

**ST' MARRY UNIVERISTY  
BUSINESSFACULTY  
DEPARTMENTOF ACCOUNTING**

**VAT PRACTICE AND COMPLIANCE WITH THE LAW  
(A CASE STUDS IN SELECTED LARGE TAXPAYERS IN  
ARADA SUB-CITY)**

**BY  
MISGUN GETANEH  
MISGANA DESTA  
MENBERE TESHOME**

**JUNE 2014  
ADDIS ABABA**

**VAT PRACTICE AND COMPLIANCE WITH THE LAW  
A CASE STUDS IN SELECTED LARGE TAXPAYERS IN  
ARADA SUB-CITY**

**A SENIOR ESSAY SUBMITTED  
TO THE DEPARTMENT OF ACCOUNTING  
BUSINESS FACULTY  
ST' MARRY UNIVERISTY**

**A RESEARCH PROPOSAL IN PARTIAL FULFILLMENT OF  
THE REQUIREMENTS FOR THE DEGREE OF BACHELOR  
OF ARTS IN ACCOUNTING**

**BY**

**MISGUN GETANEH  
MISGANA DESTA  
MENBERE TESHOME**

**JUNE 2014  
ADDIS ABABA**

# ST' MARRY UNIVERISTY

## VAT PRACTICE AND COMPLIANCE WITH THE LAW A CASE STUDS IN SELECTED LARGE TAXPAYERS IN ARADA SUB-CITY

BY

MISGUN GETANEH  
MISGANA DESTA  
MENBERE TESHOME

FACULTY OF BUSINESS  
DEPARTMENT OF ACCOUNTING

APPROVED BY THE COMMITTEE OF EXAMINERS

_____	_____
Department Head	Signature
_____	_____
Advisor	Signature
_____	_____
Internal Examiner	Signature
_____	_____
External Examiner	Signature

## **ACKNOWLEDGEMENTS**

First of all we would like to extend our sincerely thanks to our adviser, Ato Habtamu Eshete, for his invaluable and constant advice to carry out this research paper.

We would also like to acknowledge and appreciate the contribution of number of people who has led to the completion of this work. Special thanks go to all the LTO staffs and the companies that are participate on filling questionnaires.

And of course we would like to acknowledge Kifiya Financial Technology P.L.C, Compassion International Ethiopia and DH Geda our current employer for approving our study leave plan and abide to it to enhance our studies to the completion of the program.

Finally, but most of all we thanks GOD for giving the strength we needed to accomplish this task.

## TABLE OF CONTENT

TITLE	PAGE
Acknolegement.....	i
Table of contant.....	ii
List of Tables.....	iv
Abbrevations.....	v
1 INTRODUCTION .....	1
1.1 Background of the Study .....	1
1.2 Statement of the problem .....	2
1.3 Research Questions.....	2
1.4 Objective Of The Study .....	3
1.4.1General Objective.....	3
1.4.2 Specific Objectives .....	3
1.5 Significance Of The Study.....	3
1.6 Scope Of The Study .....	4
1.7 Research Design and Methodology.....	4
1.7.1 Research Design .....	4
1.7.2 Population And Sampling Technique.....	4
1.7.3 Type of  Data collected.....	5
1.7.4 Methods of Data Collection .....	5
1.7.5 Data Analysis Method .....	5
1.8. Limitation of The Study .....	5
1.9. Organization Of The Paper .....	6
2 REVIEW OF RELATED LITERATURE .....	7
2.1 Definition Of Taxation .....	7
2.2 Definition Of Tax .....	8
2.3 Objectives Of Taxation.....	9
2.4 Classification Of Taxation .....	11
2.5 History Of Vat .....	12

2.6 VAT In Ethiopia.....	12
2.7 Meaning Of Value Added Tax (Vat).....	13
2.8 Nature Of VAT .....	14
2.9 Types Or Kinds Of VAT.....	15
2.10 VAT Administration .....	16
2.11 Advantage And Disadvantage Of VAT.....	16
2.11.1 Advantage Of VAT .....	16
2.11.2 Disadvantage Of VAT.....	19
2.12 VAT Accounting .....	20
3 DATA PRESENTATION, ANALYSIS AND INTERPRETATION .....	25
3.1 Background Of The Organization.....	25
3.2 Analysis Of The Findings Of The Study.....	26
4 SUMMARY,CONCLUSIONS AND RECOMMENDATIONS.....	47
4.1 Summary .....	47
4.2 Conclusion.....	48
4.3 Recommendation.....	49

## LIST OF TABLES

Table 3.1.	Staff by Gender in LTO .....	27
Table 3.2.	Staffs By Age Group In LTO .....	28
Table 3.3.	Educational Levels of Employees In LTO.....	29
Table 3.4.	Staffs By Years Of Services In LTO .....	30
Table 3.5.	Evaluating The Implementation Of VAT .....	31
Table 3.6.	Problem Related To VAT Application .....	32
Table 3.7.	Feeling Of VAT Registered Parties .....	33
Table 3.8.	Responsibility Towards Collection Of VAT .....	34
Table 3.9.	Problem Exist While Collecting VAT .....	35
Table 3.10.	Awareness Of Tax Payers About VAT .....	36
Table 3.11.	Shows The Attitude Of Tax Payer To VAT.....	37
Table 3.12.	Beneficiaries From VAT .....	38
Table 3.13.	Business Types Of Respondents .....	39
Table 3.14.	Year Of Services In The Business.....	40
Table 3.15.	VAT Payment Situation .....	41
Table 3.16.	Respondents Registration Situation.....	42
Table 3.17.	Attending Awareness Creation Training .....	43
Table 3.18.	Major Problems On The Application On And Collection Of VAT ..	44
Table 3.19.	Respondents Penalty Payment Experience .....	45
Table 3.20.	Respondents Late Payment Experience.....	45
Table 3.21.	Respondents Preferred Date To Declare VAT .....	46

## **ABBREVIATIONS**

VAT	-	Value Added Tax
GST	-	Goods and Services Tax
TOT	-	Turn Over Tax
LTO	-	Large Tax payer Office
FDRE	-	Federal Democratic Republic of Ethiopia
ERCA	-	Ethiopian Revenues and Customs Authority
BDS	-	Business Development Services
SPM	-	Selected Planning and Management
TCA	-	Tax and Customs Administration



# CHAPTER ONE

## INTRODUCTION

### 1.1 Background of the study

Taxation is a system of compulsory contributions levied by a government or other qualified public body on people, corporation and property in order to fund public expenditure in deciding who, what and how much to be taxed. All government has economic and social objectives. (Encarta, Taxation)

Tax is compulsory levy to a person who is eligible for tax payment on the basis of the prescribed tax criteria . Those persons on whom the taxes are imposed have no other choice than paying. Refusal to pay tax can lead to punishment by law. If tax were not a compulsory contribution, no one would probably be willing to pay it. (Misrake Tesfaye; 2011 G.C)

VAT is a tax not on the total value of the good being sold, but only on the value added to it by the last seller who is liable to pay a tax not on its gross value, but net value, that is the gross minus the value of inputs. (Bahitia, HL; 1998)

VAT is an indirect tax that is charged whenever a taxable person makes a taxable supply of goods and services in the course of his business although it is finally born by the consumer. (Hancock; 1995)

The government of Ethiopia has undertaken a comprehensive tax since July 2002 and changing the former sales tax to VAT. All domestic and foreign enterprises are subject to both direct and indirect taxation. Indirect taxes are mainly VAT, TOT

and other consumption taxes. The government of Ethiopia implemented VAT by proclamation number 285/2002 and by regulation No. 79/2002, although collection of VAT started from January 1, 2003. (ERCA manual)

Therefore, the purpose of this research is to assess the VAT practice and compliance with the law on the selected large tax payers in Arada sub-city.

## **1.2 Statement of the problem**

Taxation is the process of raising money to finance government at all level, local state and national require people and business to pay taxes. Among types of taxes value added tax belongs to sales tax. Therefore it were helpful if we briefly distinguish between different forms of sales tax. A general sales tax is a tax on sales transaction but it is applied at only one stage of business activity from manufacturing to retailer.

Value Added Tax (VAT) is a general consumption of tax assessed on the value added to goods and services. It is a general tax that applies in principle to all commercial activities involving the production and distribution of goods and the provision of services. It is a consumption tax because it is borne ultimately by the final consumer. It is not a charge on companies. It is charged as a percentage of prices, which means that the actual tax burden is visible at each stage in the production and distribution chain. It is collected fractionally, via a system of deductions whereby taxable persons (i.e., VAT-registered businesses) can deduct from their VAT liability the amount of tax they have paid to other taxable persons on purchases for their business activities. This mechanism ensures that the tax is neutral regardless of how many transactions are involved. "VAT" - value added tax has spread throughout the world since its introduction in 1955. Its format has

changed and now incorporates what was once an offshoot - "GST" (Goods and Services tax.)

The study has significant role in providing information for both the government and the taxpayer's. Value Added Tax is a recent phenomenon for Ethiopian people and its economy. The introduction of VAT law is intended to be a tax and final consumers or businesses buying goods or services. Manufacturer and retailers do not bear the effect (impact) of VAT; rather they transfer taxes to their ultimate consumers. Thus it is the consumers and businesses can usually pass the VAT that they pay on their purchase of similar goods and services to their own consumers. So, that the only cost they incur as a taxpayer are the cost of recording administering and collecting the available tax revenue from their customers for the benefit of government.

Various problems were encountered during the implantation of VAT for the past few years. Of the many challenges encountered knowledge towards VAT issue, negative attitude developed for VAT and lack of the required level of skills on collecting VAT are worthy mentioning. Hence, this study is designed to conduct on assessment on the current practice of VAT collection processes and activities.

### **1.3 Research questions**

Specifically this study is thoroughly answering the following questions:

- ❖ What are the strengths and weaknesses of VAT collection in Arada Sub city?
- ❖ To what extent is VAT payer developed awareness towards VAT?
- ❖ What are the challenges faced by VAT collection in Arada Sub City?

## **1.4 Objective of the study**

### **1.4.1 General objective**

The general objective of the study is to see and assess the practice and compliance with the existing VAT law on selected large tax payers.

### **1.4.2 Specific objectives**

The specific objectives of the study are:-

- ❖ To see the strength and weakness of VAT collection in Arada Sub-city.
- ❖ To assess the level of VAT payers awareness towards VAT.
- ❖ To assess VAT collection challenges in Arada Sub-City.
- ❖ To make recommendation and solution.

## **1.5 Significance of the study**

This study has been the following significance:

- ❖ Help to develop the researcher's experience.
- ❖ It has been provide the meaningful information to those interested in VAT.
- ❖ To explore the problem of VAT administration.
- ❖ It serves as a basis for further investigation in the area of VAT related issues.

## **1.6 Scope of the study**

The research study focuses on the assessment of VAT practice and compliance with the law. Since it is difficult to assess the whole VAT payers, it emphasizes

only the selected large tax payers in Arada sub-city that means among the business people whose annual sales are greater than or equal to 27 million birr. The researchers also believe that selected large tax payers represents the whole large tax payers and also the study conducted in large tax payer office (LTO), to see the VAT practice and compliance with the VAT law. The study were consumed around 5 months from proposal development to paper defense, February 2014- June 2014.

## **1.7 Research Design and Methodology**

### **1.7.1 Research design**

The research is description. this choice was dictated by the purpose of the study being requirements for BA degree and insufficient time and logistics.

### **1.7.2 Population and sampling technique**

The target population considered in this study is large tax payer organizations in Arada sub-city which means among the business people whose annual sales are greater than or equal to 27 million birr and the staffs of large tax payers office (LTO).

In aggregate there are 1,010 large tax payers in Addis Abeba. From these 86 of them are located in Arada sub-city. Among the total population of large tax payers in Arada sub-city the data has been collected from 55 large tax payers who are engaged in various business area in Arada sub-city. These samples has been selected using randomly sampling techniques. The researchers use sampling because of the shortage of finance and time constraints. The sample size has been determined by personal judgment and budgetary approach.

On the other hand, totally there are 315 employees working in large taxpayers Office. Out of these 34 employees who are directly related to VAT collection activities are our target populations. Since the size of population, 34, are manageable all the population used as respondents.

### **1.7.3 Type of data collected**

The valuable information, which is critical for this survey, has been obtained from both primary and secondary sources.

### **1.7.4 Methods of data collection**

The primary data has been gathered using questionnaires and the secondary data has been gathered through published and unpublished document such as: journals, conference papers, books, proclamation and various other sources of data issued by ERCA.

### **1.7.5 Data analysis method**

The analysis part of the study has been devoted to analyze and interpret the collected data. The information that gathered through questionnaire is analyzed by using qualitative method and it has been presented using simple statistical measures such as percentage and tables.

## **1.8 Limitation of the study**

To conduct this study there were various limitations. Some of these are:

- ❖ **Time:** It was the main resource to study the research. The time which was given to study is not sufficient. So this is one of the limitations to conduct the research.
- ❖ **Financial Problem:** To conduct the study sufficient amount of money was important. It is vital resource to copy materials, secretaries, transportations, stationaries and other costs. As a result of these costs, it was difficult to afford to do the research.

### **1.9 Organization of the paper**

The paper has four chapters. The first chapter is an introductory part which contains backgrounds, statement of the problem, objectives, significance, scope and methodology of the study. The second chapter deals with review of the related literature. The third chapter is about the data presentation and analysis. The last chapter contains summary, conclusion and recommendations.

## CHAPTER TWO

### LITERATURE REVIEW

#### 2.1 Definition of Taxation

Taxation is a system of raising revenue by a government through tax. It is a system of collecting money by a government to finance the government operations. Every government is expected to fulfill at least three operations.

1. Defense of the country
2. Maintenance of law and order, and
3. Socio-economic development

Defense is given the top priority by every government with the result that a major portion of the resources is devoted to fulfill its obligation towards defense management which becomes important to keep the sovereignty and integrity of the country in fact. Equally important is the maintenance of law order without which the country may be exposed to conflict between different social groups and other forces of social unrest to the point of dragging the country to the brink of civil war which may pose a serious threat to the farer of nationhood .Socio-economic development such as the provision of social amenities in the form of education, health and sanitation faculties, the services of public utilities like electricity and water supplies , infrastructure of transportation and communication , recreation facilities, and support of the incapable. All those and other government functions require expenditures so that government support themselves parity by taking a portion of the wealth of their citizens. The chief means by which governments do this through tax. Then what tax? (Misrake Tesfaye 2011 G.C)

#### 2.2 Definition of Tax

Tax may be defined as a compulsory contribution (Levy) Payable by an economic unit to a government without expectation of direct and equivalent



return (quid pro quo) from the government for the contribution made. From this definition, it may be noted that tax:-

- ❖ Is not a voluntary but is a mandatory contribution. A person on that the tax is imposed can't refuse to pay it. Refusal to pay tax can lead to punishment by law. The contribution can be financial (money) or non-financial such as grains and Corves. Corves is a type of annual tax that is payable as labor by the serf or villain for the monarch, vassal, overlord of lord of the manor.
  
- ❖ Is contributed by an economic unit which is also called assesses or a tax payers. An assess is a person (an individual, a body or an association) who is liable to pay tax according to the rules and regulations prescribed by law.
  
- ❖ Is contributed to a central government, state government or a functional equivalent of a state such as tribes and secessionist movements.
  
- ❖ Is contributed without expectation of direct and equivalent return for the contribution made. This means, there is no direct relationship between the compulsory contribution to a government and the amount of the service received from the government for the compulsory contribution made. Rather, the benefits of government expenditures may go to any one irrespective of the taxes paid, thus, a compulsory contribution in order to be a tax; the absence of quid pro quo is must. (Misrake Tesfaye 2011 G.C

### **2.3 Objectives of Taxation**

Earlier it has already been stated that tax is a compulsory contribution without direct and equivalent return for the contribution. Then, why does a government impose tax? Here are the main objectives of taxation. (Misrake Tesfaye 2011 G.C)

## **Raising revenue by a government to finance expenditures of its activities**

The primary objective of taxation is to raise revenue by a government to support expenditures of its activities. A government as a body has a number of activities to its society. Some of the activities are the provision of social amenities such as education, health, and sanitation facilities; the provision of public utilities such as electricity supply, and communication means; maintaining law and order in the country; and defense. All those activities require expenditures, and governments use primarily taxation to raise revenue and support its expenditures. (Misrake Tesfaye 2011 G.C)

## **To minimize income and wealth inequalities**

To narrow the gap between the rich and the poor, most governments adopt progressive taxation system. In such system the higher income groups pay more amount of tax, the middle income groups pay lower amount of tax and the lower income groups are exempted from tax. Then, the taxes collected from the higher and middle income groups are used by the government subsidize the lower income groups and unemployed. (Misrak Tesfaye 2011 G.C)

## **To ensure economic stability/ stabilize economy**

Governments use taxation to control inflation and deflation (depression) Pressures. During inflation period, governments may increase the existing tax rates or impose additional taxes to reduce the abnormal (excess) demand. During deflating period, governments may reduce the existing tax rates or remove certain taxes to increase demand and encourage business activities. Thus, taxation has role in economic stabilization. (Misrake Tesfaye 2011 G.C)

### **To discourage the consumption of harmful products**

By imposing high/heavy taxes on harmful products that worsen people's health such as tobacco and alcoholic products, governments can reduce the consumption of such products. For instance, in Ethiopia case tobacco products are subject to 20% - 75% excise tax and alcoholic products are also subject to 50% - 100% excise tax. Imposing heavy taxes on such products increases their price and the majority of the society may be discouraged to buy those products. (Misrake Tesfay 2011 G.C)

### **To promote private investment**

Through the provision of tax exemption, tax recession (reduction) and tax holiday, government's promote private investment in their countries. For instance, to promote investment in the country, the Ethiopian government grants exemption on business profit tax and customs duty association with investment on an approved manufacturing and agro-industry from 2 to 8 years. Depending up on the area of investment, the volume of export and the location in which the investments are undertaken. (Misrake Tesfye 2011 G.C)

### **To enhance capital formation/accumulation**

Government may give tax exemption or recession (reduction) on income derived from saving such as deposit, investment in provident funds, life insurance and financial assets like treasury bills, bond and shares that can lead to large amount of capital formation which is essential for future investment and reinvestment. (Misrak Tesfaye Jan 2008 )

## **2.4 Classification of Taxation**

Taxes are a compulsory levy, imposed by government, on either income expenditure per capital assets, for which the tax payer receives nothing

specific (Hancock, 1995) The money received in this regard is to be utilized for financing develop efforts of a country . Two types of taxes can be identified direct taxes and indirect taxes. (Hancock, 1995)

A. Direct tax & B. Indirect tax

### **A. Direct tax**

- ❖ Are demanded from the every person who it is intended on desired should pay it
- ❖ Is either really paid by the person on whom it is legally imposed on one person but it is paid portly of fully by another person
- ❖ which are based on the receipt of income is retuned direct, where as those levied on expenditure one direct tax.
- ❖ Is the whose burden is born by the person on whom it is levied, the cannot transfer the burden of the tax to some other person
- ❖ In the case of a direct tax both the impact an incident of tax pall on the same person.(Hancock, 1995)

### **B. Indirect tax**

- ❖ Are those which on demand from one person in the expectation an intention that he/she shall indemnity himself at the expense of the other.
- ❖ According to this criterion a sales tax, custom duty, or on excise they would be indirect tax.
- ❖ Indirect tax is that far which is initially paid by the one individual but the burden of which is ultimately borne by another individual.
- ❖ The impact an incidence of tax falls on different person. (Hancock, 1995)

## **2.5 History of VAT**

Emergence and rapid spread of VAT is among the most important tax development of the later 20<sup>th</sup> c VAT invested in 1954 by a French economist

Maurice Laurie who was joint director of the French tax authority. The theory is that the end consumer carries the burden of VAT, not the business, which is merely collecting the VAT on behalf of tax authority. According to international monetary fund report 2004, more than 4 billion, 70% of the world population now live in countries with VAT, raise about 18 trillion in tax revenue, roughly one quarter of all government revenue over 136 (72%) of them have made VAT part of their tax system, and from 53 member of countries of African union 33(60%) of them are introduced VAT ( Gebrie , 2008,pp.186-187).

## **2.6 VAT in Ethiopia**

VAT is a new tax system introduced in Ethiopia this tax system is not new to other countries. The modern concept of VAT was truly introduced in France in 1954. The concept of VAT was propounded first by American experts by 1920's. But at that time Americans failed to implement it. In Ethiopia, VAT was introduced since January 1/2003 designed to replace the cut dated sales tax which was served for more than four decades, which was collected at manufacturing level. VAT is taken as dispensable components of tax reforms in developing countries such as Ethiopia by considering it a miracle tax to replace direct and indirect taxes entirely. Since 1993 the Ethiopia government has made major economic shift from central planning to market oriented economic system (Yohanes and Sisay, 2009, pp. 186-187).

## **2.7 Meaning of Value Added Tax (VAT)**

Different authors who wrote about the tax have defined value added tax ( VAT ), According to encyclopedia Britannica VAT is "A sales tax designed like other sales taxes to tax private consumption by individual of the goods or services subjected to tax" this definition failed to list out other features that

distinguishes VAT from other kinds of taxes. One can understand from this definition VAT is a variety of sales tax and the tax is imposed on consumer. Black law dictionary on its parts provides that "VAT is a tax assessed at each step in the production of a commodity production on cost and its selling price" (Yohanes and Sisay, 2009 pp.66).

The VAT belongs to the family of sales tax a VAT way be defined as "a tax to be paid by the manufactures or traders of good and service on the basis of value added by them" . It is not a tax on the value of the commodity being sold but on the value added to it by the manufacture or trader. They are not liable to pay the tax on the entire value of the commodity. But have to the tax only on the net value added by them in the production or distribution (Dr. R. Parameswaran, 2005, p. 105).

It is broad tax based because it is charge in different stage at production and distribution chain rather than on – time imposition. It also affects sectors, that is, import manufactures whole seller and retailer sector. VAT is family at sale tax sales tax is a tax imposed on a sale of goods or services and computed as a percentages of the total tax collected at multiple stage. VAT is a self-assessed tax since the VAT liability is calculated paid by the tax payers (proc, No 285/2002).

## **2.8 Nature of VAT**

VAT is characterized by the following features

- ❖ VAT is "general tax or comprehensive" that applies in principle to all commercial activities in valuing the production and distribution of good and provision of services.
- ❖ VAT is "consumption tax" because it is levied in sales of good and the provision of service rather than income, capitals or saving.
- ❖ VAT is "broad based tax" since the government collects such tax from all sectors that is importer, manufacturing whole sale, and retailer sector.

- ❖ VAT is “percentage of price” which means, the actual tax burdens is visible at each stage in the production and distribution chain.
- ❖ VAT is collected “fractionally” because each time the item is changes hand in the process of production and distribution the VAT is assessed on the incremental value.
- ❖ VAT is “neutral” because regress of how many transactions are involved VAT liability the amount of tax they have paid to other person on purchases for their business activities.
- ❖ VAT is indirect tax because VAT is paid total authority by the seller of the goods, who is the taxable person but it is actually paid by the buyers to the seller as part of the price.

The federal democratic republic of Ethiopia (FDRE) has adopted VAT in to be a tax system in 2003. It has been introduced on January 1/2003, replacing the former sale tax system. The VAT proclamation no 285(2002) has been ratified by the house of people representatives six months before VAT implementation.

VAT is introduced in Ethiopia by proclamation (285/2002 replacing sale tax, with the following objective.

- ❖ To collect tax on the added value whenever the sale transaction is conducted since the former sale tax system did not allow collection is conducted.
- ❖ To minimize the damage that may be caused by attempts to avoid and evade the tax and ascertain the profit obtained by tax payers
- ❖ To enhance economic growth and improve the rational relationship between the gross domestic production and gross revenues.
- ❖ To enhance saving and investment as it is a consumption tax and doesn't a tax capital.

## 2.9 Types or Kinds of VAT

The VAT can be determined in different forms. It may way depend up on the form of tax base. The forms may differ on the items to be included in the tax base.

The common type of VAT is given below:-

**A. Consumption VAT:** in the type of VAT the firm is allowed to deduct from gross value of its product not only the non-capital input purchased from other firm but also the capital equipment purchased.

**B. Production VAT:** in the production type VAT the value of the input purchased by the firm from other firms is not dedicated in full only the value of non-capital purchases is dedicated.

**C. Income type:** according to this form the firm is allowed to deduct the depreciation of the capital goods (during the year) a part of the full value of its non-capital purchase. Here, firms cannot deduct the entire value of its capital goods purchased during the year but they can deduct the respective amount of depreciation attributable to that year (Dr. R. Parameswaran, 2005 p.106)

## 2.10 VAT Administration

The VAT replaced the current sales tax on manufactured and imported goods and service on January 1/2003. The responsibility for the correct calculation and timely payments of VAT rests on the Tax payers himself. The VAT is a broad based tax on the consumption of goods and service. It is collected at all the stages in the production and distribution process

beginning with the importers and producers of raw materials and ending with retailers cascading of the tax (i.e.

tax on tax is avoided by providing for a credit for the tax paid at the preceding level unlike the sales tax system, where relief is granted only to raw materials used directly in the production of goods under a VAT relief is granted for tax paid on capital goods, distribution and administration inputs. Sales of exported goods are not subject to the VAT.



Removing the tax content (on input) from exported goods makes the goods more competitive in international markets. VAT is a tax on consumer expenditure. It is collected on business transaction and imports. Most business transaction involve supplies of goods or service and VAT is payable if they are supplies made in Ethiopia, made by a taxable person, made in the course of furtherance of a business are not specifically exempted or zero-rated ( Gebrie, 2008, pp. 190-191) .

## **2.11 Advantage and Disadvantage of VAT**

### **2.11.1 Advantage of VAT**

The following are some of the advantages of VAT

#### **a. It avoids cascading effect of tax (tax on tax)**

VAT works on the principle of that when the raw material passes through various manufacturing stages and manufactured products through various distribution stages, tax should be levied on the incremental value at each stage and not on the gross sale price. This insures that some commodity does not get taxed again and again, and this there is no cascading effect. Putting the concept in simple terms, in VAT system, each input is taxed only once (Misrak, 2008, p. 310).

#### **b. It is major comprehensive and equitable tax system**

Even though the ultimate burden of VAT full on the final customer, VAT is collected by the government from all sectors that is from import manufacturing, whole sale and retail sectors. Therefore, it is a more compressive and equitable taxes system. On the contrary, sales tax is normally levied at one stage of whole marketing (Misrak, 2008, p. 310).

**c. It reduces the possibility of the tax erosion**

In the case of VAT the taxes are divided into several parts depending on the number of stage of production and sales. In each stage every transaction is made using VAT invoice approved by tax authority. In addition each VAT registered person (supplier) has to maintain appropriate records on their sale and purchase transaction. Those obligations make tax evasion difficult (Misrak, 2008, p. 310).

**d. It has less tax burden**

Under VAT system, the tax is collected in small fragments at different stage of production and sale. Hence, the VAT payers feel the burden of the less (Misrak, 2008, p. 310).

**e. It is neutral**

Regardless of the number of stage of production and distribution, VAT is collected in each stage, therefore; VAT is expected to be perfectly neutral in the location of resources in the form of production and commercialization (Misrak, 2008, p. 310).

**f. It improves productivity**

VAT system, a firm has to pay tax even though it goes into loss. The firm cannot claim any exception for loss because it pays taxes on the value produced and not on profits. So, firms will always try to improve their performance and reduce the cost of production. As a result, the overall productivity of the country will be improved (Misrak, 2008, p. 310).

**g. It promotes capital investment and saving**

VAT is a consumption tax since one pays VAT on its expenditure and has the option to save so as not to be taxed. Furthermore, relief from tax on capital

goods may encourage investment. Potential investors also consider tax legislation as one of the factors in making investment decision (Misrak, 2008, p. 311).

#### **h. It enhances exports**

Exports of goods and services in most countries that implement VAT are liable to VAT. At zero rates this may make exports internationally competitive and thus encourage exports (Misrak 2008, p. 311).

### **2.11.2 Disadvantage of VAT**

The following are some of the main disadvantages of VAT

#### **a. It is regressive in nature**

A straight forward single rate VAT with few exemptions would tax lower income groups (the poor) more heavily than the higher income groups (the rich). It is thus incongruent with the basic.

Principles of taxation which states that reason should be taxed according to his ability to pay. This makes VAT regressive tax system.

In order to compensate for its regressive effect a number of countries have exempted basic goods particularly food items from VAT (Misrak, 2008, p.311).

#### **b. It require advanced economic structure**

The proper implementation of VAT system required organization and advanced financial and economic structure as it complicated system. VAT system also requires proper record keeping of invoice at each stage of production and sale by both the seller and buyer. Hence, it becomes, difficult

to implement the system in all types of economy (Misrak, 2008, p. 312)

**c. It put additional burden to tax authority**

In VAT system, the manufactures whole sellers and retailers have to fulfill various legal formalities in the form of manufactures various records, accounts, books, etc. the verification of those formalities put additional burden to the enforcing authorities (Misrak, 2008, p. 312).

**d. It is uneconomical**

VAT system involves high of administration, assessment, verification collection, etc. hence; it is highly uneconomical (Misrak, 2008, p. 312).

**e. It has reams loopholes for tax evasion**

Although VAT system requires proper record keeping of invoices at each stage of production and distribution by both the buyer and seller, it has ream loopholes for tax evasion. This may include the following:

- ❖ Tax payers could over report sales of zero rated goods.
- ❖ Tax payers could use invoices they received for personal purchase to claim tax credits.
- ❖ It enables buyers and sellers to strike secret deals with regards the issuance of receipts.
- ❖ It could lead to the formulation of forged ponies' recipients to claim tax credit on input VAT, etc (Misrak, 2008, p. 312).

**2.12 VAT Accounting**

VAT accounting refers to the value of supply on which the taxpayer calculates VAT on VAT sales invoice and the subsequent record keeping process.

Impact on the salient features of the tax a government's policy objectives as a whole. In this regard, Tanzi and Election (1995) (cited in like ell (2007) noted that poor tax administration would change the manner in which taxation affects government's policy objectives, namely economic stabilization, resource allocation and redistribution of income. In developing countries the poor performance of taxes is likely to be daring to weal tax administration (i.e. the incapacity of the administration to implement the tax in practice). This is perhaps caused by such factors as resource constraint and signing the tax separately from the administration. Concerning the latter, Bird and Gendron (2005) noted that developing and transitional countries, unlike developed countries, appear to have fragmented economies. Large informal sectors, low tax morale, rampant evasion, and total distrust between tax administrators and taxpayers. In these countries, thus, simply adopting a successful VAT's design attributes of developed countries, thus, simply adopting a successful VAT's design attributes of developed countries would not make the tax successful (Bird and Gadroon 2005). The design ought to consider the tax administration dimension and the socio-economic developing country in question. In discussion the importance of tax administration in general, Bird (1989 and 2004) noted that tax administration dimension ought to be placed at the centre, not periphery, of tax reform. Jantscher (1990:179) also stated that "---- in developing countries tax administration is tax policy."

Considering the significance of the administration, many studies have been conducted in some developing and transitional countries with respect to the main VAT administration tasks. These studies include Jantscher (1990), demission and gird (2004), Bird and Gendron (2005), grand colas (2005) and Bird (2005). These papers assessed how VAT administrators in developing and transitional countries perform their duties and how the effective taxpayer requirements differ from the legislation. More specifically, the analyzed focused on practices of different developing countries with respect to taxpayer identification. Invoicing, filing and payment process countries with respect to

taxpayer identification. Invoicing, filing and payment process control of filling and payments, refunds, audits and penalties. In addition, the costs of VAT administration were briefly examined in the case of Jantscher's (1990) study. The main conclusion of these studies is that VATs prevailing in developing countries were quite different from the broad based tax discussed in public finance literature and that administrative problems, in turn, may be partly caused by administrative constraint.

VAT administrative costs can include costs incurred by tax authorities in performing the tasks entrusted to them. In developing countries, estimates of VAT administrative costs are scant. In fact, as a measure of efficiency some governments attempted to develop percentages of administrative costs to the revenues generated by taxes. In the case of VAT, Jantscher (1990) indicated that fragmentary data, supplemented by the impressions of administrators, suggest that administrative costs usually range between one and two per cent of the VAT revenues collected. In addition to the administrative activities and the availability of administrative resources, VAT administration deals with issues such as administrative organs (who should administer the tax) and their mode of organization. Of particular importance for this paper is the VAT administrative organ. It suffices, however, to note that for successful VAT the significance of appropriate institutional setup with proper human and material deployment must not be underestimated.

In respect of the VAT administrative organs, as Martinez-Vazquez and Timorese (2005) noted the assignment of responsibilities ought to be seen as an element that must interact and be compatible with the rest of the design of a decentralized financial system. The decision (who should administer VAT) should be made within the framework of the overall fiscal system, particularly the assignment of VAT. In this context, examination of the theory of fiscal federalism shows the guidelines for the assignment of functions and fiscal instruments to different levels of government. According to this theory, the central government should have the basic responsibility for macro economic stabilization, income redistribution and resource allocation (Musgrave 1959

and oats 1972 cited in Pates 1999). In view of this conventional theory and the practical difficulties of implementing the tax, sub-national VATs were considered to be unfeasible. In this regard, Bird and Gendron (1998) quoted that the usual understanding was not to assign the VAT to sub-national governments (McLure 1993) and that the simplest practical way to run a federal state sales tax system including VAT was to adopt a revenue sharing scheme similar to the federal republic of Germany (Tait 1988). As a result, in most countries that have already introduced VAT, the tax has been assigned to central (federal) governments.

However, against the above supposition that sub-national VATs are unworkable, recently, tax experts including Dined Geneon (1998), Bird (2001), and McClure (2000). And Keen and Smith (1996 and 1999) argued that sub-national VATs are feasible. Their arguments used the Canadian dual VATs and the VATs in the European Union member states as evidence they suggested different structures of sub-national VATs including dual and compensating VATs, which require a good administration and information exchange among tax authorities. More specifically, Bird (2001) suggested that compensating VAT would be fairly feasible and potentially attractive in developing countries—at least in large countries in which states have major expenditure role, the VAT is the major source of actual and potential revenue, and tax administration is not up to developed countries' standards. In general, however, according to Bird and Gendron (2005) in the context of developing and transitional countries a centralized VAT with some of the

Revenues shared with regional governments on a formula basis are the best approach to finance regional governments.

Following the assignment of VAT revenue, the question would be who should administer VAT? On this issue there are different possibilities, the extreme ones being central government only (centralized) or regional governments only (full decentralized). Between these two extremes there may be different

arrangements. There are arguments, at least conceptually, on the advantages and disadvantages of centralized and decentralized tax administration in terms of economies of scale and cost efficiency. Mikesell (2007) noted that innovation of new approaches and techniques are cited as advantages of decentralized administration while economies of scale and expertise are for a centralized administration and constraints involved are weighted and also on the nature of the tradeoff among them examine the VAT practices. It is, hence, not known whether the administration of VAT in Ethiopia is per the legislation, and which features of VAT are being affected due to administrative weaknesses. Furthermore, in Ethiopia, administrative practices that are compromising the VAT's In general, it can be concluded that although there have been stales on VAT administration in some developing countries. In Ethiopia there are no comprehensive studies that operation are not known. In this context, the objectives of this paper are to examine the practice and compliance of VAT with the law and identify the main problems that deserve the government's sue attention, and briefly examine the decentralization of VAT revenue and administration as a way forward for future research.



## CHAPTER THREE

### Data Presentation, Analysis And Interpretation

#### 3.1 Background of the Organization

The Ethiopian Revenues and Customs Authority (ERCA) is the body responsible for collecting revenue from customs duties and domestic taxes. In addition to raising revenue, the ERCA is responsible to protect the society from adverse effects of smuggling. It seizes and takes legal action on the people and vehicles involved in the act of smuggling while it facilitates the legitimate movement of goods and people across the border. The ERCA traces its origin on July 7, 2008 as a result of the merger of the Ministry of Revenues, the Ethiopian Customs Authority and the Federal Inland Revenues into one giant organization. ([www.erca.gov.et](http://www.erca.gov.et))

According to article 3 of the proclamation No .587/2008, the Authority is looked upon as "an autonomous federal agency having its own legal personality". The Authority came into existence on 14 July 2008, by the merger of the Ministry of Revenue, Ethiopian Customs Authority and The Federal Inland Revenue Authority who formerly were responsible to raise revenue for the Federal government and to prevent contraband. Reasons for the merge of the foregoing administrations into a single autonomous Authority are varied and complex. ([www.erca.gov.et](http://www.erca.gov.et))

#### **Vision**

To be a leading, fair and modern Tax and Customs Administration in Africa by 2020 that will finance Government expenditure through domestic tax revenue collection. ([www.erca.gov.et](http://www.erca.gov.et))

## **Mission**

ERCA will contribute to economic development and social welfare by developing a modern Tax and Customs Administration that employs professional and highly skilled staff who promote voluntary compliance amongst individuals and businesses, and take swift action against those who do not comply. (www.erca.gov.et)

## **Values**

ERCA will understand its customers and their needs, treat them with trust and respect and help them meet their obligations. We will act with integrity, transparency and professionalism, and enforce customs and tax related laws. We will work closely with stake holders and ensure the participation of women. (www.erca.gov.et)

## **Organizational Structure**

The ERCA has its headquarters in Addis Ababa. It is led by a Director General who reports to the Prime Minister and is assisted by five Deputy Director Generals, namely D/Director General for Program Designing of Operation and Development Businesses; D/Director General for Branch offices' Coordination and Support; D/Director General of Enforcement Division; D/Director General, Corporate Functions Division; Change Management and Support Sector; and Enforcement Sector. Each deputy director general oversees at least four directorates. Both the Director General and the Deputies are appointed by the Prime Minister. (www.erca.gov.et)

## **3.2 Analysis of the Findings of the Study**

In this section data collected from LTO staffs and selected large tax payers in Arada sub city through questionnaire are presented. The researchers distributed 34 questionnaires to LTO Staffs, who are directly related to VAT activities, but out of them only 28(82.35%) were collected. Also the researchers distribute questionnaire to 55 randomly selected large tax payers in Arada Sub-City. All which means 100% of the questionnaires filled and returned by those large tax payers.

The Researchers used the completed and returned questionnaire to present and analysis the data.

### **Data Analysis of the Findings of LTO Staffs**

In this section the data collected from 28 LTO staffs through questionnaires are analyzed and interpreted.

#### **3.2.1 Background of Respondents**

It is important to assess the background of respondents to enhance employee contribution for the success of the organization. Assessment of manpower distribution helps the organization to forecast the required number of and quality of employee in the work of the organization.

The researchers try to assess background of the respondents by gender, age, level to education and years of service within the organization.

**Table 3.1** Staff by Gender in LTO

No	Description	No of respondents	Percentage
1	Gender		
	Male	18	64
	Female	10	36
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.1 indicates that the distribution of LTO employees by gender. According to the respondents 18(64%) of the sample respondents are male and 10(36%) of the sample respondents are female .This indicates the number of male employee is greater than female.

**Table 3.2** Staffs By Age Group In LTO

No	Description	No of respondents	Percentage
1.	Age in Year		
A	18-24	11	40
B	25-30	9	32
C	31-35	4	14
D	Above 35	4	14
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.2 indicates that the age distribution of employee in LTO. Out of total respondents 11(40%) are between 18 and 24 years, 9(32%) are between 25

and 30 years, 4(14%) are between 31 -35 years and 4(14%) are above 35 years.

From these the researchers can conclude that LTO has more employees of between 18 and 30 years ages people.

**Table 3.3** Educational Levels of Employees In LTO

No	Description	No of respondents	Percentage
1.	What is your educational level?		
A	High school complete	-	-
B	Certificate	2	7
C	Diploma	5	18
D	Bachelor Degree	18	64
E	Above degree	3	11
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.3 indicates the educational level of LTO employees. Of the sample respondents 2(7%) are certificate, 5(18%) are diploma, 18(64%) are bachelor degree and 3(11%) are above Bachelor Degree. From this the researchers can conclude that most of the employees in LTO are bachelor degree holders.

**Table 3.4** Staffs By Years Of Services In LTO

No	Description	No of respondents	Percentage
1.	How long have you been working in LTO?		
	A. Less than 1 years	9	32
	B. 1-2 years	13	47
	C. 2-4 years	2	7
	D. Above four year	4	14
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.4 indicates the year service of workers in LTO from total respondents 9(32%) are below 1 year service 13(47%) are between 1 and 2 years' service, 2(7%) is between 2 and 4 years of service and 4(14%) are above 4 years' service.

There for the researchers conclude that most of the employees in LTO have experiences of between 1 and 2 years.

### **3.2.5 Evaluating The Implementation Of VAT In LTO**

Respondents were asked that have do they evaluate the implementation of VAT in their office. The respondents response are given below.

**Table 3.5** Evaluating The Implementation Of VAT

No	Description	No of respondents	Percentage
1.	How do you evaluate implementation of VAT in your administration?		
A	Very good	4	14%
B	Good	15	54%
C	Fair	9	32%
D	Bad	0	-
	<b>Total</b>	<b>28</b>	<b>100%</b>

Source: Compiled from questionnaire

As shown in the above Table 3.5 the evaluation on the implementation of VAT, 4(14%) of the respondents said that the implementation of VAT in LTO is very good, 15(54%) of the respondents said good and the remaining 9(32%) of the respondents said fair. The researchers conclude that the implementation of VAT at the administration is good.

### **3.2.6 Problem Related To VAT Application**

The problems related to VAT application that experienced by the employee are shown in the table below

**Table 3.6** Problem Related To VAT Application

No	Description	No of respondents	Percentage
1.	What are the major problems you have experienced to VAT application?		
	A. unwillingness of tax payers	8	28
	B. Late Payment of VAT	7	25
	C. lack of awareness about VAT	12	43
	D. others	1	4
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.6 indicates the problems that related to VAT application. According to the respondents 8(28%) of the VAT application problem is unwillingness of Tax payers, 7(25%) are late payments of VAT, 12(43%) of the respondents said lack of awareness about VAT and the remaining 1(4%) said all of the above problems are shown.

This indicates the main problem of VAT application is the lack of awareness about VAT.

### **3.2.7 Feeling Of VAT Registered Parties**

The respondents were asked about the feeling of VAT registered parties. The respondents response are given below



**Table 3.7** Feeling Of VAT Registered Parties

No	Description	No of respondents	Percentage
1.	How do you evaluate a feeling of VAT registered while they registered for VAT?		
	A. Feel very Good	4	14
	B. Feel Good	8	29
	C. Feel Fair	12	43
	D. Feel Bad	4	14
	E. others	-	-
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

As shown in the above table 3.7, 4(14%) of the respondents said that the feeling of VAT registered parties are very good, 8(29%) are said feeling good, 12(43%) said feeling fair and 4(14%) of the respondents said that they feel bad. Therefore most of the VAT registered parties feeling fair.

### **3.2.8 Responsibility Towards Collection Of VAT**

The responsibility towards collection of VAT is shown as follows:

**Table 3.8:** Responsibility Towards Collection Of VAT

No	Description	No of respondents	Percentage
1.	Who is more responsible for VAT collection?		
	A. Tax payers	3	11
	B. Customers	1	4
	C. Any government body	4	14
	D. Tax office	17	60
	E. Others	3	11
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.8 above indicates that a more responsible parties for VAT collection. Our of total respondents 3(11%) are said tax payers, 1(4%) are said the customer,4(14%) are said any government body ,17(60%) are said tax office and the remaining 3(11%) are said others. This sample indicates that tax offices are more responsible for VAT collection.

### **3.2.9 A problems Exist While Collecting VAT**

The respondents were asked about the problems exist while collecting VAT. The respondent's response is given below.

**Table 3.9** Problem Exist While Collecting VAT

No	Description	No of respondents	Percentage
1.	What are problem you have faced while collecting VAT?		
	A. Most of tax payers not pay a required amount on time	9	32
	B. All of tax payers not pay a required amount on time	5	18
	C. Less of tax payers not pay a required amount on time	14	50
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.9 indicates the problem exist while collecting VAT. Out of total sample respondents 9(32%) are said most of tax payers not pay a required amount on time, 5(18%) are said all of tax payers not pay a required amount on time and 14(50%) are said less of tax payers not pay a required amount on time. This indicates the problem exist while collecting VAT is some tax payers do not pay their tax liabilities within the time.

### **3.2.10 Awareness Of Tax Payers About VAT**

The respondents were asked the awareness of tax payers about VAT. The respondents response are given below

**Table 3.10:** Awareness Of Tax Payers About VAT

No	Description	No of respondents	Percentage
1.	How do you evaluate the awareness of tax payers about VAT?		
	A. very high	2	7
	B. high	8	29
	C. low	14	50
	D. very low	4	14
	<b>Total</b>	<b>28</b>	<b>100</b>
2.	How do you judge the awareness of VAT payers in the Arada Sub-City?		
	A. They have Very good awareness	7	25
	B. They have good awareness	2	7
	C. They have less awareness	12	43
	D. They have poor awareness	7	25
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

As refer from the above Table 3.10 of item number 1 the awareness of tax payers about VAT, 2(7%) said it is very high, 8(29%) said it is high,14(50%) said it is low and 4(14%) are said it is very low. This indicates the awareness of tax payers about VAT is low.

As shown in item number "2" of table 3.10 respondents response about the awareness of tax payers about VAT in Arada sub-city shows 7(25%) are said

that they have a very good awareness, 2(7%) are said that they have good awareness, 12(43%) are said they have less awareness and the remaining 7(25%) are said they have poor awareness. This shows the awareness of tax payers about VAT in Arada sub-city is less.

### 3.2.11 The Attitude Of Tax Payers To VAT

The respondents were asked about the attitude of tax payers to VAT .the respondent's response are given below.

**Table 3.11** Shows The Attitude Of Tax Payer To VAT

No	Description	No of respondents	Percentage
1.	What do you judge the attitudes of tax payers to VAT?		
	A. very good	4	14
	B. Good	6	21
	C. low	11	40
	D. bad	5	18
	E. worst	2	7
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.11 indicates the attitude of tax payers to VAT. Out of the total respondents 4(14%) are said that it is very good, 6(21%) are said good, 11(40%) are said low, 5(18%) are said bad and 2(7%) said worst.

Therefore, the levels of attitude of tax payers to VAT are low.

### 3.2.12 Beneficiaries from VAT

The respondents were asked about beneficiaries from VAT. The respondent's response is given below:

**Table 3.12** Beneficiaries From VAT

No	Description	No of respondents	Percentage
1.	Who more benefited from VAT?		
	A. Tax payers	4	14
	B. Government	6	21
	C. Citizens of the country	18	65
	<b>Total</b>	<b>28</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.12 indicates the beneficiaries from VAT. Out of total respondents 4(14%) are said the tax payers get more benefit from VAT, 6(21%) are said government gets more benefit from VAT and the remaining 18(65%) are said that citizens of the country gets more benefit from VAT. The researchers conclude that citizens of the countries are more beneficiaries from VAT.

## Data analysis of the finding of Large Tax Payers

In this section data collected from 55 large tax payers in Arada sub-city are analyzed and interrelated. The questionnaires are compiled by finance managers because they are mostly responsible for financial matters including VAT issues.

### 3.2.13 Business Types Of Respondents

The selected sample large tax payers in Arada sub-city are engaged in different types of business.

The respondents were asked about their business type. The respondents' responses are as follows

**Table 3.13** Business Types Of Respondents

No	Description	No of respondents	Percentage
1	Business type		
	A. Manufacturer	18	33
	B. Wholesaler and Retailer	25	45
	C. Service	12	22
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.13 indicates the business types of the respondents. Out of the total sample respondents 18(33%) are manufacture, 25(45%) are whole sealers and

retailers and 12(22%) are service provider. This indicates the majority of large tax payers businesses are whole sellers and retailers.

### 3.2.14 Year Of Services In The Business

The respondents were asked how long have they experience in the business. Their response is shows as follows.

**Table 3.14** Year Of Services In The Business

No	Description	No of respondents	Percentage
1.	How long have you been in this Business?		
	A. Less than a year	0	0
	B. 2 – 5 years	19	35
	C. More than 5 years	36	65
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.14 indicate that the respondents in the business out of the total 19(35%) of them have 2 to 5 years working Experience and the rest of them 36(65%) have more than 5 years working experience in the business. This shows the greater number of business have more than 5 years of working experience in the business.

### 3.2.15 VAT Payment Situation

They were asked whether they pay their tax liabilities within the period or not. The respondents' responses are shown below.



**Table 3.15** VAT Payment Situation

<b>No</b>	<b>Description</b>	<b>No of respondents</b>	<b>Percentage</b>
1	Do you Pay Tax for every Accounting period by respecting the deadline for VAT?		
	Yes	44	80
	No	11	20
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

As indicated in the above table 3.15 the VAT payment situation of the respondent are shows that 44(80%) of them are paying their tax liabilities within the deadline and 11(20%) of them are not pay within the dead line. Therefore, the research concludes that most of the tax payers pay their tax liabilities before the deadline.

### **3.2.16 Respondents Registration Situation**

The respondents were asked they registered for VAT whether voluntary or obligators. Their responses are shown as follows:

**Table 3.16** Respondents Registration Situation

No	Description	No of respondents	Percentage
1	Are you voluntary of obligatory registered for VAT?		
	Voluntary	39	71
	Obligatory	16	29
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.16 shows that the business registration for VAT whether voluntary or obligatory. The response shows 39(71%) of the businesses are registered for VAT voluntary and 16(29%) are registered for VAT by obligation. This indicates most of business registered for VAT without force, voluntary.

### **3.2.17 Attending Awareness Creation Training**

The respondents were asked about the training which creates awareness about VAT. Their response shown as follows

**Table 3.17** Attending Awareness Creation Training

<b>No</b>	<b>Description</b>	<b>No of respondents</b>	<b>Percentage</b>
1	Did you attend any awareness creation training from the government or any other body?		
	Yes	20	36
	No	35	64
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

As indicated in the above Table 3.17 the respondents which attend the awareness creation training. From the total respondents 20(36%) of them are training which create awareness about VAT and 35(64%) of them never attend any training which create awareness about VAT. This indicates large number of business was not attending training which create awareness about VAT.

### **3.2.18 Major Problems On The Application And Collection Of VAT**

The respondent's major problems on the application and collection of VAT are shown as follows.

**Table 3.18** Major Problems On The Application On And Collection Of VAT

No	Description	No of respondents	Percentage
1	What are the major problems you have experience related to VAT application and collection?		
	A. Lack of simple and fast service	18	33
	B. Lack of awareness about VAT	37	67
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

As shown in the above Table 3.18 the major problems on the application and collection of VAT, 18(33%) of the respondents faced problems in lack of simple and fast services and 37(67%) of them said that the lack of awareness about VAT. The researchers conclude that the major problem faces the tax payers are lack of awareness about VAT.

### **3.2.19 Respondents Penalty Payment Experience**

Their responses about penalty payment experience are shown as follows

**Table 3.19** Respondents Penalty Payment Experience

No	Description	No of respondents	Percentage
1	Did you pay VAT penalty for the past periods		
	Yes	15	27
	No	40	73
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.19 indicates the respondents' penalty payment experience. Among the total respondents 15(27%) of them are pay penalty two times and 40(73%) of them were not pay any penalty. There for, the researchers conclude that the large number of business was not pay penalty.

### 3.2.20 Respondents Late Payment Experience

The respondent's late payment experience was shown as follows.

**Table 3.20** Respondents Late Payment Experience

No	Description	No of respondents	Percentage
1	Did you pay late payment VAT for the past periods life history?		
	Yes	19	35
	No	36	65
	<b>Total</b>	<b>55</b>	<b>100</b>

Source: Compiled from questionnaire

As indicate in the above Table 3.20 the respondents late payment experience, out of the total respondents 19(35%) are said paid late and 36(65%) are not late payers. This indicate most business does not late to pay their tax liabilities.

### 3.2.21 Respondents Preferred Date to Declare VAT

The respondents preferred date to declare VAT is shown as follow

**TABLE 3.21** Respondents Preferred Date to Declare VAT

No	Description	No of respondents	Percentage
1	Which date do you prefer to pay or declare the VAT monthly?		
	A. First week of the month	9	16
	B. Middle of the month	13	24
	C. Last week of the month	33	60
	<b>Total</b>	<b>10</b>	<b>100</b>

Source: Compiled from questionnaire

Table 3.21 indicates the respondent preferred date to declare VAT. Among the total respondents 9(16%) are preferred the first week of the month, 13(24%) are preferred the middle of the month and the remaining 33(60%) are preferred the last week of the month. Therefore, the researchers conclude that most business preferred the last week of the month to declare the VAT.

## CHAPTER FOUR

### SUMMARY, CONCLUSION AND RECOMMENDATION

The objective of the study is to see and assess the practice and compliance with the existing VAT law on selected large tax payers.

In order to attain this goal, related literature review and questioner were distributed for the staffs and selected large tax payers. The data obtained and analyzed using percentage. Based on the findings, the following summary, conclusion and recommendation are forwarded.

#### 4.1 Summary

To summarize the findings of the study which is the data gathered and analyzed from the LTO Staffs, 15 respondents which are equivalent to 54% of the respondents' responded that the implementation of VAT in the administration is good. Among those sample respondents, 12(43%) of them said that the main problem of VAT application is tax payers lack of awareness about VAT also 12(43%) of those respondents evaluation indicate that the fillings of VAT Registered parties are positive or fair.

As 17 respondent's response, which is equivalent to 60% of the respondents, indicate tax offices are more responsible for VAT collection. Almost half of the respondents, which means 14(50%), agreed that the problem while existing VAT is some tax payers does not pay their tax liabilities within the time.

The majority, 12(43%) and 11(40%) respondents respectively said that the awareness and the level of attitudes of VAT in Areeda sub-city is less.

The most, 18(65%) of the sample respondents agreed that the citizens of the countries are more beneficiaries from the VAT.

On the other hand the finding which is from the selected larger tax payers data shows that, most of the respondents, 39(71%) mentioned that as they registered for VAT without any force and the majority, 44(80%) of the sample respondents said that most of them pay their tax liabilities before the deadline.

Among the sample respondents, 35(64%) of them were not attend any training which create awareness about VAT and the majority, 33(67%) of the sample respondents shows that the main problem face the tax payers are lack of awareness.

Among the respondents, 40(73%) response shows that most business were not pay penalty and as 33(60%) of them preferred the last week of the month to declare the VAT.

## **4.2 Conclusion**

Depending on the findings the researchers conclude the following points

- ❖ The implementations of VAT in the administration are good.
- ❖ The major problem faced the administration and the tax payers is lack of awareness about VAT.
- ❖ The feelings of VAT Registered parties are affair.
- ❖ The tax offices are more responsible for VAT collection.



- ❖ Some tax payers do not pay their tax liabilities within the time.
- ❖ The levels of attitude of tax payers to VAT are low.
- ❖ The citizens of the countries more beneficiaries from VAT.
- ❖ Most of businesses are registered for VAT voluntarily.
- ❖ Most of the business workers not attend the training which creates awareness about VAT.
- ❖ Most of the businesses were not penalized.
- ❖ Most business prefer the last week of the month to declare the VAT.

### **4.3. Recommendation**

As to the study conducted there are certain problems to VAT Practices and compliance with the law. Based on the research findings the following points can be forwarded as recommendation.

- ❖ As shown in the above findings the major problems with VAT collection have been emanated from lack of awareness that means no awareness creation was made so far. Likewise, the problem goes with the authorities and the concerned bodies for the poor awareness creation to the tax payers. What the researchers have understood from the respondents' responses is that they don't take training on the issue.

Therefore, to develop the awareness of tax payers against VAT the authority has to use various mechanisms, such as: providing workshops, short terms training as well as using mini and mass Medias like TV, Radio and newspaper etc.

- ❖ As shown in the finding the other problems of vat collection is that some tax payers don't pay their tax liabilities with the time set by the tax authority, so in one hand, the authority's tax revenue will decrease

by the same amount; on the other hand, the uncollected amount will need additional time and effort which in turn have negative impact of the tax collection process.

Therefore, in addition to creation of awareness the authority should properly exercise the existing vat laws to enforce the tax payers and to decrease the uncollectable tax revenue.

## BIBLIOGRAPHY

1. Bhatia, H.L. (1998).**Public Finance**. 19th edition,New Delhi: VikasPublishing House Private Limited.
2. Bhatia, H. L. (2003).**Public Finance**.New Delhi: VikasPublishing House Private Limited,
- 3.Ethiopian revenue and custom Authority. (2012 E.C)."Revenue Sector Public Relations".**GebiLelimatMagazine**.
- 4 Ethiopian revenue and custom Authority. (2002 E.C)."Education and public relations".**Hand Book**.
5. Ethiopian revenue and custom Authority. (2002 E.C)."Education and public relations".**Brochures**.
6. Eyasu,Zemedu.(2006, August).**VAT Practice AndCompliance With The Law**.
7. FDRE. (2002, July)"Value Added Tax Proclamation". **Federal NegaritGazeta**. No.285/2002, 8th year No. 32 and 4th
8. FDRE. Council of Ministers. (2002, December) "Value Added Tax Regulation". **Federal NegaritGazeta**, No.79/2002, 9th year No.19
9. Gillis,MalcelmEtal. (1998, June). "VAT In Developing Countries".**A World Bank Symposium**
10. Hancock, Dora, (1995).**Taxation Polices and Practice**. 3rd edition.
11. Misrake, Tesfaye (2011) Ethiopian Tax Accounting Principles and Practice. New Revised Edition, Addis Ababa.
12. Richard A. Musgrave and Peggy B. Musgrave. (1989). **Public Finance In Theory And Practice**.5th edition, Hill Book Company.
13. www.erca.gov.et
14. www.imf.org: Tanzi, vito. and Howell, Zee. IMF.**Tax Policy For Developing Countries**.

**ST' MARRY UNIVERSITY**  
**BUSINESS FACULTY**  
**DEPARTMENT OF ACCOUNTING**

Survey questionnaires for VAT practice and compliance:

This research questionnaire is designed to collect primary data about the VAT practice and compliance with the law on selected large tax- payer organizations. The result of this study is intended to serve for academic purpose. Reminding you of the fact that your genuine response is highly valuable and have great contribution for the quality of the research. Confidentiality of your information is kept in that results were to be aggregated and presented only in summary form.

Finally, we would like to say thanks in advance for your participation.

1. Job specification and description of the respondents

A. Level of responsibility.....

B. Responsibility .....

2. Type of your business

A. Manufacturer  B. Retailer

C. Service  D. Others specify.....

3. Do you pay tax for every accounting period by respecting the deadline for VAT?

A. Yes  B. No  C. Comment.....

4. Are you voluntary or obligatory registered for VAT?

A. Voluntary  B. Obligatory  C. Comment.....

5. Did you attend any awareness creation training from the government or any other body?

A. Yes  B. No  C. Comment .....

If your answer is "yes" for question 5, how many times?

---

6. How long have you been in this Business?

- A. Less than 1 year       B. 2-5 year       C. More than 5 year

7. What are the major problems you have experienced related to VAT application and Collection?

- A. Lack of simple and fast service       B. lack of awareness about VAT

C. if others, specify \_\_\_\_\_

---

8. Do you use your tax- payer identification number on all VAT invoices and official communications with the authority?

---

9. Do you give VAT invoices to the person who receives the goods and services, when you carry out a taxable transaction?

- A. Yes       B. No       C. Comment -----

10. Did you pay VAT penalty for past periods?

- A. Yes       B. No       C. Comment .....

11. If your answer is "yes" for question 9, how many times?

---

12. Did you pay a late payment VAT tax in the period of your business life history?

- A. Yes       B. No       C. Comment .....

13. If your answer is "yes" for question 11, how many times?

---

14. Which date do you prefer to pay or declare the VAT?

- A. First week of the month       B. Middle of the month

C. Last week of the month       Comment.....

**Thank You**

**ST' MARRY UNIVERSITY**

**BUSINESS FACULTY**

**DEPARTMENT OF ACCOUNTING**

Dear respondents this is a questionnaires intended to obtain relevant information onVat practice and compliance with the low a case study in selected large tax payers in Arada sub-city which is use for academic purpose . the finding of study greatly depend on your cooperation for which are grateful in advance to achieve this you are kindly requested to corporate giving response for following question , please tick () on the box your choice and fill the blank space.

1. Sex: - male  female

2. Age 18-24  25-30  30-35  >35

3. Education status:-

Elementary and junior complete  high school complete

Certificate  Bachelor Degree Diploma  above degree

4. Work experience: - less than a year  1 – 2 year

2- 4 year above 4 years

5. How long have you been working in LTO Taxing Unit?

Ayear  2-4 year  4 year  and above

6 How do you evaluate implementation of VAT in your administration?

Very good  good  fair

Bad  worst  others, please specify \_\_\_\_\_

7. What are the major problems you have experienced related to VAT applicationand Collection?

Unwillingness of VAT payers  late payment of VAT  lack of awareness about VAT  if others, specify \_\_\_\_\_

8. How do you evaluate VAT registered parties feeling while they registered for VAT?

Feel Very good  feel good  feel fair  feel bad

Other, please specify \_\_\_\_\_

9. Who is more responsible for VAT collection and assessment?

Tax payer's  customer  any government body  tax office

Other, specify - \_\_\_\_\_

10. What are problem you have faced while collecting VAT?

Most of VAT payers not pay a required amount on time

All of VAT payers not pay a required amount on time

Less of VAT payers not pay a required amount on time

Least of VAT payers not pay a required amount on time

Others, specify \_\_\_\_\_

11. How do you evaluate the awareness of VAT payers about VAT?

Very high  high  low  very low

If your answer low specify \_\_\_\_\_

12 How do you judge the awareness of tax payers about Vat in AradaSub-city?

They have good awareness

They have very good awareness

They have less awareness

they have poor awareness

If out these, specify \_\_\_\_\_

13. If your answer is poor, specify

---

---

14. If your answer is very high, specify

---

---

15 what are the attitude of VATpayers?

Very good  fair  satisfactory  bad  worst

Other, specify \_\_\_\_\_

16. Who benefited from VAT more?

VAT payer's  government  citizens of the country

If say VAT payers, specify \_\_\_\_\_

17. In your opinion what are the major VAT assessment and Practice problem?

Please specify

---

***Thank You***