International Journal of Business Management, Entrepreneurship and Innovation, Volume 6, Issue 1, 2024, PP 169-189, ISSN 2707-8027

Tax Compliance Procedures and Tax Compliance of Small and Medium Enterprises in Thika Town, Kiambu County, Kenya

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ABSTRACT

Small and medium-sized enterprises are an important part of the taxpayer population in any country around the globe. Their taxation usually poses a number of challenges. They are numerous but contribute relatively little to the state coffers, while often absorbing a large share of scarce tax administration resources much needed elsewhere in administering the tax system. The purpose of the study is to investigate the effect of tax procedures complexity on tax compliance of Small and Medium Enterprises in Kiambu County. The theories guiding the study include the ability-to-pay taxation theory, Prospect theory of taxation, and the Allingham and Sandmo theory. This study adopted a cross-sectional survey design because the design is best suited for finding out the prevalence of a phenomenon, situation, problem, attitude or issue, by taking a cross-section of the population as it stands at the time of the study. The target population comprised of 3616 registered businesses in Kiambu County. A sample of 385 SMEs managers and owners were selected using stratified random sampling method. Primary data was collected with structured questionnaires. Secondary data was collected by use of secondary data collection sheet to supplement the primary data. A pilot study was undertaken on 38 SMEs to test the reliability and validity of the questionnaire. The tool of analysis that was used for this study was Statistical Package for Social Sciences version 28. Correlation and multiple linear regression analyses was used to determine the relationship between the tax code complexity and tax compliance among small and medium sized enterprises in Kiambu County. Before taking part in the study, top management of the SMEs were asked for their informed consent in order to ensure that the research is carried out in a suitable setting free from internal interferences and influences. The study findings established that tax filing procedure, tax registration, tax remittance and tax rate determination have significant effect on tax compliance of small and medium enterprises. It is concluded that the procedures for online tax filing provided by the tax agency are a bit complex to understand by small and medium enterprises. The study concludes that tax registration by small businesses is received positively and not misconstrued as been punitive. Further, the tax agency should roll out tax filing education programs to small traders to make it easy to file taxes and the tax filing period should be reviewed to be flexible. The tax collector should revise the current compulsory requirements to register for tax by SMEs as it was found to affect tax compliance.

Key Words: *Tax Compliance Procedures, Tax Compliance, Small and Medium Enterprises*

DOI 10.35942/ rwk93v04

Cite this Article:

Kamau, S., & Wanjohi, F., (2024). Tax Compliance Procedures and Tax Compliance of Small and Medium Enterprises in Thika Town, Kiambu County, Kenya. *International Journal of Business Management, Entrepreneurship and Innovation*, 6(1), 169-189. https://doi.org/10.35942/rwk93v04

1.0 Introduction

1.1 Background of the Study

The increased sophistication of business dealings and the globalization of markets have given rise to more complex and refined mechanisms of tax evasion (Masudi & Gambo, 2019). Furthermore, tax authorities have passed more complex anti-abuse regulations. However, tax complexity created to serve as a barrier against tax fraud, tax evasion and other ways of reducing or entirely avoiding one's commitment to pay taxes, ultimately often becomes a springboard for the realization of these same schemes of tax noncompliance, by exploiting the ambiguities and loopholes that tax complexity provides. This is a vicious circle, in which tax non-compliance and tax complexity nowadays frequently emerge as cause and effect of one other.

Complexity of the various regulatory and administrative obligations that have to be observed by enterprises is one of the most common complaints by business organizations. Compared to larger companies, SMEs suffer disproportionately from the regulatory burden. This is because the smaller enterprises often do not have sufficient financial and human resources to manage their obligations in the most efficient way. Tax obligations such as payment of taxes and other activities such as registration, documentation, reporting and recording constitute some of the most important requirements that enterprises have to comply with. Enterprises require either internal resources and/or external resources, e.g. tax consultants and accountants for their various tax compliance procedures. The cost factor presented by tax compliance is too vital to be underestimated.

In South Africa, studies conducted by economy watch dog on tax burdens on SMEs revealed that tax requirements procedures acted as stumbling blocks to tax compliance. A majority of SMEs experience their tax liability as an increasing burden since they lack enough skilled staff to handle tax compliance issues and are therefore, forced to incur “extra‟ tax costs. Most SMEs do not even recognize the tax incentives and services available to them. The study also noted that changes in tax policies sometimes result in an even more complex tax system. A clear finding was that elaborate tax incentive schemes which require sophisticated systems and skilled staff would often result in increasing compliance costs rather than provide real tax relief. The South African survey of “tax practitioners” identified the “capturing and processing errors made by the South African Revenue Service (SARS) and the time taken to correct these errors “as the most burdensome aspect of corporate income tax, provisional tax, and employees’ taxes. For VAT, it was the period taken to register as a VAT vendor and the time taken to be notified of such registration” (FIAS, 2018).

Kenya, in contrast to many other Sub-Saharan nations, has a high tax yield, with a tax to GDP ratio of above 20%. Compared to other nations in the region, Kenya is able to finance a far larger portion of its budget from internal resources than do other nations (Wagacha, 2019). Like the majority of developing nations, it has struggled with the common issues associated with tax systems that have rates and structures that are challenging to administer and comply with, are insensitive to growth and discretionary tax measures, resulting in low tax productivity, and generate little money but cause serious economic harm. They make an effort to use income taxation to achieve equitable goals, but Kenya and many other nations that sought to employ income taxation for redistribution fell victim to the same trap (Karingi & Wanjala, 2016).

There are challenges associated with the tax compliance levels among the SMEs in Kenya due to the nature of the firms (Simiyu, 2015). The turnover tax in Kenya introduced through the Finance Act of 2007 specifically targets the SMEs especially those with less than 5 million annual gross income (Osebe, 2015). Some of the challenges facing the taxation of the SMEs in Kenya include the fact that small businesses are normally owned by the owners who are also in charge of the accounting book (Muhangi, 2016). There is thus less incentive to comply with tax requirements

Kenya lost just over 2 billion USD, Tanzania lost 1.9 billion USD, and it lost 856 USD in 2011. According to historical patterns, revenue collection rose from Ksh. 800.5 billion in the 2012–2013 fiscal year to Ksh. 1.21 trillion in the 2015–2016 fiscal year. This reflects a 13.8% yearly growth rate overall. At 54% in 2013, Kenya's tax compliance levels were still viewed as being below the KRA's aim of 65% by 2018. (Kenya Revenue Authority, 2016). These numbers make it quite evident that tax compliance levels in Kenya are typically poor. A tax code is a law that prescribes the levies imposed by a government on individuals, businesses, other entities and on transactions, such as property sales, that are subject to its jurisdiction, to fund its operations. Tax complexity was described by Jackson & Milliron (2016) as one of the primary tax compliance behavior drivers, with the main assumption being that taxpayers can evaluate different complex choices through the right assessment of the accessible information, from which they make selections to lead to the best outcome (Walsh, 2012). Therefore, tax complexity basically involves calculations, ambiguity, changes, excessive detail, forms and record-keeping (Long & Swingen, 2017).

Complying with the tax code is expensive. IRS researchers recently estimated that corporations and partnerships spent more than $100 billion complying with the federal income tax for tax year 2009 (Contos, 2012). That figure includes both out-of-pocket expenses and the value of worker time devoted to compliance. The taxation of SMEs faces several major policy challenges. The first one concerns compliance costs of taxation. Existing empirical evidence clearly indicates that small and medium sized businesses are affected disproportionately by these costs: when scaled by sales or assets, the compliance costs of SMEs are higher than for large businesses. Given that small start-ups and research-oriented SMEs are generally considered as important factors for economic growth, tax compliance cost may slow down the economy.

Tax compliance is the taxpayers' ability and willingness to comply with the relevant tax laws and regulations (Ayuba, Saad, & Ariffin, 2016). This is also referred to as the accurate reporting of income and claiming of expenses in accordance with stipulated tax laws (Saipei & Kasipillai, 2014). Tax compliance is the readiness of businesses to abide by the tax authority's rules and regulations (Kanyinga, 2016). Tax compliance is generally understood by the IRS (2019) as the capacity and desire of taxpayers to comply with tax rules, declare the correct incomes in each year, and pay the appropriate taxes on time. In a broader sense, tax compliance calls for a certain level of sincerity, sufficient tax knowledge and the ability to use that knowledge, timeliness, correctness, and sufficient records in order to complete the tax returns and related tax documents (Singh & Bhupalan, 2016). According to Khadijah (2014), being tax compliant has three components: filing, reporting, and payment compliance. As a result, a taxpayer becomes non-compliant if the three dimensions are not met. The use of electronic filing systems is one method of achieving the higher voluntary compliance that most tax changes aim to achieve.

In Uasin-Gishu County, Kibiwott (2018) examined the factors that affect tax compliance. Based on the sample of 230 SMEs, the study came to the conclusion that revenue authorities should fairly manage the tax system and that tax compliance decisions are a factor in the delivery of quality service. The many elements influencing Kenyan landlords' voluntary tax compliance were studied by Karanja (2016). According to the study, when people believe the government is abusing their taxes, their tax attitudes shift, which has a significant impact on their tax compliance. The study's results also showed that landlords with higher levels of rental revenue have higher levels of compliance with the rental income tax. The study also made clear that a taxpayer's perception of the tax system, high relative tax rates, and greater tax knowledge are important elements that greatly influence their degree of tax compliance.

Kenya has a complex tax system that makes it expensive for taxpayers to comply with an increased cost of doing. A tax system that is more complex is costlier to administer, and hence is more expensive for taxpayers to comply. Corporate income tax rate is 30 percent, personal income tax rate ranges between 10 percent and 30 percent, VAT rate is 16 percent and while withholding tax rates begin from 2 percent and depend on income source and whether one is a Kenyan or not (Government of Republic of Kenya, 2012). Thiga and Muturi (2015) conducted a study on Factors That impacts Tax Laws compliance amongst Kenyan SMEs and found tax rates and tax compliance expenses are highest tax compliance contributing factor.

According to Bjork's (2003) theory, tax code complexity changes affect compliance, and lowering non-compliance leads to increased tax revenue. Because of their small size and weak organizational structure, SMEs bear an excessive amount of regulatory and tax responsibilities (Pope & Abdul-Jabbar, 2008). Due to their lack of resources and necessary expertise to comply with tax rules, SMEs face a significant problem with tax compliance. High compliance expenses also contribute to tax evasion and avoidance among SMEs. Because counties are less competitive as a result of unattractive taxation, this discourages investment. Tax evasion is a prevalent issue, according to studies (Kasipillai &Abdul Jabbar, 2006). According to Fagbemi, Uadile, and Noah (2010), tax evasion is more common in developing nations, which slows economic progress and causes socio-economic issues.

Small and Medium businesses (SMEs) are types of small firms that don't generate a lot of revenue and just employ a few people. These businesses are typically sole proprietorships, companies, or partnerships that are privately owned and run. Since the average SME pays a very tiny amount of tax compared to what a larger business would, tax authorities often focus more on larger corporations (Livoi, 2017). In developing countries, tax compliance is currently a hot topic as governments at all levels look for ways to increase the effectiveness of tax revenue collection in order to finance their budgets.

In Thika Twon there are thought to be 3616 SMEs in Kiambu County that are registered and employ between 5 and 50 people (Loo, McKerchar & Hansford, 2019). On the basis of this, KRA ought to develop a platform for SME tax compliance. In order to promote positive economic growth and development, reduce poverty, and raise County residents' quality of life, the creation of SMEs should be supported and promoted (Munyoro, 2017). Kiambu county works to provide SMEs with the essential support so they can maximize their business earnings. The County Government requires all Kiambu County Government agencies to enhance, create, and maintain conditions that are the County's SME-friendly environment (Bett, 2020).

Small and medium-sized enterprises (SMEs) represent untapped income potential and an unequal playing field in many nations (Kanyi & Kalui, 2014); as such, they must be included in the tax net. However, despite the fact that laws are a necessary regulator for the establishment of the necessary social security regulations and the protection of the business environment and the security of economic agents, they may also impede compliance and the expansion of the business through additional costs and administrative challenges.

1.2 Statement of the Problem

Tax compliance is concerned on the timely and accurate submission of tax remittance information to the revenue authority. The tax code complexity has a direct impact on the tax compliance levels (Nakiwala, 2015). The cumbersome tax system in most countries, both on the policy and the administration side, is considered as one of the top reasons for operating in the informal economy. The government has implemented a variety of tax reforms to combat tax evasion. However, it has not yet been conclusively determined whether or not the aforementioned measures have led to the targeted voluntary tax compliance by SMEs that was intended (Livoi, 2017).

There are challenges associated with the tax compliance levels among the SMEs in Kenya due to the nature of the firms (Simiyu, 2013). The turnover tax in Kenya introduced through the Finance Act of 2007 specifically targets the SMEs especially those with less than 5 million annual gross income (Osebe, 2013). Some of the challenges facing the taxation of the SMEs in Kenya include the fact that small businesses are normally owned by the owners who are also in charge of the accounting book (Muhangi, 2012). There is thus less incentive to comply with tax requirements.

Although there are several studies on tax compliance challenges in Asian countries, very little research has been done in the Kenyan MSMEs context. Suleiman (2021) researched on tax compliance challenges among SMEs in Saudi Arabia and established that equipping taxpayers with adequate tax knowledge and proper education reduces compliance costs and fines and increases compliance. It is clear that these studies have concentrated on other counties, middle-class taxpayers, and large taxpayers, leaving a contextual research gap. As a result, this study aims to close this knowledge gap by examining how tax compliance procedures in Thika town, Kiambu County affect small- and medium-sized business performance.

1.3 Objective of the Study

To investigate the effect of tax compliance procedures on tax compliance among Small and Medium Enterprises in Thika town, Kiambu County.

2.0 Literature Review

2.1 Theoretical Review

2.1.1 Ability-To-Pay Taxation Theory

The theory was propounded by Adam Smith the father of economics in 1776. The theory on Ability-to-pay is a progressive principle that guides taxation administration in different jurisdictions. According to the ability-to-pay principle, individuals should pay taxes that correspond with their income.

According to the principle, taxes payable by an entity should be premised on the amount of money that people and businesses earn from their operations. Subsequently, people who earn more money should and are expected to pay more money through higher rates of taxation. Higher taxation rates imply that a significant portion of the income of the business ends up as taxation (Downer, 2016). The ability-to-pay theory does not consider the amount of services that the taxpayers use. The taxation model can be described as a form of progressive taxation that holds that taxes should always be levied based on the taxpayer's capability to pay. Moreover, the provisions of the theory stipulate that individuals with most resources contribute towards the public services available to the masses. Businesses and the public within a country rely on government services such as healthcare, education and security. Subsequently, ability-to-pay theory ensures that businesses and individuals that can best pool financial resources should pay more taxes. According to the theory on ability-to-pay, low-wage earners most likely require all their earnings and having a low taxation rate ensures that they keep a larger percentage as this will stimulate the economy (Schwarz, 2017). The theory is subjective as it considers the sacrifice an individual or business undergoes in paying a tax. Payment of tax causes disutility and the individual feels a pinch that equates to the sacrifice they make in the process of business operations.

Equal taxpayers and individuals should be treated equally and therefore, persons with similar ability to pay taxes should pay similar taxes. The theory, of ability-to-pay corresponds with the study independent variables of tax rates. SMEs business decisions depend on the availability of funds which can be constrained through high rate of taxes that limit liquidity.

2.1.2 Prospect Theory of Taxation

The prospect theory was proposed by psychologists Daniel Kahneman and Amos Tversky in 1979, and later in 2002 Kahneman was awarded the Nobel Prize in economics for it. Under prospect theory, the taxpayer's utility function is concave for gains. On the other hand, if the advance tax payment were lower than actual tax liabilities, then by subsequently reporting additional income the taxpayer would owe taxes to the government, a loss. Prospect theory is often used to predict individuals' risky tax decisions. For example, individuals who are in a tax due (refund) position are predicted to engage in more (less) tax noncompliance. This is known as the "withholding phenomenon". However, tax noncompliance is not just risky, it is also unethical.

Prospect theory posits that when individuals are in a loss (gain) situation it causes aggravation (pleasure) and these emotional reactions lead individuals to take (avoid) risks in the loss (gain) domain (Kahneman & Tversky, 1979, KT hereafter). Prospect theory is often assumed to explain risky and ethically-sensitive tax compliance decisions (e.g., Schepanski & Kelsey, 1990; White, Harrison, & Harrell, 1993; Jackson & Hatfield, 2005; Brink & Lee, 2015). However, prospect theory is about decision making under conditions of risk, *not* about ethical behavior. This is important because making an unethical choice causes negative feelings of its own, such as feeling guilty or violating one's moral standards (Bhattacharjee, Berman, & Reed, 2013).

Under prospect theory the taxpayer's utility function is convex for losses and thus might be more willing to take the gamble of evading taxes. Therefore, the level of obligatory advance tax payments can complement the deterrence ability of the tax authorities. Bernasconi and Zanardi (2004) applied cumulative prospect theory to tax evasion by considering a "general" reference point. There are two states of the world, 'income is audited' and 'income is not audited'. In their setting, it is possible for the tax evader to be in the domain of gains or in the domain of losses in both states of the world. The theory supports tax filing, tax registration and tax remittance variables in the study.

2.1.3 The Allingham and Sandmo Theory

The Allingham and Sandmo argument contend that the government discourages tax evasion through a punishment arrangement and audits, according to Nguyen et al. (2020). When a taxpayer decides that the cost of dodging tax is too low and that it is unlikely that they will be caught or subject to an audit, they will choose to break the law and avoid paying their taxes. When a taxpayer believes that the cost of compliance is significant, they are also more likely to avoid taxes. Involved and time-consuming tax systems and procedures frequently encourage tax avoidance. Tax evasion will occur if a taxpayer feels that the tax rate is too high and harsh. According to Ng'eni (2016), there is a negative association between tax evasion, the likelihood of being caught, the severity of the punishment, and the high transaction costs related to tax legislation.

Allingham and Sandmo pioneered income tax evasion in 1972, where a wise and moral taxpayer increases predicted utility, which solely depends on pay (Mondal, 2021). When caught, the operator is required to pay fines based on the amounts of unpaid wages. When the tax rate increases, competing salary and substitution effects may promote essentially tax compliance, which is a significant relative static outcome. The substitution effect encourages evasion because the marginal benefit of fraud increases with the tax rate. Contrary to popular belief, the pay impact will often discourage tax evasion since a higher tax rate makes a taxpayer who has reduced their overall risk avoidance feel worse off and hence reduces risk taking. As a result, the overall result is unclear.

Wagacha (2019) showed that the replacement effect vanishes when the penalty is imposed on the amount of taxes that have been evaded, all things considered under most existing tax legislation. In the first ideal, there is no substitution impact because the penalty for hidden wage increases is proportional to the tax rate. The remainder of the salary effect is responsible for encouraging the taxpayer to commit less fraud. The end result is better compliance as a result. This finding, which prompted a ton of fantastic extensions, is maybe the most important one in the early work on tax avoidance, according to Yilma (2020). Due to their challenges in adhering to tax regulations, businesses are more likely to engage in tax evasion. They must adhere to stringent deadlines and maintain accurate books of accounts. Tax evasion occurs in this type of setting. The notion can be used to explain why paying for tax compliance is necessary. When tax payers believe the cost of compliance to be excessive, they would evade paying taxes. The study supports tax compliance variable in the study.

2.2 Empirical Review

2.2.1 Tax Filing Procedures and Tax Compliance

Several empirical studies on tax filling procedures have been conducted, albeit in various contexts. Pippin and Tosun (2014) study in United States analyzed the demographic, socio-economic and geographic factors affecting electronic tax filing (e-filing). Research results indicated that there was significant variation in e-filing rates across and within different states. E-filing rates were found to be more common in rural areas that had low population size, states that had a lower share of female population and areas with higher population of Hispanics, Afro-Americans and Asians. However, the study by Pipping and Tosum focused on demographic and socio-economic factors and not tax code complexity as is the focus of the current study thus present conceptual gaps. Further, the study was done in USA which has differing socio-economic environment to Kenya.

A study conducted by Atawodi and Ojeka (2012) in North-Central Nigeria to evaluate the factors that affect tax compliance of SMEs found that most SMEs attributed their non-compliance to high tax rates and complex filing procedures. They recommended that Small and Medium Enterprises should be levied lower amounts of taxes so that they will have enough funds for other activities that will lead to business growth. Furthermore, they opined that it would help SMEs get better equipped to survive in a competitive market. The study, however, was done in Nigeria and focused on high tax rates thus present contextual and conceptual gaps.

Gidisu (2012) examined the automation system procedures of the Ghana Revenue Authority on the effectiveness of revenue collection. The evidence suggested a positive impact of automation system usage and the cost of tax administration, automation and effectiveness of revenue collection. Additionally, automation was significantly related with tax clearance time. In Gambia, Jallow (2016) examined the nature and prospects of computerization in tax and customs administration from The Gambia's tax system perspectives. The study found out that some challenges were yet to be resolved in the area of the payment, registration and audit modules that were not interrelating seamlessly. The results of the study revealed significant positive relationships between automation and tax, and customs administration. However, the study by Jallow was limited to computerization in tax administration and talked nothing about tax complexity and tax compliance.

Muturi and Kiarie (2016) looked at the online tax system effects on tax compliance among small taxpayers in Meru County, Kenya. Specifically, the study looked at online tax registration and its effect on tax compliance. The study adopted a descriptive research design. Data was collected using structured questionnaire, which covered all the variables of the study from 60 sampled taxpayers from Meru County tax District. Data obtained were subjected to quantitative methods of data analysis using SPSS (version 20). In addition to descriptive statistics, both correlation and regression analyses were done and summaries presented. The findings of the study were that online tax system does affect tax compliance level among small taxpayers in Meru County. However, the study present conceptual gaps as it narrowed down to online tax system and not tax code complexity.

Sagas, Nelimalyani, and Kimaiyo (2015) evaluated the effect of the electronic tax register on Kenya's western region's revenue collection by the Kenya Revenue Authority. According to the results of their investigation, 75% of the respondents believed that ETR devices have reduced instances of tax evasion. Due to their effectiveness, 86% of the respondents believed that ETRs had contributed to an increase in revenue collection. Ming, Nuruld and Aham (2010) looked at the ICT skills required of a recent accounting graduate who is joining a tax firm, the use of electronic tax (e-tax) applications in tax practice, how senior tax practitioners rated the ICT and e-tax applications skills of recent graduates, and whether tax practitioners had any thoughts on incorporating ICT knowledge and tax software into tax courses. The study used a questionnaire-based survey research design that was carried out online. According to the study, student knowledge of ICT and electronic tax systems had a favorable effect on compliance. However, the study context was focused on tax practice and not tax code complexity and compliance in SMEs context.

Bernard, Memba and Oluoch (2018) looked at the influence of costs on ability of the tax payers to comply with taxes. The study focused on investor in the Export Processing Zones. The study leveraged on survey design covering 152 firms and the census was used. It was shown that the cost of compliance had a significant influence on ability of the tax payers to comply with taxes. These costs of compliance included indirect as well as direct costs including the costs of auditing, the cost inured in hiring of the personnel, experts and the agents, time that one tax in completion of tax assessment and filling of returns as well as keepings staff so as to comply. However, the study by Bernard et al., (2019), focused on costs and its implication on tax compliance and failed to link tax code complexity to tax compliance as is the case in the current study.

Chindengwike and Kira (2022) researched on the effect of tax rate on taxpayers' voluntary compliance in Tanzania. A cross-sectional survey research design technique was used. The study employed document review, and survey in collecting both primary data and secondary data. Besides, systematic, unsystematic random sampling and purposive sampling were used as sampling procedures in this study. The study involved a sample size of 99 respondents who are SMEs' taxpayers. The findings of the study showed that there is a negative effect of the tax rate on taxpayers' voluntary compliance. Again, the study indicates that the presence of good tax rates improves taxpayers' voluntary compliance and the tax rates influence taxpayers' voluntary compliance. However, the study presents conceptual gaps as it focused on tax rate and not tax rate determination in the context of MSMEs. However, the study by Chindengwike and Kira was limited to tax rates and not tax code complexity.

Kanyinga (2016) came to the conclusion that the majority of SMEs said they use e-tax registration and file their return online in his study on the impact of tax reforms on compliance with turnover tax among small and medium firms in industrial areas. To increase TOT compliance among Kenya's small and medium-sized businesses, KRA has integrated information technology into its operations. SMEs concurred that computerization, SIMBA, ITMS, ITR, and EFT are the primary forces promoting compliance and, thus, increasing revenue collection. SMEs claimed that KRA had instructed them on how to pay turnover tax. It is possible to infer from the justifications given that teaching people how to calculate tax payments and file returns while registering for turnover tax results in higher compliance. The majority thus concurred that TOT training significantly influences compliance. However, the study adopted differing theoretical constructs to measure tax code complexity as to those adopted in the current study.

3.0 Research Methodology

Cross-sectional survey methodology was used in this study because it is the most effective method for determining the prevalence of a phenomena, situation, problem, attitude, or issue by using a cross-section of the population at the time of the study. One fundamental feature of this research method is the use of a questionnaire to collect all measures for a sample at one time (Gujarati, 2017). Registered by KRA in Thika town as of June 2023 and operating for more than three years in Thika town made up the target population of this study, with a focus on the owners and/or managers of these SMEs. The 3616 SMEs that were officially registered by KRA in Thika town as of June 30, 2023, representing a variety of industries, made up the target population, as stated in Table 3.1 by the KRA. By focusing on data from a small subset rather than all potential cases or elements, sampling techniques offer ways to help limit the amount of data that must be collected (Creswell, 2014). Using the estimated proportion ($p = 0.5$) and margin of error ($e = 0.05$), the sample size for the study targeting 3,616 participants will be as follows;

$$n = (Z^2 * p * (1-p)) / (e^2)$$

$n = (1.96^2 * 0.5 * (1-0.5)) / (0.05^2)$

$n = (3.8416 * 0.25) / 0.0025$

$n = 0.9604 / 0.0025$

$n \approx 385$

The stratified random sampling approach was used to divide SMEs in to different clusters based on their nature. Then simple random sampling approach was used to allocate the computed sample size across the different SMEs clusters based on their population. Stratified sampling is utilized when a population from which a sample is to be drawn does not consist of a homogeneous group, according to Kochetov (2020). The technique also involves segmenting the population into a number of pertinent strata, suggesting that the sample is probably more representative (Yin, 2017).

Structured questionnaires were used to capture primary data (Jebb & Tay, 2017). To gather data on important variables from the study's target respondents, a questionnaire was created. The survey included structured questions on a Likert scale with five possible responses. According to Yin (2017), Likert scales are beneficial because they show how strongly a respondent feels about the topic of the questions, are simple to analyze, make it simple to gather data, are more comprehensive, and are also rapid. These respondents were chosen precisely because of their capacity to offer useful data for the study. Secondary data was collected from SMEs performance reports, books, and articles. Journals and books from relevant research studies can be used to supplement primary data. According to Darlington and Hayes (2016), surveys have the advantage of making it simple to contact a large number of respondents. They also offer analytically simple, quantitative responses.

A pilot study helps the research determine whether the tools used for data gathering have any errors, restrictions, or other problems. Prior to the start of the study, it enables the researcher to make any necessary changes. Odoh and Chinedum (2018) claim that in order to pre-test the questions, a pilot study entails giving the questionnaires to a small sample of the target population. Therefore, pilot research was conducted with 38 SMEs randomly picked in Kikuyu town to evaluate the validity and reliability of the questionnaire. This mostly hinges on the conventional wisdom that a pilot test should make up 1–10% of the sample (Kumar, 2019). The 38 SMEs were not included in the final analysis.

Validity, according to Jebb and Tay (2017), is the precision and significance of inferences drawn from research findings. In other words, validity is the extent to which findings from data analysis accurately reflect the phenomenon being studied. The KMO-Bartlett test, the most used internal consistency metric, will be employed by the researcher. Although it is possible to declare that its value ranges from 0 to 1, a satisfactory value of more than 0.6 is necessary for the scale to be dependable. A scale or measurement tool that is reliable produces consistent results. It means a test will be regarded as reliable if it is administered using any instrument for a specific subject and the results are consistent across all attempts. The stability and consistency of the test result are what reliability is mainly concerned with (Quan-Haase & Sloan, 2017). This was accomplished by identifying the correlation between scores acquired from various scale administrations. The scale is dependable if there is a strong relationship since it produces repeatable results. The internal reliability of the questionnaire used in this study was evaluated using Cronbach's alpha. The range of values is 0 to 1.0, with 1.0 denoting perfect reliability and 0.7 being regarded as the lower level of acceptability (Jebb & Tay, 2017).

With regard to the study's objectives, the data will be gathered, handled, and analyzed using both descriptive and inferential statistics. The Statistical Package for Social Sciences (SPSS) version 28 was the analytical tool used for this investigation. Descriptive statistics like mode, median, mean, and standard deviation was used to analyze the data. F-tests (ANOVA) was used to assess research hypotheses in order to gauge the statistical significance of the relationships between the variables and derive study-related conclusions. Additionally, to ascertain the connection between tax policy revisions and tax compliance among small and medium-sized businesses in Kiambu County, multiple linear regression and correlation studies will be utilized.

The regression model adopted is as follows:

$Y_{ij}=\beta_0+\beta_1x_{1ij}+\beta_2x_{2ij}+ \beta_3x_{3ij} + \beta_4x_{4ij} +e_{ij}$

Where:

Y = SMEs tax compliance

$\beta0$= Constant

X1= Tax filing procedures

X2= Tax registration

X3= Tax remittance

X4 = Tax rate determination

e_i= Error term

The Graduate School at Kenyatta University was contacted for ethical approval, and the National Commission for Science, Technology, and Innovation was contacted for a research permission. Before taking part in the study, top management of the SMEs were asked for their informed consent in order to ensure that the research is carried out in a suitable setting free from internal interferences and influences. All study participants received comprehensive information about the study's goals so they may decide for themselves whether to join or not. The study's participants' data were handled with the strictest secrecy.

4.0 Data Analysis, Findings and Discussion

4.1 Descriptive Results

4.1.1 Tax Filing Procedures

Table 1: Tax Filing Procedures

	Mean	Std deviation
Online tax filing procedures provided by KRA are complex to understand	4.17	.231

There is no ease of tax filing as the systems are not straight forward	4.23	.536
The filing of tax period provided by KRA is not flexible	4.02	.444
The filing of tax requirements from KRA makes it difficult for my business to file tax returns	4.26	.703
The tax filing procedures requires computer knowledge which am lacking	4.01	.849

The results in Table 1 have shown that respondents agreed that online tax filing procedures provided by KRA are complex to understand and that in there is no ease of tax filing as the systems are not straight forward as indicated by a mean of 4.17 and mean of 4.23 respectively. Respondents also agreed that the filing of tax period provided by KRA is not flexible (mean=4.02) and that the filing of tax requirements from KRA makes it difficult for my business to file tax returns (mean=4.26). Respondents agreed that the tax filing procedures requires computer knowledge which they lack (mean=4.01).

4.1.2 Tax Registration

Table 2: Tax Registration

	Mean	Std. Deviation
Tax registration process through online portal for MSMEs has been simplified	4.41	.817
The requirements by KRA for tax registration makes it hard for MSMEs to register for tax	2.15	.634
Tax registration by small businesses is viewed as punitive and it is avoided at all costs	4.26	.509
The availability of iTax registration system makes it easy to register for tax	3.01	.822

Tax registration by small businesses has many compulsory information fields which most businesses do not have	4.10	.277

The results in Table 2 have shown that respondents agreed that tax registration process through online portal for MSMEs has been simplified and that the requirements by KRA for tax registration makes it hard for MSMEs to register for tax as indicated by a mean of 4.41 and mean of 4.26 respectively. However, respondents disagreed that tax registration by small businesses is viewed as punitive and it is avoided at all costs (mean=2.15). Respondents were indifferent to the statement that the availability of iTax registration system makes it easy to register for tax (mean=3.01). Respondents agreed to the assertion that tax registration by small businesses has many compulsory information fields which most businesses do not have (mean=4.10).

4.1.3 Tax Remittance

Table 3: Tax Remittance

	Mean	Std. Deviation
The tax remittance frequency provided by KRA is difficult to comply with in my business	4.13	.882
The self-assessment tax remittances have simplified tax remittance process	4.20	.887
Tax remittance by small businesses is costly as most owners seek paid services	4.82	.883
The tax category requirement during remittance process is hard to understand in the case of small businesses	4.89	.881
The remittance of taxes by small businesses requires enforcement	3.18	1.012

The results in Table 3 have shown that respondents agreed that the tax remittance frequency provided by KRA is difficult to comply with in my business and that the self-assessment tax remittances have simplified tax remittance process as indicated by a mean of 4.13 and mean of 4.20 respectively. Respondents also agreed that tax remittance by small businesses is costly as most owners seek paid services (mean=4.82) and that the tax category requirement during remittance process is hard to understand in the case of small businesses (mean=4.89). Respondents were indifferent to the statement that remittance of taxes by small businesses requires enforcement (mean=3.18).

4.1.4 Tax Rate Determination

Table 4: Tax Rate Determination

	Mean	Std. Deviation
The small businesses experience challenges in determining tax rates due	3.66	.753
The tax code provided by KRA is easy to understand and calculate	4.66	.748
The small business owners/managers do not have access to tax rate code	4.52	.741
The KRA tax rate code is ambiguous and not easy to understand which tax affects particular small business	3.64	.756
The KRA provides tax calculator to small scale traders which makes it easy to understand the tax due	2.37	.549

The results in Table 4 have revealed that respondents agreed that the small businesses experience challenges in determining tax rates due and that the tax code provided by KRA is easy to understand and calculate as indicated by a mean of 3.66 and mean of 4.66 respectively. Respondents also agreed that the small business owners/managers do not have access to tax rate code (mean=4.52) and that the KRA tax rate code is ambiguous and not easy to understand which tax affects particular small business (mean=3.64). Respondents disagreed that KRA provides tax calculator to small scale traders which makes it easy to understand the tax due (mean=2.37).

4.2 Correlation Analysis

Table 5: Correlation Coefficient Results

		TP	TReg	TR	TRD	TC
Tax filing procedures	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	297				
Tax registration	Pearson Correlation	.296**	1			

	Sig. (2-tailed)	.000				
	N	297	297			
Tax remittance	Pearson Correlation	.504**	.776**	1		
	Sig. (2-tailed)	.000	.000			
	N	297	297			
Tax rate determination	Pearson Correlation	.361**	.487**	1	1	
	Sig. (2-tailed)	.000	.000			
	N	297	297	297	297	
Tax compliance	Pearson Correlation	.597**	.466**	.239	.519	1
	Sig. (2-tailed)	.000	.000	.000	.017	

**. Correlation is significant at the 0.01 level (2-tailed).

Correlation results revealed that tax filing procedures had significant and positive correlation with tax compliance as indicated by r of 597. Also, bivariate correlation between tax registration and tax compliance was found to be favorably and moderately correlated. This is supported by a correlation coefficient of 0.466 and a p-value of 0.000. As shown by a r of 0.239 and a p-value of 0.000, the bivariate correlation between tax remittance and tax compliance was found to be significant and positive. The correlation between tax rate determination and tax compliance was revealed to be significant and positive (r = .519).

4.3 Diagnostic Test Results

4.3.1 Test of Normality

Table 6: Test of Normality

	Shapiro-Wilk		
	Statistic	Df	Sig.
Performance	.853	296	.119

The p-value was .119 which implies that residuals assumed a normal distribution.

4.3.2 Test of Multi-collinearity

Multi-collinearity test was conducted with the view of establishing the interrelationships between predictor variables and how such could potentially compromise the results of multiple regression analysis. It is indicated that multi-collinearity occurs when there are several variables (more than 1 variable) in a multiple regression analysis, and which are significantly correlated to each other. Consequently, some of the significant variables under study are made to be statistically not significant (Young, 2017). The variance inflation factors (VIF) as well as tolerance level (T) are the parameters used to test for multi-collinearity. Variance inflation factor is employed to measure the extent to which the variance of the estimated regression coefficient is inflated if and/or when the predictor constructs are correlated. Notably, VIF is reciprocal to T (Shrestha, 2020). Variance inflation factor less than 5 are acceptable since they demonstrate only moderate correlation between independent variables (Gupta & Gupta, 2022). The results of multi-collinearity test are shown in Table 7.

Table 8: Test of Multicollinearity

	Collinearity Statistics	
Study Constructs	**Tolerance**	**VIF**
Tax filing procedures	.945	1.039
Tax registration	.965	1.045
Tax remittance	.911	1.077
Tax rate determination	.889	1.113

a. Dependent Variable: Performance

According to the results shown in Table 8, all the four independent variables, that is, tax filing procedures (VIF = 1.039), tax registration (VIF = 1.045), tax remittance (VIF = 1.077), and tax rate determination (VIF = 1.113). This meant that there were no serious multi-collinearity problems detected in the study.

4.4 Multiple Regression Analysis

Table 9: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.698[a]	.487	.431	.74480

a. Predictors: (Constant), Tax registration, Tax filing procedure, Tax remittance, Tax rate determination

The regression results in Table 9, showed a moderate regression between the study variables. In the model summary, the R^2 is 0.487 indicating that predictors explain 46.1 per cent change in tax compliances.

Table 10: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1047.516	4	261.879	69.316	.000[b]
	Residual	1103.429	292	3.778		
	Total	2150.945	296			

a. Dependent Variable: Tax compliance

b. Predictors: (Constant), Tax registration, Tax filing procedure, Tax remittance, Tax rate determination

From the ANOVA results in Table 10, it was established that the significance value in testing the reliability of the model was obtained as 0.000 which is less than 0.05, the critical value at 95% significance level. Therefore, the model is statistically significant in predicting the relationship between the study variables.

Table 11: Regression Coefficients

	Unstandardized Coefficients		Standardized Coefficients		
Model	B	Std. Error	Beta	t	Sig.
(Constant)	11.519	4.061		2.836	.000
Tax filing procedures	.438	.199	.175	2.201	.035

Tax registration	.175	.059	.127	2.966	.020
Tax remittance	.519	.216	.483	2.403	.042
Tax rate determination	.407	.122	.175	3.336	.000

a. Dependent Variable: Tax compliance

The derived regression coefficients of the model are:

$$Y = 11.519 + .438X_1 + .175X_2 + .519X_3 + .407X_4$$

The regression results showed that independent variables had significant value less than 0.05 implying that they are all significant. From the results, it showed that holding all factors constant at zero, the change in tax compliance would be 15.012. Further, the regression results showed that a unit change in tax filing procedures would lead to 0.438 unit change in tax compliance. A unit change in tax registration would lead to 0.175 unit change in tax compliance. Further, a unit change in tax remittance would lead to 0.519 unit change in tax compliance and finally, a unit change in tax rate determination would lead to 0.407 unit change in tax compliance.

5.0 Summary, Conclusions and Recommendations

5.1 Summary of the Findings

The objective of the study was to investigate the tax compliance procedures and tax compliance of small and medium enterprises in Kiambu County. The response rate was 77.1% which was good. Majority of small businesses have registered with KRA and many businesses had been in operation for 8 years on average. According to the descriptive findings, respondents agreed that online tax filing procedures provided by KRA are complex to understand and that in there is no ease of tax filing as the systems are not straight forward. Respondents also agreed that the filing of tax period provided by KRA is not flexible and that the filing of tax requirements from KRA makes it difficult for my business to file tax returns. Respondents agreed that the tax filing procedures requires computer knowledge which they lack.

According to a descriptive analysis, respondents agreed that tax registration process through online portal for MSMEs has been simplified and that the requirements by KRA for tax registration makes it hard for MSMEs to register for tax. However, respondents disagreed that tax registration by small businesses is viewed as punitive and it is avoided at all costs. Respondents were indifferent to the statement that the availability of iTax registration system makes it easy to register for tax. Respondents agreed to the assertion that tax registration by small businesses has many compulsory information fields which most businesses do not have.

According to the descriptive findings, respondents agreed that the tax remittance frequency provided by KRA is difficult to comply with in my business and that the self-assessment tax remittances have simplified tax remittance process. Respondents also agreed that tax remittance by small businesses is costly as most owners seek paid services and that the tax category requirement during remittance process is hard to understand in the case of small businesses. Respondents were indifferent to the statement that remittance of taxes by small businesses requires enforcement. According to a descriptive study, respondents agreed that the small businesses experience challenges in determining tax rates due and that the tax code provided by KRA is easy to understand and calculate. Respondents also agreed that the small business owners/managers do not have access to tax rate code and that the KRA tax rate code is ambiguous and not easy to understand which tax affects particular small business. Respondents disagreed that KRA provides tax calculator to small scale traders which makes it easy to understand the tax due.

5.2 Conclusions of the Study

The study concludes that tax filing procedure has significant effect on tax compliance of small and medium enterprises. It is concluded that the procedures for online tax filing provided by the tax agency are a bit complex to understand by small and medium enterprises. Also the tax systems are not straight forward thus making it difficult for tax filing by the small traders and the filing of tax period provided by KRA is not flexible. The study concludes that the tax requirements regarding filings are the source of non-compliance in filing returns by small traders as many of them lacks computer use knowledge which is necessary to file returns.

The study concludes that tax registration has significant effect on tax compliance among small and medium enterprises. The process of tax registration through online portal is simple. However, the requirements by KRA for tax registration makes it hard for MSMEs to register for tax. The study concludes that tax registration by small businesses is received positively and not misconstrued as been punitive. The availability of iTax registration system makes it easy to register for tax and the compulsory requirements to register for tax by MSMEs poses a challenge to tax compliance as many small businesses lacks many of the required fields.

The study concludes that tax remittance has significant effect on tax compliance among small and medium enterprises. The study comes to the conclusion that the frequency of tax remittance required of small businesses by tax agency makes it difficult to comply. However, the availability of self-assessment has made it simple for small businesses to remit tax. The study concludes that there is issue of cost during tax remittance by small businesses as many small businesses engage third parties to remit taxes for them. Also, the tax category requirement during remittance process is hard to understand in the case of small businesses and enforcement is what makes small businesses to comply with tax remittance requirements. The study concludes that tax rate determination has significant effect on tax compliance. The tax rate determination by small and medium enterprises is challenging. The study concludes that the tax code provided by KRA is easy to understand and calculate. The tax rate code is inaccessible to owners/managers of MSMEs and it is ambiguous and not easy to understand. The tax agency does not provide tax calculator to small scale traders and this impacts tax rate determination by small traders.

5.4 Recommendations of the Study

The study recommends that the Kenya Revenue Authority should work on simplifying online tax filing procedures as they were found to be more complex by SMEs. Further, the tax agency should roll out tax filing education programs to small traders to make it easy to file taxes and the tax filing period should be reviewed to be flexible. In addition, the tax filing requirements by KRA should be as low as possible and many requirements deters small businesses from filing tax returns. The application for tax filing should be compatible in all electronic mobile devices as many small traders are computer illiterate. The study recommends that the tax registration through online platform should be simplified so as to motivate as many small businesses as possible to register. The Kenya Revenue Authority should simplify tax registration so as to make SMEs to register for tax as it was established that tax registration by small businesses is received positively. The Kenya Revenue Authority should reliably ensure availability of iTax registration system as it was found to make tax registration easy. The tax collector should revise the current compulsory requirements to register for tax by SMEs as it was found to affect tax compliance.

The study recommends that tax collector review the frequency of tax remittance required as it was found to affect compliance by SMEs. The tax agency should expand availability of reliable self-assessment tools so as to enhance tax remittance by small traders. The study recommends that the tax remittance process should be as simple as possible as many businesses engage services of third parties to remit tax for them thus attracting unnecessary costs in the process. The KRA should simplify tax category requirement during remittance process as it was found to be hard to understand. The study recommends that the tax collector should build mechanisms to aid small traders in determining tax rates due as it was found to be challenging. The tax rate should be made easy to calculate even without basic accounting knowledge and KRA should ensure tax rate code is accessible to owners/managers of SMEs and made easy to understand. Where necessary, the tax collector should provide tax calculator to small scale traders as this would encourage tax compliance.

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