

Research Paper



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ASSESSMENT OF TAX EVASION TECHNIQUES OF BUSINESS PROFIT TAXPAYERS (A CASE STUDY ON DESSIE, WOLDIYA, & KEMISSIE TOWNS)

Tsega Zemen Fantaye¹¹Department of Accounting and Finance, Wollo University, Dessie, Ethiopia

ABSTRACT

Tax is a compulsory payment by an economic unit to a government without the expectation of proportional benefit from the government. In an ideal world, all taxpayers would voluntarily pay their taxes and comply with all of their tax obligations willingly. But in fact, no one enjoys by paying tax to the government and as much as possible every economic unit tries to minimize its tax burden by any means. The general objective of the study was to assess the possible techniques of tax evasion for business profit tax. Descriptive research design and two stage sampling techniques were applied to achieve the study objectives. Further, the study used both primary and secondary data as well as data were analyzed using descriptive statistics after the data were coded and filled using the latest version of SPSS. The study identified the possible techniques of tax evasion as acquiring goods without receiving relevant and legal supporting documents from the suppliers from various corners of the country especially from the capital city of Ethiopia-Addis Ababa, doing businesses illegally, overlooking economic transactions and lack of taxpayers' honesties to give true and legal receipts to their clients at the time of selling products, availability of fabricated business contractual agreement made with partners at time when renting properties or making a promise to provide certain products, not recording business transactions and provide financial statements to the tax authority on the expected time, availability of diversified financial statements by the taxpayers which may be used for various purposes, unethical behavior of authorized accountants, violating GAAP in preparing F/S, and the government's limitations in relation to controlling the business peoples' store, confirming sold and unsold goods of the business people, auditing business profit taxpayers' F/S, and creating adequate awareness about the advantages of maintaining book of accounts and preparing F/S to business profit taxpayers. Finally the study also forwarded credible recommendations to the tax offices in order to block tax evasion techniques in the study areas.

KEYWORDS: Tax, taxpayers, Governments, tax evasion, public services

INTRODUCTION

Taxes are collected to finance government expenditure. Government expenditure encompasses the provision of vital public services such as national security, maintenance of law and order, health care, education and training, disaster relief and infrastructure. There for it is vital that government act to prevent tax

evasion (which is illegal) and to control tax avoidance, since both the result in less tax being paid (Gupta, 2010).

The provision of public infrastructure and government services is a key factor for economic development. In many developing countries, 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. A lack of tax revenue is one of them. In 2005, the average tax revenue to GDP ratio in the developed world was approximately 35%. In the developing countries, it was approximately 15%, and in the poorest of these countries, the group of low income countries, tax revenue was just 12% of GDP. This gap can partly be explained by the fact that demand for public services increases more than proportionally as income rises. But it also reflects weaknesses in the ability of developing countries to raise the revenue required for the provision of adequate public services (Cob ham, 2006).

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. The domestic component of tax evasion and avoidance would include, for instance, non-declared or under-reported income from work or domestic business activities. The international component of tax avoidance and evasion includes practices like transfer price manipulation by multinational firms or the holding of financial assets in offshore bank accounts by private individuals with the purpose of concealing capital income.

STATEMENT OF THE PROBLEM

Governments have great responsibility to fulfill public needs and protect their nations from both internal and external divergence. In order to do these responsibilities government has different opportunities to get finance such as tax, donation, service provision, selling assets, penalties, and so on. However, tax is the major source and also risk free from direct and indirect influence of social, political, cultural and moral issues unlike donation.

Governments have the right to collect different types of taxes directly or indirectly from citizens. To collect true amount of tax, government should establish suitable and moderate tax system and should have ethical as well as skillful tax officers. In addition, tax awareness creation should be made to citizens in different mechanisms like using media, brusher, education, panel discussion, giving reward for true taxpayers, and so on.

Previous studies in USA, Malaysia, Check Republic, Chaina, Kenya, Uganda, and Tanzania revealed that large company owners evaded their taxable income by hiding their transactions, underreporting

significant revenues, and by reporting window dressing expenses in their financial statements.

OBJECTIVES OF THE STUDY

The study also had the following specific objectives.

1. To assess the level of the tax offices for ensuring business profit taxpayers in relation to keeping and providing reliable supporting documents for their transactions in the study area.
 2. To assess the tax offices' effectiveness in checking the reliability and uniformity of business profit taxpayers recorded book of accounts and financial statements within the budget year in the study area.
 3. To evaluate how the tax offices confirm the reliability of legal contract agreement documents of business profit taxpayers with their business partners in relation to their business activities.
 4. To investigate the tax offices controlling effort to business profit taxpayers in presenting and recording relevant expenses on their permanent books of accounts and report on their financial statements.
- ✚ a bench mark for further research in the study area

RESEARCH DESIGN

In this study the researcher employed descriptive research design. This is because the study is designed to describe the methods how business people evade their taxable income.

SAMPLE SIZE AND SAMPLING TECHNIQUE

The study was used two stage sampling. In the first stage, the researcher was purposively select Dessie, Woldiya, & Kemisie towns. This is because the above towns are the main research boundary areas of Wollo University and also these towns have large number of taxpayers. Thus, non-probability particularly purposive sampling applied in the first stage. In the second stage, the study selected 200 tax officers in the above three towns randomly out of the total of 543 tax officers using the following formula. Hence, random sampling was the second sampling technique that will be applied in this study.

According to the tax offices report, currently there are 198 tax officers in Dessie town tax office, 180 tax officers in Woldiya town tax office, and 165 tax officers in Kemmissie town tax office.

$$n = \frac{Z^2 pqN}{e^2(N - 1) + Z^2 pq}$$

Where: n=sample size; p= the maximum population proportion; q=p-1; N= number of population size; Z= standardized normal variable and its value that corresponds to 95 % confidence interval equals 1.96; p = 0.5 and e = allowable error (0.05).

Therefore, n = 200 of which 198/543x200=73 will be taken as a sample from Dessie town tax office employees, 180/543x200= 66 will be taken as a sample from Woldiya town tax office employees, and 165/543 x 200= 61 will be taken as a sample from Kemmissie town tax office employees.

Data type and Data Collection Method

In order to achieve the objective of the study, the researcher used primary data for discussion and analysis as well as secondary data such as literatures, articles, manuals, and websites for review of related literature. The secondary data were obtained by reviewing websites, manual, and annual report using.

Data Analysis and Interpretation

After the data were collected and sorted in a systematic manner, the researcher had been analyzed and interpreted using quantitative and qualitative approaches. Data gathered through close ended questionnaires had been analyzed using frequencies, percentage, mean and standard deviation, whereas data gathered through interviews and document reviews were analyzed through description and narrations.

Dependent and explanatory variables

Dependent variable: The dependent variable for the study is the techniques of tax evasion.

The following are the explanatory variable for the study:

- ❑ Availability of reliable and legal supporting documents for each transaction.
- ❑ Taxpayers’ experience in recording all of their transactions in permanent books of accounts and prepare uniform f/s for various purposes.

GENERAL INFORMATION

In respect to the general background of the respondents, the profile questions were addressed about their gender, level of education, work experience, and their job title. The responses were summarized as follows.

The above research provided that out of 170 taxpayers 122 (72%) were males and 48 (28 %) were females.

As for the respondents’ education level; 29 (17%) of them were diploma holders, 133(78%) have first degree, and the rest 8(5%) have masters degree.

Regarding their work experience, 26 (15%) of the respondents have less than one year experience, 56 (33%) of the respondents have 1-3 years work experience, 45(27%) of them have 4-5 year experience and the remaining 43(25 %) of them have more than 5 year work experience.

Out of the total respondents 36 (21%) were internal auditors of the tax offices, 53 (31%) were tax assessor, 8 (4 %) were daily cash collectors, 13 (7%) were tax educators, 3 (1%) were head of the tax offices and the remaining 57 (36 %) were assigned on different positions such as human resource, data base, customer service, accountant and so on.

The above data generally indicated that more of the respondents were male, degree holders, and well experienced. This implied that the authority had well educated as well as experienced currently in the study area.

Maintaining supporting documents practices of business peoples for their transactions

SL NO		Response					Frequency							
		S.A	A	D	S.D	N	Total	S.A	A	D	S.D	N	Total	
1	The business people in your town acquired all of their merchandises using legal receipts	7	50	87	20	6		4	29	52	12	3		
	Total						170							100%
2	The business people in your town doing their business legally	4	68	70	22	6	170	2	40	41	13	4		
	Total						170							100%



3	The business people in your town give receipts to their customer for every transaction	8	3 4	9 5	28	5		5	2 0	5 6	16	3	
	Total						170						100%
4	The business people in your town have legal and true documents for their business contractual agreements	9	7 3	5 2	26	1 0		5	4 3	3 1	15	6	
	Total						170						100%

Survey result, 2015

According to the above table 2, 7(4%) of the respondents were strongly agree; 50(29%) of them were agree; 87(52%) of them were disagree; 20(12%) of them were strongly disagree; and the rest 6(3%) of them became neutral about the acquisition of merchandises using receiving legal documents by business people in the study areas.

This implied that most of the business people in the study areas acquired goods without receiving relevant and legal supporting documents from the suppliers from various corners of the country. As the respondents stated in the open ended question, suppliers of merchandises which are particularly located in Addis Ababa are not willing to give legal receipts that indicate the true price of the goods sold to their customers.

On the other hand; 4(2%) of the respondents strongly agree, 68(40%) of them were agree, 70(41%) of them were disagree, 22(13%) of them strongly disagree, and the remaining 6(4%) of them were neutral about the issue whether business people in the study areas run their business legally.

This implied that though the government is trying to minimize illegal business practices, still there are more and more people that are doing their business illegally in the study areas.

In addition; 8(5%) of the respondents strongly agree, 34(20%) of them were agree, 95(56%) of them were disagree, 28(16%) of them strongly disagree, and the remaining 5(3%) of them were neutral about the issue whether business people in the study areas sold their products by giving true and legal receipts to their clients.

This implied that though business peoples specially category 'A' and 'B' taxpayers are legally required to use either manual or cash register machine to record their sales transactions and should give receipt that indicates the actual selling price of products to their customers, there are currently more taxpayers in the study areas that do not record their transactions and give true and legal receipts to their clients at the time of selling products.

Further, 9(5%) of the respondents strongly agree, 73(43%) of them were agree, 52(31%) of them were disagree, 26(15%) of them strongly disagree, and the rest 10(6%) of them were neutral about the issue whether business people in the study areas have legal and true documents for their business contractual agreements.

This implied that still there are business peoples that hide their revenue and have different contractual agreements for the same product from their business partners in the study areas as a result they evaded their true taxable income.

4.2.2 Keeping book of accounts for business transactions and preparing financial statements

Recording and preparation of financial statements practice of business people for their economic transactions

S.NO.		Response						Frequency						
		S.A	A	D	S.D	N	Total	S.A	A	D	S.D	N		
1	The business people in your town record and report their transactions to the tax authority on time	11	78	62	11	8		7	46	35	7	5		
	Total							170						100%
2	It is believed that business people may prepare diversified financial statements for the same fiscal year	8	88	37	15	17		5	53	23	9	10		
	Total							170						100%
3	Most authorized accountants may record and prepare financial statements based on the interest of their clients	19	87	35	18	11		11	52	21	10	6		
	Total							170						100%
4	The business people in your town do not violate GAAP at the time of recording business transactions and prepare financial statements	6	59	74	21	10		3	35	44	12	6		
	Total							170						100%

Survey result, 2015

As shown in the above table 3, 11(7%) of the respondents were strongly agree; 78(46%) of them were agree; 62(35%) of them were disagree; 11(7%) of them were strongly disagree; and the rest 8(5%) of them became neutral about the timely recording of business transactions and reporting of financial statements to the tax authority by business people in the study areas.

This implied that most of the business people in the study areas record business transactions and provide financial statements to the tax authority on the expected time, but still there are taxpayers who failed to do so though the tax rules and regulations require category ‘‘A’’ and ‘‘B’’ taxpayers to keep book of accounts and prepare necessary financial statements for their economic transactions for each budget period and then report to the tax authority based on the stated period.

Beside; 8(5%) of the respondents strongly agree, 88(53%) of them were agree, 37(23%) of them were disagree, 15(9%) of them strongly disagree, and the other 17(10%) of them were neutral about the issue business people may prepare diversified financial

statements for the same fiscal year in the study areas.

This implied that most of the respondents believed that business profit taxpayers are expected to have diversified financial statements which may be used for various purposes such as for financial institutions to request loan, for the tax office to levy and pay their tax liability, for potential investors to attract them in order to invest in their business, and so on for the same fiscal year in the study areas.

On the other hand; 19(11%) of the respondents strongly agree, 87(52%) of them were agree, 35(21%) of them were disagree, 18(10%) of them strongly disagree, and the remaining 11(6%) of them were neutral about the issue authorized accountants may record and prepare financial statements based on the interest of their clients in the study areas.

This implied that majority of the authorized accountants who are working in the study areas prepared financial statements’ of the interest of their clients rather than based on the acceptable accounting principles for the purpose of not to lose their clients, which is unethical. As the study revealed in the open ended

questions, there are also some authorized accountants who rent their stamp to others for the financial statements that are not prepared by their own selves.

Moreover, 6(3%) of the respondents strongly agree, 59(35%) of them were agree, 74(44%) of them were disagree, 21(12%) of them strongly disagree, and the rest 10(6%) of them were neutral about the issue whether business people in the study areas do not violate GAAP at the time of recording business transactions and prepare financial statements.

This implied that still there are business peoples that have permanently hired accountant that hide their revenue by violating GAAP at the time of recording business transactions and prepare financial statements and not paying true amount of tax to the government in the study areas.

The tax office’s effort to minimize tax evasion for business people

The government effort to minimize evasion for business profit tax

S. N O.		Response					Frequency						
		S.A	A	D	S.D	N	Total	S.A	A	D	S.D	N	Total
1	The tax office’s effort in your town is effective in relation to controlling the business peoples’ store	13	66	61	19	11		8	39	36	11	6	
	Total						170						100%
2	The tax office’s effort in your town is effective in relation to checking sold and unsold goods of the business people	13	59	53	42	3		8	35	31	25	1	
	Total						170						100%
3	The tax office’s effort in your town is effective in relation to auditing business profit taxpayers’ F/S	8	93	47	12	10		5	55	27	7	6	
	Total						170						100%
4	The tax office’s effort in your town is effective in relation to creating adequate awareness about the advantages of maintaining book of accounts and preparing F/S to business profit taxpayers	10	83	53	16	8		6	49	31	9	5	
	Total						170						100%

Survey result, 2015

Based on the above table 4, 13(8%) of the respondents were strongly agree; 66(39%) of them were agree; 61(36%) of them were disagree; 19(11%) of them were strongly disagree; and the rest 11(6%) of them became neutral about the effectiveness of the tax offices’ effort in relation to controlling the business peoples’ store in the study areas.

This implied that the tax offices in the study areas have significant limitation in relation to controlling properly the warehouse of business profit taxpayers in order to know the size of the goods available for sale and guess their tax liability for a given budget period.

On the other hand; 13(8%) of the respondents strongly agree, 59(35%) of them were agree, 53(31%) of them were disagree, 42(25%) of them strongly disagree,

and the remaining 3(1%) of them were neutral about the effectiveness of the tax offices’ effort in relation to confirming sold and unsold goods of the business people in the study areas.

This implied that the tax offices in the study areas have serious problem in relation to checking sold and unsold goods of the business people in the study areas as a result unable to estimate the true amount of the taxpayers’ tax liability.

In addition; 8(5%) of the respondents strongly agree, 93(55%) of them were agree, 47(27%) of them were disagree, 12(7%) of them strongly disagree, and the remaining 10(6%) of them were neutral about the effectiveness of the tax offices’ effort in relation to auditing of business profit taxpayers’ F/S in the study areas.



This implied that the tax offices' effort in the study areas in relation to auditing business profit taxpayers' F/S is encouraging though it needs better improvement.

Finally, 10(6%) of the respondents strongly agree, 83(49%) of them were agree, 53(31%) of them were disagree, 16(9%) of them strongly disagree, and the rest 8(5%) of them were neutral about the effectiveness of the tax offices' effort in relation to creating adequate awareness about the advantages of maintaining book of accounts and preparing F/S to business profit taxpayers in the study areas.

This implied that still the tax offices effort for awareness creation in the study areas with regard to the advantages of maintaining book of accounts and preparing F/S to business profit taxpayers is not adequate even though there is undeniable change.

FINDINGS

- ▶ Most of the business people in the study areas acquired goods without receiving relevant and legal supporting documents from the suppliers from various corners of the country especially from the capital city of Ethiopia-Addis Ababa.
- ▶ Even though the government is trying to minimize illegal business practices, still there are more and more people that are doing illegal business in the study areas.
- ▶ Even if business peoples particularly category "A" and "B" taxpayers are legally required to use either manual or cash register machine to record their sales transactions and should give receipt that indicates the actual selling price of products to their customers, there are currently more taxpayers in the study areas that overlook their transactions and do not give true and legal receipts to their clients at the time of selling products.
- ▶ Still there are business peoples that have fabricated business contractual agreement from their business partners at time when renting their property or making a promise to provide certain products in the study areas.
- ▶ Still there are business peoples that have permanently hired accountant that hide their revenue by violating GAAP at the time of recording business transactions and prepare financial statements in the study areas.

SUGGESTIONS

- ↳ Since suppliers of goods who are found in Addis Ababa are not volunteer to give true

and legal receipts to their business partners in the study areas, the Tax Revenue and Custom duty Bureau of Amhara Regional State together with other concerned government body should work with Addis Ababa city administration in order to take legal measurement for those business peoples who are selling goods without giving true and legal receipts or with legal receipts that revealed fictitious price of goods.

- ↳ The tax offices together with trade, investment and market development offices in the study areas should work jointly such as creating awareness about the rights and obligations of business people before giving trade license, taking care about the history and working address of peoples who are requesting trade license, and taking legal measurement for those peoples who are doing business without getting trade license in order to minimize the number of peoples who are doing business either without having legal trade license or with fabricated trade license.
- ↳ The tax offices in the study areas should compare and contrast the amount of revenue generated by renting a certain property or by providing services with that of the amount expense of the taxpayers' business partners which is revealed on the two parties profit or loss statement.
- ↳ The tax offices in the study areas should be serious in penalizing and not compromise with those business profit taxpayers either who fail to have supporting documents and keeping book of accounts for their business transactions as well as preparing financial statements or whose financial statements are not accepted by the tax offices due to violation of Generally Accepted Accounting Principles (GAAP).

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