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PERSPECTIVE OF NON-TAXPAYERS' PERCEPTIONS ON ISSUES OF ETHICS AND EQUITY IN TAX COMPLIANCE

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This paper presents the findings pertaining to the perceptions of non-taxpayers on ethics and equity in relation to tax compliance. A majority of these non-taxpayers agreed that if they were taxpayers, they themselves would, and they also believe that most other individuals would consider tax compliance as legal and social obligations. They would also comply if they believe that they would be paying only their fair of tax and that the tax system is fair. However, they believe that most other individuals would likely not comply if these individuals considered that the taxes payable are too high; that taxpayers' money are being misappropriated or spent on wasteful projects; that they are not getting a fair share of the benefits that are financed out of taxpayers' money or that others are also not complying with their obligations. On the issues of under-reporting income; altering the incident of taxes and making fictitious claims for relief and expenses, in the context of ethics, although they considered such acts as unjustifiable, however, they believe that such acts are being practiced by most individuals.

Keywords: *Tax Compliance / Tax Ethics / Equity in Tax*

Introduction

For the purpose of the study, tax compliance is define as the ability and willingness of taxpayers to lodge appropriate tax returns in accordance with the requirements of the law. An appropriate tax return refers to one that is correctly prepared, containing full disclosure as required by the tax law and lodged within

the statutory specified deadline at the designated tax administration office. In this context, tax compliance is a function of taxpayers' cognitive and affective attributes. Cognitive attributes are associated with the knowledge and understanding of specific subject matter and the ability to apply and execute them to arrive at the desirable outcomes. Taxpayers' cognitive attributes would, therefore, encompass their level of knowledge and understanding of the technical and legal aspects of the tax law, relevant tax literature, tax administration's rulings and procedures and the ability to apply them when lodging appropriate tax returns. On the other hand, taxpayers' affective attributes are behavioural in nature, and would encompass factors such as attitudes, intentions and perceptions in the context of equity, ethics and moral. Although higher rates of tax compliance were found to be associated with higher ethical attitudes (Chan et al, 2000; Kasipillai et al, 2003a), the relationship between taxpayers' ethical beliefs and their tax compliance decisions is not simply direct and one dimensional (Henderson & Kaplan, 2005).

Tax Compliance Behaviour

Tax compliance behaviour may be perceived as a rational economic decision-making process; as a reaction to perceived fairness; as an ethical conduct or as an action due to ignorance. Each of these factors in isolation may not by itself contribute to a particular compliance behaviour. In fact, analysis of the findings of some empirical studies indicated that tax compliance behaviour varies widely over individual circumstances (Friedland et al, 1978) and influenced by factors such as the desire to avoid sanction (Smith & Kinsey, 1985 and 1987) as well as being subjected to group influence (Wallschutzky, 1993). Taxpayers may under-declare their income and would be deterred only by the chances of detection and penalties imposed (Allingham & Sandmo, 1972; Srinivasan, 1973).

Equity and Compliance

Other factors contributing to non-compliance might be the ethical values and attitudes of taxpayers (Song & Yarbrough, 1978; Buchanan, 1985) and the perceptions of fairness (Harriss, 1985). Taxpayers who perceived that their relationship with the government lacks equity are more likely to engage in non-compliance as a means to reduce the perceived inequity (Arrington & Reckers, 1985). Non-compliance was found to be positively correlated to perceived inequity (Keenan & Dean, 1980) and higher among those who feel disadvantaged by tax inequities (Spicer & Hero, 1985). Non-compliance was also found to be inter-related with the taxpayers' assessment of the fairness and burden of taxation, satisfaction with the government fiscal policy and that there were significant correlation between non-compliance and dissatisfaction with the tax administration (Elffers et al, 1987; Feld & Tyran, 2002).

Ethics and Compliance

Moral judgements form the basis of the ethical aspects of non-compliance. Moral appeal might be feasible (Mason, 1990) and could be effective on attitudes towards compliance

(Jackson & Jaouen, 1989). When tax is considered a burden or where tax fraud is so common, these might be perceived as acceptable justifications for non-compliance (Song & Yarbrough, 1978).

A study on the possible justifications for non-compliance (Keenan & Dean, 1980) suggested that tax evasion is justified for ordinary people because they perceived that the rich and famous cheat the government, or that the income tax system is unfair to them personally. Others might feel that it is morally right, though legally wrong not to pay taxes if taxpayers' money have been immorally or illegally wasted. Tax evasion behaviour may also depend on taxpayers' perceptions of the behaviour of others (Spicer & Lundstedt, 1976; Song & Yarbrough, 1978). This may imply that moral commitments to tax compliance would depend on the moral behaviour, ethical values and attitudes of other taxpayers as well as those non-taxpayers who may have enjoyed benefits paid out of taxpayers' money and also on the ethical and moral behaviour of those who administer taxpayers' money.

Addressing Non-Compliance

In the context of the Malaysia tax regime, in its drive to enhance tax compliance, the tax administration's emphasis seems to be on aggressive enforcement, with penalties and increasing the probability of detection to address non-compliance (Singh & Bhupulan, 2001). However, tax compliance is also influenced by sociological factors such as cultural norms and moral as well as psychological factors such as values and equity (OECD, 2004). Besides, successful means of preventing tax evasion is to improve tax ethics and people's conception of fairness of the tax system (Eriksen & Fallan, 1996). Although tax education may be extended towards assisting taxpayers to file their tax returns, there should also be focus on ethical values (Kasipillai et al, 2003a). In the Malaysian context, no effort seems to have been taken to understand taxpayers' behaviour and perceptions of ethics and equity in relation to tax compliance. Failure in this respect is a reflection of not taking cognition of the possible impact of taxpayers' affective attributes on tax compliance.

Objective of Study

The principal objective of this study is to examine perceptions in relation to factors in the affective domain that may influence tax compliance behaviour. These factors would have traces of ethical and moral values as opposed to factors in the cognitive domains that basically encompass knowledge and understanding in relation to the technical and legal aspect of taxation.

This study focuses only on the perceptions of taxation students. The rationale of examining students' perceptions pertaining to tax compliance is that they are likely to be future taxpayers or even tax practitioners. Although as students, they are being exposed to the technical and legal aspects of taxation, they have not experienced any actual tax compliance exercise, and therefore, would unlikely harbour any conflict of interest as most taxpayers would likely have. In this context, it is very pertinent, since taxpayers who do not comply

would often deny doing so (Hite, 1988), and some taxpayers might have been so embittered with the tax administration that they might intentionally attempt to distort the outcomes of a study (Schmolders, 1970).

This study examines the perceptions of these non-taxpayers in relation to factors that may be considered as reasons for complying or not complying, as well as what might be considered as justifiable or not justifiable in relation to specific hypothetical tax evasion settings.

Methodology and Limitations

Questionnaires were administered to students pursuing taxation courses in two universities, one a public and the other a private university. The taxation course contents of the two universities are similar, as both are courses on Malaysian Taxation. Generally, in these courses, students are taught and exposed to the technical and legal aspects of taxation, which formed the core of the course objectives. The ethical and behavioural aspects of taxation are not being pursued in these courses.

The questionnaires consist of three sections. In Sections A and B, respondents were to express their perceptions (on a five-point Likert Scale, ranging from strongly agree to strongly disagree) in relation to the reasons for complying or for not complying. In Section C, respondents were to indicate their views (on a five-point Likert Scale, ranging from definitely yes to definitely not), as to whether the respective hypothetical acts in relation to taxation issues in specific hypothetical settings are justifiable or otherwise, and whether the respondents believe most other individuals in similar settings would have acted in similar manners.

The principal limitation is that the respondents, being students, have not experienced paying income taxes nor experienced any encounter with the tax administration on tax matters. Thus, this study merely examines inexperienced, third parties' perceptions and views on hypothetical settings. However, in tax compliance studies, participants are frequently students (Andreoni et al, 1998; Kasipillai et al, 2003b; Trivedi et al, 2005; Devos, 2005) and there are evidence that responses from students as participants do not seem to be different from that of other categories of participants (Erisken & Fallan, 1996).

Discussions

Reasons for Complying

Eight factors are listed as the possible reasons why most individuals and the respondents would likely to exercise compliance. The respondents were required to express their perceptions as to whether they:- (1) strongly agree; (2) agree; (3) neither agree nor disagree; (4) disagree or (5) strongly disagree with the reasons. The respondents were then required to similarly express their perceptions as to whether they would likely comply because of these eight similar reasons if they were to be taxpayers.

For the purpose of discussion, those with “strongly agree” and “agree” responses are taken collectively as having agreed and similarly those with “disagree” and “strongly disagree” responses are taken as having disagreed with the reasons for complying or not complying (see Table 1 and Table 2).

Table 1: Reasons Why Most Individuals Would Likely Comply

Tax Compliance - Most individuals would likely comply because:-	SA %	A %	N %	D %	SD %	mean	Std. Dev.
It is a social obligation.	14.2	50.5	25.8	9.5	Nil	2.31	0.830
It is a moral obligation.	5.8	42.1	36.8	13.7	1.6	2.63	0.849
It is a legal obligation.	38.4	48.4	7.4	3.7	2.1	1.83	0.877
The tax system is fair.	7.9	38.9	38.4	12.1	2.6	2.63	0.892
One is only paying one's fair share of tax.	8.9	46.8	28.9	14.2	1.1	2.52	0.882
Others are also paying their fair share of tax.	5.3	27.9	47.9	17.9	1.1	2.82	0.825
The IRB administration is transparent.	6.8	31.1	43.2	15.8	3.2	2.77	0.906
The government administration is transparent.	6.3	31.1	36.8	21.6	4.2	2.86	0.966

** (1) SA = Strongly Agree; (2) A = Agree; (3) N = Neither Agree nor Disagree; (4) D = Disagree; (5) SD = Strongly*

Table 2: Reasons Why Respondents Would Likely Comply

Tax Compliance - The respondents would likely comply because:-	SA %	A %	N %	D %	SD %	mean	Std. Dev.
It is a social obligation.	12.6	52.6	26.3	7.9	0.5	2.31	0.812
It is a moral obligation.	11.1	46.3	28.9	11.6	2.1	2.47	0.912
It is a legal obligation.	32.1	54.2	8.4	2.6	2.6	1.89	0.860
The tax system is fair.	11.6	45.8	31.6	10.0	1.1	2.43	0.863
One is only paying one's fair share of tax.	7.9	60.0	21.1	10.0	1.1	2.36	0.810
Others are also paying their share of tax.	4.7	38.4	39.5	14.7	2.6	2.72	0.867
The IRB administration is transparent.	7.4	32.6	40.0	16.3	3.7	2.76	0.938
The government administration is transparent.	8.4	31.1	38.4	16.8	5.3	2.79	0.995

** (1) SA = Strongly Agree; (2) A = Agree; (3) N = Neither Agree nor Disagree; (4) D = Disagree; (5) SD = Strongly Disagree*

As to why most individuals and the respondents themselves would likely comply, about 86% agreed that legal obligation is the reason, which is consistent with the fact that tax compliance is a statutory requirement. Only about two-thirds agreed that social obligation is the reason for compliance. However, about 57% agreed that they themselves would likely comply because they also considered it to be a moral obligation while less than 50% agreed that most individuals would likely comply because of similar reasons.

As for the other possible reasons for complying, the respondents agreed that they would likely comply because they believe the tax system is fair (57.4%); and they would only be paying their fair share of taxes (67.9%), while a majority (55.8%) agreed that most other individuals would likely comply because these individuals believe that they are only paying their fair share of taxes.

For the following variables, namely, that others are also paying their fair share of taxes and that the tax administration and the government administration as a whole are transparent, only a minority of the respondents agreed that these are the reasons why most individuals and they themselves would likely comply.

Reasons for Not Complying

Eight variables are also listed as the possible reasons as to why most other individuals and the respondents themselves would likely not comply. The respondents were required to express their perceptions as to whether they:- (1) strongly agree; (2) agree; (3) neither agree nor disagree; (4) disagree or (5) strongly disagree with the reasons.

A majority of the respondents agreed that most other individuals and they themselves would likely not comply if they considered the taxes payable is too high; believe that taxpayers' money are being spent on wasteful projects and that others are also not complying. While only about 50% agreed that they themselves would likely not comply because of taxpayers' money being misappropriated but about 57% of them agreed that most other individuals would likely not comply due to the same reason (see Table 3 and Table 4).

About one-half of the respondents also agreed that most other individuals would likely not comply if these individuals consider the penalty and chances of being caught for non-compliance is low and that they are not getting a fair share of benefits financed out of taxpayers' money. That others are getting more than others' fair shares of benefits financed out of taxpayers' money is considered by less than 45% of the respondents as a reason for most other individuals likely not to comply.

Acts of Tax Evasion

Eight hypothetical settings in relation to acts of non-reporting of income; making fictitious claims for expenses and personal relief; altering the incidence of tax and collaboration in tax evasion scheme were presented to the respondents. These eight hypothetical settings are (1) an individual not reporting hard earned part-time income; (2) a husband declaring

Table 3: Reasons Why Most Individuals Would Likely Not Comply

Tax Compliance - Most individuals would likely not comply because:-	SA %	A %	N %	D %	SD %	mean	Std. Dev.
The penalty for non-compliance is considered to be low.	12.1	37.9	26.3	21.6	2.1	2.64	1.018
The amount of taxes to be paid are considered to be too high.	20.5	50.5	18.9	8.4	1.6	2.20	0.915
Taxpayers' money are being misappropriated.	16.8	40.5	31.6	9.5	1.6	2.38	0.929
Taxpayers' money are spent on wasteful projects.	18.4	37.9	25.3	17.4	1.1	2.45	1.016
Chances of being caught for non-compliance is believed to be low.	10.5	40.0	27.9	21.1	0.5	2.61	0.952
They are not getting a fair share of benefits financed out of taxpayers' money.	12.1	41.6	25.8	17.9	2.6	2.57	1.004
Others are getting more than their fair share of benefits financed out of taxpayers' money.	7.9	36.3	39.5	14.7	1.6	2.66	0.881
Others are not complying with their tax obligation.	10.0	50.0	25.8	12.6	1.6	2.46	0.894

* (1) SA = Strongly Agree; (2) A = Agree; (3) N = Neither Agree nor Disagree; (4) D = Disagree; (5) SD = Strongly Disagree

Table 4: Reasons Why Respondents Would Likely Not Comply

Tax Compliance - The respondents would likely not comply because:-	SA %	A %	N %	D %	SD %	mean	Std. Dev.
The penalty for non-compliance is considered to be low.	5.8	27.4	31.1	32.1	3.7	3.01	0.989
The amount of taxes to be paid are considered to be too high.	16.8	41.6	20.5	20.0	1.1	2.47	1.027
Taxpayers' money are being misappropriated.	14.2	36.3	34.7	13.7	1.1	2.51	0.936
Taxpayers' money are spent on wasteful projects.	12.1	42.1	29.5	14.7	1.6	2.52	0.941
Chances of being caught for non-compliance is believe to be low.	6.8	32.1	26.8	31.1	3.2	2.92	1.015
They are not getting a fair share of benefits financed out of taxpayers' money.	10.0	35.3	30.5	20.0	4.2	2.73	1.027
Others are getting more than their fair share of benefits financed out of taxpayers' money.	7.9	30.5	42.1	16.3	3.2	2.76	0.927
Others are not complying with their tax obligation.	13.7	42.1	27.9	13.2	3.2	2.50	0.991

* (1) SA = Strongly Agree; (2) A = Agree; (3) N = Neither Agree nor Disagree; (4) D = Disagree; (5) SD = Strongly Disagree

income earned by him as income earned by his wife so as to reduce their joint tax liabilities; (3) a father claiming child relief although he did not incur any expenditure on the maintenance of the child; (4) a father claiming expenses on the maintenance of a child as salaries of an employee since the child occasionally helped the father in his business; (5) a business operator claiming expenses for family dinner as business expenses; (6) an owner of a property not reporting the rental income because the annual repayment of loan to acquire the property is more than the annual rental received; (7) an individual claiming actual income derived as gains from lottery winnings and (8) an individual “selling” a winning lottery ticket at a premium while being aware of the “buyer’s” intention to evade tax.

It must be emphasized that lottery winnings are not taxable in Malaysia. Except for “selling” a winning lottery ticket at a premium, all the other acts as portrayed in the hypothetical settings are in violation of the income tax law, and would be classified as wilful evasion of tax. The act of “selling” a winning tickets *per se*, as portrayed in the setting may not be in violation of any law, but it may be construed as abetting another to evade tax. The respondents, being taxation students, are well aware of the legal position as portrayed in each of the eight hypothetical settings. However, this study attempts to examine whether taxation students, as non-taxpayers and on ethical grounds consider such acts as justifiable or otherwise and whether they believe that most individuals would act likewise.

On a scale of one to five, where:- (1) definitely yes; (2) probably yes; (3) not sure; (4) probably not and (5) definitely not, the respondents were requested to express their views pertaining to each hypothetical setting, where two responses were required. Firstly, the students were required to indicate whether the acts so portrayed in each of the eight hypothetical settings are justifiable or otherwise. Secondly, they were to indicate whether they believe most other individuals in similar settings and positions would act in similar manner as portrayed in each of the eight hypothetical settings.

Again, for the purpose of discussion, those with “definitely yes” and “probably yes” responses are taken collectively as indicating “justifiable”. Likewise, collectively the “probably not” and “definitely not” responses are taken as “not justifiable” (see Table 5 and Table 6).

Non Compliance – Justifiable or Not Justifiable

A majority of the respondents considered the following as not justifiable, namely, not reporting income earned on a part-time basis; declaring income earned by oneself as income earned by one’s spouse; claiming expenses for family dinner as business expenses and claiming actual income derived as gains from lottery winnings. Nearly one-half considered claiming expenses on the maintenance of a child as salaries of an employee and not reporting rental income as not justifiable. Overall, less than one-half of the students considered each of the eight acts as justifiable.

Table 5: Acts of Evasion: Justifiable or Not Justifiable

Justifiable or Not Justifiable for individuals in the hypothetical settings:-	DY %	PY %	NS %	PN %	DN %	mean	Std. Dev.
Not to report his hard earned part-time income as an insurance agent.	7.4	23.2	13.2	30.0	26.3	3.45	1.299
To report his income as income earned by his wife in order to reduce their tax liabilities.	5.3	25.8	14.2	35.3	19.5	3.38	1.210
To claim child relief although not incurring any expenses on the maintenance of the child.	17.9	30.0	14.7	21.6	15.8	2.87	1.363
To claim an allowance given to child as an employees' salaries.	3.2	25.8	22.1	29.5	19.5	3.36	1.156
To claim expenses for family dinner as business expenses.	3.2	15.3	14.2	39.5	27.9	3.74	1.119
Not to report rental income because repayment of loan is more than the rental received.	6.8	22.6	21.1	30.5	18.9	3.32	1.212
To make fictitious claim that income earned is from lottery winnings.	4.2	12.6	15.8	36.3	31.1	3.77	1.144
To 'sell' a winning lottery tickets at a premium although aware of tax evasion intention of the 'buyer'.	7.4	25.8	28.4	24.2	14.2	3.12	1.164

* (1) DY = Definitely Yes; (2) PY = Probably Yes; (3) NS = Not Sure; (4) PN = Probably Not; (5) DN = Definitely Not

Table 6: Acts of Evasion: Would Most Individual Evade

Would most other individuals in similar hypothetical settings also act likewise, i.e:-	DY %	PY %	NS %	PN %	DN %	mean	Std. Dev.
Not to report his hard earned part-time income as an insurance agent.	30.5	47.9	12.6	6.3	2.6	2.03	0.962
To report his income as income earned by his wife in order to reduce their tax liabilities.	19.5	45.3	21.1	12.6	1.6	2.32	0.979
To claim child relief although not incurring any expenses on the maintenance of the child.	32.1	45.3	12.1	8.4	2.1	2.03	0.986
To claim an allowance given to child as an employees' salaries.	11.1	41.1	33.7	10.5	3.7	2.55	0.951
To claim expenses for family dinner as business expenses.	14.2	38.9	23.2	19.5	4.2	2.61	1.082

Cont'd

Cont'd Table 6: Acts of Evasion: Would Most Individual Evade

Not to report rental income because repayment of loan is more than the rental received.	18.4	49.5	21.6	7.4	3.2	2.27	0.953
To make fictitious claim that income earned is from lottery winnings.	13.7	3.63	34.7	12.1	3.2	2.55	0.979
To 'sell' a winning lottery tickets at a premium although aware of tax evasion intention of the 'buyer'.	18.4	40.0	32.6	8.9	nil	2.32	0.877

* (1) *DY* = *Definitely Yes*; (2) *PY* = *Probably Yes*; (3) *NS* = *Not Sure*; (4) *PN* = *Probably Not*; (5) *DN* = *Definitely Not*

Non-Compliance Behaviour

Although most of the acts as portrayed in the hypothetical settings are considered as not justifiable, the respondents nevertheless believe that most other individuals would act likewise in similar settings. About two-thirds or more believed that most individuals in similar settings would not report income earned on a part-time basis; would declare income earned by oneself as income earned by one's spouse; would claim child relief although not incurring any expense on the maintenance of the child and would not report rental income because the repayment of the loan is more than the rental received. About one-half believe that in similar settings, most individuals would claim expenses for the maintenance of a child as salaries of an employee; claim expenses for family dinner as business expenses; claim actual income derived as gains from lottery winnings and would "sell" a winning lottery ticket at a premium although the "seller" was aware of the "buyer's" intention to evade tax.

Conclusion

Although legal and social obligations are perceived as reasons for most individuals to comply, misappropriation of taxpayers' money and spending of taxpayers' money on wasteful projects are perceived as reasons that most individuals would likely not comply with their tax obligations. Besides, having to pay high taxes and the belief that others are also not complying with others' tax obligations are also being perceived as reasons as to why most individuals would likely not exercise tax compliance.

The administrative transparency of the tax and government administrations and the belief that others are paying their share of tax are not perceived as reasons for most individuals to comply with their own tax obligations. Thus, other than being a statutory obligation, social obligation ranks higher than moral obligation as reasons for exercising tax compliance. Besides, perceptions of how taxpayers' money are being utilized are also considered as possible factors influencing compliance behaviour. In relation to the specific

hypothetical acts of tax evasion, although a majority consider these acts as not ethical, however, there is a belief that most individuals nevertheless would engage in such acts.

In order to ensure that tax-payers exercise appropriate compliance and lodging tax returns in accordance with the requirements of the law, the efforts and emphasis of the tax administration should not merely be on enforcement and penalties. Emphasis by way of tax education programmes should also be directed at uplifting the level of services to assist taxpayers in tax compliance. It is essential that tax education programmes should not only emphasise on the technical aspects of filing tax returns, but should also incorporate discussions on ethical values (Kasipillai et al, 2003a). Besides, there should also be attempts to understand taxpayers' attitudes and behaviour and their perceptions of the tax administration and administrators, as arresting and rectifying any undesirable perceptions, attitudes and behaviour of taxpayers would contribute towards positive tax compliance outcomes.

The current study is not intended to compare the perspective of IPTA and IPTS students on the tax issue. Nevertheless, available data could be used for future work to address on such comparisons.

Note

¹ Copies of the questionnaires can be obtained from the writers upon request.

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