

eJournal of Tax Research

Volume 15, Number 3

December 2017

CONTENTS

- 387 The purpose of tax law: A perspective on financial instruments' fair value adjustments in Portugal
António Martins and Daniel Taborda
- 402 Encouraging superannuation income streams with tax-free earnings to b

GST compliance and challenges for SMEs in Malaysia

Yong Mun Ching¹ Jeyapalan Kasipillai² and Ashutosh Sarkar³

Abstract

Malaysia introduced GST in April 2015 to reduce its budget deficit. This study investigates how the introduction of GST impacts SME owners in the retail sector. We conducted semi-structured face-to-face interviews with owners of GST-registered SMEs within the context of the theory of reasoned action model. Findings reveal mixed results on the attitudes and perceptions of the interviewees. Compliance costs are proportionally higher among SMEs and these enterprises are often not adequately prepared to accommodate the new tax provision into their businesses. The study identifies the relationships among the factors that influence the intention to compliance behaviour.

1. INTRODUCTION

One of the major concerns of goods and services tax (GST) introduction is its strong impact on small and medium-sized enterprises (SMEs). Malaysia introduced a GST in April 2015 in order to generate sustainable revenue streams and in the hope that its implementation would reduce budget deficit to 3% in 2015 (2010: 7.4%; 2012: 4.5%; 2013: 3.9% and 2014: 3.5%) (Kraal & Kasipillai, 2016). In 2017, the revenue collection is expected to expand at around 3% to MYR 7 billion, with a targeted fiscal deficit of 3% of GDP in 2017, compared with 3.1% in 2016. In 2015, SMEs contributed 36.3% to Malaysia's economy (GDP), a steady growth from 32.5% in 2011. SMEs employed 65.5% of the country's workforce in 2015. As Malaysia endeavours to achieve the status of a developed nation by 2020, the country deals with varied tax-collection and revenue-generation issues. To lessen its over-reliance on income from petroleum, which constitutes more than 40% of federal government revenue in 2014, the country replaced the sales tax and services tax with a GST. The government sought to achieve a steady source of revenue by broadening the tax base (Alappatt & Shaikh, 2014; Narayanan, 2014; Shaari, Ali & Ismail, 2015). The GST contributed MYR41.2 billion in 2016 compared to a predicted figure of MYR18 billion from the sales tax and services tax.⁵ In addition, the GST will cast the revenue net wider by capturing the entire economic chain that includes the shadow economy, estimated at 30% (Zhou, Tam & Heng-Contaxis, 2013). Although the government has taken several measures to reduce the compliance burden for tax-paying owners of SMEs, such as providing them with e-vouchers to upgrade or purchase GST-compliant software and training (Mokhtar, 2015), it has yet to address compliance issues facing SMEs.

This study investigates the major challenges encountered by GST-registered SMEs in Malaysia, namely GST-compliance readiness, compliance costs and attitudes. To this end, we pursue a qualitative approach (Orell 2009; 2013) and use the theory of reasoned action (TRA) model (Ajzen & Fishbein, 1980; Fishbein & Ajzen, 1977). The research strategy used in this study is phenomenology, which allows us to report our findings to closely resemble the participants' experience in implementing GST and their perception towards its introduction. This paper uses the abbreviations GST and value added tax (VAT) interchangeably.

In line with our research strategy, we conducted semi-structured face-to-face interviews, which included 16 interrelated questions (see Appendix 1) that focused on the research objective, with nine owners of GST-registered SMEs in the retail sector in the state of Selangor and the Federal Territory (Kuala Lumpur) of Malaysia. Interviews were conducted at the premises of the businesses between 16 July and 16 September 2015. The results indicate that business owners are

(psychological and social costs). After reviewing the tax literature, we identified three factors influencing GST implementation among SMEs: GST taxpayers' perception of fairness, GST compliance readiness of businesses and external factors (developments) that affect the business.

This study identifies the perception of fairness regarding the GST system, the GST compliance readiness of businesses and external factors influencing the behavioural intention of taxpayers. Further, the degree of support from family members, friends, fellow retailers and external consultants, known as subjective norms (perceived social influence), also determine the behavioural intention of taxpayers. The identification of factors influencing the behavioural intention of taxpayers is crucial because taxpayers could be influenced and nurtured to engage in GST-compliance activities over time.

2. THEORETICAL PERSPECTIVE

The TRA, which is a theory of social behaviour, was developed by Martin Fishbein and Icek Ajzen. According to Ajzen and Fishbein (1980), human beings are assumed to be rational and consider the outcomes of their actions before they make a decision to perform, or not to perform, a given behaviour. Behavioural and tax-compliance studies have widely used the TRA model to analyse tax compliance (Bidin & Shamsudin, 2013; Ishak, Othman & Omar, 2015).

Figure 1 illustrates the theoretical relationships of behaviour, attitude, subjective norms, intention and action as expounded by TRA. A behavioural intention to take action or not to take action (e.g., pay or not to pay tax) is assumed as the immediate factor that influences behaviour (e.g., tax compliance or non-compliance). The TRA model uses two components, namely attitude (personal) and subjective norms (social influence) to predict behavioural intention.

Figure 1: Theory of reasoned action



Source: Adapted from Ajzen and Fishbein (1980)

Attitude refers to a person's belief and inner evaluation of certain implications as a result of a particular behaviour. Subjective norms are 'perceived social pressure' exerted on an individual to take, or not to take action (Bidin & Shamsudin, 2013). As such, generally individuals will intend to take an action when they have a positive evaluation on the action, and when they believe that their social groups think they should do it. In this study, the TRA framework is used to analyse the motivating factor (behavioural intention) that affects actual behaviour of GST taxpayers. Desirable compliance behaviour among taxpayers can be influenced or persuaded via engaging in activities that enhance attitude and subjective norms of taxpayers' behaviour.

Using the TRA as its theoretical framework a survey of 103 respondents in the manufacturing sector in the states of Kelantan and Perlis in Malaysia, Bidin and Shamsudin (2013) affirmed that subjective norms and attitude have a significant and positive influence on the intention to comply with GST. In our study the most significant factor influencing compliance intention behaviour was subjective norm (social pressure), which refers to peers or business partners.

3. LITERATURE REVIEW

Our literature review covers the theoretical underpinning of the study and we examine prior studies in the areas of compliance behaviours and empirical studies on GST (or VAT) implementation experiences in five countries, namely Ethiopia, Bangladesh, Singapore, New Zealand and Australia. New Zealand applied GST from 1986, Bangladesh in 1991, Singapore from 1994, Australia in 2000 and Ethiopia in 2003. Other than Ethiopia, all of them are Commonwealth countries and they have all economically benefitted from introducing this new consumption tax.

3.1 Empirical studies on GST implementation

Our review of the experiences of implementing GST in five countries, namely Ethiopia, Bangladesh, Singapore, New Zealand and Australia assisted in tracing common issues and hidden costs faced by taxpayers in these countries. Certain GST implementation problems and issues in Ethiopia and Bangladesh are anticipated to arise in Malaysia too. In the case of Bangladesh, some of the common challenges in GST implementation, after more than two decades of implementation include: difficulty in understanding the legal provision; lack of availability on updated version of law; excessive and unnecessary documentation; delay in getting refunds; disappointing computerised accounting system; and financial hardship (Bala, 2010). A study of compliance costs and problems in the Ethiopian VAT system by Yesegat (2008) highlighted major problems, including insufficient tax administration resources and gaps in administration in the areas of refunding, filing, invoicing, audits and penalties. The author also identified little tax awareness among the public, weak educational programs, and lack of trust between the taxpayers and administrators as the major challenges to the VAT system.

In Australia, SMEs incur high compliance costs, mainly due to tax complexity and compliance burden to determine whether their goods and services are exempt from GST (MYOB Business Monitor, 2015). This study reported that complying with Australia's GST rules costs small businesses more than AUD13.5 billion a year. Hence, GST compliance is the major source of red-tape burden that adversely affects small business. Similar GST compliance burdens are evident in the Malaysian context as Malaysian SMEs have to ascertain, in some instances, whether goods and services they supply are exempt or zero-rated. Contrastingly, the critical success factors for GST implementation in New Zealand and Singapore are largely contributed by their well-planned implementation strategies, coupled with the design of GST system, which are easy to administer. A single GST rate is used in both countries, which covers a broad range of goods and services with minimal exemptions and exceptions. According to Sussman (2007) 'exceptions' to the general GST rules are also referred to as 'refinements' and they provide more specific outcomes while increasing tax complexity.

The more complex the rules are, the more likely taxpayers will not understand or comply

2. GST readiness which covers ~~step~~ undertaken to prepare for GST implementation, challenges encountered, the extent of support received from consultants and trade associations ~~clubs~~ chambers of commerce and the extent of support and interactions the business ~~esse~~ had with Royal Malaysian Custom Department (RMCD); and
3. Compliance costs, including initial costs ~~recurring~~ costs, psychological costs and non-compliance costs ~~153 TDaGo~~ of support received from

Chart 1: Profile of SMEs in Malaysia (2010)

Source: Department of Statistics Malaysia (2014b)

We adopted convenience and snowballing sampling procedures to recruit participants until data collection reached a saturation point. At this point no new or relevant information emerged with respect to the themes gathered earlier in the research. In qualitative research it is common to use convenience sampling procedures to facilitate access to individuals (Eriksson & Kovalainen, 2008). Furthermore, it is very difficult to recruit participants for exploratory research that investigates sensitive matters such as GST, revenue and business profitability. We succeeded in recruiting five participants using initial convenience sampling. From these contacts, the researchers snowballed to recruit more participants.

4.3 Procedures

The trustworthiness of this study is affirmed by the researchers maintaining a detailed trail of decisions made during the data collection and analysis process, including measures undertaken to collect data ethically, recruit participants and transcribe interviews. The researchers also undertook self-reflection throughout the study to ensure that personal biases and interests were consciously set aside in the process of data gathering, evaluation and interpretation.

Figure 3: Thematic map of GST implementation in Malaysia

5.2.1 Theme 1: Business owners attitudes and perceptions

According to TRA, one of the determinants which affects behavioural intention to take action or not to take action (to pay tax or not to pay tax) is attitude. This refers to a person's evaluation of certain implications as a result of a particular behaviour. Generally, a person intends to take action when one views the action positively and vice versa. Hence, this theme explains the application of the TRA in understanding GST taxpayer's behavioural intention, which eventually leads to their actions.

Further investigation into the attitudes and perceptions of participants reveals a number of factors that influence these attitudes and perceptions. Their attitudes and perceptions towards GST acceptance, readiness and implementation are interpreted and presented under three sub-themes below, namely attitudes towards GST implementation, attitudes towards GST regulations and perception of the GST as a burden.

(i) Attitudes towards GST implementation

Generally, participants expressed negative views towards GST implementation. However, we do note a number of positive views, such as the perception of GST as a more effective and transparent mechanism to collect tax for national development purposes. Furthermore, GST periodic reporting to RMCD has resulted in an improved audit trail within business entities as each transaction is now documented and reported to RMCD. Having said that, Retailer 4 commented that some businesses actually view improved transparency in business dealings positively as they can no longer be involved in creative accounting such as manipulation of financial results.

Another positive view we observed was that GST implementation is seen to have indirectly caused a reduction in illegal and unregistered businesses in Malaysia. Illegal business evades taxation and regulatory oversight, and is estimated to account for 20% to 50% of the Malaysian economy. This account was highlighted by Retailer 9:

Prior to 1 April 2015, one of my suppliers confided in me that her business was negatively affected by closure of about 20 businesses (customers) that were not legally established. Some of these businesses were owned by Indonesians in Chow Kit market. This is indeed a piece of good news for me

monetary support, the RMCD offered ~~5~~ ⁵ Ge-voucher of MYR1,000 to businesses for

Another challenge relates to education staff in compliance with GST rules and

a major change. In compiling the estimated recurring compliance costs for 2015, these costs were inflated with some amount of embedded learning costs in the first year of GST implementation. According to this study, the estimated recurring costs for GST include participants' persohāime, hiring of additional staff and costs paid to independent GST consultants (see Table 6).

Table 6: Recurring GST costs analysis

Revenue (in RM)	Retailer	Compliance cost/revenue (percentage)	Estimated compliance costs (in MYR'000)
< 1 million	2, 3 & 4	3.43–6.67	

government, without gaining any benefit in

Figure 4: Application of TRA for GST taxpayers in Malaysia

6.1 Attitude towards behaviour

We identify three main factors that affect attitudes, namely: GST taxpayers' perception of fairness; GST readiness of business; and external factors affecting business operations. Previous studies have shown that a negative perception of fairness towards a tax system may increase non-compliance behaviours among taxpayers (Oh & Lim, 2011b). In our study, we note a number of major factors that influence a taxpayer's perception of fairness, including: high compliance costs; tax complexity; the extent of support from the government; and psychological costs in coping with a new system, all amidst a difficult business environment (external factors). These major factors are closely linked with each other in influencing any perception of fairness among taxpayers. For example, the extent of GST compliance costs are closely associated with the degree of tax complexity and support from the government, which eventually culminate in a certain amount of hidden costs (psychological costs) borne by GST taxpayers.

The degree of GST readiness of a business may influence the attitude of certain taxpayers. Businesses that are more prepared to handle GST implementation tend to have a more positive attitude towards GST. The GST readiness of a business is generally determined by two main components: firm resources and owner's/participant's ability to cope with change. Firm resources include financial resources (i.e., ability to cope with initial and recurring compliance costs and increased working capital requirements); level of infrastructure (IT system and processes); and manpower. In the Malaysian context, most SMEs are heavily involved in the day-to-day running of the business; hence the owner's ability to deal with the new tax regime is crucial. The ability of the owner is dependent on their level of education, age,

particularly important when we consider that Malaysian SMEs are predominantly micro businesses with fewer than five employees. In general terms, financial, human and IT resources are lacking in such micro businesses, and these businesses therefore need more time and support in order to transition to a new regulatory environment.

The government should also critically assess the financial and social impact of closure of small businesses as a result of GST implementation. In addition, a more sympathetic

Grant, B. M. & Giddings, L. S. 2002, 'Making sense of methodologies: A paradigm framework for the novice researcher', *Contemporary Nurse*, vol. 13, no. 1, pp. 10–28.

Hamilton, B. & Teo, B. 2015,

- 1) The Government has introduced GST which is effective from 1 April 2015. What are your views as to the implementation of GST among SMEs (relates to perception of taxpayers)
- 2) Why are businesses not receptive towards a new system? List 3 to 5 potential burdens (if any). (relates to challenges in implementation i.e., regulatory, financial and psychological costs)
- 3) What is your view towards GST regulations as a whole? Select one statement that best summarise your view (relates to attitude of taxpayers)
 - a) Positive: Regulation is generally beneficial to my business as it raises standards of doing business in Malaysia thus improving the competitiveness of business environment;
 - b) Negative: Regulation is generally detrimental to my business because it increases the cost of operation and it makes my life more difficult in running my business; and
 - c) Neutral: Regulation makes little difference to my business operations and to my business environment.
- 4) What steps do you undertake to prepare for GST implementation? List 3 to 5 steps. (relates to GST readiness)
- 5) Are you aware of the available grant or resources provided by Royal Malaysian Custom Malaysia (RMCD) for SMEs? (relates to level of support rendered by the Government)
 1. For example, GST e-voucher of MYR1,000 for GST accounting software;
 2. Have you participated in any GST workshops or training courses organised by RMCD?
- 6) List 3 main challenging issues facing your business when implementing GST (Potential challenges identified are cash-flow, resources, business process changes, managing customers, GST software not working well, submission of GST return, claiming of refund, and compliance with GST Act 2014).
- 7) Do you get advice or support from consultants (i.e., accountant, IT services and tax advisors on direct and indirect tax) on the implementation?
- 8) Are your existing available resources adequate to address your concerns?
- 9) If not, how do you comply with GST requirements? What kind of support do you expect from RMCD i.e., consultation via GST Hotline and GST Portal?

10.2 Appendix 2 — Approval letter on ethics

