

Does Ethiopia is Effective in Implementing a Presumptive Tax System? Evidence from Hawassa City, Sidama Regional State

Addisu Abebe, Barassa Balguda, Mathewos Yure, Kanbiro Orkaido*
Furra Institute of Development Studies and Education, Furra College, Yirgalem, Ethiopia, East Africa

Abstract

This study was set out to examine presumptive tax system implementation effectiveness in Hawassa city of Ethiopia. To achieve the objective of this research, the study used a mixed research method. The primary data sources were collected through a structured questionnaire and focus group discussion. The analysis has been done. Then, the result of this study showed that the Hawassa city revenue authority is not effective in presumptive tax system implementation. Also, this study revealed that lack of equity and fairness in presumptive tax assessment, lack of clarity and simplicity of tax procedure, the complexity of tax rules, taxpayers' poor awareness of the presumptive system, the existence of unethical and corrupt tax officials, and poor social norms between taxpayers and the tax authority were the key challenges faced by the city tax authority. Finally, the findings of the study inform policymakers about presumptive tax system implementation effectiveness in Hawassa, Ethiopia.

Keywords: presumptive tax system; implementation; effectiveness, Ethiopia

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1. Introduction

Tax can be collected from taxpayers in multiple ways. A presumptive tax system is among these ways of collecting tax revenue to promote the economic growth of the nation (Serbinenko, 2016). Most developing countries in the world were introduced the presumptive tax system in the 20th century. Similar to developing countries, Ethiopia introduced a presumptive tax system in 1995 to broaden the tax base, reduce non-compliance attitude, and increase tax revenue for promoting the economic development of the nation (Geda & Shimeles, 2005). Business income taxpayers were categorized into A, B, and C in Ethiopia. Category A taxpayer is corporate enterprises that have an annual turnover of Birr 1,000,000 or more. Category B are those which have annual turnover having an annual gross income of Birr 500,000 or more but less than 1,000,000 and; category "C" taxpayer being a person other than a company, having an annual gross income of less than Br 500,000. Category A and B are required to maintain adequate books of accounts and their income tax are subject to the statements of accounts they produced. While Category "C" taxpayers are not required to maintain accounts (FDRE, 2016). This makes it difficult for the tax administrations to collect taxes from this group using a conventional tax system. In Ethiopia, the presumptive taxation concept is applied to category "C" taxpayers. Category "C" taxpayers are not required by law to declare their income or keep a book of accounts and are considered as a hard-to-tax group (Thuronyi, 2004; (Bongwa, 2009).

Development of presumptive tax system without effective implementation system. Few researchers have been studied the issue. For instance, empirical studies like Endegen (2017); Abera (2019); Workneh et al.(2019); Getachew (2019); Boru (2019); Gebreslassie (2020); Mengistu et al., (2020); Abebaw (2020); Tumoro, 2020); and Gebreyesus (2020) studied the related topic and found out that implementation of the presumptive tax system is burning issue in developing countries across the globe. Based on the above-stated problems, the current study identifies if Hawassa city of Ethiopia is effective in presumptive taxation implementation. Especially, the paper was answered the following research questions.

- a) Does Hawassa of Ethiopia's tax authority is effective in the implementation of a presumptive tax system?
- b) What are the challenges faced by the city tax revenue authority in the implementation of the presumptive tax system?

The rest part of the paper was organized into four sections. Section 2 is a literature review. Section 3 address the methodology. Section 4 presents results and discussion. Section 5 concludes the paper and section 6 provides implications for future research.

2. Literature Review

Presumptive taxation involves the use of indirect means to ascertain tax liability, which differ from the usual rules based on the taxpayer's accounts (Gordon 1996; Taube & Tadesse 1996; Tanzi et al 1987; Thuronyi 2004; Wube et al. 2012; Kassim et al. 2014; Tilahun & Yidersal, 2014). Government has different objectives when levying the tax. These can be maximizing tax revenue, bringing equity, ensuring economic stability. The presumptive tax aims at improving the efficiency of collection by targeting three groups of effects: a) reducing taxpayers' compliance costs; b) reducing the administrative compliance costs; and c) bridging way from informal to formal activities and from an assessment based on indicators (Pashev, 2005; Pashev, 2006; Yesegat & Fjeldstad 2016; Tehulu,2016;

Fikade et al. 2017). The presumptive taxes seek to use indirect means to assess the liability of a specific taxpayer, which different from usual rules based on taxpayer accounts. Many countries use some form of presumptive taxation to simplify the rules for businesses and individuals that frequently escape taxation.

Ethiopia uses presumptive taxation as a simplified method of revenue collection from small informal sector firms. To implement its presumptive tax, the Ethiopian Revenue and Customs Authority carries out an assessment process to estimate the income earned by small informal sector firms or category C' taxpayers those with an estimated annual turnover of less than 500,000 ETB such firms are subject to a 'turnover based or 'indicator-based presumptive assessment. Annual tax bills are then levied on the assessed income of Category "C" taxpayers (Beza, 2015; Meshesha, 2015).

Even though the history of presumptive taxation is as old as that of state formation, still there are gaps in the implementation of the system in Hawassa, Sidama regional state, Ethiopia. Hence, understanding the presumptive tax system implementation effectiveness would help the city to improve the current status of presumptive tax implementation and solve the challenges related to it. Different studies conducted on the topic were focused only on taxpayers' points of view but considered tax authority ideas. So, it would fill the literature gap that was not addressed by prior studies. So studying such a topic becomes constructive for policymakers and tax authorities in Hawassa, Ethiopia.

3. Methodology

3.1 Research Approach and Design

In this paper, the researcher employed both approaches due to the qualitative and quantitative nature of data. The descriptive research design was employed to achieve the objective of the research.

3.2 Data Type, Collections, and Analysis tools

In this research, the researcher used primary data. To collect primary data, structured questionnaires and focus group discussions were used. After accomplishment of the data collection procedure, data were analyzed using descriptive statistics frequency, percentage, mean and standard deviations through SPSS version 21.0.

3.3 Target Population, Sampling Techniques, and Sample Size Determination

The target population of the study was 306 tax officers in Hawassa city revenue authority during February 2021. To determine the sample size of tax officers in the city, the formula of Yamane (1967) was used. It is assumed that the sample would have 95% reliability about population and a sampling error will be 5%. This simplest formula is:

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

Where N= study population, n= sample size and e = error margin

To select the sample from 306 tax officers in Hawassa city administration revenue authority the researcher also used the same scientific formula as follow:

$$n = \frac{306}{1 + (0.05)^2 * 306} = 173$$

Hence, the representative sample size for this study is 173 tax officers in Hawassa city administration tax authority.

3.4 Reliability and Validity Test

Reliability refers to random error in measurement. Reliability was established using a pilot test by collecting data from 10 subjects, and these will be not included in the sample. Data collected from the pilot test will be analyzed using SPSS version 21.0. In the current paper, the researcher employed Cronbach's Alpha which is the most common measure of scale reliability and a value greater than 0.7 is very applicable. This has tested for all variables as follow:

Table 1 Reliability Test

Cronbach's Alpha	N of items
0.952	9

Source: Personal survey, 2021

This indicates that all the variables under consideration accounts above the scientifically accepted threshold, therefore the study is reliable under this circumstance. This implies that the data incorporated in SPSS is reliable.

3.5 Ethical Considerations

The ethical considerations such as voluntary participation; no harm was to participants, anonymity, and confidentiality, not deceiving the subjects, and privacy of participants have been given attention by the researcher while conducting this research.

4. Results and Discussions

To achieve the research objective, the questionnaires were distributed to target 173 tax officers out of which 150 of them were properly filled and returned questionnaires on the specified period. Hence, the response rate is 86.70 % which implies the majority of the respondents have participated in the process of data collection. Then, the analysis of the data was based on the questionnaires.

4.1 Analysis on presumptive tax effectiveness by Hawassa city tax authority

In the following table, the researcher asked the tax authority about the effectiveness of tax authority in implementing the presumptive tax.

Table 2: Presumptive Tax implementing Effectiveness

Do you believe that the Hawassa city tax authority is effective in implementing a presumptive tax system?		Frequency	Percentage
Valid	No	150	100.0
	Yes	0	0
	Total	150	100.0

Source: Personal Survey, 2021

As showed in table 2, the researcher asked the tax officers sampled about the existence of presumptive tax implementing committees. Out of a total of 150(100%), responded that the tax authority of the city is not effective in implementing presumptive taxation. This indicates that the Hawassa city administration revenue authority is not effective in presumptive tax implementation. According to focus group discussion responses, this study found out that there is a poor familiarity of taxpayers with parameters to estimate the average daily revenue and there are inadequate implementing committees in the tax assessment and collection process.

4.2 Respondent Opinion on Challenges of Presumptive Tax Implementation

Table 3. Respondent opinion on challenges of presumptive taxation implementation in Hawassa

Put your agreement on the following items	N	Minimum	Maximum	Mean	Std. Deviation
There is a lack of equity and fairness in presumptive tax assessment	150	1.00	5.00	3.9667	.90053
There is a lack of clarity and simplicity of tax procedure	150	1.00	5.00	4.0000	.81923
There is Favoritism in the tax administration system	150	1.00	5.00	4.0000	.82738
There is a Complexity of tax rules	150	1.00	5.00	4.2667	.87980
There is Low level of taxpayers awareness of taxation	150	1.00	5.00	3.8733	.83784
The existence of corruption	150	1.00	5.00	4.2333	.86247
Taxpayers' negative attitudes toward the government	150	1.00	5.00	4.1267	.89964
Poor social norms between taxpayers and tax Authority	150	1.00	5.00	3.9400	.85318

Source: Personal Survey, 2021

As can be seen from the above table the respondents were asked to express their opinion on the challenges of presumptive tax. The opinion on first items the lack of equity and fairness in presumptive tax assessment has to mean value 3.9667, second item Lack of clarity and simplicity of tax procedure 4.0000, third item nepotism in the tax administration system 4.0000, fourth complexity of tax rule 4.2667, fifth item taxpayers' poor perceptions of tax evasion 3.8733, sixth item the existence of unethical and corrupt tax officials 4.2333, seventh item taxpayers' negative attitudes toward the government 4.1267 and last item poor social norms between taxpayers and the Ethiopian revenues and customs authority 3.940 falls in agree and strongly agree on level respectively. Overall mean & Standard deviation 4.0478 and 0.9843 respectively. The overall mean fall with agree level means the respondents on average agreed on all item asked to the challenges of presumptive tax. This tells us Hawassa city administration tax authority is not effective in presumptive tax system implementation due to problems such as lack of equity and fairness in presumptive tax assessment, lack of clarity and simplicity of tax procedure, nepotism in the tax administration system, the complexity of tax rules, taxpayers' poor awareness on taxation, The existence of corruption, taxpayers' negative attitudes toward the government, poor social norms between taxpayers and the tax authority. While focus group discussion the respondents answered similar ideas.

5. Conclusions

The major purpose for introducing a presumptive tax system by the government of Ethiopia is to broaden the tax

base and to increase tax revenue for promoting the economic development of the nation. The effective implementation presumptive tax system is a challenging subject in developing countries especially Ethiopia. So the result of this study showed that Hawassa city revenue authority is not effective in presumptive tax system implementation due to problems such as lack of equity and fairness in presumptive tax assessment, lack of clarity and simplicity of tax procedure, favoritism in the tax administration system, the complexity of tax rules, taxpayers,' poor awareness on the tax system, the existence of corruption, and poor social norms between taxpayers and the tax authority were key problems hindering the presumptive tax system implementation effectiveness.

6. Future Research Direction

The finding will be improved if other researchers addressed the topic by considering more than one city in other regional states and national levels. The study will improve if it is conducted on determinants of presumptive taxation effective implementation in the same study area, at regional, national, and international levels by incorporating econometric modeling.

Declaration of competing interest

The author declares that he has no known financial interests or personal interests that appeared to influence the work reported in this paper.

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