

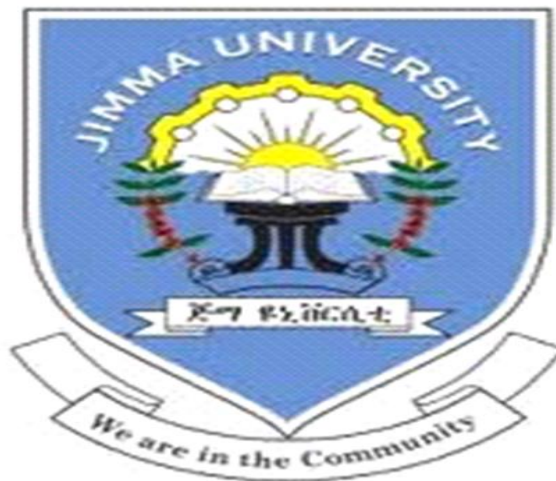
***IMPLEMENTATION PRACTICE OF VALUE ADDED TAX:***

***In case of Hosanna town administration***

***A Thesis Submitted to School of Graduate Studies of Jimma University in  
Partial fulfillment of the Requirements for the Award of the Degree of  
Masters of Public Management (MPM).***

***BY***

***AMANUEL DESALEGN UNTISO***



**JIMMA UNIVERSITY**

**BUSINESS AND ECONOMICS COLLEGE**

**MPM PROGRAM**

**June 21 /2017**

**Jimma, ETHIOPIA**

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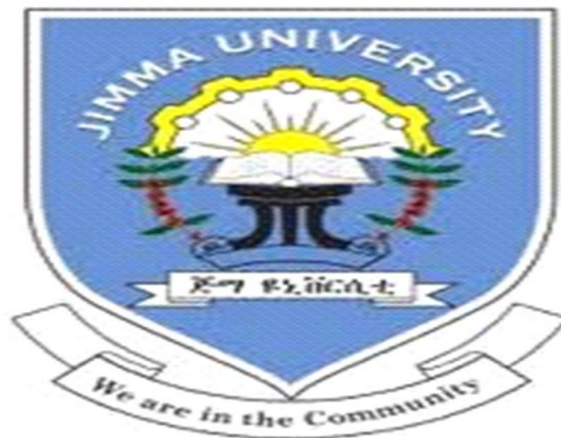
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**Under the guidance of**

**Ato. Taye Amogne**

**And**

**Ato. Demissie Beyene**



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**MPM PROGRAM**

**June 21 /2017**

**Jimma, Ethiopia**



## **Declaration**

I hereby declare that this thesis entitled “Implementation Practice of Value Added Tax: In Case of Hosanna Town Administration” has been carried out by me under the guidance and supervision of Ato. Taye Amogne and Ato Demissie Beyene.

The thesis is original and has not been submitted for the award of any degree or diploma to any university or institution.

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## Certificate

This is to certify that research entitled “ Implementation practice of Value added tax: in case of Hosanna town”, submitted to Jimma University for the award of degree of Masters of Public Management (MPM) research work carried out by Mr. Amanuel Desalegn Untiso under our guidance and supervision.

Therefore, we hereby declare that no part of this thesis has been submitted to any other University or institution for the award of any degree or diploma.

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## **Acronyms/ Abbreviation**

Art. = Article

BRO = Baltic countries, Russia, and other countries of the former Soviet Union

ERCA = Ethiopian Revenue and Customs Authority

FAD = Fiscal Affairs Department

FIRA = the Federal Inland Revenue Authority

MoFED = Ministry of Finance and Economic development

GDP = Gross Domestic Product

GNP = Gross National Product

GST = Goods and service tax

IMF = International Monetary Fund

P.A.Y.E = Pay As You Earn

RST = Retail sales Tax

TIN = Tax payer identification number

VAT = Value Added Tax

WTO = World trade organization

## **Abstract**

*This study was conducted with the title implementation practice of value added tax in Hosanna town, which is found in SNNPR with the objective of the analyzing consistency of value added tax practice with its rules, proclamation and to identify the major hindrance problems in its implementation. To achieve all these the researcher used mixed, quantitative and qualitative type of data, descriptive research design and sample from target population by using stratified random sampling technique. After that the researcher used questionnaires, interviews for sampled respondents and reviewing related documents to collect the intended data and analyzed the obtained data by simple static model with frequency, Percentages and presented on tables. In finding the main challenges those encountering in effective implementation of VAT are: misunderstanding of the public in general and business community in particular regarding the VAT implementation objectives, resistance from registrations for VAT by some traders, administration inefficiency from tax office, non-issuance of receipt to customers by registered business enterprises. On the basis of these findings, the researcher recommended that the authority should train the taxpayers about the rules and regulations of VAT continuously, recruiting new skilled employees and give training for the existing one, it should also increase its follow-up and investigation to control noncompliance enterprises, as well as effectively and efficiently performing the tasks of identification of VAT payers, controlling collections, recognizing genuine taxpayers and local public should be sensitive for the revenue of country as well as town by contributing their effort on effective implementation.*

*Key words: Article, Business community, Hosanna town, Proclamation, Value Added Tax,*



# CHAPTER –ONE

## INTRODUCTION

### 1.1 Background of the study

To boost socio-economic development projects of the country governments' mostly generate revenue from taxes. Tax is a liability imposed up on the tax assesses who may be individuals, groups of individuals, or other legal entities. It is a liability to pay an amount on account of the fact that the tax assesses have income of a minimum amount and from certain tangible or intangible property, or that they carry on certain economic activities which have been for taxation (Bhatia, 1996)

According to Shenk,A & Oldman,O, (2007), indirect taxes have been the backbone of all taxation in developing countries and it contributes two-thirds or more of tax revenues in many countries. Similarly, indirect tax is more important instrument for the poorest countries to enhance domestic tax revenues on goods and services.

Value added tax (VAT) is one type of indirect tax, which is replaced in current time in terms of sales tax. Value added tax is a tax on consumption of goods and services and it is to be collected on the value of imports and on value added on goods and services supplied by one business to another until it reaches to final consumers (Bird, 2005).

Again VAT is defined as broad-based tax imposed on commodity sales up to and including the production stage, with systematic offsetting of tax charged on commodities when purchased as inputs-except perhaps on capital goods (Ebrill, et al., 2001).

VAT is proclaimed as the most important of the latter twentieth century and definitely the most breaking and with its significant influence on the domestic economy and the government policies (Ping, Z, 2006).

Over the last few decades, VAT has swept the world. The principal reasons for the rapid of this form of taxation were, first, the early adoption of this form of taxation in developing and transitional economies by the International Monetary Fund (IMF) in particular and by international agencies and advisers in general (Richard, 2006).

Value added tax adoption and implementation introduced in Ethiopia on January 1, 2003 by the aims to raise more revenue, modernizing tax administration and to encourage investment and trades. It is a consumption tax because it is ultimately borne by the consumer, who pays a fixed percentage of the final sale price of a product (Yohannes & Sisay, 2009). Major objectives and benefits of VAT include: Removing the tax on inputs from exported goods to make goods more competitive in international markets, domestically produced goods will be more competitive with imported goods, relief from tax on capital goods will encourage investment, and Value Added Tax (VAT) raises more government revenue than the replaced Sales Tax (Ibid).

A good tax system should have one or a combination of desirable characteristics as economic efficiency, administrative simplicity, flexibility, political accountability and fairness for the purpose of good tax system. This is so because, when the implementation and administration of tax system is effective, the government's revenue that helps to fulfill the socioeconomic needs of the society will be amplified. It is possible to say that the major function of taxation is to marshal the necessary funds to finance the increasingly expanding level of public expenditures.

According to the VAT proclamation of Ethiopia 285/2002, supply of goods and provision of services are subject to standard 15% tax rate except those exempted and zero – rated by the VAT tax law. This standard rate is the same as the replaced sales tax, which were implemented only to imports and domestically manufactured goods. But unlike the sales tax, Value added tax provides relief of tax on all business inputs including capital goods, operating and administrative expenditures, and will further encourage investment by the zero rating of exports and the international transport of goods and passengers. Its exemption has been extended to the fundamental necessities such as Education, Medical services, Electricity, Water, Kerosene, Basic foods, Transportation Services, the sales of a used dwelling or the lease of dwelling, the supply of goods and rendering services in the form of humanitarian aid.

## **1.2 Statement of the problem**

External financial resources were used as a source to fund their developmental activities in case of most less developing countries for the past decades. As a result, their budgetary problems become more aggravated. To overcome this situation and problems, these nations



have tried to exploit and strengthen their domestic financial resource base in order to bring about sustainable development for their nations. Among this domestic financial sources tax which includes VAT is the one to rise government revenue for the increasing of socio-economic developmental projects and to fill the budget deficit (Tareke, Hagos, Kassa, & Temesgen, 2013).

The concept and implementation of VAT is arguable and/ controversial in the side of conservatives and liberals, conservatives argue that taxes should impose on consumption rather than investment, because it at least create incentives for people to save and invest not to spend and this helps to enhance growth of economy in a given nation, While liberals propose that the tax that places a disproportionate burden on the people who are low level of income, because those people spend much larger on their consumption, so it likes a regressive tax (Hailemariam, 2011).

When we came to Ethiopia the concept and implementation of VAT is a recently replaced sales tax with some modification and it is still in growing stage came into realization in 2003.

To continue Value added tax revenue role increasing in the government's finance source, it is essential to ensure that the revenue generated by VAT is collected as efficiently as possible. However, in Ethiopia revenues generated by VAT are usually gathered at the expense of erosion in its salient features. This may be caused by the many factors including poor VAT administration (Wollela, 2009).

According to Tanzi & Pellechio, (1995) cited in Mikesell, (2007) Poor tax administration can interrupt the manner in which taxation effects government's policy objectives, such as economic stabilization, resource allocation and redistribution of income to the whole public. In developing countries the poor performance of taxes is likely to be due to weak tax administration (i.e., the incapacity of the administration to implement the tax law in practice).

With respect to this, the issue of VAT practice is not as much researched in Ethiopia and even some researches done, they have some gaps:

The analysis of Gebre-Egziabher, (2010) with the title VAT Administration and Revenue Performance: More focuses on administration Challenges and revenue performance not bother on views of public and business communities about VAT.

Jalata, (2014) Value added tax as a tool for national development in Ethiopia, focuses more on the contribution of VAT for national development in Ethiopia rather than consideration on the practice and challenges of collection. In addition to this issues those initiate researcher for this study are:

- There are few businesses undertake their business with VAT in the town compared to other towns.
- Issuing of VAT receipt is not well experienced by side of business enterprise for all purchasers and consumers.
- Most local societies have negative attitude about VAT

In addition to this most business enterprises in case of Hosanna are eager to cease business activity which includes VAT, new business undertakers have no willing to register on VAT unless they enforced by tax authority.

By these cases researcher initiated to conduct study and tried to find out what is the reason behind for these.

### **1.3 Basic research questions**

- To what extent the business community/enterprises clearly know the VAT rules and regulations in the town?
- How VAT has been collect from local society or consumers of goods and services by registered business community.
- What are the challenges those can hinder the implementation of VAT in the Hosanna town?
- What are the remedial measures has been taken to overcome these implementation problems in the town?

### **1.4 Objectives of the study**

The main objective of the study was to assess and analyze the value added tax practice such as implementation and administration of value added tax and its challenges in case of Hosanna town.

### **1.4.1 Specific objectives of the study**

- ✓ To assess and analyze the understanding level of business community on rules and regulation of value added tax in the town.
- ✓ To assess value added tax collection system of business community from local society in case of Hosanna town.
- ✓ To identify the major problems those can hinder the implementation practice of VAT in the town.
- ✓ To evaluate the activities taken as a remedial measure to overcome the implementation problems of VAT so far.

### **1.5 Significance of the study**

It is fact that the socio-economic needs of the public will fulfill and can be magnify if and only if there is an effective and efficient administration and collection of taxes, among this VAT is one because it helps to rise government revenue. According to this, the study will be significant or serve:

- ❖ For the researcher it serve as a partial fulfilment for the award of master's degree in public management.
- ❖ It help for the tax authority of Hosanna town and other higher officials in Ethiopia in VAT administration to understand what will have to do by identifying the strengths and weaknesses of themselves in addition to administration system;
- ❖ For VAT registered business community and local society it creates wide understanding about the rules and regulation, objective and advantages of VAT implementation.
- ❖ To the theory of value added tax concept it will contribute some suggested concepts through analysis of people's perception and finally it will use as a reference to initiate future researchers on the issue of value added tax.

### **1.6 Limitations of the study**

This study focused only on VAT implementation practice and its challenges on Hosanna town from many types of taxes impose on the business communities, government employees and other property taxes and it is conducted on a specific area Hosanna town only. In addition to this, even on the conducted title it doesn't incorporate auditing practice, the impact of VAT on

economic growth and the relationship of VAT with government revenue within a specified area. Hence, all these are considered as a research limitation.

## **1.7 Structure of the Paper**

The paper is organized in five chapters: In the first chapter included items are the background of the study, statement of the problem, basic research questions, general and specific objectives, the significance, the scope and limitations of the study.

Chapter two was generally review of related literature which include conceptually, theoretically and empirical studies about the VAT. Chapter three was Research Methodology; those are research design, sampling technique, source and collection method of data.

Chapter four was aimed at dealing with discussion and interpretation of collected data.

The last chapter five deals with major finding, conclusions and recommendations depending on the results discussed under the fourth chapter.

# CHAPTER –TWO

## RELATED LITERATURE REVIEW

### 2.1 Conceptually Value Added Tax (VAT)

According to Black's law dictionary on its part provides that “VAT is a tax assessed at each step in the production of a commodity based on a value added at each step by the difference between the commodities production cost and its selling price”.

Value added tax is defined as broad-based tax which imposed on commodity sales up to the production stage, with systematic offsetting of tax charged on commodities when purchased as inputs-except perhaps on capital goods-against that due on outputs (Ebrill, et al. , 2001).

VAT is designed to be charged on the value added which is the difference between the value of sales and value of purchase goods and services at the point of transaction throughout the production and distribution chain. Value added =total transaction-intermediate transaction. Final sale = GDP =wage + interest + profit + rent + depreciation (Hyman, 2002).

Any producer of goods and service owes tax only in the value added on the transaction, in practice this means that the producer will have a chance of refund for VAT paid on all the purchases of inputs. VAT is a compulsory levy and those who are taxed have to pay the sums irrespective of any corresponding return of services or goods by the government. In generally VAT belongs to the family of sales taxes and a tax not on the total value of the goods being sold, but only on the value added to it by the last seller (Bhatia, 1994).

According to Rosen, (1988) Value Added Tax (VAT) is a percentage tax on a value Added applied at each stage of production. Even if, the VAT main intention is not generally intended to be a tax on value added as definition indicates rather it is usually intended as a tax on consumption. Most countries in the world exclude exports from the VAT, in the sense that tax is not levied on sales for export but tax paid on inputs is recoverable, in addition to this some (in the BRO region, the Baltic countries, Russia, and other countries of the former Soviet Union, at least until recently) are systematically imposed VAT on some exports. Some countries extend the Value added tax only to the manufacturing stage; others do not levy it on

services. Practices also vary in how tax offsetting is implemented by depending on the countries policies: by far the most common method is through the use of invoices, but the same effect can be achieved on the basis of books of account (Hailemariam, 2011)

Because of the diversity of implementation practice, there can be disagreement as to whether a given tax is properly called a VAT or not. For definiteness, though at the risk of creating the impression of an overly sharp dichotomy, we take a VAT to be: A broad-based tax levied on commodity sales up to and including, at least, the manufacturing stage, with systematic offsetting of tax charged on commodities purchased as inputs-except perhaps on capital goods-against that due on inputs. This leaves scope for dispute, but does highlight what is taken here to be the key feature of the VAT: the tax is charged and collected throughout the production process, with provision for tax payable to be reduced by the tax paid in respect of purchases (Ebrill, 2001).

Value added tax is a consumption tax because it is borne ultimately by the final consumer and it is collected as a percentage of prices, which means that the actual tax burden is visible at each stage in the production and distribution chain. VAT is a tax not on the total value of goods being sold, but only on the value added to it by the last seller who is liable to pay a tax not on its gross value, but on the value that is the gross value minus the value of inputs.

Value Added Tax has also become an indispensable component of tax reform in developing countries. It is the most important tax innovation of the second half of the twentieth century. In line with this perception, an increasing number of developing countries have converted their sales tax to Value Added Tax (VAT). The continuing introduction and evolution of general sales taxes, especially of the value added tax has been the outstanding feature in development of taxation in recent years (Goode, 1984).

## **2.2 Theoretically Value Added Tax**

Even if there was no exact sources that can concludes from where and when the VAT was invented for the first time across the world, many of the investigations on such area such as (Reischauer, 1992) and et al. quoted France was the first implementer of VAT by 1954 in the world. At that time even if France introduced VAT at a national level, its original coverage was limited and never reached to the broader retail sector until 1968. But it is the Denmark that

applies full VAT among European countries by 1967 even though she did not join the European Economic Community at that time. And among the African countries, it is Cote d'Ivoire that adopts VAT for the first time in 1960.

Charlet & Butdens, (2012), shows as more than 150 countries which becomes about 75% of the world has now been implementing VAT and today, most countries have a VAT, which raises, on average, about 25 percent of their tax revenue. This makes VAT is the first tax system which spread quickly within a short period of time after its introduction.

In 2003 among the 53 member countries of the African Union about 31 of them introduced and adopt VAT. The table below illustrates those African countries with their rates of VAT and year of introduction.

Table 1: African countries with VAT

country	Date introduced	Standard Rate (%)	Country	Date introduced	Standard Rate (%)
Algeria	1992	21	Mauritania	1995	14
Botswana	2002	15	Mauritius	1998	10
Burkina Faso	1963	18	Morocco	1986	20
Benin	1991	18	Mozambique	1999	17
Cameroon	1999	18	Namibia	2000	15
Chad	2000	18	Niger	1989	17
Congo republic	1997	18	Nigeria	1994	5
Cote-devoir	1960	20	Senegal	1980	20
Ethiopia	2003	15	Rwanda	2001	15
Egypt	1991	10	South Africa	1991	14
Gabon	1995	18	Sudan	2002	10

Ghana	1998	10	Tanzania	1998	20
Guinea	1996	18	Togo	1996	18
Kenya	1990	16	Tunisia	1998	18
Madagascar	1994	20	Uganda	1996	17
Malawi	1989	20	Zambia	1995	17.5
Mali	1991	15			

Misrak, (2008).

The following table also shows the VAT rates of some European and non-European countries (other than African countries).

Table 2 : world countries with VAT

Country	Standard Rate (%)	Country	Standard Rate (%)	Country	Standard Rate (%)
Australia	20	Romania	19	Lebanon	10
Belgium	21	Slovakia	19	Moldova	20
Bulgaria	20	Slovenia	20	Macedonia	18
Cyprus	15	Spain	16	Malaysia	5
Czech Republic	19	Sweden	25	Mexico	15
Denmark	25	United Kingdom	17.5	New Zealand	12.5
Estonia	18	Argentina	21	Norway	25
Finland	22	Australia	10	Paraguay	10
France	19.6	Bosnia & H	17	Peru	19
Germany	19	Canada	6	Philippines	12
Greece	19	Chile	19	Russia	18
Hungary	20	China	17	Serbia	18
Ireland	21	Croatia	22	Singapore	5



Italy	20	Ecuador	12	South Korea	10
Latvia	18	El Salvador	13	Sri Lanka	15
Lithuania	18	Guyana	16	Switzerland	7.6
Luxembourg	15	Iceland	24.5	Thailand	7
Malta	18	India	12.5	Turkey	18
Netherland	19	Israel	15.5	Ukraine	20
Poland	22	Japan	5	Venezuela	8
Portugal	21	Kazakhstan	14	Colombia	45

Misrak, (2008).

### 2.3 Types of VAT

**Income Type VAT:** This type of tax is where the firm permitted to deduct the full value of its non-capital purchase from other firm. This approach in fact gives they prepare net value added for the country as whole the aggregate tax base in the absence of international trade would be net national product (NNP). In other word here the tax base is sale minus material minus depreciation for each firm (Bhatia, 2003).

The value added tax of income type thus different from that the consumption type in that former permit the firm to deduct depreciation while later per unit it to deduct gross investment i.e. purchase capital (Musgrave, 2004 ).

**Consumption Type VAT:** In this case the firm in question is allowed to deduct from the gross value of its product or service not only the capital in puts purchased from other business firm but also the capital equipment so purchased. In the absences of the foreign trade the greatest base of this tax for the economy as a whole became wage (w) plus profit (p) plus depreciation (d)minus investment (I), therefore, the aggregate tax base became;  $C = GNP - I$ .

**Gross National Product Type VAT:** Under this to arrive at the value added tax by the firm the value of the input purchased from the other firm not allowed to deduct in fully only the value of none capital equipment purchased is deducted no depreciation is permitted on purchase of capital good even in subsequent year.

This type of value added tax most of the time cannot be popular with the government because it militates against the use of capital and referred economic growth  $GNP = IG + C$   $IG$ =gross investment  $C$  = consumption (Musgrave, 2004).

**Wage Type VAT:** This Variety of VAT is where the firm is able to deduct the net earnings from its capital in order to arrive at the tax base since earnings from capital amount to profit plus interest. Therefore the balance left to be taxed is equivalent to wage and it is also unlikely to be used for taxation by any government.

## **2.5 Importance of Value Added Tax**

The necessity for VAT originates from the very weakness of the sales tax that it is intended to replace (Purhoit, 2000). First, sales tax has a cascading effect as a result of the fact that it is charged on the gross value without allowing any credit or set off the taxes paid on inputs. As a result, consumer's price will increase by an amount higher than accrues to the government department in charge of revenue by way of revenue from it. Secondly, VAT has the advantage of minimizing the cost of production of goods and services through its inherent refund system and the fact that it does not burden exports.

Thirdly, it offers total transparency of the incidence of tax as VAT is multistage sales tax imposed as proportion of the value added. A very important thing that quotes the need of VAT is less tax evasion. This is due to the tax is divided into parts and therefore the incentive to evade tax by any one firm is reduced. If any firm understates its output, it will be caught by the disclosures of the firms buying inputs from it (Hailemariam, 2011).

## **2.6 Advantages and Disadvantages of Value Added Tax (VAT)**

### **2.6.1 Advantages of Value added tax**

1. The polarity of VAT with authority is mainly due to its administrative advantage. It is much easier to assess and evaluate tax liability of a firm by using credit method. There is greater chance for cross-checking of return submitted by firm. A general VAT is supposed to be neutral to the resource allocation forms of production and business organization, in contrast, turnover tax encourage vertical integration of production so as to avoid the intermediary sales and taxes to acquire a competitive advantage over other. A VAT, on the other hand, is neutral between

the processes of integration and therefore helps the economy in adopting that form of production which is economically more suitable.

2. VAT is also neutral between factors expenses because it taxes all value added. As against this, the existing corporation taxation discourage the usage of equity capital and punishes profit earning, VAT does not hinder adoption of technology which may be capital intensive.

3. It is argued that VAT avoids cost-cascading effect. The conventional sales tax lead to compounding of tax liability, while VAT does not.

4. An implied advantage of VAT is its neutrality with regard to resource allocation.

5. A very important advantage quoted in favor of VAT is that lesser tax evasion. Firstly, this happens because the tax is divided into part and therefore the incentive to evade tax by any one firm is reduced. Secondly, it is in the interest of firm to the account for the tax paid by earlier firms through which is the inputs have come otherwise this firm pays the tax itself. If any firm therefore understands its inputs, it will be caught by the disclosure of firms buying input from it. These types of cross-auditing enable the authority to plug the tax leakages.

6. The use of VAT helps a country in encouraging its exports. In order to get competitive edge over others, a country may refund the taxes paid the on the exportable goods.

It is easier to separate the tax from cost of production in case of VAT, but not so in case of other taxes which get mixed up with the cost of production (since they relived at gross value in each case). To other advantage is that the. General agreement on trade in tariffs also recognized VAT rebate as legitimate practice of encouraging exports.

7. It is also claimed that VAT is conducive efficiency since a firm is not exempted from its tax liability even if it runs into loss. It pays a tax not on its profit but on the value produced. It therefore, tries to improve its performance, and reduced the cost of production.

8. It is argued that for various reason, some good should enjoy a tax exemption (zero tax rate) while the remaining one's need not be subjected to a uniform tax rate. In practice, it has been possible to incorporate these features into VAT. Multiple (including zero) rates are now commonly found in vat systems. A multiple tax rate variety can also easily accommodate credit

systems (that is, dedicate tax liability of a firm by the amount of taxes paid by other firm on its purchases). All this imports a great deal of administrative flexibility to VAT so that its exact content can be modified to suit different policy objective of the authorities (Misrak Tesfaye, 2008).

### **2.6.2 Disadvantages of Value Added Tax (VAT)**

VAT is not just a bundle of advantages. Rather it has serious limitations especially for underdeveloped countries because what it has not yet become popular (HL bhiatia, 1996).

1. VAT is a complicated system and need honest and efficient government machinery to do the cross checking and link up various production activities and the resulting tax liability of each firm. It is, therefore, necessary in its financial and economic structure and the firm should be in the habit of keeping proper accounts.
2. This system depends a lot upon cooperative the tax payer. Each firm itself calculate it tax liability to begin with, and also find out the taxes paid by curlier firms. Once, however, the seller realize that the administrative machinery or the government is ill-equipped to do all the necessary cross-checking, they will resort to the creation of false purchase invoices showing taxes paid by others. To the extent this happens becomes a major possibility and a common practice.
3. Unless the rates of VAT are extraordinary high, the state would end up with smaller tax revenue as against the collection from sales tax.
4. Even if the tax payers are fully honest of, the system of taxation forces them to maintain elaborate and costly account. This becomes uneconomical, especially for smaller firms.
5. The difficult of maintaining accounts, cross checking and preventing tax evasion increase if the system contains some exceptions (such as for food item) and differential rate of taxation ( luxurious are likely to be taxed at higher rate than necessity ). And once the authority decides to adopt he selective pattern, vested interest developed and exert pressure for exemption and concession. In such circumstances actual decision may not remain fully objective.
6. Critics of VAT doubt that it includes efficiency. The claim that in a shortages economy like ours speculative hoarding, non-competitive price rise and similar practice are quite common.

In a seller market, producers and sellers have no incentive to increase their efficiency and reduce cost since goods will sell irrespective of their in for quality and high price (Abay, 2015).

## **2.7 Empirical Studies about Value Added Tax (VAT)**

The analysis of Purohit, (1993) on the adoption of VAT in India considering its problems and prospects discloses as the implementations of the VAT by a rapidly growing number of countries has been one of the most incredible events in the evolution of commodity taxation in this century. The author concludes that VAT can generates sufficient amount of revenues for the government that enables to boost the country's economic growth in general.

The study of Bogetic & Hassan, (1993), on the emerging conventional wisdom based largely on practice and numerous country case studies, discussed as Indonesia introduced VAT in 1983 and by 1988; the ratio of VAT revenue to GDP had risen to 4.5%.

As supported by the analysis and finding of Adereti, et al. , (2011), when revenue was collected from VAT, it contributes to the total government revenue and hence enhance economic growth.

Brautigam, et al., (2008) on the analysis deal with VAT increases government revenue, improves economic efficiency, promotes exports, reduce disincentives to formal activity, raise revenue rapidly, simplify the tax administration procedures, widen the tax base and be an instrument of economic growth.

The study of Aizenman & Jinjarak, (2005) explained as the VAT revenue is unavoidably collected as far as there were the chain of production and consumptions of goods and services.

As stated by Emrana & Stiglitzc, (2005) countries that do impose a VAT have a tendency to be larger, wealthier, and more industrialized than those that do not. This is due to the reason that VAT is imposed on buyers at each stage of value adding chains, and no one refuses to pay it unless otherwise refuses to purchase the goods and services.

Alemu, (2011), empirically analyzes the contributions of VAT for economic development and social spending in Ethiopia from 2003 to 2010 using the variables of Health sector development, education sector development, agricultural and natural resource development, infrastructural development, other development indicator sector and development indicator

sector indicated as VAT revenue had a significant contribution for the development of the economy during the period under study though the contributions are statistically significant only to health and agricultural and natural resource development sectors.

Wollela, (2009), Despite the concentration of most of the prior tax compliance literature on direct taxes (mainly income tax) neglecting indirect taxes, it was noted that VAT noncompliance appeared to be predominant, especially in developing countries. VAT noncompliance could take various forms including not registering for VAT, registering but not levying VAT (partially or wholly) on sales, levying VAT on sales but not reporting (partially or wholly), claiming credit on purchases more than the input tax paid, not claiming input VAT credits and not maintaining proper books and supporting documents. The prevalence of these forms of VAT noncompliance could be because of any of the determinants of tax noncompliance; and the level of VAT compliance costs was shown to be one of the factors potentially affecting VAT compliance decision of taxpayers.

Bekure Herouy, (2004), the classic ingredients of VAT that determines how the tax does work are: The tax is charged on certain transactions such as the sale of goods, the provision of services, and other types of supplies. It is charged at each stage of the production and distribution chain by businesses and other persons carrying on a continuous or taxable activity. Specified supplies are charged at the rate of 0% or are exempt from the tax. Zero rated businesses can claim a credit for VAT paid on inputs, exempt businesses cannot.

## **2.8 VALUE ADDED TAX IN ETHIOPIA**

### **Introduction**

VAT is a tax not on the total value of goods sold or services rendered but only on the incremental value or newly created value by the last seller. The incremental value is the difference between sales proceeds and purchases of intermediate goods or services excluding the preceding VAT. It is the base for VAT computation.

### **2.8.1 VAT Administration in Ethiopia**

Due to the reason that VAT has multidimensional advantages to the country, many states to which Ethiopia is not an exception adopted it. This can be assumed as the government and tax revenue is hand and glove for each other.

Hence, according to the VAT proclamation No 285/2002, Ethiopia adopted and implemented VAT by January 1st 2003 with the single standard rate of 15%, zero rate and some exemptions treated under the law and regulations.

In the world there are three most important models regarding to VAT: European, Japanese and New Zealand styles. Among these, even though most jurisdictions of the state across the world adopted that of the European model of VAT, many commentators and experts of taxation related to tax revenue and its administrations assumes as the New Zealand's model of VAT is the most ideal and preferable among all. To that extent, the VAT implemented in Ethiopia has the ideal model related to that of New Zealand's model though each country has its own unique application of the VAT system as related to their socio-economic, political and living standard of its citizen's (Jalata, 2014).

The Ethiopian constitution, (1995) provides the central and regional governments with the power of taxation, and the bases up on which revenue is shared between the government is established by proclamation No. 33/1992. The ERCA administers VAT nationally as per the joint decision made by the house of representative and council of federation. Although VAT is administered centrally by ERCA, the revenue is shared between central and regional governments based up on the established revenue sharing.

Some of the ERCA basic tax administration activities are identifying and register the taxpayers, controlling collection, processing returns, securing delinquent declarations and collection of tax arrears, making refunds, auditing taxpayers account, make different investigation to minimize and avoid tax fraud and evasion, and following up of tax office have to be revitalization measure taken in order for VAT to live up to the expectation as an efficient and fair source of country revenue (Gebre-Egziabher, 2010).

The following were administration measure taken by ERCA before exercising the VAT proclamation and regulations effectively: Identification of taxpayers to be registered for VAT

and distribution of booklet was made and orientations about VAT were given to taxpayers for the purpose of introduction of rules and regulations.

The Value Added Tax (VAT) proclamation No 285/2002 which has rescinded and replaced the sales and excise tax proclamation No. 68/1993 (as amended) and which has come into force as of January 1st, 2003 is a consumption tax which is levied and paid as value added tax at a rate of 15% (percent) of the value of every taxable transaction by a registered persons, every import of goods, other than an exempt import and an import service rendered in Ethiopia for a person registered in Ethiopia for VAT or any resident legal person by a non-resident person who is not registered for VAT in Ethiopia (Article 7 (1) (a)-(c) and Article 23 (1) and (2)).

A taxable transaction is a supply of goods or a rendition of services in Ethiopia in the course or furtherance of a taxable activity other than an exempt supply. (Article 7(3)) A taxable activity is any activity, which is carried on continuously, or regularly by any person in Ethiopia, or partly in Ethiopia, whether or not for a pecuniary profit that involves, in whole or in part, the supply of goods or services to another person for consideration. Article 6 (1) and (2)) Supply means the sale of goods or rendition of services or both and rendition of services means anything done, which is not a supply of good or money.

(Article 2(17) and Art. 4(1)) For the purpose of the VAT proclamation the following are considered as taxpayers on whom the VAT law is applicable. These are: -

(a) A person who is registered or is required to register for VAT; (b) A person carrying out a taxable import of goods to Ethiopia; (c) A non-resident person who without registration for VAT renders service in Ethiopia for any person registered in Ethiopia for VAT or any resident legal person (Article 3(1), (a)-(c) and Article 23 (1) and (2)).

## **2.8.2 VAT Rate**

The VAT law contains two VAT rates. One is the standard 15 percent rate and the other is zero rated. According to [Article 7 (2) (a) - (d)] the following taxable transactions are charged with tax at a rate of zero percent.

a. The export of goods or services



b. The rendering of transportation or other services directly connected with international transport of goods or passenger, as well as the supply of lubricants and other consumable technical supplies taken on board for consumption during international flights

c. The supply of gold to the National Bank of Ethiopia; and d. A supply by a registered person to another registered person in a single transaction of substantially all of the assets of a taxable activity or an independent functioning part of a taxable activity as a going concern. There is a basic difference between VAT exemption and zero rate VAT. The difference is that though zero rate transactions do not pay VAT on the goods and services they render under transactions listed in (a) – (d) above, for the purpose of VAT registration they are considered as taxable service thus enabling and making these transactions eligible for collecting tax rebate.

This has the advantage of granting VAT rebate which can help redress in put tax paid on purchase of goods and services necessary for the furtherance of the zero rated transactions. On the other hand, VAT exemptions granted by the VAT law does not allow for the collection or entitlement of VAT rebate for the simple reason that they are assumed not to have paid in put tax, therefore disabling exempt categories from registering for VAT and taking advantage of the VAT rebate provisions.

### **2.8.3 Registration Procedure**

A person applying to register for VAT is required to do so in such a form as is established by the implementation directives issued by the Ethiopian Revenue and Customs Authority; When a person carrying out taxable transactions files an application to be registered for VAT, the authority is required to register the person in the VAT register, and to issue a certificate of registration within 30 days of the registration; A person registered for VAT is required to use his taxpayer identification number on all VAT invoices, and on all tax returns and official communications with the authority.

The registered person is required to issue the VAT invoice to the purchaser of goods or services up on the supply or rendering, but not later than 5 days after the transaction.

There are two ways of registration stated in the VAT proclamation no. 285/2002. Obligatory registration and voluntarily registration.

#### **2.8.4 Obligatory Registration**

A person who carries on the taxable activities and is not registered is required to file an application of VAT registration in the authority if at the end of any period of 12 calendar months the person made, during that period, taxable transactions the total value which exceeded 500,000 birr; Or if at the beginning of any period of 12 calendar months there are reasonable grounds to expect that total value of taxable transactions to be made by the person during that period will exceed 500,000 birr. Depending on this sub-articles (sub-articles 1(16) in article 16) the nine trade activities (line) whose annual taxable income is expected to be more than 500,000 birr to be registered for VAT and registering all companies having legal entities for VAT without any prerequisite at the current condition.

#### **2.8.5 Voluntary Registration**

According to countries context, taxpayers attitudes, knowhow and consensuses determines the number of voluntary taxpayers. This kind of registration is made by a person who carried on taxable activities and is not required to be registered for VAT, may voluntarily apply to the authority for such registration, if he/she regularly is supplying or rendering at least 75% of his goods and services to registered persons. In the voluntary registration input VAT can be recovered if a person is registered. It will therefore be beneficial to voluntarily register where the person makes mainly zero-rated supplies. In such a case, input VAT will be recovered, and no VAT will be charged on zero-rated outputs (Article 17).

#### **2.8.6 Cancellation of VAT Registration**

A person who has registered for VAT may cancel his or her registration by arrangement with ERCA, department of VAT. The reason for deregistration include:

If the business closes trading permanently, If the business is sold, When the value of taxable supplies falls consistently below the VAT registration threshold, If he or she has been registered in error, or she has ceased to be a taxable person.

When registration for VAT is cancelled, the authority is required to remove the person's name and all other details from the VAT register and the person is required to return back the issued certificate of registration. VAT registered person cannot charge VAT or issue tax invoices for

any supplies made and cannot claim a refund of VAT incurred on any goods and services purchased from the date of the registration is cancelled.

### **2.8.7 Exemption for Specific Categories of Goods and Services**

Tax-exempt goods and services are supplies on which VAT, both the standard rate and zero-rate tax, are not paid on. If a person who is engaged in a taxable activity that fully falls under the tax exempt category, such a person cannot register for VAT. If a person is engaged partially in a tax exempt category activity and partially in a taxable activity, such person cannot register for VAT and be eligible for tax rebate which could be beneficial to redress cost paid for input tax on his taxable transactions.

In a similar manner Income Tax Proclamation No 286/2002, Article 13 (e) has empowered the Council of Ministers and the Minister of Finance and Economic Development to exempt by regulation any income for economic, administrative or social reasons.

The Council of Ministers for the proper interpretation of the VAT proclamation issued the Value-Added Regulation No 79/2002.

The major areas on which proper and broader interpretation has been rendered include exemptions granted by the VAT proclamation whereby general areas of exemptions have been listed without detailed interpretation and implementation terms and conditions. In this regard, the regulation clearly states what falls under the exempted items and what does not fall under or constitute exemption under the VAT proclamation. These exemptions include inter-alia provision relating to religious or church-related services and provisions relating to supplies of humanitarian aid.

The Regulation provides that generally, services rendered by a religious organization that are integral to the practice of that religion come within the exemption. The donation in kind or money (such as church plate donation) or services is not subject to tax if there is no direct link between the payment and any benefit received by the donor (Article 23 (1), (2), (4) and (6)). A religious organization that operates taxable activities through a development commission or similar entity must separately register the commission or the similar entity.

The Regulation also provides that the exemption for supplies of humanitarian aid applies to goods imported or purchased locally by organizations registered as humanitarian organizations for such purpose. (Article 26 (1) and (2))

The exemption covers the import of goods or purchase of goods locally with an announcement or declaration of a natural disaster, industrial accidents, or catastrophe by the Disaster and Prevention Commission. An exemption by agreement covers tax exemption for certain import of goods only if the agreement is entered into by the government or the agreement is entered into with permission granted by the government (Article 28 (3) and (4)).

## **2.8.8 Tax credit, procedures for filling tax return and payment of VAT and VAT refund or rebate**

### **2.8.8.1 Tax Credit**

Under the VAT law the amount of VAT that is creditable is the amount of VAT payable (paid) by: a registered person in respect of tax invoices or customs declaration issued to the person for: a. Imports of goods that take place during the current accounting period; and b. Taxable transactions involving the supply of goods or rendering of services that are considered to take place during the current or preceding accounting period.

Where the goods or services are used or are to be used for the purpose of the registered person's taxable transactions (Article 21(1) (a) and (b)). In cases where only a part of the supplies made by a registered person during a tax period are taxable transactions, the amount of tax credit or rebate for that period is determined;

- a. In respect of a supply or import received, which is directly allocable to making of taxable transactions, the full amount of tax payable in respect of the supply or import is allowed as credit or rebate. b. In respect of a supply or import received which is directly allocable to the making of exempt transaction, no amount of tax payable in respect of the supply or import shall be allowed as a credit or will be allowed as a credit.
- c. In respect of a supply or import received which is used both for the making of taxable and exempt transactions, the rule of apportionment of the credit will be determined by a directive to be issued by the Ministry of Revenue (Article 21 (2) (a) – (c)).

(Article 21(5) A person who registers for VAT after the introduction of VAT will be entitled to credit in the first accounting period in which the person is registered for VAT paid or payable on goods (including capital goods) that are on hand on the date of registration. However this will be applicable only to the extent that the purchase or import of the goods occurred not more than six months prior to the date of registration (Article 21(6)). A beneficiary of the duty draw – back scheme under proclamation No. 249/2001 – a proclamation to establish Export Trade Duty Incentive Scheme is not entitled to a refund of VAT paid on imports under the VAT credit system of the VAT law (Article 21(7)).

### **2.8.8.2 Procedures for filing tax return and payment of VAT**

Under the VAT law every registered person is required to: (a) File a VAT return for each accounting period, whether or not tax is payable in respect of that period; and (b) pay the tax for every accounting period by the deadline for filing the VAT return. The VAT return for every accounting period must be filed not later than the last day of the calendar month following the accounting period (Article 26, 1(a) and (b) and (2)).

### **2.8.8.3 VAT refund or rebate**

If at least 25 percent of the value of a registered person's taxable transactions for the accounting period is taxed at a zero rate, the tax authority will refund the amount of VAT applied as a credit in excess of the amount of VAT charged for the accounting period within a period of two months after the registered person files an application for refund, accompanied by documentary proof of payment of the excess amount (Article 27(1)). In the cases of other registered persons, the amount of VAT applied as a credit in excess of the amount of VAT charged for the accounting period is to be carried forward to the next five accounting periods and credited against payments for these periods, and any unused excess remaining after the end of this five- month period shall be refunded by the tax authority within a period of two months after the registered person files an application for refund, accompanied by documentary proof of payment of the excess amount.

## **2.9. Administrative penalties**

The following penalties are imposed for violations of the VAT proclamation:

Where any person engages in taxable transactions without VAT registration where VAT registration is required-100% of the amount of tax payable for the entire period of operation without VAT registration; Where any person issued incorrect tax invoice resulting in a decrease in the amount of tax or increase in accredit or in the event of the failure to issue a tax invoice-100% of the amount of tax for the invoice or the transaction; Where a person who is not registered for VAT issues a tax invoice-a penalty of 100% of the tax which is indicated in the tax invoice and is due for transfer to the budget but has not been transferred; and where a person fails to maintain records required-2,000 Birr for each month or portion thereof that the failure continues. A person who fails to file a timely return is liable for a penalty equal to 5% of the amount of tax underpayment for each month (or portion thereof) during which the failure continues, up to 25% of such amount. The penalty is limited to 50,000 Birr for the first month (of portion thereof) in which no return is failed. If any amount of tax is not paid by the due date, the person liable is obliged to pay interest on such amount for the period from the due date to the date the tax is paid. The interest is set at 25% over and above the highest commercial lending interest rate that prevailed during the preceding quarter VAT proclamation 285/2002

# **CHAPTER - THREE**

## **RESEARCH METHODOLOGY**

### **3.1 Research design**

Research design is a plan of collecting and analyzing data in an economic, efficient and relevant manner. According to this, the nature of this research was descriptive type that incorporates fact finding inquiries and surveys with regard to the Value Added Tax implementation practice. The purpose of this study was to describe practices, challenges of VAT implementation in Hosanna town and trace areas of weaknesses and strengths towards the implementation of VAT Objectives. According to Burns and Grove (2003), descriptive research is designed to provide a picture of a situation as it naturally happens. It may be used to justify current practice and make judgment and also to develop theories.

### **3.2 Target population of the study**

In conducting study on which the researcher was mainly focused to collect relevant data and analyze the condition on their business activity and administration system the target population were Hosanna town VAT registered business communities and town tax authorities. Those total target population 615(450 of sole proprietorship, 150 partnership/ enterprises and 15 tax officials) in the town.

### **3.3 Sampling technique**

The study was conducted sampling and take sample, because to analyze the practice of VAT in all business community is time consuming and very expensive. So in order to cope up with these challenges and to report sensible study the researcher employed stratified sampling from random sampling methods by based on the ownership of the business this means by making strata of enterprises/partnership and proprietorship businesses, those may have different view about VAT application in the town. This sampling method was selected to create homogeneity from heterogeneous groups of business communities on VAT implementation problems on their business in the town.

### 3.4. Sample size determination

Sample size is a number of elements and precision of the study are directly related. This sample size, the researcher mostly used to distribute the study questionnaires' and on that they can reflect their idea on VAT implementation challenges. To determine the sample researcher used 95% of confidence level and consider 5% acceptable error

The sample size for this study was determined using Kothari (Kothari, 2004) sampling design formula.

$$n = \frac{Z^2 * N * p * q}{(N-1)e^2 + Z^2 p * q}$$

Where n = sample size of the respondents

N = Total population of the sample size

Z = 95% confidence interval under normal curve (1.96)

e = acceptable error (0.05),

P and q are estimated of the proportion of the population to be sample.

$$n = \frac{1.96^2 * 615 * 0.5 * 0.5}{(615-1) * 0.05^2 + 1.96^2 * 0.5 * 0.5} \quad n = 236$$

Sample from each strata are calculated by  $n1 = \frac{N1 * n}{N}$

Where, n1 =sample size of each stratum, N1 =Total population of each stratum and N= Total or target population of the study area.

Stratum	Size of population(N)	Sample size
Tax office employees	15	6
Sole proprietorship	450	173
Partnership/enterprise	150	57
Total	615	236

Source: Own computed data, 2017



### **3.5 Source and Type of data for the study**

Regarding to the source of data the research used both primary and secondary data sources. The main sources of primary data were the sample of respondents who are value added tax registered business community and tax administrative authority in the town and the secondary sources to undertake the study were published and unpublished written documents including internet, reports in the office, rules and regulations and mixed, quantitative and qualitative data type employed .

### **3.6 Data collection methods and instruments**

From the sources mentioned above study employed mixed approach of quantitative and qualitative. From the quantitative method, the researcher used survey, collecting closed-ended questionnaires whereas, from the qualitative approach, open-ended and in-depth interview was selected to collect available and relevant data from sampled respondents and selected tax officers respectively these questionnaires adapted from Bizualem, (2015) and Hailemariam, (2011) research papers. In addition to this secondary data by reviewing the written materials include internet, books, reports, regulations and proclamations.

### **3.7 Data analysis and discussion**

After all the activities undertaken especially after data collection is completed from primary and secondary sources carefully, the researcher conducted editing, coding, classification and tabulation of collected data so that they are usable to analysis.

The descriptive statistical analysis method is conducted based on Percentages, frequencies and tables. The data collected from survey questionnaires were carefully coded and organized, because the survey is cross-sectional provides a quantitative or numeric description of trends, attitudes, or opinions of a target population by studying a sample of that population.

After that it entered into the Statistical Package for Social Scientists (SPSS) statistical package SPSS version 20. Descriptive statistics method employed to analyze data, because it is largely the study of distribution of one variable.

# CHAPTER -FOUR

## DISCUSION AND INTERPRETATION

The survey is conducted by distributing questionnaires and conducting interview to both VAT registered taxpayers these are sole proprietor VAT registered taxpayers, partnership/enterprises VAT registered tax payers as well as the selected employees of Hosanna town tax office. The distributed questionnaires to VAT registered taxpayers were prepared with an Amharic version so as to avoid language barriers and minimize response biases due to misunderstanding.

From the target population 615, sample 236 was taken and questionnaire distributed and interview were conducted. Among these sample the usable returned amount of questionnaires with answer was 190 (80.5%).

The data collected from survey questionnaires were carefully organized, coded and entered into the Statistical Package for Social Scientists (SPSS) spreadsheet. The analysis performed with SPSS version 20. Descriptive simple statistical method employed to analyze data. The following table summarizes about the returned response amount from both sides.

Table 3 4.1: VAT registered business community and tax authority officials' respondents' response rate.

VAT registered tax payers	Sample size	%	Number of respondents who provide their replay	%
Sole proprietor VAT registered tax payers	173	75.2	145	77.5
Partnership/Enterprises VAT payers	57	24.8	42	22.5
Total	230	100	187	100
Employees of tax office	6	100	3	100
Total	6	100	3	100
Grand total	236		190	

Source: Own computed survey data, 2017

Table 4 4.2 Demographic information/ Profile of respondents

		Frequency	Percent
Age of the respondents	20--30	60	31.6
	31--40	81	42.6
	41--50	36	18.9
	>50	13	6.8
	Total	190	100
Sex of the respondents	Male	115	60.5
	Female	75	39.5
	Total	190	100
Educational level of the respondents	12 grade and below	57	30.0
	Diploma	76	40.0
	Degree	49	25.8
	Masters	8	4.2
	Total	190	100

Source: own computed survey data, 2017

The above table is used simply to describe the respondents' profile, specially their age, sex and educational status. Accordingly from the participated respondents of VAT registered business community on their age interval 42.6% are age between 31—40, 31.6 % ( 20—30), 18.9% (41—50) and 6.8 % ( above 50).

60.5% (male) and 39.5% (female) based on their sex and in their educational status, 40 % (diploma), 30% (12 grade and below), 25.8% (degree) and 4.2% (masters) in the town from whom data collected. Therefore, this shows that in the town most of the VAT registered tax payers are found in age between 31—40 and are male with their diploma level in education and they are capable to reading and reflecting their idea on questionnaires.

Table 5. 4.2.1 Background information of Respondents

Type of business	Frequency	Percent
Café, restaurant and hotel	78	41.1
Home and office furniture manufacture and whole sale	25	13.2
Building material store	70	36.8
Electronics	10	5.3
Others	7	3.7
<b>Total</b>	<b>190</b>	<b>100</b>
<b>Your status in your business</b>		
Owner	105	55.3
Manager	73	38.4
Casher	12	6.3
<b>Total</b>	<b>190</b>	<b>100</b>
<b>Year of experience in your business</b>		
1—2 years	50	26.3
3—5 years	98	51.6
6—9 years	30	15.8
>10 years	12	6.3
<b>Total</b>	<b>190</b>	<b>100</b>

Source: Own computed survey data, 2017

The above table indicates that even if there are a several business type in the town, the most VAT applied businesses are Café, restaurant and hotel 78 (41.1%) in case of town. Building materials 70 (36.8%) is the second major from where VAT collected mostly and the remaining home and office furniture 25 (13.2%), electronics 10 (5.3%) and others are very few in numbers in the town experience according to collected data.

The above businesses based on the ownership 105 (55.3%) owner, 73(38.4%) manager and 12(6.3%) cashier from the respondents those filled the questionnaires.

The year of experience on a specific business among respondents as shown from the collected data 98 (51.6%) 3-5 years, 50(26.3%) 1-2 years, 30(15.8%) 6-9 years and 12(6.3%) are greater than ten years of experience respectively.

These all are directly and indirectly contributes to the study especially ownership of the business and experience, because they know very well the changes on their business loses and profits ,customer changes, preference of customers and others.

#### 4.2.2 VAT for the first time

Based on the VAT proclamation No 285/2002, Ethiopia adopted and implemented VAT on January 1st 2003 with the single standard rate of 15% of the value of every taxable transaction by a registered person, zero rate and some exemptions allowed under the law and regulations.

According to this, before registration and implementation on their business, the business communities should understand its essence through deep government training. In relation to this, the sampled business communities were asked about,

Table 6 4.2.2 How did you hear about VAT and its implementation for the first time?

	Frequency	Percent
By government training	111	58.4
By media	64	33.7
From other business competitors	15	7.9
Total	190	100.0

Source: own computed survey data, 2017

As the data on the above table from the total respondents, 111(58.4%) responded that they heard from government training, 64(33.7%) responded that they heard from media and 15(7.9%) responded that they heard from other business competitors.

This shows that before implementation government gave training about the VAT for the business owners and tax authority employees even if it did not reach to the whole public and business activities up to local level by a decentralized manner. Because of this, some of the

business communities heard from media like TV, Radio and others. Beyond this some others heard from other similar business competitors when they implement on their business. Therefore, in generally some business communities did not hear about VAT in a formal training before implementation in the town experience.

### **4.2.3 Business community awareness level of all VAT proclamation and regulations**

The adopted VAT proclamation No 285/2002 has its rules and regulations specified by articles to which every business communities and tax officials have to adhere and undertake their business and responsibility accordingly. In its articles what kind of activities included in the VAT, what is expected from business communities, what are the punishments and when registration for VAT is obligatory are briefly stated. According to this, to assess the awareness level of VAT law from respondents the question were asked,

Table 7 4.2.3 As a taxpayer, do you think that you/your organization are well aware of all the VAT proclamations and regulations?

	Frequency	Percent
Yes	32	16.8
To some extent	91	47.9
Not aware	67	35.3
Total	190	100.0

Source: Own computed survey data, 2017

On the above table from total respondents 32(16.8%) responded yes, 91(47.9%) responded to some extent, 67(35.3%) responded that not aware.

This indicates that majority of the respondents 91(47.9%) are not fully aware of VAT proclamation and regulation, 67(35.3%) not aware about the each proclamation and regulation and 32(16.8%), which is very few of them replied clearly know about VAT proclamation. Hence, this kind of not having adequate understanding of the VAT laws create challenges on businesses communities to undertake their responsibilities as expected manner without any grievance.

#### 4.2.4 The replacement of VAT on sales tax

The Value Added Tax (VAT) proclamation No 285/2002 which has rescinded and replaced the sales and excise tax proclamation No. 68/1993 amended and which has come into implementation on January 1st, 2003 as a consumption tax which is imposed and paid as value added tax at a rate of 15% by the aims of increasing tax base and improving tax administration policies.

Comparing sales tax to Value Added Tax, sales tax is narrower because it is focused and limited only to sales transaction, manufactured goods and few selected services. Further, by its introduction, VAT has been more revenue generative than sales tax (Teferra, 2004).

With this respect the survey question were asked respondents,

Table 4.2.3 Do you think that the introduction of VAT in Ethiopia is necessary by replacing the sales tax?

	Frequency	Percent
Yes	99	52.1
No	23	12.1
I don't know	68	35.8
Total	190	100.0

Source own computed survey data, 2017

The result of above table states among respondents 99(52.1%) responded that yes, 23(12.1%) responded that no, 68(35.8%) responded that I don't know.

This reflects that most of the respondents agreed on the replacement of VAT on sales tax, if it applied in effective and according to VAT law to raise more revenue to the government even if some respondents said no and I don't know due to lack of adequate awareness on VAT laws and advantage of it.

#### 4.2.5 Beneficiaries of VAT revenue

VAT basically introduced in Ethiopia with the proclamation No 285/2002 to raise more revenue for the purpose of expanding the developmental projects for the increasing demand of public in addition to modernize the tax policies. After this VAT starts implementation with the agenda of from the public for the public, because it can collect from every one where ever and whenever he/she consume taxable product/service and the collected revenue uses to develop

public projects which demanded by public. In relation to this, to evaluate the business communities' view the survey question were asked respondents,

Table 8 4.2.5 Who do you think is the primary beneficiary of VAT?

	Frequency	Percent
Society	69	36.3
Government officials	121	63.7
Total	190	100.0

Source: Own computed survey data, 2017

On the above table from the total respondents, 69(36.3%) responded that society/public, 121(63.7%) respond that government officials. Since, the above data of respondents implied that most of the business communities think that the only beneficiaries is government officials from VAT revenue due to insufficient knowledge on the VAT and tax officials become rich as soon employed on the office in the town experience. The remaining respondents think that the ultimate beneficiaries are society if it implemented according to law.

#### **4.2.6 Main objective of VAT in Ethiopia**

Some of the major objectives of introducing the Value Added Tax by replacing the sales tax are to enhance saving and investment as it is a consumption tax and does not tax on capital and to enhance economic growth through brooding tax base and filling budget deficit to the increasing demand of public time to time.

To this view, the survey was conducted and respondents were asked to analyze the business enterprises views about the aim of VAT,



Table 9 4.2.6 In your understanding, what is the main aim/ intention of VAT implementation in Ethiopia and all other towns including Hosanna

	Frequency	Percent
Encouraging investment and export for foreign investors only	10	5.3
To generate adequate revenue for local public expenditure	41	21.6
To create consumption reduction by inflation of goods and services price	71	37.4
I have no clear idea about aim of VAT	68	35.8
Total	190	100.0

Source: Own computed survey data, 2017

Out of 190 respondents, 71(37.4%) replied that to create consumption reduction of customers by inflation of prices, 68(35.8%) replied that they have no clear idea on the aim of VAT, 41(21.6%) replied that to generate adequate revenue and the remaining 10(5.3%) replied that to encourage investment and export for foreign investors only.

From this study concludes that the majority of respondents have not clear and specified idea/understanding on VAT aim and its implementation. Since, some of them said to create inflation even majority of respondents 71(37.4%), some of them said to generate adequate revenue of government, some others for encouraging investment and export to foreigners and others clearly explained they are not clearly understand the basic objective of VAT implementation 68(35.8%). To this the tax authority is strictly expected to give close attention on the issue.

#### **4.2.7 The extent of VAT contribution to revenue by business communities' opinion**

Although the specific reasons for adopting the VAT differ from one country to another, the main argument is that a properly designed VAT raises more revenue with less administrative and economic costs than other broadly based taxes. Hence, money collected from taxes and custom duties is one of the major sources of the government revenue or finance.

The replacement main reason is to collect more revenue from the public by business enterprises on the behalf of government in every town in a legal manner. As expected VAT plays crucial

role on the revenue of each town from where it collected in particular and to the revenue of country in general. In this case the survey was conducted and question were asked respondents to assess their view on the contribution of VAT to the town revenue.

Table 4.2.7 In your opinion extent of VAT contribution for revenue generation of town as a VAT payers in the town

	Frequency	Percent
Very high	19	10.0
High	30	15.8
Average	65	34.2
Low	54	28.4
Very low	22	11.6
Total	190	100.0

Source: own computed survey data, 2017

From total respondent, 65(34.2%) responded that the contribution is on average, 54(28.4%) responded that the contribution is low, 30(15.8%) responded that the contribution is high, 22(11.6%) responded its contribution is very low and the remaining 19(10%) responded that its contribution is very high.

This indicates that majority of respondents(34.2%) the contribution of VAT to the revenue of town is on average level not much as expected, the other majority 28.4% said low contribution.

#### **4.2.8. The overall capacity and motivation of tax authority in controlling the VAT practice**

The Ethiopian Revenue and Customs Authority administer the Value Added Tax nationally as per the joint decision made by the house of representative and council of federation. Although VAT is administered centrally by ERCA, the revenue is shared between central and regional governments based up on the established revenue sharing organized with appropriate material and human resources.

The main tasks that must be performed by any branch office in charge of VAT are: identification and registrations of taxpayers, processing returns, controlling collections, making refunds, auditing taxpayers, investigation for tax frauds and evasion or levying

penalties. In order to administer these tasks, the branch office in charge has to be well organized and conduct publicity taxpayer’s education and information during the moment in time (Hailemariam, 2011).

The survey was conducted by asking the respondents whether the tax administration is strong enough to control non-registered and illegal activities of VAT payers.

Table 10 4.2.8 How do you rate the overall capacity and motivation of tax authority in controlling the practice of VAT in this town?

	Frequency	Percent
Excellent	16	8.4
Very good	33	17.4
Good	82	43.2
Very poor	59	31.1
Total	190	100.0

Source: Own computed survey data, 2017

Among the respondents, 82(43.2%) responded that good, 59(31.1%) responded that very poor, 33(17.4%) responded that very good and the remaining 16(8.4%) respond excellent.

This implies that in the side of tax authority has many weak sides in the town, as the result most of respondents are not well satisfied by the capacity and motivation of tax office employees of hosanna town and by this case they said well, the other majority of respondents’ feedback was very poor.

#### **4.2.9 Training about VAT on the town**

VAT (value added tax) introduced and adopted in Ethiopia with the proclamation No 285/2002 from already adopted and well-practiced sales tax in all business areas in Ethiopia.

Since, it is recent tax system and concept on the view of many business enterprises and whole public in the country, it needs strong regular training to the business enterprises, local public as well as capacity building to tax authority in order to administer effectively the implementation of VAT. In addition to this its proclamation has many exemption and procedure to register specified on the VAT law.

This all requires regular formal training and awareness creation to the public general and business communities in particular so as to generate expected revenue to the country's economic growth.

In relation to this, the questionnaire were asked respondents weather they got regular training from tax office as intended or not,

Table 4.2.9 Do you get training about VAT from tax officials in the town?

	Frequency	Percent
Yes regularly	20	10.5
Yes yearly at once	90	47.4
NO, never I got	80	42.1
Total	190	100.0

Source: own computed survey data, 2017

Among respondents, 90(47.4%) replied that yearly at once, 80(42.1%) replied that never they got and remaining 20(10.5%) responded they got regularly.

This reflects that even if the business communities need formal and regular training to the VAT collection and handling by fully understanding of VAT regulations there is insufficiency of training provided by the tax office as we seen from the above response.

Even some respondents responded that they never got necessary training about the value added tax such as how to register goods on the VAT machine when customers order to buy, how to collect VAT revenue and others.

#### **4.2.10 New business ventures willingness for VAT registration**

According to Article 17 of Ethiopian VAT proclamation 285/2002, a person who carries on taxable activity and is not required to be registered for VAT may voluntarily apply to the Tax Authority for such registration, if he regularly supplying or rendering at least 75% of his/her goods and services to registered persons. In addition to this, in the case of town many new business ventures are emerging to execute the business activity and to compete with the already existed business owners on the market. But in order to undertake any business activities and to compete in the market with others they have to register voluntarily or obligatory and pay government tax accordingly to be legal business enterprise in the town.

With respect to this, the survey question were asked to evaluate the existing VAT registered business communities view by considering the tax administration practice in the town,

Table 11 4.2.10 Do you think new business ventures starts business in this town willingly register for VAT application on their business?

	Frequency	Percent
Yes	27	14.2
No	100	52.6
I don't know	63	33.2
Total	190	100.0

Source: Own computed survey data, 2017

From the total respondents, 100(52.6%) responded that no on the current condition of town, 63(33.2%) responded that they don't know by thinking of they may or may not be, the remaining 27(14.2%) responded that yes they will register.

From this as observed on the table majority of respondents replied the emerging businesses will not register willingly unless and otherwise obligatory measures applied and the next majority replied they don't know.

This implies that in the town tax administration system has many problems in their practice and controlling of business communities.

#### **4.2.11 Business ventures being VAT registering for their business activity**

Now a days in the country any town has the more and more business enterprises emerging including Hosanna town to exploit the increasing demand opportunity in the market. This is a good news in one way to fulfil the market demand, but it creates strong competition with the existing legal business enterprises and interruption in the administration system of tax in another way. So, in order to generate more revenue to the government and to make themselves legal competent business in the market should register on the tax system.

With this regard respondents were asked their opinion weather they support other businesses registering for VAT or not.

Table 4.2.11 Do you support other business venture being VAT registering for business activity as of you?

	Frequency	Percent
Yes it helps to equal competition	111	58.4
No it create consumption reduction on our customers	79	41.6
Total	190	100.0

Source: Own computed survey data, 2017

Among respondents, 111(58.4%) replied that yes, it creates equal competition for us in the market, 79(41.6%) replied that no, it create consumption reduction on the customers.

This shows that every business enterprise weather it is already existed or newly emerged should register for equal competition in the market in one way and to collect VAT revenue on the behalf of government on another way as supported by respondents' response.

#### **4.2.12. VAT unregistered business enterprise who have to register in the town**

Under the VAT law of Ethiopia any person who carries a taxable activity and at the end of any period of 12 calendar months has made, during that period, taxable transactions the total value of which exceeds 500,000 Birr or at the beginning of any period of 12 calendar months there are reasonable grounds to expect that the total value of taxable transactions to be made by the person during the period will exceed 500,000 Birr, which adjusted recently 1000,000 Birr has the obligation to register for VAT (Article 16(1)(a) and (b)).

This is in order to raise sufficient government revenue and to broaden tax base to the economic growth of the country, all eligible businesses have to register for tax besides voluntarily registering business enterprises in the case of town. With respect to this, the survey questionnaires were asked the sampled respondents to analyze views of VAT registered businesses on this issue.

Table 12 4.2.12 Do you think that there are VAT unregistered business in your area?

	Frequency	Percent
Yes	99	52.1
No	48	25.3
I don't know	42	22.6
Total	190	100.0

Source: Own computed survey data, 2017

Among the respondents, 99(52.1%) reflected their idea that yes, whereas 48(25.3%) responded that no, and the remaining 42(22.1%) responded that they don't know clearly having or not having such kind of business enterprises in the town. From the above result study concluded that there are some business enterprises who are not still registered but have to register on VAT implementation on their business based on the majority of respondents' response 99(52.1%). This could be happen due to many reasons and can hamper the business activity of already registered tax payers in the town.

#### **4.2.13 Actions taken by tax authority on unregistered business enterprises**

Some of the shared authority and responsibility to ERCA; central, regional and zonal branch offices tax administration activities are identifying and register the taxpayers, controlling collection, processing returns, securing delinquent declarations and collection of tax arrears, making refunds, auditing taxpayers account, make different investigation to minimize and avoid tax fraud and evasion, and following up of tax office have to be revitalization measure taken in order for VAT to live up to the expectation as an efficient and fair source of country revenue.

From the above mentioned activities, identifying and registering any business ventures who have to register in the VAT implementation is one basic responsibility of tax officials in case of Hosanna town. In this case the questionnaires were asked the sampled business enterprises to know whether the tax officials take any action to make the unregistered business to be register,

Table 13 4.2.13 Is there any action taken by the tax officials on the unregistered business to make them registered on the VAT process?

	Frequency	Percent
Yes	15	7.9
No	100	52.6
I don't know	75	39.5
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents majority of them 100(52.6%) were respond no, whereas 75(39.5%) responded they don't know whether the action taken or not and the remaining 15(7.9%) responded yes. This the above data of respondents indicates that the action that must be taken to control such kind of unregistered business and to register, tax officials in the case of town were not taken, even if some actions has taken rarely it didn't adequate to control as expected based on the majority respondents 100(52.6%) view on the issue.

#### **4.2.14. The number of and skilled man power of tax office in the town**

ERCA established a separate VAT department in central, regional and other branch offices in the country, and organized with appropriate material and human resources. Human resource is basic and crucial one to accomplish every activities either government organizations or private organizations.

So to execute any activity as effective and efficient manner in any organization must fulfil the adequate and skilled manpower, especially on the tax offices in the country in general and in the town in particular.

With respect to this, the survey conducted and questionnaire were asked to investigate whether there have adequate number and skilled manpower in the tax office on the respondents view.



Table 4.2.14 In your opinion do you think that the Authority have adequate number of and skilled man power/ tax officials in the town to lead and control tax practice?

	Frequency	Percent
Yes they can lead an intended manner	80	42.1
No, because it has many challenges in implementation process	110	57.9
Total	190	100.0

Source: Own computed survey data, 2017

Among the respondents, 110(57.9%) were replied no, because it has unsolved many challenges, whereas the remaining 80(42.1%) responded that yes, they can lead the process as intended.

The above result shows that in the town tax office there have no adequate number and skilled man power on the tax office based on the majority respondents 110(57.9%) result computed.

#### **4.2.15 Declining the number of customers when business implement VAT**

VAT initially adopted in most of the countries in the world with the intention of raise more revenue to the country's economic growth and it leads to saving and investment on the side of low level of income who expends more than others. With this similar intention Ethiopia adopt it with the proclamation No 285/2002.

However Ethiopia categorized in low level of income in economic condition. Due to this reason, majority of people prefer low price product and in addition to this VAT introduced in the country recently, people of Ethiopia not understand as well the advantage and contribution to economic growth.

To this end the questionnaire were asked the sampled respondents, the extent of customer declining after application of VAT on their business.

Table 14 4.2.15 How much you faced/ noticed a decline in the number of your customers since your business implemented VAT?

	Frequency	Percent
Small change	28	14.7
Medium change	42	22.1
Significant change	93	48.9
No change	27	14.2
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents, 93(48.9%) replied that they faced significant amount, 42(22.1%) replied that they faced medium amount, 28(14.7%) replied that they faced small amount and the remaining 27(14.2%) replied that no change of customers.

From the above data study concluded that local communities of town are price sensitive and after application of VAT on their business, business enterprises face significant amount declining of their customers by depending majority respondents 93(48.9%) result.

#### **4.2.16 Collection of VAT from final users**

As Ethiopian VAT law, VAT is collected at every stage where value added on goods and service and transaction takes place, but the collectors of VAT must be registered and legal business entity besides of this, the way of collection must be in a legal manner.

So as to avoid any tax evasion by business community the collection method must be legally published/sealed receipt or cash register machine. According to this, the questionnaire were asked the respondents during the collection what legal material they use to collect VAT.

Table 15 4.2.16 How do you settle/collect Vat during delivery/providing goods and services for final users?

	Frequency	Percent
Cash register machine	120	63.2
Manual Receipt	70	36.8
Total	190	100.0

Source: Own computed survey data, 2017

Out of 190 respondents, 120 (63.2%) responded that they use cash register machine whereas 70(36.8%) responded that they use manual receipt.

This implies that majority of business owners/ majority of respondents 120(63.2%) in the town uses cash register machine and few business enterprises uses receipt during collection of VAT. But as possible as it is better to use all business community cash register machine on their business activity.

#### **4.2.17 Payment or reporting VAT to tax authority**

Since the government’s main source of revenue is money collected from taxpayers, the system using to collect this money needs to be effective and efficient in assessing and collecting mechanisms.

Voluntary compliance needs timely filing and reporting of the required tax information and the timely payment of those taxes without any reminder.

In addition to this in order to carryout expected responsibility from any registered business community and to play important role in raising government revenue every business have to report or pay the collected VAT without any delinquency.

By this case the respondents were asked whether they report VAT on time or not to tax authority.

Table 4.2.17 As a responsible business man you always pay VAT to tax authority on time and as expected?

	Frequency	Percent
Yes always	95	50.0
rarely	74	38.9
No, never	21	11.1
Total	190	100.0

Source: Own computed survey data, 2017

From the total sample, 95(50%) responded that yes always, 74(38.9%) responded rarely and the remaining 21(11.1%) responded that never they report on time.

The above result indicates that majority of registered business community/ respondents 95(50%) report or pay VAT according to the VAT law of the country even if some others pay VAT rarely on time to the tax authority in the town experience. This requires government and

tax officials' closer attention and corrective action on the remaining tax payers in order to collect expected amount on time.

#### **4.2.18. Reward and recognition certificate of tax authority to honest VAT payers**

As every citizen of Ethiopia has rights to exercise as the same time obligation/ duty to respect briefly mentioned in the countries mother law/ constitution. According to Ethiopian VAT law stated every eligible registered business enterprise has responsibility and obligation of paying VAT to tax authority for respected tax office who belongs.

This is expected from legal responsible business, however VAT is recent phenomenon in the case of country and for all its towns' business communities. Therefore, till to all business enterprises well understand handling of VAT on their business and fully exercise their expected responsibility by paying necessary tax on time to the government, the tax authority should motivate them by giving reward and recognition associated with continues training when they pay according to VAT law.

This creates them more confident on their responsibility and feeling of good behavior, more over it initiates other business enterprises for this responsibility.

According to this, to evaluate the town practice on this issue questionnaire were asked respondents whether they got or not,

Table 16 4.2.18 When you pay VAT honestly to the tax authority, do you get necessary recognition and reward from the authority?

	Frequency	Percent
Yes	64	33.7
No	126	66.3
Total	190	100.0

Source: Own computed survey data, 2017

Among respondents, 126(66.3%) replied that no, they never got, whereas 64(33.7%) replied that yes, when they start implementation of VAT in this town. The computed result implies that there is no such kind of motivation of business community in the town currently based on

majority respondents 126(66.3%) result even if based on the others remaining response it had rarely before a long period of time.

#### **4.2.19 Satisfaction of business community on their business after application of VAT**

Happiness/ satisfaction on a given activity creates or motivates that person to do more that activity. In the case of town there are many business communities some are registered and some others are unregistered to VAT.

To the significance of this study the researcher were asked respondents,

Table 4.2.19 Are you happy on your business activity when you undertake with VAT?

	Frequency	Percent
Yes	49	25.8
No	141	74.2
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents, 141(74.2%) responded that no, they are not happy on their business and the remaining 49(25.8%) responded yes, they are happy on their business.

Based on the majority response the result shows that most of the business community are not happy on their business activity after the implementation of VAT on business.

The few other respondents 49(25.8%) said that they are satisfied or happy on their business activity even after the implementation of VAT (value added tax) on the business.

#### **4.2.20 The single rate (15%) VAT policy in Ethiopia**

Ethiopia is applied to be a member of World Trade Organization (WTO) that demands the country to reduce other tariffs that has a direct effect on the total revenue. Therefore, Ethiopia forced to work hard to increase and make efficient the VAT system in order to compensate other tariff reductions.

According to the VAT proclamation of Ethiopia, introduced in January 1st, 2003, VAT is payable and would be levied at the rate of 15% if: the supplies are made in Ethiopia, made by a taxable person, made in the course or furtherance of a business and are not specifically exempted from tax or zero charged.

However many business traders, as well as the majority of the people complained about the high rate of VAT. However, it should be noted in this regard that the Ethiopian rate of 15 percent is not excessive by international standards and is in fact, fairly typical of VAT rates around the world.

VAT with this single rate plays crucial role in increasing revenue of the country more than other taxes, because it can collect from every one. With regard to this, the questionnaire were asked whether they support or not the adopted single rate,

Table 17 4.2.20 Do you support a single rate (15%) VAT policy on all the goods and services?

	Frequency	Percent
Yes	115	60.5
No	75	39.5
Total	190	100.0

Source: own computed survey data, 2017

Among the respondents, 115(60.5%) reflected their idea that they support, whereas 75(39.5%) replied that not support the single rate. The computed result shows that most of the business community support the single rate VAT in the town and the remaining few respondents doesn't support single rate VAT on their business in the town.

#### **4.2.21 Issuing practice of receipt to consumers in the case of town**

As per the VAT proclamation, according to article 22(1), a person registered for VAT that carries out a taxable transaction is required to issue a VAT invoice to the person who receives the goods or services. A person who is not registered for VAT does not have the right to issue a tax invoice.

But registered business traders are expected to issue VAT receipts to all buyers without fail and depositing collected amount to the government account every month. This is actually, an indication how the business community well understood the VAT proclamation to put into practice.

As a responsible registered business enterprise this is obligation to issue the receipt either by legal cash registration machine or legal manual sealed form and every customer or purchaser

has the responsibility to ask and receive the receipt of the purchased product so as to avoid evasion of tax by business communities intentionally.

But this is really practiced in the town in terms of business communities issuing receipt and in terms of final users asking the receipt? To check and analyze this, the respondents of the study asked when they issue receipt to customers,

Table 18 4.2.21 When do you issue the receipt to the customer in your business activity?

	Frequency	Percent
With the product/service they ordered	72	37.9
When they ask to pay	118	62.1
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents, 118(62.1%) replied that they issue receipt when after the asking of customers to pay, whereas the remaining 72(37.9%) replied that they issue receipt when the customers ordered the product/service. This reflects that majority of respondents or business enterprises issue receipt when the customers ask the receipt unless and otherwise they don't have willing to issue, but few business enterprises issue when the order is ordered based on the computed above response.

#### **4.2.22 Registration of business on VAT process for the first time in case of town**

According to Article 16(1) (a) and (b) of Ethiopian VAT law any person who carries on a taxable activity and at the end of any period of 12 calendar months has made, during that period, taxable transactions the total value of which exceeds 500,000 Birr or at the beginning of any period of 12 calendar months there are reasonable grounds to expect that the total value of taxable transactions to be made by the person during the period will exceed 500,000 Birr, has the obligation to register for VAT.

With this respect respondent were asked whether the above mentioned criteria for registration of any business evaluated critically by the tax authority during their registration on VAT in the case of town or not.

Table 19 4.2.22 During your registration time, how you/ your business registered on VAT?

	Frequency	Percent
After evaluation of my business by tax authority in terms of market place and minimum threshold level i.e (500,000)	30	15.8
When similar businesses are registered	68	35.8
By the decision of tax authority without any criteria	92	48.4
Total	190	100.0

Source: own computed survey data, 2017

Among the respondents, 68(35.8%) responded that they are registered by the simple decision of tax officials in the town without any criteria evaluation, 92(48.4%) responded that they are registered when tax officials decide as similar businesses registered and the remaining 30(15.8%) responded that they registered after the evaluation registration criteria of their business by tax officials.

This reflects that in the case of town majority of business enterprises registered by the simple decision of tax officials if the similar business activities in the area registered, without any registration criteria due to their carelessness of responsibility.

#### **4.2.23 The threshold level of businesses registration for VAT**

In Ethiopian VAT law according to proclamation No 285/2002, article 16 (1) (a) and (b) were any business person who undertake taxable transactions the total value of which exceeds 500,000 Ethiopian Birr decided must be register and pay VAT to generate more revenue and to make inclusive taxation of most business community.

But currently it is adjusted by considering current purchasing power of birr to a minimum threshold level 1000,000 Ethiopian birr to the obligation of any business enterprise registration on VAT.

According to this by conducting the survey, questionnaire were asked sampled respondents of business community to analyze their views on this adjusted minimum threshold level,



Table 4.2.23 Do you think the adjusted VAT minimum threshold level 1000,000 is reasonable to generate expected revenue in the town?

	Frequency	Percent
Yes	76	40.0
No	114	60.0
Total	190	100.0

Source: Own computed survey data, 2017

Among respondents, 114(60%) replied that no, it is not reasonable/ necessary in the case of town, whereas 76(40%) replied that yes, it is reasonable by considering current condition of economy.

From this result it concluded that majority of business community 114(60%) were not agreed on the adjusted threshold level because of by considering business competition and it doesn't incorporate all business enterprises those are actively compete in the market but are not registered for VAT by this higher level of the threshold. It affects only those few and honest business enterprises whose annual returns is  $\geq 1000,000$  birr, there are few business enterprises whose annual turnover  $> 1000,000$  birr in case of town as compered by other cities.

#### **4.2.24 The process of VAT registration of business community when the registration time.**

Business activity needs effective use of time and availability within the business, because they don't know when their customers came to purchase and their competitors' effective use of time negatively affects their business in the market competition. Therefore they strongly need effective and fast service from tax authority without any delay and interruption of their working time during their registration on VAT.

With regard to this to investigate the town's practice of registration process the survey questionnaire were asked whether the VAT registration process is easy and fast as business community need or not.

Table 20 4.2.24 Do you believe that the process of VAT registration is smooth and easy for taxpayers?

	Frequency	Percent
Yes	70	36.8
No	120	63.2
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents, 120(63.2%) responded that no, the process is not easy and fast as expected for us, whereas 70(36.8%) responded that yes, the process is fast during registration time. This computed result states that during registration on VAT majority of business community are challenged and still challenging due to many reasons in the case of town by depending most respondents' response 120(63.2%).

It needs higher tax officials critical and closer attention to solve the business communities complaining problems on this process and to improve the system.

### **2.2.25 VAT refunding or rebating process in case of town**

In Ethiopian VAT law, according to Article 27(1) If at least 25 percent of the value of a registered person's taxable transactions for the accounting period is taxed at a zero rate, the tax authority will refund the amount of VAT applied as a credit in excess of the amount of VAT charged for the accounting period within a period of two months after the registered person files an application for refund, accompanied by documentary proof of payment of the excess amount.

(Article 27 (2)) Where the tax authority is satisfied that a person who has made an application for refund has overpaid tax, the tax authority shall first apply the amount of the excess in reduction of any tax, levy, interest, or penalty payable by the person under the VAT proclamation, the customs proclamation, the income tax proclamation, or the sales and excise tax proclamation and then repay any amount remaining to the person if the amount to be refunded is more than 50 Birr.

According to this, the questionnaire were asked respondents whether VAT refunding/rebating being made on time according to law or not,

Table 21 4.2.25 Do you think that the VAT refunding processes being made in case of Hosanna town are on time and effectively?

	Frequency	Percent
Always	31	16.3
Rarely	58	30.5
Never	101	53.2
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents, 101(53.2%) replied never refunded in case of town, 58(30.5%) replied that rarely after a much dealing and the remaining 31(16.3%) replied as they got refund according to law. This indicates that based on majority response 101(53.2%) refunding VAT never applied even refunding condition fulfilled on their business even if few respondents respond they got refund always and rarely.

#### **4.2.26 Customers or local communities' willingness to purchase product with VAT**

In its introduction VAT was mainly required to generate high amount of revenue for the countries developmental expenditures through collection from every individual when he/she consume the taxable product.

But in case of Ethiopia for the public there is no sufficient knowledge on the importance and main intention of VAT to willingly participate and purchase any product with VAT.

This is basic condition on the hosanna town general public or consumers' attitude about the VAT implementation. In case of this, the respondents were asked whether the customers or local public are not willing to purchase goods and services with VAT or not,

Table 22 4.2.26 Are there customers who are not willing to purchase goods and services with VAT?

	Frequency	Percent
Yes	98	51.6
No	76	40.0
I don't know	16	8.4
Total	190	100.0

Source: Own computed survey data, 2017

Among respondents, 98(51.6%) replied that yes, the local society are not willing to purchase with VAT by thinking of VAT raises the price of product they need, 76(40%) replied that no, the local communities are willingly purchase with VAT and the remaining 16(8.4%) replied that they don't know the willingness of local society.

This shows that local communities of the town were not well aware of aim and importance of VAT and because of this they are not willing to purchase with VAT based on the majority 98(51.6%) response.

#### **4.2.27 Competition of VAT registered business enterprise and non VAT registered business.**

The introduction of VAT has been perceived by registered and non-registered businesses as having a number of negative impacts. The most significant of these are unfair competition and additional costs to record keeping, training and hiring external professionals to handle VAT collection. By the experience of town there are many business enterprises and they are increasing time to time even though the registered business enterprises are few in number and most of them are unregistered on VAT.

In relation to this the questionnaire were asked their opinion based on the market competition,

Table 23 4.2.27 Do you think that the non-VAT registered taxpayers are more benefited than those of VAT registered enterprises from the competition in the market?

	Frequency	Percent
Yes	110	57.9
No	22	11.6
I have no idea	58	30.5
Total	190	100.0

Source: Own computed survey data, 2017

Among them, 110(57.9%) responded that non- VAT registered businesses are more benefited, 58(30.5%) responded that they don't know whom benefited more from competition and 22(11.6%) responded that the registered businesses benefited more from the competition.

The survey result shows that non-registered businesses are more benefited by attraction of more customers than the registered one from market competition based on the majority respondents view 110(57.9%) in case of town experience.

**Table 4.2.28 Problems of VAT administration that needs improvement**

VAT is recent concept this means not well practiced tax system in Ethiopia for a long period of time in the zonal towns and local public. Because of this reason it may have many problems on its implementation to collect more revenue in the side of tax officials, business community and general public who consume good and service.

In order to check this by the conducted survey the questionnaire were asked respondents,

Table 24 4.2.28 Are there problems in the VAT administration that needs to be improvement in this town?

	Frequency	Percent
Yes	99	52.1
No	38	20.0
I don't know	53	27.9
Total	190	100.0

Source: Own computed survey data, 2017

From total respondents, 99(52.1%) replied that there are many problems in its implementation and controlling, 53(27.9%) replied that they don't know whether having or not having the problems and remaining 38(20%) replied that there are no problem on VAT administration. The result implies that there are many problems of VAT administration on its implementation that need improvement based on the majority 99(52.1%) response in case of town.

### **4.3 Analysis of open indeed questionnaires and interview**

For the purpose of cross checking and analyzing consistency of response from the business community and tax office employees the same questions provided to tax administration officials by means of interview and blank space to fill by own words and understanding by registered business communities.

#### **4.3.1 VAT refunding/ rebating process of Hosanna town tax administration:**

When the business communities face the input tax/VAT exceed output VAT, they apply to the tax office by fulfilling criteria stated on VAT law, but the tax office do not respond or not accomplish the repayment on time by raising many unnecessary questions, again and again checking our file, by another day appointment, on the appointed day they also create new question and by others; they don't serve VAT registered business community as expected according to Article 27(1). This all creates crises and delay on their business in the case of town based on the majority respondents opinion.

Interviewed tax officials to this issue raised that this kind of problems really happening due to not only tax official weakness but also the applicants for VAT repayment sometimes intentionally made by over stating purchase and under stating sales, miss- statement their financial statement and by others they tried to refund the VAT, by this case critical evaluation and identification of their files is essential according to (Article 27 (2)). By this and work overload in the office they cannot serve the business community as expected.

#### **4.3.2 Non- registered business community/enterprise for VAT**

There are some unregistered business community who have to register for VAT and those can create strife competition with registered businesses in the town.

According to current condition of local communities' attitude VAT creates inflation and negatively affect their purchasing power, they always search low price products and want

purchase anything from such kind of business enterprises. This is a good opportunities for VAT unregistered business enterprises, because they can attract many customers from the market and can transact their business quickly. By this case, the registered businesses couldn't compete with those unregistered business. This is a big problem in fair competition on the business activity and to collect VAT revenue for the development of town as well as country, based on a majority response.

The tax officials were address similarly with registered business respondents, having unregistered business communities in the town and it is one challenge to collect VAT revenue as expected. This is due to by hoarding product from shop in other place, time to time address changing and by other cases during estimation and registering.

From this it can concluded there was a negative attitude on unregistered businesses about VAT and needs awareness creation for both business community and general public in the area.

#### **4.3.3 Tax /VAT evasion practice and remedial measures by tax office**

According to Ethiopian tax law Tax Evasion means a person who evades the declaration or payment of tax, or a person who, with the intention to defraud the government; applies for a refund he is not entitled to, commits an offence and, in addition to any penalty under Section, may be prosecuted and, on conviction, be subject to a term of imprisonment of not less than five (5) years.

In this case the questionnaire were asked respondents to reflect their opinion freely on the provided sheet. Majority of business community explained as even if tax evasion is crime according to tax law, some business enterprise/community intentionally try to evade tax by thinking of becoming rich and leader in business activity as of every business enterprises wish, but sometimes this evasion may be made unintentionally by simple mistake like by registration of product on the machine, calculation of the VAT rate, making of financial statement and by others factors in its handling process.

This is due to lack of sufficient awareness and skill on how to process it effectively and it leads us to huge penalties in birr, imprisonment and up to shutting of our business by tax office.

The remedial measures for this, the first one is providing strong regular training and awareness creation of how to handle the general VAT revenue till to report for tax authority.

After this if the evasion is tried to make by business enterprise giving be careful announcement as immediately and if beyond from this take a balanced penalties for the crime he/she made

according to the tax law. But in the case of town if such kind of crime made even unintentionally and by mistake the tax office eager to penalize by their simple decision without any consideration on the issue based on the majority opinion.

However in the side of tax office explanation in the town some business communities trying to evade tax most of the time intentionally due to this reason they are taking immediate corrective action associated with training according to the law. This implies that there are selfishness problems in the side of some business community and administration weakness in the side of tax officials especially in the town experience.

#### **4.3.4 VAT administration problems in the town**

In principle, VAT is collected from consumption of goods and services. Like it has been observed in many developing countries, VAT implementation in Ethiopia has faced different problems till to date.

Problems that are observed during the implementation of VAT related with both tax officials and business enterprises. With regarding to this the respondents were asked their opinion on the problems in the side of tax officials, they mention many problems:

for the tax office itself has no adequate number of employees and are not well skilled on the tax issue, they have tendency of rent seeking/ corruption feeling, not giving equal and fair treatment to all business communities, deficiency of materials to serve business enterprises as effectively and efficiently, carelessness on their responsibility and punctuality, tendency of penalizing the business community in any mistake, not providing training and follow-up of either registered or unregistered businesses, not implementing of collected revenue from any tax including VAT to the development of town and others.

The problems in the side of whole business community and local public as explained by tax office: the implementation of VAT in this town is not an easy task, because existence of eligible business entities that have not yet registered for VAT by hoarding the goods from estimation and address changing time to time, existence of some VAT registered business enterprises that have collected the tax with not issuing VAT invoice/ receipt, the presence of taxpayers that did not declare the tax they collected as per the law, low level of tax awareness of the local community, provisions of miss- statement file application to VAT refund, as well as the lower level of the purchasing power of the community which increases the needs of searching goods and services that excludes VAT value from its prices.



From this study concluded that in an effective implementation of VAT in the town there are many challenges those needs to improvement in the side of tax office, business community as well as in the side of general public based on the majority opinion.

#### **4.3.5 Generally in order to improve VAT administration and to maximize revenue of town what activities should be done?**

The country's economic development issue is not the only responsibility of tax officials, business communities and local consumers of goods and services, but it is the responsibility of all in an inclusive manner. Because those all are beneficiary from the country's development fruits when its economic growth become increase.

In relation to this business community's opinion to improve VAT administration and to maximize VAT revenue: tax authority have to be free of rent seeking activity/ corruption, broaden fair system of tax administration, treating all business community equally without any bias, providing training and advise on the VAT handling as expected for registered businesses, registering and strongly follow-up unregistered business enterprises, conducting developmental projects by collected tax revenue that motivates all society, conducting research on the issue of VAT to gather business communities and local society views on different parts of country and adjusting policies accordingly, all registered business have to pay VAT revenue transparently and responsibly to tax authority, the local community have to change negative attitude on the tax.

Similarly tax office employees stated: all are should be exercise their responsibility as a citizen according to tax law without expectation of tax office, unregistered business enterprises should came voluntarily to register, registered business should report VAT on time without any fail, they should abstain from falsification of files to apply VAT refund, local communities should transact with VAT, government should provide materials as per business enterprises requirement.

## **CHAPTER- FIVE**

### **MAJOR FINDING, CONCLUSION AND RECOMMENDATION**

#### **5.1 Major finding from analysis of questionnaires and interview**

##### **❖ Knowledge of business community on VAT regulations and proclamation**

Knowing or understanding the rules and regulations of the countries as well as tax laws, especially VAT proclamation helps any citizen to exercise his/ her rights and responsibility according to the law. But in the case of town some business communities/enterprises heard about VAT for the first through media, other business competitors, moreover the continues training never provided by tax officials , as the result of this most of the business community are found not fully aware of all VAT proclamations and regulations to adhere for it.

- ❖ As its introduction to generate more revenue from general consumption and at each stage where value added, VAT is necessary in replacement of sales tax as found from the analysis.
- ❖ VAT is collected from all consumption of taxable products to the benefit of country's development, but the major beneficiaries of VAT revenue is only tax officials as found respondents view. For this kind of thinking the tax administration problems and awareness level VAT proclamation of business community play an important role.
- ❖ To accomplish the assigned responsibility on a specific office it must be fulfilled with adequate number of employees, well skilled on the issue, necessary materials and employees' capacity and motivation is necessary to lead the tax implementation effectively. But these are not fulfilled in terms of skilled manpower, materials even the hired employees motivation to their responsibility is not well as expected in the town as found respondents view.

##### **❖ VAT registration problems in the town**

Sometimes VAT registration decided by tax office simply based on the similar business in the town, without any estimation of annual turnover according to article 16(1). But after their decision the process of registration is not easy as they decide, there is a gap/ delay on the

publishing legal certificate, providing cash register machine or legal sealed form as a result of this new business willingness to registration is negative as the registered respondents view.

#### ❖ **VAT collection practice**

According to Ethiopian VAT proclamation, fifteen percent (15%) of VAT from taxable products transaction collected to government revenue. It is collected from consumers by VAT invoice/receipt and the registered businesses have to report /pay quarterly in a year or in every third month the deposited amount to the tax authority. In case of town some business enterprises uses manual receipt, this is more vulnerable to evasion and some are uses cash register machine, however by either of them the issuing practice of VAT invoice with the order of customer is very less in the side of business communities and asking of receipt not well practiced in the side of local consumers.

Many taxpayers lack skills to provide accurate information on total sales, especially related to VAT and this all contributes to tax evasion in addition to business communities' selfishness. Due to these reason VAT is not collected as expected amount and on time to the town revenue.

#### ❖ **Local communities view about VAT**

Ethiopia categorized in low level of income in economic condition. Due to this reason, majority of people prefer low price product from the market.

More over local people are not well understand about the VAT advantage and its contribution to economic development of the country, due to this they looks low price of products from unregistered business enterprise to save VAT amount. In addition, the outcomes of the research shows lack of tax awareness among the society and strong education programs as well as lack of trust between taxpayers and administrators as major challenges to the VAT system in the town.

#### ❖ **VAT unregistered businesses**

In the case of town there are some unregistered business communities those can compete equally with registered businesses in any countries developmental fruits and government benefits like bid without any differentiation, but those can benefit more from the negative view of local communities on the VAT by reducing price of the product VAT amount. But to register them and to create equal competition there is no strong follow-up and corrective action taken by the tax office.

### ❖ VAT administration problems

A good VAT administration is critical in fully implementing tax and reducing gaps between the effective taxation and what it is supposed to be in the proclamation. In general, a good VAT administration is important to achieve the policy objectives of a government

But in case of town, some identified weaknesses of tax authority are:

- ✓ Weaknesses in its intelligence unit in identifying those not issuing VAT receipts and not getting registered as VAT payers after fulfilling the Birr 500,000 annual turnover, affects the tax collection rate.
- ✓ Relies heavily on thinking of revenge when simple mistake made on coercion, penalties and imprisonment rather than giving training for transgression which the VAT payers of both complying and not complying are very much frightened off.
- ✓ VAT refunds are legally mandated to be made within a period of 90 days. However, VAT refunds are mostly carried over from one tax year to the other when it happens.
- ✓ Unfair treatment of all business enterprises and even registered ones, weakness of awareness creation to the general public, rent seeking tendency, unpunctual behavior of tax office employees.....etc.

## 5.2 Conclusion

It is obvious that an economic development of a country can be certain by an effective and efficient administration and collection of taxes. Taxes can be classified as direct and indirect taxes. VAT is one of the indirect taxes levied on consumption where the value of goods and services increases as they charge hands in course of production, distribution and final sales to the consumer.

A good tax system should have one or a combination of desirable characteristics as economic efficiency, administrative simplicity, flexibility, political accountability and fairness for the purpose of good tax system. This is so because, when the implementation and administration of tax system is effective, the government's revenue that helps to fulfill the socioeconomic needs of the society will be amplified. It is possible to say that the major function of taxation is to marshal the necessary funds to finance the increasingly expanding level of public expenditures.

The government of Ethiopia has introduced VAT on January 1, 2003 replacing the sales tax aiming to raise more revenue, modernize its tax administration and encourage investment and

trades. The rate of VAT is uniform and the scope of exemption under this tax is limited and it is applied at each stage of production and distribution i.e. whenever additional value is added the tax is applied.

VAT in Ethiopia could be helpful in simplifying and modernizing the tax administration with its invoice based characteristics and its requirements for the registrants to hold a systematic book of accounting. Economically, VAT does encourage investment by providing a refund for a tax paid on inputs and encourage export by zero rating items exported.

In Ethiopia, the implementation of VAT which is a new and sophisticated tax that differs significantly from the well familiar tax schemes with the formerly existed taxes is not an easy task. Hence, various misunderstanding regarding its objective, its application, and its benefit to the national economy and its advantage to simplify the tax administration system were normal and due to this local communities, business enterprises have negative thinking in its application.

These misunderstandings initiates the researcher to think about the gap of the Value added tax implementation practice and the challenges it is encountering. Accordingly a survey was conducted with the objective to identify, asses and analyze the implementation problems, local consumers feeling and business communities view of VAT by distributing questionnaires for sampled respondents and data gathered from VAT registered taxpayers and employees of Hosanna town tax office.

Based on the results of the data findings, VAT implementation has faced different problems by the side of tax authority, registered and unregistered business community and local consumers/public when it comes to the ground. The major once are: administration inefficiency to control noncompliance taxpayers, lack of responsible taxpayers, existence of unwilling enterprises to register for VAT, existence of unwilling customers to buy goods and services priced with VAT, the authority's weak follow-ups and controlling mechanisms against those taxpayers registered but doesn't use proper VAT invoices, inability of the authority to render quality services.

The main causes for these problems were raised from lack of awareness and deliberate resistance not to comply with the VAT laws of the business community, absence of sufficient materials and skilled manpower, the negative attitudes of some business societies towards

VAT, weak purchasing powers of the society forcing them to search goods and services without VAT.

Identifying taxpayers, assessment on VAT execution (includes identifying taxpayers and tax evades as well as the registered and unregistered taxpayers among the business communities), processing returns, controlling collections, making refunds, auditing taxpayers, and levying penalties are the major activities in VAT administration.

However, due to the absence of sufficient and skilled manpower in the office, there is a gap on accomplishing these responsibility.

Based on the results of the survey the authority has taken legal measures focuses more on unbalanced penalizing noncompliance business communities to the VAT law either it made intentionally or unintentionally rather than giving training for them in the case of town.

To overcome the all identified obstacles for the effective implementations of VAT in the town, the local public at large and the government specially tax authority should have to create alliance to work together to increase the taxpaying habits of the business community and society. Since, the ultimate goal of tax specifically VAT is to collect sufficient amounts of money that significantly be able to help the government to finance social and economic development and reduce poverty.

### **5.3 Recommendation**

Recommendation is a possible insight or suggestion given to the specific issue or identified problems for the future improvement. Accordingly, the researcher forwarded the following suggestion to the identified problems in the implementation practice of VAT in case of hosanna town.

#### **➤ Recommendations forwarded to the tax office in the town**

Since a poorly administered VAT raises less revenue for the town as well as to the country that can change the nature of the tax resulting in unintended economic distortions.

Therefore tax office has to build its administration capacity on both human and material resources to carry out its duties and responsibilities effectively and efficiently.

This can be maintained through hiring of more qualified employees, provision of consistent training and development for staffs who will join and who have joined.

Tax office has to strength the administration capacity to control noncompliance and tendency of evasion of tax payers by selfishness.

Tax office should be free from rent seeking/corruption feeling and unfair treatment of even registered business community.

The present system whereby taxpayers are subject to stiff penalties for even minor errors, but that mistakes by taxpayers should be corrected by providing deep training for every tax system and consultancy on their business activity rather than penalizing. While office of tax employees suffers no sanction for equivalent errors and corruption is patently unfair, to this government should give close attention on controlling them.

In order to educate and motivate the tax payers, tax office should differentiate those honest business community to give priority in any government benefits like bid, facilitating investment opportunities and recognition certificate and reward when they pay tax honestly.

They should be punctual on working time and give priority to serve the customers as intended. The tax office should implement fully as possible as the collected tax revenue for the development of town because there are many problems of infrastructures like road, pumped water supply, town's beauty, social services and electricity. Electricity specially interrupt business activity during issuing the VAT receipt, because electricity infrequently interrupt in the town.

When penalizing those noncompliance businesses they should not think as a revenge but they should penalize balanced penalty and it should be by only birr without any long period imprisonment, this is due to by considering the fined birr amount help to tax authority revenue maximization and for economic development on one way and by considering closed business serve many local customers demand and the business owner dependent family as most business community's view.

The current adjusted threshold level of VAT registration should be readjusted since it collected from public only 15% based on the business communities' opinion to make inclusive tax of most businesses and broaden tax base, because currently in the town only few business enterprises are on position of this threshold. But before adjustment it should be researched in different parts in the country to collect opinion of majority on this issue.

For the effective service and to capacity development tax office should provide suggestion box in office to collect customers feeling on their activity.

For the effective implementation and collection of more revenue from the general public, tax office has to conduct strong education campaign and awareness creation for general public

through media like TV, Radio, especially FM, the best opportunity for this is recently established Hosanna FM 95.3 to disseminate information and awareness creation about objectives of VAT and to announce for registered business reporting deadline.

➤ **Recommendation forwarded to registered business communities**

In addition to the tasks performed by the tax authority, the business communities should also obey the current VAT rules and regulations, develop the culture of taxpaying as a sign of modernization, pay attentions towards the government's effort to collect and fund the long run projects carrying out all through the country.

Consider paying tax as a means of directly or indirectly putting one's own contribution to change the life of each citizen and they perform their activities according to the current VAT laws as well as start to work in cooperation with the authority in fighting against those enterprises that are violating the rules and regulations of VAT.

They should be free of selfishness thinking by evading tax and should responsibly and transparently issuing VAT receipt to all customers when transaction takes place on their business.

They should keep record and report/ pay VAT revenue genuinely to the tax office on time.

➤ **Recommendation forwarded to the general public**

There is a strong believe that well-informed local public/ society can be considered as an important asset for the tax authority.

Therefore all the society should avoid such negative thinking of VAT create inflation and looking unregistered business enterprise for purchasing goods and service, even though their economic level restrain them.

They should motivated to purchase goods and service with VAT since it collected from every society a little only 15%, but after collection from many society it became huge amount and help for socio-economic development to the all in the town.

They should also develop asking VAT receipt when they order goods and services and after consumption destroying it.



## **5.4 Future Research Implication**

Tax is a main source of government revenue in any developing and developed countries for any developmental projects and for public expenditure.

Therefore it should be implemented and effectively and efficiently collect without any delinquency from liable person to the government. However for this effective implementation it is necessary to have good tax policy, good tax administration system and informed and responsible society in the country.

For all of these good tax policy, tax administration system and responsible society it needs to research time to time for the evaluation of policy implementation, identification of challenges and assesses of societies' perception on a specific issue to the improvement for the future.

Accordingly this thesis conducted only on limited issues of Value added tax implementation practice and didn't collect idea from local public. So, the future researches should conduct on the general public perception about VAT, should analyze and evaluate the auditing practice of VAT and should conduct in different parts of country on the adjusted threshold level.

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# **APPENDIX -I**

## **Jimma University**

### **College of business and economics Graduate studies**

#### **MPM program in the department of public management.**

Appendix 1: Questionnaires for VAT registered taxpayers

Dear participants:

You are kindly requested to participate in a survey study that aims to assess VAT implementation practice which incorporates collection method, administration system and viewpoints of business communities and general public in case of Hosanna town. In addition to these identifying basic challenges in the side of tax authority and business community and providing possible solutions to overcome these problems. This can be achieved only by your active participation and cooperation by providing necessary information and suggestion. Therefore, I respectfully request your kind cooperation in answering the following questionnaires of the study. When you fill the questionnaires, I want to assure your response will be highly confidential.

Thank you in advance for your kind cooperation!!

Demographic information/ profile

Answer by putting an ex (X) in one of the blank spaces corresponding to 1-3 questions for others fill that belongs you.

1. Age (in year): 20-30 \_\_\_\_\_, 30-40 \_\_\_\_\_, 40-50 \_\_\_\_\_, 50+ \_\_\_\_\_

2. Gender: Male \_\_\_\_\_, Female \_\_\_\_\_

3. Educational achievement/level: 12 grade and below \_\_\_\_\_, certificate \_\_\_\_\_, diploma \_\_\_\_\_, bachelor degree \_\_\_\_\_, masters and above \_\_\_\_\_

4. Type of the business/unit \_\_\_\_\_

5. Your status/position in the unit/business \_\_\_\_\_

6. Year of experience in the specific business units \_\_\_\_\_

Section II: Questions related to the study



Choose the best answer from the given alternatives by your opinion and circle on it, for other questions please provide your answers on your own words.

1. How did you hear about VAT and its implementation for the first time?

A/ Government training B/ Media C/ Neither of them but from my business competitors

2/ As a taxpayer, do you think that you/your organization are well aware of all the VAT proclamations and regulations?

A) Yes B) To some extent C) Not aware

3/Do you think that the introduction of VAT in Ethiopia is necessary by replacing the sales tax? A) Yes B) No C) I don't know

4/ Who do you think is the primary beneficiary of VAT revenue?

A) Society B) Gov.t officials

5/ In your understanding what is the main aim/ intention of VAT implementation in Ethiopia and all other towns including Hosanna?

- A) To Encouraging investment and export for foreign investors only
- B) To generate adequate revenue for local public expenditure
- C) To create consumption reduction by inflation of goods and services price
- D) I have no clear idea about aim of VAT implementation

6. In your opinion the extent of VAT contribution for revenue generation of town as a VAT payers in the town

A) Very high B) High C) Average D) Low E) Very low

7. How do you rate the overall capacity and motivation of tax authority in controlling the practice of VAT in this town?

A) Excellent B) Very good C) Good D) Very poor

8. Do you get training about VAT from tax officials in the town?

A) Yes regularly B) Yes yearly at once C) No never I got

9. Do you think new business ventures starts business in this town willingly register for VAT application? A) Yes B) No C) I don't know

10. Do you support other business venture being VAT registering for business activity as of you? A) Yes it helps to equal competition for us B) No it create consumption reduction on our customers

11. Do you think that there are VAT unregistered business in your area?

- A) Yes    B) No    C) I don't know
12. Is there any action taken by the tax officials on the unregistered business to make them registered on the VAT process? A) Yes    B) No    C) I don't know
13. In your opinion do you think that the Authority have adequate number of and skilled man power in the town to lead and control tax practice?            A) Yes they can lead as intended manner            B) No, because it has many challenges in implementation process
14. How much you faced/ noticed a decline in the number of your customers since your business implemented VAT? A. Small change    B. Medium change    C. Significant change  
D. No change
15. How do you settle/collect Vat during delivery/providing goods and services for final users?  
A) Cash register machine            b) Receipt
17. As a responsible business man you always pay VAT to tax authority on time and as expected?    A) Yes, always    B) rarely    C) No, never
18. When you pay VAT honestly to the tax authority, do you get necessary recognition and reward from the authority?    A) Yes    B) No
19. Are you happy on your business activity when you undertake with VAT?  
A) Yes            B) No
20. Do you support a single rate (15%) VAT policy on all the goods and services?  
A) Yes            B) No
21. When do you issue the receipt to the customer in your business activity?  
A) With the product/service they ordered    B) When they ask to pay
22. During your registration time, how you/ your business registered on VAT? A) After evaluation of my business by tax authority in terms of market place and minimum threshold level i.e (500,000)    B) When similar businesses are registered  
C) By the decision of tax authority without any criteria.
23. Do you think the adjusted VAT minimum threshold level 1000,000 is reasonable to generate expected revenue in the town?    A) Yes            B) No
24. Do you believe that the process of VAT registration is smooth and easy for taxpayers?  
A) Yes            B) No
25. Do you think that the VAT refunding processes being made in case of Hosanna town are on time and effectively? A) Always    B) rarely    C) never

If your answer for question no.25 is **Never**, what do you think of the reasons?

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26. Are there customers who are not willing to purchase goods and services with VAT?

- A) Yes      B) No      C) I don't know

27. Do you think that the non-VAT registered taxpayers are more benefited than those of VAT registered enterprises from the competition in the market?

- A) Yes      B) No      C) I have no idea

If your answer for no.27 is **yes**, how do you think of they are as so?

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28. What do you think of the measures that have to be taken by the tax Authority over the business activity that are evading VAT payments?

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29. Are there problems in the VAT administration that needs to be improved in this town? A)

- Yes      B) No      C) I don't know

If your answer is yes; List top three problems below

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

30. Generally, in order to improve VAT administration and maximize revenue of the country as well as the Hosanna town; list top three ideas that needs action;

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

**APPENDIX -II**

**Jimma University**

College of business and economics Graduate studies

MPM program in the department of public management.

Appendix 2: Interview for tax authorities.

Dear participants of Hosanna town tax administration officials:

You are kindly asked to participate in a survey study that aims to assess VAT practice which incorporates collection efficiency, administration system and viewpoints of business communities in case of Hosanna town business activities and by identifying basic challenges, providing possible solutions to overcome the problems. This can be achieved only by your active participation and cooperation by providing necessary information and suggestion. So, I respectfully request your kind cooperation in answering the questions that follow a clearly and frankly as possible.

Thank you in advance for your kind cooperation.

**Interview Questions related to the study**

1. Do you think that the VAT refunding processes being made in case of Hosanna town are on time and effectively? A) Always B) rarely C) never

If your answer for question no.25 is **Never**, what do you think of the reasons?

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2. Do you think that the non-VAT registered taxpayers are more benefited than those of VAT registered enterprises from the competition in the market?

A) Yes B) No C) I have no idea

If your answer for no.27 is **yes**, how do you think of they are as so?

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3. What do you think of the measures that have to be taken by the tax Authority over the business activity that are evading VAT payments?

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4. Are there problems in the VAT administration that needs to be improved in this town? A) Yes B) No C) I don't know

If your answer is yes; List top three problems below

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

5. Generally, in order to improve VAT administration and maximize revenue of the country as well as the Hosanna town; list top three ideas that needs action;

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

