THE EFFECT OF TAX REFORMS ON FINANCIAL PERFORMANCE OF REAL ESTATE FIRMS IN KENYA.

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DECLARATION

I, Georgeena Kanini Kimeu, hereby declare that this research project is my original work and my own effort and that it has not been submitted to other institution of higher learning for any academic purposes.

Date:

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This project has been submitted for examination with my approval as

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DEDICATION

This research project is dedicated to my husband Frank, my mother, Jane Kimeu and my two children Ian and Michelle for their understanding, unreserved support and encouragement.
ACKNOWLEDGEMENT

I am heartily thankful to my supervisor, Dr Josiah Aduda, whose encouragement, insightful guidance and appropriate coaching in my research work has enabled me to deepen my understanding of the subject. His insightful scholarship and meticulous accuracy were instrumental in shaping this work to its final form. My deepest gratitude goes to my beloved children, Ian and Michelle and my loving husband for their continuous love, encouragement and support in every aspect of my academic pursuit.

This project would not have been possible without constant support from my employer, Kenya Revenue Authority, in granting me a scholarship and study leave at the University of Nairobi. Equally, I wish to extend special gratitude to the management of the Real Estate Firms for their cooperation and facilitation in providing the requisite data for this project.

Words are not enough to describe my indebtedness to my mum, Jane Kimeu, who sacrificed so much and shaped my life to reach this far. To all my classmates and colleagues from whom I received valuable comments, I say a big thank you. And to my Almighty God, I thank you for your mercy, grace and gift of life that has enabled me to walk this journey and witness the auspicious attainment of my academic pursuit.
ABSTRACT

Tax reforms determine economic growth, equitable development and financing of an adequate level of social public expenditure for growth while limiting budget deficits. It is usually used as a requirement for financial assistance to developing countries’ governments by international development agencies. The effects of Tax reforms on the financial performance of real estate firms are very critical to the government and particularly to the Kenya Revenue Authority whose mandate is to administer and enforce laws relating to revenue collection on behalf of the government. It forms the basis for this study.

Previous empirical studies on tax reforms have exclusively focused on the impact of tax reforms on various sectors of the economy other than on its effects on financial performance. Arising from those studies, a number of key findings as well as limitations emerge that have informed the structure and approach of this study. Previous studies portray hostility between the taxpayers and tax collectors on issue relating to tax reforms. Equally, the studies present sounding evidence indicating that taxpayers are able to complete on-line filing with much easy where the government provides a more user-friendly on-line tax filing system.

The results of this study show that tax reforms have a positive effect on the financial performance of the real estate firms in Kenya. However, those effects are rather weak. Of the determinants explored, experience in the implementation of tax reforms, filling of returns on-line and tax relief present the most influencing positive effect on the financial performance of the real estate firms; with implementation of tax reforms taking the most single important position in influencing financial performance.

The action of taxpayers, whether due to ignorance, deliberate evasion or weaknesses in the tax administration implies that non-compliance with the tax law remains a challenge? To curb this, tax administration authorities should put in place strategies, structures and systems that ensure that non-compliance with tax reform laws is kept to minimum. They should also implement computer-assisted tax reform programs that are well balanced and incorporate a good mix of both proactive and reactive systems as well as approaches that cover all aspects of tax reforms management from education through enforcement to prosecution. In addition, the reform programs should be designed in such a manner as to leave economic behavior unaffected, minimize efficiency losses associated with any new reform system while at the same time yield sufficient revenues to fund socially and economically empowering programs without creating substantial inequity.
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LIST OF ABBREVIATIONS

ANOVA   Analysis Of Variance
EAC     East African Community
DC      Developing Countries
DTD     Domestic Tax Department
GDP     Gross Domestic Product
ICT     Information and Communications Technology
ITMS    Integrated Tax Management System
KIPPRA  Kenya Institute for Public Policy Research and Analysis
KNBS    Kenya National Bureau of Statistics
KRA     Kenya Revenues Authority
NSE     Nairobi Security Exchange
OECD    Organization for Economic Co-operation and Development
OTPR    Office of Tax Policy Research
PIN     Personal Identification Number
PWC     Price Waterhouse Coopers
RARMP   Revenue Administration Reform and Modernization Programme
R&D     Research and Development
REP     Real Estate Property
TAT     Technology Acceptance Theory
TPB     Theory of planned behavior
USA     United States of America
VAT     Value Added Tax
WDI     World Development Indicator
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CHAPTER ONE
INTRODUCTION

1.1 Background of the Study

Tax reforms has often determines Economic growth, equitable development, and financing of an adequate level of social public expenditure for growth, while limiting budget deficits, are conditions for financial assistance usually required of developing countries’ governments by international development agencies. These conditions are usually linked with requirements to reform the developing countries’ tax policies and Tax Administration systems and practices. Therefore, major tax administration/policy reform objectives often define the overall context of many modernization projects funded by international development agencies. Such objectives expressed in various ways on different projects): Broaden the tax base, Strengthen the organization and its management, Control tax evasion, Improve tax collections, Facilitate voluntary compliance for taxpayers. In modern reality, attainment of each of the reform objectives is inextricably dependent on the successful design and implementation of computerized, integrated tax information systems.

The real estate property sector plays an important role in the Kenya economy. In terms of growth, Kenya’s real estate market is still superior in comparison to her peers in the region. Although the rest of East Africa is also making considerable headway with much improved infrastructure and renewed interest by developers to build and sell more in trying meet the growing demand in both residential and commercial property segments according to Daniel Ojijo (2013) real estate sector going 2013. Growth drivers are quite similar across the region with factors such as rapid urbanization, modern household formations, regional economic growth, and improved government policies among others. Nairobi is a prime market in a major way especially because of infrastructural development and market interest. Investors are being attracted by the city’s potential to offer high returns on the property market. There is also a notable high demand especially in the high-end market, which is expected to grow even more as interest rates come down. To give you a clearer picture, the City Council of Nairobi approve an estimated
12,000 residential and commercial building plans each month. However, with the formation of county governments, there is bound to be more keen interest in real estate development in other towns.

In the wake of the global financial crisis, there has been dwindling receipts of Diaspora remittances from Kenyans working abroad, though the growth in mortgage financing in the country has enhanced the growth of the property market in the country this is according to Loise, W, & ABN, D (2013) report. It is also worthy to note that in some segments such as luxury real estate it has been observed by analysts that the cities of Nairobi and Mombasa are global trailblazers. Through the literature review and this study will be able to try to establish if there is positive relationship between tax reforms and financial performance of real estate firms in Kenya.

Both experts in finance and economics have debates on the impacts of tax reforms on financial performance of real estate firms for decades. Large quantities of research were discussing about the effects of the Tax Reform Acts in the Kenya, such as the effects on economic condition, financial market, investors’ strategy and financial performance, etc. We aim to investigate the impact of the taxation legislation changes on real estate financial performance.

The Kenya Revenue Authority (KRA) has embarked on an aggressive program to modernize and automate revenue administration. Among the KRA’s impressive, recent accomplishments is the integration of formerly separate departments for income taxes and value added taxes under a new Domestic Tax Department (DTD); acquisition and implementation of a modernized customs system (SIMBA); and development of a KRA-wide Information and Communications Technology (ICT) Strategy, Plumley (2002). Electronic filing of tax returns is increasingly used by tax administrators around the world to reduce the data capture overhead during returns processing and to increase security and confidentiality of taxpayer data. Other advantages of e-filing are reduced paper storage for taxpayers and the tax authority, faster and more accurate return filing process.
The taxpayer registration process/module of the Integrated Tax Management System have the primary responsibility of the managing the PIN database for both individuals and legal entities (corporations, partnerships etc.). As part of the Redesigned Business Processes the VAT and PIN, databases are merged into one database. The taxpayer recruitment function (currently housed in Taxpayer Services) is to recruit persons/entities, which have income or revenue liable for tax but are currently not in the tax net.

Tax Reform Acts, Sinai and Gyourko (2004)’s work on the Taxpayer Relief Act in 1997, Elayan et al. (2006)’s event study on Self-Lease Back transactions of REITs during 1986 to 1999, Amromin et al. (2006)’s research on 2003 Dividend Tax Cut and so on. However, the findings were mixed. We argue that one of the reasons is the lack of control in the studies. We test the hypothesis that REIT will gain return that is more excess after each tax reform than before it.

1.1.1 Factors Affecting the Real Estate Property Sector

Demand for real estate property is controlled by taxation, monetary policies and many others factors, such as employment, immigration policy etc. The activities of the real estate sector also are influenced by financial support measures from government, both at the Commonwealth and the State levels. Examples include public housing policy and the financial assistance scheme (i.e., First Home Owner Grants and rental assistance).

1.1.2 Rental Income

All rent, premium or any other consideration for use or any other consideration for use or occupation of property. All persons in receipt of rental income unless exempted under any law is assessable and taxable. Disallowable expenses in the calculation of rental income are specified under section 16 of the Income Tax Act are which include depreciation cost of maintaining self and family capital expenditure general provisions of bad debts, tax paid to the government etc. Allowable expenses include cost of acquisition of land, professional fee paid to quantity surveyor, architects, civil engineering, electrical engineers, cost of
building material, labour and interest on money borrowed to earn investments, hire expenses for equipments and commercial vehicles

1.1.3 Incentive to Real Estate Developers

Section 20C of the Income Tax Act exempts income of real estate investments trust (REITs) from taxation effective from 1 January 2012. A REIT is a vehicle, which allows investors to pool resources together and invest in real estate. The shareholders of REITs acquire units, which are tradable in stock market. Commercial Building allowance on the cost of construction of commercial building at a rate of 25% (w.e.f 1 January 2010) where roads, power, water, sewer and social infrastructure are provided by the investor. Residential buildings constructed in a planned development area approved by the Minister for Housing at the rate of 5% (w.e.f 1 January 2008). Wear and Tear allowance on machinery and equipments as per the second schedule of the Income Tax Act, Cap470. Deduction of interest paid on mortgage for owners-occupied property, subject to a maximum of Kes 150,000 per year.

1.1.4 Tax administration in Kenya

The Kenya Revenue Authority, hereinafter referred to as KRA or the Authority, was established on 1st July 1995 under an act of Parliament, the KRA Act Cap 469, as a central body for the assessment and collection of revenue, for the administration and enforcement of the laws relating to revenue and provisions for connected purposes. It is mandated to administer and enforce the laws relating to revenue as contained in the first schedule to the Act. The main laws are the Income Tax Act (Cap.470), Value Added Tax Act (Cap 476), the Custom and Excise Act (Cap. 472) and the Traffic Act (Cap 403). The authority is therefore charged with the responsibility of collecting revenue on behalf of the government. In its mission statement, KRA aims 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 Taxpayers Charter outlines five primary obligations on taxpayers; 1) to fill timely returns/Custom entries; 2)
to make accurate reports on all returns/entries; 3) to pay the required taxes voluntarily and timely; 4) to give revenue officers maximum cooperation and accord them their due respect and freedom to carry out their lawful duties; 5) to disclose and produce all relevant information, records and documents to tax officials. The Economic Recovery Strategy for Wealth and Employment Creation, which was implemented by the new regime from 2003 to 2007, was successful in reversing the economic decline of the past two decades. In 2007, for the first time since the 1970s, the annual rate of real GDP growth reached 7%. While the post 2007 election violence and onset of the global financial crisis resulted in a slump in real GDP growth in 2008, to 1¾% (IMF, 2010), it is projected that GDP growth will be about 5% in 2010.

In the short-to-medium, there are four key fiscal governance drivers. First, an expensive bureaucracy, as reflected in Kenya’s wage bill to GDP ratio compared to other countries in the region, needs to be sustained. In 2007/08 the wage bill to GDP ratio was estimated to be 7.4% (IMF, 2010), which was the highest amongst EAC countries. Second, there are ambitious social welfare goals that are reinforced in the Bill of Rights in Kenya’s new (2010) Constitution. Third, elite capture of fiscal governance, as depicted by two initiatives by Members of Parliament (MPs) in recent years – in terms of introduction of the Constituency Development Fund, which is under the control of individual MPs, and the arbitrarily high self-pay awarded by MPs. Fourth, the ambitious development goals for the country as aptly captured in Kenya’s Vision 2030. This underlies the recourse to using infrastructure bonds, amounting to about KES 52 billion in 2009 and 2010 (equivalent to about US$650 million). Nonetheless, given the comparative resilience of Domestic Revenue Mobilization in Kenya over the years, barring any unforeseen adverse political or socio-economic developments, Kenya’s fiscal governance trajectory is solid. Tax payers education and tax administration systems modernization.

1.2 Research Problem
Tax reforms effect on firms' financial performance is a very vital and important issue and the main idea of this study was to examine whether or not the tax reforms taken into consideration at this study can affect and determine the firms’
financial performance of a real estate firm. Taxation has significant implications for corporate behavior and the impact of taxes reforms on resource allocation and economic welfare has long been a topic of much interest to academics, policy makers and the wider community. From the perspective of the financial sector, the primary focus has been on the implications of taxes reforms for asset valuation particularly in the areas financial performance of real estate firms.

According to research carried out by Nada Eissa of KPMG (2009) on real estate policy issues in Kenya, capital are exempted from the personal income tax in Kenya. Although there are arguments against the taxation of capital gains, it appears that the dominant reason for the real estate, the ownership of which is concentrated in the hands of political elite. A research carried out by Africa Development Bank on Resource Mobilization for Poverty Reduction in East Africa and in particular, Kenya (2010) showed the resent reforms and development in tax systems and reforms but did not state how to analyze how to match the effects of tax reforms and the financial performance of real estate firms.

A research carried out by Ndungu (2011) on designing a property tax reforms strategy for Sub-Saharan Africa an analytical applied to Kenya established that although policy debate concerning tax base definitions, exeptions and tax rates structure is a favorable topic among public finance economist, the reality in the developing world is that improving administration not fine-tuning policy-is the critical key to better property tax performance. As the case study of Kenya illustrates there is tremendous potential from improving basic property tax administration in terms of increasing the coverage, valuation and collection ration. According to Prof, W.O. (2010) Revenue Autonomy and property Taxation in Anglophone East Africa: Opportunities, Emerging Trends and Challenges. The global urbanization trend indicates that a large number of the world population is moving towards the urban areas. This continued migration to the urban areas calls for increased provision of adequate urban infrastructure and social service notwithstanding the limited sources of revenue revenue available. The paper concludes that property taxation reforms is facing challenges that need to be addressed if it is to remain significant and calls for institutional of reforms in the implementation of property tax systems.
1.3 Objectives of the study
To establish the effects of the tax reforms on the financial performance of real estate firms in Kenya.

1.4 Significance of the study
The results of the study will be useful in filling the gaps that have been left by the previous studies on impact of tax reforms on financial performance of real estate firms in Kenya and to the following group of people. The management of KRA will use the study to understand how effective the authority’s activities are on the levels of taxpayer’s data becoming integrated to be able to access one system, look for better ways of raising compliance rates, and hence maximize revenue.

The policy officials at the Treasury may also use the study to understand the impact of tax reforms on real estate sector to increase the tax base hence to reduce the budgets deficit hence economic growth. The real estate firms to understand the tax incentives available hence will use the study to predict various tax reforms which if adopted will help in future forecasting of revenue, profits and expenditure trends. It helps the academicians and researchers to know the areas of real estate research, which has never been covered fully, and CBK for monetary and fiscal policy formulation.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction
This chapter provides a discussion of the theoretical and the empirical literature explaining and related to this study. There are three theories that explain the impact of tax reforms financial performance of real estate firms. These theories are, Economic Theory, The Pittsburg Theory. The above two theories explains the economic effect on change in tax rate, the other theory states the effects of tax reforms and how individual firms behave towards the tax reforms.

The empirical studies on the effects of tax reforms in different countries show that there is positive effects on the effect the reduction tax rates and incentive on real estate firms. As shown by Pittsburg experience compliance.

2.2 Review of Theories
There are several theories on the effect of tax reforms on financial performance of real estate firms, which include:

2.2.1 Economic Theory
Economic theory provides researchers with powerful tools, suggesting the types of behavioral responses that are likely or feasible in response to a particular tax change. Indeed, much of what we “know” about the effects of tax reforms is really based primarily on economic theory, rather than direct observation. For example, we “know” that, other things equal, an excise tax on a particular commodity will reduce demand for that commodity, even if no such tax has been imposed in the past. Theory tells us that demand curves slope downward, we may even “know” how responsive to the tax demand will be, based on estimates of the price elasticity of demand. Standard theory tells us that a tax-induced price increase should have the same impact on demand as any other price of equal magnetite and we have no evidence to the contrary.
2.2.2 The Pittsburgh Theory

After Pittsburgh further increased the difference between the tax rate for land and the tax rate for buildings in 1979-80, the city experienced a substantial increase in building activity. Oates and Schwab (1997) provided suggestive evidence that Pittsburgh’s change in tax rates played a major role in stimulating the building boom. They noted that this finding is surprising; however, because public finance theory suggests that increasing the land tax while leaving the buildings tax unchanged should have no effect on building activity. It is also worth noting, however, that according to Oates and Schwab, the city of Pittsburgh granted tax cuts for new building construction. These tax cuts essentially indirectly lowered the tax rate on new (but not on existing) buildings.

2.2.3. Theory of Planned Behavior

Early studies mainly focus on theory of reason action (TRA) as identified by (Fishbein and Ajzen, 1975). TRA is based on the fundamental variables of attitude and subjective norm. The two variables are seen to have a positive effect on individuals’ behavioral intentions, which positively induce individuals’ actual action. Attitude is an individual’s positive or negative evaluation of self-performance of a particular behavior. The concept is the degree to which performance of the behavior is positively or negatively valued. Subjective norm is an individual’s perception about particular behavior, which is influenced by the judgment of significant others (e.g., parents, spouse, friends, teachers). Behavioral intention is an indication of an individual’s readiness to perform a given behavior and it is assumed immediate antecedent of behavior. However, the basic hypothesis of TRA states that the occurrence of behavior is based on volitional control of one’s willpower (Fishbein and Ajzen, 1975). Thus, the behavior occurs mostly from one’s willing. Thus, Ajzen (1985) modifies TRA and further proposes the theory of planned behavior (TPB). Ajzen (1985) proposes TPB to explain and predict human behavior patterns. TPB extends the theoretical framework of TRA and adds perceived behavioral control to account for individuals’ uncontrollable factors. TPB is founded the three factors as perceived behavioral control, attitude, and subjective norms. Hence, behavioral intention is influenced by perceived behavioral control, attitude, and subjective norms. Actual
behavior is in turn, determined by behavioral intention. Among all, perceived behavioral control refers to individual’s perceived ease or difficulty of performing the particular behaviors. In recent years, there have been widespread tax reforms and more diversifications in real estate sector. Studies on TPB applying on electronic commerce have increased. Tan and Teo (2000) integrate TPB and diffusion of innovation theory to investigate the factors that affect people’s intention towards using internet. Empirical results show that attitude and perceived behavior control would positively affect people’s intention to use internet banking. In the subsequent studies, Huang et al. (2006) find that TPB indeed can be explained the people’s behavioral intention of on-line tax filing. Hsu et al. (2006) review users’ continual behavior towards internet shopping by longitudinal investigation, which not only employ TPB factors (attitude, subject norms and perceived behavior control) but also integrate expectation Disconfirmation theory to construct the research model. The empirical results show that subjective norms, attitude, and perceived behavior control are the major factors affecting consumers’ continuous intention of internet shopping. In addition, equity concept, which is respected by accounting scholars (Jackson and Milliron, 1986; Moser et al., 1995; Efebera et al., 2004), is also omitted in the pre-factors. To sum up, the empirical results of the above-mentioned literatures prove that TPB could be applied to explain the behavioral process of human being engaged in or accepted information technology.

2.2.4 Performance Measurements in Real Estate Firms

The financial performance of real estate firm is of central importance if accumulated assets are used to meet real estate firm obligations. Its measure is therefore perquisite for effective investments as it serves the purpose of analyzing both the performance and projecting future. Several techniques exist for measuring the financial performance of real estate firms. Miller and Hanhooose (1993), however point out that the current profitability is the most widely acceptable measure and is evaluated either using return on asset or equity. Unfortunately this measure alone cannot permit one to judge the long term performance of real estate firms either alone or in group. Consequently the authors proposes other measure to be considered along with profitability such as
asset growth, earning per share, dividend payout ratio, return achieved on investment targets, reduced administration cost or any combination. Asset growth provides reasonable indicator of both current and long term performance and prospect.

2.3 Review of Empirical Studies

Though not so much as the theoretical literature, the empirical investigations of tax reforms impacts on the financial performance of real estate firms had been carried out recently followed three primary lines of inquiry. First most empirical work in the 2009 were undertaken to examine the influences of tax changes by simulation modeling to estimate the impacts of tax reforms on the firms’ financial performance and value, i.e. Fisher and Lentz (2006), Hendershott et al. (2008). Despite the extensive studies in this area the estimations may not reflect the real impacts from tax changes because of including some potential simultaneous-equation bias Sanger et al. (2007). In this study, we examine the effects of tax reforms on financial performance of real estate firms. Will try to largely avoid the obstacles that complicate the interpretation of results from prior studies i.e the hostility between the tax payers and the tax collectors on issues relating to tax compliances and evasion cases.

William (2011) is of the view that very few empirical studies have attempted to investigate the effects of the tax reforms real estate financial performance. Most of those that have attempted to do so have focused almost exclusively on the impact of tax rates rather others tax measures. As Tanzi (2007) points out tax administration determines the real (or effective) as opposed to the statutory tax system. There is need to differentiate between tax policies from tax administration. In Kenya, promulgation of tax policy is the domain of the Ministry of Finance (Treasury), while tax administration is vested in the Kenya Revenue Authority (KRA). The operational metaphor for the relationship between KRA and the Ministry is Principal and agent. For the purposes of this study, the tax administration referred to both KRA and the treasury. This is because according to Tanzi (2007), tax administration is tax policy. Empirical literature reviewed suggests that there are some research gaps regarding the effect tax reforms on
property tax this mainly because of lags in maintaining tax base of coverage, inaccurate valuation and inadequate collection and enforcement of the tax management system. Kelly (2011). Thus any property tax reforms strategy must recognize this administration-intensive nature and importance of direct and active government administration for its revenue buoyancy.

As discussed, the event study method has limitations on controlling the factors other than tax legislation changes. Even though the analysis could be so detailed tested that every single event date was explored in the study, the method still could not access the reliable results without the controls. Therefore, this study adopts a control experiment, which is widely applied in scientific research, to investigate how the changes of taxation legislation affect the REITs market. There is little research in economics or financial area employing the controlled research model. That may because the controlled samples in the two areas are too difficult to find. Methodology that is more rigorous will be applied in this study, which is probably the first empirical test on the effect of taxation legislation changes on REITs. First the effects from stock market on REIT’s return are controlled by using the excess return of REIT as the dependent variable. In addition, same-date-event influences are controlled by an inter-emporia and a cross-sectional interaction variable in two countries in the empirical model. This model was initially established in Yiu (2010)’s work and has been intensively applied in Yiu (2007)’s work for the investigation of the property price gradients in Hong Kong and Macau, and Yiu (2009)’s work for the exploration on the impacts from implementation of pedestrian scheme on retail rents.

Empirical evidence on the ground shows there has been hostility between the taxpayers and tax collectors on issue relating to tax reforms- how about tax evasion cases reported daily in our local newspaper (Daily Nation, July 7, 2006, pg 3) because of lack of proper system to fast track the operation and transactions of business entities in Kenya. Empirical review by past researchers has shown that taxpayers are able to complete the filing easier if the government provide a more user-friendly on-line tax filing system (simple operation, easy-to-understand interface, and check the tax exemptions automatically) (Ramayah et al., 2009).
The possibility of using on-line tax filing will be increased at the same time. Thus, this paper infers that higher perceived ease of use will on the other hands allow the taxpayers to know the advantages of the system only if it is easy to operate (Warkentin et al., 2002). They will also have a positive attitude toward the system. When users perceive that the system is easy to operate, they will have more positive attitude hence comply.

Past research has indicated that it is reasonable to assume that tax authorities seek to use their resources in an optimal way. It is also reasonable to assume that tax administration seek to collect the tax correctly payable according with the tax laws. Therefore as part of the process in allocating resources to achieve maximum effectiveness, it is appropriate to identify areas (issues and/or taxpayers) of low or non – compliance, and then be able to rank them. Brooks (2001) states that many tax administrations today have within their corporate objectives or goals the improvement of integrated tax system. Potentially, these administrations may have difficulty in establishing their performance against this objective, especially so if there is no effective way of measuring any move in compliance levels over time. It is expected that many administrations currently measure the effectiveness of their integrated tax system improvement strategies solely on revenue return, which is, of course, not synonymous with compliance improvement. For the future, such administrations need to develop ways to measure trends in taxpayer compliance to measure their overall effectiveness (OECD, 2001).

From information quality perspective, personalization, completeness, relevance, easy of understanding and security quality dimensions are used to measure electronic information system content issue (DeLone and McLean, 2003). While, based on Chang et al. (2005), information quality has been defined by the degree to which users are provided with quality information regarding their needs. In practices, the e-Filing system benefits taxpayers because tax returns are sent electronically to the KRA, which saves taxpayers’ time, and in this system, promotion campaign, the tagline ‘easy to use, accurate and safe to use’ were used. As a user of e-Filing system, we need a convenience and usefulness services in order to get quality information, so IRBM should increase the use of information
and communication technologies to improve the delivery of public services and dissemination of public administration information to the public.

Service quality or in another words, overall support delivered by the service provider towards electronic information system, are measured using assurance, empathy, responsiveness quality dimensions (DeLone and McLean, 2004). Service quality is the key to measure user satisfaction (Pitt et. al., 1995). As a user, the most important aspect of service quality in e-Filing system is security. As stressed out by KRA CEO, the e-Filing system is secure and it is difficult to get into anyone’s personal tax file because they need to enter personal identification number (PIN) and a password (The Star Online, April 27th, 2007). Meanwhile, in Malaysia, the adoption of the electronic tax filing is voluntary. Ann Ngugi (2010) suggested that a system that is usefulness and easy to use are important for taxpayers to voluntarily e-file their tax returns. Thus, the government should increase its efforts to promote the usefulness and user-friendliness of the e-Filing system. There are several studies conducted to develop measurement instruments for electronic service quality in the area of online retailing service quality, web site design quality, and online service quality.

2.4 Concept of Tax Reforms

Computerization of tax and revenue authorities can contribute to reaching the goal of good (financial) governance. It improves accountability and transparency of the revenue authorities. Nevertheless, while reforming and modernizing the tax system is an essential part of improving domestic resource mobilization, such a reform will be sustainable only in conjunction with more profound changes in the administrative and political structure of a state. Efficient internal revenue collection is a major step towards self-sufficiency and independence. To realize this goal, Developing Countries (DC) have a difficult starting position. Industrialized Countries (IC) are organizationally and technologically better equipped and thus better placed to utilize their (tax) resources more efficiently. Whereas ICs generally manage to capture about 90% of the given tax potential, in DCs this can be as little as around 40%. Taxes can be dichotomized into direct taxes and indirect taxes. The income tax is a direct tax. Indirect taxes include the
sales tax, also called consumption tax. Other indirect taxes include the value added tax (VAT), excise tax, estate tax, gift tax, employment tax, and user fees. The VAT is applied at each stage of production for the value added to the goods. As with all taxes, the tax burden ultimately falls on the consumer because companies can reclaim taxes paid.

The payment of tax is obligatory duty of every citizen whether natural or corporate citizen. As a civic duty, it is expected that citizens will voluntarily comply with such obligation but that is not the case with some citizens. Alm Martinez-Vazquez and Schneider (2003) acknowledged that most people do not like to pay taxes as a result; it is difficult for tax authority to impose and collect taxes anywhere and anytime. In order to ensure compliance with tax rules and regulations, tax system made up of tax laws, tax policy and tax administration is in place. According to Marti (2000), the existence of tax system forces individuals and organizations to give part of their income to the government as tax payment. Silvani (1992) added that the goal of tax administration is to foster voluntary compliance.

KRA is divided into regions such as North Region, Rift Valley Region, Western Region, Southern Region and Central Region and departments such as Customs Services Department, Domestic Services Department, Road Transport Department and Support Services Department. KRA administers different types of taxes under different Laws (Acts) such as Income Tax, Value Added Tax, Custom duties and Excise Tax among many others. Hence, KRA is supposed to ensure taxpayers comply with the respective tax laws.

Integrated tax system is enforced on taxpayers who are unwilling to pay their taxes through the threat and application of audit and fine (Kirchler, 2007). In its submission, Organization for Economic Cooperation and Development (OECD, 2001) categorized tax compliance into administrative compliance and Technical compliance. Administrative compliance is made up of reporting compliance, procedural compliance and regulatory compliance and it is generally concerned with complying with the rule relating to lodging and payment of tax while
technical compliance is concerned with meeting up technical requirement of tax laws in computation of tax liability. Franzoni (2000) and Chatopadhyay and DasGupta (2002) stated that compliance with tax laws involves true reporting of the tax base; correct computation of the tax liabilities; timely filling of tax returns and timely payment of the amount due as tax. Any behavior by the taxpayer contrary to the above constitutes noncompliance.

2.4.1 On-Line Tax Filing

There are three ways to file tax, which are manual filing, on-line tax filing and two-dimensional bar code tax filing (Efebera et al., 2004; Briggs, 2008). This study focuses on integrated on-line tax filing that is defined as individual taxpayers or companies file their taxes via internet. Internet security assurance service has provided Kenyan on-line tax filing system with reasonable guarantee of secure transaction mechanisms, such as information disclosure, transaction transmission, information privacy, in order to reduce perceived risk of taxpayers’ on-line tax filing. Because governments in various countries pay high attention to the electronic services, there are many studies on on-line tax filing. For examples, Warkentin et al. (2002) discuss the factors affecting the public to use e-government services, including cultural variables, trust, perceived risk, and perceived behavioral control. However, this research is a descriptive paper which only out the theme but lack of empirical investigation on the feasibility of the research framework. Hsu and Chiu (2004) investigate the acceptance model of the public toward e-government service based on TPB. The empirical result shows that taxpayers’ continuance intention is determined by TPB factors (self-efficiency, perceived controllability) and satisfaction. In further studies, Efebera et al. (2004) employ TPB to explore the determinants of on-line tax filing which include subjective norms and legal sanctions. The contributions of this literature are to (1) increase the importance of low-income individual taxpayer in tax compliance model; (2) add vertical, horizontal and exchange equity as the new variables that affect the intensity of tax compliance. The on-line tax filing acceptance model of taxpayers can be explained effectively with the integration of TPB factors (perceived behavioral control and subjective norms)
and tax equity perceptions (horizontal, vertical and exchange equity). Fu et al. (2006) believe that the Taiwan government still needs the help of information technology in multi-aspect. They integrate partial TPB factors and partial TAM factors to investigate the determinants affecting taxpayers on the choice of tax filing methods. Empirical results show that perceived usefulness is one of the TAM factors affected on-line taxes filing intention; while subjective norms and self-efficacy are the TPB factors affected on-line tax filing intention.

2.4.2 Rationalizing Tax Exemptions

There is an array of tax exemptions given by GoK. The more prominent ones are around the EPZ, once-off capital investment deductions, the 150% capital deduction, exemptions given on withholding tax, and the zero rating of VAT payable for goods and services procured by public bodies, privileged persons etc. Many research studies on tax exemptions and incentives confirm the conclusions of a 2008 IMF assessment of the investment incentive regimes offered in Kenya and Tanzania, that these are not important in attracting foreign investment. Rather such incentives create distortions and result in the loss of tax revenues. In addition, the socio-economic rationale for VAT zero rating is questioned in that in most instances, it does not result in lowering consumer prices for the targeted beneficiaries. In the latter perspective, it has been argued that zero rating of local products may benefit business people as windfall profits. Nonetheless, it can be expected that, at least politically and diplomatically, cases of tax exemptions and incentives will arise. Therefore, a key challenge is in rationalizing them.

2.4.3 Tax Reform Objectives and Computerization

Economic growth, equitable development, and financing of an adequate level of social public expenditure for growth, while limiting budget deficits, are conditions for financial assistance usually required of developing countries’ governments by international development agencies. These conditions are usually linked with requirements to reform the developing countries’ tax policies and Tax Administration. Therefore, major tax administration/policy reform objectives often define the overall context of many modernization projects funded by international development agencies. Such objectives expressed in various ways on
different projects): Broaden the tax base, Strengthen the organization and its management, Control tax evasion, Improve tax collections, Facilitate voluntary compliance for taxpayers. In modern reality, attainment of each of the reform objectives is inextricably dependent on the successful design and implementation of computerized, integrated tax information systems.

2.5. Conclusion
The literature review has provided a clear indication regarding the effect of tax reforms on financial performance of real estate firms. Both the theoretical literature and empirical literature have shown that tax reforms can be used to regulate the overheated real estate and monitor the effect of tax reforms on revenue growth and performance of ever-growing Kenyan real estate sector.

Since the tax is levied on property, any investment that increases the value of the property will subject it to a higher tax. For this reason, higher property taxes are expected to discourage density. If, on the other hand, higher property taxes reflect higher levels of service, it is unlikely that there would be any impact on location or land use. To the extent that the allocation of service costs is based on property values and not on services consumed, some taxpayers pay more or less for services than the benefits they receive.

Existing empirical studies were insufficient in helping to explain the corporate financing behavior of the real estate firms and a specific study on the impact of tax reforms on the financial performance of real estate firms, which is the centre of this study.
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction
In this chapter, the research methodology that was followed in the study is discussed. This includes the research design, sampling design, measuring instruments and data analysis.

3.2 Research Design
In order to determine the effect of the tax reforms to the financial performance of real estate firms, descriptive sample survey research design was used to measure the effect of tax reforms on financial performance of real estate firms. Descriptive design is preferred due to its robustness to gain more information about a particular characteristic within a particular field of study. It was used to develop theories, identify problems with current practice, justify current practice, make judgment or identify what others in similar situations may be doing. Descriptive studies are principal research tools in measuring income behavior in relation to tax changes, Odhiambo (2006)

3.3 Population
A population is a well-defined or specified set of people, group of things, households, services or events that are being investigated (Ngechu, 2004). The population for this study comprised 197 real estate firms which had been registered between 2009-2012 in Kenya, are operational and have annual turnover in excess of Kshs.500 Million.

3.4 Sample
The sampling unit for this study was derived using Systematic Sampling Method as a statistical method. This technique involves the selection of elements from a population frame. In the list of registered firms, every thirtieth real estate firm was selected for the study. According to Mugenda and Mugenda (1999), a 10% sample size from a population of 300 and above is found adequate whereas a population of less than 300 requires a sample size of 30%. Going by Mugendo’s
principle, 44 real estate firms which had been registered between 2009 and 2012 had a turnover in excess of Kes 500 Million were selected for the study.

3.5 Data Collection
The study used both primary and secondary data. The primary data was collected through administration of questionnaires distributed to senior and middle management staff of the selected real estate firms. Each of the sampled firms were issued with five sets of questionnaires; there questionnaires were issued to senior management staff and two questionnaires to middle management staff. The secondary data was be collected from KIPPRA, NSE and KNBS for the financial periods from 2009 to 2012.

3.6 Data Analysis
Both quantitative and qualitative analysis data analysis was undertaken. For the quantitative data, data capture, analysis and tabulation was conducted by use of the statistical package for social science (SPSS – 12). Percentages, means and frequency distribution tables were run to present the results. Relationships between the independent and the dependent variables were established using multiple regression analysis. This approach was critical to test the respondent’s perception on tax reforms.

3.6.1 Model Specification
The study used multiple regression model as recommended by Hair, Black, Babin, Anderson and Tatham (2006: 209). The authorities claim that stepwise multiple regressions are the best method for predicting multivariate association. The model specification is presented hereunder.

\[ \text{FPER}_i = \alpha + \beta_1 \text{TREFILING}_i + \beta_2 \text{TREFFICIENTAXS}_i + \beta_3 \text{TRTAXPROG}_i + \beta_4 \text{TRONLREG}_i + \beta_5 \text{TRREICOMRE}_i + \beta_6 \text{TRRELIEFS}_i + \beta_7 \text{TRTOTAL}_i \]

Where:
- FPERi – Financial Performance score
- TREFILING i - Tax Reforms on filing of returns
- TRINTEGRATAX i – Tax Reforms on integrated tax management system
- TRREINOME i - Tax Reforms on rental income
TRRELIEFS - Tax Reforms on reliefs
TRTOTAL - Total Reforms score
AGE - Age of the firm

The multiple regression model were used to predict the values of $\alpha_0$ and $\beta_i$, which explains the association between the independent variables and dependent variable. This method is preferred due to its predictive power of multivariate association $\beta_4$, estimated coefficient of correlation $R$. The coefficient of determination $R^2$ will be used to explain the relationship between the dependent and independent variable; the T-test to assess the significance of individual betas and standard b-coefficients were compared (beta weights) to explain the relative predictive power of independent variables and the overall model.

3.7 Data Validity and Reliability

The research instruments used were subjected to data validity and reliability tests. An instrument is considered reliable if the results of a study can be reproduced under a similar methodology. Reliability is therefore the extent to which measures yield consistent results. To be considered reliable, the measuring instrument must be free of errors and the results or observations must be replicable or repeatable (Joppe, 2000). The consistency or reliability implied in the research instrument must meet three conditions: (1) the degree to which a measurement, given repeatedly, remains the same (2) stability of a measurement over time and (3) the similarity of measurements within a given time period. Reliability of a measuring instrument is established by determining the association between the scores obtained from different administrations of the instrument. An instrument is considered reliable if the degree of association is high.

Validity of the measuring instrument determines whether the research truly measures that which it was intended to measure or how truthful the research results are. Validity thus involves ascertaining whether the means of measurement are accurate and whether they are actually capturing the variables, they were supposed to measure (Golafshani, 2009).
CHAPTER FOUR
DATA ANALYSIS, RESULTS AND PRESENTATION

4.1 Introduction

This chapter describes data analysis and presentation but focuses more on the results of the study. The chapter is divided into four main sections; introduction, descriptive statistics; analysis and results and interpretation of findings. The analysis section has four parts. Part 1 examines the level of taxpayers’ knowledge about tax reforms while part 2 looks at the relationships between tax knowledge on reforms and the financial performance. Part 3 looks at the effects of tax reform factors on the financial performance behavior of real estate firms while part 5 identifies determinants of financial performance with control variables. The data was collected from the field using structured questionnaires.

4.1.1 Response Rate

The study achieved an effective response rate of 77.5%; implying that 34 out of the sampled 44 real estate firms responded to the by returning completed questionnaires. This response rate is quite commendable given the hostility and jittery reactions associated with most studies dealing with taxation issues especially on tax reforms.

4.2 Descriptive Statistics

This section describes the demographics and other characteristics of taxpayers. Specifically, the section examines some demographic and tax reform variables which from the literature review were found to have influencing effect on the behavior of taxpayers. They include rental income, E-filing and reforms on reliefs, among others. The probability of filing returns on-line was tested using T-tests and Analysis of Variance technique (ANOVA). Tables 4.2.1, 4.2.2, 4.2.3 and 4.2.4 present some of the key results from the analysis which is closely linked to the objective of the study.
Table 4.2.1 Mean difference between variables (t-test)-A5 (Frequency of Filling Tax Returns)

<table>
<thead>
<tr>
<th></th>
<th>A</th>
<th>MEAN OF FINANCIAL PERFORMANCE VARIABLES</th>
<th>SD</th>
<th>t</th>
</tr>
</thead>
<tbody>
<tr>
<td>B1</td>
<td>Yes</td>
<td>18.76</td>
<td>5.45</td>
<td>5.45</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>17.63</td>
<td>5.58</td>
<td></td>
</tr>
<tr>
<td>B2</td>
<td>Yes</td>
<td>5.91</td>
<td>2.68</td>
<td>9.40</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>6.56</td>
<td>2.70</td>
<td></td>
</tr>
<tr>
<td>B3</td>
<td>Yes</td>
<td>27.49</td>
<td>5.15</td>
<td>8.338</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>26.30</td>
<td>5.14</td>
<td></td>
</tr>
<tr>
<td>B4</td>
<td>Yes</td>
<td>18.76</td>
<td>5.45</td>
<td>6.491</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>17.63</td>
<td>5.58</td>
<td></td>
</tr>
<tr>
<td>B5</td>
<td>Yes</td>
<td>32.46</td>
<td>5.91</td>
<td>.743</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>32.01</td>
<td>6.32</td>
<td></td>
</tr>
<tr>
<td>B6</td>
<td>Yes</td>
<td>18.13</td>
<td>5.63</td>
<td>.987</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>18.56</td>
<td>5.34</td>
<td></td>
</tr>
</tbody>
</table>

**Source: Research Findings**

Real estate firms which had filed tax returns had a mean of 18.76 (SD=5.45) compared to those which had not with a mean of 17.63 (SD=5.8). Similarly, the two groups had significant mean differences with respect to their frequency of filling returns particularly B2 and B6 with t=9.40 and .987 respectively (p<0.01).
Table 4.2.2: Mean difference between variables (t-test) – A15 Implementation of Tax Reforms

<table>
<thead>
<tr>
<th>A</th>
<th>MEAN OF FINANCIAL PERFORMANCE VARIABLES</th>
<th>SD</th>
<th>f</th>
</tr>
</thead>
<tbody>
<tr>
<td>B1</td>
<td>Yes</td>
<td>25.45</td>
<td>6.73</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>26.56</td>
<td>5.08</td>
</tr>
<tr>
<td>B2</td>
<td>Yes</td>
<td>6.97</td>
<td>2.47</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>6.42</td>
<td>2.71</td>
</tr>
<tr>
<td>B3</td>
<td>Yes</td>
<td>34.58</td>
<td>17.63</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>30.97</td>
<td>16.89</td>
</tr>
<tr>
<td>B4</td>
<td>Yes</td>
<td>17.72</td>
<td>4.97</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>17.82</td>
<td>5.59</td>
</tr>
<tr>
<td>B5</td>
<td>Yes</td>
<td>24.65</td>
<td>5.34</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>22.65</td>
<td>6.23</td>
</tr>
<tr>
<td>B6</td>
<td>Yes</td>
<td>18.94</td>
<td>5.81</td>
</tr>
<tr>
<td></td>
<td>No</td>
<td>18.42</td>
<td>5.36</td>
</tr>
</tbody>
</table>

Source: Research Findings

Table 4.2.2 presents the results of the regression analysis by examining the relationship between experience of implementing the tax reforms implemented by KRA and financial performance of real estate firms. From the table, it emerges that there was no significant mean difference between the firms that had experience of implementing tax reforms and those that had not with regard to their financial performance (A6:B1). However, there was significant mean differences between experienced and non-experienced taxpayers (A6:B5 and A6:B6) in regard to implementation of tax reforms as evidenced by (B5) with $t = 6.168$ ($p < 0.01$) and $0.325$ ($p<0.10$) respectively.
Table 4.2.3 Stepwise Multiple Regression-Tax Reforms and Financial Performance

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>t</th>
<th>Significance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>49.060</td>
<td>17.531</td>
<td>.000</td>
</tr>
<tr>
<td>TREFILING(_i)</td>
<td>.413</td>
<td>5.327</td>
<td>.000</td>
</tr>
<tr>
<td>TRINCOME(_i)</td>
<td>.614</td>
<td>4.750</td>
<td>.000</td>
</tr>
<tr>
<td>TRTOTAL(_i)</td>
<td>.067</td>
<td>2.510</td>
<td>.012</td>
</tr>
<tr>
<td>R</td>
<td>.36</td>
<td></td>
<td></td>
</tr>
<tr>
<td>R(^2)</td>
<td>.126</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: Research Findings*

Note:

\[ FPER_i = \alpha + \beta_1 TREFIL\_i + \beta_2 TRINCOME\_i + \beta_3 TRTOTAL\_i + \]

Where:

- FPER\(_i\) – Financial Performance score
- TREFILING\(_i\) - Tax Reforms on filing of returns
- TRINTEGRATAX\(_i\) – Tax Reforms on integrated tax management system
- TRREINCOME\(_i\) - Tax Reforms on rental income
- TRRELIEFS\(_i\) - Tax Reforms on reliefs
- TRTOTAL\(_i\) - Total Reforms score
- AGE- Age of the firm

The results from stepwise multiple regression show that real estate firms’ experience in filling of returns and implementation of tax reforms on rental income appears to be significantly correlated with financial performance (PER\(_i\)). This evidence becomes more vivid when we examine the t statistics for the constant and the four independent variables presented in tables 4.2.1 through 4.2.3. The estimated coefficient for constants B1, B2, B6 and B7 are found to be statistically significant at 1% level (as \( p \) value < 0.01). Further, all the variables present a positive effect on the financial performance. The estimator on coefficient of correlation (\( R = 0.36 \)) shows a fairly reasonable linear correlation between tax reforms and financial performance.
Table 4.2.4 Regressions Results and Analysis

<table>
<thead>
<tr>
<th></th>
<th>Coefficient</th>
<th>t</th>
<th>Significance</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>20.773</td>
<td>9.979</td>
<td>.000</td>
</tr>
<tr>
<td>FILLING OF RETURNS</td>
<td>-.247</td>
<td>-5.131</td>
<td>.000</td>
</tr>
<tr>
<td>INTEGRATED TAX SYSTEM</td>
<td>.090</td>
<td>1.923</td>
<td>.055</td>
</tr>
<tr>
<td>RENTAL INCOME</td>
<td>.049</td>
<td>.773</td>
<td>.439</td>
</tr>
<tr>
<td>TAX RELIEFS</td>
<td>-.042</td>
<td>-.897</td>
<td>.370</td>
</tr>
<tr>
<td>IMPLEMENTATION OF REFORMS</td>
<td>-.279</td>
<td>-5.136</td>
<td>.000</td>
</tr>
<tr>
<td>AGE OF THE FIRM</td>
<td>.030</td>
<td>.479</td>
<td>.632</td>
</tr>
<tr>
<td>TNTOTAL</td>
<td>-.008</td>
<td>-.963</td>
<td>.336</td>
</tr>
<tr>
<td>TURNOVER</td>
<td>.581</td>
<td>4.020</td>
<td>.000</td>
</tr>
<tr>
<td>KNOWLEDGE ABOUT REFORMS</td>
<td>-.012</td>
<td>-.093</td>
<td>.926</td>
</tr>
</tbody>
</table>

Model fit:

- \( R = .504 \)
- \( R^2 = .254 \)
- Std. error = 4.052
- F statistic = 23.06

Source: Research Findings

\[
FPER_i = 20.7733 + 0.247(FILREURNS) + 0.090(INTEGRATEDTAX) + 0.049(RENTALINCOME) \\
+ 0.042(TAXRELIEFS) + 0.279(IMPLEMENTATION) + 0.030(AGE) + 1.208(IMPLEM) + 0.581(TURNOVER)
\]
Table 4.2.4 summarizes the results of the supplementary regression analysis model which incorporates several control variables. The results of the analysis show that the model is significant at p < 0.01 level (F statistic 23.06) while the R is estimated at .504. IMPLEMENTATION OF TAX REFORMS, FILLING OF RETURN, and TAX RELIES appear to be the key determinants influencing financial performance. The supplementary regression model further suggest that IMPLEMENTATION OF TAX REFORMS remain the most single important determinant influencing tax compliance (r= −.279) while FILING and RELIEFS follow closely as the second most important determinants of financial performance (p<0.01).

Regarding the significance of the control variables, the results show that RENRAL INCOME and INTEGRATED TAX SYSTEM appear to be significantly and positively correlated with tax financial performance. Similarly, the association between TURNOVER and TAX FINANCIAL PERFORMANCE (FPERi) was positive and significant (p<0.001). Similarly, the association between TURNOVER and TAX FINANCIAL PERFORMANCE (FPERi) was positive and significant (p<0.001), implying that higher income is significantly associated with more financial performance. The association between AGE and FPERi was also positive and significant (p<0.001). However, KNOWLEDGE was found to have had no significant association with financial performance (FPERi).

4.4 Interpretation of the Findings

In summary, this study established that implementation of reforms is an important determinant of financial performance among the real estate firms. With regard to the significance of control variables, the results from the analysis show that TURNOVER and KNOWLEDGE about tax reforms appear to be significantly correlated with financial performance. Specifically, the association between TURNOVER and FPERi was significant but negative (p<0.001).
Similarly, the association between KNOWLEDGE about reforms and FPERi was negative and significant (p<0.001), thus supporting the hypothesis that knowledge on tax reforms is significantly less important in influencing financial performance. Other control variables examined, namely; AGE, RELIEFS and RENTAL INCOME were found to have no significant association with FPERi.

TNTOTAL becomes out as the main determinant with Beta coefficient of .254, followed by TAX REFORMS (β = -.106). The results further suggest that TURNOVER had a significant impact on financial performance; the filling the gap as suggested by several scalars. This study suggested that KNOWLEDGE ABOUT TAX REFORMS, TURNOVER, RENTAL INCOME, TAX RELIEFS AND TAX REFORMS IMPLEMENTATION appears to be significantly correlated with financial performance behavior, thus rejecting the null hypothesis. These results point demonstrate that real estate firms with higher implementation rates of tax reforms potentially tend to improve their financial performance.

The $F$ statistic ($F= 37.82, p = 0.000$) was substantiated at 1% significance level, implying that the null hypothesis that regression coefficients were all zeros can be rejected at 1% level of significance. Thus the estimated regression was efficient for prediction.

Real estate firms that have implemented tax reforms would ordinarily be expected to report better financial performance in comparison with those firms that have not. However, in a new Kenya in which tax laws and regulations keep on changing, tax reforms during the previous one to two years might not be as effective as new regulations are brought into place i.e. Tax knowledge is likely to be rendered on only limited use and within fairly short periods. This may not be true for all types of tax reforms. For example, those reforms aimed at general tax knowledge have proven that implementing tax reforms significantly increases financial performance. But central to this study is the need to determine if TAX KNOWLEDGE increases financial performance behavior. Real estate firms who have never implemented tax reforms might
attempt to misreport their actual income and make false deductions. The acts of transparency and the facilitation of communication to the taxpayer is bound to increase compliance.

Efficient tax reforms and systems have been shown to have positive relationship with the financial performance. Hence, the introduction of tax reforms will improve the tax administration efficiency rates. This claim has been advance by different authors. Competing explanations to the various arguments have also been shown. It was however, not possible to confirm the relationship between real estate financial performance and some of the prepositions because of lack of relevant comparative data from other groupings of real estate firms. Future work should attempt to explore the linkages between transparency, communication, and performance in more depth and by use of different techniques.

From the empirical results of the literature review, we find evidence of the explanatory power of the changed tax legislation on REIT's return which has never been explored by the previous researchers. Comparing the various methods, we find that the method used to overcome the shortcomings of event study method has the power to control for non-tax factors, such as the flow of global fund. This notwithstanding, the Global Fund Flow Model is suitable for capturing the exact effects of tax reform on REITs than the event study method.

Using the event method, we document the exact market effects of REITs on the tax reforms. However, in this study, we have not analyzed the effects of each tax reform. Limited by the data availability, the effects due to changes in corporation tax, dividend tax, relaxation of regulatory requirements and investment restrictions have not been separately explored. Further research could examine them in the future.
CHAPTER FIVE
SUMMARY, CONCLUSION AND RECOMENDATION

5.1 Summary
The study examines the effects of tax reforms on real estate financial performance. Although the study finds underpinning issues pertaining to the implementation of tax reforms especially from taxpayer’s perspectives, the study also tried to establish how tax reforms could enhance tax collection, efficiency and optimal employment of human resource in assessing tax returns. The effects of tax reforms on financial performance in relation to key factors affecting the real estate firms were measured through the use of structured questionnaire while regression analysis model was used to analyze the data.

Arising from the study, it was established that the authority to determine tax system lies with the tax administrators and thus taxpayers ultimately have to comply with any system that is introduced, even when they perceive the system as unfair. However, as financial performance is not an absolute, the level of financial performance will vary based on a variety of factors. Equally, the levels may change from year to year as the tax reforms changes. Managing the levels of financial performance in the face of tax reforms are therefore key challenges that the real estate firms have to resolve. It was further established that the main factors that affect the financial performance of real estate firms are hinged on how the firms implement the tax reforms and how to make the taxpayer be aware of the new tax reforms and attendant legislations. The study further found out that among other key factors that have been documented by previous researchers as significant in affecting financial performance are turnover and level of implementation.

The study finds significant mean differences between experienced and non-experienced taxpayers in relation to implementation of tax reforms. The study further finds significant mean differences between the real estate firms which had prior experience in filing returns on-line compared to those which had not. These findings have both policy and reform significance which the tax regimes could use to inform the scope of tax administration.
5.2 Conclusion

This study breaks new ground in answering the important research question of what the tax administration in Kenya can do to foster better tax reforms. The study found that knowledge on tax reforms is an important determinant in influencing financial performance of modern real estate firms. This finding reaffirms earlier research empirical findings that greater tax reforms knowledge have positive impact on financial performance on real estate firms according and could be an important input, particularly to the KRA, designing future tax reforms geared towards enhancement of tax collection and achievement of real estate firm’s financial performance targets.

It can be concluded that increase in turnover, encouragement of tax reforms implementation and expansion of knowledge on tax reforms are key drivers for enhancement of financial performance of real estate firms. However, one of the main barriers the study found in implementing tax reforms is voluntary compliance with tax reforms as it involves an array of other intervening factors ranging from knowledge about tax reforms through accurate filling of tax returns to attitude and the taxpayer’s perceptions of fairness of the system. These are key challenges that tax reform administrators need to ponder through as they develop new strategies to enhance voluntary compliance.

To deepen the understanding of the issues, the following underpinning questions need to be addressed in future research work: what are the constraining factors that make taxpayers less knowledgeable about tax reforms? Do the various tax reform changes – ranging from actual mechanics in filing tax returns through assessment to actual administration encourage and/or influence their behavior?

Further, whereas, Real estate firms that have prior knowledge and experience in implementing tax reforms are expected to report significant improvement in their financial performance in comparison with real estate firms that have never implemented tax reforms, this claim was not conclusively ascertained by the evidence adduced from the data gathered from the firms investigated. What could be a plausible explanation to this discrepancy? These are critical research questions that require further investigation.
5.3 Policy Recommendation

The primary goal of revenue authority is to collect taxes and duties payable in accordance with the law and to do this in such a manner as to instill confidence in the tax system and its administration. The action of taxpayers whether due to ignorance, deliberate evasion or weaknesses in the tax administration means that failure rate to comply with the law is inevitable. To curb this, tax administration should have in place strategies, structures and systems that ensure that non-compliance with new tax reforms laws and systems is kept to minimum. An important ingredient in the development and implementation of a computer-assisted tax administration program is that it must be well balanced. It should include a good mix of both proactive and reactive systems as well as approaches that cover all aspects of tax reforms management from education through enforcement to prosecution. For the future, revenue authority needs to develop strategies to measure trends in taxpayer compliance in order to measure their overall effectiveness.

Tax reform laws by their very nature are subject to frequent reviews through introducing new ones or amendments to existing ones. At the end of every financial year, the cabinet secretary responsible to table annual budget speech introduces new systems, laws, amendments or even cancels existing ones. These frequent changes do create confusion in the minds of taxpayers as it requires them to keep track of both existing and emerging reforms in the tax system. After a few years, these changes and amendments become so many that the taxpayer find it difficult to know which reforms are in force and the system to follow. In this regard, there is need for the tax administration to undertake periodic consolidation of the enforceable tax reforms. Equally, the tax administration could have all the changes compiled into one system which both tax taxpayers and tax administration can access and implement with ease.

Tax reforms system should be designed in such a manner as to leave economic behavior unaffected. Such a policy measure will minimize efficiency losses associated with any new reform system. In addition, it should not only avoid economic behavior distortion but should also yield sufficient revenues to fund socially useful expenditure without creating substantial inequity. It is recommended that revenue authority should implement tax system that is neutral that minimizes discrimination in terms of its application of tax rate.
5.4 Limitations of the Study

It is acknowledged that this study has a number of limitations. First, questions regarding tax knowledge as well as the scope of questions asked in the questionnaire were only limited and applicable to those sections of Income Tax Act (CAP. 470 which cover some levels of tax knowledge. As a result, the researcher was unable to determine the effects of tax reforms in all the relevant statutes as stipulated in the act. Taking that route would have been time consuming, made the questionnaire lengthy, created respondents fatigue and seriously compromised on the effective response rates.

Secondly, the use of a survey questionnaire, though most appropriate under the circumstances, was apparently less reliable, especially when the information sought on tax is of sensitive nature and potentially incriminating or embarrassing. As a result, the actual behavior of the respondents may vary from the responses given. This notwithstanding, it is still believed that use of a survey questionnaire was the most suitable approach to solicit reasonable responses or predict taxpayers’ awareness about tax reforms as direct questions (face to face) would have led respondents to answer the questions dishonestly and could even be potentially embarrassing.

Financial performance determinants such as inflation, marginal tax rates, market competition and culture could have improved the spread and reliability of the empirical results and further reduce measurement error. This study was unable to include those variables due to their intrinsic nature and requirement to apply other measurements to test their multi-collinearity.

The more robust approaches recommended for measuring tax reforms and their effects on financial performance (i.e. by using a survey instrument) might have called for different research designs and hence produce results that are slightly different from those obtained through use of interviews or experiment. Comparability of these research findings should take into account the differences research design and the limitation stated.
5.5 Suggestions for Further Studies

The area of tax education related to tax reforms knowledge and levels of financial performance offers opportunities for additional research. Instead of using a survey, other methods of data collection i.e. interviews may provide different results. It is expected that two-way communication via an interview could produce other meaningful results; however, non-anonymous methods such as interviews can be problematic in revealing the truth, especially when questioning respondents regarding tax reforms matters, as failure to appropriately address the questions would harm or embarrass respondents.

Other determinants which were not tested in this study such as political affiliation real estate firms, cultural influence and religiosity could also be explored in the future. This study was unable to include these variables because these variables require a series of questions in order to be accurately measured, hence these factors were excluded from this questionnaire but could be included in future studies to examine their impact on the explanatory power of the models used.

Further study should also be undertaken on tax legislation reforms as an environmental base for strategic position taken to generate funds, and at the same time manipulate social as well as political demands of the nation.

There is need to conduct more research, by the tax administration and other researchers on the suitability of various taxes, tax law and enforcement activities as well as the tax amnesties and quality services to be able to conclusively determine their role in enhancement of financial performance of real estate firms which pay taxes co. A comprehensive study of small, medium and large taxpayers from all sectors will also give more insight into this subject.
REFERENCES


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Kirk, A. M. (1986) Understanding Data Reliability and validity in qualitative research; vol.8 pp.598


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APPENDIX I
LIST OF REAL ESTATE FIRMS IN KENYA

1. Knight Frank
2. Suraya Property Group
3. Cfc Properties
4. Chagwel Ltd
5. Housing Finance
6. Ryden International
7. Global Properties
8. Halifax Ltd
9. Centro Ltd
10. Devine Management
11. Equity Trustees Ltd
12. Flexi Property Trust
13. Florest Place
14. Hudson Investments
15. Bunning Warehouses
16. Carrigdale Property Ltd
17. Ceder Woods Property Ltd
18. Land Lease Corp Ltd
19. Property Leo Ltd
20. Daebak Trust
21. Euro Trust
22. Easy Ltd
23. Macquarie Leisure
24. Grand Group
25. National Housing
26. Investments And Mortgage
27. Abigroup Ltt
28. Savings And Loans
<table>
<thead>
<tr>
<th>No.</th>
<th>Company Name</th>
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<tr>
<td>29</td>
<td>Ozzbeco K Ltd</td>
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<td>30</td>
<td>Menzola Ltd</td>
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<td>31</td>
<td>Quabic Group</td>
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<td>32</td>
<td>Amazon Property Management</td>
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<td>33</td>
<td>33 Van Rees B V</td>
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<td>34</td>
<td>34 Diamond Properties</td>
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<td>35</td>
<td>35 Investments And Morhgage</td>
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<td>36</td>
<td>Dunhill Investments</td>
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<td>37</td>
<td>Hass Consultants</td>
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<td>38</td>
<td>Regent Investments</td>
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<td>39</td>
<td>Westmond Property Investment</td>
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<td>40</td>
<td>Standard Investments Ltd</td>
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<td>41</td>
<td>Britam Investments</td>
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<td>42</td>
<td>Dancourt Investments</td>
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<td>43</td>
<td>Jamco General Merchants</td>
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<td>44</td>
<td>Jamlands Commercial Agencies</td>
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<td>45</td>
<td>Jawamu Estate And Property Managers</td>
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<td>46</td>
<td>Jem Properties</td>
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<td>47</td>
<td>Jimly Properties Limited</td>
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<td>48</td>
<td>Jiwa Properties</td>
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<td>49</td>
<td>Joe Musyoki Consultants Limited</td>
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<td>50</td>
<td>Jomwan Commercial Agencies</td>
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<td>Josannah Properties Ltd</td>
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<td>Joski Plant Management</td>
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<td>Josmarg Agencies Ltd</td>
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<td>Josmos Commercial Agencies</td>
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<td>Jospak Investment Limited</td>
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<td>Josuma Enterprises</td>
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<td>57</td>
<td>Justland Properties</td>
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<td>58</td>
<td>Kambaa Commercial Agencies</td>
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<td>59</td>
<td>Kangei &amp; Nyakinyua Building Co. Limited</td>
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<td>60</td>
<td>Kauti Investments Limited</td>
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<td>61</td>
<td>Kenval Realtors(Ea)Limited</td>
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<td>62</td>
<td>Kenya Industrial Property</td>
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<td>63</td>
<td>Kenyatu Trading Companylimited</td>
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<td>64</td>
<td>Kogo Holdings Limited</td>
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<td>Kuria Holdings Limited</td>
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<td>66</td>
<td>Kwoba Commercial Agencies</td>
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<td>67</td>
<td>L.P.Holdings Ltd</td>
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<td>68</td>
<td>Landmark Consultants</td>
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<td>Landvalue Ltd</td>
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<td>Landview Management Ltd</td>
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<td>71</td>
<td>Langata Link Limited</td>
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<td>72</td>
<td>Laxmi Plaza Ltd</td>
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<td>73</td>
<td>Liberty Real Estate Ltd</td>
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<td>74</td>
<td>Lorian Developers Limited</td>
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<td>75</td>
<td>Lustman &amp; Company(1990)Ltd</td>
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<td>76</td>
<td>Maestro Properties Limited</td>
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<td>Maisha Boro Development Co. Ltd</td>
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<td>Mak Property Company</td>
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<td>Makye Investments</td>
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<td>Malindi Homes &amp;Properties</td>
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<td>Ncm House</td>
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<td>82</td>
<td>Neat Properties Ltd</td>
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<td>Nenyon Co Ltd</td>
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<td>Neptune Shelters Limited</td>
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<td>Ngombe Holdings Company Limited</td>
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<td>Ngomongo Development Company Limited</td>
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<td>87</td>
<td>Oceanic Property Consultants Limited</td>
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<td>Opus Properties Limited</td>
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<td>89</td>
<td>P And T Employees Housing Co-Op Society Ltd</td>
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<td>Pamoja Two Agencies</td>
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</table>
91. Pan African Properties (K)Ltd
92. Paragon Property Consultant Ltd
93. Patonic Real Estate Agents
94. Relisa Housing Co-Op Society Limited
95. Resma Commercial Agencies
96. Rics Properties Ltd
97. Rinaka General Merchants
98. Rochman Investments Ltd
99. Rosewa Agencies Limited
100. Rosus Commercial Agencies Ltd
101. Royal Farm Property Consultants
102. Ryden International Limited
103. Safetycom Delivery Services Ltd
104. Sam Company Ltd
105. Samiyan Shelters Enterprise
106. Yaya Towers Ltd
107. Young Trader Limited
108. Dunhill Consulting Ltd
109. Llyod Masika
110. Hillside Homes Ltd
111. Guardian Properties Ltd
112. Yamarin Group Ltd
113. Prolines Investment
114. Landmark Realtors Ltd
115. Cornerstone Real Estate Ltd
116. Bishop's House Marsabit
117. Kavia Contractors
118. Nduati Wamae And Associates Co. Ltd
119. Prestige Management Valuers
120. Lavender Properties Ltd
121. Kenbanco House Ltd
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<td>Langata Development Co. Ltd</td>
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<td>126</td>
<td>Idime Enterprises Limited</td>
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<td>Texcac House Service Station</td>
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<td>Nairobi Homes Msa Limited</td>
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<td>Embu Gatuuri Housing Co-Op Soc Limited</td>
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<td>Adn Advisory Valuers</td>
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<td>Wakasha Enterprise</td>
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<td>Ebony Estates Ltd</td>
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<td>Afridawa Holdings Ltd</td>
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<td>148</td>
<td>Kamuthi Farmers Co-Operative Society Ltd</td>
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<td>149</td>
<td>Value Consult Limited</td>
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<td>150</td>
<td>Gimco Limited</td>
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<td>151</td>
<td>Mavueni Enterprises</td>
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<td>152</td>
<td>Focus Management Limited</td>
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</table>
153. Kuki Properties
154. Datoo Kithii Limited
155. Fedha Plaza Ltd
156. Philda Agencies Ltd
157. Knight Frank Ukay Centre
APPENDIX II

LETTER OF INTRODUCTION

Georgeena Kanini Kimeu

P.O.Box 703-00100,

Nairobi.

To: __________________________

___________________________

___________________________

Dear Sir/Madam,

RE: INTRODUCTION LETTER FOR MRS. GEORGEENA AKANINI KIMEU

I’m an MBA student in the School of Business, University of Nairobi. In partial fulfillment of the requirements of the degree of Master of Business Administration (MBA), I’m conducting an academic research project titled the “The Effect of Tax Reforms on Real Estate Financial Performance”.

Your participation in this exercise will be highly appreciated as an integral part of this study, hence the request for your assistance to fill out this questionnaire.

The results of this research are for educational purposes only and will be treated with utmost confidentiality.

Thank you in advance for your cooperation.

GEORGEENA KANINI KIMEU
APENDIX III: QUESTIONNARE

Section A: General (please tick [ ] where appropriate.

1. Confirm the position you hold in the organization?
   
   1. Managing Director [ ]
   2. Accountant [ ]
   3. Public Relations Officer [ ]
   4. Others. [ ]
   
   (Specify)…………………………………………………

2. For how long has your business been in existence?
   
   1. 2 years and below [ ]
   2. 3-4 years [ ]
   3. 5-6 years [ ]
   4. Over 6 years [ ]

3. Which Town is your firm operating?
   
   1. Nairobi [ ]
   2. Mombasa [ ]
   3. Kisumu [ ]
   4. All over Kenya [ ]
4. What is the nature of your business?

1. Construction [    ]
2. Property Agent [    ]
3. Mortgage financing [    ]
4. Others [    ]

(Specify)……………………………………………….

SECTION B (TAX REFORMS AWARENESS) (Tick or circle where appropriate)


5. How often has your company submitted annual income tax returns to KRA over the past 5 years? [1] [2] [3] [4] [5]

6. How often do you think your company’s annual income?

tax returns and accounts submitted to KRA were correctly Stated in the past 5 years. [1] [2] [3] [4] [5]

7. How often did the company pay annual real estate income tax?

Liabilities over the past 5 years to KRA by the due date? [1] [2] [3] [4] [5]

Please state your opinion for each given statements using the following scale
1. Strongly disagree
2. Disagree
3. Not certain
4. Agree
5. Strongly agree

I wish **TO COMPLY** with tax reforms for the following reasons

<table>
<thead>
<tr>
<th></th>
<th>Tax reforms has improved your ways of doing business in the real estate business</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
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<td>9.</td>
<td>I believe the tax reforms has improved the efficiency in reporting your annual income</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
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<td>10.</td>
<td>I believe that the tax reforms has double your turnover over the last three years</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
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<tr>
<td>11.</td>
<td>I pay all the taxes included in the real estate income</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
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<tr>
<td>12.</td>
<td>All tax requirements are taken into consideration while computing the cost of real estate revenue generation</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
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<tr>
<td>13.</td>
<td>The tax reform is easy and simple to implement in the real estate business</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
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</table>
SECTION (C) TAX REFORMS EFFICIENCY

15. Have you ever used ‘implemented all tax reforms in your business?’

Yes ☐ No ☐

16. How can you assess the overall performance of Tax reforms in the real estate firms?
Excellent [ ] Very Good [ ] Fair [ ] Poor [ ]