



The Impact of Covid-19 on Tax Compliance Behaviour Among Malaysian Taxpayers

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Permalink/DOI: <https://doi.org/10.15294/jejak.v15i2.37483>

Received: May 2022; Accepted: July 2022; Published: September 2022

Abstract

The unexpected Covid-19 crisis presents major challenges to Malaysia's revenue administrator due to worsening economic conditions as they anticipated growing in tax arrears, loss reporting by business and increasing in tax non-compliance and tax evasion. Therefore the objective of this study is to investigate the impact of the crisis on tax compliance and look at the willingness of the taxpayer to ensure the survival of the country while they themselves are facing financial uncertainty due to the pandemic. Adopting convenient sampling method, a survey was conducted among taxpayers in the south region of Malaysia. The findings show that 28.6% of respondents have deferred their tax e-filing and tax payment during the Covid-19 crisis. Nevertheless, those who have filed, make an early submission with intention to get tax refund in facing potential income reduction. Interestingly, 59.3% of respondents are still willing to pay tax, during and after the Covid-19 period at same marginal tax rate. In conclusion, this study provides important input to the tax administrator on the likelihood of future shortfalls in tax collection and suggests how to minimize the anticipated negative effects of the pandemic.

Key words: Tax Compliance, Covid-19, e-Filing, Economic Crisis, Tax Compliance Behavior

How to Cite: Othman, R., Ismail, Z., Sapari, A., & Bakar, S. (2022). The Impact of Covid-19 on Tax Compliance Behaviour Among Malaysian Taxpayers. JEJAK, 15(2), 11-21. doi:<https://doi.org/10.15294/jejak.v15i2.37483>

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INTRODUCTION

The Covid-19 virus, which first emerged in Malaysia on the 25 January 2020 has triggered health and economic crisis locally. Within a month, positive cases have increased to 22 cases and it has ballooned tremendously to 428 cases by the middle of March. As a precautionary measure, the Malaysian government announced a Movement Control Order (MCO) starting on 18 March 2020 and instructed non-essential businesses and services to shut down and all interstate travel was prohibited. As at 25 March 2020, a total of 1,796 positive cases had been identified with 99 recovered, while 20 have passed away. The outbreak of Covid-19, not only resulted in a serious health crisis but also a huge drop-in economic activity. The Malaysian Institute of Economic Research reported that Malaysia's Gross Domestic Product (GDP) may shrink by about 2.9% in 2020 compared with 2019 (MIER, 2020). The repercussion is, 2.4 million people are estimated to lose their jobs, where 67% are unskilled workers.

By now, it is clear that Covid-19 will intensely damage the Malaysian macroeconomy as well as its citizens' economic welfare. Besides interruption on international import and export business, the domestically imposed MCO measure had a devastating effect on private consumption and business investment. Businesses and individual's livelihood is highly at risk since it adversely affects business revenue and results in immediate cash flow constraint. If the effect cannot be controlled, the entire economy will decline resulting in business insolvency, bankruptcy and disturbance in the financial system resulting from non-performing loans.

The worse scenario facing the country is an economic recession which is generally defined as a slowdown in economic activities

and has many attributes which can occur simultaneously. These attributes include decline in economic activity, government spending, employment level, business profit, money supply, net export activities and finally reduced GDP (Gbegil, Adebisi, & Tosin, 2017). At the same time, there are many interrelated factors that could cause revenue to decline in relation to GDP, such as; (1) the probability that some tax bases will decline faster than GDP during the economic downturn, (2) a decline in commodity prices (especially oil) and other related revenues and, (3) discretionary changes in tax policy to accommodate the economic crisis. However, another important factor that is able to highly affect revenue performance and has received less attention is the possibility of changes in taxpayers' compliance behaviour during the economic crisis (Brondolo, 2009).

Therefore, it is imperative to study the impact of the Covid-19 pandemic on tax compliance behavior among Malaysian taxpayers. Its huge impact on the economy might change taxpayers' perception towards their tax responsibility. An early warning for shifts in taxpayer compliance is crucial for prevention of non-compliance. The sooner a tax authority can identify and understand the non-compliance, the faster it can respond. As the country might be struggling to cope with its future fiscal deficit, collection may fall well below initial expectations. Even though reduced tax compliance may have some countercyclical effects on the economy, it should never be condoned. This is because, noncompliance is distortionary, inequitable, and might hamper the rebuilding of tax bases over the medium-term (Brondolo, 2009).

Understanding tax compliance is very crucial since it helps the tax authority to ensure the adequacy of tax collection and to maintain the principles of tax administration, which is fairness, certainty, convenience and efficiency. Tax compliance studies have evolved over time. Economic of Crime model by Alingham &

Sandmo (1972), assumed that taxpayers are money maximizing and self-centered. This approach stands by the claim that taxpayers are homogeneous and able to make rational decisions regarding individual material benefit and cost of compliance. However, an intriguing debate in social science has been raised regarding the taxpayer motivation to comply with tax laws. The sociological approach argues whether all people are instrumentally rational and suggest that their decisions might be driven by other factors such as norms of fairness and reciprocity (Chaudhuri, 2011). The economic model also failed in explaining the high levels of voluntary compliance found in many countries despite the benefits of non-compliance which far outweigh the risks to the taxpayer (Murphy, 2008).

Tax compliance studies have also adopted the Theory of Reasoned Action, introduced by Ajzen & Fishbein in 1980 to predict the behavioral intentions and actual behavior. This theory divides beliefs into behavioral belief and normative belief. The first is suggested to be the underlying influence of an individual's attitude towards performing the behavior. Whereas the second influences the individual's subjective norm about performing the behavior. This means that salient beliefs affect intentions and subsequent behavior either through attitudes or through subjective norms. It is important to note that subjective norm is proven to be an influential factor towards explaining tax compliance behavior (Bobek, Robert & Sweeney, 2007).

More recent tax compliance studies also involve Slippery Slope Framework Prinza, Muehlbacher & Kirchler (2014), where taxpayers' compliance was reported as being affected by taxpayers' perception of the government. The "slippery slope framework" suggests two main determinants of tax

compliance, which is (i) trust in authorities and (ii) power of authorities. When both trust and power are low, taxpayers aim at maximizing individual payoffs by evading taxes. The model also asserts that increasing power of authorities leads to enforced compliance, whereas boosting trust will result in enhanced voluntary compliance.

Tax noncompliance behavior can also be explained by a social and psychological approach. Therefore, social influence theory and social exchange theory are frequently referred to in studying this issue. The theory of social influence claims taxpayers' behavior is intentionally or unintentionally shaped by others in the environment. The behavior is a result of continuous common interaction between cognitive and behavioral environmental influences. Social exchange theory suggests that human behavior is based on subjective cost-benefit-analysis and comparison of options (Cherry, 2010). Social effect model also suggests that tax compliance is closely related to tax morality which is defined as taxpayers' intrinsic motivation to pay tax or their feeling of guilt for not complying with tax law (Luttmer & Singhal, 2014).

In relation to the effect of Covid-19 pandemic, previous studies suggest that tax compliance tend to worsen during an economic downturn. Taxpayers will adopt a social norm where they perceive that the tax agency will be more flexible with the tax law. They also expect more people will evade tax as it becomes less risky and accepted as a norm among themselves (Lesnik, Kracun & Jagric, 2014; Ukaj, 2014). During recession, some businesses may declare impermissible losses, believing that the tax authority will be unable to distinguish them from genuine losses. The current self-assessment system has also put the taxpayer in a permanent dilemma which requires them to continually assess their self-interest of whether to keep their money for themselves or paying part of it over to

the government. This 'self-interest' factor represents 'Machiavellianism' attitude created by Niccolo Machiavelli to ensure self-gain and defend it (Tang & Chen, 2007). Machiavellianism is based on manipulation, utilization and exploitation in an incorrect manner and follows the principle without decency, honor and trust. Due to economic crisis, the taxpayer is expected to prioritize their self-interest either by deferring tax payment or committing tax non-compliance to ensure more income is kept for themselves to face the uncertainty of Covid-19. Therefore, as Machiavellianism is associated with tax evasion, self-interest factors are expected to have a negative effect on tax compliance.

However, despite the negative effect of economic crisis on tax compliance, the basic models of income tax compliance suggest compliance might in some respects improve as incomes fall during recession. The first reason is because taxpayers may become discouraged to take the risk of tax evasion due to less income to pay the penalty if caught. Second, reduced income during recession implies lower marginal tax rate, therefore providing smaller gain from evasion. This leaves the taxpayers with less incentives for evading tax (Brondolo, 2009). From another perspective, when facing difficult times, taxpayers of a country are more willing to pay tax when patriotism is widespread in the population. Patriotism is a 'nation-interest' or 'public-interest' compliance factor which is defined as citizen love and devotion to the country and is satisfied with non-monetary benefit (MacGregor & Wilkinson, 2015). Clift (2009), define economic patriotism as the behaviour of people who conduct business in which they make decisions that can ultimately benefit the state from an economic aspect. Qari, Konrad, & Geys (2011), suggest the patriotism criterion can also be explained as taxpayers' willingness to pay taxes to help

the country and the authors perceive those who cheat on their taxes as not patriotic.

Since tax compliance issues highly relate to moral and ethical factor, its main dilemma is to determine which is 'good or bad' and 'right or wrong' decision. John Dewey as cited in Morris (2012), define a moral problem as a struggle between "values each of which is an undoubted good in its place, but which now get in each other's way". Moral problem may arise because of conflicting duties or loyalties. It is also concerned about a self-interest and short-term benefit which conflict with a nation-interest and far-off benefit. In the case of tax non-compliance, the moral struggle is between the immediate benefit for the taxpayer and the future benefit for the society where the taxpayer is also a member. In facing the economic crises resulting from the Covid-19 pandemic, striving for taxpayers' own interest and disregarding the interest of the country is often associated with ethical or psychological egoism (Morris, 2012). Deciding whether to pay taxes during an economic crisis represents a social dilemma where self-interest and nation-interest go against each other. This is clearly because paying taxes is individually costly but benefits the whole nation (Weber, Fookan, & Herrmann, 2014).

Based on the above discussion, this study endeavors to investigate the effect of Covid-19 on tax compliance behavior, especially with regards to economic crisis. It will examine the self-interest factors and nation-interest factors towards explaining Malaysian taxpayer compliance behavior. This study proposes two hypotheses:

(H1) There is a relationship between self-interest factors and taxpayers' compliance behavior during the Covid-19 economic crisis. And (H2), there is a relationship between nation-interest (public-interest) factors and taxpayers' compliance behavior during Covid-19 economic crisis.

METHOD

This study used quantitative methods that focus on primary data collection or via survey instruments as a tool to gather information from respondents. The questionnaire is a self-administered questionnaire using Google form and distributed to groups of salaried and business owner taxpayer in the south region of Malaysia (Johor, Melaka, and State Nine (Negeri Sembilan)) using electronic mail. Several WhatsApp groups representing the same group of respondents were also choosed and forwarded the link to ensure that the survey reaches the respondents accordingly and to increase the number of participants. Out of approximately 300 emails and contact numbers, only 133 were returned with complete response and this represents 43% response rate. The south region is selected in this study for future comparison with the other 3 regions of Malaysia.

The study measures self-interest variable using the adaptation survey questionnaire on Machiavellianism from MacGregor & Wilkinson (2015), whereas the nation-interest questionnaire was adapted from Tang & Chen (2007), in their study regarding patriotism. The questions for self-interest factor, consist of 5 questions and presented in the second part of the survey followed by 3 questions on nation-interest factor which is presented in the third part of the survey. The dependent variable (taxpayer

compliance behaviour) is measured by respondents' willingness to pay taxes based on factors such as additional tax rates, trust to the government and religious obligation.

RESULTS AND DISCUSSION

As summarised in Table 1, most of the respondents that participated in the survey were salaried taxpayer (91.7%) meanwhile the others were business taxpayer (4.5%), self-employed (3%) and others (1.5%) which covers pensioners and unemployed respondents. 69.9% of the respondents worked in the public sector, followed by 27.8% in private sector and the rest were in the corporate sector. The categories of taxpayer were classified into individual taxpayer (94%), Sole proprietor taxpayer (4.5%) and Company (1.5%). In terms of income level of respondents, 10.0% earned income below RM34,000 per annum whereas 12.8% and 22.6% earned more than RM34,000 to less than RM50,000 and RM50,000 to less than RM70,000. The largest percentage of respondents were in the income class of RM70,000 to less than RM100,000 representing 32.3%. 21.8% of respondents earned income of more than RM100,000 per annum. Despite of the convenient sampling method used by the study, majority of the respondents were found to derived from salaried income group taxpayer and therefore, the result is bound to be generalized only to this group.

Table 1. Respondents' Background

Items/ Questions	Categories	Frequencies	Percentage (%)
Occupation	Salaried	122	91.7
	Business	6	4.5
	Self-employed	3	2.3
	Others	2	1.5
Taxpayer category	Individual	125	94.0
	Sole proprietor	6	4.5
	Company	2	1.5

Items/ Questions	Categories	Frequencies	Percentage (%)
Income sector	Public sector	92	69.9
	Private sector	38	27.8
	Corporate	3	2.3
Annual Income (per annum)	<RM34,000	14	10.5
	>RM34,000 - RM50,000	17	12.8
	>RM50,000 - RM70,000	30	22.6
	>RM70,000 - RM100,000	43	32.3
	>RM100,000 - RM150,000	23	17.3
	>RM150,000	6	4.5
	Tax declaration status	Active (declared every year)	120
Partly Active (did not declare every year)		9	6.8
Not Active (never declared)		4	3.0
Tax payment status	Active (paid taxes every year)	113	84.9
	Partly active (did not pay tax every year)	7	5.3
	Not active (never paid taxes)	13	9.8
Did you pay your income tax?	Yes	95	71.43
	No	38	28.57
When did you do your e-filing?	Within:		
	4 weeks ago	67	72.0
	3 weeks ago	12	12.9
	2 weeks ago	2	2.2
When do you plan to do your e-filing?	Within :		
	4 weeks from now	8	21.0
	3 weeks from now	10	26.3
	2 weeks from now	4	10.5
	1 week from now	16	42.2

In regards to respondent status as taxpayers, the questionnaire segregates them into 2 categories of (i) those who declared their income every year and (ii) those who paid their tax every year. These categories were then sub-divided into (i) active (declared income and paid tax every year), (ii)

partly active (declared income and paid tax, but not every year) and (iii) not active (did not declare income and never paid tax). Table 1 shows that 120 (90.2%) respondents declared their income through e-filing every year, even though only 113 (84.9%) of respondents were actually having taxable income to be paid every

year. As for those who were partly active, 9 of them were partly active in terms of declaring their income but only 7 of them were partly active in terms of paying tax. The 'not active' respondents' group, shows 11 and 7 of respondents' have never pay tax nor declared their income to the tax authority, respectively.

The result also shows respondent's e-filing submission status which were originally scheduled on the 30 April 2020 (employment) and 30 June 2020 (business) but which were both subsequently extended to 30 June 2020 and 30 August 2020 respectively by the Inland Revenue Board of Malaysia (IRBM). Most respondents (95 respondents or 71.43%) had filed their tax returns via e-filing and 38 (28.57%) of them have yet to submit. 71% of them filed their tax returns more than 4 week ago, 12.9% within 3 week ago, 2.2% within 3 week ago and 12.9% filed their tax returns within 1 week ago. The results also show 42.2% respondents, who have not filed their tax returns, plan to file their tax returns within 1 week from now, 10.5%, within 2 weeks from now, 26.3%, to file their tax return 3 weeks from now and 21% plan to do the e-filing 4 weeks from now.

The finding indicates that filing compliance among Malaysian taxpayers is at a satisfactory level, as more than 70% of the taxpayer filed their tax returns on time. The survey was distributed over 2 weeks starting from 1st May to 15th May 2020 and 72% of respondents had made an early submission via e-filing in early April 2020 (for employment income). Those who have not filed the tax returns, 42.2% of them intended to file the tax return "within 1 week from now", even though the dateline has been extended. Respondents also provided reasons for early submission, where 58.95% and 38.95% of respondents submitted their tax returns because they had all the required information and adequate knowledge,

respectively, to do submission. As for those who defer their submission, insufficient information and procrastination are among the reasons, with 18.42% and 15.79% of them, respectively, hoping that tax payment will be deferred as they need the money for themselves in facing the pandemic.

Descriptive analysis on the responses towards statements of dependent and independent variables were analyzed based on a 4-point Likert scale ranging from: 1: Strongly Disagree, 2: Disagree, 3: Agree and 4: Strongly Agree. The mean for dependent variable of the study (taxpayers' compliance behavior) showed an overall mean score of 2.832 which implies on the average respondents 'disagree' to comply to taxes during Covid-19 economic crisis. This phenomenon is supported by Brondolo (2009), as the study generally expected tax income to worsen when income is decreasing. Lesnik, Kracun & Jagric (2014), also highlighted that reduction in income during economic crisis will result in increasing tax debt. The highest mean score was 3.1880 for the statement "I am willing to pay tax because I believe it is not only a responsibility towards the nation, but also towards the religion". This finding indicates that Malaysian taxpayer do take their tax responsibility as part of their religion obligation as its benefits others and for the wellbeing of the nation. Jalil (2012), highlighted that cheating on taxes is unethical for Muslim taxpayers if their government is purely Islamic and follows Islamic law. McGee (2012), also opined, it is unjust to commit non-compliance if the government in power uses tax collection both for raising revenue for the government function and for wealth distribution to the needy.

On the other hand, the lowest mean score was 2.3233 for the statement "I am willing to contribute to my country through higher tax rate to ensure it is able to develop after Covid-19 crisis". This finding implies that even though Malaysian taxpayers are willing to pay tax during

economic crisis, they disagree to pay tax at higher rates, basically due to financial constraint. This input should be taken into consideration by the tax authority in order to recover the country’s revenue in the post Covid-19 period.

As for the first independent variable of the study, the mean analysis for taxpayers’ self-interest factors showed a mean score of 3.3293 which indicates that on average, respondents agreed with the statements that they need to prioritize their own self-interest during the Covid-19 crisis. The highest mean score referred to the statement “I need to have sufficient saving to survive in post Covid-19 crisis” (mean = 3.7368). Meanwhile the lowest mean score was obtained on the statement “Covid-19 will not affect my ability to pay my future taxes.” (mean = 2.8797). The finding confirms the existence of Machiavellianism attitude among Malaysian taxpayer especially during the Covid-19 crisis. The underlying reason for this, is to increase their chances of benefitting economically, which again is a selfish motive (Castille & Buckner, 2018).

The result of mean analysis for taxpayers’ nation-interest factors showed a mean score of 3.5163. This indicates that on average, respondents agree towards the importance of having nation-interest during Covid-19 crisis. The highest mean score referred to the statement “Without tax revenue, I believe our country will not be able to ensure the future development and wellbeing of the nation.” (mean = 3.5639). Meanwhile the lowest mean score was obtained for the statement “Even though the economy is expected to worsen, I’m still willing to allocate my income for taxes.” (mean = 3.4887). The finding show that Malaysian taxpayers had concern for the future for the country and were willing to sacrifice for the present. The result is in line with MacGregor & Wilkinson (2015), where Malaysian taxpayers with patriotic attitude are more positive about paying tax to support their country.

Table 2, below presented the Cronbach’s Alpha coefficients for all 3 variables in the questionnaires. The reliability results for all variables are acceptable since all the reliability coefficients are over 0.70.

Table 2. Reliability Statistic

Variables	Cronbach’s Alpha	Number of items in constructs
DV ₁ (Compliance Behavior)	0.728	5
IV ₂ (Self-interest)	0.756	3
IV ₃ (Nation-interest)	0.728	3

Pearson Correlation Coefficient Analysis was conducted to assess the relationship between the variables. This test also looks at the direction and magnitude of relationship between them. The result showed, only the nation-interest factor was a significant moderate positive relationship with taxpayers’ compliance behavior, where $r = .496$, and $p\text{-value} < .001$. Even though self-interest factor showed a negative relationship

with taxpayers’ compliance behavior, it is not significant.

To predict the outcome of the dependent variable from one or more predictor variables, regression analysis is used. The result of regression coefficient is as follows:

$$\text{Taxpayers Compliance Behavior} = \alpha + \beta_1 \text{ Self-interest Factors} + \beta_2 \text{ Nation-interest Factors} + \epsilon \tag{1}$$

$$\text{Taxpayers Compliance Behavior} = .477 - .017 (\text{Self-interest Factors}) + .677 (\text{Nation-interest Factors}) \quad (2)$$

Based on the above model, when taxpayers have no self-interest and no nation-interest, their compliance behavior is very low (.477). Apart from that, the result also showed that for every unit increase in self-interest, taxpayer compliance attitude will decrease by .017. At the same time, for every unit increase in nation-interest, the taxpayers' compliance attitude will increase by .677.

The model summary of multiple regression analysis showed a R square of .243 which suggest that 24.3% variation in taxpayers' compliance behavior can be explained by the variation in taxpayers' self-interest and nation-interest factor, while another 75.7% is due to other factors outside this study.

F-test was conducted for overall significance of the model and to determine whether both independent variables have a significant linear relationship with the dependent variable. Results of the F-Test showed that the significant value (p-value)

was less than .001. It signifies that the overall model is significant where $F(2,130) = 20.873$, $p\text{-value} < .001$. Thus, the results indicate that at least one independent variable has a significant linear relationship with taxpayers' compliance attitude. Hence, the null hypothesis is rejected.

Finally, T-test is used to determine whether there is a significant linear relationship between dependent variable and each independent variable. Based on Table 3.3.2, the p-value for self-interest is .863. Thus, it indicates that self-interest has no linear relationship on taxpayers' compliance behavior (where $t(30) = -.173$, $p\text{-value} = .863$). Therefore, the first hypothesis (H_1) is rejected. Even though self-interest factor has a negative co-efficient, this is not significant, hence, it does not affect Malaysian taxpayers' compliance behavior. The insignificant result is expected due to the majority of respondents coming from employment income taxpayers. In Malaysia, Scheduler Tax Deduction system leaves salaries taxpayer with no option but to pay tax every month. Even though they want to keep the money for themselves, tax will automatically be deducted by their employer for tax payment.

Table 3. Regression Coefficient

Coefficients Model	Unstandardized		Standardized	t	Sig.
	B	Std. Error	Beta		
(Constant)	.477	.495		.963	.337
Taxpayers' Self-interest Factor	-.017	.098	-.013	-.173	.863
Taxpayers' Public- interest Factor	.677	.105	.493	6.485	.000

The result also showed that the p-value of nation-interest is .000. Thus, it indicates that the nation-interest factor has significant positive linear relationship on taxpayers' compliance behavior (where $t(130) = 6.485$ $p\text{-value} = .000$). Therefore, the second hypothesis (H_2) is accepted. This study

concludes that nation-interest factors does affect Malaysian taxpayers' compliance behavior. Konrad & Qari (2012), had results in-line with the current study's finding since it found a strong and statistically significant positive correlation between the strength of patriotism and tax morale. Qari, Konrad, & Geys (2011), also

claim that patriotism is positively related to tax compliance since their finding shows a negative relationship between tax compliance with shadow economy.

CONCLUSION

The economic crisis following the Covid-19 pandemic caused uncertainty about the future revenue of the country as tax compliance is expected to decrease. This has forced the taxpayer into a dilemma in making compliance decision based on self-interest and nation-interest factor. However, even though self-interest factors are expected to negatively affect taxpayers' decision during this period, it does not significantly relate to their compliance behavior. This study confirms that the nation-interest attitude positively supports Malaysian taxpayers' compliance decision in assisting the country towards surviving the pandemic. The study also concludes that the issue of social contracts gives the impression that the more patriotic a person is, the greater the sacrifice he can afford for the sake of the state. From the tax authority perspective, a careful mechanism to recover the future revenue of the country must be formulated. Introducing higher tax rate could be counterproductive and causes huge impact on the overall compliance behavior. It is recommended for the government to keep the growth rate of the nation's spending below the growth of GDP in order to reduce future budget deficit and keep the country back on track.

Finally, this study also subjects to several limitations. First, the findings are unable to be generalized to the whole population of Malaysian taxpayer due to underrepresented of business and self-earned income group taxpayers in the sample. Secondly, since there are scarce tax compliance studies focusing on the effect of economic crisis period in Malaysia, other variables such as economic stimulus package

provided by the government should be considered in affecting Malaysian taxpayers' compliance behavior. Nevertheless, both limitations led to recommendation for future study since other income taxpayers may behave differently in facing the economic crisis of Covid-19.

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