SME logs in they are asked to reset their password and answer a couple of security questions. They are given the option to provide an email address to which all future correspondence and updates from HMRC can be sent, making communications faster and easier
- The online account consists of three tabs: an 'account' tab, a 'support' tab and a 'tools' tab
- The account tab includes a comprehensive list of all tax contributions to date, including Corporation Tax, SA, PAYE & VAT where appropriate
- The support tab includes details of upcoming dates and deadlines for that specific SME and links to advice and support
- The tools tab includes widgets for making calculations

#### RATIONALE

The rationale behind this idea is quite wide ranging, as it is designed as a tool through which to house many of the other tools and resources tested in the research. At the most basic level it would provide a new, efficient and direct route for HMRC to channel the information and support SMEs need to pay their taxes, founded on the 'habits and practices' lever by encouraging improved record keeping. The benefits to HMRC from this include reducing some of the pressure on HMRC's other support services, and providing low cost 'help' to SMEs in line with the department's customer strategy. This tool would also exploit the 'engagement' lever by encouraging SMEs to consciously engage with tax by logging on a regular basis to manage tax contributions online. Furthermore by providing easy access to free help tools and support designed specifically for businesses, the tool may make it easier for SMEs to see how HMRC is supporting them as part of the fair exchange.

#### INSIGHT

Feedback suggests that this idea has strong merit not only as a standalone tool but also as a platform to extend functionality, for example, to add more tools and resources to the support tab, or allowing the small business owner to tailor tools and resources that they have found particularly useful or perhaps link to other business accounts. As this potential rule breaker states:

As a gateway to support tools and services then, feedback was broadly positive, however, more detail would be required on the entire suite of tools and functionality of this element in order for customers to make a full appraisal on how and when they might envisage using it.

More intuitive benefits that SMEs across segments identified in this tool were the ability to have immediate access to their records in a format that many are already familiar with (i.e. as similar to internet banking). This meant that the vast majority, with the exception of some willing but needs help/unaware SMEs (detailed below), felt confident that they would be able to log on and use it straight away without the need to invest time in familiarising themselves in the platform.

A particularly key benefit identified in this tool was the idea of being able to view different kinds of tax that the business pays in a single location, something which could align the HMRC system more closely



## Motivating SME Compliance

with the way in which SMEs think about their business tax, i.e. as all part of the same kind of business outgoing.

In terms of the online account providing a single gateway, customers also identified the ability to share the log in details with their accountant for information sharing as a plus.

If we look at the reception of specific segments to this idea, potential rule breakers and willing SMEs were equally positive. Indeed only the unaware and willing but need help segments noted particular anxiety, based on worries surrounding security. This is felt to be related to the fact that the willing but need help segment appeared to be the least tech savvy group in our research and were the most likely to mention a lack of trust with HMRC, specifically based on historical cases of lost data:

Other concerns highlighted by a small number of SMEs included a perception that the online account may be an attempt by HMRC to reduce the involvement of agents. This anxiety was again predominately noted amongst unaware/need help groups. A minority of Potential rule breakers also cited the increased visibility of data held by HMRC as raising some 'Big brother' concerns but the vast majority recognised that this was data that the department already held.

On the whole SMEs viewed the online account as a logical progression for managing any accounts (everyone is moving online) and a practical way by which both they and 'the government' could save time, effort and costs which in the current economic climate is widely welcomed.

### b. The tax ready reckoner

#### IDEA OUTLINE

- An easy to use tax calculator, which the SME finds via a link in the 'Tools' section on the HMRC online account
- The tool is also located on the Business Link website
- By entering some financial data, the SME can then use Ready Reckoner to work out how much money they should be setting aside on a yearly, quarterly or monthly basis in preparation for filing taxes

#### RATIONALE

A fairly straightforward proposition, the ready reckoner tool allows SMEs to make an estimated calculation of what their next contribution will be by answering a short series of questions online. For the purposes of this research the calculator was shown on the tabs tool of the online account but could equally be housed anywhere online or as a download. For the SME it represents a clear and practical means by which HMRC is seen to offer support to the SME as part of fair exchange. This information can be broken down into time periods that suit their business (e.g. yearly, quarterly or monthly) helping to generate a rhythm for tax that SMEs can manage easily. It could particularly help businesses whose finances may fluctuate, ensuring that they are setting enough money aside each year. By helping businesses properly estimate future contributions, HMRC could reduce the risk of businesses failing to pay the right amount as a result of cash flow problems and getting into financial difficulty at the end of each tax cycle. Use of the tool encourages SME engagement with tax and could improve habits and practices in the long term.

#### INSIGHT

The reckoner tool was a popular concept across each of the three segments, mainly due to the fact it offers *customised* support and is therefore specifically relevant to that individual SME. Though some SMEs use accountants to help them estimate their monthly contributions, some stated that it may potentially save them some accountancy fees where they are currently outsourcing small calculation requests. Those who didn't have accountants saw the biggest benefit though as they stated it would help them to plan and budget much more effectively. In terms of segment, this idea was less well



---

## Motivating SME Compliance

received by willing SMEs than other segments, but only because many of them already had systems to estimate future tax contributions:

This tool is, however, of significant stated benefit to the willing but needs help, unaware and the potential ruler breaker segments who appreciate the transparency as much as the simplicity of being able to make calculations quickly online.

A small minority of SMEs also had some slight concerns that entering this kind of data through an online tool assigned to them they may be 'committed' to the figures entered.

In summary, as a tool with potential to minimize tax 'shock' and encourage saving discipline amongst those who are currently less able to predict their contribution this tool was very well received but more importantly the reception of this tool clearly reflected the intention that it is a simple but effective way by which HMRC can demonstrate willingness to provide help and support as part of the fair exchange.

### c. The tax ISA

#### IDEA OUTLINE

- Information about the Tax ISA can be found either on the support tab of HMRC online account or local high street bank
- The Tax ISA will allow an SME to set aside money specifically for tax purposes in a single, tax free account with a competitive rate of interest
- Up to £10,000 per year can be deposited into the account on a monthly basis via a standing order from a bank account
- The SME is reassured that they will retain complete control over his money and can make a withdraw from the account at any point, but they will immediately lose its tax free status and interest should they choose to do so before the account comes to fruition. This will be scheduled for a few days before their tax payment is due

#### RATIONALE

The 'Tax ISA' (a term that was used predominantly to facilitate easy interpretation) is essentially a long term savings account specifically for businesses, aiming to ensure that money is set aside for next year's tax bill allowing greater confidence and planning as part of developing a better 'rhythm for tax'. Although this is not envisaged as a tool provided directly from HMRC, the ability to build up interest over time represents a clear financial benefit to the SME in paying tax as part of fair exchange. The ability to make tax payments directly to HMRC via the account and potentially manage their account quickly and securely online via the 'online account' (as was suggested in the version showed for the research) would hold benefits for the SME by potentially simplifying their transactions. The benefits for HMRC in this idea though are potentially further reaching; whilst encouraging businesses to start their tax preparations early and start saving in advance holds clear benefits in itself, it is thought that by signing up to a tax ISA SME's are committing to a contract that encourages consistency. Although this would not be a public commitment, as demanded by the purest theory behind this lever, the requirement to make a commitment both to HMRC and the bank handling the ISA is thought to be more likely to engender long term consistency.

#### INSIGHT

The feedback for Tax ISA was generally positive. Most SMEs quickly acknowledged the savings benefit and the more efficient tax payment option. For both the willing and potential rule breaker segments, this facility seemed to fit well with their current approaches. As this willing SME states:

## Motivating SME Compliance

This indicates a strong connection with the intention of this tool to encourage structure and discipline, improving general habits and practices amongst SMEs. The reverse implication of this though is that the unaware/need help segments were less enthusiastic because the inflexible payment structure of the ISA, designed to ensure that the ISA would in fact improve habits and practices, would present a substantial financial commitment. These segments were more likely to cite the need to move money around often, perhaps as a result of poor planning and therefore felt that they would be unable to financially commit in the medium and long term. Many SMEs also felt that having 'another' account would further complicate their finances, particularly because it was related to tax:

On the whole, it is the potential return that is the stand out feature for SMEs, as with any savings account, most stated that their likelihood to use a 'tax ISA' would be dependent on the potential return and how competitive they perceived it to be in the market. SMEs acknowledged for example that there could be a potentially significant emotional advantage to this kind of scheme, providing reassurance that the tax bill would be covered at the end of the year, but this benefit would only be related to the HMRC account if it was seen to be offering something over and above other commercial accounts (e.g. in terms of interest and support) to ensure that perception reflected reality.

### d. Public tax clinic

#### IDEA OUTLINE

- The SME is emailed a link to the support tab on the HMRC website which provides details of an upcoming tax support clinic being held in their local area.
- The SME is able to book an appointment via their online account
- The clinics are led by trained HMRC officials and are designed to demonstrate the tax process for a small business. Afterwards, attendees are encouraged to ask questions and seek support on their specific tax issues

#### RATIONALE

The public tax clinic would allow SMEs to get access to free tax support in their local area and represents a clear and practical means by which HMRC is seen to offer support to the SME as part of 'fair exchange'. Public tax clinics would allow SMEs to learn some general principles on how to set up and run an efficient tax system for their business, thereby supporting SMEs in generating better 'habits and practices'. The proposition would also allow SMEs to ask more private questions about their businesses taxes in confidence and anonymity for those who may be nervous or reluctant to seek assistance through other channels. For HMRC though, the benefits are thought to be wider reaching. On the first level this would be a method of getting out into communities and getting a range of small businesses to think about tax issues, increasing SME 'engagement' with tax, as well as their knowledge and skills. On a second level though is thought that speaking with small businesses in a public forum may respond to the 'social proof' theory, based on the principal that SMEs witnessing others participating in a 'public' clinic will act as a positive example.

#### INSIGHT

SMEs warmed to the idea of public tax clinics on the grounds that they were lead by a well trained HMRC official and that the session was specifically designed for small businesses. Although willing businesses are, understandably, very unlikely to use this idea themselves they recognised the benefit for start-ups. Willing but needs help and unaware SMEs were understandably much more in favour of this idea:

## Motivating SME Compliance

Potential rule breakers appreciate support that helps to demystify the tax system, but there is a suggestion that potential rule breakers were more in favour of this idea as a result of the potential for anonymity:

When SMEs discuss the way in which they would envisage tax clinic working, there is some scepticism around the ability of HMRC to efficiently manage one on one appointments as a 'drop in' offering, even where the potential to book appointments in advance was presented. Many questioned the value of a 'pop up' clinic if you were scheduling appointments anyway. The expectation that a tax clinic would probably more closely resemble a kind of 'seminar' session meant that the most significant benefit is attributed to new start ups who stand to gain the most in terms of potential new information. Those who have had their businesses for some time were more sceptical about any potential support being specific enough to suit them. Events specifically tailored to key life stages (such as VAT registration) that could be pre-advertised does however present some appeal to the wider SME audience.

As previously discussed there can be little suggestion gained from direct feedback as to whether the tax clinic would have the desired social proof impact but there remains an appeal among a smaller section of the SME community for face to face interactions which this idea may serve.

### e. Tax assurance visit

#### IDEA OUTLINE

- The SME receives information about the tax assurance visit via an email from HMRC
- If the SME wishes to receive a visit, it is arranged for a day that suits the SME and is conducted by their own/an accountant using an HMRC certified system
- On the day of the visit the accountant runs through their current filing systems for tax accounts and makes suggestions for ways in which they can keep records more accurately and reduce any potential errors

#### RATIONALE

The tax assurance visit is a more personal proposition than the tax clinic, providing an opportunity to talk to a tax expert face to face about any issues they may be experiencing. It represents a clear and practical means by which HMRC is seen to offer support to the SME as part of a reciprocal 'fair exchange'. It is thought that receiving advice that is tailored to their business may further improve 'habits and practices' in a more permanent way than a simple call, reducing SME stress in the long term. For HMRC this is a thorough way of providing tailored support, reducing the number of filing errors made through inaccurate filing or record keeping but more importantly SMEs are encouraged to actively engage with tax as part of the process and by asking SMEs to sign up for the scheme it forms part of commitment to future behaviour. In the long term it may also reduce some of the pressure on HMRC's other support services.

#### INSIGHT

Feedback on the tax assurance visit was mixed. Trust and fear of HMRC is a big factor as many saw it as another form of inspection. Perhaps surprisingly it was the willing SME segment that cited most strongly that this felt like an inspection through the 'back door' and would therefore cause a great deal of anxiety. This may, however, be as a result of an inflated sense of the 'power' of HMRC. Willing but needs help and unaware SMEs were mixed in their feedback as although they recognised that it would benefit them in theory, the execution brought up similar anxieties to those stated by the willing segment. Potential rule breakers, were the only group that stated there may be some benefit in an independent expert conducting the session, but on the understanding that it would be HMRC-funded

---

## Motivating SME Compliance

and therefore constituted a 'free' accounting session. On the whole there may be some appeal for this as a service that targeted start ups exclusively as this would ensure that the discussion was focused on future improvements and advice without risking any issues concerning uncovering past errors:

### f. Tax certificates

#### IDEA OUTLINE

- The tax certificate confirms the SME has completed their tax return on time and the payment has been received by HMRC.
- The certificate also contains a courteous 'thank you' message from HMRC and a statistic that states they company are part of the 90% group of small businesses that return on time. It also assures them that the 10% who haven't will be receiving automatic penalties.
- The Certificate is sent electronically in PDF format.
- As part of the email the company receives, they are informed that they can also apply to receive their payment confirmation in a range of other formats (e.g. paper certificate, tax disk for a car)

#### RATIONALE

The theory of the tax certificate is that SMEs would receive automatic confirmation that their tax return and payment has been received which could close the loop for SMEs, as demanded by a 'rhythm for tax'. The certificate would also allow SMEs to demonstrate to a range of peers and clients that their business is tax registered and has been paid on time, building on the 'social proof' lever for HMRC. Although, as discussed in the main body of this report, it is difficult to test this kind of outcome as part of this research, social proof theory suggests that SMEs displaying certificates could generate a sense of pride around compliance, reinforcing compliant behaviour.

#### INSIGHT

The tax certificate received the least positive feedback of all of the ideas, though it was strongly backed by certain businesses that pride themselves on transparency and legitimate procedure (e.g. firms who rely upon government or charity funding or those that deal more directly with members of the public): Willing SMEs on the whole felt that this is an unnecessary scheme as paying taxes should be seen as something everyone has to do anyway:

Potential rule breakers were the only group to see some value to the idea of receiving additional confirmation of payment, but it is thought that this may be due to a misconception that this would represent 'irrefutable proof' of full payment. This finding does highlight the need amongst SMEs to experience some sense of finality for HMRC, where significant peace of mind may be achieved by 'closing the loop' on their tax transactions. However, this reception does not relate to a displayed certificate as all three segments struggled to relate to the 'social proof' context. Few could see any benefit from promoting the fact that they are a 'reputable' business, other than those businesses previously mentioned that rely on an exceptional public image. Indeed many question payment of tax as a sign of reputability, either in their own business or others. However, this response is not entirely surprising given the difficulty of testing the impact of social proof in research of this nature (i.e. direct concept testing), as social proof operates at a subconscious level.

---

## Motivating SME Compliance

### Executive summary of main findings

Engendering attitudinal and behavioural change in small business owners with regard to tax compliance has been the core objective for this project from the outset. Whilst this objective is clearly ambitious in its scale it has been built from the understanding that any real change amongst this audience can only be achieved when the relationship between compliance attitudes and behaviours is considered.

For this reason the project began with a holistic approach, building a greater understanding of SME 'environment' – the myriad influences that inform how SMEs think, and behave. This enabled the research to then focus less on stated improvements to what exists today and more on deriving new opportunities based on the realities of the tax landscape for small businesses. This approach yielded a number of fertile territories for the development of new HMRC tools, communications and initiatives designed to remove barriers to SME compliance, and these were considered worthy of development, refinement and consideration.

The more immediate opportunities identified were in improving tax as an *experience* for SMEs as well as developing new *tools and resources* to facilitate compliance. These include:

1. Helping SMEs embed new habits and practices internally
2. Creating a rhythm for tax that echoes the natural cycles that exist inside SMEs
3. Helping SMEs reconnect with tax by emphasising relevance
4. Redefining and reinforcing the quid pro quo of paying tax in the mind of the SME

At this stage it was clear that in order for the opportunities that sit behind these fertile territories to be better understood and for HMRC to begin to be able to integrate and leverage them with SMEs they would need to be tested as propositions. The opportunities were thus developed, through workshop sessions, into a suite of ideas that could be tested with the SME audience not only to evaluate the merit of the ideas themselves but to better understand the potential of the territories that sit behind them. As standalone offerings the research has identified a number of ideas that may present significant potential for engendering both behavioural and to some extent attitudinal change in SMEs including:

- A Tax ISA - a saving account specifically designed to help small businesses save for their tax bill
- A ready reckoner – an online calculator that could allow SMEs to make regular estimates for their end of year payment
- A personalised online tax account – which could hold all of their tax information as well as tailored support resources

These ideas stand out specifically amongst those tested because they hold an obvious attraction for SMEs and overcome some of the fundamental behavioural barriers that the research has uncovered. These ideas also hold potential as initiatives that can complement each other to have even greater impact.

However, whilst it is felt that these products have significant potential to have a positive impact on SME compliance on their own, the research also uncovered some more fundamental attitudinal issues, which these products have limited capacity to influence. Over the course of the project, the furore over MP's expenses exploded across the media and became front of mind for the non-political classes. This episode had profound implications for another theme emerging from this study: that the small business owner's inclination or disinclination to pay the right amount of tax at the right time is influenced as much by what they see around them as their own principles around the rights and wrongs of paying tax.

The concept of social proof is not new, but it was felt that if exploited in the right way, it could be a very powerful lever in encouraging SME compliance. Used effectively, social proof can stimulate a person's compliance with a request by informing him or her that many other individuals, perhaps some that are role models display this behaviour. Further, this concept is particularly relevant where people are unsure of what to do and their situation is ambiguous (as amply evidenced in SMEs' behaviours around tax); in these cases,

---

## Motivating SME Compliance

they are more likely to observe the behaviour of others and to accept that behaviour as correct. The existing social proof created by the alleged fraud of MPs, creates the wrong sort of social proof for SMEs with regard to adherence to the spirit and letter of tax law. In many ways, this increases the opportunity and potential impact for this lever even further.

Furthermore, the research highlighted a marked absence in SMEs' level of *positive* commitment to paying tax. Commitment is inextricably linked with consistency, a core component of sustainable compliance. Today, many SMEs are driven by fear – complying reluctantly is a common theme. The opportunity to encourage *ongoing* positive compliance through allowing SMEs to make a commitment to desired tax behaviours was thought to be potentially very powerful.

However, leveraging 'social proof' and 'commitment and consistency' within the department is challenging. Having tried and tested a number of ideas as part of this research which were designed to leverage these territories, it is clear that these levers will require a more robust approach. Whilst negative examples of social proof remain the dominant influence over public consciousness, SMEs can struggle to identify being 'compliant' as something to be proud of or that others should or could be interested in.

The first step in the process would therefore need to be focussed on building momentum and pride around paying tax, counteracting the high profile influence of evaders. One method by which the research suggests that this may be achieved is by building up social consciousness through a marketing communications campaign, which then sets up a more robust social expectation to pay taxes. A marketing campaign could then be potentially used as a mechanism to begin to build on the principles of social proof. By encouraging SMES to show support to a campaign (e.g. a kind of 'tax matters' campaign) in a public way the theory suggests that others are more likely to follow suit. Online campaign groups are a good example of the way in which this can work where individuals are influenced by the social proof of others signing up and are encouraged to make a public commitment to achieve objectives related to the cause.

Given the nature of these levers involve subconscious responses, there are many factors that present significant challenges for traditional proposition testing; it is possible that the true potential of these levers may only be understood by taking a 'leap of faith' and piloting them.

Finally, throughout this project we learned much about what works and doesn't work when attempting to nudge SMEs towards more positive compliance behaviours. These have been distilled into eight 'design principles' which can be used by HMRC teams who are planning and designing the future for SMEs in HMRC.