

**FACTORS AFFECTING TAX ADMINISTRATION IN THE INFORMAL SECTOR: A  
CASE STUDY OF LUSAKA DISTRICT**

**BY**

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**A Dissertation submitted to the University of Zambia in partial fulfilment of the  
requirements for the award of the Degree of Master of Science in Human Resource  
Management**

**THE UNIVERSITY OF ZAMBIA**

**LUSAKA**

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## DECLARATION

I, **Violet Mtonga**, do hereby declare that this work is my original work achieved through personal reading and research. This work has never been submitted to the University of Zambia or any other Universities. All sources of data used and literature on related works previously done by others, used in the production of this Dissertation have been duly acknowledged. If any omission has been made, it is not by choice but by error.

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## APPROVAL

This Dissertation by Violet Mtonga approved as a fulfillment of the requirements for the award of Degree of Master of Science in Human Resource Management.

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## ABSTRACT

The Study is an evaluation of Factors Affecting Tax Evasion in the Informal Sector: A case Study of Lusaka. The study was guided by the following objectives, To establish factors that lead to non-compliance on tax remittance in informal sector. To identify the challenges that affect revenue mobilization by Zambia Revenue Authority from the informal sector and to determine how ZRA can improve upon tax collection in the informal sector by incorporating good tax Administration principles, procedures and practices in Zambia. The study adopted a mixed method design that was used in this study was a convergent parallel mixed-methods design. An approach to inquiry that embeds both qualitative and quantitative methods concurrently, prioritizing both methods almost equally throughout the process of data collection. A total of sixty – eight (68) respondents were interviewed and with closed and open-ended questions. A total of three (3) ZRA key informants were interviewed with open ended questions. The research used mixed method research design in order to come up with the findings. The research also used both secondary and primary data. The empirical result obtained from the study showed that tax evasion in the informal sector is mainly influenced by low incomes, illiteracy, complicated tax processes and the tax rate been too high. The study also established that the non-permanent place of work of informal sector participants, cash-based transactions and poor record keeping in the sector were among the many challenges that the Zambian Revenue Authority faced in taxing the informal sector. The study also found out that Tax advertisement and education, increase of ZRA pay points, Mandatory registration of informal businesses would encourage the informal sector to pay tax. Finally, study has recommends among othe that the Zambian government in conjunction with ZRA should reduce tax rates, expand tax pay points, embark on serious tax education and advertisement, employ more tax administrators and simplify the process of remitting tax in order to increase tax revenues from the informal sector.

**Keywords:** *Tax Administration, Tax Evsion, Informal Sector, Zambia Revenue Authority, Tax Administrators.*

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## **DEDICATION**

This Dissertation is dedicated to my late mother Mrs Regina Manda Mtonga and my late father Mr Fredrick Mtonga who set the bar high for me and who in light of the toughest adversities re-emphasised that there was no substitution for education.

## TABLE OF CONTENTS

|  |      |
|--|------|
| <b>DECLARATION</b> .....                       | i    |
| <b>COPYRIGHT</b> .....                         | ii   |
| <b>APPROVAL</b> .....                          | iii  |
| <b>ABSTRACT</b> .....                          | iv   |
| <b>ACKNOWLEDGEMENTS</b> .....                  | v    |
| <b>DEDICATION</b> .....                        | vi   |
| <b>LIST OF TABLES</b> .....                    | xii  |
| <b>LIST OF FIGURES</b> .....                   | xiii |
| <b>LIST OF ACRONYM AND ABBREVIATIONS</b> ..... | xiv  |
| <b>CHAPTER 1</b> .....                         | 1    |
| <b>INTRODUCTION</b> .....                      | 1    |
| 1.1 Background of the Study .....              | 1    |
| 1.2 Statement of The Problem .....             | 3    |
| 1.3 Aim of Study .....                         | 3    |
| 1.3.1 Specific Objectives .....                | 4    |
| 1.3.2 Research Questions .....                 | 4    |
| 1.4 Significance of the Study .....            | 4    |
| 1.5 Scope of Study .....                       | 4    |
| 1.6 Assumptions .....                          | 5    |
| 1.8 Conclusion .....                           | 5    |
| <b>CHAPTER 2</b> .....                         | 6    |
| <b>LITERTURE REVIEW</b> .....                  | 6    |
| 2.0 Introduction .....                         | 6    |
| 2.1 Purpose of Taxation .....                  | 7    |



|  |           |
|--|-----------|
| 2.1.1 Economic Growth .....  | 8         |
| 2.1.2 Stabilization.....   | 8         |
| 2.1.3 Distribution of Income .....   | 8         |
| 2.2 reasons why non-compliance with income tax is high in the in the informal sector ..... | 9         |
| 2.3 Challenges faced by tax authorities in taxing the informal sector. ....                | 10        |
| 2.4 Good Tax Practices .....   | 11        |
| 2.6 Conceptual Framework .....   | 14        |
| 2.7 Theoretical Framework .....  | 15        |
| 2.7.1 Benefit Theory.....  | 15        |
| 2.7.2 The Sacrifice Theory .....   | 16        |
| 2.8 Summary of Chapter .....   | 16        |
| <b>CHAPTER 3 .....</b>   | <b>17</b> |
| <b>RESEARCH METHODOLOGY.....</b>   | <b>17</b> |
| 3.0 Introduction .....   | 17        |
| 3.1 Research Design.....   | 17        |
| 3.2 Target Population .....  | 18        |
| 3.3 Sample Selection .....   | 18        |
| 3.4 Data Collection Techniques .....   | 19        |
| 3.4.1 Secondary Data Collection.....   | 19        |
| 3.4.2 Primary Data Collection.....   | 19        |
| 3.5. Questionnaire (Qn).....   | 20        |
| 3.6 Interviews .....   | 20        |
| 3.7. Data Analysis .....   | 21        |
| 3.8 Pilot Study .....  | 21        |

|   |           |
|---|-----------|
| 3.9 Ethical Considerations.....   | 22        |
| 3.10 Validity and Reliability of the Study.....   | 22        |
| 3.11 Elimination of Bias.....   | 23        |
| 3.12 Limitations .....  | 24        |
| 3.13 Conclusion.....  | 24        |
| <b>CHAPTER 4 .....</b>  | <b>26</b> |
| <b>PRESENTATION AND ANALYSIS OF FINDINGS.....</b>   | <b>26</b> |
| 4.0 Introduction .....  | 26        |
| 4.1 Demographic Characteristics of Respondents.....   | 26        |
| 4.1.1 Gender of Respondents .....   | 26        |
| 4.1.2 Age of Respondents .....  | 27        |
| 4.1.3 Education Level of Respondents.....   | 27        |
| 4.2 Objective One: Factors that Lead to Non-Compliance on Tax Remittance in Informal Sector.....                          | 28        |
| 4.2.1 Compliance of the Respondents to Payment of Tax .....   | 28        |
| 4.2.2 Key Factors that Cause Non-Tax Compliance.....  | 28        |
| 4.2.3 Perception of informal Sector Business People about Tax Remittance .....  | 29        |
| 4.2.4 Chi-Square Test on the correlation between positive perception of taxes and levels of education .....               | 30        |
| 4.3 Objective Two: Challenges that Affect Revenue Mobilization by Zambia Revenue Authority from the Informal Sector ..... | 31        |
| 4.3.1 The Mobility Nature of the Informal Sector Businesses.....  | 32        |
| 4.3.2 Predominance of Cash Transactions .....   | 32        |
| 4.3.3 Poor Record Keeping .....   | 33        |
| 4.3.4 High Illiteracy Levels.....   | 34        |

|  |    |
|--|----|
| 4.4 Objective Three: To determine the Practices, Procedures and Principles that would incorporate good Tax Administration in the Informal Sector. .... | 34 |
| 4.4.1 Tax Education and Advertisement .....  | 34 |
| 4.4.2 Ease of Tax Remittance.....  | 35 |
| 4.4.3 Expansion of The Tax Pay Point.....  | 35 |
| 4.4.4 Mandatory Informal Sector Business Registration .....  | 36 |
| <b>CHAPTER 5</b> .....   | 37 |
| <b>DISCUSSIONS AND INTERPRETATIONS OF FINDINGS</b> .....   | 37 |
| 5.0 Introduction .....   | 37 |
| 5.1 Factors that lead to Non-compliance on Tax Remittance in Informal Sector .....   | 37 |
| 5.2 Challenges that Affect Revenue Mobilization by Zambia Revenue Authority from the Informal Sector.....  | 40 |
| 5.3 Incorporation of good tax administration principles, practices and procedures to incorporate good tax administration in the informal sector.....   | 42 |
| 5.3.1 Tax Education and Advertisement .....  | 42 |
| 5.3.2 Ease of Tax Remittance.....  | 42 |
| 5.3.3 Expansion of The Tax Pay Points .....  | 43 |
| 5.3.4 Mandatory Informal Sector Business Registration .....  | 43 |
| <b>CHAPTER 6</b> .....   | 44 |
| <b>CONCLUSION AND RECOMMENDATIONS</b> .....  | 44 |
| 6.0 Introduction .....   | 44 |
| 6.1 Conclusion.....  | 44 |
| 6.2 Recommendations .....  | 45 |
| 6.2.1 Reduction of Tax Rates .....   | 45 |
| 6.2.2 Tax Education and Advertisement .....  | 46 |
| 6.2.3 Ease of Tax Remittance.....  | 46 |

|   |    |
|---|----|
| 6.2.4 Expansion of The Tax Pay Points .....                                     | 47 |
| 6.2.5 Mandatory Informal Sector Business Registration .....                     | 47 |
| 6.2.6 Intensive and Regular Monitoring.....                                     | 47 |
| 6.2.7 Capacity Building.....  | 47 |
| 6.2.8 Political Incentives .....  | 48 |
| 6.2.9 Segregation of Tax Administration .....                                   | 48 |
| 6.2.10 Review of The Law in Order to Strengthen It to Address Tax Evasion ..... | 48 |
| 6.2.11. Reward System.....  | 49 |
| 6.2.12. Collaborations .....  | 49 |
| <b>REFERENCES</b> .....   | 50 |
| <b>APPENDIX I: QUESTIONNAIRE</b> .....  | 54 |
| <b>APPENDIX II: INTERVIEW GUIDE</b> .....                                       | 57 |
| <b>APPENDIX IV: INTERVIEW GUIDE</b> .....                                       | 58 |

## **LIST OF TABLES**

|  |    |
|--|----|
| Table 1: Key Factors that Cause Non-Tax Compliance.....  | 29 |
| Table 2:Chi-Square Test on the correlation between positive perception of taxes and levels of<br>education ..... | 30 |

## **LIST OF FIGURES**

|   |    |
|---|----|
| Figure 1:Gender of Respondents.....   | 26 |
| Figure 2:Age of Respondents.....  | 27 |
| Figure 3: Compliance of the Respondents To Payment of Tax .....                   | 28 |
| Figure 4:Perception of informal Sector Business People about Tax Remittance ..... | 30 |
| Figure 5: Challenges that Affect Revenue Mobilization.....                        | 31 |

## **LIST OF ACRONYM AND ABBREVIATIONS**

|        |   |
|--------|---|
| CSO    | Central Statistics Office                                 |
| IGT    | Identifiable Group Taxation                               |
| ILO    | The International Labour Organization                     |
| LCC    | Lusaka City Council                                       |
| MTN    | Mobile Telephone Network                                  |
| PACRA  | Patents & Companies Registration Agency                   |
| SPSS   | Statistical Package for Social Sciences                   |
| VAT    | Value Added Tax   |
| ZAMTEL | Zambia Telecommunications Company Limited                 |
| ZICTA  | Zambia Information and Communication Technology Authority |
| ZRA    | Zambia Revenue Authority                                  |

## **CHAPTER 1**

### **INTRODUCTION**

#### **1.1 Background of the Study**

This chapter presents the statement of the problem, the factors that affect tax Administration in the Zambian economy, which will be followed by the objectives of the study, aim of the study, scope of the study and finally a conclusion will be drawn from the discussion. This chapter will also explain what will be discussed in the next chapter.

Many developing countries including Zambia are faced with the problem of raising the necessary revenues to meet governments 'expenditures. Governments 'budgeted revenues usually fall short of the expected expenditures. Owing to the lack of liquidity on the international market due to the current financial crisis domestic revenue mobilization is seen as the most reliable source of revenue mobilization. Taxation is therefore seen as the most efficient and effective means of raising revenue domestically for the government.

Over the past four decades, like many emerging economies, Zambia's informal sector has experienced rapid growth. A lot of informal, unregistered and unregulated businesses have mushroomed in city centres such as city market, Soweto market, and inter-city bus terminus as well as city streets alike. The formation of the informal sector has largely been influenced by the limited employment opportunities in the formal sector which accounts for only 11% of the country's total labour force, in a country with a population of over 16.59 million people (Zambia Labour Force Survey, 2016).

With respect to revenue, the informal sector forms a large, and, in many countries, growing share of gross national product, and thus represents a potentially significant source of revenue (Schneider and Klinglmair 2004, Schneider et al, 2010) which becomes crucial for reducing budgetary deficits, improving monetary policy, carrying out social-economic projects such as infrastructure development and in the long term, building a sustainable economy. It is of general consensus among many tax experts that broadening the tax base in emerging economies is highly



dependent on the ability of the tax system to actualize the tax potential of the informal sector as opposed to further taxation of the already highly burdened formal sector. In Zambia, however, despite the arguably evident tax potential of the informal sector, Zambia's tax regimes have not duly been effective in ensuring the maximum collection of taxes in the informal sector.

The concept of taxing the informal sector is not a new phenomenon. Extensive research by different scholars has been carried out on the topic, as such; there exists different schools of thought on the topic. For example, Prichard (2009) advocates that the informal sector needs to be exempted from paying taxes because the sector is alleged to be the poorest sector of any given economy, therefore, taxing the sector would shrink the business potential of most participants of the sector and consequently reinforce the poverty cycle (Ibid, 2009:72). On the other hand, scholars like Joshi (2002), argue that the informal sector should be taxed extensively; especially that it forms the largest sector of an economy in most developing countries (Joshi, 2002: 31). Joshi's prepositions have shaped current debate; recent literature has focused more on finding effective and sustainable ways of taxing the informal sector as opposed to the conventional argument of whether or not the informal sector should be taxed.

In the recent past many developing countries have subscribed to the notion of broadening their tax base by means of effectively taxing the informal sector and this is evidenced by the many different tax reforms that governments in such countries have embarked on over the past four decades. For example, in Ghana, the Ghanaian government in the 1990's introduced the Identifiable Group Taxation (IGT), a form of associational taxation, which used informal sector associations as tax collection agents. These associations collected tax from their members on a daily or weekly basis in order to reduce the burden on low-income members having to pay large lump sums. Similarly, the South African government in 2010 introduced tax reforms that were aimed at including the informal sector in the country's tax net. In the same fashion, the Zambian government in 2004 introduced similar tax policies such as presumptive taxes on public service vehicles intended for the informal sector, but just like in the case of South Africa and Ghana, Zambia's informal sector still remains untaxed.

## **1.2 Statement of The Problem**

Zambia's informal sector has grown to levels of up to 89% of the country's economic activities, leaving only 11% to the formal sector (Zambia Labour Survey, 2016). Despite this growth, the informal sector's tax contribution remains proportionately low, and in an effort to maximise the sector's tax contributions, the government of Zambia in 2004 put in place deliberate tax policies such as the presumptive tax on public service vehicles, the turnover tax and advance income tax. However, these policies have not yielded much and the informal sector has remained the largest untaxed sector due to tax evasion and no compliance of income tax from the informal sector with its tax contribution accounting for less than 10% of the country's total tax revenue (Zambia Labour Survey, 2016) which has consequently left the Zambian government incapacitated to mobilize the much-needed revenue for undertaking critical social economic projects.

As a rapidly urbanizing country that has struggled to generate sufficient structural transformation to create formal jobs (Resnick and Thurlow 2017), the informal sector remains the main source of employment in Zambia. Within the capital of Lusaka, 72 percent of the labour force works in the informal sector (Central Statistical Office 2019), and this rate has barely shifted over the last decade. Many of those within the sector labour as traders, tailors, hairdressers, or food sellers within the city's more than 60 open-air markets, or they hawk their goods along the capital's streets. Since 2004, the Zambian Revenue Authority (ZRA) has applied a range of informal sector taxes, including a base tax on marketeers, a turnover tax on businesses with turnover falls below a certain threshold, a tax on minibuses and taxi drivers, and an advance income tax on imports by cross-border traders who are not registered with the ZRA. In addition, there are a range of taxes collected by the Lusaka City Council (LCC) and the market cooperatives that allow individuals to trade or run a business in the markets.

## **1.3 Aim of Study**

Due to the increase in volume of businesses in Zambia's informal sector and the difficulties that ZRA encounters to collect tax from them, the aim of the study was to examine the factors affecting tax Administration in Zambia's informal sector.

### **1.3.1 Specific Objectives**

The study aimed at achieving the following:

1. To establish factors that lead to non-compliance on tax remittance in the informal sector.
2. To identify the challenges that affect revenue mobilization by Zambia Revenue Authority from the informal sector.
3. To determine the factors that would incorporate good tax administration principles, procedures and practices in Zambia

### **1.3.2 Research Questions**

1. What factors lead to non-compliance on tax remittance in informal sector?
2. What challenges affect revenue mobilization by Zambia Revenue Authority from the informal sector?
3. How can ZRA improve upon their tax collection in the informal sector by incorporating good tax administration principles, procedures and practices in Zambia?

### **1.4 Significance of the Study**

The study would help policy makers to be able to understand the factors underlying the individual's decision as to whether to pay taxes or not. Also, it would help the self-employed in the informal sector to know their rights as taxpayers and besides, they would be motivated to appreciate the need to pay taxes regularly and on time.

Again, since the study unveiled some of the problems associated with tax collection in the informal sector in Lusaka, Zambia and recommend ways of solving them, it would serve as a guide to management for future policies and programs relating to tax collection in the informal sector. In addition, it would provide some directions for future research and serve as source of reference for future research into the subject matter.

### **1.5 Scope of Study**

The study covered all informal sector businesses such as hairdressers (saloons and Barbershops), Mechanic, Fabricators, carpenters, artisans, Food vendors in Lusaka's central Business District.

The area considered as the Central Business District in this study was the grid plan section of Lusaka, extending from Kabwe Roundabout in the North of Kafue Roundabout in the South and from the Railway line to Lumumba Road in the west.

The study area was purposively chosen because the area is home to many of Lusaka's informal businesses that are purported to be evading tax. As such, the researcher had fewer challenges in locating informants of the study.

### **1.6 Assumptions**

The researcher's assumptions in this research were that the respondents would be truthful about why they do not pay tax and give reasons why they do not pay tax. The researcher assumed that people would be honest to give their own opinions because it is hard to collect tax from the informal sector and ZRA has tried to come up with ways in order to collect tax from the informal sector but it has not fully succeeded. The researcher also assumed that the respondents from ZRA would be honest about the factors that make it difficult for them to collect tax from the informal sector and how they can improve on tax collection in the informal sector.

### **1.8 Conclusion**

In conclusion, this chapter sought to find out the source of evasion of tax in Zambia's informal sector which led to the main objective of the research carried out in order to find out the factors affecting tax Administration in Zambia's informal sector. The area considered as the Central Business District in this study was the grid plan section of Lusaka, extending from Kabwe Roundabout in the North of Kafue Roundabout to the South and from the Railway line to Lumumba Road in the west. The study area was purposively chosen because the area is home to many of Lusaka's informal businesses that are purported to be evading tax. As such, the researcher had fewer challenges in locating informants of the study. The next chapter will discuss the literature review of the research.

## **CHAPTER 2**

### **LITERATURE REVIEW**

#### **2.0 Introduction**

This chapter defines the key terms of the research such as Taxation, informal sector, Tax evasion and Tax Administration. This will be followed by literature review on what other scholars have said about tax administration worldwide. Then a conceptual and theoretical framework of the research will be given.

The evolution of the informal sector and the complexity of tax evasion have come with different definitions and interpretations of what the terms mean. Different scholars have coined and characterized the two phenomena differently. For example, Hartzenberg and Leimann (1992) defined the informal sector as all economic activities pursued without the sanction of the authorities.

Joshi (2014) differentiated the informal sector from the formal using the legal status of businesses as the drawing line. According to him, the informal sector consists of all unregistered businesses operating in an economy without complying with relevant legislation (Ibid; 89). The International Labour Organization coined the informal sector as a variety of businessmen such as carpenters, masons, tailors and other tradesmen, as well as cooks and taxi-drivers, offering nearly the full range of basic skills needed to provide goods and services for a larger though often poor section of the population (ILO, 2013).

According to James and Nobes (1997) tax evasion is an act of not respecting the tax law and rules of a country by not paying the tax or by not declaring the true value of the actual income. Kesselmen (1997) goes on to define tax evasion as performing an illegal act of avoiding paying tax. The process of tax evasion involves non-reporting, understatement, or misreporting of taxable income, profits, or sales (Kesselmen, 1997).

Taxation is a sovereign right of the state used to transfer resources from private to public use in order to achieve the economic and political goals of society (Bird, 1992).

According to Bannock et al., (1998) taxation is a compulsory transfer of money (or occasionally of goods and services) from private individuals, institutions or Groups to the government.

The US Treasury Department also defined it as a compulsory payment for which no specific benefit is received in return (Slavin, 1999). Tax policy is concerned with the reasoning behind how much revenue the government is collecting, what the revenue is being used for, and whether the government is collecting revenue in the most appropriate way.

The Vocabulary dictionary defines Evasion as “Evasion means "dodging something you are supposed to do" like your evasion of your chores by pretending to be sick. Evasion can also mean "the deliberate act of failing to pay money," like tax evasion, not paying your taxes. Though evasion comes from the Latin word *evadere*, "to escape," if you owe the government money, you'll surely be caught eventually”.

According to Wikipedia Tax Administration is the Planning, directing, supervising and evaluating the levy and collection of national tax administrations and local tax administrations. Directing, supervising and evaluating the anti-corruption efforts of all levels of tax administration

Tax Administrations, like private companies and other organizations, have a core business. The core business of Tax Administrations is the levying and collection of taxes imposed by law. It is important that Tax Administrations establish a clear definition of their core business from the outset and make it known to their stakeholders. The core functions of a Tax Administration include inter alia:

## **2.1 Purpose of Taxation**

The imposition and collection of taxes is simply one of the fundamental policy instruments use to achieve governmental social and economic goals. The objectives of tax policy are similar to those of public policy in developing countries and overlap with the purposes of the tax system or the purpose of most governments. Edgar and Sandler (2005) revealed that there are five purposes for collecting revenue through taxes: to give government power to allocate resources; to enable government to provide/support social development; to stabilize the economy; to constitute and define the market place; and to encourage optimal economic growth. Furthermore, three of these

are of greatest urgency in developing countries: economic growth; internal and external stability; and ensuring that incomes are distributed appropriately.

### **2.1.1 Economic Growth**

Most developing countries are extremely focused on economic growth in both the private and public sectors. Even in primarily market-based economies, governments need to acquire assets for public sector capital formation and development related expenditures (Bird, 1992). There appears to be no limit to the tax gadgetry used in different countries to stimulate economic growth. Most developing countries encourage foreign direct investment to stimulate economic growth through the use of tax incentives and many developing countries impose higher taxes on retained profits than on distributed profit in order to encourage distribution. However, the effectiveness of some of the policies especially of incentives remains uncertain because there is still insufficient data to link such policies with growth performance (Shihata, 1991).

### **2.1.2 Stabilization**

The use of tax instrument to enhance economic stability is important in developing countries because this enable them to ensure elasticity with respect to changes in the value of money and income levels. If tax yields rise when national income rises, governments have less need to rely on deficit financing to maintain and expand the level of public – sector activity in a growing economy (Bird, 1992).

### **2.1.3 Distribution of Income**

The distributional role of taxes in developing countries is another important purpose of tax system. Disparities in income can block development and increase demands for government social spending. The main redistributive tax in most tax systems is personal income tax (Zee, 2005). In practice, the personal income tax in developing countries is far from being progressive due to large disparities in incomes. These disparities are compounded by the influence of the rich, who may end up paying fewer taxes due to numerous exemptions or favours from the Government.

## **2.2 reasons why non-compliance with income tax is high in the informal sector**

A study to investigate the determinants of tax evasion in the informal sector among artisans carried out by Slemrod (2011) examined the consequences of the marginal tax rate on the rate of tax compliance. The study found that the high tax non-compliance in the informal sector was as a result of the marginal tax rate. According to Slemrod (2011), the higher the tax rate, the less likely that informal sector participants will comply with the laid down tax laws. The study found that most informal sector participants felt the tax rate was high, beyond what their business could afford to remit. While Slemrod's study offers a valuable explanation of a plausible cause for tax evasion in the informal sector, there is need to exercise caution before the results of the study could be generalized.

In a similar study, Sousa et al (2012) measured the impacts of import taxes on tax evasion in the informal sector and found that a rise in the import tax rates directly triggered tax evasion among informal sector businesses. Sousa's study argued that informal traders who are involved in imports find paying tax as an unnecessary expense which potentially reduces the profit margin of the business as they would have already spent on the import taxes. Although Sousa's study finds a comprehensive causal relationship between import taxes and tax evasion, a number of questions regarding his findings remain to be addressed. For example, the study focuses solely on informal sector participants who are concerned with importing of tradable goods and are influenced to evade tax on income by virtue of their expense on import taxes. However, the informal sector is characterized by many different participants such as farmers, artisans and hawkers who do not incur any expenses on import tax, therefore, import tax cannot be justified as the means for evading tax. Therefore, Sousa's study cannot be considered as conclusive because the study only targeted a unique group of informal sector participants, the import traders.

Another study by Jackson and Milleron (1986) established that tax evasion in the informal sector was highly driven by the complexity and the evolution of the tax system over time. The study found that because tax systems are modernized and become more complex over time in both developed and developing countries around the world, the complexity of these tax systems become a major tax evasion determinant, particularly in the informal sector, where it is purported



most participants are illiterate and fail to cope with the modernity and complexity of the tax system (Jackson and Milliron 1986; Richardson and Sawyer, 2001).

Previous research that has used archival and survey data methodologies such as Clotfelter (1983) and Vogel (1974) have provided stronger empirical evidence that show a positive relationship between the complexity of a tax system and tax evasion in the informal sector. Although Jackson and Milliron's research did not use the most vigorous research methodologies, their results appear consistent with prior research, as such, the results of this study to a large extent can be generalized.

Mustafa (1996) in his study carried out in Malaysia investigated the perceptions of taxpayers in the informal sector on whether they felt the tax system was complex or not and if this in any way influenced them to evade tax. The study found that the Malaysian tax system was complex and the presence of the complexity, particularly in terms of record keeping, too much detail in the tax law and ambiguity influenced the extent to which the informal sector participants were able to remit tax. Mustafa's findings were consistent with the results in a recent study by (McKerchar, 2001; 2003) who found that there were six potential complexity parameters of tax systems which were labelled as: ambiguity, calculations, changes, details, forms and record-keeping and this greatly influenced tax evasion in the informal sector.

### **2.3 Challenges faced by tax authorities in taxing the informal sector.**

In 2010 Prichard (2010) carried out a study to investigate the different challenges that tax authorities face in taxing the informal sector. The study was a cross sectional study done in three countries that is Malaysia, India and Indonesia. In his study, Prichard (2010) found that one of the reasons that make the informal sector hard to tax is the capacity constraint. The study found that due to the complex nature of the informal sector coupled by the large numbers of participants, most tax authorities in developing countries lack the resources (technology, materials and people) to initiate, implement, monitor and enforce tax laws (Prichard, 2010).

Just like Prichard (2010), Joshi (2009) also studied the different challenges faced in taxing the informal sector. The study found that political interference was one of the biggest challenges that taxing authorities were faced with in their effort to maximise the tax potential of the informal

sector. Joshi (2010) indicated that informal sector workers form the largest population of voters and as such tax officials are pressurized by politicians to turn a blind eye to the activities in the informal sector. State authorities and legislators deliberately ignore to exercises in the informal sector with a specific end goal to hold their support base; at the same time, organize informal division workers to literally force government authorities to decrease enforcement (Joshi, 2009). Tendler (2016) arrive at similar findings as those of Joshi (2009).

Tendler (2016) argue that there are inherent agreements made by government officials, that permit taxation rates to be reduced on non-formal and small business activities in return for political vote (Tendler, 2010). This is the thing that Tendler has coined the —devil's deal. — Vote for me and I will shield you from paying taxes, I will be your godfather and defend you in times of trouble, you would not be harassed by public officials because we will be there for you be it environmental or labour regulations; and I will protect you from the police and tax inspectors from troubling you (Tendler, 2010).

Another study carried out in Ghana by Emmanuel (2009) indicated that the predominance of cash transactions, lack of laid down procedures, poor record keeping, little or no barriers to entry and the peripatetic nature of the informal sector makes it hard to tax the sector (Emmanuel, 2009). This study focused more on the technicalities of business management; however, the current study will take a holistic approach to factors that make the informal hard to tax.

## **2.4 Good Tax Practices**

In their study, (Loo *et al.*, 2009) found that education attainment is one among other key determinants of tax evasion in the informal sector.( Loo et al, 2009) claim that that education has two elements: the general degree of fiscal knowledge and the specific degree of knowledge about tax evasion opportunities. They claim that by enhancing the level of general fiscal knowledge, tax compliance improves due to more positive perceptions about taxation. Increased knowledge of tax evasion opportunities has a negative impact on tax compliance as it aids non-compliance. Although very insightful, the findings of Loo *et al's* study are discredited on account of the methodology used to come up with the conclusions of the findings. The study was a

desktop study that purely used secondary data without collecting first-hand information on issues concerning the causes of tax evasion in the informal sector.

Developing countries increasingly rely on simplified taxes for assessing the informal sector that often take the form of so-called presumptive taxes. Under a presumptive tax regime, tax liabilities are estimated on the basis of simple indicators of business performance (such as turnover) or certain “visible” firm characteristics (such as transport capacities), and taxes are often paid on a lump-sum basis. The rationale behind presumptive taxes is to collect some additional tax revenues with a reasonable amount of administrative and tax compliance costs (Dube & Casale, 2016), which somehow mirrors the economic “cost-benefit-analysis” described earlier.

In a recent publication, Dube & Casale (2016) provide some evidence on presumptive taxation in four countries in Sub-Saharan Africa (Ghana, Tanzania, Zambia and Zimbabwe). Although the presumptive taxes vary greatly with respect to their design, coverage and implementation, there are some common observations regarding their effectiveness and efficiency, which turns out to be generally limited. Some tax administrations found it difficult to implement the presumptive taxes due to severe capacity limitations, in particular with respect to adequate manpower. Administrative constraints also sometimes lead to a lack of monitoring and enforcement, so that taxpayers failed to pay. The lack of compliance was also stressed by the fact that taxpayers were not informed about the taxes, and that they questioned the legitimacy of tax collectors.

To examine drivers of tax compliance and implications for representation among informal workers in Zambia’s capital city. Informal employment in Zambia is defined as employers and business owners who have not registered their enterprises with a national authority, such as the Patents and Companies Registration Agency (PACRA), as well as those who lack contributions to a social security scheme and entitlements to annual paid and sick leave (Goursat and Pellerano, 2016).

The informal economy represents not only a major contributor of employment for Lusaka’s residents but also a critical source of foods for low-income households in the city (Mulenga, 2013). The growth in Lusaka’s informal economy is closely tied to Zambia’s broader economic

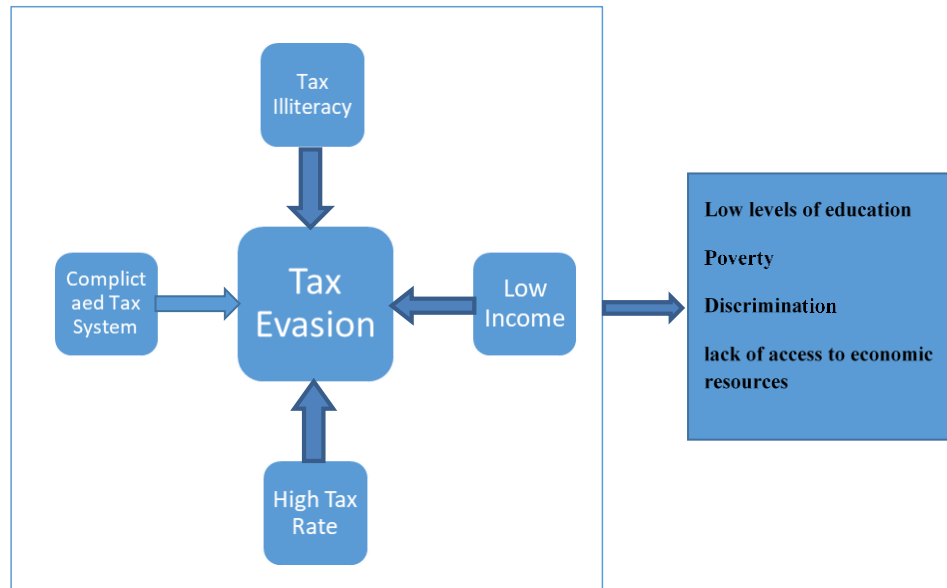
decline in the early 1990s when manufacturing contracted in the wake of privatization and trade liberalization. Not only did the number of jobs in the formal sector decline but also the removal of controls on foreign exchange, imports, and prices reduced barriers to entry into the informal trade sector (Hansen, 2007)

In addition to agricultural products, second clothing, known locally as *salaula*, became a major source of merchandise among informal traders during this period because unlike some other African countries, Zambia did not place quotas on these imports (Hansen, 2000). By 2008, three-quarters of Lusaka's labour force worked in the informal economy, a level that persisted almost a decade later (Central Statistical Office, 2011).

As a rapidly urbanizing country that has struggled to generate sufficient structural transformation to create formal jobs (Resnick and Thurlow 2017), the informal sector remains the main source of employment in Zambia. Within the capital of Lusaka, 72 percent of the labour force works in the informal sector (Central Statistical Office 2015), and this rate has barely shifted over the last decade. Many of those within the sector labour as traders, tailors, hairdressers, or food sellers within the city's more than 60 open-air markets, or they hawk their goods along the capital's streets. Since 2004, the Zambian Revenue Authority (ZRA) has applied a range of informal sector taxes, including a base tax on marketers, a turnover tax on businesses with turnover falls below a certain threshold, a tax on minibus and taxi drivers, and an advance income tax on imports by cross-border traders who are not registered with the ZRA. In addition, there are a range of taxes collected by the Lusaka City Council (LCC) and the market cooperatives that allow individuals to trade or run a business in the markets.

Taxation is always political and especially so in Zambia where, during the multiple electoral campaigns of the Patriotic Front under the late president, Michael Sata, the slogan of "more jobs, lower taxes, and more money in your pockets" resonated strongly among urban marketers and street vendors (Resnick, 2014). In Zambia and elsewhere, the trade-off between needing money and not wanting to excessively burden the poor is a common challenge.

## 2.6 Conceptual Framework



**Figure 1.** Conceptual Framework of Tax Evasion in Zambia

In the model above, the dependent variable is tax evasion which is a function of the independent variables, high tax rate, the tax system, tax illiteracy and low income.

**1. Tax Literacy:** involves providing information about Taxation. Tax literacy can be done through the distribution of brochures, leaflets, talk shows and taxpayer's days. On the other hand, Tax illiteracy is the opposite of Tax literacy. High levels of Tax illiteracy will lead to high levels of tax evasion. If people are given adequate tax education the levels of tax evasion would go down.

On the other hand, the informal sector has a high number of people with low incomes.

**2. Low Incomes:** contribute to high levels of tax evasion. This is because people find it difficult to give part of the low incomes made to the government due to the hardships of the economy. The large number of potential taxpayers in the informal sector, and the difficulties of monitoring "hidden" entrepreneurs and small-scale firms, can give rise to serious revenue collection costs for tax authorities in developing countries. At the same time, the revenue potential of taxpayers in the informal sector is fairly modest, as their taxable incomes are usually quite low (Joshi et

al., 2014). Informal sector activities are often located in rural areas or come from self-employed sellers living near the subsistence level (La Porta & Shleifer, 2014).

**3. High Tax Rates** are also a cause of tax evasion. When the tax rate is high there will be more tax evasion in a country. Higher tax rates provoke tax evasion. The reaction of people in that country becomes so intense that "tax increases may even produce a reduction rather than an increase in tax revenues.

**4. Complex tax systems** due to the simplicity of the tax structure, it is clear that complex tax systems favour evasion and avoidance, in as much as they create uncertainty with respect to scope of the tax regulations, increase the costs of examination and compliance and multiply the *evasion* and avoidance formulas or mechanisms.

## **2.7 Theoretical Framework**

This study rested on two theoretical underpinnings:

### **2.7.1 Benefit Theory**

The Benefit Theory proposes that the state is supposed to levy taxes on businesses according to the benefits conferred on them. The theory implies that, the taxes paid by an individual or a business should be commensurate to the benefits derived from the activities of the state. This theory seeks to ensure that each individual's tax obligations are as far as possible based on the benefits that he or she receives from the enjoyment of public services (Luoga, 2010). Applying this theory in the Zambian informal setting would be such that, different informal sector participants for example, bus operators, artisans or construction workers would pay tax only to an extent to which they benefit from government facilities such as infrastructure. In this regard, informal sector participants would avoid paying tax if they feel they are not benefiting from any government public services.

The benefit theory has been criticized on the premise that the expenses incurred by government are for the purpose of benefiting all members of a society, as such, it is practically impossible to

estimate the benefits enjoyed by every individual in isolation of the whole society (Ibid, 2010: 87).

### **2.7.2 The Sacrifice Theory**

The sacrifice theory suggests that tax compliance or indeed the remitting of taxes is heavily dependent on the sacrifice that an individual or business makes towards the support of the government (Luoga, 2010). The measure of such sacrifice is found in the giving up of enjoyments, which is, giving up a portion of individuals' means (income) of satisfying wants (consumption). Practically the sacrifice theory demands that individuals should only pay tax on that portion of income that is spent on luxuries, the sacrifice should only be in respect of individuals' means over and above subsistence (Ibid, 2010: 87). In the Zambian informal sector context, the sacrifice theory would be hard to implement because many businesses in the informal sector are small to medium businesses that enjoy less to zero luxuries hence creating a trade-off between what is a surplus in the business and what should be channelled towards tax would almost be blurry.

## **2.8 Summary of Chapter**

Without ignoring the fact that literature reviewed herein has provided insights for the present study, it is vital to make overall comments on the literature. To start with, studies on the international arena though providing vital insights do not provide a contextual basis of application of the findings to the Zambian context. Further, these findings may not necessarily be applicable in Zambia because of the disparities in many social-economic areas of the study areas in the literature and the Zambian set up. It can further be argued that the methodologies employed by literature reviewed herein included, desktop reviews, mixed methods among others which may have had their own demerits as far as reaching conclusive findings was concerned. To add on, the samples of some of the studies also extended to tax evasion in the formal sector. However, the reviewed literature provided an entry point for exploring new insights on tax evasion in the informal sector. The next chapter describes the research method and processes that were used in the collection of data, procedures and techniques used in data analysis and the presentation of data.

## **CHAPTER 3**

### **RESEARCH METHODOLOGY**

#### **3.0 Introduction**

This chapter describes the research method and processes that were used in the collection of data, procedures and techniques used in data analysis and the presentation of data. This chapter therefore will focus on the research design, target population, sample design and data collection and analysis applied during the study.

#### **3.1 Research Design**

According to Adèr, Mellenbergh, & Hand (2008), a research design is the outline for a study. Its main purpose is to lay out the research questions, with appropriate data to be collected and used, and how the results are to be analysed (Adèr, Mellenbergh, & Hand, 2008). The study adopted a mixed method as a way of data collection. It is imperative that both approaches be incorporated in the study because as Ritchie and Lewis assert, it is not possible to know the extent and consequences of something through quantitative measurement alone, but there often are occasions where the contexts or consequences need to be understood at a deeper level and for which a qualitative investigation is needed (2003).

The type of mixed method design that was used in this study was a convergent parallel mixed-methods design. An approach to inquiry that embeds both qualitative and quantitative methods concurrently, prioritizing both methods almost equally throughout the process of data collection, analysis, interpretation and presentation (Creswell and Clark, 2011). In other words, a parallel convergent mixed-method design occurs when the researcher collects and analyses both quantitative and qualitative data during the same phase of the research process and then merges the two sets of results with same weight into an overall interpretation. A researcher collects both quantitative and qualitative data, analyses them separately, and then compares the results to see if the findings confirm or disconfirm each other. Sambili (2000) supported the combination of the methods so as to reveal many ways to deal with shortcoming of each approach and to double-check findings by examining them from different angles. In terms of priority, both qualitative



and quantitative approaches were given equal weight and in terms of sequence the researcher collected both quantitative and qualitative data at the same time (Lyambanino, 2016).

While qualitative research method was used to interpret the data within the context of the study, quantitative research method answered questions like “how many” and “how often”, while the qualitative research method answered questions like “why”. The research sought to find out how many and how often businessmen and women in the informal sector evade tax, in this case quantitative data was used because the research sought to find out the number of people evading tax in Zambia’s informal sector. In this research, therefore quantitative data was collected so as to assess the impact or the widespread of tax evasion among the businessmen in the informal sector; while qualitative data was collected so as to determine the factors that would incorporate good tax principles and practices in collecting tax from the informal sector.

### **3.2 Target Population**

Population refers to the whole group of individuals with similar or common characteristics. It is also perceived as the larger group from which the sample is derived (Kombo and Tromp, 2006). The target population of this study included all the informal sector participants in Lusaka’s Central Business area. These are men and women who own small businesses such as hairdressers and beauticians, mechanics, artists, carpenters, fashion designers, food vendors, butchers and fabricators these respondents were targeted to establish how tax administration in the informal sector was being done as well as establishing the factors that led to tax evasion in the informal sector.

### **3.3 Sample Selection**

A sample is a portion or part of individuals that are selected from an entire group of people that have at least one feature in common (Kasonde-Ng’andu, 2013). The researcher used Cluster Random Sampling to sample out the informal sector business owners. This was done in two stages; firstly the researcher divided the respondents according to the sectors Hairdressers and Beauticians, Mechanics, Artists, Carpenters, Fashion designers, Food vendors, Butchers and Fabricators; and then secondly, the researcher divided the respondents according to the streets they operate from in Lusaka Central business Area and the Streets sampled were Soweto Market,

City Market, Katunjila Road, Katondo Street, Nkwazi Road, Freedom Way, Lumumba Road, and Chachacha Road. Hence from 9 different sectors and 8 different streets, the total number of respondents came to 72. These helped to provide most of the quantitative data (which was very cardinal for assessing the impact of the situation) needed for the research.

For in-depth and qualitative data, 3 key informants from Zambia Revenue Authority HQ were selected purposively these responded to all range of questions on all the objectives of the study such challenges faced by Human Resource Officers in implementing SHRM practices among tax administrators at by ZRA; suggesting measures that can be put in place to enhance the collection of tax from the informal sector.

### **3.4 Data Collection Techniques**

Both Primary and Secondary data were collected in this research and can be explained as follows;

#### **3.4.1 Secondary Data Collection**

Secondary data is research data that has previously been gathered and can be accessed by researchers. In this research therefore secondary data was collected through a desk review method. Existing literature such as Journals, Reports from government institutions, Text books, and Research work from previous researchers were used to collect secondary data. These documents were collected from Government Public Service Departments, Libraries, Internet searches, Censuses and Surveys. Secondary data proved to be very important to this research as it provided vital information such as how the trends on tax evasion have been in the past. It also gave insight to the researcher to understand more on the topic in question. This information could not be captured using primary data.

#### **3.4.2 Primary Data Collection**

Primary data is original data that researchers collect for a specific purpose. Primary data was cardinal to this research. Importance of primary data collection is that it acts as a source of empirical evidence on the topic under investigation.

In this research, there were two main sources of primary data. The first source was the survey that was taken by the researcher through the distribution of questionnaires to Informal business operators in Lusaka Central Business Centre; and the second source were the interviews that were conducted by the researcher with 3 Informants from the Zambia Revenue Authority. Primary data proved to be very important to this research as it provided information on the current prevailing situation on tax evasion among Informal Business Operators.

### **3.5. Questionnaire (Qn)**

According to Kumar (2005), a questionnaire is a written list of questions, the answers to which are recorded by the respondents. The questionnaire was meant for the survey for the 72 respondents who were business owners in the inform sector.

### **3.6 Interviews**

An interview as defined by Leedy and Ormond (2001) is an oral administration of a questionnaire. This study used semi-structured interviews. Semi-structured interviews contain the components of both, structured and unstructured interviews. In semi-structured interviews, interviewer prepares a set of same questions to be answered by all interviewees. At the same time, additional questions were asked during interviews to clarify and/or further expand certain issues. This is so in order to allow the respondents to express themselves as comprehensively as possible for each asked question, as well as follow-up questions resulting from issues brought up by the respondents themselves.

In this research three key informants from ZRA because they have experience and knowledge about the collecting tax from the informal sector. The interviews were conducted separately in order to avoid the respondents from influencing each other when responding to the questions. To ascertain consistency and accuracy in their responses, similar questions were rephrased and asked differently. The interviews are qualitative in-depth interviews with people who know what is going on in the community. The purpose of the strategic key informant interviews was to collect information from different people of the community including community leaders, professionals, or residents who have first-hand knowledge about the community. These community experts,

with their particular knowledge and understanding, provided insight on the nature of problems and gave suggestions for solutions on tax administration in Zambia's informal sector.

### **3.7. Data Analysis**

For quantitative data, SPSS (Statistical Package for Social Sciences) version 16.0 was used to analyse data. SPSS is the set of software programs that are combined together in a single package. The basic application of this program is to analyse scientific data related with the social science. This data can be used for market research, surveys, data mining, etc. Before the data was entered into the SPSS, the questionnaires were coded. Coding converts the data from word form into computer language. Then the information was entered into the database created in SPSS. The SPSS was used to generate measures of central tendencies, relationships between variables and to what extent independent variables affected the dependent variables. Analysed data was then presented in form of Tables and Figures for easy of interpretation of key findings to the research. For qualitative data, data from interview guides was categorised according to the objectives of the research before analysis.

### **3.8 Pilot Study**

A pilot study is a small-scale study that helps them refine their research topic and study methods. Pilot studies can be used in both quantitative and qualitative social science research. Therefore, before conducting this study, pilot study was conducted so as to test the research tools, determine the best research methods to use, troubleshooting unforeseen issues in the project, and determining whether a research project was feasible. In this case, the pilot study was conducted in Chilanga's Freedom market. A sample of 20 people was selected as respondents to help with the exercise. The researcher used Chilanga's Freedom Market and not Lusaka Central Business Centre because the researcher did not want the pilot study to affect the actual survey. Results from the pilot study showed that the respondents were able to answer the questionnaires without difficulties hence the reason why the researcher classified the questionnaires as self-administered.

### **3.9 Ethical Considerations**

This study took into account research ethics such as not answering research questions on behalf of the respondents and exercising confidentiality as a researcher concerning the respondent's participation. In cases where privacy of any individual or subject was concerned and where such issues arose; clearance was obtained from the University of Zambia Ethics Committee. Anonymity of participants was guaranteed in both data collection and processing. This was done by using members, groups, averages, percentages, official titles, organization or department names, as opposed to using names of participants. Observing anonymity helped to avoid biased responses from participants in this study, Bless and Achola (1998). Participants were also assured that the information given would be treated with confidentiality and that data would be used for the stated purpose of research, that is, academic and that, where possible, government may access the report documents but not necessarily the interview data. Assurance of confidentiality made respondents feel free to give honest and complete information, mostly, where data was collected by using interview methods.

### **3.10 Validity and Reliability of the Study**

Validity can be seen as the core of any form of assessment that is trustworthy and accurate (Bond, 2003:179). Validity, according to Messick (1989) always refers to the degree to which empirical evidence and theoretical rationales support the adequacy and appropriateness of interpretations and actions based on test scores. Borsboom, Mellenbergh and van Heerden (2004, p. 1061) have a different take on validity stating that: "a test is valid for measuring an attribute if the attribute exists and variations in the attribute causally produce variation in the measurement". They do not agree with Messick's conception of validity. In this study Messick's viewpoint will be followed. On the whole, validity is seen as a unitary concept. An example would be if various researchers had to examine one specific research study and also come up with the same conclusion, then the research study would be internally valid. Conversely, with external validity the results and conclusions can be generalised to other situations or with other subjects. This research was seen to be valid as the outcomes of the research were in line with the theories that the research adopted. These theories have been used by other previous researchers who did

similar research work to this one. The researcher also did some comparisons with other outcomes from other researchers to validate outcomes of this research.

A test is seen as being reliable when it can be used by a number of different researchers under stable conditions, with consistent results and the results not varying. Reliability reflects consistency and if it is replicable over time. Furthermore, reliability is seen as the degree to which a test is free from measurement errors, since the more measurement errors occur the less reliable the test (Fraenkel & Wallen, 2003; McMillan & Schumacher, 2001, 2006; Moss, 1994; Neuman, 2003). In the same way, Maree and Fraser (2004) ask how far the same test would produce the same results if it was administered to the same children under the same conditions. This helps the researcher and educator to make comparisons that are reliable.

The more errors found in an assessment the greater its unreliability, and vice versa. Reliability is a very important factor in assessment and is presented as an aspect contributing to validity and not opposed to validity. To ascertain the reliability of the research tools, the researcher did a pilot survey in Chilanga's Freedom market and made some changes where the tools seemed to be failing. This gave confidence to the researcher during the actual survey. This research also used empirical investigations by means of Research analysis. Following Messick's (1989) concept of validity and reliability interrelating within an assessment. These empirical investigations that took place led the study to integrate a Positivist theoretical framework which aided in investigating the items and the level of validity of the assessment distinct from the learners or other factors.

### **3.11 Elimination of Bias**

Bias is any trend or deviation from the truth in data collection, data analysis, interpretation and publication which can cause false conclusions. Bias can occur either intentionally or unintentionally. Intention to introduce bias into someone's research is immoral. Nevertheless, considering the possible consequences of a biased research, it is almost equally irresponsible to conduct and publish a biased research unintentionally. This research tried as much as possible to eliminate bias in data collection, data analysis and data interpretation. One of the ways of eliminating bias, the researcher avoided conducting the research in one area of the business centre

hence the decision to conduct the research in 8 different streets of Lusaka Central Business Area. Another way to eliminate biasness, the researcher avoided interviewing business men and women with the same type of business hence the use of random sampling. The researcher also avoided interviewing multiple respondents at the same time. Finally, the researcher avoided asking leading questions.

A researcher can introduce bias in data analysis by analysing data in a way which gives preference to the conclusions in favour of research hypothesis. By interpreting the results, one needs to make sure that proper statistical tests were used, that results were presented correctly, and that data are interpreted only if there was a statistical significance of the observed relationship. During analysis, the researcher avoided biasness by not doctoring the data when results did not come as expected. Instead, the researcher considered other variables that may have not been considered in the research so as to establish the reason why some outcomes may not have come out as expected in the hypothesis.

### **3.12 Limitations**

The research was strictly carried out in Lusaka district. The area considered as the Central Business District was the grid plan section of Lusaka, extending from Kabwe Roundabout in the North to Kafue Roundabout in the South and from the Railway line to Lumumba Road in the west. This was a limitation as it does not depict the views of the whole Lusaka District business operators. However, to avoid getting same or bias responses, the researcher conducted the research in multiple streets of the business centre. The other limitation of the study was the time frame in which the research had to be done. The researcher was given a few months in which to conduct the research by the school, meaning the research had to be done quickly to beat time. Hence the time frame was a limitation.

### **3.13 Conclusion**

In conclusion, this chapter described the research method and processes that were used in the collection of data, procedures and techniques used in data analysis and the presentation of data. The chapter also gave reasons to why the research was considered valid and how the research eliminated bias in data collection, analysis and interpretation. Then finally the limitations of the

study were given. The next chapter will discuss the presentations and analysis of the research conducted.



## CHAPTER 4

### PRESENTATION AND ANALYSIS OF FINDINGS

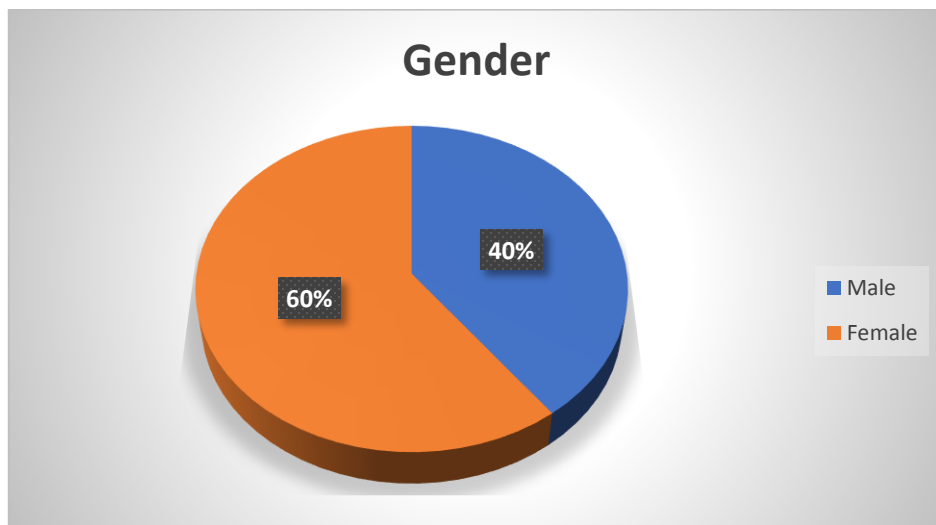
#### 4.0 Introduction

This chapter discusses the presentation and analysis of the research conducted. The findings of this study are presented in this section. The findings were analyzed using descriptive statistical tools depicted with the use of tables, bars and charts to draw conclusions. The findings were presented in the order of the objectives of the study.

#### 4.1 Demographic Characteristics of Respondents

##### 4.1.1 Gender of Respondents

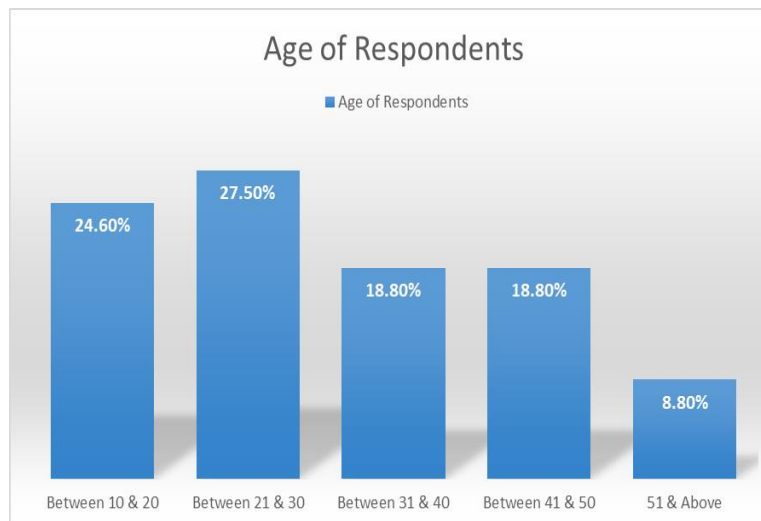
The graph above shows the gender distribution of the respondents of the study. (60 %) of the respondents were female whilst (40%) were males. This means that the informal sector is predominantly dominated by women.



**Figure 4.1: Gender of Respondents**

#### 4.1.2 Age of Respondents

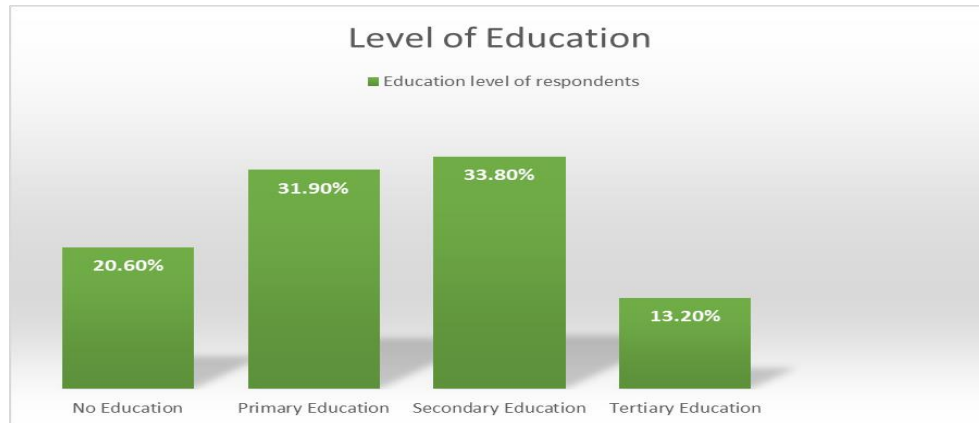
The graph above represents the age distribution of the respondents in the survey. The data indicate that the majority of the respondents were aged between 21 and 30 years, representing (27.5%) of the total distribution whilst those aged between 10 and 20 years were 17, representing (24.6%) of the total respondents. Those between 31 and 40 years and those between 41 and 50 years were evenly distributed with each of the two groups representing (18.8%) of the total distribution, respectively. Only (8.8%) of the interviewees were 51 years and above. The implication of this distribution is that majority of informal sector participants are aged between the ages 10 and 30 years. Mason and Calvin (1978) conducted a survey including 800 adults from Oregon whose 1 of four accepted that they evade. The higher level of tax evasion was evidenced from young people with low income, thinking that it was a low probability for detection.



**Figure 4.2: Age of Respondents**

#### 4.1.3 Education Level of Respondents

The table above represents the distribution of respondents according to the education attained. The majority of the respondents (33.3%) attained secondary education, followed by (31.9%) who only attained primary education whilst (20.3%) had neither primary, secondary nor tertiary education and only (13.0%) had attained tertiary education.

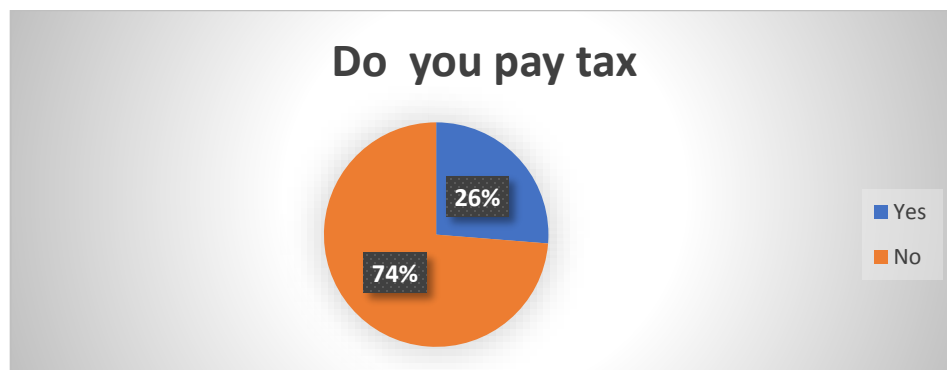


**Figure 4.2: Age of Respondents**

## 4.2 Objective One: Factors that Lead to Non-Compliance on Tax Remittance in Informal Sector

### 4.2.1 Compliance of the Respondents to Payment of Tax

The first variable on this objective was intended to establish how many people paid tax and how many did not pay it was established that. The study reviewed that the majority (73.1%) of business owners in the informal sector do not pay tax whilst only (26.1%) pay tax.



**Figure 3: Compliance of the Respondents to Payment of Tax**

### 4.2.2 Key Factors that Cause Non-Tax Compliance

According to the findings, majority of the respondents, representing a distribution of 28.6% indicated that they did not pay their taxes because the process of paying tax was too complicated.

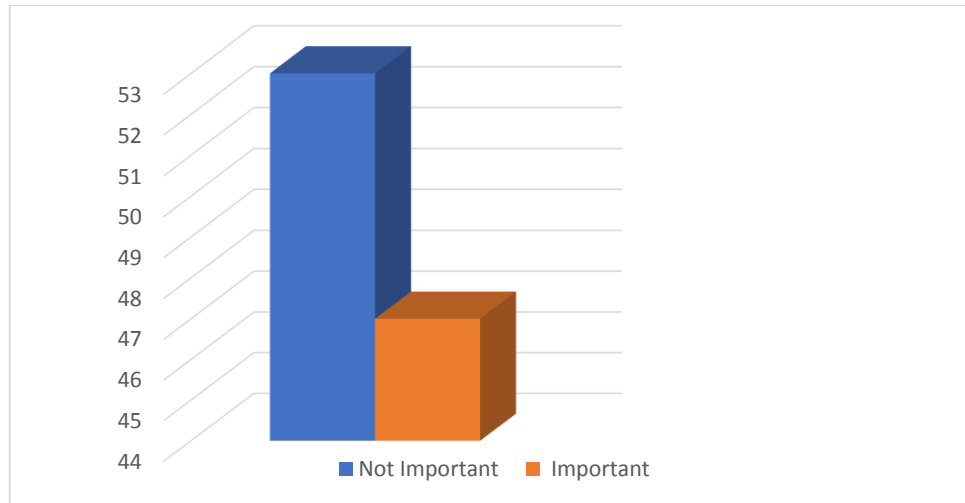
(26.5%) of the respondents indicated that they did not pay tax because the tax rate was too high, while 24.5% of the respondents said that they evaded tax because of their incomes were too low to sustain their tax obligations and 10.1% of the sampled alluded to the lack of any tax education as being the reason why they did not remit tax. Only (6.1%) of the respondents gave alternative reasons for evading tax.

**Table 1: Key Factors that Cause Non-Tax Compliance**

|                                | Frequency | Count | Percent | Cumulative Percent |
|--------------------------------|-----------|-------|---------|--------------------|
| Rate is too high               | 13        | 3.8   | 5.5     | 26.5               |
| Cost of paying tax is too high | 14        | 4.3   | 3.6     | 55.1               |
| Income is too low to pay tax   | 12        | 7.4   | 4.5     | 79.6               |
| Don't know anything about tax  | 7         | 0.1   | 4.3     | 93.9               |
|                                | 3         | .3    | .1      | 100.0              |
|                                | 49        | 1.0   | 0.0     |                    |
|                                | 20        | 0.0   |         |                    |
|                                | 69        | 0.0   |         |                    |

#### 4.2.3 Perception of informal Sector Business People about Tax Remittance

In order to establish how the business people from the informal sector perceived tax remittance, they were asked to give their opinions as to whether they viewed taxes as important or not important. The majority of the respondents (53 %) felt it was not important to pay tax whilst (47%) of the respondents felt paying tax was important as shown in the graph above. The perceptions on the importance of tax have serious implications on tax evasion and this is seen in the reasons given by the different respondents who felt paying tax was not important. For example, over half of the 52.9% who indicated that tax was not important felt that paying tax was not important because they felt they did not benefit directly from the taxes paid, whilst the rest of the respondents felt that paying tax was not important because the revenue raised through taxes were not used for intended purposes by the government.



**Figure 4: Perception of informal Sector Business People about Tax Remittance**

#### **4.2.4 Chi-Square Test on the correlation between positive perception of taxes and levels of education**

Null Hypothesis: There is no correlation positive perception of taxes and levels of education.

Alternative Hypothesis: There is a correlation between positive perception of taxes and levels of education.

The results show the Pearson value 316.620<sup>a</sup> with the significance figure of 0.00, since the significance figure is less than 0.05, we reject the Null hypothesis and therefore infer that there is a correlation between positive perception of taxes and levels of education. This indicates that respondents who had attained a at least secondary school level of education where more likely to perceive payment of taxes as important compared to those that who had only attained a maximum of primary education.

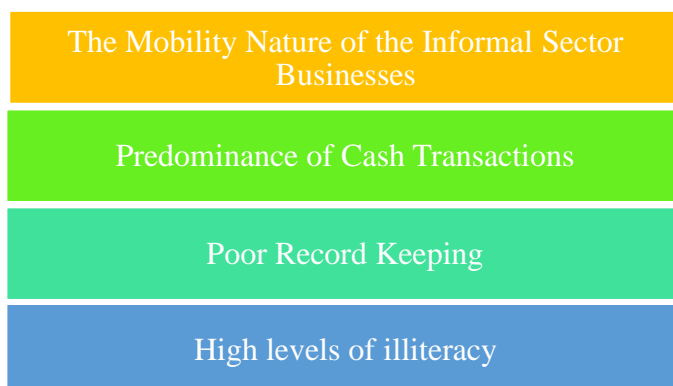
**Table 2: Chi-Square Test on the correlation between positive perception of taxes and levels of education**

| Chi-Square Tests             |                    |    |                                   |
|------------------------------|--------------------|----|-----------------------------------|
|                              | Value              | df | Asymptotic Significance (2-sided) |
| Chi-Square                   | 5.620 <sup>a</sup> | 16 | .000                              |
| Likelihood Ratio             | 9.030              | 16 | .000                              |
| Natural Log Likelihood       | 5.177              | 1  | .000                              |
| Fisher's Exact Test          |                    |    |                                   |
| Linear by Linear Association |                    |    |                                   |
| N of Valid Cases             | 69                 |    |                                   |

a. 80.0% of the cells (80.0%) have expected count less than 5. The minimum expected count is

#### **4.3 Objective Two: Challenges that Affect Revenue Mobilization by Zambia Revenue Authority from the Informal Sector**

This section presents the findings on the key challenges faced by the tax authorities in taxing the informal sector, as informed by Zambia Revenue Authority key informants. Attached at the end of the research is the Appendix showing the responses from the respondents on the interview guide questions. The Mobility Nature of the Informal Sector Businesses; Predominance of Cash Transactions and High levels of illiteracy



**Figure 5: Challenges that Affect Revenue Mobilization**

#### **4.3.1 The Mobility Nature of the Informal Sector Businesses**

According to the interviewees from ZRA one of the major challenges faced by ZRA in collecting tax from the informal sector is the mobility nature of the informal sector businesses; One among the many challenges alluded to by the key informants in taxing the informal sector was the mobility nature of informal sector businesses. The study discovered that many informal sector businesses did not have permanent residence of conducting business hence they are always on the move roaming from one place to the other in the quest to increase their sales.

*It becomes, extremely difficult to tax the informal sector because there is no permanent place to find most the informal sector participants. For example, a number of traders at intercity bus terminal do have a fixed trading location. Instead, they move from one bus to the other in order to find customers for their products so that they can earn a living. Collecting tax from such individuals would not be easy because ZRA would not have a specific person and location in mind in order to carry out this task (ZRA Official, Interview: 2021)*

#### **4.3.2 Predominance of Cash Transactions**

Predominance of cash transactions is another theme that emerged on the challenges faced by ZRA in their quest to administer taxes in the informal sector, according to respondent number 2 in appendix III of the interview guide “one of the challenges faced by ZRA in taxing the informal sector is that there is lack of financial records in the informal sector that can assist ZRA to collect tax from these vendors” There is lack of documented transactions in the informal sector due to cash transactions. The study also found that the informal sector was predominantly characterized by cash transactions which leave no evidence of occurrence of the transaction for the tax authority to follow up on taxing such businesses The interviewee, argued that;

*The cash transactions do not leave any documentation trail as informal businesses usually do not keep record of such transactions. Cash sales, therefore, make it difficult to tax income generated in the informal sector. The underlying challenge here is that informal sector participants sell on cash basis and do not keep records of their daily sales. As such, this situation makes it very difficult to determine the sales income of businesses that do not*

*record their transactions hence it becomes extremely difficult to collect tax in this sector (ZRA Official, Interview: 2021).*

He however, argued that, with the introduction of swiping machines, it is easy to collect tax from some companies and some of the informal sector businesses. But most traders in the informal sector are not privileged to own swiping machines and most of them prefer using cash transactions because they find it easy to carry out their daily businesses. The difficulties of taxing the informal sector originate from its characteristics that include: high tax collection cost, mobile nature of the operators, cash operation, aggressive nature of the actors, absence of business premises and absence of data and information. All these characteristics make the informal sector hard to tax hence making it a huge challenge for tax revenue collection (ZRA Official, Interview:2021).

#### **4.3.3 Poor Record Keeping**

According to respondent number 2 there is lack of financial records that can assist ZRA to collect tax from the business owners. He said that;

*There was generally poor to zero record keeping in the informal sector. Here the Zambia Revenue Authority informant argued that there exist no records from which the authority could determine the accounting net profit of most informal sector businesses from which the authority adjusts the taxable income, therefore, rendering the sector almost untaxable. (ZRA Official,2021)*

In some countries with weak tax systems and enforcement laws, most tax evaders are self-employed professionals such as architects, accountants, engineers, lawyers and doctors. However, these professionals are easy to identify as they are registered and licensed with professional bodies and in most instances, conduct much of their businesses with the public. There should always be the need to pay closer attention by tax administrators to the composition of small and medium taxpayers to ensure that some big potential tax payers do not hide in the informal sector



#### **4.3.4 High Illiteracy Levels**

According to all the 3 respondents, high illiteracy levels in the informal sector was also cited as one of the major reasons why the tax authority have it hard to collect tax from the sector. The study found that a large number of informal sector participants were illiterate and as such were very ignorant about the tax system and their obligations to pay tax. The common perception of informal sector activities is that they are mainly those of petty traders, street hawkers, shoeshine boys and other groups underemployed on the streets of the big towns. However, empirical studies indicate that the bulk of employment in the informal sector is economically efficient and profit-making, though small in scale and limited by simple technologies, little capital and lack of links with the formal sector. Within the informal sector, the employed are a variety of carpenters, masons, tailors and other tradesmen, as well as cooks and taxi-drivers, offering nearly the full range of basic skills needed to provide goods and services for a large though often poor section of the population (ILO, 2013).

#### **4.4 Objective Three: To determine the Practices, Procedures and Principles that would incorporate good Tax Administration in the Informal Sector.**

This section presents the findings on the practices, principles and procedures that would incorporate good tax administration in the informal sector. Attached at the end of the research is the Appendix showing the responses from the respondents on the interview guide questions.

##### **4.4.1 Tax Education and Advertisement**

All the three respondents said there is need for different educational campaigns such as radio, television and print media campaigns in Zambia's widely spoken local languages can be rolled out with the aim of educating the many businessmen and women on their tax obligations. There should be regular tax education for the general public using both the electronic and print media. Billboards should be mounted at vantage points in the district to educate the public about the importance of taxation.

*It would be of great help if us as ZRA embarked on serious Tax Education and Advertisement. We can do this through different platforms such as radio, TV, Billboards*

*and newspapers. We can also do physical trainings on education in order educate people on the informal sector on the importance of paying tax (ZRA Official,2021)*

#### **4.4.2 Ease of Tax Remittance**

Respondent 1 and 3 To reduce tax evasion that is caused through this channel, it is highly recommended that the processes of paying taxes are further simplified, particularly, for informal sector participants who are purported to be highly illiterate. It is therefore, recommended that the Zambia Revenue Authority should device the simplest ways of paying tax, for example, the filling in of forms can be minimized or completely done away with. With the massive record keeping campaigns, the authority may not require taxpayers to fill out any forms or make long ques, instead, all they will be required is look through the records of the financial transactions of the business and from there they can deduce what is liable for payment.

*As an institution we need to reduce on the paperwork and processes involved in paying tax. Many of our customers find it difficult to pay tax because of the system which seems to be a little complicated for them, this pushes people away because the entire process of paying tax consumes time (ZRA Official, 2021).*

#### **4.4.3 Expansion of The Tax Pay Point**

All the 3 respondents suggested that capacity of the tax authority also needs to be increased. This can be done by setting up more convenient revenue points in the busiest town centers. This will reduce the hustle of lining up and will create motivation among informal taxpayers in paying taxes. For example, ZRA can come up with ZRA booths to be easily accessed by people so that they can easily pay their taxes. These booths can be placed in the busiest business areas of our country to that our traders can be reminded on the importance of paying tax.

*There is need to come up with different revenue points in Zambia's busiest town centres. This will enable people to easily pay their taxes and not come all the way to ZRA or the few registered places to make payments. (ZRA Official, 2021).*

#### **4.4.4 Mandatory Informal Sector Business Registration**

All the respondents said that it was mandatory for ZRA to introduce Mandatory Business Registration. As such, in order to effectively capture and follow up on taxes in the informal sector, it is recommended that every business in the informal sector be registered with the tax authority and a database of such businesses is created to help monitor the frequency of tax remittance by such businesses. This will help the tax authority follow up on individual businesses even if they do not have permanent residence of operation.

*It is recommended that every business in the informal sector be registered with the tax authority and a database of such businesses is created to help monitor the frequency of tax remittance by such businesses (ZRA Official, 2021).*

## **CHAPTER 5**

### **DISCUSSIONS AND INTERPRETATIONS OF FINDINGS**

#### **5.0 Introduction**

This chapter presents the discussions and interpretations of the main findings of the study as regards the specific objectives of the research. The objectives of this research were as follows;

1. To establish factors that lead to non-compliance on tax remittance in informal sector.
2. To identify the challenges that affect revenue mobilization by Zambia Revenue Authority from the informal sector.
3. To determine the factors that would incorporate good tax administration principles, procedures and practices in Zambia

#### **5.1 Factors that lead to Non-compliance on Tax Remittance in Informal Sector**

It was widely perceived by majority of informal sector participants that paying tax was not important. This was seen in the statistical distribution of the respondents where 53% answered ‘‘NO’’ to the question ‘‘Do you think paying tax is important’’. Only 47% of the respondents felt otherwise. However, even those that answered ‘‘YES’’, not everyone actually paid tax because they don’t know much about paying tax (tax illiteracy) and the tax rate is too high.

The informal sector forms a large and growing proportion of most economies in developing countries. A larger proportion of economic activities in most of these countries are conducted within the informal sector. It is perceived that the increases in economic activities resulting from a growing informal sector should correspond with an increased tax base for the government. Governments and policy makers have been seeking for means on how to fully benefit in terms of tax revenues from businesses earning above the subsistence level in this sector. The informal sector is considered hard to collect tax from.

Taking both economic and administrative factors into account, it is less attractive in terms of returns to tax a large number of poor people and small enterprises in the informal sector. The sector is usually given less priority by tax authorities as the returns are perceived to be low and

attempts of collecting the tax are most likely to be unpleasant, difficult, or even dangerous (Fjeldstad and Heggstad (2013:68). It is for this reason that the Value Added Tax (VAT) system for some countries offers exemptions to selected basic commodities heavily consumed by poor people. Furthermore, some countries have adopted a progressive income tax system, which excludes low earning workers who fall into a zero-percentage tax band from paying tax.

Dube (2014:49) explains that taxing the informal sector raises equity issues. This is because people at the same economic level are supposed to be treated equally (horizontal equity) while those at different economic level are supposed to be treated differently (vertical equity) for tax purposes. However, JCTR (2014:27) explains that the tax system must be equitable and neutral in that it must be seen to be fair and non-discriminatory. It must not prescribe a different tax regime for one group of citizens and another regime for others. The tax system must also not unduly influence the consumption behavior of citizens. However, when dealing with taxation of the informal sector, tax authorities are forced to depart from the norms of equity and neutrality because of the characteristics of the sector.

The factors identified in the study as being the main drivers of non-tax compliance in the informal sector were; high tax rate, complicated tax system, illiteracy and low incomes among informal sector participants. It was found that most informal sector participants found the tax rate are too high to pay, participants were ignorant about their tax obligations, had a low income or found the process of remitting tax too cumbersome.

Tax Literacy involves providing information about Taxation. Tax literacy can be done through the distribution of brochures, leaflets, talk shows and taxpayer's days. On the other hand, Tax illiteracy is the opposite of Tax literacy. High levels of Tax illiteracy will lead to high levels of tax evasion. If people are given adequate tax education the levels of tax evasion would go down.

On the other hand, the informal sector has a high number of people with low incomes. However, from this research it was found that 10.1 % of the respondents did not know anything about tax. In their study, (Loo et al., 2009) found that education attainment is one among other key determinants of tax evasion in the informal sector. Loo et al, (2009) claim that that education has two elements: the general degree of fiscal knowledge and the specific degree of knowledge about

tax evasion opportunities. They claim that by enhancing the level of general fiscal knowledge, tax compliance improves due to more positive perceptions about taxation. Increased knowledge of tax evasion opportunities has a negative impact on tax compliance as it aids non-compliance.

Low incomes contribute to high levels of tax evasion. This is because people find it difficult to give part of the low incomes made to the government due to the hardships of the economy. In this research 17.4 % of the respondents gave the reason of their incomes been too low to pay tax.

The large number of potential taxpayers in the informal sector, and the difficulties of monitoring “hidden” entrepreneurs and small-scale firms, can give rise to serious revenue collection costs for tax authorities in developing countries. At the same time, the revenue potential of taxpayers in the informal sector is fairly modest, as their taxable incomes are usually quite low (Joshi et al., 2014). Informal sector activities are often located in rural areas or come from self-employed sellers living near the subsistence level (La Porta & Shleifer, 2014).

Consequently, given the low “value for money” in revenue terms, tax administrations have often given little priority to the taxation of the informal sector firms (Fjeldstad, 2014), which can also be related to equity consideration, namely that taxation falls more strongly on the shoulders of lowing come informal firms (Joshi et al., 2014). From a conceptual perspective, the direct revenue impacts of informal sector taxation and the associated costs might also be highly difficult to assess as data availability and quality is poor for many developing countries.

High tax rates are also a cause of tax evasion. In this research conducted, 18.8 % of the respondents said the tax rate is too high that is the reason why they do not pay tax. When the tax rate is high there will be more tax evasion in a country. Higher tax rates provoke tax evasion. The reaction of people in that country becomes so intense that "tax increases may even produce a reduction rather than an increase in tax revenues.

Complex tax systems due to the simplicity of the tax structure, it is clear that complex tax systems favour evasion and avoidance, in as much as they create uncertainty with respect to scope of the tax regulations, increase the costs of examination and compliance and multiply the evasion and avoidance formulas or mechanisms. However, in this research 20.3 % of the respondents said that the process of paying tax is too complicated that is why they do not pay tax.

The study confirmed the findings of Slemrod (2011), Joshi (2010) and Loo et al (2009) who in their studies found that tax evasion in the informal sector was driven by a complicated tax process, high tax rates, low incomes earned by informal sector participants and illiteracy respectively. This would seem to suggest that in Zambia, a larger proportion of businesses have only fair knowledge of the tax and tax system. However, as relates to the general public, studies have shown that the general understanding of tax policy concepts such as progressive taxation is inadequate (Roberts, Hite, & Bradley, 1994). Further it has been found that the public's knowledge of taxes and tax policy is remarkably low (Kasipillai & Mustafa, 2000).

## **5.2 Challenges that Affect Revenue Mobilization by Zambia Revenue Authority from the Informal Sector.**

The challenges faced by the tax authority in taxing the informal sector were fourfold; and these are, the mobile nature of the informal sector businesses, the predominance of cash transactions, poor record keeping and high illiteracy levels among informal sector participants.

One among the many challenges alluded to by the key informants in taxing the informal sector was the mobility nature of informal sector businesses. The study discovered that many informal sector businesses did not have permanent residence of conducting business hence they are always on the move roaming from one place to the other in the quest to increase their sales. Therefore, according to the first interviewee, it becomes extremely difficult to tax the informal sector because there is no permanent place to find the informal sector participants. For example, a number of traders at intercity bus terminal do have a fixed trading location. Instead, they move from one bus to the other in order to find customers for their products so that they can earn a living. Collecting tax from such individuals would not be easy because ZRA would not have a specific person and location in mind in order to carry out this task.

The study also showed that transactions in the informal sector were highly liquid, that is, for most part; the transactions in the sector were cash transactions. It is against this characteristic of the informal sector that the tax authorities charged that it was extremely difficult to collect tax in the informal sector because cash sales leave no evidence of sales and therefore some revenue may not be captured in total revenue. Cash sales, therefore, make it difficult to tax income

generated in the informal sector. The underlying challenge here is that informal sector participants sell on cash basis and do not keep records of their daily sales. As such, this situation makes it very difficult to determine the sales income of businesses that do not record their transactions hence it becomes extremely difficult to collect tax in this sector.

For example, with the introduction of swiping machines, it is easy to collect tax from some companies and some of the informal sector businesses. But most traders in the informal sector are not privileged to own swiping machines and most of them prefer using cash transactions because they find it easy to carry out their daily businesses. The difficulties of taxing the informal sector originate from its characteristics that include: high tax collection cost, mobile nature of the operators, cash operation, aggressive nature of the actors, absence of business premises and absence of data and information. All these characteristics make the informal sector hard to tax hence making it a huge challenge for tax revenue collection (TAKNET, 2010).

The study also found that there was generally poor to zero record keeping in the informal sector. Poor recording keeping in the informal sector was another reason cited for the difficulty in taxing the sector. It was discovered that most informal sector businesses did not have records of their day to day transactions, as such, determining how much they needed to remit in taxes was almost impossible. Here the Zambia Revenue Authority informant argued that there exist no records from which the authority could determine the accounting net profit of most informal sector businesses from which the authority adjusts the taxable income, therefore, rendering the sector almost untaxable. In some countries with weak tax systems and enforcement laws, most tax evaders are self-employed professionals such as architects, accountants, engineers, lawyers and doctors. However, these professionals are easy to identify as they are registered and licensed with professional bodies and in most instances, conduct much of their businesses with the public. There should always be the need to pay closer attention by tax administrators to the composition of small and medium taxpayers to ensure that some big potential tax payers do not hide in the informal sector (Bird and Wallace, 2003).

Similarly, the high levels of illiteracy in the sector also contributed to the challenges in taxing the sector. This study was informed that most informal sector participants were highly illiterate and did not know their tax obligations. The common perception of informal sector activities is



that they are mainly those of petty traders, street hawkers, shoeshine boys and other groups underemployed on the streets of the big towns. However, empirical studies indicate that the bulk of employment in the informal sector is economically efficient and profit-making, though small in scale and limited by simple technologies, little capital and lack of links with the formal sector. Within the informal sector, the employed are a variety of carpenters, masons, tailors and other tradesmen, as well as cooks and taxi-drivers, offering nearly the full range of basic skills needed to provide goods and services for a large though often poor section of the population (ILO, 2013).

### **5.3 Incorporation of good tax administration principles, practices and procedures to incorporate good tax administration in the informal sector.**

#### **5.3.1 Tax Education and Advertisement**

From the study, we can deduce that the majority of Zambia's informal sector participants are highly illiterate and do not know what the law expects of them in light of paying taxes. The study revealed that 10.1% of the respondents did not know anything about paying tax. Therefore, it is against this background that this study suggests that in order to maximise tax collection from the informal sector there is need for the Zambia Revenue Authority to familiarise participants in the informal sector on their tax obligations. Different educational campaigns such as radio, television and print media campaigns in Zambia's widely spoken local languages can be rolled out with the aim of educating the many business men and women on their tax obligations. There should be regular tax education for the general public using both the electronic and print media. Billboards should be mounted at vantage points in the district to educate the public about the importance of taxation.

#### **5.3.2 Ease of Tax Remittance**

According to the findings of this study, amongst the many variables that influence tax evasion in the informal sector was the complications in the process of remitting tax. To reduce tax evasion that is caused through this channel, it is highly recommended that the processes of paying taxes are further simplified, particularly, for informal sector participants who are purported to be highly illiterate. It is therefore, recommended that the Zambia Revenue Authority should device the simplest ways of paying tax, for example, the filling in of forms can be minimized or completely

done away with. With the massive record keeping campaigns, the authority may not require tax payers to fill out any forms or make long ques, instead, all they will be required is look through the records of the financial transactions of the business and from there they can deduce what is liable for payment.

### **5.3.3 Expansion of The Tax Pay Points**

Capacity of the tax authority also needs to be increased. This can be done by setting up more convenient revenue points in the busiest town centers. This will reduce the hustle of lining up and will create motivation among informal tax payers in paying taxes. For example, ZRA can come up with ZRA booths to be easily accessed by people so that they can easily pay their taxes. These booths can be placed in the busiest business areas of our country to that our traders can be reminded on the importance of paying tax.

### **5.3.4 Mandatory Informal Sector Business Registration**

The study also observed that one of the major challenges faced by the tax authority to tax the informal sector was the mobile nature of most informal sector businesses. As such, in order to effectively capture and follow up on taxes in the informal sector, it is recommended that every business in the informal sector be registered with the tax authority and a database of such businesses is created to help monitor the frequency of tax remittance by such businesses. This will help the tax authority follow up on individual businesses even if they do not have permanent residence of operation.

## **CHAPTER 6**

### **CONCLUSION AND RECOMMENDATIONS**

#### **6.0 Introduction**

This chapter presents conclusions to the research findings and recommendations on how best Zambia's Informal Sector Can Be Effectively Taxed.

#### **6.1 Conclusion**

The study sought to examine tax evasion in Zambia's informal sector. A total of 68 respondents were interviewed and with closed and open-ended questions. 3 key ZRA informants were interviewed using open ended questions. The empirical result obtained from the study showed that tax evasion in the informal sector is mainly influenced by low incomes, illiteracy, tax processes and the tax rate. The study also established that the non-permanent place of work of informal sector participants, cash-based transactions and poor record keeping in the sector were among the many challenges that the Zambian Revenue Authority faced in taxing the informal sector.

The study revealed that 10.1% of the respondents lacked tax education in the municipality. Majority of the tax payers were either averagely satisfied or not satisfied with the use of tax revenue by the government and the greater percentage of people pay their taxes in anticipation of benefits from government. The survey revealed that the respondents interviewed had a fairly limited knowledge of tax and the tax system in Zambia. The majority of respondents have not received any training in tax literacy indicating that ZRA has limited programs on increasing tax literacy among taxpayers. This is despite putting in place the Taxpayers Education and Advisory Services programs and a taxpayer Charter. This gap provides the ZRA with the opportunity to develop training and dissemination strategies in order to increase tax literacy. The respondents perceived company tax, PAYE, import duty, excise duty and VAT to be high and that all were positively related to tax evasion. Of the tax types, company income tax was regarded to be the most complicated and therefore more vulnerable to tax evasion than the others. Simplifying the tax code is necessary to make application of tax simple and readily usable.

Though this survey was not statistically representative, it offered an insight on what could be part of the big picture on tax system and tax evasion in Zambia. There is need to formulate comprehensive legal and administrative tax policy reforms that will address tax literacy levels and compliance. ZRA should come up with strategies on training, dissemination of already existing programs and policy documents, aimed at minimizing tax evasion. Further, penalties should be stiffened. For example, monetary fines should include interest at above the market rate. The prison sentence already in place should be strictly enforced as a deterrent to tax evasion and a strong signal to would be offenders' conclusion, taxing the informal sector depends on a combination of approaches and mechanisms.

Tax collection is an important governance challenge that depends on a compliance culture, the values and norms of a society, its history and above all the capacity of the government to deliver. The potential for taxing the informal sector depends upon a) the degree of pressure on governments to increase revenues and b) the existence of collective actors in the informal sector having institutionalized channels for negotiation with the state (Stella 1993 cited by (Aryee, 2007)). Above all, there must be a different way of thinking politically about taxation of the informal sector that could lead to a substantial new research agenda. In other words, to make inroads into the difficult problem of taxation of the informal sector we need to think differently about the issue. Maximizing voluntary compliance is therefore a must which must be taken seriously by any reform or new research agenda.

## **6.2 Recommendations**

The following are the main recommendations in tackling the rampant tax evasion in Zambia's informal sector;

### **6.2.1 Reduction of Tax Rates**

From this study 18.8% of the respondents said they do not pay tax because the tax rate was too high. The lower the tax rates the more people would come on board to pay taxes. This would promote economic growth in the country. It would mean more people in the informal sector would pay tax and ZRA would collect more tax from more people. This would increase the tax been collected countrywide. The HR, Directors, and Managers of ZRA can come together and

discuss the benefits of tax reduction with the current government of Zambia and therefore implement the reduction of tax rates. The lower the Tax rates, the more people would pay their taxes from the Informal Sector.

### **6.2.2 Tax Education and Advertisement**

From the study, we can deduce that the majority of Zambia's informal sector participants are highly illiterate and do not know what the law expects of them in light of paying taxes. The study revealed that 10.1% of the respondents did not know anything about paying tax. Therefore, it is against this background that this study suggests that in order to maximise tax collection from the informal sector there is need for the Zambia Revenue Authority to familiarise participants in the informal sector on their tax obligations. Different educational campaigns such as radio, television and print media campaigns in Zambia's widely spoken local languages can be rolled out with the aim of educating the many business men and women on their tax obligations. There should be regular tax education for the general public using both the electronic and print media. Billboards should be mounted at vantage points in the district to educate the public about the importance of taxation.

### **6.2.3 Ease of Tax Remittance**

According to the findings of this study, amongst the many variables that influence tax evasion in the informal sector was the complications in the process of remitting tax. To reduce tax evasion that is caused through this channel, it is highly recommended that the processes of paying taxes are further simplified, particularly, for informal sector participants who are purported to be highly illiterate. It is therefore, recommended that the Zambia Revenue Authority should device the simplest ways of paying tax, for example, the filling in of forms can be minimized or completely done away with. With the massive record keeping campaigns, the authority may not require tax payers to fill out any forms or make long queues, instead, all they will be required is look through the records of the financial transactions of the business and from there they can deduce what is liable for payment.

#### **6.2.4 Expansion of The Tax Pay Points**

Capacity of the tax authority also needs to be increased. This can be done by setting up more convenient revenue points in the busiest town centers. This will reduce the hustle of lining up and will create motivation among informal tax payers in paying taxes. For example, ZRA can come up with ZRA booths to be easily accessed by people so that they can easily pay their taxes. These booths can be placed in the busiest business areas of our country so that our traders can be reminded on the importance of paying tax.

#### **6.2.5 Mandatory Informal Sector Business Registration**

The study also observed that one of the major challenges faced by the tax authority to tax the informal sector was the mobile nature of most informal sector businesses. As such, in order to effectively capture and follow up on taxes in the informal sector, it is recommended that every business in the informal sector be registered with the tax authority and a database of such businesses is created to help monitor the frequency of tax remittance by such businesses. This will help the tax authority follow up on individual businesses even if they do not have permanent residence of operation.

#### **6.2.6 Intensive and Regular Monitoring**

Officials of ZRA should undertake regular and intensive field operations by ensuring regular monitoring of the operatives within the informal tax net. Secret personnel or spies should be engaged to download verifiable information about all tax evaders for rewards. This will result in people fearing to withhold money that is meant for tax because of the consequences that may follow due to not paying tax.

#### **6.2.7 Capacity Building**

More tax officials should be employed to augment the staff strength of ZRA. Also, training and re-training of tax official in modern trends of tax assessment is key. Therefore, tax official should be well equipped in the area of tax education programs. Again, as an interim measure to solve the shortage of staff problem the Zambia Revenue Authority should use the leaders of identifiable

groups such as Hairdressers and Beauticians Association, Butchers Association, Dressmakers and Tailors Association and so on to collect taxes from their members.

#### **6.2.8 Political Incentives**

Politics always plays an important role in tax reforms. tax administrative reforms are often highly political processes posing a threat to important domestic stakeholders. The successful implementation of any tax reforms requires political will and support from the highest level of government. In the Zambian context, there should be a reduction in political resistance to tax the informal sector but endeavor to come up with strategies that are grounded on the principle of reciprocity.

#### **6.2.9 Segregation of Tax Administration**

Another recommendation is that tax administration should be segmented with specialised units for both the small and medium enterprises (SMEs) and large taxpayers from the formal sector each pursuing a consistent set of goals. For the Zambian government, investing in latest technological innovations is an important milestone. The use of mobile or internet banking to facilitate payment of taxes from the informal sector can ease the cost of collections for the state. In addition, such an approach gives the taxpayers the freedom to freely make payments at their convenient time and avoid the risks of harassment, collusions and corruption.

#### **6.2.10 Review of The Law in Order to Strengthen It to Address Tax Evasion**

This might include; Simplification of tax laws. Simple tax laws are easy to understand and comply with stiffer penalties: Charge interest at above market rate, strengthening enforcement on jail sentences. The law must create tax courts to deal with tax offenders, revocation of operating licenses and blacklisting the directors of companies involved in tax evasion. The law on Double Taxation Agreements should be strengthened to prevent Zambian citizens evading tax. Review the law to include filing of personal income returns by the self-employed and wage-earning

#### **6.2.11. Reward System**

A reward system should be initiated whereby the best small tax payers at the district levels would be awarded annually as in the case of farmers, teachers, and health workers among others. This will serve as incentive for tax compliance among the small taxpayers. A small gift of appreciation such as a Calendar, diary, a month free of Tax goes a long way and promotes loyalty in Tax payers.

#### **6.2.12. Collaborations**

The Zambia Revenue Authority should collaborate with other institutions such as Airtel money, MTN money, Zamtel and the banks at large. This is in order to make sure that payment of taxation is made easier for the informal sector. Zamtel, Airtel money and MTN money booths are easily accessible. Taxation of the informal sector allows informal firms to hold the state accountable for the use their payments and can thus contribute to an emerging sense of democratic participation and ownership over governmental actions.



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## APPENDIX I: QUESTIONNAIRE

### SECTION A;

#### DEMOGRAPHIC INFORMATION

1. What is your gender?

(a) Male [ ]

(b) Female [ ]

2. How old are you?

(a) Between 10 and 20 [ ]

(b) Between 21 and 30 [ ]

(c) Between 31 and 40 [ ]

(d) Between 41 and 50 [ ]

(d) Between 51 and above [ ]

3. What is your marital status?

(a) Single [ ]

(b) Married [ ]

(d) Divorced [ ]

(e) Widowed [ ]

4. What is your highest level of education?

(a) No Education

(b) Primary Education [ ]

(c) Secondary School [ ]

(d) Tertiary Education [ ]

(e) Other (specify).....

5. What category of business are you involved in?

(a) Transport Business (Taxi/Bus)[ ]

(b) Hair Dressing (Saloon / Barbershop) [ ]

(d) Food Supplies [ ]

(e) Clothing [ ]

(e) Crafts [ ]

(f) Other (specify).....

## **SECTION B;**

### **PERCEPTIONS OF TAX AMONG INFORMAL SECTOR PARTICIPANTS**

6. Do you think paying taxes is important?

(a) Yes [   ]

(b) No [   ]

9. If “NO” in question 6, why do you think paying tax is not important?

(a) I feel I do not directly benefit from the revenue collected through taxes [   ]

(b) I feel revenue raised through taxes is not used for the intended purposes [   ]

(c) Other (specify).....

8. If “YES” in question 6, why do you think paying taxes is important?

(a) Increases government revenue [   ]

(b) Accelerates Economic growth [   ]

(c) Other (specify).....

## **SECTION C;**

### **VARIABLES THAT INFLUENCE TAX EVASION IN THE INFORMAL SECTOR**

9. Does your business pay taxes?

(a) Yes [   ]

(b) No [   ]

10. If “NO” in Question 9, what are your reasons for not paying tax?

(a) The tax rate is too high [   ]

(b) The process of paying tax is too complicated [   ]

(c) My income is too low to pay taxes [   ]

(d) I do not know anything about taxes [   ]

(e) Other (specify).....

11. If “YES” in question 9, what are your reasons for paying tax?

(a) Because I am required by law [   ]

(b) I am scared of the penalties of not paying tax [   ]

(c) Because the tax I pay contributes to the growth of the economy [   ]

(d) Other (specify).....

12. If “YES” in question 9, how often do you pay tax?

- (a) Every month [    ]
- (b) Every three months [    ]
- (c) Every six months [    ]
- (d) Every year [    ]
- (e) Other (specify).....

## APPENDIX II: INTERVIEW GUIDE

1. What is your general opinion about taxing the informal sector?

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2. What are the main factors that influence non-compliance of tax in the informal sector?

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3. What are the main challenges faced by the Zambia Revenue Authority in taxing the informal sector?

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4. What measures have been put in place to curb the challenges of taxing the informal sector?

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5. To what extent do you think these measures have been successful?

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## **APPENDIX IV: INTERVIEW GUIDE**

### **CHALLENGES FACED BY THE TAX AUTHORITY IN TAXING THE INFORMAL SECTOR**

#### **Q1. What is your opinion about taxing the informal sector?**

**Respondent 1:** there is revenue loss in taxing this sector. Taxing the informal sector can be a good move as it would contribute to increased domestic revenue generation.

**Respondent 2:** Taxing this sector would not be convenient considering the welfare/conditions under which the participants of this sector operate. The places where they trade from are not secure and they generate low pay.

**Respondent 3:** Taxation of the informal sector is a challenge in our country Zambia. Compliance levels are low due to a number of factors such as low levels of education among business owners, lack of tax education, issues of locating the physical addresses of the business owners and negative perceptions about taxation.

#### **Q2: What are the main factors that influence tax non-compliance in the informal sector?**

**Respondent 1:** the procedure of paying tax is not easy and the long distance to the ZRA station is a contributing factor.

**Respondent 2:** lack of information in the informal sector on how to pay tax. Lack of adequate inspection by the ZRA officials in the informal sector. Lack of documented transactions in the informal sector. They mostly rely on cash transactions.

**Respondent 3:** the levels of the income generated in the informal sector is mostly low. Lack of information on the importance of paying tax. Unprotected labour laws.

#### **Q3: What are the main challenges faced by the Zambia Revenue Authority in taxing the informal sector?**

**Respondent 1:** low literacy levels among business owners and poor comprehension of taxation.

**Respondent 2:** lack of fixed locations of the business owners in operating their businesses  
Lack of financial records that can assist the authority to collect tax from these vendors.

**Respondent 3:** low levels of education among tax payers in the informal sector. Low levels of responsibility on contributing to national development. Lack of awareness on tax laws. Challenges in ZRA locating the physical location of these vendors. Challenges in understanding and sticking to compliance procedures. Lack of honesty in declaring the actual income earned.

**Q4. What measures have been put in place to curb the challenges of taxing the informal sector?**

**Respondent 1:** intensified taxpayer's education activities on radio and TV program. Introduction of user-friendly systems such as tax on phone to simplify the payment of taxes.

**Respondent 2:** ZRA has on the vast invested in human resources. Tax on phone

**Respondent 3:** introduction of tax on phone. Reinforcement of existing tax policies by putting emphasis on penalties. More publicity on the need for payment of tax on radio and TV programs.

**Q5. To what extent do you think these measures have been successful?**

**Respondent 1:** non-compliance of tax is slowly reducing due to increased publicity and sensitization and reduction of ques at the service centres due to introduction of tax on phone.

**Respondent 2:** ZRA has seen some improvements in compliance of tax from the informal sector but there is still room for improvement.

**Respondent 3:** further intervention is needed in the informal sector because the number of business owners paying tax are still very low