**BINDURA UNIVERSITY OF SCIENCE EDUCATION**

 **FACULTY OF COMMERCE**



**DEPARTMENT OF ACCOUNTANCY**

**TAX COMPLIANCE AND INFORMAL: CASE OF GLENVIEW, HARARE**

**BY**

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**A DISSERTAION SUBMITTED IN PARTIAL FULFIMENT OF THE REQUIREMENTS FOR THE BACHELOR OF ACCOUNTANCY HONOURS DEGREE OF BINDURA UNIVERSITY OF SCIENCE EDUCATION FACULTY OF COMMERCE.**

**JUNE 2023**

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# **DEDICATION**

I would like to dedicate my work to my family. They instilled in me a desire to learn and made sacrifices so I would have access to high quality education from an early age. Also, this is dedicated to my close friends who have always supported me throughout my years of studies.

#

# **DECLARATION**

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# **ABSTRACT**

Informal sector is growing rapidly in Zimbabwe due to the shrinking formal sector. The expansion of informal sector and shrinking formal sector reduces tax base hence low revenues since most of the informal sector players are out of the tax net. In trying to increase the tax base, government introduces various methods of collecting tax from the informal sector and presumptive tax is one of the methods implemented in Zimbabwe. Although presumptive tax and other measures were introduced, there is still poor performance in the informal sector in terms of tax compliance. The study looked at the reasons behind tax non-compliance in the informal sector, challenges encountered by the informal traders when complying with tax regulations, challenges faced by revenue authorities when collecting taxes from the informal sector and lastly the measures which can be put in place so as to improve voluntary tax compliance. The results from the findings suggests that revenue authorities must engage in two-way communication with the informal sector before establishment of statutes, continuous offering of education, measures which eliminate or reduce corruption in the tax system, simplified tax systems and fewer tax heads will improve voluntary tax compliance hence revenue collections.

# **ACKNOWLEDGEMENTS**

First and foremost I offer my sincerest gratitude to The Lord Jesus Christ, without him none of this would exist. In extension, many people have contributed to the successful completion of my research project. To them I owe a debt of thanks for their support, moral or otherwise in seeing me through. I wish to acknowledge the help provided by my supervisor Mrs Masukume(Mutero) from the beginning up to the completion, my husband, friends and family. May God bless you all.

Contents

[**APPOVAL FORM** ii](#_Toc137967201)

[**RELEASE FORM** iii](#_Toc137967202)

[**DEDICATION** iv](#_Toc137967203)

[**DECLARATION** iv](#_Toc137967204)

[**ABSTRACT** iv](#_Toc137967205)

[**ACKNOWLEDGEMENTS** v](#_Toc137967206)

[**Chapter One** 1](#_Toc137967207)

[**Introduction** 1](#_Toc137967208)

[**1.1 Background of the study** 2](#_Toc137967209)

[**1.3 Statement of the problem** 5](#_Toc137967210)

[**1.4 Purpose of the Study**: 6](#_Toc137967211)

[**1.5.1 Objectives of the study** 6](#_Toc137967212)

[**1.5.2 Research questions** 6](#_Toc137967213)

[**1.6 Significance of the study** 6](#_Toc137967214)

[**1.6.1**  **The researcher** 6](#_Toc137967215)

[**1.6.2** **The government** 7](#_Toc137967216)

[**1.6.3** **Informal sector** 7](#_Toc137967217)

[**1.6.4** **Future researchers** 7](#_Toc137967218)

[**1.6.5 Tax Consultancy Firms** 7](#_Toc137967219)

[**1.7 Assumptions** 7](#_Toc137967220)

[**1.8 Delimitation of the study** 7](#_Toc137967221)

[**1.9 Limitations of the study** 8](#_Toc137967222)

[**1.10 Definition of key terms** 8](#_Toc137967223)

[**1.11 Summary** 9](#_Toc137967224)

[**CHAPTER TWO** 10](#_Toc137967225)

[**LITERATURE REVIEW** 10](#_Toc137967226)

[**2.0 INTRODUCTION** 10](#_Toc137967227)

[**2.1** **Informal sector and Taxation** 10](#_Toc137967228)

[**2.1.0** **Methods of taxing the informal sector** 13](#_Toc137967229)

[**2.2Taxation compliance** 14](#_Toc137967230)

[**2.2 Theoretical framework** 15](#_Toc137967231)

[**2.2.0** **Taxation compliance theories** 15](#_Toc137967232)

[**2.3** **Challenges faced by informal sector players when complying with tax regulations** 17](#_Toc137967233)

[**2.4 Challenges faced by tax authorities when collecting taxes from the informal sector.** 20](#_Toc137967234)

[**2.5 Measures to increase voluntary compliance.** 21](#_Toc137967235)

[**2.6 Review of Related Literature.** 24](#_Toc137967236)

[**2.7** **Chapter Summary** 25](#_Toc137967237)

[**CHAPTER THREE** 26](#_Toc137967238)

[**METHODOLOGY** 26](#_Toc137967239)

[**3.0 INTRODUCTION** 26](#_Toc137967240)

[**3.1** **Research Design** 26](#_Toc137967241)

[**3.2** **Population and Sampling** 27](#_Toc137967242)

[**3.2.0** **Targeted population** 27](#_Toc137967243)

[**3.2.1** **Sampling design** 28](#_Toc137967244)

[**3.2.2** **Sample size** 29](#_Toc137967245)

[**3.3 Sources of Data Collection** 30](#_Toc137967246)

[**3.3.0 Primary sources** 31](#_Toc137967247)

[**3.3.1** **Secondary sources** 33](#_Toc137967248)

[**3.4 Validity and Reliability** 33](#_Toc137967249)

[**3.5 Data presentation and analysis** 34](#_Toc137967250)

[**3.6 Ethical Consideration** 34](#_Toc137967251)

[**3.7 Chapter Summary** 35](#_Toc137967252)

[**CHAPTER FOUR** 36](#_Toc137967253)

[**DATA ANALYSIS, PRESENTATION, AND INTERPRETATION** 36](#_Toc137967254)

[**4.0 INTRODUCTION** 36](#_Toc137967255)

[**4.1** **Response rate of the study** 36](#_Toc137967256)

[**4.2** **Background information of respondents** 37](#_Toc137967257)

[**4.2.0** **Informal traders** 37](#_Toc137967258)

[**4.1.2** **Small consultancy firms** 40](#_Toc137967259)

[**4.2 Presentation and Analysis** 41](#_Toc137967260)

[**4.2.0 Reasons behind non-compliance in the informal sector** 41](#_Toc137967261)

[**4.2.1** **Challenges faced by informal traders when complying with tax systems.** 44](#_Toc137967262)

[**4.2.2 Challenges faced by revenue authorities when collecting revenue from informal sector.** 45](#_Toc137967263)

[**4.2.3 Measures to increase voluntary compliance.** 47](#_Toc137967264)

[**4.4 Chapter Summary** 49](#_Toc137967265)

[**CHAPTER FIVE** 50](#_Toc137967266)

[**SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMENDATIONS** 50](#_Toc137967267)

[**5.0 INTRODUCTION** 50](#_Toc137967268)

[**5.1** **Conclusion** 50](#_Toc137967269)

[**5.2.0** **Reasons behind tax non-compliance in the informal sector** 51](#_Toc137967270)

[**5.2.1** **Challenges faced by the informal sector when complying with tax laws.** 51](#_Toc137967271)

[**5.2.2** **Challenges faced by revenue authorities when collecting revenue from the informal sector.** 52](#_Toc137967272)

[**5.2.3** **Measures which can be put in place to improve voluntary compliance.** 52](#_Toc137967273)

[**5.3 Recommendations** 53](#_Toc137967274)

[**5.3.0 Recommendations to ZIMRA** 53](#_Toc137967275)

[**5.3.1** **Recommendations to the government and policy makers** 54](#_Toc137967276)

[**5.3.2 Recommendations to the informal sector** 54](#_Toc137967277)

[**5.4 Areas of further study** 55](#_Toc137967278)

**LIST OF ACRONYMS**

GDP Gross Domestic Product

ILO International Labour Organization

VAT Value Added Tax

PAYE Pay As You Earn

ZIMRA Zimbabwe Revenue Authority

ESAP Economic Structural Adjustment Programme

ZIMSTARTS Zimbabwe Statistics Agency

USD United States Dollar

SME Small to Medium Enterprises

**List of tables**

Table 1: Attributes of the sample…………………………………………

Table 2: Sectors represented in the sample.

Table 3: Response rate

Table 4: Ownership distribution

Table 5: Tenure in business frequency distribution

Table 6: Educational qualifications

Table 7: Registration status

Table 8: Reasons behind tax non-compliance

Table 9: Measures to improve voluntary compliance.

**List of Figures**

Fig1: Tenure of service in domestic taxes (ZIMRA officials)

Fig2: Tenure of service: Tax consultancy

Fig 3: Effectiveness of collection methods

# **Chapter One**

## **Introduction**

Due to job creation, the informal sector has taken over as the primary provider of urban livelihoods because of the formal sector shrinkage in Zimbabwe. Due to the socio-economic problems which can be traced from the early 1990s to late 2000, the country’s informal sector growth surpasses that of formal sector as pointed out by Parliament of Zimbabwe (2014). Besides economic struggles, some individuals go the informal way by choice. Some are attracted by profits, job satisfaction, and favorable working hours.

In Zimbabwe there has been poor performance when it comes to tax compliance. According to Nyatanga (2016) there are several types of taxes in the Zimbabwean tax system, which includes Pay As You Earn (PAYE), Value Added Tax (VAT), Corporate Tax, and Customs, Income Tax, Surtax – levied on imported cars older than 5 years as well as excise tax, capital gains tax, and presumed tax and mining and taxes on royalties. The tax rates on these tax heads differ and also the due dates. The purpose of introducing presumed tax in 2005 and expanding its application in 2011 was to include unregistered business owners in the tax system, broaden the tax base, and hence increase revenue collection (ZIMRA, 2011).

Nyatanga (2016) believes that the main reason why taxes are levied is to collect revenue for the government and several Acts have been passed to ensure strict enforcement of Tax Compliance in Zimbabwe. Some of these Acts include Income Tax Act (Chapter23:06), Chapters 23:04 of the Finance Act, 23:01 of the Capital Gains Tax Act, 23:12 of the Value Added Tax Act, and Chapter 23:05 of the Estate Duty Act all deal with taxes.

Although tax compliance and revenue collections were expected to increase following the implementation of presumptive tax, ZIMRA (2016) acknowledges the tax non-compliance by the majority of those in the informal sector may affect the stability of the economy. Presumptive tax income has been doing poorly and is categorized under other taxes, Munjeyi (2017).In 2016 annual report, ZIMRA noted that USD $60.25 million was collected under other taxes head and Capital gains and withholding tax contributes significantly. Joshi et al (2014) claims that revenue from informal sector is modest since the incomes are low in this sector.

The chapter begins by outlining the background of the study, the problem statement, its objectives, its research questions, its justification, and its scope. The chapter will finish by outlining the structure of the research and highlighting the crucial components of each chapter, going from chapter 1 to chapter 5.

## **1.1 Background of the study**

The informal sector has a vital a part to play internationally and globally by allowing a proportion of population to escape poverty through its activities which generates employment for many Ajeku (2018). According to ILO (2018), the informal sector employs 85.8% of the population in Africa, 68.8% in the Pacific, 68.2% in Asia, 40% in America, and 25.1% in Europe and Central Asia. The statistics shows that informal sector is the biggest employer in Africa. The reason why there are relatively fewer people in the informal sector in the West and East is due to high employment rates in these countries. The same cannot be said for Africa as there are few job opportunities in the formal sector due to wars and poorly run economies.

 Zimbabwe is one of the countries where informal sector is increasing rapidly. In 1980, the percentage rate of informal sector was estimated to be 10%, double to 20% between 1986 and 1987, continued to increase to 40% by 2004 (Ndiweni and Verhoeven,2013). According to International Monetary Fund (IMF) (2018) Zimbabwe was the second country in the whole world with 60.6% of its population employed in the informal sector. Bolivia being the highest with 62.3% and the lowest rates found in Switzerland and Australia with 7.2% and 8.9% respectively. The informal sector includes activities from professional consultants, vegetable vendor’s, hairdressers, carpenters, public transport operators, food kiosks and hawkers of all sorts of wears.

According to ZIMSTATS (2022), the unemployment rate in Zimbabwe is 5.17 % which is far less than that estimated in the media. The variance between the sources is caused by differences in views and interpretation of the informal sector. ZIMSTATS (2022) notes that 44.7% of the over 3.2 million people defined as employed in Zimbabwe are working in the informal sector and about 769 311 thousand are in the agriculture sector. ZIMSTATS defines unemployment as lack of any means of contributing to the country’s GDP. Informal traders contribute to gross domestic product and it may as well contribute to the economic development (Ndiweni et al, 2014) therefore informal traders are included on the employment rate. Nyoni & Bonga (2018) argues that over half of the private sector is making a living from small to medium enterprises and contributes about 60% to GDP. Mangudya (2017) notes that informal sector is comprised of 2.8 million enterprises of different sizes, creating employment for over 5.7 million people and about 4.2 million are below the age of 35.

Due to shrinking formal sector, informal sector increases significantly in Zimbabwe (Sikwila, 2013). In trying to broaden the tax base government introduces presumptive tax in 2005 and additionally enforce it in 2011 so as to increase revenue base hence revenue in view of the growth of informal sector (ZIMRA 2011) A tax called presumed tax is imposed on unregistered dealers, small-scale miners, cottage industries, and transportation providers. In the event that a tax-compliant operator obtains a valid tax clearance, presumptive tax is not applied to him. Presumptive tax is intended to bring informal market participants into the tax system, broaden the tax base, and raise revenue. Presumptive tax in Zimbabwe is divided into categories and each category has its own tax rate as well as due date. For instance, transport operators presumptive tax fares differ depending on the number of passengers and ZINARA was appointed as a government agent in 2014 to collect taxes from transport operators, taxi-cabs and driving schools (ZIMRA, 2014).

 Despite all the efforts by the revenue authority Utaumire et al (2013) argues that although the aim of presumptive tax is to increase revenue base and hence revenue, revenue is kept of leaking through the informal sector due to the loopholes in the system. According to Alm, Martin-Vazquez, and Schneider (2003), presumptive tax is most appropriate when self-assessment for taxable income is unreliable, and it can reduce the possibility of tax evasion and increase revenue base hence revenue collections. On the other hand, Somouah (2011) argues that since transactions in the informal sector are mostly in cash and bookkeeping is poor, it is very difficult for authorities to trace and revenue base may continue to shrink.

According to Sparks & Barnett (2010), Since the informal sector accounts for the biggest portion of global market share, taxing it might increase income. Most markets in the world are dominated by informal sector ranging from food stuffs, clothing, electrical appliances, and furniture. Taxing these firms will increase government revenue collections. Schneider et al (2010) contends that in order for impoverished countries to exist, the informal sector must provide a significant source of income. This means that taxing the informal sector will increase revenue collections which can be channeled to infrastructure development in developing countries. According to World Bank (2021), developing countries need more revenues but are facing challenges in collecting taxes. In addition, developing country’s tax systems are complicated which leads to high levels of evasion, informal sector, corruption, and fewer investments. On the other hand, Keen (2012) pointed out that it is not necessary for tax authorities to tax informal traders because the costs of collecting the revenues are higher than the revenues being collected.

Tax compliance has been a serious issue in many countries, developing, transition and developed. There are many studies done concerning tax compliance issues in different parts of the world, for instance a study conducted by Chandarasorn in 2012 on income tax behavior in Thailand. In this study, the author found that taxpayer’s behavior in Thailand is influenced by the degree of fines and penalties. Most respondents pointed out that the fines and penalties on tax evasion are very low to the extent that taxpayers are not afraid to take part in tax evasion. Also, the tax law enforcements are poor and not able to detect who evades and who obeys tax laws and lastly the degree of corruption by government officials is very high and it demotivates taxpayers to comply.

There are also various studies carried out in African countries like Ghana and Nigeria. Studies on informal sector compliance concerns and the connection between taxation and economic growth have been conducted in Ghana, Ameyaw et al (2016). According to the study taxpayers comply mostly if they are benefiting from their tax payments and ethical values plays a significant role in compliance decisions to individual taxpayers. The economic factors affecting compliance identified are tax rates, income levels, tax audits, fines and penalties and audit possibilities. The gap between amounts of tax owed to and paid to Ghana Revenue Authority motivates the author(s) to investigate taxpayer’s behavior in Ghana. In 2018, Akeju researched on formalization of informal sector through trade unions in Nigeria. The study points out that formalization of informal sector can create a tax culture and provides access to opportunities like credit facilities and seminars hence growth of traders and increase of revenue collections in Nigeria.

Tax compliance issues differ with countries and individuals in question. The most important point of this study was that although the government does not actively assist the expansion of the informal sector, revenue authorities perceive it as a source of income. However, in recent times the government has been making strides through ZIMRA to try and collect revenue from the informal sector. Nyamwanza et al.'s (2014) investigation of SMEs' attitudes and behaviors regarding tax compliance is the topic of another research. The main focus was on retail operators in Gweru. Zivanai, Chari & Nyakurimwa (2015 performed research on the difficulties SMEs in Zimbabwe have in complying with their tax requirements. Also, Ligombeka (2019) investigates the taxation of flea market vendors in Zimbabwe in order to make a contribution to the discussion of the informal sector and tax compliance, the focus areas being on merchants at flea markets around Harare and Bulawayo. The study's goal was to determine whether there was a correlation between taxation impacts and gender, specifically whether taxes paid by flea market vendors affected men and women equally.

However, none of these studies address the rationale behind taxpayer’s non-compliance to tax laws and regulations specifically in Glenview home industries, Harare Zimbabwe. A more up to date study on this area is needed taking into consideration the growth of informal sector activities in this particular location.

## **1.3 Statement of the problem**

Due to continuous decrease in formal sector because of company closures, the informal sector has managed to grow rapidly and has become the backbone of the economy and the biggest employer. To bring unregistered business owners into the tax system, presumptive tax was introduced by the government expecting that it will increase tax base hence revenue collections. However, the contribution of presumptive tax is insignificant due to non-compliance to tax regulations in the informal sector. Therefore, this study seeks to investigate the rationale behind taxpayer’s non-compliance to tax laws and regulations.

## **1.4 Purpose of the Study**:

The study's goal is to explore the reasons behind tax evasion by the informal economy and find ways in which they can be encouraged to abide with the tax regulations of the country with our main focus being on the informal sector in Glen View, Harare, Zimbabwe.

### **1.5.1 Objectives of the study**

 The points that follow are the study's key goals:

1. Investigating and explaining the reasons of not complying with tax regulations by informal sector in Glenview, Harare, Zimbabwe.
2. To assess the problems faced by informal traders in complying with the tax regulations.
3. Examine the encounters faced by revenue authorities in collecting taxes from the informal sector.
4. To evaluate policies that can be put in place to increase voluntary compliance.

### **1.5.2 Research questions**

1. Why informal traders are not compliant to tax regulations?
2. What are the obstacles encountered by the informal traders when following with tax regulations?
3. What are the challenges faced by revenue authorities when collecting revenue from the informal sector?
4. How to improve voluntary compliance?

## **1.6 Significance of the study**

This part of the study is looking at the beneficiaries and how are they going to benefit from the research.

### **1.6.1 The researcher**

The researcher is enhancing personal growth by improving on research skills and by understanding the subject of tax compliance.

### **1.6.2 The government**

Helps tax administration agencies to implement policies which encourages citizen compliance and hence increase in revenues.

### **1.6.3 Informal sector**

The study will contribute significantly to the informal sector by assisting them to understand the meaning of non-compliance and to what extent it can affect them and also the formal sector.

### **1.6.4 Future researchers**

Future researchers interested in the field of rationale behind tax non-compliance will have reference.

### **1.6.5 Tax Consultancy Firms**

Small firms that look into penetrating the informal sector will have an idea of how best to approach them and advise them on the need to be tax compliant.

## **1.7 Assumptions**

For the purposes of this study, the following assumptions are made:

1. Informal sector players are aware of their tax obligations.
2. As number of informal sector players increases, tax base increases.
3. Taxpayer’s behaviour has influence on decision to comply.

### **1.8 Delimitation of the study**

The study’s goal is to evaluate the reasons behind non-compliance to tax regulations by the informal sector. Due to the decrease in employment opportunities in the formal sector which results in shrinking of the tax base, taxing the informal sector will expand the tax base hence increase in revenue collections. The study is restricted to the informal traders, who are in carpentry, metal fabrication, transport services, hairdressing saloon and food vending in Glenview Harare and also ZIMRA liaison officers and small consultancy firms in Harare. Areas of focus being Glenview home industries, Harare. Prior studies cover areas like Gweru, Bulawayo, Chitungwiza (Nyamwanza et al 2014, Mpofu 2021 Dube 2014) and other surrounding areas of Harare and there is no existing evidence when it comes to Glenview of which there are many informal activities conducted especially carpentry and has become the hub of many informal sector.

## **1.9 Limitations of the study**

* The research is focusing only on small enterprises which can make the findings not to be generalized. However, the researcher made sure that the sample was a total representation of the whole population.
* Complexity - Informal sector is a complex sector with too many divisions within it. Due to its complexity, the researcher is only focusing on the behaviour of carpenters, metal fabricators, hairdressers, transport operators and food vendors selling different food staffs at home industries in Glenview. These groups of informal sectors are preferred because of easy accessibility, and they are common in most parts of Zimbabwe.
* Resistance and fear- Given the researcher was asking questions in relation to incomes and taxation, the informal traders were not comfortable to disclose such information fearing that it could be incriminated against them. Many visits were made by the study's author to the locations where informal traders operate and assured them that she is non-political, and the study is only for academic purposes.
* Difficulties in translating everything that was said by the participants as some of them answered using vernacular language. However, the researcher transcribed everything that was said by the participants.

## **1.10 Definition of key terms**

* Tax – according to Taddesse (2022) is the mandatory contributions we all make to the Government monthly, quarterly, or annually as the law mandates. In this study, the researcher defined tax as an unconscionable fee imposed by the government on people and businesses.
* Compliance – according to Taddesse (2022) compliance is about taxpayers’ willingness to pay taxes. The researcher in this study defined compliance as the degree to which taxpayers adhere to taxation laws and regulations.
* Informal sector these are activities which State lacks access control mechanisms, and these business owners do not pay the necessary taxes, regardless of whether they are registered as a corporation and if they hold permits from the authorities.
* Presumptive tax is imposed on unregistered traders, small-scale miners, cottage industry, and transport providers. If an operator is in compliance with tax laws and has a current tax clearance, presumptive tax is not applied.

## **1.11 Summary**

This chapter explains the study's context, the issue statement, and its goal, which is to analyze the causes of the informal sector's noncompliance with tax laws and suggest solutions. Additionally, the study's purpose, importance, and limits are examined.

#

# **CHAPTER TWO**

# **LITERATURE REVIEW**

## **2.0 INTRODUCTION**

The subject of this chapter is theoretical and empirical literature about taxation compliance, with a focus on the concept of the informal sector and taxation, taxation compliances, challenges encountered by informal sector players when complying, problems encountered by revenue authorities when collecting revenue from the informal sector, and finally strategies for improving voluntary compliance.

## **2.1 Informal sector and Taxation**

The unofficial sector has been identified and interpreted to accommodate various situations (Hussman, 2004). For instance, (Hart, 1973) refers informal sector as the vast majority of urban poor people who were unable to secure substantial wage jobs and (Tanzi, 1982) defines the informal economy as the “underground economy”. (Maliyamkono and Bagachwa, 1990) define the informal sector as the “second economy”. In a similar vein, (Masarirambi, 2013) defines the informal sector as that part or sector which is not supervised and taxed by the government as compared to the formal sector. This sector consists of pursuits that fall outside the ambit of governmental rules and laws. Activities in the informal sector are not managed by the government although some traders for example flee-markets are paying rentals to the city councils. However, it is worth noting that the government has made strides in trying to formalise this sector with the Ministry of Woman Affairs, Community, SMEs Development dealing directly with this sector.

According to (Adekoya, Olaoye & Lawal, 2020) informal sector is the major driver of economic development in developing countries since it creates jobs for most people, it generates revenue and serves as a means of eradicating poverty. Major players in the informal sector are flea market operators, furniture manufacturers, producers and suppliers of farm produce, and street vendors (Chidoko, 2011). The informal sector is believed to have the highest share of the market as compared to the formal sector and most of the traders are into mining, manufacturing, transport, and commerce (Sparks & Barnett, 2010). In Zimbabwe, there are so many reasons behind the expansion of the informal sector over the years. (Sikwila, 2013) argues that hyperinflation between 2002 and 2008 led to the increase of informal sector players in Zimbabwe. During this era of economic meltdown, most citizens lost their jobs leaving them without an option prefer to work in the unofficial sector so in order to irk a living.

 According to (Sakuhuni, 2014) unemployment; structural adjustment policy, economic slide, wealth creation, and drought are the major drivers for informal sector expansion in Zimbabwe. On the same note, (Magure, 2014) argues that the closure of companies due to Economic Structural Adjustment Programme (ESAP) led to the build-up of a shadow economy resulting in the reduction of the tax base and hence low revenues which led to poor provision of public goods and services. Supporting the same view, (Zhou and Pindiri, 2016) argue that Economic Structural Adjustment Programme (ESAP) and the current political crisis are the major contributors to the increase in the informal sector in Zimbabwe. Besides economic struggles, (Stephen et al, 2015) argue that some informal sector players engage in these activities so as to avoid government regulations and most of them go informal so as to maximise their incomes. Also, (Zogli et al, 2017) believe that it is not always the case that the unemployed are the ones in the informal sector, some are employed in the formal sector but due to low incomes they take part in informal sector activities in order to supplement their incomes.

In the majority of developing nations, the informal economy is quite common and widespread, yet at the same time, governments struggle to generate enough revenue to meet their numerous needs. According to (Obara and Nangih, 2017) argue that developing countries lack sufficient funds to achieve their financial expenditures. The financial deficits in the majority of developing nations, including Zimbabwe, will be reduced by formalising and levying charges against the unorganized sector. As stated by (Mel et al, 2012) formalising and taxing the unorganized sector may contribute to the economic expansion of an economy and also provides greater benefits to the existing formal sector.

Taxation maybe be explained as the implementation of mandatory fees by the government on persons or entities. Benjamin Franklin once observed, "In this world, there is nothing that can be considered to be certain, except death and taxes" (James, 2012). The definition of tax depends on an individual’s perception as pointed out by (Olowokere and Fasina,2013). So, an increase or decrease in the tax rate will affect the government, entities, and individuals differently. Certain Sub-Saharan African nations reportedly encounter difficulties bringing both informal and official taxpayers into the tax net (Dube & Casale, 2016). This will lead a decrease in income, which will negatively affect the economy's capacity to provide public goods and services.

(Adekoya, Olaoye & Lawal, 2020) provide the three important factors for taxing the informal sector these are:

1. Revenue

The common and the primary purpose of taxes is to generate income to pay for the government's different expenses. The informal sector forms a significant percentage of activities in most countries and taxing it will increase revenue to the poor economies in order for them to survive (Schneider, Buehn, and Montenegro, 2010). Informal traders are mostly trading in similar goods and services leading to stiff completion and hence low incomes and even if they are taxed the revenues will still be low (Magure, 2014). Although the informal sector is growing and there is potential revenue, (Keen, 2012) is against taxing the informal sector since the administration costs will be more than the revenue to be collected.

1. Growth

Informal traders have limited access to credits, government contracts, training, and government grants and this will affect their potential to grow. (De Mel, McKenzie, and Woodruff, 2012) believe that formalising their businesses through registering with revenue authorities will unlock their potential to grow since it allows them to easily access credits and government grants. Furthermore, (Basley and Persson, 2014) argue that the informal sector players have low economies of scale and low exportation opportunities, formalising these firms will lead to greater benefits. On the other hand, (Klapper et al, 2010 suggest that there is a connection between growth and taxing the unorganized sector is not guaranteed, unclear and uncertain. Furthermore (Joshi, Prichard, and Heady, 2014) pointed out that formalisation of the informal sector might lead to economic gains but its impact on economic growth is not guaranteed.

1. Governance

Taxing the informal sector and enhancement of compliance will promote good governance in a way through trust, transparency, and accountability (Adekoya, Olaoye and Lawal, 2020). The willingness to register and pay taxes in the informal sector will be affected by the transparency of government expenditures and government accountability. Good governance will motivate traders to register with revenue authorities and do the right thing while bad governance will lead to the expansion of informal traders in an economy.

### **2.1.0 Methods of taxing the informal sector**

a) Presumptive tax

A tax known as presumed tax is imposed on unregistered dealers, small-scale miners, cottage industries, and transportation providers. According to (Shome, 1995) presumptive tax is used mostly as a stand-in for an income tax on small enterprises. A tax-compliant operator is relieved from presumptive tax given that he possesses a current tax clearance. Presumptive tax was implemented in Zimbabwe in 2005 and strengthened in 2011 so as to increase the tax base and hence revenue collections (ZIMRA, 2022). Income Tax Act (23:06) section 36C outlines the selected sections for presumptive tax; these include hairdressing operators, transport operators, bottle store operators, and driving schools. Presumptive tax has been under constant review from ZIMRA due to the rapidly changing economic landscape in the country, with the last review having been in January 2022 (ZIMRA, 2022)

The whole presumptive tax can be paid monthly, but transport operators must have done so by the 20th day following the end of each quarter. The presumptive taxpayers have the option of paying in US dollars at the current auction rate on the transaction date. Benefits associated with presumptive tax include enabling horizontal and vertical equity, and high revenue potential (Thomas, 2013). On the other hand, presumptive tax violates the rule of equity because tax is imposed based on the features or characteristics of the business in a one size fit all manner (Yitzhaki, 2007 cited in Sebele-Mpofu and Mususa, 2019). Another benefit of note as allured by (Shome, 1995) is that presumptive taxes may also enhance efficiency and equity of the tax system. Presumptive tax has the potential to increase the tax base by bringing in more taxpayers if implemented properly.

 Despite the benefits, (Semboja, 2015) argues that presumptive tax can lead to high-risk turnover under the declaration of revenues and there are high chances of corruption. On the same note (Zivanai et al, 2014) opinion that it is difficult to exclude large or medium enterprises from the presumptive tax system, and also some firms will remain small forever since there is no provision on to what period a business will remain covered under the presumptive tax. Supporting the same view, (Joshi, Prichard, and Heady, 2012) argue that as far as presumptive tax reduces the amount of tax for small businesses, it promotes reluctance to the informal traders.

b) Use of Association for Tax collections

Tax in the informal sector can be collected by the trade associations on behalf on the revenue authorities. For instance, in Zimbabwe Vendors Association can be an agent of collecting revenue from the informal sector guided by the principles and regulations provided by ZIMRA. According to ZIMRA (2022) ZINARA was chosen to act as an agent to collect alleged taxes from transport providers, taxicabs and driving schools. On the other hand (Sebele-Mpofu and Mususa, 2019) argues that there has been no improvement in presumptive tax collections in the transport sector since ZINARA took over. This method is not popular in Zimbabwe although used and it is producing great results in some African countries like Nigeria. According to (Adekoya, Olaoyo and Lawal, 2020) trade association leadership plays a crucial role as far as tax collections from the informal sector are concerned in Nigeria. (Ajeku, 2018) argues that taxing the informal sector can be efficient and successful by allowing trade association leadership to act on behalf of the government on revenue collection.

##  **2.2Taxation compliance**

Most developing countries are facing financial challenges to achieve their long and short-term economic goals due to taxation non-compliance since taxes are believed to be the most effective way in which governments fund their projects and expenses (Ameyaw et al, 2016). According to (Thiga and Mutuni, 2015) tax compliance refers to the capacity to perform tax payment obligations as required by the law. It is the taxpayer's commitment to follow local and international tax laws. Saw (2017) argues that capability to comply with tax laws is timely prepare and submit tax returns alongside the liability declared to the revenue authority. Tax non-compliance could be in the form of under-reporting of incomes on statements of affairs to the tax authorities for the purposes of tax assessment (Williams and Krasniqi, 2017). Taxation compliance either voluntary or enforced.

*Voluntary compliance* describes the willingness of the taxpayer to file returns and pay the liability without any form of influence from the authority (Gangl, Hofmann, and Kirchler, 2015). Taxpayers must pay the taxes and submit the required tax returns voluntarily without fearing the consequences of not doing so. According to (Modugu et al, 2012), voluntary compliance can only be achieved if there is trust. Taxpayers have to trust the revenue authority first before paying their share of taxes.

*Enforced compliance* is achieved when the revenue authority applies force on the taxpayers for them to comply. Revenue authorities may enforce high penalties for non-compliant taxpayers, punishment, or high chances of being caught then taxpayers might comply with tax laws fearing the consequences of not doing so (Adekoya, Olaoye, and Lawal, 2020). Supporting the same view, (Alm, 2018) opinion that it is of greater importance to combine investment enforcement facilities and trust may increase. In addition, this may not only enhance enforced compliance but also quasi-voluntary compliance.

## **2.2 Theoretical framework**

### **2.2.0 Taxation compliance theories**

There are two basic theories to the problem of taxation non-compliance which are economic theory and behavioural theory.

1. ***Economic theory***

Economic theory assumes that taxpayers are utility maximisers who increase their disposable income by not remitting their fair share of taxes to the authority. According to (Sandmo, and Allingham, 1972) in their A/S model, taxpayers will only comply with tax laws and regulations when the penalties and probability of detection are high. The model outlines three assumptions which are:

* Taxpayers are utility maximisers.
* Taxpayers have actual and perfect knowledge concerning the tax system.
* Increase in penalties and detection rate will lead to greater income declaration.

According to A/S model, one measure should be used at a time in order to curb non-compliance that is if penalties are high, detection levels should be low. Furthermore, they argued that mild punishment and high levels of detection are more effective since most taxpayers might not evade tax if the chances of being caught are high. Criticising this model (Srivanson, 1973) notes that if the likelihood of discovery is regardless of revenue, then there is a positive relationship between taxpayer’s income and evasion that is as income increases, non-compliance can also increase. On the same note, (Slemrod, 2007) argues that no research has been done to determine how the fine for evasion is applied to non-compliance.

Many scholars contribute to the economic theory by trying to identify and correct the loopholes in the A/S model.(Graetz, Reinganum, and Wilde, 1986) added to the theory by pointing out that the A/S model offers an insufficient theory of revenue collection and proposing a more sophisticated model for analyzing tax compliance incorporating a "game". This model states that the level of the evaluation of penalties, audits, and compliance is based on the relationship of the taxpayer and the revenue authority. Furthermore, (Smart, 1999) quoting (Cuccia, 1994) noted that the A/S model assumes that taxpayers have complete expertise ignoring the variations between the real and perceived audit, penalty, and parameter decisions. On the other hand, (Wallschutzky, 1984) points out that economic theory only focuses on taxpayers’ selfishness ignoring other important factors like equity although there is evidence that they contribute to non-compliance.

1. ***Behavioural theory***

This theory uses other academic disciplines to suggest that there are other additional factors that are important in motivating tax compliance. (Wenzel, 2003) contributed to the theory by suggesting that taxpayers are no longer selfish utility maximisers but human beings or businesses which are motivated to pay taxes by different attitudes, norms, beliefs, and feelings. According to (Slemrod, 1959) in his “tax mentality concept”, taxpayers are more willing to comply with tax regulations if they have a positive attitude towards the revenue authority and taxpayers have separate perceptions pursuing their own interests rather than enhancing the community interest.

Contributing to the behavioural theory (Spicer, 1974) states that taxpayers’ attitude toward paying tax is influenced by the quantity and quality of public goods and services produced by the government. In case the government is failing to produce basic public goods or producing at poor quality then taxpayers might find it not necessary to pay taxes. (Ajzen and Fishbein, 1980) provide Theory of Reasoned Action (TRA), in this model they are of the opinion that taxpayers’ actions toward tax compliance can be influenced by social groups. If the individuals around the taxpayer have a positive perception of paying taxes and they do then the taxpayer tends to do the same. Supporting the TRA theory (Lewis, 1982) suggests that there are three variables that can affect non-compliance intentions these age, moral stance, and opinions of people engaging in taxation non-compliance.

 (Kinsey, 1986) brings the concept of willingness to the theory. He argued that the level of following tax laws is determined by the readiness to corporate of the taxpayer, those who are willing to corporate are more compliant than those who are not. According to (Alm, Jackson and McKee 1992) the level of tax compliance may be determined based on how equitable the tax system is. The amount of tax paid by the taxpayer in relation to the benefits received in return for paying taxes, from the government; if the benefits are higher, the taxpayer may consider paying taxes to be worthwhile; if the benefits are lower, they are more likely to underpay or not declare the full amount.

Tax compliance theories are crucial for comprehending the idea of taxation compliance, but revenue authorities should employ them in tandem. For instance, in order to obtain high tax compliance, the amount of detection must be reasonable while still fostering confidence between the taxpayer and the revenue authority.

## **2.3 Challenges faced by informal sector players when complying with tax regulations**

Most informal sector players operate on designated and allocated stalls and they pay rentals to the city council authorities, on the other hand, they are not authorised by the department of company registration, Zimbabwe Revenue Authority and other relevant authorities (Uzhenyu, 2015). The informal sector in Zimbabwe is not registered with the department of company registration and ZIMRA meaning they only pay for the city council rentals and no other taxes. Some traders are not formalising their businesses due to formalisation costs and other reasons. According to (Goyal and Heine, 2021) formalisation of business is associated with financial costs and is sometimes time-consuming. In addition, they argue that these costs can be outweighed by the potential benefits of formalisation.

Attitude towards formalisation differs among individuals, most informal traders associate the formal sector with delicate tax laws and hefty taxes administration procedures (Slemrod and Weber, 2012; Schneider and Enste, 2013). The informal sector players perceive the formal sector as a very complicated sector with complex demands in terms of taxation and administration. More so (Williams and Nadin, 2014) argue that traders are not always forced to stay in the informal sector by necessity, sometimes they are attracted by opportunities available in the sector. Even if they register with the registrar of companies and the revenue authority, most of them will not file the returns or they will file nil returns. According to (Moore, 2020) among taxpayers registered with African national tax authorities, more than half do not pay any taxes.

According to (Dublin, 2014), tax non-compliance is in three forms which are under-reporting, under-payment and non-filling. This means that even if the taxpayer declares and pays the correct amount but failed to lodge the returns on time, he is not compliant. (Dome, 2013) argues that four essential compliance factors dimensions which include: registering a taxpayer when the necessary conditions are satisfied, submitting tax returns on time, paying taxes on time, and properly reporting tax liabilities. Failure to meet any of these dimensions the taxpayer is no longer compliant to tax regulations.

When trying to comply with tax regulations, taxpayers encounter some challenges in the process. (Tabandeh et al, 2012) argue that inflation, high tax rates, complex tax regulations, and trade openness are some of the challenges faced by the informal sector players when complying with tax laws. Given that most informal traders are trading on the same products there is very stiff competition in the sector which leads to low prices hence low incomes (Magure, 2014) believes that it will be difficult for the traders to pay taxes from the little income they have. High tax rates will make evasion more attractive, lack of trust in the government, and limited or nonphysical benefits contributes to informal trader’s non-compliance with tax regulations (Fakile and Adegbie, 2011).

According to (Sebele-Mpofu and Coetzee, 2019) high tax rates are a serious challenge hindering informal/ small traders to pay their fair share of taxes. High taxes are associated with low tax morale, high non-compliance, and a large shadow economy. Furthermore, they argued that in most developing countries, governments are failing to deliver quality public goods negatively affecting the morale of taxpayers. On the other hand, (Horodnic, 2018) argues that in some countries even though the tax rates are high, compliance and tax morale tend to be high due to the availability of trust between the taxpayer and the authority and also good governance.

A high compliance cost is the most critical challenge faced by the informal sector. These costs emanate from operations including the preparation of returns, tax accounting, and receipt collecting, tax clearance certificates, and tax planning (Eichneider and Vaillancourt, 2014). Furthermore, costs related to compliance are caused by complexity of tax laws, the understandability of tax regulations, and the number of tax rates (Sawyer, 2011). For instance, in Zimbabwe, there are various tax heads, and each tax head has its own tax rate and frequency of tax regulation changes (Eichfelder, Kegels and Schorn, 2011).

Tax compliance requires a lot of time to prepare the returns, declare the correct amounts, and pay the taxes to the authorities. According to a study carried out in South Africa by (Smulder et al., 2012) a small business requires an average of 255 hours per annum to deal with complex matters. (Adebis et al., 2010) state that unjust facility allocation, bad administration and mismanagement of tax revenue, and inaccessibility of taxpayers to government services are some of the problems leading to non-compliance in the informal sector. On the same note (Gurama, Mansor and Pantamee, 2014) assert that if taxpayers are not getting any service from the government, the level of compliance will decrease. According to (Horn, 2011) the informal sector comprises young and old aged people and most of whom are uneducated. Due to this fact tax law complexity will affect their behaviour (Ackermann, Fochmann and Mihm (2013), and also it will increase the demand for tax advice (Eichfeider et al, 2012) hence decreasing their willingness to comply with tax regulations (Alm, 2010).

Despite all the challenges believed to be faced by the informal sector traders when trying to comply with tax regulations, (Leyira, Chukuma and Asian, 2012) assert that some traders do not comply with tax regulations due to personal interests and governance.

## **2.4 Challenges faced by tax authorities when collecting taxes from the informal sector.**

Zimbabwe Revenue Authority (ZIMRA) presented a suppositional tax head in 2005 and further enforced it in 2011 in order to cover the informal sector under the tax net (ZIMRA, 2011). According to (Utaumire et al, 2013) proper application of presumptive tax legislation has the potential to increase revenue in Zimbabwe. Despite the introduction of presumptive tax as a measure to increase revenue, ZIMRA missed its annual collection targets by 6% and 7% in 2014 and 2015 respectively (Sebale-Mpofu and Mususa, 2019). This questions the effectiveness of presumptive tax in Zimbabwe.

According to (Keen, 2012) taxing the informal sector is a waste of resources since the costs incurred in the process might be more than the revenue to be collected in the informal sector. (Benhassine et al, 2018) assert that the revenue base was expected to increase through collections from the informal sector however, the attempt to correct revenue from this sector is limited due to the high costs of collection. It is highly challenging and expensive for the authorities to tax the so-called “hard to tax “sector. According to (OECD, 2010) taxing the unorganized sector is extremely difficult and challenging to the revenue authorities due to political and administrative issues.

Furthermore, (OECD, 2010) states that “the main strategy for raising administrative capacity has been to improve revenue collection... The biggest barrier to governments' capacity to generally collect taxes is frequently cited as being administrative”. According to (Adekoya, Olaoye and Lawal, 2020) it is very difficult for the revenue authorities to tax the informal sector because of administration problems, human capital and personnel shortages, the nature of record keeping, and finally nature of economic activities in the sector. In addition, taxation is not only an economic issue but also a political one. IMF (2012) argues that politics is negatively affecting taxation, especially in the informal sector. For instance, taxation regulations can be manipulated by politicians to win elections, especially by the incumbent.

Revenue authorities are facing challenges in capturing informal and formal taxpayers into the tax system due to a lack of funding (Dube and Casale, 2016). (ZIMRA, 2015) noted that the rapid expansion of street vendors in Zimbabwe shows a large number of potential taxpayers. However, (Vingirayi et al, 2020) assert that most if not all of them do not maintain accurate records, which makes it challenging for the authority to trace and obtain income from them. In addition, they pointed out that poor administrative constraints are the major issues contributing to poor collections in the informal sector.

Most informal sector traders transact in cash eliminating third parties like revenue authorities and some create shadow entities for goods and services not actually supplied, identifying them requires special skills and resources which can be expensive to the authority (Dube, 2014). Supporting the same point (Gallien, Moore and Boogaard, 2021) state that although it might be possible to deploy revenue authority officers in the streets to hook the informal traders, it is difficult to nab the professional ones, and technical skills are required to trace and nab them.

Corruption is very high among tax authorities making non-compliance very easy through bribing the officials (Nyamwanza, 2014). According to (Fjeldstad and Moore, 2009) when corruption levels are perceived to be high, taxpayers became unwilling to pay taxes they would rather bribe the officers as a means of lowering the tax obligation or not to pay at all hence reducing the levels of compliance. (Horodnic and Williams, 2016) state that widespread corruption and political interference in tax systems will lead to low morale, high evasion, and significant noncompliance. (Udoh, 2015) outlines the challenges of the informal sector on tax assessment and revenue collection as follows:

* Poor accounting and bookkeeping of business transactions.
* Poor relationship between the taxpayer and the revenue authority that is taxpayers lose trust in their government.
* High costs of collection outweigh revenues collections from the informal sector.
* Nature of activities carried out in the informal sector; they are many making it complex to establish a tax base.

## **2.5 Measures to increase voluntary compliance.**

Due to the challenges encountered by both the informal sector and revenue authority, there is a need to establish and enforce measures to improve compliance, tax base, and finally revenue. Voluntary compliance can be achieved by considering the following factors:

1. Emphasising transparency, services, and engagement

Voluntary compliance can be achieved through emphasising transparency, taxpayer services, and engagement. According to (Pinchard et al, 2019) transparency should be on overall revenue collections, public expenditure as well as on allocation of resources on selected sections. On the same note (Adekoya et al, 2019) argue that transparency will lead to fairness and hence increase tax compliance. If the taxpayers have the knowledge of how revenues from taxes are being used and they are seeing tangible results their willingness to pay may increase. On the other hand, (Khan, 2014) states that the quality of public goods provided by the government and transparency issues will lead to reduced budget flexibility and creates high expectations from the taxpayer. (Adekoya and Akintoye, 2019) assert that transparency and accountability on tax revenue collections will build trust and motivates taxpayers to comply with tax regulations.

1. Tax education and awareness

Educating the informal sector traders about taxation is very crucial as far as tax compliance is concerned, this can be through the media, posters, billboards, and roadshows. According to (Fatt and Khim, 2011) tax literacy and tax knowledge plays a significant role in taxpayers’ behaviour toward tax compliance for instance the ability of a taxpayer to use the e-filing system depends on one’s knowledge. (Gash, 2014) urges the authorities to continuously provide tax education and updates if there are any to the taxpayers. On the same note, (Sebele-Mpofu and Mususa, 2019) assert that ZIMRA should provide information to potential taxpayers and taxpayers through text messages, radio, newspapers, workshops, and seminars. Furthermore, they noted that educational programs like seminars and workshops should be carried out at zonal, district, provincial, and national levels.

1. Corruption control measures

(Adekoya and Enyi, 2020) define corruption as a form of dishonest and fraudulent actions taken by an individual entrusted with public power for private gain. Corruption is the use of public power for personal gains (Alm and Liu, 2018). Most developing countries are losing revenue from taxes due to bribery and corruption (Syadullah and Wibowo, 2015). Corruption can range from grand corruption (highest level) to petty corruption (small scale) and it can be in any form of activities which includes bribery, theft, fraud, and blackmail (IMF, 2016). ZIMRA should invest more in whistle-blowing and make sure those doing corrupt activities are thoroughly punished so as to set examples for others (Sebele-Mpofu and Mususa, 2019). In addition, ZIMRA officials, council officials, and any other officials working with informal traders should be empowered and motivated so that they can perform their duties with integrity.

1. Quality of tax services

Voluntary adherence can be achieved through better in terms of services the tax authority provided. According to (Adekoya, Folajimi and Ayodele, 2020) quality of tax services offered by the authority has a crucial impact on their behaviour and it determines the relationship between the taxpayer and the authority. A study carried out by (Eichfelder and Kegels, 2014) shows that a friendly relationship between taxpayers and Belgium tax authorities reduces compliance coast by 20% on average hence increasing compliance levels. More so a research project by (Hallsworth et al, 2017) in the United Kingdom shows that tax compliance can be increased by the application of two-way communications between the taxpaying individual and the taxing body on the issues of compliance. That is the authority must have the power to communicate with the taxpayers on the consequences of non-compliance to economic development and also, they should be able to listen and take into account queries from the taxpayers. (Bojuwon and Obid, 2015) classify the quality of tax services into three:

* *Responsive* refers to the time taken by the authority to respond to various queries and questions posed by taxpayers.
* *Formative* describes thetype of details supplied by the authority for example on websites and how current is the information.
* *Reliability* relates to the standardof the details supplied by the authority
1. Simplified tax laws

Tax laws should be written in simple and clear language so that most potential taxpayers and taxpayers will understand them. According to (Batrancea, Nichita and Batrancea, 2012) Tax laws for informal sector operators must be easy so as to enhance better interpretation that will help them understand more. In addition, they argue that a lack of knowledge and tax laws will grant the tax authority more power resulting in tax laws being made in the government’s favour.

1. Other measures

Revenue authorities must consider working with other institutions in collecting revenue that is instead of collecting revenue alone they can appoint trusted institutions as agents. For example, in Zimbabwe ZINARA was assigned as an agent to collect presumed taxes from transport operators, taxicabs and driving schools. According to (Sebele-Mpofu and Mususa, 2019) ZIMRA must work with other stakeholders in order to enhance compliance for example commuter omnibus operators should agree that operators should not pass through a tollgate or roadblock without a tax clearance certificate. (Adekoya, Olaoye and Lawal, 2020) argue that infrastructure development plays a vital role in increasing tax compliance. They assert that the availability of good infrastructure like good roads, constant electricity supplies, good telecommunication systems, good banking systems, good justice, and better security will change the perception of taxpayers towards taxation.

According to (Gallien, Moore and Boogaard, 2021) there are better ways to raise revenue efficiently and effectively other than focusing on the informal sector. Some of the ways provided are taxing wealth through income, property, and Capital gains, closing loopholes through and addressing the dysfunctional tax loss through corporate exemptions, and taxing digital transactions.

## **2.6 Review of Related Literature.**

Many authors have shown interest in the topic of the informal sector and tax compliance. There are also various studies carried out in African countries like Ghana and Nigeria. Studies in Ghana include informal sector compliance issues and the relationship between taxation and economic growth by (Ameyaw et al, 2016). According to the study, taxpayers comply mostly if they are benefiting from their tax payments and ethical values play a significant role in compliance decisions for individual taxpayers. The economic factors affecting compliance identified are tax rates, income levels, tax audits, fines and penalties, and audit possibilities. The gap between the amounts of tax owed to and paid to the Ghana Revenue Authority motivates the author(s) to investigate taxpayer behavior in Ghana.

Ameyaw et al, (2016) conducted a comparative study using descriptive and regression analysis in Ghana to explain the informal sector and compliance issues. The research findings of the study show that taxpayers’ attitudes, subject norms, and behaviour are the principal determinants of tax compliance, and also dishonesty in the tax system is negatively affecting the behaviour of taxpayers towards paying taxes. On the same topic, (Ajeku, 2018) conducted a study in Nigeria using survey methodology. The aim of the study was to identify whether formalisation of the informal sector through trade associations can improve revenue collections. In this study, it was observed that some traders are not aware of their tax obligations and some are not compliant due to poor service delivery by the government. Therefore, associations can play a significant role in increasing revenue collections only when the taxpayers know their citizen’s obligations.

Furthermore, Zivanai et al, (2016) carried out a study using surveys in Bindura, Zimbabwe, the study's primary goal is to identifying and explaining the possible causes of non-compliance to tax regulations by the small traders in Bindura. The findings show that social groups have a strong impact on tax non-compliance. When a taxpayer is surrounded by people who are not complying with tax regulations, he tends to do the same. Munjeyi et al, (2017) also contributed to the topic and a literature review was employed as methodology. The findings of this study show that there are no effective methods of collecting tax from the informal sector in Zimbabwe.

Thus, this study employed an exploratory design in the form of a survey using both qualitative and quantitative data collection method such that there is a greater understanding tax compliance and the informal sector critically focusing on Glen View area which is the hub of all informal sector in Harare and Zimbabwe at large and it had whiteness a massive increase in the informal business being done in this particular location only behind Mbare. Hence, a more up-to-date study on this area is needed taking into consideration the growth of informal sector activities in this particular location.

## **2.7 Chapter Summary**

This section initially discusses the concept of informal sector and taxation, compliance, challenges faced by the informal sector traders when complying with tax laws, problems encountered by ZIMRA when collecting taxes from the informal sector, measures that can be considered for improving voluntary compliance, and finally the empirical evidence reviewing previous studies carried out by different authors around the topic.

# **CHAPTER THREE**

# **METHODOLOGY**

# **3.0 INTRODUCTION**

To understand the concerns with informal sector taxation and compliance, this chapter outlines the methods the researcher utilized to acquire data for this specific study. Initially, it reviews the research design, population, sampling design, sample size, sources of data, validity, and reliability of data. Finally, the presentation techniques are going to be employed in the next chapter which is the findings chapter.

## **3.1 Research Design**

Durrheim (2004) claims that research design is a tactical framework for action that connects the research questions to the execution, or application, of the research strategy. Kumar (2009) further assets that a research design is a plan used to collect, analyses, evaluate and talk about the research's data. This study follows an exploratory research design in the form of a survey and both qualitative and quantitative data were collected. According to Saunders et al., (2012) Exploratory research design is a technique created to investigate phenomena that have not been studied or sufficiently described. In exploratory research design the researcher gains a general understanding and use research as a tool to help them find issues that need to be handled sooner. Exploratory research aims to provide light on the why and what of the topic being studied. Thus, the purpose of this study was to discover why there is non-compliance in the informal sector and what are the reason for this non-compliance thus making the exploratory research design the best research approach used in this study. However, it does not seek to answer the research questions definitively and conclusively; rather, it only delves into the subject of the research at various depths (Boru 2018).

A mixed research approach was employed through the use of two data collection techniques which are questionnaires and interviews. According to Green, (2007) mixed method design can be defined as “Multiple ways of seeing and hearing”. Kemper, Springfield, and Teddie, (2003) believe mixed method design includes both quantitative and qualitative data collection techniques. Questionnaires were used to gather quantitative data while interviews were used for qualitative data. This particular research methodology was selected because it is suited for the study since it aims to delve deeper into people's attitudes, feelings, and viewpoints regarding problems with informal sector taxation and compliance issues. According to Corbin and Strauss (2015) the combination of two data collecting tools produce the best enlargement of knowledge about the information being investigated. It also enables participation from a large population and guarantees a more representative sample, allowing for the generalizability of the results. Moreover, surveys are adaptable since they may be conducted in a variety of ways, including paper, telephone, and in-person interviews.

## **3.2 Population and Sampling**

### **3.2.0 Targeted population**

According to Mohom (2022) population is the group of people from which a statistical sample is taken for a research. The population comprised of informal traders from Glenview home industries in Harare, ZIMRA officials from domestic taxes at Kurima house in Harare and small tax consulting firms also located in Harare. The traders in the carpentry, metal fabrication, hair salon, and food vendor industries are chosen to represent the informal sector. For traders who were in carpentry the primary focus was on those manufacturing furniture like base beds, chairs, tables and wardrobes, and for those into metal fabrication the main concentration was on traders who are in door frames, window frames, screen doors and metal gates. The population of the informal sector also includes food vendors who sell basic grocery items like mealie-meal, sugar, salt, cooking oil, and other items, as well as traders who run saloons with a focus on manicures and hair braiding. The traders have moreover been working in the informal sector for at least five years. The researcher believes that during the course of their operations, these traders have picked up some valuable market or industry information. They also had little knowledge on accounting and tax filing data.

The population includes the employees who have worked in the small client's liaison office and register department for at least five years as domestic taxes department officers or who are presently employed there. The officials' further level of education includes a bachelor's degree and a ZIMRA qualification certificate, courses in taxation like ACCA and Chartered Governance and Accountancy Institute. Since they work with SMEs often, employees from these firms are thought to have knowledge of tax concepts and changes throughout time as well as a greater understanding of SMEs. The researcher thinks that because these officers have first-hand experience working with small businesses, they have a better understanding of them. They may also be aware of the policies that were implemented from 2015 to 2023 with the goal of assisting informal merchants and enhancing tax compliance in this industry. Eventually, there are a few small consulting firms that have been doing tax consultancy in Harare for at least five years. The personnel with a bachelor's degree and taxation courses like ACCA who have worked for these firms for at least five years worry the researcher since they deal with SMEs on a daily basis, these companies' employees are thought to have awareness of tax concepts and changes throughout time.

### **3.2.1 Sampling design**

Since it is difficult, if not impossible, for the researcher to survey the entire population, a sample is crucial, claims (Saunders, 2003). The researcher wants to acquire information pertaining informal sector and taxation from various informal sectors around Glenview, Harare. Owners of unregistered businesses in Glenview engaged in carpentry, metal fabrication, hair salons, and food vending were chosen to represent the unregistered sector for the purposes of this study. Owners of these firms were generally selected since they are frequently the managers and are familiar with the date of incorporation, sources of income, registration status, tax history, compliance status, and reasons for operating in the informal sector. The sample includes traders with and without academic credentials because the researcher was not interested in the academic credentials held by informal dealers. Due to practical considerations, Glenview's informal traders were chosen as a sample. Also, the researcher chose informal traders who have been in business for more than five years since they feel they have faced enough obstacles and have a better understanding of the market. Similarly, the researcher collaborates with representatives of the informal sector who are prepared to offer their opinions on tax evasion in the informal sector.

Particularly ZIMRA employees from Harare, Kurima House domestic taxes department who have worked or are currently working in the registry and the small client liaison office for the authority for five years or more. Those in this group were favored mostly because they had or still have direct working relationships with small businesses. Also, they are knowledgeable about company registration, compliance history with regards to returns and payments, as well as the difficulties associated with working with SMEs.

Also, the small consultancy firms that have been providing tax consultancy services for at least five years. The researcher must have access to information about taxation, such as the interactions between SMEs and tax consultancy firms or how these firms deal with SMEs on tax issues, the costs of various tax services, and their opinions regarding tax non-compliance. Tax consultancy firms provide tax services to SMEs and are aware of their challenges regarding tax issues. The time frame was chosen to make it simple for the researcher to track the pattern in terms of fares and operational circumstances.

### **3.2.2 Sample size**

The study used a technique called purposive sampling. A non-probability sampling method based on the study's goals and demographic characteristics is known as "purposeful sampling." Because the researcher needed to swiftly contact the intended group, this sampling strategy was helpful. 35 people made up the sample size, 20 of them worked in the informal sector, including 8 carpenters, 5 metal fabricators, 3 saloons, and 4 food vendors. Five small consultancy firms based in Harare and 10 ZIMRA staff were expected to participate from the sample size.

The number of SMEs the researcher ultimately ends up with, their age, registration status, and ownership status of the participants are all shown in the table below.

**Table 1: Attributes of the sample**

|  |  |  |  |
| --- | --- | --- | --- |
| **Activity** | **Age of SME****5-7 years 8-10 years** | **Registration Status****Registered Non-reg** | **Ownership****Owners Employees** |
| Carpentry | 4 | 2 | 3 | 3 | 5 | 1 |
| Metal fabrics | 2 | 3 | 4 | 1 | 3 | 2 |
| Saloon | 2 | 1 | 0 | 3 | 3 | 0 |
| Food vendors | 2 | 2 | 0 | 4 | 3 | 1 |
| **Total** |  **18** |

*Source: Primary data*

In table 1 above, for example, carpenters, and 6 traders out of an 8-person sample participated. Of those, 4 have been engaged in that particular activity for between 5-7 years, and 2 have been doing so for between 8-10 years. Finally, 5 of the participants were owners of the firms, while 3 were not registered with the revenue authorities for tax purposes, and 1 was an employee.

**Table 2: Sectors represented in the sample.**

|  |  |
| --- | --- |
| **Economic sector** | **Representing activities** |
| Manufacturing | Carpentry, metal fabrication |
| Tertiary/Services: (Retailing)  Services | Food vendingSaloonTax consultancy firms |
| Government services | ZIMRA  |

*Source: Primary data*

## **3.3 Sources of Data Collection**

According to Ndlovu (2021) data collection is the systematic method of gathering and obtaining data that answers the research questions. Throughout the study, both primary and secondary materials were used. According to Mesly, (2015), information can be gathered from primary sources (researchers are the ones who first receive data) or secondary sources (the researcher obtains data from existing sources for example tax filing information from informal traders, ZIMRA reports, and tax filling history from the revenue authority, registry department). In other words, primary sources are those that the researcher uses to gain information that has never been obtained by another researcher before, whereas secondary sources are those that allow the researcher to gather information from previously published papers. For this study's primary sources, questionnaires and interviews were used. For secondary sources, tax returns from SMEs, ZIMRA reports, and the revenue authority's registration department's tax filing history were used.

### **3.3.0 Primary sources**

a) Questionnaire

Questionnaires were used to collect data from informal traders and ZIMRA officials. 18 participants from the informal sector, including 6 carpenters, 5 metal fabricators, 3 saloon dealers, and 4 food sellers, were given questionnaires. Ten ZIMRA officials were also given a different set of questionnaires. Both closed-ended and open-ended questions were included in the survey. While closed-ended questions only allowed yes or no responses, open-ended questions allowed respondents to select one response from a range of alternatives and were formatted on a Likert scale. This was the primary data source used in conjunction with interviews. Questionnaires were completed electronically for convenience’s sake and respondents were free to answer questions without the researcher’s interference also at their own space of time.

In order to collect quantitative data, closed-ended questions were utilized, whereas open-ended questions were used to collect qualitative data. The researcher can learn more about the respondents' priorities and opinions on non-compliance and informal sector taxes issues by using open-ended questions. According to (Tichapondwa, 2013), open-ended inquiries enable the researcher to gather the information that may be buried deep within people's thoughts and emotions. Furthermore, the questionnaire was written in plain and simple language. In other terms, layman’s language was used so that traders in the informal sector could understand it, and respondents were free to disclose their personal experiences without fear. Due to the nature of the topic being studied, a questionnaire was important and necessary for the study. This method permits the researcher to collect sufficient data in a brief period of time.

b) semi structured Interviews

Interview was defined by Cohen, Manion and Morrison (2011) as a discussion between two or more persons about a subject of interest to both of them that aims to produce knowledge. The study employed semi structured interview for further information from 3 consultancy firms out of a total of 5 consultancy firm and 3 interviews were conducted with each participant one session lasting between 30 to 45 minutes as to gain maximum and full cooperation. A private and conducive place were found for each and every participant from the consultancy firm. According to Horton et al (2011) cited by Mudhovozi (2012) claims that a semi-structured interview gives the researcher some latitude to express their ideas, to draw attention to areas of special interest and expertise that they felt they had, to allow for more in-depth questioning of specific responses, and in particular to draw out and resolve apparent inconsistency. When conducting a semi-structured interview with participants, the researcher utilized questions that elucidate the reasons for non-compliance of informal sector and how they can be improved and allow them to answer using everything but in relation with the topic under study. Where necessary and when greater clarity was required, the researcher might go deeper. Semi-structured interviews were advantageous because they gave the researcher the opportunity to address the phenomena in depth while giving the informants a room to convey their experiences in detail, as closely as possible to reality (Padilla-Diaz 2015).

(c)Pretest of questionnaire and interviews

A pretest study was done in Glen view, ZIMRA officials and tax consultancy firm that were not participants in the actual study were given the opportunity to answer to interviews questions and questionnaire. The effectiveness of the research instrument of semi structured interview and questionnaire was to check bias, sequence, clarity, and correction where they need to be done. This kind of excise helps the researcher to determine the usefulness and trustworthiness of semi structured interview and questionnaire guide which has been set by removing ambiguities and inadequate wording from the question (Marshall and Rossman 2011)

### **3.3.1 Secondary sources**

Using secondary sources involves acquiring information from previously published texts that are in the public domain. Data was gathered for this study from prior tax returns, ZIMRA reports, website information, and tax history provided by the revenue authority. According to Tichapondwa, (2013), secondary data analysis is extremely important since it supports the interviews and questionnaires. Also, it might help in finding answers to queries that can't be answered through questionnaires or interviews. Since the primary goal of using, it was to compile the information already available on compliance and informal sector taxation, this source greatly contributes to the researcher's understanding.

## **3.4 Validity and Reliability**

The research was carried out as nearly as was practical to those restrictions in order to assure dependability and validity. In order to eliminate subjective questions that led to incorrect answers, Saunders et al. (2009) argue that the validity and reliability of the data obtained depends on question designs and questionnaire structure. According to Bryman and Bell (2008), reliability was related to the tool's consistency, whilst validity was related to the results' veracity and correctness. The researcher in this instance conducted a pilot test of the questionnaire and interview guide as a method to increase the validity and reliability while continuously analyzing the data gathered. Participants who were carefully recruited and who shared all of the target group's characteristics were given the instruments.

Furthermore, to increase clarity for this study's objectives, information triangulation from various sources of data collection was used. Data triangulation, according to (Ritchie and Lewis, 2003), can be utilized to solve the challenges associated with relying on only one source for research and improve validity. According to (Patton, 2000), who supports the same point of view, data triangulation gives one confidence when drawing conclusions. In addition, according to (Lincoln, 1995), one advantage of data triangulation is its capacity to combine and complement other methodologies, producing conclusions that are more trustworthy and valid.

## **3.5 Data presentation and analysis**

Data will be gathered, analysed, and then presented in a precise and comprehensible way. According to (Jewel, 2001), after data collection, a clear presentation is necessary to facilitate communication and the drawing of conclusions. The main data from the sample elements served as the basis for the analysis. Both frequency analysis and descriptive statistics will be performed. Microsoft Excel was the computer program used in the study. The method enables the researcher to think analytically based on the goals of the investigation. The respondent's right to privacy and confidentiality was respected throughout the data collection process. Tables, pie charts, distribution tables, and bar graphs will all be used to illustrate the results of the data analysis.

## **3.6 Ethical Consideration**

According to Bryman (2012) Ethical consideration are principle that guide research process and they protect both research participants and the researcher during the whole research process. Ethical consideration creates a win-win situation between the participants and the researcher. The researcher paid particular attention to the following ethical consideration when she conducted the study confidentiality and informed consent.

(a) Confidentiality

Confidentiality refers to the ability to keep the identities of the research participants unknown. The researcher ensured that the research participants remained anonymous through the use of pseudo names. In a bid to guarantee confidentiality the researcher also maintained privacy with the researcher participants. The researcher also made effects to ensure that the identities of the participants remained anonymous.

(b) Informed Consent

According to Smith (2013) informed consent refers to granting of permission to the researcher to attain and later disclose information. The researcher thoroughly explained what the study was about, why the study was being conducted and the possible benefits as well as disadvantages to the study. The researcher also upheld informed consent by letting participants sign consent forms prior to the study. This also ensured the ethical consideration of voluntary participation as the participants could decide whether to participate in the research study or not. Through informed consent the research subjects were made aware of their rights to refrain from participating in the research study at any moment and their ability to not disclose the information if they fill uncomfortable or they feel it could infringe with their rights.

## **3.7 Chapter Summary**

In conclusion, this chapter covered the data collection techniques and provided a comprehensive explanation of the research design, population, sampling design, sample size, and data sources. The chapter also aims to describe the approach used to gather data for the issue of non-compliance and informal sector taxation, with Glenview, Harare, as the focus region. Also considered were the data's quality and dependability. Research findings and data analysis will be covered in the following chapter.

#

# **CHAPTER FOUR**

# **DATA ANALYSIS, PRESENTATION, AND INTERPRETATION**

## **4.0 INTRODUCTION**

The chapter is presenting, analysing, and discussing the findings from interviews, questionnaires, and secondary sources. Initially it provides the response rate from respondents and background of the respondents. It goes on to present, analyse and discuss the findings of the study, for analysis descriptive analysis was used and for presentation tables, bar charts and pie charts were used.

## **4.1 Response rate of the study**

Table 3: Response rate

Frequency Percent Valid Percent Cumulative percent

Questionnaire 28 80% 80% 80%

Interviews 3 8.6% 8.6% 88.6%

Non-response 4 11.4% 11.4% 100%

Total 35 100% 100%

*Source: Primary data, 2021*

From table 3 above questionnaire were distributed to 30 respondents and 5 interviews were expected to be done. Out of 30 questionnaires, 20 were directed to informal traders and 10 ZIMRA officials. Twenty-eight (28) questionnaires were returned fully completed that is 18 from informal traders and 10 ZIMRA officials representing 80% of the response rate. Interviews were administered to 3 respondents out of a sample size of 5 representing 8.6% of the response rate. 2 informal sector questionnaires were not responded to and also 2 interviews were not successful making 11.4% non-responses. The study achieved a response rate of 88.6% and non-response of 11.4%. As stated by Krejicie and Morgan table (1970), the table entails that the population of 30-35, should have at least 28 respondents. Therefore, the response rate was enough to represent the population under study and it allows the results and conclusions to be generalised.

## **4.2 Background information of respondents**

### **4.2.0 Informal traders**

Table 4: Ownership distribution

 Frequency Percentage Valid % Cumulative%

Owners 14 77.8% 77.8% 77.8%

Employees 4 22.2% 22.2% 100%

Total 18 100% 100%

*Source: primary data*

Out of 18 respondents from informal sector, 14(77.8%) were the owners of the firms and 4 (22.2%) respondents were employees. The distribution shows that the aim of having owners of the SMEs so as to obtain information needed for the study was achieved.

Table 5: Tenure in business frequency distribution

Period (years) Frequency Percentage Valid % Cumulative %

5-7 10 55.6 % 55.6% 55.6%

8-10 8 44.4 % 44.4% 100%

Total 18 100% 100%

*Source: Primary source*

The trading period distribution presented on table 5 shows that 10 (55.6%) informal sector respondents have been operating in this sector for the period between 5 to 7 years and 8 (44.4%) have been operating for a period between 8 to 10 years. This indicates that the respondents participated in this study were in the sector for some time and they appreciate the operating conditions and the demands for the sector. As stated by Mahamed (2015) traders who operate in a particular industry offering same type of products have more knowledge on the requirements of the industry and tax obligations as compared to new entries. However, Mel (2013) argued that if an informal trader operates in the same line of production for a long period of time, the chances of non-compliance could be high since they appreciate the techniques and operating conditions hence can easily find smart ways to evade taxes without being caught or with minimum chances of being caught.

Table 6: Educational qualifications

Qualification Frequency Percentage Valid % Cumulative%

Primary level 0 0 0 0

Secondary 5 27.8% 27.8% 27.8%

Advanced 7 38.9% 38.9% 66.7%

Diploma 4 22.2% 22.2% 88.9%

Degree 2 11.1% 11.1% 100%

Total 18 100% 100%

*Source: Primary data*

Table 6 shows the educational levels of the informal respondents participated in the study. 27.8% had secondary level, 38.9% advanced level, 22.2% diplomas and 11.1% degrees. According to Helhel and Ahmed (2014) educational qualification plays a crucial role on tax compliance matters since those with higher education tend to comply more because they can understand the tax laws better than taxpayers with low levels of education. Maseko (2014) concurs with the thought by pointing out that educational qualification contributes to understandability of tax responsibilities. However, Nyamwanza et al (2014) opposed the opinion by revealing that there is no correlation to support the relationship between tax compliance and taxpayer’s educational levels therefore compliance behaviour cannot be determined by one’s educational levels.

Table 7 below shows the registration status of the respondents participated in the study. It reveals that only 7 (38.9%) are registered for tax purposes and 11(61.1%) were not registered due to various reasons which includes low incomes and ignorance to tax obligations. This is in line with Joshi et al (2014) who pointed out that formalisation of informal sector may help them to expand since they can easily access loans, government support and tenders. On the other hand, McKenzie, and Sakho (2010) argues that formalisation of informal traders and registering for tax purposes might not be beneficial to them due to sizes of their businesses.

 Table 7: Registration status

Registration status Frequency Percentage Valid% Cumulative%

Registered 7 38.9% 38.9% 38.9%

Non-registered 11 61.1% 61.1% 100%

Total 18 100% 100%

*Source: Primary data*

**4.1.1 ZIMRA officials**

Tenure of service in domestic taxes (ZIMRA officials)

Fig 1

*Source: Primary data*

Fig 1 above shows the tenure of service of ZIMRA officials in the domestic taxes department (liaison and registry officials). All the respondents were employed and stationed in the domestic taxes department and they never transferred to customs. 30% (3) of the respondents have been in service for more than 10 years, 50% (5) have been in domestic taxes for 8 years and 20% (2) respondents have been there for 6 years. Because of the diversity in experiences, the tenure distribution allows the study to collect enough diverse and quality data from these respondents on tax compliance and the informal sector.

### **4.1.2 Small consultancy firms**

Fig 2 below shows the tenure or period of operation for small consulting firms participated in the study. It shows that 60% (3) of the respondents have operating as tax consultancy for the period between 5 to 8 years, 40% (2) serves in the industry for more than 8 years. The differences in tenure of operation assures that the respondents are aware of the tax rates, changes in tax policies and other tax matters occurred between 2021 and 2023.

**Fig 2**

## **4.2 Presentation and Analysis**

This section analyses the data collected from the selected samples of the informal sector, ZIMRA officials, and tax consultancy firms.

### **4.2.0 Reasons behind non-compliance in the informal sector**

The questionnaire asked ZIMRA-registered respondents which tax head they were registered under and whether they declared and paid the correct amount to the authority. All of the 7 respondents who said they were registered with ZIMRA were registered for income tax, however, several were also responsible for PAYE because they had employees. Whether or whether they remit the correct amount of taxes to the authority, 4 (57%) indicated that their paying behaviour depends on the earnings in that particular period. They stated that if their income is low, they will pay less or not pay at all, however, if their income is great, they will pay the whole or nearly full amount. The remaining three (33%) respondents stated that they fully comply with tax regulations regardless of income level or other considerations. These findings support Moore's, (2020) who states that registering with the authority does not ensure high revenue collections because the majority of registered SMEs submit no returns. This is further supported by Magure (2014) who found out that paying taxes in the informal sector can be difficult due to low incomes.

The findings revealed that the reasons for noncompliance of informal sector are due to their incomes which are low owing to competition in the industry, of which paying taxes will deplete their incomes as supported by 80% of the participants. The findings also revealed that some informal sectors are unaware of their tax obligations and do not grasp the distinction between council rates and taxes collected on behalf of the government by ZIMRA as supported by 20% of the participants. The participants also revealed that the tax rates are excessively high, particularly for presumptive tax, and that the majority of respondents do not keep financial records, making it difficult, if not impossible, to account for income tax. This is consistent with the findings Tabandeh et al (2012), which found that high tax rates, complex tax systems, and high inflation rates are important drivers to tax non-compliance. This is in line with the behavioural perspective, Kinsey, (1972), which states that tax system inequity influences taxpayer compliance behaviour. Furthermore, according to the A/S model Allingham and Sandmo (1970), low fines and detection levels incentivize noncompliance.

The findings also revealed that the vocabulary used in tax regulations can be foreign to most informal merchants as postulated by the tax consulting firms “*the tax heads are too many, and informal traders require an understanding of their peculiarities as well as the requirements for each tax head*”. This is consistent with Hon (2011), who states that some SMEs fail to comply with tax requirements because they do not grasp the statutes due to the wording utilised. Furthermore, tax consultancy firms suggested a strategy to increase compliance of informal traders need to understand the difference between ZIMRA taxes and council rates.

In a questionnaire, respondents (informal merchants) were questioned whether the nature of tax systems influences tax compliance and how the government allocates tax revenues affects their desire to pay tax. These assertions were evaluated as strongly disagree, disagree, uncertain, agree, and very agree, with respondents' responses accurately representing their beliefs on each topic pertaining to why they were neglecting to pay taxes. The outcomes are shown in table 8 below.

**Table 8: Reasons behind tax non-compliance**

 Nature of tax systems affects the willingness Government expenditure affects our

 to comply with tax laws willingness to comply

Strongly disagree 1 1

Disagree 1 4

Uncertain 3 0

Agree 5 3

Strongly agree 8 10

Total 18 18

The table shows that 1(5.6 %) respondent strongly disagreed with the view that nature of tax systems (complexity or simplicity) affects their behaviour towards tax compliance, 1 (5.6%) disagreed, 3(16.7%) were uncertain, 5(27.8%) agreed and 8(44.4%) strongly agreed with the view that the nature of tax systems affects their compliance behaviour. On the opinion that how government spend or distribute income affects their willingness to pay taxes a group of 1 (5.6%) respondents strongly disagreed with the opinion, 4(22.2%) disagreed, 0 were uncertain, 3(16.7%) agreed that government expenditure affect their willingness to comply and 10 (55.6%) strongly agreed that how government spend or distribute income has an impact on their willingness to pay taxes.

In view of the above analysis, the study found that informal trader’s willingness to pay taxes can be affected by the complexity or simplicity of tax systems as well as how government distribute or spend tax revenue. This was shown by 8(44.4%) and 10(55.6%) respectively who strongly agreed to the statements. This is similar to the findings of Tabandeh et al (2012) the complexity of tax systems affects taxpayer’s compliance behaviour. Findings from the study and literature agree that high tax rate, complex tax systems, low incomes are major drivers of non-compliance in the informal sector. In addition, the study pointed out that the way government spent revenues has an impact on taxpayer’s compliance behaviour. More so the study pointed out that some traders are not aware on the difference between taxes and council rates. Finally, too many tax heads confuse the taxpayers reducing their willingness to comply with tax laws.

### **4.2.1 Challenges faced by informal traders when complying with tax systems.**

The researcher offers the floor to the informal traders to discuss the obstacles they experience, which affect their tax compliance and registration with the revenue authority in some way. According to their responses, 80% of respondents do not know how to go about the registration procedure, filing returns online, or paying. Furthermore, they stated that their level of tax education is so low that they do not know the difference between council rates and tax rates. “*There is need to use simple terms and methods to try and make the informal traders understand the difference between taxes and council rates … it’s easier to use layman’s terms for them to understand better the differences between the two”* This is in line with Hon (2011) who states that the levels of education on tax matters affect the understand-ability of taxpayers hence affecting their compliance behaviour.

The findings revealed that informal traders face challenges as their activities take a lot of time and that their schedules do not always allow them to do other things like prepare returns as supported by 5% of the participants. *“Most of the informal traders have limited time due to the nature of their work which prohibits them from filing tax returns from the stipulated time frame”* This is consistent with the findings of a study conducted by Smulders et al (2012), which reveals that the procedure leading to compliance is time intensive.

Furthermore, 15% of respondents claimed that the complexity of tax systems and several tax heads is a key difficulty since they occasionally register on incorrect tax heads due to a lack of sufficient tax expertise. This is in consistent with Eichfeider et al (2012), the complexity of the tax system necessitates tax guidance from specialists, resulting in a rise in compliance expenses.

Furthermore, Glenview respondents reported receiving little or no government assistance in order to expand and achieve higher wages*. The only time we have seen government officials here is if they want support on government projects however, they have never come here with solutions on how best we expand our businesses. We have experienced major setbacks where our wares have been destroyed by fire and government has not chipped in with any help*. This is in agreement with the findings of Fakile and Adegbie (2011), who states that most governments in developing countries do not support the informal sector, which may lead to noncompliance because traders may see no reason to pay taxes if they are not benefiting from them. Furthermore, respondents were asked who controlled their books of accounts, and the majority stated that they keep the books themselves since they lack the financial resources to engage a tax accountant. Because traders may see no incentive to pay taxes if they are not profiting from them.

The researcher questioned tax consulting organisations about the services they provide to small businesses, the fees they charge, and the obstacles they believe informal traders have when it comes to tax matters. Small businesses, according to the respondents, require registration services, tax clearance, and return submission. The fares were $150 USD, $50 USD, and $30 USD, respectively. This concurs with Eichneider and Vaillancourt (2014) who states that, tax compliance costs include consultancy services (tax guidance and planning). Furthermore, the study discovered that social groupings have an impact on tax compliance; if the leader(s) of a social group decide not to pay tax, all group members may follow suit.

Based on the above analysis the study and prior literature agree that low government support, high compliance costs, poor tax education, and time consumption are the major challenges faced by the informal sector. In addition, the study found that most SMEs’ books of accounts are being managed by the owners as they cannot afford consultancy services.

### **4.2.2 Challenges faced by revenue authorities when collecting revenue from informal sector.**

Out of 10, ZIMRA officials 7 officials were currently working in the liaison office with small traders and 3 working in the registry section. Responding to the question on which ways government put in place in order to collect tax from the informal sector, the methods provided by the officials includes issuing of permits to informal traders, use of Income Tax Act (chapter 24:06), use of government authorities and lastly presumptive tax. All the respondents indicated that the most common method is presumptive tax. Income Tax Act (23:06) outlines the activities which are covered under presumptive tax.

The respondents were asked to comment on the effectiveness of these methods as a way of collecting taxes from the informal sector. This helps to identify the effective method of collecting revenue from the informal sector which can be fully implemented. The results were rated in terms of ineffective, poor, effective, and very effective.

Information presented in fig 3 below shows that a group of ZIMRA officials represented by 10% rated the methods of collecting taxes from informal sector as very effective, 15% rated them as effective, 30% rated them as poor and finally 45% indicated that the methods are very ineffective. This is in agreement with Thomas (2013) presumptive tax is effective in developing countries as it enables horizontal and vertical equity and also aid to lessen tax burden from the formal sector. On the same note Sebele-Mpofu and Mususa (2019) cited by (Yitzhaki, 2007) argued that the repressiveness of presumptive tax violates the rule of equity since the fares are equal to a certain group and it does not consider the differences in incomes.

**Fig 3: Effectiveness of collection methods**

*Source: Primary data*

The findings revealed that the challenges faced by tax authorities when collecting revenue from the informal sector include insufficient administration resources as supported by 80% of the participants. The officials pointed out that ZIMRA does not have the capacity in terms of labour and finances to acquire sufficient and suitable material which can facilitate the collection of revenue from the informal sector*. We are incapacitated in terms of resources and the salaries we get are being easily eroded by hyperinflation…so we are not motivated to do our jobs to the extent that sometimes we end up doing side hustles at the time we are expected to be doing our jobs.* These findings concur with Joshia and Anye (2009) who found out that revenue authorities from developing countries lack sufficient resources or personal capacity to establish, implement, monitor, and enforce tax laws and regulations.

The other challenge faced by ZIMRA officials is lack of power to enforce payments, information sharing challenges and massive corruption are some of the challenges affecting tax authorities when it comes to revenue collections from the informal sector. *We face resistance from informal sector who mistake us as council police who usually ask for bribes…. Also, the authorities sometimes fail to explain thoroughly to the informal sector why they should pay tax*. This is also similar to the findings of the study carried out by Nyamwanza, (2014) who states that corruption in the tax systems is hindering the revenue authorities from collecting revenues in the informal sector.

In addition, the respondents indicated that due to poor bookkeeping and the complexity of activities in the informal sector it is very difficult to collect taxes and if managed the costs of collections will be too high than the revenues to be collected. As pointed in the literature by Benhassine et al (2018) costs of collections are too high hindering the authorities to act in full capacity. This is further supported by Udoh (2015) who pointed out that informal traders usually do not keep records of finances and activities making it difficult to the authorities to manage them.

### **4.2.3 Measures to increase voluntary compliance.**

Table 9: Measures to improve voluntary compliance.

 Frequency Percentage Valid % Cumulative %

Simple tax systems 8 44.4% 44.4% 44.4%

Improved communication 4 22.2% 22.2% 66.6%

with informal traders.

Less tax heads 4 22.2% 22.2% 88.8%

Provision of public goods 2 11.2% 11.2% 100%

Total 18 100% 100%

Respondents were asked to provide suggestion on how government can improve voluntary compliance in the informal sector and the answers are presented in table 9. Out of 18 respondents from the informal sector, 8 (44.4%) suggested that simple tax systems may improve tax compliance in the informal sector. The finding concurs with Batrancea, et al (2014) that simplified tax laws have positive impact on taxpayer’s compliance behaviour.

The findings revealed that two-way communications between informal sector and revenue authorities is important especially when putting in place new tax legislations directing to them or when increasing tax rates as supported by 4(22.2%) of the participants. *They can introduce seminars to teach the informal sector on the importance of paying tax.* This is agreement with Eichfeider and Kegels (2014) who states that the relationship between taxpayers and tax authorities is very important and positive relationship enables two-way communications which allows better services from the authority hence positive attitude towards paying taxes.

 In addition, 4 (22.2%) respondents pointed out that there is need to decrease the number of tax heads in the tax system is essential. This is consistent with the findings to Batrancea, Nichita and Batrancea (2012) who found out that tax laws for informal sector operators must be easy so as to enhance better interpretation that will help them understand more.

lastly 2(11.2%) of the respondents indicated that provision of public goods and services by the government to appreciate the tax paid by traders is very crucial as far as tax compliance is concerned. *There is need to introduce policies that reward those who pay tax. This may encourage many to pay tax*. These findings are the same as of Pinchard et al. (2019) transparency should be on overall revenue collections, public expenditure as well as on allocation of resources on selected sections.

Respondents from ZIMRA indicated that voluntary compliance can be achieved through continuous offering of education to the informal sector, reduction of tax heads, sharing of information between revenue authority and all other government or private sectors working with the informal sector so as to maintain the uniformity of information from all parties. This is similar to findings of Gash, (2014) pointed out that continuous provision of tax education is importance as it enhance better understanding on tax laws to the informal traders. Furthermore, measures to reduce levels of corruption must be put in place; the officials suggested that this can be done through motivating employees by both financial and non-financial means. This is in line with Sebele-Mpofu and Mususa (2019) who states that tough measures must be put in place so as to control the levels of corruption in the tax system. Finally, the officials suggested that government should support revenue collection programmes at the same time providing public goods back to the society.

The findings indicated that transparency and accountability on government expenditure will motivates the informal traders to register and pay taxes hence increase in the revenue collection. This is similar to the findings of Pinchard et al, (2019) who identified that taxpayers are more willing to fulfil their tax obligations when they are aware of the national budget and how finances are being allocated. This is further supported by Khan (2014) who indicated that fair distribution of incomes among districts, provinces have impact on taxpayers’ behaviour towards compliance.

## **4.4 Chapter Summary**

The findings from questionnaires and interviews are explained, analysed, and presented in this chapter. It first displays the structure of the answer rate, as well as the characteristics of informal traders' respondents, such as age, duration of operation, and gender. It then goes on to provide and assess the results of surveys given to informal sector and ZIMRA officials, as well as the findings of interviews conducted with omnibus operators, tax consulting firms, and Glenview municipal authorities. The following chapter will examine the researcher's proposals, which may lead to the decrease or eradication of the problem of tax noncompliance in the informal sector.

#

# **CHAPTER FIVE**

# **SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMENDATIONS**

## **5.0 INTRODUCTION**

This chapter summarises the study findings, draws a conclusion, and makes recommendations to address the problem of tax non-compliance in the informal sector. Initially, the chapter provides summary findings and conclusions on the reasons for informal sector non-compliance, challenges faced by the informal sector in complying with tax regulations, challenges faced by revenue authorities in collecting revenue from informal traders, and finally, suggestions on policies or measures that can be implemented to improve voluntary compliance. It then makes recommendations on how to lessen or eliminate the problem of tax noncompliance, as well as areas for additional research.

## **5.1 Conclusion**

The study concludes that taxing the informal sector is very significant and vital in developing countries since it can increase revenues while alleviating obligations on the official sector. The most important conclusion reached from this study is that the revenue authority in this case ZIMRA, lacks the resources to collect tax from the informal sector, which is marked by complex operations that may be difficult to manage. Informal sector traders, on the other hand, lack adequate information about their tax obligations. Presumptive taxation is a superior means of collecting income from informal traders; nevertheless, all revenue leakages must be closed for it to be effective and produce better returns. The study discovered that the majority of SMEs are not registered, demonstrating the poor performance of presumptive tax to the fiscus, and finds that the primary causes of non-compliance are low incomes, complex tax systems, and high compliance costs. Furthermore, the study finds that government support for tax programmes, tax head reductions, the provision of public goods, and tax education may boost citizens' desire to comply with tax regulations.

### **5.2.0 Reasons behind tax non-compliance in the informal sector**

The research found that, most informal traders in Glenview, Harare, do not comply with tax requirements due to poor income. Because of market competition, the prices of goods and services offered in the informal markets are low, resulting in low levels of revenue. Furthermore, the survey discovered that most traders are breadwinners with at least one dependent in their households, implying that they seek more income to maintain their families and that paying taxes may deplete their earnings. The nature of presumptive taxation was also identified as a barrier to tax compliance in the informal sector.

Presumptive taxation is regressive, which means that the tax band is the same for everyone, regardless of income level. Furthermore, the study discovered that complex tax systems and an abundance of tax heads lead to noncompliance. Excessive taxation without sufficient education will confuse informal traders, limiting their motivation to comply with tax procedures. In addition, poor supply of public goods and services, as well as government assistance in the informal sector, discourages people from paying taxes. As a result, the study suggests that low incomes, poor tax education, complex tax systems, high tax rates, inadequate supply of public goods, and an abundance of tax heads all contribute considerably to informal sector noncompliance.

### **5.2.1 Challenges faced by the informal sector when complying with tax laws.**

The study observed that, the key issues faced by the informal sector include high compliance costs, a lack of information and tax understanding, and the complexity of tax systems. Because of the low levels of income made by Glenview's informal carpentry traders, metal fabricators, food sellers, and hairdressers, consultancy services are too expensive for the majority of them. Furthermore, the study discovered that informal traders in this area lack information about tax obligations and are not consulted when tax rules change or are going to change. Furthermore, the study discovered that the nature of informal sector activity necessitates a significant amount of time, making it difficult for merchants to devote time to completing returns and researching tax issues. Finally, the study found that the informal sector lacks government support to grow and participate in activities that would benefit the economy more. As a result, the study indicates that the key obstacles faced by informal traders are high compliance costs, a lack of government support, a lack of information about tax matters, and the complexity of tax systems.

### **5.2.2 Challenges faced by revenue authorities when collecting revenue from the informal sector.**

The study discovered that weak tax administration limits were the biggest obstacles faced by tax authorities in collecting revenue from informal traders in carpentry, metal manufacturing, food vending, and hair salon. This is demonstrated by a lack of labour and financial resources to register and monitor informal sector activity. Furthermore, the study discovered that presumptive tax is the most often used method in Zimbabwe, but the outcomes were unsatisfactory due to a lack of funding that allows for follow-ups with traders.

Furthermore, the study discovered that revenue authorities have another issue due to corruption in the tax system. Traders that buy items outside of Zimbabwe for resale admit to paying bribes to ZIMRA employees in order to avoid or lessen tax liability at the expense of paying taxes to the government. The survey also discovered that traders in the food vending and saloon industries purchase goods from foreign countries for resale and enter the nation through undesignated locations in order to avoid paying taxes. As Kus (2010) points out, the majority of informal traders in developing nations enter through designated or undesignated points without paying presumptive tax to the authority, limiting income flows to the fiscus. Furthermore, the study discovered that ZIMRA has fewer capabilities to implement tax rules without political interference, as well as a lack of information sharing skills with other interested parties on tax matters. As a result, the study determined that the key issues encountered by revenue authorities were a shortage of labour and funding, corruption, political influence, and a lack of information exchange.

### **5.2.3 Measures which can be put in place to improve voluntary compliance.**

The study observed that, two-way contact between informal traders, groups that represent informal traders, and tax authorities will promote voluntary tax compliance. Consultations with informal merchants or their representatives before to creating legislation affecting them is critical since they become aware of the laws prior to implementation. Tax cuts for specific tax heads will also boost compliance in the informal economy. A few good tax heads may lead to tax compliance in the sense that traders may comprehend the tax heads, register under the appropriate tax head, and pay the appropriate tax liability.

Furthermore, the study discovered that government support for revenue collection operations carried out by ZIMRA will result in tax compliance, as will transparency in government expenditure and the provision of public goods and services to society. Furthermore, tax education via seminars, fliers, radio shows, and updated website material will help informal traders comprehend tax issues, perhaps increasing their desire to pay. Finally, the study discovered that information sharing between ZIMRA and other commercial and public organisations representing SMEs is critical since it results in consistent and uniform information being shared with the enterprises. As a result, the study suggests that communication between merchants, their representatives, and revenue authorities is critical, as is tax education, less good tax heads, government responsibility, and openness.

## **5.3 Recommendations**

Given the findings in this study the following recommendations were made to department of taxes (ZIMRA), Government and informal sector operators.

### **5.3.0 Recommendations to ZIMRA**

* The study recommends that the department of taxes provide ongoing tax education to informal traders through workshops, radio shows, roadshows, and brochures. This will increase informal traders' comprehension of tax problems, as well as their willingness to comply with tax legislation, because they understand their commitment and the reason for performing it.
* Improve communication between the government, the informal sector, and public and commercial entities that represent the informal sector. This can be accomplished by incorporating them in tax policy discussions prior to modifying or implementing new regulations affecting the informal sector.
* Implement efforts to control corruption in the tax system, such as teaching traders on how to report corruption offences and encourage them to report corruption to the appropriate authorities.
* Continuous staff training on issues of integrity, as well as the implementation of staff motivational approaches.
* Sharing information with stakeholders representing the informal sector or SMEs in order to ensure uniformity of information to informal traders; this can be accomplished by updating the website whenever there is a change in the tax system.

### **5.3.1 Recommendations to the government and policy makers**

* The research advises the government to cut tax heads through the ministry of finance. Fewer good tax heads with simple explanations may boost the trader's desire to pay taxes. Also, the presumptive tax system is being revised to account for variances in income that may be caused by differences in operating locations. For example, the tax liability for hairdressers working in the city core should differ from that of those working in high-density suburbs.
* Furthermore, the government is encouraged to provide financial assistance to ZIMRA in revenue collection projects, which might enhance awareness in the informal sector and hence tax compliance.
* Transparency and accountability in government spending, as well as the provision of public goods and services to society.

### **5.3.2 Recommendations to the informal sector**

* The study observed that, informal sector traders should register with the tax authorities, declare and pay the right amounts of tax liability. Also, must operate in defined zones so that officials may easily regulate and monitor their operations. Registration with the authority will help to growth since they will be able to get financial aid from banks, the government, and tenders.
* In addition, informal traders who buy items for resale in other countries are encouraged to use authorised sites to declare and pay presumptive taxes to the authorities.
* The study also advises the informal sector to report and refrain from engaging in corrupt practises.

## **5.4 Areas of further study**

* The informal sector includes a wide range of activities, from roadside vendors to professional consulting. There is a need to conduct research on self-employed informal merchants who work as architects, engineers, health practitioners, and real estate brokers.
* A qualitative study should be carried focusing much on the experiences of the informal sector in the hands of ZIMRA officials.

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**APPENDICES**

**APPENDIX I QUESTIONNAIRE**

Bindura University of Science Education

P Bag 1020

Bindura

Dear Respondent

I am an undergraduate student at Bindura University of Science Education and I am carrying out a study titled **TAX COMPLIANCE AND INFORMAL SECTOR.CASE OF GLENVIEW, HARARE.** You are kindly asked to complete the following questionnaire. The researcher is aware of the importance of confidentiality and therefore guarantees that the information that you will provide will be used for academic purposes only. Do not disclose your identity in any way.

For any queries, please contact the researcher on **0772 986 729**

**INSTRUCTIONS**

* Fill in with ink
* Do not disclose your identity on any page of the questionnaire
* Please tick where applicable

**Questionnaire: Informal sector** Informal sector questionnaire

What are you trading in?

Carpentry Metal fabrication Hairdressing Food vending

For how long have you been trading?

Less than 5 years 5-7 years 8-10 years over 10 years

Business registration status

Registered Not registered

If registered with ZIMRA, which tax heard (s) are you registered for?

Income tax PAYE Presumptive tax

Are you paying any tax to the authorities?

Yes No

If No, Why? If Yes, are do you declare actual income and expenditures

……………… ………………………..

Does paying taxes affect your income?

Yes No

What is (are) the challenges your firm face in meeting their tax obligations

………………………………

What do you think are the reasons why informal traders and small business are not paying taxes?

…………………………

Does the nature of tax system (complex or simple) affect tax compliance?

Strongly disagree disagree uncertain agree strongly agree

Does how the government use tax revenue affects your willingness to pay?

Strongly disagree disagree uncertain agree strongly agree

Does government tax policy changes affects tax compliance?

Strongly disagree disagree uncertain agree strongly agree

In your opinion what should the government go to improve tax compliance?

…………………………..

**Revenue officer questionnaire**

For how long have you been employed by ZIMRA

Less than 5 years 5-10 years More than 10 years

Which section are you working from?

……………..

What are the major causes of low compliance levels in informal sector in Zimbabwe?

……………………….

Are there any measures in place to encourage tax compliance?

…………………………….

Are they measures effective?

……………………………

What are the major challenges faced by the authority in trying to collect revenue from the informal sector?

………………………….

What are the measures which can be put in place to improve voluntary compliance in the informal sector?

……………………….

**Interview guide: Tax consultancy firms**

1. Personal information that is name of the interviewee, academic qualifications and name of the company he (she) is working for.
2. Tenure of service in that particular company and also as a tax consultant
3. What type of services offered and also their fares?
4. In your opinion what are the major contributors to the expansion of informal sector?
5. Are informal sector traders compliant to tax regulations?
6. How often do you work with SMEs and what is your experience working with them?
7. In your opinion what are the reasons behind informal sector non-compliance?
8. What can be done to encourage voluntary compliance in the informal sector?

**APPENDIX II REQUEST FOR PERMISSION**

Bindura University of Science Education

P Bag 1020

Bindura

Office of Administration

ZIMRA Head Office

P O Box 4360

Harare

31 July 2017

**RE: REQUEST FOR PERMISSION TO CARRYOUT A RESEARCH**

**Dear sir/ madam**

I am an undergraduate student at Bindura University of Science Education studying towards a Bachelor of Accountancy Honors Degree. I am conducting a research project on **TAX COMPLIANCE AND INFORMAL SECTOR: CASE OF GLENVIEW, HARARE** and I hereby appeal for permission to carry out research on your organization. The researcher is aware of the importance of confidentiality of internal information, therefore the information you provide is purely for academic purposes only and it will be treated as highly confidential.

I hope my request will be considered.

Yours faithfully

B192127B