



**THE EFFECTIVENESS OF EXTERNAL AUDIT  
ON TAX COLLECTION IN ETHIOPIA:  
THE CASE OF LARGE TAX PAYERS OFFICE**

**BY: ASRAT ABADI**

**A THESIS SUBMITTED TO THE DEPARTMENT OF ACCOUNTING  
AND FINANCE, COLLEGE OF BUSINESS AND ECONOMICS IN  
PARTIAL FULFILLMENT OF THE REQUIREMENT FOR MASTER OF  
SCIENCE IN ACCOUNTING AND FINANCE**

**JUNE, 2019  
ADDIS ABABA, ETHIOPIA**

**THE EFFECTIVENESS OF EXTERNAL AUDIT  
ON TAX COLLECTION IN ETHIOPIA:  
THE CASE OF LARGE TAX PAYERS OFFICE**

**BY: ASRAT ABADI**

**A THESIS SUBMITTED TO THE DEPARTMENT OF ACCOUNTING  
AND FINANCE, COLLEGE OF BUSINESS AND ECONOMICS IN  
PARTIAL FULFILLMENT OF THE REQUIREMENT FOR MASTER OF  
SCIENCE IN ACCOUNTING AND FINANCE**

**ADVISOR: HABTAMU BERHANU (PhD.)**

**JUNE, 2019**

**ADDIS ABABA, ETHIOPIA**

## **Statement of Declaration**

I, the undersigned, declare that this thesis is my original work, prepared under the guidance of Habtamu Berhanu (PhD). All sources of materials used for the thesis have been duly acknowledged. I further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for earning any degree.

Name: Asrat Abadi

Signature \_\_\_\_\_

Date \_\_\_\_\_

Place and date of submission: Addis Ababa University, June 2019

## **Statement of Certification**

This is to certify that Asrat Abadi has carried out his research work on the topic entitled “The Effectiveness of External Audit on Tax Collection in Ethiopia: Case of Large Tax Payers” Office. The work is original in nature and is suitable for the submission for the reward of MSc Degree in Accounting and Finance.

**Advisor: Habtamu Berhanu (PhD):**

**Signature:** \_\_\_\_\_

**Date:** \_\_\_\_\_

**ADDIS ABABA UNIVERSITY  
COLLEGE OF BUSINESS AND ECONOMICS  
DEPARTMENT OF  
ACCOUNTING AND FINANCE**

***THE EFFECTIVENESS OF EXTERNAL AUDIT  
ON TAX COLLECTION IN ETHIOPIA:  
THE CASE OF LARGE TAX PAYERS OFFICE***

**BY: ASRAT ABADI**

Habtamu Berhanu (PhD)

\_\_\_\_\_  
Name of Advisor

\_\_\_\_\_  
Sig.

\_\_\_\_\_  
Name of External Examiner

\_\_\_\_\_  
Sig.

\_\_\_\_\_  
Name of Internal Examiner

\_\_\_\_\_  
Sig.

## ABSTRACT

*This paper provides some evidences how the government benefited from the external auditors effectiveness on tax collection by minimizing the loopholes which exposed for tax avoidance, evasion and shelter. Research data collected from the population auditing firms based in Addis Ababa and sample were taken from twenty firms based on their size and number of employees. 100 questionnaires were distributed to external auditors titled senior and above constructed by 5 point likert scale. 82 responses are obtained from the respondents and summarized by using excel spread sheet before processed by STATA software to have descriptive and regression analysis quantified results. The qualitative data from interview was used to triangulate the respondents result from Stata. Eight hypotheses was proposed and checked as a result competence, independence, regulatory body and tax audit have significant effect and strong relation with the effectiveness of external auditors performance on tax collection in comparing with audit firm size, audit fee and audit tenure. In contrary awareness of tax by the external auditors inversely related. The study recommended the governing body should work in co-operation with AABE, finance professional association and individuals, there must be a comprehensive tax manual used as a reference, a controlling mechanism should be set for external audit professionals, the training and education department must be well arranged and structured to provide support, AABE should to revise audit firm certification criteria to increase the number of external audit firms and at last tax audit by the tax authority preferably should be done as soon as tax report delivered by the tax payers.*

**Key words:** *External Auditors, Tax Collection.*

## **Acknowledgments**

I would like to thank the almighty GOD for his permission to complete this research work from the commencement. With a great respect for Alemzewed Ayele and Arefayine Wodajo to acknowledge the support in each progress of this research work. My deepest gratitude to Habtamu Berhanu (Dr.) for his advice and productive comment as well as inspiration through every step of this thesis. The author would also like to express appreciation for each respondents of the questionnaire in the audit firms and interviewees at LTO office, who gave me their precious time by considering the value of the work and AABE employees in every department.

## **ACRONYMS AND ABBREVIATIONS**

AABE= Accounting and Auditing Board of Ethiopia

APB= Auditing Practice Board

ASE= Accounting Society of Ethiopia

EA=External Audit

EAFs=External Audit Firms

EEAA = Ethiopian External Auditor Association

EPAAA= Ethiopian Professional Association of Accountants and Auditors

ERCA= Ethiopian Revenues and Customs Authority

IAASB= International Auditing and Assurance Standard Board

ICAEW= Institute of Chartered Accountants in England & Wales

IESBA= the International Ethics Standards Board for Accountants

IFRS= International Financial Reporting Standard

IRS= Internal Revenue Services

LTO= Large Tax payers Office

NAS= Non-Audit Service

OECD =Organization for Economic Co-operation Development

OFAG= Office of the Federal Audit General

PCAOB=Public Company Accounting Oversight Board

SEC = Security Exchange Commission

SOX=Sarbanes-Oxley

## TABLE OF CONTENT

Statement of Declaration .....	I
Statement of Certification .....	II
ABSTRACT .....	IV
Acknowledgement .....	V
ACRONYMS AND ABBREVIATIONS .....	VI
Table of Content .....	VII
List of Tables .....	X
List of Figure .....	XII
<b>CHAPTER ONE: INTRODUCTION</b> .....	1
1.1 Background of the study .....	1
1.2 Statement of the problem.....	3
1.3 Objectives of the Study .....	5
1.3.1 General Objectives .....	5
1.3.2 Specific Objectives.....	5
1.4 Research Questions .....	6
1.5 Hypothesis Development .....	6
1.6 Significance of the study .....	14
1.7 Scope and limitation of the study .....	15
<b>CHAPTER TWO</b> .....	16
LITERATURE REVIEW .....	16
2.1 INTRODUCTION.....	16
2.2 Theoretical review .....	16
2.2.1 Theoretical Review on Auditing .....	16
2.2.1.1 Definition of Auditing.....	16
2.2.1.2 Theories of Auditing .....	16
2.2.1.2.1 The Lending Credibility Theory .....	18
2.2.1.2.2 The Theory of Inspired Confidence (Limperg, 1932).....	18

2.2.1.2.3 Agency Theory , (Watts and Zimmerman).....	19
2.2.1.2.4 The Police man theory.....	19
2.2.1.2.5 Moderator of Claimants’ Theory: .....	19
2.2.1.2.6 Quasi-Judicial Theory: .....	19
2.2.1.3 An effective external audit process .....	20
2.2.2 Theoretical review on tax.....	23
2.2.2.1 Introduction on Taxation.....	23
2.2.2.2 Objectives of Taxation .....	23
2.2.2.3 The Ability-to-pay Theory of Taxation.....	25
2.2.2.4 Ethiopian tax laws .....	25
2.3 Empirical Review .....	30
2.4 Summary on Literature Review.....	34
2.5 Conceptual Framework .....	35
<b>CHAPTER THREE .....</b>	<b>36</b>
<b>REASEARCH METHODOLOGY .....</b>	<b>36</b>
3.1 Introduction .....	36
3.2 Research Method .....	36
3.3 Research Design .....	36
3.4 Population and Sampling of the Study .....	37
3.4.1 Population of the study.....	37
3.4.2 Sampling Design.....	37
3.5 Data Analysis .....	39
3.5.1 Quantitative Data Analysis.....	39
3.5.2 Qualitative Data Analysis .....	40
<b>CHAPTER FOUR.....</b>	<b>41</b>
<b>DATA ANALYSIS AND INTERPRETATIONS.....</b>	<b>41</b>
4.1 Introduction .....	41

4.2 Econometric Data Analysis.....	41
4.2.1. Respondents’ Profile.....	41
4.2.2. Descriptive Statistics.....	44
4.2.3. Reliability Analysis.....	50
4.2.4. Assessment of Ordinary Least Square Assumptions.....	51
4.2.4.1. Assessment of Normality.....	51
4.2.4.2. Assessment of Multicollinearity.....	52
4.2.4.4. Assessment of Autocorrelation.....	54
4.2.5. Regression Results for EA effectiveness.....	55
4.3. Data Results and Interpretation.....	57
4.3.1. Competence of External Auditors.....	58
4.3.2 Awareness or attitudes of External Auditors.....	59
4.3.3 Independence of External Auditors.....	60
4.3.4 Presence of Regulatory Body.....	61
4.3.5 Audit Firm Size of External Auditors.....	62
4.3.6 Audit Fee Paid to The Auditor.....	63
4.3.7 Audit Tenure With The Client.....	64
4.3.8 Tax Audit By The Tax Collector Office.....	64
<b>CHAPTER FIVE.....</b>	<b>66</b>
<b>CONCLUSIONS AND RECOMMENDATIONS.....</b>	<b>66</b>
5.1 Conclusions.....	66
5.2 Recommendations.....	67
<b>REFERENCES.....</b>	<b>69</b>
<b>APPENDIX (1).....</b>	<b>78</b>
Questionnaire for Audit Firms.....	78
<b>APPENDIX (2).....</b>	<b>84</b>
Interview for ERCA Tax Audit Department.....	84
<b>Schedule.....</b>	<b>86</b>
Time Schedule .....	86
Cost Budget.....	87

## LIST OF TABLES

Table 2.1 The tax rates of employment income .....	31
Table 2.2 The tax rates of business income .....	32
Table 4.1 Age of External Auditors.....	45
Table 4.2 Educational Level of External Auditors.....	46
Table 4.3 Years of Work Experience for External Auditors.....	46
Table 4.4 Current Position of External Auditors.....	47
Table 4.5 Descriptive Statistics of Competence of External Auditors.....	48
Table 4.6 Descriptive Statistics of Awareness or Attitudes of External Auditors.....	48
Table 4.7 Descriptive Statistics of Independence of External Auditors.....	49
Table 4.8 Descriptive Statistics of Regulatory Body.....	50
Table 4.9 Descriptive Statistics for Audit firm Size.....	50
Table 4.10 Descriptive Statistics for Audit Fee.....	51
Table 4.11 Descriptive Statistics for Audit Tenure.....	52
Table 4.12 Descriptive Statistics of Tax Audit .....	52
Table 4.13 Reliability Statistics for Cronbach's Alpha.....	53
Table 4.14 Inter Item Correlation Matrix.....	54
Table 4.15 Assessment of Normality.....	55
Table 4.16 Assessment of Multicollinearity.....	56
Table 4.17 Pearson Correlation Matrix.....	57
Table 4.18 Durbin Watson Test Model Summary.....	58
Table 4.19 Regression Results for EEA on Tax Collection.....	59
Table 4.20 Regression Results Coefficients.....	59

**LIST OF FIGURE**

Figure 2.1 Conceptual Frameworks for Effectiveness of External Audit.....38

# CHAPTER ONE

## INTRODUCTION

### 1.1 Background of the study

In the early years of auditing, the keeping and maintaining of accounting records was done primarily to detect fraudulent activity by the independent auditors after the act passed in 1900. The early 2000s saw various accounting scandals like WorldCom, Enron, Tyco, etc. Auditors have been responsible for detecting fraud in many stages. Initially, auditors were responsible for detecting fraud, as one of the main objectives of the review process, about the extent to which the financial statements are free of fraud and that they reflect honestly and fairly the financial position of the company (Alarbeed, Alothman, & Assee, 2014).

The external audit represents the audits operations for the parties outside of the entity under auditing, by experts specialized independent of entity under auditing, or its staff or officers, called the external auditors. These auditors are qualified and independent, and the external auditor performs the audit in accordance with the International Auditing Standards (IAS) (Lotfii, 2005). (Kassem & Higson, 2016) Illustrated that the auditor's responsibility to detect and report misstatements resulting from illegal acts having a direct and material effect on the determination of financial statement amounts is the same as that for misstatements caused by error or fraud. While (Ojo, 2006) showed that the role of the external auditor in the supervisory process requires standards such as independence, objectivity and integrity to be achieved.

The importance of auditing is determined by providing service for multiple parties who used the audited financial statements in making decisions, and examples of these parties are as follows (Al-Bawab, 2012) (1) Management: The auditor's report illustrates the impact of effective management, where it depends upon the development plans, monitoring and evaluation of the performance of the management. (2) Investors: The auditors' report to investors represents a safety tool for their money, where the investors depend on the financial statements certified by an auditor who is independent and impartial when they think about making any decision related to their savings and their investments in order to gain the highest return possible. (3) Lenders: In general, banks prefer to rely on financial statements audited when examining the financial centers of the projects that apply for credit facilities and loans from them. (4) Government bodies: based on the

audited financial statements for many purposes, including planning, control and taxation, pricing, and the report of subsidies to some industries (Budur, 2008).

One of the parties who used the audited financial statements as indicated above is government bodies. The reports are generated from the external auditors. It has an opportunity in elevating the tax compliance behavior.

Tax is a compulsory contribution imposed by public authority irrespective of the exact amount of service rendered to the tax payer in return (Saleemi, 2008). The objectives of tax are: first to raise revenue that is sufficient for public spending without the government having to borrow heavily in order to finance its activities and secondly to mobilize revenue in equitable manner that is able to minimize its disincentive effects on economic activities (Eliud & Eric, 2006). For most developing countries, taxation goes hand-in-hand with economic growth and taxes are lifeblood for governments to deliver essential services and to make long-term investments in public goods as stated a report from OECD (Organization for Economic Co-Operation and Development) by (Asa, Christopher, Jens, Bert, & Laura, 2008).

In Ethiopia the Ethiopian Revenues and Customs Authority (ERCA) is responsible to perform tax activities. It was established by the proclamation No. 587/2008 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 enhancing the mobilization of government revenues, while providing effective tax and Customs administration and sustainability in revenue collection. Generally the main objective of the establishment of ERCA was to make more efficient the public revenue generation function by bringing the relevant agencies under the umbrella of the central revenue collector body (Minyichel, 2017). In addition to raising revenue, it is also responsible to protect the society from adverse effects of smuggling and contraband. It seizes and takes legal action on the people and vehicles involved in the act of smuggling, any tax evasion and avoidance while it facilitates the legitimate movement of goods and people across the border (Bayou, 2017).

The tax evasion can be minimized not only by ERCA or the concerned government offices but also the contribution of responsible parties. From these valuable co-operators external auditors have significant role by giving a quality assurance service on the financial reports. If the reports are reasonably assured the tax growth activity will be increased and provide a great support to meet the millennium development goal.

The study focused on assessing and evaluating the effectiveness of external audit on tax collection in the ERCA (Ethiopian Revenues & Customs Authority) Large Tax Payers Office (LTO). And it wants to give direction to meet the effectiveness of tax collection process by considering the external auditors substantial importance.

## **1.2 Statement of the problem**

In recent years the trend of tax collection shows an incremental in total tax collection but performance of tax collection is decreasing from year to year (Belay Z. , 2015). The performance of tax collection has been constrained by a lot of factors. If the government paves the obstacles and strongly accountable for tax, the contribution of tax is vital for countries development and it would have a great share of the total GDP, but in Ethiopia the contribution of tax to GDP remained consistently low and is relatively shrinking as studied by (Akalu, 2016). As per the evidences obtained Ethiopia's ratio of tax revenue to gross domestic product (GDP) is still well short of the international average. The ratio of tax revenue to GDP in Ethiopia is less than 11 %, while in many African countries the ratio exceeds 20 per cent. It is about 40 per cent in higher income countries (Abate, 2009). The United Nations considers that achieving the Millennium Development Goals (MDGs) requires developing countries to raise at least 20% of their gross domestic product (GDP) in taxes. It indicates that the government should exert a substantial effort to embrace all tax payers to pay their liability until the last drop.

In an ideal world, all taxpayers would voluntarily pay their taxes and comply with all of their tax obligations willingly. But in fact, no one enjoys by paying tax to the government and as much as possible every economic unit tries to minimize its tax burden by any means. (Fentaye & Nageswararao, 2015). Behind the tax evasion, tax shelters and accounting scandals process professional service providers have a great involvement.

The perception of the users of financial statements on independent auditors report is declining after the auditor's involvement in major scandals. The research work by (Linda, 2004) revealed, during the late 1980s and 1990s, consulting, much of the accounting scandals involving the design and implementation of aggressive tax transactions became a substantial moneymaker for accounting firms. The main problems on audit firms are accounting scandals made by big

companies, the Enron debacle or disaster is a prime example of the cascading effect of accounting irregularities by Arthur Andersen, this is a considerable scandals by Enron, and SEC forced to issue an act of 2002. Such accounting scandals also occurred in our country however there are no reported scandals that involve auditors, but with the increasing number of private audit firms and the increasing number of business companies many studies should be conducted on audit quality to tackle or minimize similar scandals. The scandals lead the government to have doubt or to lose trust on the tax payers financial statements. The government has its own reason being pessimist even if it amplifies. The tax payers have an adviser in addition to their own “knowledge” to participate in the tax shelter, tax evasion and accounting scandals activity. As Ernst & Young made for Enron, accounting firms found in this country also participatory.

“Auditors only do their job in a way that secures their personal careers, their continuing contracts as auditors or promotes the other business interests of their firm rather than a way that fulfills their legal and moral professional obligation to shareholders and other stakeholders (Abdi, 2017)”. These make the auditors to accomplish their duty with out effective characteristics and are not allowed to express opinions in a manner directed by International Auditing Standards. Such ineffectiveness declines the government tax collection ability and understates the amount of tax to be collected.

Most of the investigation on the determinants of tax revenue performance in Ethiopia federal government the variables used were foreign direct investment, public debt, foreign aid, inflation, GDP, industry, agriculture, per capital income, export, interest rate, trade openness, exchange rate, disposable income and foreign direct investment as stated on the works of (Belay Z. , 2015), (Anwar, 2014), (Teskaye, 2015) and (Minyichel, 2017). Those variables listed are not the only factors which hinder the tax collection process. External audit firms have also a great impact and contribution for the tax collection performance. As a result, it is better to consider the variables which affect the external audit quality or performance in the other aspect for variables examined by other researchers.

From the variables examined, studies show inadequacies in the way provides a theoretical analysis of the hindering factors on failure to achieve full potential by using the external auditors on tax revenue collection in Ethiopia. The researcher believes that this study fills some gaps in the area of tax revenue collection factors not tested in the other study for the

coming researchers. In this prospect the effectiveness of the audit firms play a great role and the variables on the effectiveness of EA well thought-out.

### **1.3 Objectives of the Study**

As per the problems discussed above, the study has both general and specific objectives.

#### **1.3.1 General Objectives**

The main objective of this research is to investigate the effectiveness of external audit on tax collection in Ethiopian Revenues and Customs Authority Large Tax Payers Office (LTO).

#### **1.3.2 Specific Objectives**

Specifically, the study has the following specific objectives:

- To investigate competence of auditors affects the effectiveness of external audit on tax collection.
- To examine awareness or attitudes of external auditors affects the effectiveness of external audit on tax collection.
- To study independence of external auditors affects the effectiveness of external audit on tax collection.
- To study the presence of regulatory body of external auditors affects the effectiveness of external audit on tax collection.
- To study audit firm size affects the effectiveness of external audit on tax collection.
- To study audit fee of external auditors affects the effectiveness of external audit on tax collection.
- To study audit tenure of external auditors affects the effectiveness of external audit on tax collection.
- To look at tax audit affects the effectiveness of external audit on tax collection.

## 1.4 Research Questions

The research has proposed to answer the following research questions;

Q1. How competence of External Auditors (EAs) affects tax collection?

Q2. What are the factors which affect awareness or attitudes of EAs for tax collection?

Q3. In what manner Independence of EAs affects tax collection?

Q4. Does the presence of regulatory body affect the effectiveness of EAs on tax collection?

Q5. In what prospect audit firm size of EAs affects tax collection?

Q6. Which constraints of audit fee of EAs affects tax collection?

Q7. What are the aspects audit tenure of EAs affects tax collection?

Q8. On what way tax audit of EAs affects tax collection?

## 1.5 Hypothesis Development

To maintain the specific and the general objectives the following hypothesis are formulated. The hypotheses are based on the role of EA firm on the growth of tax collection. .

- A competency is the ability of an individual to perform a job or task properly, being a set of defined knowledge, skills, and behavior. On the study of (Mansouri,et.al, 2009) on “Audit Competence and Audit Quality: Case in Emerging Economy” to examine the relationship between audit competence and audit quality they concluded that audit competence have a positive effect on detecting frauds. Other researchers studied the effect of audit competence and audit independence on audit quality (Halim, et.al, 2014) based on their respondent result audit quality will increase with the higher audit competence and higher auditor’s independence. To strengthen the hypothesis Bayou Tsegaw studied (Auditors Perception of Audit Quality in Ethiopia) and his result on the relationship between competence and audit quality Concluded that the respondents agree the audit competence is associated with higher audit quality.

**H1:** There is a positive relationship between Competence and effectiveness of EA on tax collection.

- Awareness represents the positive and negative evaluations that an individual holds of objects. It is assumed that attitudes encourage individuals to act according to them (Akalu, 2016). If every citizen considers the amount of tax he/she paid is for the sake of his/her interest, the tax collection process becomes effective and efficient and the government expenditure increases to satisfy the public interest. Awareness or attitudes towards tax is extremely important in a tax system which is based largely on voluntary compliance (Song, 1978). As an element of the population external auditors should have optimistic view in paying of tax and preparation of their customers' financial statements for the payment of tax. A taxpayer with positive attitudes towards tax evasion is expected to be less compliant than a taxpayer with negative attitude. Attitude towards tax evasion are often found to be quite positive (Kirchler, 2008). They should have awareness, the amount of money from them & their customers pocket is for the nation's existence. This is explained in the study of (Alm, 1992), If there is an increase in the amount individuals receive from a given tax payment, their compliance rate increases. Individuals then pay taxes to receive government services even when there is no chance to be detected or punished when evading.

As suggested by many studies awareness or attitude remains important for both the power and trust dimension. On the one hand, favorable attitudes will contribute to trust in authorities and consequently will enhance voluntary tax compliance. On the other hand, attitude towards tax authorities are also important as tax attitudes and ethics generally depend on perceived use of the money collected by the government (Kirchler, 2008)

Since taxes are an involuntary payment for government services, taxpayers have a strong incentive to minimize their tax liabilities either through avoidance (legal) or through evasion (illegal). (Bayou, 2017)

**H2:** There is a positive relationship between awareness or attitudes of EA on tax collection.

- Auditor independence refers to the independence of the external auditor. It is characterized by integrity and an objective approach to the audit process. The concept requires the auditor to carry out his or her work freely and in an objective manner. It is essential that auditors are independent and impartial, not only in fact or mind but also in appearance, it is a basic requirement for audit work as stated in Ethiopian Code of Ethics for professional Accountant (OFAG, 2009). The recent accounting scandals and the constraints imposed by SOX (Sarbanes-

Oxley), the SEC (Security Exchange Commission), and the PCAOB(Public Company Accounting Oversight Board) have greatly increased the sensitivity to and scrutiny of auditor independence (Bedard & Paquette, 2010). The users of audit reports must have confidence in the integrity and objectivity of auditors. Auditor-client relationship and taxpayer-tax officer relationship will affect the independence on audit report. (2012) Studied and concluded that independence, experience and accountability simultaneously affect the audit quality. Independence and accountability partially affects the audit quality. Independence of external auditors contribute a great share for audit quality, it is proven by the study of (Halim,et.al, 2014) and they found out that audit quality will increase with the higher audit competence and higher auditor's independence .additionally other researchers (Halim et al, 2014) studied “The Effect of Competence and Auditor Independence on Audit Quality with Audit Time Budget and Professional Commitment as a Moderation variable” and (James & Izien, 2014) studied Audit Firm Characteristics and Audit Quality in Nigeria auditor independence has a positive effect on audit quality).

Recent studies by (Abdi, 2017) on “Assessment of the Role of Audit Firms in Reducing Fraud” in 2017 and (Adane, 2014) on “Auditor responsibility and fraud detection: In Ethiopian private audit firm” in 2014 result showed that independence of extrnal auditors had a positive perception and influences auditors' expert performance to fraud detection. As a result independence significantly and positively affects the performance of external auditors to prepare an unqualified audit report.

**H3:** There is a positive relationship between Independence and effectiveness of EA on tax collection

- In our country there is no standard set by the government on the bases of audited and non-audited financial reports to report their tax liability. A tax payer at every category is allowed to present a financial report whether audited by external firms or not except corporate tax payers at LTO. This doesn't advocate tax payers to audit the financial statements. Tax payers audited there financial statements mainly for bank loan and shareholder reporting purpose.

In Ethiopia there is no quality review of auditors work, local professional accountancy qualification and strong professional association. Enforcement mechanisms of financial reporting requirements are nonexistent because of lack of capacity in regulatory institutions

and the absence of penalties in the regulations (World Bank, 2007). The absence of regulatory body tends external auditor to have little concern financial statements impact on tax collection. Other researchers work evidences also support the hypothesis, (Abdi, 2017) articulated lack of a professional accounting body which is strong and independent and absence of well-organized professional body in Ethiopia may cause auditors not be aware of and not to properly exercise their professional and legal responsibilities. And it is also stated on the work of (Engida, 2016), absence of regulatory body is a major factor behind the irregularities. Associations of auditors as well as accountants found in our country like EPAAA ( Ethiopian Professional Association of Accountants and Auditors), ASE ( Accounting Society of Ethiopia) and EEAA ( Ethiopian External Auditor Association) are not capable to guide the professionals ( (Kassahun, 2010); (Dessalegn, 2009). The emergence of AABE and its current activities propose to have a great hope to perform on the responsibilities carried by the government.

**H4:** There is a positive relationship between the presence of regulatory body and effectiveness of EA on tax collection.

- Audit firm size defined by (Arens A. A., 2012) as, “CPA firms’ size is a distinction of audit firm’s size based on: total revenues, number of partners, number of staff professionals, and number of offices. The four classifications based on such categories, are follows: Big 4 international firms, national firms, regional and large local firms, and small local firms”. (DeAngelo, 1981) Argues that the size of the audit firm is a proxy for audit quality. It so happens that no individual client has been audited by large a CPA firm, and hence a large CPA firm more likely to avoid tuitions that can interfere with their independence compared to small audits firm.

On the study of (Achyarysyah & Molina, 2014) titled “Audit Firm tenure, audit Firm size and Audit Quality” cited, Dopuch and Simunic (1980) work and revealed that large CPA firms provide high quality services because they have to maintain their reputation. Riyanto (2007) states that many researches use the size of audit firm as a proxy to measure audit quality. The research proves empirically that there is a big difference in audit quality between large audit firms (Big 4 audit firms) and small audit firms (Non Big 4 audit firms). Doogar 2005; Choi et. al. 2010). Preliminary studies found that the big 4 audit firms are relatively less frequently sued, and they are rarely penalized by the SEC (St. Pierre and anderson 1984; Palmrose 1988; Feroz et. al. 1991).

Furthermore, (Lawrence, Minutti, & M., 2011) says that the Big 4 provides higher audit

quality as large CPA firms support training programs, standardize audit methodology and provide more opportunity for peer review by another partner. In our nation the result is similar with the international as (Bayou, 2017) studied and asks six questions on the relationships between audit firm size and audit quality. The results of the responses for the questions show that the respondents agree that the big audit firms are associated with higher audit quality.

In contrast with most of researchers as cited on the work of (Bayou, 2017) audit firm size exhibited a non significant positive relationship with audit quality Enofeet al, (2013) studied the determinants of audit quality in the Nigerian business environment. This is also supported by the work of (Bethitina, 2015) and resulted audit firm size has little or no significance on audit quality.

**H5:** There is a positive relationship between audit firm size and effectiveness of EA on tax collection.

- Audit fee is the cost incurred by the company to pay a public accounting firm in order to audit the financial statements of the company (Toto & Stephanus, 2015). Audit fee sometimes can become an issue when abnormal rate is charged for a certain client. In some cases to have a better audit opinion, a client may pay a higher audit fee rate than it should pay.

In the dissertation (Rusmanto, 2002) on “An Investigation of factors Influencing Auditor Independence: A case of Indonesia” and (Asthaana & Boone, 2012) on “Abnormal Audit Fee and Audit Quality, Auditing”, they found that abnormal audit fees (audit fees that are beyond the norm / above average) negatively associated with audit quality issued by the audit firm. While research made by of (Barkess, R., & P., 1995) on “The Effect of Client Fee Dependence on Audit Independence” does not support that the audit fee does not affect the independence of the auditor.

As per studies conducted in our country there are similar findings that audit fee has significant effect on audit quality. (Solomon, 2016) and (Tamirat, 2014) both on commercial banks the result revealed that audit fee has a positive effect on audit quality. The result made by (Bayou, 2017) has shown that the respondents were neutral on the effect of high audit fee on audit quality. The respondents also believed that competition on audit fee will impair audit quality in Ethiopia and receiving high audit fee will impair auditor’s ability to withstand client pressure.

So there are no conclusive results or the agreement of the results of previous studies on the impact on the audit fee auditor independence or audit quality work.

**H6:** There is a positive relationship between audit fee and effectiveness of EA on tax collection.

- The audit tenure is “the duration of the auditor relationship with a client” as per a statement issued by (Sinason, Jones, & Dan, 2001). Other researchers like (Achyarysyah & Molina, 2014) as cited on the study of Amir and Farooq (2011) defines audit tenure as “the audit firm’s (auditor’s) total duration to hold their certain client or number of consecutive years that the audit firm (auditor) has audited its certain client”. Furthermore, (Carey & Simnett, 2006) on the study of “Audit Partner Tenure and Audit Quality” defines audit tenure as “period of engagement between the auditor with the client, namely the length of the auditor on the company’s audit clients. The auditor indicates the length of their work for clients in a matter of years”.

(Ghosh & Moon, 2005) The study on “Auditor Tenure and Perception of Audit Quality” found that the increase of audit quality is in line with the length of audit tenure. This statement indicates that the length of auditor-client relationship can improve audit quality. Effort to reduce the threat of undermining the objectivity of the auditor would be to ask the audit firm for rotation within a certain time frame. The other argument supporting the positive side of the length of audit states that an understanding of the business client and the industry is obtained after continuously repeated audits, thus improving audit quality. Furthermore, (Bamber & Iyer, 2007) on their work “Auditors' Identification With Their Clients and Its Effect on Auditors' Objectivity, Auditing” found that the length of engagement of auditor with client correlated to the increasingly high quality of the audit.

In the perspective of researches made in our country, the reasearchers have different results. The result shown on the work of (Shume, 2016 Determinants of pereceptions of External Auditors" Independence in Ethiopia Private Audit Firms), discovered that audit tenure has significant effect on auditor independence. Contrarily (Bayou, 2017) revealed that the respondents were neutral on the effect of long audit tenure on audit quality. On the other direction (Bethitina, 2015) on her study resulted that audit firm tenure has little or no significance on audit quality in manufacturing companies in Addis Ababa, Ethiopia .

**H7:** There is a positive relationship between audit firm tenure and effectiveness of EA on tax collection.

- Today financial statements audits are conducted in many different forms of organizations. The purpose of auditing is to discover, check, verify and control some or other aspects in an

organization. It can therefore be said that one of the main characteristics of an audit is that to diagnostic (Mutarindwa & Rutikanga, 2014).

In recent times tax agencies typically lose some percentage of total revenues due to tax evasion and other types of noncompliance known as the “tax gap” (Brown & Mark, 2006). The primary goal of a revenue body’s compliance activity is to improve overall compliance with their tax laws, and in the process instill confidence in the community that the tax system and its administration are fair. Instances of failure to comply with the law are inevitable whether due to taxpayers’ ignorance, carelessness, recklessness and deliberate evasion, or weaknesses in administration. At a time when tax evasion techniques have grown more sophisticated, tax agencies have simultaneously been hit with a cascade of budgetary and staffing restrictions, continually changing tax statutes and more rigorous requirements for privacy. As a result of these pressures, many tax agencies continue to rely on audits of taxpayers’ business records and financial affairs to ensure taxpayers have computed their tax payable in accordance with current tax laws and regulations and this implies the tax revenues growth otherwise, tax agencies can lose significant revenues opportunities.

Any tax system needs instruments to enforce fiscal laws. The most common instrument that has been used throughout the years is auditing the taxpayers. If a taxpayer is found not to be compliant, a fine is commuted. This scheme can be considered to be the most successful because it is the most widespread. However, the effectiveness of audits has only recently been investigated (Urpis, 2015/2016).

In more detail, according to (DeBacker, 2015) two opposite outcomes are possible, as taxpayers are influenced by two opposite effects: the target effect and the bomb-crater effect.

Under the target effect, audits can lower the level of evasion, since audited and fined taxpayers will change their expectations upward and declare more taxes to avoid incurring further audits. However, this effect may last for only a certain period of time, since, if no more audits take place, the expectation will shift downward. In the end, after an audit, a taxpayer’s level of compliance will immediately increase, but it will later decrease to the previous level.

The bomb-crater effect is the total opposite. Some taxpayers will believe that they will be very unlikely to incur another audit immediately after a control. Since these taxpayers

do not believe that an immediately subsequent audit is going to affect them, they will evade a great deal in the subsequent year(s) in order to recover from having to pay the fine.

Tax audit process is not fully covered by the Ministry of Revenues, it may be due to the small number of employees or poor administration. They give priority for the high risk tax payers, shut down businesses and audit request tax payers. Whereas, if the tax authority execute the audit process timely without delay the differences made between the external auditor and the tax auditor will be reconciled timely without bearing interest or penalty. In addition new regulations, laws and proclamations will be updated by the external auditors, which are distributed only to the tax authority offices or departments or any interested governmental body from the originate body. While the new regulations and laws are not addressed to external auditors directly by the tax authority or the concerning issuing body, tax auditors will be aware only by their own effort in result the tax collection process will not be adequate to meet the objectives

The delayed tax audit by ERCA exposed the tax payers for the unnecessary penalty and interest payment without any excuse even if the delay was made by the tax authority inefficiency. To the reverse when a tax payer has a refund amount for VAT or any other tax category the tax authority has not been calculated interest amount for the delayed period.

Attentive auditing will decrease the in-compliances behavior to minimize the liabilities to pay fines and penalties. Researchers' findings on fines and penalties showed, there is a clear suggestion to increase compliances, and provide in consistent results. However some studies resulted slight relation and tax audit may not increase the compliance behavior (Friedland, 1978). Additionally (Tilahun, 2014) probability of being audited have no significant impact on tax compliance behavior. Therefore, rather than trying to keep tax paying obligation of the tax payers by fines and penalties it is better to adopt serious and harmonized tax collection system.

Tax evasion behavior will be reduced if tax audit implemented on the tax payers financial statements (Dubin, 2004). Researchers who studied on tax audit proposed tax payers who have never been audited are not allowed to report their actual income (Hyun, 2005). However, the tax authority will incur an administrative cost during the tax audit work, it is a constraint of the fixed administration cost, an increase in the level of tax audit is required to decrease the level of other administrative functions, like tax payers service, tax collection etc (Akalu, 2016).

In the study of (Jeff & Jhon, 2018) the tax audit function increases compliance with tax and accounting regulations. In their study Prior to 2011, all Norwegian firms were required to be audited. In 2011, a law change allowed small Norwegian firms to choose not to be audited. After this change, the Norwegian Directorate of Taxes conducted on- and off-site inspections of a representative sample of 2,117 Norwegian firms, with a focus on compliance with specific requirements in tax and accounting regulation. They use the results from these inspections to construct a compliance quality score (CQS). They found that the firms that chose to opt out of auditing have lower CQS than do firms that chose to continue to be audited.

Finally, when tax audit is well conducted, taxpayers understand that their returns will be quickly and scientifically analyzed, voluntary compliance rates may rise which could help tax agencies avoid costs and further improve revenue collections, (Brown & Mark, 2006). Tax audit and compliance system, a comprehensive, integrated solution designed to improve tax auditor productivity and increase tax revenues.

In all developed countries, revenue agencies devote significant efforts and public resources to auditing taxpayers' reports and sanctioning taxpayers if they are found guilty. Despite the magnitude of the administrative and compliance costs created by these activities, the literature on the actual impact of audits has developed only recently. (Urpis, 2015/2016)

**H8:** There is a positive relationship between tax audit and effectiveness of EA on tax collection.

## **1.6 Significance of the study**

This study focused to find out the elements of effectiveness on performing a financial statement audit made by external auditors to bring an essential knowledge for the government to maximize its revenue expected from the tax payers which is a fundamental resource to build a country.

The study has the following importance;

- The absence of empirical evidences on the effectiveness of external auditors for tax collection in the country make difficult to understand and to measure the contribution of external auditors on tax collection, this study will provide an initial indication for further investigation on the issue
- It directs the government to think about the importance of external auditors on tax collection to

bear a binding regulated responsibility to perform their duties effectively for the contribution of a country growth.

- Absence of influential professional association as stated by (Dessaegn, 2009) and (Kassahun, 2010) the professional associations can't measure the effectiveness of accounting professionals like external auditors. This study will bring an insight to AABE to improve the association significance on the tax collection process.
- The study provides a contribution to the profession's development in Ethiopia.
- The study can be used as a reference for further researches.
- It gives positive insight for audit firms on how to add a value on effectiveness of external audit specifically to contribute a significance influence on the tax collection process in the country.
- It discloses the current status of external auditors in Ethiopia on their contribution of tax collection process.

### **1.7 Scope and limitation of the study**

This study is restrained within the territory of the effectiveness of external auditors on tax collection in Ethiopia; particularly those external audit firms based in Addis Ababa prepared an audit report for their clients reported their tax at LTO.

Lack of previous research studies and unavailability of sufficient current literatures on the subject of the effectiveness of external auditors on tax collection is another offensive factor. This research could not be seen from Ethiopian revenues and Customs Authority viewpoint which is in fact relevant to include this to come up effective results and the researcher believed this will be another research area. It is assuming *ceteris paribus*, which influences the tax collection process and have no relation with external audit.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 INTRODUCTION**

This chapter deals with the literature review and tries to relate the existing literatures crucial for this study. The principal interest of this chapter is to provide understanding about the theories and empirical evidences on the effectiveness of external audit, theories of auditing and tax.

The review has two sections. Section one presents a review on auditing and its objectives, effectiveness criteria of external auditors, theories of auditing, factors affecting auditor expert level of fraud reduction capabilities and concepts of auditing, tax regulation and theories of tax This is followed by a review of the relevant empirical studies on effectiveness of external audit on tax collection . At the last, conclusions on the literature review and knowledge gaps are presented in section.

#### **2.2 Theoretical review**

##### **2.2.1 Theoretical Review on Auditing**

###### **2.2.1.1 Definition of Auditing**

Auditing is a process for the accumulation and evaluation of information whether a company's financial statements are in compliance with established criteria and legislative requirement and confirm the information stated on the financial statement is materially correct and add value by forming an opinion which enhance the credibility of the information contained on the company's financial statement as its stated by IAASB (International Auditing and Assurance Standard Board, 2009).

###### **2.2.1.2 Theories of Auditing**

Auditing has been present for years in different stage of development following the evolution of accounting. Starting since the epoch when the records were approved after a public reading, to the era when government's officials were measured by their honesty. Followed by the times of the industrial revolution

were the ownership of companies started separating from management; when owners required more protection of their investments increasing the use of auditors, consequently; to the times were an auditor was always searching for frauds or errors (Whittington & Pany, 2004).

However, the acceptance of auditing as an academic discipline is not old and just after the development of different concepts and techniques within the audit model such as the use of sampling, the study of the internal control environment, and the risk assessment, is when more focus to the theoretical and conceptual framework of auditing it is been devoted.

Sayer (1992) discussed the concept of theories in social science from the perspective of “theory as an ordering-framework”, indicating that theory allows the use of the observed data and their relationships to predict and explain empirical events. Additionally (Cooper & Schindler, 1998) define theory as “a set of systematically interrelated concepts, definitions, and propositions that are advanced to explain and predict phenomena (facts)”. Another concept is expressed by (Singleton & Straits, 2005) explaining theory as a “set of interconnected propositions”. The success in the explanations or predictions of any phenomena depends on the level that the theory holds and do not fails fitting in the situation, and the challenge is to perfect the process of matching theory and fact (Cooper & Schindler, 1998).

Different authors have started the development of the audit theory such as (Mautz & Sharaf, 1961) with their publication titled “The Philosophy of Auditing”; also and David Flint (Flint, 1988) with his book Philosophy and principles of auditing. The auditing analysis in this demonstration will be framed on the postulates proposed by (Flint, 1988) as a foundation for the theory of auditing.

Flint (1988) Stated that there is a matter of public accountability demanding an independent audit for its demonstration with clear definition and intention, based on evidence that only skilled auditors gather, measure it, and compare it against the standards, which generates economic or social benefit. Following are the seven postulates or assumptions stated by Flint (1988):

1. There is a relationship of accountability or a situation of public accountability.
2. Accountability cannot be demonstrated without an audit.
3. An audit requires independence and freedom.
4. The subject matter of audit is susceptible to verification by evidence.
5. Auditors are skilled judges who are able to measure and compare actual performance against standards of accountability.
6. The meaning, significance, and intention of statements to be audited must be clear.
7. An audit produces an economic or social benefit.

On the study of (Mahdi, 2011) about “Audit expectation gap: concept, nature and trace” explained, the demand for audit arises from the potential conflict of interest that exists between stakeholders and managers. The contractual arrangement between these parties normally requires that management issue a set of financial information that purports to show the financial position and results of operations of the entity. A brief analysis of the theories advocating the need for auditing giving rise to contractual arrangement under: (a) The Lending Credibility Theory (b) The Theory of Inspired Confidence (Limperg, 1932) (c) Agency Theory, (Watts and Zimmerman) ; (d) The Police man theory (e) Moderator of Claimants’ Theory and (f) Agency Theory

#### **2.2.1.2.1 The Lending Credibility Theory**

This theory derives from another public perception that the primary function of auditing is the addition of credibility to the financial statements. Audited financial statements are used by management to enhance the stakeholders’ faith in management’s stewardship. If stakeholders such as stockholders, government, or creditors have to make their judgments based on the information they receive, they must have faith that this is a fair representation of the economic value of the firm. An audit thus reduces the “information asymmetry” between management and other stakeholders. However, there is an efficient markets theory that holds that audited information does not form the primary basis for investors’ investment decisions.

#### **2.2.1.2.2 The Theory of Inspired Confidence (Limperg, 1932)**

Unlike the other theories, this theory addresses both the demand and the supply of audit services. According to Theodore Limperg the demand for audit services is the direct consequence of the participation of outside stakeholders (third parties) in the company. These stakeholders demand accountability from the management, in return for their contribution to the company. Since information provided by management might be biased because of a possible divergence between the interests of management and outside stakeholders, an audit of this information is required. With regard to the level of audit assurance that the auditor should provide, (the supply side), Limperg argues that the auditor should act in such a way that he does not disappoint the expectations of a “rational outsider” on the one hand, while, on the other hand, he should not arouse greater expectations in his report than his examination justifies. So, given the possibilities of audit technology, the auditor should do everything to meet reasonable public expectations.

#### **2.2.1.2.3 Agency Theory , (Watts and Zimmerman)**

A reputable auditor (Watts & Zimmerman, 1983) - an auditor who is perceived to meet expectations - is appointed not only in the interest of third parties, but also in the interest of management. A company is viewed as the result of more or less formal “contracts”, in which several groups make some kind of contribution to the company, given a certain “price”. Company management tries to get these contributions under optimum conditions for management: low interest rates from bankers, high share prices for stockholders, and low wages for employees. In these relationships, management is seen as the “agent,” trying to obtain contributions from “principals” such as bankers, stockholders and employees. Costs of an agency relationship are monitoring costs (the cost of monitoring the agents), bonding costs (the costs, incurred by an agent, of insuring that agents will not take adverse actions against the principals), and residual loss (effective loss that results despite the bonding and monitoring costs incurred)

#### **2.2.1.2.4 The Police man theory**

This was the most widely held theory on auditing until the 1940s (Hayes, Schilder, Dassen, & Wallage, 1999). Under this theory, an auditor acts as a policeman focusing on arithmetical accuracy and on prevention and detection of fraud. However, due to its inability to explain the shift of auditing to, ‘Verification of truth and fairness of the financial statements,’ the theory seems to have lost much of its explanatory power (Mahdi, 2011).

#### **2.2.1.2.5 Moderator of Claimants’ Theory:**

Under this theory, it is important that all vital participants in an organization continue to contribute. In order to continue these contributions, it is important that each group believes it receives a fair share of the company’s income by giving an opinion on the various interests represented in the amounts shown therein (Mahdi, 2011)

#### **2.2.1.2.6 Quasi-Judicial Theory:**

In this theory, the auditor is regarded as a judge in the financial distribution process (Hayes et al., 1999). However, (Porter, 2003) concludes that (i) an auditor’s decisions and decision process

are not publicly available; (ii) the doctrine of precedence/consistency is not guaranteed in auditing; and (iii) an auditor's independence differs from a judge's independence because of the different reward system involved (Shodhganga, 2019)

### **2.2.1.3 An effective external audit process**

An effective audit process is defined by several authors, association and organizations from which Institute of Chartered Accountants in England and Wales (ICAEW) 2003, has documented the following formal definition; "Effectiveness can be regarded as a composite of competence, procedural arrangements, quality control and quality assurance. The procedural arrangements can be regarded as the tools used by firms and individuals to ensure that audits comply with technical standards, i.e. legal requirements, regulators' requirements and auditing standards set by the APB [Auditing Practices Board], and taking into account the supplementary material in APB Practice Notes and Bulletins". In the view of Ken Williamson on the journal article stated (Williamson K., August 2015), a high quality audit truly challenges and tests the contents of the financial statements in order to form an opinion on whether they present a true and fair view. Fundamentally, an effective audit process must deliver the right audit opinion supported by appropriate audit evidence and professional judgments, in which shareholders and other stakeholders have confidence.

Ken Williamson (2015), who is a Partner Head of Corporate Governance in UK, updated his 2013 report on "Assessing the effectiveness of the external audit process A practical guide and tool for audit committees" by adding two relevant publications by The Financial Reporting Council (FRC) and The Center for Audit Quality (CAQ). On his report external auditors must comply with all relevant auditing and ethical standards and professional and regulatory requirements. Beyond that, an effective audit must include: (a) An audit process tailored to the risks facing the company, the business structure and the regulatory environment. (b) An audit team that is technically strong, rigorous, perceptive, intellectually curious and independent-minded – bringing an informed professional skepticism to bear on management's approach and assertions. (c) An audit team that supports and promotes a culture of consultation and fully integrates specialists and experts. (d) An audit approach that is based on an understanding of the company's control environment, including the role

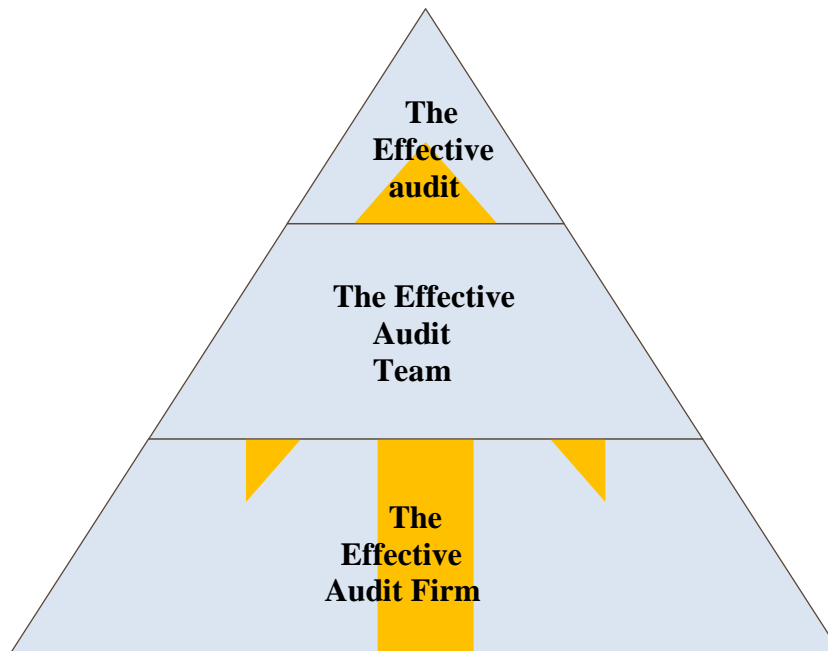
of information technology in supporting the financial reporting process. (e) A culture in the audit firm that seeks continuous improvement and increased quality and that sets the right tone on professional and ethical matters including quality, objectivity and integrity.

**Other characteristics of an effective audit include:**

- i. Communications and reports to those charged with governance that reflect the audit team's thought processes and rationale for conclusions. These should discuss management's approach, alternatives considered, relevant comparators and a clear articulation of the final conclusion.
- ii. Effective interaction between the auditor, management and the audit committee throughout the audit process – everyone must understand what the 'audit issues' are, why they are issues and how they will be resolved.

Whilst the external auditor is in large part responsible for the effectiveness of the audit process, management and the audit committee have an important influence. Their contributions should also be considered in the overall assessment of the effectiveness of the external audit process.

## Appendix – The pyramid of audit effectiveness



Ruth Bender (2006) on the journal of “The Voice of Business” under the title of “What is an effective audit and how can you tell” figured out the pyramid of audit effectiveness as per shown above. The aim is to achieve an effective audit. In order to achieve this aim, both the audit team and the audit firm need to be considered. It is unlikely that an effective audit could be done by an ineffective audit team, except by accident. Thus the effectiveness of the team is an essential precondition for audit effectiveness. Likewise, an effective audit team is most likely to come out of an effective firm, one that has the ability to attract good people, and the systems in place to train and support them in their professional activities. An effective firm is no guarantee of an effective team; and an effective team is no guarantee of an effective audit. However, the absence of any of these building blocks must cause concern to the audit committee in its evaluation of the audit

## **2.2.2 Theoretical Review on Tax**

### **2.2.2.1 Introduction to Taxation**

Taxation is an imposition of compulsory levies on individuals or entities by governments. Taxes are levied in almost every country of the world; primarily to raise revenue for government expenditures, although they serve other purposes as well (Neumark, S.Cox, & E.Maclure, 2019).

In modern economies taxes are the most important source of governmental revenue. Taxes differ from other sources of revenue in that they are compulsory levies and are unrequited—i.e., they are generally not paid in exchange for some specific thing, such as a particular public service, the sale of public property, or the issuance of public debt. While taxes are presumably collected for the welfare of taxpayers as a whole, the individual taxpayer's liability is independent of any specific benefit received. There are, however, important exceptions: payroll taxes, for example, are commonly levied on labor income in order to finance retirement benefits, medical payments, and other social security programs—all of which are likely to benefit the taxpayer. Because of the likely link between taxes paid and benefits received, payroll taxes are sometimes called “contributions”. Nevertheless, the payments are commonly compulsory, and the link to benefits is sometimes quite weak.

It is important to note that taxation goes along with citizenship responsibility and participation in the tax system of an economy. Individual taxpayers are required to pay taxes on all personal income earned in a given tax year. The Ethiopian tax year usually begins on the 8<sup>th</sup> of July and ends on the 7<sup>th</sup> of July. Incomes earned in a given tax year should to be reported between 8<sup>th</sup> of July and 10<sup>th</sup> of November of the following tax year. A tax payer shall not change its accounting year unless it obtains prior approval, in writing, from the tax authority and complies with any condition that may be attached to the approval

#### **2.2.2.2 Objectives of Taxation**

As per the statement by Ritika Muley on economic discussion web site (Muley, 2019), the primary purpose of taxation is to raise revenue to meet huge public expenditure. Most governmental activities must be financed by taxation. But it is not the only goal. In other words, taxation policy has some non-revenue objectives.

Truly speaking, in the modern world, taxation is used as an instrument of economic policy. It affects the total volume of production, consumption, investment, choice of industrial location and techniques, balance of payments, distribution of income, etc.

Here we will discuss the objectives of taxation in modern public finance:

**i. Economic Development:**

One of the important objectives of taxation is economic development. Economic development of any country is largely conditioned by the growth of capital formation. It is said that capital formation is the kingpin of economic development. But Least Developing Countries (LDCs) usually suffer from the shortage of capital.

To overcome the scarcity of capital, governments of these countries mobilize resources so that a rapid capital accumulation takes place. To step up both public and private investment, government taps tax revenues. Through proper tax planning, the ratio of savings to national income can be raised.

By raising the existing rate of taxes or by imposing new taxes, the process of capital formation can be made smooth. One of the important elements of economic development is the raising of savings- income ratio which can be effectively raised through taxation policy.

However, proper care has to be taken, regarding investment. If financial resources or investments are channelized in the unproductive sectors of the economy the economic development may be jeopardized, even if savings and investment rates are increased. Thus, the tax policy has to be employed in such a way that investment occurs in the productive sectors of the economy, including the infrastructural sectors.

**ii. Full Employment:**

Second objective is the full employment. Since the level of employment depends on effective demand, a country desirous of achieving the goal of full employment must cut down the rate of taxes. Consequently, disposable income will rise and, hence, demand for goods and services will rise. Increased demand will stimulate investment leading to a rise in income and employment through the multiplier mechanism.

**iii. Price Stability:**

Thirdly, taxation can be used to ensure price stability—a short run objective of taxation. Taxes are regarded as an effective means of controlling inflation. By raising the rate of direct taxes, private spending can be controlled. Naturally, the pressure on the commodity market is reduced.

But indirect taxes imposed on commodities fuel inflationary tendencies. High commodity prices, on the one hand, discourage consumption and, on the other hand, encourage saving. Opposite effect will occur when taxes are lowered down during deflation.

**iv. Control of Cyclical Fluctuations:**

Fourthly, control of cyclical fluctuations—periods of boom and depression—is considered to be another objective of taxation. During depression, taxes are lowered down while during boom taxes are increased so that cyclical fluctuations are tamed.

**v. Reduction of Balance Of Payments (BOP) Difficulties:**

Fifthly, taxes like custom duties are also used to control imports of certain goods with the objective of reducing the intensity of balance of payments difficulties and encouraging domestic production of import substitutes.

**vi. Non-Revenue Objective:**

Finally, another extra-revenue or non-revenue objective of taxation is the reduction of inequalities in income and wealth. This can be done by taxing the rich at higher rate than the poor or by introducing a system of progressive taxation.

### **2.2.2.3 The Ability-to-pay Theory of Taxation**

M. Slade Kendrick, who is a professor at Cornell University (Slade, 1939) developed a well known theory “The Ability-to-pay Theory of Taxation”. According to this theory the fundamental issue is “Ability to pay” the dominant theory of taxation is usually interpreted in terms of sacrifice. It is held to justify progressive taxation under any one of three possible interpretation of sacrifice the equal, equal-proportional and least-sacrifice theories. These theories rest in turn on three assumptions: the declining marginal utility of money with an increase in its supply, the existence of sacrifice. Analysis disclose each of this supports to be defective and there by breaks down the

theory of ability to pay. Progressive taxation may however be justified on other grounds. These grounds should be founded on the broad realities of the economic systems. Taxes have economic effects and these effects entail social consequences. The choice of the taxes to be laid and rates at which they are to be applied expresses a preference for one set of effects, and hence of consequences, to another. The theory of taxation, progressive or other should correspond to these facts. The thin nebula of hedonism in reverse is no longer adequate.

This theory was explained in the work of (Bayou, 2017), this doctrine has been in trend for at least as long as the benefits theory. This theory was bound to be supported by socialist thinkers because of its conformity with the ideas and concepts of justice and equity. However, the doctrine received an equally strong support from non-socialist thinkers also and became a part of the theory of welfare economics. The basic principle of this theory is that the burden of taxation should be shared by the members of society on the principles of justice and equity and that these principles necessitates that the tax burden is apportioned according to their relative ability to pay theory.

#### **2.2.2.4 Ethiopian tax Laws as per income tax proclamation No. 979/2016**

##### **I. Categories of tax payers**

As per the federal income tax proclamation No 979/2016 (Parliament, 2016) , the following business taxpayers are categorized. Category “A” taxpayer, being a company or any other person having an annual gross income of Birr 1,000,000 or more. Category “B” taxpayer being a person, other than a Company, having an annual gross income of Birr 500,000 or more but less than 1,000,000. Category “C” taxpayer being a person other than a Company, having an annual gross income of less than Birr 500,000.

The Minister of Revenue may, after ascertaining by economic analysis, change the annual gross income for the classification of a taxpayer as a category “A” taxpayer category “B” taxpayer or category “C” taxpayer.

##### **II. Residence**

The following are residents of Ethiopia, (a) a resident individual; (b) a resident body; (c) the Government of Ethiopia, and any regional state or city government in Ethiopia. A resident

individual is an individual who: (a) has a domicile in Ethiopia; (b) is a citizen of Ethiopia who is a consular, diplomatic, or similar official posted abroad; (c) is present in Ethiopia, continuously or intermittently, for more than 183 days in a one-year period.

An individual who is a resident of a tax year (referred to as the “current tax year”), but who was not a resident individual for the preceding tax year shall be treated as a resident individual in the current tax year only for the period commencing on the day on which the individual was first present in Ethiopia.

An individual who is a resident individual for the current tax year but who is not a resident individual for the following tax year shall be treated as a resident individual in the current tax year only for the period ending on the last day on which the individual was present in Ethiopia.

A resident body is a body that: (a) is incorporated or formed in Ethiopia; or ( b) has its place of effective management in Ethiopia. A resident company is a company that is a resident body. A non-resident is any person who is not a resident of Ethiopia.

### **III. Source of Income**

1. Employment income derived by an employee shall be Ethiopian source income: (a) to the extent that it is derived in respect of employment exercised in Ethiopia, wherever paid; or (b) if it is paid to the employee by, or on behalf of, the Government of Ethiopia, wherever the employment is exercised.
2. Business income derived by a resident of Ethiopia shall be Ethiopian source income except to the extent that it is attributable to a business conducted by the resident through a permanent establishment outside Ethiopia.
3. Business income derived by a non-resident shall be Ethiopian source income to the extent that it is attributable to: ( a) a business conducted by the non-resident through a permanent establishment in Ethiopia; (b) sales in Ethiopia by the non-resident of goods or merchandise of the same or similar kind as those sold by the non-resident through a permanent establishment in Ethiopia; or (c) any other business activity conducted by the non-resident in Ethiopia of the same or similar kind as that conducted by the nonresident through a permanent establishment in Ethiopia.
4. Despite sub-articles (1), (2), and (3) of this Article, income derived by a person shall be Ethiopian source income if it is: (a) a dividend paid to the person by a resident body; (b) rental

income from the lease of: (1) immovable property located in Ethiopia; or (2) movable property located in Ethiopia subject to tax under Article 57 of the Proclamation; (c) a gain arising from the disposal of the following: (1) immovable property located in Ethiopia; (2) a membership interest in a body, if more than 50% of the value of the interest is derived, directly or indirectly through one or more interposed bodies, from immovable property located in Ethiopia; (3) shares in, or bonds issued by, a resident company; (d) an insurance premium relating to the insurance of a risk in Ethiopia; (e) income from a performance or sporting event taking place in Ethiopia; (f) winnings from a game of chance held in Ethiopia; (g) interest, a royalty, management fee, technical fee, or other income subject to tax under this Proclamation: (1) paid to the person by a resident of Ethiopia, other than as an expenditure of a business conducted by the resident through a permanent establishment outside Ethiopia; or (2) paid to the person by a non-resident as an expenditure of a business conducted by the non-resident through a permanent establishment in Ethiopia.

5. Foreign income is any income that is not Ethiopian source income.

#### **IV. Schedules of Income**

1. The Proclamation provides for the taxation with the following schedules:

- a) Schedule 'A', income from employment;
- b) Schedule 'B', income from rental of building
- b) Schedule 'C', income from business;
- c) Schedule 'D', other income;
- d) Schedule 'E', exempt income.

2. Subject to Article 60(2) of the Proclamation number 979/2016, a taxpayer that derives income from different sources subject to tax under the same Schedule for a tax year shall be taxable under the Schedule on the total income for the year.

## V. Employment Income Tax Rates

**Table 2.1 ; The tax rates of employment income tax are:**

<b>Employment Income (per month) Birr</b>	<b>Employment Income Tax Rate</b>
0 – 600	0% (Exempted)
601-1,650	10%
1,651-3,200	15%
3,201-5,250	20%
5,251-7,800	25%
7,801-10,900	30%
Over 10,900	35%

Source: Proclamation number 979/2016

## VI. Business Income Tax Rates

1/ The rate of business income tax applicable to a body is [30%].

2/ The rates of business income tax applicable to an individual are:

**Table 2.2 ; The tax rates of business income tax are:**

<b>Taxable Income (per year) Birr</b>	<b>Business Income Tax Rate</b>
0 – 7,200	0%
7,201-19,800	10%
19,801-38,400	15%
38,401-63,000	20%
63,001-93,600	25%
93,601-130,800	30%
Over 130,800	35%

Source: Proclamation number 979/2016

## 2.3 Empirical Review

This section of review focuses on the previous studies or researches conducted by various researchers on the issue effectiveness of external auditor on tax collection. There are a lot of researchers studied on the issue of external audit and tax collection separately, as far as the researcher reviewed it is difficult to gather related documents in our country on the issue of the effectiveness of external audit on tax collection small number of researches investigated abroad. The essence of this empirical review is to understand former researchers' findings on the relation between external audit report and the tax collection. This will be an indication to direct the loopholes. The researcher tried to investigate the cases which have a direct impact for tax growth when an audit is conducted by external audit firms in our country at corporate level.

The audit profession is crucial to current economies because of the reasonable assurances that auditors provide to users of financial statements. Auditing increases the reliability of financial information provided to investors, owners, creditors and other users because fraudulent activities very affect to entity and auditors play an important role in detection and prevention fraud (Arens, A.A., & Leobbecke, 2000). The need for external auditors may be seen as a response to the agency problem and the audit functions as a mechanism to attest to the accountability and stewardship of company management to reduce the possibility of innocent mistakes and deliberate misstatements such as fraud and management manipulation .

The availability of professional service providers or external auditors plays an important role to the tax growth activity. This value has been conceived by the government of Ethiopia, as a testimony, under the Prime Minister a board was established which controls the accounting professional services known as AABE. To increase the “competence and responsibility” of the accounting professionals the criteria set by AABE to be an authorized auditor or an accountant is very strong when comparing with other professions. It confirms us how much the government wants to keep the profession.

Financial statements audited by external audit firms has better value by Ethiopian Revenues and Customs Authority (ERCA) than compared to non-audited. One of the indication for this is the proclamation issued by House of Representatives (Representative, 2016) , it explained about loss carry forward under proclamation no 979/2016 article 26. If a tax payer has a loss for a tax year, the tax payer shall carry the amount of the loss forward to the next following

tax year and the loss shall be allowed as a deduction in computing the taxpayer's taxable income for that following year. However the proclamation will be exercised if and only if the loss amount has been approved by the external audit firms. Not only by the tax collector office but also the National Bank of Ethiopia needs an audited financial statements from borrowers of banks if the amount of borrowing is more than five million Ethiopian birr. Additionally stakeholders of corporate companies expect audited financial statements at the time of annual general meeting to decide on dividend amount and investment expansions. Such optimistic feeling of financial statement users for the audited report revealed that the necessity of external auditors services and the weight of audited financial statements.

The emergence of professional service firms in recent years has resulted from a growing demand from businesses for specialist advice to help them achieve business advantage in an increasingly competitive market place. Much of this advice is requested from audit firms, first because auditors are trained to understand the dynamics of a business from an external perspective and also because independent viewpoint can often shed light on problems that may appear intractable from within an organization.

Corporations can hide aggressive tax planning in aggregate numbers on tax returns and financial statements. Company directors either are uninformed about, or acquiesce in or agree, potentially abusive tax planning. Audit firms do not highlight these issues for directors or investors and, in some cases, actively assist in designing aggressive tax shelters for lucrative fees (Linda, 2004). Abusive tax and accounting gimmick or tricks sometimes go hand-in-hand. Tax savings boost book revenues. Corporations that engage in sham tax transactions may be more likely to take questionable accounting positions, and auditors that promote abusive tax shelters may be more likely to acquiesce in abusive accounting. The rapid expansion of accounting firms into multidisciplinary practice areas facilitates companies' participation in tax shelters and undermines directors' and investors' assessments of tax risks.

Similarly directors likely have insufficient information about a reporting company's tax risks to permit effective monitoring of internal tax and accounting functions or company participation in potentially abusive tax transactions. Those information asymmetries also leave investors without tax risk information that would otherwise factor into investment decisions

Tax shelter strategy or hiding tax payments by clients of audit firms or by external auditors whether it is intentional or not will result a massive damage. In our country the ERCA auditors

audit tax payers financial statements for last five years report based on a regulation issued or “Yirga” law. If that is a criminal case it extends to ten years. The findings by auditors are the liabilities of the tax payers which are the unpaid tax amount (Fire Gibir), this is an amount result by the difference of the paid and the total tax amount which is the un-paid tax amount. This unpaid tax costs the tax pair to pay penalty and interest which is measurable amounts the tax payers forced to pay. Within five years and above the interest amount equals the tax amount or more than. Under the provision of tax 979/2016 as it is also stated on the study of (Akalu, 2016), if any amount of tax is not paid by the due date, the taxpayer is obliged to pay interest on such amount for the period from the date the tax is due to the date it is paid.

The interest rate is set at 25% (twenty five percent) over and above the highest commercial lending interest rate that prevailed during the preceding quarter, but the amount of interest doesn’t be more than the tax liability as per the federal tax administrative law article 48 (EFDRE, 2016) .

These costs of accounting scandals has been shown all over the globe, (Linda, 2004) stated, the participation in abusive tax shelter transactions can result in significant economic costs and market distortions. If a transaction is discovered on audit, companies will likely spend considerable sums for legal and accounting assistance in defending the strategy. At some point, a decision will have to be made to settle or contest the assessed tax liability. Settlement may entail interest and penalties in addition to taxes. Although small settlements are not likely to lead to further financial problems, a substantial tax claim and related interest and penalties could impact liquidity and debt servicing costs.

Costs of accounting scandals mount quickly. They include legal and investigative costs, damages in securities lawsuits, inability to pass costs on to insurers, liquidity problems and higher debt service costs, and rating agency downgrades. The Enron debacle is a prime example of the cascading effect of accounting irregularities: total loss of investor confidence, the implosion of its long-term auditor, and, ultimately, bankruptcy.

On the work of Linda M. Beale (2004) “Putting SEC Heat on Audit firms and Corporate Tax Shelters: Responding to Tax Risk with sunshine Shame and Strict Liability” stated, in the U.S.A. the treasury has reported “anecdotal evidence” that abusive corporate tax shelters reduce federal tax revenues by \$10 billion annually, at a minimum. The strategy for curbing or restriction abusive corporate tax shelter growth shows promise but could be enhanced by

performance measure. (Pamela, Gardner & Gordon, & Milbourne, 2001). Yearly 25 to 45 billion dollar of lost tax revenues annually from abusive tax schemes (Silow, 2003).

In the U.S.A. corporate income tax revenues declined significantly over the last half-century as a proportion of the gross domestic product, from 4.18% in 1949 to barely more than 1.50% in 2004, a 64% decline. (Robert & T.D., 2000) Reported that corporations have shouldered a declining share of the income tax burden in the last decade, from around 21% of total taxes paid in 1994 to 17% in 2000, based on reviews of income tax records of 250 public companies. The 2002 fiscal year statistics shows that the share of federal taxes paid by corporations has declined further to 10.5%.

Tax revenue (% of GDP) in Ethiopia was reported at 8.7647 % in 2013, according to the World Bank collection of development indicators, compiled from officially recognized sources. And also, as per a report announced by nazret.com sentenced by Groum Abate (Abate, 2009) Ethiopia's ratio of tax revenue to gross domestic product (GDP) is still well short of the international average. The ratio of tax revenue to GDP in Ethiopia is less than 11 %, while in many African countries the ratio exceeds 20 per cent. It is about 40 per cent in higher income countries.

The Ethiopian average for the last five years is also 11 per cent, while other Sub Saharan countries managed to collect over 16%. Other middle income countries also manage to get 25 %.

According to the paper presented by Belachew Beyene, Director of Duties and Tax Audit at the Federal Customs and Revenue Authority, cited by Groum Abate at a seminar organized by the Association of Chartered Certified Accountants (ACCA) , the authority is working to improve the low ratio percentage of GDP by establishing a modern revenue assessment and collection system; enhancing voluntary compliance; enforcing tax and customs laws by preventing and controlling contraband as well as tax fraud and evasion; and to collect tax on time. Thus to avoid fraud and evasion the revenue authority is expected to deal with external auditors limitations, because the financial statements reported by this entities are susceptible to fraud and evasion to decrease the tax amount paid by their clients.

The professional service providers must cooperate with the authority to facilitate the tax collection process. The government also considers the value of these firms for the goal of its objectives to stimulate the tax payers' awareness; otherwise it's difficult to meet the mission. According to the information obtained from large tax payer's office, as Akalu kibret studied on

determinants of tax compliance behavior of large corporate tax payers in Ethiopia, number of non filers, null-declarants and amount of tax collected from enforcement activity showed continual increment. These corporate taxpayers have a major share of the total tax revenue. In our country 70 % of the country's tax revenue originates from corporate tax payers; however it only constitutes 5% of the total tax payers.

## **2.4 Summary on Literature Review**

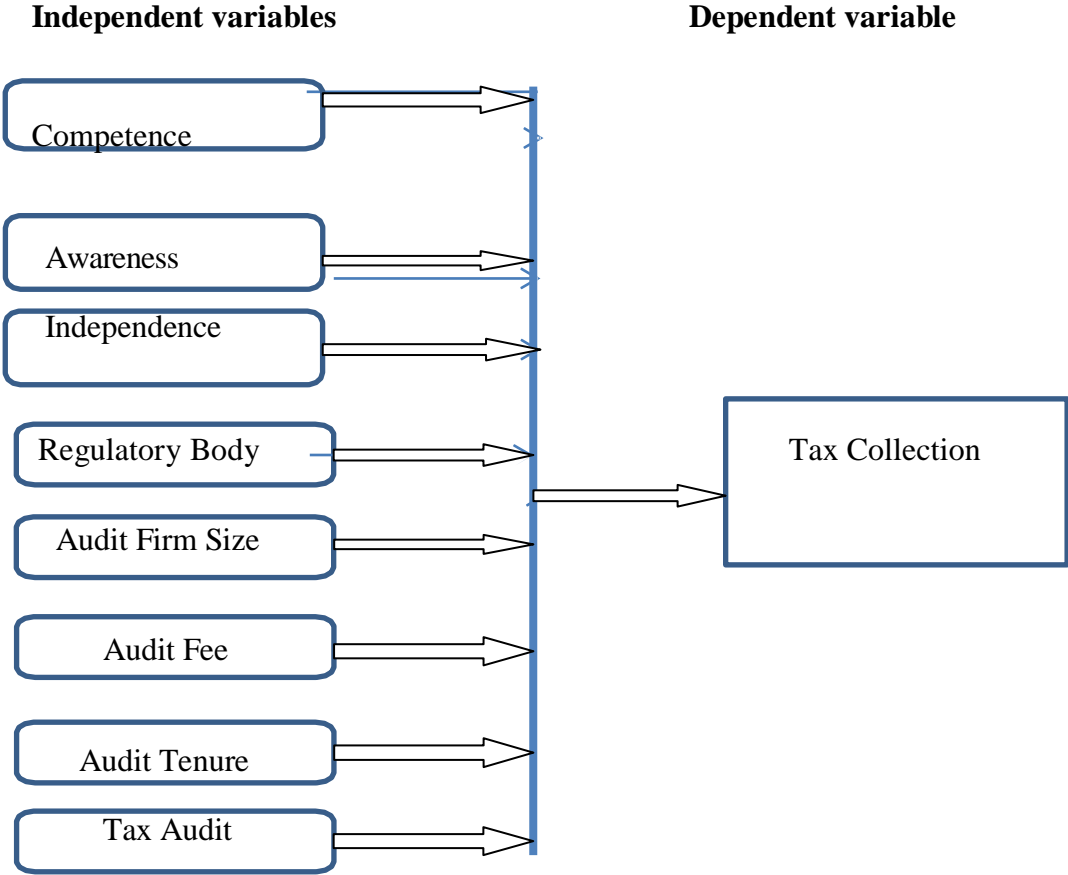
The tax collection process has influenced by a lot of factors, the factors may arise from internal or external sources. In Ethiopia there is no enforceable act that tax payers would to submit a financial statement audited by the audit firms. It is difficult to find out, audited financial statements has an adverse effect or not on tax collection. There is no research to support this as far as I traced. But the Ministry of Revenues has optimistic view on the audited financial statements, not only audited but also the financial statements prepared by accountants certified by AABE.

The effectiveness of external auditors is vital for the financial statement report as it was discussed on the literature reviews. On the tax perspective the effect must be studied in the future researches at different national level category. This research will brought an insight for other researchers on the issue.

## 2.5 Conceptual Framework

The conceptual framework summarizes the model of the study in terms of variables relationships. The main variables of the study are; Competence, Awareness, Independence and Controlling Body .The variables are considered in the study as independent variables which impact on the amount tax revenue in ERCA LTO.

Figure 2.1 conceptual Framework



Source: Developed (constructed) by the researcher from different literatures.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

This chapter presents the methodological concerns used in conducting this research, and provides justification for each step taken. It involves the research method, research design, population and sampling of the study, sample size and sampling technique, Sources of data, research instrument and methods of data analysis.

#### **3.2 Research Method**

To achieve the main objectives of the study a mixed approach (both quantitative and qualitative) data used. The purpose of using such a mixed approach is to gather data that could not be obtained by adopting a single method and for triangulation so that the findings with a single approach could be combined with others wherever possible. The triangulation is between ERCA officers of tax audit department who have a title of team leader ( Budin Astebabari) the response obtained by interview and the response obtained from external auditors through questioners.

The study will be used surveys of auditors in sampled audit firms which are found in Addis Ababa with semi- structured questionnaires. The surveys were planned to obtain data relevant on roles and responsibilities of external auditors in achieving effective result, constraints exist on external auditors in attempt to exercise their responsibility and from revenue employees' side to know the benefits of audited financial statement in aggravating the tax collection process with the aim of showing and exploiting useful information which is not available from other sources..

#### **3.3 Research Design**

The study used explanatory research design; it is a type of study that involves observation of all of a population, or a representative subset, at one specific point in time. It is descriptive in its nature and is opposite of longitude research.

The study used a quantitative, descriptive research using a questionnaire. A descriptive research is a research for which the purpose is to produce an accurate representation of persons, events or situations (Saunders et al, 2009). The questionnaires are prepared by Likert scale

questions. Mostly, Likert scale questions have five degrees namely Strongly Agree, Agree, Neutral (Undecided), Disagree, and Strongly Disagree that are combined into a single composite score/variable during the data analysis process (Kothari, 2004; Boone Jr & Boone, 2012). A “good” Likert scale is a scale which is balanced on both sides of a neutral option, creating a less biased measurement. The actual scale labels, as well as the numeric scale, may vary (Vanek, 2012). The numbers indicate in the questions provided to feed ordinary scale measurement and to generate data suitable for quantitative analysis (Boone Jr & Boone, 2012).

### **3.4 Population and Sampling of the Study**

#### **3.4.1 Population of the study**

Defining the population is the first step in designing the sample (Creswell, 2009). The population of the study is external auditors based in Addis Ababa. Therefore, the population of the study is external auditors expected that have adequate knowledge of the variables in the hypothesis as all of the variables relate to external audit practices. External auditors supposedly possess intimate knowledge of several aspects of their organizations, the government tax laws and regulations, the countries trade law and related knowledge with regarding their professions. Thus, their views considered appropriate source of data.

#### **3.4.2 Sampling Design**

As noted in (Jonker & Pennink, 2010) it is obvious that researchers are typically unable to study the entire population. Therefore, researchers typically study a subset of the population which known as a sample. A sample is a portion of the population that inferences are to be made about the population. However, it is important that the sample be representative of the population from which it was selected.

The population considered in this study is the number of private audit firms in Addis Ababa, first audit firms had been selected and then auditors and other people in the audit firms like audit firm managers. According to (Agresti & Finlay, 2008), Multi-stage sampling represents form of cluster sampling in which larger clusters are further subdivided into smaller, more targeted groupings for the purposes of surveying. According to AABE web site, the total numbers of

private audit firms authorized by AABE are 125. According to Cohen et al. (2005), covering the entire companies in the study makes the study difficult. Therefore, out of the total number of private audit firms in Ethiopia, the researcher decided to draw 20 sample audit firms based in Addis Ababa of the whole population for investigation. The rationale behind to select only 20 audit firms are taking in to account the previous research studies and judgments, for example research conducted by Muluneh (2009), the available resources, time, and budget. Given audit firms which have more than five auditors they are relatively large in size which means they do have the opportunity to deal with different sectors (clients) which gives them a terrific experience for many audit related problems. This is invaluable for the main intent of the paper. The proportion of the total audit firms to the sample selected was not equal size. According to Mui (2010) study on external auditors expert performance, auditors and audit firms provide the same professional service despite their legal classification. Hence, the equal selection of audit firms based in Addis Ababa despite their variation in proportion does not have a significant impact for this study. To get the advantage of equal number of respondents the researcher drawn, five auditors from each selected audit firms with a sampling technique purposive. The rationale behind to select five auditors is that to allot equal number of respondents from each representative firm that gives a total of one hundred observations that is convenient for the researcher and the main intent of the study.

### 3.5 Data Analysis

#### 3.5.1 Quantitative Data Analysis

##### Model specification

This section covered multiple regression models used in the study. The multiple regression model used for this study to determine the effectiveness of external audit on tax collection at ERCA LTO. The model is adopted from various researchers.

The researcher used multiple regression model and ordinary least square (OLS) estimation method. The characteristics of the model and proposed variables likely not violate the classical assumption underlying the OLS model. Researchers rationality to use OLS is to find the line of “best fit”, that is, the line that minimizes the total distance between the actual data points and the predicted line (or residuals).

To analyze the data STATA software were used. According to the survey instrument selected

$$TC = \beta_0 + \beta_1 \text{COMP} + \beta_2 \text{AWAR} + \beta_3 \text{INDP} + \beta_4 \text{REGB} + \beta_5 \text{AUFS} + \beta_6 \text{AUFE} + \beta_7 \text{AUTE} + \beta_8 \text{TAAU} + e$$

##### Where:

TC = Tax Collection

$\beta_0$  = Slope Parameter or Constant Term

$\beta_1$  to  $\beta_8$  = The slope which represents the degree with which effectiveness of external auditors on tax collection changes as the independent variable change by one unit variables.

COMP= Competence of External auditors

AWAR= Awareness of External Auditors

INDP= Independence of External Auditors

REG= Absence of Regulatory Body

AFS=Audit Firm Size

AUF=Audit Fee

AUR=Audit Tenure

TAU=Tax Audit

e = error term

### 3.5.2 Qualitative Data Analysis

Qualitative research as stated on the study of (Getaneh, 2011). Qualitative research approach explores attitudes, behaviors and experiences through methods such as in-depth interview and/or focus group discussion (Dawson, 2002). It uses narrative, phenomenological, ethnographies, grounded theory and case studies. The researcher collected open-ended emerging data with the primary intent of developing themes from the data (Creswell, 2007). Qualitative approach attempts to get an in-depth opinion from participants. Apart from this, it facilitates responses, and provides data in-depth with leading respondents (Dawson, et.al., 2002). It is capable to generate a theory by addressing issues which cannot be quantified. It also explores issues which are not studied in the past properly (Creswell, 2007). However, this approach has been given less than a fair sense of appreciation. It has been criticized for lack of scientific rigor, small samples, subjective and nonreplicable efforts. The researcher's interference in the research process is very high that results bias due to small sample size and uniqueness of the research setting. It is also very difficult to make generalization to the whole population.

## **CHAPTER FOUR**

### **DATA ANALYSIS AND INTERPRETATIONS**

#### **4.1 Introduction**

The main purpose of this chapter is to provide the overall results given from both a questionnaire survey and semi-structured interviews. The study analyzes the collected data using various statistical tools and presents the results and discussion accordingly. In the preceding chapters, the review of relevant literature helped this study to understand the problem and design an appropriate research approach to deal with; remainder of this chapter is organized as follows:

The chapter is organized in two sections. The first sub section presents the result which in turn includes descriptive statistics, correlation analysis and the regression results. The second section is dedicated to the interview. Questionnaires were sent to 100 senior and above titled external auditors, who are employed in 20 audit firms. At the end of the collection process, the researcher received 82 respondents from the 100 questioners sent to the senior external auditor, it implies that a response rate of 82.00%. (Remenyi, Williams, Money, & Swartz, 2002) suggesting that a response rate above 60% is considered exemplary. The data collected from the returned questionnaire were entered into STATA and excel Microsoft Office application to summarize. Finally correlation and regression analysis were performed. In this study, a multiple regression analysis was made by using all the discrete variables (dependent and independent) variables available in the dataset.

#### **4.2 Econometric Data Analysis**

This section presents the results of econometric data analysis by the data collected using self-administered questionnaire from sample of 100 senior and above titled external auditors from 20 audit firms in Addis Ababa.

##### **4.2.1. Respondents' Profile**

It is necessary to analyze the demographic profile of the respondents to validate reliability of data collected. Accordingly the respondents were asked to respond to their age

category, level of education, years of experience and the position in the firms. The information processed by STATA is summarized as follows.

The field surveys of the study point out their age. Thirty seven respondents (45.12%) have 20-30 years of age; Twenty five respondents (30.49%) have age 31-40 years; Twenty respondents (24.39%) have age above 40 years. Majority of the respondents, forty five in number (54.88%) are matured enough to exercise their professional skill. Descriptive statistics of the data are presented in table 4.1.

**Table 4.1: Age**

<b>Age</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
20 - 30 Years Old	37	45.12	45.12
31 - 40 Years Old	25	30.49	75.61
Above 40 Years Old	20	24.39	100.00
Total	82	100.00	

Source: STATA Field Survey, 2019

As per the field survey the participants of the study point out their field of study. All 82 respondents (100.00%) have Accounting and Finance educational background; 54 respondents (65.85%) have Bachelors’ of Art degree; 17 respondents (20.74%) are ACCA (Association of Certified Chartered Accountants) certified in addition to BA degree; 4 respondents (4.88%) have Master’s degree alone and the remaining 7 respondents (8.53%) have ACCA in addition to Master’s degree. This shows that the respondent auditors have sufficient knowledge in external audit work. Descriptive statistics of the data are presented in table 4.1. Having professional qualified staff improves the quality of audit report. Professionals for the profession have a great value for the engagements (Cohen & Sayag, 2010)

**Table 4.2: Educational Level**

<b>Educational Level</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
BA	54	65.85	65.85
BA and ACCA	17	20.74	86.59
Master's	4	4.88	91.47
Master's and ACCA	7	8.53	100.00
Total	82	100.00	

Source: STATA Field Survey, 2019

Respondents working experiences in External Audit Firm ranged from less than five years and over twenty years. Thirty six respondents (43.9%) have less than five years experience; Twelve respondents (14.63%) have six to ten years experience ; Twenty six respondents (31.71) have eleven to twenty years work experience and the remaining eight respondents (9.76%) have over twenty years of work experience in the finance sector. This shows that respondents have adequate work experience in auditing activity. The majority of the respondents (56.1%) have more than five years of experience between Five years and above Ten years in public sectors. Descriptive statistics of the data are presented in table 4.3.

The respondents experience revealed that the external audit firms have adequate years of experience in the industry. As a result they can easily engage their duties to produce a fair financial report.

**Table 4.3: Years of Work Experience**

<b>Years of Work Experience</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
Less Than 5 years	36	43.90	43.90
6-10 Years	12	14.63	58.54
11-20 Years	26	31.71	90.24
Over 20 Years	8	9.76	100.00
Total	82	100.00	

Source: STATA Field Survey, 2019

Respondents current working position starts from senior auditor to principal or partner in the auditing firm. Fourteen respondents (17.07%) are Audit Manager; Four respondents (4.88%) are Deputy Audit Manager; seventeen respondents (20.73) are Principal or Partner; forty seven (57.32%) respondents are Senior Auditors. This implies that the respondents have a good understanding to measure the audit quality and benefits of unqualified financial report made by the external auditor. Descriptive statistics of the data are presented in table 4.4

**Table 4.4: Your Current Position**

<b>Current Position</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
Audit Manager	14	17.07	17.07
Deputy Audit	4	4.88	21.95
Principal/Partner	17	20.73	42.68
Senior Auditor	47	57.32	100.00
Total	82	100.00	

Source: STATA Field Survey, 2019

#### **4.2.2. Descriptive Statistics**

The survey result of respondents under table 4.5 from question number one to five which observe the competence of external auditors shows that most respondents agree on all items of question with a mean value of above 3 as per (Best & Kahn, 1977) Likert Scale standard and standard deviations value approaches to 1 which illustrate respondents opinion with regard to competence of external auditors are similar. A mean value of 2.84 for question number 3 indicates external auditors are not proactive to control a situation.

**Table 4.5: Descriptive Statistics for Competence of External Auditors**

Variable	Obs	Mean	Std. Dev.	Min	Max
External auditors have adequate educational background.	82	3.17	1.489	1	5
Do you think the audit department or division has improved in terms of appropriately qualified or professional staff?	82	3	1.387	2	5
External auditors are proactive (creating or controlling a situation rather than just responding).	82	2.84	1.290	1	5
External auditors undertake continuous professional development trainings or attend educational seminars	82	3.09	1.398	1	5
External auditors have adequate educational background.	82	3.41	1.482	1	5

Source: Field Survey, 2019

As demonstrated in table 4.6 the mean value of question numbers 1, 2 and 3 is above three and it discloses that external auditors are aware the benefits and the consequence of unfair presentation of financial reports for tax purposes, almost majority of auditors agreed on the variable. On the other aspect question number 4 and 5 have a mean value below three that indicates the external auditors are not supported whether by the audit firm or the ministry of education to have a good understanding on tax issues, they understood and aware on tax issues by exerting their personal effort alone. The standard deviation for awareness closed to 1, this referred all the responses on awareness are not that much fragmented.

**Table 4.6 : Descriptive Statistics for Awareness or attitudes of External Audit**

Variable	Obs	Mean	Std. Dev.	Min	Max
External audit staffs are aware on the value of tax for the nation development.	82	3.18	1.368	2	5
Awareness about the value of tax makes external auditors to present fair financial statements to the tax authority.	82	3.38	1.504	1	5
The External Audit Firm staffs knows the consequence of not reporting fair financial statements to the tax authority on the tax payers or clients.	82	3.54	1.433	2	5
There are a complied books or magazines or library in the audit	82	2.56	1.055	1	5

firm to improve tax awareness for their staffs.					
The Ministry of education curriculum will add a value to create awareness on tax issues.	82	2.63	1.192	1	5

Source: Field Survey, 2019

Independence of external auditors has a great weight on the engagement of auditing as per table 4.7 result delivered. The mean value of the questions is nearer to 4 and it exhibits that all respondents are agreed on the independence of auditors whether mentally in mind or physically in appearance as it is verified in table 4.7. The standard deviation for Independence closed to 1, this referred all the responses on independence are not that much fragmented.

**Table 4.7: Descriptive Statistics for Independence of External Audit**

Variable	Obs	Mean	Std. Dev.	Min	Max
The value of auditing depends heavily on the independence of auditors in mind and appearance.	82	3.77	1.408	1	5
Auditors exercise their independence as an auditors in their audit Firms during the audit duties.	82	3.39	1.455	2	5
Audit firms support auditors to be independent when undertaking audit duties.	82	3.46	1.459	2	5
Reliable audit report performed by independent auditors is very important for financial statements users.	82	4.27	1.296	2	5
Independence of Auditor is the reason for the existence of auditing profession that provides audit service.	82	3.56	1.508	1	5

Source: Field Survey, 2019

The survey result of respondents under table 4.8 from the five questions which observe the regulatory body support and controlling activity on external auditors and audit firms shows that almost all respondents agree on all items of question with a mean value of above 3 and standard deviations of approaches to 1 which illustrate respondents opinion with regard to regulatory body of external auditors are similar and they believe that the regulatory body whether Ministry of Finance or ERCA or any concerned governmental organization must

consider the significance of external auditors on tax collection process. Mean value of 2.32 for question number 1 (ERCA work co-operatively with the external auditors to facilitate the tax collection process) indicates most of the respondents disagree on the degree of government co-operation with the auditors.

**Table 4.8 : Descriptive Statistics for Regulatory body**

Variable	Obs	Mean	Std. Dev.	Min	Max
ERCA work co-operatively with the external auditors to facilitate the tax collection process.	82	2.32	1.005	1	5
The existence of well capable associations in the field of finance have a value to produce a quality audit.	82	3.12	1.435	1	5
The absence of tax manual prepared by the regulatory body reduces the effectiveness of external auditors.	82	3.44	1.389	1	5
The assignment of capable and experienced staff by a regulatory body facilitates the tax collection process.	82	3.33	1.449	1	5
Acknowledgement by the regulatory body to audit firms has a great contribution to the tax collection process.	82	3.09	1.317	1	5

Source: Field Survey, 2019

As verified by the respondents stated on table 4.9 the mean value of all the five questions numbers is below three and it revealed that external auditors are disagree on the value of audit firm size or they are indifference or reluctant to facilitate the tax collection process, it implies that it has no significant impact or no observation on the effectiveness of tax collection. The standard deviation for awareness closed to 1, this tells us all the responses on audit firm size are not much deviated from the mean.

**Table 4.9: Descriptive Statistics for Audit Firm Size**

<b>Variable</b>	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
Audit firm size is a strong reason to increase tax collection	82	2.55	1.188	1	5
Large audit firms maintain their independence without any interference because of their financial strength.	82	2.41	1.077	1	5
Large auditing firms are less willing to acquiesce to client pressure to provide substandard reporting.	82	2.39	.8714	1	5
Large audit firm are associated with high accurate accounting estimates than were smaller accounting firms.	82	2.41	1.143	1	5
Large auditing firms are more likely to detect and report material problems.	82	2.57	1.197	1	5

Source: Field Survey, 2019

Table 4.10 questions are related to audit fee, the responses from the external auditors have a mean value approaches to 3 and it implies that their reaction on audit fee is neutral. The impact of audit fee on the effectiveness of external auditors on tax collection has no clear result or the respondents are impartial. The standard deviation for Independence closed to 1, this referred all the responses on audit fee are fairly distributed.

**Table 4.10 : Descriptive Statistics for Audit Fee**

<b>Variable</b>	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
large audit fee paid by the client doesn't make the auditor more economically dependent on the client.	82	2.49	1.033	1	5
Do you think less audit fee reduce the scope of audit effort to detect fraud?	82	2.65	1.391	1	5
Competition between audit firms on audit fee will affect audit quality	82	2.88	1.461	1	5
The amount of audit fee received doesn't affect the audit quality as far as the external auditor keep the professional ethics.	82	2.99	1.444	1	5

Source: Field Survey, 2019

All the responses related to the questions about audit tenure are approached to 2, it implies that most of the respondents are not agree on the impact of audit tenure for the tax collection. The responses are summarized on table 4.11. The standard deviation for Independence closed to 1, this referred all the responses on audit tenure are not that much fragmented.

**Table 4.11: Descriptive Statistics for Audit Tenure**

Variable	Obs	Mean	Std. Dev.	Min	Max
The risk of an audit failure is likely to increase as the audit tenure period increases due to client management becoming too familiar with the auditor's approach and procedures	82	2.40	.914	1	5
Audit firms receive more litigation in the beginning of their audit than their later years.	82	2.41	.769	1	5
The likelihood of receiving a Substandard quality audit increases with the length of the auditor client relationship.	82	2.46	.971	1	5
The risk of an audit failure is higher in the early years of an audit tenure period.	82	2.48	.906	1	5

Source: Field Survey, 2019

Tax audit made by ERCA auditors has a value for the tax collection process, the respondents reaction is illustrated on table 4.12. The mean value of the questions approaches to three. The standard deviation for tax audit closed to 1, this referred all the responses on awareness are not that much fragmented.

**Table 4.12 : Descriptive Statistics for Tax Audit**

Variable	Obs	Mean	Std. Dev.	Min	Max
The frequent tax audit carried by the tax auditor without delay will improve the tax collection process.	82	3.01	1.419	1	5
The external auditor assumed future tax audit investigation has an impact on the work of his/her current clients financial report not to exposed the client for unnecessary fines (interest and penalty)	82	2.56	.969	1	5
Tax audit undertaking by the ERCA has an advantage for	82	2.60	1.120	1	5

the external auditor to share the new issued tax laws and regulations.					
Even if the financial statements are audited by the external audit firms, clients believed that their interaction with the authority staff makes easier their obligation to pay actual tax.	82	2.57	.969	1	5

Source: Field Survey, 2019

### 4.2.3. Reliability Analysis

Any research based on measurement must be concerned with the accuracy or dependability or, as usually call it, reliability of measurement. A reliability coefficient demonstrates whether the test designer was correct in expecting a certain collection of items to yield interpretable statements about individual differences. Lee Cronbach's, famous study of coefficient alpha demonstrate a method to test the reliability and validity of data collected through questionnaire by using Cronbach's alpha coefficient (Cronbach's, 1951). If the Cronbach's alpha coefficient ( $\alpha$ ) result is greater than 0.7 and less than 0.8 the internal consistency is acceptable .The value of the Cronbach's alpha for the data collected for all variables is 0.7154 as per table 4.13 the reliability analysis value, this indicates that the responses from the respondents are reliable or consistent to make a data analysis to measure the tax collection.

**Table 4.13: Reliability Statistics for Cronbach's Alpha**

<b>Cronbach's Alpha</b>	<b>Cronbach's Alpha Based on Standardized Items</b>	<b>No of Items</b>
0.7068	0.7154	9

Source: Field Survey, 2019

In literature, the average inter-item correlations in the range of 0.15 to 0.50 are considered as an indicator for an acceptable level of consistency. Looking at inter-item correlations for reliability is just one part of many for looking at the validity of a scale.

Typically, items below 0.15 have poor inter-item correlations, suggesting they're really not that well related to each other and might not be suitable for measuring a single construct. However, items that are above 0.50 tend to be very similar to each other, almost to the point that they're redundant, Clark & Watson, (1995). As per the table 4.14: Inter-Item Correlation Matrix illustrated below indicates most of the variables (73.33%) in the range of 0.15 to 0.50, it reflects that the correlation in between the variables is most favorable.

**Table 4.14: Inter-Item Correlation Matrix**

	Competence of External Audit	Awareness or attitudes of External Audit	Independence of Internal Audit	Regulatory body	Audit Firm Size	Audit Fee	Audit Tenure	Tax Audit	Tax collection
Competence of External Audit	1.0000								
Awareness or attitudes of External Audit	0.4954	1.0000							
Independence of External Audit	0.3492	0.1693	1.0000						
Regulatory body	0.3339	0.2215	0.3817	1.0000					
Audit Firm Size	0.0496	0.1129	-0.1528	0.2148	1.0000				
Audit Fee	0.0621	0.1275	0.0710	0.2745	0.2795	1.0000			
Audit Tenure	0.0899	0.1145	0.1363	0.2463	0.2055	0.3230	1.0000		
Tax Audit	0.0216	0.1707	0.1099	0.1725	0.1735	0.4260	0.5138	1.0000	
Tax collection	0.1619	0.0420	0.4297	0.3358	0.1457	0.2733	0.3450	0.4332	1.0000

#### 4.2.4. Assessment of Ordinary Least Square Assumptions

##### 4.2.4.1. Assessment of Normality

Statistical errors are common in scientific literature, and about 50% of the published articles have at least one error. Many of the statistical procedures including correlation, regression, t tests, and analysis of variance, namely parametric tests, are based on the assumption that the data follows a normal distribution or a Gaussian distribution (after Johann Karl Gauss, 1777–1855); that is, it is assumed that the populations from which the samples are taken are normally distributed . The assumption of normality is especially critical when

constructing reference intervals for variables. Normality and other assumptions should be taken seriously, for when these assumptions do not hold, it is impossible to draw accurate and reliable conclusions about reality (Asghar & Saleh, 2012).

As per the book (Brooks C. , 2008) stated as normality assumption is required in order to conduct single or joint hypothesis test about the model parameters The most commonly applied test for normality is the Bera-Jaque (BJ) test. The BJ uses the property of normally distributed random variable that the entire distribution is characterized by the first two moments, those are mean and variance. The Skewness and Kurtosis tests with a normal distribution value must be within the range of +3 and -3. The result on table 4.15 shows the skewness and kurtosis are in between +3 and -3, it implies that the data set is well modeled by a normal distribution.

**Table 4.15: Assessment of Normality**

	<b>N</b>	<b>Skewness</b>	<b>Kurtosis</b>
Competence of External Audit	82	0.550	2.354
Awareness or attitudes of External Audit	82	0.406	2.245
Independence of External Audit	82	-0.682	1.655
Regulatory body	82	0.535	2.224
Audit Firm Size	82	0.853	4.043
Audit Fee	82	0.716	2.817
Audit Tenure	82	1.982	8.488
Tax Audit	82	0.844	2.841
Tax collection	82	0.558	1.841

**4.2.4.2. Assessment of Multicollinearity**

Multicollinearity occurs when independent variables in a regression model are correlated. This correlation is a problem because independent variables should be independent. If the degree of correlation between variables is high enough, it can cause problems when you fit the model and interpret the results (Jim, 2019). Multicollinearity test help to identify the correlation between explanatory variables and to avoid double effect of independent variable from the model.

As stated on table 4.17 Pearson correlation matrix, many of correlations that have occurred among independent variables are weak correlations which show non-existence of Multicollinearity. Even though some high correlation existed between some variables, researcher ignored those near Multi collinearity problems but, not without scholar's reason (Belay, 2015). As cited by (Belay 2015) in his research work Cooperand Schindler (2009) and Hailer et al. (2006) recommended that Multicollinearity problem would be corrected when correlation level to be above 80% and 90% respectively. As indicated on the correlation matrix, for instance Competence has positive correlation with awareness or attitudes of external auditors (0.4954), independence of auditors (0.3492), regulatory body (0.3339), audit firm size (0.0496), audit fee (0.0621), audit tenure (0.0899), tax audit (0.0216) and with tax collection (0.1619). In comparison competence is relatively more correlated with awareness, independence and regulatory body but the degree of multicollinearity has no influence with other explanatory variables, to the reverse weakly correlated with audit firm size, audit fee, audit tenure and tax audit.

**Table 4.16: Assessment of Multicollinearity**

<b>Variable</b>	<b>VIF</b>	<b>Tolerance (1/VIF)</b>
Tax Audit	1.56	0.642
Competence of External Audit	1.54	0.649
Audit Tenure	1.44	0.695
Regulatory body	1.42	0.705
Awareness or attitudes of External Audit	1.38	0.724
Independence of External Audit	1.36	0.734
Audit Fee	1.35	0.749
Audit Firm Size	1.22	0.823
Mean VIF	1.41	

**Table 4.17: Pearson Correlation Matrix**

	Competence of External Audit	Awareness or attitudes of External Audit	Independence of External Audit	Regulatory body	Audit Firm Size	Audit Fee	Audit Tenure	Tax Audit	Tax collection
Competence of External Audit	1.0000 82								
Awareness or attitudes of External Audit	0.4954* 82	1.0000 82							
Independence of External Audit	0.3492* 82	0.1693 82	1.0000 82						
Regulatory body	0.3339* 82	0.2215 82	0.3817* 82	1.0000 82					
Audit Firm Size	0.0496 82	0.1129 82	-0.1528 82	0.2148 82	1.0000 82				
Audit Fee	0.0621 82	0.1275 82	0.0710 82	0.2745* 82	0.2795* 82	1.0000 82			
Audit Tenure	0.0899 82	0.1145 82	0.1363 82	0.2463 82	0.2055 82	0.3230* 82	1.0000 82		
Tax Audit	0.0216 82	0.1707 82	0.1099 82	0.1725 82	0.1735 82	0.4260* 82	0.5138* 82	1.0000 82	
Tax collection	0.1619 82	0.0420 82	0.4297* 82	0.3358* 82	0.1457 82	0.2733* 82	0.3450* 82	0.4332* 82	1.0000 82

**4.2.4.4. Assessment of Autocorrelation**

Auto correlation is a characteristic of data which shows the degree of similarity between the values of the same variables over successive time intervals. This assumption of OLS as stated by (Brooks, 2008)  $cov(U_i, U_j) = 0$ , this is another assumption that made of the CLRMs disturbance terms is that the covariance between the error terms over time should be zero. That means the errors are uncorrelated with one another. If errors are not uncorrelated with one another, it would be stated that they are auto correlated or serially correlated (Belay, 2015). The most common test of this assumption is using the Durbin-Watson test. It assumes that the relationship between an error and the previous of an error. In this type of test, the null hypothesis can't be rejected when DW result is close to 2. Table 4.18 the Durbin-Watson

(DW) statistics value of this study is 1.478 and close to 2. Therefore, there is no evidence of autocorrelation among error terms in this study.

**Table 4.18: Durbin Watson Test Model Summary**

<b>Model</b>	<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Durbin-Watson</b>
1	-.951a	0.3880	0.3210	1.478

Source: Field Survey, 2019

#### **4.2.5. Regression Results for External Auditor Effectiveness**

The sign of a regression coefficient tells us whether there is a positive or negative correlation between each independent variable with the dependent variable. A positive coefficient indicates that as the value of the independent variable increases, the mean of the dependent variable also tends to increase. A negative coefficient suggests that as the independent variable increases, the dependent variable tends to decrease. The coefficient value signifies how much the mean of the dependent variable changes given a one-unit shift in the independent variable while holding other variables in the model constant (Jim, 2019). This property of holding the other variables constant is crucial because it allows us to assess the effect of each variable in isolation from the others. The coefficients in my statistical output are estimates of the actual population parameters. To obtain unbiased coefficient estimates that have the minimum variance, and to be able to trust the p-values.

After the researcher have fit a linear model using regression analysis I need to determine how well the model fits the data. There are a variety of goodness-of-fit statistics, R-squared ( $R^2$ ) is common in practice (Reisinger H. , 1997). R-squared does not indicate whether a regression model is adequate. You can have a low R-squared value for a good model, or a high R-squared value for a model that does not fit the data. Thus, the best value for R-square depends on what the researcher measured. The value of  $R^2$  as per the table 4.18 is 39%, i.e, the contribution of the independent variables for the effectiveness external auditors is 38%.

**Table 4.19: Regression Results for EEA on tax collection****ANOVA**

<b>Model</b>	<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
Regression	45.201	8	5.650	5.79	000b
Residual	71.286	73	.976		
Total	116.488	81			

Based on Table 4.19, the ANOVA shows the significance of the model by the value of F- statistics ( $P=.000$ ) and  $F= 5.79$  which indicates there were a strong relationship between the predictors and the outcomes of the regression variables. It is at the best fit of the model to predict the effectiveness EA on tax collection.

**Table 4.20: Regression Results Coefficients**

<b>Tax collection</b>	<b>Coef.</b>	<b>Std. Err.</b>	<b>t</b>	<b>P&gt;t</b>	<b>Beta</b>
Competence of External Audit	.063	.136	0.46	0.646	.052
Awareness or attitudes of External Audit	-.215	.154	-1.40	0.167	-.150
Independence of External Audit	.427	.125	3.42	0.001	.365
Regulatory body	.135	.144	0.93	0.354	.102
Audit Firm Size	.183	.168	1.09	0.280	.109
Audit Fee	.065	.167	0.39	0.699	.041
Audit Tenure	.172	.231	0.74	0.460	.081
Tax Audit	.569	.202	2.81	0.006	.321
_cons	-.951	.759	-1.25	0.214	

### 4.3. Data Results and Interpretation

Data interpretation refers to the implementation of processes through which data is reviewed for the purpose of arriving at an informed conclusion. The interpretation of data assigns a meaning to the information analyzed and determines its signification and implications (Mona, 2018).

The importance of data interpretation is evident and this is why it needs to be done properly. Data is very likely to arrive from multiple sources and has a tendency to enter the analysis process with haphazard ordering. Data analysis tends to be extremely subjective. That is to say, the nature and goal of interpretation will vary from business to business, likely correlating to the type of data being analyzed. While there are several different types of processes that are implemented based on individual data nature, the two broadest and most common categories are “qualitative analysis” and “quantitative analysis”.

Qualitative data analysis can be summed up in one word – categorical. With qualitative analysis, data is not described through numerical values or patterns, but through the use of descriptive context (i.e., text). Typically, narrative data is gathered by employing a wide variety of person-to-person techniques. These techniques include: observation, documents and interviews.

Quantitative data interpretation could be summed up in one word (and it really can't) that word would be “numerical.” There are few certainties when it comes to data analysis, but one can be sure that if the research engaging in has no numbers involved, it is not quantitative research. Quantitative analysis refers to a set of processes by which numerical data is analyzed. More often than not, it involves the use of statistical modeling such as standard deviation, mean, median and regression analysis (Mona, 2018).

In this study, the hypotheses testing used to test a significant influence of the explanatory variables on the effectiveness of external audit on tax collection process by using the beta coefficient, t value and p values. To support research findings within this study the researcher used data triangulation for the qualitative data which refers to the use of independent sources of data techniques.

### **4.3.1. Competence of External Auditors**

To be an auditor is expected by many people to get the trust as the parties that are able to conduct an audit of the financial report and responsible for the opinion given. Professionalism becomes the main requirements for an auditor. As (Mansouri, et.al, 2009) stated Professionals are characterized by their unique expertise gained through education and training, a commitment to lifelong learning, service to society, a code of ethics, an agreement to abide by their professions code, and participation in the self-governance and monitoring of the profession.

The analysis showed competence of external auditors as per the table 4.20 shown has a beta value 0.063 for the tax collection, it implies that they are positively correlated with the effectiveness of external auditors at a statistical significance level 0.64 value and from the respondents reply the mean value of competence is more than 3 as a result the external auditors specialization in the industry is a corner stone for the audit quality as the respondents answered, this influences the tax collection process by providing unqualified audit report during the tax reporting time.

An interview was conducted with ERCA LTO team leaders of the tax audit department, according to the interviewee response on the question raised related to competence of auditors, they are agreed on the professional skills of external auditors and they observed a quality difference from the financial statement reports of the tax payers. One interviewee from the team leaders said “when undertaking an audit for one tax payer company, inventory was recorded by using a FIFO costing method and asked the auditor how he prefers this method and he replied me “this is one option provided to compute cost of inventory as per GAAP” but he has no knowhow about inventory recording in our country as per the tax regulation. Finally we calculated the inventory cost by using weighted average costing method as per the regulation announced and his client was penalized and paid interest for the tax difference amount.” By observing such and other related differences and taking in to consideration the tax audit has been done by a sampling technique it is difficult to cover the whole document and period of limitation (yirga) after five years of tax period blocked to be audited, as a result it is assumed that the government losses a tax amount left because of the errors made by the external auditors incompetence.

External auditors' competence is also found to have a positive relationship with tax collection in other studies as well, (Mansouri, et.al, 2009), (Bethitina, 2015), (Halim, et.al, 2014), (Bayou, 2017). The above results are in line with the research hypothesis,

**H1:** "There is a positive relationship between Competence and effectiveness of EA on tax collection."

#### **4.3.2 Awareness or attitudes of External Auditors**

Auditor-provided tax services improve internal control quality by accelerating audit firm awareness of transactions material to the financial statements (Simon, Ege, & Bridget, 2015). Tax awareness by external auditors as per the respondents from table 4.6 of descriptive statistics has a mean value above three for the questions related to the awareness of tax by the external auditors; the result approaches to four and it indicates that the external auditors have awareness on the issue but questions raised about the initiation to the side of the audit firm and ministry of education are reluctant or weak as per the mean value, which is below three.

The regression analysis on table 4.20 the value of beta coefficient -0.215 this contradicts the hypothesis; it tells that they are inversely related.

**H2:** There is a positive relationship between awareness or attitudes of EA on tax collection. On the other parameters value of P is 0.167, this results insignificant relation with the dependent variable and the value of t equals -1.4, which is by far from 2, it indicates that there is weak relation with the tax collection.

Even if the regression analysis opposes the hypothesis the qualitative data obtained from interview support the hypothesis. One of the interviewee who is represented by no. 4 said "most of the time financial statements prepared by external auditors focused to obtain acceptance by the shareholders, this is supported also by the managers. But to keep the consistency of the business the external auditor has a great responsibility to worried about tax related issues within the financial reports. As we see from our tax audit report there are companies which can't carried the burden of tax liability, interest and penalties occurred from the difference of the external audit report and tax audit report. This led the company to be shut down." From the view of the tax audit team leader, it is possible to conclude that the external auditor should be aware on tax issues, related laws and tax administration regulations, if so happen he/she keep his/her client from un necessary obligations and contribute significant value to the tax growth activity.

The hypothesis was supported by other research work like (Simon, et.al, 2015)

### **4.3.3 Independence of External Auditors**

The auditor should be independent from the client company, so that the audit opinion will not be influenced by any relationship between them. The auditors are expected to give an unbiased and honest professional opinion on the financial statements to the shareholders. Accordingly the report is used for the tax reporting purpose and any stakeholders interest.

Doubts are sometimes expressed regarding the independence of external auditors. It can be argued that unless suitable corporate governance measures are in place, a firm of auditors may reach audit opinions and judgments that are heavily influenced by the wish to maintain good relations with the client company. If this happens, the auditors can no longer be said to be independent and the shareholders cannot rely on their opinion.

Accounting firms sometimes engage set audit fees at less than the market rate and make up for the deficit by providing non-audit services, such as management consultancy and tax advice. As a result, some audit firms have commercial interests to protect too. This raises concerns that the auditor's interests to protect shareholders of a company and his commercial interests may conflict with each other. A high profile example would be the relationship between Enron and their auditors, Arthur Andersen.

The analysis based on the respondents of the questionnaire in likert scale showed independence of external auditors as per the table 4.20 shown has a beta value 0.427 for the tax collection, it implies that they are positively correlated with the effectiveness of external auditors at a statistical significance level 0.001 for ( $P < 0.05$ ), implies independence of external auditors significantly affect the tax collection process, in similar measurement the value of  $t$  equals 3.42. A  $t$ -value of less than 2 is indicating a weak relationship between the independent and dependent variables (Hair, et.al, 1998). As per the result from table 4.19 regression table a  $t$ -value 3.42 is more than 2 independence of external auditors has strong relationship with tax collection. To strengthen the relation of the explanatory variable it is better to refer the mean value of the respondents of the questionnaire, it is above three for the four questions and for the question "reliable audit report performed by independent auditors is very important for financial statement users" has a mean value 4.27 it explain the respondents are strongly agree for the reliability or independence of external audit report without hesitation.

External auditors' independence is also found to have a positive relationship with audit

quality and other dependent variable results in other studies as well, (Bedard & Paquette, 2010), (Halim,et.al, 2014), (James & Izien, 2014), (Abdi, 2017), (Adane, 2014).

The above results are in line with the research hypothesis,

**H3:** “There is a positive relationship between Independence and effectiveness of EA on tax collection.”

#### **4.3.4 Presence of regulatory body.**

A regulatory body is a public organization or government agency that is set up to exercise a regulatory function. This involves imposing requirements, conditions or restrictions, setting the standard for activities, and enforcing in these areas or obtaining compliance. Regulatory bodies cover a wide variety of professions, but not all professions are regulated and may be self-regulated. A regulatory body might also be referred to as a regulatory agency, a regulatory authority or a regulator (Cuthbert & Young).

In the descriptive analysis under table 4.8 of the questionnaire the value of the mean for the question except number one all have a mean value greater than 3, it implies that most of the respondents agree on the presence of well organized and structured regulatory body. The regulatory body is expected to have competent and capable staff to support the external auditors’ professional growth, to acknowledge their profession has a driving force for the tax collection process because most of the large tax payers tax report asserted by the external auditors, as the researcher explained before almost 70% of the total domestic tax collected from these large tax payers, as a result the external auditors have the chance to advice to keep the government tax regulations and proclamation.

At the recent time AABE has the power to administer, to measure to qualify and to give permission to work in the financial activity industry. However AABE has its own limitation to carry out its responsibilities since its duration from the commencement is short. Prior to AABE the regulatory bodies whether Ministry of Finance and Economic Commission or ERCA has little significance impact to work co-operatively with accounting and auditing professionals associations or weak relation with finance professionals individually.

The mean value of question number 1 under table 4.8 for the question “ ERCA work co-operatively with the external auditors to facilitate the tax collection process.” Is 2.32, it is below three and closed to neutral response from the respondents.

The regression analysis from table 4.20 revealed that the beta coefficient has a value

0.135, it indicates the regulatory body has directly relationship with tax collection, this is similar with the hypothesis the researcher pointed out,

**H4:** There is a positive relationship between the presence of regulatory body and effectiveness of EA on tax collection. The presence of regulatory body is also found to have a positive relationship in other studies as well (Abdi, 2017), (Dessalegn, 2009), (Engida, 2016), (Kassahun, 2010).

The p value for the independent variable is 0.354 reflects there is a less significance relation with the tax collection in similar manner the t value 0.93 is the result of weak relation with the dependent variable. To the contrary the responses obtained from the ERCA LTO tax audit department through interview strengthen the significance of the variable. Interviewee number 9 explains his opinion on the issue said “there is no mediatory to close the gap in between the external auditors and the regulatory body employees particularly with the tax audit department. The training department in ERCA is not established as per the current advancement requires and also the staff arrangement has not been assigned based on competence and experience, that is why when training was given for the tax payers and their employees a trainer was being selected from the audit department rather from the training department.” The researcher also observed the plan and budget department at LTO is not properly established based on staff and office layouts that is why it was difficult to collect data and know the concerned department or staff. To generalize the interviewees’ remark, the tax collection process facilitated when the regulatory body works hand-in hand with the finance professionals and it is better to consider as one element for the tax growth.

#### **4.3.5 Audit firm size of the External Auditors**

Satisfactory levels of audit quality are usually more evident in large audit firms than in small ones, one reason being that the larger the firm, the higher the number of clients, and the greater the probability that the range of services provided is bigger. This minimizes dependency on particular clients (Sawan & Alsaqqa, 2013).

The descriptive analysis from table 4.9 confirms that the mean value is below three, this reflects the respondents for the whole question are indifference or neutral for the significance of audit firm size to the effectiveness of external auditors for tax collection. On the regression analysis the beta coefficient positive value 0.183 confirms the hypothesis that:

**H5:** There is a positive relationship between audit firm size and effectiveness of EA on tax

collection. And the p-value 0.28 lies on the insignificance of this variable to the tax collection process. Additionally the value of t 1.09 is below 2 indicates there is weak relation with the variable of the dependent. These regression results are not in contrary with the questionnaire respondents. However the result from the interview addressed that audit firms engaged in Ethiopia like HST and one of the big four audit firms in the world Deloitte audit reports have a good quality in comparison with other small firms reports. As the researcher visited at the time of questionnaire distribution HST has better firm size than most of the audit firms found in the country.

The hypothesis was supported by other researchers like (DeAngelo, 1981), (Lawrence, et.al, 2011), (Bayou, 2017). In contrary researchers like (Bethitina, 2015) doesn't support the hypothesis or the view is inversely.

#### **4.3.6 Audit fee paid to the Auditor**

Tax avoidance reduces the transparency of enterprises and weakens the quality of accounting information. As a result, auditors will face more audit risk and have to make more efforts. Certified public accountants would correspondingly raise the pricing of audit services. We wonder that whether tax avoidance will arise higher audit fees. In addition, the property rights of different enterprises may have an impact on the relationship between tax avoidance and audit fees (Hu, 2018). To check the audit fee price has effect on audit quality and tax avoidance a descriptive and regression analysis was done by the researcher.

As per the descriptive analysis found on table 4.10 for the questions raised the respondents answered and have a mean value below three, it implies that all the respondents for the whole question are impartial. So it is difficult to say audit fee has a significance effect on tax collection process as per the regression analysis t value 0.699 hence it is below 2 and also the value of t 0.39 results there is weak relation between audit fee amount paid by the clients and effectiveness of external auditors on tax collection. Even if the relation is insignificant and weak the value of beta coefficient 0.65 revealed that they have direct relationship. This supports the hypothesis made by the researcher previously;

**H6:** There is a positive relationship between audit fee and effectiveness of EA on tax collection. The hypothesis is in line with the findings of other researchers (Solomon, 2016), (Tamirat, 2014), (Toto & Stephanus, 2015).

### **4.3.7 Audit tenure with the client**

Auditors play a major role in accounting operations, so income tax can be influenced by auditors' thinking. The current research deals with the impact of audit or tenure on tax avoidance. Since tax activities have required more proficiency than accounting is expected the long term auditors' tenure to increase the information value related to tax. Therefore, longer the relation between an auditor and its customers, higher the auditors abilities and tendencies to cooperate in tax strategies of his customers and create more intimacy with managers of his customers would be. Regarding to the investigations of many researchers about tax avoidance, they reported that "tax avoidance means decrease in clear tax through legal and illegal tax planning (Serafat & Barzegar, 2015).

The result shown on table 4.11 of the descriptive statics the mean value of the respondents is below three and approaches to 2, that tells us the respondents are disagree with impact of audit tenure to increase effectiveness of external auditors for tax collection. As per the regression analysis value of p 0.46 audit tenure has no significance effect and also weak relation by the t value of 0.74 with the dependent variable. When we see the beta coefficient of the dependent variable 0.172, it is directly related and similar with the hypothesis

**H7:** There is a positive relationship between audit firm tenure and effectiveness of EA on tax collection. And the hypothesis was supported by other researchers like (Ghosh & Moon, 2005), (Bamber & Iyer, 2007), (Shume, 2016).

### **4.3.8 Tax audit by the tax collector office**

To collect taxes properly from the tax payers a well implemented tax compliance strategy that can safeguard tax administration, sustain the confidence of taxpayers and tax audit programmes need to be embraced in order to monitor and detect the non-compliance traits of taxpayers.

This research finding on tax audit from the regression analysis on table 4.20 value of p 0.006 disclosed that there is significant relation with the effectiveness of external auditors on tax collection for (p<0.05) more over the value of t 2.81 addressed strong relation with the independent variable for t>2. The descriptive analysis from table 4.12 results shown the value of the means for most questions raised to the respondents has a value below 3 and it approaches

to three indicates the fillers are neutral on the dependent variable. The beta coefficient positive value 0.569 refers tax audit has directly related with the effectiveness of external auditors for tax collection, this strengthen the hypothesis set by the researcher;

**H8:** There is a positive relationship between tax audit and effectiveness of EA on tax collection. The test supported by other researchers finding Dubin (2004), Hyun (2005), Akalu (2016) and Jeff & Jhon (2018).

## **CHAPTER FIVE**

### **CONCLUSIONS AND RECOMMENDATIONS**

This chapter of the paper discusses on topics about the conclusion driven from the analysis of the study and possible recommendations are made.

#### **5.1 Conclusions**

External auditors provide important and valuable insight into the information that exists within an organization. Their findings and audit processes give businesses the confidence and reassurance that their information and the way they conduct business is suitably kosher. Their opinion on the financial statements acts as agency for the shareholders, in addition it should to clean in advance unnecessary future tax liabilities by reconciling the financial statements of the client with the tax laws and regulations.

The fundamental reason of this study was the effectiveness of external auditors on tax collection process and growth. The major findings concluded, the variables result from the regression analysis has positive effect on the effectiveness of external auditors.

Competence of external auditors has a valuable importance for external auditors. The competence thinking must be observed not only from the professional knowledge alone but also the external auditors consciousness on the nation's tax laws, experience and the exposure on tax issues to keep the client business. The developed countries GDP component composed of almost 40% from tax; it is difficult to compare with our nation. Every citizen confident by paying his/her tax liability for the government in the developed world. Without tax the existence of a nation is questionable

Awareness of external auditors plays a vital role to enhance tax compliance. The external auditors' independency not only in fact or mind additionally in appearance has a great value as per the respondents result. Integrity and objectivity confidence must be set in the mind of the tax collectors that the auditors are not influenced by their client.

Quality review of external audit reports by the regulatory body is not maintained. To control and direct the industry the governing office has no structured and well organized plat

form or road map. Without a strong co-operation with external auditors it is difficult to seek the mission in the tax collection process.

Some external audit effectiveness on tax collection variables such as audit fee, audit firm size and audit tenure with the client are subject to great debate about their effectiveness for external auditors on tax collection process. However, the response of the interviewee to triangulate with external auditors answer, large audit firms provide high quality services by arranging training programmes, standardize audit methodology and opportunity for peer review by another partner. Understanding of the business client and the industry is obtained after continuously repeated audits, thus improving audit quality.

The existing literature offers no better measures and they are used extensively in auditing other topic research. The other variables analyzed on the study have significant effect and strong relation with the audit quality as a vital input for the tax collection process. Despite its potential limitations, this research signifies to the existing literature on the effectiveness of external auditors on tax collection in general. The study reveals findings that will enable the government to consider the great value and to work co-operatively with external auditors to improve the tax collection.

## **5.2 Recommendations**

The researchers suggest a number of recommendations that could contribute to improving effectiveness of external audit on tax collection in ERCA large tax payers office. The purpose of this research work is to identify elements which have importance and aggravate the tax collection process by exceeding the quality of the external auditors.

- To improve the competence of staff in audit firms the governing body should lay a bench mark for a minimum requirement to the staff recruitment by the audit firms at least an experience and educational qualification to increase the effectiveness of external auditors on tax collection process.
- Measurement criteria must be set by the government to improve the tax collection process and growth by preparing a tax manual and makes to sit the external auditors for exam within a specified period of time to update their information on tax cases.

- Because of the limited number of audit firms in Ethiopia, AABE must set other alternatives to certify audit firms. The current situation to be certified for the audit firm the auditor must be an ACCA member, this limit the number of audit firms in the country. So in order to create a competitive industry to provide a quality audit service the number of audit firms must be increased.
- There must be an institution in the country like ACCA in UK, CPA in U.S.A, which certifies accountants based on their competence, accounting norms in the country, and other related criteria. However, even if AABE is a pioneer there must be a great attention by the governing officials to advance AABE by considering its vital importance. In addition professional associations must empower their capacity to growth the profession.
- AABE and ERCA must work cooperatively by establishing one body to follow tax payers financial statements report whether they are presented as per tax law, GAAP or IFRS as soon as the tax payers delivered the report to the tax office. Tax audit by ERCA auditors usually made years after the reporting time before five years of report to keep period of limitation (yirg) time or by the request of the tax payers for liquidation or to block delayed interest and penalty payments. This way of controlling doesn't give mutual benefit to the tax payer and the tax office.
- Post Tax audit by the ERCA must be done as soon as the tax payer paid his liability or within a short period after the reporting time. It inform the external auditors the reasons why the difference occurred in the tax audit to correct future works based on the rules and regulations stated by the authority and the concerned offices. In addition it decreases the amount of penalty and interest burden resulted by the poor administration of ERCA.

## References

- Abate, G. (2009, June 15). www.nazret.com. Retrieved 04 08, 2019, from nazret.com.
- Abdi, T. (2017, June). Assessment of the Role of Audit Firms in Reducing Fraud. Addis Ababa, Ethiopia.
- Achyarsyah, P., & Molina. (2014). Audit Firm tenure, audit Firm size and Audit Quality. Global Journal of Business and Social Science Review , Review 2 (4)69-76.
- Adane, W. (2014, May). Auditor responsibility and fraud detection: In Ethiopian private audit firms.
- Agresti, A., & Finlay, B. (2008). Statistical Options for The Social Science (4 ed.). Upper Saddle River, NJ: Prentice Hall.
- Akalu, K. (2016). Determinants of tax compliance behavior of large corporate tax payers in Ethiopia. Addis Ababa.
- Alarbeed, E., Alothman, M., & Assee, A. (2014). The Role of Governance Rules in Improving The Auditor's Ability to detect Fraud in The financial Statements:Field Study on Companies Listed In The Syrian Securities Commission. Tishreen University Journal for Research and Scientific Studies-Economic and Legal Sciences Series , 36 (5), 453-475.
- Al-Bawab, A. (2012). The Factors Which Affecton The Choice of External Auditor in Jordanian banks From The Perspective of The External Auditor In Jordan(An Emperical Study). International Journal of Humanities and Social Science , 2 (6), 180-192.
- Alm, J. (1992). Estimating The determinants of Tax Payer Compliance with Experimental Data. National Tax Journal .
- Anwar, M. (2014). Determinants of Tax Revenue Performances in Ethiopia:Case of Ethiopian revenues and Customs Authority.
- Arens, A. A., Elder, R. J., & Beasley, M. s. (2012). Auditng and Assurance Services: an Intergrated Approach. 14th ed. New Jersey: Pearson Prentice Hall.
- Arens, A.A., & Leobbecke, J. (2000). Auditing: An integrated approach. 8th ed. Englewood Cliffs, nj: Prentice Hall.
- Asa, J., Christopher, H., Jens, A., Bert, B., & Laura, V. (2008). Tax and Economic Growth. OECD ( Organization for Economic Co-Operation and Development).
- Asghar, G., & Saleh, Z. (2012). Normality Tests for Statistical Analysis: A Guide for Non-Statisticians. International Journal of Endocrinology & Metabolism , 10 (2), 486-489.

- Ashbaugh, H., LaFond, R., & Mayhew, B. (2003). Do Non-Audit Services Compromise Auditor Independence. *The Accounting Review* 78(3) , 611-639.
- Asthaana, S., & Boone, J. (2012). Abnormal Audit Fee and Audit Quality, *Auditing. A Journal Practice and Theory* , 31 (3), 1-22.
- Bamber, M. E., & Iyer, V. M. (2007). Auditors' Identification With Their Clients and Its Effect on Auditors' Objectivity, *Auditing. A journal of Practice and Theory* , 26 (2), 1-24.
- Barkess, L., R., S., & P., U. (1995). The Effect of Client Fee Dependence on Audit Independence. New South Wales, Wales: University of New South Wales.
- Bayou, T. F. (2017, February). Auditors Perception of Audit Quality in Ethiopia.
- Beale, L. M. (2004). Putting SEC Heat on Audit firms and Corporate Tax Shelters: Responding to Tax Risk with sunshine Shame and Strict Liability. *Corporation Law*, Vol. 29 .
- Bedard, J., & Paquette, S. (2010). Perception of Auditor Independence, Audit Committee Characteristics, and Auditor Provision of Tax Service. Quebec: University Laval Quebec City.
- Belay, Z. (2015). Determinants of Tax revenue Performance: In Case of Ethiopia federal Government.
- Bender, D. R. (2006). What is an effective audit and how can you tell? CBI; The Voice of Business, Ernst & Young .
- Best, J. W., & Kahn, J. V. (1977). *Research In Education*. Boston: Englewood Cliffs, N.J Prentice Hall.
- Bethitina, L. (2015, January). The Determinants of External Audit Quality Evidence From Manufacturing Share Companies of Addis Ababa Ethiopia. Addis Ababa, Ethiopia.
- Boone Jr, H. N., & Boone, D. A. (2012). Analyzing Likert Data. *Journal of Extension* , 50(2), 1-5.
- Brooks, C. (2008). *Introductory Econometrics (Second ed.)*. New York: Cambridge University Press.
- Brown, R. E., & Mark, J. M. (2006). "IRS's Comprehensive Approach to Compliance Measurement" Internal Revenue Service. *Forum on Tax Administration Compliance*, (pp. 4-5).
- Budur, J. (2008). Factors Affecting The External Auditor's Fees in The Hashemite Kingdom of Jordan. *Arab Journal of Accounting* , 11 (1).
- Carey, P., & Simnett, R. (2006). Audit Partner Tenure and Audit Quality. *The Accounting Review* , 81, 653-676.

- Clark, L. A., & Watson, D. (Sep 1, 1995). Constructing validity: Basic issues in objective scale development. *American Psychological Association* , 7 (3), 309-319.
- Cohen, J. (1988). *Statistical Power Analysis for The Behavioral Science*. New Jersey: Lawrence Erlbaum Associates, Hillsdale New Jersey.
- Cooper, D. R., & Schindler, P. S. (2006). *Business Research Methods*. 9th ed. New York: Mc Graw-Hill/Irwin.
- Cooper, R. D., & Schindler, S. P. (1998). *Business Research Method* (6th ed.). Irwin/McGraw-Hill, 1998.
- Creswell, J. (2007). *Research Design: Qualitative, Quantitative, and Mixed Methods Approaches*, (2nd ed.). London, London: Sage Publications.
- Creswell, J. W. (2009). *Research Design: Qualitative, Quantitative, and Mixed Methods Approach*. 3rd ed. California, USA: Sage Publications Inc.
- Cronbach, L. J. (1951). Coefficient alpha and the internal structure of tests. Netherlands: Klaas Sijtsma—Tilburg University.
- Cuthbert, S., & Young, J. (n.d.). <https://www.safeopedia.com/definition/625/regulatory-body>. Retrieved May 22, 2019, from [www.safeopedia.com](http://www.safeopedia.com).
- Dawson, C. (2002). *Practical Research Methods: A user-friendly guide to mastering research techniques and projects*. London, UK: How To Books Ltd, Oxford OX4 1RE, UK.
- DeAngelo, L. (1981). Auditor Size and Audit Quality. *Journal of Accounting and Economics* , 3, 183-199.
- DeBacker, H. B. (2015). Once bitten, twice shy? The Lasting Impact of IRS audits on individual tax reporting. *Journal of Financial Economics* , 117(1), 122-138.
- Dessalegn, G. (2009). *Accounting Professionalization Amidst Altering State Ideology in Ethiopia: External Auditors " Unethical Behaviour and Corporate Business"*. Emerald .
- DeVellis, R. (2003). *Scale Development: Theory and Applications*. 2nd ed. California : s.n.
- Directive. (2003). *Internal Audit Directive*. Federal Government of Ethiopia Directive No. 7/2003.
- Dubin, J. (2004, June). Criminal investigation enforcement activities and tax payer non-compliance IRS research conference.
- EFDRE, H. o. (2016). *Federal tax Administrative Law*. Addis Ababa: Birhanina Selam printing Press.

- Ejigsew, A. (2016, February). The Impact of Provision of NAS to Audit Clients on Auditors Independency and Audit Quality. Addis Ababa, Ethiopia.
- Eliud, M., & Eric, R. (2006). Taxation and Tax Modernization in Kenya: A Diagnosis of Performance and Options for Further Reform. Nairobi: Institute of Economic Affairs.
- Engida, B. (2016, February). Threats to Professional Ethics: Among selected Authorized Accountants and Auditors in Ethiopia. Addis Ababa, Addis Ababa, Ethiopia.
- FDRE. (1961). The Government of Ethiopia , Auditor general proclamation, No. 179/1961, Negarit Gazette.
- Fentaye, T. Z., & Nageswararao, T. (2015). The Tax Payer Assessment of Tax Evasion causes for Business Tax Payers-A Study on Amhara National Regional State, Ethiopia. The Journal of Indian Management , 5 (4), 74-84.
- Firas A., N.-D. (2018). The Role of External Auditor in Protecting The Financial Information Listed in The Financial Statements in The Jordanian Industrial Companies. Journal of Modern Accounting and Auditing , 14 (1), 6-16.
- Flint, D. (1988). Philosophy and Principles of Auditing.
- Friedland, N. (1978). A Simulation Study of Income Tax Evasion. Journal of Public Economic .
- Getaneh, M. (2011, June). Tax Audit Practise in Ethiopia: The Case of Federal Government. Addis Ababa, Ethiopia.
- Ghosh, A., & Moon, D. (2005). Auditor Tenure and Perception of Audit. The Accounting Review , 80 (1), 585.
- Halim, A., T. Rosidi, S., & Achisin, M. (2014). Effect of Competence and Auditor Independence on Audit Quality with Audit Time Budget and Professional Commitment as a Moderation variable. International Journal of Business and Management Invention , 3 (6), 64-74.
- Hayes, R., Schilder, A., Dassen, R., & Wallage, P. (1999). Principles of Auditing: An international Perspective. London: McGraw-Hill.
- Hyun, J. (2005). Tax compliance in Korea and Japan: Why are they different?
- IAASB. (2009). International Auditing and Assurance Standard Board.
- ICAEW. (2018). Retrieved 2018, from [WWW.icaew.com/technical/ethics/auditor-independence/provision-of-non-audit-services-to-audit-clients](http://WWW.icaew.com/technical/ethics/auditor-independence/provision-of-non-audit-services-to-audit-clients).

ICAEW. (2003). An Effective Audit Process. Institute of Chartered Accountants in England and Wales.

IESBA. (n.d.). Code of Ethics of Professional Accountants.

rg/guidance/standards-and- guidance/ippf/practice-advisories/.

James, I. O., & Izien, O. F. (2014). Audit Firm Characteristics and Audit Quality in Nigeria. *International Journal of Business and Economic Research* , 3 (5), 187-195.

Jean, B. H. (2018). Effect of Tax Audit on revenue Collection in Rwanda. *Global Journal of Management and Business research:Accounting and Auditing* , 18 (2).

Jeff, D., & Jhon, C. L. (2018). Audit Exemptions and Compliance with Tax and Accounting regulations.

Jim, F. (2019). An Intuitive Guide For Using and Interpreting Linear Model.

Jonker, J., & Pennink, B. (2010). The Essence of Research Methodology: A concise guide for Masters and Phd students in management science.

Jr., K., R., W., Palmrose, Z.-V., & Scholz, S. (2004). Auditor Independence, Non-Audit Services, and Restatements: Was the U.S. Government Right. *Journal of Accounting Research* 42(3) , 561-588.

Kassahun, G. (2010). General Concept of Auditing in Ethiopia.

Kassem, R., & Higson, A. (2016). External Auditors and Corporate Corruption: Implications of External Audit Regulators. *Current Issues in Auditing* , 10 (1), 1-10.

Kirchler, E. (2008). Enforced Versus Voluntary Tax Compliance: The "Slippery Slope" Framework. *Journal of Economic Psychology* .

Kothari, C. (2004). *Research Methodology Methods and Techniques*. 2nd Revised Edition ed. New Delhi: New Age International Limited.

Lawrence, A., Minutti, M., & M., P. (2011). can Big 4 versus Non-Big 4 Differences in Audit Quality Proxies be Attributed to Client Characteristics? *The Accounting Review* , 86, 259-286.

Lee, T. (1993). *Corporate Audit Theory*. London: Chapman & Hall.

Limperg, T. (1932). *The Theory of Inspired Confidence*.

Linda, M. ( 2004). Putting SEC Heat on Audit firms and Corporate Tax Shelters: Responding to Tax Risk with sunshine Shame and Strict Liability. *The Journal of Corporation Law*, Vol. 29

- Lotfii, A. (2005). Different Auditing for Different Purposes.
- Mahdi, S. (2011). Audit Expectation Gap: Concept, Nature and Trace. *Africa Journal of Business Management* , 5(21).
- Mansouri, A., Pirayesh, R., & Salehi, M. (2009). Audit Competence and Audit Quality: Case In Emerging Economy. *Canadian Center of Science and Education (CCSE)*.
- Matsuda, P., & Silva, T. (2005). *Second language writing research: Perspectives on the process of knowledge construction*. Lawrence Erlbaum.
- Mautz, R. K., & Sharaf, H. A. (1961). *The Philosophy of Auditing*. Minesota, University of Minnesota: American Accounting Association.
- Minyichel, B. (2017, June). Factors affecting tax revenue in Ethiopia. Addis Ababa, Ethiopia.
- Mona, L. (2018, August 22). <https://www.datapine.com/blog/data-interpretation-methods-benefits-problems/>. Retrieved April 21, 2019, from [www.datapine.com](http://www.datapine.com).
- Monk. (2017, May 12). Audit Monk. Retrieved April 20, 2019, from <https://auditmonk.wordpress.com>: <https://auditmonk.wordpress.com/2017/05/12/brief-history-of-auditing/>
- Mui, G. (2009). Defining auditor expert performance in fraud detection, 2009 Accounting and Finance Association of Australia and new Zealand(AFAANZ) (Accounting and Finance Association of Australia New Zealand, Adelaide, Australia).
- Muley, R. (2019). [WWW.economic discussion.net](http://WWW.economic discussion.net). Retrieved March 28 March 2019, 2019
- Muluneh, B. (2007). Auditors Professional Responsibilities and Legal Liability with regard to Private Auditors in Ethiopia. Addis Ababa, Ethiopia.
- Mutarindwa, S., & Rutikanga, J. D. (2014). The Impact of Tax payers Financial Statements Audit on Tax Revenue Growth. *International Journal of Business and Economic Development (IJBED)* , 2.
- Neumark, F., S.Cox, M., & E.Maclure, C. (2019). Taxation. *Encyclopaedia Britannica*.
- OFAG. (2009). *Ethiopian Code of Ethics for Professional Accountant*. Addis Ababa.
- Ojo, M. (2006). The Role of External Auditors and International Accounting Bodies in Financial Regulations and Supervision. 354 , 1-14. *Munich Personal RePEc Archive (MPRA)*.
- Olaoye, C. O., & Ekundayo, A. T. (2019). Effects of Tax Audit on Tax Compliance and Remittance of Tax Revenue in Ekiti State. *Open Journal of Accounting* , 8, 1-17.

- Parliament. (2016). Federal Income Tax Proclamation. Addis Ababa: Federal Negarit News Paper.
- Porter, B. (2003, April). [www.media.wiley.com](http://www.media.wiley.com/productdata/exerpt/170/04708429/0470842970.pdf). Retrieved April 04, 2019, from [www.media.wiley.com/productdata/exerpt/170/04708429/0470842970.pdf](http://www.media.wiley.com/productdata/exerpt/170/04708429/0470842970.pdf).
- Reisinger, H. (1997). The Impact of Research Designs on R<sup>2</sup> in Linear Regression Models: an Exploratory Meta-Analysis. *Journal of Empirical Generalizations in Marketing Science* , 2(1), 1-12.
- Remenyi, D., Williams, B., Money, A., & Swartz, A. (2002). *Doing Research in Business and Management*. London: Sage Publication.
- Representative, H. o. (2016). Federal Income Tax Proclamation (Vol. 979/2016). Addis Ababa, Ethiopia: Birhanina Selam Printing Press.
- Robert, S. M., & T.D., C. N. (2000). <http://www.ctj.org>. Retrieved from <http://www.ctj.org>.
- Rusmanto, T. (2002). An Investigation of factors Influencing Auditor Independence: A case of Indonesia. Indonesia: University of Wollongong.
- Saleemi, N. (2008). K.A.T.C. Financial Accounting Simplified. Nairobi: Mount Kenya University.
- Sarens, G. (2009). Internal Auditing Research: Where are we going? Editorial. *International Journal of Auditing* , 13(1), 1-7.
- Saunders, M., Lewis, P., & Thornhill, A. (2009). *Research Methods for Business Students*. (Vol. 5th ). Harlow, England: Pearson Education Limited.
- Saunders, M., Lewis, P., & Thornhill, A. (2009). *Research Methods for Business Students*. 5th ed. Harlow, England: Pearson Education Limited .
- Sawan, N., & Alsaqqa, I. (2013). Audit firm size and quality: Does audit firm size influence audit quality in the Libyan oil industry. *African Journal of Business Management* , 7 (8), 213-226.
- Sayer, A. (1992). *Method in Social Science: A realistic approach* (2nd ed.). USA and Canada.
- SEC. (2002). Sarbanes-Oxley Act of 2002. U.S.A: Securities and Exchange Commisiion.
- Serafat, S., & Barzegar, G. (2015). Investigating the relation between tax avoidance and auditor tenure in the listed companies in Tehran stock exchange. *Journal of Scientific Research and Development* . , 2 (4), 1-5.

SShodhganga. (2019, April 04). Retrieved 2019, from [www.shodhganga.inflibnet.ac.in>bitstream](http://www.shodhganga.inflibnet.ac.in/bitstream).

Shume, G. W. (2016). "Determinants of perceptions of External Auditors" Independence in Ethiopia Private Audit Firms. Addis Ababa.

Silow, M. L. (2003). IRS Stands to Get Aid in Tax Shelter Battle, 228 *Legal Intelligencer*.

Simon, L. D., Ege, M. S., & Bridget, S. (2015). Internal Control Quality: The Role of Auditors-Provided Tax Services. *American Accounting Association* , 90 (4), 1469-1496.

Sinason, D., Jones, J., & Dan, S. S. (2001). An Investigation of Auditor and Client Tenure. *The Mid-American Journal of Business* , 16 (2), 31-40.

Singlton, J. R., & Straits, B. (2005). *Approach to Social Research* (4th ed.). New York: Oxford University Press.

Slade, M. K. (1939). The Ability-to-pay Theory of Taxation. *The American Economic Review* , 29, 92-101.

Solomon, K. (2016). *factors Affecting Quality of External Auditing: The Case of Ethiopian Commercial Banks*. Addis Ababa University.

Song, Y. (1978). Tax Ethics and Tax Payer Attitudes: A Survey *Public Administration Review*. *American Society of Public Administration* , 38.

Steven, C. (2011). *Interpretation and Application of International Standards on Auditing*. Chichester, United Kingdom: John Willey and Sons Ltd.

Suyono, E. (2012). Determinant Factors Affecting The Audit Quality: An Indonesian Perspective. *Global Reveiw of Accounting and Finance* , 3 , 42-57.

Tamirat, A. (2014). *Audit Fees Determinants and Audit Quality in Ethiopian Commercial Banks*.

Tandon, B. N., Sudharsanam, S., & Sundharabahu, S. (2010). *A Hand Book of Practical Auditing: 14th edition*, pp. 112-115, New Delhi: S. Chand & Company Ltd.

Tesfaye, A. (2015). *Determinants of Tax Revenue Performances in Ethiopia: Case of Ethiopian revenues and Customs Authority*.

The World Bank in Ethiopia. (n.d.). Retrieved June 13, 2018, from [www.worldbank.org/en/country/ethiopia/overview](http://www.worldbank.org/en/country/ethiopia/overview).

Tilahun, A. (2014). Determinants of Tax compliance Behaviour in Ethiopia: The Case of Bahirdar City Tax payers. *Journal of Economics and Sustainable Development* , 5 No. 15.

- Toto, R., & Stephanus, R. W. (2015). factors Influencing Audit Feein Indonesia publicly Listed Companies Applying GCG. Elsevier , 172, 63-67.
- Tsegaw, B. F. (2017). Auditors Perception of Audit Quality in Ethiopia.
- Turley, S., & Zaman, M. (2007). Audit Committee Effectiveness: Informal Processes and Behavioral Aspects. Accountability Journal , 20(5), 1-30.
- UK, E. (2018). Concepts and Theories of Auditing.
- Urpis, E. (2015/2016). Essays on Tax Compliance.
- Vanek, C. (2012). Likert scale-What is it? When to use it? How to analyze it? s.l.: Survey Gizmo.
- Watts, L. R., & Zimmerman, L. J. (1983). Agency problems, Auditing, and The theory of the firm: Some Evidences. Journal of Law and Economics , XXV.
- Whittington, R., & Pany, k. (2004). Principles of Auditing and Other Assurance Services (Vol. 16). MCGraw-Hill/Irwin,2004.
- Williamson, k. (August 2015). Assessing the effectiveness of the external audit process; A practical guide and tool for audit committees. EY .

## APPENDIX (1)

**ADDIS ABABA UNIVERSITY**  
**COLLEGE OF BUSINESS AND ECONOMICS**  
**DEPARTMENT OF ACCOUNTING AND FINANCE**  
**MSc IN ACCOUNTING AND FINANCE**

### Questionnaire for Audit Firms

This study is entitled “*The Effectiveness of External Audit on Tax Collection in Ethiopia: Case of ERCA LTO*”. It is purely intended for academic purpose and is for the partial fulfillment for the award of master’s degree in Addis Ababa University College of Business and Economics department of Accounting and Finance. Your participation in this study is completely on voluntary bases and you have the right to take part or to contact at any time. The information that you will provide is quietly useful to know about the effectiveness of external audit on tax collection. I would like to assure you, your name will not be mentioned in anywhere. The information that you will give us will be kept confidential and only be used for the research purpose.

Best Regards

Asrat Abadi

Tele 0911377671

## Section A: *Demographic Background*

Please kindly put (X) your answer in the appropriate boxes or respond by writing if required.

1. Age:

20-30 years old

31-40 years old

Above 40 years old

2. Education level

TVET, Diploma

Bachelor's degree

Master's degree

Other (please specify)

3. Years of work experience:

Less than 5 years"

6 - 10 years

11 - 20 years"

Over 20 years"

4. Your current position

Senior Auditor

Deputy Audit

Audit manager

Senior Audit

Principal/Partner

## Section B: External audit questions

In this section the researcher is seeking your specific perceptions towards “*The Effectiveness of External Audit on Tax Collection*” Please kindly indicate the appropriate scale for your opinion by putting (X) on the spaces that indicate your choice from the options that range from

1=Strongly Disagree (SD),

2=Disagree (D),

3=Neutral (N),

4=Agree (A),

5=Strongly Agree (SA),

<b>NQ</b>		<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
	<b>Questions</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
<b>A. Competence of External Auditors</b>						
1	External auditors have adequate educational background.					
2	Do you think the audit department or division has improved in terms of appropriately qualified or professional staff?					
3	External auditors are proactive (creating or controlling a situation rather than just responding).					
4	External auditors undertake continuous professional development trainings or attend educational seminars					
5	External auditors have adequate educational background.					

<b>NQ</b>	<b>B. Awareness or Attitudes of External Auditors</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1	External audit staffs are aware on the value of tax for the nation development.					

2	Awareness about the value of tax makes external auditors to present fair financial statements to the tax authority.					
3	The External Audit Firm staffs knows the consequence of not reporting fair financial statements to the tax authority on the tax payers or clients.					
4	There are a complied books or magazines or library in the audit firm to improve tax awareness for their staffs.					
5	The Ministry of education curriculum will add a value to create awareness on tax issues.					
<b>NQ</b>	<b>C. Independence of External Auditors</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1	The value of auditing depends heavily on the independence of auditors in mind and appearance.					
2	Auditors exercise their independence as an auditors in their audit Firms during the audit duties.					
3	Audit firms support auditors to be independent when undertaking audit duties.					
4	Reliable audit report performed by independent auditors is very important for financial statements users.					
5	Independence of Auditor is the reason for the existence of auditing profession that provides audit service.					
<b>NQ</b>	<b>D. Regulatory Body</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1	ERCA work co-operatively with the external auditors to facilitate the tax collection process.					
2	The existence of well capable associations in the field of finance have a value to produce a quality audit.					
3	The absence of tax manual prepared by the regulatory body reduces the effectiveness of external auditors.					
4	The assignment of capable and experienced staff by a regulatory body facilitate the tax collection process .					
5	Acknowledgement by the regulatory body to audit firms has a great contribution to the tax collection process.					

<b>NQ</b>	<b>E. Audit Firm Size</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1	Audit firm size is a strong reason to increase tax collection					
2	Large audit firms maintain their independence without any interference because of their financial strength.					
3	Large auditing firms are less willing to acquiesce to client pressure to provide substandard reporting.					
4	Large audit firm are associated with high accurate accounting estimates than were smaller accounting firms.					
5	Large auditing firms are more likely to detect and report material problems.					
<b>NQ</b>	<b>F. Audit Fee</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1	large audit fee paid by the client doesn't make the auditor more economically dependent on the client.					
2	Do you think less audit fee reduce the scope of audit effort to detect fraud?					
3	Competition between audit firms on audit fee will affect audit quality					
4	The amount of audit fee received doesn't affect the audit quality as far as the external auditor keep the professional ethics.					

<b>NQ</b>	<b>G. Audit Tenure</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1	The risk of an audit failure is likely to increase as the audit tenure period increases due to client management becoming too familiar with the auditor's approach and procedures					
2	Audit firms receive more litigation in the beginning of their audit than their later years.					
3	The likelihood of receiving a Substandard quality audit increases with the length of the auditor client relationship.					
4	The risk of an audit failure is higher in the early years of an audit tenure period.					

<b>NQ</b>	<b>H. Tax Audit</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1.	The frequent tax audit carried by the tax auditor without delay will improve the tax collection process.					
2.	The external auditor assumed future tax audit investigation has an impact on the work of his/her current clients financial report not to exposed the client for unnecessary fines (interest and penalty)					
3.	Tax audit undertaking by the ERCA has an advantage for the external auditor to share the new issued tax laws and regulations.					
4.	Even if the financial statements are audited by the external audit firms, clients believed that their interaction with the authority staff makes easier their obligation to pay actual tax.					

<b>NQ</b>	<b>I. Tax Collection</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
1.	Effectiveness of external audit increases the tax collection.					
2.	Audited financial statement has a great value to increase the tax collection.					
3.	The government and external auditors' cooperation has a vital benefit for tax collection.					

## **APPENDIX (2)**

**ADDIS ABABA UNIVERSITY**  
**COLLEGE OF BUSINESS AND ECONOMICS**  
**DEPARTMENT OF ACCOUNTING AND FINANCE**  
**MSc IN ACCOUNTING AND FINANCE**

### **Interview for ERCA Tax Audit Department**

This study is entitled “*The Effectiveness of External Audit on Tax Collection in Ethiopia: Case of ERCA LTO*”. It is purely intended for academic purpose and is for the partial fulfillment for the award of master’s degree in Addis Ababa University College of Business and Economics department of Accounting and Finance. Your participation in this study is completely on voluntary bases and you have the right to take part or to contact at any time. The information that you will provide is quietly useful to know about the effectiveness of external audit on tax collection. I would like to assure you, your name will not be mentioned in anywhere. The information that you will give us will be kept confidential and only be used for the research purpose.

Best Regards

Asrat Abadi

## **Interview Questions**

1. To what extent do private auditors exercise their professional responsibilities?
2. Do you believe that audited reports provided by the tax payers has better value than the non audited? If your answer is yes, how?
3. Would the professional qualification of external auditors affect the reliability of published financial statement?
4. Do you believe that each external auditors have a moral obligation to report all of their clients' income and to make to pay the correct amount of corporate income tax?
5. How do you think the Independency or Competence of external auditors on the reported financial statements?
6. To what extent does audit firm size or audit tenure or audit fee have an effect on the tax amount?
7. Do you think that the tax audit made by your office has an impact on the performance of the external auditors to facilitate or improve the tax collection process? If your answer is "yes", how?

## Financial Budget and Time Table

### Time Schedule

Ser. No.	Activites to accomplish	Accomplishment periods in months and Weeks																																							
		April 2018				May 2018				June 2018				July 2018				August 2018				Sept 2018				October 2018				Nov 2018				Dec 2018				January 2019			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4				
1	Review of literature			x	x	x	x	x																																	
2	Proposal writing (Draft)											x	x	x	x	x	x																								
3	Proposal writing (Final)																																								
4	Data collection																																								
5	Data analysis and Interpretation																																								
6	Report writing																																								
7	Report (Draft)																																								
8	Correcting & Editing First Draft																																								
9	Report (Final)																																								
10	Presentation																																								

### 3 Cost Budget

Item	Measurement Unit	Quantity	Price per unit	Total price in Birr
Pen	Piece	4	7.00	28.00
Paper sheet	Pack	1	185.00	185.00
Flash disc 8 GB	Piece	1	250.00	250.00
Printing	Page	230	1.00	230.00
Photocopy for necessary materials	Page	300	1.00	300.00
Fuel oil for data collection	Km	500	0.75	375.00
Allowance to be used While Collecting Data	Days	45	100.00	4,500.00
Miscellaneous expense	-	-	-	500.00
Binding the Research Paper	Piece	4	13.00	52.00
Agenda	Piece	1	80.00	80.00
Text Marker	Piece	1	25.00	25.00
Office Rent appropriated	Day	60	3800.00	7,600.00
<b>Grand Total</b>				<b>14,125.00</b>