

**FACTORS AFFECTING TAXATION OF THE INFORMAL SECTOR IN KENYA**

**CASE OF ELDORET TOWN**

**By**

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AND TECHNOLOGY**

**OCTOBER 2020**

**DECLARATION**

This research project is my original work and has not been presented to any other examination body. No part of this research should be produced without my consent or that of Kenya School of Revenue Administration.

.....

**Date.....**

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**HDB336-C016-0845/2019**

This research project has been submitted for examination with my approval as the university supervisor

.....

**Date.....**

**Dr. Marion Nekesa**

## **DEDICATION**

I wish to dedicate this project to my family for the support they accorded me which made it easier for me to accomplish the studies.

## **ACKNOWLEDGEMENT**

This research paper would not have been possible without the guidance and tireless support from my supervisor Dr. Marion Nekesa. I am very grateful for the time she spent reading and providing me with feedback and assisting me at every stage of this research. I have benefitted greatly from her expertise, immense knowledge of the subject and mentorship. God bless you.

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## **ABBREVIATIONS AND ACRONYMS**

<b>GDP</b>	Gross Domestic Product
<b>KRA</b>	Kenya Revenue Authority
<b>SME</b>	Small & Medium Enterprises
<b>TCC</b>	Tax Compliance Certificate
<b>TOT</b>	Turnover Tax

Financial literacy reflects individuals' ability to understand financial concepts, financial products and services and enables them to control their personal financial resources (Bahovec et al, 2014)

Tax literacy may be defined as the knowledge which an individual should possess in order to manage the issues concerning personal taxation effectively (Bhushan, Medury, 2013).

## ABSTRACT

This study aims to determine the effect of tax incentives on rental revenue collection in Kenya. The study was guided by the following specific objectives: - to determine the effect of financial literacy level on taxation of informal sector in Kenya, to analyze the effect of tax literacy on taxation in Kenya and find out the effect of taxpayers' attitude on taxation in Kenya. The study will adopt a descriptive Research design. The target population was drawn from 1200 registered small and medium taxpayers and a sample of 120. The study used primary data collected through closed structured questionnaires to meet the objectives of the study. A pre-test on a different sample was conducted to give a Cronbach's alpha greater than 0.7 for all the variables as a rule of thumb. Data analysis was used through descriptive statistics and inferential statistics by use of using Standard statistical techniques including Pearson correlation coefficient and regression analysis employed in the analysis. All the analysis was conducted using the statistical package for social sciences (SPSS Version.24). Analysis of variance (ANOVA) was used to establish if there is a statistical significance between the observed and expected values with the Pearson Chi square giving the degree significance of the relations, hence establishing the hypotheses. In multivariate analysis, multiple regression analysis model was used to determine the type of the relationship that existed between independent and dependent variables. The coefficient for tax literacy is 0.354 so for every unit increase in level of awareness, we expect 0.35 point increase in taxation of informal sector. For taxpayer attitude is represented by a coefficient of 0.246, meaning for every decrease in taxpayer attitude a 0.24-unit decrease in taxation of informal sector is predicted holding all other variables constant the study recommends that Kenya Revenue Authority being the Tax Administration Authority should employ more technical staff and train them in interpreting the law which shall ensure that proper sensitization of this is done to the tax payers. Policy makers should introduce stringent measures with respect to tax penalties and fines on the informal sector

## **CHAPTER ONE**

### **INTRODUCTION**

#### **1.1 Background of the Study**

The informal sector can have some serious negative impacts on developing countries' tax revenue potential and, consequently affecting their ability to raise domestic revenues for financing sustainable development. However, as outlined in Joshi et al. (2014), efforts to improve informal sector taxation must not necessarily lead to substantial increases in governmental revenues in case that the associated costs of tax collection are high. In this sense, taxation of the informal sector as a means of revenue mobilization is inherently a matter of costs and benefits. The large number of potential taxpayers in the informal sector, and the difficulties of monitoring "hidden" entrepreneurs and small-scale firms, can give rise to serious revenue collection costs for tax authorities in developing countries. At the same time, the revenue potential of taxpayers in the informal sector is fairly modest, as their taxable incomes are usually quite low (Joshi et al., 2014). Informal sector activities are often located in rural areas or come from self-employed sellers living near the subsistence level (La Porta & Shleifer, 2014). Consequently, given the low "value for money" in revenue terms, tax administrations have often given little priority to the taxation of the informal sector firms (Fjeldstad, 2014), which can also be related to equity consideration, namely that taxation falls more strongly on the shoulders of low income informal firms (Joshi et al., 2014). From a conceptual perspective, the direct revenue impacts of informal sector taxation and the associated costs might also be highly difficult to assess as data availability and quality is poor for many developing countries. Having this in mind, Joshi et al. (2014) point out that arguments in favor of an expanded informal sector taxation often rely more strongly on the indirect benefits of the latter.

### **1.1.1 Global Perspective**

Taxation of the informal sector allows informal firms to hold the state accountable for the use their payments, and can thus contribute to an emerging sense of democratic participation and ownership over governmental actions. The state, in turn, has an incentive to demonstrate accountability and responsiveness to taxpayers in order to foster voluntary tax compliance based on a social norm of paying taxes (Joshi et al., 2014). As outlined earlier, the informal sector is inherently hard to tax therefore improved voluntary compliance might be a cost-efficient way of raising additional taxes since this method will go hand in hand with sensitizing the taxpayers of the need to register their businesses and the benefits that will attract through to them and the government as well as easing operations in their businesses the comparison is made in relation to pure enforcement through tax authorities. State legitimacy also depends on the existence of strong governmental institutions and state capacities, of which the capacity to tax is a particular important one (Gaspar et al., 2016). In addition, the contractual relationship between taxpayers and the state implies that informal sector taxation might help to strengthen collective action and political participation among business associations in the informal sector (Joshi et al., 2014). As noted by Joshi et al. (2014), although some studies find a positive relationship between informal sector taxation, accountability and collective action, the evidence is limited. The effects described in the literature relate to different channels of good governance and include bargaining between the state and informal business associations, stronger public engagement, as well as higher levels of trust resulting from formalization.

At the same time, Joshi et al. (2014) point out that the success of bargaining between informal associations and the state authorities can be crucially affected by the organisational structure and political power of the former. Informal sector taxation might even emphasize the weaknesses of informal sector associations and lead to a marginalization of certain groups, as well as to a stronger fragmentation of political voice.

The formalization of informal sector activities has received some particular attention in the international development agenda, and taxation is often regarded as a key ingredient (Joshi et al., 2014). In particular, the Addis Ababa Action Agenda outlines that the international

community will need to invest continuing efforts to integrate the informal sector into the formal economy in line with country circumstances” (UN, 2015, p. 11). In the same vein, Target 8.3 of the Sustainable Development Goals (SDGs) stresses the need to encourage the formalization and growth of micro-, small- and medium-sized enterprises in order to promote sustainable and inclusive economic growth. Widespread informal activities are usually regarded to be a persistent phenomenon in developing countries (Besley & Persson, 2014; La Porta & Shleifer, 2014).

Broad-based taxation is a central element in the process of formalization, and can have some strong implications for economic growth (Joshi et al., 2014). A particularly important channel through which growth could be triggered is the increase in firm productivity, which is usually low for informal sector firms in developing countries. Empirical findings suggest that the “productivity gap” between formal and informal firms can be substantial. La Porta & Shleifer (2008), for instance, show for a sample of developing countries that the value-added of informal firms is only 15% when compared to the value-added of formal firms. For some countries, it this ratio can even become as small as 1%-10%. As outlined by La Porta & Shleifer (2014), this lack of productivity is driven by some “generic” elements of informal 6 “Multi Indicators, Multiple Causes” 7 sector firms, which include their relatively small size, inefficiency, as well as the observation that they are often run by poorly educated entrepreneurs. In addition, small informal firms also have fewer opportunities to benefit from economies of scale and exporting opportunities, given that they operate outside of the legal system (Besley & Persson, 2014). For formal firms, competition with the informal sector might have some serious consequences for their business operations. This might be particularly true for larger or less poor informal firms competing with formal firms with a similar or lower income (Dube & Casale, 2016). Figure 3 shows that informal practices might be a serious obstacle for business activities of formally registered firms in developing countries. Evidence from the World Bank Enterprise Surveys Data suggests that, on average, 61.3% of formal firms in low-income have to compete with unregistered or informal companies, compared to only 32.0% in OECD countries. Likewise, 33.4% of firms in low-income countries identify informal sector competition as a major obstacle for doing business (compared to 14.2% in OECD

countries). Figure 3: Informal sector competition Source: World Bank Enterprise Surveys Data (2010-2017). In addition, as argued by Singh (2014), the informal sector may limit overall state capacities, which are necessary for the expansion of a more productive formal sector. Other studies have argued that smaller informal firms especially are too inefficient and too different from formal ones to pose a threat on the latter (La Porta & Shleifer, 2014). In addition, while informal firms might be able to reap the benefits of non-taxation, they are at the same time excluded from some other positive effects of formalization therefore opting for the formal economy which dictates compliance with tax laws and obligations, might bring some important benefits for informal sector firms, which can ultimately trigger growth and productivity some among the benefits are:- the access to capital markets, new market opportunities, less exposure to police and municipal officers, and access to training and capacity building (Joshi et al., 2014).

However, as argued by La Porta & Shleifer (2014), other studies draw a quite different picture and suggest that informal firms rarely become formal even when barriers for entry are reduced, and that they are too inefficient to survive in formal markets. In addition, they claim that informal firms are too different from formal ones (e.g. in terms of the products offered) to pose a threat on the latter. According to La Porta & Shleifer (2014), these observations are supportive of a “dual view” of informality, namely that informal and formal firms are largely segregated. In summary, the effects of informal sector taxation on growth are complex, and the results of the studies cited above are somehow inconclusive. However, as Joshi et al. (2014) note, there is a growing body of literature that empirically supports the assumption that formalization (including through taxation) can have significant positive impacts in terms of profitability, investments, and growth. Yet, there remains uncertainty whether these effects also apply to small or micro informal firms, and which channels are the most important ones.

The specific characteristics of the informal sector render it challenging to directly apply formal sector tax policies. In some instances, the informal sector is instead covered indirectly through standard tax regimes, as in the case of the Value Added Tax (VAT). Unregistered informal sector firms have an incentive to enter the tax system in order to

claim VAT refunds in case that they are a dealing with formal firms. Another indirect approach is the reliance of withholding taxes on transactions with informal firms, which are collected by formal firms or the government. Again, withholding taxes provides an incentive to become formal because withheld payments can be credited against formal tax liabilities (Joshi et al., 2014). In addition, developing countries increasingly rely on simplified taxes for assessing the informal sector that often take the form of so-called presumptive taxes. Under a presumptive tax regime, tax liabilities are estimated on the basis of simple indicators of business performance (such as turnover) or certain “visible” firm characteristics (such as transport capacities), and taxes are often paid on a lump-sum basis. The rationale behind presumptive taxes is to collect some additional tax revenues with a reasonable amount of administrative and tax compliance costs (Dube & Casale, 2016), which somehow mirrors the economic “cost-benefit-analysis” described earlier. In a recent publication, Dube & Casale (2016) provide some evidence on presumptive taxation in four countries in Sub-Saharan Africa (Ghana, Tanzania, Zambia and Zimbabwe). Although the presumptive taxes vary greatly with respect to their design, coverage and implementation, there are some common observations regarding their effectiveness and efficiency, which turns out to be generally limited. Some tax administrations found it difficult to implement the presumptive taxes due to severe capacity limitations, in particular with respect to adequate manpower. Administrative constraints also sometimes lead to a lack of monitoring and enforcement, so that taxpayers failed to pay. The lack of compliance was also stressed by the fact that taxpayers were not informed about the taxes, and that they questioned the legitimacy of tax collectors.

Taxation, be it on the national or subnational level, has the primary objective of raising revenues for financing public goods and services and for providing quality state institutions. Depending on their degree of tax autonomy and other factors, SNGs in developing countries are sometimes more and sometimes less successful in raising own source taxes. A general impression, though, is that SNGs in low-income countries significantly suffer from financial resources in general and own-source or shared tax revenues in particular (see Figures 4 and 5). In general, from a political economy perspective, central and local government can be thought to compete over the same taxable

incomes. The central government might thus be reluctant to give up own revenue sources by assigning some collection rights to SNGs (Bird, 2010; UN-HABITAT, 2015). Transfers and subsidies from the central government, which on average represent more than 60% of SNGs revenues in low-income countries, might also crowd out efforts for improved own local taxation. However, SNGs might be in some instances able to reach out to some parts of the revenue base that would be otherwise left untaxed by the central government, either because the latter is not willing due to high administrative costs (e.g. taxation of small businesses) or not able due to a lack of monitoring and control (e.g. informal activities). In this sense, SNG revenue authorities might have a comparative advantage in identifying local businesses for the purpose of taxation, as they oversee licensing and regulatory activities, among others. From the perspective of the central government, the successful implementation of local taxes might even lead to a better revenue position in case that own-source taxation reduces the need for central government transfers (Bird, 2010). It has been for instance proposed to shift taxation of the informal sector to local authorities.

### **1.1.2 Kenyan Perspective**

Similarly, in Kenya, the informal sector is quite large, estimated at 34.3% and accounting for 77% of employment statistics. Over 60% of those working in the informal sector are the youth, aged between 18-35 years, and 50% being women (Ouma, 2009). Compared to the other sectors of the economy, the contribution of the SME sector to the country's Gross Domestic Product (GDP) increased from 13.8% in 1993 to over 18% in 1999, (Sessional Paper No. 2 of 2005). Currently, it is estimated that the contribution to the GDP by this sector stands at over 25% (Economic Survey, 2017).

Njeru (2012), argued that “taxing the booming informal sector presents the hope of generating extra income to make up for the deficit in tax revenue, yet this is not without its problems”. Joshi and Ayee (2009) opined that “how to tax the informal sector remains a pressing question”. Njeru (2012) further opined that “there seems to be a consensus that African governments and their tax authorities would have to work around the clock to bring the informal sector into tax bracket, as efforts by governments to widen the tax base will greatly increase revenue leading to a reduction in the reliance on donor funding and in incidences where governments are forced to increase taxes on basic commodities. Despite

the low compliance by this sector, the government is still determined to expand the tax net (base) to the informal sector since ignoring the sector's activities will dampen compliance morale of the few already complying and by extension lead to not just further drop in tax revenue but increased rise on generalized non-compliance among tax payers in the both sectors.

Indeed, the large numbers of SMEs, their high turnover rates and their sheer diversity present challenges to all administrations. For SMEs, key considerations are to minimize administrative costs while ensuring compliance, including considering the drivers and impacts of operating in the informal economy.

Nada and Jack (2009) examined tax reforms in Kenya particularly in regard to policy and administrative issues. The study acknowledges that tax system in Kenya has undergone perpetual reform over the past two decades. For instance, from the policy perspective there has been rationalization and simplification of rate schedules, a new value-added tax introduced, and external tariffs brought on board in order to tally with those of East African countries. It is observed that it is imperative to have continued reform of both policy instruments and both administrative and enforcement capacity of the tax system. The Government introduced Turnover Tax (TOT) regime which came into effect as from 1<sup>st</sup> January 2007. This was meant to bring into tax bracket resident person whose income from business is accrued in or derived from Kenya, and does not exceed five million shillings during any year of income.

Due to the myriad challenges experienced, the authority has continuously failed to meet the target. In FY 2016/2017 only 102M was collected against a target of 425M with a performance of 24%. The target for FY 2017/2018 was reduced to 127M.

KRA introduced several reforms in order to enhance compliance in the informal sector. This includes collaborating with County Governments to impose possession of a valid Tax Compliance Certificate (TCC) when renewing single business permits and when applying for or renewing liquor licenses. This ensures that all taxpayers who require the document must be up to date for them to get the vital document from KRA.

Kenya relied on unified tax policies and an administrative system jointly administered by the initial three members of the EAC. This was a legacy of British colonial administration that all the three countries inherited at independence. At that point, the government's three main sources of tax revenue were: income tax; customs and excise duties; and Inland Revenue. Changes in both policies and administration were collaboratively determined and minimal until early 1970s. Following a decision to assign responsibility for income tax to each EAC member state, Kenya adopted the community legislation and enacted the Income Tax Act of 1973 (A.D.B, 2010) Thereafter, three distinct phases of major initiatives in tax policy reforms can be discerned for Kenya. Initial efforts at widening the tax base after independence, the first major change to the tax system, was the introduction of a consumption tax - the sales tax in 1973. The impetus for this change derived from adverse effects on customs duty revenue receipts brought about by restrictions on imports associated with an import substitution industrialization policy and seal leakage loopholes (Moyi and Ronge, 2006). With respect to income taxes, government reduced the top marginal rates for: personal income tax (PIT) from 65% in 1986/87 to 45% in 1993 to 35% in 1995/96 – by 1999/00 the top rate was 30%; and corporate income tax from 45% in 1987/88 to 30% in 1999/00 (ADB, 2010). Government launched the VAT in 1990 to increase revenue through the expansion of the tax base. Tax policies introduced during the third phase: 2003/04 to 2008/09 Key changes to tax policy made by the NARC government (2003-2008) and coalition government (2008-2009) has so far evolved around ensuring equity, further widening the tax base, promoting increased investment and reducing the tax compliance burden.

To promote equity GoK widened income tax bands by 5% in 2004/05. Tax bands had remained unchanged since 2002. In the same year, GoK also increased personal relief by 10%. From 16 June 2006, GoK increased the threshold turnover for VAT from KShs 3 million p.a. to KShs 5 million p.a. with a view to reducing the compliance burden for three quarters of registered taxpayers who either file nil returns, or whose turnover is not substantial (ADB, 2010).

## **1.2 Statement of the Problem**

The large number of potential taxpayers in the informal sector, and the difficulties of monitoring “hidden” entrepreneurs and small-scale firms, can give rise to serious revenue collection costs for tax authorities in developing countries. At the same time, the revenue potential of taxpayers in the informal sector is fairly modest, as their taxable incomes are usually quite low. According to a World Bank study in year 2006, Kenya’s informal sector constituted 98 percent of all businesses in the country, absorbed annually up to 50 per cent of new employment seekers and had an employment growth rate of 12-14 percent. In the endeavor to realize this goal, KRA faces several problems when dealing with the informal sector. Some of these problems include financial literacy level of the taxpayers, lack of tax information and taxpayer’s attitude. Fischer tax compliance model provides a framework for understanding the influence of socio-economic and psychological components on taxpayer’s compliance decision. AS theory holds that the government deters tax evasion through a sanction arrangement and audits.

A tax payer will decide to violate the fiscal laws and evade his or her tax obligations when he or she perceives that the cost of evading tax is too low, believing he or she does that he or she is unlikely to be detected or audited. The SMEs are prone to tax evasion as they face difficulties in complying with tax laws. They are expected to comply with strict deadlines, keep proper books of accounts. This kind of environment leads to tax evasion.

In Kenya, Memba, Gakure and Karanja (2012) posit that the informal sector is not only a provider of goods and services but also a driver in promoting competition, innovation and enhancing the enterprise culture which is necessary for private sector development and industrialization. They further argue that it is growingly economically important and should effectively respond to challenges of creating productive and sustainable employment opportunities, promoting economic growth and poverty eradication in the country. On the contrary to expectation, Waweru (2007) found collecting turnover tax from these businesses both a challenge and coupled with dwindling revenues. In the endeavor to realize this goal, KRA faces several problems when dealing with the informal sector. Some of these problems include lack of information on taxation matters, lack of equipment like computers, literacy level of the businessmen and accessibility by the taxmen to the

businessmen. This study therefore sought to investigate the factors affecting taxation of informal sector; a case study of Eldoret town.

### **1.3 Objectives of the Study**

The general objective of the study is to investigate the factors affecting taxation of the informal sector in Kenya, a case study of Eldoret town.

#### **1.3.1 Specific Objectives**

The specific objectives of this study are as follows:

- i. To determine the effect of Financial literacy level on taxation of the informal sector in Eldoret town.
- ii. To establish the effect of tax literacy on taxation of the informal sector in Eldoret town.
- iii. To find out the Taxpayers' attitude on taxation of the informal sector in Eldoret town.

### **1.4 Research Questions**

- i. What is the effect of financial literacy level on taxation of the informal sector in Eldoret town?
- ii. What is the effect of tax literacy on taxation of the informal sector within Eldoret town?
- iii. How does the Taxpayers' attitude affect the taxation of the informal sector within Eldoret town?

### **1.5 Significance of the Study**

#### **1.5.1 KRA Management**

The study will help the management of Kenya Revenue Authority to identify the factors which affect the taxation of the informal sector and help strengthen the identified weak areas to achieve their goals and remain to be a leading organization with which other organizations can benchmark against.

### **1.5.2 Policy Makers**

The study will inform the management and help the institutions like the National Treasury to fast track the necessary measures and policies required.

### **1.5.3 SMEs**

The research will be useful to the business community and organization's management teams for purposes of knowing the tax compliance environmental factors and how the conditions can be improved or dealt with. This will also lead to registration of many Small and Medium Enterprises therefore improving compliance of those particular businesses as well as opening opportunities like tendering with government and parastatals on different projects.

### **1.5.4 Future researchers**

The information gathered will help other researchers to advance their understanding on the findings that have been made and improve on them. It will also act as a basis for further references and a source of literature review.

## **1.6 Scope of the Study**

The study was conducted at Eldoret town located in Uasin Gishu County on Kenya. The study independent variables are; financial literacy level, Lack of tax information and Taxpayers attitude. The dependent variable is Taxation. The study collected data through questionnaire for registered taxpayers from informal sectors (SMS) at Eldoret town.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

This chapter presents a review of literature on taxation in general and turnover tax. It first discusses three theories that provide the theoretical background of this study. The second part discusses the factors affecting taxation of the informal sector in Kenya ending up with a conceptual framework explaining the relationship between the challenges. The final part of the literature review discusses other studies conducted that are relevant to this study.

#### **2.2 Theoretical Framework**

This contains a discussion of the relevant theories on this study and how they relate to the variables contained in the study.

##### **2.2.1 Allingham and Sandmo Theory**

According to (Sandmo, 1972) The AS theory holds that the government deters tax evasion through a sanction arrangement and audits. A tax payer will decide to violate the fiscal laws and evade his or her tax obligations when he or she perceives that the cost of evading tax is too low, believing he or she does that he or she is unlikely to be detected or audited. Tax payers would also evade tax when he or she perceives the cost of compliance is high. Tax systems and procedures that are involving and cumbersome tend to encourage tax evasion. Tax payers who feel that tax rate is high and punitive will evade tax.

There is a negative correlation between tax evasion, the probability of detection, the degree of punishment and high transactional costs associated with tax laws. Income tax evasion was pioneered by Allingham and Sandmo (1972), where a rational and a moral taxpayer maximizes expected utility, which solely depends on income. When caught, the agent must pay penalties, imposed on the amount of evaded income. A key comparative static result is that when the tax rate goes up, competing income and substitution effects

might lead to more or less tax compliance. The substitution effect encourages evasion since the marginal benefit of cheating goes up with the tax rate. On the contrary, the income effect tends to suppress evasion taking into consideration that a higher tax rate makes the taxpayer with decreasing absolute risk aversion feel worse-off, and thus decrease risk-taking. Therefore, the net effect is ambiguous.

However, Shlomo Yitzhaki (2002) showed that when the penalty is imposed on the amount of evaded taxes, as it is under most current tax laws, the substitution effect vanishes. At the original optimum, the penalty paid on concealed income increases proportionally with the tax rate, and hence, there is no substitution effect. The remaining income effect is responsible for inducing the taxpayer to cheat less. Therefore, the net effect is better compliance. Yitzhaki's (2002) result is perhaps the single most important finding in the early tax evasion literature, having spurred a lot of remarkable extensions. The SMEs are prone to tax evasion due to the challenges they face for instance complying with strict deadlines, keeping proper books of accounts as a way of keeping at par with tax laws, it is due to this type environment which they find unfavorable opting to evade tax.

### **2.2.2 Agency Theory**

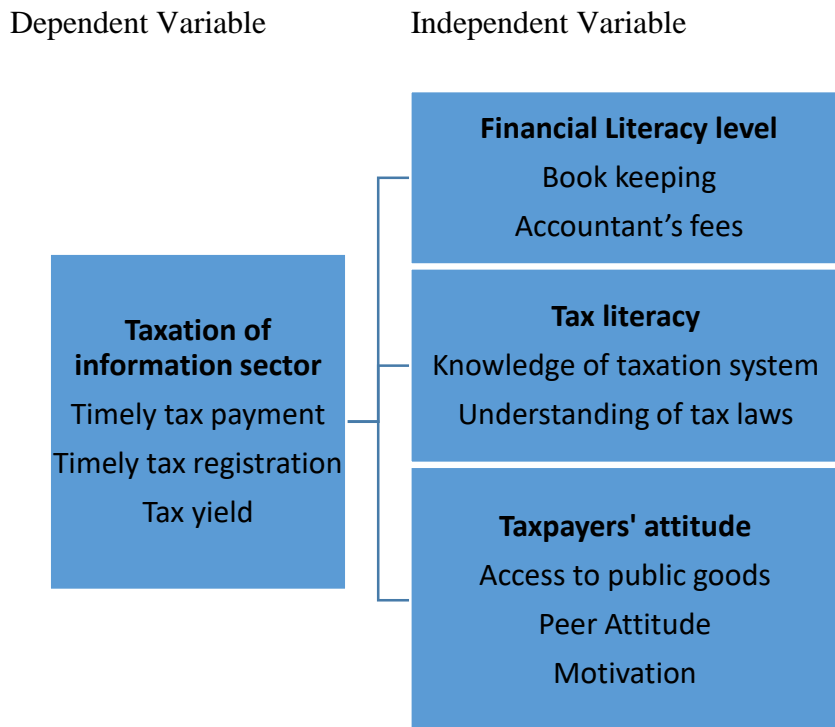
In general, agency theory suggests that policy-makers and tax administrators should be wary about any assumption that uncompelled agents or vendors will represent the state and collect the tax. This does not mean firms will never comply with a request to contribute to society. In fact there is substantial evidence of corporate social responsibility (Tucker and Henkel, 1992). Finding behavior of people who contribute to the good of an organization or association on a purely voluntary basis is common. Religious organizations, voluntary fire departments, and boys and girls clubs are among many examples. There are also situations in which groups participate in programs that benefit the community, even though they are only partially compensated for their activities. In agency models, the government (i.e. the principal) pre-commits to an audit strategy in order to encourage maximum compliance by taxpayers. For instance, Reinganum and Wilde (1985) model the taxpayer as a risk-neutral agent of the government who has private knowledge of his own income. The government, whose goal is to maximize tax revenues net of audit costs, cannot observe

actual income without costly investigation. Reinganum and Wilde use this setting to compare a random audit strategy of the type implied in early models with a cut-off audit strategy in which an agent triggers an audit by reporting below a certain level of income. They show that the use of a cut-off strategy weakly dominates a random audit strategy because it will induce truthful reporting at the least cost. In addition to the desirable effect on compliance, they argue that such a strategy would enhance horizontal equity ex- post over random auditing since those with equal incomes will be audited with equal certainty.

### 2.3 Conceptual Framework

The study sought to investigate challenges facing taxation of the informal sector in Kenya. The independent variables will include financial literacy, lack of tax information and taxpayer’s attitude while dependent variable will be taxation

**Figure 2.1 Conceptual Framework**



Source; Author (2020)

## **Figure 2.1 Conceptual Framework**

**Source; Author (2020)**

### **2.4 Empirical Literature**

The formalization of informal sector activities has received some particular attention in the international development agenda, and taxation is often regarded as a key ingredient (Joshi et.,al., 2014). In particular, the Addis Ababa Action Agenda outlines that the international community will need to invest continuing efforts to integrate the informal sector into the formal economy in line with country circumstances” (UN, 2015, p. 11).

In the same vein, Target 8.3 of the Sustainable Development Goals (SDGs) stresses the need to encourage the formalization and growth of micro-, small- and medium-sized enterprises in order to promote sustainable and inclusive economic growth. Widespread informal activities are usually regarded to be a persistent phenomenon in developing countries (Besley & Persson, 2014; La Porta & Shleifer, 2014).

It has been suggested, for example, that some of the largest and fastest growing business sectors in African countries, such as the retail and construction sector, are dominated by informal firms and entrepreneurs (Benjamin et al., 2014).According to the World Bank, the informal sector accounts for the 40% of gross national products (GDP) of low-income countries (Farrell 2004). Despite their significant contributions to the economies of developing countries, they are the least taxed (Patrick Sownali 2011).

The term informal sector originally proposed by Hart (2009), was initially used to refer to employment outside of formal labor markets. The idea was to distinguish businesses on their degree of rationalization, or embodiment of impersonal principles of social organization (Hart 2005). Some studies estimate that informal businesses account for 35-50% of GDP in many developing countries. In general, from a political economy perspective, central and local government can be thought to compete over the same taxable incomes.

The central government might thus be reluctant to give up own revenue sources by assigning some collection rights to SNGs (Bird, 2010; UN-HABITAT, 2015). Transfers

and subsidies from the central government, which on average represent more than 60% of SNGs revenues in low-income countries, might also crowd out efforts for improved own local taxation.

However, SNGs might be in some instances able to reach out to some parts of the revenue base that would be otherwise left untaxed by the central government, either because the latter is not willing due to high administrative costs (e.g. taxation of small businesses) or not able due to a lack of monitoring and control (e.g. informal activities). In this sense, SNG revenue authorities might have a comparative advantage in identifying local businesses for the purpose of taxation, as they oversee licensing and regulatory activities, among others. From the perspective of the central government, the successful implementation of local taxes might even lead to a better revenue position in case that own-source taxation reduces the need for central government transfers (Bird, 2010).

Yankon (1992) stated that the operators of this sector mostly lack adequate financial resources to import more advanced technology so the sector heavily relies on labor-intensive mode; for its production. Available literature indicates that there is a strong relationship between the informal sector and the inability of the Government to collect the requisite taxes. From the informal sector's point of view, tax evasion is driven generally by a perception that the tax burden is too high.

The formalisation of informal sector activities has received some particular attention in the international development agenda, and taxation is often regarded as a key ingredient (Joshi et al., 2014).

In particular, the Addis Ababa Action Agenda outlines that the international community will need to invest continuing efforts to integrate the informal sector into the formal economy in line with country circumstances" (UN, 2015, p. 11). In the same vein, Target 8.3 of the Sustainable Development Goals (SDGs) stresses the need to encourage the formalization and growth of micro-, small- and medium-sized enterprises in order to promote sustainable and inclusive economic growth. Widespread informal activities are usually regarded to be a persistent phenomenon in developing countries (Besley & Persson, 2014; La Porta & Shleifer, 2014). It has been suggested, for example, that some of the largest and fastest growing business sectors in African countries, such as the retail and construction sector, are dominated by informal firms and entrepreneurs (Benjamin et al.,

2014). Recent data from Schneider & Buehn (2018) displayed in Figures 1 and 2 provide an overview of the size of the informal economy for different country income groups and world regions:

As noted in the introduction, increasing attention to the taxation of the informal economy is grounded in its potential importance to revenue, growth and governance. However, it is important to interrogate the basis for this enthusiasm carefully. Most notably, the direct revenue benefits of taxing the informal sector are likely to be relatively modest, and the implications for vertical equity potentially adverse. As such, much of the argument for taxation of the informal sector is grounded in potentially more indirect revenue benefits, the prospects of accelerated growth and the potential for governance gains. These effects are less well established empirically. On balance, they nonetheless present a convincing argument for increased efforts to expand taxation of the informal economy, though there is a need for sensitivity to potential costs and greater research into predicted benefits.

#### **2.4.1 Financial Literacy Level**

Atkinson and Messy (2005) define financial literacy as the combination of consumers'/investors' understanding of financial products and concepts and their ability and confidence to appreciate financial risks and opportunities, to make informed choices, to know where to go for help and take other effective actions to improve their financial well-being (Siekei, Wagoki & Kalio, 2013). Problems like tax complexity; low tax morale, low tax compliance and shadow economy may all be reduced increasing the level of taxpayers' (individuals') financial literacy. According to the OECD (2013) large informal economy in most developing countries presents a key reason for engaging in taxpayers' education. Engaging and educating individuals could help them overcome tax system complexities and strengthen their feelings of responsibility and identity to the state. Also, increased revenues could impact the improvement of the quality of public goods and services. Moreover, OECD (2013) in their publication states that taxpayer education campaigns can be an efficient and effective way of building trust and increasing public engagement. Developing and transition countries continue to face the challenge of creating a society of well informed and willing taxpayers. This kind of state of mind, in economies where continuous inefficiencies, inequalities, corruption and lack of transparency are

everyday problems, presents a challenging venture difficult to achieve. It is well established that about sixty percent of the informal sector entrepreneurs are unlettered. Associated with this problem (i.e. illiteracy) is the problem of filing out of income returns, preparation of accounts and in general the lack of voluntary compliance. Generally, income return forms are complex to complete and hence calls for one to be fairly educated to enable one peruse the return and complete it appropriately. Again, the income return form does not come in the local languages that the illiterates can easily understand, hence the non-declaration of income form of tax evasion (Otioku, 1988)

#### **2.4.2 Tax literacy**

Tax literacy is a rather new and still developing concept which is highly related to financial literacy. Financial literacy presents a very broad concept which is usually defined as basic financial knowledge and financial skills needed to make informed financial choices. Financial literacy reflects individuals' ability to understand financial concepts, financial products and services and enables them to control their personal financial resources (Bahovec et al, 2014). Worthington (2006) argues that although policy makers and researchers have attempted to define financial literacy, it can mean different things to different people. It might be a broad concept involving an understanding of economics, or alternatively a narrower concept focused mainly on basic money management. International Adult Literacy Survey (IALS) defines literacy as "the ability to understand and employ printed information in daily activities, at home, at work and in the community - to achieve one's goals, and to develop one's knowledge and potential." Similarly, UNESCO (2012) considers that "literacy is the ability to identify, understand, interpret, create, communicate and compute, using printed and written materials associated with varying contexts." Financial literacy itself includes several different components. However, very little of research, if any, has focused on what elements should in fact, be measured as components of financial literacy. It is argued that taxation should be considered as one of the important components since it has a strong potential to influence on individual's or household's financial wellbeing.

The ability to meet tax liabilities on time, prepare returns accurately and claim all available entitlements would certainly impact on a person's overall financial position). According to Waris and Murangwa (2012) tax literacy is intended to firstly, help provide information about taxes, secondly, not to support any particular type or amount of taxes, but to simply explain taxes within a domestic system as well as a regional and international system, and how it impacts on those being informed. Furthermore, tax literacy can be defined as the ability to fill in the tax form and calculate tax liabilities independently (Bardai, 1992; Razman and Ariffin, 2000). Tax literacy may be defined as the knowledge which an individual should possess in order to manage the issues concerning personal taxation effectively (Bhushan, Medury, 2013). According to study made by Madi et al (2010) a person can be considered functionally literate if he/she can read, write and calculate for his/her own self. By analogy tax literacy may be defined as follows: a person is considered functionally tax literate if he/she can independently read and understand tax reports, can engage independently in various tax calculations and is aware of possible tax risks in its financial environment.

In 1992, Kenya adopted the self-assessment system of paying taxes. The responsibility of Declaring and paying the correct taxes is vested on the tax payer. A tax payer is required by law to file a self-assessment return by the end of the six month after year end. After filing the returns, Kenya Revenue Authority (KRA) reviews them and if it has reason to believe that a tax payer did not disclose the correct taxes, it is empowered under the law to carry out an in-depth tax audit to verify the information disclosed by the tax payer. This is where problems start! The tax payer then goes through the rigorous process that is both time consuming and costly for errors or omissions that would have been avoided had advance tax rulings been in place (Muiru, 2012)

Further, businesses contemplating significant transactions are often faced with the problem of not knowing, with some degree of certainty, what the tax outcome of those transactions would be. This uncertainty could sometimes mean a deal is aborted because an adverse tax treatment could make it commercially non-viable. The situation is further complicated by the complexity of our tax laws and the fact that they are subject to change from time to time.

### **2.4.3 Taxpayers attitude**

Tax payers attitude maybe influenced by many factors which eventually influence taxpayer's behavior (Ambrecht, 1998). Some of these factors which influence tax compliance behavior and tax compliance behavior are many and are different from one country to another and from one individual to another. They include taxpayers perception of the tax system and revenue authority; peer attitude; tax payers understanding of tax system and tax laws; Motivation such as rewards and penalties; Cost of compliance; enforcement efforts such as audit; probability of detection; difference across culture; Equity of the tax systems and demographic factors such as sex, age and size of income.

There is a very strong relationship between the taxpayers' attitudes and tax compliance in Kenya, in that taxpayer's attitudes encourages tax compliance in and all that influence the taxpayers' attitudes, equally affect the taxpayers' compliance with the tax requirements. In a research conducted in Kenya (Wanjohi, 2010) the following conclusions were arrived at: First, most taxpayers view the Kenyan tax system as unfair. This was because most respondents differed that they are paying a fair share of tax; that their neighbors or friends, the tax laws are not easy to understand such as calculation of tax filing and paying dates. Secondly, some of the factors for tax non-compliance were found to be: the inability to understand tax laws, for example, rates of tax, filing and paying dates, a feeling that they are not paying a fair share of tax, negative peer attitude, and a belief that their neighbors are not reporting and paying tax honestly, and non-rewarding taxpayers.

The attitude issues from the various studies rotate around the tax fairness; improper use of revenue collected by government and pure intent to evade payment of tax for the collective good vis-à-vis the individual interest. Attitudes represent the positive and negative evaluations that an individual holds of objects. It is assumed that attitudes encourage individuals to act according to them. Thus, a taxpayer with positive attitudes towards tax evasion is expected to be less compliant than a taxpayer with negative attitudes. Attitudes towards tax evasion are often found to be quite positive (Kirchler, 2001). Many studies on tax evasion found significant, but weak relationships between attitudes and self-reported tax evasion (Trivedi, 2005) . A model of tax evasion behavior developed by Weigel, Hessing considers social and psychological conditions, including attitudes and moral beliefs about tax evasion's propriety, as antecedents of tax compliance.

Data collected from fined tax evaders and honest taxpayers showed that attitudes explain in part self-reported tax evasion, but are insignificant predictors of actual behavior.

However, the correlations between self-reported tax non-compliance and attitudes are significant but fairly weak. These findings suggest a rather complicated relationship between tax evasion and attitudes, nevertheless we can be confident in our general prediction that if tax attitudes become worse, tax evasion will increase (Lewis, 2005). The attitudes are important for both the power and the trust dimension. On the one hand, favorable attitudes will contribute to trust in authorities and consequently will enhance voluntary tax compliance. On the other hand, attitudes towards the authorities will be relevant for the interpretation of the use of power as benevolent or malicious. Tax attitudes in general also depend on the perceived use of the money collected and therefore are connected to knowledge (Kirchler, 2001)

#### **2.4.4 Taxation of informal sector**

Tax plays an important role in the growth of Small and Medium Enterprises (SMEs) in low income countries like Kenya. The role of SMEs is critical in pushing the socio-economic development agenda of the country further. Therefore, alignment of the tax system to the environment specific SME growth needs can be considered an important agenda for the policymakers. (Mika Mungaya, IJMBS Vol. 2, Issue 3, July - Sept 2012).

In the 1970s, SMEs in Kenya were perceived as marginal to mainstream activity. They were typically cast as habitual avoiders and evaders however the 1980s the service sector took off and represented a higher and growing proportion of GDP in the country. SMEs are an important force for economic development and industrialization in poor countries. It is increasingly recognized that these enterprises contribute substantially to job creation, economic growth and poverty alleviation. The 2005 World Development Report suggests that creating “sustainable jobs and opportunities for micro entrepreneurs are the key pathways out of poverty for poor people” (World Bank, 2004). Like any other developing countries, Kenya has taken a number of measures to promote the growth of private sector and Small and Medium Enterprises (SMEs). SMEs were estimated to account for a significant share of Gross Domestic Product (GDP).

The government formulates and implements various policies aimed at increasing job opportunities, development of infrastructure as well as income generation through the creation of new SMEs and improving the performance and competitiveness of existing one, the revenue collected from taxes represents the major funding source for governmental expenditures (Baurer, 2005). If the tax structure is not adequately designed to the specific environmental conditions, it may create a greater burden to the tax-paying organizations and eventually affecting the final consumer due to the shifter ability of tax. SMEs in developing countries often face difficulties when dealing with tax matters. It would be rare indeed not to hear complaints about the complexity and or ambiguity of the tax laws, high tax rates, and the lack of an integrated fiscal strategy that takes social taxes, and local taxes and fees into account when determining the overall tax burden placed on the business community (Baurer, 2005).

This implies that as a policy maker and regulator, Government must consider the factors that could affect the competitiveness of the enterprises. Assessing the impact of tax systems on SMEs is not simply a matter of looking at tax rates.

Tax systems play an important role in encouraging growth, investment and innovation and facilitating international trade and mobility. For SMEs key considerations are to minimize administrative burden while ensuring compliance, including considering the drivers and impacts of operating in the informal economy.

Kolstad, (2006) indicated that taxes are perceived to be a major problem for both young and old firms. Therefore, taxation has showing a way towards impacting small and medium enterprise. The GoK has attempted to mobilize revenue by bringing more SMEs to the tax bracket by introducing Turnover tax (TOT). There are four broad categories of obligations identified as Registration in the system, Timely filling or lodging of the required information, reporting of complete and accurate information and payment of taxes in time. The definitions of SMEs differ from country to country, region to region and there is no universal definition. Small and Medium Enterprises (SMEs) play an important economic role in many countries. In Kenya, for example the SME sector contributed over 50 percent of new jobs created in 2005 but despite their significance, most SMEs evade tax. Nevertheless, the factors that attribute to the tax evasion among SMEs are not well understood. Hostility towards tax compliance dates back to history of taxation. Taxes are

considered a problem by everyone, not surprising, taxation problem date back to the earliest recorded history (World Tax Organisation, April 7 1999) Kenya is ranked among low income countries and low compliance countries and is further faced with the difficult task of ensuring efficient and effective tax administration.

The small sizes of the businesses make it easier for them to remain outside the taxation bracket. Mistrust and weak structural dialogue between informal sector and government is another factor that hinders taxing of the informal sector. There is a general mistrust between tax agents and taxpayers, with agents perceiving the SME as tax evaders, unwilling and unable to pay their taxes. The operators too are wary of government agencies' high-handedness in collection of taxes.

There is lack of structured dialogue between the SME and the government as well as other law enforcing authorities. This has led to mistrust and prevents the sector from engaging constructively with the government in reform processes (Programme Issue No. 29 September 2012 ) Other bottlenecks according to a publication of the IEA budget information program include the lack of opportunity to grow and adapt good culture of corporate governance.

## **2.5 Critiques of the study**

Kolstad, (2006) indicated that taxes are perceived to be a major problem for both young and old firms. Therefore, taxation has showing a way towards impacting small and medium enterprise. The GoK has attempted to mobilize revenue by bringing more SMEs to the tax bracket by introducing Turnover tax (TOT). There are four broad categories of obligations identified as Registration in the system, Timely filling or lodging of the required information, reporting of complete and accurate information and payment of taxes in time. The definitions of SMEs differ from country to country, region to region and there is no universal definition. Small and Medium Enterprises (SMEs) play an important economic role in many countries. In Kenya, for example the SME sector contributed over 50 percent of new jobs created in 2005 but despite their significance, most SMEs evade tax. Nevertheless, the factors that attribute to the tax evasion among SMEs are not well understood. Hostility towards tax compliance dates back to history of taxation. Taxes are

considered a problem by everyone, not surprising, taxation problem date back to the earliest recorded history (World Tax Organisation, April 7 1999) Kenya is ranked among low income countries and low compliance countries and is further faced with the difficult task of ensuring efficient and effective tax administration.

According to a research conducted in Kenya by African Research review, the problem of tax noncompliance among business firms constrains the realization of revenue collection targets by Kenya Revenue Authority (K.R.A). The research aimed at investigating the relationship between the size of taxpayer's income, inspection by the tax authorities, use of tax registers and VAT compliance. A sample of 233 registered firms was selected and data collected using self-administered questionnaires to personnel in finance department of the selected firms. The data was analyzed both descriptive and correlation analysis. The study revealed that VAT noncompliance is high among the middle-income business firms and that Inspection of business firms by tax authorities had a slight positive relationship with VAT compliance ( $r = 0.15$ ,  $p < 0.05$ ) The study revealed that effective and regular use of Tax Registers had a significant positive relationship with VAT compliance ( $r = 0.622$ ,  $p < 0.05$ ). The study recommends that stringent compliance measures and close monitoring should be observed among the mid-sized private firms. Tax authorities should also encourage effective use of tax registers through regular but impromptu inspections (Naibei, 2012)

Tax compliance is low among SMEs as a result of several factors such as poor management and internal control practices as many of the enterprises are merely trying to make ends meet. Another contributory factor to low tax compliance among SME's is the informal approach to establishment, operation and dissolution which creates an ease of mobility, consequently making it difficult for the tax administration to keep pace with them. Cash-based economies have also had inadequate accounting records and audit trails in practice. Tax compliance is low among SMEs also because compliance costs for the SMEs are much higher relative to larger business operations that they are competing against. In addition, small businesses have limited resources and technical capacity. Often, the priority of a tax administration is to focus on large taxpayers because of the high delinquency rate and low revenue yields associated with small businesses,

With very little enforcement action. This ultimately encourages non-compliance (Masinde, 2010) from the perspective of tax administration, the major obstacle which hinders government in ensuring that the SME is incorporated in the taxation bracket is the nature of businesses.

The small sizes of the businesses make it easier for them to remain outside the taxation bracket. Mistrust and weak structural dialogue between informal sector and government is another factor that hinders taxing of the informal sector.

There is a general mistrust between tax agents and taxpayers, with agents perceiving the SME as tax evaders, unwilling and unable to pay their taxes. The operators too are wary of government agencies' high-handedness in collection of taxes. There is lack of structured dialogue between the SME and the government as well as other law enforcing authorities. This has led to mistrust and prevents the sector from engaging constructively with the government in reform processes (Programme Issue No. 29 September 2012) other bottlenecks according to a publication of the IEA budget information program include the lack of opportunity to grow and adapt good culture of corporate governance. The informal sector has limited access to training and professional services that would enable them adapt to a sound culture of corporate governance.

Osambo, (2009) Complicated tax systems and numerous processes (licensing etc.) make it difficult and expensive for start-up firms to act in good faith. Policies regarding the informal sector are poorly coordinated and disseminated across five different but related government ministries namely finance, trade, industrialization, local government and labour. This confusion often places sector operators at a disadvantaged position more so in terms of accessing policy updates (Programme Issue No. 29 September 2012)

The current policy reforms regarding business regulations and taxation laws and systems have been formulated with little participation of the informal sector. As a result, many workers and business entrepreneurs in the informal sector feel left out.

## **2.6 Knowledge gap**

From the review of literature, it is clear to date, there has been research exploring factors that influence compliance among SMEs. The main objective of this study was to identify the factors that affecting taxation informal sectors. The research focused on tax rate, tax

information, and tax compliance cost and taxpayers attitude. The research outlined in this paper aims to address the tax gap of non-filing, under reporting and under payment. The specific aim of the research is to gain insight into the factors that taxation in informal sector in Eldoret. It is expected that the findings will help decision makers and particularly K.R.A gain a better understanding of SMEs enabling them to plan and design services more effectively.

## **2.7 Summary**

The informal sector is a crucial sector of most of the developing countries. The liberalization and privatization processes have resulted to the states' failure to be the employer. The private sector is left to take up this role. This indeed is the reason why informal sector should be supported and encouraged. In most cases, the informal sector is viewed as illegal and its activities barred by the government as well as the people working in the formal sector. Urbanization in Kenya on the other end has been occurring in the context of weak economic growth resulting in poor infrastructure, housing and services especially in the slums. Kenya like any other developing country follows an import substituting industrialization strategy for industrial development. This is usually concentrated on large-scale, capital intensive industry, mostly foreign-owned and uses imported technology. There is also duty-free import of capital goods (but micro enterprises are taxed on importation of capital goods), assistance to the large-scale enterprises by the governments to compete with the small scale enterprises (micro Enterprises), subsidized interest rates and access to finances, and direct support measures all by the government. However, there is ambiguity of operation associated with the informal sector especially in Kenya. In Kenya, just as Meier and Rauch argue "low-income consumers do not simply consume less: they consume goods and services which serve similar purposes but at a much lower price..." (Meier & Rauch, 2000)

## CHAPTER THREE

### RESEARCH DESIGN AND METHODOLOGY

#### 3.1 Introduction

This section highlights the research design and methodology of the study. It is divided into five parts namely; research design, target population, sampling design, and data collection instruments and data analysis methods.

#### 3.2 Research Design

The study employed descriptive research design. According to Cooper and Schindler (Cooper, 2003) descriptive design discovers and measures the cause and effect of relationships between variables. Mugenda and Mugenda (Mugenda, 2003) state that a descriptive research determines and reports the way things are and attempt to describe possible behavior, attitude, values and characteristics of such things.

#### 3.3 Target Population

The study target population was 1200 registered SMEs. The targeted SMEs operating their business in Eldoret town. The unit of analysis for the study tax registered SMEs by the Kenya Revenue Authority.

**Table 3.1 Target Population**

Type of enterprise	Target Population
Small scale enterprise	900
Medium scale enterprise	300
<b>TOTAL</b>	<b>1200</b>

### 3.4 Sample and Sampling technique

#### 3.4.1 Sample Size

The sample size is an important feature of any empirical study in which the goal is to make inferences about a population from a sample. In practice, the sample size used to study was determined based on the expense of data collection, and the need to have sufficient statistical power. Sample size is important primarily because of its effect on statistical power. Statistical Power is the probability that a statistical test will indicate a significant difference when there truly is one. (Morgan, 2001)

The study used Krejcer and Morgan to determine the ideal sample size for this study.

$N/k$ :

Where;  $N$ = Total number of companies in any given sector

$k$  item = every tenth organization selected in succession from  $N$  to form the sample

E.g. If the sample size was 1,200 firms divided by 10 = 120 Organizations

The study employed a systematic sampling technique. The respondent selected the first sample unit at random and then the remaining units were automatically selected in a definite sequence of the 10th. The sample size of the study was 120.

**Table 3.2 Sampling frame and sample size**

Type of enterprise	Target Population	Sample size 10%
Small scale enterprise	900	90
Medium scale enterprise	300	30
<b>TOTAL</b>	<b>1200</b>	<b>120</b>

Source: Kenya Revenue Authority, 2020

### **3.5 Data Collection Methods**

#### **3.5.1 Primary Data**

This study used primary data collection through questionnaires. The questionnaires were used because of their economy, their ability to ensure anonymity and use of standardized questions. It also provides time for subjects to think about responses. The questionnaires were made up of closed-ended questions in the form of a Likert scale. This method helped the study to collect enough information, which would otherwise be impossible through use of interviews and observations.

#### **3.6 Data Collection Procedures**

The relevant data was collected from the field with the aid of a research assistant, as the questionnaires were distributed on a drop and pick later method to allow the respondents time to sufficiently go through them and give feedback.

#### **3.7 Pilot Study**

The study was conducted a pilot test to pretest the validity and reliability of data collected using the questionnaire. A pilot group of 15 individuals from the target population was selected to test the reliability of the research instruments. The pilot data was not included in the actual study.

##### **3.7.1 Reliability of Research Instruments**

In order to test the reliability of the instruments, internal consistency techniques were applied using Cronbach's Alpha. The alpha value ranges between 0 and 1 with reliability increasing with the increase in value. According to (Mugenda, 2008), a coefficient of 0.6-0.7 is a commonly accepted rule of thumb that indicates acceptable reliability and 0.8 or higher indicated good reliability.

##### **3.7.2 Validity of Research Instruments**

According to Berg and Gall (1989), validity is the degree by which the sample of test items represents the content of test is designed to measure. Content validity was employed by this study to measure the degree to which data collected using a particular instrument represents a specific domain or content of a particular concept. Mugenda and Mugenda

(1999) contend that the usual procedure in assessing the content validity of measure is to use a professional or expert in a particular field

### **3.8 Data Analysis and Presentation**

Qualitative and quantitative approaches were used in this study as advocated for by Neuman (2000); and Babbie and Mouton (2001). These two main research approaches will be examined with respect to their suitability to the current research.

#### **3.8.1 The Qualitative Analysis**

Qualitative data collected through questionnaires were edited and response rate calculated. The data was then categorized into different themes according to research variable and descriptive statistics such as mean, standard deviation and frequency distribution which according to Kothari (2012) measures the point about which items have a tendency to cluster and describe the characteristics of the data collected was computed.

#### **3.8.2 The Quantitative Analysis**

Quantitative data from the questionnaire was coded and entered into the computer for statistical analysis. The Statistical Package for Social Sciences (SPSS version 20) was used for analysis. Frequencies, mean and standard deviation used to summarize the data.

Regression model was used to assess variables that are considered in assessing the factors that influence taxation of the informal sector. Regression Analysis is a statistical modeling technique used to identify meaningful, stable relationships among sets of data. The application of analytical procedures is based on the premise that, in the absence of known conditions to the contrary, relationships among information may reasonably be expected to exist. Regression measures the causal relationship between one dependent and one independent variable. Multiple regression analysis measures the effects of multiple independent variables on one dependent variable.

The study also adopted a multi regression model

$$Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \varepsilon$$

Where:

Y = Taxation

$\beta_0$  = Constant Term

$\beta_1$  = Beta coefficients

X1 = Financial Literacy level

X2 = tax literacy

X3 = Taxpayers attitude

$\varepsilon$  = Error term

### 3.9 Measurement of Variables

Table 3.1 gives a summary of research objectives, variables of study, their indicators, level of measurement, tools of analysis for each objective and type of tool employed for each objective.

**Table 3.3: Measurement of Variables**

<b>Variable</b>	<b>Indicators/measures</b>	<b>Likert scale</b>
<b>Financial literacy level</b>	Bookkeeping Accountant fees	5 points
<b>Tax literacy</b>	Level of access Knowledge of taxation system Understanding of tax law	5 points
<b>Taxpayers attitude</b>	<b>Access of public services</b> Peer attitude Motivation	5 points
<b>Taxation of informal sector</b>	Growth Target	5 points

## CHAPTER FOUR

### DATA ANALYSIS, PRESENTATION AND INTERPRETATION

#### 4.1 Introduction

This chapter presents the findings of the study and makes reference to relevant research to support the findings of the study. The findings include demographic information about the sample and results obtained from the descriptive statistics on challenges facing taxation of the informal sector in Kenya. In general, analysis was conducted using descriptive statistics and regression model.

#### 4.2 Response Rate

The researcher administered a total of 120 questionnaires and 118 were completed and returned. This represents a response rate of 96% as shown in Table 4.1. This response rate was adequate to allow the researcher to continue with the analysis. The questionnaires were composed of questions that addressed the objectives of the study.

**Table 4.1 Response rate**

Category	Frequency	Percentage
Completed and returned	118	96
Not returned	2	4
Total	120	100

### 4.3 Reliability test results

Reliability is measure of the degree to which a research instrument yields consistent result after repeated trials (Mugenda & Mugenda, 2003). The results are depicted in table 4.2 below.

**Table 4.2: Reliability tests results**

<b>Constructs</b>	<b>Reliability</b>		<b>Reliability</b>
	<b>Comment</b>	<b>No of</b>	
	<b>Cronbach's alpha</b>	<b>Items</b>	
Financial literacy	0.873	6	Accepted
Tax literacy	0.721	6	Accepted
Taxpayers' attitudes	0.766	6	Accepted
Taxation of informal sector	0.756	6	Accepted

The results of the reliability test produced an overall Cronbach Alpha correlation coefficient of 0.812 while specific findings indicated that, financial literacy had a coefficient of 0.873, tax literacy had a coefficient of 0.721, taxpayers' attitudes had a coefficient of 0.766 and taxation of informal sectors had 0.756 Table 4.2 shows that all the study variables yielded Cronbach alpha coefficients values of more than 0.7, which is the recommended value. This indicates that the instrument was reliable to obtain data on factors affecting taxation of informal sectors

#### 4.4 Descriptive Statistics

This section presents the descriptive results on financial literacy, tax literacy, and taxpayer's attitudes.

##### 4.4.1 Financial Literacy

The first objective of the study was to investigate the effect of financial literacy on taxation of the informal sector in Kenya. The respondents were asked to respond on statements on financial literacy. The responses were rated on a five likert scale as presented in Table 4.3. Majority of 88.10% (35.60%+52.50%) of the respondents agreed with the statement that problems like tax complexity; low tax morale, low tax compliance and shadow economy may all be reduced increasing the level of taxpayers' (individuals') financial literacy, 93.20% agreed with the statement that engaging and educating individuals could help them overcome tax system complexities and strengthen their feelings of responsibility and identity to the state, 78.00% of the respondents agreed that tax literacy is intended to firstly, help provide information about taxes, secondly, not to support any particular type or amount of taxes, but to simply explain taxes within a domestic system as well as a regional and international system, and how it impacts on those being informed, 76.20% agreed that a person is considered functionally tax literate if he/she can independently read and understand tax reports, can engage independently in various tax calculations and is aware of possible tax risks in its financial environment while 84.70% of the respondents agreed that income return forms are complex to complete and hence calls for one to be fairly educated to enable one peruse the return and complete it appropriately. The study findings are supported by a number of studies which includes (Patrick Sownali 2011).

**Table 4.3: Financial Literacy**

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	<b>Strongly Agree</b>	<b>Agree</b>	<b>Neutral</b>	<b>Disagree</b>	<b>Strongly Disagree</b>
<b>Statements</b>					

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Problems like tax complexity; low tax morale, low tax compliance and shadow economy may all be reduced increasing the level of taxpayers' (individuals') financial literacy.	35.60%	52.50%	11.90%	0.00%	0.00%
Engaging and educating individuals could help them overcome tax system complexities and strengthen their feelings of responsibility and identity to the state.	54.20%	39.00%	6.80%	0.00%	0.00%
Tax literacy is intended to firstly, help provide information about taxes, secondly, not to support any particular type or amount of taxes, but to simply explain taxes within a domestic system as well as a regional and international system, and how it impacts on those being informed.	45.80%	32.2%	22.00%	0.00%	0.00%
A person is considered functionally tax literate if he/she can independently read and understand tax reports, can engage independently in various tax calculations and is aware of possible tax risks in its financial environment.	20.30%	55.90%	16.90%	6.80%	0.00%
Income return forms are complex to complete and hence calls for one to be fairly educated to enable one peruse the return and complete it appropriately.	61.00%	23.70%	10.20%	5.10%	0.00%

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#### 4.4.2 Tax literacy

The second objective of the study was to investigate the effect of book keeping on taxation of the informal sector in Kenya. The respondents were asked to respond on statements on financial literacy. The responses were rated on a five likert scale as presented in Table 4.4. Majority of 74.50% (18.60%+55.90%) of the respondents agreed with the statement that accounting records in small business performance in that MSEs that kept proper books of account were able to measure accurately the performance of their businesses, 45.70% agreed with the statement that most micro-enterprises do not keep books of accounts that will allow them to extract useful accounting information due to lack of accounting knowledge, 83.00% of the respondents agreed that poor book keeping and poor financial management among a majority of MSEs has been attributed to low level of financial literacy especially among the adult population across countries, 72.90% agreed that the high fees charged by the accountants make it even more difficult for the few self-employed taxpayers who are willing to keep accounts of their business to hire the services of the accountants while 91.60% of the respondents agreed that use of accounting software to improve accounting practices. The study findings are supported by a number of studies which includes (Siekei, Wagoki & Kalio, 2013).

**Table 4.4: Tax literacy**

Statements	Strongly		Neutral	Strongly	
	Agree	Agree	Disagree	Disagree	Disagree
Accounting records in small business performance in that MSEs that kept proper books of account were able to measure accurately the performance of their businesses.	18.60%	55.90%	25.40%	0.00%	0.00%
Most micro-enterprises do not keep books of accounts that will allow them to extract useful accounting	23.70%	22.00%	39.00%	15.30%	0.00%

information due to lack of accounting knowledge.

Poor book keeping and poor financial management among a majority of MSEs has been attributed to low level of financial literacy especially among the adult population across countries.	57.60%	25.40%	16.90%	0.00%	0.00%
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The high fees charged by the accountants make it even more difficult for the few self-employed taxpayers who are willing to keep accounts of their business to hire the services of the accountants.	10.20%	62.70%	22.00%	5.10%	0.00%
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Use of accounting software to improve accounting practices.	44.10%	47.50%	8.50%	0.00%	0.00%
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### 4.4.3 Taxpayers attitudes

The third objective of the study was to investigate the effect of taxpayers' attitude on taxation of the informal sector in Kenya. The respondents were asked to respond on taxpayers' literacy. The responses were rated on a five likert scale as presented in Table 4.5. Majority of 83.00% (25.40%+57.60%) of the respondents agreed with the statement that evidence reveals that apart from access to capital and an enabling environment, the success of MSEs largely depends on the financial management skills of the managers, 86.40% agreed with the statement that to what extent, in your opinion, does your company value the payment of taxes to the Kenyan government, 89.80% of the respondents agreed that to what extent, in your opinion, does your company value the payment of taxes to the Kenyan government, 74.50% agreed that The informal sector is not only a provider of goods and services but also a driver in promoting competition, innovation and enhancing the enterprise culture which is necessary for private sector development and industrialization. The study findings are supported by a number of studies which includes Makongoro (2014).

**Table 4.5: Taxpayers attitude**

Statements	Strongly		Neutral	Strongly	
	Agree	Agree	Disagree	Disagree	Disagree
Evidence reveals that apart from access to capital and an enabling environment, the success of MSEs largely depends on the financial management skills of the managers.	25.40%	57.60%	16.90%	0.00%	0.00%
To what extent, in your opinion, does your company value the payment of taxes to the Kenyan government	20.30%	66.10%	13.60%	0.00%	0.00%

To what extent, in your opinion, does your company value the payment of taxes to the Kenyan government	59.30%	30.50%	10.20%	0.00%	0.00%
The informal sector is not only a provider of goods and services but also a driver in promoting competition, innovation and enhancing the enterprise culture which is necessary for private sector development and industrialization	23.70%	50.80%	13.60%	11.90%	0.00%

#### **4.4.4 Taxation of informal sector**

The dependent variable of the study was taxation. The respondents were asked to respond on statements on taxation. The responses were rated on a five likert scale as presented in Table 4.5. Majority of 86.40% (57.60%+28.80%) of the respondents were serious with the statement that KRA website lacks enough information on various tax procedures, 67.80% were serious with the statement that the system is slow / not functioning and there are long queues in gaining access to KRA offices, 79.60% of the respondents were serious that there were technical details on brochures and tax Acts that they don't understand delay in receiving feedback on queries raised, 59.30% were quite serious that there is lack of internet to download forms for filling returns while 64.40% of the respondents did not consider it serious that there is high fees charged by tax consultants and other professionals. The study findings are supported by a number of studies which includes (Joshi et al., 2014).

**Table 4.6: Taxation of informal sector**

<b>Statements</b>	<b>Not Serious</b>	<b>Indifferent</b>	<b>Quite serious</b>	<b>Serious</b>	<b>Very serious</b>
KRA website lacks enough information on various tax procedures.	0.00%	0.00%	13.60%	28.80%	57.60%
System slow / not functioning Long queues in gaining access to KRA offices.	0.00%	8.50%	23.70%	40.70%	27.10%
Technical details on brochures and tax Acts that I don't understand Delay in receiving feedback on queries raised.	0.00%	0.00%	20.30%	27.10%	52.50%
Lack of internet to download forms for filling returns.	0.00%	11.90%	59.30%	28.80%	0.00%
High fees charged by tax consultants and other professionals.	39.00%	25.40%	20.30%	15.30%	0.00%

## 4.5 Correlation Analysis

### 4.5.1 Correlation results on independent variables

Correlation shows the relationship existing between variables in the study. The study's dependent variable taxation of informal sector and the independent variables consist of financial literacy, tax literacy and taxpayers' attitudes

The results depicted in table 4.7 below

**Table 4.7: Correlation between independent variable and dependent variable**

Variables		Taxation of informal	Financial literacy	Tax literacy	Taxpayers attitudes
Taxation of informal sector	Pearson Correlation	1			
Financial literacy	Pearson Correlation	0.423	1		
	Sig. (2-tailed)				
Tax literacy	Pearson Correlation	0.436	1		
Taxpayers attitudes	Sig. (2-tailed)	0.002			
	Sig. (2-tailed)	0.001	.0012		

In an attempt to show the relationship between the study variables and their findings the study used the Karl Pearson’s coefficient of correlation (r). According to the findings as indicated in table 4.7, it was clear that there was a positive correlation between taxation of informal sector and financial literacy as depicted by a correlation value of 0.423. This implies that financial literacy were linearly related to taxation of informal sector. The study also depicted that there was a positive correlation between tax literacy and taxation of informal sector with a correlation value of 0.422 and another correlation was between taxpayers’ attitudes and taxation of information sector. This shows that there was a positive correlation between financial literacy, tax literacy, taxpayers’ attitude and taxation of informal sector.

## 4.6 Regression Analysis

The variables have a curvilinear relationship thus requiring use of analysis of variance (ANOVA) in order to develop a predictive model. From the correlation matrix, regression analysis was carried out in order to develop a model showing the relationship between independent variables and dependent variable. The purpose of the regression analysis was to get the relationship between the variables and come up with predictions model.

### 4.6.1 Model Summary

The study further analysed regression analysis of the challenges facing taxation of the informal sector in Kenya.

**Table 4.8: Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.694	.481	.453	.28828	.735

From the model summary, there is a strong positive correlation between the variables of the study as shown by the 69.4% while 48.1% of variations in the dependent variable can be explained by changes in the independent variables hence, the remaining 51.9% is representative of other factors not accounted for in the study.

### 4.6.2 Analysis of Variance – ANOVA

Analysis of variance determines whether mean scores of the effects of enterprise resource planning components on performance of public entities differ significantly from each other. It also determines whether the various variables interact significantly with each other.

**Table 4.9: ANOVA**

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	4.241	2	1.414	16.991	.000 <sup>b</sup>

Residual	4.576	118	.083
<b>Total</b>	<b>8.816</b>	<b>120</b>	

The overall model significance was presented using the ANOVA test table. The results in Table 4.9 shows that the overall model was a good fit since (F-value=16.991 and p-value=0.000<0.05) the findings there imply that all independent variables were statistically significant in explaining taxation of informal sector. ANOVA was used to test whether the regression analysis model used is fit or the relationship of the variable just occurred by chance.

Significance of F ratio is used to determine whether model used was fit or not. If the F ratio is significant the model used is considered fit and vice versa. A P - value of less than 0.05 indicates that the F statistics is high.

#### 4.6.3 Regression Coefficients

An estimation of the model coefficients emanating from the correlation matrix was done through analysis of the dependent and independent variables. The estimated co-efficient are shown on table 4.10.

**Table 4.10: Coefficients Matrix**

Model	Unstandardized		Standardized	T	Sig.
	Coefficients		Coefficients		
	B	Std. Error	Beta		
(Constant)	.480	.144		2.742	.000
X1 Financial Literacy	.293	.129	.611	2.193	.033
X2 Tax literacy	.254	.114	.004	.017	.047
X3 Taxpayers attitude	-.246	.122	-1.172	-5.580	.000

The correlation matrix coefficients were used to derive a prediction model for the challenges facing taxation of the informal sector in Kenya. Thus the correlation coefficients derived from the matrix have been used to come up with a standard prediction model.

The following equation was derived from the regression coefficients in the matrix.

$$Y = .480 + 0.293X_1 + 0.254X_2 - .246X_3$$

The coefficient financial literacy was 0.293 so we expect 0.29 unit increase in the taxation of informal sector holding all other variables constant. The coefficient for tax literacy is 0.354 so for every unit increase in level of awareness, we expect 0.35 point increase in taxation of informal sector. For taxpayer attitude is represented by a coefficient of 0.246, meaning for every decrease in taxpayer attitude a 0.24-unit decrease in taxation of informal sector is predicted holding all other variables constant.

## **4.7 Discussion of the key findings**

### **4.7.1 Financial literacy**

The first objective of the study was to establish the effect of financial literacy on taxation of the informal sector; findings reveal that problems like tax complexity; low tax morale, low tax compliance and shadow economy may all be reduced by increasing the level of taxpayers' (individuals') financial literacy. Which stated that, large informal economy in most developing countries presents a key reason for engaging in taxpayers' education. Engaging and educating individuals could help them overcome tax system complexities and strengthen their feelings of responsibility and identity to the state. Further collinearity analysis was done and the results revealed that financial literacy had a positive and significantly related to taxation of informal sector ( $r = 0.293$ ,  $p\text{-value} = 0.00 < 0.05$ ). The findings concur with OECD (2013)

### **4.7.2 Tax literacy**

The second objective of the study was to determine the effect of book keeping on taxation of the informal sector: findings reveal that most micro-enterprises do not keep books of accounts that will allow them to extract useful accounting information due to lack of accounting knowledge, 83.00% of the respondents agreed that poor book keeping and poor financial management among a majority of MSEs has been attributed to low level of

financial literacy especially among the adult population across countries. Whose study established the relevance of accounting records in small business performance in Nigeria and found that MSEs that kept proper books of account were able to measure accurately the performance of their businesses. Further collinearity analysis was done and the results revealed that tax literacy had a positive and significantly related to taxation of informal sector ( $r = 0.254$ ,  $p\text{-value}=0.00<0.05$ ). The findings concur with, Ezejiofor et al., (2014)

#### **4.7.3 Taxpayers attitude**

The third objective of the study was to determine the effect of taxpayers' attitude on taxation of the informal sector; findings reveal a negative impact on taxation of informal sectors. Further collinearity analysis was done and the results revealed that taxpayer attitude had a negative and insignificantly related to taxation of informal sector ( $r = -0.246$ ,  $p\text{-value}=0.00<0.05$ ).

## **CHAPTER FIVE**

### **SUMMARY, CONCLUSIONS AND RECOMMENDATIONS**

#### **5.0 Summary of Findings**

The study sought to establish the Challenges facing taxation of the informal sector, it therefore sought to establish how selected factors: financial literacy, tax literacy and taxpayers' attitude affect taxation in informal sector at Eldoret town.

#### **5.1 Summary of the findings**

The findings of the study have been summarized below as per the study objectives. The findings were supported by the frequencies of the responses

##### **5.1.1 Financial Literacy**

The study found that person is considered functionally tax literate if he/she can independently read and understand tax reports, can engage independently in various tax calculations and is aware of possible tax risks in its financial environment. Also tax return forms are complex to complete and hence calls for one to be fairly educated to enable one peruse the return and complete it appropriately. The overall mean score of response regarding financial literacy and taxation of informal section indicated that majority of the respondents agreed that financial literacy affects the taxation of information sector at Eldoret town. Correlation results indicated that there was a positive and significant relationship between financial literacy and taxation of informal sector. It was therefore concluded that financial literacy has significant positive effect on taxation of informal sector at Eldoret.

##### **5.1.2 Tax literacy**

The study found that the high fees charged by the accountants make it even more difficult for the few self-employed taxpayers who are willing to keep accounts of their business to hire the services of the accountants and that use of accounting software would improve accounting practices and minimize the inefficiencies and loopholes in tax administration. The overall mean score of response regarding tax literacy and tax literacy affects the taxation of informal sector at Eldoret town. Correlation results indicated that there was a

positive and significant relationship between tax literacy and taxation of informal sector. It was therefore concluded that tax literacy has significant positive effect on taxation of informal sector at Eldoret.

### **5.1.3 Taxpayers attitude**

The study found out that the overall mean score of response regarding taxpayers' attitude showing that taxpayers' attitude affects the taxation of information sector at Eldoret town. Correlation results indicated that there was a positive and significant relationship between taxpayers' attitude and taxation of informal sector. It was therefore concluded that taxpayers' attitude has insignificant negative effect on taxation of informal sector at Eldoret town.

## **5.2 Conclusions**

The study therefore concludes that informal sector taxation is not a new concept despite going by the findings and familiarity with respondents. It thus can be concluded that the parties that are involved in transactions that attract this tax are well conversant with its working. The study also concludes that financial literacy is a challenge to the taxation of the informal sector. This is so since some of entrepreneurs involved in the informal sector lack the proper and sufficient know how on accounting practices as well as filing the tax returns.

## **5.3 Limitations of the Study**

The research encountered few challenges. First the resources were limited especially due to the expense incurred during the entire research period since most required finance to ensure efficiency. Final limitation to the study was the aspect of time, thus limiting the scope and depth of the research study owing to the fact that it was time bound with deadlines that required a balance stricken between works and conducting the study.

## **5.4 Recommendations**

From the study's findings the following are the recommendations;

For a different research, more variables should be used as well as widening of the scope, which would help for comparison with the current study's findings. For managerial

purpose, the study recommends that Kenya Revenue Authority being the Tax Administration Authority should employ more technical staff and train them in interpreting the law which shall ensure that proper sensitization of this is done to the tax payers.

Policy makers should introduce stringent measures with respect to tax penalties and fines on the informal sector firms and tax payers who violate and act as an obstacle in the administration of this tax.

### **5.5 Areas of Further Research**

Further research can be done by expanding the scope of coverage to a different sector of the country's economy other than the informal sector. This would serve further to explain the different demands and unique needs attached to the sectors with regards to taxation. Also research could be done on this particular sector with the aim of establishing which other factor(s) constitute the 51.9% the analysis of this study's findings was referring to.

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## **APPENDICES**

### **APPENDIX II: INTRODUCTION LETTER**

Trizah Cheronu,  
P.O Box 19613-00202,  
Nairobi, Kenya.

Dear Respondent,

**RE: DATA COLLECTION**

I am a student at KESRA currently undertaking a research study to fulfill the requirements of the Award of Post Graduate Diploma in Tax Administration on the factors affecting taxation of informal sectors at Eldoret town. You have been selected to participate in this study and I would highly appreciate if you assisted me by responding to all questions in the attached questionnaire as completely, correctly and honestly as possible. Your response will be treated with utmost confidentiality and will be used only for research purposes of this study only.

Kindly note that the study will be conducted as academic research and the information you provide will be treated as confidential. Your participation in the exercise is voluntary and so you are free to choose to or not to participate. But it would be helpful if you could participate fully. Kindly spare a few minutes from your busy schedule to complete the attached questionnaire.

Thank you in advance for your co-operation.

Yours Faithfully,

**Trizah Cheronu**

## APPENDIX I – QUESTIONNAIRE

For each of the question below, please tick in the space provided for the answer that describes your opinion

### SECTION B:

#### A) Financial Literacy

Using the following scale, state your opinion by ticking on the space

1- Strongly Agree 2- Agree 3- Neutral 4- disagree 5- Strongly Disagree

Statement	1	2	3	4	5
Problems like tax complexity; low tax morale, low tax compliance and shadow economy may all be reduced increasing the level of taxpayers' (individuals') financial literacy.					
Engaging and educating individuals could help them overcome tax system complexities and strengthen their feelings of responsibility and identity to the state.					
Tax literacy is intended to firstly, help provide information about taxes, secondly, not to support any particular type or amount of taxes, but to simply explain taxes within a domestic system as well as a regional and international system, and how it impacts on those being informed..					

A person is considered functionally tax literate if he/she can independently read and understand tax reports, can engage independently in various tax calculations and is aware of possible tax risks in its financial environment					
Income return forms are complex to complete and hence calls for one to be fairly educated to enable one peruse the return and complete it appropriately					

**B) Tax literacy**

Using the following scale, state your opinion by ticking on the space

1- Strongly Agree 2- Agree 3- Neutral 4- disagree 5- Strongly Disagree

Statement	1	2	3	4	5
Is Information about taxes in Kenya readily available?					
How does the lack of tax information affect your company's tax compliance?					
As an organization we are able to correctly calculate the tax amount payable based on Available information.					

**C) Taxpayers attitude**

**Using the following scale, state your opinion by ticking on the space**

**1- Strongly Agree 2- Agree 3- Neutral 4- disagree 5- Strongly Disagree**

<b>Statement</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
Evidence reveals that SMEs are unable to public services/goods					
To what extent, in your opinion, does your company value the payment of taxes to the Kenyan government?					
To what extent does your company receive access to public utilities and services funded by the taxes collected for the government by the KRA?					
To what extent do you view other SMEs value the payment of taxes?					
the informal sector is not only a provider of goods and services but also a driver in promoting competition, innovation and enhancing the enterprise culture which is necessary for private sector development and industrialization					

**d. Taxation of informal sector**

**Tick your opinion on a scale of 1-5; where 1= „Not Serious“ and 5 for „Very serious**

<b>Challenges affecting taxation of the informal sector</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
KRA website lack enough information on various tax procedures					
System slow / not functioning Long queues in gaining access to KRA offices					
Technical details on brochures and tax Acts that I don't understand Delay in receiving feedback on queries raised					
Lack of internet to download forms for filling returns					
High fees charged by tax consultants and other professionals					

**Thank You for Your Cooperation**

**APPENDIX 1V: WORK PLAN**

<b>ACTIVITY (2018)</b>	<b>DECEMBER(2019)</b>	<b>FEBRUARY(2020)</b>	<b>JUNE (2020)</b>
Draft proposal			
Proposal presentation			
Designing the research instrument			
Proposal defense			
Field work & data Collection			
Data Entry / Analysis			
Report Writing			
Presentation of 1 <sup>st</sup> draft			
Presentation of 2 <sup>nd</sup> draft			
Submission of final report			