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MAXIMIZING THE INDONESIAN'S TAX REVENUE FROM MICRO, SMALL, AND MEDIUM ENTERPRISES (MSMES) SECTOR

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ABSTRACT

Micro, Small, and Medium Enterprises (MSMEs) have an essential role in Indonesian's economy. However, the contribution of MSMEs to Indonesian taxation is still far from reaching the maximum point. This research examines the effect of three critical factors on tax compliance among the Micro Enterprises in Indonesia, namely Tax Knowledge, Tax Rate, and Equity and Fairness, by using multiple regression. An online survey was conducted to collect data from 122 respondents in Surabaya and focused on micro-enterprises taxpayers. The result indicates that Tax Knowledge, Tax Rate, Equity and Fairness significantly impact tax compliance among the micro-business taxpayers. Tax Knowledge had the most significant impact on compliance behavior among the taxpayers.

Keywords: *Tax Compliance; Tax Rate; Tax Knowledge; Equity and Fairness; MSME*

INTRODUCTION

Since the 2008 tax reforms in Indonesia, taxpayers rise exponentially from 10,1 million to approximately 42 million in 2019. Unfortunately, the correlation between the number of taxpayers and the tax ratio is negative statistically. In 2016, Indonesia's tax ratio was among the lowest compared to other countries in South-East Asia. Besides, it also lower than OECD's average, LAC, and Africa in 2018. Based on the IMF, Laos, Indonesia, and Myanmar had tax ratios of 12.94%, 10.33%, and 6.41% consecutively, while the rest had managed to reach more than 13% tax ratio. The Directorate General of Taxes (DGT) as tax authority in Indonesia only collected tax revenue around 84.44% of the revenue target around IDR 1.577,56 trillion, which accounted for only IDR 1.332,06 trillion 2019 (The DGT Annual Report, 2020). Unfortunately, the failure of the DGT to maximize the revenue occurs during a decade. Meanwhile, the contribution of taxation increases significantly in the Indonesian Annual Budget (APBN), from 74% in 2014 to 82,5% in 2019. It means that tax revenue plays a significant role in the economic sector in Indonesia.

Indonesian tax authority faces some challenges to maximize the revenue from the taxation sector. The challenges come from both internal and external factors and being driven by the international factor. Decreased commodity prices contribute to low tax revenue. Thus, the tax revenue performance of the oil, gas, and mining sectors fell significantly. Besides, the alleviation of international trade leads to the low VAT revenue level, accounted for 81.3% of the target. Next, the government regulated some tax incentives, tax holidays, and tax allowance that drive to reduce the revenue from many sectors. Furthermore, the internal factor also generates a significant impact on tax revenue. The data and information do not harness optimally, particularly from the cross-border transactions in the digital economy era.

The other significant challenge to maximizing revenue is the low contribution of Micro, Small, and Medium Enterprises (MSMEs). Even though MSMEs play a significant role in Indonesian economic development, their numbers reach 62 million units, accounting for around 60% of the total Gross Domestic Product (GDP) and 97% of the total workers in 2017 (Ministry of SME Indonesia, 2017). The contribution to taxation is still far from reaching the maximum point. Some reasons become significant issues with collecting revenue from MSMEs. Firstly, due to the enormous number of enterprises, it is impossible to scrutinize more than a small fraction of the taxpayers intensively. Secondly, the incomes of MSMEs are relatively small and often below the poverty level. Next, MSMEs are not compelled by business reasons to keep adequate books of account. MSMEs sell mainly to the population for cash so that the application of withholding to collect their income is not practicable, in part due to the above factors that can conceal the income easily. Lastly, the low compliance and tax knowledge level is imperative to become significant grounds to avoid paying taxes.

However, the DGT must bring the MSMEs sector under taxation thoroughly. Even though that sector generates a minuscule contribution to tax revenue, equal treatment for all business types becomes the central issue for equity and fairness. Therefore, it is inevitable for the DGT to regulate the best scheme to improve tax compliance and increase revenue among the MSMEs. A suitable design mechanism is also imperative to collect the sector's revenue and keep the industry economically. This paper aims to find the effect of tax knowledge, tax rate, and the perception of equity and fairness on the tax compliance among the micro-business taxpayers. Besides, it will diagnose the challenges and then outline as well as assess the policy alternatives. Finally, it will recommend some policy strategies to increase the contribution of the MSMEs sector.

LITERATURE REVIEW

Tax Compliance

Tax compliance and evasion are global phenomena hassling, both developed and developing countries (Masoud et al., 2014). Fauzia et al. (2016) defined tax compliance as all the required tax returns are filed at the proper time and tax liability following tax law applicable when the return is filed is accurately reported in returns. Brainnyah (2013) stated that tax compliance could be defined as the degree to which a taxpayer complies or fails to comply with their country's tax rules. According to Mas'ud et al. (2014), there are two types of tax compliance: proper compliance and administrative compliance. Judicious compliance is when taxpayers adhere to tax laws stipulated in relevant regulations, while administrative compliance is the filling of tax return forms with accuracy.

Meanwhile, tax noncompliance is not complying with the tax law and administration set up in a country. Kasipillai (2012) stated that the term noncompliance encompasses intentional evasion and unintentional noncompliance due to memory lapses, calculation errors, and inadequate understanding of tax laws. Tax non- compliance can be divided into two types, which are tax avoidance and tax evasion. According to Kasipillai (2012), tax avoidance is the legal utilization of the tax regime to one's advantage, to reduce the amount of tax that is payable by means that are within the law, while tax evasion is the non-payment of the tax which would adequately be chargeable to a taxpayer if the taxpayer made full and accurate disclosure of assessable income and allowable deductions.

The Perception of Tax Rate

Some previous studies investigate how tax rate perception influences taxpayers' decision to comply with tax regulations. Kirchler (2007) states that there is no significant impact on the tax rate's perception of tax compliance among SMEs. However, the impact of the tax rate perception remains debatable on tax compliance. He also indicates that lowering tax rates does not necessarily increase tax compliance. Inasius (2015) has the same suggestion that there is no significant effect of the perception of tax rates on tax compliance. Besides, he also states that the impact of tax rates on increasing tax compliance is unclear. Kirchler et al. (2008) suggest that the government's role is quite remarkable for ensuring that the tax rates positively influence tax compliance. When trust is low, taxpayers perceive a high tax rate as unfair, and when trust is high, taxpayers might consider the same level of the tax rate as contributing to the community (Kirchler et al., 2008).

Tax structure in a country, for example, through tax audits, penalties, and tax rates. There are lots of theoretical and empirical evidence to support the punishment perspectives, such as higher audit probabilities and penalties will encourage compliance but increment on tax rates will discourage compliance (Swistak, 2016). Mas'ud et al. (2014) stated that any taxpayers who are alert with their tax rate change and become highest than average tax rates that others paid would have more probability of evading any tax charged to them. Consequently, the taxpayer's perception of their payment with a high tax rate can exceed their overpayment through tax evasion. Moreover, most of the research findings showed that the high tax rate is positively related to tax evasion and tax compliance negatively.

However, other studies found no relationship or, in fact, an even positive relationship between tax rate and tax compliance Freire and Panades (2013). Besides that, Seidu et al. (2015) examined and modeled the causes of tax default among MSMEs in the Tamale Metropolis of Ghana. The findings revealed that tax default reasons are high tax rates, inadequate tax education by tax authorities, and multiple taxations. They encouraged the government to design tax policies that make tax payments attractive and unavoidable by both formal and informal sectors. Mas'ud et al. (2014) found that high tax rates, the complicated filling procedure will cause tax noncompliance among MSMEs. They proposed that the MSMEs sector be charged at a lower percentage of tax rates to authorize enough funds and capital for business development and a better possibility of survival in a competitive market.

From the previous review, it is evident that there are mixed findings on the relationship between tax rate and tax compliance. Other studies have confirmed this trend of conflicting findings (Richardson, 2006). Thus, it is suggested that since the economic literature on the effect of tax rate and tax compliance is not conclusive due to mixed findings by various studies, the issue still requires further investigation (Freire-Serén & Panadés, 2013). Thus, it is based on this suggestion that this study is undertaken to provide more evidence on the effect of the tax rate on tax compliance. The study is different in two ways. One, it is carried out in developing African countries was evidence is lacking. It is a cross-country analysis in nature as the current study comes across only one study that examines the effect of the tax rate on tax compliance. Thus, using cross-country analysis to examine this relationship will provide more facts on the tax rate's influence on tax compliance.

Tax Knowledge

A study conducted by Oladipupo and Obazee (2016) stated that tax knowledge plays an essential role in increasing tax compliance as tax knowledge could encourage taxpayers to be more discreet in completing their tax returns. Oladipupo and Obazee (2016) findings are further supported by a few studies that also stated that tax knowledge significantly affects individual taxpayers' compliance. Their study also suggested that the tax service office should provide intensive counseling to taxpayers to raise the taxpayer's awareness to comply with paying their tax obligations. This action is considered as an effort to increase the tax revenue. Mukhlis et al. (2015) affirmed that tax knowledge has a significant positive effect on tax compliance.

Moreover, based on a study by Palil et al. (2013), employees with adequate tax knowledge can minimize unintentional noncompliance; in other words, it means that tax knowledge can increase the level of tax compliance. However, Brainyyah (2013) claimed that tax knowledge does not significantly affect MSMEs' tax compliance behavior. Because more MSMEs entrepreneurs to be acquainted with the ins and outs of taxation, there is a probability that they would also know the ways to escape the taxation regulations. In return, it may even result in tax evasion. Fauziati et al. (2016) concluded that tax knowledge has no impact on SMEs' tax compliance.

The perception of Equity and Fairness

Many studies about the impact of fairness and equity's perception of taxpayers on tax compliance had been conducted in recent decades. It is since one of the foremost principles of the taxation design is equity or fairness. Moreover, equity can be described into two significant matters, namely horizontal and vertical equity. Horizontal equity is a principal in which taxpayers should pay a similar amount of taxes to compare to others with a similar income level. For vertical equity, taxpayers will be imposed by the higher taxes paid when their tax base is higher than before without comparing with the other taxpayers. Therefore, fairness always is mentioned by the taxpayers when they are asked about the tax system.

Furthermore, another previous study conducted by Richardson (2008) states that the tax system's perception of equity and fairness also influences tax compliance. Besides, Inasius (2018) finds a significant relationship between equity and fairness and tax compliance, statistically, to increase tax compliance. Moreover, It shows that the higher the perception of fairness and equity, the greater the taxpayers' compliance. Moreover, fairness becomes one of the explanatory variables that will be examined in this master project. The importance of equity and fairness, particularly in the digital economy era, is undoubtedly immense.

METHOD

In this study, multiple regressions are used to figure out whether the tax rates' perception, the understanding of taxation, and the perception of equity and fairness substantially affect the taxpayers' behavior in complying with tax laws and regulations. Based on the study conducted by Inasius (2018), this model proportionally estimates the level of the relationship between the dependent variable and explanatory variable. Data is estimated by applying multiple regressions to examine the previous hypotheses. To test the hypotheses and construct the impact of three explanatory variables on tax compliance as the dependent variable, the researcher uses the following equation.

$$TC = \alpha + \beta 1 TR + \beta 2 TK + \beta 3 EF + \varepsilon_i$$

Where

α The coefficient of the regression model

β1 The coefficient value of The Perception of Tax Rate

β2 The coefficient value of The Perception of Tax Knowledge

β3 The coefficient value of The Perception of Equity and Fairness

ε_i Error or Standard Deviation

TC **Tax Compliance**. The total score minimum for each respondent is 15. It comes from score 1 (completely disagree) multiplied by 15 (the number of questions), and it shows that the respondent is noncompliant. Conversely, the maximum total score is 75 that comes from score 5 (completely agree) multiplied by 15 (the number of questions), and it suggests that the respondent is fully compliant.

TR **Tax Rate**. The total score minimum for each respondent is 5. It comes from score 1 (completely disagree) multiplied by 5 (the number of questions), and it shows that the respondent is noncompliant. Conversely, the maximum total score is 25 that comes from score 5 (completely agree) multiplied by 5 (the number of questions), and it suggests that the respondent is fully compliant.

TK **Tax Knowledge**. The total score minimum for each respondent is 5. It comes from score 1 (completely disagree) multiplied by 5 (the number of questions), and it shows that the respondent is noncompliant. Conversely, the maximum total score is 25 that comes from score 5 (completely agree) multiplied by 5 (the number of questions), and it suggests that the respondent is fully compliant.

EF **Equity and Fairness.** The total score minimum for each respondent is 5. It comes from score 1 (completely disagree) multiplied by 5 (the number of questions), and it shows that the respondent is noncompliant. Conversely, the maximum total score is 25 that comes from score 5 (completely agree) multiplied by 5 (the number of questions), and it suggests that the respondent is fully compliant.

Data

The data are based on the information that will be collected by distributing an online survey. However, a pilot project is conducted by sending the questionnaire to 10 chosen micro business in Surabaya Area to maintain data reliability and validity. Moreover, to minimize the problems and enhance the probability of being valid, the dependent variable will be represented by fifteen questions in the survey. The question will be divided into three-part in which each part will consist of five questions. There are three final points for the question: the tax rate, the tax knowledge, the perception of equity, and fairness. Besides, respondents will be asked to give their responses to the same statements using the Likert scale. This scale uses an ordinal number from 1 to 5, in which one means the respondent disagrees with the statement. In contrast, five means the respondent agrees with the statement.

RESULT AND DISCUSSION

Validity and Reliability Test

Table 1. Validity Test Table

Item	r_{count} – *value*	r_{table} - *value* (*df = 120, alpha=0.05*)	Conclusion
Q1	0.40930511	0.1779	Valid
Q2	0.58978653	0.1779	Valid
Q3	0.19622325	0.1779	Valid
Q4	0.18228801	0.1779	Valid
Q5	0.46064383	0.1779	Valid
Q6	0.41650141	0.1779	Valid
Q7	0.50255072	0.1779	Valid
Q8	0.50374688	0.1779	Valid
Q9	0.42743469	0.1779	Valid
Q10	0.26605631	0.1779	Valid
Q11	0.48459766	0.1779	Valid
Q12	0.5235714	0.1779	Valid
Q13	0.48037955	0.1779	Valid
Q15	0.42287116	0.1779	Valid

Criteria: The question is valid if r_{count} - *value* > r_{table} - *value*

Table 2. Reliability Test Table

Raw alpha value	Standard alpha value
0.69	0.6

Based on the results, the control group is reliable from the raw alpha value of 0.69, which is greater than 0.6 so that the data is reliable.

Normality Test

$H_0: F(\varepsilon_{it}) = F_0(\varepsilon_{it})$, error normally distributed

$H_1: F(\varepsilon_{it}) \neq F_0(\varepsilon_{it})$, error not normally distributed

Table 3. Normality Test Table

	Value	**Criteria**
D – Value	0.497	$D \geq D_{IT}$
P-Value	0.000	*p-value* < α.

Conclusion	With significance level 5% (α = 0,05), obtained p-value = 0.000 <α then H0 is rejected. It means that errors are not normally distributed. However, because the sample used is quite large, namely 122, no problems will arise if normality is not fulfilled. According to Gujarati (2003), OLS estimators tend to be normally distributed if the number of samples increases infinitely. In summary, the OLS estimator of the regression coefficient tends to be normally distributed asymptotically.

Heteroskedasticity Test

H0: var(ε_{it}) = σ^2, no heteroskedasticity

H1: var(ε_{it}) $\neq \sigma^2$, heteroskedasticity

Table 4. Heteroskedasticity Test Table

	Value	Criteria
BP – Value	3.1918	$BP \geq \chi^2_{\alpha,k}$
P-Value	0.363	*p-value* $\leq \alpha$
Conclusion	With significance level 5% (α = 0,05), obtained p-value = 0.363 < α then H0 is accepted which means that there is no heteroskedasticity.	

Multicollinearity Test

Table 5. Multicollinearity Test Table

Variable	*Variance Inflation Factor (VIF)*	Conclusion
Tax Rate	1.074937	There is no multicollinearity
Tax Knowledge	1.141667	There is no multicollinearity
Equity and Fairness	1.196940	There is no multicollinearity

Autocorrelation Test

H_0 : $\rho = 0$ no Autocorrelation

H_1 : $\rho \neq 0$ Autocorrelation

Table 6. Autocorrelation Test Table

	Value	Criteria
DW- Value	1.8741	$d < dL$ = Positive Autocorrelation $d > (4\text{-}dL)$ = Negative Autocorrelation $dU < d < (4\text{-}dU)$ = No Autocorrelation $dL \leq d \leq dU$ or $(4\text{-}dU) \leq d \leq (4\text{-}dL)$ = Cannot be Decided
P – Value	1	*p-value* < α.
Conclusion	Based on the Durbin-Watson table with significance level α = 0.05 and n = 122, the value of dL = 1.65452 and dU = 1.75515 is obtained. Obtained a value of d = 1.8741 where the value is at dU = 1.65452 <d = 1.8741 <(4-dU) = 2.24485, this indicates that there is no	

	autocorrelation. So that H0 is accepted, which means that there is no autocorrelation in the error of the model.

Partial t-Test for regression

Table 7. t-Test

Variable	Estimate	t – value	p-value
Intercept	1.127939	93.25	0.0000*
TR_Ln	0.311078	105.51	0.0000*
TK_Ln	0.383410	107.42	0.0000*
EF_Ln	0.294386	105.06	0.0000*

Each variable with a p-value <0.05 means that the independent variable affects the dependent variable individually. From the table above, it indicates that all independent variables affect the dependent variable.

The Determination of Coefficients

Table 8. The Determination of Coefficient

R – Squared	Adj. R – Squared
0.998	0.9979

The value of R-Squared = 0.998 means that the independent variables TR, TK, and EF can explain the TC variable by 99.8 percent. Therefore, it can be explained that the TC variable is explained by the model obtained by 99.8 percent. While the remaining 0.2 percent is explained by other factors that are not included in the model.
Based on the analysis results, the regression equation is obtained as follows:

$$\mathbf{Ln(TC) = Ln(1.127) + Ln(0.311\ (TR)) + Ln(0.383(TK)) + Ln(0.294(EF)) + e}$$

Based on the model above, it can be explained that the TR, TK, and EF variables each influence the TC of 0.311, 0.383, and 0.294. It means that the addition of TR and TK is also considered constant, so Ln (TC) will increase by Ln (1.127) + Ln (0.311 (1)) and so on. The results show that MSME’s perspective correlates significantly and statistically with the perspective of taxpayers regarding the perspective of tax rates, the perspective of tax knowledge, and the perspective of equity and fairness. It also supports previous studies in the literature review.

What is the most important factor that affect the tax compliance among the MSMEs taxpayers?

In this study, Tax Knowledge is the most imperative factor in determining the tax compliance among the MSMEs taxpayers. The understanding of tax regulations can be a trigger for the taxpayers to do their tax obligations. Generally, the taxpayers will not participate in taxation if they do not know the regulations such as the mechanism and sanction. In line with

Oladipupo and Obazee (2016), Mukhlis et al. (2015), and Palil et al. (2013), employees with adequate tax knowledge can minimize unintentional noncompliance; in other words, it means that tax knowledge can increase the level of tax compliance. Furthermore, their studies also indicate that tax knowledge plays an essential role in increasing tax compliance as tax knowledge could encourage taxpayers to be more discreet in completing their tax returns. Therefore, it is imperative to the DGT as tax authority to increase the tax knowledge among the MSMEs taxpayers by conducting some counseling programs, tax class, and tax seminar. Simplifying the tax regulation is also critical to rewduce the complexity that increase the taxpayers' unwillingness to learn the regulations. Considering that the tax regulations change unconsistently, thus the tax mechanism simplification is critical to increase the tax compliance.

Moreover, The Perception of Tax Rate also affect the tax compliance, but it is not as big as Tax Knowledge. Kirchler (2007), Inasius (2015), and Richardson (2006) indicate that there is no significant effect of the perception of tax rates on tax compliance. Besides, they also state that the impact of tax rates on increasing tax compliance is unclear. Thus, it is suggested that since the economic literature on the effect of tax rate and tax compliance is not conclusive due to mixed findings by various studies, the issue still requires further investigation (Freire-Serén & Panadés, 2013). However, this study found that the perception of tax rate positively affected the tax compliance among the MSMEs sector. Therefore, the DGT should reduce the tax rate for this sector since it would be affecting their compliances. Lastly, in this study, the perception of equity and fairness is the least factoir that affect tax compliance among the MSMEs sector. This result also is found by Inasius (2015) and Richardson (2006) that suggested a significant relationship between equity and fairness and tax compliance, statistically, to increase tax compliance. Finally, the previous results can be used by the DGT as the determination before formulating the tax regulations and policies.

CONCLUSIONS AND RECOMMENDATIONS

Taxation is the most significant revenue portion for the Indonesian economy and shares around 83% of total revenue in 2019. Unfortunately, the Indonesian tax ratio is lower than the other countries, particularly among the South East Asian countries, accounted for just above 11% in 2018. Some reasons become the imperative ground that contributes to the low tax revenue. However, the low contribution of the MSMEs sector becomes one of the most critical grounds that have to be addressed by the DGT as tax authority in Indonesia. Based on the data analysis, the tax compliance among the micro business taxpayers is affected considerably by their knowledge on tax regulations. Besides, tax rate also plays a significant role to affect their compliances. The higher the tax rates, the lower their willingness to conduct their tax obligations. Lastly, the perception of equity and fairness also affects the tax compliance among the small-business. Therefore, it is imperative to the DGT to consider those factors when constructing the tax regulations in the future.

The DGT enacted some regulations to maximize the tax revenue from the MSMEs sector, from simplifying-standard regime before 2013 to presumptive-standard regime after the same period. However, the contribution of the MSMEs sector to Indonesian tax revenue still far from expected. In 2018, the DGT enacted the current regulation to increase the tax revenue and tax compliance among the MSMEs called PP 23. The status quo seems attractive because it caters to simplicity and a lower tax rate than previous regulations. Unfortunately, the status quo does not promise a better result regarding the tax revenue and tax compliance among the MSMEs taxpayers. Thus, it is imperative to propose a well-designed strategy that would solve the current problems and cater to the most effective and efficient regulation.

This paper suggests a proposed strategy, namely the combination between the Piggyback Tax System and the Presumptive-Combination Regime. The former strategy will involve the local tax authority to collect tax revenue, while the latter improve the current regulation to increase tax compliance by enacting an indicator to be treated as MSMEs taxpayer. This combination will reduce the possibility of tax avoidance and increase MSMEs taxpayers' participation to comply with tax regulations.

There are some limitations to collecting the data from the online survey. Firstly, considering that the willingness to answer the question depends on the personality of the tax officer. Besides, the answer's quality also depends on understanding the MSMEs sector among the tax officers. Another problem is the inconsistency of the respondents by answering the following statements. However, it will be reduced by creating the statements as straightforward as possible and providing them with a well-designed questionnaire to make sure that respondents respond firmly and unbiasedly. Therefore, it is imperative for the future study to collect more data from more respondents, increase the validity and reliabity data from the questionnaire, and reduce the number of bias responds. Finally, the future study could be adding more critical factors that would be able to increase tax compliance among the MSMEs sector and catering the more feasible and valuable recommendations.

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