

# The Influence of Penalties on the Tax Compliance Behaviour of Small Business Owners

**Mphagahlele O. Ndlovu**

<https://orcid.org/0000-0003-4850-8834>

University of South Africa

[ndlovmo@unisa.ac.za](mailto:ndlovmo@unisa.ac.za)

**Daniel P. Schutte**

<https://orcid.org/0000-0001-7283-247X>

North-West University, South Africa

[danie.schutte@nwu.ac.za](mailto:danie.schutte@nwu.ac.za)

## Abstract

**Purpose:** The purpose of this study was to investigate the influence of penalties on the tax compliance behaviour of small business owners.

**Research design:** This study employed a qualitative research approach. An interpretive phenomenological research approach underpinned the study design. The study utilised semi-structured interviews to explore the lived experiences of small business owners in Gauteng, which is the business hub of South Africa.

**Findings:** The findings indicate that to an extent, penalties do encourage small business owners to pay taxes on time. However, the charging of substantial penalties has the potential to discourage small business owners from registering at all for taxes. Furthermore, non-compliance is often a result of cash flow challenges, in which case the penalties become an unavoidable cost of doing business. A lack of skills and basic tax knowledge lead to unintentional non-compliance; therefore, the penalties must be accompanied by training, awareness and education.

**Originality/Value:** There are conflicting results on the influence of penalties on tax compliance behaviour in the literature. This study contributes to the body of knowledge by adding a South African small business perspective. Furthermore, the qualitative approach applied in this study adds to the body of knowledge and provides original contextual descriptions of the lived experiences regarding the influence of penalties on the tax compliance phenomenon.

**Keywords:** interpretive phenomenology; small business owners; small and medium enterprise taxation; South Africa; tax penalty



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## Introduction

Taxation is the major source of revenue for governments around the world (Adams 2001; Afubero and Okoye 2014; SARS 2021a). It provides the means for governments to deliver public services, invest in development and cater to the needs of the most vulnerable in society (Sadress et al. 2019). Small businesses are essential players in a country's tax system (Kamleitner, Korunka and Kirchler 2012; Schutte and Van der Zwan 2019). Small businesses act as agents for tax authorities in collecting Value Added Tax (VAT) and payroll taxes from their clients and employees. In this regard, during the 2020/21 fiscal year, small businesses remitted VAT payments worth R37 billion over to the South African Revenue Service (SARS 2021b). The Small, Medium and Micro Enterprise (SMME) sector provides employment to over 10 million people in South Africa (SEDA 2020). The small businesses are therefore expected to remit payroll taxes on behalf of these employees to SARS. Furthermore, a total number of 123 461 Small Business Corporations (SBC), with an annual turnover not exceeding R20 million, were assessed for a total tax amount of R2.3 billion (SARS 2021b). The R2.3 billion figure excludes taxes from many more small businesses that may not necessarily meet the requirements to be classified as an SBC in terms of Section 12E of the Income Tax Act (ITA) No. 58 of 1962 (RSA 1962).

Taxation is an unreciprocated payment since the benefits received from the government are not in direct proportion to the payments made (Swistak 2016). As the perceived benefits, in the form of public services, is inconsistent, taxpayers may resist the act of paying taxes (Swistak 2016). The level of resistance of taxpayers will also be influenced by the perceived efficiency of government spending (OECD 2013; Torgler 2006; Vythelingum, Soondram and Jugurnath 2017).

South Africa has entered an era where there is a trust deficiency between the state and taxpayers. The Judicial Commission of Inquiry into State Capture Reports laid bare the weaknesses of the state when it comes to the efficient utilisation of tax money (RSA 2022). An environment of low trust is not conducive to voluntary tax compliance (Kirchler, Hoelzl and Wahl 2008). Moreover, an environment of low trust has the potential to reduce the guilt that is associated with tax non-compliance. It is for this reason that taxpayers may feel justified to withhold taxes if it is likely that their taxes may not be used for the intended purpose. In support of this statement, SARS' debt book exceeds R238 billion (SARS 2021b), suggesting that a large number of taxpayers are resistant to the act of paying taxes.

In any society, there will be taxpayers who comply voluntarily; however, there will also be those who need to be compelled to comply (Tan and Braithwaite 2018). Most tax authorities use enforcement methods such as penalties to force taxpayers to honour their tax obligations (Lederman 2018). In South Africa, the Tax Administration Act (TAA) No. 28 of 2011 (RSA 2011) imposes penalties on the non-submission or late submission of tax returns, as well as on late payment of taxes (RSA 2011). These penalties are

usually levied at 10% of the tax amount due; however, in certain instances, the penalty can reach up to 200% if the taxable income is under reported intentionally (RSA 2011).

The relationship between penalties and tax compliance is multifaceted. Alm, Jackson and McKee (1992) as well as Feld and Frey (2007) found a negative association between tax compliance and tax penalty rates. Namusonge, Biraori and Kipicoech (2014), Oladele et al. (2019) and Remali et al. (2018) found a positive relationship between penalties and tax compliance. Oladipupo and Obazee (2016) found an insignificant positive relationship between tax compliance and penalties.

The studies presented above demonstrate conflicting results on the influence of penalties on tax compliance behaviour. Furthermore, these studies were not conducted in a South African context. This presents an opportunity to add a South African small business perspective to the body of knowledge. Therefore, the objective of this article is to report on a study that investigated the influence of penalties on the tax compliance behaviour of small business owners in South Africa. The article comprises the introduction; the literature review; the research design; the findings; and the conclusion which provides recommendations as well as outlining the contribution and value of the study.

## Literature Review

### **Tax Compliance**

Collecting taxes from the small and medium enterprise (SME) sector is often described as a daunting task (Benjamin and Mbaye 2012; Fox and Murray 2014). Furthermore, small businesses' financial records are frequently not well maintained (Slemrod et al. 2017). Unlike salaries and wages, income from small businesses is not completely subjected to third-party reporting. The Internal Revenue Service in the United States reported a compliance rate of 44% for taxable income that is not subjected to third-party reporting (Slemrod et al. 2017). Furthermore, small businesses often accept payments in cash which can be hard to monitor (Gordon and Li 2009).

The Organization for Economic Co-operation and Development (OECD 2004) highlighted that small businesses are more vulnerable to tax cheating compared to other taxpayer groups. Tax compliance encompasses the honest declaration of income and expenses as well as the payment of taxes on time (Oladipupo and Obazee 2016). Not all taxpayers are willing to voluntarily comply with tax laws, however, and some need to be pushed. Penalties are levied on late submission of tax returns, late payment of taxes as well as on the incorrect declaration of income and expenses. The penalties are imposed to encourage as well as compel taxpayers to honour their tax obligations on time. The aim is to make tax non-compliance costly and unattractive (SARS 2022).

According to Doran (2009), tax penalties not only support tax compliance, but also define it. The deterrence measures in the form of penalties are necessary to encourage and enforce tax compliance. However, these penalties should be implemented in a way

that will influence taxpayers' behaviour by preventing non-compliance (Swistak 2016). Further, the penalties should be more punitive compared to the fulfilment of a given tax obligation, yet not repressive (Swistak 2016). Tax penalties are not always successful in encouraging or compelling compliance. If the taxpayers perceive the penalties to be fair and acceptable, compliance is reinforced; however, if they are perceived to be unfair and repressive, they instead foster resistance (Swistak 2016). Swistak (2016) argues that while penalties are important and needed to enforce or encourage tax compliance, they tend to produce better results when supplemented by other measures.

Therefore, the state cannot rely purely on punitive measures in the form of penalties to enforce tax compliance. This is especially true when it pertains to small businesses. There are other hindrances that stand in the way of compliance for small businesses, such as, lack of basic tax knowledge and the specialised nature of tax skills (Coolidge, Ilic and Kisunko 2009). Furthermore, regressive tax compliance costs weigh heavily, particularly on small businesses and may have a negative impact on tax compliance (DeLuca et al. 2007; Hasseldine et al. 2012; Ndlovu, Schutte and De Clercq 2021; Smulders and Stiglingh 2008).

In this regard, the rule of law ought to be implemented in a personalised and systematic way avoiding the enforcement of the law to crowd-out tax morale (Arcos Holzinger and Biddle 2016). Traditional deterrence policies must be merged with those that emphasise cooperation (Braithwaite 2006). Therefore, when taxpayers are treated with respect on early non-compliance, they tend to be compliant in the future (Arcos Holzinger and Biddle 2016). Guala and Mittone (2005) argue that tax administrators must pay particular attention to nascent entrepreneurs, as they are likely to be more receptive because they have not yet developed perceptions and behaviours that will be hard to change. The first experience of support with these nascent entrepreneurs is likely to yield positive results and increase their confidence in tax authorities and thereby build an increased willingness to comply in future (Kamleitner, Korunka and Kirchler 2012). According to Murphy (2004), however, severe sanctions at first encounter may backfire, leading to hostility and resistance.

Oladipupo and Obazee (2016) found that tax knowledge has an increased likelihood of promoting tax compliance among small businesses more than penalties. Alm, Jackson and McKee (1992) and Feld and Frey (2007) found a negative association between tax compliance and tax penalty rates. On the other hand, Alkhatib, Abdul Jabbar and Marimuthu (2018); Namusonge, Biraori and Kipicoech (2014); Oladele et al. (2019); and Remali et al. (2018) found a positive relationship between penalties and tax compliance.

Therefore, there is a need to further investigate the influence of penalties on tax compliance behaviour. Firstly, there are conflicting results regarding the relationship between penalties and tax compliance in the literature. Secondly, there is limited research in South Africa that has looked at the influence of penalties on tax compliance

behaviour. Thirdly, small businesses are an important part of the tax system as they are entrusted with the important role of collecting VAT and payroll taxes and remitting these payments to SARS. However, small business income sources are rarely subjected to third-party reporting and therefore voluntary compliance is likely to be impacted negatively. Enforcement becomes essential when voluntary compliance is low.

### **Theoretical Framework**

This study was underpinned by the deterrence theory. It is a theory of decision under risk settings and declares that people try to maximise expected utility in choices that are flanked by risky options (Levy 1992). According to the deterrence theory, tax evasion is dependent on the maximisation of expected utility (Allingham and Sandmo 1972). People first weigh the utilities of individual results by their probabilities and then choose the option with the highest weighted amount (Luce and Raiffa 1957).

Small business owners tend to act in a rational manner, and they are steered by the intent to maximise the expected utility from the tax evasion gamble (Alkhatib, Abdul Jabbar and Marimuthu 2018). In this regard, they contrast the benefits linked to successful tax evasion with the penalty if they are caught (Alkhatib, Abdul Jabbar and Marimuthu 2018). Therefore, the deterrence theory suggests a negative relationship between penalty rates and tax non-compliance (Allingham and Sandmo 1972; Oladipupo and Obazee 2016).

The extant research suggests that small business owners are more susceptible to tax non-compliance compared to other taxpayer groups (Kamleitner, Korunka and Kirchler 2012). They are therefore considered to be a high-risk group regarding tax compliance (OECD 2004). This study sought to investigate the influence of penalties on tax compliance by encouraging small business owners to reflect on and talk about their lived experiences and perceptions. They were asked, among other things, whether they believe penalties are an effective form of deterrence for small business owners.

## **Research Design and Methodology**

### **Research Methodology**

A qualitative method utilising semi-structured interviews was employed in the current study. The aim was to understand and present the contextual meaning of the lived experiences of small business owners rather than to measure or predict their tax compliance behaviour. Therefore, a qualitative method was deemed appropriate for this study as it uses a naturalistic approach which seeks to comprehend phenomena in situation-specific settings (Patton 2001). It also pursues insight and understanding (Golafshani 2003).

## **Research Design**

An interpretive phenomenological research approach underpinned the study design. It provided the researchers with an opportunity to obtain an understanding of the small business owners' tax compliance behaviour regarding the influence of penalties. This is because an interpretive phenomenological research approach enables researchers to obtain insights into people's motivations and actions (Feeley and Thomson 2016). The insights into people's motivations and actions are further enhanced by the ability of the interpretive phenomenological research approach to convey what may usually be taken for granted by "pulling away layers of forgetfulness or hiddenness that are present in our everyday existence" (Frechette et al. 2020, 2).

## **Target Population**

The target population for this study included small businesses in Gauteng, which is the business hub of South Africa, with an annual revenue of up to R20 million. The R20 million threshold resulted from the ITA definition of an SME (RSA 1962). Approximately 35% of all SMMEs operate in Gauteng, making it the province with the largest share of SMMEs out of the nine provinces (SEDA 2018).

## **Sampling Technique**

A combination of purposive and snowball sampling techniques was employed to meet the objectives of depth, rigour and richness (Marshall 1996; Merriam 2002; Silverman 2010; Tracy 2010; Wynter 2014). The sampling process for a qualitative study has a totally different purpose from that of a quantitative study. Qualitative sampling ought always to be purposeful, thus the participants must be selected deliberately (Morrow 2005). The participants in a phenomenological study need to be cautiously selected as being individuals who have all experienced the phenomenon under investigation (Creswell 2007).

## **Sample Size**

A suitable sample size for a phenomenological study may range between six and ten participants (Haase 1987; Morse 1994). According to Groenewald (2004), the sample sizes for interpretive phenomenological studies are usually small, with ten being a common size. In the current study, new meanings and rich data continued to emerge even after the first 10 interviews. It was for this reason that the researchers extended the sample size to 25. At that point, the researchers were satisfied that they were able to uncover the multiple layers of hiddenness of the tax compliance phenomenon within its context (Frechette et al. 2020). No new meanings continued to emerge after the first 22 interviews. Mason (2010) analysed sample sizes of 25 phenomenological studies and found that the median sample size in these studies was 20. This indicates that large sample sizes are not at all unusual in phenomenological studies.

## Data Analysis

The aim of the analysis was to try and reveal or discover the essence of the life experiences of small business owners. This affords the readers an opportunity to understand these experiences even though they may not have lived them (Lewis 2010). Furthermore, the data analysis sought to discover anything unexpected in the ordinary as well as anything strange in the taken for granted (Van Manen 2016).

The researchers presented the phenomenological results thematically following guidelines offered by Max van Manen, wherein the emerging themes are used as generative guides for writing the article (Chagadama 2018; Van Manen 1997). The analysis process followed these four steps: (i) uncovering thematic aspects; (ii) isolating thematic statements; (iii) composing linguistic transformations; and (iv) gleaning thematic descriptions.

Uncovering thematic aspects entails the process of preparing the interview transcripts to ensure they are accurate and ready for the next step of the analysis process (Ritruethai et al. 2018). It is a process wherein the researchers engage with and reflect on the text (Ritruethai et al. 2018). The researchers checked the accuracy of the transcripts by listening to the digital audio files while at the same time reading the transcripts. This process afforded the researchers the opportunity to re-live the interviews.

Isolating thematic statements entails the process whereby the researchers repeatedly read the transcripts and reflect on the text yet again, this time with the aim of assigning codes. During this process, five levels (rounds) of coding emerged, namely: (i) holistic coding; (ii) separating the data into manageable parts; (iii) highlighting significant statements; (iv) assigning codes to the significant statements (line by line coding); and (v) assigning codes to a paragraph containing a significant statement. An inductive approach to coding was followed. Therefore, the majority of the codes were data driven. The aim was to elevate the voice of the small business owners by allowing the primary data to speak for itself.

Composing linguistic transformations and gleaning thematic descriptions entails the development of themes from the first cycle codes. This was done through ongoing dialogue and engagement with the first-cycle codes. During this process of developing themes, the first cycle codes were first reorganised and reconfigured to generate a list of categories. A number of categories were thereafter grouped together to form sub-themes. The sub-themes were brought together and lifted to form the themes which are discussed next.

## Findings

Twenty-five small business owners consented to participate in the study. Nine of the 25 small business owners were females and 16 were males with no notable differences in their lived experiences regarding tax compliance. At the time of the study, 24 of the

small businesses were registered as private companies with the Companies and Intellectual Property Commission (CIPC), while one was trading as a sole proprietor. The number of years in operation of the small businesses at the date of the interviews spanned between two years and 25 years, with the majority operating for at least five years. The interviews lasted between 24 minutes and 93 minutes, with an average time of 55 minutes per interview.

The small business owners displayed mixed reactions to the influence of penalties on tax compliance behaviour. Small business owners 6, 16, 17, 20, 21 and 22 argued that the charging of penalties by SARS encouraged them to submit their tax returns and pay the amount owed to SARS on time:

I think it [charged automatic tax penalties] has happened on two occasions. So now what I do is I do a bit better forward planning. And so, I realise that perhaps this time like round about the 7th of April I realise that I am traveling, or I might have programs, so I am very busy, so I then ask them to put through two tax payments in advance. So, they create the documentation that I can pay in advance. So yes, for sure ... Yes, they [automatic tax penalties] do work. (Small business owner 21)

This assertion by these six small business owners is in alignment with the findings by Namusonge, Biraori and Kipicoech (2014), Oladele et al. (2019) and Remali et al. (2018) who found a positive relationship between penalties and tax compliance. However, many of the small business owners (4, 5, 9, 10, 11, 12, 15, 18, 20, 22, 23 and 25) raised concerns regarding the charging of penalties on small businesses. These small business owners argued that, in certain circumstances, there are compelling reasons behind their non-compliance. In this regard, four key themes emerged from the small business owners' comments.

Firstly, the charging of penalties has the potential to discourage small business owners from registering at all for taxes. Secondly, the small business owners made it clear that the charging of penalties is not the key reason they comply timeously. Thirdly, the small business owners argued that late payment of taxes is often a result of cash flow challenges. Fourthly, the small business owners reasoned that non-compliance is sometimes due to a lack of skills and basic tax knowledge. These four key themes are summarised in Table 1 and discussed below.

**Table 1:** Summary of themes

No.	Theme
1	Registering for tax
2	Motivation for small business owners to comply
3	Cash flow challenges
4	Lack of skills and basic tax knowledge



## **Registering for Tax**

Penalties are usually levied at 10% of the amount outstanding (RSA 2011). However, in certain circumstances, tax penalties can reach up to 200% (RSA 2011). This is especially the case when the taxpayer intentionally conceals income from SARS. Small business owners 15 and 23 had a first-hand experience of substantial penalties levied after an audit was concluded by SARS. According to these small business owners, harsh penalties carry with them the potential to discourage entrepreneurial activities. Furthermore, the substantial penalties have the potential to discourage non-compliant taxpayers from coming forward for fear that they may lose everything. In this instance severe sanctions lead to hostility and resistance (Murphy 2004):

... what I can tell you is it [SARS] is very brutal in terms of their system. It is very brutal they want people to comply. And it is actually discouraging business ... So, they came and charge me a lot of money to say that I have under declared with R150 000.00 ... they have added the penalties on R150 000.00 it came to around R500 000.00. (Small business owner 15)

... that if I have made a mistake I should just disappear permanently. That is why they prefer to be out of the system that they do not want, they get de-registered. (Small business owner 23)

The imposition of penalties is consistent with the deterrence theory (Allingham and Sandmo 1972; Oladipupo and Obazee 2016). Although the intention is to discourage non-compliance, tax authorities need to carefully consider the unintended consequences associated with penalties.

## **Motivation for Small Business Owners to Comply**

Small business owners 15 and 18 argued that the penalties are not necessarily the stick that compels them to comply on time. According to them, the main driver of compliance is the need to always ensure that they are in good standing with SARS. Small business owners 1, 3, 4, 5, 6, 8, 11, 13, 14, 15, 17, 18, 20, 24 and 25 all indicated that the main driver of timely compliance for them is to ensure that they are in good standing with SARS. This is because if they are not, they will not be able to do business with the state and some private organisations. Therefore, timely compliance is not always a result of the fear of penalties:

So, the penalty is not really, for me they are not a stick to make sure I pay. However, what is a stick for me is our tax clearance. That is more important. So, anything that compromises our tax clearance, if we are not paying VAT it compromises our tax clearance I make sure they sort it out as soon as possible. (Small business owner 18)

... myself I have got a number of companies that I run it has nothing to do with government I might as well pay that penalty later but for these ones that I deal with government then I will avoid ... But for business that has got nothing to do with

government I will not worry, off course it is a cash out flow from your side when you have to pay all those things, but I will not stress about it. (Small business owner 15)

State organisations and selected private corporations enforce compliance indirectly by requiring a tax compliance certificate (tax clearance) when engaging small businesses. In this regard, non-compliance has negative repercussions on the ability of small businesses to source business or receive payments if they are non-compliant at any point in time. The small business owners considered this indirect form of enforcement to be effective in encouraging timely compliance compared to penalties.

### **Cash Flow Challenges**

Small business owners 1, 4, 5, 20, 22, 24 and 25 expressed the concern that oftentimes they struggle with cash flow, whereby they do not have enough working capital for their business operations. Consequently, should anything happen out of the ordinary, they will likely be unable to meet their short-term tax obligations:

... that is the thing that we are missing it for small businesses the cash flow is everything. We are not like big corporates that have six or 12 months' worth of cash flow. We literally have like 30 days, everybody works a 30-day cash cycle in small businesses ... (Small business owner 22)

There are so many ways where you can lose money in unexpectedly like let's say breakdowns. The truck broke the engine it wants R50 000.00, so you take from that money, from the business money. You need that truck to run because if that truck do [does] not run you take the money and pay SARS and the truck is not running ... how will you make another money to pay SARS. But if you do not pay SARS you make that truck run, you will make double money and you pay SARS ... (Small business owner 12)

Due to insufficient working capital, small business owners are usually conflicted when it is time to pay taxes. They must often make the difficult decision of whether to pay SARS or pay employees and suppliers first. The small business owners declared that they would pay their employees and suppliers before SARS:

... the late payments comes [come] in this way. Maybe the end of that month you pay SARS you will have more accounts to pay and to pay SARS or pay the account because otherwise you will not run your business if you do not pay your account because you will not have a supplier. So, what you do, you stop paying SARS and pay the account. So, you get another stock, you sell it and then you pay SARS that is where the delay comes in ... (Small business owner 12)

The charging of penalties does not suddenly make it possible for small businesses to pay taxes on time. Therefore, the penalties simply add to the cost of doing business:

It [tax penalty] does not force me to pay on time, it does not. Because all of the time, most of the time when I am not complying is because I had cash flow problems. And

the fact that I am going to pay penalties later it really does not matter at that time when I am having cash flow problems ... I really feel that all these laws were made thinking of big businesses in mind. You know, they were not made thinking of a small business who is on the same equal footing as a big business. (Small business owner 4)

Vendors are required to remit VAT monies to SARS (RSA 1991). In theoretical terms, the payment of VAT to SARS should not pose any difficulty since the small business owners are merely acting as agents. As VAT vendors, the small business owners are collecting the VAT money from their customers and remitting it to SARS. However, it does appear that it is not as simple as that, since small businesses are not always paid on time by their clients. The failure to receive payments on time means that no tax monies would have been collected for the goods sold or services rendered by these businesses and therefore there is nothing to be remitted to SARS. These late payments mean that small business owners are likely to incur penalties as they are required to account for VAT on an invoice basis. The invoice basis of accounting implies that VAT must be accounted for when an invoice is issued to the customer and not necessarily when the payment is received (RSA 1991):

You see the challenge is sometimes when you do government jobs ... You will find they take six months [to pay] they will tell you so and so is not there to sign ... (Small business owner 25)

Meanwhile, the accounting of VAT on an invoice basis has the potential to discourage honest declaration. The fear of incurring late payment penalties may drive small business owners to think about illegal creative ways to avoid these penalties. For this reason, taxpayers may choose to submit nil returns or to omit invoices for which they have not received payment yet. Since the tax legislation requires VAT to be accounted for when an invoice is issued and not necessarily when payment is received, not declaring an unpaid invoiced amount is against the tax rules (RSA 1991):

You find people with more especially VAT instead of issuing tax invoices like medical doctors they issue a pro forma invoice with an amount of VAT inclusive in there. Once you have paid them, once you paid that invoice then they convert it in to a VAT invoice. And it is then that they submit. (Small business owner 23)

In instances where small business owners are experiencing working capital challenges, the charging of penalties makes it even harder for these businesses to survive. This is because the penalties add to the cost of doing business, for the reason that they are unavoidable at that point in time. Furthermore, accounting for VAT on an invoice basis may lead to dishonest behaviour wherein certain invoiced amounts are excluded from the calculation of VAT due. Lastly, small business owners may sometimes incur penalties due to a lack of skills and basic tax knowledge as discussed next.

## **Lack of Skills and Basic Tax Knowledge**

Small business owners lack the skills and basic tax knowledge that is necessary to be tax compliant (Coolidge, Ilic and Kisunko 2009). This lack of skills and basic tax knowledge often leads to unintended non-compliance (Newman et al. 2018). Small business owners 5, 11 and 22 argued that they incur penalties since they are not aware of their basic tax compliance responsibilities. The small business owners suggested that the penalties be accompanied by awareness, education and training initiatives. This is since there is sometimes a lack of understanding on the part of the business owners regarding the reasons for the penalty as well as how it can be avoided. In this regard, they argued that it will be difficult to avert the penalty in future if there is a lack of an understanding as to why it was levied in the first place. The suggestions put forth by these three participants support an argument made by Oladipupo and Obazee (2016), tax knowledge has an increased likelihood of promoting tax compliance among small businesses more than penalties:

Us entrepreneurs are sometimes not even aware of the implication of non-submission or late submission. More education need [needs] to be given for us to understanding fully the financial and legal implication of non-compliance. (Small business owner 5)

You see when you comply you do this and that so that next time we will not penalise you this amount of money. So, the problem is you say that I am penalising you, but the person has not, one of those people have not understood what really is going on. (Small business owner 11)

Owing to the lack of skills and basic tax knowledge, many small business owners are not able to be compliant by themselves. Thirteen small business owners (4, 12, 14, 15, 16, 17, 18, 19, 20, 21, 23, 24 and 25) outsource the tax compliance functions to a tax expert. The majority partially outsource these services to minimise the cost associated with outsourcing. This means that there are certain tax compliance functions that they still carry out by themselves or with the assistance of consultants at SARS branches. Unfortunately, some of the small business owners (7 and 8) cannot afford to outsource any of the tax compliance functions to a tax expert. Small business owners who do not have the skills or know-how and who cannot afford to outsource any of the tax compliance functions rely heavily on the SARS branch network for assistance:

Well in terms of the returns I am used to going to the SARS offices every year before March to update my returns and to get a new tax clearance ... (Small business owner 8)

A new norm was brought in by the COVID-19 pandemic in March 2020, wherein the SARS branches were closed, and taxpayers were requested to file returns using the e-filing system (SARS 2021c). Although the pandemic is mostly over, taxpayers are still requested to make appointments prior to visiting a SARS branch. Therefore, a taxpayer cannot simply walk into a branch as and when they need assistance. Small business owners 11 and 16 who partially outsource the tax compliance functions were levied with penalties for not submitting returns on time. The reason for non-submission was due to

not being able to access the SARS branches during the COVID-19 pandemic. Although SARS asked taxpayers to use online platforms, these small business owners did not have the skills to use digital platforms such as e-filing:

I am one of those who have been penalised for not submitting my returns in time. And one of the reasons why number one lockdown happened, e-filing system happened ... Because everybody was turned down at SARS premises being told that you have to go online. (Small business owner 11)

The small business owners suggested that the charging of penalties be accompanied by awareness, education and training initiatives to avoid penalties in future.

### Concluding Remarks

The small business owners displayed mixed reactions to the influence of penalties on tax compliance behaviour. Many of the small business owners agreed that penalties do encourage them to pay taxes on time. However, they noted with concern that the charging of substantial penalties has the potential to discourage small businesses from registering at all for taxes. Furthermore, they argued that non-compliance is often involuntary. They sometimes miss deadlines for when their returns ought to be submitted and paid because of a lack of skills and basic tax knowledge.

In addition, small business owners are often faced with tough choices to make in their businesses as a result of cash flow challenges. Oftentimes, taxes are due at the same time as salaries, wages and other operational expenses. In this regard, small business owners must decide whether to honour their tax obligations or put the needs of their businesses first. Usually, small business owners put the needs of their businesses first and by so doing they incur penalties on a regular basis. Therefore, penalties become just another cost of doing business. In this instance of involuntary non-compliance, penalties become disheartening to the small business owners.

The requirement to account for VAT on an invoice basis is impractical for small businesses as they are not always paid on time by their clients. In its current form, the invoice basis of accounting for VAT discourages honest declaration by the small business owners. To avoid penalties, small business owners may choose not to declare unpaid invoices, thereby acting against the prescripts of the tax legislation.

Although the penalties are necessary to compel taxpayers to pay taxes on time, they must be implemented in a cautious and sensible manner. Especially as it relates to small businesses that are already trying to do the right thing. These penalties must be complemented with awareness, training and educational initiatives as well as policies that make it easier for small business owners to comply. Care should be taken to ensure that penalties do not discourage small business owners from registering at all for taxes.

Qualitative research carries with it some limitations. Although it brings to the surface rich understandings and contextual meaning, the findings may not be transferred to the broader SME community. In addition, the researchers co-constructed knowledge and meaning of the essence of the participants' experiences which may result in biased interpretations. However, the use of direct quotes and an audit trail that documented the researchers' decisions during the data collection and analysis phase minimised the bias concern.

The current study has provided new perspectives on the influence of penalties on the tax compliance behaviour of small business owners. It has laid a foundation for future studies by focusing on small business owners who have already taken the step to comply. More research is needed to understand the influence of penalties in dissuading informal businesses from formalising due to fear of prosecution.

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