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TAX AUDIT PRACTICE AND ITS CHALLEGES: EVIDENCE FROM GAMO GOFA ZONE TAX AUTHORITY, ETHIOPIA

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ABSTRACT

The study aimed in assessing tax audit practice and challenges in Gamo Goffa zone Revenue Authority (SNNPR, Ethiopia). Mixed research approach and descriptive research design was employed. For this study, the researchers employed descriptive survey using the fact that a descriptive research design is used to describe the data and characteristic about what is being studied. Self-administered Questionnaires and interview were used to collects the data. Descriptive method of analysis is employed and descriptive presentation methods such as tables, charts, graphs and percentages are used for presenting the findings of the study. The result of the study revealed that the Revenue Authority of Gamo Goffa zone (SNNPR, Ethiopia) extensively use comprehensive types of audit. Due to this the audit coverage of the revenue authority was too low, cases were selected based on associated risk but not used the standard risk identification criteria as of business process Re-engineering. The Authority was not performing the audit work in predetermine time. Generally, the revenue authority was not performing tax audit according to the standards required by government. Audit Case selections were made only based on associated compliance risk. The Revenue Authority of Gamo Goffa zone not fully used automated risk score system and previous case selection system (random selection). There is no reference tax modalities for auditor and the staff to holding this position.

KEY WORDS: Tax Audit, Challenges, Gamo Goffa Zone, Ethiopia.

- **INTRODUCTION**

The development of any nation depends on the amount of revenue generated and applied by the government on public infrastructure for the benefits of members of that society. Taxes, and tax systems, are fundamental components of any attempts to build nations, and this is particularly the case in developing or transitional nations (McKerchar and Evans, 2009). Taxation may not sound exciting, but it is central to the development of nations. Now a days, taxation is part and parcel of all economic and financial activities to achieve the goal. Tax collection it's a challenges for developing countries, because they faces internal and external challenges as to tax design and administration. Taxation is a complex system, frequently the authorities are faces with new challenges and issues.

Tax administration refers to the identification of tax liability based on the existing tax law, the assessment of this liability, and the collection, prosecution and penalties imposed on recalcitrant taxpayers. Tax administration, therefore, covers a wide area of study, encompassing aspects such as registration of taxpayers, assessments, returns processing, collection, and audits (Kangave, 2005) According to Biber (2010),

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tax audit is an examination to determine whether a taxpayer has correctly reported and assessed their tax obligations. An effective audit program will have significantly wider impacts than just raising revenue directly from audit activities.

The evaluation of tax in audit, when a taxpayer has filed its tax liability and fulfilled other obligations. The line of an audit program in a modern tax administration must extend beyond merely verifying a taxpayer reported obligations and detection of discrepancies between a taxpayer☐ declaration and supporting documentation.

Like many other jurisdictions, Ethiopia's tax system is highly wide-open to tax evasion. One factor that significantly contributes to tax evasion is lack of intensive audits and absence of predetermined audit criteria accompanied by low level of computerization in the ERCA encourages evasion (ERCA, 2010). Gamo Goffa Zone revenue office in 2005 E.C annual report highlights there is tax evasion and a gap between tax reported by taxpayers and actual taxable income. Tax reported by the taxpayer is less than the tax payable under the low. Increasing operating expenses, exaggerating non VAT sale, incorporating a related expenses to business are the reasons for decreasing taxable income. The report also shows that the Revenue Authority collects less revenue from business profit tax (59%) compared with the plan.

The successful audit program would be implemented which is capable to investigate, detect and prevent loss of tax revenue. The administration should be provided with appropriate enforcement tools, including conduct of effective audit. Accordingly, this study aimed at investigating tax audit practices and challenges affecting the effectiveness of tax audit in Gamo Gofa Zone Tax Authority, Ethiopia. The researcher believes that the study fills an important gap in understanding the factors affecting effectiveness of tax audit in the developing economy. Such an understanding is important, because it equips tax administrators with applied knowledge for determining factors that affect tax audit effectiveness. To be specific, revenue authority understand the existing tax audit performance, evaluating tax audit challenge to make some adjustment in the procedure and strengthens the weakness of tax audit practice. From a theoretical point of view, it provides an important data for comparing challenges tax audit between developed and developing economies. Based up on the above facts the researcher will search answers for the following basic research questions: - such as

• What types of tax audit are frequently performed in Gamo Goffa Zone Revenue Authority?
• How Gamo Goffa Zone Revenue Authority select case for audit?
• What are the factors that hinder effective tax audit program in the zone revenue authority?
• What are the existing performances of Tax Audit in the office?

DATA AND METHODOLOGY
Research Design and Research Approach
For this study, the researchers employed descriptive survey using the fact that a descriptive research design is used to describe the data and characteristic about what is being studied. The researchers also used quantitative and qualitative research approaches (used mixed method) in order to generate the advantage of both approaches like to address different objectives of the study, which cannot be achieved by a single method and to enable one approach to inform another approach, either in design or in interpretation. Kercher (2010) argues that "each strategy has its strength and weaknesses and the drive for mixed method research is to use one strategy to inform, validate, or compensate for the weaknesses of another."

Data Type and Data Collection Instruments
Both primary and secondary types of data were employed. The primary data's were collected through self-administered questionnaire and unstructured interview with tax officials. The questionnaire was comprised of both closed and open ended questions. Secondary data was also collected from the Revenue Authority annual report from 2014-2016. Data related to number of tax payers registered, number of audited taxpayers, and gained revenue due to tax audit and categories of tax payers which are selected

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for audit. In addition to annual report, tax declaration and BPR manual was used to collect data. While collecting and using these data for the study, more considerations were given to their time period, reliability, and relevance to the purpose of the study. The interviews were designed and administered to sampled tax officials & it aimed at eliciting information on the tax audit challenge, including types of audit performed, case selection techniques, capability of the staffs and the overall tax administration system.

Sample Design

To collect primary data through questionnaire, the study used all 11 Tax Auditors employed in Gamo Gofa Zone revenue authority. Usually there are times in which addressing the total population in the study is not possible because of different special reasons. But in this case, since the numbers of tax auditors were small, the study assumed the data of all tax auditors taking as a sample, there is no need of taking sample from the frame. Therefore, the sampling and the sample should be the same. In addition to tax auditors, interviews were conducted with Gamo Gofa Zone tax authority officer.

Methods of data analysis

In accordance with the data types, quantitative (will include numerical data that come out from the response) and qualitative (also include opinion data that pertains from the collected responses) data descriptive analysis are employed. After necessary coding and editing are conducted on raw data, descriptive presentation methods such as tables, charts, graphs and percentages are used for presenting the findings of the study.

• Descriptive survey result and Analysis

This study was designed to assess tax audit practice and its challenge in Gamo Goffa zone Revenue Authority, Ethiopia. The results obtained based on the data collected from respondents are presented and discussed in this section. That includes general characteristic of the respondents, the response rate and findings of the study about the tax audit practice and the determinant factor/challenges that affected sound implementation of tax audit.

RESPONSE RATE ANALYSIS

The field survey result indicates that from 11 questionnaires that were distributed to the respondents, 10 were returned back, representing 90.9 percent which represent highest achievement level of response rate.

Types Audit Performed and Audit cases performed

The survey results in table 1.1 shows, Gamo Gofa Zone revenue authority exhaustively conducts comprehensive audit (70%) followed by desk audit (30%). The interview result also reveal, Gamo Gofa Zone Revenue Authority commonly used comprehensive audit to ensure compliance behavior of taxpayers and desk audit for data cleaning and increasing the number of Audit coverage.

Table   1.1: Types of Tax Audit Performed and Audit cases conducted per month.

SN	Variables/Items	Auditors Responses	
		Frequency	Percentage
1	**What types of Audit are usually performed**		
	1.1 Desk Audit	3	30
	1.2 Refund Audit	-	-
	1.3 Field Audit	-	-
	1.4 Fraud Investigations	-	-
	1.5 Comprehensive Audit	7	70

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	1.6 Other	-	-
	Total	10	100
2	**How many audit cases on average an individual (one) desk auditor has expected to complete within a month**		
	2.1 Less than 10 cases	8	80
	2.2 10 to 20 cases	2	20
	2.3 20 to 30 cases	-	-
	2.4 Above 30 cases	-	-
	Total	10	100
3	**How many audit cases on average an individual field auditor has expected to complete in a month**		
	3.1 Less than 4 cases	9	90
	3.2 4 to 6 cases	1	10
	3.3 7 to 10 cases	-	-
	3.4 Above 10 cases	-	-
	Total	10	100

Source: Primary

The result in table 1.2 response on tax auditor's responses concerning Audit case performed. The above data indicated that 80 % of Tax payer and their 10 cases solve within a month. The result indicated that an individual auditor performs less than 4 cases in average within month as responded by 90 per cent of Tax Auditors .The survey also further shows that most tax auditors conduct their audit work less than the standard required by Ethiopian Revenue and Custom Authority (ERCA). The result indicated that Tax Auditors perform their report without pre plan. Developing an Audit plan is necessary to determine the number of cases to be audited in the period by the offices, and to segment industry, tax types and audit type (Thomson 2008).

Audit Case Selection

Regarding audit frequency as show in Table 1.3 out of 10 respondents (80%) of tax auditors stated that sometimes similar tax payers are selected for audit in consecutive years, (10%) of the respondents stated that tax payers who audited in previous were not selected for the next audit.

Table 1.2: Repetitive Tax Audit performed by the Revenue Authority

| SN	Variables	Response Alternatives	Auditors Responses	
			Frequency	%
1	Tax auditors in Gamo Goffa Zone Revenue Authority repetitively audit the same tax payer in consecutive period?	Yes	1	10
		Usually	-	-
		Sometimes	8	80
		No	1	10

Source: Primary

Regarding the reason for repetitive audit, (60%) of respondents (tax auditors) replied that when serious tax fraud and evasion found, the taxpayer is selected for audit for a consecutive audit period. The other 30 percent of Tax Auditors replied that taxpayers were selected for repetitive audit, when report their return less than previous return. Ten percent of respondent (Tax Auditors) also replied that repetitive tax audit is found when taxpayers have large tax potentials.

Figure 1.1 and Table 1.2 inferred that repetitive audit on individual taxpayers were found. This situation might have effect on compliance behavior of taxpayers and Tax audit effectiveness. Regarding

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taxpayers' cooperation in providing required information for tax Auditors and assessors, table 1.4 reveals that taxpayers were not cooperative enough in providing information regarding their businesses transactions particularly those taxpayers not required for record keeping by Ethiopian tax law.

Figure-1.1 Reasons for repetitive audit
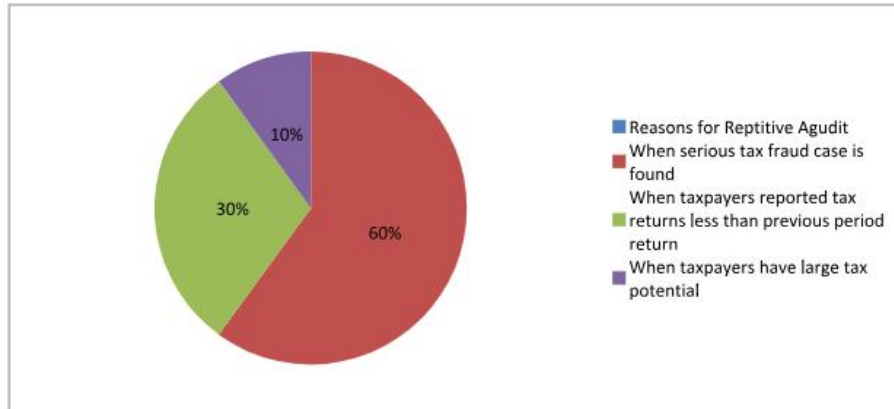
Regarding Case selection criteria (see table 1.2), majority of the respondent (Tax Auditors) replied that taxpayers have been selected based on their associated compliance risk (compliance risk indicators) and based on the occurrence of serious evasion and fraud by taxpayer for audit purpose. Almost all respondents reveals that resource availability and taxpayers' tax potential are not base for audit case selection purpose in Ethiopia. The result of the study also shows, tax auditors were not select audit cases based on their knowledge of tax payer's behavior and environment. The table also depicts that Tax Auditors responses regarding case selection through screening and case review. Here, in this item, the result revealed that taxpayers were not selected through screening and case review method, 90 percent of respondent responded against this method. The respondents were also requested to rate audit cases selection on random bases. High percentage (80%) of Tax Auditors respondents replied "strongly disagree" and 20 percent of respondent Tax Auditors are neutral. This implies that Tax Auditors selected audit cases non-randomly. The result of the survey also shows that respondent response in relation to case selection through data mining techniques. Accordingly, 100 percent of respondent replied "Strongly disagree". This indicates that Taxpayers selection for audit is not based on data mining techniques.

Techniques of Audit case selection

In table 1.3 the respondents were requested to rate audit case selection by using statistical techniques and prior period audit. 80 % of respondent tax auditors responded "strongly disagree".

Table 1.3: Techniques of Audit case selection

S.N	Statement	Percentage				
		S.Agree	agree	neutral	disagree	S. Disagree
1	Taxpayers (audited) are selected based on their associated compliance risk	60%	40%			
2	Case selection is based on the availability of resource for audit				100%	
3	Selection is based on tax payer's high tax potential.	10%	20%		70%	
4	Series evasion and fraud are basis for selection	30%	70%			
5	Auditors select audit cases manually based on their own knowledge of taxpayer's behavior and environment			10%	30%	60%

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6	Tax payers selected for audit is through screening and case review				10%	90%
7	Tax auditors select audit cases randomly.			20%		80%
8	Taxpayers to be audited was selected through data mining techniques					100%
9	Tax payers to be audited selected using Statistical techniques using prior tax audit results		10%		10%	80%
10	Rule base and automated risk scoring system.		40%			60%

Source: Primary

Respondents were also requested to rate their evaluation on identification of non- compliance taxpayers. The majority of the respondent Tax Auditors (60 %) responded "strongly disagree" whereas the rest 40% said they agreed. This implies that non- compliance of taxpayers were identified for audit without standard rule and automated risk identification system. Though the Revenue Authority has fourteen point risk identification criteria, but Tax Auditors were not using these standard criteria. The response of the interviewee on the reason for not using the standard risk identification criteria was the complexity of the risk identification criteria and difficulty to understand. The office currently employed and followed traditional system that delay in tax payment with fine, nil tax returns, nil tax declaration, showing loss report, profit significantly indicated from prior periods.

Challenges for Tax Audit effectiveness

Audit effectiveness is dependent on auditor's capability and efficiency to perform audit activities in a well-organized manner, tax auditors resources allocated for audit and the Revenue Authority tax administration system. The other factors that affect the effectiveness of audit work is the link between intelligent information and tax audit, if distorted link exist between these variables it strongly challenges the effectiveness of the tax audit activities and overall tax administration (Andreoni, 1998)

Table 1.4: Factors affecting audit effectiveness

S.N	Statement	Percentage				
1	Audit is performed based on audit manual	S.Agree	agree	neutral	disagree	Strongly.D
		-	80%		20%	
2	Taxpayers can easily understand and be aware of the rules, forms	-	-	-	90%	10%
3	Continuous and sufficient trainings for tax auditors	-	-	-	80%	
4	Apply standard risk identification criteria for identify highly risky business for audit	-	-	-	-	90%
5	The audit work to be started and completed within a predetermined time frame.	-	-	-	-	70%
6	Tax administration has enough audit staff resources to perform onsite audits on all taxpayers	10%	-	-	80%	10%
7	Enough material and equipment for audit program	10%	20%	-	60%	10%
8	Qualified audit staff /well experienced staffs are Available	-	30%	-	60	10%
9	Well organized structure and suitable work office	-	-	-	80%	20%

Source: Primary

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Table 1.4 above indicated that the response of respondent Tax Auditors regarding tax audit performed by the revenue authority was based on audit manual. An audit manual is required to provide: consolidation of policies and procedures; a reference guide for auditors; a training tool; consistency in approaches; and aid quality assurance, governance and accountability. According to the result 80 percent of respondent Tax Auditors agreed that Revenue Authority has audit manual but the audit works were performed without Audit manual. Regarding registered tax payers awareness level on tax rules and regulation, 90% and 10 % of respondent Tax auditors said "disagree" "Strongly disagree" respectively. This shows that tax rules and regulations were not communicated to tax payers and the lack of training for compliance of tax law.

Item 3 on table 1.4 depicted the response of Tax Auditors regarding the Revenue Authority's provision on continuous and sufficient training for Tax Auditors to increase their efficiency. The majority (80) of respondent Tax Auditors reveal that tax authority did not provide continuous and sufficient training for the Auditors. The interview result also supports the responses given by tax auditors. As the responses of the interview shows, Revenue Authority provide only 15 days training after one year delay on task after recruitment. The standards of auditing it is essential that revenue authority prepare both initial training (classroom and on-the-job instruction) to bring auditors up dated required level and continued training so that their skills are kept up to date and relevant.

According to BPR manual, the time to complete a single audit was 15 days. Due to complexity of taxpayers' business transaction and the size of the taxpayers, Gamo Goffa Zone Revenue Authority tax audits were not completed on the standard time required to complete the audit. As the result of the survey, about 70 percent of the respondents strongly agreed that as the audit works were not completed within predetermined time frame. As Erard (2007), the Revenue authority should have enough audit resources to perform effective audit and to minimize tax evasion and increase voluntary compliance. Auditor's qualification and capabilities, taxpayers awareness regarding tax rules and regulation and resources required for audit are factors that hinder audit effectiveness.

On contrary, the result in table 1.3 indicates, Gamo Gofa zone Revenue Authority has no enough audit staff to perform onsite audit on all taxpayers and has low enforcement capacity. The table also indicates that only small portion of the respondents (20%) of Tax Auditors was agreed that the authority has enough staffs to conduct on site audit. For the effective and efficient tax audit not only the skill and qualification of tax auditor's but also adequate number of tax auditors, materials and equipment necessary for audit have greater impact. Table 1.3 item seven, shows that the 60% percent respondents of the Revenue Authority has agreed that the authority has no enough materials and equipment to facilitate audit program. Sixty percent respondents were responded that the Authority have no well experienced audit staffs to perform audit. The result further shows that the Revenue Authority has no suitable offices to perform Audit. About 80 percent respondents were responded that the Authority has no suitable offices to perform Audit and rooms are small and uncomfortable offices to perform audit work as well as to put taxpayers' document in a safe way. The office is also not safe to discuss with tax payers and other people on tax related issues. Generally, Gamo goffa zone Revenue Authority has no enough audit staffs, no enough materials needed for audit and not have suitable offices.

Gamo Goffa Zone Revenu Authority Tax Audit Performance Level

According to table 1.5 item one, the primary purpose of Tax Audit is to ensure compliance behavior of taxpayers. Ninety percent of the respondent tax auditors were agreed that tax audit performed in the Zone revenue authority is to ensure compliance behaviors of the taxpayers. According to item two, majority of the respondent (70%) tax auditors agreed that tax audit was for assessing taxpayers and need for additional revenue for the Government. Majority respondents were also agreed tax auditors, investigators and assessors are expected to detect noncompliance behavior of individual taxpayer and tax audit is for reducing tax evasion and tax fraud.

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Table 1.5: Purpose of tax audit and Level of performance

S.N	Statement	Percentage				
		S.Agree	Agree	Neutral	Disagree	S. Disagree
1	The primary purpose of tax audit performed in tax administrations is to ensure compliance in accordance with tax law	90%	10%			
2	The primary purpose of tax audit performed in tax administrations is to assess and collect additional tax revenue.		70%			
3	Tax audit performed in tax administrations is to educate taxpayers.		40%	10%	50%	
4	Tax auditors, investigators and assessors expected to perform during an audit period is detecting noncompliance behavior of individual taxpayer.		70%			
5	Tax audit is for reducing tax evasion and tax fraud		80%	20%		

Source: Primary

The interview with tax officials also showed that the purpose of tax audit is primarily to assess unreported income and additional revenue for the Government. The respondent by the interviewer stated that the duty of taxpayers' necessary awareness creation. Consequently, Gamo Goffa zone Revenue Authority tried to create tax awareness through electronic media, printed materials. More ever, taxpayer awareness creation mechanisms for the tax administrations is a vital factor for public within a given tax jurisdiction.

The respondent tax auditors also responded on the existing challenges and possible actions needed to tackle the challenges and for improvement of the overall tax administration that leads for audit quality. Strength service delivery to create strong enforcement, make clear and accountable work environment must be created, create awareness give weekly/monthly meeting with tax payers, given information through Radio and TV on local areas language, magazines, workshops, brushers, newspapers , house to house impressively and openly discusses with tax payers to curb tax evaders and corruption, recognize model tax payers as well as tax officials, adjusting rules and regulation based on tax payers feedback, monitor and evaluate the tax employees, creating tax day celebration, strengthen strong political commitment, penalty does not teach tax payers instead education, respect every taxpayers as customer, make a notice before any harsh measurement.

Table 1.6: Gamo Goffa Zone Revenue Authority Tax Audit plans Vs Achievement

S.N	Fiscal Year	No of files to be Audited	No of files Audited	Planned Revenue	Revenue Obtained	Plan vs. Revenue Collected (%)	
						From Nº File	From Revenues obtained
1	2014	162	47	18,820,000	7,038,328.07	29.3	37.4
2	2015	210	87	25,460,643	5,235,333.66	41.5	20.6
3	2016	296	109	32,469,791	13,229,301.96	36.9	40.8

Source: Gamo Goffa Zone Revenue Authority Annual Report 2014-2016.

The effectiveness of tax audit was also measured by volume of tax audit or coverage of tax Audit performed. According to table 1.6, the revenue authority performs is ranked below 50 percent from revenue obtained and number of files (Category A and B) audited when compared with plan. The report and the survey result show that the audit performed by the Revenue Authority of was very low. However, the Revenue Authority audited only 47 taxpayers out of 162 files (29.3 per cent), and planned to detected and

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found evaded tax revenue of birr 18,820,000 and obtained only 7,038,328.07(37.4%) in the 2014 G.C fiscal year. In 2015 G.C fiscal year, the authority audited 87 taxpayers out of 210 registrants (41.5 per cent), and planned to detected and found evaded tax revenue of birr 25,460,643 and obtained only 5,235,333.66(20.6%). Similarly, In 2016 G.C, the authority audited 109 taxpayers out of 296 registrants (36.9 per cent), and planned to detected and found evaded tax revenue of birr 32,469,791 and obtained only 13,229,301.96 (40.8%).

The above data indicated that the Gama Goffa zone revenue authority should be active to find out compliance risk and increase tax revenue through the audit coverage. Thus, there is insufficient audit and revenue authority. The minimize audit rate coverage and slow progress of audit may less growth tax revenue, along with insufficient manpower and less training, Generally, audit performed by the authority was very low.

• CONCLUSION AND RECOMMENDATION

Conclusion

To fulfill the government revenue objectives, a well-structured tax audit program is important to fulfill the fiscal health of the country in particular, and maintain the tax system by reducing tax gap between voluntary tax payers and additional tax collections. The objective of this paper was to assess current audit practices, the performance and challenges of tax audit in Gamo Goffa zone Revenue Authority. In particular, the study explored Types of Tax Audit performed, and challenges and effectiveness of tax audit and risk identification criteria for case selection. These investigations were addressed by employing survey questionnaires, semi structured interview given to tax officials. In line with the objective of the study the following conclusions are made.

Gamo Goffa zone Revenue Authority audit used intensively comprehensive audit and the Audit program is fixed and not employed mixed types of audit in relation to simplicity and complexity of cases. Taxpayers are bound for audit and selected audit cases are expected to be finalized within 15 days of audit cases and the size of the taxpayers. The conclusion, there is unreasonably consumption of audit resources and not going the systematic manner as well as increase the hardship associated with repetitive audits for fully compliant taxpayers.

The study indicated that the audit coverage is limited area that might be due to inappropriate audit program adopted and lac of resource constraint. Case selection was only based on associated compliance risk. The Revenue Authority of Gamo Goffa zone not fully used automated risk score system and previous case selection system (random selection). As per the audit result, there is lac of modern training and less emphasis is given for continuous upgrading the capability.

RECOMMENDATIONS

Based the major finding of the study the following recommendations are forwarded to the concerned government officials and future researches.

- Gamo Goffa zone Revenue Authority must strive implement different ranges of audit to increase the audit coverage and employee a wide range of audit methodologies rather than use of full comprehensive audit because to address risk and audit quality. The spot issue qualification and type of audits that are not yet in place should be implemented to improve taxpayers.
- The Revenue Authority should design pre- audit procedure to select highly risky business. In addition the authority should use proper software for tax audit, and maintain the audit selection strategy and rewards the taxpayer compliance with a systematic and harmony manners. The Authority should use standard risk identification criteria to give priority for highly risky businesses and to encourage compliance taxpayers by minimizing taxpayers' compliance cost.

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- Gamo Goffa zone Revenue Authority should prepare the15 days audit program with the consideration of the serious cases and the size of the taxpayers to be audited. The authority should emphasize more time for serious cases and audit of large taxpayers to properly detect audit quality.
- To increase the awareness level of taxpayers the Revenue Authority should strive to educate communities as well as taxpayers through different techniques like mass-media, preparing broacher and using different structures (School, church, and kebele 1 to 5 approach). In addition to this the revenue authority provides house to house education and discussion by considering the type and size of taxpayers. It is also recommendable to work with educational institution like Arba Minch University in order to provide update and relevant training for tax auditors and taxpayers.
- To maintain the audit quality the Revenue Authority should increase the audit staffs through appropriate vacancy for employees and identified the gap. Auditors should have continuous training and updated knowledge skills for relevant work process. Also the authority should facilitate sufficient computers and instruments to the concerned offices.
- The authority should use appropriate short cut techniques to increase the audit quality and coverage.

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