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Effect of Penalties on Turnover Tax Compliance Among Small and Medium Enterprise Traders in Limuru Town, Kiambu County

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Abstract

Compliance with turnover tax remains a concern in Kenya, as it greatly affects domestic revenue mobilisation and the sustainability of public financing. Despite the Kenya Revenue Authority's (KRA) continued efforts to address non-compliance bottlenecks, including the consistent use of penalties to deter evasion, many traders still face challenges with filing, accurate turnover declaration, and timely turnover tax payment. This study thus aimed to assess the effect of penalties on SME traders' compliance with turnover tax in Limuru Town, Kiambu County. The study was grounded in Economic Deterrence Theory and adopted an explanatory research design. The target population included 1345 SME traders in Limuru Town who are registered under the turnover tax regime. A sample of 308 was determined using Yamane's (1967) formula and selected through stratified random sampling to ensure representation across retail, hospitality, services, manufacturing, and agriculture sectors. Structured questionnaires were used to collect data, and SPSS (Statistical Package for Social Sciences) was used for analysis. Descriptive statistics, Pearson correlation and simple linear regression analysis were used to analyse the data. The results showed a statistically significant positive Pearson correlation between penalties and turnover tax compliance ($r = 0.672$). The regression analysis also showed a positive, statistically significant relationship between penalties and turnover tax compliance ($B = 0.351$, $\beta = 0.368$, $t = 5.661$, and $p < 0.001$). The results suggested that, controlling for other factors, a one-unit increase in penalties led to a 0.351-unit increase in turnover tax compliance among the sampled SME traders. The study concluded that penalties were an effective enforcement instrument for increasing turnover tax compliance among SME traders. The study recommended that KRA should continue applying penalties while ensuring that administration is consistent, transparent, and proportionate to the nature of the tax offence. It also called for improved communication to ensure SME traders understood applicable penalties and their turnover tax liability. The results support Economic Deterrence Theory, as higher consequences for non-compliance correlated with higher taxpayer compliance.

Keywords: *Penalties, turnover tax, tax compliance, small and medium enterprises, SME traders, tax enforcement, Limuru Town.*

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1. Introduction

Turnover tax compliance is a vital statutory obligation that directly affects domestic revenue mobilization. Tax compliance among small and medium-sized enterprises (SMEs) remains a global concern, as they account for a significant portion of economic activity while operating within diverse tax regulatory and administrative environments (Waskita & Ashari, 2025). Compliance behaviours include the timely registration, correct declaration of business income, timely filing of tax returns and the payment of taxes due (Lavic, 2023). Adem et al. (2024) note that taxpayers' knowledge of tax obligations, perceptions of fairness, administrative convenience, and tax enforcement factors all contribute to compliance levels. Research further shows that tax administrations worldwide have continued to improve practices and policies that encourage tax payment under simplified tax regimes while minimizing opportunities for under-declaration and non-payment (Waskita & Ashari, 2025).

In Africa, SMEs contribute greatly to employment creation, income generation, and economic development, making their tax compliance important for expanding the domestic revenue base. In many African countries, however, Mpofu (2023) highlights that informality, inadequate financial records, and low levels of tax awareness and capacity make it difficult for tax administrations to secure consistent compliance from small businesses. Consequently, tax administration has become more focused not only on educating taxpayers but also on implementing enforcement measures to promote voluntary compliance with tax obligations among businesses (Moore, 2023). Among these mechanisms, penalties are designed to increase the consequences of tax compliance failures, and therefore tip the scales in favour of fulfilling tax obligations in good time and in full (Moore, 2023).

In Kenya, turnover tax (TOT) is a simplified tax regime that allows qualifying small-scale businesses to pay tax based on turnover rather than taxable profits (Kaanzo, 2022). Thus, eligible businesses must correctly declare turnover, file returns within the time limits, and pay the corresponding tax to comply with TOT (Gwokyalya & Okumu, 2023). The Kenya Revenue Authority (KRA) uses several enforcement strategies to ensure taxpayers meet these obligations, including late-filing penalties, interest on unpaid tax, and late-payment penalties. Nyondo (2022) emphasizes that although penalties are intended to discourage non-compliance by making it more expensive to violate tax obligations, their actual impact on SME traders' compliance may differ based on the type and implementation of the sanctions.

The SME traders in Limuru Town, Kiambu County operate across retail, hospitality, services, manufacturing, and other business activities and are a significant part of the local commercial economy. Their compliance with TOT obligations is, therefore, important for effective tax administration and domestic revenue mobilisation. Empirically, however, the influence of penalties on TOT compliance among the small and medium traders in Limuru Town remains a concern. This study therefore aimed to assess the impact of penalties on compliance with turnover tax among small and medium enterprise traders in Limuru Town, Kiambu County.

1.1 Problem Statement

Ideally, the aim of Turnover Tax (TOT) is to ensure high and sustained compliance among eligible small and medium enterprises (SMEs) by accurately declaring their turnover, submitting tax returns on time, and paying the tax due on time (Kaanzo, 2022). The Kenya Revenue Authority (KRA) introduced a simplified TOT regime to ease compliance for qualifying businesses, with returns and payments due by the twentieth day of the following

month (Kaanzo, 2022). The regime also provides clear consequences for non-compliance, including a KSh 1,000 per month penalty for late filing and a 5% penalty for late payment.

In reality, compliance with TOT remains a concern even with these administrative and enforcement measures. This concern is evident in KRA's consistent inability to meet its targets. For instance, KRA recorded total revenue of KSh 2.166 trillion for the financial year 2022/23, falling short of the projected KSh 2.274 trillion by KSh 108 billion, or 95.3% (KRA, 2022/23). Studies on TOT compliance among SMEs in Kenya consistently show that the compliance rate remains below expectations (Ndirangu, 2022; Okuku, 2022). Continued non-compliance may reduce government revenues, lower the effectiveness of the simplified tax system, and increase penalties and difficulties in tax enforcement and recovery (Youde & Lim, 2023).

Available empirical studies, while offering key insights, produce inconsistent findings on the effect of penalties on tax compliance. For instance, Muhwa and Omboi (2023) found that penalties and interest had a positive and statistically significant effect on tax compliance among SMEs in Nairobi County. Likewise, Okuku (2022) found that penalties and fines had a positive and significant impact on tax compliance among SMEs in Embu County. However, most evidence has focused on tax compliance in general rather than TOT-specific compliance, and existing TOT studies have concentrated largely on Nairobi and other locations, paying little attention to Limuru Town. Therefore, a contextual and tax-specific empirical gap remains regarding how penalties affect TOT compliance among SME traders in Limuru Town. This study therefore aimed to determine whether penalties significantly affect SME traders' turnover tax compliance in Limuru Town, Kiambu County.

1.2 Purpose of the Study

This study aimed to assess the effect of penalties on turnover tax compliance among Small and Medium Enterprise Traders in Limuru Town, Kiambu County.

1.3 Hypothesis of the Study

H_{01}: Penalties have no statistically significant effect on turnover tax compliance among small and medium enterprise traders in Limuru Town, Kiambu County.

1.4 Significance of the Study

The findings are relevant to the Kenya Revenue Authority (KRA) because they offer insights into how penalties affect turnover tax compliance among small and medium enterprise traders in Limuru Town, Kiambu County. The findings help KRA identify whether penalties are effective in encouraging timely filing of tax returns, accurate declaration of turnover and turnover tax payments among eligible traders. The study also provides evidence on the difficulties SME traders face in tax compliance, which can help improve tax enforcement practices, tax education, and compliance administration. Additionally, the results are significant for policymakers designing policies that encourage sustainable tax compliance while considering SMEs' financial situation.

The study findings are also beneficial to SME traders, researchers and scholars. SME traders from Limuru Town gain insights into the value of timely payment and timely filing of turnover tax and the implications of late filing and payment. The results could encourage traders to invest in better record-keeping, ensure timely tax payments, and minimize exposure to tax penalties. The study also adds to the available empirical evidence on tax compliance and

enforcement in Kenya. It acts as a reference for future research on penalties, compliance with tax on turnover and other factors affecting the taxpayer behaviour of SMEs.

1.5 Scope of the Study

Conceptually, this study aimed to assess the effect of penalties on turnover tax compliance among SMEs in Limuru Town, Kiambu County, focusing on penalties as the independent variable and turnover tax compliance as the dependent variable. Contextually, the study focused on SME traders operating under the turnover tax regime in Limuru Town, Kiambu County. The study's target population included 1345 registered SME traders under the turnover tax regime in Limuru Town. The study was therefore limited to traders within this geographical and tax-regime context and excluded SMEs outside Limuru Town or businesses subject to other tax regimes.

Methodologically, the study used an explanatory research design. It used Yamane's (1967) formula to calculate a sample size of 308 respondents, selected through stratified random sampling to ensure equal representation across all SME categories. The study obtained primary data through structured questionnaires administered to the sampled respondents. The study analyzed the collected data using descriptive and inferential statistics, including frequencies, percentages, means, standard deviations, correlation analysis, and regression analysis, with the regression model used to test the effect of penalties on turnover tax compliance. The study period was 6 months, from May 2026 to October 2026.

2. Literature Review

This section reviews relevant theoretical and empirical literature on the effect of penalties on SME traders' tax compliance. It reviews the theoretical frameworks that underpin the study, empirical findings on penalties and tax compliance, and gaps in the existing literature that justify the present study.

2.1 Theoretical Review

The theory of economic deterrence was first formulated by Allingham and Sandmo (1972) and is an extension of the economic theory of crime proposed by Becker (1968), which states that people make rational choices based on the possibility of getting caught and the punishment they face for their illegal behaviour (Abramovaite et al., 2023). This theory suggests that if the penalties, costs, and risks of tax evasion outweigh the perceived benefits, taxpayers will abide by tax laws. The theory assumes taxpayers are rational agents who weigh the potential benefits of evasion against the certainty of audit and sanctions (Abramovaite et al., 2023). It suggests that the risk of being caught and the severity of punishment are directly related to compliance, and that higher risk and harsher punishment would reduce non-compliance. Within Economic Deterrence Theory, compliance reflects a cost–benefit calculation and is therefore useful for research on enforcement strategies such as penalties and audits.

Economic Deterrence Theory has been extensively used in tax research to examine the impact of enforcement measures on compliance results. For instance, a recent study by Muhwa and Omboi (2023) was founded on economic deterrence theory and empirically examined the effectiveness of penalties and audits on tax compliance among SMEs, and found that the more effective penalties and audits were, the greater the tax compliance behaviour. Other researchers, including Ya'u et al. (2023), have used economic deterrence theory to study tax evasion in specific sectors and have found strong correlations between enforcement variables

and tax outcomes. Further, field experiments in different settings have shown that messages designed to deter and increase audit risk can drive measurable improvements in voluntary compliance (Dong et al., 2025). Despite the increasing development of behavioural insights and their impact on the theory's assumptions, the theory has remained a key instrument in explaining the relationship between enforcement mechanisms and taxpayer choices in modern research. Studies consistently support deterrence logic as a key element in interpreting compliance or payment evasion.

Economic Deterrence Theory was highly relevant to this study and served as the main theoretical framework, as it supported research on the effect of penalties as an enforcement tool on turnover tax compliance among SME traders. The theory directly supports the hypothesis that penalties increase the perceived costs of non-compliance, ultimately enhancing compliance with tax obligations. This is especially important in settings where turnover tax regimes are strictly enforced through fines and sanctions, such as Limuru Town and similar setups. The study's deterrence logic provides a strong framework for understanding and interpreting the impact of penalties on SMEs' compliance decisions. The theory also provides an explanation for variations in compliance according to the degree of enforcement stringency and provides a lens to analyse survey or administrative data relating to the impacts of penalties.

2.2 Empirical Review

This section reviews empirical studies on the relationship between penalties and turnover tax compliance, with an emphasis on evidence from global, African, and Kenyan contexts. It reviews the results, methodology, and context of previous studies to identify existing evidence and gaps that justify the current study.

2.2.1 Penalties and Turnover Tax Compliance

Several empirical studies have examined the relationship between tax penalties and tax compliance globally, with most findings supporting the deterrent effect of tax penalties. Ali et al. (2020) examined tax compliance among SMEs in Selangor, Malaysia and found that tax penalties significantly and positively affected compliance. The study found that penalty severity and enforcement were associated with taxpayers' willingness to file returns and pay taxes on time. In the same way, Wicaksono (2024) conducted research targeting tax behaviour among restaurants in Indonesia and found that tax sanctions such as fines and interest rates had an overwhelming impact on increasing the level of compliance among taxpayers. The results support the economic deterrence view, which posits that the cost of non-compliance rises with the penalties imposed, thereby raising compliance behavior among taxpayers. However, both Ali et al. (2020) and Wicaksono (2024) caution that excessive enforcement measures, such as over-implementing penalties, can generate fear and resentment, which can result in resistance and evasion of the rules.

In the African setting, evidence also shows a strong correlation between penalties and tax compliance, though findings are sometimes mixed. For example, Gwokyalya and Okumu (2023) reported that presumptive tax penalties applied consistently and clearly to taxpayers led to better compliance in their study of small businesses in Uganda. The authors explained that predictable enforcement mechanisms lowered the uncertainty and prevented intentional under-reporting of turnover. Other research in Africa, however, indicates that penalties alone are ineffective when informality is high and follow-up is low (Hardy, 2021; Lund & Sarin, 2021). For example, Lund and Sarin (2021) noted that taxpayers may feel penalties are unfair and

unrealistic, particularly when they feel tax authorities are not transparent or meaningfully engaging with taxpayers. This implies that while penalties matter, their effectiveness in Africa depends on institutional credibility and administrative fairness.

Empirical studies in Kenya show similar patterns in how penalties influence turnover tax compliance. A study by Muthinji (2022) on tax compliance among MSMEs in Nairobi found that enforcement measures, including penalties, positively affected tax compliance among micro, small, and medium enterprises in Kenya. The study showed that the more SMEs were informed about penalties for late filing and non-payment, the more likely they were to comply. Similarly, Samo (2020), in his research on SMEs in Mombasa, noted that penalties strongly incentivized compliance, especially when SMEs were confident they would be penalized for non-compliance. However, both studies also highlighted that many SMEs were not fully aware of the tax provisions; therefore, penalties were not fully effective. This implies that, in the Kenyan context, penalties can encourage compliance, but their effect is stronger when used alongside taxpayer education and supportive administrative measures.

2.3 Research Gaps

Several gaps in the reviewed empirical literature warranted the current study. First, a contextual gap existed because previous Kenyan evidence on turnover tax compliance focused on locations such as Roysambu and Mombasa, with limited evidence from Limuru Town, Kiambu County. For instance, Muthinji (2022) analyzed the determinants of MSMEs' attitude to turnover tax compliance in Nairobi and found that economic, political, and psychological factors significantly affect MSMEs' attitudes toward turnover tax compliance, but did not specifically isolate penalties as the explanatory variable. Likewise, Samo (2020) studied compliance with turnover tax of SMEs in Mombasa North, Kenya, with specific attention to tax rate, tax education and tax laws rather than penalties. Second, a conceptual gap exists in the literature, as most studies used a general measure of the determinants of turnover tax compliance and did not explicitly identify the impact of penalties as a separate compliance tool. Third, the reviewed studies used varying designs, populations, sampling methods, and analytical tools, making it difficult to extrapolate the results to SME traders in Limuru Town. Lastly, an empirical gap remains: previous evidence shows how different tax administration factors relate to tax compliance, but there is limited location-specific evidence on the impact of penalties on tax compliance among registered SME traders in Limuru Town. This study fills these contextual, conceptual, methodological, and empirical gaps by investigating the effect of penalties on turnover tax compliance among SME traders in Limuru Town, Kiambu County.

2.5 Conceptual Framework

The conceptual framework visually outlines the hypothesized relationship between the independent variable (penalties) and the dependent variable (turnover tax compliance). It provides a framework of the expected impact of penalties on the compliance behaviour of SME traders in Limuru Town, Kiambu County.

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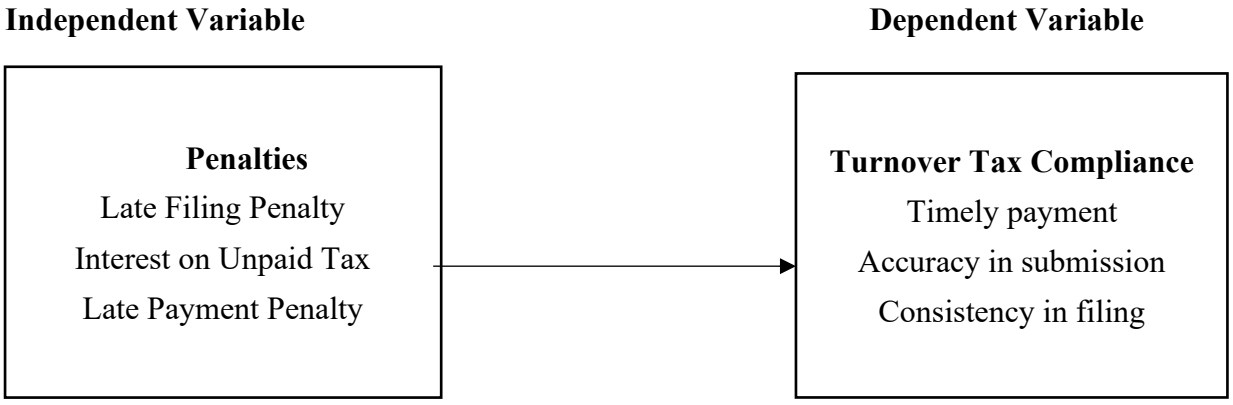


Figure 1: Conceptual Framework

3. Methodology

3.1 Research Design

The study adopted an explanatory research design to assess the effect of penalties on turnover tax compliance among small and medium traders in Limuru town, Kiambu County. The design was suitable because it allowed the study to go beyond describing the variables and determine whether penalties had a statistically significant effect on turnover tax compliance (Ansari et al., 2022). It also made it easier to apply inferential statistical methods to test the study hypothesis and determine the direction and strength of the relationship between penalties and turnover tax compliance.

3.2 Target Population

The study targeted 1,345 registered SME traders under the turnover tax regime in Limuru Town, Kiambu County. The population comprised traders from five key business categories: retail, hospitality, services, manufacturing, and agriculture. These traders constituted the relevant population because they were directly subject to turnover tax obligations and the penalties associated with non-compliance. The population distribution was derived from Kenya Revenue Authority (KRA) records (2026).

3.3 Sample Size and Sampling Technique

The study selected 308 respondents from the target population of 1,345 SME traders. The sample size was calculated using Yamane's (1967) formula with a 5% margin of error, and stratified random sampling was used to select respondents from their respective categories. The sample size was proportionately distributed as follows: retail 49 respondents, hospitality 80 respondents, services 74 respondents, manufacturing 65 respondents, and agriculture 40 respondents, as shown in Table 1. This methodology ensured each sector was represented in proportion to its share of the target population and allowed selection of eligible traders.

Table 1: Sample Size Distribution

Sector	Target population	Sample Allocation	Size	Sample Percentage
Retail	211	49		16%
Hospitality	362	80		26%
Services	319	74		24%
Manufacturing	282	65		21%
Agriculture	171	40		13%
Total	**1345**	**308**		**100**

3.4 Data Collection Instrument

This study used a structured questionnaire to collect data. Most questions were closed-ended and measured on a five-point Likert scale, with items developed to measure penalties and turnover tax compliance based on the study objectives and conceptual framework. This structured format ensured uniformity in the information obtained from respondents and made quantitative analysis of the study variables easier.

3.5 Data Collection Procedure

The researcher collected the data after obtaining proper authorization and ethical clearance from the relevant institutions, including an approval letter from NACOSTI. The researcher administered the questionnaires to selected SME traders, briefed respondents on the study's purpose, and informed them that participation was voluntary and that the data collected would be kept confidential and used only for academic purposes. Questionnaires were delivered by hand and/or electronically as preferred by the respondent. The team then checked questionnaires for consistency and completeness and prepared them for analysis. The data collection process took 14 days.

3.6 Pilot Testing

A pilot study was conducted with 30 SME traders selected from Roysambu Sub-county, Nairobi County, outside the main study area. The pilot participants' characteristics were comparable to those of the SME traders targeted in Limuru Town. A pilot test was conducted to evaluate the clarity, relevance and suitability of the items of the questionnaire and to detect any weaknesses in the questionnaire before the main data collection (Hossan et al., 2025). The pilot study results were used to fine-tune the instrument and improve its reliability and clarity.

Validity of the Research Instrument

The questionnaire's content and face validity were evaluated to determine whether it was suitable for measuring the intended constructs. The researcher strengthened content validity by linking the questionnaire items to the study's goals, research questions, conceptual framework, and indicators of penalties and turnover tax compliance. The research supervisor and relevant

taxation and research methodology experts also reviewed the questionnaire, and the researcher incorporated their recommendations to improve its relevance, clarity, and comprehensiveness.

Reliability of the Research Instrument

The reliability of the research instrument was determined using Cronbach's alpha coefficient. The test measured the internal consistency of the questionnaire items measuring penalties and turnover tax compliance. A Cronbach's Alpha coefficient of 0.70 or higher was considered acceptable, indicating adequate internal consistency for the main study.

3.7 Data Analysis and Presentation

Coding, cleaning, and analysis of the collected data were done through the SPSS (Statistical Package for the Social Sciences) software, Version 30. The data collected in relation to the study variables were summarised using descriptive statistics (frequencies, percentages, means and standard deviations). Inferential analysis techniques, including Pearson correlation analysis and linear regression analysis, were used to determine the relationship between penalties and turnover tax compliance. The hypothesis was tested at the 5% level of significance, and the results were presented in tables and charts for easier interpretation.

3.8 Ethical Considerations

This study followed ethical principles to safeguard participants' rights and dignity. Informed consent was obtained, and a clear explanation of the purpose of the study, rights, and voluntary participation of respondents was provided before commencing the data collection process. The researchers ensured respondents' anonymity and confidentiality by not collecting any personal identifiers, and they did not share responses for other purposes. Participants could also withdraw at any time without negative consequences. The researchers also obtained ethical clearance from the National Commission for Science, Technology and Innovation (NACOSTI) to ensure adherence to ethical guidelines and standards.

4. Findings

This section presents the study results. The results are reported based on the study objectives and data collected from sampled respondents.

4.1 Reliability Test Results

The reliability of the research tool was assessed using the internal consistency of the questionnaire items with Cronbach's alpha coefficient. Izah et al. (2023) suggested that tools with a Cronbach's Alpha coefficient of 0.70 or higher are acceptable, 0.80 or higher are good, and 0.90 or higher are excellent. We conducted a reliability analysis for each study variable based on responses from the pilot study.

Table 2 showed that all study constructs had Cronbach's alpha coefficients greater than the recommended 0.70, indicating good internal consistency of the questionnaire items. Penalties had a reliability coefficient of 0.823 and that of Turnover Tax Compliance was 0.806, all of which are within the range considered to be "good." The overall Cronbach's alpha was 0.815, further confirming that the research instrument was reliable and appropriate for collecting data for the main study. Therefore, no items were dropped or revised because each construct met the minimum acceptable reliability level.

Table 2: Reliability Test Results

Variable	Cronbach's Alpha	Number of Items	Comment
Penalties	0.823	4	Good Reliability
Turnover Tax Compliance	0.806	3	Good Reliability
Overall	**0.815**	**19**	**Good Reliability**

4.2 Response Rate

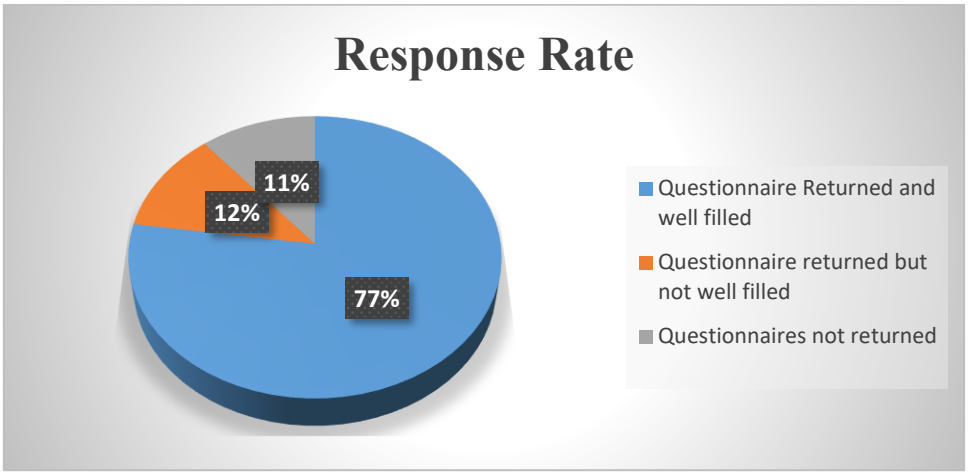


Figure 1: Response Rate

A total of 308 questionnaires were distributed to the sampled SME traders in Limuru Town as presented in Figure 1 and Table 2. As shown in the table, 238 questionnaires (77.3%) were correctly completed and returned, making them suitable for analysis. An additional 36 questionnaires (11.7%) were returned but inadequately completed and therefore excluded from the analysis because of missing or inconsistent responses. Moreover, 34 questionnaires (11.0%) were not returned. The effective response rate was therefore 77.3%, which was considered good for further statistical analysis and higher than the recommended minimum acceptable rate for survey research, indicating that the study results could be trusted and were representative of the target population.

Table 3: Response Rate

	Number	Percentage
Questionnaire returned and well filled	238	77.3%
Questionnaire returned but not well filled	36	11.7%
Questionnaires not returned	34	11%
Total	**308**	**100%**

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4.3 Descriptive Statistics

This section presents the descriptive statistics for the study variables. The analysis summarizes respondents' perceptions regarding penalties and turnover tax compliance using frequencies, percentages, means, and standard deviations. The average scores reflect the overall level of agreement with each statement, and the standard deviations indicate the variation in respondents' opinions. The descriptive results provide an overview of the study variables and serve as the basis for subsequent inferential statistical analysis.

4.3.1 Descriptive Statistics of Penalties

Table 4 shows that respondents generally agreed that penalties effectively promote turnover tax compliance among SMEs in Limuru Town, as reflected in the composite mean score of 4.06. The relatively high mean scores across all statements indicate that most respondents believe penalties effectively deter tax non-compliance. Specifically, the highest mean score of 4.18 for the statement that penalties generally ensure taxpayers fulfill their tax obligations shows that SME traders believe penalties encourage them to meet their tax obligations. Similarly, the high level of awareness of penalties for late filing (Mean = 4.12) suggests that most traders understand the consequences of failing to comply with turnover tax requirements, which may have a positive effect on their compliance behaviour.

Respondents' opinions on the effectiveness of penalties as an enforcement measure were fairly consistent, as reflected in the relatively low standard deviations (0.79 to 0.94). This limited variation indicates that SME traders share a similar perception of penalties as a compliance mechanism, regardless of differences in business characteristics. The results also suggest that while financial penalties are generally perceived as effective in discouraging non-compliance, their effectiveness may depend on taxpayers' knowledge and understanding of the penalty provisions. Overall, the descriptive results preliminarily support the view that penalties are an important enforcement tool that can improve turnover tax compliance and warrant further investigation using inferential statistical analysis to assess the magnitude and significance of their effect on compliance.

Table 4: Descriptive Statistics for Penalties

Statement	N	Mean	Std. Dev.
I am aware of the penalties for late filing of taxes.	238	4.12	0.81
The interest charged on unpaid turnover tax effectively discourages non-compliance.	238	3.89	0.94
Penalties for late payment are effective in encouraging timely tax payments.	238	4.05	0.87
Generally, penalties as an enforcement measure are effective in ensuring turnover tax compliance.	238	4.18	0.79
Average	**238**	**4.06**	**0.85**

4.3.2 Descriptive Statistics of Turnover Tax Compliance

The results in Table 5 suggest that respondents generally agreed they meet turnover tax requirements, as shown by the composite mean score of 3.70. This indicates a moderate to relatively high degree of turnover tax compliance among SME traders in Limuru Town. The highest mean score (3.82) was recorded for the statement on accurately submitting the turnover tax owed to KRA, implying that respondents place considerable importance on correctly declaring their tax liabilities. This finding reflects the increased awareness of the repercussions of inaccurate declarations, including penalties, audits, and other enforcement measures by the Kenya Revenue Authority.

Although overall compliance was positive, the statement on consistently filing turnover tax returns without missing deadlines had the lowest mean score (3.59) and the highest standard deviation (0.96). This suggests that many SME traders still struggle with timely filing, with respondents holding relatively diverse views on their ability to consistently meet filing deadlines. The finding suggests that while many businesses strive to comply with turnover tax requirements, practical issues like poor record-keeping, limited understanding of filing procedures, cash flow constraints, or competing business needs may affect timely compliance. However, the composite mean above the neutral point shows that most of the respondents consider themselves good taxpayers, but there is room for improvement, especially in the timely and regular submission of turnover tax returns. These findings provide an important foundation for inferential analyses examining the effect of penalties on turnover tax compliance.

Table 5: Descriptive Findings on Turnover Tax Compliance

Statement	N	Mean	Std. Dev.
I always pay turnover tax on time.	238	3.68	0.92
I accurately submit all the turnover tax owed to KRA.	238	3.82	0.87
I consistently file my turnover tax returns on time.	238	3.59	0.96
Average	**238**	**3.70**	**0.92**

4.4 Correlation Analysis

The correlation results in Table 6 indicated a positive and significant relationship between penalties and SME traders' turnover tax compliance in Limuru town. The Pearson correlation coefficient ($r = 0.672$) indicates a relatively strong positive association between penalties and turnover tax compliance. This meant that higher penalties were associated with higher turnover tax compliance among the SME traders surveyed. The correlation was statistically significant at the 5% level ($p < .05$). The results indicated that penalties were linked to greater compliance with turnover tax obligations, providing preliminary evidence for the hypothesis that penalties affect turnover tax compliance.

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Table 6: Pearson Correlation Matrix

Variables	Penalties	Turnover Tax Compliance
Penalties	1	
Turnover Tax Compliance	.672*	1

4.5 Regression Analysis

Table 7 shows that penalties had a positive and statistically significant effect on turnover tax compliance among SME traders in Limuru Town. Penalties had a coefficient of B = 0.351, a standard error of 0.062, a standardized beta of 0.368, and a statistically significant t-value of 5.661 ($p < 0.001$). This implies that a one-unit increase in penalties is associated with a 0.351-unit increase in turnover tax compliance, holding other factors constant. Further, the constant of 0.814 indicates that, when penalties are zero, the estimated turnover tax compliance is 0.814 units. The positive, statistically significant coefficient suggests that higher penalties are linked to higher turnover tax compliance.

Table 7: Regression Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.814	0.227	–	3.586	0.000
Penalties	0.351	0.062	0.368	5.661	0.000
Dependent Variable: Turnover Tax Compliance					

4.6 Discussion

The results showed that penalties positively and significantly affect turnover tax compliance among SMEs in Limuru town ($\beta = 0.368$, $p < 0.001$). This suggests that SMEs are more willing to comply with turnover tax obligations when they face financial penalties for non-compliance. In particular, the regression results indicated that, holding other factors constant, a one-unit increase in penalties corresponds to a 0.368-unit increase in turnover tax compliance. These results align with the Economic Deterrence Theory proposed by Becker (1968), which assumes taxpayers act rationally and make decisions based on the expected costs and benefits of compliance and non-compliance. The theory holds that taxpayers are more inclined to comply with the tax laws if the expected costs of not paying taxes, including fines, interest charges and penalties, exceed the possible gains of evasion. The results thus confirm that a penalty is an effective deterrence mechanism that can impact tax behaviour and encourage voluntary compliance by SMEs.

The study results also align with the empirical evidence reviewed in the literature review section. Globally, the results are similar to those of Ali et al. (2020), who reported that tax penalties promote tax compliance among SMEs in Selangor, Malaysia, by increasing taxpayers' perceptions of the costs of non-compliance. Likewise, the results align with Wicaksono (2024),

who studied Indonesia and concluded that tax sanctions, such as fines and interest rates, positively affect taxpayer compliance by motivating taxpayers to comply.

In the African context, these findings align with Gwokyalya and Okumu (2023), who found that regularly imposing tax penalties increased tax compliance among small businesses in Uganda by reducing uncertainty and intentional under-reporting of turnover. The results, however, differ from those of Hardy (2021), who contended that penalties alone might not be very effective in settings with weak tax administration, low institutional trust, and high informality, and those of Lund and Sarin (2021), who suggested that failing to guarantee fair play in tax collection may lead to the erosion of compliance. These contrasting results suggest that while penalties are an effective enforcement tool, their effectiveness may depend on the institutional contexts in which they are implemented.

The results further support evidence from the Kenyan context. They are consistent with Muthinji (2022), who revealed that micro, small and medium enterprises were more likely to comply with tax regulations when they perceived that non-compliance would result to penalties. Similarly, the findings corroborate Samo's (2020) study, which concluded that penalties can influence SMEs' compliance with turnover tax provisions in Mombasa when taxpayers believe detection and punishment are likely. However, both Muthinji (2022) and Samo (2020) noted that penalties are more effective when taxpayers have adequate tax knowledge. The findings generally showed that penalties are among the best and most effective methods for improving turnover tax compliance among SMEs in Limuru Town, supporting the assertions of the Economic Deterrence Theory and the growing empirical literature that well-designed and well-enforced penalties can lead to better voluntary tax compliance.

5. Conclusion

The study concludes that penalties have a positive and significant effect on turnover tax compliance among SME traders in Limuru Town, Kiambu County. The results showed that an increase in penalties also led to an increase in compliance with turnover tax, indicating that penalties played an important role in encouraging SME traders to fulfil their turnover tax obligations. Specifically, the regression results indicated that penalties had a positive relationship with turnover tax compliance, and the relationship was statistically significant at the 5% significance level, with a coefficient of 0.351. The study therefore established that penalties were an important enforcement instrument in enhancing turnover tax compliance among SME traders in the study area.

6. Recommendations

The study further recommends that the Kenya Revenue Authority (KRA) should maintain and strengthen penalties as an effective enforcement tool to encourage SME traders to comply with their turnover tax obligations. However, penalties ought to be applied in a consistent, clear and appropriate manner, taking into account the extent and nature of non-compliance without unnecessarily burdening small businesses. KRA should also improve communication by clearly explaining to SME traders which penalties apply for late filing and late payment of turnover tax, as well as other violations. In turn, SME managers and business owners should keep appropriate business records, keep track of their turnover tax liabilities, and ensure timely filing and payment to avoid unnecessary penalties.

From a policy perspective, the study recommends that tax authorities and policymakers should develop enforcement policies that provide clear, predictable, and consistently applied penalties for turnover tax violations. The results indicated that penalties could be an effective component of tax administration when taxpayers understand their obligations and the consequences of non-compliance. Theoretically, the results supported the Economic Deterrence Theory, which asserts that taxpayers are more likely to comply when the potential expenses of non-compliance are high. Thus, the finding that penalties have a significant positive effect on turnover tax compliance provides empirical support for applying deterrence principles to explain taxpayer behavior among SME traders.

The study also recommends that future research examine other determinants of turnover tax compliance among SME traders, such as taxpayer education, tax administration, perceived fairness, digital tax systems, and tax knowledge. Further research is also warranted on how business size, business age, and other sector-specific variables influence the relationship between penalties and turnover tax compliance. Since this study was carried out in Limuru Town, further studies should be conducted in other towns and counties across Kenya to determine whether the results are consistent across different business and socio-economic settings. Future research could also use longitudinal designs to determine how the impact of penalties on turnover tax compliance changes over time.

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