



**PERCEPTION OF TAX AUDIT PRACTICES: EVIDENCE FROM
ETHIOPIAN REVENUE AND CUSTOMS AUTHORITY LARGE
TAX PAYERS OFFICE (LTO)**

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fulfillment of the award of Master of Science (MSC) degree in
Accounting and Finance

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Statements of declaration

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

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Statement of Approval

This is to certify that the thesis entitled **“Perception of Tax Audit Practice: Evidence from Ethiopian Revenue and Customs Authority Large Tax Payers Office (LTO)”** prepared by Solomon Shumetie under the supervision of Temesgen Worku (PhD) and submitted in partial fulfillment of the requirements for the Master of Science (MSC) Degree in Accounting and Finance complies with the regulation of the university and meets the accepted standards with respect to originality and quality.

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Lists of abbreviations

ERCA: Ethiopian Revenues and Customs Authority

LTO: Large Taxpayers Office

EAMTPBO: Eastern Addis Ababa Medium Taxpayers Branch Office

WAMTPBO: Western Addis Ababa Medium Taxpayers Branch Office

GDP: Gross Domestic production

OECD: Organization for Economic Co-operation and Development

IT: Information Technology

EC: European Commission

VAT: Value Add Tax

TOT: Turn Over Tax

ABSTRACT

The overall objective of this study was to assess Perception of Tax Audit Practice evidence from Ethiopian ERCA Large Taxpayers Office. The specific objective includes examining problems related to perception of tax audit practice regarding tax audit program and type of tax audit used, audit case selection methods and the experience and capability of audit staff resources and its conducive working environment. The study adopted mixed method approach in order to answer research questions and achieve the research objectives. Specifically, the techniques used in the study include survey with tax auditors, interviews with tax audit head and documentary analysis. According to the result of study Ethiopian Revenue and Customs Authority Large Tax Payers Office, Audit case selection is not based on the availability of resource for tax audit. Regarding taxpayers' characteristics during tax audit practice, Tax payers were not cooperate to give their source documents, do not respect the tax law, lack of good awareness on tax, not happy while they are noticed to be audited and Taxpayers are mostly unwilling to release vital records. The managements were not cooperate as well as did not have job security. Moreover, the branch did not facilitate short and long term trainings in any business sectors. Thus the study recommended that the branch management should work closely with tax audit department, supply sufficient audit materials and revised the time frame to give all business sectors to be audited.

Key words: Taxation, tax audit

CHAPTER ONE

INTRODUCTION

This chapter discusses about background of the study, description of the study area, statement of the Problem, objective of the Study, research questions, scope and limitations of the study the significance of the study and organization of the Study.

1.1 Background of Ethiopian Revenues and Customs Authority

The Ethiopian revenues and customs authority (ERCA) is the body responsible for collecting revenue from direct and indirect taxes. The plan of the government is to cover the government expenditure by domestic revenue sources. The government is committed to expanding its domestic revenue mobilization efforts to ensure fiscal sustainability.

According to article 3 of the proclamation No 587/2008, the Ethiopian revenues and Customs Authority was established and came into existence on 14 July 2008, by the merger of the Ministry of Revenue, Ethiopian Customs Authority and The Federal Inland Revenue Authority for the purpose of raising revenue for the Federal government for the objective of modern tax system and customs administration, avoiding unnecessary and redundant procedures that results delay, to be more effective and efficient in resource utilization, information and service delivery.

As per the information that the researcher obtained from the branch human resource department, there are ten federal tax office branches' in Ethiopia (Addis Ababa: LTO, EAMTPBO & WAMTPBO, Adama, Dire Dawa, Hawassa, Jimma, Bahir Dar, Mekele and Kombolcha) that are engaged in administering taxes of category "A" tax payers (Private Limited, share company and corporate company).of which the country's huge revenue is collected from the large tax payers office (LTO).

1.2 Background of the study

Currently, the primary objective of taxation is to raising government's revenue to finance its expenditure for all economic activities. There is growing international interest in improving the ability of developing countries to collect domestic revenue from taxation. It also used to re-distribute income and wealth and to reflect other social and political objectives even though it fails to meet its intended objectives in several developing countries. Developing countries face many serious problems to collect taxes efficiently due to tax administration and design. They are also in trouble to provide basic social services from taxation (Damme et al. 2008). Therefore taxation emerges as one of the most effective domestic tools that governments have direct control over to develop the resources needed to meet their social, economic, and political goals. (Tanzi et al. 2000).

The development of any nation depends on the amount of revenue generated and applied by the government on public infrastructure for the benefits of members of that society. Taxes, and tax systems, are fundamental components of any attempts to build nations, and this is particularly the case in developing or transitional nations (McKerchar et al. 2009).

As Brautigam (2008) stated that taxes underwrite the capacity of states to carry out their goals; they form one of the central arenas for the conduct of state-society relations, and they shape the balance between accumulation and redistribution that gives states their social character. Taxes build capacity of state by provide security, meet basic needs or foster economic development and build legitimacy and consent (McKerchar et al, 2009). In addition, Azubike (2009) noted that a tax system is an opportunity for the government to collect additional revenue needed in discharging its present obligations. Okezie (2003) states that a tax is a burden which every citizens must bear in order to sustain his or her government thus enabling that government perform certain basic functions to the benefit of those its' governance. Thus, it is evident that a good tax structure plays a multiple role in the process of economic development of any nation. The government of Ethiopia has several options to finance its public expenditures and pursue its fiscal policy. These options include imposing of taxes on businesses and persons, and non-tax revenues such as service, property and investment income, privatization of public enterprises, and domestic and foreign grants.

Among others, tax along with customs collections is an important source of revenue for every government, and is a heart to a country's wellbeing (Damme et al. 2008).

The proper amount of tax must be collected on a timely manner for successfully improving and maintaining steady economic progress of a nation. A tax audit is an examination of whether a taxpayer has correctly reported its tax liability and fulfilled other obligations. It is often more detailed and extensive than other types of examination such as general desk checks, compliance visits or document matching programs (OECD, 2006a).

Tax is a compulsory levy by government through its agencies on the income, consumption and capital of its subjects. These levies are made on personal income such as salaries, business profit, interest, dividend, discount or royalties to obtain revenue. It is levied against company profit, petroleum profit, capital gains and capital transfer (Bello, 2001). Therefore, taxation is a compulsory payment or transfer of resources from private to public sector levied on the basis of the determined criterion and without reference to specific benefits received in order to accomplish some of the nation's economic and social objectives. Taxation is primarily aimed at generating revenue for government in order to cater for its expenditure (Al Zakari, 1995).

Tax audits are an examination of taxpayer's business records and financial affairs to ensure taxpayers have computed their tax payable in accordance with the current tax laws and regulations (Isa et al. 2011). Tax audit is an examination of the historical financial statements and other documentary evidences for the preparation of current tax returns, as well as the supporting working statements, followed by an audit report giving the auditor's opinion about the degree of correspondence between the information contained in the tax return and the regulatory provisions of tax laws.

Tax audit is a means of ensuring compliance with tax law. Tax auditors have a good grasp of accounting knowledge to be highly efficient and effective. Audit is not supposed to be an open-ended affair since it is not an investigation. Investigation result from suspicion or actual knowledge of the existence of tax evasion or tax fraud. Tax investigations need special training and competence in investigation techniques.

The vision of many developing countries have become preoccupied with improving tax system to expanded domestic revenue especially taxation, offers a promise of greater autonomy in the future and a break from restrictive aid and loan condition. For example, in the case of Ethiopia, the government replaced the sales tax with Value Added Tax (VAT) & Turn over Tax (TOT) to increase its domestic revenue.

1.3. Statement of the problem

Properly designed and administrated taxation system is important for developed and developing countries to increase domestic revenue from taxes. The system should have been simple and transparent administrative procedures (Tanzi et al. 2000). Under insufficient tax administration of audit program, the potential amount of tax revenue in developing and transitional countries has not been collected in an efficient and equitable manner (Edmiston et al. 2004). Moreover, weak tax administration may make the tax system unfair so that compliance taxpayers would bear heavier tax and inappropriate tax burden so that, the compliance taxpayers are in turn to work in the illegal economy.

Tax audit is an activity or a set of activities performed by tax auditors to determine at taxpayers' correct tax liabilities for a particular accounting or tax period, by examining of a taxpayers' organization procedures and financial records in order to assess compliance to tax laws and verifying the true, fair, reliable, and accuracy of tax returns, and financial statements (ERCA, 2010).

The Ethiopian government used taxation for raising revenue to meet its public expenditure. However, due to the lack of awareness of taxpayer's tax regulation and laws, firms or individuals do not like to pay taxes, reducing their tax liabilities under different actions like tax evasion and avoidance. So, the government is not collect as much tax revenue in the country.

Tax administration is an extremely important area for public sector reform in Ethiopia as it is a key issue raising domestic revenue to support the delivery of Ethiopians public services. The studied branch is a large taxpayers' office is established by the tax authority to provide service for customer/taxpayers whose annual turnover is above 80 million birr and this

branch office contributes the largest portion of the total domestic tax revenue collected by the tax authority. If tax evasions and avoidances take place or occur in this branch it adversely affects the government's revenue.

As per the study conducted by Getaneh (2011) revealed that tax audit program remains undeveloped with slight range of tax audit activities performed targeting aptly specific risks at federal level. The study also shows low audit coverage, the absence of compliance risk-based audit case selection strategy. On the other hand, the research done by Getaneh (2011) and Samuel (2016) found that there were scarcity of audit resources, tax auditors in particular, and absence of proficient and experienced tax auditors as well as incompetent auditors to tackle tax evasion and avoidance.

By improving the perception of tax audit practice, the tax administration should be implemented a successful audit program, the resources available, the methods of audit case selection practice and availability of suitable and free working environment for tax auditors which is capable to investigate and prevent loss of tax revenue, and to improve voluntary compliance and tax potential. In view of its importance this area will have invaluable contribution in identifying weak areas and recommending possible solutions to the tax authority to achieve its objectives and to improve its tax administration. Hence, the researcher becomes interested to assess the perception of tax audit practice in large taxpayers' office which is limited to the tax audit.

Currently few researches have been done in this area. Their main concern is to show, the positive relationship between Tax Audit and to that of Government revenue and Tax compliance. In their analysis part they indicated that Tax Audit has increased Government revenue by Increasing Tax compliance and decreasing tax evasion and avoidance as well.

Furthermore, there are three studies reviewed regarding tax audit in different settings. Yesegat (2008) studied VAT administration problems at large, VAT audit in particular, Mesfine (2008) studied tax audit and its role in increasing government revenue in Ethiopia and Getaneh (2011) examines tax audit practice in Ethiopia (the case of federal government).

The objective of this thesis is, therefore, to review and examine the perception of tax audit practice evidence from Ethiopia ERCA-LTO, which is presented as general objective and specific objectives. Details are mentioned as follows:

1.4. Objective of the Study

1.4.1 General Objective

The main objective of the study is to examine the perception of tax audit practice evidence from Ethiopia ERCA-LTO.

1.4.2 Specific Objectives

Thus, the study accomplished the following specific objectives in line with the problems stated in the next section:

- To assess ERCA-LTO's performance according to their tax audit plan.
- To examine the resources available for ERCA-LTO in performing their tax auditing.
- To examine the methods of audit case selection practice in ERCA-LTO.
- To examine availability of suitable and free working environment for tax auditors at ERCA-LTO.

1.5. Significance of the Study

This work is done with the anticipation that, once the perception are identified a better solutions are find Revenue Authority understands the existing Tax Audit performance, evaluating Tax Audit practice to make some adjustment on the existing tax audit systems.

Moreover, it will provide positive feedback about the efficiency in the procedure, strengthens and the weakness of Tax Audit practice to tax administration and the ERCA- LTO is able to raise enough revenue for the government.

The study to be supporting document for ERCA- LTO to realize the need to equip its staff, educate and motivate them effectively for efficient working attitude. The Study also provide

feedback to the tax authority regarding the tax audit practice and its perception for the government to improve the tax administration in order to collect reasonable tax revenue and improve voluntary compliance. Finally it is an initiation for those who are interested to conduct a detailed and comprehensive study regarding the perception of tax audit practice.

1.6. Scope and Limitations of the Study

Due to resource, constraints and shortage of time the study focused particularly audit part of one branch ERCA- LTO excluding other ERCA Medium taxpayer's branch offices and regional tax authority. The study has examined the perception of tax audit practice focusing on performing tax audit programs for all tax payers, sufficient resource in performing tax auditing, audit selection methods and suitable working environment for tax audit. Thus, the study is not without limitations. The major limitation is the absence of integrating the tax audit practice of other taxpayer's branches office.

1.7. Organization of the Study

This research paper is presented into five chapters. The second chapter is concerned with the systematic review of existing literature which provides evidence regarding the tax audit practice. The third chapter deals with the methodologies used in conducting the study. It consist of research design, data sources, sample size and sampling procedures, data collection instruments, data collection procedures and methods of data analysis. Chapter four is discusses the results and analysis of the findings of the study. Finally the fifth chapter covers conclusions and recommendations of the study.

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2. Introduction to literature Review

In the previous chapter, the main problems and objectives to be addressed in the study have been stated. This chapter presents the review of related literature. The chapter is organized in three sections. The first section reviews theoretical studies on tax audit in a tax administration system while the second section presents the empirical evidence on tax audits and related issues. The final section provides concluding remarks on the review of the literature and identifies the knowledge gap that has been addressed in the study.

2.1 Theoretical Review

2.1.1 Meaning of Tax Audit

According to Hornby (2000) Tax means “money that you have to pay to the government so that it can pay for public services”. He also defined Audit as “an official examination of business and financial records to see that they are true and correct”. The Association of Chartered Certified Accountants (2009) defined an audit as an exercise which provides assurance to the shareholders and other stakeholders of a company on the financial statements because it is independent and impartial.

Adediran et al. (2013) opined that, tax audit just like financial audit involves the gathering of information and processing it for determining the level of compliance of an organization with tax laws of the territory. For a successful audit, it is necessary that the auditor organizes his work in such a way that the assignment is accomplished completely and efficiently.

A professional tax auditor or investigator must possess sound accounting and taxation knowledge, and must be sharp in interpreting the tax laws. Moreover, the auditor and/or investigator must display high intelligence in applying tax laws, and must have sound knowledge of investigation techniques. Apart from technical skills, he/she must be alert and open minded with good communication skills.

These are necessary personal prerequisite for any tax auditor or investigator to be successful for tax audit assignments. A tax as we already know is a charge imposed by governmental authority upon property, individual or organization to raise money for public purpose. An audit on the other hand can be seen as the examination of the records underlying a financial statement as will enable the auditors to report authoritatively, whether in his opinion, the statement gives a true and fair view(Izedonmi, 2000; Okoye,2006).

A tax audit is an examination of whether a taxpayer has correctly reported its tax liability and fulfilled other obligations. It is often more detailed and extensive than other types of examination such as general desk checks, compliance visits or document matching programs (OECD, 2006a). As Biber (2010) noted, the role of an audit program in a modern tax administration must extend beyond merely verifying a taxpayers reported obligations and detection of discrepancies between a taxpayer's declaration and supporting documentation.

Tax auditors are a tax authority's 'public face' (OECD, 2006). They are the ones who implement the audit policy, interact with the different behaviors of taxpayers and determine audit outcomes (Bahl et al. 2008; Long et al.1991). They possess a great deal of discretionary power; in many instances, tax auditors are in effect prosecutor, judge and jury in tax assessments matters (Roberts, 1995). Tax auditors' tasks might become complicated when audit issues encroach on the grey area separating evasion and acceptable tax avoidance for example, the issue of transfer pricing (Reynolds, 2007) and lack of audit evidence due to a paperless system (Gilbert et al. 2001). These issues require tax auditors to understand taxpayers' business intentions and use suitable audit strategies in determining the correct amount of tax.

2.1.2 Reasons for Tax Audit

According to Erard (1994) mentioned some reasons for tax audit which include, to assist the government in collecting appropriate tax revenue necessary for budget, maintaining economic and financial order and stability, to ensure that satisfactory returns are submitted by the tax payers, to minimize the degree of tax avoidance and tax evasion, to ensure strict compliance with tax laws by tax payers, to improve the degree of voluntary compliance by tax payers and to ensure that the amount due is collected and remitted to government.

2.1.3 Objectives of Tax Audit

The objectives of tax audit are to enable the tax auditors to determine whether or not:

- i. Adequate accounting books and records exist for the purpose of determining the taxable profits or loss of the taxpayer and consequently the tax payable.
- ii. The tax computations submitted to the tax authority by the taxpayer agree with the underlying records.
- iii. All applicable tax legislations have been complied with.

Other objectives of tax audit include: to educate taxpayers on various provisions of the tax law; discouraging tax evasion; detecting and correcting accounting and/or arithmetical errors in tax returns; providing feedback to the management on various provisions of the law and recommend possible changes; identifying cases involving tax frauds and recommend them for investigation; forestalling taxable persons' failure to render tax returns; forestalling taxable person's rendering of incomplete or inaccurate returns; and encouraging voluntary compliance this is the strong reasons in support of the self-assessment scheme.

2.1.4 Types of Tax Audit

There are different types of Tax Audit which are applied in different countries based on types of tax being audited. These types of audit services are: Audit of the financial statements of the company to provide assurance on the financial statement; Compliance audit to find whether the company has complied with the required laws and regulations and Operational audit to check for the operational efficiency and effectiveness of a process.

Form the above type of tax audit service: operational efficiency and effectiveness is an audit of performance but audit of financial statement and compliance audit are mostly applied for tax audit.. However, audits can vary in their scope and the level of intensity in which they are conducted. So that, various terminologies have evolved to describe different types of audit activity.

Full audits: These types of audits are comprehensive and field audits. Given their broad scope, these types of audits are typically costly to undertake a substantial program of full audits will require considerable resources and reduce the rate coverage of taxpayers that could otherwise be achieved by a more varied mix of audit types.

i. Comprehensive Audit

Ebrill (2011) defined comprehensive audit is an examination of all information relevant to the calculation of a taxpayer's tax liability for a given period. This audit may cover all tax obligations over a number of tax periods, or extended to several years up to the limit provided for in the law. All cases where serious underreporting or evasion has been detected under any of other audits should be forwarded to a unit responsible for undertaking comprehensive audits of all tax liabilities.

ii. Field Audit

A field audit is usually carried out outside the Inland Revenue's office in the taxpayer's business premises. The need to carry it out in the taxpayer's premises is to enable the tax auditor's carry out the examination of applicable documents and also obtain appropriate information directly from the officials of the business. This takes more time and more basic documents are always required. Some documentation can also be taken down to the office for detailed verification OJONTA (2011). Comprehensive and field audits are sometimes overlapping due to their nature of audit activities.

Limited scope audits: Limited scope audits are confined to specific issues on the tax return and/or a particular tax scheme arrangement employed by the taxpayer. The objective is to examine key potential risk areas of noncompliance. These audits consume relatively fewer resources than full audits and allow for an increased coverage of the taxpayer population.

i. Desk audit or verification

As soon as a tax return is received in the Inland Revenue's office, such would be subjected to examination by the Inspector. This examination is carried out in the tax office and routine

basis indicating that most if not all the returns submitted to the tax offices are subject to this audit. The focus of the desk audit would be to ensure completeness of the items submitted for tax purposes. The Inspector carrying out a desk audit will also look for apparent errors or mistakes in the tax computations and/or in the accompanying documents and records. The outcome of a desk audit may lead to the conduct of a field audit whenever additional information or documentary evidence is required to satisfy the Inspector of Taxes carrying out the desk audit. The essence is to ensure some level of compliance with tax laws, rules and regulations as well as confirming the administrative check or returns submitted (OJONTA, 2011).

ii. Refund audit

Grandcolas (2005) noted that Refund audit should focus only on the period covered by the claim. A pre refund audit should be undertaken to verify the taxpayer's entitlement to a refund prior to processing a first refund claim particularly for new registrants. It is also carried out where the refund claim varies significantly from established patterns and trends. Audits of further claims should be carried out selectively.

Single issue audits: According Grandcolas (2005), issue oriented audit focus on a single tax type and covers no more than one or two reporting periods. Single-issue audits are confined to one item of potential noncompliance that may be apparent from examination of a taxpayer's return. Given their narrow scope, single issue audits typically take less time to perform and can be used to review large numbers of taxpayers involved in similar schemes to conceal non-compliance. In practice, the scope and nature of any audit activity undertaken for a particular taxpayer will depend on the available evidence pointing to the likely risks of noncompliance and a taxpayer's prior history. Extensive audit inquiries may also be justified simply because a taxpayer's financial and /or business activities are unusually complex.

i. Registration check

Registration check is a form of unexpected visits to taxpayer's premises for new enterprises (mainly small and medium sized) to discover businesses operating outside the tax system and a quick check on businesses to establish that they are correctly registered. It should not take

more than half a day (OECD, 2006). According to Ebrill (2001) in this visit, the tax officer ensures that the taxpayer: has a basic understanding of their obligations; keeps appropriate records (book keeping review should be mandatory in case of voluntary compliance when the turnover of the taxpayer is below the registration threshold) and Issues proper invoices when required by law.

ii. Record keeping audit

According to OECD (2006), it is unannounced visits to the taxpayers' business premises to check whether the appropriate records are kept and VAT invoices are issued. The visit points out the obligations of the taxpayer regarding the keeping of records and followed up with penalties if the taxpayer continues to disregard record keeping requirements.

iii. Advisory audits

It involves the auditors visit to newly established businesses. They advise them regarding tax types, filing of returns, payment of amounts due, record keeping to be maintained, refund claims, risk of audit and sanctions of noncompliance. These visits are very appropriate when introducing new tax laws (OECD, 2006).

Fraud Investigation: According to Krelove (2005).Fraud investigation is a type of tax audit that investigates criminal which arises from where the most serious cases of noncompliance. It helps to detect fraud, evasion, and criminal activity Fraud investigation requires special skill including meeting evidentiary requirements, seizure of evidences or records, testimony from key witnesses and preparing briefs for courts. Hence, it should be undertaken in accordance with criminal procedure laws. OECD (2004a) stated that, revenue authorities should maintain a dedicated organizational unit responsible for the handling of serious cases of tax fraud or evasion.

In practice, the scope and nature of any audit activity undertaken for a particular taxpayer will depend on the available evidence pointing to the likely risks of non-compliance and a taxpayer's prior history. Extensive audit inquiries may also be justified simply because a taxpayer's financial and /or business activities are unusually complex.

2.1.5 Tax Audit standards

In conducting a tax audit the auditor should apply the generally accepted practices of auditing as one would do in the case of other audits, e.g. an audit of a company under the companies act (Kangave, 2004). The generally accepted auditing practices are communicated in the various pronouncements of the respective country. The auditor should get the financial statements as well as the statement of particulars authenticated by the assessed before he verifies them. The auditor can apply the technique of selective verification depending on his evaluation of the internal control system prevalent in the entity under audit and the materiality of transactions.

In conducting the audit the auditor should keep in mind that the basic objective behind is to assist the authorities in assessing the collect income of the assessed. For conducting the tax audit effectively an auditor needs to develop an approach which is a synthesis of taxation laws and auditing principles. The nature of tax audit is such that an auditor has to rely on various legal pronouncements in the field of taxation.

2.1.6 The Efficiency and Effectiveness Tax Audit

Audit effectiveness is measured by examining the amount of evidence selected for examination in relation to the total available evidence and an optimal level of evidence. Audit efficiency is then defined as audit effectiveness per unit of time by taking the audit

Effectiveness measure divided by minutes spent on the task (Kangave, 2004). The key findings were that time pressure (manipulated by four levels of a time budget for the task) affected performance only at the extremes, with the highest time pressure group performing more efficiently than the auditors in the lowest time pressure group. Efficiency was also affected by audit program structure, with high structure (more detailed audit procedures listed) being associated with increased efficiency.

Apostolou et al. (1993) defined Audit efficiency as the ability to meet the budget and operationalize it as the percentage deviation between actual and budgeted hours. This research examined the effect of leader behavior on audit efficiency. Two leader behaviors;

(1) Facilitating cooperation and teamwork and

(2) Administering discipline; resulted in increased audit efficiency. On the other hand, showing consideration contributed to reduce audit efficiency (Apostolou et al. 1993).

2.1.7 Tax Audit Program

The audit program of a revenue body performs a number of important roles that, effectively carried out, can make a significant contribution to improved administration of the tax system. Most governments around the world charged with overseeing the process of tax collection from individuals and companies that reside within the jurisdiction (SD) (OECD, 2006).

A tax audit is an examination of whether a taxpayer has correctly reported its tax liability and fulfilled other obligations. It is often more detailed and extensive than other types of examination such as general desk checks, compliance visits or document matching programs (OECD, 2006a). As Biber (2010) noted, the role of an audit program in a modern tax administration must extend beyond merely verifying a taxpayer's reported obligations and detection of discrepancies between a taxpayer's declaration and supporting documentation. An important issue for any government and revenue collecting authority is to obtain knowledge and understanding of the reasons for taxpayer non-compliance.

The tax audit program provides visibility to the compliance and enforcement arm of the tax administration (Thomson, 2008). According to Tait (1988), effective tax auditing minimizes tax evasion and also helps tax agencies to achieve revenue objectives that ensure the fiscal health of the country and individual states. Additionally, Barreca et al. (2004) noted that the purpose of tax audit is to check the evasion of tax and ensure compliance in accordance with the laws and regulations.

Furthermore, a well-structured tax audit program can provide valuable support in gathering information on the health of the tax system (including patterns of taxpayers' compliance behavior), educating taxpayers (improving future compliance), and identifying areas of the tax law that require clarification or addressing deficiencies in the law (OECD, 2006a).

Accurate and timely self-assessment and compliance with tax by taxpayers is achieved only through highly visible and effective audit programs, including the consistent application of strong sanctions where noncompliance is encountered. Taxpayers must feel that there is a good chance that unreported liabilities and other forms of non-compliance have been detected during an audit (Biber, 2010).

On the other hand, if an audit program is not effective, it may result in the deterioration of tax compliance and a loss of credibility of the tax administration. Taxpayers may not be deterred from minimizing their tax liabilities if they believe that there is a little chance of being audited (Ebrill et al. 2001). A good audit program employs strategies to optimize both the direct and the deterrent effects of audits. The first can be achieved by auditing a higher percentage of the large taxpayers (Biber, 2010). Although the frequency of audit is a contentious issue, the judgment is always a delicate balance between the treat of audit to check the temptation to evade and the cost. Where the tax system is fairly well established, audits of registered traders are less cost a year to be audited. However, it is not only the crude number of audits that is the most useful measure of need (Tait, 1988).

The deterrent effect is best achieved by extending the program to as many taxpayers as possible at all levels (Tait, 1988). Through adequate audit strategy, tax administrations must foster, and not simply enforce, tax compliance. Tax compliance can be facilitated through improving services to taxpayers by providing them with clear instructions, understandable forms, and assistance and information as necessary. Monitoring compliance requires information systems as well as appropriate procedures to detect non-compliance (EC, 2006).

Developing an overall compliance strategy and programs, respectively, is critical for the tax authorities' ability to improve taxpayer compliance and to enhance revenue collection (Russel, 2010). The purpose of a taxpayer compliance program is to identify and respond to the most significant risks in the tax collection system through a range of measures aimed at the underlying causes of the noncompliant behavior.

Its ultimate objective is to achieve the widest possible impact on voluntary compliance across the taxpayer population. As part of a compliance program tax administrations should

improve revenue analysis capabilities and develop (further) indicators for tax compliance in the different tax categories. A taxpayer compliance program should be authorized at a high level, describe and prioritize resources for the most significant compliance risks and set out the detailed response by tax administration to those risks. Compliance programs are structured around major taxpayer segments (e.g., large businesses, medium-size enterprises, small and micro enterprises, and high income individuals) or types of taxes with a high risk of fraud (e.g. corporate income tax, vehicle taxation, value added tax (VAT), deductions for commuting expenses in personal income taxation) and address compliance risks relevant to these segments (Jensen et al. 2012).

The program addresses the risks in each of the taxes administered in each taxpayer segment and describes how the revenue agency intends to respond to these issues and risks in an action plan. Risk-based verification programs segmenting taxpayers into co-players and opponents have proved efficient. Segmenting taxpayers improves compliance behavior by detecting and deterring non-compliance through the use of risk management approaches. Taxpayers are more likely to comply if they perceive the likelihood of detection as high and see blatant non-compliers being brought to account.

Therefore, voluntary compliance is generally enhanced by increasing the number of taxpayers audited than by auditing fewer taxpayers with large tax potential. Perversely, revenue is increased by concentrating on those taxpayers where a large amount of revenue is at risk. But there should be a careful planning when there is a widespread belief that most tax returns are underreported, otherwise there may be an over selection of returns for audit, with the result that the inventory of work in process may increase to unmanageable proportions and make an orderly approach to an annual audit work plan impossible (Tait, 1988). Thus, the actual number of audits planned should depend on the audit resources available to the program. Thus, the actual number of audits planned should depend on the audit resources available to the program. The international standards as to the total staff assigned to audit should be close to 40 percent of the total staff of the tax administrations (Biber, 2010).

According to Biber (2010), effective planning is required to ensure that the audit program is adequately developed to: focus on and address the most significant risks, target

noncompliant taxpayers and not harass compliant taxpayers, make optimal use of limited resources and influence compliance across the broader taxpayer community.

According to OECD (2006), effective audit plan should be:

- Flexibility to allow for unusual audit issues, adequacy of internal controls and the adequacy of books and records;
- Alignment with any quality assurance framework; and
- A clear focus, with potential areas of concern noted during the preliminary review and audit procedures selected that can address the concerns

2.1.8 Audit Case Selection of Taxpayer

The roll of revenue authority is to manage and improve compliance with the tax laws, and in the process sustain confidence in the tax system and its administration. The tax audit can play a major role in improving tax administration and overall taxpayer compliance by impacting on taxpayer behavior. In addition to raising revenue directly from audit activities, by selecting the highest risk cases, efficiently detecting non-compliant taxpayers, applying appropriate sanctions, and publicizing results of audit activity (either generally or specifically), taxpayers get the message that any attempt to avoid tax presents a high risk of detection and the penalty for non-compliant taxpayers is substantial. Tax audits therefore provide the tax administration with important power across the community rather than only impacting on the taxpayer selected for audit and collecting the tax that should have been paid in the first place. Compliance risk is the failure to comply with the tax law by taxpayers whether due to their ignorance, carelessness, recklessness, deliberate evasion, or weaknesses in tax administration itself, and have been addressed only by enforcement through an audit-based approach (OECD, 2004a).

Compliance risk is the failure to comply with the tax law by taxpayers whether due to their ignorance, carelessness, recklessness, deliberate evasion, or weaknesses in tax administration itself, and have been addressed only by enforcement through an audit-based approach (OECD, 2004). However, tax administrations do not have sufficient resources to perform

thorough on-site audits of the activities of all taxpayers or comprehensive crosschecking of all invoices or transactions. Tax administration, with limited resources and relatively large numbers of taxpayers to administer (especially in the small and medium enterprises), must design the audit program to deploy audit resources in a risk-based way with a view to achieve the most possible compliance and revenue objective (Thomson, 2008; OECD, 2004). Regardless of how automated and efficient the audit process, audit effectiveness would not be realized under the selection of inappropriate audit candidates (Milack undated). According to Barreca et al. (2004) hence, managing an effective auditing program involves decisions as to the selection of best audit case strategy or combination of strategies. The selection strategies may vary by tax type. It may be based on either reported tax amounts or the industry type

Case selection through the use of risk management techniques is necessary to ensure that the audit program is fully in line with the administration's compliance strategy, and to set up the necessary audit trails to show why cases have, and have not, been made the subject of an audit (OECD, 2006). Ebrill et al. (2001) stated that the most effective systems utilize taxpayer profiles and criteria to identify the highest risks for the revenue. These systems are frequently based on the crosschecking of internal information. In tax administration, a risk is anything that can negatively affect the administration's ability to achieve its compliance and revenue objectives. Risk management is a formalized and systematic approach, based on sound analysis, designed to set the best course of action under the uncertainty of risk. The technique involves identifying, assessing, understanding and acting on risks that impinge on the organization's ability to achieve its objectives (Thomson, 2008).

Risk management starts with risk identification, which includes a rough estimation of the risk related tax gap, the number of taxpayers involved and possible relations with other risk areas (EC, 2006). The tax gap (the potential tax yield minus the actual tax revenues) reflects the financial extent of the risk field. Although the determination of the tax gap is not easy, a rough estimation is usually done. The calculated gap can be further broken down into areas such as barely legitimate tax avoidance, fraud, serious noncompliance, error, and debt. This provides additional information on areas of risks that should be addressed. Strictly theoretical, the sum of the aforementioned individual risks identified must be equal to the

entire tax gap (EC, 2006; EC, 2010). According to EC (2010) and Thomson (2008), compliance risk reduces tax yield, and can be categorized as register risk, filing risk, payment risk, and declaration risk. This classification makes tax administration in a stronger position to determine the appropriate treatment technique.

Register risk includes reduction of tax yield because ineligible taxpayers for tax registration become registered and/or remain registered when eligibility ceases, fail to register by those that fulfill registration requirements, and registration with erroneous information. Payment risk and filing risk are closely related but they should be analyzed separately since the treatments may vary. Payment risk is non-payment of amounts due on tax returns and assessments whereas filing risk is failure of taxpayers to file their returns by the due date. In order to provide the correct preventive and corrective treatments there is a need to be able to target those taxpayers likely to file their returns late, or not at all. Finally, declaration risk is a risk that the amounts shown on the tax return are incorrect by error or deliberate act and many tax administrations traditionally concentrated on this risk area with the intention of determining which cases should be selected for conducting audit activity (EC, 2006; EC, 2010). In addition to compliance risk identification, in an efficient audit management structure, there are pre-audit case management factors that need to be recognized to assure the taxpayers in that the burden of audits not fall disproportionately on any segment. These include inappropriate auditors' contact with taxpayers, audit cycle or enquiry window, materiality, and collectability (OECD, 2006).

Inappropriate auditors: according to OECD (2006), it is useful to have regulations to preclude individual auditors from repeatedly auditing the same taxpayer and to require an auditor to exclude itself from taking up an audit where they are acquainted with the taxpayer selected for audit. Such rules protect both auditor and the customer from the danger of such inappropriate contacts. The policy of repetitive audit procedures (RAP) may be used which holds that if a taxpayer is audited for non-business issues only (similar to an audit aspect) for the current year and the audit results in no additional taxes owed, the taxpayer is granted relief from audit for the next two years if no substantial changes take place. The intent is to eliminate non-productive and time-consuming audits for tax authorities and to reduce the hardship associated with repetitive audits for fully compliant taxpayers.

Audit cycle or enquiry window: OECD (2006) stated that, Regulations may be established to require that all audits must be started or completed within a predetermined timeframe. However, it gives certainty to taxpayers that after some period of time the danger of audit may pass. Thus, it needs to be supported by powers of discovery to overturn the enquiry window where substantial tax fraud is found

Collectability: The collectability concept implies that a taxpayer's inability to pay a future proposed tax assessment would be sufficient basis for not conducting the audit. Those administrations that do not use this concept report that collectability is a secondary objective and should not diminish the primary objective of a correct assessment of tax liability. In addition, the limitation of collectability considerations to the current tax period may not provide a complete financial picture for the taxpayer as it excludes consideration of future payment potential (OECD, 2006).

Materiality: According to OECD (2006), business selected for audit was based on the level of noncompliant high-risk; the materiality of the projected tax consequence versus the auditor's labor cost of pursuing the high-risk item may override the non-compliance aspect.

Audit selection methods range from simple random selection to more complex rule-based selection, sophisticated statistical and data mining techniques. Selection strategies can vary by tax type and even within a single type. The common case selection methods include random selection of cases, screening or case review by auditors, rule base and automated risk scoring systems, and data mining and statistical analysis (Barreca et al. 2004).

Random selection: It has no bias in audit case selection, and useful to fight corruption. This method is perceived as fair by taxpayers. However, it clearly not focused on highest risks, may have high opportunity cost if used as sole case selection method (Vellutini, 2010).Gupta (undated) noted, simple random selection has a major drawback in that both honest and dishonest taxpayers are equally treated since probability selection give equal chance of being selected for both. However, the criteria or information based selection system too has a drawback in that it presupposes certain clue of noncompliance, which may actually be sign of other things such as change in economic condition in that particular trade(OECD, 2006).

Screening or case review by auditors: It is the traditional method by which audit cases have been selected, and dates from the time when there was little or no IT support, the data available was in any case limited, and the compliance risk management techniques at a strategic level less well developed. Such a methodology has a benefit that it makes full use of local knowledge, creates significantly less caseworkers resistance, can be used to attack specifically defined risks and can be operated substantially without IT support (OECD, 2004a ; OECD, 2004b). Vellutini (2010) noted that, Manual selection of audit cases is based on the auditors own knowledge of the taxpayers' behavior and environment. However, it cannot find out patterns of noncompliance hidden in the history of noncompliance in the same area, sector, or as determined by other taxpayer attributes. It also favors rent seeking and corruption in the tax administration since it is discretionary and subjective approach.

Automated and rule base risk scoring systems:It allows for the bulkprocessing and risk assessment of returns data. The data is reviewed against a set of risk indicators and the results be ranked in terms of the risk of noncompliance identified. Such system is an essential tool in facilitating the exclusion of bulk of returns with no or very low identified risks and allowing the resources for risk identification to concentrate their efforts only on those cases with significant identified risks (OECD, 2004a). However, this system has its own inherent perception. First, many of the rules by which a case is scored are dependent on financial ratio analysis and other industry benchmarking that can be changed overtime. The rules also may be, in themselves, standard factors to be achieved when they become known within the population. Thus, attention needs to be given to continually update the risk rules. Second, the rules need to be responsive to the local knowledge of the front line staff who is working on the cases when selected. Final case selections need to be able to reflect the local knowledge of the caseworkers themselves whilst retaining appropriate propriety within the case selection system. Automated selections with no opportunity to be influenced such local knowledge can create resistance and lead to suboptimal working once the cases are underway. In addition, the risk rules need to be responsive to the knowledge gained by front line workers from working their cases. Such knowledge can be about new risks, changes in commercial behaviors, or new technical tax devices and the impact of that knowledge can be significantly leveraged if it can be captured within a flexible and developing set of risk rules. Third, the

rules should bring together from dissimilar sources such as tax returns, third party information, and public domain information from internet. This level of analysis requires considerable investment in IT resources. Finally, the rules need to have the capability to be changed reasonably and quickly to take in to account new strategic appreciation of compliance risk. Once again, if the rules are themselves hardwired in to IT coding then this may be a resource intensive business (OECD, 2004).

2.1.9 Examination Techniques

Biber (2010) stated that, there are different approaches to investigate and review the organization record depending on up on the area of risk, nature of the tax payers operation and the tax payers' condition. The decision regarding the type of tests to be undertaken as well as the records needed by the auditor to address specific issues is influenced by the nature of the taxpayer's operations, adequacy of books and records and materiality of potential adjustments. OECD (2006) indicated that there are different techniques used for tax audit examination. Those are analytical review, investigative approach, field examination and counter party examination

Analytical review: An analytical review of financial statements and returns are often completed during the preliminary stages of the audit. Ratios, such as gross profit and inventory turnover are used to test the accuracy of taxpayers' reported sales, cost of sales, or ending inventory. The unusual variances (abnormal deviation of calculated ratios from the previous experience) are noted and addressed during the interview with the taxpayer and additional audit procedures developed where necessary (OECD, 2006).

Investigative approach: Auditors are encouraged to use an investigative approach in their audits. Such an approach uses information obtained through observation, discussion, documents or records obtained from either the taxpayer or other sources. It requires judgment, imagination and using information outside the accounting records to perform the audit (OECD, 2006).

Field examination: according to OECD (2006), this is utilized when information gathered on significant events such as underhand trade, disguised transaction and other data concerning

transactions. The examination also include on sight survey of the current conditions of the taxpayer's business through physical checks of original transaction records and vouchers, assets and liabilities and other aspects of the business.

Record examination: The main approaches to detect false accounting include the examination of books and documents conducted at the taxpayer's business office or branches, counterpart examinations and examination of savings and deposit accounts (OECD, 2006).

Counterpart examination: It is an examination performed based on third party information where warranted. OECD (2006a) stated, information can be obtained during the course of an audit from third parties to verify the taxpayer's income, for example: Financial institutions and public companies information on interest and dividends matched with what taxpayers report in their tax return, information from Government regarding social benefit payments, and employer information concerning salary and wages paid and tax deducted, both for income and non-monetary benefits.

2.1.10 Audit Workforce Capabilities

According to OECD (2006a), revenue bodies must manage and develop their audit workforce to deliver their planned outcomes through increasingly designing and implementing capability or competency models. Capability or competency model refers to a formal specification of the skills, knowledge and attributes of staff that are required to perform a specific job in an efficient and effective manner. The model generally contains job descriptions, functional descriptions and competency profiles using task-related competencies. It is typically supported by training and educational requirements to ensure and build capability. Different capabilities are required for work performed in different market segments or on clients exhibiting different behaviors towards tax compliance. Typical points of difference are capabilities required for noncompliant aggressive clients, audit work with large businesses (deeper and more specialized knowledge about specific regulations is required for this segment), performing system and electronic data base audits, and conducting criminal and fraud cases (OECD, 2006b).

According to OECD (2006a) the required capabilities of auditors are generally identified by analyzing the activities required to perform particular audit tasks and through practice and experience. In addition to their primary role of detecting and deterring noncompliance, tax auditors are often required to interpret complex tax laws and conduct intensive examinations of taxpayers' books and records. Hence, revenue bodies pay close attention to the overall management of the tax audit function and particularly to the strategies and methods used for recruiting, developing and managing individual audit staff. Thus, tax auditors should have a capability to: conduct investigations, determine compliance, tax accounting and financial analysis, conduct research and analysis, make effective decisions under the law, effective communication, apply work processes and procedures, and manage own work and relationships (OECD, 2006b).

Capability gaps: According to OECD (2006), revenue bodies may develop staff and address capability gaps through recruitment processes and the use of programs such as training and development programs, mentoring and coaching programs, accreditation models, job rotation and/or placement programs, career paths, knowledge sharing initiatives and knowledge tests. Capability gaps are typically gathered from various sources including quality management system results, performance system interviews and appraisals, client professionalism, satisfaction and other similar surveys, and training program evaluations

Competency assessment: It is important for tax administrations to assess and evaluate the competencies of their staff. The direct manager commonly performs competency assessments during recruitment and promotional processes on an annual or semiannual basis for those staff maintaining current positions (OECD, 2006a). Assessments performed as part of recruitment processes are often performed by external specialists, human resource departments and/or panels of internal subject matter experts. Other events triggering capability assessments include prior to performing a new type of work, prior to starting a new role, and ongoing informal assessments and learning and development activities (OECD, 2006).

2.1.11 Working Environment

Rehaman (2012) argued that future opportunities for the employees also help in retaining employees because these opportunities are associated with more pay, additional work responsibilities, superior work environment and different incentives plans. Enhancing open lines of communication between managers and employees can improve the overall quality of working relationships. Many interventions designed to make the workplace more hospitable can lead to improved retention (Griffeth et al. 2001).

Administrative transparency can assist not only in achieving high voluntary tax compliance, but also in reducing opportunities for corruption by tax officials. Standardized procedures and electronic and physical tax forms, which are made widely available to taxpayers, limit one-on-one contact between tax officials and taxpayers.

The tax administration must include policies and procedures to detect and deter corruption. All plans and operations should be designed to make corrupt practice difficult and to provide for accurate records of all transactions, their underlying motivation, and the offices and individuals responsible for all actions.

The auditing service is therefore an ethical issue in collecting government revenues and the auditors flow from the code of ethics which includes discipline, loyalty, honest, courage and tact.

Training

It is vitally important that staff receive appropriate training for the duties they are expected to perform within the tax administration. As tax laws become more complex over time and taxpayers learn new techniques, training should become an ongoing activity, not just a one-off action for new recruits.

It is also important that managers are able to differentiate between honest mistakes made by inadequately trained staff and deliberate errors designed and made for rent-seeking purposes. Ethics training, therefore, should be included as a part of continuing professional education. Moreover, if the risk of unethical behavior is great, the frequency of training should be

increased. In any event, ethics seminars and courses should become an integral part of the training curriculum, forming a part of initial orientation of new staff and becoming a staple of ongoing professional education.

Employment Conditions

Staff from the top to the bottom needs to have a degree of job security and know that the organization has fair personnel policies. Unfair practices will only further alienate discontented staff, who may then use a perceived lack of fairness as a justification for unethical behavior. The quality of managers, tutors, and mentors is a vital element in setting new hires off along the right road. In the absence of adequate selection processes and training, there is a risk that a lack of integrity will develop in new recruits.

Professional advancement within the administration must be based exclusively on merit and qualifications, free from political influence and private connections. In any tax administration, there must be a clear career path for officers to permit staff to have a realistic view of potential advancement.

Job satisfaction

Job status may play an important role in reducing turnover and organizations use it as a career reward and incentive to retain qualified employees (Zhao et al. 2008). Employees who are placed in jobs that are too difficult for them or whose skills are underutilized may become discouraged and quit. Inadequate information about skill requirements that are needed to fill a job may result in the hiring of either under skilled or overqualified workers (Handelsman, 2009).

According to Clarke et al. (2000) effective career management is that at all levels in the organization there are well qualified workers who can assume more responsible positions as needed and that as many members of the organization as possible are highly motivated and satisfied with their jobs and careers.

2.2 Empirical Review

Mesfin (2008), examined Tax Audit Practice And Its Significance In Increasing Revenue In Ethiopia The Case Of Addis Ababa City Administration and recommends among others it is clear that most taxpayers of any country do not want to pay taxes unless compelled by a situation where they are left with no option other than to pay the taxes. Therefore, for better tax compliance, a system should be designed that automatically extracts taxes rather than leaves the payment of taxes to the voluntary choice and morality of taxpayers. To this view tax audit is one of the most powerful revenue administration tool that enforces tax payers to pay their tax liability without evasion. Therefore the tax audit function should be strengthened to minimize both deliberate and innocence tax evasion made by many tax payers with appropriate expertise and the necessary resources should be allocated for this tax administration function.

Ibrahim et al. (2014) examined the contribution of tax audit and investigation to the sustainable development of the Nigerian economy and concluded that the practicing accountants should uphold the fundamental principles of professional ethics while rendering consultancy services since they often act for taxpayers in their dealing with the relevant tax authority.

Afubero et al. (2014), examined impact of taxation on revenue generation in Nigeria and recommends among others that Well Equipped Data Base in all tax payers should be established by the Federal, State and Local Governments with the aim of identifying all possible sources of income of tax payers for tax purpose however the tax collection processes must be free from corruption.

Getaneh (2011), examined Tax Audit Practice in Ethiopia: The Case of the Federal government and recommends among others ERCA should sufficiently use an investigative approach to check the accuracy of tax returns to establish what have not been recorded in the accounting system. It should use an investigatory approach to establish the completeness, accuracy, timeliness, credibility and validity of taxpayer's declarations, disclosures, and other financial arrangements.

Adediran et al. (2013), examined The Impact of Tax Audit and Investigation on Revenue Generation in Nigeria and conclude that Tax audit and investigation should be embraced as it has a dual purpose or benefit. On the part of the taxpayer, it serves as a check on the proffers guiding tax administration and also helps in strengthening the activities of the taxpayer. To the authorities, it maximizes the collection of revenue which enables the government addresses developmental projects that will benefit its citizenry. Generally, it serves as a reminder to all parties that it does not pay to engage in deliberate tax evasion. Tax audit and investigation are critical to causing the tax payer to be on their toes. This is particularly true for the taxpayer who is marginally complying and can easily be moved to the realm of tax evaders. He recommended that Tax audit and investigations should be carried out more often and as thorough as possible to accomplish its task of increasing the revenue base and stamping out tax evasion in the country.

Netsanet (2014), examine assessment of tax audit practice: the case of Hawassa city administration and conclude that to achieve the objectives of government revenue objective a well-structured tax audit program is vital to ensure the fiscal health of the country, and sustain the health of the tax system by reducing tax gap through voluntary compliance improvement and additional tax collections. Further, it might provide valuable support in identifying areas of the tax law that require clarification or addressing deficiencies in the law, and to influence compliance across the broader taxpayer community at all levels. Hawassa City Revenue Authority audit used intensively comprehensive audit and the Audit program is unchanged and not used different types of audit in relation to simplicity and complexity of cases. Taxpayers are selected for audit based on risk criteria, and selected audit cases are expected to be performed within 15 days period regardless of the complexity of audit cases and the size of the taxpayers. Taxpayers might be repetitively audited if there is an indication of serious tax fraud and when they report less tax return than previous return. As a result, there is unreasonably consumption of audit resources as well as increase the hardship associated with repetitive audits for fully compliant taxpayers. Corruption might also arise due to repetitive contact between the same taxpayers.

Eugene (2011) study in Ghana and conclude that regarding processes, the Unit performs virtually all processes manually; this seriously hampers accountability and transparency in

the tax system, as well as the effectiveness and efficiency of the audit practice and tax collection. It also impairs supervision and access to many sources of information. Even though the employees in the unit have the necessary skills which enable them to perform their duties and responsibilities, there is the need for adequate short term and refresher training to keep them abreast with current trends of auditing and investigations and also the numerous amendments to the tax laws. The other important issue which should be seen seriously is that, the prevailing tax audit practice as seen in Domestic Tax Revenue Department of Ghana Revenue Authority is carried out mostly based on documents produced by tax payers, these internally produced documents cannot be a wholly reliable source of information for tax purposes there is therefore the need to tool the unit to be able to source for third party information for verification and authentication of audited records. Furthermore, even though the tax audit is performed by tax auditors mostly in the tax payers premises, there is the need to expand and improve on the number of field audits and in order to improve the efficiency and effectiveness of audit operation and to make a better impact on domestic revenue collection.

As per Mirera (2014) studied in Kenya and conclude that tax audit actually has an effect to revenue collection as according to the t-tests there is significance in the correlation between tax collected before the audit and after the audit. This clearly indicates that tax audit increases revenue collection. That in essence means that the more the tax audit conducted the more revenue is collected. Thus it is right to say that tax audit is directly related to revenue collection. All the tax audits are important because they add something to revenue and thus should be encouraged as it assists the government in collecting appropriate tax revenue necessary for budget, maintaining economic and financial order and stability, to ensure that satisfactory returns are submitted by the tax payers, to organize the degree of tax avoidance and tax evasion, to ensure strict compliance with tax laws by tax payers, to improve the degree of voluntary compliance by tax payers and to ensure that the amount due is collected and remitted to government.

Samuel (2016), examined Tax Audit Practice and its challenges : The Case of the Large Taxpayers Office and recommend that ERCA should improve audit standard, the public awareness of the importance of tax payment. Tax audit should get support from the

intelligence and investigation department when needed so that audit could be done based on risk management and penalties should be used taxpayers' education and services in order to achieve greater compliance. ERCA should improve the network quality in collaboration with the concerned government body which is the serious problem in providing fast services to its customers and case for audit should be selected using data from SIGTAS rather than screening committees so that biasness can be minimized. Tax audit should aimed at reducing the problems of tax evasion, tax avoidance and other tax irregularities for standardization to improve the level of filing, payment and reporting compliance by supporting taxpayers how to file, report and how to settle payments. Tax authority should continuously review the tax laws by collecting information from the tax auditors and other stakeholders so that the loophole of the laws can be addressed without adversely affect the tax revenue of the government.

2.3. Conclusions to the literature review and knowledge gap

In the theoretical review, to the knowledge of the researcher there is no adequate literature regarding in the perception of tax audit practice. The empirical studies that have been reviewed in this research paper focused on the different tax audit activities.

Depends on numbers of empirical studies which have been made in national level on tax audit and related issue, the researcher concludes that there are no adequate studies in the perception of tax audit practice. The study by Mesfin (2008) specific to Tax Audit Practice and Its Significance mainly focused In Increasing government Revenue in Ethiopia the case of Addis Ababa City administration. The study by Netsanet (2014) examines assessment of tax audit practice: the case of Hawassa city administration and focused on the achievement of objectives of government revenue and about structured tax audit program. On the other hand Getaneh (2011) examines tax audit practice in Ethiopia the case of federal government that focused on investigate tax audit operation by the case of the federal government in Ethiopian tax system.

These three studies did not broadly examine issues regarding the perception of tax audit practice development by considering issues like types of audit program performed, audit case selection approaches, capacity and experience of tax auditors and suitable and free working

environment of tax auditors in Ethiopia. Based on these gaps in the literature together with the problems stated in chapter one, the following main research question is developed. “How are the perception of tax audit practice in ERCA-LTO in respect of the type of audit performed, audit case selection methods used, the experience, capacity and quality of audit staff resources and conducive working environment?” and the next chapter discusses the research design and research methods that are implemented for the study with suitable reason for the selection of appropriate research methods.

CHAPTER THREE

RESEARCH METHODOLOGY

This chapter discusses the processes and techniques to be used in carrying out the study. It also provide an outline of research design and the instruments for data collection.

3.1. Research approaches

According to Creswell (2009) there are three basic types of research approaches such as quantitative, qualitative and mixed methods approach.

Quantitative research generates statistical data through the use of large scale survey research, using methods such as close-ended questionnaires and/or structured interviews. In quantitative approach data is collected through questionnaire survey and the results can be quantified with the help of statistical tools. In this approach it is possible to compare and study several determinants and analyzing and testing them empirically to prove if there are relations to be found in order to draw conclusions.

According to Kothari (2004) qualitative approach have an emphasis on understanding, observing and interpreting the data in a natural setting and with a sort of insider's view. In this study, the researcher used both quantitative and qualitative approach (mixed approach) in collecting and analyzing data was adopted..

3.2. Research Design

The purpose of this research is to investigate the Perception of Tax Audit Practice: evidence from Ethiopian Large Tax Payers Office (LTO). This section explains the research design and methodology that were applied to achieve this objective.

According to Kothari (2004), descriptive research includes surveys and fact-finding enquiries of different kinds. The major purpose of descriptive research is description of the state of affairs as it exists at present. Therefore, the researcher was conducted using descriptive research method. In conducting this study, both primary and secondary sources of data were

used that a describe research design, data and characteristic about what is being studied. Descriptive survey also enables to obtain the current information. It is also used in fact finding studies and helps to formulate certain principles and give solutions to the problems related to concerning issues. Descriptive survey method focuses on investigating the current status, related to the perception of tax audit practice of ERCA Large Tax Payers Office (LTO).

3.3. Data collection instruments

This thesis has an objective of describing the applicability of the type of tax audit program, audit case selections method, audit resources and it's suitable and free working environment. Thus, to achieve this objective, the study was using both primary and secondary data which were collected from ERCA LTO.

Regarding the primary data source, the researcher was tried to obtain information through direct personal interview with tax audit processor owner and questionnaires comprise mainly close and some open ended questionnaires were distributed to tax auditors, and secondary data from different sources like the ERC-LTO tax audit manual and annual bulletins of different publication as well as internet site browsed were used.

3.4. Population and conduct of the census

As per the data that researcher found from large taxpayers office (LTO) human resource department, currently, the office has 467 employees and 770 large tax payers whose annual turnover is 80 million birr and over. The population under this research comprised ERCA-LTO audit officers. The reason in which this research work based on this ERCA-LTO is that the largest tax collection of ERCA which contributes up to 75% of annual domestic tax collection as of 2016/17 is made from this branch. Hence the audit program, audit resources and working environment should be organized than the other branches, which is focusing the researcher on this branch.

This research was working on single department which is tax audit office in ERCA –LTO and the number of auditors in this branch was 98 and the research was conducted to all

auditors. The reason for selecting is that they are a close attachment with tax audit functions and deep knowledge in the area of the study. Thus, questionnaires were distributed to all auditors.

3.5. Data Analysis Method

The research used descriptive data analysis method using software of STATA which is a general-purpose statistical software package that enables users to analyze and manage data collected by researcher and to present the outcomes of the result. To make all the data collected and stored meaningful and consumable appropriate analysis was made by using tabular and percentage form of presentation accompanied by relevant explanation.

3.6. Reliability and Validity Tests

Reliability

Field (2009) explained reliability as “a means that measure (in this case questionnaire) should constantly reflect the construct that it is measuring”. “Reliability refers to the consistency and stability of findings that enables findings to be replicated” Cronbach’s Alpha is very useful in developing attitude scales and questionnaires as the alpha level (or reliability) indicates if the items are measuring the same construct. Items that are not measuring what the rest are can be identified and deleted. Cronbach’s Alpha Should is over 0.70 to produce a reliable scale and any scale less than this alpha coefficient should be eliminated according to Field (2009).

Table 3.1. Reliability analysis

Average inter item covariance	.2629756
Number of items in the scale:	51
Scale reliability coefficient:	0.88

Validity

Whilst reliability relates to the accuracy and stability of a measure, validity relates to the appropriateness of the measure to assess the construct it purports to measure (Field, 2009). To make the study valid the researcher used different techniques such as preliminary survey to ensure the measurement and assessment of the real situation. The content of the items were also analyzed with the help of experienced peoples and literatures related to tax audit. Moreover, to make valid and predictive the outcome of the study, the researcher was distributed personally each questionnaire by communicating and convincing all respondents the purpose of the study.

3.7. Ethical consideration

When questionnaires were distributed the researcher informed respondents on the introduction part of the paper about the title and objective of the study. Besides, to develop respondents confidence they were informed that their responses to be kept confidentially and the information uses only for academic purpose. To avoid misunderstanding and problems related with questionnaires in acquiring information from tax auditors the researcher design of the questionnaires is clear and understandable manner.

CHAPTER FOUR

RESULTS AND DISCUSSIONS

4.1. Survey Results

The questionnaires were distributed to all tax auditors. 98 questionnaires were prepared and distributed to the above respondents. Out of 98 questionnaires distributed to the respondents, 86 respondents were completely filled and returned the questionnaires. As Getaneh (2011) stated, the response rate of 84.6 percent was rationally fine. For this study the response rate was 87.75 percent and 12.25 percent of the questionnaires were not returned at all due to their different reasons. The remaining discussion in this section presents the survey outcomes regarding respondents' background information, types of tax audit program, audit case selection methods applied, audit resources, conducive working environment and taxpayer characteristics during audit and the capability and experience of tax auditors in particular.

4.2. Background information of respondents

4.2.1. Gender Information

Out of the total respondents, 60.47% were males and 39.53% were females. This implies that male were highly involved in the study. However there is no biased in the survey instrument related to gender and it is the composition of the gender in the branch that makes male participation were high (Table 4.1).

Table 4.1 Gender information

Gender	Count	Percent
Male	52	60.47
Female	34	39.53
Total	86	100

Source: Survey outcomes, 2018

4.2.2. Age of the respondents

The majority of respondents (74.42%) were under the age category of between 26-35 years, and the second frequent age categories of 12.49% were under 25 years and 6.98% of respondents were in age category of 36-45 years and 5.81% of respondents were in age category of 46-55 years (Table 4.2). The age bracket showed that the respondents were consisting of various groups which enabled the researcher to get different response across the same topic. Moreover, the survey indicates that, the administration has been performed by the young and energetic group of audit staff.

Table 4.2 STATA output for age group

Age Group	Count	Percent
less than 25 years	11	12.79
26-35 years	64	74.42
36-45 years	6	6.98
46-55years	5	5.81

Source: Survey outcomes, 2018

4.2.3. Educational level and Field of study

Regarding educational level, 81.40% of respondents were BA degree, 16.28% of respondents were MSc/MA and above and 2.32% attended diploma (Table 4.3). In addition the survey result revealed that the respondents studied Accounting and finance were 54.65%, Management 26.74%, Economics 10.47% and the rest 10.14% of respondents studied other fields (Table 4.3). Here, the majority of respondents studied accounting and finance followed by management and economics fields which shows their knowhow with the subject matter addressed in the study.

Table 4.3 STATA output for educational level and field of study

Variables		Count	Percent
Educational status	Diploma	2	2.32
	BSc/BA	70	81.40
	MSc/MA and above	14	16.28
Field of study	Accounting Finance	47	54.65
	Economics	9	10.47
	Management	23	26.74
	Others	7	8.14

Source: Survey outcomes, 2018

4.2.4. Job Occupation

Regarding current job occupation, 61.63% of respondents were tax auditors, 13.95% occupied other positions (senior tax auditors), 11.63% of respondents were junior tax auditor, 8.14% were tax investigators, 3.49% were tax audit coordinators and the rest 1.16% was tax audit head (Table 4.4). This study tries to incorporate all LTO tax auditors from tax audit processor to junior tax auditors for data analysis purpose. Based on this result, the majority of the respondents were tax auditors.

Table 4.4: STATA output for current job occupation

Variables		Count	Percent
Current job occupation	Junior tax auditor	10	11.63
	Tax auditor	53	61.63
	Tax investigator	7	8.14
	Tax audit coordinator	3	3.49
	Tax audit head	1	1.16
	Others	12	13.95

Source: Survey outcomes, 2018

4.2.5. Selection criteria to be an auditor in LTO

Tax auditors were selected for their current job position based on related to their field of study 43.03%, training and exam attended 41.86%, past work experience 38.36% and level of education 15.11% (Table 4.5). The survey result showed that, most of the respondents was hired based on their field of study, training and examination as well as past work experience. Similarly the same answer was obtained during interview with tax audit processor owner. This study result is consistent with the research done by Getaneh (2011) studied at ERCA federal level.

Table 4.5: STATA output for selection criteria to be an audit staff in ERCA-LTO

The criteria to be selected an auditor	Frequency	Percentage
Related to past working experience	33	38.36
Based on exam and training	35	41.86
Related to field of study	37	43.03
Related to level of education	13	15.11

Source: Survey outcomes, 2018

* Multiple answers were possible

**Figures do not add up

4.2.6. Audit Experiences

Regarding to auditors' past experience, the survey result showed that 61.63% of the respondents have no any audit experience before employed as tax auditor at LTO and 38.37% were have experience in other sector. Out of 38.37% past experience: 13.95% of the respondents has less 2 years of experience, 10.47% has 4-7 years of experience, 9.30% has 2 -4 years and 4.65% above 7 years of experiences before employed at LTO (Table 4.6).

On the other hand, out of the total audit staff, 56.98% of the survey respondents have tax audit experience of less than five years in their current job position and 6.98% of the respondents have above 8 years of tax audit experiences (Table 4.6).

When the study investigated the reasons for the less availability of the senior auditors in the branch, the researcher interviewed the tax audit head and obtained the following reasons. Most auditors leave from their position after two to five years of work tax audit experience due to various reasons such as: workload without additional benefits, absence of freedom, suitable and free working environment, absence of satisfactory allowance for their duties and uneven compensation payment for similar field activities, and absence of performance based promotion.

Table 4.6. STATA output for work experience of tax auditors.

	Characteristics	Freq.	Percent
Experience before employed at ERCA	Yes	33	38.37
	No	53	61.63
Year of experience before employed at ERCA	No audit experience	53	61.63
	less than 2 year	12	13.95
	2-4 years	8	9.30
	4-7 years	9	10.47
	above 7 years	4	4.65
Current experience at ERCA-LTO	Less than a year	14	16.28
	2-5 years	49	56.98
	5-8 years	17	19.77
	above 8 years	6	6.98

Source: Survey outcomes, 2018

4.3. Types of tax audit performed

The survey results showed that, 81.40% of LTO exhaustively conducts comprehensive audit. In addition, 20.93% and 19.76% of the branch conducted fraud and field audits respectively (Table 4.7). As ERCA Domestic Tax Audit Manual 2014 stated that, the major type of audit performed at ERCA are: Comprehensive audit, Issue audit, Desk audit, Advisory Visit audit, Investigation audit, Refund and De-Registration audit. However, comprehensive type of audit were mostly performed at ERCA.

In addition, as per the information that the researcher obtained from interviews and document reviews showed that large number of tax audit type performed by the branch was comprehensive audit and it is conducted using five-year taxpayer information to check whether taxpayers filed and paid the appropriate tax returns in line with the tax law and accounting principles, investigation audit which is a serious cases of non-compliance with criminal implications and require special skills in investigation audit and sometimes field or desk audits are performed.

Table 4.7: STATA output for the types of tax audit performed in ERCA-LTO

Types of audit	Freq.	Percent
Field audit	17	19.76
Comprehensive audit	70	81.40
Fraud audit	18	20.93

Source: Survey outcomes, 2018

* Multiple answers were possible

**Figures do not add up

Regarding the documents reviewed that the branch planned to audit 180 taxpayers in 2010EC, but actually accomplished 131 taxpayers with a total collection of Birr 6,257,052,189.00. However, as interview showed that 60 percent of audited taxpayers' were appealed.

Table 4.8. Outcome of the actual audit report

Audit type	No. of taxpayers audited	Additional tax assessed	Interest	Penalty
Comprehensive Audit	83	2,473,666,019.00	1,398,397,594.00	2,193,248,878.00
Fraud Audit	12	78,438,354.00	49,241,434.00	14,207,586.00
Field Audit	36	27,559,421.00	17,301,044.00	4,991,854.00
TOTAL		2,579,663,794.00	1,464,940,073.00	2,212,448,318.00

Source: LTO Audit Report (2010E.C)

4.4. Selection criteria for tax audit and its reasons for selection

The study noted that, 63.95% of respondents replied that construction and real estate sectors were frequently audited by the branch tax auditor and 61.62% were manufacturing sector, 41.85% were merchandise sector followed by service sector of 31.39% (Table 4.9).

As per the respondents the main reason for the selection of the above business sector for audit was due to their compliance risk (53.49%) and 45.35% of survey respondent replied that the sector has large tax potential risk (Table 4.10). Moreover, the respondents justification for the sector selection for audit was similar with that of the interview results obtained during the interview.

However, this study is inconsistent with the study conducted by Getaneh (2011) discovered that Merchandising sectors were mostly selected for audit at federal level.

Table 4.9. STATA output for business sector usually selected for audit.

Mostly selected business sector for Audit	Freq.	Percent
Manufacturing sector	53	61.62
Merchandising sector	36	41.85
Service sector(professional, financial, hotels, hospitals)	27	31.39
Construction and real estate sector	55	63.95
Others	3	3.49

Source: Survey outcomes and own computations, 2018

* Multiple answers were possible

**Figures do not add up

Table 4.10. STATA output reasons for selection of business sector taxpayers for audit.

Reason for selection of audit	Freq.	Percent
The sector has compliance risk	46	53.49
The sector has large potential risk	39	45.35
The sector has no well-organized record	8	9.30
Others	3	3.49

Source: Survey outcomes, 2018

* Multiple answers were possible

**Figures do not add up

4.5. The main objective of tax audit at ERCA-LTO

The survey result showed that, 47.66% of respondents replied that the main objective of tax audit in ERCA-LTO were for assessing and collecting additional revenue. Further, 46.52% and 34.88% of respondents replied that discourage tax evasion and encourage voluntary compliance and to educate tax law for taxpayers respectively (Table 4.11).

As ERCA Domestic Tax Audit Manual issued in 2014 stated that, “ the overall objective of tax audit is to improve the compliance of taxpayers, whether they declare the correct amount of tax and paid at the right time.” And similar answers were responded by the tax audit head of the branch as the main objective of tax audit is to increase compliance and educate taxpayers about tax law. But the questioner result responded by the tax auditor described that the objectives of tax audit is to collect additional revenue. The survey results were consistent with the research done by Samuel (2016) studied at LTO that the ultimate goal of tax audit is to increase the government revenue. And also, the study result found during interview with the tax audit head is consistent with the research done by Getaneh (2011) studied at ERCA federal level that, the purpose of tax audit is performed to ensure compliance in accordance with tax law.

Table 4.11. STATA output the main objective of tax audit at ERCA-LTO

Main objective of tax audit	Freq.	Percent
Discourage tax evasion and encourage voluntary compliance	40	46.52
To educate tax law for taxpayers	30	34.88
To provide feedback to management of taxpayers	11	12.80
For assessing and collecting additional revenue	41	47.66
Others	1	1.16

Source: Survey outcomes and own computations, 2018

* Multiple answers were possible

**Figures do not add up

4.6. Reasons for noncompliance behavior of the taxpayers

As per the survey result, the main reasons for noncompliance behavior of the taxpayers to be arise was: lack of awareness, weakness in tax administration, deliberate action of taxpayers and their carelessness with the respondents percentage of 47.67%, 43.02%, 37.21% & 16.28% respectively (Table 4.12). This study result is consistent with the research done by Getaneh (2011) that the main reason for non compliance behavior were due to lack of awareness and weak tax administration.

Table 4.12. STATA output for the reasons noncompliance behavior of taxpayers to be arise

Reasons for the noncompliance behavior	Freq.	Percent
Lack of awareness	41	47.67
Deliberate action	24	37.21
Carelessness	13	16.28
Weakness in tax administration	37	43.02

Source: Survey outcomes , 2018

* Multiple answers were possible

**Figures do not add up

4.7. Tax audit resources

Audit resources are very important to effectively discharge tax audit activities within the branch. And when the researcher reviewed literatures regarding this point, it is found that internationally the total staff assigned to audit should be close to 40 percent of the total staff of the tax administrations (Biber, 2010). Having this concept in to consideration and the studied tax administration office human resource structure, the study tried to assess the tax audit resources of the ERCA LTO through questionnaires and the interview as well as document review results were presented as follows:

As per the questionnaires results indicated that 41.86% respondents replied that not enough audit staffs were available at LTO with a mean 3.02 standard deviation (SD)1.08. Regarding audit resource materials, 39.54% of survey respondents replied with a mean 2.93 standard deviation (SD)1.07. The respondents were disagree with that of the availability of enough audit resource materials for audit program. Further, 37.21 % of respondents with a mean 3.17 standard deviation (SD) 0.98 responded about ERCA-LTO tax audit staff has not enough qualified and experienced audit staff to perform tax audit program. Similarly, 44.18% of respondents with a mean 2.75 standard deviation (SD) 0.93 were disagree that the branch has performed a continuous assessment to improve the capability of auditors and staff resources. The standard deviation was less than one and it shows that the respondents perception was almost similar with each other.

Despite the unavailability of adequate resources in both material and human resources, the respective auditors and tax audit head responded that an individual auditor averagely accomplished audit cases assigned a year and the branch averagely accomplished audit cases according to its tax audit plan with a mean 3.63 standard deviation (SD) 0.98 and 3.52 standard deviation (SD) 0.97 respectively (Table 4.13).

According to interviews reviewed that tax auditors assigned to accomplished their audit work with in 45 days for every business sectors. While reviewing the document , the researcher found that the total number of the branch staffs were 467 and from which the audit staffs were 98 including tax audit processor, tax audit coordinators, senior auditors, investigate auditors, auditors and junior auditors with a ratio 20.99% of the branch total staff. Moreover,

the planned number of audit staff were 164, but the actual were 98 which is only 59.76% of audit staff was fulfilled by the branch. And when the study assessed tax audit activity with its audit plan, it was noted that 180 taxpayers were planned to be audited during the fiscal year 2010E.C but the actual audit performed were 131 taxpayers with the ratio of 72.78% to the audit plan and from total number of tax payers registered in the branch (770), the number of audited tax payers during the year 2010 EC were (131) which was 17%. From the survey result, the tax audit staffs available in the branch is not enough as per their tax administration structures and as per international standards too.

Table 4.13. STATA output tax audit resources

Statements	Percent					Mean	Std. Dev.
	strongly disagree	Disagree	Neutral	Agree	Strongly agree		
	1	2	3	4	5		
ERCA-LTO has enough audit staff to perform auditing to all selecting taxpayers'	2.33	39.53	22.09	25.58	10.47	3.02	1.08
ERCA-LTO has enough audit resource materials for audit program	6.98	32.56	27.90	25.58	6.98	2.93	1.07
ERCA-LTO has enough qualified and experienced audit staff to perform tax audit program	1.16	36.05	29.07	25.58	8.14	3.17	0.98
ERCA-LTO perform a continuous assessment to improve the capability of auditors and staff resources	5.81	38.37	32.56	20.93	2.33	2.76	0.93
An individual auditor averagely accomplished audit cases assigned a year	2.33	19.77	27.90	36.05	13.95	3.62	0.98
ERCA-LTO averagely accomplished audit cases according to its tax audit plan		34.88	25.58	26.74	12.79	3.52	0.97

Source: Survey outcomes , 2018

4.8. Audit case selection methods

Case selection through the use of risk management techniques is necessary to ensure that the audit program is fully in line with the administration's compliance strategy, and to set up the necessary audit trails to show why cases have, and have not, been made the subject of an audit (OECD, 2006). Ebrill et al. (2001) stated that the most effective systems utilize taxpayer profiles and criteria to identify the highest risks for the revenue. Thus, the study tried to explore the ERCA LTO tax audit selection methods as depicted or described as follows:

As per the respondents responded and agreed that that the tax audit department have responsible audit team for selecting the audit cases, (percent = 52.32%; mean = 3.10 ; standard deviation (SD) = 1.37) (Table 4.14). And the tax audit case selection is supported by intelligence input (percent = 45.35%; Mean = 3.29 ; standard deviation (SD)= 1.08). Furthermore, 44.18% of respondents with a mean of 2.88 standard deviation (SD)1.27 stated that every tax payers at ERCA-LTO were not audited once in five year. ERCA-LTO audit case selection is not based on the availability of resource for tax audit as responded by 39.54% of respondents with a mean 2.83 standard deviation (SD) 1.13.

The tax audit selection team select the tax payers to be audited based on their associated compliance risk with a mean 3.62 standard deviation (SD) 1.11 as responded by 72.09% of respondents. Similarly Audit case selection isS based on taxpayer's high tax potential risk responded by 48.84% with mean 3.30 tandard deviation (SD) 1.17. The standard deviation was greaterr than one and it indicated that the respondents perception differ one another (Table 4.14).

The interview result also showed that taxpayers were selected by risk managements department for audit based on the risk criteria. According to ERCA Domestic Tax Audit Manual 2014 stated that, compliance risk is an indication of risk which showed that the taxpayers were to be selected for audit. Moreover, risk measured the taxpayers due to not pay outstanding taxes, submitted incorrect declarations, repetitive loss report and past case histories of taxpayers were usually selected for audit. Then the researcher found that the tax payers were selected for audit based on risk management department of the branch.

Table 4.14. STATA output for audit case selection methods

Statements	Percent					Mean	Std. Dev.
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree		
	1	2	3	4	5		
Does the tax audit department have responsible audit team for selecting the audit cases?	11.63	29.07	6.98	38.37	13.95	3.10	1.37
Does tax audit case selection is supported by intelligence input?	8.14	18.60	27.91	41.86	3.49	3.29	1.08
Does every tax payers at ERCA-LTO audited once in five year	9.30	34.88	23.26	19.77	12.79	2.88	1.27
Audit case selection is based on the availability of resource for tax audit	8.14	31.40	33.72	19.77	6.98	2.83	1.13
Series tax evasion and fraud are basis for audit tax selection	3.49	9.30	20.93	53.49	12.79	3.59	1.06
Tax payers are selected based on their associated compliance risk.	5.81	8.14	13.95	59.30	12.79	3.62	1.11
Audit case selection is based on taxpayer's high tax potential	5.81	16.28	29.07	36.05	12.79	3.30	1.17

Source: Survey outcomes, 2018

4.9. Working environment at LTO in tax audit

Enhancing open lines of communication between managers and employees can improve the overall quality of working relationships. Many interventions designed to make the workplace more hospitable can lead to improved retention (Griffeth et al. 2001). Rehaman (2012) argued that future opportunities for the employees also help in retaining employees because these opportunities are associated with more pay, additional work responsibilities, superior

work environment and different incentives plans. Taking in to account the above literature reviews, the study assessed the working environment of LTO and the results were discussed as follows:

Regarding conducive working Environment, 43.01% of survey respondents with a mean 3.42 standard deviation (SD) 1.28 showed that ERCA-LTO tax audit performed and reported their audit findings with full independency. However, 45.35% of respondents with a mean 3.03 standard deviation (SD) 1.21 showed that, ERCA-LTO tax auditor perform their audit work without IT support; 46.51% of survey respondents with a mean 3.08 standard deviation (SD) 1.24 replied that the LTO top management were not cooperated with tax auditors. Further, 55.82% of respondents with a mean 2.47 standard deviation (SD) 1.07 the survey result showed that the branch management did not facilitate short and long term training for tax auditors. In addition, the LTO has not well organizational structure and suitable office as responded by 70.93% of respondents with a mean 2.07 standard deviation (SD) 1.23. Job security and other facilities concerned, the respondent responded that there is no job security & other facilities in the branch responded by. 67.45% of respondents with a mean 2.15 standard deviation (SD) 1.16 (Table 4.15).

The interview with tax audit head showed that tax auditors are fully independence while performing their audit activities but management supports by facilitating training to upgrade them and IT support to tax auditors were not that much enough. The study result that the researcher obtained through questionnaires and interview were the same that means the audit staff did not supported by IT, not cooperate by management, did not have facilitate training, did not have job security and not have well organizational structure. Thus, the working environment not attractive that motivate the auditors to do their work effectively.

Table 4.15. STATA output for conducive working Environment

Statements	Percent					Mean	Std. Dev.
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree		
	5	4	3	2	1		
Does ERCA-LTO tax audit perform and report audit findings with full independency?	10.47	31.40	15.12	29.07	13.94	3.42	1.28
Does ERCA-LTO tax auditor perform their audit work with IT support?	11.63	33.72	17.44	30.23	6.98	3.03	1.21
Does ERCA-LTO management have cooperated with tax auditors?	16.28	30.23	18.60	27.91	6.98	3.08	1.24
Does ERCA-LTO management facilitate short and long term training for tax auditors?	19.77	36.05	24.41	17.44	2.33	2.47	1.07
Does ERCA-LTO have well organizational structure and suitable office?	41.86	29.07	9.30	17.44	2.33	2.07	1.23
Does ERCA-LTO perform job security and other facilities to tax auditor?	32.56	34.89	13.95	17.44	1.16	2.15	1.16

Source: Survey outcomes, 2018

4.10. Taxpayer characteristics during audit practice

Regarding taxpayers' characteristics during tax audit, 51.17% of survey respondents showed that taxpayers did not cooperate to give their source documents (Essential information

necessary for performing tax audit) with a mean 2.72 standard deviation (SD) 1.40. Similarly, 46.52% of respondents also stated that taxpayers did not respect the tax law, regulation and directive with a mean 2.72 standard deviation (SD) 1.22. As 56.97 % of survey respondents replied with a mean 2.55 standard deviation (SD) 1.17, tax payers have lack of good awareness on tax. Further, 63.96% of respondents with a mean 2.20 standard deviation (SD) 1.18 stated that taxpayers feel not happy while they are noticed to be audited and taxpayers are mostly unwilling to release vital records as responded by 53.49% of respondents with a mean 3.28 standard deviation (SD) 1.06 (Table 4.16).

The interviews result showed that most of the taxpayers did not cooperate to give the source documents during audit. However, after audit exist, the taxpayers raised appeal that they have all supporting documents and give to the appeal department or the court. Therefore, the characteristics of taxpayers during audit were difficult to tax auditors to perform their activities effectively and efficiently.

Table 4.16. STATA output for taxpayers' characteristics during tax audit

Statements	Percent					Mean	Std. Dev.
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree		
	1	2	3	4	5		
Tax payer cooperate to give their Source documents (essential information necessary for performing tax audit)	19.77	31.40	6.98	34.88	6.98	2.72	1.40
Tax payers respect the tax law, regulation and directive.	15.12	31.40	20.93	27.91	4.65	2.72	1.22
Tax payers have good awareness on tax	13.95	43.02	19.77	17.44	5.81	2.55	1.17
Tax payers feels happy while they are noticed to be audited	31.40	32.56	20.93	11.63	3.49	2.20	1.18
Taxpayers are mostly unwilling to release vital records	5.81	13.95	26.74	50.00	3.49	3.28	1.06

Source: Survey outcomes, 2018

4.11. Capacity of tax auditors

Regarding capacity of tax auditors, the survey respondents showed that appropriate and skilled officers are assigned during tax audit, tax audit manual enhance their capacity during audit, ERCA Tax audit plan and procedures, which develop during audit, are helpful to enhance their competency and their respective means were:(Mean = 3.57, standard deviation (SD)=1.01), (Mean = 3.52 standard deviation (SD) = 1.12), (Mean = 3.66, standard deviation (SD)=0.89) (Table 4.17).

Further, the survey result showed that tax auditors were not take sufficient training on different business sectors, construction and real estate, manufacturing, merchandise and services sectors respectively with a mean 2.48 standard deviation (SD) 1.06, 2.48 standard deviation (SD) 1.06, 2.47 standard deviation (SD) 1.08, 2.43 standard deviation (SD) 1.09 and 2.35 standard deviation (SD) 1.04. The standard deviation indicated that the respondents perception were not similar. Accordingly,51.17% of the respondents with a mean 3.29 standard deviation (SD) 0.96 also stated that in the LTO there was audit quality on their audit result. As 69.93% of survey respondents replied with a mean of 3.60 ± 0.96 , Auditors have the capacity of analyzing the financial statement.

In addition, 50% of respondents with a mean 3.28 standard deviation (SD) 1.06 stated that the tax audit manual is widely used by tax auditors during audit. Similarly, the audit manual provides adequate assurance for quality standards by 46.51% of respondents with a mean 3.28 standard deviation (SD) 1.08. However, 54.66% of respondents with a mean 3.73 standard deviation (SD) 0.95 the survey showed that, audited taxpayers usually appeals were very common (Table 4.17).

Auditors have ability to conduct investigation of taxpayers book account as responded by 69.77% of respondents with a mean 3.56 standard deviation (SD) 0.91. Auditors have ability to determine compliance or non-compliance with regard to tax law as responded by 69.77% of respondents with a mean 3.63 standard deviation (SD) 0.95. Auditors are competent enough with regard to tax accounting and financial analysis as 63.95% of survey respondents replied with mean 3.5 standard deviation (SD) 1.06. Auditors are competent enough with regard to applying tax law, regulation and directives as 63.95% of survey respondents replied

with mean 3.60 standard deviation (SD) 0.90. Auditors have good competency with respect to make effective decision/assessment of tax obligation as 60.47% of survey respondent replied with mean 3.53 standard deviation (SD) 0.81. Auditors are effective to make communication with respect to the result to tax payer as 63.93% of survey respondent replied with mean 3.58 standard deviation (SD) 0.94. Effective to audit process and procedures as 62.80% of survey respondent replied with mean 3.62 standard deviation (SD) 0.90. Auditors are efficient to manage their own audit work including preparing, using and summarizing their audit work on working paper as 68.61% of survey respondent replied with mean 3.76 standard deviation (SD) 0.88. Auditors are effective in managing the relationship among their team member as 61.64% of survey respondents replied with mean 3.66 standard deviation (SD) 0.94 (Table 4.17).

As the researcher interviewed with tax audit head and understood that the tax audit department is trying to improve the auditors' audit skill through both internal and external short term training. Eventhough, the training was given for auditors in the above means, because of the business complexity of the audited entity, there were a shortage of tax experts to train in all type of business sectors.

Table 4.17. STATA output for the regarding capacity of tax auditors

Statements	Percent					Mean	Std. Dev.
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree		
	1	2	3	4	5		
Appropriate and skilled officers are assigned during tax audit.	3.49	9.30	18.60	60.47	8.14	3.57	1.01
Tax audit manual enhance your capacity during audit	6.98	8.14	17.44	56.98	10.47	3.52	1.12

Tax audit plan and procedures, which you develop during audit, are helpful to enhance your competency.	3.49	3.49	20.93	65.12	6.98	3.66	0.89
Tax auditors take sufficient training on audit in different business sectors	15.12	41.86	22.09	19.77	1.16	2.48	1.06
Tax auditors take sufficient training on construction accounting.	10.47	50.00	25.58	6.98	6.98	2.47	1.08
Tax auditors take sufficient training on Manufacturing sector	12.79	47.67	26.74	5.81	6.98	2.43	1.09
Tax auditors take sufficient training on Merchandise sector	12.79	48.84	23.26	9.30	5.81	2.43	1.09
Tax auditors take sufficient training on Services sector	13.95	51.16	20.93	10.47	3.49	2.35	1.04
There is audit quality on your audit result	3.49	15.12	30.23	48.84	2.33	3.29	0.96
Auditors have the capacity of analyzing the financial statement.	2.33	11.63	15.12	62.79	7.14	3.60	0.96
The tax audit manual is widely used by tax auditors during audit	3.49	16.28	30.23	46.51	3.49	3.28	0.98
The audit manual provides adequate assurance for quality standards.	3.49	17.44	32.56	37.21	9.30	3.29	1.05
Appeals by audited taxpayers are very common	16.28	4.65	24.42	52.33	2.33	3.73	0.95
Ability to conduct investigation of tax payers book of account	3.49	8.14	18.60	66.28	3.49	3.56	0.92
Ability to determine compliance or non-compliance with regard to tax law	2.33	9.30	18.60	60.47	9.30	3.63	0.95
Competent enough with regard to tax accounting and financial analysis	3.49	12.79	19.77	54.65	9.30	3.50	1.06
Competent enough with regard to applying tax law, regulation and directives.	1.16	10.47	24.42	53.49	10.46	3.60	0.90

Have good competency with respect to make effective decision/assessment of tax obligation.	1.16	8.14	30.23	55.82	4.65	3.53	0.81
Effective to make communication with respect to the result to tax payer	2.32	10.49	23.26	53.49	10.44	3.58	0.94
Effective to audit process and procedures	1.16	9.30	26.74	51.16	11.64	3.62	0.90
Efficient to manage your own audit work including preparing, using and summarizing your audit work on working paper.	1.16	5.81	24.42	52.33	16.28	3.76	0.88
Effective in managing the relationship among your team member	2.32	5.81	30.23	45.36	16.28	3.66	0.94

Source: Survey outcomes,2018

4.12. Summary

The chapter has presented the results and analysis of the study along with the presentation of research objective and questions, interviews and documentary reviewed. In the research objective and questions were presented to connect them with the results of the study and has presented the outcomes of both qualitative and quantitative research methods adopted in the study separately. Specifically, the results of surveys with branch tax audit head, tax auditors, coordinators and investigators. The results obtained through these instruments were employed to investigate the perception of tax audit practice in evidence from Ethiopia ERCA-LTO which focus type of tax audit performed, the purpose of audit, the audit case selection methods, sufficiency of audit resources, conducive working environment, taxpayers characteristics during tax audit practice and the experience and capacity of tax auditors in particular.

From the above findings and the literature reviews along with the ERCA tax audit manual, the researcher concluded that lack of training in any business sectors, management cooperates, insufficient audit resource, external inefficiency like taxpayers characteristics during audit, internal inefficiency like audit skills experience and capacity and suitable and free working environment, the auditors are incompetent.

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

The previous chapter presented the results and analysis of the study. This chapter provides the conclusions and recommendations in line with the findings of the study. The chapter is structured in two sections. The first section deals with conclusions whereas the second section presents some recommendations suggested as a solution to problems that have been identified in the study.

5.1. Conclusions

The objective of this research was to assess the perception of tax audit practice in evidence from Ethiopia ERCA-LTO. The study used questionnaires prepared for tax auditors and interviews to tax audit processor owner (tax audit head) and document reviews as a source of data. The responses obtained from survey of tax audit department staffs were tabulated and interpreted by using STATA software through descriptive statistics while result from interviews and documentary reviews were presented to support the survey result. The perception of tax audit practice was studied in terms of type of audit performed, selection of taxpayers for audit, tax audit resources and working environment. Then based on this, the study discovered the following points:

Tax auditors selection criteria were based on field of study, training and examination as well as related past experiences. However, auditors in the branch has a work experience less than five years and shortage of senior auditors in the branch. As per the interviews the main reasons for their shortage was: workload without additional benefits, absence of suitable and free working environment, absence of satisfactory allowance for their duties and uneven compensation payment for similar field activities and absence of performance based promotion.

The type of audit program performed in ERCA-LTO were mostly comprehensive audit followed by fraud and field audits respectively. However, the ERCA tax audit manual required the tax audit department to audit other types of audit such as Desk audit, Advisory

visit audit and Refund & De Registration audit. The selection of business sectors for audit at the branch was most of the time construction and real estate followed by manufacturing, merchandising and service sectors respectively. The study also noted that there is shortage of tax audit staff as per the tax administration human resource structure and as per international standards.

The risk management and audit teams are responsible for selecting the audit cases. As the result ERCA-LTO tax audit case selection is supported by intelligence input. In addition to that tax payers are selected based on their associated compliance risk. Similarly audit case selection is based on taxpayer's high tax potential risk, series tax evasion and fraud are basis for audit tax selection is applicable.

Regarding working Environment, ERCA-LTO tax audit perform and report audit findings with full independence. But their audit activities in the branch is not supported by IT, the branch management have not cooperated with tax auditors, management did not facilitate short and long term training, has no well organizational structure and suitable office and does not perform job security and other facilities to tax auditor as responded by tax auditors.

5.2. Recommendations

From the discussion and conclusion the researcher found that tax auditors need continuous training audit skill to competent audit to discourage tax avoidance and evasion, to improve the tax compliance level and to increase the tax revenue. Therefore, based on the findings of the study, the researcher has tried to provide briefly the following recommendations:

1. The primary objective of tax audit in LTO should be detection of compliance risk and increase compliance taxpayers and educate tax payers rather than to assess and collect additional revenues, which should be the end goal of the objective.
2. The management of ERCA-LTO should increase the number of tax auditors and improve the capability of total audit staff resources and facilitating both short and long term training schedules based on the gap identified for any business sectors that help to improve their audit skills.

3. ERCA-LTO should supply sufficient necessary audit materials for auditors to facilitate their work and provide suitable and free working environment such as fair treatment, by providing different promotional schemes based on their performance.
4. To retain the experienced tax auditors, ERCA-LTO should investigate the reason for the reassignment from their position after some years of experience and give appropriate solution for the problem.
5. The authority should revise the time frame allocation and give more time for complex cases to properly detect noncompliance and achieve the required audit quality. Giving equal time, 45 days per audit cases, for all business to be audited might result operational inefficiency including decrease in audit quality and coverage.

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Appendix 1: -Questionnaires

ADDIS ABABA UNIVERSITY

COLLEGE OF BUSINESS & ECONOMICS

DEPARTMENT OF ACCOUNTING AND FINANCE

Tax auditors' survey instrument

Dear Participant

My name is Solomon Shumetie. I am MSc (in Accounting and Finance) student at the Addis Ababa University. Currently, I am doing research on the **“Perception of Tax Audit Practice: Evidence from Ethiopia Large Taxpayers Office (LTO)”**.

The aim of the research is to explore the perception of tax audit practice in evidence from Large Tax Payers Office. To supplement the data, I seek to gather relevant information from all tax auditors, and audit processor owner (audit head) using self-administered questionnaire. Participation in this research is completely voluntary. I would promise that all information you provide would be strictly confidential. Individual responses will not be disclosed in the investigator's MSc thesis.

I thank you very much in advance for your cooperation.

For further information, please contact me by the following address:

E-mails: solomonsh21@gmail.com

Part I: Demographic information

1. Gender: Male Female

2. Age: Less than 25 years 25-35 years 35-45 years
45-55 years Above 55 years

3. Level of education:

Certificate BSc/BA
Diploma MSc/MA and above
Others Please specify _____

4. Field of study (multiple answers are possible):

Accounting & Finance Economics
Management others Please specify _____

5. Job occupation in ERCA-LTO :

Junior tax auditor Tax auditor
Tax investigator Tax audit coordinator
Tax audit processor owner
Others please specify _____

6. Did you have audit experience before you employed in ERCA?

Yes No

7. If your answer in question #6 is yes, how many years did you have?

Less than 2 year

4-7 years

2-4 years

above 7 years

8. How long did you have been working as tax auditor in the ERCA?

Less than a year

5-8 years

2-5 years

above 8 years

9. What is the criteria to be selected an auditor in your branch (multiple answers are possible)?

Related to past working experience

Based on exam and training

Related to field of study

Related to level of education

Others , please specify _____

Part II: Questions regarding type of tax audit program

10. What type of audits are repetitively performed by the ERCA-LTO (multiple answers are possible)?

Field audit

Comprehensive audit

Fraud audit

Others , please specify _____

11. Which business sectors are mostly selected for tax audit in this branch (multiple answers are possible)?

Manufacturing sector

merchandising sector

Service sector (professional services, hotel, and financial sector)

Construction and real estate sector

Others , Please specify _____

12. What is the reason this and/or these business sector that you have selected in question #11?

The sector has higher compliance risk

The sector has large tax potential risk

The sector has no e well organized business records

Others , please specify _____

13. What is the main objective of tax audit at ERCA-LTO (multiple answers are possible)?

Discourage tax evasion and encourage voluntary compliance

To educate tax law for taxpayers

To provide feedback to management of taxpayers

For assessing and collecting additional revenue

Others , please specify _____

14. What are the main reasons for the noncompliance behavior of the taxpayers to arise (multiple answers are possible)?

Lack of awareness

deliberate action

Carelessness

Weakness in tax administration

Others , please specify _____

Part III: Questions regarding tax audit resources

No	Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
		5	4	3	2	1
15	ERCA-LTO has enough audit staff to perform auditing to all selecting taxpayers’					
16	Does ERCA-LTO have enough audit resource materials for audit program?					
17	ERCA-LTO has enough qualified and experienced audit staff to perform tax audit program					
18	Does ERCA-LTO perform a continuous assessment to improve the capability of auditors and staff resources?					
19	An individual auditor averagely accomplished audit cases assigned a year					
20	ERCA-LTO averagely accomplished audit cases according to its tax audit plan					

Part IV: Questions regarding audit case selection methods

No	Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
		5	4	3	2	1
21	Does the tax audit department have responsible audit team for selecting the audit cases?					
22	Does tax audit case selection is supported by intelligence input?					
23	Does every tax payers at ERCA-LTO audited once in five year					

24	Audit case selection is based on the availability of resource for tax audit					
25	Series tax evasion and fraud are basis for audit tax selection					
26	Tax payers are selected based on their associated compliance risk.					
27	Audit case selection is based on taxpayer's high tax potential					

Part V: Questions regarding conducive working Environment:

No	Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
		5	4	3	2	1
28	Does ERCA-LTO tax audit perform and report audit findings with full independency?					
29	Does ERCA-LTO tax auditor perform their audit work with IT support?					
30	Does ERCA-LTO management have cooperated with tax auditors?					
31	Does ERCA-LTO management facilitate short and long term training for tax auditors?					
32	Does ERCA-LTO have well organizational structure and suitable office?					
33	Does ERCA-LTO perform job security and other facilities to tax auditor?					

Part VI. Questions regarding taxpayer characteristics during audit practice

No	Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly disagree
		5	4	3	2	1
34	Tax payer cooperate to give their Source documents (essential information necessary for performing tax audit)					
35	Tax payers respect the tax law, regulation and directive.					
36	Tax payers have good awareness on tax					
37	Tax payers feels happy while they are noticed to be audited					
38	Taxpayers are mostly unwilling to release vital records					

Part VII. Questions regarding capacity of tax auditors

No	Statements	Strongly Agree	Agree	Neutral	Disagree	Strongly disagree
		5	4	3	2	1
39	Appropriate and skilled officers are assigned during tax audit.					
40	Tax audit manual enhance your capacity during audit					
41	Tax audit plan and procedures, which you develop during audit, are helpful to enhance your competency.					
42	Tax auditors take sufficient training on audit in different business sectors					
43	Tax auditors take sufficient training on construction accounting.					
44	Tax auditors take sufficient training on Manufacturing sector					
45	Tax auditors take sufficient training on Merchandise sector					
46	Tax auditors take sufficient training on Services sector					

47	There is audit quality on your audit result					
48	Auditors have the capacity of analyzing the financial statement.					
49	The tax audit manual is widely used by tax auditors during audit					
50	The audit manual provides adequate assurance for quality standards.					
51	Appeals by audited taxpayers are very common					
52	Ability to conduct investigation of tax payers book of account					
53	Ability to determine compliance or non-compliance with regard to tax law					
54	Competent enough with regard to tax accounting and financial analysis					
55	Competent enough with regard to applying tax law, regulation and directives.					
56	Have good competency with respect to make effective decision/assessment of tax obligation.					
57	Effective to make communication with respect to the result to tax payer					
58	Effective to audit process and procedures					
59	Efficient to manage your own audit work including preparing, using and summarizing your audit work on working paper.					
60	Effective in managing the relationship among your team member					

61. Do you have any additional ideas that can be done to solve perception of tax audit practice, please state?

Appendix 2 – Interviews with branch tax audit head

1. What is the aim of conducting tax audit?
2. Do you believe that ERCA-LTO achievable its tax collection revenue from tax payers? What is the contribution of branch tax audit to enhance taxpayers' to be compliant?
3. What type of audit mostly performed in your branch (desk audit, field audit, comprehensive audit, advisory audit, refund audit, fraud investigation and single audit)? Would you please tell me the reason to conduct the type of audit?
4. What are the criteria that audit case files are assigned to tax auditors? (Junior, auditor and senior auditors?)
5. Is there standard to assign tax auditors to audit high risky taxpayers?
6. Is there time frame to complete audit work with a given period?
7. Do you have a criteria and requirements to hire individuals as a tax auditor?
8. Is there continuous training and/or tutor to enhance to auditor skill and knowledge?
9. How long a tax auditor works on average in ERCA-LTO? Are tax auditors resign by themselves? IF your answer is "yes," can you tell me the reason behind this please?
10. Is there anything to add an additional idea that is not mentioned please?

Source: From theoretical literatures and empirical studies of Getaneh (2011).