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A Proposed Model of Non-compliance Behaviour on Excise Duty: A Moderating Effects of Tax Agents.

Perabavathi Sinnasamy^{a*}, Zainol Bidin^b, Syed Soffian Syed Ismail^c

^{a,b,c} School of Accountancy, Universiti Utara Malaysia, 06100 Sintok, Kedah, Malaysia,

Abstract

Taxation became a source of revenue in most of the developed and developing countries. However, tax non-compliance remains as a serious issue around the globe. The negative impact of tax non-compliance on economy and evolving nature of indirect tax in Malaysia have induced this study. The smuggling activities involved cigarettes, liquor and imported vehicles have caused a great loss to the tax revenue in Malaysia. Hence, this study attempts to propose conceptual framework by integrating tax agents as moderating effects between tax rate, penalty rate, tax fairness and peer influence with non-compliance on excise duty.

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1. Introduction

Taxation is always classified as a fundamental and crucial tool in managing national revenue especially in most of the developed and developing countries (Tabandeh, Jusoh, Nor, & Zaidi, 2013). Hence, tax is the most important means in financing government expenditures. In the economic perspective, tax is considered as an income redistribution mechanism from the rich to the poor apart from generating revenue for the public finance (Saez, 2004). Furthermore, taxes are also introduced to improve the health and safeguard the environment. For example, by introducing certain taxes called sin tax to cigarettes, it is expected that their usage will be reduced to encourage a healthier way of life and protect damage caused by cigarette smoke (Miskam, Noor, Omar, & Aziz, 2013).

* Corresponding author. Tel.: +6012-4901909.
E-mail address: mbsrpraba@yahoo.com

However, people are reluctant to pay taxes and thus cause problems for tax authority to collect and impose taxes anywhere and timely (Alm, Martinez-Vazquez, & Schneider, 2004). Taxpayers' failure to comply with the tax laws involves committing a non-compliance act (Kirchler, Muehlbacher, Kastlunger, & Wahl, 2007). In line with this, Franzoni (2008) mentioned non-compliance is a tax administrative most common and critical problem.

Tax non-compliance is a severe issue that exists globally including Malaysia (Hai & See, 2011a). Non-compliance signifies failing to meet tax declaration requirements or failure to engage tax responsibilities intentionally or unintentionally (Kinsey, 1988). Despite the escalating tax non-compliance problem in Malaysia, only a few studies have been conducted to examine the determinants of this phenomenon (Abdul-Jabbar, 2009). These studies mainly focused on income and corporate taxes behavior, excluding the studies by Tayib (1998) and Nor Aziah (2004) regarding the local government taxes. However, smuggling offences and customs tariff are not always highlighted by tax authority and researchers (Delipalla, 2009). Giles, Tedds, and Werkneh (2002) defined smuggling activities as all transactions whether legal or illegal, market or non-market done to evade taxes from the tax authority. The indirect taxes evasion often related to smuggling offences especially on customs tariffs. The smuggling offences affects monetary as well as non-monetary revenue such as embargo, product quality and quotas (Ayitey Stephens, Boddewyn, & Ross Sproul, 1991). Furthermore, only a few academic scholars have done research on non-compliance because of the difficulties faced, especially on measurement involving companies, individuals whether they are involved unintentionally or intentionally in tax payments (Hai & See, 2011b). Therefore, this study focuses on the phenomenon and the determinants of excise duty non-compliance among importers as taxpayers.

2. Literature Review

2.1 Tax Non-compliance

Tax authorities play fundamental roles in ensuring tax compliance among taxpayers by abiding tax rules and regulations. Despite the arrangements, the confrontation in human society still exist which causes the numerous cases of tax non-compliance. James and Alley (2002) described tax non-compliance as a failure of taxpayer to accommodate tax responsibilities whether they performed unintentionally or intentionally. Tax non-compliance treated as a contrary conduct or attitude of tax compliance. Tax non-compliance examples are tax evasion and tax avoidance which carries negative impacts on tax compliance and tax collections. Kasipillai, Aripin, and Amran (2003) anticipated tax evasion as a conduct caused to reduce the taxes owed in reality. Whereas, tax avoidance is described as taxpayers declaring their tax affairs creatively according to the rules and regulations to lower the tax liabilities and this action is legal in tax administrator's point of view.

In Customs context smuggling activities is one of the important determinant causing non-compliant. Smuggling activities consists of three types which are incorrectly declaring the amount, for instance declaring less quantity and price, incorrectly declaring the descriptions of goods and state at lesser than legally practiced (Cooper & Bhagwati, 1974). The popular smuggling methods and Customs frauds involves fake invoicing, complicated transactions attempts, using two invoices, the false invoices are used for declaration and the genuine invoices are used for record purposes, tariff code miss-classification, over stated and under stated valuation and shipments (Thanasegaran & Shanmugam, 2007). In Malaysia's context indirect taxes are avoided through falsifying the declaration, smuggling or Customs fraud (Miskam et al., 2013).

2.2 Excise Duties

Excise duty is one of the components in indirect taxes. The excise duty imposed to import into Malaysia and locally manufactured goods as stated in Section 6 of Excise Act 1976. This duty is used as a mechanism to alter the trend of public consumptions or social engineering (Delipalla, 2009). The commodities bound in Excise duty act includes liquor, tobacco, cigars, cigarettes, four wheel drive, multi-purpose vehicles and playing cards.

2.1 Tax rate

According to Fischer's model, tax rate is one of the factor influencing the tax non-compliance behavior. Prior studies investigated tax rate and tax compliance produced mixed results. For instance, if the marginal tax rate is increased the taxpayers' are likely to understate their tax returns (Skinner & Slemrod, 1985). This is what they referred to as higher tax rates caused the higher pressure of taxpayers' which motivates to non-compliance behaviour (Atawodi & Ojeka, 2012). Additionally, Mohd Yusof, Ming Ling, and Bee Wah (2014) reviewed tax non-compliance among small-and-medium sized corporations in Malaysia and identified that significant effect exist between marginal tax rate on corporate tax non-compliance. Under the Economic Deterrence theory, the increases in tax rate will decreases the compliance level (Allingham & Sandmo, 1972). According to Richardson (2006) through cross-national study identified tax rates have significant and negative relationship with tax compliance which implies higher tax rates will lower the taxpayers' compliance level. However, study done by Pommerehne, Hart, and Frey (1994) shows the positive relationship between marginal tax rate and tax evasion, increasing in marginal tax will increase tax evasion. Therefore, the proposed hypothesis for the current study is:

H1a: There is a relationship between tax rate with non-compliance of excise duty by importers.

It is equally important to be aware that the consultations given by the tax agents may also have moderating effect on the impact of the tax rate on non-compliance. According to Doyle, Hughes, and Glaister (2009) tax agents have significant influence in deciding the amount of the tax declared and paid by their clients. Hence, tax agent has strong effect on the tax rate and excise duty non-compliance (Sekaran, 2006). Therefore, the moderating effect hypothesis to tax agents between tax rate and non-compliance of current study is:

H1b: Tax agents will moderate the relationship between the tax rate with non-compliance of excise duty by importers.

2.2 Penalty rate

The taxpayers' detained under the audit and investigations process will be penalised by the tax authority. Penalty is correlated with punishment or sanctions. There are mixed findings on the impacts of penalties and tax non-compliance. A majority of the tax compliance prior academic scholars showed a significant association between penalties and tax compliance behavior (Maciejovsky, Schwarzenberger, & Kirchler, 2012). According to Devos (2013) there is a positive association of penalties and tax compliance. A study done by Slemrod (2004) indicates the penalty severity might deter the taxpayers from reporting accurate tax returns based on the tendency of profit is greater than the tendency for losing. This shows the negative relationship between the penalty rate and tax compliance. Therefore, the propose hypothesis is:

H2a: There is a relationship between penalty rate with non-compliance of excise duty by importers.

The tax declaration service provided by tax preparers, shows a conflict with the services that taxpayers' seek. Tax agents represent customers with hostile tax situation. While, taxpayers' hire tax agents to increase accuracy and avoid any penalties enforced by tax authorities (Stephenson, 2007). Therefore, the current study's hypothesis moderating effect in influencing penalty rate is:

H2b: Tax agents will moderate the relationship between the penalty rate with non-compliance of excise duty by importers.

2.3 Tax Fairness

Tax fairness has an important role in determining tax compliance behaviour. Most of the prior studies on tax compliance indicate mixed results pertaining tax non-compliance and tax fairness. The taxpayers attitude and

perceptions on tax system's fairness is identified as a fundamental determinant that have significant impacts on the tax compliance behaviour (Alabede, 2012). If the taxpayers perceived the tax system is unfair to them, it will motivate to non-compliance behaviour (Gilligan & Richardson, 2005). Moreover, Spicer and Lundstedt (1976) stated if taxpayers believed tax system is unfair, they are more prone not to comply to the tax rules and regulations. According to Porcano (1984) the fairness of tax system is determined by the ability to pay and fulfilled the needs of taxpayers. Additionally, Richardson (2006) found significant negative correlation between tax evasion and tax system fairness. However, (Murphy, 2004) identified procedural fairness and tax compliance have direct and positive effect. Similarly, Verboon and van Dijke (2011) indicates procedural fairness and deterrence variables positively related with tax compliance. From the above elaboration, the related hypotheses to be tested in this study is as stated below.

H3a: There is a relationship between tax fairness with non-compliance of excise duty by importers.

Tax agents playing dual roles as an advocates to the taxpayers' deal as an intermediaries in the tax system. Tax agents' position is challenging to maintain the boundaries as an advocates and professionals (Bobek & Hatfield, 2003). If the taxpayers' perceived the tax system is unfair to them will prefer for aggressive tax reporting may lead to non-compliance (Hite & McGill, 1992). Tax agents as a moderating effect might enhance or reduce the relationship between independent variables or dependent variable (Lindley & Walker, 1993). Therefore the below hypothesis is proposed:

H3b: Tax agents will moderate the relationship between the tax fairness with non-compliance of excise duty by importers.

2.4 Peer Influence

Peer influence comprises of 'members of the family', 'current or future employer', 'close friends', and 'spouse / significant others' (Hanno & Violette, 1996). Prior studies on tax compliance showed mixed results in peer influence towards tax compliance. Peer influence is the perception on others action in a particular situation will lead to the determinant of approval or disapproval behaviour of an individual (O'Shaughnessy, 2014). Peer influence and tax compliance shows mixed results based on the previous studies findings. In the prior tax compliance literatures, it has been identified taxpayers are more likely to evade taxes if believed their peers are doing so (Grasmick & Scott, 1982; Spicer & Becker, 1980). This phenomenon is elaborated in Theory of Reasoned Action known as social psychology theory, explained individual's intention formed by attitude and subjective norms (Ajzen & Fishbein, 1980). Attitude perceived as a positive or negative will influence behaviour (Ajzen & Fishbein, 1980). Whereas, subjective norms referring to individuals believes on referent groups that caused to perform a specific behaviour (Bobek, Roberts, & Sweeney, 2007). For instance, if tax evasion is tolerable among the group norms and expectations it will induced the individual to perform the same behaviour (Chan, Troutman, & O'Bryan, 2000). According to Mason and Calvin (1978), the knowledge received from peers on taxes and politics will increases tax evasion. Whereas, Alon and Hageman (2013) found negative relationship between particularized trust. Similarly, Torgler (2012) found significant and negative relationship and indicates dissatisfied individuals are more prone discussed political issues with peers. Therefore, the hypothesis stated will be as below:

H4a: There is a relationship between peer influence with non-compliance of excise duty by importers.

Tan (2011) also mentioned the advice given by tax agents to the clients depend on the clients risk profile shows the impacts of clients in determining ethical decision making by tax agents. Hite and McGill (1992) indicates the tax agents' aggressiveness as a moderator in preparing tax returns influenced by the opinion given by their peers. From the above elaboration, the related hypothesis to be tested in this study is as stated below.

H4b: Tax agents will moderate the relationship between peer influence with non-compliance of excise duty by importers.

2.5 Tax agent

Tax agents playing a vital role in determining the compliance level of importers as a taxpayer'. Their significant role as a tax preparers have tendency in affecting the direction of the relationship between independent variables and dependent variable. Therefore tax agents have strong effect on independent and dependent variables and modify the original relationship between them. Edwards and Lambert (2007) mentioned the moderator is introduced when have the influence in strengthening the relationship between the independent variables and dependent variable and its effect on behaviour. In the previous research done by academic scholars indicates there are mixed results on compliance behaviour of tax agents and taxpayers. The tax professionals' impacts in determining Australian individual taxpayers' studied by Devos (2012), the results revealed there was statistically significant association between the advices furnished by tax professionals and Australian individual taxpayers' compliance behaviour. While, Blaufus, Hechtner, and Möhlmann (2014) investigated the association between the expenses incurred for tax preparation by tax professionals' and tax compliance. The negative relationship between expenses exceeded the estimated tax savings caused for the non-compliance. Whereas in Malaysia the research done by Choong, Tong, and Tan (2008) shows significant relationship between age, gender and education level with the nature of ideal tax practitioners preferred.

3. Research conceptual framework

This study is underpinned by the Deterrence theory associated with the Fischer's Model by considering economic, social and psychological factors in determining noncompliance behaviour among importers as taxpayers for cigarettes, liquor and vehicles. Kastlunger, Lozza, Kirchler, and Schabmann (2013) pointed out not only the economic model will influence the compliance behaviour but have to consider social and psychological factors as well. Based on the prior studies results the conceptual framework for the current study as illustrated in figure 1.1.

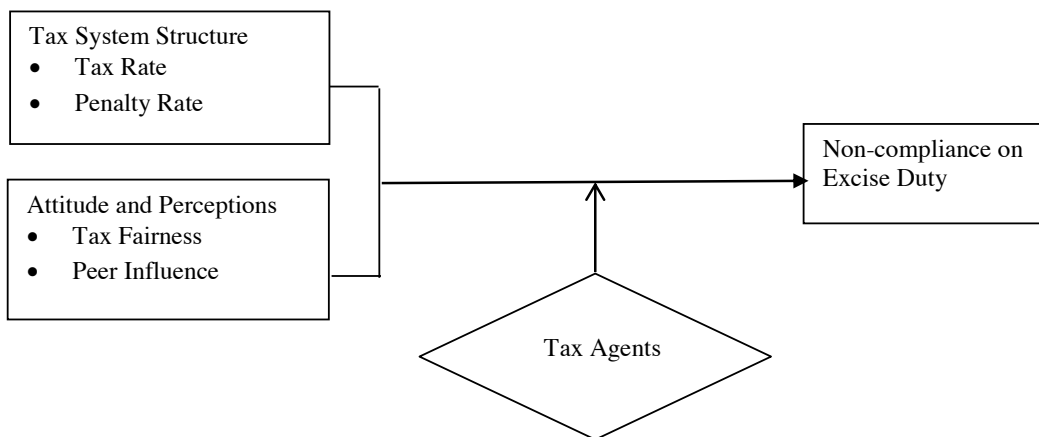


Figure 1.1 Research Proposed Model

4. Conclusion

The current study emphasized on indirect tax non-compliance on excise duties particularly on indirect tax involves cigarettes, liquor and imported vehicles. Furthermore, this study developed a conceptual model by enhancing and integrating Fischer's Model in determining non-compliance on excise duty. The factors that influenced the tax non-compliance on excise duty based on the tax compliance and tax non-compliance literatures. The determinants of excise duty non-compliance in current study comprising tax rate, penalty rate, tax fairness, peer influence and tax agents as a moderating effect.

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