ADDIS ABABA UNIVERSITY

COLLEGE OF BUSINESS AND ECONOMICS

FACTORS CONTRIBUTING TO TAX EVASION: THE CASE OF SMALL AND MEDIUM ENTERPRISES IN ADDIS ABABA CITY ADMINISTRATION

BY:

BIRUK TESFAYE

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DECLARATION

I, **Biruk Tesfaye**, declare that this MA thesis entitled "**Factors Contributing to Tax Evasion: the Case of Small and Medium Enterprises in Addis Ababa City Administration** is the outcome of my own original study. I firmly declare that it is not made available to any other party institution anywhere for the award of any academic degree, diploma, or certificate. The opinion of the research participants have been duly acknowledged in this research. To the best of my knowledge, I have fully acknowledged the materials and pieces of information used in the study. All the research procedures do comply with the expected standards and regulations of Addis Ababa University.

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LIST OF ABBREVIATIONS AND ACRONYMS

CR	Corruption
ERCA	Ethiopian Revenues and Customs Authority
GDP	Gross Domestic Product
IMF	International Monetary Fund
MoFED	Ministry of Finance and Economic Development
MoR	Ministry of Revenue
OECD	Organization for Economic Co-operation and Development
SEM	Structural Equation Modeling
SMEs	Small and Medium Enterprises
SPSS	Statistical Package for Social Science
STD	Standard Deviation
TAT	Negative Taxpayers' Attitude towards Tax
TCC	Tax Compliance Costs
TE	Tax Evasion
TF	Tax Fairness
TK	Tax Knowledge
TOT	Turn over Tax
TPE	Tax Penalties and Enforcements
VAT	Value Added Tax
VIF	Variance Inflation Factor

ABSTRACT

The study's objective was to determine the elements that influence tax evasion in Addis Ababa's Small and Medium Enterprises. In addition to using purposive and stratified sample procedures, the research used both descriptive and explanatory research designs. Questionnaires and interviews were used to collect the primary data for the study, and it was then analyzed using descriptive and inferential statistics. Just 310 out of the 371 surveys questionnaires that were collected from randomly chosen taxpayers were fully completed, returned, and used in the research. The study's findings demonstrated that tax evasion is positively and significantly impacted by the negative attitudes of taxpayers regarding taxes, the cost of tax compliance, and corruption. Yet, tax knowledge, tax fairness, and tax fines and enforcements each have a negative and significant impact on tax evasion. The most positive and substantial impact on tax evasion is caused by negative attitudes of taxpayers regarding taxes from the six predictor factors. The study then made the suggestion that in order to reduce the expense of tax compliance, the tax authority should make sure the tax system is clear and straightforward. The study also recommended that the government use taxpayer funds wisely and transparently, communicate with taxpayers about tax programs to promote the benefits of paying taxes in order to improve tax compliance and reduce tax evasion, in order to change the negative attitude developed by taxpayers toward tax.

Key Words: Factors Contributing to Tax Evasion, Small and Medium Enterprises, Addis Ababa, Negative Taxpayers' Attitude towards Tax

CHAPTER ONE

1. INTRODUCTION

Taxation is critical for both advanced and developing nations' economic growth. In underdeveloped countries, tax evasion is a major challenge for tax revenue collection (Abebe, 2019). Governments raise tax revenue in order to provide essential social services to its citizens for the fostering of social and economic development. However, despite the varying importance of taxation for the productivity growth of both developing and developed nations, Ethiopia, as a developing country, confronts tax evasion challenges (Adane, 2020). Tax evasion is a serious phenomenon since it affects any country that relies on taxes for revenue (Al-Rahamneh & Bidin, 2022). When compared with advanced economies, tax evasion activities are worsening in developing economies. For the governments, it is somewhat similar to an epidemic that they cannot control (Kassa, 2021). Tax evasion affects a government's ability to improve the living standards of its citizen and to allocate a budget for expenditure; it hinders the economic growth of countries, costing an estimated 20% of tax revenue (Hurre, 2022). Despite numerous attempts to address this dilemma, it remains a threatening and intractable challenge and Tax evasion not only depletes a nation's revenue, but also interrupts infrastructure provision, thus, harming the nation's socio-economic well-being (Assfaw & Sebhat, 2019).

The taxpayers' ability to pay tax is crucial towards achieving a successful and long-term inflow of tax revenue. According to statistics, SMEs represent 90.1% of the companies from all businesses in Ethiopia, roughly 23% of the Gross Domestic Product (GDP) and 41% of total jobs (Adane, 2020). SMEs play a critical role in the economic development of a country, serving as its financial backbone. SMEs make significant contributions not only in terms of numbers, but also in the provision of jobs (Kassa, 2021). Their contribution to income and well-being drives opportunities and business improvement, individual ability and self-confidence, political stability and social change, distributary and democratic objectives, and also reduces poverty and unemployment (Manaye et al., 2020). SMEs that are sufficiently and successfully developed will have a significantly positive effect on national economic growth.

In Ethiopia there are three categories of tax payers. These are: Category A tax payers whose annual turnover greater than 500,000 birr and category B tax payers' annual turnover in between 100,000 and 500,000 birr. While those with the turnover of less than 100,000 birr are grouped

under category C (MoR, 2023). The tax authorities narrowly missed their target as they collected 324.3 billion Birr from tax and related revenues in the first three quarters of the 2022/23 Ethiopian fiscal year. The amount is three billion Birr less than the 328.3 billion Birr target tax authorities set for the first nine months of the fiscal year, as per the Ministry of Revenues (MoR) (2022/23) report. Minister of Revenue (MoR) put the nine-month tax collection success rate at 97.8 percent (MoR, 2023).

Addis Ababa City administration has more than 418,133 registered taxpayers that are classified in three categories based on their annual sales turnover. About 73,294 are categorized under the 'largest taxpayers group' or category A while close to 45,875 taxpayers fall under category B or medium taxpayers. The remaining 298,964 taxpayers are under category C (AARB, 2023). This indicated that the majority of the SMEs taxpayers fall under category C taxpayers and because of their huge number of SMEs and huge number of taxpayers the researcher conducted this study in Addis Ababa. Addis Ababa Revenues Bureau has collected over 43.15 billion birr from direct tax and other sources of revenues in the past nine months of the fiscal year, achieving 95.5% of its target (AARB, 2023).

According to the data obtained from World Bank (2022) the tax-to-GDP ratio for Ethiopia from 1990 to 2020 showed that the average value for Ethiopia during that period was 8.33 percent with a minimum of 5.6 percent in 1992 and a maximum of 11.26 percent in 1998. The latest value of tax-to-GDP ratio from 2020 is 6.2 percent. For comparison, the tax-to-GDP ratio of the world average in 2020 based on 118 countries is 16.42 percent. From the global ranking Ethiopia is ranked 116 out of 118 countries in the world. Beside this in Ethiopia, 36% of the economy is not reported and captured by the official statistics. At the same time, the amount of tax evasion reached 10% of the economy (Adane, 2020).

Based on the above statistics, there are two important aspects that need to be addressed. Firstly, there is a need to immediately act to collect tax revenue from the unsupervised economy. Secondly, a deeper knowledge is required to understand why taxpayers evade paying tax and how this problem can be addressed, or at the very least, mitigated. To enforce compliance, tax authorities have largely relied on deterrent measures such as conducting tax audits and investigations and imposing harsher penalties on obstinate taxpayers (Tarekegn, 2015). Therefore, a deeper understanding of the economic deterrence factors such as tax penalties and

enforcement, tax audits, tax agency efficiency, cost of tax compliance, and perceptions of government spending; and psychological factors such as tax fairness, tax literacy, corruption, and the attitudes of the taxpayers to taxes that influence taxpayer behavior is critical, as it supplements the limitations of deterrent measures. Psychological factors such as tax fairness, peer influence, and moral obligation are not completely new in the domain of taxes. However, there is still a scarcity of literature on tax evasion among SMEs. Thus, the current study provides important empirical evidence regarding the effect of economic deterrence and psychological factors on tax evasion among SME owner-managers. Furthermore, these factors may be perceived in different ways in developing countries. Countries with well-developed socio-economic infrastructure may regard the various elements of economic deterrence and psychological factors as insignificant in influencing the tax compliance of SME owner-managers. The contrary occurs for SMEs in developing countries, where most of the areas remain underdeveloped (Hurre, 2022).

Due to the lack of streamlined access to and clarification of tax laws and procedures, lack of knowledge of tax laws and regulations, and insufficient filing and reporting systems, small and medium business owners in Ethiopia are unable to comply with tax laws and regulations in a practical manner (Derar, 2016; Kassa, 2021). In order to determine what causes tax evasion in SMEs in Addis Ababa city, both from the perspective of tax payers and Ministry of Revenue auditors, was the goal of this study.

1.1. Statement of the Problem

A taxpayer's purposeful unwillingness to comply with his or her tax obligations is characterized as tax evasion (Fagariba, 2016). It covers things like income underreporting, expense overestimation, and low-benefit announcements, among other things. As a result of tax evasion, the number of public services supplied by the government reduces while the amount of resources accumulated by taxpayer’s increases, which has a negative impact on economic growth. In other word, tax evasion has negative effects on the entire economic system (Roy & Raffaella, 2011).

Tax evasion is becoming a growing international and domestic problem for tax authorities and policymakers as it poses a serious threat to governments' ability to generate revenue, particularly in developing countries such as Ethiopia (EMoFED, 2010). Taxpayers are unable to meet their

responsibilities for various reasons. Tax evaders experience a tax revenue gap, which is defined as the difference between the hypothetical (planned) tax revenue and the actual tax collected.

The Ministry of Finance and Economic Development stated in the Growth and Transformation Plan (2010) that the five-year plan would increase the tax rate to 17% of GDP. However, new evidence suggests that the tax-to-GDP ratio has fallen. The contribution of income taxes to total government revenue to GDP was 12.2%, which compares to other African countries such as Rwanda (14.1%), Malawi (15.6%), Zambia (17%) and Kenya (17.7%) lower (Muleye, 2016). In Ethiopia, taxes are not mobilized and collected to the extent required by the government. The main reason for this poor performance in collecting revenue lies in the attitude of corporate income taxpayer's towards non-compliance with taxes and poor tax administration (IMF, 2015). This difficulty requires a thorough investigation of the root causes of the problem as well as the discovery of any other hurdles that remain to be discovered.

In addition, Amina and Sinya (2015) in Jimma, Tarekegn (2015) in Dessie, Derar (2016) and Bayu (2016) in Addis Ababa and the Ethiopian Ministry of Finance (2019) have exposed serious business tax fraud in several regions of the country. This is a typical indication of taxpayer non-compliance in the country. Due to the fact that it is managed by the aforementioned ministry, the city of Addis Ababa is not immune to tax evasion.

By examining determinants of tax compliance behavior, Aemiro and Dinberu (2014) conclude that, in contrast to the work of (Assfaw & Sebhat, 2019), penalties turn out to be statistically significant for tax compliance. In contrast to (Adane, 2020), the audit probability also proves to be highly significant. In addition, Ali et al. (2013) conclude that tax knowledge and awareness are positively and significantly correlated with attitudes towards tax compliance, resulting in taxpayer avoidance. In contrast Kasipillai et al. (2003), Nguyen (2017), and Kirchler and Enachesu (2018) find that a good understanding of taxes leads to less tax evasion. In addition, Arbex (2013) and Kiri (2016) concluded that high levels of political fairness can significantly reduce tax evasion. However, Nguyen (2017) found that political fairness has an insignificant impact on tax evasion.

Most of the leading theories, hypotheses and empirical studies were originally developed on the basis of developed countries. In fact, it has been carried out to some extent in some developing countries such as Kenya, Pakistan, India, Malaysia and Ethiopia. However, the issue of tax

evasion in developed countries is by no means the same as in developing countries (Asaminew, 2014; Martini, 2014 and Aumeerun et al., 2016). As a result, it seems reasonable to focus this research on developing countries, particularly Ethiopia, and the researchers' aim is to see whether the ideas, hypotheses and empirical evidence are similar to those found in rich countries. To the best of the researcher's knowledge, some researchers such as Aemiro and Dinberu (2014), Amina and Sinya (2015), Tarekegn (2015), Mekonnen (2016), Muleye (2016), Adane (2020) and Kassa (2021) have identified tax evasion issues in Ethiopia. However, they differ significantly from this study in various methodological aspects such as data type and source, variables studied, study area and time period, as they submitted further research studies.

In this study, the researcher looked at two theories of tax evasion; economic deterrence theory (which includes factors such as tax penalties and enforcement, tax audits, tax agency efficiency, cost of tax compliance, and perceptions of government spending); and psychological theory (which includes factors such as tax fairness, tax literacy, corruption, and the attitudes of the taxpayers to taxes) included (Riahi-Belkaoui, 2004; Oladipupo & Obazee, 2016). Some of the earlier research in Ethiopia used only one of the tax evasion factor theories or other models, but none of the studies conducted in Ethiopia used a combination of economic deterrence and psychological theory factors. For example, Kassa (2021) used psychological theory factors such as moral obligation, tax justice, tax awareness, subjective norms and taxpayer attitudes towards tax evasion to identify factors affecting taxpayer involvement in tax evasion of micro, small and large enterprises in Woldia City affect administration. Also, Kenno (2020) conducted a study on factors influencing taxpayers' perceptions of the severity of tax evasion in the Municipality of Bale Robe, Oromia, Ethiopia, using Fischer's model of tax compliance factors such as demographic factors, opportunity factor for non-compliance, tax system/structure considered (institutional factors), attitude and peer influence (social factor).

Manaye et al. (2020) conducted a study on the determinants of tax evasion in the Southern Regional State, Ethiopia, by considering a combination of Fischer tax compliance factors and psychological theory factors. These factors include factors such as income level, tax rate, likelihood of being audited, tax awareness, fines and penalties, perceptions of justice and fairness, perceptions of government spending, affinity groups, corruption, compliance costs, the role of tax authorities, and demographic factors. Apart from that, only the psychological theory factors were used in the study by Tarekegn (2015) and Muleye (2016) in Dessie Town

Administration and Adane (2020) in Bahir Dar City SMEs. Finally, a study conducted by Mekonnen (2016) in the Lideta Sub-City of Addis Ababa used only the economic deterrence theory factors.

Therefore, as shown above, to the best of the researchers' knowledge, no research was conducted in Addis Ababa that sampled SMEs from more than one sub-city and considered two theories (i.e., psychological and economic factors of deterrence theory) as contributing factors to tax evasion. As a result, the researcher investigated factors contributing to tax evasion in SMEs in the Addis Ababa municipality in order to fill the empirical gap mentioned above and minimize the prevailing challenges faced by the selected SMEs.

1.2. Objective of the Study

1.2.1. General Objective of the Study

The main objective of the study was to identify Factors Contributing to Tax Evasion: The Case of Small and Medium Enterprises in Addis Ababa City administration

1.2.2. Specific Objectives of the Study

The specific objectives of the study were:

a. To examine how the components of the economic deterrence theory—namely, tax fines and enforcements and the cost of tax compliance—affect tax evasion in SMEs in Addis Ababa.
b. To investigate how the psychological theory facts—namely, tax fairness, tax knowledge, corruption, and negative taxpayers' attitudes toward tax—contribute to tax evasion in SMEs in Addis Ababa.
c. To evaluate the efforts made by the tax authorities to encourage SMEs to lessen tax evasion and abide by the tax laws.

1.3. Hypotheses of the Study

The researcher has formulated the following hypotheses from the literature reviews:

H_{a1}: Tax fairness has a negative and significant influence on tax evasion.

H_{a2}: Tax knowledge has a negative and significant influence on tax evasion.

H_{a3}: Tax penalties and enforcement negatively and significantly influences tax evasion.

H_{a4}: Corruption has a positive and significant effect on tax evasion.

H_{a5}: Negative attitude of tax payers towards tax has a positive and significant effect on tax evasion.

H_{a6}: Tax compliance cost has a positive and significant influence on tax evasion.

1.4. Significance of the Study

This study is anticipated to be significant in a number of ways, starting with the researcher's ability to gain the skills necessary for research and earn an MSc in Accounting and Finance. Second the result of the above formulated hypotheses will help the government (Federal, State and Local level) and their agencies to formulate and implement adequate tax policies with respect to tax revenue administration. Thirdly, by supplying more research on the idea of tax evasion, particularly among small and medium-sized businesses, it will give future academics and researchers more insight.

1.5. Scope of the Study

This study focused on investigating the causes of tax evasion among small and medium-sized businesses in Addis Ababa from December 2022 to June 2023. Conceptually, the study concentrated on the factors that influence taxpayers to engage in tax evasion activities that were found in the literature, including (tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative attitude of tax payers toward tax, and tax compliance cost). Owners and managers of SMEs provided the study's primary data through self-administered questionnaires, and MoR auditors from each Addis Ababa sub-city provided the study's primary data through interviews.

1.6. Limitations of the Study

Only small and medium-sized businesses in Addis Ababa were the subject of this study. In the Addis Ababa city administration, samples were only collected from small and medium-sized businesses, leaving out large corporations and other businesses. Large businesses were excluded for this reason: they have the expertise to file their taxes, conduct their business honestly, and provide regular updates to the tax authority. Additionally, in developing nations like Ethiopia, tax evasion is more common in SMEs than in large corporations (OECD, 2018). Second, because the population sampled in this study was made up of SMEs located in Addis Ababa's sub-cities and included their owners or managers as well as auditors from the Ministry of Revenue of each

Sub-city; it is difficult to generalize the study's findings to the entire population. In order to get around this restriction and increase the study's credibility, the researcher tried to estimate a representative sample size and included all SMEs in each sub-city. Another drawback of this study is that, as is typical of most academic studies, all primary data came from respondents through cross-sectional research. However, the study's limitations open the door for further investigation and longitudinal research on the topic. As a result, all of the research's analysis and findings were limited to the case study area that was chosen, and as a result, the findings' conclusions and results might not apply to other locations.

1.7. Organization of the Study

This study was organized with five distinct chapters. The first chapter of this study covered the background of the study, statement of the problem, objective, hypotheses, scope, limitations, significance, and organization of the study. The second chapter of this study is primarily devoted to the literature review section, which covers theories, empirical evidences, conclusions, and knowledge gaps as well as conceptual framework. The third chapter discusses the study's methodology. The results and discussions from the data that were gathered were presented in chapter four. The fifth chapter concludes by presenting conclusions from the fourth chapter and potential recommendations.

CHAPTER TWO

2. REVIEW OF RELATED LITERATURES

In this part, review of literature provided both theoretical and empirical concepts regarding to the concept of tax and tax evasion. The fundamental ideas about tax evasion and factors that affect it were covered.

2.1. Basic Concepts of Tax and Tax Evasion

A tax, in the words of Bhatia (1996), is a debt owed by the tax assesses, who may be specific people, teams of people, or other kinds of legal entities. Due to the tax assesses' income from certain tangible or intangible assets, or the fact that they engage in certain economic activities that have generated tax revenue, they are obligated to pay a certain amount. According to Lymer and Oats (2009), a tax is described as a mandatory levy placed by the government or another entity in charge of collecting taxes on capital assets, income, and expenditures for which the taxpayer receives no specific benefit.

Businesses, governmental bodies, and private citizens are all subject to taxation by the government without having to file a return. Taxes are a government's most important tool and main source of funding. According to Mansor and Gurama (2016), the revenues are required to pay for basic amenities and services that are used by everyone, such as infrastructure projects like road building and environmental protection as well as important social programs like health care and education. In order for a country to develop economically, taxes are crucial. It contributes to the country's existence and financial independence and aids the government in funding social welfare initiatives and infrastructure development nationwide. By restricting imports through high taxes, it helps with the equitable distribution of wealth, the fair and just allocation of resources, the elimination of foreign dependence, and the protection of domestic industry from foreign industrialists (Awan & Hannan, 2014). Direct and indirect taxes are the two different categories of taxes. Indirect taxes are collected through consumer payments, whereas direct taxes are collected from business profits and individual incomes (Aktan, 2006).

When people, organizations, and companies refuse to give the government the required sum of money, they are committing tax evasion. The entire tax collection process faced many challenges, but the biggest one was tax evasion, which is against the law and is a criminal

offense (Nangih & Dick, 2018). By breaking the law, a taxpayer can lessen their tax liability by engaging in tax evasion. This action involves the taxpayer disobeying the formal taxation requirements that are now their responsibility, falsifying documents, or filling out data with inaccurate and incomplete information (Rantelangi & Majid, 2018).

Tax evasion is viewed as a serious loss of tax revenue, which puts pressure on the government to deliver public services efficiently. As a result, the government and tax authorities have found it difficult to raise tax revenue from the taxpayers due to the problem of tax evasion. Tax evasion is characterized as a criminal act committed while paying taxes. It occurs when taxpayers purposefully fail to pay their taxes, either by failing to file their returns, reporting their income incorrectly, or paying less than the actual amount owed despite being able to do so (Rashid, 2020). According to Korndörfer et al. (2014), tax evasion is a criminal act that violates the law and departs from social norms that call for paying taxes. Tax evasion is "the willful attempt to defeat or circumvent the tax law in order to illegally reduce one's tax liability," according to Gottschalk (2010).

Taxpayers who deliberately avoid and conceal numerous documents that could be used as evidence by tax collectors are said to be engaging in tax evasion. The entire economic, political, and social fabric of a nation can be impacted by the crime of tax evasion. Tax evasion affects how fairly income is distributed among individuals and commercial entities, which leads to unfair competition (Aumeerun et al., 2016).

As shown above the topic of tax evasion has several definitions in finance. It is common knowledge that the taxpayer deceives the financial services in order to avoid paying the required tax. According to Gravelle (2016), tax evasion is the use of legal or illegal means to avoid paying taxes, which implies that the taxpayer pays the tax and then disposes of it in part or in full. This has a negative impact on the state's coffers by lowering tax revenue.

2.1.1. Types of Tax Evasion

According to Al Baaj et al. (2018), there are two types of tax evasion: lawful evasion, often known as tax avoidance, and tax fraud, which is the illegal collection of taxes.

a) Tax Avoidance

Because the taxpayer has constitutional rights, he exercised them as every conduct is legally guaranteed. Tax avoidance, often known as "legal evasion," refers to the removal of the tax burden in whole or in part without making a statement or breaking the law's requirements (Zucman, 2014). Although it benefits from both the internal and exterior layers of the tax system, tax evasion does not take place outside of it. Internally, this implies that any financier can invest his entire portfolio in a state-issued, tax-free loan to encourage membership. In this case, the taxpayer doesn't have to pay any tax on his earnings. Financers can avoid some types of taxes at the international or external level, such as businesses that set up shop in nations that do not impose considerable taxes on ship and company earnings, due to the regional character of the tax system and the different tax systems of other countries. Tax avoidance is achieved by refraining from both the tax-creating event and from acting or disposing of the tax (Gallemore & Labro, 2015).

b) Tax Fraud

Tax fraud is an illegal form of tax in which a taxable entity wilfully and purposefully falsifies information on a tax return in order to decrease the amount of tax liability, as opposed to legal tax avoidance. Falsifying data on a tax return is considered tax fraud since it allows the perpetrator to avoid paying the entire amount due. The procedures the taxpayer used for this reason must be mentioned. These infractions typically entail the taxpayer's purpose and are clear-cut, premeditated acts. The taxpayer may violate the law when determining the tax base or when collecting the tax in order to evade tax collection (Saxunova & Szarkova, 2018).

2.1.2. Reasons for Tax Evasion

There are several uncontrollable factors that lead to tax evasion. They are heavily reliant on financial rules, as well as social, economic, and political variables, as well as levels of expertise and productivity. Among the explanations mentioned by Mertens and Ravn (2013) are the following ones:

a. **Legislative Motives:** The most prevalent justifications for avoiding taxes are legislative in nature. This is most likely caused by a dearth of tax legislation, a lack of drafting guidelines, and the existence of tax-evasion loopholes.

b. **Economical Motives:** One of the most frequent reasons for tax evasion is the taxpayer's belief that his/her income is significantly reduced by taxes.
c. **Administrative and technical factors:** When the administration's integrity and effectiveness are lacking, tax administration is a helpful executive tool since it encourages tax evasion.
d. **Social and ethical considerations:** In some tax allocations, the society's perception of evasion is a commendable perception and appreciation given that it was stolen by the state's public treasury through which tax evasion is no longer robbed in reverse in European societies that try to fulfill all of their moral obligations.
e. **Political Motives:** Tax evasion is influenced by a nation's lack of political stability, lack of independence, and public spending policies. In other words, the more effectively taxpayers use public funds, the less tax evasion there is.

2.1.3. The Effects of Tax Evasion on Taxation

All forms of tax evasion have negative effects on society's economy, psychological health, and social fabric. One of the effects on the economy is the reduction in state budget revenue from financial resources. The state is currently having trouble meeting all of its fundamental obligations to its citizens, which has an effect on revenue. Tax evasion has a negative impact on taxes and has turned into a moral corruption that affects taxes because it undermines society's trust in the government, its ability to provide citizens with needed services, and financial management (Glaeser et al., 2000). The lack of comprehension among those tasked with upholding the ideals of equality and justice is a manifestation of the societal effects of tax evasion. The idea of "justice" alludes to the fact that the tax applies to everyone. If any of them are not required to pay taxes, then the general rule of social justice has been broken (Mehrara & Farahani, 2016).

2.2. Theories on Tax Evasion

The best measures to prevent tax evasion are a topic of debate. Many firms won't pay taxes if they have the option unless there is an incentive to do so. Some people (Riahi-Belkaoui, 2004) think that increasing tax incentives is the best course of action, while others think that increasing tax penalties is the best course of action (Oladipupo & Obazee, 2016). In general, there are two

types of tax evasion theories. These are the psychologically based theory and the theory based on economic deterrence.

2.2.1. The Economic Deterrence Theory

The idea holds that taxpayers are always economically logical individuals because they will avoid taxes when they believe the profit from doing so outweighs the predicted punishment of getting found (Hasseldine & Bebbington, 1991). To stop tax evasion behavior, this idea recommends using audit and legal enforcement to identify and penalize tax evaders. The deterrence model was discovered by Hasseldine and Bebbington (1991) and involved two factors. First, a taxpayer's risk aversion level affects how they behave when it comes to tax evasion. The prospect theory also takes into account this perspective. If the taxpayer perceives themselves to be in a gain situation, there is less probability of tax evasion; otherwise, they would choose to take the risk when they are in a loss situation (Ahmed, 2016). Second, taxpayers' compliance behavior is influenced by their awareness of the tax administration's capacity to identify tax evaders and its authority to levy penalties against them. Taxpayers are encouraged to avoid more taxes due to the ineffectiveness of the tax administration because doing so would put them on an uncertain situation. The lack of information among taxpayers is the cause of this ambiguity, which discourages them from engaging in tax evasion. Furthermore, Chen Loo et al. (2009) stated that maintaining a compliance behavior requires tax expertise. Contrary to their lack of sufficient tax knowledge, taxpayers' perceptions of the tax system's complexity lead them to engage in noncompliant activity.

According to the economic deterrence theory, tax authorities' high audit probabilities (i.e., when the company is examined by qualified and impartial auditors), high enforcement initiative (i.e., tax fines), and high efficiency will lead to a decrease in tax evaders.

2.2.2. Psychology Theory

According to the cognitive structure hypothesis described by Jackson and Milliron (1986), a taxpayer's attitude and intention toward tax evasion are directly reflected in their subsequent action. According to the psychological contract hypothesis, the agreement between taxpayers and the government, in which taxpayers pay taxes in exchange for government services, is seen as a key component of the relationship (Scholz, 2003). In order to create a fair and reciprocal duty between the government and taxpayers based on a situation where one side contributes and the

other gets something, Feld and Frey (2007) developed the psychological tax contract concept. According to the hypothesis, taxpayers become discouraged to pay tax if they believe the government is providing them with a benefit that is less than the amount of tax they are paying. Moreover, taxpayers may view tax evasion as moral if they believe that their governments and tax officials are unfair, corrupt, or biased against them (McGee et al., 2016).

According to psychology theory, psychological factors have an impact on taxpayers' willingness to comply with their tax duties. It focuses on the values and ethics of the taxpayers. According to the notion, a taxpayer may cooperate even if there is a small chance that they may be discovered. Psychology theory places focus on modifying individual attitudes about tax systems, as opposed to the deterrence theory, which stresses greater penalties as a remedy to compliance concerns. Tax education is thus a tool for modifying taxpayers' attitudes on tax-related issues. It is expected that more tax compliance will result from enhanced tax education, and vice versa (Oladipupo & Obazee, 2016).

The relationship between psychological theory and this research is that tax evasion is more likely to occur when tax officials are unjust, dishonest, or discriminatory toward taxpayers, as well as when taxpayers have less tax expertise.

2.3. Taxation in Ethiopia

2.3.1. Taxation and Tax Reform in Ethiopia

More than 50 years of legislative and tax reform attempts have led to the current Ethiopian tax structure. It lacked an overall set of overarching principles to guide its judgments and a top lawgiver to guide and direct it from behind. Since its modest beginnings in the 1940s, the current Ethiopian tax system has developed and evolved in fits and starts as income requirements have emerged, administrations have changed, the economy has changed, and global events have altered. During this time, significant changes as well as numerous piecemeal adjustments were made to the Ethiopian tax system (Tadesse, 2012).

Ethiopian tax administration was for a long time neglected by ministries due to a lack of administrative expertise in tax determinants and collection. However, the Federal Inland Revenue Authority, Ethiopian Customs Authority, and the Federal Government's National

Lottery were combined into one authority, the Ethiopian Revenues and Customs Authority (ERCA), in 2008.

The Federal Tax Administration has been reorganized, moving tax administration from a ministerial level to an authority while actually enhancing the Tax Authority's authority. Recent tax administration reforms have resulted in many changes to Ethiopia's tax administration, however just a handful of these improvements are covered here for their educational value (Tadesse, 2012).

Tax reform can take the form of altering policies to address insufficient revenue, removing distortions that harm economic welfare and growth, or undertaking measures to lessen inequality. The two components of Ethiopia's tax reform project are modernizing the tax code and enhancing tax collection. The reform strives to retain fairness, equity, and transparency in tax administration while also fostering trade and investment and building a long-term domestic revenue base (Yalemtesfa, 2011). The tax may not succeed in less developed countries like Ethiopia, where there is a substantial informal economy, low tax morale, unchecked evasion, and total mistrust between the public and the taxing authorities. Lack of simple tax administration procedures is one of the causes (Mekonnen, 2016).

2.3.2. Tax Evasion in Ethiopia

In Ethiopia, a sizable portion of economic activity is unreported and unaccounted for by official data (36 percent of the documented economy). In the present, tax evasion represents 10% of the GDP. The conclusion has substantial ramifications for tax policy (increasing the tax rate versus the tax base) and incentive structure if small and medium-sized businesses are to be the driving forces behind Ethiopia's development (Emrta, 2010).

Government revenue is typically far lower than government expenditures in poor nations like Ethiopia. This poor tax revenue return can only be explained by the ineffective enforcement of tax laws, which may be the result of administrative shortcomings or taxpayer disobedience (Adane, 2020).

Tax evasion peaked in the 1970s and 1980s, when it accounted for 10.4% of the entire GDP. Notwithstanding recent drops in the GDP share as a percentage of GDP, it has climbed in nominal terms by roughly 19 percentage points since 2000. From 1991, when the ratio of tax income to GDP started to climb until bending downward in 2004, it has remained high but has

been declining. The tax-to-GDP ratio has been trending downward since 2004 as a result of the quickly expanding economy and the ineffective tax collecting operations (Emrtat, 2010). Keep in mind that Ethiopia, with a tax-to-GDP ratio of 9.7% (MoFED, 2010), has one of the lowest levels in Sub-Saharan Africa, compared to roughly 18% for the rest of the continent. Compared to high-performing nations like South Africa and Namibia, where tax collection is at 25% and 30.1 percent, respectively, it is much less (Tarekegn, 2015).

Between 1977 and 1991, when the nation was torn apart by civil conflict and turmoil, the informal economy in Ethiopia expanded, fostering the expansion of illegal enterprises. It contributed on average 41.5 percent of the GDP throughout this time. The informal economy shrank to 30% (1998-2006 average) of the official economy as a result of the reform packages put in place since 1993. The rate of informality appears to have increased recently, peaking at 33.3% in 2007–2008 (Emrta, 2010).

According to contemporary public management theories that place an emphasis on efficiency, accountability, and the requirements of good governance, the tax administration department of government is in charge of monitoring the procedures and use of public funds. Governments must administer and enforce tax laws in order to collect money from businesses so they can provide public goods and services. Ethiopia must rely on domestic resources, the majority of which come from domestic taxation (Mekonnen, 2016).

Evaded taxes would have been a useful resource for the country's infrastructure and public service development due to the prevalence of unreported economy. The responsible authority's challenging mission of bringing the unreported economy within the tax net has had significant repercussions for the nation's tax policy (Emrta, 2010).

2.4. Factors Contributing to Tax Evasion

A number of variables contribute to tax avoidance, which might result in criminal behavior on the side of taxpayers. One of the factors that encourage taxpayers to participate in this activity is economic incentives. The level of tax burden, corporate sanctions, and company slowdown are all seen as critical economic factors. On the other hand, the most crucial aspects include legal considerations, sociological features, demographic factors, mental illnesses, and moral issues (Saxunova & Szarkova, 2018).

The causes of tax evasion are thoroughly described by Kirchler (2008), who categorizes them, into three groups (i.e., social-psychological, political and economic determinants). According to him, political factors such as the complexity of the legal and tax systems, or fiscal policy, and economic factors such as the rational decision-making process and the impact of audits, fines, tax rates, and income on tax behavior are all examples of social psychological factors that influence tax behavior.

Age, gender, education, income, occupation or status, peers' or other taxpayers' influence, ethics, legal sanctions, complexity, relationships with taxation authorities, sources of income, perceived fairness of the tax system, likelihood of being audited, and tax rate are some of the determinants or factors that have influenced tax evasion as discussed by various researchers, according to Rashid (2020). The desire of a taxpayer to participate in tax evasion is influenced by a number of factors. Among the elements considered in this study were the following ones: The following topics were covered: tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative taxpayer attitudes toward tax and tax compliance costs.

2.4.1. Tax Fairness and its Effect on Tax Evasion

Tax fairness is a factor that encourages tax evasion among taxpayers and is a non-economic factor that affects a nation's tax collection (Alleyne & Harris, 2017). Fairness is characterized by taxpayers' desire to pay the tax assessed and its effect on the fight against tax evasion. The belief that the tax system is fair is one of several elements that affect taxpayers' impression of tax evasion (Rashid, 2020). One of the guiding principles of the design of the taxation system is tax equity and fairness. This can be understood through three dimensional perspectives, including horizontal equity (people with the same income or wealth brackets should pay the same amount of taxes), exchange equity (expecting the same share of public service from the government in exchange for paying tax) and vertical equity (taxes paid rise with the amount of the tax base or taxable income) (Wallschutzy, 1984). Fairness is acknowledged in tax collection systems, principles, and implementation. Unethical behavior may take place as a result of the tax collection process' unfairness. Taxpayers may be persuaded to pay more because the tax is justifiable. If the tax rate is not reasonable and acceptable, payers will regret using tax evasion techniques, and they will inform the authorities of their annual income without disputing the

specific amount. The maintenance of the fairness of the taxation system is aided by taking into account one's ability to pay or acceptable tax rates (Rantelangi & Majid, 2018).

Governments select who will pay a high tax rate and how much to tax. A factor that encourages taxpayers to pay a smaller percentage of their income in taxes is the tax rate. The tax rate ought to be fair and suitable for the taxpayers (Nangih & Dick, 2018). According to Allingham and Sandmo's model, the tax rate on payment might be positive, zero, or negative, suggesting that an increase in the tax rate could result in an increase, a stay-the-course, or a decrease in the tax payment. The theoretical literature refuted the assertion that raising taxes will result in a rise in tax evasion (Gravelle, 2016). Because not all taxpayers may pay the same amount of tax, the subject of whether or not taxes is fair is controversial (Ahmed & Kedir, 2015). According to Farrar et al. (2018), taxpayers' sense of fairness encourage them to cooperate and comply with tax authorities more, which reduces tax evasion. According to Richardson (2016), a tax system may encourage tax compliance if the tax administrator treats the taxpayers with respect. According to research by Rashid (2020) and Jurney et al. (2017), there is a negative correlation between tax fairness and tax evasion. So, this study suggests that there is a link between tax evasion and taxpayers' opinion of fairness:

H_{a1}: Tax fairness has a negative and significant influence on tax evasion.

2.4.2. Tax Knowledge and its Effect on Tax Evasion

Tax knowledge serves as a beneficial tool to encourage taxpayers to desist from tax evasion by giving them a grasp of the country's tax structure and laws (Pui Yee et al., 2017). The degree to which a taxpayer is knowledgeable and aware of tax-related issues affects that taxpayer's attitude significantly, and a taxpayer who is knowledgeable about taxes will be aware of their rights, obligations, and the processes involved in paying taxes as well as the repercussions of non-compliance (Machogu & Amayi, 2013).

For taxpayers to comprehend the causes and effects of engaging in tax evasion, tax knowledge is necessary. Taxpayers who are knowledgeable about tax evasion are less likely to commit the crime; on the other hand, taxpayers who lack that knowledge are more likely to do so. Prioritize tax-related content to advance the understanding of taxpayers and authority specialists (Pui Yee et al., 2017). Taxpayers may increase the nation's tax revenue by being knowledgeable about taxes. Taxpayers will be less inclined to participate in tax evasion if the authorities offer them a

variety of tax evasion and other tax-related training (Rashid, 2020). Whether or not a taxpayer would participate in and maintain tax evasion activities depends on their level of tax competence. Taxpayers expose themselves to various risks that could result in tax evasion when they go about their regular activities without thinking about taxes (Rantelangi & Majid, 2018).

Moreover, Tishar and Hasanuzzaman's (2019) study discovered that those who have received tax education are less likely to violate income tax laws. According to Torgler et al. (2008), greater income tax return submission uncertainty is correlated with lower tax awareness. By encouraging people to voluntarily comply with tax regulations, basic tax knowledge will lessen the likelihood of tax evasion (Mohamad et al., 2013). Further research by researchers including Ahmed (2013), Ndekwa (2014), Saad (2014), and Geletaw (2017) revealed that tax knowledge and education have a detrimental and significant impact on tax evasion; when the taxpayer's educational background improves, a decrease in tax evasion attitude may be anticipated. However, the research by Tadesse and Goitom (2014) and Ahmed and Kedir (2015) showed that tax evasion and knowledge of taxes were not significantly connected. In light of this, the study suggested the following hypothesis:

H_{a2}: Tax knowledge has a negative and significant influence on tax evasion.

2.4.3. Tax Penalties and Enforcements and its Effect on Tax Evasion

A fine or penalty is cash that is typically paid to a government agency as retribution for a crime or other offense (Muoki et al., 2014). The steps taken when taxpayers pay less tax than their actual obligations or fail to file their income tax return at all are referred to as tax fines and enforcement initiatives. The steps taken by the authority to enact measures following an audit have a significant impact on taxpayer compliance with a tax system (Calimani & Pellizzari, 2014).

Lower non-compliance among tax payers was the outcome of increased tax deterrence sanctions pertaining to detection likelihood and the harshness of fines. Fines and penalties have a favorable impact on tax compliance levels; the greater the penalty and, consequently, the audit risk, the greater the deterrent effect on prospective tax evasion (Muoki et al., 2014; Paper et al., 2016). The level of tax penalties has a statistically significant impact on tax compliance levels and a favorable impact on tax compliance behavior (Paper et al., 2016; Yunus et al., 2017). Additionally, research by Helhel and Ahmed (2014), Aemiro et al. (2014), and Ahmed and Kedir

(2015) demonstrated a significant positive relationship between the size of the penalty and taxpayers' intentions to comply with tax laws. In other words, when taxpayers believe that there is a high penalty rate for any non-compliance, the level of non-compliance will decrease. Alm (2019) contends that tax cheating fines can reduce tax evasion because tax evaders tend to become more risk-averse when they hear about the imposition of such penalties. Chen (2003) discovered that punishment-fines minimize tax evasion if the cost of enforcement is not excessive, but Deb and Chakraborty's (2017) investigation indicated that the penalty and legal proceedings had a substantial impact on taxpayers' propensity to evade taxes. Additionally, tax evasion is less likely in a country with a better level of legal enforcement, according to Mohamad et al. (2013). The study therefore presupposes the following hypothesis:

H_{a3}: Tax penalties and enforcement negatively and significantly influences tax evasion.

2.4.4. Corruption and its Effect on Tax Evasion

From the dawn of human society, two ubiquitous interacting phenomena—corruption and tax evasion—have been practiced (Neal et al., 2015). According to Nelson (2015), the presence of corruption among politicians, bureaucrats, government employees, and their family and friends in a state encourages the behavior intention of taxpayers toward tax cheating. Benk et al. (2018) investigation of bribery as a component of corruption revealed no substantial view of it as a serious crime. Moreover, Ivanyna et al. (2016) shown that tax evasion is significantly impacted by the culture of corruption. Furthermore, when it is believed that the government is corrupt, tax evasion is defended as ethical by Oberholzer and Stack (2014) and Alasfour et al. (2016). Also, a study by Assfaw and Sebhat (2019) found a positive and substantial correlation between tax evasion and corruption. As a result, the study suggests that there is a causal link between tax evasion and corruption and makes the following hypotheses:

H_{a4}: Corruption has a positive and significant influence on tax evasion.

2.4.5. Negative Taxpayers' Attitude towards Tax and its Effect on Tax Evasion

In the context of tax evasion, the terms attitude and perceptions are commonly used interchangeably because people's attitudes are formed by their perceptions (Pui Yee et al., 2017). A person's attitudes are their positive and negative evaluations of objects, concepts, or living things, according to Ahmed and Kedir (2015). The vast majority of past studies found that when a tax system is unfair, dishonest, or discriminatory, tax evasion is acceptable (McGee & Tusan,

2008). McGee et al. (2016) discovered that while tax evasion cannot be justified in some situations—such as when the government engages in dictatorship or corruption—it may be in others.

A statistically significant correlation between tax attitudes and tax compliance levels was discovered by Paper et al. (2016). According to studies by Palil and Mustapha (2011) and Waithira (2016), people generally have a good attitude toward paying taxes. As a result, tax evasion may decline and compliance may rise. Taxpayer opinions toward the tax system and personal income tax compliance were found to have a substantial positive link by Beza (2014), Aronmwan et al. (2015), and Paper et al. (2016). Contrarily, taxpayers who view taxes favorably are more likely to carry out their obligations to the authority. Those who are opposed to paying taxes are less inclined to do so (Assfaw & Sebhat, 2019). With the justification provided, the study's hypothesis would be as follows:

H_{a5}: Negative attitude of tax payers towards tax has a positive and significant effect on tax evasion.

2.4.6. Tax Compliance Costs and its Effect on Tax Evasion

Businesses must pay fees to comply with tax regulations, which are separate from their tax obligations. The cost experienced by taxpayers to satisfy their statutory tax duties in addition to their real tax debt is referred to as "tax compliance cost" by Abdul-Jabbar and Pope (2008). The three main components of tax compliance costs are financial expenses, time-related costs, and psychological costs to the taxpayers (Evans, 2008). The cost of employing tax professionals (such as tax agents and accountants), as well as the cost of taxation manuals, books, communications, and other incidentals, are all examples of money-related charges. Time costs include the time a taxpayer spends maintaining records for the purpose of submitting a tax return, putting together tax data for tax professionals, and communicating with the tax authorities. One instance of a psychological cost is the stress associated with addressing complicated tax issues (Smulders et al., 2012).

According to Amina and Sniya's (2015) study on the topic, Ethiopia experienced relatively high tax compliance expenses during the fiscal year 2011–2012. The entire expenses of tax compliance are anticipated to be 5.8 billion Ethiopian Birr, or around 4.5 percent and 1% of tax revenue collection and GDP in the years under consideration. The results of the study show that

the costs associated with tax compliance are disproportionately higher for smaller enterprises in Ethiopia. The majority of the costs were attributed to charges associated with commercial profit tax, VAT, and TOT compliance, the study's findings show. The complexity, particularly in connection to the tax regime for relatively smaller firms and the regularity of reporting with regard to VAT and TOT, results in significant expenses associated with company profit tax compliance.

High compliance costs can lead to tax evasion, tax fraud, and the suppression of investment because the country's attractiveness in terms of taxes has dropped due to lower competitiveness (Ojeka, 2012). According to Aumeerun et al. (2016), the majority of Kenyan small and medium-sized firms think that consultancy fees and the cost of employing suitable staff are unreasonably expensive. In order to comply with regulatory requirements and computerize their accounting records, many small firms rely on skilled tax experts. All of these programs must be funded by the taxpayers. He discovered a negative correlation between tax compliance and non-compliance, as well as a positive correlation between compliance fees like those tax advisors charge. The majority of consumers are driven to utilize qualified tax advisors as a result of the perceived technical nature of submitting tax returns (Aumeerun et al., 2016). Taxpayers lack the expertise required to prepare tax returns due to the various legal amendments that occur each year. Legal documents including legal terminology, tax rules and regulations are difficult for normal taxpayers to comprehend. Small and medium-sized firms can also save time and money by engaging a tax professional to complete their tax returns in the most time- and money-efficient way possible. Simplifying tax regulations is required to lower administrative and compliance expenses, as well as to eliminate taxpayer uncertainty and boost tax compliance rates (Beza, 2014).

In addition to lowering compliance costs and tax evasion, Silvani and Baer (1997) assert that making the tax return simpler will encourage taxpayers to prepare their own returns as opposed to hiring tax professionals. In their study, Giombini et al. (2018) discovered a link between the difficulties with the tax system, the cost of tax compliance, and tax evasion. As a result, the study put out the following theory, presuming a positive correlation between tax compliance expenses and tax evasion:

H_{a6}: Tax compliance costs have a positive and significant influence on tax evasion.

2.5. Empirical Review of the Study

Kassa (2021) conducted research on the micro, small and large enterprise taxpayers in Woldia City administration to determine the factors that contribute to tax evasion. In order to analyze the data, the researcher used a quantitative research approach and a descriptive and explanatory research design. With the aid of questionnaires and a stratified and straightforward random sampling technique, the researcher gathered primary data from 370 respondents. The collected primary data were analyzed by using Pearson correlation and multiple regression analysis through SPSS. The study's findings showed that tax fairness, tax knowledge, and moral obligation significantly influence taxpayers' decision to evade taxes, while the remaining moral obligations and subjective norms have no statistically significant impact on this decision.

Determinants of Tax Evasion in Addis Ababa City Administration: The Case of Bole Sub City Category "A" Taxpayers is the title of a study done by Demle (2019). From a total of 1,625 populations, 335 respondents were chosen as the sample size for the study using a stratified and simple random sampling technique. The researcher used questionnaires as the primary data collection method. The category "A" taxpayers were divided into the following seven strata: construction, wholesaler trade, retail trade, manufacturing (process), import, and export. Using SPSS, descriptive and inferential statistics (i.e., correlation and regression) were used to analyze the collected primary data. The study's findings showed that the following factors have a statistically significant impact on tax evasion: tax rate, income level, and probability of detection, penalty rate, and complexity of the tax system, perceived role of the government, peer influence on tax evasion, age, gender, and education. The researcher also recommended that the tax authority revise the perceived high tax rates, launch a national campaign to increase awareness and education about the advantages of voluntary compliance, increase the percentage of taxpayers who are audited, punish defaulters and "name and shame" them, simplify tax laws, close loopholes in tax laws, and train tax inspectors in order to reduce tax evasion.

Yohannis and Zerihun (2013) assessed the gaps and issues that exist between the business community and the Dire Dawa tax administration in their study. According to their research, the majority of taxpayers were generally in favor of general tax principles, but they were paying more than they could afford and lacked confidence in the authority's employees or the system as a whole for calculating, assessing, and collecting taxes. Additionally, they claim that the tax

authority of the Dire Dawa City Administration failed to ensure that taxpayers could objectively, clearly, and comprehend the tax procedure. They therefore think that enhancing the tax authority's operational framework and increasing transparency will gradually increase taxpayer confidence in the tax system.

Daniel (2017) conducted research on the variables that affect category 'C' taxpayers' attitudes toward voluntary compliance in Arbaminch. He found that among category "C" taxpayers, lack of awareness was the primary cause of non-voluntary compliance. On the other hand, socio-cultural factors have both positive and negative effects on taxpayer attitudes. Efficiency and effectiveness on the part of the tax authority in improving tax assessment and collection procedures, raising awareness, and enforcing tax law have positive effects on taxpayers' voluntary compliance. On the other hand, he asserts that political influences had little impact on the attitudes of taxpayers in his study area.

In their article, Mesele and Tesfahun (2016) identified problems with tax payers and revenue authorities in Dessie Town. According to the findings, the problems that taxpayers were facing included tax justice and equity, the organizational capability of the tax authority, the degree of taxpayer awareness, cultural factors, and the availability of social services from the government. On the other hand, tax authorities had to deal with problems like low tax payer perceptions of the significance of paying taxes, taxpayers delaying tax payment and disclosure, starting a business without a trade license, and outdated tax collection methods.

With a focus on the Tigray Regional State, Redae and Shailinder (2016) worked together on a study of taxpayers' perspectives on corporate taxation in Ethiopia. Their study's objective was to obtain a comprehensive picture of Tigray state business income tax payers' knowledge of Ethiopian tax law. Their research's conclusions showed that educated and younger residents of the state were engaged in business and self-employment. The majority of taxpayers who pay business income taxes were, however, unaware of their classification. Additionally, this study discovered that a significant portion of taxpayers were having trouble gathering all the paperwork required for the purposes of determining their tax liability because they lacked business knowledge. People found it challenging to understand the nation's tax code and methods of generating revenue in the area because the government ignored efforts to raise awareness and improve tax payer understanding.

Muleye (2016) conducted research for his article on the Dessie town government's tax evasion environment and tax payer attitudes. The most significant barrier to building a long-term base was revealed by his research, which revealed that there was a pervasive "culture" of not paying taxes. The study also showed that intentional tax evasion is common and growing because a large majority of taxpayers think that evading taxes is only a minor crime, despite the fact that they are aware that it is their civic duty to pay their tax obligations. The severity of tax evasion in Dessie was related to the existing culture as well as beliefs about tax justice, the ineffective use of public funds, and the absence of punishment.

In a developing nation, Rashid (2020) conducted research on the factors that affect taxpayers' attitudes toward tax evasion, including the moderating impact of demographic traits on tax evasion. The primary data gathered from various sections of respondents were analyzed using structural equation modeling (SEM) as the tool. According to the study, perceptions of fairness, tax knowledge, auditing, and enforcement efforts have a negative impact on taxpayers' attitudes toward tax evasion, whereas corruption, discrimination, and the complexity of the tax code have a positive impact. The study also discovered that men, who are younger, married, educated, self-employed, and have low incomes, are more likely to be affected by tax evasion factors than women, who are older, single, less educated, employed, and have higher incomes.

Determinants of Tax Evasion in Ethiopia: A Study by Manaye et al. (2020). To handle the analysis of the primary data obtained from 376 respondents using SPSS, the researchers used an explanatory research design, correlational analysis, and ordered logistic regression. The study found 14 potential factors that could influence tax evasion, including tax rates, audit probabilities, the role of tax authorities, tax knowledge, fines and penalties, perceived equity and fairness, perceived government spending, referent group, compliance costs, outcome favorability, level of income, age, gender, and education. The study's findings showed that there is a statistically significant correlation between gender, educational attainment, tax rates, audit probabilities, tax knowledge, fines and penalties, perceived equity and fairness, income level, and tax evasion at ($p < 0.05$ and $p < 0.01$). The main factors influencing tax evasion were found to be perceived equity, income level, fines and penalties, and gender with regard to tax compliance.

Kenno (2020) conducted a study on taxpayers and tax officers of Category "A", "B" & "C" in Bale Robe town of Oromia Regional State, Ethiopia. The researcher combined a descriptive research design with a quantitative research strategy to handle the data analysis. Out of the total target population of 4,160 taxpayers in the town, the researcher used purposive and straightforward random sampling techniques to collect primary data by using questionnaires from a sample of 358 taxpayers. The study's findings showed that tax evasion was caused by a lack of tax knowledge, the perception of tax evasion as a cultural norm, the prevalence of tax audits and the degree of detection, the perception of tax evasion as a low-level crime, and problems with tax fairness and equity. The study's findings, according to Kenno (2020), suggest that tax authorities and policy makers continuously work hard to improve unfair and unequal tax payment trends. This is done by providing taxpayers with training and education about taxes.

2.6. Summary and Research Gap

The literature on tax concepts, tax evasion types, reasons for evading taxes, and the impact of evasion on taxation has been reviewed in this chapter. By attempting to establish a theoretical basis for Ethiopian taxation, tax reform, and tax evasion, it has sought to accomplish this goal. In addition, the researcher attempted to review empirical studies on the factors that influence tax evasion by taking into account tax fairness, tax knowledge, tax penalties and enforcements, corruption, unfavorable taxpayer attitudes toward tax, and the cost of tax compliance. Some say the best solution is to increase incentives, while others argue that the best solution is to increase penalties (Feld & Frey, 2007). Two of the most popular theories of tax evasion are those based on economic and psychological principles.

Economic theories are also known as deterrence theories, because they emphasize incentives. The theory holds that taxpayers are amoral value maximizes who are influenced by commercial considerations like profit maximization and detection probability. As a result, they weigh the pros and cons of various compliance strategies, including whether or not to evade taxes, the likelihood of being discovered, and the ensuing repercussions, before selecting the strategy that maximizes their anticipated after-tax returns after accounting for risk (Oladipupo & Obazee, 2016). For instance, they would try to understate their income in an effort to pay less in taxes, and if the tax authorities did not catch them, they would benefit from the tax savings (Hasseldine & Bebbington, 1991).

The economic deterrence theory (Hasseldine & Bebbington, 1991) states that a variety of factors, including tax fines and enforcement, tax audits, the effectiveness of tax authorities, the cost of tax compliance, and taxpayer opinions of government spending, have an effect on taxpayer behavior. If evading taxes is likely to be caught and the penalties are severe, few people will do it. When audit opportunities are slim and fines are minimal, evasion is expected to yield a high return. Next, a high level of non-compliance is predicted by the model. It makes sense that taxpayers are concerned about how the government spends their money in terms of taxpayer perceptions of government expenditure in relation to tax compliance (Ojeka, 2012). Ojeka (2012) asserts that if people think their taxes are being misused by the government, they will not pay them. High compliance costs can also cause tax evasion, and when the tax authority is effective, less people evade taxes (Ahmed, 2016).

On the other hand, non-economic or psychological theories are focused on the morals and ethics of the tax payers. The theories suggest that a taxpayer may comply even if there is little chance of being discovered. Psychology theories concentrate on altering people's attitudes toward tax systems rather than focusing on elements like increased audits and fines as remedies to tax evasion issues (McGee et al., 2016). Tax fairness, tax knowledge, corruption, and taxpayer attitudes are some of these psychological theory components. According to psychological theory, tax compliance costs and the likelihood of tax evasion will increase if tax officials treat taxpayers unfairly, corruptly, or discriminatorily and if taxpayers are not well-informed about taxes (McGee et al., 2016).

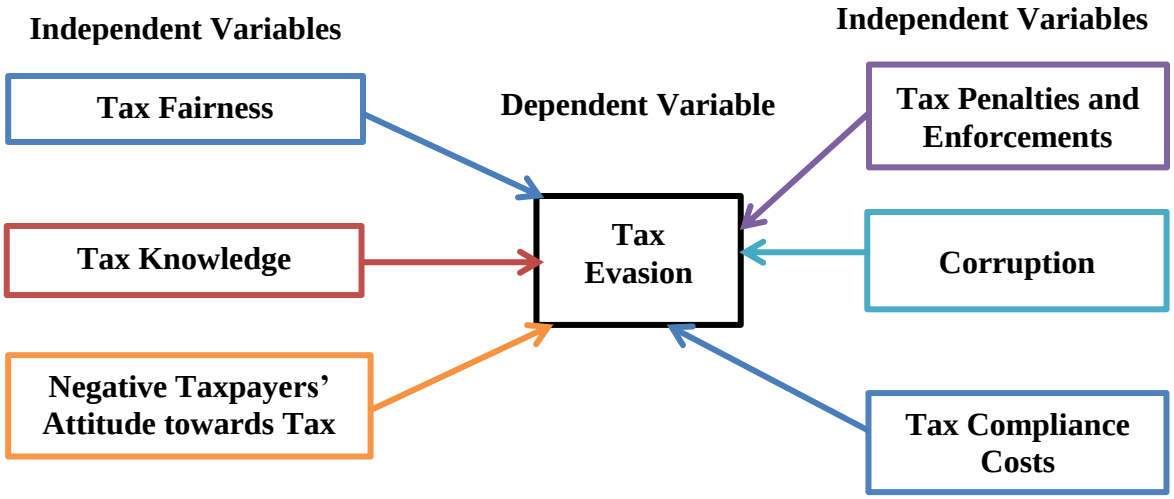
According to reviews, previous studies on tax evasion by business firms in Ethiopia either included elements from the economic deterrence theory or psychological theory in their studies—but not both—or included elements from other theories like Fischer's Model of Tax Compliance Factors. Studies based solely on psychological theory were conducted, for instance, by Tarekegn (2015) and Muleye (2016) in Dessie Town, Adane (2020) in Woldia City Administration, and Kassa (2021) in Bahir Dar City SMEs. Others, like Mekonnen (2016) in the Lideta Sub-City of Addis Ababa, used only the economic deterrence theory factors; Kenno (2020) in the Bale Robe Town Administration of Oromia, Ethiopia, used only the factors from Fischer's Model of Tax Compliance; and Manaye et al. (2020) in the Southern Regional State, combined the factors from Fischer's Model of Tax Compliance and psychological theory factors. Apart from that, very few studies have been conducted in developing countries like Ethiopia. To

the best of the researcher's knowledge, no studies have been done in Addis Ababa SMEs that take into account both psychological and economic deterrence theory aspects. To close the empirical gap and lessen the challenges faced by the chosen SMEs, the researcher is motivated to investigate the factors that contribute to tax evasion in SMEs within the Addis Ababa City administration.

2.7. Conceptual Framework of the Study

The following conceptual framework was created in light of the numerous literatures evaluated in the preceding section to provide justification for the investigation. Tax evasion that is revealed to taxpayers as well as to tax collectors or tax authority is the dependent variable for this study. The independent variables are tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative attitude of tax payers toward tax, and tax compliance costs. In Figure 2.1 below, the researcher illustrated the link between independent and dependent variables:

Figure 2.1: Conceptual Framework of the Study



Source: Based on Rashid (2020) and a literature review.

CHAPTER THREE

3. RESEARCH METHODOLOGY

This chapter deals with the research design, research approach, data type and source, target population of this study, sample design, data collection method and instrument used for data collection, method of data analysis and ethical consideration.

3.1. Research Design

A research design is a blueprint for performing a study with the greatest amount of control over elements that could skew the results' validity (Saunders et al., 2009). The research design for this study was descriptive and explanatory study design to identify factors contributing to tax evasion in Addis Ababa SMEs. The researcher used the explanatory research design to show the cause and effect link between independent and dependent variables, whereas descriptive research can be used to describe the event as it is.

3.2. Research Approach

The research approach of this study was both qualitative and quantitative research approaches for conducting the research because the overall strength of the study would be greater when both qualitative and quantitative research approaches are used (Creswell, 2009). A mixed approach or a combination of quantitative and qualitative research approach is used when more than one data collection technique is used with associated analysis techniques (Saunders et al., 2009). For instance in this study questionnaires were used to collect quantitative data and analyzing these data using statistical (quantitative) procedures and data collected from auditors through interviews and document reviews were used to collect qualitative data and analyzing these data using non-numerical (qualitative) procedures.

3.3. Data Type and Source

To achieve the objective of the study both primary and secondary sources of data were used. The primary data was collected from the SMEs owners and managers by using questionnaires, and also from auditors of the tax authority or from MoR through questionnaires and interviews. Beside this the secondary data were collected by reviewing of materials, reports of various government institutions like MoR, MoFED, and IMF database and various journals and literatures to support the findings of the study.

3.4. Target Population of the Study

The target populations of the study were 5129 taxpayers of micro and small enterprises found in Addis Ababa city as shown in Table 3.1

Table 3.1: Taxpayers of Micro and Small Enterprises in Addis Ababa

No	Sub-city Name	Small	Medium	Number of SMEs per Sub-city
1	Yeka Sub-city	522	90	612
2	Nifas-Silk Lafto Sub-city	457	191	648
3	Lideta Sub-City	207	37	244
4	Kolfe Sub-city	408	140	548
5	Kirkos Sub-city	221	38	259
6	Gulele Sub-city	339	198	537
7	Bole Sub-city	426	94	520
8	Akaki Sub-city	372	204	576
9	Addis-Ketema Sub-city	252	161	413
10	Arada Sub-city	455	167	622
11	Lemi-Kura Sub-city	100	50	150
Total		**3,759**	**1,370**	**5,129**

Source: Addis Ababa City Job Creation and Enterprise Development Bureau (2022)

3.5. Sample Size and Sampling Techniques

The target population for this study incorporated SMEs taxpayers found in Addis Ababa (i.e., 5,129). To select sample SMEs taxpayers, a sampling technique known as multi-stage were employed. First to identify the target participants or sample size in this study, the researcher used Yamane's (1967) formula because the target population in this study is finite population. Hence, the formula is described as follows:

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

Where

N = target population, n = sample size, e = error term

$$\mathbf{n = \frac{5129}{1 + 5129(0.05)^2} \approx 371}$$

Secondly, tax payers were then stratified into two strata according to their categories namely "small" and "medium" enterprises as shown in Table 3.1 above. From the total taxpayers, 3,759 are categorized under level "small enterprises" and the remaining 1,370 taxpayers were categorized under level "medium enterprises".

After identifying the sample size using the above equation the researcher allocated the estimated sample size to each stratum in the study area under the study to maximize the predictive power of the model. One method is proportional allocation. Thus the proportional allocation will be done using the following formula adopted from (Kothari, 2004) as shown in Table 3.2 below.

$$N_h = \frac{nN_1}{N}$$

Where:

N_h = Proportional sample to the strata

n = Sample size determined using the formula provided by (Yamane, 1967)

N_1 = Total number of population in each strata

N = Target population

Table 3.2: Types of SMEs and Sample Size Appropriation

No	Sub-city Name	Small	Medium	Sample Size
1	Yeka Sub City	522*371/5129 = 38	90*371/5129 = 6	44
2	Nifas-Silk Lafto Sub-city	457*371/5129 = 33	191*371/5129 = 14	47
3	Lideta Sub-City	207*371/5129 = 15	37*371/5129 = 3	18
4	Kolfe Sub-city	408*371/5129 = 29	140*371/5129 = 10	39
5	Kirkos Sub-city	221*371/5129 = 16	38*371/5129 = 3	19
6	Gulele Sub-city	339*371/5129 = 24	198*371/5129 = 14	38
7	Bole –Sub-city	426*371/5129 = 31	94*371/5129 = 7	38
8	Akaki Sub-city	372*371/5129 = 27	204*371/5129 = 15	42
9	Addis-Ketema Sub-city	252*371/5129 = 18	161*371/5129 = 12	30
10	Arada Sub-city	455*371/5129 = 33	167*371/5129 = 12	45
11	Lemi-Kura Sub-city	100*371/5129 = 7	50*371/5129 = 4	11
Total		**271**	**100**	**371**

Source: Addis Ababa City Job Creation and Enterprise Development Bureau (2022)

For instance for Yeka Sub City small enterprises 522*370/4979 = 39 respondents were selected and for medium enterprises 90*370/4979 = 7 respondents were selected. By using the same procedures for the rest of Addis Ababa sub-cities sample respondents were selected as shown in Table 3.2 above. Finally, after dividing the population by level, the researcher applied a simple random sampling technique to select respondents.

Also 20 auditors/tax collectors, 2 from each sub-city offices were purposefully selected for interview questions, except from Lemi-Kura Sub-city because it's new.

3.6. Methods of Data Collection

Self-administered questionnaires and interviews were the main data collection instrument used in this study. In order to collect the primary data for this study the researcher divided instruments for collecting primary data in to two sections, the first section were questionnaires that are going to be answered by managers and owners of SMEs and the second section were interviews to be filled by the tax collector's. Beside the researcher used both close-ended and open-ended (interviews) questions. The secondary data were collected by reviewing of materials, reports of various government institutions like MoR, MoFED, and IMF database and various journals and literatures.

3.7. Method of Data Analysis

In order to investigate the factors contributing to tax evasion in Addis Ababa SMEs, the data gathered from the questionnaires were examined for consistency and completeness at the end of each field data collection day and before the data were stored. The IBM Statistical Package for Social Science (SPSS) version 23 program was used to conduct the analyses. Prior to conducting the study, reliability and validity scores were evaluated to test the psychometric qualities of the constructs. The interview responses were used to triangulate the result of the quantitative data by making logical interpretation, justification, and suggestions, the data were tallied. To show and analyze the data, descriptive and inferential statistics (such as frequency, mean, standard deviation, correlation, and regression findings) were computed.

3.7.1. Reliability and Validity Analysis

The quality and reliability of the data must be verified before conducting any statistical analysis. According to Hair et al. (2010), the degree to which a variable or group of variables is consistent in what it is meant to assess is known as dependability. The consistency of a questionnaire was

evaluated using reliability analyses. Although there are other ways to test for reliability, Cronbach's alpha was thought to be the most appropriate method for this study because it is the most often used reliability indicator. Cronbach's alpha values with a minimum threshold of 0.7 are considered to be good, according to Nunnally (1978).

Unfortunately, there is no one certain sign of a scale's validity, and the validation of a scale involves gathering empirical data regarding its use (Hair et al., 2010). The validity of a scale refers to the extent to which it measures what it is intended to measure. The researcher looked at the content validity, which refers to how well a measure or scale has drawn a sample from the specified population or topic domain. A detailed examination of earlier literature on the factors contributing to tax evasion was conducted in order to confirm the content validity of the surveys.

3.7.2. Descriptive Statistics Analysis

The demographic data of the respondents, such as gender, age, marital status, education level, SMEs sectors, forms of business ownership and tax experience of SMEs, were reduced using descriptive analysis and also, a summary of the factors contributing to tax evasion by using tabulations, frequency, percentages, and measures of central tendency (mean and standard deviation) were presented. Descriptive statistics were used in this study to compare the various factors that were used, as well as to determine the extent or degree to which the practices tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative attitude of tax payers toward tax, and tax compliance costs contributed to tax evasion.

3.7.3. Inferential Statistics Analysis

Hair et al. (2010) suggested that prior to performing any data analysis, it is important to verify any assumptions made regarding the sample size, scales of the variables, multivariate normal distribution, outliers, and their multicollinearity.

3.7.3.1. Pearson Correlation Analysis

Using Pearson's correlation coefficient or measure of relationships, this study looked at the relationship between the independent variables parts (i.e., tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative attitude of tax payers toward tax, and tax compliance costs) and the dependent variable (i.e., tax evasion). The coefficient of correlation, a statistical indicator of the link between two variables, ranges from r = +1.0 for a perfect positive

correlation to r = -1.0 for a perfect negative correlation. No connection is suggested for r = 0. The degree and direction of the link between two variables are revealed by the correlation coefficient. When "r" approaches 0 on either side, there is a weak link between the dependent variable and independent variable (Hair et al., 2010).

3.7.3.2. Multiple Regression Analysis

In multiple linear regression, it is believed that a variable Y (the dependent variable) and K independent variables Xj (j = 1, 2,..., K) have a linear relationship. When determining the effect of two or more independent variables on a dependent variable is sought, this technique of analysis is appropriate (Hair et al., 2010). The following multiple linear regression model was taken into consideration in order to examine the impact of the factors contributing to tax evasion (i.e., tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative attitude of tax payers toward tax, and tax compliance costs) have on tax evasion in Addis Ababa SMEs. The specified model looked like this:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \varepsilon$$

Where

Y = Tax Evasion,

X_1 = Tax Fairness,

X_2 = Tax Knowledge,

X_3 = Tax Penalties and Enforcements,

X_4 = Corruption

X_5 = Negative Taxpayers' Attitude towards Tax, and

X_6 = Tax Compliance Costs

β_1, β_2, β_3, β_4, β_5 & β_6 = beta coefficients,

β_0 = constant,

ε = other elements that were not considered in the research (0.05 random error)

However, in order to ensure the model is legitimate, it must first be checked to see if it adheres to certain assumptions common to linear regression models. Which are:

Sample Size and Observational Independence

The first assumption has to do with observational independence and sample size. Generalizability is in doubt in this situation. In other words, a researcher may obtain a result with

small samples that cannot be generalized (repeated) with bigger samples. If results cannot be transferred to other samples, they have little scientific importance. Then, how many cases or themes are needed? Numerous books frequently offer contradictory advice regarding the number of instances required for multiple regression. Tabachanick and Fidell (2007) give the following computation, taking into consideration the number of independent variables intended to be used, to determine the required sample size: In this scenario, there are 310 cases, therefore $N > 50 + 8m$ (where m is the number of independent variables), which is more than I would need since I have six independent variables. The independence of the observations was guaranteed because 310 different people each responded to one of the 310 questionnaires that made up the sample.

Detecting Outliers

Multiple regression allows for the highly sensitive detection of outliers (extremely high or low scores). The second premise is to look for inflated scores, and this ought to be done as part of the initial data screening process. It will be done for all of the dependent and independent variables used in the regression analysis. A variable value that is high but not significantly different from the other scores in the cluster can be assigned to outliers, or they can be eliminated from the data set altogether. Outliers can be located by examining the Skewness and Kurtosis values, which should be between -1 and 1, as well as the typical residual plot that can be requested (Hair et al., 2010).

Test for Homoscedasticity

The third supposition's focus is on the residuals' homoscedasticity. Remaining are the differences in scores between the obtained and predicted dependent variables (DVs). The residuals' value must remain constant for the duration of the observation interval, and the null value average must depict the homogeneous variance's center. The residual scatterplot charts of the model, which display whether or not there is a pattern and suggests equal variances, supported this supposition. The variance of the residuals about the expected dependent variable scores, or homoscedasticity, should be true for all predicted scores, claim Hair et al. (2010).

Normality Test

The topic of the fourth presumption is the normal distribution of residuals. The normal distribution of residuals graphic demonstrates the regularly distributed nature of the model's errors. The residuals should simply be normally distributed around the predicted dependent

variable scores, or simply the distribution mean should be 0 and the standard deviation should be 1 to indicate a normal distribution of errors (Hair et al., 2010).

Test of Linearity

The linearity assumption states that the small circles should be near the diagonal line or that the residuals should have a straight line relationship with the predicted scores of the dependent variables (Hair et al., 2010).

Test for Multicollinearity

The sixth assumption, which states that multicollinearity exists when there is a strong correlation between two or more independent or predictor variables in a regression model, has been tested for across all independent variables. Utilizing the correlation coefficients, with a correlation coefficient of 1 representing strong collinearity, is the easiest diagnostic for identifying the presence of multicollinearity. High correlations (generally 0.90 and higher; Hair et al. 2010) are typically indicative of strong collinearity, according to the general rule. Other common measurements are the tolerance value and the Variance Inflation Factor (VIF).

An extremely low tolerance value of 0.10 or a high VIF value of 10 or more, in accordance with Hair et al. (2010), are indicators of excessive collinearity. If there is significant collinearity between two independent variables, the researcher will omit that variable from the analysis. After making sure there isn't a lot of collinearity between the independent variables, the researcher will examine each independent variable alongside the dependent variable to discover its distinct effects on the dependent variable. The coefficient of determination (R^2) measures how much of the overall variance in the dependent variable can be accounted for by understanding the value of the independent variable. In the derived regression equation, the coefficient of determination (R^2) ranges from 0 (where the dependent variable does not change) to 1 (when all points are on the regression line), i.e., $0 < R^2 < 1$.

The Standard Multiple Regression approach was utilized to conduct a multiple linear regression analysis with SPSS software in order to test the suggested assumptions.

3.8. Definition and Operationalization of Variables

There are two major variables under this study. These are the dependent and independent variables. The dependent variable is tax evasion resulted from the six independent variables (i.e.,

tax fairness, tax knowledge, tax penalties and enforcements, corruption, negative attitude of tax payers toward tax, and tax compliance costs) in the study area.

3.8.1. Dependent Variable

3.8.1.1. Tax Evasion

The concept of employee performance refers to the level and quality of effort, cooperation, commitment, tardiness and absence,

According to Korndörfer et al. (2014), tax evasion is a criminal act that violates the law and departs from social norms that call for paying taxes. Tax evasion is "the willful attempt to defeat or circumvent the tax law in order to illegally reduce one's tax liability," according to Gottschalk (2010). Tax evasion is characterized as a criminal act committed while paying taxes. It occurs when taxpayers purposefully fail to pay their taxes, either by failing to file their returns, reporting their income incorrectly, or paying less than the actual amount owed despite being able to do so (Rashid, 2020). It was operationalized using eight items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of tax evasion.

3.8.2. Independent Variable

3.8.2.1. Tax Fairness

Tax Fairness is characterized by taxpayers' desire to pay the tax assessed and its effect on the fight against tax evasion. The belief that the tax system is fair is one of several elements that affect taxpayers' impression of tax evasion (Rashid, 2020). Tax fairness is a factor that encourages tax evasion among taxpayers and is a non-economic factor that affects a nation's tax collection (Alleyne & Harris, 2017). It was operationalized using five items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of tax fairness.

3.8.2.2. Tax Knowledge

The degree to which a taxpayer is knowledgeable and aware of tax-related issues affects that taxpayer's attitude significantly, and a taxpayer who is knowledgeable about taxes will be aware

of their rights, obligations, and the processes involved in paying taxes as well as the repercussions of non-compliance (Machogu & Amayi, 2013). Tax knowledge serves as a beneficial tool to encourage taxpayers to desist from tax evasion by giving them a grasp of the country's tax structure and laws (Pui Yee et al., 2017). It was operationalized using five items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of tax fairness.

3.8.2.3. Tax Penalties and Enforcements

A fine or penalty is cash that is typically paid to a government agency as retribution for a crime or other offense (Muoki et al., 2014). The steps taken when taxpayers pay less tax than their actual obligations or fail to file their income tax return at all are referred to as tax fines and enforcement initiatives (Calimani & Pellizzari, 2014). It was operationalized using five items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of tax penalties and enforcements.

3.8.2.4. Corruption

According to Nelson (2015), the presence of corruption among politicians, bureaucrats, government employees, and their family and friends in a state encourages the behavior intention of taxpayers toward tax cheating. Moreover, when it is believed that the government is corrupt, tax evasion is defended as ethical (Oberholzer & Stack, 2014; Alasfour et al., 2016). It was operationalized using four items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of corruption.

3.8.2.5. Negative Taxpayers' Attitude towards Tax

A person's attitudes are their positive and negative evaluations of objects, concepts, or living things (Ahmed & Kedir, 2015). Therefore taxpayers who view taxes favorably are more likely to carry out their obligations to the authority and those who are opposed to paying taxes are less

inclined to do so (Assfaw & Sebhat, 2019). This variable was operationalized using five items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of negative taxpayers' attitude towards tax.

3.8.2.6. Tax Compliance Costs

Businesses must pay fees to comply with tax regulations, which are separate from their tax obligations. The cost experienced by taxpayers to satisfy their statutory tax duties in addition to their real tax debt is referred to as "tax compliance cost" (Abdul-Jabbar & Pope, 2008). The three main components of tax compliance costs are financial expenses, time-related costs, and psychological costs to the taxpayers (Evans, 2008). The cost of employing tax professionals (such as tax agents and accountants), as well as the cost of taxation manuals, books, communications, and other incidentals, are all examples of money-related charges. Time costs include the time a taxpayer spends maintaining records for the purpose of submitting a tax return, putting together tax data for tax professionals, and communicating with the tax authorities. One instance of a psychological cost is the stress associated with addressing complicated tax issues (Smulders et al., 2012). This variable was operationalized using six items; managers and owners of SMEs in Addis Ababa were requested to rate the variable on five points Likert-scale measurement: strongly agree (5), agree (4), neutral (3), disagree (2) and strongly disagree (1). Using this approach, the researcher treated these questions as formative indicators of tax compliance costs.

3.9. Ethical Considerations

A researcher must abide by the principle of voluntary consent, which calls for respondents to consent to participate in research voluntarily, according to Mugenda & Mugenda (2003). Informed consent should be based on details like the research project's purpose, the researcher's identity, and any potential benefits. According to Mugenda and Mugenda (2003), participation in research is voluntary and subjects are free to leave the study at any time without facing any repercussions. Before the study began, the researcher informed the respondents of this. To make sure that all respondents understood every aspect of the study, the researcher trained assistants. No respondent was coerced into participating in the study; all participation was voluntary.

According to Creswell (2009), plagiarism is the act of misrepresenting someone else's work as your own by taking credit for their hard work. It occurs when you use someone else's ideas as though they are your own. The utmost care was taken to ensure that all work that was taken from other academics was properly cited.

CHAPTER FOUR

4. DATA PRESENTATION, ANALYSIS AND DISCUSSIONS

The researcher's investigation, which was carried out utilizing the procedures described in Chapter 3, was summarized in this chapter. It includes demographic data on the respondents, background data on SMEs, a thorough discussion of the three specific goals, an analysis of descriptive statistics, and correlation and regression tests using IBM SPSS version 23. Cronbach alpha was used to assess the internal consistency of the major factors influencing tax evasion dimensions in SMEs under Addis Ababa City Administration, and content validity was assessed by selecting pre-existing scales from the pertinent literature. In light of the literature review presented in Chapter Two, the study's results were also examined.

4.1. Questionnaire Response Rate

The study's target sample size was 371 respondents, as shown in Table 4.1 below, and 310 of them completed and returned surveys, yielding an 83.56 percent response rate. Because it acted as a representative sample, this response rate was ideal for drawing conclusions about the study (Mugenda & Mugenda, 2003).

Table 4.1: Questionnaire Response Rate

Questionnaires Issued	Fully Returned	Percentage of Return Rate
371	310	83.56%

Source: Own Survey Result (2023)

4.2. Reliability and Validity Assessment Results

How closely the actual results match those anticipated serves as a gauge of how reliable the data collection techniques used in the study were. The word "reliability" describes a measurement of the consistency of the variables under investigation. The reliability of the data was compared to the explanatory factors using the Cronbach's Alpha test, as shown in Table 4.2 below. For all variables taken into consideration, Cronbach's Alpha Statistics for the explanatory factors exceeded the permitted standard of 0.7 (Hair et al., 2010). This may indicate that the study's data was accurate and reliable. Additionally, validity is referred to as an investigation's credibility (Creswell, 2009). It has to do with figuring out whether the tools used to collect the data accurately reflect what they should be counting. The researcher worried about content validity by

merely examining the content of data collection tools to ascertain whether they were genuine, with the approval of her supervisor. The researcher adhered to Cooper and Schindler's (2011) recommendations, which included locating pre-existing scales in the pertinent literature, in order to obtain content validity.

Table 4.2: Reliability Analysis Results

Variables	Number of Items	Cronbach Alpha
Tax Fairness	5	0.850
Tax Knowledge	5	0.860
Tax Penalties and Enforcements	5	0.895
Corruption	4	0.799
Negative Taxpayers Attitude toward Tax	5	0.895
Tax Compliance Costs	6	0.895
Tax Evasion	8	0.932

Source: Own Survey Result (2023)

4.3. Background Information of the Respondents

The background of the SMEs and the respondents' demographic traits are covered in this section.

4.3.1. Demographic Characteristics of the Respondents

Gender, age, marital status, and level of education are all included in the demographic characteristics of the respondents. The frequency and proportion of SMEs' owners or managers who responded to the Addis Ababa City Administration's survey are shown below.

According to Table 4.3 below, there were 240 (77.4%) male respondents and 70 (22.4%) female respondents who were the owners or managers of SMEs in Addis Ababa City Administration respondents. This demonstrates the dominance of men in the management of SMEs in Addis Ababa town. On the other hand, as shown in Table 4.3 below, 165 respondents, or 53.2% of the total, fell into the age range of 31 to 40 years. The remaining 85 (27.4%), 51 (16.5%), and 9 (2.9%) owners or managers of SMEs were, respectively, between the ages of 20 and 30; 41 and 50; and above 50. This demonstrates that the majority of the SME sector in the town is managed and owned by the young population.

Table 4.3: Demographic Characteristics of the Respondents

No	Indicators	Category	Frequency	Percent
1	Gender	Male	240	77.4%
		Female	70	22.6%
Total			**310**	**100.0%**
2	Age	20-30 years	85	27.4%
		31-40 years	165	53.2%
		41-50 years	51	16.5%
		Above 50 years	9	2.9%
Total			**310**	**100.0%**
3	Marital Status	Single	85	27.4%
		Married	166	53.5%
		Divorced	39	12.6%
		Widowed	20	6.5%
Total			**310**	**100.0%**
4	Educational Level	Primary School	53	17.1%
		Secondary School	123	39.7%
		Diploma	71	22.9%
		First degree	50	16.1%
		Master's degree and above	13	4.2%
Total			**310**	**100.0%**

Source: Own Survey Result (2023)

More than half of the respondents, or 166 (53.5%), were married, as can be seen in Table 4.3 above regarding their marital status. The remaining owners or managers of the SMEs 85 (27.4%), 39 (12.6%), and 20 (6.5%) were single, divorced, and widowed, respectively. This finding indicates that married individuals managed and owned the majority of the SMEs in Addis Ababa City Administration.

Regarding the respondents' educational backgrounds, as shown in Table 4.3 above, the majority, or 123(39.7%), of the SMEs owners or managers were educated up to the secondary school level, followed by 71(22.9%) of the respondents who held diplomas, 53(17.1%) of the respondents

who were educated up to the primary school level, 50(16.1%) of the respondents who had first degrees, and only 13(4.2%) of the respondents who had master's degrees or higher. The findings indicate that every respondent has the level of literacy necessary to comprehend the questions posed, and as a result, they can all provide accurate information about the tax evasion committed by SMEs. As a result, the tax authority can easily inform the taxpayer about the relevant laws, rules, and regulations.

4.3.2. Background Information of the SMEs

This section covers the business sectors that SMEs engage in, the different business ownership structures that exist today, and the tax experiences that SMEs have. The frequency and percentage of the SMEs' backgrounds are shown in Table 4.4 below.

According to Table 4.4 below, the majority of SMEs—or nearly half (47.1%) of the 146 SMEs in the Addis Ababa City Administration—were engaged in trade-related business activities. followed by 112 (36.1%) SMEs engaged in the service sector, 25 (8.1%) SMEs engaged in manufacturing, 16 (5.2%) SMEs engaged in construction, and 16 (5.2%) SMEs and only 11 (3.5%) of the SMEs in the Addis Ababa City Administration were engaged in urban agriculture, coming in fifth place behind. As a result of the low startup costs for such businesses, this result showed that the majority of SMEs operating in Addis Ababa City Administration were in the trade sector. The manufacturing and construction industries, which need a lot of money and knowledge, cannot say the same. This outcome might support the tax authority's efforts to manage taxpayers strategically and effectively in order to prevent tax evasion.

According to Table 4.4 below, the majority of the SMEs in the study area—205, or 66.2%—were owned by sole proprietorships, followed by partnerships (63, or 20.2%), private limited companies (27, or 8.7%), and 15 (4.8%), which were owned by cooperatives and families. With over two thirds of the SMEs in the Addis Ababa City Administration controlled by sole proprietorships, this result amply demonstrates the dominance of these business forms.

According to Table 4.4 below, the majority of SMEs—151, or 48.7%—had experience paying taxes for more than ten years. Following closely behind were 118, or 38.1%, who had experience paying taxes for five to ten years, and only 41, or 13.2%, who had experience paying taxes for less than five years. This finding suggested that the majority of the SMEs included in this study

had more than ten years of tax experience. This can make it easier for the tax authorities to explain the causes of and effects of tax evasion on the expansion of the nation's economy.

Table 4.4: Background of the SMEs

No	Indicators	Category	Frequency	Percent
1	SMEs Sector of Business Activities	Trade	146	47.1%
		Services	112	36.1%
		Urban Agriculture	11	3.5%
		Manufacturing	25	8.1%
		Construction	16	5.2%
Total			**310**	**100.0%**
2	Forms of Business Ownership	Sole Proprietorships	205	66.2%
		Partnership	63	20.3%
		Private Limited Companies	27	8.7%
		Other Associations	15	4.8%
Total			**310**	**100.0%**
3	Tax Experience of SMEs	Below 5 years	41	13.2%
		5 to 10 years	118	38.1%
		More than 10 years	151	48.7%
Total			**310**	**100.0%**

Source: Own Survey Result (2023)

4.4. Descriptive Analysis of the Study Variables

This section of the analysis was created using data from a survey that was conducted using a 5-point Likert scale and completed by 310 owners or managers of SMEs in the Addis Ababa City Administration. Tax Fairness, Tax Knowledge, Tax Penalties and Enforcements, Corruption, Negative Taxpayers' Attitude toward Tax, and Tax Compliance Costs are the study's six independent variables. Tax Evasion is the study's dependent variable. The following criterion, which is described in Table 4.4, was applied to ensure consistency in the interpretation of descriptive analysis.

Table 4.5: Five-Scaled Likert's Criterion

No.	Mean Range	Response Options
1	[1.00, 1.80)	Strongly Disagree
2	[1.80, 2.60)	Disagree
3	[2.60, 3.40)	Neutral
4	[3.40, 4.20)	Agree
5	[4.20, 5.00]	Strongly Agree

Source: Al-Sayaad et al. (2006)

4.1.1. Factors Contributing to Tax Evasion Dimensions

The researcher used statements to evaluate the levels of the six variables of factors contributing to tax evasion dimensions in the chosen SMEs of Addis Ababa City Administration in order to identify the factors that may contribute to tax evasion. The degree to which each participant agreed with the aforementioned statements was rated. On a 5-point Likert scale, where 1 signified Strongly Disagree, 2 meant Disagree, 3 meant Neutral, 4 meant Agree, and 5 meant Strongly Agree, the responses were scored. Beside this the result of the interviewed auditors of ERCA also presented after the descriptive statistics results of data collected from SMEs owners and managers for each variables of the study.

4.4.1.1. Tax Fairness

According to the results shown in Table 4.6 below, the tax fairness items had average mean scores between 2.06 and 2.14 and standard deviation scores between 0.66 and 0.70. Because the mean values fall between 1.80 and 2.60, as described by Al-Sayaad et al. (2006), this showed that the owners or managers of the selected SMEs of Addis Ababa City Administration disagreed on the overall items of tax fairness dimensions. In addition, the five questions with a standard deviation of less than 1 demonstrated that respondents' perspectives on the issues are generally similar. This result showed that there was disagreement among the owners or managers of the chosen SMEs of the Addis Ababa City Administration regarding the absence of tax corruption, the fairness of tax collection practices and principles, and the non-discriminatory tax assessment. The respondents were divided on whether there was consistency in the tax burden or whether the tax assessment was not made based on subjective judgments. The respondents also disagreed that

there is a lack of ambiguity in tax laws that causes them to be interpreted incorrectly and that a sizable portion of the funds raised is used for initiatives that do not directly benefit them.

Table 4.6: Descriptive Statistics of Tax Fairness

Code	Statements on Tax Fairness	Statistics	
		Mean	**STD**
TF1	There is no existence of corruption practice in the tax system	2.09	0.67
TF2	The tax collection procedures and principles are fair or there is no discriminatory tax assessment	2.14	0.67
TF3	There is no inconsistency in tax burden or the tax assessment is not based on arbitrary decisions	2.06	0.70
TF4	There is no ambiguity of tax regulations that leads to misinterpretation of tax regulations	2.13	0.66
TF3	A large portion of the money collected is spent on projects that does benefit me	2.06	0.68
Aggregate Mean and Standard Deviation		**2.10**	**0.68**

Source: Own Survey Result (2023)

The aggregate mean of 2.10 and the standard deviation of 0.68 also indicated that the tax system was unfair, as evidenced by the existence of corrupt tax practices, unfair tax collection practices, principles, and discriminatory tax assessments, as well as by the existence of inconsistent tax burdens or assessments based on arbitrary judgments. Taxpayers also believed that the tax system was unfair because a sizable portion of the money collected is spent on initiatives that do not benefit them, which was the result of the ambiguity of tax regulations, which causes misinterpretation of tax regulations.

The results of the interview are nearly identical to the results of the earlier study: taxpayers are occasionally required to pay unauthorized tax expenses because they fail to maintain the required records for taxation. This might be the result of the taxpayer being aware of the expenses that can be written off from taxes and submitting the necessary paperwork to the tax authority on time. As a result, assessments or tax burdens may be determined arbitrarily, leading to unfairness in the tax system. According to the respondents to the interviews, some SMEs base their tax

payments on arbitrary calculations of daily income or estimates of average daily revenue, which has drawn criticism from taxpayers who believe the tax system is unfair.

The tax officials interviewed stated that determining tax liability based on arbitrary daily income decisions or average daily revenue estimates resulted in many of the SMEs taxpayers' suspicions because businesses engaged in the same activities in the same geographic location were occasionally assessed by different individuals or even different committees. This confirmed many of the SMEs taxpayers' suspicions. Different assessors and committees applied the assessment standards differently because they lacked objectivity and comparability. Because of this, SMEs taxpayers believed the tax system was unfair and were biased when determining tax liabilities among taxpayers operating similar kinds of businesses. Additionally, according to interviewed respondents, some wholesalers sell goods to retailers without giving them receipts, which makes it challenging for the tax authority to determine the source document for taxes. Inequity in the tax system resulted from the tax authority making arbitrary decisions regarding the taxation of retailers or SMEs as a result of this.

4.4.1.2. Tax Knowledge

As can be seen in Table 4.7 below, the average mean score for the tax knowledge items ranged from 2.05 to 2.12, and the standard deviation was between 0.66 and 0.74. Because the mean values range between 1.80 and 2.60, it was clear that the owners or managers of the selected SMEs of the Addis Ababa City Administration disagreed on the overall items of tax knowledge dimensions (Al-Sayaad et al., 2006). In addition, the five questions with a standard deviation of less than 1 demonstrated that respondents' perspectives on the issues are generally similar. This result showed that there was disagreement among the owners or managers of the chosen SMEs of the Addis Ababa City Administration regarding their knowledge of the sources of income they must declare, their payment of taxes in anticipation of receiving public services, and their understanding of the legal repercussions of intentional tax evasion. The respondents disagreed with the statements that the tax authorities gave them various training about tax evasion and other tax-related issues, as well as the statements that they were well-informed about taxes and tax evasion.

The aforementioned findings were also supported by the aggregate mean and STD value of 2.08 and 0.69, as shown in Table 4.7 below, and they also demonstrated that taxpayers lacked

knowledge of the tax system. This was a result of their ignorance of the sources of income they were required to report to the tax authorities, of the fact that taxes were paid in anticipation of public services, and of the legal repercussions of intentional tax evasion. In addition, the respondents claimed that they lacked sufficient knowledge of taxes and tax evasion, and that neither they nor the taxpayers had received any training from the tax authorities on these or other tax-related topics.

Table 4.7: Descriptive Statistics of Tax Knowledge

Code	Statements on Tax Knowledge	Statistics	
		Mean	**STD**
TK1	I know well which sources of income I must declare	2.09	0.69
TK2	Tax is paid in anticipation of public services	2.05	0.74
TK3	I know about criminal penalties for intentional tax evasion	2.08	0.68
TK4	I am well informed about tax and tax evasion	2.08	0.67
TK5	The tax authorities provided me different training about tax evasion and other tax-related issues	2.12	0.66
Aggregate Mean and Standard Deviation		**2.08**	**0.69**

Source: Own Survey Result (2023)

According to the respondents who were interviewed, the tax authority is not adequately supplying SMEs with the necessary awareness or knowledge about taxation. The tax authorities do not implement ongoing education programs or efficient monitoring procedures to ensure that taxpayers have a good and reasonable understanding of tax matters. The respondents who were interviewed stated that since the success of tax education depends on the readiness, acceptance, and honesty of taxpayers, the awareness and attitude of the taxpayer himself is more crucial. In addition, the respondents who were interviewed said that the SMEs taxpayers would be compelled to engage in tax evasion because they were poorly informed about the significance of taxes for the development of the nation and the grave problems associated with it.

4.4.1.3. Tax Penalties and Enforcements

According to Table 4.8 below, the tax penalties and enforcements items had an average mean score between 2.11 and 2.18 and a standard deviation value between 0.69 and 0.72. Because the mean values range between 1.80 and 2.60, it was clear that the owners or managers of the

selected SMEs of the Addis Ababa City Administration disagreed on the overall items of tax penalties and enforcements (Al-Sayaad et al., 2006). In addition, the five questions with a standard deviation under 1 demonstrated that respondents' perspectives on the issues were similar. This outcome showed that there was disagreement among the owners or managers of the chosen SMEs of the Addis Ababa City Administration regarding the fines and penalties imposed on MSEs who evade taxes, the sufficiency of the current penalties to force MSEs to obey tax laws, as well as the ability of the anti-corruption commission to take action against tax evaders. The respondents also disagreed that the tax authorities punished MSEs who failed to file taxes and that the tax laws were fairly and consistently applied to MSEs who failed to file their income tax returns.

Table 4.8: Descriptive Statistics of Tax Penalties and Enforcements

Code	Statements on Tax Penalties and Enforcements	Statistics	
		Mean	**STD**
TPE1	Fines and penalties are imposed on the MSEs who evade tax	2.14	0.71
TPE2	Currents penalties are enough to make MSEs obey tax laws	2.11	0.71
TPE3	The anti-corruption commission is capable of taking action against tax evaders	2.13	0.69
TPE4	The tax authority will punish MSEs who do not file taxes	2.13	0.72
TPE5	The tax laws are enforced on those MSEs that are not submitting their income tax return	2.18	0.69
Aggregate Mean and Standard Deviation		**2.14**	**0.70**

Source: Own Survey Result (2023)

The results are also supported by the aggregate mean and STD value of 2.14 and 0.70, as shown in Table 4.8 above. This result showed that MSEs who evade taxes are not subject to fines or penalties, that the current penalties are insufficient to force MSEs to comply with tax laws, and that the anti-corruption commission is powerless to prosecute tax evaders. In addition, the outcome demonstrated that MSEs who do not file taxes were not penalized by the tax authority, and those MSEs who do not consistently file their income tax returns were not subject to the tax laws' enforcement.

These outcomes match those of the respondent who was questioned. To force SMEs to abide by tax laws, not enough fines and penalties were imposed on those who evade taxes on them, and the tax authority did not penalize those who do not consistently file taxes and submit income tax returns. This is because the managers or owners of SMEs failed to record all of their transactions for taxation-related reasons and also carried out transactions without receipts. In addition, the respondents who were interviewed said that the decision to evade taxes depends on the severity and frequency of fines and penalties; if tax authorities believe they will catch them, they will punish them; otherwise, they will decide to evade taxes if they believe they won't be caught. In other words, there will be less tax evasion if the rate of fines and penalties is high.

4.4.1.4. Corruption

According to Table 4.9 below, the corruption items had an average mean score between 3.71 and 3.81 and a standard deviation value between 0.64 and 0.68. The fact that the mean values fall between 3.40 and 4.20 indicates that the owners or managers of the chosen SMEs of Addis Ababa City Administration concurred on the overall items of corruption (Al-Sayaad et al., 2006). In addition, the four questions that had a standard deviation value less than 1 demonstrated those respondents' perspectives on the issues were similar. This result showed that the owners or managers of the chosen SMEs of the Addis Ababa City Administration agreed that there is too much corruption in the operations of the tax authority and a sizable portion of the money raised from taxes ends up in the pockets of dishonest politicians or their families and friends. The respondents also concurred that there is widespread corruption among government employees and bureaucrats, and that the tax authority discriminates against people based on their race, religion, or ethnicity.

The results are also supported by the aggregate mean of value 3.75 and STD of 0.66, as shown in Table 4.9 below. According to this finding, tax payers believed that the tax authority's operations were too corrupted and that its employees discriminated against people based on their religion, race, or ethnicity. Additionally, according to the respondents, there is a high level of corruption among bureaucrats and government employees, and a sizeable portion of the tax revenue ends up in the pockets of dishonest politicians or their relatives and friends.

Table 4.9: Descriptive Statistics of Corruption

Code	Statements on Corruption	Statistics	
		Mean	STD
CR1	There is too much corruption in the tax authority operations	3.76	0.65
CR2	A significant portion of the money collected from taxes winds up in the pocket of corrupt politicians or their families and friends	3.81	0.64
CR3	There is a high level of corruption among bureaucrats and government officials	3.71	0.66
CR4	The tax authority discriminates against people because of their religion, race, or ethnic background	3.71	0.68
Aggregate Mean and Standard Deviation		**3.75**	**0.66**

Source: Own Survey Result (2023)

4.4.1.5. Negative Taxpayers Attitude toward Tax

According to Table 4.10 below, the average mean score for the taxpayers who had a negative attitude toward tax-related items was between 3.90 and 4.05, with a standard deviation between 0.67 and 0.76. Because the mean values fall between 3.40 and 4.20, this showed that the owners or managers of the chosen SMEs of Addis Ababa City Administration agreed on the overall items of taxpayer's attitude toward tax (Al-Sayaad et al., 2006). In addition, the five questions with a standard deviation under 1 demonstrated that respondents' perspectives on the issues were similar. This result showed that the owners or managers of the chosen SMEs of the Addis Ababa City Administration agreed that the tax system was unfair and unequal, that the tax administration was ineffective at identifying SMEs who inaccurately reported their income and punishing tax evaders, and that tax evasion was not regarded as a serious offense. The respondents also concurred that the nation's tax system as a whole is too complicated to comprehend, and they saw tax evasion as moral behavior because social justice is not universally practiced.

The results are also supported by the aggregate mean value of 3.96 and STD of 0.71, as shown in Table 4.10 below. This result showed that taxpayers believed the tax system to be unfair and unequal, that the tax administration was ineffective at identifying small businesses that reported their income inaccurately and pursuing tax evaders, and that taxpayers did not view tax evasion

as a serious crime or offense. In addition, the respondents said that because social justice is not well established throughout the nation, they believed tax evasion to be an ethical behavior and that the overall tax system is too complex to understand.

SMEs taxpayers do not currently associate any social services provided by the government with tax; instead, they simply view tax as a payment to the government, according to the majority of tax officials interviewed. They also clarified that the majority of SMEs taxpayers and even large business taxpayers do not take into account wealth distribution or social services, but they pay taxes because ERCA requires them to. This finding suggested that SMEs taxpayers have a negative attitude toward taxes, but the tax officials who were interviewed said that there are only a very small number of devoted taxpayers in the nation, so their responses cannot be considered representative of all taxpayers who might have similar questions.

Table 4.10: Descriptive Statistics of Taxpayers Attitude toward Tax

Code	Statements of Negative Taxpayers Attitude toward Tax	Statistics	
		Mean	**SD**
TAT1	The tax system is unequal and unfair	3.96	0.70
TAT2	The tax administration is inefficient to find out SMEs who declare their income inaccurately and thereby punish tax evaders	3.92	0.76
TAT3	Tax evasion is not considered a serious offense	3.90	0.71
TAT4	The overall tax system is too complex to understand	4.05	0.67
TAT5	Tax evasion is ethical because social justice is not established all over the country	3.97	0.69
Aggregate Mean and Standard Deviation		**3.96**	**0.71**

Source: Own Survey Result (2023)

According to the tax officials who were interviewed, SMEs taxpayers have a lower propensity to evade taxes if they believe the tax system is fair. In addition, according to the tax officials who were interviewed, citizens will only agree to pay taxes if they believe that the tax rate is within their means, that a sizable portion of the money collected is used wisely and invested in worthwhile initiatives that benefit the citizens, and that the level of general government service is adequate. But in this instance, the opposite is true. The tax officials who were interviewed revealed that some of the actions taken by SMEs taxpayers to avoid tax assessment by ERCA

officials included: Removing or hiding goods from retail shelves to reduce the cost of the average daily revenue estimation, giving the tax officials inaccurate and inappropriate information, purposefully closing their businesses to avoid tax assessment, and also leaving intentionally unsuitable individuals in charge of their shops who were not knowledgeable about the business and were unable to provide the necessary information to the tax officials, etc.

4.4.1.6. Tax Compliance Costs

According to Table 4.11 below, tax compliance costs items had an average mean score between 3.85 and 3.90 and a standard deviation value between 0.67 and 0.77. The fact that the mean values fall between 3.40 and 4.20 indicates that the owners or managers of the selected SMEs of Addis Ababa City Administration concurred on the overall items of tax compliance costs (Al-Sayaad et al., 2006). In addition, the six questions with a standard deviation under 1 demonstrated that respondents' perspectives on the issues were similar. This result showed that the owners or managers of the selected SMEs of the Addis Ababa City Administration agreed that the cost of stationery, a computer, a cash register machine and its operation, as well as the cost of software and the internet is high for them and that the penalty for failing to pay taxes is less severe than the tax savings. The respondents concurred that it would be expensive for them to hire salespeople and accountants, so they typically pay extra money for external services (tax consultants) to file their tax returns.

The results are also supported by the aggregate mean value of 3.88 and STD of 0.72, as shown in Table 4.11 below. This result showed that tax payers believed the penalty for not paying tax was less severe than the amount of money they would have saved by paying it; they also believed that the costs associated with complying with tax laws, such as those for stationery, computers, cash registers and their maintenance, software, and the internet, as well as the salaries of salespeople and accountants, were high. Additionally, the outcome showed that the managers or owners of SMEs frequently pay additional fees for external services (tax consultants) in order to file tax returns.

Table 4.11: Descriptive Statistics of Tax Compliance Costs

Code	Statements on Tax Compliance Costs	Statistics	
		Mean	**STD**
TCC1	The penalty due to not paying tax is lower than my tax saving	3.87	0.67
TCC2	Cost of stationaries, computer, etc. is high	3.90	0.77
TCC3	Cost of cash register machine and its operation is high	3.85	0.71
TCC4	Cost of software and internet is high	3.89	0.77
TCC5	Cost of hiring staff such as accountant and sales man is high	3.87	0.69
TCC6	Most of the time I hire external services (tax consultant) to file tax returns and I pay additional costs	3.88	0.71
Aggregate Mean and Standard Deviation		**3.88**	**0.72**

Source: Survey Data Output (2023)

The cost of tax services to SMEs is a complicated issue, according to all of the tax officials who were interviewed. Even though the cost is not very high compared to the services offered to them, the majority of SMEs are unaware of the importance of the services. As a result, they are hesitant to pay or value the contribution and work of the tax consultants. Due to the aforementioned factors, the majority of tax officials reported that the hired tax consultants pay their service fees promptly, that is, as soon as the work is finished but before delivering it to the enterprises. This indicates that after the service is provided, the majority of SMEs' owners hesitates or delay paying their service fees. Similar to this, tax officials stated that while the tax consultant's service fee can have a small impact on SMEs' decisions to evade taxes, the intention to do so, the process for filing returns with the Tax Authority, and the salaries of accountants and the cost of stationery have a larger impact.

In addition, the tax officials who were interviewed said that it is expensive for SMEs to maintain accounting records because they must hire an accountant, rent offices, and buy computers, stationery, and software, among other expenses. The filing of monthly and quarterly tax returns, which can take up to three days or longer, is another time-consuming process that is expensive for SMEs. Accordingly, tax evasion by SMEs profit taxpayers is influenced by compliance costs such as accountants' salaries, tax consultants' fees, the cost of cash register machines and their

maintenance, the time required to file VAT and TOT and income declarations, and the cost of computers, stationery, and software used in the record-keeping process.

4.4.1. Descriptive Statistics Analysis of Tax Evasion Dimensions

Tax evasion dimensions were evaluated using eight measurement items, as shown in Table 4.12 below, with mean scores ranging from 3.80 to 3.92 and standard deviations between 0.66 and 0.73. This demonstrates that the owners or managers of the selected SMEs of Addis Ababa City Administration were in agreement that the high rates of income tax, low rates of penalties, a low likelihood of detection, the complexity and unfairness of the tax system, the weakness of the audit system, and the inefficiency of the tax authorities were the causes or reasons for taxpayers to engage in tax evasion. Additionally, the owners or managers of the chosen SMEs of Addis Ababa City Administration concurred that the majority of MSEs taxpayers do not report all of their income to the authority, and they perceived tax evasion as ethical behavior because they believed a significant amount of the money collected by the public authorities was wasted. The results are also supported by the aggregate mean of 3.86 and STD of 0.69, as shown in Table 4.12 below.

Table 4.12: Descriptive Statistics of Tax Evasion Dimensions

Code	Statements on Tax Evasion	Mean	STD
TE1	High rates of income tax are one of the reasons for tax evasion	3.92	0.66
TE2	Low rates of penalties are responsible for causing tax evasion	3.80	0.69
TE3	A low probability of detection may be the cause of tax evasion	3.83	0.73
TE4	The weakness of the audit system is responsible for allowing tax evasion	3.90	0.67
TE5	The unfairness of the tax system is the causes of tax evasion	3.86	0.70
TE6	The inefficiencies of the tax authorities are the causes of tax evasion	3.92	0.66
TE7	Tax evasion is ethical if a large portion of the money collected by the public authorities is wasted	3.83	0.73
TE8	The complexity in the tax system is the reason for tax evasion	3.86	0.70
Aggregate Mean and Standard Deviation		**3.87**	**0.69**

Source: Survey Data Output (2023)

In addition to the aforementioned closed-ended questions, the ERCA tax officials who were being interviewed were also given the chance to voice their opinions via the provided open-ended questions. What recommendations do you have to lessen tax evasion in city SMEs or, better yet, the entire country?

As a result, the majority of those who were questioned ERCA tax officials and asked for their opinions on how to reduce tax evasion in SMEs run by the Addis Ababa City Administration did so. Although there were many comments, the general themes are almost identical to those that were covered in the above closed-ended questionnaire. Therefore, it can be said that the tax evasion of SMEs can be minimized by opening new branches close to the taxpayers, improving internet connections, streamlining tax filing and collection procedures by introducing e-filling and e-payment systems, strengthening bonds and establishing trust with the taxpayers by communicating the tax programs with the taxpayers, creating awareness through regular training and education on tax laws and procedures, ensuring fairness in the tax system and by making accessible of any changes to the tax laws and directives to the taxpayers timely.

4.5. Results of Inferential Statistics

The results of inferential statistics are presented in this section. Multiple Regression Analyses and Pearson's Correlation Coefficient were performed in order to achieve the study's goals. Using inferential statistical techniques, conclusions and decisions about the research hypothesis are produced and presented below.

4.5.1. Pearson Correlation Analysis

A statistical method for assessing the strength of a linear relationship between two variables is correlation analysis. The correlation coefficient, which is always between -1 and +1, was used to estimate the magnitude and strength of the linear relationship between two variables. A correlation coefficient of 1 denotes a significant and positive linear relationship between two variables. On the other hand, a correlation value of -1 denotes a strong negative linear relationship between two series. When the correlation between two variables is 0, it means that there is no linear relationship between them. The correlation result in Table 4.14 below demonstrates the significant positive and negative relationship between the independent variables and the dependent variable. Table 4.13 below provides a general rule of thumb for the strength of correlation of coefficients.

Table 4.13: Rule of Thumb for about the Strength of Correlation of Coefficients

Range of Coefficient Description of Strength	Range of Coefficient Description of Strength
±0.81 to ±1.00	Very Strong
±0.61 to ±0.80	Strong
±0.41 to ±0.60	Moderate
±0.21 to ±0.40	Weak
±0.00 to ±0.20	None

Source: Bhattacherjee (2012)

The coefficient of correlation between tax fairness and tax evasion, which is listed in Table 4.14 below, was -0.752, indicating a strong and adverse relationship between the two. The relationship is significant at the 0.01 or 1% level of significance. This suggests that when tax justice or fairness is functioning effectively, it will lessen taxpayers' tax evasion. Tax justice also seems to have a strong and negative relationship with tax evasion. The findings of this study are consistent with those of Manaye et al. (2020) study, which found that if the government wants to lessen the scope of tax evasion, it should implement fair tax policies. Therefore, greater tax fairness can discourage taxpayers from engaging in tax evasion.

Tax knowledge was another variable used in the study. The relationship between tax knowledge and tax evasion is significant at the 0.01 or 1% level of significance, as shown in Table 4.16 below. The coefficient of correlation between tax knowledge and tax evasion is -0.742, indicating that there is a negative and strong correlation between tax knowledge and tax evasion. This suggests that SMEs taxpayers will be less likely to engage in tax evasion activities if they have a good understanding of the tax system. This result is consistent with that of Assfaw and Sebhat (2019), who discovered that taxpayers who are more aware of their tax obligations are less likely to engage in tax evasion activities.

According to Table 4.14 below, there was a -0.612 correlation between tax fines and enforcements and tax evasion. This graph shows that there is a strong and unfavorable relationship—significant at the 1% level of significance—between tax penalties and enforcements and tax evasion among MSE taxpayers in Addis Ababa. This suggests that tax evasion will decline as tax collectors increase their tax penalties and enforcement efforts. This

finding is consistent with the finding of Alm (2019), which suggests that enforcing penalties for tax fraud can reduce tax evasion because the news of such sanctions frequently makes tax cheats more risk-averse.

Table 4.14: Correlation Coefficient Matrix

	TE	TF	TK	TPE	CR	TAT	TCC
TE	1						
TF	-.752**	1					
TK	-.742**	.747**	1				
TPE	-.612**	.586**	.523**	1			
CR	.659**	-.516**	-.524**	-.388**	1		
TAT	.825**	-.657**	-.650**	-.590**	.565**	1	
TCC	.807**	-.656**	-.627**	-.467**	.562**	.719**	1
**. Correlation is significant at the 0.01 level (2-tailed).							
TE = Tax Evasion, TF = Tax Fairness, TK = Tax Knowledge, TPE = Tax Penalties & Enforcements, CR = Corruption, TAT = Negative Taxpayers' Attitude towards Tax, and TCC = Tax Compliance Costs							

Source: Survey Data Output (2023)

According to Table 4.14 above, the correlation between corruption and tax evasion was 0.659. This demonstrated that there is a strong and favorable relationship—significant at the 1% level of significance—between tax evasion and corruption among MSE taxpayers in Addis Ababa. The SMEs taxpayers in Addis Ababa may have simply believed that the presence of excessive corruption among bureaucrats, government officials, and tax authority operations, as well as the fact that a sizable portion of the tax revenue ends up in the pockets of dishonest politicians, led to an increase in tax evasion. This result is consistent with Rashid's (2020) findings, which suggested that citizens are discouraged from obeying the law if their government discriminates against them because of their race, religion, politics, culture, or ethnicity. Due to the discrimination that prevents some taxpayers from receiving the same benefits from government services as others, they are dissuaded from paying their taxes on time, which in turn encourages tax evasion.

According to Table 4.14 above, the correlation between a taxpayer's negative attitude toward taxes and tax evasion was 0.825. This demonstrated that there is a very strong and favorable relationship—significant at the 1% level of significance—between tax evasion and negative

taxpayer attitudes in Addis Ababa's MSE taxpayers. Or simply the Addis Ababa SMEs taxpayers believed that the existence of an unfair, complicated, and unequal tax system, as well as the ineffectiveness of the tax administration, led to an increase in tax evasion. This result is consistent with those of Beza (2014), Aronmwan et al. (2015), and Paper et al. (2016), who suggested that tax evasion is acceptable in the eyes of the taxpayers if there existed unfairness, discrimination, complexity, and inefficient tax administration in a tax system. This, in turn, will cause the taxpayers to develop a negative attitude toward tax, which in turn increases tax evasion.

The study also used tax compliance costs as a variable. According to Table 4.14 above, the coefficient of correlation between tax compliance expenses and tax evasion is 0.807, indicating a very strong and positive correlation between the two. The relationship is significant at the 1% level of significance. This suggests that tax evasion in SMEs in Addis Ababa will be significantly reduced if the costs of tax compliance (i.e., cost of stationary, cost of tax consultant, cost of penalty for not paying tax, cost of cash register, cost of software & internet, and cost of hiring staff) were reduced in the process. This finding is consistent with those of Amina and Sniya (2015) and Aumeerun et al. (2016), who hypothesized that tax evasion, would rise if the cost of tax compliance also rose.

4.5.2. Multiple Regression Analysis

In order to determine the effect and strengths of the relationship between the independent variables of factors contributing to tax evasion (i.e., tax fairness, tax knowledge, tax penalties & enforcements, corruption, negative taxpayers' attitude towards tax, and tax compliance costs) and the dependent variable, which is tax evasion, multiple regression analysis was used in this study. By using the coefficient of determination, also known as R square, multiple regression analysis can explain or predict variations in a dependent variable as a result of the independent variables (Hair et al., 2010). The larger the coefficient of determination, the greater the influence of the independent variable have on the dependent variable. The researcher can compare the relative significance of each independent variable using the coefficients or beta weights for each variable. In this study, the multiple regression equations' unstandardized and standardized coefficients are provided. Discussions, however, are based on the unstandardized coefficients for each variable being studied.

4.5.2.1. Tests of Multiple Regressions Assumptions

The following presumptions were confirmed before running the regression model:

Adequate Sample Size and Independent Observation

According to a method presented by Tabachanick and Fidell (2007), N > 50 + 8 * m (where m = number of independent variables), the minimal sample size for multiple regression was determined as 50 + 8 * 6 = 50 + 48 = 98, with m = 6 because there were 6 independent variables. As a result, the sample size for regression analysis to test the hypotheses in this study was determined to be appropriate at 310 respondents. By obtaining sufficient variation in responses from multiple respondents, the researcher was able to demonstrate the independence of the observations.

Detecting Outliers

Due to the fact that multiple regression is very sensitive to outliers (extremely high or low scores or values), the researcher used Skewness and Kurtosis to look for extreme scores during the initial data screening stage. In terms of normalcy, the Skewness and Kurtosis of the nine constructs behave well. There are no outliers or extreme values that could compromise the validity of the analysis, as shown by the Skewness and Kurtosis values in Table 4.15 below, which are almost between 1 and +1.

Table 4.15: Skewness and Kurtosis Values of the Study Variables

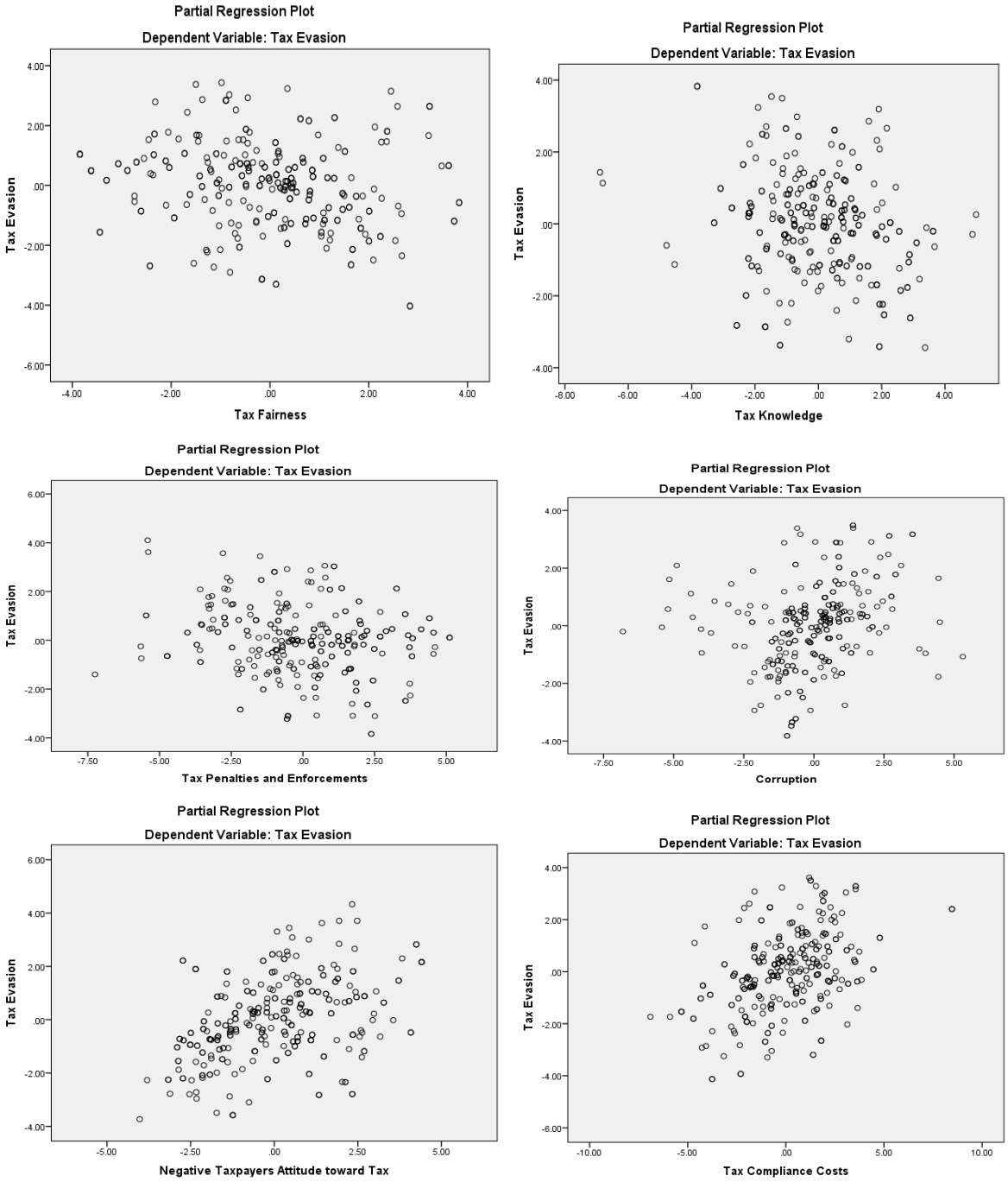
Study Variables	Skewness	Kurtosis
Tax Fairness	–0.062	–1.105
Tax Knowledge	–0.123	–1.044
Tax Penalties and Enforcements	–0.106	–1.132
Corruption	0.289	–0.127
Negative Taxpayers Attitude toward Tax	–0.153	–0.694
Tax Compliance Costs	–0.293	–0.430
Tax Evasion	–0.009	–0.502

Source: Survey Data Output (2023)

Test for Homoscedasticity

As can be seen in Figure 4.1 below, the scatterplot of the regression model's residuals exhibits no pattern and is randomly distributed, leading the researcher to assume that the residual variances are equal or that the variances in the data are homogeneous.

Figure 4.1: Regression Model Residuals Scatterplot Plot

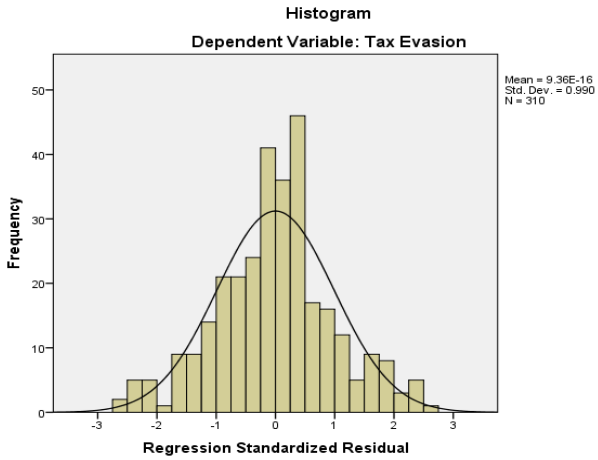


Source: Survey Data Output (2023)

The Normality Test

Since the mean value was roughly close to zero (0) or (mean = 9.36E-16) and the standard deviation value was roughly close to one (1) or (Std. Dev. = 0.990), the histogram in Figure 4.2 below indicated that the data were acceptable for normality.

Figure 4.2: Regression Model's Histogram

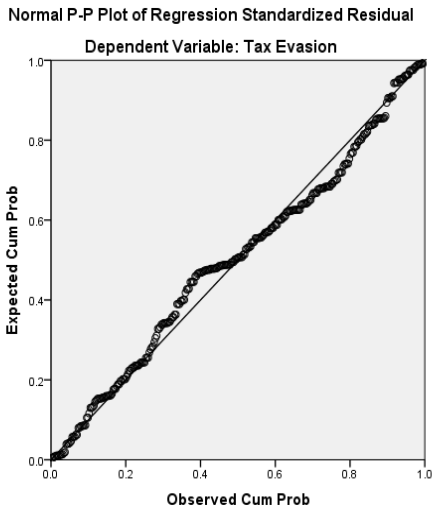


Source: Survey Data Output (2023)

Examining Linearity

When a regression is linear, the outcome variable, or the small circles in the typical Predicted Probability (P-P) plot close to the diagonal line, is related to the predictor variables in a straight line. The small circles in Figure 4.3's P-P plot showed that they were near or followed the diagonal or normal lines, demonstrating the linearity of the data.

Figure 4.3: The Regression Model's Normal P-P Plot



Source: Survey Data Output (2023)

Multicollinearity Test

When two or more independent or predictor variables in a regression model have a strong correlation, multicollinearity exists. Multicollinearity of the regression result for this study was tested using Pearson correlation matrix, for each of the regression model correlation between the predicators variables were below 0.90 as shown in Table 4.14 above. This is also supported by the statistics of collinearity test results Multicollinearity is indicated when Tolerance value is below 0.20 and VIF is more than 5 in a regression model. As shown in Table 4.16 below, Tolerance value ranges from 0.346 to 0.606 and VIF from 1.649 to 2.894 for all the predictor variables. Therefore, there is no reported problem of collinearity. Since all the five assumptions were not violated, the researcher examined the data collected by the schedule using multiple regression models as follows:

Table 4.16: Results of Multicollinearity Test

Variables	Tolerance	VIF
Tax Fairness	0.346	2.894
Tax Knowledge	0.383	2.612
Tax Penalties and Enforcements	0.579	1.728
Corruption	0.606	1.649
Negative Taxpayers' Attitude Towards Tax	0.356	2.809
Tax Compliance Costs	0.399	2.506

Source: Survey Data Output (2023)

Six predictors of multiple linear regression models were proposed in order to identify the most effective set of predictors of Tax Evasion (TE). Tax Fairness (X_1), Tax Knowledge (X_2), Tax Penalties & Enforcements (X_3), Corruption (X_4), Negative Taxpayers Attitude toward Tax (X_5), and Tax Compliance Costs (X_6) were the six predictor variables. The proposed multiple linear regression model's equation was as follows:

$$Y(TE) = \beta_0 + \beta_1(X_1) + \beta_2(X_2) + \beta_3(X_3) + \beta_4(X_4) + \beta_5(X_5) + \beta_6(X_6) + \varepsilon$$

Where: β_0 = Constant, ε = Error

R square is 0.839, which indicates that 83.9% of the dependent variable is explained by independent variables, according to Table 4.17 below. The adjusted R square is 0.835, which indicates that the model fits the data well because the value is higher than 0.60. Hair et al. (2010)

assert that a good fit model should be able to forecast at least 60% of the variation resulting from tax evasion (dependent variable). In light of this, the summary of the regression model showed that the coefficient of determination (R^2) was 0.839, indicating that all six of the independent variables—namely, tax fairness, tax knowledge, tax penalties & enforcements, corruption, negative taxpayers' attitude toward tax, and tax compliance costs—explained 83.9% of the variation in tax evasion (TE). As a result, other factors outside the scope of this model or study were responsible for the remaining 16.1% of the changes in the dependent variable (TE).

Table 4.17: Model Summary of the Regression Analysis

Model Summary[b]				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.916[a]	.839	.835	1.37096
a. Predictors: (Constant), Tax Compliance Costs, Tax Penalties and Enforcements, Corruption, Tax Knowledge, Negative Taxpayers Attitude toward Tax, Tax Fairness				
b. Dependent Variable: Tax Evasion				

Source: Survey Data Output (2023)

The F-statistics and probability (F-statistics) for the regression are displayed in Table 4.18 below, which is the ANOVA result. At a 1% level of significance, the F-statistic's null hypothesis—which states that the Adjusted R-squared is equal to zero—was rejected. Strong statistical significance is shown by the F-value of 0.000, which improved the model's validity and reliability. Indicating that there is a linear relationship between all six predictor variables (i.e., tax fairness, tax knowledge, tax penalties & enforcements, corruption, negative taxpayers' attitude towards tax and tax compliance costs) and Tax Evasion (TE), the estimated linear regression model line's slope is not equal to zero. This shows that Tax Evasion (TE) is significantly predicted by the eight predictor variables.

Table 4.18: Results of the Analysis of Variance (ANOVA)

ANOVA[a]						
Model		**Sum of Squares**	**df**	**Mean Square**	**F**	**Sig.**
1	Regression	2957.582	6	492.930	262.261	.000[b]
	Residual	569.502	303	1.880		
	Total	3527.084	309			
a. Dependent Variable: Tax Evasion (TE)						
b. Predictors: (Constant), TCC, TPE, CR, TAW, TAT, TF						

Source: Survey Data Output (2023)

The multiple regression model coefficient results of the factors that contributed to tax evasion in Table 4.19 below showed that the estimated unstandardized beta coefficients of β_0 (constant) was 26.355; β_1 (Tax Fairness) was –0.156; β_2 (Tax Knowledge) was –0.178, β_3 (Tax Penalties & Enforcements) was –0.106, β_4 (Corruption) was 0.242, β_5 (Negative Taxpayers' Attitude towards Tax) was 0.342 and β_6 (Tax Compliance Costs) was 0.378. Hence the estimated model was:

$$Y(TE) = 10.895 – 0.156X_1 – 0.178X_2 – 0.106X_3 + .242X_4 + 0.342X_5 + 0.281X_6$$

The regression model's unstandardized beta coefficients ($\beta_5 = 0.342$, $t = 7.770$, $p < 0.05$) showed that negative taxpayers' attitude toward tax has the most detrimental and significant impact on tax evasion. Accordingly, tax evasion will incline by 0.342 when negative taxpayers' attitude toward tax increases by one point. This suggests that in order to decrease tax evasion, tax collectors in Addis Ababa should focus more on changing the negative taxpayers' attitude toward tax in SMEs. Tax compliance costs came in second with the second highest positive and significant value to have an impact on tax evasion ($\beta_6 = 0.281$, $t = 7.969$, $p < 0.05$). This indicates that for every unit increase in the cost of tax compliance, there was a 0.281 unit increase in tax evasion.

The unstandardized beta coefficients value for corruption was the third-highest positive and significant value to have an impact on tax evasion ($\beta_4 = 0.242$, $t = 5.033$, $p < 0.05$). This suggests that for every unit increase in corruption, there was a corresponding increase in tax evasion of 0.242 units. The unstandardized beta coefficients value for tax knowledge was the fourth highest negative and significant value to have an impact on tax evasion ($\beta_2 = –0.178$, $t = –3.888$, $p <$

0.05). This suggests that for every unit increase in tax literacy, there was a 0.242 unit drop in tax evasion.

Table 4.19: Analysis of the Regression Model Coefficients

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	10.895	1.414		7.705	.000
	TF	-.156	.050	-.124	-3.154	.002
	TK	-.178	.046	-.145	-3.888	.000
	TPE	-.106	.035	-.092	-3.046	.003
	CR	.242	.048	.149	5.033	.000
	TAT	.342	.044	.301	7.770	.000
	TCC	.281	.035	.291	7.969	.000
a. Dependent Variable: Tax Evasion (TE)						
TF = Tax Fairness, TK = Tax Knowledge, TPE = Tax Penalties & Enforcements, CR = Corruption, TAT = Negative Taxpayers Attitude toward Tax, TCC = Tax Compliance Costs						

Source: Survey Data Output (2023)

The unstandardized beta coefficients value for tax fairness was the fifth highest negative and significant value to have an impact on tax evasion ($\beta_1 = –0.156$, $t = –3.154$, $p < 0.05$). This suggests that for every unit increase in tax equity, there is a 0.156 unit drop in tax evasion. Last but not least, tax penalties and enforcements had the least significant negative impact on tax evasion ($\beta_3 = –0.106$, $t = –3.046$, $p < 0.05$). This showed that a 0.106 unit decrease in tax evasion followed a one unit increase in tax penalties and enforcements.

4.6. Hypothesis Test Results

The six hypotheses of this study regarding factors that may lead to tax evasion in SMEs of the Addis Ababa City Administration were tested using multiple linear regression models and the Pearson correlation model, as shown in the regression tables above. The results were based on the beta and correlation coefficient with a 95% confidence level and p-value to test whether the hypothesis is accepted or rejected.

Hypothesis - 1

H_{a1}: Tax fairness has a negative and significant influence on tax evasion.

The unstandardized beta coefficient with ($\beta_1 = -0.156$, $t = -3.154$, $p < 0.05$) indicated that tax fairness has a negative and significant effect on tax evasion. The regression analysis as shown in Table 4.19 above supports this finding. In other words, a 0.156 unit decrease in tax evasion follows a one unit increase in tax fairness. As a result, the findings do not support the null hypothesis, and the researcher is compelled to accept hypothesis one, which postulates that tax fairness has a negative and significant impact on tax evasion in SMEs of the Addis Ababa City Administration. The findings of this study are consistent with those of Manaye et al.'s (2020) research, which suggests that if the government wants to lessen the scope of tax evasion, it should implement fair tax policies.

Hypothesis – 2

H_{a2}: Tax knowledge has a negative and significant influence on tax evasion.

The unstandardized beta coefficient with ($\beta_2 = -0.178$, $t = -3.888$, $p < 0.05$) demonstrated that tax knowledge has a detrimental and significant effect on tax evasion is confirmed by the regression analysis as shown in Table 4.19 above. Accordingly, a 0.178-unit decrease in tax evasion occurs for every one unit increase in tax awareness. As a result, the findings do not support the null hypothesis, and the researcher is compelled to accept alternative hypothesis number two, which postulates that tax knowledge has a detrimental and significant impact on tax evasion in SMEs under the control of the Addis Ababa City Administration. This result is also in line with a previous study by Assfaw and Sebhat (2019), who discovered that people who are more aware of and knowledgeable about taxes are less likely to engage in tax evasion.

Hypothesis – 3

H_{a3}: Tax penalties and enforcement negatively and significantly influences tax evasion.

The unstandardized beta coefficient with ($\beta_3 = -0.106$, $t = -3.046$, $p < 0.05$) indicated that tax penalties and enforcement has a negative and significant effect on tax evasion. The regression analysis as shown in Table 4.19 above supports this finding. This implies that for every unit increase in tax fines and enforcement, there is a corresponding decrease in tax evasion of 0.106 units. As a result, the results do not support the null hypothesis, forcing the researcher to accept alternative hypothesis number three, which postulates that tax penalties and enforcement have a

negative and significant impact on tax evasion in SMEs of the Addis Ababa City Administration. Demle's (2019) conclusion is consistent with the findings of this study, which found that the likelihood of tax evasion decreased with increased tax penalties and enforcements in a nation.

Hypothesis – 4

H_{a4}: Corruption has a positive and significant effect on tax evasion.

The unstandardized beta coefficient with (β_4 = 0.242, t = 5.033, p < 0.05) indicated that corruption has a positive and significant effect on tax evasion. The regression analysis as shown in Table 4.19 above supports this finding. This implies that for every unit increase in corruption, tax evasion increases by 0.242 units. As a result, the results do not support the null hypothesis, forcing the researcher to accept alternative hypothesis number four, which postulates that corruption has a favorable and significant impact on tax evasion in SMEs of the Addis Ababa City Administration. This finding is consistent with Rashid's (2020) findings, which suggested that tax evasion will rise if tax collection corruption also rises. Rashid (2020) also suggested that if the government discriminates against citizens because of their religion, race, politics, culture, or ethnicity, they will be less likely to abide by the law, which will raise tax evasion.

Hypothesis – 5

H_{a5}: Negative attitude of tax payers towards tax has a positive and significant effect on tax evasion.

The unstandardized beta coefficient with (β_5 = 0.342, t = 7.770, p < 0.05) indicated that tax payers' negative attitudes toward taxes have a positive and significant impact on tax evasion. The regression analysis displayed in Table 4.19 above supports this finding. This indicates that for every one unit increase in taxpayers' negative attitudes toward taxes, there is a 0.342 unit increase in tax evasion. As a result, the results do not support the null hypothesis, and the researcher is compelled to accept alternative hypothesis number five, which postulates that a tax payer's negative attitude has a positive and significant impact on tax evasion in SMEs of the Addis Ababa City Administration. This result is consistent with those of Beza (2014), Aronmwan et al. (2015), and Paper et al. (2016), who suggested that tax evasion is acceptable in the eyes of the taxpayers if there existed unfairness, discrimination, complexity, and inefficient tax administration in a tax system. This result suggests that if there existed these factors, the taxpayers would develop a negative attitude toward tax, which would increase tax evasion.

Hypothesis – 6

H_{a6}: Tax compliance cost has a positive and significant influence on tax evasion.

The unstandardized beta coefficient with ($\beta_6 = 0.281$, $t = 7.969$, $p < 0.05$) indicated that tax compliance costs have a positive and significant effect on tax evasion. The regression analysis as shown in Table 4.19 above supports this finding. This implies that for every unit increase in the cost of tax compliance, there is a 0.281 unit increase in tax evasion. As a result, the findings do not support the null hypothesis, and the researcher is compelled to accept alternative hypothesis number six, which postulates that tax compliance costs have a favorable and significant impact on tax evasion in SMEs of the Addis Ababa City Administration. This result is consistent with those of Amina and Sniya (2015) and Aumeerun et al. (2016), who hypothesized that tax evasion, would rise if the cost of tax compliance also rose. This suggests that tax evasion will significantly increase in Addis Ababa's SMEs if the cost of tax compliance (i.e., stationary, tax consultant, penalty for not paying tax, cost of cash register, cost of software & internet, and cost of hiring staff) increases.

Table 4.20 below illustrate that the summary result of hypothesis testing, hypothesis of H_{a1}, H_{a2}, H_{a3}, H_{a4}, H_{a5}, and H_{a6} are accepted, that means tax fairness, tax knowledge, tax penalties & enforcements, corruption, negative taxpayers' attitude towards tax and tax compliance costs are found to be significant contributing factors of tax evasion at 5% significance level.

Table 4.20: Summary of the Hypothesis Test Results

Hypothesis	P-value	Expected Relationship	Result	Decision Accept/Reject
H_{a1}: Tax fairness has a negative and significant influence on tax evasion.	0.002	Negative	Negative	Accept
H_{a2}: Tax awareness has a negative and significant influence on tax evasion.	0.000	Negative	Negative	Accept
H_{a3}: Tax penalties and enforcement negatively and significantly influences tax evasion.	0.003	Negative	Negative	Accept
H_{a4}: Corruption has a positive and significant effect on tax evasion	0.000	Positive	Positive	Accept
H_{a5}: Negative attitude of tax payers towards tax has a positive and significant effect on tax evasion.	0.000	Positive	Positive	Accept
H_{a6}: Tax compliance costs have a positive and significant influence on tax evasion.	0.000	Positive	Positive	Accept

Survey: Data Output (2023)

CHAPTER FIVE

5. CONCLUSIONS AND RECOMMENDATIONS

5.1. Conclusions

Finding the causes of tax evasion in SMEs under Addis Ababa City Administration was the study's main goal. This study examined six potential causes of tax evasion, including tax fairness, tax knowledge, tax penalties & enforcement, corruption, unfavorable attitudes toward taxes among taxpayers, and the cost of tax compliance.

The following conclusions about tax evasion are drawn from the qualitative data obtained through interviewing and the researcher's triangulation. The tax being imposed isn't fair and equitable, say the tax officials who were interviewed, because it occasionally depends on estimates of the average daily revenue. The tax officials who were interviewed stated that maintaining accounting records is expensive for SMEs because it requires them to hire accountants, rent offices, and buy computers, stationery, and software, among other expenses. As a result, the tax compliance costs for SMEs are high. Additionally, there are discrepancies between the number of SMEs paying taxes and the number of auditors working for the tax authority or ERCA, which reduces the likelihood that an audit will catch the problem. It consequently weakens one's desire to voluntarily comply and raises tax evasion. According to both the quantitative and qualitative findings, tax awareness is a crucial component of improved voluntary compliance and lowers tax evasion. The respondents who were questioned also mentioned that there will be less tax evasion if the rate of fines and penalties is high.

According to the tax officials who were interviewed, the tax authority's inefficiencies allowed SMEs taxpayers to evade taxes by not declaring and underreporting income, overstating business expenses and deductions, underreporting and over reporting trading stock, and deducting personal expenses as business expenses to conceal the precise tax liability. Because they believed that a significant amount of the tax revenue was used inefficiently and allocated to unworthy projects that did not benefit the taxpayers, this demonstrated that the SMEs taxpayers had grown to have a negative attitude toward taxes.

The ERCA tax officials who were interviewed concluded that in order to reduce the tax evasion of SMEs, ERCA should establish new branches close to the taxpayers, improve internet

connections, streamline tax filing and collection procedures by implementing e-filing and e-payment systems, improve relationships and build trust with the taxpayers by communicating the tax programs with them, and raise awareness through regular training and education on tax laws.

All of the explanatory variables (i.e., tax fairness, tax knowledge, tax penalties & enforcements, corruption, negative taxpayers' attitude towards tax and tax compliance costs) have a statistically significant impact on tax evasion, according to the multiple regression analysis of the dependent and independent variables.

Tax evasion is negatively and significantly impacted by tax fairness. This conclusion can be justified by the idea that fair taxation will lower tax evasion. Taxpayers will be discouraged from engaging in tax evasion by an equitable distribution of tax justice. The findings of this study also indicated that if the government wants to lessen the scope of tax evasion, it should implement fair tax policies. The researcher came to the conclusion that it would be simple to prevent tax evasion in Addis Ababa's SMEs with better tax fairness.

Due to its detrimental effects on taxpayers' attitudes toward tax evasion, tax knowledge is also essential for reducing tax evasion. This result indicated that people who are more aware of and knowledgeable about taxes are less likely to engage in tax evasion. Nearly all types of respondents agreed that people's awareness and knowledge of tax payment procedures, tax calculation systems, and the sources of income they should declare, and the current penalties for intentional tax evasion lead to a reduction in tax evasion. Therefore, researcher concluded that the government must take the necessary steps to increase tax awareness and knowledge among Addis Ababa's SMEs taxpayers.

Tax enforcement and penalties have a detrimental and significant impact on tax evasion. The results demonstrate that having a high rate of tax fines and enforcements will reduce tax evasion. Additionally, the researcher concludes that tax evasion is less likely in countries with higher levels of tax penalties and enforcement.

Tax evasion is positively and significantly impacted by corruption. The results demonstrate that the presence of corruption in tax authority operations, corruption among bureaucrats and government officials, discrimination, and the possibility that a sizable portion of tax revenue ends up in the pockets of dishonest politicians will discourage taxpayers from paying taxes on time, which will increase tax evasion. The researcher concluded that discrimination deprives

taxpayers of equal access to government services provided to others and, as a result, deters taxpayers from paying taxes on time. As a result, the government should provide all facilities equally to all of the nation's citizens, regardless of their race, religion, or cultural background.

Taxpayer attitudes that are unfavorable to taxes have a positive and significant impact on tax evasion. The results demonstrate that the presence of unfairness, discrimination, complexity, and ineffective tax administration in a tax system led to the development of a negative attitude among taxpayers toward taxes, which in turn increases tax evasion. This result showed that tax evasion is acceptable in the eyes of the taxpayers if there existed unfairness, discrimination, complexity, and inefficient tax administration in a tax system. This result suggests that if there existed these factors, the taxpayers would develop a negative attitude toward tax, which would increase tax evasion.

Tax compliance costs have a positive and notable impact on tax evasion. These results demonstrate that taxpayers feel burdened by the need to pay other expenses in addition to taxes, and that this burden may lead some taxpayers to engage in tax evasion. This result indicated that tax evasion, would rise if the cost of tax compliance also rose. The researcher came to the conclusion that tax evasion will significantly increase in SMEs in Addis Ababa if tax compliance costs (i.e., cost of stationary, cost of tax consultant, cost of penalty for not paying tax, cost of cash register, cost of software & internet, and cost of hiring staff) were increased.

Out of the six predictor variables used in this study, taxpayers' negative attitudes toward taxes has the largest positive and significant impact on tax evasion, followed by tax compliance costs and corruption, which have a positive and significant impact on tax evasion as well. The remaining predictor variables, which are tax knowledge, tax fairness, and tax penalties and enforcements, are positioned from three of six and have a negative and significant impact on tax evasion, respectively. In addition to the six predictor variables, 83.9% of tax evasion in Addis Ababa SMEs was explained. Therefore, other factors outside the scope of this study were responsible for the remaining 16.1% of changes in the dependent variable (tax evasion).

5.2. Recommendations

The researcher developed a number of recommendations to deter tax evasion among SMEs based on the study's findings. These include:

- Timely and necessary tax training about tax rates and tax systems should be given by using different Medias such as TV, Radio, different publications, Magazines, and training activities by ERCA. Tax proclamation, guidelines, and any changes therein should be available to SMEs business profit taxpayers. So that it will raise taxpayer awareness, close loopholes for tax evasion issues, and raise timely payment of the tax by SMEs business profit taxpayers.
- In order to monitor informal suppliers who transact without using legal receipts and to include all SMEs businesses in the tax system, ERCA should strengthen the tax enforcement team. This is because the presence of people who do not pay taxes has a negative impact on how taxpayers view paying taxes. To ensure uniform application of tax laws and procedures and to ensure a fair tax system for businesses of a similar size, the frequency and scope of supervision should be expanded.
- In order to reduce the costs associated with tax compliance, they should also make sure that the tax system is clear and straightforward to encourage tax payers to complete tax returns and calculate their own tax liability rather than seeking the assistance of tax agents or other bodies, the tax authorities should simplify the tax returns and tax forms, tax calculation, and payment deadlines.
- The tax return, system, and forms should be less complicated, and the tax processes themselves should be simple to follow. Additionally, tax payers should be given the opportunity to understand the tax rules and regulations in their native tongue. SME business taxpayers should be consulted, particularly when changing the tax law (system).
- According to the study's findings, most SMEs taxpayers in Addis Ababa, Ethiopia, have negative attitudes toward taxes because they don't believe in an equitable tax system. By modifying the negative attitude that has been developed by taxpayers toward taxes, this factor can be used to reduce tax evasion of SMEs. Therefore, in order to improve tax compliance and lower tax evasion, the government should use taxpayer money wisely, transparently, and in communication with the public about tax programs.

- Only with the voluntarily participation of society can tax evasion be avoided or reduced. Stick-only tactics don't produce any lasting results. Therefore, the taxing authority must do everything in its power to encourage taxpayers to voluntarily settle their tax debts.
- The tax authority needs to do its part to raise awareness. Not only should laws and penalties be understood, but also the needs and justifications for taxes. Taxpayers also have a right to the most recent information regarding how the tax system works, how their taxes are assessed, and what their tax rate is. The complexity of the situation should be reflected in every piece of information provided to taxpayers, allowing them to better understand their tax affairs. The authorities may carry out this duty in a number of ways.

5.3. Direction for Further Research

There will inevitably be some limitations in every study. As a result, the current study has some limitations. It initially only addressed the elements influencing tax avoidance in SMEs under Addis Ababa City Administration. Therefore, it may be difficult to generalize this finding about all SMEs taxpayers found in other regions of Ethiopia or at the national level. However, the findings of this study can be generalized for SMEs taxpayers found in Addis Ababa City Administration. In order to produce insightful and inclusive papers by comparing factors contributing to tax evasion of taxpayers in various business sectors, future researchers should concentrate on other taxpayer categories and cover wider geographical areas. Since this study only looked at eight factors, future research can also take into account additional factors that contribute to tax evasion but were not covered in this study. Additionally, cross-sectional data, which is thought to be static rather than dynamic in nature, was used in the data analysis for this study. In order to provide a better understanding of the factors contributing to tax evasion over time, future researchers may want to consider conducting longitudinal studies.

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APPENDIX

Appendices 1: Research Questionnaires

Addis Ababa University

College of Business and Economics

Department of Accounting and Finance

Dear respondent,

As part of his degree requirements, **Biruk Tesfaye** a master's student in accounting and finance at Addis Ababa University, will conduct this research. Working on a study titled "Factors Contributing to Tax Evasion: The Case of Small and Medium Enterprises in Addis Ababa City Administration" at the moment.

I want to congratulate you for being one of the most qualified and reliable survey respondents selected. In order to provide a fair assessment of the current state of Factors Contributing to Tax Evasion: The Case of Small and Medium Enterprises in Addis Ababa City Administration, kindly assist me in providing accurate and comprehensive information. Your participation in the survey is entirely voluntary and anonymous.

Last but not least, I want to reassure you that any information you share with me will be kept confidential and used only for academic research. The identities of respondents will not be disclosed or published, and individual comments won't be identified.

Regards, Sincerely,

Biruk Tesfaye

Instructions

1. You don't have to write your name down.
2. For statements that use a five-point Likert scale, indicate your answers by placing a checkmark (√) in the appropriate block.
3. For multiple choice questions indicate your answers by encircling the letter of your choice.

Note: Please feel free to contact the researcher at the following addresses if you have any further questions, comments, or suggestions:

Name: Biruk Tesfaye

Mobile: 0911 24 58 00

E-mail: btesfaye927@gmail.com

I sincerely appreciate your time and valuable cooperation in advance.

Part I: Backgrounds of the Respondents and Their Business

Instructions: Please encircle the letter of your choice.

1. Gender
    a. Male
    b. Female
2. Age
    a. 20 – 30 years
    b. 31 – 40 years
    c. 41 – 50 years
    d. Above 50 years

3. Marital status
    a. Single
    b. Married
    c. Divorced
    d. Widowed
4. Educational Qualification
    a. Primary School
    b. Secondary School
    c. Diploma
    d. First Degree
    e. Master's Degree and above
5. SMEs Sectors of business activities
    a. Trade
    b. Service
    c. Urban Agriculture
    d. Manufacturing
    e. Construction
6. Forms of Business Ownership
    a. Sole Proprietorships
    b. Partnership
    c. Private Limited Companies (PLC)
    d. Other Associations

7. Tax Experience of SMEs

   a. Below 5 years
   b. 5 to 10 years
   c. More than 10 years

Part II: Factors Contributing to Tax Evasion

According to the Addis Ababa City Administration, the following are the main causes of tax evasion in SMEs. Please indicate how much your organization is impacted by the factors contributing to tax evasion. After reading each of the Factors Contributing to Tax Evasion, assess them in relevance to your organization, and then mark the options with a check mark (√). Whereas 1 indicates Strongly Agree, 2 indicate Neutral, 3 indicates Agree, 5 indicate Strongly Agree, and 4 indicate Agree.

Overall Factors Contributing to Tax Evasion

Code	Tax Fairness	1	2	3	4	5
TF1	There is no existence of corruption practice in the tax system					
TF2	The tax collection procedures and principles are fair or there is no discriminatory tax assessment					
TF3	There is no inconsistency in tax burden or the tax assessment is not based on arbitrary decisions					
TF4	There is no ambiguity of tax regulations that leads to misinterpretation of tax regulations					
TF5	A large portion of the money collected is spent on projects that does benefit me					
Code	**Tax Knowledge**	**1**	**2**	**3**	**4**	**5**
TK1	I know well which sources of income I must declare					
TK2	Tax is paid in anticipation of public services					
TK3	I know about criminal penalties for intentional tax evasion					
TK4	I am well informed about tax and tax evasion					
TK5	The tax authorities provided me different training about tax evasion and other tax-related issues					
Code	**Tax Audit**	**1**	**2**	**3**	**4**	**5**
TA1	The probability of getting caught by tax audit is high.					
TA2	The MSEs have no chance to evade their taxes or filing taxes less than actual obligation due to tax audit by tax authorities.					
TA3	The audit departments of the government inspect or audit whether the taxpayers are complying with tax laws regularly.					

TA4	The tax authority will find out if MSEs do not file taxes documents.					
Code	**Tax Penalties and Enforcements**	**1**	**2**	**3**	**4**	**5**
TPE1	Fines and penalties are imposed on the MSEs who evade tax.					
TPE2	Currents penalties are enough to make MSEs obey tax laws.					
TPE3	The anti-corruption commission is capable of taking action against tax evaders.					
TPE4	The tax authority will punish MSEs who do not file taxes.					
TPE5	The tax laws are enforced on those MSEs that are not submitting the income tax return.					
Code	**Tax Authority's Efficiency**	**1**	**2**	**3**	**4**	**5**
TAE1	The tax authority employees are skilled and professional.					
TAE2	The tax authority employees are knowledgeable and willing to help.					
TAE3	The tax collectors do not harass the taxpayers.					
TAE4	The tax administration has put a sound and efficient tax system in place.					
Code	**Corruption**	**1**	**2**	**3**	**4**	**5**
CR1	There is too much corruption in the tax authority operations.					
CR2	A significant portion of the money collected from taxes winds up in the pocket of corrupt politicians or their families and friends.					
CR3	There is a high level of corruption among bureaucrats and government officials.					
CR4	The tax authority discriminates against people because of their religion, race, or ethnic background.					
Code	**Negative Taxpayers Attitude toward Tax**	**1**	**2**	**3**	**4**	**5**
TAT1	The tax system is unequal and unfair.					
TAT2	The tax administration is inefficient to find out SMEs who declare their income inaccurately and thereby punish tax evaders.					
TAT3	Tax evasion is not considered a serious offense.					
TAT4	The overall tax system is too complex to understand.					
TAT5	Tax evasion is ethical because social justice is not established all over the country.					
Code	**Tax Compliance Costs**	**1**	**2**	**3**	**4**	**5**
TCC1	The penalty due to not paying tax is lower than my tax saving					
TCC2	Cost of stationaries, computer, etc. is high					
TCC3	Cost of cash register machine and its operation is high					
TCC4	Cost of software and internet is high					
TCC5	Cost of hiring staff such as accountant and sales man is high					
TCC6	Most of the time I hire external services (tax consultant) to file tax returns and I pay additional costs.					

Part III: Tax Evasion Dimensions

The following is a description of the extent of tax evasion in Addis Ababa City Administration SMEs. Please explain how these problems affect your organization's tax payment procedure. After reading each of these factors, evaluate them in light of your organization, and then check the appropriate boxes (√) next to the choices. Whereas 1 indicates Strongly Agree, 2 indicate Neutral, 3 indicates Agree, 5 indicate Strongly Agree, and 4 indicate Agree.

Tax Evasion Dimensions

Code	Tax Evasion	1	2	3	4	5
TE1	High rates of income tax are one of the reasons for tax evasion					
TE2	Low rates of penalties are responsible for causing tax evasion					
TE3	A low probability of detection may be the cause of tax evasion					
TE4	The weakness of the audit system is responsible for allowing tax evasion					
TE5	The unfairness of the tax system is the causes of tax evasion.					
TE6	The inefficiencies of the tax authorities are the causes of tax evasion.					
TE7	Majority of the MSEs taxpayers do not report all of their income to the authority.					
TE8	Tax evasion is ethical if a large portion of the money collected by the public authorities is wasted.					
TE9	Tax evasion is less considered as serious crime among the society or MSEs.					
TE10	The complexity in the tax system is the reason for tax evasion.					

Thank you once again!!

Appendices 2: Interview Questions for the Tax Collectors

Addis Ababa University

College of Business and Economics

Department of Accounting and Finance

The following list of interview questions has been prepared to evaluate operational officials' evaluations and observations of tax evasion cases involving SMEs in Addis Ababa City Administration's sub-cities small and medium tax payer's revenue and customs branch office:

1. How do you describe/evaluate the factors contributing to tax evasion opportunities in the SMEs in your sub-cities and tax office?
2. How do you describe the tax fairness of the tax system for SMEs and your office as a whole?
3. How do you evaluate the tax knowledge of the taxpayers and the tax office?
4. How do you evaluate the tax audit performance of your office in minimizing tax evasion of the taxpayers?
5. What look like the tax penalties and enforcements levels of your office towards SMEs tax evaders in your sub-city?
6. How do you evaluate your offices efficiency in fighting tax evasion of SMEs in your sub-city?
7. How do you evaluate the negative tax payers' attitude towards tax in SMEs found in your sub-city?
8. How do you describe the tax compliance cost of the taxpayers and also the tax office workers?
9. What suggestion do you have to alleviate tax evasion in the city SMEs or better yet in the country as a whole?