A Proposed GST Compliance Model of GST Registered Person in Malaysia

Lee Heng Liang, Mohd Norfian Alfiaiah, Loo Ern Chen

Abstract: This paper attempts to identify the determinant factors that may influence the tax compliance behaviour of Goods and Service Tax (GST) registered persons in Malaysia. Revenue from broad based indirect taxation of consumption plays an important role in the Malaysian economy. The issue of GST compliance, such as over claiming of input tax and under declaring of output tax by the registered persons motivated this study. Thus, this study attempts to propose a conceptual framework for GST compliance behaviour by integrating economic factors such as tax system structure of GST, tax rate, audit, penalty and compound/fine, and psychological and sociological factors, including attitude towards GST and GST knowledge.

Index Terms: Keywords: GST; Tax Compliance Behaviour; Registered Person.

I. INTRODUCTION

Tax compliance is a global issue for developed and developing countries. Tax revenue is crucial to funding government spending on the provision of public goods and services. Hence, enhancing tax compliance is an important objective for governments and tax authorities. From a government’s view point, taxation is an important economic tool that can be used to generate economic growth and provide funds for national development projects (Kasipillai, 2005; Olaoye et al., 2017). These objectives can be achieved if taxpayers voluntarily comply with their tax obligations, thus generating higher tax collection and reducing tax gaps. In many countries, one way to achieve voluntary compliance is through introducing a self-policing tax system or a self-assessment tax system. The implementation of self-policing in the Goods and Services Tax (GST) system in Malaysia and also in other countries is to increase voluntary tax compliance, reduce administrative costs and simplify the tax structural system (Khadijah, 2014).

In a self-policing GST system, the assessment for tax liability lays with the GST registered persons. A ‘registered person’ is a person who is registered under the Goods and Services Tax Act 2014. Under the self-policing GST system, many GST registered persons are unaware of their responsibilities, particularly in ensuring accurate payments when filing GST returns and the consequences of submitting incorrect returns. Hence, issues concerning GST registered persons include their attitude and perception, as well as competency in GST knowledge, and the GST system structure (Natrah, 2010; Mohd Rizal, 2010). GST registered persons’ knowledge is important, as a lack of tax knowledge may result in unintentional non-compliance and consequently cause inaccurate tax payment (McKerchar, 1995).

Thus, tax system structure, such as fairness and tax simplicity are keys factors in improving tax compliance under the self-policing environment. According to Khadijah (2014), taxpayers would comply if they regard and perceive the tax system to be easy and simple to follow. In contrast, taxpayers may be deterred from complying, either intentionally or unintentionally if the tax system structure is complex and confusing (Loo and Ho, 2005). In order to overcome such problem, researchers had suggested that clear rulings and guidelines are needed to reduce complexity of the tax law. In Malaysia, the self-policing GST system was in force for three years and five months before it was revoked on 31st August 2018, following the change of government after the 14th General Election on 9th May 2018. Although, GST has been replaced with Sales Tax and Service Tax (SST) with effect from 1st September 2018, it is important to explore and evaluate the compliance behaviour of the GST registered persons in order to enhance tax compliance and to contribute to the literature in taxation.

The self-policing GST system required GST registered persons to voluntarily account for GST on taxable supplies made, claim the correct amount of input tax allowable, submit GST returns (GST-03) and pay the correct amount of tax by the due date, and to keep adequate and relevant records of all business transactions. However, studies have found that there has always been a reluctance to pay tax by taxpayers (Alm et al., 1992; Lamberton et al., 2014). In Malaysia, studies on indirect taxation revealed that tax compliance by SST and Excise Duty licensees, and importers and exporters is a problem (Sinnasamy et al., 2015; Zainol et al., 2015). Hence, this paper examines factors that may influence tax compliance behaviour of GST registered persons in Malaysia and proposed a GST compliance model so as to improve and enhance the Malaysia taxation system.

A. Indirect Taxation in Malaysia

In Malaysia, the Federal Government’s tax revenue is classified into direct tax and indirect tax. Direct tax is a tax which is imposed directly on taxpayers and paid directly to the tax authority by the persons on whom the tax is imposed. Indirect tax is where the tax burden imposed on the taxpayers may be distributed or transferred to another

Revised Manuscript Received on 04 May 2019
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person or a third party. Direct taxes are administered by the Inland Revenue Board of Malaysia (IRBM), while indirect taxes are administered by the Royal Malaysian Customs Department (RMCD).

Generally, direct taxes are imposed on income or gains. An indirect tax is generally based on expenditure incurred, and is also usually referred to as consumption tax. Consumption tax, also known as expenditure tax, is a tax paid by consumers as and when they spent on goods or services. As economists (Hall and Rabushka, 1995) put it, income tax is a tax on what people contribute to the economy, while taxing consumption tax is on what is taken out.

The Global Director of Indirect Tax 2015 reports that there are four trends that shape the global indirect tax landscape in the world. Firstly, indirect taxes continue to grow, while direct taxes stagnate; which means that GST systems are spreading and growing on a global scale. Secondly, indirectly tax systems are adapting to the new economic realities of e-commerce and virtual currencies to capture these transactions. Thirdly, the global trade landscape is changing and moving fast although there are trade restrictive measures in many regions of the world. Fourthly, tax authorities are focusing on efficiency and effectiveness of enforcement of tax audits in indirect taxes with new tools and legislations. Hence, in Malaysia, the government, through the RMCD has to embrace these changes in order to encourage registered persons to voluntarily comply for the effective collection of revenue.

In Malaysia, indirect taxes (before 1st September 2018) comprise of Customs Duty, Excise Duty, Windfall Profit Levy, Goods and Services Tax and Tourism Tax. To ensure efficiency of the tax system in terms of administration and payment of taxes, several laws have been enacted, such as the Customs Act 1967, the Excise Act 1976, the Windfall Profit Levy Act 1988, Goods and Services Tax Act 2014 and Tourism Tax Act 2017. Provisions in the legislations concerning fines/compound and penalties including prison sentences are to deter non-compliance and to mitigate revenue leakages. Nevertheless, the problem of non-compliance continues to increase every year and it poses a challenge to the RMCD (Zainol et al., 2015).

II. LITERATURE REVIEW

A. Tax Compliance Behaviour

History has shown that tax compliance is also a perennial problem to tax authorities and administrators, as tax laws are not always clear (James and Alley 2002). Andreoni et al. (1998) defined tax compliance as taxpayers’ willingness to obey tax laws, while Kirchler (2007) defined tax compliance as taxpayers’ willingness to pay their taxes. A more comprehensive definition of tax compliance is by Roth et al. (1989), who defined tax compliance as reporting all requirements in tax returns which accurately report tax liability in accordance with the revenue code, regulations and court decisions applicable at the time when the returns are filed.

As for this study, tax compliance means that GST registered persons willingly declare and accurately account for all GST due on the supply of taxable goods and services, while correctly claiming input taxes allowable as provided by the tax laws, guidelines and procedures. In addition, tax compliance means using the correct tax code accordingly to declare, in the correct taxable period and on time, based on either the accrual (invoice) or payment (cash) basis of accounting, by using the prescribed return Form GST-03 and keeping all records updated, aside from abiding with all the laws, rules, orders, and guidelines regardless of GST. Generally, tax compliance behavior means adhering to the tax laws. In Malaysia, non-compliance rate is about 20 percent (Lai et al., 2013) due to taxpayers not being fully aware of their tax responsibilities (Choong and Lai, 2008). Despite this, only a few studies have been conducted to examine the determinants of this phenomenon (Hijattullah, 2009) especially in the indirect tax system.

Compliance behaviour of taxpayers are also influenced by economics, psychological and sociological factors, such as taxpayers’ attitudes towards public institutions, knowledge, perception towards fairness of the taxes and complexity of tax laws, prevailing social norms, and the chances of non-compliance being detected and punished. These factors that influence tax compliance or non-compliance behaviour differ from one country to another and also from one individual to another (Alm, et al., 1995; Kirchler, 2007). Studies have found that non-compliance can be deterred through detection and sanctions. As such, the issue of compliance creates unhappiness among taxpayers with the tax authority, which led to this study.

B. GST System in Malaysia

1) An Overview

Goods and Services Tax, implemented on 1st April 2015 with a tax rate of 6 percent to replace the Sales Tax and Service Tax (SST) was part of the Government Transformation Programme (GTP) that was tabled on 25th October 2013 in Parliament (Alappatt and Shaikh, 2014). However, the GST rate of 6 percent was reduced to 0 percent effective from 1st June 2018 until 30th September 2018 [Malaysia Federal Government Gazette, P.U.(A) 118, 16th May 2018]. The implementation of GST has long been proposed by the International Monetary Fund (IMF) as a method to improve the efficiency of a tax system, to increase a country’s tax collection and to overcome budget deficits (Mohd Rizal et al., 2013).

The introduction of GST was a major tax reform in the Malaysia tax system over the last 30 years, and had a significant impact on revenue collection. GST mechanism has also been used by governments around the world, including in Malaysia, to collect revenue and tackle their countries’ budget deficits (Narayanan, 2014). According to the 2015/2016 Economic Report by the Finance Ministry of Malaysia, RM27 billion was collected in 2015 from GST, and had helped to cushion the blow of lower crude oil prices (Kasipillai and Krever, 2016).

In countries such as the United Kingdom, France, Denmark, Ethiopia and Nigeria, GST is also known as ‘Value Added Tax’ (VAT) (Behan and Jenkins, 2005; Kasipillai and Krever, 2016).
The term GST and VAT have therefore been used interchangeably (Loo and Mohd Shukry, 2017). Prior to 1st June 2018, the 6 percent GST rate that was implemented in Malaysia is the second lowest rate in the world after Yemen, which imposed a 2 percent GST rate, while the highest rate is in Hungary which practices VAT since 1988 and charges a 27 percent rate (RMCD GST Portal, 2014).

2) The GST Scope and Model

Pursuant to Section 9(1) GST Act 2014, GST would be levied on any supply of goods and services made in Malaysia and any goods imported into Malaysia. For the purpose of determining the requirement to be registered in GST system, Section 20(1) GST Act 2014 provided for mandatory registration if the annual turnover of a business exceeded RM500,000. The Malaysian GST model is divided into taxable supply and non-taxable supply, with four types of supply, namely: standard rated supply, zero rated supply, exempt supply and out of scope supply. Table I summarises the four types of supply in the Malaysian GST Model.

Table I: Types of Supply in Malaysia GST Model

<table>
<thead>
<tr>
<th>Types Of Supply</th>
<th>Rate of Output Tax</th>
<th>Input Tax</th>
<th>Goods and Service Applicable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard-rated</td>
<td>6%</td>
<td>Claimable</td>
<td>Local</td>
</tr>
<tr>
<td>Zero-rated</td>
<td>0%</td>
<td>Claimable</td>
<td>Local and Export</td>
</tr>
<tr>
<td>Exempt</td>
<td>No GST Charged</td>
<td>Not</td>
<td>Local (regulatory and enforcement), Non business outside Malaysia</td>
</tr>
<tr>
<td>Out Of Scope GST</td>
<td>No ambit in</td>
<td>Claimable</td>
<td></td>
</tr>
</tbody>
</table>

(Source: RMCD GST General Guide as at 24th August 2017)

There is a mechanism for input tax and output tax in the GST model for GST registered persons to determine the amount of GST payable to the RMCD. All imported goods would be subjected to GST, except those goods that are prescribed as zero-rated supply, exempt supply or given a relief from the payment. In summary, a GST registered person has to pay the tax to RMCD, if the output tax is more than the input tax incurred. Fig. 1 summarises the submission of return Form GST-03 by a registered person.

Fig.1: Submission of Tax Returns
(Source: RMCD GST General Guide as at 24th August 2017)

3) GST Strengths

GST is a comprehensive indirect tax system which covers each stage of the distribution network. GST is more effective, efficient, transparent and business friendly and able to spur economic growth in the global market. Due to the consumption nature of GST, it is capable of generating a more stable revenue because GST is less susceptible to economic fluctuations as compared to revenue from income tax and petroleum revenue (Liu and Lu, 2015; Kasipillai and Krever, 2016). Besides, GST can enhance the efficiency and effectiveness of the indirect taxation system, as it is a self-policing system, and has an in-build cross-checking feature. Comparatively, the GST system involves less bureaucracy as GST registered persons would manage their own accounting for tax.

4) GST Audit

A GST audit is a process of examining and verifying the correctness of GST returns and to determine the level of a registered person’s overall compliance with the GST legislations. The main objective of a GST audit is to encourage voluntary compliance. GST audits carried out periodically by the RMCD are also aimed at educating GST registered persons, as well as to create awareness of their rights and responsibilities under the provisions of the GST legislations. Generally, a GST audit may cover a period of three to six years, depending on the types of audit to be carried out. Nevertheless, the period to be covered in an audit may be less than three years in some cases. The audit period may extend beyond six years if initial findings reveal irregularities or existence of fraud. The RMCD General Guide dated 27th April 2016 states that there are eight types of GST audit that would be conducted by RMCD as shown in Table II.
A registered person is required to give his fullest cooperation to the RMCD auditors throughout the audit. During the course of an audit, the RMCD auditors should be allowed to examine all business records including records kept electronically and to physically inspect stocks and equipment for the purpose of the GST liability verification. All records which relate to supplies made and received by registered persons must be kept for seven years and be made available to the RMCD auditors.

5) Penalties/Fine in GST

Under the GST Act 2014, penalties may be imposed (see Table III) if the following offences are committed by the GST registered person when there are:
- Any deficiency on the net tax payable
- No GST return is made
- A GST return is submitted without payment or a lesser payment
- Any refund paid to which there is no proper entitlement
- Failure to register

Pursuant to Section 90 GST Act 2014, any person who commits an offence under the GST Act 2014 for which no penalty is expressly provided shall, on conviction, be liable to a fine of not exceeding thirty thousand ringgit or to imprisonment for a term not exceeding two years or to both.

C. Tax System Structure

A tax system structure can be classified as complex or simple depending on whether the tax system creates comfort and encourages compliance. In many developing countries, a tax system structure is commonly known to be one of the factors that cause tax non-compliance behaviour (Lutfi Hassen and Hijattullah, 2015). A study by Jackson and Milliron (1986) found that there are 14 key factors that influenced tax compliance. Later, Fischer et al. (1992) categorized the factors of Jackson and Milliron model into four groups, namely demographic, non-compliance opportunity, attitudes and perceptions and tax system structure.

Studies had discovered that tax system structure is a major determinant of tax compliance behaviour (Fischer et al., 1992; Jackson and Milliron, 1986; Richardson and Sawyer, 2001). Tax revenue of a country relies very much on the effectiveness and efficiency of its tax system (Alabede, 2012; Muzainah et al., 2005). The four factors that determine the effectiveness of the tax system structure in Fischer’s model are probability of detection, penalty, tax rate and complexity of tax system. Empirical studies also revealed that these factors are related to tax compliance behaviour (Chan et al., 2000; Fischer, 1993; Jackson and Millron, 1986).

1) Tax Rate

Tax rate can be one of the factors that influence taxpayers’ compliance behaviour (Fischer et al., 1992). Previous investigation on tax rate and tax compliance produced mixed and unclear results (Kirchler, 2007). Under the Economic Deterrence Theory, increases in tax rate will decrease taxpayers’ compliance level, as taxpayers are likely to underreport their tax liabilities (Alm et al., 1990, 1992; Clotfelter, 1983; Skinner and Slemrod, 1985). Higher tax rate will cause higher pressure on taxpayers towards non-compliance behaviour or to be less compliant (Alm et al., 1999; Atawodi and OJeka, 2012). Nevertheless, lowering tax rate would not necessarily increase tax compliance...
behaviour (Trivedi et al., 2004; Kirchler, 2007), as Mohd Rizal (2010) and Slemrod (2007) argued that tax rate has no effect on tax compliance, regardless of whether the tax rate is high or low. Based on these conflicting findings, effects of tax rate on compliance needs to be further studied, hence the hypothesis below.

H1: There is a relationship between tax rate and tax compliance behaviour of GST registered persons.

2) Tax Audit

The Deterrence Theory emphasises on incentives, whereby taxpayers would be influenced by economic motives to utilise the maximization of profit and probability of being audited to decide on either to comply or not to comply. Studies have shown that tax audits have a positive impact on tax non-compliance (Dubin, 2004; Jackson and Jaouen, 1989; Mohd Rizal and Ahmad Fariq, 2011), more so in a self-policing system, as tax audits can play a vital role in increasing voluntary tax compliance. Taxpayers would be more prudent in completing their tax returns, in reporting all income and claiming the correct deductions when there are tax audits. Engida and Baisa (2014) reported that taxpayers who have never been audited might be tempted to under-declare their revenue and to make false deduction. Thus, there are deterrence effects of tax audits on taxpayers’ compliance behaviour (Dubin, 2004; Mohd Rizal and Ahmad Fariq, 2011). A study by Alm et al. (2004) found that tax audits do have a direct deterrent effect on both taxpayers being audited and not being audited. Therefore, tax audits in the GST system are taken as a variable in this study due to inconsistent results.

H2: There is a relationship between tax audits and tax compliance behaviour of GST registered persons.

3) Penalty/Fine

Tax penalties/fines are punitive measures for failure to submit timely file returns or for under-declaring revenue (Oladipupo and Obazee, 2016). In a self-policing system, penalties and compounds/fines also play a significant part in influencing tax compliance. Mohd Rizal and Ahmad Fariq (2011) and Namusonge et al. (2014) revealed that penalties have an impact on tax compliance in a self-assessment and self-policing system. From the deterrence approach perspective, studies have shown that penalties are factors that influenced compliance behaviour (Allingham and Sandmo, 1972; Rillstone, 2015). High penalty discourages potential non-compliance. However, there are studies which found that penalties and fines/compounds are not related to tax compliance behavior (Webley et al., 1991; Mohd Rizal, 2010). Thus, there are no clear evidence on the impacts of penalties/fines on tax compliance behavior, that why this variable needs to be studied further.

H3: There is a relationship between penalty/fine and tax compliance behaviour of GST registered persons.

D. Attitude towards GST

In the Theory of Reason Action, attitude is an element consisting of feelings, beliefs and other emotional elements that influence a person decision in performing certain behaviour (Ajzen and Fishbein, 1980; Ajzen, 2005). In this context, attitude towards tax compliance refers to an individual’s assessment towards whether or not to comply with tax obligations based on emotional belief and behavioural belief. Thus, attitude is an important tax compliance determinant. Studies by Lumumba et al. (2010) and Abdullah et al. (2014) found that there is a very strong relationship between taxpayers’ attitudes and tax compliance. Taxpayers who have a positive attitude towards paying tax will have higher intention to pay and vice versa. A person’s attitude is motivated by a belief in the fairness of, and benefits received from the tax system, including belief in the government wisely spending the revenue collected (Walsh, 2012). Nonetheless, it is reasonable for attitude to be taken as a variable to be tested in this study, as attitude might change according to the time when GST was first implemented.

H4: There is a relationship between attitude and tax compliance behaviour of GST registered persons.

E. GST Tax Knowledge

Previous studies found that tax knowledge plays a vital role in influencing taxpayers’ compliance behaviour (Eriksen and Fallan, 1996; Mohd Rizal, 2010; Oladipupo and Obazee, 2016). Tax knowledge is defined as the ability of taxpayers to understand the tax laws and compute tax liability (Ahmad et al., 2007; Agbadi, 2011). Previous study reported that higher level of tax knowledge leads to higher compliance (Kasipillai and Hijjattullah, 2006; Kirchler et al., 2006; Loo et al., 2010a). In contrast, higher tax knowledge or education is also associated with better access to information to avoid taxes (Loo et al., 2010b). This finding is consistent with the findings of Braithwaite and Ahmed (2005) and McKerchar (1995) who found that the absence of tax knowledge causes either intentionally or unintentionally tax non-compliance. Taxpayers were found to have unintentionally committed mistakes in their tax returns due to their lack of tax knowledge (Loo et al., 2010a). Low level of education or tax knowledge may be related to low tax compliance (Bobek et al., 2007). The studies on tax knowledge as a factor affecting tax compliance revealed inconsistent and mixed results. Therefore, this study proposes to examine the effect of GST tax knowledge on tax compliance behaviour of the GST registered persons.

H5: There is a relationship between GST tax knowledge and tax compliance behaviour of GST registered persons.

III. RESEARCH CONCEPTUAL FRAMEWORK

This study applies the combination of the Deterrence Theory (an economic theory) and Fischer’s Model (which is based on psychological and sociological theories) in determining the factors that may influence tax compliance behaviour of the GST registered persons in Malaysia. This study also addresses the call by Kastlunger et al., (2013) that, in order to enhance taxpayers’ compliance behaviour, the economic factors as well as social and psychological factors have to be taken into consideration. The model of this study uses tax compliance behaviour as the dependent variable and tax system structure, attitude towards GST and GST knowledge as independent variables. The proposed Conceptual Framework of GST Registered Person...
Compliance Behaviour Model is illustrated in Fig. 2.

IV. CONCLUSION

This paper proposes the model of GST compliance behaviour of GST registered persons in Malaysia as compliance behaviour has been a perennial problem. Having a single comprehensive propose model of compliance would enable policy makers and tax authorities to have a better understanding of GST registered persons’ real and actual compliance behaviour when formulating suitable policies, guidelines and budgets for the country. In addition, this model would be able to enhance and improve voluntary tax compliance by incorporating economic factors of tax system structure (tax rate, tax audit, penalty and fine/compound) and social and psychological factors such as attitude towards tax and tax knowledge.

![Fig. 2: Compliance Model of GST Registered Persons in Malaysia](image)

REFERENCES


[58] Royal Malaysian Customs Department, GST General Guide as at 24th August 2017.


