Voluntary Tax Compliance and the Slippery Slope Framework

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ARTICLE DETAILS

ABSTRACT

Purpose__ The research provides an insight in to the most popular debate around the globe about tax compliance. The research focusses on SMEs in premises of Bahawalpur division, Pakistan, by proposing a reliable solution for interstitial gaps existing between tax authorities and compliance behavior of taxpayers. It expands the Fisher model of compliance (1992) and deploys it as a base by adding new variables namely Power of authority, Tax audit and Electronic filing. The data has been statistically analyzed by using SPSS through running test of correlation and regression. Positive correlation and causation were established among variable leads to analysis of data through Ordinary Least Square (OLS), which ratify the role of attitude and perception as moderator in overall relationship. Results show that Power of authority directly influence compliance behavior while other two variables indirectly effects the relationship through moderator, thus nurturing the voluntary behavior of taxpayer.

Design/Methodology/Approach___ A research framework has been developed for identifying the effect of different factors which may in boosting up compliance behavior of taxpayers. Quantitative approach was used and data has been collected through Questionnaire from almost 50 SMEs of Bahawalpur Division.

Implications___ Policy makers may use the findings of the study to encourage voluntary compliance from the non-tax paying SME. Further study can be expanded by increasing sample size and by gathering detailed information for tax authorities.

Originality/Value___ The proposed Model and findings may contribute in paving path for increasing voluntary compliance. Research also emphasize on other factors which should be focused for improvement and could play a crucial role in compliance.

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1. Introduction

Tax compliance has been never ending topic and in today's circumstances its importance cannot be denied.

1.1 Current position of Pakistan

After 1971, fiscal performance of Pakistan has not been satisfactory at any stage and has accumulated huge deficit budgets. Whilst non-compliance attitude is a global phenomenon, its ratio rises significantly in government and tax agencies. Pakistan continuously faces challenge of revenue from domestic growth (Khan & Ahmad, 2014). This problem is majorly due to smaller tax base, and weak administration tax avoidance practices by business class (Ahmed, Talpur, & Liaquat, 2015). Recent initiatives of the tax regime include offering huge incentives and workable solutions to SMEs by offering them 20% income tax as compare to 29% for bigger firms. Further announcing tax subsidy for next four years, with decrease of 1% every year up till 15% by 2023. 20% tax regime has been approved by Tax Reforms Implementation Committee (TRIC). In addition to this a 10% rebate is approved for those firms which are showing extraordinary growth in their first three years of operation under normal provisions (Pakistan Today, 2019).

1.2 Electronic filing initiative

Pakistan started its E-filing system (SAS) in 1979. Fenwick and Browstone (2002) debate that a country adopting for E-filing needs radical changes in their fundamental structure, operations, management of resources etc. Basic motive of every tax authority is to increase voluntary compliance behavior by reducing "tax and compliance gap" (Silvani, 1992).

1.3 Tax Statistics

According to survey of 2016, total number of people employed in Pakistan are 56.5 million in which only 3.6 million are registered for PIT. However, survey also indicates that there are almost 5.7 million people who report their threshold income above than 400,000. While companies registered for corporate income tax are 25,551 out of 60,000. Number of active CIT filer is only 0.8% of number of commercial and industrial users (Express tribune 14 Jan, 2016). Out of almost 65,000 companies registered with the Securities & Exchange Commission of Pakistan, round about 25,000 filed their taxes (38 percent of total). Out of these, 40 percent don't declare their profit.

In tax year 2016, indirect taxes constituted about 62 percent of the Federal Government's tax revenues. Such a heavy reliance on indirect taxes has given rise to a regressive tax system in Pakistan. World Bank Doing Business Survey of 2015 ranked Pakistan 171 out of 189 in ease of paying taxes, same ranking goes in 2016 as well. Adding to the burden on already existing complex system, segregation of powers between federal and provincial government has made situation more terrible.

1.4 History of SMEs in Pakistan

Fiscal regulation of SMEs started with foundation of Small Medium Enterprises Development Alliance (SMEDA) that is established under selected services of ventures. It helps SMEs to develop and progress on right track, guiding them to fulfill proper procedures and requirements of their respective field according to universal standards. It also has a workshop, training and a preparatory system that stresses out SMEs development all over Pakistan (Chugtai & Alam, 2014). In Pakistan SMEs are autonomous, independent firms employing people less than 250 or having their paid up capital of Rs. 25Million and sales about Rs.250 million per annum (Kureshi et al., 2009)..

1.5 Problem Statement

The issue to be address is "How government can increase voluntary tax compliance among individuals by transforming attitudes of tax payers? This study seeks to find a solution that is interstitial for the current problem.

1.6 Objective of Study

This research builds its inference on Fischer's model of compliance. The main objective of the study is to provide a balanced approach that can mold the attitude of tax payer towards compliance. Objectives can be summarized as
- Effect of using "power of authority" on compliance behaviour

- Filer trust on tax authorities
- Tax upgradation (software) effect on compliance attitude (E-filing).
- Tax Audit role in compliance

A strong tax system is likely to affect the behavior of taxpayers in Pakistan with the need to identify those factors which are working behind this perception building of taxpayers.

2. Brief Review of Literature
2.1 Tax compliance
The first study on economic side of compliance and evasion was done by (Allingham & Sandmo 1972), followed by (Srinivasan 1973) and (Yitzhaki 1974). This is also referred to as "economics of crime" which is a gambler position, choosing between compliance and evasion, and in other words between legal and criminal activity (Alm, Cherry, Jones, & McKee, 2010; Christian & Alm, 2014; Casagrande, Cagno, Pandimiglio, & Spallone, 2015; Castro & Scartascini, 2015).

The extent to which taxpayers are complying with laws is called tax compliance behavior (James & Alley, 2004). Tax compliance refers to the degree of honesty which taxpayer possess in compiling their returns with sufficient knowledge and accuracy of all required documents (Singh & Bhupalan, 2001). Developing this habit of compliance is tough and a taxing taskn itself (James & Alley, 2004).\

Tax compliance could be broadly classified into two major approaches for understanding. The first one is economic and other is behavioral approach. Economic approach deals with penalties, while behavioral approach is based on awareness and environmental factors (Siti Musyarofah & Adi Purnomo, 2008). Many scholars define the affecting variables as economic, social and psychological factors (Brook, 2001; Kirchler, 2007; Devos, 2008). Tax compliance has been stated as a voluntary or enforced compliance, voluntary is only possible through trust and cooperation between both parties however in distrust and lack of cooperation creates a hostile climate which leads to enforced compliance through threat and fines (Kirchler, 2007).

Continuous communication and fairness in system has got direct and positive impact on voluntary compliance because it builds a level of trust among the two parties. Similarly, tax avoidance occurs due to lack of fairness and communication in the system (Siahaan, 2012). Higher complexity in system leads to higher compliance cost faced by tax authorities, and the correlation between complexity and compliance is significant, while at the same time fairness has got significant effect on compliance behavior (Brainyyah & Rusydi, 2013).

2.2 Tax Determinants
Tax determinants are factors which influence taxpayers to comply with tax laws. According to studies these determinants are broadly classified as social, economic, individual, demographical, behavioral, and institutional factors (Kirchlar 2007, Loo 2006, Palil, 2010, Palil & Mustapha, 2011). The major factors influencing compliance attitude of taxpayers include the inefficient tax officials and their rude abusive behavior which also affects the trust level (Job & Honaker, 2003; Job, Stout & Smith, 2007). Whenever a taxpayer pays his taxes, he tends to attach a sense of affiliation with the outcomes so the revenue generated by government from taxes should be spent in accordance with will of public and state should be accountable for it (Young et al., 2013). The lack of it may cause a hanging position for tax payers' commitment to pay taxes. When probability of detection increases, it causes a direct positive affect on compliance behavior (Aim, 1991).

2.3 Fisher's Model of Compliance
A comprehensive and detailed review of tax literature was carried out by Jackson & Milliron in 1986, who shortlisted 14 factors affecting compliance behavior and attitude of taxpayer. The summary of these factors was compiled by Fisher et al. 1992 into four major groups named (i) Demographics (ii) Noncompliance opportunity (iii) Attitudes and perceptions (iv) Tax system. The proposed model was named as Fisher model. Fisher model inculcates economic, sociological and psychological factors in one comprehensive model. Major construct in the Fischer model is tax rate. Evidence through empirical researches has indicated that progressive and flat tax rates have a significant effect on compliance behavior (Clotfelter, 1983).

2.4 Modification to Fischer Model
2.4.1 Slippery Slope Framework
Latest work on tax compliance includes the basic concept of tax morale and SSF (slippery slope framework). Slippery slope framework further explains compliance as voluntary or enforced which is influenced by trust on tax authorities and power exercised by tax authorities respectively (Frey & Torgler, 2007; Cummings, MartinezVazquez, McKee, & Torgler, 2009). Basic SSF consists of three main dimensions (i) trust in tax authorities, (ii) power of tax authorities, and (iii) tax compliance.

2.4.2 Technology and Media Role
Fairness is regarded as the most important factor in judging the criteria of tax system. The unfairness of tax system allows tax shift from dishonest to honest taxpayers (Brooks 2001). In order to solve this situation Indonesian government adopted a new system named self-assessment system (SAS) through this system tax payer is fully open to calculate, deposit and report all his taxable income, increasing overall obligations, and also increasing the trust level among taxpayers (Ratriana Dyiah Safri, 2013). Familiarity with tax system through E-taxation reduces the resistance from taxpayer and increases their compliance behavior (Schaupp, Carter, Mcbride, 2010: 641).

Electronic system is defined as a general method of doing transaction using electronic way. E-businesses provides a flawless interactive link between all stakeholders including all suppliers, and partners. This electronic way gives a sophisticated collaboration and activities at all level. (Papazoglou and Ribbers 2010: 2). The decision of filing returns through electronic means depends on many factors including knowledge of taxpayer, his attitude and general perception, his experience and surrounding (Coolidge and Yılmaz 2014:1). Taxpayers having large business, more capital intensive sector, multiple taxes are more likely to use E-filing, while in addition to aforesaid characteristics the knowledge of tax payments, computer familiarity, reliable internet are important in building compliance attitude (Coolidge and Yılmaz (2014: 2). Challenge faced during E-filing is complex structure of software and lack of proper guidance when asked for online assistance, website help desk are not capable for guiding them. Many people prefer to go for in-person tax professional for guiding them in proper way for filing their returns through E-filing. Same case was faced by SARS; it faces a lot of problems but draw maximum benefits out of it through amending their software from time to time (Dwilson 2014).

Research figured out the skills needed by fresh graduates in order to use E-filing system after completing their education are very much important for increasing compliance. The research also indicated that those students with sound knowledge and education are more compliant and have positive mindset for filing returns so the ICT skills needed for students got great importance (Lai Ming et al., 2010). The greatest flaw in system arises due to inexperienced taxpayers who have little information of using tax software while filing returns, this leads to over and under stating of their taxes which ends up with complications and negative consequences (Eining et al., 1997; Davis & Kotemann, 1994).

3. Research Methodology
3.1 Research Design
The data has been collected through adapted questionnaires from previous researchers (Mohd Rizal Palil 2010, Mutatembwa William 2013,Noor Sharoja Sapiei et. al. 2014, Sophia Naroog Kuug 2016, Kelvin Gitaru 2017). Random Sampling technique has been adopted for selection of almost 50 samples. Study is covering SMEs of only Bahawalpur division.

3.2 Research Instrument
Questionnaire adapted uses five point Likert scale. The data has been analyzing deeply through SPSS version 20. Different tests have been run for identifying and thoroughly analyzing the results of respondents.

A total of almost 130 questionnaires were send from which almost 50 SMEs give responses, overall response rate was almost 40%. This research is Quantitative plus qualitative in nature as the whole process is carried out through survey

by using questionnaire but the factors under study is behavioral in nature. Correlation and linear regression has been applied to test hypothesis. OLS method is applied for checking out moderator affect through Haye's approach.

3.3 Theoretical Model

Fisher model of compliance (1992) has been used as a base for developing the research framework. Its major factors were classified in four main categories naming as

- demographics,
- noncompliance opportunities,
- attitude and perception,
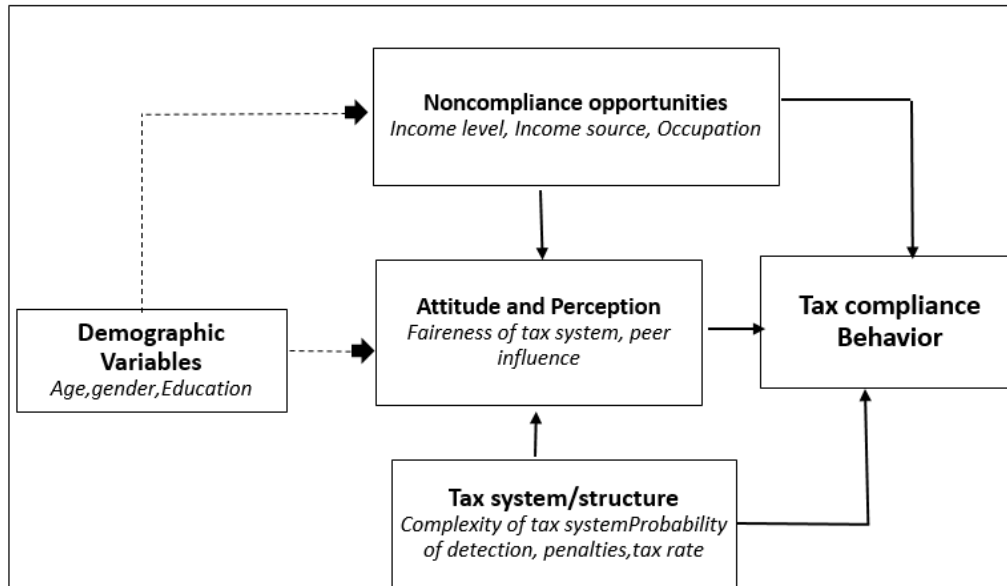- tax system and structure

The model has been presented below

Figure 3. 1: Fisher et al.(1992) tax compliance model

3.4 Modification to Fisher Model

In the proposed model modification, there are three additional variables that have been added, namely Tax Audit, Electronic Filing, and Power of Authority. The variable POA (Power of authority) is also related with trust level. A slippery slope framework has been developed in previous researches to check the influence of these two variables on compliance behavior.

A second model has also been developed for checking out the moderating role of these variables on compliance behavior. A cross check has been made focusing on tax structure effect on compliance behavior while attitude and perception factors are acting as moderator.

4. Research Framework and Data Analysis

The research framework has been developed by already existing fisher model by adding some variables in it
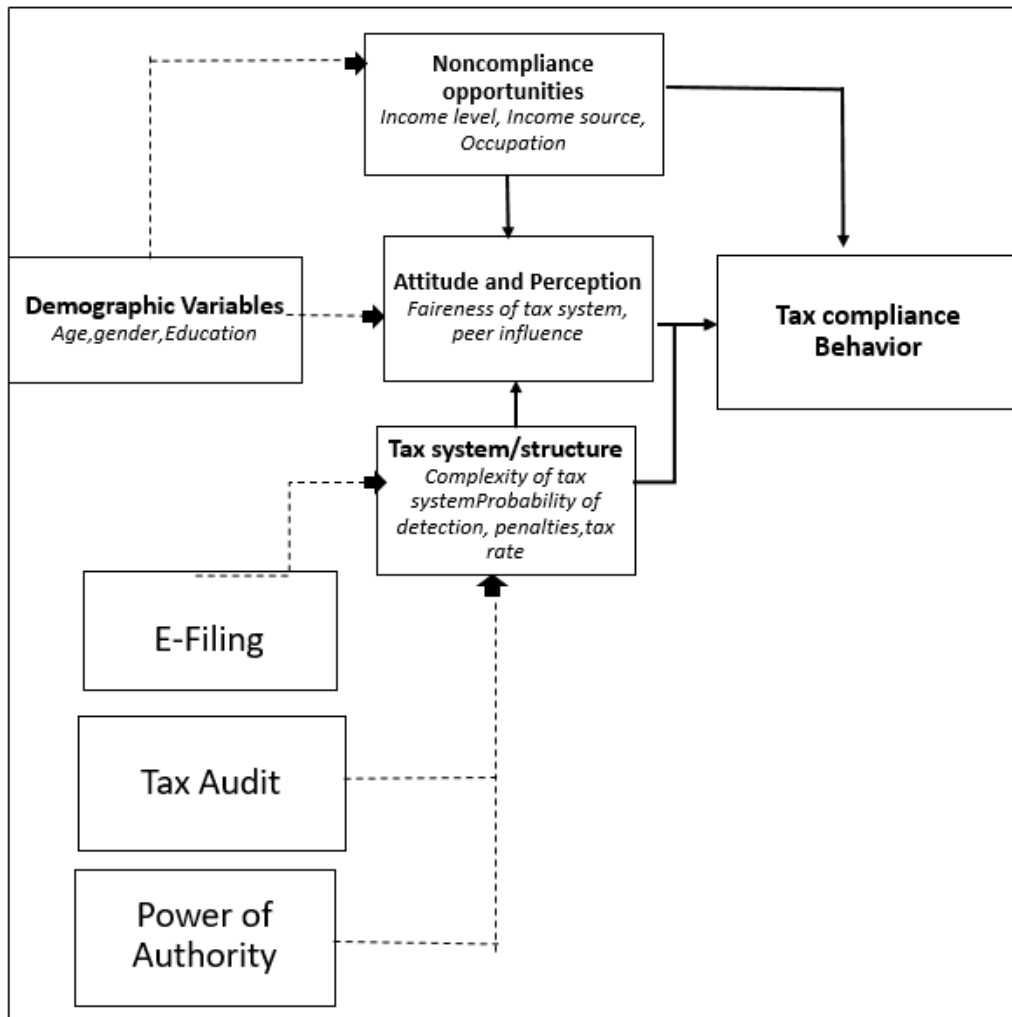
Figure 4.1: Modification in Fisher's tax compliance model
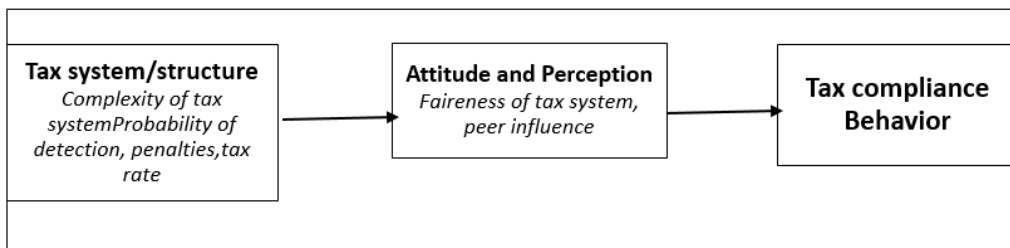
Figure 4.2: Moderating effect and its impact on compliance behavior

4.1 Descriptive Analysis

Descriptive analysis enables us to get mean, median, mode, standard deviation values. Beside this it also tells us about skewness and kurtosis of data.

Table 4. 1: Descriptive Statistics

	Mean	Standard Deviation	Skewness	Kurtosis
Demographics	2.10	0.42	0.98	-0.20
Compliance Behavior	2.59	0.32	-0.25	-0.35
Attitude and Perception	2.69	0.42	0.15	-0.41
Tax System and Structure	2.62	0.47	-0.01	-1.23

Non -compliance opportunity	2.33	0.45	-0.38	-0.56
Power of Authority	2.59	0.64	-0.75	-0.26
Tax Audit	2.80	0.46	0.07	-0.67
Electronic filing	2.62	0.35	0.63	0.33

The normal range for skewness is +1 to -1. In our current data demographics, attitude and perception, tax audit and electronic filing have value of positive skewness. Beside this demographics and electronic filing value is closer to 1 indicating a skewed and asymmetrical data. On other hand kurtosis tells us the length of peak. Its value lies between -1 to +1. In current data except electronic filing, all other variables are having negative value. The negative value of kurtosis indicates that tail side of distribution is lighter and has flattered peak.

4.2 Reliability Analysis
The reliability analysis is done for testing the data consistency and validation of instrument.

Table 4. 2: Reliability Statistics

Cronbach's Alpha	N of Items
.512	8

Cronbach alpha's value is 51%. Standard value of reliability is 70%. 51% value of Cronbach alpha value shows that our questionnaire is weak and it's not quite enough for depicting better results. At this point we have to check Item-Total Statistics.

Table 4. 3: Item-Total Statistics

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Cronbach's Alpha if Item Deleted
Compliance Behavior	0E-7	12.842	.051	.545
Attitude And Perception	0E-7	11.864	.196	.494
Tax System And Structure	0E-7	9.970	.517	.366
Noncompliance Opportunity	0E-7	10.346	.449	.395
Power Of Authority	0E-7	12.541	.094	.530
Tax Audit	0E-7	10.078	.498	.374
Electronic Filing	0E-7	11.265	.292	.458
Demographic	0E-7	13.992	-.107	.596

After going thoroughly from above data we can see that if we delete Ddmographic item from scale then it can increase overall reliability of data up to 60% which is quite acceptable.

Reliability Analysis Excluding Demographic

Table 4. 4: Reliability Statistics

Cronbach's Alpha	N of Items
.596	7

The value of 60% is quite acceptable in finance because as we are dealing with variable which are used for prediction of behavior so it's quite difficult to achieve a full reliable scale.

	Demographics	*Compliance Behavior*	*Attitude & Perception*	*Tax System & Structure*	*Non - compliance opportunity*	*Power of Authority*	*Tax Audit*	E-Filing
Demographics	1	-0.8						
Compliance Behavior	-0.88	1						
Attitude and Perception	0.64	-0.21	1					
Tax System and Structure	-0.38	0.26	0.31	1				
Non - compliance opportunity	-0.14	0.08	0.07	0.51	1			
Power of Authority	-0.11	0.15	-0.01	0.05	0.09	1		
Tax Audit	0.12	-0.09	0.37	0.30	0.42	0.10	1	
Electronic filing	-0.21	0.08	0.06	0.58	-0.82	-0.16	0.35	1

Table 4. 5: Correlation marix

4.3 Correlation Analysis

Correlation analysis is statistical analysis which measures the direction and strength of relation between two or more variables. Correlation value ranges between -1 to +1.

Table 4. 5: Correlations

Demographics which is having significant relationship with tax system and structure got value of -0.382 indicates that when your demographic conditions are better then you start avoiding the rule of tax system. Compliance behavior got negative relation with attitude/perception and tax audit, however that is not significant. It has got positive relation with rest of variable indicating a positive trend. Attitude and perception got significant relationship with tax system/structure and tax audit. Both these are positively correlated and have significant value While it has got weak positive correlation with noncompliance opportunity and electronic filing. Tax system and structure has got significant positive relationship with noncompliance opportunity, tax audit and electronic filing. Overall result indicates that improvement in tax system and structure positively affects the electronic system and noncompliance opportunity.

Power of authority is negatively correlated with electronic filing and positively related with tax audit.
Noncompliance Opportunity has got significant positive relation with tax audit.

Tax audit has significant positive relationship with electronic filing. This may mean that when one is more prone towards filing one's returns online then chances of being audited increase.

4.4 Regression

Table 4. 6: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.454[a]	.206	.084	.30904

a. Predictors: (Constant),Electronic Filing, Attitude And Perception, Power Of Authority, Noncompliance Opportunity, Tax Audit, Tax System And Structure

Our dependent variable is compliance behavior. While independent variables are electronic filing, attitude and perception, power of authority, noncompliance opportunity, tax audit and tax system/structure. Our independent data was so dispersed so in order to get a centralized and standardized value we have made a check on all independent variables and get Z-Score of them which will help us in better prediction. We have got R-Square value of 20%, this change is too small but it's quite acceptable because the variable we have chosen are mostly related with behaviors and its always complex and tricky task to predict behavior in quantitative terms.

Table 4. 7: Coefficients

Model		Standardized Coefficients Beta	Sig.
	(Constant)		.000
	Attitude And Perception	-.331	.060*
	Tax System And Structure	.499	.027*
1	Noncompliance Opportunity	-.100	.589
	Power Of Authority	.118	.436
	Tax Audit	-.055	.767
	Electronic Filing	-.119	.550

a. Dependent Variable: Compliance Behavior

The above table is showing separate effect of independent variables over dependent one. The beta value of table is showing the actual result.

We have seen that tax audit and electronic filing got negative effect on compliance behavior while power of authority has got positive affect on compliance leading to acceptance of our hypothesis. The significant effect of these two variables gives us an indication of moderating effect.

4.5 Regression Analysis Run Including Moderator
In order to analyze the role of moderator and its effect on dependent variable we will be running another test of regression using moderator. OLS test will help us in identifying the existence of any linear relationship between variables of interest.

4.5.1 Ordinary Least Square (OLS)
Basic purpose of running OLS is the we set one variable as a predictor of investigating effect of other variable. This can be simply explained as using one variable as an alternate of other. In variable terms it is known as "moderating

effect".

Table 4. 8: Model Summary

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.536[a]	.288	.237	.28204

a. Predictors: (Constant),Tax System And Structure, Attitude And Perception), Moderator1

Moderator is the product of Attitude/Perception and Tax system/Structure. By running this model, we got result indicating R-square change of approx. 29%. This is more than the previous analysis we did which was 20%. This means that in explaining the relationship between all independent variables and dependent moderator is playing significant role. Attitude/perception is a very good predictor of tax system/structure and is playing role of moderator. This moderator is directly giving effect on our final dependent variable i.e. compliance behavior.

Table 4. 9: Coefficients*

Model		Standardized Coefficients	Sig.
		Beta	
1	(Constant)		.000
	Moderator1	.401	.010
	Attitude And Perception	-.470	.003
	Tax System And Structure	.552	.001

* Dependent variable: Compliance behavior

This significance value is at confidence interval of 90%. Looking at it closely will reveal the inter related dependency. The tax system/structure (independent variable) is explaining 55% change in dependent variable (compliance behavior). Moderator which is Attitude and Perception is playing 40% role in explaining the change in dependent variable.

Our findings suggest that tax audit and electronic filing have significant positive relation with tax system/structure, concluding that these proposed variables are causing effect on tax structure which in turn acts as moderator for building attitude/perception of individual leading to voluntary compliance behavior.

5. Conclusion

The results of analysis indicate that along with the identified additions to Fisher's model and slippery slope framework, there may be many unknown factors contributing towards compliance behavior. The variables which we selected got low significant relationship with compliance behavior, however, the hypothesis relating to power of authority having positive relation with compliance behavior is accepted nevertheless. This indicates that when authorities choose to be strict, it will increase the compliance behavior. The other two proposed variables i.e. electronic filing and tax audit have visibly negative relation with compliance behavior. This may imply that if there

will be more penalties from audit and strict law and order implementation then overall compliance will decrease. Same inference goes for for electronic filing, where it increases the compliance level tends to decrease.

Beside this another factor that plays important role in boosting up overall compliance behavior is attitude and perception. This behavioral factor acts as a moderator between tax system and compliance behavior. Electronic filing is a component of tax system. When tax system will improve, this will lead to more voluntary compliance behavior. However, poorly managed tax system has a negative relationsip with compliance decision because complexity in

filing returns and complicated tax structure leads to irritation and noncompliance among individuals. Investing resources on tax system and amending it according to public demand can lead to increase in voluntary compliance.

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