DECLARATION

This research project is my original work and has not been presented for a degree in any other University.

Signature __________________ Date 3/12/2012

Mokua Nyandieka Kenyanya
BA Economics (Major), University of Nairobi
Reg. No: K102//21217/2010

This research project has been submitted for examination with our approval as University supervisors.

Signature __________________ Date 3/12/12

Dr. James Maingi
Department of Applied Economics
Kenyatta University
Nairobi, Kenya

Signature __________________ Date 3/12/2012

Dr. Jennifer Njaramba
Department of Econometrics and Statistics
Kenyatta University
Nairobi, Kenya
ABSTRACT

The implementation of the Kenya vision 2030, coupled with financing expenditures under the devolved government in the new constitution requires enormous resources. The vision requires the government to ensure that the bulk of its expenditures are met from tax revenue and that overall expenditure should be controlled to ensure stable macroeconomic environment. The Government of Kenya continued to carry out tax reforms over the years with an aim of improving taxation efficiency and increasing the amount of revenue raised to finance the ever raising government expenditure. Despite the continuous tax reforms since 1986, the envisaged improvement on tax productivity to Gross Domestic Product Ratio of 28 percent has not been achieved. This study sought to investigate the impact of the reforms that have been undertaken in Income tax, Excise duty, Import duty and sales/Value Added tax on revenue productivity. Income tax is levied on individual and corporate incomes thus as the economy keep expanding the contribution of this category of tax to revenue is bound to increase, assuming the reforms are aimed at broadening the tax base. Similarly, Value Added tax is a consumption tax charged on both local sales and importation, as opposed to import duty, which is levied on the value of imports. Excise duty is levied selectively on particular goods and services. Compared to Import and Excise duties, Value Added tax has more potential to increase revenue through reforms aimed at increasing consumption spending in Kenya. The specific objective of this study therefore was to estimate the effect of tax reforms on buoyancy of Income tax and Value Added tax, as well as estimating the effect of the reforms on elasticities of the tax system. The study was guided by the Tax Modernization Programme of 1986 and the Kenya Vision 2030. Published secondary data was used to analyze the relationship between tax reforms and revenue productivity and before, after piecemeal/policy and during the comprehensive reform buoyancy and elasticities were estimated using regression analysis. The regression result showed that total tax in Kenya was inelastic during the three periods, but it was buoyant during the pre-reform and piecemeal reform periods. The study also showed that the reforms had a positive impact on productivity of income tax, but did not have a positive impact on productivity of Value Added Tax. The positive of reform on the productivity of income tax was as a result of the relative effectiveness of income tax reform that made the tax system simpler and reduced avenues for evasion and corruption, whereas the low elasticity of value added tax might have been caused by tax evasion and collusion between the tax collectors and tax payers. In spite of the good performance of income tax as a result of reforms, further reform needs to be done particularly on the inelastic value added tax. These reforms include: reduction of rates and exemptions, increasing the number of tax collectors, imposing tougher penalties for those found guilty of evasion, strengthening audit skills, taxation of absentee landlords and income from rental houses.