

## The Effect of Dispute Resolution Reform on Rental Income Tax Compliance Among Residential Landlords in Ruaka Town, Kiambu County, Kenya

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### Abstract

Rental income tax compliance is important as it has a direct impact on revenue for most governments around the world. The Kenya Revenue Authority has, of late, failed to meet its revenue targets, particularly rental income tax targets. The purpose of the study was to determine the effect of dispute resolution reform on rental income tax compliance among residential landlords in Ruaka Town, Kiambu County, Kenya. The theory that guided this study was Procedural Justice Theory. An explanatory research design was adopted. The target population was 2103 residential landlords in Ruaka Town, Kiambu County, and a sample size of 336 respondents was calculated using the Yamane formula. Primary data was collected using a structured questionnaire. A pilot study was done to test the validity and reliability of the research instrument. Both descriptive statistics and inferential statistics were carried out with the help of the SPSS software. Inferential statistics such as Pearson correlation and multiple regression analysis were used to test the relationship between the study's dependent variable and the independent variables. The beta coefficient results revealed that Dispute resolution reform had a positive and significant effect on rental income tax compliance ( $\beta = 0.099$ ,  $p = .020$ ). The significant positive effect of dispute resolution reform suggests that the government should strengthen tax dispute mechanisms by ensuring fairness, transparency, and accessibility in conflict resolution processes. Future researchers could investigate the effects of attitude and perception, which are behavioral factors that might be analyzed to find their relative effect on the taxpayers in compliance with the rental income tax.

**Keywords:** *Dispute Resolution Reform, Rental Income Tax Compliance, Residential Landlords*

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### 1. Introduction

Tax is essential to the development of the state, both as a source of revenue to finance infrastructure and redistribution, and the establishment of a fiscal social contract between the government and the citizens. This becomes an urgent constant in case tax is not sufficient to finance the necessary spending in other spheres like infrastructure, health, and education

(Forstater, 2019). Tax compliance is the level of compliance with the tax rules and regulations by a taxpayer (Sapiei, 2023).

Rental income tax is a tax on the gains or profits comprising royalty, premium, or other consideration received as a result of the use or occupation of property (Chapter 470, Income Tax Act, section 6). There is a direct tax on rent income through self-assessment, as compared to expenditure consumption tax. One of the basic sources of revenue for the government and local authorities is rental income taxes (Tyson, 2020). The volume of revenue that can be raised by these sources is, however, subject to numerous factors. Kirchler (2021) defines the factors as individual, institutional, and economic. With respect to rental income taxpayers, Rizali (2021) set the attitudinal and knowledge difference, high tax rate, taxation system, lack of honesty of rental taxpayers, lack of awareness, complexity of tax legislation and regulation, which can result in high tax noncompliance levels.

Rental Income Tax is a tax payable by resident persons (individual or company) on rental income earned for the use or occupation of a residential property (KRA, 2015). In Kenya, rental income tax compliance is governed by the Income Tax Act, which mandates that resident individuals and companies earning rental income from residential properties adhere to specific tax obligations. Effective January 1, 2024, the Monthly Rental Income (MRI) tax rate is set at 7.5% of the gross rental income received. This tax applies to landlords whose annual rental income exceeds KShs. 288,000 but does not surpass Kshs. 15 million. The MRI is considered a final tax, meaning that taxpayers are not required to declare this income in their annual returns. To enhance compliance, the Kenya Revenue Authority (KRA) has implemented measures such as appointing rental income tax agents responsible for collecting and remitting the tax to the Commissioner.

Dispute resolution reform in tax compliance is the modernization of the mechanisms of resolving disagreements between taxpayers and tax authorities, and improving them to be fair, efficient, and restore trust in the tax system. Traditional tax dispute processes are often time-consuming, costly, and inaccessible, which can discourage compliance and fuel perceptions of bias or inefficiency. Reforms in this area typically involve streamlining administrative appeal procedures, introducing alternative dispute resolution (ADR) methods such as mediation and arbitration, and enhancing the independence and capacity of tax tribunals. As noted by Baistrocchi and Olimid (2022), effective tax dispute resolution systems contribute significantly to improving voluntary compliance by providing taxpayers with transparent and impartial forums to resolve grievances. By minimizing litigation burdens and offering quicker resolutions, these reforms help to foster a more cooperative tax environment and reduce resistance to enforcement.

### **1.1 Problem Statement**

In many countries, taxes are the main source of income that governments use to provide their citizens with goods and services. However, because some taxpayers do not comply, low compliance has always been a problem. The house rental taxation system has encountered many difficulties from both taxpayers and bureaucrats, much like any other tax system. Due to the high number of citizens involved, most third-world countries have considered house rental taxes to be economic transactions that are fairly difficult to detect (Lai et al., 2022).

Ever since the introduction of the Rental Income Tax in the Finance Act 2015, a complex structure has been crafted with the objective of educating and helping landlords to adapt to the

simplified taxation regime. Although the Kenya Revenue Authority has been performing reforms to boost its revenue collection, it has not been able to achieve its targets in revenue, especially the rental income tax targets. A report conducted by KRA (2024) reveals that KRA has been operating at a loss of its targets. In the 2023/2024 financial year, the authority received Rental Income Tax of Kes 14.4 billion, in an amount of Kes 16.3 billion as the set target. The failure of KRA to meet its target is impacting the development of infrastructure and the delivery of social services by the government.

## 2. Literature Review

### 2.1 Theoretical Review

#### 2.1.1 Procedural Justice Theory

Procedural Justice Theory was developed by Tyler in 1990. This theory centers on the idea that people's willingness to comply with rules and accept decisions is strongly influenced by their perception of the fairness of the procedures used to make those decisions, rather than solely by the outcomes themselves. Tyler's foundational work, *Why People Obey the Law*, emphasizes that individuals are more likely to view authority as legitimate and comply with legal rules when they feel they have been treated with respect, given a voice in the process, and encountered neutrality and fairness during their interactions with institutions.

Tyler identifies four key elements of procedural fairness: voice (the opportunity to express one's perspective), neutrality (unbiased decision-making), respect (dignified treatment), and trust (the belief that authorities are benevolent and acting in good faith) (Bello & Mazur, 2014). These components are essential in building the perceived legitimacy of legal and administrative systems. In contexts such as tax compliance, if taxpayers believe the tax authority acts fairly and allows them to contest decisions or appeal penalties through transparent and respectful processes, they are more likely to voluntarily comply with tax laws even when outcomes are not in their favor (Lind, 1988).

The theory has profound implications for public administration and governance, suggesting that legitimacy and cooperation are not achieved through coercion or fear of punishment alone, but through procedural integrity and fairness. In practice, this means designing dispute resolution systems and service delivery models that prioritize fairness, transparency, and citizen engagement. For example, accessible tax appeal processes or taxpayer education programs that treat citizens respectfully can significantly improve trust in the tax system and increase compliance. The theory supports dispute resolution reform.

## 2.2 Empirical Review

### 2.2.1 Dispute Resolution Reforms

The study by Maple and Jones (2021) was a comparative study of small tax dispute resolution in New Zealand. It compared the case of New Zealand with Australia and Canada. The paper determined that the administrative reforms proposed by the New Zealand tax dispute process, as practiced by Inland Revenue in 2020, such as the option to exit the process after the conference and the duration of NOPAs, are encouraging. The study advised that when the dispute is still pending in whole or in part, the rights of taxpayers to review and appeal are compromised in one way or the other.

In Tanzania, the tax appeal procedures for Tax disputes are normally through the tax revenue appeal board, the tax revenue appeal tribunal, and the Court of Appeal of Tanzania. In conclusion, the tax appeal tribunal aids in settling disputes that pertain to taxation in Kenya, and this aids in tax compliance and revenue collection in Kenya, since once a tax decision has been made after an assessment, the taxpayer will pay the sum that the tribunal decided, and in exchange, they will become compliant. It also acts as a forum of first instance, prior to the commencement of tax litigation on a tax dispute.

Moore (2019) reviewed the importance of alternative dispute resolution (ADR) in tax systems in sub-Saharan Africa. In their work, they note that tools of ADR, including mediation and arbitration, can enhance compliance with taxation by providing less formalized, more accessible forms of dispute resolution. Their study had discovered that taxpayers are better placed to accept and comply with tax obligations when tax disputes are resolved promptly with ADR instead of depending on protracted court battles. Moreover, they promote a shared way of solving the problems, which contributes to better relations between taxpayers and tax authorities

### **2.2.2 Rental Income Tax Compliance**

The Organization for Economic Co-operation and Development (OECD) has found that keeping the rental industry liable to tax is essential in both keeping the tax system fair and making sure that all income streams are well taxed (OECD, 2022). Around the globe, governments are attempting to use the data-sharing channels and digital solutions to enhance compliance and identify underreporting of rental revenue. The tax on the income from the rent of residential buildings is the tax on the income from the rent. Because whatever form of income one gets through renting out a property is subject to taxation under income tax law, the owners of the property must declare such income on their tax returns. This revenue may be because of renting land or buildings (Berhane & Yesuf, 2022).

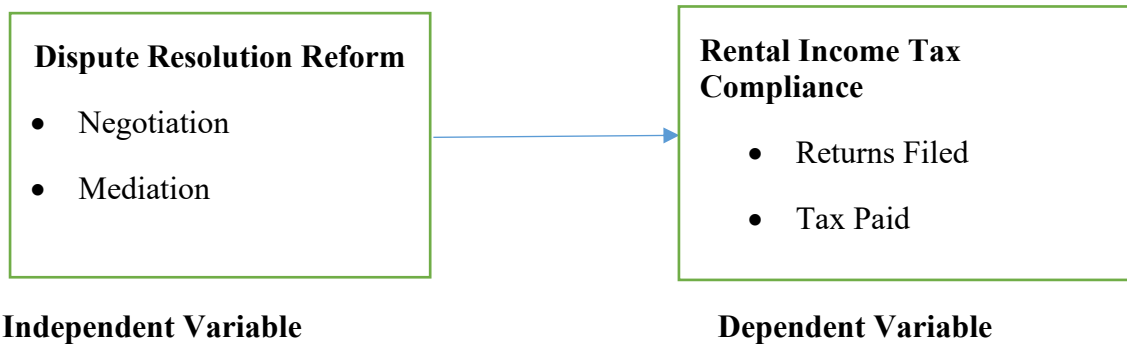
Rental income tax performance can be enhanced in several ways. An option is to claim deductions and tax credits on rental income, including the residential energy credit and the mortgage interest deduction (Maharaj, 2019). Moreover, property owners are able to think about buying more efficient energy-saving appliances and home renovations to minimize their monthly utility rates and, consequently, boost rental incomes. Lastly, the owners of property also seek a method to minimize their tax payment by utilizing tax deferral measures or utilizing tax incentives provided by their local authorities (Rothman, 2020).

According to Kingoina (2020), the level of compliance with rental income tax compliance has remained low in Kenya despite the administrative reforms in place because of poor knowledge of the law on rental income tax compliance and negative perceptions and attitudes towards payment of rental income tax compliance. It is estimated that every year, an average of 30 percent of the total number of taxpayers do not file their tax returns on rental income compliance, and a great number continue to be prosecuted yearly due to non-filing of full returns.

### **2.3 Conceptual Framework**

According to Cooper and Schindler (2018), a conceptual framework is a construct that demonstrates the relationship between the study variables. The framework assists in specifying and defining the concepts of the problem under study. Conceptual framework refers to

generalized ideas and principles borrowed from pertinent areas of enquiry to be applied to form a later presentation (Kombo & Tromp, 2009). The conceptual framework has Rental Income Tax Compliance as the dependent variable, whereas Dispute Resolution Reform is the independent variable, as shown in Figure 1.



**Figure 1: Conceptual Framework**

### 3. Methodology

Research design refers to the road map to be followed when conducting a research study to ensure that it is able to answer the research problem. It gives a guide within which the information is gathered, and the analysis of the information is determined. These research designs can be broadly divided into three, which include exploratory research design, descriptive research design, and causal research design (Blatter & Haverland, 2012). The research design used was explanatory research. According to Saunders et al. (2007), explanatory studies aim at describing the characteristics of the variables as well as exploring the causal relationships among variables. The target population can be defined as the sample of individuals or research population that is comparable in some aspect or more, and which acts as the subject of study in each study in a given survey (Orodho, 2003). The target population was 2,103 residential landlords in Ruaka Town, Kiambu County (KRA, 2024). The sample size was 336 residential landlords in Ruaka Town, which was calculated using the Yamane formula. The response rate in Table 1 shows that the study targeted a sample size of 336 respondents, and after response collection and tallying of the responses, 252 respondents correctly filled and submitted their questionnaires, indicating a 75% response rate.

**Table 1: Response Rate Analysis**

	Number	%
Response Rate	252	75.0%
Non-Response Rate	84	15.0%
Targeted Sample	336	

### Reliability Analysis

Measurement inconsistencies can arise from various sources, making perfect replication challenging. To assess the internal consistency of scale items, this study employed Cronbach's alpha, a widely accepted reliability coefficient. A threshold of 0.7 was adopted as the minimum acceptable value, aligning with contemporary recommendations that suggest values at or above this level indicate satisfactory reliability for research instruments (Frost, 2023). In this pilot

study on table 2, Cronbach’s alpha values were computed for five constructs: rental income tax compliance (.973) and dispute resolution reform (.948 ), each measured with five items.

**Table 2: Test of Reliability of Questionnaire**

Factor	Number of Items	Cronbach's Alpha score	Conclusion
Rental income tax compliance	5	0.973	Reliable
Dispute resolution reform	5	0.948	Reliable

## 4. Results and Discussion

### 4.1 Descriptive Statistics

#### 4.1.1 Descriptive Statistics on Dispute Resolution Reform

Table 3 shows that the statement, “I find the Dispute Resolution process fairly shorter compared to the Tax Appeal Tribunal and court system,” had a mean of 4.06 (SD = 0.547), indicating strong agreement with low variability among respondents. The statement, “I am aware of channels for raising customer complaints if displeased with the ADR process,” had a mean of 4.00 (SD = 0.609), reflecting strong agreement with moderate variability. The statement, “I find it easy to use KRA systems/processes,” had a mean of 3.96 (SD = 0.523), indicating strong agreement with low variability. The statement, “The DR process makes it easy for me to settle tax cases fairly and would thus recommend it to others,” had a mean of 3.91 (SD = 0.568), reflecting moderate to strong agreement with low variability. The statement, “I find legal/agent fees affordable compared to when using the Tax Appeal Tribunal and court system,” had a mean of 4.05 (SD = 0.524), showing strong agreement with low variability. The overall mean of 4.00 suggests that, on average, respondents strongly agreed with the statements regarding the efficiency, accessibility, and fairness of the Dispute Resolution (DR) process compared to traditional legal avenues. The generally low standard deviations indicate consistent agreement, while skewness and kurtosis values suggest mostly symmetrical and moderately peaked distributions.

**Table 3: Dispute Resolution Reform**

	N	Mean	Standard Deviation
I find the Dispute Resolution process fairly shorter compared to the Tax Appeal Tribunal and the court system.	252	4.06	.547
I am aware of channels for raising customer complaints if displeased with the ADR process.		4.00	.609
I find it easy to use KRA systems/processes.		3.96	.523
The DR process makes it easy for me to settle tax cases fairly and would thus recommend it to others.		3.91	.568
I find Legal/agents' fees affordable compared to when using the Tax Appeal Tribunal and court system.		4.05	.524
Overall Mean		4.00	

#### 4.1.2 Descriptive Statistics for Rental Income Tax Compliance

Table 4 shows that the statement, “I always file my rental income tax compliance returns as stipulated by the law,” had a mean of 4.00 (SD = 0.599), indicating strong agreement with low variability. The statement, “I promptly register for new tax obligations once I meet the legal criteria,” had a mean was 3.97 (SD = 0.624), reflecting strong agreement with moderate consistency. The statement, “I correctly compute and pay my rental income tax by the deadline,” had a mean of 3.94 (SD = 0.644), showing strong agreement with moderate variability. For “I file my rental income tax returns voluntarily, without enforcement pressure,” the mean was 4.04 (SD = 0.670), demonstrating strong agreement with moderate variability. The statement, “I always declare the full and accurate amount of my rental income,” had a mean of 4.06 (SD = 0.689), reflecting strong agreement with moderate variability. The overall mean of 4.00 suggests that, on average, respondents strongly agreed with the statements regarding rental income tax compliance, demonstrating consistent adherence to tax filing, registration, computation, voluntary filing, and accurate income declaration.

**Table 4: Rental Income Tax Compliance**

	N	Mean	Standard Deviation
I always file my rental income tax compliance returns as stipulated by the law	252	4.00	.599
I promptly register for new tax obligations once I meet the legal criteria.		3.97	.624
I correctly compute and pay my rental income tax by the deadline.		3.94	.644
I file my rental income tax returns voluntarily, without enforcement pressure.		4.04	.670
I always declare the full and accurate amount of my rental income.		4.06	.689
Overall Mean		4.00	

#### 4.2 Correlation Analysis

The correlation analysis was utilized to determine the relationships between dispute resolution reform and rental income tax compliance among residential landlords in Ruaka Town, Kiambu County, Kenya. Table 5 showed that Dispute Resolution Reform was positively and significantly correlated with rental income tax compliance ( $r = .652$ ,  $p .004 < 0.05$ ), highlighting that accessible and fair mechanisms for resolving tax disputes foster a favorable compliance environment. Taxpayers are more likely to participate voluntarily when they believe that the resolution process is impartial and supportive (Waweru, 2017; Mugambi & Jagongo, 2019).

**Table 5: Correlation Statistics**

	Rental income tax compliance	Dispute Resolution Reform
Rental income tax compliance	1	0.652**
Dispute Resolution Reform	0.652**	1
Sig.	0.004	

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

### 4.3 Regression Analysis

Table 6 showed that Dispute Resolution Reform had a positive correlation with Rental income tax compliance, trade of up to 65.2% or (R= 0.652). The results reveal that Dispute Resolution Reform caused a variation of ( $R^2=0.425$  and adjusted  $R^2 =0.425$ ) on Rental income tax compliance.

**Table 6 Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.652 <sup>a</sup>	.0425	.421	.34278

a. Predictors: (Constant), Rental income tax compliance  
 \_mean

Table 7 shows that there was an F statistic of 367.819 and a p-value of  $0.000 < 0.05$ , which indicates that the model was significant in explaining the variance caused by Rental income tax compliance.

**Table 7: ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	69.150	1	69.150	367.819	0.000
	Residual	47.206	250	0.188		
	Total	116.356	251			

a. Dependent Variable: Rental income tax compliance

b. Predictors: (Constant), Dispute Resolution Reform

Table 8 showed that a unit change in Dispute Resolution Reform caused a 0.099 increase in Rental income tax compliance. The study found that Dispute Resolution Reform had a positive and significant effect on Rental income tax compliance,  $\beta =0.099$ , p-value  $=0.020 < 0.05$ . Consequently, the null hypothesis was rejected.



**Table 8: Regression Coefficient Analysis**

Model		Standardized Coefficients $\beta$	Std. Error	Unstandardized Coefficients $\beta$	t	Sig
1	(Constant)	1.475	0.273		5.403	0.000
	Dispute Resolution Reform	0.099	0.029	0.068	2.345	0.020

a. Dependent Variable: Rental income tax compliance

#### 4.4 Discussion of the Findings

The study sought to establish the effect of dispute resolution reform on rental income tax compliance among residential landlords in Ruaka Town, Kiambu County, Kenya. The correlation analysis found that dispute resolution reform was positively and significantly correlated with rental income tax compliance ( $r = .652$ ,  $p = .004$ ), highlighting that accessible and fair mechanisms for resolving tax disputes foster a favorable compliance environment. Taxpayers are more likely to participate voluntarily when they believe that the resolution process is impartial and supportive (Waweru, 2017). The regression model found that Dispute resolution reform had a positive and significant effect on rental income tax compliance ( $\beta = 0.099$ ,  $p = .020$ ). This implies that enhancing the fairness and accessibility of conflict resolution processes can influence compliance, albeit marginally. Studies confirm that a transparent mechanism for handling grievances fosters public trust and increases tax morale (Mugambi & Jagongo, 2019).

#### 5. Conclusion

The objective of the research was to establish the impact of dispute resolution reform on the rental income tax compliance among residential landlords in Ruaka Town, Kiambu County, Kenya. The outcomes reached the conclusion that the change in dispute resolution produced a positive and significant impact on compliance with the obligation to pay the rental income tax.

#### 6. Recommendations

The significant positive effect of dispute resolution reform suggests that the government should strengthen tax dispute mechanisms by ensuring fairness, transparency, and accessibility in conflict resolution processes. Future researchers could investigate the effects of attitude and perception, which are behavioral factors that might be analyzed to find their relative effect on the taxpayers in compliance with the rental income tax.

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