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Power and Trust as Determinants of Tax Compliance Costs

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Abstract:

Compliance with tax laws by taxpayers is fundamental to the collection of tax revenue. Taxpayers can either comply voluntarily or they can be forced by a revenue authority to comply. Revenue authorities can thus embrace a customer service-oriented approach (based on trust) or an enforcement approach (using power) to ensure taxpayer compliance. Using a combination of the Slippery Slope Framework (SSF) and a Structural Equation Modelling (SEM) analysis, the effect of power by and/or trust in the South African Revenue Service (SARS) on small, medium and micro enterprises' (SMMEs') tax compliance costs is investigated. It was established that while the use of power has no statistically significant impact on tax compliance costs, trust significantly reduces SMMEs' tax compliance costs. This finding may be important to all revenue authorities who wish to ensure improved taxpayer compliance.

Keywords:

Tax Compliance Costs, SMME, Power and Trust, Revenue Authority Behaviour, Slippery Slope Framework (SSF)

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Introduction

In South Africa, the tax collected for the year ending 31 March 2023 amounted to R1 686.7 billion, an increase of R122.9 billion from the prior year (National Treasury and SARS, 2023). This is remarkable, as for revenue authorities to collect taxes from taxpayers, taxpayers must comply with relevant tax regulations – and in South Africa with its complex tax legislation (Davis Tax Committee, 2018), tax compliance may place a high burden on taxpayers. Compliance by taxpayers with tax laws is fundamental to the collection of tax revenue because the higher the level of non-compliance by taxpayers, the higher the tax burden of compliant taxpayers and/or the danger that revenue authorities may fail to raise sufficient revenue (Richardson and Sawyer, 2001; Yong et al., 2019). Taxpayers can either comply voluntarily or be forced to comply with tax regulations (Kirchler, 2007). Tax compliance behaviour is a complicated phenomenon, considering that various factors may influence taxpayer compliance decisions (Yong et al., 2019). Nevertheless, revenue authorities must consider taxpayer compliance behaviour in formulating a tax collection approach. This is why revenue authorities have moved from merely enforcing tax laws, to rather becoming a service provider to facilitate tax compliance by taxpayers (OECD, 2014). For example, the South African Revenue Service (SARS) Strategic Plan 2020/2021 to 2024/2025 states that if taxpayers are willing to comply (voluntarily), SARS will make it easy for them to comply, but conversely, if taxpayers decide not to comply, they will be met by the full force of the law and will be forced to comply (SARS, 2020). This response from revenue authorities such as SARS, exemplifies the complex interaction between taxpayers and revenue authorities, where revenue authorities behave in a certain way to ensure tax compliance (Feld and Frey, 2007).

Research (Batrancea et al., 2019; Gangl, Hofmann and Kirchler, 2015; Hofmann et al., 2014; Kastlunger et al., 2013; Pereira et al., 2019) indicates that revenue authorities can take two approaches: a customer service-oriented approach (based on trust between the taxpayer and revenue authority) or an enforcement approach (where the revenue authority uses its power over taxpayers) to ensure compliance. The delicate balance in this power/trust nexus may also influence the tax compliance cost burden for taxpayers, which refers to those costs that would disappear if there were no need to comply with tax regulations (Guyton et al., 2003). According to Evans (2008), the tax burden comprises three elements: the taxes themselves, the efficiency costs that lead to market distortions induced by a tax, and the operating costs of the tax system. The operating costs of the tax system consist of the costs to the government (ultimately borne by taxpayers) of administering and collecting the taxes (administrative costs) and the costs expended by taxpayers in complying with the tax laws, commonly referred to as tax compliance costs.

Several studies have investigated tax compliance costs (European Commission, 2022; Matarirano et al., 2019; Smulders et al., 2012). Eichfelder and Kegels (2014) specifically investigated the actions by

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revenue authorities to reduce overall tax compliance costs and thus improve tax compliance by small, medium and micro enterprises (SMMEs), concluding that revenue authority behaviour can increase tax compliance costs and reduce tax compliance by SMMEs. This paper investigates the use of power by SARS and/or trust in SARS on tax compliance costs of SMMEs. A quantitative survey was used to measure SMMEs' tax compliance costs and ascertain the determinants of these costs. The Slippery Slope Framework (SSF) (Kirchler et al., 2008) was employed to investigate the effect of the use of power by SARS and trust in SARS on SMMEs' tax compliance costs. A Structural Equation Modelling (SEM) analysis was performed to determine the structural paths from each SSF construct to the total tax compliance costs, including the covariance relationships between the SSF constructs. Research on whether and how SARS's power and/or trust influences tax compliance costs may assist in finding ways to reduce tax compliance costs for SMMEs. This is important because reduced tax compliance costs may provide tangible benefits to SMMEs, allowing them to become more tax compliant (Lewis and Alton, 2015), which will ultimately benefit the fiscus. Although performed in a South African context, the results may also be relevant to other countries wishing to improve taxpayer compliance

Literature Review and Conceptualisation of Terminology

SMME Defined

One of the challenges in tax compliance cost studies for SMMEs is that there is no universal definition of the term SMME (Ardic et al., 2011; Berisha and Pula, 2015). After examining the definition of a SMME from an international economic perspective and a South African economic and taxation perspective, it was deemed appropriate to use turnover to determine whether a business qualifies as an SMME. The use of turnover is also supported by the following: First, most prior studies undertaken on tax compliance costs in South Africa used turnover as a basis to define small businesses (FIAS, 2007; Govender and Citizen Surveys, 2008; Matarirano et al., 2019; Smulders et al., 2012). Secondly, in countries where presumptive tax systems were introduced to encourage small businesses to enter the formal tax system, turnover is usually used as a benchmark for qualification (Loeprick, 2009). Turnover is also one of the three criteria used to classify an enterprise as either micro, small or medium prescribed in the National Small Enterprise Act (1996), and the most frequently used criterion to determine whether a business qualifies for small business tax concessions. Accordingly, turnover categories were established for the micro, small and medium segments of SMMEs, namely R1 million or less for micro entities, more than R1 million but not exceeding R20 million for small entities, and more than R20 million but not exceeding R250 million for medium-sized entities.

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Tax Compliance Costs

The literature recognises that the following costs form the basis of tax compliance costs: the cost of time spent by taxpayers on tax compliance activities, the cost of expertise to assist taxpayers in tax compliance activities, and any incidental costs incurred by taxpayers in fulfilling their tax compliance activities (Evans, 2008, 2019; Smulders et al., 2016). Internal costs are the costs of labour or time spent on tax compliance activities by the owner/s of the SMME, an employee and/or an unpaid friend or relative to learn and understand the tax law and the obligations that the law imposes, and the time required to obtain documents and data to complete a tax return, submit a tax return, pay the taxes, and any other post-tax return submission activities (Evans 2008). External costs are the costs paid to an external service provider to provide the SMME with tax services to remain compliant and non-labour costs are incidental costs incurred by an SMME's personnel who deal with tax compliance activities (Evans 2008).

Tax Compliance Behaviour

To examine tax compliance behaviour, it is crucial to first comprehend the meaning of the term “tax compliance” (Richardson and Sawyer, 2001). According to Roth et al. (1989), tax compliance entails: “that the taxpayer files all required tax returns at the proper time and that the returns accurately report tax liability in accordance with the Internal Revenue Code, regulations, and court decisions applicable at the time the return is filed”. However, economic and psychological variables must also be taken into account to comprehend tax compliance (Kamleitner et al., 2012). Kirchler (2007) refers to tax compliance as “probably the most neutral term to describe taxpayers' willingness to pay their taxes”. James and Alley (2009) discuss the concept of tax compliance, considering it from a narrow perspective to law enforcement to a broader economic perspective. They conclude that tax compliance might be “the willingness of individuals and other taxable entities to act … within the spirit as well as the letter of tax law and administration without the application of enforcement activity” (James and Alley, 2009). James (2012a) shortens this definition to “[t]he willingness of taxpayers to act in accordance with the statutory requirements or intentions of the tax law and administration”. He notes that a complete definition should thus include compliance with both the spirit and the letter of the law.

The willingness of taxpayers to act according to the spirit and the letter of the law is a complex issue. Some taxpayers comply voluntarily; others need to be nudged; some must be forced into compliance (Tan and Braithwaite, 2018). Voluntarily compliant taxpayers pay their “fair share” without hesitation, while enforced compliance refers to taxpayers who pay because they fear being audited or fined, and these may employ avoidance tactics wherever they find a way to evade tax law without being caught (Wahl et al., 2010). These two interpretations incorporate opposing attitudes towards tax compliance, but they do not imply a full understanding of taxpayer behaviour – they should merely be seen as different interpretations of varying degrees of tax compliance behaviour (Wu, 2012).

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A tax compliance model developed in Australia and New Zealand demonstrates how their revenue authorities handle taxpayers' opposing attitudes to ensure tax compliance (James, 2012b), where the action of one of the parties prompts a response from the other party. For example, revenue authorities can enforce tax compliance by employing the full force of the law where non-compliance from taxpayers is detected, but, on the other hand, if taxpayers are willing to do the right thing, the revenue authority can endeavour to make it easy for them to comply. In South Africa, a similar tax compliance strategy is followed (SARS, 2020). Some examples of proactive behaviour by SARS include introducing the Tax Administration Act 28 in 2011, establishing the office of the Tax Ombud (Office of the Tax Ombud, n.d.) in 2013 and the release in 2018 of its Service Charter, which outlines taxpayers' rights and responsibilities, as well as service standards that taxpayers can expect (SARS, 2018). SARS's approach to achieving voluntary tax compliance is based on three principles: taxpayers are made aware of their obligations, SARS makes it easy for taxpayers to comply with these obligations, and SARS will act against those who break the law (SARS, 2020). SARS wants to enhance voluntary compliance by establishing trust, but it will use its power to force non-compliant taxpayers into compliance.

There are two groups of models to analyse tax compliance behaviour: the standard economic model and behavioural models (Kirchler, 2007). The standard economic model was introduced by Allingham and Sandmo (1972) and drew many of its premises from the literature on the economics of crime, as well as on optimal portfolio choice (Allingham and Sandmo, 1972; Kirchler, 2007; Weber et al., 2014). This model follows a neoclassical approach, where the taxpayer is regarded as a rational person who takes a calculated risk of not declaring income honestly (Alm et al., 2012; Horodnic, 2018). It relies on the assumptions of the expected utility theory, which states that taxpayers decide between risky or uncertain conditions by comparing expected utility values (Akhand, 2012). Applied to tax compliance studies, this model suggests that taxpayers maximise their wealth by trading off the different outcomes of the cost of tax evasion against the cost of total tax compliance (Olsen, Kang, et al., 2018). Although this standard economic model was extended, it still allows only for a few factors influencing tax compliance: the tax rate, the taxpayer's level of risk aversion, detection probability, and the penalty imposed for tax evasion (Slemrod and Gillitzer, 2014). Because the level of tax compliance is predicted only by the taxpayers' fear of detection and punishment, this model is also known as the economic deterrence model (Olsen, Kang, et al., 2018). Using this model, in theory, revenue authorities just need to increase the frequency of audits and severity of penalties on any under-declaration of taxes for tax compliance to improve (Kirchler, 2007), but taxpayers do not always react rationally, as predicted by the standard economic model (Wittberg, 2016). This is why the purely rational benefit-cost calculation regarding a taxpayer fails to explain why the observed level of tax compliance is higher than the predicted level of tax compliance in tax compliance experiments (Olsen, Kang, et al., 2018; Torgler, 2002). One of the reasons why the standard economic model fails is that it neglects the importance of

non-monetary factors. Hence, researchers study the effect of other non-monetary factors on taxpayer compliance behaviour (Horodnic, 2018). Therefore, there was a paradigm shift from considering only economic factors to including psychological and socio-psychological factors that may influence tax compliance behaviour (Alm et al., 2012), forming the basis for behavioural models.

Taxpayer compliance behaviour on a socio-psychological level deliberates the effect of taxpayers' motivational postures. Taxpayers evaluate revenue authorities on how they act and perform. Based on these evaluations, taxpayers develop an attitude or motivational posture toward the regulatory authority (Braithwaite, 2002). Motivational postures from a taxpayer perspective entail the interconnected sets of beliefs and attitudes consciously held by taxpayers towards revenue authorities (Braithwaite, 2002) and reflect taxpayers' willingness to comply or not comply with tax regulations (Hofmann et al., 2008). Five motivational postures are considered in the context of taxpayer compliance behaviour: commitment, capitulation, resistance, disengagement, and game-playing (Braithwaite, 2002; Kirchler, 2007). For example, a committed taxpayer believes in the benefits of the tax system and considers tax compliance to be morally just; a capitulating taxpayer tries to comply but does not always succeed; a resistant taxpayer doubts the intentions of the revenue authorities and disputes them, and therefore does not want to comply; a disengaged taxpayer is wholly detached from the tax office and does not comply; and a game-seeking taxpayer seeks to take advantage of particular laws and loopholes within the tax system (Olsen, Kasper, et al., 2018).

The motivational postures elicit different strategies from the revenue authorities to exploit or counter the types of taxpayer attitudes, as indicated in the tax compliance model developed in Australia and New Zealand (James, 2012b). This tax compliance model is based on the seminal work of John Braithwaite (Ayres and Braithwaite, 1992) and based on the general theory of responsive regulation (Freedman, 2012). The responsive regulation theory is conceptualised as a compliance pyramid and can be applied to the tax environment to determine whether revenue authorities should enforce compliance or motivate voluntary compliance based on the behaviour of taxpayers (Holzinger and Biddle, 2016). Although the theory accepts that most taxpayers comply voluntarily, some taxpayers need to be assisted by revenue authorities to comply. At the tip of the pyramid, some taxpayers evade tax and need to be dealt with by revenue authorities using the force of the law (Ahmed and Braithwaite, 2005; Freedman, 2012). In short, revenue authorities' action is based on the behaviour of the taxpayer – hence the term responsive regulation theory.

Most governments rely on voluntary compliance from taxpayers (Jimenez and Iyer, 2016); hence, the implementation of optimal tax policy must consider tax compliance behaviour. However, tax compliance behaviour is subject to the dynamic interaction of the various factors and the behaviour of the participants involved (Alm et al., 2012). Recent research has shifted towards a more psychological

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approach to explain tax compliance behaviour (Enachescu and Kirchler, 2019). The SSF is one such approach that combines an economic and psychological perspective to explain tax compliance behaviour (Kirchler, 2007).

Slippery Slope Framework

The SSF focuses on the interaction between tax revenue authorities and the taxpaying public, and how the style of interaction adopted by the authorities influences taxpayer behaviour. In other words, the SSF suggests that taxpayers either comply voluntarily or resist complying because they feel that they are forced to comply due to the behaviour of revenue authorities (Enachescu and Kirchler, 2019). Thus, the SSF is based upon two main dimensions: the power of the revenue authorities and the trust in the revenue authorities (Kirchler et al., 2008). According to this framework, enforced compliance is primarily influenced by the authorities' power, whereas voluntary compliance is elicited by the taxpayers' trust in the authorities (Eichfelder and Kegels, 2014). Furthermore, the level of tax compliance decreases sharply where trust in the revenue authorities and the power of the revenue authorities are reduced to lower levels. Due to this interaction, it is sometimes challenging to ensure tax compliance in a social setting (because power may enhance trust, but too much power can destroy trust). This trend explains the name, "slippery slope", for this framework (Lozza et al., 2013).

From the original conceptualisation of the SSF, it was extended as a response to the inconsistent results from different studies regarding the dynamics between power and trust, where some researchers argued that trust and power are negatively related, and others the opposite (Alm et al., 2012; Gangl et al., 2012). Gangl et al. (2015) suggest that different conceptualisations of power and trust cause these differences, and also from diverse operationalisations in empirical investigations. To explain these differences in the results, the extension of the SSF was introduced to provide for the forms of power and trust (Gangl, Hofmann and Kirchler, 2015; Hofmann et al., 2014).

Power is a party's ability or perceived ability to influence another party to obtain the outcome that the influencing party desires (Gangl, Hofmann and Kirchler, 2015; Simpson et al., 2015). Therefore, the power of the revenue authority is the revenue authorities' ability (or perceived ability, from the taxpayers' viewpoint) to influence the taxpayer to be tax compliant. This power may take the form of coercive power or legitimate power (Turner, 2005). Coercive power exists when one party perceives another party to have the ability to punish them for either doing something wrong or for not doing something they should have done (Simpson et al., 2015). From the viewpoint of a taxpayer, it can therefore be seen as “harsh” power the revenue authority has over the taxpayer by imposing penalties on the taxpayer if the taxpayer has done something wrong or has omitted to do something the taxpayer should have done (Kastlunger et al., 2013).

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Contrary to coercive power, legitimate power exists when one party accepts and recognises that the other party has the right to control their actions and therefore submit to this influence (Cruz, 2019; Simpson et al., 2015; Turner, 2005). From the viewpoint of a taxpayer, this is a “soft” power the revenue authority exerts over the taxpayer because this power is not based on the force or pressure from the revenue authorities but on the use of information, charisma, legitimisation, and expertise by the revenue authority which will convince taxpayers to be voluntarily tax compliant (Gangl, Hofmann and Kirchler, 2015; Kastlunger et al., 2013; Kirchler et al., 2008; Turner, 2005). According to Kastlunger et al. (2013), legitimate power can increase trust in the revenue authorities, whereas coercive power has the opposite effect. Therefore, the dynamics of trust also must be considered in investigating taxpayers' tax compliance behaviour.

Trust is a foundational orientation between parties in a relationship that incorporates all three forms of human experience – emotion, cognition and behaviour (Lewis and Weigert, 2012). The level of trust is crucial in the establishment of power dynamics in relationships (Simpson et al., 2015). One party is willing to act on another party's words, actions, and decisions based on the level of trust the party has in the other party (McAllister, 1995). According to Alm et al. (2012), most definitions in the literature distinguish between reason-based trust and implicit trust. Reason-based trust arises from a deliberate decision by a trustor based on goal achievement (the trustor evaluates whether the trustee pursues a goal that is important to the trustor); dependency of the trustor on the trustee; internal factors (for example, the trustor considers the trustee competent, willing, and harmless), and external factors (such as the perceived opportunities and dangers in the relationship) (Gangl, Hofmann and Kirchler, 2015; Gobena and Van Dijke, 2016). From these definitions, it may be deduced that a taxpayer would be inclined to trust the revenue authority if there are reasons for the taxpayer to do so; for example, if the taxpayer perceives the revenue authority to be competent and working for the common good (Enachescu and Kirchler, 2019; Gangl, Hofmann and Kirchler, 2015; Gobena and Van Dijke, 2016).

According to Gobena and Van Dijke (2016), implicit trust is “an automatic, unintentional, and unconscious reaction to stimuli originating from associative and conditioned learning processes in which shared social identities are likely to arise”. Implicit trust, therefore, transpires without a conscious reason recognised by the trustor to trust the trustee. From the relationship viewpoint between taxpayers and the revenue authority, it means the taxpayers trust the revenue authority without considering any reasons to trust the authority. Instead, they base this automatic trust on shared norms, signalled values, and habits (Gangl, Hofmann and Kirchler, 2015). For example, revenue authorities may induce implicit trust by presenting themselves to taxpayers as warm, friendly, and customer-oriented (Enachescu and Kirchler, 2019). Reason-based trust and implicit trust are related, in the sense that reason-based trust may develop into implicit trust if the taxpayer has repeated positive experiences, coming to trust the

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revenue authority automatically in the long run, without considering any current reasons for the decision to trust (Enachescu and Kirchler, 2019; Gangl et al., 2019).

The dynamics between the power of and the trust in revenue authorities may create three different cooperative climates: an antagonistic, service or confidence climate, which may lead to different levels of cooperation by taxpayers (Gangl et al., 2012, 2019; Hofmann et al., 2017). A negative relationship between coercive power and implicit trust, which suggests that, in an environment where there are high levels of coercive power from the revenue authorities and low levels of implicit trust in them, there will be an antagonistic climate, where taxpayers perceive the revenue authorities as an institution whose primary goal is to catch them as tax evaders (Gangl et al., 2019). This climate results in mutual distrust between the revenue authorities and taxpayers, and the need to force taxpayers to comply (Gangl, Hofmann and Groot, et al., 2015; Hofmann et al., 2014). High levels of implicit trust may create a confidence climate, leading to committed cooperation by taxpayers (Enachescu and Kirchler, 2019). This climate exists where there is mutual trust and respect between taxpayers and the revenue authority. In such a climate, the use of “harsh” power by the revenue authorities is unnecessary, with taxpayers seeing the payment of taxes as a moral obligation (Gangl et al., 2019). In contrast to the negative relationship between coercive power and implicit trust, it has been found that legitimate power stimulates reason-based trust, which results in a service climate where taxpayers comply voluntarily (Hofmann et al., 2014). In a service climate, revenue authorities and taxpayers have a customer-client relationship, in which revenue authorities interact to serve taxpayers as clients, which results in taxpayers who perceive the revenue authorities as supportive and competent, which is likely to result in voluntary compliance from taxpayers (Gangl et al., 2012).

Eichfelder and Kegels (2014) found that revenue authority behaviour (which influences taxpayers’ perceptions and behaviour) significantly impacts the burden of complying with the tax law and a customer-unfriendly revenue authority (which decreases trust in the revenue authority) and the use of power by the revenue authority, increases tax compliance costs for taxpayers. In this article, possible relationships between tax compliance costs and the behaviour of the revenue authority towards SMMEs are explored from a South African perspective, because one of the factors influencing the tax morale of taxpayers is the relationship between revenue authorities and taxpayers (Feld and Frey, 2007).

Research Method

Design

A positivist research philosophy was followed (Saunders et al., 2019) using a quantitative approach. Combined with the regulatory perspective, this research falls within a functionalist paradigm (Saunders et al., 2019), as the article investigates the use of power by SARS and/or trust in SARS on tax

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compliance costs. An online survey was deemed the best technique to collect the data because online surveys are rapid and cost-effective when accessing a large sample over a wide geographical area (Cooper and Schindler, 2014); they allow quantitative data to be collected for statistical analysis purposes and previous studies on tax compliance costs in South Africa have successfully adopted this technique (FIAS, 2007; Smulders et al., 2012).

A survey instrument was developed: 1) to obtain information on tax compliance costs and 2) to use the SSF to investigate the effect of the use of power by SARS and trust in SARS on SMMEs' tax compliance costs. The design of the survey instrument was based on local and international best practices to ensure comparability where possible. Best-practice questionnaires were adapted and expanded to suit the South African context and the research objective. The questionnaire included five broad components, namely background information on the responding SMME, external tax compliance costs, internal tax compliance costs, non-labour costs related to tax activities incurred by SMMEs, and the interaction of SMMEs with SARS to obtain respondents' perceptions regarding the dimensions of the power of and/or trust in revenue authorities in line with the SSF.

To detect weaknesses in the design of the questionnaire and the procedures and protocols used during the data collection process, pilot tests were initiated - first involving local and international academics involved in tax compliance cost research and second SARS's internal personnel. In a third pilot test, SARS sent the link to the updated questionnaire to 90 randomly selected SMME taxpayers. The only concern raised was the length of the survey, but due to the research objective, it was decided not to remove any questions. All ethical considerations associated with the study and internet-mediated research were adhered to.

Population and Responses

The target population was SMMEs in South Africa registered with SARS for tax purposes, and the sample frame was the SMMEs for which SARS had an e-mail address. A census approach was followed by sending the questionnaire to the entire database to maximise the response rate, obviating the need to use any statistical sampling techniques. SARS sent the e-mail containing the link to the final questionnaire to SMMEs on 18 March 2019 and a reminder e-mail was sent on 26 March 2019. The number of responses added up to 4 557, representing a response rate of 3.06%. To achieve the research objective, fully completed surveys were needed to calculate the tax compliance costs of SMMEs, therefore only 771 of the responses were usable after data cleaning, which represents a response rate of 0.51%. Even though this response rate is considered low, Saunders et al. (2019) indicate that internet-based surveys outside organisations typically have a response rate of 10% or lower. For example, in a study in Germany focusing on the tax compliance costs of private households, a response rate of 0.54%

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was documented, but when only usable responses were taken into account, the response rate dropped to 0.33% (Blaufus et al., 2019).

Because a relatively low response rate was achieved, evaluating the possibility of non-response bias was necessary to establish whether it affected the survey results. Therefore, differences between early (first 10% of respondents who completed the survey) and late respondents (last 10% of respondents who completed the survey) were tested using an independent-sample t-test and a non-parametric test. Even though the last wave of respondents did show a higher tax compliance cost estimation than the first wave, there was no statistically significant difference between the two groups. Therefore, assuming that late respondents can be used as a proxy for non-respondents (Tran-Nam et al., 2016), the results suggest the absence of non-response bias, implying that the results are not biased in this respect.

Results and Discussion

First the quantification of tax compliance costs. External tax compliance costs consisted of the costs respondents incurred in respect of a professional tax adviser to assist with tax-related activities and obligations. The internal tax compliance costs were quantified by first establishing the time (in hours) taken by respondents internally (per tax type, tax compliance activity and type of employee) to comply with tax legislation. These hours were then multiplied by externally verified rates. This multiplication provided the Rand values of the internal tax compliance costs. In addition, if an SMME formed part of a group structure and incurred internal tax compliance costs because of this relationship, these costs were added to the abovementioned cost. The non-labour costs were the costs respondents incurred in respect of the following items: office space and/or parking at the office; furniture, fixtures and fittings; tax software; utilities; staff travel and tax conferences.

Second the effect of the use of power by SARS and trust in SARS on SMMEs' tax compliance costs. The validity of the SSF constructs was investigated by using exploratory factor analysis (Hair et al., 2010; Taherdoost et al., 2014). Confirmatory factor analysis was not considered appropriate as the items grouped under each construct were adapted from different instruments to suit the current research content (Yahaya et al. 2018). Cronbach's alpha value was used to assess the internal consistency (reliability) of the items. A good reliability score (alpha) should exceed the threshold of 0.7, but George and Mallery (2003) argue that a Cronbach alpha value of 0.5 is generally accepted in exploratory factor analysis. Hence, factors with Cronbach alpha values between 0.5 and 0.6 were considered acceptable and retained for further analysis (Field, 2018). Composite reliability, which is recommended by Malhotra (2020), was also provided, due to some criticism of Cronbach's alpha (Sijtsma, 2009). A summary of the exploratory factor analysis is provided in Table 1. Principal axis factoring was used as the extraction method and Promax as the rotation method. Discriminant validity was assessed using the correlation between the latent factors using the HTMT criterion (Rönkkö and Cho, 2022; Voorhees et al., 2016). No

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values exceeded the threshold of 0.85, and therefore discriminant validity between the constructs was confirmed.

Constructs and items	KMO & Barlett's test (sig. value)	% variance explained	Factor loadings		Cronbach's alpha
Q8.2 Administration quality of SARS	0.873 p <0.001	63.9%	Factor 1		0.912
Q8.3 Tax law complexity	0.887 p <0.001	58.6%	Factor 1		0.906
Q8.4 SARS's power to manage tax evasion (legitimate power)	0.835 p <0.001	62.6%	Factor 1		0.888
Q8.5 Expertise and abilities of SARS officials (reason-based trust)	0.939 p <0.001	68.3%	Factor 1		0.945
Q8.6 Interactions between tax personnel of the business and SARS officials (implicit trust)	0.828	61.9%	Factor 1		0.912
Q8.7 Administrative procedures of SARS (procedural justice)	0.893 p <0.001	66.8%	Factor 1		0.923
Q8.8 Decisions of SARS (procedural justice)	0.905 p <0.001	60.7%	Factor 1		0.912
Q8.9 Fairness (distributive justice)	0.550 p <0.001	50.5%	Factor 1	Factor 2	0.670 (Final factor)
Q8.10 Assessments, audits and penalties (retributive justice – proxy for coercive power)	0.913 p <0.001	60.4%	Factor 1		0.913
Q8.11 Consultation from SARS (procedural justice)	0.500 p <0.001	83.2%	Factor 1		0.909

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Constructs and items	KMO & Barlett's test (sig. value)	% variance explained	Factor loadings			Cronbach's alpha
Q8.12 When the business pays its taxes as required by the South African tax laws and regulations, it does so ... (voluntary corporation)	0.871 p <0.001	51.9%	Factor 1	Factor 2	Factor 3	0.764 (Factor 3)
Q8.13 When the business pays its taxes as required by the South African tax laws and regulations, it does so … (committed cooperation)			Factor 1	Factor 2	Factor 3	0.889 (Factor 1)
Q123 When the business pays its taxes as required by the South African tax laws and regulations, it does so … (enforced compliance)			Factor 1	Factor 2	Factor 3	0.797 (Factor 2)
Q124 Between SARS and SMMEs there exists a climate ... (antagonistic climate) Between SARS and SMMEs exists a climate … (Service and confidence climate)	0.849 p <0.001	61.7%	Factor 1	Factor 2		0.750 (Factor 2) 0.941 (Factor 1)

Table 1: Summary of the exploratory factor analysis

The KMO was above the recommended threshold of 0.5 (Field, 2018), except for the two-item factor analysis for Construct 8.11, which would always result in a value of exactly 0.5 and is still acceptable in this case. The Bartlett's Test of Sphericity was statistically significant (p <0.001) (Field, 2018) for the items in each of the 15 constructs, indicating that exploratory factor analysis was appropriate.

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The analysis was conducted separately for each of the 15 SSF constructs that were defined in the literature and adapted for this research. The analysis confirmed unidimensionality for Construct 8.2, Construct 8.3, Construct 8.4, Construct 8.5, Construct 8.7, Construct 8.8, Construct 8.10 and Construct 8.11 because the analysis identified only one factor based on the eigenvalue criterion, an eigenvalue greater than 1 (Field, 2018). These constructs were subsequently labelled “Administration quality of SARS” (8.2), “Tax law complexity” (8.3), “SARS’s power to manage tax evasion (legitimate power)” (8.4), “Expertise and abilities of SARS officials (reason-based trust)” (8.5), “Administrative procedures of SARS (procedural justice)” (8.7), “Decisions of SARS (procedural justice)” (8.8), “Assessments, audits and penalties (retributive justice)” (8.10) and “Consultation from SARS (procedural justice)” (8.11).

The exceptions were Construct 8.6, Construct 8.9, Construct 8.12, Construct 8.13, Construct 123 and Construct 124. For Construct 8.6, the analysis identified two factors. Only one item, namely Item 8.6.1, double-loaded on Factor 1 and Factor 2. However, after rotation, Item 8.6.1, which was double-loaded, did not load high enough (above 0.3) on the second factor. The solution is thus unidimensional, as Item 8.6.4 also did not load above 0.3 and was therefore omitted from further analysis. Construct 8.6 was subsequently labelled “Interactions between tax personnel of the business and SARS officials (implicit trust)”. For Construct 8.9, Items 8.9.3 and 8.9.4 loaded onto a second factor with Item 8.9.3 double-loaded after rotation. After consideration, Item 8.9.3 was retained with Factor 1. Thus Item 8.9.4 was the only item under Factor 2. As a single item cannot constitute a factor, it was omitted. Then one factor remained, consisting of Items 8.9.1 to 8.9.3. Construct 8.9 was subsequently labelled “Fairness (distributive justice)”. Construct 8.12, Construct 8.13 and Construct 123 were based on the same opening statement. The analysis for these areas identified three factors. Items 8.12.1 to 8.12.5 loaded onto Factor 3 and were subsequently labelled “When the business pays its taxes as required by the South African tax laws and regulations, it does so... (voluntary cooperation)”. Items 8.13.1 to 8.13.4 loaded onto Factor 1 and were subsequently labelled “When the business pays its taxes as required by the South African tax laws and regulations, it does so… (committed cooperation)”. Items 123.1 to 123.5 loaded onto Factor 2 and were subsequently labelled “When the business pays its taxes as required by the South African tax laws and regulations, it does so… (enforced compliance)”. For Construct 124, the analysis identified two factors. Items 124.1 to 124.3 loaded onto Factor 2 and were subsequently labelled “Between SARS and SMMEs there exists a climate... (antagonistic climate)”. Items 124.4 to 124.9 loaded onto Factor 1 and were subsequently labelled “Between SARS and SMMEs exists a climate… (service and confidence climate)”.

The Cronbach alpha values were above the accepted threshold of 0.7 for all the constructs (Field, 2018) and were thus considered satisfactory, except for Construct 8.9. However, 0.6 is considered the threshold for exploratory factor analysis (Hair et al., 2010), and the reliability was therefore also considered acceptable.

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Considering that the included SSF constructs each consisted of a set of items, the researchers took the investigation further by using a SEM analysis to understand the relationships between the SSF constructs and tax compliance costs. The SEM analysis determined the structural paths (size and direction of relationship) from each SSF construct to total tax compliance costs, including the covariance relationships between the SSF constructs. SEM uses various models to investigate a series of dependent relationships among variables, with the primary goal of providing a way to test a theoretical model developed by the researchers (Schumacker and Lomax, 2010). This technique offers an advantage over first-generation statistical tools such as regression analysis, because SEM enables a researcher simultaneously to model relationships among independent and dependent constructs (Anderson and Gerbing, 1988; Gefen et al., 2000), and measurement error is considered at the item level (Schumacker and Lomax, 2010).

Figure 1 shows that the effect of power and trust on tax compliance costs was investigated through testing the structural paths. Power and trust are influenced by several factors therefore, following the extended SSF, the influence of power of and/or trust in SARS on SMMEs' tax compliance costs was tested by investigating the structural paths. It is submitted that perceptions of power and trust result from the climate between SARS and SMMEs (antagonistic, service or confidence), which in turn stems from the type of compliance from SMMEs (enforced, voluntary or committed).

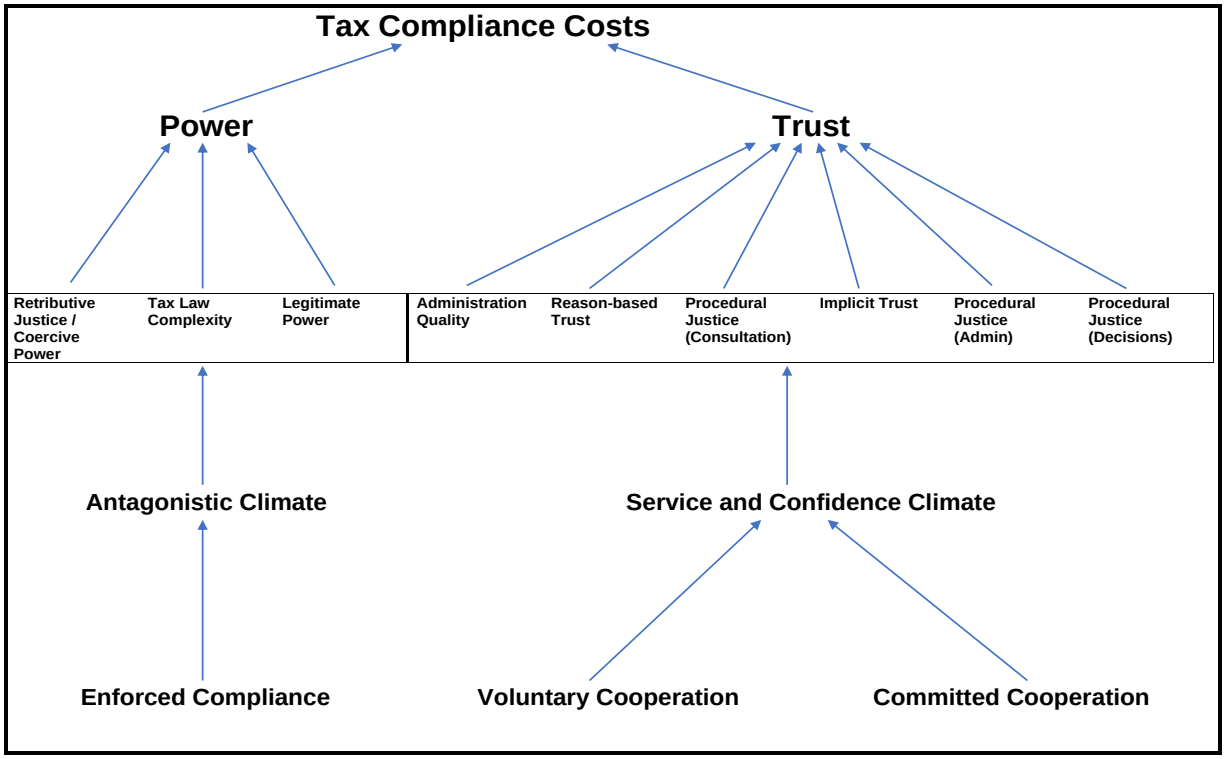

Figure 1: Conceptual relationships

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The results of the model are graphically presented in Figure 2. The paths from each construct to the dependent variable (total tax compliance costs) are indicated by a single-sided arrow.

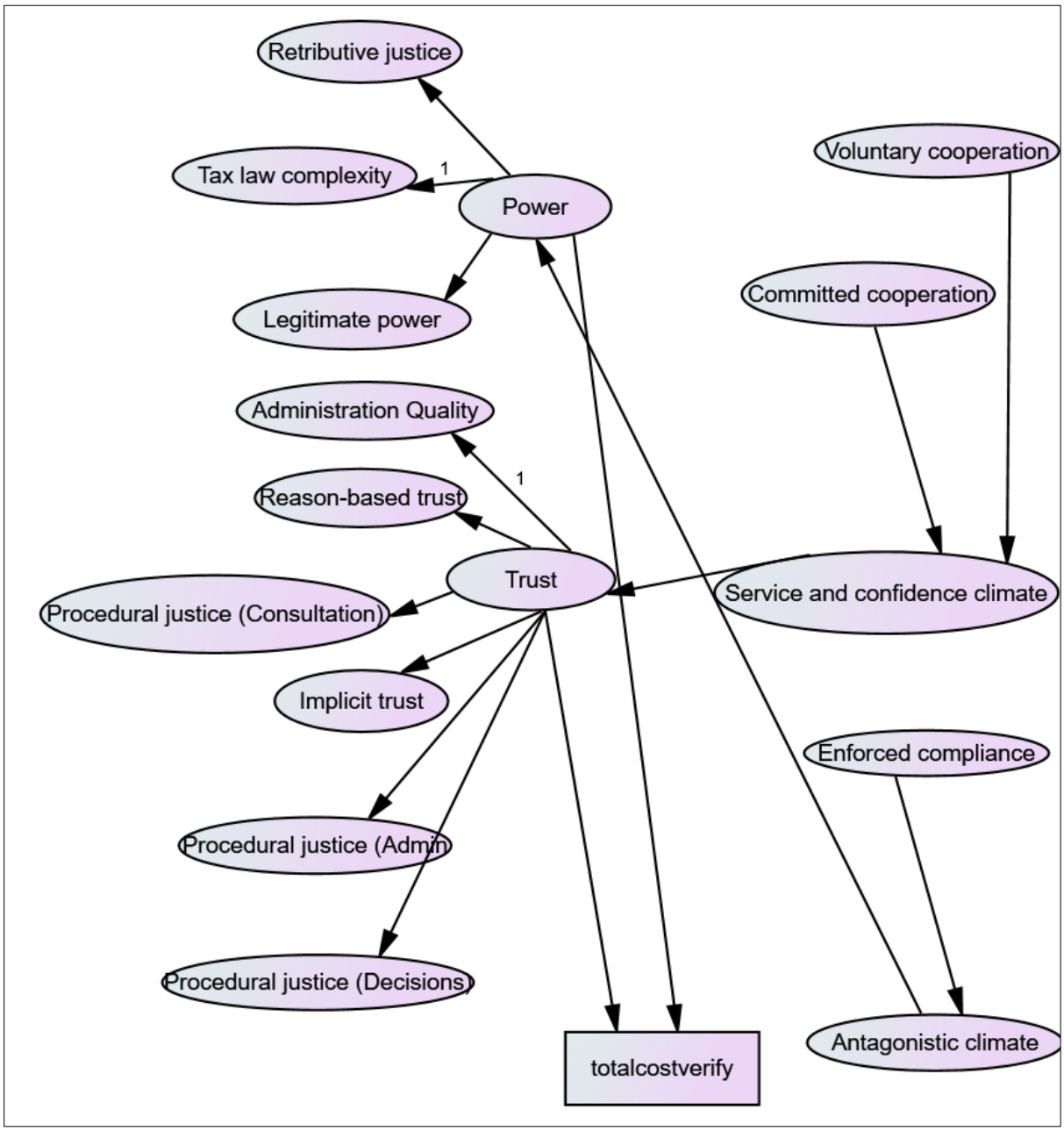

Figure 2: Testing the effect of power and trust on tax compliance costs

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As presented in Table 2, the fit indices and the threshold values presented in each column in Table 2 were applied to establish the fit of the model.

Model	CMIN (X^2)	df	P	CMIN/df	RMSEA	CFI	TLI	IFI
Model	7915.0	2683	0.000	2.950	0.05	0.880	0.875	0.880
Indicate acceptable fit	-	-	-	<3 or <5	≤0.08	≥0.90	≥0.90	≥0.90

Table 2: SEM fit indices

When the structural model was fitted to the data, the RMSEA was good at 0.05 and below 0.08, the CFI (0.880), TLI (0.875) and IFI (0.880) were slightly below 0.90, and CMIN/df (2.95) fitted the data under the threshold of <3. Various authors have indicated that a value above 0.8 for CFI, TLI and IFI is permissible for SEM (Hu and Bentler, 2009; Lai and Green, 2016; Wisting et al., 2019). Therefore, the relationships indicated in the model (Figure 2) were interpreted and represented in the hypothesis set for the model. Table 3 presents the structural path coefficients, namely the standardised regression weights.

Relationships			Standardised regression weights and statistical significance
Antagonistic climate	<---	Enforced compliance	0.239***
Service & confidence climate	<---	Voluntary cooperation	0.229***
Service & confidence climate	<---	Committed cooperation	0.136*
Trust	<---	Service & confidence climate	0.712***
Power	<---	Antagonistic climate	-0.842***
Total tax compliance costs	<---	Power	0.050
Total tax compliance costs	<---	Trust	-0.273***
*** Significant at a 0.1% level of significance (p-value <0.001) ** Significant at a 1% level of significance (p-value <0.01) * Significant at a 5% level of significance (p-value <0.05)			

Table 3: Structural path coefficients

The results reported in Table 3 indicate the following: the relationship between Total tax compliance costs and Power was positive, but very weak and not statistically significant (β = 0.050; p >0.05); the relationship between Total tax compliance costs and Trust was negative, moderate, and statistically significant (β = -.0.273; p <0.001); the relationship between Service and confidence climate and Trust was positive, strong, and statistically significant (β = 0.712; p <0.001); the relationship between Antagonistic climate and Power was negative, strong, and statistically significant (β = -0.842; p <0.001); the relationship between Committed cooperation and the Service and confidence climate was positive, weak, and statistically significant (β = 0.136; p <0.05); the relationship between Voluntary cooperation

and the Service and confidence climate was positive, weak, and statistically significant (β = 0.229; p <0.001); and the relationship between Enforced compliance and Antagonistic climate was positive, weak, and statistically significant (β = 0.239; p <0.001).

From these results, it appears that an increase in enforced compliance leads to an increased antagonistic climate (although the relationship is positive and weak). An antagonistic climate reduces the perception of the power of SARS (the relationship is negative and strong). Still, this perception of the power of SARS and total tax compliance costs is not statistically significant, implying that increased use of SARS's powers does not have a statistically significant impact on the total tax compliance costs of SMMEs.

However, contrary to this result, the relationship between voluntary cooperation and committed cooperation by taxpayers to a service and confidence climate was positive and weak (but statistically significant), which indicates that voluntary cooperation and committed cooperation lead to an increased service and confidence climate. Furthermore, increased levels regarding a service and confidence climate appear to lead to an increased perception of trust in SARS (there was a positive and strong relationship). Most importantly, a higher level of trust in SARS seemed to reduce tax compliance costs (there was a negative and moderate relationship).

Conclusion

The research objective was to investigate the effect of the power of SARS and/or trust in SARS (resulting from the climate of interactions between SARS and SMMEs) on SMMEs' tax compliance costs. With no study seemingly investigating the effect of the power of SARS and/or trust in SARS on SMMEs' tax compliance costs in South Africa, the research results contribute to the current body of knowledge on various levels. First, the results indicated that while the use of power has no statistically significant impact on tax compliance costs, the use of trust does have a significant impact. Second, the research used a combination of the SSF and a SEM analysis to ascertain the effect of power by and/or trust in SARS on SMMEs' tax compliance costs. The SEM analysis determined the relationship among the different SSF constructs according to the determinants that statistically significantly predicted the dependent variable, enabled a better understanding of the influence of the power of SARS and/or trust in SARS on SMMEs' tax compliance costs, which would not have been possible with a regression analysis.

SMMEs are internationally acknowledged as the life-blood of modern economies, and the importance of these enterprises to the industrialised world cannot be overemphasised. Rising tax compliance costs are one of SMMEs' main challenges, as these can affect their viability and growth. Therefore, policymakers need to know which elements of tax compliance costs are possibly adding to the tax

compliance burden for businesses and should, therefore, be targeted for reform. Given that SARS is making a concerted effort to increase tax compliance and provide a customer-friendly environment for taxpayers, this research will assist them to continue trying to reduce tax compliance costs for taxpayers from the revenue authority's side. Moreover, this research could be valuable toall revenue authorities striving to provide a customer-friendly environment for taxpayers. Therefore, it is recommended that these revenue authorities make an effort to address those aspects under their control which will affect SMME taxpayers' trust in them. Taxpayers who trust revenue authorities will incur lower tax compliance costs. In return, the tax compliance behaviour of SMME taxpayers will improve, creating a win-win situation for both parties.

The research did not explore tax compliance benefits and the effect thereof on tax compliance costs. In addition, although psychological costs are relevant and recognised in the SMME environment, these costs cannot be measured objectively and consistently (Blaufus et al., 2019; Evans, 2019). Therefore, it is recommended that future research endeavours find innovative ways to quantify or report on these benefits and psychological costs associated with tax compliance.Despite proving the absence of non-response bias by conducting a wave analysis, it is recommended that future research consider face-to-face interviews in addition to an online survey (funding and time permitting) to mitigate the low response rate that typically results from online surveys.

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