# THE EFFECTS OF TAX AUDIT ON REVENUE COLLECTION: CASE OF KENYA REVENUE AUTHORITY

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# DECLARATION

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To my dear wife,

Ruth Moraah

Your support was invaluable

And

My daughters

Kayla Bosibori,

Leslyn Kerubo and

Milkah Nyamoita

For the moral support

This is my challenge to you to excel beyond this

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# LIST OF ABBREVIATIONS

KRA Kenya Revenue Authority

ITA Income Tax Act

Y Total revenue

RTA Random Tax Audit

COTA Cut-off Tax Audit

CTA Conditional Tax Audit

# ABSTRACT

The study was on the effects of tax audit on revenue collection a case of the Kenya Revenue authority. The study is limited to the Nairobi West region of the Kenya Revenue Authority. This study adopted a descriptive approach. Data sources that were used were secondary data from Kenya Revenue Authority reports. Data was analyzed using T-test analytical model. From the t-statistics results the parametric Pearson correlation or 'r' value is significant for tax paid before audit and tax paid after audit as it clearly indicates there is an increase in the tax paid after audit, this is clear for random tax audit, cut-off tax audit and conditional tax audit. Also from the analysis of the taxes collected from a certain firm two years prior to the audit and two years after the audit, there is an increase in tax collected after the audit. Thus it is right to say that tax audit is directly related to revenue collection. Therefore it is clear that the more tax audits conducted the more revenue collected in the audit and in the subsequent years as the companies are better informed. The study recommends that the tax audit reports be submitted to the public and a standard procedure to be found in choosing the companies that random audit is conducted. A study should be conducted on the procedures followed during audit to see if all the Kenya Revenue employees follow the same procedures or a standard procedure is in place and adhered to.

# CHAPTER ONE

# INTRODUCTION

## 1.1.1 Tax Audit

Kircher (2008) stated that tax audit is the examination of an individual or organization's tax report by the relevant tax authorities in order to ascertain compliance with applicable tax laws and regulations of state. He further reported that tax audit is a process where the internal revenue service tries to confirm the numbers that you have put on your tax return. Ola (2001) stated that the process of tax audit involves tax returns that are selected for audit using some selection criteria. Thereafter, the underlying books and records of the taxpayers are examined critically to relate them to the tax return filed. Tax audit is important because it assist the government in collecting appropriate tax revenue necessary for budget, maintaining economic and financial order and stability, to ensure that satisfactory returns are submitted by the tax payers, to organize the degree of tax avoidance and tax evasion, to ensure strict compliance with tax laws by tax payers, to improve the degree of voluntary compliance by tax payers and to ensure that the amount due is collected and remitted to government.

## 1.1.2 Revenue Collection

In more formal usage, revenue is a calculation or estimation of periodic income based on a particular standard accounting practice or the rules established by a government or government agency. Two common accounting methods, cash basis accounting and accrual basis accounting, do not use the same process for measuring revenue. Corporations that offer shares for sale to the public are usually required by

law to report revenue based on generally accepted accounting principles or International Financial Reporting Standards.

Government revenue includes all amounts of money (i.e. taxes and/or fees) received from sources outside the government entity. Large governments usually have an agency or department responsible for collecting government revenue from companies and individuals. Government revenue may also include reserve bank currency which is printed. This is recorded as an advance to the retail bank together with a corresponding currency in circulation expense entry, that is, the income derived from the Official Cash rate payable by the retail banks for instruments such as 90 day bills. There is a question as to whether using generic business-based accounting standards can give a fair and acc0urate picture of government accounts, in that with a monetary policy statement to the reserve bank directing a positive inflation rate, the expense provision for the return of currency to the reserve bank is largely symbolic, such that to totally cancel the currency in circulation provision, all currency would have to be returned to the reserve bank and cancelled. (Bringham et al, 2008)

### 1.1.3 Effect of Tax Audit on Revenue Collection

Tax audit affects revenue collection in that it promotes voluntary compliance of taxpayers which increases revenue. It also determines the accuracy of returns so as to ensure the right taxes are submitted. With tax audit tax liability can be easily declared and matters that need adjustment are identified. It also helps in collecting tax interests and penalties which thereby increase revenue collection. Tax audit also helps to implement changes to eradicate evasion. Thus, tax audit is positively related to ta collection.

### 1.1.4 Kenya Revenue Authority

The Kenya Revenue Authority (officially abbreviated as K.R.A) was established by an Act of Parliament, Chapter 469 of the laws of Kenya, which became effective on 1st July 1995. The Authority is charged with the responsibility of collecting revenue on behalf of the Government of Kenya. It collects a number of taxes and duties, including: value added tax, income tax and customs. Since KRA's inception, revenue collection has increased dramatically, enabling the government to provide much needed services to its citizenry like free primary education and Health Services to all. Over 90% of annual national budget funding comes from local taxes collected by the KRA. The vision of KRA is to be the leading Revenue Authority in the world respected for professionalism, integrity and fairness to maximize tax revenue to ensure the government can sustain itself from internal revenue sources. Its mission Statement is to promote compliance with Kenya's tax, trade, and border legislation and regulation by promoting the standards set out in the Taxpayers Charter and responsible enforcement by highly motivated and professional staff thereby maximizing revenue collection at the least possible cost for the socio-economic well being of Kenyans. (The constitution of Kenya, 2010)

The role of KRA in the economy as Saleemi, (2007) continues to write is to administer and to enforce written laws or specified provisions of written laws pertaining to assessment, collection and accounting for all revenues in accordance with these laws. To advise on matters pertaining to the administration or and the collection of revenue under written laws. To enhance efficiency and effectiveness of tax administration by eliminating Bureaucracy, Procurement, Promotion, Training and Discipline. To eliminate tax evasion by simplifying and streamlining procedures and improving tax payer service and education thereby increasing the rate of

compliance. To promote professionalism and eradicate corruption amongst K.R.A. employee by paying adequate salaries that enables the institution to attract and retain competent professionals of integrity and sound ethical morals. To restore Economic Independence and Sovereign pride of Kenya by eventually eliminating the perennial budget deficits by creating organizational structures that maximize revenue collection. To ensure protection of local Industries and facilitate economic growth through effective administration of tax laws relating to trade. To ensure effective allocation of scarce resources in the economy by effectively enforcing tax policies thereby sending the desired incentives and shift signals throughout the country. To facilitate distribution of income in socially acceptable ways by effectively enforcing tax laws affecting income in various ways. To facilitate economic stability and moderate cyclic fluctuations in the economy by providing effective tax administration as an implementation instrument of the fiscal and stabilization policies. To be a 'watchdog' for the Government agencies ( such as Ministries of Health, Finance, etc ) by controlling exit and entry points to the country to ensure that prohibited and illegal goods do not pass through Kenyan borders.

## 1.2 Research Problem

Taxes are the main revenue for the government and thus the department or agent concerned should ensure they are collected the right way. They should start with taxpayer identification so as to register and educate. They are then assesses after which they are sensitized on how and when to submit taxes. Through the procedures put in place then revenue is collected. The system must be monitored to avoid evasion and wrong submissions. Once these are in place and the right tax policy is followed, then there is taxpayer mobility and there are other sources of revenue

other than tax, the revenue collected will increase. That is when there is no political interference and the season is right otherwise the revenue collected will decrease.

The study will be on the relationship between tax audit and revenue collection and thus, as revenue collected is determined by the tax audit then the study will seek to determine the relationship and find out the effects of tax audit on revenue collection.

The citizens do not understand the relationship between revenue collection and tax audit and therefore they see it as a waste of time and a bother to them. This study was intended to fill the gap by establishing the relationship between revenue collection and tax audit in Kenya Revenue Authority. The research questions guiding the study are:

1. What is the effect of tax audit on revenue collection in Kenya Revenue Authority?
2. How should tax audit be done so as to have impact on revenue in Kenya Revenue Authority?

## 1.3 Objective of the Study

The general objective of the study was to establish the effects of tax audit on revenue collection a case study of KRA.

## 1.4 Value of the Study

The study established the effects of tax audit on revenue collection in Kenya Revenue Authority. The outcome of the study will be useful such that it will emphasize the theories in place and will add to theories the relationship between the two and it will also be used when coming up with policies for companies or for the

government. The outcome will also help management to be able to come up with new policies to implement in revenue collection. The outcome of the study will be useful to citizens in Kenya by knowing the relationship of revenue collection and tax audit and thus, place relevance on the procedure. The KRA staff will be able to place importance on the procedures in order to incorporate measures in their planning to ensure and that they contributed towards improved services. The study will also be able to add value to academics as it will show the practicability of theories and give scholars a practical view of the theories. The data will also help scholars in their studies on the same topic.

# CHAPTER TWO

# LITERATURE REVIEW

## 2.1 Introduction

The chapter explains the theoretical contributions from various authors on tax audit and revenue collection. It also gives contribution of various research studies as carried out by various authors and then concludes on the general view of the various authors.

## 2.2 Specific Theories

Awe (2008) defines auditing as an independent examination of the books and accounts of an organization by a duly appointed person to enable that person give an opinion as to whether the accounts give a true and fair view and comply with relevant statutory guidelines. The American Accounting Association (1971) in its Statement of Basic Auditing Concepts in Hayes, Schilder, Daseen and Wallage (1999) described auditing as: a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between these assertions and established criteria and communicating the results to interested users. Akinbuli (2010), Hayes et al (1999) reported that several theories of auditing were made to specify and determine the audit functions. Some of these theories include:

### 2.2.1 The Policeman Theory

This theory of auditing was formulated by Awe, (2008) on assumptions that once monitoring is done on the systems at unspecified times then that is like policeman

guarding a place and thus, called it policeman theory. It was further asserted that auditing is purely on the arithmetical accuracy and on the prevention and detection of fraud. This theory makes the auditor to detect and prevent errors and fraud in organizations. It then adds a factor of monitoring to the auditing theory.

### 2.2.2 The Lending Credibility Theory

This theory of auditing regards the primary function of auditing to be the addition of credibility to the financial statements. Akinbuli (2010) who states that audited financial statements can enhance stakeholders' faith in management's stewardship assumed that for one to be sure that the financial statements are true and fair then an independent person has to go through the statement, substantiate them then produce a report. It was asserted that shareholders and stakeholders trust the report of the auditor and feel secure. The theory was modified from the initial by Hayes et al (1999) that stated that it was through financial statements that the revenue authorities are able to ascertain the amount to be collected. The factor of credibility was added to the theory of auditing.

### 2.2.3 Theory of Inspired Confidence

This theory states that stakeholders demand accountability from the management in return for their contribution to the organization as stated by Due, (2003). It was made on the assumptions that stakeholders want to know how their resources are utilized and that the managers are responsible and geared towards the same objectives as stakeholders. The theory asserted that it is through audited financial statements that the accountability can be substantiated. Then accountability is introduced in auditing.

### 2.2.4 The Moderator of Claimants Theory

This theory is stated by Frey, (2003) that it is important that all vital participants in an organization continue to contribute. In order to continue these contributions, it is important that each group believes it receives a fair share of the organizations income. This is based on the assumption that when one gets a fair share then a fair share will be contributed. To the auditing theory then fairness is introduced.

### 2.2.5 Agency Theory

This theory is associated with conflicting interests of shareholders and management of organizations, suggesting that the less informed party will have to demand for information that monitors the behaviour of better informed manager (Akinbuli, 2010). According to Hayes et al (1999), assumptions are made that agency theory can be used to explain the supply side of the audit market. The contribution of an audit to third parties is basically determined by the probability that the auditor will detect errors in the financial statements and the auditor's willingness to report these errors. Then independence is emphasised in auditing.

### 2.2.6 Classical Theory of Tax Compliance

This theory of tax compliance initially formulated by Toggler, (1970) is also called the A-S models based on the deterrence theory. In the theory the taxpayer is assumed to maximize the expected utilities of the tax evasion gamble, balancing the benefits of successful tax cheating against the risky prospect of being caught and punished by tax authorities (Sandmo, 2005). Alabede et al (2011) asserted that the deterrence theory depends largely on tax audit and penalty. They further stressed that this theory of tax compliance makes taxpayers to pay tax as a result of fear and sanctions. Trivedi and Shehata (2005) says that the deterrent theories suggest that taxpayers "play the audit lottery", that is they make calculations of the economic

consequences of different compliant alternative. Verboon and Dijke (2007) stated that the essence of the deterrence model of tax compliance is to chiefly examine the interaction between probability of detection and sanction severity that should affect non-compliance. Brook (2001) says that classical theory is only based on economic analysis but social and psychological variables are equally important in understanding the issue of noncompliance to tax. Some of the important studies about the effects of deterrence on compliance include Hasseldine (2000), Torgler (2002) and Kirchler (2007). Elffers (2000) and Braithwaith (2003) argued that if deterrence (that is the probability of detection and sanction severity) would be the most significant variable in explaining compliance, rational individuals in most societies of the world would be non-compliant because the levels of deterrence are low. The theory has contributed to theory the fact that revenue authorities should seek audited statements or perform audits to ascertain compliance.

### 2.2.7 Theory of Planned Behaviour

The theory of planned behaviour states that the behaviour of individuals within the society are under the influence of definite factors, originate from certain reasons and emerge in a planned way (Erten, 2002). It was assumed that the ability to perform a particular behaviour depends on the fact that the individual has a purpose towards that behaviour. Therefore, it was asserted that the factors that determine the purpose towards that behaviour are attitude towards behaviour, subjective norms and perceived behavioural control. Ajzen (2002) says that these factors are under the influence of behavioural beliefs, normative beliefs and control beliefs. It is also asserted that sociological and psychological factors have proved to be important in understanding the high levels of tax compliance. In such analyses, concepts such as

trust in authorities perceived fairness of the system moral considerations and norms are added to theory and are used to promote better understanding of tax compliance.

## 2.4 Empirical Studies

Niu (2010) in a study found a positive association between the audit and the voluntary compliance. The finding suggests that the audit productivity may be under estimated in many studies in the literature. It reminds us that when considering the productivity of the audit work. Besides the direct audit collections, we should also take the audit impact on the voluntary compliance into consideration. For this reason, the finding may provide tax professionals and tax authorities with incentives to strengthen the audit power and to better structure their audit organization to generate more revenue for the state. Niu (2010) Historical population data of a New York State economic sector were used in this study instead of experimental data or randomly selected sample data often used in the literature. The results of both Ordinary Least Squares (OLS) and Time Series Cross Section (TSCS) autoregressive modeling methods. The results of both methods suggest that after an audit, a firm would report a higher sales growth rate.

Jin Kwon (2004) study in Korea observed that a more rigorous analysis to evaluate the determinant of tax culture for the study of tax compliance and tax audit. There are three types of tax audit. Badara (2012) stated these three types of audit include the random tax audit, cut-off tax audit and conditional tax audit. The random tax audit scheme simply provides each self report of income an equal chance of being chosen for verification by an audit. Cut-off audit scheme, audit resources are employed to verify reports of the tax payers reporting the lowest income levels. The conditional audit scheme requires in addition to the reported income, sources of

information representing a noisy signal of tax payers' thorough income earning potentials.

Badara, (2012) Questionnaire distributed to forty-eight (48) respondents using descriptive statistics. The result shows that the Relevant Tax Authority (RTA) employed tax audit towards achieving target revenue, that tax audit reduce the problems of tax evasion, that tax payers do not usually cooperated with tax audit personnel during the exercise. There are several theoretical and empirical studies on tax audit and tax compliance. These studies provide mix reactions on the relationship between tax audit and tax compliance.

Alm and McKee, (2006) investigates the application of experimental methods to examine the individual compliance responses to a "certain" probability of audit, and conclude that the compliance rate rises if an individual knows he will be audited and the rate falls if he knows he will not be audited. Slemrod et al, (2001) examines randomly selected taxpayers and inform them that their filling will be "closely examined' and found evidence of taxpayers' behavior changes in response to an increased probability of audit, although the responses are not uniform among different groups of taxpayers.

Mittone (2006) investigates that early experience of audits in taxpayers' "tax life" is a more effective way to increase compliance than later audits. Also Kastlunger et al, (2009) study of experimental research also suggests that, although the effectiveness of audits and fines cannot be completely confirmed, early audits in taxpayers' "tax life" have a positive impact on compliance. Kleven et al (2010) 40,000 individual

tax filers using experimental design and randomization test and SKAT's Business object Database with ordinary least square. Their research found that tax evasion rate is small for income subject to third party reporting, but substantial for self reported income; marginal tax rates have a positive impact on tax evasion, but that this effect is small; prior audits substantially increase self reported income and threat of audit letters also have a significant effects on self reported income, and the size of this effect depends positively on audit probability expressed in the letter. Hyun (2005) Japan & Korea using world value survey dataset and descriptive statistics and multiple regression for analysis. Japan has the higher level of tax culture than that of Korea; and the legal system is relatively more important factor to determine the level of tax culture which eventually affects the level of compliance. Plumley et al (1996) Data set from 1991-2001 using Ordinary Least Square The result found a significant effects attributable to many tax policy and tax administration parameters; including: audits; third party information documents; the issuance of targeted non-filer notices; criminal tax convictions; marginal tax rates.

## 2.5 Conclusion

The role of KRA in the economy is to administer and to enforce written laws or specified provisions of written laws pertaining to assessment, collection and accounting for all revenues in accordance with these laws. To advise on matters pertaining to the administration or and the collection of revenue under written laws. To enhance efficiency and effectiveness of tax administration by eliminating Bureaucracy, Procurement, Promotion, Training and Discipline. To eliminate tax evasion by simplifying and streamlining procedures and improving tax payer service and education thereby increasing the rate of compliance.

Further reported that tax audit is a process where the internal revenue service tries to confirm the numbers that you have put on your tax return. The process of tax audit involves tax returns that are selected for audit using some selection criteria. Thereafter, the underlying books and records of the taxpayers are examined critically to relate them to the tax return filed. Tax audit is important because it assist the government in collecting appropriate tax revenue necessary for budget, maintaining economic and financial order and stability, to ensure that satisfactory returns are submitted by the tax payers, to organize the degree of tax avoidance and tax evasion, to ensure strict compliance with tax laws by tax payers, to improve the degree of voluntary compliance by tax payers and to ensure that the amount due is collected and remitted to government.

Government revenue includes all amounts of money (i.e. taxes and/or fees) received from sources outside the government entity. Large governments usually have an agency or department responsible for collecting government revenue from companies and individuals. Government revenue may also include reserve bank currency which is printed. This is recorded as an advance to the retail bank together with a corresponding currency in circulation expense entry, that is, the income derived from the Official Cash rate payable by the retail banks for instruments such as 90 day bills. There is a question as to whether using generic business-based accounting standards can give a fair and accurate picture of government accounts, in that with a monetary policy statement to the reserve bank directing a positive inflation rate, the expense provision for the return of currency to the reserve bank is largely symbolic, such that to totally cancel the currency in circulation provision, all currency would have to be returned to the reserve bank and cancelled.

# CHAPTER THREE

# RESEARCH METHODOLOGY

## 3.1 Introduction

This chapter explored the research methodology that was employed in the study. It outlined the research design, area of study, population of the study, sampling size and procedures, data sources, data collection instruments used, data analysis, data presentation and ethical considerations.

## 3.2 Research Design

A research design is a plan for collecting and utilizing data so that desired information can be obtained as defined by Paul et al (2009). This study adopted a descriptive approach. A descriptive approach is an approach that describes a situation qualitatively as per Trevor, (2010). The study described the relationship between revenue collection and tax audit in Kenya Revenue Authority. The study then adopted a survey research design which as per Kothari, (2009) is

## 3.3 Population of study

The study was carried out among the 58 taxpayers audited in 2010 located in Nairobi West area because reports from other areas are sent there for clarification and record keeping thus, considered it an area that was a good representative of the whole Kenya Revenue Authority.

## 3.4 Sample

The study used a sample of 58 taxpayers audited in 2010 located in Nairobi. In all the 58 ‘companies from different industries, the data has been classified in terms of

the reasons which the company was picked for audit, that is either random, cutoff or conditional.

## 3.5 Data collection instruments

The study used secondary data only which was collected from KRA audit report summaries and monthly and yearly reports. Based on the three criteria, 35 companies conducted random, 16 conducted cutoff and 7 conducted conditional audit.

## 3.6 Data analysis

Collected data was analyzed through descriptive statistics. Excel software helped transform the variables into format suitable for analysis, after which SPSS was used for data analysis. The significance of the findings were tested using the paired t-test regarding the treated and the control group. When two samples are involved and the values for each sample are collected from the same individuals (that is, each individual gives us two values, one for each of the two groups), or the samples come from matched pairs of individuals then a paired-samples t-test may be an appropriate statistic to use. The paired samples t-test can be used to determine if two means are different from each other when the two samples that the means are based on were taken from the matched individuals or the same individuals.

### 3.6.1 Student's t-test model for the comparison of two means

This test assumes: (a) A normal distribution for the populations of the random errors, (b) there is no significant difference between the standard deviations of both population samples.

The two means and the corresponding standard deviations are calculated by using the following equations ($n_A$ and $n_B$ are the number of measurements in data set A and data set B, respectively):

$$\overline{x}_A = \sum_{i=1}^{n_A} x_i \Big/ n_A \qquad \overline{x}_B = \sum_{i=1}^{n_B} x_i \Big/ n_B$$

$$s_A = \sqrt{\frac{\sum_{i=1}^{n_A} (\overline{x}_A - x_i)^2}{n_A - 1}} \qquad s_B = \sqrt{\frac{\sum_{i=1}^{n_A} (\overline{x}_B - x_i)^2}{n_B - 1}}$$

Then, the **pooled** estimate of standard deviation $\mathbf{s_{AB}}$ is calculated:

$$s_{AB} = \sqrt{\frac{(n_A - 1)\, s_A{}^2 + (n_B - 1)\, s_B{}^2}{n_A + n_B - 2}}$$

Finally, the statistic $\mathbf{t_{exp}}$ (experimental t value) is calculated:

$$t_{exp} = \frac{|\overline{x}_A - \overline{x}_B|}{s_{AB}\sqrt{\frac{1}{n_A} + \frac{1}{n_B}}}$$

$\mathbf{t_{exp}}$ value is compared with the **critical** (theoretical) $\mathbf{t_{th}}$ value corresponding to the given **degree of freedom** N and the confidence level chosen. If $\mathbf{t_{exp}}$>$\mathbf{t_{th}}$ then $H_0$ is rejected else $H_0$ is retained.

The sample means for the respective variables (random, cutoff and conditional) were formulated as follows;

$\overline{X_a}$ This represented mean before audit

$\overline{X_C}$ This represented mean during audit

$\overline{X_b}$ This represented mean after audit

### 3.6.2 Hypotheses

The following hypotheses were tested based on the variables;

i. There is no significant relationship between Tax paid before audit and Tax paid during the audit for random tax audit

ii. There is no significant relationship between Tax paid before audit and Tax paid after audit random tax audit

iii. There is no significant relationship between Tax paid during the audit and Tax paid after audit random tax audit

iv. There is no significant relationship between Tax paid before audit and Tax paid during the audit for cut off

v. There is no significant relationship between Tax paid before and Tax paid after audit for cut off

vi. There is significant relationship between tax paid during the audit and Tax paid after audit for cut off

vii. There is no significant relationship between Tax paid before audit and Tax paid during the audit for Conditional

viii. There is no significant relationship between Tax paid before audit and Tax paid after audit for Conditional

ix. There is significant relationship between tax paid during the audit and Tax paid after audit for Conditional

# CHAPTER FOUR

# DATA PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

## 4.0 Introduction

The chapter presents data collected from secondary sources to meet the objective of the study which is to establish the relationship between tax audit and revenue collection.

## 4.1 Random tax audit

Income tax audit is the examination of a business or individual tax return by the internal revenue service or state tax authority which in this case is Kenya Revenue Authority. The terms audit, review and notice are used to describe enforcement of tax codes and filing returns accurately. Random tax audit is when a certain amount of tax payers are chosen to be audited. No errors have to be found for the revenue authority to examine the tax return. Random tax has been criticized in the past that it is burdensome and intrusive.

**Table 4.1: Random tax audit report**

| S/No. | TAX PAID BEFORE AUDIT | | TAX PAID FROM THE AUDIT | TAX PAID AFTER AUDIT | |
|---|---|---|---|---|---|
| | 2008 | 2009 | | 2011 | 2012 |
| 1 | 1,250,939 | 1,489,153 | 1,131,232 | 2,802,576 | 3,669,338 |
| 2 | 26,159 | 31,826 | 924,347 | 3,046,478 | 3,583,353 |
| 3 | 7,018,683 | 10,255,074 | 9,651,434 | 12,039,835 | 12,563,558 |
| 4 | 223,619 | 2,825,147 | 1,303,815 | 4,364,734 | 5,295,095 |
| 5 | 800,000 | 777,431 | 115,376 | 1,214,962 | 1,140,635 |
| 6 | 1,507,956 | 1,237,383 | 300,505 | 1,279,570 | 1,213,712 |
| 7 | 800,000 | 1,931,381 | 1,533,753 | 2,245,745 | 2,368,253 |
| 8 | 620,381 | 613,761 | 4,356,230 | 3,672,439 | 8,217,154 |
| 9 | 915,665 | 1,476,019 | 6,843,460 | 5,649,639 | 4,970,174 |
| 10 | 3,434,892 | 2,565,745 | 654,908 | 4,181,459 | 4,986,602 |
| 11 | 853,839 | 970,432 | 1,021,087 | 1,319,053 | 1,908,190 |

| | | | | | |
|---|---|---|---|---|---|
| 12 | 1,100,267 | 2,293,425 | 74,460 | 3,395,885 | 3,077,492 |
| 13 | 1,827,732 | 1,940,260 | 1,188,898 | 3,128,236 | 3,494,116 |
| 14 | 1,058,322 | 1,335,749 | 5,212,549 | 4,373,911 | 4,764,921 |
| 15 | 1,163,547 | 1,010,747 | 2,242,698 | 1,476,859 | 1,821,426 |
| 16 | 1,103,572 | 1,690,682 | 5,891,080 | 1,704,350 | 5,560,045 |
| 17 | 372,387 | 919,285 | 1,092,740 | 1,551,721 | 1,650,874 |
| 18 | 2,056,780 | 2,589,386 | 295,219 | 3,233,513 | 3,268,966 |
| 19 | 211,825 | 1,689,601 | 447,385 | 3,071,487 | 3,039,336 |
| 20 | 1,145,698 | 1,444,514 | 1,047,572 | 2,270,568 | 2,343,236 |
| 21 | 1,237,464 | 1,243,036 | 1,751,600 | 2,066,970 | 4,205,232 |
| 22 | 412,851 | 642,162 | 671,321 | 1,034,954 | 2,703,634 |
| 23 | 1,221,507 | 1,040,452 | 724,866 | 2,033,652 | 2,165,356 |
| 24 | 434,696 | 485,877 | 324,300 | 979,737 | 1,458,708 |
| 25 | 4,323,803 | 5,193,321 | 674,030 | 6,239,013 | 6,748,812 |
| 26 | 2,483,364 | 3,690,881 | 932,200 | 4,456,000 | 6,813,062 |
| 27 | 1,746,776 | 1,458,999 | 4,564,472 | 1,191,947 | 1,872,867 |
| 28 | 3,019,639 | 2,424,179 | 9,135,781 | 4,366,154 | 5,126,435 |
| 29 | 187,811 | 896,175 | 1,145,712 | 2,577,422 | 2,985,000 |
| 30 | 1,112,591 | 1,046,386 | 244,999 | 2,144,581 | 2,429,139 |
| 31 | 933,422 | 337,069 | 517,426 | 1,100,083 | 1,182,253 |
| 32 | 649,753 | 1,211,424 | 1,018,250 | 1,221,821 | 1,525,346 |
| 33 | 2,077,146 | 2,560,090 | 591,952 | 3,863,451 | 3,817,387 |
| 34 | 1,128,404 | 1,289,966 | 867,428 | 2,425,310 | 2,141,496 |
| 35 | 3,538,780 | 3,732,771 | 550,744 | 4,107,402 | 4,351,360 |
| **Total** | **52,000,268** | **66,339,790** | **69,043,829** | **105,831,517** | **128,462,563** |

Source: KRA data (2012/2013)

When a tax audit is conducted there is revenue collected in the process as noted from table 4.1 an amount of Ksh. 69,043,829 was collected in the process. Some firms or individuals submit the taxes but either from ignorance or innocent error they submit the wrong amount of tax. After an audit the remaining figure has to be submitted within a stipulated time or else it will attract a penalty. When you compare the amount of tax collected from a certain company two years before the audit and two years after the audit as indicated from the above figure 4.0 its clear that after the audit more taxes are paid.

**Table 4.2: Descriptive statistics for Random tax audit report**

| | N | Minimum | Maximum | Mean | Std. Deviation |
|---|---|---|---|---|---|
| Tax paid before audit | 35 | 28992.35 | 8636878.50 | 1.6906E6 | 1.55694E6 |
| Tax paid from the audit | 35 | 74460.00 | 9651434.00 | 1.9727E6 | 2.51628E6 |
| Tax paid after audit | 35 | 1141168.00 | 12301696.48 | 3.3471E6 | 2.15219E6 |

From the findings, the lowest mean score according to Random tax audit report for the 35 audited companies tax paid before audit was 1.6 million, while that paid during audit was 1.9 million while 3.34 million was paid after the audit. In addition, the standard deviation depicts a slight variation in the tax paid before, during and after audit.

### 4.1.1: Random tax Audit analysis Model

Relationship between Tax paid before audit and Tax paid during the audit for random tax audit. The study tested the following hypothesis: There is no significant relationship between Tax paid before audit and Tax paid during the audit for random tax audit.

**Table 4.3: Paired Samples Statistics for Random tax Audit**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | Tax paid before audit | 1.6906E6 | 35 | 1.55694E6 | 2.63171E5 |
| | Tax paid from the audit | 1.9727E6 | 35 | 2.51628E6 | 4.25328E5 |

**Table 4.4: Paired Samples Correlations for Random tax Audit**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | Tax paid before audit & Tax paid from the audit | 35 | .431 | .010 |

The results indicate that the parametric Pearson correlation or ‘r’ value is significant

at 0.431 and the p-value (Sig) for the correlation coefficient is less than p < .05 and significant. (The above table is a working table to link to the next table).

**Table 4.5: Paired Samples Test for Random tax Audit**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid before audit - Tax paid from the audit | -2.82109E5 | 2.31979E6 | 3.92116E5 | -1.07898E6 | 5.14767E5 | -.719 | 34 | .477 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid before audit - Tax paid from the audit | -2.82109E5 | 2.31979E6 | 3.92116E5 | -1.35196E6 | 7.87739E5 | -.719 | 34 | .477 |

From the findings, the t calculated at 34 degrees of freedom both at 95% and 99% confidence interval of the difference = -.719. The critical t values are 2.03 and 2.733 at 95% and 99% confidence interval of the difference respectively. Since p=.477 (greater than 0.05 at 95% and greater than 0.01 at 99% level of confidence), we accept the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid from the audit for in random tax audit.

#### 4.1.1.1 Relationship between Tax paid before audit and Tax paid after audit random tax audit

The study tested the following hypothesis: There is no significant relationship between Tax paid before audit and Tax paid after audit random tax audit

**Table 4.6: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | Tax paid before audit | 1.6906E6 | 35 | 1.55694E6 | 2.63171E5 |
| | Tax paid after audit | 3.3471E6 | 35 | 2.15219E6 | 3.63786E5 |

**Table 4.7: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | Tax paid before audit & Tax paid after audit | 35 | .827 | .000 |

The results indicate that the parametric Pearson correlation or 'r' value is highly significant at 0. 827 and the p-value (Sig) for the correlation coefficient is less ($p < .05$) and significant. (The above table is a working table to link to the next table).

**Table 4.8: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid before audit - Tax paid after audit | -1.65649E6 | 1.23122E6 | 2.08115E5 | -2.07943E6 | -1.23355E6 | -7.959 | 34 | .000 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid before audit - Tax paid after audit | -1.65649E6 | 1.23122E6 | 2.08115E5 | -2.22430E6 | -1.08867E6 | -7.959 | 34 | .000 |

From the findings, the t calculated at 34 degrees of freedom both at 95% and 99% confidence interval of the difference = -7.959. The critical t values are 2.03 and 2.733 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05 at 95% and less than 0.01 at 99% level of confidence), we reject the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid after audit random tax audit.

#### 4.1.1.2 Relationship between Tax paid from the audit and Tax paid after audit random tax audit

The study tested the following hypothesis: There is no significant relationship between between Tax paid from the audit and Tax paid after audit random tax audit.

**Table 4.9: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | tax paid from the audit | 1.9727E6 | 35 | 2.51628E6 | 4.25328E5 |
| | Tax paid after audit | 3.3471E6 | 35 | 2.15219E6 | 3.63786E5 |

**Table 4.10: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | tax paid from the audit & Tax paid after audit | 35 | .609 | .000 |

The results indicate that the parametric Pearson correlation or 'r' value is highly significant at 0. 609 and the p-value (Sig) for the correlation coefficient is less ($p < .05$) and significant. (The above table is a working table to link to the next table).

**Table 4.11: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid from the audit - Tax paid after audit | -1.37438E6 | 2.08967E6 | 3.53219E5 | -2.09220E6 | -6.56550E5 | -3.891 | 34 | .000 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid from the audit - Tax paid after audit | -1.37438E6 | 2.08967E6 | 3.53219E5 | -2.33810E6 | -4.10657E5 | -3.891 | 34 | .000 |

From the findings, t calculated at 34 degrees of freedom both at 95% and 99% confidence interval of the difference = -3.891. The critical t values are 2.03 and 2.733 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05 at 95% and less than 0.01 at 99% level of confidence), we reject the null hypothesis that there is no significant relationship between between Tax paid from the audit and Tax paid after audit random tax audit.

### 4.2 Cut-off tax audit

Cut-off tax is conducted on the back-up systems and monitoring systems of a firm to ensure the correct information is submitted to the tax authority. It is usually conducted on firms that have skipped a financial period without submitting tax. The audit is actually done to ensure all the transactions are posted in the right financial period. Any operating firm is audited in the event that it used to submit large amount of tax and it does not submit or according to the revenue collection department it seems unrealistic in a certain period (Casanagra and Bird, 2012).

**Table 4.12: Cut-tax audit report**

| S/No. | TAX PAID BEFORE AUDIT | | TAX PAID FROM THE AUDIT | TAX PAID AFTER AUDIT | |
|---|---|---|---|---|---|
| | 2008 | 2009 | | 2011 | 2012 |
| 1 | 197,056 | 2,796,617 | 2,100,020 | 3,176,247 | 3,648,505 |
| 2 | 950,763 | 2,394,338 | 390,915 | 3,872,223 | 5,127,393 |
| 3 | 163,864 | 1,068,800 | 456,790 | 2,623,274 | 2,394,028 |
| 4 | 697,469 | 1,613,400 | 269,850 | 2,706,481 | 3,107,380 |
| 5 | 158,181 | 2,265,480 | 269,850 | 2,730,567 | 2,658,931 |
| 6 | 137,057 | 422,637 | 789,650 | 1,845,060 | 2,236,062 |
| 7 | 1,007,103 | 1,361,600 | 1,280,170 | 1,298,005 | 1,433,362 |
| 8 | 2,802,617 | 2,317,216 | 4,321,670 | 3,847,315 | 3,266,113 |
| 9 | 1,072,372 | 1,179,685 | 277,579 | 2,314,322 | 2,372,331 |
| 10 | 1,864,631 | 2,265,786 | 6,794,457 | 2,598,287 | 2,854,731 |
| 11 | 1,621,949 | 1,535,980 | 1,360,079 | 3,065,306 | 3,465,606 |
| 12 | 899,565 | 1,276,587 | 961,959 | 1,702,995 | 3,905,041 |
| 13 | 1,232,112 | 1,559,958 | 2,603,200 | 7,461,633 | 7,277,737 |

| | | | | | |
|---|---|---|---|---|---|
| 14 | 349,546 | 295,550 | 2,316,872 | 5,001,916 | 4,323,307 |
| 15 | 1,550,448 | 1,340,275 | 633,966 | 1,949,488 | 1,702,372 |
| 16 | 997,044 | 926,956 | 2,344,948 | 3,064,980 | 3,365,068 |
| **TOTAL** | **15,701,776** | **24,620,864** | **27,171,975** | **49,258,100** | **53,137,966** |

Source: KRA data (2012/2013)

Some firms have been noted to get to adjust their accounts to match the amount of tax they want to submit while in their back-up of their reports they have the right accounts for the benefit of the company. In the event of a cut-off tax audit revenue is collected as from table 4.12 there was a total of Ksh. 27,171,975 was collected. In the comparison of the two years before audit and two years after audit it is clear from the above table 4.12 that more taxes are paid after the audit.

**Table 4.13: Descriptive statistics for Cut-tax audit report**

| | N | Minimum | Maximum | Mean | Std. Deviation |
|---|---|---|---|---|---|
| Tax paid before audit | 16 | 279846.88 | 2559916.48 | 1.2601E6 | 5.84702E5 |
| Tax paid from the audit | 16 | 269850.00 | 6794457.00 | 1.6982E6 | 1.76586E6 |
| Tax paid after audit | 16 | 1365683.53 | 7369684.88 | 3.1999E6 | 1.41240E6 |

From the findings, the lowest mean score according to cut-off tax audit report for the 16 audited companies tax paid before audit was 1.2 million, while that paid during audit was 1.69 million while 3.19 million was paid after the audit. However, the standard deviation depicts high variation in the tax paid before and after audit.

## 4.2.1: Cut – off Tax Analysis Model

### 4.2.1.1: Relationship between Tax paid before audit and Tax paid from the audit for cut off

The study tested the following hypothesis: There is no significant relationship between Tax paid before audit and Tax paid from the audit for cut off.

**Table 4.14: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | Tax paid before audit | 1.2601E6 | 16 | 5.84702E5 | 1.46176E5 |
| | Tax paid from the audit | 1.6982E6 | 16 | 1.76586E6 | 4.41464E5 |

**Table 4.15: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | Tax paid before audit & Tax paid from the audit | 16 | .541 | .031 |

From the findings, the parametric Pearson correlation or 'r' value is significant at 0. 541 and the p-value (Sig) for the correlation coefficient is less ($p < .05$) and significant. (The above table is a working table to link to the next table).

**Table 4.16: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid before audit - Tax paid from the audit | -4.38166E5 | 1.53100E6 | 3.82750E5 | -1.25398E6 | 3.77647E5 | -1.145 | 15 | .270 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid before audit - Tax paid from the audit | -4.38166E5 | 1.53100E6 | 3.82750E5 | -1.56602E6 | 6.89689E5 | -1.145 | 15 | .270 |

From the findings, the t calculated at 15 degrees of freedom both at 95% and 99% confidence interval of the difference = -1.145. The critical t values are 2.13 and 2.94 at 95% and 99% confidence interval of the difference respectively. Since p=.270 (greater than 0.05 at 95% and greater than 0.01 at 99% level of confidence),

we accept the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid from the audit for cut off.

#### 4.2.1.2: Relationship between Tax paid before and Tax paid after audit for cut off

The study tested the following hypothesis: There is no significant relationship between Tax paid before and Tax paid after audit for cut off.

**Table 4.17: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | Tax paid before audit | 1.2601E6 | 16 | 5.84702E5 | 1.46176E5 |
| | Tax paid after audit | 3.1999E6 | 16 | 1.41240E6 | 3.53099E5 |

**Table 4.18: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | Tax paid before audit & Tax paid after audit | 16 | .128 | .637 |

From the findings, the parametric Pearson correlation or 'r' value is not significant at 0.128 and the p-value (Sig) for the correlation coefficient is high ($p > .05$) and insignificant. (The above table is a working table to link to the next table).

**Table 4.19: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid before audit - Tax paid after audit | -1.93979E6 | 1.45789E6 | 3.64472E5 | -2.71665E6 | -1.16294E6 | -5.322 | 15 | .000 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid before audit - Tax paid after audit | -1.93979E6 | 1.45789E6 | 3.64472E5 | -3.01379E6 | -8.65801E5 | -5.322 | 15 | .000 |

From the results, the t calculated at 15 degrees of freedom both at 95% and 99% confidence interval of the difference = -5.322. The critical t values are 2.13 and 2.94 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05 at 95% and less than 0.01 at 99% level of confidence), we reject the null hypothesis that there is no significant relationship between Tax paid before and Tax paid after audit for cut off.

#### 4.2.1.3: Relationship between tax paid from the audit and Tax paid after audit for cut off

The study tested the following hypothesis: There is no significant relationship between relationship between tax paid from the audit and Tax paid after audit for cut off.

**Table 4.20: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | tax paid from the audit | 1.6982E6 | 16 | 1.76586E6 | 4.41464E5 |
| | Tax paid after audit | 3.1999E6 | 16 | 1.41240E6 | 3.53099E5 |

**Table 4.21: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | tax paid from the audit & Tax paid after audit | 16 | .224 | .405 |

From the findings, the parametric Pearson correlation or ‘r’ value is not significant at 0.224 and the p-value (Sig) for the correlation coefficient is high (p > .05) and insignificant. (The above table is a working table to link to the next table).

**Table 4.22: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | tax paid from the audit - Tax paid after audit | -1.50163E6 | 1.99946E6 | 4.99865E5 | -2.56707E6 | -4.36192E5 | -3.004 | 15 | .009 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | tax paid from the audit - Tax paid after audit | -1.50163E6 | 1.99946E6 | 4.99865E5 | -2.97459E6 | -28669.89105 | -3.004 | 15 | .009 |

From the findings, the t calculated at 15 degrees of freedom both at 95% and 99% confidence interval of the difference = -3.004. The critical t values are 2.13 and 2.94 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05 at 95% and less than 0.01 at 99% level of confidence), we reject the null hypothesis that there is no significant relationship between relationship between tax paid from the audit and Tax paid after audit for cut off.

### 4.3 Conditional Tax Audit

Conditional tax is conducted on request of a firm when according to the management they do not feel the other audits of previous periods have been true and fair. In the event they request for a different auditor other than the one that has usually been auditing their accounts and request that tax officer witness the audit to ensure the correct tax has always been submitted. The audit is rarely done. (Musgrave, 2010)

**Table 4.23: Conditional tax audit report**

| S/No. | TAX PAID BEFORE AUDIT | | TAX PAID FROM THE AUDIT | TAX PAID AFTER AUDIT | |
|---|---|---|---|---|---|
| | 2008 | 2009 | | 2011 | 2012 |
| 1 | 538,835 | 679,612 | 324,224 | 2,273,830 | 5,515,095 |
| 2 | 2,127,329 | 1,613,400 | 279,584 | 3,833,002 | 3,642,014 |
| 3 | 950,000 | 1,641,646 | 452,500 | 2,483,165 | 2,328,450 |
| 4 | 515,844 | 917,647 | 104,557 | 3,432,629 | 4,019,730 |
| 5 | 280,492 | 1,071,209 | 960,544 | 2,933,052 | 10,008,011 |
| 6 | 1,203,688 | 1,188,684 | 1,439,615 | 5,597,258 | 5,763,403 |
| 7 | 2,436,245 | 2,339,117 | 1,517,290 | 3,823,500 | 4,234,432 |
| | **8,052,433** | **9,451,315** | **5,078,314** | **24,376,436** | **35,511,135** |

Source: KRA data (2012/13)

The auditors who do auditing for the firms are doubted but at times they do the right auditing and give correct amounts of tax, although the fact that there are others who miscalculate is not overlooked. As seen from figure 4.2 there was Ksh. 5,078,314 tax collected from the conditional audit conducted. From the analysis of two years prior to the audit and two years after the audit there is an improvement in the taxes collected.

**Table 4.24: Descriptive statistics for Conditional tax audit report**

| | N | Minimum | Maximum | Mean | Std. Deviation |
|---|---|---|---|---|---|
| Tax paid before audit | 7 | 609223.15 | 2387681.00 | 1.2503E6 | 6.71909E5 |
| Tax paid from the audit | 7 | 104557.00 | 1517290.00 | 725473.4286 | 5.79094E5 |
| Tax paid after audit | 7 | 2405807.50 | 6470531.50 | 4.2777E6 | 1.35920E6 |

From the findings, the lowest mean score according to conditional tax audit report for the 7 audited companies during audit was 0.72 million, while that paid before audit was 1.25 million while 4.27 million was paid after the audit. In addition, the standard deviation depicts high variation in the tax paid before and after audit and a low variation in tax paid before and during the audit.

## 4.3.1: Conditional Tax Audit Analysis Model

### 4.3.1.1: Relationship between Tax paid before audit and Tax paid from the audit for Conditional

The study tested the following hypothesis: There is no significant relationship between Tax paid before audit and Tax paid from the audit for Conditional.

**Table 4.25: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | Tax paid before audit | 1.2503E6 | 7 | 6.71909E5 | 2.53958E5 |
| | Tax paid from the audit | 725473.4286 | 7 | 5.79094E5 | 2.18877E5 |

**Table 4.26: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | Tax paid before audit & Tax paid from the audit | 7 | .440 | .324 |

From the findings, the parametric Pearson correlation or 'r' value is not significant at 0.44 and the p-value (Sig) for the correlation coefficient is high ($p > .05$) and insignificant. (The above table is a working table to link to the next table).

**Table 4.27: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid before audit - Tax paid from the audit | 5.24794E5 | 6.66808E5 | 2.52030E5 | -91900.59349 | 1.14149E6 | 2.082 | 6 | .082 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid before audit - Tax paid from the audit | 5.24794E5 | 6.66808E5 | 2.52030E5 | -4.09588E5 | 1.45918E6 | 2.082 | 6 | .082 |

From the findings, the t calculated at 6 degrees of freedom both at 95% and 99% confidence interval of the difference = 2.082. The critical t values are 2.44 and 3.70 at 95% and 99% confidence interval of the difference respectively. Since p=0.082 (greater than 0.05 at 95% and greater than 0.01 at 99% level of confidence), we accept the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid from the audit for Conditional.

#### 4.3.1.2: Relationship between Tax paid before audit and Tax paid after audit for Conditional

The study tested the following hypothesis: There is no significant relationship between Tax paid before audit and Tax paid after audit for Conditional.

**Table 4.28 : Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | Tax paid before audit | 1.2503E6 | 7 | 6.71909E5 | 2.53958E5 |
| | Tax paid after audit | 4.2777E6 | 7 | 1.35920E6 | 5.13730E5 |

**Table 4.29: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | Tax paid before audit & Tax paid after audit | 7 | -.274 | .553 |

From the findings, the parametric Pearson correlation or ‘r’ value is not significant at 0.44 and the p-value (Sig) for the correlation coefficient is high (p > .05) and insignificant. (The above table is a working table to link to the next table).

**Table 4.30: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | Tax paid before audit - Tax paid after audit | -3.02742E6 | 1.67286E6 | 6.32281E5 | -4.57455E6 | -1.48028E6 | -4.788 | 6 | .003 |
| | | | | | | | | | |
| | Tax paid before audit - Tax paid after audit | -3.02742E6 | 1.67286E6 | 6.32281E5 | -5.37155E6 | -6.83279E5 | -4.788 | 6 | .003 |

From the findings, the t calculated at 6 degrees of freedom both at 95% and 99% confidence interval of the difference = -4.788. The critical t values are 2.44 and 3.70 at 95% and 99% confidence interval of the difference respectively. Since p=.003 (less than 0.05 at 95% and less than 0.01 at 99% level of confidence), we reject the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid after audit for Conditional.

### 4.3.1.3: Relationship between tax paid from the audit and Tax paid after audit for Conditional

There is no significant relationship between tax paid from the audit and Tax paid after audit for Conditional.

**Table 4.31: Paired Samples Statistics**

| | | Mean | N | Std. Deviation | Std. Error Mean |
|---|---|---|---|---|---|
| Pair 1 | tax paid from the audit | 725473.4286 | 7 | 5.79094E5 | 2.18877E5 |
| | Tax paid after audit | 4.2777E6 | 7 | 1.35920E6 | 5.13730E5 |

**Table 4.32: Paired Samples Correlations**

| | | N | Correlation | Sig. |
|---|---|---|---|---|
| Pair 1 | tax paid from the audit & Tax paid after audit | 7 | .544 | .207 |

From the findings, the parametric Pearson correlation or 'r' value is not significant at 0.544 and the p-value (Sig) for the correlation coefficient is high (p > .05) and insignificant. (The above table is a working table to link to the next table).

**Table 4.33: Paired Samples Test**

| | | Paired Differences | | | | | t | df | Sig. (2-tailed) |
|---|---|---|---|---|---|---|---|---|---|
| | | Mean | Std. Deviation | Std. Error Mean | 95% Confidence Interval of the Difference | | | | |
| | | | | | Lower | Upper | | | |
| Pair 1 | tax paid from the audit - Tax paid after audit | -3.55221E6 | 1.15182E6 | 4.35348E5 | -4.61747E6 | -2.48695E6 | -8.159 | 6 | .000 |
| | | | | | 99% Confidence Interval of the Difference | | | | |
| | Tax paid from the audit - Tax paid after audit | -3.55221E6 | 1.15182E6 | 4.35348E5 | -5.16623E6 | -1.93819E6 | -8.159 | 6 | .000 |

From the findings, the t calculated at 6 degrees of freedom both at 95% and 99% confidence interval of the difference = -8.159. The critical t values are 2.44 and 3.70 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05 at 95% and less than 0.01 at 99% level of confidence), we reject the null hypothesis that there is no significant relationship between tax paid from the audit and Tax paid after audit for Conditional.

# CHAPTER FIVE

# SUMMARY, CONCLUSION AND RECOMMENDATIONS

## 5.0 Introduction

The chapter gives an overview of the study to show if it really met the objective of establishing the relationship between revenue collection and tax audit.

## 5.1 Summary of Findings

Income tax audit is the examination of a business or individual tax return by the internal revenue service or state tax authority which in this case is Kenya Revenue Authority. The terms audit, review and notice are used to describe enforcement of tax codes and filing returns accurately. The random tax audit evidenced the largest amount of tax collected and actually it is the one that is mostly conducted as shown on figure 4.0. The others that are cut-off audit and conditional audit have a smaller amount of tax collected. When a random tax audit was conducted an amount of Ksh. 69,043,829 was collected. From the cut-off tax audit Ksh. 27,171,975 was collected. Conditional tax audit collected an amount of Ksh. 5,078,314. From the figures 4.0, 4.1 and 4.2 it is also clear that when you compare the amount of taxes a company was paying two years prior to the audit is smaller than the ones that is collected from the same company two years after the audit. This indicates that after the audit the companies are more informed about their tax obligations and they know better in terms of tax computation hence higher taxes collected from the companies as evidenced in appendix D which has the raw data.

From the t-statistics results the parametric Pearson correlation or 'r' value is significant at 0.827 and the p-value (Sig) for the correlational coefficient is less than $p < .05$ and significant for Tax paid before audit and Tax paid after audit for random tax audit. In addition, the t calculated at 34 degrees of freedom both at 95% and 99% confidence interval of the difference = -7.959. The critical t values are 2.03 and 2.733 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05) we reject the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid after audit random tax audit.

From the findings, t calculated at 15 degrees of freedom both at 95% and 99% confidence interval of the difference = -5.322. The critical t values are 2.13 and 2.94 at 95% and 99% confidence interval of the difference respectively. Since p=.000 (less than 0.05) we reject the null hypothesis that there is no significant relationship between Tax paid before and Tax paid after audit for cut off

Also, the t calculated at 6 degrees of freedom both at 95% and 99% confidence interval of the difference = -4.788. The critical t values are 2.44 and 3.70 at 95% and 99% confidence interval of the difference respectively. Since p=.003 (less than 0.05) we reject the null hypothesis that there is no significant relationship between Tax paid before audit and Tax paid after audit for Conditional.

From the t-statistics results the parametric Pearson correlation or 'r' value is significant for tax paid before audit and tax paid after audit as it clearly then indicates there is an increase in the tax paid after audit, this is clear for random tax audit, cut-off tax audit and conditional tax audit.

## 5.2 Conclusion

Tax audit actually has an effect to revenue collection as according to the t – tests there is significance in the correlation between tax collected before the audit and after the audit. This clearly indicates that tax audit increases revenue collection. That in essence means that the more the tax audit conducted the more revenue is collected. Thus it is right to say that tax audit is directly related to revenue collection. All the tax audits are important because they add something to revenue and thus should be encouraged as it assists the government in collecting appropriate tax revenue necessary for budget, maintaining economic and financial order and stability, to ensure that satisfactory returns are submitted by the tax payers, to organize the degree of tax avoidance and tax evasion, to ensure strict compliance with tax laws by tax payers, to improve the degree of voluntary compliance by tax payers and to ensure that the amount due is collected and remitted to government.

## 5.3 Recommendation

The study recommends that the tax audit reports be submitted to the public and a standard procedure to be found in choosing the companies that random audit is conducted. This is to assure the public that those audited randomly are not eyed or discriminated but at least they see the result and be aware of the procedure used in the selection. The public is also urged to submit their taxes fully and seek clarification wherever they are not sure of what to do.

## 5.4 Limitations of the Study

This study had several limitations. First, it is possible that the nature of data from the audit reports is impacting the results in an unanticipated manner or limits the power

of the tests to detect associations. This may be created by variation of statistical figures illustrating the key variables measurements.

It is possible that the statements do not indicate low or high audit quality. A control variable is a variable that is held constant in a research analysis. The use of control variables is generally done to check observed relationship between two variables if a direct one or indirect with intervening.

The study did not use control variable specifications as specified by Richardson et al (2002). It is thus possible that lack of inclusion, cause alterations in interpretation.

Finally, the use of secondary data provided an opportunity to search for a more genuine and intrinsic relationship between the variables. This afforded the researcher the benefits of a greater focus on analyzing the available data more closely in a way that would enhance the achievement of the study objectives. However, selecting the right combination of variables to proxy for unobservable phenomena is always a problem in empirical quantitative research. However, in most quantitative investigations, the effects and methods of handling measurement error in the dependent variables have been well documented and efficient.

## 5.5 Recommendations for Further Research

This study examined the effects of tax audit on revenue collection over a period of less than 5 years. There is a need for further studies to carry out similar tests for a longer time period.

A similar study should also be carried out on more companies within Nairobi as well as in other companies in other Counties. In addition, more variables depicting tax

audit should be adopted to uphold the study's findings that indeed audit influences revenue collection.

Due to the importance of having high quality audit, further studies should explore the areas that relate to audit quality such as customer service satisfaction, customer loyalty, auditors switching and auditors turnover. This will go along incorporating quality and independence of management and board membership; internal audit considerations.

Further, there is need for a study on how the size of a company influences the auditing as there is variation for various organizations based on the size. Further, a study should be conducted on the procedures followed during audit to see if all the Kenya Revenue employees follow the same procedures or a standard procedure is in place and adhered to.

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# APPENDICES

## APPENDIX A

## LETTER OF INTRODUCTION

DANIEL MIRERA NYAKAMBA,

UNIVERSITY OF NAIROBI,

P.O. BOX

NAIROBI.

THE KENYA REVENUE AUTHORITY,

THROUGH,

THE COMMISSIONER DOMESTIC TAXES,

Dear Respondent,

**RE: DATA COLLECTION**

I am a student at University of Nairobi undertaking a Masters degree in Business Administration (MBA).As part of the requirement of the course I am required to undertake a project in my area of study. My research topic is on "To establish the relationship between revenue collection and tax audit" Therefore the staff has been selected as respondents in this project. Your sincere and correct answers will be important in attaining this goal. All information will be treated with utmost confidentiality for learning purpose only.

Thank you in advance,

Yours sincerely,

Daniel Mirera Nyakamba.

# APPENDIX B

## SCHEDULE OF ACTIVITIES

| ACTIVITY | JANUARY | FEBRUARY | MARCH | APRIL | MAY | JUNE | JULY |
|---|---|---|---|---|---|---|---|
| Proposal defense | xxx | | | | | | |
| Sending data checklist | | Xxx | | | | | |
| Booking appointments | | Xxx | | | | | |
| Data collection | | | Xxx | xxx | | | |
| Data analysis | | | | | xxx | | |
| Report writing | | | | | | xxx | |
| Final presentation | | | | | | | Xxx |

# APPENDIX C

## BUDGET

| Item | Cost (sh.) |
|---|---|
| Stationary | 16,000 |
| Cyber services | 5,000 |
| Typesetting and printing | 14,000 |
| Communication | 2,000 |
| Commuting | 8,000 |
| Miscellaneous | 5,000 |
| Total | 50,000 |

# APPENDIX D

# RAW DATA

| S/No. | TAX PAID BEFORE AUDIT | | TAX PAID FROM THE AUDIT | TAX PAID AFTER AUDIT | |
|---|---|---|---|---|---|
| | 2008 | 2009 | | 2011 | 2012 |
| 1 | 1,250,939 | 1,489,153 | 1,131,232 | 2,802,576 | 3,669,338 |
| 2 | 26,159 | 31,826 | 924,347 | 3,046,478 | 3,583,353 |
| 3 | 7,018,683 | 10,255,074 | 9,651,434 | 12,039,835 | 12,563,558 |
| 4 | 223,619 | 2,825,147 | 1,303,815 | 4,364,734 | 5,295,095 |
| 5 | 800,000 | 777,431 | 115,376 | 1,214,962 | 1,140,635 |
| 6 | 1,507,956 | 1,237,383 | 300,505 | 1,279,570 | 1,213,712 |
| 7 | 800,000 | 1,931,381 | 1,533,753 | 2,245,745 | 2,368,253 |
| 8 | 620,381 | 613,761 | 4,356,230 | 3,672,439 | 8,217,154 |
| 9 | 915,665 | 1,476,019 | 6,843,460 | 5,649,639 | 4,970,174 |
| 10 | 3,434,892 | 2,565,745 | 654,908 | 4,181,459 | 4,986,602 |
| 11 | 853,839 | 970,432 | 1,021,087 | 1,319,053 | 1,908,190 |
| 12 | 1,100,267 | 2,293,425 | 74,460 | 3,395,885 | 3,077,492 |
| 13 | 1,827,732 | 1,940,260 | 1,188,898 | 3,128,236 | 3,494,116 |
| 14 | 197,056 | 2,796,617 | 2,100,020 | 3,176,247 | 3,648,505 |
| 15 | 950,763 | 2,394,338 | 390,915 | 3,872,223 | 5,127,393 |
| 16 | 163,864 | 1,068,800 | 456,790 | 2,623,274 | 2,394,028 |
| 17 | 697,469 | 1,613,400 | 269,850 | 2,706,481 | 3,107,380 |
| 18 | 158,181 | 2,265,480 | 269,850 | 2,730,567 | 2,658,931 |
| 19 | 137,057 | 422,637 | 789,650 | 1,845,060 | 2,236,062 |
| 20 | 1,058,322 | 1,335,749 | 5,212,549 | 4,373,911 | 4,764,921 |
| 21 | 1,163,547 | 1,010,747 | 2,242,698 | 1,476,859 | 1,821,426 |
| 22 | 1,103,572 | 1,690,682 | 5,891,080 | 1,704,350 | 5,560,045 |
| 23 | 372,387 | 919,285 | 1,092,740 | 1,551,721 | 1,650,874 |
| 24 | 2,056,780 | 2,589,386 | 295,219 | 3,233,513 | 3,268,966 |
| 25 | 211,825 | 1,689,601 | 447,385 | 3,071,487 | 3,039,336 |
| 26 | 1,145,698 | 1,444,514 | 1,047,572 | 2,270,568 | 2,343,236 |
| 27 | 1,237,464 | 1,243,036 | 1,751,600 | 2,066,970 | 4,205,232 |
| 28 | 412,851 | 642,162 | 671,321 | 1,034,954 | 2,703,634 |
| 29 | 1,221,507 | 1,040,452 | 724,866 | 2,033,652 | 2,165,356 |
| 30 | 434,696 | 485,877 | 324,300 | 979,737 | 1,458,708 |
| 31 | 1,007,103 | 1,361,600 | 1,280,170 | 1,298,005 | 1,433,362 |
| 32 | 2,802,617 | 2,317,216 | 4,321,670 | 3,847,315 | 3,266,113 |
| 33 | 1,072,372 | 1,179,685 | 277,579 | 2,314,322 | 2,372,331 |
| 34 | 1,864,631 | 2,265,786 | 6,794,457 | 2,598,287 | 2,854,731 |
| 35 | 1,621,949 | 1,535,980 | 1,360,079 | 3,065,306 | 3,465,606 |
| 36 | 899,565 | 1,276,587 | 961,959 | 1,702,995 | 3,905,041 |
| 37 | 1,232,112 | 1,559,958 | 2,603,200 | 7,461,633 | 7,277,737 |
| 38 | 349,546 | 295,550 | 2,316,872 | 5,001,916 | 4,323,307 |

| | | | | | |
|---|---|---|---|---|---|
| 39 | 1,550,448 | 1,340,275 | 633,966 | 1,949,488 | 1,702,372 |
| 40 | 997,044 | 926,956 | 2,344,948 | 3,064,980 | 3,365,068 |
| 41 | 4,323,803 | 5,193,321 | 674,030 | 6,239,013 | 6,748,812 |
| 42 | 2,483,364 | 3,690,881 | 932,200 | 4,456,000 | 6,813,062 |
| 43 | 1,746,776 | 1,458,999 | 4,564,472 | 1,191,947 | 1,872,867 |
| 44 | 3,019,639 | 2,424,179 | 9,135,781 | 4,366,154 | 5,126,435 |
| 45 | 187,811 | 896,175 | 1,145,712 | 2,577,422 | 2,985,000 |
| 46 | 1,112,591 | 1,046,386 | 244,999 | 2,144,581 | 2,429,139 |
| 48 | 649,753 | 1,211,424 | 1,018,250 | 1,221,821 | 1,525,346 |
| 49 | 2,077,146 | 2,560,090 | 591,952 | 3,863,451 | 3,817,387 |
| 50 | 1,128,404 | 1,289,966 | 867,428 | 2,425,310 | 2,141,496 |
| 51 | 3,538,780 | 3,732,771 | 550,744 | 4,107,402 | 4,351,360 |
| 52 | 538,835 | 679,612 | 324,224 | 2,273,830 | 5,515,095 |
| 53 | 2,127,329 | 1,613,400 | 279,584 | 3,833,002 | 3,642,014 |
| 54 | 950,000 | 1,641,646 | 452,500 | 2,483,165 | 2,328,450 |
| 55 | 515,844 | 917,647 | 104,557 | 3,432,629 | 4,019,730 |
| 56 | 280,492 | 1,071,209 | 960,544 | 2,933,052 | 10,008,011 |
| 57 | 1,203,688 | 1,188,684 | 1,439,615 | 5,597,258 | 5,763,403 |
| 58 | 2,436,245 | 2,339,117 | 1,517,290 | 3,823,500 | 4,234,432 |
| **TOTALS** | **75,754,477** | **100,411,969** | **101,294,118** | **179,466,05** | **217,111,66** |