

## FACTORS AFFECTING TAX COMPLIANCE AMONG COOPERATIVES TAXPAYERS IN MALAYSIA

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**Abstract:** Like other tax administrators in the world, Inland Revenue Board of Malaysia (IRBM), has continuously focuses on tax avoidance and tax non-compliance problem which affect the nation's tax collection. Recently, increased attention is given to cooperatives taxpayers as its contribution towards Malaysian's GDP is expected to increase up to 5% in 2025 compared to 3%-4% in year 2021. However, despite of 14,427 cooperatives registered with Commission of Malaysia (SKM) in 2018, only 3,534 registered as taxpayer under Form CI category. To understand this phenomenon, a study is conducted to understand the effect of tax knowledge, tax awareness and compliance cost toward compliance behavior among cooperatives taxpayer in the southern region of Malaysia. Adopting Attribution theory, this study is expected to shed some light on the issue and provides suggestion to improve the role of SKM and IRBM in ensuring higher tax compliance among Malaysian's cooperatives.

**Keywords:** Tax compliance, Cooperatives, Attribution Theory

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### Introduction

Since 1922, cooperatives have been a great help to the rural people in Malaysia where the main purpose of cooperative's establishment is to protect them from being exploited (Mahazril Aini et al., 2012). Since then, cooperatives have played a significant role in the country's economic growth, where cooperatives nowadays, had expanding further by entering business in the fields of production and agriculture (Suruhanjaya Koperasi Malaysia., 2018). In 2018, annual report by SKM, reveal the number of registered cooperatives is 14,247. This shows an increasing pattern since the number of registered cooperatives in 2011 was only 8,300 (Suruhanjaya Koperasi Malaysia., 2018). In term of number of memberships, it has reached 7,609,204 in 2018 compared to 6,060,732 members in 2013. The reported revenue of the total cooperatives in 2018 was RM33 billion compared to RM40,318.14 million five years back in year 2013

(Musa et al., 2020). The increase in revenue was believed due to the continuous supports by the government to assist the growth of cooperatives' movements in Malaysia.

In term of the taxation, treatment for cooperatives taxpayers is similar to other business entities that generates income. Cooperatives are taxed on its income, either arising from its mutual or nonmutual activities (Inland Revenue Board, IRB). In accordance with Income Tax Act 1967, under section 77A, "a co-operative society has to submit the ITRF (Form C1) to the Director General of Inland Revenue within 7 months from the date following the close of the accounting period which constitutes the basis period for a year of assessment". In order to promote tax compliance, IRBM has focuses on numbers of taxpayers education and awareness programs to educate taxpayer towards their tax responsibility. These programs were implemented to promote voluntary compliance, since under Self-Assessment System (SAS) the taxpayers are requires to assess their own tax liability and file their own tax return (Azmi et al., 2020). With the trust given to taxpayers in managing their own tax affairs, SAS also necessitates taxpayers to have a proper record keeping for audit purposes. This requirement was perceived to increase the complexity of the system and increase compliance cost at the same time. Beside IRBM, the SKM also play its role in educating cooperatives on their responsibility toward tax. SKM offers accounting courses with taxation module and this course was made compulsory for the board members of the cooperatives.

However, despite of increasing revenue of the cooperatives and implementation of various taxpayers' education program, the contribution of cooperatives as taxpayers is still relatively limited (Rahayu, 2020). As the GDP contributed by the cooperatives is expected to grow in the future, it is very important for the tax authority to understand the factors that promote cooperative taxpayers' compliance. Understanding these factors will help the government to ensure the returns on incentives provided to promote cooperatives' economic growth.

## Literature Review

### Tax Compliance

The terms of tax compliance has been defined differently in the previous literatures. For instance, [8], define tax compliance by describing it through the degree of compliance with the tax law by the taxpayers. Another literature by [9], defines tax compliance through the process of making payments in full on all taxes due. Together, the definition of tax compliance can be said as the ability of taxpayers, together with their willingness, to bind by the rules and regulations under tax law, and declaring and reporting their income and thus, paying those reported income within the time specified [10]. Reference [11] has added on the definition of tax compliance in term of duration of tax payments. It defines tax compliance as an act of a person in filing the tax return by declaring the taxable income honestly and truthfully, and then, make a prompt payment on the tax due by not waiting any follow-up actions from the tax administrators.

In regard to tax compliance, there is a large volume of published studies focused on the issue of tax compliance, especially among business. This is because, the more advanced is the business, the more complex the compliance become. Despite of numerous taxpayer education and awareness programs being implemented, tax compliance level among Malaysian taxpayers still need further attention. It was reported only 15.4% registered labor force and 17.2% registered companies were paying tax in year of assessment 2018. Taxpayers' failure to fulfil their responsibility has raised concern on the effectiveness of taxpayer education programs and

enforcement activities which have been intensively enhanced, with implementation of SAS. Less responsible taxpayer will lead to tax gap problem which able to cause losses of revenue, unequal distribution of wealth and distort the future development of the country.

### **Tax Knowledge**

Reference (Azmi et al., 2020) highlighted that it is a taxpayer's responsibilities to equip themselves with knowledge in order for them to disclose, reports and, simultaneously, pay tax. They also believe one's tax knowledge is one of the determinant factors in tax compliance. Knowledge, in general, can be defined as obtainment of information, facts and expertise through experience or education (Hamid et al., 2019). Thus, tax knowledge is referred to taxpayer's ability to understand the tax system based on the knowledge that they have on taxation in term of its laws and the system. According to (Wong & Lo, 2015), in order for a taxpayer to comply with tax laws, he or she needs to have both technical and general knowledge about tax system. In the countries with high level of tax compliance such as Canada, Switzerland, United States and New Zealand, education on taxation had been started at the earlier stage of education. It believes by getting them equipped with tax knowledge at early age, it can help the future taxpayer to get prepared and embraced their responsibility towards the country's development.

The influence of tax knowledge on tax compliance have been studied extensively in previous literatures (Hamid et al., 2019), (Manual & Xin, 2016) & (Musimenta, 2020). Most of these studies suggest that tax knowledge is the most significant factors in determining taxpayer's compliance behavior under the self-assessed system. It is further supported by the study done by (Wong & Lo, 2015), where they found education is positively associated with tax compliance. This is because, tax knowledge helps the taxpayers to understand the tax rules and enable them in filing the tax return. Reference (Azmi et al., 2020) suggested that lacking or limited tax knowledge will cause non-compliance, either intentionally or unintentionally. Reference (Kamil, 2015) states that without a proper knowledge and understanding of tax rules and obligations, people may hesitate to pay tax. This study also added that, by having good understanding and knowledge in taxation, people will open their mind as they believe that the amount of tax paid is essential for the fiscal of its nations.

However, (Palil, 2010), argued that gaining tax knowledge is time consuming. Self-assessed method and record keeping requirements under SAS has caused taxpayers to employ accountant or tax agent to help them in fulfilling their tax responsibility. Thus, lacking of tax knowledge also caused an increased in compliance cost. Despite of the above statement, (Kamil, 2015) found that having an understanding of tax, can minimized the level of corruption and fraud from occurring.

### **Tax Awareness**

According to (Hastuti., 2014), tax awareness is self's awareness of the taxpayers on their responsibilities to calculate, report and pay tax. Reference (Savitri & Musfialdy., 2016) laid out three forms of awareness or consciousness that attracts taxpayers to pay tax. Firstly, is on their realization that tax is part of source of funds to a country's development. By knowing this, taxpayers are willingly to pay tax as they don't want to be at the disadvantage's sides. Secondly, is on their realisation that by delaying tax payment and reducing the tax burden will negatively affects the country. In this way, taxpayers are in awareness that by delaying tax payment and reducing the tax burden, it will, simultaneously, delaying the development of the country. Finally, the third form of awareness is recognizing tax as part of law and can be enforced.

Through this realisation, taxpayers will pay their tax, due to their awareness that pay tax is part of their obligation.

By having these three forms of awareness, taxpayers will be more conscious that the amount of tax paid by them are important in funding the development of the country. Therefore, by doing so, they are having faith on the government to manage the funds. Reference (Damayanti & Martono, 2018) opined that tax awareness are likely to be increased when the taxpayers are having trust with the tax authorities. Reference (Azmi et al., 2020) stated that tax authorities must play an active role such as conducting awareness programs to instill tax responsibility among the public. By implementing awareness programs, tax authorities can easily monitor taxpayers compliance level in terms of the number of tax file being registered and tax paid.

Awareness on the obligation towards tax, will result in either, compliance or disobedience towards tax. Due to awareness, taxpayers are willing to contribute funds, out of their wealth, for the development of the country (Nurkhin et al., 2018). Therefore, the higher taxpayer's awareness, the more compliant they will be come. Besides, a conscious taxpayer is less likely to question under what reason he or she should pay tax. However, lack of tax awareness has become one of the main factors in non-compliance as they fail to know the benefits that they will received for the amount of tax they have paid. Reference (Kamil, 2015) examines the effect of tax awareness on tax compliance and found a significant positive relationship between the variables. Similar to (Abdulazeez, 2018), the study also found a positive and significant relationship between taxpayers' awareness with taxpayer compliance.

However, (Azmi et al., 2020) shows that tax awareness among Grab drivers doesn't affect taxpayers' compliance behavior. The negative effect can be explained by (Saira et al., 2010) that highlighted the concept of false awareness among optimistic citizens. Optimistic citizens refer to those who have overestimated tax burden or inaccurately estimate public services burden with the tax imposed to the public. Therefore, the government should be more transparent about the taxation matters, so that the taxpayers could have a clear understanding on their tax responsibility. The government should explain the reasons for the tax collected and rationalize the benefit of taxes that they will receive later on.

### **Tax Compliance Costs**

In the area of taxation, compliance cost can be described as the cost to be borne by the taxpayers in fulfilment of their tax requirements (Ahmad, 2018). This study highlights three elements of tax compliance costs, known as; (1) taxpayers' monetary cost (2) time cost and (3) psychological costs. Money cost refers to the cost of hiring a tax professional (such as tax agents, accountants or consultants) as well as all the related expenses such as buying of taxation guidance books. As for the time cost, it is measured through the time spent by taxpayers in term of records keeping of tax information, hours spent on completing the tax form as well as hours spent to prepare tax details to be given to the tax professionals. It also includes hours spent in dealing with tax authorities on tax matters. Meanwhile, phycological cost is the impact on taxpayers' emotions while dealing with their complex tax affairs and result in increased taxpayers anxiety.

Reference (Pope & Hijattulah, 2008) defines compliance cost in different views than other literatures by looking at all costs, other than the actual liability of tax. They had included in their study the cost incurred by taxpayers during the process of becoming a compliant taxpayer. The compliance cost covers avoidance cost and cost of non-compliance (including the cost

related to tax evasion, psychology and bribery cost). Six types of compliance cost that have been identified are (1) administrative cost (2) time spent and psychological cost (3) internal and external costs (4) computational and tax planning costs (5) commencement and recurring cost and (6) accounting and tax costs.

A study by (Sapiei & Ismail, 2014) found that 78% of tax compliance cost of PLCs in Malaysia consists of computational costs, while another 22% involves in planning and other cost. The result also shows that a company with small annual sales turnover incurring more costs on the computational work. In another study on SMEs, by (Mansor & Ekonomi, 2008) found that 45% of the respondents agree that the burden to comply with tax, involves cost incurred. The amount of cost was also influenced by factors such as the size of the companies, nature of business, types of tax advisors, as well as the business's location.

However, in another study done by (Ahmad, 2018) on SMEs in the southern region of Malaysia, found that there is no significant relationship between tax compliance costs and compliance behavior. This finding is further supported by (Jabbar & Pope, 2008) where they also found no association between compliance costs and compliance behavior.

### **Attribution theory**

Attribution theory was developed by Fritz Heider in 1958 explains one's behavior through the combination of internal and external factors (Nurkhin et al., 2018). Internal behavior is derived from the individual itself, through a person's ability and effort. While external behavior comes from the outside which is surrounding or the environment of a person. Through the external factors, the theory explains that a person needs to behave according to the demand of the situation or environment. In simple word, the theory rationalized the reason that causes a behavior or an act. The questions of what is causing what, and what makes the people to behave in that way, is directly related to the theory.

Attribution theory also used to explain the willingness of the taxpayer to pay tax, together with the perception on their responsibility to assess the tax itself. In a situation where taxpayers need to understand the tax laws, it is in-line with the theory of internal attribution since the decision of a person to behave, is influenced by the factors underlying with the internal control (Nurkhin et al., 2018). Meanwhile, for a person to know how to behave, their perceptions on a situation will be influenced by surrounding external factors (Kamil, 2015). Therefore, Attribution theory is expected to explain how the internal and external compliance factors able to determine compliance behavior among of cooperatives taxpayer in Malaysia.

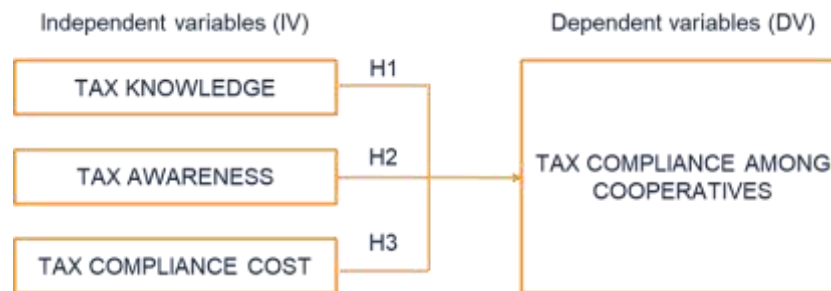
### **Methodology**

The study conducts a comprehensive search of the literature from various peer-reviewed journals and media reports focusing on the impact of tax knowledge, tax awareness and compliance cost on compliance behavior among cooperatives taxpayers in Malaysia. Review was performed on the most recent selected literature from both relevant online platform and news portal as well as academic journals to extract the most current and contemporary issue. The keywords searched were "Tax compliance", "Cooperatives" and "Attribution theory". The data were grouped into separate themes such as the compliance factors, current issues and tax regulations related to cooperatives. This method provides an opportunity to comprehend the current concerns and consequently to depict some critical policies to respond on the issues focuses by this study.



## Conceptual Model

Figure 1 below portrays the proposed conceptual model which surrounds compliance behavior among cooperative taxpayers. Tax knowledge, tax awareness and compliance cost are proposed to integrate and operationalised within the Attribution theory to explain compliance among the cooperatives in Malaysia.



**Figure 1: Conceptual Model**

This conceptual model works when cooperatives were equipped with tax knowledge, either from courses provided by the SKM or taxpayers education programs by the IRBM. The Co-operative Institute of Malaysia (IKM) is an academic wing of SKM which offers compulsory courses to be enrolled by the board member of the registered cooperatives. These courses include module on accounting and taxation. IRBM at the same time also conduct numerous taxpayer education programs through several channels from face-to-face seminar, media broadcast, online platform, printed material and billboards advertisement to increase taxpayers' knowledge on taxation.

These tax courses and education programs are expected to establish higher awareness among the cooperatives taxpayers on their tax responsibilities and related policies. Based on Income Tax Act 1967 (ITA), cooperatives were provided with 5 years tax exemption starting from the year of incorporation and only required to pay tax in the sixth years under certain conditions. With this knowledge, cooperatives are expected to be well prepared for their future tax responsibilities and ensure certain action is taken to comply with tax regulations. With adequate tax awareness, cooperatives are expected to be more compliant towards tax.

Like other business entities, cooperatives also obliged to maintain sufficient and proper record keeping under Section 82 of ITA 1967 for audit purpose. They are also require to assess their own tax liability and furnish their own tax return under SAS. These requirements result-in compliance cost as the cooperative might need to hire competent accounting staff or external tax practitioner to help them in fulfilling their tax responsibilities (Musimenta, 2020). The existence and increments of compliance cost is expected to affect cooperatives' compliance towards tax.

The integration of the internal factors (tax knowledge and tax awareness) and the external factor (compliance cost) is expected able to determine compliance behavior among cooperatives taxpayers. Increased in compliance, which result from cooperatives' understanding on the reason to pay tax, the benefit it gives to the others and perception towards other cooperatives' compliance behavior, portrayed the operationalization of the Attribution theory in Malaysia.

## Conclusion

The major purposes of taxation are to raise and generate revenue for public expenditure, to redistribute income and wealth, to correct market system inefficiencies, and to control and maintain the money and price circulation in order to stabilize the economy. Tax is collected from various types of taxpayers which generates income defines under Section 4, ITA 1967.

Recently, cooperatives in Malaysia have shown a substantial increase in revenue. This is in-line with various incentives provided by the government to boost up the cooperatives' business. In March 2022, the Ministry of Entrepreneur Development and Cooperatives (Medac) through the Commission of Malaysia (SKM) has allocated RM230 million for the implementation of new products of the Malaysian Cooperative Commission Revolving Capital Fund (TMPSKM). With potential business expansion and higher expected contribution in GDP, tax collected from this category of taxpayers is expected to show an increasing trend.

Due to scarce number of research focusing on tax compliance among Malaysian cooperatives, the low number of cooperatives registered as taxpayers with IRBM, has raised concern on its compliance issue. It is very important to understand the reasons of this occurrence and to answer the question of why tax contribution among cooperatives in Malaysia is still reported as relatively low (Rahayu, 2020). Further study shall be conducted using the proposed conceptual model to see the effect of internal and external factors towards cooperatives' tax compliance behavior. The finding will help the IRBM and SKM to evaluate the effectiveness of the taxpayer education and awareness program implemented by the related bodies. At the same time, it is also crucial to understand the effect of compliance cost among cooperatives and the surrounding factors that able to promote compliance among cooperatives. Understanding the effect of this factors will help the government to maintain adequate compliance level in order to ensure the objectives of taxation is achieved.

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