

**EFFECTS OF TAX REFORMS ON TAX COMPLIANCE OF SMALL AND
MEDIUM ENTERPRISES IN KENYA: A CASE OF MOMBASA COUNTY**

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DECLARATION

This research project is my original work and has not been presented for a postgraduate diploma in any other academic or non-academic institution.

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

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Date

DEDICATION

This proposal is dedicated to my parents for their support and motivation. To my classmates and friends; for their encouragement and standing by me.

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LIST OF ABBREVIATIONS AND ACRONYMS

FGD	Focus group discussion
GDP	Gross Domestic Product
GOK	Government of Kenya
IEA	Institute of Economic Affairs
IFC	International Finance Corporation
ILO	International Labor Organization
IMF	International Monetary Fund
IT	Income Tax
KRA	Kenya Revenue Authority
SMEs	Small and Medium enterprises
OECD	Organization of Economic and Cooperation Development
PBO	Parliamentary Budget Office
PAYE	Pay As You Earn
PIN	Personal Identification Number
WHVAT	Withholding Value Added Tax
UNDP	United Nations Development Program
USA	United States of America
VAT	Value Added Tax
WB	World Bank

DEFINITION OF TERMS

Compliance -Taxpayers willingly fully abide by the law, rules and regulations requiring them to pay taxes liable to them to tax authorities.

Compliance costs- Costs over and above the actual payment of tax and over and above any distortion costs inherent in the nature of tax incurred by taxpayers in meeting the tax requirements.

Corporate tax -A direct tax on incomes made by corporate bodies as provided by The Income Tax Act Chapter 470.

Income Tax -A tax charged on income earned by a person whether resident or Non-resident as defined under the Income Tax Act Chapter 470.

Small and Micro Enterprises- Refers to businesses which employ one or more persons and enterprises in the formal sector employing up to 50Persons.Sessional Paper No. 3 of 2004 of Kenya.

PAYE (pay as you earn) -A tax payment method in which an employer is required by law to deduct income tax from an employee's taxable wages. Income Tax Act CAP 470

Revenues- Refers to the gross proceeds received from taxes, fees, and other levies.

Tax -Is a financial charge or levy imposed on an individual or a legal Entity by a state.
According to (Bhartia, 2009)

Tax Modernization- Refers to the creation, amendment, or repealing of numerous tax related statutes and review of procedures and methods of work Performance. Institute of Economic affairs December 2006.

Tax audit -Is an examination of an individual or a corporation's tax return to verify its accuracy.

Tax evasion -Entails taxpayers illegally and misrepresenting or concealing the true state of their affairs to the tax authorities to reduce their tax liability. Tax procedures Act 2015

Value Added Tax- Is a consumption tax levied on designated local supply of goods and services and on imports in accordance with the provisions of The VAT Act Chapter 476.

ABSTRACT

In recent years, Kenya has experienced Tax compliance fluctuations, which have had an impact in the economy. It has had an effect on the country's competitiveness, international trade, inflation and general economic growth. This research therefore assessed the effect of each determinant factor on Tax compliance by examining the Withholding value added Tax, Rental Income Tax, and Itax system as the Independent variables of Tax Compliance. The study examined the global major studies with a focus on the big three determinants. The study employed a questionnaire to collect primary data for the period January, 2018 to September 2018 sourced from the Kenya Revenue Staff and Kenya Revenue websites. The research utilized descriptive statistics in the evaluation of the study by performing Regression Analysis and Correlation Analysis using the Statistical Package for Social Sciences (SPSS). Linear Regression Model was the empirical model used to analyze the depth of influence of each of the determinants on Tax Compliance by regressing tax compliance against changes in the determinants. The Pearson Product Moment Correlation was used to test the relationship between the variables. Tables, graphs and charts were used to present the findings. The study established that most of the SMEs operators had considerable experience and they had been in existence for a while. Based on the findings it can be concluded that the three tax reform determinants have positively resulted in tax compliance by SMEs.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

1.1.1 Global Perspective

World over, taxation is one of the government policy instruments used to achieve equity and efficiency in the economy (Jackson & McKee, 1992). Taxation is the known practical source of public finance in many economies, besides other sources like non-tax revenue like user-fees and licenses charged for rendered services by the government foreign aids, agencies and departments (Marina & Killis, 2002). The system of taxation is the origin of public finance in development projects such as providing of infrastructure like good roads, stable water and power supply among others. Which combine to create a conducive environment for businesses and in turn economic growth greatly (Duanjie, *et al.*, 2002). Tax collected by governments depends on Taxpayers' voluntary compliance whereby the taxpayers fulfill their tax obligation freely and completely (Walsh, 2012).

However, developing economies face challenges of raising sufficient tax revenue to finance the ever increasing public expenditures due to non-compliance amongst the taxpayers (Marti, 2010). Countries in the Sub-Saharan Africa not having revenue that is enough results in large budget deficits. Except when short-term fiscal stimulus can be considered suitable for macroeconomic reasons, deficits normally lead into undesirable macroeconomic results like the crowding out private investment and increasing of inflation.

To avoid deficits needs good control over both the revenue and expenditure government sides. The legislated budget should be structured every year to operate exactly within the estimates of likely revenue receipts. However for long term basis, effective tax strategies must be identified and implemented swiftly (James, 2008). There is need for appropriate tax systems with expanded tax base and improved compliance which can harness tax revenue (Pfister, 2009).

In many economies of the world, small and medium-sized enterprises (SMEs) have emerged as the potential and the unexploited tax revenue to address bedeviling fiscal deficits (Loeprick & Engelschalk, 2011).

According to World Bank (2007), SME includes those enterprises that are either officially registered businesses, with a turnover of between Kenya Shillings 8 to 100 million annually, with at least Kenya

Shillings 4 million worth of asset base or employ about 5 to 150 employees. The SMEs accounts contribute to 35-50 per cent of global Gross Domestic Products. SMEs are the dominant and vast majority of firms in many economies in the world (Venter & Clerk, 2007); for instance on average of over 90% of the developing countries enterprises like in Africa. The SMEs perform a very important role in contributing towards economic development, increase household income and also create jobs among others (Cynthia, *et al.* 2009).

Within Europe, 99 per cent of employment enterprises comprises of small and medium-sized enterprises which employ two thirds of the total workforce (Cynthia, *et al.*, 2009). Small enterprises play a role which is similar on the African continent. For instance, in 2003 in Nigeria, the small businesses were held responsible for official manufacturing activity worth 95 per cent. 70 per cent of the business enterprises in Ghana consists of microenterprises which have less than five employees and approximately 70 percent of the Ghanaian manpower is employed in SMEs sector.

SMEs are commonly characterized by uncertainty, innovation and evolution for instance within Nigeria they are usually family or owner managed small business offering essential goods and services, which may lack management and organizational structures while the ones in towns tending to be more structural than their counterparts in rural areas. Mostly the SMEs are partnerships or sole proprietorships although locally, they may be registered as Limited liability Companies of which they are usually not separate legal entities. Olorunshola (2003) further expounds that this ownership style has made small and medium enterprises to acquire a straight forward management structure compounded a small number of manpower and the proprietor allow level of education. Since there is no legal personality among the small and medium enterprise and its owners, this shows that the enterprise's lifespan is dependent on its owners lifespan ;that is there is no perpetual continuity. (Trivedi, C. & Shehata, N., 2005)

The production process of the SMEs is labor intensive, with raw materials locally sourced; they serve as suppliers to large established enterprises (Suwastika, N. & Anand, C., 2012). Their management decision being subjective since they are controlled and managed by the same individual and the employee-employer association found in most SMEs is mostly informal (Phillips, M., 2010). Further SMEs vary in sizes and organizational form; sizes varying from minor retail outlets to highly paid professionals, and substantial manufacturing enterprises and while forms vary from sole proprietorships (with or without employees), small corporations (public or private), partnerships and

professionals. The input that SMEs make to tax revenue tend to normally be lower compared to their contributions to employment and output (International Tax Dialogue, 2007).

Like other profit generating entities, SMEs are also supposed to pay their taxes, but however, the tax amount that they should be levied is the main concern. SMEs need special treatment because they are unstable establishments (Orodho, J.A. ,2005). They are commonly referred to as hard to tax taxpayers characterized by allow tax compliance which can be either by ignorance or by intent (OECD, 2012).

The concepts of behavioral insights is an emerging area in an attempt to explain taxpayers' compliance more so of the SMEs(Pficster, ,2009).The tax administration functions depends to some extent on the self-assessment of taxpayers based on their voluntary compliance. In this context, there is clearly possibilityto influence behavior to better compliance by understanding the reasons taxpayers are compliant or not.This can acquaint the work of tax administrations across range of their functions in regards to record keeping, seeking advice of tax experts and influence of other business (Blame, 2009).

According to OECD (2012) a large number of voluntary compliance is possible from the SMEs if there are simplified tax laws and proper tax administrations. The tax administration must help administer compliance which entails ensuringthat those people that should be in the system are in the system and they comply with the tax requirements(OECD. ,2005). First, if there is a registration requirement for taxpayers, the process of registration should be as easy as possible. Those who do not register voluntarily must be identified by the systems in place. An appropriate unique tax payer identification system should be adopted by the tax authorities in order to facilitate compliance and enforcement. Secondly, a process for determining tax liabilities is needed by the tax authoritiesby either administratively or through the self-assessment procedure. (Neshamba, F. ,2004)

Tax reforms aims to enhance compliance and create public perception of the fairness of the tax laws hence impacting positively on compliant businesses(Nada, O. &William, J. ,2009) . SMEs' tax reforms specifically include enacting special type of tax regime which is different from the normal tax regimes for large enterprises and administrative reforms. The special tax regimes for the SMEs includes granting of tax exemption as incentives for instance in India where agriculture is exempted from the income tax (Archie &Santorum 2007). In the United States, the Government implemented a number of policies and laws tohelp improve the level of WHVAT compliance among SMEs.

These measures included requiring withholding of tax at the source of income which means that the organization paying for services or goods withholds VAT there on and forwards it to the Government (Brockmann, Genschel, & Seelkopf, 2016).

In Egypt, SMEs are taxed under a uniform tax (or patent) or as business segment irrespective of the size or turnover of the individual enterprise or indicator based systems which use external indicators as proxy for business income (also used in Italy, Spain, and Argentina) (IFC, 2007). Further, taxation of SMEs can be based on agreement between taxpayer and the tax administration as used in Syria (OECD, 2012). However, according to Mage (2011) despite these SMEs tax reforms, most developing countries where SMEs sector contributes a significant percentage of GDP (average 41%) continue to be tax non-compliant. The compliance of tax involves all tax obligations fulfilled freely and completely as specified by the law.

1.1.2 Kenyan Perspective

According to the Sessional Paper No. 3 of 2004 in Kenya, SME is an enterprise with about 1 to 50 employees and the SME bill 2011 defines SMEs based on the number of workforce/manpower and the company's annual turnover. This sector accounts for 75% of the total employment in Kenya while contributing 4 percent of the country's Gross Domestic Product (GDP), this industry has been identified to be the driver of Vision 2030 (World Bank, 2007b).

The major tax reforms in Kenya started from mid 1980s under tax modernization programs (TMP) since before 1980s the government then suffered very minimal fiscal deficits and would contain its expenditure within the recurrent revenue limits (Muriithi & Moyi, 2003). The aim of TMP was to enhance saving and investment, enhance equity, increase on compliance through allow and rationalized tax rates, improve administration of tax through sealing leakage loopholes and broader tax bases (Moya & Range, 2006). The reason KRA was formed in 1995 was elaborated under TMP to improve administration of tax and implement organizational changes in order to modernize tax administration (Karingi & Wanjala, 2005).

The next phase in tax policies changes under NARC government (2003-2008) and coalition government (2008-2012) from 2003//04 to 2008//2009, since then we have concentrated around ensuring equity, the broadening of tax base, promote more investment and reduce the cost of compliance. Morse, S. C. et al (2009).

Withholding VAT was first introduced in Kenya in the year 2003 then suspended in 2011 but later re-introduced in the year 2014. Withholding VAT is governed by VAT Act 2013 however Section 26 of

the Finance Act 2014 amended VAT Act 2013 by inserting a new section 25 A which re-introduced Withholding VAT (WHVAT) system at the rate of 6% which came into effect from 19th Sept. 2014. Bonga (2017) indicated that reforms are also initiated to help modernize the tax policies to take into account the changes in the operating environment.

It is a tax deducted at source on acquisition of taxable goods and services by the withholding VAT Agent. Withholding Value Added Tax reduces the burden on the taxpayer though no reduction of liability on him, the sharing in payment has a psychological effect of not feeling much pinch on payment of VAT due to the government.

In addition KRA continued training and enlightening taxpayers to proceed to settle their taxes through banks and not KRA counters in order to reduce revenue leakages (IEA, 2012). Despite tax reforms there is considerable revenue leakage with continued existence of untaxed informal sector exhibiting varied tax behaviors relative to formal sector. The SMEs tax measure like not keeping records, negative attitudes and influence among the SMEs could have impact on tax compliance (Parliamentary Budget Office, 2011).

Hence its important to understand the effects of tax reforms on SMEs compliance (Mohd, R. P. & Mustapha, A. F. ,2011) .This creates the need for a proper tax reforms practices on compliance study on SMEs in Kenya, using case of enterprises in Mombasa County. Specifically, this study will establish how Withholding Value added Tax, Rental Income Tax and Itax affect compliance of the SMEs operating in Mombasa County; and develop strategies that will improve tax compliance among the SMEs and make policy recommendations based on these findings. (Maskell, P. & Malmberg, A. ,2002).

1.1.3 Tax Compliance

Tax compliance definition is the full payment of all taxes due (Braithwaite, 2009). While Tax non-compliance is referred to as any gap between the actual amount of taxes paid and the taxes due. The difference comes about due to overstating and understating income, expenses, and deductions. Non-compliance consists of both intentional evasion and unintentional non-compliance, which arises as a result of errors in calculation and an improper understanding of tax laws (Robben et al., 1990 and Webley, 2004). As stated by James, S. (2008.), the mistakes of taxpayers can be unintended and hence, do not necessarily represent evasion attempts or that they may even lead to over reporting of tax.

According to John (2006) tax compliance is the timely filling and reporting of required tax information, the correct self-assessment of taxes owed, and the timely payment of those taxes without enforcement action. From this definition, there are three dimensions of tax compliance: filing, reporting, and payment compliance. Filing compliance refers to whether the taxpayer submitted the correct forms to the revenue authority. Reporting compliance refers to whether the return was accurate, while payment compliance refers to whether the taxpayer paid his/her reported tax liability in a timely manner. Therefore, a taxpayer would be called non-compliant if the three dimensions are not properly accomplished. (Venter, J.M.P. & Clercq B., 2007).

1.2 Statement of the Problem

Many tax systems worldwide have undergone changes aimed at broadening the tax base and harness more tax revenues for public finance (Moya & Range, 2006; OECD, 2012). SMEs accounts for 90 per cent of the registered enterprises and contribute 35-50 percent global GDP. They have emerged as a new challenge to tax systems as their tax contribution hardly goes beyond 5 per cent (OECD, 2012). Kenyan Government enacted tax reforms like Withholding Value Added tax and rental income tax to bring the SMEs sector into taxation into tax bracket. According to Kenya Parliamentary Budget Office (2011) SMEs make up of 98% of all registered businesses in Kenya, contribute 34 per cent to GDP, and with tax potential of Kenya shilling 79 billion but actual collection is less than one billion. The SMEs have continued to be non-compliant (Mage, 2012).

Clough *et al* (2014) established that tax revenue loss in Kenya in the year 2013 was 8 per Cent of the total revenue collection mostly from the SMEs. The uncollected revenues which besides impacting negatively on compliant taxpayers also deprived the government much required finance in provision of infrastructures for enabling business growth. Consequently the government has been under-collecting tax, given that it failed to achieve its target for the year ending 2012 by Kshs 10 billion (IEA, 2012). Although the Government has Implemented tax reforms meant to improve compliance, it has not yet been established as to whether the said reforms have achieved tax compliance by SMEs as envisaged or not. The study by the Institute of Economic Affairs (2012) focused on the informal sector and Taxation. (Mage, 2012).

According to Lumumba *et al* (2010) the focus was on taxpayers' attitudes while Mage (2011) focused on the adoption of the IFRS by SMEs. In recognition to the role of tax reforms in raising the SMEs compliance; empirical literature on the compliance practices outcome of SMEs in a Kenyan

context which is scanty, a detailed study on the subject matter was necessary. This is supported by Mayo (2012) that the government could continue losing tax revenue from the SMEs sectors if equal measures like those of large enterprises are not emphasized. This study therefore sought to look at the effects of the tax reforms in relation to compliance in Mombasa County (Mage, 2012).

1.3 Objectives of the Study

1.3.1 General Objective

The general objective of the study was to determine the effect of tax reforms on compliance of the Small and Medium-sized Enterprises (SMEs) in Kenya, with reference to Mombasa County.

1.3.2 Specific Objectives

The specific objectives were:-

- i.** To establish the effect of Withholding Value Added tax on compliance of small and medium-sized Enterprises in Mombasa County.
- ii.** To determine the effect of rental income tax reform on tax compliance of small and Medium-sized enterprises in Mombasa County.
- iii.** To find out the effect of Itax on tax compliance of SMEs in Mombasa County.

1.4. Research Questions

- i.** How does Withholding value added tax affect tax compliance of small and medium-sized Enterprises in Mombasa County?
- ii.** How does rental income tax reform affect tax compliance of small and Medium-sized enterprises in Mombasa County?
- iii.** How does Itax affect tax compliance of Small and Medium Enterprises in Mombasa County?

1.5. Significance of the Study

1.5.1. Small and Medium Enterprises

This study documents tax reforms in terms of Withholding Value Added tax, rental income tax and Itax which affect tax compliance. The study finding was necessary to SMEs to understand how tax reforms affect their enterprises.

1.5.2. Academicians and Researchers

It is of value to the academicians and general public since SMEs tax matters have been viewed as a complex subject for a long time that should be left to tax experts largely and the Government. Such perception has contributed to the huge knowledge gaps on tax policy matters, tax governance and tax performance reaching the public. Academicians and researchers will use the research results as reference data for further research.

1.5.3 Government or Policy Makers

Tax reforms and compliance is an important Tax policy. Decisions have different effects on different people, businesses and the economy at large. For instance taxation affects prices of goods and services and peoples' income, businesses and individuals will react differently in response to income changes, and in similar prices, emanating from taxation. Therefore, the analysis of the effects of tax reforms on compliance of SMEs is critical for government decision makers and the public to make informed policy decisions. The tax reforms is critical to the government given the fact that the government to achieve vision 2030 tax collection and sustainability is recognized the most important element. Hence the study would go a long way to establish the effects of tax reforms on compliance of the SMEs and propose the mitigating measures that should be put in place in taxation of the SMEs in Kenya. An indepth understanding of the SMEs and taxation can assist policymakers design policies that not only encourage, nurture the culture of tax compliance and improve on tax revenue collection in the country; but also design policies that encourage SMEs growth. This would enable policy makers in using this as a basis for effective strategies for handling tax problems. The business community in Kenya would benefit from the study, since they would be able to establish how taxation affects them.

1.5.4 General Public

This study is useful to the general public who are widely interested in understanding the taxation of SMEs in Kenya. It also contributes to the existing literature due to the scarcity of publications about taxation and SMEs in Kenya.

1.6 Scope of the Study

The study focused on KRA tax officers in Mombasa County and SMEs in Mombasa County with specific reference to Withholding Value added Tax, Rental Income Tax and Itax. The study was limited to the sample size of 207 respondents out of a population of 561. The study findings were therefore generalized in the area of study only, although a number of findings was expected to have valid implications for the whole country. The study was conducted in 2018.

1.7 Limitations of the Study

Key limitations of the study included limited time and resources for actual field study where the researcher was required to get in touch with the SMEs and their owners to administer the questionnaires. To counter this, the researcher was obliged to seek the help of research assistants to aid in data collection. Securing appointment from the selected respondents also proved troublesome. To solve this problem, the researcher booked appointments early enough and made a follow up. Primary data collection was the main source of obtaining the relevant information in this research; However, not all respondents were comfortable with providing information, as they were unsure on the use of the information that they provided. To counter this, the researcher assured the respondents that the information sought would be used for academic purposes and that utmost confidentiality would be assured to them.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter presents a review of literature on the subject under study and was structured on the various thematic areas namely theoretical review, empirical review, critical issues, gaps to be filled and conceptual framework.

2.2. Theoretical Review

This study sought to determine the relationship between the tax reforms and compliance of the SMEs in Kenya with reference to Mombasa County. Tax compliance is a complex phenomenon, given the chance, a lot of businesses and individual taxpayers would not pay taxes unless there was motivation to do so. While some believe that the best way is to increase incentives (Feld & Frey, 2007) others believe the best way is to increase penalties. The tax compliance theories examined by this study were; economics based theories and psychology based theories. The first being the theory of economics that explain the change in taxpayer compliance behavior and the second is concerned with the studies based on theories of psychology and sociology that explain the varying levels of taxpayer compliance.

2.2.1. Economic Theory

The theory of Economics on tax compliance commonly known as deterrence theory, suggest that taxpayers are moral utility maximizers and emphasize on incentives to compliance (Manzo, M., 2011). The theory implies that taxpayers are a moral utility maximizers which means they are influenced by economic intentions like maximization of profits and the possibility of being detected. The taxpayers examine compliance paths alternatives for example, the possibility of being detected, whether or not to evade tax and the outcome of such consequences and then select the option that maximizes their expected returns after tax, after adjusting for risk. This process is referred to as “playing the audit lottery” by Trivedi and Schemata (2005).

The theories imply that the behavior of taxpayers is influenced by economic motives such as maximization of profit and possibility of being detected based on the chances of audits and penalties as a settlement to compliance problems (Trivedi & Schemata, 2005).

According to this Theory, for compliance to be improved; penalties and audits should be increased for non-compliance. This theory believes in government's that are aggressive in seeking to stabilize the economy based on value judgment has the capacity to improve the economy. This theory supports the taking of a bigger role by the government in the economy and a more general confidence in the governments ability to intervene and manage efficiently. In spite this theory fascination with uncertainty and his uncertain talents in the marketplace, the theory presumed the knowledge of the government to be superior to that of the marketplace. (Trivedi & Schemata, 2005).

2.2.2. Psychological and Sociological Theory

Lately, however, studies on compliance of tax have been based on social, fiscal and psychological theory which is not based on audits and penalties but however focusing on changing on the factors influencing individual decisions like behaviors among others. The proponents of this theory postulate that tax authorities should strive to ensure that they enact policies that influence the behaviors of the taxpayers positively towards tax compliance. The theories indicates that a taxpayer may comply even when the detection possibility is low. As opposed to the economic theories that emphasized on more penalties and audits as the answers to compliance issues, psychology theories base their emphasis on changing individual attitudes towards tax systems (Davos, 2012). This field studies on research claim that the element of humans play a significant role in taxpayers personal decision in regards to compliance. Especially, Kinsey and Smith discovered that perceptions in people are modelled by their social associations and networks, attitudes and beliefs which later influence how they respond to actual and perceived sanctions (Davos, 2012).

Based on this theory, rational choice see social interaction as a process of social exchange and according to this view, people are motivated by wants or goals that express their preferences (Scotts, 2000). Consequently, tax evasion has negative effect on the society and can harm the economy in many ways. More often, punishment of tax evasion act as deterrence yet still many countries face the challenges of tax revenue collection.

For instance during a recession period, when compliant tax payers are going through real hardship, the need to detect, deter and prosecute those who evade tax is more than ever. However many countries fail to detect and deter tax noncompliance which affect revenue collection (Trivedi & Schemata, 2005).

Hence, the fiscal psychologists insists that a taxpayer's belief in the tax system other than the penalty structure is more important in generating compliance. Trivedi and Schemata (2005) in conclusion noted that the behavior of some taxpayers may follow economic theories while others may follow the psychological theories and a mixture of the two is also possible. (Marina, K.&Kilis, D. ,2002).

2.3 Conceptual Framework

The study focused on assessing functional relationship between a set of three tax reform variables against tax compliance of the SMEs in Mombasa County. The explanatory variables are withholding Value Added tax, Rental Income Tax and I tax. The dependent variable is Tax compliance. The conceptual framework is presented below.

Independent variables

Dependent variable

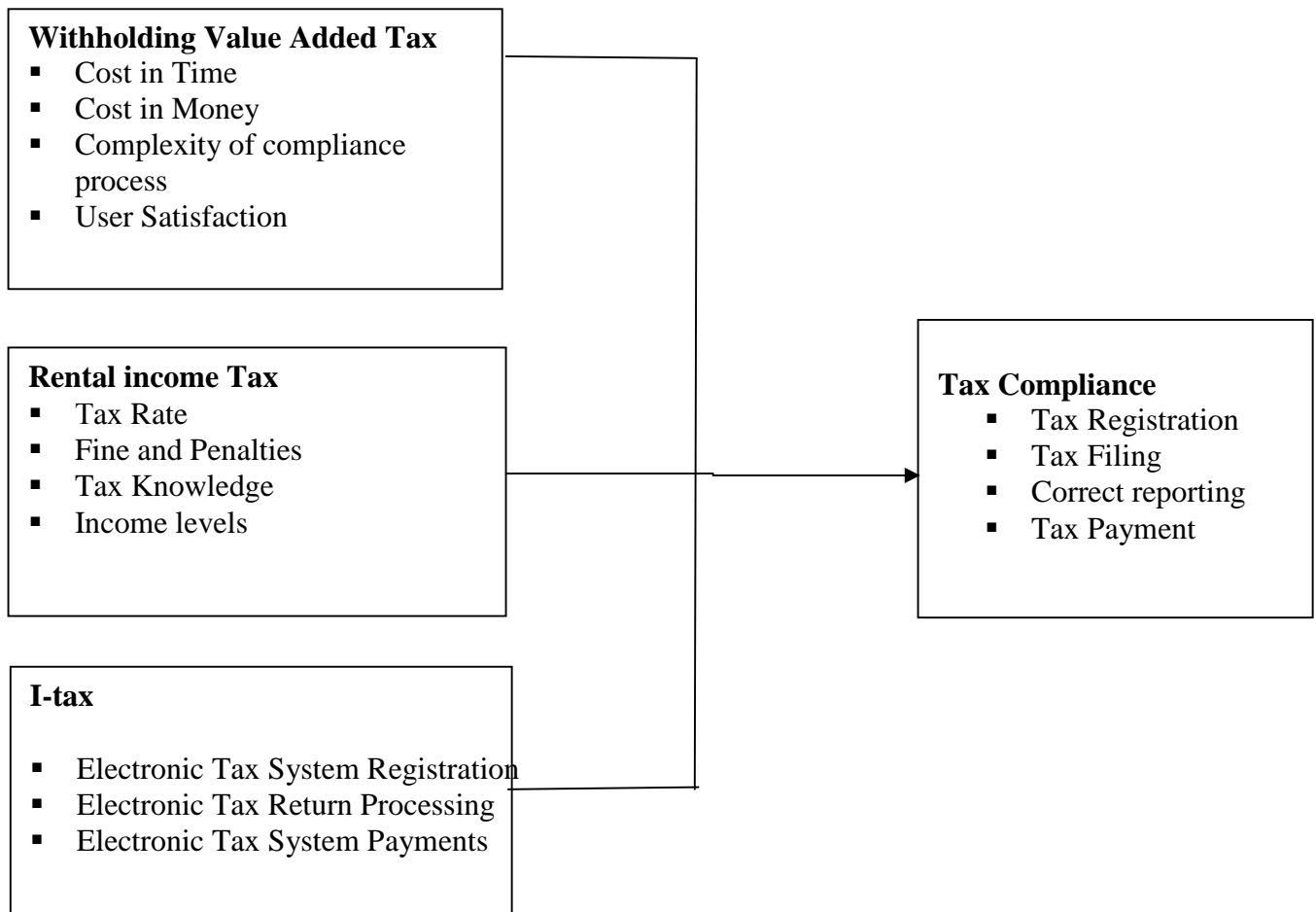


Figure 2.1. Conceptual framework

2.3.1. Operationalization of Variables

2.3.1.1 I-tax

The study reviewed the influence of **I-tax** in enhancing tax Compliance of the Small and Medium Enterprises in Mombasa County. I-tax was assessed by Electronic Tax System Registration, Electronic Tax Return Processing and, Electronic Tax System Payments.

2.3.1.2 Withholding Value added Tax

The study reviewed the effects of withholding Value Added Tax in enhancing tax Compliance of the Small and Medium Enterprises in Mombasa County. Withholding value added tax was assessed by Cost in Time, Cost in Money, Complexity of compliance process and User Satisfaction.

2.3.1.3 Rental Income Tax

The study reviewed the effects of Rental Income Tax in enhancing tax Compliance of the Small and Medium Enterprises in Mombasa County. Rental Income tax was assessed by Tax Rate, Fine and Penalties, Tax Knowledge and, Income levels.

2.4 Empirical Review of Variables

2.4.1 Withholding Value added Tax and SMEs in Kenya

Withholding VAT was first introduced in Kenya in the year 2003 then suspended in 2011 but later re-introduced in the year 2014. Withholding VAT is governed by VAT Act 2013 however Section 26 of the Finance Act 2014 amended VAT Act 2013 by inserting a new section 25 A which re-introduced Withholding VAT (WHVAT) system at the rate of 6% which came into effect from 19th Sept. 2014. Bonga (2017) indicated that reforms are also initiated to help modernize the tax policies to take into account the changes in the operating environment.

The Institute of Certified Public Accountant of Kenya (ICPAK) defines withholding tax system as encompassing withholding taxes and other withholding systems of taxation that could take the form of pay as you earn (PAYE), Value added Tax (VAT), and the withholding tax (WHT). The tax collection bodies across the world have advocated for withholding of taxes due to the benefits that come with it.

Some of the benefits include: decreased collection costs, faster remittance to the Government hence it can use the money sooner in funding its programs steadily throughout the year, reduces the need to save a gigantic payment in June of every year. The institute further notes that withholding has also been found to increase compliance and decreases evasion and underpayment because people don't notice how much tax they are paying in a withholding system hence there is less sense of anger (ICPAK, 2016).

WHVAT is a design of VAT; it is a system that encompasses the statement of VAT by both the supplier and his customer (KRA). It is a tax deducted at source on acquisition of taxable goods and services by the withholding VAT Agent. Withholding Value Added Tax reduces the burden on the taxpayer though no reduction of liability on him, the sharing in payment has a psychological effect of not feeling much pinch on payment of VAT due to the government.

Where a person makes a taxable supply and has issued a tax invoice, withholding vat is calculated based on a government's guidelines. For instance, in Kenya, WHVAT rate applicable is 6%. Assuming a taxable value of Ksh. 100,000 has been supplied, the agent with withhold Ksh. 6,000 that is $(100,000 * 6\%)$. The withholding of VAT by a withholding VAT Agent shall NOT relieve the supplier (Taxable person) of the obligation to charge VAT at 16% and file monthly returns in accordance with the relevant provisions of the VAT Act 2013 (KRA). The supplier is expected to pay the balance of 10% to account for the balance of vat charged at 16%.

The study reviewed the effects of withholding Value Added Tax in enhancing tax Compliance of the Small and Medium Enterprises in Mombasa County. Withholding value added tax was assessed by Cost in Time, Cost in Money, Complexity of compliance process and user Satisfaction.

Withholding Tax is important for it is a tracking system for taxpayers who reduce their actual tax liability or evade on payment of tax due on taxable goods and services. When the income on which WHVAT is deducted at source the tax authorities are aware of the transaction between the withholding agent and the taxpayer therefore the tax withheld becomes a basis for the tax expected. The taxpayer has therefore an obligation to pay the balance after matching the actual tax liability against the tax withheld.

WHVAT was re-introduced in 2014 in Kenya and the authority argues that it has increased VAT performance attributing such performance on the WHVAT framework.

2.4.2 Residential Rental Income Tax Compliance

Residential rental income tax is imposed on the rental income from residential buildings. Since any income received from renting out a property is legally chargeable to income tax, the property owners are expected to declare this specific income on their returns when filling. The source of this income can be from renting out land or buildings (Schiebold, M.,2011).

The rental income tax rate of 10% tax on gross rent took effects on 1st January 2016. This is applicable to rental income received from the month January 2016. Persons who are eligible are expected to file their tax return via ITax System (KRA, 2015). This 10% rate on tax on gross rental income is payable by a resident person whether individual or a no individual and is applicable to income from rent that has accrued in or is derived from Kenya for the use of residential property where the rent income does not exceed KShs.10 million per annum (The Finance Act, 2015).

This change is a segment of the KRA efforts to encourage tax compliance of property owners. Computing this tax is very simple since it is based on a percentage of the gross rentals income and is lower than the standard rate of 30% to echo the fact that the landlords do not receive a deduction for the expenses incurred to generate the income (KPMG, 2015). Some residential rental income tax benefits include tax computation that is simple at 10% flat rate of the gross rent and not at 10% -30% rates. The records to accounting for expenses are not a requirement for landlords to produced. The Finance Act also provides for an amnesty on taxes, penalties and interest on rental income for the period prior to 2014 (KPMG, 2015)., in addition to simplifying the taxation of rental income.

The study reviewed the effects of Rental Income Tax in enhancing tax Compliance of the Small and Medium Enterprises in Mombasa County. Rental Income tax was assessed by Tax Rate, Fine and Penalties, Tax Knowledge and, Income levels.

2.4.3 I-tax and Tax compliance

Kenya Revenue Authority has an e-filing system known as ITax. Through this system, a taxpayer is able to register as a taxpayer, file tax returns, make payments (through tax e-slip), view ones ledger record, apply for and receive tax refunds, apply for and obtain through e-mail Tax Compliance Certificate (TCC), and even make follow-up on KRA audit queries. Majority of taxpayers who have embraced this online system are either in Medium or Large category of taxpayers, yet majority of taxpayers in Kenya are categorized as small taxpayers (KRA,2010).

ITax is a computer based application system that furnishes a fully integrated and automated solution for administration of government revenue enhancements. ITax requires the use of technology (computers and smart phones) to access it. The benefits of an ITax system over submitting manual returns to the tax authorities are that the returns are uploaded directly to the system with negligible possibilities of errors because the system would not allow an upload with an omission or error in any field of the excel form. ITax is more advantageous than manual filing due to its secure features, (Ramayah, 2013). Practice has shown that the old systems of tax administration that involved manual returns and direct contact between the taxpayers and the tax officials resulted in huge tax revenue loss due to corruption and the propensity by the taxpayer to pay less than the due tax. An ITax system integrates the processes of tax filing, tax registration and tax payment. ITax enables taxpayers to avoid the hassles of visiting the tax offices, wasting time on queues and having direct contact with tax officials.(Fincham, J. E. ,2008).

ITax has made corporation tax compliance simple by ensuring that the annual returns which involve entering substantial data from audited financial statements cannot be submitted with an error as the ITax system would not accept the upload and directs the taxpayer to what could be wrong with therecord they have input. The taxpayer is able to file his/her corporation tax, make payment registration on reported tax and prepare payment slip all on ITax for submission to the bank for payment in an efficient manner.

The study reviewed the influence of **Itax** in enhancing tax Compliance of the Small and Medium Enterprises in Mombasa County. Itax was assessed by Electronic Tax System Registration, Electronic Tax Return Processing and, Electronic Tax System Payments.

2.4.4 Tax Compliance

Tax compliance is defined as the full and complete payment of all taxes due (Braithwaite, 2009). Tax non-compliance is referred to as any gap between the actual amount of taxes due and the amount of taxes paid. This discrepancy may occur because of overstating and understating income, expenses, and deductions. Non-compliance may consist of both deliberate evasion and unintentional non-compliance, which may be as a result of calculation errors and a lack of understanding of tax laws (Robben et al., 1990 and Webley, 2004). According to James, S. (2008.), the mistakes of taxpayers may be unintended and therefore, they necessarily do not amount to attempts to evade or even lead to over reporting of tax.

According to John (2006), tax compliance is the timely filling and reporting of required tax information, the correct self-assessment of taxes owed, and the timely payment of those taxes without enforcement action. From this definition, there are three dimensions of tax compliance: filing, reporting, and payment compliance. Filing compliance refers to whether the taxpayer submitted the correct forms to the revenue authority. Reporting compliance refers to whether the return was accurate, while payment compliance refers to whether the taxpayer paid his/her reported tax liability in a timely manner. Therefore, a taxpayer would be called non-compliant if the three dimensions are not properly accomplished. (Venter, J.M.P. & Clercq B., 2007)

The dream of all governments has been getting citizens to pay their taxes painlessly without hissing. However, the task has never been simple, until the modern information technology introduction. The world has experienced an unprecedented pace of improvement in the information technology field, since the early 1980s. These technological innovations are having a profound impact on the administration of fiscal systems and the way in which taxation is administered. In order to achieve tax compliance the majority of taxpayers voluntarily file their tax returns and pay resultant tax liabilities as set out in the tax laws, without the intervention of the tax authorities through enforcement. If voluntary compliance is low however, then measures of enforcement like audit and collection are resorted to. Tax compliance has been extensively reviewed (Pficster, M. ,2009). In this study, compliance was looked at comprehensively as filing

compliance, reporting compliance and payment compliance, quarterly and annually. Filing compliance was measured through, timely filing, e-return acknowledgement receipt and penalty imposed for non-compliance. Reporting compliance was measured through the selected tax base by the taxpayer either on preceding year's tax liability or on the current year's self-assessment estimates. Payment compliance was measured through payment registration slip based on the reported tax due and bank confirmation receipt. (Jackson, F. & McKee, M. ,1992).

2.5 Critiques of Existing Literature

According to Bird and Wallace (2004) the critical issue is whether the presumptive taxes are really efficient first in bringing SMEs into the formal economy and compel them to move into the normal tax system, while reducing the number of firms that move from the normal tax regime into the simplified one. In order to be appealing for informal firms the methods need not only to be based on information which is readily available but also to be simple to reduce compliance costs (as stressed by Thuringia and Victor (2004), based on the normal tax rules, they should also provide for an efficient taxation that will be lower than that .Nonetheless, this would discourage firms from ever moving into the normal tax regime and attract firms that were in the formal sector to move to the presumptive regime, resulting in revenue loss to the Tax Authority. The solution to this problem may be a periodical threshold revision for eligibility for the simplified regime and a time limit eligibility being placed for the systems (Schiebold, 2011).

As much as it is known that the behaviour of taxpayers' is controlled by a number of factors (both economic and non-economic) which is variable lacking research in Kenya is the influence of tax reforms and their role in individual SMEs taxpayer compliance (Water, 2007). Aristidis *et al.*, (2005) evaluated difficulties and challenges encountered by entrepreneurs businesses in Albania. It was established by the study that the most important difficulties faced by entrepreneurs in Albania were lack of financial resources,unfair competition, changes in taxation procedures and problems related to public order. However in the study, corruption and bureaucracy were not to indicate important obstacles to entrepreneurship.The study therefore recommended for changes of regulatory policies which should mostly concerntrate upon small business and enterprise development and should be applied by the governments in order to attain a transparent fiscal reform and create a more favorable business environment.(James, S. ,2008)

Small business owners play an significant role in the tax system and the study by Bernadette *et al.*, (2012) highlighted tax compliance situation of small business owners. The study found that three key aspects seem to distinguish small business owners' perceptions of their tax situation: small business owners tend to perceive more opportunities to avoid complying than taxpayers who are employed; they are likely to have a lack of meaningful knowledge on taxation; and they are also likely to face decision frames that render taxes as painful losses. The study recommend for a focus on strategies that aim to influence taxpayers 'perceptions of their own evasion opportunities, their level of legislative and procedural knowledge, and their sense of ownership of tax money. Such a strategy is suggested to be particularly likely to be effective in the phase of nascent entrepreneurship and in a climate of mutual trust between taxpayers and tax authorities.(International Finance Corporation, 2007)

Duanjie *et al.*, (2002) in their study on implications of tax policies on the expansion of SMEs and entrepreneurships among the OECD members established that most tax systems are biased against SMEs and entrepreneurships and hence discourage startup of the SMEs. For instance they noted that tax systems favor debt over equity in financing through double taxation. They recommended for improvement for preferential tax treatment to SMEs and entrepreneurships by offering better tax climate for the SMEs among the OECD members. However this study did not clearly point out the benefits of taxation of SMEs and entrepreneurship. (OECD 2003)

Moyi and Ronge (2006) reviewed tax design as well as tax revenue performance and changes in the administration during the period 1996 - 2005 to be able to identify further tax reform priorities. The study established that the taxation system in Kenya is burdensome in terms of the time one takes to prepare and submit the tax returns. The study deduced that there should be more than reforms as the one done are not enough and also involve taxpayers in the crafting of tax policy and planning for any reforms. Chang and Dina (2007) studied effects of corporate tax reforms since 1980 to 2004 among six European Union member countries (Austria, Finland, France, Germany and UK) on SMEs' decisions on investment under specific consideration of inflation.

The study compared Tax incentive effects of such reform on the small and medium sized enterprises investment decisions like the tax rates and depreciation rules. It was established that these reforms did not bring about productive results to SMEs and entrepreneurships for instance existence of non-neutrality of tax between the financing methods which favors bigger firms with

easier access to bank loans. However this study only covered corporate taxes and hence ignored other taxes which all affect SME. Manzo (2011) examined corporate taxation and SMEs in Italy between the year 1997 and 2004. The author established that growth of SMEs and entrepreneurship is more sensitive than larger and older firms to changes in corporate tax rate, which are attributed to difficulties in accessing debt financing. Further it was established that the investment undertaken by the old and medium firms are affected negatively by the user cost of capital; which implies that older firms are more profitable than the younger ones and therefore more affected by the corporate tax adjusted user cost of capital. (John, M. & Lineth, N. ,2006).

This study improves Chang and Dina (2007) study; who had concluded that the objectives of the reforms have not been achieved. A three-sector comparative (manufacturing, retail and businesses) study of the taxation effects on small and medium sized enterprises in Gauteng South Africa was carried out by Venter and Clerk (2007). The study established that the size of an enterprise and the sector in which it operates has an impact on how the enterprise's tax responsibilities are administered and managed thereby influencing business outcomes. Majority of the small and medium sized enterprises in the business sector outsource their tax responsibility because of inadequacies of necessary resources. The study recommends that the regulatory environment which affects small and medium sized enterprises should be reformed like reduction of interest and penalties charged as one of the measures of tax relief. This study is in support of other studies (Duanjie et al, 2002; Chang & Dina 2007; Brays 2011) which recommend for preferential tax treatments of the SMEs but which dwelt on the developed economies. (Fjeldstad, O. & Rakner, L. ,2003).

2.6 Research Gaps

The factors influencing tax compliance among taxpayers is well documented in the literature reviewed (Duanjie *et al* 2002; Thuringia & Victor, 2004; Sandman, 2004; Chang & Dina 2007; Brays 2011; Bernadette *et al* 2012; Walsh, 2012). In recognition thereof, many policy makers were unanimous in making changes to their tax systems in their countries to capture these factors influencing tax compliance culminating into tax reforms. Tax reforms have been implemented in many economies in the world (Moya & Range, 2006; OECD, 2012). However new aspects influencing tax compliance keep on emerging for instance SMEs taxation. This view is supported by Mage (2012) that world over government is still grappling on the appropriate way of

taxing SMEs. Previous studies focusing on tax reforms have concentrated on tax reforms on large and established enterprises in developed economies Europe and USA while ignoring developing countries like Kenya (Bird *et al.*, 2004; Aridis & Ersanja, 2005; Wendell, 2005; Balladry, 2006; ;Archie Santoro,2007;Venter & Clerk ,2007; Bernadette *et al.*, 2012). Even though the SMEs forms the greater number of the (90 %) of the registered enterprises and contribute to 35-50 percent of the global Gross Domestic Products but their tax contribution hardly goes beyond 5 per cent (OECD, 2012). A review of literature on the Kenyan context on tax reforms and SMEs compliance revealed limited studies on the matters pertaining to this subject. This study found on the subject by the Institute of Economic Affairs (2012) concentrated on the taxation of the informal sector.

In recognition of the role of taxation on reforms,a detailed study on the subject matter was necessary.This is supported by Mayo (2012) that the government could continue losing tax revenue from the SMEs sectors.The study therefore seeks to look at the effects of the tax reforms in terms of Withholding Value Added tax, Rental Income Tax and Itax on compliance.

2.7 Summary

This chapter covered literature review relating to the theory of sociological and economic theory. First, the study looked at the theoretical framework where it outlined the theories on which the study is grounded. The theories covered were Economic theory, Psychological and Sociological theory. In addition, the chapter established the conceptual framework for the research project based on the determinant factors and empirically reviewed the variables. This chapter also critiqued the existing literature relevant to the study and finally established the research gaps based on the literature review. Following a critical examination of literature and the empirical studies conducted by different researchers on compliance of tax and its determinants, we can deduce theoretically that the different factors vary on their impact on changes and volatility of the tax compliance.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the methodology that was used in carrying out the study namely the Research design, target population, sampling frame describing the sample size and how it was selected, data collection instruments and their administration, data analysis techniques and tools.

3.2. Research Design

The study adopted a descriptive design. This research design allows for a detailed description and analysis of the variables under study; the design allows for describing and presenting their accurate profiles as it exists without influencing it in any way and explaining their relationship without manipulation as supported by Saunders *et al.* (2009). In addition the design produces results that are holistic, contextual and rich in detail on the subject of the Study. This design allows for inductive and deductive reasoning to arrive at generalization of the study findings on tax practices and SMEs' compliance in Kenya. In addition this research design was appropriate for this study since the problem under study was structured and well understood, therefore requiring precise rules and procedures regarding collection and analysis of data.

3.3 Target Population

The target population was SMES registered with KRA Mombasa and tax compliance officers in KRA Mombasa tax station. Each of tax compliance officer and SME manager constituted the main respondents. The study determined the influence of tax reforms on tax compliance of SMEs from the perspective of both KRA officials and SMEs enterprises. As per the statistics obtained from the Department of Human Resources at KRA on 31st June 2017, there were approximately 56 Revenue officers in Mombasa tax station. While from compliance section of KRA on 31st June 2016 there were 505 registered SMEs taxpayers. This gives a total target population of 561.

Table 3.1 Target Population

Business Sector(Strata)	Total count
Trade sector	308
Manufacturing sector	46
Construction sector	57
Service sector	94
Subtotal	505
Mombasa KRA	
Station manager	1
Section heads	4
Supervisors	11
Officers	40
GRAND TOTAL	561

SOURCES: (KRA 2017)

3.4. Sample Size and Sampling Techniques

The respondents of the study were selected through simple random sampling techniques. According to Mugenda Mugenda (2003) a sample size of 30% is adequate for generalization purposes in a population. For the SMEs a sample size of 30% was taken from the population of 505 SMEs, while for the KRA officers since they are few all of them were sampled .

Table 3.2 Sampling Frame

Business Sector(Strata)	Total Count	Sample Percentage	Sample Size
Trade sector	308	30%	92
Manufacturing sector	46	30%	14
Construction sector	57	30%	17
Service sector	94	30%	28
Sub total	505		151
Mombasa KRA			
Station manager	1	100%	1
Section heads	4	100%	4
Supervisors	11	100%	11
Officers	40	100%	40
GRAND TOTAL	561		207

Source Researcher (2018)

Proportionate Stratified random sampling was used in the study for equal chance in selection to the individuals in the population (SMEs). A list of all SMEs operating within Mombasa County and KRA Tax officers was obtained in order to construct a sampling frame from which the individual respondents were picked and included in the sample. After constructing a sampling frame a total of 151 SMEs respondents were randomly selected together with the 56 KRA officers a total 207 respondents were chosen.

3.5 Data Collection Instruments and Procedure

To obtain quantitative and qualitative data, the study used questionnaires, and interview schedule.

3.5.1 Questionnaires

Questionnaires were the main research instruments used in this study for data collection. The Questionnaires were vital in deriving quantitative interpretation on the effect of tax reforms on compliance of SMEs within Mombasa County.

The study used closed ended questions in this study for all the respondents ;SMEs and KRA compliance officers in Mombasa station. According to Kothari (2006) questionnaires have the ability to gather data of a large sample size, save time, and uphold confidentiality of the respondents. While according to Rodeo (2005) a combination of open and closed ended questions produces and provides a situation of generalization. The questionnaires were administered by the researcher directly (by hand delivery) to the respondents at their work station (for KRA officers) and business premises (for SMEs) so as to increase response rate. To limit a delay in response rate from the respondents who preferred interview instead of filing the questionnaires, the researcher read and filled the responses on their behalf. A likerth scale was used to denote the questionnaire for easy data analysis and interpretation.

3.6 Piloting of the Study

A pilot study was conducted to a randomly selected 24 SMEs and two KRA officers' in Malindi town whose participants did not participate in the main study. The pretested respondents had similar characteristics as those of the actual respondent's in Mombasa but were informed that it was a pretest. The pilot study showed ambiguities in the research instrument before its actual administration and helped determine whether the statistical tools used were useful for effective results in the ultimate study. Further the pilot study ensured that the questionnaires were clearly phrased and wordings understood by the respondents, arranged in logical and easy to follow sequence, relevant and were not personal, discouraging and time consuming in nature to the respondents.

3.6.1 Reliability of Research Instrument

The questionnaires were tested for reliability during the pilot test of 24 SMEs and two KRA officers' in Malindi. Reliability is the extent to which any measuring procedure gives the consistent results on repetition. Even though there are different forms of reliability, this study used internal consistency reliability whereby several items in the questionnaire would measure same general construct by producing similar results and findings .The research instruments were assessed by the supervisor for consistency in questions and answers received, during the pilot study changes were made before being officially administered.

3.6.2 Validity of research instrument

Validity involves the degree to which obtained results from data analysis actually represents the phenomenon under study and can be tested by consensual judgments by experts (Kothari, 2006). One of the type of validity is criterion which determines whether a test reflects a certain set of abilities and while content validity involves whether operational definition of a Construct validity: Based on the study objectives, individual questions were developed so as to reveal whether the wording of items used to measure a concept were related to that concept or one of its dimension. The purpose of this check was to ensure that each measure adequately assess the construct it purported to assess. Face validity: Then the questionnaires were subjected to checks by the experts (supervisors And others) for clarity, word choice, time frame and response set to ensure that the instruments were carefully defined, with no language barriers and good to administer.

3.7 Data Analysis

3.7.1 Qualitative Analysis

Qualitative data generated from the field was transcribed and summarized based on themes in relation to the objective under study. The descriptive statements were developed and analysis was carried out on the data.

3.7.2 Quantitative Analysis

Quantitative data was analyzed through frequencies, means, tables and charts.

Correlation analysis was used to show the relationship between the variables while regression analysis was used to measure the depth of the relationship between them.

The empirical model in this study was on the following equation:

$$Y=f(X_1,X_2,X_3)$$

The linear regression model is given by:

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

Where,

Y= Tax compliance

β_0 = Constant

X_1 =Withholding Value added tax

X_2 =Rental income tax

X_3 =Itax

=Error term

The standardized beta coefficients from the linear regression analysis indicates the effect of the regressor variables on the dependent variable. By standardizing the variables before running the regression, you have placed all the variables on the same scale and you can analyze the magnitude of the coefficients to see which one has more of an effect. Therefore the strength of effect of each determinant factor was measured using the standardised beta coefficients of the explanatory variables in the linear regression model because the beta coefficients show the independent contribution each explanatory variable had to the prediction of the response variable. It answered the questions as to the extent to which the determinant factors influenced tax compliance by comparing the values of Beta 1, Beta 2 and Beta 3.

CHAPTER FOUR

PRESENTATION AND DISCUSSION OF FINDINGS

4.1 Introduction

This chapter presents and discusses the main findings of the study as set out in the research methodology. The purpose of the study was to establish effects of tax reforms on tax compliance of SMES in Mombasa County. This chapter also presents analyzed data using frequencies, charts, and tables. The findings are presented in the following thematic areas: demographic characteristics of the respondents; Withholding Value added tax; Rental Income Tax; I-tax; and Tax Compliance. Primary data was collected using questionnaires, the data was tested for reliability and validity and there after analyzed using Statistical Package for Social Sciences (SPSS) and presented using tables and charts.

4.2 Response Rate

Out of the 207 respondents who included SME owners and KRA revenue officers in Mombasa County, 198 responded to the research tool against 9 who did not. This formed a response rate of 95.65%. The response rate was adequate to examine the factors affecting tax compliance of SMEs since it is above 50% as recommended by (Mugenda).

4.3 Demographic Characteristics of the Respondents

As a preliminary intent to measure the quality of responses from the respondents, the study explored the gender of the respondents, age characteristics, level of education, forms of business organization and level of experience in tax matters.

4.3.1 Demographic Gender of the Respondents

The first demographic trait of the respondents tested was gender. The study tested the quality of respondent in regard to gender composition and the findings are in Figure 4.1

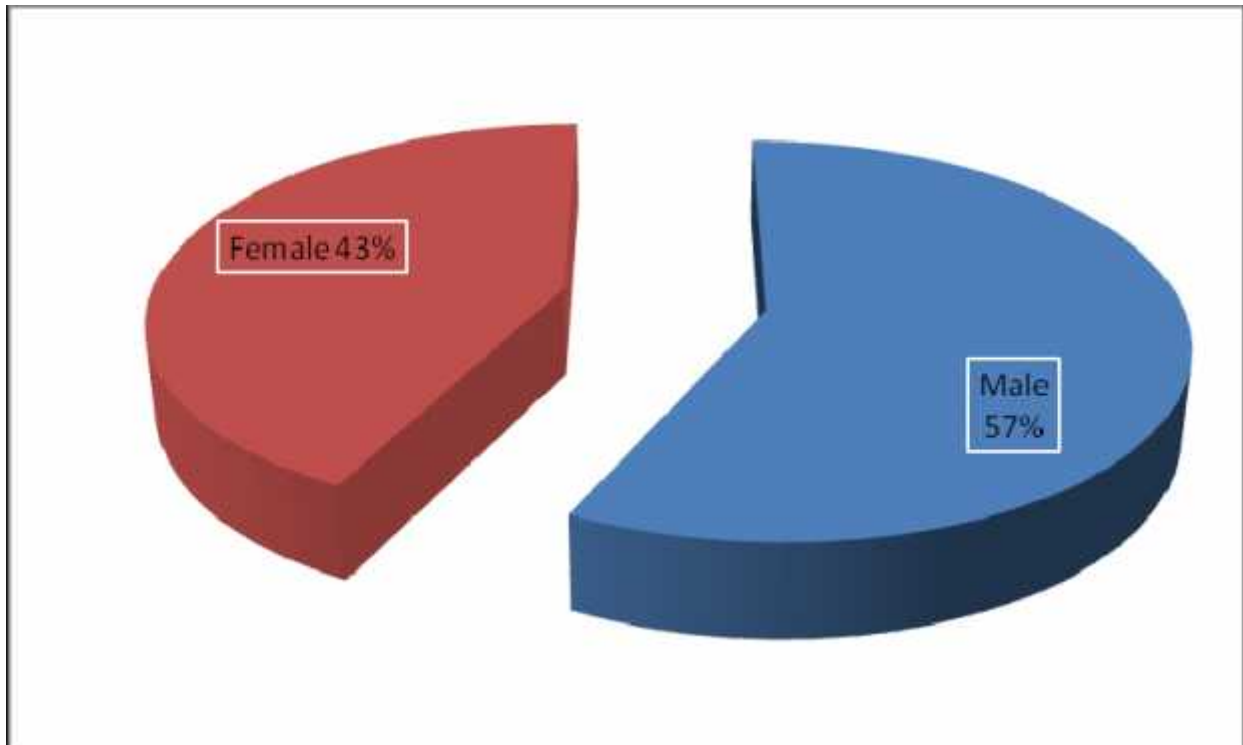


Figure 4.1 Gender distribution of the respondents

Males were 113 (57%) while the females were 85 (43%). The findings in figure 4.1 imply that the majority of the respondents were males and therefore SMEs in Mombasa County are male-dominated. The gender of the taxpayer is a vital factor in determination of the compliance of tax. According to Walsh (2012), gender has a role to play in regard to tax compliance in that female taxpayers are risk averse hence have a tendency to be more tax compliant than their male counterparts.

4.3.2 Demographic Age of the Respondents

The demographic age of the respondents in the study was vital since it indicated the quality of respondents in regards to handling and exposure to taxation. The study tested the respondents' age distributions as a measure of the quality of the sample characteristics in providing quality data. The findings are presented in Table 4.1

Table 4.1 Age distribution of the respondents

Respondents age bracket	Frequency	Percentage
20-30 years	63	32%
30-40 years	46	23%
40-above years	89	45%
Grand Total	198	100%

Source: Research Findings (2019)

From the study findings, 63 respondents (32%) were aged between 20-30 years, 46 respondents (23%) were aged between 30-40 years while 89 respondents (45%) were aged 40 years and above. This showed that most businessmen were aged 40 years and above and had had experience in running of businesses. According to OECD (2012), demographic age of the owners or proprietors of Small and Medium enterprises (SMEs) affects their tax compliance. For instance, people who are old are more tax compliant, because they are generally more risk averse than young people who are risk takers.

4.3.3 Respondents' Level of Education

Further to the ascertainment of the quality of respondents in providing quality data, the study sought to determine level of education of the respondents. Educated people are better and well informed of the laws pertaining to taxation, which should positively influence compliance. They also have better knowledge for tax evasion opportunities. The findings on the level of the respondents are presented in Figure 4.2.

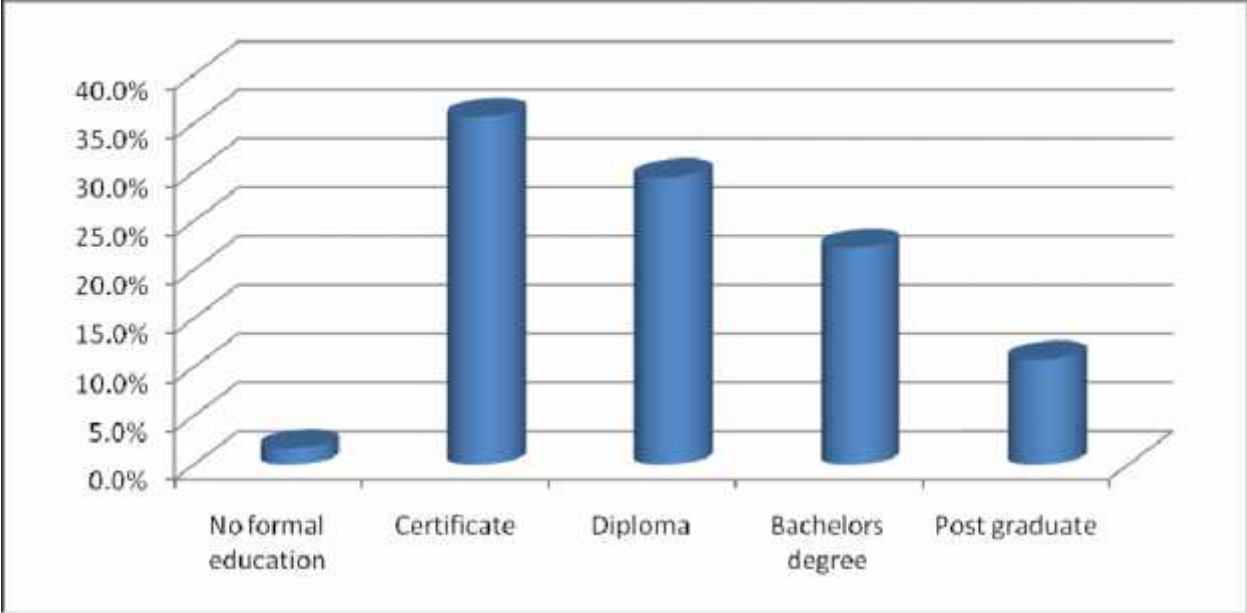


Figure 4. 2 Education Level of the Respondents

The study established that most of the respondents were educated and they were able to interpret the tax laws and comply with it. Only 2% (4) had no formal education, 37% (73) had basic education that is certificate, 27% (53) had diploma and 25% (50) had bachelors’ degree while 9% (18) had postgraduate education. The respondents without formal education were assisted to answer the questionnaires while the rest of the respondents were given self-administered questionnaires. Therefore all the respondents not only were they well suited to understand and answer questions in the study, but also they had the ability to read tax laws since most of the respondents had basic education.

4.3.4 Respondents’ Business Structure

Further to the ascertaining of the quality of the respondents in providing quality data, the respondents were asked the type of their organizations. The findings are presented in Table 4.2

Table 4.2: The Respondents' Business Structure

Type of Business	Frequency	Percentage
Sole proprietorship	89	45%
Partnerships	39	20%
SACCOs	20	10%
Limited Company	50	25%
Total	198	100%

Source: Research Findings (2018)

According to the study findings, majority 45% (89) of the respondents were operating as sole proprietorship and 20% (39) were operating as partnerships and 10% (20) as SACCOs. Only 25% (50) of the respondents indicated that their organization were limited companies. From the study data, most of the respondents were operating as sole proprietors and self-employed. According to Venter (2007) sole proprietors and the self- employed people are less compliant on average and have high compliance costs and more opportunity to evade taxes.

4.3.5 Respondents' Working Experience

The experience of the respondents, that is SMEs managers and KRA officers in Mombasa, was another demographic variable considered under the study. Respondents with more experience are likely to provide quality data as compared to inexperienced respondents. The finding is presented in Table 4.3

Table 4. 3 Distribution of Respondents by Working Experience

Work experience	Frequency	Percentage
Less than 2 years	8	4%
2-3 years	18	9%
4-6 years	30	15%
7-8 years	55	28%
9-10 years	57	29%
More than 10 years	30	15%
Total	198	100%

Source: Research Findings (2019)

The study established that only 4% (8) had been in their organization for less than two years and 9% (18) had been with their organization between two and three years. Fifteen percent (30) had been in their organization for 4-6 years, 28% (55) had been in their organization for between 7-8 years, 29% (57) between 9-10 years, 15% (30) 10 years and above. This implies that most respondents were knowledgeable and experienced in their work in regard to taxation. The respondents were taken to have acquired experience at different levels and hence they were people who had handled tax matters. According to Walsh (2012), educated and experienced people may be informed better of the laws of tax, which should positively influence the tax compliance; however, the same may present risk of tax avoidance.

4.4 Test of Assumption

Besides descriptive data analysis, tests of assumption was done to determine the level of association between the independent variables and the dependent variable in the outcome of the study. In order to ensure that the data used was reliable, multicollinearity of independent variables and Normality Test Results of the Dependent Variable were done.

4.4.1 Multicollinearity Test

During regression, correlational effects amongst independent variables may affect the outcome of the measurement of the causal relationships between independent and dependent variables hence producing misleading or biased results. In order to avoid this scenario, it was necessary for the independent variables to be subjected to multicollinearity test so as to establish if there was any collinearity between them. This was therefore done using Variance of Inflation Factor (VIF) and Tolerance tests so as to help clear this doubt. Sasa-Escudero et al (2009) argues that when multicollinearity is present, the model tends to have a VIF of more than 10 or a tolerance level of less than 0.2. As indicated on table 4.4, all the VIF did not exceed 10. This implied that there was no Multicollinearity in the dataset and hence the data was suitable for regression modeling. Similarly, the tolerance levels for all the independent variables were less than 0.2 meaning that they did not have any effect on each other.

Table 4.4 Multicollinearity Test

Constant	Collinearity Statistics	
	Tolerance	VIF
Withholding VAT	0.157	7.213
Rental Income Tax	0.109	6.899
ITax	0.111	7.102

a. Dependent Variable: Tax compliance of SMEs

Source: Research Findings (2019)

4.4.2 Normality Test Results of the Dependent Variable

To test for normality of the dependent variable (tax compliance of SMEs), Kolmogorov-Smirnova and Shapiro-Wilk tests were conducted. This was important in order to establish the suitable tests to be conducted and ensure that the assumptions of a normal distribution were not violated (Math-Statistics-Tutor, 2010). Kolmogorov-Smirnova and Shapiro-Wilk test for normality were used to detect all departures from normality (Math-Statistics-Tutor, 2010). The

tests reject the hypothesis of normality when the p-value is greater than or equal to 0.05 (Sharpiro& Wilk, 1965). Table 4.5 shows that the Kolmogorov-Smirnova and Shapiro-Wilk statistics were 0.132 and 0.817 respectively. The associated p-value was .004 and .116 for Kolmogorov-Smirnova and Shapiro-Wilk statistics respectively. Since the p-values were greater than the significance level (0.05) (not significant if $p < .05$), this implies that the variables were normally distributed.

Table 4.5 Normality Test Results for Dependent Variable

Factors	Kolmogorov-Smirnov ^a			Shapiro-Wilk		
	Statistics	df	Sig	Statistics	df	P-value
SMEs tax compliance	.132	198	.004	.817	133	.116

a. Lilliefors Significance Correction

Source: Research Findings (2019)

4.4.3 Linearity

Linearity refers to a situation where the amount of change or degree of change between scores on two sets of variables is constant for the entire range of scores for the variables (Bai & Perron, 2008). Therefore, it is the consistent slope of change that represents the relationship between an independent variable and a dependent variable (Granger & Tera, 2007). If a linear model is fitted to data which are nonlinearly related (is in violations of linearity), predictions are likely to be seriously in error (Hansen, 2009). The problem of linearity is fixed by removing outliers (Hansen, 2009). Hence, the study assumed linearity of the independent variables since outliers had been dropped.

4.5 Descriptive statistics

4.5.1 Withholding Value Added Tax System and Tax Compliance

The study sought to determine whether the implementation of Withholding value added tax contributed to enhancement of tax compliance of SMEs operating in Mombasa County.

The respondents were tested on parameters, which measured the effects of the Withholding value added tax on tax compliance. The specific parameters analyzed in the study were withholding value added tax cost in time, cost in money, complexity of compliance process, and user satisfaction. The study sought the views of the respondents through the use of Likert question to measure the level of agreement or disagreement with the items that were formulated to elicit their opinions based on their understanding and experience of the Withholding value added tax.

The Likert question was based on a 5-likert scale where strongly disagreed =1; disagreed =2; neutral =3; agree = 4 and strongly agreed = 5. On the scale of 1 to 2 it is assumed as Non-compliance or non-awareness total Withholding Value Added tax; as from 4 to five is taken as compliance and hence awareness total Withholding value added tax while 3 is between compliance and non-compliance.. The findings are presented in Table 4.6

Table 4.6 Effects of Withholding value added tax on Tax compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Likert Mean
Withholding VAT has reduced the time required in Tax compliance	3%	12%	6%	35%	44%	3.87
Withholding VAT has reduced the cost incurred during tax filing	3%	6%	6%	41%	44%	3.99
Withholding VAT has made the compliance process less complex	8%	15%	2%	27%	48%	3.86
More of the business owners are satisfied with Withholding VAT	15%	15%	3%	32%	35%	3.48
Overall Likert Mean						3.8

Source: Research Findings (2019)

4.5.2 Effects of Withholding Value added tax on Tax compliance

From the findings, 79% of the respondents agreed that Withholding Value added tax had reasonably reduced time spent in tax compliance of the SMEs, 85% of the respondents agreed that Withholding value added tax has reduced the financial cost incurred in tax compliance,

75% of the respondents agreed that as a result of withholding tax the process of tax compliance was less complex and 67% of the respondents agreed that they were satisfied with the implementation of Withholding value added tax. The overall mean was 3.8, which implied that Withholding tax had a positive effect on tax compliance. These findings agree by a study done by the institute of Certified Public Accountants of Kenya who further note that withholding has been found to increase compliance and decreases evasion and underpayment because people don't notice how much tax they are paying in a withholding system hence there is less sense of anger (ICPAK, 2016).

4.6 Rental Income Tax and Tax Compliance

This study sought to determine the extent to which Rental Income Tax was effective in enhancing Tax compliance of the SMEs in Mombasa County. The specific Rental Income Tax aspects measured were tax rate, fine and penalties, tax knowledge, and Income levels. Table 4.7 gives this summary.

Table 4.7 Effects of Rental Income Tax on tax Compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Likert Mean
Tax Rate;10% residential rental income tax rate is fair to property owners	15%	15%	3%	32%	35%	3.48
Tax Rate; The lowered tax rate has influenced willingness of residential rental property owners to be tax compliant	7%	12%	5%	32%	44%	3.79
Fine and Penalties; Fines and penalties are very punitive to property owners	10%	15%	7%	36%	32%	3.44
Fine and Penalties; Fines and penalties discourage non-compliance with of residential rental income tax obligations.	5%	8%	8%	31%	48%	3.85
Fine and Penalties Periodic waiver of fines and penalties could encourage tax compliance .	15%	10%	7%	31%	37%	3.44
Tax Knowledge; Knowledge about tax laws plays a major role in determining property owners' tax	12%	6%	9%	35%	38%	3.54

compliance.						
Tax Knowledge; Lack of proper records on expenses incurred greatly contributed to non-compliance by property owners in the previous regime	8%	15%	2%	27%	48%	3.86
Income levels; Property owners with low income levels are more likely to be non-compliant	4%	2%	5%	52%	37%	4.01
Overall Likert Mean						3.68

Source: Research Findings (2019)

4.6.1 Effects of Rental Income Tax on tax compliance

From the findings, 67% of the respondents agreed that Tax Rate; 10% residential rental income tax rate was fair to property owners, 76% of the respondents agreed that Tax Rate; The lowered tax rate had influenced willingness of residential rental property owners to be tax compliant, 68% of the respondents agreed that Fine and Penalties; Fines and penalties are very punitive to property owners, 79% of the respondents agreed that Fines and penalties discourage non-compliance of residential rental income tax obligations, 68% of the respondents agreed that Fine and Penalties; Periodic waiver of fines and penalties could encourage tax compliance, 73% of the respondents agreed that Knowledge; Knowledge about tax laws plays a major role in determining property owners' tax compliance, 75% of the respondents agreed that Tax Knowledge; Lack of proper records on expenses incurred greatly contributed to non-compliance by property owners in the previous regime, 89% of the respondents agreed that Income levels; Property owners with low income levels are more likely to be non-compliant. The overall mean was 3.68, which implied that Rental Income Tax has had a positive effect on tax compliance. These findings agree by a study done by (KPMG, 2015) who further note that Some of the benefits of the residential rental income tax include simplified tax computation at 10% flat rate on gross rent and not at 10% -30% rates. Landlords are not required to produce records to account for expenses. In addition to simplifying the taxation of rental income, the Finance Act also provides for an amnesty on taxes, penalties and interest on rental income for the period prior to 2014.

4.7 I -Tax and Tax Compliance

The study also sought to establish the effects of Itax on tax compliance. The specific variables analyzed were Electronic Tax Registration, Electronic Tax Return Processing, and Electronic Tax System payments. The summary of these findings is presented in table 4.8.

Table 4.8 Effects of Itax on tax compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Likert Mean
Electronic Tax Registration; Our business has registered on Itax	6%	11%	4%	44%	35%	3.79
Electronic Tax Return Processing; iTax filing has reduced our company's costs considerably.	4%	10%	5%	40%	41%	3.89
Electronic Tax Return Processing, I find using iTax system quite friendly	11%	19%	2%	38%	30%	3.51
Electronic Tax Return Processing; Most of our taxes are filed online	7%	15%	8%	25%	45%	3.62
Electronic Tax System payments; eases tax payments	8%	17%	3%	30%	42%	3.72
Electronic Tax System Payments; Are more accurate	9%	16%	9%	12%	54%	3.59
Electronic Tax System payments Update ledger in real time	15%	12%	6%	29%	38%	3.45
Overall Likert mean						3.65

Source: Research Findings (2019)

4.7.1 Effects of Itax on tax compliance

From the findings 79% of the respondents agreed that Electronic Tax Registration; Their businesses have registered on Itax, 81% of the respondents agreed that Electronic Tax Return Processing; I-Tax filing has reduced our company's costs considerably, 68% of the respondents

agreed that Electronic Tax Return Processing, I find using ITax system quite friendly , 70% of the respondents agreed that Electronic Tax Return Processing; Most of our taxes are filed online, 72% of the respondents agreed that Electronic Tax System payments eases tax payments, 66% of the respondents agreed that Electronic Tax System Payments are more accurate, 67% of the respondents agreed that Electronic Tax System payments ; Update ledger in real time tax .The overall mean was 3.65, which implied that Itax implementation had a positive effect on tax compliance. These findings agree by a study done by Fincham J.E.,2008 that ITax enables taxpayers to avoid the hassles of visiting the tax offices, wasting time on queues and having direct contact with tax officials. His further findings established that ITax has made corporation tax compliance simple by ensuring that the annual returns that involve entering substantial data from audited financial statements cannot be submitted with an error as the ITax system would not accept the upload and directs the taxpayer to what could be wrong with the record they have input.

4.8 Tax Compliance

The study also sought to establish the indicators of tax compliance and the extent to which SMEs are tax compliant. The specific variables analyzed were Tax Registration of SMEs, Filing of Tax Returns by SMEs, Tax Reporting by SMEs, and Tax Payments by SMEs. These findings are summarized in table 4.9.

Table 4.9 Indicators of Tax Compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Likert Mean
Our company has been registered with the KRA online system	31%	37%	7%	15%	10%	2.15
Our company files its tax returns on time	31%	48%	8%	5%	8%	1.87
Our company reports the correct tax at the KRA portals	27%	48%	2%	8%	15%	2.3
Our company is Tax compliant with the tax payments to KRA	35%	38%	9%	12%	6%	1.89
Overall Likert mean						2.05

Source: Research Findings (2019)

4.9.1 Indicators of Tax Compliance

From the findings 25% of the respondents agreed that their company has been registered with the KRA online system, 13% of the respondents agreed that their company files its tax returns on time, 23% of the respondents agreed that their company reports the correct tax at the KRA portals, 18% of the respondents agreed that their company is Tax compliant with the tax payments to KRA. The overall mean was 2.05, which implied that most of the SMEs are not Tax Compliant. These findings agree by a study done by the Kenya Parliamentary Budget Office (2011) that SMEs make up 98% of all registered businesses in Kenya, contribute 34 per cent to GDP, and with tax potential of Kenya shilling 79 billion but actual collection is less than one billion; which shows they are not compliant and (Mage,2012) who established that the SMEs have continued to be non-compliant.

4.8.4 Correlation of Independent and Dependent Variables

A correlation analysis was done to ascertain how independent variables, i.e. Withholding VAT (X_1), Rental Income Tax (X_2), and I-Tax (X_3) influence the dependent variable, SMEs tax compliance (Y). Multiple regression analysis was subsequently done to establish the kind of relationship that existed between the independent and dependent variables. The correlation matrix in Table 4.10 illustrates the relationship among independent variables and the dependent variable.

Table 4.10 Multiple Correlations

		Withholding VAT (X ₁)	Rental Income Tax(X ₂)	I-Tax (X ₃)
Withholding VAT (X ₁)	Pearson Correlation	1	.262 [*]	.002
	Sig. (1-tailed)		.010	.493
	N	198	198	198
Rental Income Tax (X ₂)	Pearson Correlation	.262 [*]	1	.267 ^{**}
	Sig. (1-tailed)	.010		.009
	N	198	198	198
I-Tax (X ₃)	Pearson Correlation	.002	.267 ^{**}	1
	Sig. (1-tailed)	.493	.009	
	N	198	198	198

*. Correlation is significant at the 0.05 level (1-tailed).

** . Correlation is significant at the 0.01 level (1-tailed).

Source: Research Findings (2019)

Correlation values that are not close to 1 or -1 show that the factors are sufficiently different measures of separate variables (Farndale, Hope, Haily & Killiher, 2010). It's also an indication that variables are not auto correlated (Farndale *et al.*, 2010). Absence of autocorrelation allows the study to utilize all the independent variables (Farndale *et al.*, 2010). From the correlation matrix in Table 4.10, there was no correlation among independent variables. On the other hand, detection of Tolerance and Variance Inflation Factor (VIF) statistics in Table 4.4 shows no presence of multicollinearity hence allowing the study to utilize all the independent variables (Farndale *et al.*, 2010; Pallant, 2010).

4.8.5 Model Summary

Table 4.11 presents findings of the coefficient of correlation R and the coefficient of determination R square.

Table 4.11 Coefficient of Correlation and the Coefficient of Determination R Square

Model	R	R Square	Adjusted R Square	Std Error of the Estimate
1	.941 ^a	.899	.862	.84395

a. Predictors: withholding VAT, rental income tax, iTax

Source: Research Findings (2019)

Based on the summary in Table 4.11, the coefficient of correlation R is .941, implying that a strong correlation exists between independent variables (predictors) and the dependent variable (outcome). The coefficient of determination R square is 0.899, implying that 89.9% change in tax compliance of SMEs in Mombasa County is explained by the independent variables. There are other factors however - apart from those considered in the study - which influences SMEs tax compliance in Mombasa County by 10.1%. Future studies can therefore focus on this fraction since the study did not address these other factors.

4.8.6 Analysis of Variance (ANOVA)

Analysis of variance (ANOVA) of the regression model was done to determine the correlation between independent variables and the dependent variable. Table 4.12 illustrates that the value of F calculated was 10.45. The value of F critical (5, 202) at 95% confidence level = 2.36, which was less than F calculated. Based on this illustration, it can therefore be inferred that the model used in the study was significant in predicting how the independent variables affected SMEs tax compliance in Mombasa County.

Table 4.12 Analysis of Variance (ANOVA)

Source	Sum of squares	Degree of Freedom (df)	Mean Square	F calculated	Sig.
Model Regression	631.29	5	148.26	10.45	.000 ^b
Residual Error	173.49	202	6.96		
Corrected Total	804.78	198			

a. Tax compliance by SMEs

b. Predictors (Constant): Withholding VAT, Itax, rental tax income

Source: Research Findings (2019)

4.8.7 Regression Coefficients

A multiple regression analysis was also performed in order to establish the strength of the relationship between independent variables and the dependent variable. The regression coefficients with p values of individual variables used in the study are illustrated in table 4.13.

Table 4.13 Multiple Regression Analysis

Predictor	Unstandardized		Standardized	t	Sig.
	Coefficients	Std. Error	Coefficients		
Constant	3.881	1.211	Beta	3.122	0.001
X ₁ (Withholding VAT)	0.135	0.065	0.071	3.613	0.011
X ₂ (Rental Income Tax)	0.127	0.032	0.033	3.012	0.012
X ₃ (Itax)	0.143	0.251	0.471	3.116	0.002

a. Tax compliance by SMEs

Source: Research Findings (2019)

Based on the statistics on table 4.13 above, the following model was established:

$Y = 3.881 + 0.135X_1 + 0.127X_2 + 0.143X_3$, where X_1 represents Withholding VAT, X_2 represents rental income tax, and X_3 represents iTax. From this model, it implies that taking all factors into consideration and at zero, the constant was 3.881 which represents the level of tax compliance by SMEs. From this analysis, it further means that a unit increase in Withholding VAT other factors held constant would lead to a 0.135 increase in tax compliance of SMEs in Mombasa County. A unit increase in rental income tax other factors held constant would lead to 0.127 increases in tax compliance of SMEs in Mombasa County. Finally, a unit increase in iTax factors held constant would lead to 0.143 increases in tax compliance of SMEs in Mombasa County. Furthermore, at 5% significance level, the study can document that Withholding VAT ($p=0.011<0.05$); rental income tax ($p=0.012<0.05$); and iTax ($p=0.002<0.05$) all had significant influence on tax compliance of SMEs in Mombasa County.

Based on the objectives of the study, the first objective aimed at establishing the effects of Withholding VAT on compliance of small and medium-sized Enterprises in Mombasa County. At ($\beta=0.135$, $p=0.011$), it means that a 1% increase in the Withholding VAT was likely to lead to 13.5% improvement on tax compliance by SMEs in Mombasa County. The second objective was to determine the effects of rental income tax reform on tax compliance of small and Medium-sized enterprises in Mombasa County. At ($\beta=0.127$, $p=0.012$), it means that a 1% increase in the rental income tax was likely to lead to 12.7% improvement on tax compliance by SMEs in Mombasa County. The third objective was to find out the effects of Itax on tax compliance of SMEs in Mombasa County. At ($\beta=0.143$, $p=0.002$), it means that a 1% increase in the iTax was likely to lead to 14.3% improvement on tax compliance by SMEs in Mombasa County.

In a general sense, although with varying degrees of their levels of influence, all the three independent variables influenced tax compliance by small and medium enterprises in Mombasa County.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1. Introduction

This chapter presents a summary of the findings, conclusion and recommendations. Policy implications and suggested areas for further studies are also presented.

5.2. Summary of the Findings

The general objective of the study was to assess the effects of tax reforms on compliance of the Small and Medium Enterprises (SMEs) in Kenya, using case of enterprises in Mombasa County. The study formulated three objectives and the findings are discussed in chapter four. The study established that most of the SMEs are dominated by male entrepreneurs who are in late 40s in age and with at least some basic education. Majority of the SMEs operators had considerable experience in that they had been in existence for a while.

5.2.1 Withholding Value added tax

From the findings 79% of the respondents agreed that withholding value added tax had reasonably reduced time spent in tax compliance of the SMEs, 85% of the respondents agreed that withholding value added tax had reduced the financial cost incurred in tax compliance, 75% of the respondents agreed that as a result of withholding value added tax the process of tax compliance was less complex and 67% of the respondents agreed that they were satisfied with the implementation of withholding value added tax. The overall mean was 3.8, which implied that withholding value added tax has had a positive effect on tax compliance. The beta coefficient value for withholding value added tax indicated a value of 0.135 while the coefficient correlation R value was 0.941, implying that a strong positive relationship exists between withholding value added tax and compliance. Thus one unit change in withholding value added tax would affect tax compliance by a coefficient of 0.135.

5.2.2 Rental income Tax

From the findings, 67% of the respondents agreed that Tax Rate; 10% residential rental income tax rate was fair to property owners, 76% of the respondents agreed that Tax Rate; The lowered tax rate had influenced willingness of residential rental property owners to be tax compliant, 68% of the respondents agreed that Fines and penalties are very punitive to property owners, 79% of the respondents agreed that Fines and penalties discouraged non-compliance of residential rental income tax obligations, 68% of the respondents agreed that Fine and Penalties; Periodic waiver of fines and penalties could encourage tax compliance, 73% of the respondents agreed that Knowledge; Knowledge about tax laws plays a major role in determining property owners' tax compliance, 75% of the respondents agreed that Tax Knowledge; Lack of proper records on expenses incurred greatly contributed to non-compliance by property owners in the previous regime, 89% of the respondents agreed that Income levels; Property owners with low income levels are more likely to be non-compliant .The overall mean was 3.68, which implied that Rental Income Tax has had a positive effect on tax compliance. The beta coefficient value for rental income tax indicated a value of 0.127 while the coefficient of correlation R value was 0.941, indicating that a strong positive correlation exists with tax compliance. Thus any rise in rental income tax rates would affect tax compliance by a coefficient of 0.127.

5.2.3 Itax

From the findings 79% of the respondents agreed that Electronic Tax Registration; their businesses have registered on Itax, 81% of the respondents agreed that Electronic Tax Return Processing; I-Tax filing has reduced their company's costs considerably, 68% of the respondents agreed that Electronic Tax Return Processing, I find using iTax system quite friendly , 70% of the respondents agreed that Electronic Tax Return Processing; Most of our taxes are filed online, 72% of the respondents agreed that Electronic Tax System payments; eases tax payments, 66% of the respondents agreed that Electronic Tax System Payments; Are more accurate, 67% of the respondents agreed that Electronic Tax System payments; Update ledger in real time tax .The overall mean was 3.65, which implied that I- tax implementation had a positive effect on tax compliance. The beta coefficient value for Itax indicated a value of 0.143 while the coefficient of correlation R value was 0.941, implying a strong positive correlation exists with tax compliance. Thus any unit change in Itax would affect tax compliance by a coefficient of 0.143.

5.2.4 Compliance

From the findings, 25% of the respondents agreed that their company has been registered with the KRA online system, 13% of the respondents agreed that their company files its tax returns on time, 23% of the respondents agreed that their company reports the correct tax at the KRA portals, 18% of the respondents agreed that their company is Tax compliant with the tax payments to KRA. The overall mean was 2.25, which implied that most of the SMEs are not Tax Compliant.

5.3. Conclusions

This study analyzed the contribution of tax reforms on compliance of the SMEs in Kenya with reference to case of Mombasa County. Based on the findings of study on the effects of the withholding value added tax on tax compliance, it can be concluded that withholding value added tax implementation significantly contributes to the tax compliance of the SMEs in Mombasa County. In relation to Rental Income Tax, it can be concluded that Rental Income Tax influences tax compliance of the SMEs taxpayer's in Mombasa County. Lastly, I-tax positively affects the tax compliance of the SMEs. The study concludes that the tax reforms targeting SMEs have positively resulted in tax compliance by the SMEs, and most SMEs are not tax compliant.

5.4. Recommendations of the Study

5.4.1 Managerial Recommendations

Based on the study's findings, the following recommendations are made on the effects of the implementation of tax reforms on compliance of the SMEs in Mombasa County. The findings in objective one indicated that withholding value added tax have significant effect on the compliance of the SMEs. This study recommends that more resources be put on the withholding value added tax to bring more SMEs who are non-compliant into tax bracket. There should be continuous emphasis on withholding value added tax among the SMEs by the KRA. SMEs business should embrace online filing and payments.

The findings in objective two indicated that there was a positive relationship between Rental Income Tax and compliance. KRA should do more in implementing the Rental Income tax,

provide knowledge, incentives and opportunity for compliance. More audits and checks should be carried out to ensure Rental Income Tax compliance by SMEs.

The finding from the last objective was that there is positive relationship between I-tax and tax compliance of the SMEs in Mombasa County. The training on the I-tax system should be done for SMEs owners as this increases tax compliance. KRA should work together with public and other stakeholders in encouraging good accounting practices.

5.4.2 Policy Recommendations

The main theme of the study was to establish effect of tax reforms on compliance of small and medium enterprises in Kenya, with reference to case of Mombasa County. A study of tax compliance among the SMEs is important for policy makers, policy implementers, practitioners and the SMEs businesses in Kenya. Since the findings and recommendations revealed that tax reforms are important in enhancing compliance among the SMEs in Kenya, it means that tax laws should be further reviewed and strengthened to seal loopholes, which are being exploited by the non-compliant SMEs. More awareness on the tax compliance among the SMEs should be enhanced and a policy which clearly classify an entity as a SMEs be implemented. There is need for the government to enhance SMEs' trust with the tax reforms for voluntary compliance. The government should use besides audits and fines more psychological factors to change tax behaviors of the SMEs for instance tax reforms awareness, personal and social norms, distributive and procedural fairness.

5.4.3 Suggestions for Further Research

Since this study focused majorly on the SMEs in Mombasa county, a similar study can be carried out to assess the factors affecting tax compliance SMEs in Kenya as a whole. Another study can be carried out on SMEs in other region across the country. In addition, future researchers can focus on carrying out a study on Itax implementation and its effect on tax compliance in Kenya as a whole. The evasion of tax is one of the major problems facing Kenya Revenue Authority. In most cases, the government has lost a lot of revenue through tax evasion. Hence, further research on tax evasion and tax education would be necessary.

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APPENDIX

Appendix I: Work plan

Time	July	Aug	Sept	Oct	Nov	Dec	Jan	Feb
Activity	2018	2018	2018	2018	2018	2018	2019	2019
Search for research topic								
Analysis of the topic feasibility for research								
Proposal writing and subsequent rectifications after approval by the supervisor								
Proposal defense								
Data collection								
Data analysis								
Writing final research project								
Final project defense								

Appendix II: Budget

Activity	Amount in KES
Photocopying of research materials and internet services	5,000
Research proposal preparation i.e. printing and binding	5,000
Final research project document preparation i.e. printing and binding	10,000
Total Amount	20,000

Appendix III: Questionnaire

SECTION A : GENERAL INFORMATION

1. What is your Gender

Male Female

2. What is your Age bracket?

20-30 years 30-40 years 40-above years

3. What is your highest level of education?

No Formal Education Certificate Diploma Degree Post Graduate

4. What is your business structure?

Sole proprietorship Partnerships SACCOs Limited Company

5. What is your work experience?

Less than 2 years 2-3 years 4-6 years 7-8 years 9-10 years

More than 10 years

SECTION B: WITHHOLDING VAT SYSTEM AND TAX COMPLIANCE

How has withholding value added tax contributed to enhancement of tax compliance of SMEs operating in Mombasa County.

Effects of withholding value added tax on Tax compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
Withholding VAT has reduced the time required in Tax compliance					
Withholding VAT has reduced the cost incurred during tax filing					
Withholding VAT has made the compliance process less complex					
More of the business owners are satisfied with withholding VAT					

SECTION C: RENTAL INCOME TAX AND TAX COMPLIANCE

How has rental income tax enhanced tax compliance of the SMEs in Mombasa County. The specific Rental Income Tax Aspects measured are tax rate, fine and penalties, tax knowledge, income levels

Effects of Rental income Tax on Tax Compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
Tax Rate; 10% residential rental income tax rate is fair to property owners					
Tax Rate; The lowered tax rate has influenced willingness of residential rental property owners to be tax compliant					
Fine and Penalties; Fines and penalties are very punitive to property owners					
Fine and Penalties; Fines and penalties discourage non-compliance with of residential rental income tax obligations					
Fine and Penalties; Periodic waiver of fines and penalties could encourage tax compliance					
Tax Knowledge; Knowledge about tax laws plays a major role in determining property owners' tax compliance					
Tax Knowledge; Lack of proper records on expenses incurred greatly contributed to non-compliance by property owners in the previous regime					
Income levels; Property owners with low income levels are more likely to be non-compliant					

SECTION D: ITAX ON TAX COMPLIANCE

Effects of the Itax System on Tax compliance. The specific variable analyzed were Electronic Tax Registration, Electronic Tax Return Processing, Electronic Tax System Payments.

Effects of Itax on Tax Compliance

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
Electronic Tax Registration; Our business has registered on Itax					
Electronic Tax Return Processing; iTax filing has reduced our company's costs considerably.					
Electronic Tax Return Processing, I find using iTax system quite friendly					
Electronic Tax Return Processing; Most of our taxes are filed online					
Electronic Tax System payments; eases tax payments					
Electronic Tax System Payments; Are more accurate					
Electronic Tax System payments ; Update ledger real time					

SECTION E: TAX Compliance

How does tax compliance of the SMEs impact on the collection. of taxes ?

Tax compliance

Statement	Strongly disagree	Disagree	Agree	Strongly agree
Our company has been registered with the KRA online system				
Our company files its tax returns on time				
Our company reports the correct tax at the KRA tax portals				
Our company is compliant with the tax payments to KRA				