



**FACULTY OF LAW**

**SCHOOL OF GRADUATE STUDIES**

**Loopholes in the tax assessment of coffee traders in Ethiopia: the case of  
Southern Nations, Nationalities, and Peoples Region and Addis Ababa**

**Thesis Submitted in Partial Fulfillment of the Master of Laws Degree (LL.M.) in Business  
Law at Addis Ababa University**

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**June 2019**

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**Plagiarism declaration**

I EPHREM TESFAYE TIRFE does hereby declare that the thesis “Loopholes in the tax assessment of coffee traders in Ethiopia: the case of Southern Nations, Nationalities, and Peoples Region and Addis Ababa” is my original work and that it has not been submitted for any degree or examination in any other university. Whenever other sources are used or quoted, they have been duly acknowledged.

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This thesis has been submitted for examination with my approval as Advisor.

Signature\_\_\_\_\_

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Date\_\_\_\_\_



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## **Dedication**

This thesis is dedicated to all people supported me in the research. Particularly to my families for their sincere love and their ever-present support of my personal endeavors. It is also dedicated to my Mom passed away Bekelech Bayisa, who taught me that hard-working. To my wife Serkalem and my children Nahom, Yonas, Meklit, Marsilas, and Arkena, without their tremendous tolerance and support this thesis couldn't be completed. My brothers and sister Ermias, Mikias and Bezayehu, who are giving me their unlimited support and spent their time carrying my family and reinforced my personal business. To my business partner Jafer Serur, he always understood my congested and hard-pressed life. Also my boss Mrs. Nejah Yusuf, her great patience in my advisory employment career with her company. Finally, not last dedicated to all you being good for me throughout my study.

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## List of abbreviations and symbols

E.C.	Ethiopian Calendar
ECTDMA	Ethiopian Coffee and Tea Development and Marketing Authority
CTSA	Coffee, Tea and Spices Authority
FDRE	Federal Democratic Republic Of Ethiopia
ERCA	Ethiopian Revenue and Customs Authority
ETB	Ethiopian Birr (currency)
FLCTC	FIRST Level Coffee Transaction Center
CTC	Coffee Transaction Center
GCE	Green Coffee Equivalent
GDP	Gross Domestic Product
GTP II	Growth and Transformational Plan II
LDCs	Least Developed Countries
MOA	Ministry of Agriculture
MOR	Ministry of Revenue
MoT	Ministry of Trade
OECD	Organization for Economic Co-operation and Development
SNNPR	Southern Nations, Nationalities, and Peoples' Region
USD	United State Dollar

**KEYWORDS:** Loopholes, Tax assessment, and Coffee conversion factors

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## **Abstract**

*Tax assessment is a technical and legal procedure to assess taxable income from prospective taxpayers. Different tax assessment methods stated in Ethiopian tax law to achieve revenue collection effort and exhaustively collect tax revenue to the entire public service. The Ethiopian economy mainly depends on agricultural goods. In 2017/18, 90 % hard currency obtained from agricultural goods export, coffee contributes 33 % of total agriculture goods. 15 % of Ethiopian people directly or indirectly engaging in the coffee business. However, tax collection from the coffee industry is not an easy task for the government for different reasons, especially in coffee supply traders. Tax collectors and coffee business regulators didn't work in harmonizing ways to achieve their common goal. There is no clear law and regulation other than general income tax law to regulate tax on the coffee business, especially in the primary production level. One of the main factors to flourish coffee smuggling business over the nation is a result of lenient tax assessment application on the coffee trade. Different types of Loophole in the tax assessment on coffee business are a public mystery, especially in coffee grower areas and local markets like Merkato. "Coffee marketing and control proclamation" the current or the previous strongly prohibited exportable coffee trading in the local market. But, the fact is in daylight exportable coffee sales in different local markets. One of the main issues in tax assessment is the coffee conversion ratio in the supply and export coffee process. Ethiopia adopts international coffee conversion agreements. This agreement holds coffee conversion factors indicators in general but tax collectors did not apply those indicators and they prefer to use the different dismantled directive and circulars. Tremendous tax compliant and litigation go to appellant bodies and courts in the past decade in SNNPR and Addis Ababa, and this comes from a loophole in the tax assessment on the coffee business. There is no national conversion to the green coffee equivalent standard applicable for tax assessment and govern a coffee marketing business tractability. In Recent move Ethiopian coffee and spices market development authority working on to issue a national coffee conversion standard applicable for the export coffee process. And SNNPR regional CTSA also submit a three consecutive year red cherry coffee conversion to green bean research data to tax collectors for the sake of tax assessment even if not welcomed tax collectors. This thesis tried to find out the loopholes in tax assessment in the coffee trade in Ethiopia in general and recommend possible ways to stakeholders.*

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## Chapter One

### 1. Introduction

Tax<sup>1</sup> is a levy made by a government on citizen and non-citizen to cover its own capital and administrative expenditures. In virtually all countries, the tax system is responsible for generating the vast bulk of the revenue that is required to fund government services<sup>2</sup>. In most cases tax levy power emanates from constitutional laws, the constitutional basis of taxation in Ethiopia is predominantly found in Article 96-100<sup>3</sup>, of the Constitution of Ethiopia. The FDRE constitution encompasses a provision that enables the two tiers of government to levy tax independently or on their exclusive and concurrent power of taxation<sup>4</sup>. Based on different subordinate tax laws tax collector organs as far as possible collect taxes and duties within a proper tax assessment producers. Tax assessment<sup>5</sup> is an act of computing the tax due, it is applicable legal and technical procedure while tax assessment. It is fundamental to tax collection. An assessment is the end result of the process of ascertaining a taxpayer's taxable income and calculating the tax payable on that income. A notice of assessment becomes final once the appellant period for reviewing it has expired. Ambiguous and divergent laws apply in different government organs will create loopholes in tax assessment activity and drives taxpayers to tax avoidance and evasion practices. Agricultural products in general subject to quality and quantity changes while passing through different processing levels. Disagreements come out between tax collectors and tax-payers on agricultural goods wasted quantity (loss of weight), out-put of main and byproducts, accusation cost (when goods purchased in the primary market), sale prices, and storage time and costs. Ethiopian economy majorly rests on agricultural commodities, such as coffee, tea and spices, oilseeds and pulses, vegetables, live trees, and other plant, gems, and precious metals, live animal and meet,

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<sup>1</sup> "The word 'tax' first appeared in the English language only in the 14th century. It derives from the Latin tax are which means 'to assess'. Before that, English used the related word 'task', derived from Old French. For a while, 'task' and 'tax' were both in common use, the first requiring labour, the second money. 'Tax' then developed its meaning to imply something wearisome or challenging. So words like 'duty' were used to suggest a more appealing purpose. Political spin has just as long a history as taxation, and neither has been detained unduly by the meaning of words."

<sup>2</sup> 'Tax Administration in OECD and Selected Non OECD Countries: Comparative Information Series 2010' 16 <<https://www.oecd.org/ctp/administration/CIS-2010.pdf>>.

<sup>3</sup> Proclamation of the Constitution of the Federal Democratic Republic of Ethiopia 1995 [proc. No. 1, Fed. Neg. Gaz., 1th year, No. 1 .].

<sup>4</sup> *ibid* Art. 96-98.

<sup>5</sup> 'Glossary of Tax Terms - OECD' <<https://www.oecd.org/ctp/glossaryoftaxterms.htm>> accessed 15 May 2019.

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and rawhides excluding fur skins. These products are mostly exportable and major hard currency earner to the Ethiopian economy, and in most cases their input or output quantity subject to disagreement when carrying out tax assessment, because of their nature, trader malpractice, lack of harmonization and gone astray from common goal in government organs and distracted government policy. Coffee is in first place in tax assessment making disagreement between tax collectors and coffee traders in all levels.

In recent arguing between MOR and stakeholder on the figure can understood that respectively 40%, 60% tax still couldn't collect from possible tax-payers in many reasons. Noncompliance is one of the main challenges to LDCs toddler economy, Ethiopia is among them<sup>7</sup>. According to the UN report, GNI per Capita of Ethiopia is USD 644, it is half from the threshold per capita of USD 1229<sup>8</sup>. To compare Ethiopian tax revenue to GTP against list OECD members still far and in desperate.

Coffee is one of the most widely enjoyed and consumed beverages worldwide. In 2018/19 alone, estimated consumers around the globe will drink about 165.18 million bags of coffee<sup>9</sup>, 1.88 percent (3.12 million bags) of that figure will be consumed in Ethiopia<sup>10</sup>. In the continent of Africa, Ethiopians are widely regarded as being the largest coffee drinkers, and apart from its cultural significance, coffee is one of the largest export currency earners for Ethiopia in this contemporary era.

With the Ethiopian economy mainly based on agriculture and service sectors. In 2016/17, Ethiopia earned \$2.26 billion from goods exported, agricultural export take over 84% the total value, Coffee is the first largest export commodity, constituting a 33% and 39% exports share of total exports and export share of total agricultural exports respectively<sup>11</sup>. To this end, in the 2018/19 budget year (nine months), coffee exports contributed over 500 million dollars to the countries budget, it is the

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<sup>6</sup> 'A Short History of TAXATION' (*New Internationalist*, 2 October 2008)

<<https://newint.org/features/2008/10/01/tax-history>> accessed 15 May 2019.

<sup>7</sup> 'Least Developed Country Category: Ethiopia Profile | Economic Analysis & Policy Division' (*Development Policy & Analysis Division | Dept of Economic & Social Affairs | United Nations*, 25 December 2015)

<<https://www.un.org/development/desa/dpad/least-developed-country-category-ethiopia.html>> accessed 16 June 2019.

<sup>8</sup> *ibid.*

<sup>9</sup> 'International Coffee Organization - What's New' <<http://www.ico.org/>> accessed 10 June 2019.

<sup>10</sup> Michael G Francom, 'Ethiopia Coffee Annual Coffee Exports Continue at Record Levels' 7, 3.

<sup>11</sup> *ibid* 5.

worst performance due to different reasons. Ethiopia is the 5th largest coffee producer and exporting country in the world. Ethiopia’s production is an estimated 7.1 million bags in 2018/19. According to ECTDMA, market development, and promotion director, Mr. Basha Daneso announcement in behalf of his office, from July 2018-February, 2019 eight-month performance reported to Ethiopian broadcast service, Ethiopia earns 422 USD from coffee export, it is 71% of a 2018/2019 eight months target<sup>12</sup>. Some reasons mentioned by Mr. Basha are unfair computation between traders, international market price declination, the international market is one factor but on the reverse local market, appreciation leads traders in contraband, export-grade coffee theft during transporting on board.<sup>13</sup> According to police report “40 tone coffee robbed on board to Djibouti in Western Shewa Zone, Lome woreda” and under sale from the international market, which means exporter sold the coffee less than the international market for chasing hard currency for their import business.

“ከውጭ አገር ሸቀጥ ሸቀጥ አስመጥተው በውድ ዋጋ ለመሸጥ ሲሉ ብቻ ወደ ኤክስፖርት ሥራ የገቡ ነጋዴዎች፣ የአገሪቱን የግብርና ምርቶች በርካሽ ዋጋ እየሸጡ መሆኑ ተነገረ..”<sup>14</sup> roughly translated “Ethiopian agricultural goods are selling cheaply in the international market for the purpose of chasing hard currency to their import business by newly joined coffee exporters”

Having to say that Loopholes in tax assessment in coffee trading mostly within first level transaction traders did not care about tax. In other business tax burden is one of the primary agenda on the master budget preparation but in coffee business not an issue, special in first level transaction industries (coffee supplier) in absence of traceable and mandatorily maintain recording system for the whole process. However, the tax law of Ethiopia clearly states about keeping books.

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<sup>12</sup> ‘የኢትዮጵያ ቡና ባለፉት 8 ወራት ከአለም ገበያ ያስገባው ገቢ ዝቅተኛ መሆኑ ተገለፀ - DisplayPage - Ebc’ <<http://www.ebc.et/web/ebcnews/-/-2253>> accessed 11 June 2019.

<sup>13</sup> ‘የምሥራቅ ሸቀ ፖሊስ የተዘረፈውን ቡና እየፈለገ ነው’ (1 June 2019) <<https://www.bbc.com/amharic/48482723>> accessed 10 June 2019.

<sup>14</sup> ‘በውጭ ምንዛሪ ሽኩቻ የኢትዮጵያ የግብርና ምርቶች በርካሽ እየተሸጡ እንደሆነ ተነገረ | ሪፖርተር Ethiopian Reporter Amharic’ <<http://www.ethiopianreporter.com/article/15857>> accessed 10 June 2019; Muluken Yewondwossen, ‘Twenty Exporters Face Severe Consequences | Capital Ethiopia Newspaper’ <<https://www.capitalethiopia.com/featured/twenty-exporters-face-severe-consequences/>> accessed 20 June 2019.

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### 1.1. Background of the problem

Being one of the most significant traded commodities worldwide, coffee trade is commonly featured in both domestic and major international trading markets. To this end, coffee is a member of the soft commodities group, there are two main types of coffee Arabica and Robusta, Arabica traded in intercontinental exchange (ICE) future contract in the US. Coffee is sighted as one of the major trading commodities in international exchange markets in New York and London.

The socio-economic impact of coffee is also very significant for Ethiopia, as nearly 15% of the country population either directly or indirectly participate in the producing, cultivating, processing, transporting, trading and marketing of this major commodity, most of them are smallholder farmers.<sup>15</sup>

Historically speaking, coffee has always been the most important cash crop in the country, repeatedly featuring as one of the largest export categories. In this regard, the coffee bean said to have originated from Ethiopia and has been traded as a major commodity for over five hundred years (from when it was first transported from Ethiopia to Arabia by traders). Today Ethiopian coffee has many destinations around the globe, Germany, Saudi Arabia, Japan, USA, Belgium, France have 68% share in volume<sup>16</sup>. Most of the Ethiopian coffee exports are done at the clean bean coffee level (without value-added), even if roasted coffee exports (value-added) occupies a small quantity.

According to different statistical data, 45% to 50% of Ethiopia coffee production is consumed domestically by growers themselves and coffee drinker throughout the nation. This consumption to production ratio is one of the highest in the world, making Ethiopia and Brazil the only coffee-producing countries that consume a significant portion of their production (approximately 50% in the case of Ethiopia).

To this end, in 2018/19 over 187,200 metric tons (Mt) of coffee was consumed in Ethiopia (total production in the same budget year amounted to 426,000 Mt)<sup>17</sup>. Regionally, Oromia and SNNPR are the largest producers of coffee in Ethiopia (hailed as being the largest caffeinated and best-

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<sup>15</sup> Francom (n 10) 2.

<sup>16</sup> *ibid* 6.

<sup>17</sup> 'Coffee: World Markets and Trade' 5 <<https://apps.fas.usda.gov/psdonline/circulars/coffee.pdf>> accessed 10 June 2019.

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flavored coffee-producing regions), with both states claiming the specific the title of ‘the birthplace of coffee’. There is general agreement among historians that coffee was first discovered in the forest of the Southwestern part of Ethiopia. There are also two competing local areas “Mankira of the present Kaffa zone and Chochee of the present Jimma zone”.

Trade of commodities such as coffee are also regarded as major sources of tax revenues for governments worldwide. Governments in the modern world depend on these tax revenues as a major source of fund, necessary to provide services and goods to their citizens. Revenue generated from the tax is nowadays considered as the major source of funding to the government of Ethiopia, to this end, the country collects tax revenues from different types of taxes either from citizens, residents, and from those who earn their income as a result of their work within the jurisdiction of Ethiopia and abroad.

Conceptually, taxation is regarded as legal obligation levied on persons, and is primarily used as one of the tools of bringing social justice and a means of wealth distribution within the nation. The collection of tax, however, is a difficult task for many countries for different sets of reasons. The existing Ethiopian taxation system also faces similar challenges and is still in need of modernization. While recent work is underway to realize this modernization effort, such as the income tax law amendment, which instituted a separate tax administration law (came in to effect as of July 7, 2017) being a prime example, major hurdles such as tax evasion and avoidance are still significant factors creating income inequality within the nation.

In addition, lack of government commitments and tax review procedures have created loopholes for ‘tax avoiders’ throughout the taxation system, this is specifically apparent in the coffee trade business. While the concept coffee smuggling business has been existing for a long time in Ethiopia, according to Ethiopian broadcast corporation news<sup>18</sup> police investigation prevails from 2000-2007 E.C, 28 individuals are arrested from 56 suspected in violation of coffee law. The suspected committed the crime in a systematic way by issuing business license using frontman (not a real business owner, but the business run by their name with a smuggler). Police said those individuals bought exportable coffee from ECX and sold in the local market and smuggled into

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<sup>18</sup> ‘Government Announced Lists of Arrested Businessmen in Connection with Alleged Corruption | Borkena Ethiopian News’ <<https://borkena.com/2017/01/12/government-announced-lists-of-arrested-businessmen-in-connection-with-alleged-corruption/>> accessed 11 June 2019.

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neighbor countries. Ethiopia lost more than USD 75 million on this coffee smuggle in hard currency and anonymous amount of tax revenue. To this end, lack of an integrated government business orientation within sectorial government agencies and the application of different laws on coffee business sectors has helped create a set of ‘loopholes’ in which ‘tax evader’ can ‘benefit’ form. In Principe, the use of ‘loophole’ in tax assessment isn’t ‘illegal’, yet it is a largely considered that the beneficiary is merely using ‘the letter of the tax law’, but not abiding by ‘the spirit of the law’. Except for small coffee growers, the taxation of coffee as a consumer good affects smallholder farmers, collectors, suppliers, exporters, retailers, roasters, and coffee shops. In most cases between these actors’ price transfer practices occur even if the regulating laws exist. Hence, this study will mainly aim to identify these ‘loopholes’ in tax assessment affecting the coffee business within Ethiopia and find ways to remedy them, specifically within the jurisdiction of SNNPR and Addis Ababa city.

### 1.2. Statement of the problem

The governance of the Ethiopian tax policy is enshrined in different primary and secondary documents.<sup>19</sup> These collections are used to understand the purpose of taxation in Ethiopia and ensure that collecting of tax is done in a fair, equitable, transparent, and efficient way.

Tax revenue as a percentage of GDP is indicative of the share of taxation to a country’s output, and it can be regarded as one of the key measures as to the degree to which the government controls its economic resources. The Ethiopia GDP recently measured at 7.7 in 2017/18<sup>20</sup>, this is significantly less than the projected average target 11.0 % in GTP II<sup>21</sup>. Tax to GDP also low when compared to other OECD and Sub-Sahara countries standards.

To this end, the coffee industry (as one of the primary tax revenue-generating sectors) is also riddled with issues of smuggling affecting business practice in most Ethiopian states, highlighted by a large number of cases in court and under police investigation in regards to coffee smuggling. Accordingly, the government has moved to alleviate this national concern by amending proclamations, regulations, and directives and re-established the Coffee and Tea Development and Marketing Authority, with a view of boosting the sector. In this regard, the national export

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<sup>19</sup> Tadesse Lencho, ‘THE ETHIOPIAN INCOME TAX SYSTEM: POLICY, DESIGN AND PRACTICE’ (2014) 109, 532.

<sup>20</sup> ‘Ethiopia Overview’ <<https://www.worldbank.org/en/country/ethiopia/overview>> accessed 18 June 2019.

<sup>21</sup> National Planning Commission, ‘Growth and Transformation Plan II (GTP II) (2015/16-2019/20)’ 99.

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coordination committee identified major bottlenecks of the coffee market and pointed out 11 major challenges within the coffee value chain. Illegal trading and legal frameworks were pointed out as a major challenge<sup>22</sup>.

The goal of most illegal traders is to avoid regulated business and evade tax, this is primarily devastating to the countries tax collecting hegemony and has pushed many legal traders from the legal business activity to being embroiled in illegal conduct. Hence, this study is conducted with the view of remedying the taxation system of Ethiopia, specific to coffee trade in order to act as a possible solution to illegal trade and benefit from ‘loopholes’ in tax assessment within the Addis Ababa and SNNPR.

#### 1.2.1. Research question

This study tried to answer the following major research questions;

- I. Is there a proper current tax policy, institutional and legal framework in Ethiopia which enables the collection of tax from coffee traders?
- II. What are the practical, legal and institutional problems that impede the government from collecting tax from the coffee sector?
- III. What are the main concerns and challenges to tax assessment in coffee conversion to green coffee equivalent?
- IV. Are there loopholes in the tax assessment on the coffee business in Ethiopia, especially in Addis Ababa and SNNPR?

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<sup>22</sup> Addis Fortune, ‘Coffee Value Chain Up for Major Reforms’ <<https://addisfortune.net/articles/coffee-value-chain-up-for-major-reforms/>> accessed 12 June 2019.

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### 1.3. The objective of the study

#### 1.3.1. General Objective

The objective of this study is to show the possible loopholes in the tax assessment of the coffee sector in Ethiopia in general, specifically highlighting the systems in place within the SNNPR and Addis Ababa jurisdiction.

#### 1.3.2. Specific Objective

Coffee is considered as a key global crop and the second most valuable commodity after oil directly exported by developing and LDCs countries, worth around US\$19 billion in 2015. Worldwide, around 2.25 billion cups of coffee are consumed each day and nearly half of all Ethiopians drink coffee regularly. Due to this significant importance of coffee to the Ethiopia economy, the problems associated with the sector need to be addressed accordingly. Thus, it the primary objective of this research to identify ‘loopholes’ in tax assessment within SNNPR and Addis Ababa City administration, and the impact it will have on the coffee trade sector in general. This study is specifically conducted to address the following specific objectives:

- I. To identify and find ways to remedy ‘loopholes’ in terms of tax assessments within the Coffee Proclamation to Provide Marketing and Quality Control (Proclamation no. 1051/2017 – hereinafter the ‘Coffee Proclamation’).
- II. To support further development of literature on the coffee sector and help the government and business traders achieve transparent taxation practices.

### 1.4. Significance of the study

According to a 2017 report, the United Nations considers Ethiopia as one of the least developed countries globally, with 23% of the governments' expenditure covered by tax revenues. Considering the impact of tax revenues to the country's economy, this study will help tax collectors and business persons engaged in the coffee sector identify problems within the current taxation structure, help fill taxation assessment loopholes, and further identify ways to generate greater tax revenues and business certainty. This study will also be giving a clear insight into the managing, planning and administration tax compliance as it relates to the coffee business. It will further be helpful for other researchers who could be interested in doing further advance work on the same topic. This study can also help us get a better idea about coffee and tax obligation (i.e. the tax

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litigation and tax appeal procedure the coffee traders within SNNPR and Addis Ababa jurisdiction). Finally, this study will also identify possible solutions towards narrowing the ‘loopholes’ in tax assessment and related problems for the benefit of the government, coffee traders, and others who suffer from this problem.

#### 1.5. The methodology of the study

Throughout the course of the study, the researcher has employed a qualitative study methodology. To this end, the researcher has used a combination of two approaches. First, the researcher has analyzed legal provisions of relating to taxation, coffee regulating and control and other related laws. The researcher has also looked into other published and unpublished pieces of literature in the area. Specifically, tax assessment, coffee conversion and others that have to do directly or indirectly with the issue, such as books, journals, case reports, etc... Were reviewed and some decided cases were analyzed.

Secondly, firsthand information was obtained from the members of the responsible government agencies through, particularly from Ethiopian Coffee and Tea Development and Marketing Authority, SNNPR-regional coffee Tea and spices Authority, Ministry of Revenue Hawassa and Western Addis Ababa branch, SNNPR-revenue Authority in the form of interviews. Based on Non-probability sampling method the respondent was sampled based on purposive Sampling Method. Informal (conversational) interview are conducted in order to collect the necessary data and information. Individuals who are experienced in the coffee business in Ethiopia also interviewed. The researcher chose to employ this methodology by weighing the interplay of both primary and secondary sources and their relevance to the outcome of the study. The information gathered from primary and secondary sources was compiled in the ways that are easy to manage and was analyzed and interpreted qualitatively using a narrative technique. Finally, the reliability and validity of these sources were strictly considered by the researcher.

#### 1.6. Limitation of the study

The researcher, throughout the course of the study, faced different challenges that have contributed to the overall limitation of the scope of the study. Lack of sufficient information with regards to limited interviewee availability and availability of sufficient cases (mainly because of the

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traditional and un-modernized case handling system of Ethiopian courts) are sited as major limitations. Additionally, the fact that most cases relating to the issue are pending in courts has had a significant impact on access to a significant body of case law. While these limitations persist, the documents collected, interviews conducted, and case assessed can sufficiently depict a vivid picture about the ‘loopholes’ in tax assessment within the Ethiopian coffee sector.

### 1.7. Organization of the paper

This study is organized into five chapters. The introduction chapter gives an overview of the background information-practical problem, research problem, objective and relevance of the study. Chapter two focuses on the theoretical perspective, specifically on tax assessment and the coffee conversion factors. Chapter three provides an overview of coffee production loss analysis within the context of Ethiopia. Chapter four highlights the existing tax structure used for tax assessment on the coffee business in Ethiopia in general, and SNNPR and Addis Ababa specifically. Chapter five gives the conclusion of this study, a summary of the findings, managerial implications, limitations, and areas for further research.

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## Chapter Two

### 2. Literature review

#### 2.1. Loopholes in the tax assessment

Theoretically, a tax loophole is a provision that drains money from the government. The term "tax loophole" is often used to denote a flaw in the language of the tax, discovered by a sharp-eyed lawyer or accountant and exploited by his client<sup>23</sup>.

Tax loopholes are either intentionally or accidentally made in tax promulgation process. Intentionally the lawmakers purposely made tax loopholes for different reasons, such as to stimulate or encourage investment, support some parts of citizen or group. "There are three questions about loopholes I intend to answer here: First, why is the law so riddled with them? Second, why, once detected, do they usually go uncorrected? And finally, should lawyers feel bad about exploiting them?"<sup>24</sup> Tax loopholes suggest that somebody is outsmarting the law. It is not true, all so-called "loopholes" are put there intentionally by lawmakers.

The basic dictionary definition of a loophole is "a narrow window, slit-opening" and could figuratively be taken to indicate an 'outlet, or means of escape'<sup>25</sup>. According to Black law dictionary 10<sup>th</sup> edition, 'A loophole is generally understood to mean an ambiguity, omission or exception that provides a way to avoid the application of a rule without violating its literal requirements'. For the purpose of this study, the concept of 'loopholes' is not indicative of the broader concept of 'tax loopholes' but rather 'loopholes' in the assessment of taxation. According to a working paper presented by United Nation development program policy recommendation, 'the tax system should be simple, clear, and transparent. Taxpayers shall not feel uncertain and overburdened with the system. Thus, the Authority shall strengthen existing tax policy, clear laws, and regulations, strong taxpayer protections, and close any loopholes that discourage taxpayers from being compliant to tax laws'<sup>26</sup>.

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<sup>23</sup> Boris I Bittker, 'Income Tax "Loopholes" and Political Rhetoric' (1973) 71 Michigan Law Review 1099.

<sup>24</sup> Loe Katz, 'A Theory of Loopholes' (2010) 39 The University of Chicago Press for The University of Chicago Law School 2.

<sup>25</sup> 'Loophole | Meaning of Loophole in Longman Dictionary of Contemporary English | LDOCE'  
<<https://www.ldoceonline.com/dictionary/loophole>> accessed 18 May 2019.

<sup>26</sup> 'Tax Administration in OECD and Selected Non OECD Countries: Comparative Information Series 2010' (n 2).

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## 2.2. Tax assessment

In the immortal words of Oliver Wendell Holmes, U.S. Supreme Court of Justice in 1904, “Taxes are what we pay for a civilized society.”<sup>27</sup> “In well-ordered taxation, there are always three distinct steps: levy, assessment, and collection. Levy, under American law, is a legislative act precedent to, and necessary to the legality of, the other steps. A tax can be levied only by a legislative body and the levy requires a statute or its equivalent. Assessment is the administrative determination of the amount each person is to pay according to the provisions of the levy. Collection (a self-explanatory term) follows, and follows only, after a levy and an assessment. These elementary definitions are repeated by way of preface.”<sup>28</sup> Tax assessment is an effective tool for tax collection. Many countries implemented a voluntary self- assessment under the existing tax law. According to tax glossary definition of self-assessment is” System under which the taxpayer is required to declare the basis of his assessment (e.g. taxable income), to submit a calculation of the tax due and, usually, to accompany his calculation with payment of the amount he regards as due. The role of tax authorities is to check (perhaps in random cases) that the taxpayer has correctly disclosed his income.”<sup>29</sup> Once files a tax report different assessment will manage based on the situation. Most economies have adopted the principle of self-assessment and then taxpayers determine their own liability under the law and pay the correct amount<sup>30</sup>.

Tax Assessment defined as “The determination of how much a person or company owes in taxes. One usually determines one's own tax assessment by declaring one's income and capital gains from the previous year and applying the methodology the government requires to arrive at the tax liability. The government has the right to audit any tax assessment”<sup>31</sup>. According to article 2(32) “Tax assessment” means a self-assessment, estimated assessment, jeopardy assessment, amended assessment, penalty or interest assessment, or any other assessment made under a tax law;” these

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<sup>27</sup> Julian Block, ‘A Brief History of Judicial Quotes on Taxes’ (*AccountingWEB*, 20 November 2017) <<https://www.accountingweb.com/tax/business-tax/a-brief-history-of-judicial-quotes-on-taxes>> accessed 18 May 2019.

<sup>28</sup> CARL C PLEHN, ‘AN ASSESSMENT ROLL FOR THE INCOME TAX’ (1920) 5 *The Bulletin of the National Tax Association* 213.

<sup>29</sup> ‘Self-Assessment: What Is Self-Assessment? Taxes Glossary, Meaning, Definition’ <[https://www.moneycontrol.com/glossary/taxes/self-assessment\\_3086.html](https://www.moneycontrol.com/glossary/taxes/self-assessment_3086.html)> accessed 18 June 2019.

<sup>30</sup> ‘Tax Administration in OECD and Selected Non OECD Countries: Comparative Information Series 2010’ (n 2).

<sup>31</sup> ‘Assessment, Tax’ (*TheFreeDictionary.com*) <<https://financial-dictionary.thefreedictionary.com/Assessment%2c+Tax>> accessed 18 May 2019.

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part and parcel of meaningful words well defined in the definition part of the proclamation<sup>32</sup>. An assessment is the end result of the process of ascertaining a taxpayer's taxable income and calculating the tax review of self-assessment payable on that income. To conclude this tax assessment in Americans law an act of administrative task, but in Ethiopian case, it is a voluntary tax notification and administrative assessment task. In both cases, the purpose of tax assessment is exhaustively manipulated tax revenue from tax-payers that the government would be claimed.

### 2.3. Coffee conversion standards and loopholes in tax assessment in Ethiopia

#### 2.3.1. Conversion factors to convert green bean equivalent

Coffee production is a multi-stage, time-bounded agricultural and industrial process, it considered as a primary hard currency generating sector in Ethiopia from the agriculture industry. Growers, collectors, suppliers, exporters, roasters, and exchange actors are the main players in the process. Until a produced coffee reaches its final consumer, it has to lose its red cherry character, shape, weight and even tests and aroma. Once handpicked from the coffee tree, red cherry is sent to primary processing line either in coffee pulper or huller industries. According to Ethiopian coffee regulating law<sup>33</sup> basically, four types of coffee products are allowed to be export: washed clean green coffee, dry clean green coffee, and roasted and milled coffee. This is primarily based on the coffee proclamation (Article 2, sub 36) stating that coffee having 1% husk content is eligible for export.<sup>34</sup>

Ripe red coffee beans manually harvested in the small scale farmer's coffee farm and moved to a wet or dry cherry process. After harvest, the beans go through mechanical or manual separation for the removal of lower specific mass beans, followed by manual selection to remove any unripe and overripe beans and other undesirable other substances that were not detected during purchasing were not removed during the manual pre-screening process. After passing pulping, fermenting, washing, drying process in case of washed coffee preparation almost 80% of its original mass lost. In coffee, with pulp preparation, 50% of its mass as also would be lost at 12% humidity.

As demonstrated in Table 1 below, coffee changed from red cherry to liquid or powder products passing through the different production stage. The ripe cherry coffee is the object of primary

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<sup>32</sup> Federal Income Tax Administration 2016, Art.25-29 [proc. No. 983, Fed. Neg. Gaz., 20th year, No. 103 .].

<sup>33</sup> Coffee Marketing and Quality Control Proclamation 2017 [proc. No. 1051, Fed. Neg. Gaz., 23th year, No. 43 .].

<sup>34</sup> *ibid* Art. 6(1).

processing in coffee-producing countries. The wet process consists of mechanical removal of the skin (exocarp) in the presence of water, and removal of all the mucilage (mesocarp) by fermentation, washing, and drying. In the so-called “dry process,” the coffee cherry is dried and the dried pericarp is removed by mechanical treatment. Both types of primary processing output in washed coffee with parchment and green coffee sold in primary coffee transaction centers in ECX.

Table-1: coffee conversion standard

These figures are indicative; actual yields may vary.

Coffee	Qty.	After conversion	output
Ripe cherry	100 kg	Coffee with parchment	20%
Ripe cherry	100 kg	Coffee with Pulp	50%
Ripe cherry	100 kg	Clean green beans	16.5 kg
Dry Arabica cherry 12 % moisture	100 kg	Clean green beans	44 kg
Parchment (wet processed)	100 kg	Clean green beans	80 kg
Roasting coffee beans	100 kg	Roasted beans	84 kg
Clean beans	100 kg	Soluble coffee	38. 5 kg
Green beans	100 k	Decaffeinated roasted bean	125 Kg

Source, World Bank 1986, agro Industry profile coffee

Accordingly, in the above-listed stages, 84.5% of the ripe red cherry weight is lost when converted to clean beans through the wet coffee process. Also in the case of the dry process, the same 84.5% of the red cherry bean’s weight is lost. These products are then sold to buyers abroad.

These conversions factors have a very tax implication in tax assessment in absence conversion manual or not take to account the international practice. To maintain fair taxation on the coffee business in the first place shall stipulate a common standard in the nation. It is not for taxation but for the sake of fair trade computation assurance. Theoretically, the implication of the convention factors illustrated in table-2 shows tax-payers noncompliance would continue if the government working on the matter. To have to say this, existing coffee regulation law or tax law couldn’t narrow the loopholes on coffee conversion to washed and byproduct coffee equivalent. Tax collectors blindly perform tax assessment on coffee trade in primary processing level on coffee supplier trade.

Table-2: Example of washed coffee supplier segment financial statement explanation:

Illustration	A	B	C
Red cherry conversion to washed and byproducts coffee respectively	18% and 2%	17 % and 1.5 %	16 % and 2 %
<b>Operating cost per k.g effect</b>			
Red cherry purchase in quantity	1,000,000.00	1,000,000.00	1,000,000.00
Unit Price paid for 1 K.g of red cherry	10.00	10	10.00
	10,000,000.00	10,000,000.00	10,000,000.00
Direct & indirect costs	900,000.00	900,000.00	900,000.00
	10,900,000.00	10,900,000.00	10,900,000.00
Washed	180,000.00	170,000.00	160,000.00
Byproducts	20,000.00	15,000.00	20,000.00
Cost of Goods sold per K.g	200,000.00	185,000.00	180,000.00
	54.50	58.92	60.56
<b>Taxable Income effect</b>			
Sales	13,764,705.88	13,000,000.00	12,235,294.12
	1,176,470.59	882,352.94	1,176,470.59
Less: COGS	14,941,176.47	13,882,352.94	13,411,764.71
	10,900,000.00	10,900,000.00	10,900,000.00
Adminstrative, Selling & Finance	4,041,176.47	2,982,352.94	2,511,764.71
	500,000.00	500,000.00	500,000.00
<b>Net taxable Income</b>	3,541,176.47	2,482,352.94	2,011,764.71

\*This illustration prevails how to alter if conversion facture changed.

On the export trade side, international practice sated by international trade center conversion to green bean equivalent mostly applied<sup>35</sup>. There is a confusing practice in the dry coffee conversion factors against international practice. According to the table -1 each coffee conversion standards on average and indicative was well stated. However, Ethiopian coffee regulators seem working this standard in somehow and apply unwritten standard on the export sector. On the case of *Mullege PLC Vs. Federal General Attorney*<sup>36</sup>, the attorney witness Mr. Assefa Mulgeta, Agricultural Marketing and Input Supply directorate from the Ministry of Agricultural and Rural Development gave his witness on the issue of coffee conversion and weight loss said ” when calculate the defendant coffee conversion we use reduced 20% for parchment loss and 2.5% for

<sup>35</sup> *The Coffee Exporter’s Guide* (3rd edn, International Trade Center 2011).

<sup>36</sup> *Mullege PLC vs Public prosecuto’s office* [2010] Federal First Instance court 160176.

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loss of weight may come out from humidity and wastage (during traveling and processing), previously loss of weight measured up to 1-3% now in accordance of our agreement (consent) adjusted to 2.5%.” Another witness who is made a calculation of conversion testimony “ in accordance with the MoA research from 100 Kg unclean coffee to clean coffee conversion process 12% coffee may go to byproducts based on the standard<sup>37</sup>. Whoever, witnesses testimony was based on standard<sup>38</sup> and the court critically investigate the fact in detail, but not mentioned at any point through entire pages on the matter of 2.5% loss of weight and 12% byproduct respectively, and the court declines the witness testimony. The loopholes exist on this customary conversion practice application in coffee export trade. There are two loopholes associated with tax assessment: First, in the standard clearly stated "loss weight" may occur during storage and transportation up to 0.5%. ”Coffee is hygroscopic, which means that it attracts or loses moisture depending on climatic conditions. It may, therefore, lose a little weight during storage and transport”<sup>39</sup>. According to ECX contract,<sup>40</sup> more than 11.5% moisture for export-grade coffee is not acceptable and subject to back to moisture adjustment through exposure to the sun with on carrying truck. But, when delivery to exporters ECX hasn’t any technical procedure to assure below 11.5% moisture to the exporter. Coffee by nature subject to climate change if not properly handle in moderate storage. If in the cold season the amount increased or in hot season decreased. This internationally well noted 0.5% loss would acceptable between seller and buyer in an international contract. When comes to Ethiopian scenario there is no concrete evidence whether the country fully applied the international standard or the customary trend developed by the coffee regulator. To see the inconsistency in national export coffee conversion it is enough to pursue a letter wrote to ERCA tax complain committee by MARD. On this letter a conversion to green equivalent and loss weight cited in accordance with the standard<sup>41</sup>. In recent move ECTDM undertaking to stipulate national conversion standard<sup>42</sup>. But on this document, there is no mentioned about 2.5%-3% loss of weight, as stated in court decision Mullege vs. General attorney.

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<sup>37</sup> Official letter from MoARD, ‘የቡና ምርት ኮንቨርሽን መጠን መግለጽን ይመለከታል’ (2000).

<sup>38</sup> *The Coffee Exporter’s Guide* (n 35).

<sup>39</sup> *ibid* 67.

<sup>40</sup> ‘ECX Coffee Contract’ 6.

<sup>41</sup> *The Coffee Exporter’s Guide* (n 35).

<sup>42</sup> Interview with Atakilt Tilahun, ‘Coffee, Tea ad Spices quality expert, Ethiopian Coffee & Tea Market Development Authority’ (1 May 2019).

This practical loopholes may be benefiting coffee exporter if they wanted. Secondly, they can transfer ending stock to the next tax year by applying 2.5% weight of loss to the expense and the excess stock between 0-2.5% they may get. Secondly, simply can sell in the black market the difference. Lastly, 12% goes to byproduct when calculating the conversion enhance coffee exporters to play a game between in domestic and international market. Sometimes local market better paid than export price, this not affect taxable income, because of tractability of the sales, but affecting the country trade balance. Another important issue associated with loss of weight is MoR directive 19/1997, this directive issued for the purpose of VAT tax guaranty for VAT tax on the coffee sale. On this law, 2% for dried coffee and 0.8% shall apply loss of weight. There is a paradox with MoA 2.5% loss of weight. See Below

Table-3 Example unwashed coffee of exporter segment financial statement explanation:

<b>Illustration-2</b>		<b>A</b>	<b>B</b>	<b>C</b>
Loss of weight		0%	2%	3%
<b>Operating cost per k.g effect</b>				
Unwashed Dried Coffee		10,000,000.00	10,000,000.00	10,000,000.00
Unit Price paid for 1 K.g of unwashed coffee		75.00	75.00	75.00
Direct & indirect costs		750,000,000.00	750,000,000.00	750,000,000.00
		60,000,000.00	60,000,000.00	60,000,000.00
		810,000,000.00	810,000,000.00	810,000,000.00
Green bean		8,700,000.00	8,600,000.00	8,500,000.00
Byproducts		1,200,000.00	1,200,000.00	1,200,000.00
		9,900,000.00	9,800,000.00	9,700,000.00
Cost of Goods sold per K.g		81.82	82.65	83.51
<b>Taxable Income effect</b>				
Sales		783,000,000.00	774,000,000.00	765,000,000.00
		84,000,000.00	84,000,000.00	84,000,000.00
		867,000,000.00	858,000,000.00	849,000,000.00
Less: COGS		810,000,000.00	810,000,000.00	810,000,000.00
		57,000,000.00	48,000,000.00	39,000,000.00
Adminstrative, Selling & Finance		5,000,000.00	5,000,000.00	5,000,000.00
<b>Net taxable Income</b>		<b>52,000,000.00</b>	<b>43,000,000.00</b>	<b>34,000,000.00</b>

\*When altering Loss of weight provision explained how to affect taxable income.

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## 2.4. Types of tax assessment in Ethiopia

### 2.4.1. Self-Assessment

Ethiopia tax system works on self-assessment on repealed Income tax law<sup>43</sup> and effective as of repealed with schedule C tax-payers<sup>44</sup>. This means that under Schedule “C” (Category A, Category B and Category C), the two categories (A and B) are in principle subject to the rule of self-assessment and must maintain books and records and fill out tax return forms and pay the taxes due<sup>45</sup>. And the taxpayers must present all their assessable income on their annual income tax report. The main objective of Ethiopia’s tax system as a whole is to efficiently raise revenue to be redistributed to the citizen in accordance with government priorities sectors. The main aim of the system of administration is to collect that revenue with minimum administration and compliance costs. “Driven by a desire to reduce administrative costs for tax authorities and aided by modern technology, most economies have adopted the principle of self-assessment. Taxpayers determine their own liability under the law and pay the correct amount. For governments, the computer system and software for self-assessment, if they function well, ensure effective quality control. Self-assessment systems generally make it possible to collect taxes earlier and reduce the likelihood of disputes over tax assessments<sup>46</sup>”.

In accordance of Ethiopian tax law, any taxpayers who are subject to keep account record is based on IFRS (it is principles-based, so that general guideline is set forth, and users are expected to use their best judgment in following the principles) standards. However, until the time frame for implementation in Ethiopia scheduled by Accounting and Audit Board of Ethiopia GAAP (it is rules-based, which means that it is full of very specific rules for how to treat a large number of transactions.) should apply<sup>47</sup>. There is a mystery to applying GAAP, which types of GAAP? US GAAP or General GAAP? This rule confused in the repealed income tax law 286/2002, Article 18.

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<sup>43</sup> Income Tax Proclamation 2002, Art 66(1) [proc. No. 286, Fed. Neg. Gaz., 8th year, No. 34 .].

<sup>44</sup> Federal Income Tax Administration (n 26) Art. 25(1); Income Tax Proclamation 2002. Art 66(1) [proc. No. 286, Fed. Neg. Gaz., 8th year, No. 34 .].

<sup>45</sup> Lencho (n 19) 370.

<sup>46</sup> ‘Tax Administration in OECD and Selected Non OECD Countries: Comparative Information Series 2010’ (n 2).

<sup>47</sup> የሒሳብ መዝገብ አያያዝ መመሪያ 152/2011 2011. Art. 8 (2)

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#### 2.4.2. Estimated Assessment

Estimated assessment is a type of tax assessment when taxpayers fail to declare his tax duties Art. 26 of tax proclamation<sup>48</sup>. However, in directive No. 138/2010, partial acceptance or total rejection of tax-payer tax record may subject to estimated assessment. In accordance with Ethiopian income tax law tax Category, A and B taxpayer mandatorily should keep books of account in a different manner.<sup>49</sup> Each taxpayer should maintain books of account according to the list in article 8<sup>50</sup>. Which means a tax-payer record is the base of its self-assessment of taxation. If tax collector not accepted all of the income or reject some of the cost may amend the self-assessed tax declaration through tax assessment performance. In agricultural products, the original shape of the goods would change through the process and would lose their initial weight and character. This change reflects in the cost of goods manufactured, because of end product variability in terms of input quality, processing system and management applied, weather condition and variety of the agricultural goods. In coffee case, so many factors affect the end product quality and output quantity in Ethiopia. There is no standard conversion rate to convert red cherry to the green coffee equivalent in all of the geographical coffee-growing areas, which is why disagreements come between tax collectors and tax-payers. Lack of uniform tax assessment application on coffee tax is painful to the government and coffee traders. In many litigations shows the main reason for rejection taxpayer record is unreliability on conversion factors. Tax collectors based on article 3<sup>51</sup> of directive tax collectors can make amend tax-payers taxable amount if additional information found. Which means in coffee tax case third party information mandatory should collect and use in the assessment task. That information may come from ECX, regional responsible offices (CTSA) and cooperative associations book records (it is not binding, but may use to know the average purchase price and outputs in that specific location). Based on third party information tax auditors may reduce or increase the purchased amount and the average price paid for 1 Kg red cherry or coffee with husk. This amendment may affect taxable income declared by taxpayers and leads in tax litigation between them<sup>52</sup>. According to an experienced tax auditor Feseha, “these third party information sometimes subject to change during tax assessment or litigation, there is

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<sup>48</sup> Federal Income Tax Administration (n 32).

<sup>49</sup> Federal Income Tax Proclamation 2016. Art. 82(1) [proc. No. 979, Fed. Neg. Gaz., 22th year, No. 104.]; የሒሳብ መዝገብ አያያዝ መመሪያ 152/2011 2011. Art. 4

<sup>50</sup> የሒሳብ መዝገብ አያያዝ መመሪያ 152/2011 (n 47).

<sup>51</sup> የገቢዎችና ጉምሩክ ባለስልጣን, የግምት ታክስ ስሌት አፈጻጸም መመሪያ ቁጥር 2010 [138].

<sup>52</sup> Interview with Hadi Mohamed, ‘Tax Audit Team Leader, SNNPR-Revenue Authority’.

inconsistency report we received in a given tax audit year from responsible offices and we challenging to assess the tax in the coffee business in the primary processing area.”<sup>53</sup> If the taxpayer income assured and purchase reject 90% the sales assigned to cost of goods and the rest 10% goes to taxable income<sup>54</sup>. Then amended tax assessment notice served to the taxpayer after briefly discussed in an exit conference<sup>55</sup>. After all, some of the taxpayers went to tax complaint, but the majority accept the amendment and paid the additional tax.

### 2.4.3. Jeopardy Assessment

Jeopardy assessment is made in situations where, prior to the assessment of a given tax period, it is determined that the assessment or the collection of such insufficiency would be endangered if regular assessment procedures were followed. In US tax law there are three factors according to internal revenue code, should be trigger jeopardy assessment: “(a) the taxpayer is or appears to be designing quickly to depart from the United States or to conceal him/herself; (b) the taxpayer is or appears to be designing quickly to place his/her property beyond the reach of the government either by removing it from the United States, by concealing it, by dissipating it, or by transferring it to another person; or (c) the taxpayer’s financial solvency is or appears to be imperiled. (This does not include cases where the insolvency is created by an assessment.)”<sup>56</sup> According to Art. 27, prior to making a jeopardy assessment, at least one of the factors outlined in the tax administration law must be present. Those factors are: (a) taxpayer ceased to carry on the activity; (b) the taxpayer to depart from the Ethiopia or unlikely to be temporary; (c) and taxpayer assumed will not file a tax declaration for the period by the due date. In both countries tax law almost have similarity, but in Ethiopia tax law stated in general statement lead vagueness “the Authority has reason to believe that a taxpayer will not file a tax declaration for the period by the due date”<sup>57</sup> and also insolvency, not mansion, may include in general statement and not elaborately mention in directive No. 138/2010, art.17<sup>58</sup>. But in USA tax law clearly stated. With association to the coffee business, a

<sup>53</sup> Interview with Fesefa Tesfaye, ‘Tax Audit Team Coordinator, MOR Awassa branch’ (5 May 2019).

<sup>54</sup> የገቢዎችና ጉምሩክ ባለስልጣን, የግምት ታክስ ስሌት አፈጻጸም መመሪያ ቁጥር 2010 [138]. Art. 9(1)(c)

<sup>55</sup> Interview with Abduhakim Redi, “Tax Risk Management and Audit Directorate director, SNNPR-Tax revenue Authority’ (6 June 2019).

<sup>56</sup> Donald Ketchum and Terry Hallihan, ‘R. JEOPARDY AND TERMINATION ASSESSMENTS’ 2.

<sup>57</sup> Federal Income Tax Administration (n 26), Art. 23(4).

<sup>58</sup> የገቢዎችና ጉምሩክ ባለስልጣን የግምት ታክስ ስሌት አፈጻጸም መመሪያ ቁጥር (n 51).

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given coffee trader may participate in coffee smuggling business may perform Jeopardy Assessment<sup>59</sup>. Jeopardy assessment, also known as protective assessment in South Africa tax administration 28, 2011<sup>60</sup>. It replaces estimation assessment the previous act and the concept is like the US and Ethiopian Law.

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<sup>59</sup> Interview with Tesfaye (n 53).

<sup>60</sup> Fayyad Cassim, 'Jeopardy Assessments under the Tax Administration Act 28 of 201' 96, 28.

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## Chapter Three

### 3. Coffee purchase and conversion process

#### 3.1. Coffee transaction in first level coffee transaction centers

##### 3.1.1. Red cherry and coffee with pulp

The red cherry coffee is first supplied by small scale coffee growing farmers, then the Coffee mill industries would subsequently purchase the coffee from first level coffee transaction center with a valid document (receipt). Yet in most cases, the receipt system is not well regulated and transactions are made in cash on the spot. In the absence of proper control during the coffee purchase in coffee auction center by responsible government organs, traders adjust quantity and price at any time they need it for tax purpose. Back record adjustment is possible, the only means to know their price and quantity what they bought within a tax year from SNNPR region CTSA zonal structure, sometimes the figures subject to change when tax assessing<sup>61</sup>. Originally in pick season coffee supplier submit report biweekly bases to the CTSA lower structures, the report includes what they purchase, produced, sent to primary market (ECX), or Sale in vertical integration and direct export, but intentionally figures hiding for the purpose of illegal trade practice for future. The office trying an ultimate effort to check the figures and actual physical stock each year to reduce the malpractice<sup>62</sup>. Agent collectors purchase the coffee on behalf of the coffee suppliers industries and provide to them to the general public, those actors are not in the framework of the tax system, they assumed as an employee of suppliers but in most cases, they are not. “Technically they are coffee traders, buy coffee from farmers and sale to suppliers without a license and tax burden” said a coffee supplier who wishes to remain anonymous. They made daily a lot of profit, but they didn’t pay tax. There is no law to obligate them to issues business license or enter in tax web<sup>63</sup>. The price of coffee depends on demand and supply variations in national and international markets but not less than from minimum price sated by CTSA regional office<sup>64</sup>, the office sating minimum and maximum price in accordance of New York future contract price. This price-fixing procedure not welcomed in tax collectors, because once suppliers know

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<sup>61</sup> Interview with Tesfaye (n 53).

<sup>62</sup> Interview with Redwan Kidir, ‘Deputy Director General, SNNPR-Regional CTSA’ (1 May 2019).

<sup>63</sup> Interview with Belehu Sisay, ‘Cofffee suplier, SNNPR-Sidama Zone’ (4 April 2019).

<sup>64</sup> Interview with Redi (n 55).

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the tax year average purchase price they manage their tax obligation based on the prior information. In some cases, supplier arranges their purchase price within the maximum price fixed by the office.

The coffee purchase transaction is based on free-market principles even if minimum and maximum price sated, thus there are no uniform price listings on the same market, and thus different industries would give their own prices. This creates severe competition and price fluctuation between wet mil industries who are playing in the market. The tax authorities' price information depends on the industries record and the data provided by the local SNNPR regional CTDA office (Third-party Information). The price information is taken from industries biweekly on Tuesday and Thursday report and compiled data record of cooperative industries average purchase price paid to 1 Kg coffee. This is the reason why tax authorities in most cases are not accepting of the industries purchase price.<sup>65</sup> Tax collectors raising their concern on the quantity and price for one-kilogram coffee would be paid to farmers. Sometimes have a tremendous gap between supplier record and third party record (CTSA)<sup>66</sup>. For tax purpose tax assessed by estimated method, 90% of selling price subject to a cost of goods, the rest 10% assigned to taxable Income when tax assessor couldn't trace the actual coffee business transaction.

This type of system has created doubt on the tax authority in regards to purchasing price and these uncertainties also spill over to quantities. There is also a lack of reliable tax payment system that is set up throughout the country. To this end, it makes it impossible to get traceable documentation that could create confidence between coffee traders and tax collectors. So this lack of traceable documenting system in taxation creates gaps for 'tax loopholes'. As we discussed tax loopholes are not illegal, but tax payer's attitudes make it illegal in practice. In most case, tax collectors reject either the price or the quantity in making their assessment with the unreliable information source available to them. This can even lead to accusations of tax evasion (as a criminal charge).

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<sup>65</sup>ibid.

<sup>66</sup> ibid.

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### 3.1.2. Washed, Unwashed and by-product coffee

ECX is considered one of the primary markets to sell washed and dry coffee. The primary aim of ECX is to assuring fair coffee exchange between exchange actors. This mandate is given to ensure that cross trading and unfair trade practices are not exercised by illicit actors.

The concept of ‘cross trading’ (or an individual who is active in the coffee business in a different capacity) is one of a loophole in tax assessment and is considered an unfair trade practice in the coffee business. The strict rules of ECX and ECXA do not allow any person to sell and purchase coffee at the same time from different (independent) persons even with in the same session. This means a person at a time cannot buy and sell the same quantity by the same price within the fair market channel. But, given businessmen having two capacity at a time as the supplier and an exporter can bypass these strict rule and will take competitive advantage against those only trading either supplier or exporter capacity. This is not illegal by any existing law, however, taxpayers simply can manipulate the loopholes through untraceable purchase and sales in supplier business as explained in table-2, it means can purchase with untraceable price and quantity and can sale in legal (ECX) or illegal (Contraband) markets. Simply understood, this means that a person must maintain a trade balance in terms of quantity and price. For instance, if 2000 Mt of coffee is stored by a supplier he or she can sale that 2000 Mt of coffee in the international market in as exporter capacity, this is because the act would mean he or she would not be affected by fluctuation of prices in international markets. If international and local markets get price appreciation tax-payers may look loopholes in coffee regulating and tax laws as stated.

When we come to taxation, this individual (if allowed to the trader in the capacity of supplier and exporter) simply can transfer price in a systematic way. This is where the above discussion of traceability of purchasing price also needs to be stressed, as he/she can simply manage to benefit from loopholes in the tax assessment.

To end this, domestic consumption coffee retailer shall buy coffee only from domestic consumption wholesaler (through ECX) or domestic roaster<sup>67</sup>. According to the coffee proclamation, a local consumption coffee must be having 15% of pure coffee been from 1

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<sup>67</sup>Coffee Marketing and Quality Control Proclamation (n 33). Art 12(2)

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kilogram<sup>68</sup>, but in practice exportable coffee available in each local kiosk shops, supermarkets, and street market. The source is obvious as discussed, smuggled coffee in the domestic market has a better price than the export selling price. At this time contain less defected coffee or looking good appearance coffee sold birr 170, it is almost 200% over than New York price, it is the public mystery at all.<sup>69</sup> All transaction couldn't trace in tax assessment by auditors on this business and third party information can't avail to them to assess taxable income.

### 3.2. Coffee conversion factors

#### 3.2.1. The primary process in the coffee-producing area

Coffee fruits undergo pulp extraction to produce green coffee seeds. The most common methods of pulp extraction are known as wet and dry methods. Coffee is harvested in Ethiopia from November to February in the form of cherries that have to be processed. There are two popular methods to process coffee in coffee-producing areas. Those are Wet and drying methods, under wet method once the cherries are harvest brought to coffee washing industries where they are de-pulped, fermented in tanks and then washed in clean water to remove the mucilage. The wet parchment coffee (the coffee “bean” with a thin layer of skin) obtained is then dried in the sun on raised beds to a moisture content of 11.5 percent<sup>70</sup>. On this process on average, 80% initial weight loss. With the dry processing method, seeds are exposed to the sun or air dryers until the moisture content is approximately 10%–12%. In this stage based on the specified standards, the red cherry is converted to Green bean coffee over 84% of its weight loss. However, the red coffee output depends on other ‘affecting’ factors. These are geographical location and environment, nature of a specific coffee variety, rain season dependency, as it affects the production in both quality and quantity, cultivation process, tight and negative computation between coffee industries, in terms of lenient quality requirement, coffee grabbing coffee pulper and huller efficiency and skilled labor.

According to research conducted by SNNPR regional CTSA trade office, there is different coffee output. MoR Hawassa branch and SNNPRs Revenue Authority consider this research information

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<sup>68</sup> *ibid.* Art.12(1)

<sup>69</sup> I visit some supermarket and shop in Awassa and Addis Ababa, packed in 1 K.g available to sale, some of them have brand label. I bought 3 packs and submit to coffee cupper “all of them are export standard coffee, and wouldn't be sold in ECX platform as domestic consumption coffee” said a coffee cupper and trading representative in ECX, working in one of frontrunner coffee export company, who wish to remain anonymous.

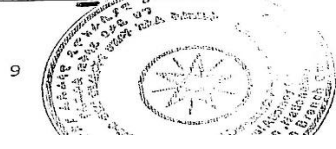
<sup>70</sup> *Agro-Processing Profiles, Coffee, The World Bank* (1986) 605.

to be a legal input to tax assessment purpose for 2002-2006 E.C tax years. This research document is challenged by some coffee suppliers, because of its red cherry conversion to washed coffee and by-products equivalent.<sup>71</sup> The research result prevails three outputs (products) from a sample of 100 Kg red cherry, those are washed coffee with parchment, handpicked coffee with parchment (ልቃሚ ቡና ከነሽሚዙ) and floated coffee with parchment (ተንሳፋፊ ቡና ከነሽሚዙ). The research was a good move to the coffee sector, but it is not attainable to tax assessment purpose. Because it left one steps process for the byproduct. To conclusiveness for tax purpose byproducts conversion to green bean, the study shall be done until dry mill process to remove the coffee parchment. But, tax collectors blindly use this inconclusive research report for tax assessment. There are two outcomes to use this research paper as a conversion factor: Firstly so many taxpayers not protested this byproducts figure, because it is too far from the actual result and making very advantageous them. Second, a law-abiding taxpayer who is transacted within the legal market faced extra tax and goes to tax complain.

Picture-1: Sample of 2006 E.C coffee conversion data

ሠንጠረዥ 6፡ ከንባታ ተንባሮ፣ ሀድያና ወላይታ ጨምሮ (ማዕከላዊ ዞን) የታጠበ ቡና ውጤት መሆኑ ዘንጤያ ቅጽ

ተ.ቁ	የዞን ስም	ወረዳ ስም	የተወሰደበት ከ 100 ክ/ግ እሽት ቡና የተገኘ ውጤት					
			ናሙና ብዛት	ቡና ከነሽሚዙ በክ/ግ	ተንሳፋፊ ከነሽሚዙ በክ/ግ	ልቃሚ ከነሽሚዙ በክ/ግ	ድምር	እርግጠኛ ገለባ በክ/ግ
4	ከንባታ ተንባሮ	ቃሚቡራ	ናሙና-1	21	1.8	1.25	24.05	75.95
			ናሙና-2	16	1.5	2	19.5	60.5
		ቀድዳጋሚላ	ናሙና-1	16	1.6	1.4	19	81
			ናሙና-2	16	1.2	1	18.2	81.8
አማካኝውጤት				17.2	1.52	1.43	20.15	79.857
5	ወላይታ	ሶዶድ	ናሙና-1	17.5	1	1.2	19.7	80.3
			ናሙና-2	16.8	1.7	1.5	20	80
		አማካኝውጤት		17.15	1.4	1.35	19.9	80.1
ጠቅላላ አማካኝ ውጤት				17.18	1.46	1.49	20.025	79.98



As we show in Picture-1 tax collectors made assessment directly a one-step process left data. According to another research made by SNNPR regional CTSA in 2010 E.C on a regional level can take as an indicative output. The conversion of 100 Kg red cherry to 17.31 washed coffee with parchment, 0.89 Kg handpicked with parchment and 1.52 kg floating coffee with parchment

<sup>71</sup> ደ/ብ/ብ/ሀ/ክ/መ ግብይት ኅብረት ሥራ ቢሮ, 'የቡና ምርት ጥራት ወጤት መረጃ ጥናት' (ደ/ብ/ብ/ሀ/ክ/መ ግብይት ኅብረት ሥራ ቢሮ 2006).

equivalent may get from wet processing industry. Both byproducts (handpicked and floating coffees) outer layer of the bean is removed by hulling and the green bean thus obtained is ready for marketing in the dry mill industry. The research result concluded conversion of 2.41 (1.52+0.89) handpicked and floater coffee to 0.541 Kg equivalent byproduct coffee.

“ከ100ኪ/ግ ቀይ እሾት ቡና አማካኝ ውጤት በክልል ደረጃ ማድረግ ከተፈለገ አማካኝ የታጠበ ቡና ከነገለፈቱ 17.31 ኪ/ግ፣ ተንሳፋፊ ከነገለፈቱ 0.89 ኪ/ግ፣ ልቃሚ ከነገለፈቱ 1.52 ኪ/ግ ና ተንሳፋፊና ልቃሚ ድምር 2.41 ሲሆን ከተቀሸረ በኋላ ተንሳፋፊና ልቃሚ ንፁህ ቡና ድምር 0.541 ኪ/ግ እና ተንሳፋፊና ልቃሚ ሸሚዝ 79.1% እደሚገኝ የጥናት ውጤት መረጃው ያሰያል።”<sup>72</sup>

Picture-2: Condensed 2006, 2009 and 2010 E.C coffee conversion to washed and byproducts equivalent.

**ማጠቃለያ- በሳሳት የተለያዩ ምርት ዘመን በታጠበ ቡና የተሠራ ናሙና ጥናት ውጤት የሚያሳይ ሠንጠረዥ**

ዞን	ናሙና የተወሰደባቸው ወረዳዎች ብዛት በምርት ዘመን			ከ100 ኪ/ግ እሾት ቡና የተገኘ ውጤት ከነ ሸሚዝ								
				በ2006 ምርት ዘመን		በ2009ምርት ዘመን		በ2010 ምርት ዘመን		የሳሳተ ምርት ዘመን አማካይ ቡና ውጤት		የተቀሸረ ንጹህ ተንሳፋፊና ልቃሚ
	በ2006	2009	2010	የታጠበ ቡና ከነ ሸሚዝ (ኪ/ግ)	ተንሳፋፊና ልቃሚ ቡና (ኪ/ግ)	የታጠበ ቡና ከነ ሸሚዝ (ኪ/ግ)	ተንሳፋፊና ልቃሚ ቡና (ኪ/ግ)	የታጠበ ቡና ከነ ሸሚዝ (ኪ/ግ)	ተንሳፋፊና ልቃሚ ቡና ከነ ሸሚዝ (ኪ/ግ)	የታጠበ ቡና ከነ ሸሚዝ (ኪ/ግ)	ተንሳፋፊና ልቃሚ ቡና ከነ ሸሚዝ (ኪ/ግ)	
ሲዳሞ	2	3	5	19.40	2.58	17.68	1.81	17.274	2.276	18.118	2.22	0.464
ጌዴኦ	5	3	2	19.86	2.64	17.45	1.33	17.75	2.74	18.35	2.23	0.464
ቤንሻንግሊ	2	1	-	19.77	2.38	17.26	0.74	-	-	18.51	1.56	0.326
ሸኑ	1	2	-	19.53	2.71	19.50	3.05	-	-	19.51	2.88	0.601
ካፋ	3	1	-	19.93	2.83	19.98	2.05	-	-	19.95	2.44	0.509
ከ/ጠንባሮ	2	3	-	17.20	2.95	16.48	3.28	-	-	16.84	3.105	0.648
የክልሉ አማካይ ውጤት	15	13	7	19.28	2.68	18.05	2.04	17.512	2.508	18.46	2.40	0.502

ማሳሰቢያ- ከ100 ኪ/ግ የታጠበ ቡና ከነሸሚዝ ለወጧል 70ቱ ሲከፈሉ በአማካይ 80 መቶው ብቻ ንጹህ ቡና መሆኑ ይታወቅ፤

Source: SNNPR- regional CTSA 2010 research paper<sup>73</sup>

<sup>72</sup> ‘በደ/ብ/ብ/ክ/መ በሚገኙ ሲዳሞና ጌዴኦ ዞኖች ከታጠበ ቡና ምርት ተንሳፋፊና ልቃሚ ናሙና በመወሰድ በተካሄደ የዳሰሳ ጥናት የተገኘ ውጤት ሪፖርት’ (በደ/ብ ክልለዊ መንግስት ቡና ሸይና ቅመማ ቅመም ባለስልጣን 2010) የዳሰሳ ጥናት 14.  
<sup>73</sup> ibid 33.

A researcher has not included one step has a limitation on by-product conversion. It did not show a final green been quantity and cannot quantify the amount that is expected to be output.<sup>74</sup> Tax collectors primarily use this research document as the basis for their tax assessments. They converted red cherry to different product based on location and came up with a new audit founding quantities that should produce and recorded by traders. The difference quantity between the trader's record and audit is subject to base additional tax calculation of 1 kg by 7.15 according to ERCA for domestically available coffee.

There are two parties who suffer financial loss on this tax assessment procedure: the government and credible taxpayers. On the government side, the loss is in millions from tax, because many of the coffee traders benefited from loopholes. By law there is only one market place locally (ECX), according to ECX other coffee contracts are not acceptable by ECX, and also there is no legal market to trade-in. In existing tax litigation ERCA vs. Danecho prevail how the government lost tax and taxpayers who are law abide getting tax burden.

Picture-3: Tax assessment working paper of Danecho Mukere PLC.

የግብር ዘመን	ሳይቱ ደረጃ ለሰጠው አካባቢ	የቡና ግዢ በቢ.ግ	ከ100 ኪ.ግ የሚገኝ ተንሳፋሪ	አጠቃላይ የተገኘ ወጪት በቢ.ግ
2002	አለቃ ወንዶ	1,184,612.00	2.5	29,615.30
2003	አለቃ ወንዶ	23,960.00	2.5	599.00
2002	ወናን	449,989.00	2.6	11,699.71
2003	ወናን	278,152.00	2.6	7,231.95
2002	ዳጥታ ሶሬ	576,481.00	3.2	18,447.39
2003	ዳጥታ ሶሬ	593,483.00	3.2	18,991.46
2002	አረካ	1,065,937.00	3.2	34,109.98
2003	አረካ	681,348.00	3.2	21,803.14
2002	ጋራ ጎዶ	791,919.00	2.2	17,422.22
2003	ጋራ ጎዶ	0	0	0
የ2002 ድምር				111,294.61
የ2003 ድምር				48,625.54
ድርጅቱ የሰጠው የ2002 ድምር				1,615.00
ድርጅቱ የሰጠው የ2003 ድምር				68,389.00
ወደ 2004 የሥራ ተንሳፋሪ ቡና ግብይት				24,215.00

**የተንሳፋሪ ቡና ስሌት**

ከግብይት እና ህብረት ስራ ጽ/ቤት የመጣው የቡና ግዢ መረጃ ተወስኖ ለአገር ወጪ ጥገና የሚወጡ የተንሳፋሪ ቡና መጠን ከላይ ባለው ሰነድ ላይ የተሰጠ ሲሆን በ2003 በጀት ዓመት በመመሪያው መሰረት ተሰርቶ የተገኘው የቡና መጠን 48,625.54 ኪ.ግ ሲሆን ከሰጠው ወገን ግብይትና ህብረት ስራ ጽ/ቤት የተወሰደ ተንሳፋሪ ቡና 68,389 ኪ.ግ ጋር ሲነፃፀር የ19,763.46 ኪ.ግ ልዩነት ያሳያል ። በማንነስ የሚታየው የቡና መጠን ከ2002 በጀት ዓመት የደረሰ ቡና ተደርጎ ተወስኗል እንዲሁም ከ2003 ወደ 2004 የሥራ ተንሳፋሪ ቡና 24,215 ኪ.ግ ታሳቢ ተደርጎ። የ2002 በጀት ዓመት የተንሳፋሪ ቡና በዚህ መሠረት ተሰርቶ 111,294.61 ኪ.ግ የተወሰደ ሲሆን ከግብይትና ህብረት ስራ ጽ/ቤት የተወሰደ የቡና መጠን 1,615 ኪ.ግ ፣ የደረሰ ቡና 19,763.46 ኪ.ግ እና ከ2003 ወደ 2004 የሥራ ተንሳፋሪ ቡና 24,215 ኪ.ግ ተቀንሶ በተረፈ 65,701.15 ኪ.ግ ተንሳፋሪ ቡና በሽያጭ ዋጋ 7.15 ብር ተባዛቶ ድርጅቱ ያላሳዘተው የተንሳፋሪ ቡና ሽያጭ ብር 469,763.24 በሰነድ/2002 ሽያጭ ላይ ተደምድል ።

Source: Tax assessment working paper attached by General Attorney defense in Tax appeal tribunal

<sup>74</sup> 'በደ/ብ/ብ/ክ/መ በሚገኙ ሲዳሞና ጌድኦ ዞኖች ከታጠበ ቡና ምርት ተንሳፋሪና ልቃሚ ናሙና በመወሰድ በተካሄደ የዳሰሳ ጥናት የተገኘው ጤን ሪፖርት' (ገ 72).

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Coffee conversion is a big deal when tax audit carrying out, traders books of account is the first source of evidence tales the traders coffee production. However, there is no confidence between tax collectors and traders in terms of input and output quantity in the coffee business. Coffee conversion issue occurred in different level of coffee production. Coffee from wet process: Red cherry to Washed coffee, then washed coffee to green coffee, and green coffee to clean green coffee, clean green coffee to roasted and milled coffee; Red cherry to coffee with pulp, Coffee with pulp to green coffee, green coffee to clean green coffee, clean green coffee to roasted and milled coffee. During those multi-stage process until reach end-users quantity loss expected in each level. According to World Bank agro- Industry profiles indicator,<sup>75</sup> 100 Kg red cherry in both processes would get 16.5 Kg clean green coffee. Which means 84.5 % of the red cherry will be wiped out through process to get clean green coffee. To demonstrate this: 100 Kg red cherry converted to 20 Kg washed coffee, 20 Kg washed coffee to 16.5 Kg clean green coffee.

### 3.2.2. The primary process in export coffee processing industries

In this stage of production, parchment coffee is hulled to be converted into cleaned coffee beans and then the sundried green coffee bean is converted to cleaned coffee. In the meantime, domestic consumption coffee and by-products (such as coffee husks) are also produced within the secondary process. In both processes, the quantity of the parchment coffee and cleaned coffee is reduced (in the parchment process 20% reduction and in the case of domestic consumption and by-products 12% is reduced). 2.5% overall quantity loss is expected to occur.

The loopholes in this process are the discrepancies which occur in the calculation of the actual and average standard weight loss. Some exporters use this gap to delay tax burden by shifting their stock to the next fiscal tax or selling these products in the domestic black markets. Tax collectors concourse only above 2.5% loss. Exporters expected to maintain stock balance as stated in the coffee proclamation. ECTDM has the mandate to control the stock movement and make reconciliation against exporter stock book. Conversion factors are very taken to the account when stocking balance calculation. But, there is a disagreement between tax collectors and exporters on conversion ratio. For this reason, there is no national conversion standard developed, however at

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<sup>75</sup> *Agro-Processing Profiles, Coffee, The World Bank (1986).*

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a time ECTDM under developing national conversion standards<sup>76</sup> to harmonize conversion ratio may in to use in coffee export business. However, Ethiopia is a member of ICO and adopted all agreements into law, this national conversion standard expected not far from international standards and makes another loophole. According to the International Coffee Organization (ICO) (01.05)<sup>77</sup> dried cherry (coffee with pulp) to green bean: multiply the net weight of the cherry by 0.5; parchment (washed coffee) to green bean: multiply the net weight of the parchment by 0.8. This is an international practice would applicable in coffee grower countries.

### 3.1. Secondary process

#### 3.1.1. Roasting for the foreign market

In Ethiopia coffee sector a small portion of the coffee produced in secondary industrial process carried out by local roasters who roast, grind and package the coffee for export. International coffee trade monopolized by big four roaster and retailer companies. Ethiopian traders that much try to engage in this market segment. In terms of capacity, countries infrastructure, trade system and business nature of traders (most are engaging in the coffee sector for hit and run than long term attachment with the business). On the other hand over the world, most dominating brands exist in the market over a century.

### 3.2. Storage

Coffee is a moisture contained commodity, according to the international standard green coffee beans should be preserved under 11% -12.5% moisture to maintain its aroma<sup>78</sup>, flavor, and color. According to international standards, the number of coffee beans is increased and decrease with fluctuating temperatures. If not coffee stored in moderate warehouse quantity fluctuation must, which means during the dry season will face quantity loss or in cold season/ wet humidity will quantity gain occurred. In most organized countries the loss of weight comes from weather condition is not an issue, because of their strong regulation and warehouse management. In the Ethiopian case, coffee storage warehouses are far from the standard warehouse and mostly not achieve minimum food management system standards based on the researcher accidental physical

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<sup>76</sup> Interview with Tilahun (n 42).

<sup>77</sup> 'World Coffee Trade-Conversions and Statistics' <<http://www.thecoffeeguide.org/coffee-guide/world-coffee-trade/conversions-and-statistics/>> accessed 11 June 2019.

<sup>78</sup> *The Coffee Exporter's Guide* (n 35) 195.

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observation on some warehouses. To this end, quantity variation in different season is should consider in tax assessment, however, the phenomena covered in 2.5 % general loss and it's difficult to Tax assessors to know what was the actual quantity. Totally, coffee traders play the paper game on end stock of according to a person who does not need to mention his identity told to the researcher.

### 3.2.1. Roasting for the domestic market

Ethiopia coffee roaster buys coffee beans only from ECX,<sup>79</sup> ECX offers an exchange market for coffee suppliers, exporters, growers, retailers and roasters of byproduct coffee. According to Proclamation 1051/ 2017 article 2(12) domestic consumption coffee consisting of 15% of pure coffee and byproducts<sup>80</sup>. But, some of the coffee roaster for local consumption uses export-grade coffee to get quality aromas, flavor, and high stimulation, even the law obliged them only and only should buy from ECX platforms. Which means some of a contraband flaw to these types roasting and packing industries. The man who is interview on the Issue he need not named in the research told in most cases to get quality coffee to local consumption couldn't with 85% defected coffee without exportable coffee input.

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<sup>79</sup> Coffee Marketing and Quality Control Proclamation (n 33).

<sup>80</sup> *ibid.*

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## Chapter Four

### 4. Loopholes within relevant and applicable laws against coffee trade in the assessment

This chapter will highlight the relevant legal frameworks and case law relevant to the tax assessment procedures within the Ethiopian coffee sector, and specifically applicable within the jurisdiction of Addis Ababa and SNNPR.

#### 4.1. Applicable and relevant laws

Currently, the primary national instrument employed to regulate the coffee trading business in Ethiopia is “Coffee Marketing and Quality control proclamation” No. 1051/2017 and its regulation No. 433/2018. These legal instruments repealed and replaced the previously existing proclamation 602/2001 and regulation no 161/2001. On the matter of coffee conversion ratio, ICO agreements those are Ethiopia adopted would applicable mostly in exportable coffee.

The key features of this legal instrumental are specifically, a detail definition and traceability procedures of coffee, coffee husk sale and the like.<sup>81</sup>

The possible practical loopholes on those proclamation are as follows:

- I. **Price fixing:** Coffee traders having the capacity as the supplier, exporter and roaster can fix price by using the legal loopholes. According to the ECXA rule, these entities cannot transact with each other but can buy or sell with other trading actors with reasonably the same price. This is a legal loophole and creates unfair competition and impeded tax assessment.
- II. **Information handling and report:** The Coffee Marketing and Quality Control proclamation only focus on coffee business development and market regulating and does not create a clear link with the tax collector by legally binding information transfer system. One of the reasons for rampant coffee smuggling practice in the country the lack of coordination coffee regulatory body and tax collectors. Tax collectors complain about information handling and transfer to the tax assessment task.<sup>82</sup>

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<sup>81</sup>

<sup>82</sup> Interview with Redi (n 55); Interview with Tesfaye (n 53). “Data fluctuation on quantity and price is commonly practiced by responsible CTSDM offices in Woreda level...”

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III. **Agent coffee buyers:** In the primary auction market are a foremost or better beneficiary from red cherry and coffee with pulp transaction. In most cases, they fix the price to buy and sell on the spot market. Based on the law their relationship as employee and employer, but in practice, they are an autonomous and pure trader. They are not part of the tax web, because they assumed as an agent for suppliers. In most cases, they are working on their own capital. This law didn't come up with this issue. On brochure prepared by ECTMD to introduce "Ethiopia coffee sector policy reform" call them commission agent in Coffee Production and Marketing value chain in Ethiopia section. Which means they recognized but not in tax web.

Apart from the above mentioned legal instruments, Circular No.20.1/10/53/00/61, 3.0/211/8 and 3.5.2/20/07 are different circulars issued for tax assessment purpose by ERCA and are seemingly against some provisions of these coffee regulating laws. These differences are mainly related to the assessment of income tax, VAT, and dividend taxes. To this end, if taxpayers coffee production output is below the expected output stated by ERCA, the difference is assessed and a new tax claim is initiated.

The possible practical Loopholes on these circulars:

- I. **Domestic coffee price:** Coffee price is dynamic and fluctuates for different reasons, specific prices should not applicable for 'all-time'. 1 kg of coffee available for domestic consumption is to be traded at birr 7.15 fixed by ERCA. It is static tax loopholes for the government or sometimes traders. This assessment practice worked until 2007 E.C and benefited many traders. In different circulars, ERCA amends comes up with an average price and currently the price taking from ECX database. However, the ECX sales price is the least compared to the black market.
- II. **ECX domestic coffee price:** Now a day MoR using for tax assessment ECX datasheet<sup>83</sup>. Even if contraband market price better than ECX transacted value. To this end, domestically consumed coffee is to be traded at a low price as mentioned in the circular,

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<sup>83</sup> Interview with Tesfaye (n 53).

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traders sometimes try to get benefit from substantially larger prices in the black market and report the sold volume at the low rate set by ERCA.

A coffee production study conducted by SNNPR regional CTSA office in 2006 E.C is one and the only instrument tax collectors use in federal and state-level until 2009 E.C and 2010 E.C research conducted. This study works as a law and retroactively, which is clearly against the basic constitutional right. This study recommended in its conclusion remakes, word by word saying “this study may use only in this fiscal year... to get the best result and to maintain stakeholders benefit should be studied further for three consecutive years.<sup>84</sup> And also SNNPR regional CTSA explain this by writing a letter to ERCA Hawassa branch<sup>85</sup>. Despite this fact, tax collectors have been using this study as a benchmark for coffee tax assessments for many years without amendment. Many coffee traders affected by this blind assessment and begging SNNPR regional CTSA office to elaborate the research to tax collectors, and then the office wrote letters to ERCA Hawassa branch and SNNPR revenue bureau<sup>86</sup> To this end, the main beneficiaries for this practice would, in turn, be are tax avoiders and evaders. Because this study stops one step before the final processing stage in the dry mill industry to get exportable under grade coffee (UGC) and domestic consumption coffee. Without this process (and against the objectives of the coffee proclamation), ERCA, states, and Zonal and Woreda administrations make tax assessment by creating imaginary market places and market prices. This practice clearly creates a loss of unaccounted government tax revenue. The researcher from the interview with traders has identified that most of the interviewees are happy with loopholes, as the black market price can generate for them more than 10 times of the tax collectors fixed price.<sup>87</sup>

Possible practical Loopholes when using this SNNPR regional CTSA coffee conversion to green bean equivalent applicable for tax assessment:

- I. **2006 E.C Yield report:** The 2006 study was made only for 2006 tax year, clearly stated on page 13. But tax collectors using to 2002 -2007 E.C. tax assessment.

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<sup>84</sup> ደ/ብ/ብ/ሀ/ክ/ሞ ግብይት ኅብረት ሥራ ቢሮ (n 71).

<sup>85</sup> ibid.

<sup>86</sup> Interview with Kidir (n 62).” I wrote a letter to tax collectors upon compliant came to the office, stated this research shall be conducted for three consecutive three years to show convincible coffee conversion ratio”

<sup>87</sup> In most time domestic market coffee price appreciating and easily can sale without additional effort and behind the tax burden.

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- II. **Absent one step industrial process:** The study conducted only in primary processing level in wet coffee processing mills and dry coffee processing mills industries. In wet coffee processing, the red cherry outputs are: washed coffee and defected coffee with parchment (Tensafafi and Leqami Buna Kenshemizu). These coffees products should pass hulling stage to get green coffee. Without passing this stage and being gradable coffee to meet ECX contract. These products are not marketable coffee, also there is no existing trading market place, and tax collectors assumed traders sold in the illegal market.<sup>88</sup>
  - III. This research may use only for the red cherry to washed coffee and dry green coffee outputs for the 2006 tax year. These are the final product on the primary process, but the rest products left incomplete by the study should be further seen.
  - IV. **Conversion ratio:** The use of this research is strongly beneficial to illegal traders and discourages loyal taxpayers and also damaging government tax revenue.

Condensed coffee research report of 2010<sup>89</sup>, presented to tax collectors in SNNPR and MOR Hawassa branch by SNNPR regional CTSA. This data made on the recommendation of the 2006 E.C research report (to get conclusive data the research should conduct for three consecutive years). In the recommendation to get conclusive result should be made a three consecutive year research. But, in many reasons such as budget, manpower and lack of inter-government cooperation this research was done after past two years, the rest two-year research conducted in 2009 E.C and 2010 E.C. SNNPR regional CTSA also perform the 2011 E.C yield coffee conversion research. In this report dried cherry conversion to green bean equivalent included. See comparison and difference the 2010 research with international accepted indicative red cherry conversion to green coffee bean equivalent standard:

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<sup>89</sup> 'በደ/ብ/ብ/ክ/መ በሚገኙ ሲዳማና ጌድኦ ዞኖች ከታጠበ ቡና ምርት ተንሳፋሬና ልቃሚ ናሙና በመወሰድ በተካሄደ የዳሰሳ ጥናት የተገኘ ውጤት ሪፖርት' (n 72).

Table-4: Comparison of red cherry coffee conversion to GCB

Conversion factors between standard and reseach report	Washed Green Bean	Washed Byproduct bean	Red Cherry Conversion to Grean coffee Equivalent
Internationally accepted red cheryry conversion to green bean coffee			16.00
Summary of SNNPR regional CTSA research report (2010 E.C)	14.768	0.502	15.27
Difference			0.73
* 18.46 (washed coffee)*80% (converted to green bean) =14.77			

Possible practical Loopholes when using this SNNPR coffee conversion to green bean equivalent applicable for tax assessment:

- I. **Coffee conversion to equivalent to green coffee:** Application of this condensed research report in tax assessment may open loopholes, because of the report focus only on the red cherry conversion to Washed coffee with parchment and green bean byproducts equivalents. This conversion indicator may mislead tax assessors. Tax assessors may not be working by analogy and directly take the figures to the calculation based on the report. Which means they accept the conversion directly as it is 18.46 for washed and 0.502 byproducts. The figures not always much in every supplier or having a great possibility transpose or shifting the output from one to another. For instance, what happens a given supplier conversion factors being 17.50 and 1.27 for washed coffee and byproducts respectively. Simply can understand both conversion equivalent are the same  $((18.46*80\%) + .505=15.27$  and  $(17.5*80\%+1.27=15.27)$ . On this scenario, tax assessors couldn't calculate in tax assessment by analogy without written direction from the responsible organ. As well as the tax assessment activity may chaos and disagreements obvious.
- II. **Predictability of conversion factors:** Suppliers once know the conversion factors may playing on the edge of the factors and come up with the adjusted conversion ratio. If their conversion is better than the research report they may calculate the invasion amount.

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## 4.2. Analysis of tax litigation in the assessment of tax against coffee traders

The following case law highlights the importance of flexibility on a case by case basis when making tax assessments.

### 4.2.1. Danecho Mukere PLC<sup>90</sup> vs. ERCA Hawassa branch

In the Danecho Mukere PLC case, the ERCA Hawassa branch conducted a two years comprehensive audit of Danecho Mukere and issued draft audit findings and held exit conference. However, Danecho Mukere PLC did not agree with these findings and on ERCA's application of relevant laws and rules.<sup>91</sup> ERCA assessment was primarily based on the company's financial record, third party information,<sup>92</sup> ECX sales invoices, research paper conducted by SNNPR regional "Gibyet bureau,"<sup>93</sup> and ERCA circular No. 20.1/10/53/00/61.

While Danecho Mukere PLC had paid its tax obligation during the audited tax year. While also declaring a profit margin for the audited years of 30%, a much higher margin as compared to the country expected a sectorial profit margin of 10% it was subject to such undue procedures form ERCA.

The company, in exist conference meeting, tried to consult ERCA about the wrong application of the law and research documents.<sup>94</sup> To this end, Danecho Mukere PLC argued regarding two critical points: the first point relates to limitations in ERCA's applied research, as it did not consider (or was not ready to consider)<sup>95</sup> the hulling process in the dry mill processing segment. Secondly, ERCA's coffee price stated in circular No.3.5.2/20/07 (birr 7.15 for 1 kg) was considered by Danecho Mukere PLC to be far from a fair market price and not recognizable with ECX traded price on that tax period.

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<sup>90</sup> Danecho Mukere PLC is a coffee supplier company in Ethiopia, it has five washed coffee pulping and one dry coffee hulling industries in SNNPR, specifically welaita, Sidamo, and Gedio zones since 2001. The company is one of model tax payers in the region and has got first class tax payer recognition from ERCA in 2003 and 2005.

<sup>91</sup> ደ/ብ/ብ/ሀ/ክ/መ ግብይት ኅብረት ሥራ ቢሮ (n 71).

<sup>92</sup> ERCA collect information in written from SNNPR Coffee marketing cooperative work office in Woreda levele that the company engaged in coffee business in the audit tax Year.

<sup>93</sup> ደ/ብ/ብ/ሀ/ክ/መ ግብይት ኅብረት ሥራ ቢሮ (n 71).

<sup>94</sup> Ato Manu Edao, Finance head of the company said" I told on exit conference about the research paper irrelevance to coffee tax assessment, because of its inconclusiveness and time limitation"

<sup>95</sup> ERCA did not consider the hulling process because in in previous instances they conducted the audit based on this audit assessment format and still continue this practice

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Yet, ERCA still kept its stand and issued a tax declaration to the company, this, in turn, led Danecho Mukere PLC to take its case to the tax review committee within ERCA. After months of deliberation, the ERCA tax review committee reaffirmed the tax declaration. This case is currently pending in Tax Appeal Commission for a decision. Danecho made three optional counter-argument to tax appeal, first this research can't apply retroactively for 2002 and 2003 E.C tax years, second the research remain one step to give conclusive result, third if the research applied not only the difference but should apply on all domestic coffee products then ERCA should refund around 2.5 million birr. However, the case still in tax appeal commission for more than three years. The tax assessment working paper explained in Picture-2. On this wrong and baseless tax assessment and research report interpretation followed by ERCA, this taxpayers couldn't get its withholding tax refund Birr 766,647.15 according to refund direction<sup>96</sup> and 50% tax paid for appeal.

#### 4.2.2. Mullege PLC vs. Ministry of Trade

“In April 2009, six large traders were banned from exporting coffee because of their presumed excessive hoarding. The government revoked their licenses, closed down their warehouses, seized their coffee stocks, and sold them on their behalf.”<sup>97</sup> Mullege PLC is one of them to face criminal legal suit by the public prosecutor.

In the Mullege PLC case, the federal public prosecutor sued Mullege PLC before federal first instance court, Lidata division file No.160176<sup>98</sup>. The case was instituted on the ground of violating proclamation 602/2000 article 14/6 and 15/7, in regards to hoarding and concealing old crop coffee inventories.<sup>99</sup> After confiscating the suspected coffee<sup>100</sup>, the ministry of trade sold the coffee in the ECX. In this case, Mullege PLC argued that the alleged confiscated coffee was not coffee concealed from the relevant authorities, but rather a product left over from its production process and bought through ECX market platform. The public prosecutor had instituted the case based on the ministry of agriculture's in office desk audit by making seasonal inventory balance which used

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<sup>96</sup> ‘የተመለሽ ጥያቄን ይመለከታል’ (2009); Income Tax Proclamation 2002 [proc. No. 286, Fed. Neg. Gaz., 8th year, No. 34 .].Art. 76

<sup>97</sup> Peter Ngibuini Kuguru, ‘Effects of Government Policies on Performance of Coffee Industry in Kenya’ 8.

<sup>98</sup> *Mullege PLC vs Public prosecuto's office* (n 36).

<sup>99</sup> Coffee Quality Control and Marketing 2008 [proc. No.602, Fed. Neg. Gaz., 14th year, No. 61 .].

<sup>100</sup> Kuguru (n 97).

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the international and local minimum standards for coffee product conversion of weight loss. Mullege PLC argued that this standard is merely an indicative measure of average possible output and that the actual output may vary from this assessment. Further, Mullege PLC stated that its output was below the minimum standard allowed for byproducts. On this basis, the court decided that the standards were indicative tools of international and national norms and are not precise and definitive indications of the actual production output and waste. This case highlighted the concept that international and national weight conversion standards used for the assessment of taxation should be viewed in a careful manner and not as strict evaluating criteria. As they could be used as tools by possible 'tax evading' private companies to report the minimum standards and sell excess products on 'black markets.'<sup>101</sup> This standard can also have a negative implication on companies such as Mullege PLC, who could be wrongly implicated by a government organization for hoarding and concealing products from taxation.

One of the major argument explain in coffee conversion part of this research, one of an argument was conversion factors of coffee. A provision assigned by MoA for loss of weight was 2.5% for dried coffee fixed. But, the defendant actual loss of weight was 2.37%. This difference is one of the factors for the alleged coffee hoarding and concealed. The court decides in favors of defendant argument and baseless 2.5% loss of weight provision used by coffee regulators and coffee traders. The expert from MoA couldn't convince the court based on evidence, only they tried referring "The coffee exporter's guide book", prepared by International trade center. It seems customs developed through time and makes tax loopholes in the tax assessment. At the end of the day this company suffered from a financial crunch. The government confiscated and sold all of its coffee inventory through ECX and deposit in clothed account a huge amount of the company working capital until the court procedure exhaust more than two years.

#### 4.2.1. Ajora PLC vs. ERCA Hawassa branch

Ajora PLC is engaging in coffee trade as a coffee supplier in SNNPR, Welaita and Gedio Zone. The company has two supply coffee processing industry in both zones. Its tax center is ERCA

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<sup>101</sup> Late Ethiopain Meles Zenawi told on the issue when held meeting with coffee exporter on the black marketed coffee before commence legal action.

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Hawassa branch, the branch performed a three years (2001-2003) tax audit and unable to compromise on the coffee conversion. Based on audit founding the branch office declared 1.8 million additional tax with rejection the company inventory book (available to sale washed and byproduct coffees). The company had not accepted the audit founding and file tax complains to ERCA head office in Addis Ababa.

The tax office used the 2006 research report, based on the conversion data available to Welaita and Gedeo Zones, Ajoras' produced coffee available to sale found under expected amount by tax assessors. The difference between the expected amount of washed coffee and coffee byproducts multiply by the average sales price of the company sales in ECX and birr 7.15 respectively and add to the net taxable income of Ajoras' sales.

The appellant tax complain was coffee yield differ village to village based on geographical altitude, coffee variety and grower's production capability. After all the tax review committee decided in favor of Ajora to reassess the tax based on the company books of account. After reassessment ERCA issued another tax declaration by asserted byproducts conversion. Then the company agreed to pay the remaining amount around 4 hundred thousand. The company hadn't information about the 2006 research report.

On this case what can understand there are different perspective in ERCA to handle the coffee conversion matter. This branch replicates the same conversion in another taxpayer even if know what will be after compliant.

## 5. Conclusion and Recommendations

### 5.1. Conclusion

Coffee production is a multi-stage process and involves different trade actors starting from the cultivating process to reaching final end-users around the globe. In most cases in Ethiopia industries are using old and highly labor-intensive technologies in the primary production process. This and other factors affect the production output of coffee. Purchasing of coffee in primary markets except ECX is not traceable. Thus, the actors in the primary process and the secondary process of coffee production are highly unregulated by tax collectors.

Conceptually speaking the use of loopholes technically allows a person or business to avoid the scope of a law or restriction without directly violating the law. Generally speaking, loopholes may be intentionally made and left by lawmakers for specific purposes, in some cases where there could be benefits to the industry, the economy, and employability of workforce in general. Yet some loopholes are not left intentionally to achieve this purpose, but rather emanated from practice and legal application. These loopholes can also manifest themselves in the form of tax evasion if the government does not detect them early and finds a legal solution.

Ethiopian government's tax collection capability is still not advanced and is regarded to be always behind taxpayers. Institutional incapacity and government commitment are also limiting tax collection. Coffee is the first biggest exported product in Ethiopia and again the second foreign currency earner after Ethiopian Airlines. Government has put in place measures to increase tax revenue according to GDP II. Agricultural business like coffee is thus highly subjected to tax attraction in terms their volume and amount, coffee traders are also high contributors of tax, which is why this study has chosen to focus broadly on this industry.

Coffee conversion standards and rules may be used as indicators, but not as mathematical certain figures. Tax collection should be based on the law and principles, and be predictable to build a positive perception upon taxpayers. We can see in the cases discussed in this study, where tax collectors or public attorneys use standard indicators as a law and the base for evidence against taxpayers. Tax assessment should be based on a factual base and should be dynamic upon

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circumstantial pieces of evidence. Thus, a multi-billion coffee business needs a dynamic tax system in order to monitor it.

Institutional gaps and old manufacturing practices contribute to making loopholes in the coffee business and inhibits tax avoidance and evasion. If tax collectors and coffee trade regulators work together to fill these gaps the researcher believes that the tax collection apparatus in Ethiopia can become efficient. To this end, the coffee and tea authority's professionals are very near and familiar to the coffee business, thus tax collectors should consult the coffee regulatory authority to achieve better results in coffee conversion issues.

Thus, the researcher believes based on the outcomes of this study, which provides a better understanding of loopholes in tax assessment in the coffee industry, the following recommendations should be addressed to fill the loopholes in the tax assessment.

## 5.2. Recommendation

- 1) Tax collection efficiency may be achieved by narrowing loopholes in tax assessment, agricultural goods like coffee mostly subject to quantity and quality change from harvest to end product. Coffee is an international traded soft commodity and is currently subjected to tax evasion trends widely in Ethiopia. Thus, dynamic laws and rules should be issued after a detailed discussion with stakeholders and related regulatory bodies to a cult or reduce this trend.
- 2) Ethiopia tax policy should give concern to agricultural products, because of its coherent nature and many people involved in the business, the government shall collect proper tax from the sector to bring social fairness. Coffee is domestically consumed and hard currency earner for the Ethiopia economy, injustice tax collection may damage the sector and may make poor people poorer. Fair taxation across coffee traders may reduce coffee smuggling and unfair computation between traders.
- 3) Coffee smuggling is the effect of loopholes in the coffee trade, prefixed purchase price and quantity conversion known by traders may easily benefiting the coffee traders and discourage tax obedience. The primary base of tax assessment should be books of accounts of the traders with the sprite of law.

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- 4) Tax collectors should develop their own professional in major fields to investigate the taxpayer's business by themselves in their institutional structure. And should develop research and development organ to enhance the technical capability of tax assessor. Many of disagreement comes from lack of sufficient knowledge about tax payer's business nature and product variety.
  - 5) Conversion factors depend on the quality and variety of imputes coffee. Tax collectors should work with international practice in line with locally developed conversion ratios. Many factors affect the conversion factors, so the red cherry conversion to washed coffee and byproducts quantities transpose each other. Tax collectors shall take to consideration against red cherry coffee conversion to green coffee bean equivalent than independent conversion. Independent conversion may mislead and makes resource worthless by unnecessary litigation. For instance, in prevailed conversion factors reported on SNNPR regional CTSA 2010 research 18.46% and 0.502% are the average minimum expected outputs. Tax collectors should not apply this benchmark conventionally, because the quantities transpose each other. The only measurement applied should be red cherry conversion to GCE, the case of the SNNPR benchmark  $((18.46 \times 80\%) + 0.502 = 15.27.27)$ . If given taxpayer books prevail 17.20 Kg washed coffee and 1.51 Kg byproducts, it is the same as the average benchmark  $((17.20 \times 80\%) + 1.51 = 15.27)$ . Tax collectors should enhance this technical knowledge.
  - 6) Any of the coffee regulators' research products shall be explained in terms of red cherry coffee conversion to GCB. This may simplify the tax assessment and avoid silly litigation on the matter, at the end of the day any reasonable person simply prevail against the fact.
  - 7) Red cherry and coffee with pulp purchasing should be based on a registered and controlled receipt system, it may reduce adjustment or produce documentation for tax purposes. It should be timely reportable to tax collectors during harvest and processing season (like as excise tax). This enables access to timely information for tax collectors and coffee regulators.
  - 8) The current tax assessment practice in first level production mainly depending on third party information, this information originally comes from traders weakly and annual reports. The reports made by traders may useful for statistical purpose but in tax, the assessment may misleading.

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- 9) Coffee conversion should be based on the yield within international coffee conversion to green coffee bean factors. Tax collectors should make an assessment line with international standards. And also take lessons from model taxpayers and update their database as useful benchmarks.
  - 10) Goods for sale (coffee) should be considered to be sold in a legally recognized market with a reasonable fair market price. Coffee at any production stage has a market price if it is allowed to be sold in the market. But, in existing coffee regulating laws, unfinished coffee products (one step left behind) could not be marketable in Ethiopia. Byproduct with coffee parchment couldn't be measured with an imaginary market price and market platform. If traders assumed coffee smuggled or concealed, the coffee regulating laws should apply to be a criminal or civil liability than tax collection.
  - 11) Tax collectors should be reasonable and rational when assessing tax, one of Danecho Mukere PLC appealing argument was that “ERCA Hawassa branch should show the market place and legal framework that unfinished defective coffee with parchments may sell”. Tax collectors should be rational on the quantity difference while assessing the tax payer’s books. For the purpose tax assessment creating imaginary market price and place may encourage coffee smugglers than strengthening tax collection effort.
  - 12) Any coffee conversion ratio should be not far from international coffee conversion standards. Because of that standard came from in detail research made over the world and most countries use it as an indicator for their national standards. It is true cultivation and production capability alter the output of green clean coffee, but the last end coffee bean which is gradable or not coffee in quantity not that much alter. For instance, the 2010 coffee conversion study shows the SNNPR coffee conversion not far from the standards.
  - 13) ECTMDA in federal and Regional structure, MOA and MOR should work together to achieve their common goal. Institutional individualism can’t bring national success. They should work in harmonizing ways to narrow loopholes used by tax evaders and coffee smugglers. This coordination may enable to alleviate impediments on tax collection from the coffee business.
  - 14) Existing coffee regulating law should amend to include transparent timely and conclusive report dissemination clauses to information user organs, such as revenue collectors.

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- 15) Tax collectors should take lessons from the model and honest taxpayers on the coffee conversion factors and average price.
  - 16) Storage and humidity shortage should be governed based on the law, this researcher couldn't find any of the research or another document on the loss weight (2.5%) tax deduction. This custom is one of the loopholes in the sector and should be applied within the traceable mechanism.

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## Glossary

Ground coffee	Roasted coffee which has undergone grinding.
Hull	Dried parchment of the coffee fruit
Hulling or dehulling	The mechanical removal of the dried endocarp from parchment coffee to produce green coffee.
Husk	Assembled external envelopes of the dried coffee fruit.
Roasting	The use of heat to generate fundamental chemical and physical modifications in the structure and composition of green coffee in order to darken the beans and develop its characteristic flavor
The drying of cherry coffee	Drying coffee cherries to reduce their moisture content in order to remove their husks and to condition them for storage
Washed-and-cleaned coffee	Dry-processed green coffee from which the silverskin has been removed by mechanical means and using water.
Wet-processed coffee	The green coffee that is wet-processed is known as washed or semi-washed coffee. Washed coffee is green coffee from which the mucilage has been totally removed and semi-washed coffee is green coffee where most of the mucilage still adheres to the parchment.
Supply coffee	coffee processed by industries located in the production area for delivery directly to the ECX or export processing industries;