



St. Mary`s university
School of Graduate Studies

ASSESSMENT OF TAX AUDIT PRACTICE AND ITS CHALLENGES: IN THE
CASE OF LARGE TAXPAYERS OFFICE, ERCA.

BY
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ADDIS ABABA

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Abstract

Tax audit is an activity or a set of activities performed by Tax auditors to determine taxpayer's correct tax liabilities for a particular accounting or tax period. Many countries have adopted a self-assessment system (SAS) including Ethiopia; Tax audit is a key feature of the self-assessment system (ERCA2010). The researcher believes that researches on this area will have invaluable contribution for the tax authority to achieve its objectives and to improve its tax administration. The main objective of this study is to assess the tax audit practice and its challenges in the case of large taxpayers' office and tries to assess the application of IT in tax audit, the proficiency of auditors, functions of auditing in the reduction of tax evasions and avoidances and how it is exercised to increase the compliance level of taxpayer. To achieve these objectives descriptive method of research was used and both quantitative and qualitative research approach were used and, data were collected from primary and secondary sources, the primary data were collected using survey method from the tax audit staffs and large taxpayers'. The primary data were collected from a well-structured questionnaire distributed to 55 tax audit staff respondents and out of these 45 were returned and distributed to 67 taxpayers' respondents out of which 58 were returned and the secondary data was from scholarly published studies, internet sources, journals and ERCA published and unpublished documents. The analysis provided the tax audit has problems in the application of information technology /SIGTAS/ maximum its capacities, incompetent auditors to tackle tax evasion and avoidance, weak taxpayers' education program which cannot improve the compliance level of taxpayers'. The study concluded that if tax audit were conducted by competent auditors, and supported by IT, it would have resulted in effective tax administration, improved compliance level and increased tax revenue. The study recommended that the tax authority /ERCA/ should improve the capabilities of tax auditors, and apply IT in its audit to its maximum. As far as the knowledge of the researcher is concerned, no research has been done on the tax audit practice and its challenge in large taxpayer's office.

Key words: tax audit, self-assessment system, SIGTAS, evasion and avoidance and compliance.

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ACRONYMS /ABBREVIATIONS/

| | |
|--------|--|
| AEO | Authorized Economic Operators |
| CPA | Certified Public Accountant |
| CRM | Client/Customers Relationship Manager |
| EC | Ethiopian Calendar |
| ECC | Ethiopian Chamber of Commerce |
| EFY | Ethiopian Fiscal Year |
| ERCA | Ethiopian Revenue and Custom Authority |
| GDP | Growth Domestic Product |
| HQ | Head Quarter |
| IT | Information Technology |
| LTO | Large Taxpayer Office |
| ND | Not Dated |
| Mo FED | Ministry of Finance and Economic Development |
| OECD | Organization for Economic Co-ordination and Development |
| OLA | Office of the Legislative Auditors |
| SIGTAS | Standard Integrated Government Tax Administration System |
| RTA | Relevant Tax Authority |
| SAS | Self-Assessment System |
| VAT | Value Added Tax |

CHAPTER ONE: INTRODUCTION

1.1. Background of the Study

Taxation provides governments with the funds needed to invest in development, relieve poverty and deliver public services. It offers an antidote to aid dependence in developing countries and provides fiscal reliance and sustainability that is needed to promote growth. Significant progress has been made by many developing countries but weak capacity, corruption and the missing reciprocal link between tax and public and social expenditures remain as challenges (IMF, OECD, UN & World Bank, and 2011:8).

Many countries have adopted a self-assessment system (SAS) including Ethiopia. The tax return furnished by the taxpayers is deemed as final and accepted at face value. Tax compliance under the SAS is highly dependent on voluntary compliance i.e. honesty of the taxpayers in computing their tax payable. Another significant aspect of the SAS is tax audit. Tax audit is an examination of taxpayers' business records and financial affairs to ensure taxpayers have computed their tax payable in accordance with the current tax laws and regulations (Isa and Pope, 2011:42-56). In a self assessment system, taxpayers should be induced to comply by being: (1) provided with information and assistance to enable them assess themselves; (2) informed that not everyone will be audited but rather that cases will be selected for audit on the basis of risk; (3) convinced that if they understate their tax liability there is a high probability that they will be audited; and (4) convinced that if they do not meet their basic obligations they will be penalized (East AFRITAC, n.d).

Following the increasing cases of tax noncompliance, especially tax evasion and its consequences on the capacity of government to raise public revenue, great amount of attentions have been paid to the issue of tax compliance globally by public policy makers and researchers for the past few decades now. However, bulk of the researches on tax compliance is on developed countries especially the US; it is limited on developing countries (Alabede, Ariffin&idris, 2011:91-140).

The audit programme of a revenue body performs a number of important roles that, effectively carried out, can make a significant contribution to improved administration of the tax system. A

tax audit is an investigation into background of tax returns submitted by an individual or business to a tax agency. The idea of a tax audit normally conjures up feelings of anxiety even in persons who believe their tax documents are perfectly in order. While it is true that a tax audit may be called due to some perceived irregularity in one or more returns, it is also true that an audit may be done simply as part of a random sampling. Most governments around the world include an agency that is charged with overseeing the process of tax collection from individuals and companies that reside within the jurisdiction (OECD, 2006).

According to ERCA (2010). Tax audit is an activity or a set of activities performed by Tax auditors to determine a taxpayer's correct tax liabilities for a particular accounting or tax period, by examining a taxpayer's organization procedures and financial records in order to assess compliance to tax laws and verifying the true, fair, reliable, and accuracy of tax returns, and financial statements. Conducting an audit, various types of information will be reviewed namely, tax returns, financial statements, accounting records, customs declaration and other source documents. Despite the fact that people need to pay taxes based on rationales of vertical and horizontal equities, it is not always the case that tax systems are comprehensible and transparent for tax payers especially for less literate business operators. Tax systems are usually not elaborated after proper consultation with the business community. The business owners complain that the tax assessment method is based on subjective estimation as a result of which they are frequently subjected to over-taxation. Since the business owners do not have simplified access to and clarification on information of the tax laws, they lack awareness on tax rules and regulations and this has an impact on the practicability of the regulations (ECC, 2005)

Tax audit has dual benefits for the tax authority: through direct assessment of additional taxes and indirectly through awareness creation of taxpayers to comply with tax law, thus tax audit plays an invaluable role in both increasing the government revenue and improving the compliance of tax payer. Thus the researcher tried to assess the tax audit practice and its challenges by collecting and analyzing data from the tax audit staffs and taxpayers of large taxpayers' office.

1.2 Statement of the Problem

A government finances its expenditures through the fund acquired from the service given by the government agencies, tax, loan and donation. From all sources of finance, tax is the major source, however, in most developing countries, like Ethiopia it is a common phenomenon to notice serious problems in developing adequate tax systems that permits a government to sufficiently finance its expenditures.

According to Tanzi & Zee (2000, as cited by Kayaga, 2007:3), explanation in developing countries where market forces are increasingly important in allocating resources; the design of the tax system should be as neutral as possible so as to minimize interference in the allocation process. The system should also have simple and transparent administrative procedures so that it is clear if the system is not being enforced as designed, developing countries would like to increase their tax-to-GDP ratios in order to reduce budget deficits, improve the services they provide, and optimize the effectiveness of their tax structures. Although it is commonly said that the only things certain in life are death and taxes, it is unmistakable that taxes are in fact far from inevitable. Individuals do not like paying taxes, and they take a variety of actions to reduce their tax liabilities. Some of these actions can be classified as tax avoidance or the legal reduction in tax liabilities by practices that take full advantages of the tax codes, such as income splitting, postponement of taxes and tax arbitrage across income that faces different tax treatment. Evasion consists of illegal and intentional actions taken by individuals to reduce their legally due tax obligation. Individuals and firms can evade taxes by underreporting income, sales or wealth, by overstating deductions, exemptions, or credits or by failing to file appropriate tax returns. From its part government must take actions to ensure compliance with the tax laws (Alm, 1999:1)

In Ethiopia the economy continued to grow rapidly the eighth consecutive year registering in 2010/11 a real GDP growth rate of 11.4%. Particularly tax revenue exhibited an impressive performance becoming 11.5% of GDP compared to what it was in 2009/10 (11.3%); after showing a declining trend for the past five years (MOFED, 2011). However, even if there is an increase in the tax to GDP ratio for last few years, it is still low as compared to the Sub Saharan countries tax to GDP ratio 18% whereas the Ethiopia tax to GDP ratio is 11.6% for the fiscal year 2004 E.C (ERCA, 2012). ERCA planned to collect (30.5 Billion, 45.5 Billion, 70 Billion, and 87

Billion) birr for the fiscal year 2002-2005 E.C and the actual collected tax was (35.7Billion, 50.82 Billion, 70.75 Billion and 84.4 Billion) birr respectively there was progress for the fiscal year 2002-2004 E.C and for 2005 E.C it only achieves 95% of its targeted plan. Tax administration is an extremely important area for public sector reform in Ethiopia as it is a key issue in raising domestic revenue to support the delivery of Ethiopia's public services.

ERCA has given attentions to taxpayers' segmentation that is large taxpayers, medium and small and micro, to provide fast taxpayers service and to handle their tax affairs in a manageable manner. Accordingly large taxpayers' office is established by the tax authority to provide service for customer/taxpayers whose Annual turnover is above 27,000,000 and this branch office contributes the largest portion of the total domestic tax revenue collected by the tax authority for instance ERCA's plan for the fiscal year 2008 E.C from domestic tax revenue is 144,348,140.000 and out of this 60,000,000,000 or (41.67%) is collected by LTO branch office, closer to 50% is collected by customs office and the remaining (8.33%) collected by other medium and small local tax branches (ERCA, 2016). If tax evasions and avoidances take place /occur in this branch it adversely affects the government's revenue, to mitigate such problems, therefore, a successful audit program should be implemented which is capable to investigate, detect and prevent loss of tax revenue, and to improve its tax administration an tax potential. Clearly the main problems are Tax to GDP ratio is low as to sub Saharan countries an there is high tax avoidance an evasion.

Thus researcher believes that researches on this area will have invaluable contribution in identifying weak areas and recommending possible solutions to the tax authority to achieve its objectives and to improve its tax administration. Hence, the researcher becomes interested to assess the tax audit practice and its challenge in the case of large taxpayers' office and the study is limited to the tax audit. Other than previous studies conducted on assessment of tax audit practice, the case of Hawassa City Administration by Netsanet Bibiso (2014) and Tax audit practice and its significance in increasing revenue in Ethiopia the case of Addis Ababa City Administration studied by Mesfin Gebeyehu (2008), this study tried to identify different factors that have fundamental effect for tax audit performance.

Research Questions

1. What are the functions of tax audit in improving the compliance level of tax payers in LTO?
2. How tax auditors are competent in ERCA, LTO?
3. How tax audit is exercised in the reduction of tax avoidance and evasion?
4. What are the challenges of the application of IT in tax audit?

1.3. Objective of the Study

1.3.1 General Objectives

The main objective of this study is to assess the tax audit practice and its challenge in ERCA large taxpayers' branch office.

1.3.2 Specific Objective

The specific objectives of the study focus on the following

1. To explore the function of tax audit in improving the compliance level of taxpayers
2. To examine the tax auditor's proficiency, integrity and competence
3. To assess how tax audit is exercised in the reduction of tax avoidance and evasion.
4. To assess the challenges in the application of information technology / SIGTAS/ in the tax audit.

1.4 Significance of the Study

The study helps in identifying the existing challenges posed on the successful tax audit practice. By identifying the major constraints, the findings of the study are expected to indicate the strategic intervention areas that might improve the audit practice, and will show those areas that need corrective measures to improve the tax administration. In addition the study will provide information related with tax audit practice and its challenges for different stakeholders such as government, and the society.

The study also provides information for policy makers to make legal amendments to improve the current tax administration in order to collect potential tax and improve voluntary compliance, by

making the tax laws simple and understandable for taxpayers, and for the researcher in fulfilling MA in business administration.

Finally, for those who are interested to make further study on the related issues/areas may be used as indication.

1.5. Scope of the Study

The research covered the Ethiopian revenue and custom authority, large tax-payers office which targets only taxpayers who resides in Addis Ababa, (i.e. excludes taxpayers who are registered in regional tax authorities). The study assessed the tax audit practice and its challenges in the branch office, the application of Standard Integrated Government Tax Administration System (SIGTAS) for the audit function, and the tax audit functions to tackle evasions and avoidance, to improve the compliance level of taxpayers and examine the proficiency and experience of tax auditors in the branch office. The study covers tax audit performance of the branch from 2006 to 2008 E.C.

1.6 Limitation of the Study

Thus the study had some limitations; the major limitations were it only focused on the audit practice of LTO without including other branches and regional tax authorities. Being unable to held an interview with the tax audit director and shortage of secondary sources of data in relation to the tax audit performance from the directorate that could enable to have more information on the study and there is also information limitation from taxpayers side for not including other business sectors other than the 4 business sectors taken as a sample because of their number being more in the branch.

1.7 Organization of the Paper

This paper is organized in five chapters each incorporating topics and sub topics. The first chapter is an introductory part that summarizes the introduction of the study, statement of the problem, objectives of the study, significance of the study, and scope and limitation of the study.

The related literatures were reviewed and presented in the second chapter. In the third chapter research methodology, techniques of data collection and analysis were presented, and the central part of the research data analysis and discussion formed the fourth chapter. Finally, the fifth chapter presents the conclusions and recommendations based on findings.

CHAPTER TWO: LITERATURE REVIEW

This section presents a brief review of existing theoretical and empirical of tax audit practices in three sections. The first section presents theoretical review of tax audit; the second section presents the empirical evidence on tax audits and related issues and the third section deals with conclusion of the chapter and the knowledge gaps that motivate this study.

2.1 Theoretical Studies

2.1.1 Definition of Tax

A tax is a compulsory levy by government through its agencies on the income, consumption and capital of its subjects. These levies are made on personal income such as salaries, business profit, internal, dividend, discount or royalties to obtain revenue. Taxation is a compulsory payment or transfer of resources from private to public sector levied on the basis of the determined criterion and without reference to specific benefits received in order to accomplish some of the nation's deals with conclusion of the chapter and the knowledge gaps that motivate this study.

Tax administration

Reaping revenue from tax requires effective tax administration. Raising revenue from base expansions requires even better administration. The best tax policy in the world is worth little if it cannot be implemented effectively. How a tax system is administered affects its yield, incidence and its efficiency. Unfair and capricious administration brings the system into disrepute and weakens the legitimacy of government (ECSU, 2012).

2.1.2 Definitions of tax Audit

A tax audit is an examination of whether a taxpayer has correctly assessed and reported their tax liability and fulfilled other obligations. Tax audits are often more detailed and extensive than other types of examination, such as general desk checks, compliance visits/reviews or document matching programmes. There are, of course, exceptions to this rule, conditions and approaches which varies from country to country (OECD, October 2006:74). Generally, an audit will examine the issues seen as most significant to achieving an accurate assessment of a taxpayer's

tax liability typically, these issues will include any indications of significant unreported income (for example, as maybe suggested by a very low ratio of net/gross business income ratio computed from a taxpayer's return) or potentially over-claimed deduction items that may be apparent from an examination of a taxpayer's tax return and other information. As well as income tax returns and other reporting, this includes supporting documents, which the taxpayer should normally have in the case of business audits, national law often requires a business to obey certain bookkeeping and accounting standards. The audit may also involve physical enquiries, such as the inspection and examination of goods in stock, premises etc (OECD, October 2006).

According to ERCA (2010), Audit is defined as the structured examination of a business' relevant commercial systems, financial and non-financial records, physical stock and other assets, internally generated data and that produced independently of the business. Tax audit is an activity or a set of activities performed by tax auditors to determine taxpayers' correct tax liabilities for a particular accounting or tax period, and this is done by examining taxpayers' organization procedures and financial records in order to assess compliance to tax laws and verifying the true, fair, reliable, and accuracy of tax returns, and financial statements.

2.1.3 Types of Audits

Audit cope and intensity: Audits can vary in their scope and the level of intensity to which they are conducted. OECD (2006:9) noted that, various terminologies have evolved to describe different types of audit activity:

Full audits: - the scope of a full audit is all-encompassing. It typically entails a comprehensive examination of all information relevant to the calculation of a taxpayer's tax liability for a given period. The objective is to determine the correct tax liability for a tax return as a whole. In some countries full audits are carried out as part of random audit programs that are used to gather data on the extent, nature and specific features of tax compliance risks, for compliance research purposes and/or the development of computerized audit selection formula. Given their broad scope, full audits are typically costly to undertake a substantial program because they require

considerable resources and reduce the rate coverage of taxpayers that could otherwise be achieved by a more varied mix of audit types.

Limited scope audits:-Limited scope audits are confined to specific issues on the tax return and /or a particular tax scheme arrangement employed by the taxpayer. The objective is to examine key potential risk areas of noncompliance. These audits consume relatively fewer resources than full audits and allow for an increased coverage of the taxpayer population.

Single issue Audits:-

Single issue audits are confined to one item of potential non-compliance that may be apparent from examination of a taxpayer's return. Given their narrow scope, single issue audits typically take less time to perform and can be used to review large numbers of taxpayers involved in similar schemes to conceal non-compliance.

2.1.4 Audit case Selection methods/techniques

As Gupta and Nagadevara(n.d), noted tax audit is a detailed exploration into the activities of a taxpayer to determine whether he/she has been correctly declaring the tax liabilities. Audits indirectly drive voluntary compliance and directly generate additional tax collections, both of which help tax agencies to reduce the 'tax gap' between the tax due and tax collected. Audit plays the pivotal role in the administration of tax and achieving the revenue objectives, ensuring the fiscal health of country and ensures a level playing field for an honest taxpayer. On the other hand, being an intrusive method, audit is not a very welcome procedure both for the taxpayers as well as the economy. Conducting of audits involves costs to the tax department as well as to the taxpayer. Tax administration agencies must therefore use their limited resources very judiciously to achieve maximal taxpayer compliance, minimum intrusion and minimum cost. Planning an regulate audit strategy there for, is a key success factor in a posteriori fraud detection (where audits are intended to detect tax evasion and fraudulent claims) as well as proactively preventing frauds and tax evasions.

Selecting returns for Audits is like looking for a needle in a haystack. Every year, a large number of taxpayers fail to declare their tax liabilities correctly, and the Tax Administration is forced to

tackle a tough task to detect them (and enforce compliance from them) without increasing the compliance costs of the tax compliant taxpayers. It is not possible to identify the likely tax evaders by simple query and reporting tools. Tax departments have access to enormous amounts of taxpayer data. However, it is impossible to ascertain the legitimacy of and intention behind a claim or a declaration in the tax return by simply looking at the return or profile of a taxpayer (Gupta & Nagadevara, n.d).

2.1.4 Risk Based Audit Selection

FRCA is required to audit some or all its taxpayers to verify if customers are paying the right tax at the right time. Conducting audits involves costs to the tax department as well as to the taxpayer. To make audit more efficient and effective and to maximize resources, audit selection based on establish risk criteria will be used to select a particular taxpayer for audit (ERCA, 2010). The following diagram demonstrates how risk based tax audit is manage.

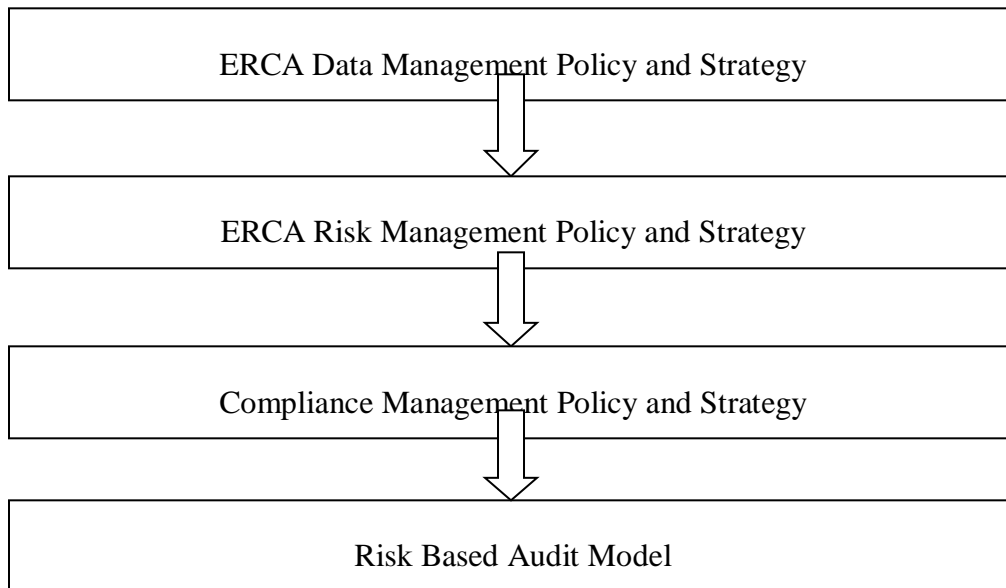


Figure 2.1: The Risk Based Audit Model

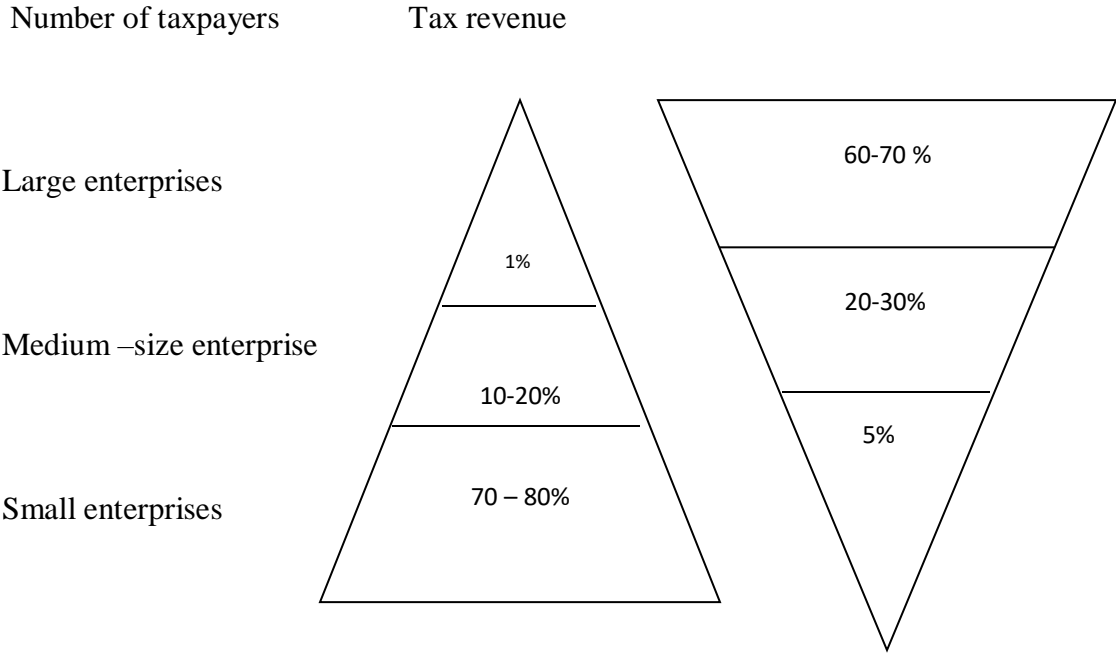
Source: ERCA (2010)

Table 2.1: Characteristics of taxpayer sectors and audit approaches

| Business Size | Small and Micro | Medium | Large |
|------------------------------|---|---|---|
| Number of Taxpayers | Large | Moderate | Small |
| Revenue at risk per taxpayer | Small amounts | Moderate amounts | Large amounts |
| Areas of Noncompliance | Receiving cash without tax withheld, poor records, not registering, not filing. | Understating sales, overstating purchases and expenses, falsification of documents, “creative” Accounting. Diversion of income to wealthy owners. | Tax treated as an expense to be minimized through: complex and dynamic structures, involving financial products, global and local non arms length and non commercial transactions, and aggressive interpretation of the law |
| Audit Treatment | Selective, simple Auditing using education and penalties ad a leverage tool to gain compliance through the broader community. | Single issue audits focusing on areas of non-compliance and using sampling and computer audit techniques. | Tailored audits by teams comprising specialists in specific taxes, industry sectors, international and computerized audit. |

An understanding of the characteristics of taxpayers, their behaviors, and areas of non-compliance, is necessary so as to be in a position to identify, assess and prioritize risks. The international and execution of appropriate treatment strategies, e.g. the particular types of audit, resources allocated, and sanctions imposed, must have a strong correlation to the nature of the risk East AFRICTA, n.d.). The table above illustrates the different characteristics of taxpayer segments and the appropriate responses from an audit program. Profiling the taxpayer population will aid an understanding of features, compliance risks and the development of appropriate treatment strategies.

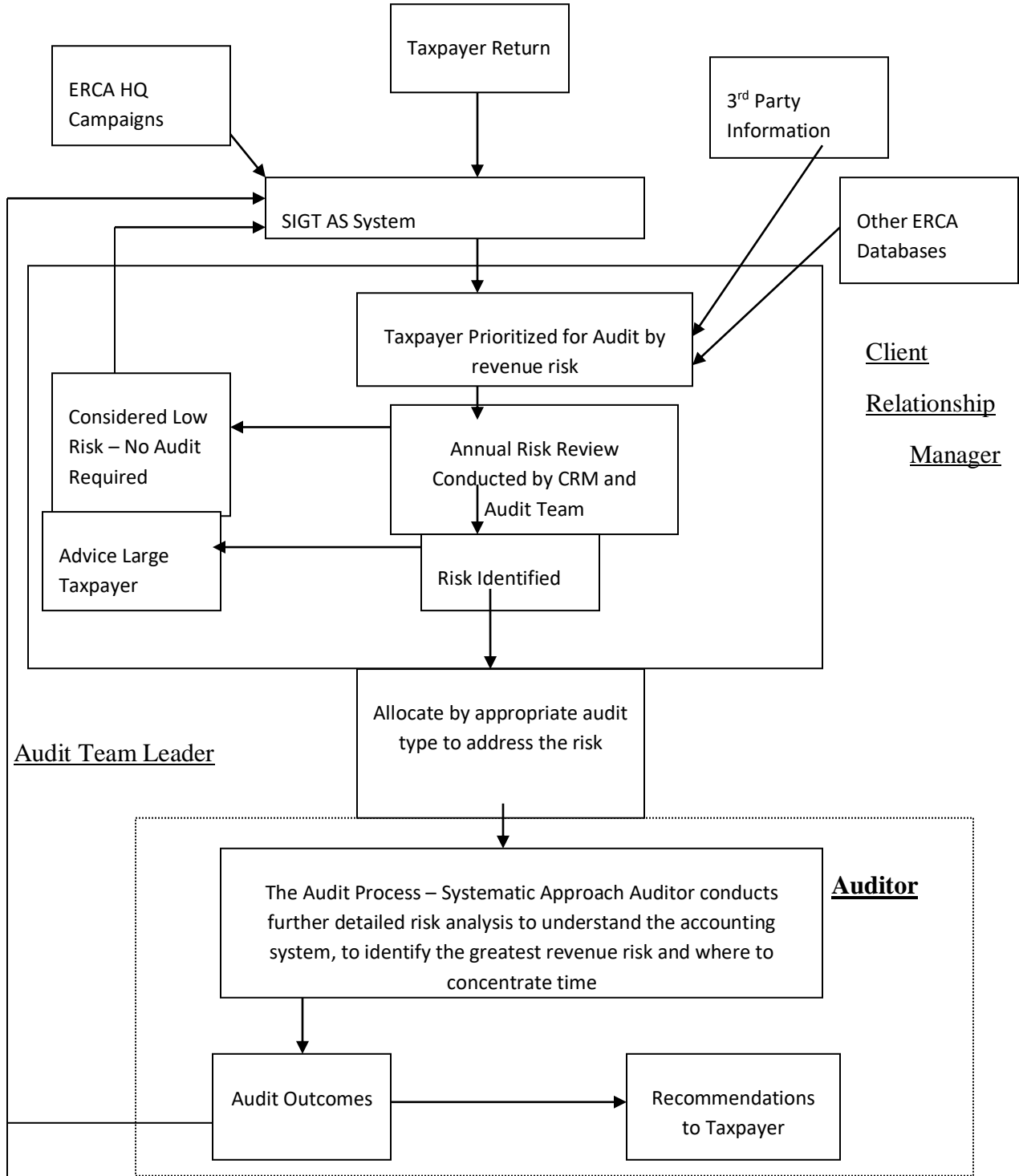
Distribution of taxpayers and revenue



Source: East AFRITAC (2007)

Figure 2.2: Distribution of taxpayers and revenue

ERCALTO Branch – Audit Selection Model



Source: ERCA (2010) Figure 2.3 ERCA LTO Branch- Audit Selection Model

2.1.5 The Roles and functions of a taxpayer audit program

Tax administrations carry out audits so as to verify that the taxpayer has complied with provisions of the tax legislation. However, the role of an audit program in a modern tax administration goes beyond verifying a taxpayer's reported obligations and detection of discrepancies between a taxpayer's declaration and supporting documentation. Audit can play major role in improving tax administration and overall taxpayer compliance by impacting on taxpayer behavior. In addition to raising revenue directly from audit activities, by selecting the higher risk cases, efficiently detecting non-compliant taxpayers, applying appropriate sanctions, and publicizing results of audit activity (either generally or specifically), taxpayers get the message that any attempt to avoid tax presents a high risk of detection and the penalty for non-compliant taxpayers is substantial (East AFRITAC, n.d) .Tax audits therefore provide the tax administration with significant leverage across the community rather than only impacting on the taxpayer selected for audit and collecting the tax that should have been paid in the first place. Additionally, a tax system that is perceived to be fair and equitable, and punishing taxpayers who do not comply builds community confidence and encourages compliance from the broader population.

According to OECD (October, 2006:8), the audit programme of a revenue body performs a number of important roles that, effectively carried out, can make a significant contribution to improved administration of the tax system. These roles are described briefly hereunder:

Promote voluntary compliance; The primary role of the audit program is to promote voluntary compliance by taxpayers with the tax laws. It seeks to achieve this by reminding taxpayers of the risks of noncompliance and by engendering confidence in the broader community that serious abuses of the tax law will be detected and appropriately penalized (OECD October, 2006).

Detect non – compliance at the individual taxpayer level by concentrating on major areas of risk (e.g.unreported cash income) and those individual taxpayers most likely to be evading their additional tax revenue collections (OECD October, 2006).

Gather information - on the “health” of the tax system (including patterns of taxpayers’ compliance behavior): the results of normal audit activity may provide information on the general well being of the tax system. Audits conducted on a random basis can assist overall revenue administration by gathering critical information required to form judgments on overall levels of tax compliance – that over time can be used to identify trends in overall organizational effectiveness and to gather more precise information that can be used to inform decision- making on future compliance improvement strategies, to refine automated risk-based case selection processes, and even support changes to tax legislation (OECD October, 2006) .

Gather intelligence: Audits can assist clarify the application of the law for individual taxpayers and to identify improvements required to recordkeeping and thus may contribute to improved compliance by taxpayers in the future (OECD October, 2006).

Identify areas of the law that require clarification: Audits may bring to light areas of the tax law that are causing confusion and problems to large numbers of taxpayers and thus require further efforts by the revenue body to clarify the laws` requirements and/or to better educate taxpayers on what they must do to comply into the future. Given the broad range of roles to be performed a revenue body’s audit program typically entails the largest allocation of a revenue body`s total staff resources. From this perspective alone, the audit program represents a sizeable strategic investment that dictates the need for sound management policies and practices (OECD October, 2006).

According to East AFRITAC, (n.d.), explanation the impact of an effective audit program should he been in terms of the following effects.

Corrective –Making adjustments to detected instances of non-compliance.

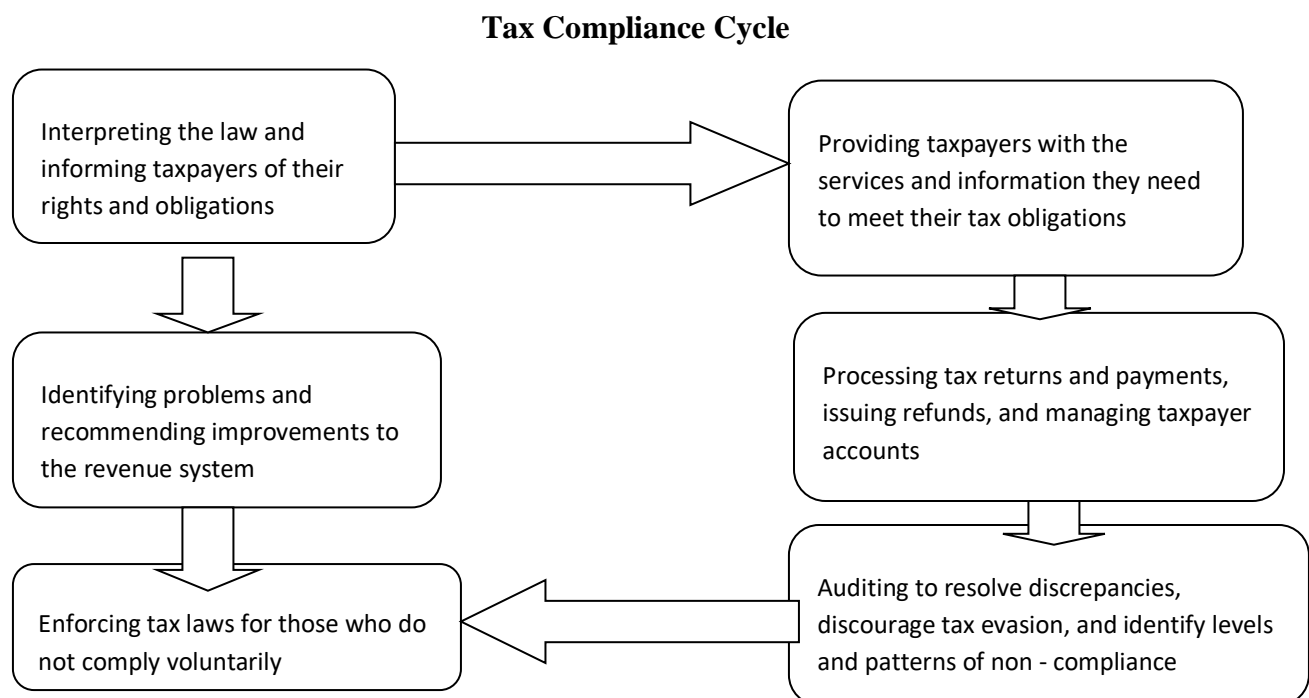
Deterrent –Influencing the behavior of the audited taxpayer or sending warning signals to potential non-compliant taxpayers to be compliant in future.

Preventive – the leverage effect of an efficient audit program on broader community compliance.

2.1.6 Tax Compliance

The taxpayers' attitude on compliance may be influenced by many factors, which eventually influence taxpayer's behavior. Those factors which influence tax compliance and/or non-compliance behavior are differing from one country to another and also from one individual to another Kirchler, (2007), as cited by Barbut, 2011:59-61).

They include: taxpayers perceptions of the tax system and Revenue Authority; peer attitude/subjective; norms, taxpayers' understanding of the tax system /tax laws, motivation such as rewards and punishment such as penalties, cost of compliance, enforcement efforts such as audit; probability of detection; difference across - culture; perceived behavioral control; ethics/morality of the taxpayer and tax collector; equity of the tax systems; demographic factors such as sex, age, education and size of income and use of informants. Tax compliance has evolved into a major research topic in economic psychology. The issue has been approached from various viewpoints shedding light on different aspects of taxpayers' behavior. Attitudes were measured, prevailing social norms and lay theories explored, which people have in mind when fulfill their annual tax declarations (Murphy, 2004:56)



Source: OLA / 2006).

Figure 2.4: Tax - compliance cycle

2.1.6.1 Factors influencing taxpayers behavior

Deterrence:- Deterrence resulting from audits, the risk of detection and/or severity of punishment is often the first response that comes to mind when the general public is asked about how a revenue body promotes compliance, however, studies demonstrate conflicting evidence as to whether deterrence strategies have the desired behavioral influence on compliant and non-compliant taxpayers - some revenue bodies have reported that deterrence activities (large audit adjustments and monetary penalties) have actually emboldened taxpayers to behave more non-compliant in subsequent years. For the habitual non-complier, a deterrence strategy involving recurring audit activity may be required. The success of deterrence strategies is also linked to taxpayers `norms. Of particular interest is the finding that deterrence is more effective where strong social norms exist. Therefore, revenue bodies could consider the use of non-monetary penalties that attach a social cost response to non-compliance behavior (OECD, January 2012).

Research findings suggest that communication plays a critical role in how a deterrence strategy is perceived by taxpayers. It is not sufficient to simply deliver a message that non-compliant taxpayers are being detected; the public must also be reassured (truthfully) that most taxpayers are honest, as this promotes a strong social norm to remain compliant. Otherwise, deterrence communication can give the impression that non-compliance is the norm, thus running the risk of promoting further non-compliance. (OECD, January 2012).

Auditing: whether intentionally or unintentionally, not all taxpayers file timely returns or pay the correct amount of tax due. The tax auditing process involves using available information to identify taxpayers who may be noncompliant. That information includes such things as federal tax return data, information reports from financial institutions, employer wage statements, and other Minnesota tax return data. Then, depending on the type of tax and nature of the error the department is trying to detect, it uses a variety of audit techniques to find and correct errors in a taxpayer`s reported tax liability (OLA, 2006).

Norms: Norms, both personal and social, are considered to be the most important drivers of compliance. However, influencing norms is not an activity in which most revenue bodies have a great deal of experience. Instead, revenue bodies have tended to focus on short-term, output-

driven indicators of performance. They have historically been reluctant to engage in longer-term strategies designed to regularly assess (using outcome measures) and permanently influence taxpayer behavior. Most revenue bodies now recognize the need for a longer-term approach based on outcomes (compliance levels). Aside from attempting to influence norms, revenue bodies should consider incorporating normative messages in their dealings with taxpayers. For instance, messaging that others have acted in a certain manner (i.e. taxpayers have changed their behavior or have complied) can influence those that have yet to do so (OECD, January 2012)

It is also important for revenue bodies to be alert to, and promptly address, public misconceptions or inaccuracies that may impact social norms (hence taxpayer behavior). For example, if a media story suggests that taxpayers are being dealt with unfairly by the administration, or that tax evasion is more widespread than in reality, a response to the effect that this is a rare case, or is not true based on factual evidence, should contribute to public trust.(OECD,January 2012).

Opportunities: Revenue bodies have traditionally sought to limit the opportunities for non-compliance and have expended much less effort on making it easier for taxpayers to comply. For example third party reporting, withholding regimes and regular legislative amendments have been used and are seen as effective in minimizing non-compliant behavior. However, revenue bodies have tended to overlook the lazy non-complier the taxpayer who would have complied if only it had been easier. Further research could also be undertaken to better understand why taxpayers unintentionally non-comply, such as by making errors in completing forms. Suggestions for making it easier to comply and/or reducing unintentional non-compliance include the use of plain language in communications and simplifying forms and tax laws (OECD, January 2012).

Fairness: Research suggests that fairness, as exhibited by the revenue body or government, can play a role in taxpayer behavior. Three types of fairness are discussed in the note. Distributive fairness is the perception that the government acts as a good custodian and wise spender of tax revenues. Procedural fairness is the perception that the revenue body adheres to procedures that are fair in dealing with taxpayers. Retributive fairness is the perception that the revenue body is fair in the application of punishment when the rules are broken. Studies show that a lack of

perceived fairness is linked to a taxpayer's inclination (or justification) to not comply (OECD, January 2012)

Economic factors: The work undertaken indicates that there has been, in general, a lack of research to link economic factors to taxpayer compliance behavior. The general conclusion is that factors that promote economic growth also tend to promote tax compliance (OECD, January 2012)

Interactions: - Not to be overlooked from the research is the need to better understand how the various drivers of compliance behavior interact with each other. In particular, a revenue body must be cautious when using controlling and supportive approaches to influence behavior. For example, if a revenue body's approach is perceived as very controlling, it can cause taxpayers to feel distrusted. Research implies that when taxpayers feel distrusted, they may adopt the same attitude towards the revenue body, and this may reduce compliance. A revenue body should send a clear signal to the general public that non-compliant behavior is seen by society as wrong, by suggesting that society (and not just the revenue body) view this behavior as wrong existing personal norms are reinforced (OECD, January 2012).

Penalties: Researchers have found that taxpayers are more sensitive to the magnitude of the penalties than to the probability of detection when the probability is very low (i.e. 4% or less) this could have implication for countries that have moved to a self –assessment environment. Study by Witte and Woodbury (1983 as cited by Devos, 2005:181), observed that there was a significant relationship between the severity of the criminal sanction and compliance by one group of taxpayers (high-income self-employed individuals). Within each of the groups this study covered, legal sanctions were most effective for the higher class and the better educated (not the best). This study did indicate however, that the threat of guilt feeling was a greater deterrent to tax evasion than the threat or stigma of legal sanctions. This finding has been supported by similar work sanctions However, the positive effect of increase sanction levels on taxpayers' compliance has been found even where relatively low (and realistic) penalty levels are used. What is major concern thought has been that taxpayers' perceptions of the true penalty levels are higher than what the penalties actually are? This has tended to skew research findings. Other research evidence suggested that a tax system that combines both penalties and rewards is

more effective in maximizing compliance than a system that focuses solely on sanctions consequently; positive inducements for compliance may also have a key role to play and should be subject to further investigation (Devos, 2005:181).

Enforcement/detection: Studies of criminal behavior in general have found that the probability of apprehension is more important than the sanctions actually imposed Title and Login (1973 as cited in Devos, 2005:182). Alternatively another influence may just be the precision of information regarding the probability that punishment will be imposed. Consequently vague information value (Friedland, 1982). Overall the economic deterrence model proposes that increasing punishment by expanding criminal sanctions decreases non-compliance and this principle supports sentencing theory and the courts right to consider the maximum penalty for an offence in order to achieve general deterrence Jackson & Milliron (1986 as cited by Devos, 2005). However, this model in its purist form falls short and has been criticized for failing to consider analyses of attitudes, perceptions and moral judgment on tax behavior Lewis (1982 as cited by Devos, 2005). Consequently while economic deterrence models are relevant in shaping compliance behavior other “behavioral” factors have also been found to influence compliance decision (Mckerchar, 2003:12-50).

2.1.6.2 Nature and Scope of tax Compliance

According to Brown and Mazur (2005, as cited in Peter and Ebimobowei, 2013:110) explanation tax compliance as a multi-faceted measure and theoretically, it can be defined by considering three distinct types of compliance such as payment compliance (timely payment of all obligations), filing compliance (the timely filing of any required return), and reporting compliance (the accurate reporting of income and of tax liability).

2.1.6.3 Tax Gap

The tax gap estimate is an aggregate of estimates for the three primary types of noncompliance; - under reporting of tax liabilities on tax returns; (2) underpayment of taxes due from filed returns; and (3) non filing, which refers to the failure to file a required tax return altogether or on time. The tax gap includes unintentional errors as well as intentional evasion, such as intentionally underreporting income, intentionally over- reporting expenses, and engaging in abusive tax

shelters or frivolous tax schemes. It does not include legal tax avoidance activities (legally lowering tax liability), taxes due from illegally derived income, or various forms of fraud (White, 2012:3).

2.1.7 Required capabilities of auditors

According to OECD (2006), the required capabilities of auditors were generally identified by analyzing the activities required to perform particular audit tasks, and through practice and experience. They were often based on the notion that auditors are generalists, who may subsequently develop into specialists to meet organizational needs.

Tax auditors also play a critical role in the effectiveness of the SAS in many countries. In addition to their primary role of detecting and deterring non-compliance, tax auditors are often required to interpret complex tax laws and carry out extensive examinations of taxpayers' books and records. The numerous roles assigned to tax auditors require a recruitment and maintenance of competent tax auditors with technical knowledge, audit skills and tacit knowledge (Isa and pope, 2011:149). Moreover, the attitudes of tax auditors during the conduct of an audit may affect corporate taxpayers' compliance behavior. The way in which tax auditors interact with taxpayers during an audit may influence their compliance behavior in the future. For example, if taxpayers are treated with respect during the audit, taxpayers may have a stronger incentive to comply voluntarily.

2.1.7.2 Improving capabilities of Auditors

Responsibility and accountability for improving auditors, audit managers and audit directors commonly lies with the staff member in question and their direct manager and/or local management team. Responsibility and accountability appears to be influenced by the organizational structure. Human resource departments (where applicable) often have joint responsibility and/or are significant contributors to this process, together with tax auditing /training departments / OECD, 2006).The tax audit policy and strategy will establish the concept that tax audit can be a strong and effective tool in helping taxpayers understand their tax /customs obligations and can help taxpayer put systems in place that will generate the right tax at

the right time. Develop the skill of ERCA's employees: the tax audit policy and strategy will focus on the development of the professionalism, integrity and competence of ERCA's tax auditors to ensure the successful delivery of high quality tax audit.

Audit Competence: -Sound knowledge and competence; commands a premium. Similarly there is a demand for competence in auditing and accountancy, including adequate training and experience in all facets of an auditor's work. Further, nowadays the profession has also placed increasing emphasis on auditing and accounting professional education programs for auditors to ensure that they keep abreast of the latest ideas and techniques in auditing and accounting. The audit should be performed and the report prepared with due professional care by persons who have adequate training, experience and competence in auditing. Auditors are expected by third parties to have academic training in accounting, taxation, auditing, and other areas related to their profession. In addition they should receive further training, both formal and informal. Throughout their careers and they should pass the CPA examination, they should stay abreast of current developments in accounting, auditing and tax matters. In fact, an increasing number of jurisdictions now require CPAs to engage in continuing education to maintain their right to practice. The success of any profession may depend on three main points as below:

- A. Advanced Information;
- B. Continuing professional education; and
- C. Minimum levels of professional qualification.

For auditing profession, the three points are covered through auditing education, research in auditing, training of auditors, and admission to the profession after obtaining desired qualifications. (Mahdi, Ali, Reza, February, 2009, Vol. 4, No. 2:18)

2.1.8 Tax evasions and avoidance

According to Fuest and Riedel (2009:4), universally accepted definitions of tax avoidance and tax evasion do not exist. Tax authorities like HMRC define tax avoidance as an activity that a person or a business may undertake to reduce their tax in a way that runs counter to the spirit and the purpose of the law, without being strictly illegal. **Tax evasion**, in contrast, is usually defined as a violation of the law. Tax avoidance comprises activities which exploit loopholes in the tax

system but run counter to the purpose of the law whereas tax evasion describes illegal activities that involve elements of concealment.

Tax evasion is said to occur when individuals deliberately fail to comply with their tax obligations. The resulting tax revenue loss may cause serious damage to the proper functioning of the public sector. Threatening its capacity to finance its basic expenses (Alberto, 1999:52)

Tax audit can be effective if its design is such a way to eliminate the problems of tax evasion, tax avoidance and other tax irregularities. The Relevant Tax Authority at all levels should improve the standard of tax audit employed for effectiveness and efficiency, tax audit should aim at reducing the level of tax evasion and relevant Tax Authority should provide a policy that would allow the tax payers to cooperate during the period of tax audit. (MU'AZU SAIDU BADARA.Vol 3, NO 4, 2012:74)

2.1.8.1 Components of tax avoidance and evasion

Tax revenue losses due to tax avoidance and tax evasion can occur for a number of reasons. Existing estimates of these revenue losses distinguish between a domestic and an international component of tax avoidance and tax evasion. Component of tax evasion and avoidance would include, for instance, non-declared or under-reported income from work or domestic business activities. The international component of tax avoidance and evasion includes practices like transfer price manipulation by multinational firms or the holding of financial assets in offshore bank accounts by private individuals with the purpose of concealing capital income (Fuest& Riedel, 2009:4-5).

2.1.9 Technology and tax administration

According to Bird and Zolt (2008:793), Technology may improve the quantity and quality of information available to taxing authorities and their ability to use that information effectively. Technology may make tax administrations more effective by improving information flow, facilitating, coordination, and improving their allocation of resources. Technological changes may reduce taxpayer compliance costs by improving information and services to taxpayers (for example, software for maintaining books and records, and for calculating tax liabilities, or return

–free filing alternatives). Technology may reduce opportunities for corruption by reducing the face-to-face interaction between taxpayers and taxing authorities.

Over the last 40 years, reform efforts in tax administration in developing countries have generally centered on information technology (IT). The gains from adopting new technology, however have often failed to reach expectations. Successful reform efforts did not simply computerize antiquated processes but re-engineered the whole system. Radical improvement in tax administration requires changes in organization and methods, and modern IT greatly facilitates the needed transformation (Bird&Zolt, 2008:794-795).

2.1.9.1 Information Technology in the Ethiopian Tax Administration

ERCA has recognized that in modern tax administration, it is necessary to computerize the tax collection procedure. This produces benefits, which satisfy both the tax administration and the collection procedure. This produces benefits, which satisfy both the tax administration and the tax payer, on 24th February 2004, the Federal Inland Revenue Authority (legacy department of ERCA) announced the development of new software which would be used to collect information through the standard integrated Government Tax Administration System (SIGTAS). SIGTAS is an integrated package with all modules necessary to manage all taxes and licenses including a risk selectivity module, it provides management tools to track amounts assessed, collected, and outstanding amounts including aging of arrears (ERCA2010).

According to ERCA, (2010) the expected benefits from the proper implementation of SIGTAS are the followings:

- increased revenues and enhanced control
- Better service to taxpayers
- standardized practices throughout departments.
- Reduction of non-value adding activities (reduced paper based mgt)
- Good time management (reminders, remittances, e.t.c.)

- integrated management of all taxes (especially for audit)
- Manages all aspects of system administration including the tracking of late-files and late-payers, exemption period-automatically,
- Provides an overall view of all taxpayer liabilities and payments, eliminates manual calculation of penalties and interest,
- Helps ensure that data collected is valid, provides an easy-to use and allows assessment calculation from previous years as well as the current year.

The automated procedures incorporated in SIGTAS include: Registration, Assessment, Cashing, collection, Audit, Objections, and Information & administration procedures.

2.2 Empirical Studies

A number of empirical studies examine tax administration in both developed and developing countries tax audit program in particular, such as Saidu(N.D), Gemmell and Ratto (2012),Ebimobowei and peter (N.D), Mesfin (2008), and Getaneh (2011). All the above mentioned researchers conduct study on the tax audit. The review of the study presents as follows:

Study by Saidu (N.D) , on ‘ the Effect of Tax Audit on Tax Compliance in Nigeria’ (A Study of Bauchistate Board of Internal Revenue) the methodology employed for data collection is only primary source, which involved the use of questionnaires, and the main finding of the study including among other, the Relevant Tax Authority (RTA) employed tax audit towards achieving target revenue, that tax audit reduce the problems of tax evasion, that tax payers do not usually cooperated with tax audit personnel during the exercise. etc. and the recommends that are forwarded by the author are; the RTA at all levels should improve the standard of tax audit employed for effectiveness and efficiency, tax audit should aim at reducing the level of tax evasion and RTA should provide a policy that would allow the tax payers to cooperate during the period of tax audit.

Study by Ebimobowei and peter (N.D), was on ‘A Causality Analysis between Tax Audit and Tax compliance` in Nigeria data was collected from primary and secondary sources and the paper applied survey research design. The primary data for the study were generated through the administration of questionnaires and the secondary sources were from scholarly published and unpublished studies. The paper concludes that tax audit is one of the compliance strategies that can be used to achieve tax compliance in Nigeria because the average Nigerian is known for tax evasion and avoidance using all the available means of not paying the relevant tax to the government.

Study by Gemmell and Ratto (2012:33-58), On Behavioral responses to taxpayer audits: UK tax payers, the data used in the study was both primary and secondary data, using a sample of individual and business taxpayers. Comparing samples of randomly selected audited and non-audited UK taxpayers, the evidence confirms predictions that audited taxpayers found to be `compliant `found to be “noncompliant.” The results highlight the importance of testing separately the responses of taxpayers facing different opportunities and incentives to evade tax in order to avoid conflating their efferent effects, and to reveal both positive and negative indirect revenue effects from random auditing. They also found that behavioral responses both positive and negative by small and medium businesses were greater than those for personal taxpayers. The available to assess the possible impact of replacing the UK’s random audit program with more risk based audits are limited.

The study by Mesfin (2008), ‘tax audit practice an its significance in increasing revenue the case of Addis Ababa city administration’ the researcher used both primary and secondary sources of data to carry out his study, primary data collection methods questionnaires and personal interviews are the main that have been most usually applied in his study, the questionnaires were open – ended that needs further elaboration and suggestion by the respondent and close ended questions about tax audit application and its efficiency and effectiveness. Secondary data are also collected from source documents, published materials, annual reports, magazines, research papers and internet. The result shows that, in history the highest tax to GDP ratio in Ethiopia is 13% which is registered in 1996 EFY. Most of the country`s revenue is from non-tax sources such as grants. The main sources of tax for the government are indirect taxes, such as VAT,

TOT, Excise tax and other import export duties levied on foreign trade. This is because, it is easy to levy and collect taxes from indirect taxes as compared to direct taxes which are applied on income of businesses and individuals. The type of tax audit performed by tax auditors is only desk audit. So far, there is no field audit although the problem of tax evasion bothers revenue agencies at different levels. Tax audit practice, which has an impact on the performance of revenue generated from tax, is weak as seen in Addis Ababa city revenue agency.

The study by Getaneh (2011), was on Tax Audit Practice in Ethiopia Case of the Federal government to conduct the study the researcher adopted mixed /qualitative and quantitative /methods approaches, the researcher applied quantitative (survey) and qualitative (in-depth interview and document analysis), the results of the study indicated that, the performance of tax –revenue is relatively poor that accounts an average of 10.76 percent of GDP during the 2004/05 – 2008/09 fiscal years, Tax audit program remains undeveloped with an emphasis on comprehensive and desk audit with the exclusion of other audit methodologies. Regarding audit staff there is no competency assessment model, and less emphasis is given for continuous upgrading the capability and knowledge of staff resources once they have given and held a particular position.

There is a slight range of tax audit activities performed targeting aptly specific risks, which might result in less proportionate and measured response in terms of additional revenue collection and voluntary compliance improvement.

2.3 Conclusion to the literature review and knowledge gap

Therefore, Even if researches have been conducted on the area of tax audit practices in Ethiopia, the researcher believes that it is not still fully addressed and can be added more on the area. In addition to this as per the knowledge of the researcher no research has been done on the tax audit practice and its challenge in Large taxpayers office, hence the researcher believes that researches must be done in the branch office because the branch office serves investors whose annual turnover is above 27,000, 000.00 birr and the country collects large amount of tax revenue from this branch. Thus tax evasion and avoidance might be significantly high if it occurs, so the

research may indicate weak area that needs corrective measure and to improve the tax administration of the branch office.

2.4 Conceptual frame work

The conceptual frame work of the study focuses on the tax audit practice and its challenge. The study assesses Case selection for audit, risk based audit program, auditors' capabilities, and tax audit practice: types of tax audit, case selection techniques, risk based audit. Challenges of tax audit: auditors capacity, application of IT, clarity of tax laws, tax payers education.

Conceptual frame work of the study

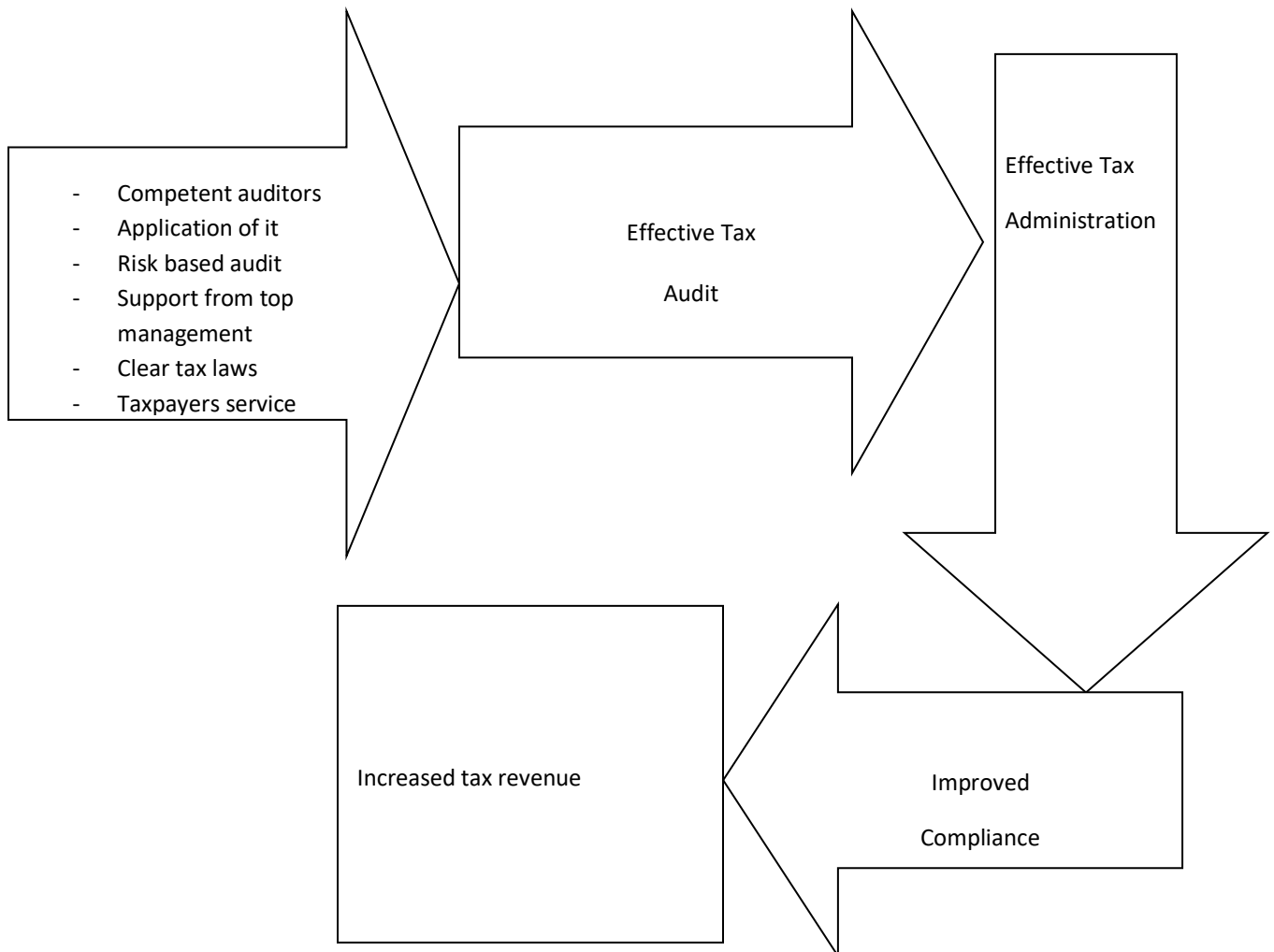


Figure 2.5: Conceptual Frame work of the study Source; Developed by the researcher own

CHAPTER THREE: RESEARCH DESIGN AND

METHODOLOGY

Research Methodology is the way that shows how the researchers systematically arrive at the solution of the research problems (Kothari, 2004:6). It is a scientific way of solving these problems. Accordingly, the research design of the study includes research approach, sample design, data source, data collection instruments, and data analysis and interpretation techniques as indicated below:

3.1 Research approach

There are two basic approaches to research, viz., quantitative approach and the qualitative approach. The former involves the generation of data in quantitative form which can be subjected to rigorous quantitative analysis in a formal and rigid fashion. Qualitative approach to research is concerned with subjective assessment of attitudes, opinions and behavior. Research in a situation is a function of researcher's insights and impressions. Such an approach to research generates results either in non-quantitative form or in the form which are not subjected to rigorous quantitative analysis (Kothari 2004:5).

In this study, both qualitative and quantitative approaches were used through questionnaire and interview.

3.2 Research Methods

Research methods are all those methods/techniques that are used to conduct a research (Kothari 2004:7). In this study, the researcher adopted survey methods, to attempt to capture attitude or patterns of past behavior. There are different tools available for the researcher to collect data these are questionnaires, observation, and interview.

The research type implemented for this study was descriptive method, because the researcher has no control of effect on the variables of the study. Where data obtained from the respondents were recorded and analyzed, and interpreted by conducting field survey. Thus, the researcher

described the audit practice and its challenge in the Ethiopian revenue and custom authority large tax- payers based on the data collected from the respondents using questioners and interview.

3.3 Sample Design

Conducting study on the complete enumeration of all population or census survey is difficult to cover due to different constraints especially if the inquiry is large (Kothari, 2004:31). Sample design is a definite plan for obtaining a sample from a given population. Therefore, the research population, sample size, the procedure that was used in selecting sample and collecting data is explained below.

3.3.1 Population Size

The population or universe under targeted for the study was the LTO branch registrant taxpayers and tax audit staffs at LTO branch. Out of the total 865 total LTO registrant taxpayers (LTO taxpayers` service database, 2008 E.C) are considered and 55 tax audit staff members which is organized by 1 process owner, 9 tax audit team coordinators and 14 senior auditors, 19 auditors and 12 junior auditors. Director of tax audit development and support directorate at head office level is also taken as a target area for the research.

3.3.2 Sample Frame

Sample frame is the source of list of the universe from which sample was drawn. It contains the names of all items of a universe (Kothari, 2004:4). Accordingly; the sample frame of the study bases the list of LTO branch taxpayers and tax audit staffs at LTO branch.

3.3.3 Sampling Techniques

An optimum sample is one which fulfills the requirements of efficiency, representativeness, reliability and flexibility. **Non-probability sampling** is that sampling procedure which does not afford any basis for estimating the probability that each item in the population has of being included in the sample whereas probability sampling is a procedure which affords equal chance of being included in the sample. In this study both probability and non-probability sampling techniques were employed. The non-probability /purposive sampling were used in deciding the

Addis Ababa residents' sample respondents from the LTO registrant taxpayers in the country, and audit staffs of LTO branch. The selection of non-probability sampling accounted for the difficulty to access/ contact the tax payers' because they are not located in one specific area, and the tax audits staff are small in size and taking survey response from all the tax audit staff was possible and manageable and increases the response rate because tax auditors go for field audit frequently so that the response rate could have been low. The simple random probability sampling was used to select from the residents of Addis Ababa taxpayers, in order to have an equal chance of being selected and included in the sample. Since taxpayers are segmented according to their annual turnover applying simple random sampling technique was appropriate.

3.3.4 Sample Size

According to Kothari (2004:56), in sampling analysis if the sample size ('n') is too small, it may not serve to achieve the objectives and if it is too large, we may incur huge cost and waste resources. As a general rule, one can say that the sample must be of an optimum size i.e., it should neither be excessively large nor too small. There are two alternative approaches for determining the size of the sample. The first approach is "to specify the precision of estimation desired and then to determine the sample size necessary to insure it" and the second approach "uses Bayesian statistics to weigh the cost of additional information against the expected value of the additional information. The first approach is capable of giving a mathematical solution, and as such is a frequently used technique of determining 'n'. The limitation of this technique is that it does not analyze the cost of gathering information Vis-à-vis the expected value of information. The second approach is theoretically optimal, but it is seldom used because of the difficulty involved in measuring the value of information.

To conduct study on personal judgment of the researcher being at 95% confidence level and a sampling error of 5%. According to Kothari (2004), the formula for finite population is as shown below.

$$n = \frac{z^2 PqN}{e^2}$$

Where N=population=865 n=sample size e=sample error at /5%/

z=the z value at confidence level of 95%=1.96 p=the proportion of defective 0.05 and q=1-p=0.95

$$n = \frac{(1.96)^2 (0.05) (0.95) (865)}{(0.05)^2}$$

$$n = \frac{(1.96)^2 (0.05) (0.95) (865)}{(0.05)^2} = 67$$

The total sample size of the tax payers was 67 residents of Addis Ababa LTO registrant taxpayers from the four sectors.

3.4 Source of Data and Data Type

To conduct a reliable and accurate research it is advisable to use primary and secondary data source (Kothari, 2004:95). In this study both the primary and secondary data were used.

3.4.1 Primary Data Source

Primary data was collected by using a sample survey/questioner and interview/, questioners were distributed to the branch office audit staffs and LTO taxpayers' resident of Addis Ababa. Tax audit process owner and tax audit team leaders were interviewed and tax payers were also interviewed so as to fill the gap of the questionnaires.

Questionnaires: were developed for the sample taxpayer respondents and tax audit staffs of LTO branch in a way that can achieve the objective of the study. The questionnaires were designed in structured open and close ended manner.

Interview: the interview questions were prepared to collect data on the overall audit activities. The interview questions were both structured and unstructured way that enable to extract the knowledge of the audit staff and taxpayers about the issue.

3.4.2 Secondary Data

The secondary sources of data were collected from various internet sources, proclamations, and magazines, journals, from ERCAs tax audit policies and ERCA's different published reports and unpublished sources, tax audit manual implementation evaluation report compiled by tax audit directorate at head office level and tax audit performance report compiled by LTO, branch.

3.5 Data Presentation

After collecting the primary and secondary data, it was edited, coded and tabulated and then it is presented using tables, figures, charts and graphs in a way that can easily be understood and suitable for analysis.

3.6 Data Analysis

The data collected using the above methods are organized, analyzed and interpreted in order to make it sensible. Computer applications of SPSS (16 version) software package in combination with excel spreadsheets were used as tools for the analysis purpose; the data were analyzed according to parts presented in questioner classification in the form of graphs, tables and descriptive form.

CHAPTER FOUR: - DATA ANALYSIS AND RESULTS

4.1 INTRODUCTION

The study was designed to assess tax audit practice and its challenges in Ethiopian revenue and custom authority large taxpayers' office. The results obtained based on the data collected from respondents are presented and discussed in this chapter. It shows general characteristic of the respondents, the response rate and findings of the study.

The questionnaires were distributed to Addis Ababa residents' large tax payers' office registrant taxpayers and LTO tax audit employees' respondents. The questioners distributed to the taxpayers were prepared in Amharic version so as to avoid language barriers and response biases minimize due to misunderstanding.

4.2 Demographic Data

In the following tables, and charts information related to sample respondents' both in response rate and demographic data such as gender, Age, educational background, work experience and current occupation of tax audit staffs and business sector of tax payers were presented and analyzed. To get this information, respondents were provided with structured question

Table 4.1: Demographic data

| | | Population Size | | | |
|---------------------------|--------|-----------------|--------------|-----------------------|-------------|
| | | Tax Payers (67) | | Tax audit staffs (55) | |
| | | Frequency | Percent | Frequency | Percent |
| Response rate (Returned) | | 58 | 86.56 | 45 | 81.8 |
| Gender | Male | 48 | 82.8 | 39 | 86.7 |
| | Female | 10 | 17.2 | 6 | 13.3 |
| Total | | 58 | 100 | 45 | 100 |
| <25 | | | | 12 | 26.7 |

| | | | | | |
|--------------------|--------------|-----------|------------|-----------|------------|
| Age | 25.35 | | | 29 | 64.4 |
| | 35-45 | | | 4 | 8.9 |
| | Total | | | 45 | 100 |
| | 30-40 | 14 | 24.1 | | |
| | 40-50 | 21 | 36.2 | | |
| | 50-60 | 17 | 29.3 | | |
| | >60 | 6 | 10.3 | | |
| | Total | 58 | 100 | | |
| Level of education | 12 and below | 16 | | | |
| | Certificate | 10 | | | |
| | Diploma | 13 | | | |
| | Degree | 16 | | 44 | 97.8 |
| | MBA/Msc | 3 | | 1 | 2.2 |
| | Total | 58 | | 45 | 100 |
| Experience | <2 years | | | 10 | 22.2 |
| | 2-4 yrs | | | 11 | 42.4 |
| | 4-6 yrs | | | 7 | 15.6 |
| | 6-8 yrs | | | 12 | 26.7 |
| | 8-10 yrs | | | 1 | 2.2 |
| | >10 yrs | | | 4 | 8.9 |
| | Total | | | 45 | 100 |

Source: field Survey Result 2016

The above table 4.1 shows the population size of registrant of tax payers and tax audit staffs of response rate, gender, age, level of education and experience of tax audit staffs. These points are discussed below:

The response rate;- 67 questionnaires distributed to LTO registrant taxpayers and 58 were returned representing 86.56 percent and from 55 questionnaires distributed to the tax audit staffs, 45 questionnaires were returned and represent 81.8 percent. In addition structured interviews were held with the tax audit process owner, tax audit team leaders and director of tax audit development and support directorate and unstructured interview with LTO tax payers.

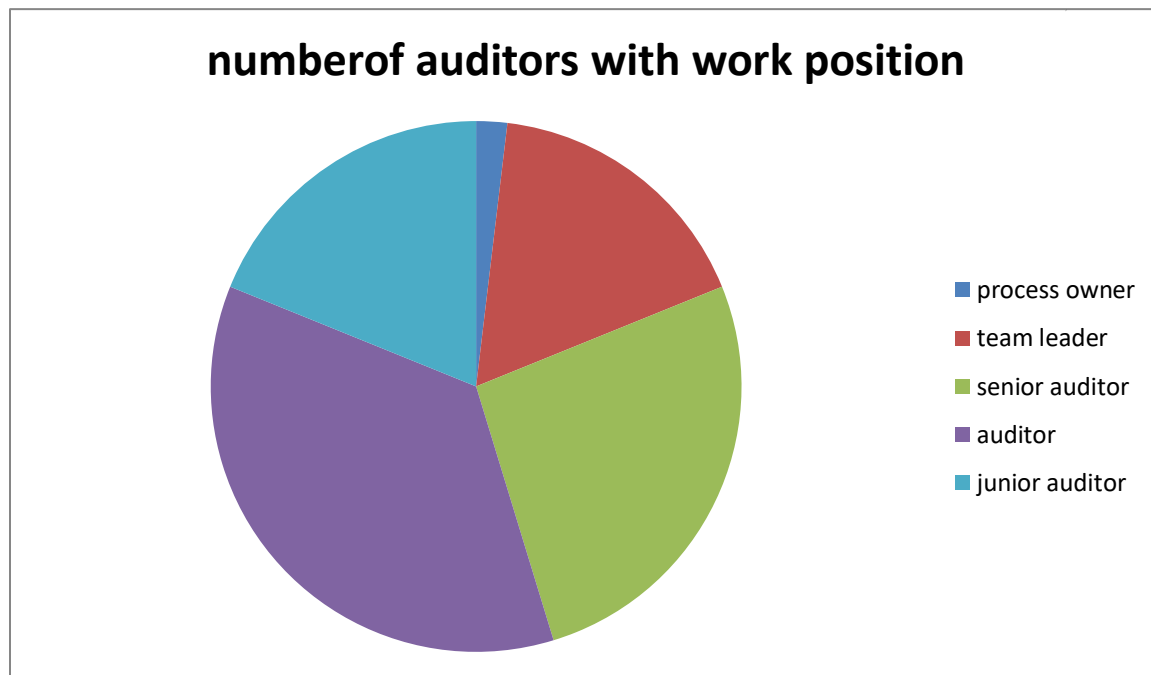
Gender: out of the 58 Taxpayers respondents are 48(82.8%) male and the remaining 10(17.2%) respondents are female taxpayers. And 39(86.7%) of the tax audit staff respondents are male and 6(13.3%) are female, the number of male respondents are much higher than female respondents. ERCA'S record about corruption shows that female workers are less engaged in corruption practices(ERCA'S Newsletter, May, 2015).

Age: out of the 45 tax audit staff respondents are 12 (26.7%) less than 25 Years old and 29 (64.4%) respondents age ranges from 25-35 years old and the remaining 4(8.9%) respondents age ranges from 35-45 years and the age of tax payers` 14(24.1%) respondents age is 30-40 years old, 21(36.2%) taxpayers are 40-50 years old, 17(29.3%) are 50-60 years and 6(10.3%) are above 60 years old. In the summary majority of the tax audit staffs` age lie between 25 and 35 years and they are young and this can be an opportunity to the tax authority if managed properly.

Level of Education:- out of 58 tax payer respondents are 16(27.6%) grade 12 and below, 10(17.2%) respondents are certificate holder, 13(22.4%) diploma, 16(27.6%) are BA/Bsc degree and 3(5.2%) are MA/MSc degree and out of 45 tax audit respondents have 44(97.8%) B.A Degree, 1(2.2%) respondents has MA or MSc Degree in different field of study. From the interview held with the team leaders the researcher realized that there are 4 auditors who are attending their masters` education currently. All the auditors/officials have good educational background and it has positive implication in improving the tax administration. Educational background has both positive and negative impact on the compliance level of tax payers.

Work experience: -in the current position of tax auditors 10 (22.2%) have less than two years, 11(24.4%) respondents have 2-4 years, 7(15.6%) have 4-6years, 12(26.7%) have 8-10 years and the remaining 4(8.9%) have more than 10 years' work experience .well experienced tax auditors/officials can tackle tax avoidance and evasions committed by non-compliant taxpayers in a better way.

Tax audit staff respondents` position/current job occupation



Source; field survey result 2016

Figure 4.1 tax audit staff respondents' position /current job occupation

The above figure depicts the respondents' current position /occupation distribution: there are 10(22.2%) junior auditors, 12(26.7%) are auditors, 13(28.9%) are senior auditors and 9(20%) are team coordinators and the remaining 1(2.2%) is process owner.

Table 4.2: Taxpayers` respondents` based on business sectors

| Business type | Frequency | Percent |
|------------------------------|-----------|---------|
| manufacturing | 16 | 27.6 |
| Construction and real estate | 15 | 25.9 |
| merchandise | 15 | 25.9 |
| service | 12 | 20.7 |
| Total | 58 | 100.0 |

Source: field survey result 2016

Data obtained from taxpayers respondent reveal that 15(27.6%) are from the manufacturing sector, 15(25.9%) taxpayers from the construction and real estate, 15(25.9%) from the merchandising sector and 12(20.7%) taxpayers respondents from the services sector.

4.2.1 Required capabilities of tax audit work force

Tax auditors detect, in their daily work, weaknesses in law that are being exploited by taxpayers, and this information is normally escalated to the tax administration's policy and legislation program so as to address the loopholes through amending the tax legislation. If auditors observe recurring patterns of avoidance, this may indicate, for example, that the penalty provisions are inadequate and require amendment to provide sufficient deterrence. Tax audit activities will not achieve the desired objectives without competent staff. The tax administration should aim at matching its staff audit skills with those of the private sector and embrace developments in the audit profession. Taxpayers will quickly realize when tax administration does not possess skilled auditors and enough manpower to detect non-compliance, a situation that should not be allowed to occur. All efforts should therefore be made by the tax administration to develop and manage a cadre of competent tax auditors (East AFRITAC, n.d)

Trained skillful human resource development is mandatory for the successful delivery of tax audit programs. Questions related with the auditors competence and capabilities were raised to tax auditor/officials.

Questions that have effect on auditors` competence in audit planning and execution process

1. Auditors prepare organized tax audit plan that can help them to identify risk areas of taxpayers` tax return which specifically bases the taxpayer`s business type?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 10 | 30 | 5 | 0 | 0 |
| percentage | percentage | percentage | percentage | percentage |
| 22.22% | 66.67% | 11.11% | 0 | 0 |

In the above table it is tried to analyze the responses given by tax auditors in relation to the auditors` competence and capacity during the process of audit execution. Besides this fact 22.22% of respondents strongly disagree with the presence of organized tax audit plan that can enable auditors to focus on risk areas of audit and specialize on different business sectors. Others respond on disagree and neutral with 66.67% and 11.11% respectively. In the interview made with the process owner and team leaders they accepted that there is no organized tax audit plan which should comprise ratio, trend and risk analysis which specifically considers the nature of the business that the taxpayer is engaged. But they said that though there is no organized tax audit plan, audit teams tried to informally identify the risk areas without organized written document.

Based on the supervision compiled by tax audit development and support directorate/head office level/, on tax audit performance of the branch, it is commented that though the necessity of preparing tax audit plan which bases the nature of business that the taxpayer is engaged is clearly indicated in the tax audit manual of the authority, no organized tax audit plan has been prepared in this large branch office till the supervision month (i.e. Feb/2017). From this summarized responses and data it is possible to say that there is no organized tax audit plan that can enable auditors to focus on risk areas and to perform the tax audit effectively and efficiently.

2. The assignment of audit cases to auditors considers their seniority and being familiar with the nature of the business?

| | | | | |
|------------|------------|------------|------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 9 | 5 | 0 | 10 | 21 |
| percentage | percentage | percentage | percentage | percentage |
| 20% | 11.11% | 0 | 22.22 % | 46.67% |

In relation to the assigning of auditors for an audit case, it is mandatory to group 2 to 3 auditors depends on the complexity of the case ,which comprises senior and junior auditors so as to enhance the experience sharing among auditors, to finalize the case with in the standard date and to reduce the case of corruption (ERCA`S directive in relation to audit case assignment and tax audit manual).Based on the response given by auditors 20% strongly disagree,11.11% disagree and 22.22% strongly agree and 46.67% agree that the assignment of audit cases has been made by considering auditors` seniority and their being familiar with the case. Based on the interview made with process owner and team leaders, it is responded that as much as possible it is tried to direct audit cases to auditors by considering their seniority (i.e. when the nature of the business to be audited is complex and huge ,like Manufacturing, Construction, Mining and others) senior auditors are assigned for the case. But businesses which are not complex are directed to auditors and juniors. Regarding auditors being familiar with the case, it is considered as one critical point

to direct cases but constraints like turnover of experienced auditors, promotion of internal senior employees with no audit experience and transferring of auditors from small scale taxpayers (sub – cities)centers to the branch make the audit case to be handled with inexperienced auditors. As a result the quality and quantity of tax audit assessment is negatively affected by working with less experienced senior auditors.

3. There is adequate team leaders` follow up so as to support and control auditors` work execution?

| | | | | |
|------------|------------|------------|------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 15 | 21 | 0 | 0 | 9 |
| percentage | percentage | percentage | percentage | percentage |
| 33.33% | 46.67% | 0 | 0 | 20% |

Concerning the adequacy of follow up of team leaders for the audit case, it is responded that 33.33% strongly disagree, 46.67% disagree and 20% agree on the question raised. Regarding this the process owner and team leaders gave an idea that the level of follow up of an audit case is not consistent among teams for the reason that there is no standardized follow up procedure in the branch, the capacity of team leaders varies greatly and team leaders are too busy in managing several meetings like compiling audit performance reports ,responding different frequent requests from top level management at head office level and there is also fear from team leaders that there is unrealistic thinking of the management that the practice of corruption is high if team leaders go to field work frequently .From the responses given it is clear that there is no adequate and standardized teams follow up procedure that can enable to enhance auditors` competency and controlling of the audit effectiveness and efficiency.

4. There is regular discussion forum which is held by tax audit teams to simplify complex tax audit issues?

| | | | | |
|------------|------------|------------|------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 8 | 25 | 0 | 4 | 8 |
| percentage | percentage | percentage | percentage | percentage |
| 17.78% | 55.56 | 0 | 8.89% | 17.78% |

Responses given in relation to the regular discussion among tax audit teams to solve complex audit cases are 17.78% strongly disagree, 55.56% disagree, 8.89% strongly agree and 17.78% agree. Both process owner and team leaders respond on this issue in the form of interview that there is group discussion among teams together with process owner but it is not done regularly. The major reasons for not making it permanent is almost all audit cases are executed in field work so teams can't meet frequently and teams are not willing and ready to come up with complex issues permanently. In addition they responded that 1 to 5 discussion which is primarily implemented by tigray regional government as a modern management tool so as to share experience among employees is only held by the tax audit process once in a week for the reason that almost all auditors are in field work though the manual for 1 to 5 requested to make discussion in every day. Another gap with 1 to 5 discussion in the branch is team discussions concentrates on tax audit performance progresses and attendance of employees but doesn't focus on complex issues faced in the process of audit execution in relation to tax laws, regulations, directives and international accounting and auditing practices. Therefore by underlying the responses given regular discussion on complex audit issues is not made permanently in the branch and this has material effect on the competence of auditors and quality of tax audit assessments.

5. When tax laws, regulations and directives are not clear/not easily available, it is briefed and availed by the concerned body so as to use it as an input for an effective tax audit assessment?

| | | | | |
|------------|------------|------------|------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 11 | 22 | 0 | 0 | 12 |
| percentage | percentage | percentage | percentage | Percentage |
| 24.44% | 48.89% | 0 | 0 | 26.67% |

For the question raised on the issue of getting response from the concerned body for unclear laws and directives that are not available in the branch is 24.44% strongly disagree, 48.89% disagree and 26.67% agree .For this issue tax audit process owner and teams replied that whenever there is a case of unclear laws and unavailability of directives specifically those issued before many years .Letter is written to law directorate to give adequate explanation on laws which creates confusion and to send the copy of directives not available in the branch. As per their response the problem on this issue is that it takes more than a month and above to get the required response from the law department. Even two different explanations/clarifications of laws are given from the directorate on one issue by different officials. In addition they raised that though the authority tries to attach laws and directives in website only some directives are attached and the web is too slow for data retrieval. Therefore it can be said that the law department is not supporting the audit process both in terms of timing and quality and this has a vital impact on auditors' competence and fair tax assessment.

Questions related with trainings and educational opportunities which influence auditors` competence

6. Continuous and relevant trainings are provided to tax auditors?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 14 | 24 | 0 | 0 | 7 |
| percentage | percentage | percentage | percentage | percentage |
| 31.11% | 53.33% | 0 | 0 | 15.56% |

Respondents were asked to scale the provision of continuous and relevant training in the branch. Based on this 31.11% strongly disagree, disagree 53.33% and 15.56% agree on the issue. From the interview held with the process owner and teams, they gave information that though training assessment need which is prepared and filled based on auditors` request is transferred at the beginning of every budget year, trainings which are not directly related with the need assessment are given and provided in a rare situation as per the willingness and readiness of tax audit directorate at head office level. They reflected that trainings like audit techniques and analysis ,sector based accounting and auditing practices and computerized accounting and auditing trainings and others are requested to be provided repeatedly but out of this it is only the manufacturing and construction sector based training is provided by the tax audit development and support directorate officials for trainers of trainees. In addition trainers assigned for the training don`t have adequate knowledge and experience on the issues reflected on the training. Furthermore it is indicated that many trainings are given in unexpected time without considering the issue of relevancy.

Taking into account the responses given, it is possible to reflect that trainings that can increase auditors` proficiency and competence are not given in the branch in a serious scheduled manner, trainings are not relevant and advanced trainings as per the need assessment are not provided.

7. Top level management of the authority facilitates auditors to be certified in ACCA, CPA and the like?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | Frequency |
| 27 | 18 | 0 | 0 | 0 |
| percentage | percentage | percentage | percentage | percentage |
| 60% | 40% | 0 | 0 | 0 |

Question raised on the issue of facilitating auditors to be certified on ACCA, CPA and other internationally accredited professional associations by the top level management of the authority, it is responded that 60% as strongly disagree and 40% as disagree. Process owners and team leaders responded that many experienced auditors are resigning from the branch and employed to different audit firms and huge private organizations for the reason that there is no encouragement and support from the top level management in facilitating auditors to have international educational access and to be highly competent in the profession.

8. Team leaders and senior auditors are committed, capable and transparent to support juniors on job trainings and in audit execution process?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 8 | 19 | 0 | 0 | 18 |
| percentage | percentage | percentage | percentage | percentage |
| 17.78% | 42.22% | 0 | 0 | 40% |

To scale the issue of team leaders and senior auditors being committed, capable and transparent in audit process, 17.78%, 42.22% and 40% are responded as strongly disagree, disagree and agree respectively. Two major points are reflected by process owner and team leaders on this issue. These are lack of adequate work experience of team leaders and process owner in auditing large taxpayers office and some senior auditors don't cooperate junior auditors to share their experience at the required level for two probable reasons: participating easily in corruption act and not being positive to share their work experience. Within the previous 3 years / from 2006 to 2008 E.C. the management has taken action on 10 employees to leave the authority as per code of conduct of employees' article.37.

Questions related with Auditors` salary earnings, benefits and the condition of the working environment which have major effect on their motivation to be competent: -

9. Salaries and different benefits earned by auditors are adequate compared to the payment effected by other sectors in the market?

| Strongly disagree | disagree | neutral | Strongly agree | agree |
|-------------------|------------|------------|----------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 0 | 5 | 0 | 16 | 24 |
| percentage | percentage | percentage | percentage | percentage |
| 0 | 11.11% | 0 | 35.56% | 53.33% |

Responses given for the question that adequate salary and different benefits are earned by auditors compared to other sectors in the market are 11.11% disagree, 35.56% strongly agree and 53.33% agree. For this question the process owner and teams informed that the salary scale and benefits are materially changed specifically from sep/2016, as an example the salary of process owner and team leaders were 8,730 birr and 7,215birr respectively and transport monthly allowance of birr 83 till august/2016 .But starting from sep/2016 it is increased by more than

double and became 20,760 and 18,345 for the process owner and team leader respectively. In addition rent allowance and transport allowance are paid to auditors with birr 1,300 and 600 birr respectively in every month. The process owner and teams indicated that though the salary and benefits are better than other sectors in the market, big private companies like those taxpayers in large taxpayers' office are attracting auditors by setting big salaries and different benefits which are not provided by the authority and for this reason some experienced auditors are still resigning after the increment of the salary. Furthermore they reflected that the authority made salary and other benefits increment after more than 5 years for this reason many experienced competent auditors resigned from the authority. From the responses provided it is possible to state that though the salary and other benefits increment is better than other sectors and enhances the work motivation of auditors to be competent, salary and different benefits set by big companies to attract experienced auditors is still one major risk area of the branch's audit performance.

10. Employees whose work performance is better than others are recognized and rewarded by the management on regular basis?

| Strongly disagree | disagree | neutral | Strongly agree | agree |
|-------------------|------------|------------|----------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 14 | 26 | 5 | 0 | 0 |
| percentage | percentage | percentage | percentage | percentage |
| 31.11% | 57.78% | 11.11% | 0 | 0 |

Question to respond on recognizing and rewarding employees with high performance was raised, based on this 31.11% of respondents strongly disagree, 57.78% disagree and 11.11% are neutral. The process owner and teams explained that the major problem of the authority is identifying high achievers and recognizing employees that enable them to be highly motivated and being competent. They also reflected that this trend was practiced in the branch before many years.

11. The work environment is convenient for auditors and helps them to complete the audit task without negative influence from different parties?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 20 | 19 | 0 | 0 | 6 |
| percentage | percentage | percentage | percentage | percentage |
| 44.44% | 42.22% | 0 | 0 | 13.33% |

Out of the respondents 44.44% strongly disagree, 42.22% disagree and 13.33% agree that the work environment is free from negative influence. For this issue the process owner and team leaders indicated that auditors are doing their job with big challenges from taxpayers because many taxpayers provoke auditors in different ways when additional tax is assessed by auditors. In addition many auditors have argument on the employees' code of conduct of the authority, article/37 which states that the director of the authority has full right to fire employees from their job whenever there is doubt that practice of corruption has been done without critical evidence. Based on these responses it is possible to figure out that there is a major problem in the area of availing suitable work environment that can inspire employees' motivation.

Questions which concerns auditors efficiency and effectiveness in audit cases assessed by the branch

12. Auditors are assessing audit cases both in number and in amount as per the audit plan and standard?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 9 | 23 | 3 | 0 | 10 |
| percentage | percentage | percentage | percentage | percentage |
| 20% | 51.11% | 6.67% | 0 | 22.22% |

Responses for the assessment of audit cases both in number and additional tax as per tax audit plan and standard is: 20% strongly disagree, 51.11% disagree, 6.67% neutral and 22.22 agree on the question.

The following tabular data which indicates the effectiveness and efficiency of auditors in the branch is provided by the tax audit process from the annual audit performance report.

Three years tax audit performance report of the branch from 2006 – 2008 E.C

| Ethiopian budget year | Number of audit cases planned in a year | Number of audit cases actually audited | difference | Expected additional tax assessment in birr | Actual additional tax assessment in birr | difference | Number of audit cases transferred to appeal committee | Number of audit cases revised by tax appeal committee in favor of tax auditors | difference |
|-----------------------|---|--|------------|--|--|----------------|---|--|------------|
| 2006 | 135 | 67 | (68) | 2.8 billion | 1.95 billion | (0.85 billion) | 31 | 14 | (17) |
| 2007 | 135 | 80 | (55) | 3.4 billion | 2.69 billion | (0.71 billion) | 24 | 17 | (7) |
| 2008 | 135 | 99 | (36) | 4.2 billion | 3 billion | (1.2 billion) | 29 | 21 | (8) |

From the above table it is understandable that numbers of auditors are the same in all years and it is for this reason that the audit plan for the number of audit cases remains constant. And it is calculated by considering the average annual working days of 240 days which is arrived after deduction of days spent without work due to rest days, public days, holidays, training days and other considerations. Based on this the standard of audit cases to be assessed annually by two auditors is 6, which is computed by dividing the annual working days by the standard number of days which takes to audit large taxpayers' file (i.e. 40 days, by two auditors and 4 tax periods for a single case), which is stated in the tax audit manual of the authority.

But when we see the actual number of audit cases which are assessed in each year, there is under performance of files by 50.37%, 40.74 and 26.67% with respect to the planned number in each

year respectively from 2006 to 2008 E.C. From this it is possible to understand that though the audit coverage is improving from year to year auditors can't achieve the planned number with a material difference. In relation to this concept, team leaders responded that the audit coverage increases for the reason that desk audit has been made for 2007 partial year and 2008 tax period on some tax payers which are assumed to be less risky. Regarding standard number of days to finalize the audit of a single case, they commented that there should be specific standard which considers the type of business that the taxpayer is engaged and there should not be a flat standard for all sectors.

At the same time the additionally expected amount of tax is above the actually assessed figure. The interviewee suggested on this issue that the amount is reduced for two major reasons. These are conducting the audit with inexperienced staff and auditing taxpayers' repeatedly.

13. Major audit cases which are assessed by tax auditors are accepted by taxpayers without any complain?

| Strongly disagree | disagree | neutral | Strongly agree | agree |
|-------------------|------------|------------|----------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 4 | 19 | 0 | 3 | 19 |
| percentage | percentage | percentage | percentage | percentage |
| 8.89% | 42.22% | 0 | 6.67% | 42.22 |

Responses for the acceptance of tax audit assessment by the taxpayer without appealing are 8.89% strongly disagree, 42.22% disagree, 6.67% strongly agree and 42.22% agree on the question.

The other point that can be grasped from the three years tax audit performance data, there are still audit cases which are appealed by taxpayers in all years though the number is getting lower from year to year as compared to the actual number of audit cases which are audited in each

year. When we see the percentage of appeals to number of audit cases assessed it is 46.27%, 30% and 29.29% respectively from 2006 to 2008 E.C. For the number of appeals it is suggested by tax audit support and development directorate /head office level/ since large taxpayers` office has a big responsibility to cover the country`s tax collection, the rate of appealing should be lower than 10%. Therefore this case can be compiled by saying that though there is a reduction of appeal rate from year to year ,there is still a material appeal number which has a vital effect on taxpayers` compliance and tax revenue collection of the branch as well the authority.

When we see the number of cases revised by the tax appeal committee in favor of the branch office it is improving from year to year even though there are revised audit cases decided to taxpayers by the appeal committee and this has a negative impact for the authority in terms of cost and time due to being inefficient and ineffective in tax audit performance.

From the above responses and tabular data it is possible to note that auditors` efficiency and effectiveness is still under question in the branch under study.

14. When taxpayers do not accept the audit assessment and proceed to appeal, assessments are revised by the appeal committee in favor of the branch rather than taxpayers at major level?

| Strongly disagree | disagree | neutral | Strongly agree | agree |
|-------------------|------------|------------|----------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 5 | 22 | 0 | 4 | 14 |
| percentage | percentage | percentage | percentage | percentage |
| 11.11% | 48.89% | 0 | 8.89% | 31.11% |

For the question which is raised on the revised decision of tax appeal committee in favor of the branch it is responded as 11.11% strongly disagree, 48.89% disagree, 8.89% strongly agree and 31.11% agree.

When we see the number of cases revised by the tax appeal committee in favor of the branch office it is improving from year to year even though there are revised audit cases decided to

taxpayers by the appeal committee and this has a negative impact for the authority in terms of cost and time due to being inefficient and ineffective in tax audit performance. From the above responses and tabular data it is possible to note that auditors` efficiency and effectiveness is still under question in the branch under study.

4.2.2 The function of tax audit in improving the compliance level of taxpayers

According to ERCA (2010), Tax Audit Policy and Strategy had been prepared to support the successful delivery of the ERCA Strategic plan. Tax audit is one of the components of the compliance risk management strategy that is designed to support the delivery of the voluntary compliance concept. Conducting tax audit involves significant costs to ERCA as well as to achieve maximal taxpayer compliance. This is best achieved by the development of a risk based audit program that rewards taxpayer compliance with a light touch approach and openly demonstrates that valuable taxpayer resource is being deployed against the non-compliant, the tax audit policy and strategy is designed to deliver the aspiration of helping customers pay the right tax at the right time and with the minimal administrative and compliance cost to both ERCA and customers.

According to ERCA (2010), the key guiding principles of the tax audit policy and strategy of ERCA are:

- **Fair and modern tax and customs administration:** the tax audit policy and strategy will establish a robust and transparent risk based approach to ensure a consistency of approach and treatment to a particular taxpayer segment by taking into consideration one size does not fit all approach.
- **Effective revenue collection:** the tax audit policy and strategy will introduce a broader range of tax audit activities that are more targeted and appropriate to specific risks, which will result in more proportionate and measured responses.
- **Promote voluntary compliance:** the tax audit policy and strategy will establish the concept that tax audit can be a strong and effective tool in helping taxpayers understand their tax/customs obligations and can help taxpayer put systems in place that will generate the right tax at the right time. Develop the skill of ERCA`s employees: the tax

audit policy and strategy will focus on the development of the professionalism, integrity and competence of ERCA's tax auditors to ensure the successful delivery of high quality tax audit.

Reducing the revenue losses arising from non-compliance with tax laws is a critical objective of all revenue bodies. Non-compliant taxpayers use different methods to understate their tax liabilities such as (OECD, 2006):

- For large businesses, deliberately concealed income streams generally accompanied by fabricated books and records.
- Unreported rental income of real property owners.
- Casual earnings derived from the provision of personal services.
- Use of ghost employees to conceal income of proprietors and etc.

Given the numbers and the diversity of non-compliance practices revenue bodies are implementing an effective strategy to reduce the overall incidence of this noncompliance is a challenging undertaking for all revenue bodies and one that is likely to require a sustained effort over a fair period of time (OECD, 2006).

There are different technique to increase the compliance level of tax payers such as educating tax payers about their social responsibilities, fairness/based on ability-to pay/and equity of a tax system also have an impact on compliance level, magnitude of penalties and enforcement/detection by audit.

Questions related with audit`s contribution to improve compliance level of taxpayers in the branch:-

1. The Audit coverage in the branch has a vital contribution soas to increase the compliance of taxpayers?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 8 | 17 | 0 | 7 | 13 |
| percentage | percentage | percentage | percentage | percentage |
| 17.78% | 37.78% | 0 | 15.55% | 28.89% |

As shown in the above table, the survey result collected from the tax auditors/officials reveals 8(17.78%) strongly disagree, 17(37.78%) disagree, 7(15.55%) strongly agree and 13(28.89) agree on the question raised.

Interviewees responded on this issue that though audit has importance to enhance compliance level of taxpayers in the branch, the audit coverage of the branch is small compared to the number of total taxpayers in the branch. For this thing to happen they highlighted that among types of audits (i.e. Comprehensive, desk, issue audit/limited scope audit, field audit, refund audit and compliance audit (for special taxpayer i.e. AEO)which are listed in the tax audit manual of the authority, it is only comprehensive audit which is practiced by the tax audit process of the branch office and this type of audit needs more time to conduct detail examination of taxpayers` financial documents and leads to cover limited number of taxpayers .

2. The audit selection program of the branch has significant effect to increase compliance?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 21 | 15 | 6 | 0 | 3 |
| percentage | percentage | percentage | percentage | percentage |
| 46.67% | 33.33% | 13.33 | 0 | 6.67% |

The other question asked was about the significance of the audit selection program for compliance. As shown in the above table, the survey result collected from the tax auditors/officials reveals 21(46.67%) strongly disagree, 15(33.33%) disagree, 6(13.33) neutral and 3(6.67%) agrees on the question.

To supplement the question an interview was held with process owner and tax audit team leaders about how cases are selected for audit. The outcome of the interview reveals that taxpayers selection for audit is conducted by assessment and audit divisions participated by tax audit team leaders and the screening committee. The screening team assesses declarations of all taxpayers and select for audit (based on accuracy in computations, declarations of prior years, type , reasonableness of expenses, margin of prior years, matters raised in prior assessment, conducting research on taxpayer (taxpayer's operations, possible compliance issues, specific legislations applicable to the taxpayer) and other relevant considerations).It is also reflected that though the selection of taxpayers for audit is done through manual system, problems like selecting taxpayers repeatedly ,limited number of criterias are utilized for selecting taxpayers for audit, human errors of capturing data and omitting taxpayers with high risk without selecting them for audit due to several reasons can be mentioned as major limitations for enhancement of compliant taxpayers.

3. Taxpayers get adequate awareness from the tax assessment?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 2 | 6 | 0 | 12 | 25 |
| percentage | percentage | percentage | percentage | percentage |
| 4.44% | 13.33% | 0 | 26.67% | 55.55% |

Regarding the adequacy of tax awareness during tax assessment, 2(4.44%) responded as strongly disagree, 6(13.33%) disagree, 12(26.67%) strongly disagree and the remaining 25(55.55%) responded with agreement as shown in the above table.

In the interview made with process owner and team leaders, it is responded that before completion of the audit, auditors and taxpayers' accountants make reconciliation on the audit findings to provide adequate room for the taxpayer to justify issues raised by auditors. When they finished the reconciliation and reached on consensus on first draft audit, official audit exit conference is held in the presence of tax audit team leader, tax auditors, taxpayer's General Manager, Finance head of the client and optionally tax audit process owner (i.e. when the taxpayer is a multinational company, the case is complex, when the additional tax assessed by the audit is greater than birr 5,000,000 (five million birr), approved loss of birr 5,000,000 (five million birr) and above, refund of birr 5,000,000 (five million birr) and above is approved by the audit).Therefore the very purpose of arranging tax audit conference before the release of tax notification is ,assessing fair tax by further justification to be made by the taxpayer on audit findings and enhancing taxpayers` awareness on the tax laws, regulations, directives, accounting and auditing principles. In connection to this point it is additionally reflected that till 2008 E.C, there is taxpayers` tax awareness improvement feedback sheet prepared by the branch and to be filled by the taxpayer at the end of the audit. The content of the form and summary of the data is presented below:-

Taxpayers` feedback on improvement of tax awareness by tax audit in 2008 E.C.

| No | Questions raised in relation to compliance improvement | No. Of satisfied taxpayers | No. Of dissatisfied taxpayers |
|----|--|----------------------------|-------------------------------|
| 1 | Auditors` motivation to enhance tax awareness | 40 | 59 |
| 2 | Auditor`s capacity to explain issues | 51 | 48 |
| 3 | Auditors` knowledge and capacity on tax laws | 52 | 47 |
| 4 | Auditors` behavior and attitudes on taxpayers | 61 | 38 |

From the above table provided by the tax audit process of the branch, in all elements of tax awareness improvement measurements more than 45% on average is filled as dissatisfaction by the taxpayer. It is also informed that no action plan and implementation follow up schedule have been made by the management so as to improve taxpayers` tax awareness in relation to the audit conducted by the branch.

4. Auditors primary objective is assessing additional tax from the taxpayer rather than enhancing taxpayers` awareness?

| | | | | |
|-------------------|------------|------------|----------------|------------|
| Strongly disagree | disagree | neutral | Strongly agree | agree |
| frequency | frequency | frequency | frequency | frequency |
| 0 | 9 | 0 | 15 | 21 |
| percentage | percentage | percentage | percentage | percentage |
| 0% | 20% | 0 | 33.33% | 46.67% |

As indicated in the above table respondents of 9(20%) disagrees, 15(33.33%) strongly agrees and 21(46.67%) agrees that the ultimate goal of tax audit is assessing additional tax more than enhancing tax compliance. According to the outcomes of the interviews with the tax audit process owner the main purposes of auditing is to create compliant taxpayers, its deterrent effect on non-compliant tax payers, to increase awareness in the tax payers and to penalize taxpayers who violate the tax laws.

Based on the branch`s case since tax audit teams are expected to assess additional tax in each year and they are evaluated on this, auditors main concern in auditing is assessing more additional tax revenue so as to achieve their plan. As a result they don`t give more concern for the compliance of the taxpayer and some tax assessments are biased by auditors specifically in relation to laws and directives which have subjective natures.

They commented that audit should not only focus on increasing the government revenue through the collection of unpaid tax rather it should focus improving the compliance level of taxpayers so that the indirect effect of tax audit outweigh the direct effect. It is also obvious that the ultimate goal of tax audit should be increasing the government revenue but due care should be given to the fact that auditors should not be evaluated with the amount of tax collected through the tax audit department rather their efficiency should be seen from the overall collection capacity of the authority and the compliance levels of taxpayers because if compliance level of tax payers is improved the amount of tax that will be collected through the assessment and collection department will be increased.

4. There is uniform and consistent tax audit practice among all teams that can increase taxpayers` compliance for being treated at the same trend?

| Strongly disagree | disagree | neutral | Strongly agree | agree |
|-------------------|------------|------------|----------------|------------|
| frequency | frequency | frequency | frequency | frequency |
| 4 | 19 | 0 | 10 | 12 |
| percentage | percentage | percentage | percentage | percentage |
| 8.89% | 42.22% | 0 | 22.22% | 26.67% |

Concerning uniform and consistent tax audit practice to enhance compliance, 4(8.89%) responded as strongly disagree, 19(42.22%) disagree, 10(22.22%) strongly agree and the remaining 12(26.67%) responded with agreement as shown in the above table.

From the interviewees it is responded that though it is tried at the branch level to have consistent and uniform tax audit practice throughout teams of the process, there are still conditions that make differences among teams: These are audit sampling techniques, materiality of amounts to fall under audit considerations and tax laws which are open, not available and lack of clarifications. Examples mentioned are the practice of estimated tax assessment (i.e. at what condition does the taxpayer`s financial book and records will not be accepted to be audited based on books and records and documents). Another point in relation to estimated tax assessment is way of assessing the estimated tax, some teams use the net profit rate table studied for individual taxpayers compiled before 10 years and others use the profitability ratio of companies under the same industry. There is also confusion in utilizing bank statement of tax payers`, production standard of companies, accepting evidences of traditional transactions and valuation of properties and others. From the above stated facts it is possible to summarize that the audit practice in the branch among teams is not uniform and consistent on tangible conditions and this leads taxpayers to be non – compliant for being treated differently on the same issues.

4.2.3 The role of tax audit in the reduction of tax evasion and avoidance

The existing tax gaps in developing countries is the result of tax evasion and avoidance and are widely believed to be important factors limiting revenue mobilization. Accordingly tax audit is believed to be the most important/vital mechanism to reduce tax avoidance and evasion.

| Do you think that tax audit in LTO is playing vital role in the reduction of tax evasion and avoidance? | Frequency | Percent |
|---|-----------|---------|
| Yes | 5 | 11.1 |
| No | 40 | 88.9 |
| Total | 45 | 100.0 |

Source: Field Survey Result (2016)

Regarding the role of tax audit in the reduction of tax evasion and avoidance out of the 45 respondents 40(88.9%) said that tax audit is not playing vital role in the reduction of tax evasion and avoidance while the remaining 5(11.1%) of the respondents respond tax audit plays vital role in the reduction of evasion and avoidance. To supplement the questionnaire an interview with team leaders and process owner was held and mentioned that the role of tax audit to reduce tax avoidance and evasion in the branch is not satisfactory because the tax audit is done with inexperienced auditors, inadequate intelligence and investigation support and lack of integrated system with different stakeholders on the economic transactions of the country. Furthermore it is reflected that taxpayers use advanced technologies which help them to manipulate tax liabilities for instance duplication of receipts, creating strong illegal market distribution channel and making economic transactions without any source document, and making business using E-commerce/on line marketing . Due to these the interviewee has doubt about the professional competency of ERCA's auditors to discover the avoidances and evasions committed by the tax payers because most private companies have employees with better skills and knowledge of auditing than the branch office auditors have, private companies provide different incentive packages to attract highly qualified labor from the market and well experienced auditors from the authority itself and as a result they manipulate the tax laws and regulation in a way that understates the taxpayers' tax liability. Another question was suggestion about the measures that has to be taken by the tax authority to avoid the loop holes of the law. ERCA needs continuous amendment of the tax law when it is believed that it has loop hole for more tax manipulation.

4.2.5 Techniques of tax avoidance taxpayers use to reduce tax liability

Three basic principles of tax avoidance within an income tax: postponement of taxes, tax arbitrage across individuals facing different tax brackets (or the same individuals facing different marginal tax rates at different times), and tax arbitrage across income streams facing different tax treatment. Many tax avoidance devices involve a combination of these three principles.

The methods by which individuals reduce their tax liabilities take a variety of legal and illegal forms, all of which are influenced at least in part by incentives created by the tax structures. These methods by which individuals rescue their tax liabilities take a variety of legal and illegal forms, all of which are influenced at least in part by incentives created by the tax structure. These

methods can be broadly classified as avoidance and evasion. Tax avoidance is any legal activity that lowers taxes, and tax evasion is the reduction in tax liabilities by illegal means.

Question related with the techniques usually non-compliant tax payers use to reduce their tax liability was raised to the interviewee and the outcome of the interview revealed that most taxpayers use tax avoidance and evasion to reduce their tax liabilities. Some of the tax avoidance mechanisms/techniques are acquiring/purchasing fixed assets at the end of the year to calculate depreciation expenses; taxpayers also use different illegal activities like printing double receipts, failure to give receipts to customers, preparation of falsified financial statements by manipulating income and expenses. Failure to declare the correct amount of income, overstating expenses, declaring personal expenses as business expenses, and using investment privileges for unintended purpose like machineries acquired for a project may be rented to third party which is not legible, raw materials imported for intelligence and investigation can tackle the above stated tax avoidance and evasion activities committed by the tax payers.

4.2.6 Application of information technology in Auditing

In modern tax administration, it is necessary to computerize the tax collection procedure. Application of IT in audit is also very important for effective and efficient utilization of resources.

Table 4.3: Regarding Application of IT

| Measures | Missed | | Yes | | No | |
|--|-----------|---------|-----------|---------|-----------|---------|
| | Frequency | Percent | Frequency | Percent | Frequency | Percent |
| Do you think that Network is a problem in the application of SIGTAS /standard integrated government tax administration system/in auditing? | 0 | 0 | 41 | 91.1 | 4 | 8.9 |
| Do auditors have taken training to apply SIGTAS in Auditing | 1 | 2.2 | 8 | 17.8 | 36 | 80 |

| | | | | | | |
|--|---|-----|---|----|----|------|
| Do you think that audit is applying information technology (SIGTAS) with full modules? | 1 | 2.2 | 9 | 20 | 35 | 77.8 |
|--|---|-----|---|----|----|------|

Source: Field Survey Result 2016

As it can be seen from table , the respondents were asked whether network is a problem in the application of SIGTAS, majority of the respondents 41(91.1%) states that it is a problem, 4(8.9%) respondents' states that it is not a problem.

Another question was raised whether auditors have taken the necessary training to apply SIGTAS in auditing or not out of the 45 respondents 36(80%) didn't take training on the application of SIGTAS in auditing while the rest 4(8.9%) of the respondents have taken the training and 1(2.2%) respondent didn't expressed opinion. Response of tax auditors/officials is very important to know whether auditors are utilizing SIGTAS modules to the maximum level.

As indicated in the above table, the data collected from respondents reveal that 9(20%) LTO apply IT with full module and 35(77.8%) respondents stated that it does not apply IT in audit to its maximum capacity and 1(2.2%) does not give opinion.

To supplement the questioner an interview was held with team leaders, how do they evaluate the contribution of SIGTAS in promoting modern tax administration and the main challenges in the application? The outcome of the interview shows SIGTAS has irreplaceable role in promoting modern tax administration however it needs well trained personnel in its application because it has modules that needs interpretation in its application, there is also severe network problem to use the system effectively and efficiently and even if training of trainers was given by the head office there is also a problem of transferring knowledge of SIGTAS application by trainers of trainees to use the SIGTAS to its maximum function.

8.3 .Survey results of Taxpayers

Response of tax payers is very important to assess the tax audit practice and its challenges so questions were developed and distributed to taxpayers and the analysis is presented as follows:-

Table 4.4: Regarding audited businesses

| How many times your business is audited by ERCA auditors? | Frequency | Percent |
|---|-----------|---------|
| Two times | 3 | 5.2 |
| Three times | 13 | 22.4 |
| More than 3 | 42 | 72.4 |
| Total | 58 | 100.0 |

Source: Field Survey Result 2016

As indicated in the above table 4.11, out of 58 taxpayers respondents 3(5.2%) were audited two times, 13(22.4%) of the taxpayer were audited three times and 42(72.4%) were audited more than three times. In summary majority of the taxpayers who fill the questioner were audited more than three times.

Table 4.5 Regarding the Tax law

| Do you think that the audit was done based on the tax law? | Frequency | Percent |
|--|-----------|---------|
| Yes | 42 | 72.4 |
| No | 16 | 27.6 |
| Total | 58 | 100.0 |

Source: Field Survey Result 2016

Taxpayer’s opinions whether their tax liability was audited in line with tax laws or not a question was forwarded as indicated in table 4.13, 42(72.4%) respondents’ states that their tax liability was audited based on the tax law and 16(27.6%) of respondents states that their tax liability was not audited based on the tax laws.

For respondents who responded that the tax audit was not done based on the tax law, additional question to state their reason and their result is raised and the response is summarized in the following table.

Table 4.6: Capabilities/ Tax Auditors’ Proficiency and ethical issue

| Reason of choice | Frequency | Percent |
|--------------------------------------|------------------|----------------|
| Missed | 42 | 72.4 |
| Auditor’s competency | 3 | 5.2 |
| Corruption | 4 | 6.9 |
| Impartiality/ neutrality of auditors | 9 | 15.5 |
| Total | 58 | 100.0 |

Source: Field Survey Result 2016

Out of the 58 respondents, 3(5.2%) have doubt on auditors’ competency, 4(6.9%) respondents associate the issue with corruption and the remaining 9(15.5%) have doubt about the impartiality/ neutrality of auditors.

4.3.1 Tax Payers’ Dissatisfaction

Taxpayers are permitted to appeal against audit and assessment; Appeals assure non - discriminatory application of the tax system, and work toward the achievement of an equitable tax. Appeals can correct oversight and protect general public. A smooth appeal process proceeds from an open hearing to an informal hearing in the department, to a hearing in a specialized tax

count, to the regular high court, helps to ensure that laws will be applied on formal and economical ways.

Table 4.7: Tax payers' dissatisfaction

| Q.1 Have you ever proceed to appeal after completion of audit case | Frequency | Percent |
|--|-----------|---------|
| Yes | 35 | 60.3 |
| No | 23 | 39.7 |
| Total | 58 | 100.0 |
| Q.2 Have you ever participate any taxpayer educational session prepared by tax audit department of the branch? | | |
| Missed | 3 | 5.2 |
| Yes | 25 | 43.1 |
| No | 30 | 51.72 |
| Total | 58 | 100.0 |
| Q.3 Do you have trust in the auditors of the tax authority | | |
| Yes | 37 | 63.8 |
| No | 21 | 36.2 |
| Total | 58 | 100 |

Source: Field Survey Result 2016

The above table 4.14 shows regarding appeal, taxpayers' education and tax payers' trust on auditors and these are discussed below:

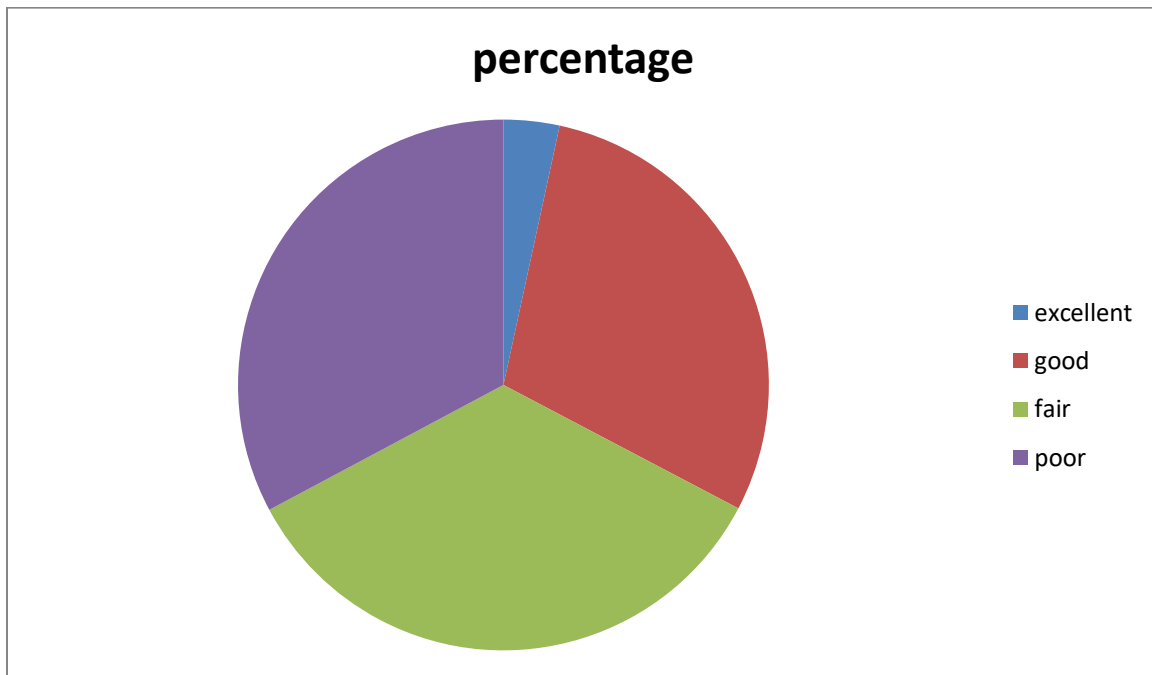
Appeal: 35(60.3%) respondents/taxpayers appealed after completion of an audit case while the remaining 23 (39.7%) respondents/taxpayers didn't go for appeal after audit case.

According to ERCA (2010), tax audit policy and strategy once taxpayers have been provided with the necessary means to meet their obligations, they must believe that there will be consequences of not complying.

Tax payers education; the respondents revealed that 3(5.2%) respondents did not give their response, 25(43.1%) respondents participated taxpayers educational session and majority of the respondents 30(51.72%) didn't attend in taxpayers educational session prepared by the tax audit department. In summary more number of taxpayers didn't get any educational session.

Tax payers' trust on auditors: - 37(63.8%) respondents have trust on tax auditors while the remaining 21(36.2%) do not have trust in auditors. In summary majority of the taxpayers have trust/confidence on tax auditors but significant numbers of taxpayers also do not have confidence/trust.

Regarding service delivery



Source: Field Survey Result 2016

Figure 4.2 Survey response regarding service delivery

For the question in relation to the tax audit department's role in the facilitation of taxpayers' service, 2(3.4%), 17(29.3%), 20(34.5%) and 19(32.8%) of the respondents revealed that it is excellent, good, fair and poor respectively. Regarding the tax payers' service satisfaction on audit significant number of tax payers responded that the service is poor and this indicates that the branch office needs to work hard to improve its service delivery.

To evaluate tax auditors' with respect to profession, competency and integrity/ethics another question was forwarded to taxpayers respondents.

Table 4.8 Taxpayers view on tax auditors' proficiency

| Measures | Excellent | | Good | | Fair | | Poor | |
|--------------------|-----------|-------|------|-------|------|------|------|------|
| | F | P | F | P | F | P | F | P |
| Professional | 20 | 34.5% | 33 | 56.9% | 5 | 8.6% | 0 | .0% |
| Competent | 14 | 24.1% | 39 | 67.2% | 4 | 6.9% | 1 | 1.7% |
| Integrated/ethical | 37 | 63.8 | 18 | 31.0% | 2 | 3.4% | 1 | 1.7% |

Source: Field Survey Result 2016

Where: F= Frequency, P= Percent

In terms of professionalism, out of the respondent taxpayers, 20(34.5%), 33(56.9%), 5(8.6%) and (0%) revealed excellent, good, fair and poor respectively. In relation to competency surveyed from respondents 14(24.1%), 39(67.2%), 4(6.9%) and 1(1.7%) responded excellent, good, fair and poor respectively and with regard to integrity/ethics 37(63.8%), 18(31.0%), 2(3.4%) and 1(1.7%) respond excellent, good, fair and poor. When the responses of taxpayers are summarized according to the taxpayers' response majority of the taxpayers states that tax auditors have good profession, competency and ethical behavior.

A statement was provided to tax payers, whether tax audit supports taxpayers in matters of difficulties while complying with tax laws or not. The data obtained from respondents is presented on the following graph.

Survey response regarding support from tax audit

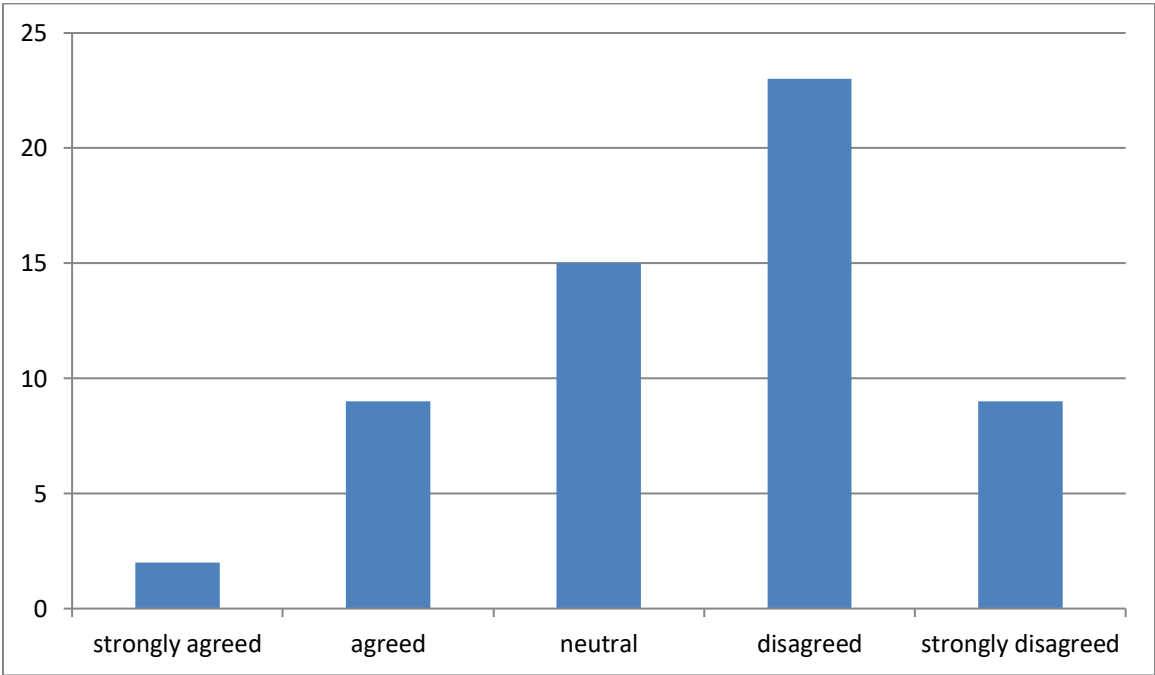


Figure 4.3 Survey response regarding support form tax audit

As indicated in the above graph respondents gave opinion about the support of tax audit for taxpayers in matters of difficulty while complying with the tax law. Out of 58 respondents 2(3.4%) strongly agreed, 9(15%) agreed, 15(25.9%) respondents are neutral, 23(39.7%) disagreed and the remaining 9(15.5%) respondents strongly disagreed with the statement. In summary more than half 32(55.2%) of the respondents states that they didn't get support from the tax audit at the time of difficulty while complying with tax laws.

4.3.2 Taxpayers compliance

The following table revealed statements regarding taxpayers' compliance, which is forwarded to respondents.

Table 4.9 Taxpayers' compliance

| Measures | Missed | SA | Agree | Natural | DA | SD | Total | |
|---|-----------|------|-------|---------|-------|-------|-------|--------|
| Taxpayers who are complying are benefited by not being subjected to partiality and unrepeated audit activity which resulted in reduced compliance cost. | Frequency | 0 | 2 | 12 | 16 | 24 | 4 | 58 |
| | Percent | .0% | 3.4% | 20.7% | 27.6% | 41.4% | 6.9% | 100.0 |
| Tax Audit Plays greater role in improving compliance level of tax payers | Frequency | 1 | 3 | 6 | 16 | 23 | 9 | 58 |
| | Percent | 1.7% | 5.2% | 10.3% | 27.6% | 39.7% | 15.5% | 100.0% |

Source: Field Survey Result 2016

For the statement taxpayers who are complying are benefited by not being subjected to partiality and unrepeated audit activity resulted with reduced compliance cost.

As shown in the above table 4.16 out of respondents, 2(3.4%) strongly agreed with the statement , 12(20.7%) agreed and 16(27.6%) are neutral to the statement, 24(41.4%) respondents disagreed

and 4(6.9%) strongly disagreed. In summary majority of the respondents 28(48.3%) disagreed with the statement.

The other statement was whether tax audit plays greater role in improving compliance level of tax payers.

As indicated in the above table 4.16 out of the 58 taxpayer respondents 1(1.7%) respondent didn't respond, 3(5.2%) respondents strongly agreed with statement, 6(10.3%) respondents

Agreed, 16(27.6%) are neutral and 23(39.7%) respondents disagreed and the remaining 9(15.5%) respondents are strongly disagreed with statement.

Table 4.10 Tax System

| Measures | | Missed | Excellent | Good | Fair | Poor |
|--|-----------|--------|-----------|-------|-------|-------|
| Simple and understandable tax laws | Frequency | 0 | 0 | 13 | 11 | 34 |
| | Percent | .0% | 0% | 22.4% | 19.0% | 58.6% |
| Service to taxpayers | Frequency | 0 | 2 | 19 | 18 | 19 |
| | Percent | .0% | 3.4% | 32.8% | 31.0% | 32.8% |
| Simple filing and payment procedure | Frequency | 0 | 4 | 13 | 15 | 26 |
| | Percent | .0% | 6.9% | 22.4% | 25.9% | 44.8% |
| Appropriate penalties | Frequency | 0 | 2 | 12 | 11 | 33 |
| | Percent | .0% | 3.4% | 20.7% | 19.0% | 56.9% |
| Effective and efficient appeals system | Frequency | 1 | 3 | 32 | 17 | 5 |
| | Percent | 1.7% | 5.2% | 55.2% | 29.3% | 8.6% |
| Automated system /SIGTAS | Frequency | 1 | 1 | 12 | 17 | 27 |
| | Percent | 1.7% | 1.7% | 20.7% | 29.3% | 46.6% |

Source: Field Survey Result 2016

Questions related with the tax system were provided to taxpayers and the results of the respondents are presented in the above table 4.17

According to the survey result for the Question whether the tax authority has simple and understandable tax laws the 58 taxpayers responded 0(0%), 13(22.4%), 11(19%) and 34(56.8%) that it is excellent, good, fair and poor respectively. They were also provided with the Question related to service to taxpayers, 2(3.4%), 19(32.8), 18(31%), and 19(32.8%) of the response said it is excellent, good, fair and poor respectively.

Another Question related with simple filing and payment procedure, 0(%), 13(22.4%), 15(25.9%) and 26(44.8%) respondents show it is excellent, good, fair and poor respectively. Penalties have effect on tax evasions and avoidance; if there is effective penalty systems applied uniformly it creates deterrent effect for non-compliant taxpayers. If the severity of the penalties is recognized by taxpayers they are forced to comply with the tax system.

For the question whether there is appropriate penalties, 2(3.4%) respondents said it is excellent, 12(20.7) said it is good and 11(19%), it is fair and the remaining 33(56%) respondents said there is inappropriate penalties. Another question to know whether the tax authority has effective and efficient appeal system or not, taxpayer respondents' opinion is very important. The survey result indicates 1(1.7%) no response, 3(5.2%) excellent, 32((55.2%) good, 17(29.3%) fair and 5(8.62%) poor. In summary the appeal system is good.

Use of information technology /SIGTAS/ enables revenue bodies to provide fast services to taxpayers, to manage taxpayers' data easily, to compute tax liabilities, audit taxpayer's tax return and for continuous follow up. Question related with the automate system particularly SIGTAS`S application was provided to taxpayers.

The data obtained from taxpayer respondents reveal that, 1(1.7%) didn't respond, 1(1.7%) it is excellent, 12(20.7) said it is good, 17(29.3%) said it is fair and the remaining 27(46.6%) respondent said the automate system is poor. In summary significant number 27(46.6%) of taxpayer respondents said it is poor.

To fill the gap of the questioner's unstructured interview was held with taxpayers about the tax system of the authority and the data reveals that the tax authority has inappropriate penalty system, before applying penalties tax payers need assistance on how to comply with the tax systems.

Slow and inefficient automation systems, serious network problem creates delay/hindrances in providing service and results in an efficient service delivery which forces taxpayers to frequently go the tax authority.

CHAPTER FIVE: SUMMARY, CONCLUSIONS AND RECOMMENDATIONS:

The main objective of this study is to assess tax audit practice and its challenges in the case of large tax payers' office. Both survey and in-depth interview techniques were employed to assess the existing challenges in the tax administration.

This chapter is structured in three sections, the first section deals with the summary of findings, the second with conclusions and the third deals with recommendations, based on the analysis and discussion of the study conclusions and recommendations are drawn:

5.1 SUMMARY OF MAJOR FINDINGS

The purpose of the study is to assess the tax audit practice and its challenges. Four major aspects are analyzed: proficiency and competence of auditors, application of IT in the tax administration especially in audit, function of audit to tackle tax evasion and avoidance and improving the compliance level of tax payers. The major findings of the study are summarized as follows:

- There is no organized tax audit plan which comprises trend, risk and profitability analysis of taxpayers' tax return that can enable auditors to focus on risk areas and to perform the tax audit effectively and efficiently.
- Assigning/directing of audit cases based on seniority and being familiar with the case is not effective in the branch because of turnover of experienced auditors, promotion of internal senior employees with no audit experience and transferring of auditors from small scale taxpayers (sub – cities) centers to the branch.
- There is no adequate and standardized teams follow up procedure that can enable to enhance auditors' competency and controlling of the audit effectiveness and efficiency.
- Regular tax audit teams' discussion on complex audit issues is not reflected regularly in 1 to 5 discussions and this has material effect on the competence of auditors and quality of tax audit assessments.

- The law department is not supporting the audit process both in terms of timing and quality of clarification of vague laws and this has a vital impact on auditors' competence and fair tax assessment.
- The top level management is not alert in facilitating auditors to have international educational access and to be highly competent in the profession and this is also one major reason for experienced employees to resign and to look for better organizations.
- Tax auditors are not effective and efficient in the tax audit performance and this has a vital effect both for the tax authority's tax revenue collection and taxpayers compliance.
- Auditors are not provided with continuous and relevant trainings and this has major effect for their being competent.
- Employees with high performance are not recognized and rewarded in the branch, and this has negative impact to enhance their work motivation.
- Auditors have argument on the employees' code of conduct of the authority, article/37 which states that the director of the authority has full right to fire employees from their job whenever there is doubt that practice of corruption has been done without critical evidence. This does not consider different ways of taxpayers' provoking unto auditors when they become sure that more additional tax will be assessed by the audit.
- There are still major audit cases which are appealed by taxpayers in all years though the number is getting lower from year to year as compared to the actual number of audit cases which are audited in each year.
- Among types of audits (i.e. Comprehensive, desk, issue audit/limited scope audit, field audit, refund audit and compliance audit (for special taxpayer i.e. AEO) which are listed in the tax audit manual of the authority, it is only comprehensive audit which is practiced by the tax audit process of the branch office. This results to cover limited number of taxpayers and has limitation to enhance taxpayers' compliance.
- Selection of taxpayers for audit through manual system is creating problems like selecting taxpayers repeatedly, limited number of criteria's are utilized for selecting

taxpayers for audit, human errors of capturing data and omitting taxpayers with high risk without selecting them for audit due to several reasons.

- Feedback from taxpayers on tax awareness improvement after audit indicates as dissatisfaction. In addition no action plan and implementation follow up schedule have been made by the management so as to improve taxpayers` tax awareness in relation to the audit conducted by the branch.
- The audit practice in the branch among teams is not uniform and consistent on major issues and this leads taxpayers to be non – compliant for being treated differently.
- It has weakness in the application of IT in auditing to its maximum capacity: use of SIGTAS for risk base audit case selection and others.
- Taxpayers didn't participate in major sessions/education prepared by the audit department and this creates barriers for taxpayers to comply with the tax laws.
- Penalties were viewed as ineffective in influencing compliance behavior, unless taxpayers develop awareness on how to comply with the tax laws because the same mistakes may be committed especially for those unconsciously committed tax gaps.
- Survey regarding tax system majority of the taxpayers respondents face difficulties to understand the tax laws due to its vagueness, the filing procedure is complex and payment system is old and lengthy, penalties are imposed on taxpayers before providing awareness creation programs, respondents didn't deny the fact that there is an appeal system established by the branch office, however it is not effective and efficient to pass decision on time, and Majority of the taxpayers respondents commented on the automation system of the tax authority that it is slow sometimes it is a serious problem.

5.2 CONCLUSION

To achieve the objectives of government revenue a well-organized tax audit program is vital to ensure the fiscal health of the country, and sustain the health of the tax system by reducing tax gap through voluntary compliance improvement and additional tax collections. Further, it might provide valuable support in identifying areas of the tax law that require clarification or addressing deficiencies in the law, and to influence compliance across the broader taxpayer community at all levels.

This paper has attempted to analyze the tax audit practice of Large Taxpayers office, ERCA. In particular, the study explored auditors 'proficiency, competence and integrity, audit's contribution to enhance compliance, role of tax audit practice to reduce the act of tax avoidance and evasion and finally tries to analyze the IT application for audit practice . These investigations were addressed by employing survey questionnaires, semi structured and structured interview given to tax officials and taxpayers and by reviewing published and unpublished documents. Finally, on the basis of qualitative and quantitative analysis of data, the findings of this study are summarized as follows:

Auditors` of the branch are not effective and efficient in their tax audit performance in relation to being incompetent. Among major factors which are considered to be vital for not being competent are lack of organized tax audit plan, inadequate follows up by teams, and lack of continuous and relevant trainings as per the need assessment of the tax audit process can be mentioned.

Based on the audit performance report of the branch, taxpayers' compliance is getting improved in the branch. But the practice of comprehensive audit for all taxpayers without considering the

risk level of taxpayers and lack of continuous and advanced taxpayers training are major factors which hinders the enhancement of compliant taxpayers to maximum level.

Tax audit practice in the branch has limitation in playing significant role in the reduction of tax avoidances and evasions for not working in collaboration with intelligence and investigation departments of the authority and concerned external bodies. In addition different tax loop holes are not identified and forwarded by the audit process for amendment of tax laws in organized way.

It obvious that IT plays significant role for tax audit activity for several reasons which are mentioned in the literature review .But the application of IT in the branch for audit practice is not effective as needed because auditors are not utilizing SIGTAS to the maximum level of modules due to lack of knowledge and commitment and very slow network.

5.3. RECOMMENDATIONS

From the summarized findings and conclusion the following recommendations are provided to achieve an effective and efficient tax audit system:

- Organized tax audit plan for each type of business and that can enable auditors to focus on risk areas and to perform the tax audit effectively and efficiently should be prepared by the management.
- Adequate and standardized teams follow up procedure that can enable to enhance auditors` competency and controlling of the audit effectiveness and efficiency should be maintained. In addition to providing advanced and continuous audit trainings to team leaders.

- Regular tax audit teams' discussion on complex audit issues should be arranged and practiced in the branch because this has material effect on the competence of auditors and quality of tax audit assessments.
- Tax Laws, regulations and different directives should be collected from different sections of the authority and be organized by modern and easily accessible IT support. In addition the law department should work in campaign so as to clear the release of wrong clarifications on different laws and should compile the right explanations and release to different branches of the authority so as to avoid confusion of auditors in their work. Furthermore they should give continuous trainings to auditors on different tax laws.
- The top level management should continuously communicate with different local and international concerned bodies to create advanced educational opportunities that can enhance auditors' proficiency and competence.
- To solve the problem of auditors' being inefficient and ineffectiveness continuous and relevant trainings which bases the need assessment of the audit process should be provided by the branch management, different external institutions and tax audit directorate /at head office level/.
- Though the authority made significant salary increment to its employees, the management should continuously assess the market to analyze the salary and benefits effected by different organizations to their employees and then to make immediate revision so as to retain experienced staffs .
- Employees with high performance should be recognized and rewarded by the management regularly so as to enhance and sustain their work motivation.
- In relation to the creation of favorable work environment, the management of the authority should consider in depth different harassments that could be done by taxpayers against auditors in audit process before firing employees based on article/37 of employees' code of conduct. And should work hard with different concerned bodies to

gather relevant evidences in relation to the practice of corruption. It is also better to see in-depth the consequence of the article and amend with a better law.

- The branch`s tax audit process should start implementing different types of audits which are listed in the tax audit manual other than comprehensive audit so as to increase the audit coverage for the ultimate goal of enhancing taxpayers compliance and increasing additional tax revenues. But due care should be taken before in analyzing taxpayers` risk level effectively.
- Taxpayers to be selected for audit should be screened by SIGTAS which works with more risk criteria selections, after arranging advanced trainings that can enable employees to utilize the maximum level of modules that can be functioned in the system.
- The management should continuously assess and prepare the required action plan in relation to feed backs raised by taxpayers to improve their tax awareness in relation to the audit conducted by the branch.
- The tax authority should continuously improve the public awareness on the consequence of being compliant and non - compliant, so that the level of compliance can be improved and non-compliance will be minimized. In addition to this continuous and intensive training and awareness creation programs should be prepared to taxpayers.
- Tax audit should aimed at reducing the problems of tax evasion, tax avoidance and other tax irregularities to improve the level of filing, payment and reporting compliance by collaborating with intelligence and investigation departments of the authority and different external stakeholders .
- Penalties should be used in combination with other measures such as taxpayers` education and services in order to achieve greater compliance.
- ERCA should improve the network quality problem in providing fast services to its customers and employees should be trained more to utilize the maximum module of SIGTAS effectively.
- The tax authority should continuously review the tax laws so that the loop hole of the laws can be addressed without adversely affect the tax revenue of the government.

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Annexes

Annex I

St. Mary's University

Masters of Business Administration

QUESTIONNAIRE ON: TAX AUDIT PRACTICE AND ITS CHALLENGES

Date-----

Dear respondents,

The purpose of this study and this questionnaire is to conduct a research on “tax audit practice and its challenges” for the partial requirement for the MBA degree. The outcomes of this study will help policy makers and tax Authorities, particularly Ethiopia Revenue and Customs Authority (ERCA)/Large Taxpayers office/, to know its weak areas and to make corrective measures, modern service to its customer, to organize the tax audit in way that promotes modern tax administration. This research is intended only for academic purpose authorized by the representative of St.Mary`s University, Thus, your ideas and comments are highly honored and kept confidential. The researcher thus appreciates in advance your cooperation and sparing your valuable time in filling this questionnaire, if you have any questions about completing the questionnaire. You may contact me with the following address.

HenokAbebe

Tel. 0913004711

Email henokarsema2020@gmail.com

Part One: Demographic characteristics of Respondents,

Please circle (tick) a response that best describes your experience so that the study will show realistic result .Thank you for your cooperation.

I. Questionnaires to be filled by tax audit staffs put in the box of your choice part

1. Gender

Male 2 Female

2. Age

Less than 25 25-35 35-45

45 - 55 5. Above 55

3. Educational background

12 complete 2. Certificate 3. Diploma

BA/BSC 5. MA/MSc 6.please specify if any other_____

4 . Field of study

Accounting & finance 2. Management 3. Economics

Please specify if any other_____

5. Work experience

Less than 2 years 2-4 years 4-6 years

6-8 years 8-10 years above 10years

6. Current job occupation

Junior auditor auditor senior auditor

Team coordinator Process owner

Part II questions related to the tax auditors competence, proficiency and

Please show the extent to which you think is appropriate by putting tick mark in any one of the five choices next to each statement.

The number is represented as:-

1. Strongly Disagree 2. Disagree 3. Neutral 4 .Strongly Agree 5. Agree

| No | Variables of auditor`s competence, proficiency and capacity | 1 | 2 | 3 | 4 | 5 |
|----|---|---|---|---|---|---|
| 1 | Auditors prepare organized tax audit plan that can help them to identify the risk areas of taxpayers` tax return which specifically bases the type of business that the taxpayer is engaged. | | | | | |
| 2 | There is a clear procedure to assign audit cases to auditors` which considers their seniority and being familiar with the case. | | | | | |
| 3 | There is adequate team leaders` follow up so as to support and control auditors` work execution | | | | | |
| 4 | There is regular discussion forum which is held by tax audit teams to simplify complex tax audit issues | | | | | |
| 5 | When tax laws, regulations and directives are not clear/not easily available, it is immediately responded by the concerned body so as to use it as an input for an effective tax audit assessment | | | | | |
| 6 | Continuous and relevant trainings are provided to tax auditors | | | | | |
| 7 | Top level management of the authority facilitates auditors to be certified in ACCA, CPA and the like | | | | | |
| 8 | Team leaders and senior auditors are committed, capable and transparent to support juniors on job trainings and in audit execution process | | | | | |

| | | | | | | |
|----|--|--|--|--|--|--|
| 9 | Salaries and different benefits earned by auditors are adequate compared to the payment effected by other sectors in the market | | | | | |
| 10 | Employees whose work performance is better than others are recognized and rewarded by the management on regular basis | | | | | |
| 11 | The work environment is convenient for auditors and helps them to complete the audit task without negative influence from different parties | | | | | |
| 12 | Auditors are assessing audit cases both in number and in amount as per the audit plan and standard | | | | | |
| 13 | Major audit cases which are assessed by tax auditors are accepted by taxpayers without any complain | | | | | |
| 14 | When taxpayers do not accept the audit assessment and proceed to appeal, assessments are revised by the appeal committee in favor of the branch rather than taxpayers at major level | | | | | |

Questions related to the audit`s contribution for enhancement of taxpayers` compliance

Please show the extent to which you think is appropriate by putting tick mark in any one of the five choices next to each statement.

The number is represented as:-

1. Strongly Disagree 2. Disagree 3. Neutral 4 .Strongly Agree 5. Agree

| No | Variables for taxpayers` compliance | 1 | 2 | 3 | 4 | 5 |
|----|--|---|---|---|---|---|
| 15 | The Audit coverage in the branch has a vital contribution so as to increase the compliance of taxpayers | | | | | |
| 16 | The audit selection program of the branch has significant effect to increase compliance | | | | | |
| 17 | Taxpayers get adequate awareness from the tax assessment | | | | | |
| 18 | Auditors primary objective is assessing additional tax from the taxpayer rather than enhancing taxpayers` awareness | | | | | |
| 19 | There is uniform and consistent tax audit practice among all teams that can increase taxpayers` compliance for being treated at the same trend | | | | | |

Questions related to the Application of IT (information technology for tax audit)

Put “√”in the box of your choice

20. Do you think that the branch office apply information technology in auditing to its maximum capacity?

Yes No

21. Do you think that network is a serious problem in the application of SIGTAS/ standard integrated government tax administration system in auditing?

Yes No

22. Do auditors have taken the necessary training to apply IT in Auditing?

Yes No

23. Large taxpayers, office is effective in auditing and enforcement.

1. Strongly agree 2. Agree 3. Neutral
4. Disagree 5. Strongly disagree

Annex II

Interview questions with tax officials (Process Owner and Team Leaders)

1. What do you say about the tax audit plan preparation for an audit case?
2. How do you assign audit cases for auditors?
3. Is there consistent and adequate team leaders follow up trend for audit cases?
4. Is there regular discussion among teams so as to reflect ideas on complex issues?
5. Do you get immediate and relevant response from the law directorate when you need any clarification on tax laws?
6. What do you say about the adequacy and nature of training provided to auditors?
7. Does top level management of the authority facilitate auditors to be certified in ACCA, CPA and the like?
8. What do you say about team leaders and senior auditors' commitment, capacity and transparency to support juniors on job trainings and in audit execution process?
9. What do say on the adequacy of salaries and different benefits earned by auditors compared to the payment effected by other sectors in the market?
10. Is there recognition and reward system for employees with high performance in the branch?
11. Does the work environment is convenient for auditors and helps them to complete the audit task without negative influence from different parties?
12. How is auditor`s effectiveness and efficiency both in number of audit cases and additional tax assessment compared to audit plan and standard?
13. What do you say about the quality of audit, especially in relation to the number of taxpayers who complained to appeal?
14. How is the rate of appeal committee`s revised decision in favor of tax auditors?
15. Do you think that the Audit coverage in the branch has a vital contribution so as to increase the compliance of taxpayers?
16. Do you believe that the audit selection program of the branch has significant effect to increase compliance?
17. How do you see the adequacy of tax awareness that taxpayers get from tax assessment?

18. Which one is auditors` primary objective in assessing additional tax or enhancing taxpayers` awareness?
19. Is there uniform and consistent tax audit practice among all teams that can increase taxpayers` compliance for being treated at the same trend?
20. What mechanisms do you suggest/advise/ the branch office should implement to reduce tax evasions and avoidances?
21. Which loop holes do taxpayers usually use to reduce their tax liability?
22. What is your suggestion about the measures that has to be taken by the tax authority to avoid the loop holes of tax laws?
23. How do you evaluate the contribution of SIGTAS and its challenges in audit practice?
24. Give your general comment on the overall tax audit practice and its challenge in the branch office.
25. Suggest how these challenges can be improved?

Part III

Questionnaires to be filled by LTO taxpayers,

Put “√”in the box of your choice

Section A personal Data

1). Gender

1. Male

2. Female

2). Age

1. Less than 30yrs

2. 30- 40yrs

3. 40-50 yrs

4.50-60yrs

5.Above 60yrs

3). Level of education

1. Grade12 and below

2. Certificate

3.Diploma

4. First Degree

5.Masters

6. PhD

4) Business type/sector

1. Manufacturing

2. Construction and real estate

3. Merchandising

4. Service

5. Other if any specify_____ -

5) How many times does your business is audited by the branch auditors?

1. One

2. Two

3.Three

4. More than three times

6) Do you think that the audit was done based on tax law in a fair manner?

1. Yes 2. No

7) If your answer for question #6 is “No” tick the reason(S) of your choice?

1. Auditor`s competency
2. Corruption
3 . Impartiality of auditors
4. Any other mention _____

8) Have you ever proceed to appeal after audit case?

1. Yes 2. No

9) Have you ever participate any taxpayer educational session prepared by tax audit department of the branch office?

1. Yes 2. No

10) What is your opinion about the tax audit department’s role in the facilitation of taxpayers’ service?

1. Excellent 2. Good 3. Fair 4. Poor

Adopted 11. How do you evaluate the strength of tax auditors with respect to the following parameters?

| List of parameters | Excellent | Good | Fair | Poor |
|--------------------|-----------|------|------|------|
| Professional | | | | |
| Competency | | | | |
| Integrity/ethics | | | | |

12) Do you have trust in auditors of the branch?

1. Yes 2. No

13) Tax audit support taxpayers in matters of difficulties while complying with tax laws.

1. Strongly agree 2. Agree 3. Neutral
4. Disagree 5. Strongly disagree

14) Taxpayers who are complying are benefited by not being subjected to harassment and Unnecessary audit activity and with reduced compliance cost.

1. Strongly agree 2. Agree 3. Neutral
4. Disagree 5. Strongly disagree

15). Tax audit plays greater role in improving compliance level of tax payers.

1. Strongly agree 2. Agree 3. Neutral
4. Disagree 5. Strongly disagree

Adopted 16. How do you evaluate the strength of the tax authority with respect to the following parameters?

| List of parameters | Excellent | Good | Faire | Poor |
|--|-----------|------|-------|------|
| Simple and understandable tax laws | | | | |
| Service to taxpayers | | | | |
| Simple filing and payment procedure | | | | |
| Appropriate penalties | | | | |
| Effective and efficient appeals system | | | | |

17) How do you evaluate ERCA's automated system in providing fast service and improving the tax administration?

1. Excellent 2. Good 3. Fair 4. Poor

Annex IV

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DECLARATION

I, the undersigned, declare that this thesis is my original work; prepared under the guidance of DR. Tilahun Mehari. All sources of materials used for the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree.

Name

St. Mary`s University, Addis Ababa

Signature

June/2017

ENDORSEMENT

The thesis has been submitted to St. Mary's University, school of Graduate Studies for examination with my approval as a university advisor.

Advisor

St. Mary`s University, Addis Ababa

Signature

June/2017

