UNIVERSITI TEKNOLOGI MARA

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Edisi 6

Tax Evasion of High-Net-Worth Individuals

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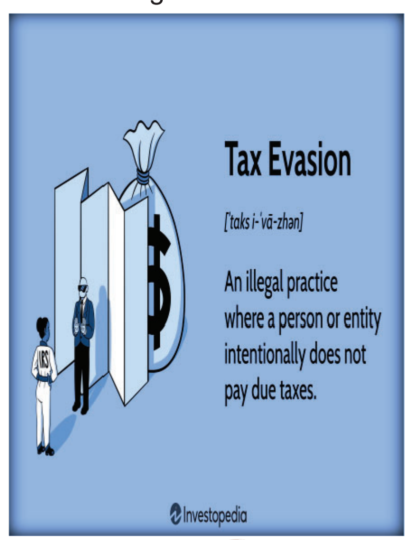
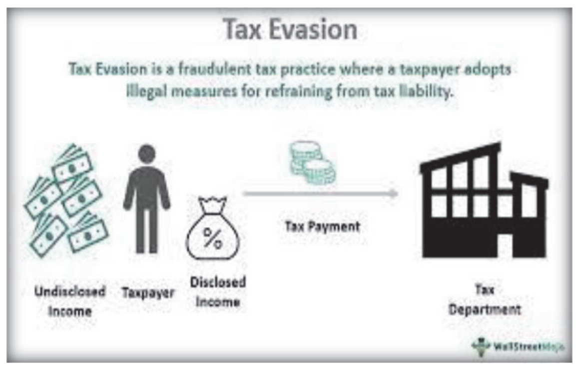
The term high-net-worth individuals (HNWIs) is commonly interpreted as individuals who have accumulated net worth or wealth that positions them at the top of the wealth scale within a country or even on a global scale (Mc Laughlin & Buchanan, 2017). The concept of net wealth is related to combining the value of financial assets and tangible assets owned by individuals and their immediate families while deducting their financial debts. Specifically, Knight Frank (2023) defined HNWIs as an individual with a net worth equal to or exceeding US$1 million. There is another term for this super-rich individual, which is ultra-high-net-worth individuals (UHNWIs), which can be defined as an individual with a net worth equal to or exceeding US$30 million. However, considering Malaysia's standpoint, the Securities Commission of Malaysia (2021) characterized the HNWIs as an individual whose collective net investment portfolio, whether held personally or jointly with their spouse, exceeds RM1 million or the equivalent amount in foreign currencies.

According to Kangave et al. (2016), the taxation of HNWIs has received significant attention in various countries for several reasons. Generally, these individuals are frequently involved with complex business transactions. Additionally, their total income significantly contributes to overall government tax revenue. However, this situation might cause them to become aggressively involved in tax planning. Lastly, the tax behavior of this group has the potential to influence the overall integrity of the tax system and can even fuel social unrest (Gangl & Torgler, 2020). Nevertheless, it is noteworthy that the prevalence of tax evasion or tax noncompliance among HNWIs critically impacts tax revenue collection, economic and social progress. This situation further contributes to the expansion of the tax gap between the wealthy and the poor (Che Rosli et al., 2018). The most commonly employed strategies used by HNWIs in Malaysia that relate to tax evasion, as identified in the study by Che Rosli et al. (2018), included underreporting other income, followed by excessive claims of relief,



excessive claims of purchases, underreporting tax liability through manipulation of sales or income, and finally, making claims for unallowable expenses.

Several factors influence tax evasion behavior among HNWIs. Sources of income have been identified as one of the determinants of tax evasion. A study by Che Rosli et al. (2018) found that HNWIs deriving business income display less compliance compared with those with employment income. This study is aligned with the studies by Richardson (2006) and Saad (2014), which similarly show that opportunities for tax evasion are based on business income. Notably, HNWIs with business income have greater opportunities to structure their taxable income to reduce their tax obligations. They often take advantage of having foreign businesses to move profits or income out of the country. Another crucial determinant is the role of a tax professional or tax agent, a factor highlighted in several studies (Che Rosli et al., 2018; Saad et al., 2021). Saad et al. (2021) emphasize that tax professionals often facilitate HNWIs in overstating expenses. Moreover, political affiliation also emerges as a significant factor, where HNWIs affiliating with the ruling government, being prone to overstating expenses (Saad et al.,2021). This is due to their perception that they can escape tax audits and penalties. Additionally, the likelihood of detection by tax authority also plays an important role, as evidenced by Saad et al. (2021). The study indicates that the higher the likelihood of detection, the lower the propensity for HNWIs to overstate expenses. The result is consistent with the previous studies by Allingham and Sandmo (1972).



The evolving financial environment, coupled with the global pandemic and ever-shifting tax landscape, has altered the global landscape in unprecedented ways. While taxing the income generated by HNWIs presents administrative complexities and challenges, failure to do so could lead to significant tax revenue losses to the country as a whole. Therefore, it is crucial for the tax authority to monitor their wealthiest individuals and promote voluntary tax compliance, thereby contributing to the betterment of society.

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