

Determinants of Sales Tax Compliance in Small and Medium Enterprises in Jordan: A Call for Empirical Research

Ahmad Farhan Alshir'ah, Hijattulah Abdul-Jabbar and Rose Shamsiah Samsudin

Tunku Puteri Intan Safinaz School of Accountancy, Universiti Utara Malaysia

Abstract: Taxation is a major source of revenue for majority of countries. Efficient tax administration and strategies is vital to minimize loss of revenues, as such losses could lead to continuous budget deficits. Non-compliance of tax provision is a global phenomenon. The causes for tax non-compliance raise significant cases for governments and tax agencies worldwide. This paper discusses the importance of sales tax in small and medium enterprise (SME) sector in Jordan and more importantly, signaling the severity of tax gap that should be addressed by Jordanian government. The paper urges tax authority and researchers, in particular, to carry out research on sales tax determinants in Jordan, by adapting the Fischer tax compliance model, which integrates both the economics deterrence and the social-psychology theories. Empirical study of this nature is highly recommended as the outcome are expected to provide significant input to the policy makers in streamlining and strategizing so as to minimize losses of revenues to the government.

Key words: Sales tax • Tax compliance • Tax gap • Small and medium enterprises

INTRODUCTION

Taxation is one of the essential tools in managing national revenues. Majority of countries around the world develop their nation primarily from tax sources, either direct taxes or indirect taxes [1]. A country's economic growth depends on how much revenue has been collected [2, 3]. In view of that, government should have sufficient revenue to finance infrastructure, social services and to provide for adequate provision of services [4] to their citizen.

The importance of taxation returns prompts to its essential role in the social, political and economic development of countries [5]. In fact, the onset of tax collection has persistent challenges in tax compliance [6], where the compliance behaviour of taxpayers is a significant matter for governments [7]. The increase of tax revenue lies in the efforts to encourage tax compliance and thus, tax compliance is a prime concern for all tax agencies worldwide [8]. The causes for tax non-compliance raise significant cases for governments and tax agencies as it affects both the justice and effectiveness of the economy [9].

Accordingly, tax non-compliance is widely acknowledged as a universal phenomenon that prevails in all economies and societies systems in developing and developed countries [10-15].

In the context of Jordan, taxes constitute a major source of revenue in the governmental budget of Jordan, specifically since tax revenues contributed on average around 67% to 73% of total revenues during the period of 2010 to 2015 [16]. A detailed breakdown indicates that tax revenue were mainly derived from sales tax, that it contributed around 70% of total tax revenues for the same period [16]. The government of Jordan resorted to borrowing from domestic or foreign sources to cover the rest of the expenditures [17]. Thus, government of Jordan is highly dependent on tax revenue, foreign aid and borrowed finances from international creditors [18, 19].

Consequently, Jordan continuously suffers from a sharp rise in net public debt, which grew by 65.4% in 2011 and a further 84.1% in 2015 of gross domestic product (GDP). The fiscal deficits in Jordanian government budget appears aggravates with the increase of tax non-compliance from Jordanian Dinar (JD)1.6 billion in 2011 to JD2.3 billion in 2014 [16]. The problem is worsened

by the fact that the economy of Jordan has only limited economic resources and it suffers from a chronic fiscal deficits to making the provision of required funding to satisfy the economic and social development requirements [20] essential.

Therefore, it is vital that relevant study to be carried out in addressing the issue of budget deficit in relation to tax collections. Besides, improvement with regards to administration and collection of taxes, addressing low tax revenues collection due to tax gap shall be investigated. Nonetheless, McKerchar [21] argues that a better understanding of non-compliance is of greater priority rather than measuring the tax gap in broader sense. Due to the fact that sales tax contributes a significant percentage to tax revenue in Jordan, this paper serve as a proposal in urging tax authority and tax researchers to investigate the determinant (s) of sales tax non-compliance in Jordan.

Tax Non-compliance by Small and Medium Enterprises In Jordan: Tax non-compliance phenomenon constitutes one of the central problems facing government and tax authority in Jordan [19, 22, 23]. In simple terms, tax compliance means obedience to tax reporting requirements [24]. Compliance reflects that taxpayer has a trust, both on the tax law and fairness of the tax system [25]. Brown and Mazur [26] classify compliance in terms of three processes, namely reporting compliance; filing compliance; and payment compliance.

Non-compliance, conversely, denotes failure of taxpayers to meet tax reporting requirements, either intentionally or unintentionally [27]. Other terms used to describe tax non-compliance include tax evasion, tax cheating, errors and misreporting [28]. The term 'tax evasion' is often used interchangeably with non-compliance, though some technical and legal differences exists [29], particularly in terms of intention. Tax evasion involves some elements of illegal behaviour, accompanied by a real intention by taxpayer to knowingly mislead, deceive or conceal from the tax authority the intention to pay less tax illegally [14]. Many tax literature recognizes that measuring the true extent of non-compliance is not possible, but estimates from the tax gap approach are generally used to indicate the possible sources and the level of non-compliance occurrences [30].

The rise in the non-compliance of tax payment has an influence on the budget deficit in Jordan negatively [31]. This problem has led to the increase in public debt which causes an absence of tax justice between the citizens and lead to the increase in the rate of tax non-compliance

especially in the sales tax. The amount of tax non-compliance for the small enterprises represents a very high percentage of non-compliance [32].

Taxpayers in Jordan generally avoid from paying tax by several ways. There are high percentage of taxpayers being late in paying tax owed to tax authority [33]. Over the years, in spite of the increase in tax revenues, the tax non-compliance also increases where the amount of tax non-compliance increases from JD1,067.4 million in 2011 to JD1,578.2 million in 2015. It is estimated that the sales tax non-compliance represent about 71% of the total tax non-compliance during the period of between 2011 and 2015 [19, 34]. Therefore, specific studies on sales tax compliance are deemed necessary.

Regarding the SMEs, Pope and Abdul-Jabbar [35] cautioned that the small and medium enterprises (SME) around the globe are likely to be characterized by tax non-compliance. A number of researchers found that SMEs businesses, especially the owner-manager, are more likely to commit non-compliance behaviour than other groups of taxpayers [25, 36, 37].

It is widely acknowledged that SMEs play a major role in majority of the countries' economies whether in developing or developed countries [38, 39, 40] and they constitute the most dynamic companies in the transitional economies and developing countries [41]. However, taxation often posed many regulatory difficulties to SMEs internationally [35]. Thus, SMEs tend to be a focus of research by researchers from various disciplines. In taxation studies several reasons are identified for increasing number of studies on SMEs sector. Firstly, SMEs are considered as having lesser tax commitment in comparison to large companies [42]. Secondly, the SMEs sector is important for the development and economic growth in most countries [43]. Finally, the SMEs are the ones collecting a number of taxes (e.g. sales tax, value added tax) on behalf of the government or tax authority [42].

In Jordan, the number of SMEs recorded is almost 166,000 in 2014. SMEs in Jordan are defined based on number of employees, as shown in Table 1.

Table 1: SME Classification in Jordan

Type of entity	Number of employees
Micro	Less than 10
Small	10 - 49
Medium	50 - 249

Source: Ministry of Industry and Trade [44].

The number of SMEs in Jordan grew from 95% in 2011 to 99% in 2014 with a stable contribution of 50% of the GDP in the same period [45, 46]. The sector also contribute 45% of exports benefit, 60% of manpower and provide about 70% of new job opportunities [47]. Thus, similar to other developing countries, the importance of SME sector towards economic growth of Jordan is indisputable.

In terms of non-compliance, the available Jordanian data indicated that around 87% of small enterprises and 35% of medium enterprises did not comply in paying their sales tax [48]. However, factors leading to tax non-compliance behaviour of SMEs are yet to be fully ascertained. Thus, SME sectors shall be given a high priority in addressing the alarming issue of tax non-compliance, particularly with regard to the sales tax.

Proposed Research Method: A quantitative method, employing the Fischer Model [49] is recommended to study the current determinant (s) of sales tax compliance among SMEs in Jordan. The primary source of data collection will be carried out by way of a survey to randomly selected sample of SMEs.

The Fischer model is built on incorporating both social-psychological and economic theories (economical and behavioural approach). The economics theory assumes that a taxpayer is rational and thus will always maximize their expected utility of the tax non-compliance, evaluating the benefits from successful tax non-compliance against the risk or probability of detection and penalty imposition. On the other hand, the behavioural approach assumes that taxpayers do not rely on selfish utility, because interaction is normally based on different norms, beliefs and attitude. Studies that integrate the factors from both economic and social-physiological theories could reasonably address the issue of non-compliance [50].

Fischer [49] categorized the 14 key determinants derived by Jackson and Milliron [51] through their comprehensive review of tax compliance studies into four groups of variables, namely tax system (tax complexity, tax audit, tax penalty, tax rates); and attitudinal and perception (tax moral, tax fairness and peer influence); demographic (age, gender, education); non-compliance opportunity (income level, occupation, income source).

Nevertheless, a few individual factors, particularly related to demographic and non-compliance opportunity, in the Fisher Model need to be adjusted with caution to suit the SMEs business context. For example, income level will be changed to sales level. This is in line with

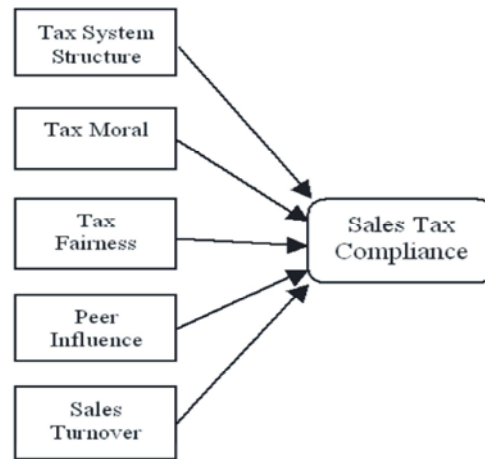


Fig. 1: Proposed framework for Sales Tax compliance Study

recommendation made by Slemrod [52] that the tax situation of both business and owners is closely related. Additionally, caution made by Woodward and Tan [53] will be given special attention too. Woodward and Tan demonstrated that the tax non-compliance opportunities for SMEs are greater than that of individuals. The proposed framework is depicted in Figure 1 below:

The key research question is what are the factors influencing sales tax compliance behaviour among SMEs in Jordan. The specific questions are as follows:

- What is the relationship between tax system structure and sales tax compliance?
- What is the relationship between tax moral and sales tax compliance?
- What is the relationship between tax fairness and sales tax compliance?
- What is the relationship between sales turnover level and sales tax compliance?
- What is the relationship between peers influence and sales tax compliance?

As for the objective of the proposed study, the main one is to determine factor (s) influencing sales tax compliance behaviour among SMEs in Jordan. The more specific objectives are as outlined below:

- To examine the relationship between tax system structure and sales tax compliance.
- To examine the relationship between tax morals and sales tax compliance.
- To examine the relationship between tax fairness and sales tax compliance.

- To examine the relationship between sales turnover level and sales tax compliance.
- To examine the relationship between peers influence and sales tax compliance.

Concluding Remarks: This study is one of the few studies which examine tax compliance in the context of business (owner-manager) by utilizing the Fischer Model [49]. The model focus on the individuals and in this study, managers and the owners of the enterprises will constitute the sample of the SMEs selected. Additionally, Fischer Model integrates both the economic and social-psychology theories. The results of this study will likely to contribute in minimizing the gap in sales tax compliance studies. Mahangila [54] and Abdixhiku [55] reported that there is a notable gap in empirical studies dedicated to sales tax compliance. Generally, the majority of the studies of this calibre, focused on income tax, whereas sales tax compliance and sales tax non-compliance were largely untouched. This is quite surprising giving the facts of the significant importance of sales tax and sales taxation in tax administration and public budget [56][57][58][59]. Hence, studies in this area is crucial for the Jordanian economy. Lastly, this study may shed some lights and provide insights on the key factor(s) that affects sales tax compliance in Jordan.

Lastly, this study may also contribute significant input to the government, tax agencies and the public economic policies by providing insights into the relationship between sales tax and compliance behaviour. It is also expected to contribute empirical evidences in the context of compliance behaviour of Jordanian taxpayers. More specifically, it provides crucial information concerning the impact of factors on the Jordanian sales tax compliance that could be used to formulate social, economic and political policies, such as information that could enable the government to be more realistic in designing strategic policy on tax compliance behaviour in Jordan.

REFERENCES

1. Palil, M.R., 2005. Does tax knowledge matters in self-assessment systems? evidence from Malaysia. *Journal of American Academy of Business, Cambridge*, 6(2): 80-84.
2. Samuel, M. and Dieu, R.J. De, 2014. The impact of taxpayers' financial statements audit on tax revenue growth. *International Journal of Business and Economic Development*, 2(2): 51-60.
3. Thananga, A.G., D.M. Wanyoike and A.J. Wagoki, 2013. Factors affecting compliance on rental income tax policy by landlords in Nakuru Municipality. *Journal of Agriculture and Environmental Sciences*, 2(1): 26-38.
4. Ndekwa, A.G., 2014. Factors for improving tax compliance among small and medium enterprises in Tanzania. *International Journal of Business and Management*, 2(10): 285-290.
5. Marandu, E.E., C. Mbekomize and A. Ifezue, 2014. Determinants of tax compliance?: a review of factors and conceptualizations. *International Journal of Economics and Finance*, 7(10): 201-218.
6. Kogler, C., S. Muehlbacher and E. Kirchler, 2013. Trust, power and tax compliance: testing the "slippery slope framework" among self-employed taxpayers. *WU International Taxation Research Paper Series*, 05: 2-18.
7. Çevik, S. and H. Yeniçeri, 2013. The relationship between social norms and tax compliance: the moderating role of the effectiveness of tax administration. *International Journal of Economic Sciences*, 2(3): 166-180.
8. Franzoni, L.A., 1999. Tax evasion and tax compliance. In B. Bouckaert and G. De Geest (Eds.), *Encyclopedia of Law and Economics*, pp: 52-94. Cheltenham, UK: Edward Elgar.
9. Devos, K., 2005. The attitudes of tertiary students on tax evasion. *eJournal of Tax Research*, 3(2): 222-273.
10. Epaphra, M., 2015. Tax rates and tax evasion: evidence from missing imports in Tanzania. *International Journal of Economics and Finance*, 7(2): 122-137.
11. Muoki, P., N. Corresponding and O.R. Peter, 2014. Analysis of factors affecting tax compliance in real estate sector?: a case of real estate owners in Nakuru town. *Kenya Research Journal of Finance and Accounting*, 5(11): 1-12.
12. Trigueros, M.P., F.P. Longinott and J.S. Vecorena, 2012. Estimating tax noncompliance in Latin America?: 2000-2010. *Tax Studies and Research Directorate Working Paper*, (3-2012).
13. Chau, G. and P. Leung, 2009. A critical review of Fischer tax compliance model: A research synthesis. *Journal of Accounting and Taxation*, 1(2): 34-40.
14. Kasipillai, J. and H. Abdul-Jabbar, 2006. Gender and ethnicity differences in tax compliance. *Asian Academy of Management Journal*, 11(2): 73-88.

15. Tanzi, V. and P. Shome, 1993. A Primer on tax evasion. *Journal of Chemical Information and Modeling*, 40(4): 807-828.
16. Ministry of Finance, Jordan, 2015. General government financial statements. General Government Bulletins for December. Retrieved from <http://www.mof.gov.jo>.
17. Alkhdour, R., 2011. Estimating the shadow economy in Jordan: causes, consequences and policy implications. (Unpublished doctoral thesis), Colorado State University.
18. Shahateet, M.I., F. Al-Habashneh and K.A. Al-Majali, 2014. Budget deficit and external debt in Jordan: causality and co-integration analysis. *International Journal of Economics and Finance*, 6(8): 268-277.
19. Jordan Economic Social Center, 2014. Tax evasion in Jordan: causes, ways. www.esc.jo.
20. Al-Zoubi, A., H. Khatatba, R.B. Salama and M. Khatataba, 2013. Methods of tax avoidance and evasion: the incapability of the Jordanian income tax law to face tax avoidance and evasion. *Journal Almanara*, 19(4): 9-36.
21. McKerchar, M., 2002. The Impact of complexity upon unintentional noncompliance for Australian personal income taxpayers. (Doctoral thesis), University of New South Wales.
22. Qblan, K.A., 2014. The impact of the accounting policies and applied procedures of the income and sales tax department on reducing tax evasion. (Unpublished master thesis), Middle East University.
23. AL-Kasasbeh, N.M., 2013. A proposed framework to improve the effectiveness of tax auditing. (Unpublished doctoral thesis), Amman University.
24. Roth, J.A., J.T. Scholz and A.D. Witte, 1989. Taxpayer compliance: An agenda for research. University of Pennsylvania, Philadelphia.
25. Kirchler, E., A. Niemirowski and A. Wearing, 2006. Shared subjective views, intent to cooperate and tax compliance: Similarities between Australian taxpayers and tax officers. *Journal of Economic Psychology*, 27(4): 502-517.
26. Brown, R.E. and M.J. Mazur, 2003. IRS's comprehensive approach to compliance measurement. *National Tax Journal*, 56(3): 689-700.
27. Kinsey, K.A., 1984. Survey data on tax compliance: A compendium and review. American Bar Association, Chicago, Taxpayer Compliance Project Working, pp: 84-2.
28. Long, S. and J. Swingen, 1991. Taxpayer Compliance: Setting New Agendas for Research, Law and Society Review, 25(3): 637-684.
29. Abdul-Jabbar, H., 2009. Income tax non-compliance of small and medium enterprises in Malaysia: Determinants and tax compliance cost. (Doctoral dissertation), Curtin University of Technology.
30. McManus, J. and N. Warren, 2006. The case for measuring tax gap, *e Journal of Tax Research*, 4(1): 61-79.
31. Al-Naimat, S.M.A., 2013. Theoretical and analytical study of tax law in Jordan according to the: income tax and sales tax and its relationship with revenues and tax evasion. *International Journal of Financial Research*, 4(3): 107-126.
32. Al-Rawabdeh, O., (2015, Jun, 1). Tax evasion leads to the increase of public debt, *Alrai Newspaper* [in Arabic]. Retrieved from <http://www.alrai.com/article/717131.html>.
33. Masadeh, A., 2015. The impact of modifications on the temporary income tax law no (28) for the year 2009 on the tax compliance for the service sector, field study on public shareholding companies in the Jordanian services sector. (Unpublished master thesis), University Jarash.
34. Jordan Independent Economic Watch, 2014. Tax burden in Jordan, reality, prospects. <http://www.identity-center.org>.
35. Pope, J. and H. Abdul-Jabbar, 2008. Small and medium-sized enterprises and tax compliance burden in Malaysia: Issues and challenges for tax administration. *Small Enterprise Research: The Journal of SEANZ*, 16(1): 47-60.
36. Kamleitner, B., C. Korunka and E. Kirchler, 2012. Tax compliance of small business owners. *International Journal of Entrepreneurial Behaviour and Research*, 18(3): 330-351.
37. Morse, S.C., S. Karlinsky and J. Bankman, 2009. Cash businesses and tax evasion. *Stanford Law and Policy Review*, 20(1): 1-67.
38. Inasius, F., 2015. Tax compliance of small and medium enterprises: evidence from Indonesia. *Accounting and Taxation*, 7(1): 67-73.
39. Atawodi, O.W. and S.A. Ojeka, 2012. Factors that affect tax compliance among small and medium enterprises (SMEs) in North Central Nigeria. *International Journal of Business and Management*, 7(12): 87-97.

40. Abrie, W. and E. Doussy, 2006. Tax compliance obstacles encountered by small and medium enterprises in South Africa. *Meditari Accountancy Research*, 14(1): 1-13.
41. Hobohm, S., 2001. Small and medium-sized enterprises in economic development: The UNIDO experience. *Journal of Economic Cooperation*, 22(1): 1-42.
42. Akinboade, O.A., 2015. Correlates of tax compliance of small and medium size businesses in Cameroon. *Managing Global Transitions*, 13(4): 389-413.
43. Maseko, N., 2014. The impact of personal tax knowledge and compliance costs on tax compliance behaviour of SMEs in Zimbabwe. *Elite Research Journal of Accounting and Business Management*, 2(3): 26-37.
44. Ministry of Industry and Trade, Jordan, 2016. The reality of the industry in Jordan. Retrieved from <http://www.mit.gov.jo>.
45. Saymeh, A.F. and S.A. Sabha, 2014. Assessment of small enterprise financing, case of Jordan. *Global Journal of Management and Business Research*, 14(2): 6-18.
46. Alzyadat, M.A., 2011. The role of small business investments in limiting the impact of the global financial crises on Jordan economy. *Canadian Social Science*, 7(6): 22-29.
47. Alrousan, M.K. and E. Jones, 2016. A conceptual model of factors affecting e-commerce adoption by SME owner/ managers in Jordan. *International Journal of Business Information Systems*, 21(3): 269-308.
48. Young Entrepreneurs Association, Jordan, 2011. Small and Medium Business Agenda [in Arabic]. Retrieved from <http://www.cipe-Arabia.org/>
49. Fischer, C., 1993. Detection probability and taxpayer compliance: A conceptual and empirical examination. (Unpublished doctoral thesis), Pennsylvania State University.
50. Al-Ttaffi, L.H.A. and H. Abdul-Jabbar, 2015. Does Muslim view on tax influence compliance behavior? International Conference on Accounting Studies (ICAS) 2015 17-20 August 2015, Johor Baharu, Johor, Malaysia.
51. Jackson, B.R. and V.C. Milliron, 1986. Tax compliance research: finding, problem and prospects. *Journal of Accounting Literature*, 5: 125-165.
52. Slemrod, J., 2004. Small Business and the Tax System', in H.J. Aaron and J. Slemrod (eds), *The Crisis in Tax Administration*, Brookings Institution Press, Washington, D.C, pp: 69-123.
53. Woodward, L. and L.M. Tan, 2015. Small business owners' attitudes toward GST compliance: A preliminary study. *Australian Tax Forum*, 30(3): 517-549.
54. Mahangila, D.N., 2014. SME's corporate income tax compliance in Tanzania. (Unpublished doctoral thesis), University of Southampton.
55. Abdixhiku, L., 2013. Determinants of business tax evasion in transition economies. (Unpublished doctoral thesis), Staffordshire University.
56. Torgler, B., 2011. Tax morale and compliance review of evidence and case studies for Europe. World Bank Policy Research Working Paper Series 5922.
57. Yusof, M.S.M., A.R. Romle, K.A.M. Kamal, N.A. Yusof, S. Othaman and S.S. Azidin, 2015. Public budgeting: Good practices budgeting in oil and gas industry, *International Journal of Administration and Governance*, 1(14): 125-129.
58. Hama, B., A.R. Romle and N. Ezzat, 2015. Toward a unifying framework for budgetary control and accountability in the public sector, *International Journal of Administration and Governance*, 1(4): 31-38.
59. Kamal, M.K.A.M., A.R. Romle and M.S. Yusof, 2015. Good governance and organization performance in public sector: A proposed framework. *International Journal of Administration and Governance*, 1(4): 63-68.