

Determining Tax Literacy of Salaried Individuals - An Empirical Analysis

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Abstract : *In personal financial planning, tax management plays a very important role. An individual should have thorough knowledge of various aspects of taxes and tax policies, which would help him to understand how much he can save even after paying taxes. Those people who have not taken any formal course on taxation finds it difficult to understand and comprehend the issues related to determination of tax liability, tax filling and tax saving. An attempt has been made through this paper to determine tax literacy level of salaried individuals based on various demographic and socio-economic factors. Findings of the study suggest that overall tax literacy level of respondents is not very high. The results suggest that level of tax literacy varies significantly among respondents. Also tax literacy level gets affected by gender, age, education, income, nature of employment and place of work whereas it does not get affected by geographic region. Findings of this paper suggest that government should adopt more aggressive approaches to educate taxpayers, thereby raising the level of tax literacy among them.*

Keywords - Tax literacy, Salaried individuals, Taxpayers, Indian Taxation System, and Government.

I. INTRODUCTION

One of the important components of financial planning is tax management. Tax management refers to tax payer's ability to manage personal taxation issues such as computation of tax liability, tax savings, payment of taxes on time and timely filing of tax return. In order to handle the issues relating to tax management, tax payer must be aware as well as knowledgeable about basic concepts of personal taxation. In this context tax literacy of an individual plays an important role. Tax literacy may be defined as the knowledge which an individual should possess in order to manage the issues concerning personal taxation effectively.

It is commonly believed that Indian taxation system is difficult to understand. Tax payer's find it difficult to understand and comprehend the issues related to determination of tax liability, tax filling and tax saving as most of them do not undergo any formal course on taxation. Earlier studies suggest that people assume that tax rates are very high in our country. On account of higher tax rates and their inability to understand tax issues, most of the people do not file in their tax returns. As a result of this government has to suffer in terms of poor collection of tax revenue. A government needs taxes because, in the long run, taxation is the most efficient way of funding the goods and services which people want the government to provide. Tax ignorance is harmful for individuals as well as for the nation. It can cause taxpayers to pay too much tax by preventing them from taking advantage of tax benefits to which they are entitled.

In India the main body, which is responsible for the collection of taxes, is the Central Board of Direct Taxes (CBDT). It is a part of the Department of Revenue under the Ministry of Finance of the Indian government. According to Indian Income Tax Act 1961, income of an individual can be classified into following five heads of Income [1]: Income from salary, Income from house property, Profits and gains of business or profession, Capital gains and Income from other sources. Any individual can have income under one head, under two or more than two heads or under all the heads. Sum total of income under all the heads is known as Gross Total Income. Deductions U/S 80 of Income Tax Act is allowed from Gross Total Income and residual amount is known as Total Income. Tax is levied on Total Income at scheduled rates prescribed for the particular assessment year.

An attempt has been made through this study to determine tax literacy level of salaried individuals based on various demographic and socio-economic factors. Assessing the level of tax knowledge amongst salaried individuals will help us to know the actual level of tax knowledge possessed by them. We will also be able to determine the factors which significantly affect the level of tax literacy. Findings of the study can be utilized by the government so as to identify those groups of tax payers which possess the lowest level of tax literacy and accordingly framing policies to educate them on issues relating to personal taxation.

II. LITERATURE REVIEW

Lewis [2] studied the impact of tax knowledge and attitudes of an individual on completing the tax returns. His aim was to study the impact of increase in tax knowledge on tax compliance behavior. He found

that there is insufficient knowledge about tax regulations amongst the population. Eriksen and Fallan [3] through their study found that fiscal knowledge correlates with attitudes towards taxation. They have suggested that tax behavior can be improved by a better understanding of tax laws. Tax payer must be given better tax knowledge in order to improve tax ethics and compliance behavior.

Gender differences in tax knowledge and attitude towards taxation were studied by Fallan [4]. The findings of this study indicate that male students have a significantly stricter attitude towards their own tax evasion and female students have a significantly stricter attitude towards other people's tax evasion. Singh [5] in his study found that general tax knowledge of an individual is correlated with tax payer's ability to understand and comprehend the rules and regulations of taxation, and their ability to comply with them.

Loo and Ho [6] examined competency of salaried individuals of Malaysia towards self assessment system and found that tax knowledge of respondents is low thus making them incompetent under self assessment regime. Nero et.al [7] studied tax literacy level among employees of Sabah and Sarawak's states of Malaysia. It was found that the tax literacy level in the two states is not quite satisfactory. Saad [9] in his study on compliance behavior of salaried taxpayers in Malaysia found the evidence that Malaysian tax payers perceive fairness of the income tax system in several dimensions. Also, tax knowledge and tax compliance were shown to affect – fairness perceptions.

After reviewing the relevant literature, it becomes clear that level of tax knowledge among individuals is found to be low in almost every study. Thus it becomes clear that developing tax knowledge among tax payers is an important element in operating a successful tax system. Also it can be said that studies related to tax literacy were mainly carried out in countries other than India. In India no such kind of study which has determined tax literacy level has been undertaken. Thus the present study bridges this gap.

III. OBJECTIVES OF THE STUDY

The following are the objectives of this present study-

1. To determine the level of tax literacy among salaried individuals.
2. To find out the relationship between tax literacy and various demographic and socio-economic factors.

IV. HYPOTHESES

For the purpose of this study following hypotheses have been proposed:

Hypothesis 1:

H₀: There is no association between gender and tax literacy level of salaried individuals

H₁: There is an association between gender and tax literacy level of salaried individuals.

Hypothesis 2:

H₀: There is no association between age and tax literacy level of salaried individuals

H₁: There is an association between age and tax literacy level of salaried individuals.

Hypothesis 3:

H₀: There is no association between education and tax literacy level of salaried individuals

H₁: There is an association between education and tax literacy level of salaried individuals.

Hypothesis 4:

H₀: There is no association between income and tax literacy level of salaried individuals

H₁: There is an association between income and tax literacy level of salaried individuals.

Hypothesis 5:

H₀: There is no association between nature of employment and tax literacy level of salaried individuals

H₁: There is an association between nature of employment and tax literacy level of salaried individuals.

Hypothesis 6:

H₀: There is no association between place of work and tax literacy level of salaried individuals

H₁: There is an association between place of work and tax literacy level of salaried individuals.

Hypothesis 7:

H₀: There is no association between geographic region and tax literacy level of salaried individuals.

H₁: There is an association between geographic region and tax literacy level of salaried individuals.

V. METHODOLOGY

For the purpose of the study a survey was conducted amongst salaried individuals (those who fall in income tax bracket) of Himachal Pradesh. Multistage sampling has been used in order to get representative sample of the population. Out of total twelve districts of Himachal Pradesh, three districts namely Shimla, Solan and Kangra were selected randomly (first stage). The selected districts were divided into sub-divisions and two sub-divisions per district were selected randomly (second stage). From each selected sub-division, respondents were selected conveniently using some common criteria like place of work (urban or rural), occupational status (government or non-government employee) so as to get representative sample of the population. Primary data

from the respondents was collected by using a structured questionnaire. A total of 516 respondents constitute a sample for this study.

In order to check the tax literacy level, thirteen questions about personal income tax were asked from the respondents. The questions were related to basic concepts of income tax, computation of tax liability, assessment rates, deductions etc. in order to assess how knowledgeable the respondents are about the concepts and issues relating to personal taxation. For each correct answer one mark was given and no marks were given for incorrect answer. The total score for each respondent was calculated which was further converted to their percentage score. The prime objective of the study is to explore the association between demographic and socio-economic factors and tax literacy level of salaried individuals. The hypothesis of this study has been tested with the help of ANOVA. The hypothesis has been tested at 5% significance level.

VI. Discussion Of The Results

6.1 Demographic Profile of the Respondents

Table 1 gives the summary of the demographic and socio-economic characteristics of the respondents. A look at demographic and socio-economic detail shows that percentage of male respondents is 68.8% and female respondents is 31.2%. 29.7% of the respondents fall in the age group of 31-40 years and 30.6% fall in the age group of 41-50 years.

Table 1- Demographic and Socioeconomic details of the respondents			
		Frequency	Percentage
GENDER	Male	355	68.8
	Female	161	31.2
AGE (Years)	20-30	101	19.6
	31-40	153	29.7
	41-50	158	30.6
	51-60	90	17.4
	More than 60	14	2.7
	EDUCATION	10+2	39
	Graduation	237	45.9
	Post Graduation	220	42.6
	PhD	20	3.9
INCOME PER ANNUM (In Rs.)	2-5 lacs	315	61.0
	5-10 lacs	177	34.3
	10-15 lacs	24	4.7
	More than 15 lacs	NIL	0.0
NATURE OF EMPLOYMENT	Government Employee	241	46.7
	Non-Government Employee	275	53.3
PLACE OF WORK	Urban	280	54.3
	Rural	236	45.7
GEOGRAPHIC REGION	Shimla	187	36.2
	Solan	178	34.5
	Kangra	151	29.3

Source: Primary Data

Majority of the respondents i.e. 45.95% in our sample are graduates followed by 42.6% having post graduate degree. The respondents also constitutes government (46.7%) and non-government (53.3%) employees. 61% of the respondents have an annual income between Rs. 2-5 lacs followed by 34.3% respondents who earn between Rs. 5-10 lacs annually. The respondents are from three different districts of Himachal Pradesh. 36.2%, 34.5% and 29.3% of the respondents are from Shimla, Solan and Kangra districts respectively.

6.2 Tax literacy level of the respondents

6.2.1 Association between gender and tax literacy level

Table 2 shows the mean score of tax literacy level of males and females. The results indicate that tax literacy of males is more than females. The mean score of males was found to be 59.46% and that of females was found to be 51.84%. From Table 2 it can be seen that F value is significant at 5% significance level, hence H_0 of hypothesis 1 – there is no association between gender and tax literacy level is rejected. Thus it can be concluded that there is a significant difference between male and female respondents in terms of tax literacy level.

Table 2- Mean, Standard Deviation and F Value of Tax Literacy Level					
		Mean	Std. Dev	F Value	Significance
GENDER	Male	59.46	13.804	31.571	.000
	Female	51.84	15.252		
AGE (Years)	20-30	53.24	14.983	3.315	.011
	31-40	57.62	14.925		
	41-50	56.77	13.184		
	51-60	60.26	16.236		
	More than 60	62.09	9.760		
EDUCATION	10+2	51.68	12.092	19.003	.000
	Graduation	53.20	12.867		
	Post Graduation	61.15	15.598		
	PhD	68.85	10.433		
INCOME PER ANNUM (In Rs.)	2-5 lacs	53.43	13.296	30.451	.000
	5-10 lacs	61.97	14.957		
	10-15 lacs	68.91	13.887		
	More than 15 lacs	NIL	0.000		
NATURE OF EMPLOYMENT	Government	55.44	13.703	5.682	.018
	Non-Government	58.52	15.382		
PLACE OF WORK	Urban	59.64	15.833	19.283	.000
	Rural	54.04	12.573		
GEOGRAPHIC REGION	Shimla	56.15	15.965	0.595	.552
	Solan	57.69	13.883		
	Kangra	57.51	13.983		

Source: Primary Data

6.2.2 Association between age and tax literacy level

Table 2 shows the mean score of tax literacy level for different age groups. It can be observed from the table that as age progresses tax literacy level also increases. Maximum tax literacy level of 62.09% is shown by respondents falling in age group of more than 60 years followed by 60.26% for age group of 51-60 years. In order to see statistical difference in mean scores based on age, hypothesis 2 is tested using ANOVA and F value is calculated. From the table, it can be seen that F value is significant at 5% significance level, hence H_0 of hypothesis 2-There is no association between age and tax literacy level is rejected. Thus it can be concluded that tax literacy level depends on age.

6.2.3 Association between education and tax literacy level

Table 2 shows that tax literacy level is correlated with the level of education. More the education level more is the level of tax literacy. Table 2 shows that tax literacy level is highest for respondents who have PhD degree (68.85%) followed by those respondents who have post graduate degree. From the table it can be seen that F value is significant- at 5% significance level. Hence H_0 of hypothesis 3-There is no association between education level and tax literacy level is rejected. Thus it can be concluded that tax literacy level depends on the education level.

6.2.4 Association between Income and tax literacy level

The results of the Table 2 indicates that more the income, more will the level of tax literacy. Table 2 shows that tax literacy level is highest for respondents having income level between Rs 10-15 lacs (68.91%) per annum followed by those who earn between Rs. 5-10 lacs (61.97%) per annum. From the table it can be seen that F value is significant- at 5% significance level. Hence H_0 of hypothesis 4 - There is no association between income and tax literacy level is rejected. Thus it can be concluded that tax literacy level depends on the income of a person.

6.2.5 Association between nature of employment and tax literacy level

On the basis of nature of employment we have divided the respondents into two categories i.e. government and non-government employees. Table 2 shows that non-government employees have higher tax literacy level as compared to government employees. From the table it can be seen that F value is significant- at

5% significance level. Hence H_0 of hypothesis 5-There is no association between nature of employment and tax literacy level is rejected. Thus it can be concluded that nature of employment influences tax literacy level.

6.2.6 Association between place of work and tax literacy level

According to place of work, employees have been categorized into two parts namely urban and rural depending upon whether the place of employment of the employee is urban area or rural area. From the results it is clear that employees working in urban areas are more tax literate as compared to those working in rural areas. From the table it can be seen that F value is significant- at 5% significance level, hence H_0 of hypothesis 6- There is no association between place of work and tax literacy level is rejected. Thus it can be concluded that tax literacy level depends on the place where employee works.

6.2.7 Association between geographic region and tax literacy level

From Table 2 it can be seen that tax literacy level of respondents is almost same for all the three districts. Also from the table it can be seen that F value is not significant- at 5% significance level, hence H_0 of hypothesis 7-There is no association between geographic region and tax literacy level is not rejected. Thus it can be concluded that tax literacy level does not depend on geographic region.

VII. Findings

The following are the main findings of the study:

1. Overall tax literacy level of 57.08% is low and points out to the fact that salaried individuals are not well versed with the basic concepts of personal taxation. Thus they may face difficulty in computing their tax liability and filing their tax returns.
2. Tax literacy level of males is higher than that of females and the difference is statistically significant.
3. Level of tax literacy is positively related to the age, education and income level i.e. our results indicate that tax literacy level increases with age, education and income.
4. Employees working in urban areas are more tax literate as compared to those working rural areas.
5. The employees working in non-government jobs are more tax literate as compared to those in government jobs and the difference is statistically significant.
6. Geographic region does not affect the level of tax literacy significantly.

VIII. Conclusion

From the above analysis it can be concluded that overall tax literacy level of 57.08% among all respondents is not encouraging. This shows that in our country people are still not much aware about their personal taxation related issues. The results suggest that level of tax literacy varies significantly among respondents on the basis of various demographic and socio-economic factors. Also the level of tax literacy gets affected by gender, age, education, income, nature of employment and place of work whereas it does not get affected by geographic region.

Overall it can be concluded that tax literacy level is very low in our country and necessary measures should be taken by government to increase awareness about tax related matters amongst the population.

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