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TO MAINTAIN COMPETIVENESS, SUSTAIN LONG TERM GROWTH AND CREATE EMPLOYMENT KENYA NEEDS TO SHIFT FROM HIGH DIRECT TAXES TO INDIRECT TAXES (VAT)

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TO MAINTAIN COMPETIVENESS, SUSTAIN LONG TERM GROWTH AND CREATE EMPLOYMENT KENYA NEEDS TO SHIFT FROM HIGH DIRECT TAXES TO INDIRECT TAXES (VAT)

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Abstract

Although Kenya had embarked on massive tax reforms in 1986, little has been achieved in terms of obtaining the tax revenue structure as that of developed countries. It is not known how the reforms have affected each tax source. VAT is the tax for the future because it is the tax based on the expenditure. Most countries are striving to have the VAT revenue income as the greater contributor of its revenue. The effectiveness of the tax revenue depends on the design and implementation of the tax policies. To achieve this high future tax revenue, favorable economic policies need to be put in place. Policies that will economically empower the majority of nation's citizens. In Kenya various effect efforts have been put in place to achieve this. Among these policies include the regionalization and trade free barriers that enable the member states free movement of factors of production and goods and services.

The broad objective of the study was to examine Kenya's tax revenue structure in light of the developed countries' structure and come up with ways in which Kenya could achieve similar tax revenue structure to those of the developed countries. The independent variables of the study were policy framework and environmental dynamism. The dependent variable was strategy implementation gaps.

This study was a comparison study to other countries that have adopted high VAT policies. The study used data collected in Kenya and compared to some of the European countries that have a high VAT collection. Data analysis was done using inferential statistics with Correlation and regression analysis. Collected data was analyzed using Statistical Package for Social Science (SPSS) and results presented in form of tables and figures.

Key Words: High Direct Taxes, Indirect Taxes, Policy Framework, Environmental Dynamism, Strategy Implementation Gaps

Background of the Study

For the smooth running of government activities, any government will need funds. Taxes are a good source of revenue for government expenditure and on the other hand aid in the distribution of income as well as wealth. Any tax charged has a distributive effect on the income of the tax payer. There are three different approaches to distribution of tax burdens: progressive taxes in which “individuals with higher incomes bear a higher tax burden than those with lower incomes”, proportionate tax where the tax rate is fixed as the amount subject to taxation increases and regressive tax which impose greater burden relative to resources on the poor than on the rich. Regressive taxes will attempt to reduce the tax incidence of people with higher ability- to-pay as they shift the incidence disproportionately to those with lower ability- to- pay and as a result low income earners are taxed proportionately higher than high income earners (Osoro, 2013).

This paper will start by looking at the background of the study. In recent years, domestic revenue mobilization in developing countries gained increasing prominence in the policy debate. Several factors explain this, including the potential benefits of taxation for nation building; independence from foreign aid; the fiscal effects of trade liberalization; the financial and debt crisis in the “West”; and the acute financial needs of developing countries. Taxation has also become an area of increasing interest amongst researchers, particularly in the field of political science and economics Altig, Laurence, Kent, and Jan, 2001).

Most developing countries have considerably liberalized international trade, often with the strong encouragement of aid donors and international organizations. Taxes on exports have been dramatically decreased and often eliminated in

many developing countries, while taxes on imports have decreased substantially and may be reduced further. African countries are likely to come under increasing pressure to further liberalize their markets. In a context of high reliance on trade revenues this could be damaging, if domestic revenues do not replace losses from trade taxes. This is generally the case in developing countries, where trade taxes represent a high share of total revenues. While trade taxes have decreased by about a third as a share of GDP in Africa, they still represent a high share of revenue with some countries raising almost half of their total revenue from trade (e.g. Gambia, Liberia, Namibia, and Ethiopia). Moreover low-income countries still register a higher share of trade tax revenues on GDP, at about 3.5% of GDP as opposed to about 2% for lower middle income ones. In this context of decreased trade revenue, other taxes, and particularly the VAT, have failed to generate the necessary amounts of revenue to replace losses from trade revenue (Baunsgaard and Keen, 2010). The process of trade liberalization therefore may imply substantial revenue losses in developing countries and particularly in Africa. It is therefore important to strengthen the capacity of countries to raise revenue from domestic sources to replace potential losses from trade taxes, and allow Africa to reap the potential benefits of further integration with the global economy.

Problem Statement

Strategy implementation is a hot topic in management today MCE (2013). After the exciting and creative process of formulating the new strategy, management is often very concerned when it comes to the implementation of their brand new strategy. Their main challenge then becomes how they can get from great plans for a successful future to actions that will actually create these successes for the organization. Once the strategies have been formulated, successful strategy implementation

remains a major challenge and must be controlled and evaluated in order to ensure that the objectives of the organization are achieved (Buul, 2010).

Taxation system in Kenya has been an issue of debate, various scholars have tried to look at the taxation system and the level of compliance in different industry and recommendations have been made on various ways of improving the compliance level. No studies has looked at the effect of taxation system on the economic growth and the ways of shifting from PAYE tax to VAT i.e. future tax which is based on consumption. Most developed countries has the majority of their revenues coming from this future taxation system with up to over 50% of the country's revenue generated from VAT. This study therefore sought ways and means by which Kenya can achieve a high economic growth through future taxation. The study try to explore possible ways of shifting from high PAYE income revenue to high VAT revenue (Toder and Alan, 2014).

Following the enactment of the VAT Act 2013, there was expectation that VAT performance would significantly improve VAT performance. VAT performance in Kenya has declined over the years till by 2012/13 it accounted for 5.1% of GDP or 24% of revenues. Recommended practice is for VAT, as a broad based consumption tax, to account for at least 35% of total revenue. VAT also dominates domestic indirect taxes in Kenya accounting for 61% of domestic indirect taxes. Domestic indirect taxes have underperformed compared to direct taxes. Hence, scaling up VAT performance will also help rebalance the direct/indirect taxes mix. It is because of this gap that the researcher tries explore means on ways in which Kenya can attain a high VAT revenue (KRA, 2014).

General Objective

The general objective of the study is to assess how taxation system affects the economic growth and ways by which Kenya can shift from high PAYE revenue to high VAT revenue.

Specific Objective

- i. Policy framework as strategy implementation gaps
- ii. Environmental dynamism as strategy implementation gaps

LITERATURE REVIEW

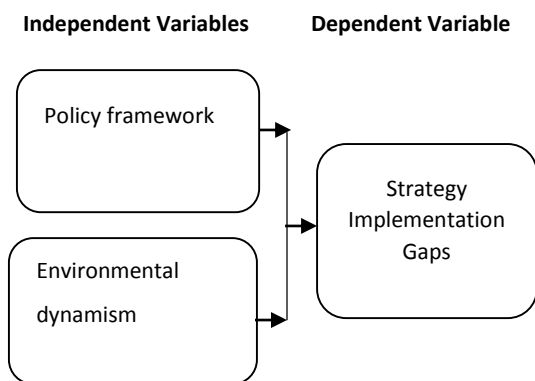
This report will be structured in such a way that it will outlines the emerging challenges faced by the tax and transfer system, and sets out a broad overview of the findings and recommendations. It will also give a detailed analysis for each area of the tax and transfer system.

Theoretical Framework

In simple terms, taxation can be defined as a process through which a country generates its revenue (Diamond, 2008). Although this definition is very simple it does not specify what actions are required in taxation system. To elaborate the issues and activities involved in taxation system, multiple taxation theories are used as below.

Conceptual Framework

This study has made use of both the Dependent and Independent Variables. In the measurement of the independent variables, effectiveness of the various components of strategy implementation was assessed. This study, proposes to explain the variable interplay as illustrated in the diagram below.



Empirical review

Policy framework as strategy implementation gaps

The tax system serves an important role in funding the quality public services that benefit individual members of the community as well as the economy more broadly (Agbeyegbe, 2004). Through its design it can have an important impact on the growth rate and allocation of resources in the economy. Raising revenue should be done so as to do least harm to economic efficiency, provide equity (horizontal, vertical and intergenerational), and minimize complexity for taxpayers and the community (Zafar, 2005).

Over the past 50 years, Kenya’s tax system have undergone an almost continual process of reform in response to a changing policy context and as problems have been identified with existing policy settings. These reforms have underpinned Kenya’s fiscal position and the fairness of the tax and transfer system and contributed to Kenya’s strong economic performance in the region. In particular, this reform process has contributed to the remarkable resilience of the Kenyan economy. Kenya has been the strongest-performing developing economy in the East Africa. The country’s per capita income has moved up while an equitable pattern of overall income distribution has been maintained (Murithi & Moyi, 2013).

The structure of tax receipts in the United States compared with the OECD average is characterized

by: Higher revenues from taxes on personal income, corporate income and property. A lower proportion of revenues from taxes on goods and services, and social security contributions and final no revenues from payroll taxes. The United States is the only OECD country that employs a retail sales tax rather than a value added tax (VAT) as the principal consumption tax. However, the retail sales tax in the United States is not a federal tax. Rather, it is a tax imposed at the state and local government levels. Currently, 45 of the 50 States impose general retail sales taxes as do thousands of local tax jurisdictions whose levies generally are identical to the state levies and are administered by the State (OECD, 2012).

Retail sales taxes and VAT belong to the same category (Taxes on general consumption) in the OECD classification of taxes. Compared to the other OECD countries, the United States has the lowest proportion of revenue from general consumption in its total tax revenue (8%), far below the OECD average (20.2%).

If “tax reform” is defined as base-broadening, rate reducing changes that are neutral with respect to the pre-existing revenue levels and distributional burdens of taxation, then tax reform is a rare event in modern U.S. history. While virtually every commission that looks at tax reform suggests proposals along these lines see, for example, the Bowles-Simpson National Commission on Fiscal Responsibility and Reform (2010), the Domenici Rivlin Debt Reduction Task Force (2010), and President Bush’s tax reform commission (President’s Advisory Panel 2005)—policy makers rarely follow through. Indeed, only the Tax Reform Act (TRA) of 1986 would qualify, among all legislative events in the last fifty years. Representative Camp’s recent proposal would also qualify, but of course it has not been enacted (Kariba, 2011).

McCulloch, Winters and Cirera, (2010) defined VAT by constraints that govern its scope, most particularly the level of the overall rate and of reduced rates, the amount and types of exemptions, and a number of administrative provisions regarding the way in which economic agents must behave (thresholds for registration as taxpayers, frequency of declarations and payments, rules on cross-border trade, etc.). The EU has attempted over the years, in line with the objectives of the Single Market, to harmonize these parameters with a series of Directives. Currently, the VAT Directive, enacted on January 1, 2007 and replacing the Sixth Directive, contains all legislations concerning the common VAT system in place. The Directive does not stipulate one uniform percentage rate for the whole Union, but sets boundaries for the Member States. For example, it restricts the minimum standard rate to 15 percent (this regulation has been extended to 31 December 2015) and allows for two reduced rates of at least 5 percent for goods and services listed in the Annex III of the EU VAT Directive (2006/112/EC). Some derogations and exceptions for Member States are in place, entailing the existence of exemptions, zero rates and super reduced rates (Agina, 2014).

Environmental dynamism as strategy implementation gaps

The comprehensive review of Kenyan tax system will examine and make recommendations to create a tax structure that will position Kenya to deal with the demographic, social, economic and environmental challenges of the 21st century and enhance Kenya's economic and social outcomes. The review will consider:

- The appropriate balance between taxation of the returns from work, investment and savings, consumption (excluding the GST) and the role to be played by environmental taxes;

- Improvements to the tax and transfer payment system for individuals and working families, including those for retirees;
- Enhancing the taxation of savings, assets and investments, including the role and structure of company taxation;
- Enhancing the taxation arrangements on consumption (including excise taxes), property (including housing), and other forms of taxation collected primarily by the States;
- Simplifying the tax system, including consideration of appropriate administrative arrangements across the Kenyan government; and
- The interrelationships between these systems as well as the proposed emissions trading system.

RESEARCH METHODOLOGY

Introduction

This chapter describes the research design employed in this research.

Research Design

The research design constitutes the blueprint for the collection, measurement, and analysis of data. It is a plan and a structure of investigation so conceived as to obtain answers to research questions. The plan is the overall scheme or program of the research. The research design is the plan aimed at achieving the objective (Cooper and Schindler, 2011).

This study was a comparison study to other countries that have adopted high VAT policies. The study used data collected in Kenya and compared to some of the European countries that have a high VAT collection. Research designed that was used in this study was inferential in nature. According to Pride and Ferrell (2008), inferential statistics discovers and measures cause and effect relationships among variables.

Population and Sampling Design

Population

Population is the set of all the individual of interest in a particular study (Gravetter & Willnau, 2007). The study was to determine how Value Added Tax system design affected tax compliance. The population was the entire economic performance data from 2010 to 2013. The study examined Kenya's budget for ten years and compared with Singapore's budget for the same period. The study picked on Singapore economy because the two country at one point were at par. The population consisted of the two country's actual income and expenditure for the same period.

Sampling Technique

The sampling technique employed in this study was a non-probabilistic sampling. The researcher studied the variable under the study using the most recent data available from Kenya and Singapore.

Sampling Size

According to Dodge (2003), sampling size is the number of sampling units which are to be included in the sample. The sample was selected from the years between 2010 and 2013.

Data Collection Methods

The main method of data collection in this study was desk study. Secondary data is data used for a research project that was originally collected for some other purpose. Data analysis involves reducing accumulated data to a manageable size, developing summaries, looking for patterns, and applying statistical techniques (Cooper and Schindler, 2011). The data that was used included documents and historic data. Its purpose was to help form a good understanding of the taxation system and measures to be taken in order for the country to realize a meaningful economic growth. Two checklists were used to collect data. The first one was used to collect data on the Kenyan revenue and Source of the revenue whereas the second checklist was used to

collect data from Singapore's revenue and sources of the revenue for the period under the study.

Data Analysis

Data analysis was done by use of inferential statistics where Correlation and regression analysis was used for this study that covered the period between 2010 and 2013. Also to be determined in the study was the mean and standard deviation of the variables under the study. Regression and correlation analysis was used to establish the relationship between taxation system and economic growth of the country. The independent variable used in the analysis was the taxation system whereas the dependents variable were the economic growth that depend on the taxation system of the specific country under the study. The trend of Kenyan revenue was analyzed during the period selected and compared with Singapore's revenue for the same period. Inferences were made based on the data obtained during this period for the two countries. The study finally made recommendations on how Kenya was to achieve economic growth through the shift from pay as you earn (PAYE) to the tax of the future, i.e. Value Added Tax (VAT).

The results were interpreted based on the correlation coefficient. $P=1$ indicates that there is a positive correlation, whereas $p= -1$ indicates a perfect negative correlation and finally $p= 0$ indicates no linear relationship between the two variables.

The value of the sample correlation coefficient was used as an estimate of the true population correlation. Large correlation coefficient indicated that one variable had a huge influence on the other variable or the relationship was causal or the variables being correlated had a number of causes in common. On the other hand, small correlations indicated that the variables were possibly not linearly related.

A test for the significance of the correlation was added. This test was added to find out if the value was significantly greater than zero. 5% significance level was used. The alternate hypothesis of the study was that future taxation system stimulates high economic growth.

RESULTS AND FINDINGS

This chapter presented the results and findings of the study. The purpose of this study was to assess how taxation system affects the economic growth and ways by which Kenya can shift from high income taxes revenue to high VAT revenue. The study relied predominantly on secondary data.

Revenue Collected

Figure 1 shows the trend of the revenue collected in Kenya for the period between 2010 and 2013. From the figure, it is clear that the amount of revenue collected in form of taxation has been gradually increasing for the past four years.

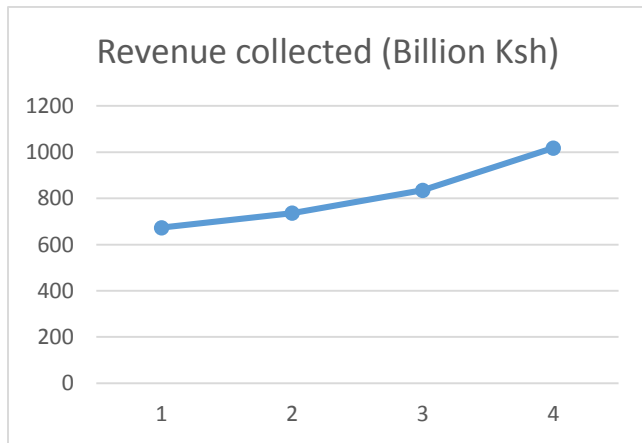


Figure 1: Total revenue collected

1	2	3	4
Year 2010	Year 2011	Year 2012	Year 2013

Kenya VAT Trend

Figure 2 shows the trend of the proportion of VAT revenue collected in Kenya for the period between 2010 and 2013. From the figure, it is clear that the amount of VAT collected has been dwindling for the past four years despite total revenue increasing.

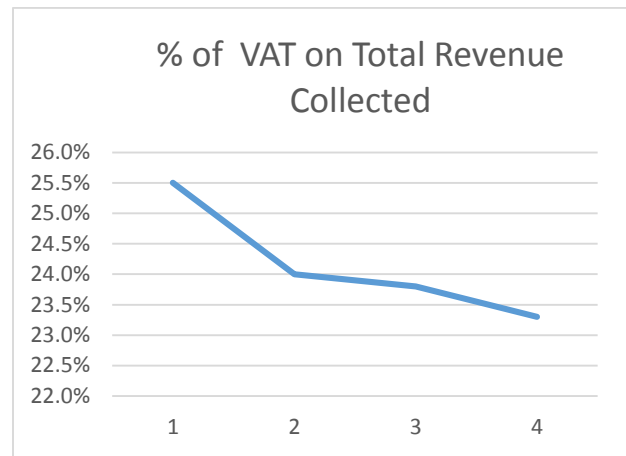


Figure 2: Proportion of VAT to the Total revenue collected

Kenya GDP Trend

Figure 3 shows the trend of the proportion of GDP in Kenya for the period between 2010 and 2013. The figure shows that GDP had a significant drop in the year 2011 before picking up gradually in 2012 and 2013.

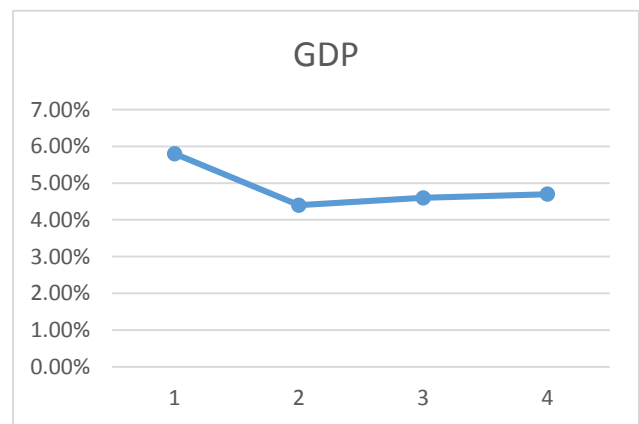


Figure 3: GDP growth

Inflation Rate

Figure 4 shows the inflation rate experienced in Kenya for the period between 2010 and 2013. In the figure, inflation stood at its highest rate of 14% in the year 2011 before dropping to 9.4% in 2012 and 4.6% in 2013.

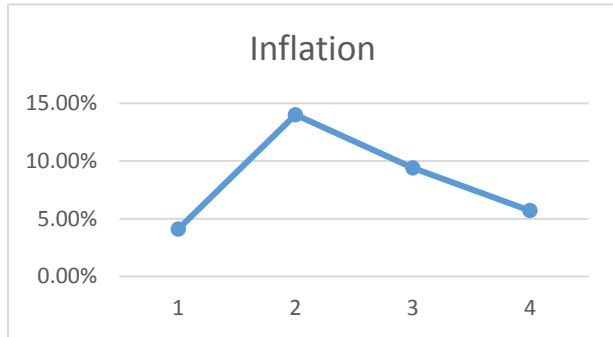


Figure 4: Inflation rate.

Policy framework as strategy implementation gaps

Table 1 shows the results obtained from a correlation between the proportion of VAT on total revenue collected against and the economic growth measured in GDP. From the table, GDP obtained a Pearson correlation value of +0.876 and a significance value 0.124.

Table 1: Correlation of GDP on VAT

Correlations			
		GDP	% of VAT on Total Revenue Collected
GDP	Pearson Correlation	1	.876
	Sig. (2-tailed)		.124
	N	4	4

Regression was also carried out to establish whether there existed a relationship between VAT collected and economic growth and whether the movement

could be predicted with changes in the Vat collected. In table 2, an R square of 0.767 was obtained that was adjusted to 0.650 with a standard error of 0.372.

Table 2: Regression of GDP on VAT

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.876 ^a	.767	.650	.372
a. Predictors: (Constant), % of VAT on Total Revenue Collected				

This study was carried to establish whether economic growth (GDP) depends on the VAT generated by a country. For the Kenyan case, the

study established a -1.673 at a confidence interval of 95% with a significance value 0.124 as shown in Table

3. This illustrates that the countries VAT does have a positive significance on the economic growth.

Table 3: GDP and % VAT

Coefficients ^a							
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
	B	Std. Error	Beta			Lower Bound	Upper Bound
(Constant)	-9.175	5.483		-1.673	.236	-32.767	14.417
% of VAT on Total Revenue Collected	.582	.227	.876	2.564	.124	-.395	1.558

a. Dependent Variable: GDP

Environmental dynamism as strategy implementation gaps

Table 4 show a correlation between GDP and revenue collected in terms of taxes. This was carried out to establish whether revenue collected in form

of taxes has impact on the growth of the economy holding other factors constant. In the table, the study established a Pearson correlation value of 0.474 at a significance of 0.526. This shows that the relationship is not significant since the P value is > 0.1.

Table 4. Correlation of GDP and Revenue Collected.

Correlations			
		GDP	Revenue collected (Billion Ksh)
GDP	Pearson Correlation	1	.474
	Sig. (2-tailed)		.526
	N	4	4
Revenue collected (Billion Ksh)	Pearson Correlation	.474	1
	Sig. (2-tailed)	.526	
	N	4	4

ANOVA on % VAT and Inflation

The analysis of variance showed that the inflation significantly affect the amount of VAT collected, F (.329) = 8.212. The ANOVA table produced an f-

statistic of .329 while the p-value was .024 as shown in Table 5. This shows a significant relationship between inflation and VAT collected.

Table 5: ANOVA on % VAT and Inflation

ANOVA ^a					
Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	8.212	1	8.212	.329	.024 ^b
Residual	49.888	2	24.944		
Total	58.100	3			
a. Dependent Variable: Inflation					
b. Predictors: (Constant), % of VAT on Total Revenue Collected					

Regression of % of VAT on Total Revenue Collected and GDP

Regression analysis was carried out to establish whether GDP has a linear dependence on the proportion of VAT on Total revenue collected. An R-square value of 0.141 was established and adjusted

to 0.288. The coefficient of determination established that VAT influenced GDP by 28.8%. The coefficient of determination (R^2) showed a strong positive relationship as the value of R^2 was equal to 0.1 ($R^2 > 0.1$). Durbin Watson value of 2.284 was established illustrating lack of non-autocorrelation in the model residuals as shown in Table 6.

Table 6: Regression of % of VAT on Total Revenue Collected and GDP

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.376 ^a	.141	.288	4.994	2.284
a. Predictors: (Constant), % of VAT on Total Revenue Collected					

ANOVA on Revenue Total Collected and VAT Collected

The analysis of variance showed that the effect of culture is significantly shown in company performance, $F(155.71) = 66950.524$. The ANOVA table produced an f- statistic of 155.713 while the p-

value was .006 as shown in Table 7. This shows a significant relationship between revenue collected and the amount of VAT collected since the significant value is $< .01$.

Table 7: ANOVA on Revenue Total Collected and VAT Collected

ANOVA ^a						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	66950.524	1	66950.524	155.713	.006 ^b
	Residual	859.924	2	429.962		
	Total	67810.448	3			
a. Dependent Variable: Revenue collected (Billion Ksh)						
b. Predictors: (Constant), VAT (Billion Ksh)						

DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

This chapter provides a summary of discussion, conclusions and recommendations of the study.

Summary

The purpose of this study was to assess how taxation system affects the economic growth and ways by which Kenya can shift from high income taxes revenue to high VAT revenue. The study was guided by the following specific objectives: Policy framework as strategy implementation gaps and Environmental dynamism as strategy implementation gaps. The study also adopted the use of a conceptual framework to elaborate the complexity of taxation system.

Inferential statistic research design was used. Secondary data was used and it was collected from the World Bank website, International Monetary Funds, OECD website, Kenya Revenue Authority and the Central Bank of Kenya. Regression, correlation statistical analysis was employed. Data analysis was done using Statistical Package for Social Science (SPSS) and results presented in form of tables and figures.

Discussion

Policy framework as strategy implementation gaps

From the study, the correlation between the proportion of VAT on total revenue collected against and the economic growth measured in GDP was established. GDP obtained a Pearson correlation value of +0.876 and a significance value 0.124. This denotes that there was no significant relationship between GDP and % VAT on the Total revenue collected. This concurs with Zafar, (2005) who noted that through its design it can have an important impact on the growth rate and allocation of resources in the economy. Raising revenue should be

done so as to do least harm to economic efficiency, provide equity (horizontal, vertical and intergenerational), and minimize complexity for taxpayers and the community.

The study was carried to establish whether economic growth (GDP) depends on the VAT generated by a country. For the Kenyan case, the study established a -1.673 at a confidence interval of 95% with a significance value 0.124 as shown in Table 3. This illustrates that the countries VAT does have a positive significance on the economic growth. This findings is also in line with OECD, (2012) report that the structure of tax receipts in the United States compared with the OECD average is characterized by: Higher revenues from taxes on personal income, corporate income and property. A lower proportion of revenues from taxes on goods and services, and social security contributions and final no revenues from payroll taxes. The United States is the only OECD country that employs a retail sales tax rather than a value added tax (VAT) as the principal consumption tax. However, the retail sales tax in the United States is not a federal tax. Rather, it is a tax imposed at the state and local government levels. Currently, 45 of the 50 States impose general retail sales taxes as do thousands of local tax jurisdictions whose levies generally are identical to the state levies and are administered by the State

Retail sales taxes and VAT belong to the same category (Taxes on general consumption) in the OECD classification of taxes. Compared to the other OECD countries, the United States has the lowest proportion of revenue from general consumption in its total tax revenue (8%), far below the OECD average (20.2%). This was the case for Kenya in this study's findings as for the Kenya case, the country has a high proportion of revenue from general consumption in its total tax revenue above the OECD average.

While virtually every commission that looks at tax reform suggests proposals along these lines see, for example, the Bowles-Simpson National Commission on Fiscal Responsibility and Reform (2010), the Domenici Rivlin Debt Reduction Task Force (2010), and President Bush's tax reform commission (President's Advisory Panel 2005)—policy makers rarely follow through. Indeed, only the Tax Reform Act (TRA) of 1986 would qualify, among all legislative events in the last fifty years. Representative Camp's recent proposal would also qualify, but of course it has not been enacted (Kariba, 2011).

McCulloch, Winters and Cirera, (2010) defined VAT by constraints that govern its scope, most particularly the level of the overall rate and of reduced rates, the amount and types of exemptions, and a number of administrative provisions regarding the way in which economic agents must behave (thresholds for registration as taxpayers, frequency of declarations and payments, rules on cross-border trade, etc.). The EU has attempted over the years, in line with the objectives of the Single Market, to harmonize these parameters with a series of Directives. Currently, the VAT Directive, enacted on January 1, 2007 and replacing the Sixth Directive, contains all legislations concerning the common VAT system in place. The Directive does not stipulate one uniform percentage rate for the whole Union, but sets boundaries for the Member States. For example, it restricts the minimum standard rate to 15 percent (this regulation has been extended to 31 December 2015) and allows for two reduced rates of at least 5 percent for goods and services listed in the Annex III of the EU VAT Directive (2006/112/EC). Some derogations and exceptions for Member States are in place, entailing the existence of exemptions, zero rates and super reduced rates (Agina, 2014). The case is not different in the Kenyan perspective as the country try to gear up for a high VAT revenue.

Environmental dynamism as strategy implementation gaps

On the environmental dynamism and strategy implementation gaps, correlation between GDP and revenue collected in terms of taxes was carried out to establish whether revenue collected in form of taxes has impact on the growth of the economy holding other factors constant. The study established a Pearson correlation value of +0.474 at a significance of 0.526. This shows that the relationship is not significant since the P value is > 0.1. According to Muriithi and Moyi (2003), the comprehensive review of Kenyan tax system will examine and make recommendations to create a tax structure that will position Kenya to deal with the demographic, social, economic and environmental challenges of the 21st century and enhance Kenya's economic and social outcomes. The review will consider: The appropriate balance between taxation of the returns from work, investment and savings, consumption (excluding the GST) and the role to be played by environmental taxes; Improvements to the tax and transfer payment system for individuals and working families, including those for retirees; Enhancing the taxation of savings, assets and investments, including the role and structure of company taxation; Enhancing the taxation arrangements on consumption (including excise taxes), property (including housing), and other forms of taxation collected primarily by the States; Simplifying the tax system, including consideration of appropriate administrative arrangements across the Kenyan government; and the interrelationships between these systems as well as the proposed emissions trading system was key to the growth of the economy irrespective of the environmental dynamics.

The analysis of variance showed that the inflation significantly affect the amount of VAT collected, $F(0.329) = 8.212$. The ANOVA table produced an f-

statistic of .329 while the p-value was .024 as shown in Table 4.5. This shows a significant relationship between inflation and VAT collected. IMF (2003) indicted that Kenya's tax system performance has been better than average as compared to other African countries in the past three decades. Kenya achieved a tax revenue collection of 23.3% of GDP in 1989/90. Revenue collection peaked in 1995/96 at 30.4% of GDP, as a result of economic liberalisation, and thereafter, declined to 20.5% of GDP in 2002/03, before increasing to 22.0% in 2007/08. This superior performance was attributed to a stronger tax administration system and a relatively large formal sector. The reforms of the 1970s and early 1980s, as well as the introduction of VAT in 1990, which widened the tax base, enabled GoK to mitigate for revenue losses resulting from the reduction in and removal of import and export tariffs, which were imposed both by global (WTO) conventions, as well as the structural economic adjustment measures. Empirical analysis by Muriithi and Moyo (2003) suggests that tax reforms in Kenya under the TMP have led to improved productivity of direct taxes. In particular, administrative reforms (e.g. lower tax rates, PIN etc.) aimed at eliminating "avenues for evasion and corruption". However, Kenya's performance effectiveness indicators suggest that whilst the tax effort is high, there is potential to increase tax revenue collection as a percentage of GDP by reducing the tax gap

Conclusions

Policy framework as strategy implementation gaps

As to whether there is policy framework and strategy implementation gaps, the study established that there exist a policy framework. The gaps that mainly exhibited in this study was the compliance gaps. The country's economy is largely informal and compliance is had to attain. Through its design it can have an important impact on the growth rate and allocation of resources in the economy. Raising

revenue should be done so as to do least harm to economic efficiency, provide equity (horizontal, vertical and intergenerational), and minimize complexity for taxpayers and the community.

Environmental dynamism as strategy implementation gaps

The issue of whether there is environmental dynamism and strategy implementation gaps was looked at and the study established that there existed some implementation gaps mainly due to the nature of the economy of the country. The country's economy is largely informal and implementations of the policies is tedious. As compared to the structure of the US where tax receipts in the United States compared with the OECD average is characterized by: Higher revenues from taxes on personal income, corporate income and property. A lower proportion of revenues from taxes on goods and services, and social security contributions and final no revenues from payroll taxes, Kenya exhibited the opposite of this.

Recommendations

Policy framework as strategy implementation gaps

From the study, we established that there existed a compliance gap for the VAT. Currently under the VAT system, one is required to pay VAT on invoicing or delivery of goods while the business terms are negotiated and agreed between customers and in most cases payments is received after thirty to sixty days after delivery or invoicing. The requirement to pay on delivery of goods or invoicing cause serious cash flow the in return discourages most tax payers to comply. The study recommends that the Kenya Revenue Authority (KRA) should simplify the VAT system to make it easy for the tax payers to comply. KRA should engage in continuous improvement of VAT registration and administration. There is need to fix the law to match the business practice.

Environmental dynamism as strategy implementation gaps

Introduction of withholding tax in Kenya where the suppliers to the government and government agencies are required to withhold 6% of the value of supply as Vat and source while already tax payers has paid full output VAT at the point of invoicing or delivery cash further cash flow problems and discourages compliance. There is need to withdraw withholding requirement. This policy is further discriminatory in nature since it applies to only those supplying to the government and not the private sector.

Suggestion for Further Study

Effective taxation is vital to the growth of any economy. Studies have established that countries with high VAT revenue are the most developed. This study sought to establish the ways in which Kenya could shift from high income taxes to high VAT. The study also established that for the Kenya case, policies to raise the proportion of VAT was in place and that the compliance gap was the main hindrance to achieving the set targets. It is therefore this study's recommendations that further research been carried out on the factors hindering compliance of VAT in Kenya to address the issue of non-compliance.

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