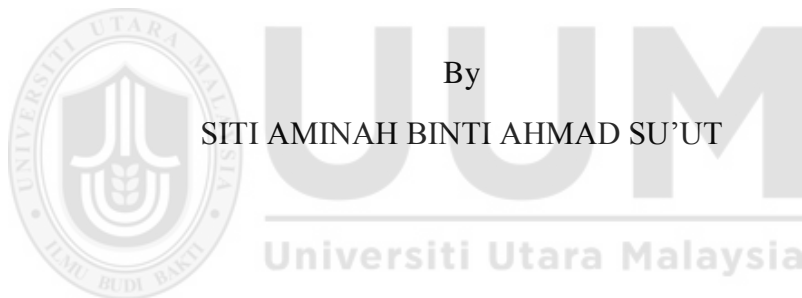


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**TAX AUDIT ADJUSTMENTS AND SMALL AND MEDIUM-SIZED  
CORPORATIONS (SMCs) CHARACTERISTICS**



Research Paper Submitted to  
Othman Yeop Abdullah Graduate School of Business,  
Universiti Utara Malaysia,  
in Partial Fulfilment of the Requirement for the  
Master of Science (International Accounting)



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## ABSTRACT

The tax system persists as the primary sources of financing Federal Government developments plans. Malaysia is a country that lagely relies on taxes. Direct taxes administered by Inland Revenue Board of Malaysia (IRBM) accounted for more than two-thirds of the Federal Government revenue in 2015 and income taxes collected from corporate sector was 38% of the federal revenue. This represents the importance of corporate tax collection in generating revenue for the nation. While the annual income tax collection of IRBM shows a positive increment each year, tax non-compliance issues are still ongoing and intensified, evidenced by an increase in the number of cases audited by tax settlement with audit adjustments and penalties. This study was performed to determine whether there was a significant difference in the motivation to conduct tax non-compliance among Malaysian Small and Medium-sized Corporations (SMCs), based on type of industry, size of company, location, and financial liquidity. The study employ quantitative research approach to analyse secondary data of field tax audit cases completed in 2015, obtained from IRBM. The research findings indicate that the type of industry, size of company, location of company and financial liquidity have influenced the probability of SMCs engaging in tax non-compliance behaviour and significant differences exist between them. SMCs engaging in services, construction and manufacturing industries has a high probability of tax non-compliance. Similar with SMCs with total assets exceeding RM10 million and SMCs located in Kelantan/Terengganu, FT Kuala Lumpur/FT Putrajaya and Selangor. SMCs with low liquidity ratio found to be less tax compliant. Therefore, research findings are expected to contribute to the body of literatures and to aid government, tax administrators, and tax practitioners especially on issues relating to SMCs tax compliance behaviour in ensuring the level of voluntary tax compliance is improved.

**Keywords:** small and medium-sized corporations (SMCs), tax non-compliance, tax audit data, financial liquidity

## ABSTRAK

Sistem percukaian merupakan sumber utama pembiayaan kepada rancangan pembangunan Kerajaan Persekutuan. Malaysia adalah sebuah negara yang bergantung kepada hasil kutipan cukai. Cukai langsung yang ditadbir oleh Lembaga Hasil Dalam Negeri Malaysia (LHDNM) menyumbang lebih daripada dua pertiga daripada hasil Kerajaan Persekutuan pada tahun 2015 dan cukai pendapatan yang dikutip dari sektor korporat adalah 38% daripada pendapatan persekutuan. Ini menggambarkan bahawa kepentingan kutipan cukai korporat dalam menjana pendapatan negara. Walaupun kutipan cukai pendapatan tahunan LHDNM menunjukkan peningkatan positif setiap tahun, isu-isu ketidakpatuhan cukai masih berlaku dan telah meningkat. Ini dibuktikan oleh peningkatan jumlah kes audit cukai yang diselesaikan dengan pelarasan audit dan penalti. Kajian ini dilakukan untuk menentukan sama ada terdapat perbezaan yang signifikan dalam penentu-penentu ketidakpatuhan cukai di kalangan Syarikat Kecil dan Sederhana (SKS) di Malaysia, berdasarkan jenis industri, saiz syarikat, lokasi, dan kecairan kewangan. Kajian ini menggunakan pendekatan penyelidikan kuantitatif untuk menganalisa data sekunder kes audit luar yang diselesaikan pada tahun 2015 yang diperolehi daripada LHDNM. Penemuan penyelidikan menunjukkan bahawa jenis industri, saiz syarikat, lokasi syarikat dan kecairan kewangan mempengaruhi kebarangkalian perilaku ketidakpatuhan cukai di kalangan SKS dan perbezaan signifikan wujud di antara mereka. SKS dalam industri perkhidmatan, pembinaan dan pengilangan mempunyai kebarangkalian tinggi ketidakpatuhan cukainya. Begitu juga dengan SKS yang mempunyai jumlah aset melebihi RM10 juta dan SKS yang bertempat di Kelantan, WP Kuala Lumpur/WP Putrajaya dan Selangor. SKS dengan nisbah kecairan yang rendah juga didapati kurang mematuhi cukai. Oleh itu, penemuan penyelidikan diharap dapat menyumbang kepada pertambahan literatur dan dapat membantu kerajaan, pentadbir cukai, dan pengamal cukai terutamanya mengenai isu-isu kelakuan pematuhan cukai SKS dalam memastikan tahap pematuhan cukai sukarela dipertingkatkan.

**Kata kunci:** syarikat kecil dan sederhana, ketidakpatuhan cukai, data audit cukai, kecairan kewangan

## ACKNOWLEDGEMENT

Alhamdulillah, first and foremost, the highest gratitude to Allah for His gift of Grace, with His will, I finally managed to complete this research paper. Deepest appreciation to my beloved husband Hasnul Hadi Mohd Amin, my children Ahmad Amin, Ahmad Iman and Alisha Husna for all their patience, support and sacrifice throughout my journey to complete this research paper as well as MSc. International Accounting. Also, many thanks to my other family members whom always given me encouragement throughout the completion of this research paper.

I would also like to express my sincere appreciation and deepest gratitude to my supervisor Prof. Dr. Nor Aziah Abd Manaf and the rest of the academic team for their assistance and guidance throughout the completion of this research paper. I humbly thank them for all the kindness and patience shown towards me. May Allah s.w.t. reward them for all their efforts.

Thank you to all colleagues, friends and all those involved directly or indirectly in the making and completing this research paper, for the undeniable encouragement and assistance. Last but not least, my upmost gratitude to the management of Inland Revenue Board of Malaysia for giving me the opportunity to undertake MSc. International Accounting and for providing necessary aid and facilities in assisting me to complete this research paper. Thank you so much.

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## LIST OF ABBREVIATIONS

ANOVA	Analysis of Variance
ATO	Australian Taxation Office
CMS	Case Management System
DGIR	Director General of Inland Revenue
GDP	Gross Domestic Product
GST	Goods and Services Tax
IRBM	Inland Revenue Board of Malaysia
ITA	Income Tax Act
ITRF	Income Tax Return Form
MDTD	Monitoring Deliberate Tax Defaulters
OECD	Organization for Economic Co-operation and Development
RMCD	Royal Malaysian Customs Department
SAS	Self-Assessment System
SGATAR	Study Group on Asian Tax Administration and Research
SMCs	Small and Medium-sized Corporations
SMEs	Small and Medium-sized Enterprises
SPSS	Statistical Package of the Social Science
TCMP	Tax Compliance Measurement Program

# CHAPTER 1

## INTRODUCTION

### 1.1 Background of the Study

It is sensible to declare that at present-day, the tax system persists as the primary sources of financing for extensive agendas of Federal Government developments that encompassed both economic and social plans. Tax revenues collection is crucial for a government to ensure its funding (Hartner, Rechberger, Kirchler & Schabmann, 2008). Thus, the government revenue generated from taxes is very much vital not only as Federal Government's revenue but also as resources for the constant growth of the nation. In addition, it is claimed that tax collection enables the Federal Government to finance all the nation's public expenses, while reducing and balancing the tax gap between those who are high income earners and low income earners (Lymer & Oats, 2009).

In Malaysia, taxes can be classified into two categories of taxes; direct and indirect taxes. Inland Revenue Board of Malaysia (IRBM) and Royal Malaysian Customs Department (RMCD) are two primary bodies that administer tax system and custom regime. They are responsible for collecting tax revenue on behalf of the government (Yunus, Ramli & Hassan, 2017). Direct taxes are administered by IRBM that includes corporate tax, individual tax, petroleum tax, real property gains tax, withholding tax and stamp duty. On the other hand, RMCD is responsible to collect indirect taxes such as good and service tax (GST), excise duty, import duty and export duty.



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## APPENDICES

### Regression Output

#### Model Summary<sup>b</sup>

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.281 <sup>a</sup>	.079	.072	.72566	1.761

a. Predictors: (Constant), USUB\_2, SIZE4, LIQ2, SIZE10, STATE4, STATE2, SIZE9, STATE3, SIZE6, LIQ4, STATE7, SIZE5, STATE5, STATE6, INDTYPE5, INDTYPE2, STATE10, SIZE3, SIZE8, INDTYPE4, STATE11, LIQ3, STATE9, SIZE7, INDTYPE3, SIZE2, STATE8

b. Dependent Variable: Log\_ADJ

#### ANOVA<sup>a</sup>

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	168.143	27	6.228	11.826	.000 <sup>b</sup>
	Residual	1958.876	3720	.527		
	Total	2127.019	3747			

a. Dependent Variable: Log\_ADJ

b. Predictors: (Constant), USUB\_2, SIZE4, LIQ2, SIZE10, STATE4, STATE2, SIZE9, STATE3, SIZE6, LIQ4, STATE7, SIZE5, STATE5, STATE6, INDTYPE5, INDTYPE2, STATE10, SIZE3, SIZE8, INDTYPE4, STATE11, LIQ3, STATE9, SIZE7, INDTYPE3, SIZE2, STATE8

#### Coefficients<sup>a</sup>

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	4.080	.060		67.991	.000	
	INDTYPE2	.281	.033	.162	8.557	.000	.695
	INDTYPE3	.102	.034	.058	2.994	.003	.654
	INDTYPE4	.249	.040	.113	6.206	.000	.744
	INDTYPE5	.335	.099	.056	3.393	.001	.912
	STATE2	.106	.073	.028	1.448	.148	.661
	STATE3	.097	.061	.035	1.606	.108	.514
	STATE4	.422	.090	.085	4.700	.000	.751
	STATE5	.264	.080	.061	3.321	.001	.739
	STATE6	.156	.057	.062	2.734	.006	.478
	STATE7	.091	.100	.016	.909	.363	.817
	STATE8	.327	.050	.200	6.489	.000	.261
	STATE9	.402	.051	.214	7.882	.000	.335
	STATE10	.138	.069	.040	2.010	.045	.639
	STATE11	.159	.066	.050	2.413	.016	.575
	SIZE2	.075	.043	.038	1.747	.081	.524

SIZE3	.140	.047	.062	2.997	.003	.580	1.723
SIZE4	.155	.050	.062	3.094	.002	.624	1.603
SIZE5	.241	.054	.085	4.450	.000	.673	1.485
SIZE6	.227	.061	.068	3.698	.000	.739	1.353
SIZE7	.355	.046	.163	7.651	.000	.545	1.835
SIZE8	.417	.049	.175	8.426	.000	.574	1.742
SIZE9	.542	.058	.183	9.288	.000	.637	1.569
SIZE10	.502	.199	.041	2.520	.012	.951	1.051
LIQ2	-.097	.027	-.064	-3.631	.000	.799	1.252
LIQ3	-.129	.036	-.063	-3.617	.000	.816	1.226
LIQ4	-.007	.082	-.001	-.079	.937	.952	1.050
USUB_2	.171	.047	.068	3.668	.000	.719	1.391

a. Dependent Variable: Log\_ADJ



**Collinearity Diagnostics<sup>a</sup>**

M	Dim	Eigenv	Condit	Variance Proportions												
				(Constant)	INDTYP E2	INDTYP E3	INDTYP E4	INDTYP E5	STATE2	STATE3	STATE4	STATE5	STATE6	STATE7	STATE8	
1	1	4.310	1.000	.00	.01	.01	.01	.00	.00	.00	.00	.00	.00	.00	.00	.00
	2	1.534	1.676	.00	.03	.00	.01	.06	.00	.02	.00	.01	.00	.00	.00	.01
	3	1.417	1.744	.00	.06	.08	.00	.00	.00	.00	.00	.00	.03	.01	.01	.01
	4	1.330	1.800	.00	.00	.02	.15	.05	.01	.04	.00	.00	.00	.00	.00	.01
	5	1.146	1.939	.00	.00	.00	.01	.06	.00	.01	.02	.03	.02	.02	.02	.00
	6	1.126	1.957	.00	.00	.00	.00	.02	.03	.02	.00	.00	.01	.23	.00	.00
	7	1.087	1.991	.00	.00	.00	.00	.03	.12	.01	.01	.11	.00	.01	.01	.00
	8	1.059	2.017	.00	.01	.00	.01	.02	.00	.05	.04	.01	.06	.03	.03	.00
	9	1.039	2.036	.00	.00	.00	.00	.00	.00	.01	.34	.05	.00	.00	.00	.00
	10	1.036	2.039	.00	.00	.00	.00	.00	.00	.00	.01	.01	.01	.00	.00	.00
	11	1.036	2.040	.00	.00	.00	.00	.00	.01	.02	.00	.00	.01	.02	.00	.00
	12	1.022	2.054	.00	.00	.00	.00	.00	.11	.00	.00	.07	.00	.09	.00	.00
	13	.991	2.085	.00	.00	.00	.00	.01	.09	.00	.05	.05	.02	.02	.02	.00
	14	.970	2.108	.00	.00	.00	.00	.01	.00	.00	.00	.07	.02	.02	.02	.01
	15	.967	2.112	.00	.00	.00	.00	.00	.06	.01	.03	.06	.02	.01	.01	.01
	16	.959	2.120	.00	.00	.00	.01	.04	.04	.00	.00	.07	.02	.00	.00	.00
	17	.950	2.130	.00	.00	.00	.00	.00	.00	.01	.01	.03	.02	.02	.02	.00
	18	.900	2.189	.00	.00	.00	.00	.00	.02	.04	.14	.02	.00	.02	.02	.00
	19	.884	2.208	.00	.00	.00	.00	.15	.11	.01	.02	.02	.02	.02	.02	.02
	20	.868	2.228	.00	.01	.01	.00	.13	.00	.00	.00	.01	.01	.23	.00	.00
	21	.816	2.299	.00	.00	.03	.01	.30	.00	.01	.02	.01	.09	.01	.01	.01
	22	.677	2.524	.00	.25	.06	.02	.01	.01	.07	.00	.01	.01	.01	.00	.03



23	.666	2.544	.00	.01	.05	.32	.01	.00	.10	.02	.00	.02	.02	.00
24	.481	2.992	.00	.02	.08	.00	.01	.00	.02	.00	.06	.01	.04	.00
25	.347	3.522	.00	.17	.14	.16	.01	.00	.00	.01	.01	.00	.00	.00
26	.241	4.226	.01	.31	.40	.25	.07	.00	.05	.01	.01	.03	.00	.02
27	.112	6.213	.01	.07	.00	.01	.00	.13	.16	.08	.09	.14	.06	.21
28	.027	12.561	.98	.04	.09	.01	.00	.26	.33	.19	.18	.42	.12	.63

Collinearity Diagnostics<sup>a</sup>

Model	Dimension	Variance Proportions															
		STATE9	STATE10	STATE11	SIZE2	SIZE3	SIZE4	SIZE5	SIZE6	SIZE7	SIZE8	SIZE9	SIZE10	LIQ2	LIQ3	LIQ4	USUB_2
1	1	.00	.00	.00	.00	.00	.00	.00	.00	.00	.00	.00	.00	.01	.01	.00	.00
	2	.01	.03	.03	.01	.01	.00	.00	.00	.01	.01	.02	.00	.00	.00	.00	.11
	3	.01	.00	.04	.01	.00	.00	.00	.00	.00	.01	.02	.00	.00	.00	.02	.02
	4	.03	.01	.02	.00	.00	.00	.00	.01	.01	.00	.01	.00	.01	.01	.00	.01
	5	.00	.04	.01	.00	.00	.01	.03	.01	.01	.00	.07	.01	.04	.09	.04	.02
	6	.00	.00	.00	.00	.00	.01	.00	.00	.00	.01	.00	.32	.00	.01	.00	.00
	7	.00	.01	.01	.00	.06	.00	.02	.05	.02	.04	.01	.02	.00	.00	.07	.01
	8	.02	.04	.00	.00	.03	.00	.01	.03	.01	.02	.01	.04	.00	.04	.08	.00
	9	.00	.00	.00	.01	.00	.00	.04	.03	.03	.01	.00	.02	.00	.04	.05	.00
	10	.00	.13	.05	.01	.02	.00	.08	.21	.00	.02	.02	.01	.00	.01	.02	.00
	11	.01	.00	.00	.02	.04	.22	.02	.03	.00	.00	.01	.01	.01	.05	.11	.00
	12	.00	.01	.00	.08	.04	.06	.04	.00	.03	.01	.01	.01	.00	.01	.01	.00
	13	.00	.03	.00	.00	.02	.00	.06	.01	.12	.02	.05	.00	.00	.01	.00	.00
	14	.00	.00	.06	.01	.03	.02	.10	.02	.00	.05	.12	.00	.00	.00	.09	.00

15	.01	.00	.01	.09	.02	.09	.00	.03	.04	.00	.02	.00	.00	.01	.01	.00
16	.00	.08	.03	.00	.01	.00	.08	.01	.01	.16	.02	.00	.00	.00	.00	.00
17	.00	.06	.02	.02	.06	.04	.02	.04	.01	.01	.00	.08	.00	.04	.25	.00
18	.00	.01	.04	.00	.00	.02	.05	.13	.00	.01	.02	.02	.03	.12	.00	.00
19	.00	.02	.00	.02	.01	.00	.00	.02	.03	.03	.00	.20	.01	.00	.01	.01
20	.00	.03	.05	.02	.03	.02	.00	.00	.03	.00	.00	.18	.00	.00	.07	.01
21	.00	.00	.00	.03	.06	.00	.01	.01	.02	.01	.07	.00	.01	.02	.04	.00
22	.01	.01	.00	.02	.00	.00	.00	.01	.00	.00	.05	.01	.02	.03	.01	.05
23	.07	.02	.02	.00	.00	.01	.00	.00	.00	.01	.01	.01	.00	.03	.01	.05
24	.04	.10	.19	.01	.00	.00	.00	.00	.00	.00	.02	.01	.00	.00	.00	.57
25	.00	.02	.00	.00	.00	.00	.00	.00	.00	.00	.00	.00	.57	.38	.07	.01
26	.04	.00	.05	.04	.03	.03	.03	.03	.07	.05	.09	.02	.25	.08	.01	.03
27	.19	.10	.13	.45	.40	.36	.29	.24	.37	.33	.20	.01	.00	.00	.00	.01
28	.53	.26	.25	.14	.12	.11	.10	.07	.16	.16	.15	.01	.02	.01	.01	.08

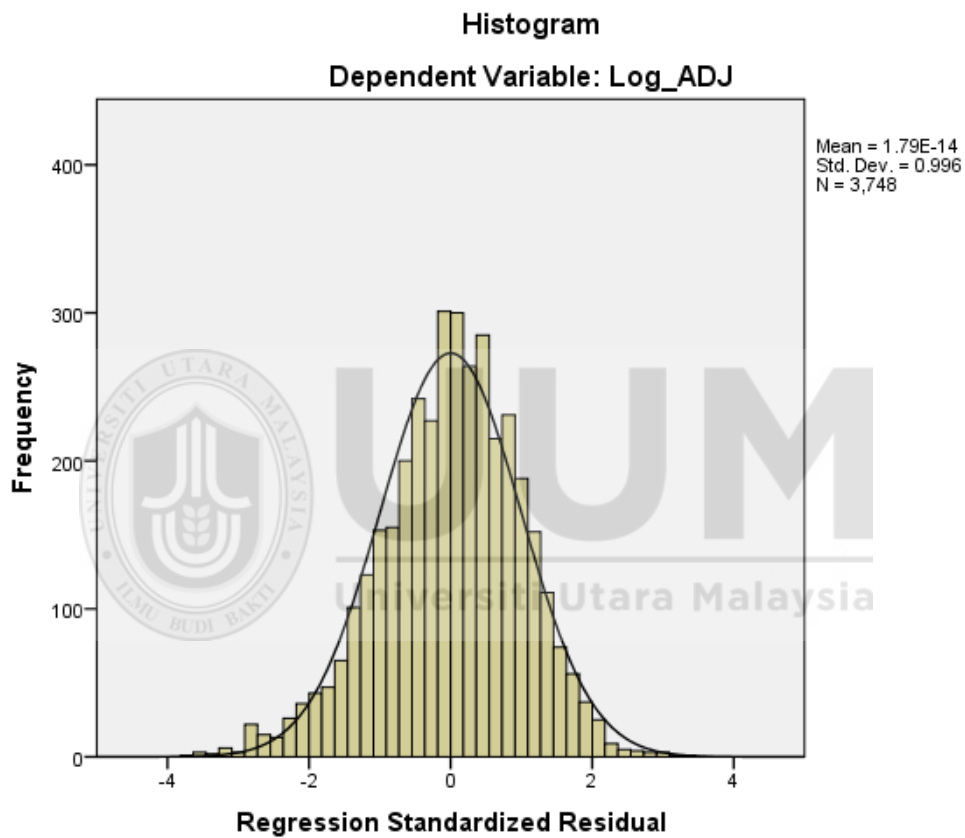
Universiti Utara Malaysia

### Residuals Statistics<sup>a</sup>

	Minimum	Maximum	Mean	Std. Deviation	N
Predicted Value	3.9826	5.3596	4.6271	.21184	3748
Residual	-2.76115	2.42208	.00000	.72304	3748
Std. Predicted Value	-3.042	3.458	.000	1.000	3748
Std. Residual	-3.805	3.338	.000	.996	3748

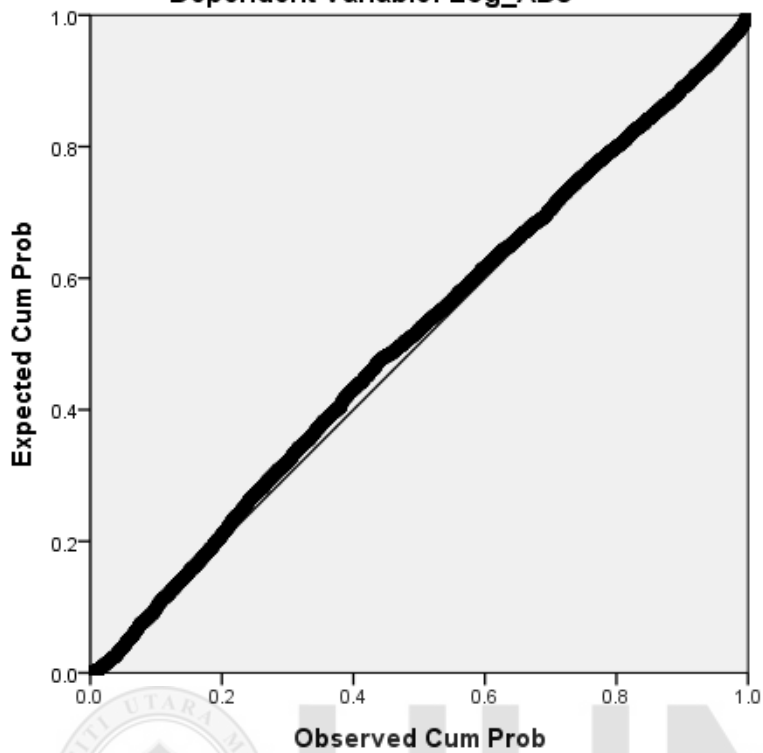
a. Dependent Variable: Log\_ADJ

### Charts



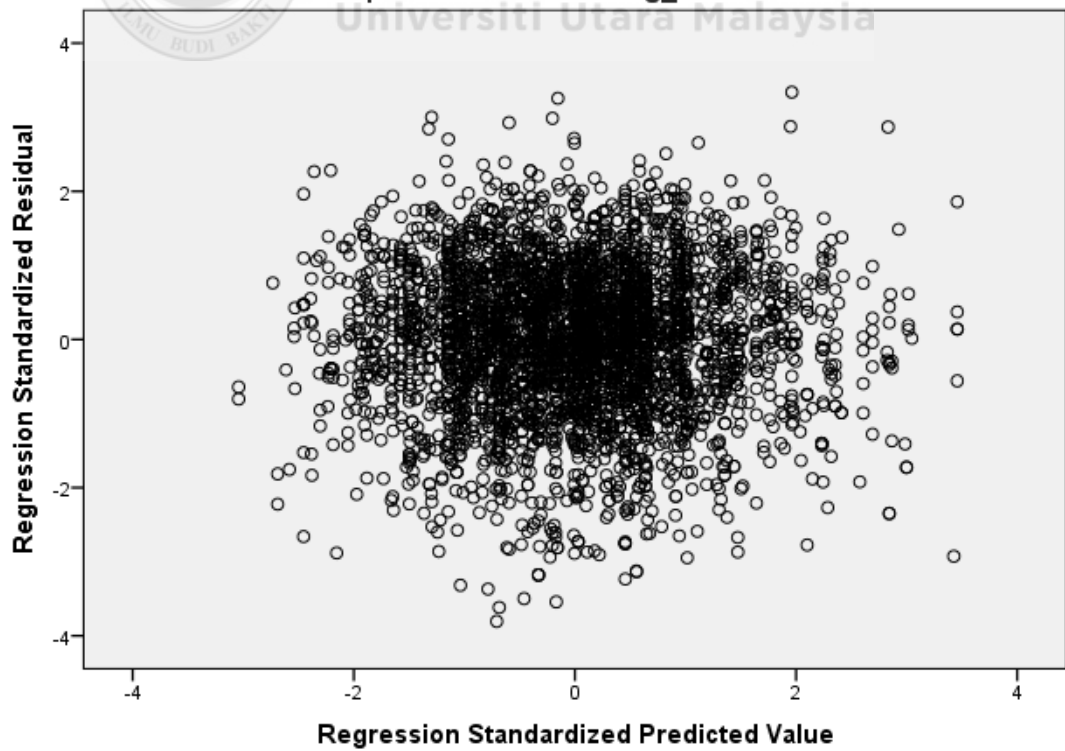
Normal P-P Plot of Regression Standardized Residual

Dependent Variable: Log\_ADJ



Scatterplot

Dependent Variable: Log\_ADJ



## Frequencies

### Statistics

	INDTYPE	LOC1 = STATE	LOC2 = U/SU	com_size _turnover	TOTAL_ ASSET	LIQ
N Valid	3748	3748	3748	3748	3748	3748
Missing	0	0	0	0	0	0

## Frequency Table

### INDTYPE

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1	1307	34.9	34.9	34.9
2	942	25.1	25.1	60.0
3	928	24.8	24.8	84.8
4	511	13.6	13.6	98.4
5	60	1.6	1.6	100.0
Total	3748	100.0	100.0	

### LOC1 = STATE

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1	337	9.0	9.0	9.0
2	154	4.1	4.1	13.1
3	304	8.1	8.1	21.2
4	89	2.4	2.4	23.6
5	116	3.1	3.1	26.7
6	374	10.0	10.0	36.7
7	66	1.8	1.8	38.4
8	1142	30.5	30.5	68.9
9	756	20.2	20.2	89.1
10	184	4.9	4.9	94.0
11	226	6.0	6.0	100.0
Total	3748	100.0	100.0	

### LOC2 = U/SU

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 0	375	10.0	10.0	10.0
1	3373	90.0	90.0	100.0
Total	3748	100.0	100.0	

**com\_size\_turnover**

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid small	84	2.2	2.2	2.2
medium	2258	60.2	60.2	62.5
large	1406	37.5	37.5	100.0
Total	3748	100.0	100.0	

**TOTAL\_ASSET**

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Less than RM500,000	520	13.9	13.9	13.9
Between RM500,001- RM1,000,000	667	17.8	17.8	31.7
Between RM1,000,001- RM1,500,000	479	12.8	12.8	44.5
Between RM1,500,001- RM2,000,000	375	10.0	10.0	54.5
Between RM2,000,001- RM2,500,000	288	7.7	7.7	62.1
Between RM2,500,001- RM3,000,000	200	5.3	5.3	67.5
Between RM3,000,001- RM5,000,000	521	13.9	13.9	81.4
Between RM5,000,001- RM10,000,000	423	11.3	11.3	92.7
Between RM10,000,001- RM50,000,000	261	7.0	7.0	99.6
Above RM50,000,001	14	.4	.4	100.0
Total	3748	100.0	100.0	

**LIQ**

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1	1443	38.5	38.5	38.5
2	1616	43.1	43.1	81.6
3	605	16.1	16.1	97.8
4	84	2.2	2.2	100.0
Total	3748	100.0	100.0	