

# EMPIRICALLY INVESTIGATING OF VALUED ADDED TAX (VAT) AND ITS IMPACT ON ECONOMIC AND SOCIETAL WELL-BEINGS (PRE- AND POST COVID19): A STUDY BASED ON KINGDOM OF SAUDI ARABIA

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## Abstract

*The government of the Kingdom of Saudi Arabia (KSA) has concluded that the country cannot achieve sustainable economic growth if it continues to rely on its oil reserves alone as a source of revenue. As a result of pressure from the IMF, Saudi Arabia implemented its first Value-Added Tax (VAT) this year. There have been some complaints about the introduction of VAT in the Kingdom, especially from the younger population who have never known a tax-free existence. The global economic impact of the COVID19 health epidemic has been substantial. As of July 1, 2020, the VAT in the Kingdom of Saudi Arabia (KSA) will increase from 5% to 15%, which may indicate a new pattern of consumption behavior. Consequently, the purpose of this research is to investigate how Saudi youth feel about VAT based on five broad categories: Income inequality (II), system knowledge (SK), and international practice (GP) are all components of a successful tax system. The results, based on a survey of 460 people, show that nearly nine in ten people are aware of the introduction of VAT. But the analysis's unfavourable findings reveal that VAT is not a good tax system to apply (average TSE = 45.6% less favourable) since it does not address income inequality (average II= 45.3% less favourable). In addition, the findings indicate that the younger generation in Saudi Arabia continues to shop even after the introduction of VAT, demonstrating that the tax has no effect on their spending habits. This study is among the first to attempt to document such an impact and to analyze it in light of recent legislative amendments brought about by COVID-19 because of the dearth of research on VAT among GCC academics. Therefore, in light of COVID-19, this study is both contemporary and pertinent in that it can shed new light on the VAT system, its adoption, and its impacts on consumer behavior.*

**Key words:** VAT, Saudi Arabia, Economic and Social-well-being.

## Introduction

The Saudi Arabian government has instituted the value-added tax in response to the growing need for government revenue. Since prior marketing research has shown that VAT encourages consumers to shop around and find better deals, it became important to conduct more in-depth research into and evaluation of consumer behavior after VAT was introduced (Adiwijaya et al., 2021). It also fortifies the locals' ability to save and invest for the future, raising incomes and mitigating tax burdens. When it comes to achieving economic goals, diversifying revenues, and reducing dependency on oil income, the value-added tax is one of the most important financial measures in the Kingdom. Furthermore, taxation is a means through which governments raise funds from individuals and businesses to invest in economic and social programs that help close the income gap in society (UFIER, 2014). Therefore, when local economies are struggling, governments often turn to taxing as a means of raising domestic revenue. In fact, the rapid drop in oil prices has coincided with the

introduction of VAT in the GCC nations, including Saudi Arabia, and is anticipated to play a key role in reshaping the direction of economic and social systems (Shukeri & Alfordy, 2020).

When governments have the flexibility to distribute resources to promote social development and market formation, it helps the economy expand, become more stable, and last for the long-term. Taxes collected are guaranteed money in the bank (De & De, 2022). In Saudi Arabia, for instance, where oil profits make up a significant amount of the country's budget, the government has made the decision to diversify the country's revenue stream away from oil and toward taxation. Recognizing the many proposals for defining taxation, we can say that their major function is to fund governmental operations and long-term projects. In certain nations, tax collections account for close to half of all government revenue (Ahmed et al., 2021). For comparison, in 2010, tax revenue as a percentage of total revenue in Finland was 45.8%, whereas in 2021, the same figure for Denmark was 48.5%. Taxes accounted for more than half of Iceland's GDP in 2021, and the figure was even higher in some countries (Tariq et al., 2021).

Any sort of tax enforcement has a number of challenges. When it comes to taxation, every developing nation has the same fundamental challenge: how to raise sufficient income to provide essential public services in a way that is both economically sound and politically secure for those in power (Hossain, 1995).

## LITERATURE REVIEW

There has been some type of taxation in the Gulf Cooperation Council (GCC) countries since at least the 1980s in places like the United Arab Emirates (UAE), Kuwait, and Saudi Arabia. For instance, between 1955 and 1975, Kuwait and Saudi Arabia enacted a number of tax laws, including a business tax and an income tax for expats. However, expats no longer had to pay income tax in Saudi Arabia after that year (Ali et al., 2022). This is because of the country's newly found oil wealth and the accompanying need to bring in a significant number of foreign workers to help stimulate the economy ("Covid 19 Pandemic Impact Micro, Small Mediu. Sized Enterp. Policy," 2022). However, Saudi Arabia reinstated its income tax for expats in 1988 to make up for falling oil earnings, and it has remained in place ever since. As international organizations officially urged GCC countries to adopt VAT as a form of taxation policy in the early 1990s (Fu et al., 2022).

GCC governments began to examine the viability of introducing VAT as a form of taxes. It was noted that there was "significant scope [in the GCC states] to eliminate tariff exemptions, expand excise taxes, and introduce a selective tax on luxury goods" (Keen & Lockwood, 2010) in the United Nations Economic and Social Commission for West Asia's 1997 annual report, but international efforts to do so eventually stalled.

Value-added tax (VAT), sometimes known as goods and services tax (GST), has been adopted in the following regions of the world, as shown in Table 1:

<b>Region</b>	<b>No of Countries</b>
GCC	3
ASIA	21
ASEAN	8
EUROPE	53
OCEANLA	7
AFRICA	44

SOTH AMERICA	11
CARIBBEAN, CENTRAL AMERICA AND NORTH AMERICA	19
Total	166

Despite the fact that value-added taxes (VAT) is one of the most extensively accepted forms of taxation in the world (Note 2), there is still some debate over whether or not it is actually effective as a taxing system (Ahlerup et al., 2015). According to the work of (Lee & Gordon, 2005), the best way to think about taxes is as a social cost that people in these societies must pay in order to provide benefits and a balance of amenities. It has also been argued that this method of raising funds has the potential to narrow the gulf between affluent and low earners within nations (Gemmell & Morrissey, 2005), who looked at the impact of VAT on income equality in Saudi Arabia, found no compelling evidence that the tax was effective at its intended goal. (Keen, 2008) sought proof that VAT is a successful tax system for fostering income equality by examining the relationship between national governance and income equality through the use of VAT. If a country's governance is strong, with less bureaucracy, greater accountability, and stability, then VAT is shown to lower income inequality. In addition, a 2015 study by (Alhussain, 2020) concluded that VAT is a cumbersome and does not encourage equal income distributions in the garment business. The value-added tax (VAT) may be too risky a tax system for the expansion of small and medium-sized businesses (SMEs), according to a study (Hongxin et al., 2022). This is because the profit margins of SMEs are often lower than those of larger corporations.

According to a study conducted in Malaysia, Goods and Services Tax (GST), formerly known as VAT, has enhanced the corporate governance regime despite having a negative effect on firms and income inequality. (Goh et al., 2021) found that several aspects of board composition specifically board independence, CEO age, and CEO family—were associated with better sales performance before, during, and after the adoption of GST. The results also showed that boards of directors had greater accountability to enhance their companies' outcomes, especially with the introduction of GST. (TAMAOKA, 1994) find that VAT has a positive effect on consumer behavior. Their research confirmed that the majority of respondents have an in-depth understanding of GST, leading them to the positive conclusion that consumers' spending habits have changed for the better as a result of the tax. With the exception of (Ezenagu, 2021), most previous literatures have revealed detrimental effects of VAT.

There is still debate over how effective and popular this type of tax system is, with many people viewing it as onerous and a source of economic stress. Research by (Khan et al., 2021), which discovered an inverse relationship between tax regimes and economic growth in underdeveloped countries, supported the claims.

## RESEARCH METHODOLOGY

This research was designed in the format of an exploratory single-country case study. A series of questions serve as the primary tool for this quantitative approach to data collection. We modified the survey from (Zhang et al., 2021) slightly to conform to Saudi regulations on taxes.

All primary data were collected through questionnaires given to 470 undergraduate business students at the Saudi Electronic University, Kingdom of Saudi Arabia, to investigate how young Saudis feel about VAT and how it has affected their purchasing habits before and after COVID19. The surveys asked participants to score their experiences with the VAT both at the old rate of 5% and the new one of 15%.

There were sixteen total questions on each survey. These components can be broken down into three groups. The first part deals with the acceptance of VAT by the millennial generation and is structured around five categorical variables: the efficiency of the tax system (TSE), the diversity of income sources (IGS), the degree of income inequality (II), familiarity with the system (SK), and global practice (GP). The second part of the survey seeks information about how value-added tax has affected the purchasing habits of the millennial generation. In this passage, we draw a sharp line between the impact of value-added tax on consumer behavior and the impact of selection taxation. The study's research structure and its operational measure are shown throughout Table 2, and Table 3 respectively; in the subsequent section of the questionnaire, participants' demographic information such as education level, field of study, background information, and age is collected.

<b>Categorical Factors</b>	<b>Operational Measure (Survey Design)</b>
Tax System Effectiveness (TSE)	The value-added tax is an attempt to modernize and simplify the tax system.
	The value-added tax is meant to improve the accounting system by making it more thorough, comprehensive, and open.
	The impact of VAT will be greater than that of the previous selective tax.
Income Generation Sources (IGS)	The introduction of VAT will raise national revenue.
Income Inequality (II)	Consumers will not be disadvantaged by VAT.
	Totally surprised by the proposed VAT system
	Low-income people are safeguarded by VAT.
System Knowledge (SK)	The introduction of VAT will lead to price increases across the board.
Global Practice (GP)	The value-added tax is the most effective tax system and is used by many countries.

<b>Impact of VAT</b>	<b>Item</b>
Behavioural Consumption	The impacts of VAT on consumer behavior are beneficial.
	Consumer behavior benefits from selective taxation.
	When gas is heavily taxed in certain areas, students are more likely to carpool to campus.

460 undergraduates from a variety of business majors and schools, with varying levels of experience and age make up the sample. Additionally, respondents were selected at random, and SPSS version 25.0 was used for descriptive analysis to determine percentages and frequencies as well as for comparison purposes.

### Demographic Analysis

The demographic profile analysis used in the study is displayed in Table 3. An estimated 31.3 % of males and 68.7% of females filled out the survey. Out of a total of 1,005 students at the University of Hail in Saudi Arabia, 470 were randomly selected to participate in the survey.

<b>Gender</b>	<b>Frequency</b>	<b>Percent</b>	<b>Cumulative Percent</b>
Male	130	31.3	31.3
Female	340	68.7	100.0
Total	470	100	100

Source: Compiled from Primary source.

The educational attainment of the respondents is broken down per year of study in Table 4. According to the data, 37.6% are in their last year of college, 24.1% are in their junior year, 16.5 % are in their second year of college, and 21.8 % are in their first year. Next, the majors of the respondents are broken down: 20 percent are business majors, 19 percent are economic and finance majors, and 67 percent are management and information systems majors. In addition, 40.2 % of respondents are between the ages of 18 and 20, 25.7% are between the ages of 21 and 23, 29.5% are older than the age of 23, and 4.6 % are younger than the age of 18. The marital status of the respondents was also highlighted in the study; it was found that 88.8 % of the respondents were single and just 11.2 % were married.

<b>Categorical</b>	<b>Particular</b>	<b>Frequency</b>	<b>Percentage</b>
	Male	130	31.3
	Female	340	68.7
		470	100
Year of Study	Freshman	75	16.5
	Sophomore	101	21.8
	Junior	131	24.1
	Senior	163	37.6
		470	100
Area of Study	Accounting	102	21.3
	Economic and Finance	87	18.7
	Management and Information system	268	60.0
		470	100
Age	Less than 18 years old	41	4.6
	Between 18 to 20 years old	176	40.2
	Between 21 to 23 years old	107	25.7
	More than 23	145	29.5
		470	100
Marital	Married	68	11.2

Status			
	Single	402	88.8
		470	100

Source: Compiled from Primary source.

Table 5 demonstrates that, as of January 22, 87% of respondents were aware of VAT's introduction. According to the most current study by (Forstenlechner & Rutledge, 2010), just 13% of respondents don't know that VAT has been implemented. Social media had a key role in the dissemination of VAT-related information and knowledge to the respondents. UOH awareness activities accounted for 5.8%, while periodicals and newspapers accounted for 3.8% and word-of-mouth among friends and family contributed the remaining 2%. These results seem to have less relevance for the younger generation given the prevalence of information technology as a means of disseminating information.

Awareness on the Implementation of VAT	Frequency	Percent	Cumulative Percent
Yes	406	87	87
No	64	13	100
Total	470	100	100

Source: Compiled from Primary source.

The remaining 87% were all-too-aware of VAT and gave the following explanations for their ignorance: Seven percent said they didn't care, five percent said they weren't directly affected, and two percent said they didn't have time to learn about VAT because it didn't apply to them. VAT Acceptance Criteria, Version 4.2.1. The study focused on five broader elements that have been studied in several previous literatures to better understand the public's acceptance of VAT. Table 6 displays the tallied elements that contributed to VAT approval, along with generic percentage ratings for each factor (Table 9). Most respondents thought VAT was a less efficient tax system (TSE = 45.6%), unable to promote income equality (II = 45.3%), and had poor levels of understanding about the VAT system (SK = 42.4%). According to the respondents, value-added tax is not a useful tool for generating income (IGS = 34.3%). Figure 1 provides more visualization of the result.



**Figure 1  
PYRAMID PRESENTATION OF VAT ACCEPTANCE**

<b>Influencing Factors</b>	<b>Strongly Disagree</b>	<b>Disagree</b>	<b>Neutral</b>	<b>Agree</b>	<b>Strongly agree</b>
Tax System Effectiveness (TSE)	20.80	23.60	26.5	17.10	10.0
Income Generation Sources (IGS)	14.40	17.60	23.50	21.40	17.10
Income Inequality (II)	24.15	21.75	22.30	17.25	14.85
System Knowledge (SK)	21.75	18.60	26.00	19.75	11.50
Global Practice (GP)	22.0	18.35	29.65	19.70	12.30

Source: Compiled from Primary source.

<b>Influencing Factors</b>	<b>Favourable VAT Acceptance</b>	<b>Unfavourable VAT Acceptance</b>
Tax System Effectiveness (TSE)	26.75	43.25
Income Generation Sources (IGS)	40.70	35.20
Income Inequality (II)	29.76	44.7
System Knowledge (SK)	27.50	47.3
Global Practice (GP)	27.40	41.2

Source: Compiled from Primary source.

In line with earlier research on VAT, such as those by (Siddiqui et al., 2021), the analysis reveals evidences that VAT causes income inequality among the people in the Kingdom. Costs of living and company compliance are both predicted to rise as a result of VAT's implementation. Lack of familiarity with the Saudi VAT system and its redistribution of resources on the welfare of Saudi society also contribute to the negative attitude towards its implementation (Table 8). This study's conclusions are congruent with those of a recent study by (Neubig, 2018), which predict that the implementation of VAT will fail due to a lack of awareness and government support.

### **Impact of vat on consuming behaviour**

In light of the mixed results on VAT's general acceptance, this research tries to fill in the gaps with a deeper dive into the tax's effect on consumers' spending habits. The results are summarized in Table 9.

<b>Impact of VAT</b>	<b>Item</b>	<b>Favourable VAT Impact</b>	<b>Unfavourable VAT Impact</b>
Behavioural Consumption	VAT has positive effects on consumers' behaviour	29.25	48.30

	Selective taxation has positive effects on consumers' Behaviour	25.10	43.60
	Selective taxation on petro encourages students to share a ride to come to the university	33.70	41.60

Source: Compiled from Primary source.

The results of the study suggest that the introduction of VAT does not change or improve respondents' purchasing habits. The study contradicts failing to provide evidence that the introduction of VAT results in a corresponding shift in consumer behavior (Hongxin et al., 2022). It comes to the conclusion that spending among the younger generation is unaffected by the introduction of VAT. According to the results, the implementation of VAT has little effect on consumers' habits of buying things. Therefore, it backs the government's new plans to raise the VAT rate from 5% to 15% to boost national income in light of the COVID-19 pandemic.

## CONCLUSION

The positive trend in Saudi Arabia's VAT collection, which totalled SAR45.6 billion, suggests that VAT may become a significant source of fresh revenue for the Kingdom. Despite the criticisms levelled at the policymaker, an education campaign on the value of value-added tax (VAT) to stimulate economic growth as an alternative to relying on oil-reserves income should be made available to the public. This research looks into what motivates young Saudis to embrace VAT and why. The study uses five category characteristics to conclude that VAT is not an effective tax system since it does not address income inequality. However, the findings provided convincing evidence that respondents had a solid grasp of VAT and are aware of government intentions and implementation plans concerning VAT. The government may choose to launch publicity and education campaigns to raise people's understanding of VAT and encourage them to adopt it.

Most noticeably among the younger demographic. One method is to increase people's familiarity with VAT by teaching them about it; this can be done, for example, by including it in required courses like Taxation. It's worth noting that value-added taxation isn't only a means by which governments extort money from their citizens; it also offers important social benefits, many of which are particularly useful in emergency situations like the present COVID-19 outbreak.

As a perceptual study rather than an empirical research study, this research is limited in its ability to draw any firm conclusions about the acceptance or effects of VAT. Additional research on the VAT collects and its distribution channel could improve the quality of the available data for VAT's beneficial effects. As the first publication of its kind, this research aims to provide the groundwork for future research on value-added tax (VAT) implementation, especially in the tax-free GCC states.

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### Conflicts of Interest

The authors declare no conflict of interest.

### Institutional Review Board Statement



Not applicable.

### Informed Consent Statement

Informed consent was obtained from the respondents of the survey.

### Data Availability

The data used to support the findings of this study are available from the corresponding author upon request.

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