



الجامعة
UNIVERSITI
TEKNOLOGI
MARA

Cawangan Negeri Sembilan
Kampus Seremban

FAKULTI PERAKAUNAN

BULETIN FPN



fa

The Impact on Individuals or Businesses of Misreporting Financial Statements for Tax Avoidance from An Accounting Perspective

Aina Syazwani Mohd Isa and Saflina Azis

Introduction

Financial statements serve as essential tools for individuals and businesses to understand their financial standing, encompassing income, expenses, assets, and liabilities. Once prepared, these statements undergo scrutiny by auditors. Subsequently, individuals and companies determine their tax obligations for the assessment year, with higher income or profits resulting in increased taxable income. Taxation plays a pivotal role in a country's revenue generation, financing expenses, and national development, while also fostering income distribution equilibrium. However, certain entities attempt to evade taxes, leading to tax non-compliance, an ongoing challenge faced by tax administration bodies like the Inland Revenue Board of Malaysia (IRB).

Many individuals and businesses resort to manipulating financial statements to minimize tax liabilities, commonly through practices like overstating expenses and understating income, known as "creative accounting." Tax non-compliance occurs when entities fail to fulfill tax obligations, such as registering, submitting tax forms, reporting accurate income, and paying taxes within specified periods. Studies indicate widespread involvement in tax non-compliance, with sole proprietorship businesses identified as significant tax evasion contributors.



Integrity and Reliability of Financial Information

Tax evasion involves deliberately manipulating financial records to decrease taxable income, often by disregarding accounting principles like GAAP or IFRS. This could entail practices such as artificially lowering reported income or inflating expenses. Notably, aggressive accounting techniques, exemplified in scandals like Enron, can result in misleading financial statements that obscure a company's true financial standing. Compliance with established accounting standards ensures financial information's accuracy, transparency, and reliability, thereby upholding public confidence in financial markets.

When financial information is distorted due to tax evasion, it impacts various stakeholders. Investors rely on accurate financial data to make informed investment decisions, while creditors use this information to assess companies' creditworthiness. Government agencies depend on financial statements to ensure tax compliance and collect revenue. Inaccurate financial information can lead to misguided decisions, financial losses for investors and creditors, and diminished government revenue, ultimately affecting society.

Legally, tax evaders face penalties, fines, and potential imprisonment under tax laws. Audits conducted by tax authorities incur costs and resources for correcting financial statements and ensuring compliance. Travel restrictions may be imposed on individuals or directors with unpaid taxes, complicating financial assessment and eroding confidence in financial reporting reliability. Overall, widespread tax evasion results in increased tax debts and penalties, posing significant legal and financial consequences for those involved.

Recommendation

Addressing tax evasion and fraudulent financial practices requires a multifaceted approach involving reforms in tax systems, strengthened enforcement of accounting standards, improved oversight of auditors, whistleblower protection, and tax compliance programs.

One critical step is to simplify and make transparent the tax system to reduce opportunities for tax evasion. Complex tax codes often contain loopholes that individuals and businesses exploit. Simplifying the tax code and enhancing transparency can discourage tax evasion by eliminating ambiguities and reducing the incentives for manipulation.



Strengthening accounting standards and enforcement mechanisms is vital for preventing fraudulent financial practices. Tighter regulations mandating detailed disclosure and reporting requirements can enhance transparency and accountability. Additionally, robust enforcement measures, such as penalties for non-compliance, serve as deterrents against fraudulent activities.

Enhanced oversight of auditors is essential for ensuring accurate financial reporting and detecting irregularities. Auditors play a crucial role in upholding the integrity of financial statements. Therefore, measures to bolster auditor independence and oversight can improve the quality and reliability of audited financial statements.

Protecting whistleblowers who report financial misconduct is crucial for uncovering fraudulent activities. Whistleblower protection laws and programs encourage individuals to come forward with information about illegal or unethical practices without fear of retaliation. By safeguarding whistleblowers, organizations can uncover and address fraudulent activities more effectively.

Implementing tax compliance programs, such as voluntary disclosure initiatives, can encourage taxpayers to report accurate income and pay their taxes honestly. These programs offer individuals and businesses the opportunity to rectify past errors or omissions without facing severe penalties, thereby promoting tax compliance and integrity.

Furthermore, offering instalment payments for taxes can assist individuals and businesses facing financial difficulties in meeting their tax obligations. Allowing taxpayers to spread their tax payments over time can alleviate financial burdens and ensure continued compliance with tax.

Overall, addressing tax evasion and fraudulent financial practices requires a comprehensive approach involving reforms in tax systems, strengthened enforcement of accounting standards, improved oversight of auditors, whistleblower protection, tax compliance programs, and flexible payment options for taxpayers. By implementing these measures, governments and organizations can promote fairness, transparency, and integrity in financial reporting and taxation.

Conclusion

In conclusion, engaging in financial statement manipulation to avoid taxes can harm individuals, businesses, and the economy overall. While it may offer short-term benefits, it carries significant long-term risks, eroding investor confidence and damaging trust in companies. Recognizing the consequences of tax evasion is crucial for promoting ethical behaviour and maintaining a transparent financial system. Therefore, fulfilling tax obligations responsibly is essential, supporting the nation's revenue and funding vital public services.

Understanding the importance of tax contributions underscores the need for accurate accounting practices. Outdated methods can lead to verification challenges and recurring errors, emphasizing the importance of regular account monitoring. Comprehensive financial statements enable informed decision-making and reduce the risk of audit investigations. Compliance with tax laws, including timely payment, is mandatory for individuals and businesses, ensuring efficient tax administration and revenue collection.

References

- Juruaudit Memainkan Peranan Penting Dalam Menggalakkan Integriti Penyata Kewangan - Siaran Akhbar dan Pengumuman. (2021, June 23). <https://www.sc.com.my/bm/sumber/siaran-akhbar-dan-pengumuman/juruaudit-memainkan-peranan-penting-dalam-menggalakkan-integriti-penyata-kewangan>.
- Keperluan Pengurusan Cukai. (2023, February 14). AKPK. <https://www.akpk.org.my/ms/keperluan-pengurusan-cukai>.
- Menjelang Tahun Baharu. (2023, December 19). Lembaga Hasil Dalam Negeri Malaysia. https://www.hasil.gov.my/media/chturc5/20231219_dewan-siswa_selesaikan-tunggakan-cukai-menjelang-tahun-baharu-bil-122023.pdf.
- Pengarah Syarikat Didakwa Elak Bayar Cukai Pendapatan. (2023, May 13). Berita Harian. https://www.bharian.com.my/berita/nasional/2023/05/1101005/pengarah-d-elak-bayar-cukai-pendapatan#google_vignette.
- Prem Sikka. (2018, January 31). Combating Corporate Tax Avoidance. *Journal of Capital Markets Studies*. <https://www.emerald.com/insight/content/doi/10.1108/JCMS-01-2018-0005/full/pdf?title=combating-corporate-tax-avoidance-by-requiring-large-companies-to-file-their-tax-returns>.
- SC Kenakan Cenda dan Denda Lima Pengarah Trive kerana Kemuka Kenyataan Palsu. (2017, December 4). <https://www.sc.com.my/bm/sumber/siaran-akhbar-dan-pengumuman/sc-kenakan-cenda-dan-denda-lima-pengarah-trive-kerana-kemuka-kenyataan-palsu>.
- Sertai PKPS 2.0 Elak Diaudit HASiL. MYNEWSHUB. (2023, December 1). MyNewsHub. <https://www.mynewshub.tv/2023/12/sertai-pkps-2-0-elak-diaudit-hasil/>
- Taknak Bayar Cukai? Bersedia Untuk Berdepan Dengan 4 Kesan Ini. (2020, March 2). *Majalah Labur*. Retrieved February 1, 2024, <https://www.majalahlabur.com/kewangan/cukai/taknak-bayar-cukai-bersedia-untuk-berdepan-dengan-4-kesan-ini/>