

FACTORS AFFECTING VOLUNTARY COMPLIANCE OF CATEGORY 'C' TAXPAYERS' ATTITUDE OF ARBA MINCH, SNNPR, ETHIOPIA

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Abstract: This study aimed to assess tax payers' attitude on factors that affect voluntary compliance of category 'C' taxpayers in Arba Minch City, SNNPR, Ethiopia. The factors like equity and fairness of the tax system, level of awareness of taxpayers, effectiveness and efficiency of tax authority, socio-cultural factors and political factors. To achieve this objective of the study primary source of data was employed via self-administered questionnaires which include both open and close ended questions from the sampled category 'C' tax payers. The study found lack of awareness as major and leading reason for non-existence of voluntary compliance among category 'C' tax payers. Further, efficiency and effectiveness of the authority in improving the tax assessment and collection procedures, creating awareness, enforcing the tax law positively affect voluntary tax compliance of tax payers. Socio-cultural factors also affect attitude of taxpayers towards taxation positively as well as negatively. However, political related factors were found insignificant in this survey.

Key Words: Factors, Voluntary Compliance, Category 'C' Taxpayers', Arba Minch

1. Introduction

The exact meaning of tax compliance has been defined in various ways. Alm (1999) and Jackson and Milliron (2001) defined tax compliance as the reporting of all incomes and payment of all taxes by fulfilling the provisions of laws, regulations and court judgments. Another definition of tax compliance is a person's act of filing their tax returns, declaring all taxable income accurately, and disbursing all payable taxes within the stipulated period without having to wait for follow-up actions from the authority (Singh, 2003). Furthermore, tax compliance has also been segregated into two perspectives, namely compliance in terms of administration and compliance in terms of completing (accuracy) the tax returns (Harris, 2006).

The taxpayers' attitude on compliance may be influenced by many factors, which eventually influence taxpayer's behavior. Those factors which influence tax compliance and/or non-compliance behavior are differing from one country to another and also from one individual to another (Kirchler, 2007). They include taxpayers perceptions of the tax system and Revenue Authority, peer attitude / subjective norms; taxpayers' understanding of the tax system / tax laws, motivation such as rewards and punishment such as penalties, cost of

compliance, enforcement efforts such as audit; probability of, detection; difference across - culture; perceived behavioral control, ethics / morality of the taxpayer and tax collector; equity of the tax systems; demographic factors such as sex, age, education and size of income (Murphy, 2004) and use of informants.

Tax compliance leads to increases in income and decreases in tax rates. Compliance is also greater when the individuals perceive some benefits from a public good funded by the tax payments while changes in fine rates appear to have little effect on tax compliance behavior (Murphy, 2004). It therefore appears that there are additional tax policy instruments beyond the standard prescription of enforcement actions that government can enact to achieve its desired degree of compliance with the tax laws. In fact, some of these standard instruments - greater penalties - may be largely ineffective in increasing tax compliance. In short, government should pursue a range of approaches in its efforts to promote compliance. Thus, the payment of fines and penalties appear for overdue taxes. These arises the need to allow audit by tax collectors if deemed necessary, especially if they suspect that there is some kind of some tax non-compliance. A key component of any tax system is the manner in which it is administered. "No tax is better than its administration, so tax administration matters a lot and an essential objective of tax administration is to ensure the maximum possible compliance by taxpayers of all types with their taxation obligations. Unfortunately, in many developing countries, tax administration is "usually weak and characterized by extensive evasion, corruption and coercion & non-compliance. In many cases overall tax levels are low, and large sectors of the informal economy escape the tax net entirely.

Ethiopia, like any other developing countries, faces difficulty in raising revenue to the level required for the promotion of economic growth. Hence, the country has been experienced a consistent surplus of expenditure over revenue for sufficiently long period of time. To address this problem, the government categorized tax payers into three categories & introduced imposition of tax (direct and indirect), among others; as major and important sources of public revenue. However, this categorization & imposition of tax couldn't still bring the required result due to a number of reasons such as lack of clear understanding about the tax system by the taxpayers, taxpayers don't comply with their tax obligation, hostility between the taxpayers and tax officials, negative attitude of taxpayer towards the tax system, that is, understating their taxable income by significant amount,... etc. For these reasons, the actual amount of tax couldn't be collected properly (Tadele, 2010).

Despite the fact that people need to pay taxes based on rationales of vertical and horizontal equities, it is not always the case that tax systems are comprehensible and transparent for category 'C' tax payers especially for those who are less literate individuals. Tax systems are usually not elaborated properly with the society. Consequently, these taxpayers complain that the tax assessment method is based on subjective estimation as a result of which they are frequently subjected to over-taxation. The extent of the impact of attitudes and attitudinal change on voluntary tax compliance behavior was not well understood. Hence the study aimed to answer the following basic research questions at the end:-

- What are factors influence the attitude of category 'C' tax payers and their level of voluntary compliance with the tax system in Arba Minch city?
- What are problems related to the overall taxation system, tax assessment, collection and service delivery of tax authorities?
- What activities were implemented to create voluntarily compliant taxpayer & to narrow the gaps and work for the better of the business community and the government by the revenue authority?

2. Taxation in Ethiopia

The history of taxation in Ethiopia has a relationship with the government structures of the country; there exist hardly any reliable documentary evidences to justify the relation of emergence of government and taxation, when exactly taxation was introduced. Different stories and evidences point out that Emperor Zeria-Yakob started taxation in Ethiopia during the 15th century. Governments which came to power in Ethiopia at different periods have frequently revised and repealed the statutory bases for various types of taxes providing for tax

bases and tax rates, time and mode payment, exemptions and offenses. However, there has been no document or materials produced which compiles tax proclamations issued at different periods. The initial statutory bases for all the tax proclamations was the 1931 Constitution of Ethiopia which later revised and become Revised Constitution of Ethiopia. Because most of the products on which tax was levied (tax bases) were agricultural products, the type of taxation in traditional periods was unstructured and mostly in kind. Taxation in that period was varying highly from area to area and was often arbitrary, i.e. the amount to pay and the mode of payment depends on the will of the chief tax collector and the kind of resources available in the area (Lemessa, 2005).

According to the Constitution of Federal Democratic Republic of Ethiopia, revenue sources are assigned between Federal government and Regional states. Regional states can endorse their income tax proclamation and regulations based on the constitution in conformity with the federal income tax proclamation. According to the current federal income tax proclamation no.286/2002 taxpayers are categorized into three categories, namely category “A”, “B”, and “C” based on their volume of sales and form of business.

Category “A” includes any company incorporated under the tax law of Ethiopia or in or a foreign country and other entities having annual turnover of Birr 500,000 and more. Those who are categorized under “A” have to maintain all records and accounts which will enable them to submit a balance sheet and profit and loss account disclosing the gross profit, general and administrative expenses, depreciation, and provisions and reserves together with supporting vouchers (Council of Ministers Regulation no. 78/2002: Article 18, Sub Article 2).

Category ‘B’ includes those enterprises having annual turnover of more than Birr 100,000 and less than Birr 500,000. This category of taxpayers must submit profit and loss statement at the end of the year. The law requires all entries in the records and accounts to be supported by appropriate vouchers (Council of Ministers Regulation no. 78/2002: Article 18, Sub Article 2).

Category ‘C’ unless already classified in categories ‘A’ and ‘B’ include those taxpayers whose annual turnover is estimated by the Tax Authority at Birr 100,000 or less. On the other hand, standard assessment is used to determine the income tax liability of Category ‘C’ taxpayers. This type of assessment is a fixed amount of tax determined in accordance with the Council of Ministers Regulation established Schedules. This category of taxpayers is the most problematic category of taxpayers and it is considered as hard to tax group. This is due to the fact that these taxpayers pay taxes at fixed rate on the income estimated by tax administration.

3. Literature review

In this literature review basic concepts about voluntary tax compliance, characteristics of good tax system, factors determining tax compliance such as attitude of tax payers, socio-cultural, political legal, administrative and ethical issues were addressed.

The problem of voluntary tax compliance is as old as taxes themselves. Characterizing and explaining the observed patterns of tax non-compliance, and ultimately finding ways to reduce it, are of obvious importance to nations around the world (Andreoni et al, 1998).The attitudes of the taxpayers (Bhatia, 2001) in this regard are influenced by a host of other factors like the political situation, natural calamities, economic situations, socio cultural and so on. Due and Friedlaender (1999) also state that a person’s preference for a tax may be influenced if the tax- or an increase in it- is tied directly to the expenditures he strongly favors. Generally, attitudes toward choice of taxes and tax structures are greatly influenced by various criteria- often called principles- of taxation that have come to be widely accepted.

As stated in (James, 2000) a good tax system is one which is designed on the basis of an appropriate set of principles, such as equality or fairness and certainty. Since fairness of a tax system is a corner stone for the tax system.Brooks (2001) also states that fairness has always been widely regarded as the most important criteria in

judging a tax system. The problem of unfairness is that a tax system allows taxes to be shifted from dishonest to honest taxpayers. According to Bhatia (2001), the attitude of taxpayers is an important variable determining the contents of a good tax system. It may be assumed that each taxpayer would like to be exempted from paying tax, while he would not mind if others bear that burden. In any case, he would want his share to be within the general level of tax burden being borne by others. If this is not so, he will feel exploited. To sum, regardless of this inherent problem ensuring the fairness or equity of a tax system is second to nothing. To put it differently, it is essential that a good tax system should appear equitable to the tax payers.

Organizational Strength of tax authorities is indicated by many scholars. According to Bird and Oldman (2003), no tax will work effectively, unless its administrators maintain an aggressive attitude with respect to the correctness of the taxpayers' actions. Some taxpayers will fail to file or make mistakes through ignorance or neglect; others will deliberately cheat. A passive attitude by the authorities towards these errors and falsifications will soon undermine the entire structure, since the diligent and honest taxpayers will almost in self-defense be forced to the level of the careless and dishonest. A tax administration which seeks voluntary compliance must protect those who comply or else compliance will not be forthcoming. Bird and Oldman (2003) further state that the sure sign of ineffective tax administration is the presence of a very large delinquency in tax payments for it indicates the lack of taxpayer respect for the tax system. The taxpayer in effect is acting on his belief that the administrative machinery may bark, but that it has no bite. These writers argue that in large part the solution for the large delinquency lies in providing the bite. In this sense effective tax collection is a facet of the larger problem of providing adequate penalties, to which reference will later be made. In other words tax is evaded to the extent that tax authorities are perceived as weak by taxpayers. Lemessa (2005) states that tax systems that depend on ad hoc administrative procedures rapidly become discredited and endanger voluntary compliance.

James (2000) argues that the norm is usually to comply rather than not to comply. As already pointed out for a tax system to be effective the majority of the taxpayers have to comply. It follows that there may be greater gains in assisting basically compliant taxpayers to meet their fiscal obligations than in spending more resources in pursuing the minority of non-compliers. Many taxpayers might be willing to comply in full, but are unable to do so because they are not aware of, or do not understand, their full obligations. Even if such tax payers understand their obligations, they may not know how to meet them or may be unable to do so for other reasons. On other side, other writers such as Smith and Kinsey (1987) argue that tax noncompliance is an intentional behavior. In countries like Ethiopia where most of the business community have no access to information, lack of awareness cannot simply be overlooked rather it can be assumed as a major determinant of tax compliance behavior.

According to Fjeldstad and Ranker (2003), increased efficiency of the tax administration, however, is not enough. Many observers conclude that a lack of paying tax 'culture' is the largest obstacle to building a firm long-term revenue base. The opposite may, however, also be the case: as long as the tax administration culture is perceived to be influenced by sectarianism, nepotism, and corruption, it is unlikely to contribute to the fostering of a more conducive paying tax culture. It is pointed out by Adams (2003) that the success of income tax rests primarily upon the honesty of taxpayers. Adams further states that one of the factors that contribute to the dishonesty of the taxpayers is the complexity of the tax system, as it may lead to administrative failures. This can be viewed as it has relation with the tax culture of the society. Practically it is difficult to obtain genuine information from taxpayers regarding their income. Hence, tax gap is created to the extent the taxpayers hide information regarding their business activity.

Lack of ability to pay, this issue holds true in Ethiopia also where several small business operators (category 'c' taxpayers) are accumulating their annual tax obligations due to lack of ability to pay. Generally when taxpayers have no enough disposable income and they used to consume the return from sales, it is clear that tax evasion is inevitable and leads to tax arrears (Lemessa, 2005)

Social factors, the issue of (non-) compliance is not only a question of state-society relationships but also a question of relationship between citizens and/ or groups of citizens within local communities. There is an existing social bond between the society and this bond influences the members of the society in complying with the tax law. That is taxpayers may be influenced by their peer groups to voluntarily comply or not to comply with the tax law. As cited by Slemrod (2000), the dimension of trust that seems to affect compliance is trust in other citizens to pay their share of service charges. In particular, trust in other citizens to pay their share seems to be important. The larger the fraction of the local population that is observed not paying, the lower perceived risk of being prosecuted. This has impacts on the individual taxpayer's perception of the credibility and trustworthiness of the revenue administration.

Attitudes towards the government (Levi, 2005) may affect the taxpayer's normative commitment to comply with law. Similarly, Due and Friedlaender (1999), also argue that, attitudes toward the general level of taxation and tax increases are dependent, of course, on attitudes about the desirability of governmental programs and on attitudes toward the government itself. On the other hand, citizens' willingness to pay taxes voluntarily rests on the local government's capacity to provide services and its demonstrated readiness to secure the compliance of the otherwise non-compliant.

Empirical literatures related tax compliance factors in Ethiopia also show similar results. For instance, Yohannes Mengesha and Zerihun Ashebir (2013), study conducted on identifying the gaps and problems that exist between the Dire Dawa business community and the tax authority results show that most of the taxpayers, especially those in the category 'C', do not exactly know how the tax is assessed or calculated and the procedures in the tax assessment and computations are not objectively understood by most of the taxpayers. The finding also reveals, over taxation as result of over estimation of daily/annual income, Nontransparent, non-participatory standard assessment by the authority on category "C taxpayers", Lack of fairness or equity of taxation among similar businesses of category "C taxpayers" Poor tax laws enforcement especially for VAT and large number of tax defaulters, Poor communication and understanding between the tax authority and taxpayers, Weakness in tax collection and unsatisfactory service delivery of tax authority.

Study conducted by Suresh Vadde and Srinivas Gundarapu (2010), on major factors that influence attitudes of rental taxpayers and their compliance behavior with tax system in mekele city administration. The study indicated that there were some dishonest rental tax payers. Even there are some individually who entirely don't report their taxable income to the concerned body. In addition to the above, the study also disclosed that with the exception of minority of the rental tax payers who hold certificate and diploma, majority of them were with an educational background of elementary and high school completed. Hence, it can be concluded that rental tax payers lack knowledge of easily understanding the laws and regulations of the tax system and how their taxable income is computed. Therefore, it can be concluded that still many respondents are not attending or participating in the tax training session.

Wollela A Yesegat and Helge Fjeldstad, (2011) jointly conduct study on tax payers views of business taxation in Ethiopia. The objectives of their study were to assess business peoples' views of paying taxes in Ethiopia and to identify (perceived) difficulties with the tax system and priorities for tax reform. Hence the result shows that the main reasons for tax noncompliance were; lack of predictability in the tax system forces taxpayers to reduce their current tax liability, difficult to compete with businesses that import goods at manipulated custom duties, It is those who are not paying taxes that are quickly growing, so why should I comply, discrimination by the tax administration forces honest taxpayers to evade taxes. Nuguss et' al (2014) conduct study on the consequences of tax assessment on tax collection of category 'c' taxpayers in Ethiopia: a case study in Mekelle city, Tigray. The study result shows that unless good service delivery is provided, tax related laws are enforced and implemented, effective awareness creation is done and fair tax assessment is conducted, there may not be efficient and effective tax collection. Even though efficient tax assessment and collection cannot be made overnight, it is up to tax administrators to ensure sufficient tax revenue. Multiple approaches are needed to enhance tax collection efficiency. No single approach is likely to fully and effectively address the tax collection

efficiency of category ‘C’. Since it has multiple causes of tax related problems, the category “C” tax payers needs more attention.

4. Research Methodology

Research Design

The research design selected for this study was descriptive research design. Descriptive studies are non-experimental researches that describe the characteristics of a particular individual, or of a group. It deals with the relationship between variables and development of generalizations and use of theories that have universal validity. It also involves events that have already taken place and may be related to present conditions (Kothari, 2004)

Target Population

The target population was category ‘C’ tax payers(are those tax payers whose annual turnover is up to or less than100,000ETB & standard assessment method shall be used to determine their income tax liability)according to income tax regulation number 78/2002. According to the Arba Minch City Tax revenue office report during the last June 2008 E.C the total number of category ‘C’ tax payers in four sub cities were Sikella (1,325), Secha (635), Abaya (610), & those of Nech-sar (734) amounting a total population of 3,304. Hence the total population of the study will be 3,304.

Sampling Technique & Sample Size

The sampling technique might have its own draw back while inferring the findings based on the sample data to the whole population. To minimize this error appropriate sample size will be taken and greater effort and caution was also undertaken to make the samples as representative as possible. The population of the study was category 'C' tax payers of the city due to the fact that these tax payers are not required by law to declare their income or keep books of account, and considered as hard-to tax group. Four city Kebeles will be selected out of eleven based on the density of these taxpayers. That is, these Kebele’s are densely populated business areas so that they can represent the remaining; this follows the concept of purposive sampling. Then proportional numbers of samples (tax payers) were allocated and which can be considered as strata and samples will be randomly drawn from each Kebele’s/ strata’s. To select the required sample size, Michael Savin (1960) model were adopted.

Table 1.1: The distribution of taxpayers in sample Kebeles’(Mandals)

S.N.	Name, Kebeles	Population	Sample Size	Percentage
1	Menehariya	356	18	22
2	Dilfana	678	34	42
3	Mehalketema	263	13	16
4	Wuha Minch	328	16	20
	Total	1,625	81	100

Source:- Primary Data

Data Sourceand Method of Data Collection

This study was used primary source of data to get pertinent information. The required data was collected via self-administered questionnaires which include both open and close ended questions from the sampled category ‘C’ taxpayers.For collecting the data suitable technique was used depending up on the nature of data. The primary data was collected from 81 category ‘C’ tax payers by using closed and open- ended self-administered questioner. Using questionnaire as data collecting tool is, due to its ability to generate relevant information as compared to others data collecting instruments which enhances the problem solving ability of the study (Greener, 2008).

Method of Analysis and Interpretation

Data analysis is very important aspect of this paper, as it basically involves the analysis of all the data that were collected. The data collected needs to be analyzed so that can be easily deducing in order to provide the justification for the work will be done during research. Data analysis is a body of methods that help to describe facts, detect patterns, develop explanations and test hypothesis. Having the goal of this study in mind, the raw

data are processed by tabulating and classifying each response provided by respondent. The data were analyzed, presented and interpreted using descriptive statistics method with table and percentage.

5. Survey Result and Analysis

This section contains survey result and analysis on the data collected from the respondents of the study. The survey covered 81 sample taxpayers from 1,625 category 'C' target taxpayers. The sample constitutes around 5% of the target population. Questionnaires were distributed to these 81 taxpayers and only 68 taxpayers responded. This shows approximately 84% response rate.

Distribution of business sectors

The Income Tax Regulation No. 78/2002 categorize business sector in Ethiopia in 69 different business sector, for the purpose of this study only the major ones were surveyed and their distribution is presented in the table 1.2.

Table 1.2: Distribution of business sectors included in the sample

S.N	Business Sector	Frequency	Percentage
1	Retail shops	20	29.41
2	Fabrics & Threads	3	4.41
3	Hotel	4	5.88
4	Electronics	2	2.94
5	Spare parts	1	1.47
6	Tailoring	4	5.88
9	Construction material	2	2.94
11	Cereal & Pulses Trade	4	5.88
12	Shoe trade	12	17.65
13	Barber& beauty salon	6	8.82
14	Household utensils	3	4.41
15	Music& video shop	7	10.29
	Total	68	100%

Source:- Primary Data

Factors that affect attitudes of tax payer's voluntary compliance

1. Taxpayers' knowledge: Why tax is paid to states?

The influence of tax knowledge on compliance behaviour has been described in various researches. The level of education received by taxpayers is an important factor that contributes to the understanding about taxation especially regarding the laws and regulations of taxation (Eriksen and Fallan, 1996). Previous studies have evidenced that tax knowledge has a very close relationship with taxpayers' ability to understand the laws and regulations of taxation, and their ability to comply (Singh and Bhupalan, 2001).

The following table 1.3 shows the response of the respondents regarding their reason of paying taxes.

Table 1.3: Why taxpayers pay taxes

S.N	Items	Frequency	Percentage
1	To avoid disturbances		
2	In the anticipation of public services	21	30.9
3	There is no opportunity to evade	4	5.9
4	It is an obligation towards the government	43	63.3
	Total	68	100

Source:- Primary Data

The above table reveals the result of tax payers’ response on why they pay taxes, majority (63.3%) of the respondents responded that they pay taxes because it is an obligation to the government or state, whereas, 30.9% responded in the expectation of public services from the government. This indicates there is a positive understanding as to why people pay taxes and if successive works are done probably better results can be registered. On the other hand, some of them (5.9%) said that they have no opportunity to evade. Particularly with respect to the response of the other 5.9% who said there is no opportunity to evade indicates the intention not to pay if they have the opportunity to do so or their compliance behavior is questionable.

Table 1.4: The tax evasion with respect to other crimes

S.N	Items	Frequency	Percentage
1	Kidnapping	4	5.9
2	Drunken driving	2	3
3	Tax evasion/fraud	28	41.2
4	Stealing someone’s phone	1	1.5
5	Bribery	33	48.6
	Total	68	100

Source:- Primary Data

Research respondents were also request to compare tax evasion in relation to other crimes. Taxpayers understand that tax evasion is a crime and as it can be observed from table 1.5, 48.6% of the respondents ranked bribery as the most serious crime and 41.2% of the respondents said tax evasion is a serious crime while the remaining respondents chosen stealing, kidnapping, and drunken driving. From this response we can understand that taxpayers perceive tax evasion as a crime, even though it is ranked second, and this indicates that there is an attention towards taxation. But the problem here is the existence of poor compliance even though tax evasion is considered as crime by the taxpayers. Perceiving tax evasion as crime is a normal and desired behavior that has to prevail in the society to build a positive attitude towards taxation and to discourage the problem of non-compliance.

2. Tax equity or fairness

One of the main principles of the taxation system design is equity or fairness, which can be perceived via three dimensional views – horizontal equity (people with the same income or wealth brackets should pay the same amount of taxes), vertical equity (taxes paid increase with the amount of the tax base) and Exchange Equity (Wallschultzky 1984 and Richardson, 2006). The perceived fairness of the tax system also has an influence on the inclination towards tax evasion (Jackson and Milliron, 1986; Richardson, 2008).When people asked whether the tax they are paying is based on their ability-to pay or not, 76.5% of them responded that the tax is not fair and not based on their ability-to pay, which was measured by overstatement or understatement of tax liability.

Table 1.5: Fairness of tax

S.N	Items	Responses	Frequency	Percentage
1	Is your tax liability overstated or understated?	overstated	52	76.5
		understated	16	23.53
		Total	68	100

Source:- Primary Data

According to table 1.5, respondents were responded on the fairness if tax they paid. From all respondents, 23.53% said that the tax they paid is fair and equitable or even understated whereas the majority (76.5%) of those who said the tax they pay is not fair responded that it is overstated. On other question in support of this issue, the respondents were asked to rank the major problems in the tax system and they responded accordingly the majority of the respondents felt that the tax rates (tax bracket) are high, and tax revenues are not spent on public services, and also said taxpayers are not willing to pay. From this response it is clear that the tax rate is

not based on the ability-to-pay principle or it is perceived to be unfair by taxpayers. This can be either really true or human beings are benefit maximizes so that it may be difficult to please taxpayers. Even though the principle says the tax should be based on the ability- to-pay, the problem here is in determining this ‘ability’ for each taxpayer. Actually the tax rate may not be as such high but the communication gap between the tax authority and taxpayers might have created this perception and it continues to be the issue as far as the understanding of the taxpayers regarding tax rates, assessment, and calculation are low. Significant number of respondents also responded the reason for tax paid is not fair. The first reason is tax revenues collected are not spent on public services. Theoretically tax revenue is used to finance services provided by the government. This might be practically true, but the public must be made aware of these social services which are being financed by the taxpayers’ money. As long there is a gap in communicating these facts to the public the above attitude problem will not be changed.

3. Organizational effectiveness of the tax authority

The respondents evaluated the Tax Authority with respect to certain parameters. The following table shows their response to these questions in percentages.

Table 1.6: Evaluation of the tax authority by respondents

S. N	Item	Excellent (%)	Good (%)	Fair (%)	Poor (%)	Total (%)
1	Service delivery	15	25	38	22	100
2	Tax collection efficiency	9	26	35	30	100
3	Law enforcement	12	17	43	28	100
4	Awareness creation	6	14	23	57	100

Source:- Primary Data

Table 1.6 above reveals that the majority of the respondents rated the tax authority from excellent to fair except for awareness creation where 57% of them said poor. In all the parameters most of the respondents rated the authority’s effort as fair and below that. This clearly shows the tax authority is not effective and not providing satisfying service for taxpayers. On the other hand, the effort of the authority in creating awareness was rated poor (57%). This can be quoted as the root cause for all the problems as far as voluntary compliance is concerned.

Table 1.7: Stakeholders responsible for poor tax compliance

S.N	Items	Responses	Frequency	Percentage
	Who is responsible for poor tax compliance?	Tax Authority	56	82.4
		City administration	9	13.3
		Tax payers	3	4.5
		Total	68	100

Source:- Primary Data

For the response on question requested in table 1.7, 82.4% of the respondents said that the tax authority and 13.3% the city administration are responsible for poor tax compliance and only 4.5% of the respondents said taxpayers are responsible. This can be directly related to the authority’s strength and effectiveness in providing services, information, and creating awareness. The respondents additionally claimed that both the tax authority and the city administration didn’t play their role in improving the tax administration procedures, creating awareness, providing social services, and other information regarding taxes. Hence the poor effort of both the tax authority and the city administration is believed as the major factor that has contributed to the underlying problem and so that both are responsible for poor tax compliance. On the other hand, even though the above comment given by the respondents cannot be undermined, the fact that people always externalize certain problems and make others responsible for the problem, might be taken into consideration while analyzing this response.

4. Taxpayers' attitude

Attitude of taxpayers toward taxation and its administration is the other key factor that has to be considered and analyzed duly. Accordingly, the respondents were asked for various questions to measure their attitude and their response is summarized in the following Table 1.8

Table 1.8: Attitude of taxpayers on different issues

S.N	Items	Frequency		Percentage	
		Yes	No	Yes	No
1	Do you have trust in the employees of Tax Authority?	50	18	73	27
2	Do you have trust in the tax system, assessment, and collection procedures?	28	40	42	58
3	If there is no penalty or legal enforcement, is there a possibility that you may not pay a tax?	29	39	43	57
4	Do you feel guilty if you are evading a tax, provided that you remain unnoticed?	61	7	90	10
5	Have you paid your current tax obligation?	59	9	85	15
General issues related to tax authority		Agree	Disagree	Agree	Disagree
6	The tax law should be respected	61	7	90	10
7	Paying tax is unfair	6	62	9	91
8	Taxpayers evade taxation if possible	26	42	39	61
9	The severity of sanctions and penalties ensure tax Compliance	28	40	41	59
10	Tax amnesty encourages noncompliance/ evasion	35	33	52	48

Source:- Primary Data

From the above table it is can be observed that majority (73%) of the respondents have trust in the employees of tax authority. But, only 42% of the respondents said that they have trust in the tax assessment, collection, and overall tax system while the remaining (58%) said they have no trust. From this we can conclude that the taxpayers have trust in the employees but not in the assessment and collection or other procedures. This shows the taxpayers do not know about the internal procedures of the tax authority i.e. how it assesses and collects taxes or sufficient information was not communicated to taxpayers. The fact that the authority's procedures are obscure from the taxpayers, it is inevitable that loss of confidence on the authority and its procedures will be created in the taxpayers. In other words, the tax system might be considered so complex and time consuming that taxpayers felt they did not have enough knowledge to feel secure about the accuracy of their records and returns despite their best intentions.

The respondents were also asked whether absence of penalty or legal enforcement have impact on their compliance with the tax law accordingly, 57% of them said there is no possibility of not paying tax even though there is no legal enforcement. This response is consistent with the previous response on why taxpayers pay taxes and majority of them responded it is an obligation towards the government or state. In this regard, if this is the assumption by the taxpayers as to why they pay taxes, so it is normal to say taxes will be paid whether legal enforcement is present or absent. But this should not have to lead to the conclusion that legal backup is unnecessary or worthless. The remaining 47% responded there is a possibility of not paying tax if penalty or legal enforcement is not in place. Even if these respondents are not the majority to reverse the finding it has been considered cautiously that this figure (47%) by itself is significant amount and it shows there is a huge gap in voluntary compliance. From the same table, there is another question asked to know whether the respondents feel guilty when they fail to pay taxes provided that they remain unnoticed and accordingly they responded that

90% of them said they feel guilty whatever the case and this is an indication about the taxpayers' attitude that they believe paying tax is a citizenry obligation which creates a sense of guilt in them when not accomplished.

Analysis continues on the same table and respondents were asked whether they agree or disagree with a number of statements that deal with general issues related to tax. The result shows that 90% of the respondents agreed that tax law should be respected, On the other hand, respondents are against the statement 'taxpayers evade if possible' (61%), and they also do not agree that severity of sanctions and penalties ensure tax compliance (59%). This should not be misinterpreted as if taxpayers do not want the presence of penalty or legal enforcement, but it simply means penalty or legal enforcement is not the only way out to ensure tax compliance. Regarding tax amnesty 52% of the respondents said that it does not encourage tax non-compliance or evasion. The remaining 48% said tax amnesty rather encourages tax non-compliance or evasion

5. Awareness

James (2000) argues that the norm is usually to comply rather than not to comply. As already pointed out for a tax system to be effective the majority of the taxpayers have to comply. It follows that there may be greater gains in assisting basically compliant taxpayers to meet their fiscal obligations than in spending more resources in pursuing the minority of non-compliers.

With respect to awareness table 1.9 below shows that 62% of the respondents have attended taxpayers' education session, 38% said they don't attended taxpayers' education session. Similarly, a question was forwarded to know how the respondents estimate the size of taxpayers who are not paying tax voluntarily, 48% responded large number of tax payers, 32% medium, 17% few and 3% said none. From this response it is easy to conclude the existence of sizable amount of individuals who have the capacity to pay tax but not paying. In other words, this shows there is high tax evasion or tax gap. The respondents were asked for possible reasons on the above problem and it is depicted lack of awareness, lack of ability to pay, negligence and poor and tiresome collection procedures as reasons for why people evade tax.

Table 1.9: Reasons why people evade taxation

S. N	Items	Responses	Frequency	Percentage
1	Do you attend awareness creation training provided by tax authority?	Yes	42	62
		No	26	38
		Total	68	100
2	Estimate the size of taxpayers who are not paying tax voluntarily?	Large	32	48
		Medium	22	32
		Few	12	17
		None	2	3
		Total	68	100

Source:- Primary Data

6. Honesty

The respondents were also asked to know how far they are loyal to the tax system. Hence their responses were summarized in the table 1.10.

Table 4.10: Response on honesty/ loyalty of taxpayers to tax system

S.N	Items	Responses	Frequency	Percentage
	How loyalty/ honesty of taxpayers to the tax system is evaluated by the taxpayers	Excellent	5	7
		Good	24	36
		Fair	20	29
		Poor	19	28
		Total	68	100

Source:-Source:- Primary Data

According to the response of sampled taxpayers with respect honesty to tax system, 7% rated the loyalty of the taxpayers is excellent, 36% good, 29% fair, and 28% of them said it is poor. Generally, this response indicates a more or less encouraging result. On the other side, the loyalty of the taxpayers is still under question even though the ratio does not take the major share.

7. Socio-cultural factors

Taxpayers’ compliance behavior can be affected by socio-cultural factors. Hence, the respondents were asked whether these factors really have an impact on tax compliance. Their responses were presented in the table below.

Table 1.11: Response on impact of socio-cultural factors

S. N	Items	Responses	Frequency	Percentage
1	Does the compliance of the other taxpayers encourage your own compliance behavior?	Yes	52	77
		No	16	23
		Total	68	100
2	Do you think that social and cultural factors have an impact on tax compliance behavior?	Yes	37	55
		No	31	45
		Total	68	100

Source:- Survey questionnaire(2008E.C)

According to the table above, majority of the respondents (77%) responded that the compliance of other taxpayers encourage their compliance behavior. Similarly 55% of them also responded that social and cultural factors have an impact on tax compliance behavior. This justifies the existence of relationship between various ethnic, religious, and social backgrounds and the tax system of a country. Since there is strong social bond between members of the same group in society, tax compliance behavior of an individual can be affected either positively or negatively by other members of the group. If there are tax compliant and influential individuals in social group or society, there is a possibility that other members follow them and affected by these individuals. Similarly when the influential individuals are tax non-compliant and against the tax law, there is a higher tendency for the followers or members to be influenced by these individual. Hence, the socio-cultural factors can have a direct or indirect relationship with the tax compliance behavior of taxpayers.

8. Political factors

In this study political factors are assumed to be among the factors that determine taxpayers’ compliance with the tax law. Based on this assumption respondents were provided with a question and their responses were summarized in the table 1.12.

Table 1.12: Responses on political factors

S.N	Items	Responses	Frequency	Percentage
1	Does the political system have an impact on your as well as other taxpayers’ attitude towards the tax system?	Yes	19	28
		No	49	72
		Total	68	100
2	Do you think that you are getting comparable social services from the government for the government for the tax you have paid?	Yes	31	45%
		No	37	55
		Total	68	100
3	Tax revenue is not used by the government for public service and it doesn’t provide enough information about how it utilizes the taxpayers’ money	Agree	50	73%
		Disagree	18	27
		Total	68	100

Source:-Primary Data

According to the responses of the respondents, 72% of the respondents said that the political system have no impact on their as well as other taxpayers' attitude towards the tax system. This can be justified by the respondent as tax is a citizenry obligation rather than a gift to the political party in power. In other words paying tax continues to be an obligation as a citizen regardless of the political ideology of the government in power. This may not be the case always because public attitude towards taxation can be adversely affected when government is highly corrupted and misappropriate the taxpayers' money. However, majority of the respondents (55%) of the respondents said they are not receiving comparable social services from the government in return of what they have paid as a tax and (73%) said that tax revenue is used by the government for non-public service and it doesn't provide enough information about how it utilizes the taxpayers' money.

6. Recommendations and Conclusion

Recommendations

Based the result of study the following recommendations are forwarded to help the tax authority and other policy makers of Ethiopia.

- The most obvious requirement for fairness or equity is to treat equal people in equal circumstances in an equal way. Maintaining tax equity and fairness is not achieved only through levying equal taxes on individuals who have equal income but also each taxpayer should pay according to his ability- to pay. Ensuring equity means encouraging and protecting honest and loyal taxpayers by adopting fair competition. This can be achieved by incorporating those taxpayers who are eligible in to the tax system. The authority must also involve the taxpayers or their representatives while estimating the daily sales or revenue of taxpayers to address the question of fairness and equity. Generally, the authority has to ensure tax fairness and equity among category 'C' taxpayers, so that voluntary compliance behavior can be developed.
- An effective compliance program requires that tax administration has sufficient powers that enable it to enforce compliance effectively. Voluntary compliance is promoted not only by an awareness of rights and expectations of a fair and efficient treatment, but also by clear, simple and user friendly administrative systems and procedures. Tax systems that depend on ad-hoc administrative procedures rapidly become discredited and endanger compliance. To encourage compliance it is equally important that tax authority administers the law fairly.
- The tax authority needs to be strong enough in order to implement the tax law effectively and efficiently. Functions such as tax assessment, collection, awareness creation, providing information, and enforcement has to performed effectively and efficiently, so that it will be perceived as strong and powerful by the taxpayers. In addition to this efficient service delivery to taxpayers is a key factor against which the strength of the authority is judged.
- To create an efficient tax administration, the tax authority needs to strengthen itself by educating and training its employees, by computerizing its operations, devoting additional resources. Training should include customer service training and cross functional training for employees so they have an understanding of the entire system of tax administration.
- In addition to this, the authority should make the tax law and procedures simple, understandable, and transparent. Voluntary compliance is enhanced when vibrant and efficient tax authority exists.
- One of the areas to stress on while dealing with the issue of voluntary compliance is the development of persuasive communications between the tax authorities and taxpayers. The most effective tool for making people more positive is to empower them with knowledge. It is submitted that there is no better tool for government to positively influence the taxpayers than to provide them with knowledge on how taxpayers' money is utilized. Any resistance or inability by government to communicate, will lead to possible speculation and resistance.
- Taxpayers' attitude toward taxation is changed only through sustainable awareness creation programs. Awareness creation should go beyond simply giving tax education to taxpayers. It should be extended to

having consultative sessions with elderly, religious leaders, prominent personalities in the society or other influential individuals. This can help to influence the whole society through these influential persons who have acceptance in their respective groups.

- There should be more preventative education for the public and increased awareness of tax responsibilities in schools. Students should be educated early in their career about tax responsibilities. All of these promote a positive view to voluntary compliance. This is to inculcate citizens a sense of responsibility toward taxes.
- The existence of positive benefits in the form of public services, security, etc. may therefore increase the probability that taxpayers will comply voluntarily, without direct coercion. Hence, the government has to provide social services to the public and it has to inform the taxpayers that these services are provided by their money. This is to convince the taxpayer that they are getting their money back and this in turn enhances voluntary compliance and increases the trust of the taxpayers on the government.

Conclusion

One of the main reasons for the tax gap is non-compliance of taxpayers with tax legislation. One of the causes for non-compliance has been demonstrated to be the attitudes and perceptions of people. It is obvious that different population groups may have differing perceptions of taxation resulting from their cultural backgrounds or social histories. These perceptions may in turn influence their attitudes towards tax compliance. This study was aimed at assessing taxpayers' attitude on factors affecting category 'C' taxpayers' voluntary compliance with the tax law. In effect the study indicated that although the majority of the respondents did not feel it is unfair to pay tax, all of the respondents have elicited certain factors that affect taxpayers' voluntary compliance. These factors which affect the taxpayers' voluntary compliance behavior can be concluded as the tax rate undoubtedly higher than what most taxpayers would like it to be. Most of the respondents feel that people should pay taxes according to their ability; in other words they feel that they do not pay the same amount of tax as others in similar situations. Awareness is a corner stone as far as voluntary compliance is concerned. The survey data has showed that majority of the taxpayers know why they pay taxes but they have no detail knowledge about taxation. On the other hand, in this study lack of awareness was quoted as the major and leading reason for nonexistence of voluntary compliance among category 'C' tax payers in Arba Minch city.

Tax authority is the responsible body for assessing and collecting the tax revenue. The amount of revenue collected is directly depends on the efficiency and effectiveness of the authority. In light of this fact the survey result showed the tax authority is not efficient and effective in various aspects such as, in improving the tax assessment and collection procedures, creating awareness, enforcing the tax law, providing services, and information regarding tax. It can be concluded that, so long as this is the fact it is not easy to bring about voluntary compliance and narrow the tax gap. The respondents additionally commented on this issue and they reasoned out that both the tax authority and the city administration didn't play their role well.

Majority of the taxpayers believe that tax law should be respected and do not feel paying tax is unfair. Similarly most of the respondents have trust in the employees of the authority but not in tax estimation, assessment and collection procedures. From this it can be concluded that the problems have been emanated from lack of awareness and lack of transparency in the activities of the authority. Still majority of the respondents said that they feel guilty if they do not pay tax and believe that their compliance is not contingent on the presence of penalty, and even agree that severity of sanctions and penalties do not ensure voluntary compliance. To conclude, the survey result shows there is a positive attitude towards taxation and the existing problems are down to lack of awareness and absence of transparency.

The survey data also revealed that socio-cultural factors have an impact on the tax compliance behavior of individuals. Especially with respect to social factors, the result indicates social relationships affect attitude of taxpayers towards taxation positively as well as negatively. Influential individuals such as elderly, religious leaders, community leaders or certain social group leaders will play a great role in influencing the attitude of other individuals. Political factor was considered as a determinant factor of taxpayers' voluntary compliance. But the results of this survey showed that the political system has no impact on the taxpayers' attitude towards taxation. The survey result indicated factors that significantly determine taxpayers' voluntary compliance behavior are equity and fairness of the tax system, level of awareness of taxpayers, effectiveness and efficiency of tax authority and socio-cultural factors

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