

**SME TAXPAYERS PERCEPTIONS ON TAX COMPLIANCE IN
TANGA CITY AND MUHEZA DISTRICT, TANZANIA**

By

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**A Dissertation submitted in Partial Fulfillment of the Requirements for the Degree
of Master of Science in Economic Policy and Planning of Mzumbe University**

2017

CERTIFICATION

The undersigned certify that I have read and hereby recommend for acceptance by the Mzumbe University a dissertation entitled SME tax payers perceptions toward tax compliance in Tanzania evidence from Tanga City and Muheza District in partial fulfillment of requirements for award of the degree of Masters of Economic policy and planning (MSc-EPP).

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Lastly, I remain responsible for any mistakes which may be detected in this work. None of the mentioned above should be responsible for any fault found in this work.

DEDICATION

I dedicate this dissertation to the lovely 32 students and 3 teachers who lost their lives in Arusha May 2017 by car accident.

LIST OF ABBREVIATIONS AND ACRONYMS

EFD	Electronic Fiscal Device
SME	Small and Medium Enterprise
SPSS	Statistical Package for Social Software
TPA	Tanzania Port Authority
TRA	Tanzania Revenue Authority
URT	United Republic of Tanzania
IFC	International financial cooperation

ABSTRACT

The present study assesses the perceptions of small and medium enterprises on factors affecting tax compliance in Tanzania. Where the research problem was based on low tax compliance as a result of increase in tax evasion. The study employed cross-sectional research design with sample size of 160 respondents (Tax payers). A purposive non probability sampling and random probability sampling technique were used to choose respondents from the study area. Semi-structure questionnaire was used to capture intended information. Data collected were analyzed by descriptive statistics, logit Model and chi2-test. The findings on analysis of demographic characteristic of the SME Tax payers revealed that majority of respondents about 48.13 percent were between 40 and 51 years. The majority which was 55.6 percent of respondents had primary education. Meanwhile 51.2 percent of respondents were married. Moreover, the results revealed that 73.13 percent of respondents had business income between 500001 and 4500000 Tsh per month while 45.6 percent of respondents had 4-49 employees in their business. However majority of respondents agreed that the tax collected assists the government in provision of services.

On the other hand the result shows that there is association between tax payer's perception on tax rate, fines, government services delivery, and penalty towards tax compliance. Furthermore the result from logistic regression model indicated that if tax rate is perceived high by SMEs tax payers, tax compliance would decrease by 25.50%. Moreover, perception of SMEs tax payers on penalty was high; penalty would be expected to increase tax compliance by 46.99%. If the perception of SMEs tax payers on fine was high, fines would be expected to increase the tax compliance by 29.58%. If perception of SMEs tax payers on government service delivery was high the tax compliance would be expected to increase by 61.93%. The study recommends that, the government should inject tax education to the education curriculum from the primary level in order to increase tax awareness to the community and remove wrong perception prevailing in the society.

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CHAPTER ONE

INTRODUCTION

1.1 Background of the Problem

Most developed countries are having a broad base of both direct and indirect taxes where by the tax liability is covered by firms and household. More than 30% of developing countries is characterized by social political and different administrative difficulties in operating their public financial system (OECD 2010). As a result developing countries are particularly pronounced by vulnerable tax evasion and tax avoidance (Non compliance behavior) of both individual tax payers and corporations Brautigam et al (2008). This creates a difference in mobilizing the fiscal resources between developed and developing countries. While tax revenues in OECD-countries amount to almost 36 per cent of gross national income in 2007, in Africa it is 23% and Latin America is even lower at 17.5% (in 2004),(OECD 2010).

In developing countries high amount of tax revenue is collected from indirect taxes such as value-added taxes (VAT). Fjeldstad *et al.* (2009) observed that, the indirect taxes amounting for up to two-thirds of total tax revenues due to low level of tax compliance. Apart from these structural differences in the tax systems between developing and developed countries, it is important to recognize that tax losses that arise in the course of tax evasion and avoidance activities, do largely contribute to the poor performance of state revenue mobilization in developing countries (Friedman *et al.* 2000).

In ensuring the attainment of social and economic goals, a presence of effective and efficient mechanism of taxation in a country is of paramount importance. In the end adequate revenue has to be collected Brautigam *et al.* (2008). The roles of ensuring revenues are adequately collected in accordance with the laws and regulations in existence remains to be the function of the country's revenue authority, Tanzania Revenue Authority (TRA) in the case of Tanzania. Tax payers are not always willing to

comply with the tax laws and hence enforcement strategies are required. Tax compliance has been differently defined. Internal revenue sources (IRS 2009) defined tax compliance as the ability and willingness of taxpayers to comply with tax laws, declare the correct income in each year and pay the right amount of taxes on time. Andreoni, *et al* (1998), defined tax compliance as the taxpayers' willingness to obey tax laws in order to attain economic development. Taxes are paid by large, medium and small registered enterprises (SMEs). SMEs are differently defined and the definition may differ between countries.

In the European Union (EU) SMEs are classified according to the number of employees and enterprise turnover, Micro enterprises are classified to have more than 10 employees with a turnover of more than 2,000,000 euro; small enterprises are classified to have more than 50 employees with a turnover of more than 10,000,000 euro; while medium enterprises are classified to have more than 250 employees with a turnover of more than 50,000,000 euro (IFC 2009). Tanzania Government has adopted a national definition of SMEs through the Small and Medium Policy that was rolled out in 2003. Similarly to the EU classification, the definition in Tanzania combines employment size and size of capital investment. As shown in Table 1.1, small enterprises are defined as those employing between 5 to 49 employees but also have a capital investment in machinery of between Tsh. 5 million and Tsh. 200 million. Medium enterprises are those employing between 50 and 99 workers and have a capital investment in machinery of over Tsh. 200 million but less than Tsh. 800 million.

Table 1.1: Category, Employees and Capital Investment in Machinery

Category	Employees	Capital Investment in machinery
Micro enterprises	1-4	Up to Tsh 5 million (USD 5,000)
Small Enterprises	5-49	Above Tsh 5 million to Tsh 200 million (USD 5,001 - 200,000)
Medium Enterprises	50 – 99	Above Tsh 200 million to Tsh 800 million (USD 200,001 to Tsh 800,000)
Large Enterprises	100+	Above Tsh 800 million (Above USD 800,000)

Source: URT (2003) SME Policy

In the event an enterprise falls under more than one category the level of investment will be the deciding factor.

According to United Republic of Tanzania, Income Tax Act no 11 of 2004, business firms with annual turnover above 40 million TZS are registered for VAT purpose while those with annual turnover of below 40 Million are also subjected to taxation (presumptive approach of taxation) system. As a result of law SMEs in Tanzania are supposed to declare their sales for income tax purposes, where each one should declare the rent cost for rental tax to be estimated; furthermore property should also be stated for him to pay property tax. Hence most of tax paid by SMEs depends on the compliances level. However, the performance of any tax system depends highly on its administration mechanism in place. The implication is that; no tax is better but administration of tax is more important than tax itself (Lewis 1982). The essential objective of any tax authority is maximizing compliances among the tax payers of all types with their obligations (Helhel and Ahmed 2014).

In many developing countries including Tanzania, tax administration is weak, corruptive and characterized by far-reaching evasion and coercion. In many cases however, most of these (developing) countries compliance levels are low and large proportion of informal sector of the economy escape the tax net entirely (Brautigam *et al.* (2008). James (2015) observed that; tax compliance is one of the major problem facing different revenue authorities. It is not a simple task in persuading tax payers to comply with the requirements sometimes, because the tax payers fail to understand the established laws and regulations. On the other side, tax payers are naturally disposed to reduce their tax liability whether legally or illegal; which cause incorrect filing of their tax returns hence loss to the government. Also, the complex regulatory system and tax regime makes tax compliance burdensome and often have negative effect to the development of tax payers including SMEs (Msato 2009). In supporting this argument, Nicoleta (2011), observed that; if the tax systems are characterized by low efficiency, high collection charges and time wastage for tax payers will result to the revenue losses.

SMEs owners operate their business in an over bearing regulatory environment with multiple taxes, cumbersome importation procedurals and high port charges that constantly increase the cost in their operations (Lumumba *at el*, 2010). SMEs tax payers are highly affected by those cost when scaled by sales or asset and likely, compliance cost affects them highly as compared to the larger business operators (Slemrod, 2007)

In Tanzania, SMEs have been observed by Kamote and Ngowi (2015) with the highest degree of non-reporting of their sales to the tax authority, especially when the transaction is conducted by cash. The experience in some of the countries in the East Africa Community; such as Kenya and Uganda manage the non-declaration of sales by increasing the monitoring of sales transactions through Electronic Fiscal Devices (EFDs machines). In Tanzania, the case sound the same, however, SMEs practice towards the use of EFD machines has not been so effective; as was reported that, out of 100 surveyed SMEs' businesses premises only one was observed to provide EFDs receipt free of demand by the customer (Kamote and Ngowi 2015). However, a serious tax evasion among business community in the country has been observed by the fifth government regime particularly on issuing of containers by the Tanzania Port Authority (TPA) without tax paid, (Makame 2015). This is a typical indication of non-compliance of tax payers in the country supported by the poor management and corruptive port administration.

However, Tanga region is none exceptional to none tax compliance due to the fact that, SMEs have been reluctant in paying their tax as per the set Tax laws and regulations. According to TRA Tanga regional tax collection report of 2016, reveals that, in a consecutive period of three years (2013 to 2015), the tax due was recorded to be 2% of tax revenue to be collected each year as the result of SMEs failure to comply with the tax laws and regulations. It is interesting to understand the perceptions of SMEs on tax compliance in order to incorporate their concerns in strategies aimed at enhancing compliance.

1.2 Problem Statement and Justification

Increasing of domestic revenue is the priority of sub-Saharan African countries (Drummond *et al.* 2012). The government is creating fiscal space and provides necessary public services by mobilizing the government revenue. However, the domestic tax bases in most African countries are undermined by widespread tax avoidance and evasion (IMF 2011). Chand and Moene (1999) argued that Tax compliance in sub-Saharan countries is affected by perceptions of tax payers and hence non compliance behaviors are more pronounced. While non-tax compliance behavior is conducted by small and medium enterprise in Tanzania, it is still ongoing and growing global problem (McKerchar and Evans 2009).

While small and medium enterprise (SMEs) contribute significantly to country gross domestic product (GDP) as well as the government revenue, evasion in tax payment has been part and parcel of their business attitude or behavior and still persists (Kamote and Ngowi 2015). The recently revealed cases of different companies which include small, medium and large enterprises reported to collect their containers from Tanzania Port Authority without paying the required tax to the TRA, is one of the indications of existence of non tax compliance (Makame 2015). However, tax evasion done by small and medium enterprises is done secretly and hence it is difficult to capture the magnitude and why it is done, Franzoni (1999). Jorgen and Lars (2004) conducted a study titled “Tax evasion in Kenya and Tanzania” which revealed that, during 2004 1% increase in tax rate led to 3.8% increase in tax evasion.

On the other hand the TRA commissioner, Alphayo (2017), reported that the government had lost Tsh 29 billion in 2016 due to fake electronic fiscal devices constructed by a certain business man and issued to the differed companies. The use of fake electronic devices is also an indication of the presence non -compliance behavior (Ng’eni, 2016). The tax evasion by large enterprises is likely to encourage small and medium enterprises to also engage in the same practices (Maseko 2014). It is also known

that, in practice the proposed use of Electronic Fiscal Devices met strong resistance by the business community.

Kamote and Ngowi (2015) have noted that tax evasion remained a long time unsolved challenges, despite voices by the concerned parties in the public sphere. It is in this direction; new strength on customs administration is sought to be reinforced so that, to bring revenue to the government for the smooth implementation of development project. Moreover, there has been various attempts of the government to introduce EFD machines to the business community, and the reported achievement in revenue collection of an average of 1.3 trillion monthly by TRA officials, nevertheless still there some resistance over the use of EFD machines particularly on the question of subsequently producing/production of the EFD receipts to customers, (Alphayo 2017).

Furthermore, it is the reality that, tax evasion is the result of malfunction of political, social and economic factors that have the tendency of influencing the tax administration mechanism in place. In view of that, other scholars such as Ojochogwu and Stephen (2012) and Nyamweza *et al* (2014) argued that higher tax rates and complex filling procedures are the most important factors, which encourage non-compliance of SMEs. Similarly, factors like multiple taxation and lack of proper enlightenment affect tax compliance among the SMEs tax payers.

The available literature is limited in explaining what the empirical situation is in context of Tanzania. Therefore, conducting of this particular study will add value to the available literature. Different studies has been conducted on the reasons for non-tax compliance amongst small business tax payers' themselves but there is no specific study conducted on SMEs tax payers perceptions on tax compliance in Tanga Region. Therefore, this study will help to determine the perception of SMEs taxpayers on factors affecting tax compliance.

1.3 Objective of the study

1.3.1 General Objective

The main objective of this study was to assess the perceptions of small and medium enterprises on factors affecting tax compliance.

1.3.2 Specific Objectives

- i. To identify the demographic characteristics of the SME Tax payers in the study area.
- ii. To assess the perceptions of SMEs tax payers on business tax regulations (with the focus on tax rate, fines and penalties), tax revenue utilization, and effectiveness of tax education on tax compliance.
- iii. To examine how the perceptions of tax payers on business tax regulations, Government service delivery and effectiveness of tax education influence tax compliance.

1.4 Research Questions

- i. What are the demographic characteristics of SME Tax payers in the study area?
- ii. What are the perceptions of SMEs tax payers on business tax regulations (tax rate, fines and penalties), government service deliveries, and tax education influence on tax compliance level?
- iii. How the perceptions of SMEs tax payers on business tax regulations, government service deliveries, and tax education influence tax compliances?

1.5 Scope of the Study

The study was conducted in Tanga City and Muheza District in Tanga Region where by the former represented urban businesses and the latter represented rural businesses. The outcome of the study will assist Tanzania revenue authority in creating environment in which the taxpayer will voluntary comply and willingly pay their tax liability accordingly.

1.6 Significance of the Study

The study has been used to generate knowledge of widening tax base to policy makers, administrators, collectors; and will enhance the revenue collectors to formulate policies that will assist to reduce some of loopholes that tax payers' use in order to reduce their tax liability. It entails to explore the perception of SMEs on factors that affect tax compliance and solution for the low tax compliance in the country. Thereby an increase of tax compliance will enhance revenue collection in the country. The research findings will provide the Tanzania Revenue Authority officials with the necessary knowledge, abilities and skills to reduce tax evasion and avoidance by instituting the necessary education and enforcement on the available tax by – laws in order to enhance the government revenues.

1.7 Organisation of the Study

The study was divided into six (6) Chapters where by chapter one deals with the background of the problem, statement of the problem, objective of the study, research questions, significant of the study, scope, limitation and organisation of the study. Chapter two deals with theoretical review, empirical literature review, conceptual frame work and research hypothesis. Chapter three deals with the type of the study, study area, study population, unit of analysis, variables and their measurement, sample size, type and sources of data, data collection technique, and data analysis method. Chapter four includes presentation of findings from descriptive, correlation matrices, and regression analysis. Chapter five includes discussion of findings which includes correlation analysis and regression analysis while chapter six includes conclusion, recommendations' and area for further studies.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

In this chapter the theoretical frame work will be given in the first part where the second part presents the empirical review and finally the conceptual frame work will be developed.

2.2 Definition of key terms

Before presenting the theoretical framework, a number of definitions adopted in this study are presented.

2.2.1 Tax

Are the compulsory contribution/ payment made to the government revenue imposed by the government on its workers income and business profit or added to the goods and services (GIZ 2010). Tax evasion and tax avoidance may imply non-tax compliances.

2.2.2 Tax evasion

Tax evasion is the purposeful action done by the business owners to reduce the tax liability by breaking the law; where this is illegal, since this is involving the breaking of tax law by making misrepresentation of data. Tax evasion is one of the non-tax compliance; which means failure to pay the amount of tax which is legally due, while this is a criminal offence and if discovered will lead to criminal cases against the tax payer. Allingham and Sandmo (1972 defined tax evasion as the deliberate action of breaking the tax law by the tax payer to hide information or fraudulent of full taxable income so as to minimize the tax liability.

2.2.3 Tax avoidance

Tax avoidance has been defined by different scholar including (Soyode and Kajola 2006) as the plan of taxpayer to use the weakness or loophole of the tax law in order to

minimize the tax liability. This is legally allowed though it is also implicating non- tax compliance. However the taxation theory suggests that in order to increase tax compliance the tax policy should observe the following principles, (OECD 2010).

2.2.4 Neutrality

The tax system should seek to be neutral and equitable between the different forms of business activities this suggest that the rising of tax revenue should minimize discrimination among the tax payer in order to apply to all tax system employed and hence this will rise tax compliance.

2.2.5 Efficiency

This tax compliance cost should be minimized to both business and tax authority as much as possible in order to increase tax compliance and this as a result will discourage the shadow economy and increase the tax revenue due to voluntary tax compliance.

2.2.6 Certainty

A good tax should be certain and simple for clear and easier understanding to both individual and business tax payer, in order to understand their obligation and entitlement; this will also increase tax revenue and willingness to comply with the tax laws and regulation.

2.2.7 Effectiveness and fairness

Taxation should result to the right amount of money at the same and should avoid the double tax and an intentional non-taxation which may be potential for evasion and avoidance to be reduced. Therefore tax compliance increased and hence the government revenue rise up.

2.2.8 Flexibility

The tax system should be flexible and dynamic in nature in order to allow any adjustment caused by technological changes and commercial development. This is because the government revenue may be insufficient to facilitate the government expenditure and in order to raise the revenue to facilitate deficit will require adjusting

the tax. Therefore being flexible will enhance the government to raise the revenue to facilitate the deficit.

2.2.9 Equity

This is an important consideration within the tax policy framework which includes both horizontal equity and vertical equity. Horizontal equity means the tax payer with the same level of income should fall under the same categories in tax payment. That means they bear the same tax burden. While vertical equity means the tax payer should pay according to the income level. This is encouraging the progressive system of tax system where the higher the income the higher the amount of tax to be paid. The presence of equity among the tax payer will increase the tax compliance.

2.3 Theoretical Framework

In this section different theories related to this study are discussed. They include Deterrence Theory by Allingham and Sandmo (1972), Social Psychological Theory by Snavelly (1990) and fiscal exchange theory the idea borrowed by Cowell and Gordon (1988) Tilly (1992). Finally these theories were used to select the variables under the study. They were used in formulating conceptual frame work of the study. The use of these theories is due to fact that each theory is formulated basing on the specific variables while perception is affected by various variable hence using only one theory other factors affecting tax payers perceptions will not be examined.

2.3.1 Deterrent Theory

This theory was first developed by Allingham and Sandmo (1972) assumes that the tax compliance behavior is influenced by economic factors. The tax payer measures the cost and benefit for tax evasion. The tax rate and penalties for fraud and probability of detection are the main determinant of cost and benefit of tax evasion. This theory views an individual tax payer as rational economic agent who asses the cost and benefit of evading tax and thus chooses not to pay if the benefit of non-compliance outweighs the cost (Walsh, 2012). This theory implies that when there are low audit probabilities and

low penalties the tax evasion tend to increase while if there are higher probabilities of detection and penalties very few people will evade taxes (Torgler 2003). The base of this assumption is that stricter audit and very heavy penalties for offenders is a base for reducing non-compliances.

The theory has been criticized in that it is not realistic in explaining the tax payer compliance as it predicts that the general substantial non-compliances beyond what is really observable (Slemrod, 2007). Despite the use of audit and penalties, tax evasion and avoidance is still common in developing countries; and significantly affect their economy through low domestic revenue collected due to non-tax compliances. In reality there are people who never attempt to evade tax even if the probability of detection is zero (Sour, 2004). Therefore a number of authors have argued that the actual question regarding tax compliance should be why people pay taxes and why not evade them (Slemrod, 2007). Furthermore the theory failed to consider behavioral factors such as attitude, perception, and moral judgments (Lewis, 1982). Other important determinant of tax compliance ignored by the theory includes code of conducts such as moral and ethical constraints that have potential to prevent people from cheating in their taxes (Sour, 2004). This study had examined the perceptions of SMEs on economic factors such as tax rate, fines and penalties as they are highly influence tax payment. The theory explains that the tax rate and penalties for fraud and probability of detection are the main determinant of cost and benefit of tax evasion.

2.3.2 Fiscal Exchange Theory

The fiscal exchange theory is well rooted in economics and political sciences like Cowell and Gordon (1988). Tilly (1992), they noted that compliances increases with the availability of social services borrowing both idea of economic deterrence and psychological theory. The theory suggests the existence of a social relationship or psychological contract between the government and the tax payer. Fjeldstad *et al* (2012). It suggest that the presence of government expenditures may serve as the motivating factor for taxpayer compliance especially when the government offers the quality and

well improved goods and services that the society expect to get (Alm,1999). Therefore the society may consider the services they get from the government as exchanging their purchasing power in the market return for government services. This means that the exchange being largely conditional and varying as the government changes its services. Therefore the taxpayers are likely to be willing to comply when they are satisfied with government services even in the absence of detection and punishment (Torgler, 2003). Generally as the theory explained the study examined the perceptions of SMEs taxpayer on government service delivery and their influence on tax payment; although the theory suggested that individual is highly influenced to pay when their satisfied with the government service provided.

2.3.3 Social Psychological Theory

This theory was first used by Snaveley (1990) who argued that it is reasonable to assume that human behavior in the area of taxation is influenced by social interactions much in the same way as other forms of behavior. Furthermore, the theory is based on social perspective of individual from their behavioral intentional. This is based on two basic determinants that include personal factor and social influences on whether to comply with tax laws or not to comply (McKerchar and Evans 2009). Personal and social norms are the basis in studies explaining the taxpayer behavior and they play very big role in determining the tax compliances (Franzon, 1999, OECD, 2010). Moreover, Ronan, (2007) specifically noted that such variables like stigma, reputation, and social norms have great effect on tax payers. Personal norms have been defined as the deeply rooted convictions about what one ought or ought not to do (OECD, 2010). They are in most cases difficult to change and often beyond the reach of public policy (Franzoni, 1999). In perspective of taxpayer behavior personal norms reflect the tax payer values, ethics and morale, where by all these have influences on tax compliances attitude. (Sour 2004) argues that engagement in act of evasion may induce feeling of anxiety, guilt or negative self image in tax payer. The fear of experiencing feeling of guilt, along with the risk of social stigmatization has greater effect than such external factors as the risk of

detection and penalty. Therefore an individual is most likely to comply with tax requirements if he believes that the member of his reference groups also comply, just as he is also likely not to comply if he believes that members of his referent group do not comply, Lewis (1982). The study had investigated the small and business enterprises owner's perceptions on factors affecting tax compliance including influence on tax education, government service delivery, tax education, and tax regulation which are also affected by social psychological factors as explained by the theory.

2.3.4. Concept of Perception

The conceptual model in this paper is informed by the perception concept. Cherry (2014) elaborated the concept of perception as ones experience of the world around them and involves both the recognition of environmental stimuli and actions in response to these stimuli. Through this process, people gain information about properties and elements of the environment that are critical to their survival. Perception not only creates ones experience of the world around them; it allows people to act within their environment. Bem (1972) defined the concept of self-perception, referring to this as individual own attitudes and other internal states partially inferred from their own overt behavior. The attitudes and behavior can be influenced by rules, regulations and other institutional arrangement and these may be subject to different interpretations.

Basing on institutional theory which describes how institutional arrangements which are essentially the rules, influence human behavior on how to act (North 1990 cited by Ng'eni, 2016). The Institutional arrangements include both formal and informal rules. Adler (2014) argues that mismatched perception can interfere with communication and hence tools are needed to help harmonize perception between different stakeholders to provide understanding. Therefore the study as introduced by concept of perception the mismatch of perception of SMEs on tax issues and tax regulation may result to the different in compliance level. The attitudes and behavior can be influenced by rules, regulations and other institutional arrangement and these may be subject to different

interpretations. Others may consider as government is unfair in tax regulation, services provision while others may consider it fairly treated.

2.3.7 Synthesis of the Theoretical Review

The deterrence theory of tax compliance assumes that compliance is influenced by economic factors like tax rates, penalties for fraud and detection probability. The theory views an individual tax payer as rational economic who asses the cost and benefit of evading tax. The social psychological theory is based on social perspective that individuals from their behavioral intention, their compliance level are influenced by stigma, reputation and social norms. Fiscal exchange theory suggests the existence of the social relationship between the government and the tax payer. The tax payer consider the government services as the compensation of the tax paid and their compliance level is likely to increase as the government services increased. The general objective of my study was to assess the perception of SMEs on the factors that determine tax compliance among small and medium enterprises in Tanga Region. From the different theoretical argument this study was guided by these theories which are social psychological theory fiscal exchange theory and economic deterrence theory. The reasons of using these theories were due to fact that each theory is limited to explain the perception of SMEs tax payers toward tax compliance. Since economic deterrence theory is basing on economic factors while fiscal exchange theory was based on individual comparison of the services delivered and amount of tax they pay and Psychological theory relied on psychological influence on tax payer's perception toward tax compliance.

2.4 Empirical Literature Reviews

This section critically reviews a number of studies on tax compliance conducted across the globe.

Razak and Adafula (2013) conducted a study in Tamale (Ghana) which evaluated taxpayer's attitude and its influence on tax compliance decision. The survey responses from the questionnaires administered to operators of SMEs in Tamale were

quantitatively analyzed. The study employed questionnaire method where 233 respondents were surveyed and the planned behavior theory were applied. Both descriptive and inferential statistics were applied; the results indicated that individuals are highly concerned with the amount of taxes they pay. Furthermore the burden of taxes paid, affects the attitude of individuals and this informs how they evaluate the tax system and consequently their compliance decision. The result shows that individual have little regard for the amount of taxes paid by them in comparison to the amount paid by high income earners.

Ojochogwu and Stephen (2012) conducted a study in North Central Nigeria, on evaluating the factors affecting tax compliance decision amongst small and medium enterprises where the surveyed questionnaires were applied. It was observed that higher tax rates and complex filling procedures are the most important factors that encourage non- compliance of SMEs. Other factors like multiple taxation and lack of proper enlightenment affect tax compliance among the SMEs surveyed. The study recommended that SMEs should be levied lower tax rates to leave enough funds for business development and better chances of survival in a competitive market.

Nyamweza *et al* (2014) conducted a study in Zimbabwe, where the general objective of the study was to find out the factors for tax compliance in Zimbabwe. The research was done on 50 businesses in retail sector in Gweru, the findings were that the minimal efforts employed to enforce tax compliances and most of tax collectors were corruptive, small and medium enterprises reduced their tax liability by paying bribes, keeping two sets of records, relocating to new premises without informing the authority, and penalties had been observed to be most effective in enforcing compliances.

On the other hand, Fjeldstad *et al* (2012) analyzed factors affecting tax compliance attitude in four countries; Tanzania, Kenya, Uganda and South Africa. The objective of this study was to find out the factors affecting tax compliance using data from the new round of Afro barometer survey using a binary logit regression analysis. The study found some of the similarities and differences in four countries. An increase in the

perception of individuals about the difficulty of evading taxes is found to increase the likelihood of tax compliant attitude in Kenya and South Africa. Furthermore the result shows that the individual who are more satisfied with the provision of public services provision are more likely to have high compliance attitude in all four countries where fair treatment and tax knowledge are also found significant in determining tax compliance attitude. In developing countries services are still poor but there high tax evasion despite of social services improved. This study will investigate the effect of improvement of government services and personal influence on tax compliance level.

Helhel and Ahmed, (2014) conducted a study on factors affecting tax attitudes and tax compliance a survey study in Yemen. The objective of the study was to bring an insight about influence of attitudes and consideration of individual tax payers on tax compliances taking internal and external factors. The study was conducted in Sanaa a capital city of Yemen to evaluate and rank the factors that reduces taxpayer compliances. A questionnaire was designed and distributed to tax payers in order to learn their opinions. The result shows that high tax rates and unfair tax system are the two most crucial factors associated with low compliance. The researcher reported that insufficient tax auditing; little deterrent effects of tax penalties and tax amnesties enacted frequently have impact on tax payer's compliance decision. On the other hand the factor like few tax officials, frequent tax code changes affect compliance to a lesser extent. It also found that tax collected is not returned to the public goods and services. When the responses are compared by gender and age, women was found to be more compliant compared to males to taxation whereas age is not a significant factor in general, especially for external factors. In addition the older group was found to be more compliant compared to younger group in terms of factors having significant difference.

Nzioki (2014) conducted a study on “analysis of factors affecting tax compliance in real estate sector a case of real estate owners in Nakuru town, Kenya” the study specifically sought 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 real estate sector. This study was guided by theory of planned behavior. The explanatory study design employed a sample size of 271 which was drawn from the targeted population of 841 real estate investors. The method of data collection employed was structured questionnaire. The finding shows that compliance cost had negative effect on level of tax compliance and both tax knowledge, fines / penalties and education had positive effect on level of tax compliance among real estate investors. Conversely, high compliances cost and high opportunity for tax evasion will reduces tax compliance among real estate investors. Thus, tax compliance cost should be in a way that does not encourage taxpayers to evade tax. There should be stiff enforcement of fines and penalties to deter tax evasion. Additionally, tax authorities should simplify processes involved in filling of returns and payment of taxes.

Maseko (2014) examined the determinant of tax compliance in Zimbabwe on small and medium enterprises SMEs for the tax period 2009 to 2011 focusing on how tax knowledge and compliance costs affected tax compliance behavior of SMEs. The main aim of the study was to examine how the unique business positions of SMEs, the perceptions of SME operators towards taxation, levels of tax knowledge and compliance costs affect tax compliance of SME taxpayers. In achieving these objectives, research propositions were stated which mainly stipulated that the current tax system in Zimbabwe does not cater for the special business needs of SMEs and that strong correlations do exist among tax knowledge, compliance costs and tax compliance. The study adopted qualitative research design. Methodological triangulation was employed, using the interview method and a questionnaire survey to collect primary data from SMEs in Harare, Chitungwiza and Bindura.

The results indicated that SMEs face different business conditions from large companies which cause them to bear high tax compliance burdens. The results also indicated that the perceptions of SME operators concerning tax fairness, tax service quality and government spending priorities greatly affect their tax compliance decisions. Tax knowledge was discovered to have no correlation with tax registration compliance but weak negative correlations with filing compliance. Compliance costs were discovered to have negative correlations with tax compliance. Therefore the study recommended that the current tax law should be amended to incorporate provisions that grant special tax incentives to SMEs in order to improve voluntary tax compliance by SME taxpayers. Furthermore the study recommended that the Zimbabwe Revenue Authority (ZIMRA) should disseminate information on tax updates more frequently in order to improve the levels of tax knowledge for voluntary tax compliance.

Muturi, and Michael, (2015) conducted a study on factors that influence compliances with tax laws among small and medium enterprises in Kenya; where the main objective was to analyze the factors influencing tax compliance among the SMEs in Kenya. To achieve this goal Kiambu County was taken as a case study. Tax understanding, tax rates, tax penalties, fines, tax compliance cost on tax compliance level has been considered as the main factors influencing tax compliances in Kenya. The study used questionnaires and oral interview method to collect data. The population of the study was a number of SMEs in Kenya and the sample size involved a number of SMEs in Kiambu County. A sample size of 400 was drawn from the target population of 2541 SMEs. His study concluded that the greatest contributors of tax compliance level are tax understanding and tax rates. The study is not striking the other factors out but their impacts are not as for these two. Generally, tax understanding, tax rates, tax compliance cost and tax fines and penalties influences tax compliance level significantly. Finally, the study concludes that tax compliance cost have the most significant effect on tax compliance. Kenya Revenue Authority (K.R.A) should set up agents who should site in different locations all over the country. Their main objective is to offer tax information devices for free. Some of the key services that they should be offering that are in great

need are ; tax computation, Filing of tax returns, which tax to be paid where, tax penalties and the due dates. If this is not possible then they can implement tax information Automatic telling machinery (ATM). The purpose of the ATM is to address direct questions. KRA can negotiate with certain banks especially Equity so that they can be located next to their ATM.

Philipp and Jan (2015) conducted a study on tax compliance in Slovenia, a field experiment with small firms with objective of identifying practices which may help to increase tax compliance of small companies. They classified the small companies in two groups which are control group and visit treatment group. The study focuses on the small accounting firms which are the group of tax payers that self-report taxable income and have high probability of non-compliant with tax laws. The result shows that there is evidence that treatment letter reminds the firms of civic duty to pay taxes and inform about it, the audit probability may increase tax compliance. Furthermore results indicated that informing taxpayers about the civic responsibility to pay taxes and audit probability may help to increase compliance.

Nicoleta (2011) conducted a study on factors for tax compliance in Romania, where the main objective was to identify the variable of tax compliance analyzed by other researcher in other country, and adopting in Romania conditions hence create a model to include factors that influence decision of tax compliance. Therefore he proposed variables that should be included in the model for predicting tax compliance after pooling of data from companies and individuals interviewed and it can crystallize the factors that have the most influence on tax compliance. Therefore these generalize the economic and non-economic factors for tax compliance.

Chebusit *et al*, (2014) conducted a study on factors affecting tax compliance in small and medium enterprises in Kitale Town Trans Nzoia in Kenya. The general objective was to asses' factors affecting tax compliance among small and medium enterprises; and establishes the influence of compliance cost, fines/ penalties and attitudes of compliance among small and medium enterprises. The population used in the study was 200 SMEs

where 132 respondents were drawn using stratified and simple random sampling. Survey questionnaire were used to collect data directly from respondents. The finding shows that, there is positive relationship between fines, penalties, compliance cost and attitude with tax compliance behavior. The study recommended that the tax system in Kenya should provide clear guidelines on how to fill the tax returns but also enhance the taxpayer education services to enable taxpayers to understand their right and obligations of tax payers.

Ng'eni, (2016) examined factors affecting tax morale and voluntary tax compliance towards effective tax administration in Tanzania. This was the desktop and library survey, which aimed at reviewing the general mechanisms of tax administration focusing on tax morale and voluntary tax compliance as a key attributes of tax revenues collections. The study shows that tax administration is most important in the process of increasing the government revenues. It also unveils crucial aspects of tax administration which tax authority should asses their cause and effect towards tax administration. It is notable that tax is the main sources of the government revenue therefore recommendations for improvement of tax administration are of importance to the policy makers and implementers in the world at large.

Adesina and Uyioghosa (2016) conducted a study on tax knowledge, penalties and tax compliance in small and medium scale enterprises in Nigeria using the survey study design. The objective of the study was to measure the effect of tax knowledge and penalties, in tax compliance. The result obtained from questionnaire were analyzed using the ordinary list square regression method, which revealed that tax knowledge had positive significant impact on tax compliance but tax penalties had insignificant positive impact on tax compliance. The study recommended that the government should therefore add more effort to increase tax knowledge and tax education should be included in school curricula at all times. Small and medium scale business owners should also hunt for tax knowledge and attentiveness for the mutual benefits of the governments and taxpayers. Therefore government should focus on increasing their

reputation and credibility, as a means of gaining the taxpayers trust which will enhance the issues of national pride and political affiliations. This will influence the increase of tax compliances.

2.4.1 Synthesis from the empirical reviews

From different studies reviewed on tax compliance was found that higher tax rates and complex filling procedures are the most important factor that encourage non-compliance of SMEs. Other factors like multiple taxation and lack of proper enlightenment are also affect tax compliance among the SMEs surveyed. Furthermore fine and penalty has been observed to have positive relationship with tax compliance amongst small and medium business surveyed.

However different studies conducted ignored demographic variable which have huge impact on tax payers perceptions on tax compliance. Since demographic characteristics such as gender, employment, income, number of household and education may affect tax payers perceptions was included under this study.

From the empirical review the tax payers seems to measure the benefit they get from the government as compared to the amount of tax they pay. And different studies like Fjeldstad *et al* (2012) concluded that SMEs tax payers are more likely to comply when their highly satisfied by the government services. Therefore the current study has examined how perception of tax payers on the government services delivery affect tax compliance in Tanga region.

On the other hand some of the studies found tax education and tax knowledge more significant in determining tax compliance attitude in developing countries. Studies such as Nzioki (2014) found tax knowledge, and tax education with positive effect on level of tax compliance among real estate investors.

Generally different literature reviewed in the empirical part involves the studies based on why SMEs do not pay tax, factors affecting tax compliance, and tax payer's attitude. Different results show that tax rate, tax education fine, penalties are the major factors

affecting tax compliance in Africa. Most of studies like Adesina and Uyioghosa (2016), Ng'eni, (2016) and Fjeldstad *et al* (2012) collected data using surveyed questionnaire from SMEs and were analyzed qualitatively whereby few of them were quantitatively analyzed. In this study the perceptions of SMEs on tax compliance will be analyzed quantitatively.

2.5 Conceptual Framework

The conceptual framework shows the way how the research will be conducted. It shows the variables and their logical relationships which can be presented by using mathematical equation charts, organ diagram or graphs (Ndunguru, 2007). This study examined the perceptions of SMEs tax payers towards tax compliance in Tanga region. The independent variables were perceptions of SMEs tax payers and the dependent variable was tax compliance. The perceptions of tax payers was based on different variables defined in the theoretical review this includes perceptions of tax payers on tax rate, fine, penalty, government services delivery, and tax education. Moreover demographic characteristics were also included in the conceptual model as it has a psychological effect on tax compliance.

From economic deterrent theory the increase of tax rate affects tax payer's perception negatively since decrease in tax rate influence tax payers positively. Therefore an increase in tax rate perceived by tax payers as increasing the benefit of tax evasion while decreasing tax rate perceived by tax payers as decreasing benefit of tax evasion therefore increasing tax rate increases tax evasion while decreasing tax rate increases tax compliances. While penalty and fine are affecting tax compliance positively which means that the increase in penalty and fine was perceived to increase the cost of tax evasion and hence discourage tax evasion and decrease in penalty and fines encourages non tax compliance.

Fiscal exchange theory suggests that the presence of government expenditures may serve as the motivating factor for taxpayer compliance especially when the government offers the quality and well improved goods and services that the society expects to get (Alm,

1999). Under Psychological theory tax education might affect perception of tax payers since an increasing tax education was likely to increase tax compliance level. The demographic characteristics were also affecting tax payer’s perception to ward tax compliance. Tax payers demographic characteristics has been observed to affect tax compliance by different studies like Ozdamar (2011) who proved that marital status has influence on tax compliance where married spouse are more likely to comply than unmarried spouses.

The conceptual model is as presented in figure 1.

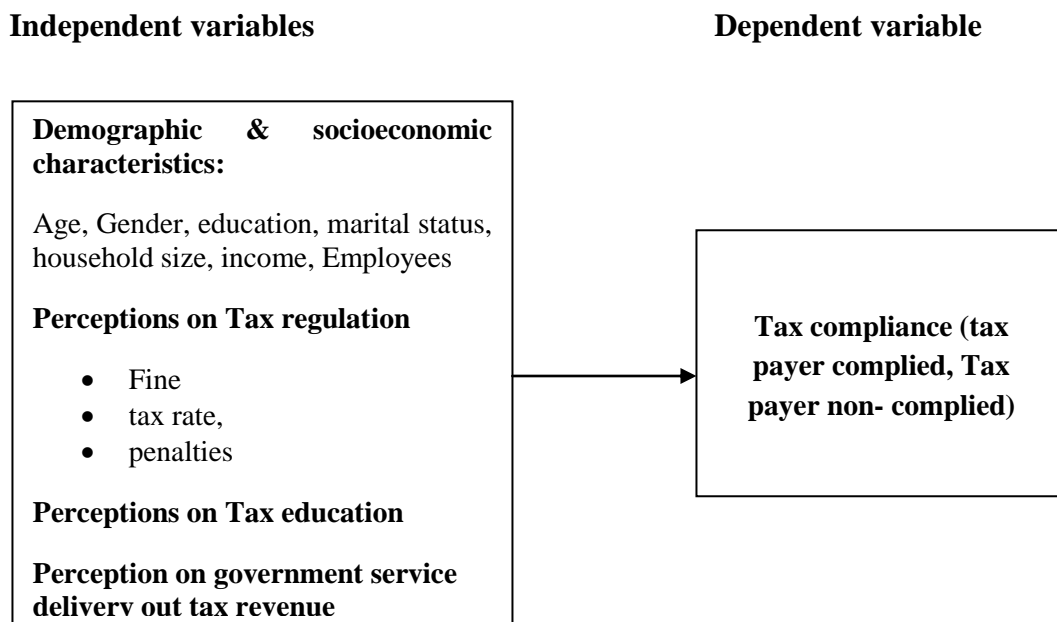


Figure 2.1: The conceptual model of the study

2.6 Research Hypothesis

Regarding to the main objective of the study, as to assess the perception of SMEs on factors affecting tax compliance amongst small and medium enterprises in Tanzania the case of Tanga region, the study makes the following set of testable hypothesis which are Null hypothesis (H0) and alternatives hypothesis (H1).

H₀: Perceptions on the level / rate of tax do not have significantly effect on tax compliance level.

H₁: Perceptions on the level / rate of tax has significantly effect on tax compliance level.

H₀: Perceptions on penalties/fines for non-compliance has significantly effect on compliance level.

H₁: Perceptions on penalties/fines for non-compliance do not have significantly effect on tax compliance level.

H₀: Perceptions on tax education / tax awareness do not have significantly effect on tax compliance;

H₁: Perceptions on tax education / tax awareness has significantly effect on tax compliance level.

H₀: Perception on government service delivery has no significantly effect on tax compliance level.

H₁: Perception on government services delivery has significantly effect on tax compliance level

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter shows the process which the research was conducted and all the methods of data collection employed. The first part of the chapter explains the research design used while the second part provides the study population. Section three of the chapter discusses the sample size and sampling techniques and the fourth part gives sources of data. The other part includes research variables and units of measurement and finally data analysis techniques.

3.2 Description of the Study Area

Tanga is located in the coastal region with a population of 1680262 compared to Dar es salaam with population of 2609000 in 1996 to 2012 where the population density is 60.2 and 1772 respectively. The coastal regions of Tanzania are critical to its future social and economic development. Despite of their reach in natural resources they contribute 32% to the national income in 1996-2012. The coastal area is characterized by substantial potential for agriculture, mariculture and fisheries, tourism, small scale farming and manufacturing, moreover 75 percent of countries industry located in coastal area. Tanga contributed 5.6% to the national income as compared to Dar es salaam which contributed 19.1% for the period of 1980 to 1994. . (Wagner and Mchallo 2003). Moreover, it has contributed an average of 5.5% to the GDP compared to Dar es salaam which contributed 20.3% in 2012. (National Population Census 2012). The area is selected for the study due to low contribution to the national income. Tangacity and Muheza District are among the 10 Councils which form Tanga region. It shares borders with Coast region on the South and East, Morogoro region to the South, Arusha region to the west and Kilimanjaro to the North. The region is situated between latitudes 3° 20' and 3°45' South of the Equator and between longitude 33° 20' and 35° 35' East of the Greenwich Meridian.

3.3 Study Design

Every empirical research has a study design (Yin (2009)). In view of this particular study, the cross-section survey study design was used because; data was to be collected once from the respective sampled SMEs tax payers. The appropriate survey techniques in the collection of required data on perceptions of SMEs tax payers on factors affecting tax compliance were employed.

3.4 Study Population

The targeted population of the study is small and medium business enterprises (SMEs) tax payers in Tanga Region; where different traders and manufacturers from Tanga City and Muheza District constitute the prospective population under study.

3.5 Sample Size and Sampling Technique

Combination of Purposeful and cluster non probability sampling techniques and random sampling technique were employed in getting the sample size in the study area. Initially the Districts in the study area were divided into two clusters based in the population criteria where Tanga, Lushoto, Korogwe, Kilindi and Handeni with population of 273332,492441,242038,236833 and 276646 respectively, were grouped to the first cluster with high population and Muheza, Pangani, Korogwe town, Handeni town and Mkinga were grouped to the second cluster with low population as 204461,54025, 68308,79056 and 118065 respectively, Tanzania population census (2012). Random selection was employed to select two Districts one from each group to represent others, where Tanga City and Muheza Districts were selected. The distributions of SMEs tax payers by ward are shown in table 3.1 and 3.2

Table 3.1: Distribution of SMEs taxpayers by ward in Tanga city council

DISTRICTS	WARD	NO OF SME	DIRECTION
TANGACITY	Tanga sis	394	South
	Kiomoni	89	east
	Maweni	189	west
	Duga	157	North
	Tongoni	96	East
	Pongwe	256	East
	Mwanzange,	120	East
	Mzingani	98	North
	Mabokweni	102	west
	Mnyanjani	145	South
	Magaoni	190	East
	Chunguliani	56	East
	Mzizima	102	North
	Marungu	106	North
	Kirare	104	North
	Usagara	319	South
	Msambweni	230	South
	Nguvumali	286	East
	Masiwani	303	East
	Makorola,	350	North
	, Mabawa	408	West
	Cental	370	North
	Ngamianikati	380	West
	Ngamianikaskazini	390	East
	, Chumbageni	280	West
	Ngamianikusini,	357	West
	Total	5877	

Tanga city trade officers report (2016)

Table 3.2: Distribution of SMEs taxpayers by ward in Muheza Districts council

DISTRICTS	NAME OF WARD	NO OF SMEs	LOCATION OF SME
Mheaza	Mbaramo	310	West
	Tanganyika	290	West
	Masuguru	167	West
	Kwemkabala	189	South
	Majengo	330	East
	Genge	156	East
	Lusanga	54	East
	Tingeni	25	North
	Kwakifua	45	West
	Songa	87	South
	Bwembera	56	East
	Kwafungo	67	East
	Togwe	34	North
	Kicheba	47	North
	Misozwe	34	North
	Kwemigoji	76	South
	Makole	45	South
	Mkanyageni	45	East
	Azimio	23	East
	Amani	38	North
	Kisiwani	24	East
	Zirai	20	North
	Kwezitu	30	West
	Shebomeza	57	East
	Kizurei	18	West
	Potwe	27	West
	Kilulu	26	West
	Mtindiro	32	East
	Mkuzi	59	North
	Magila	38	North
	Magoroto	24	North
	Kigombe	35	West
	Mpapayu	76	West
	TOATAL	2587	

Muheza district trade officers report (2016)

Given the total population of 8464 in both Tanga city and Muheza District, Kothari, (2004) suggested the formula below for sample size calculation.

$$n = \frac{N}{N \times d^2 + 1}$$

Where; n = number of Sample

N = Total number of population = 8464

d = error margin = 0.0783 (7.84%)

$$n = \frac{8464}{8464 \times 0.0783^2 + 1} = 160.0246451 \approx 160$$

Therefore the sample size for this study was 160 respondents.

Moreover, the research sample size employed is supported by Tabachnick and Fidell, 2007 cited by Maseko (2014) proposed the formula; $N \geq 50 + 8m$ where the formula as a rule of thumb for determining sample size for the multiple regression analysis. N explains the sample size, whereas; m is the number of variables involved in the model. Using this formula the number of sample size employed exceeded the required sample size which increases the accuracy of the study. Ward was selected randomly in each district where 10 wards were selected from Tanga City and 4 wards were selected from Muheza districts covering all geographical positions to avoid biasness. Consider table 3.3 below.

Table 3.3: Sample size and Technique employed for each districts

Districts	Number of wards	Ward selectd	Total SME in wards selected	SMEs tax payers sampled (proportionate)
Tanga city	27	10 purposeful selected	2524	$n = \frac{2524}{8464} \times 160 = 111$
Muheza	34	4purposeful selected	693	$n = \frac{693}{8464} \times 160 = 49$
Total	61	14	3217	160

Source (Surveyed data, 2017)

Furthermore, from each districts as Table 5 shows that 49 respondents selected from Muheza district and 111 were selected from Tanga City council. The distribution is presented in table 3.4.

Table 3.4: Sample size and Technique employed for each ward in each District

Districts	Ward selected	Number of SMEs tax payer in the each ward	SMEs tax payers sampled (proportionate)
Tanga city	Kiomoni	89	$n = \frac{89}{2524} \times 111 = 4$
	Tanga sisi	394	$n = \frac{394}{2524} \times 111 = 17$
	Maweni	189	$n = \frac{189}{2524} \times 111 = 8$
	Duga	157	$n = \frac{157}{2524} \times 111 = 7$
	Chumbageni	280	$n = \frac{280}{2524} \times 111 = 12$
	Ngamiani kaskazini	390	$n = \frac{390}{2524} \times 111 = 17$
	Mabawa	408	$n = \frac{408}{2524} \times 111 = 18$
	Mnyanjani	145	$n = \frac{145}{2524} \times 111 = 7$
	Central	370	$n = \frac{370}{2524} \times 111 = 16$
	Mabokweni	102	$n = \frac{102}{2524} \times 111 = 5$
Muheza	Mbaramo	310	$n = \frac{310}{693} \times 49 = 22$
	Genge	156	$n = \frac{156}{693} \times 49 = 11$
	Kwemkabala	189	$n = \frac{189}{693} \times 49 = 13$
	Magila	38	$n = \frac{38}{693} \times 49 = 3$
TOTAL		3217	160

Source (Surveyed data, 2017)

3.6 Sources of Data

The data were collected from primary sources. The data collected focuses on perceptions of SMEs (traders and manufacturers) on factors affecting tax compliance in Tanga Region. Primary data on perceived factors affecting tax compliance to both traders and manufacturers was collected.

3.7 Data collection instruments

The major tool for data collection was a semi-structured questionnaire. This tool was used in collecting data from managers or owners of the SMEs tax payers in the study area. The semi-structured questionnaire, which consist of both open and closed ended questions constructed to capture both qualitative and quantitative data. The questionnaire was organised into three parts. The first part aimed to obtain background information, the second part was on perceptions of SMEs on business regulation, the third part intended to obtain data on perceptions of SMEs on government service deliveries and forth part aimed at gathering data of SMEs perceptions on tax education to tax compliance.

3.8 Research Variables

The principle independent variables are in four categories which are personal characteristics, perception of SME on tax regulations, perception of SME on government services delivery, perception of SME on tax education, and the dependent variable is tax compliance.

3.8.1 Dependent Variable

The tax compliance explains the way the tax payers comply with tax rule and regulation abided with small and medium enterprise. The tax payer may be complied by fulfilling the requirement of the rule and regulation set by tax Authority. On the other hand, tax payer may be not complying with tax regulation and rules guiding the small and medium enterprise operation.

3.8.2 Independent Variable

The independent variables fall into business characteristics, perception of tax payers on business regulation, tax education and government service delivery. However, independent variables in qualitative data were measured in dummy, while quantitative variable were measured in continuous number. More elaboration of the variable used in logistic regression is given in the Table 3.5.

Table 3.5: Operationalization of the Variables and measurement

S/N	Variable	Definition and measurement	Unit	Data Source
Dependent variable				
Y	Tax Compliance	1 if tax payer complied 0 for non-compliance	Choice	Field Survey
Independent variables				
X ₁	Age	Age of respondent	Year	Field Survey
X ₂	Sex	1 if respondent is male, 0 otherwise	Dummy	Field Survey
X ₃	Education	1= No education, 2= primary, 3= secondary 4=post secondary	Dummy	Field Survey
X ₄	Marital status	1 if married, 0 otherwise	Dummy	Field Survey
X ₅	Household	Total number of individuals in household	Number	Field Survey
X ₆	Perception on Tax rate	1 if tax is high, 0 otherwise	Dummy	Field Survey
X ₇	Perception on Fine	1 if high, 0 otherwise	Dummy	Field Survey
X ₈	Perception on Penalty	1 if high, 0 otherwise	Dummy	Field Survey
X ₉	Perception on Tax education	1 if high, 0 otherwise	Dummy	Field Survey
X ₁₀	Government service	1 if encourage tax payer, 0 otherwise	Dummy	Field Survey

Source (Surveyed data, 2017)

3.9 Econometric model

Binary Logistic regression is an analytical tool used to investigate the dependent variable when the outcome is dichotomous, that is the dependent variable has two categories (Kohler and Kreuter, 2005; Hill *et al.*, 2008). The most commonly used models in studies related to the aspects of choice such as choice decision are the probit and logit models, both of which have dependent variables bound between 0 and 1. The models are convenient for dichotomous choice variables. However, many literatures and studies have used logistic regression. According to Griliches 1957 and Rogers, 1995 they advocate that the use of the logit model is consistent with the literature on choice which described the choice process as taking on a logistic nature. The Logit model have also been applied in several choice studies by Kato (2000); Boahene *et al.*, (1999); Nkonya *et al.*, (1997); as well as Shakya and Flinn (1985). In regards with several studies, this study opted to use logistic regression.

In a view of the assumption is that, the identified factors may not or have been perceived by SMEs tax payers negatively on tax compliance. Therefore, tax payer may be complier or non-complier with tax regulation and that is what drives the study to opt logistic binary choice model. Mathematically according to Pedace, (2013) the model is represented as follows;

$$P = \frac{e^{\beta x}}{1 + e^{\beta x}} \dots\dots\dots i$$

$$1 - P = 1 - \frac{e^{\beta x}}{1 + e^{\beta x}} = \frac{1}{1 + e^{\beta x}} \dots\dots\dots ii$$

Where, P is the probability of a tax payer to comply or not comply β is the given coefficient e denotes the base of natural logarithms, X_i represents the *ith* and represents vector of parameters to be estimated. The first equation shows the probability of tax payer to comply and the second equation presented shows the probability of tax payer not to comply.

$$Y = \beta_0 + \beta_i X_i + \varepsilon$$

Where Y= tax compliance (1 if one comply, 0 if one do not comply)

X_i = set of independent variables (Factors)

ε = error term

From equation (ii) the study had analyzed this regression equation as follow

$$\text{Log}\left(\frac{Y_i}{1 - y_i}\right) = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \beta_7 X_7 + \beta_8 X_8 + \beta_9 X_9 + \beta_{10} X_{10} + \varepsilon$$

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \beta_7 X_7 + \beta_8 X_8 + \beta_9 X_9 + \beta_{10} X_{10} + \varepsilon$$

Where by

Y=Tax compliance

X₁ =Age

X₂ = Gender

X₃= Education

X₄= Marital status

X₅= Household size

X₆= taxpayers perception on penalties

X₇= taxpayers perception on fines

X₈= taxpayer perception on government Services delivery

X₉ =tax payer perception on tax-education

X₁₀ =tax payer perception on tax rate

μ = error tem

3.10 Data processing and Analysis

Data collected were organised, managed, coded and checked for accuracy and finally data analysis was conducted. Data analysis involved simple descriptive statistics analysis, followed by logistic regression analysis of an econometric model that was developed for the study. T-statistics was used to test the significance of the estimated relationship between perceptions of SMEs tax payers on factors affecting tax compliance (independent variables) to tax compliance levels (dependent variable). However, likert scale with five point are used as many of respondents are often not comfortable with providing a solid yes or no, agree or disagree, like or dislike, and they like to hide their responses on the contrary as a researcher must be interested with how many agree or

disagree, like or dislike and if there is statistical tie. This test was originally developed and used by Leo and Yulia (2014) for analysis of a prediction survey for an Indian business magazine. In likert scale survey different question requires a respondent to either strongly agree, agree, neutral, disagree and strongly disagree. For this case the analysis of any likert scale will be converted in to binary responses, for those who are strongly agree, agree, neutral will be corded as 1 and for those who are disagree and strongly disagree was corded as 0

CHAPTER FOUR

PRESENTATION OF THE FINDINGS

4.1 Introduction

This chapter presents the finding of the study which includes demographic characteristics, perception of SMEs tax payers on tax regulation towards tax compliance, perception of SMEs tax payers on Government Service delivery towards tax compliance and perception of SMEs on tax education towards tax compliance. In attempt of capturing information for the study, survey questionnaires with 25 questions were distributed to respondents to respond to various questions. All questionnaires were filled by 160 respondents from Muheza and Tanga City council. Based on total number of SMEs, 49 respondents were from Muheza District and 111 respondents from Tanga City.

4.2 Demographic characteristic of the SME Tax payers

4.2.1 Age of respondents

The result from table 4.1 indicates that 15 percent of interviewed respondents were between 18 and 29 years, 25 percent of interviewed respondents were between 29 and 40 years, 48.13 percent of interviewed respondents were between 40 and 51 years while 11.88 percent of interviewed respondents were between 51 years and above. This implies that majority of respondents were 40 and 51 years.

Table 4.1: Age of respondents

Age of respondents	Frequency	Percent
18-29 years	24	15.0
29-40 years	40	25.0
40-51 years	77	48.13
51 years and above	19	11.88
Total	160	100.0

Source (Surveyed data, 2017)

4.2.2 Gender of respondents

The table 4.2 shows distribution of the 160 respondents based on marital status. The analysis shows that 35 percent of the respondents were female while 65 percent of respondents were male. The results indicates that majority of respondents were male. This may be explained that male have responsibility to ensure family get daily bread and other services. This pushes male to participate in business activity that generates income for fulfilling the family expenditure. The finding contradicts with Msato (2009) who found that women are participating more in small and medium enterprises than men.

Table 4.2: Gender of respondents

Gender	Frequency	Percent
Female	56	35.0
Male	104	65.0
Total	160	100.0

Source (Surveyed data, 2017)

4.2.3 Education level of respondents

The table 4.3 shows distribution of the respondent based on their level of education. In analysis, it was found that 9.4 percent of the respondents had informal education, 55.6 percent of respondents had primary education, and 25 percent of respondents had secondary education while 10 percent of respondents had college or university education. Therefore, majority of interviewed respondents had primary education level. This may be explained that people with primary education opt to do small and medium business due to little chance of having employment in either government or private companies.

Table 4.3: Education level of respondents

Education level	Frequency	Percent
Informal Education	15	9.4
Primary education	89	55.6
Secondary Education	40	25.0
College or University Education	16	10.0
Total	160	100.0

Source (Surveyed data, 2017)

4.2.4 Marital status of respondents

The table 4.4 shows distribution of the respondent based on marital status. In analysis, it was found that 12.5 percent of the respondents were single, 51.2 percent of respondents were married and 21.2percent of respondents were widow while 15.0 percent of respondents were divorced. In conclusion, majority of respondents were married. This may be explained that married spouses should work hard in order to finance their family. On the other hand, married spouses help to share responsibility of the families which increase the household income.

Table 4.4: Marital status of respondents

Marital status	Frequency	Percent
Single	20	12.5
Married	82	51.2
Widowed	34	21.2
Divorced	24	15.0
Total	160	100.0

Source (Surveyed data, 2017)

4.2.5 Household size of the respondents

The results from table 4.5 reveals that 53.75 percent of respondents were living together in the household of 1-3 people sharing the same dish, 34.38 percent of respondents lived in the household of 3-5 people together sharing the same dish, 10.63 percent of respondents lived in the household of 5-7 people together sharing the same dish while 1.25 percent of respondents lived in the household of 7.9 people together sharing the

same dish. The majority of the households had 1.3 people living and sharing the same dish in the family. The possible explanation may be authority on family planning help people to change behavior and focus on the small family which enable them to handle provisions of good service to them.

Table 4.5: Household size of the respondents

House hold size	Frequency	Percent
1-3 people	86	53.75
3.5 people	55	34.38
5-7 people	17	10.63
7-9 people	2	1.25
Total	160	100.0

Source (Surveyed data, 2017)

4.2.6 Respondent's business income

The results from table 4.6 reveals that 73.13 percent of respondents had business income between 500001 and 4500000 Tsh per month, 20.00 percent of respondents business income fall between 4500001 and 8500000Tsh per month, 6.25 percent of respondents had business income between 8500001 and 12500000 Tsh per month and 0.62 respondents had been captured with business income between 12500001 and 16500000 Tsh per month. The possible explanation may be that most of the SMEs had involved in small business with small capital thus why their incomes become small.

Table 4.6: Respondent's business income

Income	Frequency	Percent
500001-4500000 Tsh	117	73.13
4500001-8500000Tsh	32	20.00
8500001-12500000Tsh	10	6.25
12500001-16500000 Tsh	1	0.62
Total	160	100.0

Source (Surveyed data, 2017)

4.2.7 Number of employees in SME

The results from table 4.7 reveals that 41.9 percent of respondents had 1-3 employees, 45.6 percent of respondents had 4-49 employees while 12.5 percent of respondents had 50-99 employees. The possible explanation may be small and medium enterprises have small capital which generates small revenue.

Table 4.7: Number of employees in SME

Number of employers	Frequency	Percent
1-4	67	41.9
4-49	73	45.6
50-99	20	12.5
Total	160	100.0

Source (Surveyed data, 2017)

4.3 The perceptions of SMEs tax payers on business tax regulations, tax revenue utilization, and effectiveness of tax education on tax compliance,

4.3.1 SME tax payer’s perceptions on Tax rate

Table 4.8, indicates the result of cross tabulation of Tax payers Perceptions on Tax rate and tax compliance. The result of Pearson Chi-square test was 3.2851 with p-value of 0.070. Since P – value (0.070) which is less than 10% level of significance: hence, there is sufficient evidence to reject the null hypothesis and therefore the findings conclude that there was association between tax rate and tax compliance.

Table 4.8: Cross tabulation of SMEs Tax payers Perceptions on Tax rate and tax Compliance

Tax Compliance	Tax payers Perceptions on Tax rate		Total
	0	1	
1	24	40	64
0	50	46	96
Total	74	86	160
Pearson chi2(1)	3.2851	Prob	0.070

Source (Surveyed data, 2017)

4.3.2 SME tax payer’s perceptions on Penalty

Table 4.9, indicates the result of cross tabulation of Tax payers Perceptions on Penalty and tax compliance. The result of Pearson Chi-square test was 33.8824 with p-value of 0.000. Since P – value (0.000) was less than 5% level of significance: hence, there was sufficient evidence to reject the null hypothesis and therefore the findings conclude that there was association between Penalty and tax compliance.

Table 4.9: Cross tabulation of SMEs Tax payers Perceptions on Penalty and tax Compliance

Tax Compliance	Tax payers Perceptions on Penalty		Total
	0	1	
1	52	12	64
0	33	63	96
Total	85	75	160
Pearson chi2(1)	33.8824	Prob	0.000

Source (Surveyed data, 2017)

4.3.3 SME tax payer’s Perceptions on Fines

Table 4.10, indicates the result of cross tabulation of perceptions of tax payers on fines and tax compliance. The result of Pearson Chi-square test was 20.0694 with p-value of 0.000. Since P – value (0.000) was less than 5% level of significance: hence, from these findings there is sufficient evidence to reject the null hypothesis and therefore the findings conclude that there was association between perceptions on Fine and tax compliance.

Table 4.10: Cross tabulation of tax payers Perceptions on Fines and Tax Compliance

Tax Compliance	Perceptions of tax payers on Fines		Total
	0	1	
1	52	12	64
0	44	52	96
Total	96	64	160
Pearson chi2(1)	20.0694	Prob	0.000

Source (Surveyed data, 2017)

4.3.4 Effectiveness of tax education on tax Compliance

Table 4.11, indicates the result of cross tabulation of tax education Campaign and tax compliance. The result of Pearson Chi-square test was 0.4618 with p-value of 0.497. Since P – value (0.497) was greater than 5% level of significance: hence, from the findings there is little evidence to reject the null hypothesis and therefore the study findings conclude that there was no association between Effectiveness of tax education and tax compliance.

Table 4.11: Cross tabulation of Effective tax education and Tax compliance

Tax compliance	Tax Education Campaign		Total
	0	1	
1	24	40	56
0	31	65	104
Total	55	105	160
Pearson chi2 (1)	0.4618	Prob	0.497

Source (Surveyed data, 2017)

4.3.5 SME tax payer’s Gender and Tax compliance

Table 4.12, indicates the result of cross tabulation of gender and tax compliance. The result of Pearson Chi-square test was 2.2161 with p-value of 0.137. Since P – value (0.137) was greater than 5% level of significance: hence, from these findings, there is sufficient evidence to support the null hypothesis and therefore the study findings conclude that there was no association between gender and tax compliance.

Table 4.12: Cross tabulation of Gender and Tax compliance

Tax Compliance	Gender		Total
	0	1	
Female	18	46	64
Male	38	58	96
Total	56	104	160
Pearson chi2(1)	2.2161	Prob	0.137

Source (Surveyed data, 2017)

4.3.6 SME tax payer's cross tabulation of Income and Tax compliance

Table 4.13, indicates the result of cross tabulation of income and tax compliance. The result of Pearson Chi-square test was 59.0291 with p-value of 0.000. Since P – value (0.000) was less than 5% level of significance: hence, from these finding there is sufficient evidence to reject the null hypothesis and therefore the study concludes that there was association between income and tax compliance.

Table 4.13: Cross tabulation of income and Tax compliance

Tax Compliance	Income		Total
	500000-900000	Above 900001	
0	64	0	64
1	39	57	96
Total	103	104	160
Pearson chi2(1)	59.0291	Prob	0.000

Source (Surveyed data, 2017)

4.3.7 The tax collected assists the government in provision of services.

Figure 4.1: Indicated that 47 percent of respondents revealed that tax collected does not assist the government in provision of services while 53 percent of respondents revealed that tax collected assists the government in provision of services. Therefore, majority of respondents revealed that tax collected assists the government in provision of services. This means majority of tax payers observed the importance of paying tax to the government as it help to improve service provision.

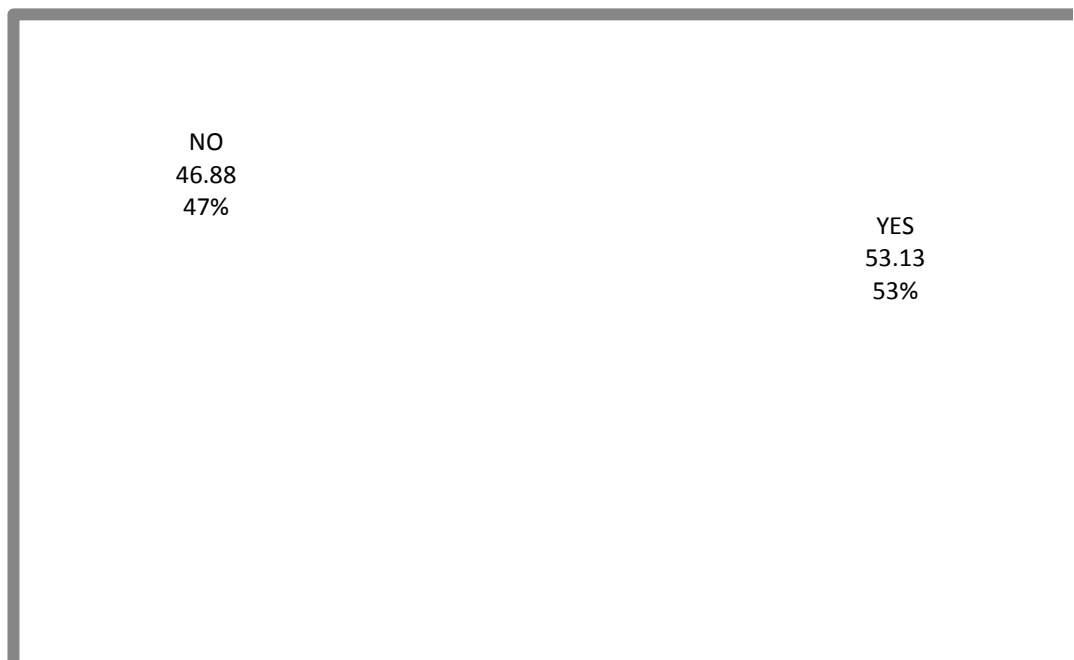


Figure 4.1: Showing distribution of response on government service provision

4.3.8 Level of satisfaction tax payers gets from government services

Figure 4.2 indicated that 13 percent of respondents interviewed had strongly disagreed that tax payers get satisfaction from government services, 15 percent of respondents interviewed had disagreed that tax payers gets satisfaction from government services, 43 percent of respondents interviewed had neutral response on either tax payers gets satisfaction from government services, 8 percent of respondents interviewed had agreed that tax payers get satisfaction from government services while 21 percent of respondents interviewed had strongly agree that tax payers gets satisfaction from government services. Therefore, majority of respondents had neutral response on satisfaction of the tax payers on government service delivery.

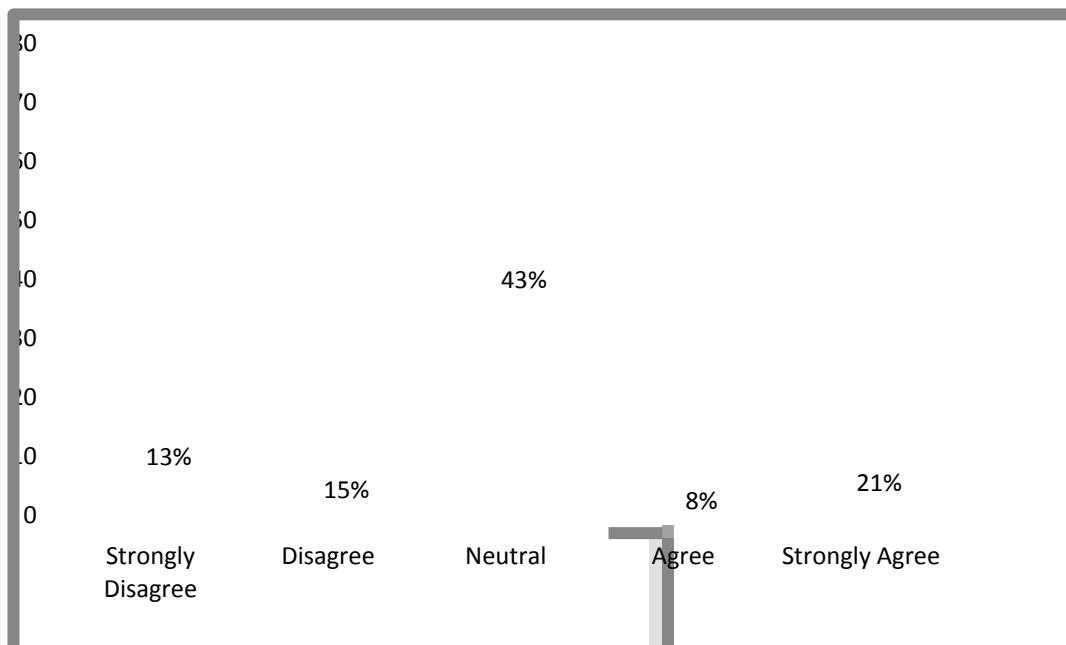


Figure 4.2: Level of satisfaction tax payers gets from government services

4.3.9 Improper accountability and utilization of Tax revenues by Government influence Tax Evasion

Figure 4.3 indicated that 15 percent of respondents interviewed had strongly disagreed that improper accountability and utilization of Tax revenues by Government influence Tax Evasion, 4 percent of respondents interviewed had disagreed that improper accountability and utilization of Tax revenues by Government influence Tax Evasion, 75 percent of respondents interviewed had neutral response on either Improper accountability and utilization of Tax revenues by Government influence Tax Evasion while 6 percent of respondents interviewed had strongly agreed that improper accountability and utilization of Tax revenues by Government influence Tax Evasion. Therefore, majority of respondents had neutral response on whether improper accountability and utilization of Tax revenues by Government influence Tax Evasion.

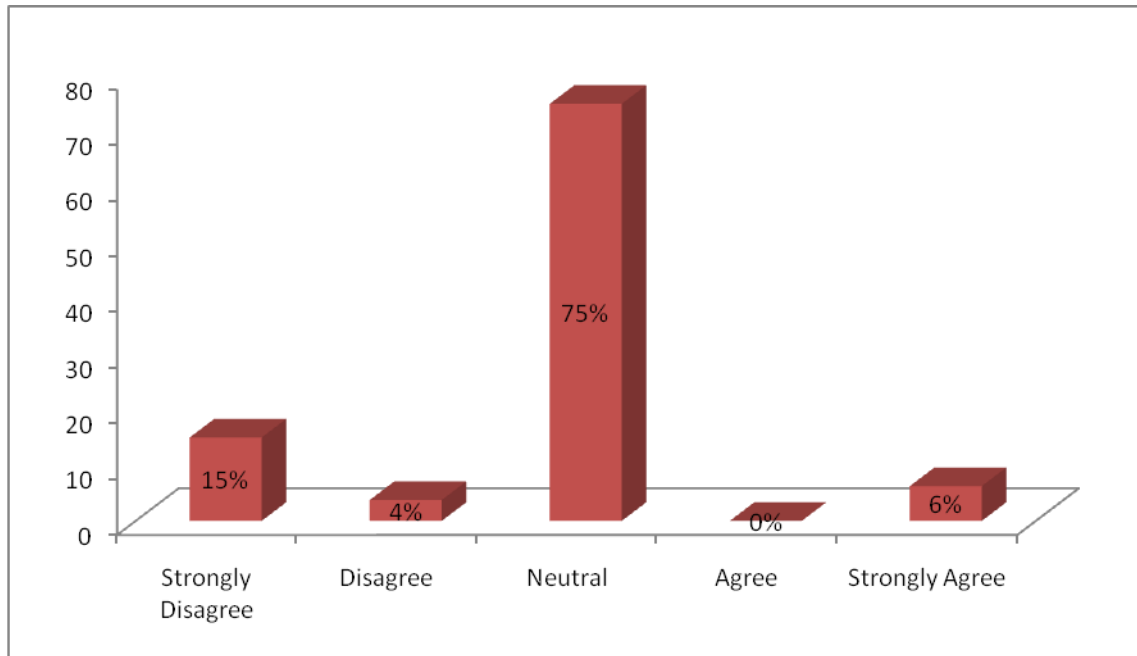


Figure 4.3: Improper accountability and utilization of Tax revenues by Government influence Tax Evasion

4.3.10 Government creates conducive environment for SMEs to pay tax

Figure 4.4 indicated that 13 percent of respondents interviewed had strongly disagree that government creates conducive environment to SMEs to pay tax, 15 percent of respondents interviewed had disagreed that government creates conducive environment to SMEs to pay tax, 43 percent of respondents interviewed had neutral response on either government creates conducive environment to SMEs to pay tax, 8 percent of respondents interviewed had agreed that government creates conducive environment to SMEs to pay tax while 21 percent of respondents interviewed had strongly agree that Government creates conducive environment to SMEs to pay tax. Therefore, majority of respondents had neutral response on whether government creates conducive environment for SMEs to pay tax.

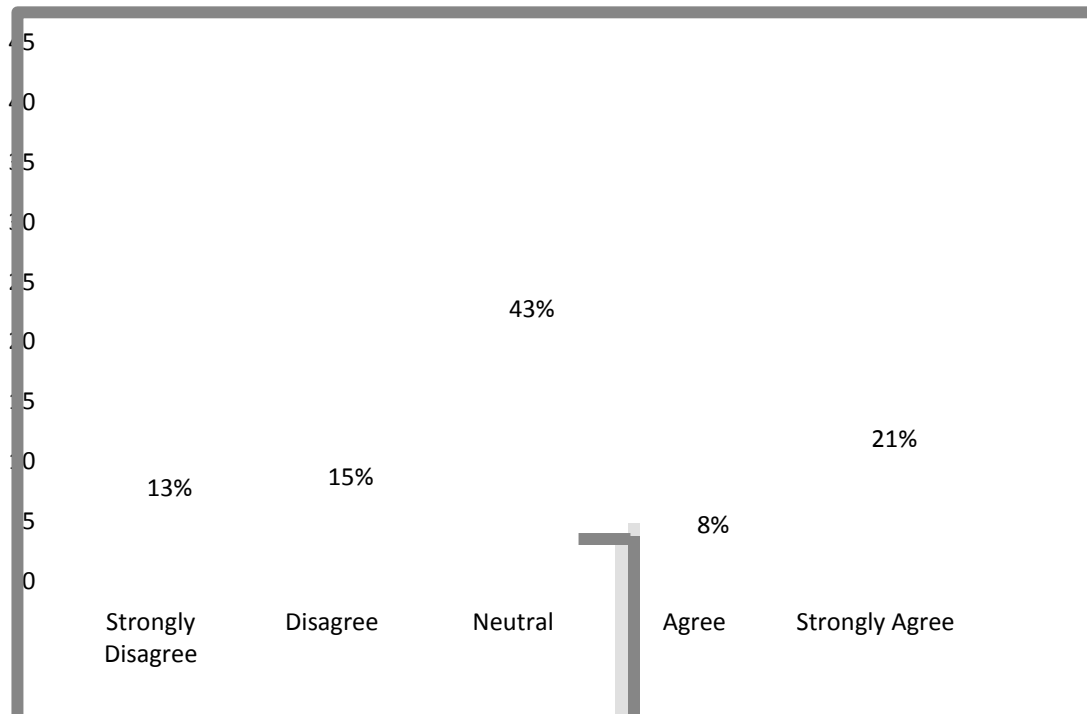


Figure 4.4: Government creates conducive environment to SMEs to pay tax

4.4 The perceptions of SMEs tax payers on business tax regulations, government service delivery, and tax education in tax compliance.

4.4.1 Correlation Matrix

The table 4.14 shows result of the correlation analysis of dependent variables with independent variables. However, results indicated that all independent variables such age, gender, education, marital status, household size, Tax Education, tax rate, penalty and Government services has no collinear relationship among themselves.

Table 4.14: Correlation Matrix

	Tax_co~e	Gender	Educat~n	Marital	Househ~d	Tax_Educ	Tax_rate	Penalty	Fine	G_serv~s
Tax_comp	1.0000									
Gender	-0.1177	1.0000								
Education	0.0000	0.0759	1.0000							
Marital	-0.0881	0.1038	0.0618	1.0000						
Household	0.1149	0.0569	0.0315	0.0005	1.0000					
Tax_Educ	0.0537	0.2414	-0.0528	0.0618	0.0399	1.0000				
Tax_rate	-0.1433	-0.1288	-0.0907	0.0121	0.0106	-0.0907	1.0000			
Penalty	0.4602	-0.0197	-0.0321	0.0493	0.0939	0.0470	0.0926	1.0000		
Fine	0.3542	-0.1765	0.0537	-0.1710	0.0492	-0.0806	0.0154	0.2045	1.0000	
G_service	0.5564	-0.0489	0.0191	0.1144	-0.0581	0.0457	-0.0275	0.2695	0.1133	1.0000

4.4.2 Logit Estimation Results of SMEs perceptions on Tax Compliance

The results of the Logit regression model estimating SME payer’s perceptions on Tax Compliance are presented in table 1. The goodness of the model has been shown by Wald Test. The Wald test was found to be 49.57 with P-value of 0.0000. The model was statistically significant at (P < 1%). The Pseudo R-square was 0.53.28 equivalent to 53%. This implies that independent variables explain the variation in dependent variable by 53%, where 47% of variation in dependent variable explained by other factors not included in the model. However, some variables in the model were statistically significant influencing tax compliance. Such variables were Gender at 10% level of significant, Marital Status Dummy at 5% level of significant, household at 10% level of significant while Tax rate, Penalty, Fine and Government services were significant at 1% level of significant in study area. Mean while age, perception on Tax education dummy and education dummy were statistically insignificant at 1%, 5% and 10% level of significant in influencing tax compliance in the study area.

Table 4.15: Logit Estimation Influence of SMEs perceptions on Tax Compliance

Tax compliance	Robust			
	Coefficient	Std. Error	Z	P < [Z]
Age	-0.0179	0.0229	-0.78	0.4350
Gender (1 if male, 0 otherwise)	-1.1338	0.6820	-1.66	0.0960
Education Dummy (1 if formal education, 0 otherwise)	-0.2167	0.5384	-0.40	0.6870
Marital Status Dummy (1 if married, 0 Otherwise)	-1.1752	0.5411	-2.17	0.0300
Household (Number of members in the household)	0.3575	0.2006	1.78	0.0750
Education (1 if perceived higher on education, 0 otherwise)	0.3156	0.5989	0.53	0.5980
Tax rate (1 if perceived high tax rate, 0 otherwise)	-1.3460	0.5058	-2.66	0.0080
Penalty (1 if perceived high penalty, 0 otherwise)	2.6029	0.6035	4.31	0.0000
Fine (1 if perceived high fine, 0 otherwise)	1.6535	0.5705	2.90	0.0040
Government services (1 if perceive high service provision, 0 otherwise)	3.8499	0.7611	5.06	0.0000
Constant	-0.7614	1.4475	-0.53	0.5990
Number of Observation			160	
Wald Chi2 (9)			49.57	
Prob > Chi2			0.0000	
Pseudo R2			0.53.28	
Log pseudo likelihood			-50.304148	

Source (Surveyed data, 2017)

4.4.3 Model Specification Test

The model specification test was performed to check whether a model is not suffering from specification bias. Gujarati (2004) argued that model for data analysis should be well specified or should not have specification bias. From test, hatsq had 0.0054 equivalents to 0.54%. Since P –value (0.9330) of hatsq is greater than 10%, hence the null hypothesis is not rejected which stated that a model is well specified while alternative hypothesis stated that a model is not well specified. Therefore, a model is well specified and not suffering from specification bias as in indicated in table 4.16.

Table 4.16: Model specification Test

Tax compliance	Coefficient.	Std. Err.	Z	P>z
_hat	0.9980	0.1574	6.34	0.0000
_hatsq	0.0054	0.0641	0.08	0.9330
_cons	-0.0139	0.3034	-0.05	0.9640

Source (Surveyed data, 2017)

4.4.4 Marginal effect of SMEs Perception on Tax Compliance

Table 4.17 shows the parameter estimates (coefficients) and marginal effects at the means of the Logit regression with their respective robust standard errors. However, to avoid repetition in discussions, the results of the marginal effects are only discussed as they can indicate both the sign and magnitude of each variable in the model. An additional insight is also provided by analyzing the marginal effects, which were calculated as the partial derivatives of the non-linear probability function, evaluated at each variable sample mean.

Table 4.17: Marginal effect of SMEs Perception on Tax Compliance

Tax compliance	Margin Effect (dy/dx)	Robust Std. Err	Z	P< [Z]
Age	-0.0035	0.0044	-0.80	0.4240
Gender (1 if male, 0 otherwise)	-0.2037	0.1049	-1.94	0.0520
Education Dummy (1 if primary education, 0 otherwise)	-0.0419	0.1035	-0.40	0.6860
Marital Status Dummy (1 if married, 0 Otherwise)	-0.2180	0.1005	-2.17	0.0300
Household (Number of members in the household)	0.0702	0.0398	1.77	0.0770
Education (1if perceived higher on tax education, 0 otherwise)	0.0633	0.1226	0.52	0.6050
Tax rate (1 if perceived high tax rate, 0 otherwise)	-0.2550	0.0926	-2.75	0.0060
Penalty (1 if perceived high penalty, 0 otherwise)	0.4699	0.0931	5.05	0.0000
Fine (1 if perceived high fine, 0 otherwise)	0.2958	0.0938	3.15	0.0020
Government services (1 if high service provision, 0 otherwise)	0.6193	0.0818	7.57	0.0000

Source (Surveyed data, 2017)

CHAPTER FIVE

DISCUSSION OF THE FINDINGS

5.1 Introduction

This chapter presents the discussion of the finding of the study which includes demographic characteristics, perception of SMEs tax payers on business tax regulation towards compliance, perception of SMEs tax payers on Government Service delivery on tax compliance and perception of SMEs tax payers on tax education towards tax compliance. In attempt of capturing information for the study, survey questionnaires were distributed to respondents to respond to various questions. All questionnaires were filled by 160 respondents from Muheza and Tanga City council. Based on total number of SMEs, 49 respondents were from Muheza District and 119 respondents from Tanga City.

5.2 The perceptions of SMEs tax payers on tax compliance

The results of Logit regression model estimating SME tax payers Perceptions on tax compliance presented in table 4.17 shows the parameter estimates (coefficients) and marginal effects. The fit of the model was statistically significant at ($0.0000 < 0.01$) at 1% level of significance. The Pseudo R^2 had 0.5328. According to Verbeek (2012) Pseudo R^2 is also referred to as Mcfadden pseudo R^2 . Mcfadden pseudo R^2 is a measure that takes on values in the interval (0, 1). With regard to this study the results shows that Mcfadden pseudo R^2 is = 0.5328 which is equivalent to 53% implies that the specified logit model fits the data very well. This suggests that explanatory variables were able to explain tax compliance in the study area. The variables in the model were negative and positive statistically significant influencing tax compliance.

However, robust Standard Error was used to clear the problem of Heteroscedasticity. Before using robust Standard Error, some variables were not of significance. This means standard errors were large. To clear or to avoid violation of assumption of homoscedasticity, robust standard error approach was used to clear the problem of Heteroscedasticity.

5.2.3 Gender of respondents

Table 4.17 revealed that perception of SMEs tax payers on gender of respondent was negative and statistically significant influencing tax compliance at 10% level of significance. However, the null hypothesis (H_0) stated that there was no significant relationship between SMEs tax payers on gender and tax compliance. The gender had -0.2037 equivalent to 20.37% with P-value (0.0520) less than 10% level of significance. Hence the null hypothesis (H_0) was rejected which stated that there was no significant relationship between perception of SMEs tax payers on gender and tax compliance, and therefore the perception of SMEs tax payers on gender had significant relationship between SMEs tax payers on gender and tax compliance.

The finding revealed that being male SMEs tax payers was likely to decrease tax compliance as compared with female tax payer, provided that other factors remained constant. Possible explanation was that tax affects SME regardless of gender. It is supported by the study conducted by Baldry (1987) on his studies on gender and tax compliance found female to be more compliant than males in an experimental tax setting. Moreover the study conducted by Fallan (1999) reports on pre-test-post-test quas-experimental using university students studying taxation found that gender has predictive power in explaining an attitude changes in tax ethics while Kirchler *et al* (2008) found that men are more compliant than women.

5.2.7 Marital status of respondents

Table 4.17 revealed that perception of SMEs tax payers on marital status of respondent was negative and statistically significant influencing tax compliance at 5% level of significance. However, the null hypothesis (H_0) stated that there was no significant relationship between perception of SMEs tax payers on marital status and tax compliance. The marital status had -0.2180 equivalents to 21.80% with P-value (0.030) less than 5% level of significance. Hence the null hypothesis (H_0) was rejected which stated that there was significant relationship between SMEs tax payers on marital status and tax compliance. This implies that there is significant relationship between perception of SMEs tax payers on marital status and tax compliance. This reveals that perception of SMEs tax payers, on married spouse tax payer was likely to influence tax compliance as perceived by respondent, provided that other factors remained constant. Possible explanation was that marital status of a tax payer may be taken into consideration when negotiating the tax payment based on tax regulation. It can be evidenced by Ozdamar (2011) who found that marital status may have an influence in tax compliance where married spouses are more compliant than single tax payers due to the fact that psychologically married spouses are afraid of disturbance.

5.2.8 Household size of respondents

Table 4.17 revealed that perception of SMEs tax payers on household size of respondent was positive and statistically significant influencing tax compliance at 10% level of significance. However, the null hypothesis (H_0) stated that there was no significant relationship between perception of SMEs tax payers on household size and tax compliance. The household size had 0.0702 equivalents to 7.02% with P-value (0.0700) less than 10% level of significance. Hence the null hypothesis (H_0) was rejected which stated that there was no significant relationship between SMEs tax payers and household size towards tax compliance. This means that perception of SMEs tax payers on household size had significant relationship between perception of SMEs tax payers on household size and tax compliance. This finding reveals that perception of SMEs tax

payers on household size was more likely to influence tax compliance as perceived by respondent, provided that other factors remained constant. This means that an increase of house hold size increases number of tax payers.

5.2.9 Tax rate

Table 4.17 revealed that of SME tax payers had negative perceptions on tax rate and was statistically significant on tax compliance at 1% level of significance. However, the null hypothesis (H_0) stated that the perception of SME tax payers on tax rate had no significant relationship with tax compliance. The tax rate had 0.2550 equivalents to 25.50% with P-value (0.006) less than 1% level of significance. Hence the null hypothesis (H_0) was rejected which stated that perception of SME tax payers on tax rate had no significant relationship with tax compliance, and therefore the perception of SME tax payers on tax rate had significant relationship with tax compliance. This signifies that a high tax rate is less likely to influence tax compliance as perceived by respondent, provided that other factors remained constant. Possible explanation was that high tax rate perceived by tax payers as a burden to small and medium enterprises although it helps government to improve infrastructure for small, medium and large business. The present findings also supported by economic deterrent theory which stated when tax rate increase, the benefit of tax evasion increase (Cowell and Gordon, 1988). Similarly Nzioki (2014) found that an increase of tax rate lead to negative perception of tax payer toward tax payment.

5.2.10 Penalty

Table 4.17 revealed that of SME tax payers had positive perceptions on penalty and was statistically significant on tax compliance at 1% level of significance. However, the null hypothesis (H_0) stated that there was no relationship on perception of SME tax payers on penalty and tax compliance. The penalty had 0.4699 equivalents to 46.99% with P-value (0.000) less than 1% level of significance. Hence the null hypothesis (H_0) was rejected which stated perception of SME tax payers on penalty had no significant relationship with tax compliance and therefore the perception of SME tax payers on penalty had

significant relationship with tax compliance. This signifies that high penalty was more likely to influence tax compliance as perceived by respondent, provided that other factors remained constant. This may be explained that penalty creates burden to tax payers which forces tax payers to incur more cost in doing business. An increase of penalty lead to an increase of business cost which makes business owner to decide way of minimizing cost so that business can continue to operate. Cowell and Gordon (1988) in deterrent theory argued that an increase of penalty decreases the benefit of tax evasion. The present study conquers with Muturi and Michael (2015) who found that penalty increases compliance level among the tax payer.

5.2.11 Fine

Table 4.17 revealed that of SME tax payers had positive perceptions on fine and was statistically significant on tax compliance at 1% level of significance. However, the null hypothesis (H_0) stated that there was no significant relationship of perception of SME tax payers on fine and tax compliance. Perception of tax payers on fines had 0.2958 equivalents to 29.58% with P-value (0.002) less than 1% level of significance. Hence the null hypothesis (H_0) was rejected which stated that perception of SME tax payers on fines had no significant relationship with tax compliance and therefore the perception of SME tax payers on fine had significant relationship with tax compliance. This signifies that high fines were more likely to influence tax compliance as perceived by respondent, provided that other factors remained constant. This may be explained that fine creates burden to tax payers. The present finding complies with deterrent theory which stated that an increase of fine led to decrease tax evasion (Cowell and Gordon, 1988).

5.2.12 Government service delivery

Table 4.17 revealed that SME tax payers had positive perceptions on government service delivery towards tax compliance and was statistically significant on tax compliance at 1% level of significance. However, the null hypothesis (H_0) stated that the perception of SME tax payers on government service delivery had no significant relationship with tax compliance. The Government service delivery had 0.6193 equivalents to 61.93% with P-

value (0.000) less than 10% level of significance. Hence the null hypothesis (Ho) was rejected which stated that the perception of SME tax payers on government service delivery had no significant relationship with tax compliance, and therefore the perception of SME tax payers on government service delivery had significant relationship with tax compliance. This explained that perception of SME tax payers on government service delivery was more likely to influence tax compliance as perceived by respondent, provided that other factors remained constant. Possibly perception of SME tax payers on government service delivery seems to create good environment of business operators hence tax payer comply with tax regulation. Nyamweza et al. (2014) argued that when an individual is more satisfied with provision of public services they are likely to have high compliance attitude.

CHAPTER SIX

CONCLUSION AND POLICY IMPLICATIONS

6.1 Introduction

This chapter presents the conclusion and recommendations of the study. It commences with conclusion based on each specific objective of the study. Moreover, the recommendations are given thereafter and areas for further research follow.

6.2 Conclusion

The main purpose of the study was to assess the perceptions of small and medium enterprises on factors affecting tax compliance. However, from the discussion of findings of the study conclusion and recommendations are presented below.

The business income may not have impact on tax compliance level. Individual may have high income but may engage in non-compliance behavior due to negative perception on tax revenue utilization by the government. On the other hand a negative perception on tax rate was likely to influence high business income earners to avoid tax payment by even understating of their income for tax purpose. Similarly when SMEs tax payer became more satisfied with government services their perceptions on tax compliance changes positively and therefore the likelihood of tax compliance level increased. Fine and penalty was very important in influencing tax payer's perceptions. When the government increases fine and penalty the likelihood of tax compliance level tend to increase. This is due to fact that SMEs tax payers perceived the increased penalty and fines as they decrease the benefit of Tax evasion as recommended by the economic deterrent theory under this study. However household size and marital status are likely to have influence on tax compliance level where married spouses were likely to comply than unmarried spouses and respondent with high number of household size are likely to comply than the respondents with low number of household size.

6.3 POLICY IMPLICATIONS

The aim of this study was to assess the perceptions of small and medium enterprises on factors affecting tax compliance. The results of the study would be used to raise awareness among policy makers, regarding the impacts associated with each factor to SME tax payers. This will enable in coming up with relative policies to address the desired impact with the aim of increasing tax payment. Based on the findings of this study, the policy recommendation are as follows:

- i. The policy message that can be derived from this finding is that policy makers need to improve the institutional environment in the small and medium enterprise by increasing the risk of being caught. In order to widening the tax base and increase tax payment fines and penalty should be increased simultaneously.
- ii. Government should empower tax payers on engaging tax knowledge and tax system of Tanzania in order to create knowledge to them. Policymakers should continue to improve the institutional environment and business environment by enacting friendly laws to SMEs.
- iii. Government and Non-Government should train SMEs so as to increase knowledge and skills for improving their business in order to increase their revenues. The increase in SMEs revenue will enhance tax payment and finally tax non-compliance will decrease.
- iv. The tax authority should decentralize their services to the ward level in order to be aware with the business environment of small and medium enterprises and to reduce compliance cost. Currently TRA is decentralized to the districts level while some of the services are still provided at regional level.
- v. Tax authority should set tax rate at minimum rate in order to encourage tax payers to clearly declare their income for the tax purpose. To reduce Tax evasion respective tools should be employed which will encourage tax payers to comply as respective fines and penalties imposed to tax non-compliances.

6.4 Limitations to the study

Despite of the success of this research still numbers of problems were encountered during the study,

Cooperation from the respondents was insufficient. This is related with the thought of some of the respondents as they perceived to be suspected to tax avoidance and tax evasion. But with the given later from the university and convincing power of the researcher, most of respondents were cooperative as they understand that the study was for academic purposes and each information they provide will be confidential.

Time limit, there was a problem of time limit while respondents requires appointment for them to participate in research program, some were ready to participate but after working ours therefore the researcher used their required time to mitigate the problem

6.5 Area for further Research

While this study demonstrated perception associated with perceptions of small and medium enterprises on factors affecting tax compliance, it also found that tax payment and business records is an important factor for business development. Further studies on the area s how business records affect tax payment among small and medium enterprise in Tanzania. In addition future research should include estimates of SME profits which would help to better understand whether SMEs is particularly reliable to pay tax from profit gained. To generate the information required to assess the likelihood to invest in business records and tax exemption. Also, a key factor that affects adoption of various technologies is varied and excluded some potentially important variables such as to access the business records.

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APPENDICES

APPENDIX 1

QUESTIONNAIRES TO THE RESPONDENTS

Dear Respondent

I am a student of Mzumbe University (Masters of Science in Economics Policy and Planning) carrying out a research study that, assess the SMEs’ perception on tax compliance in Tanzania, using Tanga Region as the case study. The case study can help the government to identify the reasons that cause people to evade tax and assist tax collectors to establish methods of how to minimize tax evasion and tax avoidance to enhance Government revenue. You are therefore kindly requested to complete this questionnaire by ticking against the appropriate answer and by filling in the space provided. Your responses will be used only for research purposes and shall be just between you and I handled.

GENERAL INFORMATION ON LOCATION

- 1. Date of interview -----
- 2. District name -----
- 3. Ward name -----
- 4. Village/Street name -----
- 5. Enumerator’s name -----
- 6. Name of Respondent-----

PART A: GENERAL INFORMATION OF RESPONDENT

- 1.1 Age of the respondents
- 1.2 Gender of the respondent
 - a) Male
 - b) Female
- 1.3 Highest Education Qualification

- a) None or Informal education
- b) Primary education
- c) Secondary education
- d) College/University education

1.4 Marital status of respondent

- a) Single
- b) Married
- c) Widowed
- d) Divorced

1.5 Number of people in the Household of respondent.....

1.6 Monthly total individual income.....

1.7 Business Category.....

1.8 Where is your business located in Tanga?

- a) Tanga City
- b) Muheza

1.9 Which of the following best describes this business?

- a) Sole proprietorship
- b) Partnership []
- c) Limited Liability Company
- d) Other, please specify

1.10 How many workers have you employed in your business?

1.11 How much capital of your business in Tshs.....

PART B: BUSINESS REGULATION

2.1 What is your opinion about the current tax rate?

- a) Very high
- b) High
- c) Fair
- d) Low
- e) Very Low

2.2 Basing on any response given in (9) above is there any influence on tax compliance level?

- (a) Yes (b) No

2.3 Basing on your experience in business undertaking, does tax rate has any influence on tax compliance level?

- a) Yes
- b) No

2.4 If Yes/ No what is your opinion(s) -----

2.5 Are you aware of the penalties for tax evasion?

- a) Yes
- b) No

2.6 How do you rate the level of fines and penalties imposed by the tax authority?

- a) Very high
- b) High
- c) Fair
- d) Low
- e) Very Low

2.7 Does fine and penalties imposed by tax authority encourage tax payers to pay their tax liability?

- (a) Yes (b) No

2.8 Do you comply with tax rules and regulation?

- a) YES.
b) NO.

PART C: GOVERNMENT SERVICE DELIVERY

3.1 Does tax collected assist the government in provision of services?

- a) Yes
b) No

3.2 If yes in 15 what level of satisfaction are you getting from government services?

- a) Very high satisfied
b) Satisfied
c) fair
d) Low satisfied
e) Very Low Satisfied

3.3 Do you agree that improper accountability and utilization of Tax revenues by Government influence Tax Evasion in Tanzania?

- a) Strongly agree
b) Agree
c) Neutral
d) Disagree
e) Strongly Disagree

3.4 Government creates conducive environment to encourage small and medium enterprises to pay tax

- a) Strongly agree
- b) Agree
- c) Neutral
- d) Disagree
- e) Strongly Disagree

PART D: TAX EDUCATION

4.1 Do you have a formal knowledge in taxation?

- a) Yes
- b) No

4.2 How did you get formal knowledge of tax?

- a) School
- b) Seminars
- c) Magazines
- d) Television
- e) Other method -----

4.3 The tax education campaign increases compliance level

- a) Strongly agree
- b) Agree
- c) Neutral
- d) Disagree
- e) Strongly Disagree

4.4 For any response in 22 above; give any three opinions to support you choice.

- a) -----
- b) -----
- c) -----

4.5 As the business tax payer are you aware of fines and penalties imposed by the tax authority?

- a) Yes
- b) No

4.6 Tax payers knows tax system of Tanzania

- a) Strongly agree
- b) Agree
- c) Neutral
- d) Disagree
- e) Strongly Disagree

4.7 Based on your experience in business undertaking what are the common challenging issues that you have encountered to ward tax compliance?

- a) -----
- b) -----
- c) -----

4.8 What should be done in order to increase tax compliance among small and medium enterprises?

STATA OUTPUTS

```
. logit Tax_compliance Age Gender Education Marital Household Tax_Educ Tax_rate Penalty Fine
> G_services, robust
```

```
Iteration 0: log pseudolikelihood = -107.68187
Iteration 1: log pseudolikelihood = -53.571082
Iteration 2: log pseudolikelihood = -50.382366
Iteration 3: log pseudolikelihood = -50.30434
Iteration 4: log pseudolikelihood = -50.304148
Iteration 5: log pseudolikelihood = -50.304148
```

```
Logistic regression                               Number of obs   =       160
                                                    Wald chi2(10)  =       49.57
                                                    Prob > chi2    =       0.0000
Log pseudolikelihood = -50.304148                Pseudo R2      =       0.5328
```

Tax_compliance	Robust				
	Coef.	Std. Err.	z	P> z	[95% Conf. Interval]
Age	-.0179084	.0229386	-0.78	0.435	-.0628672 .0270504
Gender	-1.133785	.6820074	-1.66	0.096	-2.470495 .2029251
Education	-.2166646	.5383862	-0.40	0.687	-1.271882 .838553
Marital	-1.175205	.5410578	-2.17	0.030	-2.235659 -.1147517
Household	.3574837	.2005598	1.78	0.075	-.0356062 .7505736
Tax_Educ	.3155891	.5988899	0.53	0.598	-.8582136 1.489392
Tax_rate	-1.345995	.5058462	-2.66	0.008	-2.337436 -.3545547
Penalty	2.602907	.6035181	4.31	0.000	1.420033 3.785781
Fine	1.653465	.570461	2.90	0.004	.5353823 2.771548
G_services	3.849909	.7611039	5.06	0.000	2.358172 5.341645
_cons	-.7614125	1.447514	-0.53	0.599	-3.598487 2.075663

. mfx

Marginal effects after logit

y = Pr(Tax_compliance) (predict)
 = .73152584

variable	dy/dx	Std. Err.	z	P> z	[95% C.I.]	X
Age	-.0035171	.0044	-0.80	0.424	-.012134 .0051	43.3125
Gender*	-.2036772	.10492	-1.94	0.052	-.409309 .001954	.65
Educat~n*	-.0418677	.10348	-0.40	0.686	-.244677 .160942	.65625
Marital*	-.2180058	.10046	-2.17	0.030	-.414913 -.021099	.5875
Househ~d	.0702083	.03976	1.77	0.077	-.007722 .148139	3.03125
Tax_Educ*	.0633274	.1226	0.52	0.605	-.176967 .303621	.65625
Tax_rate*	-.2550427	.09263	-2.75	0.006	-.4366 -.073486	.5375
Penalty*	.4699093	.0931	5.05	0.000	.287437 .652381	.46875
Fine*	.2957825	.09376	3.15	0.002	.11202 .479545	.4
G_serv~s*	.61932	.0818	7.57	0.000	.459004 .779636	.43125

(*) dy/dx is for discrete change of dummy variable from 0 to 1

. linktest

Iteration 0: log likelihood = -107.68187
 Iteration 1: log likelihood = -51.094626
 Iteration 2: log likelihood = -50.39888
 Iteration 3: log likelihood = -50.301111
 Iteration 4: log likelihood = -50.30064
 Iteration 5: log likelihood = -50.30064

Logistic regression	Number of obs	=	160
	LR chi2(2)	=	114.76
	Prob > chi2	=	0.0000
Log likelihood = -50.30064	Pseudo R2	=	0.5329

Tax_compliance	Coef.	Std. Err.	z	P> z	[95% Conf. Interval]
_hat	.9980439	.1573757	6.34	0.000	.6895932 1.306495
_hatsq	.0053539	.0640925	0.08	0.933	-.1202652 .1309729
_cons	-.0138666	.3034222	-0.05	0.964	-.6085632 .58083