Perception on justice, trust and tax compliance behavior in Malaysia

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ABSTRACT

The relationship between justice and trust with tax compliance behavior in Malaysia was studied. Previous studies have acknowledged the perception that justice does have an impact on tax compliance. This study distinguishes justice into procedural justice, distributive justice, and retributive justice. Therefore, this study examined the effect of these three types of justice on tax compliance. Trust also influences the act of tax compliance and it also has a relationship to the element of justice. Perceptions from individual taxpayers were gathered using questionnaires from previous studies. The findings suggest only procedural justice and trust affect tax compliance and procedural justice was positively and significantly correlated to trust. However, trust does not mediate the relationship between justice and compliance. This research will contribute to the tax literature with widened scope on justice in Malaysia.

Introduction

The Malaysian tax system is currently practicing a Self-Assessment System (SAS) which empowers taxpayers to assess, determine, and pay their tax liability in accordance with tax legislation. This system encourages taxpayers to be more transparent and responsible in their tax computation. Nevertheless, some taxpayers may try to manipulate their financial matters to reduce their requirement to pay tax or even to make it zero (Murphy, 2004).

Considering the possibility, the Inland Revenue Board of Malaysia (IRBM), as the Malaysian tax authority, take efforts to cope with the non-compliance issue. As an example, civil and criminal tax investigation in high profile cases has been conducted to increase tax compliance. In 2013, 588 cases with tax penalties of MYR 485.6 million for civil tax investigation were completed (Inland Revenue Board of Malaysia, 2013). In the same year, 29 reports based on criminal tax investigations were completed involving MYR 24.8 million (Inland Revenue Board of Malaysia, 2013). In 2014, 618 cases of civil and criminal investigation were settled (Inland Revenue Board of Malaysia, 2014). Other than that, under Section 104 of the Malaysian Income Tax Act 1967, taxpayers who fail to pay their tax liability will be prevented from leaving the country. Consequently, 25,811 income taxpayers were barred in 2014, with tax arrears amounting to MYR 494.94 million.

The statistics indirectly reveal evidence of non-compliance by taxpayers in Malaysia even when strict actions have been taken by the Malaysian authorities. Non-compliance may happen due to their perception of justice

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that influences their action (Saad, 2009). This is more so in a situation where the taxpayers think that individuals with the same economic standing or income must be taxed at the same rate (Gravelle & Gravelle, 2006). In other words, taxpayer with the same income, wealth, and liability must be taxed at the same rate.

Justice is also one of the four characteristics of a tax system, as discussed by Adam in 1965 (as cited in Lymer & Oats, 2009). The principle of justice emphasizes that individuals must be taxed according to their ability and has been explained in terms of horizontal and vertical justice. In horizontal justice, individuals with the same income must be taxed at the same rate or be subject to the same tax liability. Vertical justice distinguishes individuals from different income positions (Barjoyai, 1987).

Thus, perception of justice in the tax system is seen to influence the level of compliance among taxpayers. A few studies have found that taxpayers are more inclined to comply when a country's tax system is perceived to be fair and just (Alm, Cronshaw, & Mckee, 1993; Azmi & Perumal, 2008; Gilligan & Richardson, 2005; Richardson, 2005).

The current study is different from previous studies on the subject of justice. First, previous studies adapted various dimensions and used factor analysis to measure the perception of justice in terms of vertical justice, horizontal justice, justice exchange, and administrative justice, among others. According to Wenzel (2002a), findings derived from factor analysis depend on the suitability of the measure to the analysis where a dimensional concept could not be determined in empirical research. He introduced a justice framework as a guideline for systematic measurement in studying the role of justice on the behavior and action of taxpayers. Wenzel (2002a) classified justice into procedural justice, distributive justice, and retributive justice which are commonly used in social psychology. Therefore, this study will examine the relationship between these three types of justice with tax compliance. Several studies found that there is a relationship between the three types and tax compliance.

Second, this study also differs from previous studies on justice conducted in Malaysia such as by Azmi and Perumal (2008), and Saad (2009, 2012). Azmi and Perumal (2008) used justice dimensions developed by Gerbing (1988) and the results showed that a perception of justice exists in Malaysia. However, the study did not unearth the impact of the perception of justice with regard to tax compliance. On the other hand, Saad (2009, 2012) studied the role of the perception of justice on tax compliance as well as the impact of tax knowledge and tax complexity on justice. Saad (2009) found that taxpayers perceive the current tax system in Malaysia as fair; however, there is no evidence showing that this perception influences tax compliance behavior. The same finding was also reported by Saad (2012) for the perception of justice on taxpayers in Malaysia and New Zealand. Taxpayers in Malaysia were found to be significantly more positive regarding the tax system in Malaysia compared to taxpayers in New Zealand. However, taxpayers in New Zealand were more compliant compared to Malaysian taxpayers.

Third, this study will also examine the relationship of the three types of justice with trust on tax authority and its relationship to tax compliance because trust is also an indicator to assess the authority's level of procedural justice (Konovsky & Pugh, 1994). Trust has been found to be able to influence tax compliance. For example, studies done by Wahl, Kastlunger, and Kirchler (2010) and Kastlunger, Lozza, Kirchler, and Schabmann (2013) found high trust regarding the tax authority could increase tax compliance. Kirchler (2007) classified trust as a factor which has a positive and significant relationship with increased tax compliance. In addition, the current study determines the relationship between distributive justice and retributive justice and trust which has not yet explored. This study will examine the impact of these factors (justice and trust) on tax compliance.

Currently, no thorough study has been reported to identify the relationship between the perception of procedural justice, distributive justice, and retributive justice with regard to tax compliance in Malaysia. Therefore, this study is an effort to fill the gap. The main objective is to determine the relation between the perception of justice in terms of procedural justice, distributive justice, and retributive justice as well as trust with tax compliance behavior in Malaysia. Furthermore, this study will examine the relation between the three types of justice with trust.

Previous Studies and Hypothesis Development

Relationship Between Justice and Tax Compliance

According to Murphy and Tyler (2008), if taxpayers are treated nicely and fairly by the tax authority, they will cooperate and be more inclined to comply with the decisions made by the tax authority. Wenzel (2002b) found procedural justice could predict the compliance level of taxpayers in Australia. From his study, taxpayers are more compliant when they believe that tax officers serve them fairly and with respect. Procedural justice refers to the perception of the service or treatment received by individuals from the authorities (Murphy, 2009) and it also relates to the process of resource division by the authorities (Kirchler, 2007).

Taxation research on procedural justice showed a positive impact on tax compliance. Empirical studies indicated that if an individual perceives that the authority is exercising a fair, existing procedure, they are more likely to trust the authority (Murphy, 2004) and more compliant with any decision made by the tax authority (Murphy & Tyler, 2008). However, previous studies on procedural justice have not reported consistent findings. Some researchers reported that procedural justice has a positive impact (van Dijke & Verboon, 2010), while others have reported different findings (Worsham, 1996).

Previous studies have acknowledged the effects of distributive justice on tax compliance behavior. Distributive justice refers to the perception of how far the input provided can garner the expected result in achieving equity (Adams, 1965; Walster, Walster, & Berscheid, 1973).

Most studies found distributive justice to have an impact upon tax compliance. Taxpayers evade tax payment when they believe there is injustice in the exchange relationship between taxpayers and the government (Kim, 2002; Porcano, 1984; Verboon & van Dijke, 2007). Taxpayers not receiving public exchange from the government believe injustice happens. The same situation applies when

taxpayers disagree with the government spending policy or they consider they did not receive fair exchange from the government, thus making them feel suppressed and influencing their non-compliance behavior (Kim, 2002).

Moser, Evans, and Kim (1995) in their study proved tax non-compliance happened when the respondent was taxed at a level higher than other taxpayers and did not receive public goods equivalent to the tax paid. The higher the return from tax received, the higher the level of tax compliance (Alm, Jackson, & Mckee, 1992; Alm, McClelland, & Schulze, 1992).

Even though there has been less research done analyzing the relationship between retributive justice with tax compliance, the findings show the two variables are related. Retributive justice refers to the perception of suitable punitive action when an act is against the norm. It comprises the requirement of inflicting suitable punishment for the wrong done (Kirchler, 2007). Various punishments are imposed for tax non-compliance; thus, the punishment must be suited to the severity of the wrong doing (Saad, 2011).

Tax compliance will increase when taxpayers perceive there is justice in the tax system that is capable of detecting and punishing those who fail to pay tax (Saad, 2011). Besides punishment, rewards for compliant taxpayers also influence compliance behavior (Falkinger & Walther, 1991). Therefore, the following hypotheses are constructed to determine the relationship of the three types of justice with tax compliance:

H1a: Procedural justice has a positive relationship to tax compliance.
H1b: Distributive justice has a positive relationship to tax compliance.
H1c: Retributive justice has a positive relationship to tax compliance.

Relationship Between Justice and Trust

Procedural justice and trust in the authority can explain the relationship between the authority and the citizen (De Cremer & Tyler, 2007). If the individual perceives that the authority has exercised fair procedures, then that person will have more trust in the authority (Murphy, 2004). In taxation, a relationship between taxpayers and the authority relies on the existence of trust and cooperation for tax compliance. Fair treatment received by taxpayers will boost their confidence and trust in the tax authority and assist in achieving high tax compliance.

In Australia, trust in the tax authority is low due to the unfair treatment received by taxpayers (Murphy, 2004). It is clear that there is a correlation between the fair treatment received by taxpayers and trust in the tax authority. This study also examines the relationship between distributive and retributive justice with trust through the following hypotheses:

H2a: Procedural justice has a positive relationship with trust.
H2b: Distributive justice has a positive relationship with trust.

H2c: Retributive justice has positive relationship with trust.

Relationship Between Trust and Tax Compliance

Trust emphasizes the relationship between the taxpayer and tax authority resulting from the trust of the taxpayer in the tax authority's actions. If a taxpayer has high trust in the tax authority, tax compliance is perceived to increase as well (Kastlunger et al., 2013).

Wahl et al. (2010) in their research studying the effect of power and trust on tax payment found a positive impact was derived from power and trust regarding tax payment. A highly reliable and trustworthy tax authority could increase tax compliance either voluntarily or through enforcement. The same findings are mentioned in the studies by Muehlbacher, Kirchler, and Schwarzenberger (2011) and Kogler et al. (2013), in which they find the trustworthiness of the tax authority increases voluntary tax compliance. This hypothesis was then constructed:

H3: Trust has a positive relationship with tax compliance.

Trust is also seen as a factor that could strengthen the relationship between procedural justice and tax compliance as a mediator (Murphy, 2004). Trust is regarded as an indicator to assess the authority's level of justice (Konovsky & Pugh, 1994). Therefore, besides having a direct impact on tax compliance, the relationship between procedural justice and tax compliance is also correlated to trust in the tax authority. This study will ascertain the mediating effect of trust upon the three types of justice. The following hypotheses are then established:

H4a: Trust mediates the relationship between procedural justice and tax compliance.
H4b: Trust mediates the relationship between distributive justice and tax compliance.
H4c: Trust mediates the relationship between retributive justice and tax compliance.

Figure 1 provides the framework for this study:

Research Methodology

This study applied a quantitative approach to obtain the respondents' perception of justice in the Malaysian tax system. Data were collected from field work using questionnaires distributed randomly to the selected respondents. In total, 300 respondents were selected from 57,613 academics teaching in public and private higher institutions in the Klang Valley (Selangor and Kuala Lumpur) (Ministry of Education, 2013). These states were chosen as they had the most public and private higher institutions. The number of samples selected was determined using the table in Krejcie and Morgan (1970) as suggested by Sekaran (2006).

The questionnaire was adapted from previous studies on trust and tax compliance by Kirchler and Wahl (2010) and Kastlunger et al. (2013). The procedural justice component was adapted from Murphy (2009) though
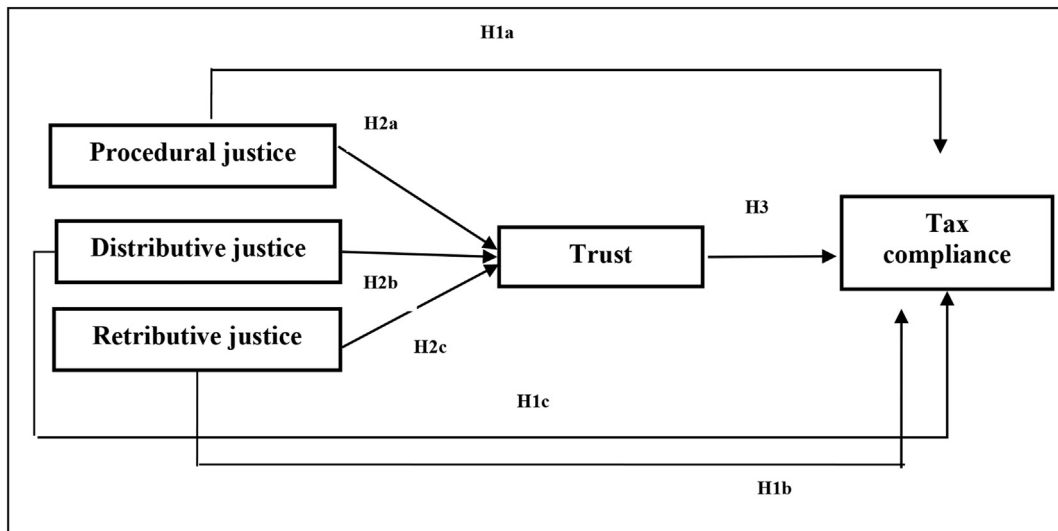
Figure 1 Research framework

initially constructed by Tyler (2006) and the distributive justice component was sourced from Verboon and van Dijke (2007), while the retributive justice component came from the study done by Saad (2011). Questions were modified according to the Malaysian situation and provided in English.

The questionnaire used in this study consisted of statements to measure each variable. Variables were measured through respondents' perception of tax compliance, trust, procedural justice, distributive justice, and retributive justice. Respondents' perceptions were measured using a 5-point Likert scale to determine the level of agreement with the statement given (in which 1 = highly disagree, 2 = disagree, 3 = not certain, 4 = agree and 5 = highly agree).

Results and Discussion

From the 300 questionnaires distributed, only 90 questionnaires could be accepted for data analysis. Table 1 shows the descriptive data of the respondents that were comprised of 53 lecturers (58.9%), 29 senior lecturers (32.2%), six associate professors (6.7%), one professor (1.1%) and one assistant lecturer (1.1%). From the total, 31 (34.4%) respondents were male and 59 (65.6%) were female, with 62 (68.9%) from public institutions and 28 (31.1%) from private institutions. Of the respondents, 49 had teaching experience of more than 10 years (54.4%), 22 respondents had five to nine years (24.4%), 16 respondents had one to four years (17.8%) and three respondents had worked for less than one year (3.3%).

Regression Test

Before conducting the regression, the reliability was tested to determine the consistency of the items in the questionnaires. Basically, the reliability is measured by referring to the value of Cronbach's alpha that should be at least .70 (Hair, Money, Samouel, & Page, 2007). Table 2

indicates the Cronbach alpha scores for each variable with only retributive justice having a score of less than .70. However, according to Hair et al. (2007), the strength of association is considered moderate if the Cronbach alpha score is between .60 and .70. Thus, for this study, it was decided to use this variable for analysis.

After determining the reliability was acceptable, the study used a regression test to analyze the relationships among variables. To test H1a, H1b and H1c, the following model was developed:

$$y = \beta_0 + \beta_1\chi_1 + \beta_2\chi_2 + \beta_3\chi_3 + \varepsilon$$

where y = Compliance behavior; χ_1 = Procedural justice; χ_2 = Distributive justice; χ_3 = Retributive justice; ε = Error.

Table 3 shows the multiple regression results between justice and tax compliance. The results identified that procedural justice, distributive justice and retributive justice had a positive relationship with tax compliance. However, only procedural justice was significantly related

Table 1
Descriptive data

		(n = 90)
	Respondent	Percentage
Gender		
Male	31	34.4
Female	59	65.6
Academic position		
Professor	1	1.1
Associate professor	6	6.7
Senior lecturer	53	32.2
Lecturer	29	58.9
Assistant lecturer/tutor	1	1.1
Institutions		
Public learning institution	62	68.9
Private learning institution	28	31.1
Teaching experience		
<1 year	3	3.3
1—4 years	16	17.8
5—9 years	22	24.4
>10 years	49	54.4

Table 2
Reliability test

Variable	Cronbach alpha
Compliance	.761
Trust	.928
Procedural justice	.948
Distributive justice	.770
Retributive justice	.600

Table 3
Multiple regression between justice and tax compliance

	R^2	β	p
Outcome: compliance			
Predictors	0.169		
Procedural justice (χ_1)		0.377	.000*
Distributive justice (χ_2)		0.070	.518
Retributive justice (χ_3)		0.109	.313

*$p < .001$

to tax compliance in Malaysia at the .001 level. Thus, tax compliance increases when taxpayers believe they have been treated fairly when dealing with the tax authority. Therefore, H1a is accepted.

The relationship between the three types of justice with trust (H2a, H2b and H2c) was established using the following model:

$$y = \beta_0 + \beta_1\chi_1 + \beta_2\chi_2 + \beta_3\chi_3 + \varepsilon$$

where y = Trust; χ_1 = Procedural justice; χ_2 = Distributive justice; χ_3 = Retributive justice; ε = Error.

Table 4 shows the regression results for justice and trust and indicates that only procedural justice can influence the trustworthiness of the tax authority with a positive significant relationship ($p = .000$). Thus, when the tax authority provides good services and fair treatment to taxpayers, this influences taxpayers' trust in the tax authority. Consequently, only H2a is accepted.

Next, in order to test H3 (the relationship between trust and tax compliance behavior), the simple regression model was developed $y = \beta_0 + \beta_1\chi_1 + \varepsilon$ with y = Compliance behavior and χ_1 = Trust. The result showed that trust in the tax authority had a positive significant relationship with tax compliance at the .001 level (Table 5). Thus, taxpayers' perception of the trustworthiness of tax authority can influence their tax compliance behavior. Therefore, H3 is also accepted.

To test the mediating effect of trust in the relationships among all types of justice with tax compliance, multiple

Table 4
Multiple regression between justice and trust

	R^2	β	p
Outcome: trust			
Predictors	0.617		
Procedural justice (χ_2)		0.759	.000*
Distributive justice (χ_1)		0.015	.841
Retributive justice (χ_3)		0.129	.081

*$p < .001$

Table 5
Simple regression between trust and compliance

	R^2	β	p
Outcome: compliance			
Predictors	0.165		
Trust (χ_1)		0.406	.000*

*$p < .001$

regression was used as suggested by Baron and Kenny (1986) and Frazier, Baron, and Tix (2004) because this study has a low response rate to utilize a Structural Equation Model (SEM) (Baron & Kenny, 1986). There are three steps to be established in testing the mediating effect using multiple regression (Frazier et al., 2004) as shown in Tables 6–8. In the first step, the relation between the predictor (procedural justice, distributive justice, and retributive justice) and the outcome (compliance) are tested. The results showed that only procedural justice had a significant relationship with tax compliance behavior (the unstandardized regression coefficient $B = 0.218$ at $p < .001$). Therefore, the requirement for mediation in step one was met for procedural justice. If step one does not show a significant result, the analysis can still be continued because sometimes the small sample size may not be able to predict the significant relationship between the

Table 6
Testing mediator effects using multiple regression for procedural justice

	B	SE B	95% CI	β
Step 1				
Outcome: compliance				
Predictor: procedural justice	0.218	0.056	0.106, 0.329	0.383**
Step 2				
Outcome: trust				
Predictor: procedural justice	0.767	0.067	0.634, 0.900	0.774**
Step 3				
Outcome: compliance				
Mediator: trust	0.158	0.088	−0.018, 0.333	0.275
Predictor: procedural justice	0.097	0.087	−0.077, 0.271	0.170

CI = confidence interval; **$p < .01$

Table 7
Testing mediator effects using multiple regression for distributive justice

	B	SE B	95% CI	β
Step 1				
Outcome: compliance				
Predictor: distributive justice	0.053	0.084	−0.113, 0.220	0.068
Step 2				
Outcome: trust				
Predictor: distributive justice	−0.031	0.146	−0.322, 0.259	−0.023
Step 3				
Outcome: compliance				
Mediator: trust	0.234	0.056	0.123, 0.346	0.408**
Predictor: distributive justice	0.061	0.077	−0.092, 0.213	0.077

CI = confidence interval; **$p < .01$

Table 8
Testing mediator effects using multiple regression for retributive justice

	B	SE B	95% CI	β
Step 1				
Outcome: compliance				
Predictor: retributive justice	0.167	0.097	−0.025, 0.359	0.181
Step 2				
Outcome: trust				
Predictor: retributive justice	0.365	0.167	0.034, 0.696	0.228
Step 3				
Outcome: compliance				
Mediator: trust	0.221	0.057	0.107, 0.335	0.385**
Predictor: retributive justice	0.086	0.092	−0.097, 0.269	0.094

CI = confidence interval; **$p < .01$

predictor and the outcome (Shrout & Bolger, 2002). Thus, step two proceeds to distributive justice and retributive justice to determine the mediating effect of trust.

In the second step, assessing the relation between the predictors with the mediator (trust), only procedural justice had a significant relationship with trust (the unstandardized regression coefficient = 0.774 and $p < .001$) and not distributive justice and retributive justice. If trust is not associated with distributive justice and retributive justice, then trust cannot possibly mediate any variable even though the step three result was significant. Thus, the next step to determine the mediating effect will be only applicable for procedural justice since the condition in step two was met.

The next step is to test the predictor simultaneously with the mediator and outcome. The finding indicated that there was no significant relationship between trust and procedural justice and compliance (the unstandardized regression coefficient = 0.158 and $p > .001$). This result did not prove that trust mediates the relationship of procedural justice with compliance, since both types of justice did not fit step three where there needed to be a significant direct result between justice and tax compliance. An additional step (step 4) only will be conducted if step 3 is met. In conclusion, trust does not mediate the relationship between procedural justice, distributive justice, and retributive justice with tax compliance behavior in Malaysia. As a result, H4a, H4b and H4c were rejected since trust has no impact on the relationships among the three types of justice and tax compliance.

From the results, we can conclude that most of the respondents would improve their tax compliance behavior if they perceived the tax authority manages to conduct good and fair treatment in tax activities and procedures. Fair treatment is more important than fair benefits or fair punishment received by taxpayers to increase tax compliance. This justice perception also will increase taxpayers' trust in the tax authority where this factor can also enhance tax compliance behavior. However, trust has been proved to have no effect in the relationship between procedural justice and tax compliance. The findings indicate that the tax authority in Malaysia will get trust, cooperation, and more compliant taxpayers if they treat taxpayers nicely and fairly in performing tax procedures.

Conclusion and Recommendation

The objective of this study was to investigate the opinions and perceptions of respondents on the impact of justice and trust on tax compliance in Malaysia. Justice was divided into three types—procedural justice, distributive justice, and retributive justice—as suggested by Wenzel (2002a). Therefore, this study tested four factors that may influence tax compliance in Malaysia. The findings from the questionnaire indicated that the perception of procedural justice in the tax system and trust toward the tax authority could increase tax compliance. Respondents believed that their compliance behavior would be increased if they received fair and just treatment when dealing with the tax authority and if they had trust in the tax authority. The findings indicate how the tax authority can enhance compliance through their actions with the taxpayers. The punishment approach may not be applicable to certain taxpayers.

This study however has its limitations. The low response rate may prevent the findings being generalized to the broader population of taxpayers in Malaysia. However, this research is still in the initial phase with findings which did not support a few hypotheses due to the minimal response rate. In addition, the respondents may not be able to distinguish between different types of justice which may have caused the lack of significance between distributive justice and retributive justice. Unclear definitions and justification of the differences may have contributed to these results.

Future research on different types of justice should be conducted incorporating the views of different types of taxpayers to obtain a more complete view on the matter. Further research on the effect of distributive justice and retributive justice on compliance needs to be considered since these two types of justice were shown to be perceived positively by the respondents but were not significant.

Conflict of Interest

There is no potential conflict of interest.

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