

The Influence of Culture on Tax Non-compliance Intention among SME Owners in Malaysia

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Abstract

The importance of SMEs as the backbone of Malaysia in generating national income is undoubted. However, little consideration was given to culture as one of the determinants of tax non-compliance. With a multicultural society that has different cultures, beliefs and values, it is important to examine the influence of culture on tax non-compliance. Therefore, this study attempts to examine the influence of culture on tax non-compliance intention. The survey collected data of 105 usable SME owners from central region of Peninsular Malaysia. Findings reveal that power distance, individualism, masculinity and uncertainty avoidance are significantly related with tax non-compliance intention, whereas long-term orientation is insignificant. Suggestions for policymakers and future researchers are also highlighted.

Keywords: *Culture, Hofstede's Cultural Dimensions Theory, Tax Non-compliance Intention, SME Owners*

Introduction

Small and medium enterprises (SMEs) as the backbone of Malaysia have led the economic local and export demand with a contribution of up to 99.2 percent of businesses and companies in Malaysia (Kamaruddin, 2014). Its contribution to the Gross Domestic Product (GDP) has

increased from 38.3 percent in 2018 to 38.9 percent in 2019 and the local sectors are expected to grow faster. However, due to the large opportunities involved in cash business transactions, SME owners tend to engage in tax non-compliance and avoid cash declaration (Mohamad, Zakaria & Hamid, 2016), especially because their actions appear to be mostly overlooked by the tax authority (Mohd Ali, 2013). The serious problem of tax non-compliance among SME owners have caught attention from tax authorities, academician and non-governmental organizations worldwide (Newman, Mwandambira, Charity and Ongayi, 2018). Nevertheless, little has been focused on the influence of culture in explaining tax non-compliance among SME owners. According to Roth, Scholz & Whitte (1989), it is very important in explaining tax non-compliance since culture itself may reflected taxpayers' values and norms that are constantly practised in their daily life, which later can shape their attitude towards non-compliance, either to comply or not to comply with tax requirements.

Besides that, this study also has been conducted to call upon study done by Yong (2011). Due to the limitations of qualitative research in explaining culture influence on SME operators in New Zealand, it was suggested that a different approach of research methodology, such as surveys, be used. It is also suggested that research be expanded to include countries that use a self-assessment system. Consistent with Chau & Leung (2009), who also suggested that cultural studies should not be limited to Anglo-Saxon countries, but should be expanded and conducted in other multiracial and multicultural countries.

Thus, the objective of the study is to determine the influence of culture on the tax non-compliance intention among SME owners in Malaysia.

Literature Review

Hofstede's Cultural Dimension Theory

The Hofstede's Cultural Dimension Theory has been introduced by a Dutch psychologist name Geert Hofstede. It is an approach using human values through cultural dimensions for the purpose of conflict management in a society. Hofstede (2001) defines culture as "the collecting programming of the mind that distinguishes the members of one group or category of people from another". A five-dimensional measure of culture has been introduced, which includes: (1) power distance, (2) individualism versus collectivism, (3) masculinity versus femininity, (4) uncertainty avoidance, and (5) long-term versus short-term orientation (Hofstede, 1980, 1991). Power distance refers to society's acceptance of differences in power distribution and represents the solution to a fundamental problem in human inequality (Hofstede, 1980). Malaysia ranks highly in the Power Distance Index (Hofstede, Hofstede & Minkov, 2010). Malaysians' current attitudes such as obedience and conformity demonstrate this, and they are still subject to autocratic decision-making and close supervision (Tsakumis, Curatola & Porcano, 2007).

Individualism versus collectivism refers to how individuals choose to be integrated into their own groups and how individuals behave toward the group (Hofstede & Bond, 1988). According to Hofstede (2001), individualism, refers to a society in which the ties between individuals are loose, where everyone is expected to look after herself or himself and her or his immediate family only. Meanwhile, collectivism refers to a society in which people are integrated from birth into strong, cohesive in-groups that continue to protect them throughout their lives in exchange for unquestioning loyalty. Malaysia, for example, has a close social relationship with each other in society (Tsakumis et al., 2007) and is listed as a collectivism country.

The measurement of masculinity versus femininity does not refer to gender dominance, but rather to the extent of social or community integration (Jones, 2007). It reveals an individual's attitude toward one's sex (Hofstede & Bond, 1988). According to Hofstede (1980), masculine societies can be categorised as assertive since they are more focused on achievement and success as their dominant values. It is in contrast to femininity society, which prefers to have good quality in life and relationships as their dominant value and can be categorised as a nurturing pole. Malaysia, on the other hand, was listed as a feminine country (Hofstede et al., 2010).

Uncertainty avoidance refers to the level of stress in society due to facing an unknown future. It does not refer to social behaviour but rather to the search for absolute truth (Hofstede & Bond, 1988). Societies with a high level of uncertainty avoidance are more rule-oriented and have a lower tolerance for accepting changes and risks (Hofstede, 1980). It contrasts with low uncertainty avoidance societies, which are less rule-oriented and more tolerant of changes and risks. As for Malaysia, it has a weak uncertainty avoidance (Tsakumis et al., 2007).

Long-term versus short-term orientation proposes time orientation as it relates with persistence and thrift, past and present, tradition and social obligations (Bond & Chi, 1997), as well as how we plan our decisions relating to saving and spending because time orientation affects individuals' behaviour (Nguyen-Phuong-Mai, 2015). Long-term oriented individuals, according to Nguyen-Phuong-Mai, are always looking for the future, are always persistent in doing the best they can, strategically plan their spending, and still obey the rules as long as it may benefit them because they believe in the "what works" approach. This is in contrast to short-term oriented individuals, who tend to seek out what they have experienced in the past and present. They enjoy showing their appreciation to others through gifts and other means. In order to conform to tradition, they tend to repeat or follow what has previously been practised because they believed in the "what is right" approach. According to Hofstede et al. (2010), East Asian countries and Eastern and Central European countries have long-term oriented cultures, whereas the United States, Australia, Latin American, and African countries have short-term oriented cultures. Muslim countries were also listed as being short-term oriented.

Culture and Tax Non-compliance Intention

Several studies have been conducted to determine the impact of culture on tax compliance. Individualism-collectivism has been studied concerning taxpayers in the United States and Hong Kong by Chan, Troutman & O'Bryan (2000) and McGee, Ho & Li (2008). Among United States and Hong Kong taxpayers, Chan et al. (2000) reveal a significant negative relationship between culture and tax compliance behaviour. Taxpayers in the United States are more inclined toward individualistic values. They are more compliant and have a favourable attitude toward taxation than taxpayers in Hong Kong, who are more inclined toward collectivism. These differences may impact taxpayers' ethical values and moral development, as well as their tax compliance behaviour (Chan et al., 2000). Even though the findings of McGee et al. (2008) are consistent with those of Chan et al., it is suggested that the study be extended to include business owners due to the limited number of respondents among advanced undergraduate business students.

Tsakumis et al. (2007) uses this model in a study, and Malaysia was chosen as one of 50 selected countries to be one of the samples. Overall, Tsakumis et al. conclude that when explaining power distance cultural value, Malaysians still practise obedience and conformity because they are still under autocratic decision making and close supervision. Furthermore, Malaysians are considered collectivist because they have a close social relationship with one another, have a moderate to weak uncertainty avoidance and lean more toward femininity, preferring to have a good relationship with one another and being concerned about quality of life.

Tsakumis et al. (2007)'s study was extended by Richardson (2008), who uses multiple tax evasion measures across countries, including Malaysia. Only individualism and uncertainty avoidance find to have a significant influence on tax evasion in the study. According to the findings, individualist and low-uncertainty avoidance taxpayers are more likely to comply with tax requirements. The importance of power distance and masculinity cultural value in explaining tax evasion find to be insignificant. However, neither of these studies addressed one of Hofstede's Cultural Dimensions Theory dimensions, i.e., long-term-short-term orientation.

Hamid (2013) conducted a mixed method cross-cultural study on tax agents in Malaysia and New Zealand and find that culture is significantly positively associated with New Zealand tax agents in both cases of overstating expenses and understating income, indicating that they had a tendency to practise individualism and higher uncertainty avoidance in performing their duties towards tax compliance. Meanwhile, Malaysian tax agents find that their culture had no influence on either overstating expenses or understating income scenarios. However, the study finds that there are inconclusive results between the survey and the interview. According to survey findings, Malaysian tax agents have a higher degree of power distance, where they work under close supervision from senior staffs and junior staffs must still practise obedience towards senior staffs. However, they contribute more to masculinity cultural value because they are focused on achievement and success. New Zealand tax agents, on the other hand, were found to be more individualist and high uncertainty avoidance. In contrast to the findings of the interviews, Malaysian tax agents reveal to have a lower power distance and a high individualism dimension. Meanwhile, New Zealanders are listed as individualist taxpayers. Nonetheless, due to the

unavailability of index data from Malaysia and New Zealand, this study does not discuss long-term-short-term orientation.

An intra-cultural study conducted by Yong (2011) towards ethnic in New Zealand, focuses on SMEs owners, uses qualitative method by conducting a face-to-face in-depth interview in collecting data on record keeping functions, seeking tax assistance, and tax payment difficulties due to ethnic differences, which are divide into four major ethnic groups, namely Asian, Europe, Maori, and Pacific. In terms of record keeping functions, the Europe and Asian groups find to have moderate to high uncertainty avoidance, medium to long term orientation, and masculinity cultural value, indicating that they are more confident and proficient in record keeping than the Maori and Pacific groups. Asian group finds to be more collectivist in seeking tax assistance, relying on friends and peers more than Europe, Maori, and Pacific groups, who seek paid tax practitioners. According to Yong, SME owners who have collectivistic values, long-term orientation values and a low power distance cultural value will incur low compliance costs because they do not rely on paid tax practitioners as much. In terms of tax payment difficulties, Maori and Pacific groups face more tax payment difficulties than Asian and Europe groups because they have lower uncertainty avoidance, more collectivist, femininity and short-term oriented cultural values. Yong concludes that taxpayers with high power distance, more individualist and masculine cultural values, a high uncertainty avoidance and a long-term orientation are able to pay their taxes on time in order to avoid tax penalties. Yong's recommendation is to extend the culture study to other multicultural countries implementing SAS because research on the influence of culture on SMEs owners has lagged behind, despite its importance in determining voluntary compliance level.

Alabede (2012) finds significant differences in tax compliance behaviour among individual taxpayers in Nigeria in a study on tax compliance behaviour in Nigeria. Alabede reveals that the Igbo ethnic group is individualist and practises full compliance with tax laws, whereas the Hausa and Yoruba ethnic groups are not in full compliance because they are collectivist.

A prior study in Cebu, Philippines by Malaya and Malaya (2012) also has been conducted in due to the problem of non-compliance behaviour in paying tax. This situation continues to be unresolved even though penalties and audits exist. Study finds that cultural plays an important role in encouraging taxpayers to comply with tax laws. Specifically, Cebu taxpayers reveal to be more collectivist.

In terms of the Malaysian environment, Kasipillai and Abdul-Jabbar (2006) conducted a culture study among taxpayers in the northern region of Peninsular Malaysia. The findings differ from those of other cultural studies. It finds that there is no significant difference in overall non-compliance attitudes between ethnic groups. However, this is due to the sample size being limited to only five urban areas in Peninsular Malaysia's northern region, namely George Town, Alor Setar, Kulim, Sungai Petani and Kangar.

Culture has been studied both intra-culturally and cross-culturally in relation to tax non-compliance behaviour. According to Li (2010), cross-cultural studies may misrepresent the analysis due to some important factors that should be considered, such as the tax burden, legal origin, culture, and income distribution of those countries. Torgler (2007) and Yong (2011) support the argument by stating that an intra-cultural study would be more useful and representative in investigating culture influence in tax compliance due to differences in countries' tax laws and regulations, types of taxes and environment.

A Malaysian study focuses on the influence of culture towards tax non-compliance intention by Md Radzi (2020) reveals that five dimensions of culture are significantly related with tax non-compliance intention among SME owners in northern region of Peninsular Malaysia. According to the findings of this study, there is a negative relationship between individualism and masculinity cultural values, as well as long-term orientation and intention of tax non-compliance intention. Meanwhile, power distance and uncertainty avoidance have been found to have a positive relationship with tax non-compliance intention. However, it is suggested that the study be extended to other regions in Malaysia, thus the findings' generalisability is not limited.

Overall, the findings on culture are still inconclusive and require further investigation, particularly in the Malaysian tax environment. This is consistent with the suggestions of Alm and Torgler (2006) and Nerre (2008) as tax culture differs from country to country and is influenced by cultural norms and the country's tax environment. Therefore, this study believes that it would be an interesting finding to discuss the influence of taxpayers' culture on dimensions introduced by Hofstede in influencing the intention of tax non-compliance among SME owners. Based on the above discussion, the following hypotheses are as follows:

H₁: Power distance significantly influence tax non-compliance intention among SME owners in Malaysia.

H₂: Individualism significantly influence tax non-compliance intention among SME owners in Malaysia.

H₃: Masculinity significantly influence tax non-compliance intention among SME owners in Malaysia.

H₄: Uncertainty avoidance significantly influence tax non-compliance intention among SME owners in Malaysia.

H₅: Long-term orientation significantly influence tax non-compliance intention among SME owners in Malaysia.

Methodology

The research framework illustrates in Figure 1 is based on Hofstede's Cultural Dimensions Theory. It considers power distance, individualism, masculinity, uncertainty avoidance and long-

term orientation as independent variables, whereas tax non-compliance intention as dependent variable.

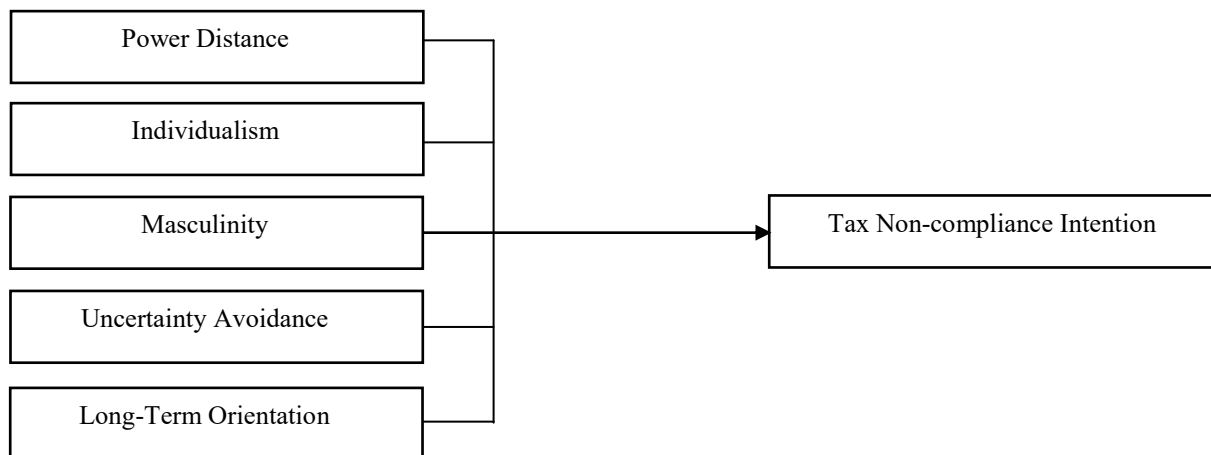


Figure 1. Research Framework.

The population comprises of SMEs registered in Malaysia under National SME Development Council (NSDC) in central region of Peninsular Malaysia. A structured questionnaire, adapted and modified from the instrument used by Hamid (2013) and Minkov and Hofstede (2012) to suit SME owners in measuring selected factors toward tax non-compliance intention, was used to administer a survey. A five-item Likert scale will be used, with a score of 5 for "strongly agree" and a score of 1 for "strongly disagree." The questionnaire was distributed and collected at random from SME owners in three states located in central region of Peninsular Malaysia, namely (1) Kuala Lumpur, (2) Wilayah Persekutuan Putrajaya, and (3) Selangor. A total of 500 samples were distributed, with 105 of them being usable, resulting in a response rate of 21 percent.

Analysis and Findings

The data has been conducted accordingly and analysed using SmartPLS version 3.3.3. In this study, all constructs are developed as reflective measurement models. Referring to Hair, Hult, Ringle and Marko (2017), the measurement model has been assessed with regards to its reliability and validity, followed by the structural model assessment by testing the hypothesised relationship. Finally, a bootstrapping method was used to evaluate the path coefficient significant and the loadings.

Assessment of PLS-SEM Measurement Model

The measurement model assesses the relationships among the indicators and the constructs. Hair et al. (2017) suggests four criteria in assessing the reliability and validity of the reflective

measurement models: (1) indicators reliability, (2) internal consistency reliability, (3) convergent validity and (4) discriminant validity.

According to Chin (1998)'s rule of thumb, the threshold values of loadings should be at least 0.708. Therefore, items with loadings below 0.708 were removed, including one item of tax non-compliance intention (INT5), one item of individualism (IND1) and two items of long-term orientation (LTO3 and LTO4). Subsequently, it increases the AVE values to be greater than 0.50 as suggested by Hair et al. (2017). With regards to composite reliability, the values are greater than 0.708 as suggested by Hair et al. Table 1 illustrates a summary of measurement model assessment.

Table 1
Results Summary of Indicator Reliability, Composite Reliability and Average Variance Extracted

Construct	Item	Loading	Composite Reliability	Average Variance Extracted (AVE)
Tax Non-compliance Intention	INT1	0.911	0.924	0.712
	INT2	0.884		
	INT3	0.915		
	INT4	0.731		
	INT6	0.758		
Power Distance	PD1	0.885	0.937	0.788
	PD2	0.937		
	PD3	0.908		
	PD4	0.818		
Individualism	IND2	0.859	0.942	0.843
	IND3	0.947		
	IND4	0.947		
Masculinity	MAS1	0.925	0.944	0.808
	MAS2	0.792		
	MAS3	0.943		
	MAS4	0.926		

Table 1 (Continue)

Uncertainty Avoidance	UA1	0.942	0.953	0.837
	UA2	0.926		
	UA3	0.942		
	UA4	0.845		
Long-Term Orientation	LTO1	0.938	0.932	0.872
	LTO2	0.930		

With regards to discriminant validity assessment, this study uses Fornell-Larcker's criterion and Heterotrait-Monotrait ratio of correlation (HTMT) as suggested by Hair et al. (2017). Under

Fornell-Larcker's approach all the square roots of the constructs are greater than their correlations with other constructs as illustrates in Table 2. Hence, the discriminant validity requirement as suggested by Ramayah, Cheah, Chuah, Ting and Memon (2018) is met. On the other hand, HTMT criterion also is met since its value is lower than 0.85 as suggested by Kline (2011). Table 3 illustrates the results of HTMT criterion.

Table 2
 Fornell-Larcker's Criterion

Construct	IND	INT	LTO	MAS	PD	UA
Individualism	0.918					
Tax Non-compliance Intention	-0.138	0.844				
Long Term Orientation	-0.203	-0.103	0.934			
Masculinity	0.049	-0.767	0.205	0.899		
Power Distance	-0.038	0.341	0.064	-0.207	0.888	
Uncertainty Avoidance	-0.060	0.722	-0.081	-0.595	0.099	0.915

Table 3
 HTMT Criterion

Construct	IND	INT	LTO	MAS	PD	UA
Individualism						
Tax Non-compliance Intention	0.152					
Long Term Orientation	0.225	0.119				
Masculinity	0.121	0.839	0.245			
Power Distance	0.093	0.358	0.082	0.213		
Uncertainty Avoidance	0.092	0.779	0.092	0.629	0.127	

Assessment of PLS-SEM Structural Model

The structural model focuses on the determination of the predictive capabilities of the model and the relationships among constructs in the model. The discussion involves: (1) coefficient of determination (R-square), and (2) path coefficients and hypothesis testing. Based on the rule of thumb provides by Chin (1998), the R-square illustrates in the above table was considered as substantial. It indicates that power distance, individualism, masculinity, uncertainty avoidance and long-term orientation can explain 74.3 percent of the variance in tax non-compliance intention.

With regards to path coefficients and hypothesis testing, bootstrapping technique use to assess the strength of the relationship as illustrated in Table 4.

Table 4
 Path Coefficient of the Model

Hypothesis	Relationship	Beta value	t-value	p-value	Decision
H ₁	PD -> INT	0.198	2.728**	0.003	Supported
H ₂	IND -> INT	-0.082	1.425***	0.077	Supported
H ₃	MAS -> INT	-0.475	4.515*	0.000	Supported
H ₄	UA -> INT	0.414	4.502*	0.000	Supported
H ₅	LTO -> INT	-0.001	0.025	0.490	Not supported

*significant at 0.01; ** significant at 0.05; *** significant at 0.10

H₁, which focuses on the significant relationship between power distance and tax non-compliance intention, reveals that power distance had a significant positive influence on tax non-compliance intention ($\beta = 0.198$, $t = 2.728$, $p = 0.003$). Thus, H₁ is supported, indicating that the likelihood of SME owners intend to engage in tax non-compliance increases as the level of power distance increases. This is consistent with Hofstede (1980), Md Radzi (2020) and Yong (2011), who found that when taxpayers perceive income inequality, they are more likely intend to engage in non-compliance, indicating that tax systems are biased.

In terms of H₂, the finding shows that individualism is negatively related to the tax non-compliance intention ($\beta = -0.082$, $t = 1.425$, $p = 0.077$). Thus, H₂ is supported, which explains that individualist SME owners are less likely intend to engage in tax non-compliance. One possible explanation given by Hofstede (1980) is people with high individualism cultural values are more likely to comply with rules and regulations because they believe policymakers apply the same value standards to all people. This is supported by Alabede (2012), Md Radzi (2020), Richardson (2008) and Yong (2011) where individualist taxpayers tend to practice full compliance with tax requirements, whereas collectivist taxpayers were not in full compliance.

With regards of H₃, masculinity is negatively significant related with tax non-compliance intention ($\beta = -0.475$, $t = 4.515$, $p = 0.000$). Thus, H₃ is supported. It means that the intention of SME owners with high masculinity cultural value are less likely to engage in tax non-compliance. Finding is consistent with the work of Md Radzi (2020) and Yong (2011), where taxpayers which more to masculinity cultural value had no problems with tax compliance and were able to pay their taxes on time to avoid being penalised by the tax authority. This is supported by Tsakumis et al. (2007), who stated that those with masculinity cultural value is less tolerant of non-compliance behaviour. Hofstede (1980) also explained that despite living in an unjust world, people with high a masculinity cultural value strive for material success, which includes ego boosting, wealth and recognition achievement.

As for H₄, there is a positive significant relationship between uncertainty avoidance and tax non-compliance intention ($\beta = 0.414$, $t = 4.502$, $p = 0.000$). Thus, H₄ is supported. It indicates that the higher the level of uncertainty avoidance, the more likely SME owners intend to engage in tax

non-compliance. One possible explanation given by Hofstede (1980), Md Radzi (2020), Richardson (2008) and Yong (2011) is that taxpayers with higher uncertainty avoidance are more likely to engage in tax non-compliance because they require written tax laws and regulations and will not tolerate uncertainty and ambiguity in complying with tax.

However, finding for H_5 reveals that long-term orientation is insignificant with tax non-compliance intention ($\beta = -0.001$, $t = 0.025$, $p > 0.10$). Thus, H_5 is not supported. It shows that long-term orientation is not an important factor to be taken into consideration in making tax-related decisions and this indicates that the tendency of SME owners who are more long-term oriented are less likely intent to engage in tax non-compliance. This finding contradicts Md Radzi (2020)'s previous research.

Conclusion

Based on empirical evidence and a theoretical perspective, this study has taken on the challenge of explaining Hofstede's Cultural Dimensions Theory to investigate the influence of culture on the tax non-compliance intention among SME owners. It discovers empirical support for Hofstede's Cultural Dimensions Theory's usefulness in explaining tax non-compliance intention. Findings suggest that power distance, individualism, masculinity and uncertainty avoidance influence tax non-compliance intention, supporting the H_1 , H_2 , H_3 and H_4 . Long-term orientation, H_5 , on the other hand is insignificant and cannot be supported.

Besides new empirical evidence and tax literature knowledge, it hopes to propose new ideas to understand the behaviour of SME owners when it comes to tax non-compliance. It is also expected to contribute to a better understanding of taxpayers' cultural value toward non-compliance intention. Although dimensions were originally used to determine organisational behaviour, it is expected to assist the Inland Revenue Board of Malaysia in implementing new strategies in raising taxpayers' awareness of potential loss to the nation due to tax non-compliance.

There are some limitations to this study, as well as some suggestions for future researchers. First, because the study was limited to the central region of Peninsular Malaysia, the findings' generalizability may be limited. Future researchers should ideally include other regions in Malaysia. Second, in examining the intention of tax non-compliance, this study only employs a non-economic approach. To solve the tax compliance puzzle, future researchers should consider economic factors as underlying by other theories. Future researchers also suggested further subdividing ethnic groups (e.g., Malay, Chinese, Indian and others) because these subgroup cultures may have different influences toward tax non-compliance.

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