

Enhancing Income Tax Collection in SMEs: A Customers' Perspective

Enhancing Income Tax Collection in SMEs: A Customers' Perspective

By

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CERTIFICATION

We, the undersigned certify that we have read and hereby recommend for acceptance by the Mzumbe University, a dissertation entitled: **Enhancing Income Tax Collection in SMEs Customers Perspective: A Case of Tanzania Revenue Authority (TRA), Kinondoni** in fulfillment of the requirements for award of the degree of Masters of Science in Accounting and Finance of Mzumbe university.

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DEDICATION

This work is dedicated to my beloved parents (late Mr. and Mrs. Malima) for their basic education foundation they laid down for me. I wouldn't have reached this stage without their efforts. It is also dedicated to my lovely daughter Navoneiwa who missed me a lot during my study absence.

ABSTRACT

This study intended to find how the attitude of tax clients of taxation system can be enhanced. Generally, the study aimed to evaluate factors promoting income tax collection from SMEs. The following were specific objectives: To determine the extent to which SMEs voluntarily comply with income tax regulations in Tanzania, to determine the effectiveness of block system administrative approach in influencing SMEs Compliance, and identify factors mostly influencing the perception of SMEs on voluntary tax returns.

The literature of the study lead to the formulation of the following theories: Clients' Tax education status does not determines the rate of voluntary compliance by tax payers, the rate of client's visitation by tax officers does not relate to client's tax compliance status, Client's experience on business has no influence to voluntary tax compliance. The study used mixed research methods to test the hypotheses in meeting stated objectives. Data were collected through survey questionnaire, interview and the review of documents. The information was based on TRA Kinondoni tax region. Data were analysed through the use of SPSS Version 20.

The results of the study observed the following facts:-

- 1) the majority of customers were not registered to TRA
- 2) Both registered and unregistered clients have low awareness of tax laws.
- 3) There is a weak block system administration
- 4) The integrity of TRA staff significantly affects the compliance of clients with income tax return regulations.

TABLE OF CONTENTS

CERTIFICATION	i
DECLARATION AND COPYRIGHT	ii
DEDICATION.....	iv
ABSTRACT	v
TABLE OF CONTENTS.....	vi
LIST OF FIGURES	viii
LIST OF ABBREVIATIONS	x
CHAPTER ONE: INTRODUCTION AND BACKGROUND INFORMATION	1
1.1 Introduction	1
1.2 Background of the Study.....	1
1.3 Statement of the Problem.....	2
1.4 Objectives of the Study	3
1.4.1 Main Objective.....	3
1.4.2 Specific Objectives.....	3
1.5 Research Questions	3
1.6 Significance of the Study	4
1.7 Delimitation of Study.....	5
1.8 Significance of the Study	5
1.9 Scope.....	6
CHAPTER TWO: LITERATURE REVIEW	7
2.1 Introduction	7
2.2 The Concept of Income Tax.....	7
2.2.1 Income tax in Tanzania	9
2.3 The concept of Voluntary compliance in Taxation system.....	10
2.3.1 Indicators (measures) of voluntary compliance	11
2.3.2 Factors for non-compliance	12
2.3.3 Measures against income tax non- compliance.....	13
2.4 SMEs and Income Tax Returns.....	16
2.5 Factors Influencing Tax Returns by SMEs	21
2.6 The Importance of the Study.....	27
2.7 Conceptual Framework	27
2.7.1 Description of Variables	28
2.7.2 Hypotheses	29
CHAPTER THREE :RESEARCH METHODOLOGY	30
3.1 Introduction	30
3.3 Research Design.....	30
3.3 Study Area.....	30
3.4 Study population	31
3.5 Sampling Procedures.....	31
3.6 Data Collection methods	31
3.6.1 Interview	31
3.6.2 Questionnaire	32

3.6.3 Secondary data.	32
3.8 Method of Data Analysis	33
3.9 Data Reliability	33
CHAPTER FOUR: PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS	34
4.1 Introduction	34
4.2 Demographic Analysis.....	34
4.2.1 Gender	34
4.2.2 Education.....	35
4.2.3 Business experience.	36
4.3 Voluntary Compliance in TRA	38
4.4.1 Factors Influencing SMEs Voluntary submission of Tax Returns.....	40
4.4.2 Education Level	40
4.4.3 Business Experience.....	42
4.4.4 Training Status	44
4.4.5 Tax laws awareness.....	46
4.5 Block Management system	48
4.6 Perception of SMEs on voluntary tax compliance.	55
CHAPTER FIVE: CONCLUSIONS AND RECOMMENDATIONS	58
5.1 Introduction	58
5.2 Summary and Conclusion	58
5.2.1 SMEs voluntary compliance	58
5.2.2 Block Management administrative approach.....	59
5.2.3 Perception of SMEs on Voluntary Compliance.	60
5.3 Recommendations	60
5.4 Directions of the Study.....	60
APPENDICES	63
Appendix I: Questionnaire for Master’s Degree Course Research.....	63

LIST OF FIGURES

Figure 2.2: Conceptual Framework.....	28
Figure 4.1: Gender of Respondents.....	35
Figure 4.2: Education of Respondents	36
Figure 4.3: Business Experience	37
Figure 4.4: Tax Registration	39
Figure 4.3 Frequencies of Physical Visits to Clients by TRA Officers	50

LIST OF TABLES

Table 4.1: Registration Status * Voluntary Submission Cross tabulation	40
Table 4.2: Education * Voluntary Submission Cross tabulation	41
Table 4.4: Experience * Voluntary Submission Cross tabulation.....	43
Table 4.5: Experience * Voluntary Submission Chi-Square Tests	44
Table 4.6: Training Status * Voluntary Submission Cross tabulation	45
Table 4.7: Training Status * Voluntary Submission Chi-Square Tests	45
Table 4.8: Tax Laws Awareness * Voluntary Submission Cross tabulation	47
Table 4.9: Tax Laws Awareness * Voluntary Submission Chi-Square Tests.....	48
Table 4.10: Registration Status * TRA Visitation Cross tabulation	51
Table 4.11: Table 4.10 Registration Status * TRA Visitation, Chi-Square Tests.....	52
Table 4.12: Experience * TRA Visitation, Cross tabulation.....	52
Table 4.13: Experience * TRA Visitation, Chi-Square Tests	53
Table 4.14: Registration Status * Training Status Cross tabulation.....	54
Table 4.14: Registration Status * Training Status Chi-Square Tests	55
Table 4.15: Registration Status * Integrity Effects Cross tabulation	56
Table 4.16: Registration Status * Integrity Effects Chi-Square Tests	57

LIST OF ABBREVIATIONS

CULAS	Custom Application Online System
EFDs	Electronic Fiscal Devices
ITA	Income Tax Act
MOF	Ministry of Finance
PAYE	Pay As You Earn
SME's	Small and Medium Enterprises
TRA	Tanzania Revenue Authority
TZS	Tanzanian Shilling
VAT	Value Added Tax

CHAPTER ONE: INTRODUCTION AND BACKGROUND INFORMATION

1.1 Introduction

The research intended to evaluate the extent which clients of Tanzania Revenue Authority (TRA) voluntarily comply with tax regulations. The chapter begins by providing the background information of the study through highlighting conditions that influence voluntary compliance. In addition, it uses the available information to identify the problem under investigation. Similarly, the following subsections are also presented in this chapter; these include research objectives, research questions, limitations and delimitation of the study, and significance of the study.

1.2 Background of the Study

Revenue collection is an important determinant of the economy of any country. This is because these revenues support government operations that range from administrative activities to infrastructure constructions. Therefore it is the business of the government, to formulate the legislation which favors revenue collection activities. Together with proper management of other sources of government revenue (such as tourism, agriculture, industrial production, fishing and mining) the government needs a sound system to trap all revenue resulting from tax so as to make sound economic progress.

Recently, there has been an increase in the amount of revenue collected by the government of Tanzania; for instance, the rate of increase between 2007 and 2010 was 172% (Tanzania Revenue Authority, 2013). These results are influenced by different improvements in taxation system. Among changes adopted by the revenue authority of Tanzania includes increasing the number of staff, defining administrative blocks and the use of technological tools such as Electronic Fiscal Devices (EFDs), income Taxation (ITAX) system and Custom Application Online System (CULAS) .

Apparently, the income tax form one of the branches of taxation system of Tanzania. In this case, the collection of all eligible income tax is managed by Tanzanian Revenue Authority (TRA, 2012). While statistics shows the improvement in the area of tax collection; a large group of eligible tax payers is yet to be reached. A number of reasons are suggests why eligible tax payers fails to comply with this category of taxation, the most concomitant factor is the unprofessional method of keeping records by entrepreneurs (Makuya, 2013). Majority of SMEs are not professionally identifying their net income. Tanzania Revenue Authority (TRA) Officers are therefore obliged to make estimates based on standardised layout; to a certain extent this method is tedious and prone to errors since it depends on business owner's integrity and officers competency.

In order to reach more clients and act effectively, TRA have re-defined its administration system to include small administrative blocks. Although the key aim for re-defining TRA administrative structure is to maximize efficiency in identifying and managing new customers this goal is yet to be met (Bugeni, 2012). While, the main goal of TRA is to improve its revenue collection; this can be well enhanced through voluntary compliance of clients. However, it is unfortunately that majority of clients are not voluntarily returning tax to the authority (TRA, 2012). It is therefore necessary to determine measures necessary in promoting voluntary income tax returns.

1.3 Statement of the Problem

The Tanzanian government invests its efforts in making sure that activities in TRA are well administered. It is because of these efforts that there is an increase in the number of employees, increase in training seminars, re-defining administrative blocks and even transforming traditional methods of service provision to the use of electronic systems for service provision (TRA, 2012). It is evident that, there is a good progress in term of revenue collection by the Tanzanian Revenue Authority; however, different reports still

suggests the presence of many TRA clients who do not submit their tax return to the authority (Makuya, 2013).

The study by Jensen & Wöhlbier (2012) suggests voluntary compliance to tax return as the key success factor for the revenue authority to meet its collection goals while allowing citizens to meet their statutory obligations. The following things are important in promoting voluntary compliance; these include tax compliance education, enhancing transparent assessment and balancing employee roles in taxation process (Khalfan, 2010). Together with these factors, this study is designed to evaluate factors promoting income tax collection from SMEs in Kinondoni Tax Region

1.4 Objectives of the Study

1.4.1 Main Objective

This study aims to evaluate factors promoting income tax collection from SMEs.

1.4.2 Specific Objectives

The study was guided by the following specific objectives:-

- i.) To determine the rate of SMEs voluntary compliance with income tax in Tanzania.
- ii.) To determine the effectiveness of block system administrative approach in influencing SMEs Compliance.
- iii.) To identify factors mostly influencing the perception of SMEs on voluntary tax returns.

1.5 Research Questions

The study addressed the following specific Research questions:

- i.) To what extent are SMEs voluntarily returning income tax to the revenue authority?
- ii.) To what extent is the block administration approach effective in influencing SMEs compliance?
- iii.) What factors are most influential to the perception of SMEs towards voluntary tax return?

1.6 Significance of the Study

This study is significant in the following ways:

i.) To Taxpayers

This study provides the knowledge on benefits that taxpayers acquire when they voluntarily comply with tax laws. It also helped them to understand the importance of complying and effects of non-compliance to tax laws. Furthermore, the study provided a guideline on how conveniently they could file in their returns.

ii.) To Policy makers

The research provides policy makers with the knowledge on effectiveness of block administration system and the rate of tax compliance. This knowledge is necessary in formulating policies related to enhancing tax collection.

iii.) To Tax consultants

The research would help the consultants to understand the challenges that face taxpayers in complying with tax laws

iv.) To Academicians

The study provided more reference in the area of Revenue Collection; particularly in voluntary compliance of clients.

v.) To the Researcher

The study is a partial fulfillment of a Master Degree in Accounting and Finance

1.7 Delimitation of Study

The study focused on the factors Enhancing Income Tax Collection in SMEs basing on Customers' Perspective in Tanzania particularly at Tanzania Revenue Authority (TRA). Questionnaires and Interview were employed in the collection of the primary information used in the study. Secondary data were obtained from Tanzania Revenue Authority (TRA) as well as Ministry of Finance and Economic Affairs.

1.8 Significance of the Study

The study increases the knowledge of users on Enhancing Income Tax Collection in SMEs basing on Customers' Perspective, since the study gives highlight on the extent of SMEs voluntary compliance with income tax in Tanzania. Moreover the study determined the effectiveness of block system administrative approach in influencing SMEs Compliance. Indeed this study is useful for a country since it shows the factors mostly influencing the perception of SMEs on voluntary tax returns.

Furthermore; practically the study helps the government of Tanzania and TRA in general on enhancing Income Tax Collection in SMEs basing on Customers' Perspective. On top of that the study opens up a way for others to conduct further studies on the issues related on Enhancing Income Tax Collection in SMEs basing on

Customers' Perspective in Tanzania. On the other hand the study enables the researcher to meet one of a necessary condition of being awarded a degree of Masters of Science in Accounting and Finance.

1.9 Scope

This study explores factors influencing voluntary compliance by clients to tax returns. Geographically, it is conducted in Kinondoni Tax Region.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter reviews the literature relevant for the study. First it introduces the concept of taxation in Tanzanian and world context. It further discusses issues which promotes taxation activities. Finally, it formulates the framework for the study and the hypothesis to be tested.

2.2 The Concept of Income Tax

Income tax is a tax charged on income. Income can be profit or gain that is generated from businesses such as company, partnership, trust and individual businesses, also from employment and investment (Ministry of Finance, 2011) Income Tax is imposed by the government on all financial income generated by all entities within their jurisdiction. (Investopedia, 2013)

Taxation is the key source of revenue that governments in both developed and developing use to provide public services such as education, health care, water, security, roads, and social security to its citizenry.

Since the advent of income tax in 1909, there had been gradual changes with regard to the growth of economy which was partly supported with tax revenue. Before other taxes (which are not income taxes) were put into practice, income tax rate was very high because other sources of revenue to the government were very few. Up to 1960s, income tax rate was over 50% which contributed to 30% of the global revenue. But due to increase in industrial investment, there rates seemed to be unfavorable to investors, hence advanced countries, those in the Organization for Economic Cooperation and Development (OECD) started to re-think on how income tax rates can be lowered. Through tax reformation, other sources of revenue to the government were suggested to

be put into action. Between 2000 and 2010 income tax was minimized up to the average of 35% and the global economy started to grow up by 2% annually. (Hungerford, 2013)

Over the last decade tax performance in East African countries has significantly improved in nominal terms averaging about 24% of the size of the economy. Taking Kenya as an example, it has enabled the government to finance 60% of its budget. Of the total tax revenue collected by the government over the last decade, the largest contributors are income tax; about 40% followed by VAT at 28 %.(Mutua, 2012)

In other developing countries, tax noncompliance is a serious challenge facing income tax administration and hindering tax revenue performance. Despite the various tax reforms undertaken by governments to increase tax revenue over the years, prior statistical evidence has proven that the contribution of income taxes to the government's total revenue remained consistently low and is relatively shrinking (Alabede et al., 2011). However, from all the taxes, personal income tax has remained the most disappointing, inefficient, unproductive and problematic tax system (Asada, 2005; Kiabel&Nwokah, 2009; Nzotta, 2007; Odusola, 2006; Sani, 2005).

Taxpayers' behavior towards tax system has evoked great attention among many Revenue Authorities in the world especially in developed countries. However, it is debatable on what has been done towards the study of taxpayers behavior towards tax system in developing countries as they concentrate more in studies which would increase their budgets "bottom-line" in terms of huge revenue collection and enforcement efforts at the expense of studies on taxpayers behavior which would make increase in this tax revenue to be realized and enforcement efforts work.(Nkwe, 2007)

2.2.1 Income tax in Tanzania

Over the past fifteen years, Tanzania has embarked an ambitious and long process of economic, social and political reforms to increase economic growth and reduce poverty. Since the adoption of the World Bank/ IMF supported Economic Recovery Program (ERP) in 1986, the government of Tanzania has undertaken various policy reform measures, including trade and exchange rate reforms, banking and financial sector reforms, and reforms in agricultural marketing. It has also embarked up on a comprehensive tax reform process. While piecemeal reforms of particular taxes have been going on since the late 1960s, the Government appointed a Commission of Enquiry into Public Revenues, Taxation and Expenditure in October 1989 to study and review the central and local government tax systems and its administration, and make recommendations. In December 1991, the Tax Commission offered a proposal for reform of the Tanzanian tax system. The proposal shares several features with reforms that have taken place or are to be implemented in other countries since the mid-1980s. The Commission recommended reducing the marginal tax rates on personal and company income, to broadening the tax base by eliminating exemptions and to introduce more efficient enforcement mechanisms, to introduce measures to simplify the tax system. (Fjeldstad, 2005)

During the 1996/97, the Government fiscal policy was set to enhance revenue collection and improve expenditure management through expenditure control measures aiming at restraining the fiscal deficit. On the revenue side the measures that were implemented included the strengthening of tax administration through the establishment of the Tanzania Revenue Authority (TRA) under the TRA Act No.11 of 1995. In year 2004, Income Tax Act was issued to provide guidance upon income tax matters.(MOF, 2004)

Under the new tax administrative arrangement the government has achieved significant transformation in revenue mobilization through initiating several administrative measures aimed at streamlining it, modernizing systems and removing inefficiencies.

For example in 2003, the economy grew by 5.6% in real terms. Inflation has been reduced to 4.6% by March, 2004 (Budget speech, 2004/2005)

In Tanzania, income tax is imposed to individuals, partners in partnership, company and trust. Income tax law of Tanzania provides guidance upon all tax matters. The process of paying income tax starts with registration of taxpayer to obtain TIN (taxpayer identification number). TIN is provided freely to all taxpayers and the process of paying tax is voluntary. According to Income tax Act, all taxpayers are obliged to submit their business returns every year for tax assessment.

According to Kitilya, (2009), income tax contributes 30% of the total revenue collected in Tanzania. Whether is collected from small, medium or large scale business, formal or informal sectors, their contribution to output and value added in the revenue of the country is substantial.

Apart from raising a significant amount of revenue which funds government operations, other importance of income tax in Tanzania is, it contributes to the overall progressivity of the tax system to the extent that the tax burden falls on capital and not on laborers.

2.3 The concept of Voluntary compliance in Taxation system

Voluntary income tax is a system of compliance that relies on individual citizens to report their income freely and voluntarily, calculate their tax liability correctly, and file a tax return on time. (Government Accountability Office, 2005)

The income tax system in Tanzania operates on either self-assessment or assessed by tax officer basis. The first one is, the government expects taxpayers to determine their own tax obligations and to pay voluntarily whatever is due both regularly (through withholding from wages and through estimated tax payments, if necessary) and at year end (by filing tax returns and paying any additional balances due). By placing the onus

on taxpayers, the government avoids the costly alternative of determining each individual's tax liability and doing whatever it must to collect it. The later option, TRA officer provide assistance to taxpayer in determining tax obligation. This group of taxpayers is called presumptive.

According to Barnett and Grown (2004), tax policy is at the heart of the political debate on the level of public services that should be provided and who should pay for them because taxes are the principal source of recurring revenue under government control.

2.3.1 Indicators (measures) of voluntary compliance

Voluntary income tax compliance is probably determined by a wide variety of factors that interact differently for each individual. Although many such factors have been suggested, and several studies have focused on some of them, nothing has emerged to guide policy-makers concerning the relative merits of alternative approaches to improving compliance. This may be due in part to the fact that no comprehensive theory exists that explains the compliance behavior of taxpayers. It may also be because very little data are available to test such theories. For the purpose of this study, two factors were identified

a. Timely filling and reporting of return

Filing return is the process whereby taxpayer declares his income to Tax Authority for the purpose of determining his tax affairs. This is done once in a year at the first quarter. According to Fjeldstad, (2005), the measure of filing compliance or filing rate, is the ratio of the number of required returns actually filed to the total number required to be filed. Reporting noncompliance can occur either by underreporting income or overstating offsets to income (i.e., exemptions, adjustments, deductions and other credits such as refunds).

Income Tax Act of Tanzania requires every taxpayer to file return at the first quarter of each year. However, only 25% of registered taxpayers do comply with this. (ITAX, 2013). This ratio is very small and indicates that there is a high level of non-compliant taxpayers.

b. Timely payment of tax dues

Again, Income Tax Act of Tanzania, provide an option to taxpayer to pay his tax liability up to four equal installments per year. However TRA records shows that, only 27% do their payments on time. This ratio is too small and indicates the high level on non-compliance of taxpayers.

2.3.2 Factors for non-compliance

Tax complexity increases the likelihood that taxpayers are non-compliant unintentionally. When taxpayers make honest mistakes, enforcing taxes is harder because it requires distinguishing between cheaters and honest-but-confused taxpayers.

The implication of tax complexity is; first, it permits additional ways to shield income from tax and, consequently, complexity increases the overall cost of tax collection for instance, that tax system with a single rate is cheaper to implement than those with multiple rates. An example of this is tax avoidance.

Tax avoidance is the legitimate minimizing of taxes, using methods approved by tax authority. Businesses avoid taxes by taking all legitimate deductions and by sheltering income from taxes by setting up employee retirement plans and other means, all legal under tax laws, (Murray, 2013). For instance long time tax exemptions given to foreign investments. From this standpoint, penalties are a less appealing means of enforcement, and increasing the probability of detection becomes more costly.

Second, it encourages tax evasion if tax law contains a loophole to do so. Tax evasion is the illegal practice of not paying taxes, by not reporting income, reporting expenses not legally allowed, or by not paying taxes owed. Tax evasion is most commonly thought of in relation to income taxes, but tax evasion can be practiced by businesses on state sales taxes and on employment taxes. In fact, tax evasion can be practiced on all the taxes a business owes.

Lastly, complexity increases the likelihood that taxpayers make inadvertent mistakes in calculating their tax liabilities if there are many complex procedures for them to fulfill.

The ideal tax compliance policy should target to minimize all necessary ways that can attract taxpayer not to comply with tax laws. The loss of revenue implies an additional economic cost because the revenue must be recouped by resorting to further distortionary taxation while a loss of welfare occurs if there is a way to allocate the same resources in a way that makes a taxpayer better off. For example, in the context of tax evasion, a taxpayer would be made better off by receiving the expected gain from tax evasion directly rather taking a risk.

2.3.3 Measures against income tax non- compliance.

TRA's its mission is to be an effective and efficient tax administration which promotes voluntary tax compliance by providing high quality customer service with fairness and integrity through competent and motivated staff. It has therefore taken several steps to strengthen voluntary income tax compliance.

a. Minimization of revenue collection cost

As TRA is aware of the fast moving trends in technology including e-government and e-commerce, TRA is bracing itself for that to enable it to accept electronic filing (e-filing) and other forms of modern business conduct. TRA has prepared and is implementing an

ICT strategy that will guide TRA in embracing the technology trends. TRA has established its own website (www.tra.go.tz) where all information regarding its operations is posted. In order to reduce the cost of tax collection to both TRA and the taxpayers, TRA is implementing a system of collecting taxes through commercial banks since July 2004. To continuously simplify this process, as this is one of the main obligations of the TRA, efforts have also been made to reach out to businesses that need help to file their tax returns. For example, to assist trading companies complete their income tax returns, an online tax calculator was made available on TRA website. The online tax calculator contains a tax computation template with commonly used schedules. Taxpayers can use it to calculate their tax liabilities.

The realized benefits include lower cost of revenue collection to TRA and move to one bank account per region. Also this has improved convenience to taxpayers in making tax payments hence to increase compliance.

b. Integration of TRA operations

With effect from July 2005, TRA has integrated VAT and Income Tax Departments to form the Domestic Revenue Department. In these offices, a taxpayer makes one visit for all type of taxes at one TRA office. It should be noted that risk based management is being implemented and the reward for compliant taxpayers is expedited services. Hence TRA has one integrated regional office in each upcountry region and Zanzibar while Dar es Salaam has three tax regional offices.

c. Provision of high quality and responsive customer service

This is based on deeper understanding of taxpayers and the factors that shape taxpayers' compliance behavior and lay the groundwork for the development of targeted strategies that will encourage taxpayers to voluntarily comply rather than resist complying. TRA seek to understand the needs of taxpayers and to fine-tune processes to suit them. One key example is education programme which is customized to suit the needs of each trade or industry association. Seminars and workshops are conducted to educate taxpayers on

existing tax rules and explain new tax changes. Seminars are targeted to newly incorporated companies and SMEs that are not represented by tax agents. Education is provided to companies on basic tax principles and other essential information to help them comply with tax rules.

A more co-operative relationship between taxpayers and TRA is established which facilitates high levels of voluntary compliance. This relationship requires commercial awareness, impartiality, proportionality, openness and responsiveness by TRA and disclosure and transparency by taxpayers in their dealings with TRA.

In the context of this relationship, the disclosure expected by TRA from taxpayers includes the information that they are statutorily obliged to provide as well as any information necessary for the revenue body to undertake a fully informed risk assessment. This will include any transaction or position that can reasonably be considered to carry a material degree of tax risk or unpredictability. Transparency is the ongoing framework within which individual acts of disclosure take place.

d. Broadening tax base

Through establishment of block management system of which a study of geographical location of each block is carried out and all taxpayers to be registered in TRA system. Also liaise with other local authorities such as Ministry of land to get other information such as the values of properties that will enhance collection of tax from real estate. Other subscriber's information are such as pension schemes for PAYE tax purposes.

e. Improving staff competence, motivation, integrity and accountability

This is achieved through trainings to tax auditors on specialized sectors such as financial institutions, telecommunication and assess implementation of taxpayer segmentation including establishment of key operations in all districts and regions and introducing online systems to improve operational efficiency

f. Application of tax laws.

TRA works with the Ministry of Finance (MOF) to put in place a comprehensive set of tax policies that encourage taxpayers to comply with tax laws.

2.4 SMEs and Income Tax Returns

The SMEs nomenclature is used to mean micro, small and medium enterprises. It is sometimes referred to as micro, small and medium enterprises (MSMEs). The SMEs cover non-farm economic activities mainly manufacturing, mining, commerce and services. In the Tanzanian business environment, production processes of SMEs are firmly locally based. This means that factor inputs like raw materials, labour and even capital are procured from local suppliers. Apart from the factor inputs, markets for the outputs are also mainly destined for local markets and there is very little export activity.

There is no universally accepted definition of SME. Different countries use various measures of size depending on their level of development. The commonly used yardsticks are total number of employees, total investment and sales turnover.

In the context of Tanzania, micro enterprises are those engaging up to 4 people, in most cases family members or employing capital amounting up to Tshs.5.0 million. The majority of micro enterprises fall under the informal sector. Small enterprises are mostly formalized undertakings engaging between 5 and 49 employees or with capital investment from Tshs.5 million to Tshs.200 million. Medium enterprises employ between 50 and 99 people or use capital investment from Tshs.200 million to Tshs.800 million. (Ngasongwa, 2002)

Illustration: Table 2.1. CATEGORIES OF SMEs IN TANZANIA

Category	Employees	Capital Investment in Machinery (Tsh)
Micro enterprise	1 – 4	Up to 5 million.
Small enterprise	5 – 49	Above 5 - 200 million.
Medium enterprise	50 – 99	Above 200 - 800 million
Large enterprise	100 +	Above 800 million.

Source: Ministry of Industry and trade, Tanzania

SMEs all over in the world are known to play a major role in social economy development. This is apparently the case of Tanzania, where SMEs contribute significantly to employment creation, income generation and stimulation of growth in both urban and rural areas. Figures from Kitilya (ibid) show that the SME sector is biggest in Kenya (20% of GDP), followed by very far by Tanzania (3.8% of GDP) - 16.2% point difference or by a factor of 5.2 - then followed by Uganda (1.02% of GDP) and Rwanda (1.0% of GDP).

From the Haki Kazi study (2005) it is revealed that the SME sector in Tanzania presently accounts for about a third of Gross Domestic Product (GDP). There are about 1.7 million SME businesses. These employ about 20% of the workforce. The sector has a huge potential for creating employment, generating income, contributing to foreign exchange earnings and overall economic development and poverty alleviation.(Ngowi & Milanzi, 2006) Though data on the SME sector are rather sketchy and unreliable, it is reflected already in the above data that SME sector plays a crucial role in the economy

Despite of various interventions aimed at improving the business environment in Tanzania, the legal and regulatory framework is bureaucratic, costly and centralized. These characteristics of the legal and regulatory environment affect all sizes of

businesses adversely. However, SMEs are further constrained in this environment in comparison to larger businesses due to the disproportionately heavy costs of compliance arising from their size. As a result most of informal enterprises have failed to formalize and micro enterprises have been unable to grow and graduate into Small and Medium Enterprises.

The tax regime in Tanzania is unfavorable for SMEs development and therefore SMEs are said to be associated with tax evasion. Taxes are many, rather high and collected by various authorities including Tanzania Revenue Authority and the Local Government Authorities. Furthermore, entrepreneurs are ignorant of tax matters and the cost of complying with tax regulations is considered high. SMEs also feel that they are harassed by the tax authorities when the latter attempts to enforce tax compliance. Whereas taxation of businesses is a necessity for national economic development, the present tax regime imposes a major burden on SMEs. (Ngasongwa, 2002)

Besides the many and high tax rates, the mechanism to collect the same is not good for SMEs. While estimation of the tax to be paid is said to be unrealistically high, its collection has been enforced by use of force including involving the police. Another problem is that SMEs as do many other tax stakeholders do not see the benefits (value for money) of the tax that they pay. While the expectation is that tax revenues go towards improvement of the climate under which SMEs work, among other uses, this is generally not the case. For example infrastructure like roads, sewage systems and utility supplies to the SMEs' premises are either not present or in a very poor condition both in terms of quantity and quality. (Ngowi & Milanzi, 2006)

In order to determine income tax liability, every taxpayer is required to keep records of his business affairs and submit to TRA authority for assessment. The challenges facing Tanzania with respect to taxation of SMEs are in particular to those in the informal sector i.e identification, registration, non-compliance, poor or non-record keeping and

non-return filling. SMEs are said have problems in keeping proper information that may be required for tax assessment purposes. Information like sales volumes, sales revenue, profits and loss are generally not available and accessible. When available and accessible they are likely to be outdated and inadequate for proper decision-making. This is because either SMEs do not keep them or they do not keep correct information in order to, inter-alia, evade tax. It is argued for example that SMEs (arguably large firms too) have two books of accounts: one for the purpose of impressing bank officials during loan applications, and one for the tax authorities for the purpose of evading tax. The record book for the bank reports profits and the one for tax authorities reports losses. These challenges may be due to traders not having permanent business premises, displaying their businesses on the streets where they keep on shifting, the record keeping problem is mainly due to illiteracy on the part of the taxpayers (Kimungu & Kileva, 2007)

In order to tax SMEs the Tanzania Revenue Authority has engaged in various programmes with the objective to promote and enhance voluntary compliance, to detect and bring to net taxpayers who are not paying taxes or correct amount of tax. The programs include, taxpayer education and sensitization (through seminars, radio and television programmes, outreach to business places or trading centers, operating help desks and customer service, conducting secondary schools & colleges tax educational programmes, installation of educational and sensitization billboards also use of drama group to sensitize taxpayers).

Another is block management system (door to door survey), whereby it aims at putting in place sustainable methods and strategies of monitoring business activities of small and medium taxpayers (SMEs) with the view of making them pay tax in a cost effective way. The mechanism is, each block is allocated to a specific group of staff performance are measured against set targets. Blocks are categorized on the basis of geographical set

up or streets. Each block does all the tax function of registering assessing, collection and accounting for revenue.

Lastly, is presumptive approach of taxation. This is the one where the desired tax base is not itself measured but is inferred from some simple indicators (turnover, assets, farm size, shop size, etc.) which are more easily measured than the base itself. This system is normally designed for taxpayers that should not usually deliver invoices or similar documents.

In the presumptive taxation, the calculation of the taxable income takes into account the taxpayer's expenses such as living expenses for him and his dependants and expenses incurred for the acquisition of assets. When the declared expenses in the taxpayer's annual tax return outweigh his declared total income, then taxable income is calculated presumptively based on the above mentioned expenses. The taxpayer is asked to provide evidence for the purchase he has done. The resulting difference, if any, between the amount of expenses made and the income spent to finance them is considered income of the taxpayer and is taxable. (Weichenrieder, 2007)

SMEs may thus find paying taxes especially burdensome, while the tax authorities are likely to find it especially unrewarding to collect it from them. All this points to relatively low levels of both compliance and enforcement for SMEs, consistent indeed with the focus on larger taxpayers that, as noted above, has been so marked in recent years. Viewed more positively, it points to potential mutual gains, to taxpayer and tax authorities, from the development of simple schemes for taxing SMEs. (Aires, 2007)

2.5 Factors Influencing Tax Returns by SMEs

The taxpayers' attitude on compliance may be influenced by many factors, which eventually influence taxpayer's behaviour. Those factors which influence tax compliance and or non-compliance behaviour are differing from one country to another and also from one individual to another Kirchler, (2007). There have been many studies to explain the behaviour of tax compliance in a more realistic situation. These studies focused on the determinants of tax compliance, respectively on economic and non economic factors.

1. Economic factors of tax compliance

In the tradition of tax compliance research, a number of factors have been considered important for explaining tax compliance: the level of actual income, tax rate, tax benefits, tax audit, audit probabilities, fines and penalties.

The level of actual income. Spicer and Lundstedt (1976) point out that self-employed have more possibilities to avoid taxes than employed taxpayers. However, self-employed taxpayers have more opportunities for tax evasion and these opportunities might further increase with the number of different income sources. Hence, in tax compliance decisions the level of income might interact with its source. A different aspect of the income source, if income was earned by hard work or an effortless job - has been studied in experiments by Kirchler, Muehlbacher, Hölzl and Webley. Participants were less compliant when they reported income earned by low effort than when they reported hard-earned income. It seems that taxpayers are reluctant to lose their hard-earned money by “gambling” with tax authorities (Kirchler et al.,2007).

Tax rate. Within the current framework, the impact of the tax rate would depend on the degree of trust. When trust is low, a high tax rate could be seen as an unfair treatment of taxpayers, as an attempt at taking from the taxpayers what is rightly theirs. When trust is high, the same level of tax rate would be interpreted as contribution to the community,

which in turn again profits each individual. In the first case, the tax rate would be interpreted as the wielding of power by some tax offices and in the second case, as a joint agreement within the community (Kirchler et al., 2008).

Tax audit is one of the most effective policies to protect the behaviour of tax evasion. The level of tax audit can be determined by two elements: one is how many taxpayers are selected for audit and the second is how much intensive the audit is. The first element is easily measured by the number of audited taxpayers divided by the total number of taxpayers. However, the second element is so difficult to measure due to no published information about the process of tax audit. It is commonly measured by the first element to indicate the level of tax audit for practical comparison (Hyun, 2005).

Fines and penalties. In an antagonistic climate, fines and penalties can be a part of the game of “cops and robbers”, in a synergistic climate, they can be perceived as an adequate retribution for behavior that harms the community. Fines and penalties are therefore connected to trust and power. Fines and penalties that are too low could be perceived as indicator that the authorities are weak and unable to control the wrongdoers, undermining trust among honest taxpayers. Fines and penalties that are inappropriate because a taxpayer involuntarily made a mistake resulting from ambiguous tax laws, or that are exorbitantly high, would undermine the perception of retributive justice and induce tax evaders to try even harder to regain their “losses” incurred by those fines (Kirchler et al., 2008). The increasing tax avoidance and tax resistance due to an increase of fines and penalties puts into question how those should be assessed to be effective. On the one hand, fines and penalties should be high enough to decrease the expected value of tax evasion and to assure its deterrent effect on taxpayers. On the other hand, if they are too high, the tax system would be perceived as unjust and unfair and taxpayers would use any possibility to legally avoid their taxes. In most countries, fines are relative to the evaded tax.

2. Non- economic factors

Attitudes toward taxes. An individual's attitude towards tax system may predict his tax compliance behaviour. It is assumed that attitudes encourage individuals to act according to them. Thus, a taxpayer with positive attitudes toward tax evasion is expected to be less compliant than a taxpayer with negative attitudes. Attitudes towards tax evasion are often found to be quite positive (Kirchler et al., 2008). Individual attitudes toward compliance have been shown to be a function of social and cultural norms. If such attitudes would carry over to actual compliance, enhancing these norms, as through increasing overall trust in government, is a desirable policy instrument to complement the usual enforcement options. (Nkwe, 2013)

The attitudes are important for both the power and the trust dimension. On the one hand, favorable attitudes will contribute to trust in authorities and consequently will enhance voluntary tax compliance. On the other hand, attitudes towards the authorities will be relevant for the interpretation of the use of power as benevolent or malicious. Tax attitudes in general also depend on the perceived use of the money collected and therefore are connected to knowledge.

Norms. Besides attitudes, norms are important determinants of tax compliance. Behavioral intentions are determined also by subjective norms. Norms are behavioral standards on three different levels: the individual level, the social level and the national level. (Kirchler et al., 2008).

On the individual level, norms define internalized standards on how to behave. Individual norms are related to moral reasoning, authoritarianism and Machiavellianism, egoism, norm dependency and values. There is considerable overlap between individual norms, values and tax ethics. The more developed the moral reasoning or tax ethics, the more likely is voluntary compliance (Trivedi et al, 2003).

On the social level, norms are usually defined as prevalence or acceptance of tax evasion among a reference group (Wenzel, 2005). Social norms are related to the behavior of reference groups, for example friends, acquaintances or vocational group. If taxpayers believe that non-compliance is widespread and approved behavior in their reference group, they are likely to be non-compliant as well. The relationship between social norms and tax compliance is complex. Wenzel (2004) argues that social norms should elicit concurring behavior only when taxpayers identify with the group to whom the norms are ascribed. Taxpayers then internalize the social norms and act accordingly.

On the level of nation, norms become cultural standards, often mirrored in the actual law. Several authors suggest that trust in political leadership and administration will lead to voluntary tax compliance when favorable national norms are established (Fjeldstad, 2004).

In general, if the norms held by taxpayers favor tax compliance, voluntary tax compliance will result. Thus, norms encompass both power and trust. First, national norms find their expression in tax laws and the role given to tax authorities, having a direct influence on their power. Second, social norms such as the belief that tax evasion is a petty crime and widespread hinder the work of tax authorities, in particular when there is no countervailing norm of community. A norm where all citizens are perceived as contributing their fair share would certainly help to increase trust in the authorities (Kirchler et al., 2008).

Perceived fairness of tax system. This is another factor that affects tax return by most SMEs. (Rawlings, 2003; Taylor, 2003). A conceptual framework for fairness considerations suggests differentiating three areas of fairness, distributive justice, which refers to the exchange of resources, (both benefits and cost) procedural justice, which refers to the process of resource distribution, and retributive justice, which refers to the

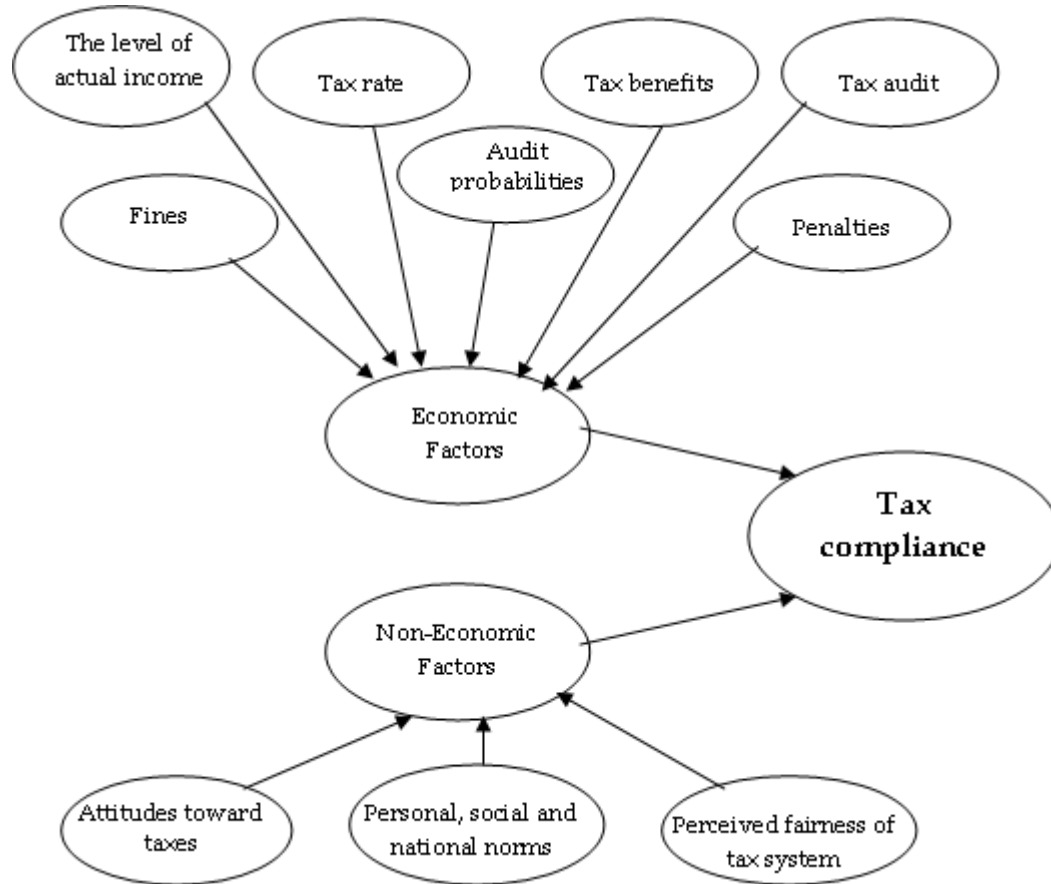
perceived appropriateness of sanctions in the case of norm-breaking (Kirchler et al., 2008).

Related to distributive justice, comparisons are made on the individual, the group, and the societal level. In both groups, taxpayers are concerned about the fairness of their outcomes, and they want to be treated relative to their merits, efforts and needs. If a tax burden of one individual or group or society is heavier than that of comparable other individuals or groups or societies, tax compliance is likely to decrease.

Related to procedural justice, the components essential for perceived fairness are neutrality of the procedure, trustworthiness of the tax authorities and polite, dignified, and respectful treatment. Comparisons again are made on the individual, group and societal level. On the individual level, taxpayers consider the treatment by the tax authorities, information provided, costs regarding compliance and administration, and the dynamics of allocation of revenues. It is argued that increased information related to tax law and explanations for changes can increase fairness perceptions of tax system. Perceived procedural justice on the individual level and a culture of interaction are important for building up trust (Job, Stout and Smith, 2007). On the group and societal level, taxpayers consider the neutrality of tax officers regarding subgroups, such as vocational groups or income groups. If tax authorities and officers treat taxpayers equally, in a respectful and responsible way, trust in the government and thus voluntary tax compliance is likely to increase on the individual, group and societal level. (Misu, 2011)

Related to retributive justice, unreasonable and intrusive audits and unfair penalties lead to negative attitudes toward the tax office and taxes in general (Wenzel and Thielmann, 2006). Thus, unfavorable retributive justice perceptions could lead to increased distrust and consequently to increased tax non-compliance.

Figure 2.3: Factors influencing tax returns by SMEs



Source: Barbuta-Misu, (2011)

2.6 The Importance of the Study

This study will enable tax authorities to identify and address the government problems encountered by taxpayers which make them to become non-compliant in returning tax as required by law.

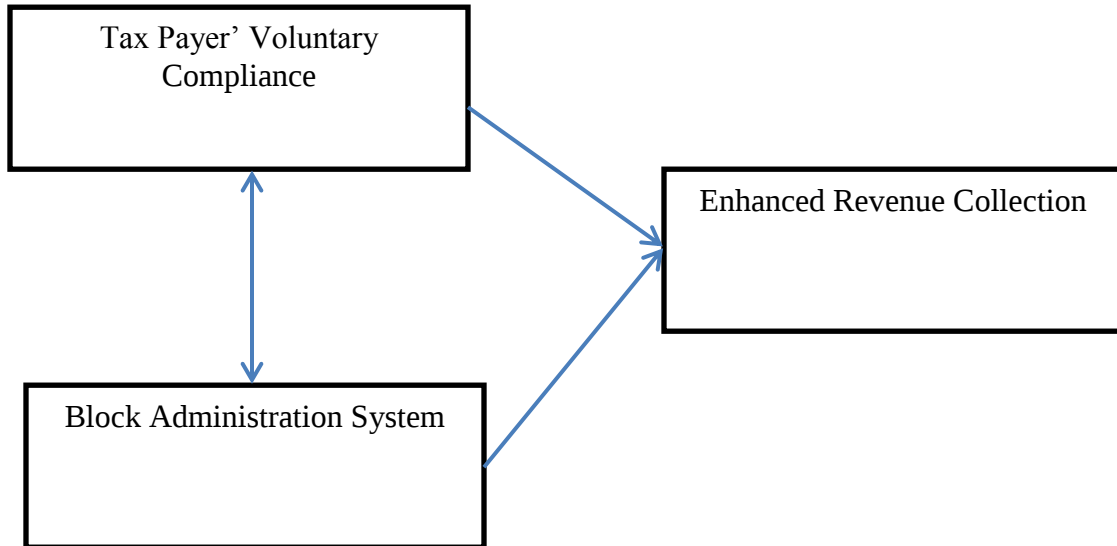
However, the study will help the government to shape tax policy and tax administration for the foreseeable future by looking at indirect behavioral response of taxpayers (as measured by changes in their voluntary filing of required income tax returns, and their reporting of income and offsets to income on those returns) to changes in TRA enforcement, TRA's responsiveness, and basic tax policies

To taxpayers, this study will help them to get understanding on the importance of them to comply with tax laws. It will help them to become patriotic since they know that the revenue collected is for the development of their own country.

2.7 Conceptual Framework

This section presents the framework that guides the implementation of the study. Figure 2.2 in below summarizes the framework. The framework includes the following independent variables; these are tax payers' voluntary compliance and block administration system. The dependent variable is the enhanced revenue collection.

Figure 2.2: Conceptual Framework



Source: Research (2013)

2.7.1 Description of Variables

This part provides explanation to variables of the study as identified in figure 2.1.

Tax Payers Voluntary Compliance

This is an attitude of SMEs of submitting their tax returns without being enforced. Taxpayer is said to be voluntary compliant if all information pertaining business are submitted to tax authority for tax assessment and computation, and taxpayer is willing to pay her obligation within timeframe indicated by tax laws. The attitude of voluntary compliance will enhance revenue collection because the cost of collecting tax will be minimized and taxes will be paid in time.

Block Administration System

This is TRA administration system whereby, taxpayers are grouped according to their geographical positions, for instance, wards can be blocks, while streets can be sub

blocks. Block administration helps in gathering statistics of taxpayers such as identifying new and existing taxpayers, identifying taxpayers who are registered with TRA, identifying non-filers of tax return for making follow up. By doing so, revenue collection will be enhanced.

Enhanced Revenue Collection

This variable is the summation of taxpayers' voluntary compliance variable and block administration system variable. It shows that, if there taxpayers are voluntary compliant and block administration system is effective, then revenue collection will be enhanced.

2.7.2 Hypotheses

This section presents hypothesis of the study. These hypotheses are formulated based on relationships of the conceptual framework in figure 2.1.

Hypothesis One

H₀: Clients' Tax education status does not determines the rate of voluntary compliance by tax payers

H₁: Clients' tax education status determine the rate of voluntary compliance by tax payers

Hypothesis two

H₀: The rate of client's visitation by tax officers does not relate to client's tax compliance status

H₁: The rate of client's visitation by tax officers relate to client's tax compliance status

Hypothesis three

H₀: Client's experience on business has no influence to voluntary tax compliance

H₁: Client's experience on business influence to voluntary tax compliance

CHAPTER THREE :RESEARCH METHODOLOGY

3.1 Introduction

Research methodology is the systematic way to solve the research problem. It may be understood as a science of studying how research is done scientifically. This chapter presents the methodology and procedures used in the study, which include research design, types of data, and methods of data collection, analysis and presentation.

3.3 Research Design

The research has been conducted at Tanzania Revenue Authority (TRA) using the case study design. This design was used to help the researcher to required, appropriate and adequate data to find out how to enhance Income Tax Collection in SMEs in Tanzania basing on Customers' Perspective. A case study is an depth comprehensive study of a person social group a community, an institute or any social unit, (Krinshnaswami, 1993). This case study design enables the researcher to be flexible in acquiring data as it employs more than one techniques, it uses historical method, employs interviewing, questionnaires, observation and documentary review.

This is a plan that specifies how data from the study was collected and analyzed. For the proposed study, a case study designed was applied to get the necessary required information. The case study design was chosen due to its ability to provide in-depth of the case to be studied.

3.3 Study Area

The study conducted at Tanzania Revenue Authority (TRA). The choice of study area was influenced by time and financial constraint that the researcher faced. Tanzania

Revenue Authority customers at Kinondoni Tax Region were used as the universe to obtain the sample.

3.4 Study population

The population of the study included SMEs and TRA employees located at Kinondoni tax region. Information studied based on how they voluntarily return their income tax.

3.5 Sampling Procedures

Sampling is the procedure of selecting a proper subset that can be used to make the inference to the population as a whole. It was difficult to probability sampling because the study could not succeed to establish a definite sampling framework. This is because the size of the population is not well known due to lack of records in TRA. The study used convenient sampling to obtain its sample and the sample size was 100 respondents.

3.6 Data Collection methods

The study utilized both primary and secondary data in collecting data. Therefore, data was collected through the use of structure questionnaire, personal interviews and documentary review.

3.6.1 Interview

Interview was conducted to collect qualitative information such as opinions and views of the study. Tanzania Revenue Authority customers were interviewed during data collection. The instrument has been used in order to supplement the questionnaires for more information. The advantages of using interview was quick method of gathering information, the researcher would know whether the respondents understand the questions and the method was not restricted to educated class alone.

3.6.2 Questionnaire

Is a pre-formulated written set of questions to which respondents record their answers, usually within rather closely defined alternatives (Kothari, 2001).

Questionnaires were open-ended questions, which allowed individuals to express their views concerning the factors which promote income tax collection from SMEs in Tanzania (see appendix I). The questionnaires were distributed to respondents aimed at getting information regarding the factors which promotes voluntary income tax collection from SMEs in Tanzania particularly at Tanzania Revenue Authority. One of the set of questionnaires was designed for Tanzania Revenue Authority customers.

3.6.3 Secondary data.

These are data obtained from literature sources or data collected by other people for some other purpose. These data provide second hand information and include both raw data and published ones. Some of data collected and stored by the organizations include details on the payroll, income statements and copies of letters and minutes of meetings, newspapers, journals and textbooks (Saunders et al, 200.) According to Kothari (2004), secondary data means data that are already been collected and analyzed by someone else.

Secondary data may either be published data or unpublished data. Published documents are books, magazines, newspapers, reports, public records and statistic, historical documents, technical and trade journals and various publications of foreign governments or international bodies and their subsidiary organizations. Unpublished documents are from diaries, letters, unpublished biographies and autobiographies, scholars and research workers, trade associations, labor bureaus and other public or private individuals and organizations. Advantages of secondary data are that it is cheap and inexpensive. It is

easily accessible. It is ready available. It saves time and efforts. It is unobtrusive. It avoids data collection problems and it provides a basis for comparison.

3.8 Method of Data Analysis

Findings have been presented by using statistical procedure/models such as tables and percentages, which were used to summarize the results in order to draw conclusion on factors which promote income tax collection from SMEs. The study applied both qualitative and quantitative analysis techniques. The researcher used Microsoft word and Excel in analyzing both primary and secondary data. With the use of Microsoft word and Excel the researcher was able to analyze the information from the findings quickly. The analysis was guided by research objectives and research questions. Also, the study used SPSS Version 20 for analysis guided by statistical modes. The statistical models used were Pearson Chi-square model and Spearman's rho correlation model.

3.9 Data Reliability

The study used Cronbach's Alpha to test the reliability of collected data. The tested question of the questionnaire showed that the overall reliability score is 0.75; this is greater than the suggested value of 0.70 (Deepak, 2012). This indicates a high degree of acceptable, consistent scoring for the different categories of the ordinal variables for this research.

CHAPTER FOUR: PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

4.1 Introduction

This chapter presents, analyze and discuss findings of the study. The analysis and discussion is based on responses from research questionnaires, interview questions and secondary data. The study intended to evaluate factors promoting income tax collection from SMEs in Tanzania, particularly at Kinondoni Tax region. The Main areas presented includes the characteristics of the sample, voluntary compliance in TRA, factors influencing voluntary compliance and perception of SMEs on voluntary compliance.

4.2 Demographic Analysis

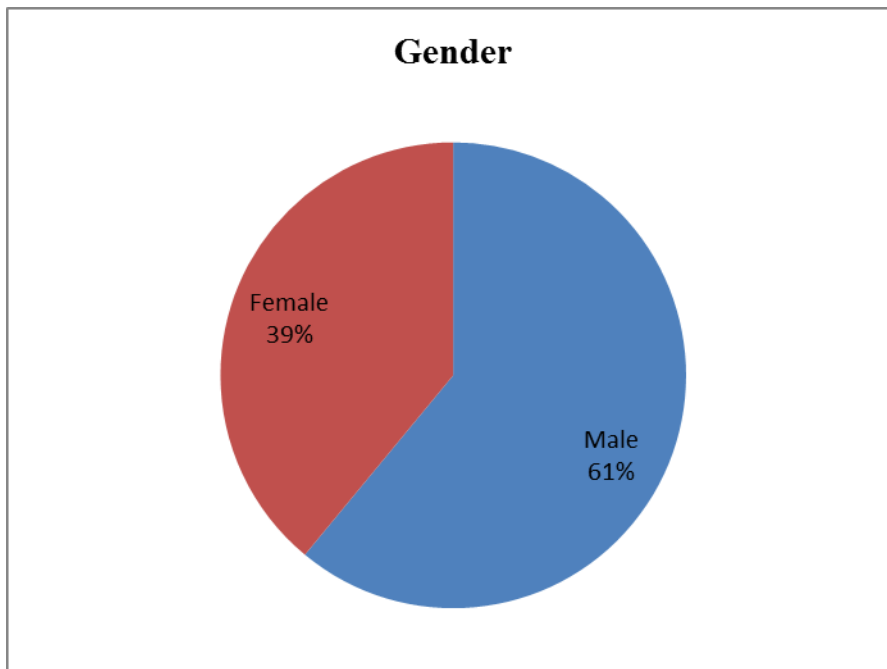
The study collected data from 100 respondents. In this section we studies general characteristics of the sample as obtained from Kinondoni tax region. The following aspects of the characteristics of the sample were studied; these included education level, business experience and gender. The following subsections discuss them in detail. The purpose is to understand how these characteristics relates with tax compliance behaviours shown by respondents.

4.2.1 Gender

Gender is part of demographic characteristic that were studied. It was necessary to know gender composition of this sample in order to determine the relationship that exists with tax compliance trend. Results presented in figure 4.1 shows that 61% are males and 39% are females. The information suggests that, there are more male SME owners than females. These results correspond to observations by Kilangi (2012) in his study on the usage of ICT in SMEs. It was observed that, there are more male business owners than females. This may be due to effects from the local culture women are mostly engaged in

taking care of domestic administration (Jabil, 2012). It is important to declare that, the observed ration do not affect general results of the study.

Figure 4.1: Gender of Respondents



Source: research data (2013)

4.2.2 Education.

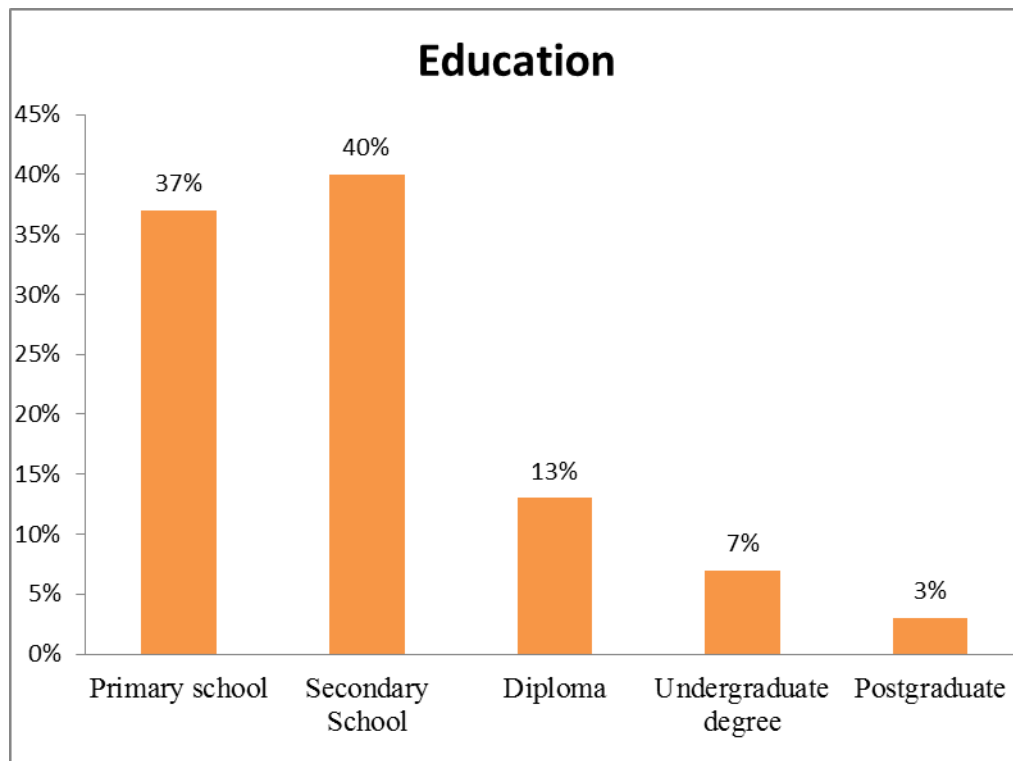
Education plays a great role in performance of the business since it enables traders to understand business matters such as opportunities, challenges, competition and strategies to overcome. This study included customers who possess different levels of education. Their level of education were categorized into primary school, secondary school, diploma, undergraduate degree and postgraduate. The aim was to find out the level of literacy within SMEs.

According to results presented in figure 4.2, majority of respondent have education level below diploma, this is about 90%. These findings compares with observation by

Mbwambo (2005) who observed that 92% of his SMEs had education level below ordinary diploma. The analysis shows a slight difference and this may have been caused by the increase of literacy in the past few years.

The above information suggests a low understanding of general business matters. Training would be valuable in improving the literacy of these respondents in business and taxation regulations.

Figure 4.2: Education of Respondents



Source: Research data (2013)

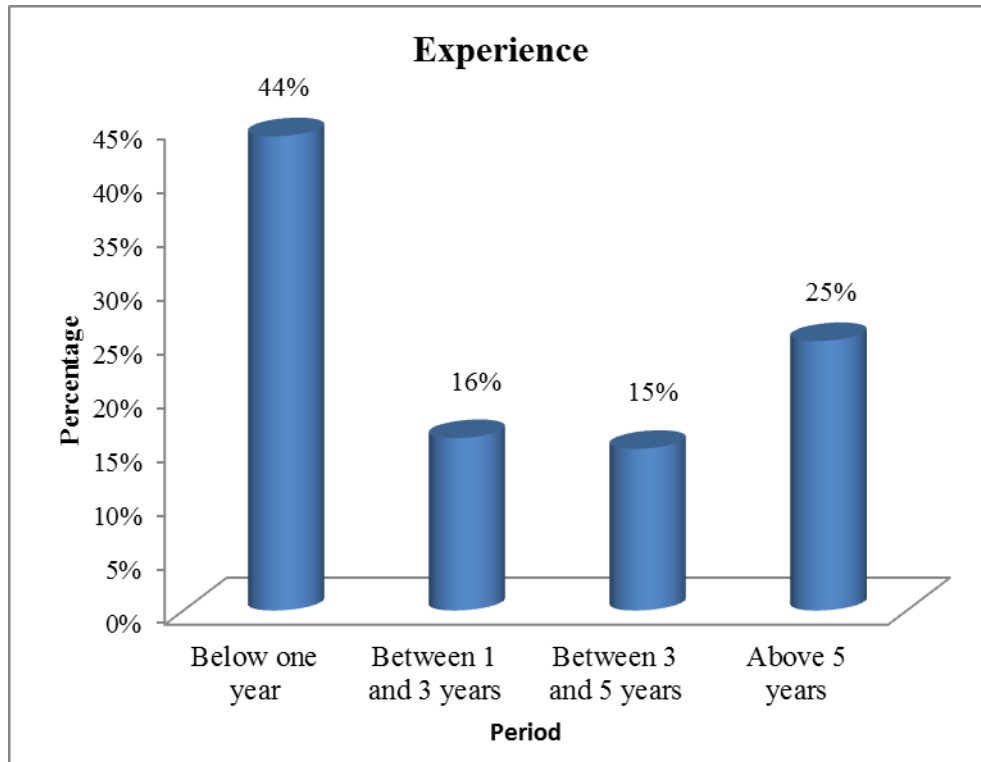
4.2.3 Business experience.

Findings by Khalfan (2010) suggested that business experience improve individual tax education. Experience develops knowledge in business education through receiving

formal and informal trainings from experts or practical work. This section studied respondents experience based on the period that an individual conducted business. The following categories of experience were studied; below 1 year, between 1 and 3 years, between 3 and 5 years, and above 5 years.

Findings presented in figure 4.3 shows that, a large number of respondents have business experience below one year; this is about 44%. Also, the study observed that, only 25% of all respondents have experience above 5 years in business. Results from the interview observed many people to have engaged in other business activities in previous. Factors such as stiff competition and inadequate capital forces majority of SMEs owners out of business within a short time. This suggests instability in small business activities. Similar study conducted by Musabila, (2010) indicated that most of SMEs have business experience below five years, he pointed out that there is intensive business competition in developing countries, Tanzania business environment is new in the economy, therefore economic changes do influence rapid emerge of new businesses.

Figure 4.3 Business Experience



Source: Research data (2013)

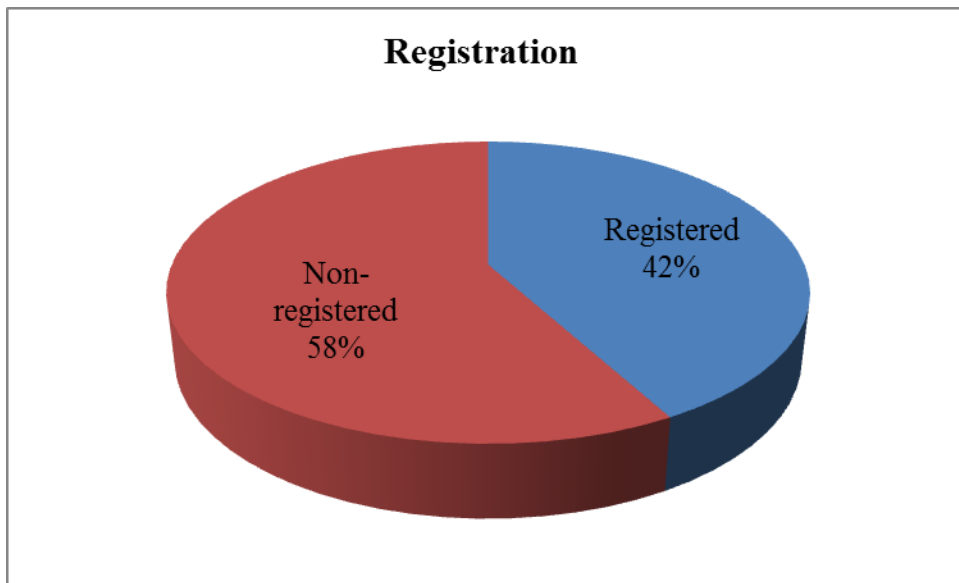
4.3 Voluntary Compliance in TRA

The findings obtained through interview suggested TRA desires business owners to submit information about their business voluntarily in every year. The reason is to assess the business to establish tax liabilities. It is unfortunate that, a number of authors reports inadequate submission of these information to tax authorities (TRA, 2013; Khalfan, 2010). However, the magnitude of the problem is not well established; therefore, it is the intention of this section to determine the degree of voluntary compliance by SMEs owners. Also, the study identified factors which mostly affect the compliance.

According to finding presented in figure 4.4, about 42% of respondents are registered with TRA. Based on this information, there are fewer businesses registered with taxation

authority. This information corresponds with comments by TRA officials who suggested that majority of business are not registered (Bugenyi, 2013; Nyachi, 2013; Interview).

Figure 4.4: Tax Registration



Source: Research data (2013)

On the other hand, the study determined the percent of clients who voluntarily files tax return. According to results presented in table 4.1, 76% of respondents registered with TRA files tax return consistently. Results from the interview suggested that, clients were reluctant to pay tax as required because it has less impact to developments of the country. On other hand responses from TRA officers showed that, TRA clients lack adequate tax education on tax affairs.

Table 4.1: Registration Status * Voluntary Submission Cross tabulation

		Voluntary Submission			Total
		Every Year	Inconsistent ly	No Submission	
Registration Status	Registered	32	3	7	42
	Not Registered	0	0	58	58
Total		32	3	65	100

Source: Research data (2013)

4.4.1 Factors Influencing SMEs Voluntary submission of Tax Returns.

The literature identified a number of factors to influence voluntary compliance in the Tanzanian SMEs. In this section, the study determines the statistical significance of these factors in influencing voluntary tax returns. Recalling from table 4.1, it was observed that 29% of respondents registered with TRA are not submitting tax consistently, and only 32% of the whole sample do submit tax voluntarily. The following factors are studied; gender, education, business experience, training status, and tax laws awareness.

4.4.2 Education Level

Under this section, the purpose was to determine whether the level of education of taxpayers do influence their attitude of voluntary compliance with tax laws. The chosen sample included taxpayers with different levels of education. For the purpose of this study, two groups of taxpayers were considered; those with education below diploma (primary and secondary education) and other group was taxpayers who possess college

and university education (diploma, bachelor degree and postgraduate degree). Table 4.2 below indicates how these two groups behave towards voluntary compliance with tax return.

Table 4.2 Education * Voluntary Submission Cross tabulation

Count

		Voluntary Submission			Total
		Every Year	Inconsistently	No Submission	
Education	Primary School	10	1	26	37
	Sec School	14	1	25	40
	Diploma	3	0	10	13
	Bachelor Degree	3	1	3	7
	Postgraduate Degree	2	0	1	3
Total		32	3	65	100

Source: Research data (2013)

The results presented in the table above shows that, 31% of respondents with primary and secondary education do submit their returns every year. These results closely compares with those who had the opportunity to obtain college education (that is diploma and above). The study observed that, 35% of respondents with at least diploma education do also submit their returns every year. The information shows the difference of 4% between the two groups.

Additionally, the study conducted an analysis to determine whether the above observed difference is significant. The study used Pearson chi-square model for analysis. Results presented in figure 4.3 indicate that, the p-value is 0.529, p is greater than 0.05. Based

on these results, there is no significant difference in tax compliance between respondents with different levels of education. This result affirms the descriptive statistics in the above paragraph, where a very small difference was observed in the percent of respondents who voluntarily files their tax between respondents with a formal college education and those without college education.

Table 4.3 : Education*Tax Compliance - Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	7.074 ^a	8	.529
Likelihood Ratio	6.033	8	.644
N of Valid Cases	100		

Source: Research data (2013)

According to results obtained through interview, the indifference observed in compliance of respondents to tax return is due to the nature of SMEs businesses, whereby most of them are simple and do not require high skills. In Tanzania, starting of an SME business does not require many legal procedures. This simplicity influences most of them to evade tax laws regardless of the education level they possess.

4.4.3 Business Experience

The purpose of this section was to examine the relationship between experience in business and the voluntary compliance of SMEs. Traders who have conducted business activities for quite a long time seem to have a better understanding of their business environment in which they operate than those with little experience. These environments include country laws and regulations associated with business operations. This study tested categories of business experience as follows; SMEs with experience below a year, between one and three years, between three and five years. Table 4.4 shows the results.

Table 4.4 Experience * Voluntary Submission Cross tabulation

		Voluntary Submission			Total
		Every Year	Inconsistently	No Submission	
Experience	Below One Year	5	1	38	44
	Between 1and 3 Years	9	0	7	16
	Between 3 and 5 years	5	1	9	15
	Above Five years	13	1	11	25
Total		32	3	65	100

Source: Research data (2013)

Results from the table above shows that registered SMEs with business experience above three years are the one who consistently submit their tax returns every year (45%), while 23% of SMEs with business experience below three years also do submit their return every year. From percentage difference, experienced SMEs seemed to comply mostly with tax return submission. This indicates that there is a strong relationship between experience in business and voluntary compliance of tax returns.

Furthermore, analysis through Pearson Chi-square test was applied to verify the significance of the difference obtained in the first observation. Result presented in Table 4.5 shows p-value of 0.004 ($p < 0.05$). This indicates that the observed difference in voluntary compliance between SMEs with business experience above five years and those with experience below one year is significant.

Table 4.5 Experience * Voluntary Submission Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	19.197 ^a	6	.004
Likelihood Ratio	20.479	6	.002
N of Valid Cases	100		

Source: Research data (2013)

Observed factor from interviews which contribute the attitude of voluntary compliance was, experienced SMEs seemed to be aware with tax laws and procedures, through trainings, seminars and regular visits by TRA officers compared to new SMEs who had few number of visits and trainings from TRA.

4.4.4 Training Status

Another factor seems to contribute voluntary compliance of tax return which the study examined was training status. TRA has a department for taxpayers' education, whose duty is to ensure that tax education is reached to the customer. This department provides tax education in form of leaflets, brochures, advertisements and organizes numerous periodic trainings to TRA customers. The aim is, to enable its customers to obtain understandings pertaining tax laws. Despite of all these efforts, few customers do attend these trainings and read materials provided.

Under this section, the study aimed on examining the extent of voluntary compliance between trained and untrained customers. Table 4.6 below shows the results.

Table 4.6 Training Status * Voluntary Submission Cross tabulation

Count

		Voluntary Submission			Total
		Every Year	Inconsistently	No Submission	
Training Status	Trained	23	0	9	32
	Untrained	9	3	56	68
Total		32	3	65	100

Source: Research data (2013)

From results presented in the table above, it reveals that, 23% of trained customers are voluntary submit their returns every year, while 9% of untrained customers do also voluntary submit their returns every year. This indicates that, trainings offered by TRA to SMEs have a great influence to them towards voluntary compliance attitude.

Similar other results were obtained through Pearson chi-square test whereby the p-value was 0.00 ($p < 0.05$). This shows that, the difference in the level of compliance between trained and untrained SMEs is significant.

Table 4. 7 Training Status * Voluntary Submission Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	34.639 ^a	2	.000
Likelihood Ratio	35.069	2	.000
N of Valid Cases	100		

Source: Research data (2013)

Results from interviews, suggested the reason for the difference between two groups is because trained customers do possess' higher understanding of tax laws and they know the importance of adhering to them compared to untrained one.

4.4.5 Tax laws awareness

The aim of this part is to identify whether tax laws awareness in SMEs influence voluntary compliance of tax payers by filing tax returns on time. In order to determine the level of awareness, the sample of respondents were grouped as follows; those who were highly aware, moderately aware, aware and highly not aware.

From the results presented in table 4.8 below, it shows that 32% of registered respondents who have an understanding of tax laws do submit their returns every year, while there 0% of submission of returns by respondents who do not know tax laws. This indicates that, awareness of tax laws plays a great part in influencing SMEs to submit their returns.

Table 4.8 Tax Laws Awareness * Voluntary Submission Cross tabulation

Count

		Voluntary Submission			Total
		Every Year	Inconsistently	No Submission	
Laws Awareness	Highly aware	7	0	0	7
	Moderately aware	15	1	9	25
	Aware	8	1	11	20
	Not aware	2	1	29	32
	Highly not aware	0	0	16	16
Total		32	3	65	100

Source: Research data (2013)

Further results were obtained through using Pearson chi-square test (Table 4.9 below); these results showed that, the showed p- value to is 0.000, and the value is less than 0.05. This indicates that there is a strong relationship between voluntary submission of tax returns by SMEs and the the level of awareness of tax laws.

Table 4.9 Tax Laws Awareness * Voluntary Submission Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	43.773 ^a	8	.000
Likelihood Ratio	52.277	8	.000
N of Valid Cases	100		

Source: Research data (2013)

From these findings, the group with good tax education do also have a large percent of those who comply with voluntary tax submission than those who have no tax education. TRA has a department for taxpayers' education, whose duty is to ensure that tax education is reached to the customer. This department provides tax education in form of leaflets, brochures, advertisements and organizes numerous trainings to TRA customers. Despite of all these efforts, few customers do attend these trainings and read materials provided. Unawareness to tax laws has lead majority of customers to be subjected to fines and penalties by conducting mistakes unknowingly for instance, using TIN certificates that are for non-business purposes, or try to evade paying tax by not registering with TRA.

4.5 Block Management system

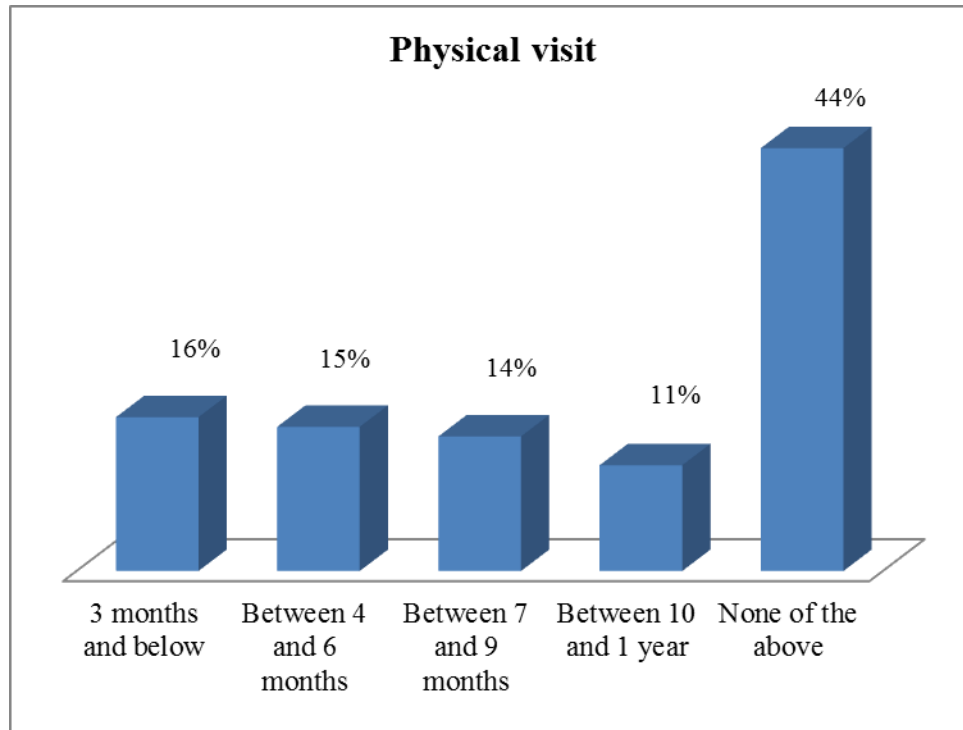
In 2011, TRA established a block system to decentralize the management of tax affairs; one of expected results of this management system is to influence voluntary compliance to tax payers through dissemination of taxpayers' education. Under this system, tax regions have been divided into blocks and sub-blocks depending on geographical areas. Customers are registered and categorized according to blocks and sub-blocks. Services given to customers, example TIN registration, physical visits, filling of returns, audits, and trainings are done according to blocks and sub-blocks in which the customer belongs.

The purpose of block management system is to simplify the work of reaching customers and collection of necessary business information for tax purposes. In managing blocks, TRA officers are assigned a duty of visiting their block customers at least once in three months to collect business information, identifying non-filers, non-registered customers and ensure that all businesses are registered, information are well updated in TRA system and all taxes are paid by businesses accordingly (TRA, 2013) .

This study determined the effectiveness of block management system in increasing the number of visits by TRA officials and the adequacy of trainings provided to customers.

Traditionally, TRA expects individual clients to be visited by their officers at least once in every three month. This is because income taxes are also payable with accordance to at least four installments in a year. Therefore four visits are expected in every year. According to descriptive results presented in figure 4.3, only 16% of respondents are regularly visited by TRA officers. The results suggest that, few clients benefits from regular inspection according to TRA traditions.

Figure 4.3 Frequencies of Physical Visits to Clients by TRA Officers



Source: Research data (2013)

It was also observed that about 44% of respondents have never been visited by TRA officers. This suggests that, the potential of block system is not adequately explored by TRA employees.

A further analysis was conducted to determine the influence of registration status of clients to the frequency which employees visit them. Results presented in table 4.10 observed that, 23% of respondents registered with TRA were visited according to TRA established tradition. Again, 10% of those who are not registered are visited accordingly. The information suggests that TRA officials dedicate more visits to clients who are already registered than new ones. This may significantly impact the efforts of the institution to increase the number of new clients. Results from the interview suggested that, this is due to inadequate manpower and facilities such as means for transport.

Table 4.10 Registration Status * TRA Visitation Cross tabulation

Count

		TRA Visitation					Total
		3 month and below	Between 4 and 6 month	Between 7 and 9 month	Between 10 month and One year	None of Above	
Registrati on Status	Registered	10	7	7	8	10	42
	Not Registered	6	8	7	3	34	58
Total		16	15	14	11	44	100

Source: Research data (2013)

An additional analysis was conducted to show whether, the registration status of respondents significantly relate to the frequency which they were visited by TRA officer. The purpose is to affirm results presented in table 4.10. The study used Pearson chi-square model. In the analysis presented in table 4.11the study observed that, the p-value is 0.007; this value is less than 0.05. Therefore there is a significant relationship between respondents' registration status and the frequency which they are visited by TRA officers. These results support results from the cross-tabulation in table 4.10. It is shown that, clients who are registered with TRA are frequently visited officer than those who are not registered.

Table 4.11: Table 4.10 Registration Status * TRA Visitation, Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	14.235 ^a	4	.007
Likelihood Ratio	14.697	4	.005
N of Valid Cases	100		

Source: Research data (2013)

Furthermore, it was the intention of the study to test the relationship between respondent's business experience and the frequency which they are visited by TRA officers. Results presented in table 4.12 shows that, 20% of respondents with business experience of less than 3 years and 10% of those with above 3 years' experience are visited accordingly. This is likely because the emphasis in in visiting new business to educate and ensure that they comply with TRA regulations.

Table 4.12: Experience * TRA Visitation, Cross tabulation

Count

		TRA Visitation					Total
		3 month and below	Between 4 and 6 month	Between 7 and 9 months	Between 10 months and 1 year	None of Above	
Experience	Below One Year	10	5	2	1	26	44
	Between 1 and 3 Years	2	1	1	4	8	16
	Between 3 and 5 years	1	3	6	1	4	15

	Above Five years	3	6	5	5	6	25
Total		16	15	14	11	44	100

In a further analysis to determine the association between business experience and the frequency of visitation, the study observed that there is a positive significant association between the two variables. The observed p-value is 0.002 and the value is less than 0.05. The information suggests a significant difference in the frequency which respondents are visited by TRA officials between respondents with short time experience and those with a significant experience. It is observed that a significant effort to visitation is dedicated to employees with low experience than those with significant experience.

Table 4.13: Experience * TRA Visitation, Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	30.319 ^a	12	.002
Likelihood Ratio	29.936	12	.003
N of Valid Cases	100		

Source: Research data (2013)

On the other hand, the study examined the adequacy of training offered by TRA as one of the purposes of block management. Interview made to TRA officials suggested that, these trainings are arranged periodically, and are provided freely to all traders, both registered and non-registered with the aim of emphasizing on the importance of voluntary compliance with tax returns and to provide understanding of tax matters pertaining to business. (Makuya, 2013).

According to results presented in Table 4.14 below, it has revealed that 57% of registered respondents have received tax trainings, while 14% of unregistered ones were

also found to obtain tax trainings. The difference between these two groups indicates that, unregistered taxpayers are more reluctant than registered ones. The reason might be high level of illiteracy which convince them not to give priority to attend those trainings and adhere to tax regulations.

Table 4.14: Registration Status * Training Status Cross tabulation

Count

		Training Status		Total
		Trained	Not trained	
Registration Status	Registered	24	18	42
	Not	8	50	58
	Registered			
Total		32	68	100

Source: Research data (2013)

Similarly, a comparable analysis was made using Pearson Chi-square test. Again p-value obtained was 0.000 which is less than 0.05. This indicates that the relationship in adequacy of tax trainings offered by TRA towards registered and unregistered customers is significant.

Table 4. 14: Registration Status * Training Status Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)	Exact Sig. (2- sided)	Exact Sig. (1- sided)
Pearson Chi-Square	21.037 ^a	1	.000		
Continuity Correction ^b	19.092	1	.000		
Likelihood Ratio	21.472	1	.000		
Fisher's Exact Test				.000	.000
N of Valid Cases	100				

Source: Research data (2013)

4.6 Perception of SMEs on voluntary tax compliance.

Despite of the efforts by TRA to educate taxpayers on the importance of voluntary compliance with tax return, making physical visits and invite them to attend trainings, majority of SMEs seem not to respond. Analysis shows that there still huge number of SMEs who are not registered with TRA and who do not submit their returns (non- filers) as required by tax law. It is the purpose of this section to identify factors mostly influencing the perception of SMEs on voluntary tax compliance. This study examined to see whether the integrity of TRA staff affects the perception of customers towards voluntary compliance. See table 4.15 below.

Table 4. 15 Registration Status * Integrity Effects Cross tabulation

Count

		Integrity Effects					Total
		Highly affecting	Affecting	Moderately affecting	Not affecting	Highly not affecting	
Registration Status	Registered	7	9	11	10	5	42
	Not Registered	7	6	21	7	17	58
Total		14	15	32	17	22	100

Source: Research data (2013)

Results from the table above indicate that 36% of registered respondents are not affected by the integrity of TRA staff. Also, for no-registered respondents, 41% agreed not to be affected as well. This means that, integrity of TRA officials has no influence on the perception of customers towards voluntary compliance. Results from interview revealed that, taxpayers' education has not yet reached to majority of customers; most of SMEs seem to be unaware with tax laws. Others are reluctant because they feel that, their taxes do not benefit them in terms of country development as a whole.

Another comparable analysis was done using Pearson Chi-square test. Results presented in table 4.16 showed that, p-value is 0.076 which indicates that there is no significant influence of TRA staff integrity towards voluntary compliance attitude of customers.

Table 4.16: Registration Status * Integrity Effects Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	8.456 ^a	4	.076
Likelihood Ratio	8.659	4	.070
N of Valid Cases	100		

Source: Research data (2013)

CHAPTER FIVE: CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

In this study we concentrated in evaluating SMEs' voluntary compliance to tax laws.. The findings of the study were categorized in three main aspects, these include the rate of voluntary compliance in TRA, Impacts of block management to voluntary tax submission and the perception of SMEs in tax compliance. This is because, ss businesses increase, the government expects more earnings through taxation; however, this is lowly attained in Tanzanian SMEs.

Following the results of the study, this section summarizes the findings and suggest relevant conclusions to the study. It also offer recommendations and the way forward in enhancing tax compliance.

5.2 Summary and Conclusion

The focus of the study was to evaluate factors promoting voluntary tax compliancy in TRA. The study was divided to three research objectives which aimed to determine the extent of SMEs voluntary compliance with income tax in Tanzania, to determine the effectiveness of block system administrative approach in influencing SMEs compliance, and finally evaluate factors mostly influencing the perception of SMEs on voluntary tax returns. The summary and conclusion arrived for each objective is stated in the below sections.

5.2.1 SMEs voluntary compliance

The study was influenced by efforts invested by TRA in making sure that tax payers comply with tax regulation. Particularly, the study focused on SMEs voluntary compliance. The study observed that, the majority of SMEs were not registered with TRA for tax return. Furthermore, the study revealed a significant percent of respondents who are registered with TRA but do not successful file their tax return. This indicated

that the level of voluntary compliance of TRA customers is significantly low even to registered clients.

The study observed that clients' education, business experience, training status and tax laws awareness significantly influence tax payers' degree of voluntary compliance. Therefore, the study concludes that improving the awareness of tax payers through training positively increase voluntary compliance.

5.2.2 Block Management administrative approach.

This is TRA system of categorizing their customers in accordance with their geographical location i.e. TRA tax regions have been divided into blocks and sub blocks. The aim of doing so was to simplify the process of reaching customers. This section examines the effectiveness of block management in numerous ways.

The study looked at the effectiveness of the block system management in relation to compliance of TRA customers. Focus was on physical survey to customers made by TRA staff and to what extent taxpayers' education has been received by customers. Here, 44% of respondents were not visited throughout a year. So, large number of customers misses important information concerning their business which can influence their compliance. Due to less number of visits, education that is provided to customers becomes little. 32% respondents agreed to receive taxpayers' education. From that, it shows that block system is very weak.

The theoretical and empirical implications drawn from study findings provide foundation for intervention programmes from the government and other interested stakeholders

5.2.3 Perception of SMEs on Voluntary Compliance.

In this study it was uniquely observed that, the level of education of tax payers significantly influence the perception of tax payers toward compliance. The level of education of clients can be uplifted through training designed to enrich them with tax knowledge.

5.3 Recommendations

The study recommends the followings:-

- i.) Increase more training to tax payers to enhance their understanding of tax regulations
- ii.) The block system have not been adequately used in visiting clients. There is a need of empowering TRA officers though adding facilities such as transport system to provide a comfortable way of making visits to clients. The government should also think of increasing the number of TRA employees to enable regual visitation to clients.
- iii.)It is noted that, tax laws are complex and require education to understand; a simplification of tax laws will enhance the ability of clients to understand them.

5.4 Directions of the Study

This study recommends more studies in the following areas:-

- i.) Factors affecting employees' visitation to clients by TRA staff.
- ii.) The contribution of electronic tools in raising tax education

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APPENDICES

Appendix I: Questionnaire for Master's Degree Course Research

Dear respondent,

I am Agnes Malima, a student of Mzumbe University Dar-es-Salaam Campus pursuing Msc. Accounting & Finance. I kindly request you, to assist in providing much information to the question as possible which represents your true views.

The study is for academic purposes only; therefore all information provided will be treated as confidential and will be used for academic purpose only and will not be used in any other way apart from the intended one.

I anticipate my gratitude to your assistance.

PART A: PERSONAL PROFILE

1) Gender	a.) Male b.) Female ()
2) Level of Education	a.) Primary School b.) Secondary School c.) Certificate/ Diploma d.) Undergraduate Degree () e.) Postgraduate
3) Business Experience	a.) Below One Year b.) Between One Year and 3 Years c.) Between 3 years and 5 years () d.) Above Five years

PART B: BUSINESS INFORMATION

- 4) (i) Are you registered with Tanzania Revenue Authority (TRA) for income tax return?
- a. Yes
 - b. No ()
- 4) (ii) If you are registered with TRA; how often do you voluntarily submit your business return (through interview or self-filing) for income tax assessment?
- a. Every year
 - b. Inconsistent (varying) submission ()
 - c. I do not submit
- 5) To what extent are you aware of laws and regulations that guide businesses in filing of tax returns?
- a. Highly aware
 - b. Aware
 - c. Moderately Aware ()
 - d. Not Aware
 - e. Highly Not Aware
- 6) After how long do TRA officers visit your business for information gathering?
- a. 3 month and below
 - b. Between 4 and 6 month
 - c. Between 7 and 9 month ()
 - d. Between 10 month and One year
 - e. None of Above

- 7) Have you ever received formal or informal tax-payers' education on benefits of voluntary compliance?
- a. Yes ()
 - b. No
- 8) Among factors which affect voluntary tax return by businesses is the low integrity by some TRA officers. To what extent does lack of integrity by TRA Officers negatively affect your attitude towards voluntary tax return?
- a. Highly Affecting
 - b. Affecting
 - c. Moderately Affecting ()
 - d. Not Affecting
 - e. Highly Not Affecting

Thank you in Advance for your Cooperation