



VAT Compliance Challenges Among SMEs: Evidence from Saudi Arabia

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Abstract

Purpose: The study addressed Value Added Tax compliance challenges facing small and medium enterprises in Saudi Arabia and rank these challenges based on their relative impacts. The research addressed four major challenges: the complexity of VAT system design, lack of VAT knowledge of taxpayers, high compliance cost, and multiple fines and audits.

Methodology: A survey research design was employed to collect relevant data from SMEs using a self-designed questionnaire, which was sent to 200 enterprises of which 97 was returned.

Findings: Results revealed that out of the four challenges, imposing rigorous fines was the most VAT compliance challenge facing SMEs, and compliance cost was the least. The study showed that equipping taxpayers with adequate tax knowledge and proper education reduces compliance costs and fines and increases compliance

Originality/Value: The study contributed to the understanding of the VAT system and possible mediation of challenges that enhance the level of VAT compliance. It is hoped that the forwarded recommendations can be helpful for researchers and policymakers investigating the implications of VAT and the enhancement of compliance.

1.0 Introduction

Small and medium enterprises (SMEs) play a vital role in the acceleration and stability of economic growth and the creation of sustainable employment (Krasniqi, 2007). Even though it was widely acknowledged that SMEs were significant drivers to economic diversity, the Saudi government has firmly prioritized the development of SMEs in its 2030 Vision. The Vision was introduced to reduce oil revenue dependence and build a sustainable economy by concentrating on strength areas and specific monetary policies and controlling budgetary deficits (Besley and Persson, 2011, 2014; Sana and Khan, 2018). The need for additional government revenues to close the fiscal gap brought about a significant Saudi tax policy change. One tax policy alternative that has been contemplated in the context of deficit reduction proposals in Saudi Arabia has been the introduction of a Value-Added Tax (VAT). VAT enforcement has been a considerable challenge for most Saudi Arabia enterprises since it is recent, unexpected, and uncommon. Ever since VAT represents the most challenging requirement that an enterprise has to deal with. Clearly, VAT impacts all business activities, and the design of the VAT system and its administration processes significantly influence all kinds of enterprises, specifically SMEs (Engelschalk, 2004). SMEs are facing greater inefficiencies in coping with the inherent burdens of VAT compliance, as they often have limited financial, human, and technical resources compared to large companies (Junpath et al., 2016; Retief, 2010).

Tax compliance is seen as onerous, time-consuming, and troublesome regulations, especially in developing countries that struggle to improve their tax revenue efficiency to meet their financial needs (SBP, 2003). Governments will continue to impose rigorous VAT regulations, creating more challenges to businesses' accessibility and records administration. Companies have to keep accurate and detailed financial records and supporting documents, including ledgers and invoices. Also, they must file returns in a specific format conforming to regulatory requirements and provide tax authorities with timely reports and relevant information to execute audits to assure adherence and compliance to VAT

requirements and law. Businesses have to adhere to returns filing guidelines and audit procedures and submit their financial records and supporting documents in a specific timeframe with smooth access to avoid penalties. Kicher (2013) asserted that the current tax corporate systems are burdensome, on SMEs, especially with a self-assessment structure.

Despite the importance and wide acceptance of SMEs as an essential stimulus to the development of any economy, few studies address compliance challenges facing SMEs, which menace their survival (SBP, 2003). SMEs are the prime center of this paper's attention, as they represent the major source of tax revenue in most developing countries, including Saudi Arabia, and their compliance enhances government tax revenue. Compliance of SMEs leads to a stable tax system and contributes significantly to achieving the objectives for which VAT has initially been initiated. Further, the lack of research on SMEs' VAT compliance practices in Saudi Arabia has given this research great importance.

This study aims to address VAT compliance challenges facing SMEs in Saudi Arabia, especially about the impact of VAT system design, tax knowledge, compliance costs, fines and audits, and to rank identified challenges based on their relative effects on SMEs. The findings of this study will provide a significant contribution to the understanding of the VAT system in Saudi Arabia and possible mediation of challenges, which eventually will enhance the level of VAT compliance for SMEs. This study can generally help researchers and policymakers investigate the implications of VAT and improve the compliance of SMEs in Saudi Arabia.

2.0 Literature Review

2.1 VAT Compliance

VAT is the primary source of indirect tax revenues and was introduced 80 years ago and remained limited to a few countries until the 1960s. Bizualem (2015) asserted that VAT had become an essential and indispensable component of tax reform in developed and developing countries. Today, VAT is an immense and reliable source of government revenue for most countries. Bird (2005) defines VAT as a tax imposed on goods as produced and distributed and services as rendered. VAT is ultimately

borne by the end consumer and is collected through traders, manufacturers, or importers. Businesses are often offset VAT paid on inputs against outputs, and practices vary in how offsetting is implemented.

Tax compliance is growing and a major issue worldwide as taxpayers are expected to find ways to evade tax or reduce their tax liability (Bird, 2005). The term compliance is complex and has a broad meaning (Walsh, 2012), but in general, the term can be referred to the degree to which taxpayers comply with the tax regulations. Accordingly, VAT compliance refers to preparing and submitting VAT returns and payments on time (Roth et al., 1989; Brown and Mazur, 2003; Yergenthren and Rajendra, 2018). Businesses are seen as compliant if they have completed tax registration and filing processes. Plumley (1996) asserted that VAT compliance is the accurate self-assessment of VAT owed and the voluntarily and timely filing, reporting of the required information, and VAT payment. Compliance can be achieved either by the enforcement of tax authorities or by the voluntary willingness of taxpayers. Considerable research has been done covering various VAT compliance issues on large enterprises; however, compliance among SMEs has attracted very little attention (Andreoni et al., 1998), an alarming situation given the great importance of SMEs taxation and the inception of VAT in a vast majority of countries including Saudi Arabia. This research study will contribute to the literature by addressing VAT compliance challenges among SMEs in Saudi Arabia.

2.2 VAT Compliance Challenges

The literature points to several VAT compliance challenges, especially in developing countries centered on VAT-specific designed features and policies. These include parametric issues on registration, base, rates, exemptions, zero-rating, return filing, thresholds, and refunding (Grandcolas, 2005; Adade, 2012; Mataire and Prescott, 2010; Ojeka and Ojochugwu, 2012). Other studies went further and have identified and linked compliance challenges to other variables as fundamental determinants of VAT compliance, namely VAT policy simplicity; perceived VAT benefits; audits and detection probabilities; satisfaction and perceived role of a tax authority; awareness on fines and penalty; financial constraint of taxpayers; and rational accounting

(Lewis, 1982; Webley et al., 1991; Elffers et al., 1991; Cowell, 1992; Plumely, 1996; Blumenthal et al., 1998; Hyun et al., 2002; Barbuta-Misu, 2011; Yong and Hooper, 2011).

Grandcolas (2005) asserted that VAT compliance depends on three key elements: the VAT administration system's quality, the designed features of the VAT, and the proper and consistent enforcement of penalties. Lumumba et al. (2010) found a strong link between SMEs' attitudes and non-compliance in Kenya as they felt paying an unfair share of tax. Similarly, Maseko (2014) assessed the impacts of Zimbabwean SMEs' perceptions towards fairness and quality of the taxation system, tax knowledge, and compliance costs on tax compliance and concluded that these factors significantly affect SMEs' compliance attitudes and decisions.

VAT compliance challenges vary among countries and enterprises. Eichfelder and Schorn (2008) noted that SMEs experience a higher compliance burden as they face tremendous tax-enforced procedures irrelative to their scale. Luiz (2002) asserted that SMEs in South Africa were facing a complicated tax system, making them unable to become compliant and effectively manage compliance costs. In line with that, Mataira and Prescott (2010) studied SMEs in New Zealand and found them having difficulties filing tax returns, especially in their early years of operation. Odongo (2011) conducted a study on SMEs in Uganda and concluded that most enterprises lacked compliance because they are ignorant of tax operations and computations. Ojeka and Ojochugwu (2012) found out that high VAT rates and complex VAT procedures led Nigerian SMEs to become non-compliance.

2.2.1 Complexity of VAT System

The design of a VAT system is essential in achieving high compliance and minimizing the compliance burden. Krever (2008) affirms that “to a very large extent, the potential effectiveness of a VAT depends on the fundamental design of the legislation as well as the way the design is translated into law” (p.9). In practice, tax policies and procedures are complex and create uncertainties. Theoretically, VAT administration and relevant laws and regulations seem very clear on documents but practically are seen as complicated, making uncertainties to taxpayers during implementation. In this regard, different

interpretations, conflicting and puzzled practices often emerge among tax officials and taxpayers. Accordingly, tax complexity refers to the difficulties encountered by taxpayers in reading, comprehending, and interpreting tax laws and the time they consumed, and the cost they incurred in complying with these laws. Ideally, a conceptually burdensome and unreasonably complex VAT would have multiple rates, a different threshold, numerous exemptions, frequent returns, zero-rating, and multiple fines and audits (pope, 1993). It is beyond the aim of this paper to address all VAT system features. Inquisitive researchers can refer to other studies for more details of VAT design.

The complexity of VAT design entails higher compliance costs and increases the probability of non-compliance as taxpayers are given the justification to evade or avoid tax. Luiz (2002) noted that SMEs in South Africa failed to comply lawfully due to the complexity of the tax system and the high costs incurred to handle tax procedures and requirements effectively. Similarly, Ojeka and Ojochugwu (2012) found out that complex VAT procedures accompanied by high VAT rates provided Nigerian SMEs with an excuse to evade tax.

2.2.2 Lack of VAT Knowledge

Tax knowledge is vital for compliance due to its strong association with taxpayers' ability to understand tax law and its regulation (Singh, 2003). Taxpayers have to understand the tax rules which are imposed on their financial transactions. If the tax rules are clearly understood, tax compliance will increase and enhance voluntary compliance, especially in getting the tax liability calculations correctly (Olowookere and Fasina, 2013; Kasipillai, 2010). The tax language of the tax law must be clear and straightforward as it includes tax aspects such as familiarity with the tax system, knowledge of tax obligations, and sources of relevant tax information (Richardson; 2006; Jared, 2016; Alghanmi,2014). Richardson (2006) asserted that taxpayers are generally unwilling to comprehend complex tax laws, and this has a great reflection of their inclination to comply and the level of tax knowledge they gain.

Numerous researches have been carried out asserting that tax knowledge possession positively affects tax compliance (Kasippilai, 2000; Loo, 2006; Kicher, 2013; Palil & Mustapha, 2011; Kassim, 2013; Odongo, 2011). Loo (2006) stated that tax knowledge

is a primary factor under the self-assessment system as it determines the compliance behavior of taxpayers. Kasippilai (2000) also documented that having proper tax knowledge is associated with a higher compliance level. The converse is also true; limited or improper tax knowledge intentionally or unintentionally leads to a lack of compliance. Odongo (2011) conducted a study on SMEs in Uganda and concluded that many enterprises are ignorant of tax operations and computations, hence, lack compliance. Bizualem (2015) studied the reasons for the non-compliance of many businesses in Ethiopia and indicated that many taxpayers lack the skills to provide accurate information on total sales, especially VAT.

Education is linked to compliance and non-compliance (Prince & Anayduba, 2014; Witt and Woodbury, 2013; Wong and Lo (2015). Palil & Mustapha (2011) explained that tax compliance could be enhanced by educating taxpayers, thereby enabling them to comply. Mukhlis et al. (2014) carried a study on Indonesian SMEs to assess if tax compliance is strengthened through some tax education and showed that SMEs were able to understand their tax obligations and responsibilities better when trained well. Wong and Lo (2015) reached similar results and argued that tax compliance could be improved via different forms of tax education. Therefore, general tax knowledge is essential for understanding tax regulations to comply with tax laws as taxpayers will be more aware of their responsibility and possible penalties to be imposed in case of non-compliance.

2.2.3 High Compliance Cost

Compliance with tax laws requires much effort to occur. Compliance must be created, cultivated, monitored, and enforced in all countries. Economically, an effort is just another word for cost, and tax compliance costs have been a concern for centuries. Costs of tax compliance referred to all costs paid or incurred to ensure proper tax compliance, including expenses related to keeping records and invoices, costs incurred in preparing and submitting all tax returns, costs associated with the time spent to manage and assure compliance, costs of professionals and consultants to address and deal with disputes with tax authorities, cost of updating accounting system to ensure the integrity of the data flow entered into and processed to obtain

accurate outputs, and any other costs to ensure compliance (Gurd et al., 1998; Evans, 2006; Arendse et al., 2006; Smulders & Stiglingh, 2008; Govender, 2008; Jared, 2016). VAT compliance cost affects the behavior of taxpayers as high compliance cost leads to tax evasion. Deogratius (2017) argued that tax compliance costs negatively affect tax compliance behavior which eventually influences compliance.

The cost of compliance is burdensome to SMEs (SBP, 2004). Relative to assets value and sales, SMEs incur more compliance costs than that of large businesses as the costs are disproportionate to their size, i.e., the smaller the enterprise, the higher the compliance cost (Slemrod & Venkatesh, 2002; Weichenrieder, 2007; Rametse, 2010; Yergenthren and Rajendra, 2018). SME taxpayers need to have profound bookkeeping skills and plenty of time preparing and submitting tax returns, hence more compliance costs. These requirements and other VAT provisions represent a significant challenge to SMEs, particularly during start-up and growth years, and affect SMEs' cash flow as the VAT provisions require sales to be taxed regardless of collection (SBP, 2003). Yergenthren and Rajendra (2018) conducted a study on 85 South African SMEs and concluded that VAT compliance is one of the most complex matters for SMEs. They argued that time consumed in compliance was one of the highest costs. They found that the age of SMEs in South Africa, on average, doesn't exceed three and a half years due to the enormous costs of compliance. Another study by Rametse (2010) with a sample of 868 SMEs found that the pre-implementation and start-up of VAT were heavily costly for these enterprises.

2.2.4 Multiple Fines and Audits

Voluntary tax compliance is unnatural and will not happen without continuous enforcement and punishment (Bird and Casangera, 1992). VAT compliance mainly occurs if taxpayers perceive the probability of detection and prosecution to be high and the penalty for non-compliance to be rigorous. According to Abel Myburgh (2016), the degree of compliance depends on how taxpayers perceive the likelihood of being detected and penalized and how they perceive the harshness of the fines. Artur (2015) argues that VAT fines are helpful in addressing tax compliance challenges and should be designed to dissuade taxpayers of tax non-compliance and

motivate the increase of tax compliance level. Cruce (2011) stated that to maintain the tax system's creditability, fines have to be enforced fairly, rigorously, and instantly. Ahiawodzi and Adade (2012) observed that the frequency of audits has a significant impact on voluntary compliance as taxpayers associate this with the perception of the likelihood of being caught. Jared (2016) argued that the highest deterrence levels from cases of tax non-compliance are achieved if there is a combination of effective fines and frequent audits. Heard (2005) asserted that fruitful deterrence requires well-planned auditing procedures and highly qualified tax inspectors with excellent investigation skills.

Empirical research indicates that both fines and audits lead to greater compliance. Park and Hyun (2003) found that both penalties and audits motivated taxpayers to increase compliance in Korea; however, the study showed that fines were found to be more effective than audits. Similarly, Asnawi (2016) found a positive relationship between audit and compliance rates in Indonesia. Naibei et al. (2012) assessed VAT compliance on 233 companies in Kenya, and the results showed that compliance level was higher with firms that had undergone a tax audit and concluded that tax audits could deter tax evasion. Mararia (2014) assessed the relationship of fines and audits and tax compliance on 100 SMEs in Nairobi and found a significant positive relationship. He concluded tax revenue collections increased due to the severity of penalties.

2.3 SMEs and VAT System in Saudi Arabia

Historically, SMEs' policies were introduced on a limited scale in the fifth development plan (1990-1995) even though there was broad recognition of the importance of SMEs in the diversification of the Saudi economy. The fifth plan was geared toward introducing specific regulations to increase SMEs' contribution, mainly in the industrial sector, due to the remarkable rise and growth of the petrochemical sector in the 1980s. Recently, Saudi Arabia has launched its Vision 2030, which entails objectives to accelerate SMEs' growth. Since then, significant reforms and initiatives have been adopted and gradually implemented to boost SMEs' empowerment. One of the key objectives outlined in the Vision was raising the

SME's contribution from 21% of the non-oil GDP to 35% and boosting entrepreneurship to promote more SMEs' founding.

The VAT system in Saudi Arabia was introduced for the first time in January 2018 at 5%. Then, the Saudi government has launched multiple VAT reforms over the past three years to align the system with international standards, adapt to the economic development in Saudi, and modernize governance and administration of the system. The first two reforms came as an increase in the VAT rate and VAT registration threshold. The General Authority of Zakat and Tax (GAZT), the tax system administrator in Saudi Arabia, has increased the VAT rate from 5% to 15% from the beginning of July 2020. The International Monetary Fund (IMF) has advised Gulf Cooperation Countries including Saudi Arabia, to strengthen government finance policy, reduce Saudi's dependence on oil and gas revenue in the longer term, improve fiscal sustainability and diversify revenues, and possibly enable the government to cope with the pandemic of Covid-19 and the effect of it on the economy. Also, the registration threshold, which started at SAR 1million, was increased to SAR375000. Further, two more reforms were introduced later in 2020 when the VAT rate in real estate was decreased from 15% to 5%, and the e-invoicing was announced to be implemented in December 2021.

VAT online registration is compulsory in Saudi Arabia for all business that makes taxable supplies of 375000 Saudi Riyal or more per annum; however, businesses can voluntarily register. GAZT classifies the VAT registered businesses for returns filling into two distinguished categories. The first category includes companies having annual sales exceeding SAR 40 million, and they are required to submit their VAT returns monthly. The second category includes companies with less than SAR 40 million sales, and they can submit quarterly. The deadline for VAT filling and payment is the last day of the following month/quarter of the tax filling unless a refund is expected or is due to the taxpayer. In the case of late registration, filling, and payments, different fines are charged to taxpayers (see Table 1). Fines are duplicated in most cases, as GAZT carries out audits a few years after the filing of returns because of the lack of qualified tax staff.

In December 2020, GAZT announced the implementation of e-invoicing regulations to be effective and mandatory for all taxpayers on December 4th, 2021 where all taxpayers must become ready to issue, receive and store e-invoices (first phase). The integration and connection will be executed in progress starting from 1st January 2023 (second phase), which establishes the integration between the electronic systems for taxpayers and the GAZT's system. Electronic invoicing aims to convert paper invoices and credit and debit notes into an electronic process that allows the exchange and processing in a more structured electronic format. This move towards tax digitization enables GAZT to gather real-time tax information and respond directly and quickly to non-compliance issues. Such amendments require all kinds of enterprises to update their VAT financial and accounting modules to meet and adhere to the new requirements. For Saudi SMEs to achieve the transition successfully, they will need to ensure that their accounting software is fit and compatible with the VAT portal of GAZT to transfer tax-relevant data smoothly. Needless to say, not all VAT registered SMEs in Saudi are aware of this shift, and concerns remain that many of them will still use and operate in the manual realm of documentation and accounting records. A significant number of SMEs will need consultants to secure online access for the first time, making VAT a substantial administrative burden. Further, some SMEs might need to purchase new accounting software packages to adhere to this new regulation.

Currently, most Saudi goods and services are subject to a 15% VAT rate with few exemptions. The Saudi VAT system, modeled on the traditional western VAT, allows certain goods and services to be exempted while others are zero-rated. Exemptions include primarily financial, medical, residential housing, and educational activities. Real estate is zero-rated if for residential rent and first housing if less than SAR 850,000. Commercial and residential housing above the base is taxed at 5%. Education programs are exempted for programs with a duration of 2-year and above, including undergraduate and postgraduate programs. Educational programs less than two years are taxed at 15%. Expatriates are taxed with 15% at all academic

programs. Soon, it is expected to shift postgraduate programs from being exempted to taxed at 15%.

The Saudi VAT system, like other countries, allows for particular special consideration for SMEs having taxable sales below a certain threshold, including a less frequency filling, use of cash accounting, tax exemption, and simplified invoicing. These considerations reduce both the compliance costs for SMEs and the administrative costs for the government and GZAT. Even though these considerations are offered for SMEs, the literature discussion shows that the VAT system in Saudi is perceived to be burdensome and unreasonably complex. To begin

Table 1. GAZT Fines List

Description of Act	Fine
Submit false documents to evade the payment or reduce VAT due or unlawfully obtain refunds for tax	At least the amount of the VAT due, up to three times the value of the goods or service subject of the evaded tax
Move or attempt to move goods in or out of Saudi Arabia without paying the VAT due.	
Failure to apply for VAT registration	SAR 10,000
Failure to submit the Tax Return	5% - 25% of the value of the Tax that would have had to be declared
Failure to pay the tax due	5% of the value of the unpaid tax for each month or part thereof the Tax has not been paid
Issuance of Tax Invoice by non-registered Person	Maximum SAR 100,000 without prejudice to any stricter penalty provided in any other law
Failure to keep Tax Invoices, books, records, and Prevention or obstruction of GAZT employees from Violation of any provision of the VAT Regulations or	Maximum SAR 50,000
Filing an incorrect tax return, amend a tax return, or file any document resulting in a lower amount due	50% of the value of the difference between the calculated Tax and the Tax due

Source: GAZT website

with, having multiple amendments in a short period poses a question of the VAT system's complexity and its consequences on SMEs. The majority of SMEs have to adhere to tax policies and procedures similar to that of large businesses even with limited knowledge and resources capacity, file VAT returns every quarter, apply accrual accounting, generate and store invoices soon in an advanced electronic

format through an electronic solution, face multiple fines, and deal with many exemptions. This complexity makes compliance burdensome and raises costs of compliance, particularly for SMEs. These challenges which SMEs in Saudi are exposed to need to be addressed, and this study aims to achieve that. Therefore, this study presents two primary questions to achieve the objectives as follows:

1. What are the VAT compliance challenges facing SMEs in Saudi Arabia?
2. What is the ranking of the addressed VAT Compliance challenges?

3.0 Research Methodology

3.1 Data Collection

This study adopted a survey research design as the primary data and used relevant reports, academic articles, and internet and library sources as secondary data. Data were primarily collected through a self-designed questionnaire using online google form both in English and Arabic languages. The questionnaire included a covering introduction to clarify the research objectives and the researcher's guarantee of information security to encourage respondents to answer the listed questions and increase the response rate effectively. It was divided into five sections: general information, the complexity of the VAT system, VAT knowledge, compliance costs, and fines and audits. All questions were closed-ended except for some general information, and responses were captured in a five-point Likert scale.

3.2 The Sample population

The target sample of this study was SMEs operating in Saudi Arabia and registered for VAT purposes. The sample comprised a total of (200) randomly selected SMEs from the registered taxpayers in the database of GZAT. Out of the surveys sent online to respondents, a total of (97) were returned. The response rate was 48.5% and is deemed suitable to achieve the objectives. Classification of SMEs in this study is according to the definition of SMEs given by the General Authority for Small and Medium Enterprises (Monshaat) in Saudi Arabia. A very tiny enterprise is an enterprise: (1) with sales of SAR 3 million or less; and (2) employing 5 persons or less. A small enterprise is an enterprise: (1) with sales of SAR 3-40 million; and (2) employing 6-50 persons. A medium enterprise is an enterprise with: (1) with sales of

SAR 40-200 million; and (2) employing 50-250 persons. The study sample comprises a selection of employees who are specialized in accounting and business-related subjects and holding different positions.

4.0 Empirical Results and Discussion

Table 2 summarizes the characteristics of the respondents. The majority of the responses (61.9%) were received from males, and (99%) of respondents having qualifications of bachelor degree and above. Of the final responses received, the majority (95.9%) of these enterprises were classified as medium-sized and small. The remaining (4.12%) were very tiny enterprises. An overwhelming (89.5%) of the respondents had no VAT training (73.2%). (86.6%) of the respondents specialized in accounting and (86.6%) of them had six years of experience and above. Most of the respondents (52.4%) were holding accounting and finance positions.

4.1.1 Complexity of VAT System

The analysis of the data confirmed that the majority of respondents (86.7%) believed that the VAT system in Saudi Arabia is complex, hence, represents a challenge to SMEs. The complexity of the VAT law poses a challenge and creates uncertainty in the interpretation of laws resulting in low tax compliance levels. As shown in Table 3, respondents were asked about the clarity and readability of VAT laws and regulations and, to some extent, the results show that only (76.3%) were able to understand and comprehend the law even though most of the respondents possess a high level of qualifications. The consequence of being unable to understand VAT laws eventually leads to non-compliance among taxpayers due to the knowledge gap.

Respondents' perception of the complexity of the VAT system could be interpreted due to the recent inception and implementation of VAT in Saudi Arabia, i.e., 2018, the multiple

Table 2. General Information of Respondents

	Answers	Freq.	Percent		Answers	Freq.	Percent
Gender	Male	60	61.9	VAT Training	Yes	10	10.3
	Female	37	38.1		No	87	89.7
	Total	97	100.0		Total	97	100.0
Qualification	Diploma	1	1.0	Specialty	Accounting	71	73.2
	Bachelor	84	86.6		Finance	2	2.1
	Master	9	9.3		Business	7	7.2
	PhD	3	3.1		Other	17	17.5
Total	97	100.0	Total	97	100.0		
Annual Revenues	Less than 187,500	14	14.4	No. of Employee	0-5	4	4.12
	187,500 To 375,000	6	6.2		6-50	34	35.1
	375,000 To	8	8.2		51-250	59	60.8
	More than	69	71.1		Total	97	100.0
	Total	97	100.0		0-5 years	13	13.4
Position	Senior	10	10.3	Experience	6-10 years	26	26.8
	Partner	5	5.2		Above 10 years	58	59.8
	Internal Auditor	5	5.2		Total	97	100.0
	Auditor	26	26.8		Less than 35	39	40.2
	Accountant	20	20.6	Age	36-50	47	48.5
Other	31	31.9	Above 50		11	11.3	
Total	97	100.0	Total		97	100.0	

reforms that took place in a short period since inception, and lack of VAT proper training and education as shown in Table 2. Consistent VAT laws mean the tax system is less complex and will encourage tax compliance. Typically, taxpayers come from different backgrounds with different knowledge levels; hence a simple tax system can enhance compliance among all taxpayers. Therefore, GAZT should aim to simplify VAT laws through rewriting VAT legislation into easy-to-read and understand language. To improve compliance, GAZT is supposed to contemplate the impacts of new reforms on SMEs before introducing recent VAT reforms and amendments. GAZT should conduct more VAT-related workshops and conferences to educate SMEs taxpayers, engage professionals and academics in disseminating current VAT information to all taxpayers, establish designated offices and customer relationship management or front service desk to cater to special needs and inquiries of SMEs. The results of this study in the effect of the complexity of the VAT system on VAT compliance are consistent with the literature (pope, 1993; Luiz, 2002).

Table 3. Complexity of VAT

Statements		Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	SD
VAT system in Saudi Arabia is complex	F	1	2	8	16	70	4.57	0.82
	%	1.0	2.1	8.2	16.5	72.2		
VAT law and regulations are clear and easily read	F	2	9	12	33	41	4.05	1.05
	%	2.1	9.3	12.4	34.0	42.3		

4.1.2 Lack of VAT Knowledge

Several questions have been designed in the questionnaire to address the effect of taxpayers' knowledge and training on VAT compliance in SMEs in Saudi Arabia. The results presented in Table 4 revealed that the majority (89%) of respondents agree that taxpayers' knowledge positively influences VAT compliance. The more knowledge taxpayers have during filling and submitting VAT, the lesser the challenge to SMEs and the greater the compliance level.

Table 4. Lack of VAT Knowledge

Statements		Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	SD
Taxpayers' knowledge positively influences VAT compliance	F	1	2	5	31	58	4.47	0.78
	%	1.0	2.1	8.2	16.5	72.2		
Taxpayers possessing VAT knowledge helped in compliance	F	2	9	12	33	41	4.05	1.05
	%	2.1	9.3	12.4	34.0	42.3		
VAT training programs must be attended to attain VAT knowledge	F	-	1	6	39	51	4.44	0.66
	%	-	1.0	6.2	40.2	52.6		
VAT training programs attended with GAZT helped attain proper knowledge	F	1	3	27	44	22	3.86	0.84
	%	1.0	3.1	27.8	45.4	22.7		

However, lack of VAT knowledge was not seen as a challenge to SMEs. The result in Table 4 shows that lack of knowledge was not a significant compliance challenge among SMEs probably because the majority of respondents, as shown in Table 2 (76.3%), possesses good VAT knowledge and have high educational qualifications with a minimum of bachelor degree (86.6%) with proper specialty-i.e., accounting (73.2%).

As shown in the results in Table 4, (92.8%) of the respondents believe training is essential in equipping SMEs with VAT knowledge to interpret the tax regulation better, hence increasing their compliance positively. Indeed, tax compliance challenges can be reduced by providing relevant tax training and education, which

will reduce the tax inclination to evade taxes. Such a high result provides evidence of the inherent desire of SMEs in Saudi to understand the law and be compliant, albeit for rigorous and instant fines policy adopted in the system. However, the results show that SMEs in Saudi are lacking proper training. The results in Table 4 show that offered training programs were not much satisfactory and beneficial; thus, GAZT should seek to tailor training programs to fit the taxpayer's requirements. Only (66.1%) of the respondents were satisfied with received training. This result raises questions over the quality and relevance of offered training by GAZT. Taxpayers, especially SMEs, are in need of more tailored training to enhance their knowledge and understanding of the complex VAT law and regulations. Training programs are necessary for equipping taxpayers with proper tax knowledge to help SMEs become more compliant. GAZT should give training more consideration to ensure that it is relevant to the need of SMEs and other taxpayers.

The results of this study in the effect of possession of knowledge and education on VAT compliance are consistent with the literature, which asserted that the level of understanding and tax knowledge greatly affects the level of compliance with the VAT (Kasippilai, 2000; Loo, 2006; Kicher, 2013; Palil & Mustapha, 2011; Kassim, 2013; Jared, 2016; Mohd, 2010).

4.1.3 High VAT Compliance Cost

The researcher sought to know respondents' opinions if the cost incurred to comply with VAT represents a challenge and if such cost negatively affects the level of compliance. As shown in Table 5 below, compliance costs were, to some extent, not burdensome for SMEs in Saudi Arabia as only a few respondents (39.2%) perceived it as such. Further, the results also show that (25.8%) of the respondents believe that compliance cost has a negative effect on VAT compliance in SMEs in Saudi. Hence, it can be stated that the compliance cost is not seen as a compliance challenge to SMEs in Saudi Arabia.

This result of the study is inconsistent with much of the literature studies, which showed that compliance costs negatively influence VAT compliance (Jared, 2016; Deogratius, 2017). The inconsistency might be due to the differences in the economic

and regulatory context and the reliance on electronic modes and possession of the respondents' high education level

Table 5. High Compliance Cost

Statements		Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	SD
The cost incurred to comply with VAT is very high	F	3	19	37	28	10	3.24	0.99
	%	3.1	19.6	38.1	28.9	10.3		
The cost incurred to comply with VAT law affects the level of compliance negatively	F	6	25	41	20	5	2.93	0.96
	%	6.2	25.8	42.3	20.6	5.2		

However, the move towards invoice digitization in Saudi is expected to increase compliance costs in the short and medium term. Most SMEs would have to hand over such tasks to consultants at some expense. Besides, for SMEs to digitize transitions successfully, they will have to ensure their financial software and documentation and record processes are compatible with the GAZT portal to meet the digitization requirements. SMEs have different accounting systems, and all of them need to be digitally linked, which will be a practical challenge for them. In economic terms, of course, need is just another word for cost. Concerns remain that extra costs will incur, and not all VAT registered SMEs can afford such costs easily; some will still use manual records, thus lacking compliance.

4.1.4 VAT Fines and Audits

Respondents have been asked two questions concerning fines and audits to identify whether SMEs see them as a compliance challenge. The result in Table 6 shows that (73.2%) of the respondents believe, to some extent, that fines and audits increase the level of VAT compliance of SMEs in Saudi Arabia. This result is consistent with Jared (2016), who concluded that fines and penalties influence the level of VAT compliance; also consistent with Artur (2015), who argued that the VAT penalties should be designed to dissuade taxpayers of tax non-compliance and to motivate them to increase the tax compliance level.

The researcher sought to know whether SMEs in the sample have ever been audited and fined for non-compliance. The result shows that few SMEs (23.7%) have been fined; hence, SMEs are compliant. This result means that the effort made by GAZT to enhance VAT compliance through audits and rigorous and instant fines is paying off

as SMEs in Saudi Arabia strive to avoid penalties and audits. This result is consistent with Abel (2016), who stated that compliance is more likely to occur when the probability of detection is perceived to be high, and fines for non-compliance are perceived to be rigorous. The high VAT compliance level among SMEs in Saudi Arabia could be related to the stringent fines policy imposed in Saudi Arabia. As shown in Table 1, fines in Saudi Arabia could reach up to three times the value of the goods or service subject to the evaded tax, as the fine calculation is made from the filing of returns and payment to the time of audit and in most cases, audits are conducted years after the filing and payment of VAT. In most cases, SMEs' failure to file and pay the accurate VAT for any reason is considered an evasion. Such tax policy represents a significant challenge to SMEs and creates more burden on SMEs who lack experience and leads to a profound negative effect on SMEs and their cash flow.

Table 6. Multiple Fines and Audits

Statements		Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	SD
Multiple fines and audits increase the level of VAT compliance of SMEs	F	2	7	17	37	34	3.97	1.00
	%	2.1	7.2	17.5	38.1	35.1		
Fines have been imposed on my company as a result of audit due to non-compliance	F	26	19	29	10	13	2.64	1.34
	%	26.8	19.6	29.9	10.3	13.4		

4.2 Ranking VAT Compliance Challenges

The researcher sought to rank VAT compliance challenges based on their impacts on SMEs. The results in Table 7 show that the highest VAT compliance challenge is fines and audits with a mean of (4.40), followed by lack of knowledge, complexity, and compliance cost. Most of the respondents (82.4%) have ranked fines and audits as the major challenge facing SMEs, and this is consistent with several studies (Ahiawodzi and Adade, 2012; Artur, 2015; Abel Myburgh, 2016). These studies found that both fines and audits motivated taxpayers to increase compliance and lead to greater compliance. As discussed early, the way fines and audits are implemented in practice in Saudi has made this feature of the VAT system the most challenge facing SMEs. To defend themselves during audits, SMEs must first pay the fines levied VAT variation before their appeal can be accepted and reviewed. Appeals are decided by

Committees supervised by GAZT, and they are a lengthy process, and such policy creates a significant challenge to SMEs and their cash flow. Such an approach does not take into consideration the limited financial and technical capacity inherent in SMEs.

The results have shown that respondents have ranked lack of VAT knowledge and training as the second challenge to SMEs as educated respondents in this study realized the importance of their knowledge in understanding the complex VAT laws and regulations and achieving compliance, and minimizing the cost of compliance. The result is consistent with other studies show that that adherence to tax regulations is higher with VAT knowledgeable taxpayers. Lack of knowledge makes SMEs face more challenges in the interpretation of VAT laws and regulations, increasing their compliance costs. The results have shown that respondents in the study were equipped with the proper knowledge then have ranked the complexity of the VAT system and cost of compliance as less challenging to them. Therefore, equipping taxpayers with tax knowledge makes them more compliant. Lack of knowledge and uncertainty of tax laws could entail applying wrong tax provisions regardless of taxpayers' willingness to comply. The level of education and training received by taxpayers significantly reduce non-compliance and the inclination to evade taxes.

Surprisingly, the results show that respondents have ranked high compliance costs as the least compliance challenge. This result is probably because registration and filing are done online. Also, the general information in Table 2 shows that most of the respondents are educated and experienced, so the cost of compliance is irrelevant. Another explanation is that the strict fines policy implemented by GAZT makes compliance costs much less than fines for non-compliance, so SMEs strive to bear costs.

Table 7. Ranking VAT Compliance Challenges

Statements		Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree	Mean	SD	Ranking
The complexity of the VAT system is a compliance challenge to SMEs	F	-	4	12	27	54	4.35	0.85	3
	%	-	4.1	12.4	27.8	55.7			
Lack of VAT knowledge is a compliance challenge to SMEs	F	-	2	14	25	56	4.39	0.81	2
	%	-	2.1	14.4	25.8	57.7			
High VAT compliance cost is a compliance challenge to SMEs	F	1	2	22	49	23	3.94	0.80	4
	%	1.0	2.1	22.7	50.5	23.7			
Complicated VAT fines and audits are compliance challenges to SMEs	F	-	3	14	21	59	4.40	0.85	1
	%	-	3.1	14.4	21.6	60.8			

5.0 Conclusion

This study aimed to address and rank VAT compliance challenges facing SMEs in Saudi Arabia. The research has ranked fines as the most compliance challenge. VAT compliance is mainly achieved through audits and rigorous as taxpayers are keen to comply to avoid severe fines. VAT compliance in Saudi Arabia is high and not costly, as taxpayers possess good VAT knowledge and process their returns, payments, and appeals online. The paper concluded that equipping taxpayers with VAT knowledge reduce compliance cost and increase compliance. Taxpayers with high qualifications and proper training can interpret tax law, and such understanding makes them more compliant.

The VAT system in Saudi Arabia has been seen as complex. The results from this study enable policymakers aware of VAT compliance challenges and the burden and issues that SMEs are exposed to in their journey of VAT compliance. Policymakers need to address these issues and design appropriate strategies that consider the interests of both governments and taxpayers. Based on the study result, considerable attention should be paid to taxpayers' education and VAT regulations training. Constant training should be offered to taxpayers to equip them with relevant knowledge and any new VAT reforms.

More work is necessary to study other VAT compliance challenges not covered in the study. Future studies should further investigate the complexity of the VAT system in

Saudi Arabia to simplify the system and assure a better compliance level by taxpayers. Future studies should also assess the impact of the expected implementation of e-invoicing and investigate the challenge SMEs might have concerning this. The study has its limitation as targeted respondents do not represent the broad population of SMEs in Saudi Arabia.

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