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**ADDIS ABABA UNIVERSITY  
SCHOOL OF BUSINESS AND ECONOMICS  
DEPARTMENT OF ACCOUNTING AND FINANCE  
(GRADUATE PROGRAM)**

*Taxpayers' tax compliance Behavior- Business  
profit taxpayers' of Addis Ababa city  
Administration*

*A Thesis Submitted to the School of Graduate Studies of Addis Ababa  
University in Partial Fulfillment of the Requirements for the Degree of  
Master of Science in Accounting and Finance.*

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## SCHOOL OF GRADUATE STUDIES

### Statement of Declaration

This is to certify that the thesis prepared by Geletaw Tsegaw Tessema entitled: “*Taxpayers’ tax compliance behavior - Business Profit taxpayers’ of Addis Ababa city*” and submitted to in partial fulfillment of the requirements for the degree of master of science in Accounting and Finance; complies with the regulations of the university and meets the accepted standards in respect of originality and quality.

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### ***Abstract***

*This paper attempted to reveal determinants of taxpayers' tax compliance behavior. Six tax compliance determinants were examined; the examined tax compliance determinants were: tax knowledge; feeling of fairness; the influence of peer groups; income level of taxpayers; detection & punishments and perception on government spending. The study adopted a mixed method research approach to test the proposed hypotheses and to answer research questions. The data has been collected from 225 business profit taxpayers of those 200 were through distributing of self-administered questionnaires and the remaining 25 through in-depth-interviews. The latest statistical package (SPSS) software, correlation and regression analysis, were used to analyze the survey and thematic analysis was applied to the in-depth interviews. The results of this combined research methodology suggest that Addis Ababa City business profit taxpayers tax compliance behavior have been highly and significantly affected by tax knowledge; feeling of fairness; the influence of peer groups; income level of taxpayers and detection & punishments variables while confidence in government spending doesn't have as such significant impact on tax compliance behavior of businesses. The analysis focuses on tax compliance and its determinants and is therefore subject to an underlying assumption of tax payers' understanding of tax and other potentially relevant information. The results of this study also provide specific insights and allow policy makers to gain a better understanding of the key variables that are significantly associated with tax compliance and enable them to implement suitable strategies to minimize potentially damaging factors, and should also allow them to improve their government's tax revenue collections. Such a study becomes imperative given limited research so far undertaken in the area. The present study may also be utilized to provide further information to assist tax authorities in designing full-fledged tax policies and in improving their respective tax collection mechanisms.*

**Keywords:** Tax Compliance Behavior, Tax non-compliance, Tax evasion, Business Profit Taxpayers', Tax avoidance, Tax compliance Opportunity, Attitudes and perceptions.

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## Acronyms

BF	Belief of Fairness
CA	Category A
CB	Category B
CC	Category C
DP	Feeling of Detection and Punishments
DP	Feeling of Detection and Punishments
ERCA	Ethiopian Revenue and Custom Authority
ETB	Ethiopian Birr
GDP	Gross Domestic Product
GERD	Great Ethiopian Renaissance Dam
GS	Confidence in government spending
GTP	Growth and Transformation Plan
IL	Income Level
IR	Tax Compliance
PAYE	Pay as You Earn
PG	Peer Group influences
SS	Sample Size
TC	Inland Revenue
TK	Tax Knowledge
VAT	Value Added Tax

## Chapter One: Introduction

### 1.1 Background of the study

The issue of taxpayers' tax compliance behavior has evoked great attention among many revenue authorities in the world. Questions about tax compliance are as old as taxes themselves and will remain an area of discovery as long as taxes exist. To understand the impact of a tax system, it is important to know who complies with the tax law as well as who does not. Tax non-compliance is a large and growing problem in almost all countries. Unfortunately, we know very little about tax morale. Economists see the problem as one of rational decision made under uncertainty. This means that cheating on taxes is a gamble paying off in lower taxes or, with the probability of detection, ending in sanctions. This view of taxpayer behavior was first presented in a formal model by Allingham and Sandmo (1972), influenced by the economics-of-crime approach. Nevertheless, such a portfolio analysis can't explain why many households comply more fully than predicted by this approach. A lot of economic approaches to tax compliance continue on this framework. Tax compliance is a finally observable action.

Complying or not is not only a function of opportunity, tax rates, and probability of detection, but also the function of an individual's willingness to comply or evade. When the tax morale is high, tax compliance will be relatively high too. Compliance decisions must be affected by other factors. How can moral rules and sentiments directly guide tax morale? In the literature we find psychological theories which are discussed in the context of tax morale. It may seem astonishing, but a lot of people do comply with the rules and laws. Kelman's (1958) work, adapted to tax compliance by Vogel (1974), illustrates how people comply for different reasons. "Compliers" pay their taxes, because people are required to do so and fear the consequences if they do not. "Identifiers" are influenced by social norms and the beliefs and behaviors of people close or of importance to them. "Internalizers" have a consistency between their beliefs and their behavior.

In additions to this, tax non-compliance has, for a long time, been a challenge to tax officials in executing their role as revenue collectors for the state. Failure to comply with tax

regulations in the country is not only a denial of the state of its needed revenue for developmental projects, but also a discouragement to others to comply. According to Terkper (2003), legitimate taxpayers in the formal sector perceive the state as being unfair in pursuing them for taxes while the informal sector continues to operate untaxed. Ignoring informal sector activities will lower compliance morale and increase the risk of generalized non-compliance.

Therefore, this paper assesses the motives behind complying with the tax legislations i.e. what shapes business profit taxpayers' attitudes to comply with the tax laws? What benefit they receive if they comply with the tax legislations? and what are the risks of non-compliance by focusing on Addis Ababa city administration business profit tax payers.

## **1.2 Statement of the Problem**

The Ethiopian government under the auspices of the Growth and Transformation plan (GTP) has been undertaking initiatives to stimulate and sustain the long run growth and development of the country's economy. It's believed that, this medium term economic endeavor will bring a tremendous change in the country's economy. As part of the GTP initiatives, the government has undertaken mega budget projects by selecting priority sectors. Due to this fact, revenue mobilization has becoming a great concern of government in recent years. However, the issue of non-compliance, tax avoidance and tax evasion has posing a serious challenge for the tax and revenue authorities.

The domestic tax bases in most African countries are undermined by widespread tax avoidance and evasion. Although taxpayers' non-compliance is a continual and growing global problem and studies suggest that developing countries, many of them in Sub-Saharan Africa, are the hardest hit. For instance, in Ethiopia non-compliance in the tax administration system can be exhibited in different economic indicators. These include persistent low tax to GDP ratio. In spite the fact that the Ethiopian economy is growing fast where in double digit, it has continued generating low tax revenues by far low even as compared with sub-Saharan Africa countries (World Bank 2010). Therefore, dealing with the problem of non-compliance requires an understanding of the factors underlying taxpayers' decision about whether to pay

or evade taxes. Better understanding of taxpayer behavior can be expected to place revenue bodies in a stronger position to design and implement effective compliance strategies, which contributes to the sustainability of taxation systems.

In Ethiopia, the issues of tax compliance behavior have not been significantly investigated. However, the study conducted by Tilahun Aemiro et.al (2014) revealed that perception on government spending; equity and fairness of the tax system; penalties; personal financial constraints; changes on current government policies; and referral group (friends, relatives etc.) as factors that significantly affects the tax compliance behavior. Notwithstanding, this study has also ignored tax knowledge as a determining factor in affecting the tax compliance behavior of business profit tax payers. In additions to this, Suresh Vadde (2014) investigated only a certain factors as determinants of taxpayers' voluntary compliance. This study neglected some of the factors (i.e. detection and punishments) which contribute its part in affecting the tax compliance behavior of business profit tax payers.

Therefore, this paper assesses factors that affects taxpayers' tax compliance behavior and what shapes their attitude to comply with the tax legislations while the benefits of non-compliance is outweighing in the case of business profit tax payers operating in Addis Ababa city Administration . As per Fishers et.al (1992) tax compliance behavior have been affected by different factors and some of them are intrinsic to individuals own motives and others are external to different situations. As a result, assessing those factors in the context of Ethiopia helps policy makers and tax authorities to better understand the behaviors of the taxpayers and develop and design full-fledged tax policies and procedures.

### **1.3 Objectives of the study**

#### **1.3.1 General objective**

In the context of the problems and research questions highlighted above, the broad objective of the study is to assess factors affecting tax compliance behaviour of businesses profit tax payers operating in Addis Ababa City Administrations. Thus, this paper tries to answer the motives behind complying or not with the tax legislations.

### 1.3.2 Specific objectives

The specific objectives are;

- ✓ To investigate factors affecting the taxpaying attitudes of business profit tax payers.
- ✓ To determine the factors motivating business profit taxpayers to comply with the tax legislations.
- ✓ To assess efforts made by tax authorities in inspiring people to comply with the tax legislations.
- ✓ To identify the risks encountered by business profit tax payers because of non-compliance with the tax legislations.

## 1.4 Research Question and Hypothesis of the study

In order to achieve the above broad objectives, the researcher had developed one research questions and six hypotheses.

*Why business profit tax payers comply with the tax legislations while the benefits of non-compliance is outweighing?*

Hypothesis 1:

*Tax knowledge (demographic factor) affects the taxpaying attitudes of business profit tax payers operating in Addis Ababa city administrations.*

Hypothesis 2:

*Belief in fairness (attitude & perception factor) affects the tax compliance behavior of business profit tax payers.*

Hypothesis 3:

*Influences of the peer groups (attitudes & perception) positively and significantly affects the tax compliance behavior of business profit tax payers.*

Hypothesis 4:

*Income level of tax payers does have positive and significant impact on the tax compliance behaviors of business profit tax payers.*



**Hypothesis 5:**

*Feeling of detection and punishments by the tax authorities does have significant impact on the tax compliance behaviors of business profit taxpayers.*

**Hypothesis 6:**

*Taxpayer's confidence in government spending significantly affects the tax compliance behavior of business profit tax payers.*

## **1.5 Research Method**

The researcher adopted mixed research approaches in order to assess factors that affect tax compliance behavior of businesses operating in Addis Ababa city administration. This mixed research approach helps to gather data that could not be obtained by adopting a single method. While acknowledging an important contribution of a mixed method approach in taxation studies, McKerchar (2010) also highlights several reasons behind the use of such an approach. The first is the need to address different objectives of the study, which cannot be achieved by a single method. The second reason is to enable one approach to inform another approach, either in design or in interpretation. The third reason is to triangulate the findings of different approaches (either performed concurrently or sequentially) in an effort to provide greater confidence to the study.

Based on the above researcher recommendations, it appears that the main reason for the researcher to adopt a mixed method approach is to enable one approach to inform another approach in the interpretation of the overall results. To be consistent with this approach, the researcher has been employed survey and interviews as a major research tools. Those methods were carried out sequentially with the intention that the interviews were enriching the findings in the survey. The researcher used both primary and secondary data's in order to analyze the research. The primary data were collected through questionnaire and interview while the secondary data has been collected from tax authorities, websites and different books.

## **1.6 Delimitation/Scope of the study**

The primary aim of this study is to examine factors affecting taxpayers' tax compliance behavior. In doing so, the researcher encountered non-response rate of 23.5%. This non-

response rate has been registered because some of the respondents are not aware of the issue of tax compliance behavior and; most of the questions are related with individuals own intrinsic and extrinsic motives. Moreover, many business owners' lacks proper educational background and expertise in order to easily understand and respond to the questionnaire and interviews.

## **1.7 Organization of the Research**

The thesis focuses on the examination of taxpayers' tax compliance behavior by focusing on Addis Ababa City Administration business profit taxpayers. Therefore, the paper has been structured as follows. Chapter 2 contains a review of the literature including tax compliance theory; factors determining tax compliance behavior and its relationships with tax morale and attitudes; a review of Ethiopian tax system and past studies and research gaps. The research design and methodology are presented in chapter 3. Chapter 4 presents the results of survey and in-depth interviews subsequently this is followed by an analysis of the results of the different methods concurrently. That is, the findings of all the different methods adopted in this study are pooled together, the research question is answered, and hypotheses tested. Finally, chapter 5 presents an overview of the thesis and its major findings, recommendation, contribution to the literature, and tax authorities and limitation of the research.

## **Chapter Two: Review of Related Literature**

In light of the above, the purpose of this chapter is to review the literature in the area of “tax payers’ tax compliance behaviour”. This review of the literature establishes the framework for the study and highlights the apparent strengths and weaknesses of the previous studies, which in turn helps to clearly identify the gap in the literature and formulating the research question for the study.

### **2.1 The Concept and Definitions of Tax Compliance**

Tax compliance is a major problem for many tax authorities and it is not an easy task to persuade taxpayers to comply with tax requirements even though tax laws are not always precise. The exact meaning of tax compliance has been defined in various ways. For example, Andreoni et.al (1998) claimed that tax compliance should be defined as taxpayers’ willingness to obey tax laws in order to obtain the economy equilibrium of a country.

A wider definition of tax compliance, defined in 1978 by Song and Yarbrough suggested that due to the remarkable aspect of the operation of the tax system in the United States and that it is largely based on self assessment and voluntary compliance, tax compliance should be defined as taxpayers’ ability and willingness to comply with tax laws which are determined by ethics, legal environment and other situational factors at a particular time and place. Furthermore, tax compliance has also been segregated into two perspectives, namely compliance in terms of administration and compliance in terms of completing (accuracy) the tax returns. Compliance in pure administrative terms therefore includes registering or informing tax authorities of status as a taxpayer, submitting a tax return every year (if required) and following the required payment time frames.

In contrast, the wider perspective of tax compliance requires a degree of honesty, adequate tax knowledge and capability to use this knowledge, timeliness, accuracy, and adequate records in order to complete the tax returns and associated tax documentation.

This perspective further reveals, although it is inevitable that tax authorities will seek to ‘influence’ the areas taxpayers have influence over determining to reduce the risks of non-

compliant behavior they face otherwise e.g. through continuously conducting tax audits of different sorts and other means such as various compliance influencing activities including tax education. Some authors have viewed tax compliance from a different perspective. For example, Allingham and Sandmo (1972) described tax compliance as an issue of 'reporting an actual income' and also claimed that tax compliance behavior was influenced by a situation whereby taxpayers have to make a decision under uncertainty Clotfelter (1983) i.e. either taxpayers would enjoy tax savings due to under-reporting income or have to pay tax on the undeclared amount at a penalty rate which is higher than they would have paid had the income been fully declared at the correct time. McBarnet (2001) suggested tax compliance should be perceived in three ways, namely;

- a) Committed compliance - taxpayers' willingness to pay taxes without complaint;
- b) Capitulative compliance - reluctantly giving in and paying taxes and
- c) Creative compliance – engagement to reduce taxes by taking advantage of possibilities to redefine income and deduct expenditures within the bracket of tax laws.

Some literatures characterize and explain tax compliance as the output of interrelation among variables including perception of equity, efficiency and incidence (public finance views). Tax enforcement aspects like penalties and the probability of detection also relate to tax compliance while other labor market behavior factors including an individual's wages and tax bracket also contribute to tax compliance (Kirchler 2007).

In contrast with tax compliance, tax non-compliance is defined as taxpayer's failure to remit a proper amount of tax, perhaps on account of the complexity or even contradictions in the tax legislation or tax administration procedure. Non-compliance is also perceived as the failure of a taxpayer to report (correctly) the actual income, claim deductions and rebates and remit the actual amount of tax payable to the tax authority on time Kirchler (2007). Furthermore, it has been defined as failure to comply with tax laws and/or report incorrect income, the act of claiming incorrect deductions, relief and rebates and/or paying the incorrect amount of tax beyond the stipulated time frame.

## 2.2 Tax Compliance Theories

Models of taxpayer behavior, including the decision whether or not to pay taxes, tend to reflect one of five theories that can be referred to as: (1) economic deterrence; (2) fiscal exchange; (3) social influences; (4) comparative treatment; and (5) political accountability. These are to some extent interconnected, and some represent an evolution of others.

### **Economic deterrence**

The economic deterrence theory states that taxpayer's behavior is influenced by factors such as the tax rate determining the benefits of evasion, and the probability of detection and penalties for fraud which determine the costs (Allingham and Sandmo 1972; Becker 1968). This implies that if detection is likely and penalties are severe, few people will evade taxes. In contrast, under low audit probabilities and low penalties, the expected return to evasion is high. The theoretical principles of economic deterrence have also been widely adopted by tax administrations when developing enforcement strategies that rely principally on penalties and the fear of getting caught.

### **Fiscal exchange**

The fiscal exchange theory suggests that the presence of government expenditures may motivate compliance and that governments can increase compliance by providing goods that citizens prefer in a more efficient and accessible manner. Alm *et al.* (1992) note that compliance increases with (perceptions of) the availability of public goods and services. Accordingly, the main concern of taxpayers is what they get directly in return for their tax payments in the form of public services (*quid pro quo*). In this perspective, taxation and the provision of public goods and services are interpreted as a contractual relationship between taxpayers and the government (Moore 2004). Individuals may pay taxes because they value the goods provided by the government, recognizing that their payments are necessary both to help finance the goods and services and to get others to contribute (Fjeldstad and Semboja 2001).

The existence of positive benefits may increase the probability that taxpayers will comply voluntarily, without direct coercion. Although most taxpayers cannot assess the exact value of what they receive from the government in return for taxes paid, it can be argued that they have general impressions and attitudes concerning their own and others' terms of trade with the government (Richupan 1987). It is then reasonable to assume that a taxpayer's behavior is affected by his/her satisfaction or lack of satisfaction with his/her terms of trade with the government.

### **Social influences**

In the social influence model, compliance behavior and attitudes towards the tax system is thought to be affected by the behavior and social norms of an individual's reference group (Snively 1990). It is reasonable to assume that human behavior in the area of taxation is influenced by social interactions much in the same way as other forms of behavior (ibid). Compliance behavior and attitudes towards the tax system may therefore be affected by the behavior of an individual's reference group such as relatives, neighbors and friends. Therefore, if a taxpayer knows many people in groups important to him who evade taxes, his/her commitment to comply will be weaker.

On the other hand, social relationships may also help deter individuals from engaging in evasion in fear of the social sanctions imposed once discovered and revealed publicly. Theoretical research on herd behavior in economic situations (Banerjee 1992) also indicates that social influences may affect compliance, in particular by affecting the perceived probability of detection. One of the most consistent findings about taxpayer attitudes and behavior in Western countries is that those who report compliance believe that their peers and friends (and taxpayers in general) comply, whereas those who report cheating believe that others cheat (Yankelovich *et al.* 1984). Evidence suggests that perceptions about the honesty of others may affect compliance behavior.

### **Comparative treatment**

The comparative treatment model is based on equity theory and posits that addressing inequities in the exchange relationship between government and taxpayers would result in

improved compliance (McKerchar and Evans 2009). Citizens may not consider their relationship with the state in a vacuum where both parties are the only actors. Likewise, they may not think about their fellow citizens without considering their own relationship with the state. They may also consider how the state treats them relative to their fellow citizens. This judgment is likely to affect not only their judgment of the state, but also how they view their fellow citizens. If the state treats certain groups preferentially, this may color the citizen's relationship with the state and the group receiving favors. A crucial variable is then not just what a person gets from the state, but what the person gets from the state (and how the state treats the person) relative to those who are in the person's wider national community. This social psychology model highlights the importance of equity theory in the study of compliance and taxpayer behavior.

### **Political legitimacy**

Finally, according to the political legitimacy theory, tax compliance is influenced by the extent that citizens trust their government (Tayler 2006; Kirchler *et al.* 2008; Fauvelle-Aymar 1999). Legitimacy could be described as belief or trust in the authorities, institutions, and social arrangements to be appropriate, proper, just and work for the common good. Political scientists have addressed how political legitimacy and civic identification are fostered. (Persson 2008) argues that African countries that upon independence emphasized building national over ethnic identity have been more successful than those who allowed ethnicity to become the main animus of politics.

## **2.3 Types of Tax compliers**

Kelman's (1965) work, which was adapted to tax compliance by Vogel (1974), illustrates how people can comply for different reasons. Compliance, identification and internalization are Kelman's tripartite typology. "Compliers" pay their taxes because people are required to do so and fear the consequences if they do not. "Identifiers" are influenced by social norms and the beliefs and behaviors of people close or of importance to them. "Internalisers" have a consistency between their beliefs and their behavior. Benno Torgler (2003) in his dissertation

(Tax morale) developed different kinds of taxpayers. For the purpose of this paper some of them are depicted below:-

### **2.3.1. Social Tax Payers**

“Social Taxpayers” are influenced by social norms, feel guilty when they under-report and escape detection and feel ashamed when they under-report and get caught. Furthermore, they are very sensitive to people’s belief, especially of those close to them. They react emotionally and very strongly to perceived changes next to them. They can be seen as conditional cooperators. If they perceive that others pay taxes they tend to pay them too. On the other hand, a reduction of others’ contribution reduces their willingness to contribute. Satisfaction and behavior are linked not only to the objective outcome levels, but also to outcomes received in relation to those which were judged to be fair.

Furthermore, a perceived inequity between one’s own exchange and the exchanges others get creates a sense of distress. Disadvantage in such situation causes anger, advantage; feelings of guilt. Anger reduces the moral costs of evasion.

### **2.3.2 Intrinsic tax payers**

Another type of taxpayer is the “Intrinsic Taxpayer”. The motivation of the “Intrinsic Taxpayers” includes among others, the feeling of obligation, which motivates a person without being forced. “Intrinsic Taxpayers” are sensitive to institutional factors, as e.g., the behavior of governments or tax administrations. Positive actions by the state are intended to increase taxpayers’ positive attitudes and commitment to the tax system, tax-payment, and thus compliant behavior.

The way people are treated by the authorities affects their evaluations of authorities and their willingness to co-operate. They have a certain intrinsic motivation to pay taxes. However, if the intrinsic motivation is not recognized, intrinsic taxpayers get the feeling that they can as well be opportunistic. When monitoring and penalties for noncompliance increase, individuals notice that extrinsic motivation has increased, which on the other hand crowds out intrinsic motivation to comply with taxes (see, e.g., Frey 1997). Their willingness to co-operate does



not depend on the amount others contribute to the public good. Thus, they are not conditional regarding the others' contribution, but they depend on the institutional conditions under which they must pay their taxes.

### **2.3.3 Honest Taxpayer**

A third type of taxpayers is called "Honest Taxpayer". These taxpayers do not even search for ways to cheat at taxes. Their behavior does not respond to changes in the tax policy parameters, as taxes, fine rates, or audit frequency. Thus, their behavior is not subject to a marginal but rather an absolute evaluation (Frey 1997).

### **2.3.4. Tax Evaders**

At the other extreme, there are the "Tax Evaders". Relative price changes due to higher punishment or higher audit probability are considered. In general they have low tax morale. It can be argued that for these taxpayers the standard economic rational choice theory comes into play. They compare the expected value of evading taxes with the value of being honest.

## **2.4 Tax Compliance Cost**

Abdul-Jabbar and Pope (2008) define "tax compliance cost" as the cost incurred by taxpayers to fulfill their statutory tax obligations, over and above their actual tax liability. "Tax compliance costs", according to Smulders *et al* (2012), include monetary costs, time costs, psychological costs, and opportunity costs to taxpayers. In the literature the following types of costs have been identified:

- *Efficiency costs* (also called *social costs*) which refer to the cost of behaviour that is not optimal and result from the tax system (Evans, 2008:452). An example is taxpayers' altering their investment decisions as a result of tax concessions that give preferential treatment to certain activities.
- *Opportunity costs* which refer to the opportunities that a taxpayer might have lost for other benefits, with the money and time spent on complying with tax matters.

- *Monetary costs* refer to expenses incurred by taxpayers in respect of professional advisers and in order to equip them, or their employees, with sufficient knowledge to understand and comply with the tax laws.
- *Time costs* refers to the time taxpayers and their employees spend on tax compliance matters, such as filing returns, keeping records, etc.
- *Psychological costs* include the stress, anxiety, frustration and dissatisfaction suffered by taxpayers as a result of trying to comply with their tax obligations (Evans, 2008:451).

According to Smulders, *et al.* (2012) and with reference to businesses (rather than individuals as taxpayers) “tax compliance costs include **internal costs**,... that is, the cost of collecting, paying and accounting for tax on products or profits of the business, and on the wages and salaries of employees together with the costs of acquiring the knowledge to enable this work to be done; and **external costs**, mainly in the form of advisors costs – using professional tax service providers is one of the main costs contributing to the cost of complying with taxation legislation.”

## 2.5 Tax Compliance Benefits

Tax compliance does not entail only costs for the taxpayer. There are also tax compliance benefits which need to be considered. Literature on “tax compliance benefits” categorized these benefits into three broad categories, namely cash-flow benefits, managerial benefits, as well as tax deductibility benefits (Smulders *et al.*, 2012).

○ *Cash-flow benefits* are the benefits derived from the use of tax revenues for a period before they must be paid over to the revenue authority, such as property tax collected by banks or supermarkets, the deduction of “pay-as-you-earn tax” (PAYE) by employers and VAT by vendors, before these are paid over to the relevant revenue authority (Smulders *et al.*, 2012). A further example is the benefit from the lawful delay that arises when the income received by a taxpayer is not immediately or fully taxed on accrual or receipt.

○ *Managerial benefits* are the benefits that may arise due to a requirement in terms of tax legislation to maintain records, such as better recordkeeping, the use of technology, improved knowledge of the financial affairs of the business in particular in the form of increased

knowledge of their complex accounting information systems and improved business or managerial decisions (Smulders *et al.*, 2012).

o *Tax deductibility benefits* are the benefits that arise when the income tax system permits some tax compliance costs to be treated as a legitimate deduction for tax calculation purposes, for example where the tax system permits a business a deduction for the services of their tax practitioners and tax-related incidental expenses from their taxable income (Smulders, *et al.*, 2012).

## **2.6 Improving Tax Compliance**

As Bird (2003) correctly points out, “assessing the relation between administrative effort and revenue outcome is by no means a simple task”. Maximizing revenue is only one dimension of the task of tax administration. How that revenue is raised, in other words the effect and impact of the revenue-raising task in equity, the level of economic welfare as well as the political fortunes of governments, may be as important. Rather than simply looking at the amount of revenue raised, that is the level of collection, to measure the effectiveness or success of a tax administration, a more accurate measure would be to measure the so-called “compliance gap” which constitutes the gap between actual and potential revenues (Casanegra de Jantscher and Bird, 1992). There are a lot of efforts that has been made by different jurisdictions in order to improve the tax compliance behavior of tax payers and some of them are depicted below:-

### **2.6.1 Accountable and Transparent Administration**

A transparent and accountable tax administration that is service-oriented is likely to have a positive impact on public trust. If the revenue is furthermore properly spent in terms of a budget which the taxpayers find agreeable, compliance should increase.

### **2.6.2 Tax Amnesties**

Governments periodically offer those who have not fully complied with their tax obligations a period in which they can voluntarily correct past violations and not suffer the full penalties that such violations would normally entail. Although revenue is a key attraction of amnesties,

they are also sometimes used to address political goals, for example, as a measure to “put the past behind us in order to move forward” (Bird, 2003). On the whole, the evidence is clear that tax amnesties are seldom successful and should rather be avoided (Bird, 2003).

Tax amnesties are popular and therefore commonly encountered. They are especially attractive to politicians who regularly (and somewhat short-sightedly) view an “amnesty as a way to obtain revenue that was owed the government but would never have been collected without the amnesty” (Mikesell and Birskyte, 2007:1058).

Apart from the importance of careful design, a tax amnesty will only be effective if the taxpayer can be certain that the amount declared during the amnesty will not result in a future investigation of possible tax evasion in years not covered by the amnesty (Bird, 2003). Mikesell and Birskyte (2007) state that one-time amnesties may enhance voluntary taxpayer compliance during the amnesty period, but that typical tax amnesties are unlikely to generate significant amounts of new revenue in the long run. To be successful, an amnesty program must do more than simply offer relief for past violations. These authors conclude: “It must also change future behavior, both of the taxpayer and the government. If the likelihood of getting caught, and thus penalized, rises after the program, then taxpayers are more likely to take advantage of the temporary amnesty as a last chance opportunity. The design of a successful amnesty might combine mild treatment of the evaders upon the disclosure with a tougher expected enforcement regime.”

### **2.6.3 Incentives and Tax Concessions**

Tax incentives and concessions are often used as measures to enhance revenues and overall tax compliance. As Bird and Zolt (2003) point out – “many countries have sought to improve their economy by introducing a variety of tax incentives for investment, for savings, for exports, for employment, for regional development, and so on... Often, such incentives are redundant and ineffective, giving up revenue and complicating the fiscal system without achieving their stated objectives. Even to the extent that incentives may be effective in inducing investors to behave differently than they would have done in response to market

signals, the result is often distorting and inefficient, diverting scarce resources into less than optimal uses.”

Tax incentives result in inequity as they purposely cause very uneven tax burdens, with domestic companies often subject to full taxation, while foreign investors benefit from tax incentives that reduce their effective tax rates (Bird and Zolt, 2003). These authors further indicate that non-tax factors, such as a sound macroeconomic policy, good infrastructure and a stable governance system are more important factors than tax concessions. Although there may indeed be cases for some tax concessions, for example, to assist the small business sector, “these tax incentives should be well-designed, properly implemented, and periodically evaluated if they are to do more good than harm” (Bird and Zolt, 2003).

In an attempt to assist micro, small and medium-sized businesses to lower or minimize their tax compliance costs and reduce their tax burden, governments often provide these enterprises with a simplified tax regime and/or a variety of tax concessions (Smulders, *et al.*, 2012). These concessions can generally be classified into two main categories, namely –

- ❖ *positive concessions* that provide a lower rate of taxation, an exemption from paying tax or an accelerated tax deduction; and
- ❖ *relieving concessions* that excuse the taxpayer from requirements otherwise imposed, for example special registration thresholds for certain taxes (relieving taxpayers from complying with a tax), simplified accounting rules and longer accounting periods (e.g., for VAT purposes).

Positive concessions have a direct impact on the tax burden, resulting in a reduction in, or exemption from, tax liability. These concessions do not have a direct impact on tax compliance costs. These concessions are generally elective and subject to complex qualifying criteria and strict rules, which means they can be rather costly to understand and adopt (Smulders *et al.*, 2012). As complexity generally increases tax compliance costs (Bird and Zolt, 2003; Mikesell and Birskyte, 2007), complex tax concessions may ultimately and rather perversely, increase tax compliance costs.

Relieving concessions can indeed have a direct impact on the tax burden, particularly in the form of tax compliance costs. For instance, a specific tax registration threshold can preclude a business from registering for a particular tax. In some cases, registration thresholds can also arguably be regarded as positive concessions. This would occur when an exemption threshold results in an exemption both from having to pay the tax (a positive concession) and from having to comply with the obligations imposed by that tax (a relieving concession). If an exemption threshold merely relieves the taxpayer from having to comply with administrative compliance requirements, but does not provide tax exemption, it would be regarded as a relieving provision only. A reduction in the number of tax payments that need to be made, constitute a real concession. It could result in less time – whether internal and/or external – being spent on a particular tax compliance obligation, which ultimately leads to a reduction of tax compliance cost (Smulders *et al.*, 2012).

Some jurisdictions have hoped to enhance revenues and voluntary compliance by granting taxpayers a discount for early payment (McCluskey and Franzsen, forthcoming). If it is not backed up with proper enforcement, it is not likely to be successful. The honest taxpayers who have been paying in the past will benefit from the discount, and the tax evaders will still evade the tax. The simple lesson is that incentives and concessions, as is the case with amnesties, must be properly designed to ensure that only those who are meant to benefit, actually benefit from the preferential treatment.

Too much political and/or administrative discretion to grant exemptions or other forms of tax relief should also be avoided. These quickly erode the tax base and if tax rates are not increased to recoup the revenue loss from the remaining taxpayers, which is seldom an acceptable (political) option, the inevitable result is a decrease in tax revenues.

Discouraging non-compliance is only one aspect of improving compliance (Bird, 2003). Treating taxpayers in a professional manner, in other words, more like customers rather than like suspects or thieves, may do much more to promote and improve compliance (Bird, 2003; Mikesell and Birskyte, 2007; Wang, 2010). Providing taxpayers with various payment options (e.g. banks, supermarkets, internet, ward offices), easy filing, and assistance (e.g. on-line or at shopping malls and sports stadiums) not only reduces actual compliance costs, but can reduce

unintentional non-compliance. A professional and effective service-oriented tax administration is crucial for improving tax compliance.

## **2.7 Factors Determining Tax Compliance Behavior**

Fischer et al. (1992) stated there are four basic factors that determine tax compliance behavior in his expanded model (Fischer Model). i.e., (i) demographic (e.g. - age, gender and education) (ii) noncompliance opportunity (e.g. income level, income source and occupation), (iii) attitudes and perceptions (e.g. fairness of the tax system and peer influence) and (iv) tax System/structure (e.g. complexity of the tax system, probability of detection and penalties and tax rates).

### **2.7.1 Demographic factors**

The relationship between demographic variables and tax compliance has long been of interest (Tittle, 1980). Three major personal characteristics for which there is evidence of a relationship are age, gender, and education (Jackson and Milliron, 1986). The Fischer model suggests that demographic variables indirectly affect taxpayer compliance by their impacts on noncompliance opportunities and attitudes and perceptions. There is a positive link between age and taxpayer compliance is reported (Jackson and Milliron, 1986). Generally they pointed out young taxpayers are more willing to take risks and are less sensitive to sanctions as well as age is a factor for intentional evaders, with younger taxpayers less complaint. In addition noncompliance is significantly less common and of lower magnitude among householders in which either the head or the heads spouse is over age of 65.

Early research (Tittle, 1980) testing the tax compliance level of males versus females reports that females are more likely to tax compliance. Traditionally “females identified with conforming roles, moral restraints, and more conservative life patterns” (Jackson and Milliron, 1986). All these attributes may promote higher tax compliance. Education, as a demographic variable relates to the taxpayers ability to comprehend and comply or not comply with the tax laws (Groenland and Veldhoven, 1983). Two aspects of education distinguished: “the general degree of fiscal knowledge and the degree of knowledge involving

evasion opportunities” (Jackson and Milliron, 1986). They find that those with more fiscal knowledge had more positive tax ethics scores than those with lower fiscal knowledge.

### **2.7.2 Non-compliance opportunity**

In the Fischer model, noncompliance opportunity can affect taxpayer compliance directly through income level, income source, and occupation. Almost all the theoretical model indicates that as income rises, tax evasions should increase over most ranges (Andreoni et al., 1998). In other way, the lower income group tends to have a lower proportion of tax compliance by under-reporting income and by over-claiming expenses than their counterparts in the higher income group. Taxpayers vary in terms of the opportunities available to them to overstating expenses and understating incomes. Greater tax noncompliance opportunity is generally resulted from self-employment and income sources not subject to withholding taxes. Sutherland (1949) point out that tax evasion considered as a white-collar crime, committed by an individual of respectability and high social status in the course of performing his employment. In addition, almost all sole proprietors those who engaged in sales from fixed locations (car dealerships, stores, restaurants etc) understated taxes by the greatest percentage.

### **2.7.3 Attitudes and perceptions**

The Fischer model suggests two major considerations for altering taxpayer's attitudes and perceptions to tax compliance are the fairness of the tax system and peer influence. Richardson (2006) it is widely believed by tax administrators and the taxpayers that growing dissatisfaction with the fairness of tax system is the major causes for increasing tax noncompliance. As well as Grasmick and Scott (1982) indicate that respondents with peers who practice tax noncompliance are more likely to commit as well.

### **2.7.4 Tax System/structure**

It is widely acknowledged that the extent of tax compliance in many developing countries has been decreasing. The underdeveloped tax system/structure is one of the major causes for this phenomenon. In the Fischer Model the effectiveness of tax system affected by complexity of tax system, probability of detection, and penalties and tax rates. As the tax law has become



increasingly complex, complexity has come to recognize as a possible reason for tax noncompliance (Jackson and Milliron, 1986). In the context of tax compliance decisions, complexity should include two dimensions, excessive detail in the tax rules and numerous computations required. In addition, if there is a higher audit probabilities and severe penalties encourage tax compliance. The third major construct of tax system/structure in the Fischer model is tax rates; which reveal that the probability of underreporting and the level of underreporting are positively related to the marginal tax rates.

### **2.7.5 Socio-economic and psychological factors**

Culture considered as one of a powerful environmental factor that affects the taxpayer's compliance. Different social norms and ethical values will create different incentives for tax compliance. These cultural differences may have a direct impact on ethical values and moral development and ultimately affecting tax compliance decisions (Chan et al, 2000). In general, the author has adopted the following charts after critically assessing the factors which is going to affect the tax compliance behaviors of business profit tax payers.

## **2.8 Relationships between Tax Compliance, Tax Morale and Tax Attitudes**

### **2.8.1 Tax Payers Attitudes and Compliance**

According to Ajzen's (1991) Theory of Planned Behavior, attitude relates to one's own personal views about a behavior. Attitude may also be defined as positive or negative views of an "attitude object"; i.e. a person, behavior or event. Mowen (1987) in his book entitled *Consumer Behavior*, defined attitudes as consisting of the following:-

- Attitudes are likes and dislikes.
- The "major characteristics that distinguish attitude from other concepts are its evaluative or affective nature".
- Attitudes are the core of our likes and dislikes for a certain people, groups, situation, object and intangible ideas.

In relation to taxation, taxpayers' attitudes may be defined as positive or negative views of tax compliance behavior. The outcome of positive views is tax compliance and negative views are tax non compliance. These views may be explained by Psychology-based theories which reveal that taxpayers' attitude may be influenced by the following factors which eventually influence taxpayers' behavior.

Individual attitudes toward compliance have been shown to be a function of social and cultural norms. If such attitudes would carry over to actual compliance, enhancing these norms, as through increasing overall trust in government, is a desirable policy instrument to complement the usual enforcement options. The attitude of taxpayers varies considerably. Some comply with the fullest extent required, irrespective of whether the IR is actively auditing them or their industry. Other taxpayers essentially play the audit lottery and either do not prepare contemporaneous documentation or prepare the absolute minimum with the hope of avoiding the imposition of penalties.

An individual's attitude towards tax system may predict (his tax compliance behavior). Theoretically, attitude is a partial indication of behavior. Attitude towards an event, object, function or person may be favorable or unfavorable. According to Ajzen (1991) and Fishbein and Ajzen (1975), individual evaluates an event or object positively or negatively and positive and negative evaluation is the main dominant characteristic of an individual's attitude.

The payment of tax is obligatory duty of every citizen whether natural or corporate citizen. As a civic duty, it is expected that citizens will voluntarily comply with such obligation but that is not the case with some citizens. Studies have established relationship between attitudes of taxpayers and compliance. The study of Eriksen and Fallan (1996) revealed that taxpayer's attitude towards tax system has influence on reinforced desire toward tax evasion and compliance.

The study of Oriviska and Hudson (2002) examined the attitudes to tax evasion and reported that evasion is condoned by large number of people who are particularly benefiting from it. Eriksen and Fallan (1996) said that dimensions of attitude towards tax evasion include:

attitude to one's own tax evasion which is referred to as tax ethic, fairness of tax system, attitude to other people's tax evasion and attitude to general crime (Alabede et al., 2011).

## **2.8.2 Tax Morale and Attitudes**

Tax morale, unlike tax evasion, measures not individual *behavior* but individual *attitude*. Tax morale which is not a new notion but has received surprisingly little attention in the tax compliance literature—can be defined as a moral obligation to pay taxes, a belief in contributing to society by paying taxes. (Schmölders, 1970; Strümpel, 1969) tried to bridge economics and social psychology by emphasizing that economic phenomenon should be analyzed from a perspective larger than the traditional neoclassical point of view (e.g., Lewis, 1979, 1982). Tax morale is also closely linked to what have been termed *taxpayer ethics*, “the norms of behavior governing citizens as taxpayers in their relationship with the government” (Song and Yarbrough, 1978: 443).

A later empirical analysis found that, compared to other variables, tax morale had the strongest significant impact on the size of the shadow economy (Weck, 1983). Torgler (2003a) also found that tax morale significantly reduced tax evasion. However, these two studies also treated tax morale as an exogenous residual. Thus, much extant research treats tax morale as a black box or residuum rather than analyzing the factors that shape or maintain it (Feld and Frey, 2002a).

## **2.9 A review of Ethiopian tax system**

At the present time payment of taxes is obligatory in all civilized nations; where the rate or imposition is at all dependent upon the taxpayer, the tax takes the form of a fee or payment for contractual services. The working law on income taxation in Ethiopia, the Income Tax Proclamation No. 286/2002, has classified sources of income into four schedules. Therefore, income taxation in the country is undertaken based on these schedules, which have been systematically classified as Schedule A (employment), Schedule B (rental of building), Schedule C (income earned from business) and Schedule D (not categorized in any of the three). However, our major concern under this topic is on Schedule C type of the tax system.

Schedule C type of tax system further divided in to three sub category such as category A, B and C.

### **Category “A” taxpayers**

Category “A” taxpayers are composed of two groups. The first group comprises of those taxpayers whose annual turnover for a single tax year is 500,000 or more. In addition, any company incorporated under the laws of Ethiopia is a category “A” taxpayer irrespective of their annual turnover. The rationale for incorporating companies under category “A” irrespective of their annual turnover seems to dwell upon the idea that given the present local and international business environment by the time companies are established they must have at least 500,000 as a starting capital. Category “A” taxpayers are required to keep books and accounts.

### **Category “B” Taxpayers**

Category “B” taxpayers are those taxpayers with annual turnover greater than 100,000 but less than 500,000 Ethiopian Birr. Like category “A” taxpayers’, category “B” taxpayers are also required to keep proper books and accounts. Nevertheless, the books and accounts to be kept by category B taxpayers are less complicated compared to category ‘A’ taxpayers. Thus, they are required to keep an account incorporating mainly profit and loss statements for the particular year. Their income tax liability will be assessed based on the books and accounts kept by the taxpayers. The same administrative penalties apply if Category “B” taxpayers fail to keep books and accounts.

### **Category C taxpayers**

Category “C” is the third and the last category. Small businesses are the main types of businesses incorporated in this category .All taxpayers with annual turnover income less than 100,000 Ethiopian Birr are grouped as category C taxpayers. These categories of taxpayers are not required to keep books and accounts. Their income tax liability will be determined through a special procedure known as presumptive taxation. They are required to pay an

income tax from their incomes they generate based on the schedules attached at the back of the income tax regulation.

## **2.10 A review of empirical studies**

The tax compliance literature has provided evidence suggesting that compliance is influenced by numerous factors. Scholars identified these factors as economic, social and psychological Kirchler (2007). To mitigate the challenge of tax non-compliance, it is necessary to understand factors influencing an individual's decision to comply with tax laws.

According to Kirchler (2007), tax compliance determinants are classified in to four categories. The four categories are 1) economic factors (tax rates, tax audits and perceptions of government spending); 2) institutional factors (the role of the tax authority, simplicity of the tax returns and administration and probability of detection); 3) social factors (ethics and attitude, perceptions of equity and fairness, political affiliation and changes on current government policy, referent groups); and 4) individual factors (personal financial constraints, awareness of offences and of penalties).

Tadesse Getachew et.al (2014) attempted to reveal determinants of taxpayers' compliance with the tax system. This study examined nine tax compliance determinants; the examined tax compliance determinants were: probability of being audited; perception of government spending; perception of equity and fairness; penalty, financial constraint; changes to current government policies; referral group; the role of the tax authority; and tax knowledge. This study used a cross-sectional survey method of research design. Given the scaled ranking information of the dependent variable (tax compliance), an ordered probit was applied to examine determinants of tax compliance in Mekelle city, Ethiopia. The study indicates that tax compliance was influenced by the probability of being audited, financial constraints, and changes in government policy.

In additions to this, Mohd Rizal Palil(2010) study also focuses on the level of individual Malaysian taxpayers' knowledge and explores how tax knowledge levels influence tax compliance behavior in a new SAS. The results suggested that tax knowledge has a significant impact on tax compliance even though the level of tax knowledge varies significantly among

respondents. The results also indicate that tax compliance is influenced specifically by probability of being audited, perceptions of government spending, penalties, personal financial constraints, and the influence of referent groups. To test the hypotheses, the data was analyzed using multiple regressions (Ordinary Least Squares (OLS)). Two measurements of tax compliance behavior were tested (direct and hypothetical questions).

Furthermore, Merima Ali et.al (2013) examined the extent to which the different theories of taxpayer compliance such as economic deterrence, Fiscal Exchange, Non-state Actors as Service Providers, Social Influence, Comparative Treatment and Political Legitimacy and Knowledge about Taxes has to contribute to explaining people's attitude towards taxation. In order to capture factors that correlate with tax compliance attitude.

Benno Torgler (2003) found a model validating the influence of detection, number of tax auditors per taxpayer, penalty tax rate, individual tax rate, income class of a taxpayer and trust in the government and confidence in the courts and the legal system on the tax moral . To investigate the impacts of those variables on the tax moral; the author has been controlled the influences of age, gender, education, marital status, employment status.

Frey and Feld (2002) also argue that tax morale is supported or even raised when tax officials treat taxpayers with respect and on the other hand is reduced when the administration considers taxpayers as individuals who have to be *forced* to pay the taxes: "The feeling of being controlled in a negative way, and being suspected of tax cheating, tends to crowd out the intrinsic motivation to act as an honorable taxpayer and, as a consequence, tax morale will fall. In contrast, if the tax official makes an effort to find out the reason for the error by contacting the taxpayer in an informal way (e.g. by phoning him or her), the taxpayer will appreciate this respectful treatment and tax morale will be upheld". They divide respectful treatment into two components: (i) transparent and clear procedure by the tax administration, (ii) as a direct personal component, how the taxpayers' character is respected by tax administrators. Their empirical analysis shows that a respectful treatment of taxpayers by the tax administration reduces tax evasion.

Other than this, Mohd Rizal Palil et.al (2013) also attempted to reveal the determinants of tax compliance in Malaysia in a self-assessment system (SAS) with special emphasis on individual taxpayers. Four tax compliance determinants are examined: the probability of being audited; the perception of government spending; tax rates; and the role of the tax authority.

Allingham and Sandmo (1972) were the first researchers to conduct empirical analysis into compliance behaviour of taxpayers and they came up with a model which became known as A- S model. In the model, the compliance decision of taxpayers is considered to be affected by income of the taxpayer, tax rate, probability of audit, and fine rate. However, factors influencing compliance behaviour of taxpayers are far more numerous than suggested in the A-S model (Alm, 1991; Jackson & Millron, 1986). Therefore, the authors underplayed the influence of psychological and social factors including the demographic characteristics on taxpayers' behaviour.

Subsequently, in a comprehensive review study, Jackson and Millron (1986) came up with fourteen key determinants for tax compliance and these determinants were later categorized into four group determinants in the study of Fischer, Wartick and Mark (1992) and became known as Fischer's model of tax compliance. Demographic variables are within one of these groups of determinants. The demographic factors in Fischer's model include gender, age, education, and income level and employment status.

As per a recent study on tax compliance in the business sector in South Africa, Wang (2010) concluded that, generally, taxpayers' decisions to comply (or not comply) are determined by the following direct factors:

- The complexity of the tax system (Mikesell and Birskyte, 2007);
- Taxpayers' confidence in government generally, but more specifically government service provision and the cost-effectiveness of the provision of public goods and services, as well as the level of fraud and corruption within government;
- Taxpayers' perception regarding the fairness of the entire tax system;
- The social setting and societal norms; and
- The effectiveness of tax authorities in detection and punishment of non-compliance.

In general, by adopting a deductive approach on the review of the literature the following section presents conclusions and knowledge gaps.

## 2.11 Conclusions and knowledge gaps

This chapter describes the relevant theories and factors that form the background of this study. Based on the discussion, tax payers' tax compliance behaviour have been affected by different factors and all of them are categorized in to four broad groups such as demographic factors, non-compliance opportunities, attitudes and perceptions and tax system or structure. A review of past studies on tax compliance behaviour indicates mixed but interesting findings. Tax compliance has been an important subject of research in a large number of developed and a number of developing countries. Since each country has its own approach to managing tax compliance levels and each has different tax laws and regulations, the factors impacting tax compliance behaviour appear to vary among countries.

The Ethiopian government had developed a five year Growth and Transformation Plan and has been working hard to achieve the planned economic growth of the country. In the GTP, the government clearly stated that efforts will be geared towards promoting compliance and equipping tax collection institutions with adequate enforcement power which will further boost revenue mobilization at federal and regional levels. As a result, assessing factors which determines tax compliance behaviour of businesses such as tax knowledge, fairness in the tax system, confidence in government spending, detections and punishments, the influence of peer groups and income level of taxpayers has to be investigated in order to increase the income earning capability of the government and to improve the business environment by encouraging voluntary compliance. In additions to this, many research's have not been made on the tax compliance behaviour of business operating in Addis Ababa city administration. This gap leads to the main research question of the thesis. *Why business profit tax payers comply with the tax legislations while the benefits of non-compliance is outweighing?* The following chapter provides details of the research method in respect of the identified research problems.



## 2.12 Conceptual framework of the study

From the aforementioned literature review part of the paper, the author had adopted (i.e. Fisher et.al 1992) the following conceptual frameworks for the study.

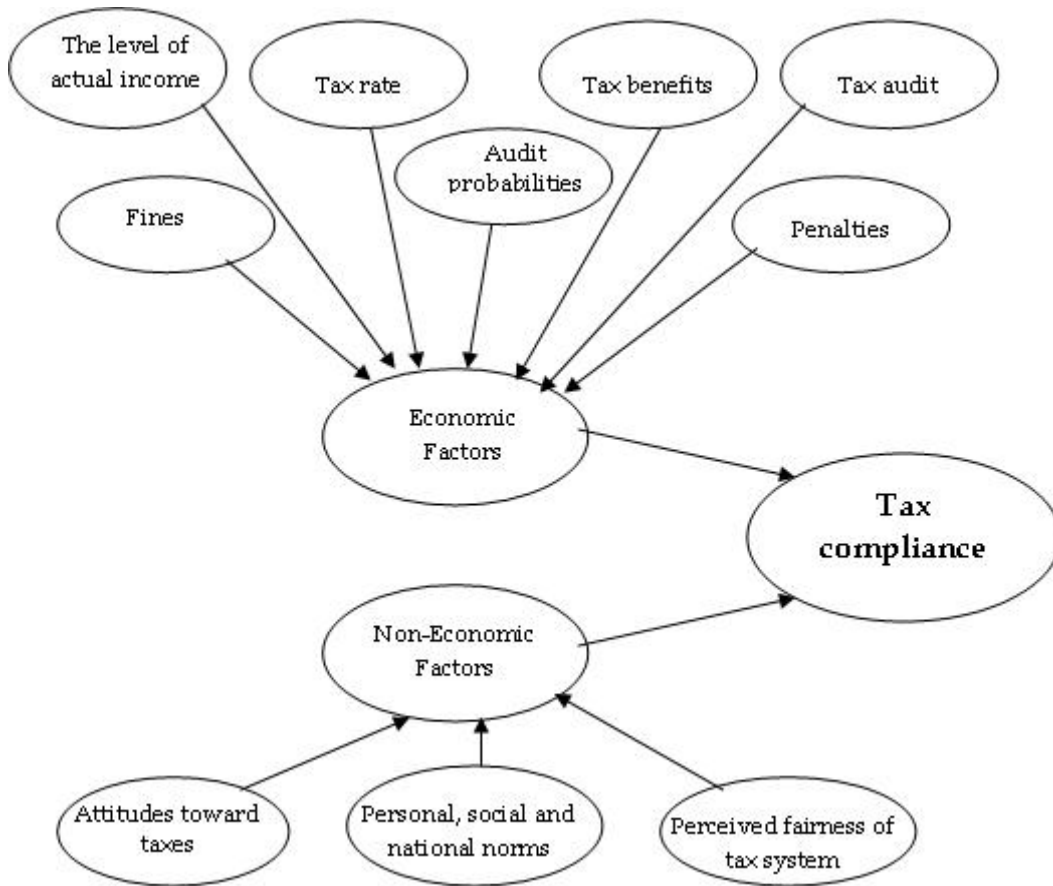


Figure 1- Economic and non-economic factors for tax compliance

## Chapter 3: Research Design

The purpose of this chapter is to present the research question and hypotheses, the underlying principles of research methodology and the choice of the appropriate research method for the thesis. This chapter has been arranged as follows: Section 3.1 presents the hypotheses and research question for the thesis. Section 3.2 presents the research approaches. This is followed by the philosophy of quantitative (section 3.2.1), qualitative (section 3.2.2), and mixed methods (along with discussion of the choice of the appropriate method for the current research) (section 3.2.3) approaches. Then, the research methods adopted in this study has been presented in section 3.3. Finally, conclusion and the relationship between research question and hypotheses, and sources of data are presented in section 3.4.

### 3.1 Hypotheses and research question

As presented in chapter 1, the broad objective of these theses is to assess factors affecting tax compliance behavior of businesses operating in Addis Ababa City administration. As per the literature, taxpayers tax compliance behaviors have been affected by both intrinsic and extrinsic factors. Therefore, the very purpose of this paper is to test those factors by applying in Addis Ababa city administrations business profit tax payers. In regard with these assumptions, the author had developed one research question and six hypotheses.

***1) Why business profit taxpayers comply with the tax legislations while the benefits of non-compliance is outweighing?***

Citizens are obliged to make financial contribution in the form of tax payment to the government. Apart from representing important sources of revenue to the government of most countries, taxation is a useful fiscal tool for stabilizing national economy as well as redistributing the national wealth. However, taxation can only perform these important functions efficiently where taxpayers are willing to comply with tax laws of a country. But it is widely acknowledged that some people do not like paying taxes and because of this reason, some portion of the taxpayers may fail to comply with a country's tax laws. Tax noncompliance is the failure of taxpayer to meet tax obligations whether the act is done

intentionally or unintentionally and this may occur through failure to file tax returns, misreporting taxable income or misreporting of allowable subtractions from taxable income or tax due such as exemptions, deductions, tax credit etc (Kirchler, 2007).

The most obvious consequence of tax noncompliance is the loss of tax revenue to government and this limits funds for execution of projects (Frazoni, 2000; Wenzel, 2005). In addition, tax noncompliance creates inequality among the people because both horizontal and vertical equity are affected (Fjeldstad & Semboja, 2001). Tax noncompliance is a universal phenomena hindering efficient tax revenue productivity in both developing and developed countries. These non-compliance behaviors have been emanated from individual intrinsic and extrinsic motives. Therefore, the research questions has been drawn in order to assess the behavioral aspect of the taxpayers' with the intentions of identifying the factors *why business profit tax payers comply with the tax legislations while the benefits of non-compliance is outweighing?* Based on the research questions highlighted, the author has developed the following hypothesis in order to test tax payers' tax compliance behavior:-

***Hypothesis 1: Tax knowledge (demographic factor) affects the taxpaying attitudes of business profit taxpayers.***

The influence of knowledge on compliance behavior has been proven in various researches Mohamad Ali *et al* (2007). Harris (1989) divided tax knowledge into two aspects, namely, knowledge through common or formal education received as a matter of course and knowledge specifically directed at possible opportunities to evade tax. In the first case, the level of education received by taxpayers is an important factor that contributes to the general understanding about taxation especially regarding the laws and regulations of taxation Eriksen and Fallan (1996). Given evidence that tax knowledge affects understanding of taxpayers, an obvious explanation that has been raised by previous researchers e.g. Singh, (2003), Eriksen and Fallan, (1996) Harris (1989) is whether enhancement of tax knowledge will increase tax compliance. Eriksen and Fallan (1996 p387) claimed that 'knowledge about tax law is assumed to be important for preferences and attitudes towards taxation.

There is little research that explicitly considers how attitude towards taxation is influenced by specific knowledge of tax regulations'. The research done by Eriksen and Fallan has illustrated the importance of tax education in a tax system. They suggested that fiscal knowledge correlates with attitudes towards taxation and tax behavior can be improved by a better understanding of tax laws.

Eriksen and Fallan's study is divided into three main parts. Firstly, the investigation is focused on taxpayers' knowledge. Secondly, the research tries to reveal the overall impact of tax knowledge on tax compliance behavior among individual taxpayers and thirdly, the research involves tax agents in order to determine their influence in determining taxpayers' behavior, tax agents are assumed to be involved more in preparing, declaring and calculating tax liability on behalf of individual taxpayers than in the directly assessed system.

Eriksen and Fallan (1996) attempted to determine the relationship between the level of tax knowledge and attitudes toward taxation; whether specific tax knowledge influences attitudes in general (not only tax attitudes) and investigate people's behavior toward traditional crime. The results of the study suggested that tax knowledge has a positive correlation with perceptions of fairness, tax ethics and attitudes to others' tax evasion. Therefore, this study aims at understanding the overall impact of tax knowledge's on tax compliance behaviors of business profit tax payers operating in Addis Ababa city administrations.

***Hypothesis 2: Belief in fairness (attitude & perception factor) affects the tax compliance behavior of business profit tax payers.***

As mentioned by Smith (1776), one of the main principles of the taxation system design is equity or fairness, which can be perceived via two-dimensional views –horizontal equity (people with the same income or wealth brackets should pay the same amount of taxes) and vertical equity (taxes paid increase with the amount of the tax base). The driving principle behind vertical equity is the notion that those who are more able to pay taxes should contribute more than those who are not. Wenzel (2003) suggested three areas of fairness from the taxpayers' point of view (social psychology): 1) distributive justice (viewed as the exchange of resources i.e. benefit and cost); 2) procedural justice (viewed as the process of

resource distribution) and 3) retributive justice (viewed as the appropriateness of sanctions when norm-breaking occurs).

1. In **distributive justice**, an individual is concerned about the fairness of their actions, and wants to be treated in relation to his merits, efforts and needs Kirchler *et. al*, (2008). If he feels that his tax burden is higher than other people within the same income group, his tax compliance probably decreases more widely at group levels; taxpayers want a fair treatment of their group relative to other income groups. If a specific group perceives that their tax liability is higher than other groups, then tax evasion might occur among the group members Spicer and Becker (1980). At a society-wide level, tax compliance is less likely if the perception is held that the tax system is unfair; wide scale tax evasion is likely to occur. Allingham and Sandmo (1972); in contrast, if the society perceives that the tax system is equitable and fair, voluntary compliance is expected to increase.
2. With regard to **procedural justice**, the main elements for perceived fairness are neutrality of procedures used, trustworthiness of the tax authorities, and the polite, dignified, and respectful treatment of taxpayers as individuals or groups. Taxpayers expect that tax authorities will provide sufficient information about the tax law and regulations so that they can complete their tax return as accurately as possible. It is argued therefore that increased information about tax law and regulations can increase fairness perception and compliance.
3. **Retributive justice**, unreasonable and intrusive audits and unfair penalties lead to stressful and dissatisfied taxpayers Spicer and Lundsted (1976). Unfavourable retributive justice perceptions could lead to non-compliant behaviour and consequently increase tax evasion and inflate the tax gap.

As can be seen from the above literatures compliance behavior of Addis Ababa city administration business profit tax payers have been affected by the belief of **distributive justice, procedural justice and Retributive justice**.

***Hypothesis 3: Influences of the peer groups (attitudes & perception) affects the tax compliance behavior of business profit tax payers.***

Both psychologists and economists believe that individuals conform to social norms established by peers. First, individuals can incur a high psychological cost (e.g. feelings of guilt, loss of self-respect) in undertaking an undesirable action when other individuals are inclined to follow the norm of truthful reporting. People tend to feel worse as the proportion of others in one's reference group who respect the norm increases. Fischer and Huddart (2008) show how 'established norms' or 'peer pressure' can influence an individual's desirable actions, because agents occur at a personal cost in not following their peers. A second reason is that agents gain information from peers' behavior and form an accurate interpretation of reality and behave accordingly. According to these views, much of one's behavior is influenced by one's perceptions of what is 'typical' or considered to be 'normal'. This suggests that when other people behave honestly, such behavior will be followed. Yet, if the number of transgressors grows, the incentive to comply can dwindle. Jackson and Milliron (1989) find that highly non-compliant peers reduce the compliance of other taxpayers. As mentioned, people respond to norms to gain an accurate understanding of how to respond effectively to social situations, especially during times of uncertainty. This shows that individuals take norms as a source of information to shape reality and as a guide to correct behavior.

According to Lindbeck 1995, conformity to a social norm is conditional on whether there is need to form expectations about other people's behavior and beliefs. We argue that individuals are affected in their compliance behavior by the behavior of their "neighbors", or those about whom they may have information, whom they may know, or with whom they may interact on a regular basis. Individuals seem more likely to file and to report their taxes when they believe that other individuals are also filing and reporting their taxes; conversely, when individuals believe that others are cheating on their taxes, they may well become cheaters themselves.

As can be tested by different authors in different countries, tax compliance behavior of business profit tax payers' have been affected by the influence of peer groups but researches

have not been made so far in the case of Ethiopia. Therefore, the paper validates those issues in the case of Addis Ababa city administration business profit tax payers.

***Hypothesis 4: Income level of tax payers (non-compliance opportunity) does have positive and significant impact on the tax compliance behaviors of business profit tax payers.***

In Fischer's model, source of income, level of income and occupation are considered as factors providing opportunity for tax noncompliance. Empirically, studies have proof the relationship between noncompliance opportunity factors and tax compliance behavior. Similarly, Manaf, Hasseldine, & Hodges (2005) found that middle-income taxpayers are more compliant. Concerning source of income, Fjeldstad and Semboja (2001) also observed that employees paying their taxes through a withholding system have fewer opportunities to be noncompliant. In another study, Richardson (2006) found that income source is significantly related to tax evasion. In respect of occupation, Andreoni et al. (1998) noted that there was an understatement of taxes by a greater percentage by sole proprietors. In contrast, Manaf et al. (2005) showed sole proprietors are likely to be more compliant. Therefore, the very purpose of this paper is to test the impact of the income level of tax payers' in affecting the tax compliance behavior of business profit tax payers operating in Addis Ababa city administration.

***Hypothesis 5: Feeling of Detection and punishments (tax system/structure) does have an impact on the tax compliance behaviors of business profit tax payers.***

The basic theoretical model used in nearly all research on tax compliance begins with the economics-of-crime model of Becker (1968), first applied to tax compliance by Allingham and Sandmo (1972). Here a rational individual is viewed as maximizing the expected utility of the tax evasion gamble, weighing the benefits of successful cheating against the risky prospect of detection and punishment, and the individual pays taxes because he or she is afraid of getting caught and penalized if he or she does not report all income.

This approach gives the plausible and productive result that compliance depends upon audit rates and fine rates. Indeed, the central point of this approach is that an individual pays taxes because of this fear of detection and punishment. The obvious implication for designing

strategies to reduce tax evasion is to increase enforcement. This economics-of-crime approach therefore gives the sensible result that compliance depends upon the enforcement policies of a tax administration. However, it is essential to recognize that this approach also concludes that an individual pays taxes because – and *only* because – of the economic consequences of detection and punishment. Again, this is a plausible and productive insight, with the obvious implication that the government can encourage greater tax compliance by increasing the audit and the penalty rates of its regulatory regime.

The many extensions of this economics-of-crime approach considerably complicate the theoretical analyses, and generally render clear-cut analytical results impossible. Nevertheless, these extensions retain the basic approach and the basic result: individuals focus exclusively on the financial incentives of the evasion gamble, and individuals pay taxes solely because they fear detection and punishment. However, it is clear to many observers that compliance cannot be explained entirely by such purely financial considerations, especially those generated by the level of regulatory enforcement. The percentage of individual income tax returns that are subject to a thorough tax audit is generally quite small in most countries, almost always well less than 1 percent of all returns. Similarly, the penalty on even fraudulent evasion seldom exceeds more than the amount of unpaid taxes, and these penalties are infrequently imposed; civil penalties on non-fraudulent evasion are even smaller. However, even in the least compliant countries evasion never rises to levels predicted by a purely economic analysis, and in fact there are often substantial numbers of individuals who apparently pay all (or most) of their taxes all (or most) of the time, regardless of the financial incentives they face from the enforcement regime. However, researches have not been made so far in the case of Ethiopia validating why businesses pay their taxes i.e. is it because of fear of detection or punishment? Is it because of moral values? Or the benefits to be received from the government spending and etc. Therefore this paper assesses those issues one by one by distributing an appropriate questionnaire.



*Hypothesis 6: Tax payers' confidence in government spending (tax system/structure) significantly affects tax compliance behavior of business profit taxpayers.*

Studies on the relationship between the specifics of actual government spending and tax compliance, particularly on tax evasion, are very limited. Logically, taxpayers, and especially those who pay high amounts of tax, will be sensitive to what the government spends their money on. Although there is limited empirical evidence, it is reasonable to assume that taxpayers will tend to evade tax if they perceive that the government spends tax money unwisely.

Lewis (1982) suggests that attitudes should be examined for the degree to which they are a product of myth and misperception. He argued that when myths and misperceptions are replaced by knowledge, a change in attitudes towards taxation would occur even if the taxpayers' basic ideology and values remain unchanged and the tax law is unchanged. He also claimed that misperception probably plays a major role shaping fairness evaluations. Meanwhile, Roberts, Hite and Bradley (1994) also suggest that attitude to one's own tax evasion (tax ethics), and attitude to other people's tax evasion are important. If the government is wisely spending the national revenue, for example for basic facilities like education, health and safety and public transportation, it is likely that voluntary compliance will increase. In contrast, if taxpayers perceive that the government is spending too much on something considered unnecessary or unbeneficial to them then taxpayers will feel betrayed and attempt to evade. Therefore, this paper tested the relationship between the government spending and tax compliance behavior in the case of Addis Ababa city administration.

## **3.2 Research Approaches**

Identifying the research approaches and discussing the rationale for choosing a specific research approach is a priority for conducting a research topic. In additions to this, identifying the researcher's beliefs and world views is also a pre-requisite in undertaking a research. Therefore, based on these assumptions the two extremely contradicting paradigms are positivism and constructivism. Thus, positivist researchers normally adopt quantitative methods and constructivist researchers adopt qualitative methods. The other paradigm is

combination of positivism and constructivism (that is mixed method). Thus, this section incorporates the philosophy of quantitative, qualitative and mixed methods approaches.

### **3.2.1 Quantitative Research Approach**

Creswell (2003) noted that quantitative research is one in which the investigator primarily uses positivist claims for developing knowledge. The positivism approach views that the world as objective realism and therefore suggested that knowledge created by deductive reasoning where by a precise and systematic process is adopted (McKerchar, 2010). Besides quantitative research is to develop and employ mathematical models, theories, and hypotheses pertaining to natural phenomena. The process of measurement is central to quantitative research because it provides the fundamental connection between empirical observation and mathematical expression of an attribute. i.e., in this approach, the research problem translated to specific variables and hypotheses. In this approach a researcher uses a theory which is an interrelated set of constructs (or variables) formed into propositions, or hypotheses, that specify the relationship among variables (typically in terms of magnitude or direction).

The systematic view might be an argument, a discussion, or a rationale, and it helps to explain (or predict) phenomena that occur in the world. Labovitz and Hagedorn (1971) add to this definition the idea of a theoretical rationale, which they define as “specifying how and why the variables and relational statements are interrelated” (p.17). Why would an independent variable, X, influence or affect a dependent variable, Y? The theory would provide the explanation for this expectation or prediction. Quantitative research favor methods such as experiments and surveys, and will attempt to test hypotheses or statements with a view to infer from the particular to the general.

This approach typically concentrates on measuring or counting and involves collecting and analyzing numerical data and applying statistical tests. Well-formulated quantitative research has a significant contribution of generalizing of the broader population. This leads to consistent procedures in sample selection, instrument design, implementation, and analysis. However, this approach does have its own setbacks and appears that there is a flexibility problem in design, which may be vital when additional information revealed through data

collection needs further exploration for knowledge. Therefore quantitative research approach alone may not bring effective result in interpretive and exploration of research problems.

### **3.2.2 Qualitative Research Approach**

Qualitative research is a means for exploring and understanding the meaning individuals or group ascribe to a social or human problem (Cresswell 2008). A qualitative approach is one in which the inquirer often makes knowledge claims based primarily on constructivist perspectives (i.e., the multiple meanings of individual experiences meanings socially and historically constructed, with an intent of developing a theory or pattern) or advocacy/participatory perspectives (i.e., political, issue-oriented, collaborative, or change oriented) or both.

It also uses strategies of inquiry such as narratives, phenomenology's, ethnographies, grounded theory studies, or case studies. The researcher collects open-ended, emerging data with the primary intent of developing themes from the data. Qualitative research is exploratory in its nature because of this in qualitative research approach there are description and inductive discovery of evolving theory that may arise after data is collected. Qualitative research design has also its own setbacks because it doesn't produce data that allow comparison; the methodological approach does not ensure objectivity, and hence the quality of the findings is questionable and the research structure and procedure do not ensure the validity and reliability of methods.

### **3.2.3 Mixed Research Approach**

These procedures developed in response to a need to clarify the intent of mixing quantitative and qualitative data in a single study (or a program of study). With the inclusion of multiple methods of data and multiple forms of analysis, the complexity of these design calls for more explicit procedures. These procedures also developed in part to meet the need to help researchers create understandable designs out of complex data and analyses. This inquiry paradigm lies between positivism and constructivism known as critical realism and pragmatism.

Researchers adopting these paradigms view the world as complex and therefore difficult to understand simply through empirical realism (McKerchar, 2010). McKerchar (2010 p,20) argues that “each strategy has its strength and weaknesses and the drive for mixed method research is to use one strategy to either inform, validate, or compensate for the weaknesses of another.” McKerchar (2010) also highlights several reasons behind the use of such an approach. The first is the need to address different objectives of the study, which cannot achieve by a single method. The second reason is to enable one approach to inform another approach, either in design or in interpretation. The third reason is to triangulate the findings of different approaches (either performed concurrently or sequentially) in an effort to provide greater confidence to the study. Based on the above researcher recommendations, it appears that the main reason for the researcher to adopt a mixed method approach is to enable one approach to inform another approach in the interpretation of the overall results. To be consistent with this strategy, a similar sampling frame used to draw the potential respondents for both approaches.

In this study as stated in the previous chapters, the overall research question is “*Why business profits taxpayers comply with the tax legislations while the benefits of non-compliance is outweighing?*” In order to address this research problem and to answer the research objective comprehensively six hypotheses and one research question were developed at the beginning of this chapter. In light of the research question and hypotheses, the studies were employed both qualitative and quantitative research approach, i.e., self administrated questionnaires and in-depth interview. Therefore, using both approaches is helpful for generating the benefits of a mixed methods approach presented earlier and mitigating the bias in adopting only either quantitative or qualitative approach. Thus, the following sections present the specific quantitative and qualitative aspects of the research method used for this study.

### **3.3 Research Method Adopted**

This section presents the specific data collection methods from both approaches. As a result of this, Section 3.3.1 presents quantitative data collection method used while section 3.3.2 and 3.3.3 present the qualitative data collection method and data analysis methods (both qualitative and quantitative components) respectively.

### **3.3.1 Quantitative aspect-Survey design (self-administered questionnaires)**

To collect relevant data for the examination of taxpayers tax compliance behavior in the case of Addis Ababa City administration business profit tax payers; survey is one method of descriptive research method that help us to gather data at a particular point in time with the intention of describing the nature of existing conditions, or identifying standards against which existing conditions can be compared, or determining the relationships that exist between specific events.

Therefore, the adoption of survey design in this study is helpful in order to represent a wider population; provides descriptive, inferential and explanatory information; gather data on a one-shot basis or gathering of information that will not be available from archive records. In this regard, Fowler (1984, p. 12) noted that the strengths of survey methods that result in their wider use included the value of statistical sampling, consistent measurement, and the ability to obtain information not systematically available elsewhere.

For the purpose of this study the author adopted self administered questionnaires. A self-administered questionnaire has the advantage of scanning a wide field of issues, population, programs etc. with low cost. However, this method is likely to result in a low response rate. On the demerits of self-administered the response rates were typically not as high as might be desired. With very low response rates, it is difficult to establish the representativeness of the sample because those who responded to the survey may be different from the population they will intend to represent. The drawbacks of the self-administered questionnaires will be believed to be mitigated largely by informing respondent through different necessary personal techniques and using other methods. In addition to the mode of collecting data, a sample survey is concerned with issues including sampling and instrument designs, and pre-survey evaluation. The subsequent sections, hence, review these issues in a sample survey in respect of the current study.

### **Sample and Sampling Techniques**

Selecting samples in a research is a common practice to generalize the targeted populations. Tabachnick and Fidell (2001) noted that ideally, samples are selected on randomly bases this

indicates the representativeness of the population. The intention of this study was to generalize the findings to all taxpayers and potential taxpayers in Addis Ababa City administration. Therefore, the sample designs and mode of collecting data would be statistically representative of tax compliance behaviors of businesses operating in Addis Ababa City Administrations. In the case of sample design, as the literature on survey method reveals, how well a sample represents a population depends on the sample frame, the sample size, and the specific procedures of selecting potential respondents.

In respect of sample frame, in a study with the intention of statistically generalizing about Addis Ababa City business profit tax payers, the sample frame from which potential respondents are to be chosen have to be representative of the population. In sample design, a sample selection about broader potential respondents giving equal chance of selection is vital to increasing the representativeness of the sample. Therefore, the target for the sample includes population consists of all businesses operating in Addis Ababa City Administration and pays business profit taxes.

Another point in sample design is the sample size. The choice of a sample size has a bearing on the reliability of a study. However, this does not mean that large sample size always leads to high level of accuracy rather it is to indicate that sample size is one of the factors that contribute to the credibility of a survey estimate. For the choice of sample size, different researchers give different ideas. For example , Alreck and Settle (995 p,63) noted that the choice of sample size is normally made after considering statistical precision, practical issues and available resources (e.g. cost and time). Fowler (1984 p, 43) noted that there is no single precise way for the determinations of sample size hence there are a number of inadequacy for deciding on sample size. For instance, in deciding of a sample size by specifying the fraction of the population to be included in the sample, there is no any right way. This is because the population from which a sample of a particular size is drawn has virtually no impact on how well that sample is likely to describe the population.

In addition, for using that a particular sample is the typical approach to studying a population may also practically lead to the wrong answer. Therefore, it is better if to see the sample size used by other researchers, because it is better if the sample size to be decided by considering

the different goals to be achieved by a particular study. Finally, also for deciding on the sample size by calculating a desired confidence interval for one variable for an entire population is uncommon. However, Fowler contends that nothing is wrong with this approach in terms of some theoretical sense. Apart from the problem of basing sample size decision on the need for precision of a single estimate and the difficulty of determining the level of specific precisions in advance, the estimation of the level of accuracy fails to take into account errors arising from sources other than sampling. The aforementioned points help us consider different conditions in deciding on the desired sample size like the availability of time and resources, and the aim of the research. However, if the final condition is employed, Fowler (1984, p. 43) indicated that for a population, the level of precision increases steadily up to sample sizes of 150 to 200. If the desire is to increase the sample size beyond this limit, there is much more gain that is modest.

In this regard, taking the available resources, time, budget, data, and geographic distances into account, a sample size of 200 were feasible from the total population of 319,319. In order to supplement the information obtained from 200 business profit taxpayers, 25 business profit taxpayers were interviewed. The researcher used stratified random sampling methods in administering the questionnaires. Due to the fact that, there are many business profit tax payers residing in Addis Ababa city administrations. The researcher therefore deemed it fit to employ the stratified random sampling method to classify all profit tax payers by their tax categories and used his personal judgment to select Domestic trade and services, Manufacturing, building and construction, hotel and tourism, import and export and etc for data collection.

Having stratified the business profit tax payers and arrived at which business sector to select from, the researcher had randomly selected from each of the categories on a randomly bases. These methods were used, because of that each of the strata or category of target population had an equal chance or probability of being included or excluded in the final sample. The use of these sampling methods is justified by the fact that they were quicker and less costly to employ and had the ability to represent a high degree of spread in the data collection.

As per the data obtained from ERCA, as of November 9, 2014 there were **319,319** business profit taxpayers operating in Addis Ababa city administrations. These are stratified in to three categories, namely category A, B and C” based on their annual turnovers. To draw a representative sample size of 200, the tax payers further stratified in to sub-cities (i.e. based on sub-cities in which their business operation has been found). Details are shown below in the table:-

**Table 1: Total Number of Tax payers as per their Respective Categories**

No.	Categories of Tax Payers	Total Number of Taxpayers as per their Categories	Percentages
1	A	51,257	16%
2	B	47,000	15%
3	C	221,062	69%
<b>Total</b>		<b>319,319</b>	

Source: Ethiopian Revenue and Customs Authority (2014)

**Table 2: Number of tax payers as per their categories and their respective sub-cities**

No	Name	Tax Payers-Category							
		A		B		C		Total	
		No.	%	No.	%	No.	%	No.	%
1	Arada	2,131	4%	4,882	10%	10,652	5%	17,665	6%
2	Gullele	2,943	6%	2,238	5%	18,357	8%	23,538	7%
3	Addis Ketema	1,723	3%	4,925	10%	12,045	5%	18,693	6%
4	Lideta	1,213	2%	2,366	5%	8,349	4%	11,928	4%
5	Bole	6,446	13%	5,211	12%	33,717	15%	45,374	14%
6	Kirkos	3,000	6%	2,500	5%	19,192	9%	24,692	8%
7	Akaki Kality	1,630	3%	5,067	11%	15,215	8%	21,912	7%
8	Yeka	4,302	9%	3,753	8%	31,177	14%	39,232	12%
9	Nifas Silk Lafto	3,954	8%	7,216	15%	33,150	15%	44,320	14%
10	Kolfe Keranyo	3,721	7%	4,019	9%	32,013	14%	39,753	12%
11	A.A. No. 1**	4,598	9%	-	-	-	-	4,598	1%
12	A. A.No.2**	5,187	10%	-	-	-	-	5,187	2%
13	Markato No.1**	3,582	7%	3,183	7%	4,955	2%	11,720	4%
14	Merkato No.2**	6,827	13%	1,640	3%	2,240	1%	10,707	3%
<b>Total</b>		<b>51,257</b>	<b>100%</b>	<b>47,000</b>	<b>100%</b>	<b>221,062</b>	<b>100%</b>	<b>319,319</b>	<b>100%</b>

Source: Ethiopian Revenue and Customs Authority (2014)



*Note: \*\* those taxpayers' are specially designated taxpayers and centrally treated by ERCA at the head office level.*

As we have seen from the above tables, Category–C tax payers (69%) received the highest percentage and most of them are distributed in Bole, Nifas silk, Kolfe and Yeka sub-cities respectively. Next to Category–C taxpayers, Category-A taxpayers incorporates 16% of the total populations and distributed in Merkato No.2, Bole, Addis Ababa No.2 and Addis Ababa No.1 respectively. In additions to these, the smallest percentages of all taxpayers' are fall under Category-B (i.e.15%) and most of them are found in Nifas Silk,Bole,Akaki Kality and Addis Ketema sub-cities respectively.

**Chart 1- Categories of Taxpayers and their distribution in their respective sub-cities (i.e. based on their rank from 1up to 4)**

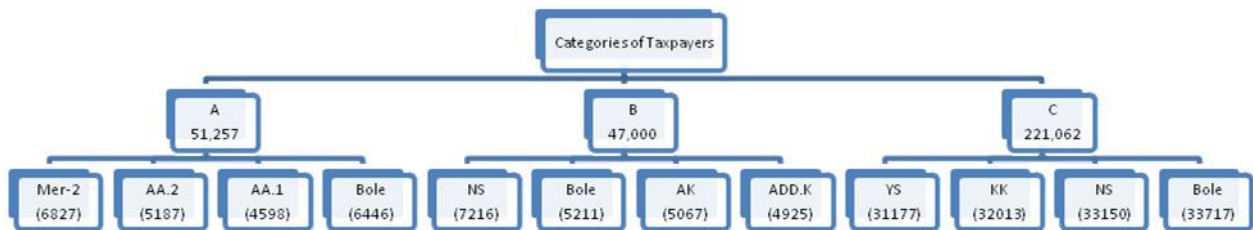


Chart 1 depicts that most of the tax payers' are distributed in six sub-cities such as Bole, Nifas Silk Lafto, Kolfe Keranyo, Yeka, Merkato, Akaki Kality and Addis Ketema and in two specially designated branches such as Addis Ababa No.1 & No.2. Considering those facts, the author distributed his questionnaires as per the following table:-

**Table 3: selected sub-cities to distribute Questionnaires**

No.	Sub-cities and Specially designated Branches'	Total number of questionnaires
1.	Bole	52
2.	Nifas Silk	46
3.	Kolfe Keranyo	36
4.	Yeka Sub-city	36
5.	Merkato-2	8
6.	Addis Ababa No.2	6
7.	Akaki Kality	6
8.	Addis Ketema	5
9.	Addis Ababa No.1	5
<b>Total</b>		<b>200</b>

Source: Taxpayers' tax compliance Survey (2015)

### **The survey instruments**

The survey instruments have been prepared in the form of structured self-administered questionnaire and served as the measuring instrument for the study. This instrument does have three sections. The first section intended to gather background information about respondents. While the second section is concerned with business profit taxpayers' tax compliance behavior specifically it was designed to assess factors determining tax payers' tax compliance behavior such as tax knowledge, the influence of peer groups, income level of tax payers, belief in fairness, feeling of detection and punishment and confidence in government spending.

In the last section respondents are provided with an opportunity to suggest possible solutions and to give further comments about how to improve tax compliance behaviors of business profit tax payers'. In order to measure, the items the researcher used Likert type-scale (i.e., "Strongly agree "to "Strongly Disagree"). In additions to this, multiple choice and multiple-response scales (which provides multiple options but the respondent can select anything from one to several alternatives) has also been used to assess information's from the respondents.

### **3.3.2 Qualitative Approach- in depth interviews**

In addition to self-administered questionnaires, this study involved in-depth interviews to provide more information to the data obtained through the survey questionnaires. The use of interviews is appropriate in obtaining either multifaceted or sensitive information, as well as understanding concepts that require detailed elaboration (Hair et al. 2007). In relation to the interview method, research in the social sciences has seen a range of interview approaches, including structured interviews, semi-structured interviews and unstructured interviews. In Nardi, P. M. (2003) book provides the underlying criteria of each type of interview described as structured, semi-structured, and unstructured interviews. Structured interview: the interviewer follows scripted questions in a particular sequence, the interviewee chooses responses from a range of options that are fixed coded quantitatively (responses provided by the interviewer), and asymmetrical structure. In addition, data analyzed via deductive analysis for hypothesis testing in multivariate studies. Whereas Semi-structured Interviews: Interview protocol is used as a guide and questions may not always be asked in the same order (the interviewer initiates questions and poses follow up “probes” in response to the interviewee’s descriptions and accounts), asymmetrical structure and data analyzed via inductive analytic methods for descriptions and interpretations in interpretive studies. Unstructured Interviews: Both interviewer and interviewee initiate questions and discuss topics, possibly less asymmetrical structure, and data analyzed via inductive analytic methods for descriptions and interpretations in interpretive studies.

With reference to the guidelines, this study adopts semi-structured interviews to collect qualitative data. It anticipated that this approach would provide richer and more accurate data to enhance the findings for this study. Twelve questions were developed as a guide for the semi-structured interview sessions. These questions were formulated with reference to the topics under study, that is: tax payers’ tax knowledge, belief in fairness, influence of the peer groups, income level, feeling of detection and punishments and confidence in government spending.

### **3.3.3 Data Analysis**

This section sets out the proposed analysis to evaluate the survey data beginning with the non-response bias test and response representativeness. Next is a brief discussion of the descriptive analysis and multiple regression models.

#### **3.3.3.1 Non-response bias and response representativeness for quantitative aspect**

A non-response bias test was performed to ensure that there is no bias on the samples. Leong, C. Y. (1980), highlight that the popular approach to prove non-response bias is by comparing first responses to responses generated after follow-ups. If there are no significant differences between the two groups of responses, it assumed that there is no problem of non-response bias. One method of proving response representativeness is by comparing the demographic background of the responses with the entire population (Leong, C. Y. 1980).

In this study, the responses considered representative of an entire population if they reflected a similar distribution in terms of category and annual turnover. Therefore result of the study indicated about the response rate, response bias and response representativeness as follows:

#### ***Response rate***

The survey was conducted between April and May 2015 and questioners' were distributed to 200 randomly chosen business profit taxpayers. All the taxpayers' survey respondents were located in Addis Ababa City. A two week return date was requested. To increase the response rate, follow-up reminders (together with questionnaires), and alternatively, telephone call reminders were made to the representatives requesting them to remind them to return the questionnaires. Out of this sample, 15 questionnaires were returned as non-answered. One possible reason for not completing the questionnaires is the subject of research itself (taxation) considered as difficult subject. Overall, 153 responses were received, giving a response rate of 76.5 percent. This shows that the response rate considered as fair. (Dillman, 2007) suggests that the response rate for a personal delivery approach varies considerably from the lower of 28 percent to the highest of 50 percent.

### *Non-response bias*

To test if there is any non-response bias on the samples, a t-test analysis performed comparing the early responses to responses generated after follow-ups (Dillman, 1992). Therefore, in order to decide whether the groups were significantly different from each other, the p-value was examined. The result shows that the majority of the items have a p-value of more than 0.05, indicating that the groups are not significantly different. While the results provide an indication that there is no problem of response bias among the early and late responses in the Addis Ababa City business profit taxpayers' sample, it is important to note that they do not guarantee that the sample is free of non-response bias considering the low response rate achieved.

### *Response representativeness*

One method of establishing response representativeness is by comparing the respondent profile with the entire population (McInnis, 2006). In this study, the responses were compared based on turnover and taxpayers category. The majority of the respondents in the survey responses are more than annual turnover of ETB 500,000. In terms of working sector, however, the percentage of the survey responses is comparable to the total population. The majority of them are **domestic trade and service sector** was represented. In sum, comparing the survey responses with the total population on two criteria signifies no major differences. Thus, it can conclude that the responses are representative of the total population (Addis Ababa business profit taxpayers').

### **3.3.3.2 Descriptive Analysis and multiple regression models**

To analyze the data both descriptive and inferential statistics were used. Descriptive statistics adopted by the researcher includes measure of central tendency (i.e. mean, mode and median), measure of variability or dispersion (i.e. standard deviation and variance). In additions to this, the author adopted inferential statistics such as multiple regression models in order to test the correlation and variability between dependent (tax compliance) and independent variables (i.e. knowledge, fairness, peer group influence, income level, detection & punishment and tax payers' confidence in government spending). Moreover, structure coefficients, F-tests and

analysis of variance (ANOVA) has also been used in order to examine the significant difference between two or more means. In order to undertake the above data analysis the researcher used Statistical Package for Social Science (SPSS) software.

### 3.3.3.3 Definition and Variable Measurement

In this study tax compliance behaviors have been measured by six hypothetical questions; and the use of those hypothetical questions can increase reliability of results and minimizes respondents' dishonesty when answering the questionnaire (Troutman, 1993). The dependent variable of the study is tax compliance behavior and which is affected by tax knowledge, fairness in the tax system, peer group influence, income level, detection and punishments and Confidence in government spending. Only those variables are selected by the author because businesses are not affected by demographic factors such as age and gender. Therefore, based on the selected factors the author had developed the following regression models:

#### The Model

Tax compliance behaviors of businesses have been measured by six factors: tax knowledge, fairness in the tax system, peer group influence, income level, detection and punishments and Confidence in government spending. For instance, peer group influence can be measured by five statements: e.g. "Positive peer attitude i.e. a belief that my neighbors are reporting and paying tax honestly encourages me to report and pay the correct amount of taxes." (5 = strongly agree, 1 = strongly disagree). The average score over the five items in each factor will be taken as an index for tax compliance. Based on this score, taxpayers were categorized into three levels of compliance: low, medium and high (adopted from Tadesse Getachew Engida et.al 2014). Given the scaled ranking information of the dependent variable, regression model have been applied. The regression result has the following form:

$$Y_i^* = \beta_0 + X_{1i}\beta_1 + X_{2i}\beta_2 + \dots + X_{ki}\beta_k + v_{zi}$$

$$Y_i^* = X_i\beta + v_{zi}$$

Where  $Y_i^*$  is the dependant variable (levels of compliance);  $\beta$  is the vector of estimated parameters and  $X_i$  is the vector of explanatory variables;  $e_i$  is the error term, which is assumed to be normally distributed (zero mean and unit variance).

$Y_i$ , the observed ordinal variable, takes on values 0 through  $m$  according to the following scheme:

$$Y_i = j \Leftrightarrow \mu_{j-1} < Y_i^* < \mu_j \text{ where, } j=0 \dots m$$

Like the models for binary data, the study is concerned with how changes in the explanatory variables transform into the probability of observing a particular level of compliance. Accordingly, the probability of each tax compliance level (low- $y_1$ , medium- $y_2$ , and high- $y_3$ ) will be computed as follows:

$$y_i=1 \text{ if } y_i^* < u_1$$

$$y_i=2 \text{ if } u_1 < y_i^* < u_2$$

$$y_i=3 \text{ if } y_i^* > u_2$$

Likewise, our regression model has been drawn from the above assumptions considering tax compliance behaviors of businesses have been affected by tax knowledge, fairness in the tax system, peer group influence, income level, detection and punishments and Confidence in government spending by controlling other factors such as gender and age. For both behavioral estimations we include some control variables (*Age* and *Gender*), and in the estimation of tax compliance behavior we include a dummy variable to reflect whether business profit tax payers affected by those variables (*effects on tax compliance behavior Dummy*) in order to control for the effect of age and gender on tax compliance behavior.

As per these study tax compliance behavior of business profit tax payers doesn't been affected by age and sex because most of the time those variables are used for assessing individual level of tax compliance behavior rather than using for assessing tax compliance behavior of business profit tax payers (such as share companies and private limited companies). Considering those factors the model has been stated as follow:

$$TC = \beta_0 + \beta_1TK + \beta_2BF + \beta_3PG + \beta_4IL + \beta_5DP + \beta_6GS + e \dots \dots \dots (3)$$

Where;

**Tax compliance (TC)** – this study adopted the definition of McBarnet (2001) and stated that tax compliance should be perceived in three ways, namely; committed compliance (i.e. taxpayers' willingness to pay taxes without complaint); Capitulative compliance (i.e. reluctantly giving in and paying taxes) and Creative compliance (i.e. engagement to reduce taxes by taking advantage of possibilities to redefine income and deduct expenditures within the bracket of tax laws). Therefore, tax compliance in this study is a dependent variable and affected by tax knowledge, fairness in the tax system, peer group influences, income level of the taxpayers, detection and punishments and confidence in government spending.

**Tax Knowledge (TK)** – is the vector of explanatory variables and includes knowledge about tax policies, procedures, rules and regulations; and which have both positive and negative impact in the tax morale or taxpaying attitude of business profit tax payers. This tax knowledge's shall be obtained through continuous training, opportunities, expertise, and nearness to tax related information's.

**Belief of Fairness in the tax system (BF)** - is also the vector of explanatory variables and explained by tax fairness relative to other tax payers, equitable determinations of tax liability, and provisions of equitable information to all tax payers, setting fair penalties and availability of loopholes(such as arbitrary estimation of tax liability by the tax assessors).

**Income Level of the tax payers (IL)** – has been considered as an independent variable and tested whether source of income, level of income and types of businesses are providing opportunity for tax non-compliance opportunity and the author incorporates questions related with the prevailing inflation level, applicable tax rates, business growth, type of business and voluntary compliance behavior in the tax administrations affects tax compliance behavior.

**Influences of Peer Groups (PG)** - has been considered as an independent variable and measured by questions related with positive peer attitudes, rewarding best tax payers, cross



checking reference groups and the feeling of guilt and loss of self respect. The author has been expected positive and significant impact on the tax compliance behaviors of businesses.

**Detection and Punishment (DP)** – this factor is considered as an independent variable and includes questions related with paying taxes because of fear of being caught and penalized, continuous audits, morality, incentives and complexity of the tax administrations. This factor is also affects tax compliance behavior of businesses as high detection and punishments by the tax authority perpetrates involuntary tax compliance behavior of taxpayers.

**Taxpayers' Confidence in Government Spending (GS)** – confidence in government spending has been regarded as a determining factor of tax compliance behaviour. In order to test those variables the author incorporates questions related with proper utilizations of taxes by the government, perceptions on benefits to be received from the government spending, voluntary tax compliance and corruption and fraud.

**E** = Error terms which is assumed to be normally distributed (zero mean and unit variance).

**Table 4: Variables description and expected associations with the level of tax compliance**

Variables	Symbols	Unit of measurement	Expected signs/hypotheses
<i>Dependant Variables</i>			
Tax compliance	TC	(1,2,3) ordinal	
<i>Independent Variables</i>			
Tax knowledge	TK	(1,2,3) Ordinal	+(high tax knowledge, high compliance)
Feeling of fairness	FF	(1-5 Likert Scale) Ordinal	+(good perception, high compliance)
Income level of tax payer	IL	(1-5 Likert Scale) Ordinal	+(High income, Higher Compliance)
The influence of peer groups	PG	(1-5 Likert Scale) Ordinal	+(high influence, high compliance)
Detection and punishments	DP	(1-5 Likert Scale) Ordinal	+(high probability, high compliance)
Confidence in government spending	GS	(1-5 Likert Scale) Ordinal	+(good perception, high compliance)

### **3.4 Conclusions and the relationship between research question/ hypotheses and sources of data**

This chapter has presented the research question and various hypotheses as well as the methods appropriate to address them. Table-5 sets out how research question/hypotheses addressed by the appropriate item in the survey and in depth interviews with business profit taxpayers. To sum up, based on the overarching research problem stated in the earlier chapter, one research question and six hypotheses have been developed. With respect to methodology, the principles of qualitative, quantitative, and mixed methods research approaches shown. Based on the underlying principles of research methods; the mixed method approach were chosen as appropriate to this research. More specifically, to address the research questions, survey (self-administered questionnaires) and in-depth interviews were shown to be the appropriate methods of inquiry for this research. The next chapter presents the results and analysis of each of these methods of inquiry.

**Table 5: Relation between the research question/ hypotheses and source of data**

Research question/hypotheses	Name of variables investigated	Items in the self-administered questionnaires and in-depth interviews
<i>Q1) Why business profits taxpayers comply with the tax legislations while the benefits of non-compliance is outweighing?</i>		Self administered questionnaires 7, 8, 9, 10, 11, 12, 13, 14 & 15 and taxpayers interviews 2,3,4,5,6,7,8,9,10 & 11.
<i>H1) Tax knowledge (demographic factor) affects the taxpaying attitudes of business profit tax payers.</i>	Tax knowledge and tax compliance behavior	Self administered questionnaires 4, 5, 6 & 7 and taxpayers interviews 1, 2, 3 & 4.
<i>H2) Belief of Fairness (attitude &amp; perception factor) increases compliance behavior of business profit tax payers.</i>	Belief in fairness and tax compliance behavior	Self administered questionnaires 6, 8 & 13 and taxpayers interviews 1, 3 & 5.
<i>H3) Influences of the peer groups (attitudes &amp; perception) do have positive and significant impact on the tax compliance behavior of business profit tax payers.</i>	Peer group influence and tax compliance behavior	Self administered questionnaires 8, 13 & 14 and taxpayers interviews 1, 2, 3 & 5.
<i>H4) Income level of tax payers (non-compliance opportunity) does have positive and significant impact on the tax compliance behaviors of business profit tax payers.</i>	Income level of taxpayers and tax compliance behavior	Self administered questionnaires 3, 10, 13 & 14 and taxpayers interviews 1, 2 & 7.
<i>H5) Feeling of Detection and punishments by the tax authorities (tax system/structure) does have an impact on the tax compliance behaviors of business profit tax payers.</i>	Feeling of detection and punishments and tax compliance behavior	Self administered questionnaires 11, 13 & 14 and taxpayers interviews 1, 2, 3 & 8.
<i>H6) Tax payer's confidence in government spending (tax system/structure) affects the tax compliance behavior of business profit tax payers.</i>	Tax payers confidence in government spending and tax compliance behavior	Self administered questionnaires 12 and taxpayer's interviews 1, 2, 3, 9, 10, 11 & 12.

## **Chapter 4: Results and Analysis**

This chapter presents the results of the various data collection methods and analysis in the context of the existing knowledge reviewed in chapter two.

### **4.1 Results**

One of the purposes of this study is to investigate Addis Ababa City business profit taxpayers' tax compliance behaviour. The principal data sources to this end are the survey and in-depth interview. The following discussion presents the results of the survey and in-depth interview therefore in section 4.1.1 presents survey results while in section 4.1.2 presents in-depth interview result.

#### **4.1.1 Survey result**

The purpose of this section is to show the results from surveys that are conducted to Addis Ababa City business profit taxpayers. Therefore, it covers the respondent's profiles in section 4.1.1.1. Investigation of general factors affecting taxpayers' tax compliance behavior in section 4.1.1.2., and in section 4.1.1.3 it covers specific factors affecting taxpayers' tax compliance behavior of businesses operating in Addis Ababa city administrations.

##### **4.1.1.1 Respondents' profile**

According to Income Tax Regulation No. 78/2002, there are different categories of business sectors. For this study, the sectors distribution of respondents was summarized in Table 6. As per the outcomes of the survey, about 56% of the respondents were engaged in domestic trade and services, while 15% and 12% were engaged in building & construction and manufacturing sectors respectively (Table 6).

**Table 6: Sectors distribution survey of respondents**

<b>Business sector</b>	<b>Frequency</b>	<b>Percentages</b>
Domestic trade and services	85	56%
Building and Construction	23	15%
Manufacturing	18	12%
Import and Export	17	11%
Others	10	6%
<b>Total</b>	<b>153</b>	<b>100%</b>

*Source: Business profit taxpayers survey and own computations (2015)*

In terms of forms of business ownership, 37 percent and 35 percent of the survey of taxpayer respondents were sole proprietors and private limited company respectively (Table 7).

**Table 7: Forms of business ownership**

<b>Type of ownerships</b>	<b>Frequency</b>	<b>Percentages</b>
Sole proprietorship	57	37%
Private Limited company	53	35%
Share company	23	15%
partnership	20	13%
<b>Total</b>	<b>153</b>	<b>100%</b>

*Source: Business profit taxpayers survey and own computations (2015)*

Assessing of business profit taxpayers survey respondents in terms of their annual turnover in the fiscal year 2014/15 showed that (49 percent) had a total turnover of more than Ethiopian birr (ETB) 500,000; while 35 percent had a turnover of between ETB 100,001 to ETB 500,000 (Table 8).

**Table 8: Respondents' turnover for the 2014/15 fiscal year**

<b>Total annual Turnover(ETB)</b>	<b>Frequency</b>	<b>Percentages</b>
<b>Up to 100,000</b>	25	16%
100,001- 500,000	53	35%
More than 500,000	75	49%
<b>Total</b>	<b>153</b>	<b>100%</b>

*Source: Business profit taxpayers survey and own computations (2015)*

In respect of knowing the position of the respondents in the sector, the result showed that about 42 percent and 25 percent of the respondents respectively were owners and others (owner & manager) while 18 percent were Managers (Table 9).

**Table 9: Respondents' positions**

<b>Position</b>	<b>Frequency</b>	<b>Percentages</b>
Owner	64	42%
Other(owner & Manager)	38	25%
Manager	28	18%
Employee	23	15%
<b>Total</b>	<b>153</b>	<b>100%</b>

*Source: Business profit taxpayers survey and own computations (2015)*

In case of the educational qualification of respondents, the survey revealed that about 53 percent had BA holders while 18 percent had a Diploma. Nearly 13 percent of respondents indicated that they had a masters Degree, while 12 percent and 4 percent were 12 grades complete and no formal schooling respectively (Table 10).

**Table 10: Respondents educational background**

Level of education	Frequency	Percentage
Bachelor Degree	82	53%
Diploma	28	18%
Master Degree	20	13%
12 Grade complete	18	12%
Below 12 Grade	5	4%
<b>Total</b>	<b>153</b>	<b>100</b>

*Source: Business profit taxpayers survey and own computations (2015)*

The most important source (see Table 11) of tax knowledge to the taxpayers' is proclamations and directives issued by the concerned government organs (29%) and the ERCA website, newsletters or advertisement (28%), though other direct forms of interaction with ERCA are of relatively low importance as sources of knowledge. For example, there is a low level of training courses offered by ERCA (8%) and of participation both in representative meetings with ERCA at national or regional levels (10%).

**Table 11: Sources of tax knowledge**

Modes of communications	Frequency	Percentage
ERCA website, Newsletters or advertisement	44	28
Meetings with ERCA at national or regional level	17	12
Proclamations and directives issued by the concerned government organs.	45	29
Training courses offered by accounting firms or consultants.	19	13
Training courses offered by ERCA	13	8
Participation in business meetings, forums and boards	15	10
<b>Total</b>	<b>153</b>	<b>100</b>

*Source: Business profit taxpayers survey and own computations (2015)*

#### 4.1.1.2 The tax system and its impact on the tax compliance behavior of businesses

The survey outcomes revealed that about 54 percent of business profit taxpayers' believes that the prevailing tax system doesn't encourage them to comply with the tax legislations. In additions to this, 30 percent of the respondents are indifferent about the impact of the current tax system on the tax compliance behavior of businesses. While 16 percent of the respondents are agreed with the proposed statements depicting that the prevailing tax system encourages them to pay their tax obligations. Details are shown on the table below:

**Table 12: Taxpayers' tax compliance behavior**

Descriptions	Frequency	Percentage
Yes	24	16%
No	83	54%
Indifferent	46	30%
<b>Total</b>	<b>153</b>	<b>100%</b>

*Source: Business profit taxpayers survey and own computations (2015)*

Moreover, in order to know the reasons behind complying with the tax legislations; respondents are asked some of the questions prescribing the factors which contributes its part to tax non-compliance behavior and the result revealed that about 44 percent showed that lack of knowledge as the major reason while 31 percent, 16 percent, and 9 percent responded that intentional behavior, lack of ability to pay, and unintentional behavior respectively as factors contributing to tax non-compliance behavior (table 13).

**Table 13: Reasons for tax non-compliance**

Description	Frequency	Percentage
Lack of knowledge	67	44%
Intentionally	48	31%
Lack of ability to pay their tax obligations	25	16%
Unintentionally	13	9%
<b>Total</b>	<b>153</b>	<b>100%</b>

*Source: Business profit taxpayers survey and own computations (2015)*



### **4.1.1.3 Specific factors affecting taxpayers' tax compliance behavior**

#### **Tax knowledge**

As per this study, taxpayers' tax compliance behaviour has been affected by one's own knowledge about tax policies, procedures, rules and regulations. Tax knowledge does have both positive and negative impact on the tax morale or taxpaying attitude of business profit tax payers. This tax knowledge's shall be obtained through continuous training, opportunities, expertise, and nearness to tax related information's.

Sometimes many business owners utilize the acquired tax knowledge to evade or avoid taxes. And doing so does have a devastating impact in reducing the income earning capability of the government. Therefore, the absolute levels of the mean response in Table 14 are all below 4 except one question prescribing sharing knowledge with ERCA increases the chance to determine the correct tax liability, the level indicating agreement. It thus appears that companies see ERCA as an important source of information but do not have a strong motivation to share information in a two-way process, despite the low risk identified. The main conclusions from this part of the survey are as follows.

- Business profit tax payers' should consider the benefits of both of higher levels of tax awareness among operational decision makers and of improved relations with ERCA. Obviously costs are an important consideration in determining the optimum structure for tax knowledge.
- ERCA should make greater use of firms' tax-related experiences by improving its methods of capturing feedback. This would enable difficulties to be identified at an earlier stage.

**Table 14: The impact of tax knowledge on the tax compliance behavior of taxpayers'**

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean score	Standard deviation
My business has the required expertise to share tax knowledge's with ERCA.	20(13%)	31(20%)	24(16%)	52(34%)	26(17%)	3.23	1.31
My business has sufficient opportunities to share tax knowledge's with ERCA.	28(18%)	31(20%)	41(27%)	50(33%)	3(2%)	2.79	1.14
My business has sufficient experience to share tax knowledge's with ERCA.	17(11%)	33(22%)	37(24%)	46(30%)	20(13%)	3.11	1.22
My business has the necessary channel of communications to share tax knowledge with ERCA.	17(11%)	42(28%)	17(11%)	61(40%)	16(10%)	3.10	1.24
Sharing knowledge with ERCA increases the chance to determine the correct amount of tax liability.	2(1%)	9(6%)	11(7%)	48(32%)	83(54%)	4.31	0.94

*Source: Business profit taxpayers survey and own computations (2015)*

Table 14 shows that majority of companies (86%) agree that sharing knowledge with ERCA enables the latter to determine the company's correct tax liability; while a minority (7%) believes that sharing knowledge enables ERCA to increase tax liability. Knowledge sharing with ERCA may therefore be seen as a low-risk activity by the majority of companies. The responses to the remaining questions in Table 14 are mixed, although differences do exist between the different tax knowledge structures.

### **Belief in Fairness**

This study incorporates various statements explaining the feeling of fairness perceptions on tax compliance behaviour of businesses. For instance, it includes statements prescribing equitability of the tax system, provisions of sufficient information and treating all taxpayers respectfully, politely and dignifying them for their actions and other similar statements to test whether the feeling of fairness perceptions affects tax compliance behaviour of businesses.

Considering those facts, the mean responses obtained from table 15 are all near to 4.0 except one question prescribing "my tax obligation is fair relative to others". That means respondents are neutral with this statements. However, the last two questions revealed that unreasonable, intrusive audits and unfair penalties, leads taxpayers towards stress and dissatisfaction (mean

response of 4.41 and standard deviation of 0.73) and the current tax system does have many loopholes(i.e. arbitrary estimation of taxes) which leads taxpayers towards corruption and tax evasion (mean response of 4.27 & standard deviation of 0.99).

**Table 15: The impact of the feeling of fairness perceptions on the tax compliance behaviour of businesses**

Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean score	Standard deviation
I believe that my tax obligation is fair relative to others.	13(8%)	35(23%)	59(39%)	35(23%)	11(7%)	2.97	1.05
I believe that the overall tax system is not equitable.	11(7%)	13(9%)	15(10%)	68(44%)	46(30%)	3.81	1.17
I believe that tax authorities provide sufficient and equitable information to all taxpayers.	9(6%)	17(11%)	9(6%)	66(43%)	52(34%)	3.89	1.17
I believe that unreasonable, intrusive audits and unfair penalties of tax assessors will lead towards stress and dissatisfaction.	2(1%)	0	9(6%)	63(41%)	79(52%)	4.41	0.73
I believe that the current tax system have many loopholes to lead taxpayers towards corruption and tax evasion.	4(3%)	9(6%)	7(5%)	55(36%)	78(50%)	4.27	0.99

*Source: Business profit taxpayers survey and own computations (2015)*

In additions to this, the impacts of fairness perceptions on the tax compliance behaviour have been divided in to three levels such as low, medium and high. Based on these categorizations the following results have been obtained:-

- As per table 16 most of the taxpayers are agreed with the statements proposed by the author with mean response of near to 4. Except the first questions prescribing my tax obligation is fair relative to others (i.e. respondents choose neutral positions).
- Regarding about the feeling of fairness perceptions, the effects of the proposed statements on the tax compliance behaviour is very high (i.e. incorporates 83% of the total populations). Details are shown below:-

**Table 16: Factors explaining feeling of fairness in the tax compliance behavior**

BF		Fairness relative to others	Overall tax system is unequal	Provision of sufficient and equitable information	Intrusive audits and unfair penalties	Loopholes will lead to invasion and corruption
Low	Mean	1.63	1.50	1.50	4.00	3.75
	Std. Dev.	1.061	.535	.535	1.414	1.753
	N	17	17	17	17	17
Medium	Mean	3.75	3.75	3.00	3.75	3.25
	Std. Dev.	.500	.957	1.414	.500	.957
	N	9	9	9	9	9
High	Mean	3.10	4.14	4.28	4.52	4.41
	Std. Dev.	.931	.847	.720	.569	.795
	N	127	127	127	127	127
Total	Mean	2.97	3.81	3.89	4.41	4.27
	Std. Dev.	1.049	1.171	1.174	.732	.992
	N	153	153	153	153	153

Source: Business profit taxpayers survey and own computations (2015)

Moreover, table 16 above shows that the feeling of fairness perception highly affects tax compliance behavior of businesses operating in Addis Ababa city administrations. Generally, from the survey result the author understood that fairness issues such as distributive justice, procedural justice and retributive justice have been highly affected by taxpayer's tax compliance behavior. For instance respondents believe that:

- ✓ The overall tax system in Addis Ababa city administration is not equitable
- ✓ Tax authorities don't provide sufficient and equitable information to all taxpayers.
- ✓ Unreasonable, intrusive audits and unfair penalties of tax assessors will lead tax payers towards stress and dissatisfaction.
- ✓ The current tax system does have many loopholes (such as arbitrary estimation of taxes) to lead taxpayers towards corruption and tax evasion.

### Influences of the peer groups

This variable assesses whether the influence of peer groups affects the tax compliance behaviour of businesses operating in Addis Ababa city administrations. In order to understand those issues the author incorporates questions related with the influence of reference groups, rewards and moral values in affecting the tax compliance behaviour of businesses. Details of the assessment results are shown below:

**Table 17: The impact of peer groups on the tax compliance behaviour of businesses**

	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean score	Standard deviation
1	Positive peer attitude i.e. a belief that my neighbors are reporting and paying tax honestly encourages me to report and pay the correct amount of taxes.	11(7%)	13(8%)	11(7%)	61(40%)	57(37%)	3.91	1.20
2	Rewarding tax payers i.e. giving a trophy for being best tax payers does have its own impact in affecting the tax compliance behavior of citizens.	2(1%)	26(17%)	7(5%)	66(43%)	52(34%)	3.91	1.10
3	Paying taxes are my obligation and I didn't see any reference groups from my neighbors.	9(6%)	26(17%)	20(13%)	52(34%)	46(30%)	3.66	1.24
4	I believe that my neighbors are evading taxes and don't report the true and fair picture of their tax liability.	2(1%)	15(10%)	55(36%)	52(34%)	28(19%)	3.59	0.95
5	I will not evade taxes because of the feeling of guilt and loss of self respect.	2(1%)	11(6%)	22(14%)	72(47%)	39(26%)	3.84	0.99

Source: Business profit taxpayers survey and own computations (2015)

- ✓ As per table 17 above respondents are agreed with the proposed statements with the mean values of near to four. However, there agreement is not as such convincing (i.e. it ranges from 3.59 to 3.91). In general, based on the assessment results it is possible to conclude that:-
- ✓ Positive peer attitudes (i.e. a belief that my neighbours are reporting and paying tax honestly encourages me to report and pay the correct amount of taxes) affects the tax

compliance behaviour of businesses operating in Addis Ababa city administrations. This statement has been confirmed by the mean response of 3.91 and standard deviations of 1.2. From the total 153 respondents about 118(77%) are agreed with the statements.

- ✓ Rewarding taxpayers (i.e. giving a trophy for being best tax payers) does have its own impact in affecting the tax compliance behaviour of businesses. This statement has been confirmed by the mean values of 3.91 and standard deviations of 1.10. From the total populations about 77% agreed with the proposed statements.
- ✓ In additions to this, about 72% of the total populations agreed with the statements prescribing “I will not evade taxes because of the feeling of guilt and loss of self respect”. Therefore, it’s possible to conclude that those taxpayers who don’t evade taxes and pay their tax obligations without any failure because of the feeling of guilt and loss of self respect rather than other factors.
- ✓ The lowest response rate i.e. a mean value of 3.59 & 3.66 and standard deviations of 0.95 & 1.24 has been obtained for questions number 4 & 3 respectively.

**Table 18: Factors explaining the influence of peer groups in tax compliance behavior**

PG		Positive peer attitude	Rewarding taxpayers	Not seeing reference groups in neighbors	Neighbors don't report true & fair taxes	Not to evade taxes due the feeling of guiltiness
Low	Mean	2.67	2.67	2.83	3.17	2.17
	N	13	13	13	13	13
	Std. Dev.	1.633	1.211	.983	.983	.753
Medium	Mean	2.86	3.14	3.86	2.57	4.07
	N	31	31	31	31	31
	Std. Dev.	1.231	.949	.949	.756	.730
High	Mean	4.36	4.28	3.92	3.70	3.98
	N	109	109	109	109	109
	Std. Dev.	.802	.904	1.313	.778	.892
Total	Mean	3.91	3.91	3.66	3.59	3.84
	N	153	153	153	153	153
	Std. Dev.	1.201	1.100	1.238	.955	.987

Source: Business profit taxpayers survey and own computations (2015)

Moreover, in order to test the level of their agreements with the proposed statements there responses have been divided in to three levels such as High, Medium and Small. Based on table 18 above, about 71% of the total populations have been highly agreed with the proposed statements with a mean value ranging from 3.7 to 4.36 and standard deviations of between 0.802 & 1.313. In general, considering the above facts it's possible to conclude that, the influence of peer groups have been highly affects tax compliance behaviour of businesses operating in Addis Ababa city administrations.

### **Income Level of taxpayers**

Income level of taxpayers' have been considered as an independent variable and expected to test whether source of income, level of income and types of businesses are providing opportunity for tax non-compliance opportunity. Therefore, the absolute levels of the mean response under table 19 are below 4. However, the highest score have been obtained from questions prescribing:-

- ✓ The current tax system doesn't take in to account the prevailing inflation level in the country (i.e. the author has found the mean response of 3.84 and standard deviations of 0.96) and depicting that the prevailing tax system doesn't consider the income earning capability of businesses; and the highest and lowest tax brackets lags behind the prevailing inflation level in the country. From the total respondents about 50% agreed with the statements proposed by the author.
- ✓ In additions to this, the author has found positive results on question number 3 & 2(see table 19) with the mean response of 3.70 & 3.67 and standard deviations of 1.05 & 1.08 respectively. Considering those results, it's possible to conclude that "Paying taxes hinders sustainable growth of businesses and the applicable tax rate is very high and deteriorates the income earning capability of businesses".

**Table 19: The impact of Income Level of taxpayers on the tax compliance behavior**

	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean score	Standard deviation
1.	The current tax system doesn't take in to account the prevailing inflation level in the country.	0(0%)	11(7%)	50(33%)	44(29%)	48(31%)	3.84	0.96
2.	The applicable tax rate is very high and deteriorates the income earning capability of businesses.	4(3%)	24(16%)	24(16%)	66(43%)	35(22%)	3.70	1.08
3.	Paying taxes hinders sustainable growth of my businesses.	4(3%)	26(17%)	9(6%)	85(55%)	28(19%)	3.67	1.05
4.	The type of business that I engaged encourages me to pay the correct amount of taxes.	4(3%)	26(17%)	57(37%)	55(36%)	11(7%)	3.27	0.93
5.	I believe that the current tax system encourages voluntary tax compliance behavior.	20(13%)	41(27%)	28(19%)	50(32%)	14(9%)	2.97	1.22

*Source: Business profit taxpayers survey and own computations (2015)*

However, the respondents' response for two of the questions in the above table (i.e. table 19) is near to 3 depicting that they choose a neutral positions. Therefore, it's possible to conclude that respondents are not aware of or don't want to give their opinion about the impact of the current tax system on voluntary tax compliance (mean response of 2.97 and standard deviations of 1.22) and the type of businesses that individuals are engaged for determinations of the correct tax liability (mean response of 3.27 and standard deviations of 0.93).



**Table 20: Factors explaining Income Level of tax payers in the tax compliance behavior**

IL		Tax system doesn't take inflation	Tax rate is very high	Paying taxes hinder growth of business	Business type encourages paying taxes	Tax system encourages voluntary compliance
Low	Mean	3.25	2.13	3.13	3.00	2.13
	N	17	17	17	17	17
	Std. Dev.	1.035	.835	.991	.926	.641
Medium	Mean	3.74	3.63	3.04	3.15	2.63
	N	59	59	59	59	59
	Std. Dev.	1.059	1.043	1.091	.949	1.079
High	Mean	4.06	4.11	4.29	3.43	3.43
	N	77	77	77	77	77
	Std. Dev.	.802	.718	.710	.917	1.243
Total	Mean	3.84	3.70	3.67	3.27	2.97
	N	153	153	153	153	153
	Std. Dev.	.958	1.054	1.086	.931	1.215

Source: Business profit taxpayers survey and own computations (2015)

In additions to these, table 20 above depicts that whether income level of taxpayers' affects tax compliance behavior of businesses or not. In order to test those issues perceptions of taxpayers on the proposed statements have been divided in to three levels such as Low, Medium and High. Therefore, the result of the study shows that:

- ✓ More than 50% of the respondents are agreed with the proposed statements i.e. income level of taxpayers highly affects tax compliance behaviour of businesses. The mean response in this category ranges from 3.43 to 4.29 and standard deviations ranges from 0.949 to 1.091.
- ✓ The lowest mean value have been obtained from questions depicting that "I believe that the current tax system encourages voluntary tax compliance behaviour (mean value of 2.97)" and "the type of business that taxpayers' are engaged encourages them to pay the correct amount of taxes (mean value 3.27)".

## Detection and punishments

Detection and punishment in tax compliance behavior does have both positive and negative impacts. For instance, taxpayers who are mistakenly accused to cheat taxes may perceive the intervention by the tax office to be controlling. Therefore their tax morale decreases or even erases. Similarly, increasing monitoring and penalties for noncompliance, individuals notice that extrinsic motivation has increased, which on the other hand crowds out intrinsic motivation to comply with taxes.

Thus, as per table 21 below, almost all business profit tax payers believe that, paying taxes are morally ethical but because of other factors such as penalties, fine rates and unfair audits they are not able to comply with the tax legislations.

**Table 21: The impact of detections and punishments on the tax compliance behaviour**

	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean score	Standard deviation
1.	I will pay my tax obligations because of fear of being caught and penalized.	24(16%)	35(23%)	11(7%)	57(37%)	26(17%)	3.17	1.38
2.	Tax assessors make continuous audits as a result there is no room to non-compliance.	28(19%)	37(24%)	44(29%)	35(22%)	9(6%)	2.73	1.18
3.	Paying taxes are morally ethical.	0(0%)	0(0%)	2(1%)	61(40%)	90(59%)	4.57	0.53
4.	I will pay my tax obligations because of the incentives I receive from tax authorities.	37(24%)	55(36%)	26(17%)	28(19%)	7(4%)	2.43	1.17
5.	The current tax system is complex and leads towards penalty.	0(0%)	33(21%)	22(14%)	48(31%)	50(34%)	3.76	1.14

*Source: Business profit taxpayers survey and own computations (2015)*

In additions to this, 65% of the respondents are agreed with the proposed statements prescribing “the prevailing tax system is very complex and leads towards penalty” (i.e. mean response of 3.76). However, respondents choose a neutral position for question number 5, depicting that “I will pay my tax obligations because of fear of being caught and penalized”. From both statements it has been noticed that, even though the current tax system is very

complex and leads towards penalty, respondents are not aware of its impact on tax compliance behavior.

As per table 22 below, perceptions of taxpayers' have been divided in to three levels such as Low, Medium and High. And, the assessment result shows that, the impact of detection and punishment on tax compliance behavior is not as such significant since 54% of respondents are fall in between high and low. However, the contributions of tax morality on the tax compliance behavior of businesses have not been neglected. Because the highest mean value i.e.4.57 has been obtained from questions prescribing "paying taxes are morally ethical". Nevertheless, Paying taxes due to the motives of receiving incentives from the government and fear of continuous audits by the tax assessors doesn't have as such significant impact in affecting detection and punishments variable in a tax compliance behavior. The simple lesson that we have taken from this part of the paper is that incentives and concessions, as is the case with amnesties, must be properly designed to ensure that only those who are meant to benefit, actually benefit from the preferential treatment.

**Table 22: Factors explaining Detection and Punishments in tax compliance behavior**

DP		fear of being caught and penalized	continuous audits	Paying taxes are morally ethical	Paying taxes due to incentives	The tax system is complex
Low	Mean	1.92	2.31	4.54	2.08	2.54
	N	28	28	28	28	28
	Std. Deviation	.641	1.109	.519	.954	.877
Medium	Mean	3.29	2.26	4.63	2.34	3.76
	N	83	83	83	83	83
	Std. Deviation	1.450	.950	.541	1.122	1.051
High	Mean	3.79	3.95	4.47	2.84	4.58
	N	42	42	42	42	42
	Std. Deviation	1.084	.705	.513	1.344	.607
Total	Mean	3.17	2.73	4.57	2.43	3.76
	N	153	153	153	153	153
	Std. Deviation	1.383	1.179	.527	1.174	1.135

Source: Business profit taxpayers survey and own computations (2015)

## Perceptions on Government Spending

The central point discussed under this topic is that, if the government is wisely spending the national revenue, for example for basic facilities like education, health and safety and public transportation, it is likely that voluntary compliance will increase. In contrast, if taxpayers perceive that the government is spending too much on something considered unnecessary or unbeneficial to them then taxpayers will feel betrayed and attempt to evade. Therefore, the mean response obtained from table 23 is less than 3 for two of the statements depicting that:

- ✓ “I believe that the government spends the collected taxes wisely” (i.e. mean response of 2.60 and standard deviation of 1.15). Thus, based on this statements, it's possible to say that taxpayers' in Addis Ababa city administrations perceives that the government doesn't spend the collected taxes wisely as a result they are always searching for any loopholes to evade and avoid taxes.
- ✓ “I believe that my business has benefiting from basic government spending like education, health; safety and etc” (i.e. mean response of 2.91 and standard deviation of 1.13).

However, most of the respondents are agreed with the statements depicting that:-

- ✓ “I believe that paying taxes are my obligation whether the government spends wisely or not” (i.e. mean response of 4.14 and standard deviations of 0.98). Therefore, about 78% of the taxpayers' comply with the tax legislations without expectations of any financial as well as non-financial benefit from the government. However, their compliance behaviour has been emanated from escaping of penalty or cancellations of trade licenses by the government authority.
- ✓ “I believe that negative acts (i.e. corruption and fraud) of tax assessors encourage non-compliance behaviour” (i.e. mean response of 4.11 and standard deviation of 1.16). The survey result depicts that, non-compliance behaviour have been perpetrated by negative acts of tax assessors and or immoral behaviour of the tax authority (i.e. 81% of the respondents are agreed with the proposed statements).

Generally, based on the survey result, it's possible to conclude that, many business owners in Addis Ababa city administrations perceives that their businesses are not benefiting from the

government spending on basic infrastructure in one way or another. This is mainly because of income variability, bureaucracy and corruptions prevailing in the country.

**Table 23: The impact of government spending on the tax compliance behavior**

	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree	Mean score	Standard deviation
1.	I believe that the government spends the collected taxes wisely.	33(21%)	39(26%)	42(27%)	35(23%)	4(3%)	2.60	1.15
2.	I believe that my business has benefiting from basic government spending like education, health, safety and etc.	17(11%)	39(26%)	46(30%)	39(26%)	12(7%)	2.91	1.13
3.	I believe that spending on basic infrastructures encourages voluntary tax compliance.	12(7%)	17(11%)	28(19%)	46(30%)	50(33%)	3.70	1.24
4.	I believe that negative acts (i.e. corruption and fraud) of tax assessors encourage non-compliance behavior.	9(6%)	12(7%)	9(6%)	50(32%)	73(49%)	4.11	1.16
5.	I believe that paying taxes are my obligation whether the government spends wisely or not.	4(3%)	4(3%)	25(16%)	53(34%)	67(44%)	4.14	0.98

*Source: Business profit taxpayers survey and own computations (2015)*

In additions to these, table 24 below depicts that whether perceptions on government spending affects tax compliance behavior of businesses or not? In order to test those issues perceptions of taxpayers on the proposed statements have been divided in to three levels such as Low, Medium and High. Therefore, it's possible to conclude that:

- ✓ Up to 50% of the total population fall in the medium category. Therefore, perceptions on government spending moderately affect tax compliance behaviour of businesses operating in Addis Ababa city administrations. Moreover, most of the respondents perceive that the government doesn't spend the collected taxes wisely and their businesses are not benefiting from the government spending.

**Table 24: Factors explaining Government spending in the tax compliance behavior**

GS		Spending wisely by the gov't	Benefiting from infrastructures	voluntary compliance	negative acts of gov't	paying taxes are my obligation
Low	Mean	1.54	2.00	1.92	3.00	3.54
	N	28	28	28	28	28
	Std. Deviation	.519	1.000	.760	1.732	1.391
Medium	Mean	2.00	2.36	3.68	4.41	3.91
	N	48	48	48	48	48
	Std. Deviation	.976	.902	1.129	.908	.921
High	Mean	3.37	3.60	4.37	4.34	4.51
	N	77	77	77	77	77
	Std. Deviation	.843	.847	.690	.765	.658
Total	Mean	2.60	2.91	3.70	4.11	4.14
	N	153	153	153	153	153
	Std. Deviation	1.147	1.126	1.244	1.161	.982

*Source: Business profit taxpayers survey and own computations (2015)*

#### 4.1.2 Correlation among variables

Table 25 below illustrates the Pearson correlation matrix for dependent and independent variables. Based on Table 25, all independent variables were significantly correlated with tax Compliance behavior and the highest correlation occurred between tax compliance and BF (belief in fairness) ( $r_s = .528$ ) followed by IL (Income Level), DP (Detection and Punishment), PG (Peer group influence), Tax Knowledge (TK) and GS (Perception on government spending). According to univariate results in Table 25, it was suggested that BF, IL, DP, PG, TK and GS were the most significant determinants. The significant correlations here suggest that all independent variables are significant determinants of tax compliance.

**Table 25: Pearson correlation Matrix**

	1	2	3	4	5	6	7
<b>Tax Compliance</b>	1.000						
TK	.327**	1.000					
BF	.531**	.343	1.00				
IL	.474**	-.277	.122	1.000			
DP	.451**	-.113	.086	.429	1.000		
GS	.314**	.083	.120	-.026	.302	1.000	
PG	.392**	-.052	.235	.503	.315	-.025	1.000

\*\* .Correlation is significant at the 0.01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

Source: *Business profit taxpayers survey and own computations (2015)*

### 4.1.3 Multiple regressions Analysis

Multiple regression analysis is conducted to identify the relationship between tax compliance behavior as dependent variable and the independent variables. The outputs of multiple regressions are shown in (Table 26).

**Table 26: Summary of the Standard Regression Model**

Variables	R <sup>2</sup>	Adjusted R <sup>2</sup>	Pearson r	Beta	Std. Error	Structure coefficient s	sig
<b>Effects on tax compliance behavior</b>	0.65	0.62					
Constant				0.372	0.273		0.177
Tax knowledge			0.327	0.248	0.060	0.404	0.000**
Belief in fairness			0.531	0.242	0.066	0.656	0.001**
Peer group influences			0.474	0.345	0.079	0.586	0.000**
Income level			0.451	0.157	0.068	0.557	0.024*
Detection and punishments			0.314	0.156	0.063	0.388	0.015*
Government spending			0.392	0.048	0.061	0.485	0.430

Notes: Dependent variable – Tax compliance

\* Significant at p < 0.05

\*\* Significant at p < 0.01

$$TC = -0.372 + 0.248TK + 0.242BF + 0.345PG + 0.157IL + 0.156DP + 0.048GS + e_i$$

$$TC = -0.372 + 0.248(TK) + 0.242(BF) + 0.345(PG) + 0.157(IL) + 0.156(DP) + 0.048(GS)$$

Source: Business profit taxpayers survey and own computations (2015)

As can be seen in table 26 above, all correlations, except perception on government spending were statistically significant. The result from multiple regressions indicated that tax compliance behavior have been significantly influenced by five variables namely tax knowledge, belief in fairness, Peer group influences, Income Level, Detection & Punishments. Our multiple regression result also suggested that peer groups becomes the main factor with a beta coefficient of .345, followed by Tax knowledge ( = .248), belief in fairness ( = .242), income level ( = .157) and detection and punishments ( = .156). The estimated correlation coefficient (R) and estimated coefficient of determination (R<sup>2</sup>) are estimated within the range of .809 and .654, respectively.

Therefore, the R<sup>2</sup> result shows that 65 percent of the independent variables explain the dependent variable i.e. tax compliance behavior. Moreover, the results imply that peer groups are highly and positively affect tax compliance behavior of businesses. Subsequently,



hypotheses H<sub>3</sub> (*Influences of the peer groups positively and significantly affects the tax compliance behavior of business profit tax payers*) is accepted. Apart from that, tax knowledge and belief in fairness are also significantly affects the tax compliance behavior of businesses operating in Addis Ababa city administration. Again, hypotheses H<sub>1</sub> and H<sub>2</sub> are also accepted. However, confidence in government spending doesn't have as such significant influence on the tax compliance behavior of businesses operating in Addis Ababa city administration.

In additions to this, the ANOVA model resulted that the prediction was statistically significant at  $F(6, 146) = 19.883, p < .001$ , and accounted for approximately 65% of the variance of tax compliance behavior ( $R^2 = .65, \text{Adjusted } R^2 = .62$ ).

**ANOVA<sup>a</sup>**

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	12.677	6	2.113	19.883	.000 <sup>b</sup>
Residual	6.695	146	.106		
Total	19.371	152			

a. Dependent Variable: Tax\_Compliance

b. Predictors: (Constant), GS, DP, TK, BF, IL, PG

#### 4.1.4 Stepwise Multiple Regression Result

In stepwise regression model, each step results in a model, and each successive step modifies the older model and replaces it with a newer one. Each model is tested for statistical significance. Therefore, Examination of stepwise regression model depicts that the final model was built in five steps; each step resulted in a statistically significant model. Examining the degree of freedom column shows that one variable was added during each step (the degrees of freedom for the Regression effect track this for us as they are counts of the number of predictors in the model).

In additions to this, one variable (confidence in government spending) has been removed from the model since the count of predictors in the model has been reduced from six to five. In the first step, as can be seen from the footnote beneath the **Model Summary** table, belief in

fairness was entered into the model. The **R Square** with that predictor in the model was .282. Not coincidentally, that is the square of the correlation between tax compliance behavior and belief in fairness ( $.531^2 = .282$ ), and is the value of **R Square Change**. On the second step, positive affect was added to the model. The **R Square** with both predictors in the model was .452; thus, the author gained .17 in the value of **R Square** ( $.452 - .282 = .17$ ), and this is reflected in the **R Square Change** for that step. By the time it's possible to arrive at the end of the fifth step, and the **R Square** value has reached .807. Note that this value is very close to but not identical to the  $R^2$  value obtained under the standard method. Details of the fifth step result have been shown on the following table:

**Table 27: Summary of the Stepwise Regression Model**

Variables	R <sup>2</sup>	Adjusted R <sup>2</sup>	Pearson r	Beta	Std. Error	Structure coefficients	sig
Effects on tax compliance behavior	0.65	0.62					
Constant				-0.365	0.272		0.184
Tax knowledge			0.327	0.249	0.059	0.405	0.000**
Belief in fairness			0.531	0.251	0.065	0.658	0.000**
Peer group influences			0.474	0.369	0.072	0.587	0.000**
Income level			0.451	0.165	0.067	0.559	0.017*
Detection and punishments			0.314	0.152	0.062	0.389	0.018*

Notes: Dependent variable – Tax compliance

\* Significant at  $p < 0.05$

\*\* Significant at  $p < 0.01$

Source: Business profit taxpayers survey and own computations (2015)

As can be seen in the above table of stepwise regression results that the differences are not significant is due to the fact that these five variables did almost the same amount of predictive work in much the same configuration as did the six predictors accomplished using the standard method. And, it's possible to conclude that belief in fairness, Peer group influences, Income level, Tax knowledge and Detection and punishments were used in a stepwise multiple regression analysis to predict tax compliance behavior and found similar results with

the standard model. Moreover table 27 above shows that, all correlations were statistically significant at 5% significant level.

#### 4.1.5 In-depth interview results

As stated in chapter 3, apart from the survey, this study employed in-depth interviews with business profit taxpayers. This aimed at obtaining taxpayers' perception on the factors affecting taxpayers' tax compliance behavior. In the study, the business profit taxpayers' were participated from different sectors and turnover levels. This in turn enables the study to assess divergent views and arguments from different angles. In the context of the above data sources, the following section presents the results of in-depth interviews with 25 business profit taxpayers. As far as this study is concerned on the issues of tax compliance behavior, the participants had reflected mixed ideas. Accordingly, from the different tax compliance dimensions, 24 percent of interviewees showed that the current tax system doesn't consider the ability to pay principle whereas the remaining 76 percent of the interviewees are given mixed responses on factors affecting tax compliance behavior(see table 28 below).

**Table 28: Summary of responses on tax compliance behavior**

<b>Responses</b>	<b>Frequency</b>	<b>Percentage</b>
Tax knowledge positively affects tax compliance behavior.	<b>4</b>	<b>16</b>
Taxes collected by the government from high-income and low-income earners are not equitable and doesn't consider ability to pay principles.	<b>6</b>	<b>24</b>
Influence of peer groups affects the tax compliance behavior of business profit tax payers.	<b>4</b>	<b>16</b>
I will pay my tax obligations because of fear of detection and punishments rather than fulfillment of my morale obligations.	<b>4</b>	<b>16</b>
My business are not benefiting from basic infrastructures such as education, health, safety and etc.	<b>3</b>	<b>12</b>
I don't have any opinion about whether the government spends the collected taxes wisely or not.	<b>4</b>	<b>16</b>
<b>Total</b>	<b>25</b>	<b>100</b>

Source: *Business profit taxpayers in-depth interview and own computation*

With respect to tax knowledge, researcher has sought that 60 percent of the participant had replayed that there were many problems in understanding, completing and filing the tax return form(s) and in understanding the tax system in general; whereas the remaining 40 percent replayed that they don't have detail knowledge on the prevailing tax system.

Besides this, 40 percent of participant of the interview reflected that the prevailing tax system is complex and affects the tax compliance behavior of businesses. Whereas 24 percent of the participant reflected that, the Ethiopian business profit tax rules are bulky and hard for taxpayers to navigate. Furthermore, 20 percent of the participant agreed that the absence of the tax structure and treatment procedure by itself is very complex (see table 29).

**Table 29: Response on tax knowledge and understanding of the tax system**

<b>Response</b>	<b>Frequency</b>	<b>Percentage</b>
Tax payers have only general knowledge and ideas of the tax system.	10	40
There are many problems in understanding, completing and filing the tax return form(s) and in understanding the tax system in general.	15	60
<b>Tax knowledge</b>	<b>25</b>	<b>100</b>
The prevailing tax system is complex and affects the tax compliance behavior of businesses.	10	40
The Ethiopian business profit tax rules are bulky and hard for taxpayers to navigate.	6	24
The tax structure and treatment procedure by itself is very complex.	5	20
Low level of readability and the tax return form and procedure is unclear.	4	16
<b>Understanding of the tax system</b>	<b>25</b>	<b>100</b>

Source: *Business profit taxpayers in-depth interview and own computation*

To sum up the above mentioned results, quantitative and qualitative methods of inquiry, namely survey and in-depth interview with business profit taxpayers were presented. Data obtained through these methods were employed to investigate factors affecting tax compliance behavior. The results of the different data collection methods revealed consistent findings. However, in order to address the research problems of this study, as detailed in chapter 3, it is crucial to examine the results of the different methods concurrently. It is therefore to pool the

results presented in this section together and comprehensively address the research question (specific research question) and hypotheses. The subsequent section, hence, endeavors to analyze the results and address the research questions holistically.

## 4.2 Analysis

As stated in chapter 2 the general research question of this thesis is “*Why business profit tax payers' comply with the tax legislations while the benefits of non-compliance is outweighing?*” In this context, the specific objective of the research is to explore factors affecting taxpayers' tax compliance behaviour in the case of the City of Addis Ababa. Therefore, the purpose of this chapter is to address the specific research question and hypotheses through considering broader objective of the study at large, using data presented in the preceding sections. Accordingly, the following analysis presents; how the research question and all the hypotheses were addressed. This is followed by a discussion of the application of the findings to the research objectives.

Hypothesis 1, *states that tax knowledge (demographic factor) affects the taxpaying attitudes of business profit tax payers operating in Addis Ababa city administrations.* Data obtained from business profit taxpayers' survey and in-depth interviews were employed to address this specific research question and hypotheses. Based on table 11, 14 and 26 tax knowledge does have both positive and negative impact on the tax morale or taxpaying attitude of business profit tax payers. This tax knowledge's shall be obtained through continuous training, opportunities, expertise, and nearness to tax related information's. The absolute levels of the mean response in Table 14 are all below 4 except the one prescribing sharing knowledge with ERCA increases the chance to determine the correct tax liability, the level indicating agreement. It thus appears that companies see ERCA as an important source of information but do not have a strong motivation to share information in a two-way process, despite the low risk identified.

In additions to this, tax knowledge does have both positive and significant impact in affecting the tax compliance behavior of businesses at 5 percent significant level indicating that knowledge about the tax rules, regulations and procedures encourages business profit tax payers to report and pay the correct tax liability. Moreover, majority of companies (86%)

agree that sharing knowledge with ERCA enables the latter to determine the company's correct tax liability; while a minority (7%) believes that sharing knowledge enables ERCA to increase tax liability. Moreover, structural coefficient obtained from table 26 depicts that a unit interventional change of tax knowledge by holding other factors constant affects tax compliance behavior by 0.404 indicating that tax knowledge significantly affects tax compliance behavior of business profit tax payers'. Whereas the finding from interviews shows that, lack of knowledge among business profit taxpayers caused difficulty for dealing with tax matters; the main reason for this as the suggestion of taxpayers is the tax authority does not provide any general, technical, and legal knowledge.

Therefore, considering the above findings it can be concluded that *tax knowledge (demographic factor) affects the taxpaying attitudes of business profit taxpayers operating in Addis Ababa city administrations; as high tax knowledge encourages high tax compliance behavior*. This result is similar with the research done by Eriksen and Fallan which illustrated the importance of tax education in a tax system. They suggested that fiscal knowledge correlates with attitudes towards taxation and tax behavior and can be improved by a better understanding of tax laws. Notwithstanding, not only tax knowledge affects tax payers tax compliance behavior but there are also other factors which perpetrates taxpayers tax compliance behavior.

*Hypothesis 2, belief in fairness (attitude & perception factor) affects the tax compliance behavior of business profit taxpayers*. In order to test this variable the author incorporates table 15, 16, 25 & 26. The mean responses obtained from table 15 are all near to 4.0 except one question prescribing "my tax obligation is fair relative to others". That means respondents are neutral with this statements. However, the last two questions revealed that unreasonable, intrusive audits and unfair penalties leads taxpayers towards stress and dissatisfaction (mean response of 4.41 and standard deviation of 0.73); and the current tax system does have many loopholes which leads taxpayers towards corruption and tax evasion (mean response of 4.27 & standard deviation of 0.99).

Rather than this, from the survey result the author understood that fairness issues such as distributive justice, procedural justice and retributive justice have been highly affected by taxpayers' tax compliance behavior. For instance respondents believe that, the overall tax

system in Addis Ababa city administration is not equitable; tax authorities don't provide sufficient and equitable information to all taxpayers; unreasonable, intrusive audits and unfair penalties of tax assessors leads tax payers' towards stress and dissatisfaction and the current tax system does have many loopholes which leads taxpayers towards corruption and tax evasion. Moreover, Pearson correlation matrix depicts that, the highest correlation i.e.0.531 has been occurred between the feeling of fairness perception and tax compliance behavior.

In additions to this, multiple regression result also shows that the feeling of fairness perceptions significantly affects tax compliance behavior of businesses operating in Addis Ababa city administration at 5% significant level; and structural coefficient obtained from table 26 supports that a single interventional change in the feeling of fairness perceptions by holding other factors constant affects tax compliance behavior by 0.656 indicating that the feeling of fairness perceptions significantly affects tax compliance behavior of business.

Interview result also showed that most of the taxpayers' believes that their tax obligation is not fair relative to others; and tax related information's are not disseminated equally; and unfair penalties are set by tax assessors and the tax system by itself does have many loopholes which leads taxpayers towards stress and dissatisfaction. Considering the above points it can be concluded that, *belief in fairness significantly and highly affects the tax compliance behavior of business profit tax payers'*.

Hypothesis 3, *Influences of the peer groups (attitudes & perception) positively and significantly affects the tax compliance behavior of business profit tax payers.* This variable has been analyzed using table 17, 18, 25 and 26. Thus, information about peer effects has complicated and subtle impacts. These results clearly indicate that peer effects matter; that is, knowing about how one's neighbors are – or are not – complying with the tax laws changes one's own behavior, even if in perhaps unintended ways. The mean response(i.e.3.91) obtained from table 17 depicts that positive peer attitudes (i.e. a belief that my neighbors are reporting and paying tax honestly encourages me to report and pay the correct amount of taxes) affects the tax compliance behavior of businesses operating in Addis Ababa city administrations.

Moreover, rewarding taxpayers (i.e. giving a trophy for being best tax payers) does have its own impact in affecting the tax compliance behavior of businesses. Rather than this, about 72% of the total populations agreed with the statements prescribing “I will not evade taxes because of the feeling of guilt and loss of self respect”. Therefore, it’s possible to conclude that those taxpayers who don’t evade taxes and pay their tax obligations without any failure because of the feeling of guilt and loss of self respect.

Moreover, Pearson correlation matrix of 0.392 depicts that the correlation between tax compliance behavior and peer group influence is significant at 5% significant level and our multiple regression result also shows that the influence of peer groups highly affects tax compliance behavior of businesses at 1% significant level and our structure coefficient obtained from table 26 depicts that an interventional change in one’s own behavior by referring a reference group in a neighbor and by holding other factors constant affects tax compliance behavior by 0.586 indicating that reference group in a neighbor significantly affects tax compliance behavior of business profit tax payers. Therefore, it can be concluded that, influences of the peer groups are positively and significantly affects the tax compliance behavior of business profit tax payers in Addis Ababa city administrations.

Hypothesis 4, *Income level of tax payers does have positive and significant impact on the tax compliance behaviors of business profit tax payers.* In order to analyze this variable table 19, 20, 25 and 26 have been used. The author had tested income level of taxpayers’ and its impact on tax compliance behavior by incorporating an indirect question to maintain its reliability. Therefore, the mean value obtained from table 19 reveals that, the current tax system doesn’t take in to account inflation levels in the country (i.e. mean response of 3.84 and standard deviations of 0.96); and depicting that the current tax system doesn’t consider the income earning capability of businesses; and the highest and lowest tax brackets lags behind the prevailing inflation level in the country.

In additions to this, the author has found positive results on question number 3 & 2(see table 19) with the mean response of 3.70 & 3.67 and standard deviations of 1.05 & 1.08 respectively. Considering those results, it’s possible to conclude that “Paying taxes hinders sustainable growth of businesses and the applicable tax rate is very high and deteriorates the



income earning capability of businesses". Pearson correlation matrix also reveals that the correlation between tax compliance behavior and income level of taxpayers pegged at 0.474 and shows that tax compliance behavior have been highly affected by income level business profit taxpayers. In additions to this, structure coefficient shown in the multiple regression models prescribes that an interventional change in the income level of business profit taxpayers by holding other factors constant affects tax compliance behavior by 0.557. Other than this; significance level shown on table 26 depicts that income level of taxpayers significantly affects tax compliance behavior at 5% significance level. Therefore, it's possible to conclude that, *income level of tax payers does have positive and significant impact on the tax compliance behaviors of business profit tax payers*. This result goes with Fischer's model, as source of income, level of income and occupation are considered as factors providing opportunity for tax noncompliance.

Our interview result also supports the findings obtained from survey instruments. For instance, as stated by many business owners inflation level prevailing in the country does have significant impact in affecting the tax compliance behavior of businesses as the tax rates, exemptions and penalties are not exposed to modifications in line with the inflation level prevailing in the country. In additions to this, many business owners believes that paying taxes hinder sustainable growth of business as some portion of their incomes goes to the government. Therefore, in order to improve tax compliance behavior the government must implement various policy mechanisms such as encouraging tax payers to pay their tax obligations voluntarily without the interference of third parties; and revising the applicable tax rates in line with the inflation levels. However, Income level of taxpayers is not the only factor threatening tax compliance behavior but there are also other factors which affects tax compliance behavior.

Hypothesis 5, *Feeling of detection and punishments by the tax authorities does have significant impact on the tax compliance behaviors of business profit tax payers*. In order to analyze this variable we have used table 21, 22, 25 and 26. The mean response of 4.57 obtained from table 21 depicts that almost all of business profit tax payers believe that, paying taxes are morally ethical but because of other factors such as penalties, fine rates and unfair audits they are not able to comply with the tax legislations.

In additions to this, 65% of the respondents are agreed with the proposed statements prescribing “the prevailing tax system is very complex and leads towards penalty” (i.e. mean response of 3.76). Moreover, respondents choose a neutral position for question number 5, depicting that “I will pay my tax obligations because of fear of being caught and penalized”. From both statements we can conclude that, even though the current tax system is very complex and leads towards penalty, respondents are not aware of its impacts on tax compliance behavior as a result it requires further investigations. Moreover table 22 depicts that, the impact of detection and punishment on tax compliance behavior is not as such significant since 54% of respondents are fall in between. However, we don't neglect the impact of tax morality on the tax compliance behavior of businesses since the highest mean value i.e.4.57 has been obtained from questions prescribing “paying taxes are morally ethical” rather than fear of detections and punishments. Furthermore, Pearson correlation matrix of 0.451 reveals that the correlation between detection and punishments' and tax compliance behavior is significant at 1% significance level (see table 25). Our multiple regression models on table 26 shows that, structure coefficient of 0.388 prescribes that an interventional change in the detection and punishment variables by holding other factors constant affects tax compliance behavior significantly at 5% significance level.

Considering the aforementioned results it's possible to conclude that *feeling of detection and punishments variable does have significant impact in affecting the tax compliance behavior of businesses. However, the feeling of being audited, detected and punished doesn't lead taxpayers' towards paying their taxes rather this kind of feelings erodes the already maintained tax morality of businesses.* This result opposes with the economics-of-crime approach which concludes that an individual pays taxes because – and *only* because – of the economic consequences of detection and punishments and the government can encourage greater tax compliance by increasing the audit and the penalty rates of its regulatory regime.

In additions to this, 39% of our interview result reveals that taxpayers' in Addis Ababa city administration pay their tax obligation not because of fear of being caught and penalized but they believes that paying taxes are morally ethical. In additions to this, Paying taxes because of receiving incentives from the government and fear of continuous audits by the tax assessors doesn't have significant impact in affecting detection and punishments variable. Detection and

punishments in collaboration with the aforementioned other variables affects tax compliance behavior; but they are not the only factors which affects our dependent variable i.e. tax compliance behavior.

Hypothesis 6, *Taxpayers' confidence in government spending significantly affects the tax compliance behavior of business profit tax payers'*. In order to test this hypothesis table 23, 24, 25 and 26 have been used. Therefore, the absolute levels of the mean response in Table 23 are below 3 for two of the questions prescribing "I believe that the government spends the collected taxes wisely" (i.e. mean response of 2.60 and standard deviation of 1.15) and "I believe that my business has benefiting from basic government spending like education, health; safety and etc" (i.e. mean response of 2.91 and standard deviation of 1.13). Therefore, based on the above results, it's possible to conclude that, taxpayers' in Addis Ababa city administrations perceives that the government doesn't spend the collected taxes wisely as a result they are always searching for any loopholes to evade and avoid taxes.

In additions to this, many business owners in Addis Ababa city administrations perceives that their business is not benefiting from the government spending on basic infrastructure in one way or another. This is mainly because of income variability, bureaucracy and corruptions prevailing in the country. As per Pearson correlation matrix on table 25, the correlation between tax compliance behavior and perception on government spending is pegged at 0.314 and which is the smallest of all explanatory variables.

Moreover, the regression model on table 26 shows that, perception on government spending doesn't significantly affects tax compliance behavior at 5% significance level as a result it was excluded from stepwise regression model on table 27. The stepwise procedure adds only one variable at a time to the model as the model is "slowly" built. In this model, each step results in a model, and each successive step modifies the older model and replaces it with a newer one. Each model is tested for statistical significance. Therefore, it's possible to conclude that *confidence in government spending don't have as such significant impact in affecting the tax compliance behavior of businesses in Addis Ababa city administration since more than 50% of the respondents believes that the government doesn't spend the collected taxes wisely and their business is not benefiting from the government spending on basic*

*infrastructure in one way or another. As per this paper, perception on government spending negatively affects tax compliance behavior of businesses.* This result have also been confirmed by our interview with the taxpayers operating in Addis Ababa city administrations because most of the respondents believes that the government doesn't wisely spend the national revenue, for basic facilities like education, health and safety and public transportation. In additions to this, respondents perceive that the government is spending too much on something considered unnecessary or unbeneficial to them and they will feel betrayed and attempt to evade.

### **4.3 Conclusions**

To sum up, the discussions in this chapter endeavoured to integrate the results of the quantitative and qualitative methods so as to address the specific research question and hypotheses and achieve the objectives of the research holistically. However, the findings in this study are not without weaknesses. The subsequent chapter, thus, presents the strengths and weaknesses of the study coupled with implications to the tax authorities and the literature with future research directions.

## **Chapter 5: Conclusions and Recommendations**

This chapter presents the conclusions and recommendations. The purpose of the chapter is to review the whole thesis and highlight future research directions. Accordingly, section one presents overview of the thesis and its major findings while the second section presents the recommendations with future research directions. The third section covers the contribution of the thesis to the literature and tax authority. The limitations of the thesis presented in the last section.

### **5.1 Major findings/Conclusions**

Based on the preceding analysis the paper has drawn the following conclusions/findings:

- Firstly, tax compliance behaviour have been affected by Belief in Fairness, Income Level, Detection and Punishment, Peer group influence and Tax knowledge while confidence in government spending doesn't have as such significant impact in affecting the tax compliance behaviour of businesses. Perceptions on government spending appear to be not significantly correlated with tax compliance decisions.
- Secondly, the current tax system does have many loopholes (i.e. arbitrary estimation of taxes) which erode the tax compliance behaviour of businesses. For instance, Mini and micro business owners do not keep their books properly as a result they are exposed to violation of the record keeping requirement of the government so their tax obligation should be imposed based on subjective estimation. This subjective estimation of tax leads the tax assessors towards corruption and illegal implementation of the tax policy. Therefore, unreasonable, intrusive audits and unfair penalties of tax assessors in Addis Ababa city administration lead taxpayers towards stress and dissatisfaction.
- Thirdly, positive peer attitudes and rewarding taxpayers (i.e. giving a trophy for being best tax payers) does have its own impact in affecting the tax compliance behaviour of businesses. However, paying taxes due to the motives of receiving incentives from the government and fear of continuous audits by the tax assessors doesn't have as such significant impact in affecting detection and punishment variable in our tax compliance behaviour model. The simple lesson that we have taken from this part of the paper is that incentives and concessions, as is the case with amnesties, must be properly designed to

ensure that only those who are meant to benefit, actually benefit from the preferential treatment.

- Fourthly, the current tax system doesn't take in to account the prevailing inflation level and the income earning capability of businesses; and the highest and lowest tax brackets lags behind the prevailing inflation level in the country. For example, the tax-exempt income threshold is considered to be very low and as a result micro and small businesses, which normally generate meagre income from their activities, are obliged to pay taxes, which they could not afford.
- Fifthly, detection and punishment in tax compliance behaviour does have both positive and negative impacts. For instance, taxpayers' who are mistakenly accused to cheat on their taxes may perceive the intervention by the tax office to be controlling. Therefore their tax morale decreases or even erases. Similarly, increasing monitoring and penalties for noncompliance, individuals notice that extrinsic motivation has increased, which on the other hand crowds out intrinsic motivation to comply with taxes.
- Sixths, the  $R^2$  result shows that 65 percent of the independent variables explain the dependent variable i.e. tax compliance behaviour. Moreover, the results imply that most of the variables except confidence in government spending are highly affects tax compliance behaviour of businesses.
- Finally, stepwise regression result shows that the differences with the standard method are not significant is due to the fact that these five variables did almost the same amount of predictive work in much the same configuration as did the six predictors accomplished using the standard method.

From the above findings, what the paper generally conclude that, though there have been considerable attempts and progresses to improve taxation system in the City, there are significant drawbacks. Unless these strains are resolved there might not be changed the perceptions and attitudes of the taxpayers as well as the social and economic development of the city.

## 5.2 Recommendations

Based on the study conducted using survey method and in depth interviews; factors affecting taxpayers' tax compliance behavior have been identified and possible recommendations would be forwarded so that it may help the tax authority and other policy makers to approach the issue accordingly.

- According to the result, the taxpayers' need various social services (such as school, road, electricity, transportation, telecommunications and etc) from the government in return of what they have paid as a tax. If there is no provision of sufficient services, the willingness and motivation of the taxpayers' to pay their tax obligation in full and on timely basis may be affected, i.e. the taxpayers' perceive that their money is being misappropriated or used for meaningless purposes. Therefore, the government should be transparent for the taxpayers' money and the service provided to the society.
- The tax authority educating the public must be considered crucial. It is possible through tax education, concepts of taxation and tax knowledge shall be imparted. Furthermore, taxpayers' need more information about their tax obligations and their role in promoting the growth of the economy of the country and the well-being of its citizens.
- In order to improve taxpayers' tax compliance behaviour the government must build transparent, non-bureaucratic, questionable and responsible institutions which in one way or another supports the tax collection tasks and encourages business profit taxpayers' to pay their tax obligations without any setbacks.
- A transparent and accountable tax administration that is service-oriented is likely to have a positive impact on public trust. If the revenue is furthermore properly spent in terms of a budget which the taxpayers' find agreeable, compliance should increase.
- Incentives and concessions, as is the case with amnesties, must be properly designed to ensure that only those who are meant to benefit, actually benefit from the preferential treatment. Too much political and/or administrative discretion to grant exemptions or other forms of tax relief should also be avoided.
- Providing taxpayers' with various payment options (e.g. banks, supermarkets, internet, ward offices), easy filing, and assistance (e.g. on-line or at shopping malls and sports

stadiums) not only reduces actual compliance costs, but can reduce unintentional non-compliance.

- The tax imposed by the government body has an impact on the firm's profitability and its existence as a firm. So, it is imperative from the government side to critically evaluate and understand the income level of the firm before imposing a tax rate.
- Many business owners do not keep their books properly, which invited to general estimations, which are often arbitrary. So training is necessary on the one hand and on the other hand, national standards for bookkeeping, which would be respected in all taxation office nationwide, need to be defined and introduced.

### **5.3 Contribution and implications of the study**

The findings of this study expected to provide updated information and advanced practices on taxpayers' tax compliance behavior which is happening in the city. In the researchers' view, the results of this study have contributed to the tax literature as well as to the tax authorities. The contributions are discussed below:-

#### ***To the literature***

This study contributes to the existing literature in several ways. First, no prior work has been performed in this area (i.e. taxpayers' tax compliance behavior) in our country especially in Addis Ababa city administration. Thus, the findings documented in this study will be a "stepping stone" for more studies in the future. Second, the mixed-method approach undertaken in this study provides complementary views from different perspectives. While the survey results emphasize the predictive power and significance level of the analysis, the in-depth interviews enhance the findings by providing explanations that are more detailed. Finally, this study helps as instrument for future researchers intending to study taxpayers' tax compliance behavior by incorporating other variables not mentioned in this paper.

#### ***To the tax authorities***

In addition to advancing academic knowledge in the taxation area, this study has also its own practical implications. First, the results of this study provides implications for the government



that specific insights should allow policy makers to gain better understanding of the key variables that are significantly associated with tax compliance and enable them to implement suitable strategies to minimize potentially damaging factors, and should also allow them to improve a government's tax revenue collections. Secondly, the role of the tax authority in minimizing the tax gap and in increasing voluntary compliance was found to be very important as the government has been placed as the main influencing factor in relation to tax compliance behavior. Finally, the government plays a central role through designing and enforcing the tax systems, and collecting taxes.

#### **5.4 Limitations of the research**

In spite of the significant contributions of this study, it has also a number of limitations. The first is the inherent weaknesses with the survey approach itself, like the respondents' differing interpretation of the questions. However, it was acknowledged that these weaknesses may remain to some extent. For example, in terms of the different interpretation of the questions by respondents, the researcher has made reasonable efforts to ensure the wording and sentences were straightforward and precise. In terms of the interview approach, the main weakness is probably the use of similar samples for the survey.

On the other hand, the study only used business profit taxpayers' (i.e. schedule C type of the taxpayers') who are largely sole proprietors and Private Limited Companies. Thus, this is very difficult to generalize this research paper to other group of the taxpayers. Besides, the respondents' attitudes in the course of giving responses perceived to be encountered with the government as a result some of them are not willing to give feedbacks to all of the questions incorporated under this study. Moreover, the absence of adequate source of materials made the work more complex. Unless the undying effort of the researcher exerted for each of the protracted problems the paper would not been reaching to this status.

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# APPENDICES!



**Appendices 1- Taxpayers survey instrument (English version)**

**Addis Ababa University**  
**School of Business and Economics**  
**Department of Accounting and Finance**

**Dear Participant**

The paper has been entitled “Tax payer’s tax compliance behavior” The case of Addis Ababa City Administration Business Profit tax payers and prepared by **Ato Geletaw Tsegaw Tessema** who is currently following his MSc (in accounting and finance) at Addis Ababa University.

The aim of this paper is to know more about the tax compliance behavior of businesses operating in Addis Ababa city administration. And the research questions focused on why businesses pay their taxes while the benefits of non-compliance is outweighing? What are the motivating factors that lead tax payers towards paying taxes and other similar issues have been investigated by focusing on Addis Ababa City administrations business profit tax payers. Therefore, to supplement the data obtained from in depth interviews, the investigator seeks to gather relevant information from randomly selected taxpayers by means of self-administered questionnaire.

All responses will be treated in strict confidence and the identity of respondents and their organization will not be disclosed.

For further information, please contact **Ato Geletaw Tsegaw** by the following address:

Tel: 0911-72-51-66 E-mail: [gechlovely@gmail.com](mailto:gechlovely@gmail.com)

**Section I-Background Information**

**Please tick ( ) on your choice**

1) In which type of business sector did you engaged?

- 1  Manufacturing                      2  Import and Export  
2  Building and Construction    4  Domestic Trade and services  
5  Other, please specify.....

2) What is your legal form of business operations?

- 1  A sole proprietorship              2  A partnership  
3  A private limited Co.              4  A share company  
5  Others please specify.....

3) In which category does your business annual turnover is included?

- 1  Under Birr 100,000                  2  Birr 100,001 – Birr 500,000  
3  More than Birr 500,000

4) What is your level of education?

- 1  Below 12 grade              2  12 grade completed              3  Diploma  
4  Bachelor degree              5  Masters or above  
6  Please specify .....

5) What is your position in the company?

- 1  Owners                              2  Employees  
3  Manager                              4  Other responsibilities, please specify

.....  
6) Which modes of communications serve as the most important sources of information to your business?

- 1  ERCA website or Newsletters.  
2  Meetings with ERCA at national or regional level  
3  Proclamations and directives issued by the concerned government organs  
4  Training courses offered by accounting firms or consultants  
5  Training courses offered by ERCA  
6  Participation in business meetings, forums and boards

7) Do you believe the prevailing tax system encourages business profit taxpayers' to properly pay their tax obligations?

1  yes                      2  No                      3  Indifferent

8) If your answer is 'No' for question number 7 what are the possible reasons?

- 1  Lack of knowledge
- 2  Intentionally
- 3  Lack of ability to pay their tax obligations
- 4  Unintentionally

**Section II- Factors Influencing taxpayers tax Compliance Behavior**

Please tick ( ) on your choice

9) **Taxpayers Tax Knowledge** – tax knowledge affects the taxpaying attitudes of business profit tax payers. Please indicate to what extent you agree with each of the following statements:

No	Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
9.1	My business has the required expertise to share tax knowledge's with ERCA.					
9.2.	My business has sufficient opportunities to share tax knowledge's with ERCA.					
9.3	My business has sufficient experience to share tax knowledge's with ERCA.					
9.4	My business has the necessary channel of communications to share tax knowledge with ERCA.					
9.5	Sharing knowledge with ERCA increases the chance to determine the correct amount of tax liability.					

**10) Taxpayer's belief in fairness-** belief in fairness affects the tax compliance behavior of business profit tax payers. Please indicate, for each of those statements, to what extent you agree:

No	Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
10.1	I believe that my tax obligation is fair relative to others.					
10.2	I believe that the overall tax system is not equitable.					
10.3	I believe that tax authorities provide sufficient and equitable information to all taxpayers.					
10.4	I believe that unreasonable, intrusive audits and unfair penalties of tax assessors will lead towards stress and dissatisfaction.					
10.5	I believe that the current tax system have many loopholes to lead taxpayers towards corruption and tax evasion.					

**11) The Influence of Peer Groups** – The influence of peer groups has been expected to affect the tax compliance behavior of businesses. Therefore, please indicate, for each of those statements to what extent you agree:

No	Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
11.1	Positive peer attitude i.e. a belief that my neighbors are reporting and paying tax honestly encourages me to report and pay the correct amount of taxes.					
11.2	Rewarding tax payers i.e. giving a trophy for being best tax payers does have its own impact in affecting the tax compliance behavior of citizens.					
11.3	Paying taxes are my obligation and I didn't see any reference groups from my neighbors.					
11.4	I believe that my neighbors are evading taxes and don't report the true fair picture of their tax liability.					
11.5	I will not evade taxes because of the feeling of guilt and loss of self respect.					

**12) Income Level of Tax payers-** This is to test whether source of income, level of income and type of businesses are considered as factors providing opportunity for tax non-compliance. Therefore, please indicate, for each of those statements to what extent you agree:

No	Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
12.1	The current tax system doesn't take in to account the prevailing inflation level in the country.					
12.2	The applicable tax rate is very high and deteriorates the income earning capability of businesses.					
12.3	Paying taxes hinders sustainable growth of my businesses.					
12.4	The type of business that I engaged encourages me to pay the correct amount of taxes.					
12.5	I believe that the current tax system encourages voluntary tax compliance behavior.					

**13) Feeling of Detection and Punishments** –this variable has been expected to test whether detection and punishments affects the tax compliance behavior of business profit tax payers. Therefore, please indicate, for each of those statements to what extent you agree:

No	Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
13.1	I will pay my tax obligations because of fear of being caught and penalized.					
13.2	Tax assessors make continuous audits as a result there is no room to non-compliance.					
13.3	Paying taxes are morally ethical.					
13.4	I will pay my tax obligations because of the incentives I receive from tax authorities.					
13.5	The current tax system is complex and leads towards penalty.					

14) Tax payer's confidence in government spending (tax system/structure) – it has been expected that taxpayers' confidence in government spending affects the tax compliance behaviors of business profit tax payers. Therefore, please indicate, for each of those statements to what extent you agree:

No	Statements	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
14.1	I believe that the government spends the collected taxes wisely.					
14.2	I believe that my business has benefiting from basic government spending like education, health, safety and etc.					
14.3	I believe that spending on basic infrastructures encourages voluntary tax compliance.					
14.4	I believe that negative acts (i.e. corruption and fraud) of tax assessors encourage non-compliance behavior.					
14.5	I believe that paying taxes are my obligation whether the government spends wisely or not.					

**Section III- Comments and Recommendations**

13) Please specify your comment (if you have any) about factors that affects tax payer's tax compliance behaviors.

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14) Please state your possible solutions about how to improve tax payer's tax compliance behaviors.

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15) please state any other comments (if you have).

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**Appendix 2 -Taxpayers' tax compliance behavior survey instrument**

**(Amharic Version)**

**አዲስ አበባ ዩኒቨርሲቲ**

**ቢዝነስ- ኢኮኖሚክስ**

**አካውንቲንግና ፋይናንስ ት/ክፍል**

**የገቢ ግብር (Business profit tax system) ጥናት መጠየቅ:-**

**የተከበሩ የጥናቱ ተሳታፊ**

የዚህ ጥናት ርዕስ “Tax payers’ tax compliance behavior in the case of Addis Ababa Business Profit taxpayers” ሲሆን አጥኚው አቶ ገለታው ፀጋው ተሰማ በአዲስ አበባ ዩኒቨርሲቲ በአካውንቲንግና ፋይናንስ ትምህርት ክፍል ተማሪ ነው።

የጥናቱ ዋና አላማ በአዲስ አበባ ከተማ ውስጥ የሚገኙ የትርፍ ግብር ከፋዮች ለምን ግብራቸውን በወቅቱና በአግባቡ እንደሚከፍሉ፤ እንዲሁም ግብራቸውን በመክፈላቸው የሚያገኙት ጥቅም ምን እንደሆነና ግብር ያለመክፈል የራሱ የሆነ የገብ ተፅዕኖ እያለው የትርፍ ግብር ከፋዮች ለምንድን ነው ግብራቸውን የሚከፍሉት የሚሉት ጉዳዮች በጥልቀት ይቃኛሉ። ይህንን ጥናት ለማድረግ ከቃለ መጠይቅ በተጨማሪ የጥናቱ አቅራቢ ይህንን መጠየቅ ያዘጋጀ ሲሆን መጠይቁን የሚሞሉት ግለሰቦችና ድርጅታቸው በጥንቃቄ የሚያዙና ለማንም ይፋ እንደማይደረጉ በመግለፅ ነው።

**ለበለጠ መረጃ:- አቶ ገለታው ፀጋውን በሚከተለው አድራሻ ማግኘት ይችላሉ**  
**☎ 0911 725166 E-mail: [gechlollely@gmail.com](mailto:gechlollely@gmail.com)**

**ክፍል I. መንደርደሪያ ሀሳብ**

**በሚፈልጉት ላይ ምልክት ያድርጉ**

1. በየትኛው የስራ ዘርፍ ነው የተሰማሩት?

1. ማምረት

3. አስመጪና ላኪ

2. በህንፃና ኮንስትራክሽን

4. የሀገር ውስጥ ንግድ

5. ሌላ ካለ ይግለፁ \_\_\_\_\_

2. የእርስዎ ድርጅት?

1. የአንድ ግለሰብ ነው

3. ሀላፊነቱ የተወሰነ የግል ማህበር ነው

2. የሽርክና ማህበር ነው

4. ሺር ካምፖኒ ነው

5. ከዚህ ውጭ ከሆነ ይግለፁ \_\_\_\_\_

2. አመታዊ ሽያጭዎ በየትኛው ክፍል ውስጥ ይመደባል?

1. ከብር 100, 000 በታች

3. ከብር 500, 000 በላይ

2. ከብር 100, 000 - ብር 500,000

4. የትምህርት ደረጃዎ

1. ከ12ኛ ክፍል በታች

4. ድግሪ

2. 12ኛ ክፍል ያጠናቀቀ

5. ማስተርስና ከዚያ በላይ

3. ዲፕሎማ

6. ሌላ ካለ ይግለፁ \_\_\_\_\_

5. በድርጅቱ ውስጥ ያለዎት የሥራ ዘርፍ

1. ባለቤት

2. ሰራተኛ

3. ማኔጀር

4. ሌላ ካለ ይግለፁ \_\_\_\_\_



6. የትኛው የመረጃ አገልግሎት ነው ለድርጅትዎ በጣም የሚያስፈልገው?

1. የገቢዎችና ጉምሩክ ባለስልጣን ድህረ ገፅ ወይም የተለያዩ ፅሁፎች

2. ከገቢዎች ባለስልጣን ጋር የሚደረጉ ሀገር አቀፍ ወይም ክልላዊ ስብሰባዎች

3. ኘሮክላሜሽኖችና ዳይሬክቲቮች

4. ትሬይኒንግ /ስልጠናዎች/

5. የአካወንቲንግ አገልግሎት የሚሰጡ ድርጅቶች ስልጠና

6. በተለያዩ ስብሰባዎች ላይ በመሳተፍ የሚገኝ ዕውቀት

7. አሁን በስራ ላይ ያለው የታክስ ሲስተም ድርጅቶች ያለባቸውን ግብር ወይም የሚጠበቅባቸውን ግብር በአግባቡ እንዲከፍሉ ያበረታታል ብለው ያምናሉ

1. አዎ

3. አስተያየት አልሰጥም

2. አላምንም

8. ለጥያቄ 7 መልስዎ “አላምንም” የሚል ከሆነ ምክንያቶቹ ምንድን ናቸው

1. የዕውቀት ማነስ

2. በማወቅ

3. የአቅም ውስንነት

4. ባለማወቅ

**ክፍል ሁለት**

**9. ግብርን በወቅቱ ለመክፈል ወይም ላለመክፈል አስተዋፅዖ የሚያደርጉ ምክንያቶች የግብር ከፋዮች የታክስ ዕውቀት፡- ከዚህ በታች ለተዘረዘሩት ዓረፍተ ነገሮች መስማማት አለመስማማትዎትን ምልክት በማድረግ ይግለፁ፤**

ተራ. ቁ	ዓረፍተ ነገሮች	በጣም አልስማማም	አልስማማም	አስተያየት አልሰጥም	እስማማለሁ	በጣም እስማማለሁ
9.1.	ድርጅቱ ከሃገር ውስጥ ገቢ ጋር የሚያግባባ ዕውቀት አለው።					
9.2.	ድርጅቱ ከሃገር ውስጥ ገቢ ጋር የሚያግባቡ ዕድሎች አሉት።					
9.3.	ድርጅቱ በቂ ልምድ አለው።					
9.4.	ድርጅቱ ከሃገር ውስጥ ገቢ ጋር የሚያግባባ የመረጃ መለዋወጫ ዘዴዎች አሉት።					
9.5.	ከሃገር ውስጥ ገቢ ጋር መረጃ መለዋወጥ ትክክለኛው የግብር መጠን እንዲወስን ይረዳል።					

**10. የግብር ከፍቶች በታክስ ስርዓቱ ላይ ያላቸው የፍትሃዊነት ጥያቄ፡-ከዚህ በታች ለተዘረዘሩት ዓ/ነገሮች መስማማት አለመስማማትዎትን ምልክት በማድረግ ይግለፁ፤**

ተራ.ቁ	ዓረፍተ ነገሮች	በጣም አልስማማም	አልስማማም	አስተያየት አልሰጥም	እስማማለሁ	በጣም እስማማለሁ
10.1.	ከሌሎች ግብር ከፋዮች አንጻር የእኔ ግብር ክፍያ የተሻለ ነው።					
10.2.	እንደኔ እምነት የግብር ስርዓቱ ፍትሃዊ አይደለም።					
10.3.	ከገቢዎች ባለስልጣን የሚሰጠው የግብር መረጃ ለሁሉም ግብር ከፋዮች በቂና እኩል ነው።					
10.4.	እንደኔ እምነት ድንገተኛና አስፈላጊ አዲት እንዲሁም ተመጣጣኝ ያልሆነ ቅጣት ግብር ከፍቶን ለጭንቀትና በስርዓቱ ላይ ዕምነት ማጣትን ያስከትላል።					
10.5.	እንደኔ እምነት በመተግበር ላይ ያለው የታክስ ስርዓት ብዙ ቀዳዳዎች ያሉትበትና ወዳልተፈለገ ሙስናና ታክስ ማጭበርበር የሚዳርግ ነው።					

**11. በዙሪያችን ያሉ ግለሰቦች አስተዋፅኦ:-** ከዚህ በታች ለተዘረዘሩት ዓ/ነገሮች መስማማት አለመስማማትዎን ምልክት በማድረግ ይግለፁ፤

ተራ. ቁ	ዓረፍተ ነገሮች	በጣም አልስማማም	አልስማማም	አስተያየት አልሰጥም	እስማማለሁ	በጣም እስማማለሁ
11.1.	በአከባቢያችን ያሉ ግለሰቦች መልካም አመለካከት ግብራችንን ባግባቡ እንድንከፍል ይረዳናል።					
11.2.	መልካም ግብር ከፋዮችን መሸለም ወይም ዕውቅና መስጠት በግብር አከፋፈል ስርዓቱ ላይ የራሱ የሆነ አስተዋፅኦ አለው።					
11.3.	ግብር መክፈል ግዴታዬ ሲሆን በዙሪያዬ ያሉ ሰዎችን አልመለከትም።					
11.4.	በአከባቢዬ ያሉ ግብር ከፋዮች ግብርን ያጨበረብራሉ ወይም ያለባቸውን ትክክለኛ ግብር ለመንግስት አያሳውቁም።					
11.5.	እኔ ግብርን አላጭበረብርም ምክንያቱም ማንነቴ አይፈቅድም እንዲሁም ግብር ማጭበርበር ውስጣዊ እርካታ አይሰጠኝም።					

**12. የግብር ከፋዮች የገቢ መጠን:-** እባክዎን ከዚህ በታች ለተዘረዘሩት ዓ/ነገሮች መስማማት አለመስማማትዎን ምልክት በማድረግ ይግለፁ፤

ተራ. ቁ	ዓረፍተ ነገሮች	በጣም አልስማማም	አልስማማም	አስተያየት አልሰጥም	እስማማለሁ	በጣም እስማማለሁ
12.1.	አሁን ላይ ያለው የግብር ስርዓት የገንዘብ ዋጋ ማጣትን ያገናዘበ አይደለም።					
12.2.	ተግባራዊ በመሆን ላይ ያለው የታክስ መጠን ከፍ ያለና የግለሰቦችን የገቢ ምንጭ ያገናዘበ አይደለም።					
12.3.	የተሰማራሁበት የስራ ዘርፍ ትክክለኛውን የግብር መጠን እንድከፍል ይረዳኛል።					
12.4.	ግብርን በአገባቡ መክፈል የድርድትን ህልውና ይፈታተናል።					
12.5.	በመተግበር ላይ ያለው የታክስ ስርዓት ድርጅቶች ያለባቸውን ዕዳ በፈቃደኝነት እንዲከፍሉ ያበረታታል።					

**13. ድርጅቱ በታክስ ባለሙያዎች ይመረመራል እና እቀጣለሁ ብሎ ማሰብ፡-** እባክዎን ከዚህ በታች ለተዘረዘሩት ዓ/ነገሮች መስማማት አለመስማማትዎን ምልክት በማድረግ ይግለጹ፤

ተራ. ቁ	ዓረፍተ ነገሮች	በጣም አልስማማም	አልስማማም	አስተያየት አልሰጥም	እስማማለሁ	በጣም እስማማለሁ
13.1.	ግብራን የምክፍለው በወንጀል እጠየቃለሁና እቀጣለሁ ብዬ በማስብ ነው።					
13.2.	የሃገር ውስጥ ገቢ ሰራተኞች በየጊዜው ቁጥጥር ያደርጋሉ ስለዚህ ግብር እንዳይከፈል የሚያደርግ ምንም ክፍተት የለም።					
13.3.	ግብርን መክፈል የሀቀኛ ሰዎች መገለጫ ነው።					
13.4.	ግብራን የምክፍለው ከሃገር ውስጥ ገቢ የማገኘውን ማበረታቻ በማሰብ ነው።					
13.5.	አሁን ላይ ያለው የግብር ስርዓት፣ ለመረዳት የሚያስቸግርና ግብር ከፋዮችን ለቅጣት የሚዳርግ ነው።					

**14. የግብር ከፋዮች በመንግስት ውጪ ስርዓት ላይ ብቻ እርግጠኝነት፡-** እባክዎን ከዚህ በታች ለተዘረዘሩት ዓ/ነገሮች መስማማት አለመስማማትዎን ምልክት በማድረግ ይግለጹ፤

ተራ. ቁ	ዓረፍተ ነገሮች	በጣም አልስማማም	አልስማማም	አስተያየት አልሰጥም	እስማማለሁ	በጣም እስማማለሁ
14.1.	እንደኔ እምነት መንግስት የሰበሰበውን ግብር ባግባቡ በስራ ላይ ያውላል።					
14.2.	እንደኔ እምነት ድርጅቱ መንግስት ለዋና ዋና አገልግሎቶች ማለትም ለትምህርት፣ ለጤና ወዘተ ከሚያወጣው ወጪ ተጠቃሚ ነው።					
14.3.	በዋና ዋና የህዝብ አገልግሎቶች ላይ ግብርን ማዋል ግብር ከፋዮችን ግብራቸውን በራሳቸው ተነሳሽነት እንዲከፍሉ ያደርጋቸዋል።					
14.4.	የግብር ሰብሳቢዎች ያልተገባ ባህሪ ግብር ከፋዮችን ግብራቸውን ባግባቡ እንዳይከፍሉ ያደርጋል።					
14.5.	ምንም እንኳን መንግስት የሰበሰበውን ግብር ባግባቡ አዋል አላዋለ ግብር መክፈል ግዴታዬ ነው።					

**ክፍል III ያለዎትን አስተያየት ይስጡ**

15. እባክዎ በግብር ከፋዮች ግብር የመክፈል ባህል ላይ ተፅኖ በሚያደርጉት ፋክተሮች(Factors) ዙሪያ ያለዎትን አስተያየት ይስጡ:-

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16. የትርፍ ግብር ከፋዮችን ግብር የመክፈል ባህል ያሻሻላል ወይም አስትዋፅኦ ያደርጋል የሚሉት ሀሳብ ካለዎት ቢገልፁ::

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17. ሌላ መግለፅ የሚፈልጉት ጉዳይ ካለ::

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### **Appendices 3- In-depth Interviews – To Addis Ababa City Business profit Taxpayers’**

1. Do you have any idea about the overall tax system of business profit taxpayers?
2. Does your business comply with the tax legislations? If yes what are the motivating factor contributing to your tax compliance behaviours?
3. If you have given an opportunity to improve the current tax system what do you do to improve the tax compliance behaviour of business profit tax payers?
4. Do you think tax knowledge affects the tax compliance behaviour of business profit taxpayers?
5. Do you think the current tax system is fair and considers the income earning capability of business profit tax payers?
6. Do you think the influence of peer groups affects the tax compliance behaviour of business profit tax payers?
7. Do you think income level of taxpayers (i.e. low, middle and high) affects the tax compliance behaviour of business profit tax payers?
8. Why do you comply with the tax legislations? Is it because of fear of detections and punishments? Or complying with the tax legislation is your morale obligations?
9. Do you think the government spends all the collected funds wisely and to the benefits of the society?
10. Do you perceive that you are benefiting from basic infrastructures such as education, health, safety and etc?
11. Do you think paying taxes are your obligation whether the government spends wisely or not?
12. Do you have any other suggestion or comments regarding about tax compliance behaviour of business profit tax payers?

**Appendices 4: SPSS Data Outputs**

**1. Correlation among variables**

		Correlations							
		Tax Compliance	TK	BF	PG	IL	DP	GS	
Pearson Correlation	Tax Compliance	1.000	.327	.531	.474	.451	.314	.392	
	TK	.327	1.000	.343	-.277	-.113	.083	-.052	
	BF	.531	.343	1.000	.122	.086	.120	.235	
	PG	.474	-.277	.122	1.000	.429	-.026	.503	
	IL	.451	-.113	.086	.429	1.000	.302	.315	
	DP	.314	.083	.120	-.026	.302	1.000	-.025	
	GS	.392	-.052	.235	.503	.315	-.025	1.000	
Sig. (1-tailed)	Tax Compliance	.	.003	.000	.000	.000	.004	.000	
	TK	.003	.	.002	.010	.175	.248	.333	
	BF	.000	.002	.	.157	.238	.161	.025	
	PG	.000	.010	.157	.	.000	.416	.000	
	IL	.000	.175	.238	.000	.	.005	.004	
	DP	.004	.248	.161	.416	.005	.	.420	
	GS	.000	.333	.025	.000	.004	.420	.	

\*\* . Correlation is significant at the 0.01 level (2-tailed).

\* . Correlation is significant at the 0.05 level (2-tailed).

**2. Model Summary- Regression results**

**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.809 <sup>a</sup>	.654	.621	.326	.654	19.883	6	142	.000	1.851

a. Predictors: (Constant), GS, DP, TK, BF, IL, PG

b. Dependent Variable: Tax\_Compliance

**Model Summary**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	12.677	6	2.113	19.883	.000 <sup>b</sup>
	Residual	6.695	146	.106		
	Total	19.371	152			

a. Dependent Variable: Tax\_Compliance

b. Predictors: (Constant), GS, DP, TK, BF, IL, PG

**Stepwise Regression results**

**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.531 <sup>a</sup>	.282	.271	.452	.282	26.677	1	68	.000
2	.672 <sup>b</sup>	.452	.436	.398	.170	20.827	1	67	.000
3	.742 <sup>c</sup>	.551	.531	.363	.099	14.574	1	66	.000
4	.786 <sup>d</sup>	.619	.595	.337	.067	11.485	1	65	.001
5	.807 <sup>e</sup>	.651	.624	.325	.032	5.936	1	64	.018

- a. Predictors: (Constant), BF
- b. Predictors: (Constant), BF, PG
- c. Predictors: (Constant), BF, PG, TK
- d. Predictors: (Constant), BF, PG, TK, IL
- e. Predictors: (Constant), BF, PG, TK, IL, DP

**ANOVA<sup>a</sup>**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.458	1	5.458	26.677	.000 <sup>b</sup>
	Residual	13.913	152	.205		
	Total	19.371	153			
2	Regression	8.758	2	4.379	27.641	.000 <sup>c</sup>
	Residual	10.614	151	.158		
	Total	19.371	153			
3	Regression	10.677	3	3.559	27.018	.000 <sup>d</sup>
	Residual	8.694	150	.132		
	Total	19.371	153			
4	Regression	11.983	4	2.996	26.354	.000 <sup>e</sup>
	Residual	7.389	149	.114		
	Total	19.371	153			
5	Regression	12.610	5	2.522	23.871	.000 <sup>f</sup>
	Residual	6.762	148	.106		
	Total	19.371	153			