Trust In Government Institutions And Tax Compliance
The Case Of Uganda

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Abstract
This paper discusses the relationship between Trust in Government institutions and tax compliance among Small Business Enterprises (SBEs) in Uganda. Using a survey population of Small Business Enterprises (SBEs) operating in Kampala district, Uganda, Purposive and simple random sampling methods were used to select samples used in the study. Self administered questionnaires were also used to collect data from SBEs. Data was collected from 274 respondents and was analysed using SPSS (Statistical Package for Social Scientist). The findings indicated that there is a significant relationship between trust in government institutions, taxpayers’ morale and tax compliance (F = 18.696, sig = 0.000). Trust in government institutions (Beta=0.241) influences more of tax compliance than taxpayers’ morale (Beta= 0.133). This paper therefore argues that to shape desired behaviour, regulators need to put in place deliberate strategies aimed at improving trust, and this would yield high levels of Tax Compliance among SBEs in Uganda

Key words; Trust, Taxpayers’ Morale, Tax compliance

1.0 Background to the Study

Tax compliance is an important factor for guaranteeing an adequate provision of public goods. Especially in times when the costs of running public office have strongly increased, governments search for strategies to generate revenues (Torgler, 2003). A high degree of tax evasion creates misallocations in resource use (Alm & Vazquez 2001). Trust in government institutions (Beta=0.241) influences more of tax compliance than taxpayers’ morale (Beta= 0.133). This paper therefore argues that to shape desired behaviour, regulators need to put in place deliberate strategies aimed at improving trust, and this would yield high levels of Tax Compliance among SBEs in Uganda

For many governments, managing non-compliance has become increasingly difficult over the past few decades. With the advent of globalization and the disturbing increase in individuals and corporate citizens exploiting loopholes in the law (McBarnet, 2003), the question of how regulators can best ensure voluntary compliance with the spirit of the law is important. Having an accurate understanding of why people are motivated to accept third party decisions and rules can go some way to answering this question (Murphy, 2004).

In Uganda, taxes are perceived to be unfair and people receive few tangible benefits in return for taxes paid (Fjeldstad & Semboja, 2001). In such circumstances only coercive methods of tax enforcement can generate revenues. Indeed, in Uganda, the government has established special military units to collect taxes and fight smuggling (Kasimbazi, 2003).

However, several researchers argue that tax compliance cannot be attained entirely by levels of enforcement (Alm, Sanchez, & De Juan 1995; Elffers 1991, 2000; Frey 1997; Graetz & Wilde 1985;
Torgler 2002). In the face of these difficulties, researchers have suggested other factors that need to be analyzed. It is plausible that tax compliance is affected by other factors such as government services, trust in government institutions, perception of others’ tax compliance, social norms among others

Trust in government institutions according to Levi & Stoker (2000) as drawn from Listhaug (1990), is defined to reflect evaluations of whether or not political authorities and institutions are performing in accordance with normative expectations held by the public. Citizen expectations…include…that it be fair, equitable, honest, efficient, and responsive to society’s needs… an expression of trust in government…is a summary judgment that the system is responsive and will do what is right even in the absence of constant scrutiny.

In the absence of a clear-cut line separating tax compliance from tax evasion a prudent treatment of the taxpayer may be a wise move in preserving voluntary compliance and citizens’ opinions of legitimacy of the tax system. Punishing a citizen because he has made a mistake in complying with their taxes or took advantage of some loophole in the tax law may be excessive and even counterproductive for future tax compliance as it may undermine the legitimacy of the tax administration’s action to the eyes of the public (Leonardo, 2008).

This therefore has prompted the researcher to investigate whether there is a relationship between trust in government institutions and tax compliance in Uganda.

2.0 Literature Review
2.1 Trust in Government institutions
According to Leonardo (2008) government institutions are not limited to the ones that traditionally form the three powers of the state -Executive, Legislature, Justice/Courts. Among those we can cite the state’s bureaucracy-the civil service- which runs several organizations responsible for delivering public services such as education, health care, pensions, and the tax administration (to cite some of the most representative). Besides the bureaucracy, we have the organizations responsible for maintaining internal order -the police, and the external integrity of the country -the armed forces. Each of those government institutions has distinct functions and responsibilities. According to Leonardo (2008) still, he posits that their specialized roles make them producing actions of a different kind; consequently, he hypothesize that different actions will have different impacts on a citizen’s opinion about the trustworthiness of government institutions.

In addition, trust in government institutions according to Levi & Stoker (2000) as drawn from Listhaug (1990), is defined to reflect evaluations of whether or not political authorities and institutions are performing in accordance with normative expectations held by the public. Citizen expectations…include…that it be fair, equitable, honest, efficient, and responsive to society’s needs… an expression of trust in government…is a summary judgment that the system is responsive and will do what is right even in the absence of constant scrutiny.

Leonardo (2008) in agreement highlights the issue of normative expectations that citizens have regarding government institutions behavior as they expect those organizations to be fair, equitable, and honest among other attributes as it points out in the direction of the actions that would elicit or undermine citizens’ trust in government.

However Gambetta (2000) defined trust as, “trust is a particular level of the subjective probability by which an agent assesses that another agent or group of agents will perform a particular action, both before(emphasis in original) he can monitor such an action (or independently of his capacity ever to be able to monitor it) and (emphasis in original) in a context in which it affects his own(emphasis in original) action… when we say we trust someone or that someone is trustworthy, we implicitly mean that the probability that he will perform an action that is beneficial or at least not detrimental to us is high enough for us to consider engaging in some form of cooperation with him. Correspondingly,
when we say that someone is untrustworthy, we imply that that probability is low enough for us to refrain from doing so.”

Leonardo (2008) adds that several things can be highlighted. First, individuals form expectations regarding other individuals or organizations’ expected behavior that will make them either cooperate (if they trust) or refrain from cooperating (if they distrust). Second, those expectations are driven by assessment of the potential actions that others may take and ruling out that the occurrence of those that would be detrimental of citizens’ well-being. Third, the expectation (trust) is formed before having the possibility of monitoring the other’s actions or, more important still, despite the impossibility of ever monitoring such actions –the “normative expectations” concept of Listhaug (1990) is relevant because it provides a benchmark for evaluating the other’s performance.

Finally, trusting an individual or institution paves the way for cooperation with such entity; conversely, mistrust refrain individuals from engaging in cooperation. Given the fact that the traditional model of tax compliance failed in explaining the observed levels of compliance –far higher than predicted in theory- then it may be said that trust in government may induce citizens into holding a predisposition to cooperate with the government exhibiting a higher Tax Morale (Leonardo, 2008)

2.2 Tax Morale

“Tax morale is the individuals’ willingness to pay taxes or, in other words, the moral obligation to pay taxes or the belief in contributing to the society by paying taxes” (Frey & Torgler, 2004). It has also been argued that tax morale -defined as the intrinsic motivation an individual has to pay his/her taxes- may help explain the high degree of tax compliance observed in many countries ( Frey & Feld 2002, Feld & Tyran 2002).

This is in agreement with Cummings et al (2004) who defines tax morale as the intrinsic motivation to pay taxes. It is the individuals’ willingness to pay taxes or, in other words the moral obligation to pay taxes or the belief in contributing to the society by paying taxes.

In a broader sense a number of studies have tried to investigate attitudes towards paying taxes which can be seen as a proxy for tax morale: the intrinsic motivation to comply and pay taxes and thus voluntarily contribute to the public good (Torgler & Schneider, 1999). However, most of the attempts failed to consider how tax morale may arise or which factors have an impact on it. Thus, tax morale is used as a residuum to capture unknown influences on tax evasion (Frey & Feld, 2002).

2.3 Tax Compliance

Tax compliance typically means, true reporting of the tax base, correct computation of the liability, timely filing of the return, and timely payment of the amounts due. (Franzoni, 1999). In addition tax compliance in respect to income tax is defined as the ratio of declared income to actual income (Chang-Gyun, Hyun & Yoo, 2000). Tax non-compliance or evasion, on the other hand, happens when taxpayers intentionally fail to comply with their tax obligations, resulting to loss of revenue, which may cause serious damage to the proper functioning of the public sector (Franzoni, 1999).

If compliance with taxes cannot be imposed by reliance on deterrent and punishment only, then governments should do something to convince citizens to cooperate and pay their taxes. Tax compliance (cooperation) does not come from incentive manipulation alone; it requires trust (Leonardo, 2008).

2.4 Trust in Government institution, Tax Morale and Tax Compliance

Talking about the effects that trust in the political and legal system might have in shaping an individual’s tax morale, Torgler (2003) wrote, “stable and easily knowable institutions help create
reliability…trust in public officials might tend to increase taxpayers’ positive attitudes and commitment to the tax system and tax-payment, which has finally a positive effect on tax compliance…if the government acts trustworthily, taxpayers might be more willing to comply with the taxes”

More specifically, Wenzel (2002) discussed how conceptions of justice and fairness may play a role in taxpayers’ evaluations of the tax system and their willingness to comply with tax laws; if they perceive unjust and unfair treatment they may refuse to provide cooperation and paying their taxes. Therefore, according to Leonardo (2008) in the absence of a clear-cut line separating tax compliance from tax evasion a prudent treatment of the taxpayer may be a wise move in preserving voluntary compliance and citizens’ opinions of legitimacy of the tax system. Punishing a citizen because he has made a mistake in complying with their taxes or took advantage of some loophole in the tax law may be excessive and even counterproductive for future tax compliance as it may undermine the legitimacy of the tax administration’s action to the eyes of the public.

Given the fact that the traditional model of tax compliance failed in explaining the observed levels of compliance –far higher than predicted in theory- then it may be said that trust in government may induce citizens into holding a predisposition to cooperate with the government exhibiting a higher Tax Morale (Leonardo, 2008).

3.0 Methodology
A cross-sectional research design was used together with the explanatory research design and analytical research design, in order to ascertain the relationship between social norms, taxpayers’ morale and tax compliance among SBEs in Uganda.

The population consisted of SBEs operating in Kampala district estimated to be 37,500 as in the Uganda Bureau Of Statistics (UBOS) 2002. However given the fact that there are high births and deaths of SBEs in Kampala, their real current number cannot be established.

The sample size used for the study was 380 SBEs. This was based on Krejcie & Morgan (1970) table for determining the sample size where they contend that a sample size of 379 is appropriate for a population of 30,000 and 380 is appropriate for a population of 40,000 SBEs. Therefore given a population of 37,500 SBEs in Kampala district, a sample size of 380 was recommended for this study. Purposive together with simple random sampling methods were used to select a representative sample.

The main sources of data for this study included primary data obtained from respondents using self administered questionnaires as well as interview administered questionnaires, secondary data was collected from previous studies on SBEs, documents and journals and published literature. Internet libraries were also a vital source of the secondary data.

The data Collection Instruments used were self-administered, structured questionnaires. The questionnaire consisted of mainly closed questions using a 5 point–scale ranging from 1-strongly disagrees to 5-strongly agree. The questionnaires were prepared in English but translated into Luganda (local language) for non-English speaking respondents.

The reliability of the questionnaires was tested using the cronbach’s alpha coefficient. The acceptable minimum is 0.5. The reliability of the questions used in the study range from 0.710 to 0.887 which is above the acceptable minimum of 0.5. This indicates that the instrument used to collect data from the respondents was dependable and reliable and yielded good results. The results and conclusions of this study can be significant for decision making. Other researchers in future can use the instrument for data collection in the same area and/ or field of research.
The data collected was edited, coded, and analysed to identify the relationship between the independent, intervening and dependent variables. Data derived from the questionnaires was analysed using SPSS statistical package. Descriptive statistics were used to describe the data. Correlation and multiple regressions were used to show strength and nature of the relationships, predictability and variability in tax compliance.

The following were the limitations to the study; the instrument used to collect data was adopted from developed countries, which may not be appropriate for our developing country. However, the researcher explained the instrument to the respondents.

Measurement scales for variables were not easy to obtain. This was mainly because of the little research done in this area of taxation in less developed countries. However, the researcher tried to achieve reliable research measurements from literature for the study.

The study was further affected by non-response from respondents that may have viewed the required information as private. The researcher obtained a letter of introduction from the University to allay fears of the respondents and assure them that results of the study were meant for research purposes only.

4.0 Findings

4.1 Inferential Analysis
Inferential analysis was done where by correlations were obtained to establish the relationship that exists between variables conceptualized in the framework.

From the table 2 of correlation matrix it can be noted that there was a significant positive relationship between trust in government institutions and tax compliance (r=0.336, P-value <0.01). This implies that trust in government institutions have a positive influence on tax compliance. So when the trust in government institutions of the small business owners and managers change, the tax compliance will also change in the same direction.

From the table 2 of correlation matrix it can be noted that there was a significant positive relationship between trust in government institutions and taxpayers’ morale (r=0.714, P-value <0.01). This implies that trust in government institutions have a positive influence on taxpayers’ morale and therefore if trust in government institutions of small business taxpayers change, taxpayers’ morale would change as well in the same direction.

From the table 2 of correlation matrix it can be noted that there was a significant positive relationship between taxpayers’ morale and tax compliance (r=0.305, P-value <0.01). This implies that taxpayers’ morale positively influence tax compliance. This also implies that when taxpayers’ morale improves, then tax compliance would proportionately improve. Hence in the attempt to improve tax compliance, URA has to try and put in place techniques to improve taxpayers’ morale.

4.2 Multiple Regression
Regression analysis was performed to explain the variability of the relationship between trust in government institutions and taxpayers’ morale as independent variables and tax compliance as a dependent variable among small business enterprises in Uganda. Regression analysis results as shown in table 3 indicated a significant relationship between trust in government institutions, taxpayers’ morale and tax compliance (F = 18.696, sig = 0.000). Trust in government institutions and taxpayers’ morale explains only 11.5% of tax compliance. Trust in government institutions (Beta=0.241) explains/ influences more of tax compliance than taxpayers’ morale (Beta= 0.133).This implies that a 1 unit change in trust in government institutions led to 0.24
change in tax compliance and a 1 unit change in taxpayers’ morale led to 0.133 change in tax compliance.

5.0 Conclusions

The findings from the present study have shown that if taxpayers feel poorly treated by a tax authority as a result of their infractions (innocent or otherwise), this can lead to a decrease in taxpayer trust. This decrease in trust can then go on to affect their willingness to comply, and might in fact lead to active resistance towards a regulatory authority. It has been proposed here that by using a strategy based on trust, regulators may be more likely to prevent widespread resistance towards their decisions, while at the same time nurturing the good will of those with a commitment to compliance.

A significant body of research on tax compliance has been accumulated. Much work has concentrated on traditional topics, such as the impact of audit, penalty, and tax rates on compliance. However, there is overwhelming evidence that observed tax compliance behavior cannot be explained entirely with the traditional economic analysis that focuses mainly on deterrence components. Instead, there are several other factors that help explain why many people are compliant, especially the notion of trust in government institutions and tax morale. Tax compliance was found to be significantly correlated to trust in government institutions. There was also a significant correlation between trust in government institutions and taxpayers’ morale, implying that trust in government institutions together with taxpayers’ morale influence whether someone will comply or not. It can be concluded that trust in government institutions and taxpayers’ morale affect tax compliance.

6.0 Recommendations

URA should have a plan for checking and nurturing trust, which will create a conducive platform for small business enterprises taxpayer compliance. The tax assessment procedures should be improved to enhance trust of the government. The more the taxpayers feel that the government and the tax officers are not trustworthy, the more they will be tempted to evade taxes. Once URA adopts this stance, they are likely to be perceived as more accountable and trustable and the taxpaying public will most likely comply in its obligation to pay.

Areas of Further Study

It would be necessary to carry out further research that involves small business enterprises in the whole country, tax compliance and how it can be enforced and to establish all other factors that predict tax compliance. The extent to which each variable predicts tax compliance would also be established.

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Sam, C. C. S., (2005) Do Hong Kong taxpayers have stronger tax morale than mainland Chinese? Hong Kong Baptist University Hong Kong
1. Conceptual Framework

Figure 1: The following conceptual framework is used to guide the study.

Appendices

2. Reliability analysis

Table 1: Reliability Analysis

<table>
<thead>
<tr>
<th>Variable</th>
<th>Alpha cronbach’s coefficient</th>
</tr>
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<tbody>
<tr>
<td>Trust in Government Institutions</td>
<td>0.887</td>
</tr>
<tr>
<td>Taxpayers’ Morale</td>
<td>0.786</td>
</tr>
<tr>
<td>Tax Compliance</td>
<td>0.710</td>
</tr>
</tbody>
</table>

3. Findings

Table 2: Correlation Matrix

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust in Government Institutions (1)</td>
<td>1.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax Payers Morale (2)</td>
<td></td>
<td>0.714**</td>
<td>1.000</td>
</tr>
<tr>
<td>Tax Compliance (3)</td>
<td></td>
<td>0.336**</td>
<td>0.305**</td>
</tr>
</tbody>
</table>

Source: Primary data

** Correlation is significant at the .01 level (2-tailed).

Table 3: Multiple Regression Analysis

<table>
<thead>
<tr>
<th>Model</th>
<th>Standard coefficients Beta</th>
<th>t-test</th>
<th>Sig.</th>
<th>R square</th>
<th>Adj. R square</th>
<th>F</th>
<th>Sig. F</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust in government institutionsTaxpayers’ Morale</td>
<td>0.241</td>
<td>12.233</td>
<td>0.000</td>
<td>0.121</td>
<td>0.115</td>
<td>18.696</td>
<td>0.000</td>
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<td></td>
<td>0.133</td>
<td>1.631</td>
<td>0.104</td>
<td></td>
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</tr>
</tbody>
</table>

Source: Primary data