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MEDIATING ROLE OF TAX KNOWLEDGE ON THE RELATIONSHIP BETWEEN TAX COMPLEXITY, TAX AGENT, TAX AUDIT AND PETROLEUM PROFIT TAX EVASION: A CONCEPTUAL FRAMEWORK

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Abstract
Low tax compliance as a result of tax evasion is gradually increasing in Nigerian oil and gas sector. In addressing this concern, this study proposed a framework to investigate the extent of tax evasion amongst oil and gas companies in Nigeria. The proposed framework is based on economic deterrence theory. This study extends the current body of knowledge in taxation field by expanding economic deterrence theory with the meditating effect of tax knowledge. Also, the study would be useful in guiding stakeholders and policymakers in developing nations on the way to curb the menace of tax evasion. If validated, the framework would provide more meaningful insight on the level of tax evasion in Nigerian oil and gas sector. Nigerian policymakers would benefit immensely from the study if finally conducted as it would help the government to reduce the level of tax evasion, thereby increasing the government revenue. The proposed framework will be empirically examined via collection and analysis of the relevant data.

Keywords: *Tax evasion; Deterrence variables; Petroleum profit tax; Tax knowledge; Oil and gas sector*

1.0 Introduction

The tax is known as the sum of cash charged by the government under the law or the relevant statute, the key purpose of levying as a contribution to meet the different government expenses and the achievement of economic and social objectives in which the government wants access to(Abu Nassar, 2016). The tax also is categorized as an indirect and direct tax; indirect taxes are taxes paid by individuals and companies through the purchase of goods and services. Whereas, direct taxes are taxes that are directly related to the taxpayers (Mdanat *et al.*, 2018).

Accordingly, taxation is indeed one of the major sources of revenues, particularly, in a country like Nigeria, where government drives huge amount of resources from taxation, for instance, according to Organization for Economic Co-operation and Development OECD (2020) that tax-toGross Domestic Product (GDP) ratio in Nigeria increased by 0.6 percentage points from 5.7% in 2017 to 6.3% in 2018. Despite the increase in tax contribution to Nigerian GDP, oil and gas sector which appears to be the one which contributes the large portion of tax revenue were faces serious tax revenue decline due to monumental tax evasion in the sector (Kyari, 2013).

Furthermore, local and multinational oil companies in Nigeria have not played the anticipated role in the economic development of the country. Studies show that oil companies derive so much value from the abundant natural resources in Nigeria, without corresponding pay-back in form of contribution to the economic development. They evade taxes despite the fact they report good profit (Ogbonna, 2011). Tax evasion by both local and Multinational Oil Companies (MOCs) operating in Nigeria is high and illicit activities are very common (Oduniyi, 2004).Indeed, some studies indicate that, oil companies are not complying with Petroleum Profit Tax (PPT) laws, they are not declaring their actual income, and ultimately, they are not paying the correct amount of taxes to the relevant authorities (Ilaboya & Ofiafor, 2014; Odunsi, 2018).Which may invariably have negative implication on the overall revenue generated from this sector and eventually affect government activities negatively (Ezigbo, 2010; Adegbie & Fakile, 2011; Otusanya, 2011; Ebimobowei & Ebiringa, 2012; Ilaboya & Ofiafor, 2014; Odunsi, 2018).It is clear from the above discussion that Nigerian petroleum sector face a lot of challenges especially regarding PPT evasion. Additionally,

Oremade (2010) reiterated that oil companies are not complying with the provision of PPT and royalty in Nigeria.

Despite the significant contributions of oil and gas sector to Nigerian economy, and the exponential tax evasion therein, studies which critically examine this phenomenon are scant in the existing literature. Hence, this study proposed new framework which if validated would help in identifying the root causes of tax evasion, as well as offering solution on how the menace can be mitigated. Consequently, the study proposed to examine the mediating influence of tax knowledge on the relationship between tax complexity, tax agent, tax audit and petroleum profit tax evasion, which to the researcher knowledge has not been empirically examine, as such the study contributes theoretically and conceptually to the domain of taxation.

2. Literature Review and Hypotheses Development

This section covers literatures related to the constructs under investigations, as well as the proposed hypothesis which can help in empirical findings if validated.

2.1 Petroleum Profit Tax Evasion (Dependent Variable)

Tax evasion behaviours refer to intentional and illegal actions taken by entities or individuals with the aim of reducing their tax liabilities or completely ignore the payment of tax obligations (Alm, Bloomquist, McKee, 2017; Alm, Liu, & Zhang, 2019; Enofe, Mbele, Obazee, 2019; Gabor, 2012; Nangih & Dick, 2018). According to Alm (2012) and Korndörfer, Krumpal, and Schmukle (2014), define tax evasion as following an illicit method of prevarication or underpayment utilized by taxpayers to decrease or escape their legally due tax obligations. Sandmo (2005) described tax evasion as a violation of tax law, whereby the taxpayer abstains from reporting income, which is, in principle, taxable. Tax evasion can also be referred to as the act concealing the actual amount of a lawful transaction to avoid or eliminate tax liabilities (Tsakumis, Curatola, & Porcano, 2007).

Furthermore, tax evasion defined as the deliberate endeavor to violate or circumvent the tax law to illegally reduce tax liability (Malkawi & Haloush, 2008). Similarly, Richardson (2008)characterized tax evasion as an intentional illegal behavior or activities that involve a direct breach of tax legislation in order to prevent tax payments. In other word, tax evasion is the willful breaking of the

tax law to escape tax payment, which is indisputably forced by the law of the tax jurisdiction (Adebisi & Gbegi, 2013). According to Elffers, Weigel, and Hessing (1987) described tax evasion as any effort or action of intentional violating the law with the sole objective of reducing taxes.

Furthermore, tax non-compliance is typically indicates that the taxpayers fail to meet their tax financial liabilities (Bakar, Jaffri, Yusof, Naraini, & Mohd Tahir, 2014; Khan & Ahmad, 2014). Kasipillai (2012) indicated that the term of noncompliance includes both unintentional non-compliance and intentional evasion. Tax non-compliance is classified as tax evasion and tax avoidance (Alabede, 2012; Bakar, Jaffri, Yusof, Naraini & Mohd Tahir, 2014). Also, it can be described by other expressions such as tax evasion, fraud, mistakes, and misreporting (Abdul-Jabbar & Pope, 2008). Tax noncompliance can be taken either intentionally or unintentionally (James & Alley, 2002; Teng & Manual, 2016).Hence, PPT evasion is the dependent variable in this study.

2.2 Tax Knowledge

Tax knowledge is considered vital in shaping taxpayer's compliance behavior (Eriksen & Fallan, 1996 Mustafa, 1997; Saad, 2014). Additionally, tax knowledge is regarded as very significant factor in influencing tax compliance (Hofmann, Hoelzl & Kirchler, 2008). Weisbach (2013) argued that to determine the desirability of tax law knowledge, three essential factors must be considered. These factors are the type of the tax, expectation about the tax in the absence of knowledge and the quality of the tax. Furthermore, Loo and Ho (2005) found that individuals who lack adequate knowledge on personal taxation, may affect their tax returns negatively. As such, Dubin and Wilde (1988), McKerchar (1995), Ritsema, Thomas and Ferrier (2003), McGee, Basic and Tyler (2009) found a negative relationship between tax knowledge and tax compliance. Although, the literature on the effect of tax knowledge and tax compliance have consistently proved that, tax knowledge encourages tax compliance.

For example, Milliron (1985), Kasipillai and Jabbar (2003), Manaf (2004), Kirchler Niemirowski, & Wearing, (2006), Palil and Mustafa (2011) investigated the relationship between tax knowledge and tax compliance, and eventually found a positive and significant relationship among the variables, regardless of their different respondents. Moreover, a significant relationship was found between tax knowledge and tax compliance (Loo McKerchar, & Hansford,2009). Based on the empirical evidence presented above, this study logically argued that tax

knowledge can serves as a potential mediating variable, in other word, due to the its significant influence in shaping taxpayers compliance behavior, tax knowledge can serve as a mechanism through which the effect of tax complexity, tax agent and tax audit can be transmitted to PPT evasion.

2.3 Proposed Hypotheses

In this section, an empirical literature related to the constructs under investigation were reviewed for hypotheses development.

2.3.1 Tax Agents and PPT Evasion

Tax agents played dual roles by acting as intermediaries between taxpayers and tax authorities, and they act as advocates of taxpayers (Sinnasamy, Bidin, & Ismail, 2015). Similarly, tax agents are meant to maintain the boundaries as professionals and advocates (Bobek & Hatfield, 2003). More so, tax agents-based models are the most flexible logical tools appropriate for understanding and exploring complex systems such as tax compliance and tax non-compliance (Andrei, Corner, & Koehler, 2014).

Additionally, Harris, Hasimzade, and Ding (2016) stressed that agent-based model can be used to investigate the social and behavioral aspects of tax compliance. Notwithstanding, empirical study regarding the influence of tax agents on tax compliance provide support for the relationship. For examples, tax agents have a significant influence regarding GST implementation (Bidin, Marimuthu &Ding, 2014). Additionally, Marimuthu, Bidin and Abdul-Jabbar (2012) found positive effects between tax agents and GST implementation in Malaysia.

Moreover, Isa, Yussof, and Mohdali (2014) postulated that tax agents' involvement under SAS has a positive relationship with tax compliance. Muhammad (2017) found positive effect of tax agents in promoting compliance. Following the above findings, coupled with the lack of empirical evidence on the effect of tax agents on tax compliance in the Nigerian petroleum sector, the following hypothesis was proposed.

H1: There is no relationship between tax agents and PPT evasion.

H1a: Tax knowledge may not mediate the relationship between tax agents and PPT evasion

2.3.2 Tax Audits and PPT Evasion

Kirchler (2008) defined tax audit as the examination of organizational and individual tax reports by tax authorities to determine compliance level. Yusof, Ming Ling, Bee Wah (2014) reported that tax audit promotes extensive tax non-compliance in Malaysia. Likewise, Ahmad, Mohd-Nor and Mohd-Saleh (2008) reported that size of firms audited has significant effect on tax evasion. However, tax audit is more essential in influencing compliance especially on newly establish companies. This assertion was made by (Guala & Mittone, 2005). On his own part, Mittone (2006) found that, it is important to specifically audit inexperienced and new taxpayers because it serves as a guide to them, which will eventually make them to be more compliant.

Consequently, empirical experimental evidence on frequent tax audits has indicated a positive support with respect to tax compliance. To support this point, Alm, Sanchez and Juan (1995) compared frequent audit rates of 5%, 30% and 60% and found proportional increase in tax compliance. Similarly, in experiments by Trivedi, Shehata and Lynn (2003) it was found that when audit rates are zero, there is a tendency for non-compliance, but when the rates rose to 25%, compliance was higher. Moreover, there are other different non-experimental empirical findings on the relationship between tax audits and tax compliance. For examples, Hsu (2013) found that, tax audit greatly influences tax compliance. Additionally, Ebimobowei and Peter (2013) found a significant relationship between cut-off tax audits, conditional tax audits and random tax audits and tax compliance. Furthermore, Alm, Cox and Sadiraj (2020) argued that high audits rates increase compliance. Following the above findings, and the lack of empirical study to this effect in the upstream Nigerian oil sector, the following hypothesis was proposed.

H2: There is no relationship between tax audits and PPT evasion.

H2a: Tax knowledge will not mediate the relationship between tax audit and PPT evasion

2.3.3Tax Complexity and PPT Evasion

The term tax complexity means the presence of ambiguity in the tax laws and procedure for tax compliance (McKercher, Ingraham, & Karlinsky, 2005). More so, a positive relationship between tax complexity and tax compliance was found

by some researchers (Kirchler et al., 2006). Even though, most of the empirical evidence regarding the effect of tax complexity and tax compliance largely shows a negative relationship between complexity and tax compliance (McKerchar, 2003; Cox & Eger, 2006; Gambo, Mas'ud, Nasidi & Oyewole, 2014). Some show insignificant effect of tax complexity on tax compliance (Forest & Sheffrin, 2002). In their own study, Abdul and McFie (2020) found significant relationship between tax complexity and fairness. Ma, Guo and Yu (2020) found a significant relationship between tax complexity and tax avoidance. Furthermore, tax complexity has significant influence on tax compliance (Heang & Yongjin, 2020). Based on the above empirical evidence, followed by lack of empirical study to that effect in the upstream Nigerian oil and gas sector, the following hypothesis was proposed.

H3: There is no relationship between tax complexity and PPT evasion.
H3a: Tax knowledge will not mediate the relationship between tax complexity and PPT evasion.

2.4 Theoretical Framework

The conceptual framework is a diagram that links variables diagrammatically and logically in order to show the relationship amongst the constructs in a proposed model. The conceptual framework is needed to understand the extent of petroleum profit tax evasion behaviour of oil and gas taxpayers, specifically among oil and gas companies operating in Nigeria, such conceptual framework maybe required. To understand tax evasion behavior in Nigerian oil and gas sector, the framework of this study includes tax complexity, tax agent, tax audits and petroleum profit tax evasion, while tax knowledge serves as mediating variable. The framework is depicted in Figure 1 below.

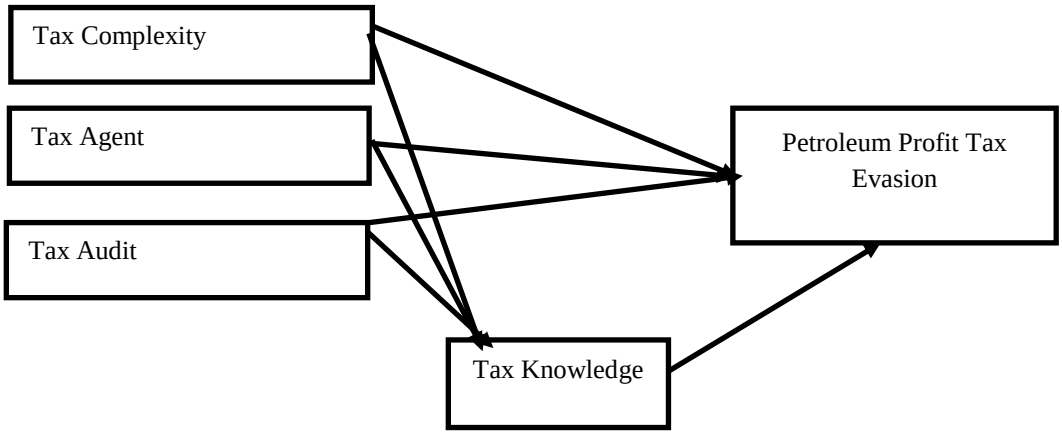

Figure 1. Proposed Conceptual Framework

3. Underpinning Theory

Underpinning theory is regarded as the foundation of scientific and philosophical studies, which assist the researcher to carry out a thorough and comprehensive work in a study. This is because it offers useful guides from the data collection point to analysis stage (Iyamu, 2013). Indeed, the rationale behind the failure of taxpayers to comply emanated from the construction of theory, which is built on the assumption that human behavior is dynamic, and this motivates all aspect of economic undertaking by individuals. The economic behavior here simply means, an individual's compare cost and benefit of their activities, which is purely based on deterrence theory (Becker, 1968; Allingham & Sandmo, 1972; Brooks, 1998).

Hence, economic deterrence theory was chosen to underpin the current study.

3.1 Economic Deterrence Theory

Initially, Becker in 1968 proposed deterrence theory by using the economic crime model, which is utilized to combat illegal actions. Becker's (1968) presumption implies that taxpayers have a rational behaviour; each taxpayer is presumed to increase the expected utility of the gamble of the tax evasion, weighing the benefits from successful tax evasion against the tax audit and penalty. This theory assumes that taxpayers prefer to evade taxes when the predicted benefit outweighs the value of legal tax statements. Likewise, this theory postulates that the decision

of taxpayers to comply is made in an environment of uncertainty based on the fear of being caught and punished.

In the study of tax evasion behaviour, the deterrence model was first formulated by Allingham and Sandmo (1972) who modified and developed the model of the economics of crime by Becker (1986). In this model taxpayers have to make the decision based on the potential cost and/or benefit of tax evasion to maximize the expected utility, taxpayers will weigh the benefits derived from evasion whether are greater than the fines or punishment when being caught later, before they decided to engage in the activities of evasion. It also depends on the level of risk preference of the taxpayers. Similarly, Hanefah (2007) argued that the principle of the theory is that if the probability of detection is high and/or punishment of the criminal is high, then this would deter individuals from committing crimes. Consequently, economic deterrence theory serves as the foundation of this study.

4. Methodology

The propositions and model set out above will be tested empirically. This study is going to employ a quantitative research approach to examine the relationship among the variables indicated in the research model; tax complexity, tax agent, tax audit and petroleum profit tax evasion, as well as the mediating effect of tax knowledge amongst the constructs. The hypotheses of this study will be tested using Partial Least Squares (PLS) path modelling. This study proposes a cross-sectional design because the data will be obtained from the respondents at one point in time. The cross-sectional design is given priority in this study because of its cost-effectiveness and timesaving (Sekaran & Bougie, 2013). In line with the previous studies taxations (e.g., Ayuba, 2016; Mas'ud, 2016), this study considers survey questionnaire for data collection purpose. The questionnaire is an appropriate approach to provide an answer to the research objectives because of its wide acceptability for data collection that entails large population, which is difficult to observe directly (Keeter, 2005). The questionnaires will be sourced from previous literatures, for instance, tax knowledge questions would be adapted from Saad (2011), tax evasion questions will be adapted from Gillingan and Richardson (2005). Additionally, tax agent's measures will be adapted from Muhd-Isa (2012), tax complexity measures will be adapted from Saad (2011) and tax audit measures will be adapted from Muhd-Isa (2012).

5. Conclusion

This study focuses on tax evasion amongst oil and gas companies operating in Nigeria. The model proposed in this work is theorised based on the extensive review of the existing literature. This study design to investigates the influence of tax complexity, tax agent, tax audit on petroleum profit tax evasion. Additionally, the paper design to examine the mediating effects of tax knowledge on the relationship between the constructs under investigation. Thus, the model is in the process of validation, if validated the model would offer more insight on the level of tax evasion perpetrated by oil and gas companies in Nigeria.

This study extends the present literature on taxation not only in Nigeria, but globally. Overall, it has been theoretically established that tax knowledge would serve as potential mediator, as such other researchers can test the effect of tax knowledge as a mediating construct in a similar complex model from different sectors of the economy. Nevertheless, since the current study is a conceptual work, the proposed model can be empirically solidified by appropriate data collection and analysis.

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