FACTORS INFLUENCING TAX COMPLIANCE AMONG SMALL AND MEDIUM ENTERPRISES IN WAJIA AREA, KENYA

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RESEARCH PROPSAL SUBMITTED TO THE DEPARTMENT OF ECONOMICS, ACCOUNTING AND FINANCE, SCHOOL OF BUSINESS IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF POST GRADUATE DIPLOMA IN TAX ADMINISTRATION AT JOMO KENYATTA UNIVERSITY OF AGRICULTURE AND TECHNOLOGY.

DECLARATION

This is my original work and has not been presented for award of post graduate diploma in any other university or any other institution of higher learning for examination.

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This research report has been submitted for examination with my approval as the University Supervisor.

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DR. MARION NEKESA

DEDICATION

I dedicate this project to my loving wife, Yasmin Abdi Ibrahim; your practical help and emotional encouragement as I pursued this course is highly appreciated. To my parents, and to my wonderful brother, Abdihafid , I would not have made it without your moral as well as financial support, understanding and perseverance during my study period.

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ABBREVIATIONS AND ACRONYMS

EAC	East Africa Cooperation
CGT	Capital Gain Tax
GOK	Government of Kenya
GDP	Gross Domestic Product
IEA	Institute of Economic Affairs
KRA	Kenya Revenue Authority
PAYE	Pay as you earn
PIN	Personal Identification Number
SME	Small Medium Enterprises
TMP	Tax Modernization Program
TOT	Turnover Tax
USD	USA Dollar
VAT	Value Added Tax

DEFINITION OF TERMS

Tax: A compulsory financial contribution imposed by a government to raise revenue, levied on the income or property of persons or organizations, on the production costs or sales prices of goods and services, etc.

Tax Compliance: The Degree to which a taxpayer complies (or fails to comply) with the tax rules of his country, for example by declaring income, filing a return, and paying the tax due in a timely manner.

Tax Evasion: It refers to the conscious or unconscious action and behavior of a person who is liable to pay tax but who fails to fulfill this duty by either under reporting his tax liability or failing to account for his income generating activities altogether. Tax evasion also refers to the reduction or minimization of tax liability by illegal methods.

Tax Rate: The tax rate is the tax imposed by the federal government based on an individual's taxable income or a corporation's earnings. Kenya uses a progressive tax rate system, where the percentage of tax increases as taxable income. It can also be defined as the percent of income paid as tax.

Tax Information: The knowledge or facts provided about taxes.

Tax Obligation: Responsibilities pertaining to tax payment and declaring of tax returns

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Tax Compliance cost: It refers to the expenditure of time or money in conforming with government requirements such as legislation or regulation.

Tax Attitude: The way of thinking or feeling about taxes

Tax Administration: annual sales turnover not exceeding Ksh 150 million.It refers to the procedures attached to tax compliance including registration and filling of returns.

SMEs: Those entities with full-time employees not exceeding 100 or annual sales turnover not exceeding Ksh 150 million.

Small Enterprises: An enterprise with 10-50 Employees

Medium Enterprises An enterprise with 50 -100 Employees

ABSTRACT

Tax is an important stream of revenue for government's development projects and therefore all efforts must be made by governments to ensure that it is accurately and efficiently collected so as to facilitate the government's operations. In an effort to maximize collection of revenue and efficiency in tax administration, key changes to tax policy evolving around ensuring equity, further widening the tax base, promoting increased investment and in so doing, reducing the tax compliance burden, have in the recent past been made by the Kenyan government. This study sought to identify the factors that influence tax compliance in Kenya, specifically focusing on SME's operating within Wajir Area. The researcher outlined a detailed literature review and identified the variables for this research to be tax rate, availability of tax information, tax compliance cost and attitude of SME's. The research was a descriptive survey. Given the large population of registered taxpayers in Nairobi, a sample size of 150 was picked as representative, to be the focus of this study. To ensure that various diverse categories of taxpayers and business entities were included in the survey, stratified sampling technique was adopted. Data was collected using self-administered questionnaires and an interview guide. The collected data was consequently analyzed using Statistical Package for Social Scientist software and the findings of the research presented using tables. The findings of the study revealed that with regard to tax rate as a factor influencing SMEs compliance, the majority view that Kenya has high tax rates with several different tax heads and this consequently hinders their level of compliance. The lack of readily available information relating to tax matters accounted to a great percent as a reason for non-compliance. The lack of information contributed to the inability of the taxpayers to correctly calculate the taxes payable; another form of non-compliance. The SMEs view that if more information would be availed to them in form of tax seminars and literature, this would demystify the complex concept of tax and greatly motivate them to be compliant. The findings of this study further revealed that 47% of the SMEs interviewed incur more than Ksh.50, 000 monthly, as costs of tax compliance. Some of these costs include bookkeeping, installation of software and internet costs, additional cost of hiring professional staff such as auditors and tax experts, accounting for the largest proportion of these costs. With regard to SMEs attitude as a factor affecting tax compliance, the respondents do agree and feel that they do have access to public utilities which are made available by the taxes paid to the government; hence they enjoy benefits of the taxes they pay. These organizations do value the payment of taxes to the government to a great extent, which affects their level of tax compliance. The findings of the study further revealed that the respondents do feel that their counterparts, fellow SMEs, also value the payment of taxes to the government to some extent. However, the taxpayers do feel and strongly agree that the taxation system in Kenya is in great need of improvement. By gaining an understanding of these underlying factors, KRA and the government will be able to make changes that will greatly improve taxpayers' tax compliance level, with the end result being increased government revenues, allowing the tax authority to give quality service to taxpayers and the government as a whole providing more and improved utilities to the public.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Tax Compliance can be defined as the degree to which a taxpayer complies (or fails to comply) with the tax rules of his country, for example by declaring income, filing a return, and paying the tax due in a timely manner. While Tax evasion can be defined as the failure by a person or business to comply with the tax obligations. It is a serious challenge to tax authorities in both the developed and developing countries. It diminishes the mobilization of resources that governments need to invest in critical areas of social and personal development including health, education and infrastructure development (Cummings, 2007). In 2011, it cost governments worldwide about 5.1 % of their Gross domestic Product (GDP). In Europe tax evasion constitutes about 8% of the GDP of economies in the region. In North and South America, tax evasion costs economies 2% and 10% of their GDP respectively. Even in the most advanced economies in the world, tax evasion undermines revenue collection substantially (Rile, 2011).

Since 1980s, a large number of developing countries have been in the process of making reforms in their financial sectors and government sectors (Das, 2011). Cheeseman and Griffiths (2005) noted that, before the reforms tax revenue in Kenya was as a result of heavy taxation of a limited tax-base, that is, a small group of people were charged large amounts; as well as high taxation of imports and exports. Reforms were introduced because of the increasing need to raise more revenue on behalf of the government through tax. Reisen and Trotsenburg (1988) observed that many developing countries urgently needed to mobilize resources to service their growing public debt.

The purpose for these reforms was to improve tax collection and reduce revenue leaks. Fjeldstad and Rakner (2003) noted that, despite important differences in their economic and cultural background, developing countries tended to modify their tax systems towards roughly the same direction.

Studies done in Africa suggest that most countries are competing against each other in giving more attractive tax incentives so as to attract more foreign direct investments to their countries but whether or not they are meeting the intended objectives is another issue (TJN –Africa, 2013). In its policy studies, the U.S Treasury policy studies department (2002) observed that the effects of tax policies should be analysed within a general framework where one explicitly recognizes the effects of tax policies on the level of services demanded from the government. Tax policies affect factor prices and the allocation of resources by the private sector and in the long run, the quantity of services demanded from the government by its citizens.

Maseko (2014) investigated the impact of personal tax knowledge and tax compliance costs behavior of SMEs in Zimbabwe. The findings of the study revealed that unlike large companies, SMEs face different business conditions which make them to endure high tax compliance load. Berhane and Yesuf (2013) assessed the challenges and opportunities of house rental income business tax in Regional state of Tigrayin Ethiopia. The study collected data via a survey questionnaire. The study findings established that there exists inefficiency and insufficient number of business house rent tax assessment and collection officers in the regional state of Tigray. Moreover, the study found that most taxpayers lack sufficient knowledge of tax assessment and collection procedures. Thus, most of business rent taxpayers do not know the existing applicable rules and regulations. Further, the study found that due to negligence, delay in tax payment and evasion are taken by taxpayers as solution to escape from payment of proper business house rental income taxes.

Kasipillai & Jabbar (2006) assessed whether gender and ethnicity differences occur in relation to tax compliance attitude and behavior. The results of t-test established that both male and female had similar tax compliant attitude and for ethnicity, similar results were also observed. In addition, regression results established that gender, education, and individual tax return preparation were statistically significant as the main determinants of non-compliant attitude.

1.1.1 Global perspective

In Europe, consisting of more than 25 member states with the same tax system. The tax system has been in existence for about 14 years. The voluntary tax compliance in Europe is actually anchored in the slippery slope framework (SSF) concept (Kirchler et al, 2008). The level of voluntary tax compliance has been determined by the government element in efficiency, absence of corruption and reliability.

As Kirchler (2008) posited, the aspect of trustworthiness was a determinant factor for the tax payers across Europe and is entrenched in the SSF model. Gangl et al (2009) in study of Dutch tax payers found out that the tax personnel had well entrenched self- respect for payers and this greatly contributed to a higher level of voluntary tax compliance. A study in UK, Austria and Czech Republic by Meuehlbacher et al (2011) found that the level of voluntary tax compliance was higher amongst the tax payers when trust, interaction and power were in the mix.

Australia, as a vibrant economy in Oceania has undergone numerous reforms from the 1990's with the thematic stand of improving the voluntary tax compliance (Pope, 2011). The government agency tasked with taxation is the Australian Agency Office (ATO). The ATO commissioned a reform strategy through a charter that articulated twelve rights of the tax payer.

The major strategies were well aligned to accountability, responsiveness, openness, professionalism and fairness. The strategies formulated by the ATO compliance model actually originated from the Cash Economy Task Force (Devos, 2014).

In effort to increase the voluntary tax payment, a four stalked pyramid system was designed and called the enforcement strategies (Lignier, 2009). It was worth noting that the voluntary tax compliance became a daunting task when there was a large social distance between tax authorities and the tax payers in Australia (Weber et al, 2014). Ethiopia, as a developing country in Africa faces myriad of challenges. When it comes to collection of required tax revenues, Ethiopia, like other developing countries across the globe have both vertical and horizontal tax systems but not fully integrated

(Desta, 2010). The lack of integration of the two systems is accrued to poor administration and tax collection measures. Belay (2015) posits that voluntary tax compliance in Ethiopia is inconsistent. In the period 1993-2014, the collection of tax revenues, depicted both upward and downward trend. The attributing factors to this lie in the difference in age group, gender, simplicity of tax systems, lack of knowledge and socio-economic activities spanning across Ethiopia country. There has been a negative publicity of the Ethiopian tax man hence impacting negatively on the voluntary tax compliance (Ermias, 2014).

According to Gcabo and Robinson (2007), tax collection is important to any country even though it is not favoured or understood by the country’s citizens. They went on to argue that, though the taxpayers acknowledge the need to pay taxes and enjoy the benefits offered by the government in form of public service, tax compliance is not favoured by the majority.

It is critical that the importance of tax compliance is understood because it determines how the government shapes lives of citizens (Oberholzer, 2008). According to Otieku (2008), a nation cannot have any significant economic development without optimistic spur from intelligent governments.

Though, the development agenda and programs of a country can merely be brought to certainty by the availability of finances. One of the most reliable sources of government revenue is through taxation. Several researches on tax compliance have conversely revealed that rental income tax compliance among the landlords leaves much to be desired. Tax system is of significant importance in running national income, particularly in developed countries and has played a vital part in cultured societies since their origin many years ago (Lymer and Oats, 2009).

However, it is important to note that not all payments to government are tax payments: for example, charges, tolls and other levies are paid to attain a specific service and are not strictly tax payments. In his book 'The Wealth of Nations' which was published in 1776, Adam Smith suggested that a good tax system is based on definite essential values, namely equity, convenience, certainty, and efficiency (Lymer and Oats, 2009). Bird (2012), Reveals that in most developing countries, more than half of the potential tax revenues tend to remain uncollected. This he further accredited to the large volume of the informal sector, dominated by the small business owners.

Flynn (2003) also noted that revenue loss from noncompliance by individual taxpayers, mainly the self-owned businesses were estimated to range from $93.20 billion to $95.30 billion for the tax year 1992. Kenya recognizing the high level of income tax non-compliance among the self-employed, has - 204 - employed several unusual way of taxation identified as self-assessment, block management, instalment tax payment. Song and Yarbrough (1978) demonstrate that in

Ghana non-compliance by the self-employed is a major factor accounting for tax authorities receiving less than what the regulation requires.

An effective revenue taxation enforcement policy is therefore necessary but the existing studies in the field of taxation have mainly centered on the problems of tax administration (Otieku, 2008), public perception of tax evasion (Song and Yarbrough, 1978) and managing small taxpayers. Tax compliance is a worldwide worry since most countries would like fund their recurrent expenditure through mobilization of domestic revenue. The complexities of rental income are evident globally. In the US, for instance, forty percent of Americans, most of who are mostly in the informal sector, are not in compliance with remittance of rental income to the tax authority.

The reasons for non-compliance are instructive. Firstly, taxpayers lack the requisite knowledge of the rental tax law or may interpret the law differently from the Internal Revenue Service. Secondly, taxpayers lack record keeping ability sufficient to satisfy the Internal Revenue Service According to GIZ, (2010) developing countries still lag far behind the developed countries in terms of tax compliance with the statistics standing at 35% and 23% respectively for developed and developing countries.

On the other hand, Marti, (2010) observed that the budgetary deficits that are pushing developing countries into high levels of public debt might be attributed to the high gap between the expected tax targets and the actual tax collections. This drives the budget into constant deficits that are slowing down the extent of economic development in these countries. Martin further indicates that developing countries must come up with strategies that will improve on policy development and implementation in order to reduce prevailing shortfalls and unhealthy dependence on donor funds.

Raising more domestic revenue is a priority for most Sub-Saharan African countries (Drummond et al. 2012). Mobilizing revenue is a way for governments to create fiscal space, provide essential public services, and reduce foreign aid and single resource dependence.

However, the domestic tax bases in most African countries are weakened by widespread tax avoidance and evasion (IMF 2011). Although taxpayer non-compliance is a continual and growing global problem (McKerchar and Evans 2009), many indications suggest that developing countries, mostly in Sub-Saharan Africa, are the hardest hit (Cobham 2005; Fuest and Riedel 2009). Li, (1999) noted that the main issue faced by all tax authorities is that it has never been easy to persuade all taxpayers to comply with the regulation of tax system.

This implies that there is a perceived lack of fairness between the two parties which this study sought to investigate and document on how this affects tax compliance in the rental income tax. Rummondet al. (2012) noted that of priority to many African countries is the need to raise more revenue domestically. The governments are after creating a more self-reliance in terms of mobilization of funds through effective revenue collection processes. This objective is hampered by among other things the low tax base, high level of tax evasion and avoidance (IMF 2011).

Italy loses €183 billion, or $242 billion, to tax evasion a year, and its debt of €1.9 trillion represents just over 10 years of tax evasion. Countries like Italy and Greece have vowed to crack down on tax evasion and cash transactions for goods and services that fall below the authorities' radar. Germany and Britain signed an agreement with Switzerland about recovering some tax revenue from accounts held by their citizens in Swiss banks. South America has the world's largest shadow economy compared with its G.D.P. followed by Africa and Europe, where income hidden from the tax authorities amounts to about 20.5 percent of G.D.P. That compares with 10.8 percent in North America (Association, 1998). Of the three East African countries of Kenya, Uganda, and Tanzania, tax evasion as a function of GDP is high. Uganda loses the least amount in tax evasion: In 2011, it lost 856 million USD, followed by Tanzania at 1.9 billion USD, and Kenya loses slightly over 2 billion USD. In 2011, the informal economy constituted 33% of the GDP in Kenya and represented 7% of total government expenditure. The tax burden in Kenya would thus be high, standing at about 20.9%. If the Kenya government is to increase its social expenditure, then it needs to reduce tax evasion in the informal economy (Griffiths, 2005).

Taxpayers' behavior towards tax system has evoked great attention among many Revenue Authorities in the World especially in Developed Countries. However, it is debatable on what has been done towards the study of taxpayers behavior towards tax system in developing countries as they concentrate more in studies which would increase their budgets bottom-line in terms of huge revenue collection and enforcement efforts at the expense of studies on taxpayers behavior which would make increase in this tax revenue to be realized and enforcement efforts work. Perhaps the less developed countries are not to blame as they run on budget deficits hence, scarce resources to see through such studies which are perceived as adding no direct value to revenue collection. Empirical evidence on the ground shows there has been hostility between the taxpayers and tax collectors on issue relating to tax compliance (Porcano, 2011)

1.1.2 Kenya Perspective

The country experiences challenges in generating revenue to the required level necessary for economic growth. For years, the Kenya government has attempted different income tax reforms aimed at enhancing revenue collection. One of the measures was the presentation of self-assessment frameworks (SA) in 1992. The objectives of this system were to increase voluntary compliance, reduce the burden of assessing tax returns and reduce tax collection costs.

It is law that any income generated from any investment in the country is subject to taxation (Karanja, 2014). However, the low tax revenue is more attributed to lack of good mechanisms to enforce tax collection. The Kenyan government needs to invest more on tax administration so as to ensure that no tax revenue is lost or uncollected. As such, Kenya is also ranked among countries with low compliance as far as tax revenue collection is concerned (Makori et al., 2013). Although there has been significant growth in tax collection by over 300% (2003-2011), the contribution by landlords has been very low despite all the efforts by government taxing all Kenyans to support the development of the economy by paying their fair share of taxes (Karanja, 2014). A tax rate of 10% on the gross monthly rental income came about when the Finance Act 2015 introduced a new section 6A in the Income Tax Act that provides for a simplified tax regime on rental income.

However, if the rent collected exceeds ten million shillings during a year of income one does not qualify to be in this bracket. Under this new regime, landlords are expected to remit the tax when they receive the rent from their tenants. This can be on a monthly, quarterly, semiannually or annually but they are required to file returns on a monthly basis and when there is a period where they do not receive any income the will file a nil return. Also in this regime one is not allowed to deduct expenses before calculating the tax.

Taxation on rental income has been in existence since implementation of the Income Tax Act of 1973. However, the majority of landlords have not been complying with the Act due to lack of government mechanisms to identify and bring landlords into the tax net. Many have also been collecting rent by themselves or using unregistered agents, thus making it difficult to trace their income for the purpose of taxation. The move by the government to tighten the law on taxation on rental income amid increasing costs of doing business in Kenya has received mixed reactions from landlords due to their impact on business.

Tax non-compliance is an area of concern for all tax authorities. The main problem is that it has never been easy to persuade all taxpayers to comply with the regulations of a tax system. In contrast to the majority of employed people, who in many countries are paid net salaries with taxes being deducted at source, real estate investors often need to self-assess and self-report their income and pay taxes voluntarily. They should only pay their income tax but take also account of various types of business taxes. The KRA faces challenges in Tax compliance, tax avoidance and tax evasion. Most individuals in lower income bracket do not understand rental income due to lower levels of literacy.

Another challenge experienced by tax payers is the discipline of keeping records especially those in sh.10 million bracket per annum. Due to this challenge, it has embarked to customer focused approaches such as tax payer's education and training seminars for both its employees and the taxpayers. Before focusing on training, KRA simplified rental income tax regime was introduced. KRA is aiming to rope in additional 66,000 landlords in the next three financial years, ending 2020/2021. A collection of 8,584 billion and growth of 41.7% in the annual revenue performance report 2018/2019 and close to 37,000 landlords are already on board.

The commercial real estate market worldwide is increasingly dominated by institutional investors. This presents a challenge to private real estate investments because individuals properties are not bought and sold on regular basis like estates and bonds, Kohnstamm, (1995).

This study will narrow down to individual investors who are in new and old regime. Old regimes are investors earning an income of over ksh. 834,000 a month which equals to over ksh. 10,000,000 a year and are taxed at 30% per annum in graduated scale. The beauty of the old regime is that taxpayers can claim for expenses of up to 40%. Payment can also be done in instalments. The new regimes are investors earning rental income of over ksh. 12,000 a month. Tax rate for new regime is 10% a month.

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. Another measure to widen the tax base was the introduction of capital gains tax (CGT) in 1975 to cash in on high property prices arising from a coffee boom. But, in 1984, in an effort to jumpstart economic growth through the construction industry, GoK suspended the CGT and formed a commission to examine economic management, and extend advice on possible changes (A.D.B, 2010).

Tax policies introduced under the TMP (Tax Modernization Program) (1986 to 2002) thrust under the TMP (1986 to 1996) was to raise and maintain revenue as ratio of GDP at 24% by 1999/2000; expand the tax base; rationalize the tax structure to make it more equitable; reduce and rationalize tax rates and tariffs; reduce trade taxes and increase them on consumption to support investment; 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.

1.2 Statement of the Problem

Tax evasion hampers government revenue collection thus inefficiency in Government spending because it diminishes the capacity of the state to mobilize domestic revenues, resources that are needed for investments. In 2010, for example the amount lost to tax evasion represented about twice the amount the country spent on health care. Tax evasion also damages the country's growth capacity by discouraging both local and foreign investors. The high tax rate and burden in Kenya, which is related to the high levels of tax evasion, is the leading disincentive to business activity (Karingi, 2005)

The increasing trend of disparity between the levels of submitted annual income tax returns, reported tax assessments and voluntarily paid tax liabilities, among SMEs, on the one hand, and the trend of business birth and growth, on the other hand, has been a cause of worry to the government of Kenya. This resulted in the government offer of an olive branch to taxpayers through the tax amnesty announced by the Minister for Finance in Kenya in 2004 (GOK, 2004)

Tax revenues have, for quite some time, remained low relative to the number of both registered and non registered firms and individuals who are legally qualify to pay tax. Continued low revenue collection levels for government is detrimental to economic development of this nation. (Cobham, 2005). A large segment of the informal sector, especially the SMEs in Industrial area in Nairobi exhibit low tax compliance levels. This is a great loss of revenues meant for public expenditure.

In Kenya, taxation has been the main source of revenue to the government. The taxes are used by the government to provide public goods and/or services to general public. Over the past years, though revenue collections by the Kenya Revenue Authority have increased, the revenues collected have not been sufficient to fund the budget proposals resulting into budget deficits (Alegana, 2014). In addition, several studies have also been carried on tax compliance around the globe. A study by Hargreaves (2008) explored the influence of tax system on New Zealand's housing market and revealed that owner-occupiers do not pay tax from a rental income. Palil (2010) also investigated tax knowledge and tax compliance determinants in self-assessment system in Malaysia and established that compliance of tax is influenced by probability of being audited, penalties, personal financial constraints and referent groups. However, the above international studies did not concentrate on residential rental income taxes.

In Kenya, a study by Osebe (2013) analyzed factors which affect tax compliance in Kenyan real estate sector and established that compliance costs, knowledge of tax and education, penalties and the perceived tax evasion opportunities influenced tax compliance. Noncompliance is closely linked to tax evasion except that it incorporates apart from evading taxes, aspects of complying with other income tax rules and regulations such as deadlines for submission of tax returns in addition, few studies on rental income taxation in Kenya are based on the old method of taxation where landlords were taxed at a rate of 30% on their net rental income in comparison to the current 10% tax rate on gross income.

It is for this reason that research need to be undertaken to identify the causes for low tax compliance among small and medium enterprises in Industrial area. It is also instructive to note that there is little research that has been done in this area. In this context SMEs in Wajir area exhibit low tax compliance levels and this requires an understanding on the determinants of tax compliance to enable the government to improve on its tax collection among the SMEs in Wajir area.

1.3 Research Objectives

1.3.1 General Objective

The general objective of this study was to evaluate the factors that influence tax compliance among Small and Medium Enterprises in Wajir area, Kenya.

1.3.1 Specific objectives of the study

This study was guided by the following specific objectives:

1. To determine the extent to which tax rates explains tax compliance among Small and Medium Enterprises.
2. To analyse the availability of tax information as a factor influencing tax compliance among Small and Medium Enterprises.
3. To find out the extent to which costs incurred by Small and Medium enterprises in being tax compliant influence their level of tax compliance.
4. To investigate how Small and Medium Enterprises attitude about tax influence tax compliance.

1.5 Research Questions

This research was guided by the following research questions:

1. To what extent do tax rates in Kenya explain tax compliance among Small and Medium Enterprises?
2. How does the availability of tax information influence tax compliance among Small and Medium Enterprises?
3. To what extent does the cost of tax compliance explain tax compliance among Small and Medium Enterprises?
4. How does the attitude of Small and Medium Enterprises about tax influence tax compliance?

1.6 Significance of the study

1.6.1 The government of Kenya

The government is not able to collect the required taxes from the targeted tax payers. From the SME point of view, tax evasion is driven generally by a perception that the tax burden is too high. This poses a number of problems to tax systems, raising difficult questions over how tax policies and tax administration may influence tax compliance incentives and behavior.

1.6.2 The Kenya Revenue Authority

This study focused on how social, cultural and personal factors influence tax compliance. It is anticipated that the results of this study will provide concepts and grounds on which to develop a framework. The knowledge accruing from this study could benefit the Government of Kenya and its revenue collection body Kenya Revenue authority in its effort to design suitable tax policies for SMEs.

1.6.3 SMEs attitude

This study has provided concepts which to develop a framework to explore tax compliance behaviour among SMEs. It has opened the underlying factors that promote tax compliance. 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.

1.6.4 Future researchers

Finally, the research will be of interest to scholars and researchers who may require developing and/or advancing their knowledge in the field of tax compliance and administration.

1.6 The scope of the study.

This study sought to identify the factors that influence tax compliance in Kenya, specifically focusing on SME's operating within Wajir Area

1.7 Limitations of the study

Time constraint was a limiting factor because the study is to be concluded within a short time. Availability of funds was also a limiting factor to the study since the researcher is self sponsored. There was no assurance that the respondents will return all the questionnaires duly completed, neither was there a guarantee that those who will be interviewed would respond to all the questions put forward to them comprehensively for fear that it would expose their non-compliance to K.R.A.

To counter these limitations, the researcher took leave from work to make time to interview the respondents and also sought for funding from relatives. The SMEs fear of participation was overcome by explaining to them the intent of the study and issuing the transmittal letter as well as the supervisors contact for verification purposes.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter outlined the various schools of thought revolving around tax compliance and evasion. This Chapter identified the various theories put across by various scholars in relation to tax compliance. For the research questions identified in Chapter One, the researcher highlighted the findings of different authors, on the factors influencing factors influencing tax compliance among SMEs.

2.2 Theoretical Framework

This study borrowed heavily from existing research that is increasing. It was influenced by the following theories which have been put across by various scholars with regard to adoption of technology in society:

2.2.1 The Tax Morale Theory

The tax morale theory was first advanced by German scholars centered around Gunter Schmolders known as Cologne school of tax psychology. Tax morale can be termed as the individual factor that motivates a person to comply with his or her tax obligations. As a determinant of tax behavior, tax morals aim to explain how and why a tax payer morality influences his or her tax behavior. Many studies have found out that tax evasion can be attributed to the tax morale (Mocetti, Vol 18 No. 6).

Tax payers would be inclined to evade tax when the communities in which they live or operate disapprove of tax evasion. Tax payers are more likely to comply with tax obligation if their friends, relatives and acquintances comply with these obligations. Also tax payers will evade taxes if they feel that other people are getting away with tax evasion.

In some instances tax payers can feel morally feel justified in evading taxes if they feel that the quality and quantity of public services and goods are unsatisfactory. The opposite is also true. In economies where the provision of pulic goods and services is satisfactory the evasion rates are low.

Tax payers will tend to comply with their tax obligation if they feel that their government is honest, democartic and participatory and also if the tax payers feel they play a meaningful role in governance (Cummings, 2007). Thus tax payers attitude are important predictors of tax evasion thus the study aims to interpreate the tax attitudes of SMEs and how it contibute to tax evasion.

2.2.2 The Allingham and Sandmo Theory (AS Theory)

This theory was advanced by Allingham and Sandmo. 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 percieves 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 probabilty 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 since 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.

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 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.

2.3 Conceptual Framework

This study sought to conceptualize how tax compliance among SMEs in Wajir is affected by tax rates, tax information, compliance cost and SMEs attitudes. Its main purpose is to establish how strongly these factors affect the level of tax compliance. Tax compliance is the dependent variable in the study while tax rates, tax information, compliance cost and SMEs attitudes are some of the independent variables. The conceptual framework is shown below.

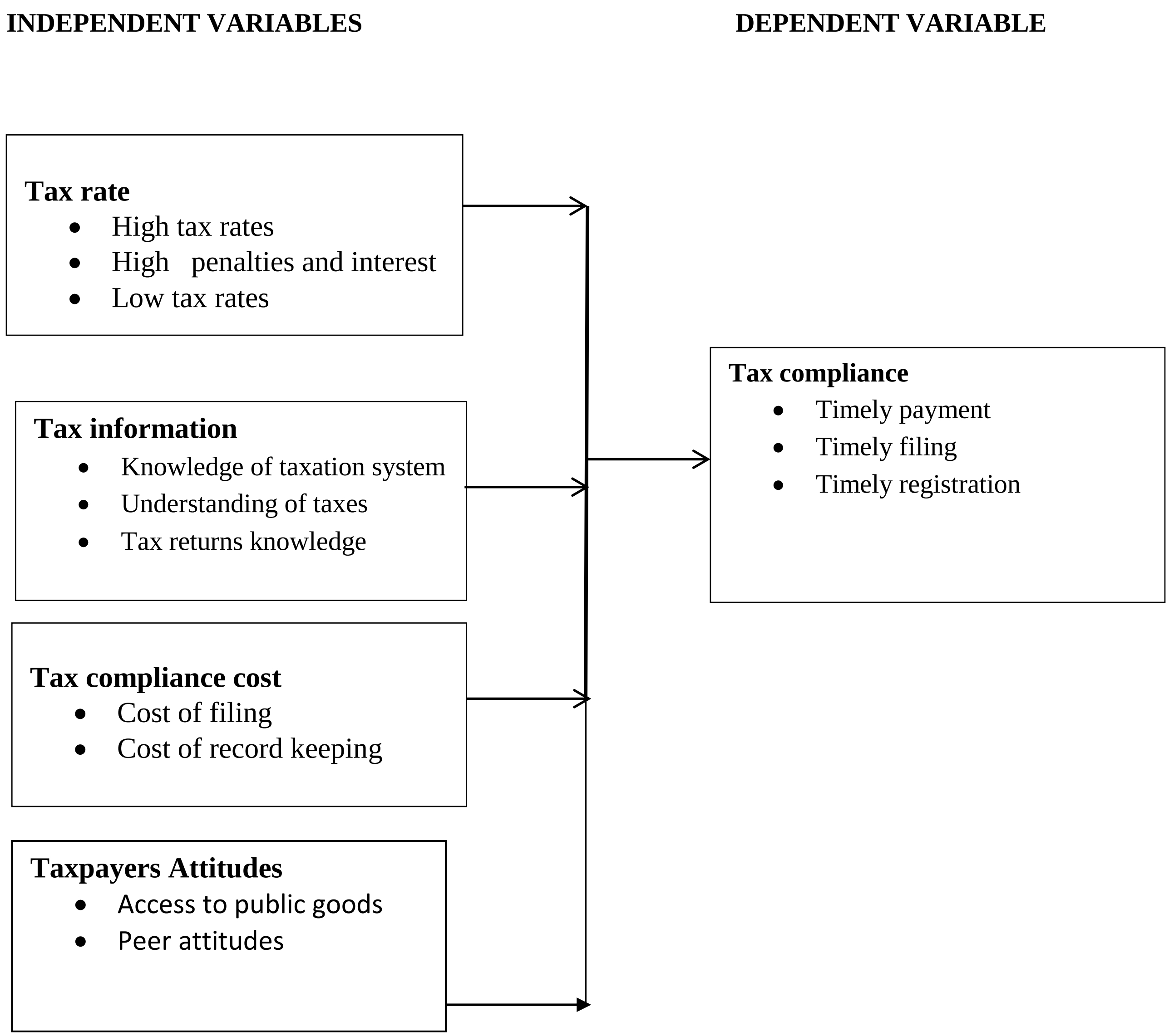

Figure 2.1: Conceptual Framework

2.4 Empirical review

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 policy makers. (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).

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.

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 non compliance 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 non compliance 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)

2.4.1 Tax Rate

It is generally believed that a high tax rate is the main cause of tax evasion. Incentives to evade tax depend on the marginal rates of taxation because these govern the gains from evasion as a sum of the sum evaded (Kaldor, 1956) One major tax evasion is the high personal income tax rates which tend to lead tax payers to evade tax. Too many and complicated rules and regulations imposed by the government tend to lead to tax evasion.

Businesses find it generally difficult often not profitable to do business legally. The heavy taxation is also a subject of worry not only in developed countries like USA but also in Kenya and other less industrialized countries in Africa and Latin America. For instance, taxes in Kenya confront the large manufacturing sector in different shapes and shades example: import duties, export & excise duties, sales and VAT, withholdings and income taxes, and PAYE etc. (KRA, 2011). The high levels of taxation of SMEs in Africa and in Kenya in particular, warrants attention on accelerated research areas aimed at addressing the overall effects of taxation on SMEs (Osambo, 2009).

By studying taxation behavior in five different countries (USA, Gambia, Nigeria, South Africa and Kenya), Derwent (2000) concluded that increased tax burden is a major threat. The results show that the increase in tax rates leads to higher production, distribution and selling costs which lead to higher prices and as a result consumers change their buying behavior. People react to the higher prices by buying less of the product. When sales fall, some manufacturers cut back on production and some workers may lose their jobs.

The productive resources i.e. land, capital, labour and entrepreneurship are allocated to other industries or go unused. For instance when the government increase taxes on items such as beer and cigarettes for the purpose of realizing revenue and discouraging their consumption people tend to buy local brews. Whenever prices increase due to increase in tax rates; prices of goods and service increase and there is a drop in the consumption rate and a decrease in sales volumes which leads to retarded growth of SMEs. Tax payment is among the outflows of cash from the business which reduce the purchasing power of an enterprise.

This is due to the fact that a large amount of cash collected is used to pay taxes rather than to expand the business. The study showed that the purchasing power of an enterprise drops immediately an organization pays taxes (Mika Mungaya, IJMBS Vol. 2, Issue 3, July - Sept 2012)

Some studies suggest that high tax rates foster evasion. The intuition is that high tax rates increase the tax burden and, hence, lower the disposable income of the taxpayer (Chipeta, 2002) However, the level of the tax rate may not be the only factor influencing people's decision about paying taxes. In fact, the structure of the overall tax system has an impact as well. If, for example, the tax rate on corporate profits is relatively low, but individuals are facing a high tax rate on their personal income, they may perceive their personal tax burden as unfair and choose to declare only a part of their income. Similarly, large companies can often more easily take advantage of tax loopholes, thereby contributing to the perceived unfairness of the system. Tax rates and the overall structure of the tax system, therefore, have a significant effect on the disposition to evade and avoid taxes.

2.4.2 Tax Information

Standard models assume that tax payers are fully informed of all the aspects that cover the tax reporting processes. However this is a strong assumption and not the case. (Andreoni J. Errard, 1998) Tax research has shown that the degree of information is an important factor on the behavior of tax payers and how it influences tax evasion. Less educated tax payer's are less exposed to tax compliance information and are less informed about relevant tax compliance information and thus are more prone to tax evasion.

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.

The way business is conducted has also become more sophisticated due to the geographical spread of enterprises. We have recently witnessed many multinational companies set up operations in Kenya in keeping pace with the wave of globalization. The world has become a global village but it is unfortunate that our tax laws have not kept pace with this trend. For instance, it is not a wonder to find a company producing goods in one country and selling in another country to benefit from tax advantages in low tax jurisdictions. The complexity of business transactions makes the application of intricate tax laws that have generally not kept pace particularly problematic.

Tax payers often find themselves in difficult situations while making important business decisions as tax laws may not be clear as to the treatment of complex business transactions. Our tax legislation does not provide for advance tax rulings though in practice, tax payers seek the Commissioner's interpretation of various tax laws or tax implications of certain business transactions. Sometimes this is done on a no-name basis in order to retain confidentiality (Muiru, 2012). Kenya has a complex tax system that makes it expensive for taxpayers to comply with an increased cost of doing. it is costly to implement occasioning losses Kenya's economy. The more complex a tax system is the more costly is its administration and the more expensive it is for people to comply with it. Taxes administered in Kenya include corporate income tax, personal income tax, Value Added Tax (VAT) and withholding tax. Corporate income tax rate is 30 percent, personal income tax rate ranges between 10 percent and 30 percent, VAT rate is 16 percent and while withholding tax rates begin from 3 percent and depend on income source and whether one is a Kenyan or not (Government of Republic of Kenya, 2012).

2.4.3 Tax Compliance Cost

A compliance cost is expenditure of time or money in conforming with government requirements such as legislation or regulation. For example, people or organizations registered for value added tax have the extra burden of having to keep detailed records of all input tax and output tax to facilitate the completion of VAT returns. This may necessitate them having to employ someone skilled in this field, which would be regarded a compliance cost

Compliance costs normally include all costs associated with obeying the law, including planning and administration, in addition to the direct time and money spent filing paperwork. Businesses especially small ones often face heavy costs in the process of preparing, filing, and paying taxes in addition to the burden of tax payments.

These compliance costs, added to fines, penalties, and the risks of inspections and demands for bribes, often deter business creation and growth in developing and transition countries. A tax compliance cost survey can provide useful information for the design of reforms to reduce compliance costs and risks for small businesses. This note highlights key findings of tax compliance cost surveys conducted in South Africa, the Republic of Yemen, Ukraine, and Peru that measured the burdens on business. These surveys helped fine-tune the design of reforms to lower costs for businesses and improve their competitiveness (Coolidge, 2010)

High compliance costs can result in tax avoidance, tax fraud, and inhibit investment by way of diminishing competitiveness of the country in terms of taxation attractiveness (Ojeka, 2012). The full cost of a tax system is more than simply the amount of tax paid. It also includes the cost of tax planning and paperwork. Economists call these "tax compliance" costs, and the IRS estimates Americans spend 6.6 billion hours per year filling out tax forms—including 1.6 billion hours on the 1040 form alone. In a study carried out on tax compliance and simplifications (OECD, 2004) established that compliance costs tend to increase with the number of taxes that an entrepreneur is subject to, the complexity of the tax rules, the frequency of submitting tax returns and the number of levels of government involved in levying and collecting taxes.

Taxes introduce complexities and costs not relevant to SMEs and the complexities may increase where more than one level of government is involved for example the devolved government in Kenya. This results to SMEs avoiding the paying of taxes as it affects the business.

2.4.4 Taxpayer's 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 behaviour and tax compliance behaviour 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 assex, 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 neighbours are not reporting and paying tax honestly, and non rewarding taxpayers.

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)

Tax compliance

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.

2.5 Critiques of the literature

(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)

Maseko (2014) investigated the impact of personal tax knowledge and tax compliance costs behavior of SMEs in Zimbabwe. The findings of the study revealed that unlike large companies, SMEs face different business conditions which make them to endure high tax compliance load.

Berhane and Yesuf (2013) assessed the challenges and opportunities of house rental income business tax in Regional state of Tigray in Ethiopia. The study collected data via a survey questionnaire. The study findings established that there exists inefficiency and insufficient number of business house rent tax assessment and collection officers in the regional state of Tigray. Moreover, the study found that most taxpayers lack sufficient knowledge of tax assessment and collection procedures. Thus, most of business house rent taxpayers do not know the existing applicable rules and regulations.

Further, the study found that due to negligence, delay in tax payment and evasion are taken by taxpayers as solution to escape from payment of proper business house rental income taxes.

Kasipillai & Jabbar (2006) assessed whether gender and ethnicity differences occur in relation to tax compliance attitude and behavior. The results of t-test established that both male and female had similar tax compliant attitude and for ethnicity, similar result were also observed. In addition, regression results established that gender, education, and individual tax return preparation were statistically significant as the main determinants of non-compliant attitude.

Musau (2015) assessed factors influencing tax compliance among SMEs in Nairobi County. The study picked a sample of 398 respondents and collected data using questionnaires which was analyzed using the binary probit regression model.

The study findings revealed that when an individual perception about difficulties of evading taxes increases, the high likelihood of being tax compliant among SMEs in Nairobi County. The findings also revealed those individuals who are satisfied with what the government is offering as public goods and service from taxes; have enough tax information; trust government officials in handling their taxes; and have the perception that if tax filing procedures are less complex, tax payers are likely to comply with tax payment.

Mukabi (2014) explored factors influencing turnover tax compliance in the Kenya revenue authority domestic taxes department in Nairobi County. The study used a sample of 56 respondents selected via stratified sampling and data collected using questionnaires. The study findings revealed that the perceptions of taxpayers towards the tax system greatly determine the level of compliance for turnover tax. The findings also found that other factors like cost of compliance and complicated systems result into the low levels of compliance. The study also established that increased tax knowledge had a significant effect on perception of tax system.

Thananga, Wanyoike and Wagoki (2013) carried out a study on how landlords in Nakuru Municipality responded to new taxation measures, and factors which influence compliance. The study used a sample of 94 respondents and questionnaires for data collection. The findings of the study revealed that compliance level to provisions of rental income tax policy by landlords was very low and non-compliance was due to expenses overstatement and deductions which would in turn reduce taxable pay.

Karanja (2014) examined factors affecting voluntarily tax compliance in Kenya by landlords in Nairobi County. The study adopted a descriptive research design and a sample of 45 respondents was selected and questionnaire used for data collection. The findings of the study established that attitude and perception that politicians misuse taxes, financial and family obligation had strong positive responses. The study findings also revealed that social norms and respondent's income levels strongly influenced tax noncompliance level among the Kenyan taxpayers on rental income.

The study concluded that attitude factors, high tax rate, unfair tax system, social norms, gender and education level factors are significant and play a great role towards the compliance or noncompliance of Kenyan taxpayers. 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.

(Chipeta, 2002) In addition, most prospective entrepreneurs are not aware of business start-up regulations and taxation procedures, mainly due to lack of effective information dissemination strategies on government policies. This prevents the sector operators from entering into formal economy and tax evasion and corruption as normal way of doing business.

The informal sector operators who opt not to pay taxes and do business without licenses operate incognito in back alleys and roadsides. They are often mobile and in most cases engage in running battles with law enforcement and council authorities.

In the process of evading taxes, they end up paying more money in the form of bribes, to the law enforcers (Programme Issue No. 29 September 2012). They also have more opportunities for tax evasion and opportunities might further increase with the number of different income sources. Hence, in compliance decisions the level of income might interact with its source. The importance of how one's economic status is perceived was demonstrated by (Vogel, 1974) taxpayers who reported improvements of their economic status were less compliant than others who reported deterioration of their financial well-being. A positive relation of SMEs income and tax compliance also found empirical support. In an experimental study, (Feld, 2002) found that tax compliance is higher on average in an endogenous fine treatment in which subjects are allowed to approve or reject the proposal of a fine as compared to an exogenous fine treatment where the fine is imposed by the experimenter.

The main explanation why people show higher tax morale if they are allowed to vote on a fine is legitimacy. Compliance rates are higher if the fine is accepted than in the case the fine is rejected. Subjects who reject the proposal of the fine show a higher compliance rate than subjects in the exogenous fine treatment even if they know that the dominant strategy under the existence of the low fine is non-compliance. Combining econometrics and surveys methods, (Spicer, 1976) sought to investigate impact of attitude and social norms in the evasion decision; the data were collected from a 1974 survey in USA.

Econometric results revealed that the propensity to evade taxation was reduced by increased probability of detection. Surprisingly, an increase in income reduced the propensity to comply. With respect to attitude variables, an increase in both inequity of taxation and the number of taxpayers who evade taxes known to a taxpayer made evasion more likely. This study also revealed that the experience of taxpayer of previous audits by the income department influences the compliance rates.

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 affect tax compliance among SMES. The research focused on tax rate, tax information, tax compliance cost and taxpayers attitude. The research outlined in this paper aims to address the tax gap of non filling, under reporting and under payment. The specific aim of the research is to gain insight into the factors that influence the tax compliance among SMEs in Kenya by focusing on those operating within Wajir area. 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.

2.6 Summary of literature review

The independent variables are tax rate and system, tax information and education, tax compliance cost and taxpayers attitude. Tax rate and system as an independent variable influencing tax compliance is indicated by the complex nature of the tax system and high tax rate. Tax information and education is the second independent variable is characterized by the lack of knowledge of taxation by SMEs as well as misunderstanding of the taxation system. Tax compliance cost is characterized by the time it takes and the cost of compliance by SMEs. Taxpayer’s attitude is indicated by the attitude the taxpayers peers have with regards to tax compliance as well as the motivation tax compliance holds for the SMEs.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter outlined the research methodology as the method of achieving the purpose of the study. This includes the research design, target population, sampling for the study, data collection instruments and data analysis. Section 3.2 outlines the research design.

3.2 Research design

A descriptive survey design was adopted for this study. A descriptive survey design was best for this study as it describes characteristics associated with the subject population, and in particular factors that make them behave the way they do. 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. The study used a descriptive design because it enables the researcher to collect a large quantity of in-depth information about the population being studied. A survey design was appropriate as the data required for analysis needed to be collected from a large population that is SMEs operating in Wajir area.

3.3 Target population

The research targeted SMEs operating their business in Wajir area. The unit of analysis for the study is any SMEs registered by the Kenya Revenue Authority. The researcher was interested in examining the tax behavior of these SMEs as shown in table 3.1.

Table 3.1 Target Population

Type of Enterprise	**Target Population**
Small Scale Enterprise	1,000
Medium Scale Enterprise	500
Total	**1,500**

Source: Kenya Revenue Authority, 2015

3.4 Sampling size and procedures

The researcher ensured a high degree of correspondence between the sampling frame and the sample population as the accuracy of the sample depends mostly on the sampling frame.

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 in a study is 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 Krejcer and Morgan table was initially used to determine the ideal sample size for this study. For the population of 1,500 taxpayers, 306 would not be an ideal sample size given the time and resources available and also considering the large population. So the researcher used the following formula;

N/kith:

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

Kith item = Every tenth organisation selected in succession from N to form the sample

E.g. If the sample size was 1,500 firms divided by 10 = 150 Organisations.

The study adopted a systematic sampling technique. The respondent selected the first sample unit at random and then the remaining units were automaticaly selected in a definite sequence of the 10th. Hence the respondents were 150.

Table 3.2 Sample Size

Type of Enterprise	**Target Population**	**Sample Size 10%**
Small Scale Enterprise	**1,000**	**100**
Medium Scale Enterprise	**500**	**50**
Total	**1,500**	**150**

3.5 Data collection methods

The study employed primary data collection. Primary data was collected through a self-administered questionnaire. The questionnaire adopted structured open ended as well as closed questions. The responses in the questionnaires helped in gaining an in-depth understanding of the factors influencing tax compliance among SMEs

The research instruments used in this study was a questionnaire and in depth interviews. A questionnaire gathered statistically meaningful data on the perspectives of respondents on an issue of interest based on a set of predetermined questions. The questionnaire had three major sections. The first dealt with the biographic data, the second section dealt with the factors influencing tax compliance while the third section dealt with strategies that can improve tax compliance in Kenya.

3.6 Data collection instruments

The researcher administered the questionnaires assisted by two research assistants. The researcher supervised the assistants and trained them. The researcher endeavored to win the trust of the respondents and allowed the respondents to tell their stories freely to maximize on their self disclosure as it is a sensitive topic in Kenya. During the interview section the researcher targeted selected Business owners, Managing directors, Finance managers and accountants with a lot wealth in taxation matters. The researcher allowed the respondents to tell their stories freely to maximize their self disclosure. In developing the questionnaire items the fixed choice and open ended formats was used. Some items adopted a Likert scale.

In depth interviews belong in philosophical terms to the constructivist or interpretive tradition. These kinds of interviews are functional in collating narratives of subjective realities or experiences.

These interviews contain detailed expressions of the meanings and effect that phenomenon have on respondent. In depth interviews seek to explore the social and human phenomenon by asking the why question (Silverman, 2006). For the interviews, the researcher had predetermined questions grouped together to address particular objectives of the study. Majority of the questions were unstructured, so as to enable the researcher gather as much information as possible in regards to the factors influencing tax compliance among SMEs. Using interview method of data collection ensured that the questions were understood thus minimizing the risk of collecting incomplete and wrong information as it is with questionnaires particularly when people are unable to understand the questions properly. This data collection method was considered by the researcher as appropriate in providing safe basis for generalization and high accuracy.

3.7 Pilot study

3.7.1 Reliability of Research Instrument

Reliability of an instrument is the measure of the degree to which a research instrument yields consistent results or data after repeated trials (Cooper, 2003). To test the reliability of the questionnaire as a research instrument, a test-retest technique was employed in which questionnaires were administering to a group of SMEs with similar characteristics as the actual sample size but not included in the final study. The test was repeated after two weeks. This was to establish the extent to which the questionnaire elicited the same responses every time it is administered. The findings were found to be consistent and therefore the questionnaire proved to be a reliable research instrument.

3.7.2 Validity of Research Instrument

Validity is the degree to which an instrument measures what it is supposed to measure. (Kothari, 2004) Therefore, the term refers to the extent to which an instrument asks the right questions in terms of accuracy. The content validity of the research instrument for this study was determined through piloting, where the responses of the subjects were checked against the research objectives. For a research instrument to be considered valid, the content selected and included in the questionnaire must be relevant to the variable being investigated. The researcher performed the pilot test with a randomly selected sample of fifteen SMEs in Nairobi's Central Business District. Content validity of the instrument was also tested using a research expert's opinion, who was the research supervisor. The research expert independently judged the validity of the items in the questionnaire in relation to research objectives.

3.8 Data collection procedure

Data collection procedures began upon approval of the proposal after its defense. An introduction letter was issued to the sampled entities for consent to collect data from the respondents. The questionnaires were administered to the respondents directly by the researcher with the help of two research assistants in order to save on time. For those respondents who were not available for a sit-in filling of the questionnaire, it was e-mailed to them. The interviews were conducted at a time and place convenient to the respondents to provide an environment in which the respondents would feel free to participate.

3.9 Data Analysis and presentation

A careful analysis of the completed questionnaires was done to ensure that the collected data was accurate and consistent with other information gathered.

Pre-processing of collected data was done through editing to detect errors and omissions and making of corrections where necessary. Data was analyzed by coding according to variables in the study for efficiency so as to reduce the replies given by respondents to a small number of classes. After completion of coding, the data was classified on the basis of common characteristics and attributes. The raw data was then assembled and tabulated in form of statistical tables to allow for further analysis. The Statistical Package for Social Sciences (SPSS) was used to aid in the statistical analysis of the data.

3.8 Measurements of the variables

Table 3.3: Operationalization of Variables

Objective	**Variable**	**Indicator**	**Measurement Scale**	**Tools of Analysis**	**Type of Analysis**
To ascertain the extent to which tax rates explain tax compliance behavior.	Independent	The high tax rate. Stiff tax penalties Several tax heads	Nominal	Mean Percentages	Descriptive statistics
To establish the relationship between availability of tax information and tax compliance by SME's.	Independent	Level of access Knowledge and understanding of Taxation by SME's.	Nominal	Mean Percentages Frequencies	Descriptive Statistics Inferential Statistics
To determine the extent to which tax compliance costs explain tax compliance.	Independent	Cost of hiring staff Cost of record keeping Amount of time and money spent in tax compliance.	Ordinal	Mean Percentages	Descriptive statistics
To determine how attitude of SME's about tax influence tax compliance.	Independent	Access to public goods Peer Attitude and motivation associated with tax compliance.	Ordinal	Percentages Mean	Descriptive Statistics
Government Policies and Regulations	Moderating	Guidelines for registration for tax and tax declaration provided in the law.	Ordinal	Scale	Descriptive Statistics

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSION

4.1 Introduction

This chapter presented the data analysis, presentation and interpretation of findings on the data collected from registered SMEs in Wajir area, based on the factors influencing tax compliance. The main objective of the study was to evaluate the factors that influence the tax compliance among SMEs in Nairobi Industrial area, Kenya. The study sought to answer the research questions: To what extent do tax rate in Kenya explain tax compliance among SMEs?How does the availability of tax information influence tax compliance among SMEs? To what extent do tax compliance costs explain tax compliance among SMEs? How does the attitude of SMEs about tax influence tax compliance? The study sampled 150 registered taxpayers operating within Wajir Area. The data was interpreted as per the research questions.

4.2 Response Rate

The study targeted 150 respondents in collecting data with regard to the factors that influence tax compliance among Small and medium enterprises in Wajir area. Out of the 150 questionnaires issued, 120 were returned, giving an 80% response rate, as shown in Table 4.1. This was commendable given the prejudices which taxpayers normally harbor toward questions relating to their tax affairs. According to Mugenda and Mugenda (2003) a 50% response rate is adequate, 60% good and above 70% is rated very good. This also concurs with (Kothari, 2004) assertion that a response rate of 50% is adequate, while a response rate greater than 70% is very good. This implies that based on these assertions; the response rate for this study, 80% is very good.

Table 4.1: Response Rate

Respondents	Questionnaires Administered	Questionnaires Filled and Returned	Percentage
Total	**150**	**120**	**80**

The positions of the respondents in the organization that constituted the objects of the study were obtained from the closed ended questions with room for specification of any other category of positions not listed. The expected object of this study was limited companies. However certain key individuals had to be interviewed through the questionnaires as the companies are artificial legal persons who cannot respond to questionnaires directly. The results of responses are shown in the frequency Table 4.2.

Table 4.2: Position of respondent in the organization

Position of Respondent	Frequency	Percentage
Business Owner	12	10
Managing Director	18	15
Finance Manager	30	25
Accountant	36	30
Others	24	20
Total	**120**	**100**

Out of the 120 respondents 10% were Business Owners, 15% were managing directors, 25% Finance Managers, 30% Accountants and the remaining 20% were other employees in the organization. 80% of the data was obtained from our focus group. This confirmed the reliability of the data sources as they emanated from key and responsible people in the organizations.

4.3 Demographic information

The study found it of paramount importance to establish the demographic information in order to evaluate the factors that influence tax compliance among SMEs in Wajir area.

4.3.1 Age of Business

The researcher sought to determine the age business under which the respondents fall and the findings are shown in table 4.3.

Table 4.3: Age of Business

Age	Frequency	Percentage
Less than One Year	10	8
1-5	18	15
6-10	28	23
Above 10	64	54
Total	**120**	**100**

The findings revealed that 64 companies are more than 10 years old representing 54% followed by 28 companies representing 23% who are between 6-10 years. The study further revealed that 15% of the companies were aged between 1-5 years and 8% were less than 1 year.

It can therefore be observed from the findings of the study that most of respondents were more than 10 years in existence.

4.3.2 Type of business activity

The respondents were also asked to indicate their main business activity and the findings are presented in table 4.4.

Table 4.4: Composition of business activity type

Type of business activity	Frequency	Percentage
Manufacturing	32	27
Service	28	23
Commercial	48	40
Others	12	10
Total	**120**	**100**

From the study findings as shown in table 4.4, 48 of the respondents representing, 40%, engage in Commercial related activities, 27% were in the service industry, 23% were in the manufacturing industry whereas 10% of the respondents were in the others category.

4.3.3 Monthly turnover

The researcher found it of importance to ask the respondents to indicate their business' average monthly turnover, as this is the factor also identifies the category under which a taxpayer falls consequently determining whether the respondents can be classified as either small or medium enterprise Taxpayers. Table 4.5 shows the results of the findings.

Table 4.5: Monthly turnover

Monthly turnover	Frequency	Percentage
Below Ksh500,000	5	4
Between Ksh500,001 and Ksh1 million	12	10
Between Ksh1,000,001 and Ksh2 million	20	17
Between Ksh2,000,001 million and Ksh3 million	25	21
Over Ksh3 million	58	48
Total	**120**	**100**

58 Respondents with a monthly turnover of over Ksh3 million accounted for 48%, followed in a distance by 25 respondent representing 21% who revealed they had monthly turnover of between Ksh 2 million and 3 million while 17% indicated that their monthly turnover is between Ksh1 million and Ksh 2 Million. The study further revealed that 10% had a monthly turnover of between Ksh 500,000 and Ksh 1 million and 4% below 500,000.

4.3.4 Personal Identification Number

The researcher inquired as to whether the respondents' business had a PIN. This was to determine that the businesses are registered for tax purposes as the PIN is a mandatory requirement for all operating businesses. The findings are presented in table 4.6.

Table 4.6: Number of respondents with PIN

Respondents with PIN	Frequency	Percentage
Yes	120	100
No	0	0
Total	**120**	**100**

As shown in table 4.6, 100% of the businesses have a personal identification number. This was quite commendable as it shows that all the organisations that participated in the survey are duly registered for tax purposes.

4.3.5 Number of Employees

The study sought to find out the number of staff employed in the organizations as illustrated in table 4.7.

Table 4.7: Number of employees in the organization

Number of Employees	Frequency	Percentage
Below 20	38	32
Between 21 and 40	35	29
Between 41 and 50	22	18
Between 51 and 80	15	13
Between 81 and 100	10	8
Total	**120**	**100**

The findings indicate that 38 of the SMEs who responded had the number of staff employed in their organization below 20. This was 32% followed by organizations with 21-40 employees representing 29%. The findings indicate that 18% of the respondents had 41-50 employees, 13% had 51-80 employees whereas 8% of the SMEs organization had 81-100 employees.

4.4 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 tale 4.2 below.

Table 4.8: Reliability tests results

Constructs	Reliability Cronbach's alpha	No of Items	Comment
Tax rates	0.773	6	Accepted
Tax information	0.831	6	Accepted
Compliance cost	0.781	6	Accepted
Taxpayers attitudes	0.765	6	Accepted

The results of the reliability test produced an overall Cronbach Alpha correlation coefficient of 0.733 while specific findings indicated that, tax rates had a coefficient of 0.773, tax information had a coefficient of 0.831, Compliance cost had a coefficient of 0.781, taxpayers attitudes had a coefficient of 0.833 and Tax compliance had a coefficient of 0.790. 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 tax compliance at Wajir.

4.4 Description statistics

4.5.1 Tax rates

It is generally believed that a high tax rate is the main cause of tax evasion. Incentives to evade tax depend on the marginal rates of taxation because these govern the gains from evasion as a sum of the sum evaded (Kaldor, 1956). The researcher sought to find out the extent to which tax rates in Kenya explain tax compliance among SMEs.

(a) ASMEs Perception of Kenyan tax rates

The researcher enquired as to whether the SMEs found the tax rates in Kenya high. The findings are presented in table 4.8.

Table 4.8: Perception of Kenyan tax rates

Perception of tax rate	Frequency	Percentage
The tax rates are high.	86	72
The tax rates are not high.	34	28
Total	**120**	**100**

86 organisations out of 120 which is 72% of the respondents think that the tax rates in Kenya are high while those who do not think that it is high were a minority and accounted for only 28%. It can therefore be deduced that to the majority of SMEs find the tax rates high.

(b) SMEs Perception of the different types of taxes

The other aspect reviewed in the study is whether they are many different types of taxes that are usually payable to KRA. The results of the study are shown in Table 4.9.

Table 4.9: Perception of forms of taxes

Perception	Frequency	Percentage
They are several types of taxes.	116	97
The taxes are not too many.	4	3
Total	**120**	**100**

The results of the study showed that 97% of the respondents felt that the tax heads are too many, while only 3% felt otherwise. This is a clear indicator that majority of SMEs feel that the number and types of taxes demanded from them are too many.

(c) Tax amount payable as a factor influencing SMEs tax compliance

The researcher sought to determine whether the SMEs compliance is influenced by the amount of tax to be paid. The findings are presented in table 4.10.

Table 4.10: Assessment of tax amount payable as a factor influencing tax compliance

Opinion	Frequency	Percentage
Tax amount to be paid influences compliance.	73	61
Tax amount to be paid does not influence compliance.	47	39
Total	**120**	**100**

73 out of 120 of respondents said the amount of tax payable does influence their level of tax compliance. They accounted for 61% of the respondents and the remainder 39% felt the amount payable does not influence tax compliance. The study can therefore conclude that to the majority of the SMEs, their level of compliance is greatly influenced by the tax amount due to KRA.

4.5.2 Availability of Tax Information

The concept of tax information was developed through the literature review in chapter two of this study and was conceptualized to mean the level of information at the disposal of the taxpayers to enable them comply voluntarily without prompting by the KRA officials. The study looked at whether information about taxes was readily available to the taxpayers and how this availability of information affects tax compliance and whether an organization is able to calculate it taxes correctly based on the information that has been disseminated.

(a) Ready availability of Information

The survey sought to find out whether the respondents find information relating to tax matters readily available and how to go about it. The findings are shown as per the results in table 4.11.

Table 4.11: Ready availability of tax information

Availability of Information	Frequency	Percentage
Information is readily available.	33	27
Information is not readily available	87	73
Total	**120**	**100**

The study findings indicate that out of the 120 SMEs, 87 of the respondents feel that information relating to tax information is not readily available while a small percentage of 27.5% representing 33 of the respondents find that information is readily available.

(b) How tax information affects SMEs tax compliance

The respondents were requested to indicate whether the lack of or availability thereof of tax information affects tax compliance. The findings are presented in table 4.12.

Table 4.12: Extent to which lack of tax information affects tax compliance

Opinion	Frequency	Percentage
Not at all	5	4
Less Extent	13	11
Some Extent	32	27
Great Extent	40	33
Very Great extent	30	25
Total	**120**	**100**

The results as shown in table 4.12 revealed that 25% of the respondents agreed that the lack of tax information affects their level of tax compliance to a very great extent. 33% of the respondents felt that their level of tax compliance was affected to a great extent by lack of tax information. This was followed by 27% who felt it was to some extent, 11% to a less extent and 4% not at all. It is therefore clear that for the majority of SMEs, the lack of tax information affects tax compliance to a very great extent

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(c) Correct calculation of taxes based on available information

The study sought to establish whether SMEs are able to correctly calculate the taxes based on the available information. This was in a bid to determine whether the level of information relating to taxes affect tax compliance. Table 4.13 presents the findings.

Table 4.13: Correct calculation of taxes

Opinion	Frequency	Percentage
We calculate the correct taxes.	31	26
We do not calculate the correct taxes.	21	17
We are not sure.	68	57
Total	**120**	**100**

The results of the findings as shown in table 4.13 revealed that 57% of the respondents are not sure whether they calculate the correct taxes, 26% felt they are able to correctly calculate taxes due from them while 17% feel that they do not calculate the correct taxes, all based on the availability of tax information at their disposal.

Information relating to tax available to SMEs, the majority of taxpayers are not able to correctly calculate tax due from them and may hence end up paying the incorrect amount.

4.5.3 Tax Compliance cost

In most developing countries including Kenya, hiring tax professionals is an added cost to the SME's (Group, 2010) and they therefore resort to doing their own tax returns, though they may not be well versed with taxation and the concept of filing returns. The cost of book keeping and recordkeeping is also a major cost to most SMEs. It is in this regard that this research sought to find out how compliance costs incurred by SMEs affect the amount of taxes remitted to KRA by these organizations.

(a) Monthly cost of compliance

The researcher found it of importance to find out on average how much an organization spends monthly in compliance cost. This is a key indicator to find out whether the cost is too high hence affecting their compliance levels. Table 4.14 shows the results of the findings.

Table 4.14: Monthly cost of compliance

Compliance Cost	Frequency	Percentage
Below Ksh 10,000	8	7
Between Ksh10,001 and Ksh50,000	15	12
Between Ksh 50,001 and Ksh 100,000	56	47
Over Ksh 100,000	41	34
Total	**120**	**100**

56 of the respondents with a monthly cost of between Ksh 50,001 and 100,000 accounted for 47%, followed by 34% who revealed they had monthly cost of over Ksh 100,000 while 12% indicated that their monthly cost is between Ksh10, 000 and Ksh 50,000. The study further revealed that only a meagre 7% had a monthly cost of below Ksh 10,000.

(b) How cost of compliance affects tax compliance

The respondents were requested to indicate whether the total cost incurred in being compliant affects their tax compliance as an organization. The findings are presented in table 4.15.

Table 4.15: Extent to which tax compliance cost affects tax compliance

Extent	Frequency	Percentage
Not at all	7	6
Less Extent	16	13
Some Extent	28	23
Great Extent	48	40
Very Great extent	21	18
Total	**120**	**100**

The results as shown in table 4.15 revealed that 40% of the respondents of the study agreed that the costs they incurred in being compliant affected their compliance levels to a very great extent. For 23% of the respondents, it was to some extent followed by 18% who felt that it was to a very great extent, 13% to a less extent and 6% not at all. It can therefore be deduced that for the majority of SMEs, the costs they incurred in tax compliance affects their compliance levels to a very great extent.

(c) Analysis of the various tax compliance costs

The respondents were requested to compare and indicate what they felt formed the highest tax compliance cost was. The findings are shown in table 4.16.

Table 4.16: Comparison of tax compliance cost

Cost	Frequency	Percentage
Hiring of Staff	45	38
Book Keeping	60	50
Software and internet	15	12
Total	**120**	**100**

60 of the respondents (50%) revealed that book keeping took the lion's share of its expenses among the compliance cost, This was followed closely by the hiring of professional staff at 38% at a distant third was the cost of software and internet usage at 12%.

4.5.4 SMEs attitude about tax

The concept of attitude was reviewed through the literature review and interpreted to mean the measure of confidence a taxpayer has in a tax system. When a taxpayer feels there is unfairness in a tax system, the voluntary tax compliance becomes replaced with intentional tax evasion. The study therefore sought to examine how attitude about tax affects the income tax compliance of SMEs in Wajir area. The aspects looked at in this study include the extent of access by companies to public utilities financed by taxes, the value companies attach to the responsibility of paying taxes to the government, and the main reasons for the various attitudinal positions taken by the companies.

(a) Access to public utilities and services

The study showed the results in respect of the extent to which access public utilities financed taxes as outlined in Table 4.17.

Table 4.17: Extent of access to public utilities and services funded by tax

Opinion	Frequency	Percentage
Not at all	14	11
Less Extent	36	30
Some Extent	42	35
Great Extent	20	17
Very Great extent	8	7
Total	**120**	**100**

The results of the study were that 35% of the respondents felt that they had access to public utilities financed by the funds collected from taxes to some extent. 30% of the respondents felt that they access to public utilities to a less extent, and 17% of the respondents felt that they had to a great extent, 11% not at all while 7% to a great extent access to public utilities financed by fund generated from taxes. The expectation of the study was that when the extent of access to public utilities by companies is high then the level of voluntary income tax compliance will be enhanced greatly. In this study only 59% accessed the public utilities to some, great and very great extent.

(b) Value the company places on payment of taxes

The other aspect examined was the extent which SMEs value the payment of income tax to the Kenyan government. The results of the study were as per table 4.18.

Table 4.18: Extent to which companies value payment of tax to Kenyan government

Opinion	Frequency	Percentage
Not at all	3	2
Less Extent	12	10
Some Extent	24	20
Great Extent	67	56
Very Great extent	14	12
Total	**120**	**100**

The results as shown in table 4.18 revealed that 56% of the respondents value payment of taxes to the government to a great extent.20% to some extent. The study further revealed that for 12% it is to a very great extent, 10% to a less extent and 2% not at all. The expectation of the study was that companies' voluntary compliance would be high when companies attach a lot of value to the payment of taxes to the government. In this study 88% attach value to some, great and very great extent to the payment of taxes to the government of Kenya. Thus we can conclude that most SMEs do value payment of taxes.

(c) Respondents view on the value other SMEs places on payment of taxes

The other aspect examined was the extent which the respondent viewed how other SMEs value the payment of income tax to the Kenyan government. The results of the study were as per table 4.19.

Table 4.19: Extent other SMEs value payment of tax to Kenyan government

Opinion	Frequency	Percentage
Not at all	10	8
Less Extent	16	13
Some Extent	56	47
Great Extent	32	27
Very Great extent	6	5
Total	**120**	**100**

The study found out that 56 (47%) of the respondents view that other SMEs value payment of taxes to the government to some extent, 27% to a great extent. The study further revealed that 13% to a less extent, 8% not at all and 5% to a very great extent. We can conclude most respondents view other SMEs do value payment of taxes

4.6 Correlation Matrix

4.5.1 Correlation results on independent variables

Correlation shows the relationship existing between variables in the study. The study's dependent variable is Tax compliance tax compliance and the independent variables consist of Tax rate, Tax information, compliance cost and SMEs attitudes

Table 4.20: Correlation between independent variable and dependent variable

Variables		**Tax compliance**	**Tax rates**	**Tax information**	**SME attitudes**
Tax compliance	Pearson Correlation	**1**			
	Sig. (2-tailed)				
Tax rates	Pearson Correlation	0.456	1		
	Sig. (2-tailed)	0.002			
Tax information	Pearson Correlation	0.431	.3421	1	
	Sig. (2-tailed)	0.001	.0014		
SMEs attitudes	Pearson Correlation	0.431,	.3120	.0000	1
	Sig. (2-tailed)	0.000	.0031	1.000	

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 4.20 it was clear that there was a positive correlation between tax compliance and tax rates as depicted by a correlation value of 0.456. This implies that tax rates was linearly related to tax compliance. The study also depicted that there is a positive correlation between tax information and tax compliance with a correlation value of 0.431. Another positive correlation was between compliance cost and tax compliance with a correlation value of 0.458 and a positive correlation between tax compliance costs and tax compliance with a correlation value of 0.431. This shows that there was a positive correlation between tax compliance cost, tax information, tax rates, SMEs attitudes and tax compliance.

4.6 Regression Analysis

4.5.1 Model Summary

Table 4.21 model summary results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.539a	.291	.202	.71664

a. Predictors: (Constant), Tax rates, Tax information, Compliance costs and SMEs attitudes

Table 4.21 shows that R-Square value (coefficient of determination) is 0.291, which indicates that the independent variables (tax rates, tax information, compliance costs and SMEs attitudes) explain 29.1% of the variation in the dependent variable (tax compliance). This means that 70.9% of tax compliance is influenced by other factors apart from the considered research variables.

4.7 Analysis of Variance

The results of the Analysis of variance are shown by table 4.10 below

Table 4.22 ANOVA

Model	Sum of Ssquares	Df	Mean Square	F	Sig
1 Regression Residual Total	8.414 20.543 28.957	5 40 45	1.683 .514	3.277	.014b

a. Dependent Variable: Tax compliance
b. Predictors: (Constant), Tax rates, Tax information, Compliance cost and SMEs attitudes

ANOVA results on table 4.7 shows regression model is significant since the F statistics value (3.277) is significant at 95% confidence level since the p-value ($0.014<0.05$). This indicate a significant relation between independent research variables tax rates, tax information, compliance cost, SMEs attitudes and tax compliance.

4.8 Regression Coefficients

Table 4.23 below shows the regression coefficients results.

Table 4.23 Regression Coefficients

Model		**Unstandardized Coefficients**		**Standardized Coefficients**	t	**sig**
		B Error	**Std.**	**Beta**		
1	(Constant)	1.490	0.745		1.999	0.052
	Tax rates	-0.148	0.184	-0.121	-0.804	0.426
	Tax information	0.522	0.211	0.373	2.476	0.018
	Compliance cost	0.170	0.184	0.132	0.920	0.363
	SMEs attitudes	0.167	0.180	0.321	0.543	0.231

a.Dependent Variable: Tax compliance

From results on table 4.11 the following regression equation was obtained

$Y=1.490+-0.148_{X1+}+0.522_{X2}+0.170_{X3+}\ 0.167_{X4}\ _{+}\varepsilon$

The coefficient for tax rates is -0.148, so we expect a -0.148 unit decrease in the tax compliance holding all other variables constant. The coefficient for tax information is 0.522 so for every unit increase in tax information, we expect 0.52 point increase in tax compliance. For compliance cost, is represented by a coefficient of 0.170, meaning for every increase in compliance cost a 0.17-unit increase in tax compliance is predicted holding all other variables constant and SMEs attitudes is 0.167 so every unit increase in SMEs attitudes we expect 0.17 unit increase in tax compliance. From the table 4.23 t and sig are the t-statistics and their associated values used in testing whether a given coefficient is significantly different from zero using an alpha of 0.05.

The coefficient for tax rates -0.148 is not significantly different from 0 because its p-value is 0.426,which is larger than 0.05.

This means that for any decrease in fines and penalties independent variables at 0 leads to -0.148 decrease in rental income tax compliance. This implies that fines and penalties greatly discourage compliance l of real estate investors and very punitive to real estate investors.

Further coefficient for tax information is 0.522 which is statically significant because its p-value of 0.017 is less than 0.05. tax information has positive influence on real estate investors compliance level since for any increase of 0.522 leads to increase in real estate investors compliance level. This also implies that by KRA creating a lot of public awareness on tax compliance positively.

Compliance cost coefficient of 0.170 is not significantly different from 0 because its p-value is 0.363 which is larger than 0.05.Meaning compliance cost has significant and positively influences compliance level. A unit increase of compliance cost by 0.170 leads to the same increase in ompliance level, for instance hiring of auditors for the purpose of filing cost less has a positive influence in tax compliance The intercept is significantly different from 0 at the 0.05 alpha level.

4.9 Discussion of the key Findings

The study result found a significant positive relation between tax rates, tax information, compliance cost, SMEs attitudes and tax compliance among SMEs.

Maseko (2014) investigated the impact of personal tax knowledge and tax compliance costs behavior of SMEs in Zimbabwe. The findings of the study revealed that unlike large companies, SMEs face different business conditions which make them to endure high tax compliance load.

4.9.1 Tax rates

Finally, the results have found that, tax rates negatively influence tax compliance but the relationship is insignificant.

This indicates an inverse relationship between tax rates and tax compliance among SMEs that indicates that a decrease in tax rates reduces tax compliance. Thananga, Wanyoike and Wagoki (2013) carried out a study on how landlords in Nakuru Municipality responded to new taxation measures, and factors which influence compliance. The study used a sample of 94 respondents and questionnaires for data collection.

With regard to tax rate, majority of the respondents do think that the tax rates are high in Kenya and that there are many different types of taxes demanded from them and this also hinders tax compliance. 61% of the respondents feel that the amount of tax to be paid by them greatly influences their level of tax compliance

4.9.2 Tax information

The findings also mean Tax information has a direct impact on tax compliance hence an increase in tax information of tax increases the levels of tax compliance among SMEs. Kołodziej (2011), support that a high compliance cost could be seen as an unfair treatment of taxpayers. The findings of the study revealed that with regard to availability of tax information, 73% of the respondents' view that information relating to tax matters is not readily available to them. This accounted for the majority who further feel that the lack of readily available information affects their tax compliance to a great extent.

This challenge in accessing information translates to 57% of the respondents of the study feeling that they, in all honesty, are not sure that they do correctly calculate the amount of tax payable by them and hence may be a factor influencing their tax compliance. For the majority of the SMEs who participated in this study, majority spend between Ksh 50,000 and Ksh 100,000 monthly in tax compliance. Book keeping costs formed the highest expenditure in terms of tax compliance.

They do feel that the tax compliance costs affect their level of tax compliance to a great extent. Majority of the respondents feel that they have access to public utilities to some extent and value the payment of taxes to the government. Furthermore, they also feel that their counterparts in the SME industry do value the payment of taxes to some extent. It is the feeling of the large proportion of respondents of this research that they strongly agree that the tax system in Kenya needs to be improved

4.9.3 Compliance cost

Compliance cost coefficient of 0.170 is not significantly different from 0 because its p-value is 0.363 which is larger than 0.05.Meaning compliance cost has significant and positively influences tax compliance. A unit increase of compliance cost by 0.170 leads to the same increase in tax compliance, for instance hiring of auditors for the purpose of filing cost less has a positive influence in real estate investors compliance level. The intercept is significantly different from 0 at the 0.05 alpha level

4.9.2 SMEs attitudes

The findings also mean SMEs attitudes has a direct impact on tax compliance hence an increase in SMEs attitudes of tax increases the levels of tax compliance among SMEs. Kołodziej (2011), support that a high compliance cost could be seen as an unfair treatment of taxpayers.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATION

5.1 Introduction

In this chapter the research findings were summarized, then conclusion and recommendations to the study are drawn and research gaps are identified for future studies as the study aimed at determining factors influencing tax compliance among SMEs in Wajir area, Kenya.

5.2 Summary of findings

5.2.1 Tax rates

The results showed that SMEs feel that tax rates for the already several tax heads, that is, corporate tax, VAT and Pay As You Earn (PAYE) are either high or very high. A high tax rate erodes taxpayer's earnings and disposable incomes thus will have a negative effect on consumption and investments. It will also encourage tax avoidance and evasion as the opportunity cost to evade is high. This may be an expected reaction from taxpayers as no single taxpayer can rate a tax rate as 'low'. There is also the problem of defining the line between 'high', 'low' and 'fair'. The findings of this study do therefore agree with those of other researchers as discussed in the literature review. As interest rates go higher, the opportunity cost to evade becomes higher and thus taxpayers get tempted to evade. (Friedland, 1978). Kenya's tax rates compare favorably with that of her neighbors, Uganda and Tanzania, who charge the same rates for corporate tax, withholding tax and VAT.

However, given the large percentage of respondents who feel that they are high, there is need to revise these rates and make them more attractive to them.

The respondents rate the current penalties as ‘very high’ or ‘high’. This is true for VAT and income tax. The respondents observe that the present 2% per month interest is extremely high and punitive to allow any organization to effect payments. Sometimes penalties and interest alone are higher than the principal tax. Penalties and interest arise out of late filing of returns and non-payment of taxes and non-disclosure of taxable income which is discovered during audit. Given the self-assessment system, audits can only be done after returns have been submitted. Hence there is some lapse of time from the time a return is submitted and the time when audit is carried out. Interest starts accruing from due date of the tax until the time an audit is complete. The penalty and interest rates are specified in the respective Acts. Since these are legislative requirements, KRA can only act to reduce interest by carrying out audits more frequently and at regular intervals. The other option is to change law and thus lower rates. Studies done show that high penalties increase compliance but marginally (Alm, 2001).

5.2.2 Tax information

The findings of this study revealed that majority of the respondents have a challenge in accessing information about taxes. As earlier discussed in the literature review section of this study, less educated tax payers are less exposed to tax compliance information and are less informed about relevant tax compliance information and thus are more prone to tax evasion. Some tax payers find the complexity of tax information more difficult to understand than others. This complexity may lead to unintentional non compliance if tax payers have problems maybe in filling of tax returns. SMEs generally find the information given by KRA fairly inadequate to enable them complete the tax returns expected from them. Some find the process to be complicated; requiring too much information thus a waste of time and resources, it is thus clear that there is a strong case for improvement of the information available. Majority of the respondents are in agreement that Taxpayer Education/Seminars plays a positive role in enhancing tax compliance.

Taxpayer education is one of the powerful tools of enhancing compliance. At this forum, knowledge is passed to taxpayers exhaustively and this enhances future compliance and through this knowledge the taxpayer is able to know the various rights and obligations accruing from services offered by KRA. Communication channels open up and this enhances friendly relations between the taxpayer and the tax authority. Consequently, taxpayers also feel part and parcel of the policy making process. KRA should strive to open 'Help' counters and website for taxpayers to seek help in dispensing information. Well-trained and knowledgeable staff should man the counters. They should also enhance taxpayer education and remove the ambiguities in the VAT and Income Tax Acts.

5.2.3 Tax Compliance Cost

High compliance costs can result in tax avoidance, tax fraud, and inhibit investment by way of diminishing competitiveness of the country in terms of taxation attractiveness. (Ojeka, 2012).The respondents of this study feel that consultancy charges and the cost of hiring professional staff is expensive. Concerning the book keeping issues, it can be concluded that many SMEs resort to engaging professional tax consultants to be able accomplish the statutory requirement to accompany annual returns with audited accounts, and at the same time a good number of companies have computerized their accounting system to go around the requirement. All these efforts do amount to some cost borne by the taxpayer, and since there is a positive correlation between book keeping and income tax compliance; the government can endeavor to improve compliance by promoting sound accounting practices. Compliance costs, in form of fees charged by tax consultants, are positively correlated with noncompliance behavior and thus negatively correlated with tax compliance behavior. Obtaining a tax clearance certificate is the highest motivation to comply with tax laws and regulations for most SME operators in Kenya. Because of the perceived technical nature of return filing, most taxpayers are forced to employ professional tax consultants.

The Acts are legal documents with legal language which is complicated for ordinary taxpayers to comprehend and given the numerous legal amendments every year, taxpayers lack the necessary expertise to complete the tax returns. It also saves time and money by engaging a tax consultant to complete the return in the most efficient manner. However, few taxpayers can afford such professional services and in most cases hire non-professional agents like family members and friends. These sub-standard agents charge moderate fees but offer unprofessional services that result in misrepresentation of the business records/status.

5.2.4 Taxpayers Attitude towards tax

In terms of attitude of taxpayers toward payment of taxes to the government it can be concluded that majority of the companies had at least some access to the public utilities financed by taxes while at the same time valued the payment of taxes to the government of Kenya .This factor can be exploited to improve income tax compliance. With regards to perceptions of bureaucracy and corruption by tax administrators and government spending, those who engage in tax evasion often justify such behavior by suggesting that the government wastes tax revenue and spends unwisely; such arguments can decrease voluntary compliance in the long run (Braithwaite, 2009) It is expected that if the government spends taxpayers' money wisely, for example on basic facilities like education, health and safety and public transportation, it is assumed that voluntary compliance will increase. In contrast, if taxpayers perceive that the government spends too much on something else, taxpayers might feel betrayed and attempt to evade. In judging their own behavior, people tend to believe the cause is due to external attributes and cannot be tax compliant. Therefore, the government should spend taxpayers' money wisely so that tax compliance will increase, thus the tax collection will also increase.

5.3 Conclusions

Findings from the study reveal that all the identified factors have a direct influence on the tax compliance among SMEs. The tax compliance factors examined included tax rates, availability of tax information, tax compliance cost, and attitude of taxpayers toward payment of income tax.

5.3.1 Tax rates

The study confirmed that KRA why uses both voluntary tax compliance strategy alongside the deterrent measures strategy. Most of the respondents felt the tax rates should be reviewed, thus the government should relook at the tax rates currently charged to SMEs.

5.3.2 Tax information

On availability of tax information, information received by taxpayers is an important factor that contributes to their understanding of tax responsibilities, especially regarding registration and filing requirements. KRA should address the complexities of annual tax returns, periodic variations in the tax laws, and levels of penalties and fines. They should pass this information regularly to SMEs via various channels like tax Seminars, Booklets and Media Channels. This will greatly improve the SMEs level of compliance as the great complexity associated with tax matters will be demystified.

5.3.3 Compliance cost

On tax compliance cost, the companies confirmed to engaging the services of tax agents and professional staff to handle accounting issues. This cost is normally a burden to the SMEs.

SMES should be encouraged to improve their bookkeeping by offering incentives, such as application of a lower presumptive tax rate for small businesses meeting certain recordkeeping standards. The government should also engage the small holders in sensitization forums on how to reduce the cost associated with tax compliance

5.3.4 SMEs attitudes

With regard to the attitude of taxpayers toward payment of taxes to the government, the study revealed that most of the companies felt they had at least some access to the public utilities financed by taxes while at the same time valued the payment of taxes to the government of Kenya .Taxpayers' attitudes encourages tax compliance in Kenya and what influence the taxpayers' attitudes, equally affect the taxpayers' compliance with the tax requirement i.e. taxpayers' attitudes encourages tax compliance in Kenya.

5.4 Recommendations of the study

Based on the findings of this study, the researcher came up with several recommendations to encourage tax compliance among SMEs. These include;

(a) Tax rates and penalty rates

Consider lowering the tax rates to enhance collections. Lower tax rates make it less attractive to evade taxes as opposed to high rates. High penalty rates will increase compliance but only marginally. This penalty rates should be kept at an optimum level not to discourage taxpayers. Also consider uniform penalty rates for all tax heads.

(b) Tax Return forms

The returns ought to be simplified and accompanying notes reconstructed into plain language that can be understood by all taxpayers. They should also be clear and brief but complete in detail to enable the taxpayers fill the return. In addition, where possible, simple computed examples should be incorporated in the notes.

(c) Taxpayer education

To enhance compliance there is need to intensify taxpayer education in terms of increasing the number of sessions and broadening coverage to include tax consultants. This will enlighten the taxpayers on existing law and any other tax liability. This will also provide a forum for taxpayers to air their complaints and or compliments

(d) Audits

Increased rates of audits that seek to reduce the time between audits will improve compliance, as taxpayers will fear the risk of being audited and penalized. The audits should also be broadened to cover a wider area with a possibility of conducting joint income tax and VAT audits based on modern audit tools. These measures are expected to result in enhanced tax collection improved sharing of information and time saving both to the authority and to the taxpayers. The criteria for selection of files for audits should be based on information given in returns and not random or subjective selection. This will make audits more productive and informative.

(e) Improved Services

The authority should strive to give taxpayers high quality services as stipulated in the corporate plan. Most of the services provided by the authority like refunds, remissions and dispute resolutions were rated poor and thus there is every reason to improve them. Where possible, officers should endeavor to adhere to the taxpayers' charter in terms of service provision to taxpayers. 'Help' counters manned by technical and knowledgeable staff should be introduced and enhanced throughout the authority's offices to bring services closer to the taxpayers. This will also improve communication between the taxpayers and the authority. Other services worth introducing include payment of VAT directly into the banks- as is the case with PAYE, and modern technology such as telephone exchanges.

(f)Training

There is need to continuously train technical staff to keep abreast with the tax law and any other changes therein. This way, the officers will impart proper and correct advice to taxpayers during the time of audits. Customer care lessons should form an integral part of this training. Recruitment of new taxpayers by the authority should be intensified and enhanced. This will broaden the tax base and reduce pressure on the complying taxpayers

5.6 Suggestions for further research

This study proposes the following areas for further study:

- Factors affecting income tax compliance among SMEs in other regions of Kenya.
- A study on the relationship between voluntary tax compliance strategy and the deterrence measures kind of strategy.
- Factors that motivate SMEs to be tax compliant.

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APPENDICES

APPENDIX I: LETTER OF TRANSMITTAL

Muktar Yaro
P.O Box 27033-00100
Nairobi, Kenya.

Dear Respondent,

I am a student of the University of Nairobi pursuing a Master of Arts Degree in Project Planning and Management. I am conducting academic research on the factors promoting tax compliance among SME's in Nairobi. I'm writing to invite you to participate in the research by filling in the questionnaire.

My research project focuses on tax rate, tax information, tax compliance costs and taxpayers' attitude. The questionnaire should take about 30 minutes to complete. Your participation is entirely voluntary and the questionnaire is completely anonymous.

I wish to assure you that the information you will provide will be treated with utmost confidentiality. Your ability to answer all the questions comprehensively and to the best of your knowledge will be highly appreciated.

I look forward to your support.

Thank you.

Yours Sincerely,

Muktor Yoru
Tel: 0720-897-944

APPENDIX II: QUESTIONNAIRE

Instructions

This questionnaire is designed to collect information on the factors affecting tax compliance in SMEs in Wajir Area, Kenya. The information obtained will only be used for academic purposes and shall be treated in utmost confidence. You are requested to complete this questionnaire as honestly and objectively as possible.

Please tick in the appropriate box and also fill in the blank spaces provided for those questions where elaborate answers are required. Use the space at the back of this questionnaire if you need more space for your responses.

SECTION A: GENERAL INFORMATION

1. Name of SME (Optional)..

2. Position of respondent in the organization.

Business Owner ☐
Managing Directors ☐
Finance Managers ☐
Accountant ☐
Others (Specify)……………………………………………….

3. How long has the organization been in existence?

Less than One year ☐
1-5 Years ☐
6-10 Years ☐
More than 10 Years ☐

4. What is your main business activity?

………………………………………………………………………………………………
………………………………………………………………………………………………

1. What is the Nature of your Business?

Manufacturing ☐
Service ☐
Commercial ☐
Others(Specify) ☐
…………………………………………………………………

6. On average, what is your business ‘monthly turnover?

Below Ksh 500, 000 [ ]

Between Ksh 500,001 and Ksh 1 Million [ ]

Between Ksh 1,000,001 and Ksh 2 Million [ ]

Between Ksh 2,000,001 and Ksh 3 Million [ ]

Over Ksh 3 million [ ]

7. Does your business have a Personal Identification Number (PIN)?

[Y] Yes [ ] No

8. Number of employees in the MSE

Below 20 [ ]

Between 21 and 40 [ ]

Between 41 and 50 [ ]

Between 51 and 80 [ ]

Between 81 and 100 [ ]

SECTION B: FACTORS INFLUENCING TAX COMPLIANCE AMONG

SMEs Tax Rates

1. Do you think the Kenyan tax rates are high?

Yes [ ] No [ ]

2. Do you think there are too many different forms of taxes in Kenya?

Yes [ ] No [ ]

2. Is the amount payable in terms of taxes influence your tax compliance?

Yes [ ] No [ ]

Availability of tax information

Tick or circle where appropriate) {Note: [1] = Not at all, [2] = Less extent, [3] = Some extent, [4] = Great extent, [5] =Very Great extent}

3. Is Information about taxes in Kenya readily available?

Yes [ ] No [ ]

2. How does the lack of tax information affect your company's tax compliance?

[1] [2] [3] [4] [5]

3. As an organization we are able to correctly calculate the tax amount payable based on available information.

Yes [ ] No [ ] Not sure [ ]

Tax Compliance Cost

Tick or circle where appropriate) {Note: [1] = Not at all, [2] = Less extent, [3] = Some extent, [4] = Great extent, [5] =Very Great extent}

4. On average how much do you spend in a month in order to be tax compliant?

Below Ksh 10, 000	☐
Between Ksh 10,001 and Ksh 50,000	☐
Between Ksh 50,001 and Ksh 100,000	☐
Over Ksh 100,000	☐

5. How does the cost of compliance affect your company's tax compliance?

[1] [2] [3] [4] [5]

6. Which of the following expenses constitute the highest tax compliance cost? Cost of Employing professional staff

Book Keeping

Software and Internet

Attitude towards tax

Tick or circle where appropriate) {Note: [1] = Not at all, [2] = Less extent, [3] = Some extent, [4] = Great extent, [5] =Very Great extent}

7. To what extent does your company receive access to public utilities and services funded by the taxes collected for the government by the KRA?

[1] [2] [3] [4] [5]

10. To what extent, in your opinion, does your company value the payment of taxes to the Kenyan government?

[1] [2] [3] [4] [5]

11. To what extent do you view other SMEs value the payment of taxes?

[1] [2] [3] [4] [5]

SECTION C: STRATEGIES THAT CAN IMPROVE TAX COMPLIANCE AMONG SMEs

1. Are there strategies that can improve the tax compliance by SMEs in Kenya? If so kindly list them down

   ....
   ....
   ....
   ....
   ....

2. Is there a need to improve the Kenya's tax system

Strongly Agree	☐	Agree	☐
Not Sure	☐	Disagree	☐
Strongly Disagree	☐		

3. What other challenges do you view affect the tax compliance among SMEs?

…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………………………………………………………..

4. Please give recommendations of how these challenges can be addressed.

…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………………………………………………………

APPENDIX III: INDEPTH INTERVIEW GUIDE

1. What kind of experiences have you had with KRA?
2. What things would you make you be willing to pay tax regularly and in full?
3. What things discourage you from meeting your tax obligations?
4. What factors do you think promote tax compliance among SMEs in Kenya?
5. What is your take on online filling of returns?
6. What would you wish the KRA would do in order to understand your business?

APPENDIX IV: KREJCIE AND MORGAN TABLE FOR DETERMINING THE SAMPLE SIZE

N	S	N	S	N	S	N	S	N	S
10	10	100	80	280	162	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	246
25	24	130	97	320	175	950	274	4000	351
30	28	140	103	340	181	1000	278	4500	351
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	181	1200	291	6000	361
45	40	180	118	400	196	1300	297	7000	364
50	44	190	123	420	201	1400	302	8000	367
55	48	200	127	440	205	1500	306	9000	368
60	52	210	132	460	210	1600	310	10000	373
65	56	220	136	480	214	1700	313	15000	375
70	59	230	140	500	217	1800	317	20000	377
75	63	240	144	550	225	1900	320	30000	379

80	66	250	148	600	234	2000	322	40000	380
85	70	260	152	650	242	2200	327	50000	381
90	73	270	155	700	248	2400	331	75000	382
95	76	270	159	750	256	2600	335	100000	384

Note: "N" is population size

"S" is sample size.

Source: (Krejcie, 1970)

A**PPENDIX 111: BUDGET**

DESCRIPTION	COST PER ITEM	TOTAL AMOUNT (Kshs)
Stationery Photocopying papers Pens, pencils, rubbers Ink cartridge (Printer) Files (12 rim binders)	 10 reams @600/=	**20,000.00**
Personnel Questionnaires administrators Stastician		**20,000.00**
Transport and subsistence Vehicles Subsistence allowance		**10,000.00**
Communication Telephone Internet		**20,000.00**
Other Services Library services Purchase of periodicals and books		**20,000.00**
<u>**Total expected cost**</u>		<u>**90,000.00**</u>

APPENDIX 1V: WORK PLAN

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