

**IMPORT TAX COMPLIANCE: A STUDY OF  
CUSTOMS AGENTS IN MALAYSIA UTILISING  
THE THEORY OF PLANNED BEHAVIOUR**

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# **ABSTRACT**

Unlike tax accountants and advisors within direct tax, Customs law in many countries requires importers to employ licensed Customs agents. This study extends the tax literature by examining the role of Customs agents in import tax compliance. In Malaysia, as an example of a country where Customs are responsible for about one-third (MYR30 billion on average between 2005 to 2014) of total government revenue collections, the function of Customs agents is to: assist importers in meeting their import tax liabilities; prepare and submit all necessary import documentation to Customs; as well as collect and pay all revenue to the Customs administration. Customs agents are bound by the Customs Act 1967 and are required to pass a public exam before becoming formally qualified and licensed Customs agents.

Exploratory interviews with senior Customs officers at The Royal Malaysian Customs Department (RMCD) suggest that a significant amount of tax revenue is lost because Customs agents do not pay the full amount of import duty and tax due. Most interviewed officers felt that tougher penalties and sanctions are required to improve compliance and root-out fraud; though some indicated that other measures may need to be developed in order to improve compliance practice.

Drawing on the tax compliance literature within the direct tax domain, the Theory of Planned Behaviour (TPB) has been identified as one of the most robust social cognitive theories to explain compliance decision making. A key output from this research is a compliance behaviour model (based on the theory of planned behaviour) that depicts various economic and non-economic variables to predict compliance behaviour.

Building on the model, a large scale survey of Customs agents across Malaysia was conducted. Overall, the response rate was 42% (n=650), representing 12.8% of the total Customs agents population located at Malaysia's primary ports of entry. The results indicate that psychological, sociological, structural / institutional factors, which consist of attitude, ethical beliefs, social norms, law, enforcement, complexity of procedure and quality of tax assessment service, are significant in explaining Customs agents' behavioural intention to comply with import tax law. However, they also suggest inconsistencies in the relationship between behavioural intention and behaviour, and the need to incorporate other factors and moderating



variables. In particular, the findings identified the influence of two referent groups (subjective norms): (i) the importers who influenced Customs agents' import tax compliance directly through instructions, as well as indirectly by sharing their ethical beliefs; and (ii) other Customs agents (their peers) who influence Customs agents' ethical beliefs.

Overall this study highlights the importance of incorporating behavioural elements and facilitating elements (such as better quality of tax assessment service and less complex procedures) together with economic variables to achieve an optimum compliance level. The findings indicate that simply applying sanctions to improve Customs agents' compliance, as is Royal Malaysian Customs current enforcement strategy does not optimise revenue yield. Appropriate reforms that go beyond sanctions and enforcement are recommended. It also identifies another essential but largely neglected strategy for improving compliance which is to work on improving the ethics of Customs agents, possibly by offering access to trade facilitation measures, or through coercion (e.g. public naming and shaming) and sanctions (e.g. withholding access to trade facilitation measures). Finally, this study also demonstrates the wide applicability of the TPB, including its application in tax compliance research and specifically in the context of import tax. The method (exploratory sequential mixed method) used in this study could also be used to replicate further studies to generate a more holistic compliance behaviour model.

# **CHAPTER 1**

## **INTRODUCTION**

### **1.1 RESEARCH MOTIVATION**

This study is an empirical investigation into the role of Customs agents in import tax compliance. The research objective focuses on assessing the factors that influence import tax compliance.

In relation to the motivation for such studies, Atkinson, Coffey and Delamont, (2003, p.99) assert that, ‘social scientists do not dream up “problems” to be investigated out of thin air’. The research problems and the selection of a particular research context are often a personal choice driven by curiosity. In my case, the curiosity to conduct a study in the area of import tax is the result of my work experience of more than 10 years as a senior officer of Customs, before embarking on my PhD study under the sponsorship of the Public Services Department of Malaysia.

I started my career with Customs back in the year 2000. My first placement was with the Customs Audit Division, where my role was to perform audit on businesses’ accounting records of Customs’ sales and service tax license holders (commonly known as VAT or GST registrants) to ensure that the tax collected from customers remitted to Customs. Having a background, and previous experience, as an internal auditor and accountant gave me an added advantage in detecting any element of manipulation in the accounting systems. The main objective was to detect any form of leakages in tax revenue. Businesses which did not comply with the law were penalised. I remember a case in which I managed to detect false accounting. Here, the business owner had to sell his property and land to settle the tax due, including the penalty which amounted to close to 1 million MYR (Malaysian Ringgit, more than GBP200,000). The owner told me that he was forced into this situation because of cash flow problem in his business. Although I felt sorry for him, as I mentioned, it was part of my work and what he did was against the law. I embarked on my Masters Degree studies soon after that. After completion of the study, I was placed in the import division and, later, I was put in-charge of Customs bonded warehousing. One of the challenging tasks for a tax assessment officer in the import

division is to ensure that duties and taxes on imported goods are paid correctly when conducting tax assessment<sup>1</sup> on import declaration<sup>2</sup>. Businesses, on the other hand, require the Customs to expedite the Customs clearance process. In most cases, Customs agents are employed by importers or exporters to handle Customs clearance matters due to complex regulatory requirements and various Customs procedures; hence reducing their compliance burden. Furthermore, Customs agents are legal third parties, authorised by the Customs administration to provide Customs related services, due to their knowledge and expertise.

As tax collection is their main concern, each import declaration is scrutinised to ensure that revenue (tax payment) is paid and collected accordingly. Technical knowledge is essential for the tax assessment officer to accurately assess tax payment and also to expedite the process<sup>3</sup> and avoid congestion at the port due to delay in Customs processing. Through the course of my work, I identified many cases of erroneous import declarations such as the misclassification of products, unclear descriptions, and declaring products at an uncommonly low price (more details are given in Chapter 2). The terms used may sound too technical for a person who has no background in, or exposure to, Customs, port and logistic industries. The intention may have been to evade tax or it may have been purely an unintentional mistake, which is not easy to prove. Whether mis-declaration in Customs import declarations is intentional or unintentional, either by Customs agents or importers, these errors are viewed as an act of tax evasion or non-compliance with import tax law. This is the reason why some unresolved cases end up in a court of law. With reference to the Malaysian Customs Act 1967, it is the obligation of the owner of goods to provide a true view of the goods imported. Failing to do so may result in heavy penalty or imprisonment. It is the responsibility of the Customs officer, who has a legal mandate to conduct tax assessment, to reassess the tax declaration if it is found that there is any form of non-compliance, such as mis-declaration. In most cases, the reassessment of tax is agreed upon by the business, and is not contested. Businesses account, and pay, for any difference in tax payment to avoid delays in the release of their cargo. These

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<sup>1</sup> Tax assessment involves checking correct product classification and price valuation, and verifying the country of origin that reflects tax computation and the final tax amount.

<sup>2</sup> Import declaration is the declaration on the description of imported goods for the purpose of determining the respective tax according to product classifications.

<sup>3</sup> One of the objectives of Customs administration is to facilitate trade movement such as speeding up the customs clearance process, whilst ensuring that tax is collected accordingly. This is part of the trade facilitation policy suggested by the World Customs Organizations (WCO).

are some examples from my experience that demonstrate the relevance of tax revenue to Customs administration and how tax non-compliance is viewed from the perspective of Customs employees. Besides personal interest or ‘curiosity’, the empirical focus on import tax<sup>4</sup> is relevant to this study. Import tax and other indirect tax<sup>5</sup> regimes provide important tax revenue for the country (OECD, 2012). In a country such as Malaysia, whose economy is progressively developing, tax revenue is very important for financing government expenditure and for the economic well being of the country. The Royal Malaysian Customs Department is the second largest tax collection agency for the government, after the Inland Revenue Board (IRB). The primary function of the department is to collect indirect tax revenue such value added tax (VAT) and import tax. Import tax accounts for more than one third of the indirect tax revenue of Malaysian Customs. In a recent government transformation programme (GTP) in Malaysia, one emphasis was on indirect tax reform, which includes the introduction of goods and services tax (GST)<sup>6</sup> in an effort to boost tax revenue. As GST is part of import tax (referred to as GST on import), it is expected to significantly increase the share of the indirect tax contribution to the government.

Many developing countries are still struggling to raise tax revenue for economic growth. Among the factors that contribute to revenue generation for the government is the level of tax compliance (Alabede, Ariffin and Idris, 2011). High levels of non-compliance could affect the revenue generated for the governments (Eshag, 1983). Without the ability to raise revenues effectively, countries are limited in terms of providing security, meeting basic needs or fostering economic development (Brautigam, Fjeldstad and Moore, 2008).

In reference to tax non-compliance for a country such as Malaysia, improving compliance levels is a challenging task, especially when considering various ethnicities, cultural backgrounds, geographical locations and the historical period of the Malacca Sultanate Empire in the 14<sup>th</sup> century, where the problem of compliance with duty payments originates. The problem of non-compliance is an internationally recognised on-going concern that poses a challenging problem for policy makers, tax

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<sup>4</sup> Import tax, depending on the type of product, generally consists of three elements, which are import duty, excise duty and sales tax.

<sup>5</sup> Indirect tax is the tax imposed on consumable goods or services such as GST/VAT, petroleum duty, import duty and excise duty.

<sup>6</sup> GST is a type of tax imposed on the consumption of either goods or services. It is commonly known as value-added tax (VAT) in some countries.

authorities and ultimately, society (McKerchar, 2001). Administering the tax system is a challenging task for any administration in any country, especially when facing tax non-compliance, which is commonly associated with a tax gap<sup>7</sup> (James and Alley, 2002). Although tax non-compliance can sometimes be an intentional act of deliberately understating tax, in many cases it is unintentional due to a lack of knowledge, ignorance, mistakes in reporting tax or the complexity in the tax system itself (Brand, 1996). According to the Malaysian Customs Department, tax non-compliance associated with under-declaration of import taxes results in losses of revenue amounting to MYR8 billion (GBP1.6 billion) uncollected duties and taxes yearly (The Star, 2012). Published studies and reports indicate that tax non-compliance such as indirect tax evasion is prevalent in developing countries and results in significant revenue losses. Factors that could affect import tax are misclassification of Customs tariff codes, under-declaration of value, under-declaration of goods and falsifying documents (Johnson, 2011; Chia, 2010; Uzzaman and Yusuf, 2010). These acts of non-compliance could affect revenue collection, harm a country's image and reputation, hinder foreign direct investment (FDI) or pose a threat to social justice (Torgler, 2003; Wenzel, 2007). This is a challenge for the administration of tax organisations (Andreoni et al., 1998; Murphy, 2005; Wenzel, 2007). The phenomenon of non-compliance needs to be curbed to avoid a country's tax system from becoming paralysed or ineffective (Silver, 1995).

Although there is evidence from practitioner experience and some background studies that justifies issues of non-compliance with import tax payment, the underlying reasons for this problem remain unknown. It is also uncertain which parties actually lead the problem of non-compliance, the importers, the agents or other business groups. Therefore, I decided to conduct a preliminary inquiry to explore the topic and identify the right group for the research inquiry. This is essential for the study to provide a valuable outcome.

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<sup>7</sup> The tax gap is the difference between the amount of tax that should be legally reported against the actual tax reported to the authority (James and Alley, 2002).

## **1.2 PRELIMINARY ENQUIRY**

A preliminary inquiry was conducted on selected samples of Malaysian Customs officers. The purpose was to investigate the phenomenon of non-compliance with respect to import declaration. However, from a wider perspective, it was also to gain understanding on businesses' compliance towards import tax payment.

Eight senior officers from the Royal Malaysian Customs Department (RMCD) comprising of operational staff, policy makers and Customs trainers at RMCD academy were selected for this purpose. The selections of respondents were based on years of experience, which included a wide range of senior managerial positions within the Customs administration. Respondents were contacted personally through a phone call requesting for an interview session. The previous position of the researcher in the Customs department gave the advantage in approaching respondents. Consequently, entire respondents contacted are willing to participate in the semi structured-interviews session.

The questions consisted of general questions about their opinion on business compliance towards Customs law to more specific questions about issues on Customs import declaration and the phenomenon of tax underpayment during the declaration of import, which has resulted in loss of revenue to the government. The finding provided an interesting insight into the issues. Majority of Customs officials who were interviewed viewed that Customs agents were responsible for assisting their clients (importers) in exploiting legal ambiguity and manipulating<sup>8</sup> import declaration, which has led to loss of Customs taxes through mis-declaration and thus, making compliance difficult. They also believed that the appropriate tools to increase compliance are penalties and sanctions to deter tax evasion, tax avoidance and other forms of non-compliance to Customs law. While, few others expressed their views that other equally important approaches could increase compliance such as incentives, continuous advice and tax education.

Generally, the finding of the preliminary inquiry provided an initial understanding that as an intermediary between importer (client) and Customs administration, Customs agents play an important function in the compliance process. In contrast to the finding from the preliminary inquiry which indicates that agents are

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<sup>8</sup> Manipulation to import declaration comes in a various forms such as alteration of weight, type, number, country of origin and undervaluation of product for the purpose of avoiding tax.

the main parties that involved in evading tax, the role of Customs agents was to facilitate compliance through providing profesional advice to their clients. This was a surprising finding given the fact that Customs agents are regulated under the law, making them liable to any misconduct. Therefore, it is important to understand the underlying factors that could motivate the agents to comply (or not to comply) with the law. This study was further explored through a review of relevant literatures and the assessment of the appropriate approach taken to operationalise the study, which was part of the exploratory phase of this study.

### **1.3 RESEARCH OBJECTIVE AND RESEARCH QUESTIONS**

The preliminary inquiry provides some background to the research problem and defines the focus of the study. Agents' having low levels of compliance with the Customs laws and regulations is a concern for Malaysian Customs officials. Therefore, the role of agents in import tax compliance is investigated.

Generally, this study aims to understand how Customs agents perceive import tax compliance in Malaysia. Specifically the research objective is to assess factors that influence the agents' import tax compliance. In order to fulfil the research objective, the study explores tax compliance and the relevant literature to investigate the similarities and differences between compliance in direct and indirect tax contexts. The study also explores relevant approaches and theories to develop a compliance model for import tax. Drawing upon tax compliance and other inter-disciplinary literature as discussed in Chapter 4 and 5, the Theory of Planned Behaviour (TPB) has been identified as the most robust theory base to understand Customs agents' compliance. Based on the TPB, three unobservable influences were examined: the influence of attitudes; the influence of referent groups (subjective norms); and perceptions of behavioural control (PBC). Further, the TPB based research model was extended with the inclusion of a seven other unobservable influences: law; law enforcement; knowledge; ethics; complexity of procedure; tax assessment service quality; and exchange of fairness. The wider research objective stated here is addressed by the following specific questions<sup>9</sup> :

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<sup>9</sup> The questions were developed through exploratory process and the review of literature as discussed in Chapter 4 and 5.

- RQ1: To what extent can the TPB be used to predict import tax compliance behaviour?
- RQ2: To what extent does attitude of agents towards tax compliance influence their compliance intention?
- RQ3: To what extent do primary and secondary referent group influence the agents' intention and ethical belief towards tax compliance?
- RQ4: To what extent does the agents' perceived behaviour control influence their tax compliance intention and tax compliance behaviour?
- RQ5: To what extent do perception of law and law enforcement influence agents' tax compliance intention and tax compliance behaviour?
- RQ6: To what extent does ethical belief influence attitude and tax compliance intention?
- RQ7: To what extent do level of knowledge, complexity of procedure, perception of tax assessment service quality and perception of exchange of fairness influence agents' tax compliance intention?

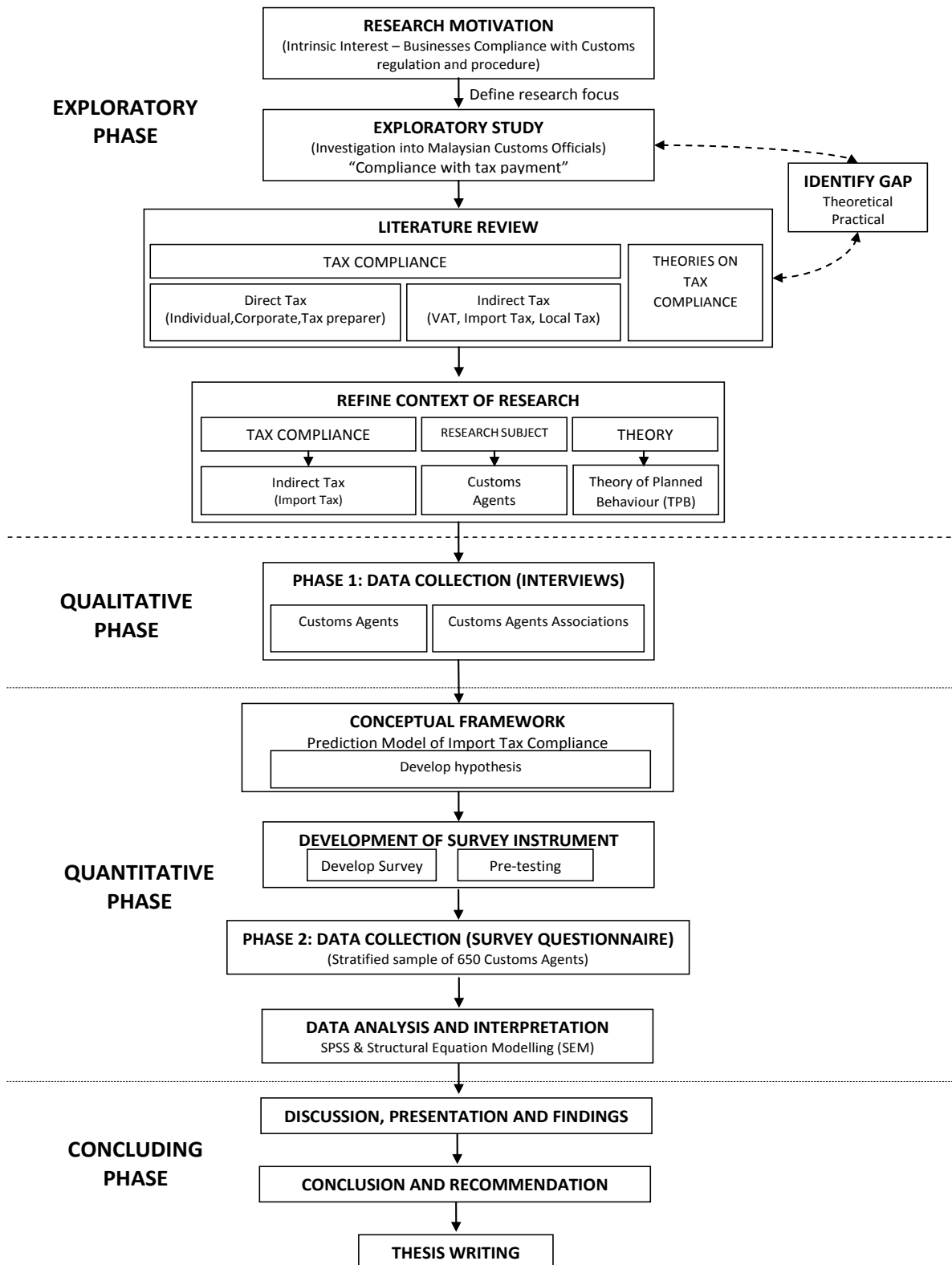
The following section will briefly describe the research process and the steps it consists of to provide an overview of this study.

#### **1.4 RESEARCH PROCESS**

Figure 1.1 shows steps of the research process followed in this study. This diagram also links the chapters in this thesis. It began with the first cycle (exploration phase) which starts with the intrinsic interest of this study with initial interviews with Malaysian Customs Officials and a review on the literature to identify the gaps in the literature where the study can make a contribution. This stage the study also involved identifying relevant theories for the purpose of model development. The second cycle (qualitative phase) involved a series of initial interviews with Customs agents and head of Customs agents associations (logistics and freight forwarders associations). The result of the interview findings was used to support the research model development. The process continued with the collection of quantitative data in the third cycle or the quantitative phase. Questionnaire instruments were developed based on the research model and tested through pre-testing and finally, the survey questionnaire distribution. Lastly, analysis was conducted on the responses. The qualitative and quantitative phases were conducted sequentially, which represented



the exploratory sequential mixed method research design of this study. The remaining part, as shown in the diagram, includes discussion on the findings from the survey data, follows by recommendations and the conclusion of this thesis.



**Figure 1.1: Research Process and Design**

Source: Author

## **1.5 SUMMARY**

This chapter provides an introduction on decision making in import tax compliance and describes the motivation to conduct the study in Malaysia based on practitioners' experience and observation during the researcher's tenure with the Royal Malaysian Customs Department. Here the author compared between his observations on the problem of compliance to import tax payment and international perspectives on tax non-compliance. The problem of compliance in Malaysia has occurred since the time of the great Sultanate (Ruler) empire of Malacca when the first Customs tax was introduced as a formal fiscal tax system. The high tax as that time created the problem of tax evasion through smuggling activities. In modern Customs administration, the problem of compliance is a continuing issue and requires a deeper understanding compared to straight-forwards smuggling cases in the early history. This leads to a preliminary inquiry with selected Malaysian Customs officials who perceived that the problem of compliance as being rooted in the way custom agents operate. According to the interview findings, Customs agents assisted their clients (importers) in exploiting the ambiguity in the law and in the manipulation of import declarations for the purpose of avoiding tax. Therefore, the role of Customs agents in import tax compliance was investigated in this study to assess factors that influence the agents' compliance decisions. Several steps such as identifying relevant theories, variables that may influence compliance and research approach were conducted in an attempt to present a compliance model for import tax.

The remainder of the thesis is organised as follows. Chapter 2 discusses the background to the research problem. Chapter 3 presents the exploratory study conducted in the initial phase of this study. Chapter 4 discusses the relevant literature and theories that form as the foundation of the study. Chapter 5 presents the theoretical context and research paradigm, followed by Chapter 6, on research method and design. In Chapter 7, the qualitative phase and the development of conceptual research model is described. The research model applied in the quantitative phase and the respective analyses are presented in Chapter 8. Chapter 9 provides the finding of the survey questionnaire with some discussions on the implications of this study. Finally, Chapter 10 highlights some limitations of this study and makes some recommendations on future research directions.

## **CHAPTER 2**

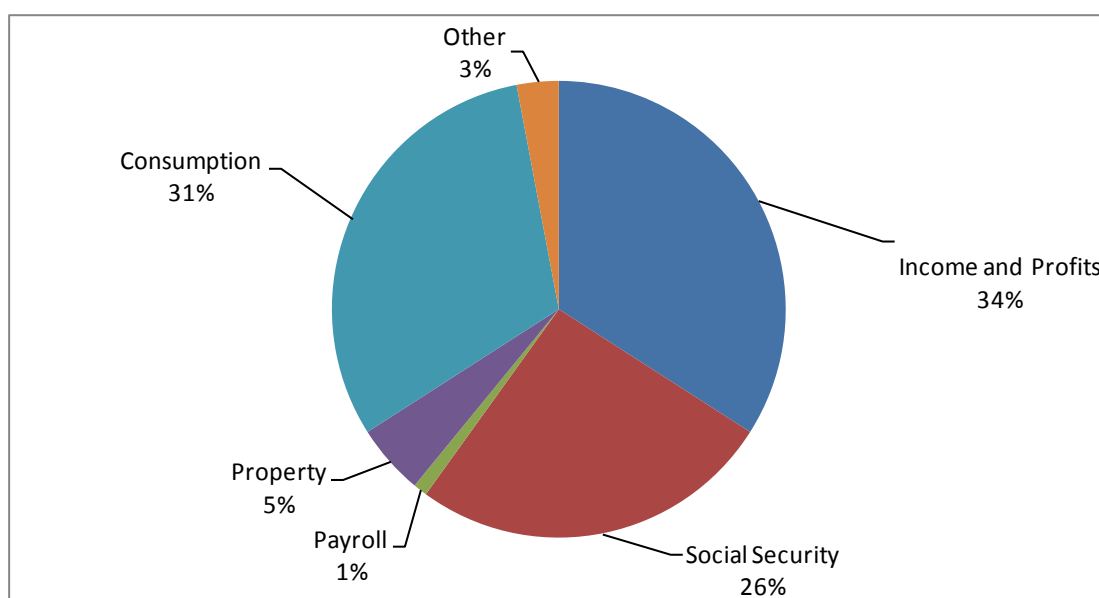
### **BACKGROUND TO THE RESEARCH PROBLEM**

This chapter provides the necessary background to frame the research problem. It begins by describing the importance of import taxes, which represent a significant portion of a country's tax revenue, especially Malaysia. The second part of the chapter demonstrates on the complexity of Customs import payment procedure and the use of Customs agents to reduce the compliance burden as mandated by many countries. The focus of this study is on Malaysia, but the subsequent section shows the relevance of the study to any other country that relies on Customs agents to make the correct Customs duty payments. The final section of this chapter sheds light on the need for further investigation to understand the issue of non-compliance.

#### **2.1 CUSTOMS AND IMPORT TAX**

Collecting indirect tax such as Customs duties and taxes on import is one of many functions of Customs administrations around the world. In many countries, indirect tax represents a significant portion of the national revenue (Sowinski, Pope, and Taelman, 2013). Customs also collect other revenue such as value added tax (VAT) / good and service tax (GST) and occasionally tax on export or export duty. Apart from collecting revenue, Customs also performs other functions such as providing trade data from import and export for national statistics; trade facilitation through providing advance Customs clearance before ships arrive; a paperless system and simplification of Customs procedures to expedite trade movement; protection of society and national security from various threats such as terrorism and drug trafficking.

**Figure 2.1: Average Tax Revenue by Category of Tax**



*Source: OECD (2014, p16)*

From a wider perspective, indirect tax revenue such as Customs duties, VAT/GST and other indirect taxes accounts for an average of 31% of all revenue collected by governments (see Figure 2.1). The share of tax on specific goods which consists of Customs duties and taxes, for instance, in the Organization of Economic Co-operation and Development (OECD) countries, as presented in Table 2.1, represents an average between 10% to 25% of the total tax revenue (OECD, 2014).

As seen in Table 2.1, among the OECD countries, Mexico (35.4%) recorded the highest percentage of Customs duties and tax contributions for the national tax revenue. Other OECD countries that indicate a high percentage of revenue contributions are Turkey (23.1%), Korea (22.1%) and Portugal (20.3%). The average of Customs duties and taxes for all OECD countries recorded is 13.6%. Belgium, the United States, France and Israel have the lowest percentages of Customs and excise duties of below 9% of total tax contributions. Other countries have a percentage between 10% and 18% contribution of Customs duties and taxes. The statistics suggest that Customs duties and tax contributions form an important source of revenue contributions among OECD countries.

**Table 2.1: Customs Duties and Taxes as a Percentage of Total Taxation in OECD Countries**

COUNTRY	1965	1975	1985	1990	1995	2000	2005	2009	2010	2011	2012	Avg
Australia	22.7	19.1	20.7	15.3	14.5	14.1	12.0	12.2	11.9	11.3	11.0	15.0
Austria	18.0	14.0	9.9	9.0	8.5	8.1	8.1	7.5	7.4	7.6	7.4	9.6
Belgium	13.0	9.8	8.2	8.5	8.5	7.1	7.3	7.2	7.3	7.1	7.6	8.3
Canada	16.8	13.6	13.0	10.3	9.9	8.6	8.9	8.7	8.8	8.4	8.2	10.5
Chile	n/a	n/a	n/a	23.0	19.2	18.8	10.9	10.1	9.8	9.4	9.4	13.8
Czech Republic	n/a	n/a	n/a	n/a	13.0	11.0	9.9	10.8	10.8	11.2	11.1	11.1
Denmark	28.9	15.0	13.0	11.0	11.4	11.1	10.6	9.0	9.3	9.3	9.0	12.5
Estonia	n/a	n/a	n/a	n/a	n/a	10.1	12.6	14.6	13.2	14.0	14.5	13.2
Finland	23.4	16.0	15.2	12.9	12.5	10.9	10.8	10.2	10.4	11.0	11.0	13.1
France	14.3	9.0	8.7	8.7	9.2	8.0	7.5	7.5	7.5	7.7	7.7	8.7
Germany	14.6	10.8	8.7	9.2	9.5	8.8	9.8	8.6	8.4	8.3	7.9	9.5
Greece	33.8	23.9	20.9	15.6	16.4	10.0	9.4	10.2	11.9	12.9	12.0	16.1
Hungary	n/a	n/a	n/a	n/a	20.9	13.8	10.8	10.7	12.1	12.5	12.6	13.3
Iceland	45.0	33.6	26.5	16.9	14.0	11.0	10.6	9.6	10.5	10.7	10.7	18.1
Ireland	43.4	29.7	22.0	20.1	17.5	13.9	11.1	11.1	11.5	11.1	10.6	18.4
Israel	n/a	n/a	n/a	n/a	4.4	4.3	5.3	6.6	6.9	6.6	6.4	5.8
Italy	24.1	14.0	9.1	10.6	11.1	9.6	9.2	8.7	8.5	8.7	8.9	11.1
Japan	25.0	15.1	12.1	7.5	8.3	8.0	7.7	7.3	7.2	7.1	6.9	10.2
Korea	n/a	47.3	37.4	25.7	21.9	19.7	15.9	13.7	15.2	12.2	12.0	22.1
Luxemburg	11.1	8.0	11.1	10.8	12.6	12.5	12.3	10.2	9.80	9.9	9.5	10.7
Mexico	n/a	n/a	48.6	34.0	35.8	33.4	36.6	29.4	31.2	34.3	34.9	35.4
Netherlands	14.7	8.1	7.2	7.5	9.0	8.9	9.3	8.9	8.7	8.6	8.0	9.0
New Zealand	18.5	13.8	11.7	9.2	8.6	7.5	6.2	6.4	6.4	6.3	6.0	9.1
Norway	18.4	16.1	18.1	15.3	15.5	9.6	7.9	7.8	7.6	7.1	6.8	11.8
Poland	n/a	n/a	n/a	n/a	17.5	13.5	13.3	12.6	13.9	13.3	12.9	13.9
Portugal	44.0	28.9	29.7	23.8	17.6	13.9	15.0	13.4	13.3	12.3	11.8	20.3
Slovak Republic	n/a	n/a	n/a	n/a	n/a	13.7	12.3	10.4	11.3	10.8	11.4	11.7
Slovenia	n/a	n/a	n/a	n/a	8.4	12.1	10.8	13.2	13.4	13.3	14.1	12.2
Spain	18.4	8.7	12.8	10.5	10.3	9.6	8.3	8.4	8.0	7.8	8.2	10.1
Sweden	19.2	10.7	11.6	9.2	8.3	7.0	6.8	6.8	6.8	6.6	6.7	9.1
Switzerland	21.3	11.9	9.5	7.	7.3	7.0	7.0	7.0	7.1	6.6	7.2	9.0
Turkey	53.5	40.9	12.4	7.3	6.0	16.4	25.5	23.6	24.1	21.7	22.44	23.1
United Kingdom	25.2	14.8	13.8	12.6	14.5	12.4	10.5	11.0	10.7	10.7	10.8	13.4
US	15.1	10.0	8.4	7.0	7.5	6.3	6.6	6.9	7.0	7.1	7.1	8.1
<b>OECD TOTAL</b>	<b>24.3</b>	<b>17.7</b>	<b>16.2</b>	<b>13.3</b>	<b>12.8</b>	<b>11.5</b>	<b>11.1</b>	<b>10.6</b>	<b>10.8</b>	<b>10.7</b>	<b>10.7</b>	<b>13.6</b>

*Source: OECD (2014, p38)*

Customs duties within EU countries account for 15% (19.1 billion Euros in 2012 and 18.6 billion in 2013) of the EU budget which exceed incomes from VAT (15 billion Euros average) and, according to official figures, 75% of the income from Customs duties is transferred to the EU and 25% remains in the state where it is collected (Gwardzińska, 2014). In Malaysia, indirect tax revenue remains an important revenue contribution for the government. Indirect tax represents an average of 26% or MYR30 billion (GBP6 billion) a year (10 years average from 2005 to

2014) through collection of customs duty, excise duty, sales tax and other indirect taxes (see Table 2.2).

**Table 2.2: Federal Government Financial Statistics. 2005 to 2014 (in MYR million)**

	AVERAGE	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005
<b>Direct Tax</b>	89047	126743	120523	116937	102242	79008	78375	82138	69396	61572	53543
<b>Indirect Tax</b>	30751	37462	35430	34706	32643	30507	28129	30760	25772	25058	27051
<b>Direct tax</b>	74%	77%	77%	77%	76%	72%	74%	73%	73%	71%	66%
<b>Indirect Tax</b>	26%	23%	23%	23%	24%	28%	26%	27%	27%	29%	34%
<b>TOTAL</b>	119799	164205	155953	151643	134885	109515	106504	112898	95168	86630	80594

*Source: Accountant General (2015, p94)*

Among the Customs revenue as presented in Table 2.3, Customs import tax represents about one-third of total revenue collection, between MYR10 billion and MYR11.5 billion for the years 2012 to 2014. Import tax contributions consists of three elements of duty and taxes, namely import duty, import excise duty and import sales tax or import VAT (value added tax). Other revenue that contributes to Malaysian Customs revenue is derived from domestic taxes such as sales tax and service tax. The sales and services tax are similar to value added tax (VAT) or goods and service tax (GST) which are imposed on consumption of goods or services. Tax on goods and services (GST) represents an average of 35% or between MYR10 billion and MYR12 billion for the years 2012 to 2014. Domestic excise duty in Malaysia is the duty collected on domestically produced goods such as cars, tobacco products and alcoholic beverages. This represents another 25% of total Customs revenue. Export revenue generated from export duty on rubber and timber contributed only 5% to 6% of total Customs revenue.

**Table 2.3: The Royal Malaysian Customs Revenue Collection by Activities for the Years 2012 to 2014**

Type of Duty and Taxes	2012		2013		2014	
	MYR/ Billion	%	MYR/ Billion	%	MYR/ Billion	%
<b>1) DOMESTIC TAX</b>						
Excise Duty (Domestic)	8,414.87	26%	8,393.67	25%	8,455.98	24%
Sales Tax (Domestic)	5,357.28	17%	5,944.50	18%	6,130.72	18%
Service Tax	5,584.99	17%	5,626.03	17%	6,277.51	18%
<b>Sub-Total</b>	<b>19,357.14</b>	<b>60%</b>	<b>19,964.20</b>	<b>60%</b>	<b>20,864.21</b>	<b>60%</b>
<b>2) IMPORT TAX</b>						
Sales Tax (Import)	4,129.45	13%	4,466.61	13%	4,805.77	14%
Excise Duty (Import)	3,770.45	12%	3,800.22	11%	4,068.13	12%
Import Duty	2,283.23	7%	2,500.64	8%	2,688.28	8%
<b>Sub-Total</b>	<b>10,183.13</b>	<b>32%</b>	<b>10,767.47</b>	<b>33%</b>	<b>11,562.18</b>	<b>33%</b>
<b>3) EXPORT TAX</b>						
Export Duty	1,968.43	6%	1,931.58	6%	1,897.79	5%
<b>4) OTHER TAX</b>	813.44	3%	463.46	1%	497.77	1%
<b>TOTAL</b>	<b>32,322.14</b>	<b>100%</b>	<b>33,126.71</b>	<b>100%</b>	<b>34,821.95</b>	<b>100%</b>

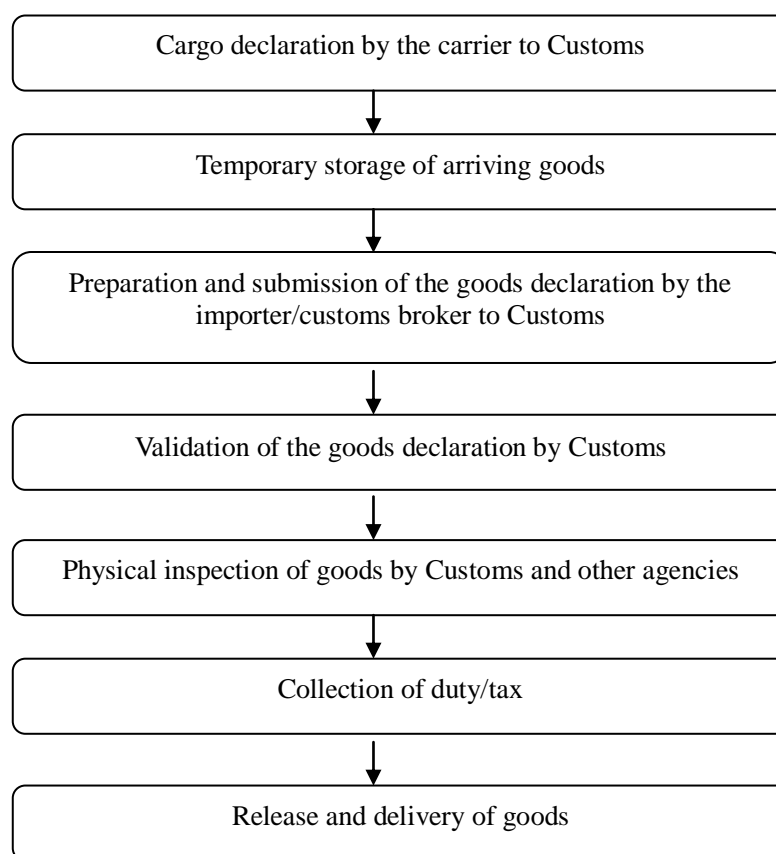
*Source: RMCD (2015a, p142; 2014b, p142)*

## **2.2 COMPLIANCE WITH IMPORT PAYMENT PROCEDURE**

Compliance with Customs import payment procedure is complex and requires familiarity with various requirements, which are technical in nature. These include tariff classification, valuation and origin rules as well as ‘Customs facilitations’. This is not including the steps involved in the process of clearance of goods which involves many agencies at the border such as the port operator, port authority, Customs, health department, agriculture department and Customs agents as the intermediaries between importers and border agencies. The remainder of this section discusses Customs compliance procedure and the importance of intermediaries such as Customs agents in assisting their clients in meeting the compliance requirements of various agencies including Customs.

### 2.2.1 How Import Tax Is Calculated

Customs import tax, referred to as import duties and taxes by the WCO, are “Customs duties and all other duties, taxes or charges which are collected on or in connection with the importation of goods, but not including any charges which are limited in amount to the approximate cost of services rendered or collected by the Customs authority on behalf of another national authority” (E20/F14, Revised Kyoto Convention). An importer who wants to bring goods into a country is subject to Customs procedures and assessment. The purpose is to determine the appropriate import tax (if applicable), typically Customs duty, import sales tax and excise duty in relation to the goods being imported. It is part of the Customs clearance process (Figure 2.2) and happens before the goods are physically released to the final destination at the designated premises.



**Figure 2.2: Import Clearance Process**

*Source: Adapted from World Bank, (2006, p63)*



Import tax is guided by both international conventions and international organisations such as The World Customs Organization (WCO), World Trade Organization (WTO), ASEAN and various legislations at national level (see Table 2.4). Failure to comply with these rules by importing parties exposes businesses to the risk of being penalised, in the form of fines, imprisonment and the seizure and forfeiture of the goods involved. For instance, sections 78 and 79 of the Customs Act 1967 require importing parties to declare, giving a full and true view of the imported goods as specified by the act. The consequences for not providing a true declaration of the goods may be a penalty of up to MYR500,000 (GBP100,000 approx.) or imprisonment for up to 5 years, or both, as outlined in Section 133 of the Customs Act 1967.

**Table 2.4: Examples of Related International Conventions, Regional and National Legislations as the Guiding Framework for Import Tax**

<p><b>INTERNATIONAL</b></p> <p><b>Revised Kyoto Convention (WCO, 2006)</b> A blueprint for Customs procedure applied by the World Customs Organization (WCO) member countries (179 countries).</p> <p><b>Harmonised Commodity Description and Coding System (WCO, 2014)</b> The framework for the classifying goods was developed and maintained by the WCO, through International Convention on the Harmonised Commodity Description and Coding System which commonly referred as Harmonised System or HS. The HS system is used by more than 200 countries.</p> <p><b>General Agreement on Tariff and Trade (GATT) (WTO, 1994)</b> A set of agreed rules governing trade among its signatories, whose number increased from 23 in 1947 to 123 in 1994. GATT was incorporated as WTO umbrella treaty for trade in goods with effect from 1995 which is still in force for the purpose of trade liberalisation and guiding principles for Customs administration in determining the Customs duty and related taxes.</p> <p><b>WTO Trade Agreement (WTO, 2014)</b> Multi-lateral agreement among 160 member countries which contains provision of lowering import tariff, subsidies and import quotas abolishment to increase growth in international trade. Also serves as a guiding principle for Customs administration to expedite the clearance process to facilitate trade as outlined in the WTO Trade Facilitation Agreement (WTO, 2013).</p> <p><b>SAFE Framework of Standards (WCO, 2012)</b> Framework that acts as a deterrent to international terrorism, secures revenue collections and promotes trade facilitation worldwide.</p>
<p><b>REGIONAL (ASEAN)</b></p> <p><b>Mutual Recognition Agreements (MRAs) (ASEAN, 2014b)</b> Establishment of trade agreement between one or more countries in ASEAN lowering tariff rates between zero and 5% (refer to Table 2.7 for details of ASEAN trade agreement participation).</p> <p><b>ASEAN Harmonised Tariff Nomenclature (AHTN) (ASEAN, 2014c)</b> The harmonised framework for the classifying goods specifically for ASEAN free trade areas which was developed based on the WCO Harmonised Commodity Description and Coding System.</p>
<p><b>NATIONAL LEGISLATIONS (MALAYSIA)</b></p> <p><b>Malaysian Customs Act 1967</b> The principle act that regulates and authorises Customs as the key agency at border to administer the import and export activities including collection of Customs duty and taxes.</p> <p><b>Subsidiary Acts</b> There are more than 26 subsidiaries acts that support the principle act (Customs Act 1967) including Customs Regulations, Restriction Order and Duties Order (refer to Appendix 7 for details).</p>

*Source: Author*

Import tax payment can be deferred in order to reduce the burden of paying tax at once and to facilitate business cash-flow especially when importing large consignments of goods. The type of deferment which is commonly referred to as Customs facilitation can come in various forms such as bonded warehousing, temporary storage or gazetted free zone areas which are under Customs control. Goods are taxed once they are released from Customs control. Examples of Customs facilitation are shown in Table 2.5.

**Table 2.5: Examples of Customs Facilitation Related Import Tax Deferral Regime**

Type of Customs Facilitation	Purpose
Exemptions	Post clearance monitoring inputs that have been granted full or partial exemption of duty/tax while they are being manufactured into finished products for re-export.
Drawback	Refund of duty/tax paid on imported inputs that are subsequently exported in finished goods.
Bonded Warehouse	Deferment of duty/tax payment on specific goods for a period of time until they can be removed and entered into home consumption.
Free Zones	Areas outside Customs territory which is gazetted for temporary storage of goods without payment of duty/tax.
Temporary Admission	Full or partial relief from duty/tax payment on imported goods for specific purposes such as exhibition goods, commercial samples, and construction equipment being used temporarily for construction purposes.
Transit Control	Deferment of duty/tax for movement of goods across a territory until it reaches its destination. Customs control system is used to track the movement of each container as it moves along the transit corridor.

*Source: Adapted from World Bank, (2006, p14-15)*

### **2.2.2 Determining the Correct Customs Duties and Taxes**

Determining the correct Customs duties and taxes is a complex process and requires technical knowledge with regards to the rules, regulation and procedures outlined by the international organisations and national requirements as described in Table 2.4. Generally, all goods that enter or leave the country are subject to Customs declaration with the emphasis on providing accuracy in the declaration (as outlined in

Chapter 3, Revised Kyoto Convention). The declaration of goods is commonly sub-contracted to Customs experts (third parties) such as Customs agents. Declared goods are assessed by Customs to determine the correct Customs duties and taxes according to three factors: (i) classification of product; (ii) Customs valuation; and (iii) the rules of origin. The total amount of Customs duties and taxes that are imposed on a particular import can be increased or decreased according to these criteria.

*(i) Product Classification*

There are various classifications of goods depending on the type of products being imported. To this purpose, goods are classified into respective product categories which are referred to as Customs tariff classifications. The objective is to determine the correct tariff rates for the assessment of duties and taxes<sup>10</sup> such as import/export duty, excise duty and VAT on import. The duty rates are determined according to the class of goods under the HS commodity system, irrespective of the value of goods. The framework for classifying goods is developed and maintained by the WCO, through the International Convention on the Harmonised Commodity Description and Coding System which is commonly referred to as the Harmonised System or HS. The HS is a universal economic language and code for goods, and an indispensable tool for international trade. It is widely used by governments, international organisations and the private sector for many other purposes such as internal taxes, trade policies, monitoring of controlled goods, rules of origin, freight tariffs, transport statistics, price monitoring, quota controls, compilation of national accounts, and economic research and analysis.

Determining the correct classification of a commodity is not a simple process. There are more than 5,000 commodity codes, each identified by six digits, which are universally accepted, and applicable to Customs administrations in more than 200 countries (WCO, 2014). The Customs commodity code consists of 99 chapters under 16 headings, of the product categories depicted in Table 2.6. Technical knowledge and training are required for Customs personnel and the respective business entities such as Customs agents to understand the application of the HS system and assign the appropriate Customs commodity codes to the correct product categories.

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<sup>10</sup> Assessment of duties and taxes refers to the determination of the amount of duties and taxes payable (E2/F19, Revised Kyoto Convention).

**Table 2.6: Harmonised Commodity Description and Coding System**

CHAPTER	PRODUCT CATEGORY
01-05	Animal & Animal Products
06-15	Vegetable Products
16-24	Foodstuffs
25-27	Mineral Products
28-38	Chemicals & Allied Industries
39-40	Plastics / Rubbers
41-43	Raw Hides, Skins, Leather, & Furs
44-49	Wood & Wood Products
50-63	Textiles
64-67	Footwear / Headgear
68-71	Stone / Glass
72-83	Metals
84-85	Machinery / Electrical
86-89	Transportation
90-92	Optical Apparatus, Clock and Musical Instruments
93	Arms and Ammunition
94-96	Miscellaneous
97-98	Art Works and Special Provisions

Source: *Customs Duties Order (2012, p11-18)*

(ii) *Customs Valuation*

Apart from the HS system for the purpose of classification of goods, all dutiable goods are subject to Customs valuation, referred to as value for duty purposes (VDP), as outlined in the General Agreement on Tariff and Trade (GATT)<sup>11</sup>. There are specific rules on Customs duty assessment in the GATT, related to article VII on valuation and article VI on anti-dumping and countervailing duties. Valuation of imported goods is derived from cost, insurance and freight (CIF). Article VII GATT on Customs valuation contains 6 guiding principles on the methods of Customs valuation. These six methods of valuation are technical in nature and involve several steps to determine the correct valuation of goods. The methods are (i) Method 1

<sup>11</sup> GATT is the multilateral agreement that provides the basic rules for international trade aimed at reducing tariffs, eliminating preferences and other trade barriers (GATT, 1947).

transaction value; (ii) Method 2: transaction value of identical goods; (iii) Method 3: transaction value of similar goods; (iv) Method 4: deductive method; (v) Method 5: computed method; and (vi) Method 6: fall-back method (Sokol and Wulf, 2005).

Most duties are calculated as a percentage of the value of imported goods for purposes of assessing the amount of Customs duty. Therefore, it is important that importers establish an accurate value of their imported goods.

Article VI on anti-dumping and countervailing duties of GATT is to counterbalance ‘unfair trade practices’. It is an additional duty imposed on dumping products<sup>12</sup> by the exporting country into the recipient country (Lee, 2012).

### *(iii) Rules of Origin*

The other rules that apply to Customs assessment procedures are the rules of origin (RoO), under the agreement of rules of origin in the GATT. The principles of rules of origin are coordinated by the Committee on Rules of Origin (CRO) under the WTO and the Technical Committee on Rules of Origin (TCRO) of WCO (Sokol and Wulf, 2005). The rules of origin are important to determine in which country the products are manufactured and originate. They serve two purposes: (i) tariff or quota control, and (ii) determining the Customs duty rates under preferential rules of origin<sup>13</sup>. The principle objective is to ensure that trading arrangements between two or more countries are restricted and benefited to only the trading partners (UNECE, 2002). Over the years many preferential trading agreements (PTAs) have been established between various economic blocs or between countries such as the EU, Asia Pacific, Africa, the Middle East and the United States (Estevadeordal and Suominen, 2005). Preferential trade agreements are also actively established at ASEAN level, as shown in Table 2.7. The establishment of PTA of ASEAN countries is mainly motivated by expansion of market access at lower tariff or duty rates which attracts tariff rates between zero and 5% on over 90% of product classifications (Calvo-Pardo, Freund and Ornelas, 2009).

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<sup>12</sup> Dumping products is defined as the introduction of products into the commerce of an importing country at less than its normal value, that is, less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting member (Lee, 2012).

<sup>13</sup> Preferential rules of origin are used to determine which goods enter a country under preferential treatment, i.e., they are used to establish whether the goods are eligible for special treatment under a trading arrangement between two or more economies. Preferential tariffs at zero or reduced rates of duty are applied to goods that are the products of or manufactured in a preferred or recipient country (UNECE, 2002, p30).

**Table 2.7: ASEAN Preferential Trade Agreement Participation**

Country	Regional	Cross-Regional
<b>ASEAN</b>	AFTA (Jan 1992)	ASEAN-Australia-New Zealand (Aug 2000)
	ASEAN-China (Nov 2004)	ASEAN-India (Aug 2009)
	ASEAN-Korea (Oct 2006)	
	ASEAN-Japan (Apr 2008)	
<b>Singapore</b>	Singapore-Japan (Jan 2002)	Singapore-New Zealand (Oct 2000)
	Singapore-Korea (Aug 2005)	Singapore-Switzerland (Jun 2002)
	Singapore-China (Oct 2008)	Singapore-Australia (Feb 2003)
		Singapore-USA (May 2003)
		Singapore-Jordan (Apr 2004)
		Singapore-India (Jun 2005)
		Singapore-Trans-Pacific South America (Jun 2005)
		Singapore-Panama (Mar 2006)
		Singapore-Peru (May 2008)
		Singapore-Gulf Cooperation Council
		Singapore-Costa Rico (Apr 2010)
<b>Thailand</b>	Thailand-Japan (Apr 2007)	Thailand-Australia (Jul 2004)
		Thailand-India (October 2003)
		Thailand-New Zealand (Apr 2005)
		Thailand-Peru (Nov 2009)
<b>Malaysia</b>	Malaysia-Japan (Dec 2005)	Malaysia-Pakistan (Nov 2007)
		Malaysia-Chile (May 2010)
		Malaysia-India (Feb 2011)
<b>Indonesia</b>	Indonesia-Japan (Aug 2007)	
<b>Philippines</b>	Philippines-Japan (Sep 2006)	

Source: Leu (2011, p34)

### 2.2.3 The Rates of Import Tax

The rates of import tax vary across its various elements (import duty, excise duty and import VAT), depending on the type of goods being imported. The rates of import tax are normally calculated as a percentage of the value of the goods with the exception of some specific goods which are calculated by weight or specific ingredients. The elements of import taxes also differ according to the country's tax system. For examples for tobacco products, only import duties are collected by US Customs (USCBP, 2012), while other duties such as sales tax and excise duties which differs in rates (for example USD 2/pack in Alabama and USD 0.37/pack in Georgia), are collected by the respective states (UST, 2012). In contrast, for countries such Malaysia, there are three elements of duty imposed when importing cigarette products which consists of import duty, excise duty and sales tax collected by the Malaysian Customs (Customs Duties Order, 2012).

(i) *Import Duties*

Import duty rates imposed on imported goods vary depending on the type of products, and the rates differ from one country to another. Agricultural products commonly attract among the lowest duty rates, ranging from zero to 20% for countries such as Malaysia (Customs Duties Order, 2012), while in some developed countries the duty rates are far higher than developing countries. For example for garlic (HS Commodity Code 0703.20.00.00) imported from outside of EU, the rate in the UK is 9.60 % + 120.00 EUR/ hectokilogram (UK Trade Tariff, 2012), whereas in developing countries such as in Malaysia, the duty rate for garlic is zero (Customs Duties Order, 2012). Other products in Malaysia such as electrical goods, textiles, motor vehicles, tobacco and alcoholic beverages generally attract higher import duty rates. The rates are generally from 15% to 30% for electrical goods, textiles and motor vehicles, while import duty rates for cigarettes are calculated according to the number of sticks and alcoholic beverages are calculated based on volume of alcohol contained in the beverages (Customs Duties Order, 2012). The rates of duty can be reduced by having a trade arrangement between two or more countries, commonly referred to as a 'preferential agreement'.

(ii) *Excise Duties*

Excise duties are commonly imposed on selected products such as cigarettes, tobacco products, alcoholic beverages and motor vehicles according to product categorisation. The rates of excise duty are among the highest duty rates compared to import duty and sales tax on import. Excise duty for alcoholic beverages is calculated per litre plus a fixed percentage rate (for example, wine - HS code 2204.21.200 at MYR15.00 + 15% duty), whereas cigarettes are calculated according to number of sticks plus fixed percentage rate (for example, MYR25/stick + 20% duty – HS Code 2402.20.200). The excise duty rate for passenger vehicles is fixed at a specific percentage according to the engine capacity and type of vehicle (MPV, SUV or car) ranging from 75% to 105% (Customs Duties Order, 2012).

In the UK and other countries, some examples of products that are subject to excise duty are tobacco products and alcoholic beverages. The rates of excise duty are based on the alcohol by volume (ABV) per hectolitre, while for cigarettes, excise duty

is charged at a fixed percentage plus a fixed value of duty per 1,000 cigarettes (HMRC, 2012).

*(iii) Sales Tax on Import (Import VAT)*

Sales tax is imposed on a broader range of products. In Malaysia, the rate varies according to the fixed percentage rates, depending to the type of goods (5%, 10%, 20%) as described in the Sales Tax (Rates of Tax No.1) Order 2012 and Sales Tax (Rates of Tax No.2) Order 2012. Exceptions are given to goods listed in the Sales Tax (Exemption) Order 2013 which are exempted from Sales Tax, such as supplies to government agencies. In the UK and other countries in the EU, sales tax on imports is referred to as import VAT. The percentage charged on import VAT in the UK is the same flat rate applied to VAT on goods sold for the domestic market (HMRC, 2012). VAT import may be reclaimed later as input tax on any VAT paid on goods (difference between input and output VAT) (HMRC, 2012) whereas sales tax is a single stage where input tax and output tax are not applicable in this context.

Exhibit 2.1 shows an example of how import tax is calculated in a typical trade transaction. The import duty payable on the importation varies as per the following bands:

1. Import duty: a % of the CIF value of the goods.
2. Excise duty: a % of the (CIF value + import duty).
3. VAT: a % of the (CIF value + import duty + excise duty).
4. Import declaration fees: a % of the CIF value or a specific minimum amount whichever is higher, is payable.

The example given provides an overview of the complexities of determining the correct Customs duty and taxes for imported products, which involves several processes, duty rates and taxes. It would be an immense task to summarise or provide direct comparisons of all product commodities across the countries, to show the differences between all three types of duty and tax, due to the huge amount of HS codes for more than 14,000 product categorisations (HMRC, 2012).



## Exhibit 2.1: Calculation of Import Tax

Vehicle Detail	: Mercedes Benz C200 Kompressor (Used)
Engine Capacity	: 1999cc
Year Registered	: 02/2007
(In the Country of Origin)	
HS Code	: 8703.23.333
Tax Rate	: Import Duty (30%), (Excise Duty 80%), Import Sales Tax (10%)
<u>Calculation of Tax (in MYR)</u>	
CIF Value	: MYR 24,328
(a) <b>Import Duty</b>	: <b>MYR 7,298</b>
(CIF x 30%)	
(b) <b>Excise Duty</b>	: <b>MYR 25.300</b>
[(CIF + Import Duty) x 80%]	
(c) <b>Import Sales Tax</b>	: <b>MYR 5,693</b>
[(CIF + Import Duty + Excise Duty) x 10%]	
<b>Total Import Tax</b>	: <b><u>MYR 38,291</u></b>
[a + b + c]	

Source: Author

Compliance with Customs procedure during the assessment of goods and making duty payment as well as other border agency requirement are essential before the goods are finally approved for clearance. The buyer or importer,<sup>14</sup> in these instances, has the obligation to comply with the trade procedure including Customs procedures. Failing to adhere to the regulatory objectives, the importer has to face the consequences of delay in clearance of goods or face a heavy penalty for trying to evade Customs duty. Although the use of Customs brokers is not mandatory, as recommended in the recent Bali Ministerial Declaration on Trade Facilitation (WTO, 2013), importers often seek the assistance of Customs agents<sup>15</sup> to handle Customs matters such as Customs clearance due to the complication of procedure and excessive regulations (Appeals and Swielande, 1998; Grainger, 2008; Sawhney and Sumukadas, 2005).

<sup>14</sup> As defined by the law, importer means any owner or other person deemed to have a beneficial interest in any goods from the time of importation until the goods are cleared from Customs control (Indian Customs Act, 1962; Malaysian Customs Act, 1967).

<sup>15</sup> Customs agents are internationally known as customs brokers by the International Federation of Customs Brokers Associations (IFCBA). Other countries use the term Customs agents (for example Malaysia), Customs brokers (for example the US) or clearing agents.

#### **2.2.4 The Role of Customs Agents**

Customs agents are defined as people or firms licensed by an importer's government and engaged in entering and clearing goods through Customs. Their responsibilities include preparing entry forms, advising importers on duties to be paid, advancing duties and other costs, and arranging for delivery to the importers (Sollish and Semanik, 2011). Customs agents are also known as 'Customs brokers' a term widely used by many countries such as The United States, Canada, Australia, China, India and Thailand. In some countries, such as Singapore, Customs agents are referred to as 'declaring agents' while in Japan the term 'Customs specialists' is applied following the registered Customs specialist system which was adopted in 1967 when the Customs Brokerage Law was established. Customs agents may also be employed or affiliated with importers, exporters, freight forwarders, shipping lines, independent businesses or trade authorities.

Customs agents represent one of the most important intermediaries connecting customers (importers), suppliers (exporters) and various agencies such as Customs for the purpose of clearance of goods at international borders and ensuring compliance with Customs and trade procedures. Most importers and exporters rely on the advice and services of Customs agents as they have technical knowledge of the Customs functions and the environment in which trade is conducted within a country (Buyonge and Kireeva, 2008). In some parts of the world, Customs brokers have been offering advice and providing services to importers and exporters for hundreds of years (West, 2010). Although there are additional costs incurred to businesses when using the services of Customs agents, the risks and potential costs may be higher of not using the expert service. These may include delays in the clearance of goods, especially for businesses that are not familiar with the requirement of various agencies at borders. Hence these uncertainties in time and costs are off-set by sub-contracting the task to Customs agents.

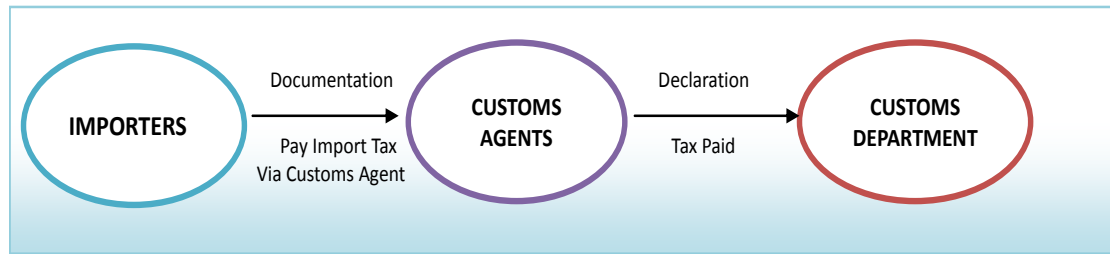
A survey conducted in the United States of third party logistic providers indicates that importers outsourced 58% of logistics functions to Customs brokers (Customs agents) to handle the clearance of their cargo (Lieb and Bentz, 2005). In Malaysia 90%<sup>16</sup> of the task of clearance of goods is outsourced to Customs agents (interview findings). The function of Customs agents also extends to tax collecting for

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<sup>16</sup> Figure derived from an interview with Customs officials.

Customs administration in Malaysia (see Figure 2.3). The diagram shows that Customs agents play dual roles in the clearance process; lodge declaration of goods and pay import tax on behalf of importers to Customs.

**Figure 2.3: Process Flow and Import Tax Payment Process**



*Source: Author*

Customs agents around the globe are represented by the International Federation of the Customs Brokers Association (IFCBA), an umbrella body aiming to standardise the practices of Customs agents worldwide (West, 2010). As part of the reform of the services of Customs agents, the IFCBA introduced the ‘best practices model for the licensing of Customs brokers’ in conjunction with the WCO, which highlights the Customs-Business Partnership (IFCBA, 2009). The principle of the best practices model is increasing the professionalism and standards of the Customs agents in providing services to their clients (West, 2010). Some of the key principles of the best practices model are:

- Customs agents should establish standards of professional practice on a national basis.
- Continuous professional development of knowledge and skills through courses, seminars and events provided by Customs brokerage associations as well as corporate in-house training, informal on-the-job training activities, and tertiary education at recognised national educational institutions.
- Customs agents must demonstrate continued financial stability.
- Customs agents must demonstrate high levels of Customs compliance.
- Customs agents training, including e-learning opportunities, should be widely available.
- Suspension or cancellation of a Customs agent’s license must be subject to appeal. Neither suspension nor cancellation should take place until finalisation of the appeal process.

(IFCBA, 2009)

**Table 2.8: Summary of the Customs Brokerage and Licensing Requirement**

Country	Handling of Customs Clearance	Licence/Certificate Required	Requirement/Licensing Parties	References
European Union	Customs representatives (direct or indirect representatives) for example: handling agents, shipping agents, clearing agents, Customs consultants, Customs brokers, etc.	No	No licensing rules apply. For example in the United Kingdom, none of them hold the status of regulated profession. Any reservation is provided with regard to particular categories of persons, as concerns one of the two modes of representation provided in article 5, Community Customs Code (CCC).	(Desiderio, 2007),
The United States	Customs Broker	Yes	Customs Broker Licensed Examination - US Customs and Border Protection	(US CBP, 2014)
Canada	Customs Broker	Yes	Customs Brokers Professional Examination Test - Canada Border Services Agency	(CBSA, 2014)
Australia	Custom Broker	Yes	Training course and national examination - Customs Broker Licensing Authority Committee	(ACBPS, 2014)
China	Customs Broker	Yes	Qualification examination test – General Administration of Customs of the People’s Republic of China	(Desiderio, 2007)
Japan	Customs Specialist	Yes	Qualification examination for registered Customs specialist – Japan Customs (Registered Customs Specialist System was adopted in 1967 when the Customs Brokerage Law was established)	(Japan Customs, 2014)
India	Customs Broker	Yes	Customs Broker Licensing Regulation 2013 – Indian Customs and Central Excise	(Indian Customs and Central Excise, 2014)
Thailand	Customs Broker	Yes	Attend training course. Licence issued by Thailand Customs Department	(Thailand Customs Department, 2014)
Singapore	Declaring Agent	Yes	Registered with Accounting and Corporate Regulatory Authority (ACRA). Assessment appraisal upon registration – Singapore Customs. Declarants must go through test before they can be formally identified as authorised declarants. Certificate of proficiency is issued to successful applicants.	(Singapore Customs, 2014)
Malaysia	Customs agents	Yes	Qualifying Examination Test. Licensed issued by The Royal Malaysian Customs Department	(RMCD, 2014a)

Source: Author

As shown in Table 2.8, Customs agents are generally required to be licensed and regulated by respective laws as required by the respective countries, such as the United States, India and Japan. In Singapore, Customs agents are subject to assessment appraisal and required to register with the Accounting and Corporate Regulatory Authority before they can officially lodge a Customs declaration. The European Union on the other hand does not regulate the activity of Customs brokers. Instead, the Customs clearance process can be conducted by a representative<sup>17</sup> as stated in Article 5 of Council Regulation (EEC) 2913/1992 on establishing Customs community code. Thus, the Customs broker is not a regulated profession under council regulation and importers or exporters may appoint third parties (not necessarily Customs brokers) to act on their behalf.

In Malaysia, Customs agents' practices are regulated under the Malaysian Customs Act 1967 which is administered by the Royal Malaysian Customs Department (RMCD). The agents are represented by their respective Customs agents associations. There are five main bodies of Customs agents associations established in Malaysia representing different geographical locations throughout the country. The five associations are:

- Selangor Freight Forwarders and Logistics Association (SFFLA);
- Johor Freight Forwarders and Logistics Association (JOFFA);
- Penang Freight Forwarders Association (PFFA);
- Sarawak Forwarding Agencies Association (SFAA); and
- Kota Kinabalu Forwarding Agents Association (KKFAA).

In line with increasing the efficiency in international trade, the Malaysian Finance Minister, through the 2003 budget speech, proposed an amendment to Section 90 of the Malaysian Customs Act 1967. It was proposed that the agents attend a course on matters relating to Customs and pass such examinations as specified by Customs (RMCD, 2003). Customs Work Order Number 45 was issued as part of the amendments to the legislation as the guidelines for the Customs to administer the issuance of Customs agent licences as well as the practices of the agents. There are

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<sup>17</sup> Representative refers to third parties, either direct representatives or indirect representatives. A direct representative acts on behalf of the importer/exporter but will have no responsibility for the customs debt arising from their actions, whereas an indirect representative will have a joint and several liability for the customs debt (Council Regulation 2913/1992).

nine codes of ethics that the Customs agents have to fulfil in engaging their duties as agents, and there is a list of prohibitions outlined in Customs Work Order Number 45 (see Appendix 1). The new requirements under the legislations are to ensure that the agents have adequate technical knowledge and practices to ensure they maintain high standards of service for their customers.

Generally, the principle of the Customs agents' practices in Malaysia is to apply the guidelines for best practice issued by the IFCBA and maintain a high standard of practice. However the role of Customs agents is not an easy task. Apart from providing advice and services, as expected by their customers, they also have to fulfil various compliance regimes as set out by the multiple border agencies such as Customs. Customs expects accuracy of goods declarations and payment of import tax. Taxpayers on the other hand seek to minimise their tax liabilities by various means such as by exploiting tax laws (McKerchar, 2007) or more aggressively through the manipulation of the goods declaration (Maclean, 2006).

### **2.3 THE ISSUE OF NON-COMPLIANCE WITH IMPORT TAX PAYMENT**

Global competition is one factor which has forced businesses to pay lower costs of import, by attempting to pay lower Customs duties and taxes. It is a major concern among importers that higher Customs duties and taxes may translate into higher cost of importation. Therefore the importer usually seeks advice either through their legal advisor, Customs broker or accountant, to prevent or circumvent cost (Weerth, 2009).

Administering Customs tax revenue is a challenging task for Customs authorities in many countries, especially when facing tax non-compliance. The problem of non-compliance is an internationally recognised on-going concern and poses a challenging problem for policy makers, tax authorities and ultimately, society (McKerchar, 2001). Published studies and reports indicate that tax non-compliance such as tax evasion is prominent in developing countries and involves significant revenue losses. Studies suggest that about 50% of income tax and 23% of indirect taxes are evaded, which is significant at about 6% of GDP, compared to tax revenues of 18% of GDP in developing countries (Engel, Galetovic and Raddatz, 2001).

Tax non-compliance is commonly associated with a tax gap.<sup>18</sup> The existence of tax non-compliance has a large impact on tax revenue collection and is of great importance, requiring immediate attention by governments (James and Alley, 2002). There are numerous ways to evade tax or opportunities to engage in non-compliance activities. Non-compliance with import tax payment commonly falls under these 6 categories: 1) under-declaration of the true value of goods; 2) misclassification of tariff category; 3) correct declaration of value and tariff classification but underpayment of import taxes based on a false assessment of tax liability; 4) duty evasion where duty is correctly assessed but never paid and the goods are released; 5) smuggling, where goods are imported without the knowledge of Customs officials; 6) falsifying country of origin documents (David Stasavage and Daubrée, 1998; Johnson, 2011; Uzzaman and Yusuf, 2010). Tax non-compliance is sometimes an intentional act of deliberately understating tax, but quite often it is actually unintentional due to lack of knowledge, ignorance, mistakes in reporting or the complexity of the tax system itself (Brand, 1996).

Cases involving non-compliance with Customs law are reported almost monthly in the relevant trade press or trade journals. Case summaries of international cases (Table 2.9) and cases in Malaysia (Table 2.10) indicate some similarities in the type of non-compliance. Under valuation, mis-classification and mis-specifying the country of origin, as shown in the example below, are the three of the most common types of non-compliance cases.

*(i) Under-Valuation of Products*

Under-valuation refers to declaring a lower value than goods are worth (Hui, 2012). The amount of duty which is calculated as a percentage of the value of the goods should be reflected by the value declared. Double invoicing is an example of under-valuation, which is a common method to defraud tax (Javorcik and Narciso, 2008). It is a procedure in which an importer and a foreign exporter agree to divide the per-unit cost between two invoices and present only one invoice at entry. The second invoice for the balance is forwarded to the importer, either before or after entry, and is paid separately. The Customs officials are able to detect the improper value of goods listed on an invoice if they are well seasoned in their work. The double invoicing scheme

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<sup>18</sup> Tax gap is the difference between the amount of tax that should be legally reported against the actual tax reported to the authority (James and Alley, 2002).

will work if all the documents are altered properly. To continue the concealment from detection during port-entry review, the importer alters the purchase order, confirmation order or contracts, changing the accounts payable ledger and attempting to divide payments or deposits. Some importers declare that they are importing fewer goods and at a lower price that they actually are in order to obtain a lower tariff rate. This type of fraud is more difficult to detect because it requires a thorough inspection of the goods imported. Sometimes the arrangement is conducted without the knowledge of their agents, such as Case 5 in Table 2.10. Under-valuation cases involve billions in revenue losses for the government (see Table 2.9 and Table 2.10).

(ii) *Mis-classification of Products*

Tariff or duty rates vary depending on the classification under which the imported goods fall. If the importers improperly describe the imported goods, this may allow them to obtain a lower or free tariff rate. For example through practitioner experience, it is common for a chemical product to be declared under the commercial name of the product. During submission of Customs declaration for clearance, the importer has to provide the material safety datasheet (MSDS) which indicates the itemised ingredients of the chemicals. Determination of the Customs commodity code is based on the type of ingredient listed in the MSDS. There are certain cases of dutiable chemicals where companies provide a false MSDS to avoid Customs duty. In order to deter importers from misstating the description of the imported goods, Customs has wide discretion and can take and retain samples to conduct tests.

Another example is based on an actual case involving a major scam, the case of a garlic importer. This involved the import of garlic amounting to GBP 1.3million by an Irish importer to the UK. In this case, garlic was declared and labelled as apple to avoid higher duty as garlic attracts duty of up to 232%. Tables 2.9 and 2.10 show detailed examples of cases of import tax fraud.

(iii) *Mis-specified Country of Origin*

Mis-specification of the country of origin is the most common method applied to fraudulently lower tariff rates; although the country of origin may also be misstated to circumvent quotas, embargoes or anti-dumping laws (USCBP, 2004). There are instances where goods are shipped from the exporter to an intermediate country and



slightly altered in the intermediate country before finally being transferred to the final destination in another country. The name of the intermediate country is listed as the country of origin even though the goods did not actually originate in the intermediate country. Table 2.9 shows examples of misstatements of the country of origin being used to avoid import tax.

**Table 2.9: Examples of Non-Compliance Cases with Customs Duty Payment - International Cases**

<b>CASE SUMMARY</b>
<p><b><u>CASE 1</u></b></p> <p><b><i>\$1 Billion revenue impact on the treasury for undervaluation of products</i></b></p> <p><i>There is a significant loss of revenue to the federal government due to textile and apparel fraud. The U.S. Treasury loses twice, first because duties are not paid and second, penalties for Customs violations go uncollected by the Customs authority. A 2008 GAO report found that Customs failed to collect half a billion dollars in AD/CVD duties and more recent estimates place that number close to one billion dollars. A large number of importers are deliberately undervaluing textile and apparel imports from China. A single case of duty evasion involving an importer of women's apparel in New York could amount to \$50 million or more (Johnson, 2011).</i></p>
<p><b><u>CASE 2</u></b></p> <p><b><i>Mis-classification of products</i></b></p> <p><i>Paul Begley, 46, of Woodlock, Redgap, Rathcoole, avoided paying Customs duty on more than 1,000 tonnes of garlic from China by having them labelled as apples. Dublin Circuit Criminal Court heard the import duty on garlic is "inexplicably" high and can be up to 232%. Onions have an import duty of 9%. The maximum sentence for the offence is five years in prison or a fine of three times the value of the goods. Officers seized a series of emails between Begley and his garlic supplier in China which were exchanged over the course of four years. He told the supplier to falsify the importation documents to describe the shipments as apples rather than garlic (BBC News, 2012).</i></p>
<p><b><u>CASE 3</u></b></p> <p><b><i>Mis-specified country of origin</i></b></p> <p><i>In an example case of anti-dumping duty on silicon metal, the Commerce Department of the U.S. issued an order imposing anti-dumping duty of 139.4% for importation of silicon metal from China. An importer essentially lied about the origin of Chinese silicon metal to avoid payment of anti-dumping duties. The case was brought to justice and the importer was held liable for almost \$13 million in duty plus interest (Neville, 2008).</i></p>

**Table 2.10: Examples of Non-Compliance Cases on Customs Duty Payment - Malaysian Cases**

**CASE SUMMARY**

**CASE 1**

***Undervaluation of products' value – the case of goods declaration by Customs agents***

*In the case of Wong Ngian Thin v. PP, on application for the removal of goods which was prepared by a Customs agent (Loon On Forwarding Agents) on behalf of their client Khom Yick & Co, the goods declaration was supported by an invoice for the goods supplied by the exporter from Shanghai China. The invoice was false in that both the quantities and prices of the goods were understated. It was accepted by the court that the Customs agent was an innocent participant in the fraud. However, Loon On, being his agent, made the false declaration and its presentation with false invoice to the Customs officers was not an offence under Section 114 (i)(h) as far as Loon On was concerned. However, a conviction for false declaration under Section 113 (i) was recorded instead.*

*(Malaysian Law Journal 167, in Hui, C.P. (2012) Customs Offences. p174)*

**CASE 2**

***Undervaluation of products – intention not to evade or defraud Customs duties***

*In the case of Sung Song Ling v. PP, the accused's explanation was that the declaration which was incorrect in both the quantity and value of goods was intended to obtain the clearance of goods from the Customs border while the correct declaration was produced the next day. The court was of the view that he was quite 'frank' about this and it was accepted by the judge. According to the judge, the preparation of the false declaration was not conclusive of the intention to use it for improper purposes, and if there is a reasonable explanation for all the circumstances, such explanation must be accepted.*

*(Malaysian Law Journal 51, in Hui, C.P. (2012) Customs Offences. p174)*

**CASE 3**

***Ignorance of the dutiable nature of goods***

*In the case of Loh Chan Wan v. PP the defendant, who was charged with attempted fraudulent evasion of duty, was a newcomer to the business of dealing in a Chinese sauce. The sauce contained more than 40% sugar and was dutiable but the defendant claimed that he did not know this. The prosecution's case was based on a letter in Chinese, from which it asked the court to infer that the accused knew that the sauce was dutiable. However the accused's explanation that he was new to the business and not aware about the contents of the sauce was accepted by the court because the translation of the letter was vague or ambiguous.*

*(Malaysian Law Journal 68, in Hui, C.P. (2012) Customs Offences. p180)*

**CASE 4**

***Mis-classification and under-valuation***

*SE Supreme Marble and Granite Sdn Bhd is a furniture manufacturer and marble top trader. The company imported marble tops (Import Duty 30% + Import Sales Tax 10%) from China, Cambodia and Vietnam and declared them as part of furniture (Import Duty 0% + Import Sales Tax 10%). The marble top is actually sold directly to their buyer instead of being used as part of furniture. Furthermore the value being declared was lower than the actual purchase value. The amount of Customs duty and taxes involved amounted to MYR74,707 (GBP15,000) was recollected according to Section 17(1) Customs Act 1967 and Section 30(1), Sales Tax Act 1972.*

*(Compendium of PASCA Import and Company Auditing Cases, p61-63 (RMCD, 2010b))*

## **CASE SUMMARY**

### **CASE 5**

#### ***Dutiable goods declared as non-dutiable with the intention to defraud Customs duties***

*Gemcard Sdn Bhd is an importer of smart cards and plastic cards, and supply their products directly to buyer. The smart cards are subject to 20% import duty and 10% import sales tax but were declared as non-dutiable under a different Customs classification code 8542.10.000 instead of 8523.30.000. The amount of Customs duty and taxes involved amounted to MYR193,546 (GBP38,709). The company was charged according to Section 133 (1)(e) Customs Act 1967 which involves fines up to MYR500,000 (GBP100,000) and 5 years imprisonment for the intention to defraud Customs duties.*

*(Compendium of PASCA Import and Company Auditing Cases, p67-69 (RMCD, 2010b))*

### **CASE 6**

#### ***Incorrect declaration of dutiable goods***

*In the case of PP v. Yong Nam Seng and Anor, One W. H. Ltd contracted with the Army to carry out certain works which require plate glass (dutiable goods) which had to be imported. The army endorsed a declaration form claiming exemption from duty (under Customs Duties Exemption Order, 1959) showing the quantity of glass required. It was found during Customs examination at the border that the quantity of glass was considerably in excess of the quantity shown in the declaration form. The defendants were charged under Section 129(1)(a) and 120(1)(e) of the Customs Ordinance.*

*(Malaysian Law Journal 85, in RMCD. (2010a), A Compendium of Customs Legislation and Cases (1932-2009) (Vol 1-3.) p520)*

### **CASE 7**

#### ***False declaration***

*In the case of Oceanborne Agencies Sdn Bhd v. PP, the defendant was charged with attempted fraudulent evasion of duty by producing a false declaration. The cargo was said to contain 289 bags of copper slag whereas in truth and in fact the cargo contained 40 bags of copper slag, 200 units of motor-car-tyres and 815 rolls of assorted textile materials. The defendant thereby committed an offence under Section 133(1)(a) of the Customs Act, 1967.*

*(Malaysian Law Journal 349, in RMCD. (2010a), A Compendium of Customs Legislation and Cases (1932-2009) (Vol 1-3.) p2481)*

### **CASE 8**

#### ***The case of Customs forwarding agents***

*In the case of Customs Director General v Ho Kwan Seng, the defendant, the sole proprietor of Oriental Forwarding Agency at Klang, was granted permission to transact business relating to import and export of goods by Customs authority under Section 90(1) of the Customs Act, 1967. However during the course of conducting his business, the defendant was alleged to have committed two offences under Section 135 (1)(g) and fined \$1,000 and \$11,530.48 respectively. The Customs agent license was revoked in connection with the offences under the pursuance of Section 90(4) Customs Act, 1967.*

*(Malaysian Law Journal 152, in RMCD. (2010a), A Compendium of Customs Legislation and Cases (1932-2009) (Vol 1-3.) p912)*

These acts of non-compliance with Customs law could affect revenue collection; damage a country's image or reputation; hinder foreign direct investment (FDI); and present a threat to social justice (Torgler, 2003; Wenzel, 2007). Although some of the reasons underlying the motives for non-compliance are unintentional, such as in Cases 2 and 3 (Table 2.10), it is apparent that non-compliance is a complex issue that requires a deep understanding. This complexity poses a challenge to the administration of the tax organisation in its aim to achieve its objectives and develop holistic plans to increase compliance levels among businesses (Andreoni et al., 1998; Murphy, 2005; Wenzel, 2007).

## **2.4 THE RELEVANCE OF MALAYSIA IN THE CONTEXT OF THIS STUDY**

### **2.4.1 Historical Context**

There are several reasons for the selection of Malaysia for the purpose of this study. The historical context of tax compliance in Malaysia provides an interesting insight into the evolution of compliance issues on Customs duty payment. In the case of Malaysia the problem of compliance has long existed since the first Customs tax was introduced during the great Malacca Sultanate Empire in the 14<sup>th</sup> century. The Malacca Sultanate was the largest and the most prominent in the Malay Archipelago and controlled the whole of the Peninsular of Malaysia and East of Sumatra (see Figure 2.4). The Malacca Sultanate was the most powerful administration during the 14<sup>th</sup> and 15<sup>th</sup> centuries. The function of Customs and other border agencies already existed through the Malacca Sultanate Administrative System. The collection of tax from both local and foreign merchants was the responsibility of the Harbour Master who reported directly to the Chief of the Exchequer or Finance Minister. Customs duties during the time of the Ruler (Sultan) of Malacca were collected from traders and shippers who came to Malacca's ports importing goods such as tin, gold dust, tobacco and opium (Hussin, 2007).

**Figure 2.4: The Malacca Sultanate Empire in the 14<sup>th</sup> Century**



*Source: Britannica (2011)*

The duties were at their highest during this period. Every commodity imported or exported was required to be weighed in accordance with the port's standard measures and custom duties were payable, with considerably higher duties imposed on imports than exports (Gullick, 1981). The high rate of duty forced the majority of traders to evade tax by smuggling goods into the territory. Although the enforcement team was established to deter smuggling activities, the long coastline of Malaysia provided opportunities for goods to be traded illegally and this practice was prevalent among European traders who avoided the high Customs duties (Hussin, 2007). This suggests that non-compliance was a problem in Malaysia as far back as the 14<sup>th</sup> century, when Customs duties were first introduced as a tax regime for the country. This history also suggests the necessary presence of an enforcement team in the early establishment of Customs administration.

#### **2.4.2 Complexity in Managing Compliance**

Malaysia is one of the fastest developing newly industrialising economies (NIEs) of South-East Asia. The industrialised 'look east policy' introduced by the former Prime Minister Tun Mahathir Mohamad in the 80's transformed Malaysia from an agriculturally based economy into an industrialised nation and placed Malaysia as one of the most important trading partners of major economies such as

the United States, China and Japan (Jomo, 2007). The value of import and export increased over the years, amounting to MYR606 billion of import and MYR702 billion of export in 2012 (Department of Statistics Malaysia, 2013).

The increase in trade through the numerous ports of entry to Malaysia added to the complexity of managing compliance and dealing with Customs clearance. There are three major ports located in the Peninsular of Malaysia, namely Penang Port in the Northern Region, Johor Port (the 19<sup>th</sup> Largest port in the world) in the Southern Region and Klang Port in the central region (the 12<sup>th</sup> largest port in the world) (WSC, 2013). These ports handle both import and export containers for traded goods, while the air cargoes are handled by the cargo handling terminal located in the central region at Kuala Lumpur International Airport (KLIA). Technology usage such as gate control systems (GCS), container scanner machines and risk assessment systems are also in place to improve compliance, facilitating trade and preventing revenue leakages through smuggling activities by targeting suspicious cargoes.

This is part of the RMCD reform, to modernise Customs administration in line with the WCO guidelines and conventions to cope with challenges in the trade environment and the need for expediting trade movement. However, the shifting of the Customs task to emphasise documentary control and minimum physical inspection (as required by international organisations) has increased the potential and opportunity for illegal trade channels or fake trade declarations for the purpose of evading payment of duties and taxes. The increasing threat of organised crime such as smuggling dangerous goods, counterfeited goods and high dutiable goods are some of the challenges that RMCD faces in the current trade environment (RMCD, 2010c). According to the RMCD Director General, part of the Customs transformation plan introduced by the department is to increase enforcement activities by the RMCD enforcement team. The teams are located at the major ports and the Malaysian border, and aim to prevent smuggling activities (Utusan Malaysia, 2013). High dutiable goods such as tyres and tiles are among the goods being commonly smuggled into Malaysia. Considering the existence of numerous ports of entry into Malaysia and the relatively high rates of duty charged on shipments imported into the country, it is believed that the amount that was successfully smuggled in was larger still, and that the amount apprehended was just the tip of the iceberg.

### **2.4.3 Increasing Cases of Non-Compliance**

Despite advancements in technology, the presence of tight legislative requirements and increasing enforcement efforts by the RMCD, non-compliance with Customs law keeps increasing over time. Compliance is the main concern of RMCD, which led to the establishment of the Compliance Division in the Customs headquarters in 2008. Statistics from RMCD, as shown in Table 2.11, indicate that uncollected revenues due to non-compliance by taxpayers are worth between MYR410 million and MYR1.8 billion for the years 2011 to 2014. Among the various forms of tax and duties, import tax (Customs duty, import sales tax and import excise duty) has the lowest level of compliance, compared to domestic sales and services tax. The average figures for 2011 to 2014 record the highest amount, worth MYR734 million or more than 60% of all non-compliance cases, compared to other types of indirect taxes such as domestic sales and services tax. Non-compliance cases in Malaysia concerning import tax commonly involve under-declaration of value, mis-specified country of origin or misclassification of products (Hui, 2012; RMCD, 2010a; The Star, 2012).

The compliance regime adopted by RMCD is heavily based on enforcement programmes such as the audit programme, which involve a huge budget and many enforcement officers (Mansor, Tayib and Yusof, 2005). The additional costs and time spent on enforcement efforts do not justify the increasing problem of uncollected duties and taxes due to non-compliance cases (such as the cases of under-declaration) that could reach as high as MYR8bil (GBP1.6 billion) yearly (The Star, 2012), as compared to the cases detected by the enforcement team. Thus, it is interesting to investigate the relevance of various compliance regimes such enforcement, as well as other international instruments, as a compliance framework to secure revenue collection and facilitate trade movement. Therefore, the case of Malaysia provides a fine example and further understanding of a small country that is seeking to improve the country's competitiveness, while struggling to improve the level of compliance, in order to avoid leakage in tax revenue.

**Table 2.11: RMCD Non-Receivable Account for the Year 2011 to 2014**

Type of Duty/Tax	2011		2012		2013		2014	
	MYR / Million	%	MYR / Million	%	MYR / Million	%	MYR / Million	%
Customs Duty	150.41	36.64	599.51	65.49	648.93	38.65	619.94	33.30
Local Sales Tax	62.89	15.32	78.60	8.59	491.35	29.27	542.26	29.13
Sales Tax Penalty	24.49	5.97	38.19	4.17	42.5394	2.53	66.61	3.58
Service Tax	48.84	11.90	59.96	6.55	75.66	4.51	101.5	5.45
Service Tax Penalty	47.62	11.60	60.46	6.60	71.77	4.28	84.94	4.56
Import Sales Tax	50.84	12.38	53.20	5.81	271.39	16.17	293.13	15.75
Import Excise Duty	24.18	5.89	20.45	2.23	68.51	4.08	137.96	7.41
Other Tax	0.23	0.06	4.16	0.45	4.01	0.24	2.76	0.15
Surcharge	0.88	0.21	0.80	0.09	1.25	0.07	1.44	0.08
Export Duty	0.14	0.03	0.14	0.02	3.37	0.20	11.05	0.59
Total	410.52	100.00	915.47	100.00	1678.78	100.00	1861.59	100.00

*Source: RMCD (2015b)*

#### **2.4.4 High Dependency on Customs Agents**

In a Malaysian context, as discussed in Section 2.3, importers outsource 90% of Customs clearance tasks on import/export of goods to Customs agents. The current framework provides the advantage that Customs agents are present and dominant in providing their services (Customs clearance services) to business communities. Unlike in other countries, such as in the EU, where importers may appoint either Customs brokers (Customs agents) or other representative such as freight forwarders, shipping agents or consultants to clear the goods on their behalf. Furthermore access to the Customs information system (SMK Dagang Net system) to lodge the Customs declarations is currently subscribed only to Customs agents and a small percentage of companies.

The recent declaration on trade facilitation which suggests the lifting of mandatory usage of agents (WTO, 2013), makes Malaysia an interesting study case, as high dependency on Customs agents might have an impact on compliance. In some countries which do not regulate the profession of customs agent, the impact on customs compliance may differ, as their customs agents may not have a direct responsibility for any liabilities. Therefore the overall impact on customs compliance differs across countries.



#### **2.4.5 Practitioner's Perspectives**

Finally, research into this area is hard to come by, despite its obvious importance, particularly to developing countries whose economies are normally characterised by various trade policies and restrictions. One possible reason for the dearth of research is the sensitivity of the issue as it relates to under-payment of duties and has legal implications for participants in research associated with it. However, the experience of the researcher with The Royal Malaysian Customs Department, and his access to the industry and data, provides an excellent opportunity to explore and gain understanding of the issues of non-compliance with customs duty payment.

### **2.5 THE NEED FOR FURTHER ENQUIRY**

The collection of customs duties and taxes on import will remain important for many countries for many years, despite the declining tariff rates due to successive rounds of trade liberalisation and major obstacles in collecting tax revenue (World Bank, 2006). The issue of non-compliance with duty payment and taxes is one of the obstacles faced by many customs administrations worldwide, and it could pose serious threats to economies and societies. Undervaluation, mis-classification of products and mis-specification of country of origin are some common practices which deflate revenue collection.

Malaysia is an example of a country which relies on customs revenue as one important source of tax revenue, but struggles with the long standing issue of compliance. The historical background, tax structure and regulatory requirements contribute to the problem of compliance in Malaysia. Furthermore, heavy reliance on customs agents, who account for about 90% of trade transactions, makes the management of customs agents' activity in Malaysia an important area on which to focus, to increase compliance. Although there are increasing enforcement efforts, and specific provisions in the Customs Act 1967 that set high penalties, tax compliance among businesses remains low, and is a major problem, according to the statistical report of uncollected revenue. Import tax which includes customs duty, excise duty and import sales tax, is the highest in terms of non-compliance cases, which account for 50%, compared to other types of indirect taxes such as domestic sales and services tax. Furthermore, practitioner experience identifies non-compliance cases such as

misclassification of products, lack of clarity in descriptions, and product prices that are declared at a lower level than commonly accepted, contribute to the reduction in customs revenue.

The problem of compliance, as highlighted, is a complex issues which needs to be further investigated. There is the possibility of examining customs agents or importers in order to understand what motivates them to comply (or not to comply) with customs law. Are they personally motivated by their own attitude to maximising personal wealth, ignorance, frustration with institutional policy, or weak enforcement by Customs? This study attempts to explore this issue by investigating senior customs officials, which is further explored in the following chapter. It aims to provide an understanding of compliance from the perspectives of customs officials. The findings provide some indication of how the compliance of customs agents, or possibly importers, could be improved and this is useful for the development of the holistic import tax compliance model of this study.

## **CHAPTER 3**

### **EXPLORATORY STUDY AND INTERVIEW ENQUIRY**

The purpose of the exploratory phase is to gain understanding and explore the under-researched phenomenon. This phase explores and describes how Customs officials perceive the phenomenon of non-compliance in Customs import declaration. Interview enquiry was conducted with eight Malaysian Customs officials. This section provides brief background information on each of the eight officers with pseudonyms assigned to each, in order to protect their anonymity. The outcome of the interviews is discussed in the remaining section of this chapter.

#### **3.1 EXPLORATORY STUDY**

The objective of this exploratory study is to gain understanding about compliance of businesses with import tax payment. As a practitioner at the Royal Malaysian Customs Department (RMCD), the decision to undertake this research is motivated by the practitioner's experience and observations of non-compliant businesses with Customs law and regulations. The problem in this study had been identified through experience and observation prior to conducting the study. Although it could be argued that choosing the research problem through personal experience seems risk-based, it could lead to greater potential for successful research (Corbin and Strauss, 1990).

Therefore, the exploratory research phase attempts to clarify the objective of this study, which is to understand compliance of businesses with import tax payment. The previous chapter outlines evidence from the practitioner's experience and relevant literature, which provides some background to the problem of this study. It is uncertain at this stage which parties, importers, Customs agents or other business groups, actually lead to the problem of non-compliance. It is not the primary purpose at this stage to provide conclusive evidence, but rather to crystallise the research problem and provide some direction for subsequent research (Zikmund, Babin, Carr and Griffin, 2013).

The exploratory research method or strategy has traditionally been viewed as a useful tool for the preliminary, or exploratory, stage of a research project (Babbie, 2007; Creswell, 2009; Maxwell, 2012; Zikmund et al., 2013). Several authors have provided references for the need to conduct exploratory study. According to Babbie, (2007), exploratory study is conducted especially if the problem in the research area has not been clearly defined, but is identified in the preliminary stage of the research. It is used to seek insights into the general nature of a problem or phenomenon without explicit expectation (Schutt, 2012). Schutt added that the method of exploratory study is highly flexible, unstructured and designed to uncover basic viewpoints, perceptions and attitudes.

Maxwell (2012) provides an interpretation of exploratory study which coincides with the purpose of this study. According to Maxwell, exploratory study “is not simply a source of additional concepts for theory; instead it provides an understanding of the meaning that these phenomena and events have for the actors who are involved in them, and the perspectives that inform their actions” (Maxwell, 2012, p228).

The common ground of the interpretations of exploratory study by various authors is about reaching a better understanding of the research problem, which includes helping identify the variables to be measured within the study. When there is little understanding of the topic, it is impossible to formulate a hypothesis without some exploratory studies. In this exploratory study, the main purpose is to diagnose the situation (Creswell, 2009; Zikmund et al., 2013) and develop an understanding in an area that is little understood (Blaikie, 2009; Marshall and Rossman, 2011) as there is little knowledge about the situation or information about how similar problems or research issues were solved in the past. Thus, it deepens the understanding of the phenomenon of non-compliance with import tax payment and the actors involved. In this study, the relationship between compliance practices of the businesses community (such as importers and Customs agents) and import tax payment is investigated, to determine the real nature of the problem.

Therefore, it assists in identifying the plausible relationships that shape the phenomenon of interest (Marshall and Rossman, 2011), providing clear answers to the various types of research questions and the research problem and determining the best research design, data collection method and selection of respondents for the study. The results of the exploratory study are anticipated to provide significant insight into

the given situation, but to be insufficient for decision-making purposes.

In exploratory study, several approaches are suggested for obtaining qualitative data depending on their suitability for the research. The suggested methods include focus groups, case studies and interviews (Zikmund et al., 2013). For the purpose of this study, the interview method is selected for a group of practitioners (Malaysian Customs officials). The pilot study was carried out to explore their views on the phenomenon of the study. Interview is the best method for this exploratory stage as the topic could be sensitive and open discussion, such as the focus group method, might not yield the desired results. Therefore, one-to-one interview is used to allow respondents to talk more freely. Through an in-depth discussion, it is anticipated that the interview would provide some research direction for the study.

## **3.2 INTERVIEWS**

### **3.2.1 Background of the Respondents**

Several authors propose specific numbers of interviews to be conducted. Polkinghorne (1989) for instance, recommends between 5 and 25 interviews, while Bertaux, (1981, cited in Guest, Bunce and Johnson, 2006) suggests 15 as the smallest acceptable sample size. However, there is no definite number of interviews that qualify as sufficient in any qualitative study; although there is the guiding principle of 'saturation', a concept which is highly debatable (Mason, 2010). Saturation is a matter of degree, when pursuing additional data becomes counter-productive and new discoveries do not add value to the ongoing research project (Strauss and Corbin, 1998).

As Murphy et al. (1998) state, study samples in qualitative research are not necessarily static or shaped by the original conceptualisations in the research design, but are recurrent and emergent in nature. This is referred to as iteration or an iterative process. Within qualitative research, the study sample is identified both at the start of the study and during the emergent research design, so it may not be possible to fully specify the number of participants required at the start of the study.

The selection of respondents is based on: (I) the number of years of practitioner experience; and (II) being ranked as a senior officer of Customs<sup>19</sup>, or equivalent managerial level in other public sector organisations. At this stage, they have reached the post-formal operational level of thinking, have intellectual capacity and have developed strong tacit knowledge in their area of expertise. In practical terms, they are the appropriate target group, capable of providing the information required for the purpose of this study (Commons, 2008; Gibbons, Limoges and Nowotny, 1994; Sweller, Merrienboer and Paas, 1998). Eight senior officers in the Royal Malaysian Customs Department (RMCD) comprising operational staff, policy makers and Customs trainers at RMCD academy were selected for this purpose. Those who participated in the interviews comprise a wide range of positions within the Customs department. The participants' positions range from Grade W41 (Customs Superintendent) to W54 (Deputy Director of Customs) with 10 to 30 years of working experience (see Table 3.1).

**Table 3.1: Background of the Key Employees of The Royal Malaysian Customs Department**

Respondent	Designation	Grade	Gender	Length of Service
Res 1^	Senior Assistant Director of Customs I	W52	M	29
Res 2^	Senior Assistant Director of Customs II	W48	M	24
Res 3^	Assistant Director of Customs	W44	M	22
Res 4*	Superintendent of Customs	W41	F	10
Res 5^	Deputy Director of Customs	W54	M	31
Res 6^	Senior Assistant Director of Customs II	W48	M	17
Res 7*	Assistant Director of Customs	W44	M	19
Res 8 *	Assistant Director of Customs	W44	M	15

Note: \* Recorded interview

^ Note taking

<sup>19</sup> Senior officers of Customs are also referred to by their professional and managerial level in the public services in Malaysia (Public Service Department Malaysia, 2011).

### **3.2.2 Interview Sessions**

The interview sessions took place between March and April 2011. All interviews were conducted by telephone, which produces data comparable to the quality of data obtained through face-to-face interviews (Carr, 2001). Although telephone interview was selected primarily due to cost (Cachia and Millward, 2011; Opdenakker, 2006) and geographic distance (Opdenakker, 2006; Sturges and Hanrahan, 2004), there are other advantages that are worth considering. It provides an opportunity to conduct interviews asynchronously at any location and at the comfort of the participants due to work commitments and time constraints (Cachia and Millward, 2011). Telephone interview also has the advantage of making it easier to openly discuss sensitive issues, compared to face-to-face interview (Opdenakker, 2006). Participants are more relaxed and willing to communicate more freely, including disclosing intimate information (Novick, 2008). They would not feel comfortable, and may be reluctant, to discuss sensitive topics if a face-to-face interview technique were applied (Opdenakker, 2006), especially in this study, which touches on paying tax and compliance with the law.

Respondents were contacted prior to the actual interview session to seek their approval to participate in the interview. Participation in the interview was on a voluntary basis, and the respondents were not obliged to participate. The respondents were briefed about the purpose of the interview, and told that their anonymity would be protected and not disclosed. Each interview session lasted approximately 15 to 20 minutes. The primary interview data recording technique was the use of a voice recording device. This has the advantage of capturing the whole interview conversation more faithfully than written notes (Hoepfl, 1997). There are views that recording the conversation is not recommended, based on the intrusiveness of the device for the interviewee (Lincoln and Guba, 1985). However, the choice of whether to use a recording device or written notes is a personal preference (Hoepfl, 1997). To ensure that the qualitative data from all the participants were captured, written notes were used as the secondary recording technique, in cases where participants refused recorded conversation.

Out of eight interviews, five respondents chose not to record the conversation. Thus, the gist of the discussion, important points and quotes from the interviews were recorded in the form of written notes. During the interview session, the respondents

were reminded about the purpose of the interview at the start of the conversation. They were first asked about the latest developments in Customs administration, rather than focusing on the core question, to allow them to feel more relaxed during the conversation and to talk more freely about the issues at hand (Burke and Miller, 2001). Subsequent questions were asked about their opinions on issues of businesses and their compliance with Customs law and regulations, specifically the declaration of import, which affects the collection of revenue for the government. The question posed was open-ended, in order to allow flexibility in the response and to allow the respondent to talk freely about the subject matter.

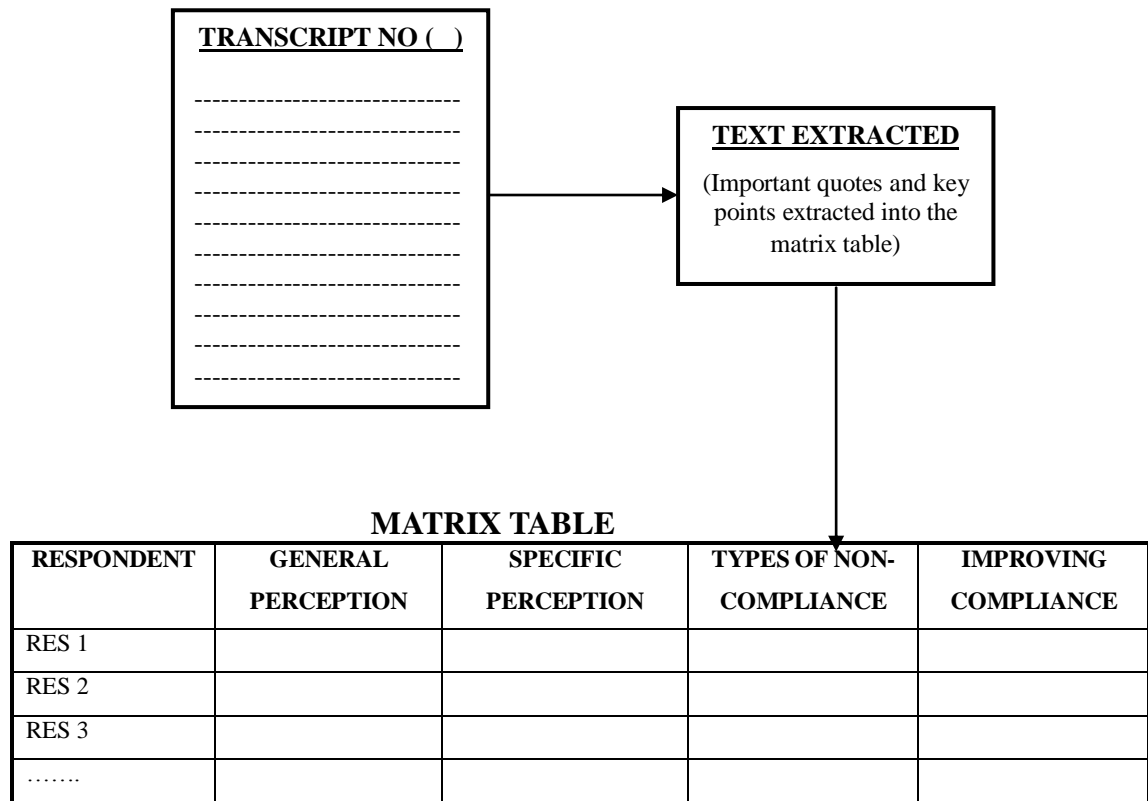
The interview was conducted in the Malay language, which is the official language used in daily communication in the public administration department in Malaysia. The interviews were later transcribed to facilitate further analysis and refine the research context.

### **3.3 DATA ANALYSIS AND FINDINGS**

#### **3.3.1 Data Analysis**

The interview data was analysed manually using Microsoft™ Excel software. This method of analysis was selected as opposed to QDAS (qualitative data analysis software) as there was a small sample size of eight interviews. As the main objective of this exploratory phase was to understand the phenomena, analysis was conducted primarily to uncover the issues and define the research focus. To achieve this, a simple analysis was conducted classifying the findings into a matrix table. For this purpose, the key findings or the quotes from the interview transcripts were extracted and pasted into the matrix. The following flowchart (Figure 3.1) provides a sketch of the process of analysing the interview data.





**Figure 3.1: Data Analysis Flow Chart**

*Source: Adapted from Lillis, (1999)*

### 3.3.2 Interview Findings

The eight senior Customs officials interviewed provided interesting insights into the issues and questions posed on the phenomena of tax underpayment in the declaration of import.

When the initial question was posed, about their opinion of business compliance with Customs law, most of the officers responded negatively with statements, as follows:

*“Regulatory compliance is a good area to look at. The issue of compliance is an on-going problem in our business community” (Res 5)*

*“Business compliance rate in Malaysia is still low compared to developed countries. It is part of the culture. We can change the procedure, increase penalty and compound, but it is hard to change the attitude” (Res 3)*

*“This is the mentality of our businesses. They are too profit-oriented and there is lack of awareness in following rules and procedures” (Res 2)*

*“This is the hardest area that we have to face in our routine work. Not all businesses are honest, especially in paying tax” (Res 1)*

Specific questions were asked about the on-going issues related to Customs import declaration, which results in loss of revenue for the government. The majority of the Customs officials interviewed said that Customs agents were the main culprits, causing Customs to lose revenue due to non-compliance in the declaration of imported goods.

*“In every import declaration, there will be a column that agents have to sign, he/she is responsible for what is being declared, not the importer.” Senior Officer 6 (Res 5)*

*“The focus on compliance should be on the forwarding agents, not the importer. Importer just furnish the required documents, while the agents manipulate the declaration to pay lower duty” Senior Officer 4 (Res 1)*

*“Agents are the one who lodge the declarations. They are supposed to know the correct way to lodge import declarations” (Res 6)*

*“ If they declare correctly, they will not gain much profit. For example, if they were given RM10000, they will try to evade part of the amount to maximise their profit. So, in theory, they will not declare accordingly” (Res 7)*

It was perceived that the issue of non-compliance in import declaration was mainly due to the Customs agents. The tax paid by the importer through the agents is often abused by the Customs agents through various means of defrauding to reduce the tax to be paid to the Customs department.

*“payment of tax by the importer is through the agents’ account because the forwarding agents are the only party that can make payment to the Customs department, which is by EFT (Electronic Fund Transfer). This is why the agents can provide their service in a ‘package’ and do not lodge the correct declaration. I think this is the main reason why non-compliance cases are rampant now” (Res 7)*

*Through my experience in ‘fabricated cases’, usually the agent who fabricates the documents wants to pay lower import tax or avoid paying import tax” (Res 8)*

*“Normally it is the agents who declare the price artificially” (Res 4)*

The Customs officials further elaborated that tax declaration on import could be defrauded in many ways such as: (1) devaluation of goods; (2) manipulation of Customs goods classifications to lower tariff of tax; or (3) manipulating the quantity of goods declared to pay less tax.

*“A lot of cases in import declaration, not all items being imported were declared especially in mixed consignments. Devaluing the prices of goods and manipulation of tariff code are common cases that we have identified” (Res 1)*

*“They sell their services as a ‘package’. They will quote their customers a specific price for a shipment and then work out on how to meet the price on the declaration. That’s where they play around with the pricing, quantity, tariff code etc.” (Res 3)*

*All of the dutiable goods are subjected to tax evasion. Even fruits were declared at lower prices. You can imagine thousands of containers of fruits being imported monthly. How much will the government lose in its revenue? That does not include high duty items such as tyre, liquor, electrical goods” (Res 6)*

*“In reality, the agents manipulate the tariff code and value to pay lower tax” (Res 8)*

*“Declare less quantity, declare lower value, declare the goods partially or declare the dutiable goods as non-dutiable goods or the tariff that has a lower tax value. These are the various ways that are commonly used by agents to evade tax payment” (Res 7)*

*“I found that the pricing of goods declared is the most problematic. Sometimes, the declared price doesn’t make sense. Fabric, for instance, is declared for less than RM1per kg. How much is it being sold on the market per meter? Does this make sense?” (Res 5)*

Although the interview findings provided some insights into the issue, it was apparent that the Customs officials viewed that the problem is longstanding, and is not easy to tackle. Thus, enforcing rules alone would not prevent non-compliance cases.

*“Enforcing the rules as outlined in our Customs Work Order No.45 where they have to sit for the test is part of the departments’ effort to increase their knowledge. They would also aware about their responsibility to the Customs and their represented client to improve the level of compliance” (Res 6)*

*“Forwarding agents represent their clients, whether importer or exporter. They need the business. They will follow what their clients want, not us. We will continue to face the problem of agent not complying with our rules and procedures especially in paying the correct amount of duties and taxes” (Res 3)*

*“We have to educate the businesses, provide them with proper advice and play our role in ensuring the laws are properly enforced so that there is no leakage in the revenue” (Res 2)*

The enquiry identified the area of focus for this study. The main research objective was to understand the factors that would influence compliance of Customs agents, focusing on import tax and Malaysia as the context of the study. The subsequent steps are to investigate the literature to understand what has been written so far in this research area, specifically (I) to identify the gap in this study and the aim in addressing this gap; and (II) to operationalise the study by finding a suitable theory and method.

### **3.4 DISCUSSION AND DEFINITION OF THE RESEARCH FOCUS**

It is highlighted in the previous section that the issue of non-compliance with import tax payment is a global phenomenon experienced by many countries, especially developing countries. The act of non-compliance affects tax revenue collection which is a significant problem for most governments, including Malaysia.

Initial interviews with eight Malaysian Customs officials provide insights into how the issue is perceived and provides some direction for the study. They all had 10 to 30 years experience with the Customs department. The results of these interviews were consistent. Their experiences and perceptions of the issue were unanimous, that Customs agents are the core focus of the issue of non-compliance with Customs import declaration. According to the interview findings, improper declarations by Customs agents<sup>20</sup> are the cause of non-compliance. According to the findings, improper declarations or mis-declaration based on value, type, number, weight, measurement or origin results in the loss of Customs tax revenue.

They are also of the opinion that Malaysian Customs could collect more revenue if Customs agents were more transparent and honest when lodging their customers' import declarations, but this is not the case. It is worrisome that this issue will lead to more serious offences if it is not handled properly. Although there is a

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<sup>20</sup> Customs agents are the intermediaries between importers, as their client, and government agencies at borders such as the Customs department during the clearance of goods. Their function includes lodging declarations of goods and paying Customs taxes on behalf of the importer.

view that the importer should be penalised, the majority of the officers disagreed with importers being the main culprit in under-declaring tax payment.



**Figure 3.2: Understanding Import Tax Payer's Compliance**

*Source: Author*

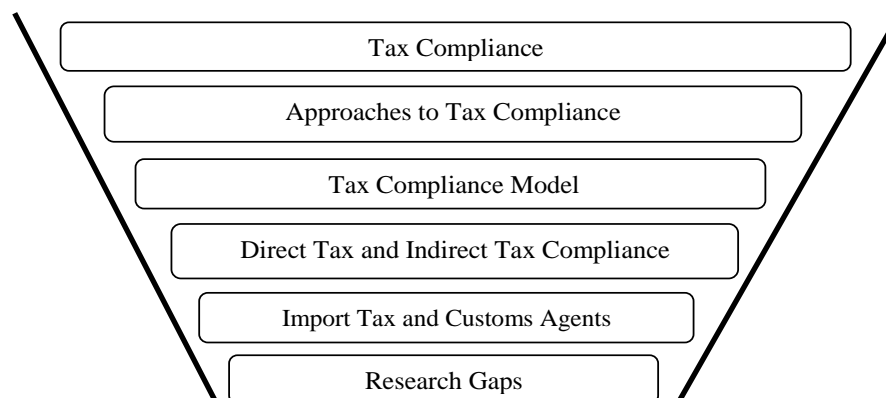
According to Schisler, (1995), three major participants affect the level of compliance: 1) the government, 2) tax agents, and 3) taxpayers. Thus, the focus of this study is based on the fact that agents play a key role in the decision for compliance. Based on the interview findings, the focus is on Customs agents, and the main subject of the study is to understand their behaviour. Figure 3.2 gives a snapshot of the focus of the study.

In understanding the phenomenon of non-compliance and the dimensions of compliance behaviour, extensive tax compliance literature is reviewed covering both direct and indirect tax, to ascertain the most appropriate model for this study. Tax compliance literature is selected as the primary literature because of its relevance to the study which involves fiscal policy on taxation, as well as the need to understand the determinants of compliance behaviour and the theories that have been applied. Chapter 4 (the literature review) elaborates on the theory and identifies models applied in studies of tax compliance.

## CHAPTER 4

### REVIEW OF LITERATURE AND RELEVANT THEORIES

The key purpose of this chapter is to provide guidance and direction for this study to develop a model of import tax compliance. The findings in Chapter 3, the exploratory study, provide an indication for this study to focus on: (I) Customs agents as the subject of this study; and (II) tax compliance on import declaration as the area of focus for this study. Aligned with this, the following sections in this chapter give an account of key tax compliance literature and other inter-disciplinary literature. The aim is to provide a solid background through the understanding of relevant research conducted specifically in the area of tax compliance, including the key theories and variables. This allows this study to identify: (I) a research gap for the study to address; (II) a suitable theory for this study; and (III) how the study can be operationalised to achieve the research objectives. Figure 4.1, below, illustrates the structure of this chapter. The first section provides background to the broad concept of tax compliance. The second section describes the two approaches to tax compliance studies. Section 3 identifies the models applied in understanding tax compliance. Section 4 further discusses the development of tax compliance studies. Section 5 refines the discussion and identifies the research gap. The chapter concludes with the way forward for this study with the application of the theory of planned behaviour (TPB) as the base theory, through which to examine various compliance determinants in the subsequent chapter.



**Figure 4.1: Literature Review “Funnel”**

## **4.1 TAX COMPLIANCE**

Tax compliance is one of the main areas of concern for tax authorities. Almost all taxation systems face the problem of taxpayers not complying with legal requirements. The following section will therefore elaborate and discuss the concept of tax compliance, the development of tax compliance studies and the research gap in tax compliance studies, specifically in the context of import tax.

### **4.1.2 Taxation and Tax Compliance**

Taxation has been the interest of study by English classical economists such as Adam Smith. Adam Smith, in his book '*The Wealth of Nations*' which was published in 1776, suggested 'four maxims' for the principle of taxation. He proposed that a tax system be based on certain basic principles, namely equity, certainty, convenience and efficiency (Smith, 1776). While the ideal tax system may build upon these four principles, the main purpose of a taxation system is to serve as an economic benefit by generating revenues for the government for public expenditure (Lymer and Hasseldine, 2002). Taxpayers are required to comply with the tax system that has been established, which is regulated by tax law (James and Alley, 2002; Niemiowski and Wearing, 2003).

To understand taxpayer compliance, it is important to understand the concept and meaning of tax compliance. There are various definitions of tax compliance, ranging from a narrow law enforcement approach to a wider definition related to economic and non-economic decisions. The definition of tax compliance in its most simple form is usually cast in terms of the degree to which taxpayers comply with the tax law (James and Edwards, 2007). Specifically, tax compliance from the direct taxation point of view is defined as "reporting all income and paying all taxes in accordance with the applicable laws, regulations and court decisions" (Alm, 1991). Alm (1991) further asserts that to remain compliant with tax law, income taxpayers have to submit all required tax returns and accurately report tax liability in accordance with specific rules and regulations. Taking a narrow perspective, tax compliance is geared towards measuring the 'tax gap', which refers to the actual revenue versus the actual amount to be collected. Moreover, under this definition of tax compliance, taxpayers' who do not comply with tax law or do not accurately pay taxes are categorised as tax evaders (Andreoni, Erard and Feinstein, 1998). Thus, it is presumed

that taxpayers who do not comply with the tax law have the intention to evade tax.

Although most legal definitions refer to the term ‘tax gap’, it has been contended that taxpayers may not always share similar interpretations to the tax authority, and there may be some difficulties for taxpayers in interpreting tax law (Bergman, 1998). Bergman (1998) asserts that tax authorities assume that legality rules taxpayers, whereas the ability of taxpayers to comply with tax law is determined by other factors, such as their willingness to comply with the tax system. Willingness to comply is similar to the definition of tax compliance used by Andreoni et al. (1998), as “voluntary” as opposed to “compulsory”. Taking into account these perspectives of tax compliance, tax authorities, therefore, require taxpayers to comply willingly without the need for obtrusive methods or legal sanctions to force taxpayers to comply with the tax law. Thus, a definition of tax compliance that emphasises the concept of it being voluntary, is provided by James and Alley (2002); “the degree of compliance with tax law and administration that can be achieved without the actual application of enforcement activity”.

Another broader definition by Song and Yarbrough (1978) describes tax compliance as “taxpayers’ ability and willingness to comply with tax laws determined by ethics, legal, environmental and other situational factors at a particular time and place”. Singh and Bhupalan (2001) add the elements of ‘honesty’, ‘adequate tax knowledge’ which relates to ‘accuracy’ and being ‘timely’ in reporting tax declarations, into their definition of tax compliance.

#### **4.1.3 Tax Compliance in the Context of Indirect Taxation**

The major difference between direct and indirect taxes is the nature of the tax. Direct taxation refers to corporate, business or personal tax. In Malaysia, real property gain tax falls under direct tax. Indirect tax refers to tax on the consumption of goods or services, whether imported or produced domestically. Common taxes under this category are VAT or GST, import duty, excise duty, petroleum duty and GST on import. The common ground of these two groups of taxes is the obligation on the taxpayer to comply with the regulations stipulated in the respective laws. Therefore, there are similarities in the concept and definition of tax compliance between indirect and direct taxes.



The discussion of the definition of tax compliance in direct tax provides an overview of the common requirement under the tax law, which is in line with the narrow definition of the 'tax gap' concept. Similarly, under indirect tax law, specifically in the context of import tax, the taxpayers' obligations are clearly stipulated in the tax law, where taxpayers are responsible for accurately lodging a declaration. It is important to note that there is no standard definition with regards to import tax compliance. The definition of direct taxation can also be applied to import tax, where agents report all information on imported goods in a declaration form and, similarly, pay import tax on behalf of their clients in accordance with applicable import tax laws, regulations and court decisions. Taxpayers who fail to satisfy the requirements of the law can be heavily penalised by a specific provision under the tax law. During the initial interviews with Customs officials, it was perceived that Customs agents, who are the tax collector for the Customs administration, are perceived as tax evaders (see Chapter 3).

It is difficult to judge whether the act of non-compliance is intentional or unintentional, but it is presumed by Customs officials to be intentional because it involves underpaid tax. Non-compliance with tax laws could be referred to as intentional and unintentional non-compliant behaviour that includes tax avoidance and tax evasion. Tax avoidance refers to tax minimisation using legal loopholes in the system (Collins, 1998), while tax evasion refers to illegal tax minimisation (Weigel, Hessing and Elffers, 1987). In other words, tax evasion refers to a deliberate act of non-compliance by paying less tax than one actually owes. Customs agents, in the case of unintentional non-compliance, may feel that they have fully complied with the tax law when they lodge the import declaration, but may end up declaring incorrectly, inadvertently. In other words, they have the willingness to comply, but due to different interpretations, they could end up misclassifying a product category, which may lead to them being non-compliant. In contrast, Customs agents who undertake deliberate non-compliance have the intention to not comply purposely, and act against the tax law by under-declaring goods to evade tax.

Consistent with Bergman (1998) and Andreoni et al. (1998), in this study the broader definition of tax compliance is applied, which emphasises the concept of 'voluntary' or 'willingness' in tax compliance decisions. In addition, the elements of 'ethics' (Song and Yarbrough, 1978); 'honesty', 'legal factors', 'tax knowledge', 'environmental factors' and 'other situational factors' (Singh and Bhupalan, 2001),

which are relevant to the broader definition of tax compliance are also applied in this study. Therefore, the working definition of tax compliance applied in the context of this study is:

*“The willingness to comply with Customs law, honestly report all information in a Customs import declaration, and pay import tax at a particular time and place which are determined by ethics, knowledge, and legal, environmental and other situational factors.*

Tax compliance is a complex subject. Researchers have long studied it in order to understand the underlying reasons for taxpayers’ failure to comply with tax law and to understand the factors that motivate taxpayers to comply. The following sections discuss the development of tax compliance studies, which have been developed more for direct tax than indirect tax. Subsequently, the discussion highlights tax compliance studies focusing on tax preparers and taxpayers, and the gap in this research.

## **4.2 APPROACHES TO TAX COMPLIANCE**

Chapter 3 identifies the problem of compliance with import tax payment as being associated with Customs import declaration. Custom import declaration in indirect tax is similar to direct tax, where taxpayers have to declare their income and expenses in a tax declaration form (manually or electronically). In Customs declaration, goods are valued according to the product category to determine the value of tax for the respective goods. During the initial interviews (see Chapter 3), it was found that tax authorities or Customs view goods as deliberately devalued to evade tax, which is a problem of compliance with the law. This view assumes that taxpayers are tax evaders, without considering the possibility that the act was unintentional, due to lack of knowledge or some other problem that may have led them to be non-compliant.

**Table 4.1: Tax Compliance Approach**

<b>Tax Compliance</b>	<b>First Approach</b>	<b>Second Approach</b>
Concept of:	Tax Gap 100% compliance less than the actual revenue	Voluntary Willingness to act in accordance with the spirit as well the letter of the law
Definition	Narrower	Wider
Tax Compliance	Economic rationality	Behavioural co-operation
Exemplified by:	Trade off: I) Expected benefit of evading II) Risk of detection and application of penalties III) Maximise personal wealth	I) Individuals are not simply independent, selfish utility maximisers. II) They interact according to differing attitudes, beliefs, norms and roles III) Success depend on co-operation
Issues of:	Efficiency in resources allocation	Equity, fairness and incidence
Taxpayer seen as:	Selfish calculator of pecuniary gain and losses	‘Good citizen’
Can be termed the:	Economic approach	Behavioural approach

*Source: James and Alley, (2002, p33)*

A variety of academic disciplines suggest that there are two approaches to understanding the problem of tax compliance: (I) to understand compliance and non-compliance in the context of economic decisions; and (II) to understand the effect of other factors that influence compliance decisions that are related to taxpayers or tax agency behaviour (James and Alley, 2002). Table 4.1 summarises these two contrasting approaches to the problem of compliance. The key distinguisher between the two approaches is the concept of the tax gap, which emphasises enforced compliance versus voluntary compliance, focusing on co-operation between taxpayer and tax authorities. The following section will provide an overview of the two approaches.

#### **4.2.1 Economic Approach: Tax Gap Concept**

The first approach to understanding tax compliance is referred to as the economic approach, where taxpayers are viewed as trying to maximise their wealth by evading tax, which is a narrow concept of economic rationality. James and Alley (2002) suggest that the economic approach is relevant in order to understand the trade-off between the expected benefit of evading tax and the application of penalties. This narrow economic view assumes, implicitly or otherwise, that individuals are immoral and operate in some sort of social vacuum. They will not comply with the tax system unless the benefit of doing so exceeds the costs of not doing so in the form of fines and penalties. Therefore, tax evasion is explained simply in terms of factors such as the levels of tax rates, the probability of being caught evading tax, the penalties that would be imposed and the degree of risk aversion.

An early model based on the concept of the 'tax gap' was published by Allingham and Sandmo (1972), inspired by Becker's (1968) 'crime and punishment' framework. Since that time, this approach has dominated the academic literature in economics and many refinements of its technical aspect have been made. This has led to research on a whole series of different aspects of economic compliance decisions. Section 4.3 will give the details of a few economic models using this approach to understanding tax compliance.

#### **4.2.2 Behavioural Approach: The Voluntary Concept**

The second approach to understanding tax compliance involves wider behavioural issues which draw heavily from the concepts of psychology and sociology research disciplines. According to James and Alley (2002), in this approach, compliance is defined more widely, as trying to avoid tax legitimately or the diligence in performing their obligation. Therefore, the behavioural approach makes understanding the environment in which taxpayers interact, such as the norms and beliefs that influence taxpayers or tax agents, more relevant in compliance decision. James and Alley (2002) further assert that the behavioural approach assumes that taxpayers are 'good citizens' as opposed to tax evaders. It emphasises the principles of voluntary compliance instead of enforced compliance using fines and penalties.

Earlier attempts to use the behavioural approach can be found in the work of

Schmolders (1959) who proposes an economic-psychological model blend, or the concept of “tax mentality” to understand tax evasion. This concept led to the emergence of new models examining other influencing factors of tax compliance, such as social influences, attitudes and demographic characteristics such as age, gender, culture and ethnicity (Jackson and Milliron, 1986). Others propose expanded economic-behavioural models emphasising newer economic determinants that have not been tested, such as compliance costs and tax withholding, blended with psychological elements (Hasseldine and Bebbington, 1991). Researchers continue to use this approach in searching for the ideal tax compliance model, by exploring the psychological and sociological aspects of tax compliance, such as moral values (Bobek and Hatfield, 2003; Feld and Frey, 2006; Torgler, 2003) and social norms or the influence of reference groups on taxpayers’ compliance decisions (Bobek and Hatfield, 2003; Bobek, Roberts and Sweeney, 2007; Wenzel, 2004). There are also studies attempting to explore knowledge and its relationship with tax compliance behaviour in seminal work conducted by Eriksen and Fallan (1996), which has been the guiding principle for other studies that emphasise tax knowledge (Hofmann, Hoelzl and Kirchler, 2008; Palil and Mustapha, 2011; Saad, 2011; Tan and Chin-Fatt, 2000), as well as other socio-psychological determinants in understanding taxpayers’ compliance determinants, to narrow the gap between enforced compliance and voluntary compliance. Section 4.3 gives details of common behavioural models related to this approach to understanding tax compliance.

#### **4.3 COMMONLY APPLIED MODELS IN UNDERSTANDING TAX COMPLIANCE**

Tax compliance has been a topic of study for more than 40 years. Various models and theories have been applied to understanding the determinants of tax compliance behaviour. Tax compliance research has evolved over time and has basically shifted from a purely economic model towards a behavioural approach to tax compliance. Generally, tax compliance studies are based on the following theoretical models: the economic-deterrence model, the economic-psychological model and the behavioural model. The following sections will briefly introduce these models in order to offer an understanding of the various economic and non-economic variables used in the current research model.

#### **4.3.1 Economic-Deterrence Model**

Earlier research on tax compliance is rooted in classical economics, and can be traced back to the work of Adam Smith in 1795 on law and punishment. The work of Adam Smith is the basis for the development of Becker's crime and punishment model (Becker, 1968), Allingham and Sandmo's tax compliance model (Allingham and Sandmo, 1972) and other economic models developed based on this platform, such as the prospect theory, the game theory and the agency theory.

##### **(a) Becker's Financial Self Interest Model**

The economic approach to compliance behaviour was tested by Becker's (1968) seminal work using a crime and punishment framework. In his approach, it was assumed that tax compliance behaviour is determined by monetary gain. Individuals would commit crime if the gain or reward were greater than what would be gained through legitimate activities. Taxpayers would evade tax so long as the consequences of being caught and punished were less than the pay-off of evading. Becker's model was an influential factor in Allingham and Sandmo's (1972) development of a formal model to analyse tax evasion behaviour.

##### **(b) Allingham and Sandmo's Tax Evasion Model**

The deterrence model is the first formal model developed by Allingham and Sandmo, (1972) to understand tax compliance. It is an extension of the financial self-interest model, developed by Becker (1968). The determinant of compliance, according to the model, consists of two elements, tax rate and audit probability. This model shows that the higher the audit probability, the higher the proportional rate of tax compliance level. During the 1970s, research started to extend the model by incorporating other factors, in order to understand compliance decisions, including the work of Cowell (1985) and Weiss (1976).

##### **(c) Other Economic Models**

Economic models are rooted in the deterrence theory, which holds that deterrence effects, such as penalty and audit probability, deter non-compliance. Advancing from the deterrence theory, the prospect theory was introduced with a slightly different view of behaviour, given uncertainty that could be used to predict tax payers' attitudes towards risk. The prospect theory proposes that taxpayers'

decisions could be based on the potential value of losses and gains, based on their risk preference (Jackson and Milliron, 1986). Several other authors have applied prospect theory in tax compliance studies, such as Schepanski and Shearer (1995), Yaniv (1999) and Schmidt (2001). The work of Allingham and Sandmo (1972) continues to occupy a central position in the economic modelling of tax compliance research. Other economic models that have dominated tax compliance research are attribution theory (Schisler and Galbreath, 2000), the game theory model and agency theory (Reinganum and Wilde, 1985).

#### **4.3.2 Economic-Psychological Model**

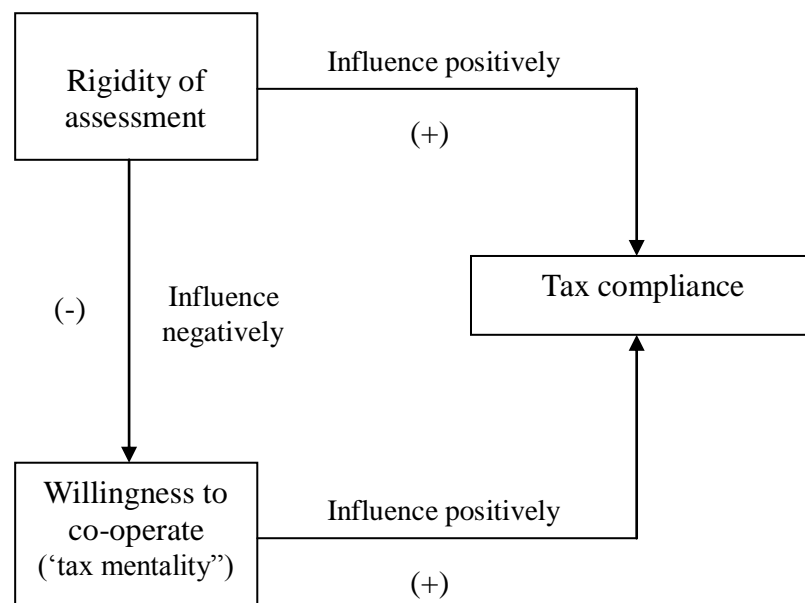
Economic models have been subject to harsh criticism from psychologist and sociologist. It is argued that the economic model assumes that taxpayers' decisions are solely based on maximising financial and economic benefits. There are other factors that may influence taxpayers' decisions, such as psychological and sociological factors. The limitations of such approaches have paved the way for the development of economic-psychological models of tax compliance. In these models, built on the grounds of psychological determinants, taxpayers are no longer seen as selfish utility maximisers, but as human beings motivated to pay taxes on the basis of different beliefs, perceptions and feelings.

##### **(a) Equity Theory**

The equity theory posits that input and output rationalisations determine an individual's decisions (Adams, 1965). Individuals who believe in the input rationalisation in the tax system, such as incentives, may label the tax system as fair if they benefit from the system. In simpler terms, it concerns an individual's judgement of fairness or the equitable distribution of resources. In the context of taxation, individuals are more likely to comply with tax payment if they perceive that they are being treated fairly under the tax system (Wallschutzky, 1984). On the other hand, individuals may resort to their own judgement of what is equitable through non-compliance with tax laws. Therefore, consistent with the equity theory, perceived equity in taxpayers' perception of government's fair/unfair treatment or distribution of resources will influence compliance behaviour.

**(b) Strumpel's Model of Tax Compliance**

Another early tax compliance model based on the economic-psychological model is Strumpel's Model on tax compliance (Hessing, Kinsey, Elffers, and Weigel, 1988). Strumpel's model captures two main elements: *rigidity of assessment* and *willingness to cooperate* by tax authorities is likely to reduce taxpayers' compliance level. *Rigidity of assessment* measures the amount of tax and the level of fines, the assessment process and the level of "red tape" involved in engaging with the tax authority. *Willingness to cooperate* relates to individuals' attitude and perception of the tax system (Kinsey, 1992). These two elements are captured in the Strumpel's Model as depicted in Figure 4.2. The variable of *willingness to cooperate* is positively related to tax compliance. As stated previously, the variable of *rigidity of assessment* however has two contrary effects on tax compliance. The direct positive relation on tax compliance are influenced by tax rate, penalty and other economic variables, whereas the negative relationship is influenced by the level of red tape involved in the tax paying process or other noneconomic variables.



**Figure 4.2: Strumpel's Model of Tax Compliance**

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Source: Hessing et.al., (1988, p526)



### **4.3.3 Behavioural Model**

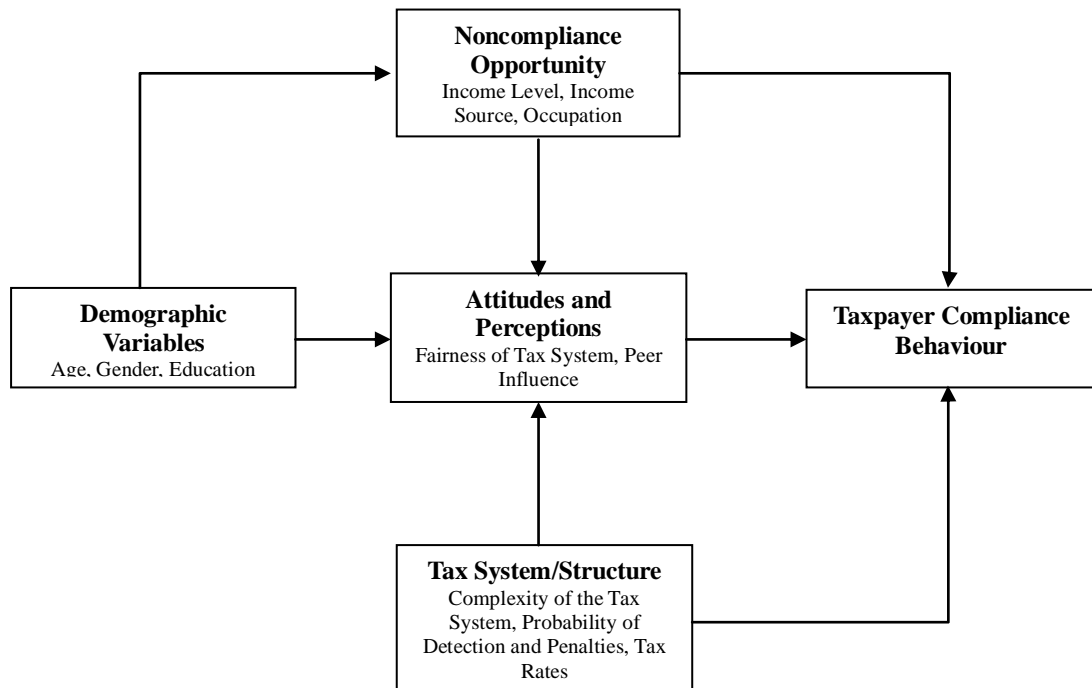
One area that has developed considerably is the behavioural approach to tax compliance. It is argued that understanding compliance goes beyond the deterrence factor and economic determinants as described in the economic model (Feld and Frey, 2006, 2007; Leviner, 2008). In order to enhance the economic model of compliance, researchers need to explore psychology, moral and social influences on compliance behaviour and integrate these factors into their models (Feld and Frey, 2007). As posited by Feld and Frey, (2007), tax compliance is a psychological tax contract that goes beyond the traditional deterrence model and explains tax morale as a complicated interaction between taxpayers and the government.

The behavioural approach has a great deal to offer in terms of supplementing and extending mainstream economic analysis. Therefore, behavioural theory as well as other psychological aspects such as morale, incentives, and emotion, between taxpayers and tax authorities are explored in order to understand compliance behaviour and achieve better compliance (Bobek et al., 2007; Feld and Frey, 2007; Torgler, 2003). Two behavioural theories: the theory of reasoned action (TRA) and the theory of planned behaviour (TPB) are influential in behavioural studies. These theories are very successful in predicting behaviour. Other tax behavioural models, such as Fischer taxpayers' compliance model, which was developed on the basis of behavioural elements, are applied in other tax compliance studies.

#### **(a) Fischer Taxpayers' Compliance Model**

Among the early attempts to link various elements of tax compliance determinants into one tax compliance model is the work of Fischer, Wartick and Mark (1992). The model developed by Fischer is based on Jackson and Milliron's (1986) review of literature on tax compliance, which identifies 14 factors associated with tax compliance determinants. Fischer further categorises these factors into four groups to create an expanded model of tax compliance known as the Fischer model. As reproduced in Figure 4.3, Fischer, (1992) posit that (i) demographics (e.g. age, gender and education), (ii) non-compliance opportunity (e.g. income level, income source and occupation), (iii) attitude and perceptions (e.g. fairness of the tax system and peer influence) and (iv) tax system/structure (complexity of the tax system, probability of detection, penalties and tax rates) influence tax compliance behaviour. The model is a comprehensive model that incorporates economic, sociological and psychological

factors. However, it is argued that this model is too centred on individual taxpayers, therefore having limited applicability to other contexts such as business taxpayers (Chau, 2009).

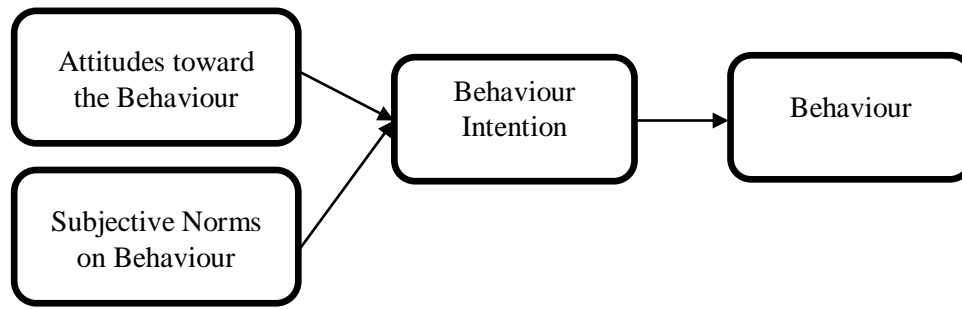


**Figure 4.3: Fischer Taxpayer' Compliance Model**

Source: Chau, (2009, p35)

### (c) Theory of Reasoned Action (TRA)

The theory of reasoned action (TRA) was developed by Ajzen and Fishbein (1980) to explain individuals' behaviour by their behavioural intention. The TRA states that the most determinant factor of a particular behaviour is intention, which is a form of motivation that influences the individual's decision to act upon his/her actual behaviour. A person will do something based on his/her intention (Pavlou and Fygenson, 2006). The stronger the intention of a person to perform a behaviour, the higher the probability of such a behaviour being executed. Apart from the influence of intention on predicting behaviour, Ajzen also identified and understood the determinants of behavioural intention. Thus, it is proposed that behavioural intention is a function of two basic determinants: (i) *attitude* and (ii) *subjective norms*. The features of the TRA are graphically presented in Figure 4.4.



**Figure 4.4: Theory of Reasoned Action (TRA)**

*Source: Ajzen and Fishbein, (1980, p8)*

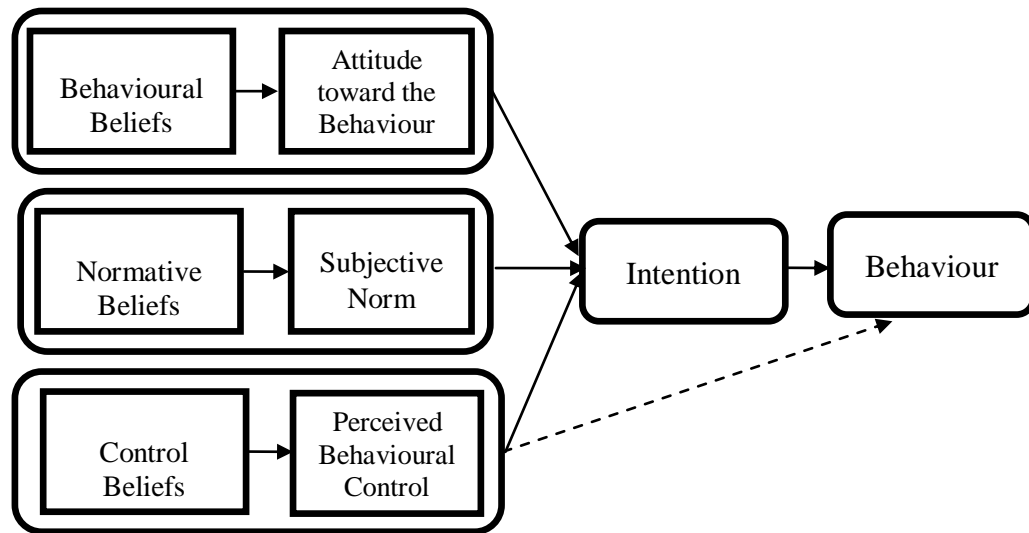
TRA has been successful in predicting behaviour in several studies, as reported in meta-analysis reviews (Langdridge, 2007). Meta-analysis supports the correlation between attitude and subjective norms, which explains between 30% and 50% of the variance in behavioural intention (Armitage and Conner, 2001; Sheeran and Taylor, 1999; Sheppard, Hartwick and Warshaw, 1988). Similarly, studies find that, on average, behavioural intention explains 28% of variance in behaviour, across 422 prospective studies, involving 82,107 participants (Trafimow, Sheeran, Conner and Finlay, 2002).

Despite the ability to predict and explain human behaviour and behavioural intention, TRA had been criticised for being limited to volitional behaviours only. TRA works most successfully when applied to behaviours that are under a person's volitional control. If the behaviours are not under full volitional control, even though a person may be highly motivated by his/her own attitudes and subjective norm, he/she may not actually perform the behaviour due to intervening environmental conditions. In other words, TRA is unsuitable for predicting or explaining behaviours that require skills or resources (Bagozzi, 1992; Liska, 1984; Ogden, 2003). Such criticisms led to the extension of TRA, and the emergence of a new model, the theory of planned behaviour.

#### **(d) Theory of Planned Behaviour (TPB)**

The theory of planned behaviour (TPB), as presented in Figure 4.5, is an extension of TRA, which was developed to understand an individual's behaviour, as predicted by behavioural intention. It overcomes the inadequacy and limitations in TRA. One of the greatest limitations of TRA is that individuals feel that they have

little power or incomplete volitional control over their behaviours and attitudes. Ajzen (1985) explains that, in this situation, the implementation of behaviour does not only depend on behavioural intentions represented by attitude and subjective norms, but is also influenced by other control factors which are represented by a perceived behavioural control (PBC) variable.



**Figure 4.5: Theory of Planned Behaviour (TPB)**

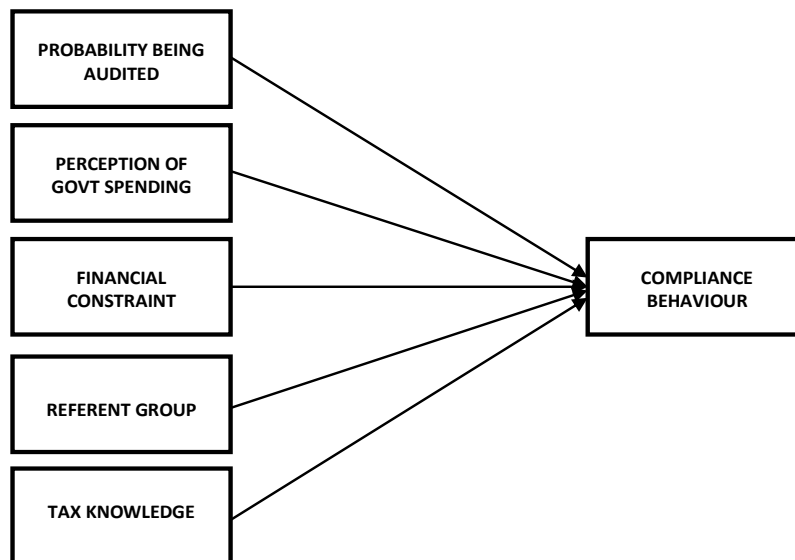
*Source: Ajzen, (2005, p126)*

A review of 76 studies reveals that TPB with the inclusion of perceived behavioural control as an additional variable, has strong predictive power, with behavioural intention explaining 40.9% of the variance in the behaviour (Godin and Kok, 1996). Details of TPB constructs are discussed further in the following chapter. Ajzen's theory of planned behaviour (TPB) has been influential in understanding attitudes and behaviours in various inter-disciplinary studies, such as the compliance of drivers with speed limits (Elliott, Armitage and Baughan, 2003; Poulter, Chapman, Bibby, Clarke and Crundall, 2008; Warner and Aberg, 2006), agriculture-environmental behaviour (Wauters, Biielders, Poesen, Govers and Mathijs, 2010), tourist behaviour (Lee, 2011), IT adoption (Huang and Chuang, 2007; Shih and Fang, 2004; Taylor and Todd, 1995), food consumption (Bruijn and Kremers, 2007), as well as tax compliance studies.

#### 4.3.4 Tax Knowledge Model

Other studies focus on tax knowledge to understand tax compliance. Studies demonstrate that tax knowledge is an important factor that may influence tax compliance decisions. Taxpayers with tax knowledge are more likely to be more compliant than taxpayers with less knowledge (Eriksen and Fallan, 1996; Hofmann et al., 2008; Palil and Mustapha, 2011). A seminal work on tax knowledge is the study conducted by Eriksen and Fallan (1996). The development of studies of tax knowledge results from the introduction of the self-assessment system, which encourages taxpayers towards self-declaration, thus requiring knowledge of tax law in order remain compliant. Although there is no comprehensive compliance model that could be specifically associated with tax knowledge, studies that explore tax knowledge commonly incorporate other tax compliance determinants into the tax compliance model (Loo, McKerchar and Hansford, 2009; Palil, 2010).

Figure 4.6 illustrates an example of a tax knowledge model of tax compliance, which emphasises the role of tax knowledge in tax compliance behaviour. Apart from tax knowledge, other determinants that are equally important are audit probability, perception of government spending, financial constraint and the influence of the referent group on taxpayers' compliance behaviour (Palil, 2010).



**Figure 4.6: Tax Knowledge and Taxpayers' Compliance Model**

*Source: (Palil, 2010, p339)*

#### 4.3.5 Summary of Key Theories/Models and Variables in Tax Compliance Studies

Variables		Punishment Theory	Fin. Self Interest Model	Deterrence Model	Prospect Theory	Equity Theory	Strumped Model	Fischer Model	TRA	TPB	Tax Knowledge
1	Law Enforcement	X									
2	Punishment / Penalty	X	X					X			
3	Detection Probability		X	X				X			X
4	Tax Rate			X				X			
5	Risk Preference				X						
6	Fairness Perception					X		X			X
7	Rigidity of Assessment						X				
8	Tax Mentality						X				
9	Age							X			
10	Gender							X			
11	Education							X			
12	Income							X			
13	Occupation							X			
14	Complexity of Tax System							X			
15	Attitude							X	X	X	
16	Actual Behaviour								X	X	X
17	Subjective Norm / Referent Group							X	X	X	X
18	Behavioural Intention								X	X	
19	Perceived Behaviour Control									X	
20	Financial Constraint										X
21	Tax Knowledge										X

**Figure 4.7: Key Theories / Models and Variables of Tax Compliance**

*Source: (Author)*

This section synthesises the key models/theories applied to understanding tax compliance. As discussed in the earlier section, various approaches have been conducted over the years to examine the variables that affect compliance. As depicted in Figure 4.7 and as discussed earlier in this section, 21 variables can be identified and extracted from the models/theories related to tax compliance.

There are various categorisations applied by authors classifying the variables. For example, Jackson and Milliron (1986) use two categorical terms, economic and non-economic variables, whereas Fischer model, as described in Section 4.3.3 (a), classifies the variables as i) demographic, ii) non-compliance opportunity, iii)

attitudinal, and iv) tax system/structure. Richardson and Sawyer (2001) provide three categorical types according to the magnitude of certainty, namely i) increase in certainty, ii) no increase in certainty, and iii) no change in certainty. Palil (2010) presents the categorisation of variables in 5 categories, i) economic, ii) institutional factors, iii) social factors, iv) individual factors, and v) other factors. For practicality, the grouping of variables in Figure 4.6, uses a combination of various categorisations, presented in Table 4.2 as i) structural factors ii) behavioural factors, iii) social factors and iv) other factors.

**Table 4.2: Variables Categorisation**

<b>Structural Factors</b>	<b>Behavioural Factors</b>	<b>Social Factors</b>	<b>Other Factors</b>
<ul style="list-style-type: none"> <li>• Tax Rate</li> <li>• Law Enforcement</li> <li>• Punishment/Penalty</li> <li>• Detection Probability</li> <li>• Complexity of Tax System</li> <li>• Rigidity of Assessment</li> </ul>	<ul style="list-style-type: none"> <li>• Risk Preference</li> <li>• Tax Mentality</li> <li>• Attitude</li> <li>• Compliance Behaviour</li> <li>• Behavioural Intention</li> <li>• Perceived Behavioural Control (PBC)</li> </ul>	<ul style="list-style-type: none"> <li>• Perception of Fairness</li> <li>• Subjective Norm/Referent Group</li> </ul>	<ul style="list-style-type: none"> <li>• Age</li> <li>• Gender</li> <li>• Education</li> <li>• Income</li> <li>• Occupation</li> <li>• Financial Constraint</li> <li>• Tax Knowledge</li> </ul>

*Source: Adapted from Chau, (1992) and Palil, (2010)*

The list of variables presented in Table 4.2 is exhaustive. As described in Section 4.3.3 (a), besides the seminal work by Jackson and Milliron (1986), which identifies the 14 tax compliance variables used in Fischer Model, Richardson and Sawyer (2001) progress further by reviewing and synthesising over 150 tax compliance studies published between 1986 and 1997. Richardson and Sawyer (2001) identify additional tax compliance variables, namely, compliance costs, tax preparers, framing, positive inducements and amnesties. Unlike the earlier review by Jackson and Milliron (1986) which focuses on studies conducted in the US, Richardson and Sawyer (2001) include other countries in their study, such as the United Kingdom, Australia, New Zealand and other countries in Europe. The focus of these studies is mainly direct tax compliance.

The review and synthesis of various tax compliance models/theories demonstrates that tax compliance is a complex subject. It encompasses various variables applied in economic models to behaviour in order to understand the means of promoting tax compliance. These variables, as discussed above, are commonly analysed in the direct tax literature and are reflected in some of the literature highlighted in the subsequent section on the development of tax compliance studies. This study also looks at the applicability of the relevant variables to direct tax compliance in the context of import tax (indirect tax). This study also explores variables from other inter-disciplinary literature in developing the research model. This is discussed further in Chapter 5.

## **4.4 DEVELOPMENT OF TAX COMPLIANCE STUDIES**

### **4.4.1 Studies on Direct Tax and Indirect Tax Compliance**

For many years, academics have vested interest in tax compliance studies. Many tax compliance models, as discussed in the previous section, have been developed over the years through various empirical studies. The seminal studies on tax compliance can be traced back to the work of Allingham and Sandmo (1972) who examined individual taxpayer behaviour on their income tax report to the tax authority. The role of the tax authority was mainly to detect any probability of under-reporting of income by the taxpayer and penalise the taxpayer for under-reporting or any act of tax evasion. This is an instance of how earlier work on tax compliance viewed the taxpayer narrowly, as maximising their wealth through evasion activities. The key driver of compliance in earlier tax theory was based on deterrence, where the tax authority played a primary role in deterring tax evasion through formal sanctions and enforcement efforts (Allingham and Sandmo, 1972; Tittle, 1977, 1980). Advancing this approach, Reinganum and Wilde (1985) used the principal-agent framework to understand individual income tax evasion. The principal in this framework is the tax collecting agency, while the agent represents the taxpayer. The expectation of the principle in the principal-agent framework is to maximise tax collection by exploiting the ignorance of taxpayer audit rules through audit optimisation. Others consider the tax rate to be an important element in influencing tax evasion. Another study by Clotfelter (1983) investigated the relationship between



tax rate and tax evasion, and indicated a positive and significant effect of tax rate and tax evasion on personal income tax evasion. Clotfelter also realised that the model was too simplistic and suggested other elements that might influence tax evasion alongside tax rate, such as enforcement and tax reporting.

This literature provides an overview of tax compliance studies that focuses on tax evasion. There is a considerable amount of literature devoted to tax compliance within the context of tax evasion. The basic contribution of these papers is to provide econometric evidence suggesting that tax evasion is influenced by various factors such as formal sanctions (Bergman, 1998; Feld and Frey, 2006; Tittle, 1980), audit probability or enforcement efforts (Davis, Hecht and Perkins, 2003; Kaplow, 1996), tax rates (Clotfelter, 1983; Slemrod and Yitzhaki, 2002) and behavioural factors such as psychological and social conditions (Hasseldine and Bebbington, 1991; Weigel et al., 1987).

There is also considerable effort focused on behavioural problems in understanding tax compliance, an issue highlighted by Weigel et al. (1987). As behaviour is a complex issue and requires in-depth understanding, various approaches have been tested to understand the behavioural elements that influence tax compliance decisions (Cummings, Martinez-Vazquez, McKee and Torgler, 2009). Adopting this approach, Eriksen and Fallan, (1996) examine the role of tax knowledge and attitudes on tax compliance decisions, using the a quasi-experimental method, with tax law students as the control group with some knowledge of tax law, and students pursuing bachelors in administration as the experimental group. The results show that better tax knowledge and attitude improves the perception of the fairness of the tax system. Casey and Scholz (1991) use a similar approach, using students as a proxy for actual taxpayers. One hundred and nine (109) university students participated in five studies, which examined their tax compliance behaviour decisions using cognitive heuristics or experience-based techniques. The study shows that their behavioural decision to comply with tax law is determined by the non-compliance risk, such as the probability of being detected by tax authorities, which affects taxpayers' preferences. They used a similar approach on 71 university students who participated in a decision making task relating to income tax, in which the probability of being caught for evading tax would influence the tax compliance decision (Casey and Scholz, 1991). Several studies apply an experimental approach using students as the experimental subjects, such as the study by Robben, Webley, Elffers and Hessing (1990), which demonstrated that

the opportunity to evade leads to higher tax evasion. In his study, Devos (2005) used university students in Australia to test the effect of demographic variables on tax evasion. Iyer, Reckers and Sanders (2010) conducted a field experiment, with the cooperation of the Washington State Department of Revenue, to examine the influence of detection and sanctions on tax compliance. In their experiment, firms were selected as the subject of study rather than individual taxpayers.

Many experimental studies have been conducted using students as the experimental subjects, but there are a few exceptions, for instance Iyer Reckers and Sanders (2010) as mentioned, and Grasmick and Scott, (1982) who used actual taxpayers in cooperation with the Internal Revenue Service, in their field experiments. Others used different approaches, such as the large scale survey method, to understand tax compliance. One early attempt that used the survey method was the work of Wallschutzky (1984). In his study, he used an actual sample of taxpayers who had been convicted of tax evasion, and whose names appeared in the Australian Commissioner of Taxation Report from 1980 to 1981. Karlinsky, Burton and Blanthorne (2004) conducted a large scale survey in California to measure the perceptions of US citizens of the seriousness of tax evasion relative to other crimes and violations. Moving on to more recent studies, the study conducted by Cummings, Martinez-Vazquez, McKee and Torgler (2009) applied experimental and survey methods to understanding the effect of tax morale and tax compliance in South Africa. Loo, McKerchar and Hansford (2010) took different perspectives by combining the survey method and qualitative interviews in their studies on tax compliance and the self-assessment system. Other examples of tax compliance studies which used actual taxpayers are studies conducted by Barr and Dokko (2006), Adams and Webley (2001), Jabbar and Pope (2008c), Palil (2010) and Saad (2010), as summarised in Table 4.3.

**Table 4.3: Examples of Tax Compliance Studies Using Actual Taxpayers**

Author	Research Focus	Method	Findings
Saad (2010)	Tax fairness and compliance decision in self-assessment system	Survey of 2,279 salaried taxpayers	Tax compliance in self-assessment system is represented by several factors, namely knowledge, tax fairness attributes, institutional and behavioural factors.
Palil (2010)	Tax knowledge and tax compliance in self-assessment system	Survey of 1,073 salaried taxpayers	The factors affecting taxpayers' compliance are audit probability, government policies, financial constraints and referent groups.
Jabbar and Pope (2008)	Tax compliance costs of SMEs	Survey of 175 SME Businesses	Tax compliance costs are regressive on small businesses.
Barr and Dokko (2006)	Tax filing experiences and withholding preferences of low-and moderate-income (LMI) households	Computer assisted survey of 1,003 LMI household taxpayers	Tax system needs to integrate LMI group. Findings also suggest that many of the LMI taxpayers used tax preparers, reflecting the complexity of tax filing system.
Adams and Webley (2001)	Small business owners' attitudes to VAT compliance in the UK	Interviews with 3 groups of 27 small business owners.	Similarities with income tax compliance include factors such as equity and sanctions. Mental accounting is the new variable identified as the compliance determinant of VAT.

Source: Author

Despite extensive research in the area of tax compliance, surprisingly the focus has been on direct taxation, especially personal income tax compliance. Business tax compliance in general and in particular consumption tax (such as import tax) have received very little attention (Murray, 1995), with the exception of some studies on consumption tax such as those of Adams and Webley (2001), Berhan and Jenkins (2005), Bergman and Nevarez (2006) and Webley and Ashby (2010). A comprehensive list of tax compliance studies summarised by James, Edwards and Alison (2010) in “*An annotated bibliography of tax compliance and tax compliance costs*”, indicated that out of 819 published tax compliance studies, only 3% or 26 studies were related to indirect tax. Among the 26 tax compliance studies, 19 were related to VAT or GST, while only 3 were related to import tax, those by Widdowson (1998), Geis, Cartwright and Houston (2003) and Shekidele (1990). Other tax compliance studies were related to local tax (Wicks and Killworth, 1967), land tax (Abdul, Hodges and Hasseldine, 2005) and sales tax (Alm, Blackwell and Mckee,

2005; Edelman, 1949 cited in Evans, 2003).

This is surprising given the economic and social importance of business taxation and the fact that consumption tax represents an important tax revenue for the government (Webley, Adams and Elffers, 2002). Generally, the few studies of indirect tax compliance are dominated by VAT or GST studies, which consist of two main areas: 1) VAT compliance costs; and 2) VAT compliance. Most focus on the economic effect of tax compliance or VAT compliance costs, while very few focus on the broader aspects of tax compliance such as understanding the effect of enforcement on VAT compliance (Bergman and Nevarez, 2006) and VAT compliance behaviour (Adams and Webley, 2001; Webley et al., 2002).

Within the field of VAT studies, indirect tax compliance is influenced by factors similar to the determinants of direct tax compliance (Webley et al., 2002). For instance, studies of direct tax compliance demonstrate that deterrent measures such as enforcement regime, generally, might enhance compliance (Davis et al., 2003; Hasseldine, Hite, James and Toumi, 2007; Kirchler, Hoelzl and Wahl, 2008) but, as asserted by Marcelo Bergman and Nevarez (2006), in a VAT compliance or indirect tax context, enforcement might not foster individual compliance in societies where cheating is the norm. A study by Adams and Webley (2001) of VAT compliance in the United Kingdom, which applies a qualitative approach, uncovers 15 key concepts that might influence compliance. The key concepts in their study were translated into five major themes: (1) equity, (2) views on authoritative body, (3) sanctions, (4) morality, which is similar to personal income tax compliance, and (5) mental accounting, an established concept in psychology but new to tax compliance, which emerged from the qualitative data. Interestingly, they also found that the respondents (VAT registrants) viewed themselves as having 'ownership' of the VAT collected instead of being a tax collector on behalf of the Customs and revenue department. This is similar to the concept of Customs agents in this study, where the agent is the tax collector for the Malaysian Customs. It may be, in this instance, that some of the Customs agents are viewed as having 'ownership' of the monies paid by their clients for the purpose of import tax payment to Customs. This view was expressed in an interview session with a senior Customs official. The agents are viewed as having the intention to deliberately evade tax through the payment collected from their customers.

In summary, direct tax compliance, particularly of individual taxpayers, has been the central focus of previous tax compliance studies. Among the limited literature on indirect tax, VAT or GST has been the focus of previous studies. These studies validate the applicability of the few direct tax compliance variables tested in an indirect tax context, such as enforcement, sanctions and morality. Further studies on the indirect tax context would further validate the variables applied in direct tax studies, and provide new insight, as demonstrated by Webley et al. (2002). Considerable room remains for future studies based on the dearth of research in this context, to understand the influences of indirect tax compliance such as import tax. The previous studies on import tax are discussed in the following section.

#### **4.4.2 Studies of Import Tax (Indirect Tax)**

The discussion in the previous section of this chapter shows that the majority of studies are conducted on direct tax, with little attention on indirect tax. Among the few indirect tax studies, VAT compliance generally dominates, and among these import tax is relatively under-explored. Three basic themes emerge, directly or indirectly, from import tax related studies:

- 1) Economic impact and modelling, which focuses on import duty evasion and its impact on the trade gap (Javorcik and Narciso, 2008), excise tax evasion through rigorous smuggling of tobacco products (Galbraith and Kaiserman, 1997; Geis et al., 2003; Stehr, 2005; Yurekli and Sayginsoy, 2010) and compliance costs of excise duty (Shekidele, 1990).
- 2) Administrative impact on Customs administration of Customs compliance (Widdowson, 1998).
- 3) Social impact, which focuses on the implications of tobacco tax (excise duty) on health and smoking habits (Chaloupka and Wechsler, 1997; Wasserman, Manning, Newhouse, and Winkler, 1991). These two studies reflect indirectly on import excise duty, as excise duty on imported tobacco products in the United States is levied in the respective states instead of during importation.

Javorcik and Narciso (2008), Galbraith and Kaiserman (1997) and Stehr (2005) apply a narrow approach to understanding tax compliance, which uses the

concept of the 'tax gap'. Using the World Bank's integrated trade solution database to examine Germany and 10 Eastern European countries using time series data from 1992 to 2003, Javorcik and Narciso (2008) demonstrated that tax evasion, defined by the trade gap between import and export, is determined by the level of tariff (or tax rate) and misrepresented import prices by under-reporting quantities or product misclassification. Galbraith and Kaiserman (1997) used a similar approach which utilised the narrow economic approach to understanding cigarette consumption of smuggled cigarettes and taxed cigarettes using Canadian time series data between 1980 and 1994. Geis et al. (2003) focused on excise duty evasion with respect to the black market of tobacco in Australia. Another study by Stehr (2005) focused on tax avoidance, using a similar approach, and indicating that tax avoidance accounted for up to 9.6% of sales between 1985 and 2001 due to higher cigarette tax leading to smuggling activities. He suggests that an effective policy to curb smuggling and tax avoidance is through alternative policies such as counter-advertising and smoking restrictions. Shekidele (1990) took a different perspective to understanding the cost to transact on excise duty, commonly known as compliance costs. He used a similar approach to direct tax compliance cost studies to measure the compliance cost of excise duty using the standard costing model.

A study by Widdowson (1998) provides a different view on Customs compliance by focusing on the institutional role of the Customs administration in adopting a systematic approach, such as using information technology. Investment in automated accounting systems is proposed to make compliance easier for highly compliant companies. Although the suggestion seems relevant, other smaller business, such as SMEs, that are equally important in the trade transaction, were not considered. Smaller businesses do not have the capacity to invest in sophisticated accounting systems, which have relatively high start-up costs (Tran-Nam, 2000).

Studies relating to import tax clearly show that the common approach to measuring tax compliance is focused on tax evasion, which is associated with the gap in tax revenue. To the best of our knowledge, there is no study on import tax which uses the broader concept of tax compliance, as defined in Section 4.1.3, which this study attempts to investigate.

#### 4.4.3 Studies of Customs Agents (Tax Preparer)

The central focus of many past studies was on individual taxpayers, either actual taxpayers or students as a proxy for taxpayers. The annotated bibliography of tax compliance studies indicates that tax preparers represent the subjects of only 27 or 3.3% of 819 published studies (James et al., 2010).

Tax preparers<sup>21</sup> play an important role in assisting taxpayers meet their compliance obligations. Increased usage of tax preparers by individual income taxpayers and business taxpayers over the past decade suggests that more and more taxpayers are seeking their advice to ensure that they are reporting accurately and complying with tax legislation. Tax preparers prepared 63 million, or 53% of US individual income tax returns in 1996, and the figure increased to 80 million, or 62%, by the year 2005 (Bloomquist, Albert and Edgerton, 2007).

Referring to Section 2.2.4, in the context of import tax, Customs agents<sup>22</sup> in Malaysia handled 90% cargo clearance, as compared to 58% in the United States. This relatively high figure could be due to a lack of knowledge and the complex trade procedures at the border involving various stakeholders such as the Customs, port management, shipping carriers and other government agencies (Grainger, 2008, 2007; Hansen and Annovazzi-Jakab, 2008), making outsourcing seem relevant to avoid unnecessary hassle and mistakes that would incur high compliance costs to the business community, such as the importers. Unlike the role of tax preparers, which do not act as agents for the government (Jackson and Milliron, 1989), Customs agents play a dual role as tax collectors and tax preparers, who act as agents for the government to collect tax on behalf of their client and remit it to the Customs administration, as well as preparing clients' import declarations. Therefore, Customs agents as tax preparers may potentially have a large influence on business taxpayers' compliance attitudes and behaviour.

Despite the relevance of tax preparers and their importance in influencing taxpayers' compliance, very little empirical evidence shows the magnitude of tax preparers' influence on taxpayers' compliance. Generally, studies on tax preparers can be classified into four areas of focus; (1) understanding factors that reflect taxpayers'

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<sup>21</sup> Tax preparers in direct taxation refers to tax accountants, tax agents, tax practitioners, lawyers, Certified Public Accountants (CPA) and non-CPAs.

<sup>22</sup> Customs agents assume the role of tax preparers. They represent their clients and lodge Customs import declarations according to customs legislation, including making tax payments on behalf of their client to the Customs administration.

engagement of tax preparers (for example, Blumenthal and Christian, 2004; Christian, Gupta and Lin, 1993; Sakurai and Braithwaite, 2003; Stephenson, 2010; Tan, 1999); (2) tax preparers' aggressiveness in tax compliance decisions (for example: Ashton, 2000; Hite and McGill, 1992; Murphy, 2004; Roberts, 1998; Schisler, 1995); (3) compliance in reporting tax returns (for example: Bloomquist, Albert and Edgerton, 2007; Hite and Hasseldine, 2003; Tomasic and Pentony, 1991); and (4) the use of tax preparers and tax compliance (for example: Klepper, Mazur and Nagin, 1991; Niemiowski and Wearing, 2003; Oats and Tuck, 2009). A large number of studies focus on the first three areas, whereas few examine the effect of tax preparers on tax compliance.

In an earlier study on tax preparers, Klepper et al. (1991) develop an econometric model to empirically test the influencing factor of the tax preparer upon the taxpayer's compliance behaviour. The findings reveal that the tax preparer might have an influence by discouraging tax non-compliance on legally unambiguous income sources, but encouraging tax non-compliance on ambiguous income sources. Furthermore, the model predicts that imposing penalties on the tax preparer might result in a positive compliance effect, but it might also increase the price of preparers, who need to recover the additional costs resulting from the penalties.

Another study by Erard (1993), which applied a similar econometric model, reveals that the use of tax preparers, particularly CPAs and tax lawyers, is associated with increased levels of non-compliance in tax returns. The level of non-compliance might increase if there was a high opportunity to evade. While, the study also stresses that tax preparers have the expertise either to assist their clients to reduce the barriers, to improve tax compliance, or exploit the opportunities for tax non-compliance.

The role of the tax auditor in enforcing the tax law is important to counter tax non-compliance, which may increase the level of compliance among tax preparers (Kaplan, Reckers, West and Boyd, 1988; Madeo, Schepanski and Uecker, 1987). However, there are conflicting results, which demonstrate that the probability of being detected by tax auditors for tax non-compliance is insignificant. An experimental study conducted by Duncan, LaRue and Reckers (1989) indicates that the audit probability or tax enforcement by the Inland Revenue Services (IRS) was the only factor that was found to be insignificant. The factors reported as significant in a tax preparer's decision to comply are knowledge, year-end payment status of client, risk preference and recent experience with audit clients. Similarly, another study about tax



preparers' attempts to discharge unethical behaviour towards tax law, indicates that the probability of audit or tax enforcement did not show a strong relationship with tax compliance (Marshall, Smith and Armstrong, 2006).

One particular study that uses a method other than a confrontational approach was conducted by Tomasic and Pentony (1991), who interviewed 141 tax preparers in Australia to examine the impact of tax practitioners on taxpayers' compliance. The study revealed that the role of tax practitioner is an advisor to their client, an unpaid employee of the tax office, an intermediary between the tax office and taxpayers, a protector of their practices and an influence on the tax system. The study also concludes that tax practitioners play an important role in increasing the level of taxpayers' compliance. They argue that tax practitioners' moral obligations or ethics may increase tax compliance more than confrontational approaches such as enforcement efforts.

A more recent study was undertaken by Niemirowski and Wearing (2003) of 62 tax agents in Australia using survey questionnaire approach. The approach was broadly defined and questions related to behaviour and values; beliefs and attitudes; competency; fairness; tax knowledge; and satisfaction and lifestyle. The study identified several factors related to tax compliance including taxpayers' experience with the tax office client service, perception of tax difficulty and the necessity of using a tax preparer for the purpose of tax returns. Niemirowski and Wearing (2003) confirm that there are similarities between taxpayers' and tax preparers' compliance behaviour, with only a few minimal differences related to their level of knowledge and the transfer of risk to the tax agent to minimise non-compliance. It can be concluded from this study that taxpaying behaviour is related to beliefs, attitudes and values, tax office client services, a sense of financial competence, difficulty in meeting tax obligations, perceptions about the necessity of using tax agents, tax knowledge and the competency of tax agents in the preparation of tax returns.

In summary, similar to the study of direct tax payers, there are considerable efforts in the studies on tax preparers to understand what motivates compliance. Although studies on tax preparers represent a small contribution to the tax compliance literature, the results of the previous studies provide an initial insight into understanding tax compliance. Generally there are similarities between tax preparer and taxpayers' compliance determinants. Variables such as tax preparers' attitude, moral obligation, tax knowledge and fairness are the common variables that influence

tax compliance. In addition, tax preparers' compliance is influenced by the level of difficulty of meeting tax obligations and tax office client services. To the best of my knowledge, there is no study of indirect tax that attempts to look at the relationship between indirect tax preparers, such as Customs agents, and tax compliance. Thus, this study provides an insight into the understanding of Customs agents as indirect tax preparers and taxpayers' compliance, as well as the similarities and differences in compliance determinants of Customs agents, who assume the role of tax preparers and tax collectors.

## **4.5 RESEARCH GAP**

The previous sections provide a review of the key literature on tax compliance, models applied in understanding tax compliance and the key findings from both direct and indirect tax compliance studies. The following paragraphs summarise the gaps that this research intends to fill in order to achieve a better understanding of tax compliance and contribute to the literature.

### **4.5.1 Research Context in Previous Studies**

Earlier sections of this chapter discuss rigorous previous studies on direct taxation. Although tax compliance studies have been established for more than forty years, very few can be linked to indirect tax compliance. For instance, as discussed extensively in Section 4.4.1, only 3% of 819 published tax compliance studies are related to indirect tax. This is surprising, as indirect tax, as extensively discussed in Chapter 2, is one of the most important revenue contributions for many governments, including the Malaysian government. This indicates a relatively large gap to be filled in the research context of indirect tax compliance (Adams and Webley, 2001; Webley and Ashby, 2010; Webley, 2004). An understanding of import tax compliance as an indirect tax regime could provide Customs administration with suitable strategies to enhance compliance.

Previous studies on tax compliance have largely been conducted in Western countries such as the United States, Australia, the United Kingdom, and New Zealand. There is a handful of literature on tax compliance behaviour in the Asia-Pacific region. Therefore, this study responds to a call to expand the number of cross-cultural

studies (Richardson and Sawyer, 2001) and to increase the understanding of tax compliance in developing countries (Andreoni et al., 1989; Chau, 2009). In view of the inadequate institutional framework and insufficient expertise and resources to monitor the complexity in the issue of tax compliance, developing countries such as Malaysia, as discussed in Chapter 2 Section 2.3, are vulnerable to tax non-compliance behaviour. As asserted by Davis et al. (2003), compliance can vary across time, geographic regions and cultures. Therefore, the experience of Malaysia adds to the existing literature on indirect tax compliance in understanding compliance behaviour in developing countries.

#### **4.5.3 Research Participants in Previous Tax Compliance Studies**

The trend in past tax compliance studies has been to find an effective approach to improve tax compliance. However, the attention has typically been focused on personal taxpayers, rather than tax preparers or Customs agents, in this context, as the research subjects. Literature suggests that tax preparers play a significant role in increasing taxpayers' compliance (Tomasic and Pentony, 1991). The initial interview findings in Chapter 3 also suggest that Customs agents, who assume the role of tax preparers, play an important role in compliance decisions. However, despite the importance of Customs agents and the surge in the demand for tax preparers in recent years, the role of tax preparers in tax compliance studies is still in its infancy (Hai and See, 2011a, 2011b; Torgler, 2003).

Customs agents, as discussed in Chapter 2 paragraph 2.2.4, are regarded as intermediaries by business taxpayers. From a broader perspective, this study attempts to respond to the call for greater attention on business tax taxpayers' compliance (Chau, 2009; Torgler, 2011; Webley and Ashby, 2010) as the behaviour of businesses or firms is distinct from that of individuals (Iyer et al., 2010). An understanding of business taxpayers' compliance determinants could provide Customs administrations and other tax authorities with suitable approaches to enhance the level of compliance. Therefore, this study attempts to address this research gap by examining the relationship between Customs agents, who play the role of tax preparers and intermediaries for business taxpayers, and the factors that influence tax compliance.

#### **4.5.4 Research Approach in Previous Tax Compliance Studies**

As discussed in Section 4.3 of this chapter, there has been considerable effort to understanding tax compliance, through various approaches, since the seminal work by Allingham and Sandmo (1972), using the econometric modelling approach based on deterrence and punishment. Nevertheless, evidence demonstrates that economic modelling fails to consider the behavioural aspects of tax compliance, which suggests a number of changes in order to make a more relevant analysis of current tax compliance issues. In particular, economic models must incorporate the various control devices used by tax administrations (Baldry, 1994).

The few previous studies, as discussed in Section 4.4.1 of this chapter, on import tax only focus on the application of the economic modelling approach. The factors considered are limited to economic variables such as level of tariff, under-reporting of prices and quantities, as well as product mis-classification. Hence, there is room to be filled in this context, particularly by the psychological research approach that can contribute to a new understanding of indirect tax compliance determinants (Adams and Webley, 2001; Webley and Ashby, 2010). As asserted by Cummings et al. (2009), tax compliance is a complex behavioural issue, hence the application of a psychological research approach, such as behavioural theory, in this study is relevant in narrowing the research gap. Furthermore, an economic deterrence approach can be integrated with the social and psychological approach to produce a conclusive approach to fully understanding compliance behaviour (Devos, 2007). The suitability of, and the reasons for, the behavioural theory selected for this study are justified in the following chapter.

#### **4.5.5 Research Design in Previous Tax Compliance Studies**

Past tax compliance studies, as discussed in the earlier sections, demonstrate that experimental and administered mail survey approaches have been the dominant approaches for understanding factors influencing tax compliance behaviour. However, as suggested by previous studies, more empirical evidence of the new understanding of tax compliance behaviour determinants should be found through other approaches, such as the qualitative interpretive approach (Torgler, 2003) or the integration of qualitative and quantitative approaches as a mixed method approach (for example,

McKerchar, 2003, 2008) to validate the findings or provide more explanations of the phenomenon under study (McKerchar, 2003).

Although, it has been some time since the issue was first highlighted, very little empirical evidence has been found using the qualitative interpretive approach to tax compliance determinants. A few studies have applied qualitative elements as a confirmatory approach (for example, Loo et al., 2010), for validation of findings rather than the exploratory approach (for example, Adams and Webley, 2001) in qualitative study. For instance, the study by Adams and Webley (2001) uses the exploratory approach through the interview method to uncover a new understanding of factors influencing tax compliance by small businesses. Therefore, this study attempts to respond to this call by adopting qualitative elements in order to discover new insight into what influences tax compliance behaviour, and integrating the finding sequentially in a mixed qualitative (interview) and quantitative (survey) approach. This is discussed in Chapter 7 and Chapter 8 respectively.

#### **4.6 WHAT'S NEXT?**

Tax compliance studies are well established in the area of direct taxation. However, little empirical evidence can be linked to indirect tax such as import tax and the role of Customs agents or similar tax preparers (in a direct tax context). A review of empirical literature provides an avenue for this study to fill several gaps in the literature. Tax compliance in this study is defined using an holistic definition, which emphasises the concepts of 'voluntary' and 'willingness to comply', compared to the narrow definition, which assumes taxpayers to be tax evaders.

Tax compliance is demonstrated by past studies to be a complex behavioural issue which extends beyond economic rationalisation. Therefore the behavioural approach is explored in this study, in order to understand the various factors that may influence Customs agents' compliance behaviour. This will be discussed further in the following chapter along with TPB, as the base theory to examine various compliance determinants.

# **CHAPTER 5**

## **THEORETICAL CONTEXT AND RESEARCH PARADIGM**

This chapter resembles the previous one in two respects: first, in presenting and discussing the theory of planned behaviour as the selected behavioural theory for this study, based on the gap identified in Chapter 4; and second, in emphasising the relevant tax compliance determinants representing various categorical factors, i.e. structural factors, behavioural factors, social factors and other factors. These factors are based on the five components of TPB (attitude, subjective norm, perceived behavioural control, behavioural intention and behaviour). This chapter also elaborates on other tax compliance determinants (law, law enforcement, tax knowledge, ethics, complexity of procedure and tax assessment service quality) which are relevant to the research model of this study. Finally, the philosophical assumptions and the selected research approach are discussed.

### **5.1 THEORETICAL ORIENTATION**

This study utilises the theory of planned behaviour (TPB) as the base framework through which to understand the compliance determinants of Customs agents. The applicability and the reasons for selecting TPB theory in the context of this study are justified in the following section.

#### **5.1.1 Rationale for Applying the Theory of Planned Behaviour**

TPB was selected as the base theory for several reasons. Firstly, as discussed in the previous section, TPB is a well received social psychological model, applied in various disciplines, including behavioural-related studies to understand and predict behaviour (Armitage and Conner, 2001). Nevertheless, only a handful studies on tax compliance have applied the psychological model of TPB, such as Bobek (1997), Bobek, Hatfield et al. (2007) and Trivedi et al. (2005), with limited factors included in the model for understanding tax compliance behaviour. As a general model that can be

applied in many fields and has been tested in the area of tax compliance, the wider perspectives of tax compliance (with the inclusion of behavioural and non-behavioural elements) and the applicability of TPB were tested in the context of this study.

The theory of planned behaviour (TPB) was also selected as the base theory due to its ability to predict the behaviour action that fits the main objective of this study, to understand factors that influence tax compliance, which is predictive in nature. TPB is recognised as having good predictive power in explaining human intentions and behaviour (Ajzen, 1991; Armitage and Conner, 2001; Godin and Kok, 1996). Since tax compliance is a complex behaviour, economic models have been found to have limitations in predicting actual compliance behaviour.

The application of TPB is well-known in understanding individual behaviour. Nevertheless, past studies also support the application of TPB to understanding the behaviour of an organisation. For instance, studies by Montalvo (2006) which used TPB, selected managers and CEOs to understand organisational behaviour in innovation. Managers and CEOs were selected as the respondents as they are the key decision makers in the company. Furthermore, their decisions and actions determine the company's direction and objectives. Similarly, other studies have selected decision makers in the company such as managers in environmental studies (Collins, Uhlenbruck, and Rodriguez, 2008) or managers and company executives (Cordano and Frieze, 2000). Organisational theorists demonstrate the importance of studying top managers to predict how the characteristics and beliefs of individuals affect the actions and decisions of an organisation. Therefore, the selection of TPB to explain the compliance behaviour of Customs agents as an organisation is relevant in this study, as the focus of this study is on the organisation, represented by the individual key decision makers.

TPB also offers a better solution for understanding the determinants of tax compliance. The elements embedded in the model such as attitudinal and sociological dimensions support previous tax compliance studies (Bobek and Hatfield, 2003; Bobek, Roberts et al., 2007; Trivedi, Shehata and Mestelman, 2005). Moreover, in previous tax compliance studies which apply TPB, limited factors have been tested such as incentive (Trivedi et al., 2005), and moral value (Bobek and Hatfield, 2003). This justifies the need to expand the model to understand other factors that influence tax compliance behaviour.

While, the main elements of TPB are generally accepted, TPB is open fit, meaning it can accept any additional variables in order to improve the research model and its explanatory quality (Ajzen, 1991; Sommer, 2011). Prior studies demonstrate that the addition of other constructs enhances the prediction of intention and behaviour (Ajzen, Brown and Carvajal, 2004; Bobek and Hatfield, 2003; Shih and Fang, 2004; Trivedi et al., 2005), which is another reason for using TPB in the current study, given that other compliance variables identified in prior research can be added successfully into the research model.

Therefore, the use of TPB as a framework, with the inclusion of additional tax compliance determinants, in the context of this study is justified.

## **5.2 TAX COMPLIANCE DETERMINANTS IN THE CONTEXT OF THE THEORY OF PLANNED BEHAVIOUR**

The following section discuss studies of tax compliance that correlate with the five TPB elements; (1) attitude; (2) subjective norm; (3) perceived behavioural control (PBC); (4) behavioural intention; and (5) behaviour. The purpose is to determine their relevance to this inquiry, and the elements that should be included in this context.

### **5.2.1 Attitude Towards Tax Compliance (Personal Norm)**

Attitude refers to elements such as feelings, beliefs and other emotional elements that influence individuals' decision in performing a behaviour (Ajzen and Fishbein, 1980; Ajzen, 2005). It consists of cognitive, affective and behavioural elements bound together, and is inseparable as an object of attitude (in excerpts of Aronson and Pratkanis, 1993).

Ajzen (1991) defines the attitude toward a behaviour as an assessment of whether performing the behaviour would be good (favourable) or bad (unfavourable) to an object or matter. The object or matter could come in various forms such as people, situations, places, ideas, institutions, events or behaviours (Oskamp, 1992). The factors that determine the behaviour, as asserted by Ajzen (1991), include behavioural trust (behavioural belief) and emotional belief. Behavioural belief relates to the evaluation of the result or consequence of the behaviour, while emotional belief is related to the feelings of pleasure or guilt. Positive individual attitudes towards



behaviour will encourage the behaviour, whereas negative attitudes will lead to negative behavioural intention, thus discouraging individuals from performing the behaviour (Fazio, Powell and Williams, 1989).

In the context of tax compliance studies, attitude towards tax compliance refers to the individual's assessment, whether or not they will comply with tax obligations based on emotional belief and the results of the behaviour (behavioural belief). Attitude, as an important tax compliance determinant, is evident in several tax compliance studies. Hanno and Violette (1996) demonstrate a positive relationship between attitude and compliance behaviour. According to the study, taxpayers' compliance behaviour depends on individuals' internal factors such as moral factors that have formed over the course of time. In agreement with this statement, Bobek, (1997) suggests that attitude towards the fairness of tax system influences positive or negative behaviour towards compliance with tax law. If the attitude is motivated by a belief in the fairness of the tax system and the benefits received from the system, individuals will judge the system as fair for them, or vice versa. Similarly, Cullis and Lewis (1997) demonstrate that attitude is an important element in taxpayers' decision making process - whether to comply or not to comply. This view is supported by Kirchler, Hoelzl and Wahl (2008), who suggest that a taxpayer with a favourable attitude towards tax evasion is less likely to be compliant, whereas a taxpayer with an unfavourable attitude would be more compliant.

Bobek and Hatfield (2003) apply TPB as the framework for investigating the applicability of the theory in tax compliance studies. They use an experimental approach with three scenarios involving the temptation to cheat; a home office scenario (dealing with disallowed deduction of expenses), a tip scenario (dealing with tips not reported as taxpayer income), and a charitable contribution scenario (dealing with deductions of charitable contributions without receipts), in order to understand non-compliance behaviour. The results reveal that attitude has a significant impact on compliance decisions in all three scenarios. On average, respondents did not consider that engaging in cheating, or tax minimising behaviour, was illegal or morally wrong. Another similar tax compliance study involving a cross cultural study in three countries, Australia, Singapore and the United States, demonstrates that attitude or personal norm is significant, and the most important factor influencing tax compliance behaviour (Bobek, Roberts et al., 2007). The significant role of attitude in tax compliance is also evident in the study by Trivedi et al. (2005), which investigates the

relationship between attitude and tax compliance (compliance and non-compliance behaviours) and suggests that attitude is paramount in both compliance and non-compliance situations. The impact of attitude on compliance behaviour in an indirect tax compliance study also shows significant results (Bidin, Faridahwati, Salleh and Othman, 2011). Their study, which also uses TPB as the framework, focuses on sales tax<sup>23</sup> in Malaysia.

Among the other studies of direct tax compliance in Malaysia, few have attempted to understand the relationship between attitude and tax compliance. It has been revealed that attitude remains consistently significant in tax compliance (Kasipillai and Jabbar, 2006). The study by Kasipillai and Jabbar (2006) uses two models to determine non-compliant attitudes and understating or under-declaring income. However, the study is limited in terms of using hypothetical scenarios as actual behaviours, which might elicit different responses. A more recent study which uses a mixed method survey instrument, case study and experiment, indicates that taxpayers with favourable attitudes could be more compliant than taxpayers with unfavourable attitudes (Loo et al., 2009).

In summary, based on the above discussion, generally it has been demonstrated that attitude plays an important role in shaping taxpayers' compliance determinants, which supports the theoretical context of attitude within the context of TPB as asserted by Azjen (1991).

### **5.2.2 Subjective Norm**

Subjective norm is defined as the influence of third parties on others and commonly refers to close referent groups such as family, friends, colleagues and business acquaintances (Ajzen, 1991). The referent group plays a significant role in determining and influencing people's intention to perform specific behaviour (Ajzen and Fishbein, 1980; Ajzen, 2005). Subjective norm, as the sociological element in TBP, is also known as, and used interchangeably with, social norm or peer influence in tax literature, and other literature such as economic literature, consumer sociology and accounting literature (Blanthorne and Kaplan, 2008; Bobek and Hatfield, 2003; Bobek, Roberts et al., 2007; Elster, 1989; Nyborg, 2003). Consistent with the

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<sup>23</sup> Sales tax is also known as value added tax (VAT) or good and services tax (GST) in some other countries.

conceptualisation of the construct, according to the respective authors, subjective norm, social norm and peer influence can be used interchangeably. According to Ajzen (1991), referent groups play a significant role in determining and influencing people's intentions to perform specific behaviour.

Previous studies in various areas support the role of subjective norms in behavioural intention and tax compliance behaviour. Direct tax literature has demonstrated that subjective norms have a positive and significant impact in influencing behavioural intention. Among studies that examine the effect of subjective norms and tax compliance behaviour, the work of Bobek can be considered the most influential. Study by Bobek and Hatfield (2003) shows that subjective norms have significant impact on tax compliance behaviour intentions in three non-compliance scenarios, using the experimental method. In support of these findings, another study by Bobek, Roberts et al. (2007), indicates a positive relationships between subjective norm and compliance behaviour. The study reveals that subjective norm is the most influential factor that motivates compliance behaviour, in Australia, Singapore and the Unites States. This study, which examines the effect of subjective norms on the behavioural intention of the taxpayer for tax refunds or overpaid tax, also indicates a significant relationships between referent group and tax compliance decision (Bobek, Hatfield et al., 2007).

Similarly, in other tax compliance studies, Hanno and Violette (1996) and Trivedi et al. (2005) report that subjective norms positively and significantly influence behavioural intention of tax compliance. In summary, previous literature supports the role of subjective norms in behavioural intention and tax compliance behaviour, consistent with the theoretical context of TPB.

### **5.2.3 Perceived Behavioural Control (PBC)**

Perceived behavioural control (PBC) is defined as the perceived ability to execute a target behaviour (Ajzen, 2005). PBC is another key variable in TPB to form the extended version of Ajzen's theory of reasoned action (TRA), which is a predictor of behavioural intention (Ajzen, 1991; Fisbein and Ajzen, 1975). TPB assumes that PBC predicts behavioural action through behavioural intention, or directly predicts behavioural action as theorised in TPB. PBC indicates that a person's motivation is influenced by the perception of the difficulty of the behaviour, as well as how

successfully an individual can perform the activity. If a person holds strong control beliefs about the existence of factors that will influence behaviour, then the individual has high perceived control over behaviour (Ajzen, 1991). Conversely, the person has a low perception of control if he/she holds strong control beliefs that impede the behaviour. This perception can reflect past experience, anticipation of future circumstances or come from the attitudes resulting from the cultural norms surrounding the individual (McKenzie and Jurs, 1993).

In the area of tax compliance, PBC not only refers to factors that encourage or hinder compliance with tax obligations in general, but also whether an individual believes he or she is able to control the performance of a specific behaviour (Bobek and Hatfield, 2003). The two aspects of performing a particular behaviour are encouragement (or the hindrance factor) and the control factor, also referred to as self-efficacy and controllability (Ajzen, 2002; Francis, Eccles and Johnston, 2004; Kraft, Rise, Sutton and Roysamb, 2005). The terms 'self-efficacy' and 'controllability' are also known as 'perceived difficulty', which refers to the extent the behaviour is perceived to be easy or difficult for an individual to perform, and 'perceived control', which refers to the extent to which the behaviour is perceived to be under an individual's voluntary control (Sparks, 1997; Trafimow et al., 2002). The controllability or 'perceived control' aspect of PBC relates to factors such as constraints, opportunity, resources and finance which determine the desired behaviour (Carrington, Neville and Whitwell, 2010; Chang, 1998; Sideridis, Kaissidis and Padeliadu, 1998). According to Ajzen (1991), a person who has the skill, resources and opportunity (or fewer obstacles) to perform a behavioural action perceives a higher degree of PBC, whereas, a lower degree of PBC relates to less opportunity or greater obstacles, and fewer resources and skills to perform the behaviour.

In tax compliance studies, PBC is not widely applied, either as an independent construct or as a full TPB model. This is justified as there are only a handful of tax compliance studies that attempt to explore the theory in understanding tax compliance behaviour. Among the few studies that examine the relationships between PBC and tax compliance behaviour, the results of the study by Bobek and Hatfield (2003) show a significant relationship in two scenarios (home office and tip scenarios) and a marginal relationship in the charitable organisation scenario, in relation to tax non-compliance decision. The study takes into account the role of moral obligation that interacts with PBC in tax non-compliance decision. The study also considers the two

control factors of income visibility or opportunity as important factors for non-compliance, and probability of detection or perceived probability of detection as an impediment to non-compliance. Similarly, in a tax compliance study conducted in the context of the self-assessment system, taxpayers' PBC was found to be significant in the behavioural intention to comply with the self-assessment system (Saad, 2010). In this study, two aspects of PBC are applied, control factor (knowledge, skill and resources) and perceived ease or difficulty in understating income as an encouragement or obstacle to the taxpayer.

However, these results are contradicted by another tax compliance study conducted by Trivedi et al. (2005), which demonstrates that there is no significant relationship between PBC and tax compliance behaviour in one hypothetical scenario and a very marginal relationship in another hypothetical scenario. The study uses two components to measure PBC, penalties and third-party reporting (such as the use of tax agents). There is a possibility that the different results may be related to the different approaches to measuring PBC components. The study does not consider 'self-efficacy' or perceived ease or difficulty as part of PBC. The study also uses different elements of the control factor, the actual penalty component such as jail term and fines, as opposed to individuals' perceptions of the probability of detection or penalty. It is argued that individual perception of probability of detection or penalty is more closely related to the decision than the actual audit or penalty rates (Bobek and Hatfield, 2003). Critics argue that there is a need to have clearer guidelines in terms of self-efficacy and control factors in PBC to identify the preferred measure of these two variables and ensure consistency in the evaluation of PBC in behavioural intention and behaviour (Armitage and Conner, 2001). However, as contended by Ajzen (2002), both self-efficacy and control factor are associated with the same concept of PBC.

In summary, PBC is the third predictor element of behavioural intention as theorised in TPB. Although there are contradictory findings, the findings of Bobek and Hatfield (2003) and Saad (2010) are consistent with Ajzen's (1991) assertion about the concept and operationalisation of PBC in the theory of planned behaviour.

#### 5.2.4 Behavioural Intention

Ajzen and Fishbein (1980) define intention as a description of the cognitive readiness to perform a behaviour. Intention is the willingness or the effort that individuals exert to perform a specific behaviour (Ajzen, 1991). Therefore, the stronger the intention to engage in a behaviour, the more successful the performance of the actual behaviour in achieving the desired objective. Ajzen further asserts that intention is the most influential factor in the prediction of behaviour and it is an intermediary (mediator) for attitude, subjective norm and PBC. Baron and Kenny, (1986, p1173) define a mediator as, “*the generative mechanism through which the focal independent variable is able to influence the dependent variable of interest (and) mediation is best done in the case of a strong relation between the predictor and criterion variable.*”

A mediator, according to Sekaran and Bougie (2011), is a variable that appears between the time the independent variables operate to influence the dependent variable and the time their impact is felt on it, which means that the influence of attitudes, subjective norms and PBC on behaviour depend on the intentions of a person to perform a behaviour.

Literature shows that intention is an immediate antecedent and a mediator of attitudes and social influences on behaviour (Ajzen, 2005). A number of studies such as (Bagozzi, 1992) and Schifter and Ajzen (1985), support the existence of a positive relationship between intention and behaviour. Meta-analyses conducted by Armitage and Conner (2001), Notani,(1998) and Sheppard, Hartwick and Warshaw (1988) support the predictive validity of behavioural intention. A report by Sheppard, Hartwick and Warshaw (1988) analysing 87 studies shows intention as a good predictor of behaviour. Similarly, a meta-analysis by Armitage and Conner (2001), which considers the effect of intention, indicates the predictability of actual behaviour on intention. The analysis demonstrates that intention and PBC have most explanatory power within the TPB framework.

Studies specifically on behaviour also support the influence of intention on behaviour, including condom use (Godin and Kok, 1996), compliance with speed limits (Elliott et al., 2003), blood donation (Giles and Cairns, 1995), engagement in leisure activities (Ajzen and Driver, 1992), information technology use (Taylor and Todd, 1995), fruit consumption (Bruijn and Kremers, 2007), consumption of soy

products (Rah et al., 2004), and electronic goods purchase (Pavlou and Fygenon, 2006).

In the context of tax compliance, among the few studies that apply TPB as the framework, a very small number of studies attempt to apply the full TPB model, which includes the effect of behavioural intention on behavioural action. Trivedi et al. (2005) and Saad (2010) provide strong support for the connection between intention to comply and actual compliance behaviour. Other studies, such as Bobek and Hatfield (2003) and Hatfield et al. (2007) do not apply the full TPB model and exclude behaviour as a variable in their study. There is a weakness in this approach as the study is unable to validate the prediction of behavioural intention on behavioural action. The application of the full TPB model should be tested in indirect tax contexts, in view of the limited studies that have looked into the role of intention as a mediator of behavioural factors. Thus, this study expects intention to be the most appropriate measure for determining agents' compliance behaviour. Intention also acts as a mediator between attitudes, subjective norms and perceived behaviour control, and import tax compliance behaviour.

### **5.2.5 Tax Compliance Behaviour**

TPB posits that behaviour is strongly influenced by behavioural intention (Ajzen, 1991). The stronger the intention to engage in a particular behaviour, the more likely an individual is to perform the actual behaviour. Intention, together with PBC, form a predictor variable for behavioural action in the TPB model.

Past studies that utilise TPB as the framework demonstrate that there are other factors that influence behaviour directly, other than the two variables of PBC and behavioural intention, as theorised in TPB. Among the few studies that utilise the full TPB model as their framework, Trivedi et al. (2005) attempt to investigate the role of ethics and its direct relationship with compliance behaviour. Ethics as a variable added to the TPB model is found to be significant. Bobek and Hatfield (2003) use moral obligation as an interaction variable to determine non-compliance behaviour. Out of the three scenarios investigated, the results indicate a strong relationship for two scenarios and a marginal relationship for another scenario. Overall, the results indicate an improvement in the predictive power of TPB model when obligation or ethics is used as an additional interaction variable with actual behaviour.

Another recent study, by Saad (2010), which applies a full TPB model, however, does not consider additional variables that interact directly with behaviour. All the studies discussed apply an experimental or hypothetical situational approach, as opposed to self-reporting compliance behaviour. Although there are advantages to this approach in reflecting actual decisions versus past experiences, what the taxpayer did or did not do in the past, which may affect the validity of the data, the use of the situational approach is argued to be biased, in terms of forcing the respondent to make a choice, which might not reflect their actual behaviour, and the respondent may not respond honestly to the question posed (Bobek and Hatfield, 2003). It is contended that past behaviour is the best predictor of future behaviour (Beck and Ajzen, 1991; Burnkrant and Page, 1988; Labaw, 1980; Tittle, 1980) based on the assumption that past behaviour relates to habit, which is a pattern of behaviour that develops reflecting future behaviour (Aarts, Verplanken and Knippenberg, 1998; Tittle, 1980). It is also argued that past behaviour provides the means to predict future behaviour, which is within the individual's 'level of consciousness', relating to their own experience rather than responding to what they might do in the future or things that have not directly affected them (Labaw, 1980). Citing an example of blood donation, Labaw's (1980) approach suggests that a person who has donated blood is more aware of their feelings about blood donation than someone who has no experience of donating blood. Therefore, their willingness to donate blood can be predicted more accurately than someone who has no direct or indirect blood donation experience. Other studies such as the prediction of fruit consumption (Bruijn and Kremers, 2007) and prediction of travel mode choices (Aarts et al., 1998) provide empirical evidence which supports past behaviour as a predictor of future behaviour.

In summary, literature supports the role of intention and other determinants in predicting tax compliance behaviour. Although there are strengths and limitations to using the experimental and self-reporting behavioural approaches, self-reported behaviour is consistent with Ajzen's (1991) contention as theorised in the theory of planned behaviour.



### **5.3 OTHER RELEVANT TAX COMPLIANCE DETERMINANTS**

As discussed in Chapter 4, some the key tax compliance determinants related to direct tax preparers' environment are formal sanctions, ethics, tax knowledge and general fairness. Other under-explored tax compliance determinants which are equally important in this context of study are complexity of procedure, tax assessment service quality and exchange of fairness. Numerous studies have provided evidence that additional components in the theory of planned behaviour might increase the predictive power of behavioural intention on behaviour (Ajzen, 1991; Armitage and Conner, 2001). The following sections, therefore, discuss these compliance determinants which may be considered additional components of the research model<sup>24</sup> for a better understanding of import tax compliance behaviour.

#### **5.3.1 Law and Law Enforcement (Formal Sanctions)**

One of the factors that may affect the intention to comply is the perception of law enforcement undertaken by the Royal Malaysian Customs. The law is an instrument to control and draw the power of an institution. Law should be administered and enforced by governing institutions such as Customs administrations in the context of indirect taxation. Provisions in the Customs Act 1967 indicate that penalties and fines will be imposed for those who fail to pay, or avoid paying, taxes. Failure to pay the penalties and duties as stated in Section 123 could lead to imprisonment (Malaysian Customs Act, 1967). Punishment meted out to offenders is seen as a lesson for the public on the effects and consequences of committing the offense. It is considered the regulatory strategy to reduce tax evasion and a control measure to ensure that the public to comply with the law (Devos, 2007; Langham, Paulsen and Hartel, 2012). The effect of enforcement on compliance indicates that increased enforcement efforts increase compliance levels (Davis et al., 2003; Hanno and Violette, 1996).

Tax administration has, for many years, relied on legal penalties (civil and criminal penalties) as the primary tool to enforce tax compliance. Among the methods applied in managing tax compliance are imposing financial penalties and imprisonment (Allingham and Sandmo, 1972; Rotunno and Vezina, 2011; Slemrod, 2007; Torgler, 2011). Several studies of taxation support there being a relationship

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<sup>24</sup> Refer to Chapter 7, Section 7.4

between the perception of law and enforcement and tax compliance. As discussed in the previous Chapter<sup>25</sup>, among the early researchers to explore the variables of law enforcement is Allingham and Sandmo, (1972), who use the economic crime approach to explain and predict tax behaviour. According to them, if the fine imposed on a tax evader is high, it will increase tax compliance. This statement was supported by Murphy (2005) and Virmani (1989), who indicate that penalty rates and action imposed through financial penalties on those who evade tax may be the best way to prevent evasion from recurring in the future. This statement is consistent with preventive theory (deterrence theory), which states that individuals will try to avoid doing a wrongful action if a valid sentence in the law (legal punishment) is heavy and swiftly executed (Sutinen and Kuperan, 1999). Similarly, a study of the Islamic tax system, or 'zakah', demonstrates that the legal instrument of law and enforcement has a strong relationship to taxpayers' decisions on zakah compliance (Bidin, 2008). The study, which involved 250 respondents using cluster sampling, reveals that positive perception of law positively influences their intention pay zakah. Interestingly, the study also finds that law enforcement has a strong but negative relationship with zakah compliance. In the Islamic tax system, zakah is a voluntary tax contribution. Therefore enforcement efforts may not work in increasing compliance, as the public may not feel comfortable if religious matters were to be enforced. This indicates that the concept of enforcement differs between conventional tax systems such direct and indirect tax system and the Islamic tax system.

Meanwhile, another study conducted by Trivedi et al. (2005) finds that increasing the audit rate has a great influence on compliance behaviour. This is supported by Feld and Frey (2007) who find that the probability of an individual being detected through audit and the fine imposed are closely related to compliance behaviour. Citing the example of study of a group of 473 taxpayers in Australia, the findings reveal that the majority of respondents were likely to claim a fictitious tax deduction if they were informed by their tax agents that there was a lower probability of being audited by the tax authority (Devos, 2012). In contrast, there are also studies indicating that the penalty rate has a negative association with evasion (Marrelli and Martina, 1988; Marrelli, 1984). Another study reveals that the effect of audit detection and punishment imposed on those who avoid paying taxes is debatable, as individual

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<sup>25</sup> Refer to Chapter 4, Section 4.3.1(b)

social factors also influence individuals' compliance behaviour (Wenzel, 2007). While most studies support the correlation between the effect of law and enforcement with compliance, some studies indicate that there are negative effects of other influencing factors that determine taxpayer's compliance behaviour.

### **5.3.2 Tax Knowledge**

Tax knowledge is an essential element in understanding tax law and it can influence taxpayer's compliance (Eriksen and Fallan, 1996). Earlier tax compliance studies established a strong relationship between tax knowledge and taxpayers' compliance (Eriksen and Fallan, 1996; Fallan, 1999). In the self-assessment system or tax declaration, tax knowledge is found to be the most influential tax compliance determinant (Loo, McKerchar et al., 2010; Loo et al., 2009; Palil and Mustapha, 2011). It has been established that greater tax knowledge in an individual leads to higher compliance behaviour (Fallan, 1999; Hungerford and Volk, 1990; Kasipillai and Jabbar, 2006; Kirchler, Niemirowski and Wearing, 2006) and greater compliance with legal requirements such as accuracy, timeliness and truthfulness in tax declaration (Loo, Evans and McKerchar, 2010; Palil and Mustapha, 2011). Conversely, lesser tax knowledge in an individual may lead to tax non-compliance. This is evident in a tax compliance study on small businesses where the absence of tax knowledge may result in unintentional tax non-compliance (Ahmed and Braithwaite, 2005; McKerchar, 1995).

The significant influence of knowledge on compliance behaviour is not only reported in the tax field, but also in other research areas such as entrepreneurship (Wood and Pearson, 2009), insurance (Lin and Chen, 2006) and online banking (Karjaluto et al., 2002). A study of entrepreneurship demonstrates that knowledge has a substantial impact on the decision to engage in entrepreneurship (Wood and Pearson, 2009). The study found that individuals are likely to invest in businesses when the knowledge related to the business is high and, conversely, when the knowledge related to the business is low, it is less likely that the individual will invest and engage in the business. Lin and Chen (2006) report a positive influence of knowledge on behaviour related to the decision to purchase an insurance policy. Similarly, individuals who possess knowledge of information technology are more

likely to use online banking compared to people who have less information technology knowledge (Karjaluoto and Mattila, 2002).

However, some studies do not support the contention that knowledge positively influences behaviour. This is evident in the study of individual's compliance with the federal income tax system, which claims that tax knowledge has no significant relationship with taxpayers' compliance behaviour (Harris, 1989). Similarly, contrary to prior research, the results of the study by Tan and Chin (2000) indicate that an increase in tax knowledge does not have a significant impact on perceptions of fairness or tax compliance attitudes. The study examines the links between an increase in tax knowledge and perceptions of fairness and tax compliance attitudes using students enrolled in an introductory taxation course in a New Zealand tertiary institution. The contradiction in the findings could be due to inconsistent results in different geographical areas. Furthermore, it is also possible that different measurements are applied in the studies, producing different results.

Despite the different results in some studies, the test of knowledge in the field of indirect taxes is further explored to understand the magnitude of its impact on compliance behaviour.

### **5.3.3 Ethics (Informal Sanctions)**

Ethics is defined as normative rules for guidance in social environments and relationships between individuals in a society (Recker et al., 1994). This social behaviour pattern is evaluated by others and accepted as a norm in society (Alm, McClelland and Schulze, 1999). For instance, in tax compliance, an individual complies as long as he/she believes that compliance is the accepted norm, whereas non-compliance is considered a crime (Alm and Torgler, 2011).

Past studies show the role of ethics to be an important determinant of tax compliance (Alm and Torgler, 2011; Blanthorne, 2013; Bobek, 1997; Jackson and Milliron, 1986; Wenzel, 2007) more than financial self-interest (Roth et al., 1989). It is argued that the decision to comply with tax obligation goes beyond the notion of the self-rationalisation of selfish, rational and self-interested actors, as portrayed in the standard neoclassical paradigm (Alm and Torgler, 2011). Conventional tax compliance models of taxpayer behaviour largely overlook the ethical aspect of tax compliance (Eisenhauer, 2008), but researchers have begun to see and emphasise

individual internal factors (such as moral factors) in their studies, because these factors could affect the results of compliance (Hanno and Violette, 1996).

Empirical evidence suggests that ethics have a significant impact on improving tax compliance because taxpayers feel that tax evasion is immoral behaviour (Jackson and Milliron, 1986). Bobek (1997) shows that consistent moral obligation influences taxpayer compliance behaviour. He finds that a stronger moral obligation for not cheating results in a stronger effect on individuals' intention to comply. Holding one's ethical behaviour consistently affects individual compliance. The higher the values are held, the higher the intention to perform a behaviour in accordance with the set rules and regulations (Bobek, 1997). Wenzel (2007) found that taxpayers who define themselves as having high ethical beliefs (tax favourable ethics) feel reprehensible if they are involved in evading tax or are apprehended by the authorities, thus making them more compliant. This statement is supported by Bidin et al. (2011), in a study of business tax compliance among 440 companies with sales tax licenses, which demonstrates that ethics has a strong influence on the behavioural intention to comply with local sales tax.

There is also empirical evidence suggesting that ethical belief might have a significant role in tax payers' compliance attitudes. Individuals with high ethical belief may have a positive compliance attitude because they assume that compliance with tax law is a moral obligation (Ho and Wong, 2008). Similarly, a study conducted in three European multicultural countries indicates a strong relationship between moral obligations or tax ethics and the attitude of compliance with tax law (Torgler and Schneider, 2007). The findings support the findings of another study, which indicate that the level of tax compliance is higher when there is a stronger belief that tax evasion is unethical (Reckers, Sanders and Roark, 1994), showing that ethical belief is the best means of improving tax compliance (Bobek and Hatfield, 2003).

#### **5.3.4 Complexity of Procedure (Procedural Complexity)**

Defining 'complexity' appears to be more complex than is initially apparent, compared to defining 'compliance', which simply means "conforming to a specification or policy, standard or law that may or may not be clearly set out" (Silveira et al., 2012). There is no absolute definition of what complexity in procedure means. In general, the term complexity is defined as "the quality or state of not being

simple; the quality or state of being complex; or a part of something that is complicated or hard to understand” (Merriam-Webster.com, 2012a). Procedure is “a series of actions that are done in a certain way or order; or an established or accepted way of doing something” (Merriam-Webster.com, 2012b). Typically, authors categorise the factors that contribute to complexity rather than provide a standard definition. For instance, in tax compliance literature, the term ‘complexity’ within the scope of taxpayers’ compliance, in a narrow definition, refers to an excessive burden of recordkeeping, tax form completion or other compliance activity placed on the taxpayer (McKerchar, 2007).

Reflecting on the term ‘Customs procedure’, as explained in Chapter 2.2, it involves a complex process or series of actions, which include tariff classification, valuation and origin rules, Customs facilitations as well as other steps applied in the process of clearance of goods. Therefore, in the context of Customs procedure, the term complexity of procedure can be defined as any type of complexity that involves excessive burden or numerous processes or steps in the clearance of goods, which includes documentation requirements, inspection, methods of determining goods classification, methods of assigning value as the basis of an *ad valorem* tariff, and origin rules.

Complexity in the tax compliance domain can be expounded in various forms of complexity such as complexity in tax computation (Hanefah, 1996; McKerchar, 2001), law complexity (Kirchler et al., 2006; Krause, 2000), readability (Hanefah, 1996; Saad et al., 2014), and procedural complexity of tax administration (Cox and Eger, 2006). In an indirect tax environment, in the context of import and export, the term complexity can be linked to the notion of trade complexity (Altomonte and Bekes, 2009) and cross border operations complexity (Grainger, 2007).

Literature suggests that complexity in the tax system, or tax complexity, is one of the determinants of tax compliance (Chan et al., 2000; Chau, 2009; Fischer, Wartick, and Mark, 1992; Forest and Sheffrin, 2002; McKerchar, 2007; Richardson, 2006; Saad, 2010). It has been established that a more complex tax system leads to non-compliance behaviour among taxpayers. For instance, a study by Richardson, (2006) based on data from 45 countries, indicates that non-economic determinants have the highest correlation with tax evasion. The results also show that complexity is the most important determinant of tax evasion. The findings indicate that the lower the level of complexity, the lower the level of tax evasion, across countries.

In a more recent study by Saad (2010) of the self-assessment system (SAS) in Malaysia, 852 samples of actual individual taxpayers were selected for the study. The results of the study are that a less complex tax system influences the perception of fairness, which may induce the intention to comply with tax law. However, according to a study by Forest and Sheffrin (2002), simplifying the tax system may not be an effective tool to deter tax evasion, because taxpayers do not consider tax simplification as a barrier to evading tax. The empirical findings of their study using econometric analysis of 1784 taxpayers' data, indicate that there is no consistent correlation between complexity and non compliance.

Complexity of the tax system is reflected in Fischer taxpayers' compliance model<sup>26</sup> as one of the determinants under the constructs of the tax system/structure that influence compliance behaviour (Chau, 2009). A related study that examines the tax system structures of the U.S. and Hong Kong suggests that there is evidence of a relationship between the tax system and tax compliance (Chan et al., 2000). However the tax system/structure is measured by examining factors such as tax rates, self-assessment and tax withholding. Specific factors that determine the complexity of the tax system as depicted in the original construct of the tax system/structure in Fischer's tax compliance model are not explored or tested in their study.

Other studies examine tax complexity in terms of procedure of tax administration, for example Cox and Eger (2006). Their study of the State Road Fund in the U.S. state of Kentucky, reveals that procedural complexity of tax administration in the vehicle fuel tax system contributes to increasing non-compliance. They argue that layers of procedure in an organisation add to the complexity of the tax system, thus making compliance more difficult. This is consistent with studies in other domains, such as Grainger's (2007), conducted on cross border operations in UK ports. The findings reveal that the complexity of cross-border trade adds to the compliance burden of the business community (Grainger, 2007). The author asserts that the complexity of the UK cross border environment includes more than 60 trade procedures required by various regulatory authorities to move cargo in or out of a port of entry. Explicitly, complexity in Customs procedures and other trade procedures constitutes a barrier to trade, therefore reform in Customs and trade procedures is essential for trade facilitation (Bolhofer, 2007; Grainger, 2011).

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<sup>26</sup> Refer to Section 4.3.3(a)

Although, there is limited literature specifically linked to the effect of complexity in procedure on tax compliance, in the larger context of tax complexity there is evidence from previous studies that supports the relationship between complexity and compliance. In summary, previous studies indicate that there is contrasting evidence from the literature that either supports or rejects the correlation between complexity and compliance. However, most cases, either in tax compliance literature or other inter-disciplinary literature, support the relationship between complexity and compliance. The construct of complexity in the context of custom procedures is further explored and tested in the research model development in Chapter 7.

### **5.3.5 Tax Assessment Service Quality**

The quality of services provided by an organisation plays an important role in ensuring customer satisfaction and loyalty, and influences behaviour (Zeithaml, Bitner and Gremler, 2006). From a broader perspective, the quality of services could also impact companies' performance and global competitiveness (Gwardzinska, 2012). Lewin and Johnston (2008) stress that quality of service is an important evaluation of the services provided and customer satisfaction level, because it influences repeat purchasing behaviour. Service quality, in this regard, can be defined as the perception or evaluation of the comparison between consumer expectations and the outcome of service performance (Zeithaml, Parasuraman and Malhotra, 2002), and the evaluation of the process involved in the service delivery (Parasuraman, Zeithaml and Berry, 1985). Disconfirmation theory posits that users are satisfied with the experience of a service if the service provided meets or exceeds their expectations (Bitner, 1990).

Alongside this theory, there are quite a number of studies, especially in marketing, that focus on service quality and its relationship with behaviour (for example, Chen and Kao, 2010; Cronin and Taylor, 1992; Liu, Furrer and Sudharshan, 2001; Yap and Sweeney, 2007; Zeithaml, Bitner and Gremler, 2006; Zeithaml, Berry and Parasuraman, 1996). Zeithaml et al. (1996) offer a conceptual model to examine the impact of service quality on behaviour, whether to remain with or defect from a company. Their results, from a multi-company survey on retail chains, automobile insurers, computer manufacturers and life insurance services, reveal that perception of service quality has a strong influence on customers' behavioural intention,



specifically on loyalty to a company and willingness to pay more. Similarly, a study by Cronin and Taylor (1992) of consumers in a south eastern city of the United States, on four industries, banking, pest control, dry cleaning and fast food, reports that the perception of service quality and satisfaction are positively correlated with repurchase behaviour. A more recent survey conducted by Chen and Kao (2010) on online travel, consisting of 240 respondents in Taiwan, also reveals that service quality and satisfaction influence online purchase behaviour. Similar findings on service quality and behaviour are also found in other studies, for example cultural diversity perception on service quality (Liu et al., 2001), service quality and consumer switching behaviour (Yap and Sweeney, 2007), and consumer satisfaction and brand loyalty (Nam, Ekinici and Whyatt, 2011).

Although the concept of service quality is most widely applied in the private sector, it is acknowledged that service quality is also an important issue in the public sector (Alessandro, 2005; McAdam, Reid and Saulters, 2002; Ramseook, Lukea and Naidoo, 2010). With the increasing need for public sector reform, aimed at enhancing service delivery, quality in the public sector is becoming more critical (Brosamle, 2012; Chittoo, Ramphul and Nowbutsing, 2009). Similarly, in Malaysia, various contemporary management practices and philosophies have been implemented in line with the notion of new public management (NPM), such as the public sector major reform under the government transformation programme (GTP) (PEMANDU, 2010). In this respect, quality service delivery has become one of the key performance indicators (KPIs) in the performance measurement system (Nabiha and Khalid, 2008).

Similar to any other public sector organisation, quality of service is important in Customs administration in relation to its role in tax collection. Furthermore, the ways in which tax authorities interact with taxpayers' impact on the public perception of the tax administration. Thus, an effective tax administration should consider the relationship with taxpayers in order to increase taxpayers' satisfaction (OECD, 2001). This leads to improved voluntary compliance of taxpayers who are satisfied with the services provided by the tax administration (Kelly and Hopkins, 2010), and ultimately increases the efficiency of tax collection (James, Svetalekth and Wright, 2009). Evidence in an indirect tax study in Malaysia by Mansor (2010), shows taxpayers' satisfaction is at a moderate level. The study, which uses the international benchmark system in measuring performance, suggests that improvements could occur in regards to quality of interactions between indirect tax administration staff and taxpayers to

improve taxpayers' satisfaction levels. This reiterates the concept of taxpayers as the customers of the tax administration. For instance, UK HM Revenue and Customs is increasing efforts in their client relationship management with large corporate taxpayers (LCT), which aims to bring businesses and revenue closer together (Oats, Tuck and Knight, 2008). This suggests that service quality is an important aspect to consider in developing a compliance framework for Customs administration, which is responsible as the indirect tax collecting agency for the government.

### **5.3.6 Exchange of Fairness**

Exchange of fairness, commonly known as fairness exchange, refers to the benefits received from the government in exchange for the tax paid (Azmi and Perumal, 2008). It is a concept derived from equity theory which describes how individuals will react upon their perception of equity. As elaborated on in Chapter 4, on equity theory, individuals behave differently, depending on their rationalisation of their contribution to, and reward from, a relationship. In the tax context, if taxpayers do not agree that they are obtaining fair exchange in tax spending policies, it influences them to report less income than taxpayers who perceive equity in their exchange with the government (Kim, 2002).

Andreoni, Erard and Feinstein (1998) recognise fairness as the most relevant psychological factor in their review of tax compliance. However, the concept of fairness is complex and past studies have conceptualised fairness in various ways (Kirchler, Niemiowski and Wearing, 2006), for instance progressive versus flat tax rate (Gerbing, 1988). This is also referred to as horizontal and vertical fairness (Kirchler, 2007). Horizontal fairness, according to Kirchler (2007), relates to equal tax treatment regardless of individuals' economic circumstances, whereas vertical fairness refers to different tax rates applied to different taxpayers according to their economic situation. Studies on horizontal fairness for instance, reveal that taxpayers are more likely to evade tax because they feel they are treated disadvantageously as compared to other taxpayers across the various tax groups (Spicer and Becker, 1980). Other types of fairness, according to Wenzel (2003), are distributive justice, procedural justice and retributive justice. This dimension of fairness relates to the exchange of resources in terms of cost and benefit; process employed to reach the distribution outcome; and the appropriateness of sanctions in tax law. However,

research related to tax fairness and tax compliance currently focuses on distributive justice (Kirchler, 2007). Distributive justice in this context is closely associated with the concept of horizontal and vertical fairness, which examines the individual's tax burden compared to the similar taxpayer group or the tax burden across different taxpayer groups. Other dimensions of fairness identified are general fairness/distribution, attitude towards taxes of the wealthy and self interest (Christensen, Weihrich and Gerbing, 1994; Christensen and Weihrich, 1996; Gerbing, 1988). These elements of fairness have been tested and are applicable in a direct tax context. However they may not be applicable to an indirect tax such as import tax, a tax regime based on consumption. For instance, there is no difference in the import tax rate imposed on higher and lower income earners, or different categories of businesses. Hence, the element of fair distribution of tax imposed on various levels of taxpayers' income, such as distributive justice, vertical fairness, horizontal fairness and attitude towards taxes of the wealthy, may not be relevant to the context of indirect tax.

Among the various types of fairness in tax compliance, exchange of fairness is the most significant component of fairness that relates to this context of study. Although there are a growing number of studies on tax fairness, there is a handful of literature that focuses on exchange of fairness with the government. These studies indicate that exchange of fairness is an important factor that influences tax compliance (for example, Azmi and Perumal, 2008; Richardson, 2005, 2006; Saad, 2010; Spicer and Lundstedt, 1976). Azmi and Perumal (2008) conducted a study of 390 taxpayers in Malaysia to understand the relationship between fairness and compliance. The responses, which include both salaried taxpayers and business taxpayers, reveal that exchange of fairness is an important factor influencing tax compliance. More recently, a study on tax fairness dimensions on individual taxpayers in Malaysia also revealed that exchange of fairness is one of the most important tax fairness dimension in tax compliance (Saad, 2010).

Richardson (2005) made similar findings in a cross-cultural study of tax fairness perception in Hong Kong and Australia. A total of 407 postgraduate business students from Australia and Hong Kong universities were selected as a proxy for actual taxpayers. The results reveal that there is a positive perception of exchange of fairness in government spending and tax compliance behaviour for Hong Kong and Australia, but indicate a significant difference between the two countries. These

differences, according Richardson (2005) are anticipated, as the government spending on services such as health, education and defence are relatively lower in Hong Kong than Australia. In a more recent study, Richardson (2006) uses a similar sampling method of postgraduate business students in two Hong Kong universities. The results are consistent with the previous findings which indicate a significant result for the relationship between exchange of fairness with the government, and tax compliance.

The findings from the above studies provide an interesting insight which demonstrates that government policies on tax spending influence taxpayers' behaviour across various cultures and jurisdictions. In Malaysia, the government budget allocation for services, and various developmental projects for the nation, account for about 40% of total tax collection (Accountant General of Malaysia, 2015). This indicates a substantial allocation of tax revenue to fund various government projects. Hence the concept of exchange of fairness is relevant in the context of import tax, as the benefits received from high spending policies by the Malaysian government can be perceived as fair/unfair compared to their tax contribution, which may influence taxpayers' decisions to declare the correct amount of import tax or to declare less. The relationship between exchange of fairness and tax compliance behaviour is further tested in the development of compliance model in Chapter 7.

To summarise, the tax compliance determinants discussed in this section (Section 5.3) comprise various factors, which represent structural factors (law, law enforcement, complexity of procedure, tax assessment service quality), behavioural factors (attitude, behavioural intention, perceived behavioural control), social factors (perception of fairness, subjective norm), and other factors such as tax knowledge. Interestingly, there are mixed findings for some of the determinants. These reviews provide the basis for the integration of various variables in the development of the research model discussed in Chapter 7. The remaining section will discuss the philosophical assumptions and research approach of this study.

## **5.4 RESEARCH PHILOSOPHY**

### **5.4.1 Research Paradigm**

A research paradigm is a set of the ideas, philosophy, conceptual framework, assumptions and beliefs, that create and guide all scientific activities (Krauss, 2005). Different assumptions lead to different ways of approaching and conducting research (derived from different paradigms). Therefore, it is important to identify, explain and justify the research paradigm adopted in any research. Debates in social science have long continued about the best research paradigm. The debate continues mainly because each paradigm has some strengths and limitations. These vary according to the researcher's aim in exploring the studied phenomena. As outlined by Creswell (2009), there are three common research paradigms used in social science research: positivism, interpretivism, and pragmatism,

Jonker and Pennink (2010) define positivism as methods used incorporating the principles of deductive logic, with appropriate empirical observation of individual behaviour. The purpose is to acquire an answer for the probability of causation that can be used to forecast general patterns in human activity. The belief is that researchers should remain distant from the research to avoid bias in the research, which can distort their objective view. However, it has been argued that it is impossible to separate researchers from their social contexts and, therefore, social science cannot be understood without examining the perception of researchers' own activities (Hussey and Hussey, 1997). Positivism relates to the facts or causes of social phenomena and attempts to explain causal relationships through the means of objective facts (Carson et al., 2001). This paradigm focuses on describing, explaining and uncovering facts, where thought is accompanied by explicitly stated theories and hypotheses (Jonker and Pennink, 2010). The position assumes that science quantitatively measures independent facts about a single reality (Guba and Lincoln, 1994). Its epistemology is that data and their analyses are value-free and therefore, the data do not change because they are being observed. In other words, it is based on the belief that researchers are independent and that science is value-free (Carson et al., 2001).

On the other hand, the interpretive approach takes "a practical orientation and focuses on the issue of social integration" as informed by Neumann (1994). To

discover how individuals experience their everyday lives and to understand what is happening in a given situation, interpretivists must learn to see things from the point of view of the people being studied. Interpretivists claim that the world is socially constructed and subjective, and they hold a central postulation that there is no reality outside people's perceptions (Carson et al., 2001). This includes consideration of multiple realities, different actors' perspectives and the researcher's involvement, taking into account the contexts of the phenomena under study and the contextual understanding and interpretation of data (Neumann, 1994).

Generally, previous tax compliance research followed the positivist tradition, where knowledge is established through causal explanation of the relationship between taxpayer and tax compliance such as tax morale (Alm and Torgler, 2006; Cummings, Martinez-Vazquez, McKee and Torgler, 2005; Torgler, 2003), tax evasion (Cowell, 1992; Franzoni, 2000; Jean and Economie, 2008; Tsakumis, Curatola and Porcano, 2007) and compliance costs (Jabbar and Pope, 2008a, 2008b). Such studies are scientific and empirical, based on and supported by theories from previous studies. However, as suggested by previous research, more empirical evidence on the new understanding of tax compliance behaviour determinants can be discovered by approaches other than hypothetical-deductive approaches, such as the qualitative interpretive approach (Torgler, 2003). Taking into consideration additional approaches, such as the qualitative interpretive, into the existing quantitative approach seems to be a more pragmatic paradigm (Creswell, 2009). However, the central focus of a pragmatic approach is on the research problem instead of the methods used to describe an experience through (i) observation and measurement, or (ii) a causal explanation, as viewed by positivists (Creswell, 2009; Mertens, 2005).

In reality, the decision whether to apply a quantitative, qualitative or a mixture of both approaches is based on belief rather than philosophical commitment to the design and methods most suitable for the purpose of the study (Johnson and Onwuegbuzie, 2004; Vanderstoep and Johnston, 2009). As highlighted by Creswell (2009, p13), "*individual researchers have a freedom of choice. They are 'free' to choose methods, techniques and procedures of research that best meet their needs and purposes.*" In the context of this study, consistent with the existing tax compliance research tradition, the positivist view fits the research paradigm based on the core focus of the study, which is to understand the influence, determinants or relationships that cause behaviour to comply, or not comply, with import tax law. As asserted by

Creswell, (2013), elements such as influence, determinants, causes, factors, relationships and effects sit comfortably within the positivist paradigm.

The post-positivist, or ontological position of post modern realist, paradigm recognises the importance of the qualitative element or a mixture of interpretivist approach with the realist school of thought. The post modern realist paradigm is commonly associated with a realist evaluation (Pawson and Tilley, 2004), emergent realism (Mark, Henry and Julnes, 1998) and critical realism (Bhaskar, 1976; Sayer and Sayer, 2000). This approach is compatible with a wide range of research approaches including a mixture of qualitative and quantitative approaches. This post modern version of realism recognises the complexity of social phenomena by enabling the role of interpretivism and explanation as a legitimate goals in social research (Sayer and Sayer, 2000). The pragmatic paradigm also recognises the mixed model of quantitative and qualitative approaches as a balanced approach, which can be associated with a 'triangulation' approach (Creswell, 2007). However, post-positivism holds that the quantitative approach tends to be predominant over the qualitative, which can be aligned with the post-positivist paradigm (Mertens, 2005). For these reasons, the post-positivist paradigm can be adopted for the purpose of social research and management effort as it is consistent with the quantitative approach, which is the dominant approach, with some qualitative elements, considered in this study. In view of the suggestion by Torgler, (2003) for more qualitative empirical evidence to understand tax compliance determinants, and especially the under-explored area of indirect tax, the post-positivism paradigm better suits this type of research ambition than the pragmatic paradigm.

#### **5.4.2 Research Approach**

As described above, the post-positivist paradigm is applied in this study and the qualitative and quantitative research approaches are employed sequentially or by mixed method. Different researchers use the terms quantitative and qualitative in fundamentally different ways. For example, Creswell (2009) and Vanderstoep and Johnston (2009) describe quantitative data as including numbers, whereas qualitative data include words, symbols, pictures and other nonnumeric data. Research is described quantitatively by the term positivism, and starts from the scientific method used in the physical sciences (Crotty, 1988). A quantitative approach to the objective of the research is done in a systematic and formal manner, and the resulting findings

are numerical data. This approach explains, tests and investigates the relationship of cause and effect, using a deductive approach (Hussey and Hussey, 1997). Meanwhile, the methodology of deductive theory, involves quantitative testing of existing knowledge, through the relationship of the proposed hypotheses and outcome of research (Bryman, 1989). The quantitative method produces legitimate scientific answers and as a result of this hard data, action is generated and changes take place. In contrast, qualitative research is guided by ideas, or an intuitive perspective on the subject to be investigated (Bryman, 1989).

Quantitative research demands a random sample selection from the study population, and a random sample assignment from the various study groups (Walker, 2005). Statistical sampling relies on the study sample to develop general laws, which can be generalised to the larger population. The advantage of results obtained from random sampling is that the findings have an increased likelihood of being generalisable. The disadvantage, and a weakness of the quantitative approach, is that random selection is time-consuming, which sometimes results in the use of more easily obtained opportunistic samples. This inhibits the possibility of generalisation, especially if the sample is too small (Walker, 2005).

However, the form of qualitative research is rather different from the quantitative approach it develops inductive theories. Findings are not in a clear format to calculate or quantify, quite the opposite. The qualitative approach, as described by Walker (2005), is used as a vehicle to study the empirical world from the perspective of subjects, not researchers. This is supported by Pyett (2003), who describes qualitative research as “a systematic method of inquiry concerned with understanding of human beings and the nature of their transactions with themselves and with their understanding”. The aim of qualitative research is to describe certain aspects of a phenomenon, with a view to explaining the subject of study (Vanderstoep and Johnston, 2009). The qualitative approach produces soft data, which have been, and still are by some, described as being inadequate in providing answers or generating any changes (Golafshani, 2003).

Qualitative research, because of its in-depth nature and the analysis of the data required, usually relates to a small, selective sample (Golafshani, 2003). A weakness of this can be the suspicion that the researcher could be influenced by a particular susceptibility, affecting the generalisability of the small-scale study (Bryman, 1988). This suggests that qualitative research has low population validity. However, the



strength of this approach is seen when the sample is well defined, as then it can be generalised to a larger population (Maxwell, 1992).

Teddlie and Yu (2007) provide a brief history of the mixed method. They reveal that a significant amount of mixed method research occurred in the traditional positivistic period, 1900-1950. Mixed method research is defined as, “*the class of research where the researcher mixes or combines quantitative or qualitative research techniques, methods, approaches, concepts or language into a single study*” (Johnson and Onwuegbuzie, 2004, p17). Specifically, it can be conceptualised as combining quantitative and qualitative research in a concurrent, sequential, conversion, or parallel way (Creswell, 2009; Teddlie and Yu, 2007).

Although a number of researchers believe that qualitative and quantitative methods cannot be mixed, since the assumptions underlying each method are so vastly different, researchers such as Creswell (2009) and Teddlie and Yu (2007), point out that using different methods in the same study minimises the potential limitations. Using both qualitative and quantitative methods allows the researcher to discover and justify the model components within one study. Furthermore, the results from one method may be used to develop or inform the other method (Vanderstoep and Johnston, 2009) and one method can be nested within another method to provide insights into different levels of units of analysis (Saunders et al., 2003). Briefly, this approach allows the researcher to generate a model that has been ascertained through both qualitative and quantitative methods and to test it within a larger sample from the total population within a study. In other words, it may involve mixed methods. Saunders et al. (2003) add that it is crucial to identify a particular strategy for the research, primarily because of the differences between the deductive and inductive approaches. A detailed explanation of the research design adopted in this study is given in the subsequent chapter.

To sum up, qualitative methods are suitable for addressing questions of how and why things occur, whereas quantitative methods are more appropriate for answering what and how questions (Yin, 1994). However, the use of mixed methods in this study enhances its strengths and reduces its weaknesses. The applicability of TPB as the base theory is also justified for this study. The various constructs including the original TPB constructs, as discussed earlier in this chapter, are selected as the basis for the research model development, which is further explained in Chapter 7. The following chapter discusses the methods and procedures applied in this study.

## **CHAPTER 6**

### **RESEARCH METHOD AND DESIGN**

The discussion in the preceding chapter provides the basis of this study, adopting an exploratory research method which employs qualitative and quantitative approaches. This is described at the beginning of this chapter, which elaborates on the exploratory sequential mixed method research design applied in this study. This is followed by a detailed description of the procedure, divided into two phases, (I) qualitative and (II) quantitative. This chapter also provides a description of the Structural Equation Modelling (SEM) method to assess the measurement and structural models. The last section highlights the ethical considerations of the study which includes matters pertaining to the anonymity of the respondents, data security and confidentiality.

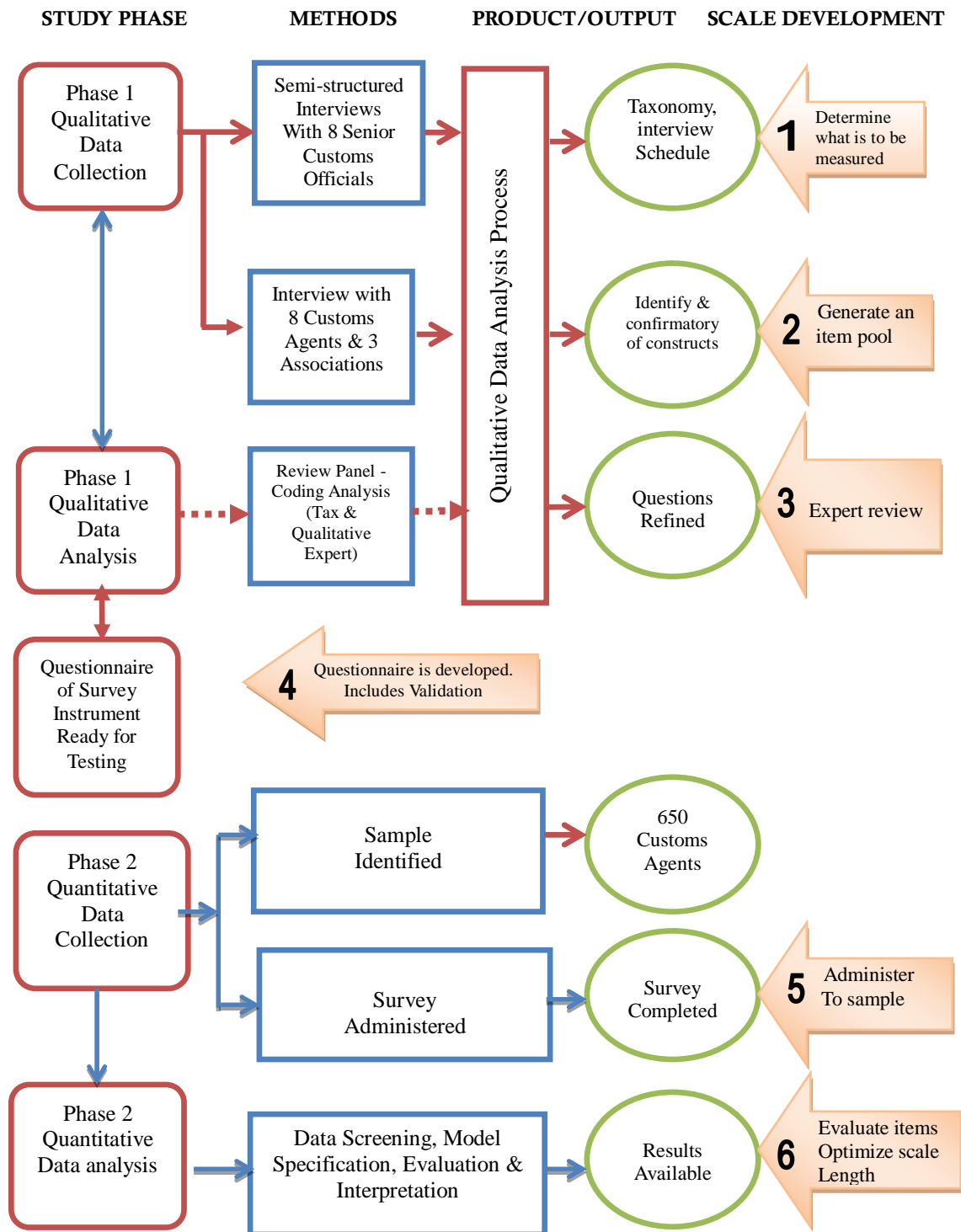
#### **6.1 RESEARCH DESIGN: EXPLORATORY SEQUENTIAL MIXED METHOD**

As identified in the preceding section, the research design that best matches this study is the two-phase exploratory mixed methods sequential design (Creswell, 2009). Phase One is an exploratory qualitative study conducted with Customs agents. The objective of this phase is to define and ascertain the dimensions of import tax compliance and the theory of planned behaviour (TPB) as the model applied to understanding compliance behaviour. This is accomplished based on the constructs identified in the literature review and then corroborated by asking Customs agents to describe their experiences and perceptions of import tax compliance.

In this regard, Creswell (2009) defines the rules of the mixed method as focusing on collecting, analysing and incorporating both qualitative and quantitative data into a series of research studies. This study combines the two forms of research methods, qualitative and quantitative. However, the mixed method design used for this study is exploratory. The design is chosen based on characteristics such as the initial phase, involving qualitative data collection and analysis followed by a quantitative data collection phase and analysis (Bryman, 2006). Greater emphasis or

weight is placed on the quantitative method in Phase Two. The findings of the qualitative phase help develop and inform the quantitative phase.

**Figure 6.1: Visualisation of the Steps Involved in the Research Design**



Source: Author

Phase One is the design exploration, as there is a need to explore in-depth a topic or phenomenon through qualitative methods, and then to generalise the results through a larger sample of quantitative designs in Phase Two. In this study, the design exploration is essential due to the lack of empirical work in the context of the study. The purpose is to identify the dimensions of tax compliance from the perspectives of Customs agents as the indirect tax agents/tax preparers. It also serves to improve the instruments used for the development of the final research model.

In other subject areas such as sociology, communications or the medical field, the use of mixed methods is long-standing. However, using mixed-method research for a tax compliance study is a relatively new paradigm. The research tradition in tax compliance has followed the route of surveys, laboratory experiments and economic analysis (Cummings et al., 2009; Torgler, 2003). Figure 6.3 shows the visualisation of the steps of the research design including its timelines.

## **6.2 OVERVIEW OF METHOD AND PROCEDURE: PHASE ONE - QUALITATIVE STUDY**

In the first phase of this study, the qualitative data are gathered through semi-structured interviews (Bryman, 1989). The interviews make up part of the mixed-method phase as the issues are extremely difficult to investigate by questionnaire alone (Vanderstoep and Johnston, 2009). The interviews give the researcher the opportunity to find out the participants' views and thoughts on import tax compliance.

### **6.2.1 Telephone Interviews**

An interview is a purposeful discussion between two or more people that can help to gather valid and reliable data relevant to the research objectives. Cohen et al. (2007) point out three main purposes of an interview: (1) gathering information, which has a direct bearing on the research objectives, (2) testing hypotheses or suggesting new ones, or as an explanatory device to help identify variables and relationships, and (3) combining with other methods in undertaking research. In this study, the telephone interview design is applied to answer two research objectives, ascertaining the dimensions of the proposed import tax compliance model, and identifying any new dimension to measure the compliance intention and behaviour of Customs agents. Furthermore, data obtained directly from the experience of Customs

agents through the interview helps to prove and clarify the cognitive and emotional perceptions of compliance behaviour and behavioural intention.

### **6.2.2 Sample Profile**

The participants selected for interview consist of Customs agents and representatives from Customs agents associations (logistics and freight forwarder associations). The selected participants are key decision makers within their companies, who are able to provide rich and in-depth information based on their experience and seniority. In practical terms, these participants are mature and psychologically-ready. To protect the anonymity of the participants, they are referred to as R1, R2, R3... instead of their actual names. Purposive sampling is used in this phase as a sampling strategy (Sekaran and Bougie, 2011). Potential participants are sourced from the database of the Royal Malaysian Customs Department. The participants are also selected based on the researcher's individual judgment, where permitted, on the grounds that they are able to provide the necessary information for this phase.

### **6.2.3 Interview Protocol and Procedure**

Participants are first emailed advising them of the survey and seeking their support. The email is followed up with a telephone call seeking a suitable time for a telephone interview. Prior to the interview, the questionnaire is emailed to the participants to aid their understanding and give them time to think about their responses prior to the interview.

The interview questions are developed based on the proposed conceptual framework of import tax compliance based on the theory of planned behaviour (TPB), which comprises of five main constructs: attitude, subjective norm, perceived behaviour control, intention to comply and compliance behaviour. All the questions are posted to the participants one week before the interview is conducted. Some examples of the main questions are (detailed questions are in Appendix 5):

- (1) I would like to hear your thoughts on the long-standing issue of improper declaration of import by forwarding agents which affects the revenue

collection of Customs department. What are the causes of this problem in your opinion?

- (2) How can this situation be improved?
- (3) In your opinion, what motivates the agents to comply with import declaration and pay import tax correctly?
- (4) Have you or other agents that you know of experienced being detected by our enforcement team for under-declaration of goods? Are they afraid of their agent's license being revoked? Are they being penalised, for example, by having to pay a high penalty or imprisonment?

Open-ended questions are posed to participants during the interviews to enable them to talk freely about the topic in their own words and to give them an opportunity to provide rich and detailed information on their experience (Bryman, 1989). The open-ended questions are often followed by additional questions in order to probe for detailed explanations (for example: Why do you think this is the case?). The interviews are audio-taped and transcribed to enable referencing of the parts of the interview, which allows the researcher to obtain an increasingly clear image of the interviews as a whole.

The sensitive nature of compliance information might create an incentive not to participate in such an interview, and might prevent them from providing honest answers. This problem is minimised by ensuring the respondents have complete confidentiality and questions which cover a broad variety of topics are posed, such as institutional issues, the regulatory framework and their general view of compliance, rather than direct questions about whether the person has evaded taxes. Thus, it can be supposed that a higher degree of honesty can be observed in the answers to these questions.

#### **6.2.4 Qualitative Data Analysis**

Data analysis for the qualitative part of the study is carried out through content analysis by drawing up a list of coded categories and 'cutting and pasting' each segment of the transcribed data into one of these categories. This step is done manually. The use of qualitative analytical tools such as NVivo could be useful, but the author has decided to perform the analysis manually as suggested by several

researchers. Bogdan and Bilken (1982), and Pope and Mays (2000) are among the few who describe the basic procedures of manual coding using various methods, such as cut-and-paste and note cards. Manual data analysis is more accurate, reliable and easy to handle (Bogdan and Bilken, 1982). Barry (1998) agrees that data analysis is more rigorous and transparent using manual methods, and hence data are interpreted more confidently. Whelsh (2002) stresses that if the data set is relatively small, it is possible to use only manual methods, although the researcher does risk human error when searching for simple information in the whole data set.

Following these steps, an expert panel reviewer assesses the process and verifies the themes and categories identified by the researcher from coding, comparing, and analysing the interview data. This is part of the validation process, to increase the validity of the analysed data for refinement.

### **6.3 OVERVIEW OF METHOD AND PROCEDURE: PHASE TWO - QUANTITATIVE STUDY**

As outlined in Figure 6.3, the quantitative phase is carried out after Phase One is complete. Data collection in Phase One of this study is related to the second quantitative phase of the study. The following subsections describe the process of quantitative study applied in this research design. They describe the selection of respondents, development of the pre-test analysis instruments, method of survey distribution and procedure of data analysis.

#### **6.3.1 Selection of Respondents**

##### **(a) Sampling Frame**

This study involves understanding the compliance behaviour of Customs agents as tax agents in Malaysia. The survey population consists of all Customs agents located in the three main geographical areas, North, Central and South Malaysia. The geographical area is exhaustively sampled, rather than choosing samples across the whole nation, because, given the complex nature of the study, geographical proximity facilitates follow-up action. Moreover, these three geographical areas are the main areas where a high number of Customs agents are

located, due to the high number of importation activities within these areas. A total of 2,179 Customs agents are located in the three main geographical areas. The largest population is located in the central zone, which has 57% of the total population, followed by the south zone. Table 6.2 shows the population of each area.

**Table 6.1: Population of Customs Agents in Malaysia**

<b>Population</b>			
<b>Cluster</b>	<b>Zone</b>	<b>Frequency</b>	<b>Percent</b>
1	Central (Selangor)	1109	51%
2	Central (KLIA)	136	6%
3	North (Penang)	356	16%
4	South (Johor)	578	27%
<b>Total</b>		<b>2179</b>	<b>100%</b>

*Source: RMCD, (2013)*

#### **(b) Sample Size**

The determination of sample size is a common aspect of study design. It is important to ensure that the selected samples are appropriate, adequate and sufficient to increase the accuracy and quality of research (Bartlett, Kotrlik and Higgins, 2001). There are various ways to determine the appropriate sample size, for instance variance estimation and error estimation (Bartlett et al., 2001; Cochran, 1963; Krejcie and Morgan, 1970; Yamane, 1967).

In this study, the sample size is determined using the sampling formula by Yamane (1967) expressed as follows:

$$n = \frac{N}{1 + N(e)^2}$$

In this formula, n represents the sample size, N is the total population, e is the error term depending on the confidence level, and P=.5 is assumed for the equation. When applying this formula to obtain the sample size from a population of 2,179 random samples, results in a recommended sample size of 337. The calculated sample size of 337 is cross-referenced with the sample calculation provided by Krejcie and



Morgan (1970), which is reproduced in Table 6.3. For a population size between 2,000 and 2,200, the suggested sample size is between 322 and 327, which is very close to the 337 calculated using the Yamane formula. This sample size is also within the recommended size of 30 to 500 samples, which is common to many studies (Sekaran and Bougie, 2011).

**Table 6.2: Population and Sample Size Calculation Table**

N	n	N	n	N	n	N	n	N	n
10	10	100	80	280	162	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	346
25	24	130	97	320	175	950	274	4000	351
30	28	140	103	340	181	1000	278	4500	354
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	191	1200	291	6000	361
45	40	170	118	400	196	1300	297	7000	364
50	44	180	123	420	201	1400	302	8000	367
55	48	190	127	440	205	1500	306	9000	368
60	52	200	132	460	210	1600	310	10000	370
65	56	210	136	480	241	1700	313	15000	375
70	59	220	140	500	217	1800	317	20000	377
75	63	230	144	550	226	1900	320	30000	379
80	66	240	148	600	234	2000	322	40000	380
85	70	250	152	650	242	2200	327	50000	381
90	73	260	155	700	248	2400	331	75000	382
95	76	270	159	750	254	2600	335	100000	384

Source: Krejcie and Morgan, (1970, p608)

N=Population, n=samples

Considering the nature of this study, the cross-sectional method is considered. According to Ruspini (1999), in the social sciences it can be very difficult or impossible to conduct longitudinal research, even in the natural environment. Therefore, the most common method used is cross-sectional data collection. A cross sectional study takes a snapshot of a population at a certain time, allowing conclusions about a phenomena across a wide population to be drawn (Martyn, 2009). The advantage of using this method is that it allows researchers to study the natural environment, thus improving the external validity of the study.

### **6.3.2 Survey Design**

Questionnaire construction is one crucial step in survey design in order to obtain the desired information. The questionnaire is designed with two goals in mind: relevance and accuracy of the information collected. Therefore, the order and wordings are designed in such a way as to obtain accurate answers and information from respondents. In addition, there are several steps involved in developing the questionnaire, including review of the relevant literature and qualitative interview findings. The details of the survey questionnaire development, including the measurements, are discussed in Chapter 8 of this thesis.

### **6.3.3 Pre-Test Stage**

Pre-testing is carried out after the development and compilation of the questionnaire instrument. Pre-testing refers to the examination of the questionnaire on a small sample of respondents to identify and eliminate potential predicaments. During the process, the survey questionnaire may require some modification of the structure, or refinement to fit the research objectives. The emphasis at this stage is placed on appropriate wording of the questions and clarity of instructions rather than reporting results (Synodinos, 2003). This approach enhances the scale content and construct validity (Malhotra et al., 2008). Content validity, on the other hand, is used to assess the appropriateness of the item scales and the comprehensiveness of measurement. Construct validity determines whether a scale adequately represents the evaluated concept and measures what it is intended to measure (DeVellis, 2003).

The survey questionnaire is pre-tested with reviewers in the field of behavioural research and taxation. At this stage, all comments and suggestions from experts are incorporated to improve the survey questionnaire prior to the actual survey distribution. The responses from experts are analysed and the information provided is used to clarify the wording of the questions as well as the sequence of the instrument and constructs presented.

### **6.3.4 Survey Distribution**

The survey questionnaire is disseminated by mail to a selected sample of agents within the three geographical areas in Malaysia: north zone, central zone and south zone. A mail survey is selected, as opposed to an on-line survey, due to an

identified limitation, the unavailability of agents' email information, mainly because the Customs information database does not store the agents' company email information. The information available is the agents' business addresses and contact numbers. Furthermore, it is a practice in the Customs administration that any formal letter or mail sent or received on paper or hard-copy, is appropriately certified and signed by the respective authorising officer. Therefore, it has been decided that the most appropriate method of disseminating the survey questionnaire is by mail. The questionnaires are sent to selected Customs agents, whose names are chosen from the Customs database.

Although there are limitations in using mail survey, it has several advantages. According to Duke and Mallette, (2011), the advantages of mail surveys include: it is suitable for large and scattered areas, provides a high precision rate if the questionnaire is returned at or near the same time, avoids mistakes or errors arising from the enumerator, and provides opportunity for subjects to think for a moment before answering.

There are also some disadvantages to using this method. It is suitable for simple questions, but not complex and difficult to understand questions. This problem is overcome by conducting a pre-test. Information received during the pre-test stage is used to improve the questions in the questionnaire. Another weakness is that the given answer is final, and it is not possible to ask about something which is vague. This problem is overcome by establishing objective questions and avoiding subjective questions. Another issue is that the answers are likely to be influenced by others, which is difficult to control for. To overcome this weakness, a formal letter is attached, asking respondents to answer questions freely and without prejudice.

There is also a possibility that respondents may not answer the survey questionnaires. The typical response rate for mail surveys ranges between 20% and 60% (Whitehead, Groothuis and Blomquist, 1993). Previous studies in Malaysia which have used mailed surveys show an average response rate of between 16% and 24% for individuals, and 43% and 65% for companies (Palil, 2010). To achieve the highest and most statistically relevant sample of 337 respondents, a total of 650 (based on approximately 50% response rate) questionnaire copies are distributed. In addition, a follow-up method, such as phone call, is used to increase the response rate.

The questionnaire copies are disseminated through the disproportionate stratified sampling method based on the ratio of each group (refer to Table 6.4). This

method of distribution is more representative than the non-probability sampling method due to the disproportionate population size of this study. This sampling method has the advantages of higher precision and optimisation of costs (Henn, Weinstein and Foard, 2006; Marsden and Wright, 2010). With this method of sampling distribution, the minority or lower density population group within the cluster has more opportunity to participate in surveys as compared to using the proportionate sampling method. The distribution size of each cluster is determined by the researcher based on a disproportionate stratified sampling distribution (Henn, Weinstein and Foard, 2006).

**Table 6.3: Distribution of Survey Questionnaire Based on Disproportionate Stratified Sampling Method**

Cluster	Zone	Population Size	Distribution Size	
		Frequency	Frequency	Weight
1	Central (Selangor)	1109	300	46.15%
2	Central (KLIA)	136	80	12.31%
3	North (Penang)	356	100	15.38%
4	South (Johor)	578	170	26.15%
<b>Total</b>		<b>2179</b>	<b>650</b>	<b>100%</b>

A general problem in tax compliance research is that some respondents might refuse to provide honest answers, since the responses obtained are directly linked to the respondents' propensity for compliance or non-compliance. This problem is minimised by guaranteeing anonymity to the respondents. Specifically, neutral envelopes are used to send back the questionnaires, and standard demographic information is asked for instead of specific personal characteristics (Dillman, 2007). In addition, indirect questions are posed, instead of direct question related to tax compliance or non-compliance. The method of using questionnaires and the absence of interviewers in mail surveys also evokes honest responses and produces valid indirect measures of behaviour (Spicer and Lundstedt, 1976). Furthermore, self reported compliance behaviour using survey questionnaire is still a dominant and popular approach to tax evasion and tax compliance research (Elffers, Robben and Hessing, 1992).

### **6.3.5 Data Analysis Procedure**

The analytical procedure applied in this study involves several stages, as follows:

- (i) The first stage involves the process of data screening and testing to meet the multivariate assumption. The aim is to look at the position and the relevance of data for the purpose of statistical analysis (Hair et al., 2010).
- (ii) After the first stage, the data are analysed at the level of exploratory factor analysis to identify the basic structure (underlying structure) of the variables in the study (Hair et al., 2010).
- (iii) In the third stage, structural equation modelling (SEM) is used to analyse the constructs related to import tax compliance behaviour. According to Hair et al. (2010), the use of this approach has some advantages because the measurement model and structure can be tested simultaneously.
- (iv) The measurement model is completed through confirmatory factor analysis to validate the scale for the measurement of the constructs (Hair et al., 2010). Constructs that passed this analysis are applied in the structural model analysis to study the relationship between the endogenous and exogenous<sup>27</sup> variables in this study. Specific discussion of the analytical techniques used is given in the next section.

#### **(a) Missing Data**

Missing data can cause sample size reduction. Furthermore, if the sample size is inadequate, it might not suit the statistical analysis (Hair et al., 2010; Schlomer, Bauman and Card, 2010). For this study, descriptive information is first obtained to identify the number of incomplete questionnaires or missing data. The percentage of variables with missing data points in each case is tabulated, followed by tabulation of the number of cases with missing data points for each variable (Hair et al., 2010). This process identifies the extent of missing data points, and any exceptionally high levels of missing data points that occur for individual cases or observations. Cases or variables with more than 10% missing data points are eliminated (Bennett, 2001; Hair

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<sup>27</sup> Endogenous and exogenous are terms used in structural equation modeling, commonly referring to dependent and independent variables.

et al., 2010). A final review of the missing data points indicates that the remaining missing data points are insignificant or below the threshold to warrant any further diagnosis (Hair et al., 2010).

#### **(b) Data Screening**

In this study, the data are screened to test their suitability and position before the multivariate analysis is performed. The data are analysed with statistical software package, SPSS software version 19. The screening process is divided into two stages, data screening and data testing, to meet the assumptions for multivariate statistical analysis (Hair et al., 2010). For data screening, three types of tests are performed, the response bias test, incomplete data (missing data), and outliers. The purpose of this process is to clean up the data so that they are in a suitable form for multivariate analysis assumptions (Hair et al., 2010). These tests are intended to be the bases for making conclusions and providing statistical results. The test is also a prerequisite for factor analysis and multivariate analysis (Hair et al., 2010).

##### **(i) Missing value estimation procedure**

Missing value is the process of assessment of any non-random missing data points, such as missing data points in a certain specific set of questions. Hair et al. (2010) suggest a close examination of the data sets to detect any non-random pattern. The missing completely at random (MCAR) test is a procedure to analyse the missing data points and determine the randomness of the missing pattern in the data sets. MCAR data indicates as a higher level of randomness and cannot be distinguished from the cases with complete data. Missing at random (MAR) indicates that incomplete cases differ from cases with complete data, which can cause generalisability issues (Bennett, 2001). A missing value analysis using the 'little MCAR' test in SPSS software produces an estimation of missing data, if the data points are missing completely at random (MCAR). Data are considered as MCAR when the  $p$ -value is significant at  $> 0.05$ .

Any missing values, whether missing completely at random (MCAR) or missing at random (MAR), are treated carefully with the appropriate method of imputation, either non-stochastic imputation methods such as regression or stochastic methods such as expectation maximisation (EM) (Schlomer et al., 2010).

## **(ii) Outliers/Extreme Value Analysis**

To test outliers, this study uses regression procedures to identify univariate and multivariate outliers. Univariate outliers are identified by looking at the value of  $z$  (z-score) calculated in the survey data set. Coakes and Steed (2003) suggest that a question in a questionnaire is a univariate outlier if the  $z$ -score is greater than  $\pm 3.0$ . For multivariate outliers, Mahalanobis distances ( $D^2$ ) test is applied to all exogenous variables. According to Hair et al. (2010), a data point is said to be an outlier of multivariate nature if the  $D^2$  / degrees of freedom (df-degrees of freedom) is greater than  $\pm 1.96$  or  $\pm 2.58$ , in which case the data have to be removed from the study.

## **(iii) Test of Normality**

The purpose of this test is to see whether the relationship between two variables is linear or otherwise. According to Coaked and Steed (2003), this test can be done using the straight-line method, which is matched with the data through a dispersion plot. The method used for the purpose of this test is according to the statistical values of skewness and kurtosis. Data is said to be normal in the probability of  $p = 0.01$  if the value of skewness and kurtosis are less than  $\pm 2.58$  (Coaked and Steed, 2003). Data are categorised as normally distributed if the skewness and kurtosis show zero value.

## **(c) Handling Non-Response Error**

There are four possible sources of error in the sampling of survey research, which can be categorised as (1) sampling error; (2) coverage error; (3) measurement error; and (4) non-response error (Dillman, 2007). These are the common types of error when any respondents in the sample fail to provide a usable response or different responses from those sampled in the study (Lindner, Murphy and Briers, 2001). For studies involving voluntary participation of the respondents, a significant difference in the given answers may occur (Matteson, Ivancevich and Smith, 1984).

One of the common methods applied to handling non-response error is comparing the two groups of early and late respondents<sup>28</sup> (Lindner et al., 2001;

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<sup>28</sup> Late respondents can be used as a predictor of non-respondents, to estimate the nature of responses of non-respondents as they share similar characteristics (Armstrong and Overton, 1977; Miller and Smith, 1983).

Matteson et al., 1984). The purpose is to evaluate if there are significant differences between the two groups of respondents, those who respond earlier and those who do so later. This procedure involves dividing the sample into two groups, respondents who submit the questionnaire in advance, and respondents who return the questionnaire after the specified time (Lindner et al., 2001).

Respondents who return the questionnaire within two weeks of its release are categorised as the early respondent group, and those who return the questionnaire after the two weeks are categorised as the late group. These two groups are coded as 1 and 2. Code 1 is the first group of respondents, while code 2 is the second group of respondents. The T-test is applied to test the difference between the two groups. A significance level of  $p < 0.05$  indicates that the data had biased response (Lahaut et al., 2002). There is no biased response if the  $t$  value is insignificant, in which case the results are generalisable to the target population (Miller and Smith, 1983).

#### **(d) Descriptive Statistics**

Apart from inferential statistics, a section that describes the descriptive statistics also features as a summary of the survey data collected for this study. Therefore, prior to data analysis, the survey data are presented as a demographic profile of the respondents. The descriptive data of the constructs and indicators applied in the research model are also presented by calculating the means, standard deviation and frequency for each construct.

#### **6.3.6 Structural Equation Modelling (SEM)**

This study applies the structural equation modelling (SEM) method. SEM is an established method for social science research and has been increasingly applied in various disciplines, predominantly in the field of marketing research (Diamantopoulos and Winklhofer, 2001; Hair, Ringle and Sarstedt, 2011; Hair, Sarstedt, Ringle and Mena, 2011; Henseler, Ringle and Sinkovics, 2009). It is an advanced multivariate technique to simultaneously examine multiple dependent relationships between variables. It helps researchers be more precise in their hypothesis specification and construct operationalisations, it takes into account the reliability of measures in tests of hypotheses in ways beyond the averaging of multi-



measures of constructs, and guides exploratory and confirmatory research by combining self-insight and modelling skills with theory (Bagozzi and Yi, 2011; Henseler, 2011). It is useful in experimental or survey research, cross-sectional or longitudinal studies, measurement or hypothesis testing, within and across groups and institutional or cultural contexts, and is easy to use.

Henseler (2011) identifies the advantages of SEM as including its ability to model latent variables, correct measurement error, specify errors and their covariance structures and estimate entire theories simultaneously. It allows a researcher to model and predict relationships between construct variables in a hypothesised manner. SEM is used in this study due to the complex structure of the framework as well as the sample size.

Two approaches to the application of SEM have been considered for this study: (1) covariance based techniques (CB-SEM) such as AMOS, LISREL, MPlus and EQS; and (2) variance-based techniques, partial least squares (PLS-SEM) such as SmartPLS, PLS Graph and LVPLS; and GSCA analysis using GeSCA software program.

#### **(a) PLS-SEM and CB-SEM**

Covariance based-SEM (CB-SEM) is a modelling technique originally developed by Karl Joreskog (Joreskog, 1978). CB-SEM is a generalisation of the path model of the two principals, component analysis (PCA) and factor analysis, to the case of several data tables associated with a causal relationship (Iacobucci, 2010). CB-SEM has been widely accepted in various fields of study and has been a popular choice for SEM, compared to PLS-SEM. PLS-SEM, developed by Herman Wold, is an alternative modelling technique for CB-SEM. PLS-SEM focuses on prediction, as it generalises the principal component analysis and path models to the case of several data connected by causal links (Fornell and Bookstein, 1982).

According to Wold (1985), CB-SEM and PLS-SEM have their own rigorous characteristics, and should not be considered as competing approaches, but more as complementing each other. There are various situations where researchers have to choose between the two approaches. This section will therefore discuss the two complementing approaches, their strength and limitations, and the suitability of the SEM method for this study, which will be justified in the subsequent section. The CBSEM and PLS approaches to data analyses are quite distinct in that each differs in

terms of its objectives, statistical assumptions and the nature of the fit statistics it produces (Gefen, Straub and Boudreau, 2000; Hair, Ringle et al., 2011; Hair, Sarstedt et al., 2011).

#### **(i) Objectives**

CB-SEM places greater emphasis on a strong theoretical foundation. It focuses on the estimation of model parameters in order to minimise the difference between the observed and predicted covariance matrix in the theoretical model (Hair, Ringle et al., 2011; Hair, Sarstedt et al., 2011; Monecke and Leisch, 2012). In contrast, PLS-SEM emphasises prediction by maximising the explained variance of the endogenous latent constructs (Hair, Sarstedt et al., 2011).

Therefore, PLS-SEM is more suited to prediction-based study, whereas in CB-SEM, it is expected that the analysis is performed using a well-developed measures with a strong theory (Anderson and Gerbing, 1988). Thus, it is more applicable for research involving theory testing, theory comparison, exploratory research or extension of existing structural theory (Hair, Ringle et al., 2011), although, it could also be applied in PLS-SEM for theory building and theory confirmation (Barroso et al., 2010).

#### **(ii) Measurement Model Specifications**

The measurement model specification is another distinct characteristic to consider in CB-SEM and PLS-SEM. In SEM, the formative and reflective measurement model indicators are important criteria when designing a model, to avoid the issue of model misspecification and statistical error (Diamantopoulos and Winklhofer, 2001; Jarvis et al., 2003). CB-SEM is designed to operate with the reflective measurement model indicator, although it can be applied to the formative under certain circumstances, with the inclusion of complex and limiting specification rules (Hair, Ringle et al., 2011). PLS-SEM, on the other hand, is less demanding on data and specification of relationships, moreover it can handle both reflective and formative measurement indicators (Fornell and Bookstein, 1982; Hair, Sarstedt et al., 2011; Henseler et al., 2009)

### **(iii) Structural Models**

PLS-SEM has the capability to handle complex models with higher number of constructs and indicators. In contrast, CB-SEM runs into difficulties when handling a model with 50 or more items (Chin and Newsted, 1999; Chin, 2010). Another distinction between PLS-SEM and CB-SEM is the type of structural model, whether recursive<sup>29</sup> or non-recursive<sup>30</sup> structural modelling, applied in the model of study. CB-SEM allows both non-recursive and recursive directional relationships among constructs, whereas PLS-SEM currently is restricted to recursive types of relationship (Barroso et al., 2010).

### **(iv) Data Characteristics and Algorithm**

In CB-SEM, data have to meet the exact assumption on sample size and data distribution, whereas these requirements are less demanding for PLS-SEM. The sample size requirement as recommended for CB-SEM is relatively large, ranging between 200 and 800 (Chin and Newsted, 1999). PLS however, can handle relatively small and larger sample sizes, so is less of a constraint, as compared to CB-SEM (Chin, Marcolin and Newsted, 2003; Hair, Ringle et al., 2011). Another distinct characteristic is the data distribution. CB-SEM can only operate when the data distribution is normal. In contrast, PLS-SEM has the advantage of being able to handle both normal and non-normal data distributions (Hair, Ringle et al., 2011).

### **(v) Model Evaluation**

Hair, Ringle et al. (2011) outline several conditions in relation to model valuation. If the study requires using the scores of the latent constructs for subsequent analysis and assessing global goodness-of-fit criteria, CB-SEM is a more suitable approach. In the case where there is a need to test for model variance measurement, PLS-SEM is the preferred approach.

The above discussion outlines five different characteristics of CB-SEM and

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<sup>29</sup> Recursive is a situation where the causal relationship between constructs is unidirectional (one line pointing from the one latent variable to another).

<sup>30</sup> In a non-recursive situation, the relationships between a pair of constructs are bidirectional, one pointing from A to B and the other from B to A.

PLS-SEM, which are the basis for choosing between the two complementing approaches. The five rules to determine the appropriate selection of the SEM approach by Hair, Ringle et al. (2011), are reproduced in Table 6.5.

**Table 6.4: Rules for Selecting PLS-SEM or CB-SEM**

Criteria	PLS-SEM	CB-SEM
1 Research Goals	Predicting key target constructs or identifying key ‘driver’	(i) Theory testing, confirmation, or comparison (ii) Exploratory research or extension of existing structural theory
2 Measurement Model Specification	Formative constructs are part of the structural model	Error term requires additional specification such as covariation
3 Structural Model	Complex structural model (many constructs and indicator)	Non-recursive model
4 Data Characteristics and Algorithm	Data do not have to meet the exact assumptions (PLS is a good approximation of CB-SEM results)  (i) Low to large sample size (a) 10 times the largest no. of formative indicators to measure 1 constructs (b) 10 times the largest no. of structural path directed at latent construct  (ii) Non-normal and normal data  (iii) Good approximation of CB-SEM result	Data has to meet the exact assumptions (minimum sample size and distributional assumptions)  (i) Large sample size  (ii) Normal data (Slightly more precise model estimate than PLS-SEM)  (iii) Couldn’t meet requirement (e.g. model specification, identification, non-convergence, data distributional assumption)
5 Model Evaluation	If required: (i) To use latent variable scores in subsequent analysis	If required: (i) goodness-of-fit criterion (ii) to test measurement model invariance

*Source: Hair, Ringle et al., (2011, p144)*

**(b) Partial Least Squares (PLS) – SmartPLS as the selected analytical tool**

The discussion in the previous section demonstrates the key differences between the covariance-based SEM (CB-SEM) and partial least squares SEM (PLS-SEM). Based on the five rules of thumb in the SEM selection process, as outlined by Hair et al. (2011), PLS-SEM application is the most advantageous for this study. The selection of SEM application is dependent on the research goal, whether for prediction purposes or for theory testing and development (Anderson and Gerbing, 1988).

The key research goal of this study is to understand the determinants of compliance behaviour through the application of TPB as the base theory, which is prediction oriented. In CB-SEM, the scores for the latent constructs cannot be estimated to predict the observed indicators due to factor indeterminacy, in which the case values for the latent constructs cannot be obtained from the observed data (Chin and Newsted, 1999). In contrast, in PLS, the latent variable scores are determinate and can be directly estimated (Fornell and Bookstein, 1982). Thus, CB-SEM may not be suitable for studies with predictive orientation. Therefore, PLS-SEM is suitable for this research goal, which has the capability of predicting the key target constructs better in the research model.

The second criterion in determining the SEM analytical approach is the measurement model specification. Although the rules outline that, if the formative constructs form the main part of the model, then PLS would be the best approach, it is important to note that PLS can handle both reflective as well as formative measurement models (Hair, Sarstedt et al., 2011; Henseler et al., 2009), which meets the criteria of measuring the reflective model in this study.

The third criterion is the structural model complexity. Hair et al. (2011) recommend using PLS if the structural model is complex and comprises many constructs and indicators. There are 78 indicators to measure 13 constructs in the structural model of this study.

The fourth criterion is based on the data characteristics in relation to sampling requirements and data distribution criteria. PLS can handle relatively small and larger sample sizes, which is less of a constraint compared to CB-SEM. The sample of this study is approximately 337 cases, which is within the size required for CB-SEM as suggested by Hair et al. (2010). However, for the purposes of this study, the size is not

considered sufficient to represent good distribution assumptions for CB-SEM due to the many constructs and indicators in the model, as mentioned. Moreover, CB-SEM can only model latent constructs where the data has a normal distribution, unlike PLS-SEM, which can handle both normal and non-normal data distributions. Therefore, PLS suits the data type in this study.

Finally, using PLS as an analytical tool has received little attention in tax compliance studies. Therefore, the interpretation of PLS application in this study proves that it can be applied successfully to a tax compliance behavioural model. For this purpose, SmartPLS 2.0 M3 application is applied, as it is a simple yet powerful analytical tool that is widely accepted in other inter-disciplinary literature. It is standalone software specialised for the PLS path model (Monecke and Leisch, 2012). The next section sets out the process of evaluating the PLS model.

### **6.3.7 Model Evaluation**

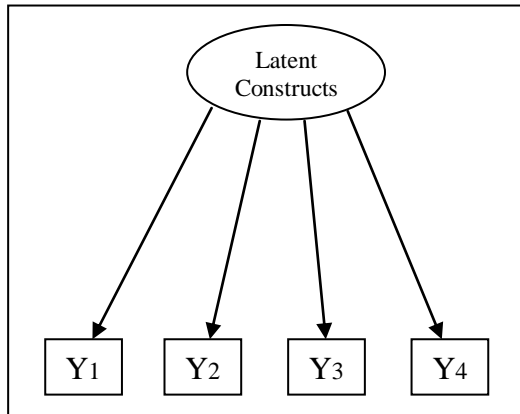
Among the considerations when developing a model are the indicators<sup>31</sup> used to measure the constructs. The constructs can be modelled as two types, reflective or formative indicator measurement models (Bollen and Lennox, 1991; Jarvis, MacKenzie and Podsakoff, 2003).

In the reflective model, as illustrated in Figure 6.2(a), the direction of causality flows from the construct to the indicator. This is referred to as the ‘effect’ indicator, which represents the respective constructs. Any changes in the constructs are reflected by changes in its indicators. Therefore, indicators representing the construct are expected to be highly correlated and interchangeable. Dropping an indicator for a construct in a reflective model does not alter the conceptual meaning of the construct (Jarvis et al., 2003; MacKenzie, Podsakoff and Jarvis, 2005). In other words, in the reflective model, the indicator measuring each construct should be uni-dimensional, but if any individual indicator is removed in the process of improving construct validity, it should not affect the content validity (Petter, Straub and Rai, 2007).

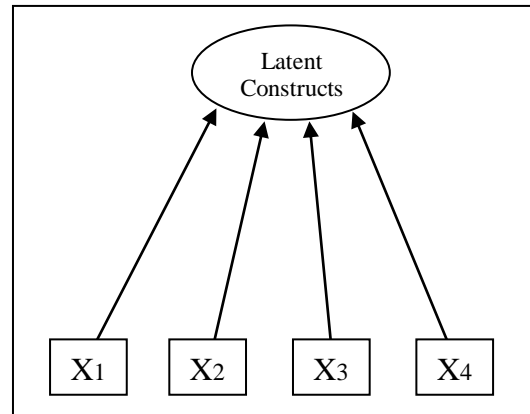
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<sup>31</sup> Indicators refer to measures or scale items which can be distinguished as either those that are influenced by (reflect) or influence (form) latent variables (Bollen and Lennox, 1991).

**Figure 6.2(a)**  
**Reflective Model**



**Figure 6.2(b)**  
**Formative Model**



*Source: Bollen and Lennox, (1991, p306)*

The second type of construct modelling is the formative model, as illustrated in Figure 6.2(b). In this model, the direction of causality flows from the indicator to the construct. This is referred to as a ‘cause indicator’, ‘formative indicator’ or ‘composite indicator’, and influences the construct. The indicators are not correlated with each other. Therefore, the implication of removing an indicator would be similar to dropping part of the construct and damaging the model (Bollen and Lennox, 1991).

There are several indicators, developed as a guide, to determine which type of measurement of constructs is to be modelled, either formative or reflective. Jarvis et al. (2003) outline four sets of decision rules to assist researchers in identifying whether to apply formative or reflective indicator measurement to their respective construct modelling. The four decision rules, outlined in Table 6.1, are: (I) direction of causality between each construct and its measures, (II) examining the inter-changeability of the measures, (III) consideration of co-variation among the measures and (IV) identifying whether the constructs have the same antecedents and consequences.

Mackenzie et al. (2005) suggest that, an indicator will be formative provided that, (a) it defines a distinct characteristic of the construct, (b) any change in its value is expected to explain changes in the construct, (c) it may or may not have a common theme (i.e. correlation) with other indicators, (d) removing an indicator may alter the conceptual domain of the construct, and (e) it may not have the same antecedents and consequences as other indicators.

**Table 6.5: Decision Rules in Determining Formative or Reflective Construct**

		<b>Formative Model</b>	<b>Reflective Model</b>
1	Direction of causality between each construct and its measures	Direction of causality is from its measures to construct.	Direction of causality is from construct to measures
2	Examining the inter-changeability of the measures	Indicators need not be interchangeable	Indicators should be interchangeable
3	Consideration of co-variation among the measures	Not necessary for indicators to covary with each other	Indicators are expected to covary with each other
4	Identify if constructs have the same antecedents and consequences.	Indicators are not required to have the same antecedents and consequences	Indicators are required to have the same antecedents and consequences

*Source: Jarvis et al., (2003, p203)*

The modelling construct indicator should be selected with caution and based on theoretical understanding. Some of the constructs are fundamentally formative in nature and should not be modelled reflectively (Podsakoff, MacKenzie, Podsakoff and Lee, 2003). If the constructs are inherently formative or reflective, they should be measured accordingly (Wilcox, Howell and Breivik, 2008). Bollen (2007) and Howell, Breivik and Wilcox (2007) further assert that the choice of measurement should be based on theoretical considerations, because constructs are not inherently formative or reflective.

Incorrect construct modelling of a reflective model as a formative model, or vice versa, could result in model misspecification error (Bollen and Lennox, 1991; Diamantopoulos and Winklhofer, 2001) and erroneous path coefficients, due to incoming and outgoing structural paths of the latent variable (MacKenzie et al., 2005). The effect of model misspecification could lead to type I and type II<sup>32</sup> errors in the measurement model, which result in an inflated or deflated model (Jarvis et al., 2003; MacKenzie et al., 2005). Measurement models are likely to be substantially inflated if the results indicate that paths emanating from a construct are mis-specified, thus leading to Type I errors. In contrast, measurement models are likely to be deflated if the paths leading into a construct are mis-specified, thus leading to Type II

<sup>32</sup> Type I and type II errors occur due to forcing quantitative analysis results, whether to reject or not to reject the null hypothesis according to predicted decisions (Hair et al., 2010; Rothman, 2010).



errors (Jarvis et al., 2003). The problem of model misspecifications are discussed in various domains, such as marketing research (Jarvis et al., 2003), leadership research (Podsakoff et al., 2003), operations and manufacturing management research (Roy and Tarafdar, 2012), as well as behavioural research (MacKenzie et al., 2005). Therefore, in this study, these attributes are carefully selected and defined for the purpose of model development in order to minimise the possibility of model misspecification.

The next process is to assess the overall quality of the model which can be achieved in two steps: (1) evaluation of the model measurement, and (2) evaluation of the structural model. The evaluation of the model measurement is also known as the outer model measurement, which relates latent constructs with their associated indicators. The evaluation of the structural model is also known as the inner model evaluation, which relates endogenous latent constructs with other latent constructs (Hair, Sarstedt et al., 2011). The formative and reflective models require different forms of assessment.

#### **(a) Reflective Measurement Model**

In assessing a reflective measurement model, construct reliability and construct validity are regarded as important elements. Construct reliability assessment focuses on the internal consistency reliability and indicator reliability, whereas construct validity relates to convergent validity and discriminant assessment (Hair, Sarstedt et al., 2011).

In assessing the internal consistency reliability, a composite reliability value between 0.70 to 0.90 is considered satisfactory, whereas less than 0.60 is regarded as indicating low reliability (Chin, 2010; Iacobucci and Duhachek, 2003; Nunnally and Bernstein, 1994). Internal consistency is considered acceptable when the value of composite reliability is between 0.60 and 0.70. There are two scenarios where the indicator can be considered for deletion: (1) loadings between 0.40 and 0.70, provided that the deletion can increase the value of composite reliability, and (2) loading lower than 0.40, which indicates very low loading (Hair, Ringle et al., 2011).

Construct validity is the extent to which the indicators of a construct, measure what they are purported to measure (Bagozzi and Yi, 2011). It focuses on convergent validity and discriminant validity assessments. An average variance extracted (AVE)

value of higher than 0.50 is considered to have a sufficient degree of convergent validity (Bagozzi and Yi, 2011; Chin, 2010; Hair, Ringle et al., 2011).

Discriminant validity postulates the extent to which a construct differs from other latent constructs (Hair, Ringle et al., 2011). Discriminant validity is assessed in two measures: (1) The Fornell-Larcker criterion, and (2) cross loadings. In the Fornell-Larcker criterion, the square root of the AVE value is compared with the correlations among the constructs. The AVE of each construct should be greater than the construct's highest squared correlation with any other construct, by at least 0.50 (Fornell and Larcker, 1981). Cross loadings are derived by correlating the component scores of each construct, including their assigned indicators, with all other construct indicators (Hair, Ringle et al., 2011). All of these measures are generated by the bootstrapping procedure in SmartPLS.

#### **(b) Formative Measurement Model**

The evaluation used in assessing reflective measurement cannot be applied to formative measurement due to the different nature of the construct. The indicators in reflective measurement are highly correlated with each other compared to formative measurement, which is represented by independent indicators. (Hair, Ringle et al., 2011). Thus, the statistical criteria to assess a model's quality are indicator weight, t-statistics and multicollinearity.

Hair, Ringle et al. (2011) suggests examining each indicator weight and loading, and using bootstrapping to assess their significance. If the indicator weight is significant<sup>33</sup>, keeping all indicators is empirically supported. Whereas, if both weight and loading are insignificant, retaining the indicators is not empirically supported; and therefore the theoretical relevance can be questioned. In this instance, it is recommended that the insignificant formative indicator is retained as long as the conceptual foundation can be justified (Henseler et al., 2009). It is important to note that removing formative indicators can adversely affect content validity (Bollen and Lennox, 1991) and damage the model (Diamantopoulos and Siguaw, 2006).

Another criteria in the assessment of formative model measurement is the variance inflation factor (VIF), which verifies that there is no redundancy due to a

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<sup>33</sup> t-value 1.65 (significance level at 10 percent); 1.96 (significance level at 5 percent); or 2.58 (significance level at 1 percent).

high level of multicollinearity between formative indicators forming the construct and causing an indicator to be non-significant (Hair, Ringle et al., 2011). This redundancy check is performed by calculating VIF to determine the degree of multicollinearity (Diamantopoulos and Winklhofer, 2001). If VIF is less than 5, it can indicate multicollinearity, whereas VIF higher than 5 indicates a potential multicollinearity problem, which implies that 80 percent of an indicator's variance is accounted for by the remaining formative indicators related to the same construct (Hair, Ringle et al., 2011). If there is a multicollinearity problem, Hair, Ringle et al. (2011) suggest the indicator be eliminated if VIF is 5 or higher, the indicator formative measurement model outer weight is not significantly different from zero and the remaining indicators sufficiently capture the domain of the construct under consideration. The higher the number of indicators in a formative constructs the more likely that one or more indicators have low or non-significant weight. Therefore, it is proposed that the indicators are grouped into two or more constructs that can be theoretically justified (Cenfetelli and Bassellier, 2009).

### **(c) Structural Model Evaluation**

The main purpose of a structural model evaluation is to test the model's predictive power and the stability of the estimates. Hair, Ringle et al. (2011) recommends the following four steps when evaluating a structural model: (1) applying the R<sup>2</sup> measures; (2) bootstrapping procedure; (3) blindfolding technique; and (4) heterogeneity. In addition, the global goodness-of-fit index is applied to assess the overall model fit.

The purpose of R<sup>2</sup> measures is to predict the power of the endogenous latent constructs. It also serves to examine the effective size and evaluate the predictor construct (independent variables), and whether the construct has a significant influence on the endogenous construct (dependent variable). A higher value of R<sup>2</sup> is an indication of greater influence/prediction on the target construct. Although there is no definite guideline for assessing R<sup>2</sup>, which can indicate a 'strong' or 'weak' construct in a structural model, the rule of thumb of 0.75 (substantial), 0.50 (moderate) and 0.25 (weak) as suggested by Hair, Ringle et al. (2011) can be applied.

The second step in the structural model evaluation is using the bootstrapping procedure. Bootstrapping procedure is used to assess the path coefficient significance.

Paths that show signs of being contrary to the hypothesised direction indicate that the hypothesis is not supported, whereas a significant path indicates that the hypothesis is supported (Hair, Ringle et al., 2011). This procedure involves creating  $n$  sample sets in order to obtain  $n$  estimates for each parameter in the model. Each sample is obtained by sampling with replacements from the original data set until the number of cases is identical to the original sample set. The suggested minimum number is 5000 and the number of cases should be equal to the number of observations in the original sample.

The third step in the structural model evaluation is applying the predictive sample reuse technique (Stone-Geisser's  $Q^2$ ), which can effectively be used as a criterion for predictive relevance (Chin, 2010; Geisser, 1974; Hair, Ringle et al., 2011; Stone, 1974). Based on the blindfolding technique,  $Q^2$  evaluates the prediction capabilities of the model through cross-validation redundancy measure for each construct, with a suggested  $d$  value between 5 and 10 (Chin, 2010; Hair, Ringle et al., 2011).  $Q^2$  larger than zero indicates that the exogenous constructs (dependent constructs) have predictive capabilities for the endogenous construct (independent construct) (Hair, Ringle et al., 2011). The rule of thumb indicates that a cross validated redundancy  $Q^2 > 0.5$  is regarded as a predictive model (Chin, 2010).

## **6.4 ETHICAL CONSIDERATIONS**

Research involving human participants is complex and can involve various legal, ethical, political and social issues, because a study may contain questions that are personal and sensitive in nature. Furthermore, various perspectives need to be considered when a study is conducted, including matters related to the anonymity of the respondents, data security and confidentiality, and any potential harm to the respondents that could lead to psychological stress, anxiety or other negative consequences.

This study has received favourable ethical opinion from the Nottingham University Business School Research Ethics Committee (refer to Appendix 4 for the approval correspondence). Therefore, in ensuring that the ethical standards are adhered to, this study follows the guidelines stipulated in the University of Nottingham's Code of Practice on Ethical Standards, and relevant academic and professional guidelines.

In addition, the research participants are made aware that, by profession, the researcher is a senior Customs officer at the Royal Malaysian Customs Department, at the time of study. A letter of support from the Royal Malaysian Customs Department (see Appendix 6) has been issued, seeking the co-operation of the Customs agents associations<sup>34</sup>, to participate in this research. It is highlighted that participation in the research is voluntary.

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<sup>34</sup> Selangor Freight Forwarding and Logistics Association (SFFLA); Penang Freight Forwarding Association (PFFA); and Johor Freight Forwarding Association (JOFFA). These three selected associations are the umbrella bodies for the Customs agents, as well as logistics and freight forwarders in Malaysia.

## **CHAPTER 7**

### **QUALITATIVE DATA COLLECTION AND CONCEPTUAL RESEARCH DEVELOPMENT**

The first part of this chapter presents the findings of the qualitative data collection (qualitative phase) from the interview sessions with Customs agents and representatives of the Customs agents associations (logistics and freight forwarders associations). The aim of the qualitative phase is to explore in depth the phenomenon of non-compliance in relation to Customs import declaration. The purpose is to support the development of the research model in relation to import tax compliance. The key outcome of this chapter is to present the import tax compliance behaviour model, which is developed based on the framework of TPB as discussed in Chapter 5. The remaining section of this chapter elaborates on the development of the research model, which forms the foundation to the survey research in the subsequent phase of this study.

#### **7.1 INTERVIEWS**

##### **7.1.1 Background of Respondents**

Eleven respondents were selected for the purpose of the interviews based on purposive sampling. The respondents consisted of eight Customs agents and three head of the Customs agents associations from three different geographical locations. The selection of respondents was based on two key criteria. Firstly, due to their number of years as Customs agents, they were potentially able to draw on a great variety of experiences. Secondly, the selection of Customs agents associations complemented the responses from the Customs agents associations provide an umbrella view of Customs agents with respect to issues of import tax compliance. In practical terms, they were an appropriate target group, capable of providing the information required for the purposes of this study.

**Table 7.1: Profile of Respondents**

<b>Respondents</b>	<b>Gender</b>	<b>Designation</b>	<b>Business Category</b>
R 1*	M	Managing Director	Private Limited Company
R 2*	M	Director (Operations)	Private Limited Company
R 3*	M	President	Business Association
R 4*	M	Senior Manager	Private Limited Company
R 5^	M	Director (Operations)	Private Limited Company
R 6^	M	Director	Private Limited Company
R 7^	M	Managing Director	Private Limited Company
R 8^	F	Senior Manager	Limited Company
R 9*	M	Vice-President	Business Association
R 10^	F	Executive Director	Private Limited Company
R 11*	M	President	Business Association

Note: \* Recorded interview  
^ Note taking

The respondents were contacted personally by telephone, requesting an interview session. The practitioner background of the researcher gave the advantage of being able to approach the respondents, and the willingness of all the respondents contacted to be interviewed. Details of the respondents are presented in Table 7.1.

### **7.1.2 Interview Sessions**

The interview sessions took place between the months of June and July 2012. All of the interviews were conducted by telephone, similar to the techniques applied in the initial interviews with Customs officials at the earlier stage of this study (see Section3). As well as being comparable in terms of quality of data to face to face interviews (Carr, 2001), telephone interviews were selected due to cost (Cachia and Millward, 2011; Opdenakker, 2006) and the interviewees being geographically disparate (Opdenakker, 2006; Sturges and Hanrahan, 2004).

Interview participants were initially contacted prior to the actual interview session to seek approval to participate in the interview. Participation in the interview

was on a voluntarily basis. The participant has no obligation, and had the right to refuse to participate in the interview. Out of eleven interviews, five participants chose the conversation not to be recorded. Thus, the gist of the discussion, important points and quotes from the interviews were recorded in the form of notes. At the start of the interview session the participants were reminded of the purpose of the interview. They were first asked about the latest general developments in Customs administration, rather than focusing on the core question. This was to allow participants to feel more relaxed during the conversation and allow them to talk more freely about the issues at hand (Burke and Miller, 2001). Subsequent question were asked about their opinion of the issues of businesses and their compliance with Customs law and regulations, specifically the declaration of import which affects the collection of revenue for the government. The questions posed were open-ended (refer to Appendix 5) in order to allow flexibility in the responses and allow the participants to talk freely about the subject matter.

The interviews were conducted in the local Malaysian language which is the official language used in daily communication in the public administration department in Malaysia. The interview sessions lasted approximately 15 to 20 minutes each. A voice recording device, as well as note taking, was used to capture the interview conversations. The interview conversations were later transcribed to facilitate further analysis and refine the research context.

## **7.2 DATA ANALYSIS AND FINDINGS**

### **7.2.1 Data Analysis**

The interview data were analysed manually, using Microsoft Excel software. This method of analysis was selected as opposed to QDAS (qualitative data analysis software) as the interview involved a small sample size, of eleven participants. A simple analysis was conducted, classifying the findings into a matrix table. For this purpose, the key findings or quotes from the interview transcripts were extracted and coded into the matrix table.

### **7.2.2 Interview Findings**

The eleven respondents who participated in the interviews provided numerous views on tax compliance. Their narrative responses were coded and categorised



according to the six constructs added to the TPB model and investigated in this study: law and law enforcement; knowledge; ethics; complexity of procedure; and exchange of fairness. Generally, most participants interviewed described agents as being in one of two groups: compliant or ignorant. The first group were those who view import tax as important and pay it accordingly. The second group were the risk-takers who see tax as a burden and try to avoid it or pay as little tax as possible through improper declaration. According to the respondents, this is the group that Customs should focus on. They should be penalised heavily as it is done intentionally. Their agents' licence should be revoked to warn them and other agents about the consequences of evading tax. It was interesting to see the similarities in their views on deterrence theory, in which increased punishment would increase compliance. They also expressed their views on various institutional issues and the important role of Customs administration that makes compliance easy or difficult. Their detailed responses were categorised according to the following dimensions.

**(a) Ethics and other influences in compliance decisions**

Ethics is one of the most important constructs in this study, as highlighted in Chapter 5. Ethical belief is a social behaviour pattern that may unconsciously or consciously be accepted as a norm in society. In relation to the understanding of ethics, participants were asked about the influence of importer and other agents that might have an influence on their decisions when filling import declarations. There were mixed reactions in their responses, as described in Table 7.2.

**Table 7.2: Evidence on Ethics, Importers and Other Agents**

Dimension	Evidence / Interpretation
Ethics	<ul style="list-style-type: none"> <li>• Possibility of under-declaration of tax</li> <li>• Competition and pressure to follow others in their unscrupulous practices</li> <li>• Belief that it is common practise for others to reduce tax for business survival</li> <li>• Feeling reprehensible by falsifying tax declaration</li> <li>• Morally wrong to be involved in unethical practices</li> </ul>
Influence of Importer and Other Agents	<ul style="list-style-type: none"> <li>• Obligation to fulfil client need to reduce tax burden versus complying with tax obligation</li> <li>• Competition and practices of other agents</li> </ul>

It was viewed that importers have a strong influence on agents' decisions in import declaration. Respondents R2, R7 and R5 stated:

*'We are being paid by the importer and as our client, we normally try to meet our client need, to be honest. I believe it goes the same with most agents' (R2)*

*'There are cases where the importer does not agree with the amount of tax calculated and if we can help them to reduce it' (R7)*

*'It's common in business, we try to save every penny and the same goes with the importer, always asking... can we pay slightly less tax?' (R5)*

When the participants were asked if they think that practices such as under-declaration are unethical, the majority of them acknowledged that they are unethical. They also suggest the possibility that agents are involved in assisting importers to under-declare tax, as claimed by respondent R6:

*'It's quite difficult to say... sometimes it is not the agents' intention to under-declare tax but the customer asking for a way that they can pay less... we do not want to have any issues and being blacklisted by Customs' (R6)*

Business survival and the influence of other agents on their business practices are also contributing factors to tax non-compliance, such as under-declaration, as stated by respondents R1 and R4:

*'We operate in a community where almost everyone knows each other quite well. There is a possibility that they under-declare the tax amount because of competition and seeing other agents doing the same thing' (R1)*

*'No doubt that some of the practices of the agents are seen as an unethical... but I think it's for business survival purpose' (R4)*

This is a social behaviour pattern that may be accepted as the norm in business practices, as reflected in the statements by respondents R9 and R1. Other agents might be influenced by unethical practices regardless of their religious belief that cheating is morally wrong, as commented on by respondent R11:

*'The percentage of tax evaders may represent a small percentage about 10% to 15%... but the effect is to other agents who feel that this is an unfair practise... other agents might follow the bad practices to sustain in the business' (R9)*

*'It's the objective of a business establishment to be profitable but not through illegal practices... this is certainly wrong... even any religious teaching doesn't allow to cheat others' (R11)*

**(b) Law and law enforcement**

Law and law enforcement are two of the essential elements investigated in this study in order to understand their relationship with compliance. The respondents were asked if the law, and enforcement of the law by Customs, are adequate in prevention of tax evasion and increasing compliance among agents and the business community. Table 7.3 shows their views about these two determinants of tax compliance.

**Table 7.3: Evidence on Law and Law Enforcement**

Dimension	Evidence / Interpretation
Perception of Law	<ul style="list-style-type: none"> <li>• Sufficient provision in Customs law</li> <li>• High penalty for tax under-declaration</li> <li>• Lack of effective implementation of Customs law</li> <li>• Heavy punishment by imprisonment for tax evaders</li> <li>• Suspension of agents' licenses in tax evasion cases</li> </ul>
Perception of Law Enforcement	<ul style="list-style-type: none"> <li>• Increasing enforcement activity</li> <li>• More shipments being detained and inspected</li> <li>• Lack of prosecution cases</li> <li>• The risk of getting caught for evading tax is higher</li> <li>• Increased audit probability</li> </ul>

It was generally viewed that Customs have increased their enforcement efforts. Respondent R8 stated:

*'I noticed that Customs is quite strict now... there are quite a number of our shipments were being held by the enforcement' (R8)*

Respondents R1 and R6 concur that their goods were inspected regularly. They also expressed their concern that this has impacted their businesses, as it may increase the cost of doing business. Respondent R6 added that this also creates redundancy in the

inspection process which may further delay clearance:

*'We normally clear the same type of goods for our client and we pay high tax... and yet the shipment being inspect regularly' (R1)*

*'Customs has increased the enforcement activity... enforcement officer always detained our goods... officer from scanner unit also frequently stopped our goods... and also the officer at the gate always stopped and checked our goods. It's difficult to do business nowadays' (R6)*

Respondent R3 acknowledged that Customs have the authority to inspect goods. However, according to R3 there are certain conditions under the World Trade Organization (WTO) multi-lateral agreement that Customs administration has to fulfil in selecting cargoes for inspection:

*'I understand that according to WTO rule Customs can't stop too many shipments... they have to release first... if there are problems the audit team can come and check' (R3)*

The respondents also took the view that there are sufficient provisions in the law and high penalties for non-compliance with the law. However, the penalisation added an extra burden if their customer didn't want to take full responsibility for the payment of the penalty. In general, they were concerned about maintaining a good reputation with their customers and remained compliant with Customs law. Respondents R2, R5, R9 and R10 stated:

*'The provision in the law is sufficient but if the enforcement activity is too heavy and many of the container being detained, it will impact on us because our customers will complain because they want their goods as quick as possible' (R10)*

*'There are agents who are not afraid to make mistakes because they rent the license from other agents... they are the culprit who evade tax... it's a risk to the agents who rent their license to others... their license can be revoked' (R9)*

*'We want to maintain our good reputation... we don't want to take any risk of cheating Customs... the penalty and offences on tax evasion is quite hefty' (R5)*

*'We already pay tax higher than previous year... officer also very strict... we might be penalised we declare wrongly... sometimes it's not our fault but our customer but the customer didn't want to pay the penalty' (R2)*

Interestingly, Respondent R11 questioned whether the law was seriously implemented:

*‘There are provisions in the Customs Act about imprisonment but are there any agents have been charged to the court and being sent to prison because of offences on tax evasion? I have never heard of any cases yet’ (R11)*

### (c) Knowledge

As discussed in Chapter 5, previous studies in direct tax compliance and other inter-disciplinary studies have demonstrated the importance of knowledge in improving tax compliance. In understanding knowledge as a determinant of tax compliance, the respondents were asked about the importance of knowledge and how it relates to improving compliance. Their responses are depicted in Table 7.4.

**Table 7.4: Evidence on Knowledge**

Dimension	Evidence / Interpretation
Knowledge	<ul style="list-style-type: none"> <li>• Knowledge acquired through training and seminars</li> <li>• Understanding latest developments and updates to comply with Customs requirements, seeking information and clarification directly through face to face channels</li> <li>• Knowledge exchange from agents to Customs</li> <li>• Usefulness of knowledge for the agents’ daily operation</li> </ul>

It was acknowledged by the respondents that knowledge is an important factor that could improve compliance. Respondents R4, R5, R8 and R11 stated:

*‘Knowledge is important if we want to increase compliance... but we also must get the proper guidance from Customs... for example the agen courses do help us to get the knowledge about Customs regulation and the offences under the Customs act’ (R11)*

*‘It is good if there’s a frequent seminar or training to explain to us on any new procedure... we also sometimes didn’t get the information on any changes of procedure... if not, different officer might officer may say differently’ (R5)*

*‘I have noticed that Customs has conducted seminar and training for agents and importers... this is good for us’ (R4)*

*‘We need to have the updated information about Customs... training and seminar to helps us to understand new development or requirements for us to comply’ (R8)*

Respondents R1 and R7 reiterated that other than training and seminars, as mentioned by R4, R5 and R8, they update themselves through direct communication with Customs rather than outdated information from websites, as stated by respondent R9:

*‘Sometimes we just ask our staff who handle the declaration matters to ask Customs for any new updates because they are always there is Customs office’ (R1)*

*‘We like to see the officer and get the latest updates... it is more faster to do this way’ (R7)*

*‘We want to get the new updates and information from Customs but sometimes it’s a bit difficult to get the information and get the latest update from Customs... take for example in the website... not much information updated in the website’ (R9)*

Interestingly, as shared by respondent R2, in the quest for knowledge acquisition, Customs officers also update themselves from the agents:

*‘Sometimes Customs also ask information and learn from us because there is a lot of junior officer who is not familiar with the process at the port’ (R2)*

#### **(d) Tax Assessment Service Quality**

The importance of service quality in public service delivery is examined to understand the relationship of tax assessment service quality and import tax compliance, whether it is difficult or easy to comply with Customs law. Table 7.5 provides a snapshot of the participants’ responses.

**Table 7.5: Evidence on Tax Assessment Service Quality**

Dimension	Evidence / Interpretation
Perception of Tax Assessment Service Quality	<ul style="list-style-type: none"> <li>• Front line staff handling the assessment on Customs import declarations are incompetent</li> <li>• Lack of knowledge and experience of tax assessment</li> <li>• Too slow in processing the Customs import declaration</li> <li>• Inefficient in the assessment of Customs declaration</li> <li>• Not delivering the service as stated in the client charter</li> <li>• Inconsistency in the assessment of Customs declarations</li> </ul>

Participants responded that the Customs department has to look into their daily operation to improve the quality of their front line services in order to increase compliance among Customs agents. It was thought that front line staffs handling the assessment of Customs import declarations were incompetent, inefficient and not knowledgeable. Respondents R6, R7, R8 and R11 stated:

*'The same product that we declare are being valued differently by different officers'*  
(R6)

*'You know lady officer... they seems to have a lack of confidence to approve the declaration... they ask too many questions'* (R7)

*'Different officer provide the different advise to us... how can we comply to Customs'*  
(R8)

*'They are many new officers who lack experience and don't even know how to classify goods according to Customs tariff classifications'* (R11)

Respondents R3 and R9 share their views that Customs should not place junior or inexperienced officers as front line officers in the assessment of Customs import declarations.

*'I think that there shouldn't be too many junior officer to do the assessment... they are inexperienced'* (R3)

*'There're many junior officers doing the assessment... and they do not have enough knowledge to do assessment'* (R9)

Respondents R1, R4 and R10 concurred, stating that this results in delays by Customs in processing Customs import declarations. Respondent R1 compared this with faster tax assessment service previously, when more experienced senior officers of Customs were placed as tax assessment officers.

*'If Customs want agents to comply with their requirement, Customs must also comply with the client charter. If they promise that the assessment process is within 30mins, please deliver within the set time frame'* (R4)

*'A lot of lady officers now at export....they are too careful and very slow in doing the assessment'* (R5)

*'We thought that we can get fast approval but yet there are a lot of queries... it is a usual good that our client import' (R10)*

*'Previously there are many experienced senior officers at import and export... clearance was fast... but many of them have been transferred now' (R1)*

Respondent R2 further questioned the ambition of Customs to be world class Customs administration with the reality of delays of Customs clearance.

*'How can Customs become world class if there's always delay in the clearance?' (R2)*

#### **(e) Exchange of Fairness**

Exchange of fairness in this study describes the willingness to comply with import tax payment in return for the benefits received from the government. The government policies on tax spending may influence taxpayers' behaviour to comply or not to comply with custom law. High perception of fairness in the exchange of government spending yields a high level of compliance. To understand further the relationship between exchange of fairness and tax compliance, respondents were asked about their views on agents who under-declare their tax and whether their decisions are influenced by the government tax spending policies. The responses are displayed in Table 7.6.

**Table 7.6: Evidence on Exchange of Fairness**

Dimension	Evidence / Interpretation
Perception of Exchange of Fairness	<ul style="list-style-type: none"> <li>• Deteriorating trust in the government on tax spending</li> <li>• Tax revenue spent by the government for election</li> <li>• Importance of tax revenue for development</li> <li>• Sense of patriotism for the country</li> <li>• No upgrading of public infrastructure</li> <li>• Impact of tax revenue for social healthcare</li> <li>• No direct impact of government spending to logistics and business community</li> </ul>

It was mentioned by the respondents that there are agents who under-declare tax. This could be solely for their financial gain or due to deteriorating trust in the government



of how the tax is being spent, while they do feel the direct impact of the government spending for development purposes. Respondents R2, R7 and R10 stated:

*'I didn't see the direct benefit of the tax paid... and yet we still have to pay for toll and road tax... and the increases from year to year' (R2)*

*'I just wonder how the government spend all the tax that we have paid because there haven't been any upgrade on this two-lane road that linked to the... port' (R7)*

*'I'm sure all the tax paid will be spent mostly for this coming election' (R10)*

The responses above indicate that there were negative perceptions of how the government spent the tax paid, especially in the heat of the country's up-coming general election, where the issue of tax was quite sensitive. However, there were also positive views about under-declaration of tax. For example, respondents R1, R3, R9 and R11 viewed it in the opposite way:

*'We must have the spirit of patriotism for the country. Those who try to evade tax are not patriotic and show no sign of caring about our country' (R1)*

*'I think it's not fair if everybody try to evade tax... that it is not good for the economy.. where the government want to get the money? (R3)*

*Evading tax not a good move... sometimes people didn't realise what the government have spent for the people... for example the Government subsidise a lot for health care' (R9)*

*'There are some out there who do not have the awareness about the important of tax for development. These are the ignorant category who just thinks about themselves' (R11)*

#### **(f) Complexity of Procedure**

Complexity of procedure, which is associated with the term tax complexity, as discussed in Chapter 5, is one of the essential constructs in this study. The majority of the respondents talked about the import declaration procedure which makes it difficult to comply. Table 7.7 provides some evidence of the participants' responses.

**Table 7.7: Evidence on Complexity of Procedure**

Dimension	Evidence / Interpretation
Complexity of Procedure	<ul style="list-style-type: none"><li>• Import declaration procedure too rigid</li><li>• Too frequent changes in the procedure</li><li>• Procedure difficult to adhere to</li><li>• No flexibility in the procedure</li><li>• Excessive documentation</li><li>• Too many requirements</li><li>• No uniformity in the procedure</li><li>• Cumbersome standards of practice</li></ul>

The majority of the respondents had a negative perception of the Customs import declaration procedure. Respondents R9 and R10 viewed frequent changes in the Customs requirements as making them difficult to comply with:

*‘Customs procedure is difficult to understand. The requirements are changing constantly’  
(R9)*

*‘There is always a new procedure introduced when there’s a changes of officer... this is difficult for us to follow’ (R10)*

Respondents R3 and R6 expressed the view that excessive documentation and requirements add to the exiting complexity of the procedure. They expressed their experience as:

*‘Import declarations are now paperless, but Customs still requires us to produce paper invoice, bill of lading, packing list and so on.’ (R3)*

*‘I just didn’t understand why Customs requires us to provide the original documents...copy of invoice are not accepted’ (R6)*

In addition, Respondents R2, R4, R8 and R11 shared their experience that there was no flexibility or uniformity in the procedure between various states and ports. They also added that cumbersome standards of practice and inflexibility of the procedures worsened the situation:

*'Customs has tightened the procedure... our goods always being required for examination... it is difficult to do business nowadays' (R2)*

*'It is the usual goods that I cleared for my client... but nowadays Customs always ask for the goods to be examined' (R4)*

*'There's no uniformity in the procedure between ports within the same states...' (R8)*

*'I found that Customs at different port have different requirements and procedure... this is a bit complicated for the agents to understand the requirements' (R11)*

### **7.2.3 Overall Results**

Nine major import tax compliance determinants have been identified from the interviews: ethics, influence of importer, influence of other agents, law, law enforcement, knowledge, tax assessment service quality, exchange of fairness and complexity of procedure.

As highlighted in Chapter 5, ethics has a strong influence on agents' compliance decisions. There is a possibility that the agents may be involved in unethical practices. It demonstrates a low level of compliance, if unethical social behaviour is accepted as the norm. On the other hand, the respondents also acknowledge that it is morally wrong to be involved in unethical practises such as evading tax. The interview findings identify two dimensions of subjective norms: importers and other agents, which are also found to have an influence on agents' compliance decisions. This shows that the decisions to comply or not to comply are influenced by external factors such as the practices of other agents and pressure from clients. Therefore the findings support that ethics, importers and other agents serve an important function in influencing compliance behaviour.

Consistent with the discussion in the literature review (Chapter 5), law and law enforcement are also identified as important variables that influence compliance behaviour. In general, it is perceived that provision in law such as high penalties and suspension of licences are adequate to deter tax evaders. Furthermore, an increase in enforcement activity may increase the level of compliance as the risk of getting caught is higher. It is shown that law and the role of enforcement is effective in deterring the agents from non-compliance.

Knowledge plays an important role in Customs agents' compliance, because most importers are very reliant on Customs agents to manage their tax compliance activities. The respondents acknowledge that continuous training and guidance from Customs may facilitate the compliance process because they could better understand the compliance requirements. Therefore, the relationship between knowledge and compliance is consistent with the discussion in Chapter 5, as knowledge is an important tool in the voluntary compliance mechanism.

Tax assessment service quality is another variable identified as influencing Customs agents' compliance behaviour. The findings reveal that several characteristics of tax assessment service quality such as staff competency, efficiency and processing time are important dimensions that make compliance easy or difficult. This finding indicates that the concept of service quality is not only important in the private sector, but also relevant in the context of the public sector, as discussed in Chapter 5.

Exchange of fairness serves as an important determinant of tax compliance. Generally, the finding revealed that the government's tax spending policies such as on public infrastructure, social healthcare or other benefits for the business community impact upon decisions to comply or not to comply with tax payment.

Finally, the complexity of the procedure is identified as a determinant of Customs agents' compliance. It is evidenced that a more complex Customs procedure may result in lower compliance levels. Several indications related to complexity that are found to be important are the rigidity of the procedure, frequent changes, flexibility, excessive documentation requirements, cumbersome practices and uniformity related to Customs procedures. Less complex procedures may facilitate and improve compliance levels. This finding indicates that there is consistency with the discussion highlighted in Chapter 5, that complexity in a tax system is one of the obstacles to tax compliance.

## **7.3 HYPOTHESIS DEVELOPMENT**

This section is informed by the literature discussed in Chapter 5 and the interview findings in the preceding section. It includes various determinants of tax compliance, including the TPB constructs. The purpose of this section is to elaborate on the development of the research model (compliance behaviour model - CBM) of import tax within the framework of the Theory of Planned Behaviour (TPB). The research model is extended by the inclusion of several other key constructs, as discussed in Chapter 5 Section 5.3, namely law, law enforcement, knowledge, ethics, complexity of procedure, tax assessment service quality, and exchange of fairness. The conceptual framework of import tax compliance behaviour model<sup>35</sup> is developed through 18 hypotheses, which are discussed in the reminder of this section.

### **7.3.1 Influence of Behavioural Intention**

TPB clarifies that intention is the most influential factor on behaviour. Behavioural intention is also an immediate antecedent and mediator of attitudes and social influences on behaviour (Ajzen, 2005). As highlighted in Chapter 5, empirical evidence in various fields of study supports the positive relationship between intention and behaviour (for example Bruijn and Kremers, 2007; Elliott et al., 2003; Godin and Kok, 1996; Saad, 2010; Trivedi et al., 2005). However, in tax compliance studies, the full potential of TPB as a complete model for examining the relationship between intention and behaviour is less explored. In fact, there are only a few studies that look into the role of intention as a mediator of behavioural factors, such as those by Trivedi et al. (2005) and Saad (2010). Intention is an important component of tax compliance, as revenue can only be collected accordingly, through the willing participation of taxpayers (Langham et al., 2012). Thus, predicting taxpayer intention to comply is as important as predicting actual compliance behaviour.

Therefore, this study expects that intention would be the most appropriate measure for determining importers' behaviour regarding paying import tax, and acts as a mediator between attitudes, subjective norms and perceived behavioural control, and import tax compliance behaviour. The prediction is that a positive intention to

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<sup>35</sup> Refer to Section 7.4

comply with Customs tax law will positively influence tax compliance behaviour. This prediction is reflected in the following hypothesis:

***Hypothesis 1: Agents' behavioural intention to comply influences their tax compliance behaviour.***

### **7.3.2 Influence of Attitude**

As suggested by Ajzen, (1991), attitude plays an important role in influencing human behaviour. Attitude is believed to have a direct impact on behavioural intention because it is a key element in decision making, which can influence intention by increasing the motivation to engage in a particular behaviour (Ajzen and Fishbein, 1980; Ajzen, 2005). The behavioural outcome (favourable or unfavourable) will determine an individual's decision whether to comply (or not to comply) with tax obligations. Compliance behaviour toward the Customs law depends on a positive attitude of members of the public to tax and its legal institutions. A positive attitude based on guilt feelings, civic duty and moral obligation, referred to as tax morale, has a significant influence on tax compliance behaviour (Cummings et al., 2009; Hanno and Violette, 1996; Eric Kirchler, 2007; Torgler, 2011).

The significant role of attitude in behavioural intention has been explained in previous studies, in various disciplines (such as Bobek and Hatfield, 2003; Ross, Kohler, Grimley and Anderson-Lewis, 2007; Taylor and Todd, 1995; Trivedi et al., 2005). A recent study in indirect taxation by Bidin et al. (2011) also demonstrates that there is a significant correlation between attitude and intention towards local sales tax compliance. Studies in the area of tax compliance by several researchers highlight the important variables influencing the attitude towards tax compliance. Thus, attitudes toward import tax are expected to have a significant positive relationship with the intention to pay import tax. The prediction is that Customs agents with a positive attitude are more likely to develop strong intention to comply with tax obligations. This prediction is stated in the following hypothesis:

***Hypothesis 2: Attitude of agents towards tax compliance significantly influences their tax compliance intention.***

### **7.3.3 Influence of Subjective Norm**

TPB predicts that subjective norm will influence individual's intention to perform specific behaviours (Ajzen, 1991). In the context of tax compliance, the important referent groups have a positive or negative influence on decisions to comply (or not to comply) with tax obligations.

Previous studies on tax compliance demonstrate that subjective norms play an important role in influencing behavioural intention (Bobek and Hatfield, 2003; Bobek, et al., 2007; Hanno and Violette, 1996; Trivedi et al., 2005). In other disciplines of research such as information technology and marketing, a positive and significant influence of subjective norms on behavioural intentions has been discovered (Bonne, , Bergeaud-Blackler and Verbeke, 2007; Pavlou and Fygenson, 2006; Taylor and Todd, 1995).

The influence of referent groups does not only have a significantly impact on behavioural intention as evidenced in previous studies, it also impacts ethics (Blanthorne and Kaplan, 2008; Chau, 2009; Wenzel, 2005). Different referent groups and ethical beliefs give different levels of motivation towards tax compliance (Chau, 2009). Tax payers' ethical beliefs, which are influenced by their close referent groups, might deter them from engaging in tax evasion activities (Blanthorne and Kaplan, 2008). In an import tax environment, the influence of reference groups is anticipated to have a strong influence on the agents' behavioural intentions to pay import tax through their ethical beliefs. The interview findings in Section 7.2.2(a) support this proposition, that agents' compliance decisions are associated with the influence of referent groups on their ethical beliefs towards compliance. The influence of referent groups on unethical practices, such as tax evasion, is that they may be perceived as the right thing to do and accepted as a norm by some agents for their business continuity (Respondents R1, R2, R4 and R5). According to respondent R9, although the figure accounts for about 10% to 15%, these unfair practices have negative consequences that might affect other agents' compliance levels.

Researchers, including Ajzen and Fishbein (1980), measure subjective norm with various reference groups, indicating that a deconstruction must be made because the views or opinions of individuals in the reference group may vary. Based on empirical evidence, subjective norms were found to have more than one dimension or group. There are researchers who divide reference groups into two, giving a primary

subjective norm and a secondary subjective norm (Bidin et al., 2011; Chu and Wu, 2004; Taylor and Todd, 1995).

Following the suggestions of Chu and Wu (2004) and Taylor and Todd (1995), the study of indirect taxation focusing on local sales tax is categorised into primary and secondary subjective norm (Bidin et al., 2011). According to Bidin et al. (2011), the basis of the separation into these two categories is due to the presence of more than one reference group: tax agent as the primary subjective norm, and colleagues in other companies responsible for managing sales tax affairs as the secondary subjective norm. Tax literature demonstrates the role of a third party in the primary referent group such as tax preparers or account preparers in influencing the taxpayers by manipulating them into non-compliance decisions (Hai and See, 2011a, 2011b; Klepper, Mazur and Nagin, 1991).

In an import tax environment, the role of agents as an interface between importers and Customs administration is prominent. Due to complex Customs and port procedures in the clearance of goods at borders, importers often rely on expertise and advice from a third party such as a Customs agent. Similarly, there is the possibility of other influences, such as the influence of a client (importer) that could influence agents' compliance decisions. Conversely, it is possible that agents are influenced by each other, making them declare less tax. The interview findings in the preceding section suggest that decisions to comply or not to comply are influenced by external factors such as the practices of other agents and pressure from clients (importers). It is acknowledged that importers have a strong influence on the Customs agents' approach to the completion of import declarations, since they are paid by the importer to lodge the import declarations (R2, R5 and R7). In addition, it is mentioned by the respondents that there is a possibility that Customs agents might be influenced by each other due to business competition, leading to declarations to pay less tax (R1 and R4). Thus, based on the described scenario, and as suggested by Bidin et al. (2011), Chu and Wu (2004) and Taylor and Todd (1995), it is reasonable to separate subjective norm into two groups the primary group (importers) and the secondary group (other agents). These two referent groups are found to have a significant influence on agents' compliance decisions directly, and through their ethical beliefs.



In summary, tax compliance literature, other disciplines of research and the interview findings all support the role of referent groups or subjective norms in behaviour. To investigate these relationships, the following proposed hypotheses are tested:

***Hypothesis 3a: Agents' primary referent group (importers) positively influence their tax compliance intention.***

***Hypothesis 3b: Agents' primary referent group (importers) positively influence their ethical beliefs towards tax compliance intention.***

***Hypothesis 4a: Agents' secondary referent group (other agents) positively influence their tax compliance intention.***

***Hypothesis 4b: Agents' secondary referent group (other agents) positively influence their ethical beliefs towards tax compliance intention.***

#### **7.3.4 Influence of Perceived Behavioural Control**

The perceived behavioural control (PBC) variables are the key variables that play an important role in influencing behavioural intentions in the theory of planned behaviour (TPB). TPB posits that a particular behaviour can be predicted by an individual's PBC, which refers to the controllability and perception of the ease (or difficulty) of performing (or avoiding) a particular behaviour (Ajzen, 1991). Ajzen (1991) asserted that individuals with high PBC have a higher tendency to perform a behaviour compared to individuals with lower perceived behavioural control.

This study investigates the influence of PBC on tax obligations, referring to the behaviour in the declaration of taxable imported goods in the presence of the two factors, controllability and self-efficacy. This is operationalised as the constraints, such as financial constraints and the presence of opportunity to evade, which determine the behaviour to report correctly in the import declaration. If the agents perceive that there are greater opportunities, and anticipate fewer obstacles and impediments, they can understate tax in the import declaration. On the other hand, if the agents perceive that there are less opportunities and higher obstacles, which hinder them from understating tax in the import declaration, they are more likely to comply

with tax law. Thus, perceived behavioural control of agents toward import tax is expected to have a significant relationship with the intention, and behaviour, to comply with tax law. This prediction is stated formally in the following two hypotheses which are proposed to test the relationships between PBC and behavioural intention, and between PBC and behaviour:

***Hypothesis 5a: Agents' perceived behavioural control significantly influences their tax compliance intention.***

***Hypothesis 5b: Agents' perceived behavioural control significantly influences their tax compliance behaviour.***

### **7.3.5 Law and Enforcement**

The literature provides evidence that law and enforcement through penalties and other means of legal punishment influence the level of tax compliance. Several studies have identified that law and enforcement are directly associated with tax compliance behaviour (Allingham and Sandmo, 1972; Devos, 2012; Feld and Frey, 2007; Trivedi et al., 2005). However, the majority of studies discussed are on direct taxation and indirect tax is less explored. Accordingly, this study expects that the Customs laws and Customs enforcement affect import tax compliance intentions in line with TPB prediction, where behavioural intention acts as an intermediary to actual behaviour.

Consistent with direct tax literature, as discussed, the interview findings in Section 7.2.2(b) suggest that law and enforcement are two important determinants for import tax compliance. Sanctions such as penalties and imprisonment are among the positive elements in Customs law provision that make the business community remain compliant (Respondents R2, R5, R9, R10 and R11). In addition, as mentioned by Respondents R1, R6 and R8, Customs has increased their enforcement efforts, with more goods inspected regularly. This may deter tax evaders and increase compliance levels as the probability of getting caught by the Customs is higher.

Based on the discussion, the prediction in this study is that a favourable perception of the Customs administration, related to law and enforcement of law, is

likely to increase behavioural intention and compliance behaviour. A positive perception of law and enforcement increases the agents' intention to comply with tax obligations. Conversely, a negative perception leads to a decrease in the intention to comply. The proposed hypotheses attempt to test the relationship between favourable (or unfavourable) perceptions of law and law enforcement and intentions, and behaviour. The predictions are formally stated in the following two hypotheses:

***Hypothesis 6a: Perception of law positively influences agents' tax compliance intention.***

***Hypothesis 6b: Perception of law positively influences agents' tax compliance behaviour.***

***Hypothesis 7a: Perception of law enforcement positively influences agents' tax compliance intention.***

***Hypothesis 7b: Perception of law enforcement positively influences agents' tax compliance behaviour.***

### **7.3.6 Influence of Knowledge**

Knowledge is expected to influence the behaviour of agents toward import tax compliance. Tax compliance studies conducted by researchers find a positive relationship between knowledge of the legal taxation system and tax compliance behaviour (Palil, 2010; Eriksen and Fallan, 1996; Schisler, 1995). This study predicts that Customs agents are more compliant if they have a better understanding of custom law. A positive knowledge of tax law increases their understanding and the consequences of unethical reporting of duties and taxes. Conversely, without knowledge and understanding of the Customs law, they are less likely to comply with tax obligations.

This is acknowledged by the respondents in the interview finding that knowledge is an important factor for improving compliance (Respondents R4, R5, R8 and R11). In these instances, the respondents mention that they acquire their knowledge through various means such as training, direct consultation and websites. According to the respondents, continuous training and guidance from Customs are

helpful to them to understand compliance requirements. Therefore, similar to direct tax literature, and as discussed in Chapter 5, the role of knowledge in the context of import tax is also essential for improving compliance.

Consistent with the theory of planned behaviour that emphasises the role of intention, the proposed hypothesis attempts to test the relationship between knowledge and the behavioural intention of Customs agents on tax compliance. The prediction is formally stated in the following hypothesis:

***Hypothesis 8: Agents' level of knowledge significantly influences their tax compliance intention.***

### **7.3.7 Influence of Ethics**

Ethics serves an important function in influencing individuals' behaviour, as discussed in Chapter 5. However, the role of ethics in influencing intention and decision to comply, in tax compliance studies is largely under-explored, especially within the context of business taxpayers and indirect taxation (Chau, 2009). Unlike in other fields of study such as consumer purchasing intention (Carrington et al., 2010; Vermeir and Verbeke, 2008), few tax compliance studies have attempted to investigate the role of ethics with behavioural intention. These include studies of individual taxpayers (Bobek and Hatfield, 2003; Bobek, 1997) and business taxpayers (Bidin et al., 2011).

The results of interviews in the qualitative phase of this study suggest that ethics has a strong influence on agents' behaviour towards compliance. As discussed in Section 7.2.2(a), the respondents view compliance decision as influenced by the ethical belief that illegal practices such as tax evasion and tax under-declaration may be accepted as the norm in business, or be morally wrong (Respondent R2, R5, R7). Respondents R4 and R6 added that, generally they have the intention to comply with Customs requirements and acknowledge that under-declaration is an unethical practice.

Therefore, this study predicts that Customs agents who hold high ethical beliefs are likely to have a stronger intention to comply with tax obligations. Conversely, Customs agents who hold lower ethical beliefs are likely to have lower intention to comply with tax obligations. There is empirical evidence to suggest that

ethical belief may have a significant role in attitude to taxpayer compliance (Ho and Wong, 2008, 2009; Torgler and Schneider, 2007). Therefore, attitude towards ethical belief is expected to influence Customs agent intention to comply with tax obligations. The proposed hypotheses attempt to test the relationship between ethics and behavioural intention and between attitude and ethics towards tax compliance intention. The predictions are formally stated in the following hypotheses:

***Hypothesis 9a: Ethical belief of agents towards tax compliance significantly influences their tax compliance intention.***

***Hypothesis 9b: Ethical belief of agents towards tax compliance significantly influences their attitude to tax compliance intention.***

### **7.3.8 Complexity of Procedure**

Complexity serves as an important factor in influencing compliance. While some studies have argued that there is a relationship between tax complexity and compliance (Chan et al., 2000; Chau, 2009; Fischer, Wartick and Mark, 1992; Forest and Sheffrin, 2002; McKerchar, 2007; Richardson, 2006; Saad, 2010), little is known about the effects of procedural complexity on taxpayers' compliance decisions. Although there has been an early attempt to investigate these relationships through a study by Cox and Eger (2006), the findings need to be substantiated further in other contexts, such as this study. As discussed in Chapter 5, the current research direction of investigating tax complexity focuses on causes of complexity such as ambiguity, calculations, changes, details, forms, record-keeping and low levels of readability (Cox and Eger, 2006; Kirchler et al., 2006; Krause, 2000; Hanefah, 1996; McKerchar, 2001; Saad, 2014). This implies the need to investigate whether or not complexity in Customs procedures has an effect on agents' compliance decisions. Further investigation of this relationship could enhance the understanding of whether the procedure, which refers to the process or steps in the tax system, facilitates or adds to the complexity of compliance decisions.

The interview findings in Section 7.2.2(f) support the discussion highlighted in Chapter 5, that complexity in a tax system is one of the obstacles to tax compliance. Generally, there are negative perceptions of complexity of procedure. Customs procedure is perceived as complex, making compliance difficult. Several indications

expressed by the respondents relate to complexity about the rigidity, frequent changes, flexibility issue, excessive documentation requirements, cumbersome practices and uniformity issue related to Customs procedures (Respondent R2, R4, R8, R9, R10 and R11). This initial investigation provides some indication that complexity in Customs procedures has an adverse effect on agents' compliance decisions.

This study is expected to answer and broaden the understanding of tax compliance and provide some insight into the complexity of procedures in the indirect tax domain. Therefore, this study predicts that the complexity of Customs procedures makes compliance more difficult. The proposed hypothesis attempts to test the relationship between complexity of procedure and tax compliance intention. The prediction is formally stated in the following hypothesis:

***Hypothesis 10: Perception of procedure complexity negatively influences agents' tax compliance intentions.***

### **7.3.9 Tax Assessment Service Quality**

Satisfying customers is a core business challenge which has attracted considerable research attention. Service quality in this context is recognised as a driver of customer satisfaction, which induces behaviour. Previous studies on service quality find a positive relation between service quality and behaviour (for example: Chen and Kao, 2010; Cronin and Taylor, 1992; Nam et al., 2011).

As recognised, and dominating service marketing literature, the concept of service quality has gained increased attention in public administration. However, as discussed in Chapter 5, only a few pieces of tax literature attempt to explore the concept of service quality in the context of tax administration (Mansor, 2010; Oats et al., 2008). It is expected that the quality of interactions between indirect tax administration staff and taxpayers improves taxpayers' satisfaction, hence improving compliance.

The initial findings from the qualitative phase of this study suggest that tax assessment service quality has a strong influence on agents' behaviour towards compliance. The findings reveal that several characteristics of tax assessment service quality such as staff competency, efficiency and processing time are important

dimensions that make compliance easy or difficult. Specifically, the respondents indicate that the Customs administration should look into its daily operations to improve the quality of front line services with a view to improving compliance among Customs agents. It is felt that front line staffs that assess Customs import declarations are often incompetent, inefficient, lack knowledge and are too slow in processing Customs import declarations (Respondents R2, R4, R5, R6, R7, R8, R9, R10 and R11). Generally, this finding indicates a negative perception of tax assessment service quality by the Customs administration.

Consistent with the above discussion, this study predicts a negative perception of tax assessment service likely results in lower compliance among Customs agents. Conversely a positive perception positively influences agents' behaviour towards import tax compliance. The proposed hypothesis attempts to test the relationship between tax assessment service quality and tax compliance intention. The predictions are formally stated in the following hypothesis:

***Hypothesis 11: Perception of quality of tax assessment service negatively influences agents' tax compliance intentions.***

#### **7.3.10 Exchange of Fairness**

Exchange of fairness, a concept that derives from the domain of tax fairness, is an important factor that influences tax compliance decisions. This is supported by previous studies which focus on personal tax payers in a direct tax context. The perception of fairness in tax payment in exchange for government spending, as discussed in Chapter 5, may influence taxpayers' compliance decisions to comply or not comply with tax payment. Taxpayers have a fair perception of the tax system if the benefits received from government spending policies are equitable compared to their tax contribution. Although there is a growing amount of literature that focuses on tax fairness (for example Bobek, 1997; Harris, 1989; Saad, 2010; Tan and Chin, 2000), little evidence can be linked to the understanding of exchange of fairness, especially in the context of indirect tax such as import tax.

As asserted by Andreoni et al. (1998), fairness is the most relevant psychological element in tax compliance. Therefore, it is anticipated that the concept of exchange of fairness in import tax is an important psychological determinant of tax compliance decisions. Since tax payments for various tax regimes such as individual tax, value-added tax (VAT) or import tax are channelled to the government, the correct amount of tax payment through tax declaration might be influenced, or judged, by government spending policies, for instance building hospitals, public schools, free motorways, or allocation of price subsidies.

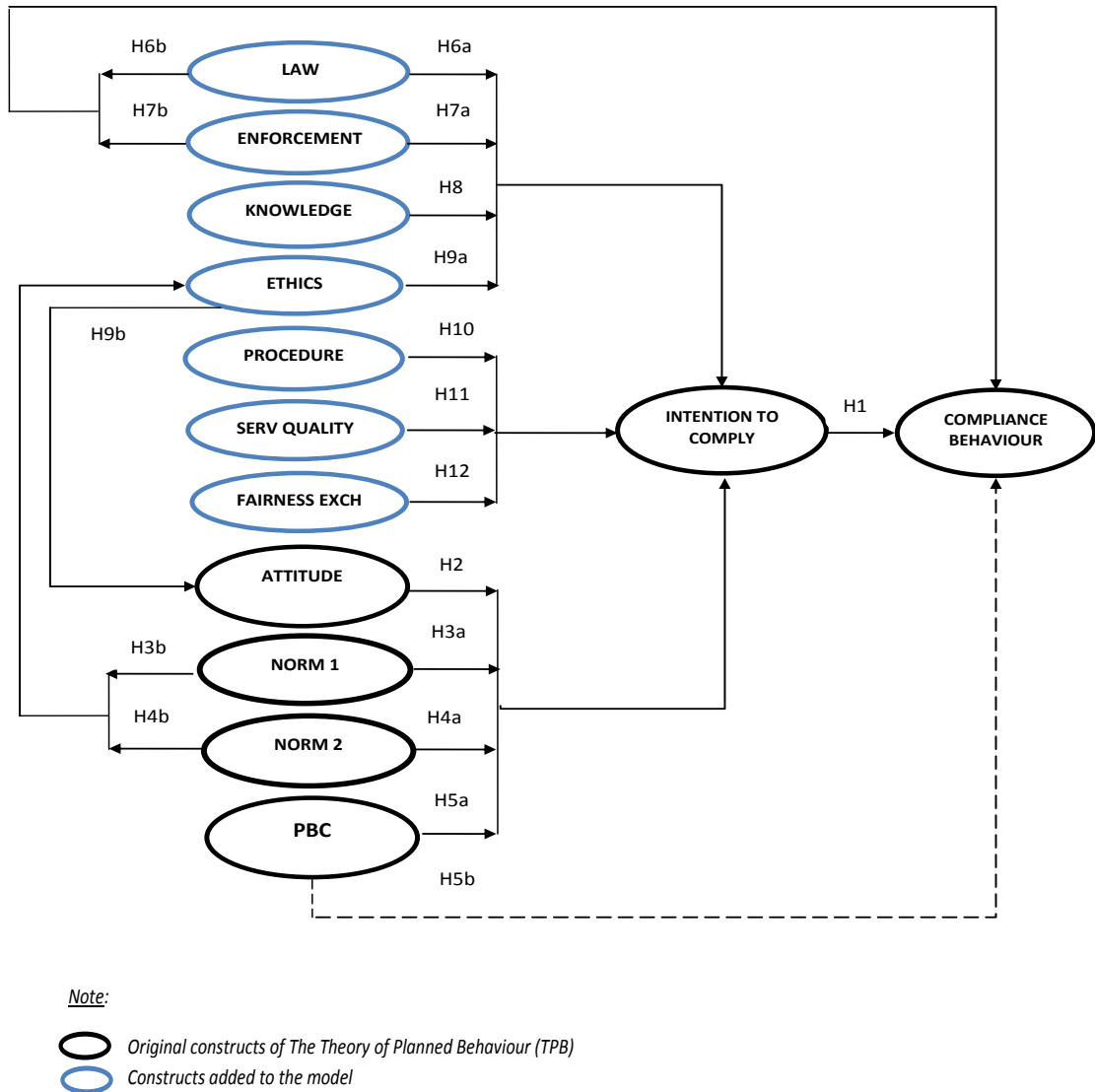
The results of the interviews in the qualitative phase of this study suggest that exchange of fairness serves as an important determinant of tax compliance. There are mixed views about government spending policies and their link to compliance decisions. Some of the respondents perceive decisions to under-declare tax to be influenced by deteriorating trust in the government over how tax is spent (Respondents R2, R7 and R10). Conversely, some respondents view government spending positively in the exchange of benefits received, such as healthcare and developing the country (Respondents R1, R3, R9 and R11).

Therefore, this study predicts that a positive perception of exchange of fairness induces Customs agents to comply with import tax law. On the other hand, Customs agents with a negative perception of exchange of fairness are less likely to comply with import tax law. The proposed hypothesis attempts to test the relationship between exchange of fairness and tax compliance intention. The prediction is formally stated in the following hypothesis:

***Hypothesis 12: Perception of exchange of fairness positively influences agents' tax compliance intention.***



## 7.4 CONCEPTUAL FRAMEWORK OF IMPORT TAX COMPLIANCE



**Figure 7.1: Conceptual Framework of Import Tax Compliance Behaviour Model**

The conceptual research model is developed based on the existing framework of TPB, a behavioural theory which is found to be relevant to tax compliance study (Bobek, Roberts et al., 2007; Feld and Frey, 2007). It is claimed that previous models of tax compliance fail to incorporate many facets of taxpayers' reality (Kirchler, 2007). Therefore, the research model is extended by the additional constructs and route structure, to form the theoretical contribution of the extended TPB model in the context of import tax compliance.

The proposed research model depicted in Figure 7.2 is developed from an

incremental study of the review of tax compliance and inter-disciplinary literature. The model integrates various factors, including structural, behavioural, social and other factors in order to better understand import tax compliance behaviour, as well as to address the gap<sup>36</sup> in current studies of import tax. It is hypothesised, based on the proposition that attitudes, subjective norms, perceived behavioural control, together with other determinants of import tax compliance behaviour such as the influence of ethics, knowledge, perception of law, perception of law enforcement, complexity of procedure, tax assessment service quality and exchange of fairness, influence agents' behaviour to comply (or not to comply) with tax law. The research model is tested through the questionnaire survey. This is elaborated on further in the remaining chapter of this thesis.

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<sup>36</sup> Refer to Chapter 4, Section 4.5.4.

## **CHAPTER 8**

### **QUANTITATIVE PHASE: SURVEY QUESTIONNAIRE**

#### **8.1 OVERVIEW**

This chapter focuses on the quantitative phase of this study, which was conducted using survey questionnaire. As discussed in Chapter 6, this study followed the exploratory sequential mixed method research design. It began with the qualitative approach and ended with the quantitative approach in the second phase. The quantitative phase is the core part of the study that serves as the validation stage for the research model developed through incremental study and some qualitative evidence to support the research model.

The first section of this chapter will, therefore, highlight the measurement of constructs, which include the original TPB constructs and additional constructs added to the research model. This is followed by the survey development, which includes the questionnaire design and the pre-testing stage that serves as the content validation stage. The subsequent section discusses the responses from the survey and the initial analysis to screen the data and tabulate the response profile and demographic. The final section outlines the analytical methods applied in this study using the structural equation modeling.

#### **8.2 CONSTRUCTS AND MODEL MEASUREMENT**

As discussed in Chapter 7, the final model of compliance behaviour consists of thirteen constructs. The six constructs formed part of the original TPB framework, which includes attitude, primary subjective norm (importer), secondary subjective norm (other agents), perceived behavioural control (PBC), behavioural intention and behaviour. The additional constructs added to the research model includes knowledge, ethics, law, law enforcement, tax assessment service quality, exchange of fairness and complexity of procedure. The following section contains a discussion on the model constructs and the multiple indicators used to measure these constructs.

### 8.2.1 Measurement Scales

The questionnaire comprised of 76 items measuring 13 constructs. The constructs used in the research model were measured using the 5-point Likert scale. A behavioural study conducted by Preston and Colman, (2000) to test the optimal number of responses categories in rating scales indicated that the 5 point scales has the advantage of being perceived by participants as relatively quick and easy to use. The study also indicated that in term of validity coefficient, there was no statistical significance in the differences of 5 point or more response categories. Moreover, 5 point scales is also a common method in most organizational studies (Hinkin, 1995)

Most of the items were measured using the lowest to highest score (scale 1 to 5). Scale 1 was assigned for “*completely disagree*”, scale 5 for “*strongly agree*“, and “*neither agree nor disagree*” as the mid-points.

For measures of knowledge, a scale ranging from 1 to 5 was used which indicate the frequency of respondents in terms of how they acquire knowledge and use of knowledge acquired. Scale 1 was assigned for “*never*”, scale 5 for “*frequent*”, and “*rarely*” as the mid-point.

For measures of behaviour (past behaviour), respondents were asked to indicate to what extent (on a scale ranging from 1 to 5) has non-compliance occurred in the past in term of offences, refused declaration and revaluation or reclassification of goods in the declaration by the authority. For this purpose, 5 points scales were used ranging from scale 1 for “*never*” to scale 5 for “*frequent*” and “*rarely*” as the mid-point.

On the formation of constructs indicator, two of the 13 constructs were measured as a formative and 11 constructs were measured as reflective. The details of the constructs measurement and indicator are discussed in the following subsections.

### 8.2.2 Construct Measurement

The construct measurement as presented in Table 8.1 provides a summary of the constructs and the respective code. It also shows the indicator measurement of the constructs, whether it was measured as a reflective or formative construct. The indicators used to measure the constructs were mainly derived from tax compliance and relevant inter-disciplinary literature. The proposed model for this study consisted

of 13 constructs, namely: behaviour (BEHV), intention (INTENT), primary subjective norm (NORM1), secondary subjective norm (NORM2), attitude (ATT), perceived behaviour control (PBC), knowledge (KNOW), ethics (ETHIC), law (LAW), law enforcement (ENFORCE), complexity of procedure (PROCEDR), tax assessment service quality (SERVQ) and exchange of fairness (FAIR).

**Table 8.1: Structure of Constructs**

SECTION	CONSTRUCT	CODE	INDICATOR TYPE
PART I			
A	Law	LAW	Reflective
B	Law Enforcement	ENFORCE	Reflective
C	Complexity of Procedure	PROCEDR	Reflective
D	Tax Assessment Service Quality	SERVQ	Formative
E	Attitude	ATT	Reflective
F	Exchange of Fairness	FAIR	Formative
G	Subjective Norm (Primary and Secondary)	NORM1 NORM2	Reflective
H	Perceived Behavioural Control	PBC	Reflective
I	Ethics	ETHIC	Reflective
J	Behaviour	BEHAV	Reflective
K	Intention	INTENT	Reflective
L	Knowledge	KNOW	Reflective
PART II	Demography		

**(a) The Research Model - Original TPB Constructs**

**(i) Attitude**

The attitude towards compliance as elaborated in Chapter 5 refers to the assessments of an individual to comply (or not to comply) with tax obligation. These assessments are based on the perceptions of whether performing the behaviour would be advantageous and improve the emotional belief on the tax obligation. Emotional beliefs are related to the feeling of pleasure or guilt for not complying or complying

with tax obligation.

Eight items were developed to measure the construct of *attitude*. Four questions were developed to capture their emotional components on performing the behaviour based on guilt feelings, civic duty and moral obligation. Additional four questions were developed to measure the participants' evaluation on the outcome of the behaviour, whether the behaviour towards compliance would be perceived as benefit or drawback. The operational definition and questionnaire items for attitude are illustrated in Table 8.2 and Table 8.3.

The indicator to measure attitude was realized as reflective because attitude is a construct that represents 'personality', which is viewed as an underlying factor that account for something unobservable (Diamantopoulos and Siguaw, 2006; Fornell, 1982; Petter et al., 2007). Furthermore, attitudes are latent in nature. They cannot be directly observed and must be inferred, usually through questionnaire responses (Plant, 2009). Previous studies have also considered attitude as a reflective indicator (example. Coltman, Devinney, Midgley, and Venaik, 2008; Wiedemann and Strebel, 2011). All of these eight items, which accounted for the observed latent constructs, were uni-dimensional and were likely to co-vary with each other. Therefore, they were considered as reflective indicators.

**Table 8.2: Operational Definitions and Source of Measurement for Attitude**

Dimension	Operational Definition	Source of Measurement
Emotional Component	Related to the feeling of pleasure or guilt towards behaviour (Ajzen, 2005).	<ul style="list-style-type: none"> <li>• Trivedi et al (2005)</li> <li>• Bobek and Hatfield, (2003)</li> </ul>
Outcome Evaluation	Attitude towards behaviour would be perceived as benefit or drawback (Ajzen, 2005).	<ul style="list-style-type: none"> <li>• Trivedi et al (2005)</li> <li>• Bobek and Hatfield, (2003)</li> </ul>

**Table 8.3: Measurement of Attitude**

<b>SECTION E: ATTITUDE</b>	
<b>Item Code</b>	<b>Measurement</b>
	<b>Emotional Component</b>
<b>ATT 1</b>	Fulfilling the obligation in paying import tax is something to be proud of
<b>ATT 2</b>	We feel that we have done something that is beneficial to the society by paying import tax
<b>*ATT 3</b>	It is not an offence sometimes to pay lower import tax than the actual value
<b>ATT 4</b>	Our company will feel reprehensive by not paying import tax
	<b>Perceived Outcome</b>
<b>ATT 5</b>	Paying import tax is an important contribution to the country
<b>ATT 6</b>	Paying import tax would avoid company from being penalised
<b>*ATT 7</b>	Paying import tax will reduce company's profit
<b>*ATT 8</b>	Paying import tax continuously will increase the cost of goods and services

*Note:*

*\*Recoded item*

## **(ii) Subjective Norm**

Subjective Norm as elaborated in Chapter 5 refers to an individual's perception that social pressure or referent group motivates the individual to engage or not to engage in a particular behaviour. In this study, the perceived social pressure that motivated agents to comply or not to comply with tax obligation was based on the influence of the reference group. It was identified from the interview findings (in Chapter 7) that these two referent groups were: (1) importers and (2) other agents. The operational definition and the questionnaire items for subjective norm are illustrated in Table 8.4 and Table 8.5.

To measure this construct, a total of eight items were developed measuring the influence of the two referent groups (*four items measuring each referent group*). The first referent group is the importers and the second referent group is the other agents. The questions developed were concerning the expectations of important referents will influence Customs agents' compliance decision. Four items measuring agents' perception on whether important referent would expect them to comply or not comply. Another four items measuring referents' behaviour on whether it would influence the agents to behave in the same manner. All these eight items were likely to

co-vary with each other and therefore, they were considered as reflective indicators.

**Table 8.4: Operational Definitions and Source of Measurement for Subjective Norm**

Dimension	Operational Definition	Source of Measurement
Primary Subjective Norm (Importers)	Primary referent group that motivates the individual to engage or not to engage in a particular behaviour (Taylor and Todd (1995).	<ul style="list-style-type: none"> <li>• Bobek, (2011)</li> <li>• Salleh (2010)</li> </ul>
Secondary Subjective Norm (Other Agents)	Secondary referent group that motivates the individual to engage or not to engage in a particular behaviour (Taylor and Todd (1995).	<ul style="list-style-type: none"> <li>• Bobek, (2011)</li> <li>• Salleh (2010)</li> </ul>

**Table 8.5: Measurement of Subjective Norm**

SECTION G: SUBJECTIVE NORM	
Item Code	Measurement
<b>Primary Subjective Norm (Importers)</b>	
<b>NB 1</b>	Our client would think that we should declare taxable good accordingly based on Customs law
<b>*NB 2</b>	Our client would think that it is not necessary to fully declare taxable goods to save some tax payment
<b>*NB 3</b>	Our client would approve our decision to understate the import tax
<b>NB 4</b>	We always follow our client's advice to pay import tax according to Customs assessment
<b>Secondary Subjective Norm (Other Agents)</b>	
<b>NI 1</b>	Other agents who important to us agree if we pay import tax according to Customs assessment
<b>*NI 2</b>	It is expected by other agents who important to us, that we should not fully-declare taxable good to save tax
<b>*NI 3</b>	Other agents who important to us usually would not fully declare taxable goods to save tax
<b>NI 4</b>	Generally other agents who is important to us would not understate import tax although they are in difficult situation

*Note:*

*\*Recoded item*

### (iii) Perceived Behavioural Control (PBC)

In the area of tax compliance, perceived behavioural control refers to not only the ease or difficulty to comply with tax obligation in general, but it refers to whether an individual believes he or she is able to control from performing a specific



behaviour (Bobek and Hatfield, 2003).

Ajzen, (2002) suggested that the construct of Perceived Behavioural Control (PBC) consisted of two components, self-efficacy and controllability. These two components have been found to be highly correlated in some studies (Ajzen, 2002; Trafimow et al., 2002). Moreover, the mixture of self-efficacy and controllability items has been found to report considerable internal consistency in meta-analysis review of studies conducted by Cheung and Chan (in excerpts of Ajzen, 2002), suggesting that tax compliance studies and some of the recent studies in various fields have maintained PBC as a uni-dimensional construct (example Ajzen and Klobas, 2013; Bobek, Hatfield, and Wentzel, 2007; Bobek and Hatfield, 2003; Kautonen, van Gelderen, and Fink, 2013; Trivedi, Shehata, and Mestelman, 2005). Consistent with the theoretical justification as discussed above, the constructs of PBC was considered as a uni-dimensional construct measured by a mixture of self-efficacy and controllability items.

In this study, the construct of PBC was measured with five items. These items were measured according to two main factors, self-efficacy and controllability, following the suggestion by Francis, Eccles, and Johnston, (2004), where:

- a) Self-efficacy – was assessed by asking respondents to report whether it was easy or difficult to perform a behaviour and was measured with three items.
- b) Controllability – was assessed by asking respondents to report whether performing a behaviour was up to them or whether factors beyond their control determined their behaviour and was measured with two items.

**Table 8.6: Operational Definitions and Source of Measurement for Perceived Behavioural Control**

Dimension	Operational Definition	Source of Measurement
Self-efficacy	Perceived to be easy or difficult for an individual to perform behaviour (Trafimow et al., 2002)	<ul style="list-style-type: none"> <li>• Francis, Eccles, and Johnston, (2004)</li> <li>• Chen, Gully, and Eden, (2001)</li> </ul>
Controllability	Presence or absence of requisite resources and opportunities to carry out the behaviour (Chang, 1998).	<ul style="list-style-type: none"> <li>• Francis, Eccles, and Johnston, (2004)</li> <li>• Bobek and Hatfield, (2003)</li> </ul>

Consistent with Ajzen, (1991), each composite measure was made up of factors that assist or hinder compliance (or encourage noncompliance), and the frequency of these factors. All five items measuring PBC construct were measured with reflective indicators. As expected for reflective constructs, these items should co-vary with each other. The operational definition and questionnaire items for PBC are illustrated in Table 8.6 and Table 8.7.

**Table 8.7: Measurement of Perceived Behavioural Control**

<b>SECTION H: PERCEIVED BEHAVIOURAL CONTROL</b>	
<b>Item Code</b>	<b>Measurement</b>
	<b>Self-efficacy</b>
<b>PBC 1</b>	It would be very easy for the company to comply with Customs law
<b>PBC 2</b>	It would be easy to understate import tax amount without being detected by Customs
<b>PBC 3</b>	Declaring taxable good as non-taxable goods for the purpose of understate tax payment is not an easy task
	<b>Controllability</b>
<b>*PBC 4</b>	If we have the opportunity we will declare the goods partially so that we can save tax
<b>PBC 5</b>	We believe that our company can manage to pay import tax accordingly even if the company faced financial difficulties

*Note:*

*\*Recoded item*

#### **(iv) Behavioural Intention**

Behavioural intention refers to respondents' intention to comply (or not to comply) with their tax obligations. The measurement of behavioural intention as a dependent variable is described as the willingness to declare accurately and pay any import tax in accordance to Customs law at the time of lodging import declaration. This was similar in direct tax compliance where taxpayer's compliance was described as the willingness to lodge the tax return form at the proper time and accurately report tax liability (Roth, Scholz, and Witte, 1989). The operational definition and questionnaire items for behavioural intention are illustrated in Table 8.8 and Table 8.9.

Eight items were developed to measure the respondents' behavioural intention to comply (or not to comply) with tax laws. The questions relates to the intention to

declare accurately involving price valuation, product classification and description of goods. All eight items measured behavioural intention. It was expected that these items would co-vary with each other and was measured with reflective indicators.

**Table 8.8: Operational Definitions and Source of Measurement for Behavioural Intention**

Dimension	Operational Definition	Source of Measurement
Intention to Comply	Willingness to declare accurately and pay any import tax in accordance to Customs law at the time of lodging import declaration (adapted from Roth et al., 1989).	Adapted from <ul style="list-style-type: none"> <li>• Ajzen and Fishbein, (2010)</li> <li>• Hanno and Violet (1996)</li> </ul>

**Table 8.9: Measurement of Behavioural Intention**

SECTION K: BEHAVIOURAL INTENTION	
Item Code	Measurement
INT 1	Our company is willing to pay the correct amount of import tax
INT 2	Our company will lodge declaration according to the actual Customs tariff code
INT 3	Our company will lodge declaration according to Customs valuation
INT 4	Our company will lodge declaration according to actual quantity of goods
INT 5	Our company will adhere to Customs import declaration procedure
INT 6	Our company is willing to pay any discrepancies during the assessment of import tax
INT 7	Our company will lodge declaration based on the actual invoice
INT 8	Our company will declare goods in import declaration based on the actual documents from importer

#### (v) Behaviour

Behaviour in this study refers to the respondents' self-reported past behaviour. This measure of self reported behaviour was used as a proxy for measuring compliance behaviour in the research model since past behaviour is considered to reflect future behaviour (Burnkrant and Jr, 1988; Tittle, 1980). Furthermore, the

influencing factor that leads to the outcome of the behaviour such as attitude and belief tend to remain stable over time (Fishbein and Ajzen, 2010). Therefore, behaviour in this study is operationalised as self-reported past behaviour on compliance with import declaration. The operational definition and questionnaire items for behaviour are illustrated in Table 8.10 and Table 8.11.

The behaviour constructs was a dependent and measured using six items: two questions on offences, two questions on refused declaration from Customs administration by risk assessment method, two questions on price revaluation and reclassification of goods in the declaration by the authority. These questions relate to the suppressed tax amount related to the declarations.

All six items were developed with specific reference to compliance behaviour. The items were expected to measure behaviour and were likely to co-vary with each other. Thus, the behaviour construct was measured with reflective indicators.

**Table 8.10: Operational Definitions and Source of Measurement for Behaviour**

Dimension	Operational Definition	Source of Measurement
Compliance Behaviour	Self reported past behaviour on compliance with import declaration (adapted from Burnkrant and Jr, 1988; Tittle, 1980; Roth et al., 1980)	<ul style="list-style-type: none"> <li>Adapted from Ajzen and Fishbein, (2010)</li> <li>Interview findings</li> </ul>

**Table 8.11: Measurement of Behaviour**

SECTION J: BEHAVIOUR	
Item Code	Measurement
<b>BEH 1</b>	Declaration in the system was suspended by Customs
<b>BEH 2</b>	Being compounded on various offence such tariff code classifications and inaccurate descriptions
<b>BEH 3</b>	Failed to produce Certificate of Origin as required
<b>BEH 4</b>	Price reassessment/revaluation by Customs due to under-declaration of value
<b>BEH 5</b>	Reclassification of Customs tariff code by Customs due to incorrect classification
<b>BEH 6</b>	Declaring incorrect descriptions of goods

## **(b) Additional Constructs to the Research Model**

### **(i) Knowledge**

Knowledge in this study refers to respondents decision to comply (or not to comply) based on their level of knowledge on Customs import declaration. The level of respondents' knowledge was measured by four components: knowledge updating, knowledge acquisition (internal and external), knowledge retention and knowledge application. Updating of knowledge emphasized on how well the agents keep themselves updated with the current knowledge. Knowledge acquisition was evaluated in the form of knowledge acquired internally and externally, for example through continuous training. Knowledge retention relates to the agents effort to retain the knowledge acquired from the trainings. Finally, knowledge application concerns the practical application by the agents from the point when they acquired the knowledge. The operational definition and questionnaire items for knowledge are illustrated in Table 8.12 and Table 8.13.

The construct of 'knowledge' was measured as a uni-dimensional construct. A total of five items were developed: two questions measuring knowledge acquisition, and each of the three questions measuring acquiring knowledge, retention of knowledge and application of knowledge. All items were measured as reflective as these items reflected the aspects of knowledge and were likely to co-vary with each other.

**Table 8.12: Operational Definitions and Source of Measurement for Knowledge**

<b>Dimension</b>	<b>Operational Definition</b>	<b>Source of Measurement</b>
Updating of Knowledge	How will individuals keep themselves updated with the current knowledge	Adapted from <ul style="list-style-type: none"><li>• Wasko and Faraj, (2005)</li><li>• Blackler, (1995)</li></ul>
Knowledge Acquisition	Knowledge acquired internally and externally	Adapted from <ul style="list-style-type: none"><li>• Wasko and Faraj, (2005)</li><li>• Blackler, (1995)</li></ul>
Knowledge Retention	Effort to retain the knowledge acquired	Adapted from <ul style="list-style-type: none"><li>• Wasko and Faraj, (2005)</li><li>• Blackler, (1995)</li></ul>
Application of knowledge	Practical application of knowledge from point knowledge was acquired	Adapted from <ul style="list-style-type: none"><li>• Wasko and Faraj, (2005)</li><li>• Blackler, (1995)</li></ul>

**Table 8.13: Measurement of Knowledge**

<b>SECTION L: KNOWLEDGE</b>	
<b>Item Code</b>	<b>Measurement</b>
<b>KN 1</b>	Ensuring knowledge on Customs is up-to-date– e.g. attended courses, refer websites or direct consultation from Customs
<b>KN 2</b>	Attended courses conducted by Customs
<b>KN 3</b>	Attended courses conducted by your associations such as SFFLA, JOFFA and PFFA
<b>KN 4</b>	Keep lecture notes from the courses that you have attended
<b>KN 5</b>	Applied the knowledge gained in your daily work

**(ii) Ethics**

Ethics in this study refers to the respondents’ decision to comply (or not to comply) with tax obligation based on their withholding ethical belief. The construct of ‘ethics’ was measured by respondents’ internal factor (such as moral values), whether they perceived the behaviour of compliance relating to under-declaration of taxable imported goods and tax evasion as something ethical, unethical, morally right or wrong. The operational definition and questionnaire items for ethics are illustrated in Table 8.14 and Table 8.15.

Five items were developed to measure the construct of ethics. All five items accounted for the observed latent constructs of ‘ethics’ and were uni-dimensional, which were likely to co-vary with each other. Therefore, they were considered as reflective indicator.

**Table 8.14: Operational Definitions and Source of Measurement for Ethics**

<b>Dimension</b>	<b>Operational Definition</b>	<b>Source of Measurement</b>
Ethical belief	Perceived behaviour of compliance relating to under-declaration of goods and tax evasion as something ethical, unethical, morally right or wrong (Adapted from Alm and Torgler, 2011).	Adapted from <ul style="list-style-type: none"> <li>• Wenzel, (2007)</li> <li>• Bidin et.al., (2011)</li> </ul>

**Table 8.15: Measurement of Ethics**

<b>SECTION I: ETHICS</b>	
<b>Item Code</b>	<b>Measurement</b>
<b>ETH 1</b>	Ethically our company will <b>feel reprehensible</b> with the involvement in falsifying import declaration
<b>ETH 2</b>	Views on fairness of import tax system will <b>not affect</b> our company's decision in import declaration matter
<b>*ETH 3</b>	Our company should <b>not feel reprehensive</b> by <b>not fully declared goods</b> in import declaration if they feel that the current tax system is not fair
<b>*ETH 4</b>	Our company should <b>not feel reprehensive</b> by <b>not declaring correct description</b> of import goods if they do not get the benefit from the tax paid
<b>*ETH 5</b>	There is <b>nothing wrong for not informing Customs</b> if there is any discrepancies and shortage in import tax payment.

*Note:*

*\*Recoded item*

### (iii) Law

Law refers to the instruments to control and draw the power of an institution. The construct of 'Law' measured on the perception of respondents towards Customs law in terms of ambiguity, adequacy, implementation, leniency and provision for punishment as stipulated in the Customs law, which would motivate respondents to comply (or not to comply) with tax obligation. The construct of 'Law' was measured by adapting the instruments used by Bidin, (2008). The operational definition and the questionnaire items for construct of law are illustrated in Table 8.16 and Table 8.17.

The construct of law was a uni-dimensional construct, measured using five items. All five items represented reflective indicator to capture the five components: ambiguity of the law, adequacy, implementation, leniency and punishment, which were likely to co-vary with each other.

**Table 8.16: Operational Definitions and Source of Measurement for Law**

<b>Dimension</b>	<b>Operational Definition</b>	<b>Source of Measurement</b>
Law	Ambiguity, adequacy, implementation, leniency and provision for punishment in the Customs law which would influence compliance decision (Adapted from Hanno and Violet, 1996 and Davis et.al, 2003)	Adapted from Bidin, (2008)

**Table 8.17: Measurement of Law**

<b>SECTION A: LAW</b>	
<b>Item Code</b>	<b>Measurement</b>
<b>LAW 1</b>	The laws on import tax are <b>ambiguous</b>
<b>LAW 2</b>	There are sufficient provision in the laws on import tax
<b>LAW 3</b>	The law on import tax are <b>not seriously</b> implemented
<b>LAW 4</b>	Penalty and imprisonment on laws related to import tax are considered <b>inadequate</b>
<b>LAW 5</b>	The laws on import tax <b>adequately</b> provide penalty and imprisonment in relation to offences committed

*Note:*

*\*Recoded item*

#### **(iv) Law Enforcement**

Law enforcement refers to the level of enforcement and the action taken by the governing institutions such as Customs administration. The construct of ‘law enforcement’ measured the perception of respondents on the level of enforcement, detection, prosecution and penalty by the Customs administration towards tax evaders. The operational definition and questionnaire items for construct of law enforcement are illustrated in Table 8.18 and Table 8.19.

To measure the construct of ‘law enforcement’, five items were developed. Three items measured detection, prosecution and penalty and another two items measured enforcement. These items measured the uni-dimensionality construct of ‘law enforcement’, were likely to co-vary with each other, and represented a set of reflective indicators.

**Table 8.18: Operational Definitions and Source of Measurement for Enforcement**

<b>Dimension</b>	<b>Operational Definition</b>	<b>Source of Measurement</b>
Perception of Enforcement	Enforcement, detection, prosecution and penalty by Customs which would influence compliance decision (Adapted from Hanno and Violet, 1996 and Davis et.al, 2003)	Adapted from Bidin, (2008)



**Table 8.19: Measurement of Enforcement**

<b>SECTION B: ENFORCEMENT</b>	
<b>Item Code</b>	<b>Measurement</b>
<b>ENF 1</b>	Agents who failed to pay import tax are always being <b>penalised</b> by Customs
<b>ENF 2</b>	Customs always <b>manage to detect</b> agents who fail to pay import tax
<b>*ENF 3</b>	Agents who failed to pay import tax are <b>not being prosecuted</b> by Customs
<b>ENF 4</b>	Customs enforcement are <b>stringent</b> with regards to tax evaders
<b>*ENF 5</b>	Customs <b>never</b> makes any inspection on forwarding agents who fail to pay import tax

*Note:*

*\*Recoded item*

#### **(v) Tax Assessment Service Quality**

Tax assessment service quality measured the perception of respondents towards the service provided by the Customs administration, which would influence compliance with tax obligation. In order to operationalised the construct of ‘quality of service’, the measurement of SERVQUAL, developed by Zeithaml, (1988) based on the performance-based scale, was adapted to measure the quality of service. The SERVQUAL instrument measured five dimensions of service quality: (1) tangibles, (2) reliability, (3) responsiveness, (4) assurance, (5) empathy.

It was further developed by Buttle, (1996) who expanded it into ten dimensions: (1) reliability, (2) responsiveness, (3) competency, (4) access, (5) courtesy, (6) communication, (7) credibility, (8) security, (9) understanding and (10) tangibles. The operational definition and items to measure ten dimensions of quality of service are illustrated in Table 8.20 and Table 8.21.

**Table 8.20: Operational Definitions and Source of Measurement for Tax Assessment Service Quality**

<b>Dimension</b>	<b>Operational Definition</b>	<b>Source of Measurement</b>
<b>Reliability</b>	Consistency in providing information	Adapted from Buttle, (1996)
<b>Responsiveness</b>	Desire to assist customers	Adapted from Buttle, (1996)
<b>Competent</b>	Knowledge and skills of Customs officer	Adapted from Buttle, (1996)
<b>Access</b>	Easy to contact and meet with Customs officer	Adapted from Buttle, (1996)
<b>Courtesy</b>	Attitude of Customs officers, whether they are considerate, respectful and friendly to customers	Adapted from Buttle, (1996)
<b>Communication</b>	Ease of communication	Adapted from Buttle, (1996)
<b>Credibility</b>	Trustworthiness of Customs officer	Adapted from Buttle, (1996)
<b>Security</b>	Assurance in terms of confidentiality of information provided	Adapted from Buttle, (1996)
<b>Understanding</b>	Effort in understanding the need or problem faced by the customers	Adapted from Buttle, (1996)
<b>Tangibles</b>	Facilities and work equipment	Adapted from Buttle, (1996)

**Table 8.21: Measurement of Tax Assessment Service Quality**

<b>SECTION D: TAX ASSESSMENT SERVICE QUALITY</b>	
<b>Item Code</b>	<b>Measurement</b>
<b>SQ 1</b>	<b>Reliability</b> <ul style="list-style-type: none"> <li>Customs officers can provide accurate information when managing customers' problem</li> </ul>
<b>SQ 2</b>	<b>Responsiveness</b> <ul style="list-style-type: none"> <li>Customs officers are very responsive in providing service to customers</li> </ul>
<b>SQ 3</b>	<b>Competent</b> <ul style="list-style-type: none"> <li>Customs officers who deals with customers are capable and knowledgeable</li> </ul>
<b>SQ 4</b>	<b>Access</b> <ul style="list-style-type: none"> <li>Customs officers are always available to assist customers</li> </ul>
<b>SQ 5</b>	<b>Courtesy</b> <ul style="list-style-type: none"> <li>Customs officers are always courteous when assisting customers</li> </ul>
<b>SQ 6</b>	<b>Communication</b> Customs officers communicates well with customers
<b>SQ 7</b>	<b>Credibility</b> <ul style="list-style-type: none"> <li>Customs officers are trustworthy</li> </ul>
<b>SQ 8</b>	<b>Security</b> <ul style="list-style-type: none"> <li>Information provided to Customs are secured</li> </ul>
<b>SQ 9</b>	<b>Understanding</b> <ul style="list-style-type: none"> <li>Customs officers are always understand customers' requirements</li> </ul>
<b>SQ 10</b>	<b>Tangibles</b> <ul style="list-style-type: none"> <li>Customs office has adequate equipments</li> </ul>

The construct of service quality in this study was measured as a uni-dimension construct. This uni-dimensional construct of service quality was represented by a set of ten formative indicators. These ten items were considered as formative indicators as it captured ten different aspects of service quality of the import tax system, which might not co-vary with each other.

#### (vi) Exchange of Fairness

Exchange of fairness refers to the benefits received from the government in exchange of the tax paid (Azmi and Perumal, 2008; Richardson, 2005, 2006). In this study, it referred to the respondents' perception towards government's spending in exchange with the import tax paid, which would influence compliance behaviour.

'Exchange of fairness' construct was measured based on three dimensions in exchange of fairness, developed by Richardson, (2005, 2006). The three dimensions are: (1) fair benefits, (2) benefits received and (3) equity benefits. The operational definition and items developed to measure the three dimensions of exchange of fairness are illustrated in Table 8.22 and Table 8.23.

The construct of exchange of fairness was measured as a uni-dimensional construct. The items that measured this construct captured different aspects of fairness, which were fair benefit, equity benefit and benefit received. Therefore, it was measured with formative set of indicators.

**Table 8.22: Operational Definitions and Source of Measurement for Exchange of Fairness**

Dimension	Operational Definition	Source of Measurement
<b>Fair benefits</b>	Fair value of benefits	Richardson, (2005, 2006)
<b>Benefits Received</b>	Tax fairness on the benefits received	Richardson, (2005, 2006)
<b>Equity benefits</b>	Reasonableness of benefits	Richardson, (2005, 2006)

**Table 8.23: Measurement of Exchange of Fairness**

<b>SECTION F: EXCHANGE OF FAIRNESS</b>	
<b>Item Code</b>	<b>Measurement</b>
<b>FA 1</b>	<b>Fair Benefits</b> <ul style="list-style-type: none"> <li>• Benefits received from government such as education, health and infrastructure in exchange of import tax paid are fair and equitable</li> </ul>
<b>FA 2</b>	<b>Benefit Received</b> <ul style="list-style-type: none"> <li>• Benefits given by the government are reasonable in exchange to the amount of import tax paid</li> </ul>
<b>*FA 3</b>	<b>Equity Benefits</b> <ul style="list-style-type: none"> <li>• Import tax rate imposed are still at a high rate compared to benefits provided by government</li> </ul>

*Note:*

*\*Recoded item*

#### **(vii) Complexity of Procedure**

Procedural complexity is a relatively under-explored construct introduced in this study. The construct of complexity of procedure refers to as any type of complexity that involves excessive burden or numerous processes or steps concerning the process of import declaration such as clarity, flexibility, uniformity of procedure, rigidity of procedure that would make compliance easy (or difficult).

The items to measure the construct of complexity of procedure were developed based on the items pooled from the findings of the qualitative interview. The operational definition and items developed to measure the construct of complexity of procedure are illustrated in Table 8.24 and Table 8.25. Eight items were developed to measure the construct of ‘complexity of procedure’. It was a uni-dimensional construct, the indicator to measure the construct was considered as reflective indicator, which was likely to co-vary with each other. Therefore, it was modelled as a reflective construct.

**Table 8.24: Operational Definitions and Source of Measurement for Complexity of Procedure**

Dimension	Operational Definition	Source of Measurement
<b>Complexity of Procedure</b>	Customs import procedure in relation to Customs declaration such as clarity, flexibility, uniformity of procedure, rigidity of procedure that would make compliance easy (or difficult).	Item pool from interview findings

**Table 8.25: Measurement of Complexity of Procedure**

SECTION C: COMPLEXITY OF PROCEDURE	
Item Code	Measurement
<b>*PR 1</b>	Import declaration procedure is <b>not flexible</b>
<b>*PR 2</b>	Import declaration procedure is <b>ambiguous</b>
<b>*PR 3</b>	Too <b>frequent changes</b> in import declaration procedure
<b>PR 4</b>	Import declaration procedure is <b>easy</b> to understand
<b>*PR 5</b>	Import declaration procedure is <b>too rigid</b>
<b>PR 6</b>	There is <b>sufficient</b> provision in import declaration procedure
<b>*PR 7</b>	There is no <b>uniformity</b> in import declaration procedure between officers
<b>*PR 8</b>	Current Import declaration procedure <b>delays</b> the process of paying tax

*Note:*

*\*Recoded item*

### (c) Demographic Variables

The purpose of collecting demographic information is twofold: I) to present and analyse the respondents' background information involved in this survey; (II) to extend and expand the scope of this study to support future works and analysis.

The demographic details captured in this study include: (1) designation, (2) gender, (3) ethnics group, (4) business category, (5) number of years license held, (6) number of clients, (7) estimated number of import declarations, and (8) location of license issued.

The designation was identified by (a) director, (b) manager, (c) executive and (d) others, which were the typical designation levels in organizational setting in Malaysia. Gender was assigned using dummy variables, 1 for male and 0 for female. To capture the ethnic group, respondents were asked to tick the appropriate group that they belonged to. In Malaysia, ethnic groups were either: (a) Malay, (b) Chinese, (c) Indian, and (d) Others.

For business category, the respondents were asked to specify the type of businesses they were registered under the Companies Commission of Malaysia (which assuming the functions of the Registrar of Companies and Registrar of Business), either as a (a) limited company, (b) private limited, (c) partnership, and (d) sole proprietorship. The categories were transformed into dummy variables, 0 for limited company, 1 for private limited, 2 for partnership and 3 for sole proprietorship.

The number of years licensed held was categorised as (a) less than 2 years, (b) 2 to 5 years, (c) 6 to 10 years, (d) 11 to 15 years and (e) more than 15 years. The number of clients was indicated by the current withholding number of clients: (a) less than 25 clients, (b) 25 to 50 clients, (c) 51-75 clients, (d) 76 to 100 and (e) more than 100 clients. The number of declarations was indicated as: (a) less than 50, (b) 50 to 150, (c) 151 to 300, (d) 301 to 500 and (e) more than 500.

The final background detail was the location where the agents' license was issued. The location was indicated by the different states in Malaysia, which was divided into different geographical areas as follows: (a) Selangor, (b) Johor, (c) Pulau Pinang, (d) KLIA and (e) others.

### **8.3 SURVEY QUESTIONNAIRE**

#### **8.3.1 A Brief Overview of Survey Questionnaire**

The questionnaire developed in this study as presented in Appendix 9, comprised of 76 items and divided into three main sections. Detail items and relevant literature that guided the development of each constructs measurements are elaborated in the previous section (Section 8.2.2). The first section of the questionnaire was about agents' perception on tax administration, concerning the administration of the law, law enforcement, administration of the import declaration procedure and the quality of tax administration. The second section consisted of questions about their

views on import tax, focusing on attitude, perception of exchange of fairness, peer influence, and belief about tax compliance. The third section comprised of questions on declaration practices, which focused on their ethics, intention and the behaviour to comply with tax laws. The final section was designed to capture the demographic information of the respondents. The questionnaire was prepared in dual language, English and Malay, to facilitate understanding and answering of the questionnaire.

### **8.3.2 Pre-Testing**

Pre-testing was carried out with four reviewers: an academic in behavioural research, two tax academics, and a tax practitioner. The comments from these experts were considered to improve the questionnaire prior to the actual survey distribution. The responses from experts were analysed and the resulting information was used to clarify the wording of the questions as well as the sequence of instrument and the constructs to be presented. A summary of the responses and feedback from the expert are presented in Appendix 8.

## **8.4 SURVEY RESPONSES**

### **8.4.1 Survey Distribution**

The survey questionnaires were mailed simultaneously to all three geographical locations (north zone, central zone and south zone). The questionnaire was disseminated to individuals entrusted by the company (Customs agents) to make decisions on matters pertaining to Customs declaration. A copy of the questionnaire was sent to every name in the list using a self contained address and envelope of researchers. All subjects were asked to fill out the questions in the questionnaire and returned within two weeks. Follow-up actions were conducted after two weeks after the questionnaire copies were distributed by a reminder letter and phone calls.

### **8.4.2 Response Rate**

The response rate for the sample was calculated as the percentage of all the respondents in the sample according to survey distribution and cluster based. Of the 650 questionnaires distributed, 279 or 42% of the questionnaires were returned. The response rate, according to the respective cluster was considered as encouraging with a response rate ranging from 35% to 54 %. The initial response analysis showed that

the number of responses was sufficient for the selected analytical approach adopted in this study, which are subjected to further data reduction and analysis. Table 8.26 shows the summary of the survey distribution and response rates for this study that will be used for further analysis.

**Table 8.26: Summary of Survey Distribution and Response Rates**

Cluster	States	Survey distributed	Survey returned	Percentage of response (Cluster)	Percentage of response (Total distribution)
1	Central (Selangor)	300	107	36%	16%
2	Central (KLIA)	80	40	50%	6%
3	North (Penang)	100	54	54%	8%
4	South (Johor)	170	78	46%	12%
<b>TOTAL</b>		<b>650</b>	<b>279</b>		<b>42%</b>

## 8.5 SURVEY RESPONSE ANALYSIS

This section discussed the initial analysis on the survey responses. The process of analysis began with data entry, followed by data screening. The analysis then continued with the bias test. This process was conducted prior to further data analysis in SEM to ensure that the data sets were statistically fit. Finally, the cleansed data were tabulated for analysis of profiling and demographics.

### 8.5.1 Data Entry Process

The data from the survey responses were entered into the SPSS software version 20. This step was performed manually as the survey was in the form of hardcopy. The data entered in the software were checked several times to ensure that they are entered correctly. The data were then used for subsequent analysis as described in subsequent section.



### **8.5.2 Data Mining/Screening**

#### **(a) Missing Data**

Missing data analysis was conducted to eliminate responses that did not fit for statistical analysis purposes. A total of 34 responses were deleted from the data set, leaving the final samples at 245 or 38 percent of usable cases for further analysis.

After performing missing data analysis, the reduced data set indicated that the percentage of missing value was less than 5 percent. It appeared that the remaining missing value was not significant, which was comparable to other studies that had reported missing values ranging from 2 to 7 percent (Vatanasakdakul, 2007; Venaik, 1999; Yue, 2004). Furthermore, with the cross-sectional data and the remaining largest set of available cases analysis are considered as reasonable for further analysis (Bennett, 2001).

#### **(b) Missing Value Estimation Technique**

The process of replacing missing data was performed using the Expectation Maximization (EM) technique in SPSS. EM technique was selected it is superior to other approaches, statistically efficient and produces parameter estimates with acceptable standard error (Peng, Harwell, Liou, and Ehman, 2007), particularly with smaller sample size (less than 250) (Pallant, 2007). EM technique estimates the value of each mean and covariance as if there is no missing data (Little and Rubin, 2002). The missing values are replaced by the means calculated by the EM algorithm involving a two step iterative process, using regression analysis to estimate the missing values and applying the maximum likelihood procedures to make parameter estimation (Schlomer et al., 2010).

#### **(c) Extreme Value Analysis**

Outlier analysis or extreme value analysis was performed to determine how much of a problem would any extreme values cause and whether the values are distorting the results (Pallant, 2007). To test for outlier, this study used the 5 percent trimmed means statistic using SPSS. The trimmed means is compared against the original mean to determine any significant difference. If there is an indication of significant difference in value, the data need to be further investigated to verify the

impact of the extreme value to the data sets (Pallant, 2007). The result of the extreme value analysis shows that there was no significant difference between the trimmed means and the original means for all variables. Therefore, the extreme values that exist in the data sets did not distort the data significantly.

**(d) Test of Normality**

The purpose of this test was to see whether the relationship between the two variables was linear or otherwise. The result of the analysis as presented in Table 8.27 shows that majority of the constructs had skewness and kurtosis which were within the acceptable range of  $\pm 2:58$ , except the construct of subjective norm, which fall out of the range. Kolmogorov-Smirnov test demonstrates that all of the constructs indicated significant values (p-value) of less than 0.05. This result suggests that the assumption of normality was achieved for all constructs; hence the data were used for further analysis.

**Table 8.27: Results of Skewness and Kurtosis Statistics for All Variables (N = 245)**

	Skewness		Kurtosis	
	Statistic	Std. Error	Statistic	Std. Error
Attitude	-.234	.156	.175	.310
Norm 1	-.721	.156	2.084	.310
Norm 2	-1.125	.156	4.679	.310
PBC	.381	.156	-.275	.310
Knowledge	-.313	.156	-.230	.310
Fairness	-.141	.156	1.254	.310
Procedure	.155	.156	.171	.310
Law	.132	.156	.749	.310
Enforcement	.264	.156	.150	.310
Ethics	-.062	.156	.337	.310
Service Quality	-.664	.156	.739	.310
Intention	.336	.156	-1.240	.310
Behaviour	-1.033	.156	.697	.310

**8.5.3 Handling Non-Response Error**

Lindner, Murphy, and Briers, (2001) recommended a non-response error test if a response rate below 85% is achieved. A total of 279 responses were received in this study or 42%, which was below the threshold of 85%. Therefore, the non response

error test was conducted by comparing early to late respondents method to examine if there was significant difference between these two groups (Lindner et al., 2001; Matteson et al., 1984).

In this study, the samples were divided into two groups: the first group was the group of respondents who submitted the questionnaire in advance and the second groups was the group of respondents who returned the questionnaire after the follow-up stage. The responses from the late respondents were used as the proxies for non-respondents (Armstrong and Overton, 1977; Miller and Smith, 1983). The first 25 percent and the last 25 percent were selected to represent the early and late respondents, respectively (Armstrong and Overton, 1977). Therefore, 70 samples from each group were selected to test for non-response error for each construct. Two groups were coded as 1 and 2. Code 1 was the first group, while code 2 was the second group. Independent samples *t*-test analysis was performed to compare the mean score for the constructs between the two groups, before and after the follow-up. The two tailed *p*-value was examined to determine the significant difference between the two groups.

Test results indicated a *p*-value of more than 0.05, thus there was no significant difference between the two groups as shown in Table 8.28. Therefore, the result of the survey responses offered some indication that respondents and non-respondents did not differ on sample characteristics that were of interest to this study. This result also provided some indication that the data were useful for subsequent analysis that will be further elaborated in the following section.

**Table 8.28: Response Bias Test for Two Groups of Respondents – Early Responses (Group 1) and Late Responses (Group 2)**

<b>Group</b>	<b>Total Respondents</b>	<b>Mean</b>	<b>Std. Deviation</b>	<b><i>t</i>-value</b>	<b><i>p</i>-value</b>
1	70	3.669	0.948	0.171	0.864
2	70	3.640	1.067		

#### **8.5.4 Respondents' and Company Profiles**

As discussed in Section 3, a total of 650 questionnaires were distributed to individuals entrusted by the company to make decisions on matters pertaining to import tax. Of the 650 questionnaires distributed, 279 or 42.92% of the questionnaires were answered and returned. Of the 279 returned questionnaires, 34 questionnaires were removed from the data sets and 5 were identified as outliers. Finally, only 245 could be used for analysis purposes. This sample size ( $n = 245$ ) was sufficient and suitable for the analysis of this study as proposed by Hair et al., (2010) and Sekaran and Bougie, (2011).

This section describes the summary of the survey respondents' and company profile as summarised in Table 8.29. The profile captured the respondent demography, which includes: designation, gender and ethnicity. The sample profile also included the demography of the company of the respective respondents, namely: business category, number of clients the company represents, number of Customs declarations issued per month and the location of registration of the agents' license.

##### **(a) Designation**

In terms of designation of the persons entrusted by the company to be responsible for Customs related matter, directors recorded the highest number of respondents (40%), followed by managers (32.10%), and executives (17.90%).

##### **(b) Gender**

The respondents comprised of male (77.10%) and female (22.90%). The data correspond with the actual environment where it is common that Customs brokerage industry in Malaysia is male dominated.

##### **(c) Ethnicity**

Ethnicity of the respondent comprised of three main races, Chinese, Malay and Indian. Chinese represented the largest respondents group (51.30%), Malay came second at 32.50%, while Indian accounted for 15% of the respondents. Other minority groups accounted for 1.30%, which represented the ethnicity of Singh and other races such Siamese indigenous in Malaysia.

**Table 8.29: Descriptive Statistics for Frequency Distribution of Respondents (n = 245)**

		<b>Frequency</b>	<b>Percent (%)</b>
<b>Designation</b>	Director	98	40.00
	Manager	78	31.80
	Executives	44	18.00
	Others	25	10.20
	Total	245	100.00
<b>Gender</b>	Male	190	77.60
	Female	55	22.40
	Total	245	100.00
<b>Ethnicity</b>	Malay	80	32.70
	Chinese	125	51.00
	Indian	37	15.10
	Others	3	1.20
	Total	245	100.00
<b>Business Category</b>	Limited	14	5.70
	Private Limited	178	72.70
	Partnership	38	15.50
	Sole Proprietorship	15	6.10
	Total	245	100.00
<b>Years license obtained</b>	< 1 years	12	4.90
	1 – 5 years	24	9.80
	6 – 10 years	46	18.80
	11 – 15 years	47	19.20
	> 15 years	116	47.30
	Total	245	100.00
<b>Number of clients</b>	< 25	34	13.90
	25 - 50	48	19.60
	51 - 75	49	20.00
	76 - 100	29	11.80
	> 100	85	34.70
	Total	245	100.00
<b>Number of Customs declaration</b>	< 50	38	14.30
	50 – 150	85	34.70
	151 – 300	61	24.90
	301 – 500	27	11.00
	> 500	37	15.10
	Total	245	100.00
<b>Location of licence issued</b>	Selangor	96	40.00
	Johor	63	26.30
	Pulau Pinang	48	20.00
	KLIA	33	13.80
	Total	245	100.00

**(d) Business Category**

Meanwhile, the data on business profile showed that private limited company represented the largest group in the industry, which accounted for 73.30%. Partnership and sole proprietorship accounted for 21.3% for both, while limited company accounted only 5.4% of the respondents.

**(e) Years licence obtained**

Years licence obtained indicate the number of years the agents have held the Customs agents licence since the company licence was first approved by the Malaysian Customs Department. The data revealed that majority of the companies that had the licence to operate the service as Customs agents for more than 15 years. Only about 15% have had the licence for less than 5 years, while the remaining 35% have had the licence for 6 to 15 years. These results indicated that the responding Customs agents were already established in their business.

**(f) Number of Clients**

The number of companies that holds more than 100 clients accounted for 35.40%. 40% of the companies had equal number of clients, ranging between 25 to 50 and 51 to 75. Companies that had less than 25 clients accounted only 12.1%.

**(g) Number of Import Declaration**

Out of 245 responses, 34% of the companies produced between 50 to 150 numbers of Customs import declarations, while 25.4% produced between 151-300 Customs import declarations. Companies which produced less than 50 and over 500 Customs import declarations had almost equal distributions which are 14.3% and 15.1% respectively.

**(h) Location of Issuance of Licence**

As expected from the disproportionate size of agents across Malaysia, the largest survey responses was recorded in the central region (Selangor and KLIA), which accounted for half of the total received survey responses compared to the northern (Pulau Pinang) and southern regions (Johor). As presented earlier in Chapter 6, the central region had the largest population of agents compared to the other two regions.

## **8.6 STRUCTURAL EQUATION MODELING**

### **8.6.1 Data Examination**

This section presents the evaluation of the Partial Least Squares (PLS) research model, which explains agents' tax compliance behaviour. There were thirteen constructs reflected in the model. Eleven of these constructs (attitude, primary subjective norm, secondary subjective norm, perceived behaviour control, knowledge law, law enforcement, ethics, complexity of procedure, intention and behaviour) were measured by reflective indicators, while the other two constructs (exchange of fairness and tax assessment service quality) were measured by formative indicators.

As discussed in Chapter 6, the constructs with formative and reflective indicators were two distinguished types of constructs requiring different methods to assess the measurement and structural models. The following section describes the relevant tests performed to evaluate the measurement model according to the nature of the constructs.

### **8.6.2 PLS Model Measurement**

#### **(a) Reflective Constructs**

The following demonstrate the results from the testing of reflective constructs. The test include those on indicator reliability (item loadings), internal consistency reliability (composite reliability), convergent validity (average variance extracted (AVE) analysis) and discriminant validity (square root of AVE and cross loading analysis) using the guidelines provided in Hair, Ringle, et al., (2011) and Chin, (2010). The results of these validity and reliability tests would provide a level of assurance that the survey items measured the constructs they were designed to measure.

##### **(i) Indicator reliability**

As described previously in chapter 6, the indicators reliability was considered to be reliable when the threshold value of the indicator loading value was above 0.70. In the initial stage of indicator reliability assessment, indicators with loading value of lower than 0.40 were eliminated. The majority of the indicator loadings showed value

higher than 0.70 after the initial assessment. The only construct that had an indicator loading of 0.40 was the newly introduced construct of ‘complexity of procedure’, which indicated a loading of 0.491(PR1). There were also few indicators with loading below 0.70 for the constructs of behavioural intention, attitude and law enforcement, which were 0.609(INT3), 0.681(ATT6), 0.685(ATT7) and 0.656(ENF3), respectively. After careful examination, it was found that there were insignificant changes to the composite reliability of the constructs when the indicator was removed. Furthermore, the composite reliability of these construct already achieved the value of composite reliability of more than 0.70. It was suggested that an indicator could be considered for removal if there was substantial increase in composite reliability as a result of the indicator removal (Hair, Ringle, et al., 2011; Henseler et al., 2009). Therefore, the remaining indicator for behavioural intention, attitude and law enforcement were retained, consistent with the recommendation by Hair et al., (2011) and Henseler, Ringle, and Sinkovics, (2009). There were also several indicators for the constructs of ‘law’ and ‘ethics’, which were removed due to low indicator loading. As a result of the removal, these two constructs were left with two indicators each, which met the minimum rule of two indicators for each construct (Bagozzi and Heatherton, 1994; Rahim, Antonioni, and Psenicka, 2001).

In total, six constructs were affected with the removal of indicators, namely 1) Attitude (ATT1, ATT2, ATT3 and ATT8); 2) Ethics (ETH3,ETH4 and ETH5); 3) Knowledge (KN1); Law (LAW2, LAW4 and LAW 5); 4) Enforcement (ENF 1 and ENF 4); and 5) Complexity of Procedure (PR 2, PR4 and PR 6). The details are described as follows:

- Attitude

All eight items measuring ‘Attitude’ are reflective in nature, which consists of emotional component and perceived outcome component. Removal of four indicators (ATT1, ATT2, ATT3 and ATT8) does not alter the meaning of the construct. The remaining indicator (ATT4, ATT5, ATT6 and ATT7) suffice the conceptualisation of emotional and perceived outcome for the construct of ‘Attitude’

- Ethics

Five indicator measuring ethics are also reflective in nature. It measures the ethical belief that tax under-declaration as morally right or wrong. Removal of



indicator (ETH3, ETH4 and ETH5), still retained the conceptual meaning of ‘Ethics’ as described in Chapter 5.3.3, as the remaining questions (ETH1 and ETH2) relates to the operation definition of ethics, where tax under-declaration perceived as ethical or unethical.

- Knowledge

Only one out of five indicators for ‘Knowledge’ was removed due to low factor loading. The removal of indicator KN1 does not affect the construct definition as the remaining indicators (KN2, KN3, KN4 and KN5) supports the operational definition and uni-dimensionality of the construct.

- Law and Law Enforcement

Five indicators measuring each construct of ‘Law’ and ‘Law Enforcement’. Three indicators (LAW2, LAW4, and LAW5) for law and two indicators (ENF1 and ENF4) were removed due to low factor loadings. The removal of these indicators does not alter the meaning of the constructs as these constructs are reflective in nature and uni-dimension constructs. The remaining indicators (LAW1 and LAW 3) support the operational definition of law. It relates to the question about the ambiguity and implementation of law which are the control measure of an institution which induce compliance behaviour whether it makes compliant difficult or easy for the public. Similarly for the construct of ‘Law Enforcement’, the remaining indicators (ENF2, EN3 and ENF5) are related to the operational definition of enforcement which consists of detection, prosecution, stringent enforcement of an institution.

- Complexity of Procedure

As highlighted in the beginning of this section, construct of ‘Complexity of Procedure’ indicate the lowest score in terms of indicator loading. Three indicators (PR2, PR4 and PR6) were removed. The remaining five indicators (PR1, PR3, PR5, PR7 and PR8) are aligned with the operational definition of ‘Complexity of Procedure’. The indicators relates to the uni-dimensional of the construct that measures complexity, i.e. frequent changes in procedure, flexibility, timeliness, uniformity of procedure, rigidness of procedure that would make compliance easy (or difficult).

**Table 8.30: Assessment of Reflective Measurement Model**

Constructs	Items	Loadings	Composite Reliability	AVE	Mean	Std Deviation
Attitude	ATT4	0.889	0.866	0.622	4.205	0.561
	ATT5	0.873				
	ATT6	0.685				
	ATT7	0.684				
Primary Subjective Norm	NB1	0.873	0.954	0.839	4.116	0.641
	NB2	0.935				
	NB3	0.922				
	NB4	0.933				
Secondary Subjective Norm	NI1	0.874	0.937	0.788	4.073	0.638
	NI2	0.942				
	NI3	0.909				
	NI4	0.821				
Perceived Behavioural Control	PBC1	0.805	0.899	0.641	4.110	0.506
	PBC2	0.826				
	PBC3	0.821				
	PBC4	0.728				
	PBC5	0.820				
Behavioural Intention	INT1	0.783	0.928	0.651	4.312	0.461
	INT2	0.884				
	INT3	0.609				
	INT4	0.900				
	INT5	0.892				
	INT7	0.783				
	INT8	0.758				
Behaviour	BEH1	0.711	0.929	0.687	3.653	0.959
	BEH2	0.769				
	BEH3	0.837				
	BEH4	0.900				
	BEH5	0.863				
	BEH6	0.877				
Ethics	ETH1	0.891	0.814	0.687	4.099	0.604
	ETH2	0.762				
Knowledge	KN2	0.693	0.814	0.527	3.274	0.804
	KN3	0.859				
	KN4	0.748				
	KN5	0.558				
Perception of Law	LAW1	0.922	0.839	0.724	3.325	0.891
	LAW3	0.770				
Law Enforcement	ENF2	0.751	0.758	0.512	3.617	0.707
	ENF3	0.656				
	ENF5	0.740				
Complexity of Procedure	PR1	0.491	0.824	0.500	2.945	0.776
	PR3	0.683				
	PR5	0.558				
	PR7	0.880				
	PR8	0.805				

## **(ii) Composite reliability**

The final results after the assessment of indicator loading indicated that generally, the data is robust in terms of its internal consistency and reliability as indexed by the composite reliability. The composite reliability of the different measures ranged from 0.758 to 0.954, which exceeds the recommended threshold value of 0.70. The result of the composite reliability is presented in Table 8.30.

## **(iii) Convergent Validity**

Assessment of the validity of the constructs was performed through the average variance extraction (AVE) method. The value of AVE is considered as valid when the value achieve a threshold of 0.50 and above, which indicates that a construct is able to explain more than 50% of the variance. The AVE for eleven of the constructs exceeded the recommended value of 0.50. Initially, the constructs of attitude and complexity of procedure indicated AVE of less than 0.50. However, the values subsequently improved when the low loading indicators were removed. The result of AVE is presented in Table 8.30.

## **(iv) Discriminant validity**

The subsequent stage of assessing the model measurement was the discriminant validity. Discriminant validity is achieved when the indicator loads more highly on its own construct as compared to other constructs or correlate weakly with all other constructs. The procedures applied to evaluate discriminant validity were (1) the square root of the AVE values and (2) assessment of the loadings and cross loadings matrix.

Here, the first procedure determined discriminant validity through AVE analysis. The square root of the AVE for each construct had to be larger than any other constructs and the correlation between the respective construct. The correlation matrix in Table 8.31 indicates that the square roots of AVE were greater than the other constructs. The result suggests that there is evidence of discriminant validity in the respective constructs in the model.

**Table 8.31: Discriminant Validity (Intercorrelations) of Latent Constructs**

Latent Variable		1	2	3	4	5	6	7	8	9	10	11
1.	ATT	<b>0.79</b>										
2.	BEHAV	0.12	<b>0.83</b>									
3.	ENFORCE	0.01	-0.07	<b>0.72</b>								
4.	ETHIC	0.17	-0.03	0.10	<b>0.83</b>							
5.	INTENT	0.22	-0.02	0.21	0.52	<b>0.81</b>						
6.	KNOW	-0.05	0.10	-0.10	-0.04	-0.10	<b>0.72</b>					
7.	LAW	0.05	0.16	0.42	-0.10	0.03	0.01	<b>0.92</b>				
8.	NORM1	0.22	-0.13	0.12	0.45	0.36	0.09	-0.11	<b>0.92</b>			
9.	NORM2	0.08	-0.24	0.07	0.45	0.45	0.05	-0.03	0.70	<b>0.89</b>		
10.	PBC	0.13	-0.17	0.10	0.48	0.54	-0.01	0.00	0.41	0.49	<b>0.80</b>	
11.	PROCEDR	0.28	0.26	0.12	-0.13	-0.25	0.08	0.44	-0.03	-0.10	-0.20	<b>0.71</b>

The second procedure determined discriminant validity by assessing the cross loading matrix of latent constructs to ensure that the indicator loads higher for the assigned construct compared to other constructs in the correlation matrix. These results are presented in table 8.32 and indicate that all items loaded on their own constructs higher than any other constructs in the matrix table. For instance, indicators for the construct of behaviour (BEH1, BEH2, BEH3, BEH4, BEH5 and BEH6) loaded higher in the behaviour (BEHAV) column compared to its own loading in other column, suggesting that the indicators for behaviour construct were the appropriate measures of compliance behaviour. The result of construct items loadings and cross loadings revealed that discriminant validity was achieved at the item level.

**Table 8.32: Outer Model Loading and Cross Loadings**

	ATT	BEHAV	ENF	ETH	INTENT	KNOW	LAW	NRM1	NRM2	PBC	PROCD
ATT4	<b>0.89</b>	0.15	-0.03	0.20	0.21	-0.01	0.09	0.18	0.07	0.09	0.28
ATT5	<b>0.87</b>	0.09	0.03	0.15	0.18	-0.02	-0.04	0.20	0.04	0.12	0.21
ATT6	<b>0.68</b>	0.02	0.05	0.09	0.16	-0.07	0.06	0.15	0.10	0.10	0.25
ATT7	<b>0.68</b>	0.06	-0.01	0.05	0.13	-0.09	0.05	0.16	0.06	0.10	0.10
BEH1	0.14	<b>0.71</b>	-0.02	0.00	-0.01	0.06	0.03	-0.06	-0.14	-0.10	0.13
BEH2	0.12	<b>0.77</b>	-0.14	-0.06	-0.03	0.07	0.10	-0.15	-0.20	-0.12	0.16
BEH3	0.15	<b>0.84</b>	-0.03	0.00	0.03	0.06	0.10	-0.06	-0.17	-0.13	0.26
BEH4	0.12	<b>0.90</b>	-0.04	-0.08	-0.02	0.09	0.22	-0.17	-0.23	-0.15	0.23
BEH5	0.04	<b>0.86</b>	-0.05	0.00	-0.04	0.09	0.12	-0.09	-0.21	-0.20	0.24
BEH6	0.05	<b>0.88</b>	-0.06	0.04	0.00	0.12	0.15	-0.08	-0.20	-0.11	0.26
ENF2	-0.06	-0.17	<b>0.75</b>	0.07	0.14	-0.04	0.31	0.09	0.05	0.02	0.12
ENF3	0.05	0.03	<b>0.66</b>	0.05	0.09	-0.07	0.25	0.17	-0.03	0.12	0.14
ENF5	0.06	0.05	<b>0.74</b>	0.08	0.19	-0.11	0.32	0.04	0.09	0.11	0.02
ETH1	0.18	0.03	0.03	<b>0.89</b>	0.51	-0.11	-0.11	0.41	0.41	0.49	-0.11
ETH2	0.08	-0.10	0.15	<b>0.76</b>	0.32	0.07	-0.04	0.33	0.34	0.28	-0.10
INT1	0.19	0.01	0.13	0.36	<b>0.78</b>	-0.10	-0.01	0.29	0.39	0.42	-0.20
INT2	0.17	0.02	0.13	0.50	<b>0.88</b>	-0.14	0.00	0.31	0.39	0.48	-0.23
INT3	0.07	-0.02	0.18	0.41	<b>0.61</b>	-0.05	0.03	0.18	0.33	0.32	-0.13
INT4	0.20	0.10	0.21	0.41	<b>0.90</b>	-0.15	0.08	0.28	0.37	0.45	-0.18
INT5	0.20	0.06	0.21	0.44	<b>0.89</b>	-0.12	0.04	0.27	0.37	0.46	-0.19
INT7	0.18	-0.12	0.16	0.37	<b>0.78</b>	-0.01	0.04	0.36	0.38	0.43	-0.25
INT8	0.24	-0.14	0.18	0.41	<b>0.76</b>	0.02	-0.02	0.32	0.30	0.47	-0.20
KN2	-0.01	0.04	-0.03	-0.04	-0.03	<b>0.69</b>	-0.05	0.09	0.08	0.00	-0.03
KN3	0.03	0.09	-0.11	-0.05	-0.09	<b>0.86</b>	0.01	0.09	0.00	-0.02	0.10
KN4	-0.13	0.09	-0.05	-0.01	-0.08	<b>0.75</b>	0.03	0.05	0.07	0.00	0.07
KN5	-0.09	0.08	0.01	0.02	0.01	<b>0.56</b>	0.04	0.04	0.03	0.04	0.08
LAW1	0.02	0.15	0.37	-0.04	0.08	0.02	<b>0.92</b>	-0.06	-0.01	0.07	0.36
LAW3	0.08	0.11	0.35	-0.17	-0.07	-0.02	<b>0.77</b>	-0.15	-0.05	-0.12	0.43
NB1	0.20	-0.04	0.17	0.43	0.31	0.08	-0.10	<b>0.87</b>	0.60	0.31	-0.06
NB2	0.20	-0.12	0.13	0.43	0.36	0.09	-0.11	<b>0.93</b>	0.63	0.34	-0.01
NB3	0.20	-0.15	0.07	0.37	0.32	0.06	-0.10	<b>0.92</b>	0.68	0.42	-0.01
NB4	0.18	-0.16	0.05	0.42	0.33	0.10	-0.10	<b>0.93</b>	0.65	0.44	-0.03
NI1	0.07	-0.21	0.09	0.41	0.41	0.02	0.00	0.65	<b>0.87</b>	0.45	-0.08
NI2	0.07	-0.20	0.05	0.46	0.43	0.06	-0.03	0.66	<b>0.94</b>	0.46	-0.07
NI3	0.04	-0.22	0.03	0.37	0.39	0.11	-0.02	0.56	<b>0.91</b>	0.46	-0.07
NI4	0.11	-0.21	0.06	0.36	0.36	-0.02	-0.07	0.59	<b>0.82</b>	0.38	-0.13
PBC1	0.14	-0.19	0.10	0.39	0.44	-0.01	0.01	0.31	0.29	<b>0.81</b>	-0.14
PBC2	0.17	-0.01	0.11	0.44	0.46	-0.04	0.01	0.30	0.32	<b>0.83</b>	-0.08
PBC3	0.09	-0.18	0.04	0.38	0.44	-0.02	-0.02	0.29	0.38	<b>0.82</b>	-0.21
PBC4	0.01	-0.12	0.02	0.30	0.34	0.00	-0.14	0.33	0.44	<b>0.73</b>	-0.22
PBC5	0.09	-0.16	0.10	0.40	0.47	0.01	0.09	0.43	0.55	<b>0.82</b>	-0.16
PR1	0.17	0.30	0.19	0.02	0.02	0.01	0.42	-0.05	0.01	0.02	<b>0.49</b>
PR3	0.19	0.12	0.20	-0.07	-0.09	0.05	0.36	0.04	-0.05	-0.15	<b>0.68</b>
PR5	0.21	0.29	-0.15	-0.06	-0.12	0.13	0.14	0.06	0.03	-0.05	<b>0.56</b>
PR7	0.20	0.15	0.12	-0.11	-0.25	0.01	0.36	-0.05	-0.11	-0.19	<b>0.88</b>
PR8	0.25	0.27	0.18	-0.11	-0.18	0.09	0.47	-0.08	-0.10	-0.16	<b>0.81</b>

## **(b) Formative constructs**

As discussed in Chapter 6, the evaluation of formative measurement required different approaches due to the different nature and characteristics from reflective construct. Assessment of formative measurement model was performed by evaluating the indicator weight, t-statistics and multicollinearity.

### **(i) Indicator weight and t-statistics**

Indicator weight and t-statistics provide an indication on construct validity and its significance in explaining the variance in the formative construct (Petter et al., 2007). The bootstrapping procedure was applied in evaluating the indicator weight and t-statistics. The number of bootstrap samples of 5000 with the number of cases according the original samples as suggested by Hair et al., (2011) was applied in this procedure.

The results, as presented in Table 8.33, reveals that the formative indicators for the construct of ‘exchange of fairness’ was statistically significant. On the other hand, the construct of ‘quality of service’ indicated a mixture of significance and non-significance for ten indicators measuring the constructs. Four (SQ1, SQ2, SQ9 and SQ10) out of ten indicators measuring the construct of ‘quality of service’ were found to be insignificant, while the other six indicators (SQ3, SQ4, SQ5, SQ6, SQ7 and SQ8) were significant. There were several reasons that can cause indicators to be non-significant, such as the existence of heterogeneous data structure and redundancy in indicator information due to high level of multicollinearity in the formative measurement model (Cenfetelli and Bassellier, 2009; Hair, Ringle, et al., 2011).

There are different views on the treatment of non-significant indicators. It is suggested that any non-significant indicator should be eliminated to achieve all significant paths (Diamantopoulos and Winklhofer, 2001), while there are views that eliminating the indicator would affect the content validity (Bollen and Lennox, 1991; Cohen, Teresi, Marchi, and Velez, 1990; Diamantopoulos and Siguaw, 2006) and alter the conceptual meaning of the constructs (Coltman et al., 2008; Henseler et al., 2009; Jarvis et al., 2003). It was decided that the non-significant indicators were retained based on the decision that the conceptual meaning is more influential on the constructs (Hair, Ringle, et al., 2011; Henseler et al., 2009; Petter et al., 2007) as opposed to statistical relevance, especially for the construct of ‘quality of service’ that

has been well conceptualised and established. Furthermore, ten of the indicators to measure the formative construct have been established through content validity process as suggested by Hair, Ringle, et al., (2011) and Petter et al., (2007). Content validity can be established through the review of literature (Petter et al., 2007) and expert opinions (Boudreau, Gefen, and Straub, 2001; Hair, Ringle, et al., 2011). Since the construct of service quality was newly applied in tax compliance studies, relevant inter-disciplinary literatures were reviewed to ensure that the measure used for the domain of construct was fully captured. As described in Section 6.3.3, experts in the field of taxation and research methodology were also asked to review and comments on the initial questionnaire during the pre-test stage of this study to establish the content validity of the survey instrument.

**Table 8.33: Assessment of Formative Measurement Model**

<b>Constructs and items</b>	<b>Weights</b>	<b>t-Statistics</b>	<b>Significance Level</b>
<b>Exchange of Fairness</b>			
FA1	0.433	2.3236	0.010
FA2	0.644	3.7026	0.005
FA3	0.583	3.7153	0.005
<b>Quality of Service</b>			
SQ1	-0.057	0.2796	not sig
SQ2	-0.491	0.2733	not sig
SQ3	0.428	1.8226	0.005
SQ4	-0.418	1.8022	0.005
SQ5	1.036	1.6024	0.010
SQ6	0.378	3.8279	0.005
SQ7	-0.372	1.6064	0.050
SQ8	0.045	1.5048	0.050
SQ9	0.202	0.1678	not sig
SQ10	-0.069	0.7795	not sig

**(ii) Multicollinearity**

The subsequent approach on the evaluation of formative model measurement was through the variance inflation factor (VIF). The purpose of this approach served as a redundancy check by calculating the VIF to determine the level of multicollinearity. The multicollinearity test was performed with SPSS with the inclusion of the indicators for the formative construct of ‘exchange of fairness’ and ‘quality of service’. The value of VIF of less than 5 can be considered as an indication of multicollinearity, whereas any value higher than 5 indicates potential multicollinearity problem, which implies that 80 percent of an indicator’s variance is accounted for by the remaining formative indicators related to the same construct.

The results, as presented in Table 8.34, reveal the average tolerance level of 0.99 and VIF of 1.00 for the construct ‘exchange of fairness’. The construct of ‘quality of service’ indicated tolerance level ranging from 0.39 to 0.65 and VIF level from 1.52 to 2.57. The result of the test revealed that multicollinearity was not a concern for both of the constructs indicators as the VIF indicates a value of less than 5 for both construct indicators.

**Table 8.34: Multicollinearity of Formative Constructs**

Constructs and indicator	Multicollinearity Statistics	
	Tolerance	VIF
<b>Exchange of Fairness</b>		
FA1	0.993	1.007
FA2	0.999	1.001
FA3	0.993	1.007
<b>Quality of Service</b>		
SQ1	0.655	1.527
SQ2	0.391	2.560
SQ3	0.498	2.010
SQ4	0.389	2.570
SQ5	0.418	2.390
SQ6	0.496	2.015
SQ7	0.446	2.241
SQ8	0.349	2.867
SQ9	0.378	2.647
SQ10	0.412	2.424



### 8.6.3 PLS Structural Model

The subsequent step after the model measurement was to evaluate the structural model to estimate the model's predictive power and the stability of the estimates. This procedure involved the following steps: (1) applying the  $R^2$  measures, (2) bootstrapping procedure, (3) blindfolding technique and (4) predictive relevance. Finally, the global goodness of fit index was applied to assess the overall model fit.

#### (a) Variance Explained ( $R^2$ )

The purpose of  $R^2$  measures was to assess the predict the power of the structural model through the  $R^2$  value of the endogenous latent constructs and to examine the effect size to evaluate the predictor construct (independent variables) whether the construct has a significant influence on the endogenous construct (dependent variable). In simpler term, it assessed to what extent the independent variables helped to explain the dependent variables.  $R^2$  value indicates the variation in the dependent variables that cannot be explained by the independent variables. A higher value of  $R^2$  indicates greater influence of the predictor construct<sup>37</sup>. In this instance, the perfect prediction value is 1 with zero unexplained variation.

There are different judgements on the value of  $R^2$ , which could be applied as guidelines in determining the level of strength or weakness in the structural model. The value of 0.25 is considered as weak in marketing literature (Hair, Ringle, et al., 2011), whereas in consumer behaviour discipline, 0.20 is judged as a strong prediction value (Bogue, Coleman, and Sorenson, 2005; Hair, Ringle, et al., 2011). In some other behavioural studies involving health behaviour, it was also reported that  $R^2$  of 0.20 as an acceptable prediction value (Harrison et al., 2003; Peel, McClure, and Hendrikz, 2006). In other studies involving user behaviour and other similar studies in tax behaviour and exploratory studies,  $R^2$  value of 0.10 is considered as an acceptable level to explain the percentage of variance in the study (Hanlon, 1999; Park, Kee, and Valenzuela, 2009; Saad, 2011), which was supported by Gaur and Gaur, (2009), in which  $R^2$  of 0.10 to 0.20 is considered as acceptable in social science research. Based on this justification, in this study, the minimum level of 0.10-0.20 was considered as

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<sup>37</sup> There is no definite guideline established in assessing  $R^2$  values to indicate a 'strong' or 'weak' construct in structural model. The value differs according to research discipline (Hair, Ringle, et al., 2011).

an adequate  $R^2$  for the purpose of determining the prediction power of the structural model. The full result of the R-squares is presented in Table 8.35

**Table 8.35: Variance Explained ( $R^2$  Values)**

<b>Construct</b>	<b><math>R^2</math></b>
Behavioural Intention	0.498
Ethics	0.241
Behaviour	0.083
Attitude	0.028

**(i) R-square of Behavioural Intention**

The  $R^2$  value of 0.498 for the behavioural intention revealed that the model accounted for 50 percent of the variance of the construct. The model in this study was able to explain 49.8 percent of the variance in the agents' behavioural intention on tax compliance. This suggests that there was a significant influence of the independent constructs on the dependent construct (behavioural intention) in this model.

**(ii) R-square of Ethics**

The  $R^2$  value of ethics indicates the extent to which the primary subjective norm (importer) and the secondary subjective norm (other agents) helped to explain the construct of ethics.  $R^2$  value of 0.241 for ethics indicates that the model in this study explained 24.1 percent of the variance in the agents' ethical belief on tax compliance. This result suggests that there was a strong indication of the influence of both importer and other agents on the agents' ethical belief towards tax compliance.

**(iii) R-square of Behaviour**

$R^2$  value of 0.083 for behaviour suggests that the independent constructs explained only 8.3 percent variance in the model. In other words, the independent constructs were able to explain only 8.3 percent of the compliance behaviour. This figure, however, was slightly lower than the average acceptance level of 10 percent or 0.10. This result suggests that not only the perception of law, enforcement, perceived behavioural control (PBC) and behavioural intention had a marginal influence on

compliance behaviour, but it also indicates that there were other factors to explain about 92 percent of the variance in the behaviour. There are also possibilities that moderating factors that influence the relationships or the type of questions might affect the interaction because it demonstrates the actual compliance behaviour.

**(iv) R-square of Attitude**

Similar to  $R^2$  for behaviour,  $R^2$  value for attitude indicates a lower value than behaviour.  $R^2$  value of 0.028 for attitude, accounted only 2.8 percent of the variance in the construct. Another 97 percent of other factors explained the variance on attitude. This result suggests that the construct of ethics in the model might not be the strongest predictor for attitude towards tax compliance. There were other combinations of prediction factors that could better explain tax compliance attitude.

**(b) Significance Test of Path Coefficients**

The second step in the structural model evaluation was using the bootstrapping procedure. Bootstrapping was used to test the path coefficient significance. Paths that show sign of contrary to the hypothesized direction indicate that the hypothesis is not supported, whereas significant path indicates that the hypothesis is supported. This procedure involved creating  $n$  sample sets in order to obtain  $n$  estimates for each parameter in the model. Each sample was obtained by sampling with replacements from the original data set until the number of cases was identical to the original sample set. The suggested minimum number was 5000 and the number of cases should be equal to the number of observations in the original sample.

The results of the bootstrapping procedure to analyse the path coefficient are presented in table 8.36, which reported the effect of each independent constructs on its corresponding dependent constructs, the path coefficients, the  $t$ -statistics and the respective  $p$ -value to indicate the level of significance. In addition, the graphical representation (SmartPLS output) of the findings from the model are presented in Figure 8.1 and 8.2.

**Table 8.36: Summarised Results from the Evaluation of the Structural Models**

<b>Propositions</b>	<b>Path Coefficient</b>	<b>t-statistics</b>	<b>Significance Level</b>
<b>Effect on Intention (<math>R^2 = 0.498</math>)</b>			
Attitude	0.207	3.835	0.01
Norm 1 (Importer)	0.183	2.605	0.05
Norm 2 (Other Agents)	-0.043	0.583	not sig
PBC	0.243	4.073	0.01
Law	0.104	1.587	0.10
Enforcement	0.108	1.997	0.05
Knowledge	-0.047	0.693	not sig
Ethics	0.198	2.868	0.05
Procedure	-0.273	4.443	0.01
Exchange Fairness	0.072	1.259	not sig
Quality Service	0.100	1.723	0.05
<b>Effect on Behaviour (<math>R^2 = 0.083</math>)</b>			
Intention	0.136	1.768	0.05
Law	0.226	2.162	0.05
Enforcement	-0.173	1.017	not sig
PBC	-0.223	2.893	0.01
<b>Effect on Ethics (<math>R^2 = 0.241</math>)</b>			
Norm 1 (Importer)	0.269	3.214	0.01
Norm 2 (Other Agents)	0.263	2.407	0.05
<b>Effect on Attitude (<math>R^2 = 0.028</math>)</b>			
Ethics	0.168	2.223	0.05

**(i) Effect on Behavioural Intention**

The result as presented in Figure 8.1 and Figure 8.2 demonstrates significant path for all independent constructs on behavioural intention except for constructs of Norm 2 - Other Agents, Knowledge and Exchange of Fairness, which had very weak path coefficients ( $\beta$  between -0.043 to 0.072). Attitude, PBC and Procedure had the strongest path coefficients of  $\beta = 0.207$ ,  $0.243$  and  $-0.273$  respectively at 0.01 significant level. The other four path coefficients for Norm 1- Importer ( $\beta = 0.183$ ), Enforcement ( $\beta = 0.108$ ), Ethics ( $\beta = 0.198$ ), Quality of Service ( $\beta = 0.100$ ) reflected moderate relationships with behavioural intention at a significance level of 0.05. The

perception on law reflected a marginal relationship with behavioural intention at 0.10 significance level. There were a number of studies which accepted a p-value of 0.10 (example Hasseldine, Kaplan, and Fuller, 1994; Jones, Sundaram, and Chin, 2002). Furthermore, significance level of 0.10 is considered as acceptable in behavioural research, which is exploratory in nature (Russell, Jarvis, and Collis, 2008).

**(ii) Effect on Behaviour**

The effect of PBC, Behavioural Intention and Law on Behaviour indicated a significant path with the exception of Enforcement. PBC demonstrated the most significant relationship with a path coefficient of  $\beta = -0.223$  at 0.01 significance level, while Behavioural Intention and Law indicated moderate relationships at 0.05 significance level.

**(iii) Effect on Ethics**

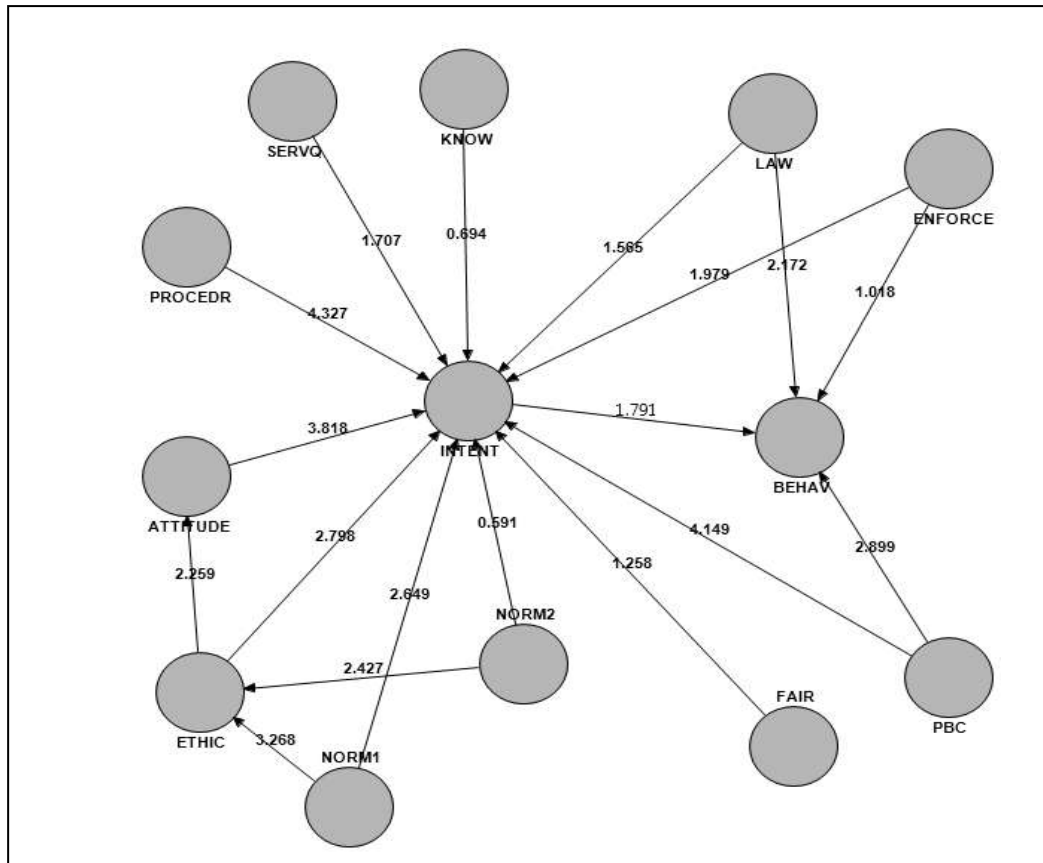
The constructs of Primary and Secondary Subjective Norm (Importers and Other Agents) reflected significant paths with Ethics. The results show path coefficients of  $\beta = 0.269$  and  $\beta = 0.263$ , respectively at significance level of at least 0.05.

**(iv) Effect on Attitude**

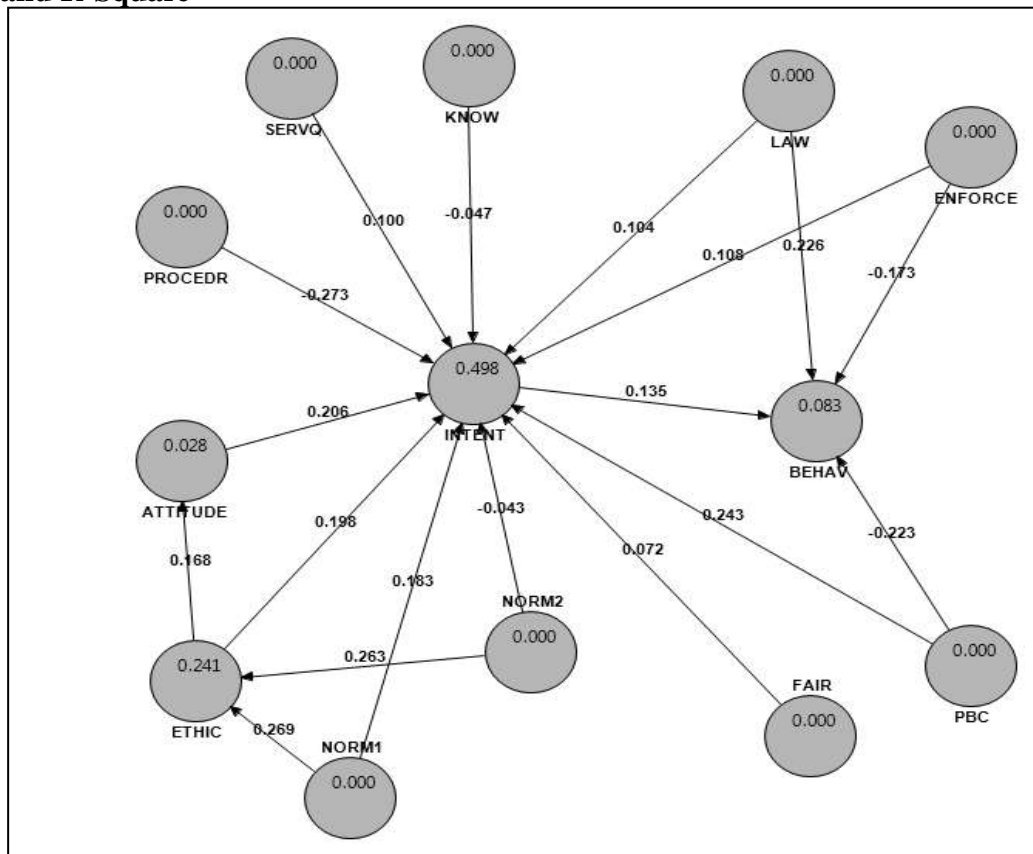
The effect of ethics revealed that there was a significant relationship with attitude towards tax compliance. The path coefficient was  $\beta = 0.168$  at 0.05 significance level.

In summary, overall the results indicate that behavioural intention, behaviour, ethics and attitude displayed relatively good fit in the model and the samples overall. The results demonstrate a mixture of strength in the relationships. The majority of the paths show significant and moderate relationships, while few indicate modest or no relationship at all, as expected in the model with many constructs and path indicators.

**Figure 8.1: Structural Model Results from SmartPLS Output– T-Statistics**



**Figure 8.2: Structural Model Results from SmartPLS Output– Path Coefficient and R-Square**



### (c) Predictive Relevance

In addition to the size of  $R^2$  as described previously, the predictive sample reuse technique (Stone-Geisser's  $Q^2$ ) was applied. The test of blindfolding technique was performed using the omission distance,  $d$  of 7 (within the suggested  $d$  value ranging between 5 and 10) in the SmartPLS program. The test was applied on all independent constructs that have the reflective measurement model (Hair, Ringle, et al., 2011). The results (table 8.37) of the test demonstrate  $Q^2$  for the dependent constructs of attitude, behaviour, ethics and behavioural intention ranged from 0.622 to 0.686, which were indicative of a highly predictive model.

**Table 8.37: Cross Validation Redundancy ( $Q^2$ )**

Exogenous Constructs	$Q^2$ Value
ATTITUDE	0.6218
BEHAVIOUR	0.6863
ETHIC	0.6857
BEHAVIOURAL INTENTION	0.6508

#### 8.6.4 Conclusion of Hypothesis Testing

The preceding sections (8.6.2 and 8.6.3) provided evidence of the adequacy on the measurement and structural models for the studied samples. This section links the results to the hypotheses established in Chapter 7 in order to ascertain which of these hypotheses were supported as results of the analyses.

This section, therefore, presents the hypotheses results of this study based on the statistical outcomes, which evaluated both measurement and structural models of this study, referred to as The Agents Compliance Behaviour Model (CBM). Every significant relationship identified in table 8.36 was characterised by a path coefficient of more than 0.1, and therefore, could not be neglected (Chin, 1998; Sellin and Keeves, 1994). The hypotheses testing results indicate that fourteen out of eighteen hypotheses were supported and only four were not supported, and therefore, rejected.

Hypothesis 1, which stated that agents' behavioural intention (*INTENT*) will have a positive influence on their tax compliance behaviour (*BEHAV*) was fully supported ( $\beta = 0.136$ ,  $t = 1.768$ ,  $p < 0.05$ ), with the paths linking behavioural intention

and behaviour being positive. The result was consistent with TPB, which posits that behavioural intention is the immediate antecedent of behaviour.

Hypothesis 2 addressed the relationship between attitude (*ATT*) and behavioural intention (*INTENT*). The results ( $\beta = 0.136$ ,  $t = 1.768$ ,  $p < 0.05$ ) displayed a positive and significant influence of attitude on tax and behavioural intention to comply. The results were also consistent as theorised in TPB, which states that attitude has an immediate direct effect on behavioural intention.

Hypotheses 3a and 3b evaluated the relationship between primary subjective norm or importer (*NORM1*) with behavioural intention (*BI*) and ethical belief (*ETHICS*). In support of hypotheses 3a and 3b, importer had a significant influence on agents' behavioural intention ( $\beta = 0.183$ ,  $t = 2.605$ ,  $p < 0.05$ ) and their ethical beliefs towards tax compliance intention.

Hypothesis 4a were tested to determine the relationship between secondary subjective norms or other agents (*NORM2*) with their behavioural intention to comply, while hypothesis 4b was tested to evaluate the influence of other agents on agents' ethical belief towards tax compliance intention. The results show that there was no significant statistical justification to support that other agents had influence on agents' behavioural intention to comply, but it strongly affected their ethical belief towards tax compliance intention. Therefore, hypothesis 4a was not supported, whereas hypothesis 4b was supported with significantly strong path correlation ( $\beta = 0.263$ ,  $t = 2.407$ ,  $p < 0.05$ ).

Hypotheses 5a and 5b were related to the original TPB constructs of PBC to test the relationship between PBC with behavioural intention, and PBC with behaviour. Both results supported the hypothesis that PBC will significantly influence agents' intention to comply and also their compliance behaviour. The results indicate a positive effect of PBC on behavioural intention ( $\beta = 0.243$ ,  $t = 4.073$ ,  $p < 0.01$ ) and a negative effect of PBC on behavioural intention ( $\beta = -0.223$ ,  $t = 2.893$ ,  $p < 0.01$ ). These findings reveal that there was a positive influence of the PBC aspect<sup>38</sup> on agents' intention to comply. However, the negative effect indicates that compliance behaviour might be higher when agents have a low level of behavioural control over avoiding and evading tax.

Hypotheses 6a and 6b examined the relationship between perceptions of law

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<sup>38</sup> Self-efficacy (hindrance or encouragement) and controllability factor (such as constraints, opportunity, resource) as discussed in chapter 6.



with behavioural intention to comply (compliance intention) and compliance behaviour. There was a significant influence of the perception of law on compliance behaviour ( $\beta = 0.226$ ,  $t = 2.162$ ,  $p < 0.05$ ), but a marginal influence on compliance intention ( $\beta = 0.104$ ,  $t = 1.587$ ,  $p < 0.10$ ). The results suggest that the higher penalty regime and imprisonment reflected in the legislation have stronger influence directly on agents' compliance behaviour compared to their compliance intention.

To determine the effect of law enforcement on agents' intention to comply and their compliance behaviour, hypotheses 7a and 7b were tested. The results suggest that stronger law enforcement effort would influence agents' compliance intention, but not their compliance behaviour. Therefore, hypothesis 7a was supported with a positive coefficient path ( $\beta = 0.108$ ), which was significant at 0.05 ( $t = 1.997$ ). On the other hand, there was no substantial statistical justification to suggest the significance of the effect of law enforcement and compliance behaviour. Therefore, hypothesis 7b was rejected.

Agents' level of knowledge was expected to have a significant influence on their tax compliance intention. It appeared that there was no indication of strong coefficient path and significance between the two factors. Therefore, hypothesis 8 was rejected. The results reveal that higher level of knowledge did not necessarily result in higher compliance level. It could possibly be greater knowledge exposed the agents to more opportunities to evade tax and therefore, less likely to be compliant. There is also possibility that their level of knowledge is at a sufficient level, therefore it does not make any difference on their compliance level.

Hypothesis 9a examined the relationship between agents' ethical belief and tax compliance intention, whereas hypothesis 9b was tested to understand the influence of ethical belief on tax compliance attitude. The results for both indicate significant relationships with positive path coefficients that were significant at 0.05. Therefore, hypotheses 9a and 9b were accepted. The results suggest that ethics reflected as an important aspect in compliance and attitude towards compliance.

Hypothesis 10 was tested based on the views (during the interviews in the qualitative phase of the study) that the procedure of import tax declaration was complex and therefore, making compliance difficult. Hypothesis 10 was formulated as *the perception of complexity of procedure will significantly influence the agents' intention to comply*. The results reveal a strong negative path coefficient ( $\beta = -0.273$ ), which was highly significant at 0.01 level ( $t = 4.443$ ). The negative result suggests

that there was a strong perception that the more complex the procedure is, the less likely are they able to comply with tax obligation i.e. it will make compliance more difficult.

The relationships between quality of service and tax compliance intention was tested based on the views (during the interviews with the agents) such as the competency, reliability of tax assessment officers in handling the assessment of import tax are profound to be part of the component of service quality constructs. It was quite an established construct in consumer and marketing literature, but under-explored in the area of tax compliance. Hypothesis 11 was formulated to evaluate if *the perception of quality of service will positively influence the agents' tax compliance intention*. The results demonstrate a positive path coefficient ( $\beta = 0.100$ ) at 0.05 significance level ( $t = 1.723$ ). Therefore, hypothesis 11 was supported.

Hypothesis 12 was also formulated based on the interview findings in the qualitative phase of this study. It states that, *the perception of exchange fairness will positively influence the agents' tax compliance intention*. It appears that the relationship was not statistically significant ( $t = 1.259$ ), with unsubstantial path correlation ( $\beta = 0.072$ ) between the perception of fairness and tax compliance intention. Therefore, hypothesis 12 was rejected as there was no effect between the perception of fairness and agents' intention to comply with the tax law.

In summary, the majority of the hypotheses listed in table 8.38, with the exception of hypotheses 4a, 7b, 8 and 12, were fully supported. In addition, all hypotheses in the original TPB model were supported as theories in the original TPB literature. The subsequent chapter (Chapter 9) will further discuss the implications of these results and the implications to Customs administration and policymaker.

**Table 8.38: Summary of Results of Hypotheses Testing**

<b>Hypothesis</b>	<b>Research Hypotheses</b>	<b>Result</b>
Hypothesis 1	Agents' behavioural intention to comply influences their tax compliance behaviour	Accepted
Hypothesis 2	Attitude of agents towards tax compliance significantly influences their tax compliance intention.	Accepted
Hypothesis 3a	Agents' primary referent group (importers) positively influence their tax compliance intention.	Accepted
Hypothesis 3b	Agents' primary referent group (importers) positively influence their ethical belief towards tax compliance intention	Accepted
Hypothesis 4a	Agents' secondary referent group (other agents) positively influence their tax compliance intention	Rejected
Hypothesis 4b	Agents' secondary referent group (other agents) positively influence their ethical belief towards tax compliance intention	Accepted
Hypothesis 5a	Agents' perceived behaviour control significantly influences their tax compliance intention	Accepted
Hypothesis 5b	Agents' perceived behaviour control significantly influences their tax compliance behaviour	Accepted
Hypothesis 6a	Perception of law positively influences agents' tax compliance intention	Accepted
Hypothesis 6b	Perception of law positively influences agents' tax compliance behaviour	Accepted
Hypothesis 7a	Perception of law enforcement positively influences agents' tax compliance intention	Accepted
Hypothesis 7b	Perception of law enforcement positively influences agents' tax compliance behaviour	Rejected
Hypothesis 8	Agents' level of knowledge significantly influences their tax compliance intention	Rejected
Hypothesis 9a	Ethical belief of agents towards tax compliance significantly influences their tax compliance intention	Accepted
Hypothesis 9b	Ethical belief of agents towards tax compliance significantly influences their attitude to tax compliance intention	Accepted
Hypothesis 10	Perception of complexity of procedure negatively influences agents' tax compliance intention	Accepted
Hypothesis 11	Perception of tax assessment service quality negatively influences agents' tax compliance intention	Accepted
Hypothesis 12	Perception of exchange of fairness positively influences agents' tax compliance intention	Rejected

## **CHAPTER 9**

### **DISCUSSIONS AND IMPLICATIONS OF THE STUDY**

This research was conducted to explore the diverse range of factors influencing import tax compliance behaviour based on the inter-disciplinary literature and the interview findings. This chapter presents a detailed discussion based on the results of testing the research model. It begins with a discussion of the findings based on the results presented in Chapter 8, followed by a discussion of the hypotheses of this study, which were developed to understand the determinants of agents' compliance with import tax. The chapter concludes with a discussion of the implications of the study

#### **9.1 SUMMARY OF RESEARCH FINDINGS**

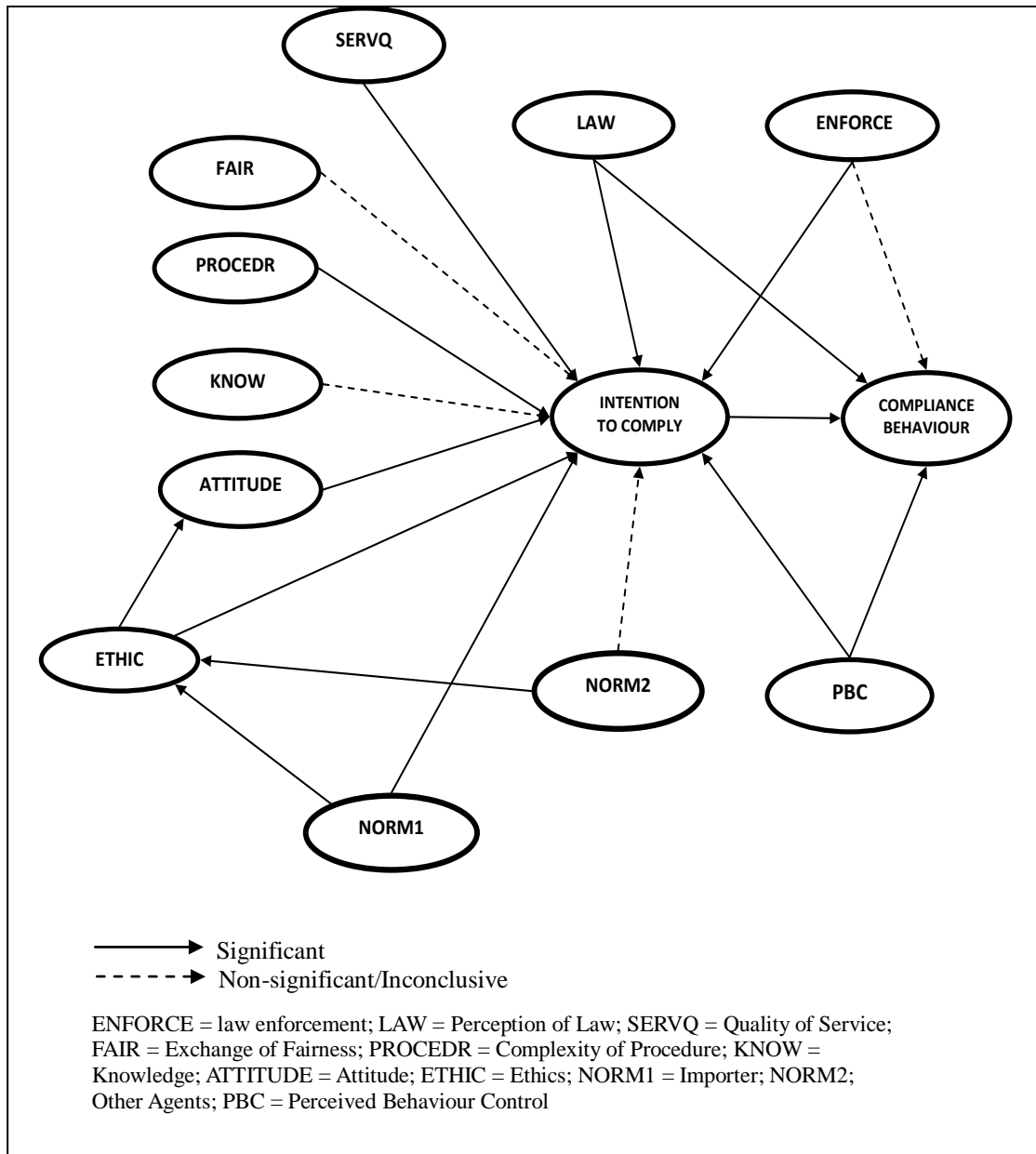
This section provides a summary and discussion of the findings. The detailed results from the analysis of survey data were presented in Chapter 8. The summarised results for the observed population sample are presented in Figure 9.1. Items in circles represent the constructs in the research model, whereas the arrow lines indicate the relationships between constructs. Significant paths are represented by the straight arrow lines, while the dotted arrow lines indicate non-significant paths or inconclusive relationships between constructs.

##### **9.1.1 The Role of Attitude in Import Tax Compliance**

Attitude is one of the principal components in the Theory of Planned Behaviour (TPB) that influence individuals' behavioural intention. Attitude towards import tax compliance refers to the assessment of an individual's intention to comply (or not to comply) with tax obligations based on their emotional beliefs, which relate to feelings of pleasure or guilt and behavioural beliefs (behavioural outcome). The role of attitude in tax compliance was hypothesised as H1 in Chapter 6. The findings of this study support a statistically significant effect of behavioural intention to comply. This outcome suggests that attitude, which refers to individual personal

beliefs and motivation to comply (or not to comply) with import tax payment, is based on the individual's personal sense of moral values, feelings of guilt and /or sense of civic duty.

**Figure 9.1: Customs Agents' Compliance Behaviour Model**



This outcome is consistent with the literature as discussed in Chapter 4, which supports the role of attitude based on tax morale as one of the primary psychological factors in TPB that influences tax compliance behaviour. Bobek and Hatfield (2003) in their study demonstrated that personal belief about offences is found to be a significant factor that influences tax compliance decisions. Similarly, taxpayers who

believe that tax evasion is a crime are more likely to comply with tax obligations (Torgler, 2007b). It was found that individuals with a sense of civic duty are more likely to be motivated to comply with tax obligations (Trivedi et al., 2005). A strong path correlation between attitude and behavioural intention to comply with import tax law also supports the assertion by Kornhauser (2007) and Murphy (2007) that personal belief such as attitude are internalised norms, which play an important role in determining taxpayers' compliance. Furthermore, tax compliance is a non-observable activity. Therefore, intrinsic factors such as attitudes, beliefs, personal integrity, reciprocity and principles of altruism are strongly associated with tax compliance (Alm and Torgler, 2006; Cummings et al., 2009; Kornhauser, 2007; Murphy, 2007).

### **9.1.2 The Influence of Subjective Norms on Import Tax Compliance**

The second TPB component that influences behavioural intention is subjective norms, commonly referred to as the referent group. In this study, the subjective norms were separated into two groups; the primary subjective and secondary subjective norms. From the results of the interview findings in Chapter 7, the primary subjective norm was identified as the importer group and the secondary subjective norm was identified as the other agents group. These two referent groups were expected to influence agents' behavioural intention to comply (or not to comply) with import tax payment and are hypothesised as H4a and H4b in Chapter 6.

The outcomes of this study revealed a significant relationship between the influence of the primary referent group, or importers, and the agents' compliance intention (whether to comply or not to comply). In contrast, the secondary referent group, or other agents, did not display a significant influence on agents' behavioural intention. This outcome supported the relevance of separation of the referent groups into two components, following the suggestion by Chu and Wu (2004) and Taylor and Todd (1995). This also indicates that the decomposition of subjective norms was necessary because the influence of the two groups: importer group and other agents group, on agents compliance decision may vary, as revealed in this study.

The empirical results also revealed that between these two referent groups, importers have a stronger influence on Customs agents' compliance decisions as compared to the influence of other agents. The direct influence of importers and the indirect influence through their ethical beliefs, are apparent in this 'principal and agent'

relationship. The role the Customs agents play in ‘representing’ the needs of their customers shapes the way Customs agents behave. In particular, the Customs agents may be unintentionally influenced by client attributes when making judgements and may have difficulty in separating their roles and responsibilities to Customs administration as required by the law. Clearly this has serious implications for compliance, as Customs agents could be swayed by importers, with regards to how the importers want to be represented. In this case, Customs agents should embrace these challenges and think creatively to help to solve business problems and assist businesses in promoting compliance. This relationship also questions the appropriateness of operating in an environment in which Customs agents act as intermediaries for the Customs administration.

Overall the influence of subjective norms on the compliance decision in this study supports the findings of previous studies, as well as the prediction of the TPB. This finding also supports the outcome of interviews with the agents (participants P2 and P7), that they could be obliged to follow their client’s requirements as they are being paid by them to provide the service.

### **9.1.3 The Effect of Perceived Behavioural Control on Import Tax Compliance**

Perceived behavioural control (PBC) is the third component that influences behavioural intention and behaviour as theorised in the TPB theory. PBC measures belief in relation to the controllability aspects and self efficacy of an individual with behavioural intention and directly measures behaviour (Ajzen, 2002). High PBC refers to a high level of behavioural intention. Thus, individuals with a high PBC may have a higher tendency to perform a behaviour compared to a lower PBC. If individuals believe that they have controllability of resources, opportunities to evade are high, and it can be done with ease (self-efficacy), it is likely that the individual may evade tax. Similarly if the PBC level is low, such as when there are low resources or a low opportunity to evade, it may be more likely that the individual’s intention and behaviour to engage with tax evasion is low. As hypothesised in Chapter 6 as H5a and H5b respectively, the result of this study significantly supported the effect of PBC on behavioural intention and compliance behaviour.

Positive PBC was reported by respondents in their intention to comply with import tax payment. Conversely, PBC emerged as a significant negative behaviour

with respect to tax compliance. Respondents who believed that they had less control over the behaviour had stronger intentions to perform the behaviour. However, their actual behaviour suggests that they are less likely to comply with import tax payment due to fewer obstacles and greater opportunities for tax non-compliance. One plausible explanation for the relationship is that the Customs agents ‘consciously’ under-report their controllability over their behaviour. The direction of this relationship contrasts with the prediction of the TPB and is not often found in TPB research. However, this is not entirely surprising as respondents had negative perception of Customs administration in relation to complex procedures which negatively influenced their behaviour to comply with import tax payment (see Section 9.1.8).

The effect of PBC is not widely tested, either independently or as a full model that measures PBC with intention and behaviour in tax compliance studies. This is possibly due to limited studies that utilise TPB as a theoretical model in tax compliance. Among the few studies that examined the effect of PBC on tax compliance behaviour, the outcome of this study validated the finding by Bobek and Hatfield (2003), which demonstrated a significant relationship between PBC and behavioural intention. In contrast, Trivedi et al. (2005) found no significant relationship in their study. This is possibly due to the different measurements applied, as in their study PBC had the elements of penalty and third party reporting. Other inter-disciplinary literature such as a technology adoption study that applied a self-efficacy and control element in measuring PBC also indicated the significant relationship between PBC and performing a behaviour (Scannell, Calantone and Melnyk, 2012). This result suggests that there was a need for more consistency in measuring PBC in tax compliance studies in order to further validate the findings and suggests the standard construct measurement for PBC.



#### **9.1.4 The Impact of Knowledge on Import Tax Compliance**

The literature suggests that an individual with adequate tax knowledge will be more compliant with tax law (Eriksen and Fallan, 1996; Palil, 2010). In this study, the relationship between knowledge of tax law and import tax compliance was examined to understand whether it can influence the agents' behaviour to comply with tax law. Knowledge was measured by capturing the three elements of knowledge: acquiring knowledge, knowledge retention and the application of knowledge.

It appeared that the relationship between knowledge and import tax compliance was inconclusive or statistically insignificant. The findings of this study appeared to contradict the general contention of some other studies, that demonstrated that having a better knowledge of the legal system of taxation would improve taxpayers' compliance (Eriksen and Fallan, 1996; Fallan, 1999; Palil, 2010; Saad, 2010). This result suggests that knowledge of import tax law is not one of the important determinants of import tax compliance, which is consistent with the study by Tan and Chin (2000) who did not find any significant impact of increased tax knowledge on tax compliance. In this context, enhancement of import tax knowledge did not necessarily enhance tax compliance among Customs agents. Such inconsistencies in the finding are also found in other studies which demonstrate a negative relationship between tax knowledge and tax compliance (Loo et al., 2009).

One plausible explanation for this outcome could be that although Customs agents were expected to have an adequate level of knowledge in order to satisfy Customs regulatory requirements, the Customs agents would weigh the costs and benefits before making any decision as to whether or not to comply, which is consistent with the contention of general economic deterrence theory. There were also some institutional elements such as the knowledge of tax assessment officers that influence tax compliance decisions of whether to approve or disapprove the import tax declaration based on his/her judgement. The present findings also suggest that the Customs agents may have a sufficient level of knowledge, which is above a critical threshold that would make some difference to their behaviour. After all, they are trained professionals, and this is dissimilar from other taxpayers such as those in a personal or business taxpayer context.

### **9.1.5 Ethical Belief and Import Tax Compliance**

Ethical belief is one of the prediction factors for attitude towards behavioural intention and intention to comply with the tax laws. In this study, ethical belief is measured by respondents' internal factors such as moral values, whether non-compliance behaviour such as tax evasion is morally right, wrong, ethical or unethical. The relationship between (1) ethical belief and attitude towards tax compliance intention and (2) ethical belief and tax compliance intention, was stated as hypotheses H9a and H9b respectively, in Chapter 6.

Both hypotheses supported the relationship, which indicates a statistically significant path coefficient. The results revealed that ethics is an important tax compliance determinant. Participants' ethical evaluation in this study predicts tax compliance behaviour directly and indirectly through their tax compliance attitude. Customs agents with high ethical belief are likely to have a more positive compliance attitude because of their sense of civic duty and the feeling that tax evasion is morally wrong.

Interestingly, the findings of this study also revealed that the role of ethics appears to be a significant determinant of tax compliance through the influence of the referent group on individuals' ethical beliefs. Two referent groups; importer and other agents strongly influence Customs agents' compliance decisions through their ethical beliefs. These relationships were stated in hypotheses H3b and H4b respectively, in Chapter 6. The findings suggest that Customs agents will be likely to comply (or not to comply) with import tax payment, judging by the ethical behaviour of people who are important to them. The tax compliance rate is higher when the people surrounding them have a stronger moral belief that tax evasion is not ethical. Therefore it appears that Customs agents will comply as long as they believe that compliance is the 'right thing to do'. Conversely, if non-compliance becomes pervasive, then the ethics of compliance may disappear. This may be relevant with the finding of qualitative interview as discussed in Chapter 7. In contrast with the finding of the survey result, some of the respondents interviewed, for example R2, R7 and R5, viewed that the right thing for them is to ensure business continuity through unethical practices, for instance assisting clients to find ways to reduce tax for their business survival.

The results suggest that there were consistencies with the findings of other studies in tax compliance such as those of Kaplan et al. (1997), Bobek and Hatfield,

(2003) and Bidin, Faridahwati, Mohd Salleh and Othman, (2011). Individuals who hold high ethical beliefs may have a positive compliance attitude because they will assume that compliance with tax law is a moral obligation (Ho and Wong, 2008). Moreover, they would feel reprehensible if they were found to avoid taxes and this will make them more compliant (Wenzel, 2005).

#### **9.1.6 Perception of Law and Enforcement on Import Tax Compliance**

To gain a better understanding of the factors affecting import tax compliance behaviour and behavioural intention, institutional factors were examined in two sets of prediction factors; (1) perception of law with behavioural intention and compliance behaviour; and (2) perception of law enforcement with behavioural intention and compliance behaviour. The relationships between law with behavioural intention and compliance behaviour were tested in hypotheses H6a and H6b, while the relationship between law enforcement with behavioural intention and compliance behaviour were tested in H7a and H7b respectively.

The results show that hypotheses H6a and H6b were supported with strong path coefficients. This indicates that there are strong relationships between the agents' perception of law with behavioural intention and compliance behaviour. However, for the perception of law enforcement, the results indicate a significant relationship between law enforcement and behavioural intention but there is an inconclusive result for the relationship between law enforcement and compliance behaviour.

The results revealed that the law is an important instrument that will influence tax compliance and concurs with the studies by Hanno and Violette (1996), Virmani, (1989) and Murphy, (2005) which demonstrate that high penalty rates increase taxpayers' compliance. The results of this study also indicate that the provisions in Customs law are perceived to be adequate, in terms of penalty rate and imprisonment term, as the main legislation framework for compliance. This suggests that severe punishment such as imprisonment can influence the taxpayer to be more compliant (Ho and Wong, 2006). Moreover law, through the provision of civil and criminal penalties, is still an important tool to prevent tax evasion (Kaplan et al., 1997; Trivedi et al., 2005).

In contrast, the finding suggests that an increase in enforcement efforts may increase the intention to comply, but it does not necessarily result in actual behaviour change towards compliance. Interestingly this study has some similarities to the

findings of the study by Verboon and Van Dijke (2007), that the probability of the taxpayer being detected and punished for tax evasion only shows a marginal impact on compliance behaviour. Taxpayers' judgement of the effect of sanctions by the tax office is not severe, therefore it does not affect taxpayers' compliance decisions. Similarly, in this study, the chances of getting caught by the Customs enforcement officers were perceived to be minimal. Interestingly, the result suggests that an increase or decrease in enforcement activities does not influence the agents' actual behaviour, as compared to their behavioural intention which shows a positive effect on compliance. This result of this study also supports the flexibility of TPB as the framework that could accommodate additional variables in explaining behavioural intention.

#### **9.1.7 The Impact of Tax Assessment Service Quality on Import Tax Compliance**

The service quality of the Customs office in relation to import tax assessment was viewed as an important compliance determinant. The quality of service was a newly introduced variable which is relatively under-explored in direct tax compliance, as well as in an indirect tax context. The concept of quality of service, which is widely applied in marketing literature, is commonly associated only with the private sector. The concept was extended and tested in this study as an extension to the concept of public service quality. It was measured using the ten service quality dimensions from the marketing literature, described by Buttle, (1996) and adapted to the context of this study to measure the quality of service in the assessment of import tax provided by the Customs administration. Positive views on the quality of service will make compliance easy, whereas negative views can be translated as poor service and make compliance more difficult.

The results of the study establish that there is a significant positive relationship between the quality of Customs tax assessment service and tax compliance intention. This result also suggests that generally, the majority of Customs agents have positive perceptions of the quality of tax service provided by Customs administration, although, during the interview with the selected sample of agents, there was a negative view about the overall quality of the Customs import tax assessment service. This study indicates that the concept of service quality in the private sector can be extended to the public sector to understand customers' satisfaction. It is now realised

by many public sector organisations that quality of service and overall service delivery are critical strategic issues that warrant attention. With the current emphasis on change management or government reforms, the service quality of the public sector is even more critical. Especially in tax related studies, the level of taxpayers' satisfaction with the way they are treated by the tax office may influence overall compliance (Kirchler, 2007; Torgler, 2007a; Wallschutzky, 1984).

The findings also indicate that service quality attributes, such as competencies related to knowledge and skills as well as responsiveness of Customs officers in relation to the assessment of goods declaration, are important in determining compliance. Customs officers who are competent and knowledgeable are able to provide sound decisions and better quality of service with regards to the Customs declaration provided by Customs agents, hence making compliance easier.

Therefore, this study validates the results of a previous study on service quality, which is considered to play a significant role in influencing behavioural intention (Chen and Kao, 2010; Yap and Sweeney, 2007; Zeithaml, Bitner and Gremler, 2006).

#### **9.1.8 Perception of Exchange of Fairness**

The concept of exchange of fairness was identified as another important finding during the interview session with the selected sample of Customs agents and Customs agents associations. It is related to the taxpayers' view of government spending in return for the import tax payment. Few pieces of literature that examined the effect of exchange of fairness suggested that exchange of fairness is an important tax compliance determinant (Azmi and Perumal, 2008; Richardson, 2005; 2006). Exchange of fairness was measured based on the three components: (1) fair benefits, (2) equity benefits and (3) benefits received.

However, the results of the study demonstrate that exchange of fairness is not an important factor in influencing import tax compliance intention. The results contradict previous findings, which indicate a strong influence of exchange of fairness on tax compliance determinants (Azmi and Perumal, 2008; Richardson, 2005; 2006). The results also indicate that the interviewees, who perceived fairness in government spending on tax paid as an influencing factor on whether or not to declare less tax, might not represent the overall view of Customs agents. Although there are growing

number of literature that examine the effect of tax fairness on tax compliance, only a handful of studies examining the effect of fairness exchange within the scope of tax fairness. Therefore, the lack of such studies prevents comparison of the current results with the results of prior studies.

One possible explanation for this outcome could be that importers pay import tax indirectly through Customs agents. The actual taxpayers in this case are the importers, which makes the effect of perception of fairness less likely to affect compliance behaviour of Customs agents. Perhaps this outcome suggests that although this is not a direct influence on Customs agents, the importers' perception of fairness may indirectly influence compliance behaviour via the Customs agents' as it influences norms associated with the importer reference group. Such a hypothesis might possibly be examined in future studies.

### **9.1.9 The Impact of Complexity of Procedure on Import Tax Compliance**

The concept of complexity of procedure is relatively under-explored concept in tax compliance. Although there was no indication of studies that examine the effect of complexity of procedure on import tax compliance, there were studies which examined the effect of complexity elements such as tax complexity (McKerchar, 2001; 2007), law complexity (Kirchler et al., 2006; Krause, 2000) and trade complexity (Altomonte and Bekes, 2009). The term 'complexity of procedure' was conceptualised in relation to the process of import declarations such as clarity, flexibility, uniformity of procedure, and rigidity of procedure that would make compliance easy (or difficult).

The results of this study established that complexity of procedure had a significant negative relationship with tax compliance intention, which implies that the majority of the agents have a negative perception of Customs procedures. These results were consistent with the findings in the second phase of the qualitative interview with the selected sample of Customs agents and Customs agents associations, where it was found that there was a negative perception about the import declaration procedure. Customs import declaration procedure was viewed as complex, and therefore compliance was difficult. The results can also be comparatively associated with relatively similar findings within the context of 'complexity'. The findings of the study support the relationship between complexity and tax compliance

(Krause, 2000; McKerchar, 2001; 2007).

This negative finding has some impact on current practices of import declaration procedures. If the system is too complicated (for instance if there are too many changes in procedure), Customs agents will face difficulty in complying with Customs import tax requirements, as complexity is likely to result in confusion when lodging import declarations. Similarly, other tax compliance studies have suggested that frequent changes in the tax system affect the taxpayers' compliance in relation to their accuracy in completing their tax returns (McKerchar, 2007). Therefore, it is important for Customs administration to review their current procedures by adopting the best practises of Customs and tax authorities in other countries to ensure that the agents and importers meet their tax compliance.

#### **9.1.10 The Influence of Behavioural Intention and Compliance Behaviour**

Behaviour is strongly influenced by intentions (or behavioural intentions) as theorised in the TPB theory, apart from the influence of law, law enforcement and PBC on compliance behaviour as discussed in sections 9.1.3 and 9.1.6. Among the handful of tax compliance studies that have utilised TPB as the compliance behaviour framework (Bobek and Hatfield, 2003; Saad, 2010; Trivedi et al., 2005), a few have attempted to include the relationship between behavioural intention and behaviour as a full TPB framework (for example Jones, 2009; Saad, 2010). In this study behavioural intention is described as the willingness to declare accurately in accordance with tax law at the time the declaration is lodged, similarly, in a direct tax environment, as suggested by Roth et al. (1989), taxpayer compliance is described as the willingness to file the return form at the proper time and accurately report tax liability.

The results confirm the findings of existing studies with a positive relationship between behavioural intention and behaviour. In other words, the agents' willingness to comply with import tax law at the time the import declaration is lodged is reflected in their actual behaviour. However, in this study the prediction power ( $R^2$  value of 0.083) indicates a marginal effect on behaviour, although in terms of path significance, it shows a positive relationship. The results indicate that the variance only explained 8.3 percent of the observed population of this study. Therefore, there are other factors that may influence compliance behaviour apart from behaviour

intention, perception of law, law enforcement and PBC. There are also possibilities that moderating factors may influence these relationships (Wong and Sheth, 1985). Another plausible explanation is the type of questions which directly ask about the respondents' actual compliance (past experience), might affect the interaction between intention and actual behaviour, because it demonstrates the actual compliance behaviour. Such inconsistencies were also acknowledged by Fishbein and Ajzen (2010) that there is an intention and actual behaviour gap that exists in some research. Similarly, in health-related studies has found that respondents do not intend to use condoms, perform cancer screening or to exercise, between 26% and 57% fail to carry out their intentions (Sheeran, 2002).

According to Fishbein and Ajzen (2010), individuals may not appear to perform actual behaviour based on their intention due to several reasons. Firstly, the behavioural inconsistencies can occur due to 'pseudo-inconsistency'. On a survey questionnaire, individual may express an intention to engage in a given behaviour, but in reality their actual behaviour may change. A second explanation attributes the discrepancy between intention and behaviour was due to substantive differences between hypothetical situations and real contexts. However, this study does not apply the hypothetical situations type of questions to measure compliance behaviour. Therefore, the hypothetical reason may not be the possible reason in this context of study.

## **9.2 CONTRIBUTION OF THIS STUDY**

The findings of this study have some interesting theoretical implications, especially for taxation and socio-psychological literature. In addition there are significant policy implications for indirect tax authorities. The contributions made by this study are discussed in this section.

### **9.2.1 Contribution to the Literature/Theoretical Implication**

This study contributes to the existing literature in several ways. This study is among a handful of studies that attempts to understand tax compliance determinants in indirect taxation. To the best of the author's knowledge, this study is the first study that focuses on import tax determinants, which specifically looks into the compliance



behaviour of Customs agents as the intermediaries for the Customs administration (indirect tax authority). Most of the focus of prior studies on indirect tax was on value-added tax (VAT) or good and services tax (GST). The few studies that have been conducted in the area of import taxes were related to the economic model, and looked into the traditional economic deterrence effect of tax rates and tax evasion. Unlike the concept of tax evasion, which is narrowly viewed, in this study, tax compliance is defined as a higher order or a broader concept. Therefore, the behavioural approach was applied, where tax compliance is viewed as voluntary compliance as opposed to enforced compliance.

This study, applied behavioural theory using TPB as the theoretical framework and this proved to be a strong base theory that was able to predict compliance behaviour and a universal theory that can be applied to other inter-disciplinary research contexts. Furthermore, among the handful of studies that applied TPB in tax compliance studies, only a few have included all TPB constructs as a full compliance model to understand the determinants of tax compliance behaviour. It was found that there were very few attempts in previous studies to extend the full model, or examine the relationship between behavioural intention and behaviour (Bobek and Hatfield, 2003; Saad, 2010; 2011). Trivedi et al. (2005) was the only other study that examined tax compliance behaviour within a full TPB Model. Trivedi et al.'s (2005) study was undertaken in Canada (a different tax jurisdiction) and the sample comprised of one group of students. Further, the TPB Model was extended with the inclusion of only one additional construct (ethics). In contrast, the TPB Model was extended with the inclusion of multiple constructs: psychological, sociological, economic and institutional constructs. Furthermore, the findings of this study, could potentially contribute to a more integrated tax compliance behaviour model.

Moreover, the newly-identified constructs that were included in the compliance behaviour model were as a result of the exploratory sequential mixed method technique applied in this study. This mixed method technique began with a qualitative approach (through interview) and ended with a quantitative approach (through survey). Although there are studies in tax compliance that began to adopt the mixed method technique, such as Loo et al. (2009) and Saad (2010), these studies tend to use a deductive method at the beginning and apply an interview approach to elaborate on and justify the findings. This approach has a limitation in discovering any new trajectories, unlike the exploratory sequential mixed method approach

applied in this study. This technique, which began with the first sequence using a qualitative approach (interviews), proved to be effective in exploring additional influencing factors for tax compliance. In this study, three constructs emerged out of the interview findings: quality of service, exchange of fairness and complexity of procedure. The quantitative approach (in the second phase of study), through survey, complements the qualitative findings. This approach is not only consistent with gradual development of taxation studies incorporating both quantitative and qualitative orientations (e.g. Loo, 2006; McKerchar, 2003), but also as an alternative to the traditional method of tax compliance research, which relied heavily on a single quantitative deductive approach, as well as the traditional mixed method approach.

This study has also developed a set of measurements for the new constructs including 'complexity of procedure' and the introduction on the concept of 'quality of service' in tax compliance study (a construct which is commonly and extensively applied in marketing literature). These two constructs emerged from the interview findings in the second phase of the qualitative study. The construct of 'complexity of procedure' was also added from existing literature that looks into various elements of complexity in tax compliance studies, such as law complexity (Krause, 2000) and tax complexity (McKerchar, 2001; 2007). The construct of 'quality of service', which is thought to be a concept that is only applicable to the private sector, is a relatively new construct introduced to public sector research, especially in relation to tax compliance studies. As such, the findings of this study contribute new evidence to the existing tax compliance literature by revealing the existence of the relationships between quality of service, complexity of procedure and import tax compliance. These new constructs perhaps would be useful for future researchers intending to undertake similar studies of indirect tax in other countries. This will further confirm the reliability and validity of the constructs and test the applicability of the constructs in tax compliance and other related studies.

In order to test the constructs, the PLS-SEM method was applied to analyse the predictive power of the structural model (compliance behaviour model). PLS-SEM is a powerful tool that is able to accommodate a mixture of formative and reflective constructs in a single model, which proves to be superior to the other SEM methods such as covariance-based SEM. This approach is a relatively new in tax compliance studies, and differs from most of the studies on tax compliance undertaken so far that commonly rely on SPSS analysis and covariance-based SEM

such as AMOS. The weakness of the previous approach is that it tends to accept or inherit a reflective model as the right/correct approach to modelling tax compliance without assessing the appropriate construct measurements, whether reflective or formative. In this study, the constructs were carefully assessed to ensure appropriate categorisation of construct modelling to avoid errors in the model, which resulted in a mixture of formative and reflective construct indicators in the model. This study is able to demonstrate the application of formative and reflective construct indicators in SEM modelling, which is more established and widely discussed in other interdisciplinary literature such as marketing and consumer behaviour.

This study also contributes to the literature by examining tax compliance determinants, that have been applied in direct tax and other literature, to the context of this study. The finding of this study suggests that tax compliance determinants between (1) direct and indirect tax contexts; and (2) personal and business taxpayers, share the same principles or have some similarities. Factors such as ethical beliefs, sanctions and deterrence through law and enforcement were relevant in an indirect tax environment, specifically in an import tax context. Collectively, psychological, sociological, economic and institutional factors or behavioural and non-behavioural elements were found to be important determinants of import tax compliance (indirect tax context). This study also revealed that import tax compliance extends beyond sanctions and deterrence factors to achieve an optimum compliance level, which supports the role of behavioural elements as demonstrated in the Theory of Planned Behaviour. Interestingly, this study also revealed that compliance decisions of business taxpayers (importers) were inferred through intermediaries (Customs agents). This was evidenced through the role of primary subjective norms (importers) which have a strong influence on agents' compliance decisions. As such, the findings of this study are valuable contributions to tax compliance and behavioural literature.

Unlike in direct tax studies, most of the previous studies on tax compliance tend to focus either on tax agents or taxpayers. To the best of the researcher's knowledge, this study is the first study that examines Customs agents who play the dual functions of both tax preparers and taxpayers. Unlike the role of tax preparers in direct tax, ~~who only prepare the tax computation and lodge the declaration,~~ Customs agents are mandated under the Malaysian Customs Act 1967 to prepare Customs import declarations as well as making payments of import tax for their clients through their agents' business accounts. Furthermore, they are also authorised by the Customs

administration to transmit tax payment via telegraphic transfer (TT) or electronic fund payment transfer (EFT). Therefore, some see Customs agents as a profession that helps to make trade easier, whereas others view the profession with scepticism and are mindful that Customs agents are responsible for manipulating import tax declarations to evade tax. Thus, this study provides some unique insights, which may not be found in a direct tax context such as in personal or corporate tax studies. Moreover, this study may enhance the understanding of the dual role of Customs agents as both taxpayers and tax preparers, viewed as one entity. As such, the findings of this study are novel and valuably contribute to the tax literature, specifically to tax agents and taxpayers' literature.

### **9.2.2 Practical Contribution and Policy Implications**

Tax compliance has always been one of the areas of concern for tax authorities around the globe. Similarly, indirect tax authorities such as Customs have been continuing to seek ways to improve, through increasing compliance levels among indirect taxpayers, which largely consists of businesses taxpayers. It is crucial that any policy design aimed at improving the level of compliance among business taxpayers does not jeopardise the flow of trade, especially the World Customs Organization (WCO) trade facilitation, which is highly placed on the Customs administration policy agenda in many countries. Therefore, designing such policies requires an understanding of taxpayers' determinants that would influence their compliance decision. This study, which incorporates a traditional compliance model based on economic theory, such as penalties and sanctions, with a socio-psychological model, which is largely based on attitudes, beliefs and social norms, makes an investigation, in order to understand compliance determinants of Customs agents as business taxpayers for import tax declaration. This study has shown that there were some similarities between direct tax and indirect tax compliance determinants, where there are lessons that can be drawn from these findings. The results of this study have identified several determinants of import tax compliance behaviour which may have implications for indirect tax authorities, such as the Malaysian Customs, and policy makers.

**(a) Implications for Customs Policy**

Reflecting upon the initial conversation with the senior Customs officials, the majority of them assume that compliance is directly correlated to sanctions, penalties and coercion. This is not surprising as the traditional approach to tax compliance, with its emphasis on penalties and sanctions, is frequently applied by tax authorities including Customs administration to increase tax revenue. Deterrence and sanctions may be one of the effective approaches to deter tax evasion and increase compliance level, but it is not cost efficient, especially for large organisations such as the Malaysian Customs. Moreover, this approach does not conclusively explain behaviour. This study demonstrates the importance of taking a different approach which includes behavioural aspects (attitude towards compliance, subjective norms such as the role of importers, ethical beliefs and perceived behaviour control) as evidenced by the results of this study. Therefore, Customs administration should focus more on developing compliance frameworks which include these behavioural aspects together with formal sanctions.

Customs administration may include moral values and promote positive aspects of tax compliance in their training modules. For instance, in the case of Malaysian Customs, the agents are required to successfully complete training prior to the issuance of a Customs agent's license. This would be a good platform for an on-going effort to instil ethical values and promote a more comprehensive programme among Customs agents, other than a seasonal campaign and awareness programme. The training aspects could be extended to Customs officers to promote change to understand a wider view of compliance. This will make them aware that factors such as pressure from certain referent group (such as customer/client) and other behavioural elements are the way to improve compliance. In this way, Customs officers could understand the agents and how to work with them better to achieve optimum compliance.

It is important to communicate the positive aspects of tax compliance to the importer group identified as the primary influence on the agents' compliance decision in the awareness programme. If taxpayer whether direct such as importers or indirect such as Customs agents, at large, believe that complying fully with import tax laws is the norm in the society, the majority will be more than likely to comply too. A positive perception of tax compliance will promote voluntary compliance (Kornhauser, 2007).

The Customs administration, together with the government, may, from time to time, also promote awareness to the public about the seriousness of committing crime such as evading tax and the harm it causes to society as a whole. Although there are cases of tax evasion that have been brought to the court of law, as shown in Exhibit 2.13 of Chapter 2, these cases have often ended up being published only in law journals for legal reference. Publishing examples in the newspapers and on social media of recent cases of tax evaders and the punishment for the crime committed may educate and have more impact on the public. In this way, more people may feel that the effort involved in defrauding an amount of tax is not worth engaging in, due to the seriousness of punishment for the crime.

As demonstrated in this study, institutional factors such as Customs procedures and service quality of Customs assessment were found to be relatively important in influencing compliance decisions. Although in general, the survey results show that there was a positive perception of the service quality of the Customs assessment offices, there were some negative views about the competencies of the assessment officers. Customs authorities should therefore focus on ensuring that the assessment officers are well-trained and competent to handle import tax assessment. Placing incompetent or new officers may impact on the overall quality of the assessment service and make compliance more difficult due to the uncertainty of the assessment. It would seem worthwhile to try to reduce negative views by emphasising the supportive role of the Customs administration. Every effort should also be made to ensure that the assessment officers are at all times courteous, knowledgeable and maintain an open mind regarding the integrity of the Customs agents and business owners. This will improve overall quality of service of the Customs administration and enhance the compliance level of businesses.

It was also acknowledged that views on Customs administration are very diverse. There were negative views on the complexity of the Customs import declaration procedure. Complex procedures will make compliance more difficult, increase the cost to businesses and disrupt the flow of trade. This provides an indication to Customs administration, especially Malaysian Customs, to increase their efforts in providing a more simplified and standardised procedure between various import assessment offices and in provide quality services to ensure that the compliance requirement is met, whilst ensuring tax is appropriately collected. Generally, Customs administration should review their current practices which require

streamlining and simplification of procedures, to make compliance as easy as possible. This is in line with the international standards and recommended practices of the WCO and WTO. Specifically, the WCO Revised Kyoto Convention provides guidelines for Customs administration on good practices, aimed at facilitating trade by harmonising and simplifying Customs procedures and practices (WCO, 2006). Similarly, at the international and regional level, WTO and ASEAN provide a framework for simplifying Customs procedure, as outlined in Para 27, Article VIII of the GATT 1994 and Article 1, ASEAN Agreement on Customs (ASEAN, 2014a).

**(b) Professional Standards of the Customs Agents**

Another important area of focus as a result of this study is the professional standards of Customs agents in an effort to promote voluntary compliance. To increase the standard of Customs agents, this study suggests a change in the way information on Customs agents is managed. It is suggested that risk assessment profiling is extended and includes the elements of attitude towards risk of agents and importers. The behavioural variables such as attitude and ethics of taxpayers are characteristics that could be looked for in previous compliance performance and account could be taken of these variables. Speeding tickets of the agents, their credit report from the central bank and other criminal records are some examples of empirical evidence that could be used in the risk profiling system by the Customs administration. This is to make sure that the agents that are selected as licensed agents are highly compliant.

This finding also suggests that Customs agents are important intermediaries for Customs administration, as the compliance decisions of importers are inferred through them. Therefore Customs administration could continue to embrace the level of professionalism, and profession of agents, by providing continuous training and support to agents who can be considered as partners. Customs agents should also continue to provide good services and expand their knowledge beyond Customs related activity. They have to think of other related activities such as providing advice on other aspects such as facilitation, the supply chain or financing in order to remain competitive in the business.

**(c) Implications for Education Policy**

Behavioural attributes are unobserved behaviours which are essential in influencing compliance decisions, as demonstrated in this study. Any act of self-sanction or self-compliance with reference to these attributes is commonly associated with voluntary compliance. Therefore, it is important for policymakers and indirect tax authorities to come up with strategies to encourage voluntary compliance. A policy such as tax education at university level or pre-university level about the importance of taxation for the country's economic development and well-being of the society would be a good start. The Ministry of Education (MOE), Ministry of Higher Education (MOHE) and other relevant government organisations should play an active role in promoting tax education. Incorporating tax education into the secondary school curriculum may also help for early exposure to tax.

**(d) Implications to the International Communities**

WCO is one of the important intergovernmental organisations which directly reflect on Customs policy and procedure. WCO could play an active role in promoting compliance and provide a facilitating function through revising its international guidelines and conventions to incorporate a wider framework, including behavioural elements. Risk management is one of the elements that have been outlined in the WCO Revised Kyoto Convention. This study has expanded the notion quite considerably in terms of describing behaviour and norms in relation to compliance. This may be relevant to WCO policy instruments that could accommodate changes to the current WCO model of recommendations on Customs risk assessment. Specifically, a risk assessment model that describes the behavioural aspects is recommended. Characteristics of agents and importers based on the credit background and past records to analyse their risk behaviour are some examples that WCO could recommend on the risk assessment best practice model. This is a more pragmatic approach to risk management for better efficiency of managing import and export procedures at borders.

Capacity building in this area is also recommended, to expose the international community such as WTO and UNCTAD (United Nation Conference on Trade and Development) to the importance of behavioural aspects of compliance alongside



operational procedures. The understanding of non-economic elements as demonstrated in this study could inform better trade policies and procedures, in order to promote compliance with international trade and policy recommendations.

### **9.2.3 The Way Forward**

This study, which focuses on Malaysia, demonstrates that tax compliance is a complex issue which consists of diverse factors including psychological, sociological as well institutional factors such as Customs procedures and the overall quality of service. This provides an indication for the current Malaysian Customs policy that there are other factors than deterrence and sanctions that may increase the level of compliance. The similarities with Customs procedure in other countries which have adopted the international conventions and guidelines of the WCO, WTO and ASEAN, show the relevance of this study as a reference case for other Customs administrations. Hence, this study is relevant for policy makers, especially Customs administration, in other countries, examining the effects of compliance using a similar approach to enhance compliance rather than purely deterrence and sanctions.

Therefore, it is suggested to incorporate various compliance determinants in an integrated indirect tax compliance model. A model that includes factors incorporating economic, socio-psychological and institutional factors in a comprehensive compliance model is suggested. This is as an addition to the traditional enforcement and penalty strategy as a desirable policy instrument for policy makers, and specifically for indirect tax authorities such as the Malaysian Customs. The correlation between these factors in a comprehensive compliance model may lead to the development of a self-regulatory model based on an economic-behavioural model.

This study will also be relevant to other countries where Customs agents as the ‘middle-men’ are used to support importers. However, there are countries such as in the EU and Singapore where company representatives and other indirect representatives could take charge of the declaration of Customs. In these instances, there are some aspects of the model of this study that might also be relevant to compliance in their policy contexts. Therefore, these findings could inform policy makers and other Customs administration on formulating policy and procedure that would lead to an optimum compliance level among various groups of taxpayers, either directly or indirectly through Customs agents.

These findings also have important implications for the profession of Customs agent. In the current economic climate where businesses are highly competitive, the role of agents is fragile and easily influenced by their clients, due to fear of losing business. There is the possibility that agents may provide adverse advice on paying the least amount of tax, and the taxpayer may ultimately make the compliance-related decisions. This study supports the influence of clients on agents' compliance decisions. Therefore, understanding how decisions are made and the role of Customs agents as 'middle-men' in the decision making process is of critical importance to the Customs administration and policy maker. Therefore the findings of this study are also relevant to international and intergovernmental organisations such as the WTO and WCO to re-examine the current guidelines to reinforce the profession of agents.

# CHAPTER 10

## CONCLUSIONS

This is the concluding chapter of this thesis, which summarises the importance of this study, the major findings that have been discovered and the contribution of the study. The chapter highlights some of the strengths of the study, and discusses some limitations identified during the course of the study. The future research ambitions, which attempt to address issues not covered by this study, are also discussed in the concluding remarks at the end of this chapter.

### 10.1 RESEARCH SUMMARY

Tax compliance is a complex behavioural issue. There has been a considerable amount of interest in this area of research for more than 40 years. Various tax compliance studies have been conducted to understand the factors that influence taxpayers' compliance. Researchers and academics have applied various models of tax compliance, from economic models and economic-psychological models to behavioural models, to tax compliance research to develop an improved understanding of tax compliance. Surprisingly, most of the focus of this research has been on individual taxpayers in the context of direct taxation. This study attempted to fill this gap by extending tax compliance research to import tax (indirect taxation), investigating the role of Customs agents who act as intermediaries for taxpayers (importers). Specifically, the objective of this study was to understand the determinants of Customs agents' compliance with import tax law.

This study reflected on practitioners' experiences and observations in Customs import tax administration. The focus was on the relationship between Customs agents (preparers) who are involved in the preparation of import tax declarations, and import tax (indirect tax) compliance. As import tax compliance in this context needs to be defined from a broader perspective, the definition used by the author is that tax compliance is: *the willingness to comply with Customs law, honestly report all information in a Customs import declaration, and pay import tax at a particular time and place which are determined by ethics, knowledge, and legal, environmental and other situational factors.*

To achieve the purpose of this study, the Theory of Planned Behaviour (TPB) was applied as the framework for developing a compliance behaviour model (CBM) to understand the determinants for compliance behaviour. TPB is a robust social cognitive theory that has been applied in various studies. Variables that have been established in direct tax compliance literature as well as additional variables identified through interviews with Customs agents and Customs agents associations were added to the TPB for large scale survey distribution purposes. The CBM model in this study represents the extended TPB model, which accounts for economic, psychological, and institutional factors to provide a more holistic view in understanding agents' compliance behaviour.

This research was conducted using an exploratory sequential mix methods design, a method which has not been widely applied in tax compliance studies. It began with the first sequence, with a qualitative approach, which involved interviews with selected samples of eight Customs agents and three Customs agents associations (logistics and freight forwarders associations) It ended with the second sequence, with a quantitative approach which involved the participation of 279 Customs agents in Malaysia who handle import declarations, in a large scale survey questionnaire distribution conducted between February 2013 and April 2013.

The findings of the first phase of this study (qualitative phase) identified three additional determinants to be added to the TPB model. These were: (i) complexity of procedure, (ii) quality of tax assessment service and (iii) exchange of fairness with tax contribution. With these incorporated into the existing compliance model, the revised CBM model consisted of 13 constructs: attitude, primary subjective norm (importer), secondary subjective norm (other agents), perceived behavioural control, behavioural intention, behaviour, ethics, knowledge, law, law enforcement, complexity of procedure, tax assessment service quality and exchange of fairness. The final CBM was tested by analysing the questionnaire survey responses from a purposely selected sample of Customs agents from across Malaysia using the Structural Equation Modeling (SEM), SmartPLS software application.

The findings from the survey data indicated that psychological, institutional and economic factors, consisting of attitude, ethics, beliefs, sanctions and enforcement, complexity of procedure and quality of tax assessment service, are equally important in explaining Customs agents' behavioural intention to comply with import tax law. However, they also suggested inconsistencies in the relationship

between behavioural intention and behaviour, and the need to incorporate other factors and moderating variables. In particular, the findings recognised the influence of two referent groups (social norms): (i) importers who influenced the Customs agents' compliance intention directly and indirectly through their ethical beliefs; and (ii) other Customs agents who influenced Customs agents' ethical beliefs. Therefore, both groups performed a significant role in influencing the Customs agents' decision, as to whether to assist their clients in devising strategies to exploit legal ambiguities or facilitate compliance.

Overall, this study illustrates the importance of incorporating behavioural elements and facilitating elements (such as a better quality of tax assessment service and less complex procedure) together with economic variables to achieve an optimum compliance level. This is an important finding as it highlights the need for an indirect tax authority, such as a Customs administration, to develop a more comprehensive approach to ensure tax compliance, beyond simply applying sanctions and enforcement as compliance strategy. Moreover, it is important to adopt an appropriate approach since major reforms will take place soon with the corporatisation of Malaysian Customs and the newly introduced goods and services tax (GST) system. Therefore, there will be a higher expectation on the new administration for a more efficient and effective tax collection system.

Another essential but largely neglected strategy for improving compliance concerns the importance of ethics in compliance, which was found in this study to be indirectly influenced by importers and other agents. Although taxpayers' personal and subjective norms are generally more difficult for tax authorities to control compared to sanctions and other institutional elements, their focus should be on taxpayers' ethical beliefs, in an effort to encourage voluntary compliance. Therefore, there is scope for improvement by indirect tax authorities reinforcing the importance of tax compliance as an ethical form of behaviour, such as in public forums involving importers and agents, or as part of the module for licensing requirements to be agents, and publicising cheaters so that tax evasion is seen as an unethical pattern of behaviour. Highly compliant agents and companies could also be enlisted, to show that these companies are rewarded with fast track clearance and other facilitations.

Finally, this study demonstrates the wide applicability of TPB, including its application in tax compliance research, specifically in the context of import tax. The method (exploratory sequential mixed method) used in this study could also be used

to replicate other studies, in order to provide a more holistic compliance behaviour model. The CBM developed in this study may also be extended to other indirect tax compliance studies such as value added tax (VAT) or goods and services tax (GST). Since there are similarities between the role of Customs agents and GST registrants as the tax collectors for the indirect tax authority and intermediaries between buyer and government, compliance determinants may be applicable in the context of the VAT or GST regimes.

This study, which focuses on Malaysia has demonstrated that tax compliance is a complex issue, which consists of diverse factors including psychological, sociological as well as institutional factors such as Customs procedure and the overall quality of service. This provides an indication for current Malaysian Customs policy, that there are other factors than deterrence and sanctions that may increase the compliance level. The similarities of Customs procedures in other countries adopting international conventions and guidelines by the WCO, WTO and ASEAN, provides the relevance of this study as the reference case to other Customs administrations. Therefore, this study is relevant for policy makers, especially for Customs administration in other countries, in examining the affect of compliance using a similar approach to enhance compliance rather than purely deterrence and sanctions.

## **10.2 FUTURE RESEARCH AMBITION**

As with all other research, this research has its own strengths and limitations. One of the main strengths of this research is its uniqueness, as it is a new area of tax compliance that is grounded on practitioner experience and observation. Unlike other tax compliance studies, this study began with an exploratory study to define the research focus and find the literature that supports the field of study. The study would not have been possible without some practitioner background through which to understand the context of the study. Moreover, for tax compliance studies, it has been a constant challenge for researchers to obtain “hard” empirical data (Kirchler, 2007, p183), leading most to resort to creating their own data. This study has the advantage of having access to actual data on Customs agents (intermediaries to actual taxpayers) and employees of The Royal Malaysian Customs Department. Hence, the findings presented are rare and unique, and are important contributions to the empirical evidence for tax compliance literature as well as to the understanding of indirect tax

compliance behaviour, specifically the role of Customs agents as intermediaries to the taxpayers.

The second strength of this study is the research design. The study applied the exploratory sequential mixed method (ESMM) research design which has not yet been tested in other tax compliance studies. Unlike other tax compliance studies that use purely questionnaire survey or qualitative methods to justify the findings of the survey (in mixed method), ESMM involves qualitative study in the first sequence and quantitative study in the following sequence. The qualitative study in the first sequence was useful to discover additional variables and to ascertain the model developed in the study. Three additional variables emerged as a result of the qualitative stage, which were added to the existing model. The model was tested and validated using a large scale survey in the following quantitative phase of ESMM. The research design adopted in this study should serve as a reference for future tax compliance studies, especially to explore a new understanding in tax compliance studies.

While most tax compliance studies assume that the same constructs applied in various models are reflective, this study went a step further by investigating each construct carefully and categorising them according to the respective reflective or formative measurement model. This was to avoid model measurement error and bias in the results which may provide an incorrect interpretation of the relationships and recommendations in studies. The measurement model was tested using the structural equation modelling (SEM) SmartPLS software application, a co-variance based SEM which is capable of analysing and interpreting both reflective and formative measurement models. The use of this construct assessment is more developed in other areas of study such as marketing and consumer behaviour than tax compliance, which is lagging behind in term of the aggressiveness of assessment of construct categorisation. Thus, this study provides fresh findings and empirical evidence to inform tax compliance literature on the appropriate approach to use when assessing constructs.

It is acknowledged that one of the limitations of this study was the available timeframe in which to complete the study. The change of research focus at the end of the first year reduced the availability of time to complete the study. Thus, it was not possible to conduct a pilot study prior to the actual survey distribution. Nevertheless, several precautionary measures were taken to ensure the reliability and validity of this

study. A pre-test was conducted with a panel of experts which consisted of tax academics and tax experts, before the survey was distributed. This stage served as the validation process and gathered feedback to improve the content of the questionnaire. Furthermore, most of the constructs selected were derived from literature established in the respective discipline of study, with the exception of one newly developed construct (complexity of procedure), which emerged from the qualitative study. Therefore, the measurements adapted have been tested in term of their validity and reliability.

Other limitations of this study are those mainly and inherently found when using a quantitative approach, such as the survey questionnaire approach. The survey approach, using self reporting, appears to be less reliable, especially as questions related to tax matters are quite sensitive, potentially incriminating or embarrassing (Hessing et al., 1988). For example, respondents may have exaggerated their perceptions or there may be non-response bias in the results. As discussed in Chapter 6, all precautionary measures were taken to minimise these problems such as comparing early respondents with late respondents to ensure that bias was not a problem using the response bias test as suggested by Dillman (2007) and Lindner, Murphy and Briers (2001). Most of the limitations highlighted were unavoidable and occur in most similar studies, with attempts to minimise the limitations. Nonetheless, the limitations do not diminish the relevance of the findings or the contributions made by the current study.

Generally, the compliance behaviour model (CBM) in this study offers a good explanation of custom agents' compliance behaviour in Malaysia with a strong prediction of behavioural intention (R-square value of 0.498). The slightly lower R-square value of 0.083 for behaviour suggests that there is inconsistency in the relationships between behavioural intention and behaviour. This inconsistency suggests that the relationship may yield more consistent results through the inclusion of moderators and other variables (Beck and Ajzen, 1991; Plant, 2009). Therefore, the CBM model developed in this study can be the reference model, with some modifications, for replication in the other area of indirect tax such as value added tax (VAT) or goods and services tax (GST). In addition, future studies should continue to extend the compliance model and also consider additional variables and moderating variables to examine the strength of the relationship between intention and behaviour. Other potential variables such as risk preference (Burton, 2007; Stephenson, 2010)



and incentives (Respondent 3, Chapter 3; Feld and Frey, 2007; Trivedi, Shehata and Mestelman, 2005) are worth considering when investigating business tax compliance as they will provide a better insight into the determining factors of compliance behaviour in business taxpayers and tax preparers.

The findings of this study have shown the importers to be one of the important variables influencing Customs agents' compliance intention. Future studies may also consider importers as the focus of study. Extension of study to the importer group would be interesting, in order to evaluate the magnitude of the relationships and to understand the compliance determinants of importers as indirect taxpayers. The findings may complement the findings of this study and provide a broader perspective on tax compliance in indirect tax studies.

Another important aspect for future research in tax compliance studies is the methodological contribution of this study with the application of co-variance based SEM-PLS and assessment of constructs as highlighted earlier. Future tax compliance may consider the assessment of constructs appropriately as suggested in the literature (for example Hair, Ringle et al., 2011; Hair, Sarstedt, Pieper and Ringle, 2012; Henseler, Ringle and Sinkovics, 2009). The correct categorisation of constructs, as reflective or formative constructs, is crucial, rather than presuming the constructs to be reflective, to avoid misleading when reporting data (Diamantopoulos and Winklhofer, 2001). SEM approach using PLS is a robust statistical technique to analyse the combination of reflective and formative constructs. Although the PLS method has received considerable attention in other research disciplines, little empirical evidence is found in tax compliance studies. Therefore, the development and empirical validation of this approach through this study is an important reference point for future tax compliance studies, to ensure that future tax compliance studies provide more accuracy in the findings through appropriate assessment of constructs and more robust analytical techniques.

### **10.3 CONCLUDING REMARKS**

Tax compliance is a complex behavioural issue and a sensitive topic. Understanding tax compliance behaviour is indeed challenging, not only from an academic point of view, but also from the perspective of governing institutions. The optimum compliance level may be possible to achieve by targeting appropriate taxpayers' groups. Therefore, it is important to understand how Customs agents or 'middle-men' make decisions and the roles played by Customs agents is of critical importance to Customs administration and policy makers.

This study has demonstrated that Customs agents, who represent the importer group, play an equally important (if not more important) role in tax compliance, either directly or indirectly influenced by their client (importer). Furthermore, the study acknowledged that socio-psychological factors and the role of institutions are equally important in increasing the level of compliance. Therefore, by understanding the interaction between taxpayers, the 'middle-men' and various tax compliance determinants, tax authorities may develop the appropriate strategies and measures to obtain the optimum compliance level. This study has made worthwhile contributions, in a different context of tax compliance studies with some fresh approaches in the methodology and behavioural theory, to tax compliance studies, by offering additional insights into the determinants of tax compliance, specifically in the context of indirect taxation.

Overall, the focus on Malaysia has demonstrated the relevance of this study to be generalisable to the policy context of other countries, due to similarities of Customs procedures which adopted the international conventions and guidelines such as those of the WCO, WTO and ASEAN. This study will also be relevant to other countries where Customs agents as the 'middle-men' were used to support importers, and for countries that allow company representatives and other indirect representatives to take charge of the declaration of Customs. There are some aspects of the model of this study that might also be relevant to examining compliance with their policy context, to achieve an optimum compliance level among various groups of taxpayers. Lastly, there is a need to reinforce the role of Customs agents and strengthen the relationship between Customs agents and Customs administration to promote voluntary compliance. This is also important for the profession of Customs agents who represent an important function that connects businesses and government.

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# **APPENDIX 1**

## **CUSTOMS AGENTS CODE OF ETHICS**

1. Under Section 90, Customs Act 1967, Customs agents, shipping agents and freight forwarder are appointed by the Director of Customs for the purpose of:
  - 1.1 To assist the Department in the course of establishing a faster, prudent and accuracy in Customs clearance service.
  - 1.2 To establish a Customs agent service quality that is respected, recognized and world-class.
  - 1.3 To promote “smart partnership” between Customs Department, custom agents and customers based on the respective law and regulations for national interest.
2. To achieve the above objectives, the Customs agents either in the organization or individual shall at all times:
  - 2.1 Adhere to Customs agents code of ethics as follows:
    - 2.1.1 Understand, comply with and are committed to the laws and Customs procedures in force to ensure that businesses would be able run properly and smoothly.
    - 2.1.2 Assist Customs in preventing smuggling and distribution of items such as dangerous drugs, firearms and prohibited goods
    - 2.1.3 Always behave honest when dealing with Customs to
      - Provide details and information that is correct and accurate when making or should apply for approval.
      - Not to cheat or conspiring or colluding with any party to defraud Customs authority and government.
      - Avoid promising or offering or giving bribes to feed in any member of Customs as an inducement or reward for doing or not doing anything involving the Customs Department.
      - Avoid giving gifts to Customs personnel. Gift is define as follows: including money, movable or immovable, vehicles, free fare, stocks, lottery tickets, travel, entertainment, services,

membership, any form of discounts or commissions, hampers, jewellery, jewellery, any grant, gift or anything of value given to or received by the officer, his wife or any other person, with no consideration (without consideration) or a reply known to the Customs personnel is not enough or sufficient.

2.1.4 Ethical, considerate and fair when dealing with Customs, namely to:

- Providing information and documents required at the time of official business.
- Do not force the Customs personnel to give special with request to do something beyond its jurisdiction or to the detriment of the other party.

2.1.5 Always courteous and be polite when dealing with Customs:

- Communicate with Customs and each other very well, mutual respect and avoid using words that sound rude and exalt.
- Dress appropriate and neat when dealing with Customs. Avoid dressing that is suggestive and ostentatious as opposed to values and ethics society.
- Avoid dealing with Customs in a state of drunkenness.

2.1.6 Act swiftly and report to the authorities the Department of Customs of any member of the Department who requests a feed of corruption or misuse of power and gifts as well as aberrant.

2.1.7 Adhere to all the time whatever the instructions and regulations issued by the Department related to the duties and responsibilities of an agent include:

- wearing uniform
- Other conditions such as in approval.

2.1.8 Every agent who deals with the Department are always required using identification passes issued by the Department within the Customs area.

2.1.9 All agents shall settle any outstanding of duties/taxes within the specified period.

## 2.2 Prohibited to do the following:

- 2.2.1 Using a pass belonging to someone else
- 2.2.2 Using another company to deal for self-interests
- 2.2.3 Approved agents cannot operate until it has been applied or have obtained Service Tax Licence control station
- 2.2.4 Company or business agents cannot be renamed, changed address, sold, transferred or assigned to any party without the permission of the Department
- 2.2.5 Exchange of premise for operations are not permitted except with the approval of the control station
- 2.2.6 Transfer employees from one company to another company other agents can only be made with the written approval of the controlling station. Once agreed upon by the station control, identification passes shall be returned
- 2.2.7 Importers and exporters will be allowed to appoint two agents for managing emissions trading. The State Customs Director may approve if more than two agents are required
- 2.2.8 Company agents cannot accept appointment as a third agent to the importer / exporter that already has two (2) business agents for the company unless specifically approved by the State Customs Director.

## 3. Procedure for Handling Misconduct / Violation of Customs Agent Code of Ethic

3.1 Pursuant to Section 90 (4) of the Customs Act 1967. Customs Director General may appoint an agent disciplinary panel to investigate suspected agent directly / indirectly in the activities of embezzlement, smuggling, fraud or misconduct code of ethics.

3.2 When agents disciplinary panel received instructions from the Director General of Customs, the following actions be taken:

- Issuing a show cause letter to agents / individuals and obtain a written reply within 14 days why action should not be taken against him.
- Conduct investigations on other parties that could help the investigation.

- To review all responses and evidence and prepare a complete report of investigation.
  - Confirm action
4. After receiving the recommendation of the Agents Disciplinary Panel, if found no prima facie, in this case Director General of Customs may impose any one or combination of the following penalties:
- 4.1 Warning and reprimand
  - 4.2 Revoke passes
  - 4.3 Cancellation of pass
  - 4.4 Blacklist
  - 4.5 Shortening the period of approval
  - 4.6 Lowering agent category
  - 4.7 Suspend the operation of the Customs
  - 4.8 Revoke license



## **APPENDIX 2**

### **INTERVIEW QUESTIONS - CUSTOMS OFFICIALS**

#### **PART 1: INTRODUCTION**

1. General introduction to researcher, affiliation, etc.
2. Technical introduction about the study

This study focuses on the compliance to Customs law specifically on the declaration of import. More specifically, questions will probe:

- The issues associated with businesses not complying with import declaration to lower import tax payment
- Identify the approach that the businesses use to lower the import tax payment
- Approach to improve compliance from the perspectives of regulatory authority.

The interview comprises a set of open-ended questions requiring your responses to ensure that I gain a full understanding of the measures you use and how you use them. Would you have any objections to the interview being tape-recorded? This would enable me to listen carefully and gain the greatest benefit from the interview. It also ensures that the accuracy of the data collected is preserved. Confidentiality is assured to all participants. No data will be associated with any individual or organisation. Ultimately, my research interest is in understanding compliance across different type of businesses involved in the process of import declaration, and not in particular cases.

#### **PART 2: IMPORT TAX AND COMPLIANCE**

- 1) **I would like hear you thought about business compliance towards Customs regulatory procedure especially about the issue of improper declaration on import activities?**

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2) What are the causes to this problem and why does this happen?

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3) Who do you think the main parties involved?

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4) What are the ways tax payment can be defrauded in the import declaration?

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5) How does this situation can be improved and what are the measures taken by Customs department in reducing the non-compliance rate?

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6) Before I end this conversation, do you have any other points to add or any other issues regarding the import declaration that you wanted to share?

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7) Thank you very much for your input on throughout this conversation. Can I call again if there is any further information that I would like to clarify from you?

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### **PART 3: DEMOGRAPHIC INFORMATION OF RESPONDENT**

DESIGNATION : \_\_\_\_\_

GRED OF SERVICE : \_\_\_\_\_

LENGTH OF SERVICE : \_\_\_\_\_ YEARS

GENDER : \_\_\_\_\_

## APPENDIX 3

### SUMMARY OF INTERVIEW FINDING (CUSTOMS OFFICIALS)

RESPONDENT NO	GENERAL PERCEPTION	SPECIFIC PERCEPTION	TYPES OF NON-COMPLIANCE	IMPROVING COMPLIANCE
RES 1	“This is the hardest area that we have to face in our routine work..not all businesses are honest especially in paying tax	“The focus on compliance should be on the forwarding agents not the importer. Importer just furnished the required documents and the agents who manipulate the declaration to pay lower duty”	“a lot of cases in import declaration, not all of the item being imported were declared especially in the mixed consignment.. devalue the price..manipulation of tariff code are the common cases..”	We also have a workshop from time to time to explain to them about the right way of making a declaration... We have to treat them as a partner and think of a softer approach rather than penalising them right away.
RES 2	“ This is the mentality of our businesses..too profit oriented..there is lack of awareness in following the rules and procedures”	“Agents know too much the trick and trade of the business..they have been in this business for so long...they have the know-how”	“The obvious case in import declaration is the STS system..the function of ‘direct-release’ ... .Because of this facility agents taking advantages with lesser physical inspection. This is why they manipulating the declaration to avoid tax..	“We have to educate the businesses..provide them with proper advice and we also have to play our role in ensuring the laws are properly enforced”
RES 3	“ Business compliance rate in Malaysia is still low compared to developed countries..It is part of the culture. We can change the procedure, increase penalty and compound but it is hard to change the attitude ”	“ Forwarding agents represents their clients whether importer or exporter...they need the business...we will continue facing the problem of agent not complying to our rule and procedures especially in paying the correct amount of duty and taxes”	“They are selling their services as a ‘package’ ...quote a specific price for a shipment and then work out on the declaration on how to meet the price. That’s where they play around with pricing, quantity, tariff code etc..’	‘Probably we have to introduce some kind of incentives to make them more compliance..for example our department can issue a certification to the highly compliant agents..with the certification they could get a special privileges such as fast track clearance”

RESPONDENT NO	GENERAL PERCEPTION	SPECIFIC PERCEPTION	TYPES OF NON-COMPLIANCE	IMPROVING COMPLIANCE
RES 4	“What has the deputy DG emphasis not is on unreasonable declaration of pricing of goods, it is the issue of under-valuation”	“The agents should be held accountable for the declaration because they are the one who lodge the declaration and provide the tax calculation to client”	“It is commonly that the agents who declare the price artificially”	“We have to play our part in increasing our enforcement effort especially PASCA team. If our PASCA team is strong and have enough manpower..I strongly believe that the WTO valuation and recommendation could be fully implemented in the import department so that clearance could be expedited and at the same time whatever amount of tax underpaid can be collect back by the PASCA team...”
RES 5	“Regulatory compliance is a good area to look at. The issue of compliance is an on-going problem with our business community ”	“Every import declaration there will be a column that agents have to signed, he/she are responsible of what being declared not the importer..there are some Customs agents out there intent to cheat Customs department especially the new up-coming agents”	“pricing of goods declared is the most problematic..the price that is being declared sometimes doesn’t make sense..fabric for instance declared for less than RM1per kg..how much it is being sold on the market per meter..does this make sense?”	“Cancel and revoke the license of agents who does not comply with our law...It is not easy now to obtain license because the issuance of new license have been stop for quite a while now”
RES 6	‘Smuggling, under-declaration or whatever you called happened because there are duties involved...and there always be an interest parties who does not like the idea of paying tax. It’s like a burden to them”	“Agents are the one who lodge the declarations. They suppose to know the correct way to lodge import declarations because we have provided training to them. Without adequate knowledge and passed the agents exam, they can’t get their licence”	“Even fruits which has low duty were declared at lower price...thousands containers of fruits imported monthly.. How much the government will lose its revenue?. That does not include high duty items such as tyre, liquor, electrical goods”	“ Enforcing the rules as in our PTK45 that they have sit for the exam is part of the departments’ effort to increase their knowledge and know what is their responsibility to Customs and represented client so that compliance could be improved”

<b>RESPONDENT NO</b>	<b>GENERAL PERCEPTION</b>	<b>SPECIFIC PERCEPTION</b>	<b>TYPES OF NON-COMPLIANCE</b>	<b>IMPROVING COMPLIANCE</b>
RES 7	“If we refer to issue on import activities the main issue is on the improper declaration referring to the price and quantity that is not declared accordingly.. if they declare correctly they will not gain much profit ”	“Normally from our experience, it is the forwarding agents that usually does not comply with our procedure because they sell their service by ‘package’ ”	“..declare less quantity, lower value, declare goods partially, declare dutiable as non dutiable goods or the tariff that has a lower tax value”	“ Have to revert back to the theory on how to lodge a correct declaration..keep educate the agents...promote awareness”
RES 8	“If the importer are willing to import the goods into Malaysia, it means that they are willing to pay import duty”	“Through my experience on ‘fabricated cases’, usually the agent who fabricates the documents to pay lower import tax or avoid paying import tax”	“In reality the agents manipulate the tariff code and value to pay lower tax”	“Issue of incorrect declaration is very hard to deter. Especially the agents are competing against each other..It’s like a price war you know..we have to keep our enforcement ongoing ”

## APPENDIX 4

### ETHICS COMMITTEE APPROVAL

#### **Ethics Review for your PhD Project**

Stella Fuller [Stella.Fuller@nottingham.ac.uk]

You forwarded this message on 28/01/2014 00:40.

**Sent:** 15 January 2013 16:41

**To:** [lixmm3@nottingham.ac.uk](mailto:lixmm3@nottingham.ac.uk)

**Determinant Factors of Agents Compliance Behaviour Towards Import Tax in Malaysia: Theory of Planned Behaviour**

Dear Mizra

I am writing to confirm a favourable ethical opinion for the above research on the basis of the documentation submitted. This opinion was given on 9<sup>th</sup> January 2013.

The following conditions apply to this favourable opinion:

1. The research must follow the protocol agreed and any changes will require prior NUBS REC approval.
2. The appropriate NUBS REC documentation must be completed at the end of the research project.

For further information about the School's Research Ethics Committee or approval process, please contact the Research Ethics Officer, Adam Golberg at [adam.golberg@nottingham.ac.uk](mailto:adam.golberg@nottingham.ac.uk) or +44 (0)115 846 6604.

Good luck with the research.

*Stella Fuller*

Research Support Administrator  
Room B34b (North)  
Nottingham University Business School  
Jubilee Campus  
Nottingham  
NG8 1BB

0115 84 67581

working hours 9:00 - 5:15 Monday to Friday

## **APPENDIX 5**

### **LIST OF INTERVIEW QUESTIONS – CUSTOMS AGENTS/ ASSOCIATIONS**

#### **List of Interview Questions**

1. I would like to hear your thought about the long standing issue of improper declaration of import by some forwarding agents which affects the revenue collection of Customs department. What are the causes to this problem in your opinion?
2. How can this situation be improved?
3. In your opinion, what motivates agents to comply with import declaration and pay import tax correctly?
4. Do any other agents/association members that you know have shared their experience about being caught by our enforcement team due to under-declaration of good? Aren't they afraid of their agent's license being revoked? Are they being penalised for example have to pay high penalty and imprisonment? Do you think there are sufficient provisions in the law to deter tax evader?
5. What is your opinion about the cost to comply with Customs requirement? Do you think that requirements are excessive, incremental in cost that makes the agent's profit margin smaller, thus finding other means to declare less to Customs?
6. Have you or any of your friends/association members have ever experienced that their client requested to declare less import tax than what they supposed to pay? What are your decisions? Do you agree to the request? Do they afraid of losing their clients by not following their client request?
7. Finally, there are views about paying less tax by various means such as under-declaration because they feel that the money will be spent unjustifiably by the government and they are not getting the fair value in terms of benefit received from the government, such as education, medical and infrastructure. Do you agree with this statement? What is your opinion?
8. How can agents assist in the overall improvement to the collection of Customs import revenue? Do you think that Customs administration plays an important role in making compliance easier?
9. Before I end this conversation, do you have any other points to add or any other issues regarding the import declaration that you wanted to share?

## APPENDIX 6

### **LETTER OF SUPPORT FROM THE ROYAL MALAYSIAN CUSTOMS DEPARTMENT**



IBU PEJABAT JABATAN KASTAM DIRAJA MALAYSIA  
KOMPLEKS KEMENTERIAN KEWANGAN  
NO.3, PERSIARAN PERDANA, PRESINT 2  
PUSAT PENTADBIRAN KERAJAAN PERSEKUTUAN  
62596 PUTRAJAYA  
MALAYSIA

No. Tel : 03-88822137  
No. Fax : 03-88895875  
Web : [www.customs.gov.my](http://www.customs.gov.my)



Diktiraf MS ISO 9001 : 2000  
Pengurusan Pembayaran Kepada Pembekal dan  
Warga Kastam Diraja Malaysia di Ibu Pejabat

Rujukan Kami : KE.HG(63)464/07-1 Klt.22 ( 49 )  
Tarikh : 4 Oktober 2012

#### **KEPADA SESIAPA YANG BERKENAAN**

Tuan,

#### **SOAL SELIDK DAN TEMUBUAL KE ATAS EJEN-EJEN PENGHANTARAN SELURUH MALAYSIA**

Dengan hormatnya saya merujuk kepada perkara di atas.

2. Sukacita dimaklumkan bahawa Encik Mirza Bin Mohamed merupakan seorang pegawai di Jabatan Kastam dan sedang melanjutkan pengajian di peringkat doktor falsafah (Ph.D) di Nottingham University Business School, United Kingdom. Beliau kini sedang menjalankan kajian berkaitan dengan Jabatan dan memerlukan input daripada ejen-ejen penghantaran di seluruh Malaysia, yang mana hasil kajian ini kelak boleh menjadi input kepada Jabatan bagi tujuan penambahbaikan kualiti perkhidmatan di masa hadapan.

3. Oleh yang demikian, adalah diharap pihak tuan dapat memberikan kerjasama kepada beliau.

Sekian, terima kasih.

**"BERKHIDMAT UNTUK NEGARA"**

Saya yang menurut perintah,

**(DATO' AHMAD NADZRI BIN EMBONG)**

Bahagian Khidmat Pengurusan dan Sumber Manusia  
b.p Ketua Pengarah Kastam  
Malaysia.

s.k Mirza Bin Mohamed  
Nottingham University Business School



## **APPENDIX 7**

### **LIST OF ACT AND SUBSIDIARY ACTS**

#### **1) ACTS**

- (i) Customs Act 1967

#### **2) SUBSIDIARY ACTS**

- (i) Customs Regulations 1977
- (ii) Customs Regulation (Prohibited Areas)(Johor Bahru) 1977
- (iii) Customs Regulation (Warehouse Rent Handling and Weighing Charges) 1977
- (iv) Customs Payment Order 1977
- (v) Customs Order (Warehouse Rent Handling and Weighing Charges) 1977
- (vi) Customs Regulations (Processed Palm Oil) 1984
- (vii) Customs Duty Order (Langkawi) 1986
- (viii) Customs Duty Order (Exemption) 1988
- (ix) Customs Order (Exemption) (Processed Oil Products) 1988
- (x) Customs Duty Order (Exemption) (Goods from ASEAN Countries) (Preferential Tariff) 1988
- (xi) Customs Duty Order (Exemption) Goods from ASEAN Countries) 1988
- (xii) Customs Duty Order (Pengkalan Kubur Free Zone) 1989
- (xiii) Customs Duty Order (Exemption) (Goods from ASEAN Countries) (Preferential Tariff) 1995
- (xiv) Customs Duty Order 1996, amended 2013
- (xv) Customs Order (Temporary Exemption) (Processed Palm Oil) 1996
- (xvi) Customs Regulations (Completely Knocked Down dan Completely Built Up) (Takrif No. 1) 1998
- (xvii) Customs Regulations (Completely Knocked Down dan Completely Built Up) (Takrif No. 2) 1998
- (xviii) Customs Regulations (Valuation Rules) 1999
- (xix) Order Takrif Nilai (Labuan) 1999
- (xx) Order Takrif Nilai (Langkawi) 1999
- (xxi) Customs Order (Sekatan Pergerakan) 2000
- (xxii) Customs Duty Order (Tioman) 2004
- (xxiii) Customs Duty Order (Goods from ASEAN Countries)(ASEAN Harmonise Tarif /Tatanama Tarif Berharmonis ASEAN and Preferential Tariff) 2004
- (xxiv) Customs Order (Nilai-Nilai) (Isi Kelapa Sawit) (Kerjasama Ekonomi Komprehensif antara ASEAN dan China) 2005
- (xxv) Customs Order (Import Restrictions/Larangan Mengenai Import) 2008
- (xxvi) Customs Order (Export Restriction/Larangan Mengenai Eksport) 2008

## APPENDIX 8

### **PRE-TEST COMMENTS AND SUGGESTIONS**

Comment No.	Detail Comments	Actions
1	Double barrel questions - please check on any double barrel question example question on laws and regulation should be break into two questions – one question on law and another question on regulation.	Separate the question into two different items
2	Background information - the categorical value should not be overlap	Re-categories the value to avoid overlapping
3	Simplify language. Some of the wording and sentences are confusing	Questions were refined with using simplified wording.
4	Set the background information/ demography as the last section so that the respondent could focus straight on the questionnaire	The questionnaire was rearranged with the demography section in the last section as this was suggested by most of the reviewer.
5	Re-arrange positive and negative questions.	The questions were rearranged. Instead placing a mixture of positive and negative questions in a sequence manner, the negative questions were place in a same grouping and sequence or vice versa.
6	Avoid lengthy questions. Questions should be short and posed in a simple language as to avoid confusion to the potential respondent.	It is decided that the constructs in the study remain unchanged as this will affect the validity of this study. However, the questions were refined with using simplified wording instead of lengthy type of questions. This will indirectly reduce the amount of time needed to understand and answer each of the questions posed.
7	The language has to be carefully selected. As the public service department, Malay language is our official language for daily communication with public. Using one language (Malay) would be the most appropriate and adding translation to each question will facilitate some of the respondents in understanding the questionnaire better.	The researcher provided a bi-lingual questionnaire.  Process: Originally, questions were formulated in the English language as most of the questions or items were adapted from the previous instrument, which was originally created in the English language. However, after taking into

		<p>account several factors, it was decided that the questionnaire should be provided in a bilingual version (English and Malay) because not all Malaysians are competent in the English language. Moreover, it was expected that a bilingual questionnaire would improve the response rate since respondents are usually comfortable to read or listen to the language that they can understand easily (Malhotra et. al., 2008). The Malay Language is the mother tongue of the Malays and has become the main and official language of Malaysia since its independence in 1957. It has also become the official language in public services. It is widespread and understood by most people in this country. The English language, on the contrary, is unofficially recognized as a second language in Malaysia. During the colonial era and after independence, the English language became the language of higher education. Today, it remains the language of international trade. Therefore, it is seen as an alternative for those who are not fluent in the Malay language. Ethnic groups to which the Malay language is not their first languages are very likely to have a good command of the English language.</p>
8	Carefully when translating from English to Malay language as certain words or sentences can bring different meaning when translated.	The translations were re-checked using the Malay-English Dictionary ( <i>Kamus Dewan Bahasa</i> ) and resend to the panel for final validation process.
9	Sentences must be in a way it asked the perception of the respondent for the purpose of analysing their behaviour towards your research objectives. Avoid double perception sentences.	All the sentences in the questions were double checked with the corresponding literature where the questions were derived. This is to ensure that the questions adapted were phrased accordingly.
10	Self developed questionnaire – make sure follow the proper protocol in developing self questionnaire. Check on the content validity process to make sure that the questions developed valid and reliable.	The questions that were derived from the relevant literature have undergone the validity process from its author. The newly developed questions were created from the item pool and were sent to the panel of reviewer as part of content validity process.

## APPENDIX 9

### SURVEY QUESTIONNAIRE

#### Bahagian 1 (Section 1)

##### A) Pentadbiran cukai import (Import tax administration)

Bagi setiap kenyataan di bawah ini, sila pilih SATU jawapan sahaja dan BULATKAN pada angka yang sesuai. Tolong tandakan jawapan bagi SEMUA soalan.

(Choose ONE answer only and CIRCLE on the appropriate number for each of the statements. Please answer ALL of the questions)

SEKSYEN A: Soalan berikut adalah berhubung dengan pandangan anda terhadap undang-undang kastam (Section A: Following questions about your opinion about Customs law)	Sangat tidak setuju (Strongly disagree)				Sangat setuju (Strongly Agree)
1 Undang-undang berhubung cukai import adalah <i>tidak jelas</i> (The laws on import tax are <i>ambiguous</i> )	1	2	3	4	5
2 Undang-undang berhubung cukai import adalah mencukupi (There are sufficient provision in the laws on import tax)	1	2	3	4	5
3 Undang-undang berhubung cukai import adalah <i>tidak dikuatkuasakan</i> dengan serius (The law on import tax are <i>not seriously implemented</i> )	1	2	3	4	5
4 Hukuman denda dan penjara dalam undang-undang cukai import adalah <i>ringan</i> (Penalty and imprisonment on laws related to import tax are considered <i>inadequate</i> )	1	2	3	4	5
5 Undang-undang berhubung cukai import <i>ada memperuntukkan</i> hukuman denda dan penjara bagi kesalahan-kesalahan yang dilakukan (The laws on import tax <i>adequately provide</i> penalty and imprisonment in relation to offences committed)	1	2	3	4	5

SEKSYEN B: Soalan berikut adalah berhubung dengan pandangan anda terhadap penguatkuasaan undang-undang kastam (Section B: Following questions about your opinion towards Customs law enforcement)	Sangat tidak setuju (Strongly disagree)				Sangat setuju (Strongly Agree)
1 Agen yang tidak membayar cukai import dengan selalu <i>didenda</i> oleh Kastam (Agents who failed to pay import tax are always being <i>penalised</i> by Customs)	1	2	3	4	5
2 Kastam selalu dapat <i>mengesan</i> agen yang tidak membayar cukai import (Customs always <i>manage to detect</i> agents who fail to pay import tax)	1	2	3	4	5
3 Agen yang tidak membayar cukai import <i>tidak di dakwa</i> oleh Kastam (Agents who failed to pay import tax <i>are not being prosecuted</i> by Customs authority)	1	2	3	4	5
4 Penguatkuasaan Kastam adalah <i>tegas</i> berkenaan pelarian cukai import (Customs enforcement are <i>stringent</i> with regards to tax evaders)	1	2	3	4	5
5 Kastam <i>tidak pernah</i> membuat pemeriksaan terhadap agen yang tidak membayar cukai import (Customs <i>never make any inspection</i> on forwarding agents who fail to pay import tax)	1	2	3	4	5

SEKSYEN C: Soalan berikut adalah berhubung dengan Prosedur Pengiklanan Import (Section C: Following questions about import declaration procedure)	Sangat tidak setuju (Strongly disagree)				Sangat setuju (Strongly Agree)
1 Prosedur pengiklanan import tidak fleksibel (Import declaration procedure is not flexible)	1	2	3	4	5
2 Prosedur pengiklanan import adalah tidak jelas (Import declaration procedure is ambiguous)	1	2	3	4	5
3 Prosedur pengiklanan import sering berubah-ubah (Too frequent changes in import declaration procedure)	1	2	3	4	5
4 Prosedur pengiklanan import mudah difahami (Import declaration procedure is easy to understand)	1	2	3	4	5
5 Prosedur pengiklanan import terlalu ketat (Import declaration procedure is too rigid)	1	2	3	4	5
6 Prosedur pengiklanan import adalah mencukupi (There is sufficient provision in import declaration procedure)	1	2	3	4	5
7 Tiada keseragaman pendapat terhadap prosedur pengiklanan import di antara pegawai (There is no uniformity in import declaration procedure between officers)	1	2	3	4	5
8 Prosedur pengiklanan import semasa melambatkan proses pembayaran cukai (Current Import declaration procedure delays the process of paying tax)	1	2	3	4	5

SEKSYEN D: Soalan berikut adalah berhubung dengan pandangan anda mengenai kualiti perkhidmatan (Section D: Following questions about your opinion about service quality)		Sangat tidak setuju (Strongly disagree)			Sangat setuju (Strongly Agree)		
1	Pejabat kastam mempunyai peralatan yang lengkap (Customs office has adequate equipment)	1	2	3	4	5	
2	Pegawai kastam sentiasa bersedia membantu pelanggan (Customs officers are always available to assist customers)	1	2	3	4	5	
3	Agen boleh bergantung harap dengan pegawai-pegawai kastam (Customs officers are trustworthy)	1	2	3	4	5	
4	Pegawai kastam bersopan-santun bila berurusan dengan pelanggan (Customs officers are always courteous when assisting customers)	1	2	3	4	5	
5	Pegawai kastam memberi maklumat yang tepat apabila menguruskan permasalahan pelanggan (Customs officers can provide accurate information when managing customers' problem)	1	2	3	4	5	
6	Pegawai kastam berkomunikasi dengan baik apabila berurusan dengan pelanggan (Customs officers communicates well with customers)	1	2	3	4	5	
7	Pegawai kastam yang berurusan dengan agen adalah berkebolehan dan berpengetahuan (Customs officers who deals with customers are capable and knowledgeable)	1	2	3	4	5	
8	Pegawai kastam sentiasa memahami kehendak pelanggan (Customs officers are always understand customers' requirement)	1	2	3	4	5	
9	Maklumat yang dikemukakan kepada pihak kastam adalah terjamin keselamatannya (Information provided to Customs are secured)	1	2	3	4	5	
10	Pegawai Kastam adalah cekap apabila memberikan perkhidmatan (Customs officers are very responsive when providing service to customers)	1	2	3	4	5	

## B) Cukai Import (Import Tax)

SEKSYEN E: Soalan berikut merupakan pandangan anda terhadap cukai import (Section E: Following questions about your views on import tax)		Sangat tidak setuju (Strongly disagree)			Sangat setuju (Strongly Agree)		
1	Melaksanakan tanggungjawab membayar cukai import adalah <b>tindakan</b> yang <b>membanggakan</b> (Fulfilling the obligation in paying import tax is something to be proud of)	1	2	3	4	5	
2	Syarikat kami merasakan telah melakukan sesuatu yang bermanfaat kepada masyarakat dengan membayar cukai import. (We feel that we have done something that is beneficial to the society by paying import tax)	1	2	3	4	5	
3	Membayar cukai import merupakan <b>sumbangan</b> penting kepada <b>negara</b> (Paying import is an important contribution to the country)	1	2	3	4	5	
4	Membayar cukai import dapat mengelakkan syarikat daripada dikenakan tindakan <b>undang-undang</b> (Paying import tax would avoid company from being penalised)	1	2	3	4	5	
5	Membayar cukai import akan <b>mengurangkan keuntungan</b> syarikat (Paying import tax will reduce company's profit)	1	2	3	4	5	
6	Adalah <b>tidak menjadi satu kesalahan</b> jika sesekali membayar cukai import kurang daripada nilai sebenar (It is not an offence sometimes to pay lower import tax than the actual value )	1	2	3	4	5	
7	Syarikat kami <b>merasa bersalah</b> jika tidak membayar cukai import dengan betul (Our company will feel reprehensive by not paying import tax)	1	2	3	4	5	
8	Membayar cukai import secara berterusan akan mengakibatkan <b>peningkatan kos</b> barangan dan perkhidmatan (Paying import tax continuously will increase the cost of goods and services)	1	2	3	4	5	



SEKSYEN F: Soalan berikut adalah pandangan anda berhubung pengurusan hasil cukai import (Section F: Following questions about the administration of import tax revenue)		Sangat tidak setuju (Strongly disagree)					Sangat setuju (Strongly Agree)				
1	Faedah yang diperolehi daripada kerajaan seperti pelajaran, kesihatan dan infrastruktur sebagai ganti kepada cukai import yang dibayar adalah adil dan saksama (Benefits received from government such as education, health and infrastructure in exchange of import tax paid are fair and equitable)	1	2	3	4	5					
2	Kadar cukai import yang dikenakan masih tinggi jika dibandingkan dengan faedah yang diberikan oleh kerajaan. (Import tax rate imposed are still at a high rate compared to benefits provided by government)	1	2	3	4	5					
3	Faedah yang diberikan oleh kerajaan adalah berpatutan hasil daripada amaun cukai import yang telah dibayar (Benefits given by the government are reasonable in exchange to the amount of import tax paid)	1	2	3	4	5					
SEKSYEN G: Soalan berikut adalah berkenaan dengan hubungan terhadap pelanggan dan rakan-rakan anda. (Section G: Following questions is about your relationship with clients and business associates)		Sangat tidak setuju (Strongly disagree)					Sangat setuju (Strongly Agree)				
1	Pelanggan kami berpendapat kami perlu mengikrarkan dagangan bercukai import dengan betul berdasarkan perundangan kastam. (Our client would think that we should declare taxable good accordingly based on Customs law)	1	2	3	4	5					
2	Pelanggan kami berpendapat adalah tidak perlu mengikrarkan sepenuhnya dagangan bercukai import supaya cukai dapat diijimatkan oleh syarikat. (Our client would think that it is not necessary to fully declare taxable goods to save some tax payment)	1	2	3	4	5					
3	Pelanggan kami menyokong jika kami dapat mengurangkan jumlah pembayaran cukai import dari amaun yang sepatutnya perlu dibayar. (Our client would approve our decision to understate the import tax)	1	2	3	4	5					
4	Kami selalu mengikuti nasihat pelanggan kami supaya mengikrarkan dagangan bercukai import mengikut taksiran kastam. (We always follow our client's advice to pay import tax according to Customs assessment)	1	2	3	4	5					
5	Rakan-rakan ejen berpendapat kami perlu membayar cukai import berdasarkan taksiran kastam (Other agents who important to us agree if we pay import tax according to Customs assessment)	1	2	3	4	5					
6	Rakan-rakan ejen berpendapat adalah tidak perlu mengikrarkan sepenuhnya dagangan bercukai import supaya cukai dapat diijimatkan oleh syarikat. (It is expected by other agents who important to us, that we should not full-declare taxable good to save tax)	1	2	3	4	5					
7	Rakan-rakan ejen lain kebiasaannya tidak mengikrarkan dagangan bercukai import sepenuhnya untuk mengurangkan pembayaran cukai import. (Other agents who important to us usually would not fully declare taxable goods to save tax)	1	2	3	4	5					
8	Secara amnya rakan-rakan ejen tidak membuat pengurangan dalam pengikraran dagangan bercukai import daripada yang sepatutnya walaupun jika berada dalam keadaan terdesak. (Generally other agents who is important to us would not understate import tax although they are in difficult situation)	1	2	3	4	5					
SEKSYEN H: Soalan berikut adalah berkaitan dengan syarikat anda apabila menguruskan urusan berkaitan cukai import. (Section H: Following questions about your company in managing import tax)		Sangat tidak setuju (Strongly disagree)					Sangat setuju (Strongly Agree)				
1	Adalah mudah bagi syarikat kami untuk mematuhi perundangan kastam (It would be very easy for the company to comply with Customs law)	1	2	3	4	5					
2	Jika mempunyai peluang syarikat kami akan mengikrarkan sebahagian sahaja dagangan supaya cukai dapat diijimatkan (If we have the opportunity we will declare the goods partially so that we can save tax)	1	2	3	4	5					
3	Syarikat kami percaya yang kami boleh mengurus pembayaran cukai import dengan betul walaupun syarikat mempunyai masalah kewangan. (We believe that our company can manage to pay import tax accordingly even if the company faced financial difficulties)	1	2	3	4	5					
4	Adalah mudah untuk membuat pelarian cukai import tanpa dikesan oleh pihak kastam (It would be easy to understate import tax amount without being detected by Customs)	1	2	3	4	5					
5	Mengikrarkan dagangan bercukai sebagai tidak bercukai bagi tujuan pelarian cukai adalah sesuatu yang sukar (Declaring taxable good as non-taxable goods for the purpose of understate tax payment is not an easy task)	1	2	3	4	5					

### C) Pengikraran Import (Import Declaration)

#### SEKSYEN I:

Soalan berikut adalah berhubung dengan etika

(Section I: Following questions about ethics)

	Sangat tidak setuju (Strongly disagree)				Sangat setuju (Strongly Agree)
1 Secara etikanya syarikat kami akan merasa bersalah untuk terlibat dengan perlakuan penipuan di dalam pengikraran import (Ethically our company will feel reprehensible with the involvement in falsifying import declaration)	1	2	3	4	5
2 Pandangan tentang keadilan sistem cukai import tidak sepatutnya mempengaruhi syarikat kami di dalam urusan pengikraran import (Views on fairness of import tax system will not affect our company's decision in import declaration matters)	1	2	3	4	5
3 Syarikat kami tidak patut merasa bersalah dengan mengikrar sebahagian sahaja dagangan import jika saya merasakan sistem cukai yang sedia tidak adil (Our company should not feel reprehensible by not fully declared goods in import declaration if they feel that the current tax system is not fair)	1	2	3	4	5
4 Syarikat kami tidak patut merasa bersalah untuk tidak mengikrar dagangan import dengan betul jika merasakan tidak menikmati faedah daripada cukai import yang dibayar (Our company should not feel reprehensible by not declaring correct description of import goods if they do not get the benefit from the tax paid)	1	2	3	4	5
5 Adalah tidak salah jika tidak memaklumkan kepada pihak kastam atas kesilapan pengikraran melibatkan cukai import kurang daripada sepatutnya. (There is nothing wrong for not informing Customs if there is any discrepancies and shortage in import tax payment.)	1	2	3	4	5

**Seksyen J: Soalan berikut merupakan kenyataan mengenai syarikat anda. Sila nyatakan sejauh manakah perkara-perkara berikut berlaku pada pengikraran import syarikat anda.**

(Section J: Following questions are about your personal statements. Indicate the extent to which any of the following have ever applied to your company's import declaration)

- Di tahan pengikraran di dalam sistem oleh pihak kastam  
(Declaration in the system was suspended by Customs)
- |                         |                    |                              |                        |                   |
|-------------------------|--------------------|------------------------------|------------------------|-------------------|
| 1                       | 2                  | 3                            | 4                      | 5                 |
| Tidak Pernah<br>(Never) | Jarang<br>(Rarely) | Kadang-Kadang<br>(Sometimes) | Selalu<br>(Very Often) | Kerap<br>(Always) |
- Dikenakan kompaun (spt. kesalahan ikrar kod tariff, ikrar tidak tepat)  
(Being compounded e.g. on various offence such tariff code classifications, inaccurate descriptions)
- |                         |                    |                              |                        |                   |
|-------------------------|--------------------|------------------------------|------------------------|-------------------|
| 1                       | 2                  | 3                            | 4                      | 5                 |
| Tidak Pernah<br>(Never) | Jarang<br>(Rarely) | Kadang-Kadang<br>(Sometimes) | Selalu<br>(Very Often) | Kerap<br>(Always) |
- Gagal mengemukakan sijil tempasal (C.O.O) seperti yang dikehendaki  
(Failed to produce Certificate of Origin as required)
- |                         |                    |                              |                        |                   |
|-------------------------|--------------------|------------------------------|------------------------|-------------------|
| 1                       | 2                  | 3                            | 4                      | 5                 |
| Tidak Pernah<br>(Never) | Jarang<br>(Rarely) | Kadang-Kadang<br>(Sometimes) | Selalu<br>(Very Often) | Kerap<br>(Always) |
- Taksiran/penilaian semula harga oleh pihak kastam disebabkan harga ikrar rendah  
(Price reassessment / revaluation by Customs due to under-declaration of value)
- |                         |                    |                              |                        |                   |
|-------------------------|--------------------|------------------------------|------------------------|-------------------|
| 1                       | 2                  | 3                            | 4                      | 5                 |
| Tidak Pernah<br>(Never) | Jarang<br>(Rarely) | Kadang-Kadang<br>(Sometimes) | Selalu<br>(Very Often) | Kerap<br>(Always) |
- Kod tariff kastam diklasifikasikan semula oleh pihak kastam disebabkan salah ikrar  
(Re-classification of Customs tariff code by Customs due to incorrect classification)
- |                         |                    |                              |                        |                   |
|-------------------------|--------------------|------------------------------|------------------------|-------------------|
| 1                       | 2                  | 3                            | 4                      | 5                 |
| Tidak Pernah<br>(Never) | Jarang<br>(Rarely) | Kadang-Kadang<br>(Sometimes) | Selalu<br>(Very Often) | Kerap<br>(Always) |
- Tidak mengikrar keterangan dagangan dengan betul  
(Not declaring correct descriptions of goods)
- |                         |                    |                              |                        |                   |
|-------------------------|--------------------|------------------------------|------------------------|-------------------|
| 1                       | 2                  | 3                            | 4                      | 5                 |
| Tidak Pernah<br>(Never) | Jarang<br>(Rarely) | Kadang-Kadang<br>(Sometimes) | Selalu<br>(Very Often) | Kerap<br>(Always) |



<b>SEKSYEN K: Soalan berikut adalah berhubung dengan niat terhadap pengikraran dagangan import</b> (Section K: Following questions about your intention on import declaration )		Sangat tidak setuju (Strongly disagree)			Sangat setuju (Strongly Agree)		
1	Syarikat kami akan membayar cukai import dengan betul (Our company is willing to pay the correct amount of import tax)	1	2	3	4	5	
2	Syarikat kami akan membuat pengikraran mengikut kod tariff kastam yang sebenar (Our company will lodge declaration according to the actual Customs tariff code)	1	2	3	4	5	
3	Syarikat kami akan membuat pengikraran berdasarkan penilaian harga kastam (Our company will lodge declaration according to Customs valuation)	1	2	3	4	5	
4	Syarikat kami akan membuat pengikraran mengikut kuantiti sebenar dagangan (Our company will lodge declaration according to actual quantity of goods)	1	2	3	4	5	
5	Syarikat kami akan patuh kepada prosedur kastam berkaitan pengikraran import (Our company will adhere to Customs import declaration procedure)	1	2	3	4	5	
6	Syarikat kami sanggup membayar cukai import jika terdapat kekurangan sewaktu taksiran cukai import (Our company is willing pay import tax on any discrepancies that arises in the import declaration during the assessment of import tax)	1	2	3	4	5	
7	Syarikat kami akan membuat pengikraran mengikut invoice sebenar (Our company will lodge declaration according to the actual invoice)	1	2	3	4	5	
8	Syarikat kami akan mengikrarkan dagangan import mengikut dokumen sebenar yang diberi oleh pengimport (Our company will declare goods in import declaration based on the actual documents from importer)	1	2	3	4	5	

**Seksyen L: Soalan berikut adalah berhubung dengan pengetahuan. Sila nyatakan sejauh manakah perkara-perkara berikut menjadi kebiasaan pada anda di dalam meningkatkan pengetahuan perkastaman. Sila pilih satu jawapan sahaja dan bulatkan bagi setiap soalan yang dikemukakan. Tolong tandakan semua jawapan bagi setiap soalan.**

Section L: Following questions are about your knowledge. (Choose only ONE answer and circle on the appropriate number for each of the statements. Please answer ALL of the questions.)

- Memastikan ilmu pengetahuan tentang perkastaman anda ditahap yang terkini (seperti berkursus, rujuk laman web atau rujuk terus kepada kastam)  
(Ensuring knowledge on Customs is up-to-date – e.g. attended courses, refer websites or direct consultation from Customs)  
 1-----2-----3-----4-----5  
 Tidak Pernah      Jarang      Kadang-Kadang      Selalu      Kerap  
 (Never)      (Rarely)      (Sometimes)      (Very Often)      (Always)
- Menghadiri kursus-kursus yang dianjurkan oleh pihak kastam.  
(Attended courses conducted by Customs)  
 1-----2-----3-----4-----5  
 Tidak Pernah      Jarang      Kadang-Kadang      Selalu      Kerap  
 (Never)      (Rarely)      (Sometimes)      (Very Often)      (Always)
- Menghadiri kursus-kursus anjuran persatuan anda (seperti SFFLA, JOFFA & PFFA)  
(Attended courses conducted by your associations such as SFFLA, JOFFA & PFFA)  
 1-----2-----3-----4-----5  
 Tidak Pernah      Jarang      Kadang-Kadang      Selalu      Kerap  
 (Never)      (Rarely)      (Sometimes)      (Very Often)      (Always)
- Menyimpan nota-nota yang diperolehi daripada kursus  
(Keep lecture notes from courses that you have attended)  
 1-----2-----3-----4-----5  
 Tidak Pernah      Jarang      Kadang-Kadang      Selalu      Kerap  
 (Never)      (Rarely)      (Sometimes)      (Very Often)      (Always)
- Menggunakan ilmu yang di perolehi di dalam kerja harian anda  
(Applied the knowledge gained in your daily work)  
 1-----2-----3-----4-----5  
 Tidak Pernah      Jarang      Kadang-Kadang      Selalu      Kerap  
 (Never)      (Rarely)      (Sometimes)      (Very Often)      (Always)



**Bahagian 11 (Section II): Maklumat dan latar belakang (Background information)**

**1) Jawatan Anda (Designation)**

- ☐ Pengarah (Director)  
☐ Pengurus (Manager)  
☐ Eksekutif (Executive)  
☐ Lain-lain (Others)

\_\_\_\_\_ sila nyatakan (Please specify)

**3) Bangsa (Race)**

- ☐ Melayu (Malay)  
☐ Cina (Chinese)  
☐ India (Indian)  
☐ Lain-lain (Others)

\_\_\_\_\_ sila nyatakan (Please specify)

**5) Sejak bila perniagaan mendapat lesen agen?  
(Since when your business obtained agent license?)**

- ☐ < 2 tahun (year)  
☐ 2 - 5 tahun (year)  
☐ 6 - 10 tahun (year)  
☐ 11 - 15 tahun (year)  
☐ > 15 tahun (year)

**7) Anggaran kuantiti pengiklanan K1  
sebulan  
(estimated number of K1 declaration per month)**

- ☐ < 50  
☐ 50 - 150  
☐ 151 - 300  
☐ 301 - 500  
☐ > 500

**2) Jantina (Gender)**

- ☐ Laki-laki (Male)  
☐ Perempuan (Female)

**4) Kategori perniagaan (Business Category)**

- ☐ Berhad (Limited)  
☐ Sendirian Berhad (Private Limited)  
☐ Perkongsian (Partnership)  
☐ Perniagaan Tunggal (Sole Proprietorship)

**6) Jumlah pelanggan anda (Number of client)**

- ☐ < 25  
☐ 25 - 50  
☐ 51 - 75  
☐ 76 - 100  
☐ > 100

**8) Sila nyatakan pejabat kastam yang  
mengeluarkan lesen agen anda  
(Customs office where your agents' license issued)**

- ☐ Selangor  
☐ Johor  
☐ Pulau Pinang  
☐ KLIA  
☐ Lain-lain