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## **LOW TAX RATES AND OBSTACLES ON SMES COMPLIANCE**

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### **Abstract**

SMEs has proven their existency as one of the pillar of the nation's economy when global crisis happened with their high endurance. Great amount of SMEs are really potential in increasing the nation's income on the tax field. Low rates of 0.5% that has been applied is indeed very supportive in regards to that income. But in its execution, there are still not as good as expected. There are still some obstacles faced by the SMEs so they will not or can not perform their responsibilities well. These problems were dug deeper in this research to learn about the problems faced by SMEs to fulfill their tax obligation. in-depth interview was performed to achieve the purpose of this research. This research was performed on the SMEs that has had obstacle in fulfilling their responsibilities, whether those problems are still going on or not. The result of this research shows the importance of business transaction record in the continuity of an enterprise. When a SMEs has the basic knowledge and practice on it, then this SMEs will prefer to fulfill their tax obligation. Other thing that may hinder this is their business development motivation that may hold them to fulfill their responsibilities because of the big amount of tax that need to be paid can be used to manage their business' needs. So it seems clear that the knowledge about fiscal correction in fulfilling tax obligation is also important for SMEs so they will keep obeying their tax obligation.

**Keywords:** SMEs Tax, Low Tax Rates, SMEs Compliance

### **1. Introduction**

Tax is a compulsory contribution of the people to the nation used to fund the nation's necessity for the greatest welfare of the people. therefore the nation needs tax income that will be used to fund the national development and also to achieve the goals in economy, education, social, culture, and so forth. One of the means used by the government to gain tax income is by giving conveniences to the taxpayer in fulfilling the tax obligation that have been charged to them. That is by lowering the tariff as much as 1% from omzet because the previous rates seemed to still be a burden to the SMEs.

High tax rates and complicated filing procedures were the main factors that causing non-compliance with SMEs. Other factors such as double taxation and a lack of proper enlightenment also affect the tax compliance. So it is advisable to impose a lower tax percentage to allow for

the adequacy of SME funds in developing better business opportunities and to survive in a competitive market (Atawodi, 2012). In regard to the low percentage to allow the sufficiency of SMEs funds the government has established a policy on 2018 about Government Regulation of the Republic of Indonesia No. 23 that established the final income tax of 0.5% from gross turnover. This rate of 0.5% is an optional rates because SMEs may freely decide between this final income tax rate or rather choose to refer to Article 17 of Law number 36 year 2008 about Income Tax. This article explains in detail about the rates applied to count the taxable income for personal or institution taxpayer. For personal taxpayer, taxable income until fifty million rupiahs charged with 5% rates; above fifty million rupiahs until two hundred and fifty million rupiahs charged with 15% rates; above two hundred and fifty millions rupiahs until five hundred millions are charged with 25% rates; and above five hundred million rupiahs are charged with 30% rates. Next for domestic institutional taxpayer and permanent establishment are charged with 28%. Then we can conclude that SMEs that have the economic power as taxpayer can choose the rates on the income gained by their business.

The optional choice should keep increasing the compliance to the tax obligation charged to the SMEs. The willingness to pay taxes strengthen the compliance potency of tax payment for SMEs, according to Pertestiana Damayanti (2018) who had performed her research at Magetan regency. So as with respondents from Maulida (2018) who said that their willingness to pay taxes with the new established rates. Eventhough SMEs stated their willingness, they also expect to obtain information and profound guidance for them to fulfill their tax obligations.

But based on the early observation on the implementation on the field, the research team still found a lot of SMEs that have not fulfill their tax obligations. Cahyani (2019) explained that the tax rates, tax understanding and tax sanction have positive impact on taxpayer's compliance. Based on the phenomenon where the low tax rates is supposed to affect the compliance of the taxpayer while in reality there are still SMEs that have not fulfill their tax obligations, this research is aimed to learn the obstacles faced by the SMEs in fulfilling their tax obligations. In depth, the researcher want to learn why the low rates of 0.5% is still become an obstacle for the SMEs to fulfill their tax obligations.

## **2. Literature Review**

### **2.1 SMEs**

SMEs is the backbone of the national economy, as the biggest source of GDP through the great amount of SMEs. SMEs always have the purpose to grow and develeop their business. Besides, the empowerment of SMEs is performed to manifest the balanced and just national economic structure; grow and develop the power of small, micro and medium business to become strong and independent enterprises; and also to increase the role of micro, small, and medium enterprises in the regional development, workfield creation, income equalization, economic growth, and to freed the people from poverty. Small, micro, and medium enterprise (SMEs) have the business criteria as follows :

Criteria	Micro	Small	Medium
Net worth	Rp. 50.000.000 most, land and building of the business not included.	More than Rp. 50.000.000 until Rp 500.000.000 most, land building of the business not included.	More than Rp. 500.000.000 until Rp. 10.000.000.000 most, land building of the business not included.
Annual sales	Rp. 300.000.000 most	More than Rp. 300.000.000 until Rp. 2.500.000.000 most	More than Rp. 2.500.000.000 until Rp. 50.000.000.000 most

## 2.2 Tax Compliance

Tax is a form of the country's income. As one of the form of income, tax revenue can be optimally developed in accordance to the needs and the condition of the people. Bazart (2014) found that the disadvantageous inequity in tax rates leads to a decrease in the level of reported income while an advantageous inequity decreases the level of evasion. Second, when social information is provided, i.e., when taxpayers learn the average reported income of the other group members at the end of the period, most of them adjust their current reported income up or down to be closer to the previous reported mean. one of the condition that happened is that many of SMEs still lacks in understanding the existence of tax obligations charged upon them, even until not fulfilling their tax onligations. On 2018 the government released the policy about the income tax on the income from the business accepted or earned by the taxpayer that have certain gross turnover.

Government Regulation of the Republic of Indonesia Number 23 Year 2018 is a policy on the income or earning from business that is received by the taxpayer who have certain gross turnover in one year of tax period. Rates charged on the income of that SMEs is aimed to give convenience and simplicity to the taxpayer in fulfilling their tax obligation on their income from their business activities. Other than that, it also have the purpose to help the development of the SMEs and maintain the cash flow to be able to use as the capital addition to minimalize the reason for the SMEs to not fulfill their tax obligations. This policy charged the income tax rates of 0.5% from omzet for SMEs.

Tax rates is the amount of percentage used as the foundation on the calculation of the tax amount that become the obligations to be paid by the taxpayer, in this case the SMEs. The lowering of final rates from 1% to 0.5% showed that this tax rate is one of the factor that affects the tax compliance of the SMEs.

## 2. Method

The Method section describes in detail how the study was conducted, including conceptual and operational definitions of the variables used in the study, Different types of studies will rely on different methodologies; however, a complete description of the methods used enables the reader

to evaluate the appropriateness of your methods and the reliability and the validity of your results, It also permits experienced investigators to replicate the study, If your manuscript is an update of an ongoing or earlier study and the method has been published in detail elsewhere, you may refer the reader to that source and simply give a brief synopsis of the method in this section.

This research used the qualitative method with in-depth interview. In-depth interview was chosen to be able gain the information through some open questions given by the researcher to the SMEs as the respondents. In this in-depth interview, the researcher dug deeper on the information on the adherence of SMEs in tax compliance. The researcher wanted to learn the problem of tax compliance in the respondent's perspective. In-depth interview was chosen because this is a sensitive and complex problem, besides the researcher can also obtain the information on the behaviour, knowledge, and perspective of the respondents regarding their tax avoidance problem so that the respondents may freely answer the question.

The first stage was started by giving open questions via verbal communication because of the COVID 19 pandemic. But then the researcher felt that the answer given is still lacking and still could not explain nor achieving the aim of the research, which is to learn the problems faced by SMEs in relation to their tax compliance. Therefore the researcher then tried to probes more into the interview to obtain more in-depth information directly so that the problem on the tax avoidance of SMEs in the perspective of SMEs can be obtained.

Who selected themselves into the sample. Describe the settings and locations in which the data were collected as well as any agreements and payments made to participants, agreements with the institutional review board, ethical standards met, and safety monitoring procedures.

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### **3. Results and Discussion**

Through verbal communication that had been given because of the COVID 19 pandemic, we can clearly learned that in fulfilling the tax obligation on the income from SMEs earnings, they find it difficult to fulfill the requirement of financial report. The difficulties in financial report then explained further into some things, such as the limited knowledge about the financial record,

time limit in doing the business transaction financial recording and the limit of human resources and also other resources that may help SMEs in performing their financial record.

Limited knowledge is mostly dominated by micro enterprises. In these micro business, business owner are dominated by the business motivation to just only to live on. So these business owners would not think about the need of financial record on their business transaction caused by their business motivation to only just to live on and the limit of their knowledge on the importance of business transaction record that may help in developing their business. In this micro business scale, business owners are mostly executing their business process individually, only assisted by their family. Therefore it became clearer that if the business process is dominantly performed by an individual, then it will indeed take more time even more so if they have to also do the financial record for their business transaction.

Resources limitation, whether its human resources or other supporting system via information is the further problem that the researcher obtained. Back to the discussion on the business process that became the characteristic of SMEs where mostly dominated by technical activities in performing their business. Business owners are mostly still dominantly involved in the production process, but they already have knowledge on the financial record, so they feel the need to perform financial recording on their business transaction. But, as their dominant involvement makes it difficult for them to record with accurate data, so these SMEs would feel the need of the availability of human resource who is an expert in finance and or supported by information technology resources so that they can effectively and efficiently arrange a financial record with the support of accurate data.

The next problem lays on the SMEs that have motivation in developing and up scaling their business. The huge amount of tax that become their obligation may motivate them to avoid their tax obligation. This avoidance was done because there are many SMEs that think that the nominal of the amount of their tax obligation can be used as a capital addition to develop and upscaling their business. This would not affect the tax adherence if those SMEs had been supported by human resources and or information technology resources that can help them in doing the fiscal correction. But when the SMEs is lack in understanding or do not know about fiscal correction, then it may allow the SMEs to be motivated to do avoidance on their tax obligation.

The majority of SMEs respondents, in this case the business owners, are lacking the knowledge about fiscal correction. Knowledge regarding fiscal correction can be mastered by SMEs, one of the means is from the human resources help who works in those SMEs who have the special skills related to accounting and taxation. Most of these SMEs also do not realized their willingness and worth to get a fiscal incentive that also happened in Zimbabwe based on the research result performed by Moses Jachi and Never mind Muchongwe in 2019. Through fiscal correction, SMEs may adjust (in accordance with the applied regulations) before calculating the tax on their business earnings. Many SMEs performed fiscal correction via experts in Accounting because this fiscal correction is happened because of the difference in treatment on income as well as cost between commercial accounting and tax accounting.

Experts or human resources who are skilled also can help SMEs in reporting their tax obligation without leaving the fiscal correction out is human resources available at taxation institution.

There is only a few SMEs that realize this, because most SMEs presumed that the available taxation institution only tasked to draw taxes on their tax obligation without any guidance in helping solving the problems faced by the SMEs. Fiscal correction performed by SMEs have the potential to increase their compliance in fulfilling their tax obligation. This statement is supported by the research done in Zimbabwe. Based on the existence of fiscal correction, fiscal incentives have the potential to contribute more to the survival and growth of SMEs in Zimbabwe, a step that will be advantageous to the country through the expansion of tax base in the long term, that is the main intermediary stage of increasing the government and important political development to improve the investment climate in the developing country.

So, there are two important things that should be mastered by the SMEs in fulfilling their tax obligations so that their compliance may be increased. Basic knowledge about business transaction record would really help the SMEs as the base/foundation in calculating the amount of tax that become their obligation. Furthermore for the SMEs that has performed their taxation obligation and also the SMEs that have the motivation in developing and up scaling their business may also deepen their knowledge on fiscal correction that can be accommodated by human resources who are skilled in their field. So that the compliance level on taxation obligation may increase even more.

#### **4. Conclusion**

SMEs are very aware on the importance of tax for the continuity of the country. Some problems on tax avoidance that befall on SMEs can be solved through qualitative method by in-depth interview. Fundamentally, the role of basic knowledge on business transaction record performed by the SMEs become very important to build a SMEs that is compliant on their taxation obligation. This is because the financial record on transaction as well as finance report is the foundation of the charge of income tax established for the SMEs, so the unavailability of financial record will make it difficult for SMEs to comply to the tax obligation charged upon them. There is no real foundation that can be used by SMEs as a reference in fulfilling their taxation obligation.

Furthermore, a deeper problem that was really felt by the SMEs is when the SMEs have the motivation to upscale their business. The amount of high tax on their business earnings may motivate the SMEs to do avoidance so the knowledge on fiscal correction become one of the important things to be mastered by the SMEs.

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