

THE EFFECT OF TAX SIMPLIFICATION ON TAXPAYERS' COMPLIANCE BEHAVIOR: RELIGIOSITY AS MODERATING VARIABLE

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Abstract

Tax compliance was an important issue for nations around the world as governments searched for revenue to meet public needs. The importance of tax simplification had long been known as a determinant of compliance behavior and it became an important issue in taxation research. The primary objective of this study was to investigate the effect of tax simplification and religiosity on compliance behavior. This study was conducted in Malang, East Java. Survey questionnaires were sent to 200 taxpayers and only 122 responded. Consistent with the prior research, this study suggested that the effect of religiosity on compliance behavior was positive and significant. Religiosity acted as moderating role on the relationship between tax simplification and compliance behavior. This study was contributed to the compliance literature. The present study also provided practical significance because the empirical result provided information about compliance behavior to help government to develop strategies toward increasing voluntary compliance.

Keywords: *compliance behavior, religiosity, taxation, tax simplification.*

Taxation in developing countries is a challenging topic and has attracted increasing attention in the last two decades. In Indonesia the dependency on tax as a source of income is unquestioned. Taxation has been used as the main policy instrument for transferring resources to the public sector. Without the revenue from tax, the government cannot do its job. The state needs tax revenue to fund social and economic programmes, and to provide public goods and services, such

as schools, universities, hospitals, clinics and roads, as well as defence and security.

For decades, tax researchers have investigated why some people pay taxes and others do not. Through experiments, random surveys, and available tax databases, researchers have identified factors that caused compliance behavior. In recent years, research interest in the area of taxpayer compliance has grown considerably. Prior researchers have examined how individual compliance is af-

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affected by tax compliance costs (Tran-Nam, 2002), audit adjustments (Chan & Mo, 2002), moral obligation (Bobek & Hatfield, 2003), complexity (Tarjo, 2010), tax fairness (Yankelovich & White, 1984; Richardson, 2006; and Siahaan, 2012), corruption (Alon & Hageman, 2013), and demographic factors (Al-Mamun *et al.*, 2014). However little attention has been paid of the impact of tax simplification on compliance behavior. Since individual behavior is determined, in part, by the perceived simplification it is logical to expect that perception of tax simplification will have an influence on individual behavior.

A good tax system—one that facilitates and encourages compliance—needs to be understandable to those who are expected to pay. Tax simplification has the potential to increase compliance behavior for at least two reasons. First, it could cause taxpayers to comply, decreasing the possibility of errors. Second, it may decrease opportunities for tax evasion, increasing intentional compliance by taxpayers who can misuse the complex law to hide their noncompliance. Previous research focused on tax complexity rather than on tax simplification. Research focusing on perceptions of complexity indicates that complexity is associated with compliance, but there is no consistent link between complexity and compliance. Cox & Eger (2006) and Shiotsugu (2007) found that the complexity of tax system contributes to an increase in tax noncompliance. However, several surveys have reported no relation between complexity and compliance (Westat, 1980 and Yankelovich & White, 1984)

Beside tax simplification, another variable that might influence compliance behavior is religiosity. The role of religiosity has been relatively neglected in the tax compliance literature (Pope & Mohdali, 2010). Differences in religious affiliations tend to influence the way people live, the choices they make, and whom they associate with. It would seem that obtaining an in-depth understanding of the dominant religion and its effect on taxpayers'

behavior would be essential to an intimate understanding of voluntary compliance. Religiosity as pointed out by Delener's study (1994), Ger (2005), and Mokhlis (2006), could affect the behavior. Study conducted by Richardson (2008) and Palil *et al.* (2013) found that there is a relationship between religiosity and tax compliance, suggesting tax compliance is expected to be at higher levels, when individuals are at higher levels of religiosity. However, Welch *et al.* (2005) findings contradict with the previous findings. The negative perceptions on how the community handles their tax matters seem to impact community members, regardless of their level of religiosity.

There are 2 important reasons that motivate the current study. Firstly, prior research has produced inconclusive results concerning the effect of religiosity on compliance behavior. Although inconclusive, the overall literature shows that religiosity may play a vital role in helping authorities to meet their target in fostering voluntary tax compliance. Secondly, the effect of tax complexity on compliance behavior has been investigated by the previous researchers. However there is no research that incorporate the role of tax simplification and religiosity in predicting compliance behavior. To the authors' knowledge, this study is the first attempt to relate tax simplification and compliance behavior with religiosity as moderating variable. This study suggests that religiosity can strengthen and weaken the relationship between awareness and purchase decision. It is claimed in some of the literature that religion is the key cultural element that determines behavior (Babakus *et al.*, 2004 and Cornwell *et al.*, 2005).

Based on the above mentioned research motivation, this research has 2 major objectives. The first objective of this study is to investigate the effect of religiosity on compliance behavior. The second objective is to analyze whether religiosity acts as a moderating variable on the relationship between tax simplification and compliance behavior.

HYPOTHESIS DEVELOPMENT

Tax Simplification

Tax simplification is commonly understood as making the tax system simpler. Tran-Nam (2004) states that to simplify a tax legislation/system could be mean any of this: (1) to improve the tax legislation/system in the linguistic and structural sense; or (2) to make the tax legislation/system simpler in the content or conceptual sense; or (3) to lower the operating costs (in absolute or relative sense) of the tax legislation/ system

Cooper (1993) pointed out that tax simplicity contain at least one or more of the following issues: (1) predictability, in this context a rule would be simple if that rule and its scope were easily and accurately understood by taxpayers and their advisers whenever necessary; (2) proportionality, a rule would be simple if the complexity of the solution were no more than reasonably necessary to achieve the intended aim; (3) consistency, this would apply where a rule deals with similar issues in the same way and without the need to make arbitrary distinctions; (4) compliance, a rule would be simple if it were easy for taxpayers to comply without incurring excessive costs; (5) administration, a rule would be simple if it were easy for revenue authority to administer; (6) coordination, a rule would be simple if it fitted appropriately with other tax rules: it would be complicated if its relationship with other rules were obscure; and (7) expression, a rule would be simple if it were clearly expressed.

Simplification has the potential to increase compliance behavior for at least 3 broad reasons. First, it could help taxpayers to comply voluntarily with more certainty, reducing inadvertent errors by those who want to comply but are confused because of complexity. Second, it may limit opportunities for tax evasion, reducing intentional noncompliance by taxpayers who can misuse the complex code provisions to hide their noncompli-

ance or to achieve ends through tax shelters. Third, tax code complexity may erode taxpayers' willingness to comply voluntarily if they cannot understand its provisions or they see others taking advantage of complexity to intentionally under-report their taxes.

Religiosity

Religion is an important cultural factor to study because it is one of the most universal and influential social institutions that have significant influence on people's attitudes, values and behaviours at both the individual and societal levels (Mokhlis, 2009). According to Delener (1990) religiosity is the degree to which individuals are committed to a specific religious group. Religious affiliation is a discrete construct that is typically measured relative to the denominational membership or religious identification of an individual (e.g. Muslim, Christian, Jew, Hindu, and Sikh). Worthington *et al.* (2003) describes religiosity as "*the degree to which a person adheres to his or her religious values, beliefs and uses them in daily living*". Furthermore, they posit that the "*supposition is that a highly religious person will evaluate the world through religious schemas and thus will integrate his or her religion into much of his or her life*".

The conceptualization and measurement of religious construct have been key issues in the field of sociology. There are considerable empirical efforts were made to refine the conceptualization of religiosity and produce valid multidimensional measures. However, there is no consensus among experts as to the number of dimensions that make up the religiosity construct. Worthington *et al.* (2003) developed a general of measure of religiosity known as the Religious Commitment Inventory (RCI-10) which has been validated across different samples. The RCI-10 is made up of statements which express intrapersonal religiosity and intrapersonal religiosity, which measure cognitive

and behavioral dimensions of religion. RCI-10 is one of the most established and validated scales to measure religiosity (Mokhlis, 2009).

Compliance Behavior

Tax compliance is defined as the full payment of all taxes due (Braithwaite, 2009). According to Brown & Mazur (2003), tax compliance is multi-faceted measure and theoretically, it can be defined by considering 3 distinct types of compliance such as payment compliance, filing compliance, and reporting compliance. Furthermore Vadde & Gundarapu (2012) define tax compliance as taxpayers' ability and willingness to comply with tax laws which are determined by ethics, legal environment, and other situational factors at a particular time and place. Thus tax compliance can be defined as the ability and willingness of taxpayers to comply with tax laws, declare the correct income in each year and pays the right amount of taxes on time.

In explaining rental taxpayers' compliance behavior, that is, the reasons why they comply and do not comply there were broadly two classes of theories—economic based theories, which emphasize incentives, and psychology-based theories which emphasize attitude (Trivedi *et al.*, 2005). Economic based theories of tax compliance are also referred to as deterrence theory suggest that taxpayers "play the audit lottery," i.e. they make calculations of the economic consequences of different compliant alternative. Such as whether or not to evade tax, the probability of detection and consequences there of, and choose the alternative which maximizes their expected after tax return/profit (possibly after adjustment for the desired level of risk). The theories suggest that taxpayers are amoral utility maximizes hence, economic theories emphasize increased audits and penalties as a solution to compliance problems. Psychology based theories of tax compliance assume that psychologi-

cal factors—including moral and ethical concerns are also important to taxpayers and so taxpayers may comply even where the risk of audit is low. Psychology theories de-emphasize audits and penalties and instead focus on changing individual attitudes towards tax system.

Linkage between Religiosity and Compliance Behavior

Religion is one of the most important social factors that influence the life of its believers (Mukhtar & Butt, 2011). It works as an accountant that unifies, divides and amalgamates social groups (McCullough & Willoughby, 2009). Religion acts as a foundation stone on which humans build their attitudes and behavior (Essoo & Dibb, 2004). Few argue that religious beliefs are tangled with cognitive elements, providing the basis of knowledge that control and justify our attitudes and behavior (Foxall & Goldsmith, 1994). This influence also plays a dominant role in shaping individual's attitude and behavior towards material goods and services (Fam *et al.*, 2004). It has been argued that religion is highly personal in nature and therefore its effects on compliance behavior depend on taxpayers' level of religious commitment or the importance placed on religion in their life. In the taxation context, religious obligations and beliefs direct peoples' attitude and feeling towards tax obligation imposed by government.

One consequence of high levels of religiosity in society can be low rates of deviant behavior, including tax fraud (Stack & Kposowa, 2006). Findings by Stack & Kposowa (2006) reinforced the conclusion that people with no religious affiliation were more likely to view tax fraud as acceptable. It is suggested that tax compliance is expected to be at higher levels, when individuals are at higher levels of religiosity. A sample size of 47 countries by Richardson (2008) confirmed a positive relationship between individuals with high

levels of religiosity and tax compliance. These arguments lead to the following hypothesis:

H₁: the effect of religiosity on compliance behavior is positive and significant

Linkage among Tax Simplification, Religiosity, and Compliance Behavior

Simplification of the tax laws can impact on compliance in a number of different ways. It may encourage compliance by providing a lower opportunity for it. Simplification may also decrease the uncertainty of the tax laws and thereby encourage greater compliance amongst risk adverse taxpayers or, conversely, complexity can frustrate taxpayers and thereby reduce their willingness to comply. For tax law that is perceived as simple, tax professionals should be relatively more confident that they have made accurate tax reporting. On the other hand, for a tax law that is perceived as being difficult (complex), tax professionals should less confident that they have made accurate tax reporting. This is because for a tax law that is perceived as relatively simple, tax professionals expect to make a correct tax judgment.

Religiosity, which measures the level of religious adherence or commitment, serves to augment the tax simplification into compliance behavior. This means that if two taxpayers had the same perception about tax simplification, then the indi-

vidual who reported a higher level of religiosity would be expected to be more likely to have higher compliance behavior. Thus it is hypothesized that religiosity moderate the relationship between tax simplification and compliance behavior. Under high religiosity—where religiosity is perceived as religious commitment—the increase of tax simplification is likely would increase compliance behavior. In other words, it can be argued that higher religiosity and higher tax simplification will improve compliance behavior. This leads to the following hypothesis:

H₂: the higher the degree of religiosity, the higher impact of tax simplification on compliance behavior

Based on the arguments developed above, the model proposed in the present study is as Figure 1.

METHOD

Data for this study was gathered by primary data collection method through a structured questionnaire. The questionnaire contains four sections. The first section of the survey sought demographic information from the respondents such as gender, age, marital status, education level. The second section asks for respondents’ perception of the simplicity of the tax regulation based on 7 given state-

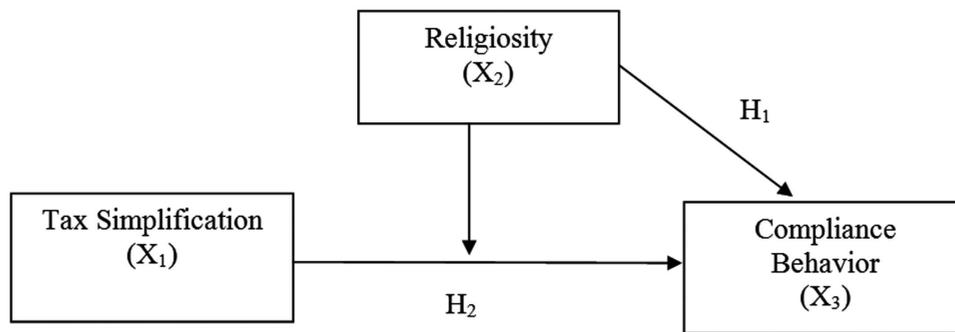


Figure 1. Model of the Present Study

ments. The third section is designed to measure religiosity which consist 10 questions. The last part of the questionnaire compliance behavior which consists of 5 statements. This study was conducted in Malang. Data for this study were collected using a questionnaire to individual taxpayers in 3 different type of industries, service, manufacturing, and merchandising. A questionnaire was administered to a sample of 200 taxpayers, 122 were returned yielding a response rate 61%. Besides, the data are not collected randomly because of the difficulty of determining population of this study.

Measurement and operationalisation of variables from this research are: (1) tax simplification, is the degree of heterogeneity and concentration among tax elements. The instrument for measuring tax simplification is modified from the questions Long & Swingen (1987). Taxpayer responded on a 5 point scale ranging from 1 (strongly disagree) to 5 (strongly agree). A high numerical response a perception of high degree of tax simplification. Cronbach alpha for this scale was good (0,611); (2) religiosity, is the degree to which a person adheres to his or her religious values, beliefs, and practices and uses them in daily living. Religiosity is measured using measurement called RCI-10 developed by Worthington (2003). The questionnaire consist 10 questions. RCI-10 is one of the most established and validated scales to measure religiosity (Mokhlis, 2009). Respondents were requested to rate their opinions according to a five point scale ranging from 1 to 5. 1 refers to not at all, 2 refers to somewhat, 3 refers to moderately, 4 refers to mostly, and 5 refers to totally. Cronbach alpha for this scale was also very good 0,820; and (3) compliance behavior, timely and fully paid return without government enforcement efforts. Five items developed by Siahaan (2012) was used to measure compliance behavior. The items covered in this study consist of the accuracy to fill the tax form, the accuracy in calculating tax liability, timeliness, and voluntary. Taxpayer re-

sponded on a 5 point scale ranging from 1 (strongly disagree) to 5 (strongly agree). A high numerical response a perception of high degree of compliance behavior. The cronbach alpha coefficient was 0,849 which indicated high internal reliability for the scale.

A simple regression analysis is used to test the hypothesis 1. To test hypothesis 2 moderated regression analysis (MRA) is used. Moderation occurs when the relationship between two variables (in this case Tax simplification and compliance behavior) depends on a third variable (religiosity). The third variable is referred to as the moderator variable. A moderated regression analysis (MRA) is used to test the model of the study as shown in the above figure. The equations are shown as follows:

$$X_3 = \beta X_2 + \varepsilon \dots\dots\dots(1)$$

$$X_3 = \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_1 \times X_2 + \varepsilon \dots\dots\dots(2)$$

Where:

- Y = Dependent variable of compliance behavior
- b_1, b_2, b_3 = regression coefficients
- X_1 and X_2 = The independent variables of tax simplification and religiosity
- $X_1 X_2$ = the interaction of X_1 and X_2
- e = error

For H_1 , the hypothesis is not rejected when p -value $< \alpha$. For H_2 , if β_3 is significant and negative ($\beta_3 < 0$), the hypotheses could not be rejected.

RESULTS

Background of Respondents

Table 1 shows demographics statistics of taxpayers indicating the frequency distribution of each characteristic under study together with its percent in the form of table.

Table 1. Demographic Profile

Characteristics	Frequency	Percentage (%)
Age		
Between 20 - 29 years	5	4.1
Between 30 - 39 years	26	21.3
Between 40 - 49 years	51	41.8
More than 50 years	40	32.8
Gender		
Male	58	47.5
Female	64	52.5
Status		
Single	3	2.5
Married	119	97.5
Highest Education Level		
Secondary high school or equivalent	9	7.4
Diploma or equivalent	95	77.9
Bachelor degree or equivalent	9	7.4
Postgraduate degree or equivalent		
Religion		
Islam	82	67.2
Protestantism	10	8.2
Catholicism	9	7.4
Hinduism	19	15.6
Buddhism	2	1.6
Company Work Place		
Service company	42	34.4
Merchandising company	16	13.1
Manufacturing company	64	52.5

Table 1 shows the most of the respondents, 51 (41.8 %) were aged between 40 to 49 years old. This is followed by 40 respondents (32.8%) were aged more than 50 years old, 26 respondents (21.3%) were aged between 30 to 39 years and 4,1% were between 20 to 29 years. In terms of gender, 58 are male (47.5%) and 64 are female (64%). In terms of status, the majority of the respondents (97.5 %) are married. On the other hand, a small proportion of respondents (2.5%) are single. Table 1 also shows that in terms of highest educational level, majority of respondents (77.9%) had

bachelor degree. There is an equal number (7.4%) of respondents who graduated from secondary school, diploma or equivalent and postgraduate degree or equivalent. Furthermore, majority of respondents (67.2%) are Muslims, Protestants 14.8% and Catholics 19 respondents (15.6%), Hindus 0.8%, and Budhists 1.6%. In terms of work place, most of respondents (52.4%) working in manufacturing company, 42 respondents (34.4%) working in service company, and 16 respondents (13.1%) working in merchandising company.

Test of Hypothesis 1

Table 2. Results of Regression of Equation 1 the Effect of Religiosity (X_1) on Compliance Behavior (X_2)

Equation (1) $X_3 = \beta X_2 + \varepsilon$				
Variable	B Value	SE	t-stat	Sig
X_1 Religiosity	0.273	0.476	5.934	0.000
R = 0.476 R ² = 0.227 F=35.207 α = 0.05				

The first hypothesis of the model requires a test of the expected positive and significant relation between religiosity and compliance behavior. To test H_1 , the effect of religiosity on compliance behavior, a linear regression model is employed, in which the independent variable is religiosity and the dependent is compliance behavior. As summarized in Table 2, it shows that religiosity has positive and significant effect on a compliance behavior [p 0,000 < 0,05]. Hence, the result support for hypothesis 1.

Test of Hypothesis 2

Table 3. Results of Regression of Equation 2 the Moderating Effect of Religiosity (X_2) on the Relationship between Tax Simplification (X_1) and Compliance Behavior (X_3)

Equation (2) $Y = b_1X_1 + b_2X_2 + b_3 X_1 X_2 + e$					
	Variable	SE	B	t-stat	Sig
X_1	Tax Simplification	0.204	1.033	4.205	0.000
X_2	Religiosity	0.139	1.272	5.247	0.000
X_1X_2	Moderating	0.05	-1.363	-3.656	0.000
R = 0.577 R ² = 0.333 F=19.645 α = 0.05					

It is expected in hypothesis 2 that the higher the level of religiosity, the stronger the effect of tax simplification on compliance behavior. The regression equation demonstrates the significant effect of the interaction between tax simplification and religiosity on compliance behavior ($p < 0.05$). The negative sign of the standardized beta coefficient ($b = -1,363$) of the interaction term between the 2 variables indicates that high tax simplification lead to higher level of compliance behavior under high tax simplification (simple tax regulation). Hence, H_2 is supported. This result shows that religiosity-religiosity commitment of taxpayers may moderate the effect of tax simplification on compliance behavior. In other words, the positive effect of tax simplification on compliance behavior may depend on the level of religiosity.

DISCUSSIONS

The main purpose of this study was to examine empirically the moderating role of religiosity in the relationship between tax simplification and compliance behavior. This research has generated two interesting findings. First, the results reveal that the effect of religiosity on compliance behavior is positive and significant. This means the higher the religious commitment the higher the compliance behavior. This study support the findings of the previous studies done by Richardson (2008) and Palil et al. (2013). The results of this study indicate that religion plays an important role in shaping individual's attitude and behavior towards tax obligation.

Second, the higher the degree of religiosity, the stronger the effect of tax simplification on compliance behavior. Religiosity is very important because it determines individual cognition and behavior. Religion is a powerful influence on human behavior and previous research has identified a variety of factors associated with religiosity that may ultimately affect behavior. Many stud-

ies focusing on the relationship between religion and behavior have confirmed that religion strongly influences an individual's emotional experience, thinking, behavior and psychological well-being (Chamberlain & Zika, 1992; McDaniel & Burnett, 1990). Furthermore, Avants et al. (2003) indicate that those who are more religious may be more likely to take risks. In another words the extent to which religion affects one's beliefs and behavior depends on the individual's level of religiosity. It is highly likely that religiosity will govern an individual's behavior, including behavior related to tax obligation. The greater the intensity of ones' religious affiliation, the higher will be the chances that he will strive to conform to his religious obligations in the context of tax obligation.

CONCLUSION AND SUGGESTION

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Suggestion

Several limitations of this study may be noted. First, as with most empirical studies, the results are generalizable to only the population from which the sample was drawn, the results cannot be generalized to other settings. Second, the study did not consider all the variables that might affect compliance behavior of taxpayers. There might be another influence compliance behavior such as trust, probability of audit detection. Third, while compliance behavior measure is well recognized in the literature. The survey instrument and conceptualization of tax simplification and religiosity are both new requiring further investigation in the organizational literature.

The findings of this study add to the limited knowledge of tax compliance research. There are still remains a significant amount of research requiring to be done in this area to replicate or extend this study. For example, it is found that being able to identify how the behavior of taxpayers is affected by their religiosity factors is critical to the success of government to collect tax from taxpayers, especially for those who operate in

multi-religious countries like Indonesia. Perhaps the major challenge for them is to understand the differences and similarities that characterize consumers' behavior across different religious. Besides this, the present study is of practical significance because the empirical result provide information about compliance behavior to help government to develop strategies toward increasing voluntary compliance. Also, the results indicate that religiosity is important antecedents of taxpayers' intention to comply. Therefore, government should design their tax campaigns focusing on creating awareness regarding tax obligation which is connected to religiosity.

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