THE EFFECT OF TAX SYSTEM SIMPLICITY ON TAX COMPLIANCE AMONG THE RENTAL INCOME EARNERS IN KENYA. A CASE OF ELDORET CENTRAL BUSINESS DISTRICT

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ABSTRACT: *The purpose of this study was to determine the effect of tax system simplicity on tax compliance among rental income earners in Eldoret town. The study sought to find out whether the simplicity of the tax system has an effect on the compliance of the rental income earners of Eldoret Central Business District. The study adopted an explanatory design. The target population of this study comprisedrental income earners within Eldoret Central Business District. The target population was 332 of which a sample of 181 waschosen using simple random sampling method. A five scale likert scale questionnaire was designed and distributed to the respondents. The validity and reliability was established through a pilot test. Data analysis was done using both descriptive and inferential statistics by the help of the statistical package for social sciences.Hypotheses were tested at 0.05, level of significance (95% confidence level) from the Chi-Square values. From the study findings it was established that the level of income of the rental income earners influenced their level of tax compliance. The study recommended that the government needs to improve on the taxation system and ensure that the tax payers can easily understand it. The findings of this study are expected to be of great assistance to the revenue collection agents, who might use the recommendations to augment the collection of tax from the rental income earners. The government will also be able to generate more revenue from rental income tax which might boost their operations.*

KEYWORDS: Compliance, Landlord, Rental Income, Tax; Tax System,

INTRODUCTION

Tax compliance has traditionally been viewed as unnecessary evil by many taxpayers. Today, though, the risks of overlooking tax liabilities and the potential benefits of an active tax compliance effort have never been higher. Many lenders will not even consider providing financing to a company that cannot demonstrate compliance with applicable sales, personal property and income taxes (Mubiru, 2009). But some may be willing to provide a larger credit line or reduce interest rates to companies that can prove compliance. Even as the rewards for tax compliance can be great, so can the risks and costs of non-compliance. Smart prospective buyers scrutinize tax payment records, and considerably discount or even entirely avoid lease portfolios or companies with questionable compliance practices.

According to Pope & Abdul-Jabbar,(2008) countries are unable to clearly establish the motivating factors for their tax payers to fully comply with the tax requirements and ensure that they pay their taxes effectively. If this dilemma could be resolved then many countries that are struggling financially will gain their financial independence. This will eventually lead to an effective way of increasing the countries revenue position hence,it can be expected to increase country's revenue position which in turn increases the financial capacity of the country

in financing the national development. Marti, (2010) noted that, it is the duty of the tax officials to make efforts in enhancing thesystematic and dynamic way for the tax payers to participate in the fulfillment of tax obligations. It is a high time that the actual payers of tax must be actively involved in the process of awarenesstowards tax compliance in their life because this will determine the countries tax revenues size which is influenced by the tax compliance.

Gabay, Remotin, & Uy, (2007) indicated that countries that need to change their tax compliance for the better must aim at embracing two of the three theories of tax ; the Ability-to-Pay Principle and the Equal Distribution Principle. These two principles stress equality and fairness. While the Ability-to-Pay talks pushes that individuals should be levied taxes based on their ability to pay, the Equal distribution Principle suggests that income, wealth, and transaction should be taxed at a fixed percentage; that is, people who earn more and buy more should pay more taxes,). According to Marti (2010) tax compliance is a complex term to define. Simply put, tax compliance refers to fulfilling all tax obligations as specified by the law freely and completely.

According to GIZ, (2010) developing countries still lag far behind the developed countries in terms of tax compliance with the statistics standing at 35% and 23% respectively for developed and developing countries. On the other hand Marti, (2010) observed that the budgetary deficits that are pushing developing countries into high levels of public debt might be attributed to the high gap between the expected tax targets and the actual tax collections . This drives the budget into constant deficits that are slowing down the extent of economic development in these countries. Martin further indicates that   developing countries must come up with strategies that will improve on policy development and implementation in order to reduce prevailing shortfalls and unhealthy dependence on donor funds.

Raising more domestic revenue is a priority for most Sub-Saharan African countries (Drummond *et al.* 2012). Mobilizing revenue is a way for governments' to create fiscal space, provide essential public services, and reduce foreign aid and single resource dependence. However, the domestic tax bases in most African countries are weakened by widespread tax avoidance and evasion (IMF 2011). Although taxpayer non-compliance is a continual and growing global problem (McKerchar and Evans 2009), many indications suggest that developing countries, mostly in Sub-Saharan Africa, are the hardest hit (Cobham 2005; Fuest and Riedel 2009).

Li, (1999) noted that the main issue faced by all tax authorities is that it has neverbeen easy to persuade all taxpayers to comply with the regulation of atax system. This implies that there is a perceived lack of fairness between the two parties which this study sought to investigate and document onhow this affects tax compliance in the rental income tax. Rummondet al. (2012) noted that of priority to many African countries is the need to raise more revenue domestically. The governments are after creating a more self reliance in terms of mobilization of funds through h effective revenue collection processes. This objective is hampered by among other things the low tax base, high level of tax evasion and avoidance (IMF 2011).

Other studies such asMcKercharand Evans (2009), Cobham (2005) and Fuest & Riedel(2009)taxpayer compliance has continual to be a major challenge both locally and globally. According to these studies it is important to understand the critical factors affecting the non compliance from the individual tax payer's point of view. According to D'Arcy (2011) the tax behavior in developing countries is still a very under researched area and the available literature only attempts to explore general factors that determine tax compliance behavior. There is

scanty literature on factors that influence the tax payment behavior among rental income earners. Carroll (2011) on taxation among women inthe informal sector in Ghana found out that despite the fact that morethan half (65 per cent) of the women surveyed were aware that they haveto pay taxes. However, more than half of thosewho participated in the study indicated that they were not certified at how the government is utilizing the taxes for their benefit.

Karingi et al, (2005) indicated that the Kenya's tax system is very burdensome to the tax payers. They evaluated the Kenyan tax system in terms of time taken for paying the taxes. On the other hand Farzbod, (2000) noted that the inefficiency, high administration costs, extended time in tax collection and the low amounts of received taxes in comparison to optimum allocation of resources is a major drawback for developing countries. Existing empirical evidence clearly indicates that most businesses whether small or large are affected disproportionately by the costs associated with the tax system.In a report by Kenya Revenue Authority, (2013) it is noted that the organization has a role to play in ensuring that the taxpayers and other parties understand their tax obligations under the tax laws. Beside the report also noted that the duty of ensuring that taxpayers and other parties need to fully participate have a role to play in meeting their obligations under the law. With the self-assessmentin EnsiLi, (1999). The main issue faced by all tax authorities is that it has neverbeen easy to persuade all taxpayers to comply with the regulation of atax system. This implies that there is a perceived lack of fairness between the two parties which this study sought to investigate and document onhow this affects tax compliance in the rental income tax. Rummondet al. (2012) noted that of priority to many African countries is the need to raise more revenue domestically. The governments are after creating a more self reliance in terms of mobilization of funds through h effective revenue collection processes. This objective is hampered by among other things the low tax base, high level of tax evasion and avoidance (IMF 2011).

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Abdul-Jabbar, (2008) and Ouma et al (2007) noted that the problem of non-compliance of the citizens on tax,continue to bite the economy in Kenya. Research findings suggest thatamong the factors that influence tax compliance include poor tax administration, lack of appropriate tax policy and low compliance. The effect of tax simplicity on tax compliance particularly among the landlords in Kenya has received little attention among the researchers. It is against this background that this paper been undertaken with the aim of assessing the affect tax simplicity on tax compliance among the rental income earners and recommend measures to be put in place by the GoK and KRA to enhance tax collection in this booming sector

Statement of the Problem

Despite the level of awareness among the tax payers on tax, the tax revenue from most of the sectors has not been commensurate. During the 2011/2012 financial year, the annual collection according to the KRA report stood at Ksh.707.4 billion against a target of Ksh.717 billion (KRA, 2012). According to a previous report by KRA the rental collection declined from 5 Billion in 2007 to 1 Billion in 2009.The report stated that a further collection of Kshs.1.5 billion was recovered from non-compliant landlords and property developers. This is an indication that when the level of compliance is low, government revenue collections always fall behind targets (KRA Rental Income Achievements 2015). The issues leading to the high level of non compliance among the rental income earners in Kenya and other developing countries have not clearly been addressed in literature.The lack of government mechanisms to address the issues of compliance not only among the rental income earners might only be one among the many challenges in tax compliance. The question under study is does the simplicity of the tax system influence the level of compliance of   It is against this background that this study has been undertaken with the aim of assessing whether simplicity f the tax system has an effect on the tax compliance among the rental income earners and recommend measures to be put in place by the Government of Kenya and KRA to enhance tax. Thus, the study hypothesized that:

$H_{o1.}$ *There is no statistically significant relationship between tax structure simplicity   and tax compliance among rental income earners.*

Theoretical Framework

The paper adopted the economic based theory in examining the effectiveness of the tax structure simplicity on compliance by the tax payers.Tax payers are influenced by the economic motives of the tax payers, the perception by the tax payer that tax is a burden especially (Vihanto, 2000).According to Trivedi and Shehata (2005), it is noted that taxpayers are thought to make calculations of the economic consequences of different compliant alternativeand choose the alternative which maximizes their expected after tax return/profit. These theories suggest that taxpayers have amoral utility maximizes hence; economic theories emphasize increased audits and penalties as a solution to compliance problems. Economic based studies suggest that taxpayers' behavior is influenced by economic motives such as profit maximization and probability of detection (Trivedi and Shehata, 2005).

From a theoretical point of view, it is consequently hardly possible to integrate this existing variety of conceptual orientations, choices, and boundaries into a single conceptual framework. Therefore, we prefer to reposition a number of these variables and processes into a new conceptual framework, that serves as a guide to integrate theoretical perspectives that interlink these variables and process and help to assess the actual determinants that influence tax compliance in rental income earners in Eldoret CBD in Kenyan Context. This study conceptualizes that the tax compliance could be affected by Simplicity of tax system. As such the study will adopt the following conceptual framework Simplicity of tax system as independent variables linked to the study dependent variable which is tax compliance.

(Independent Variable)   **(Dependent Variable)**

Simplicity of tax Structure		Tax Compliance

Figure 1: Conceptual Framework of Tax Compliance

Simplicity of tax system was explained as the simplicity in filing returns, calculation of taxes and use of ETR machines.

LITERATURE REVIEW

Silvani and Baer (1997) outlined the importance of the fact that a tax authority should have a simple tax return system from a taxpayer's point of view. A tax authority might assume its tax return is simple and easy to complete but it may not be so from the taxpayers' point of view. Therefore, before the final and actual version is delivered to taxpayers, it would be normal to put the forms through a series of 'pilot' tests to validate that the tax return is simple and easy to complete. In the UK, evidence suggests that uncomplicated tax returns play a major role in improving tax compliance (Silvani and Baer, 1997). Although tax knowledge and the simplicity of tax returns have a different impact on compliance (Kirchler, et al., 2008), it is noted that a taxpayer with low tax knowledge may be able to file the tax returns accurately provided the tax returns are simple, clearly explained and consistent.

The current year of tax returns should be the same as the previous one or at least largely the same. This can encourage taxpayers to file their tax returns correctly. Over an extended period, research focusing on complexity of a tax system in SAS has reported that there is an association between complexity and compliance, but the extent of the association remains in part uncertain. There has been mixed finding among authors such as McKerchar, (2002); Ritsema, Thomas and Ferrier, (2003);Blanthorne and Kaplan, (2008) on the impact of complexity of the tax system on compliance. In contrast, Clotfelter (1983) noted that when the level of tax complexity increases it significantly increases non-compliance among taxpayers. It was further noted that business taxpayers were more likely to seek advice from tax practitioners as tax system complexity rose; hence the issue of complexity appeared to be significant to them.

It has also been argued that simplifying tax laws might encourage compliance among taxpayers as they might more easily interpret and understand the law and the tax structure, and so possibly be better able to declare their income and compute their own tax liabilities correctly (Baldry, 1999). However, Forest and Sheffrin (2002) assert that simplifying the tax system (and therefore generating simpler tax returns) implicitly might not be an effective deterrent to tax evasion because taxpayers may not necessarily consider a complex tax system to be unfair. Forest and Sheffrin were unable to identify any relationship between complexity and perception of unfairness and concluded that while simplifying the tax law would not automatically improve compliance, many taxpayers perceive that tax systems are always complex and burdensomeAlthough Forest and Sheffrin suggested that the impact of the simplicity of the tax systems was insignificant since the filling of tax returns which require a high degree of understanding. It was therefore important to establish whether the simplicity of

the tax system has an influence on the tax compliance among rental income earners in Eldoret town.

MATERIALS AND METHODS

The study adopted an explanatory design. An explanatory study uses hypotheses to account for the forces that caused a certain phenomenon to occur.   The target population of this study was332registered rental income earners within Eldoret CBD (Uasin GishuCounty Revenue Section, 2015). From the target population of 332, Taro Yamane (1973) sample size formula was used to select a sample size of 181 individuals owning rental houses within Eldoret CBD. The study thereafter employed simple random sampling technique in the selection of the sample. Primary data was collected directly from the respondents using questionnaires. Secondary data on the other hand was gathered through review of available relevant materials on taxation.

Data Analysis

Data collected was carefully compiled, sorted, edited, classified, coded and checked for accuracy and relevancy. Then it was entered, edited and serial means was used to cater for the missing values. This was done with the help of excel spread sheet and SPSS programme using statistical description, factor analyses and correlation and regression tests. Analysis and interpretation of data was done bearing in mind the objectives and the research hypothesis of the study. Both descriptive and inferential data analysis was done. Descriptive analysis helped to establish the frequencies, percentages, means and standard deviation. While inferential statistics included correlation, chi square analysis and regression analysis.

Demographic data was analyzed using descriptive statistics since it sought to provide a summary of the responses and compare with each other to make conclusion.Descriptive statistics were also used to summarize the responses from the various items defining the objectives.Factor analysis was done to compute the factor loading. KMO analysis was also used to check data adequacy. Cross tabulation was done to determine the Correlation. Pearson's correlation (r) was used to check the nature of the relationship between the dependent and independent variables and test the independence of the variables. Multiple regression model was used to test hypothesis at 95% confidence, that is the p-value should be less than 0.05 (which is the alpha level associated with a 95% confidence level).

FINDINGS

The study found out that 147 persons responded to the questionnaires representing 81.2% while 18.8% of the respondents did not respond to the questionnaires. \

The Simplicity of Structure of the Tax System and Tax Compliance

The simplicity of structure of the tax system and tax compliance was also put into account by the study. This was the fourth objective which was tested using a number of statements that sought to evaluate whether the structure of the tax system influenced tax compliance among the rental income earners. A five scale likert ranging from 5- strongly agree to 1- strongly disagree was used to establish the opinion of the respondents.

Descriptive Statistics And Factor Analysis

This was done to establish whether all the factors used to test the objective met the required threshold of 0.5 loading. The results presented in Table 1. The results in Table 1 shows that only six items out of 9 questionnaires were considered for further analysis as they met the expected threshold of 0.5 of the factor loading expected. This was done to establish the frequency, percentages, mean and standard deviation. These items help to describe the quantities of the responses. As presented in Table 4.2. Only the six factors were considered for further analysis in both descriptive and inferential statistics. The descriptive summary of percentages and frequencies are presented in Table 1. The results in the table 1 shows that most of the respondents knew how to use the ETR machine. It was also noted that it was easy to understand all the processes of the current tax system This indicates that the rental income earners usually complain about the ETR programmes. The study also sought to establish whether the tax structure makes it possible for tax payers not report all of their income in order to pay less income tax. Lastly the study sought to find out whether tax structure ensures that all information is presented to avoid tax evasion.

Table 1   Descriptive Statistics And Factor Analysis

Factors	Mean	SD	Loading
It is easy to use ETR machine	2.96	1.072	0.675
It easy to understand all the processes of the current tax system	3.14	1.077	0.637
We never complain about ETR programmes	2.82	1.49	0.835
The tax structure makes it possible for tax payers not report all of their income in order to pay less income tax.	3.55	0.952	0.553
Tax structure is appropriate and makes tax payers to comply	3.83	0.612	0.579
Tax structure ensures that all information is presented to avoid tax evasion.	3.74	0.768	0.583

Tax Compliance

This section of the study sought to establish tax compliance among the rental income earners. The results of the study are illustrated in table 4.4. The study has established that rental income earners have never been penalized for tax failure because the system is perceived as very effective (mean = 3.84, SD = 0.75). They also comply with the tax since the tax system is fair (mean = 3.72, SD = 0.7). Additionally, they have never delayed to pay taxes because the system is very fair (mean = 3.71, SD =1.093).

Table 2:   Tax Compliance

Statements	Mean	Std.
I comply with the tax because the tax system is fair	3.72	0.7
I have never been penalized for tax failure because the system is perceived as very effective	3.84	0.75
I pay actual tax as assessed because I have a lot of trust in the tax system.	3.7	0.895
I have never delayed to pay taxes because the system is very fair	3.71	1.093

Source: Survey Data (2015)

Correlation Analysis

It was important to establish whether there was an association between the Structure of the Tax Systemand tax compliance among the rental income earners. Pearson's correlation r was computed using cross tabulation and the results were presented in table 2. From the results provided in Table 2 it is noted that there is a moderate positive and significant association between the structure of tax system and tax compliance among rental income earners in Eldoret CBD (Pearson's r = 0.303; significance p- value = 0.000). The Cramer's V value also shows that the level of income might influence tax compliance by 46.2%. This is not by chance since the association is significant at p- value of 0.000 which is much less than the 0.05 recommended. Similarly, the t test value indicates that the association between the structure of the tax system and tax compliance is significant since the t-value is 3.825, which is higher than recommended +2.

Table 3   Correlation Analysis

		Value	Approx. Tb	Approx. Sig.	
Nominal by Nominal	Phi	1.46			0
	Cramer's V	0.462			0
Interval by Interval	Pearson's R	0.303	3.825	.000c	

Test of hypothesis

The findings indicated that the model correlation coefficient was 0.409. The R Square shows variability of tax compliance with perceived simplicity of tax structure in tax system which explain 16.8% of the factors affecting tax compliance among rental income earners as represented by R Squared (Coefficient of determination). This relationship was significant considering the F – value of 8.74 at p- value at 0.000 which is much less than the predetermined value of 0.05.

The simplicity of tax system, has a sufficient contribution to tax compliance, (P-value = 0.05 =0.05) which suggest that the relationship between simplicity of structure of tax system and tax compliance is significant. This allows us to reject the null hypothesis in this case which stated that there is no significant relationship between simplicity of tax system and tax compliance and adopt alternative hypothesis H_1 which in this case will be there is a significant relationship between structure of tax system and tax compliance in Eldoret CBD. The better coefficient $\beta = 0.238$ which is positive implies that an simplifying tax structure in the tax system results to a 0.238 units increase in tax compliance. The t-statistic (1.928) on the other, indicates the unique contribution the tax structure variable contributes to the model when other predictors are held constant, this contribution is noteworthy. This agrees with studies by Silvani and Baer, (2007) that uncomplicated returns play a vital role in improving tax compliance. Also, this study's findings are consistent with the findings of Baldry (1999) who indicated that simplifying tax procedures in SAS system might encourage compliance among taxpayers as they might more easily interpret and understand the law and the tax structure, and in so doing they are better able to declare their income and compute correctly their tax liabilities as required.

Table 4   Regression Results For Effect Of

	Unstandardized Coefficients		Standardized Coefficients			Correlations
	B	Std. Error	Beta	t	Sig.	Zero-order
(Constant)	2.372	0.185		12.795	0	
Structure of the tax system	0.157	0.053	0.238	2.957	0.004	0.238
R Square	0.057					
Adjusted R Square	0.05					
F Change	8.741					
Sig. F Change	0.004					
a Dependent Variable: TAXCOMPLIANCE						

CONCLUSION

The paper sought to establish whether there is a statistical association between tax compliance and tax simplicity among the rental income earners. The descriptive analysis showed that most respondents agreed that the level of income has an influence on the tax compliance income earners among the rental. Most of the statements had a mean of 3 which indicated that over 75% of the respondents agreed with the statements that defined the influence of tax simplicity on the tax compliance of the rental income earners in Eldoret town.It was also established that there is a positive and significant correlation between the tax simplicity and tax compliance among the rental income earners in Eldoret. This association was not by chance since the value of Chi-square was more than the tabulated value and the p- value was less than 0.05.

The purpose of this paper was to examine the influence of simplicity of tax system on tax compliance among the rental income earners in Eldoret town. Based on the study findings the study concludes that simplicity of the tax system issignificantly associated with tax compliance. Meaning that rental income earners in Eldoret town agreed that the simplicity of the tax system influence the land loads tax compliance.

RECOMMENDATIONS

From the findings of the study it is recommended that the government through various bodies such as the KRA should ensure that the tax system is simplified to ensure that the tax payers are able to understand the system and hence are able to comply with the tax payment. This will also ensure that the government can effectively enforce the law since most people understand what they are required to do with the payment of tax.

Further Research Recommendations

Despite the fact that thefindings of this study have added important information to the literature on tax compliance there are certain areas that require further study in order to understand the impact of other factors affecting tax compliance. This research was conducted in Eldoret town CBD and whether the results from this research would be consistent with other towns or cities

tax compliance on rental income earners would need to be tested through further research. Future studies focusing on tax compliance in other counties and towns are required inorder to evaluate whether a similar conclusion can be noted in regard to tax compliance among rental income earners.

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