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CONTENTS

- 155 The Effect of the Human Rights Act 1998 on Taxation Policy and Administration
Natalie Lee
- 183 Towards Community Ownership of the Tax System: The taxation Ombudsman's perspective
Philip Moss
- 192 Trusts and Double Taxation Agreements
John Prebble
- 210 Tax Reform in the China Context: The corporate tax unit & Chinese enterprise
Nolan Sharkey
- 226 **Perceptions of Tax Evasion as a Crime**
Stewart Karlinsky, Hughlene Burton and Cindy Blanthorne
- 241 Globalisation, Innovation and Information Sharing in Tax Systems: The Australian experience of the diffusion and adoption of electronic lodgement
Liane Turner and Christina Apelt

Perceptions of Tax Evasion as a Crime

Stewart Karlinsky*, Hughlene Burton†, Cindy Blanthorne‡

Abstract

This paper considers on aspect of the deficit faced by the U. S. economy. It considers the contribution to this deficit made by the taxpayers that do not fully report taxable income and/or do not pay taxes on their income. The gap between what is owed in tax and the amount of tax actually paid is estimated at \$310 billion. What portion can be attributed to underreporting and non filing? The study reported in this paper attempted to measure the perceptions of US citizens as to the seriousness of tax evasions relative to other crimes and violations. The results show that tax evasion ranked 11th among the twenty-one offences surveyed. This means that the average person views tax evasion as only somewhat serious. Compared to other white collar crimes it ranked below accounting fraud, violation of child labour laws and insider trading, and equal to welfare fraud and higher than violation of minimum wage laws.

INTRODUCTION

Today the U. S. economy faces the largest deficit in its history. There are many factors that contribute to this problem. One of those factors is the vast number of taxpayers that do not fully report taxable income and/or do not pay taxes on their income. The difference between the amount of tax that is theoretically owed versus the amount of tax actually paid is called the ‘tax gap’. The Internal Revenue Service (IRS) estimated that the tax gap was \$95 billion in 1992 and \$275 billion in 1998 (IRS, 1996, 2002). More recently, the National Taxpayer Advocate, Nina Olson suggested that the single largest part of the estimated \$310 billion tax gap is attributable to self-employed non-compliance (Tax Notes, 2004).

Although filing a tax return is “voluntary”, it is against the law to underreport your income to the IRS. Yet, in a recent field study (Karlinsky and Bankman, 2002), researchers noted that small business owners were remarkably open and honest about their tax evasion behaviour relative to the non-reporting of cash income. One potential reason for this openness is that taxpayers may view tax evasion as a relatively minor offence. Obviously, the public’s perception of the severity of a crime has important implications for society. As discussed in Roberts and Stalans (1997), the government and its judges have an interest in how societal members perceive the seriousness of offences. First, in order to secure compliance with the law, the public must believe that the laws are legitimate (Robinson and Darley, 1995). Also, punishment that exceeds public perception of the severity of an offence may lead to Constitutional issues under the cruel and unusual punishment provisions of the Eighth Amendment (Finkel, Maloney, 1995). It is also helpful for public prosecutors to use public perception of an offence’s severity to allocate scarce resources (Miethe, 1984).

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This study was designed to measure the perceptions of U.S. citizens as to the severity of tax evasion relative to other offences (crimes and violations). If tax evasion is not viewed as a serious offence, it may somewhat explain the degree of non-compliance with the tax laws. The current study investigated people's perceptions of the severity of tax evasion as a crime when compared to twenty other offences. The results of the study show that tax evasion ranked 11th among the twenty-one offences surveyed. The results indicate that the average person views tax evasion as only somewhat serious. When compared to similar white collar crimes it ranked less severe than accounting fraud, violation of child labour laws and insider trading, while it was ranked equal to welfare fraud and higher than violation of minimum wage laws. The results of this study are important as they emphasize the fact that people do not perceive tax evasion as a serious crime. This perception plus lack of enforcements efforts¹ has led to an environment where some people may not be afraid of cheating on their tax return. The study also tries to observe if there is a correlation between the relative severity of a crime by whether a victim is involved or not.

LITERATURE REVIEW

There are numerous studies on the severity of crimes in the U.S. and international criminal justice, sociology and psychology literature, but very few in the accounting and tax literature.

Rosenmerkel (2001) found that people rate white collar crimes², such as tax evasion, to be less serious than other types of crimes. In the current study people's perception of the seriousness of white collar crime was examined by including insider trading, tax evasion and accounting fraud as factors in the study. Given the charged atmosphere in the press and in Congress in light of Enron, WorldCom, Tyco and corporate tax shelters, it may be interesting to see if the wrongfulness of white collar crimes will be perceived differently today.

Another study that looked at people's perception of crimes was performed by the Australian Institute of Criminology (1986). This study had people rank the seriousness of 13 different offences. Stealing a bicycle was used as the benchmark offence and the subjects were asked to evaluate how many times more serious was a particular crime. The authors gave a one line scenario for each of the offences like "A person stabs a victim to death" or "A person illegally receives social security cheques worth \$1,000". In this study, murder was viewed as 27 times more serious than stealing a bicycle. Tax evasion was viewed as roughly 6 times more serious than stealing a bike, and was rated about the same as Medicare fraud, but less serious than social security fraud (which was 7.5 times more serious than bicycle theft). Interestingly, the social security fraud scenario involved \$1,000 and yet it was viewed as more serious than a \$5,000 evasion on either their income taxes or excess Medicare receipts by doctors. The Australian Institute noted that the top 7 offences were found to be crimes involving a victim. The current study updates and expands on this study.

¹ The IRS estimates that the audit rate for all taxpayers is less than 1 percent. This rate has decreased from 1.37% in 1996 to .48% in 2002 (IRS, 2003).

² Unfortunately, his categorizing of white collar crime, such as overcharging for automotive repairs or overcharging for credit when selling goods, is very different than in the current study and therefore, there is no pre-Enron benchmark to compare the results to.

The perceived seriousness of crimes may be measured across countries and cultures³. IVCS Survey polled individuals in 17 countries (including Australia, England, Netherlands, Sweden, Canada, USA, France, Japan and Switzerland) and found that Unrecovered Car Thefts was the most serious offence of those crimes surveyed followed by sexual assault, recovered car thefts and then robbery involving a weapon. The least serious crime was bicycle theft. We included several of these offences in our survey instrument, namely carjacking, robbery and bicycle theft.

In a February 2001 Criminal Intelligence Service Alberta telephone interview study⁴ examined 26 different crimes (but no violations) of which seven (7) overlapped with the current study's focus. Using a 10 point scale (10 being the most serious) the interviewees were asked to rate the seriousness of various crimes. Sexual exploitation of children was ranked the most serious crime (9.53) with murder being slightly less serious (9.39) followed by robbery (8.66). Interestingly, prostitution was viewed as more serious (7.38) than car theft (6.92) or insider trading (6.61). Demographic factors solicited were gender, marital status and age.

In one of the few studies that examined the perception of the seriousness of tax evasion, Song and Yarbrough (1978) investigated taxpayers' perceptions of tax ethics in a small rural university town in North Carolina⁵. As part of their survey, they asked the subjects to measure tax evasion against eight other crimes (four of which were violent crimes and four were property related crimes). The result of their survey was that people viewed tax evasion more like a violation than a crime⁶. Almost 50% of respondents felt that tax violators should be fined but not punished with jail time. When tax fraud was compared with four violent crimes, it was ranked a distant fifth. Compared to property related crimes, tax evasion was ranked slightly higher in perceived seriousness than stealing a bicycle and lower than bribery, embezzlement and arson.

The current study extends Song and Yarborough (1978) by investigating current societal perceptions of the seriousness of a crime. First, our study uses a richer litany of offences by examining 20 other crimes and violations (besides tax evasion), and includes some offences that involve victims and others that are victimless (see survey instrument in Appendix A). Second, the Song and Yarborough (1978) study was performed a generation ago and perceptions may have changed in the interim, especially given Enron, WorldCom, Tyco, and the publicity of corporate tax shelters. Also the current study uses subject from both North Carolina and California urban and suburban communities.⁷

Song and Yarbrough (1978) also looked at various demographics to see if there is any correlation between a subject's characteristic and tax ethics. We have included in our study many of the demographics that they (and other studies) utilized including gender, income level, home ownership, political affiliation, and marital status. Because the focus of the current study is tax evasion, respondents were also asked if

³ see, *Criminal Victimization in Seventeen Industrialised Countries*

⁴ *Provincial Public Opinion Survey on Organized Crime: Alberta Canada*

⁵ The town's population was 34,000 in 1975 when the study was conducted.

⁶ A violation is an offence that is usually punishable by a fine while a crime is an offence that is punishable with a jail sentence.

⁷ The subjects were principally drawn from the California Bay Area including San Jose which is the country's 11th largest city and from the Charlotte, NC region which is the country's 35th largest city.

they prepared their own tax returns and/or if they had ever been audited by the IRS. This study also extends the work of Song and Yarborough (1978) by examining the relative perceived severity of white collar offences such as insider trading, accounting fraud and tax evasion. Another study (Eicher 2002), tested peoples' perception of various crimes, including cheating on their tax return, focusing on potential difference between men and women respondents. When asked "How much, if any, do you think is an acceptable amount to cheat on your income taxes?", roughly 1/3 of both the male and female subjects responded that they cheated a little here or there. 18% of men and 9% of the women said as much as possible, while 49% of men and 59% of women said it is not at all acceptable to cheat on your income taxes. The study found that overstating tax deductions was acceptable to 44% of the males and 36% of the females.

The Eicher study also examined six behaviours of which five have the roughly equivalent offence in our study (speeding, tax cheating, DUI, running a red light, shoplifting). The study found that driving 10 miles over the speed limit was somewhat or very acceptable for 82% of women and 78% of men. Overstating tax deductions was somewhat or very acceptable to 44% of the males and 36% of the females. Shop lifting was viewed as not at all acceptable by 44% of men and 54% of women. This is to be compared with running a red light which 51% of men and 57% of women said should not be at all acceptable. DUI was viewed by 83% of the females and 67% of the male subjects as not at all acceptable behaviour. In effect, this study found that DUI was by far the most serious offence, running a red light was the second most serious offence, with tax cheating and shoplifting being almost equivalent offences, followed by speeding which was viewed by both men and women as the least offensive (with only 22% of men and 18% of women viewed driving at 10 miles over the speed limit as not too acceptable or not at all acceptable).

Based on the previous studies it appears that people do not view tax evasion as a serious offence. However, all of the prior work was performed pre-Enron and contained a very limited number of offences, especially with regards to white collar offences. The current study adds to the body of knowledge because it extends the research to a post-Enron time frame and expands the number of offences examined.

METHODOLOGY

Survey Instrument

A four page survey was administered. The survey took the subjects less than ten minutes to complete (see Appendix A). The first page explained that the participant's identity would be kept anonymous to encourage a frank and candid response to the survey instrument. Since respondents were being asked for their personal perceptions, the survey emphasized that there was no right or wrong answer. The perceived severity of each offence was rated on a five-point Likert scale ranging from Not Serious (1) to Extremely Serious(5)⁸.

In the survey instrument, Q.2 asked if the person had trouble understanding any of the offences listed. Only four people (out of over 360 subjects) responded to Q.2. Two comments were that they did not know the degree of the offence. For example, was

⁸ To control for any order effect, there were five randomised versions of the test instrument used. Tests showed there was no order effect in the results.

the Speeding at a safe speed or out of control. One subject did not know what jaywalking was and left it blank, and another person did not know what DUI/DWI was and left that factor blank.

In exit interviews with several people, we were complimented for the simplicity of the test instrument. Comments like 'it was easy to use', 'it was quick and simple' and 'other surveys should take lessons from this instrument' were expressed by test subjects.

Sample

The sample included surveys from 364 respondents. The respondents came primarily from California and North Carolina. The sample was made up of 144 from California and 202 from North Carolina. Fifty-eight percent of the sample was male.

RESULTS OF THE SURVEY

Table 1 shows the overall rating of all 21 offences. The rating is the average of all response in the survey. The most serious offences rated by the sample were not surprisingly, Murder, Rape and Child Molestation, while Jaywalking, Illegal Parking and Ticket Scalping were rated as the least serious offences. The average rating for tax evasion was 3.3, which was the eleventh most serious or least serious offence in the survey depending upon your point of view.

TABLE 1: AVERAGE SCORES OF CRIMES SURVEYED

Crime	Overall rating	Ranking
Murder	5.0	1
Rape	4.9	2
Child Molestation	4.8	3
Robbery	4.0	4
DWI	3.9	5
Carjacking	3.8	6
Child Labour	3.8	7
Accounting Fraud	3.7	8
Insider Trading	3.3	9
Welfare Fraud	3.3	10
Tax Evasion	3.3	11
Minimum Wage	3.3	12
Shoplifting	2.8	13
Prostitution	2.8	14
Running a Red Light	2.6	15
Bike Theft	2.3	16
Smoking Marijuana	2.3	17
Speeding	2.1	18
Ticket Scalping	1.8	19
Illegal Parking	1.5	20
Jaywalking	1.3	21

The average rating for tax evasion (3.3) was compared to the three violent crimes in the survey, Murder, Rape and Child Molestation (4.9). Based on a t-test, the difference between the rating for tax evasion and violent crimes was significant at a .01 level (See Table 2). These results support the findings of both Rosenmerkel

(2001) and Warr (1989) that white collar offences were rated as less serious than violent offences.

In previous studies white-collar offences as a whole have been compared to violent offences or to property offences. The prior studies have not broken white-collar offences out to various types. In our survey there are six white-collar offences: tax evasion, accounting fraud, violation of child labour laws, insider trading, violation of welfare laws and violation of minimum wage laws. The ranking of tax evasion was compared to the rankings for the other five white collar offences in the survey. Based on the results of the paired t-tests, there was a significant difference in peoples' perception of the seriousness of tax evasion and accounting fraud and violation of child labour laws, but there was no difference between tax evasion and insider trading, violation of welfare laws or the violation of minimum wage laws (See Table 2).

TABLE 2: COMPARISON OF TAX EVASION TO OTHER CRIMES

Tax evasion	Violent crimes	Accounting fraud	Violation of child labour laws	Insider trading	Violation of welfare laws	Violation of minimum wage laws
3.3	4.9*	3.7*	3.8*	3.3	3.3	3.3

* Significant at the .01 level

Of the six white collar offences, violation of child labour laws and accounting fraud were rated as the most serious. However, the rankings of all six white collar offences fall together in the list, ranking from the six most serious offence to the twelfth most serious offence in our survey. These results support prior research that suggests people do not perceive white collar offences to be as serious as violent offences but more serious than most property offences⁹ (Warr, 1989). The significant difference between tax evasion and accounting fraud may be a product of the current business environment and the related press coverage surrounding the Enron, Worldcom, and Tyco scandals and the subsequent Sarbanes-Oxley legislation.

Ball (2001) found that citizens in different communities had different opinions as to the seriousness of a crime. In addition, Davis (1990) and Smith and Huff (1982) found a difference in the perception of crime between urban residents and their rural counterparts. However, Weisheit, Falcone and Wells (1996, 1994) did not find a clear difference between urban and rural perceptions. In fact, their 1996 study suggests that any difference between urban and rural perceptions appear to be decreasing. The typical definition of rural is low density population or small size, but rural can also relate to the type of economy, the character of social life, cultural attitudes, beliefs and values of an area (Weisheit, et al., 1996). Our survey includes respondents from the San Jose area of California, a very progressive and liberal area of the United States and from the area surrounding Charlotte, North Carolina, a more conservative part of the country. The perception of the seriousness of tax evasion was compared based on where the respondent lived (See Table 3). The results showed that respondents in

⁹ Robbery and carjacking are property offences that have historically been viewed as more serious in nature which is consistent with our findings. On the other hand shoplifting and bike theft are property crimes that have been perceived as low on the severity scale.

North Carolina rated tax evasion as more serious than those in California. Based on the t-statistic, this difference was significant at the .01 level; thus, supporting prior research (Ball 2001; Davis, 1990; and Smith and Huff, 1982) that location makes a difference in people's perceptions of crimes.

TABLE 3: PERCEPTION OF TAX EVASION BASED ON LOCATION

	California	North Carolina
Total Sample	3.2	3.4*

* Significant at the .01 level

VICTIM VS. VICTIMLESS OFFENCE ANALYSIS

From the law literature, we note that there is a need to differentiate between violations and crimes. The latter is an offence that warrants going through the entire criminal justice system (including arrest, processing, arraignment and trial, etc.). Violations, on the other hand, are punished with a summons, ticket or sometimes just a warning. The literature is replete with findings that people would classify violations as less serious than crimes, and those offences that involve people are viewed as more severe than those involving property. The current study included four of the Big Seven crimes (murder, rape, robbery and grand larceny auto, but excluded felony assault, burglary and grand larceny)¹⁰. These are crimes that police stations track on a regular basis.

We will use the current study to investigate people's perceptions of the severity of victim vs. victimless crimes and violations by including at least three offences in each of four standard categories: crime/victim, crime/victimless, violation/victim, violation/victimless. The crime/victim class would clearly include murder, rape and child molestation. The crime/victimless category would include tax evasion, prostitution or welfare fraud. By victimless we mean that no one else was involuntarily involved in the offence. For example, prostitution or ticket scalping involves two people, but both participants are voluntary. A violation/victim includes insider trading, violating minimum wages laws or violating child labour laws. A victimless violation would include speeding jaywalking, or ticket scalping.

As can be seen from Table 4, with two exceptions (shoplifting and bike theft), crimes involving victims were perceived as more severe than crimes without victims. The two exceptions are likely due to the perceived low nominal dollar value involved in the theft. In effect, its wrongfulness is high but its harmfulness is minimal.

When you compare perceived severity of violations, every victim violation is rated significantly higher than a victimless violation.

¹⁰ The reason that three of the big seven were excluded is that it was felt that it may be difficult for the general population (as opposed to a law enforcement agent or an attorney) to understand the fine distinction between burglary, grand larceny and robbery, and to understand what a felony assault is.

TABLE 4: RELATIVE SEVERITY OF VICTIM/VICTIMLESS OFFENCES

Crime/Victim		Crime/Victimless	
Murder	5.0	DWI	3.9
Rape	4.9	Welfare Fraud	3.3
Child Molestation	4.8	Tax Evasion	3.3
Robbery	4.0	Prostitution	2.8
Carjacking	3.8	Smoking Marijuana	2.3
Accounting Fraud	3.7		
Shoplifting	2.8		
Bike Theft	2.3		
Violation/Victim		Violation/Victimless	
Child Labour Law	3.8	Running a Red Light	2.6
Minimum Wage	3.3	Speeding	2.1
Insider Trading	3.3	Ticket Scalping	1.8
		Illegal Parking	1.5
		Jay Walking	1.3

DEMOGRAPHICS

Following Song and Yarbrough (1978) we included demographic variables in our survey to see if there was a correlation between a respondent's characteristics and tax ethics. Based on our tests there was no significant difference in the average scores for the seriousness of tax evasion between males and females, Democrats and Republicans, churchgoers and non-churchgoers or those that had their tax returns professionally prepared versus those that prepared their returns personally.

LIMITATIONS

There are two primary criticisms about this type of survey. First, critics may argue that the scales do not explicitly define what is meant by the term seriousness (Blum-West, 1985). Sherman and Dowdle (1974) determined that there would be a consensus among respondents in studies that were vague as to the definition of the term seriousness. However, when respondents apply their own concepts of criminal harm, they base judgments on a varying scale of crime importance. Rossi and Henry (1980) found that more variation would occur if respondents were instructed to rate seriousness based on their own opinions. To control for this problem, respondents in the current survey were asked to rate the seriousness of crimes based on their own opinions and experiences, which should provide variation in the respondents' answers.

A second criticism of the type of scale used in this study is the reliance on samples of offences that are not representative of everyday crime. Too few offence types have been included in prior studies to permit generalizing the findings to all offences (Rosenmerkel, 2001). Most crime seriousness studies over represent serious, violent criminal acts (Rosenmerkel, 2001). For example, more than 90% of all crimes are property crimes (Meier and Short, 1982). Over representation of serious crimes has the potential to sensitise respondents to the crimes that are most uncommon (Meier & Short, 1982). The current study included 21 offences, only three of which would be

classified as violent criminal acts. Of the remaining 18 crimes there are five property crimes, six white-collar crimes, three motor vehicle offences and four other types of crime

CONCLUSION

It is important to understand why people do not report taxable income and/or pay their income taxes. Prior research indicates that one reason may be that they do not perceive tax evasion to be a serious crime. Our study surveyed 364 people to see how serious they perceived tax evasion to be. We found that in a list of twenty-one crimes, tax evasion was ranked 11th and rated only as somewhat serious. We also found that tax evasion was considered to be less serious than the white collar crimes of accounting fraud and violation of child labour laws. We also tested to see what characteristics correlated with tax ethics and found that where the respondent lived made a difference on how serious a crime tax evasion was considered but other characteristics tested did not. We also confirmed that offences involving victims are perceived as more serious than victimless crimes. This would lead to the tax policy concept that if the tax evasion crime could be personalized more, then the perception of its severity might be increased with a concomitant higher tax compliance rate.

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APPENDIX A

Survey Document

We are three professors doing a study on people's perceptions of the seriousness of selected offences. Thank you in advance for taking five or ten minutes out of your busy schedule to share your opinions with us.

Since we are only interested in your opinion, there are no right or wrong answers. So, please just tell us how you honestly feel about each offence. Please note that your responses are totally anonymous.

To make full use of your responses, we need you to answer all opinion and background questions.

Thank you,

Cindy Blanthorne
UNC Charlotte

Hughlene Burton
UNC Charlotte

Stewart Karlinsky
San Jose State University

1. In your opinion, how serious is each offence listed below?

Item	Description of offence	Not serious	Somewhat serious	Serious	Very serious	Extremely serious
1	Bicycle theft					
2	Welfare fraud					
3	Speeding					
4	Carjacking					
5	Prostitution					
6	Accounting fraud					
7	Robbery					
8	Shop-lifting					
9	DWI / DUI					
10	Illegal parking					
11	Violating child labour laws					
12	Smoking marijuana					
13	Child molestation					
14	Insider stock trading					
15	Jay walking					
16	Running a red light					
17	Murder					
18	Ticket scalping					
19	Tax evasion					
20	Paying employees less than minimum wage					
21	Rape					

2. If you had trouble understanding any of the offences listed, please identify the problems (by item number or description of offence) and briefly explain the problem.
3. Please rank the five *most* serious offences (list the most serious offence first).

Seriousness	Item Number or Description
<i>Most</i> serious offence	
Second <i>most</i> serious offence	
Third <i>most</i> serious offence	
Fourth <i>most</i> serious offence	
Fifth <i>most</i> serious offence	

4. Please rank five *least* serious offences (list the least serious offence first).

Seriousness....	Item number or description
Least serious offence	
Second least serious offence	
Third least serious offence	
Fourth least serious offence	
Fifth least serious offence	

Participant Background Information

Our goal is to identify trends among different people. To do this, we need some anonymous background information.

5. What is your primary employment status?

- self employed student retired
-employee not currently working

6. What is the highest level of education that you have completed?

-some high school some college graduate degree
-high school college degree

7. What is your political affiliation?

-Republican Independent None
-Democrat Other

8. What is your household income level?

-<< \$20K \$41 – 60K >> \$80K
-\$20 – 40K \$61 – 80K

9. What is your age range?

-<< 20 years 31 – 40 years >>60
-20 – 30 years 41 – 60 years

10. Is English you first language? Yes No

11. Do you own your own home? Yes No

- | | | |
|---|------------|--------------|
| 12. Are you married? |Yes |No |
| 13. Do you attend church regularly
(at least once a month)? |Yes |No |
| 14. Do you hire someone to prepare
your income tax return? |Yes |No |
| 15. Are you a tax professional
(tax preparer, IRS agent, etc.) |Yes |No |
| 16. Has your income tax return been
audited (by IRS or state)? |Yes |No |
| 17. Have you or someone close to you had
personal experience
with any of the offences listed? |Yes |No |
| 18. Are you male or female? | Male | Female |
| 19. Please indicate the state in which you live? | | |

THANK YOU. Your contribution is greatly appreciated!