Governance Quality of Political Stability and Rule of Law on Tax Compliance: A Mediation Analysis of Tax Morale
(Kualiti Tadbir Urus Kestabilan Politik dan Kedaulatan Undang-undang Mengenai Pematuhan Cukai: Analisis Pemboleh Ubah Pengantara Moral Cukai)

Mohd Allif Anwar Abu Bakar
(Faculty of Business, Economics and Accountancy, Universiti Malaysia Sabah)
Mohd Rizal Palil
Ruhanita Maelah
(Faculty of Economics and Management, Universiti Kebangsaan Malaysia)

ABSTRACT

The unresolved tax compliance dilemma gives a signal of consideration/ requirement of additional factors that will influence tax compliance, such as a governance-based approach. This paper investigates the association between governance quality and tax compliance, with tax morale as a mediator. Two dimensions of governance quality were considered: political stability and the rule of law. A quantitative survey of 592 salaried and self-employed taxpayers in East Malaysia was conducted. Partial Least Squares-Structural Equation Modelling (PLS-SEM) was used to analyse the data. Theoretically, the present research contributed to knowledge by supporting the significant role of tax morale in the mediation association between the rule of law and tax compliance. Tax compliance can also be improved when taxpayers have high tax morale. Practically, the findings aid policymakers and governments that an ideal governance mechanism via a stable political environment is crucial to increasing tax compliance. Nevertheless, the government's approach to enforcing an effective rule of law was viewed as a more promising strategy for boosting the morale of taxpayers.

Keywords: Political stability; rule of law; tax compliance; tax morale; mediation

ABSTRAK

Dilema pematuhan cukai yang tidak dapat diselesaikan memberikan isyarat pertimbangan/ keperluan faktor tambahan yang akan mempengaruhi pematuhan cukai seperti pendekatan berasaskan tadbir urus. Kajian ini mengkaji perkaitan antara kualiti tadbir urus dan pematuhan cukai, dengan moral cukai sebagai pengantara. Dua dimensi kualiti tadbir urus telah dipertimbangkan: kestabilan politik dan kedaulatan undang-undang. Tinjauan kuantitatif terhadap 592 pembayar cukai bergaji dan bekerja sendiri di Malaysia Timur telah dijalankan. Partial Least Squares-Structural Equation Modelling (PLS-SEM) telah digunakan untuk menganalisis data. Dari aspek teori, penyelidikan ini menyumbang kepada pengetahuan dengan menyokong peranan penting moral cukai dalam hubungan pengantara di antara kedaulatan undang-undang dan pematuhan cukai. Pematuhan cukai juga boleh dipertingkatkan apabila pembayar cukai mempunyai moral cukai yang tinggi. Secara praktikalnya, penemuan ini membantu penggubal dasar dan kerajaan bahawa mekanisme tadbir urus yang ideal melalui persekitaran politik yang stabil adalah penting untuk meningkatkan pematuhan cukai. Namun begitu, pendekatan kerajaan untuk menguatkuasakan peraturan undang-undang yang berkesan dilihat sebagai strategi yang lebih menjanjikan untuk meningkatkan moral pembayar cukai.

Kata kunci: Kestabilan politik; kedaulatan undang-undang; pematuhan cukai; moral cukai; pengantara

INTRODUCTION

Tax compliance is a major problem for governments in many developing nations. Despite several tax reforms governments have implemented over the years, the Inland Revenue Board of Malaysia (IRBM) still strives to increase tax compliance. For a record, only 2.27 million (15.24%) Malaysians claimed to have paid tax in 2018 out of a total workforce of 14.9 million, with 33.76 per cent being registered taxpayers but do not pay taxes and the remaining 51 per cent do not register themselves as taxpayers (The Edge 2018). The IRBM also reported that 79,786 individuals, businesses, and organisations in Malaysia had remarkable wealth but failed to declare the right tax amount (The Star 2018a).

Nowadays, the public expects governments to be accountable for all their fiscal, economic, and national policy implementations. Researchers have lately discussed the quality of governance in light of mounting concerns about its benefits (Sen 2014). The rationale is that citizens finance the government's activities by allocating tax monies; hence, any government activities should be of interest to taxpayers. Over the past five decades, the tax compliance literature has suffered from a few limitations that need to be highlighted.

At first glance, most prior research employed the governance index of World Governance Indicators (WGI) to measure governance quality (see, for example, Cummings et al. 2009; Mohammed Abdullahi Umar et al. 2019; Rodriguez-Justicia & Theilen 2018; Torgler et al. 2007). Contrarily, the current research uses taxpayers' perceptions of how well or how poorly the government institutions perform their jobs to the satisfaction and discontent of citizens. While the governance index incorporates a broad component of governance from the macroeconomic perspective, the study's findings may not be generalised to the whole population (in this example, Malaysia in general), as taxpayers in East Malaysia (region of Sabah and Sarawak) and West Malaysia may perceive different opinion on governance quality.

East Malaysia is also unique from its counterparts in West Malaysia. For example, Sabah and Sarawak belong to rich ethnic diversities (Malay Mail 2015), are ranked among those with the lowest median income (Department of Statistics Malaysia 2020) and maintain a distinct legislative autonym (The Star 2018b). Besides, there is a huge socio-economic gap between East and West Malaysia. The basic needs and infrastructures in East Malaysia, such as banks, hospitals, roads, utilities, water, the internet, and telephones, were less developed, particularly in the rural districts of Sabah and Sarawak (Business Today 2021). Moreover, depending on how each administrator performs, the impact of governance may be localised regionally and differently from each other. For instance, the Japanese and Chinese are the happiest with their governments' performance, whilst Russians and Americans are less satisfied (Wang 2010).

Although past studies investigate the direct association between governance quality and tax compliance (see, for example, Alasfour et al. 2016; Nkundabanyanga et al. 2017; Ortega et al. 2016), the incorporation of tax morale into their discussion has been studied far less often. Embedding tax morale as a mediator is necessary because standard behaviours stem from psychological attitudes, for instance, how people view their actions and react to others (Slemrod 2019). In this reasoning, the political aspect is important to be studied because economic growth is made possible only by political stability, and the effectiveness of the rule of law ensures sufficient sanctions and penalties for those who break the tax laws. The assumption is that citizens support the government and its functions by paying taxes. In return, citizens have a right to know how money is spent and its benefits. With the above in mind, the objective of this study is two folds. First, the study investigates the association between governance quality (political stability and the rule of law) and tax morale with tax compliance. Secondly, this study investigates whether political stability and the rule of law affect tax compliance through tax morale.

This paper reviewed the literature with the development of hypotheses and a research model. Then, research methodologies are closely reviewed, followed by results and discussion. Next, theoretical and practical implications are explained. Finally, limitations and future research conclude the study.

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

THEORY OF PLANNED BEHAVIOUR

Using the TPB as its theoretical foundation, this research examined the influence of governance quality on tax morale and compliance. TPB postulates that attitude, subjective norms, and perceived behavioural control influence intention, ultimately affecting behaviour. Nonetheless, the idea of TPB in this study posits that political stability and the rule of law can be best explained by attitude and subjective norms because taxpayers behave by watching the government's performance in delivering services and goods in exchange for taxes paid. For example, a positive attitude taxpayers will perceive better political stability and the effective rule of law to rationalize their support of high tax morale, thus implying better tax compliance. This corroborates Bobek (1997) that the desire to participate in behaviour is proportional to a person's attitude toward tax payment.

Additionally, subjective norms illustrate people's inclination to imitate others. Taxpayers who experience a stable political climate and the effective rule of law will encourage others to arrive at the same conclusion in rationalizing better tax compliance. In TPB, variance in tax morale can also be best explained by the changes in attitude because taxpayers behave by following their ethics, values, morals and emotions. In testing this behavioural change, Bobek et al. (2013) found that taxpayers' morale is primarily affected by their attitude/ethical beliefs. For instance, a taxpayer's commitment to compliance behaviour that goes against their values/principles will affect their moral judgement. In this case, the premise that taxpayers with a favourable attitude tend to exhibit more tax morale is justified, positively influencing their compliance behaviour. Therefore, the theoretical foundation of the study believed that taxpayers are more likely to have the intention to comply if they have a high tax morale, which supported by positive attitude and greater subjective norms on political stability and rule of law.

GOVERNANCE QUALITY

Governance quality is essential to citizens because of the advantages it provides. Rodriguez-Justicia and Theilen (2018) found that poorly governed nations with little oversight of corruption cause lower tax morale among people with less education. Furthermore, citizens' tax morale and compliance are adversely affected by the perceived lower quality of goods and services provided by the government (Everest-Phillip & Sandall 2009). However, taxpayers will be more motivated to pay their fair share of taxes if they see that the government is transparent and accountable in its use of public funds (Meagher 2018). In this vein, positive tax compliance can be observed when the government are effective (for example, well management of external debt and an efficient financial system) (Nkundabanyanga et al. 2017).

POLITICAL STABILITY AND TAX COMPLIANCE

Aizenman and Jinjarak (2008) discovered a favourable association between tax-collecting success and political stability, thus asserting that committing more resources to tax enforcement increases tax compliance. When it comes to taxation in a developing economy, long-term economic growth via consistent tax collections is also made possible by political stability (Radu 2015). Contrarily, the effectiveness of tax administration and tax compliance can be hampered by political instability and the intervention of politicians who want to conceal their businesses and families from tax authorities (Sebele-Mpofu 2020). Similarly, Damania et al. (2004) reported that countries that experience political instability only weaken judicial efficiency, allowing corruption to become prevalent. Based on these considerations, it is hypothesised that:

H_1 Political stability positively increases tax compliance

RULE OF LAW AND TAX COMPLIANCE

Countries with a well-established and the effective rule of law are often accepted as a social norm by their citizens, contributing to a higher degree of compliance (Bergman 2009). This corroborates Mohammed Abdullahi Umar et al. (2019) that people are more likely to pay taxes when the rule of law is effective with adequate sanctions for those who violate tax laws. The idea that high compliance can be achieved via strict enforcement of the rule has been documented by the previous scholar. For instance, Debacker et al. (2018) found that strict randomising audits in the United States increased the reported taxable income by more than US$1,000 in the following years. Additionally, imposing an aggressive tax audit to detect tax fraud and bring those responsible to justice have a favourable impact on the compliance rate of honest taxpayers in Brazil (Da Silva et al. 2019). Nevertheless, the low probability of being audited and the inefficiency of the tax system and tax authority in executing the tax law negatively affect tax compliance in Malaysia (Mohd Rizal Palil et al. 2013). This leads the study to hypothesise the following:

H_2 The effective rule of law positively increases tax compliance

TAX MORALE AND TAX COMPLIANCE

According to Christian and Alm (2014), people with low levels of empathy and compassion have a lower moral coefficient and are more likely to commit tax evasion. However, Ortega et al. (2016) discovered that the right to pay taxes mirrors individual tax support irrespective of government spending and tax policies. Chong and Arunachalam (2018) also conclude a larger tendency for compliance for those with high tax morale. This is consistent with Taing and Chang (2020), which support the idea of improved engagement in compliance intention due to increased tax morale. In light of the TPB, a positive attitude is typically presumed to cause favourable behaviour and is assumed to change compliance positively, and vice versa. The findings above serve the development of the following hypothesis:

H_3 High tax morale positively increases tax compliance

POLITICAL STABILITY AND TAX MORALE

Granting taxpayers democratic space to hold the government accountable and reduce corruption is responsible for the increased trust in the government and tax morale (Torgler 2003). Then, Torgler (2011) reported that political stability, voice and accountability and effective regulations offer larger positive and significant effects on tax

morale than the rest of the governance indicators. According to Rodriguez-Justicia and Theilen (2018), taxpayers have greater regard for tax morale in nations with a stable political climate and effective government. Contrarily, a decrease in tax morale can be seen in taxpayers and tax administrators if the tax administration experiences excessive political instability and corruption (Sebele-Mpofu 2020). Nonetheless, Tedds (2010) posited otherwise that political instability did not affect the willingness to underreport tax; however, political instability may impair a country's capacity to collect the tax. Therefore, the study hypothesised the following:

H4 Political stability positively increases tax morale

RULE OF LAW AND TAX MORALE

Torgler and Schneider (2009) evident a negative influence on people's willingness to pay taxes if the rule of law and its institutions are politicised. Due to the weak rule of law, tax morale is negatively affected when corruption is prevalent, poor transparency, and government officials have been granted unchecked authority and uncontrolled power (Torgler et al. 2007). Sebele-Mpofu (2020) also asserted that a lack of trust in the rule of law, the legislature, courts, police and parliament have a detrimental effect on taxpayers' morale and the efficiency of tax authorities in collecting taxes. However, effective law enforcement, such as strict penalties and greater audits, strengthen taxpayers' legitimacy and morale (Slemrod 2019). Besides, increased tax morale is also attributed to several factors, including the probability of getting detected and higher fines, the belief that others pay taxes, and less corruption (McCulloch et al. 2020). The following hypothesis is then derived from these considerations:

H5 The effective rule of law positively increases tax morale

THE MEDIATING ROLE OF TAX MORALE

The discussion of tax morale as a mediator in the tax compliance model can be justified by the norms model that taxpayers are motivated to comply with their tax duties by a desire to adhere to specific social or personal norms, for instance, reciprocating the cooperation of others or respecting legal obligations (Doran 2009). This is synonymous with the psychological attitude that the normative behaviours arise from how individuals evaluate their actions and the actions of others, for example, willingness to comply with the tax law because they perceive it to be just (Slemrod 2019). Besides, human behaviour may be influenced by the imposition of moral costs for compliance and non-compliance, as every individual has unique social preferences and concerns for others and one's appearance (Horodnic 2018).

Moreover, tax morale varies across individuals due to distinct intrinsic motivations, peer influences and societal pressures (Luttmer & Singhal 2014). These variances may shed light on how a person should behave. Given the importance of tax morale, the concerns surrounding governance quality within the scope of political stability and the rule of law deserve attention. For instance, when political stability favours taxpayers due to its benefits in promoting economic growth, intrinsic motivation to pay tax will be developed, ultimately increasing compliance behaviour. Similarly, when taxpayers believe that the rule of law effectively upholds that guarantee sanction, the taxpayer's morale, hence the intention to pay tax, is assumed to increase. Therefore, tax morale that serves as a mediator in the relationship between governance and tax compliance is illustrated in Table 1.

TABLE 1. Mediator of tax morale in the relationship between governance quality (political stability and the rule of law) and tax compliance

Governance Quality	Tax Morale	Tax Compliance
Taxpayer's perception of government's performance in: 1. political stability 2. the rule of law	Taxpayers' morale responses are assumed to change due to their different perceptions of political stability and how effective the rule of law is	Taxpayers are presumed to exhibit higher (lower) tax morale, subsequently willing to comply (non-comply) tax under the conditions of: 1. political stability, which promotes business confidence, investment development and economic growth 2. the effective rule of law to guarantee sanctions or penalties for non-tax compliance

Thus, the study hypothesised the following:

H6 Tax morale mediates the effect of political stability on tax compliance.
H7 Tax morale mediates the effect of the rule of law on tax compliance.

Based on the seven (7) hypotheses, an integrated research model is developed as in Figure 1.
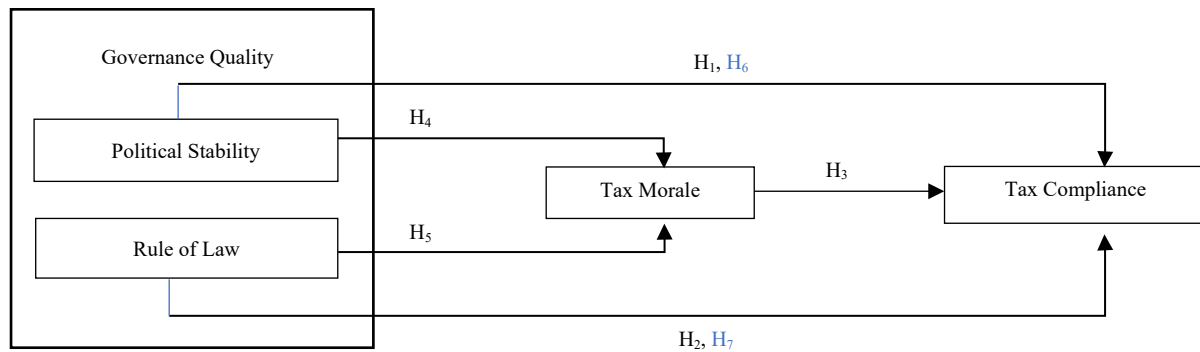
FIGURE 1. Research model

RESEARCH METHODOLOGY

SAMPLING

In this study, a quantitative survey was employed. Given the constraint of privacy and confidentiality of taxpayer information by IRBM, the study could not determine the appropriate sample frame for Sabah and Sarawak, respectively. Hence, this grants the study to use a non-probability sampling method relative to stratified random sampling. Based on G*Power analysis (power = 0.80, α = 0.05, f^2 = 0.15, three predictors), the minimum sample size was 77 respondents. Due to covid-19 restrictions, more online surveys were distributed to individual taxpayers (salaried and self-employed).

In total, 10,227 email invitations have been sent to respondents, with 3,861 sent in Sabah and 6,366 sent in Sarawak. Nevertheless, the online survey results are comparable to paper-based (Loomis & Paterson 2018). Finally, a total of useable 592 samples were gathered. In this process, two categorical questions were developed to act as control variables; 1) taxpayer status to differentiate between taxpayer and non-taxpayer, and 2) occupational status to differentiate between employed and self-employed taxpayers.

Research on East Malaysia (Sabah and Sarawak) is worth investigating for a few grounds. First, East Malaysia suffers from a lack of knowledge about governance's impact on tax morale and compliance. For the record, few researchers investigated tax compliance in East Malaysia, but only to a lesser extent linking the Self-Assessment System and tax knowledge to tax compliance. Secondly, Sabah and Sarawak were ranked 11th and 12th in Malaysia regarding median income, respectively, out of 16 states/ regions/ territories (Department of Statistics Malaysia 2017). Thirdly, taxpayers' perception of government quality in East Malaysia may differ from West Malaysia due to economic imbalance (wealth, household income, and infrastructure), ethnic variety, and administrations that institutionalise Sabah and Sarawak locally. For illustration, according to the Malaysia Agreement (MA 1963), the local government of Sabah and Sarawak maintain a high degree of legislative autonomy regarding land acquisition, immigration and birth registration.

RESEARCH INSTRUMENTS

The questionnaire is developed using the existing tax literature measures. Taxpayers were asked to rank their opinions from 1 (strongly disagree) to 5 (strongly agree). The questions have been modified to suit the Malaysian taxation environment. Four sections make up the questionnaire, which was written in English. The first section consists of five (5) items examining the respondents' background, such as gender, location, employment status, taxpayer status and monthly income before tax. The second section has five (5) items related to tax compliance. In this study, taxpayers' likelihood of complying voluntarily with tax is the dependent variable adopted from Kirchler and Wahl (2010). Following Torgler (2011) arguments, only two governance variables were studied in this research, where political stability and the rule of law have the greatest positive significant impacts on changing taxpayer behaviour than the other governance variables. Therefore, the third section, with three (3) items on political stability and four (4) items on the rule of law, seeks to ascertain respondents' perceptions of governance.

The World Bank's definition of "*the traditions and institutions by which authority in a country is exercised*" (Kaufmann et al. 2011: 222) is the most commonly used to describe governance. For this study, the Asian Barometer (2020) Second Wave Core Questionnaire was used to operationalize taxpayers' notion of governance. Asian Barometer Survey (ABS) is applied research that assesses individuals' satisfaction by asking about various governance concerns. Table 2 summarises part of the two-dimension that cut across in measuring governance quality as presented by Kaufmann et al. (2011).

TABLE 2. Governance quality measures

Dimension	Description
Political Stability	The strength of political aspects of local governments and the consistency of their policies, including the possibility of political disturbance in the community.
Rule of Law	The government's ability to execute rules and laws that bind society, such as property rights, contract laws, courts and police, and the effectiveness of such regulations in settling crimes or violent incidents.

Meanwhile, six (6) items in the last section aim to gauge taxpayers' tax morale. Tax morale is characterised as an intrinsic motivation to pay taxes (Luttmer & Singhal 2014; Torgler et al. 2007). The current study borrowed the measurement of tax morale from Torgler (2003). The constructs and items used in the study can be seen in Appendix.

RESULTS

This study has taken care of all relevant data cleaning and screening procedures. For data analysis, the study utilised IBM SPSS and SmartPLS (Ringle et al. 2015). Given that the multivariate skewness and kurtosis are larger than the cut-off values of 3 and 20, respectively (Mardia 1974), PLS-SEM is appropriate because the data is not a multivariate normal distribution. Hence, the study adopted two consecutive procedures in PLS-SEM: (1) measurement model and (2) structural model (Hair et al. 2019). Using SmartPLS software, the model's reliability, validity, and significance level were assessed. Further discussion of the two assessments was reported in the next section.

Table 3 depicts the demographics of the respondents. A near balance of 300 male (50.7%) and 292 female (49.3%) taxpayers were included in the survey. The near distribution of respondents can be seen in Sabah (48.6%) and Sarawak (51.4%). Most respondents (79.7%) are salaried, while 20.3 per cent are self-employed. Taxpayers with monthly income before tax of RM4,501 to RM6,500 (41.9%) outweigh those of RM6,501 to RM10,500 (36.8%). However, only 15.2 per cent of taxpayers earn between RM10,501 and RM15,000 per month, while only a small number (6.1%) earn more than RM15,000.

TABLE 3. Demographic information of respondents

Demographic	Category	Frequency (N = 592)	Percentage (%)
Gender	Male	300	50.7
	Female	292	49.3
Location	Sabah	288	48.6
	Sarawak	304	51.4
Status of	Salaried taxpayers	472	79.7
Employment	Self-employed taxpayers	120	20.3
Monthly Income	RM4,501-RM6,500	248	41.9
(Before Tax)	RM6,501-RM8,500	137	23.1
	RM8,501-RM10,500	81	13.7
	RM10,501- RM15,00	90	15.2
	More than RM15,000	36	6.1

Note: The income was in Ringgit Malaysia (RM). RM1 was equal to $0.25 U.S Dollars at the time of data collection.

ASSESSMENT OF MEASUREMENT MODEL

Measurement models were tested via internal consistency reliability, discriminant validity and convergent validity. According to Hair et al. (2017), items that reflect a construct with equal scores indicate internal consistency reliability. The Composite Reliability (CR) index is favoured above Cronbach Alpha (α) because the α indicator strongly relies on the number of items in the construct (Hair et al. 2017). In light of this, CR is recommended as a superior alternative for reliability measures (McNeish 2017). In this study, items loading at least 0.70 were retained, whereas loadings below 0.40 (item TaxM_6) were deleted. Nonetheless, items PolS_3 and RuL_4 with loadings ranging from 0.40 to 0.70 were omitted to increase the Average Variance Extracted (AVE) value greater than 0.50. As shown in Table 4, all constructs exhibit CR > 0.708 and AVE > 0.50, thus, meeting the measurement model's requirement (Hair et al. 2017).

TABLE 4. Measurement model

Constructs	Items	Outer Loadings	α	CR	AVE
		> 0.60	> 0.70	> 0.708	> 0.50
Political	PolS_1	0.802	0.523	0.807	0.677
Stability (PS)	PolS_2	0.843			
Rule of Law (RL)	RuL_1	0.755	0.656	0.804	0.579
	RuL_2	0.836			
	RuL_3	0.684			

Tax Morale (TM)	TaxM_1	0.750	0.905	0.929	0.723
	TaxM_2	0.768			
	TaxM_3	0.839			
	TaxM_4	0.810			
	TaxM_5	0.753			
Tax Compliance (TC)	TaxC_1	0.820	0.845	0.889	0.616
	TaxC_2	0.832			
	TaxC_3	0.848			
	TaxC_4	0.904			
	TaxC_5	0.845			

Based on the empirical standard, discriminant validity is the degree to which a construct differs from other constructs and does not measure anything else by chance (Urbach & Ahlemann 2010). Henseler et al. (2015) proposed the Heterotrait-Monotrait Ratio of Correlations (HTMT) as a better alternative to Fornell and Larcker (1981) criterion for evaluating discriminant validity. Two methods for diagnosing HTMT: (1) HTMT criteria and (2) HTMT inference. The output in Table 5 showed no violations of discriminant validity in the cross-matrix rows and columns because the value of the HTMT criterion is below the cut-off value of HTMT.85 (Kline 2011) and the HTMT.90 (Gold et al. 2001), respectively.

TABLE 5. Discriminant validity (HTMT criterion)

	Political Stability	Rule of Law	Tax Compliance	Tax Morale
Political Stability				
Rule of Law	0.804			
Tax Compliance	0.260	0.219		
Tax Morale	0.177	0.208	0.371	

On the other hand, the Confidence Interval Bias Corrected (CIBC) lower and upper bounds of HTMT inference in Table 6 did not contain the value of one, consistent with the HTMT criterion in Table 5, which indicates no violation of discriminant validity.

TABLE 6. Discriminant validity (HTMT inference)

	Original Sample	Sample Mean	CIBC 5%	CIBC 95%
Rule of Law -> Political Stability	0.804	0.809	0.679	0.928
Tax Compliance -> Political Stability	0.26	0.262	0.164	0.354
Tax Compliance -> Rule of Law	0.219	0.225	0.141	0.295
Tax Morale -> Political Stability	0.177	0.192	0.099	0.263
Tax Morale -> Rule of Law	0.208	0.228	0.140	0.253
Tax Morale -> Tax Compliance	0.371	0.372	0.295	0.441

COLLINEARITY ASSESSMENT

Before diagnosing the structural model, it is essential to confirm the non-existence of lateral collinearity. It is possible that the problem of lateral collinearity might mislead the conclusions since the model's strong causal influence can be masked even though discriminatory validity has been demonstrated (Kock & Lynn 2012). Hair et al. (2017) claimed that the Inner Variance Inflation Factor (VIF) values above 5 suggest the presence of lateral multicollinearity problems. Nevertheless, the study reported that all inner VIF values of the other independent variables (political stability $_{VIF}$ = 1.262, the rule of law $_{VIF}$ = 1.290 and tax morale $_{VIF}$ = 1.040) are below 5, hence confirming the absence of collinearity issues (Hair et al. 2017).

DISCUSSION

ASSESSMENT OF STRUCTURAL MODEL

The hypothesised association in the model follow the suggestion of Hair et al. (2019) that the path coefficients, p-values, t-values, standard errors (SE) and confidence intervals were generated using bootstrapping procedures (5,000 resamples). Instead of assessing p-values and t-values to establish significance, the CIBC will also be checked. For a result to be significant, the bootstrap value of the confidence interval of the lower and upper bound does not straddle zero (Hair et al. 2019).

Direct Effect Given that the study's direct effect hypothesis is directional, the study follows the suggestion of Ramayah et al. (2018) to use a one-tailed test with a 0.05 significance level. Based on Table 7, the direct association of political stability on tax compliance showed a positive and significant influence (β = 0.120, t =

2.430, $p < 0.05$, 95% CI = 0.035, 0.197), thus supporting H_1. The study's findings support Radu (2015) that a stable political system is necessary for institutions to increase tax compliance. According to the former Deputy Director General (Macro), Economic Planning Unit, Prime Minister's Department, Datuk K Yogeesvaran, some degree of political stability during the post-covid-19 pandemic in Malaysia is required for society to earn rewards and economic benefits. In this conception, political stability ensures revenue collections on the part of the government, which results in the provision of high-quality public services and goods. Additionally, a stable political climate aids in the development of consistent and ongoing tax collection.

However, H_2 was rejected, given a non-significant outcome between the rule of law and tax compliance (β = 0.057, t = 1.092, $p > 0.05$, 95% CI = -0.033, 0.138). These findings postulated that the ideology of the government's approach to administering the effective rule of law may influence taxpayers' opinions about the government's effort to curb collective violence and crime but cannot be translated into how it could affect tax compliance. Nevertheless, another perspective of the rule of law, translated into clarity, fairness and simplicity of tax rules, may provide another insight into taxpayer's compliance because tax rules are sometimes ambiguous and subject to frequent changes than laws in general. For instance, taxpayers tend to distance themselves from the tax system because complicated tax rules make compliance increasingly challenging (Bornman & Ramutumbu 2019). Furthermore, a significant positive relationship between tax morale and tax compliance was evident (β = 0.311, t = 7.919, $p < 0.01$, 95% CI = 0.240, 0.369), supporting H3. In line with most previous research, improvement in tax compliance can be observed when taxpayers have high tax morale. In West Malaysia, increased tax morale has been linked to tax compliance (Chong & Arunachalam 2018; Hafizah Mat Nawi et al. 2020).

Nonetheless, political stability (β = 0.045, t = 0.815, $p > 0.05$, 95% CI = -0.048, 0.135) showed an insignificant effect on tax morale, contrary to the significant outcome of the rule of law on tax morale (β = 0.171, t = 3.479, $p < 0.01$, 95% CI = 0.077, 0.242), thus rejecting H_4 and supporting H5, respectively. The idea that the effective rule of law increases taxpayers' morale corroborates Sebele-Mpofu (2020). The rejection of H_4 is congruent with Tedds (2010), that evidence of no influence of political instability on willingness to under-report tax. This study revealed that exposure to political climate on a broad scale has little effect on morale dilemmas. According to Malaysian Unity Foundation Chairman Prof. Dr Suresh Kumar Govind, political ideologies in the form of race-based politics in East Malaysia are not prominent and political interference is not so dramatic as in West Malaysia. Additionally, political ideologies and state nationalism in Sabah and Sarawak emphasise the best interests of its citizens, irrespective of race or religion, and refrain from allowing personal feelings or emotions to cloud their judgement (Chin 2018).

The R^2 value of 0.137 in Table 7 implies that political stability, the rule of law, and tax morale account for 13.7 per cent of variances in tax compliance, representing moderate predictive accuracy. Contrarily, variances in the political stability and the rule of law contributed to 3.8 per cent in the tax morale, implying weak predictive accuracy. This follows Cohen (1988) that R^2 values of 0.02, 0.13 and 0.26 are considered weak, moderate and substantial predictive accuracy. Hair et al. (2019) also recommended reporting the effect size (f^2) and predictive relevance (Q^2) when using PLS-SEM. Based on Cohen (1988), f^2 values of 0.35, 0.15 and 0.02 indicate substantial, medium and small effects. The f^2 in this study demonstrate the medium effect of tax morale in generating tax compliance. In contrast, a small effect can be seen in generating the R^2 of tax compliance by political stability. Nonetheless, the rule of law does not affect producing tax compliance. However, the f^2 outcome addressed the rule of law as having small-sized effects on tax morale but none on political stability. Then, the study's path models of Q^2 are greater than zero, indicating the establishment of predictive relevance (Geisser 1974; Stone 1974).

Mediating Effect   As suggested by Hair et al. (2017) and following the recommendation of Preacher and Hayes (2008), this study utilised a bootstrapping technique with 5,000 subsamples to investigate a mediation effect. Since the study's mediation hypothesis is non-directional, a two-tailed test with a 0.05 significance level was utilized for mediation analysis (Ramayah et al. 2018). Then, the magnitude of the mediation was diagnosed following the suggestion of Zhao et al. (2010: 201). Bootstrapping output in Table 7 demonstrated that the relationship between the rule of law and tax compliance is significantly mediated by tax morale (β = 0.053, t = 3.175, $p < 0.01$, 95% CI= 0.019, 0.084), thus providing support for H_7. As seen in Table 8, although the direct effect (c') was insignificant for (*RL -> TC*), a significant indirect effect (a*b) of (*RL -> TM -> TC*) was detected in the study, thus signifying indirect only (full mediation). This study revealed that the rule of law has a beneficial impact on tax morale. The effect then disseminates positively to tax compliance, with tax morale as a mediator. The study asserted that high-morale taxpayers have a more positive attitude toward compliance if they perceive the government uphold the rule of law, such as guaranteeing sufficient sanctions. For this reason, what matters most to taxpayers is how effectively the government punishes lawbreakers (Organisation for Economic Co-operation and Development 2013).

However, a non-significant mediation effect via tax morale was evident between political stability and tax compliance (β = 0.014, t = 0.794, $p > 0.05$, 95% CI = -0.023, 0.048), hence rejecting H6. Despite the study's insignificant indirect effect of (*PS -> TM -> TC*), this study found a significant direct effect of (*PS -> TC*), thus,

concluding direct only (no mediation). In this study, political stability was demonstrated to be a weak predictor of increasing tax morale on its own. Thus, the study concludes that the mediating function of tax morale between political stability and tax compliance is still ambiguous and merits more empirical examination.

TABLE 7. Structural model

Direct Path Model	β of c'	SE	t	p	CIBC LL	CIBC UL	Decision	f^2	R^2	Q^2
H1: PS -> TC	0.120	0.049	2.430	0.008	0.035	0.197	Supported	0.013		
H2: RL -> TC	0.057	0.053	1.092	0.137	-0.033	0.138	Rejected	0.003	0.137	0.094
H3: TM -> TC	0.311	0.039	7.919	0.000	0.240	0.369	Supported	0.108		
H4: PS -> TM	0.045	0.055	0.815	0.208	-0.048	0.135	Rejected	0.002	0.038	0.020
H5: RL -> TM	0.171	0.049	3.479	0.000	0.077	0.242	Supported	0.024		
Mediating Path Model	β of (a*b)	SE_{Boot}	t	p	CIBC LL	CIBC UL		Decision		
H6: PS -> TM -> TC	0.014	0.018	0.794	0.427	-0.023	0.048		Rejected		
H7: RL -> TM -> TC	0.053	0.017	3.175	0.002	0.019	0.084		Supported		

Note: PS = political stability, RL = rule of law, TM = tax morale, TC = tax compliance

TABLE 8. Type of mediation

Mediating Path Model	Indirect Effect (a*b)	Direct Effect (c')	Direction (a*b*c')	Type of Mediation
H6: PS -> TM -> TC	0.014 (ns)	0.120 (Sig.)	n/a	Direct only (No Mediation)
H7: RL -> TM -> TC	0.053 (Sig.)	0.057(ns)	n/a	Indirect only (Full Mediation)

Note: PS = political stability, RL = rule of law, TM = tax morale, TC = tax compliance, ns = non-significant, Sig = Significance, n/a = not applicable

THEORETICAL IMPLICATIONS

Few theoretical and practical contributions can be drawn in a few ways. Given that there is a lack of systematic research on tax morale as a mediating factor in the array of governance quality, this research theoretically affirmed the significant mediation of the rule of law on tax compliance via tax morale. The research gap in population constituted another lacuna. Prior studies on governance quality focus on Western countries, with limited attention on taxpayers from the Asian region, especially East Malaysia. Consequently, the current study represents the first attempt to fill these gaps in population in the tax literature. Alternatively, the study's findings also offer a different perspective on how taxpayers perceive the governance quality, in contrast to previous studies that used the Governance Index

PRACTICAL IMPLICATIONS

The findings also offer practical implications for policymakers and governments that an optimum governance quality supported by a stable political climate is necessary to promote tax compliance. This implies that politicians and political parties in Malaysia, irrespective of coalition or opposition, should work together to maintain a thriving political climate that benefits the country; otherwise, political unrest will be retaliated with non-compliance by taxpayers. In a taxation context, this might require a certain level of political stability for the government to require that people participate in the form of tax payment, or else violence and protest; hence, non-compliance will occur. Although the study showed no evidence that the rule of law significantly influences tax compliance; however, it positively affects tax morale. It is advised that the government should put a stronger emphasis on the effective rule of law to establish legitimate institutions that can win the hearts and morale of taxpayers. Another approach that the government might consider is to combine the concepts of justice and security, which are concerned with issues such as violence, conflict, and crime.

CONCLUSION

The scepticism regarding governance compels the study investigates factors that motivate taxpayers to rationalize their tax compliance. Specifically, two research objectives are studied: (1) examining the relationship between governance quality (political stability and the rule of law) and tax morale with tax compliance and (2) determining the extent of mediating effects of tax morale in the relationship between governance quality (political stability and the rule of law) and tax compliance. Concerning the first objective, this study found that taxpayers' belief in the country's political stability significantly increases their tax compliance level. Furthermore, a positive attitude with high tax morale consistently serves as an impetus to motivate them to pay taxes, thus suggesting that the effective rule of law was more promising to mould taxpayers' morale. In addition, the second objective's findings also confirm that the rule of law influences tax compliance through tax morale. Theoretically, this study evidences the importance of tax morale in the relationship between the rule of law and tax compliance. Practically, this

finding aids policymakers and governments in their quest for the best approaches for successfully enhancing governance quality to influence taxpayer morale and tax compliance.

This study is not free from limitations. Due to the Covid-19 pandemic, internet questionnaires were used more than paper surveys, which could cause response bias as internet surveys may lack anonymity, especially when respondents are unwilling to reveal their true feelings about sensitive matters. Besides, only a small minority of high-income respondents participated. Future research should consider replicating the same study in another region to gain further insight into the subject. Future studies can include demographic variables as moderators, such as age, gender, and income level. In summary, this research established a set of frameworks that relate governance quality to tax morale in a tax compliance model.

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Mohd Allif Anwar Abu Bakar (corresponding author)
Faculty of Business, Economics and Accountancy
Universiti Malaysia Sabah
88400 Kota Kinabalu, Sabah
MALAYSIA
E-Mail: allif@ums.edu.my

Mohd Rizal Palil
Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600 UKM Bangi, Selangor
MALAYSIA
E-Mail: mr_palil@ukm.edu.my

Ruhanita Maelah
Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600 UKM Bangi, Selangor
MALAYSIA
E-Mail: ruhanita@ukm.edu.my

APPENDIX

LIST OF MEASUREMNT ITEMS

Constructs		Items	Source
Tax Compliance		*When I pay my income taxes as required by the Malaysian tax laws and regulations,*	Kirchler and Wahl (2010)
	TaxC_1	I do so to support the country and other citizens.	
	TaxC_2	I do so because I like to contribute to everyone's good.	
	TaxC_3	I do so because for me it's the natural thing to do.	
	TaxC_4	I do so because I regard it as my duty as a citizen.	
	TaxC_5	I do so because I am sure I am doing the right thing.	
Political Stability	PolS_1	I am NOT satisfied with the way democracy works in Malaysia.	Asian Barometer (2020)
	PolS_2	I am satisfied with the current ruling government parties	
	PolS_3	Politics in Malaysia seem so complicated that I CAN'T understand what is going on.	
Rule of Law	RuL_1	Our current courts always punish the guilty even if they are high-ranking officials.	
	RuL_2	When the government breaks the laws, there is NOTHING the legal system can do.	
	RuL_3	The legislature in Malaysia is capable of keeping the government in check	
	RuL_4	When the country is facing a difficult situation (for example handling the pandemic of COVID-19), it is acceptable for the government to DISREGARD the law in order to deal with the situation	
Tax Morale	TaxM_1	Since everybody evades taxes, we can hardly be blamed for doing it.	Torgler (2003)
	TaxM_2	Taxes are so heavy that tax evasion is necessary for many to survive.	
	TaxM_3	Cheating on taxes is justifiable in light of the unfairness of the tax system	
	TaxM_4	Since everybody evades taxes, we can hardly be blamed for doing it.	
	TaxM_5	There is NOTHING bad about under-reporting taxable income on one's tax return.	
	TaxM_6	Taxes are something which is taken away from me	