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Understanding tax morale of SMEs: A qualitative study

Recep Y¿cedoĵ ru

-managers about their company's wellbeing that ma
Prior literature suggests that there are six relevant factors/constructs that influence SMEs' tax moral
costs, professionalism, tax advisors' effect, company structure, size of economic obligation and risk a
conceptual model of tax morale, we utilise an exploratory qualitative methodology and provide findin
analysis of twenty semi-structured interviews with SMEs owners-managers in Turkey. Our study cont
by explaining the six constructs and by being one of the very few research studies of tax morale in S
country.

Keywords: tax morale, SMEs, risk aversion, compliance costs, qualitative analysis, interview analysis

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1. INTRODUCTION

Identifying and understanding the causal variables of voluntary tax compliance has been an interest of many tax scholars over the last several decades. The extant literature discusses many independent variables of taxpaying behaviour, including: those derived from expected utility models of tax evasion such as tax audits and the fear of being caught and penalised (Allingham & Sandmo, 1972; Andreoni et al., 1998; McKerchar & Evans, 2009), compliance costs (Hasseldine, 2001), and equity and fairness of the tax system (Spicer & Becker, 1980). Nevertheless, moral and cultural motivations of taxpaying behaviour which can play an effective role on taxpayers' compliance are relatively underexplored (McGee, 2006; Torgler, 2007). Specifically, in the tax morale literature, nearly all prior research has focused on the tax morale of individuals (Pope & McKerchar, 2011). There are only very few exceptions to our knowledge such as the studies of Alm and McClellan, (2012), Ahmed and Braithwaite (2005), Abdixhiku, (2013) and Mickiewicz et al., (2012) which investigated the tax morale in the firm level. Abdixhiku, (2013) and Mickiewicz et al., (2012)

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with other constructs such as ‘social norms’ (Alm et al., 1999), perceptions of ‘power’ and ‘trust’ (Kirchler et al., 2008) and ‘fiscal exchange’ (Feld & Frey, 2002).

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Tax morale and related constructs, such as social and moral aspects of taxpaying behaviour, are not widely discussed in the literature (Frey & Torgler, 2007; Kornhauser, 2006; Alm & McClellan, 2012). Further, as most prior work has taken place within Western economies, a gap in the literature to study tax morale in a non-western society, such as Turkey, became more apparent as some of the literature already suggests (McGee et al., 2011; Tekeli, 2013).

Ahmed and Braithwaite (2005) w

Saunders et al. (2003) state that a structured interview is more appropriate for a descriptive or explanatory based study while a semi-structured interview is more suitable for exploratory based studies. They further argue that the in-depth interview is more useful for studies which are exploratory in nature and one of the most common qualitative approaches. This is probably due to its flexibility (Bryman & Bell, 2011) since even though the researchers has a list of questions and themes to be covered these may vary from one interview to the other (Saunders et al., 2003). It also has the ability to disclose important aspects of human behaviour (Qu & Dumay, 2011) because a semi-structured interview could reveal not only the 'what' and 'how' but also the 'why' (Saunders et al., 2003).

Selected SMEs who participated in semi-st

process of coding the data according to the described framework, and third, finding related themes and analysing the themes to check for consistency.

The process of transcribing the recording is important because it reflects how the researchers interprets the data (Bailey, 2008). On average, it took approximately six to eight hours for the first author to transcribe the recording of each interview. This is because, as suggested by Bailey (2008), transcription involves close observation of the data through repeated careful listening to the audiotape. Since all interviews were conducted in Turkish, all analyses were run in the same language and the results of the analyses have been translated into English.

Validity in qualitative research is defined according to how accurate the data represents the realities of the interview participants toward understanding social phenomena (Creswell & Miller, 2000; Patton, 2002). One common method to determine validity in a qualitative study is to use the 'member checking procedure' (Creswell, 2009; Creswell & Miller, 2000; King & Horrocks, 2010). Member checking involves requesting the interview participants to confirm the credibility of the information by asking the participants to check the data, whether the themes are correct and the overall information is accurate (Creswell & Miller, 2000). Although the literature does not suggest a rule of thumb for the number of participants for member checking procedures, Creswell (2009) argues that a minimum of two members is preferred. In order to determine participants for the member checking procedure, the researchers emailed the interview participants with the information about the research aims and how the analysis is carried out and asked them about their participation. Three participants agreed to participate. Following the suggestion by Creswell (2009), the researchers requested those participants to check the transcripts, identified themes and their feedback as a procedure to determine the validity of the findings. The feedback confirmed validity and the feedback were used to increase the validity of the interview analysis. Lastly, expert feedback was used to determine the coding validity of the interview analysis. Expert feedback is hig2 (q8u7e 6 (-1.141 Td [(co)

Analysis also showed different approaches to compliance costs that are not strongly stressed in the literature. Participants 1, 5 and 9 mentioned that financing taxes heavily affects their compliance cost burden rather than other compliance costs. Financing taxes mainly referred to paying VAT which is due on the 26th of the following month after the invoice date of their sales. However, the average due date of invoices varies between two and four months in many sectors. Consequently, small companies that lack working capital find it difficult to pay their taxes on time because their taxes are due before their debtors pay.

Additionally, procedural difficulties to solve tax problems with the Turkish Revenue Administration (TRAD) were also mentioned as generating unforeseen compliance costs by participants 4 and 9, such as reaching authorised tax officers on duty, solving problems without dealing with further paperwork etc.

> They (TRAD) flagged my 100 Turkish Liras (TL) tax debt into enforcement. For some reason, I had forgotten it. I had not remembered, nobody reminded me. I went there to pay the amount. I realised they put an enforcement annotation on three of my cars that is worth 90 000 TL i391 0 Td5 (L)-8.7-4.6 (

penalties. In support, Marrelli and Martina (1988) claim that staff capability in companies is negatively correlated with tax evasion.

Participants were asked about their understanding of professionalism and whether they would define their company as a professional one. In the sample, projections of professionalism vary amongst the participants. The majority of participants

evidence of the in

4.3 Tax advisors' effect

Roth et al. (1989) defined tax advisors as professionals with whom taxpayers discuss tax matters and from whom they receive advice about actual risks and rewards of the tax compliance. Tax advisors provide three sorts of services: return preparation, tax advice and risk advice. Each of these advice types has potential effects on tax compliance and tax morale of taxpayers (Hasseldine et al., 2007). The importance of tax advisors on the tax compliance decisions of taxpayers is widely discussed in the tax literature (Hasseldine et al., 2007; Marshall et al., 1998; Roth et al., 1989; Sakurai & Braithwaite, 2003; Torgler, 2005). Hite and McGill (1992) suggest that small businesses need tax advisors because they want assurance that they are correctly fulfilling their tax obligations. Additionally, they found that small business owners

6 8 5 ,

> Nobody changes an accountant (CPA) because of his poor service. Change can only be exceptional as a result of a major mistake or very big harm that is caused to the company. I did not seek a high quality accountant when I started my company. I asked my trusted friends' reference about their accountants. It [decision to employ an accountant] must be made through advice or reference otherwise it will not work. Because he will know everything about you; your system, off-record activities, everything! (Participant 15)

It is clear that the trust factor creates interdependency between SMEs and tax advisors, leading to long-standing relationships. Considering the fact that CPAs are not mutually responsible for the company's tax penalties, the possible risk of sharing knowledge about a company's activities with third parties might be one reason for these long-standing relationships. In addition, it appears that tax advisors who were ex-civil servants (experts or inspectors) in TRAD established trust and confidence with SME owner-managers more than other tax advisors. Two participants highlighted that CPAs with former civil servant experience are preferable because they know the 'inner circle' of tax offices better than others.

However, three participants admitted they could not develop a trustworthy relationship with their CPAs. Although they are not the majority in the sample, motives of mistrust were associated with negative experiences of former CPAs and their disorganised services. Therefore, these participants indicated that they are hesitant to follow the advice of their CPAs, although they encourage them to comply with the tax system. On the other hand, participants who trust their CPAs said they are inclined to follow their accountant's advice even if it involves paying more tax.

> My accountant (CPA) is an old fox. He smells the air better than me especially when it comes to tax. (Participant 12)

> He [his CPA] asked me to apply for the 2011 tax amnesty.[3] Initially I thought there was no need to apply for it and pay more taxes. However, I decided that he had a better understanding of the tax office. Therefore, I applied and paid an additional eleven thousand liras just to avoid the risk of facing a tax penalty. (Participant 16)

Participants were asked about their tax advisors' intermediary position in tax compliance in order to understand their positions between small firms and the state. Interview analysis revealed that tax advisors adopted one of three positions of client advocacy, namely: predominantly advocating for the client, acting as an advocate for the government/state, or maintaining a neutral position. Among these groups, the CPAs taking a neutral intermediary stance appeared to be more common than those who favoured either side of the tax compliance relationship. Eleven participants agreed that their CPAs do not provide aggressive tax planning or advice on over-compliance. Five participants complained that their tax advisors usually favour the state and even consider over-compliance to avoid possible inspections or inconvenient interactions with the tax office. These participants suggested possible the reasons for

Apart from tax advisors, some participants also sought advice from trusted colleagues who were generally older and more experienced. This advice tended to be more concerned with processes and relationships rather than tax legislation or technicalities.

Overall, the analysis suggests that the influence of a tax advisor on tax compliance decisions has several different dimensions such as trust and the capability of CPAs to influence a tax bill. Certainly, there is clear evidence of the effect of tax advisors on tax compliance of SMEs.

4.4 Company structure

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4.5 Size of economic obligation

Taxes are economic obligations and consequently the tax burden that taxpayers face has been the subject of many studies (Andreoni et al., 1998; Roth et al., 1989). The literature is unanimous that the perceived size of tax burden significantly affects tax compliance and tax morale (Andreoni et al., 1998; Bernasconi et al., 2014; Kirchler, 2007; Strümpel, 1966; Tanzi & Shome, 1993). Torgler (2007) documented a negative correlation between the size of economic obligation and voluntary tax compliance.

Fifteen participants reported that tax burdens were high for their companies. Six participants even admitted that the scale of their tax burden forced them to investigate tax avoidance/evasion possibilities in the last year.

> Our bigger shareholder is the state. He takes his share regardless of what we earn. He does not care whether you actually earn any money or you actually sell anything. The only thing he cares [about] is his slice (share) in my cake. (Participant 17)

> I paid more [taxes] than I earned last year. You might think [do] how I compensate [for] the difference. I accepted the fact that I have to work for my company within the working hours, I have to work at evenings, and Saturdays for [the] state only. That is how I managed it. (Participant 19)

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them from complying with their tax obligations. Consequently, a majority of participants suggest that the perceived size of their economic obligation influences their tax morale.

4.6 Risk aversion

SME risk aversion is considered a factor that shapes corporate behaviour towards voluntary tax compliance and tax morale. In the early literature, risk aversion was viewed as an influential factor of tax compliance—defined as the probability of being caught under-reporting income (Allingham & Sandmo, 1972). Related concepts include audit probability (Cronshaw & Alm, 1995) and the probability of detection (Andreoni, 1996). In this research, participants were asked about their risk aversion to understand their prediction of the possibility of a tax inspection of their companies. Moreover, their understanding of the inspection process was also

Five participants mentioned that they agreed to increase their declared tax to reduce their inspection probability because their tax advisors advised them to do so even when they made a loss during the declaration period.

> Even if our profit decreased, we tend to keep our ta

from the new perspective of professionalism if the benefits of

Overall, the findings of this study provide a basis for future research. This study investigates the corporate factors of tax morale using a qualitative approach, and is valuable for documenting evidence of the six factors in a relatively unexplored area of tax research. Further research might explore any or all of these factors in more detail. In addition, we hope this study will be followed by a more extensive survey-based empirical study. The results of a large-scale survey of Turkish (or other countries') SME owner-managers on this topic would provide a 'baseline' which could then act as a benchmark for future studies, and even potentially be used in international comparisons, which might provide useful evidence for governments' tax and business policies.

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7. APPENDICES

Appendix 1: Interview Protocol

Thank you for agreeing to be interviewed. I am carrying out a number of interviews to understand tax morale effect on taxpaying (compliance behaviour). I have a number of questions to ask you that will generally take 45 to 60 minutes. Please feel free to just talk. If you are comfortable, I would like to record the interview, so that I can concentrate on listening to you and asking questions rather than taking notes. Your talk records (Voice or Type) will be kept anonymous and will be treated under protection of *Data Protection Act 1998* and Turkish *Data Protection Act 2007*. This is also a requirement of the University of Nottingham Code of Research Conduct and Research Ethics. Some quotes may be used, but these will not be attributable to you. My contact details will be provided after interview. Please indicate if you need any clarification for the process.

Are you happy for me to do the interview?

Demographics:

1. Could you please tell us about yourself?

2. What kind of business are you in and how long have you been in the business?

Corporate Behaviour:

1. Could you please tell me about your business in general?

2. Could you please tell me what is like to be a small business operator in Turkey?

3. Do you think that SMEs should be favoured by state? Why?

4. Can you define your company as a professional one? Why?

5. Do you think that are you going to be inspected in next three years?

6. How do you think that inspection probability is effecting your tax compliance decision?

7. Have you ever inspected or received tax penalty?

8. Do you think that you will receive a fine if you have an inspection? Or inspector can find anything from your book which can be counted as evasion?

9. Do you trust your tax advisor?

10. How long have you been working with your current tax advisor?

11. Have you ever experienced problems on tax issues with your accountant as result of miscommunication?

12. Do you think better quality tax advice will reduce your tax bill?

13. Do you believe that your accountant may increase or decrease you tax bill, if desired?

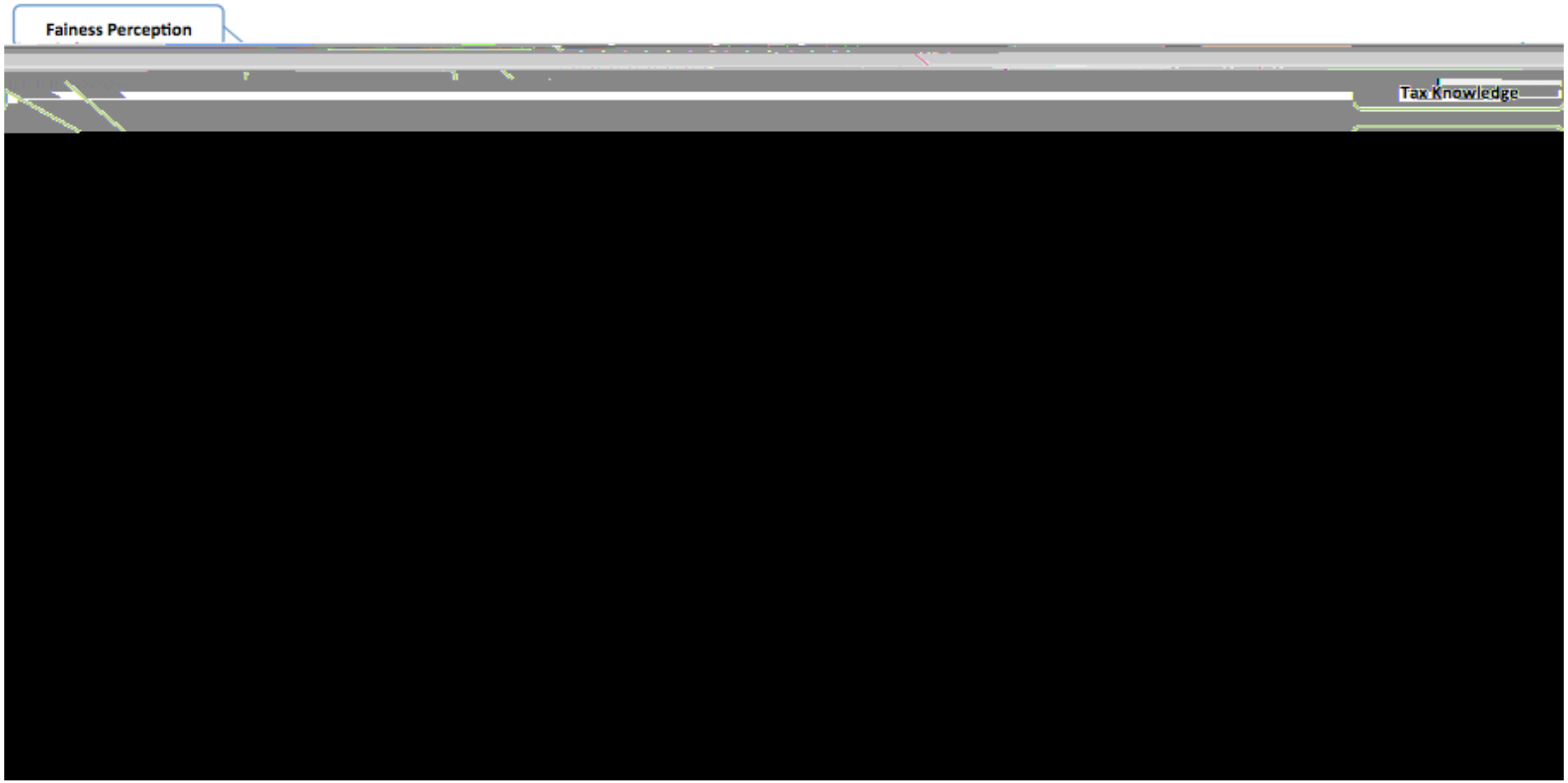
Appendix 2: Interview Participants

Interviewee number	Sector	Experience in sector (years)	Education status	Interview length
1	Automotive	11	University	00:56:17
2	Machinery	23	High School	01:15:29
3	Metal	16	University	00:36:11
4	Construction	11	University	01:09:20
5	Metal	13	High School	01:10:55
6	Publishing	17	University	00:47:20
7	Retailer	3	University	00:48:22
8	Construction	9	Masters	01:00:50
9	Metal	4	University	00:48:30
10	Furniture	20	High School	01:12:16
11	Textile	6	High School	01:17:39
12	Metal	16	University	01:31:33
13	Catering	34	Masters	01:11:58
14	Law	8	Master	01:13:01
15	Services	2	University	01:01:00
16	Textile	23	Masters	01:02:11
17	Textile	30	University	01:14:24
18	Services	6	High School	00:59:18
19	Publishing	17	High School	01:10:00
20	Construction	21	High School	01:25:38
				21:52:12

Appendix 3: Current Tax Advisors of the Participants

Interviewee Number	Sector	Experience in sector (years)	Trust in accountant	Years with current CPA	Sworn-in CPA
1	Automotive	11	Yes	From start	No
2	Machinery	23	Yes	10	No
3	Metal	16	Yes	From	

Appendix 4: Model of Tax Morale of the SME and its Determinants



Source: Yucedogru, 2013