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**EFFECT OF TAXATION ON THE PERFORMANCE OF SELECTED SMALL AND  
MEDIUM-SCALE ENTERPRISES**

**CASE STUDY: NAKAWA DIVISION.**

A dissertation presented to

**FACULTY OF AGRICULTURE**

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*Making a Difference*

**UGANDA MARTYRS UNIVERSITY**

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**Master's Dissertation**

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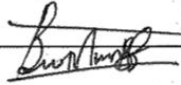
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## **DEDICATION**

I dedicate this dissertation to my family whose unwavering support and encouragement has been my anchor in this journey. To my parents who taught me to value education and to work hard. Your love and belief in me have been my greatest inspiration to push on.

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### **List Of Abbreviations**

SMEs.	- Small and Medium enterprises
URA	- Uganda Revenue Authority
VAT	- Value added Tax
GDP	- Gross Domestic Product
SPSS	- Statistical Package for Social Sciences
CVI	- Content Validity Index

## **Abstract**

This study examined the effect of Taxation on the Performance of Selected Small and Medium Scale Enterprises in Nakawa Division, Kampala District, with the aim of generating evidence to inform tax policy design and compliance strategies. Specifically, the study was guided by four objectives: (1) to assess the level of SME taxpayers' knowledge of taxation; (2) to evaluate the effect of tax rates on SME performance; (3) to determine the influence of tax incentives on SME growth; and (4) to assess the relationship between tax filing requirements and SME performance. A cross-sectional design was employed, integrating both qualitative and quantitative approaches to enable triangulation of findings. The study sampled 278 SMEs using a combination of simple random and purposive sampling techniques. Data were collected through structured questionnaires and in-depth interviews, and analyzed using SPSS Version 27, applying both descriptive statistics and Pearson correlation analysis. Findings indicated that while SMEs demonstrated moderate awareness of taxation, significant knowledge gaps persisted, particularly regarding tax obligations and incentive access. A statistically significant positive relationship was found between tax incentives and SME performance ( $r = 0.375$ ,  $p < 0.001$ ), and tax rates also showed a notable influence. Overall, the study revealed a moderate to strong correlation between key elements of taxation and the performance of SMEs, suggesting that effective tax policies and improved taxpayer education can positively impact SME growth and sustainability. The study recommends that the Uganda Revenue Authority (URA), in collaboration with the Ministry of Finance, scale up tax education campaigns targeting SMEs and implement a tiered tax incentive structure based on enterprise growth stages. These interventions are essential to enhance compliance, reduce business constraints, and promote long-term economic development within Uganda's SME sector.

## **CHAPTER ONE: INTRODUCTION AND BACKGROUND**

### **1.1 Introduction**

Small enterprises are defined by Ntirandekura & Mushamba (2022) as an enterprise employing between 5 and 50 people with an annual revenue turnover not exceeding 360 million Uganda shillings while a medium enterprise is an enterprise that employees more than 50 people with an annual revenue turn over of between 360 million Uganda shillings and 30 billion Uganda shillings (Irumba et al., 2023). Taxation refers to the act of imposing taxes on people, entities, properties and businesses (Gorton, 2024). These SMEs are instrumental in shaping the landscape of emerging markets. Their ability to innovate, generate employment and contribute to regional development makes them indispensable (Liberto, 2023). However, despite their role in economic development, SMEs in Nakawa Division often face numerous challenges, one of which is navigating through complex tax policies set by governments (Manzoor, Wei & Sahito, 2021). This study aimed to investigate the effect of government tax policies on the performance of SMEs, aiming to provide insights that can inform policy decisions and support the growth of these enterprises.

### **1.2 Background**

#### **1.2.1 Historical background**

The history of taxation dates to ancient civilizations like Egypt, Rome and the Greeks whereby they used rudimentary forms of taxation on economic activities. The ancient Greeks and the Roman Empire relied on taxes to finance military activities and public works projects. These taxes were collected in the form of money, goods and services. During the Middle Ages, feudal lords primarily collected taxes, and they served the purpose of financing the maintenance of castles, roads and other infrastructure (Kancelaria & Bernard, 2023).

In East Africa, taxation dates to the British colonial administrators who introduced the structure of compulsory public works such as road construction, the building of administrative headquarters and schools, forest clearance and other similar works (URA, 2023). Income tax was introduced in 1940 by a Protectorate ordinance. It was mainly payable by the Europeans and Asians but was later extended to Africans. In 1952, the ordinances were replaced by the East African Income Tax

Management Act, which laid down the basic legal provisions found in the current income tax law. The East African Income Tax Management Act of 1952 was repealed and replaced by the East African Income Tax Management Act of 1958 (URA, 2023).

In Uganda the first formal tax was called the hut tax which was introduced in 1900 and from this, Ugandans started paying duty as an indirect tax which involved imposition of an ad valorem import duty at a rate of 5% on all goods entering East Africa, through the port of Mombasa and destined for Uganda. Upon gaining independence, Uganda inherited the tax system from the colonialists and continued to apply them to generate revenue. In 1986, the government of president Yoweri Museveni implemented economic reforms which mostly aimed at liberalizing the economy and promoting private sector development. These tax reforms were mainly introduced to broaden the tax base, simplify tax administration, and enhance revenue collection. This included the adoption of a value-added tax (VAT) which replaced the old sales tax system (Lucy, 2023).

In recent years, Uganda has continued to implement tax reforms to support economic growth and development. This has included efforts to enhance tax compliance, expand the tax base, and improve revenue mobilization. Today, taxation of SMEs remains a critical aspect in Uganda's economic landscape, playing a pivotal role in revenue generation, economic development, and social welfare

### **1.2.1 Conceptual background**

SMEs play a critical role in the development of an economy therefore their performance is highly considered. In Uganda, SMEs play a critical role in job creation, innovation, and economic dynamism (Mugabo, 2019). However, the enabling environment, especially regarding taxation, gives rise to significant challenges. Understanding the impact of taxation on SME performance is essential for informing policy formulation to enhance business growth (Tasha et al., 2023.).

Taxation as the independent variable in this study encompasses tax incentives, tax rates and overall tax burden on SMEs. Tax Incentive means any exemption from taxation, tax holiday, reduction in tax rate or similar tax relief, including any state research tax credits. Tax incentives enhance business performance by freeing up resources for investment and expansion (Mayende, 2013). High tax rates burden SMEs, reducing their profitability and operational efficiency. The dependent

variable performance of SMEs is measured through various metrics including profit margin, growth and survival rate. Profit margin is the proportion of revenue that remains as profit once all expenses are deducted. A high profit margin shows that the company is effective in managing its costs and generating sufficient revenue relative to its expenses (Maverick, 2023). An increase in profit margin suggests that the SME is successful in maintaining profitability, which is vital for sustainability and growth. Growth refers to the rise in the size or value of an SME over a specific period. This is a key indicator of SME's ability to expand its operations, attract new customers, and increase its market presence. Survival rate is the percentage of businesses that continue to operate over a specified period. Survival rate is a critical performance metric, as it indicates the ability of an SME to endure market challenges, economic fluctuations, and operational hurdles (Muhwezi & Niclous, 2023).

This research study sought to explore these relationships to offer critical insights for policymakers and business owners, offering evidence-based recommendations for tax reforms that support the growth and sustainability of SMEs in Nakawa Division.

### **1.2.3 Contextual background**

SMEs have emerged and now form the backbone of African economies through representing a diverse range of businesses operating with various sectors. These range from agriculture and manufacturing to services and technology contributing significantly to the GDP, employment, and poverty alleviation (Elumelu, 2024). According to recent studies, SMEs account for a substantial portion of employment opportunities, employing millions across the continent. SMEs account for approximately 80% of jobs in Africa and this making them a significant mechanism for socio-economic growth (African Union, 2022). The Sustainable Development Goals and the African Union acknowledges that Africa's drivers of economic growth and long-term sustainability for emerging markets are dependent on the potential of the effective development of the SME business model (African Union, 2022).

In Uganda, SMEs represent approximately 90% of private sector production making it significant in blossoming the economy. They are accredited for identifying and creating new markets and serving as the foundation for new companies that are emerging. This is consequently providing a

source of income for millions of Africans. Thus, they are an enabling factor in wealth creation by driving the demand for goods, services, investments, innovation, technology, and trade.

However, even though they have a positive influence towards the development of the economies of the Africa continent, SMEs are still facing challenges and obstacles that are affecting their long-term survival and contribution to the development of Africa especially those related to taxation policies and regulations. Ocheni (2015) notes that the system of taxation used in any country determines the performance of businesses whereby countries with auspicious and progressive tax rates have propagated successful businesses. Small and Medium Enterprises (SMEs) operating in emerging economies encounter distinct regulatory challenges compared to those in developed economies. Ibrahim & Muritala, (2015) also adds that taxes levied from individuals/ business organizations that are not proportionate to the income/wealth of the business can be a demotivating factor that forces businesspeople to transfer their capital to another sector. Moreover, regulatory frameworks in emerging economies are often characterized by greater complexity, inconsistency, and bureaucratic hurdles, which can pose significant barriers to SME growth and sustainability. These challenges include cumbersome administrative procedures, opaque regulatory processes, and a lack of transparency and accountability in regulatory enforcement.

This study therefore assessed how the performance of SMEs is influenced by the taxation policies and regulations in Nakawa division since majority of the SMEs are in the urban centers.

### **1.3 Problem statement**

In Uganda, companies are subject to multiple taxes such as stamp duty, excise duty, value-added tax, and corporation tax. Although most business owners are aware of their tax obligations, many remain uncertain about the methods of tax assessment, and little structured support is provided in terms of tax awareness and education (Tasha et al., 2023). This knowledge gap leaves SME owners ill-informed about applicable tax rates, incentives, and compliance requirements, which undermines both growth and sustainability. As Iremba (2023) notes, the absence of adequate tax knowledge, combined with perceptions of high tax rates, has positioned taxation as a significant barrier to SME performance in Uganda. Even where tax incentives exist, they are often inaccessible or insufficient to ease the burden on SMEs, thereby exacerbating compliance challenges.

Despite deliberate government efforts to promote SME growth, taxation factors remain a critical obstacle. According to Turyatamba et al. (2022), taxation continues to hinder the competitiveness and survival of many SMEs, while Ronald et al. (2023) emphasizes that SMEs contribute nearly 90% of private sector production in Uganda, underscoring their vital role in employment and economic development. If taxation-related barriers are not addressed, the underperformance of SMEs will not only limit entrepreneurial growth but also slow Uganda's broader economic transformation agenda. Against this backdrop, this study seeks to examine the effect of taxation on the performance of selected SMEs in Nakawa Division, providing evidence to inform both policy reforms and practical interventions to enhance SME growth and sustainability.

## **1.4 Study objective**

### **1.4.1 General objective**

To analyze the effect of Taxation on the Performance of Selected Small and Medium Scale Enterprises in Nakawa Division

### **1.4.2 Specific Objectives**

1. To examine the knowledge of taxpayers regarding taxation in selected SMEs in Nakawa Division.
2. To assess the effect of tax rates on the performance of selected SMEs in Nakawa Division.
3. To determine the effect of tax incentives on the performance of selected SMEs in Nakawa Division.
4. To assess the effect of taxation and the performance of selected SMEs in Nakawa Division.

## **1.5 Research questions**

1. What is the level of Knowledge of taxpayers regarding taxation in selected SMEs in Nakawa Division?
2. How do tax rates affect the performance of selected SMEs in Nakawa Division?
3. What is the effect of tax incentives on the performance of SMEs?
4. What is the effect of taxation on the performance of selected SMEs in Nakawa Division?

## **1.6 Significance of the study**

This study on the Effect of Taxation on the Performance of Selected Small and Medium Scale Enterprises valuable insights into the relationship between tax rates, tax incentives, tax burden and SMEs, which are very vital drivers of growth and development in an economy. Through examining how taxation impact SMEs, this study can inform tax authorities like URA, policy makers, and business owners about the effectiveness of existing tax frameworks and bring to light areas for improvement. Furthermore, this study will shed light on the challenges, opportunities and contributions of SME to the economy within the taxation landscape. The study may also help in the formulation of targeted and supportive tax policies that will help SMEs to thrive and grow, thereby leading to economic prosperity.

## **1.7 Justification of the study**

The justification for this study stems from the critical role of SMEs in Uganda's economic transformation. SMEs account for the majority of business establishments and provide significant employment opportunities, making them central to private sector growth and national development. Despite this importance, SMEs continue to face taxation-related challenges, including limited knowledge of tax obligations, complex and often unclear tax rates, and difficulties in adopting digital tax systems. These challenges reduce compliance levels, constrain financial resources, and limit the potential for innovation and expansion, thereby weakening the contribution of SMEs to Uganda's Vision 2040 and the National Development Plan IV.

Focusing on SMEs in Nakawa Division is particularly important because the area has one of the highest concentrations of SMEs in Kampala, serving as a hub for trade, services, and manufacturing. Yet, many of these enterprises remain vulnerable to the pressures of taxation. By examining how knowledge of taxation and tax rates affect SME performance, this study will generate evidence to support both policy and practice. The findings are expected to guide policymakers and the Uganda Revenue Authority (URA) in designing SME-friendly tax policies and compliance frameworks, while also empowering SME owners with knowledge to improve compliance, optimize financial management, and strengthen business sustainability.

## **1.8 Scope of the study**

### **1.8.1 Geographical scope**

This study focused on Nakawa Division in Kampala District. The Division was purposively selected because it hosts one of the largest concentrations of SMEs in Uganda, operating across diverse sectors such as trade, manufacturing, services, and agro-processing. These enterprises contribute significantly to employment, household income, and local revenue mobilization in Kampala.

Nakawa is also strategically important because it falls within the jurisdiction of the Uganda Revenue Authority (URA) Nakawa Domestic Taxes Office, which is one of the most active tax administration centers in the country. This proximity facilitates direct engagement between SMEs and URA in areas such as tax registration, filing, compliance monitoring, and enforcement. As such, SMEs in Nakawa experience first-hand the opportunities and constraints associated with taxation policies and practices, making the Division a representative case for understanding the effects of taxation on urban SMEs in Uganda.

By situating the study in Nakawa, findings are expected to generate insights that not only inform SME support strategies but also contribute to policy recommendations for URA and other tax administrators, particularly in improving compliance frameworks and balancing revenue mobilization with SME growth.

### **1.8.2 Content scope**

The study focused on assessing the effect of taxation on the performance of selected SMEs. It assesses the effect of tax incentives and tax rates on the performance of SMRs as well as the overall tax burden on SMEs. The study employed both qualitative and quantitative analyses, using data from business reports, academic literature, industry surveys, and expert interviews. Performance was measured through indicators such as profitability, sales growth, customer base expansion, and business survival rates.

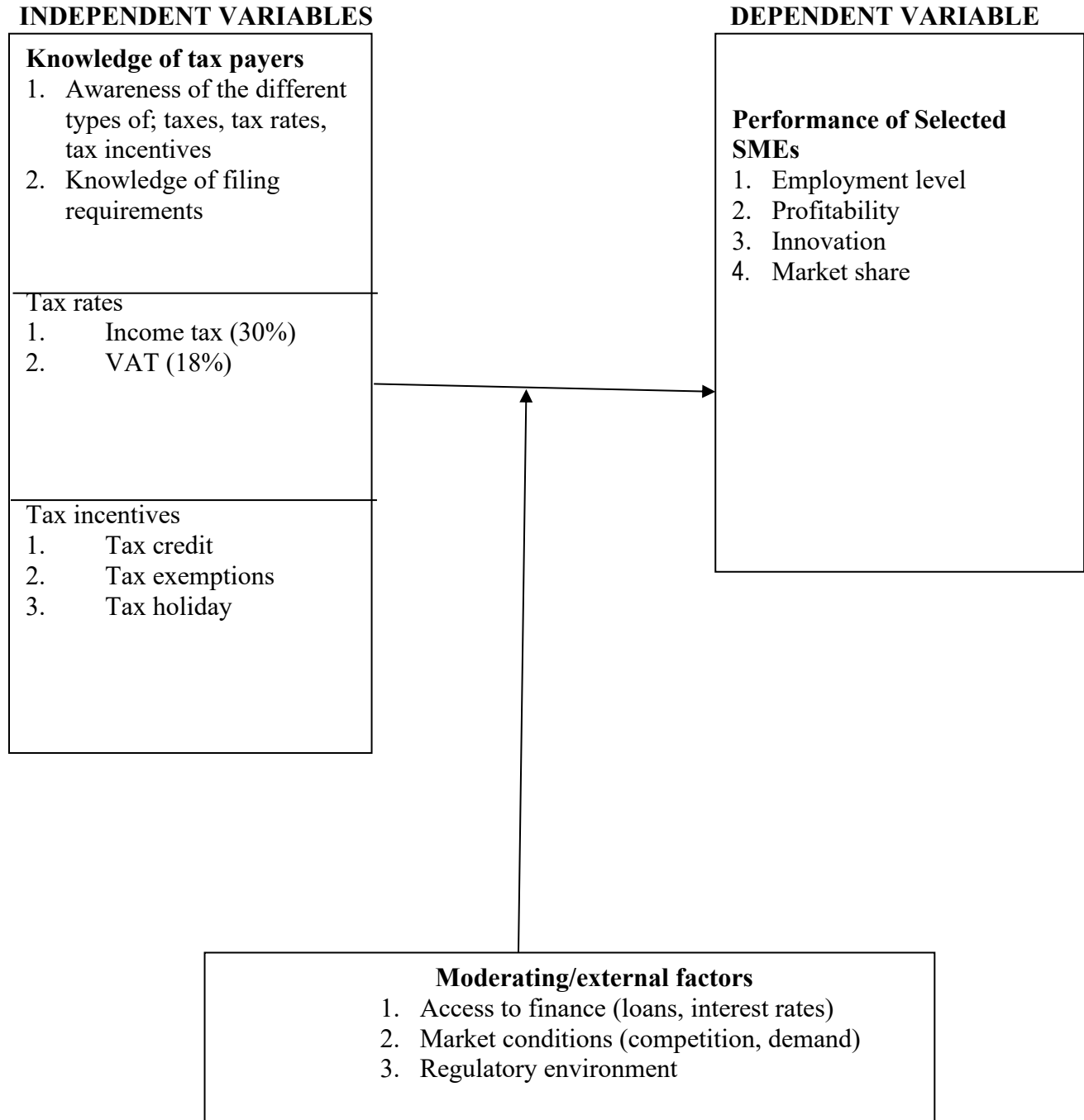
### **1.8.3 Time scope**

This study covered the period from July 2024 to February 2025. This scope was deliberately chosen to align with Uganda's financial year cycle (July–June), which is critical for analyzing the effect of taxation on SME performance. The period enabled to capture a full tax year, including the processes of tax assessment, filing compliance, and enforcement by the Uganda Revenue Authority (URA).

The study also incorporated post-year reflections and reporting, ensuring that data collection included not only SME operational and financial records but also perspectives from regulators and industry stakeholders. This approach provided a comprehensive understanding of taxation trends and their implications for SMEs during the study period.

## 1.9 Conceptual framework

The conceptual framework in figure 1 below shows the interplay between taxation factors and their effect on performance of selected SMEs as well as the moderating or external factors affecting the performance of SMEs.



**Source: Adopted with modification from Daniel & Faustine (2019)**

**Figure 1: Conceptual framework for the study on Effect of taxation on the performance of selected SMEs in Nakawa Division**

### **1.9.1 Narrative of the conceptual framework.**

The above conceptual framework examines the influence of taxation on the success of Small and Medium Enterprises. It shows how knowledge of taxpayers, tax rates and tax incentives affect the performance of SMEs as measured by profitability, employment level and innovation. It asserts that a substantial level of tax knowledge among SME owners can enhance their capacity to effectively leverage tax incentives which can lead to reduced tax burdens thus boosting profitability. Higher tax rates can strain financial resources and as a result hinders employment growth and overall performance. The link between taxation and success of SMEs is moderated by external aspects such as access to finance, market conditions and the regulatory environment. Easy access to finance at lower interest rates can help mitigate the impact of high tax rates and improve their competitive edge in the demanding market. Also, a favorable regulatory environment can simplify compliance and enable SMEs to capitalize on tax incentives more effectively leading to better employments rates, higher profitability and better innovation.

### **1.9 Operational definitions**

**Taxation:** This is the process of imposing taxes on people, entities, properties and business (Cox, Neumark and McLure, 2025)

**Tax:** This is a mandatory financial charge or some other type of levy imposed upon a taxpayer (an individual or other legal entity) by a governmental organization in order to fund various public expenditures (Boqiang & Zhijie, 2019).

**Policy:** Policy is a law, regulation, procedure, administrative action, incentive, or voluntary practice of governments and other institutions (CDC, 2024).

**Regulation:** This refers to a rule or directive made and maintained by an authority (Merriam-Webster, 2025).

**Small and Medium enterprise:** This is an enterprise employing between 5 and 50 people, with an annual sales/revenue turnover total asset of up to Uganda Shillings (USH.) 360 million

**Business performance:** company's ability to profit from its resources and achieve its objectives

## **CHAPTER TWO: LITERATURE REVIEW**

### **2.1 Theoretical review**

A theoretical framework is a foundational review of existing theories that serves as a roadmap for developing the arguments you will use in your own work (Vinz, 2022). This framework provides a structured basis for understanding, analyzing and interpreting taxation. This framework helps one understand the underlying principles and assumptions. Taxation has various theories that different authors have come up with and have been used for ages. These theories help us understand taxation better and what the authors discuss about each.

This study was based on two theories that is ability to pay theory and benefit theory

#### **2.1.1 The ability to pay theory**

The ability to pay theory was espoused in 1776 by Adam Smith who is regarded as the father of economics. Smith argued that individuals in each state should contribute to government support according to their ability, which is proportional to the income they derive from the state's protection (Kagan, 2024). Ability to pay, the dominant theory of taxation, is usually interpreted in terms of sacrifice. It is held to justify progressive taxation under any one of three possible interpretations of sacrifice: the equal, equal-proportional, and least-sacrifice theories (Kendrick, 1939).

The Ability to Pay Theory advocates proportionate taxation based on financial capability, with those possessing greater resources shouldering a heavier tax burden (Seriah, 2024). According to this theory, the income level of an individual determines the ability-to-pay. Those with lower income are apportioned to lower tax rates, while higher-income earners are presumed to have more disposable income. Therefore, they will not suffer as much as a tax burden (Eliza & Tina, 2023). This theory does not take into consideration the amount of these services that taxpayers use. For instance, all taxpayers contribute to public schools, even if they do not have any children in the school system (Eliza & Tina, 2023).

The ability to pay theory rests on several assumptions which include the declining marginal utility of money with an increase in its supply, the existence of sacrifice (Kendrick, 1939).

Proponents of ability-to-pay taxation contend that individuals who have gained the most from the nation's way of life, through higher incomes and greater wealth, have the means to contribute more and should be expected to support the system further (Kagan, 2024). On the other hand, those who oppose this theory argue that it is inherently unfair. They believe it penalizes hard work and achievement while diminishing the motivation to earn more. Many believe that a uniform income tax rate, commonly referred to as a flat tax, would create a fairer system (Kagan, 2024).

A significant benefit of the ability-to-pay taxation model is that it enables the government to pool more revenues to fund its services. More revenue collection is made possible whereby people with more income contribute more taxes to fund services needed by all (Eliza & Tina, 2023).

The ability to pay theory was relevant to the study because it justifies equity as a principle of taxation and can also be applicable to SMEs to improve performance. SMEs sacrifice a portion of their income to the government, which is then used to fund public services. The sacrifice is measured both in terms of the burden that SMEs bears on sacrificing their income to the public but also the ease with which they got that income (Jepkosgei, 2014)

### **2.1.2 Benefit theory**

The benefits-received principle of taxation refers to a theory of income tax fairness whereby citizens who use or benefit from certain government goods and services pay taxes for them in equal measure (Greta & Kaitlin, 2023). The benefit approach was originally formulated by two economists of the Stockholm School, Knut Wicksell (1896) and Erik Lindahl (1919). The approach was further developed in the work of Paul Samuelson, Richard Musgrave and others (Richard, 1959). It has also been applied to such subjects as tax progressivity, corporation taxes, and taxes on property or wealth (Richard & Peggy, 1973). Historically, the Benefits Principle derived from the concept that taxpayers are consumers of government services, just like they are consumers of goods and services from businesses.

The benefit Principle is a theory proposing that people must be taxed in accordance with the level of benefits they use or receive from public expenditure. According to the Benefits-received principles, those who benefit more from government services, infrastructure, and public goods ought to bear a greater portion of the tax burden.

Lindsay (2019) notes that Benefits taxation has several advantages. As an ethical claim, it appeals to intuitive principles of fair cooperation. As a rule of procedural justice, it tends to protect against oppressive tax schemes. The Benefit Theory also increases the perception of fairness in tax distribution, which enhances the likelihood of compliance and reduction in tax evasion (Belahouaoui & Attak, 2023). Although benefits theory has the resources to respond to some of the most historically influential criticisms, it faces additional challenges. These include specifying a yardstick for gauging benefits and fair treatment of taxpayers who take a public-spirited view of government spending as opposed to those who are mainly concerned with their private advantages. It also has a challenge of difficulty in quantifying usage and benefit of public goods and services; potential for over-taxing citizens if not carefully applied (Lindsay, 2019).

However, the Benefit Theory has some limitations in its practical implementation has got some limitations. Measuring benefits is challenging since it is difficult to quantify the benefits received from public goods. Moreover, public goods are accessible to all citizens irrespective of their contribution, meaning they are non-excludable. This makes it challenging to link specific benefits to specific payments (Greta & Kaitlin, 2023).

## **2.2 Taxation of SMEs in Uganda**

According to Uganda Revenue Authority (URA), a small business is one that makes total sales between Ugx 10,000,000 and 150,000,000 in a year. This business should at least make sales of Ugx 27,500 in a day (URA, 2023). The largest domestic revenue sources are VAT and excise duty (22 percent), pay-as-you-earn income tax (Paye) (18 percent) and corporate income tax (8 percent).

### **2.2.1 Tax rates**

Tax rates for small enterprises with less than total sales of 150,000,000 per year are subjected to the taxes as shown in Table 1 below.

Table 1: Tax rates for small businesses in Uganda

Total sales in a year	Tax payable	
	With records	Without records
Total sales do not exceed Ugx 10 million	Nil	Nil
Total sales more than Ugx 10 million but less than Ugx 30 million	0.4% of annual total sales more than 10 million	Ugx 80,000
Total sales more than Ugx 30 million but does not more than Ugx 50 million	Ugx 80,000 plus 0.5% of the total sales more than Ugx 30 million	Ugx 200,000
Total sales more than Ugx 50 million but not more than Ugx 80 million	Ugx 180,000 plus 0.6% of the annual total sales more than 50 million	Ugx 400,000
Total sales more than Ugx 80 million but not more than Ugx 150 million	Ugx 360,000 plus 0.7% of the annual total sales more than 80 million	Ugx 900,000

*Source: URA (2023).*

For Value Added Tax (VAT), The standard VAT rate is 18%. SMEs with an annual turnover of UGX 150 million or more must register for VAT and comply with VAT regulations. SMEs with a turnover below UGX 150 million are not required to register for VAT, simplifying their tax compliance.

### 2.2.2 Tax incentives

Tax incentives are exemptions or reductions provided to individuals or companies to mitigate the effects of taxation with the aim of fostering savings and investments. In an effort to boost SME growth, several countries have implemented tax incentives aimed at both investors and listed firms

to encourage activity on SME stock exchanges. Offering tax benefits to investors is the more prevalent strategy, especially in developed economies (Daniel & Faustin, 2019). Findings by Kamara (2024) identified investment tax allowances as the highest contributing factor of tax incentives aimed at supporting growth of SMEs and tax holidays ranked the second contributing factor of tax incentives to growth of SMEs. In Uganda, there are various tax incentives available for businesses and these include; tax holidays, tax exemptions, tax allowances, tax credit.

Tax holidays are a kind of fiscal incentive whereby businesses are granted temporary exemptions from paying certain taxes for a specified period. Tax holidays are a temporary reduction or elimination of tax liability for qualifying taxpayers, while accelerated depreciation allows firms to depreciate the costs of certain new investments faster and thereby reduce their overall tax liability (UNU-WIDER, 2024). The sole purpose of tax holidays is to attract both domestic and foreign investment by reducing initial tax burdens. Tax holidays in Uganda offer four types of special 10-year tax exemptions. These exemptions apply to firms exporting over 80% of their production, firms operating within industrial parks, and those in special economic zones (UNU-WIDER, 2024). A one-year tax holiday that might be prolonged is granted for firms that start new agro-processing operations (URA, 2023).

Tax exemptions refer to specific incomes or transactions that are exempt from taxation. This reduces the taxable income or amount, effectively lowering the tax liability. In Uganda there are various numbers of tax exemptions which includes income tax exemption for Collective Investment Schemes

Tax allowances are specific amounts that can be excluded from a taxpayer's total income to minimize the taxable base. These are usually standard amounts set by tax authorities (Kagan, 2024).

Tax credits are amounts that can be subtracted directly from the tax owed, rather than from taxable income. These are often designed to encourage specific activities or to provide relief for taxpayers. Resident taxpayers are eligible for a credit against foreign income taxes paid on income earned from foreign sources that is included in their gross income. The foreign tax credit granted depends on the prevailing income tax rate (i.e. 30%) in Uganda (URA, 2024).

## **2.3 Key Performance indicators for SMEs**

Performance of SMEs is very vital to the economic landscape of Uganda. Key performance indicators (KPIs) are the vehicle for long-term success for small- and medium-sized businesses. KPIs are a collection of quantifiable measurements that a business uses to evaluate or compare performance as it relates to operational and strategic goals. KPIs provide a foolproof management system (Serdar, 2019).

Performance can be understood in two perspectives, that is the quantitative perspective and qualitative perspective. In the quantitative perspective, performance measured, operational efficiency, financial performance, production output, total customer base, market position, profit margins, costs and liquidity among others (Zimon, 2018). On the other hand, the qualitative perspective as indicated by Annet et al (2023) includes goal attainment, leadership methodology, employee conduct, customer satisfaction, product and process innovation, organizational and marketing innovation. Balunywa (2017) & Faridah et al. (2023) in their work, evaluated a set of 14 performance indicators including reputation, productivity, employee contentment, profitability, sales figures, timely order processing, adequate working capital, operational effectiveness and product quality. In addition, other indicators included success in meeting targets, number of customers, supervisory ease, reduction in manufacturing cost and product diversification.

## **2.4 Empirical review**

### ***2.4.1 Knowledge of taxpayers regarding taxation***

Taxpayer knowledge refers to a person's understanding that helps them follow their rights and duties according to tax laws (Chandra et al., 2021). Cahyadi & Jati (2016) also defined tax knowledge as the taxpayer's understanding of tax rules, including tax rates and the advantages of complying with tax payments (Chandra et al., 2021) quoting Marjan (2014) indicated that there are different types of tax awareness that motivate people to pay taxes, with three main forms being the most important Firstly, recognizing that taxes play a role in supporting societal growth can encourage taxpayers to comply, especially when they feel that tax collection is fair and they are not being treated unfairly. They acknowledge that taxes are allocated to foster economic growth, and they can also help strengthen the state's economy. Taxpayers are more likely to pay taxes when

they understand that delays or avoiding taxes can lead to a shortage of financial resources, which may slow down the country's development. Secondly, it's important to recognize that taxes are set by law and must be followed. Taxpayers are more likely to meet their tax responsibilities when they understand that paying taxes is legally required and considered a civic duty (Chandra et al, 2021). Knowledge refers to the information taxpayers gain to help them understand taxation. Those who lack this knowledge are more likely to ignore tax rules or commit fraud (Chandra et al., 2021).

The education level received by taxpayers is a critical factor that contributes to the understanding of tax requirements, especially regarding registration and filing requirements. Earlier research has indicated that general tax knowledge has a very close relationship with taxpayers' ability to understand the laws and regulations of taxation, and their ability to comply with them (Chandra et al., 2021). Taxpayers often do not know what they should pay in taxes, given a complex and uncertain tax system. As a result, they have increasingly come to rely upon paid tax practitioners (and tax preparation software) in the preparation of their taxes (Musimenta, 2020). Alm (2018) found out that taxpayers vary considerably in their knowledge of tax requirements, their capacity to learn about their responsibilities, their perceptions of the consequences of not meeting those responsibilities and their awareness of any services to assist them with their taxes.

A study by Irumba (2023) revealed that most business owners within the SME sector cannot understand the Ugandan tax system. In other words, they cannot interpret what the various tax laws stipulate and the other tax compliance requirements (Mark et al., 2023). Faridah et al (2023) in their study found that when it comes to paying taxes, most business owners need assistance to understand how much to pay when to pay according to the size and capital of their businesses. Additionally in the study by Irumba (2023), it was found that most SMEs can interpret tax laws and compute tax liabilities. This shows that most of them do not have sufficient tax knowledge regarding when to pay taxes and in what proportions.

Studies in Uganda show that while most SMEs are aware of income tax obligations, their understanding of indirect taxes such as Value Added Tax (VAT), excise duties, and withholding tax remains very limited. Many SMEs fail to register for VAT even when they surpass the statutory threshold of UGX 150 million annual turnover, largely because of a lack of awareness of the requirement or misconceptions that VAT is only applicable to larger corporations (Naggayi &

Sekisws, 2024). The complexity of VAT procedures—including filing returns, distinguishing between exempt, zero-rated, and standard-rated supplies, and calculating input versus output tax—further discourages compliance. This lack of knowledge often results in inaccurate reporting and late filings, which expose SMEs to penalties and interest charges from the Uganda Revenue Authority (URA) (Amondong & Kalimu, 2024). The problem is compounded by low levels of tax education, with most sensitization programs focusing on income tax rather than indirect taxes (IDS, 2025).

Moreover, SMEs display limited awareness of excise duties and withholding tax, which often apply in contractual transactions. For instance, business owners frequently fail to withhold tax when required or do not claim withheld tax as a credit, thereby increasing their effective tax burden unnecessarily (Irumba, Kabanda & Matovu, 2025). This gap is worsened by inadequate bookkeeping and the absence of trained accounting personnel in most SMEs, leading to reliance on informal financial practices that are insufficient for proper VAT and excise duty compliance (Grefalde, 2020). Beyond exposing SMEs to sanctions, this limited knowledge also denies them potential benefits, such as input tax credits that could ease cash flow constraints. In the long run, poor understanding of indirect taxes undermines SMEs' ability to integrate into formal supply chains, constraining both their growth and competitiveness in Uganda's economy (Shema, Babirye & Kabanda, 2024).

Furthermore, the adoption of digital tax systems in Uganda such as e-tax portals, Electronic Fiscal Receipting and Invoicing System (EFRIS), and integrated digital platforms has enhanced the accessibility and efficiency of tax administration. These digital tools have reduced reliance on paper-based processes and enabled online filing, payment, and real-time transaction tracking, which contribute to greater transparency and administrative efficiency. Studies suggest these initiatives hold promise for improving SME compliance and reducing overall tax compliance costs.

However, many SME owners continue to face significant barriers due to low digital literacy, weak infrastructure, and unreliable internet connectivity. A case study of Kira Division revealed that taxpayers experienced difficulties using the e-taxation system because of internet outages, confusing web portal interfaces, and a lack of historical tax record access; these challenges, as well as concerns about data security, have negatively impacted adoption rates (Benah, Muhammad &

Nancy, 2025). On a broader scale, national data highlight that digital literacy remains limited as 97% of Ugandans had not used a computing device in the previous three months, and only 1.3% owned a personal computer with the main obstacles cited were lack of knowledge, skill, and affordability (NITA-U, 2022). These structural deficiencies mean that, despite digital platforms being available, many SMEs remain unable to use them effectively, which hinders voluntary compliance and limits the potential benefits of tax digitalization.

In conclusion, the knowledge of SMEs on taxation in Uganda remains limited, especially in areas such as VAT, excise duties, withholding tax, and available tax incentives. While most owners understand basic income tax obligations, gaps in interpreting complex tax laws, recordkeeping, and filing requirements often expose them to errors, penalties, and missed opportunities for relief. The adoption of digital tax systems like e-filing and EFRIS offers potential benefits, but low digital literacy and weak infrastructure hinder effective use. Without targeted taxpayer education and support, many SMEs remain only partially compliant or outside the tax net altogether, which constrains both their growth and Uganda's revenue mobilization. Strengthening awareness and building SME capacity in taxation is therefore essential for improving compliance and fostering sustainable economic development.

#### **2.4.2 Tax rates and the performance of SMEs**

Various studies have shown that tax rates are a hindrance and a barrier to the performance of SMEs (Irumba, 2023; Ahumuza, Arinaitwe and Agaba, 2023).

Irumba (2023) found that for most SME owners, tax rates lack clarity regarding payable taxes. This means that respondents in the SME world are unaware of the amount to remit to the tax authorities. Additionally, the tax rates place a heavy burden on SMEs.

SMEs report that the taxes are burdensome to their businesses which affects their operations. Winny et al (2023) indicated that taxes charged are burdensome to most businesses therefore inhibiting the growth and expansion of these enterprises in Uganda. Results from Irumba (2023) had similar findings as most of the respondents concurred that indeed taxes were burdensome to their businesses meaning that the taxes levied from the SMEs are inhibiting to the growth and performance of these enterprises in Uganda. The study revealed that the taxes were high, and this

imposes high costs on their businesses yet most of them are struggling to keep operating. During an interview from a study by Irumba (2023), one of the respondents said, "VAT is 18% addition to the price being paid; this means that if one has to pay all VAT without having considered deductions, this trader will be selling expensive goods and sooner than later it will be out of business". (Irumba, 2023).

Multiple taxation also serves as a barrier to the success of SMEs. For instance, retail shops are obligated to remit income tax to URA, import duty tax whenever they import small merchandise in association with fellow traders, in addition to this KCC requests them to pay for license fees. This makes taxes not only to be an impediment to the success of SMEs in Uganda but have by driving up operational costs through taxes, which in turn has dampened their performance (Irumba, 2023).

According to Bolboros (2016), tax rates play a critical role in shaping economic financial performance and regulating money flows, with progressive tax rates leading to higher income tax collections.

Exorbitant tax rates reduce the capital base of SMEs which inhibit their growth and overall performance. Irumba (2023) indicated that the regressive nature of taxes on SMEs reduces their revenue base. Additionally, most of the respondents stated that the tax rates charged are not fair and not economical to SMEs meaning that the taxes levied from SMEs are reducing the capital base of these enterprises and thus hindering their performance.

Tax rates affect SME performance by influencing profitability, as the impact of corporate income tax rates is absorbed by business owners through reduced profits, by employees via lower wages, or by customers through higher prices. A significant tax rate has a significantly negative effect on both the pre-tax and post-tax rates of profit. On the other hand, lower tax rates reduce compliance and administrative costs which improves profitability and increases money available for investment thus improving their overall performance (Ahumuza & Arinaitwe, 2023). Simplified tax regimes also encourage the formalization of informal businesses, boosting economic activity and growth. Excessive tax rates discourage SMEs from formalizing their businesses as they try to avoid taxes that are burdensome with elevated compliance costs (Amos et al., 2024). SMEs in

countries with reduced corporate tax rates and fewer administrative tax burdens tend to exhibit higher growth rates and better performance metrics. Simplified tax systems lead to better compliance and more resources for growth (OECD, 2022). Irumba (2023) noted that there are various types of taxes applied to small and medium enterprises, and the specific taxes paid depend on the type and size of the business.

### **2.4.3 Tax incentives and the performance of SMEs**

A study by Ahumuza et al., (2023) found that tax incentives, investments and performance of SMEs are closely linked. Countries that offer tax relief to SMEs argue that preferential tax treatment generates significant employment opportunities and promotes entrepreneurship, which is linked to flexibility, speed, risk-taking, and innovation (Daniel & Faustin, 2019).

Tax incentives attract private investors to the SME sector. Ahumuza et al., (2023) in their study, most SMEs reported that having tax incentives increases investment in businesses and thus improves the performance of SMEs. Holding tax as a tax incentive for businesses reduces tax burden on businesses and this enables businesses to reinvest thus leading to their growth and overall performance (Brian & Jacob, 2023). The analysis based on empirical data indicates that all observed tax holidays correlate with increased levels of new investments and higher expenditures on personnel by firms, which may indicate a potential connection between the incentives and elevated employment levels, especially outside of the capital area (UNU-WIDER, 2024).

Megersa (2019) also found that tax incentives contribute to predicting GDP growth, it has positive effect on research and development expenditure and causes sizeable increase in employment, output, fixed capital and total number of companies or businesses in each country.

Siyanbola et al (2017) discovered that tax incentives are a significant strategic drive for business and industrial growth in Sub-Saharan States. Besides, the more governments make revenue, the more they are better positioned to provide incentives to taxpayers. Research shows that tax exemptions decrease the tax load of SMEs more than the tax rates (Liakhoyets, 2014), which positions them to reinvest their capital for their efficient functioning. Government's support in form of tax reduction and simplification of taxation system also stimulates SMEs' growth (Louis & Macamo, 2011). Tax reduction, lower tax amount payable and tax exemption could support the

growth of SMEs. In each empirical comparative study in Uganda, it was discovered that firms with incentives performed better than firms without incentives in terms of gross sales and value added (Mayende, 2013). Better still, streamlining tax incentives was a strong stimulus to improving firm performance (Mayende, 2013).

Furthermore, tax incentives also reduce operational costs therefore enabling businesses to break even during hard times when business is slow. This indicates that the survival of some SMEs has been due tax incentives which have cut down the operational costs and enabled the SMEs to continue operating and thus enhanced the success of SMEs (Ahumuza., 2023). Irumba (2023) also had similar findings whereby tax incentives for SMEs lowered the operational costs associated with the payment of taxes for small and medium enterprises. Proponents of using business tax cuts as incentives for firm location argue that increases in job creation justify losses in revenue, while detractors argue that incentives have little economic impact and mostly benefit firm owners (Juan & Owen, 2020).

Tax incentives are crucial for the growth, development, and long-term survival of SMEs. However, the tax benefits provided by tax laws are not fully utilized by SMEs, with most of the incentives being enjoyed by larger taxpayers (Daniel & Faustin, 2019).

## **2.5 Summary of literature review**

This chapter has discussed the various theories that show the impact of taxation on the success of SMEs. It has also given an in-depth review of the variables under study and an empirical review of previous studies that are relevant to this study. The review has laid a strong foundation for this current study revealing the necessity for tax policies that can effectively promote the growth and development of SMEs while still supporting fiscal responsibility. The insights from this review will also contribute to the formulation of practical recommendations for optimizing tax regimes to support SME development and growth.

## CHAPTER THREE: MATERIALS AND METHODS

### 3.1 Study design

A cross-sectional design was used in this study combining both qualitative and quantitative approaches. Cross-sectional study design is a type of observational study design where the investigator measures the outcome and the exposures in study participants at the same time (Setia, 2016). This design was used due to its advantages in describing and explaining events as they are. It also enabled the researcher to collect both primary and secondary data to ensure that all the relevant materials required for the study are put to use.

### 3.2 Study area

The study was conducted in Nakawa Division, one of the five divisions of Kampala Capital City Authority (KCCA). Nakawa is the largest division in size and population, with over 300,000 residents (UBOS, 2016). Strategically located along the Kampala–Jinja highway, it is a major hub for trade and commerce. The division hosts more than 1,000 registered SMEs (UBOS, 2023), including retail shops, service providers, and small-scale manufacturers, which contribute significantly to employment and income generation. However, these enterprises face challenges such as high tax obligations, limited access to finance, and operational constraints, making Nakawa a suitable area for examining the impact of taxation on SME performance.



### 3.4 Sample size

The sample size was determined using the Krejcie and Morgan formula (Krejcie & Morgan, 1970)

$$n = \frac{x^2 NP(1-P)}{d^2(N-1) + x^2 P(1-P)}$$

Where:

n= Required sample size

N = Population size

P = Population proportion (assumed to be 0.5 when unknown)

d = Degree of accuracy (margin of error)

$x^2$  = Chi-square value for 1 degree of freedom at the desired confidence level (typically 3.841 for 95% confidence)

$$n = \frac{3.841 * 1000 * 0.5(1-0.5)}{0.05^2(1000-1) + 3.841 * 0.5(1-0.5)} = 277.71 \approx 278$$

Therefore, 278 SMEs were considered for the study.

### 3.5 Sampling technique

Sharma (2017) defined sampling as a procedure used to systematically select a comparatively smaller number of representations for a particular study tentative items or individuals from a pre-defined population. In this study, simple random sampling was used to select 278 SMEs from the population, while purposive sampling was applied to select 78 key respondents who provided in-depth information relevant to the study.

#### 3.5.1 Simple random sampling

In this study, simple random sampling was applied as a probability method where every respondent had an equal chance of being selected (Kothari, 2015). This approach was chosen because it minimizes bias and ensures fairness in the selection process (Horton, 2024). The researcher used this method to minimize bias and also to give the respondents equal chance of participation in the study. In this study, simple random sampling was used for selecting SMEs. A list of all SMEs

owners in Nakawa Division was obtained from Federation of Small and Medium Enterprises-Uganda (FSME) and these were written on separate pieces of paper, with a piece of paper selected one at a time until the required sample size was met.

### **3.5.2 Purposive sampling**

Purposive sampling was also applied in this study, where respondents were deliberately selected based on their relevance to the research objectives. This technique ensured that only participants with the required knowledge and experience were included (Bhardwaj, 2019). This sampling method was employed to purposively select key informants like managers, directors, marketing executives since they are reliable and knowledgeable about the variables of the study.

## **3.6 Data source**

Data was collected from both primary and secondary sources.

### **3.6.1 Primary data**

This study relied on primary data collected through the use of questionnaires and the Key informant interviews. Primary data in this study was information directly collected by the researcher using tools such as surveys and interviews, designed to specifically address and understand the research problem (Sulbuha, 2024). Obtaining primary data is expensive, long but the researcher collects real time data, and it is specific to the researcher's needs.

### **3.6.2 Secondary data**

Secondary data in this study refers to information obtained from existing sources such as government databases, previous research studies, and published journals and reports (Sulbha, 2024). Obtaining secondary data is cheap, easy and economical. In this study secondary data regarding the "effect of taxation on the performance of SMEs" was obtained from journal articles, government publications, books, websites and others.

### **3.7 Data collection methods**

#### **3.7.1 Questionnaire method**

Questionnaire method was used to capture data from the selected SME owners in the following areas service delivery (e.g., hairdressing, consultation), agriculture, retail/wholesale businesses, and restaurant/food processing. Sekaran (2003) defines a questionnaire as a preformulated written set of questions to which respondents record their response usually within rather closely defined alternatives. Questionnaires are favored as they enable respondents to write down their answers without bias and also help the researcher to conveniently reach many people at a relatively low cost. The questionnaires designed were self-administered to the sample whereby the respondents completed the questions by themselves or it was administered by the research assistant for some.

#### **3.7.2 Interview method**

An interview is a qualitative research method that relies on asking questions to gather data. Interviews involve at least two people, one of whom is the interviewer asking the questions (Tegan, 2023). Structured interviews were held with key informant interviews. The interview method was used therefore to collect qualitative data to explain how taxation affects the performance of SMEs. These interviews provided the researcher with an opportunity to probe the respondents in case of ambiguities in the responses. Interviews were used to complement the data collected through questionnaires.

### **3.8 Data collection tools**

#### **3.8.1 Questionnaire**

A self-administered questionnaire was employed for this study. The questionnaire was distributed to respondents engaged in service delivery (e.g., hairdressing, consultation), agriculture, retail/wholesale businesses, and restaurant/food processing. According to Pritha (2021), a questionnaire is a series of structured questions or items designed to collect information from respondents regarding their attitudes, experiences, or opinions. The instrument consisted primarily of close-ended questions aimed at measuring perceptions using a five-point Likert scale, ranging from Strongly Disagree (1), Disagree (2), Not Sure (3), Agree (4), to Strongly Agree (5). This scaling method facilitated the quantification and analysis of variables.

### 3.8.2 Interview guide

An interview guide was used to collect information from key informants like URA officials, KCCA officials and some managers of SMEs. The interview guide was used because it is user friendly, flexible and allows the researcher to concentrate on the areas of the study thus creating in-depth information by examining several issues that arise during the interview (Saratankos, 2005). This interview method is considered the key informants have vital information yet no time to fill in questionnaires (Sekaran, 2003). The structured interview guide used the face-to-face strategy as it is considered suitable when interviewing key informants for the purpose of acquiring more in-depth information (Sekaran, 2003).

### 3.9 Data quality control

To ensure validity and reliability the following were done

#### 3.9.1 Validity

The validity of the research instruments was ensured by discussing the questionnaire and interview guide with the supervisor before data collection, to guarantee the accuracy and meaningfulness of the inferences drawn from the results (Megenda, 1999). A pilot study was also executed before the actual data collection for more validity. After constricting the questionnaire, the researcher contacted the supervisor and other experts to get expertise judgment on validity. Construct validity of the research instruments will be refined based on expert advice to ensure that the tools accurately measure the intended concepts (Gay, 1996). According to Amin (2005), an instrument is valid if the pretest value exceeds 0.7 and is less than 1. Content validity index (CVI) was computed to highlight the validity of the research instrument.

C.V.I = Relevant items by both judges

Total number of items in the questionnaire as shown below;

CVI = No. of items rated relevant

Total number of items

$$CVI = \frac{40}{47} = 0.851$$

After computation of the Content Validity Index (CVI), the research instrument achieved a CVI value of 0.85, which exceeds the recommended threshold of 0.7 (Amin, 2005; Kothari, 2004; Mugenda & Mugenda, 2003). This indicates that the questionnaire and interview guide were considered valid and relevant by the expert judges. The pilot study further confirmed that the items were clear, understandable, and capable of capturing the intended information. Therefore, the instruments were deemed appropriate for data collection in the main study.

### **3.9.2 Reliability**

Mugenda (1999) defines reliability as an indicator of how effectively a research instrument produces results or data after repeated trials. Reliability the relays dependability of a measure (Heale & Twycross, 2015). The reliability of instruments was grounded on the preliminary results obtained from the pilot study where the interview guide and questionnaire will be pretested on persons with closely connected characteristics to those of respondents, to establish the degree to which they are reliable.

### **3.10 Data management and analysis**

According to Sekaran (2024), data analysis is the process of bringing order, structure, and meaning to the mass of raw information gathered for purposes of getting a feel for reliability and testing the hypotheses. After collecting the data, it was reviewed to ensure it was complete. Data was then coded, edited, classified and analyzed by subjecting it to various statistical tests to assess the extent to which the data can be considered to indicate and reach conclusions (Kothari, 2004). This section outlines data analysis strategies for both qualitative and quantitative data.

#### **3.10.1 Quantitative data**

Quantitative data was examined using Statistical Package for Social Sciences (SPSS) version 27. The data was imported to SPSS and both descriptive and inferential statistics were conducted to summarize the results.

#### **Descriptive statistics**

Descriptive statistics were used to determine measures of central tendency and dispersion including frequencies, percentages, mean and standard deviation and the results were presented in

tables showing the responses of each category of variables based on the five-point like scale ranging from strongly agree to strongly disagree. To obtain the mean, the responses on the likhert scale were categorized as follows; Strongly Disagree=1, Disagree=2, Neutral 3, Agree=4 and Strongly Agree=5. All the responses were then concerted to numerical value and the mean was calculated with the formula

$$mean = \frac{\sum x}{n} = \frac{sum\ of\ all\ data\ points}{number\ of\ data\ points}$$

Once the mean is in place the they were interpreted as follows:

Likert-Scale Descriptions	Likert-Scale	Likert Scale Interval
Strongly disagree	1	1.00-1.80
Disagree	2	1.81-2.60
Neutral/Uncertain	3	2.61-3.40
Agree	4	3.41-4.20
Strongly Agree	5	4.21-5.00

*Source: Nyutu et al., (2020).*

The standard deviation was calculated with the formula below

$$Standard\ Deviation = \sqrt{\frac{\sum(x_i - \mu)^2}{N}}$$

The standard deviation was calculated to measure the dispersion of responses around the mean. A low standard deviation below 1 indicates that majority responses were close to the mean, showing a general consensus among participants, whereas a high standard deviation suggests a wider range of opinions and less agreement.

### **Inferential statistics**

#### **Pearson’s correlation**

For the inferential statistics, Pearson’s correction coefficient was run to test the relationship between tax rates and the performance of SMES, tax incentives and the performance of SMEs and

taxation and performance of SMEs at 95 confidence limits. A regression analysis using Anova statistics of adjusted R<sup>2</sup> values, beta, t values and significance values as supported by (Amin, 2005). These techniques were employed to determine the extent to which taxation affects the performance of SMEs in Nakawa Market.

### **Multiple linear regression**

Multiple Linear Regression was used to model the relationship between performance of SMEs and taxation indicators. Multiple Linear Regression is a statistical method used to model the relationship between a dependent variable and two or more independent variables, enabling more accurate predictions and insights into how each predictor influences the outcome (Bevans, 2020). The formula for multiple linear regression is:

$$Y = \beta_0 + B_1X_1 + \beta_2X_2 + B_3 + \dots + \varepsilon$$

Where:

- Y = Dependent variable (Performance of SMEs)
- $\beta_0$  = Intercept (constant term)
- $\beta_1, \beta_2, \beta_3$  = Regression coefficients for independent variables
- X<sub>1</sub>, X<sub>2</sub>, X<sub>3</sub> = Independent variables (predictors)
- $\varepsilon$  = Error term (residual)

Regression outputs such as adjusted R<sup>2</sup>, beta coefficients, t-values, and p-values were interpreted to evaluate model significance and predictive power.

### **3.10.2 Qualitative data analysis**

Qualitative data was examined using content analysis technique. Content analysis was utilized to edit qualitative data and reorganize it into meaningful shorter sentences. Content analysis was used because it is flexible and can be used to transform large amounts of texts into highly organized summary of key results (Rathmore & Patwa, 2020). Content analysis was done manually which allowed the researcher to extract insights that could be missed by automated methods. The process of content analysis involved transcribing interviewee responses. The researcher then carefully read through the transcripts repeatedly to identify emerging codes. Similar codes were grouped together

to form broader categories, allowing for a structured interpretation of the data and formation of themes. The themes identified were presented with supportive quotes to retain the voice of the respondents and enhance credibility.

### **3.11 Measurement of Study variables**

In this study taxation is the independent variable while performance of SMEs is the dependent variable. Both variables were measured using the five-point Likert scale (1-Strongly disagree, 2-Disagree, 3-Not sure, 4-Agree, 5-Strongly agree). Likert scales were used because they permit respondents to select one of the response alternatives that best defines their attitudes, beliefs, and experiences towards a given phenomenon. (Yamashita, 2022). The study variables were measured as follows: SME performance was quantified using indicators such as profitability, sales growth, and business expansion, with respondents providing data on profit margins, annual revenue growth, and number of employees. Tax knowledge was measured using a structured questionnaire with items on awareness of tax types, tax rates, and filing requirements, rated on a Likert scale from 1 (strongly disagree) to 5 (strongly agree). Tax rates were measured using nominal percentages of corporate income tax, VAT, and other applicable taxes for SMEs, while SME liquidity and working capital were assessed based on reported monthly cash flow, available capital, and ability to meet operational expenses. Additionally, qualitative data from interviews and open-ended questions were coded thematically to capture perceptions of tax burden, compliance challenges, and operational impact. All variables were quantified or coded appropriately to allow analysis using descriptive statistics in SPSS.

### **3.12 Ethical Considerations**

According to Creswell (2018), ethical considerations are vital because of the need to safeguard participants; cultivate confidence with them; encourage the truthfulness of research; lookout against misbehavior and indecency that might reflect on the researchers' organizations or institutions; and manage new challenging problems. An introduction letter was obtained from the university and this was presented to the participants. Informed consent was sought from the study participants in order to participate in the study. Respondents were assured that the study is purely for academic purposes and the information given was used for that reason only and kept

confidential. To warranty confidentiality, private particulars also remained unknown during the study including names, codes were used instead of names to keep the study participants anonymous.

### **3.13 Limitations for the study**

Although the study aims to provide valuable insights on the effect of taxation on the performance of Small and Medium Enterprises (SMEs), it is essential to acknowledge certain limitations therein and these include:

- a) Some extraneous variables may be beyond the researchers control such as respondent's honesty, personal biases and uncontrolled setting of the study.
- b) External factors such as changes in regulatory environments, economic conditions or unforeseen global events could influence taxation and performance of SMEs but may not be fully accounted in for this study.
- c) Generalization of findings may be limited by the diversity of organizational structures, industries and economic contexts represented in the sample.

## CHAPTER FOUR: RESULTS AND DISCUSSIONS

This chapter presents and explains the study's findings, based on data gathered through both qualitative and quantitative methods. It builds on the materials and methods detailed in Chapter Three and aligns the results with the objectives stated in Chapter One. Each finding is examined in relation to the literature reviewed in Chapter Two, situating the study within the wider academic context. This integration across chapters ensures coherence and a consistent thematic progression. The analysis is structured around four specific objectives: assessing the level of tax knowledge among SMEs in Nakawa Division; determining the effect of tax rates on SME performance; evaluating the influence of tax incentives on SME performance; and examining the overall link between taxation and the performance of selected SMEs. The results are presented using both descriptive and inferential methods and are critically analyzed in relation to existing literature.

### 4.2 Response Rate

**Table 2: Response rate**

Category of respondents	Sample size	Actual response	Percentage (%)
SMEs	278	240	86.3
KIIs	13	13	100
<b>Actual response rate</b>			<b>86.3</b>

Table 2 above indicates the response rate of questionnaires distributed among the respondents.

Out of the 278 questionnaires distributed, 240 were completed. Of the remaining 38, 5 were damaged, 23 were not returned, and 10 were incomplete due to missing information. The response rate stood at 86.3%. Mugenda & Mugenda (2023) notes that when a response rate in a study is 70% and above, it is assumed to be appropriate for data analysis. A high response rate of 86.3% provides sufficient data for reliable interpretation and reinforces the validity measures outlined in Chapter Three. It also enhances the generalizability of findings, ensuring robust policy recommendations

### 4.3 Descriptive data analysis

The variables under descriptive analysis included the demographics of business owners and information regarding the businesses. These included; gender, age, level of education of business owners, position at the firm, type of business, years of operation and number of employees.

#### 4.3.1 Gender of Participants

**Table 3: Gender of participants**

<b>Gender</b>	<b>Frequency (n)</b>	<b>Percentage (%)</b>
<b>Male</b>	134	55.8
<b>Female</b>	106	44.2
<b>Total</b>	240	100

Results in Table 3 above shows that 55.8% of the business owners were male and 44.2% of the respondents were female, suggesting that males were the majority in the study highlighting the necessity to assess whether existing policies and programs support female entrepreneurs adequately. The male dominated population size may introduce bias which affects generalizability of the study to female business owners. This is due to the fact that without sufficient representation of female entrepreneurs, the study might overlook gender-specific issues, leading to incomplete or skewed conclusions. Research consistently indicates that women entrepreneurs face unique obstacles in contrast to their male peers which affects their participation in business ventures thus leaving businesses to be dominated by men (Ssekiziyivu, Twaki & Kabahinda, 2024). For instance, limited access to finance. Female led businesses receive a significantly smaller proportion of venture capital funding compared to male-led businesses, a disparity that is a global issue (Awuku-Asabre et al., 2021). Harvard Business Review found that female entrepreneurs receive approximately 2% of all venture funding, even though they own 38% of the businesses in the sector (Falchermann & De Concini, 2020). This gender gap can be bridged by providing institutional support including financial assistance and favorable government policies, is positively associated with the sustainability of female-owned businesses (Mwesigwa et al., 2024).

### 4.3.2 Age of Respondents

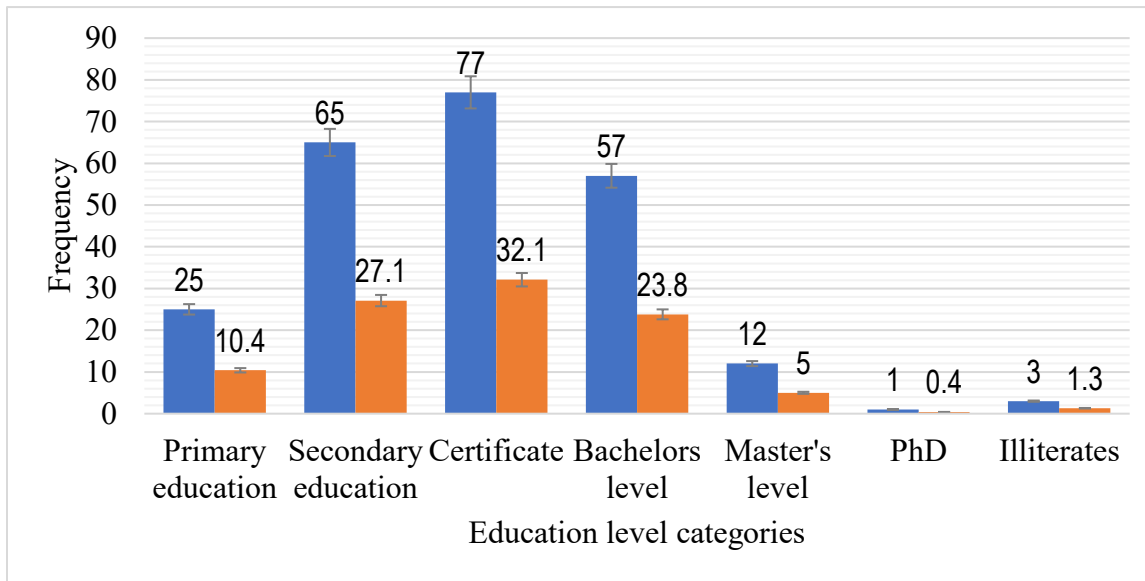
**Table 4: Age of respondents**

Age	Frequency (n)	Percentage (%)
Below 25 years	38	15.8
25-35 years	100	41.7
36-55 years	83	34.6
56 years and above	19	7.9
<b>Total</b>	<b>240</b>	<b>100.0</b>

Table 4 above shows age distribution as follows; 38 (15.8%) were under 25, 100 (41.7%) were aged 25-35 years, 83 (34.6%) were between 36-55 years and 19 (7.9%) were aged 56 years and above. This distribution reflects a workforce predominantly composed of individuals aged 25 to 55, accounting for 76.3% of participants which suggests a blend of early-career professionals and those with substantial experience, showing typical working-age groups actively engaged in business operations. potentially enhancing organizational performance through diverse perspectives (Bashir, 2021). The underrepresentation of individuals under 25 in the study (15.8%) may be attributed to factors such as limited work experience or continuing education which make them less likely to occupy key positions within businesses (International Labor Organization, 2022). A study adopting an intellectual capital perspective found that the diversity in age has a positive effect on organizational performance by boosting human social capital (Li et al, 2021). Therefore, the varied age distribution among the study participants offers a comprehensive perspective on business operations, combining youthful innovation with seasoned experience fostering an inclusive environment that leverages the strengths of all age groups to enhance organizational performance.

### 4.3.3 Level of Education

The education status of respondents varied as seen in the graph below



**Figure 2: Education level of respondents**

Figure 2 above shows that majority of the respondents in the quantitative study were certificate holders 77 (32.1%), followed by secondary education level 65 (27.1%), Bachelor's level 57 (23.8%), primary education 25 (10.4%), master's level 12 (5%), Illiterate 3 (1.3%) and lastly PHD level 1 (0.4%). This distribution indicates that a significant portion of respondents possess formal education, with the majority holding certificates or higher qualifications. This suggests that the study participants possess advanced knowledge, potentially enhancing business operations through informed decision-making and efficient management practices. The short error bars in the data indicate minimal variability in the responses, suggesting a consistent trend in the educational qualifications of business owners and employees. This reinforces the reliability of the findings, as the distribution of the education levels among respondents does not significantly vary. The consistency in the data implies that most businesses in the study are operated by individuals with at least a basic level of formal education, which may contribute to improved business management and decision making. Studies show that educational attainment is closely linked to business performance. Higher education levels often provide individuals with the ability to think critically, technical knowledge, and innovative capabilities (Van Damme & Zahner, 2022; Kayyali, 2023).

This finding contributes to the existing body of knowledge by highlighting the educational composition of business owners and employees in Uganda. The predominance of certificate holders and the substantial representation of bachelor's degree holders indicate a trend towards formal education in the business sector. Additionally, understanding the educational distribution among business professionals can inform policy decisions and training programs that focus on entrepreneurship education and training (Galvão, Marques & Ferreira, 2020).

#### 4.3.4 Current position at the Enterprise

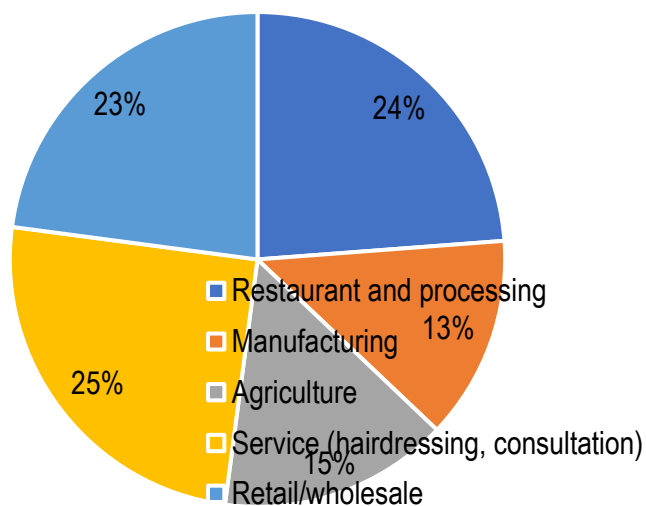
**Table 5: Position at the firm**

<b>Position at the business</b>	<b>Frequency (n)</b>	<b>Percentage (%)</b>
Owner	135	56.3
Manager	54	22.5
Employee	51	21.3
<b>Total</b>	<b>240</b>	<b>100.0</b>

Table 5 above shows that the majority 135 (56.3%) of the respondents were business owners. The predominance of business owners among the respondents suggests a strong entrepreneurial presence within the study sample. The substantial representation of managers and employees reflects the hierarchical structures within these businesses, essential for operational efficiency and growth. This distribution highlights the critical role of business owners in driving economic activity and employment confirming the recent reports that Uganda's MSMEs account for an impressive 90% of the private sector, contributing 75% to GDP and employing over 3 million people (Mumbere, 2025). The substantial representation of managers and employees reflects the hierarchical structures within these businesses, essential for operational effectiveness and expansion (Jerab & Mabrouk, 2023). These insights are essential for guiding policies focused on strengthening the MSME ecosystem and promoting sustainable economic development.

### 4.3.5 Business type

Respondents were asked the type of business they are involved in and their responses are shown in the figure below.



**Figure 3: Type of Business**

Figure 3 above shows the type of businesses the respondents are involved in. Results indicate that the majority of respondents (25%) are in service delivery (e.g., hairdressing, consultation), while the least (13%) are in agriculture and retail/wholesale business. The results indicate that service and restaurant/food processing industry are the dominant sector, and this indicates a significant demand from consumers for personal services and food-related businesses. The varied distribution reflects the diverse nature of SMEs in Uganda, which span multiple industrial sectors. In Uganda, at least ten sectors each account for a minimum of five percent of the MSME base, highlighting

the broad distribution of MSMEs across various industries (MTIC, 2024). This finding adds to the broader understanding of SME diversity in Uganda, highlighting the importance of creating targeted support strategies that address the specific challenges and opportunities of each sector. In conclusion, acknowledging this diversity is essential for developing effective policies and support systems that foster sustainable economic growth and enhance the resilience of these businesses.

**4.3.6 Business operation Period**

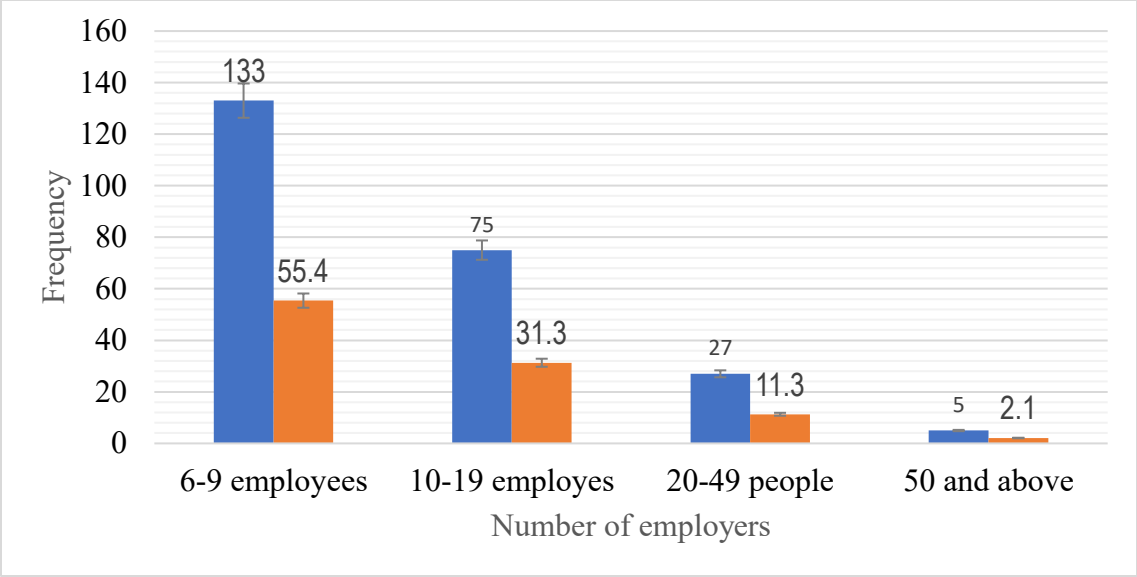
**Table 6: Business operation period**

<b>Business operation period</b>	<b>Frequency (n)</b>	<b>Percentage (%)</b>
Less than 5 years	116	48.3
5-10 years	81	33.8
10-14 years	27	11.3
Above 15 years	16	6.7
<b>Total</b>	<b>240</b>	<b>100.0</b>

When asked about the number of years the business has been in operation, responses showed that the majority of SMEs (48.3%) have been in operation for fewer than 5 years, while the least (6.7%) have operated for 15 years and above. The data indicates that over 80% of the businesses had operated for less than a decade, with nearly half (48.3%) having run for less than five years. This suggests a dynamic entrepreneurial environment but also points to challenges in sustaining business operations over time. Research has similar reports showing that many Ugandan businesses do not make it to the 5th birthday with factors influencing business survival being firm size, ownership structure, and innovation capacity (Kahunde, 2020; Muhwezi & Niclous, 2023). The predominance of newer businesses in the study highlights the need for targeted support to enhance their survival and growth prospects including capacity building, access to finance and market access. Understanding this distribution of business operation periods aids policymakers in designing interventions that address the specific needs of businesses at various stages of development, ultimately producing a more resilient and sustainable SME sector.

**4.3.7 Number of people employed in the business**

The number of people employed in the businesses are shown in the figure below.



**Figure 4: Number of people employed in the business.**

Figure above indicates the number of people employed in the business. The majority of businesses (55.4%) employed 5–9 people, while the least (2.1%) employed 50 or more people. The data reveals that a significant majority (86.7%) of businesses employ between 5 and 49 individuals, with over half (55.4%) maintaining a workforce of 5 to 9. This distribution suggests that small to medium-sized enterprises (SMEs) are predominant, aligning with the broader characteristics of Uganda's MSME sector as the major employer in Uganda (Okumu & Buyinza, 2020). The small proportion of businesses (2.1%) employing over 50 people suggests that while SMEs dominate Uganda's business landscape, only a limited number of enterprises reach a size that necessitates a larger workforce.

The short error bars indicate low variability in responses, meaning that the reported employment figures are relatively consistent across the businesses surveyed. This suggests that SMEs in Uganda tend to have a stable workforce size, reinforcing the reliability of the data.

**4.4 Performance of selected SMEs**

The dependent variable in this study was performance of selected SMEs. For this variable, key statements regarding performance of SMEs were chosen based on insights from the literature review, and respondents were requested to express their agreement or disagreement with each

statement. The responses were embedded in a five-point Likert scale. From the analysis, a mean range of 3.50-5.00 indicated agreement and a mean of 1.00-3.49 indicated disagreement as shown in Table 7 below.

**Table 7: Performance of selected SMEs in Nakawa Division**

Statements	SD %	D %	N %	A %	SA %	Mean	Std.
<b>Profitability</b>							
Our business' profitability has increased steadily over the past year.	5(2.1)	10(3.8)	35(14.2)	166(69.2)	24(10.8)	3.81	0.75
We consistently meet or exceed our profit margin targets.	4(1.7)	18(3.8)	30(11.7)	127(52.9)	61(25.4)	3.93	0.85
The profitability of our business enables us to reinvest in our operations.	1(0.4)	23(9.6)	23(9.6)	97(40.4)	96(40.0)	4.10	0.79
<b>Innovation</b>							
Our business frequently introduces new goods or services to the market.	0(0.0)	10(4.2)	22(9.2)	136(56.7)	72(30.0)	4.13	0.72
We invest in research and development to drive innovation within our company.	14(5.8)	24(10.0)	31(12.9)	115(47.9)	56(23.3)	3.73	1.10
Our business culture encourages creativity and generation of new ideas.	1(0.4)	8(3.3)	18(7.5)	115(49.7)	98(40.8)	4.25	0.77
<b>Market share</b>							
Our business has captured a larger share of the market in our industry over the past year.	4(1.7)	18(7.5)	33(13.8)	126(24.6)	59(24.6)	3.91	0.91
We have effectively expanded our market presence into new regions or customer segment.	4(1.7)	20(8.3)	31(12.9)	106(44.2)	79(32.9)	3.98	0.97
Our marketing strategies have been successful in increasing our market share	1(0.4)	11(4.6)	26(10.8)	113(47.1)	89(37.1)	4.16	0.86
<b>Employment rate</b>							
Our business has consistently increased the number of employees over the past year.	10(4.2)	35(14.6)	19(7.9)	135(56.3)	41(17.1)	3.68	1.05
Employee turnover in our business is low due to good working conditions and opportunities.	3(1.3)	18(7.5)	17(7.1)	123(51.2)	79(32.9)	4.07	0.90

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Our business is focused on retaining skilled employees through competitive salaries and benefits.	2(0.8)	1(0.4)	14(5.8)	125(52.1)	98(40.8)	4.32	0.68
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*Source: Primary Data, 2025: where SD= Strongly Disagree, D=Disagree, N=Neutral, A=Agree, SA=Strongly Agree*

The overall mean of performance of selected SMEs in Nakawa Division is 4.00 which suggests that majority of SMEs view their performance as good, indicating positive outcomes based on the performance indicators used, which include employment rate, market share, profitability and innovation. Regarding the statement, “Our business’ profitability has increased steadily over the past year”, majority of the respondents as confirmed by 3.81 and allow standard deviation of 0.75. The results suggest that on average, respondents perceive an increase in the business's profitability over the past year. These findings contrast with a study conducted by Mayanja (2020) who found that 65.7% of respondents disagreed regarding profitability of their businesses, 32.0% affirmed profitability and 2.2% were not sure about the profitability status of their businesses. This discrepancy may be attributed to differences in sample characteristics, economic conditions, or timeframes between the studies. The positive perception of profitability among respondents offers valuable insights into the current state of MSMEs in Uganda. It suggests that, despite previous challenges, there may be an emerging trend of improved financial performance within this sector.

The results above also show that majority of the Businesses confirmed that they meet or exceed their profit margin targets as the majority of respondents (69.2%) agreed, while the least (2.1%) strongly disagreed with a total average score of 3.93 and a standard deviation of 0.85. additionally, when asked if the profitability of their businesses allow them to reinvest in their operations, 0.4% Strongly Disagreed, 9.6% Disagreed, 9.6% were Neutral, 40.4% Agreed and 40.0% Strongly Agreed scoring an average of 4.10 and a standard deviation of 0.79. This indicates that a significant majority of businesses are meeting or exceeding their profit margin targets, with 80% of respondents agreeing or strongly agreeing. These strong agreement levels indicate that majority of businesses are achieving their profit goals and generating sufficient profits to reinvest in their operations which is crucial for sustaining growth, enhancing competitiveness, and ensuring long-term viability. The results confirm a report that Uganda's GDP grew by 6.7% in the initial quarter of the 2024/25 financial year, up from 5.6% in the same period of the previous year attributed to sectors such as agriculture, wholesale trade, construction indicating that the businesses are doing

well (Rupiny, 2025). However, this is contrasted by the Business Health Index report which indicated that there was a decline in enterprise profitability, dropping from 34.78 in Q3 2023 to 29.89 in Q1 2024, primarily attributed to increased operational costs (UDB, 2024). Therefore, while many businesses feel confident about their profitability and ability to reinvest, it is vital to consider external elements that could influence these perceptions. Continuous monitoring and supportive policy interventions are vital to ensure that these positive sentiments translate into long-term economic growth and stability.

On the innovation indicator, when asked if the business frequently introduces new goods or services to the market, 4.2% Disagreed, 9.2% were not sure, 56.7 Agreed and 30.0% Strongly agreed (Mean=4.13, Std.=0.72). additionally, regarding the statement “We invest in research and development to drive innovation within our company”, majority agreed with 23.3 Strongly Agreed, 47.9% Agreed, 12.9% were not sure, 10.0 Disagreed and 5.8 Strongly Disagreed (Mean=3.73, Std.=1.10). Additionally, majority of the respondents expressed their agreement that their business culture encourages creativity and generation of new ideas as 40.8% Strongly Agreed, 49.7% Agreed, 7.5% were Neutral, 3.3% Disagreed and 0.4% Strongly Disagreed (Mean=4.25, Std.=0.77). The results suggest that most respondents from SMEs strongly support research and development along with creativity and new ideas for innovation. This aligns with innovative business models which emphasize continuous improvement and technological advancements which focus on rethinking how businesses operate, create value and adapt to market demands (Brenner & Drdla, 2023). However, the significant portion that were unsure or disagreed to supporting research and development suggests barriers to innovation investment such as financial constraints, quality of human resource, government support, economic condition and business partners could hinder innovation (Indrawati, Caska & Suarman, 2020).

Regarding market share, respondents were asked if their businesses had captured a larger share of the market in our industry over the past year and their responses varied with 24.6% Strongly Agreed, 52.5% Agreed, 13.8% were neutral, 7.5% Disagreed and 1.7% Strongly Disagreed (Mean=3.91, Std.=0.91). On the statement, “We have effectively expanded our market presence into new regions or customer segment”, 32.9% Strongly Agreed, 44.2% Agreed, 12.9% were Neutral, 8.3% Disagreed and 1.7% Strongly Disagreed (Mean=3.98, Std.=0.97). Additionally,

when asked if the marketing strategies used by the businesses have been successful in increasing their market share, most were positive as 37.1% strongly Agreed, 47.1% Agreed, 10.8% were not sure, 4.6% Disagreed and 0.4% Strongly Disagreed (Mean=4.16, Std.=0.86). Majority of businesses agreed or strongly agreed that they had captured a larger share of the market, expanded market presence and had successful marketing strategies in their respective industries over the past year suggesting a general positive growth trend in market presence. The increase in market share could be influenced by competitive pricing, product innovation, customer engagement, and effective marketing strategies (Chicilia & Yuliana, 2024). However, the respondents that disagreed or were neutral could show that some businesses experienced insignificant market growth due to market saturation, high competition, financial constraints, or operational inefficiencies (Surajwancy & Kulkarni, 2024).

Another indicator was employment rate and respondents still had varying responses. Use When asked if the business has consistently increased the number of employees over the past year, 17.1% Strongly Agreed, 56.3% Agreed, 7.9% were Neutral, 14.6% Disagreed and 4.2% Strongly Disagreed (Mean=3.68, Std.=1.05). Majority of the businesses acknowledges that their employee turnover in is low due to good working conditions and opportunities with the scores of 32.9% Strongly Agreed, 51.2% Agreed, 7.5% were Neutral, 7.1% Disagreed and 1.3% Strongly Disagreed (Mean=4.07, Std.=0.90). Regarding the statement “Our business is focused on retaining skilled employees through competitive salaries and benefits”, 40.8% Strongly agreed, 52.1% Agreed, 5.8% were Neutral, 0.4% Disagreed and 0.8% Strongly Disagreed (Mean=4.32, Std.=0.68). The high percentage of agreement indicate that an overwhelming majority of the businesses prioritize retaining skilled employees by offering competitive salaries and benefits suggesting that most businesses recognize the importance of competitive compensation in employee retention. The findings above highlight that most businesses increased number of employees and focused on retaining skilled employees experience thus had a low employee turnover due to favorable working conditions and available opportunities suggesting that most employees are content with their work, leading to higher retention rates (Lasanov et al., 2023), which enhances productivity, employee morale and overall business performance (Chang, 2024).

#### 4.5 The knowledge of taxpayers regarding taxation in selected SMEs in Nakawa Division.

The first objective was to examine the knowledge of taxpayers regarding taxation in selected SMEs in Nakawa Division. Key statements regarding taxation were identified from reviewed literature and respondents were asked to express their degree of agreement or disagreement with each statement on a five-point Likert scale as shown in Table 8 below.

**Table 8: Descriptive statistics on knowledge of taxpayers regarding taxation**

Statement	SD%	D%	N%	A%	SA%	Mean	Std.
The purpose of paying taxes is clear to me.	41(17.1)	36(15.0)	19(7.9)	70(29.2)	74(30.8)	3.42	1.48
I am aware of the various types of taxes (Income tax, value added tax, excise duty, custom duty) applicable to businesses.	34(14.2)	63(26.3)	11(4.6)	74(30.8)	58(24.2)	3.25	1.43
I know how to accurately calculate my tax liability based on my income and expenses.	37(15.4)	71(29.6)	10(4.2)	71(29.6)	51(21.3)	3.12	1.43
I have adequate knowledge of the tax filing process.	49(20.4)	54(22.5)	17(7.1)	71(29.6)	49(20.4)	3.07	1.47
I am informed about the penalties for non-compliance with tax regulations.	48(20.0)	33(13.8)	30(12.5)	77(32.1)	52(21.7)	3.22	1.44
I know where to find accurate information about tax laws and regulations.	36(15.0)	49(20.4)	18(7.5)	77(32.1)	60(25.0)	3.32	1.43
I have clear understanding of my tax obligations and how to comply with tax regulations effectively.	36(15.0)	53(22.1)	20(8.3)	74(30.4)	57(23.8)	3.26	1.42

*Where SD= Strongly Disagree, D=Disagree, N=Neutral, A=Agree, SA=Strongly Agree*

Table 8 above shows the responses from respondents regarding taxation knowledge. Regarding clarity on the purpose of paying tax, 30.8% Strongly Agreed, 29.2% Agreed, 7.9% were Neutral, 15.0% Disagreed and 17.1% Strongly Disagreed (Mean=3.42, Std.=1.48). Also, for the statement “I am aware of the various types of taxes (Income tax, value added tax, excise duty, custom duty) applicable to businesses”, 24.2% Strongly Agreed, 30.8% Agreed, 4.6% were Neutral, 26.3% Disagreed and 14.2% Strongly Disagreed (Mean=3.25, Std.=1.43). To this, a senior tax officer with an eight-year of experience responded, “*Income tax, VAT and local service taxes dominate SME obligation*” per K1. Another respondent who is a tax compliance advisor added, “*Added business license fees and withholding taxes are additional to income tax, VAT and Pay-as-you-earn (PAYE) for businesses with employees*”. K2

The results above reveal that a significant proportion of respondents who are unclear about the purpose of paying taxes highlights a significant knowledge gap which can eventually affect tax compliance rates among small and medium-sized enterprises (SMEs). A similar study by Arinaitwe & Ahumuza (2023) found that a large proportion of respondents within the SME sector do not have clear understanding of the Ugandan taxation system. Numerous studies have indicated a strong relationship between clear understanding of taxation and compliance since business owners and managers or employees do not understand the rationale behind paying taxes, they are less likely to comply (Oromo et al., 2023; Magara, Arinaitwe & Omendo, 2023). The data highlights the need for improved tax education and awareness among SMEs in Uganda

On the statement “I know how to accurately calculate my tax liability based on my income and expenses”, 21.3% Strongly Agreed, 29.6% Agreed, 4.6% were not sure, 29.6% Disagreed and 15.4% Strongly Disagreed (Mean=3.12, Std.=1.43). Additionally, when asked if they had adequate knowledge of the tax filing process, 20.4% Strongly Agreed, 29.6% Agreed, 7.1% were Neutral, 22.5% Disagreed, 20.4% Strongly Disagreed (Mean=3.07, Std.=1.47). The findings show that a significant percentage of the respondents cannot calculate their tax liability based on income and expenses and similarly a substantial proportion of respondents did not have adequate knowledge of the tax filling process. Similar studies by Ahumuza & Arinaitwe (2023) and Faridah et al. (2023) that found that many SME owners lack formal training in financial management, leading to difficulties in tax computation and filing and this gap can result in non-compliance which

negatively impact tax revenue collection. This can be addressed through interventions such as tax education programs and simplified tax guides that can be easily understood by the SME operators.

When asked if they were informed about the penalties for non-compliance with tax regulations, 21.7% Strongly Agreed, 32.1% Agreed, 12.5% were Neutral, 13.8% Disagreed and 20.0% Strongly Disagreed (Mean=3.22, Std.=1.44) this suggests that most respondents are aware of credible sources for tax related information. Additionally, for the statement, “I know where to find accurate information about tax laws and regulations”, 25.0% Strongly Agreed, 32.1% Agreed, 7.5% were Neutral, 20.4% Disagreed and 15.0% Strongly Disagreed (Mean=3.32, Std.=1.43). The data reveals that majority (57.1%) of the respondents know where to find accurate tax information as supported by an SME owner who had this to say, “*Mostly from my accountant, Uganda Revenue Authority (URA) offices, and sometimes from online resources. Occasionally, I seek advice from fellow business owners or tax agents.*” per respondent 8. However, a significant portion (35.4%) do not know where to find accurate information suggesting that tax information accessibility varies among business owners. Findings from other studies indicate that SMEs often rely on informal sources such as accountants, peers, or social media, which may not always provide up-to-date or accurate information (Ahumuza & Arinaitwe, 2023; Mugisha et al, 2023). This knowledge gap leads to misinformation which affects compliance and adherence to tax regulations. Improving access to accurate information can lead to better compliance and business sustainability.

When asked if they were informed about the penalties for non-compliance with tax regulations, 21.7% Strongly Agreed, 32.1% Agreed, 12.5% were Neutral, 13.8% Disagreed and 20.0% Strongly Disagreed (Mean=3.22, Std.=1.44) this suggests that most respondents are aware of credible sources for tax related information. Additionally, when asked if they were informed about the penalties for non-compliance with tax regulations, 21.7% Strongly Agreed, 32.1% Agreed, 12.5% were Neutral, 13.8% Disagreed and 20.0% Strongly Disagreed (Mean=3.22, Std.=1.44) this suggests that most respondents are aware of credible sources for tax related information. Similarly, Respondents were also asked if they have clear understanding of tax obligations and how to comply with tax regulations effectively and 23.8% Strongly Agreed, 30.4% Agreed, 8.3% were not sure, 22.1% Disagreed, 15.0% Strongly Disagreed (Mean=3.26, Std.=1.42). The results reveals that while a slight majority (54.2%) of respondents believe they have a clear understanding of their

tax obligations a significant portion (37.1%) do not share this confidence. This is supported by one of the respondents from the interview who had this to say, *“I have a basic understanding of SME tax regulations, such as deadline for filing and the percentage rates for VAT.”* Per respondent 10. Another respondent added, *“I have limited knowledge about the tax regulations. The tax regulatory officials are always helpful to me when it comes to computing taxes”*. Per respondent 5. Another also said, *“I have basic understanding, but tax policies can be confusing. I try my best to comply but sometimes I need help understanding certain requirements.....”* Per respondent 9

This disparity in self-assessed tax understanding among SMEs is concerning, as inadequate knowledge can lead to unintentional non-compliance and hinder business growth (Ahumuza & Arinaitwe, 2023).

In an interview, when asked whether they had ever participated in any training or workshops on taxation for SMEs, respondent 8 said,

*“Yes, I attended a tax workshop organized by Uganda Revenue Authority. I learned about tax filling procedures, how to calculate VAT, and the value of keeping proper financial records.....”*

However, some respondent had never attended any training or workshop regarding taxation and in regard to this, respondent 9 had this to say.

*“No, I have never attended any formal training. However, I would be happy to learn more about tax requirements and benefits for small businesses.....”*

Respondent 6 said,

*“.....I usually do my trainings by following the information on the website of Uganda Revenue Authority. This has helped me to get some information concerning tax laws and regulations.....”*

The responses from the respondents above show varied levels of tax knowledge and engagement regarding taxation training among SMEs. While some respondents like respondent 8 have attended and benefitted from trainings organized by Uganda Revenue Authority, other respondents like respondent 9 have never participated in any structured training. Respondent 6 however, relies on

online resources from URA for tax-related Knowledge. The mode of training or insufficient training causes varied levels of knowledge as SMEs that attend formal training sessions tend to have better tax knowledge, Improved compliance and reduced tax related challenges (Appiah, Domeher & Agana, 2024). The SMEs that resort to self-learning online resources suggest that digital tax education plays a role in bridging the knowledge gap and therefore should be strengthened.

The findings above address objective one and suggests varies levels of tax knowledge among SMEs. The results also indicate that limited tax knowledge negatively influences compliance and affects performance of SMEs.

**4.6 Empirical findings on the effect of tax rates on the performance of selected SMEs in Nakawa Division.**

The second study objective was to assess the effect of tax rates on the performance of SMEs in Nakawa Division. Key statements were chosen in line with the literature review and respondents were asked to express their degree of agreement or disagreement with each statement as the five-point Likert scale.

**Table 9: Descriptive statistics on the effect of tax rates on performance of selected SMEs in Nakawa Division**

Statements	SD%	D%	N%	A%	SA%	Mean	Std.
The tax rates in my country influence the growth of SMEs.	7(2.9)	7(2.9)	19(7.9)	136(56.7)	71(29.6)	4.07	0.87
Tax rates influence profitability of businesses	1(0.4)	3(4.2)	8(3.3)	135(56.7)	92(38.3)	4.34	0.64
Tax rates influence my decisions on hiring and maintaining staff.	1(0.4)	10(4.2)	31(12.9)	108(45.0)	90(37.7)	4.15	0.83
The complexity of tax compliance due to high tax rates takes significant resources from other business operations.	2(0.8)	8(3.3)	29(12.1)	143(59.6)	58(24.2)	4.03	0.76

Tax rates influence formalization of businesses to avoid tax burden	17(7.1)	7(2.9)	23(9.6)	109(45.4)	84(35)	4.15	2.74
Increased tax obligations limit my ability to invest in new technologies or innovations.	2(0.8)	11(4.6)	19(7.9)	130(54.2)	78(32.5)	4.13	0.81
Reducing tax rates would improve the financial stability of my business.	0(0.0)	1(0.4)	15(6.3)	122(50.8)	102(42.5)	4.35	0.62

**Source: Primary Data, 2025, where SD= Strongly Disagree, D=Disagree, N=Neutral, A=Agree, SA=Strongly Agree**

Results from Table 9 above show that most of the respondents agreed that tax rates influence the growth of SMEs as 29.6% Strongly Agreed, 56.7% Agreed, 7.9% were not sure, 2.9% Disagreed and another 2.9% Strongly Disagreed (Mean=4.07, Std.=0.87). Additionally, when asked if tax rates influenced the profitability of businesses, 38.3% Strongly Agreed, 56.7% Agreed, 3.3% were Neutral, 4.2% Disagreed and 0.4% Strongly Disagreed (Mean=4.34, Std.=0.64). The results indicate that a significant majority of respondents perceive tax rates as influential on both the growth and profitability of SMEs. Specifically, 86.3% agreed that tax rates affect SME growth (Mean=4.07, Std.=0.87), and 95% concurred regarding profitability (Mean=4.34, Std.=0.64). The findings align with a study by Ahumuza & Kobusingye (2025) which highlighted that tax rates have a negative impact on profitability.

For the statement, “Tax rates influence my decisions on hiring and maintaining staff”, 37.7% Strongly Agreed, 45.0% Agreed, 12.9% were not sure, 4.2% Disagreed, and 0.4% Strongly Disagreed (Mean=4.15, Std.=0.83).

Regarding the statement, “The complexity of tax compliance due to high tax rates takes significant resources from other business operations”, 24.2% Strongly Agreed, 59.6% Agreed, 12.1% were not sure, 3.3% Disagreed, 0.8% Strongly Disagreed (Mean=4.03, Std.=0.76). These findings show that high tax rates impose considerable administrative burdens on SMEs. This finding is similar to a study by Tax foundation where it was found that businesses indicated an increase in income tax complexity since 2017, with a weighted average increase in funds dedicated to compliance costs of 32 percent from 2017 to 2023 (McBride, 2024). This high tax compliance hinders SME growth

by diverting resources from important business activities impacting their competitiveness and sustainability (OECD, 2022). These concerns should be addressed through establishing targeted tax policy reforms that can enable operational efficiency and growth of SMEs.

Respondents had varying responses when asked if tax rates influence/influenced the formalization of business to avoid tax burden. 35.0% Strongly Agreed, 45.4% Agreed, 9.6% were Neutral, 2.9% Disagreed and 7.1% Strongly Disagreed (Mean=4.15, Std.=2.71). High tax rates act as a barrier to formalization. A high percentage of SMEs operate informally to avoid taxes due to their burdensome and complicated nature (Amos et al., 2024).

For the statement, “Increased tax obligations limit my ability to invest in new technologies or innovations”, 32.5% Strongly Agreed, 54.2% Agreed, 7.2% were Neutral, 4.6% Disagreed, 0.8% Strongly Disagreed (Mean=4.13, Std.=0.81). To this respondent 6 commented, *“The existing tax rates restrict the capacity to invest in new technologies, redirecting funds that could have been used for technology advancement as it is used to meet the taxes, ..... taxes have been increasing to the point where I was demoralized and I resorted to dodging them though it comes with a negative impact as well for example bribing some tax officials”*. The results are similar to findings by Ssabavuma (2024) also showed that increased tax rates increase s the operation costs of the business reducing net profits and limiting funds available for reinvestment therefore negatively affecting expansion and growth.

Finally, when asked if reducing tax rates would improve the financial stability of the business, the scores were; 42.5% Strongly Agreed, 50.8% Agreed, 6.3% were Neutral and only 0.4% Disagreed (Mean=4.35, Std.=0.62). in addition to this, respondents had this to say in the interview, ***“The current tax rates for SMEs are not reasonable. The SMEs are charged very high taxes, and the tax burden shifts to the final consumer in form of high prices....”*** Per respondent 4. Another respondent added, ***“We are forced to increase the prices of different commodities due to the high taxes charged by the tax regulatory bodies. Even if the taxes increase, the seller will ensure that he makes profits, and this is done through increasing the prices of the products....”***. Respondent 7 also had this to say, *“The tax rates do not favor growth of businesses because they are a burden to the taxpayers. That is why businesses in Kampala have been striking due to new taxes by the government....”*. The results highlight that high tax rates reduce financial stability through

increasing the cost of doing business, forcing the burden to pass on to consumers through higher prices. High tax rates on SMEs also lead to reduced profitability, increased informality, and business closure (Ahumuza & Arinaitwe, 2023).

When tax officers were asked if they think tax rates influence the growth and expansion of SMEs, they responded, *“High tax rates deter investment and innovation, forcing the SMEs to prioritize survival over growth”*. Per respondent K1. Another officer added, *“Taxation heavily affects startups, limiting their ability to scale or compete with larger businesses. Elevated tax rates with low awareness discourage compliance. Seasonal businesses are particularly affected by cash flow issues”*. Per respondent K2

The results show that most of the respondents reducing tax rates would improve financial stability of the businesses. This is supported by other studies as one reported that tax rates and the cost of compliance reduce stability and sustainability of the business. The study by Ahumuza, Kobusingye and Musiimenta (2025) found that for every 1% increased cost of compliance, sustainability decreases by 0.26 units.

**Table 10: Pearson’s Correlation Between Tax rates and performance of selected SMEs**

		Mean performance of selected SMEs	Mean Tax rates
<b>Mean performance of SMEs</b>	Pearson Correlation	1	.462
	Sig. (2-tailed)		<.001
	N	240	240
<b>Mean tax rates</b>	Pearson Correlation	.462	1
	Sig. (2-tailed)	<.001	
	N	240	240

\*\*Correlation is significant at the 0.01 level (2-tailed).

The R-value of 0.462 indicates a moderately strong positive correlation between tax rates and SME performance indicating that as tax rates change, there is a noticeable impact on performance of SMEs. Additionally, a P-Value <0.001 indicates that the connection between tax rates and SME

performance is statistically significant meaning that while tax rates play an important role in determining performance of SMEs, other factors such as market access also contribute to performance outcomes (Ahumuza & Arinaitwe, 2023).

**Table 11: Model Summary for Tax rates and selected SME performance**

Model	R	R Square	Adjusted R Square	Sig. F Change
1	.462 <sup>a</sup>	.213	.210	<.001

a. Predictors: (Constant), Mean tax rates

Results from the Table 11 above shows an R square value of 0.213 indicating that 21.3% of the variance in the SME performance is explained by the tax rates. However, though tax rates have a moderate effect on the SME performance, 78.7% of the variance in performance is due to other elements other than tax rates.

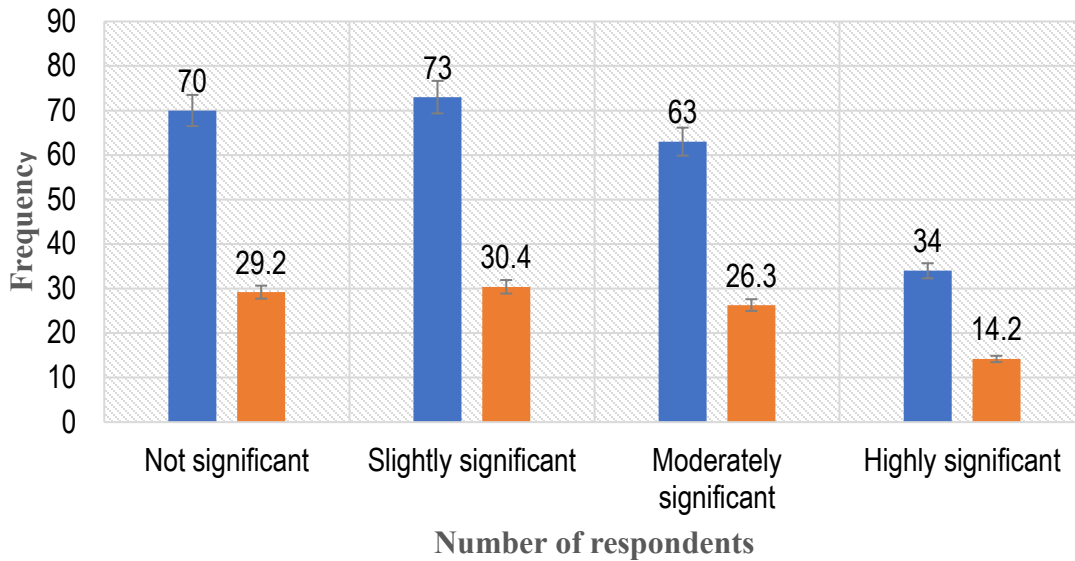
This findings above address objective two and suggests that tax rates, when perceived as excessive by SMEs in Nakawa Rivision and directly inhibits SME performance and growth.

#### **4.7 Empirical findings on the effect of tax incentives on selected SME performance in Nakawa Division.**

The third study objective was to assess the effect of tax incentives on the performance of SMEs in Nakawa Division and questions were asked basing on tax incentives and their responses are shown in the following subsections.

##### **4.7.1 Significance of tax incentives in improving SME performance**

Respondents were asked how significant tax incentives were in improving their business performance and their responses are noted in the figure below.



**Figure 4: Significance of tax incentives in improving business performance**

Figure 4 above shows that 73 (30.4%) of the respondents said tax incentives were slightly significant, 70 (29.2%) said they were not significant, 63 (26.3%) said they were moderately significant and 34 (14.2%) said they were highly significant in improving business performance. The short error bars in the graph suggest that respondents had relatively consistent opinions on the significance of tax incentives, indicating a low degree of variability in responses. The findings were supported by tax officials had this to say,

*“Tax incentives are moderately effective, though awareness among SMEs remain a significant limitation” respondent K1*

*“Informed SMEs have benefited, but inconsistent implementation reduces the overall effectiveness of these incentives”.*

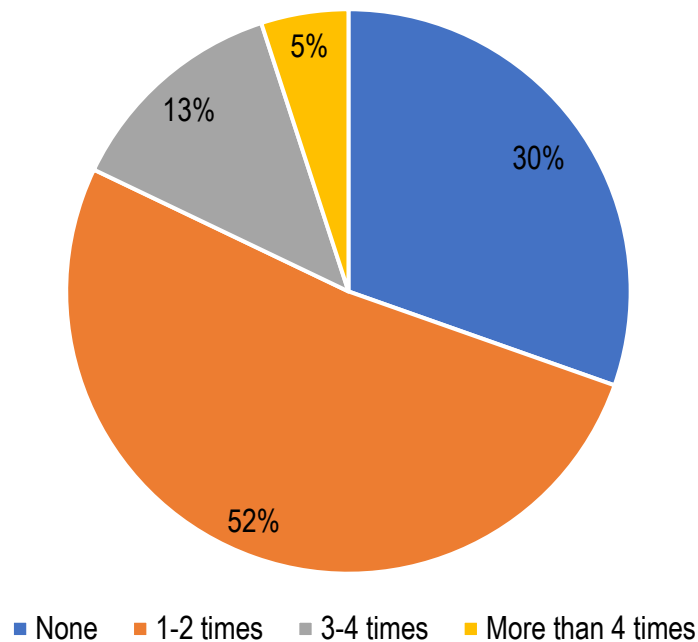
The findings above indicate that tax incentives play part in improving business performance, though their effectiveness is limited by low awareness and poor implementation (Ahumza & Arinaitwe, 2023). Another study by Sibebe, Gomera & Sibanda (2022) found that the implementation of tax incentive was not transparent as it gave an opportunity for corrupt behavior. Lakuma (2019) found out that the awarding of corporate income tax was discretionary. Some

companies enjoyed capital allowances assets and tax holidays while others did not. The findings show policy makers the need to improve awareness and transparent implementation of tax incentives to ensure they effectively support SME growth.

This finding address's objective three and suggests that SMEs perceive tax incentives as significant in improving business performance.

#### 4.7.2 Number of times business applied for incentives over the last year

Regarding applications for incentives over the past year, responses of respondents are blotted in the figure below.



**Figure 5: Application for incentives by SMEs in Nakawa Division over the past year**

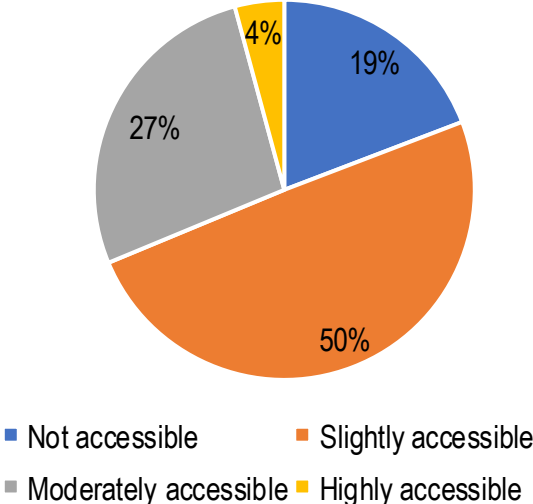
Figure 5 above shows majority of the SMEs 124 (51.7%) applied for incentives 1-2 times in the past year, 73 (30.4%) did not apply at all, 31 (12.9%) applied 3-4 times and 12 (5.0%) applied more than 4 times. The results suggest that there could be potential gaps in awareness or relevance

of the incentives leading to many SMEs not applying for them and the majority applying for only 1-2 times in a year. A smaller percentage of SMEs applied 3-4 times and only 5% applied more than 4 times implying that frequent utilization of incentives is uncommon among SMEs. The data indicates that incentives are underutilized suggesting that many SMEs may not be optimizing available financial relief measures, which could enhance their profitability and reinvestment capacity (Sebele, Gomera, Sibanda, 2022).

The findings address Objective Three by revealing low SME application rates for tax incentives, suggesting that limited awareness or accessibility hinders their full utilization, ultimately affecting profitability and performance.

### 4.7.3 Accessibility of tax incentives

Respondents were asked how accessible tax incentives in their line of business are and below are their responses.



**Figure 6: Accessibility of Tax incentives to SMEs**

Results from Figure 6 shows that 50% of SMEs acknowledged that tax incentives are slightly accessible, 27% said they were moderately accessible, 19% said they were not accessible and 4% said they were highly accessible suggesting that while some SMEs can access tax incentives to a certain degree, many SMEs still face significant barriers, limiting the effectiveness of these

incentives in supporting their growth. This suggests that despite the existence of tax incentives, their practical accessibility remains limited for many SMEs. The low usability according to OECD (2025) is due to bureaucratic procedures, lack of awareness, and stringent eligibility criteria preventing SMEs from benefiting fully from tax incentives. Ahumuza & Arinaitwe (2023) also notes that in Uganda, the complexity of tax policies and insufficient communication from tax authorities contribute to low utilization of available incentives.

The findings above address Objective Three by showing that many SMEs find tax incentives only slightly or moderately accessible, with barriers such as complex procedures and poor communication limiting their use

#### 4.7.4 Tax incentive can improve business financial stability

To gain insight into their views on financial support, respondents were asked whether they believed tax incentives could enhance their business's financial stability, their respondents were as in the Table 12 below.

**Table 12: Descriptive statistics on tax incentives improving business financial stability**

<b>Do you believe tax incentives can/have improved your business financial stability?</b>	<b>Frequency (n)</b>	<b>Percentage (%)</b>
Strongly Disagree	39	16.3
Disagree	26	10.8
Neutral	40	16.7
Agree	115	47.9
Strongly Agree	20	8.3
<b>Mean</b>		<b>3.21</b>

Results from Table 12 shows that most of the respondents agreed that tax incentives can improve financial stability in a business as 155 (47.9%) of SMEs agreed, 20 (8.3%) strongly agreed indicating positive perception possibly due to past experiences with the tax incentive, 40 (16.7%) were neutral suggesting uncertainty or lack of awareness about the benefits of the incentives, 26 (10.8%) disagreed and 39 (16.3%) strongly disagreed indicating dissatisfaction or skepticism possibly due to past experiences with tax incentives. The finding suggests a generally positive

perception of tax incentives among SMEs, with a majority (47.9% agreeing and 8.3% strongly agreeing) acknowledging their potential to enhance financial stability. This is similar to other studies which asserts that well-structured tax incentives can reduce financial strain on SMEs, allowing for reinvestment and business expansion therefore enhancing SME performance (Sebele, Gomera, Sibanda, 2022, Ahumuza & Arinaitwe, 2023).

Tax officers were asked the tax incentives offered to SMEs in Nakawa Division and these were their responses,

*“Tax holidays for newly registered SMEs and reduced corporate tax rates in sectors like manufacturing and agriculture”. Per respondent K1*

Another added,

*“Added VAT deferrals and local service tax exemptions for qualifying SMEs”. As per respondent K2*

*Respondent K3 highlighted,*

*“Accelerated depreciation allowances for capital investments as an incentive aimed at reducing operational cost”. Respondent K3*

**Table 13; Pearson’s Correlation Coefficient Between Tax Incentives and Performance of SME**

		Mean performance of selected SMEs	Mean Tax incentives
<b>Mean performance of SMEs</b>	Pearson Correlation	1	.372
	Sig. (2-tailed)		<.001
	N	240	240
<b>Mean Tax incentives</b>	Pearson Correlation	.372	1
	Sig. (2-tailed)	<.001	
	N	240	240

\*\*Correlation is significant at the 0.01 level (2-tailed).

Results from the Pearson’s Correlation Coefficient ( $r=0.372$ ) shows a moderately positive association between tax incentives and SME performance suggesting that as tax incentives improve or become more accessible, the performance of SMEs also improves though the association is not strong.

A significance level of  $p<0.001$  shows that the correlation is statistically significant indicating that tax incentives have a meaningful impact on SME performance in the study population. This finding is similar to finding of a study done by Ahumuza, Arinaitwe and Agaba (2023) and Daniel & Faustin (2019) who found that there is a strong link between tax incentives and performance of SMEs as tax incentives enhances the level of entrepreneurship.

**Table 14;Model Summary for Tax Incentives and Performance of selected SMEs**

<b>Model</b>	<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Sig. F Change</b>
<b>1</b>	.372 <sup>a</sup>	.138	.134	<.001

a. Predictors: (Constant), Mean incentives

R Square value of 0.138 indicates that tax incentives explain 13.8% of the variance in the dependent variable which is performance of SMEs implying that while the model is statistically significant ( $p$ -value  $<.001$ ), only a small portion of variability in performance of SME is explained by tax incentives.

The findings above address objective three and suggest that tax incentives have a significant effect on the performance of SMEs.

#### 4.8 Empirical findings on the relationship between taxation on the performance of selected SMEs in Nakawa Division.

The fourth study objective was to assess the relationship between taxation on the SME performance in Nakawa Division.

**Table 15: Relationship between taxation and performance of SMEs**

Statements	SD%	D%	N%	A%	SA%	Mean	Std.
Taxation has an influence on the overall financial performance of businesses.	1(0.4)	5(2.1)	12(5.0)	155(64.6)	67(27.9)	4.18	0.65
The current tax rates affect the profitability of my business.	0(0.0)	5(2.1)	11(4.6)	114(47.5)	110(45.8)	4.37	0.67
Businesses allocate a significant amount of resources to meet tax obligations.	1(0.4)	4(1.7)	36(15.0)	106(44.2)	93(38.8)	4.19	0.78
Tax rates affect the pricing and affordability of my products or services.	0(0.0)	2(0.8)	22(9.2)	144(60.0)	72(30.0)	4.19	0.62
Taxation influences the amount of available capital for reinvestment in my business.	0(0.0)	14(5.8)	28(11.7)	113(47.1)	85(35.4)	4.12	0.83
Taxation has an impact on the long-term growth prospects of my business.	0(0.0)	4(1.7)	22(9.2)	140(58.3)	74(30.8)	4.18	0.66
Overall, taxation has a significant impact on the performance and growth of SMEs.	1(0.4)	0(0.0)	13(5.4)	116(48.3)	110(45.8)	4.39	0.63

*Where SD= Strongly Disagree, D=Disagree, N=Neutral, A=Agree, SA=Strongly Agree.*

Results from Table 15 show that majority of the respondents agreed that taxation has an influence on the overall financial performance of businesses, 0.4% Strongly Disagreed, 2.1% Disagreed, 5.0% were not sure, majority agreed with 64.6% Agreed, 27.9% Strongly Agreed with a mean of 4.18 and a low standard deviation of 0.65. Most of the respondents (Mean=4.37, Std=0.67) agreed that the current tax rates affect the profitability of business. Regarding the statement, 2.1% Disagreed,

4.6% were Neutral, 47.5% Agreed and 45.8% Strongly Agreed. Regarding this, Respondent 8 had this to say, *“Taxation has increased operational costs which affects cash flow and profitability. However, we try to comply to avoid penalties”*. Respondent 7 added, *“High taxes have caused us to also increase the prices and this has resulted into reduced sales in the company hence reduced profits”*. The results show that a significant majority agree that tax rates affect profitability and performance of SMEs. Taxation influences operational cost and reinvestment capacity of businesses thus limiting business expansion and profit margins. Excessive tax rates reduce competitiveness of SMEs due to the struggle to balance other operational costs with tax compliance costs (Mayanja, 2020).

On the statement of *“Tax rates affect the pricing and affordability of my products or services.”*, 0.8% Disagreed, 9.2% were Neutral or not sure, 60.0% Agreed and 30.0% Strongly Agreed. A mean score of 4.19 and a very low standard deviation of 0.62 was realized. A significant majority of respondents agreed that tax rates affect the pricing and profitability of taxes. The tax rate influence prices set on services and products as businesses try to accommodate taxation compliance costs. This leads to increase in prices and reduced demand thereby affecting sales in the business and overall performance (Ssabavuma, 2024).

Results on whether businesses allocate a significant amount of resources to meet tax obligations revealed that 38.8% Strongly Agreed, 44.2% Agreed, 15.0% were Neutral, 1.7% Disagreed and 0.4% Strongly Disagreed with a mean score of 4.19 and a standard deviation of 0.78. The results show that the majority of the respondents affirmed that indeed businesses allocate a significant amount of resources to meet tax obligations. This aligns with other scholars who also found that SMEs use a considerable portion of their resources to cater for tax obligations. The costs include administrative costs, tax payments and consultation costs for those that use third parties to better understand taxation (Ahumuza, Kobusingye & Arinaitwe, 2025; Ahumuza & Arinaitwe, 2023).

On the statement of *“Tax rates affect the pricing and affordability of my products or services.”*, 0.8% Disagreed, 9.2% were Neutral or not sure, 60.0% Agreed and 30.0% Strongly Agreed. A mean score of 4.19 and a very low standard deviation of 0.62 was realized. A significant majority of respondents agreed that tax rates affect the pricing and profitability of taxes. The tax rate influence prices set on services and products as businesses try to accommodate taxation

compliance costs. This leads to increase in prices and reduced demand thereby affecting sales in the business and overall performance (Ssabavuma, 2024).

On whether taxation influences the amount of available capital for reinvestment in SMEs, 5.8% Disagreed, 11.7% were not sure, 47.1% Agreed and 35.4% Strongly Agreed with a mean of 4.12 and a standard deviation of 0.83. Regarding this, respondents commented, *“Taxation has negatively influenced my ability to invest and reinvest. The system is not favorable; corruption is ever increasing while the taxes themselves are too high”*. Per Respondent 2. Another respondent added, *“.....however much taxes are important for the grow of the nation/GDP, the taxes that are imposed to us are not normal. The government should revise these taxes again because they do not favor investment”*. Per Respondent 6. Respondent 2 also had this to say, *“Taxation has influenced our business in a way that we invest less capital than we would have invested if we were not paying all that much taxes”*. The results show that the majority of the respondents agree that taxation influences the amount of capital available for reinvestment in SMEs. Increased tax rates increase s the operation costs of the business reducing net profits and limiting funds available for reinvestment therefore negatively affecting expansion and growth (Ssabavuma, 2024).

When asked if taxation has an impact on the long-term growth prospects of businesses, 1.7% Disagreed, 9.2% were neutral while a high percentage of 58.3% Agreed and 30.8% Strongly Agreed. The statement was rated with a mean of 4.18 and a very low standard deviation of 0.66. The data reveals that a substantial majority of respondents (89.1%) perceive taxation as having a significant impact on the long-term growth prospects of their businesses. This aligns with empirical evidence as a study on impact of taxation on SMEs in Nigeria also found that excessive taxation hinders long-term growth as it diminishes internal funds thereby reducing output and productivity (Olayeye, 2025). The complex tax system also imposes additional compliance cost burden diverting resources from the business impacting long-term growth (OECD, 2022).

Regarding the statement, *“Overall, taxation has a significant impact on the performance and growth of SMEs”*, 0.4% Strongly Disagreed, 5.4% were not sure, 48.3% Agreed and 45.8% Strongly Agreed. A mean score of 4.39 and a low standard deviation of 0.63 confirmed the statement. The results indicate that an overwhelming majority of respondents (94.1%) perceive taxation as having a significant impact on the performance and growth of small and medium-sized

enterprises. Studies that align with the findings show that taxation affects financial performance of businesses, innovation, limits growth and expansion, imposes compliance and administrative burden (Ssabavuma, 2024).

**Table 16: Pearson correlation of taxation and performance of SMEs**

		Mean performance of selected SMEs	Taxation
<b>Mean performance of SMEs</b>	Pearson Correlation	1	.506**
	Sig. (2-tailed)		<.001
	N	240	240
<b>Taxation</b>	Pearson Correlation	.506**	1
	Sig. (2-tailed)	<.001	
	N	240	240

\*\*Correlation is significant at the 0.01 level (2-tailed).

Pearson Correlation Coefficient of 0.506 indicates a moderate to strong positive relationship between taxation and performance of SMEs suggesting that changes in taxation (tax rates, incentives, knowledge about taxation) is associated with corresponding changes in performance of SMEs. P-value of less than 0.001 indicates that the relationship is statistically significant indicating that taxation plays a substantial role in influencing the performance of SMEs (Irumba, 2023).

**Table 17: Model Summary for overall taxation and performance of selected SMEs**

Model	R	R Square	Adjusted R Square	Sig. F Change
1	.506 <sup>a</sup>	.256	.253	<.001

a. Predictors: (Constant), Taxation

R Square value of 0.256 indicates that 25.6% of the variance in performance of SMEs is explained by taxation meaning that taxation accounts for one-fourth of the differences in performance of SMEs. The results suggest that taxation is an important factor in explaining performance of SMEs

but not the sole determinant as 74.4% of the variance is influenced by other factors not captured in the model.

These findings above address Objective Four and suggest a multidimensional relationship where the tax variables (tax rates and tax incentives) jointly shape SME outcomes.

## **CHAPTER FIVE: CONCLUSION AND RECOMMENDATIONS**

### **5.1 Conclusions**

This study examined the impact of taxation on the performance of selected Small and Medium Enterprises (SMEs) in Nakawa Division, Kampala District. The findings are consistent with existing literature, which highlights a significant relationship between taxation and SME performance. Below are more specific conclusions based on the research objectives.

#### **5.1.1 Knowledge of selected SMEs regarding taxation**

The overall mean score for selected SMEs' knowledge of taxation was 3.24, indicating a moderate level of awareness. This reflects a partial understanding of tax-related matters, with notable gaps in comprehension of tax laws and regulations. The study concludes that many SMEs face challenges in navigating complex tax frameworks and often miss out on available benefits, contributing to widespread non-compliance. To bridge this knowledge gap, it is recommended that financial institutions and business associations collaborate to provide continuous tax education and advisory services to SMEs. Strengthening tax literacy will empower business owners to make informed financial decisions, thereby enhancing overall business performance.

#### **5.1.2 Effect of tax rates on selected SME performance**

The findings of this study indicate a significant and moderately positive relationship between tax rates and the performance of selected SMEs. It is concluded that tax rates play a critical role in influencing SME performance where higher or unfavorable rates may impede growth, while favorable rates can enhance profitability and sustainability. However, the moderate strength of the correlation also suggests that other factors, such as market conditions and access to capital, equally contribute to the overall performance of SMEs.

#### **5.1.3 Effects of Tax incentives on performance of selected SMEs**

The results of this study indicate that tax incentives have a moderately positive and statistically significant relationship with the performance of selected SMEs, as demonstrated by the correlation analysis ( $r=0.375$ ,  $p<0.001$ ). The researcher therefore concluded that tax incentives contribute

positively to an enhanced performance of SMEs, however, their effect is not strong because of under usage and accessibility to these incentives remain a challenge for some businesses limiting their effectiveness as majority of respondents admitted to applying for the tax incentives only 1-2 times in the past year. The under usage is also because only big taxpayers get to enjoy them compared to small businesses that do not pay many taxes. Other factors such as lack of awareness and eligibility constraints also make businesses not to fully utilize the tax incentives. This therefore calls for creating awareness through awareness campaigns and policy improvements so that SMEs can fully benefit from the available tax relief measures.

## **5.2 Recommendations**

Taxation has a significant impact on the performance of SMEs, influencing key aspects such as profitability, investment decisions and financial stability. The study revealed that limited awareness and understanding of taxation, including tax rates and available incentives, present major challenges to the growth and success of SMEs. Based on these findings, the following recommendations are presented, aligned with each research objective.

### **5.2.1 Knowledge of taxation**

- a) The Uganda Revenue Authority (URA) should expand its Taxpayer Education Program to include a targeted SME education track. This should focus on practical aspects of Uganda's tax system, such as presumptive tax, VAT registration thresholds, withholding tax obligations and how to access incentives under the Income Tax Act. Outreach can be delivered via regional URA offices, local government forums, and digital platforms, including *eTax* and *URA TV*.
- b) URA, in partnership with the Uganda Registration Services Bureau (URSB), should require new SMEs to undergo a short, basic tax orientation as part of the registration process. This training should introduce registrants to URA's *eTax portal*, tax identification number (TIN) application and basic obligations under the Income Tax Act and VAT Act. This will enhance early-stage compliance and reduce the risk of future penalties or non-filing.

- c) URA and the Ministry of Finance, Planning and Economic Development (MoFPED) should formalize partnerships with associations like the Uganda Small Scale Industries Association (USSIA), Uganda Manufacturers Association (UMA) and private sector foundations to deliver localized tax clinics. These partnerships should offer continuous advisory services, mentorship on filing returns, and access to URA’s mobile services—especially in underserved districts.
- d) URA should review and simplify tax guidance documents to reflect the language and comprehension levels of micro and small enterprise operators. Core documents such as the Presumptive Tax Guide, VAT compliance guidelines, and Taxpayer Rights and Obligations should be translated into major local languages (e.g., Luganda, Runyankole, Ateso, Luo) and disseminated through RDC offices, SACCOs, and community radios to enhance inclusive understanding.

### **5.2.2 Tax rates**

- a) The Government of Uganda, through the Uganda Revenue Authority (URA) and Ministry of Finance, Planning and Economic Development (MoFPED), should review the current presumptive tax regime and VAT threshold structure. Specifically, consideration should be given to reducing the VAT rate for SMEs with annual turnovers below UGX 150 million from 18% to 12%, or exempting qualifying SMEs under a refined category. This would ease cash flow constraints, increase working capital for business growth and incentivize formalization.
- b) Tax authorities should implement predictable tax policy changes by providing advance public notice and justification for any rate revisions. This includes publishing policy briefs and conducting stakeholder dialogues at least one fiscal quarter before implementing new tax rates. Such measures will promote transparency, reduce uncertainty, and allow SMEs to plan and budget effectively.
- c) URA, in partnership with MoFPED and the Uganda Bureau of Statistics (UBOS), should conduct regular tax incidence and impact assessments to evaluate how tax rate changes affect SME growth, competitiveness, and sustainability. These

assessments should inform the design of targeted tax instruments that promote inclusive growth, especially in priority sectors such as agribusiness, ICT and manufacturing.

### 5.2.3 Tax Incentives

- a) The Government, through the Ministry of Finance and URA, should enhance sector-specific tax incentives tailored to the unique needs of SMEs across industries. By aligning incentives with national priorities (e.g., agro-processing, ICT, manufacturing) and taking into account sector-specific constraints, the policy will promote targeted growth and encourage investment in key areas of the economy.
- b) URA should establish an automated SME tax incentive portal integrated with the *eTax* system, where businesses with strong compliance records (e.g., timely filings, consistent TIN usage) are auto-assessed and rewarded through credits, deferrals, or rebates. This will foster a compliance-driven incentive culture among SMEs.
- c) Introduce a graduated incentive model where start-ups and early-stage SMEs enjoy higher exemptions and deferrals while mature businesses benefit from scaled-down reliefs. This progressive approach ensures that small enterprises retain capital for reinvestment during their most vulnerable growth stages.
- d) MoFPED, in partnership with URA and UBOS, should develop an online monitoring and evaluation dashboard to track SME utilization of tax incentives. This system should collect data on business growth, employment generation, and reinvestment, enabling evidence-based refinement of incentive policy over time.
- e) URA should collaborate with SME support networks such as USSIA, PSFU and regional business hubs to conduct quarterly awareness workshops on available tax incentives, eligibility requirements and application procedures. These engagements will bridge the information gap and increase uptake among qualified SME
- f) Tax authorities should simplify the application process for accessing tax incentives for SMEs. This recommendation is based on the study's finding that the majority of

respondents held certificates or had only secondary-level education. URA should simplify the application process for tax incentives by using visual forms, translated guides, and user-friendly interfaces. Introducing *in-person helpdesks at district URA offices* and multilingual chatbots will ensure inclusive access to incentive schemes for all entrepreneurs.

### **5.3 Suggestions for future research**

The study investigated the effect of taxation on SME performance however; several gaps and emerging issues call for deeper research to be done. The following areas can be researched by other researchers to explore further the connection between taxation and the performance of SMEs.

- a) A sectoral comparison of tax policies could help identify the unique impact of taxation on different industries. Such research would offer insights into how tax obligations affect SMEs operating in, for example, agriculture, manufacturing, ICT, or retail, and inform sector-specific tax reforms.
- b) Further studies should examine how the costs associated with tax compliance such as filing returns, hiring accountants or legal professionals, and adhering to regulatory requirements affect SME profitability, operational efficiency, and long-term sustainability.

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Appendix 1: Morgan and Krejcie table

<b>N</b>	<b>S</b>	<b>N</b>	<b>S</b>	<b>N</b>	<b>S</b>	<b>N</b>	<b>S</b>	<b>N</b>	<b>S</b>
10	10	100	80	280	162	800	260	2800	338
15	14	110	86	290	165	850	265	3000	341
20	19	120	92	300	169	900	269	3500	246
25	24	130	97	320	175	950	274	4000	351
30	26	140	103	340	181	1000	276	4500	351
35	32	150	108	360	186	1100	285	5000	357
40	36	160	113	380	181	1200	291	6000	361
45	40	180	118	400	196	1300	297	7000	364
50	44	190	123	420	201	1400	302	8000	367
55	48	200	127	440	205	1500	306	9000	368
60	52	210	132	460	210	1600	310	10000	373
65	56	220	136	480	214	1700	313	15000	375
70	59	230	140	500	217	1800	317	20000	377
75	63	240	144	550	225	1900	320	30000	379
80	66	250	148	600	234	2000	322	40000	380
85	70	260	152	650	242	2200	327	50000	381
90	73	270	155	700	248	2400	331	75000	382
95	76	270	159	750	256	2600	335	100000	384
<p>Note: "N" is Population Size          "S" is Sample Size.</p>									