

TAX COMPLIANCE COSTS OF BUMIPUTERA SMALL AND MEDIUM ENTERPRISES IN NORTHERN MALAYSIA

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ABSTRACT

This paper explores and measures the level of tax compliance costs among Bumiputera small and medium enterprises in the Northern Region of Malaysia for the year of assessment 2003. The findings revealed that the tax compliance costs have a significant relationship with the paid up capital (size of enterprises). Overall, the tax compliance cost of Bumiputera small and medium enterprises was RM880,110 for the assessment year 2003. Furthermore tax compliance cost of smaller Bumiputera enterprises amounted to RM413,670 while the larger Bumiputera enterprises was RM466,440. The average tax compliance cost is RM22,003. Most of the large Bumiputera enterprises incurred more external tax compliance costs than internal compliance costs (62.34%) compared to the smaller Bumiputera enterprises (37.66%). In contrast, the smaller Bumiputera enterprises incurred more internal tax compliance costs of about 83% as compared to external tax compliance costs (17%). The results also indicated that small Bumiputera enterprises have a higher percentage of tax compliance costs based on tax revenue, which is 2.57 times more compared to large Bumiputera enterprises, which amounted to only 0.46 times.

ABSTRAK

Kajian ini mengumpul dan mengukur tahap kos pematuhan dalam kalangan Industri Kecil dan Sederhana (IKS) Bumiputera dalam kawasan utara Malaysia untuk tahun taksiran 2003. Hasil kajian menunjukkan bahawa kos pematuhan cukai mempunyai hubungan yang signifikan dengan modal

berbayar (saiz perniagaan). Pada keseluruhannya, kos pematuhan IKS Bumiputera adalah RM880,110 untuk tahun taksiran 2003. Di samping itu kos pematuhan IKS Bumiputera yang kecil ialah RM413,670 dan IKS Bumiputera yang besar ialah RM466,440. Purata kos pematuhan cukai ialah RM22,003. Kebanyakan IKS Bumiputra yang besar mengalami lebih kos pematuhan luaran daripada kos pematuhan dalaman (62.34%) berbanding dengan IKS Bumiputera yang kecil (37.66%). Sebaliknya, IKS Bumiputera yang kecil mengalami lebih kos pematuhan dalaman iaitu sebanyak 83% berbanding dengan kos pematuhan luaran (17%). Hasil kajian juga menunjukkan bahawa IKS Bumiputera yang kecil mempunyai peratusan kos pematuhan cukai yang tinggi berdasarkan hasil cukai iaitu 2.57 kali lebih berbanding dengan IKS Bumiputera yang besar iaitu sebanyak 0.46 kali sahaja.

INTRODUCTION

In today's global economic system, taxation plays an important role in the country's development. It is significant not only for the developed countries, but also the developing countries. In all countries, tax revenue forms a major component of the total revenue and its efficient collection is very important. In Malaysia, the contribution of tax revenue for the year 2004 was RM72,050 million as compared to RM64,891 million in the year 2003, which represented an increase of 11%. Tax revenue continued to increase by 8.73% for the year 2005 to RM 80.6 million (Malaysia Ministry of Finance, 2003-2006). Tax revenue is projected to rise by 9% to RM 87.9 billion in 2006 with direct taxes accounting for 51.9% of the total revenue (Budget 2006).

Although tax collection shows an upward trend for the past decade, the taxpayers nevertheless should not be burdened with extra compliance costs. An increase in tax compliance costs could also come from the complexity of the tax system itself (Ariff & Pope, 2002). Changes in the Malaysian tax system from Official Assessment System (OAS) to Self Assessment System (SAS) as announced in the 1999 budget announcement has resulted in an increase in the tax compliance costs of taxpayers.

According to Sandford (1990) self-assessment system would lead to evasion, and evidence also show that self-assessment would lead to higher tax compliance costs. Many studies have been conducted in various countries on tax compliance costs. For instance studies done by Vaillancourt (1989); Blumenthal and Slemrod (1992); Sandford and Hasseldine (1992); Pope and Chen (1993); Pope, Fayle, and Chen,

(1991); Ariff, Loh, and Talib, (1995); Loh, Ariff, Ismail, Shamser, and Ali, (1997); Rametse and Pope, (2001); and Slemrod and Blumenthal (1996) are studies on tax compliance costs. A number of studies on tax compliance costs have also been conducted in Malaysia. Loh *et al.* (1997) carried out a study on listed companies on Kuala Lumpur Stock Exchange (KLSE) while Mustafa, Ariff, and Jeyapalan (2001) had undertaken a study on small and medium size enterprises (SMEs). Loh *et al.* (1997) was the first Malaysian study on tax compliance costs. They suggested a number of ways how the government could keep the costs low and how companies as taxpayers could manage tax compliance costs.

Implementing the self-assessment system in Malaysia (SAS) has also increased the taxpayers' burden. This extra burden in the form of tax compliance cost may not be a problem to big enterprises, but for small and medium-scale taxpayers it poses a heavy burden. Tax compliance costs could impose tremendous financial pressure on SMEs. As such, this study investigated compliance costs of Bumiputera SMEs in Malaysia. Perceptions of the Bumiputera entrepreneurs on whether compliance cost is a burden are also investigated and discussed in this paper.

Why Study Bumiputera Small and Medium Enterprises?

Tax compliance costs are unavoidable. Previous studies have justified that small-sized taxpayers incur higher tax compliance costs rather than large-sized taxpayers. Slemrod and Blumenthal (1996) suggested that corporate compliance costs among corporate taxpayers are lower than individual income taxpayers in the United States. Blazic (2002) found that the compliance costs of personal income tax (31.39%) are higher than companies' compliance costs (19.31%) in Croatia for year of assessment 2001/2002.

This study is important because currently there is a lack of tax compliance cost studies in Malaysia and none on Bumiputera SMES. Bumiputera's involvement in business is still low and has yet to achieve the 30% equity target outlined in the New Economy Policy (NEP). Moreover, the selection of Bumiputera rather than non-Bumiputera SMEs is because their business and tax knowledge and awareness are still relatively low.

Definitions

Tax Compliance Costs: Tax compliance costs are costs incurred by a taxpayer in addition to the tax payable to the government. According

to Ariff and Pope (2002), tax compliance costs are costs incurred in confirming with the mandatory requirements of a tax regime involving the preparation and submission of timely tax returns in accordance with the relevant tax laws of a country at a given time.

Source of Tax Compliance Costs: Source of tax compliance costs could be categorised into external and internal tax compliance costs.

External Tax Compliance Costs: Ariff and Pope (2002) described external tax compliance costs as payments to acquire the service of lawyers, accountants, tax agents or other advisers from outside the business. These external costs are normally measured in monetary terms. External costs are more easily recognisable and quantifiable.

Internal Tax Compliance Costs: Internal costs are incurred internally inside the business and cover such costs as staff and miscellaneous costs. These compliance costs can be measured via monetary and time spent. Staff costs consist of costs related to accounting/bookkeeping, computer, legal, secretarial, directors/management, and other costs. Internal costs arise from time costs spent by staff of company on maintaining and preparing information for professional advisers, completing tax reforms, and dealing with revenue authorities on matter pertaining to inquiries, objections, and appeals (Mustafa *et al.* 2001).

Bumiputera Small and Medium Enterprises: Bumiputera enterprises refer to Malay owned enterprises in Malaysia. There are many definitions on SMEs in Malaysia, which are normally categorised according to the number of employees, paid-up capital, amount of assets and turnover. According to the Ministry of International Trade and Industries (MITI) (1999), SMEs are defined as “*companies with employees not exceeding 150 with an annual sales turnover not exceeding Malaysia Ringgit (RM) 250 million*”. This study adopts the definition used by the Small and Medium-Sized Industry Development Corporation (SMIDEC). SMIDEC (2004) has classified SMEs into two groups; manufacturing or manufacturing-related services and agro-based industries, and the other group as services, primary agriculture, and information and communication technology (ICT).

Small manufacturing-related enterprises are “*companies with sales turnover between RM250,000 and less than RM10 million or having full time*

employees between 5 and 50". On the other hand, small services, primary agriculture, and ICT enterprises are with sales turnover between RM200,000 and less than RM1 million or having full time employees between 5 and 19. Medium manufacturing or manufacturing-related service and agro-based industries are "companies with sales turnover between RM10 million and RM25 million or having full time employees between 51 and 150". Meanwhile, medium service companies are primarily agriculture and ICT enterprises and "companies with sales turnover between RM1 million and RM5 million or full time employees between 20 and 50".

REVIEW OF LITERATURE

Bumiputera Small and Medium Enterprises

The growth of small and medium enterprises (SMEs) in developing economies shows an increasing trend. According to Rusmawati (2000), about 99% of Canada and United Kingdom's economy is sourced from SMEs, whereas in South Korea and in Japan it is about 99.3% and 99.4% respectively. Khairuddin (2002) suggested that the SME sector in Malaysia should play a significant role in the national economy. According to Eighth Malaysia Plan 2001-2005, (Economic Planning Unit 2001) there were about 97,500 Bumiputera enterprises listed under the Registrar of Companies until 1999, as compared to 67,700 enterprises in 1995. In addition, 70% of Bumiputera enterprises are small with paid-up capital of RM100,000 and below.

The Ministry of Trade and Industry (MITI) is also concerned about SME contribution to the national economic growth. SME contribution was RM4.3 billion or 20% of the Gross Domestic Production (GDP) in 1991, and this is expected to increase to 50% in 2020. Under the Malaysian plans, the government has put more effort in promoting and assisting the SME sector. One of the main objectives is to encourage the SME sector growth and to develop Bumiputera entrepreneurship.

The government supports the growth of SMEs and the Bumiputera in particular from every aspect since the First Malaysia Plan. The government is also committed to reduce the cost of doing business by the SMEs. In the National Budget 2005, the government has given more incentives for the development of SMEs. The Budget has outlined several soft loans and matching grants for SMEs in order to increase their technological capabilities. Various tax incentives are also made available by the government for SMEs in Malaysia.

Small and Medium Enterprises (SMEs) and Tax Compliance Costs

A number of studies have been carried out to measure tax compliance costs incurred by taxpayers that include corporate and individual taxpayers and others. According to Ariff and Pope (2002), compliance costs in the United States (US) are ever increasing and over the next few years it is expected to increase from US\$140 billion in 2001 to US\$170 billion in 2006. Furthermore in 2001, this cost amounted to nearly 12% of all income tax revenue collected.

In the Asia-Pacific region there are several studies on tax compliance costs that have been carried out, e.g. in Malaysia (Mustafa *et al.* 2001, Loh *et al.* 1997), Hong Kong (Cheung, Chan, & Ariff, 1999), Singapore (Ariff *et al.* 1995), India (Das-Gupta, 2003), and others. Cheung *et al.* (1999) found that the average tax compliance costs of corporate taxation (public listed companies) are high in Hong Kong (overall mean is US\$1.26 per US\$1,000 of sales) compared with those in Singapore and Australia. Ariff *et al.* (1995) found that mean compliance cost estimate was over S\$78,396 (RM172,417) for Singapore public listed companies. However, average compliance costs incurred by public listed companies in Malaysia were estimated per company to be RM68,836. Additionally, there were a number of studies that found that tax compliance costs are influenced by a number of factors. The dominant factor affecting the level of tax compliance costs (either the level of tax compliance costs increases or decreases) is the tax system itself.

Chattopadhyay and Das-Gupta (2002) indicated that tax simplification can lead to lower or higher compliance costs. According to Gandhi (1996), the complexity of tax system has resulted in frustrating and burdensome experiences to taxpayers; for example complexity of the forms and publications and the lack of clarity of correspondence, variety of rigid penalties to promote tax compliance, and changes in tax requirements and regulations. Furthermore Small Business Project (SBP) (2003) suggested that the stability in the tax system itself is a good way to avoid increasing compliance costs.

A study on the determinants of personal income tax compliance costs by Chattopadhyay and Das-Gupta (2002) found that gross income and type of occupation besides tax reform influence the level of tax compliance costs. Most of the studies have identified size of business (measured by annual turnover) to have a significant impact on tax compliance costs (Erard, 1997; Haughton, 1998; Pillai, 2000, Mustafa *et al.*, 2001; Rametse & Pope, 2001; Das-Gupta, 2003. Nevertheless the

type of industry has been used in many studies to measure the level of tax compliance costs (Ariff *et al.*, 1995; Erard, 1997; Cheung *et al.*, 1999; Mustafa *et al.*, 2001).

Several studies have found tax compliance costs of business to be influenced by the appointment or engagement of an external tax advisor (professional fees) (Johns, Dunlop, & Sheehan, 1983); (Erard, 1997; Rametse & Pope, 2001; Ariff & Pope, 2002). According to Johns, *et al.* (1983), about 90% of small businesses have used outside advisors or assistance to deal with taxation problems. Pillai (2000) suggested that small traders could reduce the tax compliance costs if they do not rely heavily on professional advice.

Tax compliance costs are a serious threat to the growth and survival of the small and medium enterprises compared to large companies. Sandford, Godwin, and Hardwick (1989) found that large firms had negative net tax compliance costs and the medium and small firms had positive net costs, which were proportionately heavier for the smaller firms. On the other hand, total tax burden upon a business enterprise should consider not only the actual amount of money transferred to the taxing authorities, but also the costs incurred by the firm in determining and discharging its tax liability. Besides the above studies, very few studies have measured tax compliance costs of small medium enterprises (SMEs) (Erard, 1997; Mustafa *et al.*, 2001; Rametse & Pope, 2001). Tax compliance costs are not only undesirable but also a disadvantage to small firms.

According to Sandford (1990), tax compliance costs for small traders in UK started to rise in the mid 1980s. This was because of heavier penalties imposed by revenue authorities on small businesses for not complying with tax regulations. They also found average tax compliance costs of SMEs to be high and compliance costs increased with decreasing firm size. Erard (1997) advocated tax compliance costs are substantially high among SMEs.

SMEs do not spend more on the external advice as compared to listed companies, but rather rely on their own staff to comply with the tax laws (Mustafa, *et al.*, 2001). According to Erard (1997) the vast majority of SMEs rely on outside professional assistance to comply with their corporate income and capital taxes. Even though there are some dissimilar views on the compliance costs especially regarding the composition of internal and external compliance costs, in Malaysia, SMEs incur higher tax compliance costs compared to public listed companies (Mustafa *et al.*, 2001).

RESEARCH METHOD

The Malaysian Entrepreneur Directory, Bumiputera Special Edition 2002 was used to select the sample size. As the research is concerned about Bumiputera enterprises, this directory is most suitable in fulfilling the research requirements. Data for this research was collected by a structured questionnaire. Most of the questions were open-ended and a few close-ended. The questionnaire was divided into four parts.

Part 1 consisted of "General Information", which covered the sector of the enterprises, business activities, location of premise, paid-up capital, number of people employed by the enterprise, turnover, as well the tax liability paid for the assessment year of 2003.

Part 2 asked questions about "External Costs", in other words information about external costs which covered questions on the hiring of external advisors including fees paid and time spent in handling taxation matters.

Part 3 contained questions about "Internal Costs" containing questions on the number of internal staff involved on tax matters, time spent, and salary paid on tax matters to managers, accountants, accounting staff, and computer officials. This part gathered information on tax return preparation work, tax advice, and tax planning carried out by the internal staff. Also included were questions on internal non-labour costs, which specifically asked about the type of accounting software used in managing tax matters and costs incurred for installing such systems.

Finally, Part 4 "Other matters" asked questions whether the tax compliance costs are a burden to the enterprises. This is important in order to find out the level of consciousness of enterprises as a taxpayer on costs incurred in order to comply with tax laws. This part also assessed the enterprises' perceptions on external tax compliance costs under the Self Assessment System (SAS), and the managers' perceptions on the determinants of tax compliance costs. The determinants were business size, business type, business location, and reputation of external advisors.

Study Sample: Based on the Directory, there were 107 Bumiputera SMEs listed in the Northern Region of Peninsular Malaysia (Kedah, Perak, Perlis, and Pulau Pinang) excluding sole-proprietorships and

partnerships. From this population, 86 were selected as respondents. Out of that, a total of 40 Bumiputera SMEs responded to the questionnaires, which was a 46.51% response rate.

Data Collection: Data for this research was collected through a structured questionnaire, which was adopted from other studies. Every effort was undertaken to ensure that the questions were simple and easily understood. Jargon and technical terms were avoided to the best possible level so that respondents would be able to provide accurate answers.

Pilot Study: A pilot study was conducted a month before the actual field study on 44 Bumiputera enterprises located in Kedah (20), Perak (10), Perlis (4), and Pulau Pinang (10). These enterprises were excluded from the final study. As for validity, tax professional views were gathered in designing the questionnaires (face validity). Every step was taken to ensure that the final survey instrument was clearly understood by the respondents.

Data Analysis Techniques:

Data Analysis: Besides descriptive analysis, this study also employed regression analysis. Regression analysis was utilised in regressing tax compliance costs on company size determined by paid up capital values. Mustafa *et al.* (2001), Pope *et al.* (1991), and Ismail, Loh, and Ariff (1996) found that the tax compliance costs were higher for large firms, though tax compliance costs per unit of revenue declined as firm size decreased due to the economy of scale effect.

To avoid measurement problems arising from possible non-normality of paid-up capital and cost variables, the variables were transformed into natural logarithmic numbers before regressing them. Thus, the formula used was:

$$\ln (CC_i) = a + b \ln (\text{PAIDUPCAP}_i) + e_i$$

Where

- | | |
|----------------------------|---|
| $\ln (CC_i)$ | = natural log of compliance costs of |
| enterprises i | = 1,...,N |
| a | = intercept of the equation |
| b | = regression coefficient |
| $\ln (\text{PAIDUPCAP}_i)$ | = natural log of paid up capital, in local
currency, of Bumiputera SMEs, |
| e_i | = the residuals in the regression |

Table 1
Profiles of Respondent of Mail Questionnaire Survey in Northern
Region Malaysia

Characteristics	Number of enterprise
(a) Turnover	
Less than RM25,000	18
RM25,000 - RM75,000	8
More than RM75,001	14
(b) Paid Up Capital	
Group 1: RM500,000 and less	29
Group 2: RM500,001 - RM2,500,000	11
(c) Sector of Business	
Construction	4
Manufacturing	11
Service	25
(d) Main Business Activity	
Construction and property development	1
Commerce/ Trading	13
Computer/ IT	2
Engineering	5
Financial, Insurance and Business Service	3
Manufacturing	3
Transport/ Storage	10
Others	
(e) Respondents Based on State	
Kedah / Perlis	5
Perak	3
Pulau Pinang	32
(f) Tax Liability	
Less than RM10,000	15
RM10,000 - RM100,000	11
More than RM100,000	3

Research Findings

Table 1 shows turnover of the Bumiputera SMEs ranging from less than RM25,000 to more than RM75,001. A total number of 18 enterprises have sales turnover of less than RM25,000 while eight enterprises have turnover between RM25,000 and RM75,000, and another 14 enterprises

with more than RM75,001. About 29 enterprises have paid-up capital of RM500,000 and less, while 11 enterprises have paid-up capital of between RM500,001 and RM2,500,000. Most of the enterprises came from the service sector (25), manufacturing (11), and construction (4). Table 1 also summarises the activities of the respective enterprises. The business activities were commerce or trading (13), followed by engineering (5), financial and business services (3), manufacturing (3), transport or storage (3), computer or IT (2), and only one was involved in construction and property development activity.

As the study was carried out in the Northern Region of Malaysia, the majority of Bumiputera SMEs were located in Pulau Pinang (32), five from Kedah/Perlis, and three from Perak. Furthermore, as shown in Table 1, the tax liability of the respondents ranged from less than RM10,000 to more than RM100,000 and RM500,000 was the highest amount paid by one respondent. About 15 enterprises paid less than RM10,000 followed by 11 enterprises paying between RM10,000 and RM100,000. The remaining three enterprises had tax liability exceeding more than RM100,000, and two were from the manufacturing sector followed by construction (1).

Table 2
RM Tax Compliance Costs Per RM 1,000 Paid -Up Capital

Group	Year of Assessment 2003 (RM)
1	413,670 (0.47)
2	466,440 (0.53)
Average	22,003

Table 2 shows the average tax compliance costs of the Bumiputera SMEs. The companies were divided into two groups (Group 1 and Group 2), based on paid-up capital of the SMEs. The grouping was done to facilitate comparison of tax compliance costs across group sizes. Group 1 comprised companies with paid-up capital of RM500,000 and less, while Group 2 consisted of companies with a paid-up capital of between RM500,001 to RM2,500,000.

Companies in Group 2 incurred higher tax compliance costs. This was expected, as companies in Group 2 were larger than in Group 1. The average tax compliance costs per RM1,000 paid up capital for SMEs

in Mustafa, *et al.* (2001) was RM22,003. The average tax compliance costs per unit of paid-up capital value for Group 1 was 47 times (RM413,670), and Group 2 was 53 times (RM466,440). The findings support the regressive nature of the tax compliance costs.

Table 3
Regression on Tax Compliance Costs on Paid-Up Capital of Enterprises

Independent variable	B	t	Significance
Paid-up capital	0.664	5.479	0.000*

N = 40
R-Square = 44.1%
F-Value = 30.023
Sig. F = 0.000*

* Significant probability level (p) < 0.01

The findings also revealed that paid-up capital has a significant relationship with the level of tax compliance cost. Table 3 shows that Bumiputra SME compliance costs are directly related to the paid-up capital of the enterprises. The R-square value of the regression was 0.441 or 44.1% with a F-value of 30.023, which is statically significant at 0.01 (R-square = 0.441, F-value = 30.023).

Sources of Tax Compliance Costs

The total tax compliance costs of Bumiputera SMEs was RM880,110 (Table 4). Table 4 shows the results of tax compliance costs based on the source and size of the enterprise.

Group 1 internal cost amounted to RM343,170 (83%) and external costs were RM70,500 (17%). Internal costs of Group 2 amounted to RM349,740 (75%) and external costs were RM116,700 (25%). This showed that the external costs of Group 1 contributed only 37.66% compared to Group 2, which constituted about 62.34% of the total external tax compliance costs.

The study also identified and measured the external tax compliance costs of Bumiputera SMEs in terms of monetary, amount of time spent, and fees paid to tax professionals. According to Mustafa, *et al.* (2001), external advisors were sought by the SMEs because

technical knowledge particularly in specialised areas were not readily available within the firm, and also because it was more cost-effective. This study's findings indicated that 80% of the Bumiputera SMEs employed external advisors to assist in their tax related matters (see Table 5). However, eight Bumiputera SMEs or 20% of the total sample did not respond to this question.

Table 4
Breakdown of Tax Compliance Costs by Sources of
Costs [(%) of Compliance Costs]

Groups	Internal costs (RM)	External costs (RM)	Total compliance costs (RM)
1	343,170 (83.0%)	70,500 (17.0%)	413,670 (100%)
2	349,740 (75.0%)	116,700 (25.0%)	466,440 (100%)
Total	692,910	187,200	880,110
Average	17,323	4,680	22,003

External Tax Compliance Costs

Table 5
Percentage of Employment of the External Advisor

External advisor	Frequency	Percentage (%)
Yes	32	80
Total	32	80

The results indicated that large Bumiputera enterprises are more likely to employ external advisors to manage their tax matters. Additionally, 59.38% of the Bumiputera SMEs stated that the external advisors were responsible for the tax computation and tax advice, especially on routine tax matters. The remaining (40.62%) indicated that their tax advisors are also responsible for tax planning in addition to tax advice, and tax computation. However, the role of tax advisors in tax planning is not common among small firms, as only 28.57% sought the external advisors advice on tax matters.

In contrast, the majority (63.64%) of the large Bumiputera enterprises made use of external advisors for tax advice, computation, and tax

planning. This shows that tax planning is given more attention by the large Bumiputera enterprises as compared to the small Bumiputera enterprises. Hiring tax professionals would nevertheless increase the compliance costs of the companies.

Furthermore, Mustafa *et al.* (2001) revealed that the smaller companies spent less on tax planning activities. Loh *et al.* (1997) also found that large companies on average spent 10 times more resources on tax planning than smaller companies. This is due to the complex nature of the business activities of large companies with more diversified investment opportunities financing pattern, which require special tax considerations.

This study's findings revealed that 80% of the Bumiputera SMEs employed external advisors, and all the enterprises employed professional accountants/tax agents to handle their 2003 tax affairs. In Malaysia, the professional accountants/tax agents could be divided into two categories, that is the Big Four accounting firms (Ernst & Young, Price Waterhouse Coopers (PWC), Klynveld Peat Marwick Goerdeler (KPMG), and Deloitte KasimChan) and Non-Big Four accounting firms, which comprises small and medium local professional accountants/tax agents.

In the northern region of Peninsular Malaysia, there are about nine Big Four accounting firms located in these states. Ernst & Young (3) has the highest number of premises, one in Perak, Pulau Pinang, and Kedah respectively. Deloitte KasimChan (2), KPMG (2), and PWC (2) have one premises each in Perak and Pulau Pinang respectively. None of the Big Four's premises is located in Perlis. From the 32 Bumiputera SMEs that employed professional accountant/tax agents, only 3.12% appointed the Big Four as external advisors. Only the large Bumiputera enterprises hired the Big Four accounting firms, but the rest (96.88%) appointed Non-Big Four accounting firms as external advisors. The majority of Bumiputera SMEs were inclined to appoint the Non-Big Four external advisors or local firms due to lower charges and professional fees.

The big Bumiputera enterprises employed the Big Four as their external advisors, which could be attributed to the complexity of the nature of the business. These big enterprises need tax experts to manage their financial and tax matters to solve various complex business issues. It also indicates that Bumiputera SMEs rely on the Non-Big Four external advisor or local firms where their fees range from RM250 to RM7,000 for the year of assessment 2003. This is consistent with Tran-Nam (1999) that most of the small enterprises rely on the services of a local accountant whose rates are more reasonable.

In addition, smaller Bumiputera enterprises have more frequent meetings with their external advisors regarding tax matters as compared to the larger Bumiputera enterprises. Even though the structure of the smaller Bumiputera enterprises is not too complex, their lack of tax knowledge may be the reason why they have frequent meetings with the external advisors. The meeting normally takes place during the opening and closing accounting dates, and also before the tax return submission date to the Malaysian Inland Revenue Board (IRB). Most of the Bumiputera SMEs meet their external advisor less than five times per year (65.63%) and their time spent is less than one and a half hours per visit. This constitutes 75.0% of their meeting time per year. In a year, these Bumiputera SMEs spend about 9,855 minutes or 124 hours and 25 minutes with their tax advisors for tax matters.

Although the external costs normally refer to the payment to the external advisors, but other costs could be incurred, for instance telephone calls to the external advisor and other incidental costs. As compliance cost is defined as hidden costs, most of the enterprises do not realise that these costs could create extra burden to them. It was found that the smaller Bumiputera enterprises make telephone calls more frequently than the large Bumiputra SMEs. This constitutes about 60.34% of total minutes per year as compared to the large Bumiputera enterprises, which only represents 39.66% from the total 3,817 minutes per year.

Small Bumiputera enterprises spent almost RM113.56 for calling the external advisors as compared to large Bumiputera enterprises, with only RM71.52. This amount is considered large as compared to the enterprise's size. Again the reason for more frequent calls is due to the lack of knowledge and expertise regarding tax matters among the small-sized enterprises.

Internal Tax Compliance Costs

This study also identified and measured the internal tax compliance costs of Bumiputera small and medium enterprises. The internal tax compliance costs comprised internal labour costs and internal non-labour costs. Findings of both types of costs are discussed below.

Internal Labour Costs

Based on the findings, it showed that there are at least four categories of staff involved in tax matters. They include the managers, accountants, accounting staff, and clerks. Even though 28 managers or about 50% deal with tax matters, their time spent is only between 15% and 78%.

The breakdown of time spent by the staff shows that the accountant's involvement in tax matters is more, which is between 60% and 85%. This is similar to Blazic's study (2002) findings whereby managers are more inclined not to engage in taxes but to leave the tasks to other highly qualified and experienced accounting staff.

Most of the Bumiputera small enterprises rely on their managers, accounting staff, and clerks to file their tax returns because they perceived that an accountant is not necessary since the nature of the business is not too complex or too big. On the contrary, large Bumiputera enterprises employ full-time accountants to do tax and accounting work. The total hours spent were 123,648 hours and about 48.08% of the total working hours was spent on tax matters (see Table 6). The small Bumiputera enterprises spent more time on the internal staff (57.28%) compared to the large Bumiputera enterprises (42.72%). This result is consistent with Mustafa, et al. (2001). Their findings indicated that as size of the enterprise decreases, internal costs would increase.

The involvement of managers in managing tax matters is small in large companies and this finding is similar to Blazic (2002). The manager's involvement in taxes may range from doing all/part of the tax work on their own or simply cooperating with others. Furthermore the findings indicated that the time spent by accounting staff (34.55%) is higher than the managers (16.95%) and clerks (10.44%) for the large Bumiputera enterprises.

The result indicated that accountants play a major role in tax preparation, tax advice and also tax planning for Bumiputera SMEs. Managers are mainly concerned about tax preparation and this finding is consistent with Blazic (2002), where it was revealed that managers are more inclined not to engage in taxes, but left the responsibility to highly qualified and experienced accounting staff. Most of the clerks (17.86%) were involved in the tax preparation, which basically involves data entry, secretarial, and clerical work, and none of them were involved in tax advice and tax planning.

Internal Non-Labour Costs

Ariff and Pope (2002) suggested that internal tax compliance costs should also include cost involved in purchasing computers and taxation software (if any). However in Malaysia, there are not many taxation software readily available in the market. Most of the accounting software are actually indirectly related to the tax matters.

Table 6
Breakdown of Time spent Based on the Position

Groups	Position of staff								Total time spent (Hours)
	Manager		Accountant		Accounting Staff		Clerk		
	No. of staff	Time spent (Hours)	No. of staff	Time spent (Hours)	No. of staff	Time spent (Hours)	No. of staff	Time spent (Hours)	
1	24	22,745 (66.80%)	2	3,312 (9.73%)	3	3,753 (11.02%)	7	4,239 (12.45%)	34,049 (100%)
2	4	4,305 (16.95%)	6	9,716 (38.26%)	7	8,722 (34.35%)	3	2,650 (10.44%)	25,393 (100%)
Total	28	27,050	8	13,028	10	12,475	10	6,889	59,442

According to Sanford *et al.* (1989), even the Organisation for Economic Co-Operation and Development (OECD) study tried to capture costs of software and hardware used but omitted them in the end.

The majority of the Bumiputera SMEs (60%) of the total respondents manage bookkeeping/tax matters manually, where no computerised system is used to produce an effective and efficient bookkeeping/tax management. Only about 40% of the Bumiputera SMEs used a computerised system in order to manage bookkeeping/tax matters internally. The SMEs also preferred to use the low-end software rather than the high-end software. According to Horizon Accounting System (1998), low-end systems are best suited for small companies, with low transaction volumes, and often are the best choice for a business which first uses a computerised system. The low-end accounting software is best suited for companies that have less than \$1 million in annual revenues and fewer than 25 employees.

The small Bumiputera enterprises also rely less on the computerised system in managing their bookkeeping/tax matters. This constitutes about 87.50% of the total companies. This is considered reasonable as the nature of these enterprises is not too complex and involve only small sum of transactions. Tram-Nam and Glover (2000) noted that a variety of different accounting software packages are utilised by SMEs. According to them both Mind Your Own Business (MYOB) software and Quick Book software are the most common.

In the current study, the majority of the Bumiputera SMEs (56.25%) used the Universal Business Solution (UBS) in order to manage the business transactions. Large Bumiputera enterprises also use UBS software, where the cost ranges from RM1,000 to RM25,000. The use of Accounting Plus software is also popular and its price ranges from RM2,500 to RM10,000. Software such as Quick n' Easy and MYOB are more popular with the smaller Bumiputera SMEs. The average cost incurred by the Bumiputera SMEs on tax related software is about RM1,503.

SUMMARY, CONCLUSION AND RECOMMENDATIONS

Since SMEs play a significant role in the development of the Malaysian economy, government authorities should ensure that their growth is not hampered by extra burden such as tax compliance costs. Tax compliance cost is a threat to the SMEs growth and their survival. By focusing on the tax compliance costs of the Bumiputera SMEs,

this study has provided vital information on issues and problems pertaining to tax compliance costs that affect the operations of these enterprises.

The findings indicated that the average tax compliance costs of Bumiputera SMEs is RM22,003 for the year of assessment 2003. The average tax compliance costs of Bumiputera small and medium enterprises are higher than the previous study (RM21,964), which focused on the SMEs as a whole.

Most of the large Bumiputera enterprises also spend more on the external sources, which was 60.41% or RM116,700 as compared to the small Bumiputera enterprises, which constituted about 39.59% or RM70,500. Interestingly, these small Bumiputera enterprises (60.43%) spend more time with the external advisors than the large Bumiputera enterprises. Most of the Bumiputera SMEs do not hire Big Four accounting firms but rather prefer local firms because their fees are lower and they have a good working relationship.

Small Bumiputera enterprises rely more on the internal staff to manage their tax matters, which constituted 83% or about RM343,170 on average as compared to large Bumiputera enterprises, which is only 75% or RM349,740. This is consistent with the previous study done by Mustafa, *et al.* (2001). The managers of small Bumiputera enterprises also handle tax matters besides managing the company's affairs.

However, most of the big Bumiputera enterprises have their own accounting department to manage tax related matters. The time spent by the manager shrinks as the size of the enterprises increases, as accountants and other accounting staff are hired by these enterprises to handle tax work. In general, the tax compliance costs of Bumiputera SMEs are higher than the corporate tax paid to the government. Furthermore, 45% of the respondents agreed that the compliance cost is a burden to them. Finally, it was found that the level of compliance costs is influenced by the size of the business, followed by type of business, the type of external advisors, and also the location.

The findings also indicated that Bumiputera entrepreneurs lack tax knowledge. Entrepreneurs should improve their tax knowledge especially in the new tax environment that has been implemented in Malaysia. It is highly recommended that there must be strong cooperation between the government and the SMEs in ensuring that the tax compliance costs will always remain at a manageable level.

There are a few limitations in this study. Firstly, this research covers only Bumiputera SMEs in the northern region of Peninsular Malaysia. Non-Bumiputera SMEs are not covered in this study, but it is highly recommended that a comparative research should be undertaken in the future. Finally, future studies in tax compliance costs should undertake a nation-wide study among individual taxpayers and also government-owned public listed companies.

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