

# Factors Affecting Tax Compliance on Small Medium Sized Enterprises in Koodboor District in Hargeisa Somaliland

Mahad Abdikadir Muhumed<sup>1</sup>, Dr. Nathan Wamalwa Wafula<sup>2</sup>

<sup>1</sup>Corresponding Author: <sup>2</sup>Lecturer; Accounting and Finance Department, School of Postgraduate Studies and Research, Amoud University Somaliland.

DOI: <https://doi.org/10.5281/zenodo.8126170>

Published Date: 08-July-2023

---

**Abstract:** Taxes are an important source of revenue for the state and all government agencies. It helps the state meet its financial obligations and also serves the general public by providing services such as health, infrastructure, and education, as well as stability and order. This study sought to determine the factors affecting tax compliance on SMEs in Kood Boor District Hargeisa, Somaliland. The specific objectives of the study were; to establish the effects of taxpayer knowledge, tax rate, tax fines and penalty and tax accountability on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland. The study adopted descriptive research design. A sample of 127 SMEs was drawn using simple random sampling. The target populations of the study were the 190 registered in Ministry of Trade, Industry and Tourism. Primary data was collected using questionnaires. Data was analyzed using binary logistic regression model to determine the association that existed between the independents and dependent variable. The study was guided by following theories; economic based theory, institutional anomie theory and resource based theory. The study findings indicates that tax payers knowledge was statistically insignificant (Exp (B) = 2.014, p=.254) at 5 percent level of significance. This implies that the odds ratio for tax payer's knowledge indicates that every unit increase in tax payer's knowledge is associated with an increase in the odds of tax compliance in SMEs in Kood Boor District Hargeisa, Somaliland as per the sample. The study further showed that tax rate was statistically significant (Exp (B) = 0.135, p=0.002) at 5%. The study findings also examined tax fines and penalties and found that is statistically insignificant (Exp (B) = 0.447, p=0.121) at 5%. Finally, the study established that tax accountability was statistically significant (Exp (B) = 0.206, p= 0.023) at 5%. The odds ratio for tax rate, tax fines and penalty and tax accountability indicates that every unit increase in tax rate, tax fines and penalty and tax accountability respectively is associated with decrease in the odds of tax compliance of SMEs in Kood Boor District Hargeisa Somaliland as per the sample. The study recommends that on tax rates, the government should come up with better reforms on tax rates to cushion the tax payer from heavy burden. Also by reducing the taxes rates this will increase the purchase power of the citizens which in turn leads to better living standards and thus tax compliance. On accountability, the study recommended that there should be more public dialogue on taxation policy and practices. The study further recommend that to strength the taxation policy and practices in Somaliland then the community actors, such as clan elders, business owners and religious leaders, should be involved in the formulation and the implementation of tax policy. Furthermore the study recommends that the Auditor General should ensure and enforce on policies that advocates for both private and public entities to publish their audited annual financial reports.

**Keywords:** Tax Knowledge, Tax Rate, Tax Fines and Penalty, Tax Accountability, Tax Compliance, Logistic Regression Model, SMEs.

---

## 1. INTRODUCTION

### 1.1 Background of the Study

In Somaliland, the tax was first introduced by the British Protection Service, but Somaliland resisted, considering the tax to be an unfair imposition. The tax system has changed a lot since then, but at the same time, most of the legislation is a legacy of the time when Siad Barre ruled Somalia, including Somaliland, from his 1969 until his early 1969. Not so much has

changed as economic reality. Somaliland currently lacks a coherent formal tax policy and Somaliland's customs and tax collection system is a patchwork quilt lacking proper legal and institutional support. The tax base is low due to the large informal economic sector, low economic growth and the fact that the largest companies do not pay taxes on their profits (Marti, 2010). In recent years, the tax collection landscape has changed from an informal system to a more professional and automated system of tax collection. Part of this reform is a decentralization process in which powers and duties are transferred from the central government to local governments. Systems and structures have been professionalized over the past decade, but the transformation is not yet complete. As a result, implementation remains problematic and tax revenue remains low. The state, on the other hand, does not have enough revenue streams to provide the services it needs. Poor business results reduce taxpayers' willingness to pay, and many taxpayers attempt to evade taxes while avoiding consequences such as business closures and, as is common in some cities, removal of front doors. Some taxpayers only pay tax on as an illustration, some people point out that they pay the road tax because they don't want to be bothered while driving on the road. At the same time, they point out, they cannot believe the money is getting where it should be because the roads are getting old while paying taxes. The key factor here is the taxpayer's ability to avoid paying taxes. For example, the taxes they pay do not reflect their true size or revenues, as they have the resources, networks and lobbying skills necessary for full tax exemption (Hassan & Tellander, 2016).

Taxes are an important source of revenue for the state and all government agencies. It helps the state meet its financial obligations and also serves the general public by providing services such as health, infrastructure, and education, as well as stability and order. Tax compliance is the ability and willingness of taxpayers to comply with relevant tax laws and regulations (Ayuba, Saad & Ariffin, 2016). Saipai and Kasipillai (2013) define it as accurately reporting income and claiming expenses in accordance with established tax laws. William and Round (2009) measured tax compliance based on timely and accurate filings. Kirchner (2014) viewed tax compliance as filling on time and correct filling. The issue of tax compliance is as old as taxes themselves. Tax violations and tax evasion are widely believed to occur in every country (Palil, 2011). Both developed and developing countries face significant challenges for tax authorities to collect taxpayers' legitimate revenues as efficiently and effectively as possible (Loo, Evans & McKerchar, 2010). This study employed accurate filing as measure of tax compliance as eluded by (William & Round, 2009).

Small businesses may unknowingly or intentionally fail to comply with tax laws. Emerging markets need to ensure that their tax regimes for small businesses are efficient, effective, and not negatively impact small businesses. The challenge facing most government agencies is inadequate taxation and inadequate tax policies. A major goal of tax policy is compliance with tax laws (James & Alley, 2004). Small and medium enterprises in Somaliland operate in the informal sector. According to the 2016 Economic Research Report, there is a small but semi-organized and unregulated activity in the sector. Understanding and interpreting tax laws determines a small business' ability and willingness to comply with tax laws. According to the Treasury, Somaliland's budget is growing rapidly and it needs more tax revenue to finance it. The National Economic Survey found that SMEs accounted for 33% of total GDP (Somaliland Small Business Finance Survey, 2018). The Somaliland Revenue Authority (SLRA) had a revenue target of US\$500 million for fiscal year 2018/19. Treasury targets showed 16.4% growth in revenue for fiscal year 2018/19 (SLRA Revenue Performance Report, 2019).

According to the SLRA's performance review and outlook for fiscal year 2019/2020, the Revenue Service failed to meet the revenue target set by the Treasury for fiscal year 2018/2019 despite a 9.6% increase in revenue. He raised \$405 million against SRA's \$500 million target his SLRA performance review for the year ended March 2019. According to the SLRA's 7th Business Plan, the SLRA collected 95% of state revenues in 2017/2018. This underscores the need for governments and tax authorities to reassess their efforts to encourage taxpayer compliance to meet revenue targets. However, according to the Public Budget Office (2019), the small business sector, which accounts for the majority of the country's GDP, is still tax deficient. The 2018/2019 total revenue target of \$500 million was only about 19% of the target in sales tax (TOT) million. Despite productivity, tax compliance in this area is low. The informal nature of the industry makes it more difficult for governments to enforce tax policies and ensure compliance. Successful taxation in this industry therefore depends on voluntary compliance. Therefore, this study aimed to explore the factors affecting SME tax compliance, focusing on small-scale traders in the Koodboord District in Somaliland.

Factors affecting tax compliance include, but are not limited to, the cost of tax compliance. This can be due to high tax rates, including costs of dealing with regulators, tax equity, and internal costs incurred in conducting tax activities. Tax evasion includes, but is not limited to, tax avoidance, benefits, ethical compliance, perceptions of institutional fairness, and adverse social consequences (Machira & Irura, 2012). Tax awareness and knowledge of tax law can be judged by the level of education, seminars and conferences attended. Another factor is the slow acceptance of online applications (technology). This may be due to knowledge of computer filing, costs associated with filing, registration as an online applicant, and

internet connectivity (Loureiro, 2014). There are several aspects to the factors that affect tax compliance. Feld and Frey (2007) measured the following factors influencing tax compliance; tax awareness and tax education, compliance costs, fines and penalty. Tambunan (2014) conceptualized the factors as tax knowledge, tax rate and tax liability. This study conceptualized the factors as tax knowledge, tax rates, tax fines and penalties and tax accountability.

Somaliland's do adhere to an informal patchwork of duty and tax collection. The duty and tax provide a large portion of the income enjoyed by Somaliland government. There are mainly two types of business taxes in Somaliland. The two are duty levied on all import and export goods at the ports and income tax charged on business sales at a rate of 5%. For instance, the duties levied at the port of Berbera generate an estimated 85% of government revenue. The latter is very similar to sale tax which is levied on sale turnover of the business at rate of 5%. Consumers also pay 5% on consumption of goods and services, which is equivalent to Value Added Tax (VAT), paid by the sellers instead of the buyers (consumers) who are the collecting agents for the government. Employees pay tax on their salaries commonly known as the payroll tax which is equivalent personal income tax (PAYE- pay as you earn) at rate of 6%. The businesses pay property tax at rate of 8% of their total property investment. Ministry of Finance collected the taxes. There are some problems facing tax compliance in Somaliland due to the cumbersome and complex tax system and codes which are not understood by the tax payers. However as developing countries there are limited research and scholarly studies about SMEs sector in Somaliland. Hence this study sought to determine the factors that affect tax compliance of SMEs in Somaliland in Kood Boor District Hargeisa Somaliland.

## **1.2 Statement of the Problem**

SMEs pay taxes and therefore play an important role in the national tax system. Although the evidence is inconclusive, we believe most studies indicate that traders who are small business owners are more likely than other taxpayer groups to commit fraud and non-compliance (Chebusit *et al.*, 2014). Small business owners have been classified as a high-risk group for tax compliance by the Organization for Economic Co-operation and Development. However, in many cases it is impossible to prove non-compliance (Nahida, Coop, Freudenberg & Sarker, 2014). Taxes play an important role in the growth of any economy. Tax compliance is therefore beneficial to the economy, as lack of tax compliance makes it difficult to collect government revenues, and government spending inefficiencies due to lower domestic revenue and mobilization power of the government (Loureiro, 2014).

In 2018, for example, the amount lost from tax revenue was about double what the country spent on health and education, according to the Somaliland Revenue Authority. He believes poor tax compliance is also discouraging domestic and foreign investors and hindering the country's ability to grow. In Somaliland, there is a hostile relationship between taxpayers and tax collectors over tax compliance. Most SMEs do not pay taxes and the lack of tax compliance among SMEs remains acute, with a tax gap of approximately 35% and 33% in 2018 and 2019 respectively (SLRA, 2020). The first quarter of 2023, the Government of Somaliland collected 541 billion SLSh in domestic revenue representing a 4% decrease from the 562 billion SLSh collected in the same period in 2022 (Ministry of Finance Development, 2023). For this reason, researchers wanted to explore the factors affecting tax compliance of SMEs in Kood Boor District. It is also useful to note that most of Somaliland's SMEs are based in this District, although extensive research has been done in this area. In this context, there was need to understand the effect of tax compliance so that local governments can improve tax collection for SMEs in Kood Boor District Hargeisa Somaliland.

## **1.3 Research Objectives**

### **1.3.1 General objective**

The study main objective was to determine the factors that affect tax compliance of SMEs in Somaliland in Kood Boor District Hargeisa Somaliland.

### **1.3.2 Specific Objectives**

1. To establish the effect of taxpayer knowledge on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.
2. To determine the effect of tax rate on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.
3. To examine the effect of fines and penalties on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.
4. To establish the effect of tax accountability on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.

#### **1.4 Research Hypothesis**

- (i) Tax knowledge has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland
- (ii) Tax rate has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.
- (iii) Tax fines and penalty has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.
- (iv) Tax accountability has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.

### **2. EMPIRICAL REVIEW**

This section discusses the relevant empirical literature that supports the research problem. This ensures that the study's content is informed by past studies that are related to it.

#### **2.1 Tax Payers Knowledge and Tax Compliance**

A study conducted by Normala (2007) to examine the influence of tax education, as a proactive approach to enhance the voluntary tax compliance, among the taxpayers, in Malaysia. Using questionnaires administered to the taxpayers and the tax officials. The 9 respondents confirm the increase in the tax knowledge increase the level of voluntary tax compliance. The statistical findings confirm that there is a significant relationship between the level of tax education and voluntary tax compliance.

Rasshid and Noor (2004) sought to evaluate the influence of tax knowledge on the tax compliance behavior among the taxpayers in Malaysia. The objective of the study was to investigate the effect of the presence of tax knowledge and understanding, on the level of tax compliance behavior. Analyzing the data collected using questionnaires to compare the compliance behavior of taxpayers with significant level of tax knowledge with those without tax knowledge. Statistical findings confirmed that those with tax knowledge had higher level of compliance than those without, which indicated a significant relationship between the level of tax knowledge and the level of tax compliance.

Study by Cyrilje (2015) to investigate the effects of tax literacy as an instrument of combating and overcoming tax system complexity, low tax morale and tax non-compliance in Croatia concluded that tax literacy in the financial dimensions possesses specific tax oriented financial knowledge on accounting and numeracy skills required for managing tax calculations. Tax literacy was intended to help individuals receive information about taxes, to explain those taxes within a domestic system as well as regional and international system. The aim of this paper was to stress out that the complexity of the taxation system as well as some other problems like those that low tax morale and low tax compliance might be combated through promotion and implementation of tax literacy initiatives and programs. By acquiring basic knowledge of taxation and public expenditures, individuals become able to efficiently manage their personal finances and understand the basic logic of possible effects of fiscal policy. On the other side, if individuals are not taught the basic concepts of taxation, and never acquire needed numeracy skills, they might be more prone to problems like indebtedness or noncompliance of their tax obligations.

Findings of a research done by Mukhlis *et al.* (2013) show that tax knowledge is strongly influenced by the education level of the taxpayers. Their research concluded that basically the SME sector businesses can understand their tax obligations when there is the aspect of justice and tax benefit can be received in real terms by businesses in the SME sector in East Java. A similar research done by Mukasa (2011) gave the result that the tax knowledge and perceived 10 fairness taxes have a causal relationship with tax compliance. Therefore, it is important to analyze the role of education as far as the role of the tax, the tax knowledge and a sense of justice taxpayer to tax compliance businesses, especially SMEs crafts field in East Java.

#### **2.2 Tax Rates and Tax Compliance**

The tax rate is an important factor in determining tax compliance behavior, although the exact impact is still unclear and debatable (Kirchler, 2007). Furthermore, raising marginal tax rates will likely encourage taxpayers to evade tax further (Ali, Cecil, & Knoblett, 2001; Torgler, 2007), whereas lowering the tax rates does not necessarily increase tax compliance (Kirchler, 2007). In line with Kirchler (2007), Inasius (2015) also indicates that the perception of the tax rate has no significant impact on tax compliance. Although the impact of tax rates is debatable, Kirchler *et al.*, (2008) and Mc Kerchar and Evans (2009) suggest that the degree of trust between taxpayers and the government has a major role in ascertaining the impact of tax rates on compliance. When trust is low, taxpayers perceive a high tax rate as unfair and when trust is high, taxpayers might consider the same level of tax rate as contributing to the community (Kirchler *et al.*, 2008).

A study by Mas'ud *et al.* (2014) examined the correlation as well as the effect of tax rate on tax compliance in Africa using cross-country data. The findings showed that there is significant negative correlation between tax rate and tax compliance. In South Africa, studies conducted by economy watch dog on tax burdens on SMEs revealed that tax requirements procedures acted as stumbling blocks to tax compliance. A majority of SMEs experience their tax liability as an increasing burden since they lack enough skilled staff to handle tax compliance issues and are therefore, forced to incur "extra" tax costs. Most SMEs do not even recognize the tax incentives and services available to them. The study also noted that changes in tax policies sometimes result in an even more complex tax system. A clear finding was that elaborate tax incentive schemes which require sophisticated systems and skilled staff would often result in increasing compliance costs rather than provide real tax relief. As a result, small businesses (and probably other taxpayers as well) would prefer simple cuts in tax rates and penalties.

A study was conducted by Helhel and Ahmed (2014) in Sana'a, the capital city of Yemen to evaluate and rank the factors that reduce taxpayer compliance. The results indicated that, high tax rates and unfair tax system are the two most crucial factors associated with low compliance. Furthermore, insufficient tax auditing, little deterrent effects of tax penalties and tax amnesties enacted frequently have impact on taxpayers' compliance decision.

A study conducted by Atawodi and Ojeka (2012) in North-Central Nigeria to evaluate the factors that affect tax compliance of SMEs found that most SMEs attributed their noncompliance to high tax rates and complex filing procedures. They recommended that Small and Medium Enterprises should be levied lower amounts of taxes so that they will have enough 14 funds for other activities that will lead to business growth. Furthermore, they opined that it would help SMEs get better equipped to survive in a competitive market.

### **2.3 Tax Fines and Penalties and Tax Compliance**

A research done by Nyamwanza, *et.al.* (2014) shows that penalties have been found to be the most effective in enforcing compliance in Zimbabwe. SMEs are struggling to meet their (The Zimbabwe Revenue Authority) ZIMRA obligations, which are made worse by the heavy penalties charged by the authorities. Authorities take a number of measures in enforcing compliance such as garnishing orders, closure of business premises, confiscation, and penalties. These measures were rated by research respondents in terms of their effectiveness as follows: penalties (42%), closure of businesses (29%), garnishing orders (12%), and confiscation (12%).

A study conducted in Bomet town concluded that a simple tax regime had the greatest effect. Online tax filing came second, and tax payers' education and training was third while stringent tax penalties had the least effect on the SMEs turn over tax compliance (Kirui *et al.*, 2017). The study also found that all the SMEs and their employees had been adequately trained by KRA staff on how to file tax returns and also understood well the dangers/penalties of failure to make returns on or before the maturity date.

Research done by Chebusit *et al.* (2014) on factors affecting tax compliance among SMEs in Trans Nzoia concluded that there was a positive effect of fines and penalties on compliance cost and tax compliance. This indicated that an increase in fines and penalty the tax compliance improves. The observed effects were weaker than expected and some studies even suggest that an increase of penalties can have undesirable effect and result in more tax avoidance (Kirchler *et al.*, 2007). On one hand, fines should be high enough to decrease the expected value of tax evasion and to assure its deterrent effect on tax payers. The study found a strong support for the argument that fines and penalties impacts highly on tax compliance, thus they recommended employment of moderate levels of fines and taxes. This way, SMEs will be encouraged to comply since they will keep accurate records for taxation purposes in order to avoid fines and penalties.

### **2.4 Tax Accountability and Tax Compliance**

Adebayo (2017) conducted a study on the effect of accountability and transparency on tax returns in Nigeria. The objective of this paper is to ascertain how transparency and accountability can propel tax returns in Nigeria. The methodology adopted was time series data and our analysis was predicated on Views where the author ran a regression model that established the good fitness of the model. The model used is an auto regressive model. Stewardship theory was used for this study. Tax accountability and transparency with greater emphasis on the various kinds of taxes such as Personal Income Tax, Companies Income Tax, Petroleum profit Tax, Duties and value Added Tax is perceived to have a direct correlation with the Gross Domestic Product (GDP). It is believed that if potent mechanism is put in place more tax returns might be



generated and where the government reciprocates this by way of qualitative governance appreciable compliance might ensue at the end of the day. The recommendation is a signal to government on the need to judiciously utilize tax proceeds to the betterment of the citizens notwithstanding the fact that even where they choose otherwise the payment of taxes remains sacred. It is therefore incumbent on Nigerian government to mimic this idea so that the citizens would be willing and enthusiastic paying the tax.

Kiow, Salleh and Kassim (2017) conducted a study on the determinants of individual taxpayers' tax Compliance behavior in Peninsular Malaysia. The findings from this review suggested that 22 tax compliance behaviors of individual taxpayers is influenced by ethical perception of individual taxpayers and their ethical perception is affected by public governance and transparency in government operations. Ethical perception plays an important role for individual taxpayers to report their income correctly. Ethical perception varies from an individual to another, which influenced by changes in their surroundings and their experiences when interact with government. Perceptions of how taxpayers' money is being utilized, benefits they derived from government or others evade to pay tax are considered as possible factors influencing their compliance behavior. Taxpayers will be more compliance if government use tax monies wisely or when taxpayers get benefits for the taxes paid in terms of public goods and social amenities that they prefer. Transparent surroundings will enhance taxpayers' confidence in public bodies. Taxpayers are concerned on transparency in public procurement as lack of transparency may cause corruption and reduces public sector efficiency. In contrast, scholars argued that greater degree of transparency could lead to less trust as it will be easier for taxpayers to audit government and they might blame government for small mistakes.

According to Adeyeye and Otusanya (2015) examined the impact of taxpayers' perception of government's accountability, transparency and reduction in fiscal corruption on voluntary tax compliance. The study obtained data through questionnaire from a sample size of 1,700 selected randomly out of the population of 11,900 tradesmen and artisans belonging to 17 trade associations in Lagos State, Nigeria. Findings of the study indicate that each of the individual independent variables has significant positive relationship with the dependent variable. The study also suggests that the combined effect of government's accountability, transparency and reduction in fiscal corruption appears to have greater impact on voluntary tax compliance. The paper argues that for most taxable adults to be tax compliant in Nigeria, government must be perceived and seen to be accountable to the citizens, be transparent in its style of governance and be perceived and seen to take necessary steps in reducing the level of corruption in Nigeria.

### 3. RESEARCH METHODOLOGY

#### 3.1 Model Specification

A logistic regression model was applied to determine the effect of factors affecting tax compliance in SMEs in Kood Boor District Hargeisa, Somaliland. The method of estimation of the coefficients ( $i = 1, 2, \dots, k$ ) is the maximum likelihood estimation (MLE). Data are entered into the analysis as 0 or 1 for the binary outcome, continuous values for continuous predictors, and dummy coding 0 or 1 for categorical (discrete) predictors (Peng, Lee, & Ingersoll, 2002). The Logistic regression model for the study is as follows:

$$\ln(p/1 - p) = \beta_0 + \beta_1 TPK_i + \beta_2 TR_i + \beta_3 FP_i + \beta_4 TA_i + e_i$$

Where:

$P_i$  = Prob ( $P=1 | X$ ) = Probability to Tax Compliance

$\beta_0$  = Constant or intercept

$\beta_1, \beta_2, \beta_3, \beta_4$  = Coefficient

$e_i$  = Disturbance term

$TPK$  = Tax payers knowledge

$TR$  = Tax Rate

$TFP$  = Tax fines and penalty

$TA$  = Tax accountability

**Table 3.1: Qualitative Measurement of Variables.**

Category	Variable Name	Indicators	Measurement Tool
Independent Variable	Tax Payers Knowledge	<ul style="list-style-type: none"> <li>● Knowledge on taxation laws</li> <li>● Information on tax laws complexity</li> </ul>	5 point likert scale, and a composite of 8 items.
Independent Variable	Tax Rate	<ul style="list-style-type: none"> <li>● High tax rates</li> <li>● Stiff fines</li> <li>● Extra cost of engaging a qualified accountant</li> </ul>	5 point likert scale, and a composite of 8 items.
Independent Variable	Tax fines and penalties	<ul style="list-style-type: none"> <li>● Penalty rate</li> <li>● Fear tax audit</li> <li>● Tax norms</li> </ul>	5 point likert scale, and a composite of 8 items.
Independent Variable	Tax Accountability	<ul style="list-style-type: none"> <li>● Public reporting</li> <li>● Impact reporting</li> <li>● Transparency</li> </ul>	5 point likert scale, and a composite of 8 items.
Dependent Variable	Tax Compliance	<ul style="list-style-type: none"> <li>● Accurate filling</li> </ul>	Binary Response

Source: Literature Review, 2023

## 4. RESULTS AND DISCUSSIONS

### 4.1 Correlations Analysis

**Table 4.1 Correlation analysis of Independent and dependent variable**

			Tax Compliance	Tax payers knowledge	Tax rate	Tax fines and penalties	Tax Accountability
Spearman's rho	Tax Compliance	Correlation Coefficient	1.000				
	Tax payers knowledge	Correlation Coefficient	.117	1.000			
	Tax rate	Correlation Coefficient	-.266**	-.076	1.000		
	Tax fines and penalties	Correlation Coefficient	-.172*	.033	-.046	1.000	
	TA Tax Accountability	Correlation Coefficient	-.227**	.083	-.039	.187*	1.000
**. Correlation is significant at the 0.01 level (1-tailed).							
*. Correlation is significant at the 0.05 level (1-tailed).							

Source; Researcher, 2023

As tabulated in table 4.1 the correlation analysis. The findings shows that taxpayer knowledge and tax compliance have a positive relationship at ( $r=.117$ ). The finding further shows that tax rates and tax compliance have a positive relationship of ( $r=.266$ ) while filling procedure had a negatively relationship of ( $r=-.172$ ) and accountability had a positive relationship with tax compliance ( $r=.227$ ). A positive coefficient means that a one unit increase in the independent variable increases tax compliance in the same direction and to the same extent. On the other hand, negative coefficients leads to lower tax compliance in the same direction and to the same extent.

### 4.2 Inferential Analysis

#### 4.2.1 Binary Logistic Regression Analysis

Binary logistic analysis of factors affecting tax compliance was undertaken. Binary Logistic analysis generates parameters used to measure the efficiency of the model in measuring the relationship between variables. An intercept only model, called Block O is the first run to establish if the predictors contributions to the analysis (Menard, 2002). Omnibus Test was used for model comparison between the intercept only and the full model.

#### 4.2.2 Baseline Model

A logistic model provides better fit to the data if it demonstrates improvement over the baseline also called the null model or Intercept Only Model. A baseline model is run without the predictors or dependent variables to gauge if the full model's predictive capacity demonstrates an improvement over the baseline model. The null model's predictions are purely base on the data sets that occur most in the variables.

The baseline model is presented in Table 4.2. The model contains only one variable in the equation which is basically a constant, meaning that the results of the model are the results that could be obtained by the chance or estimation without the dependent variable. The baseline model is the constants only and it is presented in the table 4.2 below.

**4.2.3 Base line model equation**

**Table 4.2**

		B	S.E.	Wald	df	Sig.	Exp(B)
Step 0	Constant	.635	186	11.582	1	.001	1.886

Source: Researcher, 2023

The constant only model shows that the variable is statically significant ( $\beta=.635$ ,  $X^2=11.582$ ,  $p=.001$ ). The score test sets out the variables not in the equation in the baseline equation. The result is presented in the table 4.3 below.

**Table 4.3**

			Score	df	Sig.
Step 0	Variables	Tax payers knowledge	1.193	1	.275
		Tax Rate	10.382	1	.001
		Tax Fines and penalties	3.462	1	.063
		Tax Accountability	6.984	1	.008
	Overall Statistics		20.308	4	.000

Source: Researcher, 2023

The model predicts that at least one of the variables will be significant with a p-value of less than 0.05 in the null model and the overall model was significant. The baseline model is generated for purpose of comparison with the full model to determine any improvement and contribution of the predictors in the model.

The Omnibus Test also explains whether the variance in a given set of data is statistically significantly greater than the overall unexplained variance. The Omnibus Test applies Chi-square test to determine if the model better fits the data compared to the baseline model with intercept only. The results of the Models are presented in the tables below.

**Table 4.4 Omnibus Tests of Model Coefficients**

		Chi-square	df	Sig.
Step 1	Step	22.061	4	.000
	Block	22.061	4	.000
	Model	22.061	4	.000
<i>Source: Researcher, 2023</i>				

The table 4.4 above indicates that the Omnibus test of the model is significant ( $p=.000$ ,  $\text{Chi-square} =22.061$ ). This demonstrates that the full model is an improvement of the baseline model ( $X^2=22.061$ ,  $df=4$ ,  $p=.000$ ).

**4.3 Hosmer and Lemeshow Test**

**Table 4.5**

Step	Chi-square	df	Sig.
1	9.025	8	.340

Source: Researcher, 2023

The Hosmer-Lemeshow test is used to show how well the model fit in other words to test the Goodness of fit. It is considered more reliable than the traditional Chi-square test. The test establishes whether the values are significant or not. A non-significant value indicates that the model is a good fit and vice versa. Table 4.5 Reveals that Homer-Lemeshow test is not significant ( $\chi^2=9.025$ ,  $df=8$ ,  $p=.340$ ) implying that the model is a good fit for the data. Full Model of Binary logistics is in Table 4.6 below.



**Table 4.6 Full Model of Binary logistics**

	B	S.E.	Wald	Sig.	Exp(B)	95% C.I. for EXP(B)	
						Lower	Upper
Tax payers knowledge	.700	.614	1.300	.254	2.014	.605	6.705
Tax Rate	2.004	.650	9.505	.002	.135	.038	.482
Tax fines and Penalties	-.806	.520	2.401	.121	.447	.161	1.238
Tax Accountability	-1.579	.697	5.137	.023	.206	.053	.808
Constant	13.296	4.028	10.899	.001	59.566		

Source: Researcher, 2023

The predictors in the full model were tax payer’s knowledge, tax rate, tax fines and penalty and tax accountability. The results are as shown in Table 4.6 above.

#### 4.4 Test of Hypothesis

##### **H0<sub>1</sub> Tax knowledge has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland**

The first specific objective of the study sought to determine the effect of tax knowledge on tax compliance of SMEs in Kood boor district Hargiesia Somaliland. The outcomes are as presented in Table 4.6. To meet this objective, a null hypothesis that tax knowledge has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland was developed. In Table 4.6, the coefficient of tax payers knowledge (Exp(B) = 2.014, p = 0.254) shows that tax knowledge is statistically insignificant. Therefore, the null hypothesis that tax knowledge has no significant effect on tax compliance amongst SMEs in Kood Boor District Hargeisa Somaliland was not rejected at 5% level of significance. This implies that tax knowledge coefficient is different from zero since the p value is more than 0.05. The odds ratio for tax knowledge indicates that every unit increase in tax knowledge is associated with an increase in the odds of tax compliance in SMEs in Kood Boor District Hargeisa Somaliland as per the sample. These findings are consistent with studies the study that carried out by (Lin and Carrol, 2000). However inconsistent with those of (Rasshid & Noor, 2004) Normala, 2007; Cyslrlje, 2015). The inconsistency in the finding could be due to differences in the economic environment.

##### **H0<sub>2</sub> Tax rate has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.**

The second specific objective of the study sought to determine the effect of tax rate on tax of SMEs in Kood Boor District Hargeisa Somaliland. The outcomes are as presented in Table 4.6. To meet this objective, a null hypothesis that tax rate has no significant effect on tax compliance of SMEs Kood Boor District Hargeisa Somaliland was developed. In Table 4.6, the coefficient of tax rate (Exp(B) = 0.135, p=0.002), shows that tax rate has statistically significant positive effect on tax compliance. Therefore, the null hypothesis that tax rate has no significant effect on tax compliance amongst SMEs in Kood Boor District Hargeisa Somaliland was rejected at 5% level of significance. The odds ratio for tax rate indicates that every unit increase in tax rate is associated with 87% decrease in the odds of tax compliance of SMEs in kood boor district Hargeisa Somaliland as per the sample. These findings are consistent with studies by (Ojeka, 2012; Mas’ud *et al.*, 2014; Inasius, 2015).

##### **H0<sub>3</sub> Tax fines and penalty has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.**

The third specific objective of the study sought to determine the effect of tax fines and penalty on tax complainece of SMEs in Kood boor district Hargiesia Somaliland. The outcomes are as presented in Table 4.6. To meet this objective, a null hypothesis that tax fines and penalty has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland was developed. In Table 4.6, the coefficient of tax fines and penalty (Exp(B) = 0.447, p=0.121) shows that tax fines and penalty has statistically insignificant. Therefore, the null hypothesis that tax fines and penalty has no significant effect on tax compliance amongst SMEs in Kood Boor District Hargeisa Somaliland was not rejected at 5% level of significance. This implies that tax fines and penalty coefficient is not different from zero since the p value is more than 0.05. This implies that the odds ratio for tax fines and penalty indicates that every unit increase in tax fines and penalty is associated with a 55% decrease in the odds of tax compliance in SMEs in Kood Boor District Hargeisa Somaliland as per the sample. This further could imply that the more the citizens are taxed and fined the more they do not comply simply

because they do not have the cash to pay those fines due to lack of enough cash low circulation the system. These findings are inconsistent with studies the study that carried out by (Nyamwanza, *et.al.*, 2014; Chebusit *et al.*, 2014). The inconsistency could be due to differences in the economic and technological differences between the countries whose outcome varies based on the environmental factors to SMEs.

#### **H0<sub>4</sub> Tax accountability has no significant effect on tax compliance of SMEs in Kood Boor District Hargeisa Somaliland.**

The fourth specific objective of the study sought to determine the effect of tax accountability on tax compliance of SMEs in Kood boor district Hargiesia Somaliland. The outcomes are as presented in Table 4.6. To meet this objective, a null hypothesis that tax has no significant effect on tax compliance of SMEs in kood boor district Hargeisa Somaliland was developed. In Table 4.6, the coefficient of tax payers knowledge penalty ( $\text{Exp}(B) = 0.206, p=0.023$ ) shows that tax accountability has statistically significant positive effect on tax compliance. Therefore, the null hypothesis that tax accountability has no significant effect on tax compliance amongst SMEs in Kood Boor District Hargeisa Somaliland was rejected at 5% level of significance. The odds ratio for tax accountability indicates that every unit increase in tax accountability is associated with 79% decrease in the odds of tax compliance in SMEs in Kood Boor District Hargeisa Somaliland as per the sample. These findings are consistent with studies by Maguta (2010), examined the effect Tax Accountability and Transparent on sample 108 SMEs collected through questionnaire. The study found out that the variable has significant relationship of tax accountability, transparent on tax compliance on SMEs.

### **5. CONCLUSIONS AND RECOMMENDATIONS**

The study concluded that tax knowledge and Tax fines and Penalties have an effect on tax compliance though not significant. While tax rate and tax accountability is statistically significant. On tax rates and tax compliance the study recommends that on tax rates, the government should come up with better reforms on tax rate to cushion the tax payer from heavy burden. On accountability and tax compliance the study recommended that there should be more public dialogue on taxation policy and practice. There have been some attempts to disseminate general information about tax and its purpose among the public, through TV and radio information campaigns, from the loud speakers on top of cars, or meetings on tax organized by local governments. However, the state's communication attempts appear to be only one-sided, with no real possibility for taxpayers to provide feedback or receive relevant information on actual spending of the raised revenue. To fill this gap, the Auditor General should unsure and enforce the policies that advocates for all public entities to publish their audited annual financial reports. This will restore trust and hence it will motivate the tax payer to comply with taxes.

The study further recommend that to strength the taxation policy and practices in Somaliland then the community actors, such as clan elders, business owners and religious leaders, should be involved in the formulation and implementation of tax policy.

The study recommends that the government should engage in improving on the public goods like construction of goods roads and repair of old roads. When taxpayers see what the government is doing for them this will motivate them to paying taxes.

The government through the Ministry of Finance Development should fast track and implementation of the national framework for tax policy formulated in 2018, which is part of the Government of Somaliland's PFM Reform Strategy, setting out the Government's goal for an "efficient, effective and accountable use of public resources as a basis for economic development and poverty eradication through improved service delivery.

The study further recommended that SLRA should have an office in every county that will address tax issues at county level and the services to be offered should include tax penalties, filing of tax returns, tax computation and tax differentiation. SLRA should also establish different deduction levels and apply the standard rate plan on the revenue turnover less standard deduction.

SLRA should continuously implement reforms on publicizing prosecution of non-compliant by providing incentives for voluntary compliance and the tax laws should be constantly reviewed to strengthen to seal loopholes that are being exploited by non-compliant SMEs. SLRA should create more awareness on the tax compliance among SMEs through policy documentation which classify different SMEs entity.

The study furthermore recommends that the SLRA should regularly educate and train SMEs on tax related issues and modes of tax payment and collection. SLRA should make the process of taxation as simple as possible so as to favor to make the compliance easy for them. SLRA should also regularly conduct trainings on tax education.

## REFERENCES

- [1] Adebayo, A. (2017). The Effect of Accountability and Transparency on Tax Returns in Nigeria. *International Journal of Innovative Development*, 48 (6), 380 – 405.
- [2] Aksnes, F. (2014). Tax Compliance, Enforcement and Taxpayer Education. *Journal of Centre for Tax and Development*, 20 (2), 30 – 31.
- [3] Alm, J, Bahl, R. & Murray, M. (1990). Tax Structure and Tax Compliance. *The Review Of Economics And Statistics Journal*, 72 (4), 603-613.
- [4] Andreoni, J, Erard, B. (1998). Tax compliance. *Journal of Economic Literature*, 36 (7), 818-60.
- [5] Atawodi, O. W. & Stephen A. O. (2012). Factors That Affect Tax Compliance among Small and Medium Enterprises (SMEs) in North Central Nigeria. *International Journal of Business and Management*, 7(12), 87-96.
- [6] Aumeerun, B., Jugurnath, B. & Soondrum, H. (2016). Tax evasion: Empirical evidence from sub-Saharan Africa. *Journal of Accounting and Taxation*, 8(7), 70-80.
- [7] Ayuba, A., Saad, N. & Ariffin, Z. Z. (2016). Does Perceived Corruption Moderate the Relationship between Economic Factors and Tax Compliance? A Proposed Framework for Nigerian Small and Medium Enterprises. *Mediterranean Journal of Social Sciences*, 7(1), 402-409.
- [8] Bampton, R. (2016). The Determinants of Tax Morale and Tax Compliance. *Journal of Evidence and Advances in Taxation*, 23 (5), 125–171.
- [9] Cooper, D. Schindler, P. (2008). *Business Research Methods*. New York, USA: McGraw Hill.
- [10] Cordon, R. & Palmer, W. (2003). *Business Research Methods*. Geneva, Switzerland: McGraw Hill.
- [11] Creswell, J. W. (2014). *A Concise Introduction to Mixed Methods Research*. New Delhi, India: Sage Productions.
- [12] Chebusit, C., Namusonge, G. S., Oteki, E. B. & Kipkoech, E. C. (2014). Factors Affecting Tax Compliance Among Small and Medium Enterprises in Kitale Town Trans Nzoia county, Kenya. *International Journal of Recent Research in Commerce, Economics and Management (IJRRCEM)*, Vol.1No.3, pp.60-75.
- [13] Cyrlje, T. (2015) the Impact of Tax Knowledge On Tax Compliance. *Journal of advanced research in business and management studies*. 6 (2), 22-30.
- [14] Devos.K (2014). Factors influencing individual taxpayer compliance behavior. *Business and taxation journal*. 17 (9), 607 -625.
- [15] Feld, Y. & Frey, I. (2007). Factors Affecting Tax Compliance Among Small and Medium Enterprises (SMESs in Nakuru County in Kenya: A Survey of SMESs in Naivasha Sub-County. Unpublished Thesis. Management University of Africa.
- [16] Hanlon, D. (2007) the normative imperatives of business and marketing strategy: grounding strategy in resource advantage theory, *Journal of Business Industrial Marketing* 19 (5) 303 -390.
- [17] Hashimzade, N., Myles, G. D. & Tran-Nam, B. (2012). Applications of Behavioural Economics to Tax Evasion. *Journal of Economic Survey*, 27, 941–947.
- [18] James, A & Alley, G (2004) Taxation Of SMEs And Sustainable Economic Development. *Journal of Public Economics*. 12 (5), 205 -240.
- [19] Kiow,S., Salleh,M., & Kassim, B.(2017).The Determinants of Individual Taxpayers' Tax Compliance Behaviour in Peninsular Malaysia. *International Business and Accounting Research Journal*, 9 (5) 405 -455.
- [20] Kirchler, E. (2007). *The economic psychology of tax behavior*. Cambridge: Cambridge University Press.
- [21] Kirchler, E., & Maciejovsky, B. (2001). Tax Compliance Within the Context of Gain and Loss Situations, Expected and Current Asset Position, and Profession. *Journal of Economic Psychology*, 22 (2), 173–194.
- [22] Kirui, S., Kamau, D. & Ombui, K., (2017). Effect of Tax Reforms on Compliance among Small and Medium Enterprises in Kenya: A Case Study in Bomet Town. *International Journal of Management and Commerce Innovations*, 5 (2), 522-531.

- [23] Kothari, C.R. (2004). *Research Methodology: Methods and Techniques*. New Delhi: New Age International Publisher.
- [24] Lin, M. T. & Carrol, C. (2000). The Impact of Tax Knowledge on the Perception Of Tax Fairness And Attitudes Towards Compliance. *Asian review of accounting journal*. 8 (1), 44–58.
- [25] Loo, E. C. (2006). *Determinants of Individual Taxpayers' Compliance Behaviors*. Kula bur, Malaysia: sofa press.
- [26] Loo, E. C., McKerchar, M. & Hansford, A. (2009). Understanding the compliance behaviour of malaysian individual taxpayers using a mixed method approach. *Journal of Australasian Tax Teachers Association*, 4 (1), 181-202.
- [27] Lumumba, O. M., Magutu, O. & Wanjohi, S. M. (2010). Taxpayers' attitudes and tax compliance behavior in Kenya. *African Journal of Business and Management*, 6 (3), 211-234.
- [28] Machogu, G. C. & Amayi, B. J. (2013). The effect of taxpayer education on voluntary tax compliance, among SMEs in mwanza city Tanzania, *International Journal of Marketing, Financial Services & Management Research*. 8 (2), 550-670.
- [29] Marti, M. (2010). Taxpayers' attitudes and tax compliance behavior in Kenya. *African Journal of Business & Management*, 9 (3), 156 – 162.
- [30] Mas'ud, A., Aliyu, A. & Gambo, E. J. (2014). Tax rate and tax compliance in Africa. *European Journal of Accounting Auditing and Finance Research*, 2 (3), 22-30.
- [31] McKerchar, M. & Evans, C. (2009). Sustaining growth in developing economies through improved taxpayer compliance: challenges for policy makers and revenue authorities. *Journal of Tax Research*, 7 (2), 171–201.
- [32] Misra, R. (2004). A Thesis on the Impact of Taxpayer Education on Taxpayer Education on Tax Compliance in South-Africa. Unpublished Thesis.
- [33] Mohd, R. (2010). *Tax Knowledge and Tax Compliance Determinants in Self-Assessment System*. London, UK: Pad Print.
- [34] Mohd, R. P. & Ahmad F. M. (2011). Determinants of Tax Compliance in Asia: A Case of Malaysia, *European Journal of Social Sciences*. 25 (8), 600 – 670.
- [35] Mukasa, J. (2011). *Tax Knowledge, Perceived Tax Fairness and Tax Compliance in Uganda. The Case of Small and Medium Income Taxpayers in Kampala Central Division*, Dissertation. Makerere University, Uganda.
- [36] Mukhlis, I., Sugeng H. U. & Yuli S. (2013). Increasing Tax Compliance Through Strengthening Capacity of Education Sector for Export Oriented smes Handicraft Field in East Java Indonesia. *European Scientific Journal*, 10 (7), 170-184.
- [37] Normala, H. (2007) *Voluntary Compliance and Tax Education Preventive*. Bucharest, Romania: Buch jet.
- [38] Palil, S. (2011) *Effect socialization of Taxation and Knowledge on Awareness Levels and Taxpayer Compliance*. London, UK: Phil.
- [39] Saipei, H & Kasipillai, R (2013) Relationship between Tax Compliance Internationally and Selected Determinants Of Tax Morale. *Journal of International Accounting, Auditing and Taxation*, 13 (7), 135-143
- [40] SLRA (2011). *Somaliland Revenue Administration Reforms in Hargeisa*, Somaliland: Sagal jet
- [41] SLRA (2020). *Somaliland Revenue Administration Reforms in Somaliland. Hargeisa*, Somaliland: NPS
- [42] Tellander, Ebba & Mohamed Aden Hassan (2016) *Accountability in the Taxation System in Somaliland*, PRIO Policy Brief, 24. Oslo: PRIO.
- [43] Williams, C.C. and Round, J. (2009) Evaluating informal entrepreneurs' motives: evidence from Moscow. *International Journal of Entrepreneurial Behavior & Research*, 15 (1), 94-107.