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Effects of High Taxation on SMES in Chipata District of Eastern Province

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ABSTRACT

The purpose of this research is to find out the effects caused by high taxation on the growth of small and medium enterprise in Chipata District. Over the years, small and medium enterprise have been the source of job creation and the empowerment of Zambian citizens, by providing about 50% of all jobs in Zambia. However, the mortality rate of these small firms is very high. Among the factors responsible for these untimely close-ups are tax related issues, ranging from multiple taxation to enormous tax burdens. This study seeks to analyze the effects of high taxation on the growth of small and medium enterprise in Chipata District.

The study was guided by the following specific objectives: To determine how high rates of tax affect the growth of small and medium enterprise and to ascertain how multiple taxes affect the small and medium enterprise. The aim of the study is to promote awareness of taxation by educating and enlightenment of business personnel about tax related issues.

In order to carry out the study effectively I have used a sample size of 50 small and medium enterprises. The research will be carried out in two sections. The first section will cover quantitative study. It involves deskwork, which is carried out by browsing the internet and reading books, published magazines, articles, and journals related to the project title. The second section will cover qualitative study. This involves interviewing people, making observations, asking people to fill questionnaires and group discussions. For this study to be achieved convenience sampling method was adopted to collect the sample and the analysis of data was done by descriptive research design using tables, charts, percentage calculations and other statistical tools of analysis.

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

In recent time the world economy has developed tremendously and this has been linked with activities of Small and Medium Enterprises (SMEs), especially in developing countries. Small and Mediums Enterprise plays an important role in building the economy of a country. Economic growth in every country is defined by the performance of its production sector. In many highly developed and developing countries a great share of production is manufactured by Small and Medium Enterprises (SMEs) – an important part of their market economies.

Enterprises make up to 65% of productive units of the economy (Ariyo, 2005). Although smaller in size, they are the most important enterprises in the economy due to the fact that when all the individual effects are aggregated, they surpass that of the larger companies. The social and economic advantages of Small and Medium Scale enterprises cannot be overstated. Panitchparkdi (2006) sees Small and Medium Enterprise as a source of employment, competition, economic dynamism, and innovation which stimulates the entrepreneurial spirit and the diffusion of skills. Because they enjoy a wider geographical presence than big companies, small and medium enterprise also contribute to better income distribution. Over the years, small and medium enterprise have been an avenue for job creation and the empowerment of Zambia's citizens providing about 50% of all jobs in Zambia and also for local capital formation. Being highly innovative, they lead to the utilization of our natural resources which in turn translates to increasing the country's wealth through higher productivity. Small and medium enterprises have undoubtedly improved the standard of living of so many people especially those in the rural areas (Ariyo, 2005).

However, the mortality rate of these small and medium firms is very high. Among the factors responsible for these untimely close-ups are tax related

issues, ranging from multiple taxations to enormous tax burdens among other issues etc. In many government policies, small and medium enterprises are usually viewed and treated in the same light as large corporations. However, their size and nature make them unique. Therefore, in dealing with small and medium enterprises, these unique qualities need to be considered. In levying of taxes for these enterprises in particular, issues that need to be considered are how these tax policies can be designed to bolster the growth of small and medium enterprise and the most effective ways to administer them. The importance of small and medium enterprise as a mechanism of economic growth and development is often ignored.

They are perceived as minute establishments that have minimal effect on the state of the economy. However, if favorable environment is created for these small and medium enterprise to grow through proper regulation, the small and medium enterprise sector has the highest propensity to transform our economy. In the same light, taxes are important for the government as they are the major source of funds for government expenditure. Income obtained from taxation of individuals and businesses are used to run governments as well as provide infrastructure such as good roads, water supply, and electricity which are essential for the smooth running of these businesses that are mainly manufacturing companies and as such rely on these commodities to survive.

However, Holban (2007) posited that taxation can contribute to development and welfare through three sources; It must be able to generate sufficient funds for financing public services and social transfers at a high level of quality, it should offer incentive for more employment and for an efficient and lasting use of natural resources, finally it should be able to reallocate income. But in the case of small and medium enterprise, tax must be imposed in such a way that puts their income and need for survival into consideration. It is expedient that enough profit is allowed them for the purpose of expanding their businesses. The tax policy must be one that will not encourage small and medium enterprise to remain in the informal sector or to evade or avoid tax payments. More so, many small firms in Africa, including Zambia, choose to remain in the informal sector because the perceived benefits outweigh the perceived costs. Firms rarely see their tax contributions at work and the compliance costs are high, thus discouraging compliance. The government is also discouraged from collecting taxes from small firms, because the cost of monitoring and collecting taxes from small businesses by revenue authorities, whose resources are usually scarce, sometimes outweighs the revenues generated by small businesses (Stem and Barbour 2005). The focus of this research, therefore, is to examine the effects of high taxation on the growth of small and medium enterprise in Chipata District and the importance of tax to the Zambia economy, to establish the relationship between tax policy and the growth of small and medium enterprise in Zambia

1.2 STATEMENT OF THE PROBLEM

Although there is a general perception that tax is an important source of fund for development of the economy and provision of social services, the problems faced are in the area of negative relationship between taxes and the business' ability to sustain itself and to expand. Businesses are faced with the problem of high taxation, complex tax regulations and lack of proper enlightenment or education about tax related issues. Not minding other challenges that businesses are facing in other developing countries like Zambia; inadequate capital, poor technical and managerial skills, environmental effects and government regulations which affect the operation of businesses, in Zambia especially this issue of high taxation which is a worm eating deeply and the large chunk of revenues generated by these businesses for their growth and survival. These have led to increase in record of death of businesses. The research is an attempt to find out the missing link by analyzing the effects of high taxation on the growth of small and medium enterprise in Chipata District.

1.3 OBJECTIVES OF THE STUDY

1.3.1 PRIMARY OBJECTIVE:

- The effects of high taxation on the growth of small and medium enterprise in Chipata District of Eastern Province.

1.3.2 SECONDARY OBJECTIVES:

- To determine how high rates of tax affect the growth of small and medium enterprise.
- To examine how multiple and high taxes affect the small and medium enterprise.
- To ascertain the challenges faced by small and medium enterprise when paying tax.
- To establish the types of tax that affects the growth of small and medium enterprise.
- To describe the criteria set by the Zambia Revenue Authority (ZRA) when getting tax from small and medium enterprise.

1.4 SCOPE OF THE STUDY

- The study focus on the effects of high taxation on the growth of small and medium enterprise in Chipata District Eastern Province.
- To promote awareness of taxation by educating and enlightenment of business personnel about tax related issues.

1.5 NEED OF THE STUDY

- To influence the government of Zambia through the Zambia Revenue Authority (ZRA) to come up with better rates taxes.
- The business people will learn their duties as tax payers. Taxes being one of the operational costs of business and must be paid.
- To implore the small and medium enterprise by educating them about the importance of paying taxes.
- To promote many small and medium enterprise by finding means of helping them through funds.
- The general public, they will learn that every business has to pay different forms of taxes. This is because a tax is a compulsory operational business expense. Even other researchers on this topic will use it as reference for future research.

1.6 RESEARCH QUESTIONS:

1. How do high rates of tax affect the growth of small and medium enterprise?
2. How can multiple and high taxes affect the small and medium enterprise?
3. What are the challenges faced by small and medium enterprise when paying tax?
4. What types of tax affects the growth of small and medium enterprise?
5. Which criteria did the Zambia Revenue Authority set for small and medium enterprise when paying tax?

1.7 LIMITATION OF THE STUDY:

- The executives interviewed were not willing to answer in-depth questions about their businesses. One reason for this unwilling might have been that they did not want to disclose what they considered was business-confidential information.
- The time frame given for the project was not enough therefore the study was done hastily and without proper and vast research and only selective materials where used due to the time factor i.e. journals, papers and articles.
- The problem of getting most appropriate interviewees to answer the questionnaire willingly was a challenge.
- The research focused on four sectors of entrepreneurship, i.e., manufacturing, production, farming and retail. Due to this limitation, the findings of the study may not be used to draw proper conclusions on a particular sector to know how each sector is performing.

2. REVIEW OF LITERATURE

2.1. Theoretical Review

The small and medium enterprise (SME) sector plays a crucial role in maintaining high employment and income generation and is therefore critical for a country to achieving sustainable growth. To enhance their role, SME's need to focus on a number of key business challenges such as reducing costs, improving employee productivity and building competitive advantage through producing quality products and services and other entrepreneurial interventions (UNCTAD, 2005). To achieve the growth potential of the SME's sector the government has to play a role of providing the necessary infrastructure to the sector and this is only achievable through taxing the same sector i.e. reaping the benefits of the said infrastructure.

According to Dalton,(1996) tax is a compulsory contribution imposed by a public authority irrespective of the amount of service rendered to the tax payer in return; Professor Seligman (2004)defined it into compulsory contributions from a person to the government to defining the expenses incurred in the common interest of all without reference to special benefits compared. The government offers these functions of administrative, development and social function effectively and adequately.

While growth of any firm or sector is measured by the contribution and number of employment it is providing and increase in sales, income, profit and thus capital which portrays a survival capability in case of any problem facing the sector or firm.

Salemi (2010) argues that there are various types of taxes i.e. income tax, cooperation tax, sales tax, excise tax, custom duty, fees, prices, fines, special assessments, VAT along others. The government levy taxes to accomplish the following purpose i.e. raise revenue, maintain economic stability, solve unemployment problem, offer protection policy, social welfare and help achieve fair distribution of resources by optimally allocating resources and increase the rate of economic formula. But when imposing any tax, the following conditions and challenges must be fulfilled i.e. Equality, certainty, convenience, economical productivity, elasticity, flexibility, simplicity and durability otherwise it won't be fulfilling its objectives. Another challenge of taxation is those who try not to pay tax through evading or avoidance. In order for SME's sectors to grow, the level of taxation set must be friendly and not stifle the running of the business. Holtz-Eakin (1995) argues as to whether there is an economic case for the preferential tax treatment of SME's. Some of the factors that could be advance in favor tax concessions for SME's includes: firstly, presence of externalities provided by small firms that benefit the economy, the rewards for which are not fully captured by small firms, for example if small firms were highly innovative, but the majority of the advantages accrued to large businesses who, because of their market power, were able to buy small firms for less than they are worth. Secondly, there is a need to provide tax breaks for small firms, on the basis of equity and thirdly the tax system should not affect the growth of the SME's in a negative way.

2.2 Characteristics of SMEs

The sector is characterized by free entry; small scale nature of the activities; self-employment with a high proportion of family workers and apprentices; little capital and equipment. Other characteristics include labour intensive technology; low skills; low level of organization with little access to organized markets, unregulated and competitive markets, less formal credit, low education and training or services and amenities and cheap provision of goods and services.

2.3 Importance of the SMEs for Zambian Economy

SMEs have been an important tool of economic development in Zambia. The future of any growing economy such as Zambia's depends on the entrepreneurial energy of vibrant SMEs because a lot of large businesses start out as SMEs. Many authors believe that they are the starting point of development in the economy towards industrialization. Udechukwu (2003) for example sees the SME sector as a very important sector that will enhance the contributions of the private sector and provide the critical building blocks for industrialization and sustainable economic growth. SMEs broaden the base of participation in society, decentralize economic power and give people a stake in the society's future (Williams, 2006). SMEs have also been recognized as a channel for improving the efficiency of domestic markets and making productive use of scarce resources, and thus facilitating long-term economic growth in poor countries (Aryeetey & Ahene, 2004). Given that a large proportion of Nigeria's population relies either directly or indirectly on small and medium enterprises for survival, their importance cannot be overemphasized.

A major contribution made by SMEs is in the area of employment (Yaobin, 2007) Small and medium-sized enterprises are a key source of new jobs, innovation, economic dynamism and greater social inclusion in the European Union. Other important they play an important role in secondary labour markets (that is, they offer a high amount of employment in casual, part-time, low training, low-skilled jobs); they are an invaluable source of 'entrepreneurship', employment growth. Findings from a study carried out by Chu, Kara & Benzing (2008) suggest that Zambians consider entrepreneurship an avenue leading to job security and improving their livelihood. They also regard business ownership as a means of controlling their destiny and deriving self-satisfaction. Being more labour intensive, SME expansion is more likely to boost employment than large enterprises where expansion means higher degree of automation and machining. Hence, SME subsidization will lead to poverty alleviation (Beck, Demirguc-Kunt & Levine, 2005)

Despite the fact that the diverse activities are widely noticeable as a source of livelihood for many Zambians, a number of issues have been raised about the sector. Concerns have basically revolved around legitimacy of the activities when they are carried out in an informal environment their operating environment and their implications and impact on the entire economy. Majority of the firms in the sector do not fulfil business registration requirements and tax obligations. Given the rapid rate at which SMEs have increased, there is an urgent need to capture their activities into the tax net. For the informal firms in the sector, there is a pressing need for a formalization strategy. This will ensure that, firstly; they are legally in the tax net. Second, their tax regime is simplified to enable them fulfil their tax liabilities at minimal costs. Third, this will help tax authorities enhance administrative efficiency, eliminate avenues for tax evasion and enhance tax compliance.

2.4 The Concept of Tax in Smes

Experiences in the past couple of years have proven that SMEs are unquestionably the growth engines of the African economy and therefore the Zambian government considers the issue of SMEs a priority. It has been obvious that there cannot be a recovery from the financial and economic crisis without small enterprises which have to be freed of burdens weighing on their activities. The SMEs tax was introduced to serve this end. This tax was set in a new direction in the income tax system. Although certain elements of the system which has been presented in the parliament may still be modified via the expected social and parliamentary debate, but it includes -besides a more favourable tax rate - two conceptual differences whether the tax levied on essential consumer goods in the VAT bill 2013 was favorable or computation for income tax based on cash flows will favour the SMEs.

Tax regimes and taxation of SMEs have become increasingly topical and governments globally have sought to accommodate and provide a means for such businesses to participate in mainstream economic activity in a legitimate fashion. Previously, tax administrations had argued that the cost of registering these enterprises and processing their returns far outweighed the benefits in terms of revenue yield. This remains true where such businesses are required to participate in the normal taxpaying regime and this has led to a significant move internationally to offer simplified regimes for this category of taxpayers. Cost versus benefit is still an important issue that needs to be carefully balanced. However, a better balance is greatly facilitated where a simplified regime is implemented.

There is a growing awareness that tax systems can go beyond merely maximizing revenue collection but over the medium- to longer-term can inculcate a higher degree of tax compliance and build a platform to support entrepreneurship and business development. Over time, perceptions regarding small businesses have changed. In the late 70's, small businesses were typically regarded as habitual tax avoiders and evaders. With the advent of private sector led development paradigm in the early 1980s, the SMEs represented a higher and growing proportion of GDP in both developing and developed countries culminating into much emphasis on taxing these businesses.

2.5 Methods of Taxing the SMEs

There are fundamental differences in initiating a tax regime in developed and developing economies. In developed economies, most small businesses are within the formal category and it has been easy to customize the existing tax legislation to suit their needs. Essentially, the system used does not represent a major departure from existing systems. Furthermore, the location of the taxpayer is easily traceable. However, in developing countries, the task is more difficult in that small taxpayers are not generally compliant with tax, registration, local government requirements and regulations (through ignorance as well as intent). Furthermore, they cannot be easily located or identified by the tax administration because they overwhelmingly operate within the informal sector.

The following are the key features of the small taxpayers sector:

- i. Small, transient, and often cash-based businesses.
- ii. High turnover rates - many new businesses created, many others fail, and a few grow. Many of them are family based, sole proprietorships, and partnerships.
- iii. Large numbers often comprising between 70-80 percent of total taxpayers.
- iv. Low revenue potential (typically 5-10 percent) of total revenues.
- v. Expensive to administer.
- vi. Many remain outside the tax net due to challenges in complying with tax and other government regulations.
- vii. They have weak accounting capabilities coupled with rudimentary accounting systems.

Tax authorities experience major problems in identifying informal sector activities, not only because they sometimes include illicit activities, but also because even legitimate activities are difficult to identify when they are mobile (traders), small-scale (basic services) or elusive (craftsmen carrying out small jobs for cash). These difficulties severely limit the personal and business income tax base that is known and reported to the tax authorities. Usually, only a fraction of small businesses register with the tax authorities. Moreover, only a small share of the overall population is on the payroll of formal sector enterprises and the government, where recorded wages and salaries are readily observable and easily taxable through employer withholding schemes. Despite such handicaps, the experience of several countries in recent years shows that substantial improvement can be achieved

with determined effort and an appropriately designed strategy.

2.6 Approaches to Taxing the Informal Sector

2.6.1 Legitimizing the Informal Sector Approach

Available literature shows that one way to capture the shadow economy into the tax net is to legitimize the sector by allowing tax holiday and/or exemptions for certain sectors. For instance, exempting typically low-yield sectors like agriculture from income taxation will significantly reduce the cost of tax administration. This system has been applied in India where the agricultural sector is constitutionally excluded from central income tax.

2.6.2 The Presumptive Approach

Presumptive taxation involves the use of indirect means to ascertain tax liability, which differ from the usual rules based on the taxpayer's accounts. The term "presumptive" is used to indicate that there is a legal presumption that the taxpayer's income is no less than the amount resulting from application of the indirect method¹. It involves simple and cost-effective techniques to capture domestic transactions and sources of income that frequently escape taxation under conventional norms. These techniques include lump-sum levies on small-scale business activities (standard assessments); the assessment of taxes through indicators or proxies that help estimate a taxpayer's income (estimated assessments); and the collection of minimum taxes irrespective of a taxpayer's actual level of business activity (presumptive minimum taxes). More recently, other methods have gained importance. They include presumptive taxes on imports; withholding schemes designed to capture the incomes of unregistered businesses; and graduated business license fees.

A presumptive tax can be assessed in two ways. These include: First, estimating the taxpayer's income estimated on a specific basis. Secondly, computing taxable income on the basis of key factors associated with income generation such as sales, turnover, number of employees, size of the firm and taxpayer's assets. Presumptive tax is of various types. These include:

- i. Minimum tax concept which is a fixed amount of tax is paid by persons in the informal sector regardless of the actual trading results;
- ii. Forfeit Tax in VAT which is similar to the minimum tax and is applicable to a class of persons referred to as small traders in lieu of Value Added Tax;
- iii. Multi bands tax liability scheme where several fixed income brackets (bands) are set based on sales or turnover.

2.6.3 The Indirect Approach

This approach imposes an appropriate tax burden on those operating in the underground economy. Indirect taxes could potentially substitute for special regimes aimed at the hard to tax sector to the extent that these taxes reach the targeted sector via the shifting of taxes into wages, returns on capital or consumer prices. It is ideal for economies where final consumption taxes significantly capture many of the informal sector activities and where the proportion of the informal sector to the entire economy is relatively large.

2.7 Types of Taxes

2.7.1 Direct Taxes and Indirect Taxes:

1. Direct taxes are those that are imposed on incomes and property of individuals. The distinguishing characteristics are that their impact and incidence fall on the persons concerned and cannot be shifted to other persons. Examples include: Personal income tax (employment income and rental income), wealth tax, capital gains tax, estate duty, inheritance duty, the capital levy, corporation tax, and super profit tax.

2. Indirect taxes – these are taxes which are not directly collected by the government but indirectly through intermediaries who are usually the business people. Indirect taxes are usually imposed on commodities but they can be shifted on to the consumers. Indirect taxes include: sales tax, excise duty, customs duty consisting of import and export duties, expenditure tax, sumptuary tax and Value Added Tax (VAT).

2.7.2 Proportional and progressive taxes

1. Proportional tax – this is a tax levied on a uniform percentage between the tax and the income. The tax liability increases in the same proportion with income.
2. Progressive tax – this is where the tax rate increases as the amount subject to taxation increases. This tax is designed to help the lower paid tax payers and therefore to redistributed income.
3. Regressive tax – is a tax imposed in such a manner that the tax rate decreases as the amount subject to taxation increases. It imposes a greater burden for the poor than on the rich.

2.7.3 Tax Policy and the Growth of SMEs

According to Tomlin (2008), economists argue that the resources smaller companies direct towards tax compliance are resources that could otherwise be used for reinvestment, facilitating future growth. Hence, there is a belief that taxes and a complex tax system put disproportionate pressure on smaller businesses. Small taxpayers under the regular system of taxation are discriminated against, since the compliance requirements, cost of compliance and tax rate are the same for both small and large enterprises. Reducing the compliance costs and tax rate increases the small enterprises profit margin. It also increases the Government's tax revenue, since the simplified provisions for a micro enterprise historically reduce the size of the shadow economy and the number of non-complying registered taxpayers (Vasak, 2008). Furthermore, SMEs usually have to operate in an overbearing regulatory environment with the plethora of regulatory agencies, multiple taxes, cumbersome importation procedure and high port charges that constantly exert serious burden on their operations.

Furthermore, SMEs usually have to operate in an overbearing regulatory environment with the plethora of regulatory agencies, multiple taxes, cumbersome importation procedure and high port charges that constantly exert serious burden on their operations. Many SMEs have to deal with myriad of agencies at great cost. As stated earlier they are heterogeneous and these differences in size and structure may in turn carry differing obligations for record-keeping that affect the costs to the enterprises of complying with (and to the revenue authorities of administering) alternative possible tax obligations. Public corporations, for example, commonly have stronger accounting requirements than do sole proprietorships, and enterprises with employees may be subject to the full panoply of requirements associated with withholding labor income taxes and social contributions (International Tax Dialogue 2007).

An overly complex regulatory system and tax regime or one opaque in its administration and enforcement makes tax compliance unduly burdensome and often have a distortionary effect on the development of SMEs as they are tempted to morph into forms that offer a lower tax burden or no tax burden at all (Masato, 2009) and this results in a tax system that imposes high expenses on the society. A poorly executed tax system also leads to low efficiency, high collection charges, waste of time for taxpayers and the staff, and the low amounts of received taxes and the deviation of optimum allocation of resources (Farzbod, 2000). Existing empirical evidence clearly indicates that small and medium sized businesses are affected disproportionately by these costs: when scaled by sales or assets, the compliance costs of SMEs are higher than for large businesses. Among the factors militating against SME tax compliance with are: high tax rates, Low efficiency, high collection charges, waste of time for taxpayers and the staff, and the low amounts of received taxes and the deviation of optimum allocation of resources.

Although there is certain policy measures geared towards SME growth in Zambia, the support needs to be increased, standardized and systematic. Iwuji (2003) believes that it is the role of the government to provide an enabling environment and social services that support businesses and persons. This means enhancing the investment climate in Zambia for increased economic growth and subsequent tax contribution from all citizens which is necessary because a good number of SMEs operate in the informal economy due to the fact that they deem the tax environment within which they operate unfavorable. These SMEs constitute untapped revenue potential and an even playing field in many countries (International Tax Dialogue, 2007) as such they need to be captured by the tax net. The legislation is a necessary regulator for protection of the business environment and security of the economic agents, for establishment of the necessary social security regulations but at the same time it hampers the business with additional expenditures and administrative obstacles, which place in different positions the SME. They can either share part of the staff or hire people to deal only with studying the legal requirements and complying with the new regulations, or contract some personal service firm (like E&Y, Deloitte and Touché, Price Waterhouse etc.) to deal with their tax compliance, planning etc. For SME this is a great expense out of their abilities (Smatrakalev, 2006). Shahroodi, (2010)

believes that for a tax system to be efficient the tax policy needs to be designed such that the tax rates are appropriate and rational, the exemptions are lower in amount, the tax authorities are more efficient, the tax burden of the indigent people should be lighter and the fight against corruption and tax evasion should be strengthened. Tax policies can be designed in such a way that they do not only directly affect SMEs but also indirectly push for their growth for example the practice in China where tax policy has been designed to encourage SME financing by granting exemptions from business tax for financial corporations that provide guarantee for loans to SMEs and granting tax deductions to market entities and venture capitalists that invest in high-tech SMEs the tune of 70% of the investment value. Another way is by designing tax policies that encourage human capital training. (Yaobin, 2007) declared that special tax regimes for SMEs may be appropriate policy instruments for minimizing the cost of collection. It is important to note that the awareness of the dangers of inadequate attention to the taxation of SMEs has grown. It can lead, for example, to distortions of competition as a result of uneven tax enforcement, with incentives created to limit growth and to avoid tax through artificial splitting of enterprises (International Tax Dialogue, 2007). Furthermore, policy incentives such as tax rebate for SMEs with emphasis on local sourcing of raw materials, serious in adding value to commodities for exports and other business ethics, should be employed by government. Similarly, government could increase funding for the development of the sub-sector through direct budgetary allocations and enhance private sector investment opportunities that will focus on specific areas of capacity enhancement. Also, tax law should be simplified continuously, mainly for three reasons, namely to lower both compliance costs and administrative costs, to reduce uncertainty faced by taxpayers; and to improve the levels of voluntary compliance (Kasipilai, 2005). Pro-business (and Pro-SME) Tax regimes and enforcement should be simple, consistent and predictable.

2.7.4 Role of taxation policy in promoting SME sector development

There are many factors that can influence the development of small and medium enterprises in the economy. The most frequently mentioned among them are: state support of the sector, proper legislative support and mechanisms of its fulfillment, access to financial resources and investment incentives (Small Business in Ukraine 1997 122). However, one of the most important factors that promotes development and growth of small and medium enterprises is the taxation system.

Research made in different countries has shown that the countries where the level of tax rates, the costs of fulfilling taxation requirements as well as costs of auditing are high, the sector of small and medium enterprises is comparatively small. For instance, in Ukraine, where policy of SME sector taxation is considered to be too burdensome, the share of the sector in GDP is only 5.5% (Analytical report on State Committee for Entrepreneurship Development 1997). Moreover, for several years the share of operating SMEs among registered ones was falling: in 1992 that index was 49.4%, in 1993 – 47.7%, in 1994 – 37.3% (Small Business in Ukraine 1997 49). On the other hand, in the Czech Republic, where taxation policy for small and medium enterprises is milder, while all the other policies supporting small and medium businesses are approximately similar, the share of this sector in official GDP is more than 50% (Materials of the Seminar «Development of Entrepreneurship» 19982).

Of course, such a big difference in numbers cannot only be due to the different taxation policies. It is understandable, that the transition in the Czech Republic started earlier and before transition the SME sector was present to greater degree in Czech economy than in Ukraine. However, in the Czech Republic proper taxation incentives were created at the very beginning of transition period. Thus, we can see that taxation policies can play a big part in promotion the development of the SME sector.

3. RESEARCH METHODOLOGY

3.1. METHODOLOGY

- Accomplished of a research requires several things. In this view, the researcher used a number of techniques that were necessary to carry out the research successfully and resourcefully. Consequently, the research methodology seeks to elucidate the variety of methods and techniques that the researcher used in order to get suitable information, sampling procedures and data analysis.

3.2. SAMPLING DESIGN

- Methodology is a vital element for a research since it shows the appropriate ways in which data will be collected. For that reason, the research was conducted in Chipata District of Eastern Province of Zambia particularly Chipata district. Sequentially to carry out this research effectively, the researcher used questionnaires; interviews, and observation techniques. These approaches were engaged in order to find out the effects of high taxation on the growth of small and medium enterprise. The entrepreneurs targeted signified a reasonable representation of all the sectors in the manufacturing, production, retail and farming.

- A survey of 50 small and medium enterprises who conduct business in Chipata district. The survey was conducted by the use of a self-administered questionnaires which contains open ended questions.

3.3. TARGET POPULATION

- The research primarily targeted small and medium enterprise, those who are involved in personal business such as manufacturing, production, retail and farming etc. in Chipata City.

3.4. SAMPLE SIZE

- Chipata town consists of thousands of small and medium enterprise of which the researcher could not manage to interview all of them; therefore, the study only sampled 50 respondents for the questionnaire.

3.5 TYPES AND SOURCES OF DATA

- In order to achieve the objectives of the research, two types of data were collected, that is, primary and secondary data.

3.5.1. PRIMARY DATA

- Primary sources data was collected using a self-administered questionnaire (Appendix I). The questionnaires contained Closed-ended questions. Questionnaires were distributed to contact persons of the selected businesses.

3.5.2. SECONDARY DATA

- The Secondary data collected constituted reviewing existing literature in form of Published Books and other Researches on the Internet, journals, magazines and any other published materials.

3.6 SAMPLING TECHNIQUES

- Convenience sampling was used to collect data from entrepreneurs in Chipata district.

3.6.1 CONVENIENCE SAMPLING

- The researcher chooses the sampling unit on the basis of convenience or accessibility. It is called accidental samples because the sample-unit enters by accident. This is also known as a sample of the man in the street. i.e., selection of units where they are sample units are selected because they are accessible.

3.7 STATISTICAL TOOLS USED

- The data was analyzed mainly by using the percentage method. Preference of the respondents towards taxes in different business sectors has been analyzed using ranking method.

3.7.1. PERCENTAGE ANALYSIS

- This is an analysis where the percentage of a particular factor with different categories is calculated, in order to help one get fair idea regarding the sample and thereby that of the population.

3.8 SELECTION OF STUDY AREA

- The researcher took into consideration different things in selecting the study area. The researcher acknowledges that the success of the research is dependent on the study area in terms of accessibility of the area.

3.9 PHYSICAL CHARACTERISTICS OF THE AREA

- Chipata Town is the provincial capital of the Eastern Province of Zambia. Having a central government administration, markets, a hospital, shopping mall and a number of schools, Chipata is the business and administrative hub that serves the region. The town boasts of a four-star hotel (Protea Hotel), a golf course, an airport, mosques and even a "welcome arch".

3.10 ECONOMIC ACTIVITIES

- The economy of Chipata is agriculture-based with groundnuts, soya beans, sunflower, maize, cotton and tobacco being the major cash crops, most of which are intended for the local and export market. Chipata district has also a large number of the growing informal sector supported by entrepreneurs as well as commercial trading and production agro-based industries. Most if not all of them need money to start (Capital) or conduct their businesses to ensure production of different products for the local and export

market.

3.11 LOCATION OF STUDY

- Chipata is a District in the Eastern Province of Zambia. According to census 2010, the district had a population of 455,783 people. Chipata Town Centre is located about 600Km from Lusaka, the capital city of Zambia, while it is only 110 Km from Lilongwe, the capital city of Malawi. Most of the population are in the urban area with a good number of its population in the rural parts of the district comprising of small and medium scale farmers.

3.12 STUDY LOCATION



Fig. 3.12 Map of Chipata

Source: Central Statistics Office (Chipata).

4.0 DATA ANALYSIS AND INTERPRETATION

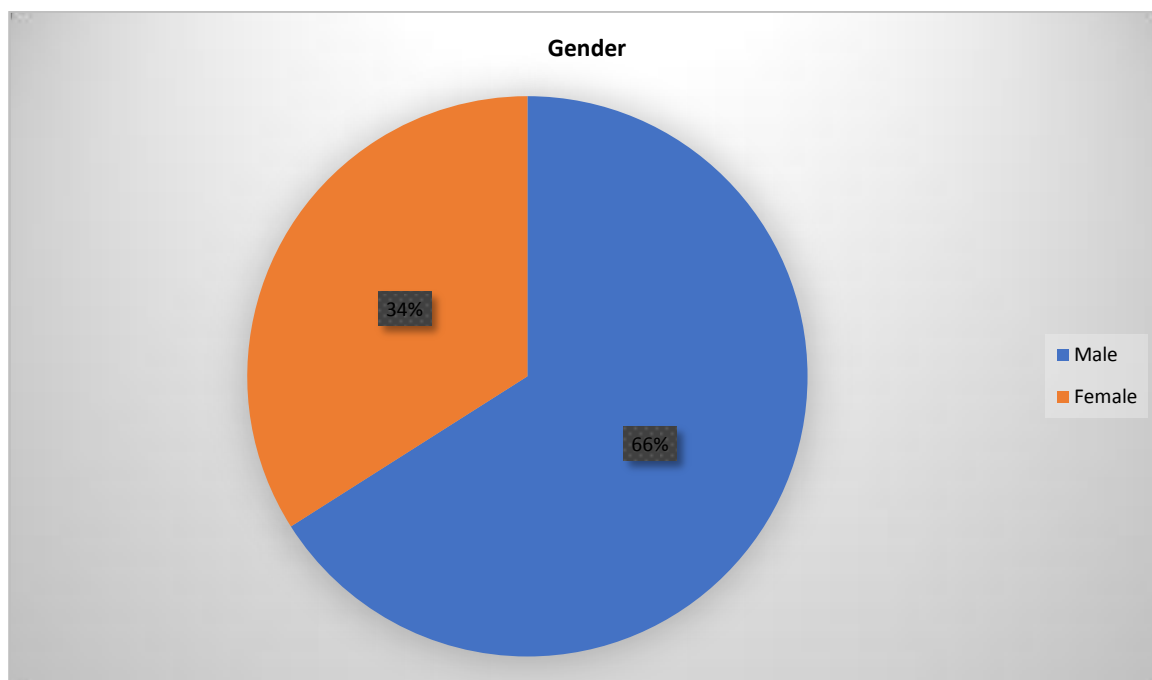
TABLE NO: 4.1

GENDER OF RESPONDENTS

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGES
1	MALE	33	66
2	FEMALE	17	34
	TOTAL	50	100%

INTERPRETATION

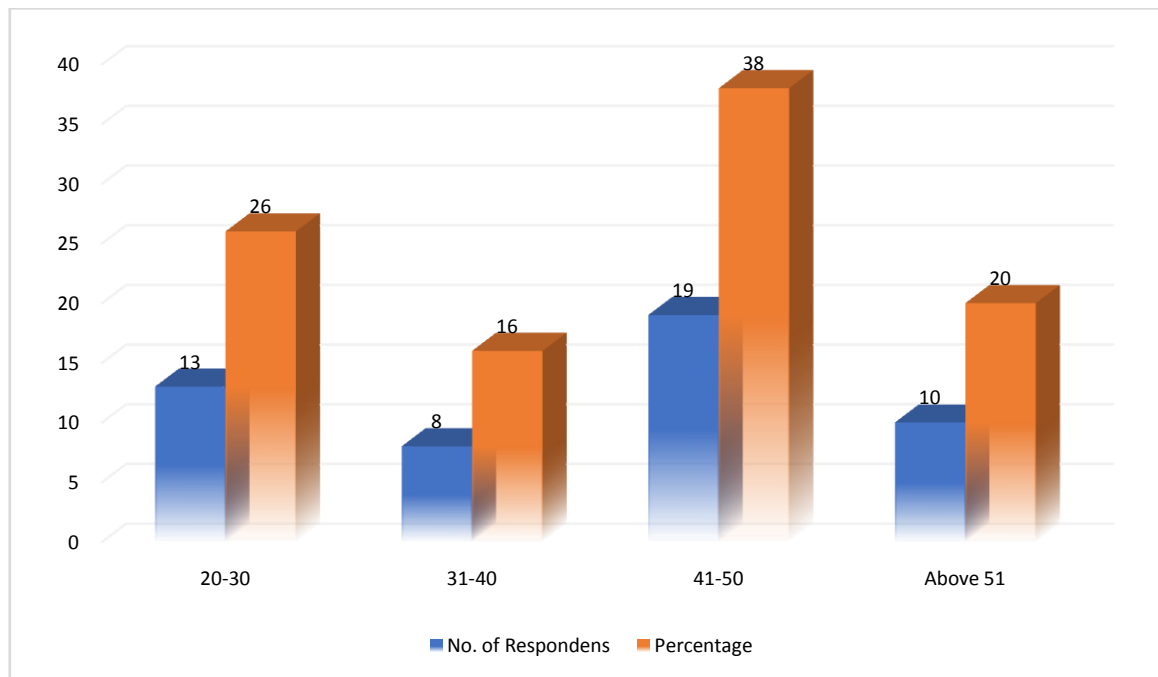
The above table shows the gender of entrepreneurs, 33 out of 50 represented by 66% of respondents being male and 17 represented by 34% of the respondents are female.

CHART NO: 4.1**GENDER OF RESPONDENTS****TABLE No: 4.2****AGE GROUP OF RESPONDENTS**

S. NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGES
1	20 – 30	13	26
2	31 – 40	8	16
3	41 – 50	19	38
4	Above 51	10	20
	TOTAL	50	100%

INTERPRETATION

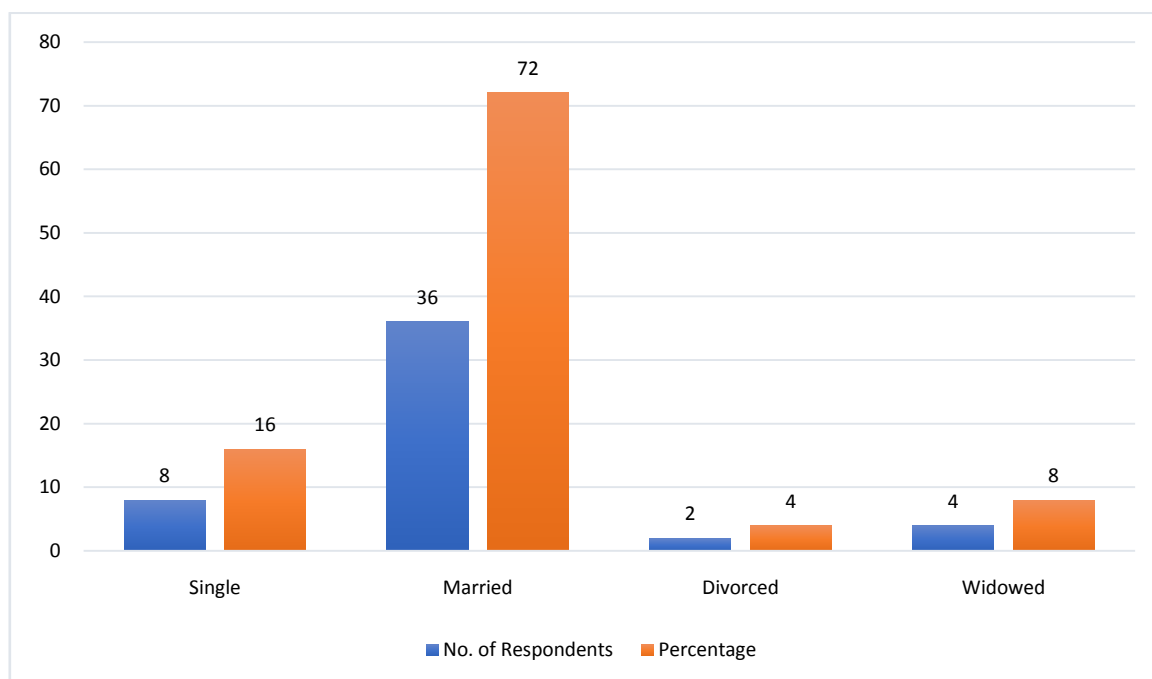
The above table shows the age group of entrepreneurs, highest number are those in the age group between 41-50 with a 38% and the lowest are in the age group of 31-40 with 16%.

CHART No: 4.2**AGE GROUP OF RESPONDENTS****TABLE No: 4.3****MARITAL STATUS**

S. NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Single	8	16
2	Married	36	72
3	Divorced	2	4
4	Widowed	4	8
TOTAL		50	100%

INTERPRETATION:

The above table shows marital status of the entrepreneurs. 36 out of 50 represented by 72% are married entrepreneurs, and 2 out of 50 represented by 4% are divorced entrepreneurs.

CHART No: 4.3**MARITAL STATUS****EDUCATION LEVEL ATTAINED**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	School level	24	48
2	Diploma level	15	30
3	Degree	5	10
4	None	6	12
TOTAL		50	100%

INTERPRETATION:

The majority of respondents in the table above had attained grade 12 O-level certificates represented by 48% and 10% of the respondents had attained degrees or higher education.

CHART No: 4.4

EDUCATION LEVEL ATTAINED

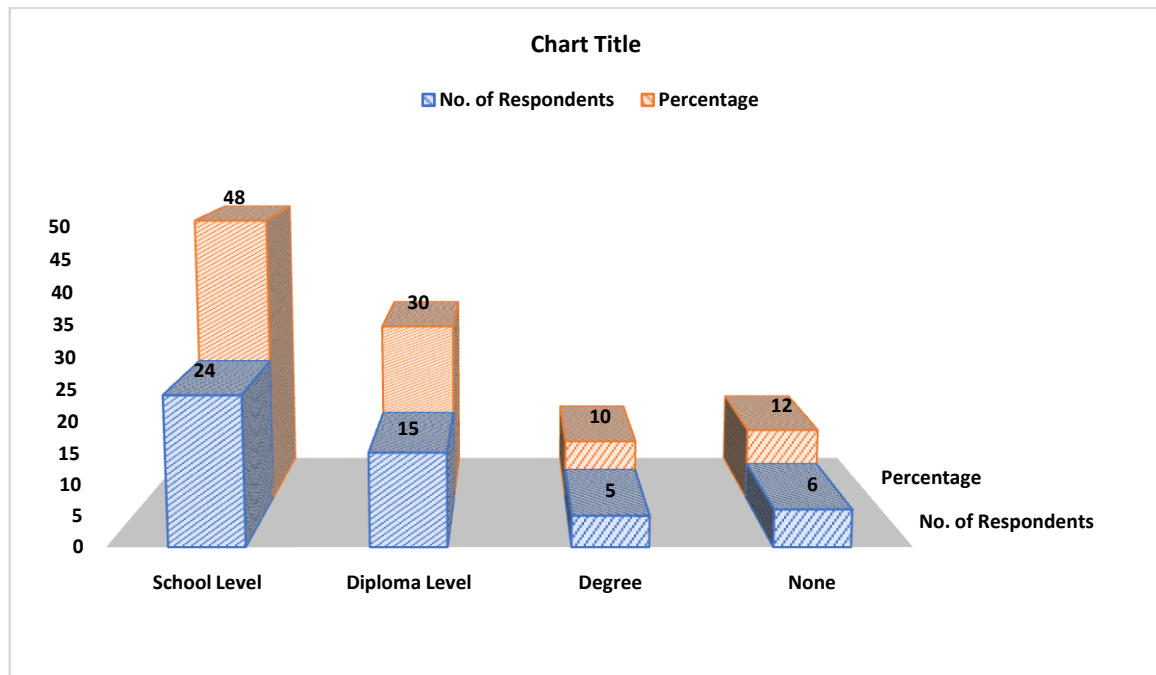


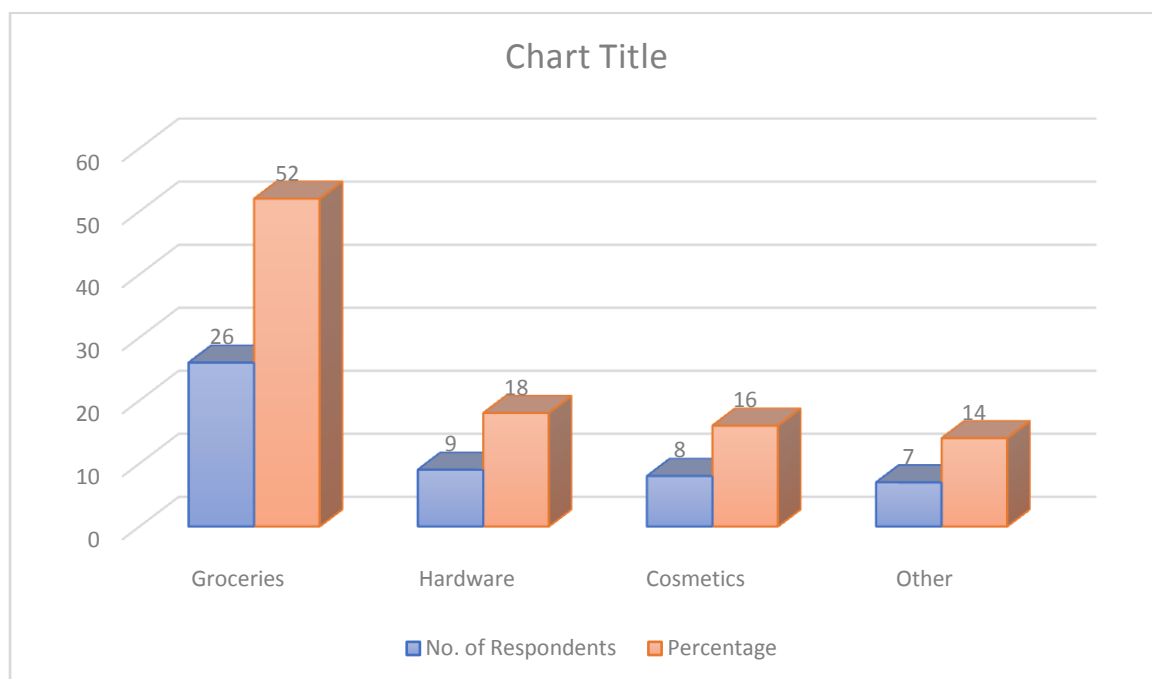
TABLE No: 4.5

TYPE OF BUSINESS DO YOU OPERATE

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Groceries	26	52
2	Hardware	9	18
3	Cosmetics	8	16
4	Other	7	14
TOTAL		50	100%

INTERPRETATION:

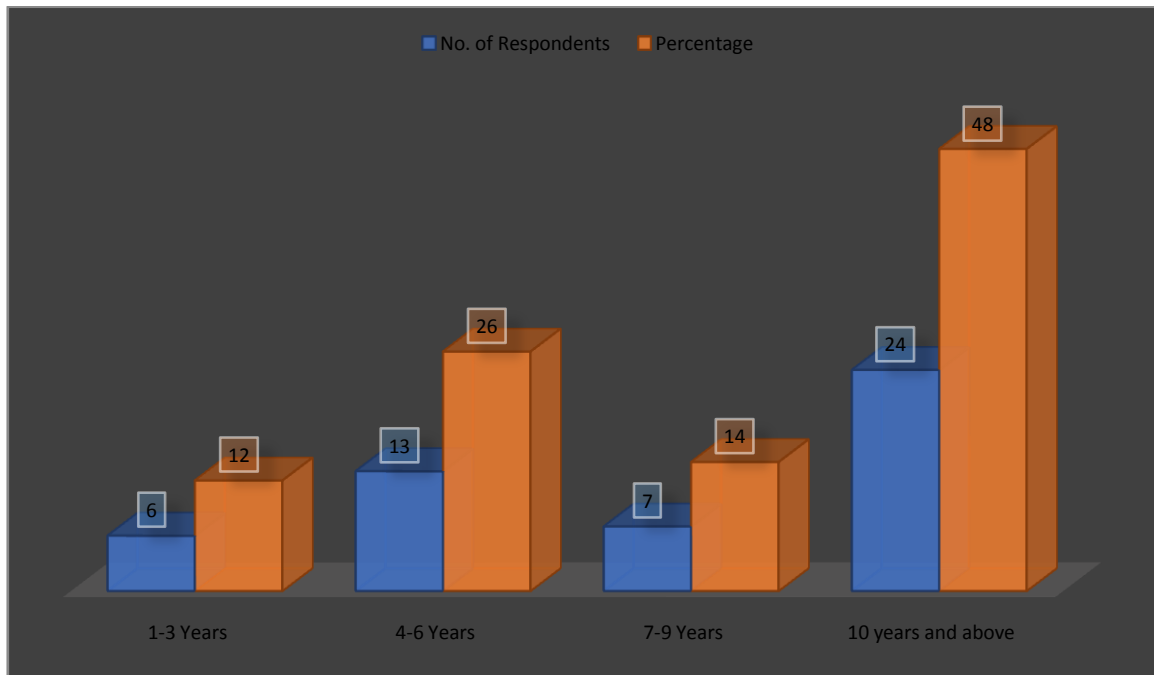
The above table shows that 26 out of 50 entrepreneurs represented by 52% run a groceries business, and 7 entrepreneurs represented by 14% do other types of business.

CHART No: 4.5**TYPE OF BUSINESS DO YOU OPERATE****TABLE No: 4.6****HOW LONG HAVE YOU BEEN DOING THIS BUSINESS**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	1 – 3 Years	6	12
2	4 – 6 Years	13	26
3	7 – 9 Years	7	14
4	10 Years and above	24	48
TOTAL		50	100%

INTERPRETATION:

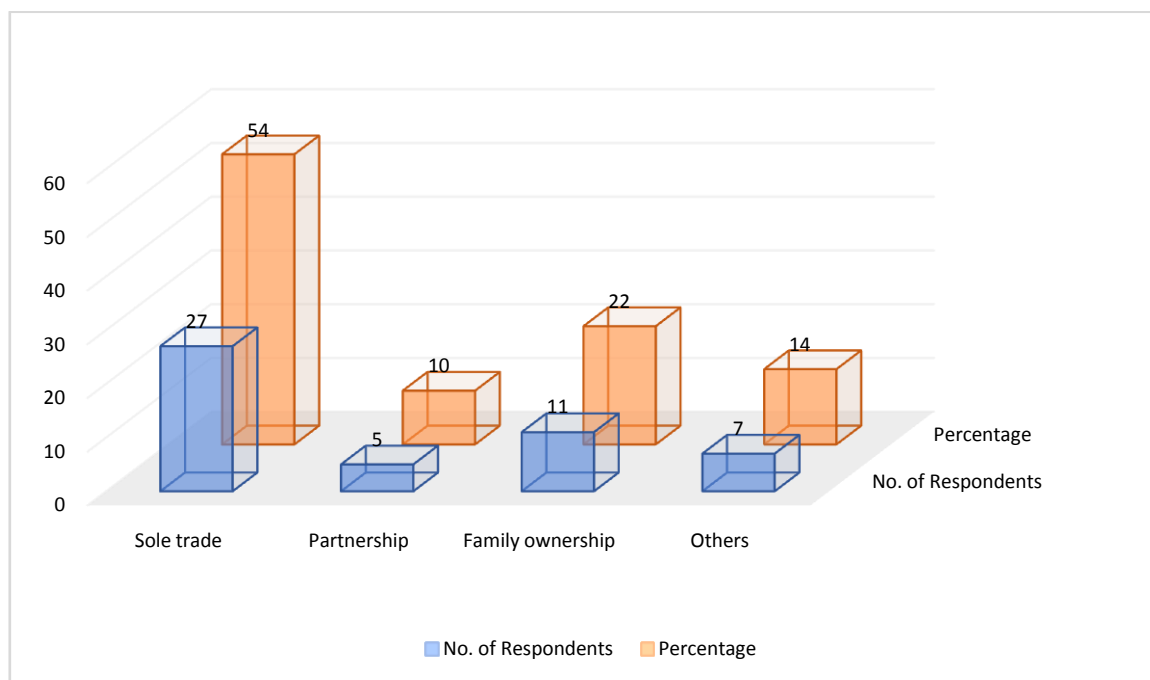
The above table shows 24 out of 50 represented by 48% who have stayed in the business for 10 years and above, and 6 represented by 12% who have stayed in business for 0-3 years.

CHART No: 4.6**HOW LONG HAVE YOU BEEN DOING THIS BUSINESS****TABLE No: 4.7****BUSINESS OWNERSHIP**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Sole trade	27	54
2	Partnership	5	10
3	Family ownership	11	22
4	Others	7	14
TOTAL		50	100%

INTERPRETATION:

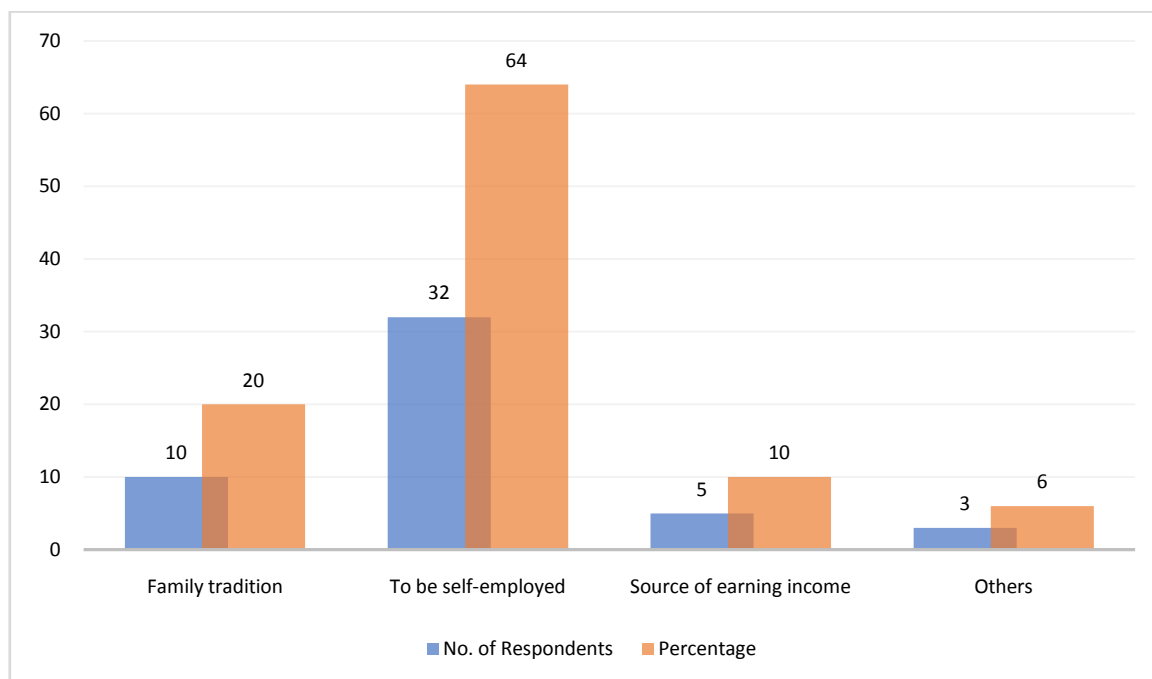
The above table shows 27 out of 50 small and medium entrepreneurs represented by 54% have sole trade ownership, and 5 represented by 10% have partnership ownership.

CHART No: 4.7**BUSINESS OWNERSHIP****TABLE No: 4.8****WHAT MOTIVATED YOU TO START THIS TYPE OF BUSINESS**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Family tradition	10	20
2	To be self-employed	32	64
3	Source of earning income	5	10
4	Others	3	6
TOTAL		50	100%

INTERPRETATION:

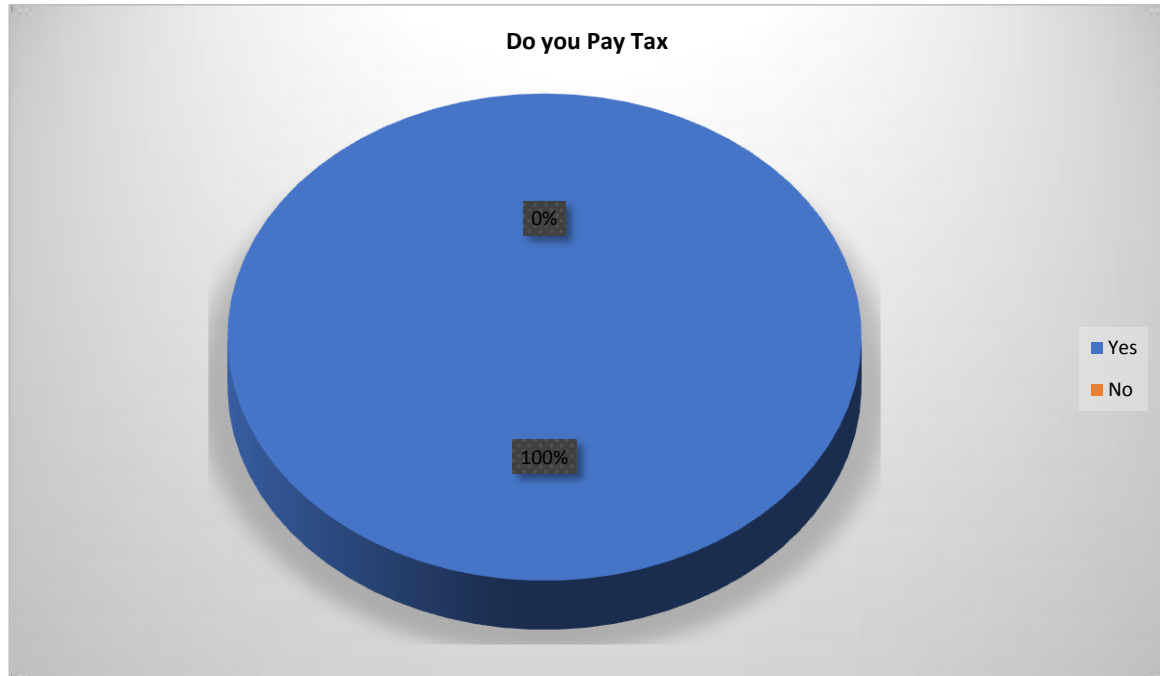
The above table shows 32 out of 50 entrepreneurs represented by 64% started their business to be self-employed, and 3 represented by 6% said that they started the business for other reasons.

WHAT MOTIVATED YOU TO START THIS TYPE OF BUSINESS**TABLE No: 4.9****DO YOU PAY TAX**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Yes	50	100
2	No	0	0
Total		50	100%

INTERPRETATION:

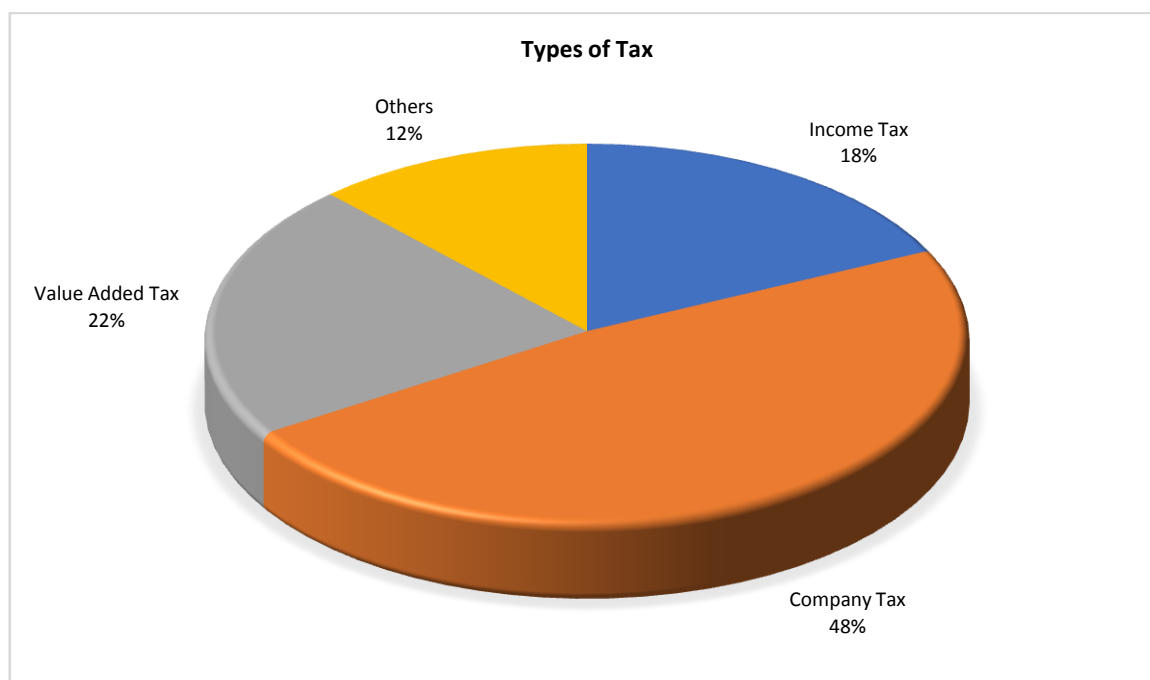
The above table shows 50 out of 50 entrepreneurs represented by 100% said 'yes' for paying tax for their business, and 0 represented by 0% said 'no' for paying tax.

CHART No: 4.9**DO YOU PAY TAX****TABLE No: 4.10****TYPE OF TAX**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Income Tax	9	18
2	Company Tax	24	48
3	Value Added Tax	11	22
4	Others	6	12
TOTAL		50	100%

INTERPRETATION:

The above table shows the types of tax paid by entrepreneurs, 24 out of 50 entrepreneurs represented by 48% said that they pay Company tax, and 6 represented by 12% said that they pay other kinds of tax.

CHART No: 4.10TYPE OF TAX**TABLE No: 4.11****FACTORS INFLUENCE YOU TO PAY THE TAX**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Compliance	14	28
2	Penalties	21	42
3	Litigation	6	12
4	Priotism	9	18
TOTAL		50	100%

INTERPRETATION:

The above table shows factors that influence an entrepreneur to pay tax. 21 out of 50 entrepreneurs represented by 42% said that they fear penalties, and 6 represented by 12% said that they fear litigation.

CHART No: 4.11

FACTORS INFLUENCE YOU TO PAY THE TAX

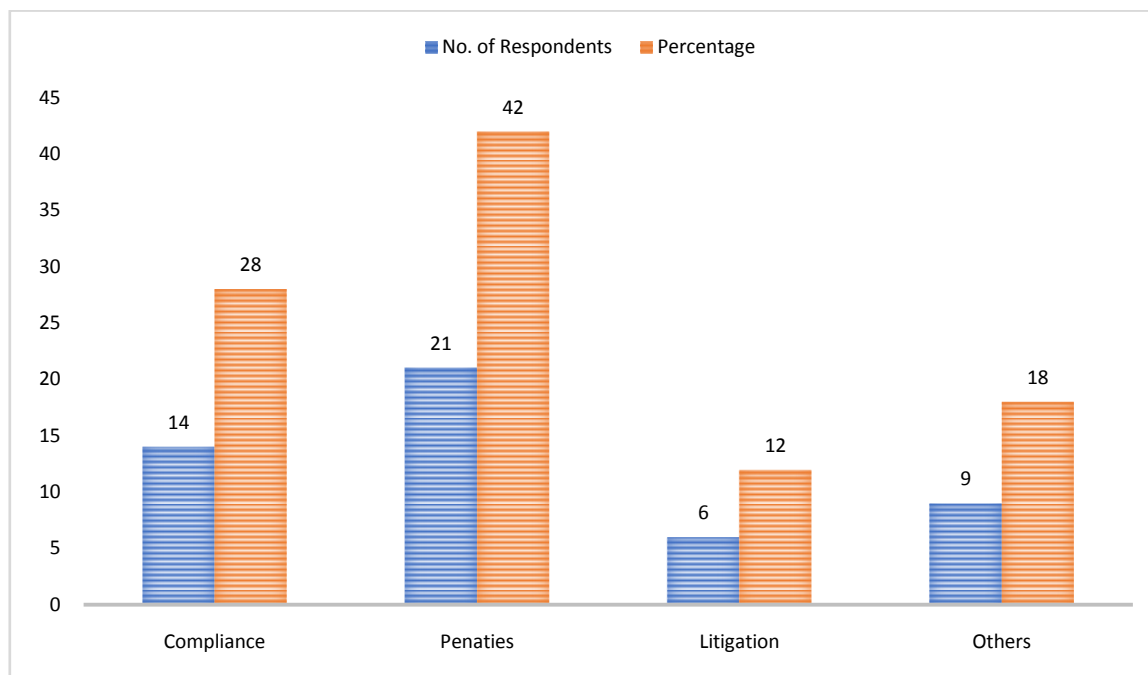


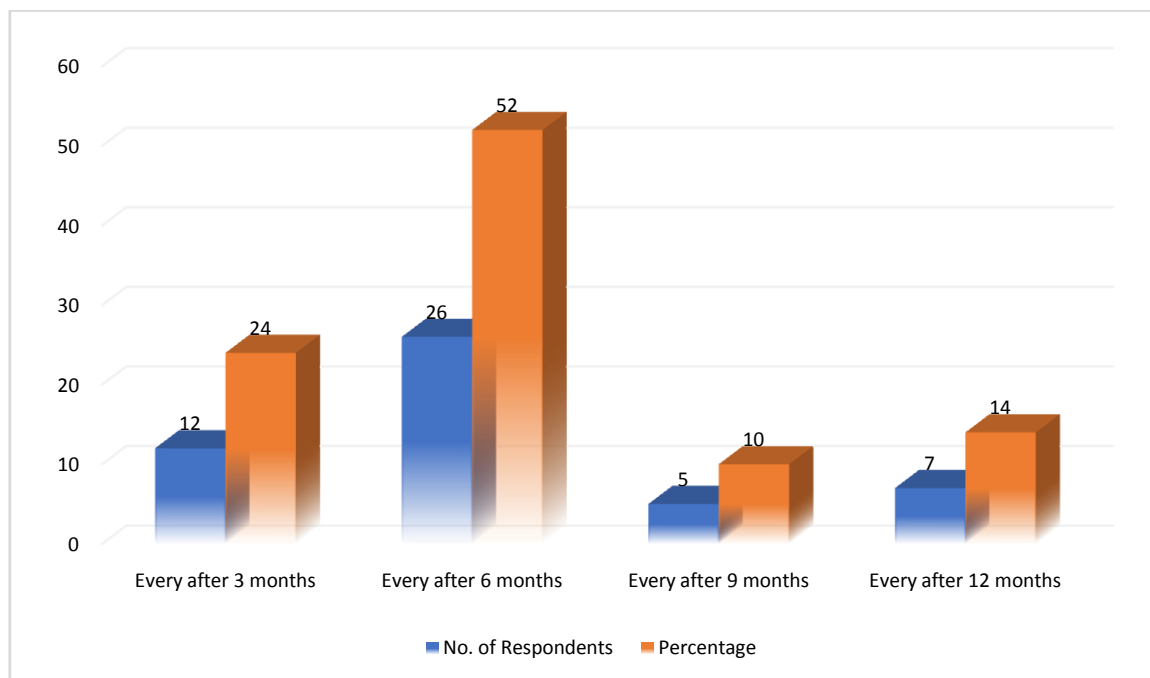
TABLE No: 4.12

AFTER WHAT PERIOD IS TAX COLLECTED

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE
1	Every after 3 months	12	24
2	Every after 6 months	26	52
3	Every after 9 months	5	10
4	Every after 12 months	7	14
TOTAL		50	100%

INTERPRETATION:

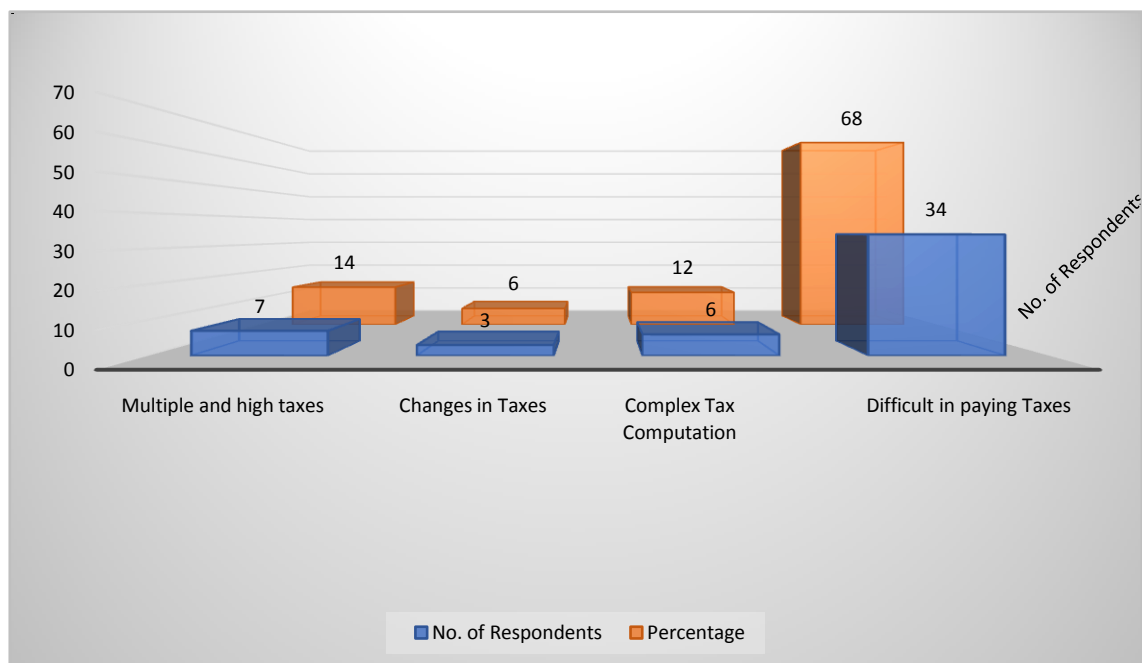
The above table shows 26 out of 50 entrepreneurs represented by 52% said that they pay tax every after 6 months, and 5 represented by 10% said that they pay tax every after 9 months.

CHART No: 4.12**AFTER WHAT PERIOD IS TAX COLLECTED****TABLE No: 4.13****WHAT ARE THE CHALLENGES FACED BY SMALL AND MEDIUM ENTERPRISE WHEN PAYING TAX**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Multiple and high taxes	7	14
2	Changes in Taxes	3	6
3	Complex Tax Computation	6	12
4	Difficult in paying Taxes	34	68
TOTAL		50	100%

TERPRETATION:

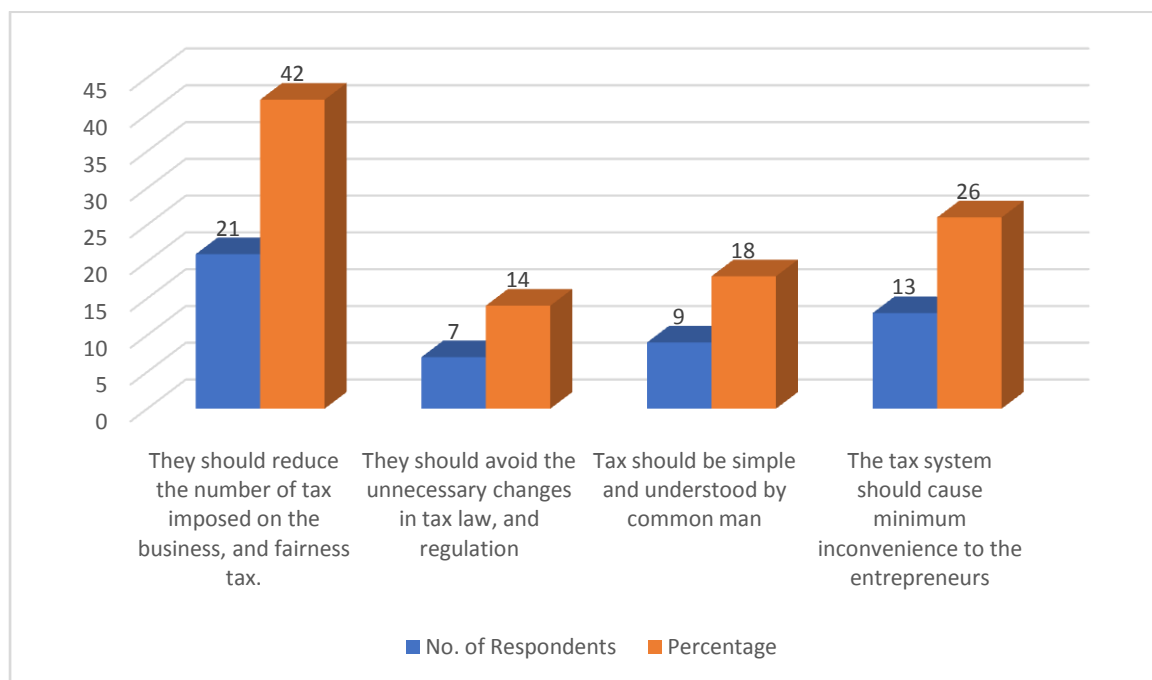
The above table shows the challenges faced by small and medium enterprise when paying tax. 34 out of 50 entrepreneurs represented by 68% said that they find it difficult in paying taxes, and 3 out of 50 represented by 6% said that they challenge which they face it's because of tax changes.

CHART No: 4.13**WHAT ARE THE CHALLENGES FACED BY SMALL AND MEDIUM ENTERPRISE WHEN PAYING TAX****TABLE No: 4.14****WHAT ARE THE MEASURE PUT IN PLACE TO OVERCOME THE CHALLENGE IN QUESTION 13**

S.NO	PARTICULARS	NO. OF RESPONDENTS	(%)
1	They should reduce the number of tax imposed on the business, and fairness tax.	21	42
2	They should avoid the unnecessary changes in tax law, and regulation	7	14
3	Tax should be simple and understood by common man	9	18
4	The tax system should cause minimum inconvenience to the entrepreneurs	13	26
TOTAL		50	100%

INTERPRETATION:

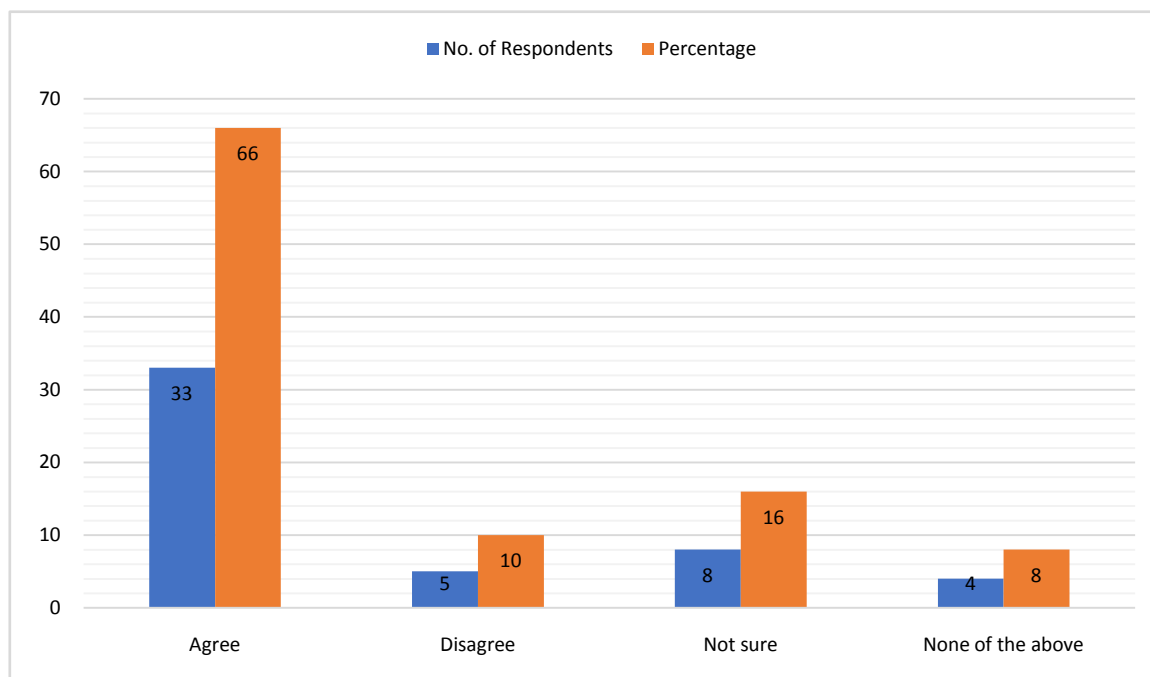
The above table shows the measure put in place to overcome the challenge in question 13. 21 out of 50 entrepreneurs represented by 42% said that they should reduce the number of tax imposed on the business, and fairness tax, and 7 out of 50 represented by 14% said that they should avoid the unnecessary changes in tax law, and regulation.

CHART No: 4.14**WHAT ARE THE MEASURE PUT IN PLACE TO OVERCOME THE CHALLENGE IN QUESTION 13****TABLE No: 4.15****TAX LEVIED ON THE SMALL AND MEDIUM SCALE BUSINESS TOO MUCH**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Agree	33	66
2	Disagree	5	10
3	Not sure	8	16
4	None of the above	4	8
TOTAL		50	100%

INTERPRETATION:

The above table shows the amount of tax levied on the small and medium scale business is too much. 33 out of 50 entrepreneurs represented by 66% agreed that tax levied to the business is too much, and 4 represented by 8% answered none of the above answers.

CHART No: 4.15**TAX LEVIED ON THE SMALL AND MEDIUM SCALE BUSINESS IS TOO MUCH****TABLE No: 4.16****HOW DOES MULTIPLE AND HIGH TAXES AFFECT THE PERFORMANCE OF YOUR BUSINESS**

S.NO	PARTICULARS	NO. OF RESPONDENTS	(%)
1	SMEs find it difficult to make profit at the end of the day	27	54
2	Staffs in SMEs are reduced due to high level of tax	5	10
3	Cost of production is reduce	10	20
4	Others	8	16
TOTAL		50	100%

INTERPRETATION:

The above table shows how the high taxes influence the performance of the business. 27 out of 50 entrepreneurs represented by 54% said that SMEs

find it difficult to make profit at the end of the day, and 5 represented by 10% said that staffs in SMEs are reduced due to high level of tax.

CHART No: 4.16

HOW DOES MULTIPLE AND HIGH TAXES AFFECT THE PERFORMANCE OF YOUR BUSINESS

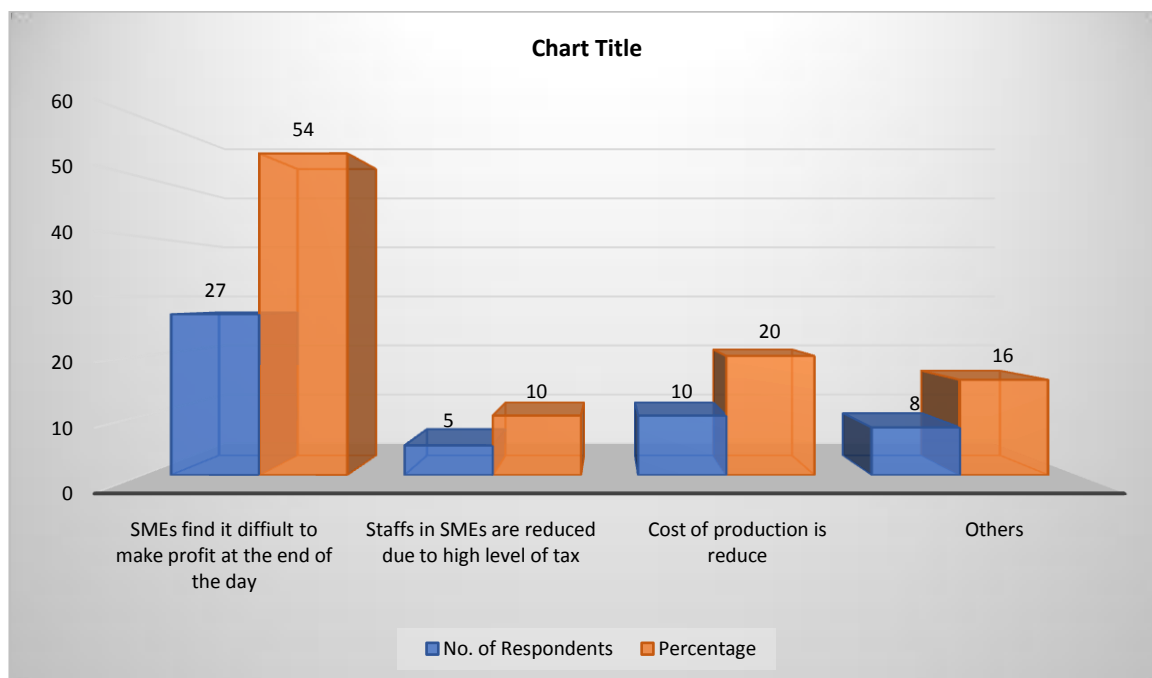


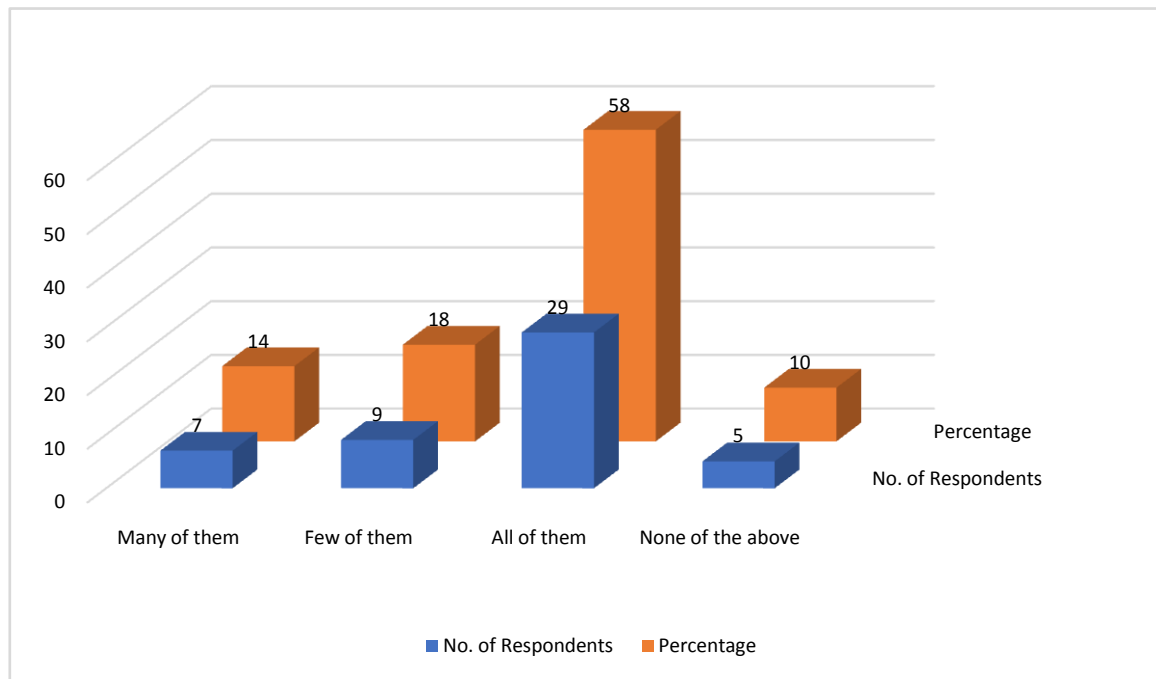
TABLE No: 4.17

WHICH OF THE FACTORS IN QUESTION 16 AFFECT SMALL AND MEDIUM SCALE BUSINESS

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Many of them	7	14
2	Few of them	9	18
3	All of them	29	58
4	None of the above	5	10
TOTAL		50	100%

INTERPRETATION:

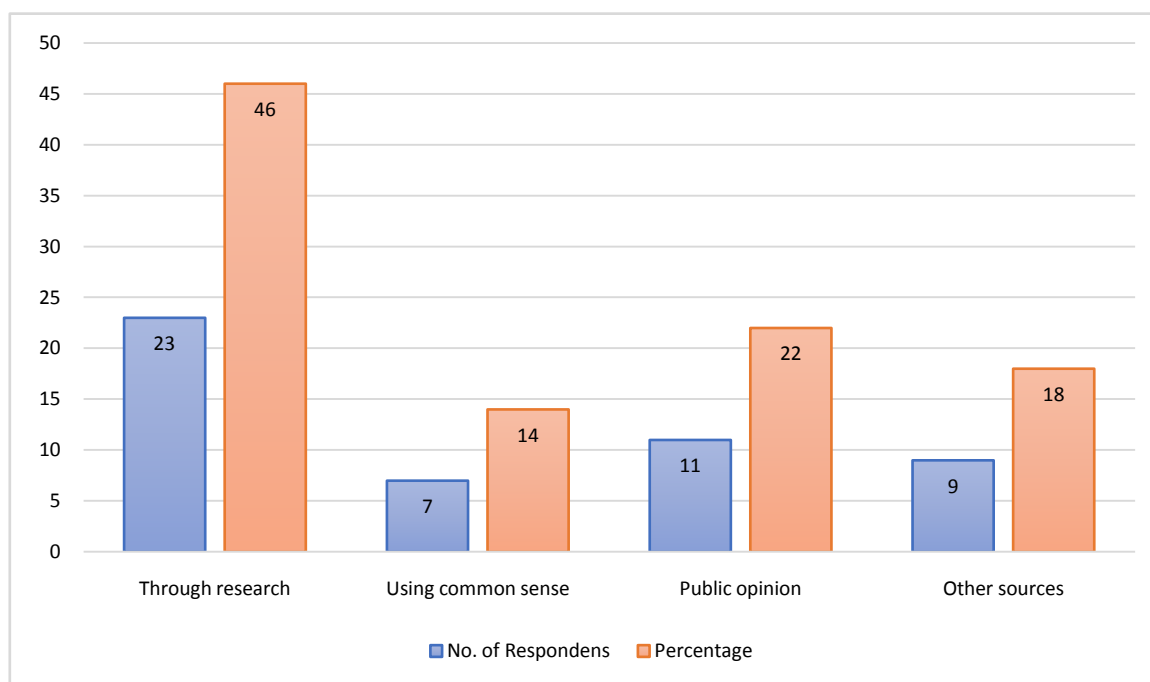
The above table shows the factors in question 16 which affect the small and medium scale business. 29 out of 50 entrepreneurs represented by 58% said that all the factors stated in 16 affect the business, and 5 represented by 10% said that none of the above stated factors affect the business.

CHART No: 4.17**WHICH OF THE FACTORS IN QUESTION 16 AFFECT SMALL AND MEDIUM SCALE BUSINESS****TABLE No: 4.18****HOW WOULD YOU TELL THAT THESE FACTORS ARE COMMON IN SMALL AND MEDIUM SCALE BUSINESS?**

S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE (%)
1	Through research	23	46
2	Using common sense	7	14
3	Public opinion	11	22
4	Other sources	9	18
TOTAL		50	100%

INTERPRETATION:

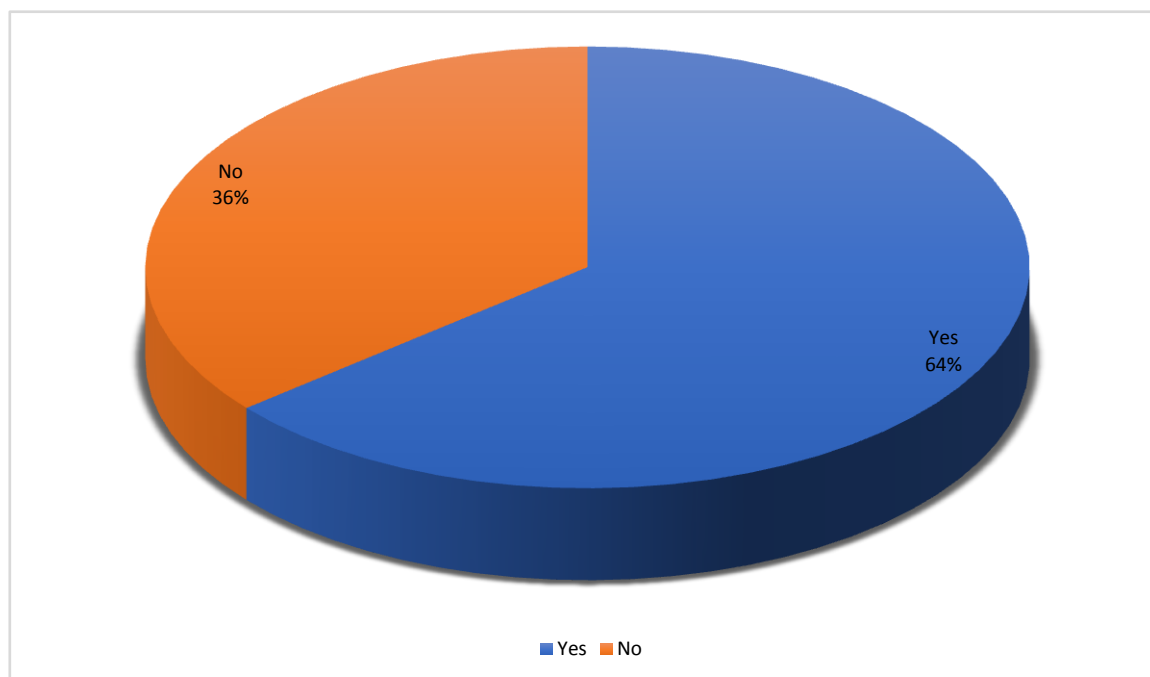
The above table shows how you can tell the factors which are common in small and medium scale business. 23 out of 50 entrepreneurs represented 46% said that through research, and 7 represented by 14% said that by using common sense.

CHART No: 4.18**HOW WOULD YOU TELL THAT THESE FACTORS ARE COMMON IN SMALL AND MEDIUM SCALE BUSINESS?****TABLE No: 4.19****DOES THE GOVERNMENT OFFER ANY SUPPORT TOWARDS THE SMALL AND MEDIUM SCALE BUSINESS?**

S.NO	PARTICULARS	NO. OF RESPONDENTS	(%)
1	Yes	32	64
2	No	18	36
TOTAL		50	100%

INTERPRETATION:

The above table shows 32 out of 50 entrepreneurs represented by 64% who answered 'yes' that government offers support towards SMEs, and 18 represented by 36% who answered 'no' that government doesn't offer support towards SMEs.

CHART No: 4.19**DOES THE GOVERNMENT OFFER ANY SUPPORT TOWARDS THE SMALL AND MEDIUM SCALE BUSINESS?****TABLE No: 4.20****WHAT KIND OF SUPPORT DOES THE GOVERNMENT OFFER TOWARDS SMALL AND MEDIUM SCALE BUSINESS?**

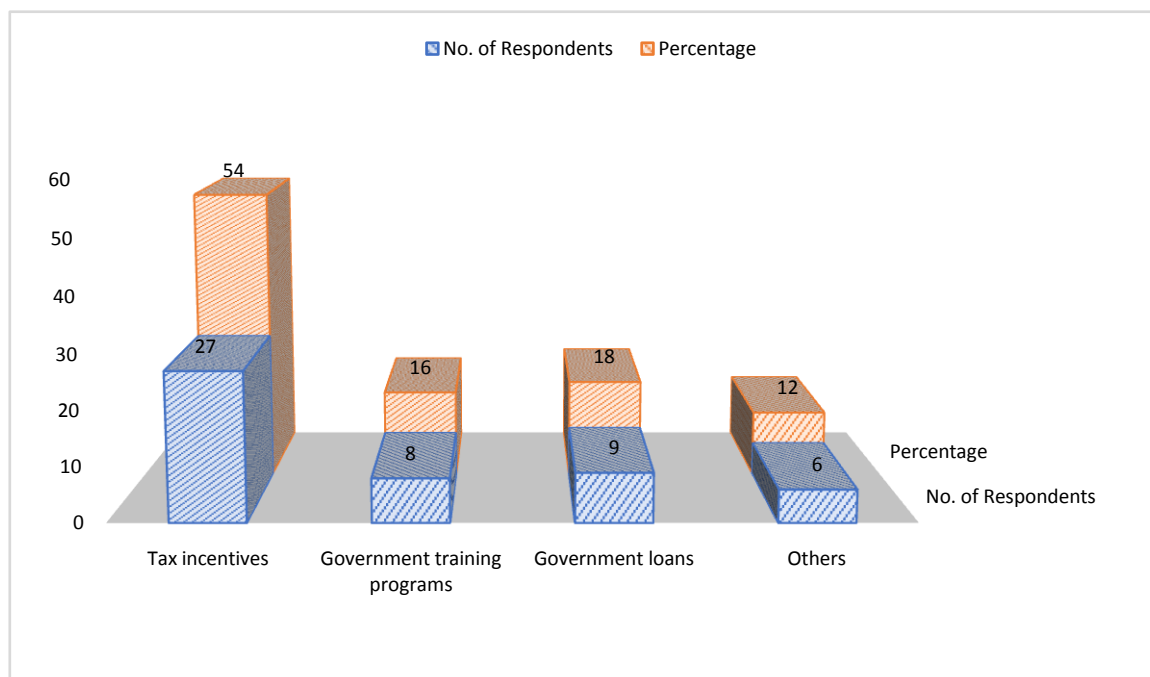
S.NO	PARTICULARS	NO. OF RESPONDENTS	PERCENTAGE
1	Tax incentives	27	54
2	Government training programs	8	16
3	Government loans	9	18
4	Others	6	12
TOTAL		50	100%

INTERPRETATION:

The above table shows the kind of support which the government offer towards small and medium scale business. 27 out of 50 entrepreneurs represented by 54% said that the support which they receive is through tax incentives, and 6 represented by 12% said that through other means of support.

CHART No: 4.20

WHAT KIND OF SUPPORT DOES THE GOVERNMENT OFFER TOWARDS SMALL AND MEDIUM SCALE BUSINESS?



5. FINDINGS, SUGGESTIONS AND CONCLUSION

5.0 FINDINGS

Percentage Analysis

- 58% of the small and medium entrepreneurs responded that high rates of tax affect the growth of their business.
- 54% of small and medium entrepreneurs responded that multiple and high taxes affect the small and medium enterprise in such way that the business finds it difficult to make profit at the end of the day.
- 68% of the entrepreneurs responded that the challenges which they face in paying tax is that they find it difficult for their small and medium enterprise to pay tax.
- 48% of the small and medium entrepreneurs responded that the type of tax that affects the growth of their business is company tax.
- 50% of the small and medium entrepreneurs responded that the criteria set by the Zambia Revenue Authority (ZRA) when collecting tax from the business is every after 6 months.

5.1 SUGGESTIONS

- The Zambia Revenue Authority (ZRA) should consider the rates of taxes which are imposed on small and medium scale enterprise.
- Taxes should be collected in relation to the sizes and profit of small and medium scale enterprise considering all other factors that can constrain the progress of such business as there is a relationship between SMEs sizes and their ability to pay taxes.
- There is need for the small and medium scale enterprise to come up with measures on how to overcome the challenge of high rates of taxes.
- There is need for the small and medium scale enterprise to find means and ways on how to pay tax because taxes play an important part in the growth of the economy.

- There is need for government of Zambia through the Zambia revenue authority to set up the criteria for tax which is favorable for each sector of business.

5.2 CONCLUSION

Since small and medium scale enterprises business is a backbone of any vibrant economy, it is imperative for the Zambian government through the Zambia Revenue Authority to create a favorable tax system for these businesses. In this case, the government should adhere to tax basic principles so it can function effectively and efficiently. Specifically, the tax system should be fair for small and medium scale businesses. Moreover, the tax provisions should be clearly articulated without any ambiguity or confusion. Consequently, the tax system should be simplified and easy to understand among the common entrepreneurs who have limited understanding of tax laws and regulations. Ultimately, the tax system should be efficient so as to minimize the compliance cost for settling tax liabilities.

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