

# Effect of Taxpayer Sensitization on Excise Duty Compliance Among Manufacturing Firms in Embakasi West Nairobi County, Kenya

Gatimu Flavian Kung'u<sup>1</sup> & Dr. Bruce Ogaga<sup>2</sup>

<sup>1</sup>Tax Administration, Kenya School of Revenue Administration

<sup>2</sup>Kenya School of Revenue Administration

Corresponding Email: gatimuflavian@gmail.com

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## Abstract

**Purpose:** Although the implementation of the excise tax has the potential to enhance revenue collection, its contribution to the GDP has remained negligible in comparison to other forms of taxation. Consistently, the total amount of the excise tax collected has been below the set targets. The general objective was to determine the effect of taxpayer sensitization on excise duty compliance among manufacturing firms in Embakasi west Nairobi County, Kenya. The study was supported by the Theory of Planned Behaviour.

**Methodology:** The study adopted explanatory research design and target a population was 416 manufacturing firms in Embakasi West Nairobi. A sample size of 203 was drawn from this population and a response of 173 which thus 85% response rate. Primary data collection was employed using closed structured questionnaires based on the study's objectives. The data was analyzed using descriptive, inferential statistics and multiple linear regression analysis.

**Results:** The study showed that taxpayer sensitization positively affects excise duty compliance  $\beta=0.270$   $p\text{-value}=0.001 < 0.05$ .

**Conclusion:** The government should implement nationwide educational campaigns to inform taxpayers about their excise duty obligations.

**Keywords:** *Manufacturing Firms Taxpayer Sensitization, and Excise Duty Compliance*

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## 1.0 Introduction

Governments all over the world depend on tax revenue to provide public goods and services. To meet the growing need for economic development and growth, these governments have come up with various tax regimes, systems, and bases (Linegar and Walbeek (2020). Collecting taxes and fees is a fundamental task for countries to generate public revenue that makes it possible to finance investments in human capital, infrastructure, and the provision of services for citizens and businesses (IMF, 2020).

Excise refers to taxes charged on every unit of a commodity on products such as alcohol and cigarettes that are sold and differs from sales tax since it is levied per unit of the commodity instead of as a percentage. One of the main goals of excise is to discourage consumption of a certain good although they are also a revenue source for government (Fitcher, 2021). According

to the OECD (2018), excise tax refers to a tax imposed on an occupation, act, privilege, sale, or manufacture and is selectively levied on certain goods and services.

Excise taxes are an important means by which local and national governments can raise additional revenue that is necessary for major projects. Often, excise taxes are levied on alcohol, cigarettes, and gambling as they are considered superfluous services and goods. Raising taxes on such products results in their prices being raised and reduce the amounts used; which is another important function of excise taxes; they result in a reduction in quantity sold as the prices consumers pay increases and revenues produced get reduced as demand falls (Needles, Anderson, & Caldwell, 2022). Taxpayer sensitization refers to the process of educating and informing taxpayers about their rights, responsibilities, and obligations regarding taxation. It aims to enhance taxpayers' awareness and understanding of tax laws, regulations, and procedures to promote compliance and minimize tax evasion OECD, (2020).

Taxpayer sensitization plays a crucial role in promoting voluntary compliance, reducing tax evasion, and building trust between taxpayers and tax authorities. By empowering taxpayers with knowledge and support, tax administrations can enhance revenue collection efficiency and contribute to sustainable economic development. The tax knowledge gained by the taxpayers would be a determinant factor towards the behavior of the taxpayers. Akintoye and Tashie (2019) stressed tax education which is significantly associated with tax compliance behavior in Nigeria. Tax officials have to realize that the easier it is for them to comply effectively, the more educated taxpayers are. Tax information in general is an appreciation of the core principles of tax policy applied to a country (Fauziati et al., 2016). Tax system enforcement describes an interpretation of SMEs' tax policies in an area. In a compliance tax system, tax education for multiple small and medium enterprises is an essential element, particularly in determining an accurate tax liability (Baru, 2016).

### **1.1 Problem Statement**

Excise Duty compliance has remained low, contributing to only 40% of total revenue collected in Kenya. Despite these reforms, Excise Duty compliance has remained low, the overriding objective of excise taxes in Kenya is to raise tax revenues, but the performance has been weak (Deloitte, 2019). The collection of Excise Duty in the financial year 2021/2022 was Ksh.662,350,000 compared to a target of Ksh.705,150,000 falling short of the target by Ksh 87,800,000 million (KRA, 2022). In the financial year 2022/2023, the set target was Kshs.195,220,000 million, yet the revenue authority only collected Kshs.183,250,000 again falling short of the target by Ksh 11,970,000 (KRA, 2023) This has raised a concern, especially on excise duty which has been declining over the years. The effect of non-compliance is giving the government a hard time in performing its obligations such as offering services as well as infrastructure development. Taxpayers in this sector are yet to fully comply with the requirements of the respective tax laws. For instance, Bidin, Sinnasamy, and Othman (2018) conducted research investigating determinants of importers' excise duty compliance in Malaysia. Chesire (2019), studied the relationship between excise tax regimes and the profitability of listed sin products (alcohol and cigarettes) manufacturers in Kenya, therefore, it is against this background that this study will fill the missing knowledge gap in literature by establishing moderating effect of digitalization on factors affecting excise duty compliance among manufacturing firms in Embakasi west Nairobi County, Kenya.

## 2.0 Literature Review

### 2.1 Theoretical Review

This theory was developed by Ajzen in 1991. It is of the view that, some definite factors influence the behavior of individuals. These factors originate from certain reasons and are usually planned by these individuals. The essential thrust of this approach is that individuals are not risk-neutral or risk-averse but simply make decisions based on their cost-benefit analysis of the gains versus the projected losses. Ajzen's (1991) theory of planned behaviour posits that individuals make rational choices to engage (or not engage) in the behaviour of interest. The choices made are influenced by individuals' own beliefs about the outcome and the evaluation of the favorableness (or unfavorableness) of the outcomes from engaging in the target behaviour. These beliefs and expected outcomes underlie three conceptually distinct salient beliefs, which are central to the theory of planned behaviour. These are behavioural beliefs (perceived beliefs about the likely outcomes from engaging in the target behaviour and the evaluation of the desirability of these outcomes); normative beliefs (perceived social pressure); and control beliefs (perceived ease or difficulty of engaging in a desired/undesired behaviour).

Behavioral intention will influence the behavior of such individuals and behavioral intention is determined by readiness attitude to respond to positive or negative objects or situations. Therefore, taxpayers have an awareness that taxes paid for the benefit of the public in general give a positive response to the taxpayers' behavior to taxes paid (Nurwanah, 2018). Taxpayers' behavior includes their intention to make tax payments, which has an impact on tax compliance behavior (Novianti & Dewi, 2018). Ullah (2019) recommended that subjective norm has a meaningful connection with individual taxpayer's intention to comply. Intention to pay taxes means that taxpayers are ready to pay those taxes and fulfill all their tax obligations (Dobos & Takács-György, 2020; Tambun & Haryati, 2022). The theory supports that compliance costs influence taxpayer compliance. This is a psychological theory that links beliefs and behaviour, and tries to explain human behaviour.

The concept was proposed by Icek Ajzen to improve on the predictive power of the theory of reasoned action by including perceived behavioural control. According to this theory, the behaviour of individuals within the society is under the influence of definite factors which originate from certain reasons and emerge in a planned way. The ability to perform a particular behaviour depends on the fact that the individual has a purpose towards that behaviour (behavioural intention). Behavioural intention, in turn, depends on three factors that is Attitude towards the behaviour, Subjective norms, and Perceived behavioural control.

## 2.2 Empirical Review

### 2.2.1 Taxpayer Sensitization

According to Tukur and Onyegbule (2011), taxpayer education is the foundation of understanding tax laws which ensures filing tax returns/payments promptly. Tax knowledge enhances tax compliance; it also assists tax authorities in designing tax education programmes and developing an understanding of taxpayers' behaviors (Palil & Mustapha, 2021). However, Sapiei & Kasipillai (2020) noted that taxpayers have knowledge of SAS as seminars and training are being facilitated by the tax authority to fulfill its responsibilities to the taxpayers. Lai, Zalilawati, Amran, and Choong (2019) stressed that studies on tax education in emerging economies are rare. This is because tax awareness in most developing countries may be below average.

Gitaru (2018) described the effect of electronic taxpayer education, print media taxpayer education, and stakeholder engagement on tax enforcement. SMEs in the CBD Tax Area of Nairobi were the target population. SMEs conducting business inside Nairobi CBD were the focus of the analysis. Data was obtained by administering pre-tested questionnaires to the business owners of SMEs. Both descriptive and inferential statistics have been used to evaluate results. Indeed, the results of the study showed that electronic taxpayer education, print media taxpayer education, and stakeholder engagement affect tax compliance among SMEs in the CBD region of Nairobi. To evaluate the association between the independent variables, the Correlation Matrix was used. The findings showed that the sensitization of stakeholders was directly connected with the education of taxpayers.

Karanja (2020) Abroad campaign to publicize tax and sensitize taxpayers need to be carried out. This includes activities such as regular radio programs, banners, permanent signs, ward meetings, street theatre, announcements at local churches, mosques, football matches, town-crier, vehicle signs, posters, newspapers, and business promotion. More so, the revenue authority can employ focused education on specific areas of tax generation as in case of KRA which has focused on education on rental income and the importance of compliance (KRA, 2012).

### **2.2.2 Excise duty Compliance**

Excise duty is a tax imposed on goods and services manufactured in Kenya or imported into Kenya and specified in the first schedule of the Excise Duty Act (2015). Governments use excise taxes to implement benefits-received approach to taxation, for instance, taxes on petroleum products. The use of petroleum is related closely to highway travel and so offers a link between taxes paid and benefits derived from the highways. The link is strengthened further by specifying areas where such taxes are to be used in offering government services relating to the activity; for instance, using fuel taxes on highway construction and maintenance (Cordes, Ebel & Gravelle, 2020).

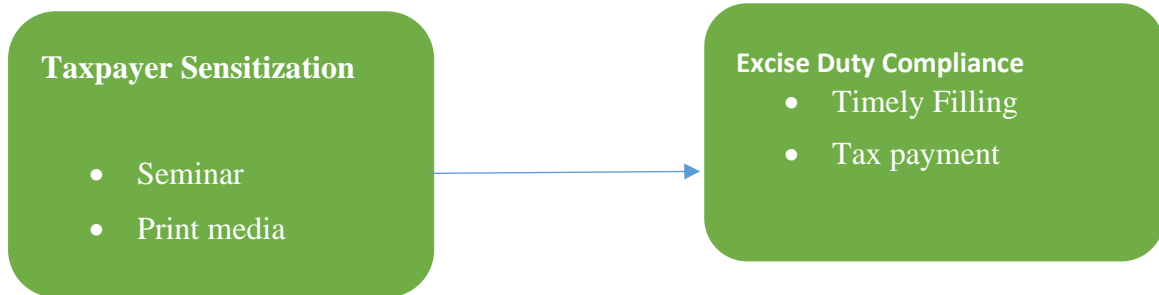
The excise tax income in Kenya exhibited growth in both real and nominal terms from 1980 to 1996. This growth was observed in two aspects: as a proportion of total ordinary revenue and as a proportion of the country's GDP. When compared to other forms of taxation, excise taxes have consistently demonstrated an upward trajectory in terms of their performance as a proportion of the GDP. In this context, the efficacy of alternative tax structures, such as income taxes, has seen a marginal increase or even a drop in recent years (value-added taxes and import duties).

Ochieng and Agwaya (2020) assert that excise taxes serve as a substantial revenue stream in Kenya. Excise taxes in Kenya have always played a substantial role in the country's overall tax revenue generation. Excise taxes provide a significant proportion of the overall revenue in the country of Kenya. Between the years 1980 and 2018, the imposition of excise taxes in Kenya resulted in an average contribution of 3.1 percent towards the nation's GDP. However, this contribution is still below the expected contribution of 4.5 percent towards the nation's GDP. This shows that the taxpayers' compliance with excise duty tax is still low.

### **2.3 Conceptual Framework**

This is an analytical tool with several variations and contexts. It is used to make conceptual distinctions and organize ideas in a way that is easy to remember and apply. Conceptual framework explains either graphically, or in narrative form, the main things to be studied, the key factors, concepts, or variables, and the presumed relationship among them (Miles et al, 1999). The Independent variables of this study is Taxpayer sensitization and. Dependent

variable was excise duty compliance.



**a. Independent Variable**

**b. Dependent variable**

**Figure 1 Conceptual Framework**

### 3.0 Methodology

A research design is the plan and structure of investigation so conceived as to obtain answers to study objectives (Bryman & Cramer, 2012). Simply put, research design is a logical strategy used by a researcher in ensuring that the research problem is effectively addressed. The study employed the explanatory research design. This design seeks to find out what is causing a certain occurrence to happen. It explains the effect of one variable on another (Gray 2013). Creswell and Creswell (2019) describe target population as the complete set of elements or objects that have the same recognizable characteristics. A population refers to a set of elements (objects or persons) that possess similar characteristics defined by the sampling criteria established by the researcher. It also includes all people or items with the characteristic the researcher wishes to understand. In this research, the target population was 416 manufacturing firms in Embakasi west Nairobi County. The study sample size was 203 manufacturing firms in Embakasi west Nairobi County KRA (2023).

Cronbach's reliability test checks if a measurement scale or questionnaire is consistent. It checks how closely related the items in a scale are. High Cronbach's alpha values (usually greater than (0.7) show that the test is reliable. Table 4.1 shows that excise duty  $\alpha=0.975$  and taxpayer sensitization  $\alpha=0.962$ . The results indicates that Cronbach's Alphas are  $>0.7$  indicating reliability in the questionnaire responses

**Table 1: Test of Reliability of Questionnaire**

Factor	Number of Items	Cronbach Alpha score	Conclusion
Excise duty compliance	0.975	5	Reliable
Taxpayer sensitization	0.962	5	Reliable

## 4.0 Results and Discussion

### 4.1 Descriptive Statistics

Descriptive statistics are essentially techniques employed to compute, portray, and condense gathered research data in a coherent, significant, and effective manner. The research utilizes these methods to present findings concerning the descriptive characteristics of the collected data, including measures such as standard deviations and means of the variables.

#### 4.1.1 Descriptive statistics for Taxpayer Sensitization

**Table 2: Descriptive Statistics Taxpayer Sensitization**

	N	Mean	Std. Deviation	Skewness	Kurtosis
I understand my Tax Obligations	173	3.83	1.089	-.507	-1.037
KRA workshops have improved my knowledge of tax laws		3.87	1.089	-.552	-.994
Our business has been sufficiently sensitized by KRA about the changes in the Act.		4.00	1.078	-.732	-.773
KRA organizes workshops to sensitize manufacturers about excise duty compliance		4.05	1.083	-.788	-.727
KRA sensitization have improved my knowledge of excise duty compliance		4.06	1.074	-.812	-.672
<b>Aggregate Mean</b>		<b>3.96</b>			

The above table presents: I understand my Tax Obligations that has a mean of 3.83 and a SD of 1.089. KRA workshops have improved my knowledge of tax laws has a mean score of 3.87 and SD of 1.089. Our business has been sufficiently sensitized by KRA about the changes in the Act and has a mean score of 4.00 and SD of 1.078. KRA organizes workshops to sensitize manufacturers about excise duty compliance and has a mean score of 4.05 and SD of 1.083. KRA sensitization has improved my knowledge of excise duty compliance has a mean score of 4.06 and SD of 1.074

#### 4.1.2 Descriptive statistics for excise duty compliance

I'm registered for the correct tax obligation has a mean score of 4.07 and SD of 1.081. I always file tax by the due date has a mean score of 4.13 and SD of 1.038. I always declare the correct amount has a mean score of 3.98 and SD of 1.086. I pay the correct tax by due date has a mean score of 4.09 and SD of 1.083. I'm always compliant with all tax policies and files tax return on time has a mean score of 4.02 and SD of 1.067. Table 4 represents the information:

**Table 3: Descriptive statistics Excise Duty Compliance**

	N	Mean	Std. Deviation	Skewness	Kurtosis
I'm registered for the correct tax obligation	173	4.07	1.081	-.809	-.710
I always file tax by the due date.		4.13	1.038	-.890	-.478
I always declare the correct amount.		3.98	1.086	-.736	-.564
I pay the correct tax by due date.		4.09	1.083	-.897	-.334
I'm always compliant with all tax policies and files tax returns on time		4.02	1.067	-.801	-.405
<b>Aggregate Mean</b>		<b>4.06</b>			

#### 4.2 Correlation Analysis

Correlation analysis was conducted to determine the nature of the relationship between the variables in the regression. Taxpayer sensitization correlates to with excise duty compliance significantly  $r = 0.605$  This means that as taxpayer sensitization increases, excise duty compliance also tends to increase.

**Table 4: Represents the correlation statistics**

	Excise duty compliance	Taxpayer sensitization
Excise duty compliance	1	0.605**
Taxpayer sensitization	0.605**	1

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

### 4.3 Regression Analysis

The results in Table 5 indicated that taxpayer sensitization had a positive correlation with Excise duty compliance up to 60.5% or (R= 0.605). The results reveal that taxpayer sensitization caused a variation of 36.6% or ( $R^2=0.366$  and adjusted  $R^2 =0.359$ ) on excise duty compliance.

**Table 5: Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.605	0.366	0.359	0.45022

a. Predictors: (Constant), taxpayer sensitization.

ANOVA was used to determine the variation caused on Excise Duty Compliance Taxpayer sensitization. Table 6 shows a F statistic of 56,556, and p-value of  $0.000 < 0.05$  indicating that the model summary significantly showed the effects of factors affecting Excise Duty Compliance.

**Table 6: ANOVA<sup>a</sup>**

Model		Sum Squares	of df	Mean Square	F	Sig.
	Regression	113.903	1	113.903	122.344	.000 <sup>b</sup>
1	Residual	159.288	171	.931		
	Total	273.191	172			

a. Dependent Variable: Excise\_Duty\_Compliance

b. Predictors: (Constant), taxpayer sensitization,

The hypothesis  $H_{01}$  stated that taxpayer sensitization has no significant effect on excise duty compliance among manufacturing firms in Embakasi west Nairobi County, Kenya. The study showed that taxpayer sensitization has a positive and significant effect on excise duty compliance  $p\text{-value} = 0.001 < 0.05$  therefor hypothesis was rejected.

**Table 7: Regression Coefficients**

Model		Standardized Coefficients		Unstandardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.571	0.242		2.360	.020
	Taxpayer Sensitization	0.270	0.077	0.281	3.506	.001

a. Dependent Variable: Excise duty compliance



#### 4.4 Discussions of findings

The study established the effect of taxpayer sensitization on excise duty compliance among manufacturing firms in Embakasi West Nairobi County, Kenya. The correlation matrix showed that taxpayer sensitization has a positive and significant relationship with excise duty compliance at 60.5%. These findings suggest that efforts aimed at sensitizing taxpayers about their obligations regarding excise duties have a meaningful impact on their compliance behaviour. The coefficient analysis indicated that taxpayer sensitization has a positive impact on excised duty compliance  $\beta=0.270$  p-value  $=0.001<0.05$ . This finding implies that educational campaigns, outreach programs, or other initiatives designed to increase taxpayer sensitization and understanding of excise duty regulations among taxpayers are effective in promoting compliance with these obligations. The study concurred with Tukur and Onyegbule (2011) who posit that taxpayer education is the foundation of understanding tax laws which ensures filing tax returns/payments promptly. Tax knowledge enhances tax compliance; it also assists tax authorities in designing tax education programmes and developing an understanding of taxpayers' behaviors.

#### 5.0 Conclusion

the study highlights the critical role of taxpayer sensitization in promoting excise duty compliance. Efforts to educate taxpayers about their obligations regarding excise duties were found to positively influence compliance behaviour. This underscores the significance of educational campaigns and outreach programs in fostering a culture of compliance among taxpayers.

#### 6.0 Recommendations

The study recommends that the government should implement and intensify nationwide campaigns to enlighten taxpayers. A study should be conducted on the effects of tax reforms on Excise Duty compliance.

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