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Goods and Services Tax (GST) Compliance among Malaysian Consumers: The Influence of Price, Government Subsidies and Income Inequality

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Abstract

The purpose of this research is to explore the correlation between price, government subsidies and income inequality towards GST compliance. Tax noncompliance remains as global phenomenon that can threaten the integrity of every tax systems hence the understanding of what people want will help to explain public dissatisfaction, heading towards the direction of developing a tax system that stimulate tax compliance in the future. Research findings has revealed that all the selected variables have significant relationship with GST compliance. To conclude, this study has bridged the knowledge in tax compliance literature, providing empirical result on potential determinants of tax non-compliance in Malaysia.

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1. Introduction

Appropriate mixture of direct and indirect tax has led to long debate in political and academic circle, concerning the virtues and flaws in both forms of taxation structure. By and large, the distinction between direct and indirect taxes can be made easily as the former is levied directly either on personal or corporate income while the latter is levied on the price of goods or services and it is collected via intermediary parties. The adoption or degree of reliance on direct tax versus indirect tax is fundamental towards optimal design of tax structures as different versions

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of tax policies may amend the state economy differently. Nevertheless, Atkinson (1977) suggested that taxpayers may grow fond for indirect taxation over direct taxation considering that it offers them choice and it is less evident. Ultimately, the diverse designs of fiscal policies adopted by government tend to demonstrate the goals of efficiency and equity a nation tries to achieve.

Many reasons were put forward in introducing GST among them are due to the dissatisfaction towards the current consumption tax structure, reduction of other taxation rate as well as the existing tax system that has not been able to keep pace with the development of the economy (RMCD, 2013). In early 1990's, there was an equal contribution proportionally in revenue between direct and indirect tax however trade liberalization policies which took place has result in the proportion of revenue to change substantially specifically in year 2012 with the contribution of direct tax and indirect tax recorded at 56.4% and 17.2% respectively. In respect of this, majorities of economic experts claimed that heavily reliance on a on direct tax and petroleum revenue will bring about adverse effect on the nation's financial position due to there are only one-tenth of the working population pays income tax in consort with the fluctuation of international petroleum price (Business Council Of Australia, 2014; MIER, 2014). Henceforth, it would seem appropriate for the government to sort out the imbalances and raising its revenue via indirect tax reform which is much stable internally.

Into the bargain, an apparent rise in consumption tax for both developing and transitions countries are observable which has led to a rapid expansion in the trade of goods and services internationally in a globalized economy. European Commission employed QUEST model in replicating the macroeconomic effects of a revenue-neutral shift in taxation from direct to indirect taxes implied that a swing in taxes may indeed strengthen economic growth and increase employment (European Commission, 2006). Similarly, Baunsgaard and Keen (2005) stated that the degree of revenue recovery via domestic consumption taxes are generally effective for middle and high-income countries however it is substantially less efficient for low-income countries. In the same vein, previous findings revealed that the degree of revenue recovery via consumption taxation is generally effective for middle and high-income countries, bringing about dynamic efficiency gains and significant growth effects (Kim, 1998; Dahlby, 2003; Li & Sarte, 2004). Giving the fact that taxes on consumption are paid by final consumer thus it is not intended to let the businesses to bear the burden of the tax itself or add cost to businesses operation (RMCD, 2013; Ikpe & Nteegah, 2013). Concisely, it is pivotal for the Malaysia government to replace foreign aid flows with domestic tax revenues as the former are not a reliable long term source of development financing.

2. Literature Review

Mclure (1989) claimed that policy makers should consider and concern on the macroeconomic impact of VAT/GST particularly in prices, income and consumption along with its output before considering its adoption. In the same vein, GST was renowned for its smooth take-off in New Zealand at the time of its introduction back in year 1986, the Minister of Finance at that time Roger Douglas has pointed out, "Traders who would be collecting GST had to be assured they could 'cope' with the new tax (James & Alley, 2008)." In respect of this, Tajudin (2014) revealed that the capability of minimum household income or the less well-off families in their purchasing power to absorb shocks as a result from GST implementation in Malaysia has not reached. The author also stressed on the rise in the cost of living is not on an equal footing with salary increment. Additionally, the household debt by end-December year 2013 was recorded at the amount of RM 854.3 billion which is equivalent to 86.8 percent of GDP, making Malaysia the most heavily indebted nation in Asia (Tajudin, 2004). Subsequently, this will bring about the impact of macroeconomic shocks on household debt-servicing capacity and vulnerability for municipal to encounter monetary tightening prior to GST. Nevertheless, Nichita and Batrancea (2012) suggested that assessing the determinants is the prerequisite for increasing tax compliance.

2.1. Tax compliance

James and Alley (2004) defined that tax compliance as the willingness of individual and other taxable entities to act accordingly along with the letter of tax law and administration without the application of enforcement activity. In

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