A PROPOSED MODEL OF CULTURE INFLUENCE TOWARDS INTENTION OF TAX NON-COMPLIANCE AMONG SME OWNERS IN MALAYSIA

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Abstract:
Despite the importance of SME as the backbone of Malaysia in generating national income, prior studies on tax non-compliance have focused little on culture influence as one of the predictors of tax non-compliance. With the multicultural society which has a different culture, belief, and value, it is important to examine culture influence towards tax non-compliance, so that actions can be taken by the IRBM to deter tax non-compliance of SME owners. Therefore, this study attempts to propose a conceptual framework of Hofstede’s Cultural Dimensions Theory to be used in examining culture influence towards the intention of tax non-compliance among SME owners.

Keywords:
Tax Non-Compliance, Intention, SME Owners, Culture Influence, Hofstede’s Cultural Dimensions Theory

Introduction
Small and medium enterprise (SME) has been known as backbone of Malaysia since it leads the economic local and export demand with a contribution up to 99.2 percent of businesses and companies in Malaysia (Kamaruddin, 2014). Despite the economic challenges, SME contribution towards gross Domestic Product (GDP) has increased from 37.8 percent to 38.3 percent and SME Corporation Malaysia (SME Corp.) believed that the local SME sector would grow higher concurrent with the contribution rate of SME towards nation to achieve more than
RM800 billion or 40 percent of GDP by 2020. SME Corp. also has released that total number of SMEs registered in Malaysia were amounting to 907,065. Such huge figures show that more taxes were expected to be collected thus would reduce tax non-compliance behaviour. However, Inland Revenue Board of Malaysia (IRBM) has released that the audited cases resolved for SME in 2016 is 541,798 cases compared to 529,010 cases for 2015. It indicates that there was an increase of 2.4 percent in the cases audited on 2016 than the year before. Despite small amount, it may be considered as an alarming signal of tax non-compliance behaviour due to its higher contribution as backbone of Malaysia economy.

Furthermore, Mohamad, Zakaria and Hamid (2016) claimed that the tendency of SME owners engaging with tax non-compliance are higher since having huge opportunities to involve in cash business transactions as well as the possibilities not to declare it. Study by Mohd Ali (2013) revealed that taxpayers with business income also found to have medium to low range of tax compliance due to higher opportunity in avoiding tax and their actions appeared to be mostly overlooked by the tax authority. Study by Mohamad et al. (2016) found that tax evasion to be greatest among micro and medium-sized SMEs located in suburban areas.

Besides that, this study will be conducted to call upon study done by Yong (2011). Due to its limitation applying qualitative approach in gaining rich and in-depth insights on the ethnic of SME operators in New Zealand, future researchers recommend applying different research methodological approach such as surveys and extend it on countries that exercised self-assessment system, for example Malaysia. This is similar to a suggestion made by Chau and Leung (2009) to not only focusing cultural study on Anglo-Saxon countries, but it should be extended and conducted on other multiracial and multicultural countries. Moreover, Yong recommended to further broke down the ethnic into subgroups (e.g. Chinese, Indian and so on) because she believed that these subgroup culture may have different influence towards tax behaviour.

Given this gap of knowledge, there appears considerable scope for further study. Thus, the objective of this study is to examine the culture influence on SME owners’ intention towards tax non-compliance. To do so, five-dimensional measure of culture in Hofstede’s Cultural Dimensions Theory known as power distance, uncertainty avoidance, individualism-collectivism, masculinity-femininity and long-term-short-term orientation will be used in this study.

**Literature Review**

Hofstede’s Cultural Dimension Theory has been introduced by a Dutch psychologist name Geert Hofstede. It is an approach using human values through cultural dimensions for the purpose of conflict management in a society. Hofstede (2001) defined culture as “the collecting programming of the mind that distinguishes the members of one group or category of people from another”. Five-dimensional measure of culture known as: (1) power distance, (2) uncertainty avoidance, (3) individualism versus collectivism, (4) masculinity versus femininity and (5) long term versus short-term orientation, has been introduced (Hofstede, 1991, 1980).

Power distance refers to the acceptance level of the society towards differences in distributing power and represents the solutions of basic problem in human inequality Hofstede (1980). Malaysia has a high score in Power Distance Index (Hofstede, Hofstede and Minkov, 2010). It can be shown by Malaysian present attitudes such as obedience and conformity and they’re still in an autocratic decision-making and under a close supervision (Tsakumis, Curatola and Porcano, 2007).
Uncertainty avoidance relates to the level of stress in a society to face the unknown future. It does not refer to social behaviour but more on searching for absolute truth (Hofstede and Bond, 1988). As for Malaysia, it has weak uncertainty avoidance.

Individualism versus collectivism refers to how individuals choose to be integrated in their own groups and show individuals behaviour towards the group (Hofstede and Bond, 1988). In the case of Malaysia, it has a tight social relationship among each other in the society (Tsakumis et al., 2007) and was listed as a collectivism country.

Masculinity versus femininity measurement does not refer to the dominance of gender but it represents to what extent the integration of social or community (Jones, 2007). It shows the individuals behaviour towards one’s sex (Hofstede and Bond, 1988). According to Hofstede (1980), masculine societies more focused on achievement and success as their dominant value and can be categorized as an assertive pole. It is opposed to femininity society, where they prefer to have a good quality in life and relationships as their dominant value and can be categorized as a nurturing pole. As for Malaysia, it was listed as feminine country (Hofstede et al., 2010).

Long-term versus short-term orientation posits time orientation which concerned to persistence and thrift, past and present, tradition and social obligations (Bond and Chi, 1997) as well as on how we plan our decision relates to saving and spending because individuals behaviour also was affected by time orientation (Phuong-Mai, Terlouw and Pilot, 2005). Phuong-Mai, Terlouw and Pilot (2005) believed that long-term oriented individuals always looks for future, always persistent in doing the best as they could, strategically plan their spending and still obey the rules as long as it may give benefits to them because they believed on “what works” approach. This is contradicting with short-term oriented individuals, where they tend to look for what they experience in past and present. They love appreciate others with gifts and others. In complying with tradition, they tend to repeat or follow what has been practiced before because they believed on “what is right” approach. Hofstede et al. (2010) present East Asian countries and Eastern and Central Europe countries as long-term oriented culture countries while United State of America, Australia, Latin American and African countries are considered as short-term oriented. Muslims countries were also categorized as short-term oriented.

A number of studies have been undertaken in determining the influence of culture in tax compliance area. Individualism – collectivism dimension has been studied by Chan et al. (2000) and McGee, Ho and Li (2008) on United States and Hong Kong taxpayers. Chan et al. found significant differences between these two cultures on collectivism and individualism towards taxpayers’ compliance behaviour. Hong Kong taxpayers found to be a collectivistic while United States is more individualist. Those individualists are more compliant and have favourable attitude towards tax. These differences might give an effect to the taxpayers’ ethical value and moral development as well as to the tax compliance behaviour (Chan et al., 2000). Chan et al. found a negative significant relationship between culture (they use national differences) and tax compliance behaviour of US and Hong Kong taxpayers. Hong Kong tends to be collectivistic, while US are more individualist. The findings are consistent with McGee et al. towards tax evasion among advanced undergraduate business students in United States and Hong Kong. However, these studies used students as their respondents and McGee et al. recommend to extend the study towards business owners, where the findings could be different and more remarkable.
There is also a study conducted by Tsakumis et al. (2007) using this model and Malaysia has been chose to be one of the samples among 50 selected countries. Overall, Tsakumis et al. concludes that in explaining power distance dimension, Malaysian still practices obedience and conformity since there still in an autocratic decision making and under a close supervision. Furthermore, Malaysian considered to be more collectivist since it has a tight social relationship among each other, has a moderate to weak uncertainty avoidance and more towards to femininity, which choose to have a good relationship with each other’s and concerns in quality of life.

A mixed method cross-cultural studies in Malaysia and New Zealand has been conducted by Hamid (2013) on tax agents. The findings are inconclusive between survey and interview. Findings from survey revealed that Malaysian tax agents have higher degree in power distance and masculinity. Malaysian tax agents found to work under a close supervision from senior staffs and junior staffs still have to practice obedience towards senior staffs as well as focused on achievement and success. Furthermore, Hamid claimed that the masculinity trait possibly would be different regarding to how respective tax agents deal with their tax authority on tax laws and provision. Contrary to interview findings, this revealed that Malaysia tax agents have lower power distance and high individualism dimension. On the other hand, New Zealand tax agents found to be more individualist and high uncertainty avoidance. Findings from interview only found higher individualism dimension in tax agents. Overall, Hamid found significant differences regards to culture influence between participating countries. Culture found to have a weak to moderate level of significantly positively association towards New Zealand tax agents in both case of overstating expenses and understating income scenario. They had tendency to practiced individualism and higher uncertainty avoidance in performing their duties, which may influence their behaviour in complying with tax. However, Malaysia tax agents found not to be influence by its culture neither in overstating expenses nor understating income scenario.

An intra-cultural study conducted by Yong (2011) towards ethnic in New Zealand, focused on SMEs owners, used qualitative method by conducting a face-to-face in-depth interview in collecting data on the differences of ethnic group. The ethnic group in Yong study broke down into four major ethnic groups, namely Asian, Europe, Maori and Pacific group. Regarding to record keeping functions, Europe and Asian group found to have moderate to high uncertainty avoidance, medium to long term orientation as well as masculinity cultural trait which showed that they are more confidence and have high level of proficiency in record keeping compared to Maori and Pacific group. Asian group also found to be more collectivist in seeking for tax assistance as they relied more on friends and peers compared to Europe, Maori and Pacific group which seek for paid tax practitioners. According to Yong, SME owners which are collectivistic, long term orientation values and low power distance cultural trait would incur low compliance cost as they are not depending too much on paid tax practitioners. In terms of tax payment difficulties, collectivistic and femininity cultural traits of Maori and Pacific group tend to face more tax payment difficulties compared to Asian and Europe group. Yong found that medium to long term oriented, medium to high uncertainty avoidance, low power distance, collectivist as well as masculinity cultural traits were able to pay their taxes timely in order to avoid tax penalties. Recommendation made by Yong on extending culture study on other multicultural countries implementing SAS since study on the influence of culture among SMEs owners has been lagged behind despite its importance in determining voluntary compliance level.
Study by Alabede (2012) on tax compliance behaviour among individual taxpayers in Nigeria found significant differences between culture in Nigeria. Study used quantitative method by distributing questionnaire in collecting data. Alabede found that Igbo ethnic tend to be individualistic and practices full compliance with tax laws whereas Hausa and Yoruba were not in full compliance since they found to be collectivist.

A prior study in Cebu, Philippines by Malaya and Malaya (2012) also has been conducted in due to the problem of non-compliance behaviour in paying tax. This situation continues to be unresolved even though penalties and audits exist. Study found that cultural played an important role in encouraging taxpayers to comply with tax laws. Specifically, three of five cultural dimensions; power distance, individualism – collectivism and long term – short term orientation, have been identified to influence tax compliance in Cebu. Collectivistic Cebu taxpayers found to have high power distance and short-term orientation cultural traits.

In the context of Malaysia environment, culture study has been conducted by Kasipillai and Abdul-Jabbar (2006) among taxpayers in northern region of Peninsular Malaysia. The finding was different with other culture studies. They found that there is no significant difference among ethnic groups on the overall non-compliance attitude. But this is due to the limitation of sample, since its limit to only five urban areas in northern region of Peninsular Malaysia, which are George Town, Alor Setar, Kulim, Sungai Petani and Kangar. Thus, the ability to generalize and represent the population is limited.

Study of culture towards tax non-compliance behaviour had been conducted intra-culturally and cross-culturally. Li (2010) argued that cross-cultural studies could misrepresent the analysis due to some important factors that should be taken into consideration such as the tax burden, origin of the legal, culture and distribution of the income of those countries. Torgler (2007) and Yong (2011) supported the argument by stated that it is more useful and representative if intra-cultural study to be conducted in investigating culture influence in tax compliance area due to the differences in countries’ tax laws and regulations, type of taxes as well as its environment.

Overall, findings on study of culture are still inconclusive and need further study especially in Malaysia tax environment. Furthermore, there is also recommendation by Yong (2011) to further tax culture study and also argument by Chau and Leung (2009) in their critical review of Fischer tax compliance model to consider cultural dimensions into tax compliance study. This is consistent with suggestion by Alm and Torgler (2006) and Nerre (2008) as tax culture in every countries are not similar and relates to its cultural norms and countries tax environment. Therefore, this study believes that it could be an interesting finding to discuss the influence of taxpayers’ culture regarding on dimensions introduced by Hofstede in influencing intention of tax non-compliance among SME owners.
Research Conceptual Framework

Figure 1 illustrates the proposed research conceptual framework to be used in this study:

<table>
<thead>
<tr>
<th>Culture</th>
<th>Intention of Tax Non-Compliance</th>
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<tbody>
<tr>
<td>Power Distance</td>
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<td>Uncertainty Avoidance</td>
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<td>Individualism vs. Collectivism</td>
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<td>Masculinity vs. Femininity</td>
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<td>Long term vs. Short-term Orientation</td>
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Figure 1: Research Conceptual Framework

Research Methodology

A survey will be carried out by using a structured questionnaire, adapted and modified from instrument used by Hamid (2013) and Minkov and Hofstede (2012) to suit to SME owners in measuring culture dimensions towards intention of tax non-compliance. A five item Likert scale will be used, and 5 score will be given for “strongly agree” and 1 for “strongly disagree”. The questionnaire will be randomly personal distributed and collected from the SME owners from five major urban towns located in the northern region of Peninsular Malaysia, namely: (1) Kangar, (2) Alor Setar, (3) Sungai Petani, (4) Kulim and (5) George Town.

Total SMEs registered in Malaysia under National SME Development Council (NSDC) amounting to 907,065 firms. Out of that, only 123,361 firms were located in northern region of Peninsular Malaysia. Based on the Krejcie and Morgan (1970) rule of thumb, the appropriate sample size of 382 shall be drawn and is considered enough to represent the population. However, it will be increase at assumption of 30 percent as suggested by Israel (1992) to avoid non-response respondents, therefore 500 samples will be considered.

Conclusion

Based on the empirical evidence and theoretical perspective, this study has taken a challenge in explaining Hofstede’s Cultural Dimensions Theory to investigate culture influence in determining intention of tax non-compliance among SME owners. Besides contribution on new empirical evidence and tax literature knowledge, it also hopes to propose new ideas to understand the behaviour of SME owners in engaging with tax non-compliance. Furthermore, it also expected to help in understanding taxpayers’ culture relating to non-compliance intention. Although dimensions originally being used in determining behaviour in organization, it is expected to assist these respective stakeholders in raising taxpayers’ awareness of potential loss to the nation due to engage in tax non-compliance.

References


