



# **The tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District**

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# DECLARATION

I, Lungisani Lucky Buthelezi, declare that this dissertation is a representation of my own work in conception and execution. This work has not been submitted in any form for another degree at any university or institution of higher learning. All information cited from published or unpublished works have been acknowledged.

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## ABSTRACT

Several attempts have been made to examine the effect of tax compliance burden in the functioning of small and medium-sized enterprises (SMEs) but to date, tax compliance is still a constraint in the functioning of SMEs. The purpose of this research was to evaluate the tax compliance burden in the functioning of SMEs in the Durban Central Business District.

The study examined the effect of tax compliance burden using a quantitative method, with data collected via questionnaires from SMEs and tax practitioners in the Durban Central Business District. The latest version of the Statistical Package for Social Sciences V1.0.0.1406 was used to analyse the results.

The study found that SMEs and tax practitioners both agreed that the tax compliance burden has a significant impact on the failure, performance, and growth of SMEs. They also agreed that high tax rates encourage noncompliance with tax laws, leading to SMEs concealing profits and a significant number of SMEs remaining in the informal sector. The analysis revealed that almost all the SMEs had never received any tax training and that SMEs rely on the services of tax practitioners to be tax compliant. SMEs and tax practitioners agreed that being tax compliant benefits SMEs. Low tax rates, electronic filing and payment of taxes, and government payments to tax practitioners to provide free services to SMEs in tax filing and record keeping are all very important in lowering tax compliance costs, as is frequent tax education, with practical and simplified tax laws. These results demonstrate that tax compliance burden is a constraint in the functioning of SMEs.

The study recommends that the South African Revenue Service assists SMEs in reducing their tax compliance burden by increasing tax education and tax incentives for SMEs, paying tax practitioners to provide free services to SMEs or by assigning a tax practitioner to an SME for its first five years of operations.

**Key words:** Small and medium-sized enterprise, tax practitioners, taxation, compliance burden, South African Revenue Service.

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## ACRONYMS

DTC	Davis Tax Committee
DTI	Department of Trade and Industry
DSBD	Department of Small Business Development
ECTC	European Commission of Tax Consultants
E-filing	Electronic Filing
GDP	Gross Domestic Product
ITR	Income Tax Return
NPC	National Planning Commission
OECD	Organization for Economic Development and Cooperation
PAYE	Pay-As-You-Earn
SAICA	South African Institute of Chartered Accountants
SARS	South African Revenue Service
SBC	Small Business Corporation
SBP	Small Business Project
SBTC	Small Business Tax Credit
SEDA	Small Enterprise Development Agency
SDL	Skills Development Levy
SME	Small and Medium-sized Enterprise
Stats SA	Statistics South Africa
TRA	Tanzania Revenue Authority
UIF	Unemployment Insurance Fund
UK	United Kingdom
USAID	United States Agency for International Development
VAT	Value-added Tax

# CHAPTER ONE

## INTRODUCTION

### 1.1 Background

According to Sephapo, Cant, and Wiid (2016), tax laws are a burden to small and medium-sized enterprises (SMEs) because of the numerous tax returns that must be filed, and preparing, completing, and filing the tax returns costs a lot of money. Tax registration processes are complex, and they require a lot of time and SMEs are unsure where to begin with the preparation, completion, and submission of their tax returns (Sephapho *et al.*2016). This is supported by the International Trade Centre (ITC) (ITC 2016), who state that SMEs must comply with a variety of tax laws, including maintaining proper records, undertaking tax planning, hiring professionals to complete and file returns, and gaining enough knowledge to allow these obligations to be met correctly. Tax laws are viewed as a burden as much time is spent addressing tax regulations and this has an impact on business productivity (Sephapho *et al.* 2016). The costs incurred in the performance of these activities are usually a significant part of SMEs' costs (ITC 2016) which might reduce small businesses' profitability and limit economic growth (Smulders, Stiglingh, Franzen and Fletcher 2016).

### 1.2 Prior literature and contribution of this study

Although empirical research on tax compliance costs is limited, surveys have been steered in various countries and regions around the world, including South Africa (Smulders *et al.* 2016) and Indonesia (Savitri 2016). According to a survey conducted by Smulders *et al.* (2016), there is a substantial optimistic relationship between revenue and tax obedience costs because increased turnover results in increased documentation, which may need to be presented to revenue authorities as proof of income. The increase in tax compliance costs due to record-keeping, on the other hand, should be minor (Smulders *et al.* 2016).

Matarirano, Chiloane-Tsoka, and Makina (2019) state that compliance costs incurred by SMEs have a noteworthy effect on their performance since SMEs are resource compelled and cannot afford to spend resources on non-value adding activities such as tax compliance; thus, the South African tax system is contrary to the principles of a good tax system from the perspective of small businesses. The tax system imposes a significant burden on small business taxpayers,

particularly in the form of external tax compliance costs, and as such, it must be carefully scrutinised (Matariano *et al.* 2019). Tee, Boadi and Opoku (2016) highlight that taxes imposed on SMEs have a variety of effects on their profit growth. Tax payments reduces the buying influence of SMEs (Tee *et al.* 2016). Ameyaw, Korang, Twum, Owosu and Asante (2016) conclude that tax policies pose a serious threat to SMEs in terms of tax payments, which affects the profitability of SMEs' business operations. Tax policies were found to affect tax compliance by SMEs (Ameyaw *et al.* 2016). Tax compliance costs affect small business attitude and behaviour towards being tax compliant due to their regressive nature and they may also result to SMEs having lower tax compliance levels than larger taxpayers (Mahangila 2017).

According to the World Bank Group (2016), one of the key considerations for the SMEs sector when deciding whether to establish, relocate, or expand its operations is the level of taxation because a high tax burden and the cost of complying with tax regulations discourage SME sector growth. This is supported by Smulders *et al.* (2016) who stated that an increase in the turnover of a business results in an increase in its tax compliance costs. As a result, tax compliance costs may overburden SMEs and, in some cases, force SMEs to close their doors or refuse to comply with tax laws (World Bank Group 2016). This is confirmed by Damayanti and Matasik (2021) who concluded that an increase in tax compliance costs of SMEs may influence the compliance behaviour levels as businesses may consider the tax system to be unfair.

The above literature review confirms that complicated tax requirements are an impediment for SMEs that want to be tax compliant. As this topic has not been investigated before using SMEs in the Durban Central Business District, this study seeks to assess the tax compliance burden in the functioning of small businesses in the Durban Central Business District.

### **1.3 Problem statement**

Zachary *et al.* (2017) argue that SMEs incur various tax compliance costs, the most significant of which are the costs of submitting and filing tax returns. SMEs therefore contend that compliance costs negatively and disproportionately affect their businesses' functioning and performance (Zachary *et al.* 2017).

To reduce the time and high costs of collecting and submitting taxes by the South African Revenue Service (SARS), as well as the cost of filing and paying taxes by SMEs, the government has instigated numerous incentives for small business owners, such as allowing small businesses not to pay tax on the first R78 750 taxable income and also allowing small business corporations to pay tax at a progressive rate beginning at 7% to 21% of taxable income exceeding R365 000 and 28% on taxable income exceeding R365 000 (SARS 2019). While the government has made efforts to assist the SME sector over the last twenty years or so, much more work is required to assist the SME sector in reducing their tax compliance burden (Botha, Smulders, Combrink and Meiring 2020). The inducements introduced by the government to support this sector needs to be stratified and targeted; for example, it should be based on the size of the business (Botha *et al.* 2020).

The above discussion indicates that tax compliance costs are constraints in the functioning of SMEs and that they may also result in many small businesses failing to do well and surviving. This has led to a need to assess the tax compliance burden in the functioning of SMEs in Durban Central Business District.

#### **1.4 Research aim, objectives and questions**

The aim of the study is to assess the effect of the tax compliance burden in the functioning of SMEs in the Durban Central Business District.

The following objectives were set to achieve the aim of this study.

- To identify the effect of tax compliance costs in the functioning of SMEs,
- To examine the level of tax knowledge of SMEs,
- To determine the costs incurred by SMEs to be tax compliant,
- To evaluate whether SMEs use tax incentives and record keeping to reduce costs of being tax compliance, and
- To assess any benefits for being tax compliant.

The study uses the perspectives of two different target groups, namely SMEs and tax practitioners, to meet the above objectives.

**The following research questions were set to determine the perspectives of the SMEs:**

- 1: What is the effect of tax compliance costs in the functioning of SMEs?
- 2: What is the level of tax knowledge of SMEs?
- 3: What costs are incurred by SMEs to be tax compliant?
- 4: Do SMEs use tax incentives and record keeping to reduce costs of being tax compliance?
- 5: What benefits do SMEs perceive for being tax compliant?

**The following research questions were set to determine the perspectives of the tax practitioners:**

- 6: What costs are incurred by SMEs to be tax compliant?
- 7: Do SMEs use tax incentives and record keeping to reducing the costs of being tax compliant?
- 8: What benefits do tax practitioners perceive for SMEs to be tax compliant?

## **1.5 Significance of the study**

SMEs are widely recognised as important for economic success, serving “not only as job creators but also as sales generators and a source of tax and thus fiscal revenue” (Bruwer, Coetzee and Meiring 2017; Organization for Economic and Development (OECD) 2017). SMEs contribute between 35 and 45 % of the country's GDP and employ between 50 and 60 % of the workforce (Long 2016).

As a result of the significant contribution by SMEs to the GDP and employment, the factors influencing tax compliance are of interest to government policymakers, practitioners, academics, and the public (Jimenez and Iyer 2016). This is because, considering increased government duties and the international monetary recession, governments are attempting to decrease duty elusion and upsurge taxpayer obedience (Jimenez and Iyer 2016).

This research evaluates the effect of tax compliance in the effective functioning of SMEs in the Durban Central Business District. As such the study provides valuable information to SARS on how it can assist SMEs in reducing tax compliance costs. It also assists SMEs and tax practitioners in understanding the factors that contribute to tax compliance.

## **1.6 Organisation of the study**

The dissertation has five chapters which are arranged as follows.

### **Chapter 1: Introduction**

The setting of this study is enclosed by this section through underlining the problem statement, the study's aim and objectives, background and significance of the study.

### **Chapter 2: Literature Review**

Chapter 2 review the existing literature relevant to the study's aim regarding the effect of the tax compliance burden in the functioning of SMEs in the Durban Central Business District.

### **Chapter 3: Research Methodology**

Chapter 3 discusses the research methods used as well as the population, sample and sampling method, the research instrument, the response rate, data preparation and analysis, the limitations, and reliability and validity.

### **Chapter 4: Presentation and Discussion of the Results**

This chapter provides the detailed analysis, interpretation and presentation of the results for this study in relation to the achievement of the research objectives.

### **Chapter 5: Summary, Conclusions and Recommendations**

This chapter presents the summary and conclusions in terms of how this study's research objectives were attained. It also outlines the limitations of this study and makes recommendations for future research.

## CHAPTER 2

### LITERATURE REVIEW

#### 2.1 Introduction

SMEs are regarded as the key in job creation and economic development in developing countries (Calza and Goedhuys 2017: 2; Department of Small Business Development (DSBD) 2016: 21). According to SARS, large corporations accounted for 57.6% (R111.17 billion) of the R193 billion in corporate income taxes collected in 2016, while small businesses accounted for 42.4 percent (R81.83 billion) (SARS 2016:19). The DSBD (2016: 20) reports that in “South Africa, small businesses constitute approximately 98% of all businesses, employ 47% of the labour force and contribute 42% to the GDP”. In the South African *2018 Tax Statistics* report, an annual report which is issued jointly by National Treasury and SARS, it was noted that as of 30 June 2018, 768 687 companies (714 422 as of 30 June 2017) were assessed for tax, with 143 768 companies (129 867 as of 30 June 2017) assessed being small business corporations which paid tax (Statistics South Africa (Stats SA) 2018).

Despite the significant contribution made by SMEs to the economy, roughly 70% of South African SMEs fail in their first year of business, ranking among the highest failure rates in the world (South Africa Government 2016). Furthermore, SMEs' performance and sustainability is poor (Van Scheers 2018: 167). The tax burden has been cited as a factor for the poor performance and ultimate failure of SMEs (Herrington and Kew 2016: 48). The South African Institute of Chartered Accountants (SAICA) argue that SMEs' failure is not driven by the tax compliance burden but that SMEs “largely fail because of cash-flow problems and an inability to manage administrative and business processes” (SAICA 2016). The greatest time-consuming and problematic regulations for SMEs in South Africa are tax compliance issues (Small Business Project (SBP) 2004). Tax registration entails entering the tax system which increases the tax burden on SMEs (Junpath, Kharwa and Stainbank 2016). As a result, even though registered taxpayers benefit from a variety of benefits, including "access to finance, improved access to business opportunities, and improved legal standing," small businesses may be hesitant to enter the formal economy by registering for tax (Junpath *et al.* 2016).

The objective of this chapter is to provide an analysis of the fundamental theoretic concepts that outline the contextual of tax compliance research and discuss relevant research on the topic.

This chapter is organised as follows: firstly, the taxation framework is discussed, followed by the importance of taxation, relevant definitions relating to the characteristics and importance of SMEs as well as the challenges faced by SMEs. Thereafter tax compliance costs are discussed. This is followed by a section on tax compliance costs and SMEs. Subsequently the initiatives to simplify the tax system for SMEs is discussed before the chapter ends with empirical research on the tax compliance costs of SMEs.

## **2.2 Taxation framework**

SME taxpayers in South Africa are obliged to comply with both the Income Tax Act (No. 58 of 1962) and the Tax Administration Act (No. 28 of 2011) (SARS 2019). The previous Act (No. 58 of 1962) was enacted 53 years ago and has since been amended by at least 97 pieces of legislation, resulting in an income tax act that is now complex and fragmented) (SARS 2019). The rules and requirements for calculating taxable income, and thus corporate income tax, are governed by income tax legislation (Income Tax Act No. 58 of 1962).

SARS levies a wide range of taxes on businesses. Corporate income tax is the most common type of tax paid by most businesses. According to the Income Tax Act, “every business registered in South Africa is required to register as a taxpayer’ (No. 58 of 1962). The Income Tax Act (No. 58 of 1962) and the Tax Administration Act (No. 28 of 2011) must be carefully considered, as SMEs must fully comply with the latter act. One of the primary goals of the Tax Administration Act (No. 28 of 2011) is to ensure effective and efficient tax collection. The Tax Administration Act (No. 28 of 2011) not only establishes SARS's duties and responsibilities, but it also specifies the administrative requirements for taxpayers and simplifies their obligations while also explaining what they are entitled to from SARS.

South African SMEs may be subject to eleven different taxes (income tax, capital gains tax (CGT), provisional tax, dividend tax, value-added tax (VAT), employee tax, employment-related levies, customs and excise duties, transfer duty, donations tax, and stamp duty). Small businesses must obtain and complete the prescribed forms as well as make timely submissions



to comply. As a result, compliance necessitates a significant amount of administration and noncompliance may lead to penalties, fines and interest (SARS 2019).

### **2.2.1 Importance of taxation**

The OECD (2016) defines tax as a mandatory payment to the general government with no expectation of a proportional benefit from the taxes paid. Taxation, according to Ponorica and Al-Saedi (2015), is an important factor in determining the business climate and a mechanism for determining government officials' accountability. However, government rules and legislature are regarded as the utmost significant barriers to SME development (Nyamwanza, Paketh, Makaza and Moyo 2016; Herrington and Kew 2017) and the costs of becoming and remaining tax compliant are also a significant impediment to small business performance (Herrington and Kew 2016: 49; Schwab 2016: 324).

The South African government acknowledges the significance of the role played by this sector not only in the economy but to the job creation and therefore has launched numerous initiatives to assist SMEs (National Planning Commission (NPC) 2012; Maye 2014). However, these initiatives often only focus on larger businesses and are not tailored for businesses of various sizes such as SMEs (DSBD 2019). SMEs are also granted with tax incentives to improve their tax compliance and boost their growth (Naicker and Rajaram 2019:126). Tax compliance and development of SMEs in the country remain a challenge, despite the availability of tax incentives and initiatives, and the situation cannot be improved because SMEs do not know which tax benefits are available to them (Maxwell, Lau and Howard 2015: 6).

The next section defines SMEs, their characteristics as well their importance in the economy and the challenges SMEs are facing to be tax compliant.

## **2.3 Small and medium-sized enterprises (SMEs)**

This section outlines the definition and characteristics of SMEs and the role played by the SMEs in the economy.

### **2.3.1 Definition of small and medium-sized enterprises**

There is no agreement on how to define SMEs. It differs from one country to the next (Eniola and Entebang 2015). Furthermore, even within the same jurisdiction, the definition of a small

business for tax purposes can differ. In South Africa, the terms "small business," "small business corporation," and "SMME" are frequently used interchangeably (Smulders and Stiglingh 2012).

The South African Income Tax Act No. 58 of 1962, section 12E (4)(a) refers to Small Business Corporation (SBC) as any close corporation or co-operative or any private company as defined in Section 1 of the Companies Act no 71 of 2008 if at all times during the year of assessment all the holders of shares in that company, co-operative or close corporation and natural persons met the following four requirements:

- Legal entity requirement,
- Holder of shares requirement,
- Gross income limitation requirement, and
- Business activity requirement.

The Small Enterprise Development Agency (SEDA) (2006:3) states that there is no collectively acknowledged description of a small enterprise, but it is usually any enterprise with 50 to 100 workers and includes profit-making enterprises (businesses) as well as not-for-profit enterprises (such as cooperatives).

For this study, the definition of a small business by the National Small Business Act (105 of 1996) as amended is adopted. This defines a small enterprise as any form of business, including cooperatives which are owned by one or more individuals and are involved in any sector of the economy. Based on this Act, SMEs are “defined as any formally registered business operating in any sector of the economy with fewer than two hundred employees, turnover not exceeding R50 million and the total gross value of assets (excluding fixed property) being less than R18 million” (National Small Business Act (105 of 1996)). The reason for the adoption of this definition is that it uses quantifiable criteria, unlike the definition of a SBC in the Income Tax Act.

### **2.3.2 Characteristics of SMEs**

Small businesses employ smaller teams of employees than larger corporations, and SMEs are run entirely by single people or small groups (Ingram 2019). Depending on the industry, a larger small-scale business employs fewer than 100 people (Ingram 2019). Many SMEs operate

from a solitary workplace, wholesale store, or service outlet, and a small business can be run from home without the need for any company facilities (Ingram 2019).

### **2.3.3 The importance of SMEs**

SMEs have long been regarded as job creators, not only in South Africa, but around the world (Singh, Khamba and Nanda 2017). They provide employment for skilled and unskilled workers (Rankin, Darroll, and Corrigan 2013; Makina 2015).

In her 2015 Small Business Development budget speech, Minister Lindiwe Zulu stated that “the government recognised the need to review the policy and regulatory environment” that remains to stymie small business development and competitiveness. This demonstrates that SMEs are critical to the economy of the country and also shows that SMEs South Africa's contribution to the economy is "no different from that of other countries such as the United Kingdom (UK), Australia, Taiwan, Latin America, and the People's Republic of China" (DSBD 2016).

However, small businesses operations are significantly affected by the tax compliance burden (Statistics South Africa (Stats SA) 2017), and, despite the significant role played by SMEs sector, unemployment in South Africa is presently at more than 27 %, while SMEs struggle to be sustainable and grow (Stats SA 2017). Furthermore growth rate of SMEs in South Africa is poor because 50% of SMEs fail to grow in their first year of operation (Cacciotti and Hayton (2015). The time and money spent by small business managers, owners, and employees dealing with tax issues represent an opportunity cost that distracts them from the more important task of running the business (Steele 2009: 91).

The Davis Tax Committee (DTC 2014), in its *Small and medium enterprises: taxation considerations, Interim Report*, states that “tax compliance costs should not stifle SMEs' growth”. This report also suggests that to encourage SME growth, a tax system that is as simple as possible be implemented (DTC 2014). This demonstrates the significance of SMEs to the South African economy, and any barriers to their success, such as tax compliance, should be investigated further.

### **2.3.4 Challenges faced by SMEs**

Regulatory compliance costs are considered material to the growth of SMEs and “valuable resources are consumed in order to ensure that these businesses in South Africa remain compliant with all the applicable laws and regulations” (SBP 2004). These resources could have been used to advance, promote, and strengthen businesses both locally and globally, but they are instead used to meet excessive compliance requirements (SBP 2004).

In South Africa, there is a lot of rules and regulations involved in starting and running a small business, including "registration and compliance with the relevant Acts and regulatory bodies" (SEDA 2016). Complicated tax laws affect SMEs progress (Sitharam 2014). When it comes to small business growth, labour laws are a major issue, particularly when it comes to employee termination (OECD 2015). High labour costs in South Africa also affect SMEs as “high minimum wages are sanctioned by South African labour law” (SEDA 2016).

In order to promote tax compliance and increase tax compliance among SMEs in South Africa, SARS grants SMEs tax incentives and initiatives which include but are not limited to reduced tax rates, accelerated depreciation, CGT relief, some relief from the skills development levy (SDL), a small business tax amnesty, reduced number of VAT returns and an increase in the VAT threshold (Naicker and Rajaram 2019:127), but despite the availability of these tax incentives and initiatives, the tax compliance burden has been distressing the growth and effective functioning of SMEs in South Africa. Tax compliance of SMEs is low as many SMEs are uninformed on the tax incentives and tax initiatives offered to them (Maxwell *et al.* 2015:6).

To summarise, tax compliance is a burden on SMEs and influences their operations. Furthermore, the costs incurred by businesses in paying their taxes have received insufficient attention in public policy debates, particularly in developing countries (Bird 2015).

The following section focuses on the definition of tax compliance costs, the components of tax compliance costs, and the factors that contribute to high tax compliance costs for SMEs.

## **2.4 Tax compliance costs**

Tax compliance costs were defined by Govender (2008) as all expenses incurred in ensuring proper compliance with relevant tax regulations. These costs include the following:

- “Expenses incurred as a result of record retention, filing and sorting records, invoices, and receipts;
- Costs incurred in preparing and submitting all relevant tax returns;
- Costs of external advisors required for tax compliance and/or resolving disputes with tax authorities; and
- Any costs to ensure compliance as well as any incidental costs and travel expenditure”.

Coolidge (2012: 251) provided a more succinct definition, defining tax compliance costs as "the costs incurred by taxpayers in meeting the requirements imposed by tax law and revenue authorities, in addition to the accrual payment of tax; these are costs that would be eliminated if the tax were repealed."

#### **2.4.1 Definition of tax compliance**

Tax compliance is defined as the taxpayers' capability and readiness to observe tax regulations, assert their actual income, and pay the correct amount of taxes on the due date to the appropriate relevant authority or jurisdiction and regulations (Ayuba, Saad, and Ariffin 2016).

Tax compliance costs are divided into two categories for the purposes of this study: administrative compliance and technical compliance. Administrative rules imply filing and making payments, as well as ensuring that the due dates and procedures are followed, whereas the technical aspect refers to the correct tax computation (OECD 2016).

#### **2.4.2 Components of tax compliance costs and tax compliance costs of SMEs**

Eichfelder and Vaillancourt (2014) outline three main key components of tax compliance costs. These are:

- External costs,
- Internal costs and
- Psychological costs.

This study only considers external and internal costs. Tran-Nam *et al.* (2000) defines external costs as additional costs incurred by the business prior to the payment of taxes and it is also considered as an additional financial cost that is dedicated solely to tax compliance. This is the amount incurred in addition to or in addition to the usual and normal payments allocated to

pay, such as employee salaries, utility bills, tax advice from tax advisors, accountants, and lawyers (Tran-Nam *et al.* 2000). Hiring an external accountant to perform accounting work in relation to tax requirements is one example of an external compliance cost (Tran-Nam *et al.* 2000).

Internal costs are the time spent by the company in preparing for tax compliance activities (Tran-Nam *et al.* 2000). They include the number of employees required to do tax-related work and the number of hours each officer spends on their tasks (Tran-Nam *et al.* 2000).

The third component (psychological tax compliance costs) is not the focus of this study (Smulder *et al.* 2016). Psychological costs refer to the fears, stress, and anxiety that a company or its employees experience when dealing with tax issues (Evans, Lignier and Tran-Nam 2013).

Being tax compliant burdens SMEs with paperwork and additional bureaucratic duties which negatively affects their performance (Matarirano, Chiloane-Tsoka and Makina 2019). However, Inasius (2019) argues tax compliance is a significant requirement for personalities and companies in both developed and developing countries, and taxpayers are responsible for correctly reporting income and paying their tax liabilities because paying taxes contributes to the development of the economy, which improves the state of the nation (SARS 2019). Tax compliance is a topical issue for nations around the world because revenue authorities are searching for more revenue to meet the demands for public goods and services (Musimenta, Nkundabanyanga, Muhwezi, Akankunda and Nalukenge 2017).

Despite a 10% increase in SMEs tax compliance between 2011 and 2016, data show that 75% of South African SMEs are still noncompliant (SARS 2016). This is due to the fact that small businesses operate in highly regulated surroundings with various taxes that continuously impose noteworthy burdens on their effective functioning (Atawodi and Ojeka 2012).

Smulders (2006) argued that “compliance with tax laws is onerous and time-consuming.” As noted previously, South African SMEs face many challenges and should be allowed to operate in ways which are not burdensome to them. Abrie and Doussy (2006) claimed that “tax compliance places a heavy administrative burden on SMEs”.

The burden typically consists of three components. First and foremost, there are the taxes themselves (Evans 2008: 447). Second, “there are the efficiency costs (also known as

deadweight losses or excess burden), which involve tax-induced market distortion” (OECD 2009: 16). “Finally, there are the operating costs of the tax system: the costs to the government (which are ultimately borne by taxpayers) of administering and collecting taxes (also known as administrative costs), and the costs expended by taxpayers in complying (or sometimes not complying) with their tax obligations” (OECD 2009). Two broad components have emerged as undeniably important core elements of tax compliance costs (OECD 2009: 16):

- Time spent by taxpayers and unpaid helpers (internal tax compliance costs); and
- Tax consultants' fees (external tax compliance costs).

Tax compliance consumes resources that could be put to better use in other areas of a firm's management. Tax compliance may force SMEs to divert productive resources away from producing goods and services and toward tax compliance (Loayza and Serven 2010). Due to a lack of skilled tax staff, SMEs may need to rely on tax practitioners to be tax compliant (Loayza and Serven 2010). It is assumed that those who do not use these practitioners will carry out these tax compliance activities internally (Lubbe and Nienaber 2012:1).

The outsourcing or meeting tax requirements internally can create incompetence in the business by affecting business activities and its competitiveness, productivity, and, in some cases, survival (Rametse 2010). This situation is being felt both internationally and in South Africa and other parts of Africa (Rametse 2010). Despite several attempts, tax compliance remains a persistent issue, particularly in developing countries (Umar, Derashid and Ibrahim 2017).

### **2.4.3 Reasons for high tax compliance costs**

Tax policy requires looking outside the dimension of tax compliance costs to contemplate the issues that may influence their greatness. In other words, what aspects of a tax or tax system are likely to result in high compliance costs?

The European Commission of Tax Consultants (ECTC) (2007) state that the main reasons for high tax compliance costs are as follows:

- Frequent changes of tax laws.
- Complexity of tax systems (tax systems are more geared to larger enterprises).
- Existence of different tax administrations.
- Incomprehensible language of tax laws, including incomprehensible forms.

- Cost of outsourcing tax services.
- Registration procedures.

The next section discusses tax compliance strategies adopted by SMEs and tax knowledge of SMEs.

## **2.5 Tax compliance costs and SMEs**

### **2.5.1 Tax compliance strategies adopted by SMEs**

Small business compliance strategies are regarded as an additional factor in tax compliance costs because they combine methods for preparing and submitting tax returns and settling assessed tax obligations (Smulders 2013). It entails using a computerised accounting system, filing tax returns, and storing supporting documents (Smulders 2013). It is widely assumed that electronic filing lowers the costs of tax compliance that would otherwise be incurred if a manual system was used (Smulders 2013:105). This is because SMEs that use computerised systems and e-filing are less likely to make errors, reducing the need to hire expensive outside service providers (Smulders 2013). E-filing reduce errors and total tax compliance costs (Yilmaz and Coolidge 2013:3).

It is against this backdrop that this study assesses the tax compliance burden in the functioning of SMEs in the Durban Central Business District. The identification of such factors would improve the quality of small businesses' tax-related decisions. Decisions would include (1) whether to outsource tax tasks, perform them in-house, or outsource some of them partially, and (2) which tasks would be performed in-house, and which would be outsourced. Thirdly (3), how much does it cost a company to outsource or perform the task in-house if some tasks are performed in-house and others are outsourced? Finally, (4) how much time does the entity spend ensuring that all tasks are completed on time, assuming that some are done in-house, and others are outsourced?

The decision to outsource tax tasks or perform them in-house may be dependent of the tax knowledge of the SMEs. This is discussed next.



### **2.5.2 Tax knowledge of SMEs**

Tax knowledge is defined as a taxpayer's understanding of tax laws and regulations (Ayuba *et al.* 2016). Puspita, Subroto, and Baridwan (2016: 139) define tax knowledge as the "taxpayers' understanding of the tax system," which includes:

- “Tax principles,
- Benefits of taxes,
- How to make tax payments,
- Filing of tax returns, and
- Consequences of failure to meet tax responsibilities”.

Tax knowledge is regarded as an effective skill that can improve small business tax compliance (Haber and Reichel, cited in Kamleitner *et al.* 2012). Tax rules, the quality of tax authorities' services, and tax knowledge all have optimistic result on personal tax obedience (Yuestia, Sudjab, Wahyuningsihc, and Mennesd 2019). Blaufus, Eichfelder, and Hundsdorfer (2011) contended that increasing tax knowledge exposes taxpayers to the possibility of tax evasion meaning that a taxpayer with a higher level of tax knowledge will be aware of any loopholes in tax regulation and will be aware of legal ways to reduce or even avoid tax, and highly knowledgeable taxpayers may increase the tax compliance cost of business because highly knowledgeable taxpayers are aware of potential “deductions and tax-related problems and are thus more willing to spend money to obtain external assistance in these areas” (Blaufus *et al.* 2011).

### **2.5.3 Knowledge of e-filing and technology**

South Africa implemented e-filing in 2003, but only for VAT and employment taxes at first. Companies and individuals were able to file their income taxes electronically beginning in 2006 (Coolidge 2012).

In South Africa, e-filing is associated with a 22.4 percent reduction in tax compliance costs. When all other factors are equal, e-filers in South Africa spend approximately 21.8 percent fewer hours on VAT compliance than non-e-filers. Firms can allocate more resources to productive activities if these costs are reduced (Coolidge 2012). In this regard, e-filing has the

potential to lower tax compliance costs for SMEs by simplifying the reporting process, less prone to errors, as well as reducing visits to the tax office (Coolidge, Ilic and Kisunko 2009).

The adoption of e-filing may prove costly for SMEs because it requires an SMEs to spend most of their resources and also their time in learning to use e-filing accurately and proficiently (Yilmaz and Coolidge 2013). It should not be compulsory for SMEs to adopt the use of e-filing until they have necessary resources e.g., electricity, computers, internet and have the computer skill to assist them in navigating the e-filing (Yilmaz and Coolidge 2013).

“Submitting returns through e-filing allows SMEs to file wherever they are, able to retrieve records of all returns submitted through e-filing and obtain tax clearance certificates” (SARS nd). However, evidence suggests that small businesses often require more than a year or two to learn how to e-file before they can expect to benefit from lower tax compliance costs (Coolidge and Yilmaz 2014).

## **2.6 Initiatives to simplify the tax system for SMEs**

The revenue authorities have proposed several initiatives to simplify the tax system for SMEs. These proposed initiatives seek to enhance the creation and extension of businesses (Naicker and Rajaram 2019).

### **2.6.1 South African initiatives**

The South African government recognised the significance of SMEs shortly after 1994, passing the National Small Business Act in 1996 and establishing the first National Small Business Council, which together established the national strategy for the development and promotion of small businesses in South Africa (Maye 2014).

In 2003, the DTI launched its *Integrated Strategy on the Promotion of Entrepreneurship and Small Business* in 2003. The main objective of this integrated strategy was to reduce the regulatory burden on SMEs. It sought to construct an empowering environment for SMEs through three pillars which were:

- “Increasing the supply of financial and non-financial support services;
- Increasing the demand for small enterprise products and services; and
- Reducing small enterprise regulatory constraints” (DTI 2003: 4).

SARS (2005) also acknowledged that too many forms and procedures in filing, as well as the frequency with which tax returns are submitted, increase the tax compliance burden on SMEs. SARS has implemented several tax initiatives to assist businesses in stimulating growth. For example, SARS introduced e-filing of VAT returns in 2001 and employee tax returns in 2008, and it has also made the e@syfile software application available to assist employers in simplifying the employees' tax reconciliation process, as well as promoting e-filing and establishing a SME focused call center (Smulders and Naidoo 2011: 38).

To improve small business tax compliance, SARS also streamlined the registration process by combining the SDL, Unemployment Insurance Fund (UIF), and Pay-As-You-Earn (PAYE) (employee tax) registration forms into one (Smulders and Naidoo 2011: 37). In February 2008, the mandatory VAT registration threshold was raised from R300 000 to R1 million, effective 1 March 2009. (Smulders and Naidoo 2011: 37). SARS also introduced the VAT package for small retailers in April 2005 (Smulders and Naidoo 2011: 37). National Treasury's (2005: 88) initiative to allow small businesses with taxable supplies of less than R1 million to file their VAT returns every four months rather than every two months played a minor but noticeable role in improving SMEs' tax compliance.

According to Abrie and Doussy (2006), a significant number of SMEs in the country are unaware of available tax initiatives, and many believe the tax system is overly complex because they lack the essential tax expertise and SARS campaign to endorse these tax initiatives are deemed ineffective in attracting SMEs to participate (Abrie and Doussy 2006). Venter and De Clerq (2007) state that many SMEs do not take advantage of available support programs not because they want to but the main reasons for not utilising these initiatives are, first, they are frequently uninformed of the various initiatives, and second, the requirements and application processes for these initiatives are a limiting factor (Venter and De Clerq 2007).

In 2009 the government introduced the turnover tax system for SMEs which is a single tax system and replaces income tax, VAT, provisional tax, capital gains tax and dividends tax. It is aimed at reducing and simplifying the tax compliance and administrative burden for small businesses with annual turnovers of R1 million or less (SARS 2020). Qualifying businesses will only have to declare and pay one (1) tax (unless they have a VAT or PAYE option) and they only start paying tax when their annual turnover exceeds R335 000 (SARS 2020). By reducing the number of returns that must be filed, the turnover tax system simplifies the filing

and payment process while also reducing tax compliance and administrative burden (SARS 2019).

In addition, the government established the DTC in 2013, with the goal of examining the tax system and its influence on SMEs. The tax initiatives were implemented to assist SMEs in growing and becoming sustainable, as well as in response to the country's high rate of small business failure and high rate of unemployment (Naicker and Rajaram 2019).

SARS understands the importance of SMEs to the economy and is dedicated to supporting their growth and that they prosper (SARS 2017), but the current tax relief initiatives introduced are ineffective, and the general perception amongst small business owners is that the government should introduce more initiatives to assist SMEs (Naicker and Rajaram 2019).

The following section discusses relevant international initiative to simplify tax for SMEs.

### **2.6.2 International initiatives**

In Tanzania, the Tanzania Revenue Authority (TRA) (2013) introduced the block management system. The system simplifies the collection of the necessary business information for tax purposes from the taxpayer. Under this system, the SARS agents are given the task of visiting taxpayers in their respective workplace at least once every three months. The aim of the visit is to find out clients' general business information and make sure that business information is up to date. This reduces tax compliance and increases the understanding of taxpayers on tax issues that can able them to comply with the tax system (TRA 2013).

The UK has introduced several initiatives which includes the establishment of a better regulation task force which can make recommendations to government on how to improve regulations and tax compliance of SMEs (Chamberlain and Smith 2006), and the establishment of the Small Business Council which is tasked with ensuring that all regulatory impact assessments include an 'SMEs Impact Test' on tax compliance (Chamberlain and Smith 2006).

It is possible that the introduction of the Tanzanian block management system in South Africa could be helpful in assisting SMEs in reducing their tax compliance costs and in making tax compliance less difficult. The visiting of tax officials once every two or three months could reduce the cost of outsourcing their tax requirements since they would be assisted by tax officials, and it will also help SMEs understand their tax obligation and their tax status.

### **2.6.3 Summary of the initiatives**

The literature review on tax initiatives confirms that numerous provision and initiatives are available to assist SMEs in achieving tax compliant.

The literature confirms that tax initiatives are available in a variety of formats. Some of the initiatives include a block management system in Tanzania and the National Small Business Council, which defines South Africa's national strategy for small business development and promotion as well as the implementation of the DTC which seeks to scrutinise the tax system and its effect on the promotion and potential tax administration of SMEs.

Having discussed the characteristics of SMEs, tax initiatives, tax compliance and knowledge of SMEs as well the definition of SMEs and tax compliance and its components, the next section discusses the empirical research on tax compliance for SMEs both in South Africa and internationally.

## **2.7 Empirical research**

The study of tax compliance began in the early 1970s (Alm, Kirchler, Muehlbacher, Gangl, Hofmann, Kogler and Pollai 2012). At the time, the decision to follow tax law was framed as purely economic (Alm *et al.* 2012). Although there has been extensive study on the costs of small business tax compliance, few studies have attempted to statistically link the effect of tax compliance costs on the functioning of small businesses (Alm *et al.* 2012). Tax compliance costs continue to be regarded as one of today's taxation issues, particularly in developing countries seeking the appropriate mechanisms for generating tax revenue in order to boost and improve their public finances (Maseko 2014).

### **2.7.1 South African studies**

Tax compliance costs consume resources that could be better used to run their businesses (Abrie and Doussy 2006). Bandara (2019) states that SMEs regard tax obligation as an accumulative burden since they lacked sufficient skillful personnel to handle tax compliance requirements, and as a result, they incur additional tax costs in form of obtaining the service of tax practitioners (Abrie and Doussy 2006).

According to Mahadea (2008), SMEs consider compliance with income tax, VAT, SDL, and UIF to be time and money consuming, and that the burden imposed by excessive regulation affects firms, particularly because regulatory compliance is costly for small businesses while the benefits of compliance are insignificant.

Mahlanza (2011) concluded that new business registration requirements (including tax registration) and compliance with labour regulations contained in the “Labour Relations Act (Act 66 of 1995), the Conditions of Employment Act (Act 75 of 1997),” and the Employment Equity Act are some of the regulatory burdens that SMEs in South Africa face.

When Smulders *et al.* (2012) analysed a survey of tax practitioners, the following were their findings:

- The number of hours required to comply with tax legislation increased in proportion to the size of the business; the hours are regressive when expressed as a percentage of turnover (Smulders *et al.* 2012: 193.).
- VAT is the most time-consuming tax for small businesses. Small businesses spent an average of 251.95 hours per year dealing with VAT, income tax, and employee tax compliance issues (Smulders *et al.* 2012: 215). Businesses required to comply with the turnover tax system used a total of 155.2 hours (of which 67.3 hours were spent complying with the turnover tax system and 87.9 hours were spent complying with employees' tax, as the turnover tax system does not replace employees' tax) (Smulders *et al.* 2012: 215).
- Recording VAT-related information is the most time-consuming tax compliance activity for small businesses (Smulders *et al.* 2012:194). Employee taxes took the most time to calculate, submit, and pay because they are submitted to SARS monthly (Smulders *et al.* 2012:194).
- VAT took 78.55 hours to record information, calculate tax, file returns, and pay tax, whereas income tax took 42.72 hours and employee tax took 53.81 hours. VAT took longer because SMEs typically submit VAT returns every two months, resulting in six returns per year, whereas income tax returns are submitted three times per year (one income tax return and two provisional returns) (Smulders *et al.* 2012).

Tax compliance has a negative impact on business operations and takes time away from other business activities (Mahlanza 2011), and the complicated tax system increases the tax liability

imposed on businesses (Gelbart 2013). This demonstrates that the current tax system in South Africa is biased against one of the most important sectors of the economy (Qabaka 2011), as well as that the government does not appear to be assisting SMEs in reducing the burden of complying with multiple regulations (Cassim, Soni and Karodia 2014: 37).

This is supported by the 2015–2016 “GEM report, South Africa received a low score of 3.1 out of 9 for supportive government policies, taxes, and bureaucracy,” indicating the South African government's ineffectiveness in assisting SMEs to reduce tax compliance burdens (Herrington and Kew 2016).

Ndlovu (2015) indicates that the tax compliance burden for SMEs in the country includes the following:

- The cost of preparing and submitting all appropriate tax proceeds;
- The time spent by SMEs staff in ensuring tax compliance.
- The cost suffered to obtain the services of tax practitioners.

Olla (2016) and Lekhanya (2016) agree that tax rates and registering for VAT are onerous challenges to small businesses and they have a substantial influence in the development of small businesses. Fluctuating tax rates and VAT registration severely impact their profit margins and their growth and innovation (Tee *et al.* 2016). According to SAICA (2016: 8), the South African government and its departments are the worst late payers to their suppliers and service providers, including SMEs. As a result, the government is quick to claim payment through SARS but slow to pay its own dues for the services provided by SMEs (SAICA 2016:8).

Employing appropriately qualified tax personnel and utilising e-filing could reduce this cost for SMEs (Smulders *et al.* 2012). Small business with tax practitioners who do not have tax or accounting qualifications would incur high compliance costs due to the tax preparer making errors whereas having personnel with appropriate skills and qualifications would result to lower tax compliance costs and furthermore SMEs that understand taxes and the use e-filing will incur lower tax compliance costs (Smulders *et al.* 2012).

Compliance costs for small businesses remain high in both absolute and relative terms and transactional taxes like VAT are still the foundation of the highest compliance costs (Evans *et*

*al.* 2014). Internal tax compliance costs constitute more than 60% of all costs by far which is the largest component of total tax compliance costs (Evans *et al.* 2014).

The higher the percentage of compliance costs, the smaller the business (Rametse 2010). This means that as a company's turnover increases, so will its tax compliance cost (Rametse 2010). The increase in turnover of the business is associated with increases in transaction documents, which should be presented to tax officials as proof of income; therefore, this results in an increase in the cost of tax compliance due to record-keeping which should be minimal (Smulders *et al.* 2016). Matarirano *et al.* (2019) argue that if the turnover of the business increases that may be a sign that the business is doing well and is growing.

When compared to burdens associated with other types of government regulations, regulatory burdens associated with tax administration significantly raise tax compliance costs (Ali 2018). According to Matarirano *et al.* (2019), small businesses' compliance costs have a significant influence on their performance. The fact that small businesses are resource constrained and cannot afford to spend resources on non-value adding activities such as tax compliance makes tax compliance costs an unwanted and unnecessary burden (Matarirano *et al.* 2019). Botha *et al.* (2020) agree that SMEs regard government red tape, compliance with regulations as main obstacles to their effective functioning.

SMEs who only have basic tax knowledge do not comply with tax laws not because they don't want to, but because they lack a deeper understanding of tax requirements (Matarirano *et al.* 2019). Tax compliance continues to be a burden for SMEs, as they don't have the necessary staff means and skills to comply with all of their tax obligations (Deloitte 2019). This is evidenced by Shiya (2018) who found that 67% of small businesses in South Africa have failed to submit their tax returns due to the complicated tax system. They acknowledged that regulations and compliance were important, but that they should be simplified to improve SMEs' tax compliance (Nieuwenhuizen 2019).

### **2.7.1.2 Summary of South African studies**

The literature review indicates that the complexity of a tax system can be an impediment for small businesses attempting to fulfill with tax rules. According to Olla (2016), not all SMEs have the necessary resources, tax knowledge, or awareness of the requirements to obey with



these tax rules. It is obvious that SMEs in South Africa incur various tax compliance costs, with most costs being tax collection and submission, as well as tax filing.

### **2.7.2 International studies**

There is strong evidence that the complication of tax regulations, the regularity of income tax modifications and the lack of tax knowledge are substantial drivers of tax compliance costs for businesses in Australia (Lignier and Evans 2012). Small businesses seek assistance from external tax service providers due to a insufficient tax information, the complexity of tax laws, and the frequency with which tax rates change this decision is likely to increase tax compliance costs (Sapiei, Abdullah, and Ismail 2013: 3).

Okpeyoha, Musahb, and Gakpetorc (2019) found in Ghana that compliance costs and tax rates have a significant impact on the effective functioning of SMEs, with a significant difference in tax compliance levels between SMEs. This difference can be attributed largely to SMEs' inability to file their tax returns on time and to keep proper books of records of their business transactions (Okpeyoha *et al.*2019). According to Tee *et al.* (2016) taxes imposed on SMEs in Ghana have a variety of effects on their profit growth.

In Nigeria, Ojochogwu and Ojeka (2012) concluded that high tax rates and complex filing procedures cause tax non-compliance among SMEs, while multiple taxation and proper enlightenment have a lesser impact. SMEs' noncompliance stems from a belief that the tax burden is excessive. Furthermore, poor tax education and low tax self-esteem are some of the factors that make ensuring tax compliance difficult (Ponorica and Al-Saedi 2015).

Tax calculation and remittance processes and procedures may also contribute to compliance costs. According to Saad (2013) in Malaysia, the massive amount of paperwork required to comply with tax obligations exacerbated the problem and encouraged non-compliance among SMEs. This is supported further by Gangl *et al.* (2014) in Austria, who emphasize that tax laws are frequently too complex for non-professionals to understand, which many SMEs owners unquestionably are. Furthermore, tax practitioners agree that tax is complicated for SMEs, and they also have a pivotal part in the failure of small businesses (Cuccia 2013).

Many SMEs still do not understand tax regulations, which affects their tax compliance (Adiasa 2013); therefore, there are many factors that affect SMEs tax compliance burden (Gangl *et al.*

2014). Akinboade (2015) identified high registration costs, extreme obedience obstacles and a lack of willingness on the part of the taxpayer to disclose information as some of the factors influencing the tax compliance burden in Cameroon. Tax practitioners in Australia also agree that complicated tax system and requirement makes compliance difficult to achieve for SMEs and tax compliance significantly affects the functioning of small businesses (Torgler 2016). The fairness of the tax system in place is another important factor that may influence taxpayers' compliance behaviour. Mohd (2013), found in Malaysia, that if a taxpayer believes the tax system is unfair, they may refuse to comply, resulting in noncompliance.

Deyganto (2018) reported that, in Ethiopia, SMEs' compliance with the tax system is hampered by a lack of tax knowledge. In Ghana, Appiah (2016) found that the main barriers to achieving tax compliance for SMEs were a lack of understanding of tax laws, a lack of proper bookkeeping, the distance between the tax office and the place of business, and the cumbersome processes involved in paying (Appiah 2016).

Being tax compliant imposes obligations on SMEs in terms of procedures and tax laws, such as proper registration and payment rules (Bozdoganoglu 2016). Taxation information, fines, and tax learning all have significant effect on tax compliance burden of Nigerian SMEs (Oladipupo and Obazee 2016). Oladipupo and Obazee (2016) concluded that improving the tax knowledge of SMEs will promote tax compliance this will benefit the governments and taxpayers. Gitaru (2017) found that informing Kenyan taxpayers about their social obligation to pay taxes can influence their willingness to comply.

Tan and Braithwaite (2018) argued that in New Zealand, taxpayers who are well-versed in tax regulations are more likely to comply with them. According to Zivanai, Chari, and Nyakurima (2016), SMEs in Kenya are generally aware of their obligations to comply with tax laws and rules, but they risk not complying because the risk of being caught is low.

In Ghana, Ameyaw *et al.* (2016) concluded that tax policies pose a serious threat to SMEs in relation to payment of taxes which affect the profitability of SMEs business operations. Koranteng, Osei-Bonsu, Ameyaw, Agyeman and Dankwa (2017), also in Ghana, asserted that complexities in tax regulatory systems pose a serious hindrance on the innovation and growth of SMEs. This was confirmed by Kashalaba (2017) who stated that, in Tanzania, most SMEs lack experience with regards to tax matters, which escalates the cost of complying with tax

regulations and as a result, revenue goes to paying taxes and complying with tax regulations instead of being invested in growing the business.

Mahangila (2017), reporting in Tanzania, states SMEs lack confidence in their ability to submit their tax return cause them to hire experts to file for them as a result they incur additional tax compliance cost. Thus, SMEs require technical skills if they want to take over this function themselves (Edward and Ambrose 2017). Inasius (2019), in Indonesia, maintains that dealing with taxation matters still poses a significant challenge to SMEs because of limited knowledge and lack of administrative abilities.

In Kenya, Aondo and Sile (2018) found that tax learning had a substantial optimistic effect on tax compliance, whereas taxation penalties had a negligible positive result on tax compliance. The ability and willingness of SMEs to comply is determined by their understanding and interpretation of tax laws and their tax compliance attitudes can be improved by improving taxation understanding (Aondo and Sile 2018). The study further established that tax rates and too complicated tax filing discourages tax compliance among the SMEs (Aondo and Sile 2018). In Nigeria, Onoja and Odoma (2020) revealed that administrative tax complexities significantly affect their operations. In Ghana, Peparah, Abdula, and Agyemang-Duah (2020) concluded that lack of tax knowledge and frequently changes and in tax rates increase SMEs' tax compliance burden.

#### **2.7.2.1 Summary of international studies**

The findings confirm that the costs of tax compliance for SMEs are substantial and regressive. According to the literature, complicated tax causes SMEs to outsource tax services which increase compliance costs and changes in tax rates negatively affects their attitudes toward taxation. Specific aspects of tax compliance may influence compliance costs for taxpayers as well as business operations. The processes and procedures used for tax calculations and remittances are the primary drivers of high compliance costs.

### **2.8 Summary**

The literature review has provided reasons for non-compliance of SME which include lack of tax knowledge by SME owners and staff, and the lack of resources required to achieve tax compliance. The literature review further confirms that tax compliance costs are burdensome

on SMEs. However, the literature search did not find any study that attempted to assess the effects of tax compliance costs on the functioning of small businesses in South Africa or internationally.

Based on this information, a gap exists to assess the tax compliance costs of SMEs and whether the costs incurred by SMEs to be tax compliant and the cost of outsourcing the service of tax practitioners has any effect in the functioning of small businesses. Therefore, this study seeks to assess the tax compliance burden in the functioning of SMEs in the Durban Central Business District. A summary of the studies and how they link to the research questions is shown in Table 2.1.

**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
<b>What is the effect of tax compliance costs on the functioning of SMEs?</b>	Botha <i>et al.</i> (2020).	South Africa	Small businesses regard government red tape, compliance with laws and legislation, engaging with the Department of Labour and engaging with SARS as being major barriers in their functioning.
	Okpeyoba <i>et al.</i> (2019).	Ghana	Tax compliance costs and tax rates have a significant impact on the effective functioning of SMEs, with a significant difference in tax compliance levels between SMEs. This difference can be attributed largely to SMEs' inability to file their tax returns on time and to keep proper books of records of their business transactions
	Matarirano <i>et al.</i> (2019).	South Africa	SMEs compliance costs incurred by SMEs have a substantial consequence on their performance. External tax compliance places heavy burden on SMEs tax compliance costs and, as such, requires close attention.
	<i>SME Landscape Report</i> (2018/2019).	South Africa	Most small businesses have been in operation for less than five years, while one-quarter of SMEs have been in operation for six to ten years.

**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
	Olla (2016).	South Africa	Tax rates and registering for VAT are onerous challenges to small businesses and they have a significant effect in their development and growth. This means that obtaining SARS compliance certificates will continue to be a thorn in the side of new entrants to the market and existing SMEs.
	Sephapho <i>et al.</i> (2016).	South Africa	SMEs agree that tax regulations have a significant effect on performance and can lead to small business failure.
	Abrie and Doussy (2006).	South Africa	Tax compliance costs consume resources that could be better used to run SMEs businesses. The fact that SMEs do not have sufficient skillful personnel to handle tax compliance requirements in their businesses result in incurring additional tax costs in form of obtaining the service of tax practitioners
<b>What is the level of tax knowledge of SMEs?</b>	Nieuwenhuizen (2019).	South Africa	Business owners claim they lack the knowledge necessary to understand the changes in tax regulation and they don't have employees who have proper skill to help them attend to all their compliance issues. They acknowledged that being tax compliant is imperative, but they believe that tax laws should be simplified to improve SMEs' tax compliance.

**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
	Deloitte (2019).	South Africa	Taxpayer education and the cost of tax compliance are significant challenges for SMEs, which frequently lack the necessary staff resources and skills to comply in a timely and comprehensive manner.
	Matarirano <i>et al.</i> (2019).	South Africa	SMEs, especially those in developing countries, find it difficult to comply, not because they do not want to comply with tax law, but because they have only basic tax knowledge and don't have a deeper understanding of tax requirements.
	Wadesango, Mwandambira, Mhaka and Wadesango (2018).	Various countries	Improving tax awareness without addressing high tax rates and frequent changes in tax rates will have no positive impact on SMEs' tax compliance.
	Shiya (2018).	South Africa	A strong relationship exists between the level of tax knowledge and tax compliance as 67% of the small businesses in South Africa are of the view that they do not have the required level of tax knowledge to be compliant and 63% of the SMEs failing to submit tax returns are doing so because they do not know how to complete tax returns.
	Sephapho <i>et al.</i> (2016).	South Africa	SMEs oppose that tax laws are written in a very complicated language.
	Smulders <i>et al.</i> (2012).	South Africa	Having tax preparers without commercial qualifications would lead to an increase in small business compliance costs most likely due to spending long hours on tax

**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
			tasks, redoing the tasks due to errors, being prone to inspections and audits, consulting tax sources and/or engaging external service providers, “whereas a small business with personnel with appropriate skills and qualifications would incur low tax compliance costs. It is through understanding tax that small businesses would be willing and able to use e-filing, which, in turn, reduces tax compliance costs”.
<b>What costs are incurred by SMEs to be tax compliant?</b>	Matarirano <i>et al.</i> (2019).	South Africa	An increase in turnover of the business does not result in an increase in tax compliance costs but there “may be a sign that the business is doing well and is an indication of growth in size, which, in itself, is associated with an increase in costs. An increase in size brings along skilled employees, who are, more often than not, expensive”.
	Nieuwenhuizen (2019).	South Africa	Many government-imposed regulatory constraints are restrictive and expensive for small businesses. “These relate primarily to business start-up and growth, SARS, post-filing and all forms of taxation including VAT, the regressive burden of tax compliance cost, labour laws, the cost of compliance in terms of time and money, paperwork and requirements”.



**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
	Smulders (2013).	South Africa	Although outsourcing of the tax returns to tax practitioners reduces the administrative burden, it simply adds to it in terms of cost.
	Smulders <i>et al.</i> (2012).	South Africa	Small businesses (not subject to the turnover tax system) required an average of 255 hours per year to comply with tax legislation. When compared to similar businesses that were not registered for this tax, turnover tax respondents spent just under two-thirds of the time (155 hours) complying with their tax obligations. Gross tax compliance costs are regressive; small businesses spent R53 356.81 per year on internal tax compliance activities and R9 982 on external tax compliance assistance.
	Rametse (2010).	South Africa	“The smaller the business, the higher the percentage of compliance costs”. This means that “an increase in the turnover of a business would lead to an increase in tax compliance costs. An increase in turnover is normally associated with an increase in transaction documents, which should be presented to tax officials as a proof of income”.

**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
<b>Do SMEs use tax incentives and record keeping to reduce costs of being tax compliant?</b>	Botha <i>et al.</i> (2020).	South Africa	SMEs “with a turnover of below R20 million tend to feel that the DSBD has not helped by creating tax incentives for small businesses to grow, Thus, although the government has over the last twenty odd years endeavoured to assist the SME sector, it is evident that a lot more work is needed. The incentives to assist this sector need to be stratified and more focused based, <i>inter alia</i> , on the size of the business”.
	Naicker and Rajaram (2019).	South Africa	To promote tax compliance and increase tax compliance among SMEs in South Africa the SARS grants SMEs with tax incentives and initiatives which include but not limited to reduced tax rates, accelerated depreciation, capital gains tax relief, skills development relief levies, small business tax amnesty, reduced annual vat returns, increase in vat threshold etc.
	Evans <i>et al.</i> (2014).	Australia	A large percentage of SMEs that were eligible for SBTCs used the SBTCs, indicating that the SBTCs were well-adopted once businesses were aware of their eligibility and the vast majority of small business taxpayers keep records not only for tax purposes, but also for accounting information for internal management and external reporting.

**Table 2.1: Summary of literature and alignment to the research questions**

Research question	Study	Country	Findings of the study
	Maxwell <i>et al.</i> (2015).	America	Despite the availability of these tax incentives and initiatives, the tax compliance burden has been significantly affecting the growth and effective functioning of SMEs in South Africa. This results in the tax compliance of SMEs to be low because SMEs are unaware of the tax incentives and tax initiatives available to them.
<b>What benefit do SMEs perceive on being tax compliant?</b>	Inasius (2019).	Indonesia	Tax compliance is an important obligation for individuals and firms in both developed and developing countries and taxpayers have the responsibility to report income and pay their tax liabilities correctly.
	SARS (2019).	South Africa	Being tax compliant contributes towards the economy's development, which improves the state of the nation.

# CHAPTER THREE

## RESEARCH METHODOLOGY

### 3.1 Introduction

The previous chapter outlined the taxation framework, the importance of taxation, the definition, characteristics, and importance of SMEs, followed by the definition of tax compliance costs, SMEs' tax compliance costs, and SMEs' tax knowledge. Finally, it discussed SMEs' tax initiatives as well as empirical research on SMEs' tax compliance costs. The objective of this study, as outlined in Chapter 1, is to assess the tax compliance burden in the functioning of SMEs in the Durban Central Business District.

**To meet this objective, the following research questions were set which were aimed at SMEs:**

Research question 1: What is the effect of tax compliance costs on the functioning of SMEs?

Research question 2: What is the level of tax knowledge of SMEs?

Research question 3: What costs are incurred by SMEs to be tax compliant?

Research question 4: Do SMEs use tax incentives and record keeping to reduce costs of being tax compliance?

Research question 5: What benefit do SMEs perceive on being tax compliant?

**The research questions aimed at tax practitioners to obtain their views on tax compliance costs were as follows:**

Research question 6: What costs are incurred by SMEs to be tax compliant?

Research question 7: Do SMEs use tax incentives and record keeping to reducing the costs of being tax compliant?

Research question 8: What benefits do tax practitioners perceive for SMEs to be tax compliant?

This chapter explains the rationale for the research method chosen to investigate the tax compliance burden in the functioning of SMEs in the Durban Central Business District. The key

topics that are discussed in this section include the research methods used as well as the population, sample and sampling method, the research instrument, the response rate, data preparation and analysis, the limitations, and reliability and validity.

### **3.2 Research philosophy**

In any research process, it is critical that the researcher understand the research philosophies or paradigms that contribute to the quality and creativity of the research (Smith and Shinebourne 2012). A research philosophy is also a belief about how data about a phenomenon should be gathered, analysed and used (Saunders, Lewis and Thornhill 2019).

This research was founded on postpositivist deterministic philosophy which grips that sources (probably) determine effects or outcomes (Creswell 2014). As an outcome, the difficulties studied by postpositivists reflect the need to identify and evaluate the causes that influence outcomes, such as those discovered in experiments (Creswell 2014). It is also reductionistic in the sense that the intention is to condense the ideas into a small, discrete set of variables to test, such as hypotheses and research questions (Saunders *et al.* 2019).

Knowledge gained through a postpositivist lens is based on careful observation and measurement of objective reality that exists "out there" in the world. As a result, for a postpositivist, developing numerical measures of observations and studying individual behaviour becomes critical (Creswell 2014). The reason for selecting this philosophy over others is that this study analyses concepts, definitions, arguments and problems, as well as seeks to gain an understanding of the underlying reason, opinions, and motivations relating to the effect of tax compliance costs on the functioning of SMEs.

### **3.3 Research design**

The research design adopted in a study refers to the general plan of action or strategy that a researcher wishes to use as a guide in obtaining the relevant information needed to address the research problem, as well as how to deal with the challenges encountered during the study process (Creswell 2014). The sections that follow describe the research design used in this study.

### 3.3.1 Research approach

The research process involves developing questions and procedures, with data typically collected in the setting of the participants, and then using data analysis to build from particulars to general themes, with the researcher making interpretations of the data's meaning (Creswell 2014). The investigation could also be deductive (as opposed to inductive). Deductive reasoning entails the development of a theory that is then put to the test through a series of propositions. This study is deductive because it seeks to examine theories relating to the effect of tax compliance costs on the functioning of SMEs, and it thus adds to the body of knowledge on a topic that has previously been researched and explored.

There are two main approaches to research: qualitative or quantitative. A combination of these two approaches is also possible, known as mixed methods. As the aim of this current study is to assess the effect of the tax compliance burden in the functioning of SMEs in the Durban Central Business District, a qualitative research approach was not considered appropriate because it lacks statistical presentation and would not have been appropriate for meeting the study's objectives.

Quantitative research is the progression of collecting and investigating arithmetical data to discover patterns and generalise results to larger populations (Bhandari 2020). According to Creswell (2014), quantitative research is a method for testing objective theories by examining the relationship between variables.

The advantages of the quantitative approach are as follows:

- Sample survey results can be generalised to the entire population and are comparable across population groups (Choy 2014).
- Data from large samples can be administered and examined using reliable and dependable measures (Bhadari 2020).
- It strives to eliminate bias so that facts, instances, and phenomena can be understood objectively (Choy 2014, Frey 2018).

The disadvantages of quantitative research are that:

- The results must be calculated in Excel, Access, or SPSS, which may not always be available in a country's programmes (Choy 2014).
- It fails to consider historical and cultural contexts that may influence data collection and results (Bhadari 2020).

- Biases such as missing data, imprecise measurements, or ineffective sampling methods can all lead to incorrect conclusions in quantitative research (Bhadari 2020).

This study adopted a quantitative approach because data in quantitative research is collected using sampling strategies to ensure accuracy, reliability, and validity; as a result, bias in the results can be avoided. Furthermore, the study used quantitative research because it deals with quantifying and analysing variables to obtain results. It entails the use and analysis of numerical data using specific statistical techniques to answer questions such as who, how much, what, where, when, how many, and how (Bhadari 2020).

### **3.4 Research strategy**

There is no single research method that can be considered the best in all circumstances. The decision is influenced by the research question, research objectives and data being accessed (Smith 2011). Questionnaires have the advantage of obtaining data in a more efficient manner in terms of researcher time, energy, and cost. The questionnaire method of data collection is most used for monetary and commercial surveys, and most of the empirical research on tax compliance is based on surveys of taxpayers (Gangl *et al.* 2014).

In survey research, the questionnaire is the primary data collection tool. It is essentially a set of standardised questions, often referred to as items that follow a predetermined scheme to collect individual data on one or more specific topics (Lavrakas 2008). Most questionnaires are self-administered which means that the respondent fills out the form without assistance from the researcher.

The quantitative approach used in this study entailed employing a descriptive survey study design, with questionnaires serving as the research strategy. This is due to the study's purpose of determining the tax obedience encumbrance in the functioning of SMEs in the Durban Central Business District. This strategy was chosen because it would allow the researcher to provide a detailed description of the study phenomenon in its current state by taking raw data and tabulating it into a usable format. Because the research relied on respondents' views and opinions on the effect of tax compliance burden on the functioning of SMEs in the Durban Central Business District, this research strategy served in achieving the objectives of this study.

### **3.5 Time horizon**

The time horizon is defined as the time frame for the research as well as the time required to investigate the phenomenon (Melnikovas 2018). There are two types of time horizons: cross-sectional or longitudinal. Cross-sectional is short term in which data is collected at a specific point in time (Melnikovas 2018). Whereas longitudinal is where data is collected repeatedly over a longer period to compare data (Melnikovas 2018).

This is a cross-sectional study because it gathered information from SMEs and tax practitioners at a precise time. Collecting data over a prolonged period may result in richer data sets; however, given the exploratory nature of this study, a cross-sectional study would adequately address the objectives of this study.

### **3.6 Target population and sample**

#### **3.6.1 Population**

The appropriateness of study partakers is an important factor in defining the populace (Graziano and Raulin 2013: 201). The target population is a grouping of all individuals or groups of individuals who represent the entirety or totality of the cases that the researcher wishes to investigate (Casteel and Bridier 2021). The population for this study was all owners and managers of SMEs in the Durban Central Business District who were responsible for keeping their taxes up to date as well as tax practitioners who assist SMEs in preparing their tax requirements. Due to the Protection of Personal Information Act, it was not possible to get an up-to-date list of SMEs from the Durban Chamber of Commerce (DCCI) and therefore the entire population of SMEs at the time this study was carried out was unknown. However, according to the DCCI (2016), the Durban Central Business District had 600 small businesses registered with it in 2016. It was decided to use this list of SMEs and supplement it with the names of other SMEs taken from the Yellow Pages Business Directory. This resulted in a further 60 names being added to the 600 SMEs already identified. A total of 660 SMEs therefore was the population for this study. If SMEs with similar characteristics were not registered with the DCCI or were not listed in the Yellow Pages Business Directory, they were excluded from this study. Therefore, the findings of this study cannot also be generalised beyond this sample of SMEs.



The contact details of 15 tax practitioners who participated in the study were obtained through personal contact. The Protection of Personal Information Act made many tax practitioners reluctant to participate in the study. As a result, the selection of tax practitioners to participate in this study was not scientific as it was through personal contact.

### **3.6.2 Sample and sampling technique**

Gravetter and Wallnau (2017) define sample size as the number of units selected to represent the population of interest. The population should be represented in the sample. This requirement is met by specifying the proper sampling frame and employing an appropriate sampling method. There are two primary considerations when selecting a sample: how many units must be in the sample (sample size) and how these units will be selected (sampling methods) (Gravetter and Wallnau 2017). As response rates can be low if only random sampling is used, for the SMEs in this study, a census was used to get enough usable responses. Using personal contact, 15 tax practitioners were identified and all of them stated that they had SMEs as clients.

## **3.7 The survey questionnaires**

The measuring instrument for this research were questionnaires which were used to collect information from the SME owners or managers and tax practitioners. The questionnaires were semi-structured, with open-ended and closed-ended questions. Closed-ended questions can only be answered with "Yes" or "No," or they have a limited set of possible answers (such as: A, B, C, or All of the Above), whereas open-ended questions allow the respondents to answer in their own words (Ozuru, Briner, Kurby and McNamara 2013). Many of the questions were closed-ended questions using a Likert 5-point scale (degree of agreement scale). The questionnaire was estimated to take 30 minutes to complete.

### **3.7.1 Content and layout**

There were two questionnaires, one for SMEs and the other for tax practitioners. Appendix 1 contains the entire set of questionnaires.

### **3.7.2 Reasons for question choice in the questionnaire aimed at SMEs**

The questionnaire began by asking the respondents to supply various background information.

### 3.7.2.1 Questions dealing with the background of the SME respondents

The background information of the SMEs was captured in section A of the SME questionnaire. These questions were deemed significant because they provided information on the type of business, its legal structure, the number of years in operation, the number of owners, their education level, the annual turnover and their income tax status. These background questions were as follows:

**Question 1:** What is the main activity of the business? Please choose only one of the following:

- Agriculture, forestry and fishing (includes farming)
- Wholesale trade
- Electricity, gas, water supply and waste services
- Manufacturing
- Retail Trade (includes shops)
- Construction (includes landscaping and repairs)
- Transport, postal and warehousing
- Accommodation and food services (includes cafes and restaurants)
- Finance, insurance services
- Rental, hiring and real estate services
- Professional, scientific and technical services (includes lawyers, accountants, engineers)
- Administrative and support services
- Public administration and safety
- Education and training
- Health care and social assistance

Other: please specify:

**Question 2:** What is the legal structure of the business? Please choose only one of the following:

- Sole Proprietorship
- Partnership
- Trust
- Incorporated association
- Private company
- Un-incorporated association

- Other

**Question 3:** For how many years has this business been trading? Please choose only one of the following:

- Less than a year
- 3-5 years
- 6-10 years
- More than 10 years

**Question 4:** How many owners (partners/directors) does the business have? Please write your answer here:

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**Question 5:** Indicate the level of education of owners (partners/directors) who are responsible for the tax matters of the business? Please choose only one option:

No formal education	
Basic education	
Tertiary education	

**Question 6:** What was the estimated annual turnover of the business for the last tax year?

- 0 – R525 000
- R525 001- R1 000 000
- R1 000 001-R3 000 000
- R3 000 001–R7 000 000
- R7 000 001- R14 000 000
- More than R14 000 000
- Not sure

While no scientific or specific approach method was used to select the turnover thresholds above, these thresholds were used in previous studies and this served to ensure reliability and validity.

**Question 7:** Which of the following categories does your business fall under? Please choose only one of the following:

- A small business corporation which pays income tax
- A non-profit organisation which is exempt from income tax
- A non-profit organisation which is not exempt from income tax
- Other please specify:

The question was limited to ‘corporations’ which pay income tax. This was necessary identify that the SMEs were taxpayers and that they were fully capable of answering the questionnaire.

### 3.7.2.2 Questions dealing with research question 1

The following section of the questionnaire concentrated on the effect of tax compliance costs on SMEs. These questions were created to address the study's first research question, which was to investigate the effect of tax compliance costs in the functioning of SMEs. These questions were as follows:

**Question 8.1:** Do tax compliance costs have any impact on the performance of your SME? Please choose only one of the following:

- Yes
- No

**Question 8.2:** Do you think tax compliance costs have a significant effect in the failure of SMEs? Please choose only one of the following:

- Yes
- No

**Question 8.3:** The following are some of the impacts of tax compliance costs in SMEs. Please indicate your level of agreement or disagreement, using a scale of 1 (strongly disagree) to 5 (strongly agree) with each of the following impacts by placing a tick in the appropriate box.

<b>Impact of compliance costs</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
Affects the SMEs’ performance					
Causes SMEs to hide profits received.					
SMEs may suffer business failure due to high compliance costs.					
The tax system and its compliance requirements are a stumbling block to the growth of small businesses.					
High tax rates promote non-compliance with tax laws.					

High tax rates are a reason most SMEs remain in the informal sector					
Tax compliance costs reduce business productivity.					
Tax compliance costs diminish business resources.					

### 3.7.2.3 Questions dealing with research question 2

The following section of the questionnaire focused on SMEs' tax knowledge. Section C of the questionnaire contained questions designed to address the study's second research question, which focused on the level of tax knowledge possessed by SMEs. These questions were chosen because they would assist in determining whether SME's level of tax knowledge plays a role in reducing or increasing the tax compliance burden. These questions were as follows:

**Question 9.1:** Have you gone for any training regarding tax matters? Please choose only one of the following:

- Yes
- No

If yes, how many times.....

**Question 9.2:** Please answer the following statements with either “YES” or “NO”.

I know:	YES	NO
How to calculate my tax liability		
How long the tax records must be kept		
When to submit my tax returns		
When to pay tax due to SARS		
How to make payment to SARS		
How to complete my tax return		
How to file my returns		

**Question 9.3:** Please read each statement carefully and then indicate the extent to which you agree or disagree, using a scale of 1 (strongly disagree) to 5 (strongly agree), with each of the following statements describing how you experienced the tax registration process of your business.

Statements on the tax registration process	1	2	3	4	5
The registration processes for capital gains tax, value added tax, employee tax and income tax are too lengthy.					
I cannot begin operating my business without having completed my tax registrations.					
I do not understand the procedures I need to follow to register for capital gains tax, value added tax, employee tax and income tax.					

Preparing the necessary documentation for the registration for capital gains tax, value added tax, employee tax and income tax takes up too much time.					
I ask for help with preparing the necessary documents for the registration of capital gains tax, value-added tax, employee tax and income tax.					
Submission of my tax registration is easy for me.					
Submitting all my tax registration forms for capital gains tax, value added tax, employee tax and income tax is quick.					
Registering my SME for capital gains tax, value added tax, employee tax and income tax cost me a lot of money.					
I do not know how to register my SME for capital gains tax, value added tax, employee tax and income tax.					

### 3.7.2.4 Questions dealing with research question 3

The following section of the questionnaire was primarily concerned with the costs incurred by SMEs to be tax compliant. Section C of the questionnaire also included questions designed to answer the third research question, which was to determine the costs associated with tax compliance. Section C concentrated on the cost incurred in the form of money.

**Question 9.4:** Using “Yes” or “No”, please indicate which of the following taxes your business pays.

	YES	NO
PAYE		
VAT		
Capital Gains Tax (CGT)		
Income tax		

**Question 9.5:** Please indicate who completes the following tax returns on behalf of the business.

	N/A	Employee or owner	External tax professionals
PAYE			
VAT			
Capital Gains Tax (CGT)			
Income tax			
Please add any other returns			

**Question 9.6:** If the tax returns are prepared by an external accounting firm, how much does it cost you to engage the external tax professionals on annual basis?

Tax returns	Estimations				
	R2 500 - R5 000	R5 001 - R7 500	R7 501 – R10 000	R10 001- R12 500	Not sure
PAYE					
VAT					
Capital Gains Tax (CGT)					
Income tax					

**Question 9.7:** If the tax returns are prepared internally by an employee or the owner, annually how much does it cost you to prepare the tax return internally?

Internal owner/ employee	Estimations					
	R1 000- R2 500	R2 501 - R5 000	R5 001 - R7 500	R7 501 – R10 000	R10 001- R12 500	Not sure
PAYE						
VAT						
Capital Gains Tax (CGT)						
Income tax						

**Question 9.8:** Have you ever paid penalties and interest for the following reasons?

Tick appropriately:	Yes	No
Non filing of returns		
Filing returns after due date		
Incomplete or incorrect calculations		

**Question 9.9:** If you answered “YES” for any of the reasons mentioned in the question above, can you please tell us how much was the penalty or interest?

.....

**Question 9.10:** This section will measure the level of tax compliance of small businesses. Please indicate by ticking a (√) in the appropriate box the extent to which you comply with the payment of taxes.

	1	2	3
Measures of tax compliance	Never	Sometimes	Always
Do you file your tax returns?			
Do you pay your tax liabilities?			
Do you observe due dates in filing and payment of taxes?			

**Question 10.1:** Did the business pay for any payroll external services in the last tax year? Please choose only one of the following:

- Yes
- No

**Question 10.2:** How much did the business pay for these services? Please note only answer this question if you answered YES to question 10.1. Please write your answer here:

--

**Question 11.1:** What is the estimated annual cost of external tax and accounting related services paid by the business?

COST OF EXTERNAL SERVICE PROVIDERS	Estimations				
	R5 000 - R10 000	R10 001 – R15 000	R15 001 – R20 000	R20 000 - R25 000	R25 000 - R30 000
Tax costs					
Accounting costs					
Payroll costs					

**Question 11.2:** Answer the following statements using “Agree” or “Disagree”.

Statements:	Agree	Disagree
Our tax laws are simple to understand		
The owners/partners and directors of the business can compute the tax liability of the business, if given little explanation of the tax laws		
The tax rate for small business is high		
There is little education about tax laws and tax administration in South Africa		
There is no equity and fairness in our tax system		
It is very expensive for small businesses to hire tax practitioners to prepare their tax returns		
Other (please add and answer)		

### 3.7.2.5 Questions dealing with research question 3

Section D of the questionnaire contained questions relating to the time spent by the business to meet tax requirements. These questions were also designed to address the study's third research question, which was to identify the costs associated with the burden of tax compliance; however, Section D focused more on the cost incurred in the form of time. These questions were as follows:



**Question 12.1:** Do you prepare your own VAT, PAYE, CGT and income tax returns? Please choose only one of the following:

- Yes
- No

**Question 12.2:** If answered “YES” on question 12.1, how many hours does the business spend on each of the following tax related activities?

- Please estimate the average time spent by your business on tax related activities during the last tax year. Include time spent by owners/partner/directors and paid full time employees.
- Leave blank spaces if you did not spend any time on a particular activity (do not type zero).

<b>Activities:</b>	<b>Value-added Tax (VAT)</b>	<b>Pay-As-You-Earn (PAYE)</b>	<b>Capital Gains Tax (CGT)</b>	<b>Income tax</b>
Recording information needed for tax				
Tax planning and tax advice				
Dealing with your tax practitioner, including providing all required information to them				
Dealing with SARS via (phone calls, e-filing, visits)				
Learning about tax laws and tax requirements				
Calculating tax requirements, completing them and paying them				
Other activities- please add any other activities				

**Question 12.3:** Please estimate the percentage of the total time spent on different taxes by the following people during the last tax year and enter the percentages below. The totals should add up to 100%.

	<b>Value-added Tax (VAT)</b>	<b>Pay-As-You-Earn (PAYE)</b>	<b>Capital Gains Tax (CGT)</b>	<b>Income tax (Tax return)</b>
Owners/partners and directors				
Employees (e.g., clerks, internal accountants)				

**Question 13:** Please indicate which of the following factors can reduce the tax compliance costs for SMEs by rating the factors as either of low importance (1), important (2) or very important (3).

	1	2	3
Low tax rates for SMEs			
Frequent tax education for SMEs			
Electronic filing and payment of taxes			
Tax practitioners to be paid by government to render free services to SMEs in tax filing and records keeping.			
Tax laws should be simplified and practical			
Tax laws should be practical			
Strong monitoring and enforcement of tax laws by tax officials			
Please add any other factors			

### 3.7.2.6 Questions dealing with research question 4

Section E of the questionnaire contained questions relating to the tax incentives that small business exercise in the business. Section F discussed the role of record keeping in reducing the burden of tax compliance. These questions were designed to address the study's fourth question: do SMEs use tax incentives and record keeping to reduce the costs of tax compliance?

Section E examined whether SMEs take advantage of available tax incentives. The questions were as follows:

**Question 14.1:** Under the South African tax system, small and medium-sized enterprises may qualify for a number of tax incentives or other simplifications measures which aim to reduce the tax compliance burden.

Was your business eligible for any of the small business tax incentives during the last tax year?

Please choose only one of the following:

- Yes
- No
- Unsure/Do not know

**Question 14.2:** Did your business use any of the small business tax incentives during the last tax year? Only answer this question if you answered “YES” in Question 14.1.

- Yes
- No

**Question 14.3:** If the business was eligible for any of the tax incentives during the last tax year and you decided not to use them, could you tell us the reason (s) why? Please choose all that apply:

- My accountant told me not to use the small business tax incentives
- My business would have paid more tax as a result of using the tax incentives
- The rules regarding the tax incentives are too complex
- Using the tax incentives would have increased my external accounting cost
- Using the tax incentives would have increased the internal time that my business spends on tax related activities
- Other please specify: .....

**Section F of the questionnaire contained questions relating to the role of recording keeping in reducing the tax compliance burden.**

These questions focused on whether SMEs do keep accounting records and whether they paid any fees if their business outsources the record keeping.

The questions were as follows:

**Question 15.1:** Which one of the following applies to your business? Please choose only one of the following:

- There is no record keeping in the business
- There is record keeping in the business

**Question 15.2:** What type of accounting system does your business use? Please choose all that apply:

- No accounting system used
- Paper based/Manual
- All the work is done by external accountant
- Other computerised software; please elaborate.....

**Question 15.3:** If your business does its own record keeping, do you incur any costs in keeping the records? Please choose only one of the following:

- Yes
- No

**Question 15.4:** if your business outsources the record keeping, how much does your business pay an external body to keep the records?

.....

### 3.7.2.7 Questions dealing with research question 5

Section G of the questionnaire included questions about the benefits SMEs perceive from being tax compliant, which were used to answer the fifth research question. The questions were as follows:

**Question 15.5:** Please rate the following statements regarding the benefits of tax compliance, using the scale of strongly disagree (1) to strongly agree (5).

Statements on the benefits of compliance	Strongly disagree	Disagree	Neither agree nor disagree	Agree	Strongly agree
	1	2	3	4	5
Complying with the tax obligation helps to improve the record keeping of the business.					
Tax compliance helps improve the knowledge of the financial status of the business.					
To comply with tax obligation helps improve the knowledge of the profitability of the business.					
Other (please add)					

**Question 16.1:** Overall, would you agree that complying with tax obligations has some benefits for your business? Please choose only one of the following:

- Yes
- No

**Question 17.2:** If you had to put value to the benefit derived by your business from complying with tax obligations, can you please estimate the value of that benefit? Please write your answer here:

**Question 18:** In the past 5 years what has your business done to cope with increasing tax compliance complexity, given your limited budget? Please tick all that apply:

- Hired more people to handle taxes
- Hired outside tax consultants
- Other please specify.....

**Question 19:** Please to add any problems you have encountered in complying with the income tax system.

If the space provided to answer this question is not enough, please to attach to a separate sheet. We would very much like to hear your views on the subject.

**Question 20:** What, in your opinion, are three factors that would improve tax compliance of SMEs?

- I. ....
- II. ....
- III. ....

The following section of this chapter discusses the questionnaire aimed at the tax practitioners.

**3.7.3 Reasons for question choice in the questionnaire aimed at tax practitioners**

**3.7.3.1 Questions dealing with the background of the tax practitioner respondents**

Section A of the questionnaire focused on the respondents' backgrounds. These questions were deemed significant because they provided information about the type of business and the number of years it has been in operation. These questions were as follows:

**Question 1:** What is the legal structure of the business? Please choose only one of the following:

- Sole proprietorship

- Partnership
- Trust
- Public company
- Incorporated association
- Private company
- Un-incorporated association
- Other

**Question 2:** How long has this business been trading? Please choose only one of the following:

- Less than a year
- 3-5 years
- 6-10 years
- More than 10 years

### **3.7.3.2 Questions dealing with research question 6 in respect of the tax practitioners**

Section B addressed questions about the types of tax activities that small businesses outsource and how much it costs to outsource these activities. These questions sought to provide an answer to research question 6, which concerned the cost incurred by SMEs to be tax compliant. These questions were deemed significant because they sought to identify the activities that tax practitioners perform on behalf of SMEs, as well as the fees they charge for providing a service to SMEs. These questions were as follows:

**Question 3.1:** What kind of tax-related activities would an SME outsource from its business? Please tick all those that apply.

- Audit-related services
- Collection matters
- Preparing the tax return (ITR12)
- Preparing the provisional tax return
- Preparing amended returns
- Preparing the VAT return (VAT201)
- Preparing the PAYE, SDL and UIF return (EMP201)
- Record keeping services

- Tax planning
- Other (please specify).....

**Question 3.2:** Kindly please indicate an estimation of the annual fee charged by the firm for pre-filing, filing and post filing?

TAX REQUIREMENTS	ESTIMATION				
	Less than R2 499	R2 500- R4 999	R5 000- R9 999	R10 000- R14 999	More than R15 000
Pre-filing activities e.g., tax planning, obtaining tax guidance and information, and maintaining tax records					
Filing activities e.g., includes the collection of data, preparation of the tax return from financial data and calculation of the tax owed (including VAT201 and EMP201 returns)					
Post-filing activities e.g., preparing amended returns, the audit process etc.					

**Question 4:** Using estimation, how much does the business charge the client for the following tax requirements?

TAX REQUIREMENTS	ESTIMATION				
	R2 000 or less	R2 001- R4 000	R4 001- R5 999	R6 000- R7 999	R8 000 or more
Calculation of taxable income (ITR)					
Pay-As-You-Earn - EMP201 (monthly)					
Value-added Tax - VAT 201 (when due)					
Capital Gains Tax (CGT)					
EMP501 reconciliation (6 monthly)					

**Question 5.1:** What is the estimated annual fee you charge the client for payroll services?

.....

**Question 5.2:** What is the estimated average time taken per annum to prepare, complete and submit tax returns?

TAX REQUIREMENTS	AVERAGE TIME TAKEN (HOURS) if the TURNOVER of the SME is between:			
	R1 – R300 000	R300 001 - R1m	R1m - R6m	More than R6m
Calculation of taxable income (ITR)				
Pay-As-You-Earn - EMP201 (monthly)				
Value-added Tax - VAT 201 (when due)				
Capital Gains Tax (CGT)				
EMP201 reconciliation (6 monthly)				

**3.7.3.3 Questions dealing with research question 7 in respect of the tax practitioners**

The purpose of this research question was to determine whether SMEs use tax incentives and record keeping to reduce the cost of being tax compliant. Section C addressed issues concerning tax incentives. These questions were considered important because they sought to determine whether tax practitioners advise their clients to use tax incentives or not, and if they do advise them to use the tax incentives, do they charge them extra fees, and do tax incentives, in their opinion, reduce the tax compliance burden for SMEs. These questions were as follows:

**Question 6.1:** Do you sometimes advise the client not to use small business tax incentives? Please choose only one of the following:

- Yes
- No

**Question 6.2:** If answered “YES” to question “6.1” which tax incentive did you advise your client not to use?

.....

**Question 6.3:** If the small business is eligible for certain tax incentives, do you charge extra fees for the calculation of those certain tax incentives? Please choose only one of the following:

- Yes
- No

**Question 6.4:** If you answered “YES” to question “6.3”, please tell us how much you charge a client annually for the calculation of those certain tax incentives?

.....



Section D covered questions relating to keeping of accounting record. These questions were deemed significant because they sought to determine whether tax practitioners keep accounting records on behalf of their clients, and if so, whether they charge extra fees for record keeping, and whether, in their opinion, keeping accounting records reduces the tax compliance burden of SMEs. These questions were as follows:

**Question 7.1:** Does the business keep accounting records on behalf of the client? Please choose only one of the following:

- Yes
- No

**Question 7.2:** If you answered “YES” to question 7.1, does business charge the client for keeping the accounting record on the client’s behalf? Please choose only one of the following:

- Yes
- No

**Question 7.3:** If answered “YES” to question 7.2, how much does the business charge the client for keeping the accounting records on the client’s behalf?

.....

**3.7.3.4 Questions dealing with research question 8 in respect of the tax practitioners**

Section E covered questions relating to the benefits of being tax compliant. These questions were considered significant because they sought to identify determine whether tax practitioners agreed or disagreed that being tax compliant has certain benefits for SMEs, and if there are benefits, then what are those benefits? These questions were as follows:

**Question 8.1:** Would you agree that complying with tax obligations has some benefits for a small business? Please choose only one of the following:

- Yes
- No

**Question 8.2:** If you answered “YES” to question 8.1, please list at least four benefits that a small business can obtain from being tax compliant?

.....

**Question 9:** Please indicate whether you “Agree” or “Disagree” with the following statements.

<b>Statements:</b>	<b>Agree</b>	<b>Disagree</b>
Our tax laws are simple to understand.		
The tax rates for small businesses are high.		
There is little education provided to small businesses about tax laws, reforms, and tax administration.		
Tax compliance has a negative effect on the survival of small businesses.		
It is very expensive to hire someone to prepare the tax returns for small businesses.		

**Question 10:** What challenges do you think affects the tax compliance of SMEs?

.....

**Question 11:** In your opinion what do think the government needs to do to improve the tax compliance of SMEs? .....

**3.8 Covering letter**

The questionnaires were sent to the participants with a covering letter. A covering letter's purpose is to inform the participant about the questionnaire and to provide details about the participants’ requested actions. The overall layout of the letter accounts for the possibility that the participant will not read it completely. One of the most important aspects is that the letter be concise, as this can help increase responses by conveying important information (e.g., research topic, survey sponsor, incentives) that is likely to influence a participant's decision to cooperate and/or fully and accurately comply with the survey task (Lavrakas 2008). Appendix C shows the letter of information which accompanied the questionnaires.

When data is collected from human participants, informed consent is a fundamental principle of social research ethics. Informed consent develops because of a process in which key information about the research is communicated to potential participants in order to obtain their voluntary agreement to participate. There are two ways to confirm informed consent: oral consent and written consent (Laurie and Jensen 2017).

Hence, the main purpose for the letter of informed consent is to assure participants that confidentiality will be maintained and that the information collected from their responses will be used solely for the purposes of this study. There would be no financial benefits or any harm to them in participating in the study. Furthermore, the letter of informed consent sought to reach agreement from the participants to take part in the study.

The following topics were also addressed in the covering letter:

- title of the research study;
- principal researcher;
- supervisors;
- a brief introduction to the study and its purpose;
- a summary of the procedures; and
- In the event of any problems or questions, contact details of the person to contact.

Appendix C also includes the letter of informed consent, which included an agreement to participate in the study.

### **3.9 Pre-testing**

Pre-testing is used prior to steering a study to identify any errors or essential research glitches with the study tool (Zinkmud, Babin, Carr and Griffin 2010: 231). It was important to ensure that those asked to pre-test the questionnaire possessed the knowledge required to offer response on the survey and that they remained not among the SMEs and tax practitioners who had been identified as participants in this current study. The questionnaire aimed at SMEs was pre-tested by asking 10 SMEs, and for the questionnaire aimed at tax practitioners by asking five lecturers, for feedback on the wording and format of the questionnaire. According to the feedback, there were no questions or statements that were vague, unclear, or difficult to understand. However, a few changes were made in response to the feedback. Questions that included more than one aspect were separated into its component parts, and other questions were edited as needed.

### **3.10 Procedure for distribution of the questionnaires**

Emails were sent to all the identified SMEs and tax practitioners. The emails contained a link to the questionnaire which had been uploaded on the QuestionPro<sup>®</sup> platform. Each questionnaire was

accompanied by a letter of consent and information. The electronic versions of the two questionnaires were checked to ensure that they were identical to the version of the questionnaires that had been pretested.

Participants were given two months to complete the questionnaires. The distribution of questionnaires on QuestionPro<sup>®</sup> was done on 1 October 2021. On 30 November 2021 the data on the QuestionPro<sup>®</sup> platform in respect of the completed questionnaires was downloaded and the links to the two questionnaires was closed.

The discussion of the response rate is covered in the section that follows.

### 3.11 The response rates

Table 3.1 shows the response rate for both the SMEs and tax practitioners. In total, 660 questionnaires were distributed to the SMEs and 15 questionnaires were distributed to the tax practitioners. Of the 660 questionnaires distributed to the SMEs, 407 were returned but five could not be used because they were partially completed. Therefore only 402 questionnaires (61%) were considered usable for the SMEs.

Participants	Planned sample	Returned	Usable	Response rate (%)
SMEs	660	407	402	61%
Tax practitioners	15	15	15	100%

### 3.12 Data analysis and interpretation

#### 3.12.1 Data preparation

To prepare for data analysis, each question in the questionnaire was assigned a unique number. All the questionnaires were checked for completeness and only five questionnaires were discarded. To ensure that the responses were captured accurately on a Microsoft Excel spreadsheet, the entries were double checked against the responses each time the capturing process was completed per questionnaire. The data captured on the Excel spreadsheet was then uploaded into SPSS.

### **3.12.2 Data processing**

To avoid confusion or difficulties in data analysis later, the data was entered into SPSS with the same numbering as on the Excel spreadsheet and was analysed using the most recent version of SPSS V1.0.0.1406.

### **3.12.3 Statistical presentation and analysis of the data**

The results were presented using descriptive statistics and cross-tabulations. In some instances, inferential statistics were used and presented.

#### **3.12.3.1 Descriptive statistics**

The statistical description of the data set is provided by descriptive statistics. Mean, median, mode, variance, and standard deviation are examples of common descriptions (Sutanapong and Louangrath 2015). Furthermore, descriptive statistics are those that meaningfully describe or summarise a data set. The two types of descriptive statistics that are most used are those that describe central tendency (including arithmetic mean) and those that summarise distribution. Furthermore, the arithmetic mean is frequently used to describe a data set's central tendency by demonstrating the size or magnitude of a typical value in that data set (Allen 2017).

According to Allen (2017), the arithmetic mean is a measure of central tendency that is used to identify a single numerical value that is most typical or representative of a data set. The arithmetic mean, also known as the average or simply the mean, is the numerical average of all values in a data set (Allen 2017). It is the most used of the three most well-known measures of central tendency, along with the median (the middle value) and the mode (the most frequent value) (Allen 2017).

The arithmetic mean can be used as both a descriptive and an inferential statistic. It is also used in calculations for a variety of other statistical processes. The arithmetic mean is computed by adding all of the values in a data set and then dividing by the number of values in that data set. It is an unbiased calculation of the average, which means that large and small outliers have the same relative effect on the arithmetic mean value (Allen 2017).

### **3.12.3.2 Inferential statistics**

Inferential statistics are defined as using the sample descriptive statistics to make an inference (estimation) of the population (Sutanapong and Louangrath 2015). The following inferential statistics tests were used in the study to analyse data.

#### **3.12.3.2.1 Chi-square goodness-of-fit-test**

The chi-square test is a statistical test that is used to determine whether the observed (sampling) distribution or outcome differs significantly from an *a priori* or theoretically predicted outcome or distribution (Frey 2018). It is used to test hypotheses about the distribution of observations in different categories. This test statistic is also used to determine if the alteration amongst perceived and anticipated standards is statistically important (Moore *et al.* 2013) or whether the observed difference was caused by chance (Frey 2018).

#### **3.12.3.2.2 Binomial test**

Binomial experiments are made up of two or more independent trials, each of which results in one of two outcomes: success or failure (Frey 2018). The binomial test is used to determine whether the number of observed successes warrants rejecting an assumed probability of success in such experiments, as well as whether a significant proportion of respondents select one of two possible responses (Frey 2018).

#### **3.12.3.2.3 One sample t-test**

The t-test, according to Frey (2018), is a statistical hypothesis in which the test statistic uses the t distribution (also known as Student's t distribution) to define the test conclusion. When the sample size is small and the distribution appears normal, this test is used. It also determines whether a mean score differs significantly from a scalar value (Frey 2018). Although the t distribution is commonly used when there is unknown variation, the t-test is not required for larger sample sizes (Frey 2018).

Having discussed data analysis and interpretation, the chapter next focuses on how the research's quality was ensured.

### **3.13 Research quality**

The validity and reliability of the findings and techniques used in a study are referred to as research quality. The notch to which a research mechanism consistently measures what it is intended to measure to provide stable and consistent results is referred to as reliability (Sekaran and Bougie 2016). The meaningfulness of research components is concerned with validity. When researchers measure behaviours, they are concerned about whether they are measuring what they are supposed to measure (Sekaran and Bougie 2016).

#### **3.13.1 Reliability**

Reliability was ensured through pretesting the questionnaire to ensure that the participants undoubtedly understood the questions and instructions in the instrument. Anonymity and confidentiality for the participants was also assured to ensure that they answered the questions truthfully and honestly.

#### **3.13.2 Validity**

The questionnaires in this study were designed in accordance with the research objectives to ensure validity. The construct and content validity of the questionnaires were also addressed. In the case of construct validity, each questionnaire was divided into several sections with each section containing several questions. To improve content validity, the questionnaires were pretested by SME owners and taxation lecturers who were not involved in the study.

### **3.14 Ethical considerations**

This study required the participation of small businesses in Durban's Central Business District as well as tax practitioners who handle tax obligations on behalf of SMEs. The Faculty Research Ethics Committee granted ethical approval for the study. All participants received an informed consent letter outlining the study's objectives which they were required to sign.

Participants were also informed that the study's findings would be used solely for the purposes of the dissertation and that their names would not appear anywhere. No one was forced to participate in the study. The respondents' right to privacy and confidentiality was always respected, and they were allowed to withdraw from the survey for any reason they deemed necessary. Appendix B contains a copy of this letter.

### **3.15 Summary**

This chapter discussed the study's research design and methodology. The justification for the study methods used to assess the tax compliance burden in the functioning of SMEs in the Durban Central Business District was discussed. Because the primary goal of this research is to seal the information opening identified on the tax compliance burden for SMEs, the research paradigm was positivist. A questionnaire with both closed and open-ended questions was used as the research instrument. The data analysis procedure was described. The chapter also described the procedures used to improve the study's reliability and validity and ethical considerations. The presentation and analysis of the findings is covered in the following chapter.



## **CHAPTER FOUR**

### **PRESENTATION AND DISCUSSION OF THE RESULTS**

#### **4.1 Introduction**

Chapter 3 discussed the current study's research design and methodology.

This chapter provides the detailed analysis, interpretation and presentation of the results concerning the tax compliance burden in the functioning of SMEs in the Durban Central Business District, as well as whether the tax compliance burden is an impediment to the efficient functioning of these small businesses. These results are presented using descriptive statistics in the form of frequency tables.

Numerous studies (Herrington and Kew 2016; Nyamwanza *et al.* 2016; Smulders *et al.* 2016; Van Scheers 2018; Matarirano *et al.* 2019; Nieuwenhuizen 2019; Botha *et al.* 2020) have been conducted to assess the effect of tax compliance in the functioning of SMEs. The objectives of the study are addressed in this chapter through investigation of responses attained from SMEs and tax practitioners in the Durban Central Business District. The current study's findings are compared to selected studies discussed in Chapter 2 for assessment tenacities.

The chapter first discusses the responses of the respondents who represented the SMEs and thereafter discusses the responses of the tax practitioners. Although 402 questionnaires were useable, not every respondent answered each question. Therefore, in some of the tables, the number of respondents is shown at number lower than 402.

The section that follows provides background information on the respondents who represented SMEs.

#### **4.2 Biographical data and background information**

Respondents provided background information by answering questions in Section A of the questionnaire. This study requires background information because it plays a distinctive part in realising the aims of the study by allowing a richer analysis of the data as they provided information regarding the type of business, the number of years the business has been in existence,

as well as the determination of its annual turnover. The information pertaining to the respondents' background is presented in Tables 4.1 to 4.7.

The following section presents and analyses the respondents' main activity of business.

#### 4.2.1 Main activity of business

The background information in terms of the respondents' main activity of business is presented in Table 4.1

<b>Table 4.1: Main activity of business</b>		
	Number	%
Wholesale trade	90	22.4
Electricity, gas, water supply and waste services	25	6.2
Manufacturing	103	25.6
Retail trade (includes shops)	115	28.6
Construction (includes landscaping and repairs)	18	4.5
Transport, postal and warehousing	28	7.0
Accommodation and food services (includes cafes and restaurants)	12	3.0
Finance, insurance services	1	0.2
Rental, hiring and real estate services	10	2.5
Total	402	100.0

Table 4.1 shows that most of the SMEs (115 or 28.6% of the total sample) are in retailing, i.e., selling goods in stores. The second-highest proportion of respondents (103 or 25.6%) trade as manufacturers. The third-highest proportion of respondents (90, or 22.4%) trade as wholesalers. Only a small percentage of respondents (1 or 0.2%) provide financial or insurance services. This could be because such businesses require a lot of capital and administration to operate as an SME. These activities demonstrate that SMEs represent a wide range of business types and are SMEs are present in many of the sectors of the economy.

#### 4.2.2 Legal structure of the business

The legal structure of the SMEs in this study is presented in Table 4.2.

	Number	%
Sole proprietorship	2	.50
Partnership	8	2.00
Incorporated association	1	.25
Private company	389	97.00
Un-incorporated association	1	.25
Total	401	100.00

Table 4.2 reveals that most of the SMEs are operating as a private company (389 or 97%). This is followed by partnerships (8 or 2%). Incorporated associations are used by a small percentage of respondents (1 or .25%). It was expected that most SMEs would be registered as a private company because when a small business registers as a private company, it receives various tax benefits. Trading separately from the owner meaning the business has its own name and banking account and it is less risky as the shareholders are protected through limited liability. The *SME Landscape Report* (2018/2019) notes that even though it may be expensive to register a company, a reason why many SMEs register as a private company is because they are aware that they will not be held liable for the debts of the business, unlike when operating as a sole proprietor or partnership where they will be liable for all the debts of the business.

The background information is further presented and analysed in terms of the number of years the business has been trading.

**4.2.3 Number of years the business has been trading**

The number of years the business has been trading is presented in Table 4.3.

	Number	%
1-5 years	214	53.4
6-10 years	139	34.7
>10 years	48	11.9
Total	401	100

Table 4.3 indicates that most SMEs (214 or 53.4%) have been in business for at least 5 years. This was closely followed by SMEs (139 or 34.7%) that have been in business for between 6 to 10 years. A small number of SMEs (48 or 11.9%) had been in operation for more than ten years. The

study's findings are consistent with the *SME Landscape Report (2018/2019)*, which noted that most small businesses have been in operation for less than five years, while one-quarter of SMEs have been in operation for six to ten years.

Moloi (2013) noted that 75% of South African SMEs fail after only three years in operation. SMEs fail mostly due to cash-flow issues and an inability to control administrative costs, inflation costs, taxation costs, and business processes (SAICA 2016). Furthermore, despite the government's targeted interventions, the challenges faced by SMEs are numerous, and SMEs continue to fail at a high rate (Brink and Cant, 2003; Ferreira *et al.*, 2010; Cant and Wild 2013; Herrington *et al.* 2017).

The background information is next presented in terms of the number of owners (partners/directors) within the business.

#### **4.2.4 Number of owners (partners/directors) in the business**

The number of owners in the SME is presented in Table 4.4.

<b>Table 4.4: Number of owners</b>		
	Number	%
1 owner	371	97.64
2 owners	7	1.84
4 owners	1	0.26
6 owners	1	0.26
Total	380	100

Table 4.4 shows that most SMEs (371 or 97.64%) had only one owner. Seven (1.84%) of SMEs had two owners (partners/directors). Two SMEs (0.26%) indicated that they had four or six owners, respectively. This was expected because SMEs believe that running their own business is safer than running a business in a group (Gherhes *et al.* 2016); however, SMEs' tendency to owner manage their businesses results in a lack of management skills and avoidance of business growth, which leads to business failure (Gherhes *et al.* 2016).

In the following section, the level of education of the individual who is accountable for the tax matters of the business is presented.

#### 4.2.5 Level of education

To determine the SMEs' skill base, the SMEs were required to indicate the level of education of the person responsible for the tax matters of the businesses. Table 4.5 shows the level of education of the persons in charge of the SMEs' tax affairs.

	Number	%
No formal education	1	0.25
Tertiary education	398	99.75
Total	399	100

Note:  
Not every respondent answered this question.

According to Table 4.5, most respondents (398 or 99.75%) who are responsible for the tax affairs of the business have a tertiary education. This implies that SMEs may believe that someone with at least a tertiary education is needed to handle their tax matters as tax returns prepared by persons with accounting and tax qualifications have a better understanding of the tax system (Blaufus *et al.* 2011:16).

Only one SME (1, or 0.25%), stated that the person in charge of tax matters lacked formal education. As most SMEs outsource this function (see Table 4.14), it would be the tax practitioners who have the necessary tertiary education. Blaufus *et al.* (2011:16) found that the qualifications and experience of the tax preparer has a role in increasing the tax compliance costs of SMEs.

In the following section, information on the annual turnover of the business for the last tax year is presented.

#### 4.2.6 The annual turnover of the business

Table 4.6 shows the various ranges in which the business's annual turnover fell during the previous tax year.

	Number	%
0 – R525 000	81	20.1
R525 001- R1 000 000	76	18.9
R1 000 001-R3 000 000	83	20.6
R3 000 001–R7 000 000	68	16.9
R7 000 001- R14 000 000	41	10.2
More than R14 000 000	53	13.2
Total	402	100.0

According to Table 4.6, most respondents (83 or 20.6% of the total sample) had an annual turnover of between R1 000 000 and R3 000 000 in the previous tax year. Smulders *et al.* (2012) found that SMEs, at that time, had an annual turnover of between R1 000 000 and R3 000 000. The second largest number of respondents (81 or 20.1%) have an annual turnover for the previous tax year of R0 to R525 000, while the third largest number of respondents (76 or 18.9%) have annual turnover for the previous tax year of between R525 000 to R1 000 000.

These lower turnovers are consistent with the *SME Landscape Report (2018/2019)*, which stated that most small businesses generate less than R200 000 in revenue per year, while other SMEs generate between R200 000 and R1 000 000. This followed by 53 (13%) of SMEs who had annual turnover that is more than R14 000 000. The smallest proportion of respondents (41 or 10%) had an annual turnover of between R7 000 000 and R14 000 000 in the previous tax year.

Lastly, the categories of taxation under which the business fell are discussed.

#### **4.2.7 Category of tax under which the business falls**

Respondents were also asked to provide details about the tax category under which their business fell to determine whether the SMEs are small business corporations that pay income tax. The question included three categories, namely, a small business corporation which pays income tax, a non-profit organisation which is exempt from income tax, and a non-profit organisation which is not exempt from income tax.

These results are shown in Table 4.7.

	Number	%
A small corporation which pays income tax	401	100
Total	401	100

All the SMEs (401, or 100%) stated that they are small businesses that pay income taxes. This was expected because, “over the last six years, the number of businesses registered with SARS has increased by 61%, from 2 034 719 in 2011 to 3 278 708 in 2016, representing a 61% increase” (SARS 2016:131). Furthermore, many of these SMEs were registered with the DCCI in 2016 (and may currently still be registered), suggesting that they met the DCCI’s requirements to be on the DCCI data base.

#### **4.2.8 Summary of background information**

The background information revealed that most SMEs are registered as private companies that are managed by a single owner and that many trade as retailers. The analysis also reveals that most of the SMEs are registered for income tax and that the person who prepares tax returns on their behalf has a tertiary education.

Finally, the analysis revealed that most SMEs have an annual turnover for the most recent tax year of between R1 000 000 and R3 000 000, followed by SMEs with an annual turnover for the most recent tax year of between R0 to R525 000. It can also be concluded that the respondents can be classified as SMEs because they have an annual turnover that is less than R50 million and that they are owned or managed by one or more individuals.

### **4.3 Small and medium-sized enterprises**

This section offers a thorough examination of the SMEs' replies to questions about the costs of tax compliance, the effect of these tax compliance costs in the functioning of SMEs, and a tax-efficient approach that SMEs can use to reduce the tax compliance burden. These questions were addressed in the questionnaire's sections B through to G. Tables 4.8 to 4.28 discuss and present the results in a logical manner.

The next sector presents and discusses the results on the effect of tax compliance costs in the functioning of SMEs.

### 4.3.1 The effect of tax compliance costs in the functioning of SMEs (research question 1)

The first research question of this study was addressed by analysing the respondents' opinions on the effect of tax compliance costs in the functioning of SMEs. Although a business has many functions, this study focused on the operations of the business (measured by performance) and other tax-related activities which are necessary to ensure that the business is and remains tax compliant.

#### 4.3.1.1 The impact of tax compliance costs on the performance of SMEs

To analyse the effect of tax compliance costs on SMEs' performance, a question was posed to which respondents could respond Yes or No. Table 4.8 displays the results.

<b>Table 4.8: The impact of tax compliance costs on the performance of SMEs</b>				
Statements	Number (%)		n	p-value
	Yes	No		
Do tax compliance costs have any impact on the performance of your SME?	395 (99.0)	4 (1.0)	399	<.001*
Do you think tax compliance costs have a significant effect in the failure of SMEs?	391 (98.2)	7 (1.8)	398	<.001*
Note: * Significant at 95%.				

Table 4.8 shows that most SMEs (395, 99.0%) agree that tax compliance costs affect the performance of their businesses ( $p < .001$ ). SMEs (391, 98.2%) also agree they have a significant effect in the failure of SMEs ( $p < .001$ ). These findings support Sephapho *et al.* (2016) who found that SMEs agree that that tax laws have a significant effect on performance and can lead to small business failure.

#### 4.3.1.2 The effect of tax compliance costs on the performance of SMEs

Table 4.9 presents the respondents' level of agreement or disagreement with a number of statements describing the possible effect of compliance costs on SMEs. These statements were posed using a Likert scale ranging from 1 (strongly disagree) to 5 (strongly agree).



<b>Statements on the effect of tax compliance costs</b>	<b>Responses as frequency (%)</b>					<b>n</b>	<b>Mean (SD)</b>	<b>T</b>	<b>df</b>	<b>p-value</b>
	<b>Strongly disagree</b>	<b>Disagree</b>	<b>Neutral</b>	<b>Agree</b>	<b>Strongly agree</b>					
Affects the SMEs' performance	2 (.05)	3 (.7)	7 (1.7)	258 (64.2)	109 (27.1)	379	4.24 (.574)	41.956	27	<.001*
Causes SMEs to hide profits received	1 (.2)	1 (.2)	1 (.2)	104 (25.9)	286 (71.1)	393	4.71 (.506)	67.044	378	<.001*
SMEs may suffer business failure due to high compliance costs	-	2 (.5)	14 (3.5)	264 (65.7)	112 (27.9)	392	4.24 (.534)	45.975	391	<.001*
The tax system and its compliance requirements are a stumbling block to the growth of small businesses.	-	1 (.2)	10 (2.5)	172 (42.8)	207 (51.5)	390	4.50 (.563)	52.573	389	<.001*
High tax rates promote non-compliance with tax laws	-	1 (.2)	-	71 (17.7)	322 (80.1)	394	4.81 (.430)	83.503	393	<.001*
High tax rates are a reason most SMEs remain in the informal sector	1 (.2)	2 (.5)	-	72 (17.9)	322 (80.1)	397	4.79 (.474)	75.350	396	<.001*
Tax compliance costs reduce business productivity	-	16 (4.0)	25 (6.2)	251 (62.4)	82 (20.4)	374	4.07 (.674)	30.621	373	<.001*
Tax compliance costs diminish business resources	-	9 (2.2)	24 (6.0)	251 (62.4)	86 (21.4)	370	4.12 (.618)	34.847	369	<.001*
Note: *Significant at 95%										

Table 4.9 shows that all the means are  $>4.00$  which indicates that, on average, the respondents agreed with all the statements. Where the respondents expressed no opinion, this may be because they were unsure of the answer since all their tax-related matters are handled by a tax practitioner. Furthermore, the registration process for provisional tax, VAT and employee tax also increases the tax burden imposed on businesses (Sephapho *et al.* 2016). Okpeyoha *et al.* (2019) stated that tax rates have a significant role in increasing tax compliance of SMEs this result to SMEs to evade tax a possible choice.

#### **4.3.1.3 Summary of the results pertaining to research question 1 (on the effect of tax compliance costs in the functioning of SMEs)**

The analysis discovered that the respondents believed tax compliance costs have a significant effect on the failure and performance of SMEs. The analysis also discovered that the respondents supported the viewpoint that the complicated tax system and requirement has a pivotal role in the failure of the growth of SMEs, and that high tax rates encourage non-compliance with tax laws, causing SMEs to conceal profits and a significant number of SMEs to remain in the informal sector.

The following section presents and discusses the results based on questions relating to the level of tax knowledge of SMEs.

#### **4.3.2 Level of tax knowledge of SMEs (Research question 2)**

The questionnaire next examined the level of tax knowledge of the respondents. The first aspect to be investigated was whether the respondents had attended any tax training.

##### **4.3.2.1 SMEs' attendance of tax training**

To determine whether SMEs had received any tax training, a question was posed to which respondents could respond Yes or No. Table 4.10 displays the results.

		Category	N	Observed prop.	Test prop.	Asymp. Sig. (2-tailed)
Have you gone for any training regarding tax?	Group 1	No	365	.99	.50	.000*
	Group 2	Yes	3	.01		
	Total		368	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. * p<.001						

Table 4.10 shows that most SMEs (365, 99%) have never attended any training regarding tax matters. Table 4.11 supports this result as it indicates that SMEs do not know how to calculate, submit, and pay tax leading to SMEs hiring the services of tax practitioners.

#### 4.3.2.2 SMEs' ability to fulfil tax requirements

Table 4.11 shows the results of a question which asked whether the SMEs could meet any tax requirements on their own. The table is divided into two groups, with group 1 representing the Yes category and group 2 representing the No category.

		Category	N	Observed prop.	Test prop.	Asymp. Sig. (2-tailed)
How to calculate the tax liability of the business	Group 1	No	395	.99	.50	.000 <sup>a</sup>
	Group 2	Yes	3	.01		
	Total		398	1.00		
How long the tax records must be kept	Group 1	Yes	10	.03	.50	.000 <sup>a</sup>
	Group 2	No	389	.97		
	Total		399	1.00		
When to submit the tax returns of the business	Group 1	Yes	7	.02	.50	.000 <sup>a</sup>
	Group 2	No	389	.98		
	Total		396	1.00		
When to pay tax due to SARS	Group 1	No	372	.93	.50	.000 <sup>a</sup>
	Group 2	Yes	27	.07		
	Total		399	1.00		
How to make payment to SARS	Group 1	No	395	.99	.50	.000 <sup>a</sup>
	Group 2	Yes	3	.01		
	Total		398	1.00		

How to complete the business's tax return	Group 1	No	396	.99	.50	.000 <sup>a</sup>
	Group 2	Yes	3	.01		
	Total		399	1.00		
How to file the business's tax returns	Group 1	No	396	.99	.50	.000 <sup>a</sup>
	Group 2	Yes	3	.01		
	Total		399	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001						

According to Table 4.11, most SMEs do not know how to calculate their business's tax liability, how long tax records must be kept and when to file their business's tax returns. Furthermore, most SMEs do not know when and how to pay tax. Given that SMEs have never received any tax-related training, this was expected (see Table 4.10). Finally, SMEs are unable to complete the business's tax return and file tax returns. The business owners do not have tax knowledge as they lack tax training (Table 4.10). Nieuwenhuizen (2019) found that SMEs conceded that being tax compliant is essential, however, tax requirement should be simplified.

**4.3.2.3 SMEs' opinions on tax registration processes**

Table 4.12 examines SMEs' opinions on their businesses' tax registration processes. The table is divided into two categories where group 1 represents the Disagree category and group 2 represents the Agree category.

		Category	N	Observed prop.	Test prop.	Asymp.Sig. (2-tailed)
Our tax laws are simple to understand	Group 1	Disagree	388	.97	.50	.000 <sup>a</sup>
	Group 2	Agree	11	.03		
	Total		399	1.00		
The owners/partners and directors of the business can compute the tax liability of the business, if given little explanation of the tax laws	Group 1	Disagree	388	.98	.50	.000 <sup>a</sup>
	Group 2	Agree	9	.02		
	Total		397	1.00		
The tax rates for small businesses are high	Group 1	Agree	393	.99	.50	.000 <sup>a</sup>
	Group 2	Disagree	3	.01		
			396	1.00		

There is little education about tax laws and tax administration in South Africa	Group 1	Agree	390	.99	.50	.000 <sup>a</sup>
	Group 2	Disagree	5	.01		
	Total		395	1.00		
There is no equity and fairness in our tax system	Group 1	Agree	34	.09	.50	.000 <sup>a</sup>
	Group 2	Disagree	365	.91		
	Total		399	1.00		
It is very expensive for small businesses to hire tax practitioners to prepare their tax returns	Group 1	Agree	392	.98	.50	.000 <sup>a</sup>
	Group 2	Disagree	6	.02		
	Total		398			
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001						

Table 4.12 shows that a significant number of SMEs (388, 97%) disagreed that tax laws are simple to understand and indicated (388, 97%) that even if they are given a brief explanation of the tax laws, they will be unable to calculate the business's tax liability. Sephapho *et al.* (2016) found that SMEs contend that tax laws are written in a very complicated language.

SMEs also agree (393, 99%) that small business tax rates are high and that there is little education in South Africa about tax laws and tax administration (390, 99%). According to Deloitte (2019), SMEs' lack of tax knowledge continues to be a challenge for SMEs as they usually do not have the necessary staff resources and skills to appropriate and completely comply with all their tax obligations.

Even though taxes are a burden and a constraint for small businesses, a sizable number of SMEs (365, 91%) disagree that the tax system lacks equity and fairness. This may indicate that SMEs accept the necessity for the government to levy tax. Finally, SMEs (392, 98%) agree that hiring tax professionals to prepare their tax returns is very expensive for small businesses. The difficulty of tax procedures, rules, laws and computations must be simplified in order to improve the tax compliance of SMEs (Onoja and Odoma 2020).

#### **4.3.2.4 Summary on research question 2 (tax knowledge)**

The analysis reveals that most SMEs have never received any tax training. This is supported by the fact that a significant number of SMEs are incapable to calculate, pay, and submit their businesses' tax returns. SMEs state they are not able to file and complete their businesses' tax

returns and they don't know how long tax records must be kept. As a result, to register for these taxes, they need assistance; however, they also claim that paying for these services is costly. Tax knowledge has the potential to enable taxpayers to have the ability to perform their tax returns, as well save SMEs from incurring the cost of outsourcing the tax services (Oladipupo and Obazee 2016).

### 4.3.3 The costs associated with tax compliance (research question 3)

This section presents respondents' perspectives on the costs incurred by SMEs to be tax compliant. The study examined the costs incurred by businesses in terms of money and time spent to become tax compliant.

The results of the SMEs' answers on the costs associated with tax compliance are presented in Tables 4.13 – 4.20.

#### 4.3.3.1 Type of taxes paid

To determine the type of taxes paid to SARS by the business, a question was asked to which respondents could respond Yes or No. Table 4.13 displays the results.

		Category	N	Observed prop.	Test prop.	Asymp. Sig. (2-tailed)
PAYE	Group 1	Yes	387	.97	.50	.000 <sup>a</sup>
	Group 2	No	11	.03		
	Total		398	1.00		
VAT	Group 1	Yes	385	.97	.50	.000 <sup>a</sup>
	Group 2	No	11	.03		
	Total		396	1.00		
Income tax	Group 1	Yes	389	.97	.50	.000 <sup>a</sup>
	Group 2	No	10	.03		
	Total		399	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001						

Table 4.13 shows that most respondents, except for 11 (PAYE and VAT) and 10 (income tax) respondents, are paying the taxes shown in the table. Some of the respondents are not paying VAT

because their total value of taxable goods or services is not more than R1 million in a 12-month period. They are also not paying income tax because their annual turnover does not exceed R335 000 annually. According to Sephapo *et al.* (2016), the majority of SMEs in South Africa are registered for income tax, provisional tax and VAT but registering a business for VAT with SARS tends to be a bigger barrier in the views of medium-sized businesses compared to other sized businesses (Botha *et al.* 2020).

#### 4.3.3.2 Completion of tax return

The questionnaire next focused on who completes the tax returns on behalf of the business. Respondents could choose between either an external person, such as a tax practitioner, or a person employed within the business. The responses in Table 4.14 are divided into two groups: Group 1 represents the use of external tax professionals by SMEs, and Group 2 represents the use of either the owner or an employee to complete tax returns.

<b>Table 4.14: Completion of tax return</b>						
Tax returns		Category	N	Observed prop.	Test prop.	Asymp.Sig. (2-tailed)
PAYE	Group 1	External tax professionals	392	.99	.50	.000*
	Group 2	Employee or owner	4	.01		
	Total		396	1.00		
VAT	Group 1	External tax professionals	392	.99	.50	.000*
	Group 2	Employee or owner	2	.01		
	Total		394	1.00		
Annual income tax return	Group 1	External tax professionals	398	.99	.50	.000*
	Group 2	Employee or owner	1	.01		
	Total		399	1.00		
Provisional tax	Group 1	External tax professionals	390	.99	.50	.000*
	Group 2	Employee or owner	2	.01		
	Total		392	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. * p<.001						

Table 4.14 shows that most of the SMEs use tax practitioners to prepare all the listed returns,  $p < .001$ . These results were expected as using a tax practitioner significantly reduces the tax compliance burden borne by small businesses (Smulders *et al.* 2016). Although outsourcing of the tax returns to tax practitioners reduces the administrative burden, it adds to it in terms of cost (Smulders 2013).

Using tax consultants raises the costs of tax compliance (external tax compliance) (Smulders *et al.* 2016). Furthermore, the tax system places a significant burden on small business taxpayers, particularly in the form of external tax compliance costs, and thus requires scrutiny. The fact that small businesses are resource constrained and cannot afford the services of tax practitioners makes tax compliance costs an unwanted and unnecessary burden (Matariano *et al.* 2019).

#### 4.3.3.3 Annual costs of outsourcing tax services

To estimate SMEs' annual cost of engaging external tax professionals, a question was posed to which respondents were asked to estimate the annual cost of engaging external tax professionals. Table 4.15 displays these findings.

Tax returns	Responses as frequency (%)					X <sup>2</sup>	Df	p-value
	R2 500-R5000	R5001-R7500	R7501-R10 000	R10 001-R12 500	Not sure			
PAYE	161 (41.1)	59 (15.1)	131 (33.4)	38 (9.7)	1 (3)	225.487	4	<.001
VAT	110 (28.1)	83 (21.2)	24 (6.1)	163 (41.6)	5 (3)	214.468	4	<.001
Annual tax return (income tax)	71 (17.8)	85 (21.4)	68 (17.1)	165 (41.5)	1 (3)	175.590	4	<.001
Provisional tax	138 (35.4)	72 (18.5)	118 (30.3)	40 (10.3)	9 (2.3)	151.289	4	<.001

Notes:  
X<sup>2</sup> tests if a significant number selected any response option(s) over others.  
Df means 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 77.0.



Table 4.15 shows that a significant number of SMEs pay for PAYE services amounts between R2500 to R5000 or amounts between R7501 to R10000, ( $p < .001$ ). The EMP201 which includes UIF and the SDL has to be completed monthly, but its complexity (and cost for completion) may depend on the number of employees in a business and the type of record keeping which is used for salaries and wages.

For VAT services, amounts between R10 0001 to R12 500, R2 500 to R5 000 and R5 001 to R7 500 ( $p < .001$ ) were the most paid. SMEs are required to complete a certain number of VAT returns depending on the VAT category the business falls under. The cost of completing the VAT201 may reflect the complexity of the businesses' transactions and the SMEs' record keeping and this may account for the varying amounts reported by the respondents. Since the DTC (2014) reported that VAT increases the tax compliance burden for SMEs and as the cost of complying with VAT requirements is the highest of all taxes, it was expected that the cost for completing VAT returns would be expensive.

For the completion of annual income tax returns, most SMEs paid between R10 001 to R12 500 ( $p < .001$ ). It was anticipated that the calculation of annual income tax returns would be costly, particularly for SMEs with a high turnover. This is because as turnover increases, so does the number of transactions, which results in an increase in the fees for outsourcing these services.

Lastly, a significant number of SMEs pay between R2 500 to R5000 or R7 501 or R10 000 ( $p < .001$ ) for completion of the provisional tax return. The provisional tax return was expected to be less expensive because there are only two returns required per year, which means that SMEs must file one provisional return by the end of August, with a second provisional return due by the end of February (end of tax season). If the amounts declared and paid in the previous submissions was insufficient, the entity may make an optional third payment within six months of the year of assessment.

These results confirm those of Smulders *et al.* (2012:202) who revealed that external tax compliance costs increased as the size of the business as measured by turnover increased. The costs were also found to be regressive, with smaller businesses spending more (Smulders *et al.* 2012).

#### 4.3.3.4 Reasons for paying penalties and interest

Table 4.16 shows possible reasons for SMEs paying penalties and interest as reported by the respondents. The table is divided into two categories where group 1 represents the Yes category and group 2 represents the No category.

		Category	N	Observed prop.	Test prop.	Asymp. Sig. (2-tailed)
Non filing of returns	Group 1	Yes	128	.33	.50	.000 <sup>a</sup>
	Group 2	No	265	.67		
	Total		393	1.00		
Filing returns after due date	Group 1	Yes	128	.33	.50	.000 <sup>a</sup>
	Group 2	No	264	.67		
	Total		392	1.00		
Incomplete or incorrect calculations	Group 1	Yes	105	.27	.50	.000 <sup>a</sup>
	Group 2	No	287	.73		
	Total		392	1.00		

Table 4.16 shows that about one-third of the respondents indicated that they have paid penalties and interest. The respondents (33%) stated that non filing of returns is one of the reasons that leads to the payment of penalties. A similar number of SMEs (33%) pay penalties because of filing returns after the due date. Finally, 27% of the SMEs emphasised that incomplete or incorrect calculations are also a reason they pay penalties and interest. Due to the complexity of their tax requirements, SMEs should seek the advice of tax practitioners to ensure they understand the penalty provisions and avoid being levied with penalties (Hall 2013).

#### 4.3.3.5 Amount of penalties and interest

Table 4.17 shows the total amount SMEs pay because of penalties and interest as reported by the respondents. Only 115 respondents answered this question.

Number	115
Mean	1 622.98
Std. deviation	1497.230
Minimum amount in rands	50
Maximum amount in rands	11 980

Table 4.17 shows that a mean amount of R1 622.98 to a maximum of R11 980 was paid by the SMEs. It can be concluded that penalties are expensive for SMEs, and they may have a significant effect in the functioning of SMEs.

#### 4.3.3.6 Outsourcing of payroll external services in the last tax year

Payroll complexities may lead SMEs to engage external help. To determine whether SMEs did pay for external payroll services in the previous tax year, a question was posed to which the respondents could answer Yes or No. These results are shown in Table 4.18.

		Category	N	Observed prop.	Test prop.	Asymp. Sig. (2-tailed)
Did the business pay for any payroll external services in the last tax year?	Group 1	Yes	383	96	.50	.000 <sup>a</sup>
	Group 2	No	14	04		
	Total		397	100		

According to Table 4.18, most SMEs (383 or 95.3%) indicated that they did pay for outsourcing payroll services in the previous tax year. Egiyi *et al.* (2020) found that outsourcing accounting services by SMEs, including payroll services, improves the company's focus on important business-related matters as it frees up time. It is possible that for these SMEs, the outsourcing of their payrolls enabled them to focus more on their day-to-day operations.

#### 4.3.3.7 Total amount paid for payroll external services in the last tax year

Table 4.19 shows the total amount SMEs paid for payroll external services in the last tax year as reported by the respondents.

Number	382
Mean	10749.2052
Std. deviation	5434.43299
Minimum amount in rands	1123.00
Maximum amount in rands	25 000

Table 4.19 shows that SMEs paid a mean amount of R10 749.21 (minimum of R1 123 and a maximum of R25 000) for payroll services. Payroll services are determined by the number of employees in the business. A small business with low turnover may have few employees, resulting

in low payroll service fees, whereas a large business with higher turnover may have more employees, resulting in high payroll service fees.

#### 4.3.3.8 Estimated annual cost of external tax and accounting related services

To determine the total amount paid by SMEs for outsourcing external tax and accounting services in the previous tax year, a question was posed in which respondents were asked to estimate the annual cost of external tax and accounting related services. Table 4.20 displays the results.

External tax and accounting related services	Responses					X <sup>2</sup>	df	Asymp. Sig. (2-tailed)
	R5 000-R10 000	R10 001-R15 000	R15 001-R20 000	R20 001-R25 500	R25 001-R30 000			
Tax cost	95 (23.6%)	57 (14.2%)	66 (16.4%)	163 (40%)	17 (4.2%)	148.322a	4	.000*
Accounting cost	127 (31.6%)	100 (24.9%)	108 (26.9%)	62 (15.4%)	1 (2.4%)	125.090a	4	.000*
Payroll costs	167 (41.5%)	126 (31.3%)	90 (22.4%)	5 (1.2%)	-	146.948b	3	.000*

Notes:  
X<sup>2</sup> tests if a significant number selected any response option(s) over others.  
Df: 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 78.0.  
\* p<.001

Table 4.20 shows that SMEs paid between R5 000 to R30 000 for tax services annually, with many (163) paying between R20 0001 to R25 500. For accounting costs, most SMEs paid between R5 000 to R20 000, and a significant number of SMEs paid between R5 000 to R15 000 for payroll costs. Kipsang and Mwangi (2017) argued that outsourcing accounting and tax services are an option for SMEs looking to improve their performance and maintain a competitive advantage in today's business environment.

#### **4.3.3.9 Summary of the results for research question 3 (on the cost incurred by SMEs to be tax compliant)**

The analysis on the costs to be tax compliant of SMEs reveal that, for SMEs to be tax compliant, they rely on tax practitioners because they believe that outsourcing tax services from tax practitioners has significant compliance and management benefits (Oosthuizen *et al* 2020). The analysis also revealed that for SMEs to engage external professional tax services on an annual basis for returns such as PAYE, VAT, the annual income tax return and provisional tax, the costs ranged between R2 500 and R10 000 per return.

The analysis also revealed that non-filing of returns, filing of returns after the due date, and incomplete or incorrect calculations are the reasons that led to SMEs paying penalties, with penalties or interest usually costing from a minimum of R50 to a maximum of R11 980. Furthermore, a significant number of SMEs outsourced payroll services, and they pay a minimum of R1 123 to a maximum of R25 000 for these services.

Finally, the analysis revealed that annual external tax and accounting related services, which include tax, accounting and payroll services, costs between R5 000 and R20 000 per year. This shows that the smallest firms may struggle with tax compliance because they may not be able to afford the fees payable to tax practitioners (Oosthuizen *et al.* 2020).

The following section presents and discusses the results on tax efficient approaches SMEs can apply to minimise tax compliance burden.

#### **4.3.4 Tax-efficient approaches SMEs can apply in order to minimise the cost of tax compliance (research question 4)**

This section provides respondents' perspectives on the tax-efficient approaches that SMEs can apply to reduce the cost of tax compliance. It addresses the fourth research question of this study, which was to examine whether SMEs used tax incentives and record-keeping to reduce the costs of being tax compliant.

##### **4.3.4.1 Factors that can reduce the cost of tax compliance**

To determine the factors that can reduce the cost of tax compliance, a question was first posed listing several statements on factors that could reduce the costs of tax compliance. Respondents

could respond by selecting less important, important, or very important against each statement. Table 4.21 displays the results.

<b>Table 4.21: Respondents' rating of the factors that can reduce the costs of tax compliance</b>						
	Responses as frequency (%)			X <sup>2</sup>	Df	Asymp Sig.
	Low importance	Important	Very important			
Low tax rates for SMEs	-	31 (7.7)	368 (92.3)	284.634 <sup>a</sup>	1	.000 *
Frequent tax education for SMEs	-	95 (50.0)	95 (50.0)	109.476 <sup>a</sup>	1	.000 *
Electronic filing and payment of taxes	-	9 (2.3)	390 (97.7)	363.812 <sup>a</sup>	1	.000 *
Tax practitioners to be paid by government to render free services to SMEs in tax filing and record keeping	1 (0.2)	72 (18.0)	326 (81.7)	439.053 <sup>b</sup>	2	.000 *
Tax laws should be simplified and practical	1 (0.2)	300 (75.4)	97 (24.3)	351.322 <sup>c</sup>	2	.000 *
Tax laws should be practical	1 (0.2)	332 (86.6)	50 (13.1)	499.963 <sup>d</sup>	2	.000 *
Strong monitoring and enforcement of tax laws by tax officials	356 (88.6)	19 (4.7)	23 (5.7)	564.005 <sup>c</sup>	2	.000 *
Notes: X <sup>2</sup> tests if a sig number selected any response option(s) over others. Df means the following: <sup>a</sup> 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 199.5. <sup>b</sup> 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 133.0. <sup>c</sup> 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 132.7. <sup>d</sup> 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 127.7. * p<.001						

Table 4.21 shows that a significant number of SMEs emphasised that low tax rates, electronic filing and payment of taxes, the government to pay tax practitioners so as to provide free services to SMEs in tax filing and record keeping, and that the tax laws should be simplified and practical as being important or very important factors in reducing the costs of compliance. Those who use computerised systems and e-filing are less likely to make mistakes, lowering the likelihood of engaging costly external service providers, and thus e-filing reduces tax compliance costs (Yilmaz and Coolidge 2013). Smulders *et al.* (2016) also stated that SMEs that use a computerised accounting system to assist with tax compliance have lower external tax compliance costs than

SMEs that use a manual system. This could be because a computerised system provides quality calculations, reports, and information to the business, eliminating the need for an external service provider to devote time to these functions (Smulders *et al.* 2016).

Although only 190 SMEs answered the question on frequent tax education, those SMEs who did answer rated frequent tax education as important or very important in reducing the costs of compliance. Finally, a sizable proportion of the SMEs (356, 88.6%) indicated that strong monitoring and enforcement of tax laws by tax officials was of low importance as a factor in lowering tax compliance costs. This is possibly because SMEs believe that instead of strong monitoring and enforcement of tax laws by tax officials the government should focus more on developing strategies for improving the compliance of SMEs. The strategies may include tax initiatives, frequent tax education on e-filing, simplification of tax laws and more tax incentives.

#### 4.3.4.2 The eligibility for tax incentives

It is possible that the use of tax incentives may reduce the costs of tax compliance. To determine whether SMEs were eligible for tax incentives during the last tax year, a question was posed to which the respondents could answer Yes or No. These results are shown in Table 4.22.

<b>Table 4.22: The eligibility for incentives during the last tax year</b>						
		Category	N	X <sup>2</sup>	Df	Asymp.Sig (2-tailed)
Was your business eligible for any of the small business tax incentives during the last tax year?	Group 1	Yes	159	164.075 <sup>a</sup>	2	.000*
	Group 2	No	18			
	Group 3	Unsure	222			
	Total		399			
Notes: X <sup>2</sup> tests if a significant number selected any response option(s) over others. * p<.001 Df means the following: a.0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 133.0.						

Table 4.22 shows that 222 SMEs responded ‘Unsure’. The awareness of the small business tax incentives appears to be problematic, particularly in South Africa (Evans *et al.* 2014). Botha *et al.* (2020) concluded that many SMEs are unaware of the tax incentives. This is due to the complexity of these concessions, which necessitates either more internal time spent understanding and applying these concessions or the use of an external service provider to assist with these functions, resulting in an increase in the external tax compliance costs of small businesses (Freedman 2006:59; Pope 2008:33; Smulders *et al.* 2016). To improve the level of awareness of these

incentives, the government could try to improve the relationship between SMEs and government agencies, particularly those dealing with taxes, by making extensive use of new technologies and improve the frequency of tax education.

#### 4.3.4.3 Use of tax incentives

To determine whether SMEs took advantage of any of the small business tax incentives during the last tax year, a question was posed to which respondents could respond Yes or No. Table 4.23 displays the results.

		Category	N	Observed prop.	Test prop.	Asymp.Sig (2-tailed)
Did your business use any of the small business tax incentives during the last tax year?	Group 1	Yes	148	.97	.50	.000 <sup>a</sup>
	Group 2	No	5	.03		
	Total		153	1.00		
Notes: Not every respondent answered this question. This may be due to the fact some of the respondents did not understand what is meant by the tax incentives. Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001						

According to Table 4.23, a significant number of SMEs responded with "YES," indicating that they did take advantage of tax incentives in the previous fiscal year. Evans *et al.* (2014) found that a significant number of eligible SMEs used SBTCs, demonstrating that SBTCs were well-adopted once businesses were aware of their eligibility. SAICA (2016) argues that SMEs with a turnover of less than R20 million believe that the created tax incentives have not aided small businesses to grow. Botha *et al.* (2020) also stated that SMEs with less than R20 million in revenue believe that the DSBD has not aided in the creation of tax incentives for small businesses to grow. As a result, despite the government's efforts over the last two decades to assist the SME sector, much more work is required. Incentives to assist this sector should be stratified and more targeted, based, for example, on the size of the business (Botha *et al.* 2020).

#### 4.3.4.4 SMEs’ record keeping

To determine whether SMEs do keep records in the business, a question was posed to which the respondents could answer Yes or No. These results are shown in Table 4.24.



		Category	N	Observed prop.	Test prop.	Asymp.Sig (2-tailed)
Which one of the following applies to your business?	Group 1	There is record keeping in the business	391	.98	.50	.000 <sup>a</sup>
	Group 2	There is no record keeping in the business	8	.02		
	Total		399	1.00		

Notes:  
 Prop test (binomial test) tests if a significant proportion selected YES or NO.  
<sup>a</sup>p<.001

According to Evans *et al.* (2014), most small business taxpayers keep records not only for tax purposes, but also for accounting information which is used for internal management and external reporting. The current study's findings are consistent with these findings, as shown in Table 4.24, where 391 (97.3%) of the SMEs indicated that they keep records in their businesses. Evans *et al.* (2014) found that while 76% of South African SMEs agreed that tax compliance improved their record keeping, only 69% said it improved financial knowledge about their business.

#### 4.3.4.5 The type of accounting system used

Table 4.25 shows the type of accounting system used in the business. Respondents were asked to select from one of three options in the questionnaire.

	Number	Percentage
No accounting system used	1	0.25
Paper based/Manual	1	0.25
All the work is done by an external accountant	392	97.50
Total	394	100

According to Table 4.25, external accountants handle all the work for 97.5% of the SMEs. This was expected given that a study found that SMEs do not have sufficient tax knowledge and do not have a deep understanding of tax issues (Wadesango *et al.* 2018). This leads SMEs to use the services of tax practitioners due to having inexperienced employees in tax matters (FIAS) 2007:20).

#### 4.3.4.6 The costs incurred in keeping records

Table 4.26 shows the results of a YES or NO question asking whether SMEs incur any costs in maintaining records.

		Category	N	Observed prop.	Test prop.	Asymp.Sig (2-tailed)
If your business does its own record keeping, do you incur any costs in keeping the records?	Group 1	Yes	9	.14		
	Group 2	No	57	.86		
	Total		66	1.00	.50	000 <sup>a</sup>
<b>Notes:</b> Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001						

Although only 66 respondents answered this question, Table 4.26 shows that a sizable proportion of SMEs (57 or 86%) stated that the keeping of records is free. This question may have been misinterpreted by the respondents, answering as to the physical storage of the records rather than the recording of any accounting transactions.

#### 4.3.4.7 The benefit of being tax compliant

Table 4.27 shows the results of a question asking whether SMEs believed that complying with tax obligations benefits their businesses. The question required respondents to answer either YES or NO.

		Category	N	Observed prop.	Test prop.	Asymp.Sig (2-tailed)
Overall, would you agree that complying with tax obligations has some benefits for your business?	Group 1	Yes	355	.90	.50	000 <sup>a</sup>
	Group 2	No	38	.10		
	Total		393	1.00		
<b>Notes:</b> Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001						

Table 4.27 shows that a significant number of SMEs (355, 90%) agreed that complying with tax obligations benefits the business. However, while countless SMEs are conscious of the benefits of being tax compliant, which includes better decision making and financial information management, a small number of them did not agree that there is a benefit in being tax compliant.

Evans *et al.* (2014) found that tax incentives and initiatives do not seem to play a pivotal role in assisting SMEs in reducing the cost that comes with being tax compliant.

#### **4.3.4.8 The benefits of being tax compliant**

Table 4.28 shows the respondents' level of agreement or disagreement with several statements about the advantages of being tax compliant. The respondents were asked to indicate their level of agreement using a Likert scale of 1 (strongly disagree) to 5 (strongly agree).

Table 4.28: The benefits of being tax compliant													
Statements	Responses as frequency (%)					T	df	Sig (2-tailed)	mean	SD	Mean difference	95% Confidence Interval of the Difference	
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree							Lower	Upper
	Complying with tax obligations helps to improve the record keeping of the business.	16 (4.0)	106 (26.4)	1 (.2)	216 (53.7)							61 (15.2)	8.677
Tax compliance helps improve knowledge of the financial status of the business.	13 (3.2)	106 (26.4)	1 (.2)	216 (53.7)	61 (15.2)	15.097	398	.000	3.52	1.091	.825	.72	.93
Complying with tax obligations helps improve knowledge of the profitability of the business.	25 (6.2)	95 (23.6)	2 (.5)	220 (54.7)	47 (14.2)	8.024	398	.000	3.47	1.179	.474	.36	.59
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. <sup>a</sup> p<.001													

Table 4.28 shows that a significant number of SMEs agreed (216) or strongly agreed (61) that complying with tax obligations helps to improve the business's record keeping ( $m=3.50$ ), and the same number of SMEs agreed or strongly agreed that being tax compliant helps to improve the business's knowledge of its financial status ( $m=3.52$ ). Furthermore, 220 SMEs agreed, and 47 SMEs strongly agreed, that complying with tax obligations helps improve knowledge of the business's profitability ( $m=3.47$ ). Although the means were all lower than 4.00 (strongly agree), this demonstrates that SMEs recognise the importance of being tax compliant, as SMEs perceive that it has an impact on the operations of their businesses; therefore, if the government can keep tax rules as clear and simple as possible, more SMEs will be encouraged to register for tax.

#### **4.3.4.9 Summary of research question 4**

The overall pattern observed for the entire analysis of respondents' perspectives on a tax efficient approach SMEs can apply in order to minimise tax compliance burden reveals that low tax rates, electronic filing and payment of taxes, as well as payment of tax practitioners by the government to render free services to SMEs in tax filing and records keeping are all very important in reducing tax compliance costs. Studies have found that electronic filing reduces the costs of tax compliance that would have been incurred if the manual system had been used (Coolidge *et al.* 2009:12; Smulders 2013:105).

According to the analysis, the importance of frequent tax education and making tax laws practical and simple are all very important in lowering tax compliance costs. Furthermore, respondents agreed that tax officials' strong monitoring and enforcement of tax laws is of low importance in reducing tax compliance costs. The analysis also reveals that many SMEs did not qualify for tax incentives and those who did qualify used the incentives during the previous tax year. SMEs also indicated that they keep records in their businesses and tax laws should be communicated to them in a simplified language.

The analysis also reveals that most SMEs use the services of tax practitioners to fulfil their tax obligations. They indicated that being tax compliant has some advantages for their businesses, such as better record keeping, and a better understanding of the financial status and profitability of the business. This was expected because the main reason why SMEs outsource tax services is that they are unable to calculate, pay and submit their tax returns, know how to file, complete the

income tax return of their businesses, or how long tax records must be kept. Almost every SMEs does pay PAYE, income tax and VAT but they are unable to register for these tax returns, so they seek assistance in preparing the necessary documents.

Finally, the analysis reveals that even if owners of SMEs are given a brief explanation of the tax laws, they are unable to compute the business's tax liability. in South Africa there is little education about tax laws and tax administration and the tax laws are not simple to understand (Musimenta 2020). Furthermore, SMEs agree that the tax rate for small businesses is high, and it is very expensive for small businesses to hire tax practitioners.

The next section focuses on the questionnaire which was aimed at tax practitioners.

## 4.4 Tax practitioners

The following section presents the background data of the tax practitioners.

### 4.4.1 Background data

The background information was obtained from the tax practitioners through answering questions in Section A on the legal structure of the business, the number of years the respondent's business has been in operation and the number of owners in the business. Background information is required for this study because it plays a unique role in achieving the study's objectives. Tables 4.29 to 4.30 present information about the respondents' backgrounds.

The following section presents and analyses the respondents' legal structure of their businesses.

#### 4.4.1.1 Legal structure of the business

Table 4.29 shows the legal structure of business according to the respondents.

<b>Table 4.29: Legal structure of the business</b>		
	Number	%
Sole proprietorship	1	5.6
Partnership	4	22.2
Private company	13	72.2
Total	18	100.0

Table 4.29 reveals that most tax practitioners operate as a private company (13 or 72.2%). This is followed by a partnership (4 or 22.2%). Only one tax practitioner was working as an unincorporated association (1 or 5.6%).

#### 4.4.1.2 The number of years in practice

Respondents were asked for how long their business has been in operation. These results are shown in Table 4.30.

<b>Table 4.30: The number of years the business has been operating</b>		
	Number	%
3-5 years	1	5.6
6-10 years	5	27.8
>10 years	12	66.6
Total	18	100.0

Table 4.30 shows that most respondents (12 or 66.6%) have been in business for more than ten years. This is closely followed by those who have been in the business for six to ten years (5 or 27.8%). The smallest proportion of respondents (1 or 5.6%) have been practicing for three to five years. This was expected because, to become a tax practitioner, a person must have three years of verifiable practical experience in a tax environment, and SMEs may evaluate the superiority of the service based on the number of years the tax practitioner has been practicing. Table 4.30 shows that most of the tax practitioners have sufficient experience to be able to provide knowledgeable answers to the questionnaire.

In summary, most of the tax practitioners were registered as a private company and have been in business for at least six years.

#### 4.4.2 Costs incurred by SMEs to be tax compliant (Research question 6)

The study first investigated, from the tax practitioners' perspectives, tax related activities outsourced by SMEs, the annual fee charged by the firm for pre-filing, filing, and post-filing, the annual cost of outsourcing the service of tax practitioners, the total amount SMEs pay for payroll services and the average time taken per annum to prepare, complete and submit tax returns. These questions aimed to answer research question 6 which was on the costs incurred by SMEs to be tax

compliant. (Note that the corresponding research question from the SMEs' perspectives was research question 3.)

#### 4.4.2.1 Tax related activities outsourced by SMEs

The tax practitioners were asked to indicate the tax-related activities which are outsourced to them. Table 4.31 shows the results of this question which listed several tax-related activities. The responses are divided into two categories, Group 1 represents the NO category and Group 2 represents the YES category.

		Category	N	Observed prop.	Test prop.	Asymp.Sig. (2-tailed)
Audit-related services	Group 1	No	1	.06		
	Group 2	Yes	17	.96	.50	.000*
	Total		18	1.00		
Collection matters	Group 1	Yes	18	1.00	.50	.000*
	Total		18	1.00		
Preparing the tax return (ITR14)	Group 1	Yes	18	1.00	.50	.000*
			18	1.00		
Preparing the provisional tax return	Group 1	Yes	18	1.00	.50	.000*
	Total		18	1.00		
Preparing amended returns	Group 1	No	1	.06		
	Group 2	Yes	17	.96	.50	.000*
	Total		18	1.00		
Preparing the VAT return (VAT201)	Group 1	Yes	18	1.00	.50	.000*
	Total		18	1.00		
Preparing the PAYE, SDL and UIF return (EMP201)	Group 1	Yes	18	1.00	.50	.000*
	Total		18	1.00		
Record keeping services	Group 1	Yes	18	1.00	.50	.000*
	Total		18	1.00		
Tax planning	Group 1	Yes	18	1.00	.50	.000*
	Total		18	1.00		
Audit-related services	Group 1	No	4	.22	.50	.031
	Group 2	Yes	14	.78		
	Total		18	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. * p<.001						



Table 4.31 shows that a significant number of tax practitioners indicated that all these types of tax services are outsourced to them by SMEs. This was expected because SMEs lack the knowledge and skills to calculate these types of taxes on their own, and small businesses rely on outsourcing tax service because they don't possess tax skills and knowledge (Lubbe and Nienaber 2012). SMEs with appropriately qualified tax personnel will incur lower tax compliance costs (Matariano *et al.* 2019).

#### 4.4.2.2 Annual fee charged for pre-filing, filing and post filing tax activities

Table 4.32 shows the annual fees charged by tax practitioners for pre-filing, filing, and post-filing tax activities. The questions were used costs ranging from R2 500 or less to R10 000 or more to determine the total fee.

	Responses as frequency (%)				X <sup>2</sup>	df	Asymp Sig.
	Less than R2500	R2500 - R4999	R5000 - R9999	R10000 - R14999			
Pre-filing activities	1 (5.6)	2 (11.1)	14 (77.8)	1 (5.6)	26.889 <sup>a</sup>	3	.000*
Filing activities	1 (5.6)	1 (5.6)	14 (77.8)	2 (11.1)	26.889 <sup>a</sup>	3	.000*
Post-filing activities.	1 (5.6)	2 (11.1)	12 (66.7)	3 (16.7)	26.889 <sup>a</sup>	3	.001
Notes: X <sup>2</sup> tests if a significant number selected any response option(s) over others. *p<.001 Df means the following: <sup>a</sup> 0 cells (100%) have expected frequencies less than 5. The minimum expected cell frequency is 4.5.							

Table 4.32 show that most tax practitioners (14, 77.8%) charge SMEs between R5 000 to R10 000 for both pre-filing activities such as tax planning, obtaining tax guidance, information, and maintaining tax records and for filing activities such as data collection, preparation of the ITR from financial data, and calculation of the tax owed (including VAT201 and EMP201 returns). Furthermore 12 (66.7%) tax practitioners indicated that they charge SMEs an annual fee of between R5 000 to R10 000 for post-filing activities e.g., preparing amended returns, the audit

process etc. To provide further analysis of these costs, the fees for filing returns was examined next.

#### 4.4.2.3 The annual fees charged by tax practitioners for tax returns

Table 4.33 shows the annual fees charged by tax practitioners for preparing the various tax returns. To determine the total fee, the questionnaire used costs ranging from R2 000 or less to R8 000 or more.

Tax returns	Responses as frequency (%)			X <sup>2</sup>	Df	Sig. (2-tailed)
	R2000 or less	R6000 - R7999	R8000 or more			
Income tax return (ITR 14)	1 (5.6)	1 (5.6)	16 (88.9)	25.000 <sup>a</sup>	2	.000*
PAYE - EMP201 (monthly)	1 (5.6)	5 (27.8)	12 (66.7)	10.333 <sup>a</sup>	2	.006
VAT - VAT 201 (when due)	1 (5.6)	1 (5.6)	16 (88.9)	25.000 <sup>a</sup>	2	.000*
EMP501 reconciliation	1 (5.6)	6 (33.3)	11 (61.1)	8.333 <sup>a</sup>	2	.016
Notes: X2 tests if a significant number selected any response option(s) over others. * p<.001 Df means the following: <sup>a</sup> 0 cells (0%) have expected frequencies less than 5. The minimum expected cell frequency is 6.0.						

Table 4.33 shows that most tax practitioners charge SMEs R8 000 or more per year for the various returns. When this finding is compared to what SMEs answered in Table 4.15 there is some agreement on the fees since SMEs stated they pay a minimum of R2 500 to a maximum of R12 500 for each tax return.

#### 4.4.2.4 The total amount SMEs pay for payroll services

As payroll services may be outsourced to tax practitioners, the tax practitioners were asked to state the amount SMEs paid for payroll services. These results are shown in Table 4.34.

Number	10
Mean	12748.7185
Std. deviation	2395.62614
Minimum amount in rands	10 350
Maximum amount in rands	18 000

Table 4.34 shows that tax practitioners charge a minimum of R10 350 and a maximum of R18 000 per year for payroll services, whereas SMEs indicated that they pay a minimum of R1 123 and a maximum of R25 000. This disparity may be because some tax practitioners charge per pay slip monthly, whereas others provide a full package of payroll services annually, which may include processing employee hours, directly depositing funds, and ensuring that employees are paid correctly on time, every time. Employee attendance and on-the-clock time are recorded and checked. Tax practitioners may also be handling all SARS and labour legislation compliance issues, ensuring accurate payroll taxes and deductions in respect of UIF. The results in Table 4.34 are possibly a reflection that the tax practitioners in this study charge for payroll services on an annual basis.

#### **4.4.2.5 Hours taken to calculate taxable income based on an annual turnover**

Table 4.35 shows the total number of hours spent preparing the ITR14. The questions were linked to the annual turnover of SMEs ranging from R1 to R6 million to determine the total hours spent.

If turnover is:	R1 - R300 000	R300 001 - R1m	R1m - R6m	>R6m
Number	18	18	18	18
Mean	2.44h	5.39h	13.19h	21.61h
Std. deviation	1.423	2.173	3.168	5.169
Minimum hours	1	1	2	2
Maximum hours	6	12	16	24

When investigating the time taken per turnover category, Table 4.35 shows that as the annual turnover of the business increases, so does the number of hours spent on income tax preparation. This could be because as turnover increases, so does the complexity of transactions, which leads to an increase in the time spent on income tax preparation.

Smulders *et al.* (2016) concluded that the number of hours required to perform income tax compliance activities increases with the size of the business (based on turnover), and the hours spent preparing income tax for smaller businesses with a turnover of between R1 million and R3

million and businesses with a turnover of R3 million or more would not be the same because businesses with a high turnover would have more complex transactions and do more tax planning Smulders *et al.* (2016).

#### 4.4.2.6 Hours taken to prepare PAYE returns annually

Table 4.36 shows the total hours spent when preparing PAYE returns by tax practitioners. To identify the total hours spent by the tax practitioners, a number of different turnover scenarios were used.

If turnover is:	R1 - R300 000	R300 001 - R1m	R1m - R6m	< R6m
Number	18	18	18	18
Mean	2.90h	5.62h	11.12h	17.34h
Std. deviation	1.860	2.572	3.144	4.960
Minimum hours	0	0	0	0
Maximum hours	6	12	16	24

Table 4.36 shows that the number of hours spent on PAYE (EMP201) preparation increases as the business's annual turnover increases (Smulders *et al.* 2016). This could be because as turnover increases, the business hires more employees, and as the number of employees increases, so does the number of hours spent on PAYE (EMP201) preparation (Smulders *et al.* 2016).

Smulders *et al.* (2016) found that the size of the business as measured by turnover is more important than the number of employees. The increased number of hours spent on PAYE could be due to the increased complexity of calculating PAYE for employees (such as offering fringe benefits) as the business's turnover increases (Smulders *et al.* 2016), because more senior employees would be required to operate a business with a higher turnover (Smulders *et al.* 2016).

#### 4.4.2.7 Hours taken to prepare the VAT returns

Table 4.37 shows the total number of annual hours per client spent when preparing VAT returns by the tax practitioners in relation to the SMEs' turnover.

If turnover is:	R1 - R300 000	R300 001 - R1m	R1m - R6m	< R6m
Number	18	18	18	18
Mean	1.18h	3.51h	12.51h	17.79h
Std. deviation	.493	1.442	3.329	4.906
Minimum hours	0	0	0	0
Maximum hours	2	5	15	22

Table 4.37 shows that the number of hours spent on VAT preparation increases as the business's annual turnover increases. This could be because as turnover increases, transactions become more complex. The findings of the study are consistent with those of Smulders *et al.* (2016) who concluded that the number of hours spent on VAT compliance increases with the size of the business (based on turnover). Another reason could be that as a company's size grows, so does the number of transactions, resulting in more VAT transactions and thus more time spent on compliance (Smulders *et al.* 2016).

#### **4.4.2.8 Hours taken to calculate EMP501 reconciliation (6 monthly) income based on an annual turnover**

Table 4.38 shows the total hours spent when preparing the EMP501 in relation to turnover.

If turnover is:	R1 - R300 000	R300 001 - R1m	R1m - R6m	< R6m
Number	18	18	18	18
Mean	1.00h	2.56h	8.47h	12.14h
Std. deviation	.000	.616	2.213	3.244
Minimum hours	1	1	2	2
Maximum hours	1	3	10	15

Table 4.38 shows that the number of hours spent on EMP501 preparation increases as the company's annual turnover increases.

#### **4.4.2.9 Summary of research question 6**

The study's findings show agreement with the SMEs that they outsource all types of tax services. This finding is consistent with what the SMEs stated in Table 4.14, that SMEs do use the services of tax practitioners in preparing PAYE, VAT, the ITR and provisional tax. This was expected because tax practitioners regard tax legislation as too complex for most taxpayers to understand;

SMEs must therefore hire accountants to manage their tax obligations, and SMEs with appropriately qualified tax personnel incur lower tax compliance costs (Matariano *et al.* 2019).

Tax practitioners charge SMEs between R5 000 to R10 000 for both pre-filing activities such as tax planning, obtaining tax guidance, information, and maintaining tax records, as well as filing activities such as data collection, preparation of the ITR from financial data, and calculation of the tax owed (including VAT201 and EMP201 returns). They also charge SMEs an annual fee of between R5 000 to R10 000 for post-filing activities such as preparing amended returns the audit process. The result of this current study further concludes that tax practitioners charge SMEs R8 000 or more annual for income tax, PAYE, VAT and R8 000 or more for EMP501 reconciliation.

According to the study's findings, tax practitioners spend a minimum of 1 hour and a maximum of 24 hours preparing a taxable income for a business with an annual turnover of between R1 to R6m, and a minimum of 6 hours and a maximum of 24 hours preparing a PAYE (EMP201) return for a business with an annual turnover of between R1 to R6m. They also spend a minimum of 2 hours and a maximum of 22 hours preparing a VAT201 for a business with an annual turnover of R1 to R6m and a minimum of 1 hour and a maximum of 15 hours preparing EMP501 reconciliation for a business with an annual turnover of R1 to R6m.

Finally, the study's findings show that the number of hours spent on income tax preparation, PAYE, VAT, and EMP201 increases as the business's annual turnover increases. The study's findings are consistent with previous research by Smulders *et al.* (2016), who discovered a significant positive relationship between turnover and tax compliance costs, implying that an increase in a company's turnover would increase tax compliance costs. Increased turnover is typically accompanied by an increase in transaction documents, which may be required to be presented to tax officials as proof should there be any queries from SARS (Smulders *et al.* 2016).

#### **4.4.3 Tax incentives and record keeping (Research question 7)**

This objective sought to ascertain whether tax practitioners advise SMEs to use tax incentives, and if so, which tax incentives do they advise them to use. It also considered whether the tax practitioner charges their clients for the calculation of tax incentives and how much they charge for the service. This section also determined whether the tax practitioner kept accounting records

for the client and how much they charged for the service. Also, does keeping accounting records reduce the tax compliance burden on SMEs?

These questions were aimed to answer research question 7 which was: do SMEs use tax incentives and record keeping to reduce the cost of being tax compliant? (This question corresponds to research question 4 which was aimed at SMEs.)

#### 4.4.3.1 Tax incentives

The tax practitioners were asked if they advise their clients to use tax incentives. The results are presented in Table 4.39. The responses are divided into two groups: Group 1 represents the YES category, and Group 2 represents the NO category.

<b>Table 4.39: Advice to SMEs to use tax incentives</b>						
		Category	N	Observed prop.	Test prop.	Asymp.Sig. (2-tailed)
Do you advise the client to use small business tax incentives?	Group 1	Yes	13	.87	.50	.007*
	Group 2	No	2	.13		
	Total		15	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. * p<.010						

According to Table 4.39, 13 of the 15 tax practitioners do advise SMEs to take advantage of tax incentives. Tax practitioners were expected to advise SMEs to take advantage of tax incentives because one of the reasons SMEs use tax services is to ensure they pay as little tax as possible, and thus they rely on the services of tax practitioners to reduce their tax liabilities using tax incentives.

#### 4.4.3.2 Types of tax incentives

The tax practitioners were then asked to list the various types of tax incentives which the tax practitioners advise their clients to take advantage of. These results are shown in Table 4.40.

<b>Table 4.40: The type of incentives advised to exercise</b>
Debt relief scheme
Current employment tax incentives tax relief tax
PAYE tax incentives relief period
Tax deferral for clients that are involved in the alcohol sector
Payment deferral incentive

This list of tax incentives shown in Table 4.40 given by the tax practitioners was more focused on the Covid-19 incentives. They did not include turnover tax which reduces and simplifies the tax compliance and administrative burden of SMEs and the fact that a small business that qualifies as small business corporation does not pay income tax on the first R79 000 taxable income.

#### 4.4.3.3 Tax practitioners' and clients' accounting records

Table 4.41 shows the responses as to whether the tax practitioners keep the clients' accounting records. The responses are divided into two groups: Group 1 represents the YES category, and Group 2 represents the NO category.

<b>Table 4.41: Tax practitioners' and clients' accounting records</b>						
		Category	N	Observed prop	Test prop	Asymp.Sig. (2-tailed)
Does the business keep accounting records on behalf of the client?	Group 1	Yes	15	.83	.50	.008*
	Group 2	No	3	.17		
	Total		18	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. *p<.010						

Fifteen of the 18 tax practitioners indicated that they do keep accounting records on behalf of the SME. SMEs also agreed (Table 4.24) that they kept their own accounting records. However, tax practitioners may also keep records on behalf of the SMEs. Keeping of accounting records is crucial as it helps the SME analyse its current financial position as well as its future profitability. Furthermore, it can help the business compare financial years as well as compare data with competitors in the industry.

#### 4.4.3.4 The costs incurred in record keeping

Table 4.42 shows the responses on whether tax practitioners charge small businesses for keeping accounting records. The responses are divided into two groups: Group 1 represents the NO category, and Group 2 represents the YES category.



**Table 4.42: Tax practitioners and their charge to small business to keep accounting records**

		Category	N	Observed prop.	Test prop.	Asymp.Sig. (2-tailed)
Does business charge the client for keeping the accounting record on the client's behalf?	Group 1	No	14	.93	.50	.001*
	Group 2	Yes	1	.07		
	Total		15	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. *p<.010						

Table 4.42 shows that 14 (out of 15) tax practitioners indicated that they do not charge SMEs for keep accounting records. This question may have been misinterpreted by the tax practitioners as they may have interpreted this question asking as to whether a charge is made for physically storing any accounting records rather than the recording of the SMEs' accounting transactions.

**4.4.3.5 Summary of research question 7**

The study's findings indicate that tax practitioners do advise SMEs to take advantage of tax incentives, which include but are not limited to debt relief schemes, current employment tax incentives, tax relief tax, PAYE tax incentives relief period, tax deferral for clients that are involved in the alcohol sector, and payment deferral incentives. Tax practitioners also keep accounting records on behalf of businesses and do not charge any fee for doing so. However, it is possible that this last finding results from a misinterpretation of the question.

**4.4.4 The benefits of being tax compliant (research question 8)**

This objective sought to determine tax practitioners' opinions on whether being tax compliant has any benefits for SMEs, and if so, what those benefits are. These questions were designed to provide an answer to research question 8, which asked what benefits tax practitioners perceive for SMEs in being tax compliant. (This research question corresponds to research question 5 which was aimed at SMEs.)

**4.4.4.1 The benefits of being tax compliant**

Table 4.43 shows the responses of respondents to the question asking whether being tax compliant has any benefits for small businesses. The questions are divided into two groups: NO and YES.

		Category	N	Observed prop	Test prop	Asymp.Sig. (2-tailed)
Would you agree that complying with tax obligations has some benefits for small business?	Group 1	Yes	15	.83	.50	.008*
	Group 2	No	3	.17		
	Total		18	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. *p<.010						

According to Table 4.43, 15 (out of 18) tax practitioners agree that complying with tax obligations has some benefits for small businesses.

#### 4.4.4.2 The benefits for being tax compliant

The tax practitioners were asked to indicate which benefits they perceived for SMEs in being tax compliant. A list of benefits was not provided in the questionnaire as the tax practitioners were required to come up with the benefits themselves. These results are shown in Table 4.44.

To get a tax clearance certificate that allows them to be able to apply for tenders
To apply for funding because most banks require businesses to be tax compliant in order to approve funding
Assists them in obtaining a tax compliance status that helps them to be able to utilise tax incentives especially those that were introduced in the COVID-19 pandemic
Helps them to apply for government support

Table 4.44 shows that there are various benefits that are obtained from being tax compliant such as obtaining a tax clearance certificate, which allows SMEs to apply for tenders and to apply for funding because most banks require a tax compliant business to approve funding. COVID relief tax incentives and applying for government support was also mentioned as benefits of being tax compliant. According to DTC (2014), the regulatory cost for small businesses is exorbitant, while the benefits of compliance are perceived as minor. Even though there may be differences from those mentioned by SMEs, this could be because SMEs were given a list of potential benefits and tax practitioners created their own; however, both SMEs and tax practitioners agree that being tax compliant has benefits for SMEs.

#### 4.4.4.3 Tax practitioners' viewpoints on tax

To conclude the questionnaire aimed at the tax practitioners, they were asked for their opinions on several tax statements. Table 4.45 shows the respondents' level of agreement or disagreement with these tax statements. The questions were divided into two categories, the first representing a Disagree category and the second representing an Agree category.

<b>Table 4.45: Tax practitioners' opinions on various tax statements</b>						
		Category	N	Observed prop.	Test prop.	Asymp.Sig. (2-tailed)
The tax rates for small businesses are high.	Group 1	Disagree	5	.33	.50	.302
	Group 2	Agree	10	.67		
	Total		15	1.00		
There is little education provided to small businesses about tax laws, reforms and tax administration.	Group 1	Disagree	1	.07		
	Group 2	Agree	14	.93	.50	.001*
	Total		15	1.00		
Tax compliance has a negative effect on the survival of small businesses	Group 1	Disagree	1	.07		
	Group 2	Agree	14	.93	.50	.001*
	Total		15	1.00		
It is very expensive to hire someone to prepare the tax returns for small businesses.	Group 1	Disagree	1	.07		
	Group 2	Agree	14	.93	.50	.001*
	Total		15	1.00		
Notes: Prop test (binomial test) tests if a significant proportion selected YES or NO. *p<.001						

Table 4.45 shows that most tax practitioners agreed that small business tax rates are high and that small businesses receive little education about tax laws, reforms, and tax administration. They also agreed that tax compliance costs have undesirable effect on the survival of SMEs and that hiring someone to prepare tax returns for small businesses is prohibitively expensive.

This finding echoes those SMEs in Table 4.8 where SMEs agreed that tax compliance costs influence the performance of their businesses, and they also agreed that tax compliance costs have a significant effect in the failure of SMEs. Table 4.12 also showed that they agreed that small business tax rates are high and that there is little education in South Africa about tax laws and tax administration. Matarirano *et al.* (2019) also stated that tax compliance costs have a significant effect on the performance of small businesses.

#### **4.4.4.4 Summary of research question 8**

According to this current study, tax practitioners agree that complying with tax obligations has some benefits for small businesses, including the ability to apply for funding because most banks require a tax compliant business to approve funding. It also allows an SME to apply for tenders, and other government funding such as that offered regarding COVID relief. Most practitioners agreed that small business tax rates are high and that there is little education provided to small businesses about tax laws, reforms and tax administration. Furthermore, the study revealed that hiring tax professionals is prohibitively expensive for small businesses.

### **4.5 Summary**

A summary of the findings discussed in this chapter is as follows:

#### **Objective 1: The effect of tax compliance costs in the functioning of SMEs**

The analysis revealed that tax practitioners and SMEs both agreed that tax compliance costs have a significant impact on the failure, performance, and growth of SMEs. They also agreed that high tax rates encourage noncompliance with tax laws, leading to SMEs concealing profits and a significant number of SMEs remaining in the informal sector.

#### **Objective 2: Tax knowledge of SMEs**

The analysis revealed that almost all SMEs have never received any tax training. As a result of which they do not know how to calculate, pay or submit their businesses' tax liability/returns. They also do they know how to file, nor do they know how long tax records must be kept. They pay PAYE, income tax, and VAT but are unsure how to file their tax returns.

#### **Objective 3: The costs associated with tax compliance**

The analysis reveals that both SMEs and tax practitioners agree that for SMEs to be tax compliant, they rely on tax practitioners, and the cost of outsourcing PAYE, VAT, the annual income tax return and provisional tax ranges between R2 500 and R10 000 per tax return, and annual external tax and accounting related services ranges between R5 000 and R20 000. The payroll services range in price from R1 123 to R25 000.

**Objective 4: Tax-efficient approaches SMEs can apply in order to minimise the tax compliance burden**

SMEs were unsure whether they qualify for tax incentives, and those who do qualify used them during the previous tax year. SMEs also stated that they maintained records in their businesses.

**Objective 5: Benefits of being tax compliant**

According to the findings, both SMEs and tax practitioners agreed that being tax compliant benefits SMEs. Low tax rates, electronic filing and payment of taxes, and government payments to tax practitioners to provide free services to SMEs in tax filing and record keeping are all very important in lowering tax compliance costs, as are frequent tax education, with practical and simplified tax laws.

A comparison of the findings are shown in Table 4.46.

<b>Table 4.46: Comparison of findings from SMEs and tax practitioners</b>		
<b>TAX PRACTITIONERS</b>	<b>SMEs</b>	<b>Remarks</b>
<b>Effect of tax compliance in the functioning of SMEs</b>		
<p>Table 4.45 shows that a most tax practitioners agreed that small business tax rates are high, little education about tax laws, reforms and administration.</p> <p>They also agreed that tax compliance costs have a undesirable influence on the survival of SMEs and that hiring someone to prepare tax returns for small businesses is prohibitively expensive.</p>	<p>Table 4.8 shows that many SMEs significantly agree that tax compliance costs has an effect on the performance and also in the failure of SMEs.</p>	<p>SMEs and tax practitioners agree that tax compliance costs has an effect on the performance of their businesses, and they also agree that small business tax rates are high, and there is little education about tax laws and tax administration in South Africa.</p>
<b>Outsourcing of tax services</b>		
<p>Table 4:31 shows that a significant number of tax practitioners indicated that all these types of tax services are outsourced to them by SMEs.</p>	<p>Table 4.14. Shows that most SMEs use tax practitioners to prepare their PAYE, VAT, annual (income tax), provisional tax returns.</p>	<p>The analysis reveals that both the SMEs and tax practitioners agree that for SMEs to be tax compliant, SMEs rely more on the service of tax practitioners.</p>

<b>Cost of outsourcing of tax services</b>		
Table 4.33 shows that most tax practitioners charge SMEs R8 000 or more per year for income tax, PAYE, VAT and the EMP501 reconciliation.	Table 4.15 shows that a significant number of SMEs pay between R2 500 to R12 500 for PAYE, VAT, and the annual income tax return.	When these findings are compared, there is some agreement on the prices since SMEs stated they pay a minimum of R2 500 to a maximum of R12 500 for each tax return.
<b>Cost of payroll services</b>		
Table 4.34 shows that the tax practitioners charge a minimum of R10 350 for payroll services and a maximum of R18 000 annually.	According to Table 4.18, the majority of SMEs indicated that they paid for payroll external services in the previous tax year and they pay a minimum of R1 123 to a maximum of R25 000	The disparity in findings could be attributed to the fact that some tax practitioners charge per pay slip monthly, whereas others provide the full package of payroll services annually. This indicates that the tax practitioners who took part in this study charge for payroll services on an annual basis.
<b>Accounting record keeping</b>		
Table 4.41 shows that a significant number of tax practitioners indicated that they do keep accounting records on behalf of the business.	In Table 4.24 SMEs indicated that they keep records in their businesses, and that the keeping of records is free	The analysis reveals both SMEs and tax practitioners agree that SMEs do keep records, with some tax practitioners indicating that they keep records on behalf of their clients.

<b>Benefits of tax compliance</b>		
Table 4.44: shows that a significant number of tax practitioners agreed that complying with tax obligations have some benefits for SMEs.	Table 4.27 shows that a significant number of SMEs established that being tax compliant has some benefit for their businesses.	The analysis reveals that both, the SMEs and tax practitioners agree that being tax compliant has some benefit for the SMEs.
<b>Tax incentives</b>		
According to Table 4.39, 13 of the 15 tax practitioners do advise SMEs to take advantage of tax incentives.	Table 4.23 indicates that SMEs did take advantage of the tax incentives in the previous fiscal year.	Tax practitioners agree that they do advise SMEs to take advantage of tax incentives and it is for this reason that SMEs stated that they did take advantage of tax incentives in the previous fiscal year.



## CHAPTER 5

### SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

#### 5.1 Introduction

The previous chapter provided and examined the findings obtained from the SMEs and tax practitioners who participated in this study. This chapter provides a summary of the study and concludes on how the research objectives were met. Recommendations are made based on the current study's findings. This chapter also looks at the study's contributions, limitations and makes recommendations for future research.

#### 5.2 Summary of the current study

According to Nyamwanza *et al.* (2016) and Herrington and Kew (2017), government rules and regulation are the greatest challenge to the development of SMEs. In Herrington and Kew's (2017) study, 60% of respondents identified these constraints as a major impediment to entrepreneurial activity. The costs associated with being tax compliant is a constraint on the performance of SMEs (Herrington and Kew 2016:49; Schwab 2016:324). Despite the significant contribution that SMEs make to the economy of the country, many SMEs fail during their first year of operation (South Africa Government 2016). Van Scheers (2018:167) states that despite the significant role played by SMEs in the economy their performance and sustainability of small has been poor. The factors cited for poor performance and, eventually, failure of small businesses is the tax burden (Herrington and Kew 2016:48). This study addressed the need to explore the effect of the tax burden in a particular setting, Durban Central Business District.

The purpose of the survey was to determine the impact of the tax compliance burden in the functioning of SMEs in the Durban Central Business District. Furthermore, it aimed at providing information to all small business owners, not just those in the Durban Central Business District, on how to reduce the burden of tax compliance.

To meet this objective, the following research questions were set which were aimed at SMEs:

Research question 1: What is the effect of tax compliance costs in the functioning of SMEs?

Research question 2: What is the level of tax knowledge of SMEs?

Research question 3: What costs are incurred by SMEs to be tax compliant?

Research question 4: Do SMEs use tax incentives and record keeping to reduce costs of being tax compliance?

Research question 5: What benefit do SMEs perceive on being tax compliant?

**The research questions aimed at tax practitioners to obtain their views on tax compliance costs were as follows:**

Research question 6: What costs are incurred by SMEs to be tax compliant?

Research question 7: Do SMEs use tax incentives and record keeping to reducing the costs of being tax compliant?

Research question 8: What benefits do tax practitioners perceive for SMEs to be tax compliant?

The literature review and empirical results presented in the previous chapter addressed the research objectives.

Chapter 1 identified the research problem, which was that the complexity of a tax system can be an impediment for small businesses seeking to comply with tax regulations. SMEs incur various tax compliance costs, with most costs incurred in the submitting and filing of taxes. Furthermore, high tax compliance costs hinder the progress and expansion of SMEs. Tax compliance costs are constraints in the functioning of small businesses, and it may result in many small businesses failing to survive. This led to a need to assess the tax compliance burden in the functioning of SMEs in Durban Central Business District

The literature review in Chapter 2 discussed the relevant aspects associated with tax compliance costs. This discussion was based on an examination of experiential and theoretical studies conducted on a national and international scale concerning the impact of tax compliance costs on the operation of SMEs.

The literature review confirmed that there is no consensus definition of SMEs, that definitions vary from country to country, and that SMEs are significantly important in a country's economy because

they create job opportunities for both skilled and unskilled labour. The literature review noted that tax regulation is one of the challenges that SMEs face, and that it has an effect in the effective functioning of SMEs.

The literature review further examined the difficulties that SMEs face in achieving tax compliance, the tax compliance costs borne by SMEs, the definition of tax compliance costs, the components of tax costs and tax compliance costs, as well as the reasons for high tax compliance costs.

Lastly, the literature review discussed both South African and international empirical research on tax compliance for SMEs.

Chapter 3 explained the reasoning behind the research method chosen to assess the tax compliance burden in the operation of SMEs in the Durban Central Business District. The target population consisted of 600 SMEs and 15 tax practitioners in the Durban Central Business District. This study was a census study because data was collected from every SME on the DCCI's (2016) data base. The data for tax practitioners was gathered from a targeted sample of 15 participants. The quantitative data was gathered using a questionnaire. This was chosen as a research instrument for this study because the responses are gathered in a standardised manner and the information is gathered relatively quickly.

Chapter 4 presented and discussed the findings of this study. The finding of this study was compared to prior experiential studies, which were discussed in Chapter 2. These findings are discussed in detail in the following section.

## **5.3 Results from the questions pertaining to SMEs**

### **5.3.1 Summary of the results pertaining to research question 1: the effect of tax compliance costs in the functioning of SMEs**

The study's findings confirm that the tax system influences tax compliance, on the failure and performance and it is also a barrier to small business development. The high tax rates encourage noncompliance with tax laws, causing SMEs to conceal profits and remain in the informal sector.

### **5.3.2 Summary of the results pertaining to research question 2: tax knowledge of SMEs**

The analysis reveals that most SMEs have never received any tax training and they do not know how to calculate, pay, and submit their businesses' tax liability/returns, how to file and complete their businesses' tax returns, or for how long tax records must be kept. The study further reveals that SMEs pay PAYE, income tax, and VAT but are unsure how to file their tax returns. Almost all SMEs in this study stated that they had never received any tax training. As a result, SMEs are forced to use tax practitioner services which are expensive and have a negative effect on the SMEs' growth and operation.

### **5.3.3 Summary of the results pertaining to research question 3: The costs associated with tax compliance**

The study reveals that SMEs rely on the services of tax practitioners to be tax compliant. Obtaining tax compliance assistance for tax returns such as PAYE, VAT, annual tax returns (income tax), and provisional tax costs SMEs between R2 500 and R10 000 per tax return annually.

The study further reveals that non-filing of returns, filing of returns after the due date, and incomplete or incorrect calculations are the reasons that lead to SMEs paying penalties, and if their business is subjected to penalties or interest, they pay between a minimum of R50 and a maximum of R11 980.

According to the study, SMEs outsource payroll services and pay a minimum of R1 123 to a maximum of R25 000 per year and the annual cost of outsourcing external tax and accounting related services, which include tax, accounting, and payroll services, ranges between R5 000 and R20 000 per year.

### **5.3.4 Summary of the results pertaining to research question 4: The tax efficient approach SMEs can apply in order to minimise the tax compliance burden**

The study reveals that low tax rates, electronic filing and payment of taxes, as well as government payments to tax practitioners to provide free tax filing and record keeping services to SMEs, are critical for lowering tax compliance costs. Frequent tax education, practicality, and simplification of tax laws are all critical in lowering tax compliance costs. SMEs agreed that tax officials' strong monitoring and enforcement of tax laws is unimportant in lowering tax compliance costs.

The study also reveals that many SMEs did not qualify for tax incentives and those who did qualify took advantage of the incentives during the previous tax year. SMEs also stated that they maintain records in their businesses, and they do not pay any fee in outsourcing the service of record keeping. The study also reveals that SMEs outsource the services of tax practitioners to perform their tax requirements, and that being tax compliant has some benefits for their businesses, such as improved record keeping, knowledge of the business's financial status, and knowledge of the business's profitability.

Furthermore, the study reveals that while SMEs pay PAYE, income tax, and VAT, they are unaware of how to register for these tax returns. As a result, they seek assistance in preparing the necessary documents to register for these tax returns, but they also claim that registering for these taxes is expensive.

The study also reveals that even if the owners/partners and directors are given a brief explanation of the tax laws, they will be unable to calculate the business's tax liability. This is because there is little education about tax laws and tax administration in South Africa, and the tax laws are complicated. Furthermore, SMEs agree that the SME tax rate is too high, and that it is expensive for small businesses to hire tax professionals.

## **5.4 Results pertaining to the questions posed to tax practitioners**

The following section presents and discusses tax practitioners' responses on the tax compliance burden in the functioning of SMEs within the Durban Central business District.

### **5.4.1 Summary of the results pertaining to research question 5: Costs incurred by SMEs to be tax compliant**

Tax practitioners indicated that SMEs outsource all types of tax services to them and that they charge SMEs between R5 000 and R10 000 for pre-filing, filing, and post-filing activities. They also charge SMEs R8 000 or more per year for the completion of the following: income tax, PAYE (EMP201), VAT and the EMP501 reconciliation.

According to this current study, tax practitioners spend a minimum of 1 hour to a maximum of 24 hours when preparing an income tax return (ITR14) for a business with an annual turnover of between R1 to R6m. Tax practitioners spend a maximum of 24 hours preparing (PAYE) EMP201

returns for a business that has annual turnover of between R1 to R6m and they also spend a maximum of 24 hours preparing VAT for businesses with an annual turnover of between R1 to R6m. They also devote a minimum of 1 hours and a maximum of 15 hours to prepare the EMP501 reconciliation for a business with an annual turnover of between R1 to R6m. Finally, the study's findings show that the number of hours spent on income tax preparation, PAYE, VAT, and EMP501 increases as the business's annual turnover increases.

#### **5.4.2 Summary of the results pertaining to research question 6: Do SMEs use tax incentives and record keeping to reducing the costs of being tax compliant?**

According to the findings of the study, tax practitioners do advise SMEs to take advantage of tax incentives such as debt relief schemes, current employment tax incentives, tax relief tax, PAYE tax incentives relief period, and they do keep accounting records on behalf of small businesses for no fee.

#### **5.4.3 Summary of the results pertaining to research question 7: What benefits do tax practitioners perceive for SMEs to be tax compliant?**

According to the study's findings, a sizable number of tax practitioners believe that small business tax rates are too high and that small businesses are not adequately educated about tax laws, reforms, and administration but, regardless of the above statements, they agree that small businesses benefit from complying with tax obligations in a variety of ways, including the ability to apply for funding, tenders and other opportunities.

### **5.5 Summary of combined findings**

According to analyses, SMEs rely on the services of tax practitioners and pay between R2 500 and R10 000 for these services. Non-filing of returns, filing of returns after the due date, and insufficient or incorrect calculations are the causes of SMEs paying penalties. SMEs also outsource their payroll requirements which costs them between R5 000 and R25 000 per year.

The analyses also revealed that tax compliance costs have a significant effect on SMEs' performance and can lead to the failure of the business; additionally, tax compliance requirements and high tax rates influence SME growth, causing SMEs to conceal profits received. Electronic tax filing and payment, frequent tax education as well as government payments to tax practitioners

to provide free tax filing and record keeping services to SMEs, all contribute to lowering tax compliance costs.

The fact that SMEs do not understand how to manage their tax matters and do not know how to register for tax returns such as PAYE, income tax returns, indicates that SARS should conduct more frequent tax education to assist SMEs in understanding their tax requirements. Even though tax compliance has a significant effect in the functioning of SMEs, SMEs believe that being tax compliant has some benefits for their businesses and that the country's tax system is equitable and fair.

The analysis revealed that tax practitioners agree that SMEs outsource all types of tax services. This was expected because even if SMEs owners are given a basic understanding of tax laws, they may not be able to complete their tax obligations. The analysis also revealed that there is a relationship between turnover and tax compliance costs. This is because as the annual turnover of the business increases, so do the hours spent preparing the tax return (Smulders *et al.* 2016)

Tax practitioners also agreed that small business tax rates are high, but to help SMEs reduce their tax compliance burden, they always advise SMEs to take advantage of tax incentives and keep accounting records on their behalf for free. They also agreed that small businesses are not adequately educated about tax laws, reforms, and administration, but they believe that complying with tax obligations has some advantages for small businesses.

It is evident from the discussion provided in this current study that tax compliance remains a significant factor in the effective functioning of SMEs.

## **5.6 Contribution of the study**

This study contributes to the existing literature in this field by highlighting the effect of tax compliance that appears to be a constraint on tax obedience and demonstrates the importance of other key tax compliance. This study adds to the evidence that tax compliance costs influences the functioning of SMEs and may lead to their failure.

This study noted that an increase in tax education, tax incentives, and initiatives in this domain could encourage taxpayers' compliance behaviour to improve. As a result, this finding may enlighten tax administrators as to additional methods for developing the most appropriate and

effective tax education programs to increase taxpayer knowledge and as such, it contributes to policy making.

Finally, this study has contributed new empirical evidence on the effect of tax compliance costs in the functioning of SMEs and is therefore of interest to other researchers, academics and policy makers.

## **5.7 Limitations**

This study has several limitations. Firstly, the sample population for this study was limited to 660 SMEs which were registered with the DCCI (2016) or were listed in the Yellow Pages Business Directory and 15 tax practitioners who only practice in the Durban Central Business District. If SMEs with similar characteristics were not registered with the DCCI or were not listed in the Yellow Pages Business Directory, they were excluded from this study. Due to the Protection of Personal Information Act, it was not possible to get a more up-to-date data base of SMEs from the DCCI. Therefore, the findings of this study cannot also be generalised beyond this sample of SMEs.

In addition, the contact details of 15 tax practitioner were obtained through personal contact. Due to the Protection of Personal Information Act, many tax practitioners were also reluctant to participate in the study. As a result, the selection approach for tax practitioners could not be scientific but it had to be through personal contact.

Secondly, the questionnaire contained questions on tax compliance. This is a sensitive area and finding suitable participants proved difficult as some SMEs were hesitant to participate in the research due to concerns about disclosing their tax status. This may also mean that some of the respondents were not truthful in their responses as they may have been unwilling to disclose their compliance status.

Third, all survey research relies on respondents giving honest replies to the questions. To some extent this was mitigated as respondents were assured that their responses were confidential and that their identities would not be revealed at all in the research process. The background information on both target groups indicates that the respondents were able to give knowledgeable opinions on and answers to the themes which were being probed in this current study.



Finally, the statistical analysis was simple, and no hypotheses were tested.

## **5.8 Recommendations for further research**

The following recommendations for further research are made.

- Research could be conducted with a larger sample size that includes all SMEs in Durban. This would benefit policymakers, particularly those concerned with the effect of tax compliance costs on SMEs in South Africa, as it would allow a richer analysis of the topic under study.
- Research could be conducted to assess the role of tax incentives in reducing the tax compliance burden in the operation of SMEs.
- A study could examine the quality of tax information provided by SARS to SMEs and its usefulness as perceived by SMEs and tax practitioners.
- A more sophisticated study with hypotheses testing could be carried out to test statistically the relationship between tax compliance and the functioning of SMEs.

## **5.9 Overview of the dissertation**

The aim of the survey was to assess the effect of the tax compliance burden in the functioning of SMEs in the Durban Central Business District. To accomplish this, a number of objectives were set, and a questionnaire was designed to be administered to two different target groups, SMEs and tax practitioners. Several relevant aspects were investigated, all of which were related to the effect of tax compliance on SMEs.

The analysis indicated that tax compliance was indeed a burden to SMEs with most of them choosing to outsource their tax matters to tax practitioners. This comes with a cost which may negatively affect the SMEs' functioning. This could be resolved through more tax training by SARS; however, tax matters are complicated, and it may also be better to use a tax practitioner in order to ensure that the SME is tax compliant.

## 5.10 Recommendations

Given that research has shown that the burden of tax compliance has a noteworthy consequence in the failure, performance, and growth of SMEs, we recommend that the South African government seriously consider the following:

- The tax laws can be simplified. For example, frequent tax education together with practical and simplified tax laws may reduce the tax compliance burden of SMEs.
- Increased tax incentives, as well as simplification of these incentives, can play a significant role in not only reducing the tax compliance burden of SMEs, but also improve their tax compliance.
- Government could pay tax practitioners to provide free tax filing and record keeping services to SMEs, and this could be critical in lowering tax compliance costs. Although this is normally outside the scope of SARS's responsibilities, SARS should consider providing SMEs with a dedicated tax practitioner in its first five years of operation. This may reduce the SMEs' business failure in the first five years of operations and the owners of SMEs will be able to dedicate their time and effort to running their businesses.

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# Appendixes

## APPENDIX A: RESEARCH INSTRUMENTS

### QUESTIONNAIRE FOR SMES

#### **The tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District**

Dear participant,

My name is Lungisani Lucky Buthelezi, Student Number 21959421. I am a Master of Accounting (Taxation) student at Durban University of Technology conducting a research study on “Tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District “. I am at data collection stage and I am requesting for your response to the questions I have listed below. Your response will be important in my study in terms of analyzing and drawing conclusions that will lead to further tax compliance knowledge and possible policy recommendations on tax compliance in South Africa. Furthermore, it will be of great help in achieving the objectives of my study. I will be thankful if you could take 30 minutes of your time to respond to the brief questionnaire/interview that I will carry out. The confidentiality of your responses is assured and your name will not appear anywhere in the completed study.

**Question 1. What is the main activity of the business? Please choose only one of the following:**

- Agriculture, forestry and fishing (includes farming)
- Wholesale trade
- Electricity, gas, water supply and waste services
- Manufacturing
- Retail Trade (includes shops)
- Construction (includes landscaping and repairs)
- Transport, postal and warehousing
- Accommodation and food services (includes cafes and restaurants)
- Finance, insurance services
- Rental, hiring and real estate services

- Professional, scientific and technical services (includes lawyers, accountants, engineers)
- Administrative and support services
- Public administration and safety
- Education and training
- Health care and social assistance

Other: please specify:

**Question 2: What is the legal structure of the business?**

Please choose only one of the following:

- Sole Proprietorship
- Partnership
- Trust
- Incorporated association
- Private company
- Un-incorporated association
- Other

**Question 3: For how many years has this business been trading?**

Please choose only one of the following:

- Less than a year
- 3-5 years
- 6-10 years
- More than 10 years

**Question 4: How many owners (partners/directors) does the business have?**

Please write your answer here:



**Question 5: Indicate the level of education of owners (partners/directors) who are responsible for the tax matters of the business?**

Please choose only one option:

No formal education	
Basic education	
Tertiary education	

**Question 6: What was the estimated annual turnover of the business for the last tax year?**

- 0 – R525 000
- R525 001- 1 000 000
- R1 000 001-R3 000 000
- R3 000 001–R7 000 000
- R7 000 001- R14 000 000
- More than R14 000 000
- Not sure

**Question 7: Which of the following categories does your business fall under?**

Please choose only one of the following:

- A small business corporation which pays income tax
- A non-profit organisation which is exempt from income tax
- A non-profit organisation which is not exempt from income tax
- Other please specify:

**These questions were as follows:**

**Question 8.1: Do tax compliance costs have any impact on the performance of your SME?**

Please choose only one of the following:

- Yes
- No

**Question 8.2: Do you think tax compliance costs have a significant effect in the failure of SMEs?**

Please choose only one of the following:

- Yes
- No

**Question 8.3: The following are some of the impacts of tax compliance costs in SMEs. Please indicate your level of agreement or disagreement, using a scale of 1 (strongly disagree) to 5 (strongly agree) with each of the following impacts by placing a tick in the appropriate box.**

<b>Impact of compliance costs</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
Affects the SMEs' performance					
Causes SMEs to hide profits received.					
SMEs may suffer business failure due to high compliance costs.					
The tax system and its compliance requirements are a stumbling block to the growth of small businesses.					
High tax rates promote non-compliance with tax laws.					
High tax rates are a reason most SMEs remain in the informal sector					
Tax compliance costs reduce business productivity.					
Tax compliance costs diminish business resources.					

**Question 9.1: Have you gone for any training regarding tax matters?**

Please choose only one of the following:

- Yes
- No

If yes, how many times.....

**Question 9.2: Please answer the following statements with either "YES" OR "NO".**

<b>I know:</b>	<b>YES</b>	<b>NO</b>
How to calculate my tax liability		
How long the tax records must be kept		
When to submit my tax returns		
When to pay tax due to SARS		
How to make payment to SARS		
How to complete my tax return		
How to file my returns		

**Question 9.3: Please read each statement carefully and then indicate the extent to which you agree or disagree, using a scale of 1 (strongly disagree) to 5 (strongly agree), with each of the following statements describing how you experienced the tax registration process of your business.**

<b>Statements on the tax registration process</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
The registration process for capital gains tax, value added tax, employee tax and income tax is too lengthy.					
I cannot begin operating my business without having completed my tax registrations.					
I do not understand the procedures I need to follow to register for capital gains tax, value added tax, employee tax and income tax.					
Preparing the necessary documentation for the registration for capital gains tax, value added tax, employee tax and income tax takes up too much time.					
I ask for help with preparing the necessary documents for the registration of capital gains tax, value added tax, employee tax and income tax.					
Submission of my tax registration is easy for me.					
Submitting all my tax registration forms for capital gains tax, value added tax, employee tax and income tax is quick.					
Registering my SME for capital gains tax, value added tax, employee tax and income tax cost me a lot of money.					
I do not know how to register my SME for capital gains tax, value added tax, employee tax and income tax.					

**Question 9.4: Using “Yes” or “No”, please indicate which of the following taxes your business pays.**

	<b>YES</b>	<b>NO</b>
PAYE		
VAT		
Capital Gains Tax (CGT)		
Income tax		

**Question 9.5: Please indicate who completes the following tax returns on behalf of the business.**

	N/A	Employee or owner	External tax professionals
PAYE			
VAT			
Capital Gains Tax (CGT)			
Income tax			
Please add any other returns			

**Question 9.6: If the tax returns are prepared by an external accounting firm, how much does it cost you to engage the external tax professionals on annual basis?**

Tax returns	Estimations				
	R2 500 - R5 000	R5 001 - R7 500	R7 501 – R10 000	R10 001- R12 500	Not sure
PAYE					
VAT					
Capital Gains Tax (CGT)					
Income tax					

**Question 9.7: If the tax returns are prepared internally by an employee or the owner, annually how much does it cost you to prepare the tax return internally?**

Internal owner/ employee	Estimations					
	R1 000- R2 500	R2 501 - R5 000	R5 001 - R7 500	R7 501 – R10 000	R10 001- R12 500	Not sure
PAYE						
VAT						
Capital Gains Tax (CGT)						
Income tax						

**Question 9.8: Have you ever paid penalties and interest for the following reasons?**

Tick appropriately:	Yes	No
Non filing of returns		
Filing returns after due date		
Incomplete or incorrect calculations		

**Question 9.9** if you answered “YES” for any of the reasons mentioned in the question above, can you please tell us how much was the penalty or interest?

.....

**Question 9.10:** This section will measure the level of tax compliance of small businesses. Please indicate by ticking a (√) in the appropriate box the extent to which you comply with the payment of taxes.

	1	2	3
Measures of tax compliance	Never	Sometimes	Always
Do you file your tax returns?			
Do you pay your tax liabilities?			
Do you observe due dates in filing and payment of taxes?			

**Question 10.1:** Did the business pay for any payroll external services in the last tax year?

Please choose only one of the following:

- Yes
- No

**Question 10.2:** How much did the business pay for these services?

Please note only answer this question if you answered YES to question 10.1.

Please write your answer here:

**Question 11.1:** What is the estimated annual cost of external tax and accounting related services paid by the business?

COST OF EXTERNAL SERVICE PROVIDERS	Estimations				
	R5 000 - R10 000	R10 001 – R15 000	R15 001 – R20 000	R20 000 - R25 000	R25 000 - R30 000
Tax costs					
Accounting costs					
Payroll costs					

**Question 11.2: Answer the following statements using “Agree” or “Disagree”.**

<b>Statements:</b>	<b>Agree</b>	<b>Disagree</b>
Our tax laws are simple to understand		
The owners/partners and directors of the business can compute the tax liability of the business, if given little explanation of the tax laws		
The tax rate for small businesses are high		
There is little education about tax laws and tax administration in South Africa		
There is no equity and fairness in our tax system		
It is very expensive for small businesses to hire tax practitioners to prepare their tax returns		
Other (please add and answer)		

**Question 12.1: Do you prepare your own VAT, PAYE, CGT and income tax returns?**

Please choose only one of the following:

- Yes
- No

**Question 12.2: If answered “YES” on question 12.1, how many hours does the business spend on each of the following tax related activities?**

- Please estimate the average time spent by your business on tax related activities during the last tax year. Include time spent by owners/partner/directors and paid full time employees.
- Leave blank spaces if you did not spend any time on a particular activity (do not type zero).

<b>Activities:</b>	<b>Value-added Tax (VAT)</b>	<b>Pay-As-You-Earn (PAYE)</b>	<b>Capital Gains Tax (CGT)</b>	<b>Income tax</b>
Recording information needed for tax				
Tax planning and tax advice				
Dealing with your tax practitioner, including providing all required information to them				
Dealing with SARS via (phone calls, e-filing, visits)				
Learning about tax laws and tax requirements				
Calculating tax requirements, completing them and paying them				
Other activities- please add any other activities				

**Question 12.3: Please estimate the percentage of the total time spent on different taxes by the following people during the last tax year and enter the percentages below. The totals should add up to 100%.**

	<b>Value-added Tax (VAT)</b>	<b>Pay-As-You-Earn (PAYE)</b>	<b>Capital Gains Tax (CGT)</b>	<b>Income tax (Tax return)</b>
Owners/partners and directors				
Employees (e.g., clerks, internal accountants)				

**Question 13: Please indicate which of the following factors can reduce the tax compliance costs for SMEs by rating the factors as either of low importance (1), important (2) or very important (3).**

	<b>1</b>	<b>2</b>	<b>3</b>
Low tax rates for SMEs			
Frequent tax education for SMEs			
Electronic filing and payment of taxes			
Tax practitioners to be paid by government to render free services to SMEs in tax filing and records keeping.			
Tax laws should be simplified and practical			
Tax laws should be practical			
Strong monitoring and enforcement of tax laws by tax officials			
Please add any other factors			

**Question 14.1: Under the South African tax system, small and medium-sized enterprises may qualify for a number of tax incentives or other simplifications measures which aim to reduce the tax compliance burden.**

**Was your business eligible for any of the small business tax incentives during the last tax year?**

Please choose only one of the following:

- Yes
- No
- Unsure/Do not know

**Question 14.2: Did your business use any of the small business tax incentives during the last tax year?**

**Only answer this question if you answered “YES” IN Question 14.1.**

- Yes
  
- No

**Question 14.3: If the business was eligible for any of the tax incentives during the last tax year and you decided not to use them, could you tell us the reason (s) why?**

**Please choose all that apply:**

- My accountant told me not to use the small business tax incentives
- My business would have paid more tax as a result of using the tax incentives
- The rules regarding the tax incentives are too complex
- Using the tax incentives would have increased my external accounting cost
- Using the tax incentives would have increased the internal time that my business spends on tax related activities
- Other please specify: .....

**Question 15.1: Which one of the following applies to your business?**

Please choose only one of the following:

- There is no record keeping in the business
- There is record keeping in the business

**Question 15.2: What type of accounting system does your business use?**

Please choose all that apply:

- No accounting system used
- Paper based/Manual
- All the work is done by external accountant
- Other computerised software; please elaborate.....



**Question 15.3: If your business does its own record keeping, do you incur any costs in keeping the records?**

Please choose only one of the following:

- Yes
- No

**Question 15.4: if your business outsources the record keeping, how much does your business pay an external body to keep the records?**

.....

**Question 15.5: Please rate the following statements regarding the benefits of tax compliance, using the scale of strongly disagree (1) to strongly agree (5).**

Statements on the benefits of compliance	Strongly disagree	Disagree	Neither agree nor disagree	Agree	Strongly agree
	1	2	3	4	5
Complying with the tax obligation helps to improve the record keeping of the business.					
Tax compliance helps improve the knowledge of the financial status of the business.					
To comply with tax obligation helps improve the knowledge of the profitability of the business.					
Other (please add)					

**Question 16.1: Overall, would you agree that complying with tax obligations has some benefits for your business?**

Please choose only one of the following:

- Yes
- No

**Question 17.2: If you had to put value to the benefit derived by your business from complying with tax obligations, can you please estimate the value of that benefit?**

Please write your answer here:

**Question 18: In the past 5 years what has your business done to cope with increasing tax compliance complexity, given your limited budget?**

Please tick all that apply:

- Hired more people to handle taxes
- Hired outside tax consultants
- Other please specify.....

**Question 19: Please to add any problems you have encountered in complying with the income tax system.**

If the space provided to answer this question is not enough, please to attach to a separate sheet. We would very much like to hear your views on the subject.

**Question 20: What, in your opinion, are three factors that would improve tax compliance of SMEs?**

- I. ....
- II. ....
- III. ....

## QUESTIONNAIRE FOR TAX PRACTITIONERS

### **The tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District**

Dear participant,

My name is Lungisani Lucky Buthelezi, Student Number 21959421. I am a Master of Accounting (Taxation) student at Durban University of Technology conducting a research study on “Tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District”. I am at the data collection stage and I am requesting for your responses to the questions I have listed below. Your truthful and considered responses will be important in my study in terms of analyzing and drawing conclusions that will lead to further tax compliance knowledge and possible policy recommendations on tax compliance in South Africa. Furthermore, it will be of great help in achieving the objectives of my study. I will be thankful if you could take 25 minutes of your time to respond to the questionnaire. The confidentiality of your responses is assured and your name will not be disclosed anywhere in the completed study.

#### **QUESTION 1: What is the legal structure of the business?**

Please choose only one of the following:

- Sole proprietorship
- Partnership
- Trust
- Public company
- Incorporated association
- Private company
- Un-incorporated association
- Other

**Question 2: How long has this business been trading?**

Please choose only one of the following:

- Less than a year
- 3-5 years
- 6-10 years
- More than 10 years

**Question 3.1: What kind of tax-related activities would an SME outsource from its business?**

**Please tick all those that apply.**

- Audit-related services
- Collection matters
- Preparing the tax return (ITR12)
- Preparing the provisional tax return
- Preparing amended returns
- Preparing the VAT return (VAT201)
- Preparing the PAYE, SDL and UIF return (EMP201)
- Record keeping services
- Tax Planning
- Other (please specify).....

**Question 3.2: Kindly please indicate an estimation of the annual fee charged by the firm for pre-filing, filing and post filing?**

TAX REQUIREMENTS	ESTIMATION				
	Less than R2 499	R2 500- R4 999	R5 000- R9 999	R10 000- R14 999	More than R15 000
Pre-filing activities, e.g., tax planning, obtaining tax guidance and information, and maintaining tax records					
Filing activities, e.g., includes the collection of data, preparation of the tax return from financial data and calculation of the tax owed (including VAT201 and EMP201 returns)					
Post-filing activities, e.g., preparing amended returns, the audit process etc.					

**Question 4: Using estimation how much does the business charge the client for the following tax requirements?**

TAX REQUIREMENTS	ESTIMATION				
	R2 000 or less	R2 001- R4 000	R4 001- R5 999	R6 000- R7 999	R8 000 or more
Calculation of taxable income (ITR)					
Pay-As-You-Earn (PAYE)- EMP201 (monthly)					
Value-added Tax (VAT)- VAT 201 (when due)					
Capital Gains Tax (CGT)					
EMP501 reconciliation (6 monthly)					

**Question 5.1: What is the estimated annual fee you charge the client for payroll services?**

.....

**Question 5.2: What is the estimated average time taken per annum to prepare, complete and submit tax returns?**

TAX REQUIREMENTS	AVERAGE TIME TAKEN (HOURS) if the TURNOVER of the SME is between:			
	R1 – R300 000	R300 001 - R1m	R1m - R6m	More than R6m
Calculation of a taxable income. ITR				
Pay-As-You-Earn (PAYE)- EMP201 (monthly)				
Value-added Tax (VAT)- VAT 201 (when due)				
Capital Gains Tax (CGT)				
EMP201 reconciliation (6 monthly)				

**Question 6.1: Do you sometimes advise the client not to use small business tax incentives?**

Please choose only one of the following:

- Yes
- No

**Question 6.2: If answered “YES” to question “6.1” which tax incentive did you advise your client not to use?**

.....

**Question 6.3: If the small business is eligible for certain tax incentives, do you charge extra fees for the calculation of those certain tax incentives?**

Please choose only one of the following:

- Yes
- No

**Question 6.4: If you answered “YES” to question “6.3”, please tell us how much you charge a client annually for the calculation of those certain tax incentives?**

.....

**Question 7.1: Does the business keep accounting records on behalf of the client?**

Please choose only one of the following:

- Yes
- No

**Question 7.2: If you answered “YES” to question 7.1, does business charge the client for keeping the accounting record on the client’s behalf?**

Please choose only one of the following:

- Yes
- No

**Question 7.3: If answered “YES” to question 7.2, how much does the business charge the client for keeping the accounting records on the client’s behalf?**

.....

**Question 8.1: Would you agree that complying with tax obligations has some benefits for a small business?**

Please choose only one of the following:

- Yes
- No

**Question 8.2: If you answered “YES” to question 8.1, please list at least four benefits that a small business can obtain from being tax compliant?**

.....

**Question 9: Please indicate whether you “Agree” or “Disagree” with the following statements.**

<b>Statements:</b>	<b>Agree</b>	<b>Disagree</b>
Our tax laws are simple to understand.		
The tax rates for small businesses are high.		
There is little education provided to small businesses about tax laws, reforms, and tax administration.		
Tax compliance has a negative effect on the survival of small businesses.		
It is very expensive to hire someone to prepare the tax returns for small businesses.		

**Question 10: What challenges do you think affects the tax compliance of SMEs?**

.....

**Question 11: In your opinion what do think the government needs to do to improve the tax compliance of SMEs?**

.....



## APPENDIX B: ETHICS APPROVAL



Student: Lungisani Lucky Buthelezi  
Student Number: 21959421  
Degree: Master of Accounting  
Email: [21959421@dut4life.ac.za](mailto:21959421@dut4life.ac.za)  
Supervisor: Prof. L Stainbank  
Supervisor email: [LesleyS@dut.ac.za](mailto:LesleyS@dut.ac.za)

**Dear Mr Buthelezi**

ETHICAL APPROVAL: LEVEL 2

I am pleased to inform you that the Faculty Research Ethics Committee (FREC) following feedback from two reviewers, has granted preliminary permission for you to conduct your research ‘Assessing the tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District’

**When ethics approval is granted:**

You are required to present the letter at your research site(s) for permission to gather data. Please also note that your research instruments must be accompanied by the letter of information and the letter of consent for each participant, as per your research proposal. This ethics clearance is valid from the date of provisional approval on this letter for one year. A student must apply for recertification 3 months before the date of this expiry.

Recertification is required every year until after corrections are made, after examination, and the thesis is submitted to the Faculty Registrar.

A summary of your key research findings must be submitted to the FRC on completion of your studies.

Yours sincerely

Dr Mogiveny Rajkoomar FREC Chair

Faculty of Accounting and Informatics Durban University of Technology Ritson Campus

Durban, South Africa, 4001.



# APPENDIX C: LETTER OF INFORMED CONSENT

## LETTER OF INFORMATION

**Title of the Research Study: The tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District**

**Principal Investigator/s/researcher:** Lungisani Lucky Buthelezi, National Diploma in Accounting and Bachelor of Technology in Cost and Management Accounting.

**Co-Investigator/s/supervisor/s:** Professor Lesley Stainbank and Mrs Mary Mutanda

**Brief Introduction and Purpose of the Study:** The aim of this study is to assess the tax compliance burden in the functioning of small businesses in the Durban Central Business District. It will provide valuable information to South African Revenue Services (SARS) on how it can assist small businesses in reducing tax compliance costs. It will also assist small business in understanding the factors that contributes to tax compliance. The study will advance the existing literature on tax compliance burden for small businesses.

Good Day

My name is Lungisani Lucky Buthelezi, Student Number 21959421. I am a Master of Accounting (Taxation) student at Durban University of Technology conducting research on “Tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District”.

I am at data collection stage and I would like to invite you to participate in the research.

**Research:** Research is a precise inquiry or enquiry for summed up new information

**Outline of the Procedures:** The research will use quantitative approach in which self-administered questionnaires will be used as a method of gathering data. The questionnaires will be distributed both electronically using Questionpro® and via email.

**Risks or Discomforts to the Participant:** There is no risk or discomfort to the participant.

**Explain to the participant the reasons he/she may be withdraw from the Study:** The

participant may be withdrawn from the study if he/she does not follow the study procedure or deliberately provides false information. The researcher may, under certain circumstances, decide to withdraw the participant from the study without penalty or loss of benefit. The participant may also withdraw from the study if he/she decides to exercise their right to do so.

**Benefits:** There are no benefits to the participant.

**Remuneration:** The participant will not receive any monetary or any type of remuneration.

**Costs of the Study:** The participant would not be expected to cover any costs of the study.

**Confidentiality:** The researcher will ensure confidentiality is maintained and no names will be used in the dissertation or in any subsequent research outputs. In addition, a letter of consent will be provided, promising confidentiality and anonymity. Participants will also be assured that the results of the study will only be used for the purposes of the dissertation and their names will not appear anywhere. Respondents' right to privacy and confidentiality will be respected at all times and they will be allowed to withdraw from the survey for any motive they may consider necessary.

**Results:** The result of this study will add to the body of knowledge in the area of academic discipline and researchers by using the findings of the research work as a basis for other studies and as a source of reference for further studies in the area of tax and compliance for small and medium-sized enterprises. Furthermore, findings of this study will be of relevance to the government, policy maker and body of academic.

**Research-related Injury:** There are no related injuries that may occur in this research since questionnaire will be distributed electronically.

**Storage of all electronic and hard copies including tape recordings:** Any materials relating to the research will be kept in a locked filing cabinet and will be destroyed after 5 years have passed.

**Persons to contact in the Event of Any Problems or Queries:** Please contact the researcher (073 740 5893) or my supervisor (Prof L Stainbank on 031 373 5836) or the Institutional Research Ethics Administrator on 031 373 2375. Complaints can be reported to the Director: Research and Postgraduate Support Dr Linda Liganiso on 031 373 2577 or [researchdirector@dut.ac.za](mailto:researchdirector@dut.ac.za).



**Full Title of the Study:** The tax compliance burden in the functioning of small and medium-sized enterprises in the Durban Central Business District

**Names of Researcher/s:** Mr L L Buthelezi

**Statement of Agreement to Participate in the Research Study:**

I hereby confirm that I have been informed by the researcher, .....(name of researcher), about the nature, conduct, benefits and risks of this study - Research Ethics Clearance Number:.....

- I have also received, read and understood the above written information (Participant Letter of Information) regarding the study.
- I am aware that the results of the study, including personal details regarding my sex, age, date of birth, initials and diagnosis will be anonymously processed into a study report.
- In view of the requirements of research, I agree that the data collected during this study can be processed in a computerised system by the researcher.
- I may, at any stage, without prejudice, withdraw my consent and participation in the study.
- I have had sufficient opportunity to ask questions and (of my own free will) declare myself prepared to participate in the study.
- I understand that significant new findings developed during the course of this research which may relate to my participation will be made available to me.

I, .....(name of researcher) herewith confirm that the above participant has been fully informed about the nature, conduct and risks of the above study.

.....	.....	.....
Full Name of Researcher	Date	Signature
.....	.....	.....
Full Name of Witness (If applicable)	Date	Signature
.....	.....	.....
Full Name of Legal Guardian (If applicable)	Date	Signature

**Please note the following:**

Research details must be provided in a clear, simple and culturally appropriate manner and prospective participants should be helped to arrive at an informed decision by use of appropriate language (grade 10 level- use Flesch Reading Ease Scores on Microsoft Word), selecting of a non-threatening environment for interaction and the availability of peer counselling (Department of Health, 2004).

If the potential participant is unable to read/illiterate, then a right thumb print is required and an impartial witness, who is literate and knows the participant e.g. parent, sibling, friend, pastor, etc. should verify in writing, duly signed that informed verbal consent was obtained (Department of Health, 2004).

If anyone makes a mistake completing this document e.g. a wrong date or spelling mistake, a new document has to be completed. The incomplete original document has to be kept in the participant's file and not thrown away, and copies thereof must be issued to the participant.

**References:**

Department of Health: 2004. Ethics in Health Research: Principles, Structures and Processes  
<http://www.doh.gov.za/docs/factsheets/guidelines/ethnics/>

Department of Health. 2006. South African Good Clinical Practice Guidelines. 2nd Ed. Available at: [http://www.nhrec.org.za/?page\\_id=14](http://www.nhrec.org.za/?page_id=14)