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Elements of Compliance Costs: Lesson from Malaysian Companies towards Goods and Services Tax (GST)

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Abstract

Various parties including academics, professionals and the society (the potential GST payers) are arguing about the introduction of GST in Malaysia. Goods and Services Tax (GST) or Value Added Tax (VAT) is a consumption tax imposed on the sale of goods and services. The Malaysian government introduce this potential tax mechanism, in order to increase the existing tax bracket and replacing the long-implemented service and sales taxes. With the introduction of GST, the Malaysian government felt it would provide them with the prospect to reduce the rates of individual and corporate income tax. However, do all companies particularly small and medium enterprises (Companies) ready to adopt the systems efficiently? If they could adopt the system, how much their compliance costs involved such as developing new software, human resource training and accounting systems? The objective of this paper is to obtain companies' compliance costs and its elements and to provide suggestions to the tax authority what are the essential of companies to minimize their compliance costs. The data was collected through questionnaire from various enterprises throughout Malaysia. This paper is expected to suggest a proposal to the relevant authorities on the impacts on those companies. The government should also provide some special tax incentives to compensate the initial compliance cost incurred by small enterprises in particular so that they are not burdened by the newly implemented GST.

Keywords: compliance costs, small and medium enterprises, Malaysia, goods and services taxes (GST)

1. Introduction

The implementation of value added tax (VAT) or Goods and Services Tax (GST) in developing countries with various levels of income earners has called many arguments among taxpayer's particularly lower income earners. It is inevitably that the expansion of tax bracket introduced by the tax authority would increase tax revenue, in contrast would increase tax incidence of the taxpayers. GST is a consumption tax imposed on the sale of goods and services. GST is a new tax mechanism soon will be established by the Malaysian government. In Malaysia, the introduction of GST has caused many arguments from various parties including academics, professionals and the society (the potential GST payers) on how GST could affect the goods and services prices (increase or decrease). The GST will take the duty in replacing the current Sales Tax and Service Tax in line with the government policy to perform the requirements policies of AFTA.

In Malaysia, Sales tax is a tax that imposed on consumers indirectly which collected by business entities on behalf of the Royal Customs and Excise Department and it's would be imposed on manufacturer upon sale and importer of taxable goods (Fatt, 2010). The rates are different depending on the goods and items (e.g. all taxable goods - 10%; fruits, food and building materials - 5%; alcoholic drinks - 20%). Same goes to service tax. It's also an indirect tax with the rate of 5% that imposed on every purchasing of food by customers in places such as hotels and restaurants, or services which engaged on professional services such as audit and legal firms (Fatt, 2010).

The introduction of GST has long recommended by the International Monetary Fund (IMF) as a mode of increasing the efficiency of the Malaysian tax system and in the end raises the collection of tax. The tax authority of Malaysia plans to introduce a rate of 4% for goods and services tax, as a proposal to vary the national revenues (Inland Revenue Board of Malaysia -IRBM Annual Report 2010). The GST is planned to balance with the direct tax collection (personal and corporate taxes). From the introduction of GST, the Malaysian government believed it's would provide them with the opportunity to reduce the rates of individual and corporate income tax.

In general, the introduction of GST with the rate of 4% to replace the Sales and Service tax apparently shows that the prices of goods would decrease (because of the lower rate than Sales and Service tax). However, the lower price is subject to the willingness of business entities to excluding the sales and service tax element from the price of goods. Can we just imagine, what would happen to the prices of goods, if the business entities (retailers) already surcharged the customers with the GST but at the same time keep going incur the sales and service tax element to the price of goods?

From the previous experiences, Malaysian retailers are very reluctant to lower the goods prices even though their already forced to do so by the government and he price of goods is rather increase (by 4% at least) from what it's supposed to (decrease). Moreover, will the government still proceed to impose a 4% GST when the cost itself in collecting GST is expected to be merely to 3% and the benefit that's government gained only 1% from net tax collection (Singh, 2010). In developed countries that already implemented the value added taxes - VAT (GST), the rates that their imposed quite high such as 17.5% in United Kingdom and 19% in France, Belgium and Germany (Tait, 1998). It is different in Malaysia, the government believed that by the introduction of GST with 4% rate, it would provide them a chance to reduce the rates of corporate and individual income tax. However, do all companies particularly small and medium enterprises (Companies) ready to adopt the systems efficiently within the stipulated period after the announcement of GST in the Parliament? If they could adopt the system, how much their compliance costs involved such as developing new software, human resource training and accounting systems? The objective of this paper is to obtain companies' compliance costs and its elements and to provide suggestions to the tax authority what are the essential of companies to minimize their compliance costs. The data was collected through questionnaire from various enterprises throughout Malaysia including Sabah and Sarawak. The organization of this paper will begins with history of GST, followed by types of GST, estimation of compliance costs, research design, results and finally conclusion and discussions.

2. History, Issues and Development of GST

The firstly introduced the GST was in France around 1950s. After that the GST broadly being adopted by more than 120 countries, including the entire member states of the European Union (EU). GST is a percentage tax on value added (the difference between sales and the cost of purchased material inputs) at each stage of production. There are three basic types of VAT (GST) that depending on how the investment is treated in the tax base which are: 1) GDP-type GST; 2) consumption-type GST; and 3) income-type GST. Under the first type (GDP-type GST) system in calculating the tax base, there not allowed any the deductions for capital investment and depreciation of capital. So, the tax is equivalent to a sales tax which applicable to both consumer and capital goods. For the consumption-type GST system, capital investment in excluded from the beginning, which is deducted from the value added in the year of purchase. This indicate the tax is equivalent to a sales tax which applicable to consumer goods. Under income-type GST system, the tax base only excludes the depreciation of capital. This mean the tax that imposed is on net domestic product, which is close to national income. According to Sanford (1995), most of the countries which already established the GST system were adopt the consumption-type GST system. Under this system, all capital goods purchased from other firms are deductible from a firm's sale (Sanford, 1995). However, some of the countries such as Argentina, Peru and Turkey were adopted the income-type GST system, and a GDP-type GST system were implemented by China, Finland, Morocco and Senegal. GST rates vary significantly among countries. The standard GST rates range implemented around the world are from 5% (Singapore) to 25% (Denmark, Hungary, Sweden & Norway). Reduced rates and tax exemption are applied to certain goods and services. Revenues from GST account for a significant portion of government revenue in many countries. General sales tax and GST are among main contributor of the total central government revenue. In Greece, Sales tax and GST accounted for 33.25% from the total central government revenue in 1998, in U.K. 31% in 1999, in France 28% in 1997, in Argentina 42.58% in 2000, in Hungary 35.7% in 2000, in Russia 30.20%, and in Ukraine 33.7% in 2000.

3. Compliance Costs

Tax compliance costs are frequently used as part of or, sometimes, just intermixed with the excess burden of taxation in the economic literature. Where they are defined they are usually given a rather broad meaning covering a variety of different characteristics relating to the overall burden of taxation – in particular cost incurred to obey the tax laws. These costs are extremely significant to the relationship between government tax legislation and firms and/or taxpayers. Perhaps, the most suitable definition of compliance costs can be accredited to Sandford et al. (1981:13).

'... costs which are incurred by taxpayers [and] or by third parties in meeting the requirements of the tax system, over and above the tax liabilities itself and over and above any harmful distortions of consumption or production to which the tax may give rise'.

It has been recognised that the studies in the economic literature have tended to look only into the excess burden of taxation as a whole, implying that the welfare loss created with tax burden is derived exclusively as a result of a whole range of 'inescapable' obligations required by the tax legal system. To suggest that the excess burden can be represented in such a way, which basically assumes the existence of unlimited sources of tax pressure, seems to be an unrealistic proposition. It is the case that, in addition to data problems of measuring excess burden in the broad sense, such an approach does not offer much help towards the monetary loss inflicted on the private sector by tax legislation. It is rather important, therefore, to acquire some knowledge on measuring tax excess burden expressing what amounts to, in monetary terms, the burden created by tax legal obligations. One of the small but rewarding parts of assessment of tax excess burden is the attempt to measure that part which has been associated to the burden of accounting for tax revenue.

Sandford (1981) outlined three separate elements to the costs of compliance:

1) Monetary/Fiscal costs - the start up costs associated to establishing a company, the employee costs of running day to day GST accounting, the cost of expertise to understand and keep up with changes in policies and rates, the cost of submitting GST returns, and the cost of external accountants for operational and advisory services. Monetary costs include sums spent on tax professionals (i.e. tax agents and accountants) and expenses relating to taxation guides, books, communication and other incidental costs.

2) Time costs -Time costs are incurred by the taxpayer, mainly on record keeping for tax purposes, completing the tax return and/or in preparing tax details for the tax professionals as well as time spent on dealing with the tax authorities.

3) Psychological costs - comprise costs such as the anxiety of handling complex tax matters. The significant worry brought about the fact that the onus is squarely on the business to conduct their GST affairs properly, with financial and even criminal sanctions for failing to do so. The GST regulations can be very complex, and many companies are aware that they lack some of the knowledge required to be certain that they are using the correct policies and rates for all their transactions. This 'fear factor' is often highlighted as a component of compliance costs, even though it is not easily quantified.

Compliance costs in relation to book keeping for GST purposes, the conditions created by the method of book-keeping becomes the major problem to many traders. To account for GST payment demands a series of necessary duties closely related to the rules imposed by the Royal Malaysian Customs Department regulations. There are a number of detailed rules concerning the 'book-keeping' arrangements to enable GST assessment to be carried out. Since adequate records and accounts of all GST trading are to be maintained to support tax claims, traders must provide invoices, tax returns, book-keeping and accounts in agreement with the GST legislation. Such records are part of the expenses the 'Business' (i.e. GST registered trader) has to incur to comply and to fulfil its role in collecting GST revenue. These are part of the tax compliance costs assessment that research works have attempted to identify and to measure in the past.

Sandford et al. (1981) in a nation-wide survey of the U. K. registered GST traders provided a thorough account of tax compliance costs for the whole economy. In their paper at least two findings were remarkably relevant to the paper of compliance costs: a) for the first time, it was clearly identified that there were benefits as well as costs with tax compliance; and b) there was a strong case to believe that apart from economies of scale between business sizes, learning-by-doing also played a crucial part in reducing the level of tax compliance costs which, in turn, can be seen as giving greater gains to the more efficient firms.

Sandford et al.'s work did not go far enough to explain the overall source and time constraint of the learning-by-doing effect on tax compliance costs. Their work also failed to provide a thorough assessment on who would pay for tax compliance costs and what effect this would have on the income of firms and taxpayers. With respect to tax compliance benefits, their paper did not enquiry on the possible existence of any other gain provided by tax compliance e. g. commercial benefits which may derive from GST. These are relevant areas of enquiry which will be incorporated into the research work to be conducted in this paper.Some relevant features of tax compliance costs emerged out of the works presented by Sandford (1973 and 1976) such as: a) its main forms and affected parties; b) too high levels; and c) incompatibility with the whole of tax operating costs. Compliance costs were not negligible and more investigation would certainly help to give better insight of the problem.Businesses incur costs to comply with tax requirements, which are additional to their tax liability.

In Malaysia, the introduction of the GST is mainly motivated by the aim of increasing the national tax collection, widening tax bracket by imposing consumption-based tax. However, as GST will affect all nations including Companies, therefore a critical ways of thinking should be in place in reducing the compliance cost among them. The GST environment involves a substantial shift of responsibility on to taxpayers in terms of their compliance obligations with tax professionals expected to play a significant role in providing services to taxpayers in complying with the tax laws at early stage. Consequently compliance costs are expected to increase significantly during the early years of GST implementation. In the longer term, the relative level of compliance costs will depend upon a range of factors, particularly the complexity of the tax laws and frequency of tax changes.

4. Compliance Cost Estimates

Compliance cost in general can be affected by many variables including the complexity of tax systems. Relatively, small companies with smaller turnover, profit and asset might be affected much rather than medium or large companies. There is no doubt that it is the very small companies just above the GST threshold who bear the heaviest burden, sometimes going well into double figures when expressed as a percentage of total tax paid. For example, a National Audit Office of United Kingdom paper in 1994 found that, in the smallest companies, the cost of compliance was some 20 per cent of the tax paid.

Complexity of business, particularly where there is an international dimension, quickly leads to high costs of GST compliance. Even where companies are willing and able to engage in creative tax planning to minimize costs, for example by trying to take advantage of low GST regimes, establishing a company here to enjoy the low standard rate implies the costs associated with establishing a new company or with purchasing an existing company in and re-registering it. In addition, it is important to recognize that the pattern of business is changing. With high-tech businesses, in particular, complexity is often built into the business model from the very start - even when the company is small.

Compliance cost estimates have been conducted internationally, mainly in the UK, USA and Australia for over 20 years. The number of countries in which turn to research in compliance costs are also increase including India, Hong Kong, Netherlands, Spain, Croatia, New Zealand, Singapore and Malaysia. The regressive nature of compliance costs for all types of business taxes and by legal form is illustrated by Australian data, as shown in Table 1. Tax compliance costs of small business, irrespective of entity, measured per AU$1,000 of turnover, is at least nineteen times greater than for both medium and large business (Evans et al., 1997: 79-80). Currently, requiring a Tax Impact Statement for tax law changes is a normal practice in the Organization for Economic Co-operation and Development (OECD) countries, including Australia, the European Union, New Zealand, UK and the US (Evans & Walpole, 1999: 21). In the UK, the requirement to produce a Compliance Cost Assessment was introduced in 1985 and it is probably the first country to recognize compliance costs as a policy issue (Sandford, 1995: 3). The historical development of tax compliance costs is not considered further. Nearly all studies have found a markedly regressive pattern of tax compliance costs i.e. the burden falls heavily on smaller firms. The same trend hold true, either measured for a single type of tax or at a combined level, for all types of business taxes.

Table 1. Compliance costs for companies income tax as a percentage of turnovers

Australia 1990/1991		**New Zealand 1990/1991**		**UK 1986/1987**	
Turnover (AU$ Million)	Compliance costs as a % turnover	Turnover (NZ$ Million)	Compliance costs as a % turnover	Turnover (£ Million)	Compliance costs as a % turnover
< 0.5	3.0	< 0.03	13.15	< 0.5	0.77
0.5 – 1	0.8	0.03 – 0.1	4.31	0.05 – 0.1	0.20
1- 2	0.8	0.1 – 0.25	2.12	0.1 -0.5	0.17
2 – 5	0.2	0.25 – 0.5	1.35	0.5 - 1	0.07
5 – 10	0.1	0.5 - 1	0.78	1 – 10	0.03
10 - 20	0.02	1 - 2	0.79	10 and over	0.01
20 – 50	0.01	2 - 10	0.28		
50 and over	0.02	10 - 50	1.04		
		50 and over	0.03		

Source: Pope et al., (1994, Table 7.2 p.87).

Table 2. Compliance costs of corporate income tax per $1,000 of turnover

Turnover evel/year	Hong Kong a	Singapore b	Singapore c	Malaysia d
(in HK$ / S$/ RM)	1995/1996	1994	1995	1995
Less than 100 million	5.41	0.55	0.40	0.36
100 – 550 million	1.17	0.39	0.29	0.17*
More than 550 million	0.21	0.19	0.08	0.11*

*Note. The turnover level for Malaysia differs slightly, i.e. between RM100 – RM500 million, and greater than RM500 respectively.

Sources: a Chan et al. (1999, p.55), b Ariff et al. (1995, p.81), c Ariff et al. (1997, p.1260), d Loh et al. (1997).

Table 3. Tax compliance costs in malaysia

	Public-listed company a	**SME**b
Year of paper	1995	1999
Tax Compliance Cost / per firm	RM68,836	RM21,964
Component of costs (%)		
Computational	61%	59%
Planning	39%	41%
Sources of costs (%)		
Internal	28%	75%
External	72%	25%

Source: a Loh et al., (1997) and b Hanefah et al., (2001).

Conversely, in the process of keeping records for GST purposes, the conditions created by the method of book-keeping becomes the major problem to many traders. To account for GST payment demands a series of necessary duties closely related to the rules imposed by the Royal Malaysian Customs Department regulations. There are a number of detailed rules concerning the 'book-keeping' arrangements to enable GST assessment to be carried out. Since adequate records and accounts of all GST trading are to be maintained to support tax claims, traders must provide invoices, tax returns, book-keeping and accounts in agreement with the GST legislation. Such records are part of the expenses the 'Business' (i. e. GST registered trader) has to incur to comply and to fulfil its role in collecting GST revenue. These are part of the tax compliance costs assessment that research works have attempted to identify and to measure in the past.

5. Research Methodology

5.1 Questionnaire Design

The development of survey instruments was based on Abdul-Jabbar (2009) and Junainah (2002). The survey question was divided to four main sections. The first section consists of background of Companies including their main business activity, turnover, profits and tax liability. The second section consists of a series of questions pertaining to respondents' compliance costs including external cost and internal cost. Several questions were asked including average hours spent by tax related employees in a week, employee wages and salaries as well as their potential expenditure as their preparation towards GST implementation. The third section consisted of respondents' perception, readiness and acceptance if GST were implemented. The last section attempts to obtain data pertaining to the impacts of GST of Companies. Junainah (2002) studied about Self Assessment System (SAS), regardless the enterprises' perceptions, awareness and readiness toward the implementation of SAS as new tax system in Malaysia. Junainah's paper was conducted two years before the implementation of SAS in Malaysia in 2004. Therefore, it is relevant for this study to use the similar instrument and approach as used by Junainah as GST will be implemented soon in the future. A total of 173 enterprises were analysed to answer the research questions and achieve the objective of this paper. The next section will discuss the results of this paper by outlining the descriptive evidence of enterprises as well as computation of compliance costs.

5.2 Data Collection

The paper draws the sample frame from both manufacturing and service sectors of companies in Malaysia. A sampling frame is a "list of sampling units from which the sample may be drawn" (Hair, Anderson, Tatham & Black, 1998). Once a sample is drawn, data need not be collected from the whole population. But the results can be inferred to the whole population (Babbie, 1990). Therefore, the correspondence between population and sample is extremely important because the accuracy of the sample relies heavily on the sample frame, which is defined by the population.

Initially, the sample was going to be selected using a probability sampling technique to ensure that each firm had an equal chance to be selected. Instead of simple random sampling, proportionate stratified random sampling was applied as it allows an appropriate size of samples to be drawn from the homogenous subsets of a population (Sekaran & Bougie, 2010; Sekaran, 2000; Malhotra & Birks, 2003). The main intention for adopting stratified sampling was to reduce the variability between the samples by creating relatively homogenous strata. Therefore, the sample was drawn from each stratum proportionate to the relative size of that stratum in the total population.

Data was collected through a structured survey among companies in Malaysia. Respondents were chosen randomly from various organizations based on inputs form SME Corporation Malaysia (http://www.smecorp.gov.my). The number of Companies in the registry stands at 548,267 but 434,939 enterprises are under the Micro category which annual sales is less than RM250,000, unlikely to be affected by the current sales and service tax nor the proposed GST. The balance 113,328 enterprises which form the sampling frame are involved in manufacturing, services and agriculture. Agriculture due to its relatedness to food industry is also excluded as food may be GST exempt. In summary, the total of 110,978 enterprises in the manufacturing and services sector are used to guide this paper.

In considering the potential for a poor response rate, a sample of 1,109 Companies was considered appropriate to provide the number of responses required for analysis. However, it should be noted that there is a common pattern of low response rates (i.e. less than 20%) for mailed academic surveys in Malaysia (Rahman, 2000; Rozita, Yusserrie & Fauziah, 2004; Che Ruhana & Foong, 2005; Saudah, 2005; Ruzita, Daing & Yusserrie., 2007). For example, Rozita et al. (2004) reported a 16% response rate; Ruzita et al. (2007) managed to get a 12% response, while Che Rohana and Foong (2005) stated a 10% response. As mentioned by Ruzita et al. (2007: 125), "…for a mail survey (a) low response rate is not unusual in Malaysia." A target response rate of 10 percent would mean a total of at least 111 responds must be obtained.

Focus was given to enterprises in the big cities to represent the entire population of the state (see Bryman & Bell, 2003; Palil, 2010). Furthermore, enterprises which located in the cities are having active business activities in response to the introduction of GST compared to respondents who are living outside the cities. This would increase the external reliability, reduce sampling errors and enrich the data (Sekaran, 2010; Sekaran & Bougie, 2010).

Since this survey represents enterprises' compliance costs in response to the introduction of GST, enumerators were employed to obtain the responses. The presence of the enumerators is expected to establish two-way interactions in explaining the strength of GST and answering any problems pertaining to the questionnaire. Although this data collection method (using enumerators) might be costly compared to other methods such as interviews and postal surveys, however, this is the most suitable method in obtaining a reliable, valid and independent data for exploratory research (Black, 2001) as this study is particularly exploring the impacts of a new government policy (GST). This paper is considered as exploratory research in the sense of GST is yet to be implemented. The finding of the descriptive statistics for this paper will be useful in gaining a deeper understanding of the challenges that facing by the companies in relation to GST.

6. Data Analysis

The survey population involved small and medium companies from three main business activities namely manufacturing, services and both manufacturing and services. The actual number of respondents is 173. However, not all questions answered by these 173 respondents, particularly in sections concerning monetary costs and implementation of GST resulting in various number of frequency being analysed. The descriptive analysis on the background of the organisation, monetary compliance costs, matters on implementation of GST, and potential impacts of GST on company are discussed in this section.

Table 4. Background of organisations

Item	Description	Frequency	Percentage (%)
Location	Central Region	42	24.3
	Northern Region	23	13.3
	Southern Region	28	16.2
	Eastern Region	34	19.7
	East Malaysia	46	26.6
Main Business	Manufacturing	49	28.3
Activities	Services	124	71.7
Turnover in 2010	RM200 000-RM500 000	97	56.7
	RM500 001-RM750 000	22	12.9
	RM750 001-RM1 000 00	16	9.4
	RM1 000 001-RM2 500 000	16	9.4
	RM2 500 001-RM5 000 000	9	5.3
	RM5 000 001-RM10 000 000	3	1.8
	Above 10 million	8	4.7
Accounting profit in	No profit	11	6.5
2010	Below RM80 000	69	40.8
	RM80 001-RM200 000	47	27.8
	RM200 001-RM300 000	12	7.1
	RM300 001-RM400 000	8	4.7
	RM400 001-RM1 000 000	11	6.5
	RM1 000 001-RM2 000 000	6	3.6
	Above RM4million	5	3.0
Corporate tax liability in	No tax liability	34	20.7
2010	Below RM20 000	66	40.2
	RM20 000-RM50 000	26	15.9
	RM50 001-RM75 000	16	9.8
	RM75 001-RM100 000	7	4.3
	RM100 001-RM250 000	7	4.3
	RM250 001-RM500 000	3	1.8
	RM500 001-RM1 000 000	1	0.6
	Above RM1million	4	2.4
Company tax	Sales tax	53	35.8
	Service tax	95	64.2
GST implementation	Subjected	77	44.5
	Not subjected	21	12.1
	Not sure	75	43.4

As shown in Table 4, the most responses came from the Companies situated in East Malaysia (26.6%) followed by Central Region (24.3%), Eastern Region (19.7%), Southern Region (16.2%), and Northern Region (13.3%). The majority of the Companies were running the service business (71.7%) followed by manufacturing (28.3%). As for the turnover in 2010, more than half (56.7%) of the Companies earned between RM200 000 and RM500 000. In terms of accounting profit in 2010, 82.2% of the Companies were in the first four levels which gained between no profit and RM300 000. Meanwhile, there were 5 (3.0%) of the Companies gained above RM4million. Out of these, more than half (60.9%) of the Companies liable for the tax liability below RM20 000 (40.2%) while 20.7% were under no tax liability. From the analysis, previously 53 of the Companies were liable for services tax while 95 of the Companies liable for sales tax. Only 25 Companies previously are not subjected to sales tax and service tax. Nearly half (44.5%) of the respondent clearly stated that they are subjected to the GST when it implement while 43.4% of the respondent still not sure whether they are subjected to the GST up to the date of data collection. Only 12.1% of Companies stated that they are not subjected to GST.

7. Compliance Cost – External Cost

External costs arise from payments made to acquire the services of accountants, tax agents, legal adviser and investment advisers from outside company. Complying with the tax laws and regulations, including filing annual tax returns with the Inland Revenue Board (IRB), may require these services. As shown in Table 7, most of Companies required the tax-related services from accounting firms (40.1%) followed by tax agents (26.5%) and the combination of accounting firms and tax agents (12.9%).

Table 5. Sources of tax-related services in 2010

Item	Frequency	Percentage (%)
Accounting Firms	65	40.1
Tax Agents	43	26.5
Accounting Firm and Tax Agents	21	13.0
Legal Advisers	10	6.2
Acc Firm, Tax Agents and Legal Advisers	5	3.1
Acc Firms, Legal Advisers and Merchant Bank	4	2.5
Others	4	2.5
Merchant Banks	2	1.2
Accounting Firms and Merchant Banks	2	1.2
Tax Agents and Legal Advisers	2	1.2
Accounting Firms, Tax Agents and Others	1	0.6
Accounting Firms and Legal Advisers	1	0.6
Legal Advisers and Merchant Bank	1	0.6
Accounting Firms, Tax Agents, Legal Advisers and Merchant Banks	1	0.6

Most of Companies stated that the main reason for using the external source of tax-related was due to the lacked of technical expertise in tax (37.3%), following their company policy (28.5%), cost effectiveness (15.8%) while the balance was the combination of them. A summary of the reasons for tax-related services in 2010 is shown in Table 6 below.

Table 6. Reasons for tax-related services in 2010

Item	Frequency	Percentage (%)
Lacked of Technical Expertise In Tax	59	37.3
Company Policy	45	28.5
Cost Effectiveness	25	15.8
Lacked of Technical Expertise In Tax & Cost Effectiveness	13	8.2
Cost Effectiveness & Company Policy	7	4.5
Lacked of Technical Expertise & Company Policy	7	4.5
Lacked of Technical Expertise In Tax, Cost Effectiveness & Company Policy	1	0.6
Others	1	0.6

Table 7. Average external cost incurred for tax-related service in 2010

	Cost incurred (RM)
Tax Computation	2 103
Tax Planning	3 222
Tax Appeal	2 063
Total	**7 388**

Based on Table 7, on average the companies paid the external tax-related service RM7 388 per year for their service. Most of the Companies spent more on tax planning (RM3 222) followed by tax computation (RM2 103) and tax appeal (RM2 063).

8. Compliance Cost – Internal Cost

Internal costs relate to the time and money spent by company staff on maintaining and preparing information for professional advisers, completing tax forms and dealing with revenue authorities on matters pertaining to inquiries, objections and appeals. Based on Table 8, on average accounting staff spent more time on tax matters (6.72 hours per week) followed by manager (6.60 hours per week) and computer staff (5.16 hours per week). Managers spent most of the time on tax planning and tax appeal compare to the others while accounting staff spent more time on tax computation. Computer staff spent less time in tax computation, tax planning and tax appeal compare to the manager and accounting staff.

Table 8. Average time spent (hours) per week in 2010 by staff on tax-related

	Manager	Accounting Staff	Computer Staff
Tax Computation	5.96	7.67	5.17
Tax Planning	8.54	3.73	4.68
Tax Appeal	6.26	6.12	5.64
Average time (per week)	**6.60**	**6.72**	**5.16**

Table 9 shows the average wages paid per month for staff involved in tax related matters. Based on Table 11, managers received the highest wages at the average of RM4 165 per month followed by accounting staff (RM2 769) and computer staff (RM1 633).

Table 9. Average wages paid per month for staff involved in tax related matters

	Manager	Accounting Staff	Computer Staff
Average Wages	RM4 165	RM2 769	RM1 633

Table 10 demonstrated the computation of internal compliance cost of Companies. The internal compliance costs were calculated as the total of time cost of three categories of staff within the business namely manager, accounting staff and computer staff. This amount was computed by multiplying annual time spent on tax activities by their respective hourly wage rate. It is found that the total amount of internal compliance cost was RM16 722.

Table 10. Computation of internal compliance cost

	Hours spent/week (a)	**Average working hours/week (b)**	**Weekly salary RM (c)**	**Compliance cost/year RM (d) = (a/b) x c X 52 weeks**
Managers	6.60	45	1,041	7 939
Accounting staff	6.72	40	692	6 045
Computer staff	5.16	40	408	2 737
Total				**16 722**

9. Compliance Cost – Additional Cost

Table 11 shows the average cost incurred by the Companies related to tax matters such as buying tax material, human resource training on tax matters and others. These costs are referring to additional cost since it is an internal cost which involved a non-staff matter. On average, the Companies spent an additional cost of RM4 296 on tax matters and the highest spending was on human resource training (RM1 552).

Table 11. Average cost incurred by companies on tax matters

	Average cost incurred (RM)
Buying tax material	1 461
Human resource training	1 552
Others : travelling, postage, stationary, photocopying	1 283
Total	**4 296**

10. Total Compliance Cost – Cost Estimate

This compliance cost estimate mainly follows similar approaches used by earlier studies. Based on Table 12, the average compliance cost per company is RM28 406 (per firm/per year) or RM2 367 (per firm/per month). The largest portion of compliance cost is represented by internal cost at RM16 722 per year (RM1 394 per month) or 58.87% of total compliance cost. The external cost is at 26.01% (RM7 388) followed by the smallest portion of additional cost at 15.12% (RM4 296). The compliances cost of Companies in 2010 are summarised in Table 12 below.

Table 12. Means compliance cost of companies in 2010 by components

	Means Compliance Cost(RM)	Percentage (%)
Internal cost	16 722	58.87
External cost	7 388	26.01
Additional cost	4 296	15.12
Total	**28 406**	**100**

11. Major Element of Compliance Costs – If GST Implemented

11.1 External Cost

When the GST is implemented soon, majority of Companies expect that they will require the external source of GST service for tax computation (70.4%) followed by tax computation and tax planning (10.4%) as well as tax planning (9.6%). On average, the Companies expect to incur an additional cost of RM6 336 for the external source of GST service per year. Most of the Companies expect to spent more on tax planning (RM2 688) followed by tax computation (RM2 006) and tax appeal (RM1 643). The summary of the above discussion are shown in Table 13 and Table 14.

Table 13. Expected external source of GST services

Item	Frequency	Percentage (%)
Tax Computation	95	70.4
Tax Planning	13	9.6
Tax Appeal	2	1.5
Tax Computation And Tax Planning	14	10.4
Tax Computation, Tax Planning And Tax Appeal	2	1.5
Tax Computation And Tax Appeal	9	6.6

Table 14. Expected average external cost incurred for GST

	Cost incurred (RM)
Tax Computation	2 006
Tax Planning	2 688
Tax Appeal	1 643
Total	**6 336**

11.2 Internal Cost

As shown in Table 15, most of the Companies expect the implementation of GST soon will increase their internal cost for tax computation and tax planning. However, the numbers of Companies which feel that the implementation of GST will give no effect on their internal cost were not far behind. In term of tax appeal, most of the Companies feel that there will be no change in their internal cost.

Table 15. Expected internal cost effect on GST implementation

Item	Increase	Decrease	No change
Tax Computation	58	14	48
Tax Planning	29	6	26
Tax Appeal	12	1	25

11.3 Additional Cost

According to Table 16, most of Companies still not ready for the implementation of GST since only 13 (7.5%) already bought a GST tax guide and software while only 17 (9.8%) of them undergo a human training on GST.

Table 16. Additional cost on GST implementation

Item	Yes	No	Not sure
Buying GST tax guide and software	13	130	30
Human resource training on GST	17	116	40

12. Discussion and Conclusions

As discussed earlier, the objective of this paper is to estimate the compliance cost of Companies when GST is implemented in Malaysia. The paper found that the compliance cost of SME in 2010 before the implementation of GST is RM28 406 (per firm/per year). The largest portion of compliance cost is represented by internal cost at RM16 722 per year or 58.87% of total compliance cost. The external cost is at 26.01% (RM7 388) followed by the smallest portion of additional cost at 15.12% (RM4 296).

In relation to the potential implementation of GST in Malaysia, we expect that there is a potential significant increase in compliance cost in the first three years as happened during the introduction of Self-Assessment System (SAS) in 2001. The paper found that the potential compliance cost when GST is implemented would increase the external source of GST service for tax computation (70.4%) followed by tax computation and tax planning (10.4%) as well as tax planning (9.6%). On average, the Companies expect to incur an additional cost of RM6 336 for the external source of GST service per year. The paper also found that most of the Companies expect the implementation of GST soon will increase their internal cost for tax computation and tax planning. This finding implies that the majority of the enterprises would have to spend more on their human resource at the early stage of the implementation of GST, which is considered as an extra burden to small and medium enterprises. Based on the findings, most of Companies are still not ready for the implementation of GST since only 13 (7.5%) already bought a GST tax guide and software while only 17 (9.8%) of them undergo a human training on GST. Results of this paper also suggest that the increment of compliance cost among companies when GST is implemented would create extra burden to small enterprises in particular and would encourage non-compliance behaviour. Increase in compliance cost means increase on their absolute tax incidence (tax liabilities plus compliance costs). Judging from the results of this paper, the respondents seem to receive less information and promotions from the relevant authorities. Many respondents were still unsure on how the GST will be implemented. The promotion regardless the GST should be done more by the government, especially through the media so that people are ready for the impacts of GST. Secondly, due to less information, the mindset of current people's will keep thinking that the GST will increase their compliance cost and tax obligations. Therefore, the government should do something in convincing those people that, the GST will not increase compliance cost significantly. If the GST increases the compliance cost, the government should have the alternatives planning to reduce the burden of companies such as increasing the exemptions for the companies and lowering the income tax rates. Thirdly, as this paper suggested that there is significant positive relationship between compliance cost and non-compliance behaviour, in the long run, the national revenue would decrease and this could potentially distort the economic growth, particularly on aggregate demand.

Conversely, even though this paper suggested that GST will increase compliance cost however, Malaysia should proceed to implement the GST in near the future as an alternative approach to increase the government revenues, although there would be many operational problems and acceptance issues from various parties such as traders and consumers in the early stage of implementation. The developed countries such as United Kingdom (17.5%) and New Zealand (12.5% - 15%) are the example of the countries that have improved their tax revenues and efficiency through the introductions of GST. So, Malaysia should receive a considerable support and cooperation from all parties not only from business entities but also from consumers like us to realize this new tax system. This paper is expected to give a general idea to the relevant authorities regardless the introduction of GST toward social and economy impacts on those companies. The government should also provide some special tax incentives to compensate the initial compliance cost incurred by small enterprises in particular so that they are not burdened by the newly implemented GST.

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