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TECHNOLOGICAL TAX REFORMS AND COMPLIANCE AMONG SMALL AND MEDIUM ENTERPRISES IN BUNGOMA COUNTY, KENYA

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ABSTRACT

Tax compliance is an area of concern in Kenya because of increased burden on borrowing from abroad. Kenya has struggled with persistent budgetary deficits due to an imbalance between government revenue and expenditure. High levels of non-compliance by SMEs have prevented the economy from receiving the necessary funds to address the ongoing imbalance. The Kenyan government has made an effort to bring SMEs under the tax net unfortunately overall level of compliance among SMEs is still low. This study therefore assessed the effect of technological tax reforms on tax compliance among Small and Medium Enterprises in Bungoma County. The study was guided by the Economic Deterrence, Social Influence and Adam smith canons of taxation theories. The study took into account a ten year period from 2011 to 2021 during which the revenue authority had implemented a wide range of tax reforms in an effort to address several tax compliance issues. A descriptive survey design was adopted where a survey was conducted on 1,527 Small and Medium Enterprises in Bungoma County, Out of this target a sample of 317 enterprises was established through Yamane formula and then randomly sampled. Quantitative primary data was obtained through a structured questionnaire then analyzed by both descriptive and inferential statistics. The results of the multiple regression analysis demonstrated that technological tax reforms (β = 0.780, $P < 0.05$) has a positive and statistically significant effect on tax compliance among Small and Medium Enterprises in Bungoma County. Pearson correlation analysis revealed that there is a moderate positive and statistically significant relationship between technological tax reforms and tax compliance among SMEs in Bungoma county as supported by ($r=0.554$, $p< 0.05$). This led to the conclusion that an increase investment by Kenya Revenue Authority towards technological tax reforms has a positive results towards tax compliance among SMEs in Bungoma County. Based on that, the study recommends expanded taxpayer education on I tax matters and employing simpler payment methods such as Mobile money services and other mobile banking advancements.

Key Words: *Technological tax Reforms, Tax compliance, Small and Medium Enterprises, Bungoma County, Kenya*

BACKGROUND OF THE STUDY

Tax compliance is a multi-faceted measure that involves an individual or entity being willing and able to pay taxes on time, as well as the timely reporting of accurate tax information (Slemrod, 2016). Tax compliance is a very important aspect of any nation since taxation is the primary source of revenue that is used to fund public goods and services that the government is required to provide to its citizens. Roads, health care, education, and a reliable water supply are examples of such goods and services, which work together to create a favorable environment for businesses and allow the economy to grow as a whole (Atawodi & Ojeka, 2012). Tax compliance among SMEs is varied among nations (Obaid, 2020) reveal that SMEs in Yemen do not voluntarily comply with the tax regulations because of high tax rate, poor tax morale, inappropriate public expenditure to the preference of tax payers and poor structure of the tax system. (Newman, 2018) revealed that it is the fear of stiff tax penalties, which compel SMEs to comply with tax laws. Gilligan and Richardson (2015) in a study that looked at people from different cultures, it was found that tax compliance was lowest in Australia because there wasn't much tax information there, and it was highest in Singapore because tax information was given to people before they started a business.

Countries worldwide depend on taxation as the major source of revenue. Tax compliance is affected by tax fraud and tax evasion. Thus, tax evasion and tax fraud have placed the government under pressure to make tax reforms (Slemrod, 2016). One of tax reforms in Kenya is technological tax reforms, Technological tax reforms in Kenya includes I-tax system, ETR machine and KRA m – services, (livoi, 2019). The I Tax system, which was introduced in Kenya in 2011, was developed by the Indian company Tata to replace the prior online system (ITMS). Businesses and individuals can use the system to file returns online, examine their tax obligations, and track their tax status 24 hours a day. They can also upload tax files, request compliance certificates, and make actual tax payments. The system connects over 30 banks to ensure that the majority of taxpayers are protected. The I Tax technology has simplified and accelerated tax compliance while also ensuring its security, lowering the cost of tax compliance in logistics. The I Tax system's further rollout and operationalization in Kenya is expected to increase revenue yield by broadening the tax base, lowering compliance costs, and improving revenue administration (Economic survey, 2015).

Small and medium enterprises operating in the informal sector tends to exhibit low tax compliance even though they are eligible to pay taxes. This robs off revenue of many countries over the globe, making them unable to meet budgetary allocation and provision of essential services to their citizens. In most cases, taxable individuals aren't happy with the tax burden, making most of them shy away from disclosing relevant information on tax compliance (Oladipupo & Obazee, 2016). The level of tax compliance among SMEs in Kenya continues to be below projections despite the establishment of statutory provisions such as the introduction of a turnover tax or a presumptive tax targeting the informal sector. The effectiveness of the turnover tax, which is directed at SMEs, has generally remained below 50%. The presumptive tax, which targeted an estimated 2.7 million informal traders and was intended to generate 15% tax on the value of business licenses, was introduced in response to concerns about the turnover tax's underwhelming performance. However, the presumptive tax performed so poorly that the government switched back to the turnover tax with effect from 1 January 2019 to fill revenue gaps (Mathenge, 2021).

Low levels of tax compliance are demonstrated by a sizable portion of the informal sector, particularly SMEs in Bungoma County. By either evading taxes or avoiding them, tax payers fail to fulfill their obligations as required and when they become due. Professionals employ tax avoidance strategies to lower tax liabilities. However, tax evasion, which is also against the law, is on the rise, depriving the government of its primary source of funding. Taxable persons feel the tax burden is high as per the rates, leading high evasion proportions. The question of why low compliance on tax payment and why deprive the government of its revenue is exhibited by many economists, administrators and scholars (Nduruchi, 2017). It remains unclear whether the wide range of technological tax reforms introduced have helped in improving the state of compliance among small and medium enterprises in Bungoma County The study specifically seeks to determine the effect of technological tax reforms on tax compliance among small and medium enterprises in Bungoma, Kenya.

THEORETICAL FRAMEWORK

The economic model of criminal doings was proposed by Becker (1968). The theory supports the notion that taxpayers are moral utility maximizers who are guided by economic objective such as profit maximization and the risk of detection (Atawodi & Ojeka, 2012). The economic deterrence theory states that the benefits and the cost of tax evasion determine taxpayers' behavior. Taxpayers will base on factors such as the probability of government detection, fines and penalties for being tax compliant (Ali, Merima, Fjeldstad Odd-Hedge, 2013). Becker's work on economic crime was extended to the taxation content by Allingham and Sandmo in the early 1970s. They looked at why people don't pay their taxes, as well as the impact of penalty rates and the likelihood of discovery on tax evasion. They came to the conclusion that there is a link between this variable and the risk of discovery, and that a greater penalty rate as well as the probability of detection deters taxpayers from avoiding taxes. Many scholars questioned the effectiveness of deterrence alone in controlling behavior in the 1980s. Because of this, they began to focus their efforts on compliance research rather than deterrence, and they recognized the importance of persuasion and cooperation as regulatory strategies for attaining regulatory compliance. The use of threat and legal coercion, particularly when perceived as unjustified, has been shown to result in negative behavior; these actions are more likely to result in further noncompliance (Murphy and Harris 2007). (Fehr and Rokenbach 2003) According to this theory, individuals are aware of the benefits and risks associated with obeying or violating the law; therefore, for the government to improve compliance among taxpayers, it should formulate policies that will regulate the payment of taxes.

The second theory that was used in the study is social influence theory by kelman (1958) which states that the social environment influences individual behavior, attitude and compliance towards the tax system. Contrary to economic deterrence theory that suggests reinforcement of law, social influence theory assumes that tax payers can be tax compliant without the government's reinforcement. When individuals and social groups perceive that tax authorities are compassionate and they work for the common good of the citizens, then they are more likely to be Tax compliant (Kirchler, Hoelzl & Wahl, 2008). Therefore when a service and client" atmosphere is created between the government and the taxpayers, it will consequently increase taxpayers trust in the government and willingness to pay taxes (Batrancea1 et al., 2012). Furthermore, it is reasonable to assume that social interaction affects the behavior of taxpayers either positively or negatively. The opinion leaders and individual reference groups such as close friends, immediate neighbors, and relatives affect taxpayers' tax behavior and attitudes (Ali, Merima, Fjeldstad Odd-Hedge, 2013). This means that if a friend or relative of a particular individual always complies to pay taxes, the individual will be influenced to pay taxes. Still, if his/her social group fails to comply with paying taxes for one reason or another, then the individual will also be influenced not to comply with paying taxes. The social influence theory postulates that psychological factors influence taxpayer level of compliance. The theory focuses on the ethical behavior of taxpayers and suggests that a taxpayer may comply even if the probability of government detection is low (Atawodi & Ojeka, 2012).

The third theory that was used in the study is Adams Smith Canons of Taxation theory (1776). According this theory a good tax system is one that is developed on the basis of a set of principles that are suitable for the situation. The tax system should strike a balance between the interests of the tax payer and the interests of the tax authorities. Four concepts known as taxation canons served as the foundation for his argument. Equity, certainty, convenience, and economy are the four canons of law that guide taxpayer decisions. In his argument of economy he postulates that for effective tax system the cost of collection should be less than the revenue collected. In order to have more money in its treasury, the government must constantly work to reduce the costs associated with collecting taxes. In view of this taxation canon, selecting the collecting method is crucial. Technological advancement has simplified the process of paying taxes. The costs that the government would incur in the event of an absence have lessened. Without technological advancement in a tax system, we cannot even begin to imagine the substantial costs the government has incurred in tax collection.

EMPIRICAL LITERATURE REVIEW

Tax compliance is described as the extent to which the tax payers observe the established tax rules by fulfilling obligations such as income declaration, filing of returns and paying of tax (Mathenge, 2021). The I Tax system, commonly known as e-pay, is one of the most major technological tax reforms undertaken by the KRA via the use of a Common Cash Receipting System (CCRS) it's a web-based system that enable taxpayers to submit returns and, more crucially, make payments online for customers whose banks participate in the scheme (Kipkemoi, 2015). I Tax is a real-time online platform that enables users to register, submit tax returns, make payments, and enquire about their account status. Commercial banks are connected into the system, and the connection between the two parties is controlled by a service level agreement (Gichuki, 2015).

Munyoro (2017) assessed the effect of recent changes from integrated tax system to I tax system, the changes were aimed to encourage the use of internet to file tax returns. The study used descriptive research design. A substantial influence on the tax compliance of the SMEs was found to be associated with the I Tax system, notably the registration of VAT by use of I Tax, filing of VAT returns online and monitoring of VAT tax defaulters as identified by the research. The increased tax compliance was associated with reduced cost, simplicity and time required to file returns for registered SMEs which encouraged them to be tax compliant. According to the study, I Tax system had made it easy and convenient for taxpayers to file their periodic tax returns anywhere any time besides enabling SMEs taxpayers to handle their tax affairs themselves which influenced increased compliance. Ondieki (2017) investigated the impact of Kenya's I-tax system on revenue collection. A comparative approach was used in the study, which was separated into two time periods: before and after the introduction of I Tax. Secondary data was employed in this study, and a descriptive survey research technique was used to gather the information. It was observed that there was a relationship between the usage of I tax and revenue collection and that Revenue collection nearly doubled after the I-tax system was implemented.

Barako (2015) conducted an evaluation of the effectiveness of the I Tax system in Kenya's tax administration. The research was mostly descriptive in nature. According to the findings of the research, the installation of I Tax resulted to an increase in the revenue return. In order to eliminate inefficiencies within the tax administration, tax processes were simplified, standardized, and harmonized, I Tax was credited with this achievement. According to the research, I Tax resulted in easier and more efficient procedures for paying and collecting taxes and reduced the potential for corruption. This resulted into improved efficiency in tax administration.

Livoi (2017) was interested in determining the impact of KRA's tax reforms on corporate tax compliance. The influence of technology tax changes, policy tax reforms, and administrative tax reforms on company compliance were investigated in the study. A descriptive survey research approach was used in the study, Kenya Revenue Authority's domestic tax department was sampled for the research, which included a census of its staff and the results were reported. In order to examine the data, descriptive and inferential statistics were utilized. A negative association between technology tax changes and corporate tax compliance was discovered in the research. In addition, Findings of the regression analysis revealed that technological tax changes had a negative influence on the level of corporate tax compliance.

The review showed the existence of mixed findings. The study by Livoi (2017) for instance, found that while technological reforms in particular I Tax was a key factor in enhancing corporate tax compliance, its effectiveness was weak to influence corporate tax compliance and that of Munyoro (2017) who found that technological reforms in particular I Tax system had a positive and significant effect on the tax compliance of the small and medium term enterprises which was associated with the reduced cost, simplicity and time required to file returns for registered small and medium term enterprises hence encouraging them to be tax compliant.

RESEARCH METHODOLOGY

The study adopted descriptive survey design to obtain a sizeable and considerable amount of data from the study population. The study target population was 1527 SMEs in Bungoma County. Yamane formula (1967) was used to determine the sample size and then randomly selected. According to Yamane (1967), for a 95% confidence level and p=0.05, the size of the sample for the study is:

$$n = \frac{N}{1+Ne^2} = \frac{1527}{1+1527\times0.05^2} = 317$$

As a result, 317 small and medium enterprises were included in the research.

Table I: Target population

Type of business	**Target population**	**Sample size**
Trade/Commercial activities	847	176
Manufacturing activities	500	104
Service Activities	180	37
Total	**1527**	**317**

Source: Research Data (2022)

The study relied on primary data that was collected using closed ended questionnaires. The questionnaires were self-administered to managers/owners of small and medium enterprises in Bungoma County. The quantitative data from the field was analyzed by both descriptive and inferential statistics. The regression model adopted was:

$Y = \beta_0 + \beta_1 X_1 + \varepsilon$

Y =is the dependent variable (Tax compliance among SMEs)

x_1 = Technological Tax Reforms

β_1 =Beta co-efficient

β_0= Constant term

ε = Error term

FINDINGS AND DISCUSSION

Descriptive statistics of Technological Tax Reforms

Descriptive statistics such as mean and standard deviation were jointly used to summarize the responses as presented in the table II. The analysis of the findings showed that most of the respondents agreed that Electronic Tax Invoice (ETR) machine has simplified tax payment procedures as shown by the mean of 4.06. However most of them agreed that the use of KRA M services has made it easy for them to make tax remittance accurately, conveniently and on time (M = 3.98), The technological tax reforms have improved enterprise tax compliance (M = 3.96), I tax has helped their enterprise save money and time related cost by allowing them to file tax online (M = 3.95), Remitting out taxes through mobile payment has affected transparency of my enterprise transaction (M = 3.91) and that since the implementation of I tax, this enterprise has had very little direct contact with tax authorities (M = 3.76). The analysis of the finding shows that responses to the 6 statements used to measure the effect of technological tax reforms on tax compliance ranged between the mean of 3.76 to 4.06 with overall mean being 3.93. This shows that majority of the respondents were in agreement with the statement that were used to measure effect of technological tax reforms on tax compliance among SMEs in Bungoma county.

Table II: Descriptive statistics of Technological Tax Reforms

Technological Reforms	Mean	Std. Deviation
I tax has helped this enterprise save money and time related cost by allowing it to file tax online.	3.95	.843
Since the implementation of I tax, this enterprise has had very little direct contact with tax authorities.	3.76	.892
Use of KRA M-services has made it easy for us to make tax remittance accurately, conveniently and on time	3.98	.928
Remitting out taxes through mobile payment has affected transparency of our transaction	3.91	1.071
ETR machine has simplified tax payment procedures	4.06	.867
Technological tax reforms has improved enterprise tax compliance	3.96	.783
Average Mean	**3.93**	

Source: Research Data (2022)

Effect of Technological Tax Reforms on Tax Compliance (correlation Analysis)

Correlation analysis was carried out to determine association between technological tax reforms and tax compliance among small and medium term enterprises in Bungoma. Pearson product moment correlation coefficient (r) was used to aid in establishing correlation between the study variables of interest. Correlation coefficient shows the magnitude and direction of the relationship between the study variables. The findings as presented by the table III shows that there is significant positive relationship between technological tax reforms and tax compliance among medium enterprises in Bungoma as supported by($r=0.554$,$p < 0.05$), this implies that increase in technological tax reforms leads to a positive increase in tax compliance.

Table III: Correlations analysis

		Compliance	Technological tax reforms
Compliance	Pearson Correlation	1	.554**
	Sig. (2-tailed)		.000
Technological tax reforms	Pearson Correlation	.554**	1
	Sig. (2-tailed)	.000	

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

Source: Research Data (2022)

Effect of Technological Tax Reforms on Tax Compliance (Regression Analysis)

The Table IV below shows the results of regression analysis on the effect of technological tax reforms on tax compliance among SMEs in Bungoma County, Kenya.

Table IV: Regression Results

Model Summary					
R	**R Square**	**Adjusted R Square**	**Std Error**		
.849a	0.721	0.718	0.19738		
		ANOVA			
	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Regression	28.159	1	28.159	727.9162	.000
Residual	10.909	282	0.039		
Total	39.068	283			
Model Coefficients					
	Unstandardized Coefficients		**Standardized Coefficients**		
	B	**Std. Error**	**Beta**	**t**	**Sig.**
(Constant)	1.106	0.135		8.200	0.000
Technological tax reforms	0.780	0.036	0.089	2.260	0.000
Dependent Variable: tax Compliance Predictor Variables: Constant, Technological Tax Reforms					

Source: Research Data (2022)

The result on model summary shows an R-square value of 0.721 which implies that technological tax reforms account for 72.1% of the variation in tax compliance among SMEs in Bungoma County. The Analysis of Variance results showed that the regression model was a good fit (P Value < 0.05). This implies that the model was statistically significant in forecasting the influence of technological tax reforms on tax compliance among SMEs in Bungoma County, Kenya. This means that there is a satisfactory goodness of fit between technological tax reforms and tax compliance. The regression model is developed as*:* $y = 1.106 + 0.780x + 0.036$

The model regression coefficients indicated that technological tax reforms have a positive and significant effect on tax compliance among SMEs in Bungoma County, Kenya (β= .0.780, P < .05). This implies that a unit increase in technological tax reforms will result to a significant improvement in tax compliance among SMEs in Bungoma County, Kenya by up to 0.780 units. The findings shows that technological tax reforms have increased tax compliance among SMEs in Bungoma County because of ,SME owners are able to file returns, declare their actual income and know their tax liability, they are also able to pay tax through mobile services and thus time and movement related cost is reduced. The findings agree with that of Livoi (2017) who concluded that technological reforms have revolutionized corporate tax compliance. Similarly, Abdul (2021) concluded that technological tax reforms play a key role in determining the level of SMEs' tax compliance. Due to I-tax, the tax payers are able to file their returns fast and on time without any human interaction. In addition, the tax payer is able to view the ledgers and interrogate their tax issues.

CONCLUSION

Based on the findings of the study, it was concluded that technological tax reforms which were implemented for the period 2011 to 2021, both individually and in combination, significantly influenced tax compliance among SMEs in Bungoma County. Because of technological tax reforms, SME owners are able to file returns, declare their actual income and know their tax liability through online services, they are also able to pay tax through mobile services and thus time and movement related cost is reduced.

RECOMMENDATION

The study recommends that Kenya revenue authority should provide education to SMEs on how to use technology to meet their tax obligation and employing simpler payment methods such as Mobile money services and other mobile banking advancements. Furthermore the study recommends that the government should improve the internet connectivity to improve tax compliance among SMEs in Bungoma County.

CONTRIBUTION TO KNOWLEDGE

This study provides a theoretical backing of the Economic Deterrence theory, which documents that given the fact that individuals are aware of the benefits and risks associated with obeying or violating the law, there is a need for the government to formulate simpler policies for ease of obeying and such policies is technological tax reforms. The study also provides a theoretical backing of Adams Smith's Canons of Taxation Theory, which emphasizes the need for the government to reduce the tax collection costs to a minimum and one of the ways is through technological reforms. Empirically, the study has provided empirical evidence that indeed technological reforms can significantly improve tax compliance among SMEs based in an urban Kenyan setting for instance Bungoma County. This can therefore open an avenue for future studies to explore further research in the area.

AUTHOR CONTRIBUTIONS

Under the supervision of both Dr. Tecla Kirwa and Dr. Fred Atandi, university lecturers in the school of Business at Kibabii University, Kenya, Kevin Namaswa Kabisa, wrote the concept paper, edited and proceeded to write the whole paper. Under their guidance, he collected and analyzed data as reflected in the work. Therefore, any grammatical issues are solely his.

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CONFLICT OF INTEREST DECLARATION

Kevin Namaswa Kabisa declares that there are no conflicts of interest regarding the publication of this Manuscript. In addition, the ethical issues; including plagiarism, informed consent, misconduct, data fabrication and (or) falsification, double publication and (or) submission, redundancy has been completely observed by the authors.

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