

**EFFECT OF WITHHOLDING VALUE ADDED TAX ON THE VALUE
ADDED TAX REVENUE IN KENYA**

BY

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DECLARATION

Declaration by the Student:

This research project is my own original work and has not been presented for award of a degree in other examination body. No part of this work should be reproduced without my consent or that of Moi University.

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DEDICATION

I dedicate this work to my family who have without holding back; supported me allthrough during the period of my study, may God bless them.

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ABSTRACT

Value-added tax (VAT) withholding tax is a significant instrument used in various tax administrations to control revenue leakages that originate from taxpayers that charge VAT on their services and supplies and then fail to remit it to revenue authorities. The Kenya Revenue Authority (KRA) implemented VAT withholding in 2014 with the expectation that it would positively impact VAT revenue collection and compliance. The motivation of this study therefore arises from the knowledge that a number of developing countries are considering implementing a withholding tax mechanism on VAT revenue. The main objective of the study was to establish the impact of withholding VAT on VAT revenue in Kenya. The specific objectives included: to determine the effect of VAT withholding administration on VAT revenue collection in Kenya, to establish the effect of VAT withholding reform on VAT revenue collection in Kenya, to assess the effect of VAT withholding rates on VAT revenue collection in Kenya. The study was anchored on the ability to pay theory, the sacrifice theory and economic deterrence theory. The target population of the study was employees at KRA in Nairobi County. The study targeted 60 KRA employees involved in administration, collection and refund of VAT revenue. All the employees participated in the study; hence it was a census. Primary data was collected using a structured questionnaire. The study applied quantitative methods to analyse data. These included descriptive statistics such as percentages, means and standard deviation. Further, inferential statistics including correlation and regression analyses were conducted to determine the relationship between the independent variables and the dependent variable. The findings indicated that withholding VAT administration ($\beta=0.347$, $p=.012$), withholding VAT reforms ($\beta=0.284$, $p=.034$), and withholding VAT rates ($\beta=0.34$, $p=0.017$) had a positive and significant effect on VAT revenue. The study concluded that withholding VAT had a significant influence on VAT revenue in Kenya. The study recommended that the government through the necessary agencies such as KRA and Treasury ministry should strengthen VAT policies relating to withholding VAT administration, reforms and rates. The focus should be; Itax system, monitoring & evaluation, and compliance audit, VAT exemptions, number of tax collectors, penalties, audit skills, zero rated supplies, goods and services exemptions. Out of the limitations of the study, areas of further research have been pointed out. For instance, a study on the effect Withholding VAT system on the VAT refund/credit.

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ABBREVIATIONS/ACRONYMS

ETR:	Effective Tax Rate
IMF:	International Monetary Fund
KRA:	Kenya Revenue Authority
NACOSTI:	National Commission for Science, Technology and Innovation
OECD:	Organisation for Economic Co-operation and Development
SPSS:	Statistical Package for Social Sciences
VAWHT:	Value Added Withholding Tax
VAT:	Value-Added Tax
VIF:	Variance Inflation Factor

OPERATIONAL DEFINITION OF TERMS

VAT revenue collection is the act or process of getting money received from consumption which is charged at all stages of production, with the provision of a mechanism enabling firms to offset the tax they have paid on their own purchases of goods and services against the tax they charge on their sale of goods and services.

VAT withholding administration focuses on the assessment, collection and audit of VAT laws.

VAT Withholding rate is levied at varying rates (2% to 6%) on a range of payments to residents and non-residents.

VAT withholding reforms are measures undertaken to improve the efficiency of tax system and to maximise the economic and social benefits that can be achieved through the VAT tax system.

CHAPTER ONE

INTRODUCTION

1.0 Chapter Overview

This chapter provides background to the study, statement of the problem, objectives, hypotheses, significance and scope of the study.

1.1 Background to the Study

A Value-Added Tax (VAT) is a consumption tax placed on a product/service whenever value is added at each stage of the supply chain, from production to the point of sale (VAT Act 2013 Revised 2018). Withholding VAT is not a tax but a method of collecting VAT, a portion of VAT due by KRA appointed agents from the payments made for local taxable supplies (goods and services). Currently, the portion of VAT that is withheld is 2% out of the 16 % VAT (Wakaguyu wa- Kiburi, 2018). Withholding VAT allows the Kenya Revenue Authority (KRA) to collect VAT in advance from suppliers of taxable supplies. Under the withholding VAT system, KRA appoints selected local entities to be withholding VAT agents.

Registered withholding VAT agents are required to withhold 6% of the taxable value at the point of paying the suppliers (EY, 2016). VAT is a tax on consumer expenditure introduced in Kenya in January 1990 to replace the sales tax which was introduced in 1973 by the government. VAT was introduced as a measure to increase Government revenue through the expansion of the tax base, which hitherto was confined to sale of goods at manufacturing and importation level under the sales tax system. VAT is levied on consumption of taxable goods and a service supplied or imported into Kenya and is collected by registered persons at designated points who then remit it to the Commissioner.

Registered persons only act as VAT agents in collecting and paying the tax since the tax is borne by the final consumer of goods and services (Kenya Revenue Authority, 1990). Withholding tax system is a method whereby the payer of certain incomes is responsible for deducting tax at source from payments due to certain payees and remitting the tax so deducted to the Commissioner, on or before the 20th day of the following month (KRA2016). In Kenya, the following sources are attributable to Withholding tax with their respective rates as per Table 1.1 below.

Table 1.1: Income Sources

Type of Income	Resident (WHT) rate	Non- resident (WHT) rate
Interest Income	15%	15%
Dividends	5%	10%
Management fees	5%	20%
Contractual fees	3%	20%
VAT	6%	20%

Source: (KRA, 2016)

VAT is an indirect tax levied under the VAT Act (2013 Revised 2018) as consumption-based VAT. It was previously levied under VAT Act Cap 476 (1989) which has undergone several amendments including the year 1989 as a replacement to Sales Tax. Several public notices have also been issued over the years. VAT is charged on both local and imported supplies (goods and services) on every sale along the supply chain. Suppliers are able to deduct VAT input tax from their VAT output tax. The full VAT cost is borne by the end consumer (Wakaguyu wa-Kiburi, 2018).

Globally, VAT was first introduced in France in 1948 according to Azaria and Robinson (2005). Since its inception, VAT has proliferated around the world and has been embraced in most of the countries worldwide with an approximate increase of 20 per cent of the tax revenue in OECD countries and worldwide (OECD, 2014). Several Latin

American countries use VAT withholding system as a means of tackling tax evasion and increased revenue collections. While this scheme is believed to help in increasing revenue collections for governments, it is likely to create burden on companies' cash flows because refunds usually take longer time (Waerzeggers, 2008).

Most African countries have initiated major tax reforms, mainly by adopting VAT. As a result, from the start of the year 2010, more than 130 countries worldwide had VAT, and among the developing countries, around 70% (104 out of 144) have implemented this kind of indirect taxation. VAT has spread in regional bursts, in countries participating in International Monetary Fund (IMF) programmes and in countries with a low tax revenue performance in the past (Keen & Lockwood, 2012).

Majority of the countries in Africa including Kenya, Ethiopia, Ghana, Guinea, Niger, Nigeria, Senegal, South Africa, Tanzania and Uganda, have managed the international adaptation of VAT, of which owes its expansion to various factors including prospective increase of revenue when properly designed and administered, broadening of the tax base, making tax systems fairer and intending to reduce the burden of personal income taxes.

For example, in Australia the introduction of its VAT was accompanied by a cut in personal income tax, increases in government benefits, and removal of a number of taxes levied by the Australian States and Territories (OECD, 2001). In Kenya, the government had initiated the use of sales tax back in 1973 and was replaced by VAT in January 1990 (KRA 2010). This tax on consumption of goods and services has undergone a number of amendments since its inception.

For instance, according to KRA (2017) consumption taxes exhibited costing performance with VAT giving 21.2% growth. This growth has been exhibited for the

four consecutive years with annual growth averaging 21.5% between 2012/13 and 2016/17. This strong performance is attributed to enhanced compliance measures which among others include the expansion of withholding VAT framework which covers in total 3,231 large taxpayers (KRA, 2017).

Not all businesses (taxpayers) should register for VAT in Kenya. However, businesses with turnover of more than Kshs 5,000,000 per year of income are required to register. In addition, there are taxpayers who register for VAT voluntarily. Currently, the supplies are taxed at two tax rates, Standard rate of 16% and Zero-rate (0%). VAT is applicable along the supply chain in the businesses and charged where applicable on all supplies that are subject to the tax by registered taxpayers. When operating a VAT system, a taxpayer is supposed to account for the VAT to determine VAT compliance.

VAT should be collected at specific tax points in the business supply chain. Tax point referring to when tax is due and payable. However, the taxpayer can defer the payment up to the 20th of the following month. Failure to adhere to the requirements of the tax point results in penalties and interests as per the VAT Act 2013 and Tax Procedures Act 2015 (Wakaguyu wa-Kiburi, 2018).

1.2 Statement of the Problem

Empirical studies have shown the linkages between VAT revenue performance of a country and its level of development. According to Ebrill et al. (2001), the research on VAT revenue advances through the withholding tax system, the government collects higher revenue and as a result it improves the economy with higher level of per capita income, lower share of agriculture, and higher level of literacy. VAT proves to be an efficient tool for revenue collection and has direct impact on development of a country.

According to OECD (2014) on member states revenue sources, it was established that VAT is one of the major sources of revenue in many developed and developing countries. In most of the OECD partner countries, in the year 2012, VAT accounted for an average of 6.6 per cent of GDP of OECD member countries (OECD, 2013). To increase further VAT revenue collections and tackle the problem of evasion, some member countries like Kenya resulted to adopt the use of VAT withholding system. Ainsworth (2011) also noted that the rationale for using VAT withholding system is to ensure that unregistered traders, particularly in hard-to-tax sectors, are forced to pay at least some VAT. It has been claimed that this system provides a way of increasing VAT collections where administration is weak and attitudes to taxation is negative, particularly among small taxpayers (traders), where the risk of non-compliance is considered to be high.

According to Waerzeggers (2008), this system can result in an increased VAT burden for the supplier that never has access to or use of the VAT payment (withheld) and which may encounter difficulties in getting any refund if the withholdings lead to excess input tax credits. VAT withholding system creates cash flow challenges for compliant taxpayers who do not receive their excess VAT credit as a refund. The withholding system can lead to confusion among taxable persons who consider that they are freed from further VAT obligations when VAT has been withheld by their clients and who thus fail to subsequently declare the taxable supplies they have made. Fossat and Bua (2013) indicate that VAT withholding schemes encourage significant abuses on the part of the withholders, including delays in payment of the VAT withheld.

While VAWHT is perceived as a good tax policy by tax administrators, there are challenges in VAT revenue associated with its introduction. This research will address on the effect of VAWHT policy with respect to VAT revenue collection in Kenya.

However, to the researcher's knowledge, there appeared to be no research done on the perceived revenue implications with the use of VAWHT system in Kenya. The current study consequently assessed the effect of VAT withholding on the revenue in Kenya.

1.3 Research Objective

The study objectives were classified into general and specific objectives.

1.3.1 General objective

The general objective of the study was to establish the impact of withholding VAT on VAT revenue in Kenya.

1.3.2 Specific Objectives

The specific objectives included;

- i. To determine the effect of VAT withholding administration on VAT revenue collection in Kenya.
- ii. To establish the effect of VAT withholding reforms on VAT revenue collection in Kenya.
- iii. To assess the effect of VAT withholding rates on VAT revenue collection in Kenya.

1.4 Research Hypotheses

- i. H₀₁: VAT withholding administration has no significant effect on VAT revenue collection in Kenya.
- ii. H₀₂: VAT withholding reform has no significant effect on VAT revenue collection in Kenya.
- iii. H₀₃: VAT withholding rates has no significant effect on VAT revenue collection in Kenya.

1.5 Significance of the Study

The study findings may be important to several stakeholders including the Government of Kenya, tax experts (tax consultants), tax payers, scholars, academicians among others. The government of Kenya, specifically the Tax authority agent (KRA), may use the findings of the research for future policy formulation and implementation on matters affecting VAT Withholding administration on VAT revenue collection in the country.

The tax experts and taxpayers may use the research findings to advise their clients (taxpayers) on the tax planning while carrying out business transactions within and outside the country. The findings and policy recommendations of this study will be especially important to the Kenya Revenue Authority's department of domestic taxes in improving VAT revenue collection.

Scholars and academicians may use the research findings to enhance their academic literature in review of the VAT withholding effects on VAT revenue in the country. This may broaden their literature review theories and recommend for areas of further studies.

1.6 Scope of the Study

The researcher sought to establish the impact of withholding VAT on VAT revenue in Kenya. It focused on three aspects of withholding VAT: VAT withholding administration, VAT withholding reform and VAT withholding rates. The study targeted 60 KRA employees involved in administration, collection and refund of VAT revenue. Since the population was small, census sampling was adopted, hence all the employees participated in the study. Primary data was collected using a structured questionnaire. The study was conducted in 2021.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter presents a review of the literature. It covers the concepts of the study, the theoretical framework that grounds the variables, literature review in line with the study variables, critiques the literature to present the research gaps and the conceptual framework.

2.2 Concepts of the Study

2.2.1 VAT Revenue

Value added tax is a multi-staged tax that is charged on the value added to any services when they are offered and goods as they go through different stages of production and distribution (James 2015). A number of developing countries moved to a VAT system from sales tax because of the perceived intrinsic advantage in the collection process (Gerard and Naritomi 2018). VAT is a broad-based tax on the supply of goods and services, with methodical crediting of the tax paid on inputs. Since the introduction of VAT in France in 1948, it has spread around the world and been adopted in more than 160 countries around the world. It raises an average of 20 per cent of the total tax revenue collected in OECD countries and worldwide (UNCTAD 2018).

The international spread of VAT is due to various factors, including its potential to raise tax revenue when it is properly designed and administered (EPS-PEAKS 2013). Additional reasons for the spread of VAT include broadening the tax base, making tax systems fairer, and reducing the burden of personal income taxes. VAT revenue collection is the act or process of getting money received from taxation. VAT is a tax on consumption which is charged at all stages of production, with the provision of a

mechanism enabling firms to offset the tax they have paid on their own purchases of goods and services against the tax they charge on their sale of goods and services.

Taxpayers registered for VAT have many tax obligations clustered into; registration in the system, timely filing and lodgement of requisite taxation information, accurate and complete reporting of information and timely payment of VAT (OECD, 2014). The revenue produced by VAT depends on three broad sets of factors: the rules describing rates, bases, threshold and other structural features of tax; the scale of taxable activities (the amount of final expenditure, for instance, on items taxable at standard rate); and the degree to which the rules are complied with, (Ebrill *et al*, 2001).

2.2.2 Withholding VAT

Withholding VAT is a system which involves the declaration of VAT by both the supplier and his customer who has been appointed as a withholding VAT Agent. Institutions appointed as withholding VAT Agents are Government institutions, parastatals, banks, financial institutions, Co-operative Societies, Insurance companies and regular exporters (Brauner & Baez Moreno, 2015). VAT reforms are designed so that revenue collection could improve cross-border compliance for business (Spenser, 2012). VAT withholding administration focuses on the assessment, collection and audit of VAT laws.

VAT withholding reforms are measures undertaken to improve the efficiency of tax system and to maximise the economic and social benefits that can be achieved through the tax system. Withholding rate is levied at varying rates (3% to 25%) on a range of payments to residents and non-residents. The VAWHT system can lead to misperception among taxable persons who contemplate that they are freed from further VAT obligations when VAT has been withheld by their customers, and who thus fail to subsequently declare the taxable supplies they have made (Mugisha 2018). VAT

withholding systems encourage substantial abuse on the part of the withholders, including delays in payment of VAT withheld (Fossat and Bua 2013).

Withholding agents fail to remit withheld VAT to the treasury, often considering the withheld amount to be compensation for their own unpaid excess input tax credits or other claims on the treasury (PWC 2019). As a result, the VAWHT system adds a layer of VAT revenue complexity for taxpayers, withholding agents and the tax administration. In general, although opinions on VAWHT differ, there appears to be consensus that the proliferation of such systems can seriously undermine the integrity and long-term health of VAT (International Tax Dialogue 2015), and that VAWHT systems are not compatible with modern VAT (Fossat and Bua 2013). VAWHT agents must register with the tax administration, issue vouchers at the time of withholding the tax, and file a declaration of withheld VAT.

Several emerging countries have adopted a withholding tax scheme to combat sales and profit tax evasion by small firms and the self-employed. While withholding tax, in principle, does not change tax liability of firms, it can improve revenue collection in economies that have widespread evasion and a low level of compliance, or non-filing firms (Brockmeyer and Hernandez 2016). Like the third-party information report, information provided by withholding tax agents can be used to improve compliance with VAT and corporate income tax. The default payment mechanism of a withholding tax scheme in increasing VAT revenue collection (Brockmeyer and Hernandez 2016), in particular, could also be applicable for corporate income tax.

The withholding VAT (WHVAT) system in Kenya was initially introduced in 2004. Upon its introduction, designated WHVAT agents were required to withhold 100 per cent of VAT on paying suppliers and remit it directly to KRA. However, due to numerous challenges posed by the system at the time, the government repealed this in

2014. These challenges included large VAT refund claims being due to suppliers who were in a VAT refund position owing to the withheld VAT, certain WHVAT agents not remitting the tax withheld to the KRA, WHVAT agents delaying the issue of withholding tax credit certificates to suppliers, and suppliers failing to provide supporting documentation for WHVAT refund claims (KRA 2016).

The Kenyan Government re-introduced the WHVAT system in 2016, once the iTax electronic tax system had been fully rolled out. This has addressed some of the administrative challenges that WHVAT initially posed to taxpayers. The system continues to lead to critical cash flow challenges for suppliers who have to pay KRA the total output VAT without the right to offset the withheld VAT against their output tax, since tax credit certificates are not issued on a timely basis (KRA 2016).

In 2019, domestic VAT in Kenya grew by 12.3 per cent, driven by 9.8 per cent growth in value added tax turnover; this was mirrored in nominal GDP growth of 10.4 per cent. The domestic VAT growth was also explained by growth in WHVAT, and in particular growth in public sector withholding, which grew by 12.1 per cent (KRA 2019). Withholding VAT is governed by VAT Act 2013 however Section 26 of the Finance Act 2014 amended VAT Act 2013 by inserting a new section 25 A which re-introduced Withholding VAT (WHVAT) system at the rate of 6% which came into effect from 19th Sept. 2014. The reforms were introduced to help modernize the tax policies to take into account the changes in the operating environment (KRA, 2015).

2.3 Theoretical Review

The study was anchored on the Ability to pay theory, the sacrifice theory and economic deterrence theory.

2.3.1 Ability to pay theory

This theory originates from the sixteenth century. It was scientifically extended by the Swiss philosopher Jean Jacques Rousseau (1712-1778), the French political economist Jean-Baptiste Say (1767-1832) and the English economist John Stuart Mill (1806-1873). This theory holds that the taxation should be levied according to an individual's income or ability to pay and is the basis of progressive tax as the tax rate increases by the increase of the taxable amount (Jones *et al*, 2011).

This theory is indeed the most equitable tax system since people with greater income or wealth and can afford to pay more taxes should be taxed at a higher rate than people with less individual income tax and has been widely used in industrialized economics. However, there is no solid approach for the measurement of the equity of sacrifice in this theory, as it can be measured in absolute, proportional or marginal terms. Withholding VAT system does not tie in with this theory because the amount of VAT on a particular good shall be the same for everyone, however much they earn. VAT is thus regressive since it represents a smaller proportion of a person's income as their income rises.

2.3.2 The Equal sacrifice theory

This theory attempts to determine the burden that rests upon an individual in virtue of his payment of taxes and how much of his or her income remains for purpose of his own subsistence. According to this theory payment of tax is a sacrifice that an individual makes towards the support of the government (Majura Ibrahim, 2013). Asirigwa (2011), the equal-distribution theory also known as Equal sacrifice or Proportionate theory holds that income, wealth, and transaction should be taxed at a fixed percentage; that is, people who earn more should pay more taxes, but will not pay a higher rate of taxes. Thus, equal sacrifice can be measured as (i) each taxpayer

surrenders the same absolute degree of utility that s/he obtains from her/his income, or
(ii) each sacrifices the same proportion of utility s/he obtains from her/his income, or
(iii) each gives up the same utility for the last unit of income; respectively Asirigwa (2011).

The modern economists, however, differ with this view. They assert that when income increases, the marginal utility of income decreases. The equality of sacrifice can only be achieved if the persons with high incomes are taxed at higher rates and those with low income at lower rates. They favour progressive system of taxation, in all modern tax regimes. However, the application of this theory is shown in Section 25A of the VAT ACT 2013 which provides that, it is mandatory for Government Ministries, Departments and Agencies are required, on purchasing of taxable supplies, to withhold six percent of the tax payable thereon at the time of paying for the supplies and remit the same directly to the Commissioner. So, it touches to every individual who trades with the appointed withholding VAT agents.

2.3.3 Economic Deterrence Theory

Economic deterrence theory was advanced by Allingham and Sandmo (1972). The theory applies the expected utility model that explains criminal activity put forth by Becker (1968) to the taxation system. Economic deterrence model captures the concept of tax evasion by an economically rational taxpayer who evaluates the differences between tax evasion pay-off and the cost of being caught and decides to evade tax provided the pay-off from evading tax exceeds the expected cost of being caught. The evading taxpayer's expected utility function was captured in a seminal economic deterrence model proposed by Allingham and Sandmo (1972). The model captures several features of tax evasion. Primarily, the taxpayer who is more risk averse is less likely to engage in tax evasion as compared to one who is less risk averse.

Moreover, knowledge on the existing taxation system by the taxpayer is crucial in making an assessment regarding the probability of being detected, as well as the severity of the penalties attached to tax evasion once the taxpayer has been detected. The model therefore stipulates the decision-making criteria for the taxpayer specifically on how much tax they report to the taxing agency. In the process of making this decision by the taxpayer, they are guided by the need to maximize their individual expected utility construed as the sum of a single outcome utility value weighted against the probability of occurrence of that particular outcome.

Allingham and Sandmo model therefore depict a situation whereby greater probabilities of audit lead to increased deterrence on tax underreporting and lower levels of reported income are realized as a result of higher rate of the proportional tax. The general derivation of the theory therefore is that tax audit as well as penalty on evasion determines VAT compliance by taxpayers resulting to enhanced tax revenue. The theory therefore supports the VAT revenue variable in this study.

2.4 Empirical Literature Review

This section focuses on other studies that have been carried out on withholding VAT system as a measure to revenue collection.

2.4.1 Withholding VAT Administration and VAT Revenue

Majoni (2021) studied the effect of the introduction of VAT withholding tax on VAT compliance in Zimbabwe. The study used data of VAT registered clients in ZIMRA over a 24-month period. The study used an ordinary least squares multiple regression analysis to investigate the effects of VAT withholding tax on VAT revenue. The study further used a difference-in-differences estimator by classifying VAT taxpayers into two groups. Empirical evidence indicated that there was a positive significant

relationship between implementing VAT withholding tax and VAT revenue. Inoti (2008) evaluated the effectiveness of tax administration through tax agents in Kenya.

The specific objectives were: To evaluate whether the VAT agents cost of implementation led to an effective administration of tax; whether the agents personnel training led to an effective administration of tax; and if the agents cost of compliance led to an effective administration of tax. Data was collected from a survey sample of 80 agents in Nairobi. The findings showed that most agents use manual or semi-manual systems and did not change their payment processes upon appointment. The additional costs of computer facilities, personnel and administration costs were within the acceptable threshold of one to three percent. Training of agents through KRA workshops, in-house training by knowledgeable peers and outside tax consultants was the frequent training methods used by the agents. The study concluded that the administration of VAT, by VAT agents was cost effective.

Gideon and Alouis, (2013) carried out a study in Zimbabwe to reviews national revenue collection in Zimbabwe, particularly interrogating major revenue sources, revenue collection strategies and soft spots for revenue leakage. The findings indicate that the revenue collection sector has over the decades gone through milestone reforms, notable ones being the establishment of a sole national revenue authority in 2001, the shifting from cumbersome Income Tax Return Forms to Final Deduction Systems, the adoption of VAT in 2004 and Toll Gate systems in 2009. The discovery of diamonds in 2006 (with a potential to generate US\$2billion dollars a year and even supply 25% of the world demand) was an added boost which is set to broaden national revenue generation and collection.

There is need to review the structural and operational frameworks governing the national revenue authority, tighten treasury control over all national revenue sources, strengthen legislative oversight and the public audit functions, plug loose areas in income tax frameworks as well as instituting transparency in national revenue remittance processes. Yesegat (2016) carried a study on the impact of withholding VAT scheme on revenue in Ethiopia of which the results indicated that the rationale for using VAT withholding scheme was to ensure that unregistered traders, particularly in hard-to-tax sectors, are forced to pay at least some VAT. It is claimed that these schemes provide a way of increasing VAT collections where administration is weak and attitudes to taxation are poor, particularly among smaller traders, where the risk of non-compliance is considered to be high.

For example, as Ainsworth (2011) notes Ecuador responded to VAT fraud in small and medium sized businesses by extending VAT withholding to third-party credit/debit card companies. As Ainsworth (2011) further indicates the Ecuadorian regime addresses a common policy concern; the problem of small suppliers. These sellers frequently make supplies, charge VAT, and do not report the transaction. VAT withholding is an attempt to limit evasion in the small business sector (Ainsworth 2011).

However, VAT withholding scheme can lead to several problems. Waerzeggers (2008) indicates that this scheme can result in an increased VAT burden for the supplier that never has access to or use of the VAT payment and which may encounter difficulties in getting any refund if the withholding leads to excess input tax credits. VAT withholding schemes create cash flow problems for compliant firms that do not receive their excess VAT credit. The cash flow difficulties this system creates have been severe enough in some jurisdictions to force VAT withholding to be removed; VAT

withholding is not the 'perfect' solution to under-reporting by small businesses (Ainsworth, 2011).

Fossat and Bua (2013) also emphasize that while VAT withholding may have an initial positive impact in terms of revenue collections it also results in serious cash flow problems for suppliers. Fossat and Bua (2013) further note that opponents of the scheme point to the increase in refund claims if withholding rates are set too high.

2.4.2 Withholding VAT Reform and VAT Revenue

Mokua (2012) carried out a study to investigate the impact of tax reforms that have been undertaken in income tax, excise duty, import duty and sales/value added tax on revenue productivity. The study sought to specifically estimate the effect of tax reforms on buoyancy of Income tax and Value Added tax, as well as estimating the effect of the reforms on elasticity of the tax system. Published secondary data was used to analyse the relationship between tax reforms and revenue productivity and before, after piecemeal/policy and during the comprehensive reform buoyancy and elasticity were estimated using regression analysis.

The regression result showed that total tax in Kenya was inelastic during the three periods, but it was buoyant during the pre-reform and piecemeal reform periods. In spite of the good performance of income tax as a result of reforms, further reforms need to be done particularly on the inelastic value added tax. Adam and Johnson (2012) in a study in the United Kingdom focused on reforms that could increase national income in the medium term, not on possible short-term stimulus to promote economic recovery. Emphasis that economic growth (that is, increases in national income) and increases in welfare are not synonymous. There are many welfare -enhancing reforms to the tax

system which should be pursued even if they don't promote growth. And there are growth-promoting but welfare -reducing reforms which should not be pursued.

In general, a tax system that is significantly more neutral than the current one would do less to distort economic activity, would involve lower administration and compliance costs, and would increase both national revenue and welfare. The scope for reform in this direction is substantial. There exists some subjective evidence about the implementation of tax reforms to enhance tax compliance, especially in African countries. Generally, tax reform deals with welfare improvement by making marginal changes in tax design and structure in fact there has been a growing concern over mobility of capital across international frontiers, Europe countries.

Muriithi and Moyi (2013) carried out a study to analyse the productivity of Kenya's tax structure in the context of the tax reforms. The findings suggest that tax reforms had a positive impact on the overall tax structure and on the individual tax handles, even though the impact of the reforms was not always uniform. The reforms had a bigger impact on direct taxes than on indirect taxes, suggesting that revenue leakage is still a major problem for indirect taxes. The better responsiveness of direct taxes can be attributed to the relative effectiveness of the reforms in direct taxes, which not only made the tax system simpler but also reduced avenues for evasion and corruption. Such reforms include the introduction of PIN, lower rates, reduction of exemptions and a shift away from multiple rates across many categories.

2.4.3 Withholding VAT Rates and VAT Revenue

Alavuotunki, Haapanen and Pirttilä (2019) studied impact of the introduction of the value-added tax on inequality and government revenues using newly released macro data. The researchers presented both conventional country fixed effect regressions and

instrumental variable analyses, where VAT adoption was instrumented using the previous values of neighbouring countries' VAT systems as an instrument. The results revealed in contrast to earlier work that the revenue consequences of the VAT have not been positive. The results indicated that income-based inequality has increased due to the VAT adoption, whereas consumption inequality had remained unaffected.

Nyangau (2017) established the effect of withholding VAT on tax compliance in Kenya. The explanatory study design was used. Data was compiled for a period spanning 7 years from the year 2011 to 2017 on Withholding VAT Revenue growth and VAT revenue growth as well as economic growth which is a control variable in the study. A regression model was used for establishing the relationship between the study variables. The one-way Anova was performed on the average figures for all the measures of performance. The results for the three categories of taxpayers revealed that there was a significant difference in the one-way Anova. From the results, the research concluded that there was significance improvement in tax compliance after the enforcement of withholding VAT tax policies in Kenya.

Asirigwa (2011) evaluated the determinants of VAT revenue in Kenya. The study utilized secondary data obtained from the KRA database for the financial years 1995/6 to 2009/10. The analysis showed that the determinants of VAT revenue have a significant effect on the responsiveness of VAT revenue. This implies that the growth in VAT revenue during the period of study was accounted for by changes in its determinants. The study found that multiple rates, higher range between highest and lowest non-zero VAT rates, and the longer the VAT has been in operation (age of the VAT) are associated with higher revenues.

2.5 Research Gaps

The review of existing literature revealed several research gaps that informed to carry out the current research. For instance, a number of the studies reviewed were conducted in other countries such as Zimbabwe (Majoni, 2021), Ethiopia (Yesegat, 2016) and United Kingdom (Adam & Johnson, 2012). These countries operate in different environments from that of Kenya, thus making it impractical to generalize their findings to explain the local situation. The current study therefore, sought to fill the contextual gap.

Further, a study by Alavuotunki, Haapanen and Pirttilä (2019) established that the relationship between VAT and revenue was not positive. The study findings contradicted those of Yesegat (2016) who had determined that withholding VAT positively influenced revenue collections. The current study sought to fill the empirical gap as a result of mixed findings. Additionally, some of the reviewed studies indicated conceptual gaps. For instance, Muriithi and Moyi (2013) focused on productivity of tax structure as the dependent variable. On the other hand, Nyangau (2017) used tax compliance as the dependent variable. The current study used tax revenue as the dependent variable.

2.6 Conceptual Framework

The VAT revenue was the dependent variable in this study. The set of factors that have to be analysed are the independent variables. As per the Figure 2.1, VAT withholding system affects the VAT revenue.

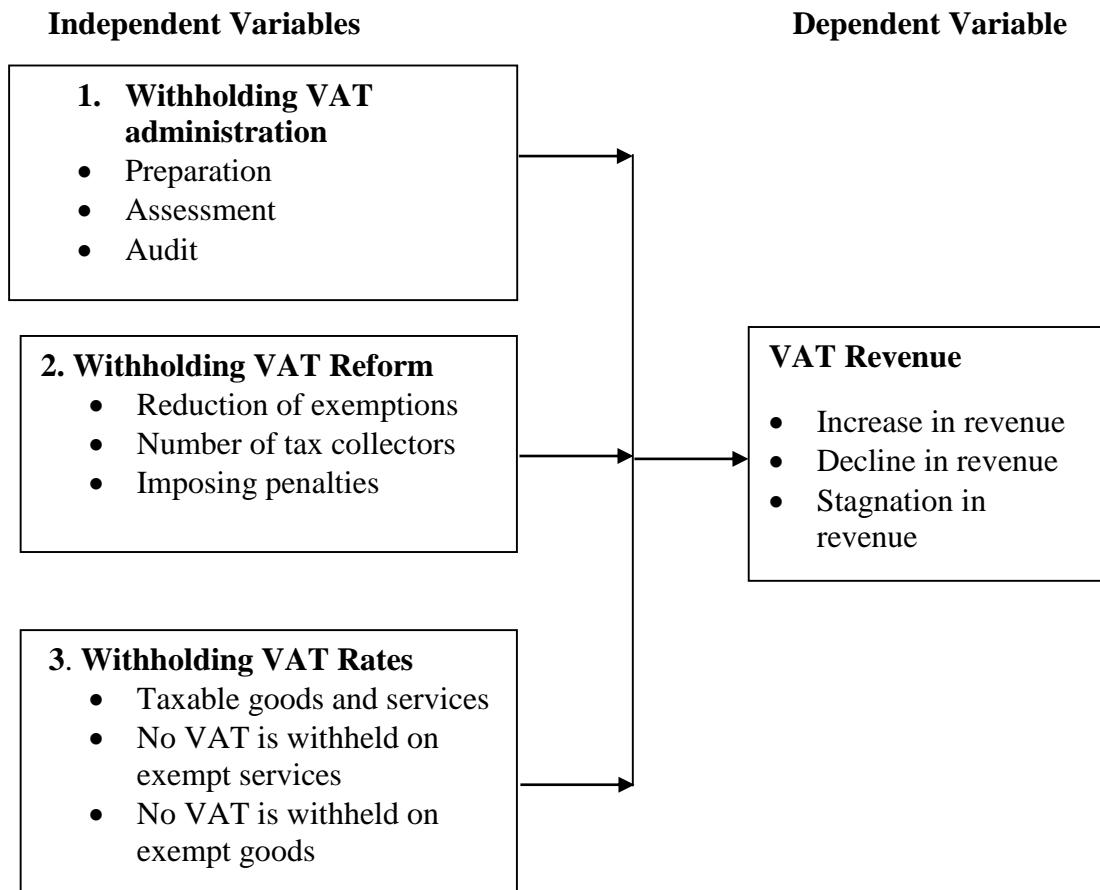


Figure 2.1: Conceptual framework

Source: Researcher (2021)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents the methods and procedures that were used to carry out the study. These included; research design, target population and sampling methods, data collection instrument and procedure, pilot study, data analysis and presentation and ethical considerations.

3.2 Research Design

Research design refers to the overall strategy that is chosen to present the research in a coherent and logical manner thus ensuring that the research problem is adequately addressed (Coopers & Schindler, 2003). The study used explanatory research design. The design helps in explaining the causal relationship between variables (Rahi, 2017). The aim of the study was to determine the impact of withholding VAT on VAT revenue in Kenya. Therefore, explanatory research design helped in establishing the relationship between these variables.

3.3 Target Population

The unit of study is the population element on which the measurement is being conducted on (Cooper, 2010). The study target population was 60 KRA employees working in the VAT administration, collection and refund department (both large and small tax payers). The choice of these employees was because they are involved with activities relating to withholding VAT. A census of all the employees was done since the number was manageable.

3.4 Type and Sources of data

This study collected primary data using a structured questionnaire. This study was purely quantitative and therefore, used questionnaires to acquire primary data from KRA employees.

3.5 Research instrument

This study used questionnaires as data collection instrument. The use of questionnaires as instrument of data collection tend to be less costly, use less time, require less administrative effort. Questionnaires also make it simple to compile data after collection. The questionnaire contained questions relating to the study variables. The questions were in form of a 5-Likert scale. The rating scale included: 1-Not at all, 2-small extent, 3-moderate extent, 4- great extent, and 5-very great extent. The questionnaire was divided into two parts. The first part asked questions related to background information. The second part contained questions relating to the study variables.

3.6 Data Collection Procedure

The researcher administered the questionnaires to the respondents using the drop and pick later method. This gave the respondents adequate time to comprehend the questions and give accurate responses. To help with data collection, the researcher acquired the services of two experienced research assistants. Prior to starting the data collection exercise, the research assistants were briefed on the data collection process.

3.7 Pilot Study

The pilot study helps to test the reliability of the data collection instrument. Mugenda and Mugenda (2003) cited that 5 to 10% of the target population is enough for pilot study. The researcher administered questionnaires to six respondents who were not part

of the study population. The responses from the pilot study indicated that Withholding VAT system has an effect on VAT revenue with respect its administration and were excluded from the main data to avoid bias.

3.7.1 Validity of Research Instrument

Validity refers to the extent to which an instrument measures what is supposed to measure (Remenyi, 2015). This study tested content and construct validity of the instrument. To ensure content validity, the study supervisor went through the questionnaire and made recommendations for improvement. Further, construct validity was assured by arranging the questionnaire into several sections based on the study variables.

3.7.2 Reliability of Research Instrument

Reliability is the extent to which a test in the research is internally consistent and yields consistent results upon testing and retesting (Orodho, 2009). The study tested the instrument's reliability using Cronbach's Alpha Coefficient (Cronbach, 1951). The alpha coefficient ranges in value from 0 to 1. Cronbach's alpha coefficient value of 0.7 was used as the cut-off point and all items with values greater than 0.7 were considered reliable.

3.8 Data Analysis and Presentation

The data captured was coded and analysed using statistical measures such as percentages, totals, mean and standard deviations. The Statistical Package for Social Sciences (SPSS) version 20 was used in data analysis. The mean, for instance, was used to measure the general response to a question by the respondents. The standard deviation was used to measure the variability in the responses to a question. The percentages were used to measure the shares of respondent in a given category.

Inferential statistics including correlation and multiple regression analyses were used to establish the relationship between the independent and dependent variable. The research findings were presented using frequency tables, charts and graphs.

The following model was estimated.

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon$$

Where;

Y = VAT Revenue

X_1 = Withholding VAT Administration

X_2 = Withholding VAT Reform

X_3 = Withholding VAT Rates

β_0 = Constant

β_1 , β_2 and β_3 = regression coefficients

ε = error term

3.8.1 Regression Assumptions

Prior to running the regression analysis, several assumptions were tested to make sure that the analysis results are accurate and free from bias. The tests included; multicollinearity, normality, linearity, and heteroscedasticity test.

3.8.2 Multicollinearity Test

Multicollinearity occurs when there is high correlation between the independent variables, which affects the significance of the individual variables. The Variance Inflation Factor (VIF) was used to check for multicollinearity. A VIF value more than 10 implies presence of multicollinearity problem while a VIF value less than 10 implies

no multicollinearity problem. Furthermore, the tolerance value greater than 0.2 implies that independent variables are not highly correlated.

3.8.3 Normality Test

Normality test improves the regression model by ensuring the data is normally distributed. Normality of data was tested using the Shapiro-Wilk test. The criterion is that the probability value should be greater than 0.05 for the data to be normally distributed (Thornhill, Saunders & Lewis, 2009).

3.8.4 Linearity Test

Linearity was tested using scatterplots, which is used to show whether there is a linear relationship between two continuous variables. It was expected that the relationship between variables should be fairly linear before the regression models are applied (Jain et al., 2017).

3.8.5 Heteroscedasticity Test

If the error variance is not constant, then there is Heteroscedasticity in the data. Running a regression model without accounting for Heteroscedasticity would lead to biased parameter estimates. Levene's test for equity of change was utilized to test for homogeneity of fluctuation (Parra-Frutos, 2013). The null hypothesis is that the variance of error term is constant. A probability value >0.05 leads to acceptance of the null hypothesis, implying that there is no heteroscedasticity.

3.9 Measurement of variables

The table 3.1 below shows the measurements of the variables:

Table 3.1: Measurements of variable

<i>Objectives</i>	<i>Variable Indicators</i>	<i>Variable type</i>	<i>Data instrument</i>	<i>Scale</i>	<i>Data analysis</i>
To determine the effect of VAT withholding administration on VAT revenue collection in Kenya	Withholding VAT administration <ul style="list-style-type: none"> • Preparation • Assessment • Audit 	Independent Variable	Questionnaire	5-Point Likert Scale	Descriptive, Correlation & Regression
To establish the effect of VAT withholding reforms on VAT revenue collection in Kenya	Withholding VAT Reform <ul style="list-style-type: none"> • Reduction of exemptions • Number of tax collectors Imposing penalties 	Independent Variable	Questionnaire	5-Point Likert Scale	Descriptive, Correlation & Regression
To assess the effect of VAT withholding rates on VAT revenue collection in Kenya	Withholding VAT Rates <ul style="list-style-type: none"> • Taxable goods and services • No VAT is withheld on exempt services • No VAT is withheld on exempt goods 	Independent Variable	Questionnaire	5-Point Likert Scale	Descriptive, Correlation & Regression

3.10 Ethical Considerations

This study observed all ethical considerations of practice and procedures that comply with issues regarding confidentiality, privacy and prior informed consent (Oso & Onen, 2008). The researcher maintained the confidentiality of sensitive information received from the respondents. The researcher also gave due credit to authors in order to avoid plagiarism. Prior consent was obtained from potential interviewees before the respondents are interviewed. The researcher also got a research permit from NACOSTI to collect the data.

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSION

4.1 Introduction

This chapter presents the study findings and discussion. The chapter starts by providing results on reliability test and response rate. Further, the findings on demographic information of the respondents are provided. Descriptive analysis results are then provided followed by diagnostic tests, correlation results and finally regression results are presented.

4.2 Reliability Results

Reliability of the questionnaire was tested using Cronbach alpha coefficients. The results are presented in Table 4.1.

Table 4.1: Reliability Test

Variable	No of Items	$\alpha > 0.7$	Comment
Withholding VAT administration	4	0.735	Reliable
Withholding VAT reforms	5	0.834	Reliable
Withholding VAT rates	5	0.910	Reliable
VAT Revenue	4	0.726	Reliable

Source: Research Data (2021)

The data obtained from the pilot study was used to run the reliability test. The variables' coefficients were as follows: Withholding VAT administration [0.735], withholding VAT reforms [0.834], withholding VAT rates [0.910] and VAT revenue [0.726]. All the variables had Cronbach alpha coefficients greater than 0.7 suggesting that the items in the questionnaire were dependable.

4.3 Response Rate

The researcher administered 60 questionnaires to KRA employees working in the VAT refund department. Out of 60 questionnaires administered, 37 were successfully filled and returned representing 62% response rate. The remaining questionnaires were either unreturned or incorrectly filled. A response rate above 50% is considered adequate for analysis (Saunders et al., 2009), The response rate obtained of 62% from this study was thus considered to be adequate for statistical analysis.

4.4 Demographic information of the respondents

This section presents findings based on the demographic information of the respondents. The specific items included gender, age, education, and work duration. Table 4.2 shows the results.

Table 4.2: Demographic information of the respondents

Variables	f	%
Gender		
Female	18	48.6
Male	19	51.4
Total	37	100
Age		
26-35 years	15	40.5
36-45 years	19	51.4
46-55 years	2	5.4
Above 55 years	1	2.7
Total	37	100
Education level		
Postgraduate	23	62.2
Undergraduate Degree	14	37.8
Total	37	100
Work duration		
5-10 years	9	24.3
Below 5 years	11	29.7
Over 10 years	17	45.9
Total	37	100

Source: Research Data (2021)

The findings indicate that majority (51.4%) of the respondents were male, while 48.6% were female. This implied that there was fair representation of both gender in this study and therefore the responses were considered reliable. Results also reveal that 51.4% of the respondents were aged 36-45 years and 40.5% were aged 26-35 years. This implied that majority of the respondents were middle aged and therefore active enough to provide relevant information relating to the study. On education, 62.2% of the respondents noted that they had attained postgraduate level while 37.8% had undergraduate degree.

This denoted that all the respondents had adequate educational qualification and therefore had a better understanding of the study topic with relevant tax policies and reforms. In terms of work duration, 45.9% of the employees cited that they had worked in the institution for over 10 years. This suggested that the employees had adequate experience, knowledge and information relating to withholding VAT and VAT revenue in Kenya.

4.5 Descriptive Analysis

This section provides descriptive analysis results based on the study variables. The specific descriptive statistics used include percentage, mean and standard deviation. A five-point Likert scale was adopted as follows: 1-No at all, 2- small extent, 3-moderate extent, 4- great extent, and 5-very great extent.

4.5.1 Withholding VAT Administration

The respondents were asked to rate statements relating to withholding VAT administration and the responses were presented in Table 4.3.

Table 4.3: Descriptive statistics of withholding VAT administration

Statement	Not at all	Small extent	Modera te extent	Great extent	Very great extent	M	S. D
KRA preparation (Itax system) affects VAT revenue collection.	2.7%	0.0%	10.8%	16.2%	70.3%	4.5	0.9
KRA Self-assessment affects VAT revenue collection.	2.7%	0.0%	5.4%	29.7%	62.2%	4.5	0.8
KRA Compliance audit affects VAT revenue collection.	0.0%	0.0%	13.5%	21.6%	64.9%	4.5	0.7
KRA Investigations audit affect VAT revenue collection.	0.0%	0.0%	18.9%	32.4%	48.6%	4.3	0.8
Aggregate mean						4.5	0.8

Source: Research Data (2021)

Majority of the respondents (70.3%) noted to a very great extent that KRA preparation (Itax system) affects VAT revenue collection, 62.2% cited to a very great extent that KRA Self-assessment affects VAT revenue collection, 64.9% noted to a very great extent that KRA Compliance audit affects VAT revenue collection and 48.6% highlighted to a very great extent that KRA investigations audit affect VAT revenue collection. The implication is that withholding VAT administration is paramount in determining VAT revenue.

4.5.2 Withholding VAT Reforms

The respondents were asked to rate statements relating to withholding VAT reforms and the responses were presented in Table 4.4.

Table 4.4: Descriptive statistics of withholding VAT reforms

Statement	Not at all	Small extent	Moderate extent	Great extent	Very great extent	Mean	S. D
Reduction of VAT exemptions affects VAT revenue collection.	2.7%	2.7%	24.3%	32.4%	37.8%	4.0	1.0
Increasing the number of tax collectors (Agents) affects VAT revenue collection	2.7%	2.7%	16.2%	18.9%	59.5%	4.3	1.0
Imposing tougher penalties for those found guilty of evasion affects VAT revenue collection	0.0%	8.1%	8.1%	40.5%	43.2%	4.2	0.9
Strengthening audit skills effects VAT revenue collection	2.7%	2.7%	10.8%	35.1%	48.6%	4.2	1.0
lowering rates affects VAT revenue collection	8.1%	2.7%	16.2%	16.2%	56.8%	4.1	1.3
Aggregate mean						4.2	1.0

Source: Research Data (2021)

The respondents agreed to a very great extent that reduction of VAT exemptions affects VAT revenue collection (37.8%), increasing the number of tax collectors (Agents) affects VAT revenue collection (59.5%), imposing tougher penalties for those found guilty of evasion affects VAT revenue collection (43.2%), strengthening audit skills effects VAT revenue collection (48.6%), and lowering rates affects VAT revenue collection (56.8%). The implication is that withholding VAT reforms are essential in determining VAT revenue.

4.5.3 Withholding VAT Rates

The respondents were asked to rate statements relating to withholding VAT rates and the responses were presented in Table 4.5.

Table 4.5: Descriptive statistics of withholding VAT Rates

Statements	Not at all	Small extent	Moderate extent	Great extent	Very great extent	Mean	Std.dev
Taxable goods and services exported are subject to double taxation on withholding VAT and this affects VAT revenue	32.4%	16.2%	8.1%	27.0%	16.2%	2.8	1.5
No VAT is withheld on exempt goods and this affects VAT revenue	27.0%	8.1%	2.7%	27.0%	35.1%	3.4	1.7
No VAT is withheld on exempt services and this affects VAT revenue	29.7%	8.1%	2.7%	27.0%	32.4%	3.2	1.7
No VAT is withheld on Zero rated supplies and this affects VAT revenue	29.7%	8.1%	0.0%	24.3%	37.8%	3.3	1.7
Reduction of withholding VAT rate has been reduced from 6% to 2% affected VAT revenue.	2.7%	5.4%	18.9%	29.7%	43.2%	4.1	1.1
Aggregate mean						3.5	1.5

Source: Research Data (2021)

The respondents disagreed with the statement that taxable goods and services exported are subject to double taxation on withholding VAT and this affects VAT revenue (32.4%), however, 27% of them agreed to a great extent with the statement. Further, 35.1% of the respondents agreed to a very great extent that no VAT is withheld on exempt goods and this affects VAT revenue, 32.4% agreed to a very great extent that no VAT is withheld on exempt services and this affects VAT revenue, 37.8% agreed to a very great extent that no VAT is withheld on Zero rated supplies and this affects VAT revenue, and 43.2% agreed to a very great extent that reduction of withholding VAT

rate has been reduced from 6% to 2% affected VAT revenue. The implication is that withholding VAT rates are critical in determining VAT revenue.

4.5.4 VAT Revenue

The respondents were asked to rate statements relating to VAT revenue and the responses were presented in Table 4.6.

Table 4.6: Descriptive statistics of VAT Revenue

Statements	Not at all	Small extent	Moderate extent	Great extent	Very great extent	Mean	Std. dev
The amount of VAT revenue collection has increased.	2.7%	8.1%	8.1%	32.4%	48.6%	4.2	1.1
The amount of VAT revenue collection has declined.	27.0%	29.7%	18.9%	10.8%	13.5%	2.5	1.4
The amount of VAT revenue collection has stagnated.	35.1%	27.0%	32.4%	2.7%	2.7%	2.1	1.0
VAT revenue as a percentage of GDP has improved.	5.4%	5.4%	24.3%	35.1%	29.7%	3.8	1.1
Aggregate mean						3.1	1.1

Source: Research Data (2021)

The respondents agreed to a very great extent that the amount of VAT revenue collection has increased (48.6%). They also agreed to a small extent that the amount of VAT revenue collection has declined (29.7%) and further disagreed that the amount of VAT revenue collection has stagnated (35.1%). In addition, the respondents agreed to a great extent that VAT revenue as a percentage of GDP has improved (35.1%). The findings implied that though VAT revenue had improved; the improvement was moderate.

4.6 Regression Assumptions

Regression assumptions were tested to ensure that the study findings were accurate and free from bias. The assumptions were; multicollinearity, normality, linearity and heteroscedasticity tests.

4.6.1 Multicollinearity Test

Multicollinearity was assessed in this study using the VIF. According to Field (2009), VIF values in excess of 10 is an indication of the presence of multicollinearity and vice versa. Results are shown in Table 4.7.

Table 4.7: Multicollinearity test using VIF

Variables	Tolerance	VIF
Withholding VAT Administration	0.797	1.255
Withholding VAT Reforms	0.821	1.217
Withholding VAT Rates	0.751	1.332

Source: Research Data (2021)

Results showed that the value of VIF ranged from 1.21 to 1.33, which was less than 10. This implied the independent variables (withholding VAT administration, withholding VAT reforms and withholding VAT rates) were not highly correlated. Hence, there was no multicollinearity.

4.6.2 Normality Test

Normality of data was tested by use of Shapiro-Wilk test. The null hypothesis was that the data is normally distributed. The rule is that if the p-value is greater than 0.05, H₀ is not rejected, if the p -value is less than 0.05, H₀ is rejected. Normality tests were conducted in Table 4.8.

Table 4.8: Normality test using Shapiro Wilk

Variables	Statistic	df	Sig.
VAT Revenue	0.933	37	0.069
Withholding VAT Administration	0.884	37	0.210
Withholding VAT Reforms	0.932	37	0.070
Withholding VAT Rates	0.848	37	0.110

Source: Research Data (2021)

The study findings indicate that all the variables had P values >0.05 , resulting to non-rejection of the null hypothesis of normal distribution. Therefore, the data was normally distributed.

4.6.3 Linearity test

Linearity test was conducted using scatter plots, which are used to indicate if two continuous variables have a linear relationship.

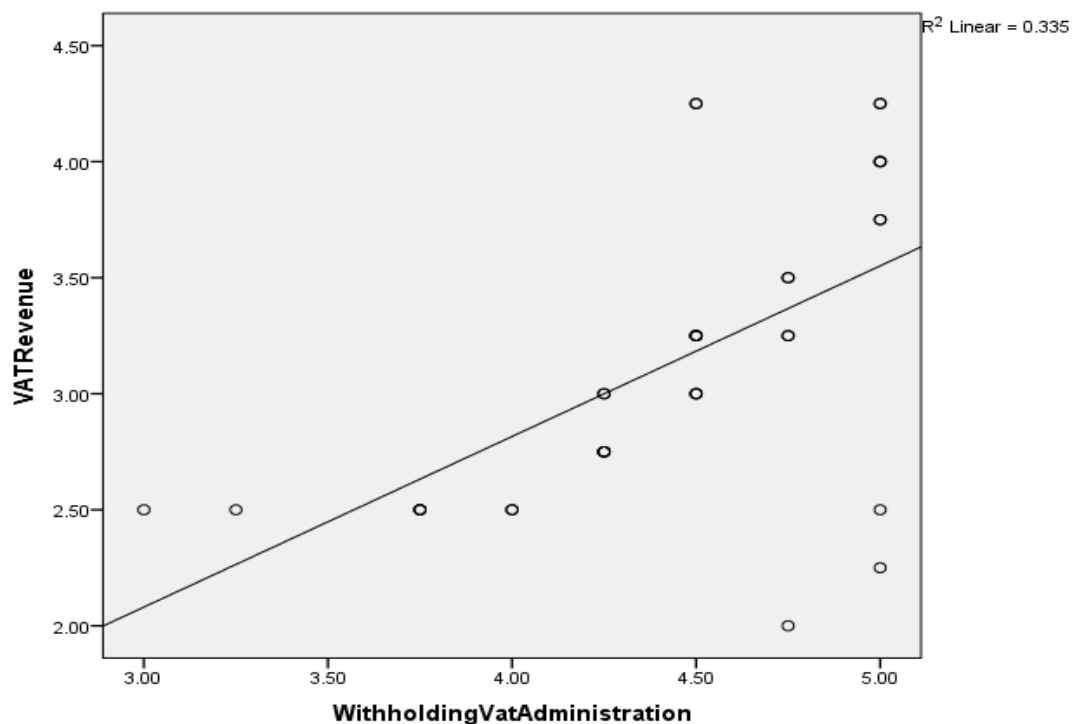


Figure 4.1: Linearity between withholding VAT administration and VAT revenue

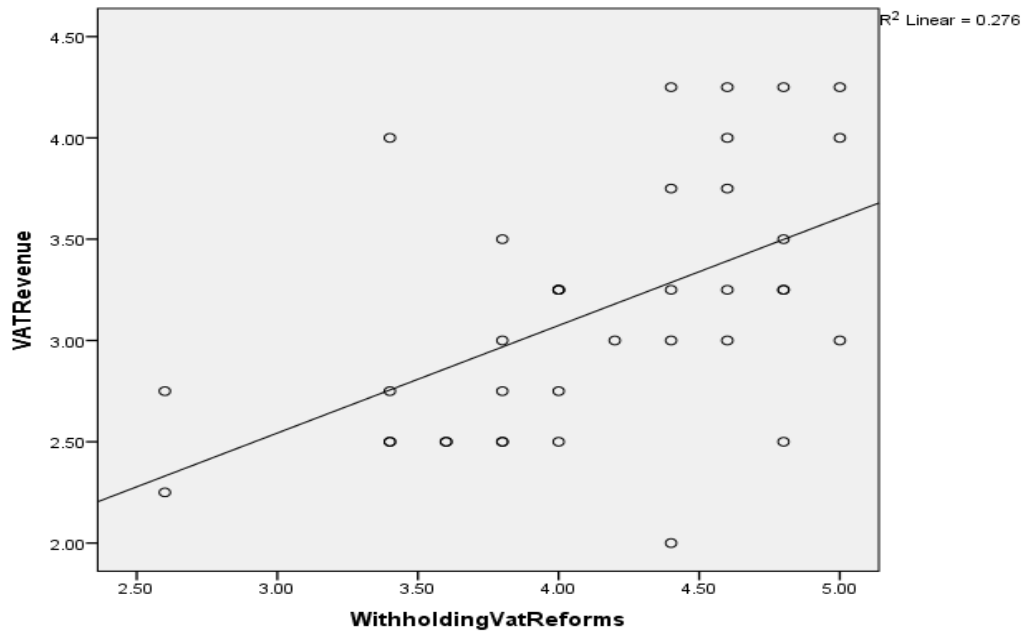


Figure 4.2: Linearity between withholding VAT reforms and VAT revenue

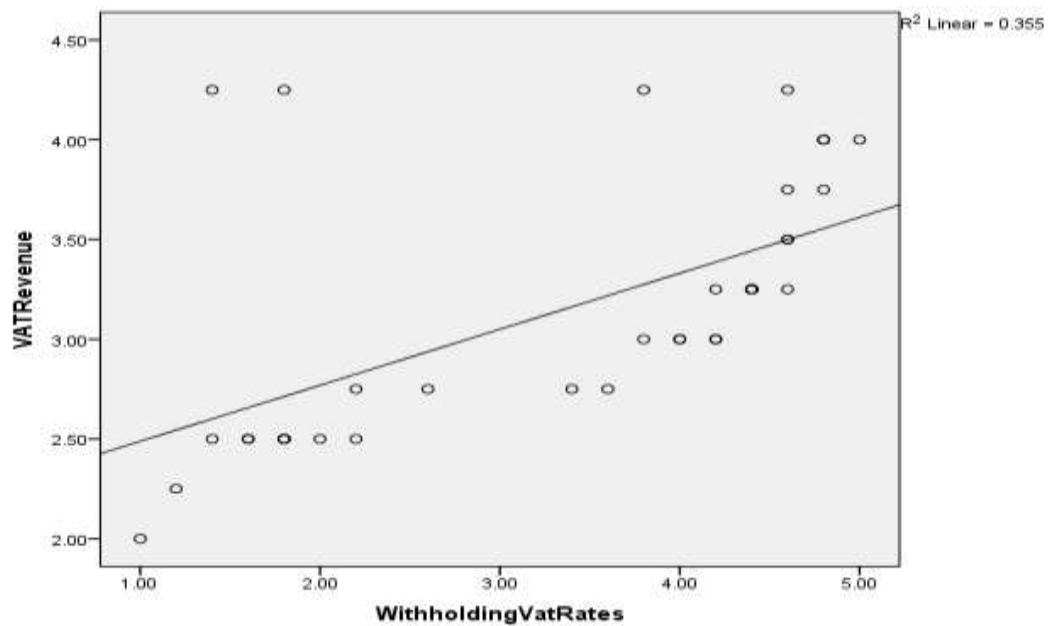


Figure 4.3: Linearity between withholding VAT rates and VAT revenue

The findings (Figure 4.1, 4.2, 4.3) reveal that the relationship between each of the independent variables (withholding VAT administration, withholding VAT reforms, withholding VAT rates) and dependent variable (VAT revenue) was linear. This was demonstrated by a straight line (line of fit).

4.6.4 Heteroscedasticity Test

Heteroscedasticity test was conducted using the Levene's test. Results are shown in Table 4.9.

Table 4.9: Levene's test

Dependent Variable: VAT Revenue			
F	df1	df2	Sig.
2.204	7	29	0.064

Tests the null hypothesis that the error variance of the dependent variable is equal across groups.

a Design: Intercept + x₁, x₂, x₃

The study findings reveal a significance (Sig.) value of 0.064, which is greater than 0.05. This implied that the null hypothesis of constant variance of error terms was accepted. Therefore, the variance of the residuals was homogeneous.

4.7 Correlation Analysis

Correlation analysis was conducted to quantify the relationship between the independent variables and the dependent variable. Pearson correlation coefficient (r) which ranges between -1 and +1 and quantifies the direction and strength of the linear association between the two variables was used. The results are presented in Table 4.10.

Table 4.10: Correlation Matrix

		VAT Revenue	Withholding VAT Administration	Withholding VAT Reforms	Withholding VAT Rates
VAT Revenue	Pearson Correlation	1	.578**	.525**	.595**
	Sig. (2-tailed)		.000	0.001	.000
Withholding VAT Administration	Pearson Correlation		1	0.314	.420**
	Sig. (2-tailed)			0.058	0.01
Withholding VAT Reforms	Pearson Correlation			1	.388*
	Sig. (2-tailed)				0.018
Withholding VAT Rates	Pearson Correlation				1
	Sig. (2-tailed)				

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

* Correlation is significant at the 0.05 level (2-tailed).

Source: Research Data (2021)

Results showed that withholding VAT administration had a positive and statistically significant association with VAT revenue ($r = 0.578$, $p = 0.000$). This meant that both variables change in the same direction. As such, an increase in withholding VAT administration is accompanied by increase in VAT revenue.

Findings also indicate that withholding VAT reforms had a positive and statistically significant association with VAT revenue ($r = 0.525$, $p = 0.000$). This meant that both variables change in the same direction. As such, an increase in withholding VAT reforms is accompanied by increase in VAT revenue.

Further, results indicate that withholding VAT rates had a positive and statistically significant association with VAT revenue ($r = 0.595$, $p = 0.000$). This meant that both variables change in the same direction. As such, an increase in withholding VAT rates is accompanied by increase in VAT revenue.

4.8 Regression Analysis

Regression analysis was done to determine the effect of the independent variables (withholding VAT administration, withholding VAT reforms, withholding VAT rates) on the dependent variable (VAT revenue).

Model summary results were presented in Table 4.11.

Table 4.11: Model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.743a	0.552	0.511	0.44076

a Predictors: (Constant), Withholding VAT Rates, Withholding VAT Reforms, Withholding VAT Administration

Source: Research Data (2021)

The model summary results showed that withholding value added tax components explained 55% (R squared=0.552) of total changes in tax revenue. This suggested that the model applied to link the variables was satisfactory. However, the remaining 45% could be attributed to other factors not included in the study model.

Table 4.12: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	7.896	3	2.632	13.549	.000b
	Residual	6.411	33	0.194		
	Total	14.307	36			

a Dependent Variable: VAT Revenue

b Predictors: (Constant), Withholding VAT Rates, Withholding VAT Reforms, Withholding VAT Administration

Source: Research Data (2021)

The ANOVA results indicate that the overall model was statistically significant as supported by a p value of $0.000 < 0.05$. This was further supported by an F statistic of 13.549 implying that withholding VAT components are a good predictor of VAT revenue.

Table 4.13: Coefficients

Mode 1		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	-0.54	0.753		-0.717	0.478
	Withholding VAT Administration	0.441	0.166	0.347	2.656	0.012
	Withholding VAT Reforms	0.287	0.13	0.284	2.21	0.034
	Withholding VAT Rates	0.16	0.063	0.34	2.526	0.017

a Dependent Variable: VAT Revenue

Source: Research Data (2021)

Coefficients (Table 4.13) results showed that withholding VAT administration had a positive and significant effect on VAT revenue ($\beta=0.347$, $p=0.012<.05$). This suggested that an increase in withholding VAT administration by one unit will result to increase in VAT revenue by 0.347 units.

The findings also indicated that withholding VAT reforms had a positive and significant effect on VAT revenue ($\beta=0.284$, $p=0.034<.05$). This suggested that an increase in withholding VAT reforms by one unit will result to an increase in VAT revenue by 0.284 units.

Further, results showed that withholding VAT rates had a positive and significant effect on VAT revenue ($\beta=0.34$, $p=0.017<.05$). This suggested that an increase in withholding VAT rates by one unit will result to an increase in VAT revenue by 0.34units.

The estimated model was as follows:

$$Y = 0.347X_1 + 0.284X_2 + 0.34X_3$$

Where;

$Y = \text{VAT Revenue}$

$X_1 = \text{Withholding VAT Administration}$

$X_2 = \text{Withholding VAT Reform}$

$X_3 = \text{Withholding VAT Rates}$

4.9 Hypothesis Testing

Hypothesis testing was based on coefficients results in Table 4.13. The criterion was to reject the null hypothesis if the p value $< .05$. The first hypothesis predicted that there was no significant effect of VAT withholding administration on VAT revenue collection in Kenya. The p value of $0.012 < .05$ meant that the null hypothesis was rejected. This implied that there was a significant effect of VAT withholding administration on VAT revenue collection in Kenya.

The second hypothesis predicted that there was no significant effect of VAT withholding reforms on VAT revenue collection in Kenya. The p value of $0.034 < .05$ meant that the null hypothesis was rejected. This implied that there was a significant effect of VAT withholding reforms on VAT revenue collection in Kenya.

The third hypothesis predicted that there was no significant effect of VAT withholding rates on VAT revenue collection in Kenya. The p value of $0.017 < .05$ meant that the null hypothesis was rejected. This implied that there was a significant effect of VAT withholding rates on VAT revenue collection in Kenya.

Table 4.14: Summary of hypothesis Testing

		P-Values	Decision
H₀₁	There is no significant effect of VAT withholding administration on VAT revenue collection in Kenya.	0.012<0.05	Reject
H₀₂	There is no significant effect of VAT withholding reform on VAT revenue collection in Kenya.	0.034<0.05	Reject
H₀₃	There is no significant effect of VAT withholding rates on VAT revenue collection in Kenya.	0.017<0.05	Reject

4.10 Discussion of the key Findings

4.10.1 VAT withholding administration and VAT Revenue

The first objective of the study was to determine the effect of VAT withholding administration on VAT revenue collection in Kenya. The correlation results revealed that withholding VAT administration had a positive and statistically significant association with VAT revenue ($r = 0.578$, $p = .000$). The regression results showed that withholding VAT administration had a positive and significant effect on VAT revenue ($\beta=0.347$, $p=.012<.05$). The study further implies that with enhanced policies on Withholding VAT administration especially Itax system and KRA compliance audit, there will be an increase in monthly VAT revenue collected by KRA. This resonates with those of Majoni (2021) who established that there was a positive significant relationship between implementing VAT withholding tax and VAT revenue. Inoti (2008) found that the administration of VAT, by VAT agents was cost effective, which boosted revenue collection.

4.10.2 VAT withholding reforms and VAT Revenue

The second objective of the study was to establish the effect of VAT withholding reform on VAT revenue collection in Kenya. The correlation results revealed that withholding VAT reforms had a positive and statistically significant association with VAT revenue ($r = 0.525$, $p = .000$). The regression results indicated that withholding VAT reforms had a positive and significant effect on VAT revenue ($\beta=0.284$, $p=.034<.05$). The study further implies that with enhanced Withholding VAT reforms especially on increasing the number of VAT tax agents and strengthening of the VAT audit skills, there will be an increase in monthly VAT revenue collected by KRA. The study findings were consistent with those of Mokuu (2012) who observed that tax reforms had significantly influenced tax revenue. Similarly, Muriithi and Moyi (2013) concluded that tax reforms had a positive impact on the overall tax structure.

4.10.3 VAT withholding rates and VAT Revenue

The third objective of the study was to assess the effect of VAT withholding rates on VAT revenue collection in Kenya. The correlation results indicated that withholding VAT rates had a positive and statistically significant association with VAT revenue ($r = 0.595$, $p = .000$). The regression results revealed that withholding VAT rates had a positive and significant effect on VAT revenue ($\beta=0.34$, $p=0.017<.05$). The study further indicates that the reduction of withholding VAT rates and the Zero rating of goods and services, creates a negative effect on the monthly VAT revenue collected by KRA. The study findings corroborate with those of Asirigwa (2011) who found that multiple rates, higher range between highest and lowest non-zero VAT rates, and the longer the VAT has been in operation (age of the VAT) are associated with higher revenues. According to Alavuotunki, Haapanen and Pirttilä (2019), tax revenue increased with introduction of VAT.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents the summary of key findings, conclusions and recommendations based on the research findings. The study adopted explanatory research design. The study population of the study was 65 employees at KRA in Nairobi County. All the employees participated in the study; hence it was a census. Primary data was collected using a structured questionnaire. The study applied quantitative methods to analyse data.

5.2 Summary of Key Findings

5.2.1 VAT withholding administration

The study established that most of the respondents agreed to a very great extent that KRA preparation (Itax system) affects VAT revenue collection, KRA Self-assessment affects VAT revenue collection, KRA Compliance audit affects VAT revenue collection and KRA investigations audit affect VAT revenue collection. Further, the study findings indicated that withholding VAT administration had a positive and significant effect on VAT revenue in Kenya. The study findings concurred with those of Majoni (2021) who established that there was a positive significant relationship between implementing VAT withholding tax and VAT revenue. Inoti (2008) found that the administration of VAT, by VAT agents was cost effective, which boosted revenue collection.

5.2.2 VAT withholding reforms

The study established that the respondents agreed to a very great extent that reduction of VAT exemptions affects VAT revenue collection, increasing the number of tax

collectors (Agents) affects VAT revenue collection, imposing tougher penalties for those found guilty of evasion affects VAT revenue collection, strengthening audit skills effects VAT revenue collection, and lowering rates affects VAT revenue collection. Further, the study findings indicated that withholding VAT reforms had a positive and significant effect on VAT revenue in Kenya. The study findings were consistent with those of Mokuu (2012) who observed that tax reforms had significantly influenced tax revenue. Similarly, Muriithi and Moyi (2013) concluded that tax reforms had a positive impact on the overall tax structure.

5.2.3 VAT withholding rates

The study established that the respondents agreed to a very great extent that no VAT is withheld on exempt goods and this affects VAT revenue, no VAT is withheld on exempt services and this affects VAT revenue, no VAT is withheld on Zero rated supplies and this affects VAT revenue, and reduction of withholding VAT rate has been reduced from 6% to 2% affected VAT revenue. Further, the study findings indicated that withholding VAT rates had a positive and significant effect on VAT revenue in Kenya. The study findings corroborate with those of Asirigwa (2011) who found that multiple rates, higher range between highest and lowest non-zero VAT rates, and the longer the VAT has been in operation (age of the VAT) are associated with higher revenues. According to Alavuotunki, Haapanen and Pirttilä (2019), tax revenue increased with introduction of VAT.

5.3 Conclusions

The study concluded that withholding VAT had a significant influence on VAT revenue in Kenya. In particular withholding VAT administration was found to have a positive and significant effect on VAT revenue. The implication was that improvement of withholding VAT administration was likely to enhance VAT revenue in Kenya.

Further, withholding VAT reforms had a positive and significant effect on VAT revenue. The implication was that improvement of withholding VAT reforms would enhance VAT revenue in Kenya. In addition, withholding VAT rates had a positive and significant effect on VAT revenue. The implication was that improvement of withholding VAT rates would enhance VAT revenue in Kenya.

5.4 Recommendations

Based on the findings of this study, the following are recommendations emanating from this study:

5.4.1 Policy recommendations

The government through the necessary agencies such as KRA and Treasury ministry should reinforce policies relating to withholding VAT Administration. The government should particularly, focus on Itax system, monitoring & evaluation, and VAT compliance audit.

Similarly, the government through the necessary agencies such as KRA and Treasury ministry should strengthen withholding VAT policies and reforms. The particular focus should be on VAT Exemptions, number of tax collectors (Agents), penalties for those found guilty of evasion and VAT audit skills.

5.4.2 Management and Practice

The study further established that withholding VAT rates had a positive and significant effect on VAT revenue in Kenya. Therefore, the government through the necessary agencies such as KRA and treasury ministry should moderate withholding VAT rates. The specific focus should be on zero rated and exemptions supplies of goods and services.

5.4.3 Implications to the theory and academics

This study adds on the existing empirical studies on the extent to which VAT withholding administration, VAT withholding reforms and VAT withholding rates influence on VAT revenue. This study contributes to academic knowledge in several ways by providing evidence pointing towards significant application of VAT withholding administration, VAT withholding reforms and VAT withholding rates in improving Value Added Tax revenue in Kenya. This study confirmed various theoretical contributions and advances support for the relationships hypothesized. The results strengthen literature by confirming the postulations of the Equal sacrifice theory and Economic deterrence theory.

5.5 Suggestion for Further Research

The study established the effect of withholding VAT on VAT revenue in Kenya. Future studies could consider inclusion of intervening variables such as inflation, VAT refunds and GDP. Further, this study variables (Withholding VAT administration, withholding VAT reforms, and withholding VAT rates) explained 55 percent of total variations in VAT revenue. Scholars could consider other factors that can be used to explain the remaining 45 percent that have an effect on the VAT revenue in Kenya. For instance, a study on the effect Withholding VAT system on the VAT refund /Credit.

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APPENDICES

Appendix I: Introduction Letter

Dear (Respondent)

RE: 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 Withholding Value Added Tax on the Value Added Tax Revenue in Kenya.*" Kindly respond to the questions in the attached questionnaire. The information provided will exclusively be used for academic purposes and will be treated with utmost confidentiality.

Your cooperation will be highly appreciated.

Yours Faithfully,

ROBERT MABEYA

Appendix II: Questionnaire

Kindly answer the following questions as honestly as possible. The information given will be treated with utmost confidentiality. Please do not write your name anywhere on this questionnaire. You are encouraged to give your honest opinion.

Instructions: Please tick [] or fill in the appropriate information on the spaces provided.

SECTION A: PERSONAL INFORMATION

1. What is your gender?

a) Male

b) Female

2. What is your age bracket?

Below 25 years 26-35 years

36-45 years 46-55 years

Above 55 years

3. What is your highest academic qualification Level?

Primary Secondary Diploma Undergraduate Postgraduate

4. How long have you worked with the institution?

Below 5 years 6-10 years above 10 Years

SECTION B: WITHHOLDING VAT ADMINISTRATION

Please rate the extent to which you agree with the following statements relating to Withholding VAT Administration. Use the scale: 1-No at all, 2- small extent, 3-moderate extent, 4- great extent, and 5-very great extent.

Statements on Withholding VAT Administration	5	4	3	2	1
KRA preparation (Itax system) affects VAT revenue collection.					
KRA Self-assessment affects VAT revenue collection.					
KRA Compliance audit affects VAT revenue collection.					
KRA Investigations audit affect VAT revenue collection.					

SECTION C: WITHHOLDING VAT REFORMS

Please rate the extent to which you agree with the following statements relating to Withholding VAT Reforms. Use the scale: 1-No at all, 2- small extent, 3-moderate extent, 4- great extent, and 5-very great extent.

Statements on Withholding VAT Reforms	5	4	3	2	1
Reduction of VAT exemptions affects VAT revenue collection.					

Increasing the number of tax collectors (Agents) affects VAT revenue collection					
Imposing tougher penalties for those found guilty of evasion affects VAT revenue collection					
Strengthening audit skills effects VAT revenue collection					
Lowering rates affects VAT revenue collection					

SECTION D: WITHHOLDING VAT RATES

Please rate the extent to which you agree with the following statements relating to Withholding VAT Rates. Use the scale: 1-No at all, 2- small extent, 3-moderate extent, 4- great extent, and 5-very great extent.

Statements on Withholding VAT Rates	5	4	3	2	1
Taxable goods and services exported are subject to double taxation on withholding VAT and this affects VAT revenue					

No VAT is withheld on exempt goods and this affects VAT revenue					
No VAT is withheld on exempt services and this affects VAT revenue					
No VAT is withheld on Zero rated supplies and this affects VAT revenue					
Reduction of withholding VAT rate has been reduced from 6% to 2% affected VAT revenue.					

SECTION E: VAT REVENUE

Please rate the extent to which you agree with the following statements relating to VAT Revenue. Use the scale: 1-No at all, 2- small extent, 3-moderate extent, 4- great extent, and 5-very great extent.

Statements on VAT Revenue	5	4	3	2	1
The amount of VAT revenue collection has increased.					
The amount of VAT revenue collection has declined.					
The amount of VAT revenue collection has stagnated.					
VAT revenue as a percentage of GDP has improved.					

Appendix III: Research Authorisation -KESRA



ISO 9001:2015 CERTIFIED

REF: KESRA/NBI/036

16th August 2021

TO WHOM IT MAY CONCERN

RE: REQUEST FOR RESEARCH PERMIT

STUDENT NAME: Robert Nyabuti Mabeya- REG NO: MU/KESRA/0111/2016,

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

The named student is undertaking Research on TOPIC: **"EFFECT OF WITHHOLDING VALUE ADDED TAX ON THE VALUE ADDED TAX REVENUE IN KENYA."**

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

Your support to KESRA in this regard will be highly appreciated.

Thank you.

Dr. Marion Nekesa PHD,
Head Academic Research
KESRA



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Tulipe Ushuru, Tujitogameef




Appendix IV: Research License- NACOSTI



 REPUBLIC OF KENYA
 National Commission for Science, Technology and Innovation
 Ref No: **260458**



NATIONAL COMMISSION FOR SCIENCE, TECHNOLOGY & INNOVATION
 Date of Issue: **23/August/2021**

RESEARCH LICENSE



This is to Certify that Mr. ROBERT NYABUTI MABEYA of Moi University, has been licensed to conduct research in Nairobi on the topic: EFFECT OF WITHHOLDING VALUE ADDED TAX ON THE VALUE ADDED TAX REVENUE IN KENYA for the period ending : 23/August/2022.

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