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THE EFFECT OF THE INFORMATION ASYMMETRY IN THE GST IMPLEMENTATION FOR SME

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Abstract. The introduction of the Goods and Services Tax (GST) in Malaysia on April 1, 2015 has attracted the cost of compliance which would be an added burden to many Small and Medium Enterprises (SMEs). The political changes that took place in Malaysia with the appointment of a new government that had abolished the implementation of the GST on 1 June 2018. Therefore, this study is based on an agency theory involving several types of costs towards the principal and agent. Among the issues that arise in this connection are the high cost of bonding (cost of compliance), asymmetry of information and poor selection. This study uses 116 handout questionnaire techniques. The results of the analysis have shown that there is a statistically significant negative correlation between information asymmetry and the cost of compliance due to poor election action by the principal (government).

Keywords: Goods and Service Tax (GST), Agency Theory, Compliance Costs, Small and Medium Enterprises.

1.0 Introduction

The idea of implementing a goods and service tax (GST) based on the value added concept was first proposed in 1988 but it was deemed unnecessary to be implemented in view of the contribution of revenue from sales tax and service tax (SST) which were found to particularly effective then (Gomes, 2010). Later, that idea came back for discussion in 2004 but it still could not be implemented because the government felt that the use of the GST model at that time needed to be reviewed (Gomes 2010). Finally, at the tabling of the 2014 Budget (that was on 25th October 2013), the government announced that the implementation of GST would be put into effect on 1 April 2015, which was the third trial attempt for Malaysia, although the original plan was for 1 January 2007. However, the new government had abolished the implementation of the GST on 1 June 2018.

According to a study conducted by Jensen and Meckling (1976), it was stated that there would be a conflict of interest between the principal and the agent of a particular organisation if there is a change in the government policy. The implementation or compliance of a regulation will create cost that eventually relates the relationship between the principal and agent. This is consistent with studies conducted by Sapiei et al., (2017) and Sivansankaran and Dasgupta (2018) which highlighted that the higher cost of compliance due to acquiring relevant software and training for staff involved, with 77% of compliance costs incurred being internal. Based on the study by Butter and Hudson (2009), in the case of bonding cost, the government will act as a principal while company or business will act as an agent. In its role as the principal, the government should monitor the activities done by the agents by implementing regulations such as licence registration (or licence renewal), environmental audit, the inspection of corporate facilities and financial records, report submission to the revenue board and other activities which show the government interference in business affairs. The monitoring carries a significant cost, as has been pointed out in the study by Jensen and Meckling (1976), in which this cost is borne by the agent instead of principal. In this situation, there will be issues from agency which involve some kind of costs towards the principal and agent. Among the issues arise in this relationship is the high bonding cost. All the compliance costs involved to adhere to all government regulations need to be considered as bonding cost.

According to Waterman and Meier (1998) as well as Shapiro (2005), information asymmetry is described as critical assumption with regards to the model in the relationship between principal and agent. Information asymmetry is an assumption in which the agent has advantage in terms of information over the principal. Although this fact is acknowledged in every affair, according to the study conducted by Waterman and Meier (1998), it was found that the government (principal) also has advantage in terms of information over company (the agent). This is shown in the legislative nature and implementation determination process of a new regulation. If the focus is provided to the government, it is clear that the principal also has the advantage in the information asymmetry. As a result, there is an issue regarding information asymmetry of which only one side is well aware and the information obtained is also flawed. In Malaysia, the government already implemented GST since 1st April 2015. Also, the Royal Malaysian Customs Department (RMC) has profusely exposed the public about GST via its website and most companies already developed GST system and trained their employees in GST-related matters. The question is, does the government will change any actions or policies pertaining to consumption tax base after the abolishment of GST? This eventually burdens and pressures the SME companies in Malaysia later on. As a result of this situation, there will be problems in form of adverse selection and moral hazard to the businesses involved. Hence, the objective of this research is to gain evidence of the effect of the change in government policy on GST system to SME companies after the abolishment of GST.

2.0 Agency Theory

The agency theory was first introduced in the economic literature to provide a theoretical model for the relationship between a party (the principal) that delegate work affairs to another party (the agent). White (1985) had described the historical background of the relationship between principal and agent. The three ongoing significances of the agency relationship were discussed in the study. Among them is the relationships between employee and employer, shareholders and managers, and finally between creditors and shareholders. Agency theory also garnered attention in the organisational control literature (Thompson, 1967; Ouchi 1979), which presents the implication of compensation, risk and information system (Eisenhardt 1985; Eisenhardt 1988; Eisenhardt 1989). The agency theory seeks to clarify the organisational behaviour by focusing on the relationship between manager as the firm agent and shareholders as the principal. Researchers from the fields of economics (Coase 1937; Williamson 1985), finance (Jensen & Meckling 1976), accounting (Baiman 1990; Seal 2006) and new law implementation policy (Kiser, 1999; Butter, Graaf & Nijsen 2009) had also adopted the agency theory as a reference in their research.

The relationship between the principal and agent in the implementation of government regulation involves three types of cost which are much discussed in agency theory that is associated with the compliance cost (Jensen & Meckling 1976). The first type of cost is the cost associated with the government. The term that is often used in the agency theory for the relationship between the principal and agent is monitoring cost. The cost includes administration or enforcement cost along the additional costs which exist due to regulatory measure design. In addition, costs such as salary payment to the civil servants who are involved in the preparatory policy, implementation and regulatory monitoring measures are also the examples of monitoring cost. Therefore, the implementation or enforcement cost incurred by the government is generally much higher than the cost that is stated in the budget (Jensen & Meckling 1976).

The second type of cost is the bonding cost for business. This cost also includes the compliance cost. All the compliance costs involved in complying with all government regulations need to be taken into account as bonding cost. The compliance cost also includes the cost of informing the government (only the bonding cost) which can be considered as an administrative liability for the business. The debate on the reduction of administrative cost liability of government regulation is typically focused on this cost only. However, the calculation of the compliance cost can be a bit tricky (Jensen & Meckling 1976). For example, when a firm want to fulfil legal requirements in the environmental preservation or safety regulations, they need to bear all the expenses to adhere to the firm management procedures and this study only reviewed the bonding cost to be borne by SME companies only.

The last type of cost is the residual loss cost, this cost is very hard to measure and quantify. The residual loss cost is the revenue difference obtained from divergent investment decision between the principal and agent. This situation arises due to the agent reaction towards the regulations imposed by the government in which the agreement made turns out to be incomplete based on the government objective and the difference is called as residual loss (Jensen & Meckling 1976).

There is also an extensive and detailed definition of the relationship among the classical authors. Jensen and Meckling (1976) define agency relationship as a contract, in which one or more parties (the principal) engage the other party (the agent) to carry out certain service and authorise the latter to make decision on behalf of the former (Jensen & Meckling 1976). Meanwhile, the definition given by Arrow (1985) explains that there are two individuals in which the agent must select an alternative action out of several possibilities. Such actions may be detrimental to the welfare of both parties either to the agent or principal. There are factors which render the principal to set additional regulations such as rewards or bonus to control action made by the agent. There are two major problems in the relationship between the principal and agent.

The first problem is information asymmetry. It can be the potential agent has efficiency (or more general information) to fulfil the task that the principal has no expertise in (Pratt and Zeckhauser, 1985) or both parties are efficient in the area but the potential agent is going to fulfil the task at a lower cost. Information asymmetry exists because the principal cannot monitor the efficiency (hidden features), ulterior motive, hidden knowledge and hidden action of the agent and consequently the principal can only monitor the agent at high monitoring cost. Although it is acknowledged that the agent has more information in every transaction, according to the study conducted by Waterman and Meier (1998) the limit of this information asymmetry has been identified. The study explained that the government (principal) also has advantage in terms of information over business (agent). For example, this is shown in legislative nature and implementation determination process of new regulation. If the focus is provided to the government, it is clear that the principal also has the advantage in terms of information asymmetry.

The second problem that exists in the relationship between principal and agent is conflict of interest due to difference of their goals. Both parties want to maximise their utility. Jensen and Meckling (1976) define agency relationship as a contract between one or more parties (the principal) engage the other party (the agent) to carry out certain service and authorise the latter to make decision on behalf of the former. If both parties in the contract want to maximise the utility the agent certainly will not always act in the best interest of the principal. As a result, the principal will bear the monitoring cost to limit aberrant activities done by the agent. In addition, in some cases the agent will bear the bonding cost to ensure that the agent will not take certain actions which would harm the principal or to ensure that the principal will be compensated for the negligence caused by the agent.

3.0 Research Methodology

3.1 Data Collection

Babbie (2010) recommended that every researcher should balance the pros and cons of the existing method with their research context and resources. So in this study, hand delivering questionnaires to SME companies was selected as the best technique. SME companies involved only with total annual turnover over RM500,000. According to the Goods and Service Tax Act (2014), all businesses are required to register for GST if the annual taxable turnover exceeds RM500,000. Respondents were chosen randomly from various organizations based on inputs form SME Corporation Malaysia. The number of companies with the total annual turnover over

RM500,000 registered with SME Corporation was 11,440. The survey conducted in this study had 462 sample size of SME companies and the selection process was conducted by the SME Corporation which was obtained through their database.

3.2 Survey design

The survey questionnaires in this study were reused from those formulated by the researchers such as Montanheiro (1988), Lignier (2008), Abdul-Jabbar (2009) and Ibrahim (2013). All survey questionnaires were translated to Malay and English languages. The questions were split into four main sections. The second part was designed to obtain information regarding perception and view on GST. Pope (1995) stated that the taxpayer attitude and view can be investigated in a tax compliance study because it can provide the respondent with the opportunity to express their opinion. All the questionnaires in the second part were measured through Likert scale in five categories. The Likert scale was extensively used in the study of tax compliance, either at the international level (eg Richardson 2005 & Lignier2008) or even in Malaysia (see Abdul-Jabbar, 2009). All questionnaires were measured by using response scale of 'strongly disagree to strongly agree'. The third part was designed to obtain information in regards to the estimated compliance cost incurred by SME companies in developing GST system on 2017. This last section was designed to gain information related to the effect of change in the GST policy made by the government after the abolishment of GST. The three questions in this section must be answered via the five categories of Likert scale, which were measured by the response scale of ‘strongly disagree to strongly agree'.
The first part would cover the general information related to the SME characteristics which are involved in this survey. The first section was designed to gain information pertaining to the first year of business, their main activity, number of employees, paid-up share capital, the company's turnover and position held.

4.0 Data Analysis

All the survey questionnaires were sent to 462 SME companies through hand delivery. The SME companies were given 2 days to answer all the questionnaires. Only 148 out of 462 questionnaires were returned. From this amount, only 116 can be used in the analysis of this study which represented 25.11 % of the whole sample. As shown in Table 1, a total of 21 respondents commenced business in 2000 to 2017, while a total of 33 respondents commenced business in 1990 to 1999. The remaining 62 respondents started business in 1989 or earlier. The activities involved in this study comprised manufacturing activities (including agro-based), manufacturing – related services and services (including information and communications technology). Many respondents were involved in this study, i.e. a total of 60 respondents were from companies which conducted services activities (including information and communications technology). There were only 26 respondents from companies which conducted manufacturing – related services and 13 respondents from companies which conducted manufacturing activities (including agro-based). Finally, companies which conducted construction activities were the lowest contributors i.e. a total of 17 respondents. Information about the average number of employees (full-time) in 2017 indicated a total of 86.2 per cent i.e. 100 SMEs had less than 50 employees. Subsequently, companies with 51 to 150 people totalled 16 companies or 13.8 per cent. Meanwhile, for information on the company paid up capital at the beginning of the company's financial year 2017 showed that a total of 53 companies or 45.7 per cent had a paid up capital of less than RM500,000. Meanwhile, 35.3 per cent or 41 companies had a paid up capital worth RM500,001 to RM2,500,000. Following this, a total of 22 companies i.e. representing 19 per cent had a paid-up share capital of the highest rate exceeding RM2,500,001. Apart from this, information related to company turnover for the financial year 2017 on the other hand showed that the turnover rate which accounted for the lowest percentage for this study was between RM800,000 or more comprised only 4 companies. While the highest contributor comprised 61 companies that had a turnover rate of between RM500,000 and RM599,999. Lastly, respondents who had answered the questionnaires were the staffs involved in financial management. 49 of them consisted of accountants, whereas the remaining 67 respondents were the Finance Manager, Managing Director and other positions.

Table 1: Respondent Background (N=116)

Item	**Subject**	**Total SME companies**	**Sample Size (%)**
Business First Year	1989 and earlier	62	53.4
	1990 -1999	33	28.4
	2000 - 2017	21	18.2
The main business activity of company	Manufacturing (including agro-based)	17	14.7
	Manufacturing – related services	26	22.4
	Service (including information and communications technology)	60	51.7
	Construction	13	11.2
Average Number of Employees	50 and less	100	86.2
	51 to 150 people	16	13.8
Company Paid-up Capital in 2017	RM500,000 or less	53	45.7
	RM500,001 to RM2,500,000	41	35.3
	RM2,500,001 or more	22	19.0
Company Turnover in 2017	RM500,000 to RM599,999	61	52.7
	RM600,000 to RM699,999	39	33.6
	RM700,000 to RM799,999	12	10.3
	RM800,000 or more	4	3.4

Position held	Managing Director	24	20.7
	Financial Manager	29	25.0
	Accountant	49	42.2
	Others	14	12.1

4.1 Reaction and View of SME Companies to GST

4.1.1 Based on Industry

In the ANOVA analysis carried out to see the reaction and view from every SME industry on GST. In this study, the industries involved were broken down into four groups, namely manufacturing (including agro-based), manufacturing-related services, services (including information and communication technology) and construction. From the results tabulated in Table 2, it was found that there was no statistically significant difference between the industries in terms of their view and reaction on GST (F (3, 112) = 1.047, p = 0.375). However, the difference was marginal due to the effect size (see equation 1) of 0.02, which was calculated by using *eta squared* formula. According to Cohen (1998), he classifies the effect size to small (0.01 to 0.05), medium (0.06 to 0.13) and large (over 0.14). *Post-hoc* and *Turkey* analyses (see Table 3) were also conducted and the results showed that there was no significant difference between manufacturing (including agro-based) (M = 20.82, SD = 5.13), manufacturing-related services (M = 18.96, SD = 4.86), services (including information and communication technology) (M = 18.87, SD = 4.45) and construction (M = 17.92, SD = 5.72).

Table 2: One-Way Variance Analysis Test Results (ANOVA) Of SME Company Reaction and View (by Industry)

	Sum of Squares	**df**	**Square Mean**	**F**	**Sig.**	**eta²**
Between groups	72.160	3	24.053	1.047	0.375	0.02
In groups	2,573.289	112	22.976			
Total	**2,645.448**	**115**				

Table 3: One-Way Variance Analysis Test Results (ANOVA) of Reaction and View by Different SME Industries – Descriptive

	Mean	Standard Deviation	Standard Error
Manufacturing (including agro-based)	20.8235	5.12634	1.24332
Manufacturing-related services	18.9615	4.86194	0.95350
Services (including information and communication technology)	18.8667	4.45112	0.57464
Construction	17.9231	5.72220	1.58705
Total	**19.0690**	**4.79624**	**0.44532**

4.1.2 Based on Position

ANOVA analysis was also conducted to find out the effect of different positions in SME companies to the reaction and view on GST. In this study, there were four groups of position, namely managing director, financial manager, accountant and other positions. Looking at the results presented in Table 4, it was found that there was no significant difference of view and reaction between the positions (F (3, 112) = 2.504, p = 0.063). Nevertheless, the moderate difference was simply due to the effect size of 0.06 which was calculated by using *eta squared* formula. According to Cohen (1998), he classifies the effect size to small (0.01 to 0.05), medium (0.06 to 0.13) and large (over 0.14). *Post-hoc* and *Turkey* analyses (see Table 3) were also conducted and the results showed that there was no significant difference between managing director (M = 18:54, SD = 5.19), financial manager (M = 17:28, SD = 4.83), accountant (M = 11.20, SD = 3.99) and other positions (M = 20.06, SD = 5.51).

Table 4: One-Way Variance Analysis Test Results (ANOVA) Of SME Company Reaction and View (by Position)

	Sum of Squares	df	Square Mean	F	Sig.	eta^2
Between groups	166.29	3	55.433	2.504	0.063	0.06
In groups	2,479.149	112	22.135			
Total	**2,645.448**	**115**				

Table 5: One-Way Variance Analysis Test Results (ANOVA) of Reaction and View by Different Positions in SME – Descriptive

	Mean	Standard Deviation	Standard Error
Managing director	18.5417	5.19179	1.05977
Financial Manager	17.2759	4.83954	0.89868
Accountant	20.1087	3.99014	0.58831
Others	20.0588	5.51669	1.33799
Total	19.0690	4.79624	0.44532

4.2 Compliance Cost due to Information Asymmetry

Looking at Table 6, a correlation analysis (*spearman's rho*) was conducted and the test results indicated that there was a statistically significant negative relationship between information asymmetry and opportunity cost (compliance cost) which was resulted from the adverse selection action by the principal (the government). This probably due to the facts that many SMEs did not understand the GST well which resulted in some being penalised for making mistakes (Sidik et al., 2019)

Table 6: Information Asymmetry with the Opportunity Cost – Correlation Analysis

		Information Asymmetry
Opportunity Cost (Compliance Cost)	Correlation Coefficient	-0.186*
	Sig. (2-tailed)	0.045
	N	116

*. Significance level was at 0.05 (2-tailed).

Discussion and Conclusion

In the agency theory, the issue which may arise from the relationship between principal and agent was described. Arrow (1985) had adapted moral hazard and adverse selection issues stemming from the hidden action and information. If only the principal which is the government that has the advantage in terms of information, this may lead to the adverse selection issue. To reflect on these issues, an objective to identify the effect of the absence of information asymmetry on SME companies was developed and the evidence in regards to the loss incurred by the SME companies when the government changed its policy on GST system after the implementation was gathered. The results from the analysis which were carried out revealed that there was a statistically significant negative relationship between the information asymmetry and opportunity cost (compliance cost) due to the adverse selection action by the principal (the government). From the results, it was shown that if the principal (the government) decides to take adverse selection action towards the agent (SME companies) by changing in government policy on GST system after the implementation of GST, there will be certain losses as a result of this actions. Meanwhile, if the principal (the government) followed what has been planned without taking any adverse selection action, the agent (SME companies) will certainly not suffer any form of losses.

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