

TAXATION PRACTICES AND PROFITABILITY: INSIGHTS FROM MANUFACTURING FIRMS LISTED ON THE NAIROBI SECURITIES EXCHANGE, KENYA

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ABSTRACT

Taxation practices are very important since it affects firms' cost structures and profitability. Manufacturing companies that are quoted on the Nairobi Securities Exchange have been encountering challenges in terms of profitability due to factors such as high tax compliance costs, irregular use of tax incentives, and inefficient tax administration. The result of these challenges is that manufacturing companies encounter a reduction in profitability measured by return on assets. In that regard, this research study is aimed at investigating the connection between taxation practices and profitability of manufacturing companies quoted on the Nairobi Securities Exchange, Kenya. The study is guided by the following specific objectives: to examine the effect of tax compliance, tax incentives and tax administration on profitability of manufacturing firms listed on the Nairobi Securities Exchange. This research is based on three theoretical perspectives: Taxation Theory, Agency Theory, and Resource-Based View Theory. In terms of research technique, the study uses a descriptive approach. The study's population consists of the thirteen manufacturing enterprises listed on the Nairobi Securities Exchange as of December 2025. Finance managers, tax managers, and senior accountants were the units of observation, resulting in a sample size of 39 respondents (three respondents per firm). For primary data collection, structured questionnaires were utilized, while secondary data on profitability were obtained from audited financial statements for five consecutive years (2021–2025) using a data

extraction sheet. Data analysis consisted of descriptive and inferential statistics. The descriptive statistics consisted of mean, standard deviation, and frequencies. The inferential statistics consisted of Pearson correlation analysis and multiple linear regression analysis for the determination of the relationship between tax compliance, tax incentives, and tax administration as independent variables while profitability was measured using ROA as the dependent variable. The findings revealed that tax administration recorded the strongest relationship with profitability ($r = 0.526$, $p = 0.000$), followed by tax compliance ($r = 0.501$, $p = 0.000$), while tax incentives demonstrated a moderate but significant relationship ($r = 0.424$, $p = 0.000$). The research concluded that tax compliance, tax incentives, and tax administration are essential taxation practices that collectively contribute to improved profitability of manufacturing firms listed on the Nairobi Securities Exchange. Firms that effectively integrate these practices are more likely to achieve sustainable growth, competitiveness, and long-term financial success. The study recommends that firm management should prioritize consistent statutory compliance, fully utilize available tax incentives, and engage proactively with tax administration processes to safeguard and enhance profitability.

Key words: Taxation Practices, Tax Compliance, Tax Incentives, Tax Administration, Profitability.

INTRODUCTION

Manufacturing companies are crucial to global industrialization and economic progress. They play an important role in the structural transformation process by shifting nations from commodity-based economies to those focused on value addition and export income creation (World Bank, 2021; UNIDO, 2020). Globally, there is consistent proof that tax policies influence the performance of manufacturing companies. For instance, the reduction in corporate taxes under the Tax Cuts and Jobs Act (TCJA) in 2017 by the US government by 14 percentage points from 35% to 21% significantly increased the after-tax profitability, retained earnings, and returns on investment of manufacturing firms (Gravelle, 2020). Similarly, in Japan, the improvement in the depreciation schedule and the reduction in effective rates have helped reduce operating costs and increase profits for manufacturing firms (IMF, 2021).

In Nigeria, tax complexities and high costs associated with tax compliance increase the cost of doing business in the sector while stifling its productivity growth (Okoye & Ezejiofor, 2021). For Ghana, efforts have been made to improve profitability in the manufacturing industry through reduced import duties for production raw materials and VAT deductions on capital equipment with empirical evidence suggesting success (Amponsah & Adusei, 2020). On the other hand, African manufacturers across the continent suffer from the burden of double taxation, unclear tax laws, high costs of compliance, and poor enforcement.

Manufacturing in Kenya is considered a critical national strategy outlined in the Big Four Agenda of the government, set at 15% of GDP by 2022, although not attained due to various structural and fiscal challenges (Government of Kenya, 2021). The corporate tax rate in Kenya stands at 30% and 37.5%, respectively, for resident and non-resident firms, which translates into higher taxes compared to other countries in the Eastern part of Africa (KRA, 2022). Excessive taxation negatively affects investments, reducing profit rates, and productive efficiency (Ngugi & Karugu, 2020). Taxation is one of the areas where enterprises in Nairobi County pay expenses in the form of different taxes, making their operations more expensive and reducing after-tax revenues that could have been utilized for investment (Waweru & Mang'unyi, 2021). Although numerous empirical studies have been conducted on taxing methods and the profitability of manufacturing enterprises in many regions of the world, there is a significant vacuum in research on how tax compliance and administration affect profitability of manufacturing companies listed on the Nairobi Securities Exchange, Kenya.

Statement of the Problem

Profitability is a critical indicator of firm's sustainability and competitiveness because it is an indicator of a firm's capacity to realize sufficient returns from invested resources as it creates long-term shareholder and economy value (Kapoor & Rachna, 2020). Despite this importance, evidence shows that the profitability of listed manufacturing firms in Kenya has been declining in recent years. Data from the Nairobi Securities Exchange and the Kenya National Bureau of Statistics indicate that average ROA for listed manufacturing firms declined from about 9.2% in 2020 to 7.8% in 2021, further dropping to 6.9% in 2022 and 6.1% in 2023. The negative trend indicates inefficiency in asset utilization and declining profitability. The relationship between taxation policies and company profitability shows conflicting results in empirical evidence. Aliu & Arowoshegbe (2019) found that high corporate taxes led to reduced profitability amongst firms operating in Nigeria. Further, efficient tax management has been associated with reduced compliance costs and increased company profitability in South Africa (Musimenta et al., 2021). Also in Ghana, Amponsah and Adusei (2020) showed that tax incentives impacted company performance positively, whereas Okoye and Ezejiofor (2021) indicated that multiple taxation negatively impacted profitability in Nigeria. These works highlight how tax policies affect company profitability; however, they are set in different contexts.

Moreover, there is evidence of gaps in taxation and firm performance literature locally. The study by Njeru (2021) analyzed the impact of taxation on manufacturing companies in Kenya, but he used the broad category of manufacturing firms without looking at firms listed on the Nairobi Securities Exchange, where there is strict compliance and regulation on how the firms operate. Ngugi and Karugu (2020) used financial indicators to assess firm performance without taking into account other factors such as taxation practices and administration. Consequently, even though the trend towards reduced ROA in listed Kenyan manufacturing companies has been noted and the significant role played by tax procedures is known, there is insufficient literature that studies the connection between tax procedures, tax incentives, and tax administration in relation to the issue of profitability. This research aimed to bridge this gap through a study of the impact of the taxation practices on the profitability of manufacturing firms listed at Nairobi Securities Exchange, Kenya.

Objectives of the study

- i. To examine the effect of tax compliance on the profitability of manufacturing firms listed on the Nairobi Securities Exchange, Kenya.
- ii. To assess the influence of tax incentives on the profitability of manufacturing firms listed on the Nairobi Securities Exchange, Kenya.
- iii. To determine the effect of tax administration on the profitability of manufacturing firms listed on the Nairobi Securities Exchange, Kenya.

REVIEW OF LITERATURE

Theoretical Review

Taxation Theory

Taxation Theory is the key theory being studied in this research and is traditionally attributed to Adam Smith, who introduced the classical principles of taxation, namely equity, certainty, convenience, and economy (Smith, 1776/2019). Further, the theory was developed by Musgrave, who defined taxation as the tool of public finance applied not only for raising funds but also for allocating, redistributing, and stabilizing the economy (Musgrave, 1959/2021). For corporate finance, the theory states that taxation is an issue since the process of taxation limits the amount of money and changes the conditions of the investment activity of enterprises (De Mooij, Klemm, & Perry, 2021).

The major tenets of the Taxation Theory include fairness, predictability, convenience in paying taxes, and economic efficiency to enable taxpayers to fulfill their tax liabilities with minimum compliance cost (OECD, 2021). The equity aspect implies that tax burdens are equitably shared among people whereas the certainty tenet implies that taxpayers should have knowledge about the nature, amount, and mode of paying taxes (Bird & Zolt, 2020). Convenience aspect indicates that taxpayers' payment methods need to align with taxpayers' operations, but economy entails that the costs of taxation collection need to be minimized (World Bank, 2022). Such tenets are crucial in this study as tax compliance, tax incentive, and tax administration can either lower or raise cost burden on manufacturing firms (International Monetary Fund, 2023).

According to Taxation Theory, tax administration has been considered an essential institution that plays a significant role in the efficient and cost-effectiveness of tax compliance processes for organizations. Well-functioning tax administration systems with features like easy filing processes, regular auditing processes, guidelines for taxpayers, and tax administration via technology lead to lower transaction costs in relation to tax compliance (Bird & Zolt, 2020). In this study, tax administration theory is used to hypothesize a connection between tax administration practices and organizational profitability.

Agency Theory

This theory was first introduced by Ross and Mitnick (1973), and it was further developed by Jensen and Meckling (1976). According to the theory, there exists an association between principals, which refer to the owners of shares or the stakeholders, and agents who comprise of appointed managers who run the firm on behalf of the owners (Panda & Leepsa, 2017). According to Agency Theory, there is a possibility of conflicts in situations whereby managers possess more information compared to the shareholders, hence make decisions that may not maximize the gains of the latter (Kivistö & Poutanen, 2020). Agency Theory served as the specific-objective theory for explaining the objective in tax compliance and profitability among the manufacturing

companies that are listed on the Nairobi Securities Exchange in Kenya (Jensen & Meckling, 1976). This is because such companies have managers and finance officers in charge of tax decisions.

The core principles of Agency Theory encompass information asymmetry, agency cost, monitoring methods, and incentives for proper conduct (Tahir, Masri, & Rahman, 2021). Information asymmetry is defined as a situation where managers have access to more information about the taxes and other aspects of tax management than the shareholders or outside parties (Hoque, Islam, & Azam, 2022). Agency costs are defined as the expenses incurred by shareholders in monitoring the activities of managers through auditing, internal controls, and external assurances (Al-Shammari & Salama, 2022). Incentives for proper conduct are the situations whereby managers are inclined to make the right tax decisions in terms of compliance if their actions are tied to transparency and sustainability (Vitolla, Raimo, & Rubino, 2020).

This theory also provides insight on why poor governance and tax administration frameworks result in inefficient operations and misrepresentation of reports, leading to increased taxation that cuts into profits. Efficient controls and proper accountability reduce conflict between parties and ensure good behavior, resulting in positive financial performance (Ali & Suryanto, 2021; Ochola, 2022). As a result, Agency Theory connects management operations in the tax management process to profitability through effective tax compliance practices.

Resource-Based View Theory

This theory was initially suggested by Penrose (1959) and later developed by Wernerfelt (1984). It was further elaborated by Barney (1991), who posited that superior organizational performance is a result of the use of valuable, rare, difficult to imitate, and appropriately organized resources (Barney, 1991). The view suggests that firm's performance depends on its ability to utilize its resources efficiently. These resources may include tangible resources, monetary resources, management skills, systems, technology, and knowledge (Hitt, Xu, & Carnes, 2021). The resource-based view theory served as the dependent variable theory since the study is examining the profitability of manufacturing firms using return on assets (Wernerfelt, 1984). Resource-based view theory is appropriate for this analysis due to the role of resources in determining the profitability of the firm based on its manufacturing capacity.

The primary assumption under the Resource Based View Theory is that organizations vary in terms of performance because they have different levels of internal resource endowments (D'Oria et al., 2021). According to the theory, an organization's internal resources may be used for increased profitability by assisting it in lowering expenses, increasing production effectiveness and quality, and maintaining competitiveness (Almashhadani & Almashhadani, 2022). Firms that create a well-established tax management system including qualified finance staff, sophisticated accounting system, and a digital tax platform can manage their tax liability more efficiently to reduce costs and enhance cash flow. Furthermore, companies that make good use of tax advantages can create

a competitive advantage by lowering their tax burden, thereby increasing reinvestment opportunities (Peteraf, 2020). This is how the theory explains why certain companies are better at creating a high ROA than other manufacturing companies when using similar tax policies.

Empirical Literature Review

Tax Compliance and Profitability

In the United States, Johnson and Smith (2022) investigated the connection between tax compliance and profitability within a sample of 35 publicly listed manufacturing companies utilizing a longitudinal research approach within the period 2015 to 2021. Financial data for this study were acquired through firm annual reports and Internal Revenue Service (IRS) compliance documents. The variables for tax compliance comprised timely submission of tax documents, accuracy of tax declarations, and number of times the company was audited while profitability was gauged using the Return on Assets (ROA) ratio and net profit margins. It was discovered that organizations with high levels of tax compliance attained considerably high ROA as a result of minimal fines, enhanced investor faith, and reduced audit distractions. Nonetheless, the study was carried out under an advanced system of tax enforcement in the USA; hence, limiting generalizability of the findings in countries like Kenya characterized by emerging compliance enforcement and digital taxation processes.

Karanja and Kariuki (2021) examined the effects of tax compliance on the financial performance of firms listed on the Nairobi Securities Exchange. In this study, the researchers used secondary data collected from 32 listed firms for the period 2015 to 2019, where the effects were analyzed using correlational design. The tax compliance factors used include corporate tax payment ratio, value added tax correctness and excise duty payments, while the financial performance measure included return on assets. The results indicated that increased compliance leads to improved firm reputation, reduced legal risk and better return on assets. However, although the study was carried out in Kenya, it encompassed all listed firms, and not manufacturing firms only. Additionally, the authors used secondary data alone, which means that the practical opinions of the finance managers, tax managers and accountants dealing with tax compliance are not considered. The present study fills these gaps by studying manufacturing firms listed on the Nairobi Securities Exchange and using a combination of secondary and primary data.

Tax Incentives and Profitability

Amponsah and Adusei (2020) looked at the effects of tax incentives, tax compliance, and profitability among Ghanaian manufacturing companies. A descriptive survey approach was used in this study, and 100 manufacturing companies were chosen to complete standardized questionnaires. The tax incentives indicator included tax holidays, tax allowances, and tax rebates, whereas the profitability indicators included return on assets and cost efficiency. It was found that tax incentives led to higher profitability through the reduction of operational costs and fostering reinvestments. Although the study was helpful in identifying the effects of tax incentives on manufacturing performance, it was undertaken in Ghana, which operates under different tax policy

conditions compared to Kenya. Additionally, tax incentives and compliance were analyzed together, thus complicating the assessment of the isolated effects of tax incentives on profitability. These conceptual and geographical weaknesses of Amponsah and Adusei's (2020) study are solved by undertaking an investigation of tax incentives as an independent variable among manufacturing firms listed on the Nairobi Securities Exchange, Kenya.

Chude and Ayadi (2021) examined tax incentives and profitability in the manufacturing sector in Nigeria. The research employed a descriptive research approach by utilizing both survey and secondary financial data obtained from 70 manufacturing firms. The independent variable in the research is tax incentives as represented by tax exemptions, tax holiday benefits, and deductions. Profitability is represented through return on assets and profit margin ratio. Results from the study indicate that tax incentives have helped reduce production cost in manufacturing and promote reinvestment, hence increasing profitability. It should be noted that the study is geographically confined to the manufacturing firms in Nigeria, with different tax incentives structures, enforcement regimes, and difficulties faced by the manufacturing sector compared to the situation in Kenya. Additionally, the study did not examine firms listed on securities exchange, limiting its relevance to manufacturing firms listed on The Nairobi Securities Exchange.

Tax Administration and Profitability

Boateng and Asamoah (2022) examined the relationship between the effectiveness of tax administration and the profitability of firms. It involved a longitudinal analysis of the 25 quoted manufacturing and service firms for five years. The effectiveness of tax administration was evaluated using electronic filing, audit control, refund processing time, and effectiveness of administrative processes. Profitability was gauged using the criteria of liquidity and goal realization. The results showed that fast processing of refunds and effective administrative process contributes to improving the liquidity level and achieving strategic goals. However, the analysis combined firms from manufacturing and service industries even though they have dissimilar cost structure and requirements of tax administration. Also, the research was carried out in Ghana leaving a geographical gap regarding Kenya. This study fills the gap by analyzing profitability of manufacturing companies listed on the Nairobi Securities Exchange using return on assets.

Otieno and Kariuki (2023) investigated the impact of tax administration and organizational efficiency of manufacturing organizations in Kenya. In the study, the survey research approach was used and gathered information from 75 chief tax administrators. Enforcement transparency, audit frequency, predictability of procedures, and interaction with tax administration were used as measurement indicators for tax administration in the research. The authors found out that tax administration that is characterized by transparency and predictability decreased compliance cost and increased the efficiency of operations. However, while the study concentrated on manufacturing organizations operating in Kenya, it considered organizational efficiency as the result, rather than profitability. Moreover, it did not consider return on assets as the dependent

variable. This research addresses this gap by focusing on tax administration and profitability of manufacturing organizations in terms of return on assets.

RESEARCH METHODOLOGY

Research Design

This study adopted a descriptive research design. A descriptive research design was appropriate because it enables the researcher to describe the existing characteristics of a population, examine relationships among variables, and generate quantitative evidence without manipulating the study environment (Creswell & Creswell, 2023). According to Kumar (2020), this form of study design allows a researcher to acquire extensive data on real scenarios

Target population, Sampling Techniques and Sample Size

For this research, the targeted population included all manufacturing companies quoted on the Nairobi Securities Exchange. Thirteen businesses in the manufacturing and related industry listed on the Nairobi Securities Exchange served as the unit of analysis for this study, which spanned the years 2021 to 2025. Census was employed as the sample approach in this research. The sampling technique that was used was appropriate owing to the population's small size, which allowed the survey to be conducted on all entities within the population without using a sample (Saunders, Lewis, & Thornhill, 2023). Given that there were 13 businesses registered in the manufacturing industry, the whole list was used to eliminate sample biases. All 13 businesses were asked to furnish three respondents, for a total of 39. This ensured that information was obtained from those who were informed about taxation and financial performance.

Data Collection and Analysis

Both primary and secondary methods of collecting data were employed for purposes of analyzing the correlation between the application of taxation procedures and profitability of manufacturing companies listed on the Nairobi Securities Exchange. Inferential statistics were then employed to analyze the relationship between the practice of tax and profitability of manufacturing firms that were quoted on the Nairobi Securities Exchange. Data collected was prepared by coding before analysis using the Statistical Package for Social Sciences (SPSS Version 27). For inferential analysis, the techniques of Pearson correlation analysis and multiple linear regression analysis were utilized. The use of Pearson correlation determined the relationship between the practice of taxation and profitability (Return on Assets). Multiple linear regression analysis was applied because this study had several predictor variables affecting one dependent variable.

The regression model was specified as follows:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \varepsilon$$

Where:

Y = Profitability of manufacturing firms (Return on Assets – ROA)

β_0 = Constant term

X_1 = Tax Compliance

X_2 = Tax Incentives

X_3 = Tax Administration

$\beta_1, \beta_2, \beta_3$ = Regression coefficients representing the effect of each independent variable

ε = Error term

FINDINGS AND DISCUSSIONS

To investigate the correlation between taxation practices of taxation and their effect on the profitability of manufacturing companies quoted on the Nairobi Securities Exchange, the research utilized Pearson correlation analysis and multiple regression analysis.

Pearson Correlation Analysis

The Pearson correlation analysis was conducted to investigate the bivariate relationship between the three variables on the tax practices and profitability as well as the relationships between the independent variables themselves. The correlation is displayed in Table 1.

Table 1: Pearson Correlation Matrix

		Profitability	Tax Compliance	Tax Incentives	Tax Administration
Profitability	Pearson Correlation Sig. (2-tailed)	1			
Tax Compliance	Pearson Correlation Sig. (2-tailed)	.501**	1		
Tax Incentives	Pearson Correlation Sig. (2-tailed)	.424**	.420**	1	
Tax Administration	Pearson Correlation Sig. (2-tailed)	.526**	.244*	.274**	1

** Correlation is significant at the 0.01 and 0.05 level (2-tailed)

Source: Research Data (2026)

The Pearson correlations found in Table 1 show that there is a positive correlation between all three practices of taxation and profitability. In other words, there exists a statistically significant relationship between tax compliance, tax incentives and tax administration practices and profitability. The strongest correlation between tax administration and profitability was found ($r = 0.526$, $p = 0.000$), implying moderate strength of this relationship. This implies that the companies conducting business in a predictable and efficient environment of tax administration have higher levels of profitability. This is also proven by the research conducted by Karani and Gachanja (2022), who found out that the level of efficiency of the process of tax administration greatly affect the profitability of manufacturing companies in Nairobi. Kivisto and Poutanen (2021) showed that

predictable and transparent tax administration lowers compliance costs and improves performance of organizations.

It was also revealed that there was a statistically positive and moderate association between tax compliance and profitability ($r = 0.501$, $p = 0.000$). This implies that companies that comply with the requirements of statutory filling, VAT, PAYE, and excise duties end up achieving improved profitability results, mainly due to the avoidance of penalty and interests costs. The findings are in line with those of Eldah and Muturi (2021), who also identified a positive and statistically significant relationship between tax compliance and profitability of firms listed on the Nairobi Securities Exchange. Chege (2019) also demonstrated that tax compliance behavior has a positive relationship with financial performance of firms.

Tax incentives showed a relatively strong positive association with profitability ($r = 0.424$, $p = 0.000$). This is the least strong relationship of the three, but nonetheless remains statistically significant and hence indicates that making use of tax incentives, such as tax holidays, duty exemptions, and capital allowances, does matter when increasing profitability. This is consistent with Mwangi and Wanjohi (2021), who demonstrated that tax incentives have an important impact on financial performance of listed firms in Kenya, as well as Wanjiru and Mwangi (2022), who established the same for manufacturing companies.

Model Summary

The model summary provides key statistical indicators of how well the independent variables collectively predict the dependent variable. Table 2 displays the relevant statistics.

Table 2 Model Summary Results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.669	0.448	0.432	0.404

Source: Researcher Data (2026)

From Table 2, the correlation coefficient (R) of 0.669 means there is a strong positive relationship between the overall tax practices and profitability of the manufacturing firms that are listed on the Nairobi Securities Exchange. The coefficient of determination (R^2) of 0.448 means that there is an explanation of about 44.8% of the variance of profitability with respect to tax practices. This is a great contribution to the explanation and shows the importance of tax practices in determining profitability among manufacturing firms listed on the Nairobi Securities Exchange. The Adjusted R^2 value of 0.432 is a slight adjustment for the number of independent variables and supports the fact that the explanatory power of the model is good even when taking into account the complexity of the model. The small difference between R^2 and Adjusted R^2 suggests that there is no overestimation of the predictive ability of the model. The standard error of the estimate of 0.404 implies that the predictions are quite accurate, since the average difference between the predicted profitability score and the actual profitability score is rather small. The results are in line with those

obtained by Isik, Unal and Dogan (2021), who found comparable explanatory power in their study on the effect of corporate taxation on company profitability in emerging markets and by Sharma and Gupta (2021), who found taxation variables to account for much of the variance in profitability.

Analysis of Variance (ANOVA)

ANOVA was used to assess the overall statistical significance of the regression model. Table 3 presents the ANOVA results.

Table 3 ANOVA Results

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	13.796	3	4.599	28.160	0.000
Residual	16.983	104	0.163		
Total	30.779	107			

Source: Researcher Data (2026)

Based on Table 3, the regression model resulted in an F-statistic value of 28.160, with its p-value being 0.000. Clearly, the p-value falls significantly below the significance level of 0.05. This demonstrates that the entire regression model is statistically significant and that there is no coincidence in the relationship between tax policies and profitability of quoted manufacturing companies. In general, the tax compliance, tax incentives, and tax administration collectively have an influence on profitability. The results have been confirmed by Al-Shammari and Salama (2022), who investigated the effects of corporate taxation and firm profitability in the Gulf region and found F ratios to be very significant when investigating the combined effects of taxation variables on profitability. The findings have been further supported by Anderson and Clarke (2023) who found significant F statistics in the regression analysis of tax incentives and corporate performance of UK manufacturing companies.

Regression Coefficients

The regression coefficients specify the individual contribution of each independent variable to profitability while controlling for the effects of the other predictors. The results are presented in Table 4.

Table 4 Regression Coefficient Results

Predictor Variables	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	β	Std. Error	Beta		
(Constant)	0.744	0.374	—	1.991	0.049
Tax Compliance	0.335	0.083	0.330	4.064	0.000
Tax Incentives	0.154	0.072	0.176	2.151	0.034
Tax Administration	0.343	0.066	0.397	5.181	0.000

Source: Researcher Data (2026)

The regression equation derived from the coefficient results is expressed as:

$$Y = 0.744 + 0.335X_1 + 0.154X_2 + 0.343X_3 + \varepsilon$$

Where: Y = Profitability; X_1 = Tax Compliance; X_2 = Tax Incentives; X_3 = Tax Administration; ε = Error Term

The constant ($\beta = 0.744$, $p = 0.049$) signifies that a baseline level of profitability persists even in the absence of the measured taxation practices, which may be attributable to other unmeasured firm-specific factors such as market positioning, capital structure, and operational efficiency.

Tax Compliance: The coefficient of unstandardized value of tax compliance was 0.335, while its standardized Beta was 0.330, $t = 4.064$, and $p = 0.000$. There is evidence of the significant and positive association between tax compliance and profitability. An increase of one unit in tax compliance effectiveness would result in an increase of 0.335 units in the profitability of companies, keeping other variables constant. This result supports the findings of Owusu and Boateng (2022), who have revealed that tax compliance was a significant predictor of profitability of sub-Saharan African firms, as well as those by Zhou and Wang (2021), who have proved the significant and positive prediction of profitability by tax compliance among Chinese manufacturing firms.

Tax Incentives: The unstandardized coefficient was 0.154, Beta = 0.176, $t = 2.151$, and $p = 0.034$, establishing a statistically significant, albeit relatively weak, positive relationship between tax incentives and profitability. It represents the least effective of the three independent variables indicating that although tax incentives utilization is indeed an important factor in profitability, the influence of this variable is relatively less significant when tax compliance and tax administration have been considered. This finding is consistent with Boateng and Asamoah (2022), who observed that although tax incentives are helpful, they usually have relatively weak effects independently on the performance of firms when considering other factors related to taxation.

Tax Administration: The unstandardized coefficient was 0.343, Beta = 0.397, $t = 5.181$, and $p = 0.000$, showing a statistically significant positive impact on profitability. This finding is based on the theory of agency, which suggests that through transparent tax administration, clear tax ruling and dispute resolution process, there could be improved accountability and minimized information asymmetry between the management, tax administrators and stockholders. Tax administration stood out as the most significant predictor among the three independent variables, highlighting the importance of effective and transparent tax administrative process including time taken to process VAT refunds, dispute resolution and clarity of the ruling of the KRA.

CONCLUSION

The study concluded that taxation practices constitute important determinants of profitability among manufacturing firms listed on the Nairobi Securities Exchange, Kenya. Tax compliance affirms that timely and accurate fulfilment of tax obligations support effective financial management and contribute to sustainable profitability. Tax incentives are equally important, as they can reduce the tax burden on firms, improve the availability of financial resources, and create

opportunities for investment and business expansion. Tax administration remains an essential component of the taxation framework. Its role in ensuring efficient tax assessment, collection, communication, and enforcement can enhance tax certainty, reduce compliance costs, and support firms in maintaining sound financial performance.

Policy Recommendations

To strengthen tax compliance, listed manufacturing firms should institutionalize automated tax compliance systems that integrate return filing, VAT declaration, PAYE remittance, and excise duty payment into a centralized digital platform. Regular internal tax audits and staff training on evolving tax legislation should be embedded within the finance function's annual calendar to minimize the risk of penalties and reputational costs.

Policymakers, including the National Treasury and the Kenya Revenue Authority, should review and streamline the framework governing tax incentives available to manufacturing firms, ensuring that eligibility criteria, application procedures, and reporting requirements are clearly communicated and administratively straightforward. Simplifying access to tax holidays, duty exemptions, and capital deductions would encourage broader and more consistent utilization of these incentives across the listed manufacturing sector, ultimately supporting sector-wide profitability and investment.

Limitations and Future Research Direction

The current study focused exclusively on manufacturing firms listed on the Nairobi Securities Exchange, which limit the generalizability of the findings to manufacturing firms operating in other markets and to firms in other sectors. Future studies should extend the scope of investigation to include manufacturing firms that are not listed on the Nairobi Securities Exchange and firms in other sectors to enable comparative analyses across different organizational and industry contexts. Such comparative studies would provide a broader understanding of how taxation practices influence profitability across firms with varying sizes, ownership structures, regulatory environments, and resource bases. The regression model in this study explained 44.8% of the variance of profitability, indicating that other factors not examined in the present study also contribute to variations in firm profitability. Future research should therefore investigate complementary variables such as tax planning strategies, tax risk management, corporate governance practices, financial management practices, firm size, leverage, technological adoption, and macroeconomic conditions as potential determinants of profitability among listed manufacturing firms in Kenya.

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