EFFECT OF TAX INCENTIVES ON FOREIGN DIRECT INVESTMENT IN THE OIL AND GAS SECTOR IN KENYA

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DECLARATION

Declaration by the Student:

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DEDICATION

This work has been dedicated to my supporting supervisors Dr. Bruce and Dr. Tenai, my family members for their uttermost support, encouragement, contribution and critiques that were a pillar to the success of the write up. Also, to my friends for their continued support and motivation during my entire period of my study. Thank you and May the Almighty God bless you abundantly.

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ABSTRACT

Over the years, foreign direct investment inflows to Kenya have not been consistent with certain cycles of low inflows. This has been attributed to deterioration in economic efficiency, as well as increasing problems with poor infrastructure and high costs of living. Previous surveys have also described the lack of well-structured and attractive tax incentives as a major barrier to the growth of FDI. The purpose of this study was to assess the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya. The specific objectives included: to determine the effect of capital deductions, income tax, VAT incentives and import duty incentives on foreign direct investment in the oil and gas sector in Kenya. The research was informed by the theory of innovation diffusion, social exchange theory and stakeholders' theory. Explanatory research design was used in the study. The target population included five oil and gas companies. The target respondents were 136 senior managers from five oil and gas companies in Kenya. A census of all the managers was done. Primary data was collected using structured questionnaires. The study applied quantitative methods to analyze data. These included descriptive statistics (percentages, means and frequencies). Further, inferential statistics (Pearson's correlation and regression) were conducted to determine the relationship between tax incentives and foreign direct investment. The findings indicated that capital deductions ($\beta1$=0.377, P = .000); income tax ($\beta2$= 0.286, P = .000); VAT incentives ($\beta3$= 0.124, P = .020); and import duty incentives ($\beta4$= 0.375, P = .000) had a positive and significant effect on foreign direct investment. The adjusted R^2 of the regression model was 0.789. The study concluded that tax incentives contribute significantly towards foreign direct investment in the oil and gas sector. Based on the findings, the study recommended that the government should strengthen aspects related to tax incentives. These include; wear and tear allowances, investment allowances, industrial deductions, loss carry-forward, withholding tax incentives, tax credit incentives, allowable deductions, exemption of goods and services from VAT, import duty incentives on machinery, raw materials, office equipment and customs duty. This study focused on the oil and gas sector in Kenya. Further studies could be conducted in other sectors for comparison purposes.

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OPERATIONAL DEFINITION OF TERMS

Tax Incentive refers to the tax obligation deduction, exclusion or exemption given as an incentive to participate in a particular investment operation (Prichard, 2016).

Foreign Direct Investment is the net inflows of investment from other countries to Kenya through the oil and gas sector (Maiga et al., 2019).

Capital Deductions Incentives is another form of direct tax incentive, which provides stipulated percentages of investment costs that could be deducted from tax liabilities (Gitonga, 2017).

Import Duty Incentive refers to measures the government takes to reduce tax levied on imported oil and gas products (Irokwe & Nnaji, 2017).

Income Tax Incentive is the government measure to reduce the amount of tax expected from business undertakings over a given period of time (Lodhi, 2017).

VAT Incentives refers to measures the government takes to reduce the consumption tax placed on a product whenever value is added at each stage of the supply chain, from production to the point of sale (Narayana, 2015).

ABBREVIATIONS/ACRONYMS

AIBUMA	African International Business and Management
CGT	Capital Gains Tax
CGTR	Capital Gains Tax Rate
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
IMF	International Monetary Fund
KES	Kenya Shillings
LDCs	Less Developed Countries
MENA	Middle East and North Africa
MNE	Multinational Enterprise
PWC	Price Waterhouse Coopers
SPSS	Statistical Package for Social Sciences
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
USA	United States of America

CHAPTER ONE

INTRODUCTION

1.0 Chapter Overview

This chapter provides background of the study, statement of the problem, objectives, hypotheses, significance and scope of the study. The purpose of the study was to investigate the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya.

1.1 Background of the Study

Foreign Direct Investment (FDI) has risen rapidly globally, because it is a significant form of international capital inflows, as well as because of its ability to turn emerging economies financially and politically (Adam & Tweneboah, 2009). The efforts of developing countries to attract FDIs are based on potential positive effects on the domestic economy, according to Njuguna (2016), such as increasing productivity, complementing domestic private investment, technology transfer, management and technical skills, the provision of an international production network, training of employees, job creation and easy access. Global studies show that tax incentives are one of the major factors driving FDI inflows into a given country (Loyford & Moronge, 2014).

FDI is the net inflows of investment from one economy to another, so FDI is calculated by the net inflow, which is the remainder of the first inflows of investment after withdrawal of the divestiture, estimated as a percentage of the GDP of the economy (Shahbaz, Lean & Kalim, 2013). FDI is useful for multinational companies as it is a way to reach the markets, access resources, and reduce production costs. It also benefits the invested nation as it generates much-needed domestic investment capital, creates

job opportunities for locals, introduces new management skills and strategies, business practices, technology and economic principles that ensure local markets, new industries and increased growth in sales that contributes to economic growth (Karthik & Kannan, 2011).

In Africa, legitimate reasons as to why tax incentives are ideal for investments exist although strong reasons also exist as to why the economic and fiscal costs could be relatively higher than the returns. Tax incentives have struggled to achieve higher investment in some countries. However, in some circumstances, without substantial reductions in investment inflows into the host nation, the incentives have been eliminated (UNCTAD, 2012).

While FDIs face many constraints, the absence of well-structured and attractive tax incentives appears invariably to be a major obstacle to the growth of FDIs in previous surveys. In African countries such as South Africa, Ghana and Nigeria among others, tax incentives contribute to the promotion strategies of the government. Different countries have adopted various tax incentives so as to boost growth, attract FDI, promote technological transfer and diversify production. Taxes influence the net return on capital and most policymakers consider it to have great impact on capital movements between nations (Morisset & Pirna, 2011).

Kenya has become very active for oil exploration, with the entry of major companies including Tullow oil, BG Group, Apache, Africa Oil, Marathon, Total, ENI, Anadarko and Camac Energy (Skouloudis *et al.,* 2011). As an economy, Kenya revolves around the oil and gas sector because, as a primary revenue earner, it exerts a huge impact on the economy. Oil and gas play a critical role in maintaining prices of goods and services

at their minimum levels. On the other hand, increased fuel prices may trigger high transport costs leading to increased prices of consumer goods and services. In the global energy system, oil and natural gas are major and dominant components (Roupas *et al*., 2011).

In 2008, Kenya unveiled its 2030 vision with the goal of achieving global FDI competitiveness and economic growth, among other items. In Kenya's FDI inflow patterns, beginning with the period 1970-1980, there have been inconsistencies. The relatively high level of development, good infrastructure, market size, growth and openness to FDI led to the selection of Kenya as their regional hub by multinational corporations at a time when other countries in the area had relatively closed regimes (Kinuthia, 2010).

1.1.1 Foreign Direct Investments

Muema (2013) defined Foreign Direct Investments (FDI) as long-term investments outside the investor's physical or economic limits. The FDI recipient country is equipped with both the capital flow and the technology flow that will aid in its growth. When a country wants to invest in another, the benefit it hopes to achieve must be greater than the risks it must face. UNCTAD (2012) describes three different FDI forms. There are: reinvested dividends, equity capital and other capital comprised mainly of intercompany loans.

Foreign direct investment generates new employment opportunities as the transfer of expertise and technical know-how as well as the provision of jobs is done while setting up business, hiring and educating the locals in the host country. FDI reflects long-term

host-country obligations, according to Kinuthia (2010). It is a preferred form of investment because it has no responsibilities to the host country.

Over the years, foreign direct investment has not been constant, with low inflows over some periods being recorded. Due to a decline in economic productivity, as well as increasing problems with poor infrastructure and high living costs, FDI in the oil and gas sector was low in the 1980s and 2010s, which had a significant negative impact on FDI inflows in Kenya (KPMG, 2012). In total, Kenya has more than 200 multinational companies in all sectors, with the main traditional sources of FDI being Britain, the USA, Germany, South Africa, the Netherlands, Switzerland, China and India (Selma, 2013).

For several foreign companies, Kenya serves as the East African business center. This translates into the reliance of FDI on the inflow of capital, which, in turn, reflects the supply of employment and the economy that these foreign investments help to develop. Kenya's FDI average percentage growth between 2007 and 2016 was 40 percent (40 percent) with inflows mainly channelled to retail and consumer goods, technology, media, telecommunications, minerals, oil and natural gas sectors from the UK, USA and India (Ernest & Young, 2015). In 2016, FDI inflows amounted to USD 1076.9 million (KES 105.29 billion), up from USD 670 million (KES 65.51 billion) the year before, a 60% (60%) increase. This money went mainly to the sectors of oil, gas and manufacturing (UNCTAD, 2016).

1.1.2 Tax Incentives

Tax incentive is the tax obligation deduction, exclusion or exemption given as an incentive to participate in a particular investment operation (Prichard, 2016). In Kenya,

investment allowances, tax exemptions or reduced tax rates, special economic zones and tax credits are among the most prevalent tax incentives. In particular, tax incentives are in the form of capital market incentives, capital credits, EPZ bonuses, and export tax remissions.

Most developing countries prefer to use tax holidays as tax incentives. According to UNCTAD (2000), tax holidays is an incentive where paying of CIT by new foreign establishments is exempted for a specified period of time, likely five years in most cases. Still, other tax liabilities the firm faces may also apply from the provision of the tax holiday, for instance, import duties and VAT from raw materials. Tax holiday incentive is a temporary measure and in most cases the exemptions of administration tax on firms is rendered during holiday seasons (Munongo, Akanbi & Robinson, 2017).

Tax incentives expand the horizon of investment opportunities and also promote the advancement of social welfare through incentives related to education and health care. Additionally, tax incentives help to reduce overreliance on agricultural production which is affected by market instabilities (Jirasavetakul & Rahman, 2018).

Proponents of tax benefits point out that, as a result of reduced tax costs, investors receive a higher rate of return, enabling them to re-invest with the additional revenue received. The host country thus increases its revenue, benefits from the transfer of technology and attracts increased FDIs. In less developed countries (LDCs), it is also argued that it is necessary to provide tax incentives to investors since these countries usually have very poor investment climates, such as dilapidated infrastructure, political uncertainty, macro-economic volatility and high business costs (Basu & Srinivasan, 2012).

Reducing the investment tax burden could mean reducing government spending or transferring the tax burden to other tax bases, such as labor, for example. Tax policy makers also need to understand whether investment taxes matter and how much they do (Keen, 2012). A sound tax policy decision should carefully weigh the benefits of a reduction in corporate taxes against the costs. It is clear that nations around the world have engaged in the process of attracting FDI through various means and instruments, including tax incentive economies (Keen, 2012).

1.1.3 The Oil and Gas Sector in Kenya

The oil and gas sector in Kenya is largely split into three segments: upstream (exploration and production), mid-stream (storage, refining and transport) and downstream (supply and distribution). The upstream section mainly includes the processes of crude oil and natural gas exploration, growth and production (Barua, 2010).

In the midstream segment, processes involving the storage, refining and transportation of crude oil into consumable oil and gas products are involved. There is only one refinery in Kenya today, which is Kenya Petroleum Refineries Limited, based in Mombasa. The downstream section includes the mechanism by which refined goods are made available to customers by, for example, supply and distribution at manufacturing and petrol stations. In Kenya today, with a multitude of players, there is a reasonably well-developed network of transport pipelines, storage and retail outlets (Barua, 2010).

The study centered on the upstream segment, which is involved in the processes of crude oil and natural gas exploration, growth and production. Tullow Oil, Zarara, ENI,

Total and Africa oil are the main businesses that constitute the upstream segment. The gas and oil sector is regarded as one of Kenya's key contributors to FDI inflows. Over the years, however, FDI has not been consistent with some times of recorded low inflows. This study therefore sought to investigate the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya.

1.2 Statement of the Problem

Foreign direct investment plays an important role in the growth of economies worldwide. In Kenya, FDI inflows are important for job development, the introduction of new management skills and techniques, business practices, technology and economic principles that ensure the growth of local businesses, new industries and increased revenue that leads to economic growth (Karthik & Kannan, 2011). According to Feldstein (2010), FDI integrates emerging technology, resulting in new methods of production as well as diversification of the output and production of a range of products.

In the recent past, Kenya has continued to report low inflows despite the important role played by FDI inflows. The report of the United Nations Conference on Trade and Development (UNCTAD, 2016) reported that Kenya was among the countries that in 2016 received less inflows of foreign direct investment compared to the previous year. The report showed, in particular, that FDI inflows to Kenya fell by 36% from Ksh 63.59 billion to Ksh 40.7 billion, even as inflows to East Africa grew by 13%. In addition, the UNCTAD (2018) study reported that Kenya's FDI inflows dropped to $0.3 billion in 2018 from $0.7 billion in 2017, a 57.1 percent decline. This clearly indicates that reduction in FDI inflows to Kenya is a persisting problem that needs attention.

The movement of individuals, capital and materials to invest in the host country anywhere in the world can be influenced by a robust tax structure. Again, many stakeholders agree that foreign investment is facilitated by a flexible tax policy and tax incentives, thereby helping the host nation to stem the tide of unemployment that generates economic growth (Easson & Zolt, 2012). Many studies have focused on the role of tax incentives in promoting FDI, but their relative effect has not been clearly defined (Voorpijl, 2011). The influence of tax incentives on foreign direct inflows is important, Hartman (2014) and Young (2013) contend. Morisset (2013) and OECD (2013) claim that the tax incentive strategy has had mixed results and has been criticized by OECD countries and multilateral organizations because it has also been linked to illicit capital flows. Morisset (2013) argued that the question is if, whether it had provided incentives or none at all, the new investment would have come to the nation or not if so then free-rider investors would benefit, while the treasury loses and the economy reaps no net profit.

These issues have highlighted the need to clearly assess the impact of tax incentives on FDI, both locally and globally. In addition, the studies reviewed in Kenya did not show how tax incentives have an effect on FDI in the oil and gas sector. This study aimed to fill the research vacuum by exploring the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya.

1.3 Objectives of the Study

1.3.1 General Objective

The general objective of the study was to investigate the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya.

1.3.2 Specific Objectives

i. To determine the effect of capital deductions on foreign direct investment in the oil and gas sector in Kenya.
ii. To establish the effect of income tax on foreign direct investment in the oil and gas sector in Kenya.
iii. To examine the effect of VAT incentives on foreign direct investment in the oil and gas sector in Kenya.
iv. To establish the effect of import duty incentives on foreign direct investment in the oil and gas sector in Kenya.

1.4 Research Hypotheses

i. H_{01}: There is no significant effect of capital deductions on foreign direct investment in the oil and gas sector in Kenya
ii. H_{02}: There is no significant effect of income tax on foreign direct investment in the oil and gas sector in Kenya
iii. H_{03}: There is no significant effect of VAT incentives on foreign direct investment in the oil and gas sector in Kenya
iv. H_{04}: There is no significant effect of import duty incentives on foreign direct investment in the oil and gas sector in Kenya

1.5 Significance of the Study

The study's findings provide a more precise and in-depth understanding of the effects of tax incentives on foreign direct investment in the oil and gas sector in Kenya as a whole and help shape the future policy formulation of the sector, thereby greatly facilitating the achievement of the country's goals of improving the reliability and efficiency of foreign direct investors.

The taxation regime for the oil and gas in Kenya, which is a specialized sector is still very new and is still growing. Through the findings of this study, the policymakers will find ways of balancing between attracting investment and optimizing tax revenue for development.

The study will also be instrumental for new investors and those already present in Kenya since it will arm them with knowledge while making investment decisions

Through this analysis the researcher was able to share a deeper and wider understanding of the impact of tax incentives on foreign direct investment in the oil and gas sector in Kenya, thus obtaining more knowledge in a field that the researcher may not be familiar with. The results of the study will serve as literature for scientists to shed more light on the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya.

1.6 Scope of the Study

The objective of the study was to examine the effects of tax incentives on foreign direct investment in Kenya's oil and gas sector. The oil and gas sector was ideal for the research. The research was in reference to five oil and gas companies namely: Tullow Oil, Zarara, ENI, Total and Africa oil that are still operating in Kenya to date. These companies also have their main offices in Nairobi and therefore, it was easy for the researcher to access them. The five oil and gas companies formed the study target population. A census of all the five companies was done. The research was carried out in 2020.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

The chapter presents the study concepts, review of past studies, theoretical review, critical analysis, research gaps and conceptual structure.

2.1 Review of Study Concepts

This section provides review of the study concepts. It outlines the meaning and measurements of the variables.

2.1.1 Foreign Direct Investment

In order to monitor the production and distribution of a company's activities in the host country, FDI is the mechanism by which domestic individuals acquire ownership of assets (Maiga, Oumarou & Coulibaly, 2019). Foreign direct investment is considered by the International Monetary Fund (IMF) to be an international investment branch where an investor acquires a long-term interest in an undertaking in one economy residing in another economy. Not only does foreign direct investment carry money, but it also speeds up the transition of technology, operational and management processes and skills, as well as the strengthening of international business relations.

According to Shah and Ali (2016), FDI has for a long time been linked with the growth of international business and remains the basis of operation of MNCs. FDIs are in most cases created by MNCs and operate as a component of the parent corporation’s attempt to defend its ability to gain profits from the control of intangible assets in line with emerging competitive forces domestically and abroad. Lawana (2016) noted that FDI

is premised on gaining higher profits from control of business operations in foreign countries.

The rise of FDI is regarded as a positive aspect in both the organization, social and economic perspective. Tax incentives and tax reductions are used by countries as instruments to stimulate FDI inflow. For instance, China has effortless reduced their taxes from 30% to 15%-24% to steer investments endeavors in specific parts of the country. Romania is another example whereby various companies have been exempted to pay custom duties and corporate duties to allow investments in the country. Such measures are directed to stimulate the countries' economies, and in the end through social contributions and the employee's personal income tax will increase in the state budget (Jirasavetakul & Rahman, 2018).

2.1.2 Tax Incentives

Tax incentives can be described as a tax liability deduction, exclusion or exemption provided as an incentive to participate in a designated investment activity (Prichard, 2016). In Kenya, investment allowances, tax exemptions or reduced tax rates, special economic zones and tax credits are among the most prevalent tax incentives. Tax incentives specifically take the form of capital market incentives, Capital allowances, EPZ benefits and tax remissions for exports.

Irokwe and Nnaji (2017) identified tax incentives as special arrangements in tax laws to: attract, retain or increase investment in a specific field, stimulate growth in specific areas and assist companies or individuals engaged in the activities specified. They further noted that the underlying basis is to ensure the overall growth of the economy and also the development of all industries. It can therefore be inferred that tax incentives

are tax concessions in order to stimulate or promote particular policies aimed at stimulating investment in certain industries or geographical areas.

Tax incentives have been extensively used as drivers of investment. Countries such as Ireland, Mauritius and Singapore have realized high levels of investment through adoption of fiscal incentives. Despite the success attributed to incentives in some countries, a number of others have not realized the anticipated investment outcomes (Sunny & Shu, 2019).

By granting tax incentives, the horizon of investment opportunities is expanded. At the same time, tax incentives promote the advancement of social welfare through incentives related to education and health care. Additionally, tax incentives help to reduce overreliance on agricultural production which is affected by market instabilities (Jirasavetakul & Rahman, 2018).

2.2 Theoretical Review

This section provides a review of theories that underpin the study. These are theory of innovation diffusion, social exchange theory and stakeholders' theory.

2.2.1 Theory of Innovation Diffusion

Rogers (1995) introduced the theory of innovation diffusion that is based on the notion of the spontaneous or planned dissemination of new ideas concerning the introduction of innovation. Rogers describes innovation as a perceived fresh concept, practice or object. The theory emphasizes that the perception of change is essential and that it should be regarded as an innovation if and when the concept appears new to the prospective adopter.

It is proposed that the nature of an invention in the innovation diffusion hypothesis is seen as creating confusion in the minds of prospective adopters (Omesa, 2015). In this situation, the absence of predictability and data relates to uncertainty. Among members of a communicating social network, diffusion is further characterized as a method of data exchange motivated by the need to decrease uncertainty. Uncertainty, along with the comparative probabilities of each of these solutions, can be regarded as the degree to which, in relation to the occurrence of a particular event, a set of solutions is viewed. To minimize this ambiguity, those interested in considering the acceptance of innovation are encouraged to look for data (Ajemije, 2020).

The theory argues that data is embodied by a technological innovation, so its implementation acts to decrease uncertainty. The theory is important in this study since it emphasizes the aspect of creating fresh thoughts that can assist improve an organization performance. Likewise, in terms of attracting FDI, new ideas such as the use of tax incentives will enable oil and gas companies to boost their efficiency. As such, the innovation diffusion theory supports the utilization of tax incentives including capital deductions, income tax, VAT incentives and import duty incentives in order to enhance foreign investment inflow.

2.2.2 Social Exchange Theory

The Social Exchange Theory (SET) was developed by Homans (1958) and views human beings as rationally seeking to maximize their material benefits from transactions with others in a free and competitive market place. However, contemporary SET theorists have recognized that the actions of human beings are not always the way utilitarian thoughts portrayed them, though the assumption underlying SET is that in their trade transactions with others, human beings are often trying to make a profit,

which is regulated to a significant extent by considerations of both material and non-material costs and benefits (Binyamin, Friedman & Carmeli, 2018).

Roch, Shannon, Martin, Swiderski, Agosta and Shanock (2019) noted that the reciprocation increases when both partners in an organization provide timely resources to the other. The resources to be exchanged becomes impersonal when it involves financial incentives or socio-emotional when it involves such attributes as care, respect, and loyalty. Most notably, these relationships are used to explain the positive results that come about when employees respond to perceived organizational support (Liaquat & Mehmood, 2017). In an exchange arrangement, where the other has provided advantages in the past or is expected to do so in the future, one party offers benefits to the other party. One party will be willing to extend benefits to the other because in return, they will expect to receive benefits in equal measure from the other (Nazir, Qun, Hui & Shafi, 2018).

In this analysis, the theory of social trade supports the idea that the government provides the oil and gas industry with tax incentives (capital deductions, income taxes, VAT incentives and import duty incentives) in exchange for a rise in foreign direct investment. Therefore, the theory describes the link in the oil and gas industry between tax incentives and FDI inflows.

2.2.3 Stakeholders Theory

Edward Freeman (1984) introduced the theory that considers a stakeholder as a group or individual with an impact on or is affected by an organization's performance and goal attainment. The stakeholder theory holds that organizational management should identify persons of interest or groups that are affected by an organization or project,

understand their needs, and stipulate measures necessary to cater for the needs of the interest groups and persons (Bonnafous-Boucher & Rendtorff, 2016). Highlighted responsibilities towards stakeholders include efficient use of capital, timely provision of accurate information, and effective business management. Taking Freeman's definition of stakeholders, internal and external stakeholders, based on their level of power and interest, unilaterally determine the strategy of an organization.

Notably, stakeholders play a crucial role in strategy implementation and influence the success of an organization. Freeman, Harrison and Zyglidopoulos (2018) noted that effective stakeholder management involves proper management of the relationship between an organization and its stakeholder. In particular, it's essential for an organization to focus on proper contracting, communication, motivation, and management of partnerships. According to (Al-Nasser & Muhammed, 2017) organization's that address the needs and interests of stakeholders perform better than organization's that fail to pay attention to stakeholders.

The instrumental perspective of stakeholder management posits that maintaining healthy relationships between stakeholders and an organization increases the firm's value, which has a positive implication on a firm's overall performance (Bonnafous-Boucher & Rendtorff, 2016). Effective management of performance drives favorable interest by stakeholders towards the organization. Notably, stakeholders have a perceived stake and expectations in an organization or project, and the perception often influences behaviors, which could be destructive or constructive for an organization. In essence, maintaining open and effective communication with stakeholders, whether direct or indirect, influences their perceptions toward the firm, which affects their response and behavior.

The principle is relevant in this analysis as it lays a foundation for stakeholder human resource and communication management. In essence, addressing stakeholder human resource and communication management needs in an organization directly fulfills the premise of catering for the needs of the stakeholders. Furthermore, articulate engagement of internal stakeholders informs the objective of stakeholder capacity building particularly in the case of empowering internal stakeholders. In turn, it's possible to analyze the effect of the study objective and stakeholder engagement to project performance.

According to Gross (2015), the theory evaluates the efficiency of a company's policy based on the expectations of the stakeholders. Any company's performance draws interest from a number of key parties. The main stakeholders interested in the performance of the companies are investors/owners, vendors, clients and staff in the case of small and medium enterprises. Stakeholders are therefore worried with the company's behavior and operations to ensure enhanced profitability. Some of the performance factors that stakeholders are interested in, based on the concept, include sales, liquidity and returns on investment. Investors' interest is in returns on investment, maximizing their wealth.

The stakeholder principle is imperative in this analysis as it brings out the expectations that stakeholders have in regard to their company's performance. Based on the theorist argument, stakeholders expect the company to perform well and to yield high returns. In the case of oil and gas industry, the expectation is that the industry will attract high FDI inflows. The theory thus supports the dependent variable in this study which is FDI.

2.3 Empirical Review

This section provides a review of past studies related to the study variables with an aim of identifying prevailing research gaps.

2.3.1 Capital Deductions and FDI

Bernstein and Anwar (2014) developed a dynamic development model to analyze the impact of tax policies on input demands and output supplies for manufacturers operating in selected industries in Mexico, Turkey and Pakistan. The tax advantages related to these sectors have included investment exemptions, accelerated capital consumption allowances, reductions in corporate income tax rates and investment tax credits. The results of the Bernstein-shah model suggest that for the six industries studied in the three countries, tax incentives for investment and production decisions are necessary. In addition, some tax incentives have been found to be more effective than others in stimulating investment per dollar in Treasury revenue losses. Among the incentive measures tested were investment allowances, accelerated depreciation provisions and investment tax credits, which proved to be cost-effective instruments to stimulate investment in Turkish industries.

Tapang (2018) looked at the effect of tax incentives on foreign direct investment in the petroleum industry in Nigeria. In the petroleum industry, the tax incentive issue has not really earned positive attention because individuals believe that the sector is wealthy enough to pay all taxes. Although tax incentives are weak in the oil sector, they can't be contrasted with what we have in the private sector. The issue of high tax rates, numerous taxes, complex tax laws and a lack of sufficient tax-related education or education is the ability to sustain and develop the petroleum sector. These have led to an increase in the record of petroleum industry shortages in Nigeria. An ex-post-facto

system has been adopted for review. The findings have shown that the tax advantage proxy for investment tax credits, non-productive leases and capital allowances has had a major effect on foreign direct investment. It is inferred, on the basis of the findings, that companies obtaining tax benefits will generate more work opportunities than companies in highly taxed regions. A favorable investment climate is a powerful prerequisite for the flow of sustainable physical investment in an economy. Tax incentives have a positive impact on living standards and income from capital and improve the option of goods at the disposal of clients.

Lawson and Bentum-Micah (2019) assessed the efficacy of targeted government policies and investment agreements in developed countries in attracting FDI flows. The influence of economic variables such as the existence of infrastructure, labor costs, annual gross domestic product rise, actual effective exchange rate and tax incentives, as well as bilateral investment treaties, on foreign direct investment inflows over a 30-year period in Ghana has been explored in order to achieve this. The study found that FDI inflows differ across the systemic break studied and that a limited percentage of bilateral investment treaties are expressed as a contributing factor to FDI. National policies have, however, proved to play an important role in attracting FDI into Ghana.

Tapang (2018) looked at the effect of tax incentives on foreign direct investment in the petroleum industry in Nigeria. In the petroleum industry, the tax incentive issue has not really earned positive attention because individuals believe that the sector is wealthy enough to pay all taxes. Although tax incentives are weak in the oil sector, they can't be contrasted with what we have in the private sector. The issue of high tax rates, numerous taxes, complex tax laws and a lack of sufficient tax-related education or education is the ability to sustain and develop the petroleum sector. These have led to

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Mutisya (2019) has examined the impact of tax incentives involving investment deduction allowances, industrial building allowances and export promotion incentives on foreign direct investment in Kenya. An explanatory research design based on a 32-year time series period starting from 1985 to 2016 followed this report. Secondary time series knowledge was used in this study. As the data was quantitative in nature, it was interpreted using descriptive and inferential statistics. The descriptive statistics included frequency distributions, mean, standard deviation and percentages. Correlation analysis and regression analysis of multivariates is used as inferential statistics. The findings have shown that the investment deduction allowance has had a positive and important effect on foreign direct investment in Kenya. The study concludes that an export promotion incentive, followed by an industrial building allowance and an investment deduction allowance, was the most significant impact on foreign direct investment. The study shows that the government needs to educate the general public about the capital allowances that are awarded to FDIs and to local businesses. In addition, there should be an incentive for a short-term strategy tailored

for individual businesses to draw up FDIs, while a long-term strategy should be to improve infrastructure, protect and reduce strict policies and regulations.

Gitonga (2017) explored the relationship between tax incentives and foreign direct investment inflows by multinational firms in Kenya. The analysis gathered secondary expertise. Data was gathered from a time series spanning twenty years (1995-2015). The study findings demonstrated that there was a strong link between wear and tear allowances and FDI inflows. This was an indication that the period of study (1995-2015) FDI inflows of multinational corporations in Kenya was a result of attraction from wear and tear allowances; a correlation coefficient of 0.5465 confirmed this relationship. However, investment deductions and industrial building allowances had no any significant relationship on FDI inflows.

The influence of tax incentives in attracting and maintaining FDI in export processing zones was examined by Thuita (2017). For the analysis, a sample size of 72 employees of companies operating under EPZs was chosen using a stratified method for companies and a purposeful method for respondents. Using self-administered questionnaires, the study used a descriptive survey design. The research showed that the use of capital deductions substantially affects FDI attraction and retention. The study concludes that tax incentives to boost the growth and expansion of foreign direct investors should be increased. However, as it did not focus on the oil and gas market, the study poses a contextual void.

2.3.2 Income Tax and FDI

Munongo and Ribinson (2018) conducted a research analysis on whether tax incentives attract foreign direct investment within the Southern African Development Community

(SADC). This study provides a detailed analysis of the effects of each tax incentive on the attraction of FDI to SADC by differentiating between the individual tax incentives used in the field of SADC. The tax advantages used in the study are tax holidays, corporate income tax, losses carried forward and decreased CIT in unique industries. The results showed that tax holidays are explained positively by FDI and CIT and have a negative impact on FDI inflows into SADC. Losses carried forward are negligible, though decreased CIT negatively affects FDI inflows into SADC in particular sectors.

Hsu, Lee, Leon-Gonzalez and Zhao (2019) used the provincial-level panel data for 1998 to 2008 before the reform in order to study whether the tax incentive was a significant determinant of foreign investment decisions. We find that the size of the market and the geographical location have had a major impact on FDI inflows to China, but tax incentive policies have not been a sufficient determinant of FDI inflows to China over the periods studied, providing a justification for the termination of FDI tax incentives at the time of the 2008 reform in China.

Murage et al. (2019) examined the relationship between tax incentives and FDI in the East Africa Group Member States. A descriptive study design panel was used for the evaluation of the relationship between tax incentives and foreign direct investment in the Community Partner States of East Africa, including Tanzania, Rwanda, Kenya, Burundi and Uganda. The research used secondary panel data from 2002 to 2017, which covered a period of 16 years. The study found that the duration of losses carried forward had no statistically significant effects on the inflow of FDI. Investment allowances, however, had a statistically positive effect on the inflow of FDI into the EAC. The study concluded that the investment allowance had a major influence on FDI inflows among the partner states of the East African community.

Olaleye, Riro and Memba (2016) analyzed the impact of company income tax advantages on foreign direct investments in Listed Nigerian Manufacturing Firms. The study adopted a descriptive research design and gathered primary data using questionnaires. With about 56,000 workers, the 74 listed manufacturing companies were the target population of the study. A sample size of 352 respondents from thirty-two (32) manufacturing firms was selected from seventy-four (74) firms using stratified purpose sampling and respondents were divided into three layers; top, middle and lower management classes. The descriptive statistics adopted were: frequencies, mean and standard deviation, while inferential statistics consisted of correlation and regression analysis. The results revealed a clear positive linear association between reduced incentives for corporate income taxes and foreign direct investment.

Lodhi (2017) researched the incentivized tax policy and its impact on investments in Pakistan. The analysis was mainly based on a quantitative investigation methodology and was intended to provide insight into the effect of tax and tariff rate changes on domestic investment, while evaluating and assessing the impact of tax and tariff rates on FDI. The research used both ARDL and regression analysis methods to analyze the relationship between the corporate tax rate, tariff rate, and domestic investment. The study's results showed that the corporate tax rate was substantially negatively related to domestic expenditure and FDI.

The effect of the corporate income tax rate on foreign direct investment (FDI) was investigated by Mandinga (2015) for Small Island Developing States (SIDS). We plan to verify whether the effective corporate income tax rate, the gross domestic product (GDPc) per capita, the size and development of the economy, the degree of transparency, the availability of natural resources, the growth of the financial sector and

the macroeconomic and political stability of the 22 SIDS countries studied between 2004 and 2013 have an impact on FDI activities. Based on data collected from the World Bank, UNCTAD and PWC Annual Reports, empirical evidence is presented. The results of the partial adjustment model with panel data show that FDI is negatively linked to both the corporate income tax rate and the initial role of fiscal policy in attracting FDI and the growth of the financial sector, demonstrating the inefficiency of the domestic finance sector in supplying the capital needed by FDI. Furthermore, per capita GDP, the size and growth of the economy, the degree of openness, and macroeconomic stability are positively related to FDI.

2.3.3 VAT Incentives and FDI

Olaniyi, Oyedokun and Ajayi (2019) have examined the impact of tax policy incentives on the inflows of foreign direct investment into Nigeria. The effects on the inflow of foreign direct investment into the country of corporate income tax incentives, incentives for petroleum gain taxes, incentives for value added taxes and incentives for customs and excise duties was directly investigated from 1994 to 2016. This study adopted the ex-post-facto style of research. The study found that customs and excise duties and value-added tax incentives had a significant impact on foreign direct investment in the region, while company income tax and oil tax incentives had a marginal effect on foreign direct investment. The study concluded that a powerful driver of direct foreign investment in Nigeria's economy is tax incentive policies.

The contribution of tax incentives to FDI inflows to Nigeria, Ghana and South Africa was evaluated by Ugwu (2018), as well as the effect of such FDI inflows on exports from those countries after the adoption of IFRSs from 1999-2015. The Ex-post-facto research architecture was adopted. In order to collect and interpret secondary data,

descriptive and inferential statistics were used. The results showed that there was a strong relationship between tax incentives and FDI and that FDI had no major impact on exports from Nigeria, Ghana and South Africa. In addition, there was no major difference in the effect of FDI on exports from all the countries analyzed in their pre- and post-IFRS adoption periods. This means that the lower the corporate tax rate, the higher the increase in other tax benefits, the higher the amount of FDI inflows to those countries, and the significant amount of FDI inflows to those countries would have a huge effect on exports.

As a case study using SMEs in Nyarugenge, the effect of tax incentives on the growth of small and medium-sized enterprises (SMEs) in Rwanda was studied by Twesige and Gasheja (2019). It has followed the approach of qualitative and quantitative analysis. The population includes 49000 small and medium-sized enterprises working in the district of Nyarugenge from the agricultural, manufacturing, service and tourism sectors. A sample of 136 SMEs was measured using Silovin and Yemen's sample size formula. In order to select the sample, basic methods of random and purposeful sampling were used. The data set was analysed using descriptive statistics. A multiple regression analysis was used to explain the relationship between variables. The study showed that the relationship between tax incentives and the growth of small and medium-sized enterprises was strongly positive and significant. The study concluded that tax incentives are the key to sustainable SME development.

Narayana (2015) stressed in his study that the experiences of many developing countries have shown that if properly designed and implemented, VAT will prove to be a better resource mobilizer than the existing sales tax systems. Owolabi and Okwu (2014) reviewed the importance of VAT and noted that developed countries are

increasingly realizing the essential position of value added tax as an instrument of economic development.

Bahizi (2016) assessed the impact of monetary policy and tax incentives on attracting FDI in Rwanda. Using a purposeful sample size of 80 respondents, the investigator conducted the study using structured interviews, questionnaires, and secondary data. The Tax Administration Body (RRA) and Foreign Private Companies conducted this report. The investigator concluded that Rwanda's investment code is phenomenal, attracting foreign investors. A significant measure is tax enforcement among foreign investors in Rwanda. Rwanda's tax structure makes a major contribution to the reduction of tax aversion among investors. The exemption is the most important tax incentive form to be highlighted. The indirect impact on revenues can be beneficial because new investments, realized by tax incentives, create new jobs and are related to the results of generating tax revenue. Furthermore in Rwanda, other variables would also appeal to FDI.

The results of research on tax incentives and foreign direct investment in the Middle East and North Africa (MENA) region by Onyeiwu and Shrestha (2015) show that VAT does not have a significant impact on the flow of FDI into the MENA region. In order to attract FDI, certain MENA states should pay more attention to non-VAT. The alternative hypothesis suggests that the listed Kenyan manufacturing companies have a substantial relationship between VAT incentives and FDI.

Kuria (2017) analyzed the impact of corporate income tax incentives and VAT incentives on EPZ corporations' outcomes in Kenya. The thesis adopted a methodology of analysis which is descriptive and explanatory. The study used both primary and

secondary data. The results showed that the relationship between corporate income tax incentives and VAT incentives and the performance of EPZ companies was positive and substantial. Based on the findings, the study concluded that the government should continue to grant tax exemptions in order to attract and maintain foreign investors in the country.

2.3.4 Import Duty Incentives and FDI

Gumo (2013) examined the effect on foreign direct investment in Kenya of tax incentives. The analysis adopted a descriptive design for research and gathered secondary data. The study found that Kenya has numerous tax incentives provided to resident businesses, including import duty. The results revealed a positive and important correlation between import duty and inflows of FDI. The study concludes that tax incentives would have a positive resulting effect on FDI and recommends that in order to promote investment, the government should revisit its policy on tax incentives and balance against accruing benefits, including by implementing evidence-based tax incentives to reduce tax evasion. However, since it did not concentrate on the oil and gas industry, which is the focus of the proposed report, the examined study poses a contextual void.

The efficiency of tax incentives in attracting foreign direct investment to Ethiopia was examined by Bora (2013). It also analyzes the differential effects of tax benefits on various industries by splitting FDI into 10 sectors. Dummy variables are used in the sectors under consideration to show the existence and absence of tax benefits, tax holidays and exemption from customs duties. The study uses panel data on 10 industries over the 1992-2012 period and an econometric model that covers tax holidays, customs duty exemptions and control variables. The empirical result shows that only tax

holidays were found to be important to tax benefits, while in the general model, the customs duty exemption was negligible. Economic openness was important among the control variables. However if the sectoral allocation of FDI is taken into account, tax holidays only have a significant effect on the manufacturing sector, while the customs duty exemption has a significant impact on the building, energy and water supply sectors. This outcome implies that FDI's exposure to tax incentives depends on the sector to which the investment flows. Since it was conducted in Ethiopia, the analysis under review presents a conceptual difference, while the proposed study will concentrate on the Kenyan oil and gas industry.

In view of current evidence of tax incentive shortcomings, developing countries have gradually resorted to using tax incentives to attract FDI. A common feature of many investment codes in sub-Saharan Africa is tax incentives. Sub-Saharan African countries see tax incentives as a means of attracting FDI, as there are no feasible alternatives per se, and accept that tax incentives should be structured to ensure that FDI advances socio-economic and technological development. Reliance on tax incentives at the expense of maximizing domestic tax revenues, however, poses a challenge to sustainable development. Ofori (2019) has analyzed Ghana and Kenya to see which of them will better achieve this balance and to make suggestions on how this balance can be improved. The analysis found that there is no successful tax incentive design and administration. The recommendations suggest that legislative and administrative reforms be made in order to make tax incentives more efficient.

One of the most significant stimuli for improving the host countries' economy is the inflow of foreign direct investment. It is therefore not surprising that countries' governments show a strong interest in foreign capital inflows and create favorable

conditions for investors. Investment rewards take different forms and are offered within the framework of goal projects as well as regulated by laws. The study by Ślusarczyk (2018) offers two of the most important examples of supporting FDI with tax incentives in Poland: State funding for Special Economic Zones (SEZ) investors and, subsequently, the exemption from property tax provided to investors by individual municipalities. A study of the legal documents and public assistance reports published in Poland, an evaluation of the activity of the Special Economic Zones and several other validated studies were the subjects of the thesis. As a result of the considerations undertaken, it is clear that foreign investors, as confirmed by the value of the capital invested by them in the form of FDIs, frequently and significantly benefit from the incentives offered by the Government of Poland. The reviewed study reveals a conceptual gap because it did not specifically focus on import duty incentives as is the case in the proposed work.

Ngure (2018) assessed tax incentives and their impact on the production of selected manufacturing companies in Kenya. In particular, the study sought to investigate the effect on the production of selected manufacturing companies in Kenya of incentives for customs duties. The researchers followed a descriptive study style. As of 2016, the study population consisted of all 725 manufacturing companies in all categories under the Kenya Association of Manufacturers directory. A pooled panel regression model was used to test the importance of the effect of the independent variables on the dependent variable. The study period was 2017 and knowledge was collected from 2011 to 2016. Custom duty rewards were found to have a positive and important impact on the company's performance, even though their impact on performance was the least. The report exposes a conceptual difference since it focuses on the output of

manufacturing companies, while FDI will be the subject of the proposed study. In addition, because the checked work used secondary data, there is a methodological discrepancy, which is used by primary data in the proposed research.

2.4 Critique of Literature Review

The reviewed studies investigated the connection between tax incentives and FDI. However, most of these studies have been conducted in other countries such as Mexico, China, Pakistan, Turkey and Nigeria (Lodhi, 2017; Bernstein & Anwar, 2014; Feldstein, 2010; & Olaleye, Riro & Memba, 2016). The mentioned countries operate in a different economic and political environment from that of Kenya. For example, China is the second richest Country in the world and happens to be a developed country. It would therefore be impractical to generalize findings of a study conducted in China to fit in the Kenyan context.

On the other hand, local studies have attempted to investigate the effect of tax incentives on FDI (Gitonga, 2017; Murage *et al*., 2019). However, these studies have aggregated FDI inflows from all sectors. It is, therefore, difficult to tell the specific inflows through the gas and oil sector. By examining the effects of tax incentives on foreign direct investment in the oil and gas sector in Kenya, the current study sought to resolve these limitations in literature.

2.5 Summary of Previous Studies and Research Gaps

A critical review of past literature shows that several conceptual, contextual and empirical research gaps exist in attempts to research the effect of tax incentives on foreign direct investment (FDI). Klemn and Parys (2009) performed an empirical study to address the question of how effective tax incentives are in attracting investment. In

over 40 Latin American, Caribbean and African nations, information was gathered between 1984 and 2014. The results have shown that lower corporate income tax rates and longer tax holidays are effective at attracting FDI, but not at boosting gross private fixed capital formation or growth. The study presents a contextual gap since it did not focus on oil and gas sector. Furthermore, the study was conducted in other countries and not Kenya.

The Babatunde and Adepeju (2012) empirical research on tax incentives showed that tax incentives had a substantial effect on FDI in the Nigerian oil and gas market. However, because it was conducted in Nigeria, which is a different setting from Kenya, the study poses a contextual void.

There is also little literature in Kenya, particularly in the oil and gas sectors, on tax incentives and foreign direct investment. The lack of adequate empirical literature in Kenya on tax incentives and FDI inflows in the oil and gas sectors and the inconsistency in previous studies' findings on the precise position of the effect of tax incentives on FDI raise the question of whether tax incentives have been effective in attracting FDIs in the oil and gas sector in Kenya.

Table 2.1: Summary of Literature Review and Research Gaps

Author/s &Year	Focus of the study	Research Gap	Focus on the current study
Bernstein and Anwar (2014)	Analyze the effects on input demands and production supply of tax policies for products operating in selected sectors in Mexico, Turkey and Pakistan.	Contextual gap: the study was conducted in other countries and not Kenya	Focus was on oil and gas sector in Kenya
Murage, Mwangi, Kaijage and Ochieng (2019)	Relationships between tax incentives and FDI in the Group Member States of East Africa	Methodological gap: the study used panel secondary data	The study used cross-sectional primary data
Feldstein (2012)	Relative efficacy of tax incentives for Pakistan and Mexico by using disaggregated dynamic computable general equilibrium models.	Contextual gap: The study was conducted in Pakistan and Mexico.	Focus was on oil and gas sector in Kenya
Lawson and Bentum-Micah (2019)	In developed countries, the success of selective government policies and investment agreements in attracting FDI flows	Contextual gap: Since it was conducted in Ghana	Focus was on FDI inflows to Kenya
Gitonga (2017)	The connection between tax incentives and Kenyan multinational corporations' inflow of foreign direct investment	Contextual gap: Since it not focus on oil and gas companies	Focus was on oil and gas sector in Kenya
Onyeiwu and Shrestha (2015	The Middle East and North Africa region's tax incentives and foreign direct investment	Contextual gap: Since it focused on MENA	Focus was on oil and gas sector in Kenya
Owolabi and Okwu (2014)	It reviewed the role of VAT and noted that developing countries are increasingly realizing the critical position of value added tax as an instrument of economic growth.	Conceptual gap: Since it focused on overall economic growth of developing countries	Focus was on FDI inflows to Kenya

Author/s &Year	Focus of the study	Research Gap	Focus on the current study
Gumo (2013)	The effect of tax incentives on Kenya's foreign direct investment.	A contextual gap: since it did not focus on oil and gas industry,	Focus was on oil and gas sector in Kenya
Munongo and Ribinson (2018)	Whether the tax incentives in the Southern African Development Community (SADC) draw foreign direct investment.	Contextual gap: The study was conducted in southern African Development Community	The study was done in Kenya.
Olaleye, Riro and Memba (2016)	Impact on foreign direct investment in listed Nigerian manufacturing companies of business income tax incentives	Contextual gap: Focused on manufacturing companies in Nigeria	Focus was on oil and gas sector in Kenya
Lodhi (2017)	Incentivized tax policy and its impact on Pakistani investments	Contextual gap: The study was conducted in Pakistan	The study was done in Kenya
Bora (2013)	Tax incentive effectiveness in attracting foreign direct investment to Ethiopia.	Contextual gap: The study was conducted in Ethiopia	The study was done in Kenya.
Ślusarczyk (2018),	Taxation incentives are a crucial factor in attracting foreign direct investment to Poland.	Conceptual gap: The study did not specifically focus on import duty incentives.	Focused on import duty incentives
Ngure (2018)	Tax incentives and their effect on the output of the manufacturing companies selected in Kenya.	Methodological gap: The study used secondary data.	The study utilized primary data
Olaniyi, Oyedokun and Ajayi (2019)	Impact on foreign direct investment inflows through tax policy incentives in Nigeria.	Contextual gap: The study was conducted in Nigeria	The study was done in Kenya.
Ugwu (2018)	Contribution of tax benefits to the influx of FDI to Nigeria, Ghana and South Africa	Contextual gap: Focused on other countries in Africa	The study was done in Kenya.
Kuria (2017)	The impact on the results of EPZ companies in Kenya of the corporate income tax incentive and VAT incentive.	Conceptual gap: since it focused on performance of EPZ firms and not FDI inflows to Kenya	Focus was on FDI inflows to Kenya

2.6 Conceptual Framework

A conceptual framework is a graphical illustration of the research concepts and how they relate with each other, which have been or have to be studied in the research graphically or in some other narrative form (Tamene, 2016). The independent variables (tax incentives) include capital deductions, income tax incentives, VAT incentives and import duty incentives. The dependent variable (FDI) is measured using corporate social responsibility, technology diffusion and managerial skills.

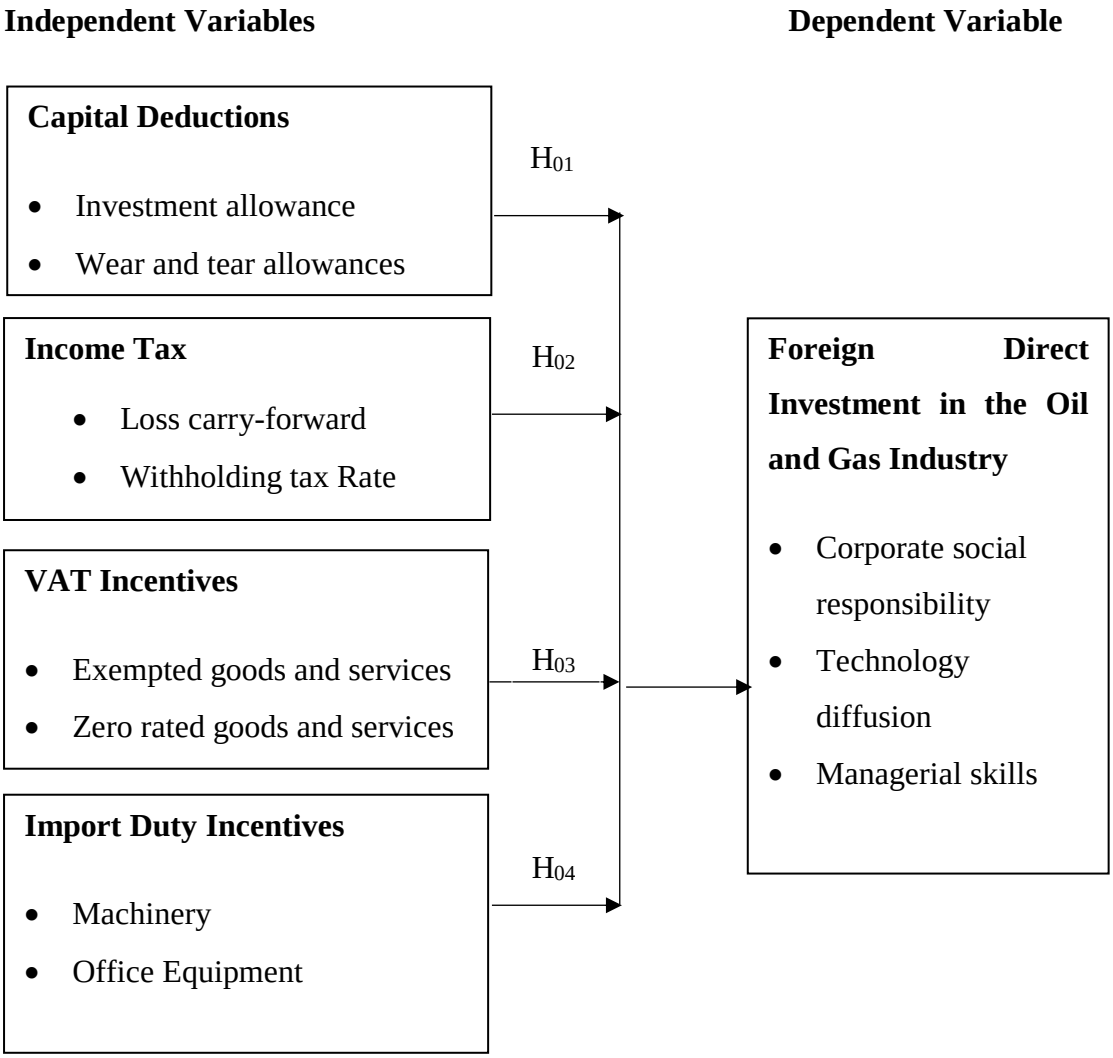

Figure 2.1: Conceptual Framework

Source: Author (2019)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The study sought to analyse the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya. It provides a blueprint for knowledge collection, calculation and study. Therefore the researcher discusses in this section the methods and techniques used in data collection, processing and analysis.

3.2 Research Design

This research adopted an explanatory research technique. This design helps in understanding the cause and effect relationship between research concepts (Rahi, 2017). In this report, the researchers sought to evaluate the influence of tax incentives on foreign direct investment in Kenya's oil and gas field. Using an explanatory study design, the investigator was thus able to assess the causal effect between tax incentives and foreign direct investment.

3.3 Target Population

This is a well-defined or identified category of persons, groups of things, families, businesses, facilities, elements or events that are being studied. Thus, a certain specification that the researcher is researching should suit the population and the population should be homogeneous (Cox, 2009). This research targeted five oil and gas companies in Kenya including Tullow, Zarara, ENI, Total and Africa oil. The five companies were purposively selected. The choice of the five companies was because they are the only ones that are still active to-date. Further, senior managers formed suitable respondents since they possessed adequate knowledge and information in

regard to the subject matter. Table 3.1 indicates the total target respondents as 136 managers.

Table 3.1: Target Population

Companies	Managers
Tullow	30
Zarara	26
ENI	34
Total	30
Africa Oil	16
Total	**136**

3.4 Sample Size

Kothari (2014) observed that when a study population is relatively small, a census should be conducted. In this study, the target respondent of 136 senior managers was considered small and therefore a census was conducted.

3.5 Research Instrument

To each member of the target group, the researcher administered a survey instrument (questionnaire). Using a standardized questionnaire, primary information was obtained directly from respondents. Based on the goals of the report, the research instrument was organized. The questionnaire consisted of questions concerning the variables in the analysis. The investigator was thus able to investigate the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya.

3.6 Data Collection Procedure

The research instruments were individually administered by the study to the target respondents from five oil and gas companies: Tullow, Zarara, ENI, Total and Africa.

To ensure that all questionnaires were given to the respondents, the researcher exercised care and control, and to do this, the researcher maintained a registry of questionnaires that were administered and received.

3.7 Pilot Testing

The purpose of the pilot study was to test the reliability of the questionnaires. According to Cooper and Schindler (2010), a pilot test is critical for testing the reliability of data collection instruments. Cox (2009) describes the reliability of research as determining whether the analysis would actually calculate what it was intended to measure or how truthful the research outcomes would be. To detect design and instrumentation vulnerabilities and to provide proxy data for sample collection, a pilot study was conducted. In this survey, the questionnaire was administered randomly to 10 percent of the target population. The respondents who participated in the pilot were excluded from the main data collection. Riff, Lacy and Fico (2014) postulated that for pilot research, 10% of the target population is sufficient.

3.7.1 Reliability of Research Instrument

Fisher (2009) defines reliability as the degree to which findings are consistent over time and an accurate representation of the total population under analysis is referred to as reliability and if the results of a study can be repeated under a similar methodology, the research instrument is considered to be reliable. Kirk and Miller (2009) established three types of reliability in quantitative research that relate to the degree to which a measurement, repeatedly given, maintains the stability of a measurement over time and the similarity of measurements over a given time period. Charles (2009) adheres to the theory that through the test-retest process, the accuracy by which questionnaire test items are answered or the ratings of individuals remain relatively the same can be

determined at two distinct times. The most common measure of internal consistency, known as the Alpha of Cronbach (alpha), was used in this study. It illustrates the degree to which it is possible to consider a number of test items as a single latent variable calculation (Cronbach, 1951). The suggested value of 0.7 was used as a cut-off of reliability for this study. The value of Cronbach alpha must be at least 0.7 or higher for the research instrument to be reliable.

3.7.2 Validity of Research Instrument

Riff, Lacy and Fico (2014) noted that the accuracy and significance of inferences are accurate, depending on the research findings. Fisher (2009) notes that validity determines whether the study really measures what it was intended to assess or how specific the research results are. The research was piloted by 10 percent of the target population. The actual research did not involve these respondents. The pilot study authorized the research instrument to be pre-tested. In order to enhance the validity and reliability of the instrument, the clarity of the research instruments was developed for the respondents. The pilot outcome allowed the investigator to fix contradictions that were seen to emerge from the tools, which meant that what was expected was calculated.

3.8 Data Analysis and Presentation

The quantitative data obtained using questionnaires was analyzed using descriptive statistics and presented by means of percentages, means and frequencies. The SPSS software aided the analysis. In addition, to evaluate the relationship between tax incentives and foreign direct investment, the study used inferential statistics (Pearson's correlation and regression analysis). Frequency tables and maps were used to display the results. The analytical model which directed the research was:

$Y=\beta_0+\beta_1X_1+ \beta_2X_2+ \beta_3X_3+ \beta_4X_4 + \varepsilon$

Whereby Y = Foreign Direct Investment

X_1 = Capital Deductions

X_2 = Income Tax

X_3 = VAT Incentives

X_4 = Import duty Incentives;

β_0 β_1 β_2 β_3 and β_4 are the regression coefficients

3.9 Regression Assumptions

Prior to running the regression analysis, several assumptions were conducted on the variables data. This was done to ensure that the analysis results were accurate and free from bias (Field, 2009). The tests included: normality, linearity, homoscedasticity, multicollinearity and autocorrelation tests.

3.9.1 Normality Test

The Shapiro-Wilk test was used to test normality. Where the observations are less than 2000, the test is favoured. The Ho is the regular distribution of the results. A probability value greater than 0,05 will lead to acceptance of the null hypothesis and vice versa.

3.9.2 Linearity Test

Using the ANOVA data, linearity was checked. The Ho is no linear relationship between the independent and dependent variables. A likelihood value lower than 0.05 would lead to the null hypothesis being dismissed in favor of the alternative.

3.9.3 Heteroscedasticity Test

Heteroskedasticity occurs when for free variables, the ward variable exhibits inconsistent fluctuation across the range. The Breusch-Pagan / Godfrey test (1979) was used to test for heteroscedasticity. The null hypothesis is that the error term variance is constant. The null hypothesis is denied if it is $P< 0.05$. If $P>0.05$, on the other hand, the null hypothesis is accepted, which means a constant variance of the error term.

3.9.4 Multicollinearity Test

Where there is a close relation between at least two autonomous variables, multicollinearity exists. The prescient strength of individual variables reduces the closeness of multicollinearity. The Variance Inflation Factor (VIF) has been used to verify multi-collinearity. A VIF of less than 3 shows no multicollinearity for all the independent variables, whereas a VIF of more than 10 shows a multi-collinearity problem (Field, 2009).

3.9.5 Test of Autocorrelation

The autocorrelation test was conducted using the Durbin-Watson autocorrelation test to determine whether the residual is serially correlated or not. The Durbin Watson test indicates a test statistic with a value of 0 to 4, where: 2 denotes no autocorrelation; 0 to 2<2 denotes a positive autocorrelation; while >2 denotes a negative autocorrelation. The rule of the decision is that statistical test values are relatively normal in the 1.5 to 2.5 range. Values may be cause for concern beyond this set (Field, 2009).

3.10 Operationalization and Measurement of Variables

Table 3.2: Operationalization & Measurement of Variables

Variable	Type of variable	Indicators	Source/ Author	Type of Questions	Tool of Analysis
Foreign Direct Investment	Dependent	-Technology diffusion -Corpoate social Responisbility -New managerial skills	Onyeiwu and Shrestha (2015)	Questionnaire -Likert scale	Descriptive, regression Analysis.
Capital Incentives	Independent	-Investment allowance -Wear and tear	Gitonga (2017)	Questionnaire -Likert scale	Descriptive, regression Analysis.
Income Tax	Independent	-Withholding tax rate -Allowable deductions -Loss carry forward	Olaleye, Riro and Memba (2016)	Questionnaire -Likert scale	Descriptive, regression Analysis.
VAT Incentives	Independent	- Exempted goods and services - Zero rated goods and services	Kuria (2017)	Questionnaire -Likert scale	Descriptive, regression Analysis.
Import duty Incentives	Independent	-Machinery -Raw materials -Office Equipment	Ślusarczyk (2018),	Questionnaire -Likert scale	Descriptive, regression Analysis.

CHAPTER FOUR

DATA ANALYSIS, INTERPRETATION AND PRESENTATION

4.1 Introduction

The data analysis, presentation, and interpretation of the research findings are discussed in this chapter. The study analyzed the effects of tax incentives on foreign direct investment in Kenya's oil and gas field.

4.2 Response Rate

This section provides the response rate results.

Table 4.1: Response Rate

Response	Frequency	Percentage
Returned	108	79.4%
Unreturned	28	20.6%
Total	**136**	**100%**

Source: Research Data (2020)

The findings in Table 4.1 indicate that out of the 136 questionnaires administered to the respondents, 108 were properly filled and returned. This represented 79.4% response rate. The remaining 28 questionnaires were either unreturned or not valid. A return rate above 50 percent is sufficient for study (Mugenda & Mugenda, 2003). This meant that the response rate was satisfactory in this sample.

4.3 Reliability Analysis

This section presents reliability results for each variable. The findings are shown in Table 4.2.

Table 4.2: Reliability Results

Variables	Number of items	Cronbach's Alpha	Comment
Foreign Direct Investment	5	0.761	Reliable
Capital Deductions	4	0.769	Reliable
Income Tax	5	0.764	Reliable
VAT Incentives	4	0.753	Reliable
Import Duty Incentives	4	0.733	Reliable
Overall		**0.756**	

Source: Research Data (2020)

The results in Table 4.2 indicate that FDI had an alpha coefficient of 0.761; capital deductions, 0.769; income tax, 0.764; VAT incentives, 0.753; and import duty incentives, 0.733. The overall alpha coefficient was 0.756>0.7. This implied that all the items measuring the study variables were dependable.

4.4 Test of Regression Assumptions

This section presents results on the evaluation of the assumptions of regression. The assumptions were: linearity, normality, heteroscedasticity, multicollinearity, and autocorrelation. The aim of testing these assumptions was to guarantee that the findings were correct and bias-free.

4.4.1 Linearity Test

Linearity test was checked using the ANOVA and results shown in Table 4.3.

Table 4.3: Linearity Test; ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	25.274	4	6.319	101.265	.000b
	Residual	6.427	103	0.062		
	Total	31.701	107			

a Dependent Variable: FDI

b Predictors: (Constant), Import, Income tax, capital deductions, VAT

Source: Research Data (2020)

The ANOVA results presented in Table 4.3 reveal that the model was statistically significant. This was supported by a significant P value of 0.000<0.05. This implied that a linear connection exists between tax incentives and FDI.

4.4.2 Normality Test

The normal distribution of the variable data was tested using Shapiro-Wilk test.

Table 4.4: Shapiro-Wilk Test of Normality

Variables	Statistic	df	Sig.
FDI	.958	108	0.493
Capital deductions	.950	108	0.102
Income tax	.945	108	0.124
VAT incentives	.910	108	0.116
Import duty incentives	.921	108	0.253

a Lilliefors Significance Correction

Source: Research Data (2020)

Based on the results in Table 4.4, value for FDI, capital deductions, income tax, VAT incentives and import duty incentives, had P value >0.05. This denotes that the study data was normally distributed.

4.4.3 Multicollinearity Test

Table 4.5: Multicollinearity Test Using VIF

	Tolerance	VIF
Capital deductions	0.401	2.492
Income Tax	0.439	2.276
VAT incentives	0.214	4.664
Import duty incentives	0.206	4.849

a Dependent Variable :FDI

Source: Research Data (2020)

The results in Table 4.5 indicate that the variables capital deductions, income tax, VAT incentives and import duty incentives had VIF values less than 10. According to Hair, Black and Babin (2010), VIF value of less than 10 denotes no multi-collinearity. Therefore, the study established that the independent variables were not highly correlated.

4.4.4 Heteroscedasticity Test

Table 4.6: Breusch-Pagan / Cook-Weisberg test for heteroskedasticity

Ho: Constant variance
Variables: fitted values of FDI
chi2(1) = 4.95
Prob > chi2 = 0.0644

Source: Research Data (2020)

Results in Table 4.6 indicate a probability value of 0.0644>0.05. The Ho was therefore not rejected. Therefore, the error term was homoscedastic implying that there was no problem of heteroskedasticity.

4.4.5 Autocorrelation Test

Table 4.7: Durbin-Watson test of Autocorrelation

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.893 a	0.797	0.789	0.24979	1.723

a Predictors: (Constant), Income tax, capital deductions, VAT
b Dependent Variable:
FDI

The findings in Table 4.7 display a Durbin-Watson value of 1.723, varying from 1.5 to 2.5, suggesting that the null hypothesis of no autocorrelation was accepted and that the residuals were not autocorrelated.

4.5 Descriptive Analysis

This section presents descriptive results relating to the study variables. The specific descriptive statistics included: percentages, mean and standard deviation.

4.5.1 Descriptive Statistics on Capital Deductions

The study sought to evaluate the effects of capital deductions on foreign direct investment in Kenya's oil and gas field. The following scale was used: strongly disagree (1) disagree (2) neutral (3) agree (4) and strongly agree (5).

Table 4.8: Descriptive Statistics on Capital Deductions

Statements	SD	D	N	A	SA	M	Std. dev
Capital allowances are a tool used to stimulate investment in Kenya's oil and gas market.	3.7%	13.9%	5.6%	36.1%	40.7%	4.0	1.2
The oil and gas companies receive capital deductions inform of wear and tear allowances	5.6%	18.5%	2.8%	36.1%	37.0%	3.8	1.3
The oil and gas companies receive capital deductions inform of investment allowances	2.8%	16.7%	0.9%	46.3%	33.3%	3.9	1.1
The oil and gas companies receive capital deductions inform of industrial deductions	8.3%	19.4%	4.6%	28.7%	38.9%	3.7	1.4
Aggregate mean						**3.8**	**1.2**

Source: Research Data (2020)

The results in Table 4.8 show that the most of the participants with an overall mean score of 3.8 and a standard deviation of 1.2 agreed with the capital deduction claims. Participants accepted that capital allowances are a tool used to promote investment in Kenya's oil and gas sector (mean=4.0), the oil and gas companies receive capital deductions inform of wear and tear allowances (mean=3.8), the oil and gas companies receive capital deductions inform of investment allowances (mean=3.9), and the oil and gas companies receive capital deductions inform of industrial deductions (mean=3.7). This implied that the oil and gas firms receive incentives in form of capital deductions. This is expected to enhance FDI through the oil and gas sector. The findings are consistent with those of Lawson and Bentum-Micah (2019) who found that policies on capital deductions are essential in promoting foreign investment.

4.5.2 Descriptive Statistics on Income Tax Incentives

The study sought to examine the effect of the income tax on foreign direct investment in Kenya's oil and gas field. Using the 5-point scale: strongly disagree with (1) disagree with (2) neutral (3) agree with (4) and strongly agree with (5), the respondents expressed their degree of agreement with the income tax claims.

Table 4.9: Descriptive Statistics on Income Tax Incentives

Statements	SD	D	N	A	SA	M	Std. dev
Introduction of income tax plays a major part in Kenya's tax policy.	3.7%	13.9%	6.5%	36.1%	39.8%	3.9	1.2
The oil and gas sector receives income tax incentive in form of loss carry-forward.	2.8%	11.1%	4.6%	36.1%	45.4%	4.1	1.1
The withholding tax benefits are offered by the oil and gas industry.	4.6%	8.3%	2.8%	41.7%	42.6%	4.1	1.1
Tax credit incentives are being offered to the oil and gas industry.	5.6%	10.2%	4.6%	41.7%	38.0%	4.0	1.2
The permissible deductions are obtained by the oil and gas industry.	7.4%	9.3%	0.9%	42.6%	39.8%	4.0	1.2
Aggregate mean						**4.0**	**1.1**

Source: Research Data (2020)

The results in Table 4.9 show that most respondents agreed to claims on income tax benefits with an aggregate mean score of 4.0 and a standard deviation of 1.1. Participants accepted that the implementation of income tax plays a major role in Kenya's tax policy (mean=3.9), the oil and gas sector receives income tax benefits in the form of carry-forward losses (mean=4.1), the oil and gas sector receives withholding tax incentives (mean=4.1), the oil and gas sector receives tax credit incentives (mean=4.0), and the oil and gas sector receives tax incentives (mean=4.1), This meant that benefits in the form of income tax were earned by oil and gas firms and this could encourage FDI inflows in the oil and gas sector. Olaleye, Riro and Memba

(2016) supported the results, which established that there are clear positive linear relationships between income tax incentives and foreign direct investment.

4.5.3 Descriptive Statistics on VAT Incentives

The research investigated the effect of incentives for VAT on foreign direct investment in Kenya's oil and gas market. Using the 5-point scale: strongly disagree with (1) disagree with (2) neutral (3) agree with (4) and strongly agree with (5), the respondents expressed their degree of agreement with the VAT incentive claims.

Table 4.10: Descriptive Statistics on VAT Incentives

Statements	SD	D	N	A	SA	M	Std. dev
International investors are encouraged to invest on products exempted from VAT.	6.5%	13.9%	5.6%	38.9%	35.2%	3.8	1.2
Investment in services exempted from VAT is encouraged by international investors.	4.6%	7.4%	4.6%	38.9%	44.4%	4.1	1.1
The oil and gas sector comply with the rules guiding VAT.	5.6%	13.0%	5.6%	35.2%	40.7%	3.9	1.2
The oil and gas industry favors the manufacture or selling of zero-rated products and services.	6.5%	9.3%	3.7%	37.0%	43.5%	4.0	1.2
Aggregate mean						**4.0**	**1.2**

Source: Research Data (2020)

The result in Table 4.10 indicates that most respondents agreed to statements on VAT benefits with an aggregate mean score of 4.0 and a standard deviation of 1.2. The respondents accepted that foreign investors should be encouraged to invest in VAT-exempt products (mean=3.8), that foreign investors should be encouraged to invest in VAT-exempt services (mean=4.1), that the oil and gas sector should comply with the VAT rules (mean=3.9) and that the oil and gas sector would prefer to manufacture or sell zero rated goods and services (mean=4.0). This implied that the oil and gas

companies receive VAT incentives and this is likely to increase FDI inflows through the sector. The results were consistent with those of Owolabi and Okwu (2014), who observed that developing countries are increasingly recognizing the crucial role of value added tax as an instrument of economic growth.

4.5.4 Descriptive Statistics on Import Duty Incentives

The study sought to assess the effects on FDI in the oil and gas sector in Kenya of import duty incentives. Using the 5-point scale: strongly disagree with (1) disagree with (2) neutral (3) agree with (4) and strongly agree with (5), the respondents expressed their degree of agreement with the import duty incentive claims. In Table 4.11, the results are shown.

Table 4.11: Descriptive Statistics on Import Duty Incentives

Statements	SD	D	N	A	SA	M	Std. dev
Oil and gas companies receive import duty incentives on machinery	5.6%	13.0%	4.6%	49.1%	27.8%	3.8	1.1
Oil and gas companies receive import duty incentives on raw materials	2.8%	9.3%	4.6%	34.3%	49.1%	4.2	1.1
Oil and gas companies receive import duty incentives on office equipment	4.6%	16.7%	1.9%	41.7%	35.2%	3.9	1.2
Oil and gas companies receive import duty incentives in form of customs duty	0.9%	14.8%	2.8%	33.3%	48.1%	4.1	1.1
Aggregate mean						**4.0**	**1.1**

Source: Research Data (2020)

The findings in Table 4.11 show that the majority of respondents, with an aggregate mean score of 4.0 and a standard deviation of 1.1, agreed to claims on import duty benefits. The participants agreed with the argument that import duty discounts on machinery are earned by oil and gas firms (mean=3.8), oil and gas companies receive

import duty incentives on raw materials (mean=4.2), oil and gas companies receive import duty incentives on office equipment (mean=3.9), and oil and gas companies receive import duty incentives in form of customs duty (mean=4.1). This meant that oil and gas firms were granted rewards in the form of import duties. In the oil and gas sector, this is expected to boost FDI. The results agree with Olaniyi, Oyedokun and Ajayi (2019)'s disclosure that custom and excise duties and value-added tax benefits have had a significant effect on foreign direct investment.

4.5.5 Descriptive Statistics on FDI

In this analysis, the dependent variable was FDI in the oil and gas sector. The respondents were asked to score their agreement against each argument made to them or otherwise. The outcomes are listed in Table 4.12.

Table 4.12: Descriptive Statistics on FDI

Statements	SD	D	N	A	SA	M	Std. dev
The presence of oil and gas firms in Kenya has increased the acceptance of new technologies in the region.	3.7%	15.7%	4.6%	37.0%	38.9%	3.9	1.2
Kenya's oil and gas companies are actively involved in initiatives of corporate social responsibility.	0.0%	7.4%	0.9%	50.0%	41.7%	4.3	0.8
New management skills in the sector have been brought by the presence of oil and gas firms in Kenya.	9.3%	7.4%	5.6%	30.6%	47.2%	4.0	1.3
There is a good prospect of attracting foreign direct investment in the oil and gas sector in Kenya.	13.0%	13.0%	1.9%	29.6%	42.6%	3.8	1.4
External investment in Kenya's oil and gas field increases the influx of foreign assets.	7.4%	14.8%	3.7%	40.7%	33.3%	3.8	1.3
Aggregate mean						**3.9**	**1.2**

Source: Research Data (2020)

The results in Table 4.12 show that the majority of respondents agreed with statements on FDI with an overall mean score of 3.9 and a standard deviation of 1.2. Participants accepted that the involvement of oil and gas companies in Kenya has increased the adoption of new technologies in the sector (mean=3.9), oil and gas companies operating in Kenya are actively engaged in corporate social responsibility activities (mean=4.3), the presence of oil and gas companies in Kenya has introduced new management skills in the sector (mean=4.0), foreign direct investment in the oil and gas sector in Kenya is highly likely (mean=3.8) and foreign involvement in the oil and gas sector in Kenya increases the flow of foreign assets (mean=3.8). This implied that new technology adoption, corporate social responsibility activities, new managerial skills and foreign assets are key indicators of FDI inflows in the oil and gas sector. The increase in FDI attraction in the sector can be attributed to tax incentives.

4.6 Correlation Analysis

This section presents findings on the correlation between technology acceptance aspects and tax compliance.

Table 4.13: Correlation Matrix

		FDI	Capital Deductions	Income tax	VAT incentive	Import Duty
FDI	Pearson Correlation	1				
	Sig. (2-tailed)					
Capital Deductions	Pearson Correlation	.794**	1			
	Sig. (2-tailed)	.000				
Income tax	Pearson Correlation	.744**	.745**	1		
	Sig. (2-tailed)	.000	.000			
VAT incentive	Pearson Correlation	.656**	.488**	.406**	1	
	Sig. (2-tailed)	.000	.000	.000		
Import Duty	Pearson Correlation	.717**	.512**	.444**	.785**	1
	Sig. (2-tailed)	.000	.000	.000	.000	
	N	108	108	108	108	108

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

Source: Research Data (2020)

The findings in Table 4.13 indicate that capital deductions (r =.794**, P = .000), had a strong positive and significant correlation with FDI. This means that the rise in capital deductions in the oil and gas sector is substantially associated with FDI. The results also reveal that income tax incentive (r =.744**, P = .000), had a strong positive and significant correlation with FDI. This means that there is a strong link between the rise in income tax incentives and FDI in the oil and gas industry.

The results further shows that VAT incentive (r =.656**, P = .000), had a strong positive and significant correlation with FDI. This means that there is a strong link between the rise in VAT rewards and FDI in the oil and gas industry. Finally, the findings reveal that that import duty incentive (r =.717**, P = .000), had a strong positive and significant correlation with FDI. This means that there is a strong link between the rise in import duty benefits and FDI in the oil and gas market.

4.7 Multiple Regression Analysis

The main goal of the study was to investigate the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya. Having separately established the existence of a significant relationship of each of the four predictors (capital deductions, income tax, VAT incentives and import duty incentives) with FDI, It was important to decide how the FDI was jointly affected by a combination of the four variables. Therefore to test the relationship between variables, a multiple linear regression analysis was carried out. Tables 4.14, 4.15 and 4.16 include, respectively, the model description, ANOVA and coefficient results.

Table 4.14: Model Summary; Tax Incentives and FDI

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.893a	0.797	0.789	0.24979

a Predictors: (Constant), Import, Income tax, capital deductions, VAT

Source: Research Data (2020)

The results in Table 4.14 show that 79 percent (adjusted R2= .789) of the total variations in the FDI were jointly explained by all four predictor variables in this analysis. The modified R-squared was chosen because (P=0.571>0.05) the constant value in Table 4.16 is negligible. The findings implied that the tax incentives (capital deductions, income tax, VAT incentives and import duty incentives) contribute greatly towards FDI inflows in the oil and gas sector.

Table 4.15: ANOVA; Tax Incentives and FDI

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	25.274	4	6.319	101.265	.000b
	Residual	6.427	103	0.062		
	Total	31.701	107			

a Dependent Variable: FDI

b Predictors: (Constant), Import, Income tax, capital deductions, VAT

Source: Research Data (2020)

In Table 4.15, the ANOVA regression model shows a F statistic of 101.265 and a recorded P value of 0.000. Therefore, the proposed model is statistically relevant (good fit) in predicting the dependent variable, as the P value is less than the alpha value (P < .05).

Table 4.16: Coefficients; Tax Incentives and FDI

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	**Std. Error**	**Beta**	**t**	**Sig.**
1	(Constant)	0.115	0.202		0.568	.571
	Capital deductions	0.339	0.063	0.377	5.389	.000
	Income Tax	0.296	0.069	0.286	4.279	.000
	VAT incentives	0.178	0.079	0.124	2.252	.020
	Import duty Incentives	0.314	0.082	0.375	3.837	.000

a Dependent Variable: FDI

Source: Research Data (2020)

There are equivalent (Likert) scales for all predictor variables, but constant value is negligible in the model, hence the use of standardized beta coefficients. The hypothesized model $Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + e$ is estimated as follows:

$$Y = 0.377X_1 + 0.286X_2 + 0.124X_3 + 0.375X_4$$

Where:

Y = Foreign Direct Investment

X_1 = Capital Deductions

X_2 = Income Tax

X_3 = VAT Incentives

X_4 = Import duty Incentives

The multiple regression results in Table 4.16 reveal that capital deductions (β1= 0.377, P = .000) is meaningful and positively related to FDI. This implied that a one unit increase in capital deductions would increase FDI inflows by 0.377 units.

The results also indicate that income tax (β2= 0.286, P = .000) is meaningful and positively connected to FDI. This implied that a one unit increase in income tax incentives would increase FDI inflows by 0.286 units.

The findings further reveal that VAT incentives (β3= 0.124, P = .020) is meaningful and positively connected to FDI. This implied that a one unit increase in VAT incentives would increase FDI inflows by 0.124 units.

In addition, the results indicate that import duty incentives (β4= 0.375, P = .000) is meaningful and positively connected to FDI. This implied that a one unit increase in import duty incentives would increase FDI inflows by 0.375 units.

Furthermore, from the model, the most significant predictor of FDI is capital deductions (β= 0.377), followed by import duty incentives (β= 0.375), followed by income tax (β= 0.286), and lastly VAT incentives (β= 0.124).

4.7.1 Hypothesis Testing

The null hypothesis (H01) that there is no major impact of capital deductions on foreign direct investment in the oil and gas sector in Kenya was denied based on the regression results in Table 4.16. This meant that capital deductions had a substantial impact on FDI in Kenya's oil and gas segment.

The null hypothesis (H02) that the income tax may not have a major impact on foreign direct investment in Kenya's oil and gas sector has been denied. This meant that the income tax had a huge impact on FDI in Kenya's oil and gas segment.

Further the null hypothesis (H03) that there is no major impact of VAT incentive on foreign direct investment in the oil and gas sector in Kenya was rejected. This meant that VAT incentives had a huge impact on FDI in Kenya's oil and gas market.

Moreover the null hypothesis (H04) that import duty incentives have no major impact on foreign direct investment in the oil and gas sector in Kenya has been dismissed. This meant that import duty incentives had a huge impact on FDI in Kenya's oil and gas market.

Table 4.17: Summary of Hypotheses Test

No	Hypotheses	P value	Decision
H01	There is no major impact of capital deductions on FDI in the oil and gas sector in Kenya	0.000<0.05	Rejected
H02	Income tax may not have a major impact on FDI in Kenya's oil and gas sector	0.000<0.05	Rejected
H03	There is no major impact of VAT incentive on FDI in the oil and gas sector in Kenya	0.020<0.05	Rejected
H04	Import duty incentives have no major impact on FDI in the oil and gas sector in Kenya	0.000<0.05	Rejected

Source: Research data (2020)

4.8 Discussion of the key Findings

The reliability results indicated that the items measuring capital deductions, income tax, VAT incentives, import duty and FDI were reliable. This was confirmed by Cronbach alpha coefficients greater than 0.7. From the descriptive statistic findings, most of the

participants agreed with statements relating to the study variables. This was confirmed by aggregate means of 3.8, 4.0, 4.0, 4.0 and 3.9 for capital deductions, income tax, VAT incentives, import duty and FDI respectively.

Furthermore the results of the correlation suggested that the relationship between capital deductions, income tax, incentives for VAT, import duty and FDI was positive and important. This was confirmed by correlation value of 0.794, 0.744, 0.656 and 0.717. The P values <0.05 also indicated a strong relationship between tax incentive components and FDI.

The regression findings indicated that capital deductions had a positive and significant effect on FDI ($\beta 1$= 0.377, P = .000). This implied that capital deductions contribute significantly towards attracting foreign investment. The results are in line with those of Lawson and Bentum-Micah (2019), who found that capital deduction policies play an important role in attracting FDI. However, the findings disagreed with Gitonga (2017) conclusion that investment deductions and industrial building allowances had no any significant relationship on FDI inflows.

The results also revealed that income tax incentives had a positive and significant effect on FDI ($\beta 2$= 0.286, P = .000). This implied that income tax incentives contribute significantly towards FDI. Olaleye, Riro and Memba (2016) supported the results, which established that there are clear positive linear relationships between income tax incentives and foreign direct investment. However the findings were in contrast to the claim by Murage et al. (2019) that losses carried forward did not have a statistically meaningful effect on FDI inflow.

The findings further indicated that VAT incentives had a positive and significant effect on FDI (β3= 0.124, P = .020). This implied that VAT incentives contribute significantly towards FDI. The findings were consistent with those of Owolabi and Okwu (2014), who observed that developed countries are increasingly realizing the crucial role of value added tax as an instrument of economic development. Similarly, Olaniyi, Oyedokun and Ajayi (2019) found that there were major effects on foreign direct investment from value-added tax incentives. In addition, Kuria (2017) found that there was a positive and important relationship between VAT rewards and the success of EPZ companies.

Lastly, the findings indicated that import duty incentives had a direct and meaningful effect on FDI (β4= 0.124, P = .000). This implied that import duty incentives contribute significantly towards FDI. Olaniyi, Oyedokun and Ajayi (2019) agreed with the disclosure that custom and excise duties and value-added tax benefits had a significant effect on foreign direct investment. The findings, however, contradict Bora (2013) assertion that in attracting FDI, custom duty exemption was negligible.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

The review of results, conclusions, recommendations and suggestions for further study is provided in this chapter. This is achieved in accordance with the study objectives.

5.2 Summary

5.2.1 Capital Deductions

The study's first objective was to assess the effects of capital deductions on foreign direct investments in Kenya's oil and gas market. The majority of respondents noted that the oil and gas sector earns capital deductions from the descriptive statistical results, reminding them of wear and tear allowances, expenditure allowances and industrial deductions.

The findings of the correlation analysis showed that a substantially positive relationship exists between capital deductions and FDI. A correlation value of .794 and a P value of 0.000 were used to endorse this. The results of the regression showed that capital deductions had a significant and meaningful impact on FDI. This led to the rejection of the null hypothesis in favor of the alternative that the deduction of capital had a substantial impact on FDI in Kenya's oil and gas market. The results align with those of Lawson and Bentum-Micah (2019), who discovered that capital deduction policies play an important role in attracting FDI. In addition, the results were consistent with the findings of Bernstein and Anwar (2014) that tax incentives such as investment allowances were more successful than others in stimulating investment per dollar of treasury income loss. Nonetheless, the findings contradicted with Gitonga (2017)

assertion that investment deductions and industrial building allowances had no any significant relationship on FDI inflows.

5.2.2 Income Tax

The second objective of the analysis was to assess the effects of the income tax on foreign direct investment in Kenya's oil and gas field. From the descriptive statistics results, majority of the respondents observed that the oil and gas sector receive income tax incentives inform of loss carry-forward, withholding tax incentives, tax credit incentives and allowable deductions.

The findings of the correlation analysis showed that a substantially positive relationship exists between income tax and FDI. This was accompanied by a .744 correlation value and a 0.000 P value. The results of the regression showed that income tax had a positive and meaningful impact on FDI. This led to the rejection of the null hypothesis in favor of the alternative that the income tax had a substantial impact on FDI in Kenya's oil and gas market. The results were corroborated by those of Olaleye, Riro and Memba (2016), who found that income tax incentives and foreign direct investment have good positive linear relationships. On the other hand, the findings disagreed with the postulation of Murage et al. (2019) that losses carried forward did not have a statistically important effect on the inflow of FDI. The results also contradicted the assertion by Munongo and Ribinson (2018) that losses carried forward are negligible FDI determinants.

5.2.3 VAT Incentives

The third goal of the study was to examine the impact of VAT incentives on foreign direct investment in the oil and gas sector in Kenya. Most of the respondents decided from the results of the descriptive statistics that foreign investors would be encouraged

to invest in goods and services excluded from VAT, that the oil and gas sector would comply with VAT regulations, and that the oil and gas sector would prefer to manufacture or sell zero rated goods and services.

The findings of the correlation analysis showed that the relationship between VAT rewards and FDI is substantially positive. A correlation value of .656 and a P value of 0.000 were used to endorse this. The results of the regression showed that rewards for VAT had a positive and meaningful impact on FDI. This led to the rejection of the null hypothesis in favor of the alternative that the incentives for VAT had a substantial impact on FDI in Kenya's oil and gas market. The findings were consistent with Owolabi and Okwu (2014)'s assertions that the crucial role of value added tax as an instrument of economic growth is increasingly recognized among developing countries. Similarly, Olaniyi, Oyedokun and Ajayi (2019) found that there were major effects on foreign direct investment from value-added tax incentives. In addition, Kuria (2017) found that there was a positive and important relationship between VAT rewards and the success of EPZ companies.

5.2.4 Import Duty Incentives

The study's fourth objective was to assess the impact of import duty incentives on foreign direct investment in Kenya's oil and gas market. Most of the respondents accepted, from the descriptive statistical findings, that oil and gas firms earn discounts for import duties on machinery, raw materials, office equipment and customs duties.

The correlation study's results showed that there is a significantly positive relationship between import duty incentives and FDI. This was accompanied by a .717 correlation value and a P value of 0.000. The results of the regression showed that there was a

positive and important effect of import duty incentives on FDI. This resulted in the rejection of the null hypothesis in favor of the alternative that import duty incentives had a significant effect on foreign direct investment in the oil and gas market of Kenya. The results were close to those of Olaniyi, Oyedokun and Ajayi (2019), who found that tax benefits for customs and excise duties had a big impact on foreign direct investment. Nonetheless, the findings contradicted Bora (2013) observation that custom duty exemption was insignificant in attracting FDI.

5.3 Conclusions

From objective one results, the study concluded that capital deductions have a statistically significant and direct connection with FDI. Furthermore, when combined with other variables, capital deductions had a significant predictive ability to determine inflows of FDI. The wear and tear allowances, investment allowances and industrial deductions were identified as key aspects of capital deductions that determine FDI in the oil and gas sector.

Based on the findings of objective two, the study concluded that income tax incentives have a statistically significant and direct connection with FDI. Furthermore, when combined with other variables, income tax incentives had a significant predictive ability to determine inflows of FDI. The loss carry-forward, withholding tax incentives, tax credit incentives and allowable deductions were found to be key aspects of income tax incentives that determine FDI in the oil and gas sector.

In line with the findings of objective three, the research concluded that VAT incentives have a statistically significant and direct connection with FDI. Furthermore, when combined with other variables, VAT incentives had a significant predictive ability to

determine FDI in the oil and gas sector in Kenya. The exemption of goods and services from VAT and zero rated goods and services were identified as critical aspects of VAT incentives that promote FDI in the oil and gas sector.

From the findings of objective four, the study concluded that import duty incentives have a statistically significant and direct connection with FDI. Moreover, when combined with other variables, import duty incentives had a significant predictive ability to determine inflows of FDI. The import duty incentives on machinery, raw materials, office equipment and customs duty were found to be essential in attracting foreign investment.

Generally, the government through the Ministry of Petroleum and Mining ,The National Treasury and The Kenya Revenue Authority should review the fiscal policy governing the Oil and Gas operations in Kenya , this is necessary so as to ensure that the fiscal regime is favourable to the country and to the investors.

5.4 Recommendations

In view of the foregoing conclusions, the study made several recommendations as presented below.

5.4.1 Recommendations to Theory

The study established a significant relationship between tax incentives and foreign direct investments. The study, therefore, makes significant contribution to theory in terms of predicting the effect of tax incentives and foreign direct investments.

5.4.2 Recommendations to Policy and Practice

The analysis established that capital deductions have a significant positive effect on foreign direct investment in the oil and gas sector. The study recommends the need for

the government to improve the capital deductions given to investors. In particular, the government should strengthen the following aspects: wear and tear allowances, investment allowances and industrial deductions

The study also found that income tax incentives have a significant positive effect on FDI in the oil and gas sector. The study recommends the need for the government to improve the income tax incentives given to investors in the oil and gas sector. In particular, the government should strengthen the following aspects: loss carry-forward, withholding tax incentives, tax credit incentives and allowable deductions.

The study further established that VAT incentives have a significant positive effect on FDI in the oil and gas sector. The study recommends the need for the government to streamline policy relating to VAT incentives. In particular, the government should strengthen the following aspects: exemption of goods and services from VAT and zero rated goods and services.

In addition, the study found that import duty incentives have a significant positive effect on FDI in the oil and gas sector. The study recommends the need for the government to improve import duty incentives given to investors. In particular, the government should strengthen the following aspects: import duty incentives on machinery, raw materials, office equipment and customs duty.

5.4.3 Suggestions for Further Studies

The study analyzed the effects of tax incentives on foreign direct investment in Kenya's oil and gas field. A similar analysis may be done for comparative purposes in other fields. This will clarify the nature of the analysis and allow the results to be generalized. The study focused on four components (capital deductions, income tax, VAT incentives

and import duty incentives), which accounted for 79 percent of variations in the dependent variable. Future studies could consider other aspects that can be attributed to the remaining 21 percent.

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APPENDICES

Appendix I: Introduction Letter

Dear (Respondent)

RE: VOLUNTARY PARTICIPATION IN DATA COLLECTION

I am a student pursuing a Masters' degree in tax and customs at Moi University and currently undertaking a research project on "**Effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya**"

You have been selected for this study to fill the questionnaire. Kindly respond to the questions in the attached questionnaire. The information provided will exclusively and solely be used for academic purposes and will be treated with utmost confidentiality. Upon request, you will be furnished with a copy of the final report.

Your cooperation will be highly appreciated.

Yours Faithfully,

MARTHA WANGUI KANYANJUA

Appendix II: Questionnaire

This research questionnaire seeks to establish the effect of tax incentives on foreign direct investment in the oil and gas sector in Kenya. The study is strictly for academic purpose.

(Tick and fill were appropriate)

SECTION A: CAPITAL DEDUCTIONS

1. Kindly indicate how you rate the following statements relating to capital deductions. Use a scale of 1-5 where; 1 = strongly disagree, 2= disagree, 3 = neutral, 4 = agree, 5 = strongly agree.

CAPITAL DEDUCTIONS	**1**	**2**	**3**	**4**	**5**
Capital allowance is a method used to encourage investment in the oil and gas sector in Kenya.					
The oil and gas companies receive capital deductions inform of wear and tear allowances					
The oil and gas companies receive capital deductions inform of investment allowances					
The oil and gas companies receive capital deductions inform of industrial deductions					

SECTION B: INCOME TAX

2. What is your level of agreement with the following statements that relate to income tax? Use a scale of 1-5 where; 1 = strongly disagree, 2= disagree, 3 = neutral, 4 = agree, 5 = strongly agree.

INCOME TAX	**1**	**2**	**3**	**4**	**5**
Introduction of income tax plays a major part in Kenya's tax policy.					
The oil and gas sector receives income tax incentive in form of loss carry-forward.					
The oil and gas sector receives the withholding tax incentives.					
The oil and gas sector receives the tax credit incentives.					
The oil and gas sector receives the allowable deductions.					

SECTION C: VAT INCENTIVES

3. To what extent do you agree with the following statements that relate to VAT incentives in your organization? Use a Use a scale of 1-5 where; 1 = strongly disagree, 2= disagree, 3 = neutral, 4 = agree, 5 = strongly agree.

VAT INCENTIVES	**1**	**2**	**3**	**4**	**5**
Foreign investors are encouraged to invest on goods exempted from VAT.					
Foreign investors are encouraged to invest on services exempted from VAT.					
The oil and gas sector comply with the rules guiding VAT.					

The oil and gas sector prefer to produce or sell zero rated goods and services.					

SECTION D: IMPORT DUTY INCENTIVES

4. To what extent do you agree with the following statements that relate to import duty incentives in your organization? Use a scale of 1-5 where; 1 = strongly disagree, 2= disagree, 3 = neutral, 4 = agree, 5 = strongly agree.

IMPORT DUTY INCENTIVES	**1**	**2**	**3**	**4**	**5**
Oil and gas companies receive import duty incentives on machinery					
Oil and gas companies receive import duty incentives on raw materials					
Oil and gas companies receive import duty incentives on office equipment					
Oil and gas companies receive import duty incentives in form of customs duty					

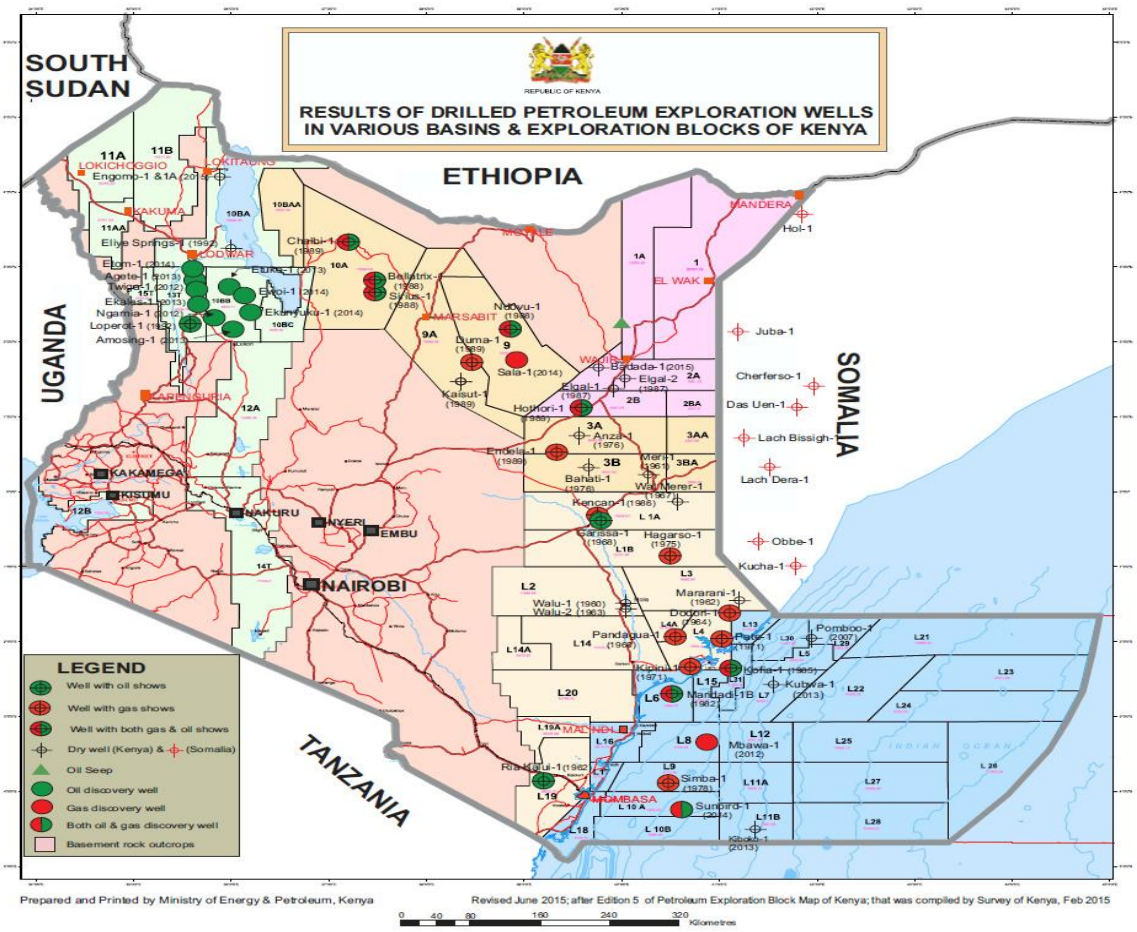
SECTION E: FOREIGN DIRECT INVESTMENT

5. Kindly indicate how you rate achievement of the following facets of foreign direct investment? Use a scale of 1-5 where; 1 = strongly disagree, 2= disagree, 3 = neutral, 4 = agree, 5 = strongly agree.

FOREIGN DIRECT INVESTMENT	1	2	3	4	5
The presence of oil and gas companies in Kenya has enhanced new technology adoption in the sector.					
Oil and gas companies operating in Kenya are actively involved in corporate social responsibility activities.					
The presence of oil and gas companies in Kenya has introduced new managerial skills in the sector					
There is high prospect in the attraction of foreign direct investment into the oil and gas sector in Kenya.					
Foreign participation in the oil and gas sector in Kenya increases the flow of foreign assets.					

THANKS FOR YOUR COOPERATION

Appendix III: Map of Oil Blocks and Selected list of Active Oil and Gas Companies in Kenya



Source: Ministry of Petroleum and Mining (2020)

No.	Companies	Block
1	Tullow Oil	Block 10BAA,10BB,12A,13T,12B
2	Zarara	Blocks L4, L13
3	ENI	Blocks L21, L23, L24
4	Total	Block L22
5	Africa Oil	Block 9

Appendix IV: Authorization Letter from KESRA

KENYA REVENUE AUTHORITY
ISO 9001:2015 CERTIFIED

REF: KESRA/NBI/036

30th October, 2020

TO WHOM IT MAY CONCERN

RE: REQUEST FOR RESEARCH PERMIT:
MARTHA WANGUI- REG. NO. KESRA/105/0083/2017

This is to confirm that the above named is a student at Kenya School of Revenue Administration (KESRA) Nairobi Campus pursuing Masters in Tax & Customs Administration.

The named student is undertaking Research on **"EFFECT OF TAX INCENTIVES ON FOREIGN DIRECT INVESTMENT IN THE OIL AND GAS SECTOR IN KENYA.**

The purpose of this letter is to request your good office to assist the above student with the information to enable her work on her project.

Thank you.

Dr. Marion Nekesa PHD,
Head Academic Research
KESRA

KENYA SCHOOL OF REVENUE ADMINISTRATION (KESRA)
DEPUTY
30 OCT 2020
NAIROBI

Appendix V: NACOSTI Research Permit

REPUBLIC OF KENYA

NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION

Ref No: 526360

Date of Issue: 11/November/2020

RESEARCH LICENSE

This is to Certify that Miss. Martha Wangui of Kenya School of Revenue Administration, has been licensed to conduct research in Nairobi on the topic: Effect of Tax Incentives on Foreign Direct Investment in the Oil and Gas sector in Kenya for the period ending : 11/November/2021.

License No: BAHAMAS ABS/P/20/7611

526360

Applicant Identification Number

Director General
NATIONAL COMMISSION FOR SCIENCE,TECHNOLOGY & INNOVATION

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