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ADDIS ABABA UNIVERSITY
COLLEGE OF LAW AND GOVERNANCE
SCHOOL OF LAW
LL.M PROGRAM IN BUSINESS LAW

Issues and Problems Associated with Value Added Registration:
Practice Oriented Analysis

By: Tesfaye Yezengaw Demisse

Advisor: Aschalew Ashagre (Assistant Professor of Law)

April, 2017

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A Thesis Submitted to the College of Law and Governance Studies, School of Law, Addis Ababa University in Partial Fulfillment of the Requirements of Masters Degree of Laws (LL.M) in Business Law

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Declaration

I, the undersigned, declare that this thesis is my original work, and has not been presented for a degree in any other university, and that all sources of materials used or the thesis have been fully acknowledged.

Tesfaye Yezengaw Demisse _____

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Acknowledgement

First and foremost, I thank the Almighty God for all things he made! My advisor Assistant Professor Aschalew Ashagre is next in line of my appreciation for his limitless assistance by reading and critically commenting up on the thesis. Without whose guidance and encouragement, I might not have been able to manage the thesis in its present form.

I express my gratefulness to all those who provide me with necessary information in writing the thesis by giving interview sacrificing precious time.

My heartfelt thanks go to my wife Frehiwot Bermeta since without her love and support this program might not be completed. I also express my sincere gratefulness to the rest of my family and all of my classmates for their encouragement.

To my Grandmother Tenagne Tesema

Acronyms

Art-Article

CCE-Commercial Code of Ethiopia

ECJ- European Court of Justice

EEC- European Economic Commission

ERCA-Ethiopia Revenues and Customs Authority

EU-European Union

FDRE-Federal Democratic Republic of Ethiopia

FTAP-Federal Tax Administration Proclamation

GC-Gregorian Calendar

IMF- International Monetary Fund

FITP- Federal Income Tax Proclamation

MoFEC-Ministry of Finance and Economic Cooperation

MOT-Ministry of Trade

OECD- Organization for Economic Cooperation and Development

UK -United Kingdom

VATP-Value Added Tax Proclamation

VATRD-Value Added Tax Registration Directive

VATR-Value Added Tax Regulation

VAT-Value Added Tax

WTO-World Trade Organization

Abstract

The administration of Value Added Tax (VAT) necessitates identification of taxable persons. Countries execute this duty through a method of registration. Any country which has accepted the VAT system should put in place institutional and legal frameworks which are instruments for the registration of taxable persons. In addition to organizing such institutional and legal frameworks, countries should also establish systems which ensure the proper implementation of such laws by the concerned governmental bodies. Moreover, they should have also a system which evaluates the performance of the institutions and revising laws dealing with VAT registration.

Ethiopia introduced the VAT system by enacting proclamation No 285/2002 in 2002. This proclamation has incorporated provisions which regulate the registration process of taxable persons and other administrative aspects of VAT. Like the laws of other countries, it has also put in place institutions which carry out the registration process. Moreover it has empowered the Ministry of Finance and Economic Cooperation (MoFEC) and the Ethiopian Revenues and Customs Authority (ERCA) to make directives pertaining to VAT registration when the need arises.

The primary objective of this research was to scrutinize the practical implementation of the VAT law provisions dealing with VAT registration and cancelation and examining practical problems associated with registration. In addition, it tried to look into treatment of grievances related to registration and cancellation. Furthermore attempt was made to evaluate the directive making process of (MoFEC) and (ERCA) whether it adheres to the principle of legality or not. In the process of doing this research, the researcher realized the existence of many practical and legal gaps related to VAT registration. Besides the existence of such practical and legal gaps, the writer of this paper has identified that the approach followed by ERCA in the process of registering the taxable person is against the principle of legality. The research work concludes that the existing legal and practical gaps are critical which can militate against the tax policy of Ethiopia in general and the rationale behind VAT registration in particular. So, the researcher strictly recommends that the reexamination of the law and the institutional frame work of Ethiopia is very much necessary.

Chapter One

1. Introduction

1.1. Background of the Research

It is a worldwide truth that any nation needs to secure certain revenue to cover the funds needed to accomplish the various functions of the government. The most important means of obtaining such revenue is taxation. From the various types of taxation, the modern world is nowadays giving a significant attention to consumption type taxes, particularly for Value Added Tax (VAT), other than the more traditional income based tax systems. This is because of the relative importance of consumption based taxes in terms of their many advantages including the widening of the tax base and lessening of the compliance cost needed to collect the tax.

Ethiopia, aware of these advantages, joined the list of countries employing the VAT in the year 2002. However, it is difficult to assert that Ethiopia is gaining the full advantages that VAT offers. Currently, there is an apparent problem and dispute in the process of identifying taxable persons. Some voices are heard complaining about the system of registration for VAT as not being neutral because of the irregular manner of determination of taxable persons and activities. One of these is the issue raised regarding the estimation of the annual turnover of their businesses in relation to the threshold for VAT registration. There are also many other issues after registration such as cancellation and grievance handling related to both registration and cancellation. For this reason, there is a need to examine whether there is a proper framework of registration of taxable persons for VAT in general and other related issues in particular as this is the only gateway for the VAT system and its associated advantages.

This research is, therefore, an attempt to identify the basic issues and problems of the type illustrated above and exploring whether the Ethiopian VAT registration system is comprehensive enough to give solutions to the identified problems and suggesting relevant solutions in the areas where the law has failed to do so.

1.2. Statement of the Problem

It has been more than a decade since Ethiopia introduced the VAT in its tax system. However, from its inception it is heard that as the existence of some problems VAT has met. Some problems are related to its understanding and proper enforcement. Since VAT is a tax that is related with registration as a taxpayer, the major issues and problems of the system as a whole begin in connection with registration.

The process of registration for VAT involves many things. One is identification of taxable persons in the sense that only persons deemed taxable are to be included in the scope of VAT. This in itself involves identifying those activities which are deemed taxable or not which in turn help us in identification of who is a taxable person. However, the practice is witnessing that there is some problem related with the distinction between taxable activities and exemptions. One illustration in this regard is the issue of most religious institutions not being registered for VAT while performing taxable activities. This may create discrimination among different taxable persons which in turn may defeat the principle of fair competition among business persons.

The other issue is that of determination of the appropriate threshold for registration since it is difficult to include every business person in the reach of VAT. Here, there is a question in the minds of many people whether the 500,000 (Five Hundred Thousand) Birr threshold fixed some 14 years ago is still appropriate given the continual inflation existing in the country. Even after fixing a certain amount deemed as a proper threshold, there is still a difficulty in determining whether a certain business person has really reached the required threshold by the law. This involves estimating the annual turnover of a taxpayer. There not being a uniform standard for estimating the annual turnover of business persons in Ethiopia and the lack of the appropriate knowledge, skill and capacity among the officers? Tax authority is the major problem in this regard.

After this entire step is passed and a business person is registered as a taxpayer, the need to leave the VAT system may arise for different reasons. This is where the issues relating to cancellation surface. Although there are different grounds for cancellation of VAT registration provided in the law, their practical implementation is seen to be limited only to full exit from the business by the business person.

Finally, as any transaction is exposed to disputes, the process of registration for VAT and its cancellation are involved numerous disputes. Consequently, although there is a need to provide for a mechanism for quickly settling these disputes, the Ethiopian VAT system has not provided any dispute resolution mechanism related to the issue at hand. This may lead to an unnecessary loss of resources from both the sides of taxpayers and the tax authority ultimately hurting the country's economy.

1.3. Research Questions

Based on the above stated problems, this research attempts to answer the following research questions:

- Are the requirements for VAT registration provided by the relevant laws practically being implemented?
- Is the tax authority currently clearly identifying those taxable activities used for determining taxable persons?
- Is the mechanism used by the tax authority to determine whether the annual turnover of business persons has reached the required threshold by the law neutral or discriminatory?
- Is the threshold for VAT registration fixed by the legislator during introduction of the VAT still appropriate in the face of the current inflation in Ethiopia?
- Are the grounds of cancelation for VAT registration compatible with the requirements of VAT registration itself?
- Is there a grievance handling mechanism regarding both registration and cancellation of VAT?

1.4. Research Objectives

The general objective of this research is to identify the major issues and problems regarding registration for VAT in Ethiopia. Specifically this research work is aim at:

- Evaluating the practical implementation of VAT registration requirements provided by the law and identifying the reasons that limit their practical implementation;
- Examining whether the tax authority is clearly identifying those taxable activities used in the process of determining taxable persons;

- Evaluating the neutrality of the mechanism used by the tax authority to estimate the annual turnover of business persons as to the reach of the required threshold;
- Evaluating the appropriateness of the threshold for VAT registration fixed by the legislator in the face of the current inflation rate in the country;
- Weighing the compatibility of the grounds of cancellation of VAT registration with regard to the cessation requirements of both mandatory and voluntary registrations;
- Examining the existence or non-existence of a grievance handling mechanism for disputes that may arise in the process of registration for VAT and cancellation.

1.5. Research Design and Methodology

This research involves doctrinal examining of relevant laws. In doing so, the thesis has managed to analyze the FDRE Constitution, VAT Proclamation and its Regulation, several Directives related to VAT, Commercial Code of Ethiopia and its Draft, Tax Administration Proclamation, Income Tax Proclamation and technical notes of both the Income Tax Proclamation and the Tax Administration Proclamation. Moreover, it encompasses several scholarly works such as books, journal articles, unpublished writings, and economic analysis. Comparative analysis has been drawn from several countries' experiences. Hence, the experiences of Ghana and Uganda are selected based on their geographical and economic proximity to the Ethiopian system. On the other hand, countries like the United Kingdom (UK) and Australia are chosen for having the best experience in VAT.

In addition to the doctrinal methodology, the research involves significant empirical features. In this regard, the actual implementation of the laws on the ground was evaluated through the use of interviews and questionnaires. The relevant personnel chosen for interview were chosen through a technique of purposive sampling in a way that was suitable for the researcher in terms of the points that needed clarification, time and resources.

Accordingly, professionals from the Ministry of Finance and Economic Cooperation (MoFEC), the head office of Ethiopian Revenues and Customs Authority (ERCA), Addis Ababa Medium Taxpayers No. 1 branch office, Eastern Addis Ababa Medium Taxpayers branch office, Addis Ketema Small Taxpayers branch office, Addis Ketema Subcity Woreda 9 Micro Taxpayers branch office, Addis Ketema subcity Trade Bureau were chosen for interview. The reason for

choosing professionals Medium, Small and Micro branch offices of the tax authority is because the issues of attainment of the threshold for registration and other similar issues are raised here and not in the large tax payer's office. The researcher specifically chosen Addis Ketema subcity, Woreda 9 of the same and Addis Ababa No.1 branch office because they represent the major areas where many disputes regarding VAT registration are raised here for involving major market areas such as Merkato. The individual tax professionals chosen to fill out questionnaire were also chosen from the above areas because they represent many business persons.

1.6. Scope and Limitations of the Research

Because VAT is a broad concept that needs deep research and analysis, this research paper is restricted to the issue of registration for VAT and related issues. Again in this domain, the practice reviewed is restricted to the city of Addis Ababa, specifically Addis Ketema Subcity for the reasons mentioned in the research design and methodology. The scope is narrowed in this manner because of the time, financial and resource limitations. Coming to the limitation, non-cooperativeness of the relevant personnel in the various governmental offices was a significant hurdle faced by the researcher. Besides this limitation the researcher also faces the problems of reference materials.

1.7. Significance of the Research

This research tries to discuss general concepts, laws, and the practice related to VAT registration. But, it cannot address all the issues. Despite this, it can serve as the starting point for other researchers in the area. In addition, it can serve as reading materials for those who are interested in subject. It has also a significant contribution for informing tax authority officials and the law makers to enable them think about the problems existing in relation to registration for VAT.

1.8. Organization of the Research Paper

This research paper consists of four Chapters. The first chapter introduces the research whereas the second chapter addresses the conceptual foundation for the VAT registration by making an attempt to discuss concepts which are related to VAT registration. The third chapter explores the legal and practical issues in relation to VAT Registration under the Ethiopian VAT regime. The last chapter gives concluding remarks and relevant recommendations.

Chapter Two

2. Registration for VAT: General Overview

This chapter gives a general overview of concepts used in relation to registration for VAT in order to clarify the subsequent discussions included in the next chapter. In this regard, when one starts to treat the topic of registration for VAT, it is mandatory to grasp a general understanding over what the concept of VAT itself is, how it developed, what its nature is and what it includes and does not include as its subject and object. The following sections each deal with these concepts followed by the manner and types of registration for VAT.

2.1 Definition and Evolution of VAT

VAT is an indirect tax¹ charged on domestic consumption² of locally produced goods and services and imports.³ It is a kind of tax intended to be imposed on the value added⁴ on the goods and services sold by the seller.⁵ Hence, the seller is liable to pay the gross value minus the value of the inputs. Practically, it is implemented that the seller will take back the VAT paid on all goods and services acquired provided that the inputs are used for taxable transactions.⁶ Basically, VAT is imposed at each stage of production and distribution chain but the final tax is

¹ Indirect tax is a tax that is imposed upon supplies before they reach the consumer who eventually pays the tax as part of the market price of the supply. See Alan Schenk and Oliver Old Man Value Added Tax a Comparative Approach with Materials and Cases, Cambridge University Press,(2007), p.6

² Tax on consumption normally refers to a tax on goods and services that are acquired by individuals for their personal use or satisfaction. It does not include goods and services that are actually used by business in the production or distribution of goods or in the rendition of services.(Id,p.1)

³ Most countries do not impose VAT on export but tax paid on inputs is recoverable. Practice shows that Russia and other countries of the former Soviet Union, have levied VAT on some exports. See Bodin, Liam, Keen, Paul, and Summers, The Modern VAT, International Monetary Fund Publication Service (2001)p.1

⁴ The value added implies that either the aggregate of wages to labor and profits to owners of the production factors including land and capital or the difference between the value of output and the cost of inputs. See Tuan Minh Le, Value Added Taxation: Mechanism, Design, and Policy Issues paper prepared for the world Bank Course on Practical Issues of Tax Policy in Developing Countries Washington D.C. (2003), P.10 Available at <<http://www1.worldbank.org/publicsector/.../practicalIssues/...Value%20added%20taxation/>> last visited on August 23, 2016

⁵ Even though its name implies that a tax imposed on the value added by the seller, it is not generally intended to be a tax on value added as such rather it is usually intended as a tax on consumption. See Alan Schenk and Oliver Old man cited above at note 1, p.34

⁶ Despite the essence of VAT calls for the seller to claim refund for VAT paid on all goods and service purchased, some countries such as china currently do not grant credits for taxes on capital goods purchases; moreover, of those that allow credits in respect of such purchases, some do not refund excess credits. See Bodin, Liam, Keen, Paul, and Summers cited above at note 3,p.1

due on the final consumer of the product.⁷ This is achieved through the process that the traders who are registered for VAT are obliged to charge VAT on their sales but such traders are allowed to recover which they pay to their own suppliers which means that registered traders suffer no VAT and the total VAT is born by the consumer at the end of the distribution chain.

The twentieth century demanded states to increase their revenue⁸. This and the necessity of avoiding the cascading effect of sales tax⁹ are the two basic causes for the evolution of VAT.¹⁰ To achieve such objectives, German businessman Wilhelm Von Siemens¹¹ came up with the idea of VAT for the first time in 1920.¹² Following Wilhelm Von Siemens' idea, Thomas Adams¹³ discussed the concept of VAT in the USA in 1921 based on the principle of reducing the tax on sales by the tax already paid on business inputs.¹⁴ VAT was first introduced at a national level in France in 1954.¹⁵ Its original coverage was limited,¹⁶ and France did not move to a full VAT that

⁷ Alan Melville, Taxation Finance Act 1997, Pitman Publishing (3rd ed. 1994), p.473

⁸ Before the introduction of VAT the main source of revenue of states was income tax and traditional indirect taxes. But such taxes could not satisfy their revenue requirements, so the introduction of VAT seemed mandatory. After its introduction it became a major source of revenue for governments around the world and it generates on average one-quarter of all government revenue. See Tuan Minh Le, cited above at note 4, p. 3

⁹ The value added tax system is planned to tackle various problems connected with the usual sales tax system. In sales tax, there is no condition for input tax credit, which means that the end consumer may pay tax on an input that has already been taxed before. This is known as cascading and leads to increases the consumer tax and price levels. The value added tax system deals with these problems quite efficiently. As VAT is imposed on value addition at every single stage – there is no incidence of cascading. See SHASHANK S. DHOND, Impact of Sales Tax, VAT & GST on the Profitability of Organizations, (2010), unpublished, Library, Department of Business Management, PADMASHREE DR. D.Y. PATIL University, p. 32.

¹⁰ A.M. Bardopoulos, Commerce and the Effects of Technology on Taxation, Law, Governance and Technology Springer International Publishing Switzerland (2015) p.4

¹¹ Wilhelm von Siemens, a German businessman who invented VAT after World War I. The main problem was concerned by Wilhelm von Siemens was cascading taxes being levied on taxes which was a common problem with manufacturers and distributors. The VAT solved this problem by giving producers and distributors a credit for taxes previously paid so double taxation was eliminated. see A.M. Bardopoulos, Cited at note 10, p.25

¹² Ine Lejeune, The EU VAT Experience: What Are the Lessons? (2011) , p.257 Available at <<http://www.taxanalysts.com/www/freefiles.nsf/Files/LEJEUNE-21.pdf/.../LEJEUNE-21.pdf>> last visited on August 23, 2016

¹³ Thomas S. Adams (1873–1933), an American economist, is credited with much of the taxation policy of the World War I and post-war period. See Shashank S. Dhond cited at note 9, p.25

¹⁴ Ibid

¹⁵ Kathryn James, Exploring the Origins and Global Rise of VAT Faculty of Law, Monash University, Melbourne. (2011), p.16 available at <[http://www.taxanalysts.com/www/freefiles.nsf/Files/JAMES-2.pdf/\\$file/JAMES-2.pdf](http://www.taxanalysts.com/www/freefiles.nsf/Files/JAMES-2.pdf/$file/JAMES-2.pdf)> last visited on August 23, 2016.

¹⁶ The French VAT system covered the industrial sector alone and the tax was limited up to the whole sales level only it does not consider the retail sales before 1968. See Shashank S. Dhond, cited above at note 9, p.69

achieved the broader retail sector until 1968.¹⁷ The first full VAT in Europe was enacted in Denmark in 1967.¹⁸

While the specific reasons for adopting the VAT differ from one country to another,¹⁹ VAT was rapidly adopted in the world in two major phases.²⁰ The first phase occurred mostly in Western Europe and Latin America during the 1960s and 1970s. The rise of VAT in Western Europe was accelerated by a series of European Economic Commission (EEC) directives requiring member states to adopt a harmonized VAT upon entry into the European Union. The second phase of VAT adoption occurred from the late 1980s with the introduction of VAT in some high-profile industrialized countries outside the European Union (EU), such as Australia, Canada, Japan, and Switzerland.²¹ This phase also witnessed a significant expansion of VAT in transitional and developing economies, most notably in Africa and Asia.²² The system of VAT has been implemented in 163 countries until 2013.²³ Ethiopia joined by issuing Proclamation No. 285/2002, which replaced the sales and excise Tax proclamation No. 68/1993 to enjoy the fruits of VAT.²⁴

¹⁷ See, Kathryn James, cited above at note 15,p.16

¹⁸ Ibid

¹⁹ Adoption of VAT systems followed both external, internal and hybrid pressures. External pressures included coercion from international financial organizations and, sometimes, advice from agencies of former colonial powers. Internal pressures included difficulties collecting sufficient revenue from income taxes, excise taxes and other levies. Hybrid pressures arose from moves to regional trade blocks and international changes to tariff regimes which often threatened tariff collections, a key source of national revenue. See, A.M. Bardopoulos , cited above at note 10, p.27

²⁰ See, Kathryn James, cited above at note 15,p.16

²¹ Ibid

²² Ibid

²³ See, Ine Lejeune, cited above at note 12,p.260

²⁴ In Ethiopia, according to IMF report, one of the focuses of the tax policy reforms is reforming indirect taxation. The main reform to indirect taxation was the introduction of Value Added Tax in January 2003. And it became the major source of revenue for the Ethiopian government. For instance, in the 2006–07 fiscal years, Federal VAT revenue (on domestic transactions) accounted for about 41 per cent of total Federal revenues from domestic sources. See, Wollela Abehodie Yesegat, Value Added Tax Administration in Ethiopia: A Reflection of Problems, e Journal of Tax Research, vol.6,No.2,(2008) p.,145

2.2 Nature and Scope of VAT

VAT is a system of taxing domestically produced goods and services and imports at each stage of the production and distribution process.²⁵ It does not depend on the gross transaction of the seller; rather it depends on the value added at each stage of production and distribution chain. Besides this, not being applicable on exports is another significant feature of VAT.²⁶

Recently, VAT is widely employed by developing and developed countries of the world and becomes significant source of government revenues.²⁷ Some of the features that make VAT preferable to other types of taxes are: - its neutrality, its self enforcing nature, its nature of transparency, certainty, its relative easiness to understand, its nature of stability with respect to source of government revenue, and its less volatility to tax evasion. Avoiding the impact of VAT on traders and exempting exports from VAT liability enables the VAT to have a nature of neutrality. Besides this it lessens the tendency for tax evasion.²⁸

For the purpose of avoiding the impact of VAT on traders, the VAT system follows different modes of computation.²⁹ Among the mode of computation of VAT, the invoice or tax credit method is the most acceptable one around the world.³⁰ According to this mode of computation, to claim refund for input VAT, the claim should be supported by purchase invoices.³¹ In other words the claim of refund of the input VAT depends on the purchase invoices. This system motivates the claimants to keep invoices of their transactions and in effect it enhances the tax authorities to check and cross-check for VAT enforcement. It also gives a nature of self enforcing for VAT.³² Such invoice or credit method of computation of VAT, allows accurate

²⁵ Value Added Tax: Characteristics, Mode Computation, Merits and Weaknesses available at <http://www.nipfp.org.in/media/pdf/books/BK_39/.../5.%20Value%20Added%20Tax.pdf > last visited on August 28, 2016.

²⁶ Ibid

²⁷ See Alan Schenk and Oliver Old man cited above at note 1, p.34

²⁸ Id,p.35

²⁹ There are three widely known methods of computing VAT liability. These are addition method, subtraction method, and invoice method. For a detailed analysis of these methods, see Alan Schenk and Oliver Old man, cited at note 1, p.38-46.

³⁰ Id,p.38

³¹ Id,p.39

³² See Tuan Minh Le, cited above at note 4, p.7

quantifying of the tax born at the earlier stages of transaction at any given stage.³³ This enhances VAT to have a nature of transparency.³⁴ Since VAT is based on transactions and not on difficult terms like income or wealth, it has the merit of certainty, making it relatively easy to understand.³⁵ The nature of stability of VAT as revenue source emanates from the fact that consumption is relatively stable than income.³⁶

To benefit from VAT and properly administer it, countries of the world should decide the scope of application of it. Accordingly, countries have tried to decide the scope of application of VAT. All sales by any person are not the subject of VAT. Basically VAT only applies when a taxable person makes taxable supplies of goods and services in the course of business transactions.³⁷ The concept of taxable person and taxable supplies is discussed in the following sections since such discussion will help to better understand the scope of VAT.

2.3. Taxable Persons

Identification of Taxable person is very important in a VAT system. Unless a VAT system of a given country efficiently and effectively identifies the taxable persons, it will be difficult for such country to apply the VAT rules and be beneficiary from the merit of VAT. The definition and practical application of the concept of taxable persons is different in different parts of the world.³⁸ For instance, the EU's Sixth VAT Directive defines taxable persons as "any person who independently engaged in any economic activity specified in any place whatever the purpose or results of that activity".³⁹ The economic activities may include, trading activities, supplying services, mining, agriculture and professional activities. For VAT purpose, the term person refer to all legal persons created under the law of the state or of a foreign country that engage in economic activities of any kind, as well as all physical persons who supply goods and/or services in the course of business.⁴⁰ There is no requirement that a profit motive should exist.⁴¹

³³ Ibid

³⁴ Ibid

³⁵ Ibid

³⁶ Ibid

³⁷ See, Alan Melville, cited above at note, 7,p.474

³⁸ See, Ine Lejeune, cited above at note 12, p.270

³⁹ Ibid

⁴⁰ Victor Thuronyi , Tax Law Design and Drafting , International Monetary Fund(Victor Thuronyi, ed.1996,) Vol.1 Chapter 6,p.13

⁴¹ Ibid

The concept of taxable persons corresponds with that of a person who is or must be registered for VAT purposes.⁴² A registration threshold is employed to relieve some taxpayers from this requirement in order to avoid a disproportionate compliance and administrative burden for taxpayers with low turnovers.⁴³

The basic issues existing in relation to the definition of taxable persons under a VAT system are:
- the treatment or otherwise of partnerships as separate legal entities under the VAT law, and the treatment of branches, group of companies, permanent establishments, holding companies, government agencies and of transactions and services rendered by non legal owners and suppliers.⁴⁴

The issue of legal personality of partnerships separate from the individuals who are its members varies from one state to another and the law may need to reflect this.⁴⁵ In most civil law countries, most partnerships are not considered as legal entities. So, generally, the managing partner is considered as a taxable person for VAT purposes but the partner who contributes only capital will be liable to the extent of his or her contribution. In the United Kingdom (UK), a common law country, the experience varies. Partnerships have legal personality only in Scotland but not in the other parts of the UK.⁴⁶ If there is a separate registration of a partnership, then the system should only recognize all relevant supplies made by the partnership and ignore those supplies made by the partners.⁴⁷

Due to tax and non tax reasons, some states also permit separate branches of a juridical person to be considered as separate taxable persons. In this case a supply by one branch to another branch is a taxable supply. When groups of companies are registered together as one taxable person, a supply by one of the companies to another will not be a taxable supply. Joint treatment of a group of companies is useful for income tax purposes. But separate registration may prove useful for VAT purposes by allowing, for example, a split between the taxable and non-taxable

⁴² Ibid

⁴³ See, Ine Lejeune, cited above at note 12, p.271

⁴⁴ See, Victor Thuronyi, cited above at note 40,p,12-13

⁴⁵ Ibid

⁴⁶ See Alan Schenk and Oliver Old man cited above at note 1, p.95

⁴⁷ Ibid

activities of a company where those separate groups of activities are carried out by different divisions of the company or organization.⁴⁸

Since the destination principle (i.e. taxation in the country in which the goods or services are used) is becoming increasingly influential in VAT, permanent establishment is usually considered as taxable persons for VAT.⁴⁹

Since the activities of governmental authorities are sovereign activities of the state and not commercial activities, governmental authorities and bodies governed by public law are not taxable persons if they engage in activities as public authorities.⁵⁰ In addition to governmental authorities pure holding companies are treated mostly as nontaxable persons for VAT purposes according to EU rules. The justification behind the exclusion of pure holding companies is that these companies are not actively involved in the management of their subsidiaries.⁵¹

There are situations where the non legal owner of property or non real supplier of the service may be treated as taxable person for VAT. Some of the situations are sales by auctions and sales by non owners.⁵² There are different situations where sales of goods and supplies of service can be made by auctions. These are, for example, when an auctioneer serves as agent of the owner,⁵³ auctions by a unit of government of goods confiscated from persons under authority of law⁵⁴ and goods repossessed on default by a debtor may be auctioned.⁵⁵ In all of these situations, the “seller” at auction is selling in the name of the person who owns the property or is treated as the person with legal authority to sell and thus treated as the agent of the seller receiving a commission for its services.⁵⁶ Generally, in many VAT systems the person making the taxable supply or sale is liable as far as the person is a VAT registered person. But in the above mentioned cases, since the auction is carried out by the agent on behalf of a principal, the supply is considered a supply by the principal. Without special rules governing auction sales, these sales

⁴⁸ Id, p.88

⁴⁹ Permanent establishment is a fixed place of business which generally gives rise to income or value-added tax liability in a particular jurisdiction. See, Victor Thuronyi, cited above at note 40, p, 12.

⁵⁰ See, Ine Lejeune, cited above at note 12, p.270

⁵¹ Holding company is a company a *company* that does not produce goods or services itself; rather, its purpose is to own shares of other *companies* to form a corporate group. Ibid

⁵² See Alan Schenk and Oliver Old man cited above at note 1,p.96-97

⁵³ Ibid

⁵⁴ Ibid

⁵⁵ Ibid

⁵⁶ Ibid

would be treated under most VATs as sales by the principal or usually by the owner of the goods. But, in exceptional cases, the auctioneers are considered as taxable persons in cases where the sales are made by private consumers or by goods dealers.⁵⁷

The other issue that arises in the process of determining a taxable person in VAT system is the sale concluded by representatives of owners, mortgagees, or executors of a deceased person's estate, and a custodian of the assets of a person. In all these cases, though the economic activities are performed by these persons, they are not considered as taxable persons but they are responsible for VAT compliance such as reporting, collecting, and paying the VAT.⁵⁸

2.4 Taxable Supplies

For VAT purpose, the terms “taxable supplies”, “taxable activities” or “taxable transactions” are employed by different literatures interchangeably. Though the term taxable supplies is mostly in use, this term is given very wide meanings that go more than the usual meanings of "supplies."⁵⁹ It charges all economic activities in particular dealing with land or other immovable property and with intellectual property rights. Therefore, the terms should not be restricted to usual meanings of the word supply.⁶⁰

Taxable supplies are defined as supplies or transactions made by a taxable person as part of his/her/its economic activities against payment or for consideration from some other person.⁶¹ According to this definition, to be considered as taxable supplies, three basic elements should be satisfied. These are the supplies should be made by taxable persons, the supplies should be related with the business activities of such taxable persons and supplies should be against payment or for consideration.

It is indicated in the above section that For VAT purposes, taxable persons include all legal persons created under the law of the state or of a foreign country, and all physical persons as far as they meet the threshold requirement incorporated by a given country law.⁶² However, not all

⁵⁷ Ibid

⁵⁸ Ibid

⁵⁹ See, Victor Thuronyi, cited above at note 40, p.20

⁶⁰ Ibid

⁶¹ Ibid

⁶² See, Ine Lejeune, cited above at note 12, p.270

economic activities made by such persons are subject to VAT. Non business activities such as the personal hobbies of an individual, gift made for personal reasons or charitable activities are not under the scope of VAT.⁶³ Taxable supplies generally are limited to transactions made in connection with a business.

Any supply, to be within the scope of VAT, should be followed by a payment or consideration.⁶⁴ This emanates from the special nature of VAT.⁶⁵ If a supply directly or indirectly does not add any value for the supplier, it is not under the scope of VAT.⁶⁶ This is because VAT relies on the value added by the supplier. This means that VAT is the difference between gross value of the output tax and the input tax.⁶⁷ The mode of payment can be in kind or in cash.⁶⁸ As a rule, if there is no payment for a supply, it is not regarded as a taxable supply. However this rule needs exceptions as it may allow for transactions to elude VAT liability.⁶⁹ The situations which create such rooms are the total avoidance of payment for tax credited supplies and in the cases where partial payment is received by the supplier for such supplies.⁷⁰ To regulate such situations, a VAT law is expected to fill such gaps by extending the definition of consideration to the extent of addressing such issues.⁷¹ In most countries' VAT laws, though the payment is not made, any consumption, gift, or use of goods purchased for business purposes by the owner of the business or by any other third parties are taken as taxable supplies.⁷² But it does not include goods such as those used for advertising and trade samples which are taken as business expenses to avoid unnecessary charge on a taxable person.⁷³ The controversial issue in the cases of a supply without consideration is determination of the amount of VAT charged on a taxable person. In this case, the law should devise a mechanism to enable the determination of the estimated value of the supply in question. It may be the open market price or some other objective mechanisms.⁷⁴

⁶³ See Alan Schenk and Oliver Old man cited above at note 1, p.103.

⁶⁴ Id,p.112

⁶⁵ Ibid

⁶⁶ HL Bhatia, Public Finance (24th. ed. 2003) p. 132

⁶⁷ Ibid

⁶⁸ See , Victor Thuronyi, cited above at note 40, p.35

⁶⁹ Ibid

⁷⁰ Ibid

⁷¹ Ibid

⁷² See Alan Schenk and Oliver Old man cited above at note 1.p.117

⁷³ Ibid

⁷⁴ For detail analysis See , Victor Thuronyi, cited above at note 40, p.45

In the cases where partial payment is made, parts of the amount of the supply will take place on different dates.⁷⁵ Any further supplies are treated by separate invoices issued in respect of each payment. Otherwise, partial payments could be used as a means to avoid or delay the payment of VAT.⁷⁶

2.4. 1 Supply of Goods

To avoid any confusion, VAT laws are expected to define supply of goods. For VAT purpose supply of goods is defined as a transfer of the right to dispose of tangible movable property or of immovable property other than land.⁷⁷ In most states, transfer of possession does not constitute supply of goods rather it is supply of services. But in the U.K, the transfer of possession of goods is taken as supply of goods in the cases where possession of goods is transferred under an agreement for the sale of goods in the future time.⁷⁸ Though the definition of supply of goods includes immovable, land is excluded from the scope of VAT. But leases and building for the owner of the land are under the scope of VAT.⁷⁹ The laws of countries extend the definition supplies of goods to supplies of power, heat, refrigeration, and supply of water.⁸⁰

2.4.2Supply of Services

The recommended and best practice of VAT system of different nations shows that the base of VAT is broad with minimal exemptions.⁸¹To ensure this, the scope of VAT statute is expected to include supplies (which are not included under the supply of goods) under the supply of service. Generally, it is understood that any transaction, other than supply of goods and land, that is done for consideration is supply of service.⁸² This approach creates no room for supplies to escape from the scope of VAT. This approach covers use of all forms of property and also transfers of the right to dispose of intangibles.⁸³ To fall within the scope of VAT, a supply of service should

⁷⁵ Id, p.38

⁷⁶ Ibid

⁷⁷ Though, supply of goods is defined indifferent manner in different VAT laws of states, most states infer the concept from EU Sixth Directive .see, Alan Schenk and Oliver Old man cited above at note 1,p.126

⁷⁸ Victor Thuronyi, cited above at note 40,p.22

⁷⁹ Ibid

⁸⁰ Id,p.23

⁸¹See, Ine Lejeune, cited above at note 12, p.267

⁸² See, Victor Thuronyi, cited above at note 40,p.25

⁸³ Ibid

be a business supply.⁸⁴ This means, as discussed in relation to taxable supplies above, the person making the supply should be a taxable person, the supply should be related with his/her/ its business transaction, and some other person should makes a payment for the supply.

2.5 Exempt Transactions

In most VAT laws of states, the general rule for taxable supplies is not absolute. It recognizes exemptions. Accordingly,

The term ‘exempt supplies’ is used in most VAT systems to describe supplies that do not allow output tax the supplier need not collect or remit any tax in respect of the supply – and do not entitle the recipient to any input tax credits in respect of tax borne on acquisitions related to the making of the supply.⁸⁵

In exempted supplies operated by a supplier, the supplier is not required to be registered for VAT and hence output VAT is not collected. So, the buyers have no right to claim any input credits on those purchases as they do not pay any when they buy exempted goods and/or services. The seller cannot claim input credits for VAT on its purchases related to such exempted supplies.⁸⁶ In this regard Victor Thuronyi argues that exemption doesn’t reduce the VAT burden on taxable suppliers; rather, it increases the VAT burden on taxable suppliers and as it does not have significant effect on the reduction of price of goods and services for the consumers.⁸⁷ With regarded to taxable suppliers, such scholars argued that:

The person running the business can balance the VAT against the VAT charged by the business, so claiming a full refund for any VAT. The person making the exempt supply will probably have had to pay VAT on some part of the supplies made to it and will therefore have to pass some VAT on to the business as part of its price. It is this VAT that can be recovered if the supply is subject to tax, but that cannot be recovered if it is exempt.⁸⁸

From the perspective of consumers, the proponents of this argument contend that even if the consumers are free from VAT burden, they will not be free from other indirect taxes; for instance, stamp duties or transaction taxes or high registration fees on the documents used for the transfers of rights. So, according to the proponents of this argument, in one or other ways the price of the goods and services consumed by the consumer is not reduced. Besides, exemption

⁸⁴ See, Alan Schenk and Oliver Old man cited above at note 1.p.127

⁸⁵ Rita de la Feria and Richard Krever, “VAT Exemptions Consequences and Design Alternatives” EUCOTAX Series on European Taxation ” Vol.37(2013) p.11

⁸⁶ See, Victor Thuronyi, cited above at note 40,p.40

⁸⁷ Ibid

⁸⁸ Ibid

creates practical problems in the process of determining the input tax credits for those taxable persons who make mixed supplies.⁸⁹ Due to these and other reasons all proposed for minimal use of exemptions.⁹⁰ Although there are strong recommendations for minimizing exemptions, no state has removed exemptions from its VAT law. Among the reasons of introducing exemptions on states VAT laws, political consideration of individual states in general and social consideration in particular and policy consideration to deliver subsidies through the tax system is the basic ones.⁹¹

The approach followed on exemption of supplies varies from jurisdiction to jurisdiction. Some states follow the standard exemption rules provided by the Organization for Economic Cooperation and Development (OECD) and EU six directives. Such as exemption of postal services, transport service, hospital and medical care, education, sporting activities, cultural services, charitable work, non commercial activities by non-profit organizations, certain fund-raising events, the supply of land and buildings, lotteries and gambling, insurance, and financial services including loan intermediary services.⁹² In contrast some states for instance Argentina and China follow the approach of listing taxable supplies rather than listing the exemptions.⁹³

For the purpose of making the discussion on exemption easy most literatures categorize exemptions into out of scope supplies exemptions, out of scope suppliers' exemptions, and technical exemptions.⁹⁴ Out of scope supplies exemptions refers to those supplies which are not included in VAT legislation or the judicial interpretation of the given country.⁹⁵ This occurs when the VAT legislation of a given country employed restrictive terminology or the judiciary interprets terms used in the law in a restrictive manner.⁹⁶

Regarding out of scope suppliers' exemptions, most VAT laws exclude three groups of persons from VAT liability. These are small businesses, deemed 'Non-business' Enterprises, Government bodies, and Charities.⁹⁷ For the purpose of determining the balance of collection costs against the value of additional tax revenues, the VAT laws provide registration thresholds

⁸⁹ See, Rita de la Feria and Richard Krever, Cited at note 85, p.13

⁹⁰ See, Ine Lejeune, cited above at note 12, p.267

⁹¹ See, Victor Thuronyi, cited above at note 40, p.39-40

⁹² See, Rita de la Feria and Richard Krever, Cited at note 85, p.12

⁹³ Ibid

⁹⁴ Ibid

⁹⁵ Ibid

⁹⁶ Ibid

⁹⁷ Ibid

to identify and register taxable persons. Those businesses and individuals below the registration threshold are exempted from compulsory registration and inclusion in the VAT system.⁹⁸ So, the taxable supplies made by such small businesses and individuals below the registration threshold are exempted supplies.

There are business enterprises which are deemed non business enterprises for VAT purpose, such as mutual business organizations⁹⁹, holding companies¹⁰⁰ and investment companies¹⁰¹. The reason behind such consideration is that all these enterprises play intermediary roles in the economy, rather than engaging in the day to day activities of the enterprises. The members of such enterprises are not the final consumers and they do not claim input tax credit. So, even though, such enterprises are business enterprises, they are considered as non business enterprises for VAT purpose.¹⁰²

Though the services provided by government bodies and charities are controversial with regard to unfair competition to the private sectors, many countries exempt most sales of goods and services rendered by government bodies and charities. Different nations follow different approaches with regard to the treatment of the service provided by the governmental bodies and charities. Some may tax sales of specific goods and services which are out of their purposes.¹⁰³ Due to technical reasons, three categories of supplies are exempted from VAT liability. These are supplies of immovable property, financial services and pooling services¹⁰⁴, including

⁹⁸ Ibid

⁹⁹ A mutual company is a private company whose ownership base is made of its clients or policyholders. The defining feature of a mutual company is since its customers are also its owners; they are entitled to receive profits or income generated by the mutual company. See, Rita de la Feria and Richard Krever, Cited at note 85,p.14

¹⁰⁰ Holding company is a type of firm that owns other investments, including whole companies, instead of engaging in operating activity itself. See, Rita de la Feria and Richard Krever, Cited at note 85,p.14

¹⁰¹ Investment companies are business entities, both privately and publicly owned, that manages, sell, and market funds to the public. They typically offer investors a variety of funds and investment services, which include portfolio management, recordkeeping, custodial, legal, accounting and tax management services. See, Rita de la Feria and Richard Krever, Cited at note 85,p.14

¹⁰² Ibid

¹⁰³ For in EU member countries activities of states, regional and local governments other than public services are subject to VAT registration regardless of the attainment of the required threshold. See, Alan Schenk and Oliver Old man cited above at note 1.p.286

¹⁰⁴ See, Rita de la Feria and Richard Krever, Cited at note 85 p.25

insurance and gambling.¹⁰⁵ It is difficult to apply VAT on these supplies because the nature of the supplies is not certain.¹⁰⁶

Most EU states in the world provide that a sale of immovable or other transfer of the title to immovable and the main services related to such properties is outside of the scope of VAT. The VAT systems of such countries, commonly does not exempt both residential and commercial immovable properties.¹⁰⁷ Rather it only exempts the residential immovable properties.¹⁰⁸ Exceptionally, there are countries which have exceptional rules on the treatment of residential immovable. For instance, in Australia, sales of new residential immovable are taxable and sales of used residential immovable are exempt from VAT liability. Canada also has the same experience as Australia.¹⁰⁹

All VAT tax systems in the world except Russia exempt financial supplies.¹¹⁰ Such financial supplies include investments in ownership rights, the loan intermediary service offered by financial institutions to lenders and borrowers, intermediary pooling service arrangements such as gambling, lotteries and insurance.¹¹¹ The basic rationale for the exemptions of financial supplies is to avoid technically complicated administrative problems.¹¹² For instance, in the cases of investments in ownership rights, it would be administratively impossible to apply the normal VAT rules to supplies of intangible ownership assets and then register all investors acquiring these supplies and process input tax refunds for the VAT imposed on the supplies.¹¹³ Alike the investments in ownership rights, the loan intermediary service and intermediary pooling services have faced similar administrative problems to measure the value added by such supplies that is why all countries exempt financial supplies from the scope of VAT.

¹⁰⁵ Ibid

¹⁰⁶ Ibid

¹⁰⁷ Id,27

¹⁰⁸ See Alan Schenk and Oliver Old man cited above at note 1,p.410

¹⁰⁹ Ibid

¹¹⁰ See, Rita de la Feria and Richard Krever, Cited at note 85,p.29

¹¹¹ Ibid

¹¹² See, Victor Thuronyi, cited above at note 40,p.42

¹¹³ See, Rita de la Feria and Richard Krever, Cited at note 85,p.30

2.6 Mixed Supply

A mixed supply is a supply that contains both taxable and non taxable supplies.¹¹⁴ Usually, mixture of different things involving both goods and services are supplied together. In these cases, it is difficult to determine whether the supply is taxable or not. Unless the status of the supply is determined, it is difficult for states to impose VAT and to give the right of recovering input tax credit on such supplies. To avoid such controversy, states follow different approaches. For instance, according to Australian Tax Office, to be taken as mixed supply the supply has to be separated as it contains separately identifiable taxable and non-taxable parts that need to be individually recognized.¹¹⁵ By contrast, if the supply contains a dominant part and it includes something that is integral, or subsidiary to that part, then the supply is not mixed, rather it is composite supply.¹¹⁶ The European Court of Justice (ECJ) also follows the criteria that if one element of a supply dominates the other elements, the dominant one is considered as the only supply.¹¹⁷ Besides such approach that it follows by itself, the ECJ also gives the authority to national courts of other European countries. This approach is also followed by non European countries.¹¹⁸

2.7 Zero Related Supplies

Zero rated supplies refer to a system of exempting supplies from output tax.¹¹⁹ It does not mean exemption, rather it brings the taxable transactions within the operation of the VAT credit for input tax, which an exemption does not.¹²⁰ VAT credit is allowed for inputs used in making taxable supplies.¹²¹ The concept of zero rating is usually linked with the concept of destination principle. According to destination principle, the VAT paid in the processes of purchasing exported goods, services and any taxable costs related to the taxable transaction by exporter is refunded but the exporter is not obliged to collect VAT from his/her/its sells.¹²² It can be a means

¹¹⁴ < <https://www.linkedin.com/.../difference-between-composite-mixed-supply-ram-sunder..> > LASTED visited on September 15, 2016.

¹¹⁵ See, Alan Schenk and Oliver Old man cited above at note 1, p.131

¹¹⁶ Ibid

¹¹⁷ Ibid

¹¹⁸ Id, 132

¹¹⁹ See, Victor Thuronyi, cited above at note 40, p.50

¹²⁰ Ibid

¹²¹ Id, p.51

¹²² Ibid

of subsidies for exports. Though any subsidies is prohibited or restricted by WTO (World Trade Organization) rules, any indirect tax adjustment is not constituted as subsidies under the WTO rule.¹²³ In addition to exports, international transports with its supporting supplies are also zero-rated supply.¹²⁴

Few states zero rate some internal supplies.¹²⁵ This is highly opposed by scholars who criticize it by claiming that it is a form of subsidy, but such scholars also raised the justifiability of some internal supplies such as monetary supplies, supplies of the currency and transfer of an ongoing business.¹²⁶

2.8 Registration for VAT

Though there is no universally accepted definition for VAT registration, from the purpose of the VAT registration it can be defined as the process of listing with the government registry as a business or individual entitled for the return of input tax and remit of output tax.¹²⁷ From this definition, it can be easily inferred that VAT registration has both entitlement of rights and the imposition of obligations on the registered person. For proper administration of VAT, a state are expected to have a system of law which can easily identify the VAT registered persons, a system of regulation of related persons, the treatment of group of companies in VAT registration and the exit of VAT registration. These and related issues are discussed as follows.

2.8.1 Mandatory Registration

Most VAT system of the world makes under the obligation of VAT registration, persons who make or expect to make at least the statutory minimum level of annual taxable sales in connection with its business or economic activity.¹²⁸ For the purpose of mandatory registration, the attainment of the statutory threshold does not consider all sales of a person.¹²⁹ Rather, only the taxable supplies of the person are taken into consideration. Taxable supplies do not include exempted supplies, supplies outside the scope of VAT and irregular business activities.¹³⁰ So, the

¹²³ See, Alan Schenk and Oliver Old man cited above at note 1,p.203

¹²⁴ See, Victor Thuronyi, cited above at note 40,p.51

¹²⁵ Ibid

¹²⁶ Ibid

¹²⁷ Id,16

¹²⁸ See, Ine Lejeune, cited above at note 12,P.271

¹²⁹ Ibid

¹³⁰ Ibid

companies or the individuals with high economic activities may not be necessarily registered, unless the economic activities are related with the taxable supplies of such individual or companies.¹³¹

For the purpose of determining whether the taxable sales of a firm or individual has reached the threshold or not, the usual rule depends on the book of accounts of the taxpayers.¹³² By default all taxpayers, except small tax payers, are obliged to maintain books of accounts, records, and other financial data.¹³³ In cases where such books and accounts are not properly kept or not accepted by the tax authority, most states employ the indirect means to ascertain tax liability that is usually called “presumptive” taxation rules.¹³⁴

Though presumptive taxation rules are usually implemented on small businesses and for the purpose of determining income tax, they are also applied on all businesses, including large companies for the purpose of determining VAT liability.¹³⁵ In the process of determining tax liability, the tax authorities are usually authorized to assess the tax liability based on their best judgment rules.¹³⁶ They can also employ different methods such as net worth, bank deposits, and some other approaches that have a factual basis for the particular case.¹³⁷

The net worth approach is the means of determining the tax liability based on the tax payer net worth over the year by adding estimated personal consumption expenses and by examining the taxpayer's lifestyle.¹³⁸ It may not be possible to use the net worth method because of the lack of evidence as information is needed from the tax payer and it needs complicated audit

¹³¹ Alan Schenk and Oliver Old man cited above at note 1, p.75

¹³² For the purpose of imposing the obligation of keeping book of accounts and for any other tax administration purpose, countries in the world employed different criteria to classify tax payers in to large, medium, and small tax payers. For example, In the Netherlands for the criterion “total turnover” is employed. But the value varies depending on the business activities. All the taxpayers with more than EUR 25 million; foreign parent company - EUR 12.5 million, Governmental organizations, and hospitals with more than EUR 37.5 million are falls under the category of large tax payers. see IOTA Report for Tax Administrations, Intra-European Organization of Tax Administrations (IOTA)(2008), p.7 available at < <https://www.iota-tax.org/.../iota-report-tax-administrations-atp-aggressive-tax-plannin...>> Last accessed on September 20, 20016

¹³³ See, Victor Thuronyi , Tax Law Design and Drafting , International Monetary Fund(Victor Thuronyi, ed.1996,) Vol.1 Chapter 12,p.2

¹³⁴ Id,5

¹³⁵ Id,8

¹³⁶ Id,9

¹³⁷ Id,9-12

¹³⁸ Id,15

works.¹³⁹ The taxpayer is usually permitted to invalidate the results under the net worth method either by providing evidence of actual receipts for consumption in addition to proving that the increase in net worth was resulted from financing by nontaxable receipts such as gifts and bequests.¹⁴⁰

The other method employed by auditors to determine the tax liability of a tax payer is securing bank information both from domestic and foreign banks.¹⁴¹ Unless the taxpayer proves the contrary, the bank deposit is considered as an income.¹⁴² This method is not helpful in the countries where the amount is transferred on a cash base.¹⁴³

The other method of determining the tax liability based on the indirect method is expenditure method.¹⁴⁴ This method depends on the cash expenditure of the tax payers. It is applied when the net worth of the taxpayer is not available for the tax authorities.¹⁴⁵ In addition to the above mentioned methods of presumptive taxation, some countries also follow percentage of gross receipts method and percentage of assets.¹⁴⁶

The process of setting the statutory threshold for the purpose of mandatory VAT registration and the amount of the threshold is different in different countries.¹⁴⁷ From the beginning, VAT was introduced to collect high revenue with less administrative costs.¹⁴⁸ To achieve this goal states are expected to select their tax payers by considering their administrative capacity of taxation. The measurement of administrative capacity starts from identification of the tax payers to final audit.¹⁴⁹ The variation of the statutory threshold is the reflection of the economic level of a state. In countries where the number of marginal small businesses is great and the peoples' economy depends on subsistence farming, it would be administratively difficult to collect VAT from such

¹³⁹ Ibid

¹⁴⁰ Ibid

¹⁴¹ Id,16

¹⁴² Ibid

¹⁴³ Ibid

¹⁴⁴ Id,17

¹⁴⁵ Ibid

¹⁴⁶ Ibid

¹⁴⁷ Clara K.Sullivan, The TAX on Value Added, Columbia, University Press(1965) p.215

¹⁴⁸ Ibid

¹⁴⁹ See, Ine Lejeune, cited above at note 12,P

people. So, it is better to exclude small traders from VAT through the use of a threshold limit.¹⁵⁰ The International Monetary Fund (IMF) has also recommended high turnovers for a threshold in the process of mandatory VAT registration.¹⁵¹ Besides the IMF's recommendation, state practices show that lower threshold is the cause of the collapse of a VAT system. For instance, both Ghana and Uganda introduced VAT in 1995 and 1996 respectively with low threshold. Hence, the tax offices of these countries tried to register a large number of small businesses that had very little understanding of the requirements for and functioning of the VAT system.¹⁵² Such practice of registration was the cause for serious demonstrations and riots. In Uganda, authorities passed immediate decision to increase the registration threshold and it ensured the continuation of the VAT system.¹⁵³ But, in Ghana, the degree of the opposition against VAT led the government to abolish the VAT law, which was reintroduced in 1999, with a significantly higher threshold.¹⁵⁴ Besides setting high threshold, a VAT law is expected to consider the future possible inflation rate of nations by allowing the authorities to change the amount set from time to time since doing so ensures that the tax is working properly.¹⁵⁵ For instance, in UK, the VAT registration threshold in 2015/16 was £82000 and for 2016/17 is £85000.¹⁵⁶ However, Mandatory registration of VAT does not always rely on the statutory threshold of business. Sometimes, small businesses are obliged to register for the purpose of preventing unfair competition between registered and unregistered tax payers.¹⁵⁷

2.8.2 Voluntary Registration

In situations where the interest of the business requires, states usually allow VAT registration for businesses whose annual turnover is below the statutory threshold.¹⁵⁸ The basic situations which force the business for voluntary registration are, in the cases where the business making wholly or mainly zero rated supplies, most of the supplies are to other VAT registered businesses and in

¹⁵⁰ See ,Jean-Paul Bodin and Vincent Koukpaizan, "The Rise of VAT in Africa – Impact and Challenges"(2009) p.183

¹⁵¹ See, Ine Lejeune, cited above at note 12, P. 267.

¹⁵² See, Jean-Paul Bodin and Vincent Koukpaizan cited at note 150,p.183

¹⁵³ Id,184

¹⁵⁴ Ibid

¹⁵⁵ See, Victor Thuronyi, cited above at note 40,p.15

¹⁵⁶ <<https://www.cchdaily.co.uk/budget-2017-vat-registration-threshold-rises-ps85k>> Last accessed on September 20, 2016.

¹⁵⁷ Fabiola Annacondia and Walter van der Corput, "VAT Registration Thresholds in Europe"(2009) p.488

¹⁵⁸ See, Victor Thuronyi, cited above at note 40,p.17

the cases where significant amounts of VAT is incurred on capital expenditure.¹⁵⁹ In this case, some states may deny the application of the voluntary registration unless the applicant fulfils specific requirements stipulated in a given VAT law of a country. For instance, in Uganda an applicant to register in the voluntary registry, should have fixed place of business, he/she/it should keep proper accounting records, he/she/it should have bank account and if he/she/it has been previously registered for VAT purposes it should not have failed to perform its duties under the VAT law.¹⁶⁰ Some scholars strictly recommend that when states allow voluntary registration, they should consider two basic things.¹⁶¹ These are: ensuring that the real intention of the business is not with a view to claiming refunds of input tax rather than continuing the business. Secondly, allowing voluntary registration should not create administrative difficulties for the tax authorities.

2.8.3 Registration of Related Parties

In practice, the owners of the business may attempt to avoid VAT registration by splitting the business into separate parts and escape the statutory threshold by creating different owners among related parties. In this situation, each party is trying to act as a separate supplier. For the purpose of avoiding this, most laws of most states authorize their tax officers to aggregate the sales of businesses owned by related parties.¹⁶² One controversial issue in this regard is defining the scope of related parties, especially in countries where there is an extended family structure in which many family members participate in the ownership and operation of a business. Most states share the concept of related parties provided under the OECD Model Convention With respect To Taxes on Income and on Capital.¹⁶³ According to this convention, to be considered as related parties or associated enterprises, the same persons or parties are expected to participate directly or indirectly in the management, control or capital of both separated businesses.¹⁶⁴

¹⁵⁹ Ibid

¹⁶⁰ Uganda Revenue Authority "What is Value Added Tax (VAT)?"(2013-14)Vol.2,p.7
<https://www.ura.go.ug/Resources/.../INLB/Value%20Added%20Tax.compressed.pdf> last accessed on September 24,20016

¹⁶¹ See, Victor Thuronyi, cited above at note 40,p.17

¹⁶² See, Alan Schenk and Oliver Old man cited above at note 1,p.83

¹⁶³ Ibid

¹⁶⁴ Ibid

As a rule, every tax payer has the right to organize his/her/it's business as he/she/it likes. However, the choice of the organization of the businesses should be consistent with government laws in general and tax laws in particular. With regard to VAT registration purpose, the incorporation of the following yardsticks in the VAT laws of states is included to avoid artificial separation of businesses. These are, the separated businesses should have a unique trading relationships, they should show sufficient independence with respect to practical operation, bank accounts, any records and annual accounts and are being operated on an arm's length' basis.¹⁶⁵

2.8.4 Registration of Branches and Group of Companies

Due to different reasons, states such as UK allow group registration of companies in one hand and separate registration of branches in the other hand. In the cases where states allow group registration of companies, two or more companies or limited liability partnerships can register as a single taxable person.¹⁶⁶ In this case, a group is treated as a single taxable person registered for VAT on its own. The registration is made in the name of the “representative member”, who is responsible for completing and submitting a single VAT Return and making VAT payments or receiving VAT refunds on behalf of the group. All the members of the group remain jointly and severally liable for any VAT debts.¹⁶⁷ From the companies' side, group registration may allow the group offsetting of excess credits of companies against the VAT liability of the other companies in order to reduce the tax payable in that tax period.¹⁶⁸ From the tax authority side, it reduces the tax compliance costs of the tax authority.¹⁶⁹ For the implementation of group registration different states stipulated different requirements in their VAT laws. For instance in UK, to be registered in group, the registered company is required to fulfill the following requirements. These are, each body should have principal or registered office in the UK and the companies should be under common control, for example 1 or more company is a subsidiary of a parent company.¹⁷⁰ And If the turnover of the VAT group is over £10 million per year and the

¹⁶⁵ Id,185

¹⁶⁶ HM Revenue and Customs, Guidance VAT registration for groups, divisions and joint venture, (2004) <<https://www.gov.uk/guidance/vat-registration-for-groups-divisions-and-joint-ventures>> Last accessed on September 22,2016.

¹⁶⁷ Ibid

¹⁶⁸ See, Alan Schenk and Oliver Old man cited above at note 1,p.89

¹⁶⁹ See , HM Revenue and Customs cited at note 166

¹⁷⁰ Ibid

group is partly owned or managed by a third party, the company can only register as a group for VAT if, no more than 50% of benefits generated by the business go to third parties, the group uses consolidated accounting and no third party consolidates the group accounts.¹⁷¹ Besides imposing such obligations the UK VAT law also gives discretion for the group to increase additional members, remove members from the existing group, and changing the representative group and it can go to the extent of splitting the group with the obligation on the group to disclose the change.¹⁷²

Even though separate registration of branches increases VAT compliance costs of states, the lack of sufficient means of communications particularly in developing countries force to employ registration of branches and divisions.¹⁷³ In cases where business units or divisions are registered separately for VAT, each unit or division would have its own VAT registration number and each must account separately for VAT.¹⁷⁴ Even though each division would be VAT registered separately, the body corporate is still a single taxable person that remains liable for any VAT debts of all the divisions.¹⁷⁵ Writers recommend that branch or regional registration should not enable a business to come within the small business exemption.¹⁷⁶ This is also supported by countries experience. For instance in UK, to have divisional VAT registration, a body corporate should have two or more branches that carry out different functions or trade in different geographical areas; each branch should have its own independent accounting systems, all divisions should be registered, even those whose turnover does not exceed the VAT registration threshold, all divisions have the same tax periods for submitting their VAT Returns and the whole supplies of the body corporate should be fully taxable supplies.¹⁷⁷ In addition to these requirements, the combination of divisional and group registration is not permitted.¹⁷⁸

¹⁷¹ Ibid

¹⁷² Ibid

¹⁷³ See, Alan Schenk and Oliver Old man cited above at note 1, p.89

¹⁷⁴ Ibid

¹⁷⁵ Ibid

¹⁷⁶ See, Alan Schenk and Oliver Old man cited above at note 1, p.89

¹⁷⁷ See, HM Revenue and Customs cited at note 166

¹⁷⁸ Ibid

2.9 Cancellation of VAT Registration

Both compulsory and voluntary registrations for VAT has their own rationales as discussed above. But whenever these rationales are not properly achieved by the registered persons, the registered persons are cancelled from VAT registration either by the application of the registered person or by the initiation of the government.¹⁷⁹ The basic reasons that cause the cancellation of VAT registration are the following.

Most states cancel registration whenever the registered persons fail to meet the required threshold.¹⁸⁰ There are states such as Australia, which maintain the registration after that business' sales fall below the required threshold for the registration.¹⁸¹ In the cases where registration is canceled some or all of the input credits claimed on property held at that time must be repaid by the registered person.¹⁸² The other ground of cancellation of registration is the cessation of the business which is different from the failure to fulfill the required threshold. In the later case the business has the option to stay with voluntary registration as far as the registered persons wishes and the tax authorities permitted but in the previous case there is no option for the business to even exist.¹⁸³

Besides the above mentioned causes, registration can be cancelled whenever the person is registered by mistake at the time of registration.¹⁸⁴ This cause has retroactive effect.¹⁸⁵ The other worth mentioning issue regarding cancellation of registration is related with voluntary registration. In the case of voluntary registration some states may fix a minimum period for the business, such as two years, in order to ensure its continuity and make sure that it is not voluntarily registered in the first place just for the sake of obtaining VAT credits. In this case the registered person cannot bring the claim of cancellation before the lapse of such period.¹⁸⁶

¹⁷⁹ See, Victor Thuronyi, cited above at note 40,p.18

¹⁸⁰ Ibid

¹⁸¹ See, Alan Schenk and Oliver Old man cited above at note 1,p.87

¹⁸² See, Victor Thuronyi, cited above at note 40,p.20

¹⁸³ Ibid

¹⁸⁴ Ibid

¹⁸⁵ Ibid

¹⁸⁶ Ibid

Chapter Three

3. Issues and Problems Associated with Registration for VAT under the Ethiopian VAT Law

3.1. General Remarks

There are different issues and problems arising in relation to VAT registration by different group of persons in Ethiopia. Such issues include the (in)appropriateness of the threshold fixed by the VAT law, the determination of taxable persons, the problems associated with the process of determining whether the presumed tax payer meets the registration threshold or not, the determination of taxable supplies, issues related to cancellation of registered persons and handling of grievance related to VAT registration and cancellation. All these and related issues will be addressed under each sub topic of this chapter.

3.2 Taxable Persons

When we talk about tax registration in VAT regime, talking about taxable persons is a must because we cannot imagine registration without defining who taxable persons are. That is why any VAT regime, including the Ethiopian one, is concerned with taxable persons. The terminology “taxable persons” and “taxpayers” are employed interchangeably by different literatures. But, according to Victor Thuronyi, “taxable person” is the right terminology than “tax payers” to define persons who are obliged to be registered for VAT and hence who are required to discharge the VAT liability.¹ The reason provided by Victor Thuronyi is that the terminology taxpayer is relevant for the real persons who bear the final burden of taxation which is relevant for income tax purpose.²

The Ethiopian VAT Law, Proclamation No 285/2002 (, here after referred to VATP) has used the term “taxpayers” instead of “taxable persons”. Our VAT Proclamation has provided that the definition of taxpayers under Article 3 of the same. But, the administrative part of this proclamation is repealed and replaced by the Federal Tax Administration Proclamation,

¹ Victor Thuronyi , Tax Law Design and Drafting , International Monetary Fund(Victor Thuronyi, ed.1996,) Vol.1 Chapter 6,p.12

² Ibid

Proclamation No 983/2008 (here after referred to FFTAP.)³ According to the latter proclamation, for VAT purpose taxpayer is a person registered or who has the obligation to register for VAT.⁴ The definition provided by FFTAP seems narrow; but it refers to the obligation part. So, in one way or the other, it should be read in light of the VATP and the directive No 25/2001 which was issued by Ethiopian Revenues and Customs Authority. The meaning provided by FFTAP consists of three elements. These are person, registration and the obligation to register. Person may include an individual, a commercial business organization created in accordance with the Commercial Code of Ethiopia or under a foreign law, partnership, public enterprise or public financial agency of government, local government, or international organization.⁵ But, all these group of persons are not necessarily tax payers for VAT purpose. To be tax payer, these groups of persons should be either registered or required to be registered for the purpose of VAT.⁶ So, generally under the Ethiopian context to be considered as a taxable person for VAT purpose the basic requirement is registration. The requirements of registration and other issues related to registration will be covered in the coming discussion.

3.3 Taxable Supplies

As it is discussed in chapter two of this paper, the terms “taxable supply”, “taxable transactions” and “taxable activity” are used interchangeably by different literatures. The VATP as amended employed the term “taxable activity” and it is defined as an activity of supplying of goods or services by any person permanently or partially living in Ethiopia for another person for consideration.⁷ Taxable activities do not include exempted transactions.⁸ The basic pillars of this definition are; the supply of goods or service and consideration. According to the amendment proclamation, the supply can be carried out by any person and it is not expected to be on a regular base as well.

³ It is clearly provided that the non applicability of any laws which contradict with the matters covered by the TAP. See, Federal Tax Administration Proclamation, 2016, Art.138, Proclamation No. 983, **Federal Neg.GAZ.**year, 22 No 103.

⁴ Id, Article, 2(41)(b)

⁵ Id,Article,2(26)

⁶ Id, Article,2(41)(b)

⁷ Value Added Tax Proclamation, 2002, Art. 6, Proc. No .285, **Neg, Gaz.**, year 8, no. 23, as amended, Value Added Tax (Amendment) Proclamation, 2008, Art, 3, Proc. No. 609, Id., year 8, no. 6

⁸ See, the Detail of the Exempted transactions under Article 8 of Proclamation No. 285/2002 and under the relevant provisions of the regulation No 79/2002.

The other part of the definition is that the delivery of taxable supplies or service should be against payment or consideration.⁹ As it is discussed earlier the basic nature of VAT is that the delivery of the taxable activity should be followed by payment. Unless the delivery of the taxable activity is followed by payment, no value is added. If it is so, the supplier will not be under the obligation of VAT or the supplies are not considered as taxable supplies. The mode of payment can be in cash or it may be made in the form of goods or services in exchange for a supply of goods or a rendition of services.¹⁰ The important issues are; are supplies by tax payers without consideration excluded from the category of taxable activities or not? If those supplies are not excluded from the category of taxable supplies, how is the value of those supplies determined? Though the definition of taxable activities requires consideration it does not mean that the supplies which are supplied without consideration are excluded from the category of taxable activities except business samples.¹¹ Concerning the determination of the value of the supplies which are supplied without consideration and in the cases where the person receives or is entitled to receive goods or services in exchange for a supply of goods or a rendition of services, the value of the supply is determined by considering the market price of the goods or services supplied including any duty, taxes, or other fee payable, but without including VAT.¹² But, method of determining the market price and even the definition of market price is not provided both in the VATP and Regulation No 79/2002, here after referred to as VATR. Concerning the practical implementation of this issue or the valuation process, the writer of this paper asked a tax officer concerning the determination of the value of supplies which are supplied without consideration. He replied that the valuation process is made when the tax payers require exiting their business and in the cases where the taxpayer is suspected of evading tax by the tax authority and when ever sudden inventory is made. He added that whenever the taxpayers require closing their business the unsold goods are taken as sold and their values are determined by taking the average value of the price of the goods which are sold by the taxpayer before. This valuation

⁹ See, the Value Added Tax Proclamation Cited above at note7, Article 6.

¹⁰ Id, Article 12(2)

¹¹ Ibid, The Amharic version of Article 12(2) is silent on the exclusion of business samples. The writer tries to explore the issue by interview but no one is answered the practical applicability of the exclusion of business samples from the scope of taxable supplies.

¹² See, the Value Added Tax Proclamation Cited above at note 7, Article12(2)

method is not applicable to capital goods; it is governed by directive number 24/2001 which was issued by Ethiopia Revenue and Customs Authority.¹³

Does market price mean the price list provided by the tax payer? The newly proclaimed FFTAP provides the definition of market price and the points that should be considered in the process of determining the market prices. Accordingly, the fair market value shall be the amount determined by the Authority provided that it is consistent with generally accepted principles of valuation.¹⁴ In the process of determining market price, the value of any similar goods, asset, service, or benefit would ordinarily obtain at that specific time and place should be taken in to consideration.¹⁵ In addition to providing these points the FFTAP authorizes ERCA to issue directives for this purpose.¹⁶ So, according to the newly proclaimed FFTAP, the valuation process should rely on the general accepted principles of valuation. Since a taxable activity includes both supply of goods and supply of services, each supplies is going to be discussed in the following sub section of the paper.

3.3.1 Supply of Goods

To be registered as a taxable person the engagement on taxable activities is a mandatory requirement. We cannot talk about registration without defining the elements of taxable activates. These are supply of goods and supply of services. Accordingly Supply of goods is defined under Article 4 of the VATP as a sale of goods, granting uses right of goods and a transfer or provision of thermal or electrical energy, gas, or water.¹⁷ The first element of the definition of supply of goods includes a sale of goods that is the combination of sale and goods. The term sale is not defined by VATP and by any other tax laws of Ethiopia. But it is defined under Black's Law Dictionary as follows; it is the transfer of property or title for a price.¹⁸ Goods include all kinds of immovable with the exception of land and corporeal movable property with the exception of money such as, thermal or electrical energy, heat, gas,

¹³ Interview with Ato Solomon Aweke, Senior Investigating Auditor at ERCA No1 Medium Tax Payers Branch office, April 10, 2017.

¹⁴ The Federal Tax Administration Proclamation, Cited above at note 3, Article, 3.

¹⁵ Id, Article 3(4)

¹⁶ Id, Article(6)

¹⁷ Value Added Tax Proclamation ,2002,Art.4, Proclamation No 285, **Federal Neg. Gaz.**, Year 8, No 33

¹⁸ Bryan A. Garner, Black's law Dictionary(8thed.2004) , p.1364.

refrigeration, air conditioning, and water.¹⁹ So, for VAT purpose sale of goods means transfer of property or title of both movable and immovable property for consideration with exception of money and land. In addition to transferring property or title, supply of goods also includes the granting of use right of such goods such as a rental agreement, credit agreement, freight contract, agreement for charter, or any other agreement under which such use or right to use is granted or transfer or provision of thermal or electrical energy, gas, or water.²⁰

3.3.2 Supply of Services

As it is discussed under chapter two of this paper, best practices of VAT systems of different nations show that extensive tax base with minimal exemptions.²¹ This is achieved through inclusion of all supplies under the taxable activities of the VAT law.²² The VATP seems try to adhere to this approach since it defines supply of service as anything done which is not included under the supply of goods and money.²³ This includes granting, assigning, ceasing and surrendering of any right or facilitating situations for doing any advantages things.²⁴ This creates no room for supplies to escape from VAT.

3.3.3 Mixed Supply

As it is discussed earlier, mixed supply is a supply that contains both taxable and exempted supplies together.²⁵ For instance, a furniture seller may sale furniture and gives transport service for the delivery of the sold furniture to his/her/its customers. In this case the sale of the furniture is taxable supply but the transport service is an exempted supply. Unless the VAT law of a given country provides clear provisions which regulate the situations that taxable and exempted supplies are supplied together, it will be difficult to impose VAT on those supplies and giving VAT credit to the tax payers. For the purpose of avoiding such problems, the Ethiopian VATP tries to regulate such instances under article 5 of the same proclamation. This article tries to

¹⁹ Value Added Tax Proclamation Cited above at note 17, Article, 4(1)(3)

²⁰ Id, Article, 4(1)(2)

²¹ Ine Lejeune, *The EU VAT Experience: What Are the Lessons?* (2011), p.267 Available at <<http://www.taxanalysts.com/www/freefiles.nsf/Files/LEJEUNE-21.pdf/.../LEJEUNE-21.pdf>> last visited on August 23, 2016

²² Ibid

²³ Value Added Tax Proclamation Cited above at note 17, Article, 4(1)(b)

²⁴ Id, Article 4(b)(1)(2)

²⁵ <<https://www.linkedin.com/.../difference-between-composite-mixed-supply-ram-sunder..>> LASTED visited on September 15, 2016.

regulate supplies related to import and other supplies by separate sub articles.²⁶ Accordingly, the major yardsticks in both cases depend on by examining that whether one supply is subsidiary or incidental to the other supply. As far as the supply is subsidiary to the taxable supply, the total transaction is considered as taxable supply and the vice versa is true.²⁷ But in the cases where a taxable transaction involving independent elements, one or more of which involves the separate supply of goods or rendering of services, which would be exempt from tax, is treated as separate transactions.²⁸ As to an exempt transaction, which involves independent elements, separate supply of taxable goods or services, are treated separately.²⁹ The basic issue that can be raised relating to mixed supply is that the treatment of costs of business which is subjected to input tax. For instance, the taxpayer may supply both taxable and exempted supplies and collect VAT from the consumers when ever he/she/it supplies the taxable one. And deduct the VAT what he/she/it's paid in the process of purchasing taxable supplies, for managing both taxable and exempted supplies, and selling both the taxable and the exempted supplies and then pay the net VAT. The question is that how the tax credit is allocated in the cases where the tax payer supplies both supply and paid VAT for the purchase of taxable supplies and for the management of both supplies? Article 21(2) (c) of VATP empowers ERCA to issue the directive for the implementation of how the tax credit is determined in the cases where taxpayers supplied both taxable and exempted supplies. Accordingly directive No 20/2001 is issued by ERCA and this directive regulates this situations.³⁰ But the writer of this paper forwarded a question for the tax auditors how this situation is treated practically and all are responded that as no one implemented this directive and they explain that as they accept any tax credit as far as it is related with tax payers business without considering the allocation process of exempted supplies and taxable supplies.³¹

²⁶ Value Added Tax Proclamation Cited at note 17, article, 5

²⁷ Ibid

²⁸ Ibid

²⁹ Ibid

³⁰ This article regulates the allocation of tax credit paid related to mixed supply for detail analysis see, የኢትዮጵያ ገቢዎችና ጉሙሩክ ባለስልጣን ቅይጥ አቅርቦት እንዲሁም የካፒታል ግንባታ ሲከናወን የተከፈለን የተጨማሪ እሴት ታክስ ስለማቀናነስ የወጣ መመሪያ ቁጥር 20/2001 (unpublished)

³¹ Interview with Ato Solomon Aweke Cited at note 13 , and Interview with Ato Henoke Kebde senior Auditor at ERCA Addis Ketema Sub City Small Tax Payers Branch Office, April 11, 2017.

3.4. Registration of Taxable Persons for VAT

Generally, the newly proclaimed FFTAP imposes an obligation on persons who are liable for tax under a tax law to apply for registration unless the person is already registered.³² The FFTAP is applicable to all tax laws on the issues which are covered by it.³³ So, generally under the Ethiopia context all persons that have obligation under a tax law are identified through the system of registration. In addition, the new FFTAP defines tax payers for VAT purpose. According to this proclamation a taxpayer for the purpose of VAT is a person who is registered or required to register for VAT.³⁴ So, all tax payers in general and taxable persons for VAT in particular are identified through a system of registration in Ethiopia. For the purpose of identifying taxable persons for VAT, VATP recognizes two types of registration. These are mandatory and voluntary registrations.³⁵ Each type of registration and the pertinent issues are going to be discussed in detail.

3.4.1) Mandatory Registration

From the cumulative reading of article 16(1) (a) (b) of VATP, it is understandable that persons who carry on taxable activity and at the end of the year their annual turnover exceeds 500,000(five hundred thousand) Ethiopian Birr are obliged to register for VAT.³⁶ According to article 16(1) (b) of VATP, the required person is not necessarily expected to wait till the end of the year as far as there are reasonable grounds at beginning of the year that show the total value of taxable transactions is likely to exceed 500,000 (five hundred thousand) Ethiopian Birr. ³⁷ The basic requirements provided by article 16 of VATP are the engagement in taxable activities and the attainment of the annual turnover threshold that is 500,000(five hundred thousand) Ethiopian Birr. For the purpose of VAT registration, these two requirements should be fulfilled cumulatively. The basic issues raised related to the VAT registration requirements are:-

- 1) How are taxable activities determined practically in the process of registration?
- 2) Does the requirement of engaging in taxable activities include governmental bodies, religious organizations and other non commercial organizations?

³² See Federal Tax Administration Proclamation , Cited at note 3, Article,9

³³ Id, Article,138

³⁴ Id, Article,2(41)(b)

³⁵ See, Value Added Tax Proclamation, Cited above at note 17, Article 16 and 17.

³⁶ Id, Article ,16(1)(a)(b)

³⁷ Id, Article, 16(1)(b)

- 3) What was the base of the legislator when it fixed the 500,000 (five hundred thousand) Ethiopian Birr threshold? Was it appropriate?
- 4) How does the tax authority determine whether the taxable person has met the required threshold or not?
- 5) Why didn't the tax authority amend the threshold fixed in 2002?

As frequently discussed in this paper, taxable activity is defined as an activity of supplying of goods or services by any person permanently or partially living in Ethiopia for another person for consideration.³⁸ This definition in general provides how the taxable and exempted activities are categorized. The law is clear. From the beginning the terminology employed by the law is taxable. This implies that the activities which are exposed for VAT in the case of VAT registration.³⁹ But, in practice all tax assessors including all the auditors and the legal head of the tax authority are not in a position to distinguish taxable and exempted supplies in the process of VAT registration.⁴⁰ In practice the tax officers simply assess all transactions of the tax payer without excluding the exempted ones.⁴¹ In the interview conducted with different tax assessors of different sub city and at Woreda level, the writer of this paper found out that all tax assessors do not consider the nature of the supplies. Rather, all focus on annual turnover of the tax payer and all confirmed that as much as possible they try to encourage VAT registration rather than limiting the registration by considering the nature of the supplies.⁴² From the previous discussion, the intention of the legislator is very clear because it uses the terminology taxable supplies and it defines tax under article 2(20).⁴³ So, it is clear that only the taxable activities of the taxable person should be considered in the process of determining registration for VAT. The restriction of the registration of VAT on taxable supplies by the law may have its own justifications. For instance, it may consider the real capacity of the tax authority to administer tax payers and the capacity of the tax payers to keep book of accounts.⁴⁴

³⁸ Value Added Tax Proclamation, as Amended Cited at note 17, Article 6

³⁹ Ibid

⁴⁰, This interviewee is confirmed that the desire of the tax authority to register more persons rather than limiting the registration process by splitting the supplies. An Interview with Ato Belete Ahmed Legal Services Directorate Director at ERCA, Aprile,11,2017

⁴¹ Interview with Ato Solomon Aweke, Cited at above at note 13.

⁴² Interview with w/ro Traza Bekle at ERCA wereda 9 micro taxpayers Tax Payers Office Head, April,8,2017.

⁴³ Value Added Tax Proclamation Cited above at note, 17, Article,2(20).

⁴⁴ Clara K.Sullivan, The TAX on Value Added, Columbia, University Press(1965) p.230

The other issue raised in relation to taxable activities is that the terminology employed in the English version and in the Amharic version seems different. The terminology employed in the English version is that “taxable activities” while the terminology employed in the Amharic version is that “taxable business activities.” Does it mean that only taxable activities of traders are considered for the purpose of VAT registration? In other words, is the intention of the legislator to exclude taxable activities carried out by non traders for instance by the governments bodies, religious institutions and by any other non commercial organizations in the process of determining VAT registration? Though the terminology employed in the Amharic and the English version seem different, in both versions it is clearly provided that the profit motive of the supplier is not considered; rather, what matters is the supplies and the fulfillment of required threshold by law is achieved by the supplier. The VATP is restricted only on defining “business taxable activities” in the Amharic version and taxable activities in the English version. It does not define business. But the newly proclaimed Income Tax Proclamation here after referred as FITP defines business as follows:-

Business means any industrial, commercial, professional, or vocational activity conducted continuously or short term, but does not include the rendering of services as an employee or rental of buildings.⁴⁵

Besides this definition, , the Proclamation by making a cross reference to the commercial code embraces all activities of Private Limited Company and Share Company as a business except rental of buildings.⁴⁶ So, if we interpret the definition of “business taxable activities” in light of the definition of business provided by the FITP, it seems that it is not clear whether it includes such non commercial business organizations, religious institutions and governmental bodies or not. Under article 10(1) of the Commercial Code it is clearly provided that non commercial business organizations are considered as commercial business organizations if they are engaged in the activities provided by article 5 of the Commercial Code.⁴⁷ From the reading of article 10 (1) of the commercial code we can conclude that non commercial business organizations are considered as a business organizations if they are engaged in the commercial activities without considering their nature. We can safely conclude that the terminology taxable business activity

⁴⁵ Federal Income Tax Proclamation, 2016, Art. 2(2) Proclamation No. 979 **Federal. Neg. Gaz.** year 22, no.104

⁴⁶ Id, Article, 2(b)

⁴⁷ Commercial Code of Ethiopia, 1960 Art.10 (1), Proclamation No, 166 **Federal. Neg. Gaz.** year 19, no.3

does not exclude those non commercial business organizations as far as they are engaged in the commercial activities.

Though governmental bodies are not obliged to register as taxable person, they are required to register as with holding agents for VAT purpose in the process of purchasing taxable supplies.⁴⁸

The obligation of governmental bodies to withhold the VAT paid in the process of purchasing taxable supplies emanates from article 7(5) of proclamation No 609/2008. This article empowers the Ministry of Finance and Economic Development to issue directives for the execution of withholding the VAT paid by the governmental bodies. Accordingly, Directive No 27/2002 and its two subsequent amendments were issued by the then Ministry of Finance and Economic Development which is called Ministry of Finance and Economic Cooperation (here after referred to as MOFEC). According to this directive and its subsequent amendments, both the Federal and regional state offices, the city administration, governmental enterprises and any government bodies are obliged to withhold the VAT to be paid by them if the amount paid in the transaction exceeds the 5000.00 Birr including the VAT.⁴⁹ In case where the amount of transaction is less than 50,000 Ethiopian birr and greater than 5,000 Ethiopian Birr, the obligation of withholding the VAT is applicable even though the supplier is not VAT registered person.⁵⁰ But in the cases where the amount is 50000 and more the governmental body is obliged to purchase from VAT registered person and withhold the VAT.⁵¹ For the proper implementation of the withholding process, the directive requires the governmental bodies to register as with holding agent, having TIN number, issuance of receipt printed by the authorization of the tax authority, and reporting to the tax authority before the end of the next month starting from the day of the transaction occurred.⁵²

The other issue raised related to taxable business activities is that is rental of commercial buildings under the scope of VAT? The definition of business provided by the FITP clearly excludes the rental of the building. Besides the exclusion of rental of the building by the definition provided by FITP, it is not included under the list provided in article 5 of the

⁴⁸ Value Added Tax Proclamation as Amended cited above at note 7 Article,7(5)

⁴⁹ በኢትዮጵያ ፌዴራላዊ ዲሞክራሲያዊ ሪፑብሊክ የገንዘብና ኢኮኖሚ ልማት ሚኒስቴር በገገርው ተይዞ ስለሚከፈል የተጨማሪ እሴት ታክስ እፈፃፀም የወጣ መመሪያ ቁጠር 27/2002 እንደተሸሻለው አንቀጽ 5(unpublished)

⁵⁰ Id, Article 5(2)

⁵¹ Id, Article 5(1)

⁵² Id, Article 6

Commercial Code.⁵³ Does it mean the rental of the buildings is excluded from the business taxable activities for VAT registration? Practically, there are many religious institutions which earn significant amount of income from the rental of the buildings though they are not register for VAT.⁵⁴ What is the reason for their non- registration? Can they raise the explicit exclusion of rental of the building from the definition of the business under the FITP and the non inclusion of rental of the building under article 5 of the commercial code as a defense? As the technical note of the FITP clearly provides rental of the building is explicitly excluded from the definition of the business. The reason provided by the technical note prepared by the draftsman of the Proclamation to the exclusion of the rental of the building from the definition of the business is that the definition is provided for the purpose of the income tax and rental of the building is governed under schedule “B” of the FITP.⁵⁵ Concerning the non inclusion of rental of the building under article 5 of the CCE, the usual debate about article 5 of the CCE is raised. Though the original drafter of the Code was of the opinion that the list was sufficiently detailed enough to cover trade activities and should, therefore, be regarded as exhaustive, the opinion given by the fourteen national experts on the CCE is that the list should only be taken as indicative and not exhaustive in the face of an expanding economic transformation that is taking place in the country.⁵⁶ This team strengthens their argument by raising the nature and scope of trade activities that existed at the time of the promulgation of the Code is certainly far more limited than what exist forty eight years after its enactment. And the team suggests as the amendment of article 5 of the CCE as follows⁵⁷

“Without prejudice to other activities that are or may be characterized as trade activities by another law, persons who professionally and for gain carry out the following activities shall be deemed to be traders”.⁵⁸

Though the team suggests that the adoption of article 5 has to be open for other activities characterized as trade by another law, it is a mere suggestion until now and the above discussion has demonstrated that rental of the building is not a business in the eyes of the

⁵³ Sec, Commercial Code of Ethiopia Cited above at note 49, article 5

⁵⁴ Interview with one Informant April 11, 20017

⁵⁵ MoFEC, Federal Income Tax Proclamation Technical Notes, p3-4 (unpublished)

⁵⁶ A Team of Fourteen National Experts, Recommendations and Position paper of the business community on the Revision of the Commercial code of Ethiopia, (2008) Addis Ababa, Chamber of Commerce and Sectoral Associations. P. 7

⁵⁷ Ibid

⁵⁸ Id, p.8

Ethiopian laws. Besides these two legal instruments, according to the Amharic version of article 16 of the VATP, activities are business taxable activities. On the other hand, article 8(2) of the VATP clearly provides the list of exempted supplies. Among the list, the lease of dwelling houses is clearly provided under the list of exempted supplies in sub article “B” of the same article.⁵⁹ So, from the reading of article 8(2) (b) only houses which are served for residential purpose are exempted. In other words, the rental of the buildings other than the dwelling houses is under the scope of taxable activities. The basic issue raised here is that how can article 8(2) (b) of the VATP, on one hand and the exclusion of rental of the building by the CCE and the requirement of business taxable activities by article 16 of the VATP be reconciled on the other hand to make rental of the building under the subject of VAT? The current Ethiopian practices show that the Ethiopian Ministry of Trade (MOT) issues business license for the owner of the commercial buildings. Regarding this issue, the writer of this paper interviewed an officer of the MOT and for two private commercial building owners and the officer confirmed that business license is issued for the commercial building owners.⁶⁰ Besides the officer of the MOT, from the interview conducted with the two private commercial building owners confirmed that as they have business license for their commercial buildings and as they are registered for VAT.⁶¹ In addition to the officer of the MOT, an interview with the registration officer of the ERCA confirmed that the owners of the commercial buildings are registered as far as they meet the required threshold by law.⁶² The other issue rose relating to the rental of the buildings is that the buildings owned by the religious institutions. As it mentioned earlier, there are many religious institutions which owned commercial buildings and earn a significant amount of income from the rental of the buildings.⁶³ The writer of this paper made a survey to get such institutions and conduct an interview with the informant of such institutions who sought anonymity. Even though, the church collects a significant amount of money, it is not VAT registered yet.⁶⁴ Concerning this issue, the registration officer of ERCA responded there are some VAT registered religious institutions. For instance, the Ethiopian

⁵⁹ Federal Income Tax Proclamation, Cited above at note 45, Article 2(2)

⁶⁰ Value Added Tax Proclamation, Cited above at note, 17 Article 16 and 8(2)

⁶¹ Interview with Ato Haile Selassie Desta, Senior officer at Addis Ketema MOT Office, April 12,2017

⁶² Interview with Ato Mekebe Melka, owner of the building in Addis Ababa situated around Libu, , April 12,2017 and Ato Kamel Yesofe, Owner of the building In Addis Ababa situated around Merkato, April 12,2017

⁶³ Interview with one informant cited above at note 54

⁶⁴ Ibid

Catholic Church income generation project is VAT registered. However, he added, the authority is not in a position to make sure whether all the branches of the Church are registered or not. Besides, he did not deny the existence of the controversy between the tax authority and the religious institutions whether the situations are bound to be registered or not. The interviewee mentioned Tinsae Zegubae Printing Press which is owned by the Ethiopian Orthodox Tewahido Church. However the church resisted VAT registration on the ground that it provides a religious service.⁶⁵ Concerning this issue the officer of MOT responded that there many religious institutions which are engaged in the business activities without business license and they try to resist registration alleging that their activities are related with their religious services. He added that they are willing to pay tax though they are not willing to be registered. According to him, they justify their resistance alleging that there is contradiction between registrations for business and hence for VAT their primary goal- rendering religious services to their followers. This officer made it clear that the issue is controversial by now. Therefore, according to him, the head of the churches as applied to the main office of the MOT for non registration and the head office has given the direction to suspend the case temporally.⁶⁶ Our concern here is that failure to register religious institutions for VAT for reasons which do not hold water; is it not discriminatory among business men as far as the religious institutions are engaged in the taxable activities? Is it not creating a room for unfair competition? In the opinion of this writer, as long as they are engaged in the commercial activities they are obliged to register for VAT. This is without prejudice to the clear exemption of the religious or church related services under article 8(2) (e) of the VATP. But, the activities of religious organizations that compete with the private sector or that are not integral to the practice of the religion do not come within the exemption. Hence, if the annual turnovers of these taxable supplies exceed the threshold under Article 16 of the proclamation, the religious organization must be registered for VAT.⁶⁷ In Ethiopia, the problem is partly attributable to the fact that has not defined what religious or church related services are. In contradistinction to the stance of the Ethiopian VAT Law, some common law countries give some guidance concerning religious services. Therefore, according to their guidance to be considered as religious services and hence to be exempted from VAT, the services should be the integral part

⁶⁵ Interview with Ato Tensa Shelmo Registration officer of FRCA at Mesrak Addis Ababa branch, April 13,2017

⁶⁶ Interview with Ato Haile Selassie Desta Cited above at note 61

⁶⁷ Value Added Tax Proclamation, Cited above at note 17, article 16

of the religion, the supply should be service and the services should be provided free of charge, there should not be consideration paid in relation to the supply of that.⁶⁸

The other issue is the 500,000 (five hundred thousand) Ethiopian birr threshold. Concerning this issue, the writer of this paper put a question to Tax policy Directorate Coordinator of MOFEC as to why this threshold was fixed. He replied that no one knows about the base of such figure and he added that in most cases such type of cases is done by the recommendations of the World Bank and the International Monetary Fund on the basis of the result of the research of economists.⁶⁹

The other issue to be raised in relation to the requirements of VAT registration is about the method followed by the tax authority to determine the meeting of the required threshold by the tax payer. The writer of this paper put this question to different tax assessors at Wereda and sub-city levels, for different registration officers of the tax authority and to private tax professionals. All of them agreed that the mechanism of determining the annual turnover of the tax payer is that the book of accounts maintained by the taxpayer and by following the system of presumptive taxation.⁷⁰ And all agreed that article 48 of the previous Income Tax Proclamation and article 62 of the current Income Tax proclamation impose the obligation of keeping book of accounts on the category “A” and category” B” tax payers .Accordingly, categories of “A” and “B “ of tax payers are expected to declare their transaction on the bases of book of accounts.⁷¹ And they continued that the mechanism of employing book of accounts is relevant for tax payers who are registered for turnover tax and at the end of the year they may graduate to VAT.

Concerning the mechanism of presumptive taxation the tax authority employed this system to determine the annual turnover of small tax payers and whenever the book of accounts of the taxpayer is not acceptable by the tax authority or in the cases where the tax payer fails to

⁶⁸ GST Hand Book, Exemptions for Churches. Available <www.youraccountant.net.au/tguide/guide/GSThbook/GST05020> last accessed date April 10,2017

⁶⁹ Interview with A to Berhanu Tadesse, at MOFEC Senior Legal expert, April,13,2017

⁷⁰ Interview with Ato Solomon Aweke cited above at note 13 and Interview with Ato Fekadu Serage private Tax accountant ,April 12,2007

⁷¹ Ibid

discharge the obligation of keeping book of accounts.⁷² In these cases the tax assessors of the tax authority estimate the annual turnover of the tax payers. The bases of assessing annual turnover of tax are the organization, the location of the business premises and the turnover of other competent business. He did not deny that in most cases all tax assessment is made by fresh staff members. Besides this, he did not deny the interest of the tax authority to register more and more persons for VAT. According to the other informant, tax assessment is made by the recommendation of the intelligence department of the authority and by the private individuals who give information to the tax authority about the tax payers. In this case, the intelligence department of the authority may gather information about the tax payers and suggest registering of a group of tax payers who are living in the same area or private individuals. According to this informant, the reason is that whenever the information is sent from the intelligence department of the tax authority the tax assessors do not freely assess the turnover of the tax payer; rather they try to execute the order of the intelligence department of the tax authority by simply gathering shallow information.⁷³ The other information comes from neighboring business people who tip the tax authority about other business persons who are engaged in similar business activities with them. In this case, the tax authority simply registers such persons without properly considering the turnover of such tax payers.⁷⁴ All the tax assessors and the Director of the legal department of ERCA confirmed that VAT registration is done on the bases of avoiding unfair competition among the tax payers who are engaged in the same sector.⁷⁵ Concerning such issues the private tax professionals interviewed by the writer of this paper confirmed that the tax assessors appointed by the tax authority are exposed highly to the lack of experience; they fear the order of their superiors and most of the assessors are as fresh graduates.⁷⁶

Basically, the system of presumptive taxation is exercised in the entire world.⁷⁷ But, it is applicable on the small business and exceptionally applied on the large tax payers.⁷⁸ The

⁷² Interview with Ato Heno Kebede cited at note 31

⁷³ Ibid

⁷⁴ Interview with Ato Solomon Aweke, Cited above at note 13

⁷⁵ Interview with Belete Ahmed cited above at note 40, and Interview with Ato Solomon Aweke cited above at note 13.

⁷⁶ Interview with Ato Tofike Ahmed , private Tax Accountant March,30,2017

⁷⁷ See, Victor Thuronyi , Tax Law Design and Drafting , International Monetary Fund(Victor Thuronyi, ed.1996,) Vol.1 Chapter 12,p.2

experience of some developed countries shows that in the process of determining tax liability, the tax authorities are usually authorized to assess the tax liability based on their best judgment rules.⁷⁹ They also employ different methods such as net worth, bank deposits, and some other approaches that have a factual basis for the particular case. As much as possible they try to depend on the factual basis for the particular case.⁸⁰ When we evaluate the Ethiopian case based on the above discussions, the method followed by the tax authority seems arbitrary. This is because the tax assessors are not professionals on tax assessment; they did not have any special training on the techniques of tax assessment and there is no a guideline which is prepared by the tax authority which should be followed by the tax assessors. These and other reasons make the assessment system arbitrary. If it is arbitrary from the beginning, it imposes unnecessary burden on the tax authority by registering non qualified tax payers which has its own impact both on the tax payer and on the tax authority. The problem associated with back registration is a good case in point that highlights the weak administration of the tax authority.⁸¹ For the tax authority, it may increase the administrative cost and it decreases the quality of the service given by the tax authority. According to this informant, the basic cause of this problem is lack of code of conduct to regulate the mistake of the tax officers and the imbalance of the work load and the tax officers. The existence of this problem is confirmed by interviews made with private tax professionals.⁸²

As it is discussed earlier, the required threshold for VAT registration when the annual turnover exceeds 500,000 (five hundred thousand) Ethiopian Birr though MOFEC is empowered to increase or decrease this threshold. However, this threshold has not been amended yet since 2002. The writer of this paper raised this issue to the Tax policy Directorate Coordinator of MOFEC. He replied that the increasing or decreasing of the registration threshold is a policy issue and as his office is established for the purpose of conducting research on tax policy issues. The issue is at the research level by the fund provided by DFID (Department for

⁷⁸ Id,5

⁷⁹ Id,8

⁸⁰ Id,9

⁸¹ Interview with Akreme Kemale a senior Registration officer at ERCA Addis Ketema Sub City lower Tax Payers Branch Office March 30,2017

⁸² Interview with Ato Yohanse Kedne Maryame , Private Tax Accountant ,March 30,2017

International Development) and the input is expected from the ERCA.⁸³ The Director of the Legal Department of the ERCA has the opinion that the increment of the threshold is not required at this time for Ethiopia. According to this informant, the ERCA is required to increase the tax base by increasing the VAT registered persons. If the tax law increases the registration threshold it may create a room for tax payers to escape from VAT registration and he concluded that nothing would be wrong if all tax payers are registered for VAT. He further maintained that as far as the capacity of the tax authority is good and as far as the tax authority is capable enough to administer the tax payers, it is better to decrease the registration threshold than increase it.⁸⁴

According to the recommendation of the International Monetary Fund (IMF) high threshold is preferred in the process of mandatory VAT registration than the lower one.⁸⁵ The purpose of the recommendation seems to decrease the administrative burden of the tax authority by exempting those tax payers who are below the required threshold by law and to make free small tax payers from the burden of keeping books of accounts. Besides the IMF's recommendation, state practices show that lower threshold is the cause of the collapse of a VAT system.⁸⁶ Though it seems difficult to conclude that the threshold fixed by the legislator during the enactment of the VATP is high or low, by now it will not be difficult to conclude that as the threshold is low. The data provided by the Central Statistical Agency of Ethiopia shows that the inflation rate in Ethiopian has by average increased at a 16.65% per year from 2006 G.C to 2016 G.C.⁸⁷ Based on this data the 500,000ETB in 2006 is approximately equivalent to 2720834.87ETB in 2016. In other words, the current Ethiopian VAT registration threshold should be 2720834.87 ETB. This figure may not be necessarily the accurate figure but it is employed to indicate the amount of the money affected by the average inflation rate during such years. The following table shows the amount of money affected by the average inflation rate and the estimated amount of the threshold after the effect of the average inflation rate during 2006G.Cto 2016G.C.

⁸³ Interview with Ato Berhanu Tadesse Cited above at note 69

⁸⁴ Interview with Ato Belete Ahmed cited above at note 40

⁸⁵ Ine Lejeune, *The EU VAT Experience: What Are the Lessons?* (2011) , p.267 Available at <<http://www.taxanalysts.com/www/freefiles.nsf/Files/LEJEUNE-21.pdf/.../LEJEUNE-21.pdf>> last visited on August 23, 2016

⁸⁶ Jean-Paul Bodin and Vincent Koukpaizan, "The Rise of VAT in Africa – Impact and Challenges"(2009) p.183

⁸⁷ <www.TRADINGECONOMICS.COM/CENTRALSTATISTICALAGENCYOFETHIOPIA> last accessed date on March 15, 2017.

Year	Initial threshold (ETB)	Average inflation rate %	The amount of money affected by the inflation rate (ETB)	The Estimated amount of the threshold after the effect of the average inflation rate (ETB)
2006	500000.00	16.65%	83250.00	583250.00
2007	583250.00	16.65%	97111.13	680361.13
2008	680361.13	16.65%	113280.13	793641.26
2009	793641.26	16.65%	132141.27	925782.53
2010	925782.53	16.65%	154142.80	1079925.32
2011	1079925.32	16.65%	179807.57	1259732.89
2012	1259732.89	16.65%	209745.53	1469478.42
2013	1469478.42	16.65%	244668.16	1714146.58
2014	1714146.58	16.65%	285405.40	1999551.98
2015	1999551.98	16.65%	332925.40	2332477.39
2016	2332477.39	16.65%	388357.48	2720834.87

Table1. This Table Shows the Estimated amount of threshold after the effect of the average inflation rate.⁸⁸

Countries' experience also showed that for the proper implementation of the VAT law, future possible inflation rate is considered by the VAT law and accordingly the threshold should be amended. For instance, in UK, the VAT registration threshold in 2015/16 was £82000 and for 2016/17 is £85000.⁸⁹ Besides the inflation rate, the administrative capacity of the tax authority should be considered to increase or decrease the VAT registration threshold. As we know, the administration of tax payers is started from registration to the final audit. If the tax authority has more VAT registered taxpayers, it should have more trained tax officers; it should enforce the law properly; it should audit the tax payers on time; it should register all persons who meet the required threshold by law and other administrative works should be done properly. The previous dissections are the good indicators as the tax authority is not capable enough to administer the

⁸⁸ Despite, the threshold is fixed in 2002, the calculation started from 2006. This is because the average inflation rate availed by the authority is during this years and to make the discussion easy and reliable the writer of this paper follows this approach.

⁸⁹ <<https://www.cchdaily.co.uk/budget-2017-vat-registration-threshold-rises-ps85k>> Last accessed on September 20, 2016.

tax payers properly. So, it is better to tax authority to focus on the selected tax payers than registering more tax payers and imposing additional work load on it.

Besides the VATP, the obligation to be registered for VAT is regulated by the aforementioned VAT registration directive. According to this directive, persons who are engaged in sale of gold, sale of electronics such as sale of refrigerator, TV and the like, importers, traders engaged in plastic business, shoe factories, contractors from level 1-9, traders engaged in sale of computers and computer accessories, and traders engaged in sale and preparation of leather products are obliged to register for VAT.⁹⁰ As mentioned earlier, this directive was issued by the ERCA. According to the power declaration clause of the directive, the delegated power of ERCA to issue this directive emanates from article 16(6), and article 18(8) of the VATP and article 39 of the VAT Regulation. When we examine the contents of these articles, they empower the ERCA to issue directives which assist for the proper implementation of the VATP and the VATR. This means that the ERCA is empowered to issue directives on procedural matters. But, the VATRD imposes an obligation on persons who are under the list of the VATRD. Does ERCA have the power to issue such a directive? Concerning this issue the Director of legal department of the ERCA replied that the issuance of directive which imposes the obligation of VAT registration on sector base is within the scope of the power delegated by the legislator to ERCA. It is thus based on the delegated power that that ERCA for the purpose of simplicity categorizes some sectors that their annual turnover is not less than the required threshold by law.⁹¹

Besides this directive, according to one informant the ERCA has also categorized some sectors for instance small cafeterias to be under the scope of mandatory VAT registration by circulars issued by the authority.⁹² Taxation should have legal base or it should be compatible with the principle of legality of taxation. According to this principle tax should be imposed on the bases of law. This principle goes to the extent of limiting the power of delegation of the legislator to other bodies of the government. In Ethiopian this principle is recognized under article 10(1) of the Federal Government financial administration law⁹³ As it is discussed earlier, the content of

⁹⁰የኢትዮጵያ ገቢዎችና ጉሙሩክ ባለስልጣን ለተጨማሪ እሴት ታክስ ስለመመዘገብ የወጣ መመሪያ ቁጥር 25/2001 አንቀጽ 4(3) (Unpublished)

⁹¹Interview with Belete Ahmed cited above at note 40

⁹² Interview with Akreme Kemale, Cited above at note 81.

⁹³ Tadesse Lencho, "The Ethiopian Tax System :Excesses and Gaps" Michigan State International Law Review, Vol.20,no,2(2012) p.336

article 16(6) and article 18(1) of the VATP and article 18(1) of the VATR clearly empowers the ERCA to issue directive on procedural matters but the authority issues VATRD which imposes an obligation of registration on a sector base. Though ERCA is empowered to impose tax on tax payers it does not mean that it imposes an obligation on tax payers which are not incorporated under the VATP. Such act of ERCA is ultra virus.

3.5.2) Voluntary Registration

The other type of registration provided by the VATP is voluntary registration. Those tax payers who are engaged in the taxable activity and do not meet the required threshold by law may register for VAT voluntarily. Nevertheless, the system of voluntary registration is not open for all tax payers. To register for VAT on a voluntary basis, the tax payer should supply or render at least 75% of his goods and services to a registered person regularly.⁹⁴ In addition to this requirement, the applicant is expected to keep proper book of accounts, submit regular and reliable tax returns, and have a permanent place of business and bank account.⁹⁵ Why are such requirements provided by law for voluntary registration in Ethiopia? According to article 21(1) of the VATP, only registered persons are entitled to tax credit for those taxes paid during purchase of raw materials or input taxes. So, taxpayers by registering voluntarily shall be entitled to get credits.⁹⁶ These may create a room for those who are not in reality engaged in business to register with a view to claiming rebates of input tax when they have no real intention of paying much output tax to the government. In addition to this, it may have the effect of making many more persons than is administratively viable. To protect the adverse effect of voluntary VAT registration, the law has stipulated such rigorous requirements on voluntary VAT registration. Is it practically implemented under the Ethiopian context? The practice on the ground shows that those who apply for voluntary registration are registered by simply signing an application that confirms they supply at least 75% of their goods and/or services to registered person.⁹⁷

He added that except providing such application form there is no system which insures for what purpose person is actually registered. Nor is there any follow up whether the registered person is

⁹⁴ Value Added Tax Proclamation Cited above at note 17, Article, 17

⁹⁵ የኢትዮጵያ ገቢዎችና ጉሙሩክ ባለስልጣን ለተጨማሪ እሴት ታክስ ስለመመዘን የወጣ መመሪያ ቁጥር 25/2001 አንቀጽ 3(4) (Unpublished)

⁹⁶ Id, Article 21(1)

⁹⁷ Interview with Ato Solomon Aweke, cited above at note 13

doing according to the declaration he made. Why isn't the practice in accordance with the law? The informant replied to this question that the tax authority has high interest to register more persons for VAT. However, this writer believes that the stance of the tax authority is not useful because, as discussed earlier, the registration of more and more person cannot be administratively viable for the tax authority and may create a room for those tax payers who need to rebate the VAT paid on their capital goods. So, allowing voluntary registration without designing a system controlling mechanism of whether the registered person is doing according to the requirement of the law or not may have destructive effect for the tax authority than increasing the revenue to the tax authority.

3.5.3) Registration of Related Persons

Registration of related persons is incorporated in different nations VAT law. This is done for the purpose of controlling business owners who attempt to avoid VAT registration by splitting the business into separate parts.⁹⁸ The VATP and VATRD have also incorporated the separate registration of related persons under article 16(7) (a) of the same proclamation and article 5 of VATRD respectively. These articles empower the tax authority to aggregate the value of taxable transactions made by related persons and register for VAT each person separately, even though the taxable transaction of a single person does not meet the required threshold by law.⁹⁹ The issue at hand is who are related persons under the Ethiopia law? Is registration of related persons practically implemented under the Ethiopian context? The definition of related persons is provided under article 4 of the FTAP. Accordingly, it defines based on the general requirements to determine related persons and based on the blood, marriage and legal relationships for natural persons and based on business relationship for bodies. Accordingly, to persons to be considered as related person, one person may reasonably be expected to act in accordance with the directions, request, suggestions, or wishes of the other person, or both persons may reasonably be expected to act in accordance with the directions, request, suggestions, or wishes of a third person.¹⁰⁰ Besides this general requirements, for natural persons unless the tax authority satisfied that one person is not under directions, request, suggestions, or wishes of the other person, the

⁹⁸ Alan Schenk and Oliver Old Man Value Added Tax a Comparative Approach with Materials and Cases, Cambridge University Press,(2007)p.83

⁹⁹ የኢትዮጵያ ገቢዎችና ጉሙሩክ ባለስልጣን ለተጨማሪ እሴት ታክስ ስለመመዘገብ የወጣ መመሪያ ቁጥር 25/2001 አንቀጽ 5 (Unpublished)

¹⁰⁰ Federal Tax Administration Proclamation Cited above at note 3,Article,4

relative of the person is considered as related persons. For the purpose of this definition relative includes, the spouse who legally married for the first mentioned individual or an individual who lives in an irregular union with first mentioned individual, an ancestor, lineal descendant, brother, sister, uncle, aunt, nephew, niece, stepfather, stepmother, or adopted child of the individual, a parent of the adoptive child of the individual, a spouse of an ancestor, lineal descendant, brother, sister, uncle, aunt, nephew, niece, stepfather, stepmother, or adopted child of the individual. For bodies to determine the issue of related persons, the definition provided by the FTAP depends on the voting power, the amount of dividend earned by share holders or the capital contribution of the member of the body or to other related body. Accordingly article 4(b) (c) of the FTAP, as far as the member of the body or other body has 25% and more of voting rights, capital contributions or has earned dividend from the bodies, the two persons are considered as related persons.

To ensure whether the registration of related persons is practically implemented or not, the writer of this paper put a question to the registration officer of the tax authority as to how the registration of related persons is implemented. He revealed the non existence of any system of registration of related persons except the VAT registered person is expected to include the name of his /her spouse in the application form. He added that though the VAT registered persons are required to include the name of their spouses in the application form, there is no mechanism of creating a link to whether the spouse of registered person is a tax payer or not.¹⁰¹ Concerning this issue, the head of the Legal Department of ERCA has the view that registration of related persons is not significant. He also underscored that registration of related persons under the Ethiopian context is not practically possible.¹⁰²

3.5.4) Divisional Registration

Though separate registration increases the compliance cost of states, to simplify the obligation of the taxpayer, states allow divisional registration as a matter of exception.¹⁰³ Like VAT laws of other states, the Ethiopian VATP has incorporated the system of divisional registration under

¹⁰¹ Interview with Ato Solomon Aweke, cited above at note 13

¹⁰² Interview with Belete Ahmed cited above at note 40

¹⁰³ See, Alan Schenk and Oliver Old Man, Cited above at note 98,p.89

article 16(4) (5) of the same proclamation.¹⁰⁴ In addition to the VATP, the VATR and VATRD have also contained provisions which regulate the divisional registration under the Ethiopia context. Accordingly, article 16(4) of the Proclamation clearly provides that the initiation of requesting the divisional registration should come from the tax payers through formal a written application¹⁰⁵ which includes the applicant's taxpayer identification number and VAT certificate number.¹⁰⁶ The registered person must file a separate application for each division seeking separate registration on the form and containing the information required by the Authority.¹⁰⁷

In the case of a person that is to be registered for the first time, such person can submit an application for registration and an application for divisional registration at the same time.¹⁰⁸ The submission of the written application by the taxpayer does not suffice. Rather, the applicant should prove that submitting a single return for its entire business operations is the cause for an onerous compliance burden for it.¹⁰⁹ Besides this, the applicant is expected to explain in detail the problems likely to be countered if divisional registration is not granted and the reasons why a consolidated VAT return for the entire business for each accounting period cannot be submitted by the due date for each tax period.¹¹⁰

When the application of divisional registration is submitted by the applicant, the tax authority should prove the fulfillment of the conditions provided under the VATP, VATR and VATRD before granting the divisional registration. These legal instruments require the applicant to conduct its operation as an incorporated company and to be a registered person for VAT purposes. But voluntarily registered persons are excluded from divisional registration. The division for which separate registration is requested must be separately identified by reference to the nature of its activities or its location.¹¹¹ Furthermore, the division or the branch should be

¹⁰⁴Value Added Tax Proclamation, cited above at note 17, Article,16(4)(5)

¹⁰⁵ Id, Article 16(4)

¹⁰⁶ Council of Ministers Value Added Tax Regulations, 2002, Art.9 (9)(b),Regulation No 79. **Federal Neg.Gaz.**, Year 1, No 19

¹⁰⁷ Ibid

¹⁰⁸ Id ,Article 9(11)

¹⁰⁹ Id, Article 9(9)(d)

¹¹⁰ Id,Article9(9)(e)

¹¹¹ Id, Article 9(9)

100k.m away from the head office.¹¹² The applicant must already be preparing divisional accounts before consolidating them¹¹³, besides checking the fulfillment of these conditions, the VATP authorizes the tax authority to impose additional conditions which are deemed necessary before approving an application for divisional registration, or may impose different conditions on a newly registering entity.¹¹⁴

As to the practical enforcement of the divisional registration, as far as the applicant met the requirements provided under the VATRD, the application is accepted and the division is registered separately. For the purpose of identifying the branches the tax authority issues sub TIN and create divisional accounts.¹¹⁵

3.5.5) Cancellation of Registration

Registered taxpayers may seek to exit from the VAT regime for various reasons. The process of getting exiting from a VAT system is called cancellation or deregistration. Cancellation of registration is not made in the sole interest of the taxpayers; rather, it needs regulation. Under the Ethiopia context, it is regulated by VATP, VATR and by directive No 24/2001 which is issued by ERCA for the purpose of calculating the value of unsold goods while the application for cancellation of the registration is approved.

According to article 19 of the VATP, the basic grounds for the cancellation of VAT registration are the cessation of taxable activities by the tax payer and the reduction of the tax payers' transaction below the required threshold by the law.¹¹⁶ Both grounds of cancellation of registration are the cessation of the requirements of mandatory registration.¹¹⁷ In other words, the cancellation of registration is granted whenever the requirements for the mandatory VAT registration cease to exist. The law does not say anything about whether the failure of the previously fulfilled requirements for voluntary registration is the ground of cancellation or not. Can't voluntarily registered persons cancelled from VAT registration? Concerning this issue, the law is silent. Practically, as discussed below the practice only considers the termination of the

¹¹² የኢትዮጵያ ገቢዎችና ጉሙሩክ ባለስልጣን ለተጨማሪ እሴት ታክስ ስለመመዘገብ የወጣ መመሪያ ቁጥር 25/2001 አንቀጽ 6(2)(ረ) (Unpublished)

¹¹³ Id,አንቀጽ 6(2)(ለ)

¹¹⁴ Council of Ministers Value Added Tax Regulations Cited at note 106,Article 9(10)

¹¹⁵ Interview with Ato Tensa Shelmo Cited above at note 65

¹¹⁶ Value Added Tax Proclamation Cited above at note 17, Article 19

¹¹⁷ See, The Mandatory registration requirements Provided Under article 16 of the Value Added Proclamation.

business rather than the examining whether the law provides any requirements or not.¹¹⁸ Article 19 of the VATP says that “ceased to make taxable transaction.” What does cessation mean? Does it mean the exit of the business? Or does it include the shift of taxpayers business to exempt transactions? As it is discussed frequently taxable activities or taxable transactions mean in short the engagement of registered persons on the supplies of goods and services which are exposed for VAT or engaging in the supplies of goods and services which are out of the list of exempted supplies under article 8 of the VATP.¹¹⁹ Besides this, article 8 of the VATP clearly provides the exempted transactions. In the cases where a person engaged in the activities listed down under article 8 of the VATP the law does not impose the obligation of registration.¹²⁰ So, the cessation of taxable activities includes both the stoppage of the business by the registered person and the shift of the registered person from supplying taxable transactions to the supply of exempted transactions. In this case, the registered person is required to apply for cancellation of registration within 30 days of the date the person ceases to make taxable transactions. The application of the registered person shall be in writing, shall state the date upon which the person ceased to make taxable transactions, and shall state whether or not that person intends to make taxable transactions within 12 months from that date. The application submitted by the registered person will be approved if the authority is satisfied that the person will not make taxable transactions at any time within 12 months from the date of cessation. If not it will be rejected.¹²¹

The cancellation of registration on the grounds of cessation of taxable activities may be effected from the date of the cessation of the taxable activities or from the date of the registration if the tax authority is satisfied that the registered person did not make taxable transactions from the date the registration.¹²²

Concerning the practical implementation of cancellation of registration by the reason of cessation of taxable supplies, the writer of this paper put as question to the registration officer of ERCA and he replied that cancellation of registration is not granted unless the business is terminated.¹²³ This view is also supported the tax professionals. Accordingly, cancellation of registration is

¹¹⁸ Interview with Ato Solomon , cited above at note 13

¹¹⁹ Value Added Tax Proclamation, Cited above at note 17, Article 6

¹²⁰ Id, Article 8

¹²¹ Id, Article 19

¹²² Ibid

¹²³ Interview with Interview with Akreme Kemale, cited at note 81

unthinkable unless the business is totally closed, and the tax payers are discouraged by the tax authority from claiming cancellation for registration.¹²⁴

The other ground for the cancellation of VAT registration is the reduction of the annual turnover of registered person below the required threshold by law. However, in order to successfully get his registration cancelled, the annual turnover of the registered person must remain below the required threshold for three consecutive years. The cancellation of the registration on the ground of the reduction of the annual turnover is effected starting from the end of the accounting period starting from the date of the application for cancellation by the registered person.¹²⁵ Cancellation of registration due to the reduction of the required threshold is not practically implemented. This confirmed by the interview conducted with the registration officer of the ERCA and by the private tax professionals. According to these informants, the tax authority is not willing even to accept the application of cancellation of registration unless the business person totally terminates his/her/ its business. The refusal of the authority to cancel the registration has become a basic fear of businessmen.¹²⁶

Cancellation of registration has two basic effects. These are the removal of the registered person's name and other details from the VAT register and the imposition of payment of VAT for the unsold goods by the previously registered persons.¹²⁷

3.5.6) Handling of Grievances Related to VAT Registration and Cancellation.

Dispute is natural in any transaction in general and in the case of taxation in particular. Generally, in taxation there are two contradictory interests that can be the main cause for disputes between the tax authority and the tax payers. These are the interest of the tax authority to increase the revenue of the government by broadly interpreting the tax laws in one hand and the interest of the tax payers to escape the tax obligation by narrowly construing the tax laws on the other hands.¹²⁸ This is true in relation to any tax in general and in VAT in particular.

¹²⁴ Interview with Ato Fekadu Serage Cited above at note 70

¹²⁵ Value Added Tax Proclamation Cited above at note 17, article 19(2)

¹²⁶ Interview with Akreme Kemale, cited at note 81 and Interview with Ato Fekadu Serage Cited above at note 70

¹²⁷ Value added Tax Proclamation Cited at note 17, article 19(4) and Value Added Regulations Cited above at 106, Article 10(5)

¹²⁸ አሰቻለው አሻግሬ, “የታክስ ከፋዮች ቅሬታ አፈታት ሥርዓት በኢትዮጵያ” MIZAN LAW REVIEW, Vol. 8, No.1,(2014) p.201

This research has attempted to appreciate complaints pertaining to VAT registration and cancellation. In the course of doing this research, the researcher realized that the complaints of tax payers related to VAT registration and cancellation.¹²⁹ Such complaints include, the arbitrary determination the turnover of the business men to register for VAT, the inclusion of exempted supplies in the course of determining the annual turnover of the business men, the unfair registration of small businesses for VAT, the retrospective VAT registration, and the rejection of the application of tax payers related to cancellation are the basic ones.¹³⁰ The issue, however, is whether or not complaint handling mechanisms have put in place in Ethiopia with regard to registration and deregistration of VAT.

Both the VATP and the FTAP have incorporated procedure of appeal under section ten, article 40ff and part nine, article 53ff respectively.¹³¹ Accordingly, the VATP establishes three appeal procedures for those who are dissatisfied by the decision of the tax authority. These are the review committee, Tax appeal commission and ordinary courts.¹³² According to article 41(2) of the VATP, the aggrieved party has the right to appear before the review committee within ten days of receipt of tax assessment notification.¹³³ The reading of this article clearly indicates that the jurisdiction of the review committee is limited to hear cases related to tax assessment only. Besides this, article 41(1) clearly provides that the jurisdiction of the review committee as on the issues related to tax assessment, penalty and interest.¹³⁴ If the party is dissatisfied with the decision of the committee with issue mentioned, he has the right to appeal to tax appeal commission within 30 days from the date of decision of the committee or from the date of receipt of the tax assessment notification.¹³⁵ Concerning the next appeal article 43(4) of the VATP cross refer to Proclamation No 286/2002 that the provisions of the Income Tax Proclamation, concerning appeals shall, mutatis mutandis, apply to appeals regarding taxes imposed by this proclamation.¹³⁶ Regarding this issue article 112 of proclamation No 286/2002 clearly provides

¹²⁹ Interview with Ato Akreme Kemale, cited at note 81 and Interview with Ato Fekadu Serage Cited above at note 70. Both these interviewees and others confirmed that the seriousness of the grievances raised by the tax payers related to registration and cancellation.

¹³⁰ Ibid

¹³¹ See, Value Added Tax Proclamation Cited above at note 17 ,Article 40ff and Federal Tax Administration Proclamation cited at note 3 Article53ff

¹³² See, Value Added Tax Proclamation Cited above at note 17, Article 40ff

¹³³ Id, Article 41(2)

¹³⁴ Id, Article 41(1)

¹³⁵ Id, Article

¹³⁶ Income Tax Proclamation, 2002, Art.112Proclamation No. 286, **Federal Neg. GAZ.**, Year 8, No 34

that as any aggrieved party with the decision of the appeal Commission may appeal to the competent court on any matter of law within 30 days from the date of receipt of the written decision of the Appeal Commission.¹³⁷ This article limits the grounds of appeal on the matter of law only.¹³⁸ On the other hands the FTAP is also provides similar appeal procedure to the previous income tax law. That is the jurisdiction of the committee is on the issues related to tax assessment and the tax appeal committee has the appellate jurisdiction on the issues heard by the committee .The jurisdiction of the court is also limited to hear cases which has legal issues only.¹³⁹

In both legal instruments, there is no clear provision which expresses about the institutional frame works and the procedures of grievance handling related to VAT registration and cancellation. If there is no apparent provision which treats dissatisfactions related to VAT registration and cancellation, what will be the fate of tax payers who are dissatisfied by registration and the cancellation processes? Concerning this issue, the practice of different branch offices of the tax authority is not uniform. For instance, the writer of this paper understood from the interview conducted with the legal head of the ERCA that as the authority hasn't any legal power to handle grievances related to VAT registration and cancellation. He recalled that the power of the review committee provided that under the VAT proclamation as the authority hasn't any power for the issue at hand.¹⁴⁰ On the other hand, the writer of this paper understood that there are other branch offices of the ERCA resolving such issues by the review committee.¹⁴¹ Such discriminatory approach is not acceptable in the opinion of this writer. Hence, what should the remedy be?

Article 37 of The FDRE (Federal Democratic Republic of Ethiopia) Constitution clearly provides that everyone has the right to bring a justiciable matter to the court of law to get a decision.¹⁴² Is the grievances related to registration and cancellation of VAT a justiciable matter? Is it appropriate to bring such cases before a court of law? We can argue that justiciable matter covers

¹³⁷ Ibid

¹³⁸ Ibid

¹³⁹ Federal Tax Administration Proclamation Cited above at note 3, Article 53ff

¹⁴⁰ Interview with Ato Belete Ahmed cited above at note 40

¹⁴¹ Interview with Ato Tensa Shelmo Cited above at note 65

¹⁴² Constitution of the Federal Democratic Republic of Ethiopia, 1995, Art,37 proclamation No.1, **Federal Neg.Gaz.** year 1 no.1

all cases unless the law provides otherwise.¹⁴³ This is clearly provided under Article 37 of the FDRE Constitution. The FDRE Constitution gives recognitions for institutions which are empowered to exercise the judicial functions by the law.¹⁴⁴ Following this constitutional base different institutions are empowered to exercise judicial functions.¹⁴⁵ Among the institutions empowered to exercise judicial functions, the tax appeal commission is the one. If we appreciate the rationale behind this constitutional provision, the purpose of this constitutional provision seems that to leave technical to expertise. When we come back to the issue at hand, it needs expertise works because as it is discussed earlier the causes of grievance related to VAT registration and cancellation, in one or the other way, are related to the tax decisions. So, it is better to incorporate in the first instance jurisdiction of the tax authority rather than leave to ordinary courts. If this case is left to courts, it may impose work load on ordinary courts and the courts may not give sound decisions on it. But, the silence of both the VATP and FTAP on the issue at hand does not mean that the tax payers have not right to go before the court of law. As it is discussed earlier, if a case is not given expressly for other institutions which are empowered to exercise judicial power, such taxpayers must have the freedom to take their case to the regular courts since the right to be heard of citizens is a constitutional right.

¹⁴³ Ibid

¹⁴⁴ Id, Article 78(4)

¹⁴⁵ Such as the Labor Relations Board, Tax Appeal Commission, Civil Service Tribunals and the 'Board of Privatization Agency the basic ones.

Chapter Four

4. Conclusion, Findings and Recommendations

4.1. Conclusions

VAT is an indirect tax which is collected at each stage of production and distribution chain of goods and/or services. This feature of VAT makes it an important source of public revenue of a country. Now days, countries almost all countries have accepted VAT to increase their public revenues. Like the other countries, Ethiopia introduced VAT in 2002 to enjoy the fruits of VAT. However, without proper identification of taxable persons, the anticipation of significant amount of revenue from VAT is absurd. Therefore, taxable persons for VAT purpose are identified through the process of registration. Though the existence of legal and institutional frame work of registration for VAT is an indisputable fact in Ethiopia, it is fraught with different problems. This research studied issues and problems associated with VAT registration in general by giving special emphasis on the practical application of the registration requirements in particular. Moreover, the center of attention of this research work is also on the issues of the handling of grievances related to registration and cancellation for VAT. In doing so, it has identified the following major legal and practical loopholes.

4.2. Findings

Having conducted this research, the researcher has identified the following gaps associated with the law and the practice. Gaps falling under each category are, therefore summarized as follows:

A. Legal Gaps

- The discrepancy of the terminology “taxable transaction” in the English version of the VATP and” taxable business transaction” in the Amharic version of the same proclamation. The Amharic version of the VATP employed the terminology “taxable business activities” while the English one used “taxable activities. For the purpose VAT the appropriate terminology is “taxable transactions” rather than “taxable business activities”, because VAT depends on transaction rather than commercial activities or business motive. But, the non compatibility of the terminology in the two versions may create a problem for VAT registration.

- The exclusion of rental of building from the category of business both in the CCE and ITP on one hand the terminology taxable business activities used by the Amharic version of the VATP, on the other hand, creates a problem for VAT registration. Though the governing law for VAT is the VATP, the cumulative reading of article 5 of the CCE, the definition provided by the ITP and the terminology used by the Amharic version seem to suggest that rental of the building is excluded from the scope of VAT. This is particularly raised as a defense by religious institutions which own and rent buildings to avoid registration for VAT and hence payment of VAT since the ultimate purpose of registration is to secure payment of VAT.
- The non amendment of the threshold fixed by the legislator during the introduction of the VAT. The data obtained from the Central Statistical Agency of Ethiopia show that the inflation rate in Ethiopian has at average increased at a 16.65% per year from 2006 G.C to 2016 G.C. Based on this data, the 500,000ETB in 2006 is approximately equivalent to 2,720,834.87ETB in 2016. In this regard, the experience of countries (for instance UK) shows that the minimum threshold set for VAT registration undergoes a periodic revision depending on the increase in the inflation of the economy. The absence of such practice in Ethiopia to amend the law based on the objective economic reality entails administrative burden on the tax authority by drawing small businesses in to the sphere of VAT.
- The adoption of various directives and circulars by the tax authority beyond its delegation power. The tax authority issues different directives and circulars which impose an obligation of registration on businesspersons. This practice of the tax authority is against the principle of legality of taxation.
- The absence of cancellation requirements for voluntary registration. The law has in clear terms provided the requirements that must be satisfied to cancel businesses that are mandatorily registered for VAT. These are cessation of the taxable business activities and failure to meet the minimum threshold requirement. In contrast, the law does not state the prerequisites that must be met to cancel voluntarily registered businesses.
- The non existence of legal provisions which govern grievances related to registration and cancellation. The VATP and the TAP have incorporated provisions which can be used to handle complaints pertaining to tax issues like assessment, penalty and interest. In contrast,

the VATP and TAP have failed to embrace provisions which can be instrumental to entertain grievances raised in relation to registration and cancellation. Consequently, parties that have complaint on the registration and cancellation process may take their case to the court. This will in turn create a challenge on the courts which entertain the case as the issue is more of technical and challenging for the judges to comprehend the matter easily.

B. Practical Gaps

- Merger of exempted and taxable transactions. The required threshold for VAT registration is determined by the assessment of the taxable transaction alone. However, the practice on the ground is contrary to the law. Practically, the tax officers fail to distinguish the difference between the taxable and the exempted transactions. As a result, the tax officers wrongfully use the summation of both the exempted and the taxable transactions to fix the required threshold for VAT registration. This emanates from two reasons- due to lack of awareness on the essence of the law and the sheer interest of the tax authority to register more persons for VAT without giving due attention to what the law provides.
- Lack of proper enforcement of the VAT registration provisions by the tax authority. The VATP law is not uniformly implemented on all taxable persons for various reasons. To begin with, due to the improper assessment of the annual turnover of taxable persons, the tax officer in some circumstances may lower or raise the turnover of the taxable persons. This creates unfair competition and arbitrariness by including persons that do not qualify for VAT and in contrast by excluding persons that may attain the required threshold. The other instance which manifests the inconsistent application of the law the failure of the tax authority to register religious institutions for VAT. In most cases, these problems do have their source in the shortage of adequate knowledge and misunderstanding of the VATP.
- Approving voluntary registration without checking the fulfillment of the requirements provided by the law. The law has provided clear requirements for voluntary registration; but, the practice shows that the tax officers accept and register anyone who is willing to register voluntarily. The downside of this approach is that it invites anyone to get registered.

Based on the above findings the writer of this paper gives the following recommendations.

4.2. Recommendations

- The revision of the VATP provision which talk about taxable activities in the manner which retains the consistency of the Amharic and the English version is necessary.
- The VAT law should be revised so as to clearly define its scope of application thereby it will be possible persons that are required to be registered for VAT.
- The frequent revision of the threshold fixed for the requirement of VAT registration depending on the increase or decrease inflation rate of the country should be practiced regularly.
- Establishing a system which controls the legality of the directives and the circulars issued by the tax authority is mandatory.
- The incorporation of provisions which regulate the cancellation of voluntary registration whenever the VATP is revised is important.
- This writer recommends that the incorporation of provisions which regulate grievances related to registration and cancellation when the VATP is revised.
- The awareness of officers of the tax authority relating to the requirements for VAT registration (by focusing on taxable and exempted supplies), the purpose of registration for VAT and cancellation of registration.
- Adoption of guideline documents (may be in the form of public advance rulings) by the tax authority which should be followed by the tax assessors whenever assessing the annual turnover of the taxable person is necessary.
- Enhancing the enforcement capacity of the tax authority in VAT registration and cancellation through training is advisable.

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