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Original Article

### The Influence of Trust on Voluntary Tax Compliance in Tanzania: A Case of Small Enterprises

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#### Date Published: ABSTRACT

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#### Keywords:

Trust,  
Voluntary Tax  
Compliance,  
Small  
Enterprise.

The study assessed the influence of trust on voluntary tax compliance from a small enterprise perspective. The study integrated both institutional trust and interpersonal trust in the hypothesized model. The study employed a quantitative approach along with an explanatory research strategy. Data were collected from 100 conveniently selected owners of small enterprises using structured questionnaires. Structural Equation Modeling (SEM) was used for data analysis whereas Smart PLS 4.0 served as a statistical tool for analysis. The results from SEM indicated that institutional trust has a statistically significant influence on voluntary tax compliance among small enterprises. Also, the results indicated that institutional trust mediates the influence of interpersonal trust on voluntary tax compliance among small enterprises. Furthermore, the total effect results from SEM indicated that interpersonal trust has a significant influence on voluntary tax compliance among small enterprises. Implicitly, both institutional and interpersonal trusts play a significant role in enhancing voluntary tax compliance among small enterprises. Respondents believe that their voluntary tax compliance would increase if they had trust-based relationships with officials and tax authorities. Therefore, in order for the tax authority to enhance voluntary compliance behaviour, it is vital to focus on tax administration strategies that would build, enhance and sustain the trustworthiness of organizations and officials to ensure sustainable domestic revenue for socio-economic development.

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## INTRODUCTION

Voluntary tax compliance offers the potential for revenue authorities to effectively mobilize domestic revenues. Hence, there is a need to enhance voluntary tax compliance, particularly in developing countries where non-compliance, weak administration systems and corruption challenges remain a big challenge and much worse compared to developed countries; (OECD, 2022; Al-ttaffi & Abdul-Jabbar, 2016; McKerchar & Evans, 2009) Furthermore, Gebrihet (2023) argues that in a democratic society, trust is a cornerstone for effective tax administration.

In an environment where full enforcement to all taxpayers is limited due to scarcity of administrative resources, inadequate tax administration systems and corruption challenges, the enhancement of voluntary tax compliance is never an option (McKerchar & Evans, 2009). Coercive measures have failed to ensure sustainability in domestic revenue mobilization in many countries particularly in developing countries; when there is voluntary tax compliance, fewer resources will be allocated to enforcement mechanisms, resulting in cost savings and optimal utilization of resources in tax administrations and sustainability in public financing (OECD, 2022; Faizal et al., 2017; Schaltegger & Torgler, 2008).

As an obligation-based relationship, the enforced compliance approach fails to enable governments to achieve higher tax compliance, and hence it undermines the ability to meet public goods; furthermore, the harsh enforcement mechanisms tend to damage the legitimacy of revenue authorities before taxpayers, forcing them to be more resistant (Kira, 2017; Andreas & Savitri, 2015; Levin, 2005). Non-deterrence approach is considered to be more

effective in boosting tax compliance than the enforced approach (Mascagni et al., 2017; Fjeldstad et al., 2018).

Trust-based relationship is considered to be one of the key and potential drivers of taxpayers' voluntary compliance; trust in the tax authority enhances voluntary tax compliance and vice versa (OECD, 2022; Faizal et al., 2017; Muehlbacher et al., 2011; Wahl et al., 2010). It is further argued that building trust as a component of the quality of the relationship between tax authorities and taxpayers is vital in promoting voluntary tax compliance in any tax system; since, the sustainable relationship between taxpayers and revenue authorities relies on the existence of trust (OECD, 2022; Faizal et al., 2017). Trust is one of the main elements of social capital which facilitates cooperative actions for mutual benefits; building a sense of partnership between taxpayers and states; hence, they tend to view paying tax as contributing to the state developments (Gebrihet, 2023; Weaver, 2018).

Various studies have found that trust has a significant influence on taxpayers' voluntary tax compliance (Appah and Doubara, 2024; Thomas et al., 2024; Gebrihet, 2023; Kumi et al., 2023). Taxpayers trust the tax authority when they perceive that the authority acts benevolently and conducts its affairs for the common good (Batrancea et al., 2019). When trust exists, taxpayers tend to have confidence in the tax administration system, actions and processes that they will act fairly and honestly for the greater good; consequently, it's their civic duty to pay their taxes; hence promoting voluntary tax compliance (Gebrihet, 2023; Murphy, 2004). Furthermore, Gebrihet, (2023) argues that in a democratic society, trust is a cornerstone for effective tax administration.

Despite the acknowledgement of the role of trust in tax compliance by previous studies; understanding taxpayers' perceptions regarding the influence of trust in voluntary compliance is never enough as it assists tax authority in developing and adjusting timely to its strategies to ensure robust strategies to enhance trust in tax administration are in place to foster voluntary tax compliance among the small taxpayers (Appah and Doubara, 2024; Thomas et al., 2024; Kumi et al., 2023; Faizal et al., 2017). This study assessed the influence of trust as a significant driver of voluntary tax compliance from small taxpayers' perspectives as they constitute a substantial part of the economy (URT, 2012). Usually, in developing countries, small enterprises are characterized by cash-based transactions, informalities and high mobility, attributes that can erode the country's tax base; making voluntary tax compliance among such taxpayers vital to improve domestic revenue mobilization and meeting public financing.

Recently, trends in tax administration reforms have shifted paradigms from demanding compliance from taxpayers to building and valuing a sustainable relationship between tax authorities and taxpayers as a tool to boost voluntary tax compliance (Faizal et al., 2017; Mustapha, 2017). As part of tax administration reforms, in July 2022 the Tanzania Revenue Authority (TRA) launched its sixth Corporate Plan (CP6) which embraces trust as one of the key drivers for sustainable domestic revenue mobilization. TRA aspires to be "*A Trusted Revenue Administration for Socio-Economic Development*" with trustworthiness as an additional core value to what existed in the fifth corporate plan (CP5). This reform embraces a non-deterrence mechanism in promoting voluntary tax compliance through building trust-based relationships between the authority and taxpayers to ensure sustainable domestic revenue mobilization. According to Sapienza (2021), trust in public institutions like TRA is a necessary condition for just and sustainable development especially where citizens' compliance is required.

As much as institutional trust is highly promoted in relation to tax compliance, the role of interpersonal trust in tax administration cannot be ignored. The way tax officials treat and interact with taxpayers has an impact on taxpayer's compliance behaviour (Nurhayati et al., 2015). When taxpayers perceive there is a trust-based relationship with the officials that they directly contact and interact with; they are likely to have confidence in, their actions, decisions and tax administration systems; and hence, promote voluntary tax compliance (Susuwa et al., 2020; Nurhayati et al., 2015; Doney & Cannon, 1997).

Further, officials in an organization play a significant role in building and fostering of trustworthiness of the organization through their actions and integrity; it is almost impossible to have a trusted organization without having a trust-based relationship between officials and stakeholders (Shockley-Zalabak et al., 2000; Doney & Cannon, 1997). That means the interpersonal trust between taxpayers and tax officials is likely to affect taxpayers' compliance behaviour; and how taxpayers view the trustworthiness of the tax authority. Therefore, this study aimed to assess how trust influences voluntary tax compliance among small enterprises by integrating the interpersonal and institutional dimensions of trust in a comprehensive manner instead of studying them in isolation.

## THEORETICAL REVIEW

### Theory of Slippery Slope Framework of Tax Compliance

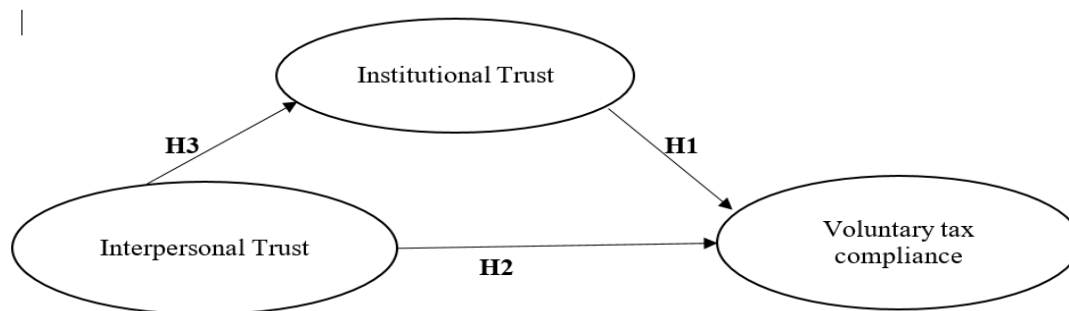
The study was guided by the slippery slope framework of tax compliance by Kirchler et al., (2008) which consists of three dimensions; trust in tax authorities, power of tax authorities and tax compliance. According to the framework, tax compliance can be influenced by both power and trust in tax authorities, the higher the trust, the higher the voluntary tax compliance; the higher the power, the higher the enforced tax compliance (Wahl et al., 2010). This theory supports the

argument that trust has a significant influence in determining tax compliance behaviour. As a modification to the slippery slope theory, interpersonal trust was added as an independent variable in this study and its impact on voluntary tax compliance and mediating effect on trust in tax authority were assessed.

### Conceptual Framework

From the modified theory of the slippery slope of tax compliance, the conceptual framework for this study was developed. The study assessed how institutional trust (IT) influences voluntary tax compliance (VC) as well as the mediating effect of IT on the relationship between interpersonal trust (PT) and voluntary tax compliance (VC). Furthermore, the study investigated the direct influence of interpersonal trust (IT) on voluntary tax compliance (VC).

**Figure 1: Structural Model**



On the basis of the above conceptual framework and aforementioned constructs, hypotheses were formulated as follows:

*H1: Institutional trust influences voluntary tax compliance among small enterprises*

*H2: Interpersonal trust influences voluntary tax compliance among small enterprises*

*H3: Institutional trust mediates the influence of interpersonal trust on voluntary tax compliance*

### RESEARCH METHODOLOGY

This study employed an explanatory research strategy which sought to understand the relationship between variables with a quantitative approach to obtain small enterprises' responses on the influence of trust in voluntary tax compliance in Tanzania. Data were collected using structured questionnaires distributed to a conveniently selected sample size of 100 owners of small enterprises as suggested minimum sample size by various studies (Hair et al.,

2014; Wolf et al., 2013). The sample size of 100 observations is considered to be a preferable minimum number when running structural equation modelling in a basic model which has less than five constructs to maintain the ability to detect the hypothesized relationship (Hair et al., 2014; Wolf et al., 2013). The Partial Least Square Structural Equation Modeling (PLS-SEM) is a non-parametric technique that can be used even when the sample size is limited (Hair et al., 2014). The perspectives from small enterprises were measured using a 5-point Likert scale to determine the level of agreement with the ordinal statements with 1 equal to strongly disagree, 2 equal to disagree, 3 equal to neutral, 4 equal to agree and 5 equal to strongly agree. A total of 21 statements were grouped under Interpersonal Trust, Institutional Trust and Voluntary tax compliance. The study assessed the influence of trust on voluntary tax compliance among small enterprises by integrating the institutional and interpersonal dimensions of trust.

The data analysis was done by using Smart PLS 4.1.0.8 4 software (Ringle et al., 2024). According to Sarstedt et al., (2017) when PLS-SEM is used, Measurement model analysis should be conducted before the Structural Model Analysis.

## FINDINGS AND DISCUSSION

### Measurement Model Analysis Results:

#### *Reliability and Validity Tests*

Cronbach's alpha and composite reliability were employed to check the reliability of the data. In this model, Cronbach's alpha values were above the recommended threshold of 0.7 confirming the reliability of data (Taber, 2017). The composite

reliability values for all constructs were above 0.8, showing there is a satisfactory internal consistency. The value of Average Variance Extracted (AVE) for all constructs was above 0.5 suggesting that convergent validity is satisfactory and acceptable. Furthermore, discriminant validity was assessed using the Fornell-Larcker Criterion; this was done by comparing the loadings of the construct and other constructs; in which the value should be greater than the value of loading of other constructs. The discriminant validity was also assessed by the Heterotrait-Monotrait Ratio (HTMT). In this hypothesized model the values were below the threshold of 0.9 (Henseler et al., 2015). Hence, the discriminant validity was confirmed.

**Table 1: Loadings, Reliability and Validity Results**

	Cronbach's alpha	Composite reliability (rho_a)	Composite reliability (rho_c)	Average variance extracted (AVE)
<b>Voluntary Tax Compliance</b>	0.917	0.921	0.933	0.666
<b>Institutional Trust</b>	0.944	0.947	0.954	0.749
<b>Interpersonal Trust</b>	0.944	0.947	0.954	0.750

**Table 2: Fornell-Larcker Criterion**

	Compliance	Institutional Trust	Interpersonal Trust
<b>Voluntary Tax Compliance</b>	<b>0.816</b>		
<b>Institutional Trust</b>	0.439	<b>0.865</b>	
<b>Interpersonal Trust</b>	0.240	0.680	<b>0.866</b>

\*The bolded values represent the square root of AVE

**Table 3: Heterotrait- Monotrait Ratio of Correlations**

	Compliance	Institutional Trust	Interpersonal Trust
<b>Voluntary Tax Compliance</b>			
<b>Institutional Trust</b>	0.467		
<b>Interpersonal Trust</b>	0.258	0.717	

#### *Multicollinearity Test Results*

The Variance Inflation Factor (VIF) was used to check for the multicollinearity between the independent variables. Multicollinearity occurs when there is a high correlation among independent variables. The results indicated that the VIF statistic

is less than the cut-off threshold of 10 suggested by Hair et al. (2014). Hence, there was no multicollinearity in both measurement and structural models as indicated by values in Tables 4 and 5 below.



**Table 4: Multicollinearity Test Results for Measurement Model**

Items	VIF
IT1: Tax officials treat taxpayers in a respectful manner and they can be trusted	2.555
IT2: I believe tax officials have the ability to deliver promised service dependably	4.563
IT3: Tax officials make taxpayers feel safe in their business activities.	4.506
IT4: Tax officials provide excellent services in tax administration	5.045
IT5: Tax officials' employees possess the required customer care	4.045
IT6: Tax officials pay individual attention to taxpayers' challenges and enquiries	5.692
IT7: I can talk freely to tax officials about tax challenges and know that they will want to listen	4.454
PT1: TRA has a good relationship with taxpayers which inspires voluntary compliance	3.175
PT2: I encounter good 'word of mouth' about TRA from other taxpayers	2.330
PT3: I have good feelings when reaching TRA offices to fulfil my tax obligations	2.699
PT4: TRA has good credibility in handling tax affairs which inspires voluntary compliance	4.121
PT5: TRA systems are transparent in tax assessment	5.113
PT6: I trust that TRA acts in the best interests of my business	6.872
PT7: I trust TRA to handle my tax affairs honestly	4.847
VC1: I settle my tax obligations without being forced (willfully) since assessments are fair	2.324
VC2: I settle my tax obligations immediately after they become due	3.438
VC3: I should honestly declare all incomes in my tax returns	2.874
VC4: There is fairness in tax assessments hence I can disclose all my incomes correctly	2.690
VC5: I know it is important to disclose all the incomes I generate	2.745
VC6: It is important to submit tax returns on or before the due date	2.945
VC7: I submit tax returns and payments after I'm satisfied with my issued tax assessments	3.625

**Table 5: Multicollinearity Test Results for Structural Model**

	VIF
<b>Institutional Trust -&gt; Voluntary Tax Compliance</b>	1.859
<b>Interpersonal Trust -&gt; Voluntary Tax Compliance</b>	1.859
<b>Interpersonal Trust -&gt; Institutional Trust</b>	1.000

The values above indicate that data reliability and validity were satisfactory suggesting the measurement model used is fit and valid. Hence, justified structural model estimation.

### Structural Model Analysis Results

#### *Coefficient of Determination ( $R^2$ )*

The smart PLS 4 bootstrapping was used to determine the coefficient of determination in this model. Falk and Miller (1992) in Aslam and Amin (2015) argue that the minimum coefficient of

determination ( $R^2$ ) should be 0.10. To establish the predictive relevance of the model made, the study employed the Stone Geisser test ( $Q^2$ ) while applying the Smart PLS blindfolding procedure, whereby, the value of above 0 suggests predictive relevance of the model and vice-versa; the  $Q^2$  values of 0.02, 0.15, and 0.35 indicates that an exogenous variable has a small, medium, or large predictive relevance (Sarstedt et al., 2017). In this hypothesized model both the  $R^2$  and  $Q^2$  values observed in this study are satisfactory.

**Table 6: The R-square and Q-square Values**

	$R^2$	Adjusted $R^2$	$Q^2$
<b>Voluntary Tax Compliance</b>	0.199	0.182	0.038
<b>Institutional Trust</b>	0.462	0.457	0.452

The results in Table 6 and Figure 1 show that interpersonal trust and institutional trust predict voluntary tax compliance among small enterprises; furthermore, institutional trust mediates the relationship between interpersonal trust and voluntary tax compliance.

#### *Significance of Path Coefficients*

#### *Direct Effects*

Path coefficients are used to determine the strength and significance of the relationship between variables in a model. This study employed the Smart PLS 4.0 bootstrapping procedure to assess the direct relationship of variables at 97.5% confidence intervals. Table 7 presents the results:

**Table 7: Results of Path coefficients, standard error, T statistics and P-values**

Hypothesis	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	T statistics ( O/STDEV )	P values	Decision
<b>Institutional Trust -&gt; Voluntary Tax Compliance</b>	0.512	0.532	0.137	3.752	0.000	Supported
<b>Interpersonal Trust -&gt; Voluntary Tax Compliance</b>	-0.108	-0.117	0.156	0.691	0.489	Not supported
<b>Interpersonal Trust -&gt; Institutional Trust</b>	0.680	0.683	0.055	12.379	0.000	Supported

#### *Indirect Effect*

To assess the mediation effect of institutional trust on the relationship between interpersonal trust and

voluntary compliance the study employed the Smart PLS 4.0 bootstrapping procedure at 97.5% confidence intervals. The results are presented below in Table 8.

**Table 8: Results of Path coefficients, standard error, T statistics and P-values**

Hypothesis	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	T statistics ( O/STDEV )	P values	Decision
<b>Interpersonal Trust -&gt; Institutional Trust -&gt; Voluntary Tax Compliance</b>	0.348	0.364	0.102	3.418	0.001	Supported

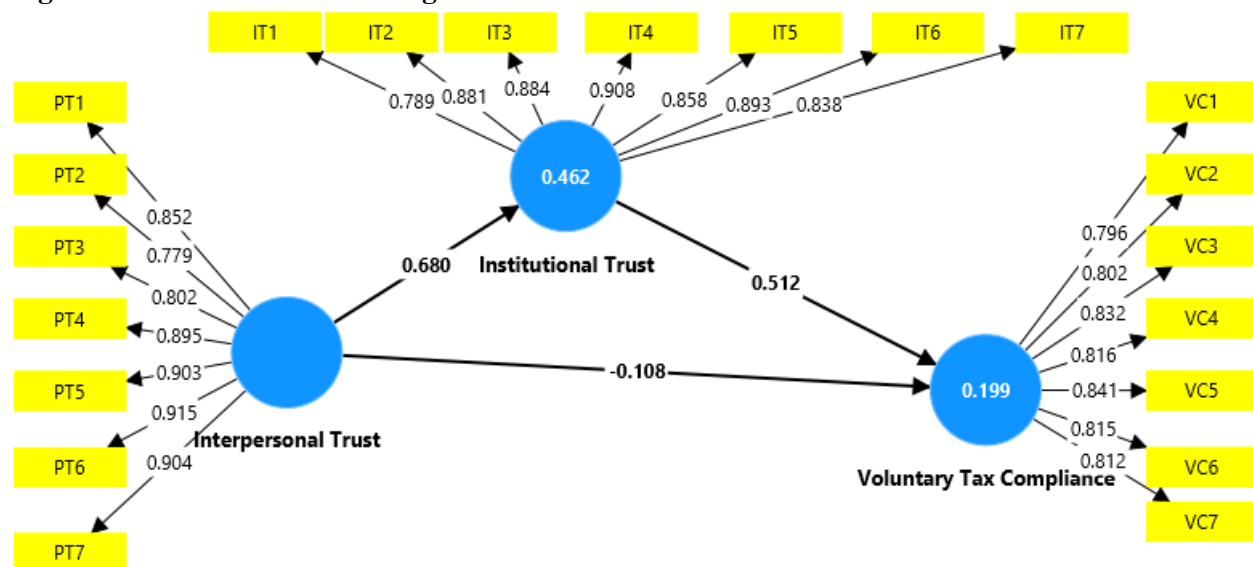
#### *Total Effects*

Subsequently, the study assessed the total effect of variables in the model using the Smart PLS 4.0

bootstrapping procedure at 97.5% confidence intervals. The results are presented below in Table 9.

**Table 9: Results of Path coefficients, standard error, T statistics and P-values**

	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	T statistics ( O/STDEV )	P values	Decision
<b>Institutional Trust -&gt; Voluntary Tax Compliance</b>	0.512	0.532	0.137	3.752	0.000	Supported
<b>Interpersonal Trust -&gt; Voluntary Tax Compliance</b>	0.240	0.247	0.107	2.246	0.025	Supported
<b>Interpersonal Trust -&gt; Institutional Trust</b>	0.680	0.683	0.055	12.379	0.000	Supported

**Figure 1: Results of PLS-SEM algorithm**

## DISCUSSION OF FINDINGS

### H1: Institutional Trust Influences Voluntary Tax Compliance Among Small Enterprises

The direct path coefficient between institutional trust and voluntary tax compliance was supported in this study, hence confirming hypothesis *H1*. The results from Smart PLS 4 confirmed the hypothesis as indicated in Table 7 above (Coefficient=0.512,  $t=3.752$ ,  $P<0.05$ ), suggesting a statistically significant relationship between the trust in tax authority (institutional trust) and voluntary tax compliance among small enterprises. The results are consistent with previous studies (Sapienza, 2021; Kirchler et al., 2008) which found that trust in

public institutions tends to foster compliance among citizens. Also, the results are consistent with the theory of the slippery slope framework of tax compliance which proposes trust in tax authority enhances tax compliance. Impliedly, voluntary tax compliance is enhanced when taxpayers perceive tax authority is trustworthy. Hence, TRA should employ strategies that foster credibility and institutional trust among small enterprises to encourage voluntary tax compliance.

### H2: Interpersonal Trust Influences Voluntary Tax Compliance Among Small Enterprises

The direct path coefficient between interpersonal trust and voluntary tax compliance was not



supported and hence did not confirm hypothesis *H2*; it showed a negative coefficient of -0.108 ( $p > 0.05$ ) suggesting a non-statistically significant inverse relationship between interpersonal trust and voluntary tax compliance contrary to previous studies which suggest a positive relationship (Gebrihet, 2023; Susuwa et al., 2020). However, by considering the total effect (table 9), the relationship between interpersonal trust and voluntary tax compliance was positive and statistically significant at a coefficient of 0.240 ( $p < 0.05$ ) suggesting interpersonal trust influences voluntary tax compliance among small enterprises. These findings indicate there is a complex interaction between interpersonal trust and voluntary tax compliance, suggesting while interpersonal trust can negatively affect voluntary tax compliance, it can enhance compliance through institutional trust. These findings can be supported by the Complacent theory, whereby it is argued that in an environment of high trust people tend to become complacent, feeling less compelled to comply with the formal settings, rules and regulations for both taxpayers and tax officials (Zybak et al., 2016; Doney & Cannon, 1997). Moreover, the findings suggest that the fostering of interpersonal trust between taxpayers and tax officials should be optimal, balanced and governed to avoid negative repercussions on voluntary tax compliance due to reduced vigilance. Hence contributing to the understanding between trust and voluntary tax compliance.

### **H3: Institutional Trust Mediates the Influence of Interpersonal Trust on Voluntary Tax Compliance**

The indirect path coefficient between interpersonal trust and voluntary tax compliance was supported in this study, hence confirming hypothesis *H3*; The results from Smart PLS 4 confirmed the hypothesis as indicated in Table 7 above (Coefficient = 0.348,  $t = 3.418$ ,  $P < 0.05$ ) suggesting that institutional trust mediates the influence of interpersonal trust on voluntary tax compliance among the small

enterprises. The results are consistent with previous studies (Susuwa et al., 2020; Nurhayati et al., 2015) which found that when taxpayers perceive there is a trust-based relationship with the officials that they directly contact and interact with; they are likely to have confidence in tax administration systems which ultimately has an effect on tax compliance.

## **CONCLUSION AND RECOMMENDATION**

The objective of this study was to assess the influence of trust on tax compliance in Tanzania from small enterprises' perspectives. The study integrated both institutional and interpersonal trust as independent variables and voluntary tax compliance as dependent variables. The findings indicated that there is a trust-tax compliance nexus whereby both trust in tax authority (institutional trust) and interpersonal trust could enhance voluntary tax compliance among the small enterprises in Tanzania. Respondents believe that their voluntary tax compliance would increase if they had trust-based relationships with officials and tax authorities. Therefore, the study findings imply that governments particularly in developing countries should focus on tax administration strategies that would build, enhance and sustain trustworthy of tax authorities and tax officials to ensure sustainable domestic revenue collection through voluntary tax compliance for socio-economic development. The findings indicate that both institutional and personal trust plays a significant role in promoting tax compliance among small enterprises.

Theoretically, the model of this study contributes to tax compliance practices; the model can be used by researchers to study the trust-tax compliance nexus hence contributing to the theory of the slippery slope framework of tax compliance which focuses on trust in authority (institutional trust) by incorporating a variable of a personal trust relationship between taxpayers and tax officials as one of the drivers which shape tax compliance behaviour among the small enterprises.

Notwithstanding the contributions offered, the study has some limitations. The study concentrated on the small enterprises perspectives with a minimum sample size; Furthermore, different taxpayers may have different perceptions of what constitutes a trust-based relationship; hence, the results may not be generalized due to the focus on small enterprises only, limiting interpretations to such a group of respondents. Future studies may take into consideration other categories of taxpayers with larger sample sizes.

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