

A Study on Tax Evasion and Avoidance in Ethiopia: The Case of Ethiopian Revenue and Custom Authority Bahir Dar Branch

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Abstract

Taxes are important sources of public revenue. Tax avoidance and tax evasion are widely believed to be significant factors limiting revenue mobilization. In Ethiopia, tax evasions and avoidances are pervasive features in tax collection process. This paper assessed the level of Tax Evasion and Avoidance in Bahir Dar city and analyzed the controlling mechanisms of tax evasion and tax avoidance. In doing so, both qualitative and quantitative data are obtained from both primary and secondary data sources using collection tools such as interviews, questionnaires and from different books & reports. Descriptive method of data analysis was used to analyze and interpret the data. The result showed that there is tax evasion and avoidance in Bahir Dar city and the major methods used by taxpayers to evade and avoid tax are non- declaration and under reporting of income, overstating business expense and deductions, overstating and understating trading stock, deduct personal expenses as business expenses to hide the exact tax liability. Consequently, it is recommended that: database for tax administration at all levels of government should be promptly computerized, it is better for the taxing authority to fulfill the required number of experienced personnel with the required qualifications and there should be continuous training for tax officers on how to provide rapid and courteous service, continuous education for citizenry has to be embarked upon and step has to be taken to convince the tax payers that the money collected in form of taxes are judiciously spent and the tax department should adopt scientific procedures in collecting data and selecting taxpayers for further audit and perform risk based tax audit.

Keywords: Tax evasion, tax avoidance, tax administration, database, risk based tax audit and under reporting

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1. Introduction

Businesses operators react to taxes, both in how they organize their activities and, perhaps, in where they carry them out. People also talk about them, complain about them, and try to dodge them when they can. How people and businesses react in turn affects the level and structure of taxation (Zolt, 2003).

Taxes are very important tools of governments' fiscal policy. That is why Zolt (2003) stated that the main purpose of taxation is to generate sufficient revenue to finance public sector activities in a non-inflationary way. Similarly, taxes are important sources of public revenue (Ethiopian Chamber of Commerce and Ethiopian Business Development Services Network, 2005). The provision of public infrastructure and government services are a key factor for economic development. In many developing countries, a lack of public service provision slows down economic growth and undermines efforts to improve the living standard of the population. There are a number of reasons for the failure of many governments in developing countries to provide sufficient public services.

The subsequent taxing system in Ethiopia can be divided into three broad categories: (i) taxes on income and profits, (ii) taxes on goods and services and (iii) taxes on international trade. Most of these taxes have been reformed and amended following the general 1992 liberalization (or reform) policy.

Tax avoidance and tax evasion are widely believed to be important factors limiting revenue mobilization (Riedel, 2009). They are terms so frequently referred to in economic and business relationships that they constitute part of our conversational language and people in general use these terms even without knowing their exact meaning and difference. Whereas tax avoidance implies a situation in which the taxpayer reduces the tax liability by taking advantage of the loop-holes and ambiguities in the legal provisions, in the case of tax evasion, facts are deliberately misinterpreted and the tax liability is understated. Thus, while tax avoidance is perfectly legal and is, at times, referred to as 'tax planning', tax evasion is illegal and, therefore, carries with it the risk of penalties and prosecutions under the tax laws. As such, the black economy comprises the sum total of all the various methods of tax evasion but does not include tax avoidance. Accordingly, the consequences of the two phenomena are different for the taxpayers, both reduce the revenue of the Exchequer and consequently need to be checked to the greatest extent possible (Jain, 1987).

1.1. Statement of the Problem

In recent years, the academic and political debate on development finance and development aid has raised the issue that tax avoidance and tax evasion may undermine the ability of developing countries to finance their public sectors. This view is based, among other things, on the perception that the shadow economy in these countries is larger than in the developed world.

Exchange of information play an important role in assisting the country to increase revenue and at the same time helps to reduce audit cost

The theoretical literature focuses on a situation where a taxpayer decides how much income to report to the government facing a probability of audit and a penalty for cheating. In particular, many have argued that observed compliance levels can only be explained by psychological or cultural aspects of tax compliance such as social norms, tax morale, patriotism, guilt and shame. In other words, taxpayers, despite being able to cheat, are unwilling to do so for non-economic reasons (Alm, 2012).

Many practitioners of tax advice in developing countries believe that the change in emphasis is essential; for example, Bird (2008), goes so far as to say that, in developing countries, "Tax administration is tax policy". It is believed that these issues are also critical in developed countries. In this setting, the issue is not the feasibility of certain taxes, but rather the optimality of alternative tax structures. For example, while in many developing countries an income tax that relies on self-reporting cannot be administered at all; in a developed country the question is to what extent optimal tax design should reflect the reality of evasion, the necessity of enforcement, and the costs of collection (Slemrod and Yitzaki, 2002).

Ethiopia, like most countries in Africa, has been making considerable efforts in recent years to restructure its tax system with a view to increase tax revenue as well as reduce distortions in the economy. The impact these reforms have had on the poor is of considerable importance to policymakers, given that the poor and the vulnerable constitute a significant majority of the population in Ethiopia. However, to analyze the distributional impact of its tax system is not so straightforward. There are several reasons for this. First, tax evasion is considered to be substantial in Ethiopia, leading to unintentional consequences on income distribution. Second, a substantial portion of tax revenue comes from commodity taxes whose effect on income distribution is essentially determined by household consumption patterns and the market structure (Shimeles, 2005).

But as per the Researchers' knowledge, researches are not well done that specifically investigates the level of tax evasion and avoidance in Ethiopia in general and in Bahir Dar city in particular. Hence, the main purpose of this study is to analyze tax evasion and avoidance in Ethiopia focusing on ERCA Bahir Dar Branch.

Hence, to address the issue, the following general guiding questions are formulated.

- Do taxpayers declare the true income generated from their business?
- Do the taxpayers report the exact tax liability?
- How much is the degree of tax evasion and avoidance?
- How dose tax administration environment of tax evasion and avoidance look like?

1.2. Objectives of The study

The main objective of this research is to study the level of Tax Evasion and Avoidance in Bahir Dar city and to analyze the controlling mechanisms of tax evasion and tax avoidance.

1.2.1. Specific Objectives

The specific objectives of the research are:

1. To assess whether there is reliable report of income by tax payers to the tax authority.
2. To analyze whether the tax payers report the exact tax liability.
3. To examine the degree of tax evasion and avoidance.
4. To assess the tax administration environment of tax evasion & avoidance.

1.3. Significance of the Study

The main outcome of this paper will be assessment of tax evasion and avoidance. Thus the findings of the study will offer policy makers on taxation, the tax authority and others an opportunity to further design and redesign policies that will use to reduce tax evasion and avoidance and to promote better tax system and to increase tax revenue.

Other Researchers can also use it as reference point in further research in the area of tax evasion and avoidance.

1.4. Scope of the Study

This study is limited on the assessment of tax evasion and avoidance of tax payers that are found in the geographical territory of Bahir Dar city.

2. Literature review

This part of the study is classified in to two: theoretical and empirical evidences as follows.

2.1. Theoretical Review

A tax is a compulsory payment or contribution by the people to the Government for which there is no direct return to the taxpayers. Tax imposes a personal obligation on the people to pay the tax if they are liable to pay it. The main theoretical principle is that the general public shall be taxed according to their ability to pay, which considered as their fair share and the people in the same financial position should be taxed in the same way without any discrimination. However, the ability to pay is left for vague base.

2.1.1. General characteristics of tax

As stated in Parameswaran (2002), a tax has the following characteristics:

- a. Tax is a Compulsory Contribution: Tax is a compulsory contribution by the taxpayers to the Government. The people whom the tax is levied cannot refuse to pay the tax. Once it is levied they have to pay it. Any refusal in this regard leads to punishments.
- b. Benefit is not the Basic Condition: For the payment of tax, there is no direct return or *quid proquo* to the taxpayers. That is, people cannot expect any return in benefit for the amount of tax paid by them, because there is no relation between the amount of tax paid by the people and the services rendered by the Government to the taxpayers.
- c. Personal Obligation: Tax imposes a personal obligation on the taxpayers. When a person becomes liable to pay the tax, it is the duty of him to pay it and in no way he can escape from it.
- d. Common Interest: The amount of tax received from the people is used for the general and common benefit of the people as a whole. Now the Government has to render enormous range of social activities, which incur heavy expenditure. A part of the expense is sought to be raised through taxation of various types. Thus, taxes are said to be the sharing of common burden by the people.
- e. Legal Collection: Tax is the legal collection. It can be levied only by the Government both Central and State.
- f. Element of Sacrifice: Since the tax is paid without any return in benefit, it can be said that there is the prevalence of sacrifice in the payment of tax.
- g. Regular and Periodical Payment: The payment of tax is regular and periodical in nature. It is levied for a fixed period usually a year. Thus, almost all the taxes are annual taxes. The payment of taxes should be regular also.
- h. No Discrimination: Tax is levied on all people without any discrimination of caste, creed etc. but according to their ability to pay.
- i. Wide Scope: Tax is levied not only on income but also on property and commodities. To enhance the revenue and to bring all the people under the tax net, the Government imposes various kinds of taxes. This enhances the scope of taxes.

2.1.2. Classifications of tax

The usual broad classification of taxes into direct and indirect is followed. This classification relates to the method of payment and collection, rather than the purpose, since in practice taxes may have more than one purpose. Direct taxes are taxes levied on incomes, to which the persons concerned make direct payment to the Board of Internal Revenue or Local Authorities. These include income tax, taxes levied on total spending, company taxes, capital taxes where they apply, and local rates. Indirect taxes are those taxes levied on goods and services, so called because the Board of Customs and Excise does not usually collect them from the consumers directly but from importers, manufacturers and intermediaries. The duty paid by these people is reflected in the prices that consumers subsequently pay (Ogbonna, 1975).

2.1.3. Taxation in Ethiopia

In Ethiopia the year 1991 marked the end of the previous policy regime of hard control that had lasted for nearly two decades. Starting from 1992, the Government has initiated a wide range of reforms that can be termed as liberalization. Reform of the tax system was among the range of liberalization policies that also extended, among others, to the exchange rate, interest rates, trade, domestic (Shimeles, 2005).

2.1.4. Major types of taxes existing in Ethiopia

1. Direct Taxes: which includes tax on income from employment /personal income tax, business profit tax, tax on income from rental of buildings, tax on interest income on deposits, dividend income tax, tax on income from royalties, tax on income from games of chance, tax on gains of transfer of certain investment property, tax on income from rental of property, rendering of technical services outside Ethiopia, agricultural income tax and land use tax.
2. Indirect Taxes: including turnover tax, excise tax, value added tax (vat), custom duty and stump duty

2.1.5. Tax evasion and tax avoidance

Tax evasion and tax avoidance are deviations from what is to be found legal, fair and just. Tax avoidance is

sometimes used to refer to a legal reduction in taxes, while evasion refers to tax reductions that are illegal (Gravelle, 2009). They occur frequently together. It is common in them that they result in losses in the tax revenue. Otherwise they are different from each other. Tax evasion is associated with breaking the law: it is a gap developed due to the taxpayers' real conduct departing from what has been promulgated as statutory fiscal law. In contrast, tax avoidance does not ensue the breaking of the law. It is yet the circumvention of law: taxpayers entangled in tax avoidance attack what can be seen as the integrity of law (Deak, 2004).

Tax Evasion may be defined as any action that results in the concealment of all or part of a person's legitimate or illegal economic activities from the tax authorities in order to escape the payment of tax. In short, it is an intentional and illegal avoidance of paying mandatory taxes to the Government (Alm, 2012). Tax Avoidance, on the other hand, is used to describe tax reductions achieved through artificial but permissible arrangements of personal or business affairs. It refers to the legitimate use of loopholes in the tax laws in order to minimize one's tax burden. There is therefore nothing illegal about it.

According to (Gravelle, 2009), international tax avoidance issues can also be differentiated by the measures that might be taken to reduce the associated revenue losses. Evasion is often a problem of lack of information, and remedies may include resources for enforcement, increased information sharing, and possibly withholding. Avoidance may be more likely to be remedied with changes in the tax law.

Tax evasion is not identical to the loss in the potential revenue that could be collected in the absence of tax evasion. If tax collection were more efficient, the tax-payers' conduct would not remain the same, and so the real economic circumstances for tax collection would also be different (Franzoni, 2000). Tax evasion is closely connected with the informal economy and associated crimes like fraud, false accounting, money laundering, bribery, etc.

2.1.6. Measuring evasion

A fundamental difficulty in analyzing tax evasion is the lack of reliable information on taxpayer compliance. After all, tax evasion is illegal, and individuals have strong incentives to conceal their cheating, given financial and other penalties that are imposed on individuals who are found cheating on their taxes. There have been many approaches to measurement, which is broadly classified as Traditional and Modern (Alm, 2012).

a. Traditional approaches

Among traditional approaches, the most accurate source of information on individual compliance is based on "direct" measurement of evasion via actual audits of individual returns. For example, from 1965 to 1988, the U.S. Internal Revenue Service (IRS) conducted detailed line-by-line audits of a stratified random sample of roughly 50,000 individual tax returns on a 3-year cycle via its Taxpayer Compliance Measurement Program (TCMP). These audits yielded an IRS estimate of the taxpayer's "true" income, which when compared to actual reported items allowed the IRS to calculate measures of income tax evasion (e.g. the "tax gap") (Alm, 2012). Another direct approach is based on survey evidence, in which individuals are asked about their evasion behavior.

b. Modern approaches

More recent approaches use a variety of novel methods. Some researchers have used measures of reported income from individual tax returns as a proxy for evasion, on the assumption that one's total income must be divided between reported income and unreported (or evaded) income. Other researchers have conducted controlled field experiments (Slemrod and Yitzaki, 2002). Some have used tax deduction-based (Feldman and Slemrod, 2007) measures as an indicator of tax evasion.

2.1.7. Indicators of tax evasion and avoidance

There are several indicators that have often been used. One approach estimates evasion via some "gap" that can be estimated, such as the gap between income reported on tax returns and income in the national income accounts, between income and expenditures in the national income accounts, or between official and actual labor forces (Alm, 2012).

It is also stated in Shome (1993) that tax evaders may not declare income; may underreport income, sales, or wealth; may over report deductible expenses; may smuggle goods or assets; or may undertake some other deception.

Tax revenue losses due to tax avoidance and tax evasion can occur for a number of reasons. Existing estimates of these revenue losses distinguish between a domestic and an international component of tax avoidance and tax evasion (Riedel, 2009).

2.1.8. Factors of Tax Evasion and Avoidance

Several factors have been identified which lead to evasion in the cash economy, international dealings or aggressive tax planning including-

- Perceptions of the tax system - community confidence in the system, high tax rates, complexity of the law, ability to conceal transactions, applicable penalties and other deterrents;
- Economic factors - competitive advantage, margin squeezing;
- Tax concessions - including those for expenditure on films, research & development providing incentives for exploitation;

- Perceptions of tax administration efficacy - uncertainty (eg less than clear statements of application of the law), perceived ability to 'get away with it' (eg detection rates, probabilities in the audit lottery), application of legislative and other penalties, perceptions about fair treatment;
- Developments in society - enhanced ease of undertaking dealings eg internet and e-banking technologies combined with design and marketing of arrangements by offshore and onshore promoters.

2.2. Empirical literatures on tax evasion and avoidance

Olabisi (2010) conducted a research on "An Assessment of Tax Evasion and Tax Avoidance in Lagos" and the study revealed that the tax administration in Lagos State is very inefficient and ineffective, and that there is no adequate information on the taxpayers in the state hence, some people can hide from their tax liabilities. It was also discovered that there is a significant relationship between tax evasion and tax avoidance and the revenue of Government and the tax rate.

Haile (2011) assessed Tax Evasion and Avoidance in Mobilizing Tax Revenue by using descriptive way of research. The result shows that the government is losing a significant amount of revenue due to tax evasion and avoidance. Only from taxpayers who are audited and assessed there are a huge amount of money (Birr 87,359,749) that had not been collected yet. The existence of other unaudited taxpayers and informal sectors, which have not been audited yet, makes the government a loser in generating more revenue. In addition to the revenue losses, the existence of tax evaders and avoiders in trade markets are also making the legal taxpayers a loser and creating a negative impact on legal taxpayers to change their behavior from compliance to noncompliance and the study recommend the necessary measures for creating compliance include: creating optimal legitimates and enforcement practices to deter the effect of tax evasion and avoidance; educating, following and handling taxpayers; and identifying, investigating and prosecuting of tax evaders and avoiders.

3. Research design & methodology

This study is designed as a descriptive research method with qualitative and quantitative data analysis approaches. Primary and secondary data related to the reporting trend of tax payers income and tax liability, the level of tax evasion and avoidance in Bahir Dar city and controlling environment of tax evasion and avoidance were collected from Ethiopian Revenue and Customs Authority (ERCA) now the Ministry of Revenue in Bahir Dar branch and private auditors found in the city.

3.1. Data sources, types and methods of collection

For this study, the Researchers applied quantitative (survey) and qualitative (in-depth interview and document analysis), and are discussed in the following sub-sections.

3.2. Sample Design

While developing a sampling design for this study, the Researchers gave attention to the following points: The populations, sample frame, sampling technique, and sample size.

➤ Population or Universe

The population/universe that this research addressed was employees of ERCA at Bahir Dar branch specifically the audit section, tax collection and enforcement section and customer handling section and private auditors and accountants in Bahir Dar city.

➤ Sampling Frame

The data were collected from a list of tax payer's financial reports prepared before tax audit and after the audit from the tax authority, identified tax officials that are working related with tax collection and private auditors and accountants who have knowledge about the tax payers' activities and their jobs are directly related to tax payers evasion and avoidance.

➤ Sampling technique and sample Size

It is very important to determine a sample size by considering the practical situation. On the one hand, selecting the sample size of the employee of the Authority and private auditors, the most important section for this research is considered to be the audit section, tax collection and enforcement section and customer handling section.

Since the population size is 81 for this study, all are used to calculate the sample size. There for, as shown in table 3.1 below, the total number of 81 respondents was selected are selected.

Table 3.1: Sample Size Selection

Sections	Population No.	Sample Selected	In %
Audit Section	14	14	100%
Collection and Enforcement Section	13	13	100%
Customer Handling Section	10	10	100%
Private auditors and accountants	44	44	100%
Total	81	81	100%

Source: compiled by the researchers

Moreover, data were collected by interviewing ERCA officials who are directly involved in the directing and managing section. For this purpose, researchers selected 3 higher level officials. On the other hand, pre-audit and post-audit financial reports of the tax payers were used to gather secondary information about the ways and the level of tax evasion and avoidance.

3.3. Methods of data analysis and interpretation

In order to make it manageable, first the data were classified on the basis of their similar characteristics, editing, coding and tabulation process have been done prior to analysis of the raw data. Then, the statistical package for social science (SPSS) and MS excel software has been used for data entry, checking, validation and data analysis. In addition to the data obtained through other methods, this study employed a descriptive analysis of documents such as periodical tax audit reports, proclamations, tax audit policy, and others documents that are relevant for the study. The document analysis were applied for examining the number of taxpayers audited in a given fiscal year, the amount of additional tax revenue through audit, the background information of the study area, and as a supportive for other tax audit activities in Ethiopian tax system.

3.4. Validity and reliability of the instrument

The Researchers distributed the questionnaires to 10 tax officers and 10 authorized accountants to rate the relevance of questions. The validity of the study instruments is performed using the content validity index (CVI) on a four point scale of relevant (4), quite relevant (3), somewhat relevant (2) and not relevant (1).

Having this, researchers also performed cronbach's alpha tests on the likert scales in the instrument for there is non-declaration or under report of income by tax payers to the tax authority, the tax payers report the exact tax liability, the degree of tax evasion, the degree of tax avoidance, methods of controlling tax evasion and avoidance. as shown below:

Reliability Test: Variables Cronbach's Alpha Value

- non-declaration or under report of income by tax payers 0.765
- the tax payers report the exact tax liability 0.705
- the degree of tax evasion and avoidance 0.721
- methods of controlling tax evasion and avoidance 0.738

Generally, a Cronbach's alpha coefficient of at least .70 is considered sufficient and. As shown above, alpha coefficient range between 0.705 and 0.765 for all scales and this suggest a satisfactory degree of internal consistency for all the variables since all the reliability statistics measured well above the threshold 0.7.

4. Results and discussions

This part of the research discusses about the findings based on the information gathered from the questionnaires, secondary data and interviewees by the researchers. Considering the general objective, the questionnaires and interviews have been designed to measure income declaration and reporting trend of taxpayers, to assess the trend of tax payers' tax liability report, to examine the level of tax evasion and avoidance and to assess possible mechanisms of controlling tax evasion and avoidance.

4.1. Response rate

In order to undertake this study, a total of 81 questionnaires were distributed to the tax officials and private auditors and accountants of Bahir Dar city and among the total questionnaires 72 (89%) were completed and returned. Moreover, all the two semi-structured interviews (out of two) were conducted with the higher officials of ERCA in Bahir Dar branch. Therefore, the collected data is representative of the sample and can be used to make conclusions. Based on the data obtained from the respondents, the following analyses and interpretations have been made.

4.2. Characteristics of Respondents

This section provides a general background about the respondents who participated in answering the questionnaires of the study. During data collection the basic characteristics like sex, age, educational background

and job position were collected.

4.2.1. Characteristics of respondents based on sex and age

The following table analyses the characteristics of respondents based on sex and age.

Table 4.1 Distribution of respondents based on sex and age

Indicator	Description	Number of respondents	Percentage
Sex	Male	55	76.4
	Female	17	23.6
	Total	72	100.0
Age	18-25 years	13	18.1
	26-45 years	55	76.4
	>45 years	4	5.6
	Total	72	100.0

Source: Field survey (2017)

As depicted in table 4.1, majority of the respondents 55(76.4%) are male and 55(76.4%) of the total respondents range in the age of 26-45 years which is followed by 13(18.1%) of respondents that ranges with in an age of 18-25 years.

4.3. Assessment of tax evasion and avoidance

Soyode and Kajola (2006) cited in Olabisi (2010) submitted that refusing to register with the relevant authority; failure to furnish a return, statement or information keep records required, making an incorrect return by omitting or understating any of income liable to tax, refusing or neglecting to pay tax, overstating of expenses so as to reduce taxable profits or income, which will also lead to payment of less tax than would otherwise have been paid. A taxpayer may also hide away totally without making any tax returns at all, and entering into artificial transactions.

Table 4.2 Descriptive statistics on tax evasion and avoidance found from questioners

R. No	Measures	strongly agree /1/		Agree /2/		Neutral /3/		Disagree /4/		strongly disagree /5/		mean	Average mean
		No	%	No	%	No	%	No	%	No	%		
A	Tax payers tax declaration and income reporting trend												
1	Not declare and reporting some income?	20	27.8	46	63.9	2	2.8	3	4.2	1	1.4	1.88	2.02
2	Omission to report several incomes from irregular sources?	10	13.9	46	63.9	12	16.7	3	4.2	1	1.4	2.15	
B	Trends of tax payers tax liability Report												
3	Overstating business expenses and deduction?	20	27.8	43	59.7	4	5.6	5	6.9			1.92	2.43
4	Overstating or understating trading stock?	4	5.6	58	80.6	9	12.5	1	1.4			2.1	
5	Deduction of personal expense as business expense?	7	9.7	49	68.1	2	2.8	10	13.9	4	5.6	2.38	
6	The society has the tendency of assuming minimizing tax liability is morally right?	7	9.7	46	63.9	8	11.1	10	14	1	1.4	2.33	
7	Most payment fillers declare their liability honestly without under reporting?			15	20.8	15	20.8	40	55.6	2	2.8	3.4	
C	Indicators /symptoms/ of Tax Evasion and Avoidance												
8	Lying to tax auditors even when audited?	6	8.3	45	62.5	17	23.6	4	5.6			2.26	2.35
9	Falsifying supporting documents?	9	12.5	54	75	6	8.3	3	4.2			2.04	
10	Failing to file a tax return together?			51	70.8	20	27.8	1	1.4			2.31	
11	Maintenance of multiple set of books of accounts?	5	6.9	35	48.6	19	26.4	12	16.7	1	1.4	2.57	
12	Securing contracts under doomy names / non-existent persons/?	3	4.2	34	47.2	28	38.9	6	8.3	1	1.4	2.56	
D	Tax administration environment for tax evasion and avoidance												
13	The system of tax administration in Ethiopia is efficient and effective?	3	4.2	12	16.7	8	11.1	33	45.8	16	22.2	3.65	3.46
14	The penalties imposed presently are enough deterrent to prevent potential tax defaulters?	4	5.6	17	23.6	10	13.9	37	51.4	4	5.6	3.28	
15	Non availability of the database of all taxable individuals by the revenue authority provides an opportunity for people to evade tax?	15	20.8	43	59.7	6	8.3	7	9.7	1	1.4	2.11	2.33
16	There is shortage of experienced and highly motivated personnel for tax assessment and tax collection?	15	20.8	45	62.5	7	9.7	4	5.6	1	1.4	2.04	
17	The procedures for tax assessment and tax collection are ambiguous?	10	13.9	46	63.9	5	6.9	11	15.3			2.24	
18	Strict punishment should be meted out on tax defaulters?	10	13.9	35	48.6	7	9.7	19	26.4	1	1.4	2.53	
19	The government at all levels should make efforts towards fighting cases of tax offences?	13	18.1	41	56.9	4	5.6	13	18.1	1	1.4	2.28	
20	Tax policies should be reviewed and updated constantly for an effective system to be in place?	11	15.3	26	36.1	6	8.3	26	36.1	3	4.2	2.78	

Source: Field survey (2017)

4.2.2. Tax payers tax declaration and income reporting trend

The response of respondents regarding tax payers' income declaration and reporting trend presented as follows.

As indicated by table 4.2 below, majority of the respondents strongly agree and agree (27.8% and 63.9% respectively) that there is none declaration and under reporting of income. Whereas, 4.2% disagree and 1.4% strongly disagree while 2.8% neutral with this.

Moreover, the table indicated that 77.8% (13.9% strongly agree and 63.9% agree) of the total respondents replied as there is omission to report several incomes from irregular sources by the taxpayers in the city. Others 4.2% disagree, 1.4% strongly disagree and 16.7% neutral with this aspect. Furthermore, the average mean of the distribution of responses were found to be 2.02, which indicates that more than half of the respondents agreed as there is none declaration and under reporting trend of income by tax payers.

From this the Researchers understood that tax payers have a trend of non-declaration and underreporting of income generated from their business.

4.2.3. Trends of tax payers tax liability report

As stated in Olabisi(2010), no one likes to pay taxes, even though tax payment is inevitable for the provision of social welfare, hence individuals and companies want to reduce their tax liabilities and they try to do this either legally, by tax avoidance or illegally by tax evasion.

➤ Primary data analysis

About five questions were forwarded to respondents to assess the trend of reporting tax liability by tax payers and the following result were drawn.

As shown by table 4.2, majority of the respondents 87.5% (27.8% strongly agreed and 59.7% agreed) implied that tax payers overstating business expenses and deduction and 5.6% disagree with this while the remaining 5.6% were neutral.

In respect to the reporting trend of trading stock by tax payers, 86.2% (5.6% strongly agreed and 80.6% agreed), 1.4% disagree and 12.5% were neutral with tax payers are overstating or understating trading stock.

The table also depicted that among the total respondents 9.7% strongly agreed and 68.1% agreed with tax payers deduct personal expense as business expense respectively. Whereas, 13.9% disagree, 5.9% strongly disagree and the remaining 2.8% of respondents were neutral with this.

Respondents opinion regarding taxpayers tax liability perception, table 4.2 depicted that 63.9% agree and even 9.7% strongly agree as the society has the tendency of assuming minimizing tax liability is morally right and 1.4% disagreed and 1.4% strongly disagree while the remaining 11.1% of the respondents were neutral on the issue.

On the other hand, 55.6% and 2.8 % of the total respondents disagreed and strongly disagree respectively that most payment fillers declare their liability honestly without under reporting. Other 20.8% of the respondents agreed and the remaining 20.8% were neutral.

Furthermore, the average mean of the distribution of responses were found to be 2.43, which indicates that more than half of the respondents agreed as tax payers are not reporting the true tax liability due from them.

Moreover, interviewed respondents assured that most of the time the tax payer understate the exact tax liability and the reasons for this are that fragile culture and poor norm of tax payers about payment of tax liability.

In general, the data collected from respondents based on questionnaire using different questions implied that tax payers overstate business expense and deductions, overstate and understate trading stock, deduct personal expenses as business expenses, have the tendency of assuming minimizing tax liability is morally right and didn't declare their tax liability honestly. These all are symptoms of tax evasion and avoidance practices.

➤ Secondary data analysis

Additional data were collected from secondary sources to assess the tax liability reporting trend of tax payers and the result is shown by table 4.3 below.

Table 4.3, Companies' tax liability before and after audit

Year	Number of Income tax audited companies	Number of VAT audited companies	Companies not report the exact tax liability			
			Income tax		VAT	
			No	%	No	%
2015	43	34	41	95%	33	97%
2016	36	18	33	92%	15	83%
2017	34	22	34	100%	20	91 %
Average	37.7	24.7	36	95.5%	22.7	92%

Source: Compiled researchers from ERCA annual reports

As table 4.3 depicted, 95% of the total taxpayers audited in 2015 didn't report the exact income tax liability. Similarly 92% of the audited tax payers in the year 2016 and all audited tax payers of year 2017 didn't report the correct income tax liability due from them. From this it is implied that on average about 95.5% of audited tax payers were not reporting the exact annual income tax liability.

On the other hand among the VAT audited companies, 97%, 83%, and 91% of them reported incorrect VAT liability in the years 2015, 2016 and 2017 respectively. On average, among the audited VAT registered companies, 92% didn't report the full amount of VAT due from them. The implication is that tax payers didn't report the exact tax liability due from them.

4.2.4. Indicators /symptoms/ of tax evasion and avoidance

Thanks to articles 52(2/b/), 95 and 97 of the FDRE constitution each regional state of Ethiopia is empowered/ authorized / to enact their own tax laws. Accordingly, the Amhara Regional State has enacted its own income tax proclamation (Proc. No. 240/2016) and income tax regulation (Regulation No. 241/2016) which was issued for the proper interpretation of the said income tax proclamation. These tax laws, among other things, have provisions which are directly or indirectly dealing with protection of tax evasion. These provisions can be categorized in to General substantive provisions, Administrative penalties and criminal Sanction.

➤ Primary data analysis

About five questions were forwarded to respondents to assess the existence and indicators of tax evasion and avoidance. The result is summarized by table 4.2 and presented in the following manner.

Among the total respondents, 8.3% strongly agree and 62.5% agree that tax payers are lying to tax auditors even when audited and only 5.6% of them disagreed on the issue. The remaining 23.6% were neutral with this.

About the delivery of supporting documents, 12.5% strongly agree and 75% agree with falsifying supporting documents by tax payers and among the remaining respondents only 4.2% disagree with the issue while 8.3% neutral.

In respect to tax payers tax return filing system, table 4.2 implied that majority of the respondents (70.8%) agree with tax payers failing to file a tax return together. Only 1.4% of the total respondents disagree and 27.8% neutral.

Moreover, 6.9% strongly agree and 48.6% of the respondents agree that there is maintenance of multiple set of accounts by tax payers whereas 16.7% of them disagree, 1.4% strongly disagree and 26.4% neutral.

Regarding contract taken by tax payers 4.2% of the respondents strongly agree and 47.2% agree that they are securing contract under doomy names/non-existing persons/. Among the remaining respondents, 8.3% disagree and 1.4% strongly disagree while 38.9% neutral with the issue.

Furthermore, the mean of the distribution of responses were found to be 2.35, which indicates that more than half of the respondents agreed that there are symptoms of tax evasion and avoidance practice by tax payers. The indicators for this are lying to tax auditors even when they are auditing, false supporting documents, failure of filing a return together, maintenance of multiple set of books of accounts and securing contract under doomy names by the tax payers.

Besides these, the interviewees said that the level of tax evasion and avoidance is at high level, and they implied major indicators such as, many business do not declare the exact income or under reporting income, many firms do not keep proper books of accounts and do not use a cash register machine or receipt for a day to day sales activities and over stating business expense.

From the above analyses, researchers understood that tax evasion and avoidance is highly practiced in the city. Further investigation was made on this variable by the Researchers using secondary data collected from ERCA and the result is shown as follows.

➤ Analysis of secondary data found from tax audit

Most taxpayers' report their tax liabilities more accurately if they believe that the tax administration has the capacity to detect any unreported liabilities and that heavy penalty may be applied when they are detected (Haile 2011). Thus, tax audit results in increased tax revenue in two ways: (1) directly through assessment of additional taxes; and (2) indirectly by discouraging underreporting of liabilities by all taxpayers. Further, Edmiston, K D and R M. Bird (2004) noted that the purpose of tax audit is to check the evasion of tax and ensure compliance in accordance with the laws and regulations.

The assessment of based on the report taken from ERCA in Bahir Dar branch as shown by Table 4.4 represented that the amount of tax evaded by tax payers in each year is much more. As shown by the table, the total amount of income tax that should be reported from the audited companies in the year 2015 were birr 28,038,705.04. However, only an income tax liability of birr 2,643,743.10(9%) has been reported by those companies. Thus, birr 25,394,961.94(91% of the total income tax expected to be reported) is considered as tax evasion in that year. Similarly, birr 5,597,286.47(53%) and 33,625,871.24(88%) income tax have been found by the investigation of tax auditors that is not reported by the audited companies in year 2016 and 2017 respectively. On average, about birr 21,539,373.22(84%) have been evaded by tax payers per year.

Table 4.4 summary of the amount of tax liability before and after audit

Year	Income tax /in ETB/			I/tax evasion in %	VAT /in ETB/			VAT evasion in %
	Before audit	Audit finding	After audit		Before audit	Audit finding	After audit	
2015	2,643,743.10	25,394,961.94	28,038,705.04	91%	12,587,230.07	13,074,902.05	25,662,132.12	51%
2016	4,993,441.12	5,597,286.47	10,590,727.59	53%	6,557,265.48	4,186,894.45	10,744,159.93	39%
2017	4,524,342.45	33,625,871.24	38,150,213.69	88%	10,949,469.30	14,648,001.42	25,597,470.72	57%
Total	12,161,526.67	64,618,119.65	76,779,646.32	84%	30,093,964.85	31,909,797.92	62,003,762.77	51%
Average	4,053,842.22	21,539,373.22	25,593,215.44	84%	10,031,321.62	10,636,599.31	20,667,920.92	51%

Source; Compiled from ERCA annual reports

In respect of VAT, the table above depicted that birr 13,074,902.05(51%), birr 4,186,894.45(39%) and 14,648,001.42(57%) were not reported as VAT liability with in the years 2015, 2016 and 2017 respectively. This implies Birr 10,636,599.31(51%) on average didn't report as VAT liability per a year. It indicated the rate of tax payers not reported the exact tax liabilities on both income tax and VAT is more than 80% at each of the years audited. Even all of the audited tax payers in the year 2017 are tax defaulters.

In general, the result found from the analysis of both primary and secondary data have been approved that the level of tax evasion and avoidance is high.

4.2.5. Tax administration environment for tax evasion and avoidance

As depicted by table 4.2, 68% of the total respondents (of which 45.8% disagree and 22.2% strongly disagree) replied the system of tax administration in Ethiopia is efficient and effective whereas 4.2% strongly agree and 16.7% agree as it is efficient and effective. The remaining 11.1% of respondents were neutral with this.

Moreover, 57% (51.4% disagreed and 5.6% strongly disagreed) with the penalties imposed presently are enough deterrent to prevent potential tax defaulters whereas 5.6% strongly agreed and 23.6% agreed while 13.9% neutral with this. Furthermore, the average mean of the distribution of responses were found to be 3.46, which implies that more than half of the respondents agreed that the tax administration system in Ethiopia is inefficient and ineffective and the penalty imposed on tax defaulters at this time is not enough to prevent them.

Majority of the respondents i.e. 80.5% (of which 20.8% strongly agree and 59.7% agree) reported as the non-availability of the database of all taxable individuals by the revenue authority provides an opportunity for people to evade tax. In contrast, 9.7% disagree and 1.4% strongly disagree with this while the remaining 8.3% neutral.

About the experience of tax officials, majority of the respondents 83.3% (20.8% strongly agree and 62.5% agree) stated as there is shortage of experienced and highly motivated personnel for tax assessment and tax collection. On the other hand 5.6% of them disagree, 1.4% strongly disagrees and 8.3% were neutral with the issue.

In respect of tax assessment and collection procedures, 77.8% (of which 13.9% strongly agree and 63.9% agree) answered that the procedures for tax assessment and tax collection are ambiguous whereas 15.3% and 6.9% disagree and neutral respectively.

Respondents' opinion on the degree of punishment on tax defaulters, as replied by the majority, is that there should be meted out on tax defaulters. Among the respondents, 3.9% strongly agree and 48.6% agree whereas 26.4% disagree and 1.4% strongly disagrees with this. But 6.9% of respondents were neutral.

As shown by table 4.2, majority of the respondents, 75% (18.1% strongly agree and 56.9% agreed) reported that the government at all levels should make efforts towards fighting cases of tax offences. On the other hand 18.1%, 1.4% and 5.6% of the respondents were disagree, strongly disagree and neutral on the issue.

Finally respondents opinion towards the tax policies were assessed and the result implied is from the total respondents, 15.3% strongly agree and 36.1% agree that tax policies should be reviewed and updated constantly for an effective system to be in place whereas 36.1% disagree, 4.2% strongly disagree and 8.3% neutral towards the need of renewal and updating the existing tax policy.

Furthermore, the average mean of the distribution of responses were found to be 2.33, which indicates that more than half of the respondents agreed that none availability of data base, shortage of experienced personal for tax assessment and collection and ambiguity of tax assessment and collection procedures are factors for the existence tax evasion and avoidance. Thus, as implied by majority of the respondents there should be strict punishment on tax defaulters, the government at all level should effort towards fighting cases of tax offences and the existing tax policy should be reviewed and updated consistently for an effective system to be played.

Furthermore, the result found from the interview implied that to set a mechanism primary the cause of tax evasion and avoidance such as: lack of civilization, lack of fair trade, corruption, poor tax administration, weak enforcement, tax laws vague and not easily understandable should be identify by the tax payer. Therefore, providing continuous tax payer education, improve human resource capacity, improve the usage of information

technology, support those who compliant and enforcing by low those who do not compliant and conducting tax audit based on risk criteria can be mechanisms in controlling or minimizing tax evasion and a avoidance.

Generally these analyses assured that there are factors that lead tax payers to evasion and avoidance practices. Some of these are: the system of tax administration in Ethiopia is inefficient and ineffective, the non-availability of the database of all taxable individuals by the revenue authority provides an opportunity for people to evade tax, there is shortage of experienced and highly motivated personnel for tax assessment and tax collection, the procedures for tax assessment and tax collection are ambiguous. Hence, providing continuous tax payer education, improve human resource capacity, improve the usage of information technology, support those who compliant and enforcing by low those who do not compliant and conducting tax audit based on risk criteria can be mechanisms in controlling or minimizing tax evasion and a avoidance.

5. Conclusion and recommendations

Based on the presentation, analysis and interpretation of data, this part of the study summarizes and puts the general conclusions about Tax Evasion and Avoidance in Bahir Dar City. And it also recommends the controlling or minimizing mechanisms of tax evasion and avoidance.

5.1. Conclusion

Based on the analysis of primary and secondary data this study summarizes the following results are summarized. Tax payers have a trend of non-declaration and underreporting of income generated from their business.

Tax payers overstate business expense and deductions, overstate and understate trading stock, deduct personal expenses as business expenses, have the tendency of assuming minimizing tax liability is morally right and didn't declare their tax liability honestly. These all are symptoms of tax evasion and avoidance practices.

In general, the result found from the analysis of both primary and secondary data have been approved that the level of tax evasion and avoidance is high.

There are factors that lead tax payer's tax evasion and avoidance practices. Some of these are: the system of tax administration in Ethiopia is inefficient and ineffective, the non-availability of the database of all taxable individuals by the revenue authority provides an opportunity for people to evade tax, there is shortage of experienced and highly motivated person

nel for tax assessment and tax collection, the procedures for tax assessment and tax collection are ambiguous.

In conclusion, there is tax evasion and avoidance practice in Bahir Dar city. The major methods used by tax payers to evade and avoid tax are non- declaration and under reporting of income, overstating business expense and deductions, overstating and understating trading stock, deduct personal expenses as business expenses to hide the exact tax liability.

5.2. Recommendations

Based on the conclusions of this paper, the Researchers recommend the following points:

- Data base for tax administration at all levels of government should be promptly computerized to ensure that the system of information storage processing and retrieval is efficient.
- It is better for the taxing authority to fulfill the work position with competent and experienced personnel so as to audit and inspect the accounts of tax payers there by protecting income tax evasions. And there should be continuous training for tax officers on how to provide rapid and courteous service.
- The government should create tax compliance culture through education by creating for example pamphlets, newspapers, television
- advertisements, and public meetings with taxpayers and continuous education for citizenry has to be embarked upon and step has to be taken to convince the tax payers that the money collected in form of taxes are judiciously spent.
- The tax department should adopt scientific procedures in collecting data and selecting taxpayers for further audit and perform risk based tax audit. For example, tax assessors should audit prominent high-profile taxpayers than relatively small taxpayers who are not providing much revenue.
- The level of punishment should be stricter and the legal provisions for doing this should be clearly stated.
- This research conducted only focused on ERCA tax payers' found in Bahir Dar city and using descriptive data analysis method. Thus, the Researchers recommend that potential researchers conduct further researches by considering other tax payers and using other methods with in the area.

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