# FACTORS INFLUENCING TAX COMPLIANCE AMONG SMES IN JUJA TOWN.

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**A PROJECT SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF BACHELOR OF SCIENCE IN ECONOMICS OF THE JOMO KENYATTA UNIVERSITY OF AGRICULTURE AND TECHNOLOGY.**

# DECLARATION

I declare that this project is my original work and has not been presented for an award of bachelor’s degree to any university.

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HDB222-0263/2017

SIGNATURE…………………. DATE…………………

This project has been submitted for examination with the approval of my university supervisor.

Dr Tabitha Naiseku

SIGNATURE………………… DATE……………

# DEDICATION

This project is dedicated to my dear family and friends for their encouragement and who’s relentless support has brought me this far. May the almighty God bless you all.

# ACKNOWLEDGEMENT

I wish to appreciate the efforts of my supervisor Dr Naiseku for her guidance. She was also very understanding and patient. Her comments and great support shaped my project proposal concerning tax compliance. Also, I would like to appreciate Jomo Kenyatta University of agriculture and technology for providing the resources throughout the project.

# ABSTRACT

Tax payment is a civic duty and an imposed contribution by the government to contribute to her main source of revenue to provide public goods and services to its citizens. It is a compulsory unrequited payment to the government. In this study, we get to establish factors affecting tax compliance among the SMEs in JUJA County. If the SMEs don’t comply, then there is less tax collected leading to deficits in the total revenue collected by the government. Research study adopted descriptive research design. Secondary data was collected using and the analysis was carried out. The study showed that taxpayer’s knowledge, tax payes attitude and compliance cost were the main factors that determined the tax compliance rate by the SMEs. Similarly, tax data and tax learning tends to advance tax compliance than organizations thus informing tax payers on taxation laws and controls by having symposia and free courses on taxation. The study also concluded that tax rates are too high in the country. The fines and penalties charged for late fillings are high and for others the cost of filling the tax returns is high which requires hiring a professional to do the filling. This is expensive. The procedure of filling returns was also highlighted in the study. Since the new ITAX system by the KRA, the process is a bit strenuous especially to the people who have little knowledge in computer. As a result of this system, there have been wrong tax returns filed by the SMEs. The forms that should be presented by taxpayers are numerous and there are delays in electronic filling and payment systems. In this study, it emphasizes on tax payers learning since it advances tax compliance in general. The study also recommends that tax rates should be reduced since reduction in tax rate leads to increased development. Tax laws should also not be complex so as not to contribute to high wrong tax returns cases. Similarly, tax accountability should be emphasized with the different kind of taxes such as firm’s income tax, individual income tax, value added tax, petroleum profit tax and stamp duties since they are perceived to have a direct correlation to the GDP.

# ACRONYMS AND ABBREVIATIONS

**CGT** Capital Gain Tax

**EAC** East Africa Cooperation

**ETR** Electronic Tax Registry

**GDP** Gross Domestic Product

**GOK** Government of Kenya

**IEA** Institute of Economic Affairs

**KESRA** Kenya School of Revenue Authority

**KNCC** Kenya National Chambers of Commerce

**KRA** Kenya Revenue Authority

**MSEA** Micro and Small Enterprise Authority

**PAYE** Pay as you earn

**SME** Small Medium Enterprises

**TMP** Tax Modernization Program

**TOT** Turnover Tax

**USD** USA Dollar

**VAT** Value Added Tax

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# CHAPTER 1

## 1.1 Introduction

Tax compliance can be defined as a tax payer's willingness to follow the country's tax rules, such as declaring income, filing returns, and paying assessments on time. However, there is a contradiction in taxes between the desires of tax payers to minimize expenses and maximize profit and the government's objective to maximize revenue through increased tax compliance. Tax evasion is defined as a person's or a company's failure to comply with tax obligations. This is a challenge for the tax authorities more so for the Kenya Revenue Authority. . It reduces the amount of money that administrations must spend on basic areas of social and self-improvement, such as health, education, and infrastructure development (Cummings, 2007)The government spent 5.1 percent of GDP on it in 2011. Tax evasion accounts for roughly 8% of Europe's GDP. Tax evasion costs the economies of South and North America, respectively, 2% and 10% of GDP. This demonstrates how tax cheating reduces income accumulation even in developed countries. (Rile 2011)

Over 183 billion euros have been lost in Italy as a result of tax evasion. This comes after nearly two trillion dollars in debt and nearly ten years of tax evasion. As a result, Italy has promised to take tax evasion and money exchanges for goods and businesses off the radar of authorities seriously. Germany and the United Kingdom also had an agreement with Switzerland to recoup tax revenue from bank accounts held in Swiss banks by their subjects. South America has a global black-market economy to its GDP, followed by Europe and Africa, where salary avoided assessment experts total 20.5 percent of GDP, compared to 10.8 percent in North America (Association 1998).

Tanzania, Kenya, and Uganda have high rates of tax evasion because taxes are a component of their GDP. Uganda suffers only minor financial losses as a result of tax evasion. In 2011, Uganda lost 856 million USD, trailed by Tanzania, which lost 1.9 trillion USD. In 2011, the informal economy in Kenya accounted for more than 33% of the country's GDP and nearly 7% of total government consumption. Kenya's taxation rate would remain high, at about 20.9 percent.

In Kenya, taxpayers are categorized as small, medium or large depending on their business turnover or levels of income. Irrespective of one’s category, taxpayers in Kenya are required to comply with VAT, PAYE, Income Tax, Withholding Taxes and Customs duties in equal measure. In Kenya, SMEs are referred to as micro and small enterprises (MSEs) or micro, small and medium enterprises (MSMEs). Micro businesses have a maximum annual turnover of Ksh 500,000 and employ fewer than ten employees, according to the Micro and Small Enterprise Act of 2012. Small businesses have annual turnovers of between Ksh 500,000 and Ksh 5 million and employ 10 to 49 people. Medium businesses are not covered by the act, but have been described as having a turnover of between Ksh 5 million and Ksh 800 million and employing 50 to 99 people. In comparison to larger firms, SMEs' proximity to their consumers allows them to gain knowledge in a more direct and faster pace.

### 1.1.1 Determinants of tax compliance

Self-tax compliance requirements may be upgraded as a result of the societal culture of conformity to assessment. However, tax morale, attitude, and behavior are not in place, particularly in countries where the culture is not to pay taxes (Braughtigam. Et.al..2008). When people lack obligations and are receptive to using their money, it creates doubt in the minds of taxpayers about how tax assessments are made and organized, affecting their enthusiasm to pay levy payments. Due to high levels of fraud, taxpayers are unable to determine whether taxes paid are fully utilized in the financing of public goods and the provision of services, resulting in a change in their ability to pay and the possibility that they will avoid taxes in the future. If the legal framework does not uphold the rule of law, it will result in a decrease in rightfulness, sowing doubt among residents. Nations will not have the will to fund administration through tax compliance and will thus seek to avoid tax liabilities (Krichler, 2007).

There is a direct relationship between the size and type of punishments meted out to non-compliants and the level of tax compliance (Fisher & Friedman, 1994). Deficiencies in tax collection may be the result of a frail framework for identifying and prosecuting tax evaders. The use of relatives in SMEs through unpaid work reduces the likelihood of recognition, influencing the taxpayer's choice of compliance. SMEs typically operate in an imperious controlling environment, with a plethora of regulating organizations, high port charges, numerous charges, burdensome importing procedures, and numerous taxes that constantly put pressure on the operations ( Kinyua,2014).

The complexity of the governing structure and the tax system is a hurdle for most SMEs, who select their compliance level, which has an impact on their growth and performance. For SMEs, the tax system imposes higher expenses that have an impact on their day-to-day operations (Msato,2009). A tax system that is inefficient by nature wastes taxpayers' time as well as authority staff's time, and has expensive collection charges (Fatzbod, 2007). The majority of SMEs are impacted by higher compliance costs than large corporations (Weichendrieder, 2007). In Kenya, there is no act of parliament that defines a small business. Neither the income tax chapter nor the turnover tax rules, which govern SMEs' taxation, provide any definitions or specify any of the phrases used to refer to, mean, or represent SMEs. Section 12c of the income tax code refers to persons and thresholds that determine who is obligated to pay turn over tax. Individuals who earn more than 500,000 from a business but less than 5 million in a calendar year must pay turnover tax, according to Rule 3(1) of the turnover tax. As a result, the rule disallows the use of the term or definition of the term SME. The use of thresholds only to define persons liable to pay turnover tax is a more convenient way of avoiding lengthy debates about what the term "SME" means and to whom it refers (Kinyua, 2012).

The recently approved microfinance statute No. 19 of 2006, which went into effect on May 2, 2008, does not identify SME or micro low-income households. The act mentions the micro or low-income households that it is meant to help. Definitions can be found in government policy papers, development plans, budgets, and the Kenya Revenue Authority's unified tax system program and reports in Kenya. In Kenya, terms like jua kali sector, MSME, and MSE are used. Micro, small, and medium enterprises are referred to as MSME. According to the UTS, a micro, small, or medium enterprise is one that employs one to nine to forty-nine people, and a medium enterprise is one that employs fifty to ninety-nine people (Wanjiru, 2010)

In this article, references to SMEs or the informal or jua kali sector refer to these variables, which identify and represent SMEs as individuals under the income tax, microfinance act, relevant government reports, seasonal papers, development plans, baseline surveys, and reports on the United Tax System.

Kinyua (Kinyua, 2014)

### 1.1.2 Tax compliance in Kenya

Tax compliance, according to Brown and Mazur (2003), is a difficult concept to define because it is a multi-faceted measure. They went on to break it down into three parts: reporting, payment, and filling compliance. Tax compliance is defined by Kircler (2007) as a taxpayer's readiness to pay taxes honestly, whereas tax evasion is defined by Cummings (2007) as a tax payer's refusal to comply with tax obligations. The complexity of tax remittance is based on the following considerations: the amount of information necessary in terms of tax regulations is excessive, particularly when it comes to the computerized component of tax compliance decision (Richardson,2006). Tax compliance is defined by Andreoni, Erdad, and Feinstein (1998) as a taxpayer's desire to observe tax regulations in order for a country's economy to achieve equilibrium. Tax evasion, according to Rile (2010), impedes revenue collection through reducing government resource mobilization.

Tax penalties, lack of awareness, high tax rates, and high compliance costs are all variables that contribute to tax fraud and evasion, according to William and Round 2009. Whether voluntarily or unwittingly, SMEs can break tax regulations. Emerging economies must guarantee that their tax systems are efficient and effective for SMEs, and that they do not harm them. Poor tax systems and policies are among the issues that most governments encounter. The basic goal of tax policy is to make sure that everyone follows the rules (James & Alley, 2004). In Kenya, SMEs operate in the informal sector, which has semi-organized and unregulated activities that are smaller, according to the 2016 Economic Survey Report.

The ability and willingness of SMEs to comply is determined by their understanding and interpretation of tax laws. When SMEs have a positive attitude toward tax compliance compared to those who have never attended any tax related workshop or seminar in areas related to taxation laws, attitudes toward tax compliance can be improved through increased taxation understanding (Mohd,2010). According to OCED 2001, compliance is divided into two types: technical compliance and administrative compliance, while Cobham 2005 explains that tax compliance affects emerging economies and is a major challenge, which has promoted and encouraged radical tax reforms in these economies. According to studies, SMEs bear the brunt of regulatory burdens ( Pope & Abdul-jabbar,2008). Kenya is one of the low-wage or low-compliance countries attempting to ensure effective and compelling tax administration. With the specific end goal of ensuring tax compliance and, as a result, increasing income. Kenya Revenue Authority administers taxes in Kenya, which was established by a parliament act on July 1st, 1995, cap 469. KRA should advance compliance with Kenyan tax guarantee dependable by exceptionally energetic and capable staff, thereby expanding income gathering in any event conceivable costs for Kenyans social-monetary prosperity.

### 1.1.3 Small and Medium enterprises in Juja Town.

Juja town is a fast-growing town due to the numerus economic activities that are ongoing as well as hosting JKUAT university which has enabled growth of very many businesses. Most businesses her are SMEs. SME is an abbreviation for small and medium-sized enterprise. They are linked to informality and are commonly referred to as the informal sector. However, it can be deduced that the various definitions of SMEs advanced were heavily influenced by one or more schools of thought. There is no universally accepted definition of SMEs, but there are certain common factors that appear in all definitions. They include the number of employees, the number of sales made, and the firm's capital assets.

According to Hall and Harvie (2003), SMEs are important in a country's economic development and growth because they create jobs and build a flexible and adaptable foundation for a competitive economy. Small and Medium enterprises (SMEs) are engines of growth, vital to most economies. Micro businesses and SMEs account for 95% of firms in most countries. In Kenya SMEs represent a vital part of the economy, being the source of various economic contributions through the generation of income via exporting, providing new job opportune The proximity of SMEs to their customers allows them to acquire knowledge in a more direct and faster flow than larger firms., stimulating competition, engine for employment, contribution to GDP, aid industrial development, satisfy local demand for services and introducing innovation and support to large firms with inputs and services. In 2014, 80% of jobs created were dominated by SMEs.

Juja Town is a fast-growing town, recently it’s on the process of transforming into a city. It has a lot of economic activities ranging from tourism, trade, construction, service industry and manufacturing. It is one of the counties that generates a lot of income in Kenya with the potential of generating even more if its full potential is tapped. This can be done through proper fiscal planning to ensure the various SMEs (Which is the majority of business in Juja ) operate in a favorable environment allowing them to easily file their remittances that are due.

## 1.2 Statement of the problem

Low tax compliance is a major concern for the policy makers in many developing countries. This is because it limits the capacity of governments to raise revenue for developmental and recurrent purposes. Tax payer education is a tool designed to enable taxpayers to understand tax laws and procedures. It involves training of special units within the revenue departments; for providing counseling and support to the taxpayers. Tax revenues have, for quite some time, remained low relative to the number of registered and non-registered firms and individuals who are legally qualified to pay taxes.

A large segment of the\r informal sector, especially the SMEs in Juja CBD exhibit low tax compliance levels which is a great loss of revenues meant for public expenditure. It is for this reason that this research was undertaken to identify the effect of taxpayer Education on tax compliance among small and medium enterprises (SMEs) in the CBD. SMEs are less tax compliant than large corporations and are thought to be more difficult to gather assets from the informal sector (Akinboade 2015). When taxpayers and revenue collection authorities fulfill their responsibilities, a country can develop a positive tax culture. Taxpayers' defiance, delusion, and demotivation stem from an inadequate understanding of the tax obligations imposed on them. Tax evasion is one of the issues that a country faces that impedes its development (Karingi, 2005).

Kenya Revenue Authority introduced online filling with the goal of broadening the tax base and increasing revenue collection. This required taxpayers to be trained on how to use the new filling system, which will increase taxpayer compliance levels. User education will increase SMEs' compliance, and they will be aware of their responsibilities and the penalties that will be imposed if they do not comply ( Mohani 2013). Several studies on tax compliance have been published. Lumumba, Magutu, and Wanjohi (2010) investigated how taxpayer attitudes and influences influence compliance among SMEs in Kerugoya.. This led to the conclusion that taxpayers believe the tax system is unfair. The majority of decent tax payments are paid in a variety of ways. Magiya (2016) led an investigation into the determinants of tax compliance among SMEs in Juja 's east area. He discovered that increased taxpayer understanding of assessment rules and tax frameworks, as well as increased government responsibility in the provision of public goods and services, result in higher compliance levels and consequently more revenue collection.

Thiga and Muturi (2015) investigated the elements that influence tax law compliance in Kenya. Tax rates and compliance costs were discovered to be the most significant contributors to tax compliance. In all of these studies, no one has looked into the factors that influence tax compliance among SMEs.

## 1.3 Objectives of the study

### 1.3.1 General Objectives

To determine factors that influence tax compliance among SME’s in Juja Town

### 1.3.2 Specific objectives

1. To assess the availability of tax information as a factor influencing tax compliance

among Small and Medium Enterprises

2. To determine how Small and Medium Enterprises attitude about tax influence tax

compliance

3. To determine the extent to which costs incurred by small and medium enterprises in

being tax compliant influence their level of tax compliance

## 1.4 Research Questions

1. How does the availability of tax information influence tax compliance among Small and

Medium Enterprises?

2. How does the attitude of Small and Medium Enterprises about tax influence tax

compliance?

3. To what extent does the cost of tax compliance explain tax compliance among Small and

Medium Enterprises?

## 1.5 Significance of the study

The findings of this study are expected to provide concepts and foundations for developing a framework for investigating tax compliance behavior among SMEs. In order to establish appropriate tax policies for SMEs, the Kenyan government and its revenue collecting organization (Kenya Revenue Authority) would obtain additional knowledge as a consequence of this study. The findings are beneficial to the business community and management teams in terms of understanding tax compliance environmental variables and how they can be addressed or dealt with. Finally, scholars and researchers who need to grow and/or advance their expertise in the field of tax compliance and administration will be interested in the study.

Firms and individuals adopting the ever-changing tax systems and laws will gain an insight on the factors and relationship in the context of tax compliance thus helping forge a good relation between the government and tax payers in the context of SMEs.

## 1.6 Scope of the study.

The study concentrated on the compliance levels of SMEs in Juja County. The study focuses on the value of tax information, the cost of compliance, and tax payers' perceptions of the impact of tax compliance.

The research was conducted on a sample of 1350 small and medium-sized businesses (SMEs) who file returns using KRA data. The study focused on SMEs that primarily operate in the following industries: service, manufacturing, and trade.

# CHAPTER TWO.

## 2.1 Introduction

This section examines the theoretical and empirical literature on tax compliance from previous investigations. It also aids in identifying knowledge gaps in relation to tax compliance and related studies. This section delves into the factors, theories, theoretical framework, and research gaps in depth.

## 2.2 Theoretical review.

### 2.2.1Theory of Reasoned Action

Martin Fishbein and Icek Ajzen developed the theory in 1980. This was done to improve Anderson's information integration theory. The behavioral intention and duration of pre-existing human attitudes serve as the foundations for enhancement. This response can be predicted by human intentions, which means that the individual will be affected or influenced not only by his perceptions but also by his expectations. According to this theory, three factors influence human behavior and intentions: personal opinion (whether it is negative or positive), favorable or unfavorable, and negative or positive. Individual attitudes must be specific because specificity allows for prediction of subsequent behavior. Second, there is the prevalent subjective social pressure from other people's expectations, which is individual normative beliefs or the need to conform to what others expect. Behavioral intention is viewed as a precursor that directly leads to actual behavior, implying that an individual will react based on behavioral intention formed and developed. Individual actions, according to the theory, are influenced by perceptions and attitudes, and the theory acknowledges that reality that indicates specific behavior and perceived social norms may contradict it. Ogjen (2003)

### 2.2.2 The Ability to pay Theory of Taxation

Mill, an English economist, (1806-1873), Jean, a Swiss philosopher, (1712-1778), and Say, a political economist, were among the first to advocate it (1767-1832). According to this view, a person's income should be taxed (Jones et al, 2011).The core concept of this theory is that the tax burden should be shared by society's members based on principles of fairness and equality, and that these values require that the tax burden be apportioned according to their respective ability to pay. According to this theory, TOT taxpayers should pay regardless of their financial ability to pay (Chigbu, Eze and Ebimobowei, 2012).

### 2.2.3 The tax morale theory

German tax psychologists were the ones who first proposed the tax morale theory. Individual factors that drive an individual to comply with his or her tax duties are referred to as tax morale. Tax morale seeks to explain how and why a tax payer's morality effects his tax behavior as a factor of tax behavior. According to studies, tax evasion is linked to low tax morale. (Mocetti,)

Taxpayers may be tempted to evade taxes if the communities in which they live or operate are opposed to tax evasion. Taxpayers are more likely to comply with their tax obligations if their friends, relatives, and acquaintances do so. Taxpayers will also evade taxes if they believe others are getting away with it. If a society tolerates tax evasion, it will encourage evasion (Waweru, 2004). Religious beliefs are a factor in tax evasion because studies show that tax payers with strong beliefs are more likely to be compliant even if they believe the tax rate is high (Gee,2006)

In some cases, taxpayers may feel morally justified in evading taxes if the quality and quantity of public services and goods are inadequate. The inverse is also true. Evasion rates are low in economies that provide adequate public goods and services. Taxpayers will lend to meet their tax obligations if they believe their government is honest, democratic, and participatory, and if they believe they have a meaningful role in government. (Cummigs,2007). Because tax payer attitudes are important predictors of tax evasion, the study aims to interpret SMEs' tax attitudes and how they contribute to tax evasion.

## 2.3Emperical review

Okoye, Aknboe, and Obara (2012) carried out an investigation into tax information, administration, and tax payer compliance knowledge. The investigation looked into the impact of tax data, organization, and learning on taxpayer compliance in Nigeria's Ekiti state. The findings revealed a positive relationship between tax data and learning. This study concluded that the legislature should educate potential taxpayers on taxation laws and controls by organizing free symposia and courses.

According to Osambo(2009), the increased rate of tax collection of small micro enterprises in Africa, particularly Kenya, necessitates consideration of research domains devoted to observing the general effects of duty accumulation on SMEs by pondering tax appraisal direct in countries. Osambo believes that a higher tax assessment rate is a serious threat. The findings show that increasing tax rates leads to higher development, appropriation, and offering costs, which leads to higher costs and, as a result, customers change their purchasing behavior. Individuals respond to higher prices by purchasing fewer items. At the point when deals fall, manufacturers cut back on generation and fe specialists may lose their employments.

Masinde (2010) discovered that tax compliance is low in SMEs in a study to determine the revenue potential of SMEs in Kenya. Several factors, including poor management and the establishment and dissolution of SMEs, make it difficult for tax administration to keep up with them.

Adesina and Obazee (2016) investigated taxation information, penalties, and assessment compliance in Nigerian SMEs. The examination was conducted using a survey design, and information was gathered via survey and broken down using the least square technique. Tax learning had a huge positive effect on tax compliance, whereas taxation penalties had a negligible positive effect on tax compliance.

According to Isa (2012), tax unpredictability is another detectable significance of taxpayers compliance factor influencing compliance behavior and may be the beginning of tax evasion. Furthermore, Loo, McKerchar, and Hansford (2010) emphasized that tax laws are excessively complicated for taxpayers, making it impossible to keep track of tax law and subsequent tax law changes. These issues could theoretically be the reason why taxpaying corporations seek the services of outside tax experts when confronted with taxation challenges.

Adeyeye and Otusanya (2018) investigated the impact of tax payers' perceptions of government accountability, transparency, and fiscal corruption reduction on voluntary tax compliance. The study's findings show that each independent variable has a significant positive relationship with the dependent variable. According to the study, the combined effort of the government's accountability, transparency, and fiscal corruption reduction appears to have a greater impact on tax compliance.

## 2.4 Conceptual framework

### 2.4.1 Tax compliance cost

A compliance cost is the time or money spent to meet regulatory obligations. Legislation or regulation, for example. People or organizations, for example, who have registered for value addition tax have the additional duty of keeping thorough records of all input and output tax to make it easier to complete VAT returns This may necessitate them hiring someone. This would be considered a compliance cost if you were not skilled in this subject. Typically, compliance expenses. Include in your budget all costs connected with following the law, including preparation and administration. in addition to the actual time and money spent on form filiing.

High compliance costs can lead to tax evasion and fraud, as well as a reduction in the country's competitiveness in terms of taxation attractiveness (Ojeka,2012). The total cost of the tax system exceeds the amount of tax paid. It also includes the cost of tax paid and paperwork. The IRS estimates that Americans spend 6.6 billion hours per year filling out tax forms, which economists refer to as tax compliance costs. According to an OECD study on tax compliance simplifications (OECD, 2001), compliance costs rise with the number of taxes an entrepreneur must pay, the complexity of tax rules, the frequency with which tax returns must be filed, and the number of levels of government involved in tax levying and collection. Taxes create complexity and costs that are irrelevant to SMEs, and the difficulties may increase where multiple levels of government are involved, such as in Kenya's devolved government. This results to SMEs avoiding taxes as it affects the business.

Tax plays an important role in the growth of Small and Medium Enterprises (SMEs) in low-income countries like Kenya. Alignment of the tax system to the specific SME growth needs can be considered an important agenda for the policy-makers. SMEs are an important force for economic development and industrialization in poor countries. Kenya's Revenue Authority is trying to mobilize revenue by bringing more SMEs into the tax bracket by introducing Turnover tax (TOT) key considerations are to minimize administrative burden while ensuring compliance, including considering the drivers and impacts of operating in the informal economy. There are four broad categories of obligations identified as registration in the system, Timely filling or lodging of the required information, reporting of accurate information and payment of taxes in time.

### 2.4.2 Tax information

Kenya introduced the self-assessment system for taxation in 1992. The tax payer bears the responsibility of correctly declaring and paying taxes. A tax payer is required by law to file a self-assessment return within six months of the end of the fiscal year. After filing the return, the KRA reviews it and, if it believes the taxpayer did not disclose the correct taxes, it is authorized by law to conduct an audit to verify the information disclosed by the tax payer (Muiru,2012).

Taxpayers sometimes find themselves in difficult positions when making significant business decisions because the handling of complicated commercial transactions is not always obvious under the law. Although our tax statute does not provide for advanced tax decisions, tax payers frequently seek the commissioner's interpretation of different tax laws or the tax consequences of specific business transactions. To maintain confidentiality, this is sometimes done on a non-name basis. (Muiru,2012)

### 2.4.3 Tax payer’s attitude.

Various studies' attitude issues revolve around tax fairness, improper government revenue collection, and pure intent to evade tax payment for the collective good of the individual interest. Positive and negative judgments of objects are determined by one's attitudes. Individuals are believed to act in accordance with their attitudes. Taxpayers who have a good attitude about evasion are predicted to be less compliant than those who have a negative attitude. The vast majority of people think evasion is a good thing (Kirchler, 2001). In a study on tax evasion released in May, researchers revealed significant, albeit minor, links between opinions and self-reported tax evasion. (2005) (Trivedi) Weigel's model of tax evasion behavior includes attitudes and moral judgments regarding the morality of tax evasion as antecedents of tax compliance. Attitudes explain only a percentage of self-reported tax evasion, but are significant predictors of actual activity, according to data from both tax evaders and honest taxpayers. There is a strong link between self-reported tax evasion and attitude. Both the power and trust dimensions are influenced by attitudes. Positive views, on the other hand, will increase trust in authority and voluntary compliance. On the other hand, opinions toward authorities will play a role in determining whether or not power is used maliciously. Tax views are also influenced by how the money is perceived to be used, and hence are linked to knowledge. (2001, Krichler)

**2.4.5 Conceptual frame work.**

Figure 1

**Tax Information**

* Level of access
* Knowledge of taxation system
* Understanding of taxes

**Tax Compliance Cost**

* Cost of hiring staff
* Cost of record keeping
* Time

**Tax Compliance**

* Increased amount of taxes paid
* Timely payment of taxes

**Taxpayer’s Attitude**

* Attitude towards public goods
* Peer attitude
* Motivation

# Chapter 3

## 3.1Introduction

This chapter outlines the research methodology as a means of reaching the study's goal. This comprises the research design, study population, study sample, data collection instruments, and data analysis.

## 3.2Research Design

For this research, a descriptive survey design was used. For this study, a descriptive survey approach was optimal since it describes features connected with the subject population, namely causes that cause individuals to behave the way they do. Cooper and Schindler (Cooper, 2003) define descriptive design as the discovery and measurement of the cause and effect of relationships between variables. According to Mugenda and Mugenda (Mugenda, 2003), descriptive research determines and describes the way things are and attempts to define potential behavior, attitude, values, and features of such things. A descriptive approach was utilized in the study because it allows the researcher to obtain a vast amount of detailed information on the population being investigated. The data required for analysis needed to be obtained from a large population of SMEs operating in Juja Town hence a survey approach was ideal.

## 3.3Target population

The study focused on SMEs operating in Juja Town. The study's unit of analysis is any SMEs registered with the Kenya Revenue Authority. According to Cooper and Schindler (2003), a population is an element that serves as the subject of measurement and the unit of study. Similarly, Mugenda and Mugenda 2013, as well as Ngechu 2004, state that a target population is an entire group of people or things with similar characteristics that the investigator prefers. This study's target population consisted of SMEs in Juja Town.

Table i

|  |  |  |
| --- | --- | --- |
| **STRATA** | **TARGET POPULATION** | **SAMPLE SIZE** |
| Manufacturing | 186 | 18 |
| Trade | 854 | 85 |
| Services | 384 | 39 |
| **TOTAL** | **1425** | **142** |

## 3.4 Sampling size and sampling technique

Sampling is a technique for picking a subset of a group from a larger population in order to represent the characteristics of the larger group or population of interest. The benefit of sampling is that it minimizes the time and expense required to conduct the investigation. Because sample accuracy is mostly controlled by the sampling frame, the researcher achieved a high degree of correlation between the sampling frame and the sample population. The sample size is a critical aspect of any empirical investigation in which the goal is to draw conclusions about a population from a sample. Furthermore, gathering data from fewer cases allows for the collection of more specific information (Saunders, Lewis, and others). According to Kothari (2004), for populations under 10,000, a sample size of 10% to 30% is a good approximation of the target population. The study used stratified random sampling to select a sample size of 10% of the target population. The sample size for this study was 135 people who were picked

## 3.5 Data collection techniques and instruments

An introduction letter was issued to the sampled entities for consent to collect data from the respondents. The questionnaires were administered to the respondents directly by the researcher. For those respondents who were not available for a sit-in filling of the questionnaire, it was e-mailed to them. The interviews were conducted at a time and place convenient to the respondents to provide an environment in which the respondents would feel free to participate.

Primary data was collected for the study. A self-administered questionnaire was used to obtain primary data. The questionnaire used both structured open-ended and closed questions. The questionnaire responses aided in acquiring a thorough grasp of the issues impacting tax compliance among SMEs. Based on a set of predetermined questions, the questionnaire gathered statistically meaningful data on respondents' perspectives on an issue of interest. The questionnaire was divided into three major sections. The first section dealt with biographic data, the second with factors influencing tax compliance, and the third with strategies for improving tax compliance in Kenya.

Secondary sources were used to collect data for the study. Secondary data was gathered from well-documented sources such as books, magazines, and newspapers, as well as journals and internet literature. The secondary data came from KRA. This data collection method was considered by the researcher as appropriate in providing safe basis for generalization and high accuracy

## 3.6 Data analysis

The research expert independently assessed the validity of the interview questions in relation to the research objectives. To determine the patterns revealed in the data collected, data analysis was guided by the aims and objectives of the research. The data collected was then coded and tabulated and analyzed using SPSS version 22 by both descriptive statistics which include mean and standard deviation to capture characteristics of the variables under study and inferential statistic which include Pearson correlation and regression coefficient which was used to analyze the relationship between independent and dependent variables The overall model significance was determined using analysis of variance (ANOVA). The calculated f statistic was compared to the tabulated f statistic in particular. To test whether the total model was significant, a crucial p value of 0.05 was utilized. The influence of independent variables on dependent variables was tested using a multivariate linear regression model. The following was the multiple linear regression model:

Y =β ₒ +β 1X1 +β 2X2 + β3X3 + + ԑ

Where;

Y = tax compliance

X1 = compliance cost

X2 = tax information

X3 = tax payer attitude

βₒ = Constant term

1 –β4= Beta coefficients

* = Error term

# CHAPTER FOUR

# RESEARCH FINDINGS AD DISCUSSIONS

## 4.1 Introduction

This section of the study focuses on the findings, presentations ad discussions. The data was gathered from the survey ad was analyzed using the SPSS and descriptive analysis statistics and presentations.

## 4.2. Response rate

During the study, the response rate was perfect where it signified 85% as provided by Mugeda and Mugeda 2003, and echoed by Kothari 2004 that any response that is 50% is good and adequate to be administered in the study. According to Babbie 2004, a response rate above 70% is excellent. Our study therefore had reached the recommended threshold.

### Table showing response rate

|  |  |  |
| --- | --- | --- |
| Variable | F(n) | Percentage |
| Returned | 120 | 85 |
| Incomplete | 22 | 15 |
| Total | 142 | 100 |

Table iii Table Table iv

## 4.3 Descriptive analysis

Table showing descriptive analysis

Table vi

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Variable** | **Strongly disagree** | **Disagree** | **Uncertain** | **Agree** | **Strongly agree** | **mean** | **Standard deviation** |
| **Tax information** | 5.90% | 2.50% | 31.90% | 11.80% | 47.90% | 3.93 | 1.2 |
| **Tax attitude** | 5.90% | 9.20% | 24.40% | 45.40% | 15.10% | 3.55 | 1.05 |
| **Compliance cost** | 6.70% | 11.80% | 5.90% | 31.90% | 43.70% | 3.94 | 1.26 |
| **Tax compliance** | 10.10% | 16.00% | 22.70% | 42.90% | 8.4% | 3.24 | 1.13 |

As in the table above we were able to get the following information on matters to do with tax information and compliance, tax payers’ attitude and compliance, compliance cost and compliance and finally compliance levels.

On tax information, we were able to find the following on importance of it as follows; 5.9% strongly disagreed, 2.5% disagreed, 31.905 were uncertain, 11.80 agreed and 47.90% strongly agreed. These findings are consistent to the study of Adesina and Obazee (2016) that established taxation information, fines and assessment compliance in Nigeria SMEs scale endevours. The findings established that tax learning had positive effect on compliance. The government tends to emphasize o tax payers’ information to encourage them to comply.

In the findings of the study about the tax payers’ attitude and its influence on compliace.5.9% strongly disagreed,9.2% disagreed,24.4% were uncertain, 45.5% agreed and 15.10% strongly agreed. These findings were consistent to the findings of Osambo (2009) which exerts that positive behaviour in tax payers attitude prompts higher development, appropriation and offering costs which prompt higher costs and customers changing their purchasing conduct.

On the tax compliance cost and compliance 6.7% strongly disagreed, 11.80% disagreed, 5.90% were uncertain, 31.9% agreed ad 43.7% strongly agreed. The study findings were in agreement with other study conducted in 2010 that established an adoption of technology enhances increased tax cost on tax compliance especially for huge tax payers since technology enhances tax compliance for large tax payers and it is a vital parcel for growth of organizations. A study of Muita(2010) established effective online filling tax requires skills and infrastructure and conducive business operating environment. Tax compliance incorporates every single formal system and related exercises that taxpayers need to conform to tax commitments. The commitments are in four categories namely: registration, timely documentation, detailing complete and exact data and finally payment of tax on time according to necessity of the law.

Finally, the study aimed at also having the number of people who comply with tax necessities the following was the response, 10.1% strongly disagreed, 16% disagreed, 22.7% were uncertain, 42.9% agreed and finally 8.4% strongly agreed. From the studies, tax compliance will mainly depend on several factors. According to Adebayo (2017) on the effect of accountability and transparency on tax returns in Nigeria and found out that tax accountability and transparency with greater emphasis on the kid of taxes such as income tax, individual income tax, value added tax, petroleum profit tax and stamp duties is perceived to have a direct correlation to the Gross Domestic Product (GDP).

## 4.4 Correlation analysis

Table showing correlation analysis

Table viii

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Variable** | **Tax compliance** | **Tax information** | **Tax payers’ attitude** | **Compliance cost** |
| **Tax compliance** | **1** |  |  |  |
| **Tax information** | **0.546\***  **0.003** | **1** |  |  |
| **Tax payers’ attitude** | **0.639**  **0.00** | **0.11**  **0.235** | **1** |  |
| **Compliance cost** | **-0.543**  **0.00** | **0.172**  **0.061** | **0.546**  **0.00** | **1** |

As in the correlation analysis, the findings show that taxpayer information and tax compliance have appositive relation at (r-0.546: p<0.00).

Tax payers’ attitude and tax compliance have a significant and positive relation of (r-0.639: p<0.000)

Compliance cost had a Negative relation with tax compliance of(r-0.543:p<0.00)

This shows an increase in tax information, tax payers attitude variable leads to an increase in tax compliance, while a increase in the compliance cost leads to a decrease in the compliance levels.

## 4.5 Regression analysis

The tax compliance was to be determined by taxpayer’s information, tax payers’ attitudes and compliance cost. They are supported by coefficient that is 47.5% that explains the study variables of the variation of dependent variable that is tax compliance. The study further explains that the model applied to link the study variables were satisfactory.

Table showing analysis of varian Table x

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Sum of squares** | **Df** | **Mean square** | **F** | **Sig.** |
| **Regression** | 34.878 | 4 | 8.719 | 25.807 | 0.00b |
| **Residual** | 38.5187 | 114 | 0.338 |  |  |
| **Total** | **73.395** | **118** |  |  |  |

The table shows taxpayer information and tax compliance have a significant and positive relation at (r-0.345: p<0.00). the finding further shows tax payers attitude and tax compliance have significant positive relation of (r-0.433: p<0.00) while compliance cost had a negative relation of (-0.203: p<0.00) .

Table Showing model fitness

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Model | R | R squared | Adjusted R squared | Standard error for the estimate |
| 1 | 0.689a | 0.475 | 0.457 | 0.058127 |

Table xiv

The significant testing of the p value shows that level of relation of the study of independent variables to dependent variables. If the study could have had a less critical value than that is referred to as probability value p that statistically set at 0.05, the conclusion would be that the model is significant in explaining the model and if not, it would be insignificant.

The ANOVA analysis shows that overall model was statistically significant and the results further show that independent variables are good predictors of tax compliance as supported by F statistics of 25.807 ad the p value (0.000) with less than conventional probability of 0.05 significant level.

### Table showing regression coefficients.

Table xv

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **B** | **Std. error** | **T** | **Sig.** |
| **Constant** | **0.902** | **0.388** | **2.327** | **0.022** |
| **Tax information** | **0.345** | **0.081** | **4.259** | **0.000** |
| **Tax payers’ attitude** | **0.433** | **0.082** | **5.26** | **0.000** |
| **Compliance cost** | **-0.203** | **0.087** | **2.35** | **0.021** |

The optimal regression generated was:

Y = 0.902 + 0.345X1 + 0.433X2 - 0.203X3

Y = tax compliance

X1 = information

X2 = tax payers’ attitude

# CHAPTER FIVE

# SUMMARY, RECOMMENDATIOS AND CONCLUSIONS

## 5.1 Introduction

This chapter presents the summary of the results of the study and the main conclusions drawn from analysis of the data in Chapter Four. It entails summary of the findings, conclusions made, policy recommendations, limitations of the study and suggestions for further research as per the findings which was to study the factors affecting tax compliance among Small and Medium enterprises in Juja CBD.

## 5.2 Summary of the findings

The study was aimed at determining the factors affecting tax compliance among SMEs in Juja County.

The study established that there is a positive relationship between taxpayers’ information and compliance among the SMEs. The study shows tax information leads to an increase in the tax compliance of SMEs. As in the correlation analysis, the findings show that taxpayer information and tax compliance have appositive relation at (r-0.546: p<0.00). These findings are consistent to the study of Adesina and Obazee (2016) that established taxation information, fines and assessment compliance in Nigeria SMEs scale endevours. The findings established that tax learning had positive effect on compliance. The government tends to emphasize o tax payers information to encourage them to comply.

Tax payers’ attitude and compliance have a significant and positive relation of (r-0.639: p<0.000). This implies that tax payers’ attitude and compliance has a positive relation. These findings were consistent to the findings of Osambo (2009) which exerts that positive tax payers attitude prompts higher compliance.

Compliance cost has a negative relation with tax compliance of(r-0.543:p<0.00). The study findings were in agreement with other study conducted in 2010 that established an adoption of technology enhances tax compliance especially for huge tax payers since technology enhances tax compliance for large tax payers and it is a vital parcel for growth of organizations but for small and medium, enterprises, this is rather an additional cost which will hence force them to evade taxes.

## 5.3 Recommendations

On the issue of tax payers information and compliance, the study recommends that tax payers learning should be emphasized since tax learning advances tax compliance than tax organization. The government through its various organizations should instruct tax payer’s on taxation laws and controls by providing free symposia and courses.

The study shows that with an increase in tax payers’ attitude, the compliance level will increase. If the tax payers lack confidence or rather have no need in paying the taxes, they will evade taxes and not comply.

The study recommends on compliance cost and compliance that tax laws on the process of compliance should not be complex so as not to contribute to wrong filling of returns. It also should lessen the time take for organizations to round up data and reduce time taken in holding up ques to file returns. The procedures should be smooth and takes less time.

The study further recommended that the tax authority KRA should have offices in each county to address issues regarding taxes such as tax penalties, filling taxes, tax computation and finally tax differentiation.

KRA should also regularly implement reforms on publicizing prosecution of non-complaints by providing incentives for voluntary compliance and laws should be reviewed to strengthen loopholes exploited by non-compliant SMEs.

KRA should create more awareness on tax compliance among SMEs through policy documentation which classify different SMEs entity

KRA should regularly educate and train SMEs on tax related issues and modes of tax payments and collection.

KRA should make the process of taxation very simple to favor SMEs owner with little or no education to make compliance easy for them

## 5.4 Conclusions.

In conclusion the study shows that tax information and tax payers’ attitude have a positive relation to tax compliance. The research established that it was important to create awareness on tax laws, create awareness on how tax system is structured and administered, have less sophisticated rules for taxation for non-professional to understand, have readily available tax rules to encourage tax payers.

SMEs may decide not to remit taxes at all due to negative perception that tax system is unfair and they are overpaying taxes and services that are provided to the government are not motivating. According to Porcano (2004) the significant determinant of tax payer willingness to pay tax is the perception they have on the fairness of tax system. Richardson (2006) established in his study findings that perceived fairness plays an important towards tax evasion. Reforms of tax laws have turned the system into more complexes and this can be another reason for tax evasion. For SMEs to enhance tax compliance the rules of taxation must be simple, clear and comprehensive in order to make computations in their own discretion. Generally, the complex nature tax system increases as the tax laws become more and increases with time. Richarsdon (2006).

Understanding and interpreting tax laws determines SMEs ability and willingness to comply. Attitudes towards tax compliance can be improved through enhancement of taxation understanding when SMEs have a positive attitude in comparison with one who never attended tax related courses and workshops Mohd (2010). A study by Hite and Hasseldie (2001) established that tax authority should emphasize on offering tax course because it will impact positively on compliance.

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**Appendix I: Questionnaire**

This questionnaire is designed to collect data on the factors that affect tax

compliance among SMEs in Juja town. The data shall be used for academic purposes only and it will be treated with great confidentiality.

**Section A: Demographic Information**

**1. Gender**

Female [ ] Male [ ]

**2. Indicate where you fall among the following age brackets (years**)

Below 25 [ ]

25-34 [ ]

35-44 [ ]

45-50 [ ]

Above 51 [ ]

**Section B: Tax Registration**

1. Do you have a KRA PIN number?

Yes [ ] No [ ]

**2. When did you register for a KRA PIN number**?

2013 or before [ ]

2014 or after [ ]

**3. If registered in 2013 and before, have you migrated to the itax system?**

Yes [ ] No [ ]

**4. What is your tax obligation?**

Turnover tax (TOT) [ ]

Value added tax (VAT) [ ]

Income tax (IT) [ ]

Pay as you earn (PAYE) [ ]

Corporation tax (CT) [ ]

Withholding tax (WT) [ ]

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**Section C: Filing Tax Returns**

**1. Do you file your tax returns**?

Yes [ ] No [ ]

If yes, when did you last file your returns?

Yes [ ] No [ ]

**2. Are you aware of the due dates for filing your tax returns?**

Yes [ ] No [ ]

If yes, what is the due date? \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

**3. Have you ever been penalized for filing your returns late?**

Yes [ ] No [ ]

If yes, did you pay the penalty fee?

Yes [ ] No [ ]

**4. What is the amount charged for failing to file or filing your returns** **late?**

Ksh 1,000 [ ]

Ksh 1,200 [ ]

Ksh 10,000 [ ]

Ksh 12,000 [ ]

**Section D: Tax payer education and trainings**

1. Are you aware of any tax payer education programs conducted by KRA?

Yes [ ] No [ ]

If yes, have you attended any of the tax payer education programs?

Yes [ ] No [ ]

**2. Which of these areas of tax payer education trainings have you been trained o**n?

KRA PIN registration [ ]

Filing tax returns through itax system [ ]

Records keeping [ ]

Payment of taxes [ ]

**3. Do you maintain any financial records for your day to day activities in your business**?

Yes [ ] No [ ]

**4. Who prepares your business records**?

Self [ ]

Clerk / Accountant [ ]

Other [ ]

**5. Who files your tax returns?**

Self [ ]

Clerk / Accountant []

Other [ ]

**6. Have you ever been penalized for wrong record keeping?**

Yes [ ] No [ ]

**7. Please rate the following statements in regards to Taxpayer awareness programs.**

Rate on a scale of 1-5 where; 1 = Not at all

2 = To a less extent

3 = To a moderate extent

4 = To a great extent

5 = To a very great extent

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 |
| Taxpayer awareness has enabled tax payers file their returns easily |  |  |  |  |  |
| Taxpayer awareness has enlightened the public on the need to pay taxes |  |  |  |  |  |
| Taxpayer awareness programs by KRA have resulted into increased tax base and revenue collection |  |  |  |  |  |
| Taxpayer sensitization has played a vital role in changing the  attitudes of taxpayers. |  |  |  |  |  |
| Workshops are more detailed and provide ample time for the  public to conceptualize ideas |  |  |  |  |  |
| Good record keeping is very important in a business so as to  facilitate correct filing of taxes |  |  |  |  |  |

8. To what extent are the following modes of training used by KRA effective in achieving the

objective of educating the tax payers?

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 |
| Stakeholder sensitization |  |  |  |  |  |
| Print media taxpayer education |  |  |  |  |  |
| Electronic taxpayer education |  |  |  |  |  |

**Tax Compliance**

1. Please rate the following statements in regards to Tax Compliance.

Rate on a scale of 1-5 where;

1= Strongly agree

2= Agree

3= Neutral

4=Disagree

5=Strongly disagree

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 |
| Tax laws should be respected |  |  |  |  |  |
| Tax revenues are not spent on public services as should be |  |  |  |  |  |
| ax rates are too high |  |  |  |  |  |
| There are dishonest tax collectors |  |  |  |  |  |
| It is unfair to pay taxes |  |  |  |  |  |