

**ST. MARY'S UNIVERSTY
BUSINESS FACULTY
DEPARTMENT OF ACCOUNTING**

**AN ASSESMENT VALUE ADDED TAX ON
THE SIDE OF TAXPAYERS
IN THE CASE OF LEDETA SUB CITY**

BY

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**A SENIOR ESSAY SUBMITTED TO THE
DEPARTMENT OF
ACCOUNTING IN PARTIAL FULLFILMENT OF THE
REQUIRMENTS FOR THE DEGREE OF BACHELOR OF ART
IN ACCOUNTING**

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ACKNOWLEDGMENTS

First and for most, our thanks goes to almightily GOD and saint virgin merry without whom we could never have been way we are today. Next, the generous cooperation of many people has contributed for the success and completion of this paper, our special gratitude goes to our advisor Ato Habtamu Eshetu for his commitment on the paper at each stage.

Thanks to all respondents of the questioner. Finally we would like to thanks all contributes that provided their support on one or the other way to accomplish this research paper.

TABLE OF CONTENTS

	PAGE
Acknowledgment.....	5
Table of content.....	5
List of tables.....	5
Acronyms.....	5
Abstract.....	5

CHAPTER

5. Introduction

1.1 Background of the study.....	1
1.2 Statement of the problem.....	3
1.3 Basic study question.....	4
1.4 Objective of the study.....	4
1.4.1 General Objective.....	5
1.4.2 Specific Objective.....	5
1.5 Significant of the study.....	6
1.6 Scope of the study.....	6
1.7 Definition of Terms.....	6
1.8 Research Design and Methodology.....	7
1.8.1 Research Design.....	7
1.8.2 Population and Sampling Technique.....	7
1.8.3 Method of Data Collection.....	7
1.8.4 Method of Data Analysis.....	8
1.9 Limitation of the study.....	8
1.10 Organization of the study.....	8

5. REVIEW OF LITRATURE

2.1 Definition of terms	9
2.1.1 Classification of Tax	10
2.2 History of VAT	11
2.3 VAT in Ethiopia	11
2.4 Types of VAT	12
2.5 Definition of VAT.....	12
2.6 VAT Terminology.....	15
2.7 Nature of VAT	16
2.8 VAT Administration in Ethiopia.....	18
2.9 VAT Registration	21
2.10 Registration Procedure.....	22
2.11 Time to Application	22
2.12 Time of Registration	23
2.13 Advantage and Disadvantage of VAT	24
2.13.1 Advantage.....	24
2.13.2 Disadvantage	24
6. Data Presentation, analysis and interpretation	
3.1 Analysis Technique	26
3.2 Analysis of data through questionnaires	27
6. Summary, Conclusion and recommendation	
4.1 Summary of finding	39

4.2 Conclusions.....	40
4.3 Recommendations	41
References.....	
Questionnaire.....	

LIST OF TABLES

	PAGE
Table 1 Profile of the respondent	26
Table 2 Age of the respondent	27
Table 3 Education status of the respondent	27
Table 4 Type of business	28
Table 5 Type of registration	29
Table 6 Years of tax paying	30
Table 7 Attitude of the respondent toward VAT system.....	31
Table 8 A responses toward VAT demand complete accounting system.	32
Table 9 A responses toward getting registered for VAT affect revenue...33	
Table 10 Attitude of the respondent toward the impact of VAT on customer.....	34
Table 11 Attitude of the respondent toward the market completion.....	35
Table 12 Attitude of the respondent against awareness created by tax administration	36
Table 13 Attitude of the respondent toward the implementation of VAT system seems complex.....	37

Acronyms

VAT – Value Added Tax

ERCA – Ethiopia Revenue Custom Authority

ABSTRACT

This study assessed value added tax on the side of taxpayers in ledeta sub city. The main objective of the research is to assess and identify the main problem and solution related to VAT in ledeta sub city taxpayers.

To fulfill this objective primary data were used. A primary data were collected through questionnaires. The major problem related to VAT payers found is the implementation of VAT seems complex and market competition. To overcome problem identified a constrictive recommendation would be made in order to improve those problems.

CHAPTER ONE

1. INTRODUCTION

1.1. Background of the Study

Like any other economic entity requires capital, governments also need funds to finance different public activities. Governments undertake a number of public projects, such as social security protection, provide other services and public utilities like electricity, water supply telecommunication services etc, provide basic social amenities in the form of education, health and sanitation facilities. In order to accomplish these services and works a government raises revenue from internal as well as external sources, such as collection of taxes, foreign and domestic borrowing, sale of public tender, gifts and donations, fees and fines etc. Among those revenue sources, tax plays the pivotal role. `` (Gabreworku, 2008) ``.

Tax is a compulsory contribution that the government collects from individuals and firms so as to enable finance government activities. The tax system of any government is generally the product of its own environment. The government has the right to impose tax on the operating businesses and collects the tax return from them. The government uses the tax revenue for maintaining law and rules, keeping natural development, establishing security system and improving social well being. "(GebrieWorku, 2008)".

VAT is a tax not on the total value of goods sold or services rendered but only on the incremental value or newly created value by the last seller. The incremental value is the difference between sales proceeds and purchased of intermediate goods or services. Is the base for VAT computation.(Encyclopedia).

The newly implemented overall tax reform program of Ethiopia consists of two main types of taxes, namely direct taxes and indirect taxes. Direct

tax is a tax where the effect (burden) is borne by the person that pays the tax. Employment income tax and other income tax, rental income tax, are the types of direct tax. Indirect tax in Ethiopia, on the other hand, is a tax intended to be borne by persons other than those who pay the tax. It is a tax paid by tax payers on goods or services entered into the chain of production but ultimately borne by consumers of goods and services. Value added tax (VAT), Excise tax, customs duty and sure tax are the kinds of indirect tax in Ethiopia (MisrakeTsfaye, 2008).

VAT is a tax charged on the newly create value of a call stage production with a means of enabling the business to offset the tax paid on purchase of goods and services against the collected by the government from someone other than the person who actually bears the cost of the tax consumer. VAT is a tax on value that business firm add to the things it buys from other firms in the producing or distributing its products or services.(MisrakeTsfaye, 2008).

Ethiopia's tax reform program has introduced VAT in 2003, to modernize the tax system and to solve problems related to tax payers and also problems with the tax authority (<http://www.erca.gov.et>). Since the system of VAT is at its early stage of development, it creates some problems both at the side of tax authority and tax payers. This study was focus on Lideta Sub-city of the Addis Ababa City as a case study. The objectives was assess value added tax at the side tax payers. The researchers also expect to suggest possible solutions to the problems.

1.2. Statement of the Problem

All Government requires funds to finance their activities such as defense and social security's, construction of infrastructure facilities, provision of foods, shelter and medical care for the poor, operating schools and hospitals and others. VAT is most remunerative tax and it plays a major role in the tax system.

However, some tax payers complain that the system is implemented inefficiently so that it does not include all the taxable persons and taxable business activities. On the other hand, the business community is blamed for not being consistent with the tax regulations and laws drawn by the government. The reason given in this matter was that the business community has not become capable to maintain appropriate book of accounts and records, which is one of the basic requirements for VAT. Due to this and other related issues, the implementation of VAT in Ethiopia faced different challenges.

Generally in Ethiopia there are some problems at the side of tax payers especially in the area of VAT among these the first one is a large number of those eligible for VAT registration are do not register for VAT because of market competition and afraid of losing their customer. The second one is lack of awareness by the business enterprise about VAT system and VAT advantages(lack of awareness the use and why they collect and pay VAT).This study was about tax payers to assess value added tax on the side of tax payers.

1.3. Basic Study Questions

In this study, the researchers address the following research questions.

- What are the main reasons for failure of the business community to implement VAT regulations?
- Why do eligible businesses try to avoid being VAT registered?
- Are all tax payers aware about VAT system?
- What is the level of understanding about rules and regulations of VAT by payers?

1.4. Objectives of the Study

The concern of this study was to assess VAT at the side of tax payers in Ledeta sub city tax payers. This study has both general and specific objectives

1.4.1. General Objective

The general objective of this study was to identify major problems and solution associated with VAT. Identification of these problems and solution was targeting on the tax payers.

1.4.2. Specific Objectives

The specific objectives of the study are:-

1. Identify the main reasons for failure of business community to implement the VAT.
2. To assess reasons why eligible businesses try to avoid being VAT registered.
3. To assess the awareness of tax payers about VAT system.
4. To assess the level of understanding about rules and regulation of VAT by payers.

1.5. Significance of the Study

This research could help to assess awareness of the tax payer towards the tax system; it helps to assess the reason why business declined to register VAT and may serve as the base for other who wants to pursue further study on similar or the same topic in the area.

The research may also help to forward some specific and practical recommendations to future actions concerning assessment related problems of VAT on the side of taxpayers. In addition, it could create

awareness and help in developing positive attitude among tax payers and tax administration about VAT.

1.6. Scope/ Delimitation of the Study

This study was limited to and concerned on VAT registered businesses in Ledeta sub-city and those which have annual sales turnover of Birr 500,000 and above. Due to valuable for the study and nearness we select Woreda 1, 3, and 4 and because of shortage of finance we concerned only on merchandise, manufacturing and service given business. The aim of the study will generally be to assess value added tax at the side of tax payers in Ledeta sub-city.

1.7. Definition of Terms

VAT- Value added tax 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 fiducially borne by the consumer .

VAT input- the VAT that your business pays over on taxable supplies made (VAT paid on purchase and can be recovered only insofar as your business is VAT – registered and makes taxable out puts.

1.8. Research Design and Methodology

1.8.1. Research Design

A descriptive study was conducted to examine the assessment of value added tax at the side of tax payers. The Research was designed in such a way that sample from a population were taken to make a quantitative analysis of the research questions.

1.8.2. Population and Sampling Technique

1.8.3. Method of Data Collection

The research considers the taxpayers who are engaged in various activities in ledeta sub-city. There are 10 werdas in ledeta sub city the researchers' select 3 werdas .The sample frame of the study considers 300 taxpayers. For the purpose of the research the researchers take 30 tax payers, because of market location and work experience. To distribute the questionnaires was take 30 of the population, VAT payers who are engaged in various businesses (15 from merchandise, 11 from service given and 4 from manufacturing business).To achieve the objective of the research the researchers were use non probability sampling technique (personal judgment) because it is more reliable and valid.

1.8.3 Method of Data Collection

Due to the nature of the data the researchers mainly used the primary data collection method. Primary data was collected from tax payers, because of its suitability and easy to get information the researcher was used questionnaires to collect primary data. In the questionnaire method of data collection, questions are prepared and ask the respondents which were taken as a sample from the total population under the study. Distribution to taxpayers by using non probability sampling technique, through judgmental sampling technique to the taxpayers.

1.8.4. Method of Data Analysis

After collecting the information by using primary and secondary data along with objectives of the study was analyzed in descriptive analysis methods with table and percentage.

1.9. Limitation of the Study

In order to study about the problem of VAT on tax payers in Ledeta sub city the researchers face some limitation such as; the sample size is not sufficient to deduce content conclusion, the researchers faces problem in collecting primary data the respondents show unwillingness to fill the questioner, and shortage of finance.

1.10. Organization of the Paper

This study was organized into four chapters. The first chapter was an introduction part which includes Background of the Study, Statement of the Problems, Objectives of the Study, Significance of the Study, Research Methodology, and Scope of the Study, Limitation of the Study and Organization of the Paper. The second chapter presents important related literature review, while chapter three discusses about data presentation, analysis and interpretation. The fourth chapter brings summary, conclusion and recommendation.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2. Introduction

Tax is one of the most important sources of revenue to every Government. In the earlier days, payment of taxes was optional. People pay taxes to avail the benefit of social amenities such as education, health and sanitation, recreation facilities etc. This type of tax collection system result tin inefficient of Government in fulfilling its obligations to the security. As a result, tax becomes compulsory contribution by every citizen to the Government. A tax, in the modern times, is a compulsory levy and those who are taxed have to pay the sum irrespective of corresponding return of service or goods by the Government. The tax payers do get many benefits from the Government but no tax payer has a right to any benefit from the public expenditure on the ground of paying tax. The benefits of public expenditure may go to any one irrespective of the taxes paid.(Gabre worku, 2008).

2.1 Definition of tax

Tax is compulsory levy irrespective of any corresponding service or good by the government. Taxes and taxation are generally regarded as unpleasant subjects. Tax may also be defined as pecuniary (financial) burden imposed on assessed by government. Tax is a liability to an assess but a major source of revenue to a government. The revenue collected through taxation is used to purchase the input necessary to produce government supplied good and services (collective goods) to redistribute purchasing power among citizens and too many other operations. (MisrakTesfaye, 2008)

Tax is a fee charged by a government on a product, income, or activity. If a tax is levied directly on personal or corporate income, then it is a direct tax. If a tax is levied on the price of a good or service, then it is called indirect tax. The purpose of taxation is to finance government expenditure. One of the most important uses of taxes is to finance public goods and services, such as street lighting and street cleaning. (HI Bhatia,2003)

2.1.1 Classification of tax

I. Direct taxes

According to Dalton, Direct taxes are those taxes, which are paid entirely by those persons on whom they are imposed. The burden of this tax is upon the who pays the tax to the authority. Direct taxes are taxes which cannot be shifted to others.

A.R Prest defines "Direct taxes as those taxes which are based on receipts of income" such as income tax, corporate tax, capital gain tax, property tax, wealth tax. These taxes should be paid according to the rate specified by tax authority.

II. Indirect tax

Indirect taxes are those the burden of which may not necessarily be borne by the assessed. Indirect taxes can be shifted to other persons. Indirect taxes are taxes on commodities like custom duties, sales taxes, excise taxes etc.

According to J.S Mill "Indirect taxes are those which are demanded from one person in the expectation and intention that a person shall indemnify himself at the expense of another". Thus, it is intended that the amount of tax should be collected from other persons by those on whom it is imposed.

2.2 HISTORY OF VAT

Emergence and rapid spread of VAT is among the most important tax development of the later 20th c VAT invented 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 Worku, 2008).

2.3 VAT IN ETHIOPIA

The federal democratic republic of Ethiopia (FDRE) has adopted VAT in to its tax system in 2003. It has been introduced on January 1, 2003. Replacing the former sales tax system The VAT proclamation No.285/2002 (VAT law) has been ratified by the house of people representatives six month before VAT implementation (July, 2002). This VAT proclamation has thirteen sections (13) and six (66) articles. In December, 2002, the VAT regulation No.79/2002 has also been issued by council of ministers pursuant to the value added tax proclamation for the implementation and regulation of VAT. The VAT regulation has three chapter (3) and forty (40) articles.). (Misrak.Tesfaye, 2008).

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.

VAT is a system whose base is sales. Any item originating from the procedure and transferred to the wholesaler, to the retailer and finally to the customer picks additional value at each step which would be taxed whenever transaction takes place. (Ethiopia Economic Association, May 2005)

2.4 TYPES OR KINDS OF VAT

In modern taxation there are four types of value added taxation system. These are:-

A. Gross product value added tax

B. Income type value added tax: according to this form the firm is allowed to deduct the depreciation the capital goods (during the years) a part of the full value of its non capita 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

C. Capital exemption type value added tax

D. Consumption type value added tax: 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.(Dr.R.Parameswaran,2005 p,106).

2.5 DEFINITION OF VALUE ADDED TAX

Value added tax (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 fiducially borne by the consumer . VAT is an indirect tax because VAT is paid to tax authority by the seller of the goods, who is the taxable person, but it is actually paid by the seller as part of the price. (Meisrak Tesfay, 2008).

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 value minus the value of inputs. VAT is a system whose base is sales. Any item originating from the procedure and transferred to the wholesaler, to the retailer and finally to the customer picks additional value at each step which would be taxed whenever transaction takes place. Value added tax (VAT) is a tax imposed by a government at each stage in the production of a good or service. The tax is paid by every company that handles a product during its transformation from raw materials to finished goods. The amount of tax is determined by the amount of the value that a company adds to the materials and services it buys from other firms. (Encyclopedia)

Value added Tax (VAT) is a tax on the value added to goods and services by enterprises at each stage of the production and distribution processes. It arises whenever a "taxable person" makes a "supply of goods or services" in the course of his business. These in some countries It arises whenever a "goods and services Tax" or GST. VAT was invented by a France economist in 1954 by Maurice Loure director of the France tax authority. VAT was invented because very high sales taxes and tariffs encourage cheating and smuggling. (Gabre worku, 2008).

A value added tax (VAT) is a form of consumption tax. From the perspective of the buyer, it is a tax on the purchase price. From the

seller, it is a tax only on the value added to a product, material, or service. From an accounting point of view by this stage of its manufacture or distribution. The manufacturer remits to the government the difference between these two amounts and retains the rest for themselves to offset the taxes they had previously paid on the input. (Encyclopedia)

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. (Yohanes and Sisay, 2009).

Unlike the turnover tax, which is applied to the full value of a product, every time the item changes hands in the process of production and distribution, the VAT is assessed, at each stage, on only the increment in value achieved by the product since the last taxable transaction. At the end of chain, the total amount of tax paid on a given commodity is determined only by the tax rate and the final price of the commodity regardless of the number of stages through which it has passed. What has been collected in fractional payments is equivalent to a single stage tax on the value of the final product. 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. But the reality is not quite so simple. (Gabrie Worku, 2008)

A type of consumption tax that is placed on a product whenever value is added at a stage of production and at final sale. Value-added tax (VAT) is most often used in the European Union. The amount of value-added tax that the user pays is the cost of the product, less any of the costs of

materials used in the product that have already been taxed. (Gebrie Worku, 2008).

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).

Comparison with sales tax

Value added tax avoids the cascade effect of sales tax by taxing only the value added at each stage of production. For this reason, throughout the world, VAT has been gaining favor over traditional sales taxes. In principle, VAT applies to all provisions of goods and services. VAT is assessed and collected on the value of goods or services that have been provided every time there is a transaction (sale/purchase). The seller charges VAT to the buyer, and the seller pays this VAT to the, it is paid tax on the gross margin of each transaction, by each participant in the Sal government. If, however, the purchaser is not an end user, but the goods or services purchased are costs to its business, the tax it has paid for such purchases can be deducted from the tax it charges to its customers. The government only receives the difference. (<http://Wikipedia.org/wiki/VAT>).

2.6 VAT TERMINOLOGIES

The following are some of the terms that are common in VAT literature.

A. Input VAT :- the VAT that your business pays over on taxable supplies made (VAT paid on purchase and can be recovered only insofar as your business is VAT – registered and makes taxable out puts.

B. Output VAT: - the VAT that your business collects over on taxable supplies (VAT paid on sales)

C. VAT payable: - this is the net VAT to be paid to federal Inland revenue authority by a taxable person. It is arrived at by the formula;

VAT payable = output tax – Input Tax

D. VAT refundable: - the net VAT that a taxable person expected from federal in land revenue authority when input VAT exceeds output. In Ethiopian case FIRA do not refund up on declaration rather taxable person shall carry forward the balance 5 months until it offset by output VAT. If taxable person doesn't sell taxable supplies within these 5 months, hence is entitled for refund.

E. Zero- rating: the supply is charged with VAT at 0% but credit can be taken for VAT paid on purchases used to make the supply.

F. Positive rate (standard rate): the supply is charged with at the rate of 15%.

G. Exemption: the supply is exempted from VAT. No VAT is charged on the supply and no credit can be taken from VAT paid on purchases used to make the supply.

H. Exempt supplies: which are not liable to VAT exempt supplies are not taxable supplies and does not form part of the taxable turn over the VAT purpose. A person making only exempt supplies cannot be registered for VAT.

I. Threshold: - this is the level of turnover of taxable supplies prescribed by the law at or above which a person must register for VAT.

J. Taxable person: is legal entity such as company, Partnership, Sole proprietor, who is liable to be registered for VAT. It is the person not the business that is registered for VAT.

K. Taxable supplies: these are business transactions which are liable to VAT at the standard rate. (Misrak Tesfaye, 2008)

2.7 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.(Misrak Tesfaye, 2008).

Exempted output Vs. Zero rate

The difference between an exempt output and a zero rated output is on input VAT. The VAT that your business pays over on supplies made to it can be recovered only insofar as your business is VAT – registered and makes taxable outputs. It does not matter whether the taxable outputs are positive rated or zero rated- so long as our business is VAT registered

and makes taxable output it can recover its input VAT in full. (Gabrie Worku, 2008).

2.8 VAT Administration in Ethiopia

The VAT replaced the current sales tax on manufactured and imported goods and services on January 1, 2003. . The VAT is a broad based tax on the consumption of goods and services. It is collected at all stages in the production and distribution process beginning with the importer and producers of raw material and ending with the retailer. Unlike the sales tax system, where by 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 in puts, sales of exported goods are not subject to the VAT. Removing the tax content form exported goods makes the goods more competitive in international markets. (Misrake Tesfaye 2008).

VAT is a tax on consumer expenditure. It is collected on business transactions and imports. Most business transactions involves supplies of goods or services and VAT is payable if they are;

- Supplies made in Ethiopia
- Made by a taxable person
- Made in the course or furtherance of a business
- Are not specifically exempted or zero rated

Supplies are outside the scope of the tax if they are ; made by someone who is not a taxable person or not made in the course or furtherance of business course or furtherance the way a taxable person to carry out its activity to develop, advance and progress the taxable activity. It refers to the normal and expected events or processes to develop the taxable activity. Anything done in connection with the commencement or termination of a taxable activity is treated as carried out in the course or

termination of a taxable activity is treated as carried Due in the course or furtherance of that taxable activity .(Gabire Worku, 2008).

For VAT purpose supplies can be classified as exempt supplies and taxable supplies. Supplies of exempt goods and services are business transactions on which VAT is not chargeable at either the standard or zero rates. Exempt supplies are not taxable supplies and does not form part of the taxable turn over for VAT registration purposes. If one makes only exempt supplies it cannot be registered for VAT. If you make taxable and exempt supplies you cannot reclaim the input tax (tax paid on purchases) related to the exempt supplies. (Gabire Worku, 2008).

According to proclamation 285/2002, the following types of supplies of goods (other than by way of export) or rendering or services as well as the following types of imports of goods are exempt from payment of VAT to the extent provided by regulation.

a. The sale transfer or lease of a used dwelling except for the following.

The sale or transfer of hotel or hostel accommodation

The sale or transfer of newly constructed residential property, unless the property has been occupied as are silence for at least two years.

b. The render of financial services; except the following

- Granting, negotiating and dealing with loans, credit, guarantees, and security for money, including management of loans, credit or credit guarantees by the grantor.
- Transaction concerning deposit and current account, payments, transfers, debts, cheques and negotiable installment other than debt collection and factoring.
- Transaction relating to share, stocks, bonds, and other securities other than custody services.

c. The supply or import of national or foreign currency, and of securities;

- d. The import of good to be transferred to the National Bank of Ethiopia;
- e. The rendering by religious organizations of religious or church related services;
- f. The import or supply of prescription drugs and the rendering of medical services;
- g. The rendering of educational services provided by educational institutions, as well as child care service for children at pre – school institutions;
- h. The supply of goods and rendering of services in the form of humanitarian aid, as well as import of goods transferred to state agencies of Ethiopia and public organizations for the purpose of rehabilitation after natural disasters, industrial accidents and catastrophes;
- i. The supply of electricity, kerosene, and water;
- j. Goods imported by the government, organizations, institutions or projects exempts from duties and other import taxes to the extent provided by law or by agreement;
- k. Supplies by the post office;
- l. The provision of transport;
- m. Permits and license fees;
- n. The import of goods to the extent provided under schedule two of the customs tariffs regulations;
- o. The supply of goods or services by a workshop employing disabled individuals if more than 60 percent of the employees are disabled; and
- p. The import or supply of books and other printed materials. (FDRE, Negarit Gazeta, 2002).

A commercial rental establishment means accommodation in any hotel, motel, boarding house, hostel, or similar establishment in which lodging is regularly or normally provided to five or more persons at a daily, or weekly, monthly or other periodic charges. Accommodation in any house,

flat, apartment or room other accommodation, which is regularly or systematically leased or held for lease as residential accommodation for continuous periods not exceeding 45 days in the case of each occupants of such house, flat, apartment, or room, if the total annual receipts and accruals from lease there of exceeded 24,000 birr or there are reasonable grounds for believing that such total annual receipts and accruals will exceeds that amount. (Gabrie Worku, 2008)

2.9 VAT Registration

In Ethiopia registration for VAT is categorized in to two;

- I. obligatory/ mandatory registration
- II. Voluntary registration

I. OBLIGATORY REGISTRATION

Any person conducting a commercial enterprise or instancing to conduct commercial enterprises or intending to conduct a commercial enterprise may apply to be registered for VAT. However if the taxable turnover of the enterprise, which is gross income for 12 calendar monthly exceeds or is likely to exceeds birr 500,000, the person conducting the enterprise must be register for VAT with FIRA or The Federal Inland Revenue. If the turnover is below birr 500,000 of business activity one may apply for voluntary registration. (Gebrie Worku, 2008).

II .VOLUNTARY REGISTRATION

A person, who carried on taxable activity and is not required to be register for VAT, may voluntarily apply to the authority for such registration. If he/she regularly is supplying or rendering at least 75% of his good and services to registered persons. (Gebrie Worku, 2008)

BENEFIT OF VOLUNTARY REGISTRATION

Input VAT can be recovered if a person is registered. It will therefore be beneficial to voluntarily register where the person makes mainly zero-rated supplies. In such a case input VAT will be recovered and no VAT will be charged on zero-rated outputs. (Gebrie Worku, 2008).

2.10 Registration procedure

Application for compulsory as well as voluntary registration must be made on application form called "APPLICATION FOR REGISTRATION" and the authority is required to register the person in the VAT register, and issue a certificate of registration within 30 days of the registration containing details of:

- The full name and other relevant details of the registered person
- The date of issuance of the certificate
- The date from which the registration takes effect and
- The registered person's tax payer identification number.

If registration is disallowed federal land revenue authority will have to notify the applicant and the reasons for the refusal. The tax authority may deny the application for voluntary registration if the person:

- Has no fixed place of residence or business
- Does not keep proper accounting records
- Has not bank account
- Has previously been registered for VAT purposes but failed to perform his duties under the VAT law. (Gebrie Worku, 2008).

2.11 Time to Application

A person, who carries on taxable activity and is not registered, is required to file an application to VAT registration. It shall file an application for

registration no later than the last day of the month after the end of the period if:

1. At the end of any period of 12 calendar months the person made during those period taxable transactions with a total value exceeding 500,000 Br or the last day of the month of the period if taxable transactions with a total value exceeding 500,000.00 birr.
2. at the beginning of any period of 12 calendar months when there is reasonable ground to expect that the total of taxable transactions to be made by the person during that period will exceed 500,000 birr.(Gebrie Worku, 2008).

2.12 Time of Registration

Registration takes place on one of the following dates, depending on which date comes first:

- In case of obligatory registration, on the first day of the accounting period following the month in which the obligation to apply for registration arose.
- In the case of voluntary registration, on the first day of the accounting period following the month in which the person applied for registration or
- On the data selected by the registered person on his application for registration a registered person who conducts taxable activity in a branch or division shall be registered only in the name of registered person. However, up on application the tax authority may allow the registered person to register on or more of its branches or divisions as separate registered persons. The tax authority allow when it is satisfied on such case that divisions or branches maintains an independent accounting system and can be identified by the nature of its activities or location. (Gebrie Worku, 2008).

2.13 Advantage and disadvantage of VAT

2.13.1 Advantage of VAT

- Under VAT, system the tax is collected in small fragments at different stages of production and sales. Hence, the vat payers feel the burden of the tax less. (Misrak Tesfaye, 2008).
- Exports of goods and services in most countries that implement VAT are liable to VAT at zero-rate. This may make export internationally competitive and, thus encourage export. (Misrak Tesfaye, 2008, p.311).
- It provides detailed information at each stage of production.
- It's collected from all sectors. That is from import, manufacturing and wholesale sector. It is, therefore a more comprehensive and equitable taxation system. Sales tax on the other hand is normally levied only at stage of the whole marketing.(Misrak Tesfaye,2008).
- VAT is a consumption tax. As such, it promotes capital information by not taxing or distorting saving and that is the main reason why many economists favor it. (H.L.BHATLA , public finance)

2.13.2 Disadvantage of VAT

- VAT system involves high cost of administration, assessment, verification, collection etc. Hence, it is highly uneconomically. It also imposes high tax compliance costs on the legal VAT tax payers. (Misrak Tesfaye, 2011,)
- VAT requires good record keeping of invoice at each stage of production both buyer and seller, therefore find compliance to vat to be time consuming and resource draining.
- In VAT system the manufacturers, retailer have to fulfill various legal formalities in the form of maintain various records, accounts, books, etc. The verification of those formalities puts additional burden to the tax enforcing authorities.

- VAT is incongruent with the basic principle of taxation, which states the person should be taxed only according to his/her ability to pay, so it is regressive taxation system. a number of countries have , However, exempted basic necessities , particularly food item from VAT in order to compensate for it regressive effect.
(H.L.BHATLA , public finance)

CHAPTER THREE

3. DATA PRESENTATION, ANALYSIS AND INTERPRETATION

In this section the overall result of the data collection were analyzed and discussed. In order to make easy and inferences were made by comparing types of owner ship (private limited, sole proprietor and share company) and type of business (service, manufacturing, and trades) with their attitude towards the VAT system. Out of 30 questionnaires distributed and only 26 questionnaires were properly filled and returned.

Therefore, these analyses are interpreted based 26 respondents of the survey as follows:

3.1. Characteristics of the study population

Table1. Profile of the respondent

No	Questions	No_ of respondents	Percentage
1	Sex		
	Male	16	53.3%
	Female	10	33.3%
	Not returned	4	13.3%
	Total	30	100

Source, Questionnaire, 2014

In respect to taxpayers, 16(53.3%) of the respondents are males and 10(33.3%) are females and the remaining 4(13.3%) are not returned it respectively. From this the greater numbers of the respondents from the taxpayers are males as compare with females.

Table 2. The Age of respondents

No	Questions	No of respondents	Percentage
1.	Age of respondents		
	18-30	16	53.3%
	31-45	10	33.3%
	46-55	-	-
	above 55	-	-
	Not returned	4	13.3%
	Total	30	100

Source, Questionnaire, 2014

As can be seen above from the table 16(53.3%) of the respondents age are found 18-30, 10(33.3%) of respondents are between 31-45, and the remaining 4(10%) 16 are not returned. This shows that from total respondents the greater number of their age is found between 18-45 so, they are found at young and productive age.

Table 3. Educational status of respondents

No	Questions	No of respondents	Percentage
1.	Educational status		
	12 th Grade or below	10	33.3%
	Certificate	8	26.6%
	Diploma	5	16.6%
	1 st degree	3	10%
	Above degree	-	-
	Not returned	4	13.3%
	Total	30	100

Source, Questionnaire, 2014

Table 3 shows the educational status of the VAT payers. As show above 10(33.3%) of the respondents are 12th Grade or below, 8(26.6%) of the respondents educational status shows they are certificate holders, 5(16.6%) of them have diploma holders, 3(10%) are degree holders and

the remaining are not returned. This shows that the more taxpayers has 12th Grade or below and certificate holder's and more of the respondent is diploma and 1st degree holders and educated so, from this we expected that they will know at least a little bit about VAT rule and regulations.

Table 4.Type of business

No	Questions	No of respondents	Percentage
1.	What is the type of your business?		
	Manufacturing	1	3.33%
	Merchandise	14	46.6%
	Service giving	11	36.66%
	not returned	4	13.3%
	Total	30	100%
2.	Work experience		
	Less than a year	4	13.3%
	1-5 years	14	46.6%
	6-15 years	7	23.3%
	16-25 years	1	3.33%
	above 25	-	-
	Not returned	4	13.3%
	Total	30	100%
3.	Form of your business?		
	Private limited	21	70%
	Share company	1	3.33%
	Partnership	4	13.3%
	not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

As shown above table from the sampled respondents 1(3.33%) engaged on manufacturing activity, 14(46.6%) are engaged on merchandising activity, 11(36.6%) are engaged on service giving activity and 4(13.3%) are not returned appropriately. The work experience of the tax payers 4(13.3%) of taxpayers has worked for less than a year, 14(46.6) has worked for 1-5 years, 7(23.3%) of taxpayers has worked for 6-25 years, 1(3.33%) of taxpayers has worked for 16-25 years and the remaining 4(13.3%) are not returned. We see in the above table more of VAT payers are new for the business and may be not much experience with the business and VAT rules and regulations and some of the VAT payers are more experience in the business they engaged and expected from them at least they know something about VAT system. Table 3.4 shows from the sampled respondents 1(3.33%) form of their business is share company, 4(13.3%) was form their business in partnership, 21(70%) form of their business is private limited companies and 4(13.3%) not return.

Table 5. Types of registration

No	Questions	No_ of respondents	Percentage
1	How did you get registered?		
	Voluntary	12	40%
	Based on my revenue	6	20%
	Decision of ERCA	8	26.6%
	Not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

The above table shows that 12(40%) of the business organization have registered voluntarily, 6(20%) of the business organization have

registered based on they revenue, while 8(26.6%) of the business organization have registered by decision of ERCA, and 4(10%) are not response. This implies that 18 (60%) of the respondents registered by voluntarily we see from this most of the VAT payers understand the VAT advantage and get registered voluntarily with out the enforcement of ERCA, the remaining 4(13.3 %%) have not responded.

Table 6. Years of tax paying

No	Questions	No of respondents	Percentage
1.	How long have you been paying tax with Ledeta sub-city revenue office?		
	less than a year	2	6.66%
	1-5 years	17	56.6%
	6-10 years	2	6.66%
	Above 10 years	5	16.66%
	not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

Table 6 shows 17(56.6%) of the target total population paying tax for the tax authority for 1-5 years, 2(6.66%) of tax payers paying tax for less than a year, 2(6.66%) of taxpayers paying tax for 6-10 years , 5(16.66%) of tax payers paying of tax for above 10 years and 4(13.3%) of tax payers not return the questionnaires. From the above table we see that most of the tax payers are new taxpayers and from the last five years up to now more tax payers registered for VAT as compare as to those 6-10 years.

Table 7. The attitude of respondent towards VAT system

No	Questions	No of respondents	Percentage
1	Are you fully aware about VAT rule and regulation and VAT system?		
	Yes	14	46.66%
	Partially	12	40%
	No	-	-
	Not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

As refer from the above table the awareness of tax payers about the VAT rule and regulation and VAT system answered as follows by respondents 14(46.66%) are yes, 12(40%) are partially, and the remaining 4(13.3%) of them not return the questionnaire. The result shows that the awareness of tax payers about VAT rule and regulation and VAT system are well so, the tax authority create enough awareness to the taxpayers. The tax authority should be creating awareness to the taxpayers that are not register for VAT due to some reasons and other community through different methods.

Table 8.A response towards VAT demand complete accounting System

No	Questions	No of respondents	Percentage
1.	Do you think VAT demands complete accounting system?		
	Yes	24	80%
	No	-	-
	I don't know	2	6.66%
	not returned	4	13.3%
	Total	30	100%
2.	Do you have?		
	Yes	24	80%
	No	2	6.66%
	Not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

From the above table 8, 24(80%) of tax payers agree that VAT demands complete accounting system, 2(6.66%) of them says I don't know and 4(13.3%) not return the questionnaire so, we see from this most of the taxpayers know about VAT because most of them agree VAT demand complete accounting system it is one of the common thing for VAT. Most of the respondents have book of account 24(80%), 2(6.66%) has do not maintain book of account and the remaining 4(13.3%) of the respondent are not returned respectively.

Table 9.a response towards getting registered to VAT affect revenue

No	Questions	No of respondents	Percentage
1.	Do you think getting registered for VAT affect your revenue?		
	Increase revenue	6	20%
	Decreases revenue	9	30%
	Will have no change	11	36.66%
	Not returned	4	13.33%
	Total	30	100%

Source, Questionnaire, 2014

The above table indicated that 6(20%) of the respondent think registered for VAT increase their revenue, 9(30%) of the respondent think registered for VAT decreases their revenue, 11(36.66%) of them says will no change in the revenue because they think VAT do not relate with revenue and 4(13.3%) respondent not return the questionnaire. As seen in the above table, some of the respondent believe that, VAT the has an impact on their revenue by stating their own opinion among these; customer in the market that are not willing to purchase goods and service with VAT because, the price increase in purchasing good and services with VAT, there is no formal (constant) system for VAT so customers shift to goods and service decrease in price. Therefore, the authority has to change the perception of taxpayers those who believe VAT has decrease their revenue. On the other hand 4(13.3%) of the respondents says registered for VAT increase there revenue the reason given by them was they create customer purchase goods and service with VAT regularly.

Table 10.attitude of respondents towards the impact of VAT on customers

No	Questions	No of respondents	Percentage
1	Is there any change in the number of your customer's caused by registration for VAT?		
	Yes	14	46.6%
	No	12	40%
	Not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

Table 10 shows that 13(46.6%) respondents think register for VAT lose there customer and the respondent put the reason why they think register for VAT lose their customer was customer are not willing to purchase goods and service that include VAT rate into its prices, in the country there are a number of business enterprises sold goods and service with out issuing sales invoice due to this reason the price of their goods is decrease as compare as VAT register enterprises, the goods available in the VAT registrant shop also available in the none VAT registrant shop with a low price and customers buy there, some business aiming to get huge profit with out paying tax they decrease the purchasing price of goods and services because of this more customer purchase goods and service with them and the absence of customers that have purchasing goods with VAT experience and habits, awareness of society about VAT is low and the number of customer decrease due to

the fact that was not understood the advantages of the tax system so they shift to non VAT paid companies but if all were registered customer will not shift since any there is 15% of VAT and 12(40%) of the respondents says they didn't lose their customer because of being registered for VAT they state their reasons; VAT registrant customer buy good and service with them for VAT input and 4(13.3%) respondent not return the questionnaire.

Table 11. Attitude of respondents towards the market competition

No	Questions	No_ of respondents	Percentage
1	Do you think that none VAT registrant is competitive than VAT registrant in the market?		
	Yes	17	56.6%
	No	9	30%
	Not returned	4	13.3 %
	Total	30	100%

Source, Questionnaire, 2014

As one can observed above table, out of the 30 taxpayer respondent, 17(56.6%) respondent said that enterprises that are not registered for VAT are more benefited from market competition, 9(30%) respondents think that VAT registered enterprises are more benefited and 4(13.3%) not returned it. from this result most of the respondent 17(56.6%) said that enterprises that are not registered for VAT are taking the advantage of the market competition . purchasing of goods and services with VAT requires incurring additional cost than with out VAT, it is obvious customer prefer to purchase goods and service from those entities that

exclude the VAT rate from the prices of the items that they provide to the customer. And 9(30%) of the respondent believe that, non-VAT registrant are less competitive than VAT registrant in the market. it is clear that non- VAT registrant can't get VAT input benefit in the purchase and they can't participate in legal activity and import and export activity. There are some eligible business enterprise in the market whose annual turnover are more than or equal to birr 500,000 but not yet register for VAT due to they think they lose their customer, lack of awareness about VAT system and advantage. If all eligible companies not register the registered companies will not be competitive in the market due to this governments revenue from VAT will decrease. thus to balance the market competition and increase the government revenue the authority should also investigate and bring those enterprises that are not yet registered for VAT but able to register.

Table 12. Attitudes of respondents against awareness created by tax administration.

No	Questions	No of respondents	Percentage
1.	Do you agree that Tax administration create enough awareness to tax payer?		
	Strongly agree	-	-
	Agree	19	63.3%
	Disagree	7	23.3%
	Don't know	-	-
	not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

Table 12 shows 19(63.3%) of respondents agrees on the idea that on the tax administration creates enough awareness about the system through orientation, training and broadcast. 7(23.3%) respondents disagrees on the idea that on the tax administration creates enough awareness about the system, and 4(13.3%) not returned. Generally seen most of the total populations agree on the idea that the tax administration create enough awareness about VAT we see in the above tables we see tax payers get enough understand about VAT.

Table 13. The attitude of respondents towards the implementation of VAT system seems complex.

No	Questions	No of respondents	Percentage
1.	Is the implementation of VAT system is complex?		
	Strongly agree	8	26.6%
	Agree	6	20%
	Disagree	4	13.3%
	Don't know	8	26.6%
	not returned	4	13.3%
	Total	30	100%

Source, Questionnaire, 2014

Table 13 shows 8(26.6%) and 6(20%) of them respectively strong agree and agree on it when we see their attitude toward its complexion and 4(13.3%) of them disagree on the idea. The remaining 8(26.6%) replay I do not know and 4(13.3%) of them not return it. The above result indicates tax administration was not crating enough awareness for tax payers. This awareness would not have been created be for implementation of tax system even after implementation some of tax payers were not agreeing about the system. That is why tax payer's

thinks as VAT is not advantageous and it will increase price on commodity. Value added tax system is complex tax system than the other tax systems. It is difficult to implement the whole concept once but users know basic principles.

CHAPTER FOUR

SUMMARY, CONCLUSION AND RECOMMENDATION

4.1 Summary of findings

The overall objective of this study was to assess Value added tax on the side of taxpayers. The method used to prepare this paper is judgmental sampling technique of non probability sampling method and used primary data obtained through questionnaires. The method of analyzing and presenting data the researchers used descriptive analysis method like percentage and tables.

Based on the analysis and discussion made in chapter three the following summary can be drawn;

- Most of the taxpayers in Ledeta sub-city have been start business at young ages who are not much experienced to the business.
- Most of the business organization registers for VAT voluntarily.
- Even if most taxpayers has positive attitude to the basic VAT rules and regulation, they afraid that register for VAT will lose their customer.
- In the sub-city most of taxpayers feel VAT as useful and their understanding about taxation is highly developed and positively awareness to VAT system.
- Most of the taxpayers agreed tax administration has created enough awareness about VAT system to the taxpayers through orientation, training and broadcast.
- 80% of the taxpayers are agreeing that VAT demands complete accounting system and all of them maintain appropriate book of account.

- Most of the taxpayers agreed implementation of VAT system is complex.
- Most of taxpayers that are found at young age and diploma and degree holder taxpayers are fully aware about VAT rules and regulations. This implies that educational status of a taxpayers are related with there level of understanding about VAT rule and regulation.
- Some of the taxpayers agreed there are some changes in the number of there customer's caused by registration for VAT.
- Most respondents relied that eligible companies which have annual sales of $\geq 500,000$ birr were not registered fully. This will affect the registered one at the time of competition.

4.2 Conclusion

As far as Government has existed and performed various activities it should come up with means of financing its activities. VAT is increasingly being used through out the world to raise government revenue with less administrative and economic costs than other broadly based taxes. On the basis of the finding the following conclusions are drawn;

The main reason for failure of the business community to implement VAT regulation is implementation of VAT system seems complex for the taxpayers, eligible business try to avoid being register for VAT because of market competition and lose of their customers. Tax administration tries to create awareness among tax payers, but it is not considers the society. Tax administrations consider the only tax payer since; VAT is indirect tax in which lived on users the society should also aware. Tax administration is not control both registered and unregistered business. This create some perception in the mind of business organizations and they do not register for VAT this will decreasing government's tax revenue, there are some eligible business enterprise in the market whose annual turnover are more than or equal to birr 500,000 but not yet register for VAT due to they think they loss their customer, lack of awareness about VAT system and advantage, aim to get huge profit with out paying VAT.

Generally seen the attitude of the tax payers towards the VAT system is well but, there are some tax payers with the negative attitude toward VAT system. They thought as it negative impact on number of customers and it crates obstacle during competition and affect their revenue. The level of understanding about rules and regulations of the VAT payers depend on their educational status, work experience and their age.

4.3 Recommendation

As to the study conducted there are certain problems to VAT on the side of taxpayers in Ledeta sub-city. Based on the research findings the following points can be forwarded as recommendation.

- Taxpayers must receive clear, precise and up-to-date information on describing what is VAT, what are the rules and regulations, how to calculate their tax liability and procedures for calculating to make implementation of VAT regulation easy .
- Tax administration should make serious control up on registered and non- registered business. If all eligible company's not register the registered companies will not be competitive in the market due to this government revenue from VAT will decrease. Thus to balance the market competition and increase the government revenue the authority should also investigate and bring those enterprises that are not yet registered for VAT but able to register.
- To improve the awareness, attitude, and feeling of tax payers the government should arrange seminars, workshop, and conference to make them aware concerning VAT, the advantage they get from VAT.
- Basically the tax is for the benefit of people and country however, since most of the people do not know this fact and awareness should be created among the people to purchase goods from those business organizations register for VAT and motive them.

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ST.MARY'S UNIVERSITY
DEPARTMENT OF ACCOUNTING

QUESTIONNAIRE FOR TAXPAYERS

The purpose of this questionnaire is exclusively for academic purpose which is intended to obtain relevant information for assessment of VAT in Lideta Sub-city. The findings of this study shall greatly depend on your cooperation for which we are grateful in advance. To achieve this you are kindly requested to co-operate by giving responses for the following questions. Please put a tick mark (P) on the box of your choice and fill the blank spaces where applicable.

N.B:

- No need of writing your name
- Where the enquiry is subjective, please use the blank space provided to give your answer
- Please try to respond as accurately as possible, and at your earliest convenience.

Questions

1. Sex: Male Female

2. Age (years): 18-30 31-45 46-55 >55

3. Educational status:-

12th Grade or below Certificate Diploma
1st Degree above 1st Degree

4. What is the type of your business?

Manufacturing Trading Service giving

5. Work experience? Less than a year 1-5 year 6-15
years

16-25 years above 25 years

6. Form of your business sector?

PLC Sole proprietor

Share company Partnership

7. How did you get registered?

Willingly Based on my revenue Decision of ERCA

8. How long have you been paying tax with Lideta Sub-city Revenue Office?

Less than 1 year 1-5 years 6-10 years

Above 10 years

9. Are you aware about VAT rule and regulation?

Yes Partially No

10. Do you think implementation of VAT demands complete accounting system?

Yes No don't know

Others, please specify _____

11. Are you maintain appropriate book of account?

Yes No

If your answer is No, please specify your reason _____

12. Do you think getting registered to VAT affects your revenue?

Increases will have no change Decreases

How? _____

13. is there any change in the number of your customer's caused by registration for VAT?

Yes No

How? _____

14. Do you think that non-VAT registrant is more competitive than VAT registrant in the market?

Yes No

15. In your opinion, do you agree that the Tax Authority has made enough awareness creation to tax payers?

Strongly agree Agree Disagree Don't know

If you agree, how? Memo broadcast training

If others, please specify _____

16. In your opinion, is the implementation of VAT system complex?

Strongly agree Agree Disagree Don't know

If others, please specify _____

DECLARATION

Advisee's Declaration

We, the underlined, declare that this senior essay is our original work, prepared under the guidance of Ato Habtamu Eshatu. All resource of materials used for the manuscript have been duly acknowledged.

Name: _____

Signature: _____

Name: _____

Signature: _____

Name: _____

Signature: _____

Place of submission: _____

Date of submission: _____

Advisor's Declaration

The paper has been submitted for examination with my approval as the university Advisor.

Name: _____

Signature: _____

Date: _____