International Journal of Innovative Research and Scientific Studies, 8(2) 2025, pages: 1558-1564

IJIRSS
International Journal of Innovative Research & Scientific Studies

ISSN: 2617-6548

URL: www.ijirss.com

Trust, power and religiosity in Indonesian micro small and medium sized enterprises tax compliance

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Abstract

This study examines tax compliance among Indonesian Micro, Small, and Medium Enterprises (MSMEs) due to their crucial role as recipients of government revenue using the Slippery Slope Framework (SSF), which focuses on the role of trust, power, and religiosity (karma phala) in shaping taxpayer behavior. A survey of 145 MSME taxpayers in Bali and 121 taxpayers in Malang-Surabaya was conducted, and data were analyzed using Structural Equation Modeling-Partial Least Squares (SEM-PLS). The study findings reveal that trust and power significantly influence tax compliance, with karma phala strengthening this relationship. In addition, tax compliance rates are higher in Bali than in Malang-Surabaya, indicating the influence of cultural and religious factors. By integrating karma phala as a moderating variable, this study extends the SSF and underscores the importance of trust-based and enforcement-based approaches in driving compliance. These insights highlight the need for tax policies that combine transparency, consistent enforcement, and cultural considerations to improve compliance among MSMEs.

Keywords: Authority, Power, Karma Phala, MSMEs, Tax Compliance, Taxpayer Trust.

DOI: 10.53894/ijirss.v8i2.5513
Funding: This study received no specific financial support.
History: Received: 27 January 2025 / **Revised:** 28 February 2025 / **Accepted:** 6 March 2025 / **Published:** 20 March 2025

Competing Interests: The authors declare that they have no competing interests.
Authors' Contributions: All authors contributed equally to the conception and design of the study. All authors have read and agreed to the published version of the manuscript.
Transparency: The authors confirm that the manuscript is an honest, accurate, and transparent account of the study; that no vital features of the study have been omitted; and that any discrepancies from the study as planned have been explained. This study followed all ethical practices during writing.
Publisher: Innovative Research Publishing

1. Introduction

Tax compliance remains a subject of global research interest, particularly in endeavors to enhance tax compliance levels in developing nations. Indonesia, categorized as a developing country, exhibits relatively low tax compliance compared to other nations. For instance, Indonesia's tax ratio in 2019 was recorded at only 11.6%, significantly below the

IMF’s tipping point value of 15% in the same year. This condition highlights the need to improve Indonesia's tax performance to address potential financial deficits.

Micro, small, and medium-sized enterprises (MSMEs) are recognized as crucial drivers of economic growth in both developed and developing countries [1], including Indonesia. Tax revenue from MSMEs forms an important part of the Indonesian government's income. MSMEs contributed 61.07% to the GDP, equivalent to IDR 8,573.89 trillion [2]. Furthermore, MSMEs play a strategic role in Indonesia’s national economy due to their greater resilience in crises compared to larger businesses [3]. Research, such as that by Campin, et al. [4], highlights the potential of MSMEs to improve community welfare, as their growth often outpaces that of large corporations [5]. However, this significant growth has not been matched by their tax contributions [6].

Before the advent of modern theories on tax compliance, such as the Slippery Slope Framework (SSF), tax compliance research was primarily grounded in economic theory. Foundational studies, including those by Allingham and Sandmo [7] and Srinivasan [8], applied the economic theory of crime to tax avoidance. Over time, interest in the broader factors influencing tax compliance expanded, leading researchers to explore psychological and social dimensions of taxpayer behavior. For example, Dulleck, et al. [9] elucidated that increased stress levels could prompt taxpayers to disregard tax regulations. Similarly, Damayanti, et al. [10] analyzed tax compliance through a social-psychological lens. Despite these developments, much of the existing research still emphasizes economic aspects, particularly sanctions and fines.

The Slippery Slope Framework (SSF), introduced by Kirchler, et al. [11], integrates economic and psychological factors to explain taxpayers' compliance behavior. The framework is based on two key dimensions: trust and power. Trust reflects taxpayers' confidence in authorities who act fairly and are committed to societal welfare. Power, on the other hand, represents taxpayers' perception of the authorities’ ability to detect and penalize tax evasion. Tax compliance increases with rising trust in or power of the tax authority, with compliance manifesting either voluntarily (due to heightened trust) or enforced (due to increased power).

This study advances the existing literature in several significant ways. First, while the Slippery Slope Framework has been widely tested in developed economies [11, 12], its application in developing countries, particularly those with diverse religious and cultural landscapes like Indonesia, remains underexplored. Indonesia's position as the world's largest archipelagic state, combined with its substantial MSME sector contributing 61.07% to GDP [2], provides a unique context for examining how the SSF's core premises operate in a developing economy setting.

Second, this research enhances the SSF by incorporating karma phala as a moderating variable, addressing calls in the literature for a more nuanced understanding of cultural influences on tax compliance [13]. While previous studies have examined religiosity's role in tax compliance [14, 15], the integration of specific religious principles into established theoretical frameworks remains limited. This study's focus on karma phala's moderating effects provides novel insights into how religious values shape the relationships between trust, power, and compliance, particularly relevant in societies where religious principles significantly influence business practices.

The Indonesian context offers compelling grounds for investigation for several reasons. Despite being Southeast Asia's largest economy with a GDP of USD 1.19 trillion, Indonesia's tax-to-GDP ratio (11.6%) remains significantly below the IMF's minimum threshold of 15%. This gap is particularly pronounced in the MSME sector, where despite contributing substantially to GDP, tax compliance remains disproportionately low [6]. Understanding the cultural and religious factors influencing this compliance gap is crucial for developing effective policy interventions.

The comparison between Bali and the Malang-Surabaya area provides a natural experiment for examining how different cultural contexts moderate tax compliance mechanisms. Bali's predominantly Hindu population, with its strong adherence to karma phala principles, offers a distinct cultural setting compared to the more religiously diverse Malang-Surabaya area. This regional comparison enables the investigation of how varying degrees of religious adherence influence the effectiveness of trust-based versus power-based compliance strategies, addressing a significant gap in the literature regarding the role of cultural context in tax compliance [15, 16].

This research is particularly timely given Indonesia's ongoing tax reform efforts targeting the MSME sector. Recent government initiatives, including the implementation of digital tax systems and simplified tax regulations for MSMEs, make understanding cultural and religious influences on compliance especially relevant. By examining how karma phala moderates the trust-power dynamics proposed in the SSF, this study provides practical insights for developing culturally sensitive compliance strategies.

Moreover, this research contributes methodologically by testing the SSF in a novel cultural context while incorporating religious values as moderating variables. This approach not only extends the theoretical framework but also provides a more comprehensive model for understanding tax compliance in culturally diverse settings. The findings have implications beyond Indonesia, offering insights for other developing nations with diverse religious and cultural landscapes seeking to improve tax compliance among MSMEs.

The study's focus on regional variations in religious adherence and their impact on tax compliance mechanisms addresses a significant gap in the literature. While previous research has established the importance of cultural factors in tax compliance [17], few studies have systematically examined how specific religious principles moderate the effectiveness of different compliance strategies. This research's examination of karma phala's moderating effects provides a framework for understanding how religious values interact with institutional factors to shape taxpayer behavior.

2. Literature Review

2.1. The Influence of Trust on Tax Compliance

The first perspective of the Slippery Slope Framework (SSF) posits that tax compliance is influenced by trust [11, 18]. Trust refers to taxpayer's belief that tax authorities are reliable and just in administering tax revenues. Enhancing trust in tax authorities is expected to foster higher levels of compliance [19]. In fact, trust is recognized as the strongest predictor for tax compliance [12, 20, 21]. Furthermore, trust in government is also closely linked to taxpayers' compliance behavior [22]. Based on these premises, the first hypothesis is proposed:
Hypothesis 1: Taxpayer trust positively influences tax compliance.

2.2.The Influence of Power on Tax Compliance

The Slippery Slope Framework also suggests that regulatory strategies grounded in deterrence enhance taxpayer's perception of the tax authorities' power, leading to compliance motivated by coercion [11]. Power is defined as the taxpayer's perception of the tax authority's ability to detect and penalize tax violations [23]. Evidence from previous studies supports this notion. For instance,Bernasconi, et al. [24] demonstrated the impact of audits, while [25] highlighted the role of fines in reinforcing the authority's effectiveness.

Research focusing on individual taxpayers and small business consistently reveals a positive relationship between the authority's power and tax compliance. Studies have shown that high levels of authority power positively affect compliance [12, 19, 26-29]. Accordingly, the second hypothesis is proposed:
Hypothesis 2: Authority power positively influences tax compliance.

2.3. The Impact of Trust and Power on Tax Compliance with the Moderation of Karma Phala

Religiosity, defined as a person's belief in values that guide behavior, is recognized as a potential factor influencing tax compliance [14]. Religiosity can function as an internal control, encouraging taxpayers to align their behavior with religious beliefs. It is also seen as a factor in people's ability to control their actions and outlook on life [14]. Therefore, a person's religiosity strengthens their compliance [30].

Hinduism has a belief in cause and effect, which is often understood as karma phala. Karma phala is a central concept in Hindu teachings, stating that every action (karma) carried out by an individual will produce consequences or fruits (phala), which can be good or bad. In the context of paying taxes, karma phala can motivate Hindus to fulfill their tax obligations responsibly, as they believe that good deeds, such as paying taxes honestly, will produce good results, both in this life and in the next. Belief in philosophical and religious values can prevent taxpayers from committing fraud or deviating from compliance, as they may fear the moral and existential consequences of the mistakes they make. Studies by Gilligan and Richardson [31] and Richardson [15] confirmed the positive relationship between religiosity and tax compliance. Further empirical research shows that religiosity moderates tax compliance, as demonstrated in a study conducted in Nigeria [32]. Therefore, the following hypothesis is proposed:
Hypothesis 3: Karma phala strengthens the effect of trust on tax compliance.
Hypothesis 4: Karma phala strengthens the effect of power on tax compliance.
Hypothesis 5: Variations in tax compliance exist between MSMEs in Bali and Java (especially Malang-Surabaya area).

3. Methodology

This study developed a conceptual framework and analytical model based on previous theoretical studies and research findings. These served as the foundation for formulating hypotheses and interpreting the research results. The conceptual framework for this research is presented in Figure 1. The research focused on MSME taxpayers in Bali and Java, particularly the Malang-Surabaya area. Primary data were collected through questionnaires completed by respondents. The questionnaire was divided into four sections, corresponding to the study variables: trust, power, karma phala, and MSME taxpayer compliance. A Likert scale ranging from 1 to 7 was employed, with response options of 1: Strongly Disagree, 2: Disagree, 3: Somewhat Disagree, 4: Do not Know, 5: Somewhat Agree, 6: Agree, and 7: Strongly Agree. This study involved 145 MSME taxpayers in Bali province and 121 taxpayers in Java, specifically the Malang-Surabaya area.

The survey conducted in this study did not involve collecting sensitive personal data, nor did it include questions that could raise significant ethical concerns. The respondents in this study do not belong to vulnerable groups, such as children, individuals with learning disabilities, cognitive impairments, or those in dependent or unequal relationships. The target population for this study exclusively consists of MSME owners or managers responsible for business decision-making. The questions in the questionnaire were specifically related to the professional behavior of the respondents. No personal data that could expose respondents to harm, stigma, or legal repercussions was collected. The information gathered pertained solely to decision-making behaviors. Furthermore, this study complies with widely accepted ethical standards, including obtaining prior consent from all participants and ensuring the confidentiality of the information provided. All data collected was anonymized and kept confidential, used solely for academic purposes, and not retained or reused once the study concluded. Given that the research involved non-sensitive data and was conducted to ensure complete anonymity, it was determined that ethical committee approval was not required. The ethical integrity of the study was preserved by ensuring that all procedures followed conformed to established ethical guidelines.

The survey for this study was distributed to respondents through the Google Forms platform. Before completing the questionnaire, respondents were required to read and accept the terms, specifically acknowledging that the data collected would be anonymous and confidential, used exclusively for academic purposes, and not for any other purpose once the study was completed. This process ensured that written consent was obtained and that participants were fully informed of the confidentiality and anonymity of their responses, thereby minimizing any potential ethical concerns.

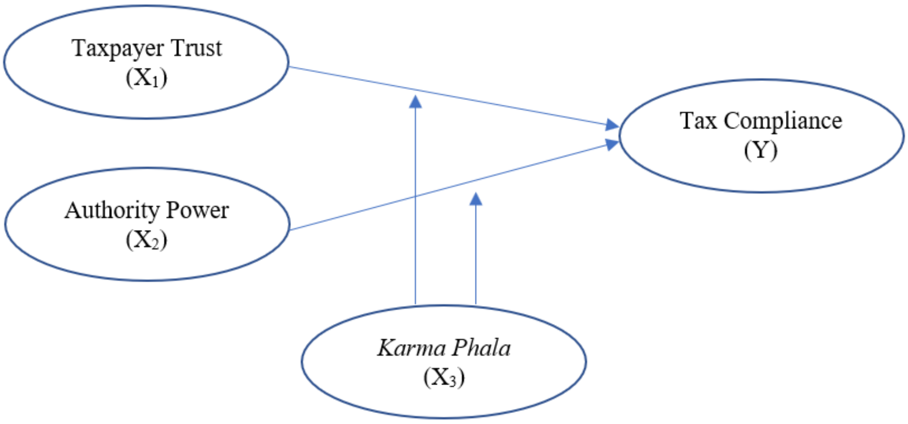

Figure 1.
Conceptual framework of research.

The research instrument consisted of statements provided to the respondents to measure four variables. The first variable, trust (X1), refers to the taxpayer's belief that the tax authority acts in the public interest and fulfills its responsibilities reliably. The second variable, power (X2), represents the taxpayer's perception of the tax authority's capacity to detect violations and impose fair sanctions. The third variable, *karma phala* (X3), is an essential aspect of religious teachings associated with tax morality. It motivates taxpayers to sincerely report tax obligations, voluntarily pay taxes, and be aware of the tax system. Religiosity, as described by Barro and McCleary [30], encourages individuals to adopt specific behaviors aligned with their beliefs. The fourth variable, tax compliance (Y), is defined as the taxpayer's willingness and ability to comply with tax laws. Compliance is influenced by ethical considerations, environmental factors, and contextual circumstances at a given time and place [33]. It encompasses accurately reporting income, correctly calculating tax liabilities, and making timely tax payments.

4. Results

4.1. Reliability Test

This research uses SEM-PLS analysis, emphasizing the reliability of measurement instruments, specifically questionnaires designed to collect data from respondents. Instrument reliability is crucial to ensure consistent and dependable data, particularly in SEM-PLS analysis. The reliability testing was carried out using Cronbach's alpha, a widely used method to assess internal consistency among questionnaire items. This study's criteria stipulate that composite reliability is significant if it exceeds 0.7, and Cronbach's alpha values above 0.6 are considered acceptable.

Table 1.
Reliability test results

Variable	Cronbach's Alpha	Composite Reliability	Results
Tax payer Trust	0.954	0.956	Reliable
Power of Authority	0.933	0.933	Reliable
Karma Phala	0.913	0.935	Reliable
Tax Compliance	0.953	0.955	Reliable

Source: Data processing result (2024).

The reliability test results in Table 1 demonstrate a high level of reliability for all instruments, with Cronbach's alpha values exceeding 0.7. These findings confirm that the instruments meet the criteria and are appropriate for measuring all latent variables. Furthermore, the reliability scores above 0.9 validate the questionnaire as a robust and consistent tool for exploring the respondents' perceptions and views on tax compliance.

4.2. Path Coefficient (Hypothesis Testing)

The path coefficient is a statistical approach used to evaluate relationships between variables based on sample data. It indicates the influence between variables, with significance determined by the P-value. For this study, the rule-of-thumb significance level is set at 5%. The results of the PLS analysis are detailed in Table 2 and Figure 2.

Table2.
Hypothesis test results.

	Original Sample	Standard Deviation	T Statistics	P-value
Trust ⟶ Tax Compliance	0.289	0.059	4.896	0.000
Powers⟶ Tax Compliance Authority	0.332	0.056	5.926	0.000
KP*Trust⟶Tax Compliance	0.103	0.057	1.801	0.036
KP*Powers⟶Tax Compliance	0.298	0.078	3.817	0.000

Note: KP: Karma phala

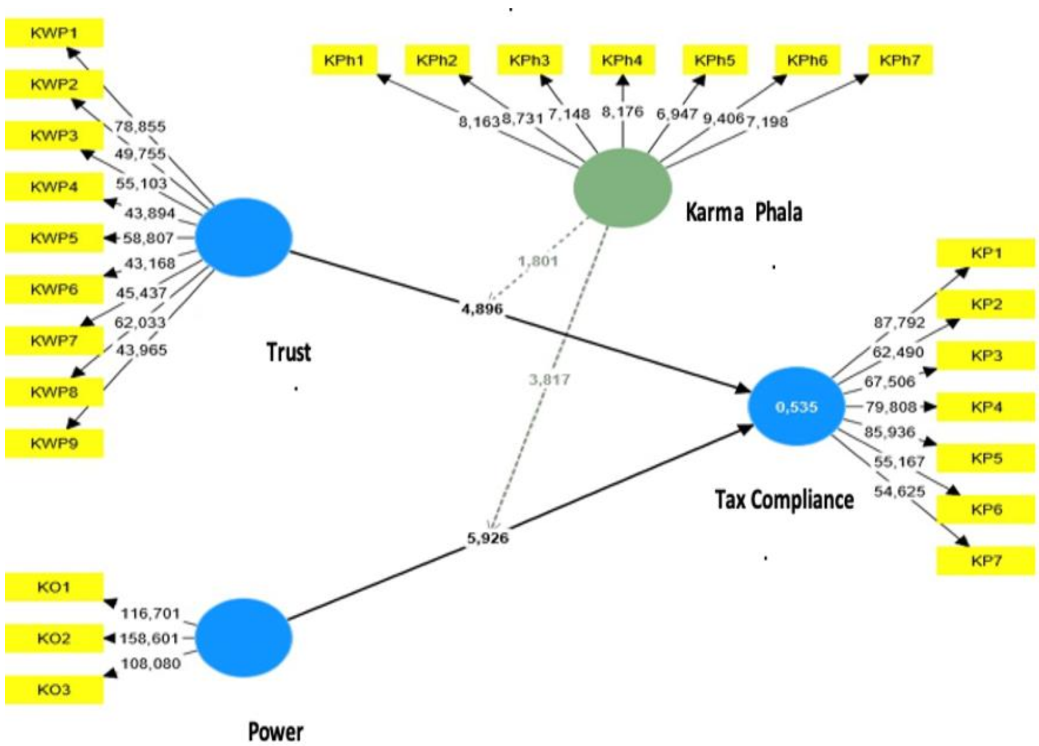

Figure2.
Inner Model

Based on Table 2, trust significantly influences tax compliance, with a P-value of 0.000 ≤ 0.05, supporting the acceptance of H1. These results indicate that taxpayer trust positively affects tax compliance. Greater trust in the Directorate General of Taxes (DJP) leads to higher tax compliance. This finding aligns with Djajanti and Subekti [34], who stated that trust in tax authorities is built on their positive attitude and commitment to serving citizens' interests. Gobena and Van Dijke [28] further emphasized factors contributing to trust, such as the competence and consistency of tax authority and tax services, transparency in tax use, benefits of tax authority policies, satisfaction with problem solutions, trust in tax officials' decisions, respect for tax authorities, and knowledge of tax authorities.

Further, power also significantly influences tax compliance, with a P-value of 0.000 ≤ 0.05, leading to the acceptance of H2. These findings demonstrate that the appropriate use of power by the DJP, including sanctions and tax rate determination, enhances tax compliance. This aligns with the Slippery Slope Framework, which underscores the necessity of power to enforce compliance [35]. Taxpayers are more likely to comply when authorities have sufficient enforcement capacity [34], ensuring collective adherence to applicable tax regulations.

Karma phala strengthens the relationship between trust and tax compliance, as evidenced by a P-value of 0.036 ≤ 0.05, leading to the acceptance of H3. This finding suggests that karma phala moderates the said relationship and that higher Hindu religious religiosity enhances the role of trust in fostering tax compliance.

Table3.
Difference test results

Comparison	Average	T-Stat	P-Value	Decision
Bali	28.6414			
Malang and Surabaya	26.8430	2.595	0.002	There are differences

Source : Data processing result (2024).

Karma phala also moderates the influence of power on tax compliance, with a P-value of 0.000 ≤ 0.05, supporting the acceptance of H4. The results highlight that the Hindu religious values amplify the authority's role in encouraging tax compliance, demonstrating that religiosity reinforces the impact of both trust and power.

The analysis in Table 3 reveals significant differences in tax compliance between MSMEs in Bali and Java (specifically in Malang and Surabaya), with a P-value <0.05. Tax compliance levels are higher in Bali compared to Java indicating regional variations influenced by cultural or contextual factors.

5. Conclusion

This study employed the Cronbach's alpha method to assess the internal consistency of questionnaire items, emphasizing the pseudo-reliability of the instrument to ensure consistency and reliability of the data obtained. The results indicate a high level of reliability for all instruments, with Cronbach's alpha value exceeding 0.9, meeting the established reliability standards. This finding confirms the questionnaire's capability as an accurate and consistent measurement tool.

The hypothesis testing using path coefficients in the SEM-PLS analysis revealed significant relationships between the observed variables, supported by the P-values below 0.05. The findings demonstrate the positive and significant influence of trust and power on taxpayer compliance, aligning with the Slippery Slope Framework. The impact of taxpayer trust on compliance is corroborated by prior studies [16, 27, 36, 37]. This research provides a robust empirical basis for understanding that the level of taxpayer trust can positively impact tax compliance. This trust encompasses confidence in the equity of the tax system, as well as trust and other psychological factors that encourage taxpayers to fulfill their tax obligations. Similarly, the positive influence of authority power on tax compliance is supported by previous research [17, 36]. This research provides evidence that power can be an essential factor in increasing tax compliance. The effective application of sanctions and consistent law enforcement can encourage compliance behavior. The moderating role of karma phala further strengthens the impact of trust and power on tax compliance. The P-value below 0.05 underscores the significant role of religious religiosity, particularly Hindu teachings, in enhancing these relationships.

This research also examined regional differences in tax compliance among MSMEs in Bali and Java (specifically the Malang and Surabaya areas). The statistical analysis revealed noteworthy differences, with higher compliance levels observed in Bali. These findings are consistent with Kirchler and Wahl [38], who suggested that tradition can influence tax compliance among small businesses. Overall, this research confirms the reliability of the measurement instruments used and demonstrates significant relationships between the observed variables and the research hypotheses. The moderating role of religious religiosity, particularly in the context of karma phala, adds a valuable dimension to understanding tax compliance dynamics. The observed differences in tax compliance between MSMEs in Bali and Java (Malang and Surabaya) may stem from variations in economic and business conditions, such as income levels, industry structure, or market characteristics. Socio-cultural factors, including values, norms, and religiosity, likely also play a role in shaping attitudes towards tax compliance. Additionally, the effectiveness of tax administration – encompassing information accessibility, rule clarity, and procedural ease – may influence MSMEs' ability to fulfill their tax obligations. These regional disparities can directly impact state revenue from the MSME sector. Lower compliance in one region could reduce expected tax revenue, highlighting the need for targeted government interventions to improve compliance and oversight.

While this study provides robust findings, generalizing these results to a broader population requires caution due to sample limitations. The geographic focus was restricted to Bali and Malang and Surabaya, potentially overlooking variations in other regions. Future research should expand the sample to include diverse geographic, demographic, and industrial contexts. Such studies can offer a more comprehensive understanding of how the observed variables influence tax compliance across broader populations.

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