DETERMINANTS OF TAX COMPLIANCE AMONG SMALL AND MEDIUM ENTERPRISES IN NAKURU CENTRAL BUSINESS DISTRICT, KENYA

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DECLARATION

This research Project is my original work and has not been presented for examination or award of any Degree in any academic institution.

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ABSTRACT

The main problem facing tax authorities in any jurisdiction lies in persuading all tax payers to comply with obligations put on them by any tax system. Tax is an important stream of revenue for government's development projects and therefore all efforts must be made by governments to ensure that it is accurately and efficiently collected so as to facilitate the government's operations. Unfortunately, Kenya Revenue Authority does not collect all the taxes that it ought to. This is attributed to high levels of tax non-compliance. In Kenya, the biggest block of taxpayers on the business sector were Small and Medium Enterprises (SMEs) which were estimated to contribute about 45% of GDP in Kenya and they account for 85% of employment statistics. This study intended to identify the factors that influence tax compliance, specifically focusing on SME's operating in Nakuru CBD. Small businesses played an important role in the tax system as it was the fastest growing sector in the Kenyan economy however non-compliance to the National tax system and County government tax systems continued to plague the sector. Guiding specific objectives were to determine; effects of tax education and knowledge, compliance costs, perceived opportunities to evade taxes and the penalties and fines imposed by tax authorities and how they affect tax compliance levels. To achieve the objectives, the study employed a survey design approach. A sample size of 212 SMES was picked as a representative of the population of 3506 licensed SMEs operating within the Nakuru CBD. To ensure that various diverse categories of taxpayers and business entities were included in the survey, stratified sampling technique was adopted. The data collection instruments were self-administered structured questionnaires. Data collected was analyzed using descriptive and inferential statistics with the aid of SPSS package. The findings of the study revealed that perceived opportunity for tax evasion has no statistically significant effect on tax compliance among SMEs $\chi^2 =106.873$, Prob> $\chi^2 =0.254$). There exist a statistically insignificant, negative relationship between perceived opportunity for tax evasion and tax compliance (rho= -0.026; p>0.05). Tax knowledge and education has no statistically significant effect on tax compliance among SMEs ($\chi^2 =90.735$, Prob> $\chi^2 =0.838$), while there exist statistically insignificant, negative relationship between tax knowledge/education and tax compliance (rho= -0.031; p>0.05). It was established that fines and penalties has statistically significant effect on tax compliance among SMEs ($\chi^2 = 131.098$, Prob> $\chi^2 =0.043$), while there exist statistically insignificant, negative relationship between fines/penalties and tax compliance (rho= -0.038, p>0.05). It was proved that tax compliance cost has no statistically significant effect on tax compliance among SMEs $\chi^2 =110.474$, Prob> $\chi^2 =0.183$). There exist a statistically insignificant, negative relationship between perceived opportunity for tax evasion and tax compliance (rho= 0.024; p>0.05). It is recommended that The Kenya revenue authority should ensure revenue streams are tracked by involving financial institutions since majority as well as enhance its manpower to ensure monitoring and tracking of all income reported by SME operators.

Keywords: *Tax-compliance, Compliance Cost, Fines, Penalties, tax knowledge, Perceived opportunity, Small and medium businesses (SMEs).*

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LIST OF ABBREVIATIONS

C.B.D. -   Central Business District

ETR -   Electronic Tax Register

G.O.K -   Government of Kenya

GDP -   Gross Domestic Product

KIPPRA -   Kenya Institute of Policy Research Analysis

KNBS -   Kenya National Bureau of Statistics

KRA-   Kenya Revenue Authority

OECD -   Organization for Economic Co-operation and Development

PAYE -   Pay As You Earn

PIN -   Personal Identification Number

SMEs -   Small and Medium Enterprises

SPSS -   Statistical Package for Social Sciences

TOT -   Turnover Tax

VAT -   Value added Tax

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CHAPTER ONE
INTRODUCTION

1.1 Background of the Study

Tax is a compulsory levy payable by an economic unit to the government with no quid pro quo to the taxpayer. It dates back to the biblical times of King Pharaoh where Israelites used to pay taxes to Egyptians where they were in captivity. Further, In the New Testament, Jesus is asked if it is right to pay tax and alleged, give to Caesar what is Caesars and to God what belongs to God (Matthew 22:21, Holy Bible), In Kenya, the colonialists imposed hut tax where each household used to pay certain amounts of money to the Governor. The 1901 Hut Tax Regulation imposed a tax of one rupee, payable in kind or through labor, upon every native hut in British East Africa. A subsequent amendment to the law allowed the tax to be levied specifically upon the owner of the hut (Waris, 2011).

The Kenya Revenue Authority (KRA) was formed on 1st July 1995 as government agency with the mandate of collecting taxes on behalf of the Government of Kenya. It collects a number of taxes and duties, which include turnover tax, income tax, value added tax, custom duty, excise duty, stamp duty and ministerial and departmental taxes (Thiga & Muturi, 2015). Since KRA's inception, revenue collection has increased noticeably, enabling the government to provide much needed services to its citizenry. These include: free primary education, maternity services and anti-retroviral medication, defense, preservation of culture, infrastructure, health and social welfare, agricultural development, fund research, tourism recovery, increase employment and payment of workers, protection of local industries, county government allocation and county development funds (Ali 2014).

Kenya's tax system has undergone more or less continual reform over the last twenty years. On the policy side, rate schedules have been rationalized and simplified, a new value-added tax introduced, and external tariffs brought in line with those of neighboring countries in East Africa. At the same time, administrative and institutional reforms have taken place. Most remarkable among these is the creation of the semi-autonomous Kenya Revenue Authority (KRA) in 1995, which centralized the administration of tax collection (Mawia & Nzomoi 2013).

The responsibility of the government to finance public services lies therefore at the heart of taxation. Applying canons of equity, simplicity, certainty, convenience, productivity, elasticity, diversity, flexibility, neutrality, economic and administrative efficiency to tax payers, KRA has been able to collect and grow taxes efficiency, effectiveness and progressively (Ngigi, 2015). The tax systems and the spending of government resources creates a virtuous circle of improving fiscal performance, good governance, fair distribution of public goods and services, and ultimately strengthens state legitimacy. It promotes compliance with Kenya's tax, trade, and border legislation and regulation by promoting the standards set out in the Taxpayers Charter and responsible enforcement by highly motivated and professional staff thereby maximizing revenue collection at the least possible cost for the socio-economic well-being of Kenyans (KRA Annual Report, 2013/2014).

Tax collection has been progressive in nature where KRA has collected Cumulative revenue in the period July 2013 - June 2014 Kshs. 963.8 billion compared to Kshs. 800.5 billion collected in the period July 2012 - June 2013 which represented a revenue growth of Ksh. 163.3 billion or 20.4 percent. To finance the KSh. 2.234 trillion budgets for this financial year, the government expects to raise KSh. 1.358 trillion from ordinary revenue during the period (Alshir'ah, Abdul-Jabbar & Samsudin (2016); Kenya Financial budget, 2015). Taxes play an important role in the budget of any economy and one of the main reasons why the governments impose taxes is to get incomes to manage the economy and redistribute resources (Stiglitz & Rosengard (2015).

Over the years, the Kenyan government has undertaken various revenue administration reforms aimed at enhancing revenue collection. One of the measures that have been implemented in order to increase revenue collection in Kenya was the introduction of self-assessment systems (SAS) in 1992. The objectives of this system was to increase voluntary compliance, reduce tax authorities" burden of assessing tax returns and increase tax collection efficiency/reduce tax collection costs (Osebe 2013; Masinde & Makau, 2010). In Malaysia, on the 1st of January 2005, in order to promote voluntary tax compliance, the Inland Revenue Board Malaysia (the IRBM) implemented the self-assessment tax system (the SAS) on individual taxpayers (Fatt & Khin 2011).

Under the SAS, individual who have income accruing in or derived from Malaysia are required to disclose taxable income honestly, compute tax payable correctly, file tax

return form and pay tax on a timely manner (Fatt & Khin 2011). In a nutshell, under SAS, the onus to assess the tax liability is on the taxpayers (Fatt & Khin 2011). As a result, taxpayers must have sufficient tax knowledge in order to assess their tax liability correctly and to file tax return forms on time (Fatt & Khin 2011). Despite various administrative reforms, levels of tax compliance have remained as a study conducted by KRA, KIPPRA and the Treasury, based on 1999/2000 data revealed that VAT payment compliance was 55% while return lodgment compliance was 65% (Muyundo, 2012).

Small businesses are responsible for collecting as well as for remitting taxes Akinboade (2015); (Sumartaya & Hafidiah, 2014). They are, hence, important players in a country's tax system. (Hanlon et al., 2007; Rice, 1992) suggests that SMEs are more likely to cheat than other groups of taxpayers (Walsh, 2013). Even the (OECD, 2004) considers small businesses a high-risk group in terms of tax compliance. In many cases it is impossible to prove non-compliance. Kenya Revenue Authority estimates that only half of corporate non-compliance is detected (Okello, 2014), and that tax audits are generally a costly matter. Increasing voluntary compliance among small businesses is thus a worthwhile endeavour. In order to do so, an in-depth understanding of the factors fostering non-compliance is essential. While paying taxes is likely to be an important topic for small businesses, the actual experience of paying taxes and small businesses' tax behaviours have received surprisingly little attention in the small business literature (Rothengatter, 2005; Williams, 2005).

Tax noncompliance is a substantive universal phenomenon that transcends cultural and political boundaries and takes place in all societies and economic systems. There are many studies that explain the behavior of tax compliance in a more realistic situation. They focus on the determinants of tax compliance, respectively on economic and non-economic factors (Nicoleta, 2011). Tax compliance and non-compliance is an area of concern for all government and tax authorities, and it continues to be an important issue that must be addressed. Regardless of time and place, the main issue faced by all tax authorities is that it has never been easy to persuade all taxpayers to comply with the regulations of a tax system (Mararia 2014). In contrast to the majority of employed people whom in many countries are paid net salaries with taxes being deducted at source SMEs often need to self-assess and self-report their income and pay taxes "out of their pocket.

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SMEs not only pay their income tax but need to take account of various types of business taxes such as corporate tax, property taxes, and payroll taxes; they need to collect sales taxes such as VAT; and they need to withhold taxes such as personal income taxes in the case of having at least one employee (Djankov, Ganser, McLiesh, Ramalho & Shleifer, 2010). While previous studies on tax compliance have focused on the general factors affecting tax compliance, the focus of this study is on the factors affecting tax compliance in the SME sector in Nakuru. The study specifically seeks to determine the effect of tax compliance cost, tax education and knowledge, fines and penalties and perceived opportunity for tax evasion on tax compliance in the SME sector in Nakuru Kenya.

1.2 Statement of the Problem

According to (Atawodi & Ojeka, 2012) tax non-compliance among businesses in developing countries is the major cause of revenue collection shortfalls by their tax authorities. Mage, (2011) further asserts that despite these SMEs tax reforms, most developing countries where SMEs sector account for such a significant percentage of GDP (average 41%) continue to be tax non-compliant. In Kenya's case many small and medium businesses' are not fully compliant to the existing tax regulations; they do not register voluntarily, while those who do register often fail to keep adequate records, file tax returns, and settle their tax liabilities promptly according to Commissioner General, John Njiraini (2015). According to figures from (KRA 2010), SME taxes declaration declined from 15 Billion in 2007 to 10 Billion in 2009.This is despite the requirement that SMEs register for VAT on commercial business with turnovers above 500000 Kenyan shillings per annum, while those that fall short of those parameters are subject to sales turnover tax of 3% of gross sales (Mwangi, 2014).

In the Budget speech of 2015/2016, the Finance Minister instructed KRA to intensify revenue collection in this sector. There is therefore a need to assess the level of tax consciousness, review factors causing non-compliance and capture the expectations of the taxpaying public with a view to formulating strategies aimed at enhancing tax collection in this sector. It is against this background that this study has been undertaken with the aim of analyzing factors affecting tax compliance in the SME sector and recommend measures to be put in place by the government and KRA to enhance tax collection in this booming sector.

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SMEs are often mentioned as a high-risk group in terms of tax compliance because their opportunities to evade are high (Kamleitner Et.al 2012). Commissioner General of KRA John Njiraini, (2015) small businesses that are now the target for recruitment into the tax database do not keep adequate records; neither do they file their annual tax returns. In the small business context, opportunities for evasion are high and resources often scarce for field auditing therefore KRA have opted for a friendly approach in dealing with the taxpayers. A high percentage (45%) of SMEs according to past researches within Kenya have been found out to be non- compliant (tax evasion) to the various tax nets that they fall under (Woodward & Tan 2015). Tax non-compliance is often hard to prove. Consequently, measures beyond tax audits are needed to tackle non-compliance (Tusubira & Nkote, 2013). The same case applies to Nakuru County therefore this research proposal seeks to investigate the causal factors contributing to non-compliance and recommend solutions to avert the same.

1.3 Objectives of the Study

1.3.1 General Objective

To identify determinants of tax compliance among Small and Medium Enterprises in Nakuru central business district, Kenya.

1.3.2 Specific Objectives

This study was guided by the following specific objectives:

i.   To determine effects of perceived opportunity for tax evasion on tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

ii. To identify if tax knowledge and education affects tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

iii. To determine effects of fines and penalties on tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

iv. To examine effects of compliance cost on tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

1.4 Research Hypotheses

H_{01}: Perceived opportunity for tax evasion has no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

H_{02}: Tax knowledge and education has no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

H_{03}: Fines and penalties have no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District.

H_{04}: Tax compliance cost has no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District

1.5 Significance of the Study

Many other researchers have predominantly dwelt on qualitative research that focus on aspects of entrepreneurship other than taxpaying, for example human resource management (Boll 2014), the entrepreneurial experience (Graham, Hanlon, Shevlin & Shroff 2013), or social processes of entrepreneurial innovation (Peng, 2016). This study seeks contribute to the quest of furthering the understanding of SMEs' tax compliance by pointing out that tax decisions tend to be made by and are personally relevant to SMEs, who can be characterized as individual decision makers. It follows from such a conceptualization that tax decisions are susceptible to psychological influencers. This reasoning forms the basis for what is considered the main contribution of this project: in a conceptual framework to identify the main and unique characteristics (perceived non-compliance opportunities, tax knowledge/education requirements, and compliance cost) that may inform SME' perceptions of and reaction to taxation.

The government raises tax revenues to finance public security, health, education, and infrastructure. In this regard, the government has to ensure that its source of revenue is effective and efficient. The findings of this study will help the government to institute the necessary legislative and administrative measures to enhance tax compliance in cases of voluntary compliance and enforce compliance in cases of non-compliance. Kenya Revenue Authority is interested in maximizing revenue collections and thus will find the study useful in instituting measures, policies, and initiatives to address or minimize non-compliance and thus enhance revenue collection. Tax Practitioners assist taxpayers to

interpret the complicated tax laws and help them to apply the law to their tax returns. This study will be of help to practitioners since it helps them understand various challenges faced by taxpayers towards voluntary compliance and help them advice their clients accordingly.

The study is of importance to the general public since it will highlight various challenges faced by taxpayers the in the quest towards full compliance and the possible solutions to these challenges. To other researchers the survey is a basis for further research, more so, when seeking to research on enhancing revenue collection through other systems that either supplement or substitute self- assessment system.

1.6 Scope of the Study

The study focused on factors influencing small business' tax compliance and was geographically limited to Nakuru town. The target population was SMEs operating within the Nakuru CBD. The study was conducted between March and April 2017.

1.7 Limitations and Delimitations of the Study

This study dealt with people as respondents and given the weighty matters of financial information and tax compliance issues the researcher expected some resistance by respondents to volunteer information. To curb this limitation, the researcher worked to gain their trust by reassuring the respondents' of their confidentiality. This study was limited to respondents within Nakuru town. This research was limited to the tax compliance factors. The main research objective, relevance and significance was explained to the respondents and identity of respondents or their responses were treated with utmost confidentiality.

1.8 Definition of Operational Terms

Small, Medium Enterprises: These are firms that have a labour force of less than 100 employees in their total operations (Moreno Et.al 2015). This proposal adopts the same meaning.

Tax compliance : Tax compliance is defined as the adherence to the administrative rules of lodging and paying taxes on time. This includes compliance with the reporting requirements, procedural rules and regulations. This entails filing tax returns on time, reporting all the income and claiming the right deductions and where taxes are due making tax payments on time full payment of all taxes due (Braithwaite, 2009). The study adopts the same meaning.

Tax compliance costs: (Eichfelder, & Schorn, 2012) defined TCC as all the costs borne by businesses and individuals for complying with tax regulation, excluding the costs of the taxes themselves. To comply with tax provisions, both businesses and individuals bear tax substantive costs (e.g. they might need to purchase specific software to fill in tax returns (Brink & Lee 2014) and tax administrative costs. The study adopts the same meaning.

Tax Non-compliance: Comprises both intentional evasion and unintentional non-compliance, which is due to calculation errors and an inadequate understanding of tax laws (Tanui, 2016). Taxpayer mistakes can be unintended and, thus, do not necessarily represent attempts to evade (Machogu, 2015) or may even lead to tax over-reporting. The study adopts the same meaning.

Tax Rates: Tax rates refer to the rate at which a business or person is taxed on income. It also refers to the rate of tax on goods and services (Nyaga, Omwenga, Murugi, Shalle, Ndung'u,

Gekara&Wairimu 2016). The study adopts the same meaning.

Tax Audits: This is an exercise undertaken by tax authorities to determine if a taxpayer paid the correct amount of tax (Ayuba, Saad & Ariffin 2016). The study adopts the same meaning.

Fines and Penalties: According to Oladipupo & Obazee (2016) a fine or penalty is money paid usually to a government authority, as a punishment for a crime or other offence. The study adopts the same meaning.

Tax incentives: According to Abeler & Jäger (2015) a tax incentive is an aspect of the tax code designed to incentivize, or encourage, a certain type of behavior. The study adopts the same meaning.

Tax avoidance: Armstrong, Blouin Jagolinzer & Larcker (2015) Refer to the legal reduction in tax liabilities by practices that take the full advantage of the tax code, such as income splitting and postponement of taxes for example through contribution to a Home Ownership Savings Plan. The study adopts the same meaning.

Tax evasion: Hanlon, Maydew & Thornock (2015) Refer to tax evasion as the illegal and intentional actions taken by individuals to reduce their legally due tax obligations. The study adopts the same meaning.

CHAPTER TWO

LITERATURE REVIEW

2.1 Theoretical Literature Review

This chapter covered the concept of Tax compliance, tax compliance models, Factors influencing Tax non- Compliance and the Conceptual Framework.

2.1.1 Prospect Theory

The theory was advanced in 1979 and developed in 1992 by Daniel Kahneman and Amos Tversky as a psychologically more accurate description of decision making, compared to the expected utility theory. In the original formulation, the term prospect referred to a lottery. The paper "Prospect Theory: An Analysis of Decision under Risk" (1979) has been called a "seminal paper in behavioral economics" (Hashimzade, Myles & Tran-Nam 2013). The Prospect Theory is a behavioral economic theory that describes the way people choose between probabilistic alternatives that involve risk, where the probabilities of outcomes are known. The theory states that people make decisions based on the potential value of losses and gains rather than the final outcome, and that people evaluate these losses and gains using certain heuristics. The model is descriptive: it tries to model real-life choices, rather than optimal decisions, as normative models do.

This theory suggests that people are more risk-seeking in the loss domain than in the gain domain. For SMEs, it might, thus, not only be painful to pay taxes, but the loss framing might also make them risk-seeking. Tax non-compliance could be a consequence. However, as Chang et al. (1987) point out, there are other possible decision frames. Taxpayers can either view the compliance decision as a choice between a certain loss (tax payment) and a possible larger loss (tax payment plus penalty if audited); or they can view it as a choice between a certain reduced gain (net income after tax payment) and a possible larger gain (gross income without tax payment if not audited). Chang et al. (1987) designed a tax lottery and asked executive MBA students how they perceived the lottery whether they applied a "loss frame" or a "gain frame."

Those applying a loss frame were significantly more risk-seeking; more likely to report to gain less from the government than what they paid; more aware of tax evasion practices among others; more knowledgeable about taxation; younger than those applying a gain frame; and, most importantly, more likely to belong to the group of

SMEs in the lottery experiment. A related stream of literature might further explains why SMEs apply the painful loss frame. SMEs are required to carry out accrual accounting. This necessitates long-term planning and, hence, anticipating and planning for additional tax payments. (Cullis, Jones & Savoia 2012) found in their study using scenario techniques that even if the self-employed were given information that allowed them to anticipate additional tax payments or refunds, this information did not influence behaviour.

Upon being informed about the outcome of their tax returns, they generally reacted with increased compliance towards tax refunds and with decreased compliance towards additional tax payments. Conversely, SMEs were sensitive towards information on expectations. Expected refunds had a positive effect and expected payments had a negative effect on compliance, whereas neither unexpected refunds nor unexpected payments had an impact on self-reported tax compliance. Differential framings of tax payments matter in particular for small businesses' tax compliance. SMEs are more likely to frame paying taxes as the loss of something that was previously theirs even if they act as collectors only and they are more likely to view paying their taxes as a burden. In addition, SMEs are frequently made aware of these limiting losses by experiencing an additional "loss" (tax payment) after tax filing (Lio & Mirichii, 2014).

2.1.2 The Theory of "Mental Accounting"

Thaler advanced the Mental Accounting theory in 1985. (Thaler, 1985; Thaler, 1999) refers to the cognitive processes that individuals use to keep track of and group (monetary) costs and benefits. Mental accounts constitute frames for outcomes that influence the perception of these outcomes. Only if taxes are perceived as different from other streams of income, hence are booked to different mental accounts will they be treated differently? As long as taxes due are seen to form part of the mental income account, paying taxes hurts and is perceived as reducing income. Even for taxes that only need to be collected and transferred, such as VAT, mental accounting might come into play and have an impact on how willingly taxes are handed over. (Muehlbacher, Hartl & Kirchler, 2015).

A UK survey among business owners, and a business simulation study reported by (Naibei & Siringi, 2011) supported the assumption that many business owners regarded themselves as owners of VAT money (at least at some point in time) while only a

minority viewed themselves as collectors. The perception of ownership indicates that tax money is not held in a separate mental account but mentally booked to accounts holding income. Perceiving VAT money as belonging to oneself was related to stronger inequity perceptions of the tax system (Muehlbacher et al. 2015) and to increased (self-reported) non-compliance (Naibei & Siringi, 2011).

The perception of VAT money as something "briefly owned then taken" may explain the dislike many SMEs reported paying VAT (Muehlbacher et al. 2015). Another line of argument for differential framing by SMEs can be derived from "reactance theory" (Brehm, 1966). Paying taxes can be perceived as a reduction of one's own financial resources and as a limitation of one's financial freedom. The perception of taxes as a limitation of financial freedom is particularly likely in response to experiencing tax payments as "out of pocket" losses. As a consequence SMEs are more likely to experience and frame taxes as threats to their personal freedom than other groups of taxpayers (Sumartaya & Hafidiah, 2014). Brehm's (1966) reactance theory suggests that people respond to a perceived loss of freedom by reactance and by endeavours to re-establish the lost control. One way to achieve this in the context of taxes is non-compliance.

Evidence on the role of perceived limitation of freedom is mixed. On the one hand, (Ng'eni, 2016) found that for entrepreneurs the word tax evokes associations indicating a perceived threat of freedom (punishment, disincentives to work, and public constraints) more often than for blue and white collar workers, civil servants, and students; and a survey of business owners (Sumartaya & Hafidiah, 2014) found a direct and strong link between perceived limitation of freedom and hypothetical tax evasion (although no link of perceived limitation of freedom and tax attitudes and morale was found). On the other hand, (Yesegat & Fjeldstad 2016) found no relation between perceived limitation of freedom and hypothetical tax behaviour. The specific tax situation of SMEs is likely to make paying taxes even more painful: compared with other taxpayers and at the time of tax filing, they seem to be more likely to face an outstanding tax balance rather than a refund (Ahmed and Braithwaite, 2005).

The impact of additional tax payments and refunds on compliance is well documented. A 1988 US Internal Revenue Service report referred to by (Kamleitner, Korunka & Kirchler, 2012) indicated that voluntary tax compliance varied depending on whether a

refund or an additional payment was due and depending on the size of such a refund or payment. SMEs who claimed substantial refunds (more than $1,000) were significantly more compliant (95 per cent) than those facing an equally substantial balance due (70 per cent). This is corroborated by survey studies (Ahmed and Braithwaite, 2005; Mas'ud, Aliyu, Gambo, Al-Qudah & Al Sharari, (2014), by an experimental business simulation carried out in six different countries (Kamleitner, Korunka & Kirchler, 2012) and by several experiments (Brink & Lee 2014).

There are even some empirical indications that tax preparers exploit the positive effects of tax refund frames. Those who have their taxes professionally prepared are more likely to receive refunds. Tax professionals may do this on purpose (Jackson et al., 2005). Receiving a refund increases taxpayers' willingness to pay for tax services (Lowe et al., 1993). Few studies conducted in this area distinguish between different types of businesses. (Sumartaya & Hafidiah, 2014) contrasted self-employed persons and SMEs in order to find out whether they framed tax payments and refunds differently. They reasoned that differences in accounting principles implied by tax codes might influence the reference point applied.

2.2 Empirical Literature Review
This section contains past empirical studies relating to study variables.

2.2.1 Perceived Opportunities for Tax Evasion and Tax Compliance
SMEs are often mentioned as a high-risk group in terms of tax compliance because their opportunities to evade are high. Opportunity has often been documented as a major explanatory factor in non-compliance (Kamleitner, Korunka & Kirchler, 2012). In particular, if incomes are not subject to automated third-party reporting, or if taxes are not withheld at source (in cases of receiving gross incomes or cash payments), opportunities to evade taxes exist (Engström, Nordblom, Ohlsson, & Persson, (2015); Shane, 2003; Williams & Round, 2009). The link between opportunity and non-compliance seems to have at least two different facets. First, in cases where people do not deliberately capitalize on opportunities, the specific circumstances leading to evasion opportunities might still lead to non-compliance. Opportunities usually come about when tax filings are not entirely automated. Through the lack of automation tax filing procedures are more likely to become error prone even without intent to capitalize on the entailed opportunities.

Consequently, opportunities may lead to an increase in intended as well as unintended non-compliance. (Kamleitner, Korunka & Kirchler, (2012) shows that an experimentally induced opportunity to cheat (more possibilities to deduct non-deductible expenses) increased non-compliance regardless of whether the participants actually intended to be non-compliant or not.

Secondly, assuming that people are willing to capitalize on opportunities, they are able to do so only if the opportunities are recognized in the first place. However, opportunities to evade often tend to remain unnoticed. While many taxpayers perceive opportunities for evading small amounts, only a minority perceives opportunities for evading larger amounts (Kamleitner, Korunka & Kirchler, 2012). Such failure to perceive opportunities even persists in laboratory experiments explicitly manipulating opportunity. Whereas controlling for intended evasion the effect of opportunity on evasion, simultaneously controlling for intended evasion and perceived opportunity re-established the main effect of opportunity on non-compliance (Kamleitner, Korunka & Kirchler, 2012). Indeed, it has been shown that those actually evading perceive increased opportunities to do so (Ashby et al., 2009; Engström et al. 2015). Overall, actual opportunities can increase both intentional and unintentional evasion. Although such a distinction is theoretically and practically meaningful, it is difficult to determine whether filing errors were intentional or not. For example, in a study by (Slemrod & Weber, 2012), taxpayers were informed that their tax files would be closely examined. Those with considerable opportunities to evade, including SMEs, reacted to this message by increasing their tax payments significantly.

Even though this might indicate severe tax evasion as assumed by (Slemrod & Weber, 2012) increased tax payments in response to the prospect of being audited may also originate from increased willingness to avoid errors. Those taxpayers facing high opportunities for evasion might feel less certain about how to pay their taxes correctly (Ahmed & Braithwaite, 2005), and consequently, threats may also elicit partly unintentional over-reporting: just to be on the safe side. Opportunity is a key constituent of small business tax compliance and its role is moderated by its perceptual correlates. Given the opportunity to evade, those unwilling to evade may become involuntarily non-compliant and those willing to evade may fail to perceive the chance to do so. To determine the actual effect of opportunity, it is necessary to control for compliance intention as well as opportunity perception.

2.2.2 Tax Education/Knowledge and Tax Compliance

In order to pay appropriate taxes SMEs must be knowledgeable about the different compliance measures and requirements. Taxation knowledge is a specific part of the general human potential of entrepreneurs, which increases the chances of business success (Haber & Reichel, 2007). The extent of non-compliance arising from knowledge deficits because of the complexity of reporting and returning requirements might be substantial: in the UK, VAT non-compliance mostly results from errors that do not stem from evasion intent with only 3 per cent attributed to tax-evasion (Naibei & Siringi, 2011).

Differential taxation, that is, the need to apply differential taxation rules depending on the amount of income or the characteristics of the taxpayer, is an important explanation for non-compliance among SMEs (Mas'ud et al. 2014): excluding source misreporting (that is, looking at the overall reported income independent of the reported source) decreases non-compliance rates substantially. Although an increase in opportunity will often be accompanied by increased knowledge requirements, this is not necessarily the case. The proportion of differentially taxable incomes changes, evading opportunities may be affected while knowledge requirements remain constant. Thus, knowledge requirements are discussed separately from opportunities.

Navigating through the legal and procedural issues related to taxation is often taxing in itself. In many countries several (sometimes complicated) forms need to be completed, and detailed records need to be kept e.g. reporting requirements in Canada (Maingot & Zeghal, 2006). Substantial knowledge about the procedural aspects of tax laws is required. This is particularly challenging since tax laws tend to be changed frequently (Chittenden et al., 2003) and to be more complex and ambiguous than laws in general (Carnes & Cuccia, 1996). Tax laws are often too complex to be understood by laymen (Sumartaya & Hafidiah, 2014), which many SMEs managers are. They were shown to have less tax knowledge than business students in an Austrian study (Yesegat & Fjeldstad 2016) and felt less competent in making their tax filings than employed persons with even less tax knowledge in an Australian study (Ahmed & Braithwaite, 2005).

Though SMEs often deal with (perceived) knowledge deficiencies by seeking the help of tax practitioners, they tend to handle part of the taxpaying process themselves (Coolidge et al., 2009) and will, at least, have to keep the necessary records. Acquiring taxation

knowledge is costly in terms of time (to become informed, to keep the records, to fill out the forms) and money (tax literature, tax practitioners). Across economies, compliance costs have been consistently shown to be highest for small businesses (Chittenden et al., 2005; European Commission, 2004; Joumard, 2002; Pope & Abdul-Jabbar, 2008) in particular if incomes are (still) low (Slemrod & Weber, 2012). In a mail survey, holding all else equal, self-employed business people spent an extra 35 hours and 69 dollars on tax handling compared with employees (Slemrod & Weber, 2012). Although there has been a trend towards simplification of tax laws and, more importantly, tax administration procedures (Kenya Revenue Office and County tax collectors; Braithwaite, 2009), compliance costs tend to remain high (Chittenden et al., 2003) and a sufficient level of knowledge necessary to ensure procedural compliance is more difficult to reach for small than for large businesses (Gaetan, 2008).

Tax practitioners acknowledge that the complexity of taxation is making compliance especially difficult to achieve for many small businesses (Torgler, 2016). It can be assumed that, sometimes, small business taxpayers are not even sure about whether they are fully compliant or not. In several countries the distinction between the earnings/income from labour and capital is particularly hard to draw in the case of small businesses (Slemrod, Collins, Hoopes, Reck & Sebastiani, 2015) and self-reported evasion within small businesses did not match actually documented non-compliance (Naibei & Siringi, 2011). This is interpreted as resulting from a lack of taxation knowledge. The relation between knowledge and tax compliance are however mixed.

Highly educated groups were shown to agree more with existing fiscal policies than less educated groups (Slemrod et al. 2015). Indeed, a low perceived complexity of tax laws (Sumartaya & Hafidiah, 2014); education concerning taxation (Kasipillai et al., 2003) as well as subjective (Yesegat & Fjeldstad 2016) and actual tax knowledge (Sumartaya & Hafidiah, 2014) were shown to relate positively to (hypothetical or intended) compliance. Some researchers found that education was negatively related to compliance (Kamleitner, Korunka & Kirchler, 2012) SMEs (Kanbur & Keen, 2014), whereas again others found no clear pattern of non-compliance across levels of education among the self-employed (Schuetze, 2002).

Chan et al. (2000) found a small positive effect (via tax attitudes) of education on tax compliance in a US sample, whereas in a Hong Kong sample, education and compliance

were unrelated. Although these cumulative findings are contradictory at first sight, a closer inspection indicates that the type of knowledge matters; both in general knowledge in terms of education as well as tax-specific knowledge influences the ability and willingness to comply or evade. General knowledge seems to be used to evade as often as it is used to comply. Tax-specific knowledge tends to lead to an increase in compliance; presumably because to learn about taxes also means to learn about their necessity in society or because this specific knowledge is a greater deterrent. The pre and posttests of two groups of Norwegian students, who took part in either a tax law course or a marketing course, suggest that specific tax knowledge renders tax attitudes more favourable; increases fairness perceptions of the tax system; and leads people to perceive (their own) tax evasion as more serious (Kanbur & Keen, 2014). Knowledge requirements for SMEs' tax compliance are relevant.

Tax-specific knowledge is necessary in order to enable SMEs to comply, as well as to increase their willingness to do so. Most taxes paid by employed people are withheld from the outset or included in gross prices. In contrast, SMEs typically pay their taxes "out of their pocket." In other words, while employed are passive recipients of information about the amount of taxes they pay, SMEs dispose of their gross income, which is mentally perceived as their own money, and actively determine taxes as representing a loss. Paying the tax share out of one's own pocket represents a loss frame. While paying taxes typically constitutes a loss for SMEs, it constitutes a non-gain for taxpayers whose taxes are withheld at the source. Research based on "prospect theory" (Kahneman & Tversky, 1979) has demonstrated that the perceived pain of a loss is greater than the perceived pain caused by an equally sized non-gain (Idson et al., 2000).

2.2.3 Fines/Penalties and Tax Compliance

Fines and penalty rates may substitute each other due to their multiplicative linkages as long as neither of them is set to zero (Sumartaya & Hafidiah, 2014). Higher fines simply make evading taxes more hazardous for taxpayers and should deter them from evasion. Empirically, the deterrent effect of fines could not always be supported. The observed effects were weaker than expected and some studies even suggest that an increase of penalties can have undesirable effect and result in more tax avoidance (Yesegat & Fjeldstad 2016). (Blackwell & McKee 2012) supports the evidence that fines do affect

tax compliance though the impact was virtually zero. Friedland*et al*,.(1978) compliance was strongly affected by the amount of fines than by audit probabilities.

Several studies however found no support for the deterring effects of fines since it was weak (Andreoni, 1998). Some of the findings suggest that a policy based on deterrence is effective only in combination with frequent Audits (Sumartaya & Hafidiah, 2014). From the tax administration viewpoint, researchers have concluded that compliance could be influenced by educating taxpayers of their social responsibilities to pay and thus their intention would be to comply. As a behavior problem, tax compliance depends on the cooperation of the public. There are greater gains in assisting compliant taxpayers meet their fiscal obligations rather than spending more resources pursuing the minority of no-compliers. Assisting tax payers by improving the flow and quality of information or education them (TV campaigns) in to becoming more responsible citizens has the potential to yield greater revenue than if it were spent on enforcement activities.

A theoretical economic model introduced by Allingham & Sandmo (1972) clearly indicates that penalties as well as audit probability have an impact on tax compliance. The higher the penalty and the potential audit probability the greater discouragement for potential tax evasion. The most extreme penalties will have no effect, if it is common knowledge that audits virtually do not occur. The increasing tax avoidance and tax resistance due to an increase of fines puts into question how fines should be assessed to be effective. On the one hand fines should be high enough to decrease the expected value of tax evasion and to assure its deterrent effect on tax payers. On the other hand, if fines are too high, the tax system would be perceived as unjust and unfair and taxpayers would use any possibility to legally avoid taxes (Sumartaya & Hafidiah, 2014).In Kenya for instance, the maximum penalty for tax evasion is 20% of the evaded amount (Sec 72 D IT Act, Cap 470). In summary evidence suggests fines have mixed impact on tax compliance, this study suggests that fines have no significant positive effect on tax compliance.

2.2.4 Tax Compliance Costs and Tax Compliance

In contrast to the majority of employed people who in many countries are paid net salaries with taxes being deducted at source. Small businesses often need to self-assess and self-report their income and pay taxes "out of their pocket." SMEs not only pay their income taxes but need to take account of various types of business taxes such as

corporate tax, property taxes, and payroll taxes; they need to collect sales taxes such as VAT; and they need to withhold taxes such as personal income taxes in the case of having at least one employee (Kanbur & Keen, 2014) argue that the various types of taxes and taxation requirements may significantly shape the perceived tax situation of SMEs. As tax system implementation is largely concerned with information processing, the bulk of costs of tax compliance are caused by information obligations, for instance, record keeping, filing in tax returns with data etc.

Tax behaviours have three main characteristics of SMEs' tax situation emerge: due to self-reporting and limited control over underlying cash flows, they have the opportunity for non-compliance; due to the need for self-reporting and facing different taxes, they require substantial knowledge in order to understand the rules and comply, due to receiving gross sums that then have to be partly passed on to tax authorities, they face differential possibilities for framing taxes (Weigel et al., 1987). SMEs tax behaviours adopted a psychological perspective and propose that the three identified main characteristics that determine SMEs tax behaviour. The three main factors play a universal role for SMEs.

Specific extent of perceived opportunity is co-determined by inter-individual factors such as risk-seeking, age, and gender (Kastlunger et al., 2010; Kamleitner, Korunka & Kirchler, 2012), and situational factors such as line of industries (Andreoni et al., 1998; Schuetze, 2002), relevant group (social) norms and social networks (Peterson, 2001; Rothengatter, 2005; Smith & Oakley, 1994), business forms (Hite et al., 1992), jurisdictions and cultural differences between Dutch & Albanians (Gerxhani&Schram, 2006) will have a direct and indirect impact on SMEs' tax behaviour and compliance. Different formal administrative requirements come along with different evasion opportunities, knowledge requirements, and framings. Similarly, non-compliance varies substantially across nations and there is a clear case to be made for the importance of cross-cultural and cross-national differences (Tsakumis et al 2007). Most of the existing evidence does, however, not allow disentangling various legislative, administrative, cultural, and political causes for observed cross-national differences. In the interest of focus and brevity, this proposal focuses solely on those factors that tend to be of universal importance in the case of small businesses: (perceived) opportunity, knowledge requirements, and differential framings. The framework acknowledges that the concrete

manifestation of these factors is itself influenced by the wider context which shapes an individual business' specific tax situation.

2.3 Tax Compliance

Tax compliance is a major problem for many tax authorities and it is not easy task to persuade taxpayers to comply with tax requirements even though tax laws are not always precise Braithwaite, 2009; (Sumartaya & Hafidiah, 2014) show that both economic and psychological variables need to be considered to understand compliance (Okoye & Ezejiofor, 2014; Organisation for Economic Co-operation & Development, 2004). (Mason & Calvin, 1984) however failed to find the usually documented link between compliance and fairness), researchers broadly agree that procedural and distributional fairness perceptions (Kim, 2002; Murphy, 2004), knowledge about taxation (Okoye & Ezejiofor, 2014), personal and social norms of tax compliance (Ashby et al., 2009; Rothengatter, 2005; Wenzel, 2005), personal attitudes such as risk attitudes or egoism (Sumartaya & Hafidiah, 2014), tax rates (Blackwell & McKee 2012), and (perceived) audit and detection probabilities (Yesegat & Fjeldstad 2016) combined with deterring fines (Okoye & Ezejiofor, 2014) relate positively to compliance.

Particularities of national tax law and culture relate to tax compliance also play a significant role. The "shadow economy" as a proxy for tax evasion varies dramatically across countries; ranging from around 10 per cent of GNP in Switzerland, Austria, the US and Japan, to slightly below 30 per cent in Italy and Greece, to 46 per cent in the Russian Federation, and to 67 per cent in Bolivia in 2000 (Schneider & Klinglmair, 2004). The political history of a country, acceptance of government, social distance between citizens and political authorities (Bogardus, 1928) as well as religion are just a few of the national cultural characteristics that affect the citizens' willingness to cooperate with authorities in general and tax authorities in particular. Despite non-compliance often being perceived as socially acceptable (Sumartaya & Hafidiah, 2014); Song and Yarbrough, 1978), including small businesses (Muehlbacher et al. 2015) are significantly more compliant than predicted by neoclassical economists who assumes that compliance depends predominantly on audit probability and fines (Andreoni 1998).

2.3.1 Tax Non-Compliance

Tax non-compliance is defined as failure to comply with tax laws and/or report incorrect income, the act of claiming incorrect deductions, relief and rebates and/or paying the incorrect amount of tax beyond the stipulated time frame (Mohd*et al*, .2011).Noncompliance is also perceived as the failure of a taxpayer to report (correctly) the actual income, claim deductions and rebates and remit the actual amount of tax payable to the tax authority on time (Sumartaya & Hafidiah, 2014). Taxpayers vary in terms of the opportunities available to them in overstating expenses and understating incomes (Chau & Leung, 2009).Greater tax noncompliance opportunity generally result from self-employment and income sources not subject to withholding taxes. Taxes can be classified into two main types: direct and indirect taxes. Direct taxes mean the burden (incidence) of tax is borne entirely by the entity that pays it, and cannot be passed on to another entity; for example, corporation tax and individual income tax. Tax non-compliance is the difference between the actual amount of taxes paid and the amount of taxes due. This difference occurs because of overstating expenses and understating income, and deductions (Martin, Wanjohi & Magutu 2010).

Indirect taxes are typically the charges that are levied on goods and services (consumptions) for example VAT (Value Added Tax), sales tax, and excise tax and stamp duties. Indirect taxes are not levied on individuals, but on goods and services. Customers indirectly pay this tax in the form of higher prices. For example, it can be said that while purchasing goods from a retail shop, the retail VAT is actually paid by the customer. The retailer eventually passes this tax to the respective authority. The indirect tax actually raises the price of the goods and the customer's purchase by paying more for that product. Unlike indirect tax, direct taxes are based on 'ability to pay' principle but (by being very obvious to the taxpayer) they sometimes work as a disincentive to work harder and earn more because that would mean paying more tax (Mansor*et al*, 2005). Individuals do not like paying taxes, and they take a variety of actions to reduce their tax liabilities.

These actions can be classified as tax avoidance, which is the legal reduction in tax liabilities by practices that take the full advantage of the tax code, such as income splitting and postponement of taxes for example through contribution to a Home Ownership Savings Plan. The other classification of actions is tax evasion which consists of illegal and intentional actions taken by individuals to reduce their legally due tax

obligations. Individuals and firms can evade taxes by underreporting incomes, sales, or wealth, by overstating deductions or by failing to file appropriate tax returns. In every jurisdiction, tax authorities are empowered to collect revenue from taxpayers. Although there are a number of taxpayers who have reported their income and paid their tax liabilities properly, there are a few taxpayers who have not done so.

For its part the government must take actions to ensure compliance with tax laws. In Kenya self- Assessment System was introduced in 1992 and the tenets of this system is voluntary compliance. Tax compliance can be divided into two categories namely: Administrative Compliance: This refers to compliance with the administrative rules of lodging and paying taxes on time. This includes compliance with the reporting requirements, procedure and regulations. Technical Compliance: This refers to compliance in the computation of taxes payable in accordance with the technical requirements or provisions of the tax laws and paying the right amount of tax. Decades of empirical work on tax compliance has produced awareness of the complexity of tax compliance and non-compliance globally. (Masinde & Makau, 2010) point out that tax compliance itself is now recognized as multifaceted construct. Many scholars such as Jackson et al., (1986) have put forward some explanatory variables in analysis of tax compliance behavior.

In the midst of enormous diversity, a notably consistent theme over the past two decades of tax research has focused on identifying the costs, be they material, social or psychological, which would deter would-be evaders and counter the lure of the benefits of evasion. A preoccupation with identifying costs and benefits with the goal of developing a risk profile for tax collection agencies has meant that less attention has been directed towards managing non-compliance once it has occurred (Masinde & Makau 2010). Based on literature, the dominant environmental factors currently shaping the performance of revenue administrators in developing countries are globalization, large informal sectors and limited administrative capacity. Individuals and firms can evade taxes by underreporting incomes, sales, or wealth, by overstating deductions or by failing to file appropriate tax returns.

Tax policy and administrative reforms generally have one or several of the following objectives: Increasing the equity of the tax system, creating an enabling environment for private sector development, Increasing revenue collection or compliance. On the

implementation side, the challenge to coordinate policy reforms with parallel reforms in tax administration has rarely been fully addressed yet the menu of administrative reform options has been greatly enriched with new approaches to organizational design, taxpayer services, ICT solutions, human resource incentives and formal anti-corruption strategies. Compliance management is no longer based purely on an enforcement – focused approach, but on a combination of enforcement and enhanced taxpayer services.

The issue of tax compliance is extremely important both to those concerned with the key role the increased tax yields can play in restoring macroeconomic balance and those concerned with tax policy and its effects on the economy in general. The level of tax collection though important is an unsophisticated measure of the effectiveness of tax administration .A more accurate measure is the level of compliance. Facilitating compliance involves such elements as improving services to taxpayers by providing clear instructions, easy to fill forms and assisting and educating them on their duties and obligations. Monitoring compliance requires establishing and maintaining current accounts of taxpayers and management information systems covering both ultimate taxpayers and third party agents such as banks involved in the tax system as well as appropriate and prompt procedures to detect and follow up on non-filers, nil filers and delayed payments. Deterring noncompliance requires establishing both a reasonable risk of detection as well as applying penalties effectively. The ideal approach is to combine these measures so as to maximize their effect on compliance as it were, to move a country from a "low compliance to a high compliance environment"(Masinde & Makau 2010).

2.4 Implications of the Study

Paying taxes is presented as a decision that is informed by perceptions. Factors increasing the relevance of the taxpaying business owner relate to the importance that perceptions have in tax decisions. Specifically, all the factors that (psychologically) tie a business owners' fate to the fate of the company will increase the perceived pain of paying taxes. One such factor is the relation between personal and company income. The stronger the link, the more likely paying company taxes will be perceived as painful. Another relevant factor in this context is psychological ownership (e.g. Mayhew et al., 2003; Pierce et al., 2003; Van Dyne & Pierce, 2004). The degree of psychological business ownership experienced by the person(s) involved in making tax decisions predicts the experienced reluctance to give something (in this case: taxes) away from the

company. There are several factors that influence the extent of psychological ownership e.g. the number of co-owners (the less co-owners, the more psychological ownership; Kamleitner & Rabinovich), the asset structure (for the effect in franchise enterprises; Hou et al., 2009), and work environment structures (the less structured, the more psychological ownership; O'Driscoll et al., 2006) are able to influence psychological ownership. In turn, it's expected that all these factors influence tax perceptions and behaviour.

Considering the psychological link between a person and her or his company also highlights an important boundary condition to the framework. If paying taxes is left to the owner-manager then outsourcing this task to tax planners and advisors should moderate the suggested relations. Most databases on tax compliance do not contain detailed information about the extent to which tax planners and advisors have been involved. It is therefore impossible to account for this systematically in a literature review. In future research, it would be interesting to investigate the possibly complex relationships between the use of tax professionals, personal relevancy of taxpaying (including individual-company income links and psychological ownership), and the perception of the tax situation and tax behaviour. Another promising line for future research relates to an investigation of how specifics of the tax situation (e.g. industry and cultural norms) relate to the extent of perceived opportunities, knowledge requirements and decision framings.

Many findings that pointing towards, cultural differences in compliance (Tsakumis et al., 2007) are at least partly mediated by accompanying differences in the three identified key factors. The issue of small businesses' tax compliance has been acknowledged by authorities and researchers on several occasions. The most frequent suggestion in this respect has been simplifying the taxation process (Joumard 2002). Steps such as unifying taxes or simplifying administrative requirements are indeed in line with this framework. Measures are needed on a structural as well as an individual level, that is, where perception takes place. Changing non-compliance opportunities requires structural changes to the tax system. The increasing influence of electronic data storage and transfer has contributed to a reduction in opportunities and is likely to continue to do so in the future.

Taxpayers' opportunity perceptions are what matter most. Actual changes in opportunity are not necessarily perceived as such. One way of reducing the perceived opportunities is to increase the salience of detection likelihood or consequences. Salience of punishment has the potential to create a threatening image of tax authorities, which may reduce voluntary compliance (Murphy, 2004). The reverse side of the coin is to increase the salience of norm-adhering behaviour. Learning that most taxpayers are compliant may not only strengthen tax morale, it may also (indirectly) raise the suspicion that non-compliance is likely to be detected. Future research that identifies new ways of decreasing perceived opportunities in a non-threatening manner, or consequences of different ways of communicating changes in evasion opportunities (being sent information material on the perception of opportunities is a promising research avenue.

Knowledge requirements are difficult to change. Nevertheless, some successful attempts to increase legal and effective simplicity (for a comprehensive review of simplification possibilities (Tran-Nam, 1999) have been made in various jurisdictions across the Organisation for Economic Co-operation and Development (Australia has introduced a pay-as-you-go system to reduce the strains associated with cash flows). Based on previous frameworks and reviews its argued that in addition to simplifying taxation factually, taxpayers have to be in a position to understand and cope with the administrative and legal requirements. One possible route of action is to increase SMEs' level of tax knowledge. There is evidence that even for experienced taxpayers' involuntary non-compliance goes down as taxpayers learn, for example, how to complete forms (Kamleitner, Korunka & Kirchler, 2012).

With increasing tax knowledge taxpayers learn both how to comply and how to evade (taxation knowledge also decreases perceived audit probability (Andreoni et al., 1998) efficiently. Depending on the effect of knowledge on tax morale and compliance intention, increasing knowledge could lead to both a decrease in unintended non-compliance and an increase in intended tax evasion. Ideally taxation knowledge should, hence, be acquired in ways that simultaneously increase the salience of the benefits of a tax system. There are clear benefits to increasing taxation knowledge among SMEs; because of their ambivalent nature actual education programmes require substantial and careful pretesting. The potential for adverse effects on compliance is not the only reason for pretesting needs. Pretests are also essential in ensuring that learning actually takes place.

The availability and accessibility of information may not be sufficient for SMEs to learn and meet the knowledge requirements. The information provided (tax laws) may be difficult to comprehend or be comprehensive to the point of being discouraging, or taxpayers may simply refuse to make use of it. It is crucial to ensure that information transfer takes place and is followed by an increase in (perceived) tax competency and ideally also tax morale. A climate of mutual trust between taxpayers and authorities is a likely prerequisite to enable both outcomes (Sumartaya & Hafidiah, 2014). Decision frames directly relate to the cognitive costs of compliance and hence to the willingness to comply. In contrast to tax knowledge internal framings are hardly recognized as part of the problem. In order to diminish the pain of paying taxes and enhance the willingness to comply, it is recommendable to discourage the application of a "loss" frame. The mental accounting literature (Thaler, 1999) suggests that this may be achieved by encouraging taxpayers to book tax payments on separate mental accounts. Having separate tax accounts might help to avoid feelings of ownership of tax money and hence feelings of loss when taxes are due.

Evidence of this comes from interviews with business owners. Some of those who held separate mental accounts for VAT reported that quite early in their business life it was made clear to them that VAT money is only collected and never possessed. Such an early encounter with this strong message might have contributed to the formation of a separate mental tax account (Muehlbacher et al. 2015). Another way to establish separate mental accounts for tax money is to focus on net prices. If business owners only communicate with their customers in terms of net prices or mainly think of net prices themselves, taxes are more likely to be booked on separate mental accounts (Muehlbacher et al. 2015). An interesting research implication is to establish the degree to which differences in price communication (net vs. gross) relate to differences in tax perception and compliance across countries. Mental accounting also focuses on the costs and benefits of transactions (Prelec & Loewenstein, 1998).

Most SMEs report that when handing over VAT they do not feel the connection between public goods or benefits and tax money strongly (Muehlbacher et al. 2015).As a result, they are often not aware of what they are paying for. In addition, they frequently perceive to benefit less from those public services that are most often in the media, such as pension systems and unemployment insurance. It seems necessary to outline the benefits received from the redistribution of tax money, making this link clear and salient

and maybe even helping SMEs to establish automatic cost-benefit associations has been argued to reduce the perceived tax burden and influence compliance positively (Kamleitner& Ho ̈lzl, 2009). Empirical support for this suggestion comes from research by Schwartz and Orleans (1967), who found that's a salience of moral reasons for compliance (contribute to public welfare by paying your share") and hence of cost benefit associations helps to increase compliance, even more than stressing the severity of sanctions. Fostering cost-benefit associations relates to internal framings, to taxation knowledge, but also to fairness considerations. Although this is no phenomenon specific to small businesses, fairness is an important consideration in tax decision making (e.g. Rawlings, 2003). Lack of trust in the fairness of a tax system and the legitimacy of tax authorities increases the likelihood of tax evasion among SMEs (Naibei & Siringi, 2011).

Trust in and perceived fairness of a tax system and authorities influence several perceptions directly and indirectly. It is a key to taxpayers' acceptance of messages (e.g. the likelihood of evasion detection) and support (e.g. information on taxation, framing) provided by tax authorities. To ensure fairness, several authors suggest a dialogic approach to address non-compliance (e.g. Braithwaite, 1995; Leviner, 2009; Rothengatter, 2005). An argument is made first to educate, inform, advise, and help taxpayers before threatening with the "big stick" and enforcing compliance via severe sanctions (e.g. Ahmed and Braithwaite, 2005; (Sumartaya & Hafidiah, 2014); Shover et al., 2001).

2.5 Comparing Small Businesses to Other Taxpayers
A broadly conceived definition of small businesses has been applied in the literature search. The organization for Economic Co-operation and Development (2004, p. 10), which characterizes small businesses as: for profit commercial entity other than those that exceed a given (high) asset threshold. Small businesses include sole proprietor, partnership and corporate forms of organization. They also include individual return filers who have income from self-employment, even if self-employment income is not their primary source of income.

All these ventures, centered around a single individual (Hankinson et al., 1997) or in the case of team founders around closely related people (for a similar conceptualization of small businesses as individuals (Studdard & Munchus, 2009). These individuals usually make, or are accountable for, all managerial and operative decisions, including revenue

generation and taxation. Their behaviour is crucial to the venture's success, which in turn tends to relate immediately and strongly to their personal incomes hence, one way to view SMEs is to portray them as entities whose behaviour is largely determined by their emotional as well as their rational perception of taxation, which is unlikely to be their core area of expertise. In larger businesses the operative side of taxation is entirely decoupled from such individual considerations. Issues of taxation are dealt with by experts who have limited personal interest in taxation outcomes and do not experience a direct link between company revenues and their own financial situations.

Ahmed and Braithwaite (2005) compared a sample of Australian SMEs with employed taxpayers and found that they did not differ in terms of the following factors: subjectively perceived deterrence from non-compliance; subjective probability of being caught for tax evasion; preference for aggressive tax planning; cooperation with and resistance against tax authorities; attitudes towards equity issues; personal norms of tax honesty; tax morale; and the level of admitted tax evasion. In line with these findings, a scenario study showed no significant differences in terms of hypothetical tax compliance between fiscal officers, business lawyers, and SMEs (Sumartaya & Hafidiah, 2014).

Although there are no notable differences in attitudinal variables, self-employed people perceive a significantly stronger imbalance between their own tax burden and state refunds; they feel a slightly higher subjective tax burden; and they feel they benefit much less from governmental benefits than other groups of taxpayers (Sumartaya & Hafidiah, 2014). Small businesses were also shown to hold less favourable fairness perceptions in terms of distributional (Strumpel, 1966) and procedural (Muehlbacher et al. 2015) fairness. Other studies add to that picture by showing that small businesses hold different mental representations of taxes than employed people. For the self-employed, the stimulus word "tax" tends to elicit thoughts of tax complexity and the limitations that taxes impose on a business. For the employed "taxes" are often associated with a necessary burden and considerations of justice (Sumartaya & Hafidiah, 2014).

Although SMEs were found to be less supportive of spending tax money on education, health, unemployment, and social welfare programmes, their commitment to values associated with security for the community and nation is even higher (Ahmed & Braithwaite, 2005). Importantly, experiences with and competence in tax matters differed significantly between SMEs and all other groups of taxpayers (Ahmed & Braithwaite,

2005): SMEs reported more experiences of contested assessment, audits, and sanctions, signaling that this group is particularly likely to be audited due to its unique exposure to the tax system. As a consequence, SMEs may attest more power to tax authorities and report that they lack competence and autonomy in dealing with tax matters (Ahmed & Braithwaite, 2005).

2.6 Nascent Entrepreneurs

The term "nascent entrepreneurship" is commonly used to describe the process of business development, from business conception to the early phase of business development (Davidson, 2006).During these early phases of a business, tax authorities are argued to be particularly successful in influencing knowledge and internal framings and in establishing a climate of mutual trust. Nascent entrepreneurs face the liability of newness and tax handling is only one of several challenges to master (Torgler, 2016; Malach et al., 2006). Having to adjust to the new role and the accompanying expectations (Vincent & Ortqvist, 2009), not (yet) understanding how to comply, and being incompetent can lead to several errors during tax filing and thus to involuntary non-compliance (Naibei & Siringi, 2011). In the start-up phase experienced threats to freedom are argued to be especially strong. Giving away some of the first money earned is a particularly painful experience that lends itself to being framed as a loss of something owned; in particular since one route into start-ups is via test runs with undeclared and therefore tax-free work (Williams, 2005).

Nascent entrepreneurs have not yet established certain behavioral and perceptional patterns that will become more difficult to change the longer they persist (Guala & Mittone, 2005). Consequently, interventions are likely to be received positively. It is hence in particular in the case of nascent entrepreneurs that a strategy of responsive regulation that involves support and advice before punishment (Braithwaite, 1995) will be effective. First encountering the "big stick" might backfire and turn involuntary non-compliance into aggressive resistance (Murphy, 2004). In contrast, an initial experience of support will build up a climate of trust between taxpayers and tax authorities. In turn this might speed up and/or enhance beneficiary learning processes and increase the willingness and ability to mould perceptions and comply. Empirical evidence suggests that focusing on nascent entrepreneurs and supporting them at an early stage is indeed promising (Waters et al., 2002). Personal age is shown to correlate positively with the degree of compliance. This was also found within self-employed people (Hite et al.,

1992; Schuetze, 2002) and may indicate the importance of focusing on early processes of business development.

Time in business correlated negatively with perceived loss of freedom (Sumartaya & Hafidiah, 2014) indicating that over time entrepreneurs become used to paying taxes and as a consequence less reluctant. Experimental simulations indicate particularly positive effects of audits on compliance if they occur early in the tax life (Kastlunger et al., 2009; Mittone, 2006). Proposed reasons are that they lead taxpayers to overestimate audit frequencies (i.e. decrease perceived opportunity) and disable the experience of early rewarding gains from undetected evasion. Depending on the nature of the audit deterrence is not all that matters. Early audits can equally be used to teach SMEs how to pay their taxes correctly, how to keep psychological and monetary compliance costs low.

Slemrod and Weber (2012) argue that the tax situation of owners and businesses should be looked at simultaneously. These predictions are derived from the usually low detection probabilities and small expected penalties. Ahmed and Braithwaite (2005) found no difference with regard to perceived procedural fairness in Australia, which is at the forefront of jurisdictions applying measures to increase and facilitate voluntary tax compliance. In contrast to low and middle-income groups, high-income groups react by reducing their tax payments. There is experimental evidence that the effect of refunds and extra payments on compliance only arises if the situation is perceived as such (Slemrod & Weber, 2012). This explains why self-reports often do not correspond to actual reports (Kamleitner, Korunka & Kirchler, 2012).Tax non-compliance is often hard to prove. Consequently, measures beyond tax audits are needed to tackle non-compliance (Sumartaya & Hafidiah, 2014).

Such measures ought to be based on knowledge about the factors leading to non-compliance in the first place. In the case of SMEs, tax decisions are often personally relevant, individual decisions. Such decisions are likely to depend on the psychological perception of the situation. SMEs face circumstances that translate into particularly averse decision influence s. Due to their individual nature and their specific tax situation they find it difficult to understand and comply with taxation procedures, they face decision frames that favour non-compliance, and they have and are likely to perceive enhanced opportunities not to comply.

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2.7 Conceptual Framework

This study conceptualizes that tax compliance could be affected by compliance cost, perceived opportunity, fines and penalties, tax knowledge/education in Nakuru Central Business District. This study tests the conceptual framework presented below.

Independent Variables
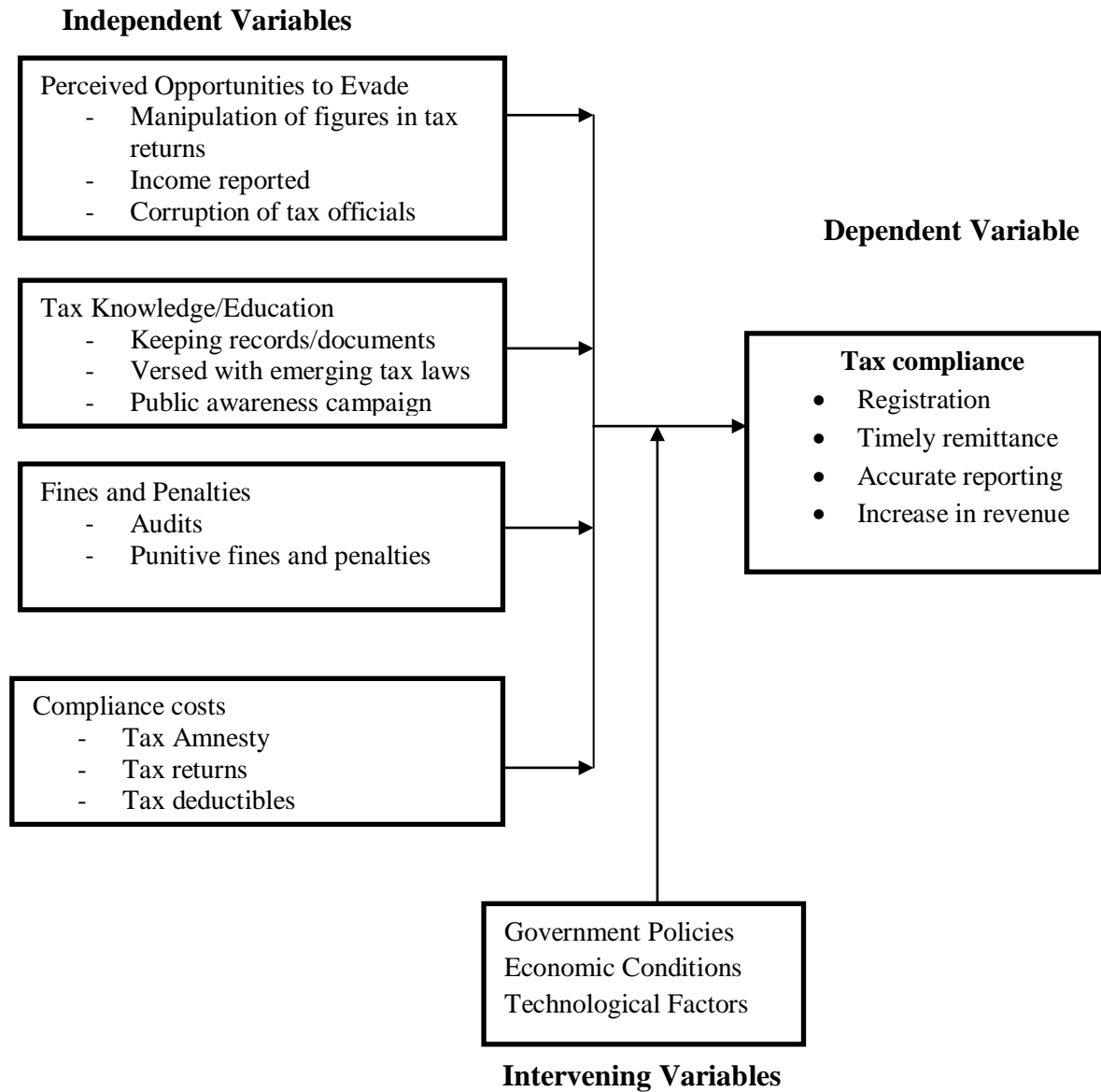
Source: Author 2016

Figure 2.1: Conceptual Framework for Determinants of Tax Compliance among SMEs

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter covered the methodology, procedures that were used, a description of the research area, an outline of the study population, sample size, sampling techniques, data sources, research instruments, data collection procedures, data analysis and presentation.

3.2 Research Design

Descriptive survey design was used in this study to examine factors influencing tax compliance among SMEs in Nakuru CBD. Descriptive research is a study designed to depict the participants in an accurate way. The study concentrated on SMEs within Nakuru town. The data was gathered at a particular point in time with the intention of describing the nature of the existing conditions, identifying the standards against which existing conditions can be compared by determining the relationship between specific events (Orodho, 2009).

3.3 Target Population

Mugenda & Mugenda (2003) describes a population as a complete set of individuals, cases or objects with some common observable characteristics. The total population comprised of 3,506 SMEs in Nakuru CBD (County Government of Nakuru, 2015).

3.4 Sample Size and Sampling Procedures

The study targeted 212 businesses from a population of 3506 licensed SMEs in Nakuru CBD. The study employed stratified proportional sampling techniques to select SMEs where owners/managers were picked from. This was because stratified sampling took into account each identifiable strata of population then divided into sub-groups and the elements were selected randomly ensuring representation of each of this group in the population. The sample of SMEs determined using the Nassiuma (2000) formula which

is as follows: $n = \dfrac{NC^2}{C^2 + (N-1)e^2}$ where c=coefficient of variation, 20≤c≤30%; e=error term, 0.02≤e≤0.05

n = $\dfrac{3506*0.3^2}{0.3^2 + (3506-1)0.02^2}$

n = 212

Where n is the sample size, N is the population size and e is the level of precision. The study allowed an error sampling of 0.02. The sample size was arrived using stratified proportional sampling using method $n_h = \left(\dfrac{n}{N}\right) N_h$

Where: n_h – size of stratum h, N_h – size of stratum h and N – total population

Table 3. 1: SME Sampling Frame

Business Category	Number of Smes (Strata)	Segment Sample (S)
Wholesale and Retail Trade	2070	124
Transport and Communications	131	8
Agriculture and Mining	147	9
Hotels and Restaurants	363	22
Financial Services	426	26
Education and Health	127	8
Manufacturing and Industry	242	15
TOTALS	**3506**	**212**

Source: County Government of Nakuru (2015)

3.5 The Data Collection Instrument

The data collection instruments are tools to collect information from the intended target population/sample (Oppenheim, 2009). The data collection instrument to be used in this study was developed by the researcher. The study used questionnaires for primary data collection. The researcher sought permission from the target SMEs through their managers/owners to collect data. The respondents were assured of their confidentiality and of any information they supplied. This was a data collection tool to which a respondent is expected to react in writing. The designed questions or items in hard copies were distributed to the respondents. This method collected a lot of information over a short period of time. In this study, the respondent was given enough time to complete the questionnaires before they can be used for analysis. The questionnaire included both structured and semi-structured questions. This allowed the respondents to give their own/institutional opinions. The questionnaires were in three parts. The first part highlighted demographic data; the next part obtained specific information in relation to factors influencing tax compliance among SMEs in Nakuru CBD. A Likert scale was incorporated to gauge the attitudes of the respondents.

3.5.1 Validity and Reliability of the Research Instrument

3.5.1.1 Validity of Research Instrument

Validity is the degree to which results obtained from analysis of the data actually represent the phenomenon under study (Best &Khan, 1993). It is the accuracy and meaningfulness of inferences, based on research results; agreement between value of measurements and its true value. Validity is quantified by comparing measurements with values that are as close to the true values as possible. Poor validity also degrades the precision of a single measurement, and it reduces the ability to characterize relationships between variables in descriptive studies. The researcher ensured the content validity of the questionnaire by involving the supervisor whose expertise was put into consideration. The results of the pilot questionnaires enabled the researcher to determine the consistency of responses to be made by respondents and adjust the items accordingly by revising the document.

3.5.1.2 Reliability of the Research Instruments

Reliability is the measure of the degree to which a research yields consistent results or data after repeated trials, degree of consistency that the research instruments or procedures demonstrate. It is qualified by taking several measurements on the same subjects. Poor reliability degrades the precision of a single measurement and reduces the ability to track changes in measurement in a study (Mislevy, 2004). Pilot testing was carried on 10% of the respondents to test reliability of data collection instruments.The results of the pre-test survey helped in restructuring of the questionnaire by incorporating the missing information, omitting irrelevant questions and paraphrasing questions that appeared ambiguous to the respondents

3.6 Data Analysis and presentation

The data was analyzed using, descriptive statistics and inferential statistics, Correlation and Chi-Square-test for goodness of fit and agreement.The analysis was done using SPSS and the results presented in frequency tables and graphs and percentages. Spearman Correlation was used to test the nature of relationship between study variables.

3.7 Ethical Considerations

Respondents' confidentiality was ensured through the study (Trochim 2006) as well as through literature review for authors' acknowledgement. The researcher also explained the purpose of the study and how the information obtained were used.

CHAPTER FOUR
RESEARCH FINDINGS AND DISCUSSIONS

4.1 Introduction

The chapter focuses on data analysis, presentation of research findings as well as findings discussions

4.2 Response Rate

The study's response rate was as presented in Table 4.1

Table 4.1: Response Rate

Business Category	Sample Size	Successful	Percent
Wholesale and Retail	124	99	79.8
Transport	8	5	62.5
Agriculture and Mining	9	4	44.4
Hotels and Restaurants	22	17	77.2
Financial Services	26	18	69.2
Education and Health	8	3	37.5
Manufacturing	15	9	56.25
Total	**212**	**155**	**73.1**

Source: County Government of Nauru (2015)

Out of two hundred and twelve questionnaires that were administered to the respondents, one hundred and fifty five were properly returned back and this was 73.1% response. 50% and above respondents' response rate is appropriate in conclusion of research findings (Mugenda & Mugenda, 2003). Response rate obtained was appropriate in answering study's research questions.

4.3 Demographic Information

Demographic information of the respondents discussed entailed; number of years that one has been in business, education level, average annual income, attendance of taxation training, operators' enterprises audit and penalization by KRA and respondents engagement in under reporting incomes or over claiming of deductions.

4.3.1 Education level

The study sought to establish the education level of the respondents.

Table 4.2: Education level

	Frequency	Percent	Valid Percent	Cumulative Percent
high school certificate	25	16.1	16.1	16.1
certificate/diploma	59	38.1	38.1	54.2
under graduate degree	23	14.8	14.8	69.0
Professional	37	23.9	23.9	92.9
post graduate	11	7.1	7.1	100.0
Total	**155**	**100.0**	**100.0**	

Table 4.2 shows that majority of the respondents 59 (38.1%) had certificate/Diploma education while 37(23.9%) had taken professional qualifications. 23 (14.8%) of the respondent had a bachelor degree, while 25(16.1%) have only a basic level of education. Only a small percentage of respondents 11(7.1%) had post graduate education. Thus majority of the respondents had a tertiary education.

4.3.2 Number of years that respondents have been in Business

The study sought to establish how long respondents have been in business.

Table 4.3: Number of years that respondents have been in Business

	Frequency	Percent	Valid Percent	Cumulative Percent
1-5 year	26	16.8	16.8	16.8
6-11 years	72	46.5	46.5	63.2
above 12 years	57	36.8	36.8	100
Total	**155**	**100.0**	**100.0**	

Number of years in business were categorized into three groups; 1-5 years, 6- 11 years, 12 years and above. Table 4.3 shows that majority 72 (46.5%) of the respondent have been in business between 6-11 years. A large number 57 (36.8%) of respondents have been in business for twelve years and above while 26 (16.8%) of the respondents have operated their business for less than 5 years. Thus it can be concluded that most of the respondents have been in business long enough and thus possess enough experience on topic under study.

4.3.3 Respondents formal taxation training attendance

The study sought to establish whether respondents have ever attended formal taxation training.

Table 4.4: Respondents formal taxation training attendance

	Frequency	Percent	Valid Percent	Cumulative Percent
Yes	39	25.2	25.2	25.2
No	116	74.8	74.8	100.0
Total	**155**	**100.0**	**100.0**	

From the results on Table 4.4, majority 116 (74.8%) of respondents had not attended a formal taxation training while 39 (25.2 %) of the respondents had attended taxation trainings. Thus from the results, majority of respondents had no formal training on how tax related matters.

4.3.4 Respondents average annual turnover

The study sought to establish the average annual turnover of the respondents.

Table 4.5: Respondents average annual turnover

	Frequency	Percent	Valid Percent	Cumulative Percent
<50,000	22	14.2	14.2	14.2
50,000-200,000	46	29.7	29.7	43.9
200,000-350,000	49	31.6	31.6	75.5
>350,000	38	24.5	24.5	100.0
Total	**155**	**100.0**	**100.0**	

Table 4.5 shows that majority 48 (31.6%) of the respondent have an average annual turnover of ksh 200,000-350,000 while 46 (29.7%) of respondents have an average annual turnover of ksh 50,000-200,000. 38 (24.5%) of the respondents operated business with annual turnover of above ksh 350,000 while 22 (14.2%) of respondents' business had annual turnover of less that ksh 50,000. Thus it can be concluded that most respondents' businesses based on reported turnovers qualified for turnover tax returns filing.

4.3.5 Respondents KRA audit

The study sought to establish whether respondents' businesses had audited by revenue authority.

Table 4.6: Respondents KRA audit

	Frequency	Percent	Valid Percent	Cumulative Percent
Yes	51	32.9	32.9	32.9
Valid No	104	67.1	67.1	100.0
Total	**155**	**100.0**	**100.0**	

From the results on Table 4.6, majority 104 (67.1%) of respondents had not been audited by KRA at any one time while 51 (32.9 %) of the respondents had at any one time been audited by KRA. Thus from the results, majority of respondents' businesses have never been audited by KRA to ascertain whether they are tax compliant or not.

4.3.6 Respondents under reporting income / over claiming deductions

The study sought to establish whether respondents under report business incomes or over claim deductions.

Table 4.7: Respondents underreporting income / over claiming deductions

	Frequency	Percent	Valid Percent	Cumulative Percent
Under Reporting Income	26	16.8	16.8	16.8
Over Claiming Deductions	23	14.8	14.8	31.6
None	106	68.4	68.4	100.0
Total	**155**	**100.0**	**100.0**	

From the results on Table 4.7, majority 106 (68.4%) of respondents had not engaged in any of the above activities while 26 (16.8 %) of the respondents reported to have under reported business income with another 23(14.8%) of the respondents over claiming deductions. Thus it can be concluded that a majority of respondents don't engage in tax related malpractices.

4.4 Descriptive statistics analysis and discussions

Descriptive statistics analysis for study research variables and discussions are presented. The study's independent variables were; perceived opportunity for evasion, tax knowledge and education, fines and penalties and compliance cost while tax compliance was the dependent variable.

4.4.1 Descriptive Analysis for perceived opportunity for tax evasion

The study sought to find out whether measured indicators of perceived opportunity for tax evasion influences tax compliance among SMEs. These indicators were a ranked on a 5 point likert ranging from "5 strongly agree" to "1 –strongly disagree".

Table 4.8: Descriptive Analysis for perceived opportunity for tax evasion

	1	2	3	4	5	X^2	P
I can manipulate figures in tax return since no need to send supporting documents to KRA	21(13.5%)	35(22.6%)	55(35.5%)	35(22.6%)	9(5.8%)	65.812	0.174
Tax authority is tolerant with me for not filling exact tax returns as per my income	73(47.1%)	57(36.8%)	19(12.3%)	5(3.2%)	1(0.6%)	86.273	0.006
There exists opportunity windows to evade tax until amnesties are granted	53(34.2%)	64(41.3%)	31(20.0%)	6(3.9%)	1(0.6%)	49.785	0.708
I believe the tax authority has limited capability to investigate all income reported to them so I have an opportunity to under report	24(15.5%)	39(25.2%)	21(13.5%)	59(38.1%)	12(7.7%)	78.148	0.027

Statement	SA	A	N	D	SD	x^2	p
Tax officers are corrupt therefore I believe that opportunities to evade taxes and get away with it are plenty	34(21.9%)	60(38.7%)	36(23.2%)	15(9.7%)	10(6.5%)	73.057	0.063
Tax authorities do not focus much energies/resources on SMEs	30(19.4%)	39(25.2%)	19(12.3%)	44(28.4%)	23(14.8%)	99.790	0.000
I believe that the probabilities of being detected by the tax authority for not declaring the exact income that I receive are low	49(31.6%)	53(34.2%)	25(16.1%)	24(15.5%)	4(2.6%)	79.646	0.021
I run other businesses elsewhere in remote areas where tax authorities never visit	24(15.5%)	42(27.1%)	40(25.8%)	42(27.1%)	7(4.5%)	57.212	0.430

The findings on table 4.8 indicates that 28.4% of respondents agreed to have manipulated figures in tax return since there was no need to send supporting documents to KRA (x^2=65.812, p>0.05). These findings are consistent with those of (Hanlon *et al.,* 2007; Rice, 1992) who suggested that SMEs are more likely to cheat than other groups of taxpayers. Majority of respondents (83.9%) disagreed that tax authority was tolerant with them for not filling exact tax returns as per their income (x^2=86.273, p<0.05). 75.5% of respondents disagreed that there exist opportunity windows to evade tax up until amnesties are granted with only a 4.5% of the respondents agreeing (x^2=49.785, p>0.05). The respondents were indifferent with a small margin with 40.7% disagreeing and 45.8% agreeing that the tax authority had limited capability to investigate all income reported to it thus giving room for under reporting (x^2=78.148 , p<0.05). A large number of respondents (60.6%) agreed that tax officers were not corrupt thus opportunities to evade taxes were minimal, with only 16.2% of the respondents holding a contrary opinion (x^2=73.057, p>0.05). 43.2% of the respondents agreed that tax authorities do not focus much on SMEs with 44.6% of respondents disagreeing (x^2=79.646, p>0.05). Majority of the respondents (65.8%) agreed that the probability of

being detected by the tax authority for not declaring the exact income was high with only 18.6% of respondents disagreeing (x^2=79.646, p<0.05). According to Okello (2014), Kenya Revenue Authority estimates that only half of SMEs tax non-compliance is detected. A fairy large number of respondents (31.6%) admitted to have run other businesses in remote areas where tax authorities never visit (x^2=57.212, p>0.05).

4.4.2 Descriptive Analysis for tax knowledge and education

The study sought to establish whether measured indicators of tax knowledge and education determined tax compliance among SMEs. These indicators were a ranked on a 5 point likert ranging from "5 strongly agree" to "1 –strongly disagree".

Table 4.9: Descriptive Analysis for tax knowledge and education

	1	2	3	4	5	X^2	P
I know which income should be included or excluded in determining the taxable income	38(24.5%)	59(38.%)	37(23.9%)	21(13.%)	-	77.872	0.002
I know how to declare actual income received from all sources to the tax authority	61(39.4%)	54(34.8%)	15(9.7%)	21(13.5%)	4(2.6%)	75.978	0.080
I understand that I should pay taxes due within the prescribed period from the date of issue of the Notice of Assessment or within the stipulated period	15(9.7%)	26(16.8%)	29(18.7%)	56(36.1%)	29(18.7%)	83.078	0.026

I know how to keep records/documents	25(16.1%)	41(26.5%)	36(23.2%)	42(27.1%)	11(7.1%)	80.095	0.043
I am well versed/keep up with the existing/ developing/ emerging tax laws/developments	97(62.6%)	56(36.1%)	2(1.3%)	-	-	48.384	0.018
I believe tax authorities need to train and make public awareness campaigns targeted at the SME sector	5(3.2%)	12(7.7%)	24(15.5%)	67(43.2%)	47(30.3%)	86.041	0.015
I know I should obtain a tax payer identification pin number as well as register my business as a tax agent	4(2.6%)	30(19.4%)	53(34.2%)	57(36.8%)	11(7.1%)	69.256	0.193

Key: 1=strongly agree, 2=Agree, 3=Not certain, 4-Disagree, 5=Strongly Disagree

The findings on table 4.9 indicates that 62.6% of respondents disagreed to have knowledge on which income should be included or excluded in determining the taxable income (x^2=77.872, p<0.05), while majority of respondents (74.2%) disagreed that they knew how to declare actual income received from all sources to the tax authority(x^2=75.978, p>0.05). 54.8% of respondents agreed that they understood that they should pay taxes due within the prescribed period from the date of issue of the Notice of Assessment or within the stipulated period (x^2=83.078, p<0.05). Only 34.2% of respondents agreed that they knew how to keep business records (x^2=80.095, p<0.05), while a larger majority of respondents (98.7%) of respondents disagreed that they were well versed with the existing tax laws (x^2=43.384, p<0.05). Taxpayers must have sufficient tax knowledge in order to assess their tax liability correctly and to file

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tax return forms on time (Fatt & Khin, 2011). 73.5% of the respondents held the opinion that tax authorities need to train and carry out public awareness campaigns targeted at the SME sector on matters relating to taxation (x^2=86.041, p<0.05), with a 43.9% of respondents agreeing that they were aware that they should obtain a tax payer identification pin number as well as register their business as a tax agent with the tax authority (x^2=69.256, p>0.05).

Table 4.10: Descriptive Analysis for fines and penalties

The study sought to determine whether measured indicators of fines and penalties influences tax compliance among SMEs. These indicators were a ranked on a 5 point likert ranging from "5 strongly agree" to "1 –strongly disagree".

Key: 1=strongly agree, 2=Agree, 3=Not certain, 4-Disagree, 5=Strongly Disagree

Table 4.10: Descriptive Analysis for fines and penalties

	1	2	3	4	5	X^2	P
The penalty rates are very low and I can afford to pay the penalty or raise from family and friends	27(17.4%)	45(29.0%)	31(20.0%	46(29.7%	6(3.9%)	18.896	0.000
I am legally not obligated to audit my books therefore successful prosecution is not possible	23(14.8%)	41(26.5%)	36(23.2%)	47(30.3%)	8(5.2%)	92.561	0.004
There exists punitive fines and penalties imposed on SMEs	26(16.8%)	45(29.0%)	69(44.5%)	14(9.0%)	1(0.6%)	70.685	0.163
The tax enforcement is very weak	11(7.1%)	22(14.2%)	44(28.4%)	60(38.7%)	18(11.6%)	83.386	0.025
I believe that the penalty is lower than my tax saving due to not complying with tax laws	12(7.7%)	35(22.6%)	71(45.8%)	35(22.6%)	2(1.3%)	51.234	0.783
Serious enforcement and penalty by the KRA may result if I do not comply	1(0.6%)	11(7.1%)	22(14.2%)	86(55.5%)	35(22.6%)	89.894	0.007

Tax authority audits and investigations are few among SME	11(7.1%)	14(9.0%)	21(13.5%)	66(42.6%)	43(27.7%)	95.958	0.002
Tax savings on non-compliance are higher than the fines and penalties levied	48(31.0%)	61(39.4%)	27(17.4%)	15(9.7%)	4(2.6%	94.386	0.003

Key: 1=strongly agree, 2=Agree, 3=Not certain, 4-Disagree, 5=Strongly Disagree

The findings on table 4.10 indicates that 46.4% of respondents disagreed that the penalty rates were very low and thus respondents could afford to pay the penalty or raise from family and friends (x^2=18.896, p<0.05), while 35.5% of respondents agreed that since they were not legally obligated to audit their books of accounts prosecution by tax authorities was not possible (x^2=92.561, p<0.05).A larger majority of respondents (44.5%) were not sure whether there exist punitive fines and penalties imposed on SMEs for tax filing non compliance with only a minority of respondents 9.6% agreeing that punitive fines and penalties exist for tax filing non compliance (x^2=70.685, p>0.05). Tax compliance enforcement among SME operators was found to be very weak as agreed by 50.3% of the respondents (x^2=83.386, p<0.05), while a majority (45.8%) of respondents were uncertain on whether penalties for non compliance were lower than their tax savings (x^2=51.234, p>0.05). 78.1% of respondents agreed that serious enforcement and penalty by the KRA may result for tax filing non compliance (x^2=89.894, p<0.05). Tax authority audits and investigations were few among SME according to a majority 70.3% of respondents (x^2=95.958, p<0.05). Okello (2014) asserts that tax audits are generally a costly matter thus explaining why tax authority infrequently carries them out. A majority of respondents (70.4%) disagreed that ax savings on non-compliance were higher than the fines and penalties levied (x^2=94.386, p<0.05).

4.4.4 Descriptive Analysis for tax compliance cost.

The study sought to evaluate whether measured indicators of tax compliance cost affects tax compliance among SMEs. These indicators were a ranked on a 5 point likert ranging from "5 strongly agree" to "1 –strongly disagree".

Table 4.11: Descriptive Analysis for tax compliance cost

Statement	1	2	3	4	5	x^2	p
Having been none compliant in the past I usually wait to tax amnesty windows to come clean	5(3.2%)	22(14.2%)	63(34.2%	53(34.2%	12(7.7%)	111.830	0.000
The cost of filing tax returns is reasonable	12(7.7%)	14(9.0%)	47(30.3%)	52(33.5%)	30(19.4%)	128.373	0.006
costs incurred in efforts to be compliant should be tax deductible	37(23.9%)	51(32.9%)	42(27.1%)	21(13.5%)	4(2.6%)	44.941	0.000
i-tax has helped in reducing compliance cost	37(23.9)	69(44.5%)	38(24.5%)	11(7.1%)	-	86.542	0.350
I have to wait for tax refunds for a longer period	37(23.9%)	51(32.9%)	49(31.6%)	13(8.4%)	5(3.2%)	118.341	0.005
The cost of hiring a tax agent is reasonable	13(8.4%)	29(18.7%)	53(34.2%)	45(29.0%)	15(9.7%)	102.759	0.000
The cost of travelling in order to follow up on refunds is reasonable	10(6.5%)	26(16.8%)	46(29.7%)	57(36.8%)	16(10.3%)	46.977	0.000
The costs of full compliance as compared to the costs of non compliance high	3(1.9%)	10(6.5%)	32(20.6%)	69(44.5%)	41(26.5%)		0.799

Key: 1=strongly agree, 2=Agree, 3=Not certain, 4-Disagree, 5=Strongly Disagree

The findings on table 4.11 indicates that 41.9% of respondents agreed that having been tax none compliant in the past they usually wait on tax amnesty windows to come clean (x^2=111.830, p<0.05), while 52.9% of respondents agreeing that the cost of filing tax returns was reasonable (x^2=86.423, p<0.006). A few respondents (16.1%) believed that costs incurred in efforts to be compliant should be tax deductible (x^2=128.373, p<0.05), with a 7.1% of respondents agreeing that i-tax has reduced compliance cost (x^2=44.941

p>0.05). On tax refunds waiting period, 11.6% of respondents said that the waiting period was long (x^2=86.542, p<0.05) and the cost of hiring a tax agent was termed as reasonable by 38.7% of respondents (x^2=118.341, p<0.05). 47.1% of the respondents agreed that the cost of travelling in order to follow up on refunds was reasonable (x^2=102.759, p<0.05), while cost of full compliance as compared to the costs of non compliance was found to be high by 71% of the respondents (x^2=46.977, p>0.05).

4.4.5 Descriptive Analysis for tax compliance level

The study sought to find out tax compliance level among SMEs.

Table 4.12: Descriptive Analysis for tax compliance level

	1	2	3	4	5	X^2	P
The business files taxes accurately	30(19.4%)	46(29.7%)	29(18.7%	38(24.5%	12(7.7%)	130.266	0.000
The business pays all taxes on time	29(18.7%)	56(36.1%)	34(21.9%)	27(17.4%)	9(5.8%)	108.019	0.000

Key: 1=strongly agree, 2=Agree, 3=Not certain, 4-Disagree, 5=Strongly Disagree

The findings on table 4.12 indicates that majority of respondents (49.1%) admitted that their businesses don't file taxes accurately (x^2=130.266, p<0.05), while only 23.2% of respondents agreed that their business pays all taxes on time (x^2=108.019, p<0.05).

4.5 Chi-square test for goodness of fit analysis

This section presents the findings of the chi-square test for goodness of fit for study's variables.

Table 4.13: chi-square test for goodness of fit

	perceived opportunity for tax evasion	Tax edu	Fines	Tax cost	Tax compl
Chi-Square	74.645[a]	100.484[a]	63.323[b]	63.226[a]	59.761[c]
Df	3	3	2	2	5
Asymp. Sig.	.000	.000	.000	.000	.000

a. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 10.3.

b. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 9.7.

c. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 19.4.

Table 4.13 presents these findings. The Chi-squared test for equal proportions is a statistical test used to investigate whether the proportions of responses in each category are equal or whether there are statistically significant differences in the proportions of responses in each category. The null hypothesis of the Chi-square test is that the proportion of responses that fall into each of these categories is equal and any differences observed are due to chance or random variation. If the null hypothesis is true, then we cannot conclude anything based on the responses we observe, as these are essentially due to chance. We reject this null hypothesis of equal proportions at the 5% significance level (95% confidence) if the p-value of the test for that question is less than or equal to 0.05. The p-values shown are less than 0.05 (x^2=74.645, p<0.05), (x^2=100.484, p<0.05), (x^2=63.323, p<0.05), (x^2=63.226, p<0.05 and (x^2=59.761, p<0.05) respectively, indicating that the results obtained are statistically significant, showing dominant and equal perception of respondents regarding the said questions.

4.6 Correlation analysis

This section presents the findings of the correlation analysis between the independent variables and the dependent variable to test the nature of relationship and answer research questions of the study. Devore and Peck (2006) recommends a guideline for assessing resultant correlation coefficients as; correlation coefficients less than 0.5 represent a weak relationship, correlation coefficients greater than 0.5, but less than 0.8,

represent a moderate relationship whereas correlation coefficients greater than 0.8 represent a strong relationship.

4.6.1 Relationship between perceived opportunity for tax evasion and tax compliance

The study examined the relationship between perceived opportunity for tax evasion and tax compliance as presented in Table 4.14.

Table 4.14: Relationship between perceived opportunity for tax evasion and tax compliance

		perceived opportunity for tax evasion	Tax compliance
perceived opportunity for tax evasion	Spearman Correlation	1	-.026
	Sig. (2-tailed)		.748
	N	155	155
Tax compliance	Spearman Correlation	-.026	1
	Sig. (2-tailed)	.748	
	N	155	155

It was established that there exist statistically insignificant, negative relationship between perceived opportunity for tax evasion and tax compliance (rho= -0.026; p>0.05). This means that as perceived opportunity for tax evasion increases, tax compliance reduces among SMEs. These findings are consistent with those of Kamleitner et al., (2012) who found that opportunities for tax evasion may lead to an increase in intended as well as unintended non-compliance.

4.6.2 Relationship between Tax knowledge/education and tax compliance

The study examined the relationship between tax knowledge/education and tax compliance as presented in Table 4.15.

Table 4.15 Relationship between tax knowledge/education and tax compliance

		Tax education	Tax compliance
Tax education	Spearman Correlation	1	-.031
	Sig. (2-tailed)		.706
	N	155	155
Tax compliance	Spearman Correlation	-.031	1
	Sig. (2-tailed)	.706	
	N	155	155

It was established that there exist statistically insignificant, negative relationship between tax knowledge/education and tax compliance (rho= -0.031; p>0.05). This means that tax knowledge/education among SMEs operators decreases, tax compliance also decreases among SMEs. Some researchers found that education was negatively related to compliance (Kamleitner, Korunka & Kirchler, 2012).

4.6.3 Relationship between fines/penalties and tax compliance

The study examined the relationship between fines/penalties and tax compliance as presented in Table 4.16.

Table 4.16: Relationship between fines/penalties and tax compliance

		Fines	Tax compliance
Fines	Spearman Correlation	1	-.038
	Sig. (2-tailed)		.639
	N	155	155
Tax compliance	Spearman Correlation	-.038	1
	Sig. (2-tailed)	.639	
	N	155	155

It was established that there exist statistically insignificant, negative relationship between fines/penalties and tax compliance (rho= -0.038, p>0.05). This means that as tax fines/penalties increase, tax compliance decrease among SMEs. if fines are too high, the tax system would be perceived as unjust and unfair and taxpayers would use any possibility to legally avoid taxes (Sumartaya & Hafidiah, 2014).

4.6.4 Relationship between tax compliance cost and tax compliance

The study examined the relationship between tax compliance and tax compliance level as presented in Table 4.17.

Table 4.17 Relationship between tax compliance costs and tax compliance level

		Tax cost	Tax compliance
Tax cost	Spearman Correlation	1	.024
	Sig. (2-tailed)		.768
	N	155	155
Tax compliance	Spearman Correlation	.024	1
	Sig. (2-tailed)	.768	
	N	155	155

It was established that there exist statistically insignificant positive relationship between tax compliance costs and tax compliance level (rho= 0.024; p>0.05). This means that tax compliance cost decrease, tax compliance among SMEs increase. Kanbur and Keen, (2014) argue that the various types of taxes and taxation requirements may significantly shape the perceived tax situation of SMEs.

4.7 Hypotheses Testing

Test of the research hypotheses were made based on the relationship chi-square analyses.

4.7.1 Perceived Opportunity for Tax Evasion with Tax Compliance

To test the effect of perceived opportunity for tax evasion on tax compliance among SMEs, the chi-square results showed that perceived opportunity for tax evasion had no significant effect on tax compliance among SMEs (p=0.254) which is greater than (alpha 0.05). Therefore the first null hypothesis "perceived opportunity for tax evasion has no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District" was accepted. As shown in the table 4.18 below:

Table 4.18: Chi-square test for perceived opportunity for tax evasion on tax compliance

	Value	Df	Asymp. Sig. (2-sided)
Chi-Square Tests			
Pearson Chi-Square	106.873[a]	98	.254
Likelihood Ratio	108.968	98	.211
Linear-by-Linear Association	.010	1	.919
N of Valid Cases	155		

4.7.2 Tax Knowledge and Education Tax Compliance

To test the effect of tax knowledge and education on tax compliance among SMEs, the Chi-squire analysis showed that tax knowledge and education had no significant effect on tax compliance among SMEs (p=0.838) which is greater than (alpha 0.05). Therefore the second null hypothesis "Tax knowledge and education has no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District" was accepted. As shown in the table 4.19 below:

Table 4.19: Chi-square test for tax knowledge and education on tax compliance

	Chi-Square Tests		
	Value	Df	Asymp. Sig. (2-sided)
Pearson Chi-Square	90.735[a]	105	.838
Likelihood Ratio	92.851	105	.796
Linear-by-Linear Association	.275	1	.600
N of Valid Cases	155		

4.7.3 Fines and Penalties with Tax Compliance

To test the effect of fines and penalties on tax compliance among SMEs, the Chi-squire results showed that fines and penalties had statistically significant effect on tax compliance among SMEs (p=0.043) which is smaller than (alpha 0.05). Therefore the third null hypothesis "Fines and penalties have no statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District" was rejected. The alternate hypothesis, "Fines and penalties have statistically significant effect on tax compliance among Small and Medium Enterprises in Nakuru Central Business District" was hence accepted. As shown in the table 4.20 below:

Table 4.20: Chi-square test for fines and penalties on tax compliance

	Chi-Square Tests		
	Value	Df	Asymp. Sig. (2-sided)
Pearson Chi-Square	131.098[a]	105	.043
Likelihood Ratio	113.047	105	.278
Linear-by-Linear Association	.026	1	.872
N of Valid Cases	155		

4.7.4 Tax Compliance Cost on Tax Compliance

To test the effect of Tax compliance cost on tax compliance among SMEs, the Chi-squire results showed that Tax compliance cost had no significant effect on tax compliance among SMEs (p=0.183) which is greater than (alpha 0.05). Therefore the fourth null hypothesis "Tax compliance cost has no statistically significant effect on tax compliance

among Small and Medium Enterprises in Nakuru Central Business District" was accepted. As shown in the table 4.21 below:

Table 4.21: Chi-square test for Tax compliance cost on tax compliance

Chi-Square Tests			
	Value	Df	Asymp. Sig. (2-sided)
Pearson Chi-Square	110.474[a]	98	.183
Likelihood Ratio	105.810	98	.277
Linear-by-Linear Association	.092	1	.761
N of Valid Cases	155		

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter discusses the summary of research findings and gives conclusions of the findings, recommendations of the study and suggestions for further research.

5.2 Summary

The main objective of the study is to assess the influence of tax payers' attitudes on tax compliance among small and medium enterprises in Nakuru central business district. The study intended to find whether Perceived opportunity for evasion, tax knowledge and education, fines and penalties and compliance cost affect tax compliance among Small and Medium Enterprises in Nakuru Central Business District. Data was collected using questionnaires and analyzed using descriptive and inferential statistics. Findings were presented using frequency tables, percentages and inferential statistics tables while respondents' response rate was 73.7%.

5.2.1 Perceived opportunity for tax evasion

The first objective of the study was to examine if perceived opportunity for tax evasion affects tax compliance among SMEs. The findings showed that 28.4% of respondents agreed to have manipulated figures in tax return since there was no need to send supporting documents to KRA (x^2=65.812, p>0.05). These findings are consistent with those of (Hanlon *et al.,* 2007; Rice, 1992) who suggested that SMEs are more likely to cheat than other groups of taxpayers. Majority of respondents (83.9%) disagreed that tax authority was tolerant with them for not filling exact tax returns as per their income (x^2=86.273, p<0.05). 75.5% of respondents disagreed that there exist opportunity windows to evade tax up until amnesties are granted with only a 4.5% of the respondents agreeing (x^2=49.785, p>0.05). The respondents were indifferent with a small margin with 40.7% disagreeing and 45.8% agreeing that the tax authority had limited capability to investigate all income reported to it thus giving room for under reporting (x^2=78.148 , p<0.05). A large number of respondents (60.6%) agreed that tax officers were not corrupt thus opportunities to evade taxes were minimal, with only 16.2% of the respondents holding a contrary opinion (x^2=73.057, p>0.05). 43.2% of the respondents agreed that tax authorities do not focus much on SMEs with 44.6% of respondents disagreeing (x^2=79.646, p>0.05). Majority of the respondents (65.8%)

agreed that the probability of being detected by the tax authority for not declaring the exact income was high with only 18.6% of respondents disagreeing (x^2=79.646, p<0.05).A fairy large number of respondents (31.6%) admitted to have run other businesses in remote areas where tax authorities never visit (x^2=57.212, p>0.05). It was established that perceived opportunity for tax evasion has no statistically significant effect on tax compliance among SMEs (Chi2 =106.873, Prob>chi2 =0.254). There exist a statistically insignificant, negative relationship between perceived opportunity for tax evasion and tax compliance (rho= -0.026; p>0.05).

5.2.2 Tax knowledge and education

The second objective of the study was to examine if tax knowledge and education affects tax compliance among SMEs. The findings showed that 62.6% of respondents disagreed to have knowledge on which income should be included or excluded in determining the taxable income (x^2=77.872, p<0.05), while majority of respondents (74.2%) disagreed that they knew how to declare actual income received from all sources to the tax authority(x^2=75.978, p>0.05). 54.8% of respondents agreed that they understood that they should pay taxes due within the prescribed period from the date of issue of the Notice of Assessment or within the stipulated period (x^2=83.078, p<0.05). Only 34.2% of respondents agreed that they knew how to keep business records (x^2=80.095, p<0.05), while a larger majority of respondents (98.7%) of respondents disagreed that they were well versed with the existing tax laws (x^2=43.384, p<0.05). Taxpayers must have sufficient tax knowledge in order to assess their tax liability correctly and to file tax return forms on time (Fatt & Khin, 2011). 73.5% of the respondents held the opinion that tax authorities need to train and carry out public awareness campaigns targeted at the SME sector on matters relating to taxation (x^2=86.041, p<0.05), with a 43.9% of respondents agreeing that they were aware that they should obtain a tax payer identification pin number as well as register their business as a tax agent with the tax authority (x^2=69.256, p>0.05).It was established that tax knowledge and education has no statistically significant effect on tax compliance among SMEs (Chi2 =90.735, Prob>chi2 =0.838). It was also established that there exist statistically insignificant, negative relationship between tax knowledge/education and tax compliance (rho= -0.031; p>0.05).

5.2.3 Fines and penalties

The study's third objective of the study was to find out if fines and penalties influence tax compliance among SMEs. 46.4% of respondents disagreed that the penalty rates were very low and thus respondents could afford to pay the penalty or raise from family and friends (x^2=18.896, p<0.05), while 35.5% of respondents agreed that since they were not legally obligated to audit their books of accounts prosecution by tax authorities was not possible (x^2=92.561, p<0.05).A larger majority of respondents (44.5%) were not sure whether there exist punitive fines and penalties imposed on SMEs for tax filing non compliance with only a minority of respondents 9.6% agreeing that punitive fines and penalties exist for tax filing non compliance (x^2=70.685, p>0.05). Tax compliance enforcement among SME operators was found to be very weak as agreed by 50.3% of the respondents (x^2=83.386, p<0.05), while a majority (45.8%) of respondents were uncertain on whether penalties for non compliance were lower than their tax savings (x^2=51.234, p>0.05). 78.1% of respondents agreed that serious enforcement and penalty by the KRA may result for tax filing non compliance (x^2=89.894, p<0.05). Tax authority audits and investigations were few among SME according to a majority 70.3% of respondents (x^2=95.958, p<0.05). Okello (2014) asserts that tax audits are generally a costly matter thus explaining why tax authority infrequently carries them out. A majority of respondents (70.4%) disagreed that ax savings on non-compliance were higher than the fines and penalties levied (x^2=94.386, p<0.05). It was established that fines and penalties has statistically significant effect on tax compliance among SMEs (Chi2 =131.098, Prob>chi2 =0.043). It was also established that there exist statistically insignificant, negative relationship between fines/penalties and tax compliance (rho= -0.038, p>0.05)

5.2.4 Tax compliance cost

The fourth objective of the study was to investigate if tax compliance cost affects tax compliance among SMEs. 41.9% of respondents agreed that having been tax none compliant in the past they usually wait on tax amnesty windows to come clean (x^2=111.830, p<0.05), while 52.9% of respondents agreeing that the cost of filing tax returns was reasonable (x^2=86.423, p<0.006). A few respondents (16.1%) believed that costs incurred in efforts to be compliant should be tax deductible (x^2=128.373, p<0.05), with a 7.1% of respondents agreeing that i-tax has reduced compliance cost (x^2=44.941 p>0.05). On tax refunds waiting period, 11.6% of respondents said that the waiting

period was long (x^2=86.542, p<0.05) and the cost of hiring a tax agent was termed as reasonable by 38.7% of respondents (x^2=118.341, p<0.05). 47.1% of the respondents agreed that the cost of travelling in order to follow up on refunds was reasonable (x^2=102.759, p<0.05), while cost of full compliance as compared to the costs of non compliance was found to be high by 71% of the respondents (x^2=46.977, p>0.05). It was established that tax compliance cost has no statistically significant effect on tax compliance among SMEs (Chi2 =110.474, Prob>chi2 =0.183). There exist a statistically insignificant, negative relationship between perceived opportunity for tax evasion and tax compliance (rho= 0.024; p>0.05).

5.3 Conclusions of the findings

The study revealed that perceived opportunity for tax evasion, tax knowledge and education, fines and penalties and tax compliance cost affects tax compliance among SMEs in Nakuru. The Kenya revenue authority has made good effort to ensure that small and medium enterprises that are taxable remit taxes with ease. However, this study has revealed that enterprises owners manipulate figures in tax return since there was no need to send supporting documents .The tax authority should ensure revenue streams are tracked by involving other stakeholders such as financial institutions where business owners hold bank accounts, since majority of the respondents also agreed that the probability of being detected by the tax authority for not declaring the exact income is high. The respondents were indifferent on whether tax authority had limited capability to investigate all income reported to it thus giving room for under reporting. KRA should enhance its manpower to ensure monitoring and tracking of all income reported by SME operators and make sure that focus is given more on SME sector as respondents agreed that tax authorities do not focus much on SMEs leading to running of other businesses by in remote areas where tax authorities never in a bid to evade paying turnover taxes.

Respondents disagreed to have that they knew which income should be included or excluded in determining the taxable income while others disagreed that they knew how to declare actual income received from all sources to the tax authority with a larger majority of respondents disagreeing that they were well versed with the existing tax laws. Thus the tax authority should organize training to sensitize SME operators on taxation matters, including required documentation and deadlines. Tax authorities need to train and carry out public awareness campaigns targeted at the SME sector on matters relating to taxation as well as conduct record keeping trainings to SME operators. The

tax authority should hike penalty rates for tax returns filing non compliance as well as conduct a frequent audit on financial records on SME operators these enforcements may enhance tax returns filing compliance among SME operators .On tax refunds waiting period should be shortened, KRA should ensure tax officers frequently visit SME operators so as to offer assistance on tax related matters as this will reduce cost incurred in hiring tax agents. Majority of SMEs operators admitted that they don't file tax returns taxes.

5.4 Recommendations

Based on findings of the study, the study recommended the following measures on the objectives that were being investigated:

It is recommended that The Kenya revenue authority should ensure revenue streams are tracked by involving financial institutions since majority as well as enhance its manpower to ensure monitoring and tracking of all income reported by SME operators. The tax authority should organize training to sensitize SME operators on taxation matters, including required documentation and deadlines, train and carry out public awareness campaigns targeted at the SME sector on matters relating to taxation as well as conduct record keeping trainings to SME operators. The authority should hike penalty rates for tax returns filing non compliance as majority of respondents said they don't file tax returns accurately and on time.

5.5 suggestions for further research

The study suggests further research on the following three areas related to this study:

A research on macro and micro factors affecting tax compliance among individual households as well as SMEs in other areas, these studies may aid in research finding generalization a fiscal policies formulation by the tax authority. A an empirical research should be influence of taxation matters training on tax compliance among Small and Medium operators.

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APPENDIX 1: QUESTIONNAIRE

The purpose of this survey is to analyze the factors affecting tax compliance in the SME sector with the aim of formulating policies aimed at enhancing tax collection. All responses/answers provided in this survey will only be used for academic purposes and will be kept confidential.

SECTION A: BACKGROUND INFORMATION OF THE RESPONDENT

1. How long have you been in business?

   Less than 5yrs (　) 　　1-5 yrs (　) 　　6-11 yrs (　) 　　Above 12 yrs (　)

2. What is your highest level of education?

   High School Certificate 　　　　( )

   Certificate/Diploma 　　　　　　( )

   Under Graduate Degree 　　　　( )

   Professional course 　　　　　　( )

   Post Graduate 　　　　　　　　( )

   Other (Specify) 　　　　　　　　( )

3. What is your average annual turnover?

   Less than Ksh 50,000 　　　　(　)

   50,000-200,000 　　　　　　(　)

   200,000-350,000 　　　　　　(　)

   Above 350,000 　　　　　　　(　)

4. Have you attended/passed any formal taxation course/training organized by KRA or university or any other?

   Yes 　(　) 　　　　　　　　No 　(　)

5. Have you ever been audited by KRA? If Yes, how many times?

   Yes 　(　) 　　　　　　　　No 　(　)

6. Have you ever engaged in the following activities?

   Under reporting incomes? 　　Yes ( ) 　　　　　　No ( )

   Over claiming deductions? 　　None ( ) 　　Yes ( ) 　　　　No ( )

SECTION B: PERCEIVED OPPORTUNITY FOR TAX EVASION

Perceived Opportunity For Tax Evasion					
	5	4	3	2	1
Since the supporting documents do not need to be sent to the KRA, I can manipulate the figure in the tax return					
If detected not reporting my exact income, I believe that the tax authority is tolerant towards my offence and will escape without any punishment.					
There are sufficient windows of opportunities to evade taxes up until amnesties are granted					
I believe the tax authority has limited capability to investigate all income reported to them so I have an opportunity to under report					
Tax officers are corrupt therefore I believe that opportunities to evade taxes and get away with it are plenty					
Tax authorities do not focus much energies/resources on SMEs					
I believe that the probabilities of being detected by the tax authority for not declaring the exact income that I receive are low.					
I run other businesses elsewhere in remote areas where tax authorities never visit					

Key:
Strongly agree (5), Agree (4), Not Certain (3), Disagree (2), Strongly disagree (1)

SECTION C: TAX KNOWLEDGE AND EDUCATION

S D (1)   Disagree (2)   Not Certain (3)   Agree (4)   Strongly A (5)

TAX KNOWLEDGE AND EDUCATION					
	5	4	3	2	1
I know which income should be included or excluded in determining the taxable income					
I know how to declare actual income received from all sources to the tax authority pertaining to income and expenditure for a period of seven years after submission of the Tax Return					
I understand that I should pay taxes due within the prescribed period from the date of issue of the Notice of Assessment or within the stipulated period					
I know how to keep records/documents					
I am well versed/keep up with the existing/developing /emerging tax laws/developments					
I believe tax authorities need to train and make public awareness campaigns targeted at the SME sector					
I know I should obtain a tax payer identification pin number as well as register my business as a tax agent					

SECTION D: FINES AND PENALTIES

S D (1)   Disagree (2)   Not Certain (3)   Agree (4)   Strongly A (5)

FINES AND PENALTIES					
	5	4	3	2	1
The penalty rates are very low and I can afford to pay the penalty or raise from family and friends					
I am legally not obligated to audit my books therefore successful prosecution is not possible					
There exists punitive fines and penalties imposed on SMEs					
The tax enforcement is very weak					
I believe that the penalty is lower than my tax saving due to not complying with tax laws.					
Serious enforcement and penalty by the KRA may result if I do not comply					
Tax authority audits and investigations are few among SME					
Tax savings on non-compliance are higher than the fines and penalties levied					

SECTION E: TAX COMPLIANCE COST

S D (1)   Disagree (2)   Not Certain (3)   Agree (4)   Strongly .A (5)

TAX COMPLIANCE COST					
	5	**4**	**3**	**2**	**1**
Having been none compliant in the past I usually wait to tax amnesty windows to come clean					
The cost of filling tax Returns is reasonable					
costs incurred in efforts to be compliant should be tax deductible					
I-tax has helped in reducing compliance					
I have to wait for tax refunds for a longer period					
The cost of hiring a tax agent is reasonable					
The cost of travelling in order to follow up on refunds is reasonable					
Costs of full compliance as compared to the costs of non compliance is high					

SECTION F: TAX COMPLIANCE LEVEL

TAX COMPLIANCE LEVEL	Strongly disagree (1), Disagree (2), Not certain (3) Agree (4), Strongly agree (5)				
	5	4	3	2	1
My business files taxes accurately					
My business pays all taxes on time					