The Effects of Online Tax System on Tax Compliance among Micro, Small and Medium Enterprises at Kangemi Harambee Market in Kenya

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Abstract

This study sought to determine the effect of online tax system on tax compliance among micro, SMEs at Kangemi Harambee market in Kenya. The specific objectives were to determine the effect of online tax registration on tax compliance, to assess the effect of online tax filing on tax compliance and to evaluate the effect of online tax remittance on tax compliance among micro, SMEs at Kangemi Harambee market. This study adopted the descriptive research design. The study's target population encompassed 656 small enterprises' at Kangemi Harambee Market in Kenya. The Yamane (1967) Formula for calculating sample size was adapted to pick 248 respondents. Stratified random sampling and simple random sampling technique was used to select vendors from the market. Questionnaires were adapted as the main data collection instruments. Data was analyzed by the SPSS software version 24. The study found that online tax registration, online tax filing and online tax remittance had a positive and significant effect on tax compliance among SMEs at Kangemi Market, Kenya. The study recommends that training needs to be done by KRA to all SMEs to ensure they understand the online tax filing system.

Key Words: Online tax registration, online tax filing, online tax remittance

1.0 Introduction

According to a research done by Sreekantaradhya (2000), taxation is of great importance to the development of any economy. It enhances dissemination, stabilization, provision and allocation of resources. Pfister (2009), during a conference at UN, in Doha 2008, acknowledged that taxation is key success to any domestic resource deployment. Automated systems have demonstrated competence in enhancing massive improvements in business that leads to increased revenue. Wasoa (2014), asserts that applying technological changes towards the government strategic goals are key in transforming the country into an entity that can provide basic needs, necessities and expectation of today's world.

Government is trying to deliver services to citizens at cost effective prices. According to Amitabh (2008) tax authorities are keeping abreast with government modifications like online tax filing to enhance their service delivery. Some of the pros of online tax filing include flexibility where tax

African Tax and Customs Review
Issue 1, October – December, 2018
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payers can file returns from the comfort of their home, reduced workload, changes in cost from tax collectors, lessening of errors linked to manual filing (Osebe,2013; Simiyu,2013).

Online tax filling begun in United States where Internal Revenue Service's (IRS) began offering tax return for tax refund only (Muita, 2011). KRA dating back to 1995 in July when it was first formed as a government agency purposefully for collecting taxes on behalf of the government of Kenya and when it was mandated to collect a number of taxes and duties including turnover tax, income tax, value added tax, stamp duty and custom duty (Maina, 2015).

According to a research done by Economic survey (2015), continued implementation of the system is projected to increase revenue returns in a bid to deepening the tax base, reduce the cost of compliance while enhancing revenue administration. In 2015 the KRA authority introduced Itax system for administration of government revenue (Muhoro, 2017).

Itax is the source of most governmental projects including infrastructures such as roads, power supply and water among others. Duanjie (2012), indicates that such developments lead to countries economic growth and creation of a good business atmosphere. Simiyu (1999) asserts that a good tax system should be unbiased, economical, transparent and competent and thus leading to improving of fiscal performance, the principle of good governance, complete circulation of goods and services eventually enhancing state legitimacy.

Tax filing is a global activity practiced by many countries such as Sweden, Norway, Singapore, Brazil, Malaysia, China, France, Finland, Malaysia, Turkey, Netherlands, Canada, Italy, United Kingdom, Chile, Germany and Ireland (Ramayan, 2008). Jackson and Mckee (2002), combat that taxation is a key element for government's vision of achieving equity and efficiency in the economy. Kenya is ranked among countries unable to meet the tax budget due to low tax compliance. According to a report done by Kenya Revenue Authority (2013), it is quite clear that an organization has a role to play in ensuring that citizens understand their tax obligation under the set laws. Reformation of a tax system occurs due to international pressure and economic crises (Mahon, 1998).

Tax compliance has been a key component that even lenders use when offering loans (Mubiru, 2009). Some go out of their way to reduce cost or offer more loans to clients that are compliant.

But as much as tax compliance has several benefits non-compliance to has severe consequences. In most third world countries the tax compliance has made several strides to enhance tax compliance. However most of those changes have made it too complex for tax payers to understand. According to Oberholzer (2008), this has led to severe problems among tax payers having little access to the tax experts.

According to Picur (2006), tax compliance has been viewed under three perspectives, uncertainty model and norms of compliance model. Economic model explains that taxpayers' objective is maximizing financial taxes to benefit from tax delinquency overshadowing the risk of detection and punishment. However, the uncertainty model is an extension of economic model only that in this perspective the theory of maximizing interest while avoiding risk and penalty in the real word is imperfect. Lastly, the norm of compliance model asserts that the canons of a tax clients' behavior are normally influenced by culture.

Research done by McKerchar and Evans (2009) suggest that taxpayer compliance has been a big challenge both locally and globally. The researchers suggest that the challenges of tax compliance should be looked at from an individual point of view. In most third world countries the aspect of tax compliance involves tax computation on a corporation's income for the year, duly filing of information and quarterly payment of due tax through the i-tax portal. The tax base is calculated as preceding year's tax liability plus a ten percent mark-up on estimated income for the year.

SMEs are small independent firms that employ less than a certain number of workers. SMEs enhance dynamism and innovation and lead to employment in developing countries. According to the World Bank (2015), SMEs account for 45 percent of employment and 33 percent of Gross Domestic Product (GDP). According to James (2007), Kangemi market begun in 1960 but the actual year when people started selling African Leafy Vegetables was 2004.

Kangemi market according to a daily nation report (2018) is congested and the government is trying to improve its infrastructure. Business continues up to the late evening at the busy market. Traders, buyers, pedestrians are a common scene throughout the day at the Kangemi market in Nairobi. Market fires have been a common factor which destroys massive goods at the market like the one that happened in 2017 and 2016. According to a daily nation report (2015), "The Nairobi City County government could be losing millions of shillings in annual revenues from city

African Tax and Customs Review
Issue 1, October – December, 2018
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markets, thanks to a mafia-like network calling the shots in the sector, The Nairobian can reveal. The cash is pocketed by a clique of county officials working in cahoots with brokers through well-orchestrated deals. The collusion involves instructions for sidekicks to achieve set levy collection targets. In most markets, new traders are regularly licensed, but this is never communicated to top bosses in the county. The collection generated ends up in the pockets of some county personnel and their foot-soldiers.

From the Tenants Purchase Scheme (TPS) on market rents, the county government hoped to collect Sh25 million quarterly, but netted only Sh22.7 million. Twenty-four of the county's 45 markets have a total of 6,559 rental slots going for between Sh500 and Sh25, 000 monthly. When issues were raised on alleged misappropriation of funds in regard to the TPS, a senior market superintendent attempted to derail efforts to probe the scheme. He subsequently quit his job. Rent payments by Burma Market traders were remitted at the TPS office but there was no issuance of receipts. Interestingly, the accounts seemed to have been adjusted and the money seemingly 'flushed' off the system. Reportedly, traders at City Park were being issued with receipts meant for City Market, while those in Kangemi and Old Ngara markets apparently refused to remit rent. Kangemi Market has been a subject of conflict over ownership between the county and private developers. The market allotment letter issued to the defunct City Council of Nairobi by National Lands Commission was purportedly taken by a private developer. The Nairobian tried reaching the County Trade and Tourism Executive Officer, for a comment without success"

Small and medium enterprises (SMEs)'s businesses in Kenya are over 2.7 million accounting for a lion share in the economy's growth and development potential (KRA, 2015). Muita (2011) ascertains that the Kenya Revenue Authority found manual system of paper work to be tedious and cumbersome on the part of the taxpayers who could spend magnitudes of time trying to file returns which on the part of Kenya Revenue Authority were hard to reconcile and validate. It is the rigidity and failures of this system that gave rise to the online tax system in Kenya.

1.1 Statement of the Problem

The electronic tax system was introduced in Kenya in 2007. While it was supposedly presumed that with the online system of tax filling and returns compliance levels were to grow heavily amongst all tax payers, Wasao (2014) found that online system do affect tax compliance level

African Tax and Customs Review
Issue 1, October – December, 2018
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among small taxpayers in East of Nairobi as far as registration, filing and payments were concerned, From the regression analysis, it was revealed that holding online tax registration, filing and payment to a constant zero, tax compliance would stand at 3.663. This is unexpected and worrying as the government through its revenue collection body (KRA) has invested a lot of money in online tax systems such as i-tax which are expected to increase compliance levels and to aid in maximum revenue collection.

Wasao (2014) researched on the effect of online tax system on tax compliance among small taxpayers in east of Nairobi tax district. Murigu (2017) determined the factors influencing the adoption of the itax online system among small and medium-sized enterprises (SMEs) in Westlands, Nairobi County. Oeta (2015) determined the effect of itax on revenue collection by Kenya Revenue Authority in Western Kenya District. These studies have failed to determine the effect of online tax system on tax compliance among micro, small and medium enterprises at Kangemi Harambee market in Kenya. This study therefore aims to fill the gap by determining the effect of online tax system on tax compliance among micro, small and medium enterprises at Kangemi Harambee market in Kenya.

1.2 Research Objective

This study's overall objective was to determine the effect of online tax system on tax compliance among micro, small and medium enterprises at Kangemi Harambee Market in Kenya

1.3 Research Question

This study aimed to answer the question, how does online tax system affect tax compliance among micro, small and medium enterprises at Kangemi Harambee Market in Kenya?

2.0 Empirical Review

According to Lai and Choong (2010), online tax registration is a compulsory electronic service offered by the government to its citizens. Plumley (1966), researched on two tax compliance; filing compliance and reporting compliance. Filing compliance involves timely and accurate filling of returns while reporting compliance is merely about correct declaration and registration of iTax based on correct tax liability.

Amitabh (2009), sought to establish the effects of paperless tax filing on young specialists in India. The regression results portrayed that the upcoming scholars depend on the simplicity of the tax system, comparative advantage, and performance of filing on the system. Online tax registration among SMEs in Harambee market can actually occur if all tax payers accept to get registered. However, according to Muita (2010) who investigated factors affecting adoption of e-filling system and it usage in Kenya. The researcher established that for e-filling to get embraced then infrastructure and the business environs should be perfect.

Muita (2010) and Makanga (2010) explored on technological advancement as a tool to enhance tax filing and compliance. The target population was the large taxpayers such as firms with a turnover of Kshs. 750 million over head. The scholars established that KRA and the business environs must adapt technology in order for the SMEs to adhere to tax compliance laws.

Lee (2008) did a research to compare different tax filing web sites in Korea and Turkey with the ease of tax payers to file returns. Turkey was found to have a complex system however taxpayers did not find it difficult to file returns as they relied on accounting professionals to assist them while Korea system was not complex but most taxpayers did not use it effectively.

Online tax remittance is the cost of sending the payments from taxpayers. Faridy (2014) sought to establish effect of VAT in Bangladesh, compliance cost and non-compliance cost in Bangladesh enterprises. According to the research most SMEs indicated complexity of VAT regulations and compliance cost as the greatest difficulty leading to non-compliance. According to Nduruchi, Makokha and Namusonge (2017), taxpayers must cover the cost of administrative cost to run the Kenyan government. The scholars did a research on cost of compliance and according to the findings, 70 percent of the respondents explained that cost of tax product is too high. Although previous researchers provide crucial research findings on tax compliance they provide no clear cut out connection between online tax system and tax compliance. This scenario exposes a glaring gap raised by empirical studies and considering the draw backs presented by micro, SMEs, it was crucial to carry out a research on effects of online tax system on tax compliance among micro, SMEs at Kangemi, Kenya.

3.0 Methodology

The study used a descriptive research design. Descriptive research design according to Mugenda and Mugenda (2004), reports how things are done showing the behavior, atttitude and characteristics of such things. This design was quite relevant as it helped the research get in-depth information about the target population. The purpose of the study was to check on the effects of ontile tax system on small and medium enterprises in Kangemi Market thus the need to use descriptive design.

The study's target population encompassed 656 micro and small enterprises' business owners at Kangemi Harambee Market in Nairobi, Kenya. The population comprises of a total of 193 green groceries vendors, 357 clothing and shoes vendors in total, 39 food vendors, 20 saloons, 25 cerial vendors and 22 poultry vendors in the market. The information regarding the target population is presented in table 3.1:

Table 3.1: Target Population of the Study

Nature of Business	Population
Green Groceries	193
Clothing and Shoe Vendors	357
Food vendors	39
Saloons	20
Cerial vendors	25
Poultry vendors	22
Total	**656**

Source: Kangemi Harambee Market Association (2017)

The Yamane (1967) Formula for calculating sample size was adapted. A 95% confidence interval level and p=.5 are assumed. The formula is as follows;

$n = N / 1 + N(e)^2$

Where:

n   :   sample size

N   :   Population size

By applying the formula:

n   = $656/1+656(0.05)^2$

       =   248 Respondents

Stratified random sampling technique will be used to select vendors from the diverse classification after which simple random sampling technique will be applied to the vendors on the day of data collection. Stratified random sampling technique is prefered because of it's accurateness, easily accessible, divisible into relevant strata and enhances contrast thereby creating representativeness in a study (Kothari, 2004). The sample size for this study was therefore be 248 respondents as shown in the table 3.2:

Table 3.2:Sample Size

Nature of Business	Sample Size
Green Groceries	75
Clothing and Shoe Vendors	135
Food vendors	15
Saloons	7
Cerial vendors	8
Poultry vendors	8
Total	**248**

The study used primary data collection method. Questionnaires were used in this case. The questionnaires were administered through drop and pick later method. Follow-ups were done through physical appearance at the respondents' place of work, phone calls and emails. The questionnaire was divided into four segments the first section representing demographic information while the other three represented each objective under investigation.

The study thus sought for research supervisors in that particular field and lecturers, entrepreneurs in the study area who rechecked and gave approval as a way of ensuring content validity.

African Tax and Customs Review
Issue 1, October – December, 2018
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Reliability was ensured by the Cronbach's alpha test which indicated reliability of data collection instruments as the average alpha value was 0.89 indicating reliability.

Data was analyzed using the Statistical Package for Social Sciences (SPSS Version 20). Data was analyzed using the regression equation below;

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (i)$$

Where;

Y= Dependent variable (Online tax system)

α - Constant

$\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ – Coefficients of Independent Variables

X_1 – Online Tax Registration

X_2 – Online Tax Filing

X_3 – online tax remittance

ε - Extraneous Error term

4.0 Analyst and results: Key Findings

4.1 Background Information of Respondents

Table 4.1: Demographic Information

	N	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
Descriptive Statistics									
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
Gender	248	1	2	1.52	.500	-.097	.155	-2.007	.308
Age bracket	248	1	5	3.17	1.258	-.188	.155	-1.134	.308
Level of education	248	1	4	1.68	.732	.649	.155	-.646	.308
Business been in operation	248	1	4	2.31	1.151	.142	.155	-1.452	.308
Nature of business	248	1	6	3.13	1.829	.172	.155	-1.451	.308
Valid N (listwise)	248								

According to table 1 above Gender of respondents stood with a mean of 1.52 and standard deviation of 3.17 while the skewness and kurtosis were at -0.097 and -2.007 respectively. The age bracket had a mean of 3.17 and a standard deviation of 1.258 while the skewness and kurtosis was at -0.188 and -1.134 respectively. The level of education of the respondents was mostly primary or high school.

The mean for level of education stood at 1.68 and standard deviation of 1.258 while the skewness and kurtosis were at 0.649 and -0.646 respectively. Moreover while considering how long has the

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business been in operation the standard deviation was 1.151 with a mean of 2.31 while the skewness and kurtosis stood at 1.151 and -1.452 respectively.

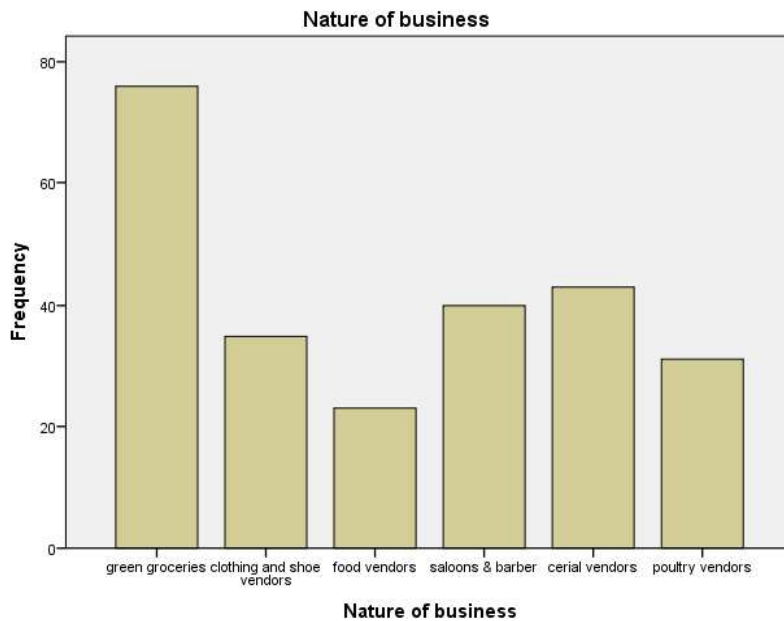**Figure 4.1: Nature of Business Owned**

Figure 4.1: Nature of Business Owned

On the nature of the business owned, the mean for green groceries and food was 3.13 while the standard deviation was 1.829; the skewness and kurtosis were 0.172 and -1.451 respectively. Male respondents had a frequency of 125 while females were at 120. The figure 1 above shows the highest age bracket was between 41 and 50 with a frequency rate of 80% while the lowest age bracket was below 20 with a frequency rate of 20%. The other age bracket was between 21 and 30 with a frequency of 60 % while those within 31-40 were at 40%. Lastly was above 50 with a frequency rate of 25%.
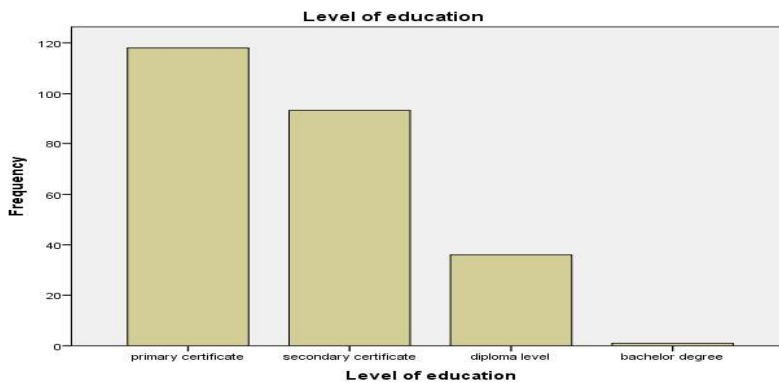
Figure 4.2: Gender of Respondents

According to Figure 2 on the level of education, most respondents were primary certificate with a frequency of 120 followed closely by secondary certificate with a frequency of 90. Last but not least was diploma level at a frequency of 35%. Finally we had bachelor's degree at a frequency of 2%.
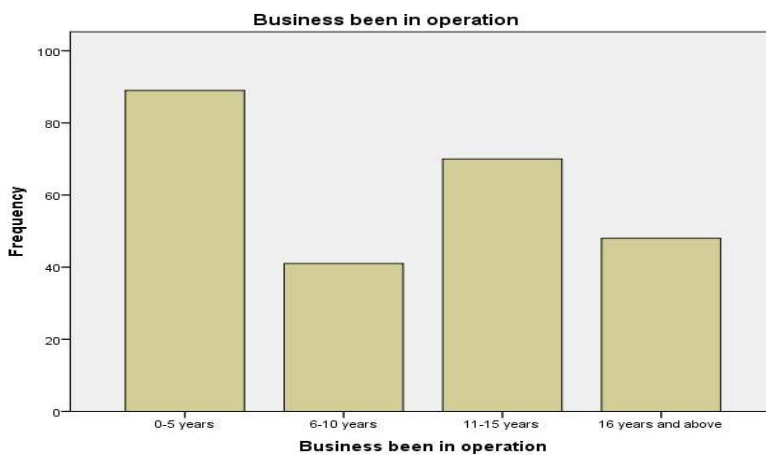

Figure 4.3: Business Been in Operation

The study realized that most of the respondents had a business in operation for a period between 0 and 5 years indicating that they had just begun working at Harambee Market. This was closely followed by entrepreneurs who had been in operation for a very long time that was between 11 to 15 years. Most of the respondents were green groceries occupying a higher percentage of 75%, followed by cereal vendors at 42%, saloons and barbers at 40%, clothing and shoe vendors at 38%,

poultry vendors at 30% and food vendors at 25%. The study indicates that all the varied respondents were well represented in this study.

The study established from majority of the respondents that they were registered for Value Added Tax (VAT) and Turnover tax (TOT) with a frequency of 99% and 98% respectively. However, we had some individuals who were not registered for either but instead were remitting their taxes through their personal income tax as individuals. The study also ascertained that 5% of respondents were registered for Pay As You Earn (PAYE). This raises concerns of the need for constant trainings to differentiate amongst individuals the different types of tax and the need to remit them as required by the law.

Table 4.2: Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.581[a]	.338	.330	.49892	.338	41.538	3	244	.000	2.076

a. Predictors: (Constant), Online tax registration, online tax filling, online tax remittance

b. Dependent Variable: Online tax system

The table 4.2 above talks about the Goodness of fit. This shows the independent variable explains 33.8 % of the variables in the research while 66.2% is explained by other variables not inclusive in the model. This model is also significant as the p-value is less than 0.05

Table 4.3: ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	31.019	3	10.340	41.538	.000[b]
	Residual	60.737	244	.249		
	Total	91.756	247			

a. Dependent Variable: Online tax system

b. Predictors: (Constant), Online tax registration, online tax filling, online tax remittance

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The table 4.3 illustrates the Analysis of Variance (ANOVA) which assesses the overall significance of the model. The results of the model indicate that it is significant at 0.0 which is actually less than 0.05.

Table 4.4: Regression Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	2.468	.257		9.608	.000
Online tax registration	.097	.023	-.227	-4.259	.000
Online tax filing	.573	.059	.523	9.741	.000
Online tax remittance	.248	.047	-.288	-5.294	.000

Using the values of the coefficient from the regression, the established equation takes the form of: 2.468= 0.097 tax registration + 0.573 tax filing + 0.248 tax remittance. The results above indicate that all the variables had a positive impact on tax compliance. Tax filling, tax registration and tax remittance has a positive impact on the online tax system. The results indicate applying tax registration results in a 0.097 change in online tax system, online tax filing results in a 0.573 change in tax filing while tax remittance results in a .248 change in the online tax system on tax compliance. The results further indicate that online tax registration, online tax filing and online tax remittance are all significant as their p-value is less than 0.05(p-value < 0.05).

4.2 Online Tax Filing

On the online tax filing and tax compliance, the respondents argued that the online tax system was friendly with a standard mean of 3.40 and a deviation of 0.847. That helped the respondents understand the registration process as supported by a mean of 3.23 and a standard deviation of 0.747. This in turn reduced most of the corruption cases at a mean of 2.58 and a standard deviation of 1.506. Thus, online tax filing helped in reducing the time wasted on long queues experienced at KRA as was supported by a mean of 3.98 and a standard deviation of 0.702 therefore, leading to cost reduction both on KRA side and clients' side.

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Table 4.4: Descriptive Statistics on Online Tax System and Tax Compliance

	N	Minimum	Maximum	Mean	Std. Deviation
Online tax system friendliness	248	1	5	3.40	.847
Understand online tax registration process	248	1	5	3.23	.747
Itax reduced corruption	248	1	5	2.58	1.506
Online system reduced time wastage on queues at KRA	248	1	5	3.98	.702
Cost reduction with Itax system	248	1	5	2.59	1.288
Valid N (listwise)	248				

On the online tax filing and tax compliance, the respondents argued that the online tax system was friendly with a standard mean of 3.40 and a deviation of 0.847. That helped the respondents understand the registration process as supported by a mean of 3.23 and a standard deviation of 0.747. This in turn reduced most of the corruption cases at a mean of 2.58 and a standard deviation of 1.506. Thus, online tax filing helped in reducing the time wasted on long queues experienced at KRA as was supported by a mean of 3.98 and a standard deviation of 0.702 therefore, leading to cost reduction both on KRA side and clients' side.

Table 4.5: Descriptive Statistics on Online Tax Filing and Tax Compliance

	N	Minimum	Maximum	Mean	Std. Deviation
Confidently file returns	248	1	5	3.16	.920
Understand online tax system	248	1	5	3.26	.741
Online tax filling connects with Tax agents	248	2	5	3.74	.935
File taxes timely on due date	248	1	5	2.74	1.065
Record keeping important to ease tax filing	248	2	5	3.74	.830
Valid N (listwise)	248				

From the study, majority of respondents had knowledge of the online tax system of filing returns as supported by a mean of 3.26 and a standard deviation of 0.741. The respondent agreed that the system connected them directly with the tax agents as supported by a mean of 3.74 and a standard deviation of 0.935. In this light, respondents were able to file taxes timely on the due date. Respondents therefore agreed that in order to file returns record keeping was very important.

4.4 Online Tax Remittance

Table 4.6: Descriptive Statistics on Online Tax Remittance and Tax Compliance

	N	Minimum	Maximum	Mean	Std. Deviation
KRA portal eased online tax remittance	248	2	5	3.59	.753
Hard access to system during peak hours	248	2	5	3.87	.720
Tax rates are high	248	2	5	4.09	1.192
Penalties on late filing are unfair	248	1	5	4.00	1.222
Valid N (listwise)	248				

Majority of the respondents argued that KRA has eased the online tax system remittance process with a standard mean of 3.59 and a standard deviation of 0.753. Access to the system during peak hours was very hard with a majority starting this as a great challenge as supported by the mean of 3.87 and a standard deviation of 0.72. Moreover, quite a number complained about the high tax rates and penalties on late filing which according to them was unfair.
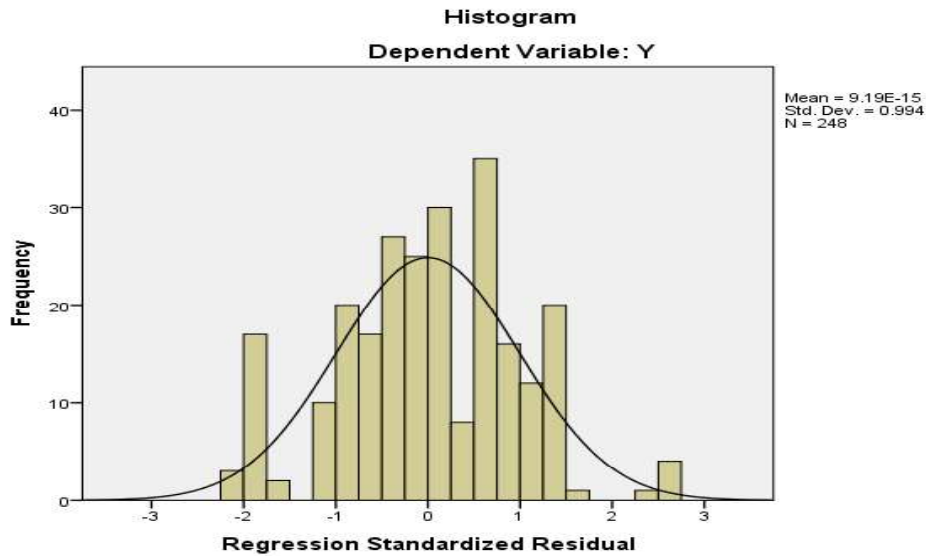
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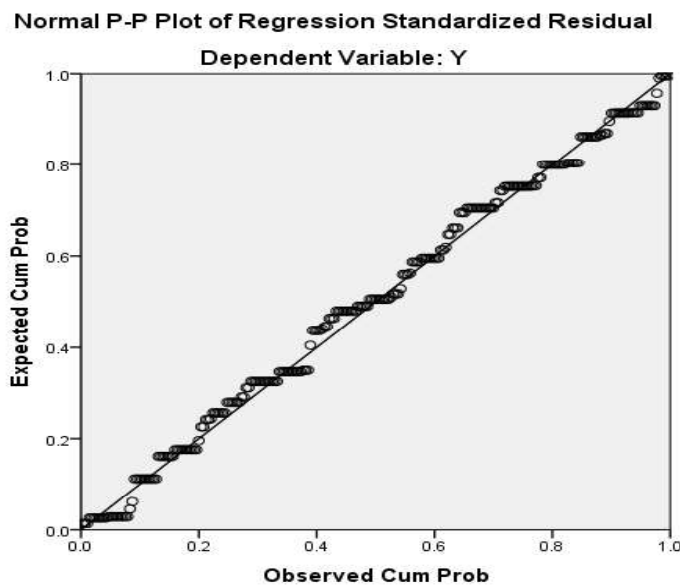**Figure 4.4: Regression Standardized Residual**

Figure 4.5: PP Plot Regression Results

1.   **Discussion and conclusions**

The main objective of the study was to ascertain the effects of online tax system on tax compliance among micro, small and medium enterprises at Kangemi Market in Kenya. The specific objectives included effects of online tax filing on tax compliance among SMEs, determining the outcomes of

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online tax remittance on tax compliance and online tax registration outcomes on tax compliance among SMEs in Kangemi Kenya.

The study found that online tax registration positively influenced tax compliance among SMEs at Kangemi Market with a coefficient of 0.097 which was also significant. Online tax registration was significant since the p-value was less than 0.05(0.00<0.05). Further analyses indicate that online tax registration had a positive and significant effect on tax compliance among SMEs at Kangemi Market, Kenya. Ceteris paribus, a unit increase in online tax registration across time and between SMEs leads to 0.573 increases in tax compliance on average.

The study also found that online tax remittance had a positive impact on tax compliance among SMEs at Kangemi market. This is so because it had a coefficient of 0.248. Ceteris paribus, a unit increase in tax remittance across time and between micro SMEs would lead to 0.248 increases in tax compliance.

The study shows that all the variables significantly affects online tax system on tax compliance hence the conclusion that a multifaceted approach in online tax system should be put in place that includes all the practices that were of focus to this research in order to realize the ultimate goal of revenue maximization. Online tax system significantly contributes to tax compliance among SMEs. The researcher therefore concludes that there is a strong relationship between online tax system of filing returns and tax compliance of Micro, Small and Medium enterprises in Kangemi, Kenya.

The study recommends that more training needs to be addressed by KRA to all SMEs to ensure they understand the online tax filing system and ensure that there can be able to file returns confidently with minimal supervision. Since the study findings also indicate that corruption is a major challenge that undermines the effort of KRA in achieving the revenue budget, suggestions indicates that sensitization needs to be extended more aggressively on the part of tax payers and that the government must ensure tough measures are put in place to curb inflation which discourages tax compliance.

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