

**THE EFFECTS OF TAXES ON THE PERFORMANCE OF SMES IN NSUUBE-KAUGA  
PARISH, MUKONO TC DIVISION**

**VICTORIA NABUKENYA**

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


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**DECLARATION**

I declare that this research report is my original work and has not been submitted to any institution of learning.

Signature...  .....

Date 07/09/2023 .....

NABUKENYA VICTORIA

S19B33/467

APPROVAL

This research report has been done under my supervision and is now ready for submission with my approval.

Signature.....~~Handwritten signature~~.....

Date ..... 07/09/2023 .....

Name: MR. AGUME ANTHONY KABISYAKI

## **DEDICATION**

I dedicate this research to my family especially my mum Mrs. Nagawa Linda who advised, supported and mentored me throughout my education up to university level. Above all, I thank God for guidance and provision towards completion of this dissertation.

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I am greatly indebted to Mr. Agume Anthony Kabisyaki |

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## ABSTRACT

The study sought to investigate the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division. The study was guided by three objectives: examining the relationship between tax rates and the performance of SMEs, establishing the relationship between tax incentives and the performance of SMEs and examining the relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division

The study was carried out using explanatory research design where quantitative research approach was utilized. Stratified sampling method was used to get a sample of 80 respondents who were SME owners and managers of the selected businesses dealing in segmented businesses and assorted merchandize in Kauga village, Nsuube-Kauga Parish, Mukono TC Division and these responded to the questionnaires that were used to collect data.

From the study findings, it was revealed that tax policies play a crucial role in shaping SMEs' growth and viability. The high agreement among respondents on the clarity of tax rates and the awareness of SMEs regarding tax payment procedures is promising. However, the study also highlights significant concerns, with many SME owners perceiving taxes as burdensome, especially due to their regressive nature, which negatively affects revenue bases. Furthermore, the lack of perceived tax incentives for SMEs hinders their potential for growth and expansion in the area. In conclusion, the study highlights the importance of tax compliance for SMEs' success. SME owners who consistently file returns, pay taxes on time, and adhere to tax regulations demonstrate a positive correlation with improved SME performance.

Finally, the study proposed a comprehensive set of recommendations to bolster the growth and ease the tax burden on small and medium-sized enterprises (SMEs). These include simplifying tax policies, introducing targeted tax incentives, enhancing tax education programs, reforming regressive tax measures, fostering collaboration between tax authorities and SMEs, conducting regular policy evaluations, and establishing a dedicated tax ombudsman for SMEs. By streamlining taxes, providing incentives, educating SMEs, and promoting cooperation, policymakers can create a supportive environment that encourages SME growth, innovation, and compliance while addressing their unique challenges.

# CHAPTER ONE

## INTRODUCTION

### 1.0 Introduction

The study was about the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division. This chapter presents the background of the study, statement of the problem, purpose of the study, objectives of the study, research questions, scope of the study, significant of the study and conceptual framework.

### 1.1 Background of the study

A tax is a compulsory levy by government through its agencies on the income, consumption and capital of its subjects. These levies are made on personal income such as salaries, business profit, interest, dividend, discount or royalties to obtain revenue. It is levied against company profit, petroleum profit, capital gains and capital transfer (Bello et al., 2013). Therefore, taxation is a compulsory payment or transfer of resources from private to public sector levied on the basis of the determined criterion and without reference to specific benefits received in order to accomplish some of the nation's economic and social objectives. Taxation is primarily aimed at generating revenue for government in order to cater for its expenditure (McIntyre and Dallago 2013).

Globally, taxes have greatly affected the way economies perform regardless of the political and social difference among countries worldwide (Oboh et al., 2012). According to OECD, "taxes are defined as a compulsory, unrequited payments to a general government." These taxes are unreciprocated whereby the welfares received from the government as a result of paying taxes is not usually commensurate to payments tax payers pay (OECD, 2016). Economists believe that smaller companies usually have small resources so they usually direct these limited resources towards tax compliance which would have been used for reinvestment and facilitating future growth. Therefore, such a tax system puts a lot of pressure on the small tax payers whereby both small and large companies face the same tax rates as well as compliance costs (Tomlin, 2018).

Small and Medium Enterprises are an important force for economic development and industrialization in poor countries (Helmsing and Kolstee 2013; Mead and Liedholm 2018;

McIntyre and Dallago 2013). It is increasingly recognized that these enterprises contribute substantially to job creation, economic growth and poverty alleviation. The 2005 World Development Report suggests that creating “sustainable jobs and opportunities for micro entrepreneurs are the key pathways out of poverty for poor people” (World Bank, 2014).

The development of small and medium enterprises is greatly affected by the level of taxation, its administration and compliance: the higher the tax rate is, or the greater the efforts to fulfill taxation requirements are, as well as to check how those requirements are met, the lower the initiatives are for SMEs to perform well. Therefore, maintaining the tricky balance between tax rate, compliance costs, tax administrating and economic development should be a main goal of every tax policy (Chu, Kara & Benzing, 2018).

Studies about taxation of SMEs in OECD and G20 countries finds that rather than being neutral in their impact on SMEs and their decisions, tax systems often provide incentives for SMEs to incorporate, and to distribute income in the form of capital, particularly in the form of capital gains, which is often lower-taxed (Yaobin, 2017). In addition, some tax systems can disproportionately affect SMEs relative to large enterprises, to the extent that they treat profits and losses asymmetrically, have a bias towards debt over corporate equity, and impose relatively high compliance costs. Governments take many measures to reduce these impacts, providing tax preferences and simplification measures targeted at SMEs (Holban, 2017).

In many highly developed countries a great share of production is manufactured by small and medium enterprises (SMEs) an important part of their market economies. For instance, the portion of SMEs in GDP of Great Britain is 50-53%; of Germany: 50-54%, of USA: 52-55%; of Italy: 57-60%; of France: 63-67% (Small Business in Ukraine, 2017). Consequently, up to 50-60 per cent of government revenues depend on the SME sector (Small Business in Ukraine, 2017). Thus, the higher is the share of small and medium businesses is in an economy, the higher the productivity that can be potentially realized with the SME sector.

In Africa, developing countries like Tanzania has taken a number of measures to promote the growth of private sector and Small and Medium Enterprises (SMEs). In Tanzania, SMEs were estimated to account for a significant share of Gross Domestic Product (GDP) of more than 30% (IPP Media, 2012). The government of Tanzania formulates and implements various tax policies

aimed at increasing job opportunities, development of infrastructure as well as income generation through the creation of new SMEs and improving the performance and competitiveness of existing one (Oludele & Emilie, 2012).

More so, many small firms in Africa, like in Nigeria, choose to remain in the informal sector because the perceived benefits outweigh the perceived costs. Firms rarely see their tax contributions at work and the compliance costs are high, thus discouraging compliance. The government is also discouraged from collecting taxes from small firms, because the cost of monitoring and collecting taxes from small businesses by revenue authorities, whose resources are usually scarce, sometimes outweighs the revenues generated by small businesses (Stern and Barbour 2015).

The Ugandan economy is supported mainly by MSMEs contributing about 90% of the private sector production. SMEs are the prime source of new jobs and play a crucial role in income generation, especially for the poor. In Uganda a considerable fraction of the businesses are sole traders operating small scale business, locally owned and managed by individuals or families and often with very few employees working at a single location (Bank of Uganda, 2022). Taxation in Uganda is based on system that existed in Britain as it was a British colony. This also applied to other colonies elsewhere and for East Africa, one tax system operated under British administration. SMEs in Uganda often face difficulties when dealing with tax matters. It would be rare indeed not to hear complaints about the complexity and/or ambiguity of the tax laws, high tax rates, and the lack of an integrated fiscal strategy that takes social taxes, and local taxes and fees into account when determining the overall tax burden placed on the business community in Uganda (Baurer, 2015).

## **1.2 Problem statement**

Although there is a general perception that taxes are an important source of fund for development of the economy and provision of social services, the problems faced are in the area of negative relationship between taxes and the business' ability to sustain itself and to expand especially with SMEs. The mortality rate of small and medium enterprises which make up 90% of the economy is very high.

According to Ademola (2014), in Uganda, 80% of small businesses collapse within seven years of its establishment. Among the factors responsible for these untimely close-ups are tax related issues, ranging from taxations to enormous tax burdens brought about by tax rates which seem to be taking an upward trend, complex tax regulations and lack of proper enlightenment or education about tax related issues. This has greatly affected the performance of SMEs as some of these businesses cannot afford paying such taxes which are high compared to their revenues leading to increased tax avoidance and hence stagnant or decline in the development of these SMEs (Atijosan, 2014). It is therefore against this background that the researcher sought to investigate the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.

### **1.3 General objective of the study**

The general objective of the study was to investigate the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.

### **1.4 Specific objectives of the study**

This study was guided by the following specific research objectives:

- i. To examine the relationship between tax rates and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.
- ii. To establish the relationship between tax incentives and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.
- iii. To examine the relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.

### **1.5 Research questions**

The study aimed at answering the following questions:

- i. What is the relationship between tax rates and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division?
- ii. What are the relationship between tax incentives and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division?

- iii. What is the relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division?

## **1.6 Scope of the study**

### **1.6.1 Content Scope**

The study focused on investigating the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division, Mukono Municipality. It was limited to; examining the relationship between tax rates and the performance of SMEs, establishing the relationship between tax incentives and the performance of SMEs and examining the relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division

### **1.6.2 Time scope**

The review of the report and documents focused at a range of 2011-2021, and the research data was focused on a time range of five years (2018 to 2022).

### **1.6.3 Geographical scope**

This study was carried out in different SMEs located in Nsuube-Kauga Parish, Mukono TC Division, Mukono district of Central region of Uganda. It was chosen because it is the second largest Municipality in Uganda in terms of population meaning that there are a lot of SMEs established in this area facing a challenge of taxation that are hindering the performance of their businesses.

## **1.7 Significance of the study**

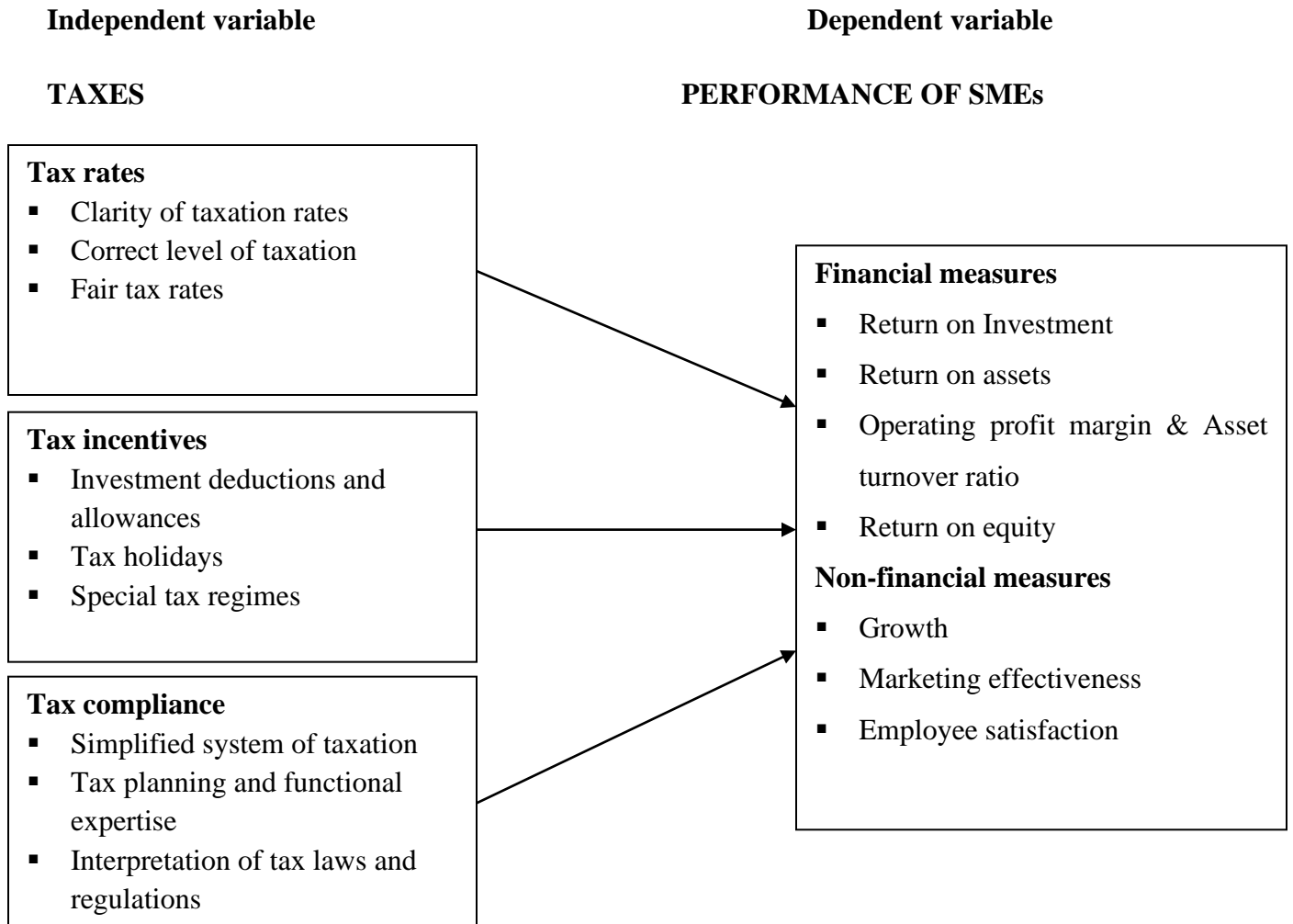
To scholars and future researchers, the findings of the study are expected to contribute to the existing literature about taxes and their influence on SMEs and the economy as a whole.

To the tax authority and government, the study will guide them in adjusting tax policies so that they suit requirements of small and medium businesses.

The accomplishment of the study will enable the researcher to acquire hands on skills about processing of research work and data analysis. This proficiency will enable the researcher to handle such related work with a lot of precision and proficiency.

## 1.8 Conceptual framework

**Figure 1: Conceptual framework**



**Source:**Adopted from(Tusubira & Nkote, 2013;Vicari, 2015;) and modified by the researcher 2023.

The conceptual framework above shows the relationship between the independent variable (tax rates) and the dependent variable (performance of SMEs). In this study, taxes are measured using tax rates which encompasses; clarity of taxation rates, correct level of taxation and fair tax rates. Followed by tax incentives which encompasses; investment deductions and allowances, tax holidays and special tax regimes and lastly it also includes tax compliance which encompasses; simplified system of taxation, tax planning and functional expertise and interpretation of tax laws

and regulations. On the other hand, the performance of SMEs is measured using financial measures and non-financial measures which include; return on Investment, return on assets, operating profit margin & Asset turnover ratio, return on equity, growth, marketing effectiveness and employee satisfaction.

## CHAPTER TWO

### LITERATURE REVIEW

#### 2.0 Introduction

This chapter outlines the various schools of thought revolving around taxes and performance of SMEs. This chapter identified the various theories put across by various scholars in relation to taxation. For the research questions identified in chapter one, the researcher highlighted the findings of different authors, on the impact of taxation on the development of SMEs.

#### 2.1 Concept of Taxes

According to Atkeson & Burstein (2005), taxation refers to the means by which governments finance their expenditure by imposing charges on citizens and corporate entities. Governments use taxation to encourage or discourage certain economic decisions. For example, reduction in taxable personal (or household) income by the amount paid as interest on home mortgage loans results in greater construction activity, and generates more jobs. See also taxation principles.

On the other hand, Chen & Scott (2004) define taxation as the act of a taxing authority actually levying tax. Taxation as a term applies to all types of taxes, from income to gift to estate taxes. It is usually referred to as an act; any revenue collected is usually called "taxes." Taxation can also refer to taxes as an abstract concept, an actual dollar amount of tax that has been levied or the material funds that have been received as taxes. Although all of these definitions are technically correct, the one listed above is the most common. Taxation is one of the primary powers of government over the people.

According to Eftekhari (2009), taxation has always been an issue for the government and taxpayers alike from the early years of civilization. The issue of taxation has generated a lot of controversy and severe political conflicts over time. According to its importance, several economic theories have been proposed to run an effective system. Gabay, Remotin & Uy (n.d) see taxation as the process by which the sovereign, through its law making body, raises revenues used to defray expenses of government, a means of government in increasing its revenue under the authority of the law, purposely used to promote welfare and protection of its citizenry, and the collection of the share of individual and organizational income by a government under the

authority of the law. Iwuji (2005) defines tax as a statutory compulsory contribution imposed by government exacted from a person's or entity's income, property or transaction for the purpose of funding governance. A tax can either be of three basic structures; proportional, regressive or progressive. Tax is said to be proportional when the taxpayer is levied an amount that is an indirect proportion of his income. A regressive tax is one that charges a higher rate to persons receiving lower income, and finally a progressive tax levies a higher rate to higher income earners.

## **2.2 Concept of Small and Medium Enterprises**

There is no generally agreed definition of a small scale enterprise globally. Different writers, researchers and policy makers (Kasekende, 2003; Mwenda and Muuka, 2014) have used different definitions for a small scale enterprise. The number of persons employed, investment in plant and machinery and sales turn over are all used to define a small scale enterprise (Najjemba, 2010).

In Uganda, a small scale enterprise is an enterprise or a firm employing less than 5 but with a maximum of 50 employees, with the value of assets, excluding land, building and working capital of less than Ug.shs 50 million (US\$ 30,000), and the annual income turnover of between Ugshs.10-50 million (US\$6,000-30,000). A Medium sized enterprise is considered a firm, which employs between 50-100 workers. Other characteristics have not been fully developed (Kasekende, 2003). This study took Uganda's definition of small scale enterprises since this study was taken in Uganda.

The concept of SMEs is relative and dynamic (Olorunshola, 2003). SMEs are characterized by uncertainty, innovation and evolution. A firm understanding of SMEs would require a good knowledge of its features. Aderemi (2003) noted that the SMEs in Uganda are usually small, owner or family managed business offering basic goods and services, which tend to lack organizational and management structures with the urban ones tending to be more structural than their rural counterparts. This is one of the most generic features of SMEs in Uganda.

Furthermore, the production processes of SMEs are usually labour intensive and they usually serve as suppliers for the larger manufacturing firms with their operations being highly dependent on raw materials sourced locally (Hanefah, Ariff, & Kasipillai, 2002). They also

require a lower startup capital than the larger companies (Akinsulire, 2010). While the decisions of the managers have a higher tendency to be subjective given that they are managed and controlled by the same individual. Also, the employee-employer relationship found in most SMEs is predominantly informal.

Another key feature of the SME sector in most countries is that it is heterogeneous, varying in size from small retail outlets to highly paid professionals, and substantial manufacturing enterprises. SMEs are also likely to vary in organizational form from sole proprietorships (with or without employees), small corporations (public or private), professionals and partnerships. This feature usually results in different obligations for record keeping for the enterprise.

### **2.3 Relationship between taxes and performance of SMEs**

Assessing the relationship between taxation and SMEs' development is not simply a matter of looking at tax rates. Taxation plays an important role in encouraging growth, investment and innovation and facilitating international trade and mobility. For SMEs key considerations are to minimize administrative burden while ensuring compliance, including considering the drivers and impacts of operating in the informal economy (ITD, 2007). Kolstad et al, (2006) indicated that taxes are perceived to be a major problem for both young and old firms. Therefore, taxation has showing a way towards impacting small and medium enterprises.

According to Tomlin (2008), economists argue that the resources smaller companies direct towards tax compliance are resources that could otherwise be used for reinvestment, facilitating future growth. Hence, there is a belief that taxes and a complex tax system put disproportionate pressure on smaller businesses. Small taxpayers under the regular system of taxation are discriminated against, since the compliance requirements, cost of compliance and tax rate are the same for both small and large enterprises. Reducing the compliance costs and tax rate increases the small enterprises profit margin. It also increases the Government's tax revenue, since the simplified provisions for a micro enterprise historically reduce the size of the shadow economy and the number of non-complying registered taxpayers (Vasak, 2008).

Furthermore, SMEs usually have to operate in an overbearing regulatory environment with the plethora of regulatory agencies, multiple taxes, cumbersome importation procedure and high port charges that constantly exert serious burden on their operations. Many SMEs have to deal with

myriad of agencies at great cost. As stated earlier they are heterogeneous and these differences in size and structure may in turn carry differing obligations for record-keeping that affect the costs to the enterprises of complying with (and to the revenue authorities of administering) alternative possible tax obligations. Public corporations, for example, commonly have stronger accounting requirements than do sole proprietorships, and enterprises with employees may be subject to the full panoply of requirements associated with withholding labor income taxes and social contributions (International Tax Dialogue 2007).

An overly complex regulatory system and tax regime or one opaque in its administration and enforcement makes tax compliance unduly burdensome and often have a distortionary effect on the development of SMEs as they tended to morph into forms that offer a lower tax burden or no tax burden at all (Masato, 2009), producing a tax system that imposes high expenses on the society. A poorly executed tax system also leads to low efficiency, high collection charges, waste of time for taxpayers and the staff, and the low amounts of received taxes and the deviation of optimum allocation of resources (Farzbod, 2010). Existing empirical evidence clearly indicates that small and medium sized businesses are affected disproportionately by these costs: when scaled by sales or assets, the compliance costs of SMEs are higher than for large businesses (Weichenrieder, 2017) because of low efficiency, high collection charges, waste of time for taxpayers and the staff, and the low amounts of received taxes and the deviation of optimum allocation of resources (Farzbod, 2000; Yaobin, (2017).

According to Gordon and Dawson (2017), through taxation, the government takes away money from SMEs they would otherwise spend on private sector. As a result, purchasing power reduces per unit of production in the private sector to the public sector. They further asserted that, one of the most frequent arguments against high income tax is that it destroys the incentive to business people and employees to work harder and more efficiently.

According to the World Bank Symposium (2011), small and medium businesses carry out tax planning so as to have a minimal tax liability and thus increasing the purchasing power. It is through taxes that the government takes away money from people/business they would otherwise spend on private sector. This loss of purchasing power reduces the demand for units of products in the private sector (Gordon and Dawson, 2017).

The taxation of SMEs is an important issue given their importance to the economies of countries. Careful design of government programs for SMEs including special tax rules, can address market failures and the disproportionately high compliance burdens faced by SMEs. Consideration of the heterogeneity of the SME sector and the different challenges faced by SMEs and their owners need to be considered in the design of the taxation rules as governments endeavor to promote the creation innovation and growth of SMEs.

## **2.4 Relationship between tax rates and the performance of SMEs**

It is generally believed that a high tax rate is the main cause of tax evasion which hinders the development of SMEs. Incentives to evade tax depend on the marginal rates of taxation because these govern the gains from evasion as a sum of the sum evaded (Kaldor, 2016) One major tax evasion is the high personal income tax rates which tend to lead tax payers to evade tax. Too many and complicated rules and regulations imposed by the government tend to lead to tax evasion. Businesses find it generally difficult often not profitable to do business legally. The heavy taxation is also a subject of worry not only in developed countries like USA but also in Kenya and other less industrialized countries in Africa and Latin America. The high levels of taxation of SMEs in Africa and in Uganda in particular, warrants attention on accelerated research areas aimed at addressing the overall effects of taxation on SMEs (Osambo, 2009) By studying taxation behavior in five different countries (USA, Gambia, Nigeria, South Africa and Kenya), Derwent (2010) concluded that increased tax burden is a major threat to the development of SMEs.

Several studies have investigated the impact of tax rates on SME profitability. Lower tax rates are generally associated with increased after-tax profits for SMEs. Research by De Mooij and Ederveen (2008) found that a reduction in corporate tax rates led to higher profitability among SMEs in European countries. This increase in profitability allows SMEs to allocate more resources to reinvestment, expansion, and innovation, enhancing their competitiveness in the market. A study by Liu and Altshuler (2013) found that high tax burdens were associated with lower profitability among US manufacturing SMEs. The reduction in after-tax profits resulting from higher tax rates limits the financial resources available for investment, which can impede SME growth and innovation.

Effective tax rates are an important instrument for businesses that demand abridged but refined information on effective tax burdens. Consequently, business owners take keen interest in assessing the effect of post-tax measures on their performance (Lammersen, 2007). Vicari, (2015) construes that an effective tax rate can be designed in such a way that it is not based on the taxable profits as demarcated in the law but on an economic measure which includes the impact of the tax base. The SMEs in a regular tax system are discriminated against since the tax rate for the small and large firms is the same which increases the costs of the small enterprises. This has distorted the growth of SMEs where most small firms have transformed into firms that are levied fewer taxes or no taxes at all (Masato, 2009).

Atawodi & Ojeka (2012) opine that the choice of the tax rate should depend on the tax preference accorded to small businesses to promote the growth of small enterprises which can be done by lowering tax rates, offering tax holidays as well as reliefs to the small businesses. The fundamental objective is to ensure that tax income is successfully increased through methods that suit the country's environment and administrative ability (Atawodi & Ojeka, 2012).

Mungaya, Mbwambo, & Tripathi, (2012) in their research on "The impact of the tax system on the growth of Small and Medium Enterprises (SMEs)" found out that high tax rates increase the cost of production within the small and medium enterprises which greatly affects performance of these firms and therefore should not be ignored. In complement, Oludele and Emilie, (2012) also highlighted that high tax rates coupled with complex tax systems have negatively affected performance within the SMEs sector.

In their 2015 report on the National Small Businesses Survey of Uganda, FSD Uganda, (2015) reported that most small businesses in Uganda had not paid their tax dues because their businesses could not afford the high tax rates being levied. In addition, Baurer, (2005) observed that it is rare not to find complaints among small businesses about the complicated tax structure involving vague tax laws and high tax rates that have hampered the growth of these small businesses. Amongst other reasons for not paying taxes highlighted were: the payment of local service taxes. Ignorance about the tax requirements, failure of the tax body to collect taxes from them, the business did not earn enough to require them to do so, etc.

Higher tax rates can impose additional compliance costs and administrative burdens on SMEs, which can negatively affect profitability. SMEs often have limited resources and capabilities to handle complex tax regulations and compliance requirements. The time and resources spent on tax compliance can divert attention from core business activities, affecting productivity and profitability. A study by Pomeranz (2015) analyzed the impact of tax compliance costs on SME profitability in developing countries. The findings revealed that higher compliance costs were associated with reduced profitability among SMEs, as these costs impose a burden on financial resources and limit reinvestment opportunities.

## **2.5 Relationship between tax incentives and the performance of SMEs**

Tax incentives refer to an exemption or relief granted to an individual or a firm to reduce the effect of taxation and thus encourage savings and investment (Kiser & Karceski, 2017). Globally, tax incentives have been offered by governments in order to attract investors and foster economic growth (Agbenyo, 2016). The importance of addressing the governance of tax incentives was raised in 2011 by the IMF, OECD, UN and World Bank in their joint report to the G-20 on supporting effective tax systems in developing countries (G20 Report, 2011). Tax incentives have been used by governments as tools to promote a particular economic goal and they take form of exemptions, tax holidays, credits, investment allowances and preferential tax rates (United Nations 2018). In addition, different tax incentives were introduced and carried out like tax holidays, initial capital allowances, withholding tax exemption, Value Added Tax (VAT) reductions, income tax rate reductions, and preferential tax rates, carry forward losses and import duty exemptions, among others, within the business sector (Mayende, 2013).

Numerous incentives have been incorporated into the Ghanaian tax system over the years. Notable among such incentives, as claimed by tax authorities, include, but not limited to, tax rebates, reduced tax rates, tax holidays, incomes exempted, capital allowances, fresh graduate incentives, free-zone incentives, double tax treaties, capital gains exempted, import duty exemptions and exempted export duties (PwC Ghana, Ghana Tax Facts and Figures Report, 2019; Ugwu, 2018; Bekoe, Danquah & Senahey, 2016). The creation of some special incentives is based on industry type, number of years of operating, nature of transactions, business size and origin of businesses and so forth (PwC Ghana, Ghana Tax Facts and Figures Report, 2019). Market failures negatively affect SMEs due to their sizes and ages in the business life cycle.

Again, tax system disproportionately goes against SMEs. These hard-hit conditions inform collectively call for SME support in terms of preferential treatments (Bozdoğanoglu, 2016).

Tax incentives are underlined by the benefit theory of tax that advances taxes that agents pay should reflect the benefit that they receive from the mix of good and services they enjoy from the state (Neill, 2000). The benefits theory of tax sets the standard lens through which local taxation is based (Scherf & Weinzierl, 2020). It, therefore, posits taxes should be zero or low for entities and individuals who receive no benefits from the state and high for those entities and individuals that derive the most benefits. Infrastructural developments that are initiated by the government provides the greatest benefits to firms (Stewart, 2015). The agency theory of tax incentive posits that tax incentives compensate for other government-created obstacles in the business environment, thus using tax to respond to fiscal failure as much as market failure (Twesige & Gasheja, 2019). Therefore, granting incentive packages in the tax system is to propel the growth of businesses in the country so as to support government's agenda of economic growth, national development, job creation and improved general welfare of the citizenry.

Megersa (2019) found that tax incentives in China contribute to predicting GDP growth, has positive effect on research and development expenditure in Taiwan, and causes sizeable increase in employment, output, fixed capital and number of firms in India. Again, Siyanbola, Adedeji, Adegbie and Rahman (2017) also discovered that tax incentives are significant strategic drive for business and industrial growth in Sub-Saharan States including Ghana. Besides, the more governments make revenue, the more they are better positioned to provide incentives to tax payers (Siyanbola, et al., 2017).

Empirically, it is found that tax exemptions decrease tax burden of SMEs more than that of tax rates (Liakhoyets, 2014), which positions them to reinvest their capital for their efficient functioning. Government's support such as tax reduction and simplification of tax system also stimulate SMEs' growth (Louis & Macamo, 2011). Tax reduction, lower tax amount payable and tax exemption could support the growth SMEs (Bozdoğanoglu, 2016). In a given empirical comparative study in Uganda, it was discovered that firms with incentives performed better than firms without incentives in terms of gross sales and value added (Mayende, 2013). Better still, streamlining tax incentives were a strong stimulus to improving firm performance (Mayende,

2013). Particularly, Twesige and Gasheja (2019), in their recent study, found that tax incentives are predictors of sustainable SME growth in Rwanda.

## **2.6 Relationship between tax compliance and the performance of SMEs**

A compliance cost is expenditure of time or money in conforming with government requirements such as legislation or regulation (Ambrecht, 2018). Tax compliance is a complex term to be explicitly defined (Marti, 2010). Otherwise, it can be construed “as the willingness of individuals and other taxable entities to act in accordance within the spirit as well as the letter of the tax law and administration without the application of enforcement activities” (James and Alley, 2002). Pope & Abdul-Jabbar, (2008) pointed out that SMEs are facing tax burdens due to the nature and size of these enterprises which has inhibited the performance of SMEs. Tax compliance costs among SMEs in developing countries, are high due to the narrow resource envelope of these small and medium enterprises to fully meet their tax obligations; in addition to the limited expertise in taxation to conform per the complex tax laws (Boadi et al., 2016).

It is not an easy task to persuade taxpayers to comply with tax requirements, since tax represents unaccounted cost (James & Alley, 2005). Tax evasion is persistent in developing countries (Atawodi & Ojeka, 2012). Tax compliance refers to taxpayers’ willingness to pay their taxes (Kirchler, 2007). Contextually, tax compliance captures the ability and willingness of taxpayers to comply with tax laws, declare the correct income in each year and pay the right amount of taxes on time (Internal Revenue Service Act, 2000 Act 592). Tax compliance covers the reporting of all incomes and payment of all taxes by fulfilling the provisions of laws, regulations and court judgments (Jackson & Milliron, 2016). Singh (2003) extended this and opines tax compliance is a person’s act of filing their tax returns, declaring all taxable income accurately, and disbursing all payable taxes within the stipulated period without having to wait for follow-up actions from the authority. Tax compliance is operationalized as the willingness of taxable entities to act in accordance with the spirit and the letter of tax law and administration without the application of enforcement. Tax non-compliance is taxpayer’s failure to remit a proper amount of tax, perhaps on account of the complexity or even contradictions in the tax legislation or tax administration procedure (Kesselman, 2014).

To tackle the issue of non-compliance, most tax regimes integrate punitive measures, such as fines, closure or even jail term, to enforce compliance (Swistak, 2016). Compliance cost, poor internal controls, tax rates (Mwangi, 2014), auditing of account/tax assessment, referral group and tax knowledge (Inasius, 2015), fairness, prompt enforcement (Swistak, 2015), attitude (Nkwe, 2013), high tax rates and complex filing procedure determine SMEs' tax compliance behaviour. Ameyaw et al. (2016) claim that taxes cannot be avoided without attracting punishment. Differences in tax compliance behaviour between small and medium enterprises may again be attributed to the position of the ability to pay tax theory espoused earlier (Kendrick, 2019).

Empirically, in Tanzania, Masanja (2019) found that issues, such as high taxes, multiple taxes unreasonable taxes, unfriendly attitude of tax administrators, difficulty in paying taxes, bureaucracy in paying taxes and changes in taxes, affect tax compliance behaviour for SMEs. Firm size positively related significantly with ability to pay tax (Ocheni & Gemade, 2015). For instance, Mukhlis and Simanjuntak (2016) found low tax compliance behaviour among SMEs. Elsewhere in Greater Accra, Okpeyo, Musah and Gakpetor (2019) found that tax compliance is higher among medium enterprises than small firms. Others also believe small firms bear higher tax compliance costs than larger companies hence having higher default risk of non-payment (Atawodi & Ojeka, 2012; Lokhande, 2020).

## **2.7 Summary of literature review**

A review of the related literature suggested that simplified system of taxation should support SME tax payers to meet their tax duties and thus reduce the burden of tax compliance within SMEs. A streamlined tax administration strategy through providing tax education is fundamental in addressing the tax compliance costs faces by SMEs. However, the empirical evidence on tax compliance of SMEs although insightful, it ignores satisfactory experiences on the influence of tax compliance of SMEs on SME performance.

Similarly, the literature review revealed that the choice of the tax rate should depend on the tax preference accorded to small businesses to promote the growth of SMEs which can be done by lowering tax rates, offering tax holidays as well as relieves to the small businesses. However, the literature on tax rates of small and medium enterprises was not only scant but also failed to offer

pragmatic proof on the influence of tax rates on the growth of SMEs. This research strived to cover the raised literature gaps by examining “the effect of the taxes on the performance of Small and Medium Enterprises in Nsuube-Kauga Parish, Mukono TC Division” to cover the information gap.

## **CHAPTER THREE**

### **METHODOLOGY**

#### **3.0 Introduction**

This chapter presents the methodology that was used in conducting the research. It described how this study was conducted. It includes the study design, the study setting, study population and the sample size. It also describes the sampling procedure definition of variables, research instruments, data analysis and management, ethical considerations, and the limitations of the study.

#### **3.1 Research design**

This study used an explanatory research design which is developed to explore a phenomenon that had not been studied before or had not been well explained previously in a proper manner. Its main intention is to provide details about where to find a small amount of information (Patrik & Ugo, 2019). It also helped in ascertaining how and why a particular phenomenon was occurring and further predicted future occurrences. Lastly, it helped in investigating patterns and trends in existing data that hadn't been previously investigated.

The researcher also employed the use of quantitative research method. Quantitative research method was used because it is more reliable and objective, it helped the researcher in use of statistics to generalize the findings and also helped in testing theories/ hypotheses and lastly, it helped in determining the relationship between the two variables (Bhawna & Gobind, 2015). Therefore quantitative research approach was used to gather statistical data from the selected SME owners or managers in Kauga, Nsuube-Kauga Parish, Mukono TC Division with the help of researcher-administered questionnaires (Haradhan, 2021).

#### **3.2 Study area**

This study was carried out in different SMEs located in Kauga village, Nsuube-Kauga Parish, Mukono TC Division, Mukono district of Central region of Uganda. It was chosen because it is the second largest Municipality in Uganda in terms of population meaning that there are a lot of

SMEs established in this area facing a challenge of taxation that are hindering the performance of their businesses.

### 3.3 Study population

According to statistics from Mukono Municipal Council (2023), there are 100 registered SMEs operating in Kauga village which are categorized according to segmented businesses and those that deal in assorted merchandize and these were included in the study as the population. Furthermore, in this study, the unit of analysis is the major entity that is being analysed in the study. Therefore the unit of analysis in this study was the selected SMEs operating in Kauga, Nsuube-Kauga Parish, Mukono TC Division.

### 3.4 Sampling method and sample size

The sampling methods provide information required about the selection of the samples. It also provides a detailed foundation where the research sample can be drawn, and for a population that is enough for a high quality selection of the participants (Lewis and Ritchie, 2003). The researcher therefore used stratified sampling which is a method under probability sampling technique. The study was carried out using the stratified sampling method whereby samples were selected from the SME owners or managers in Kauga village grouped under segmented businesses and those that deal in assorted merchandize. This was due to their convenience about the topic and area under study hence they were expected to represent each element in the population. This technique helped in reducing on the costs of collecting and analyzing data. The table below shows how stratified sampling was used by the researcher;

**Table 1: Showing how stratified sampling was used**

Category of Sole Proprietor Businesses	Population	Sample Size
Assorted merchandize	60	48
Segmented businesses	40	32
<b>Total</b>	<b>100</b>	<b>80</b>

**Source:** *Mukono Municipal Council (2023)*

### 3.5 Sample size

The researcher used Krejcie and Morgan's (1970) table to determine the sample size since the population study was known and calculated by the scholar as follows:

**Table 2: For determining sample size of a known population**

Table 3.1 <i>Table for Determining Sample Size of a Known Population</i>									
N	S	N	S	N	S	N	S	N	S
10	10	100	80	280	162	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	346
25	24	130	97	320	175	950	274	4000	351
30	28	140	103	340	181	1000	278	4500	354
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	191	1200	291	6000	361
45	40	170	118	400	196	1300	297	7000	364
50	44	180	123	420	201	1400	302	8000	367
55	48	190	127	440	205	1500	306	9000	368
60	52	200	132	460	210	1600	310	10000	370
65	56	210	136	480	214	1700	313	15000	375
70	59	220	140	500	217	1800	317	20000	377
75	63	230	144	550	226	1900	320	30000	379
80	66	240	148	600	234	2000	322	40000	380
85	70	250	152	650	242	2200	327	50000	381
90	73	260	155	700	248	2400	331	75000	382
95	76	270	159	750	254	2600	335	1000000	384

*Note: N is Population Size; S is Sample Size* *Source: Krejcie & Morgan, 1970*

**Source:** *Krejcie and Morgan's (1970)*

Therefore from the table above, the sample size was 80 respondents got from a total population of 100 registered SMEs operating in Kauga village, Nsuube-Kauga Parish, Mukono TC Division.

### 3.6 Sources of data

While carrying out the research study, both primary and secondary data were used by the researcher.

#### 3.6.1 Primary source

Primary data are important for all areas of research because they are accurate information about the results of an experiment or observation. Primary data from the field was obtained through personal interviews and self-administered questionnaires to selected respondents in order to get

their opinions. Primary data helped the researcher in collecting information for the specific purposes of their study. The researcher collected the data herself, using questionnaires.

### **3.6.2 Secondary source**

Secondary data refers to handling, collecting and possibly processing data by people other than the researcher in question. For the purposes of a historical research project, secondary sources are generally scholarly books and articles. This source was used to collect data from already written literature for example e-books, journals, published articles and periodicals. Documentary resources are classified in order to facilitate the data collection and textual analysis (Mubazi 2008).

### **3.7 Data collection methods**

The researcher of this study used one type of data collection instruments. This includes questionnaire survey which was briefly explained in the following subsection.

#### **3.7.1 Questionnaire survey**

A questionnaire survey is a research method for collecting information from respondents using standardized questionnaires (Mugenda & Mugenda, 2003). This method involved collecting information from a sample of respondents who were the owners or managers of the selected SME owners or managers operating in Kauga village in a systematic way. A questionnaire survey was used because it provides a high level of general capability in representing a large population. Due to the usual huge number of people who answers survey, the data being gathered possess a better understanding of what is being studied. Because of the high representativeness brought about by the questionnaire survey method, it is often easier to find statistically significant results than other data gathering methods. Questionnaire survey was also used for these categories of respondents to save on time because their number was big to interview (Amin, 2005).

### **3.8 Validity and Reliability of the data collection instruments**

In order for the data collection instruments to be sound, they must be free of bias and distortion. Reliability and validity are two concepts that are important for defining and measuring bias and

distortion. The following subsections explain how validity and reliability were determined in this study.

### 3.8.1 Validity

According to Cohen, Manion and Keith (2007), Validity is ensured by; choosing an appropriate scale, ensuring that there are adequate resources for the required research to be undertaken, selecting an appropriate methodology for ensuring the research questions, avoiding having too long or too short an interval between pre-test and post-test, ensuring standardized procedures for gathering data or for information administering tests, and tailoring the instruments to the concentration span of the respondents.

Validity was done in order to find out whether the questions are capable of capturing the intended data. Experts in research reviewed the questions to see whether they were capable of capturing the intended response. A Content Validity Index (CVI) was calculated in order to establish the validity of the research instrument. The researcher used the following formula to establish validity of the research instruments as seen below.

$$\text{Content validity Index (CVI)} = \frac{\text{Relevant items by all judges as suitable}}{\text{Total number of items judged.}}$$

The CVI was 0.81 which was greater than the recommended 0.70 (Kent, 2001) hence implying that the questionnaire was valid for data collection.

### 3.8.2 Reliability

Mugenda and Mugenda (2003) defined reliability as a measure of the degree to which a research instrument yields consistent results or data after repeated trials. Reliability of the questionnaire instrument was assessed using Cronbach's coefficient alpha. A pilot study was carried out on 10 respondents and the reliability results were computed using the Statistical Package for the Social Sciences (SPSS). The following formula was used to calculate the Cronbach's coefficient alpha

$$\alpha = \frac{k}{K-1} \left( \frac{1 - \sum SDi^2}{\sum SDt^2} \right)$$

Where  $\alpha$  = coefficient alpha

$\sum SD_i^2$  = sum variance of items

$\sum SD_t^2$  = sum variance of scale

The coefficient was 0.83 which was above the recommended .70 (Amin, 2005) hence implying that the questionnaire was suitable for data collection.

### **3.9 Procedure of data collection**

After approval of the proposal from Uganda Christian University, the researcher was given a letter of introduction to take to the selected SME owners or managers operating in Kauga village, Nsuube-Kauga Parish, Mukono TC Division. This served to secure permission in order to carry out the study in this area. The researcher presented a letter of consent to the respondents, after which, questionnaires were distributed. The respondents were given time within which they should have returned the fully filled questionnaires. After the questionnaires had been filled, the researcher collected them, sorted them and coded them.

### **3.10 Data analysis**

#### **3.10.1 Quantitative data analysis**

Data analysis was done with the aid of the package (SPSS) which besides being user friendly, is appropriate for handling the correlations between the variables plus regressions in the study. All variables were assigned with names and coded for computer entry. Secondly all the responses were coded to facilitate computer data in-put. Thirdly, after data entry was completed, negatively worded scales were recorded and assigned with new values. Fourthly, in order to get composite scores for items on a scale, target variables were computed. Fifthly, data was screened in order to minimize data entry errors. Quantitative data was analyzed using descriptive statistics and Pearson Correlation to examine the relationship between the independent and the dependent variable in the study.

### **3.11 Ethical considerations**

The researcher took into consideration a number of ethical issues including:

Confidentiality of respondents was kept: Respondents were not required to reveal their names nor their contacts on the questionnaires. Identification numbers were used instead of names to avoid information given being traced to a respondent.

All data gathered was used only for the purpose of this study and nothing else.

The research procedures were explained to all the respondents before they took part in the research and their informed consent obtained.

All the sources of literature were acknowledged throughout the whole study through proper citations and referencing.

Personal bias was avoided during the entire study that is to say during interviews, data analysis and reporting.

### **3.12 Limitations and delimitations of the study**

First and foremost, the research instruments were not standardized. Therefore a validity and reliability test was done to produce a credible measurement of the research variables.

Secondly, the researcher was limited by funds that were needed to facilitate the research such as motivating the respondents, printing fees and even daily transport to the organization to collect data. However the researcher used self-initiatives and strategies to mobilize financial assistance from family.

## CHAPTER FOUR

### PRESENTATION, INTERPRETATION AND DISCUSSION OF RESULTS

#### 4.0 Introduction

This chapter presents and discusses the results of analysis that has been done to look at the specific objectives of the study and in relation to the reviewed literature. The study was carried out using questionnaires with SME owners or managers located in Kauga village, Nsuube-Kauga Parish, Mukono TC Division totaling to 80 respondents. The findings are presented with the help of tables for purposes of clarity and interpretation.

#### 4.1 Findings on demographic characteristics of respondents

This section presents the general background information about the respondents in relation to their gender, age, education level, category of business and period spent operating the business as shown in the table below;

##### 4.1.1 Gender of the respondents

The table below summarizes the gender of the respondents that are SME owners or managers in Kauga and the data in the table was interpreted below.

**Table 3: Gender**

	Frequency	Percent	Cumulative Percent
Male	45	56.3	56.3
Female	35	43.7	100.0
Total	80	100.0	

**Source:** *Primary data*

Findings in the table 3 above show that the majority of respondents, represented by 56.2% are male while female constituted the minority, 43.8% of the total respondents. Therefore there were more males involved in the study compared to their female counterparts. However, the inclusion of both male and female in the survey was to get a different view from the respondents about the topic under study.

#### 4.1.2 Age of the respondents

The table below summarizes the gender of the respondents that are SME owners or managers in Kauga and the data in the table is interpreted below.

**Table 4: Age**

	Frequency	Percent	Cumulative Percent
21-30 years	24	30.0	30.0
31-40 years	33	41.3	71.3
41-50 years	15	18.7	90.0
Above 50 years	8	10.0	100.0
Total	80	100.0	

**Source:** *Primary data*

Findings in the table 4 above show that the vast majority of the respondents fell between the age group of 31-40 years represented by 41.3%, followed by the respondents who fell between the age group of 21-30 years represented by 30%, followed by those between 41-50 years represented by 18.7% and lastly, 10% of the respondents were above 50 years. This therefore implies that there was no age discrimination since information was gotten from people with different age groups.

#### 4.1.3 Education level of the respondents

The table below summarizes the education level of the respondents that are SME owners or managers in Kauga and the data in the table was interpreted below.

**Table 5: Level of education**

	Frequency	Percent	Cumulative Percent
Primary	15	18.7	18.7
Secondary	25	31.3	50.0
Tertiary	30	37.5	87.5
Others	10	12.5	100.0
Total	80	100.0	

**Source:** *Primary data*

Findings in the table 5 above revealed that majority of respondents represented by 37.5% have at least attained tertiary level of education, followed by 31.3% who have at least attained secondary level of education, followed by 18.7% who have at least attained primary level of education, whereas 12.5% have no education background. It can therefore be noted that most of the respondents were able to read and understand the questionnaire with ease although questionnaire interpretation was done for those with no education background.

#### 4.1.4 Category of business respondents operate in

The table below summarizes the category of business the respondents that are SME owners or managers in Kauga operate in and the data in the table was interpreted below.

**Table 6: Category of business**

	Frequency	Percent	Cumulative Percent
Segmented business	34	42.5	42.5
Assorted merchandise	46	57.5	100.0
Total	80	100.0	

**Source:** *Primary data*

Findings in the table 6 above revealed that majority of respondents represented by 57.5% operate segmented businesses like saloons, printing bureaus, boutiques and repair maintenance businesses among others, whereas 42.5% operate businesses that fall under assorted merchandise like retail and wholesale shops.

#### **4.1.5 Period spent operating the business**

The table below summarizes the period respondents that are SME owners or managers in Kauga have spent operating their businesses and the data in the table was interpreted below.

**Table 7: Period spent operating the business**

	Frequency	Percent	Cumulative Percent
1-5 years	26	32.5	32.5
6-10 years	39	48.7	81.2
Above 10 years	15	18.8	100.0
Total	80	100.0	

**Source:***Primary data*

Findings from the table 7 above show that majority of respondents, 48.7% have spent 6-10 years operating their respective businesses, followed 32.5% who have been operating their respective businesses for a period of 1-5 years, where those who have spent more than 10 years operating their respective businesses constituted the minority represented by 18.8%. The findings imply that the respondents have the necessary information about the topic under study since majority of them have spent reasonable time operating different businesses in Kauga, Mukono district.

#### 4.2 The relationship between tax rates and the performance of SMEs in Kauga

Table 8 summarizes respondents' responses the relationship between tax rates and the performance of SMEs in Nsuube-Kauga Parish, Mukono by using a Likert scale where SA (Strongly Agree), A (Agree), NS (Not Sure), D (Disagree) and SD (Strongly Disagree).

**Table 8: Relationship between tax rates and the performance of SMEs in Kauga**

Statements	Extent of agreement and disagreement				
	SA	A	NS	D	SD
	Freq. (%)	Freq. (%)	Freq. (%)	Freq. (%)	Freq. (%)
The tax rates charged are clear in terms of payable taxes	42 52.5%	24 30.0%	00	10 12.5%	4 5.0%
There are diverse and many taxes imposed on small and medium enterprises	23 28.8%	35 43.7%	6 7.5%	11 13.7%	5 6.3%
The taxes charged on SMEs are burdensome to the business	19 23.7%	38 47.5%	7 8.8%	15 18.7%	1 1.3%
Taxes are only charged when the business is operating hence allowing for momentary closures of business	21 26.3%	34 42.5%	5 6.3%	20 25.0%	00
The regressive nature of taxes on SME reduces their revenue base	23 28.8%	35 43.7%	10 12.5%	12 15.0%	00
SMEs have information on how much tax when to pay tax, where to pay and mode of tax payment	24 30.0%	40 50.0%	00	16 20.0%	00

**Source:** Primary data

Table 8 represents the descriptive statistics on tax rates among SMEs in Nsuube-Kauga Parish, Mukono TC Division. According to the study in table 8 above, 82.5% of the respondents agreed that the tax rates charged are clear in terms of payable taxes, whereas 17.5% of the respondents disagreed with the statement put across. The study illustrated that 72.5% of the respondents agreed that there are diverse and many taxes imposed on small and medium enterprises, 7.5% were not sure, whereas 20% of the respondents disagreed and strongly disagree respectively with the statement put across.

The study established that 71.2% of the respondents agreed that the taxes charged on SMEs are burdensome to the business, 8.8% were not sure whereas 20% of the respondents disagreed with the statement put across. The study further noted that 68.8% of the respondents agreed that taxes are only charged when the business is operating hence allowing for momentary closures of business, 6.2% were not sure whereas 25% of the respondents disagreed and strongly disagreed with the statement put across.

Furthermore, the study found out that 72.5% agreed that the regressive nature of taxes on SME reduces their revenue base, 12.5% were not sure whereas 15% disagreed with the statement. Finally, the findings established that 80% of the respondents agreed that SMEs have information on how much tax when to pay tax, where to pay and mode of tax payment, whereas 20% of the respondents were not sure of the statement put forward.

Therefore the findings of the study illustrated that majorly, there are diverse and many taxes imposed on small and medium enterprises and that the taxes charged on SMEs are burdensome to the businesses which has greatly affected the overall performance of SMEs in Kauga which were represented by 82.5% and 80% of the respondents who agreed respectively. The findings of the study concerning the relationship between tax rates and the performance of SMEs in Nsuube-Kauga Parish, Mukonowere further determined using Pearson’s correlation that was conducted as shown below;

**Table 9: Pearson’s correlation statistics on tax rates and the performance of SMEs**

**Correlations**

		Tax rates	Performance of SMEs
Tax rates	Pearson Correlation	1	.875**
	Sig. (2-tailed)		.000
	N	80	80
Performance of SMEs	Pearson Correlation	.875**	1
	Sig. (2-tailed)	.000	
	N	80	80

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

**Source:** Primary data

The findings indicated in table above shows that there is a significant positive relationship between tax rates and the performance of SMEs in Nsuube-Kauga Parish, Mukono. This relationship is affirmed by r-values of 0.875\*\* with significant p-values of 0.000 at the level of 0.05 (2-tailed). It should further be noted that the p-value is below the significance level of 0.05 which means that we accept the null hypothesis. This means that there is a significant positive relationship between tax rates and the performance of SMEs in Nsuube-Kauga Parish, Mukono.

#### 4.3 The relationship between tax incentives and the performance of SMEs in Kauga

Table 10 summarizes respondents' responses on the relationship between tax incentives and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division by using a Likert scale where SA (Strongly Agree), A (Agree), NS (Not Sure), D (Disagree) and SD (Strongly Disagree).

**Table 10: Relationship between tax incentives and the performance of SMEs in Kauga**

Statements	Extent of agreement and disagreement				
	SA	A	NS	D	SD
	Freq. (%)	Freq. (%)	Freq. (%)	Freq. (%)	Freq. (%)
The government has given special tax treatment to SMEs in the form of tax holidays	00	00	2 2.5%	58 72.5%	20 25.0%
Tax incentives have stimulated the growth and expansion of SMEs in Uganda	00	00	3 3.8%	63 78.8%	14 17.5%
Tax incentives have protected the infant small and medium enterprises in Uganda	00	2 2.5%	2 2.5%	54 67.5%	22 27.5%
Tax incentives have encouraged a reasonable number of traders in the SME sector to continue operating	00	00	4 5.0%	57 71.3%	19 23.8%
Special tax treatment for SMEs has corrected market imperfections in the country	00	31 38.7%	00	49 61.3%	00
Tax incentives for SMEs have lowered the operational costs associated with payment of taxes for SMEs	00	00	4 5.0%	57 71.3%	19 23.8%

**Source:** Primary data

Table 10 represents the descriptive statistics on tax incentives among SMEs in Nsuube-Kauga Parish, Mukono TC Division. According to the study in table 10 above, 97.5% of the respondents disagreed that the government has given special tax treatment to SMEs in the form of tax holidays, whereas 2.5% of the respondents disagreed with the statement put forward. The study illustrated that 96.3% of the respondents disagreed that tax incentives have stimulated the growth and expansion of SMEs in Uganda, whereas 3.8% were not sure of the statement put across.

The study established that 95.0% of the respondents disagreed that tax incentives have protected the infant small and medium enterprises in Uganda, 2.5% were not sure whereas 2.5% of the respondents agreed with the statements put across. The study also noted that 95.0% of the respondents disagreed that tax incentives have encouraged a reasonable number of traders in the SME sector to continue operating, whereas 5% of the respondents were not sure of the statement put across.

The study further noted that 61.3% of the respondents disagreed that special tax treatment for SMEs has corrected market imperfections in the country, whereas 38.7% agreed with the statement put forward. Finally, the study findings revealed that 95.1% of the respondents disagreed that tax incentives for SMEs have lowered the operational costs associated with payment of taxes for SMEs, whereas 5% of the respondents were not sure of the statement put across.

Therefore the major findings of the study illustrated that majorly, the government has not given special tax treatment to SMEs in the form of tax holidays and that tax incentives have not stimulated the growth and expansion of SMEs in Uganda which were represented by 97.5% and 95% of the respondents who disagreed respectively. The findings of the study concerning the relationship between tax incentives and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division further determined using Pearson's correlation that was conducted as shown below;

**Table 11: Pearson’s correlation statistics on tax incentives and the performance of SMEs**

**Correlations**

		Tax incentives	Performance of SMEs
Tax incentives	Pearson Correlation	1	-.848**
	Sig. (2-tailed)		.001
	N	80	80
Performance of SMEs	Pearson Correlation	-.848**	1
	Sig. (2-tailed)	.001	
	N	80	80

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

**Source:** *Primary data*

The findings indicated in table above shows that there is a significant negative relationship between tax incentives and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division. This relationship is affirmed by r-values of -0.848\*\* with significant p-values of 0.001 at the level of 0.05 (2-tailed). It should further be noted that the p-value is below the significance level of 0.05 which means that we accept the null hypothesis. This means that there is a significant negative relationship between tax incentives and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.

#### 4.4 The relationship between tax compliance and the performance of SMEs in Kauga

Table 12 summarizes respondents' responses on the relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division by using a Likert scale where SA (Strongly Agree), A (Agree), NS (Not Sure), D (Disagree) and SD (Strongly Disagree).

**Table 12: Relationship between tax compliance and the performance of SMEs in Kauga**

Statements	Extent of agreement and disagreement				
	SA	A	NS	D	SD
	Freq. (%)	Freq. (%)	Freq. (%)	Freq. (%)	Freq. (%)
I always file my returns in time	23 28.8%	51 63.8%	4 5.0%	1 1.3%	1 1.3%
I always pay tax on time without intervention of tax officials	19 23.8%	53 66.3%	7 8.8%	00	1 1.3%
I always disclose all my income for tax purposes	21 26.3%	54 67.5%	4 5.0%	1 1.3%	00
I always follow tax rules and regulations governing SMEs operations	23 28.8%	51 63.8%	4 5.0%	2 2.6%	00
I feel it is wrong if I do not report all my income in order to pay less income taxes	20 25.0%	58 72.5%	2 2.5%	00	00
Taxes are so heavy that sometimes it is justifiable to cheat on taxes	19 23.8%	57 71.3%	4 5.0%	00	00

**Source:** *Primary data*

Table 12 represents the descriptive statistics on tax compliance among SMEs in Nsuube-Kauga Parish, Mukono TC Division. According to the study in table 12 above, 92.6% of the respondents agreed that they always file their returns in time, 5% were not sure, whereas 2.6% of the respondents disagreed and strongly disagree respectively with the statement put across. The study established that 90.1% of the respondents agreed that they always pay tax on time without

intervention of tax officials, 8.8% were not sure, whereas 1.3% of the respondents disagreed with the statement put across.

The study further noted that 93.8% of the respondents agreed that they always disclose all their income for tax purposes, 5% were not sure, whereas 1.3% of the respondents disagreed and strongly disagreed with the statement put across. The study found out that 92.6% agreed that they always follow tax rules and regulations governing SMEs operations, 5% were not sure, whereas 2.6% disagreed with the statement.

Furthermore, the findings established that 95% of the respondents agreed that they feel it is wrong if they do not report all their incomes in order to pay less income taxes, whereas 5% of the respondents were not sure of the statement put forward. Finally, the study findings revealed that 95.1% of the respondents agreed that taxes are so heavy that sometimes it is justifiable to cheat on taxes, whereas 5% of the respondents were not sure of the statement put across.

Therefore the major findings of the study illustrated that majorly, the SME owners always file their returns in time and that they always pay tax on time without intervention of tax officials which has been influential for them in attaining improved performance of their SMEs which were represented by 97.5% and 95% of the respondents who agreed respectively. The findings of the study concerning the relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division were further determined using Pearson's correlation that was conducted as shown below;

**Table 13: Pearson's correlation statistics on tax compliance and performance of SMEs**

**Correlations**

		Tax compliance	Performance of SMEs
Tax compliance	Pearson Correlation	1	.833**
	Sig. (2-tailed)		.000
	N	80	80
Performance of SMEs	Pearson Correlation	.833**	1
	Sig. (2-tailed)	.000	
	N	80	80

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

**Source:** Primary data

The findings indicated in table above shows that there is a significant positive relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division. This relationship is affirmed by r-values of 0.833\*\* with significant p-values of 0.000 at the level of 0.05 (2-tailed). It should further be noted that the p-value is below the significance level of 0.05 which means that we accept the null hypothesis. This means that there is a significant positive relationship between tax compliance and the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.

## CHAPTER FIVE

### SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

#### 5.0 Introduction

This chapter presents the summary and description of findings derived from the study. The chapter also provides findings, conclusions and recommendations for policy as well as recommendations for further research.

#### 5.1 Summary of findings

The findings revealed that a significant proportion of respondents agreed that tax rates charged are clear and there are diverse and many taxes imposed on SMEs. Moreover, a considerable number of respondents perceived the taxes on SMEs as burdensome to their businesses. Additionally, many respondents agreed that taxes are only charged when the business is operating, allowing for momentary closures. Furthermore, the majority agreed that the regressive nature of taxes reduces SMEs' revenue base, and SMEs have sufficient information on tax payment. Pearson's correlation analysis supported the findings, indicating a significant positive relationship between tax rates and SMEs' performance ( $r = .875^{**}$ ,  $p < .05$ ). Overall, the study suggests that the burden of multiple taxes and unclear tax policies has negatively impacted the performance of SMEs in the area.

Furthermore, the findings revealed that the majority of respondents disagreed that the government has given special tax treatment to SMEs in the form of tax holidays and that tax incentives have stimulated the growth and expansion of SMEs in Uganda. Similarly, most respondents disagreed that tax incentives have protected infant small and medium enterprises in Uganda and encouraged a reasonable number of traders in the SME sector to continue operating. Additionally, the study noted that a majority disagreed that special tax treatment for SMEs has corrected market imperfections in the country and that tax incentives for SMEs have lowered operational costs associated with tax payment. Pearson's correlation analysis supported the findings, indicating a significant negative relationship between tax incentives and the performance of SMEs ( $r = -.848^{**}$ ,  $p < .05$ ). Overall, the study suggests that the perceived lack of significant tax incentives has negatively impacted the performance of SMEs in the area.

Finally, the findings revealed that the majority of respondents agreed that they always file their returns in time, pay taxes on time without intervention of tax officials, disclose all their income for tax purposes, and follow tax rules and regulations governing SMEs operations. Additionally, most respondents felt that it is wrong not to report all their income to pay fewer income taxes and disagreed that taxes are so heavy that sometimes it is justifiable to cheat on taxes. Pearson's correlation analysis supported the findings, indicating a significant positive relationship between tax compliance and the performance of SMEs ( $r = .833^{**}$ ,  $p < .05$ ). Overall, the study suggests that SME owners' adherence to tax compliance, timely filing, and payment of taxes without evasion has positively influenced their SMEs' performance in the area.

## **5.2 Conclusions**

In conclusion, the study findings on the relationship between tax-related factors and the performance of SMEs in Nsuube-Kauga Parish, Mukono, it is evident that tax policies play a crucial role in shaping SMEs' growth and viability. The high agreement among respondents on the clarity of tax rates and the awareness of SMEs regarding tax payment procedures is promising. However, the study also highlights significant concerns, with many SME owners perceiving taxes as burdensome, especially due to their regressive nature, which negatively affects revenue bases. Furthermore, the lack of perceived tax incentives for SMEs hinders their potential for growth and expansion in the area. Moreover, the study highlights the importance of tax compliance for SMEs' success. SME owners who consistently file returns, pay taxes on time, and adhere to tax regulations demonstrate a positive correlation with improved SME performance.

## **5.3 Recommendations**

From the above discussions of findings and conclusion, the following measures are recommended in response to the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division.

The study recommends that the government should streamline tax policies. To address the negative impact of multiple and burdensome taxes on SMEs, policymakers should consider streamlining tax policies. Simplifying tax structures and consolidating various taxes can alleviate the administrative burden on SMEs, making it easier for them to comply with tax regulations.

The study also recommends the need to introduce targeted tax incentives for SMEs. To stimulate the growth and expansion of SMEs, the government should introduce targeted tax incentives. Providing tax breaks or holidays to SMEs, especially during their early stages, can encourage investment, innovation, and job creation in the region.

The study further recommends the need to enhance tax education and awareness programs. To improve tax compliance among SME owners, the study recommends implementing comprehensive tax education and awareness programs. These programs should focus on informing SMEs about tax regulations, filing processes, and available incentives to ensure they can fully benefit from the existing tax policies.

More so, the study recommends the need to address regressive tax measures. Policymakers should review and reform regressive tax measures that disproportionately impact SMEs' revenue bases. By introducing progressive tax structures, the government can support SMEs' financial stability and foster long-term growth opportunities.

In addition, the study recommends the need to foster collaboration between tax authorities and SMEs: The study suggests promoting closer collaboration between tax authorities and SMEs. Regular engagement and open communication can help build mutual trust and understanding, enabling SMEs to comply with tax regulations more effectively and receive appropriate support when needed.

Last but not least, the study recommends the need to conduct regular tax policy evaluations. Policymakers should conduct periodic evaluations of tax policies' impact on SMEs' performance. Assessing the effectiveness of tax measures and their alignment with SMEs' needs will enable timely adjustments and improvements to support the sector's growth.

Finally, the study recommends the need to develop a tax ombudsman for SMEs. To address tax-related grievances and concerns raised by SMEs, the study recommends establishing a tax ombudsman dedicated to handling SME-specific tax issues. This entity can act as a mediator, ensuring fair treatment and timely resolution of tax-related disputes.

#### **5.4 Areas for further research**

Since this study examined the effects of taxes on the performance of SMEs in Nsuube-Kauga Parish, Mukono TC Division, the study recommends that a longitudinal study should be conducted to explore the long-term impact of tax compliance and tax incentives on the performance and sustainability of SMEs. Follow a cohort of SMEs over several years, tracking their tax compliance behaviors, changes in performance metrics, and business outcomes. This research could shed light on the lasting effects of tax compliance practices and tax incentives on SMEs' financial health, expansion, and overall success in the long run.

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5. How long have you been operating this business?

- a) Less than 1 year                       b) 1-5 years
- c) 6-10 years                               d) Above 10 years

**Note:** In these subsequent sections, use the scale provided to tick in the box of the relevant answer that describes your opinion. **NB: 5=Strongly Agree, 4=Agree, 3= Not Sure, 2= Disagree and 1=Strongly disagree.**

**Section B: Taxes**

	Questions	Responses				
<b>PART 1</b>	<b>Tax Rates</b>	<b>5</b>	<b>4</b>	<b>3</b>	<b>2</b>	<b>1</b>
<b>TR1</b>	The tax rates charged are clear in terms of payable taxes					
<b>TR2</b>	There are diverse and many taxes imposed on small and medium enterprises					
<b>TR3</b>	The taxes charged on SMEs are burdensome to the business					
<b>TR4</b>	Taxes are only charged when the business is operating hence allowing for momentary closures of business					
<b>TR5</b>	The regressive nature of taxes on SME reduces their revenue base					
<b>TR6</b>	SMEs have information on how much tax when to pay tax, where to pay and mode of tax payment					
<b>PART 2</b>	<b>Tax Incentives</b>	<b>5</b>	<b>4</b>	<b>3</b>	<b>2</b>	<b>1</b>
<b>TI1</b>	The government has given special tax treatment to SMEs in the form of tax holidays					
<b>TI2</b>	Tax incentives have stimulated the growth and expansion of SMEs in Uganda					
<b>TI3</b>	Tax incentives have protected the infant small and medium enterprises in Uganda					
<b>TI4</b>	Tax incentives have encouraged a reasonable number of traders in the SME sector to continue operating					

<b>TI5</b>	Special tax treatment for SMEs has corrected market imperfections in the country					
<b>TI6</b>	Tax incentives for SMEs have lowered the operational costs associated with payment of taxes for SMEs					
<b>PART 3</b>	<b>Tax Compliance</b>	<b>5</b>	<b>4</b>	<b>3</b>	<b>2</b>	<b>1</b>
<b>TC1</b>	I always file my returns in time					
<b>TC2</b>	I always pay tax on time without intervention of tax officials					
<b>TC3</b>	I always disclose all my income for tax purposes					
<b>TC4</b>	I always follow tax rules and regulations governing SMEs operations					
<b>TC5</b>	I feel it is wrong if I do not report all my income in order to pay less income taxes					
<b>TC6</b>	Taxes are so heavy that sometimes it is justifiable to cheat on taxes					

### Section C: Performance of SMEs

No.	Statements	Responses				
		1	2	3	4	5
<b>PART 4</b>	<b>Performance of SMEs</b>					
<b>P1</b>	Taxes have reduced the return on investments of small and medium firms					
<b>P2</b>	Taxes have not affected the sales turnover of SMEs through increasing the operational costs					
<b>P3</b>	Taxes have affected the liquidity position of SMEs					
<b>P4</b>	The profits of the small and medium enterprises before taxes are always high					
<b>P5</b>	Taxes have reduced capital resources for investment in research, innovation, and development					
<b>P6</b>	Taxes have inhibited the growth of SMEs in Uganda					

<b>P7</b>	The taxes levied from SMEs have made it difficult for the small and medium firms to achieve their goals					
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**Thank you very much for your cooperation**