Global Business and Management Research: An International Journal
Vol. 13, No. 4s (2021)

Determinant Factors of Tax Evasion

Siti Hawa Shuid *
Universiti Teknologi MARA Seremban Malaysia
Email: hawashuid@uitm.edu.my

Ainol Sarina Ahmad Zazili
Universiti Teknologi MARA Melaka Malaysia
Email: ainol776@uitm.edu.my

Siti Aisyah Basri
Universiti Teknologi MARA Melaka Malaysia
Email: aisyah936@uitm.edu.my

** Corresponding Author*

Abstract
Purpose: Tax evasion has become a major issue throughout the world. Literature revealed that tax evasion can deceive investors and public authorities, worsen unequal competition between the rich and poor, and significantly affect tax revenue collection. As there is an increasing issue of tax evasion all over the world, it is a concern whether people will become more tolerable toward this financial crime. On the basis of this premise, this study explores the key determinant factors that may influence taxpayers to commit tax evasion.
Design/methodology/approach: This is primarily a conceptual paper. Statistical analysis will be used to examine individuals' perspectives on tax evasion. Data will be collected using a questionnaire from undergraduate students at a public university.
Findings: Based on the review of past literature, it was found that there are four main categories of determinant factors that influence tax evasion; (1) demographic; (2) cultural and behavior; (3) legal and institutional; and (4) economic factors.
Research limitations/implications: This is a theoretical paper, lacking empirical research.
Practical implications: The results of this study are expected to be useful for the tax authorities in taking proactive measures to curb tax evasion by developing strategies and creating a new model based on the specific profile of taxpayers as well as the key determinant factors why people cheat on tax.
Originality/value: The study contributes to the tax evasion literature by revealing the key determinant factors of this financial crime activity.
Paper type: Conceptual paper

Keywords: Determinant factors, Financial crime, Tax evasion, Tax fraud

Introduction

Tax evasion has created a great deal of concerns for countries around the globe, as it has become a common occurrence in both developed and developing countries. Apart from money laundering and international bribery, which have negative consequences on the country's social and economic system, this financial crime has been identified as one of the key activities that can generate illicit financial flows (Organisation for Economic Co-operation and Development, 2014; United Nations, 2020). Tax evasion or tax fraud can be characterised as the purposeful

misrepresentation or hiding of the essential state of a business's affairs in order to lower the amount of tax that must be paid (Akhtar et al., 2019).

This financial crime can have an extremely negative effect on the collection of government revenue. As reported by the OECD (2014), because developing nations have fewer resources, tax evasion has a greater social and economic impact. It may exacerbate societal inequity by promoting income disparity, and, worst of all, people may react immorally to the tax system by becoming tax evaders (Vousinas, 2017). Furthermore, the massive loss of revenue may force countries to run fiscal deficits, necessitating the continued use of enormous quantities of debt, putting even more strain on already fragile developing economies (Alleyne & Harris, 2017; Vousinas, 2017). The difficulty in predicting the magnitude of tax evasion (Hearson, 2019), as well as the lack of consistent statistics (United Nations, 2020) due to the fact that tax evasion is hard to trace and is associated with the black economy (Khlif & Achek, 2015), could restrict the authority to combat this serious offence. Malaysia, too, has experienced difficulty in the absence of official statistics on tax evasion, but the Inland Revenue Board of Malaysia (IRBM) enforced tax investigation as a step to curb tax evasion in Malaysia (IRMB, 2020). Unfortunately, findings from the tax investigation revealed that there were some taxpayers involved in financial reporting fraud, which resulted in lower tax payable. In 2012 alone, the IRBM was credited with resolving 764 cases totalling RM695.66 million in taxes and fines (Inland Revenue Board of Malaysia, 2013). Tax evasion cases in Malaysia stayed on a rising trend from 2012 to 2016, as evidenced by the taxes and penalties charged, as shown in Table 1. As tax evasion becomes more common in all countries, it's unclear whether this crime will grow more socially accepted. Furthermore, the IRBM's direct taxes account for more than fifty percent of the national revenue, and this never-ending condition will result in significant tax revenue losses.

Therefore, this study aims to explore the key determinant factors that may drive taxpayers to engage in tax evasion by reviewing the empirical literature. The identification of key determinant factors that could influence tax evasion is possibly more crucial in developing countries because tax evasion has become one of the major sources of illicit financial flows. Hence, the target of combating illicit financial flows by year 2030 must be on the national agenda as a support to achieving one of the targets of the Sustainable Development Goals.

The remainder of this paper is structured as follows. Section 2 discusses the underpinning theory related to the determinant factors of tax evasion. Section 3 briefly reviews the literature related to the determinant factors of tax evasion. Section 4 describes the prospective research methodology. Section 5 presents the conclusion.

Table 1: Resolved Tax Investigation Cases in Malaysia

Year	Number of Resolved Tax Investigation	Amount of Taxes and Penalties (RM Million)
2012	764	695.66
2013	588	486.56
2014	689	543.96
2015	1,063	755.44
2016	1,212	844.68

Source: Annual Report IRBM 2013, 2015 and 2016

Relevance Theory

There are two theoretical perspectives that attempt to explain why taxpayers evade the tax. These are the theory of planned behaviour and the economic deterrence model.

According to the theory of planned behaviour, three determining elements can predict a taxpayer's intention to undertake behaviours: attitudes, subjective norms, and perceived behavioural control (Ajzen, 1991). In turn, this taxpayer's intention can influence the actual behaviour. Another aspect that motivates taxpayers to engage in interest-based behaviour is moral obligation (Beck & Ajzen, 1991). This theory considers cultural and behavioural factors as determinant factors which may influence tax evasion activities.

Meanwhile, in an economic deterrence model, economically rational taxpayers are believed to be motivated to cheat taxes as long as the pay-off from evasion outweighs the expected cost of detection (Allingham & Sandmo, 1972). Taxpayers have some level of risk aversion. The more risk-averse taxpayers are, the less likely they are to evade taxes (Hasseldine & Bebbington, 1991). This model considers both legal and institutional (e.g. complexity of tax laws, tax rates, tax penalty) and economic as determinant factors which may influence tax evasion activities.

In conclusion, these models might be viewed as complimentary aspects in explaining why people avoid paying taxes. Tax evasion is motivated not just by the economic rewards and costs of tax evasion, but also by non-economic variables relating to taxpayers' psychological characteristics.

Determinant Factors That Could Influence Tax Evasion

This study identified four key categories of determinant factors that could influence people and company to evade tax by referring to study done by Mohamad et al. (2016), Khlif and Achek (2015) and Richardson (2006). The four main categories are (1) demographic; (2) cultural and behavior; (3) legal and institutional; and (4) economic factors.

Demographic Factors

Among demographic factors that would encourage tax evasion are age, gender, level of income, source of income, and tax return forms completed by tax practitioners. Alasfour et al. (2017) claimed that young people are more likely to cheat on their tax obligations. They argued that the threat of punishments affects older people more than younger people. However, Che Rosli et al. (2018) found that because they have more time to build wealth, older people make up a bigger share of those participating in tax evasion.

With regard to the gender of taxpayers, the results have been mixed. While Che Rosli et al. (2018) reported that males are more likely to be involved in tax fraud than females, other studies have found that females seem to be more likely than males to participate in tax fraud (Alasfour et al., 2017; McGee & Guo, 2007).

According to Alleyne and Harris (2017), taxpayers with a higher income are more likely to commit tax fraud than those with a lower income. In the Malaysian context, however, Tabandeh et al. (2012) identified that there is a negative relationship between tax payers' income and tax evasion. This is because Malaysia's tax rate has been decreasing for the past ten years. This implied that people with lower incomes tended to evade their taxes.

The source of income does play an important role in tax behaviour. A vast majority of the research found that sole proprietorships or self-employed individuals have a better opportunity to evade taxes compared to individuals with employment income (Che Rosli et al., 2018; Richardson, 2006). They transfer the income or profit to their businesses overseas. Saad (2014) noted that self-employed taxpayers seemed to have an insufficient understanding of the relevant aspects of the regulated tax laws, which may have contributed to this crime.

The provision of tax return filing services by tax practitioners is another determinant factor to consider. In the most recent research, Che Rosli et al. (2018) found that tax practitioners such as accountants and financial consultants play a role in escalating harmful tax practices. In the same vein, Erard (1993) claimed that professional aid had a detrimental impact on tax equity

and tax efficiency. The opposite result was obtained by Mohamad et al. (2016), who used data comprised of small and medium-sized enterprises (SMEs). They discovered that SMEs without tax practitioners appear to have a strong incentive to avoid paying taxes. Tax practitioners have a better understanding of accounting and tax procedures, so SMEs who hire them are less likely to evade taxes.

Other factors that may have an influence on tax evasion cases are the level of education and the types of tax evasion. Vousinas (2017) and Richardson (2006) found that the lower level of education leads to higher tax evasion. Less educated taxpayers do not fully understand that taxation is the main revenue source for funding the public goods which fulfil crucial social needs. Based on research done by Marriott and Sim (2017) and Alasfour et al. (2017), they found that those with a lower level of education were more likely to recommend that there were no differences between two different crimes. However, more educated respondents with an undergraduate or postgraduate qualification can recognise a dissimilarity between different crimes.

Md Noor et al. (2012) found that types of tax evasion, such as sales, working capital, and debts, were significantly associated with a company's tax evasion. They provided evidence that financially viable businesses with high turnover and debt had a greater tendency to evade tax. This contradicts the findings of Alm et al. (2018), who found that financially strained businesses are substantially more likely to evade tax. This is because tax evasion activities help companies deal with financing issues caused by resource constraints.

Cultural and Behavioural Factors

There are many factors that can be categorized under cultural and behavioural factors. Among the factors are attitude, perceived behavioural controls, fairness perception, social exchange, and moral obligations.

Non-compliance with the tax laws can also be attributed to a greedy attitude among taxpayers. They lack the sense of community to share their income with other citizens (Saad, 2014). Alleyne and Harris (2017) found that people who have negative attitudes against tax fraud are less motivated to be involved in this financial crime. The average person does not regard tax fraud as a severe unlawful act (Benk et al., 2015; Marriott & Sim, 2017). This perception, along with a lack of prosecution attempts, might contribute to some people's being willing to cheat on their tax obligations.

Perceived behavioural control is also identified as another important determinant factor of tax evasion. According to Alleyne and Harris (2017), taxpayers who have a low perception of their potential to evade tax are less inclined to do so. The taxpayers were seriously worried about being penalised. However, according to Saad (2014), high perceived behavioural control provides incentive for them to refrain from tax obligations. The taxpayers believe that the possibility of getting caught is lower. The effect is stronger with assistance provided by the accountants.

One predictor of tax evasion is also found to be fairness perceptions of the income tax system. They had evaded paying taxes due to a perceived lack of trust in the income tax system, notably in the income tax rates and utilization of government expenditure (Alleyne & Harris, 2017; Richardson, 2006; Saad, 2014). The average taxpayer is dissatisfied with paying taxes because he believes the government is taking a piece of his income (Malkawi & Haloush, 2008).

The benefit or direct reward obtained from the public service in exchange for the payment of taxes is known as social exchange (Yee et al., 2017). However, taxpayers in Jordan believe that there are no infrastructural upgrades for public convenience, hence, there is no reason to fund the government's activities (Malkawi & Haloush, 2008).

A strong sense of moral obligation has also been viewed as an important variable in tax fraud. Tax evasion is less prevalent among individuals who have a strong moral obligation (Alleyne & Harris, 2017; Richardson, 2006).

Legal and Institutional Factors

In addition to the two aforementioned factors, many studies also include a large number of legal and institutional factors as determinants of tax fraud. The determinant factors consist of higher tax rates, ambiguity of the tax policy, frequent changes in tax law, size of the government, favours and cronyism, and lack of enforcement.

Higher tax rates, according to previous studies, are the driving force behind tax evasion activities (Alm et al., 1992; Bayer, 2006; Bayer & Sutter, 2009; Crane & Nourzad, 1986). According to Vousinas (2017), Bayer and Sutter (2009) and Bayer (2006), higher tax rates result in a higher tax burden when compared to the aggregate income. This indicates that more money is being wasted on the income hiding and detection process. The statutory corporate tax rate influences multinational corporations ("MNCs") propensity for tax evasion (Akhtar et al., 2017). An increase in tax rates will encourage individuals to engage in tax evasion activities since they do not see any benefits from the public goods that are paid for by their tax obligations (Alm et al., 1992).

The ambiguity of the tax policy, which forces individuals into non-compliance behaviours, also promotes taxpayers' engagement in tax evasion activities (Saad, 2014; Richardson, 2006). When direct taxes, such as income taxes, dominate the tax system, there is a greater incentive to cheat the system since businesses have more avenues to hide their tax responsibilities than individuals (Vousinas, 2017).

A frequent change in income tax laws has also become a significant factor in tax evasion. This made it difficult for taxpayers to complete their tax returns correctly (Malkawi & Haloush, 2008). Tabandeh et al. (2012) found that government size had a strong influence on tax fraud. It becomes more difficult for the government to keep control over each sector of the economy as it expands in size. As a result, tax evasion has grown commonplace in that environment.

Taxpayers may be hesitant to file accurate returns due to apparent favours and favouritism in the environment. Tax evasion is more common among well-connected businesses and individuals (Malkawi & Haloush, 2008).

The classical model developed by Allingham and Sandmo (1972) claims that effective tax evasion depends on prosecution and on the expected benefits of tax fraud. When the predicted benefits outweigh the penalty of tax evasion, taxpayers will avoid paying taxes.

Economic Factors

Economic factors also play a role in the increased rate of tax evasion. The major factors are inflation, trade openness, the extent to which the economy has developed and is organised, and the degree of market and business organization.

Inflation is one of the significant determinants of tax non-compliance. Many past studies have proved that tax evasion is positively related to inflation (Caballe & Panade, 2004; Crane & Nourzad, 1986). Taxpayers prefer to keep their money throughout a price hike in order to maintain their net wealth. This economic situation may make taxpayers hesitant to meet their tax obligations. The penalties and fines imposed on audited taxpayers become smaller in real terms. The revenue accruing from the penalties and fines, therefore, turns out to be decreasing (Caballe & Panade, 2004; Tabandeh et al., 2012).

Tabandeh et al. (2012) found adopting more complicated regulations and tighter government controls on commerce leads to an increase in smuggled goods, which encourages tax evasion. As Vousinas (2017) points out, well-organised economies may readily reduce the trend of tax

evasion. Any transactions involving taxpaying units can be easily tracked. To properly carry out their task, the tax authorities may have more reliable information, such as transaction documentation.

Vousinas (2017) discovered that when the economy is structured in such a way that important economic transactions are conducted in kind, the likelihood of tax evasion increases. When all transactions are completed in cash, evasion activities will be decreased.

Prospective Research Methodology

The research is a quantitative research. The individuals' perspectives on tax evasion will be investigated through statistical analysis. The survey questionnaire will be adapted from McGee and Guo (2007). The survey questionnaire will approximately consist of 15 statements. This survey questionnaire will use a five-point Likert scale.

This questionnaire will be disseminated to undergraduate students in UiTM Negeri Sembilan, UiTM Melaka and UiTM Johor. These UiTM's branches are located in the southern region of Peninsular Malaysia. This group of respondents was chosen because they will be potential Malaysian taxpayers.

This research plans to use the sample-to-item ratio as its basis to determine the sample size. Memon et al. (2020) has cited that a 20-to-1 ratio has been used in many previous studies. Therefore, this research will need 300 respondents.

Conclusion

The high prevalence of tax evasion has had a substantial impact on government revenue, which may make it harder for the government to supply greater social services. As a result, the government should take a number of actions in order to promote voluntary tax compliance and combat tax evasion. The actions that should be taken rigorously are providing tax knowledge and education, performing tax audits and tax investigations extensively, enforcing stricter tax laws, and improving tax fairness. The IRBM must ensure that tax evasion is made a crime and that it is made public.

Practical and Social Implications

This study is intended to assist tax authorities to take proactive measures to curb tax evasion by developing strategies and creating a new model based on the specific profile of taxpayers as well as the key determinant factors why people evade tax. As a result, the goal of significantly reducing illicit financial flows by 2030 must be placed on the national agenda as a means of achieving one of the Sustainable Development Goals.

Limitations and Suggestions for Future Research

This is a theoretical paper, lacking empirical research. Therefore, further research will be focusing on the perspective of tax evasion among future taxpayers in Malaysia.

Acknowledgment

The authors are grateful to the management of Universiti Teknologi MARA (UiTM) and Money Laundering Research Group (MLRG) for their beliefs and continuous support.

References

Ajzen, I. (1991). The theory of planned behaviour. *Organisational Behavior and Human Decision Processes, 50*(2), 179-211. https://doi.org/10.1016/0749-5978(91)90020-T

Akhtar, S., Akhtar, F., John, K., & Wong, S.W. (2017). Multinationals' tax evasion: A financial and governance perspective. *Journal of Corporate Finance, 57,* 35-62. https://doi.org/10.1016/j.jcorpfin.2017.11.009

Alasfour, F., Samy, M. & Bampton, R. (2017). The determinants of tax morale and tax compliance: Evidence from Jordan. *Advances in Taxation, 23,* 125-171. https://doi.org/10.1108/S1058-749720160000023005

Alleyne, P., & Harris, T. (2017). Antecedents of taxpayers' intentions to engage in tax evasion: Evidence from Barbados. *Journal of Financial Reporting and Accounting, 15* (1), 2-21. https://doi.org/10.1108/JFRA-12-2015-0107

Allingham, M.G., & Sandmo, A. (1972). Income tax evasion: A theoretical analysis. *Journal of Public Economics, 1,* 323-338. https://doi.org/10.1016/0047-2727(72)90010-2

Alm, J., Jackson, B., & McKee, M. (1992). Estimating the determinants of taxpayer compliance with experimental data. *National Tax Journal, 45,* 107–114. https://doi.org/10.1086/NTJ41788949

Alm, J., Liu, Y., & Zhang, K. (2018). Financial constraints and firm tax evasion. *International Tax Public and Finance, 26,* 71-102. https://doi.org/10.1007/s10797-018-9502-7

Bayer, R.C. (2006). A contest with the taxman – The impact of tax rates on tax evasion and wastefully invested resources. *European Economic Review, 50,* 1071–1104. https://doi.org/10.1016/j.euroecorev.2005.03.002

Bayer, R.C., & Sutter, M. (2009). The excess burden of tax evasion—An experimental detection–concealment contest. *European Economic Review, 53,* 527–543. https://doi.org/ 10.1016/j.euroecorev.2008.09.004

Beck, L., & Ajzen, I. (1991). Predicting dishonesty actions using the theory of planned behavior. *Journal of Research in Personality, 25,* 285-301. https://doi.org/10.1016/0092-6566(91)90021-H

Benk, S., Budak, T., Püren, S., & Erdem, M. (2015). Perception of tax evasion as a crime in Turkey. *Journal of Money Laundering Control, 18*(1), 99-111. https://doi.org/10.1108/JMLC-04-2014-0012

Caballe, J., & Panade, J. (2004). Inflation, tax evasion, and the distribution of consumption. *Journal of Macroeconomics, 26,* 567–595. https://doi.org/ 10.1016/j.jmacro.2003.06.001

Che Rosli, R., Ling, L.M., & Embi, R. (2018). Tax malfeasance of high net-worth individuals in Malaysia: Tax audited cases. *Journal of Financial Crime, 25*(1), 155-169. https://doi.org/10.1108/JFC-11-2016-0070

Crane, S.E., & Nourzad, F. (1986). Inflation and tax evasion: An empirical analysis. *The Review of Economics and Statistics, 68*(2), 217-223. https://doi.org/10.2307/1925500

Erard, B. (1993). Taxation with representation: An analysis of the role of tax practitioners in tax compliance. *Journal of Public Economics, 52*(2), 163-197. https://doi.org/10.1016/0047-2727(93)90019-P

Hasseldine, J., & Bebbington, K.J. (1991). Blending economic deterrence and fiscal psychology models in the design of responses to tax evasion: The New Zealand experience. *Journal of Economy Psychology, 12,* 299-324. https://doi.org/10.1016/0167-4870(91)90018-O

Hearson, M. (2019). Fair tax for development. *Sustainable Goals.* https://www.sustainablegoals.org.uk/fair-tax-for-development/

Inland Revenue Board of Malaysia. (2013). *Annual Report 2013.* http://phl.hasil.gov.my/pdf/pdfam/ANNUAL_REPORT_2013_bi.pdf

Inland Revenue Board of Malaysia. (2015). *Annual Report 2015.* http://phl.hasil.gov.my/pdf/pdfam/annual_report_2015.pdf

Inland Revenue Board of Malaysia. (2016). *Annual Report 2016.* http://phl.hasil.gov.my/pdf/pdfam/annual_report_2016.pdf

Inland Revenue Board of Malaysia. (2020). *Public Ruling: Tax Investigation Framework*. http://www.hasil.gov.my/pdf/pdfam/Tax_Investigation_Framework_2020_2.pdf

Khlif, H., & Achek, I. (2015). The determinants of tax evasion: A literature review. *International Journal of Law and Management*, *57*(5), 486-497. https://doi.org/10.1108/IJLMA-03-2014-0027

Malkawi, B.H., & Haloush, H.A. (2008). The case of income tax evasion in Jordan: Symptoms and solutions. *Journal of Financial Crime*, *15*(3), 282-294. https://doi.org/10.1108/13590790810882874

Marriott, L., & Sim, D. (2017). Tax evasion and welfare fraud: Do punishments fit the crime or the perception of the crime? *Pacific Accounting Review*, *29*(40), 573-589. https://doi.org/10.1108/PAR-10-2016-0094

McGee R.W., & Guo, Z. (2007). A survey of law, business and philosophy students in China on the ethics of tax evasion. *Society and Business Review*, *2*(3), 299-315. https://doi.org/10.1108/17465680710825488

Md Noor, R., Abdul Aziz, A., Mastuki, N.A., & Ismail, N. (2012). Tax fraud indicators. *Malaysian Accounting Review*, *11*(1), 43-57. https://ari.uitm.edu.my/main/images/MAR/vol11-1/chap3.pdf

Memon, M.A., Ting, H., Cheah, J., Ramayah, T., Chuah, F., & Cham, T.H. (2020). Sample size for survey research: Review and recommendations. *Journal of Applied Structural Equation Modeling*, *4*(2), i-xx. https://doi.org/ 10.47263/JASEM.4(2)01

Mohamad, A., Zakaria, M.H., & Zarinah, H. (2016). Cash economy: Tax evasion amongst SMEs in Malaysia. *Journal of Financial Crime*, *23*(4), 974-986. https://doi.org/10.1108/JFC-05-2015-0025

Organisation for Economic Co-operation and Development (OECD). (2014). *Illicit financial flows from developing countries: Measuring OECD responses*.https://www.oecd.org/corruption/Illicit_Financial_Flows_from_Developing_Countries.pdf

Richardson, G. (2006). Determinants of tax evasion: A cross-country investigation. *Journal of International Accounting. Auditing and Taxation*, *15*, 150–169. https://doi.org/ 10.1016/j.intaccaudtax.2006.08.005

Saad, N. (2014). Tax knowledge, tax complexity and tax compliance: Taxpayers' view. *Procedia: Social and Behavioural Sciences*, *109*, 1069-1075. https://doi.org/ 10.1016/j.sbspro.2013.12.590

Tabandeh, R., Jusoh, M., Md. Nor, N.G., & Zaidi, M.A.S. (2012). Estimating factors affecting tax evasion in Malaysia: A neural network method analysis. *Prosiding Perkem VII*, *2*, 1524-1535. https://www.ukm.my/fep/perkem/pdf/perkemVII/PKEM2012_5D4.pdf

United Nations. (2020). *SDG Pulse 2020: UNCTAD takes the pulse of the SDGs.* https://sdgpulse.unctad.org/wp-content/uploads/Unctad_SdgPulse_2020.pdf

Vousinas, G. L. (2017). Shadow economy and tax evasion. The Achilles heel of Greek Economy. Determinants, effects and policy proposal. *Journal of Money Laundering Control*, *20*(4), 386-404. https://doi.org/10.1108/JMLC-11-2016-0047

Yee, C.P., Moorthy, K., & Soon, W.C.K. (2017). Taxpayers' perceptions on tax evasion behaviour: An empirical study in Malaysia. *International Journal of Law and Management*, *59*(3), 413-429. https://doi.org/10.1108/IJLMA-02-2016-0022