

EFFECTIVENESS OF TAX AUDIT: A STUDY IN KEMBATA TEMBARO ZONE, SOUTHERN ETHIOPIA

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Abstract

Purpose- The aim of the study is to assess factors affecting tax audit effectiveness as effective tax audit enhances tax administration.

Research methodology – To achieve objective of the study, both qualitative and quantitative research methods have been employed. The Sample respondents selected for the study were 146 by employing purposive sampling technique out of which 106 questionnaires were returned back. Descriptive statistic and multiple linear regression analysis via Statistical Package for Social Science (SPSS) Version 20.0 were employed.

Findings- The result revealed that management support, audit quality, taxpayers' awareness, and standardized integrated government tax administration system have statistically significant positive effect on audit effectiveness, while tax law complexity and tax accounting and reporting have statistically significant negative effect on tax audit effectiveness.

Research limitations- The empirical research was carried out on tax audit effectiveness by using tax officials who are working in Tax Authority, but it did not include taxpayers in the study. Because of this and limited scope of the study area may not ensure that the indicated results are characteristic for the tax audit activity in Ethiopia at national level. Future researchers on the topic can include taxpayers' opinion and widening the scope of the study area.

Practical implications- It is recommended that the concerned authority should simplify the area of complex tax laws and encourage taxpayers who declare using relatively good accounting system by assessing tax on their accounting records rather than assessing by estimation. In addition, assessing tax on the specified period of five years to save taxpayers from the unnecessary burden of penalty and interest.

Originality/Value- Previous studies did not address effect of tax audit in tax administrative functions on taxpayers' registration, return reporting and effect of SIGTAS on tax audit.

Keywords: *Kembata Tembaro Zone, Revenue Generation, Self-Assessment, Tax Assessment, Tax Audit, Tax Estimation*

JEL Classification: H25

1. Introduction

Tax is a pecuniary burden levied upon individuals or property to support the government, and its payment exacted by legislative authority (Aronson, 1985). It is compulsory payment which is related with certain business activities. Revenues collected via taxation are used to buy the inputs essential to provide government supplied goods and services or to reallocate purchasing power among peoples (Hyman, 2011). According to Bird (2010), political willingness, a clear strategy and adequate resources are ingredients that are essential to effective tax administration. Unfair and unpredictable tax administration might bring tax system into disrupt and deteriorate legality of government.

Registering for tax; filling tax returns on time; correctly reporting tax liabilities; and paying taxes on time are four universal classes of obligation likely exist for almost all taxpayers (OECD, 2014). An examination of whether a

taxpayer has appropriately assessed and declared their tax liability and fulfilled other tax legislative responsibilities is referred as tax audit. Effective audit of tax can significantly contribute to the administration of the tax system. Tax administration and tax revenue collection of the government improved by the efficient and effective tax audit. Specifically, a tax audit supported by information technology plays vital role (Zabihollah, Ahmad, Rick & Peter, 2018). Weak tax administration can make unfair competition among taxpayers and cannot address the problem of tax avoidance and evasion (Organization for Economic Cooperation and Development (OECD), 2006).

According to Ethiopia Constitution HPR (1994), Proclamation No 1/1994), there are political, economic, social, cultural and environmental objectives of taxation. The implementation of tax legislation helps for attainment of the government objective. In order to achieve such objectives, a good tax system contributes a lot which require citizens understanding of the tax laws of the country. Major components of the reform in 1990 to 2003 had given due attention on dropping income tax rate of corporation from 35% to 30% and the upper limit of income tax rate for individual taxpayers and associations who are not categorized under corporation from 40% to 35% and replacement of sales tax with VAT and TOT (Geda & Shimeles, 2005). According to Export Initiative and Partnerships Division (2016), fiscal deficit in 2013/14 was 2.6% of GDP and projected to remain for coming years. Tax revenue to GDP ratio is 12.7%, which is much bellow from sub-Saharan Africa average of about 20%. Also tax revenue covers 84.2% of the total government revenue, which requires high mobilization of tax revenue through effective tax administration and dynamic tax reforms. According to Birskyte, (2013), tax audit increases the revenue of the government directly and detect taxpayers who fail to fulfill tax obligation and may impose penalty and fines.

2. Statement of the Problem

Tax reform in Ethiopia focus on three broad categories in addition to the administrative reform: they are taxes on income and profits, taxes on goods and services and taxes on international trade. Major components of the reform in 1990 to 2003 were due attention on dropping income tax rate of corporation from 35% to 30% and the upper limit of income tax rate for individual taxpayers and associations who are not categorized under corporation 40% to 35%. Subsequent to this reform, HPR (2002a) Income Tax Proclamation 286/2002, HPR (2002b) Turnover Tax Proclamation No 308/2002, HPR (2002c), Value Added Proclamation No 285/2002 and other tax law issuance and amendments of existing tax laws have been undertaken in the country (Geda & Shimeles, 2005).

Some empirical studies have been undertaken in the tax audit practice, effectiveness of tax audit practice, impact of tax audit in revenue generation and factors affecting the tax audit practice (Ayalew, 2014; Adediran, Alade & Oshode, 2013); Bibisso, 2014; & Mihret, 2011. However, neither of these studies have addressed the effect of tax audit in the tax administrative functions on taxpayers' registration, declaration of return and financial reporting. Moreover, the effect of SIGTAS in the effectiveness of tax audit practice has not been addressed on those studies. Therefore, the main objective of this study is to investigate detrmnats of tax audit effectiveness taking evidence from Kambata Tembaro Zone, Ethiopia.

3. Literature Review

3.1. Tax Audit Effectiveness (TAE)

According to Chen (2013), tax audit is aimed to enhance the compliance behavior of taxpayers with the tax legislations in the self-assessment system. Specifically, Clement, Stephen, Festus (2018) found that effective field tax audit has significant positive impact on tax productivity in Nigeria. Similarly, Zakir (2018) found that large corporate tax payers tend to comply with the tax law as a result of rigorous tax audit in Bangladesh. Tax assessors are required to undertake their responsibilities professionally and successfully to confirm that taxpayers are filling their tax requirements. On the other hands, a tax investigation is the procedure of gathering evidence to decide the projected quantity of tax evaded and the likely suit of taxpayers engaging in tax evasion endeavors.

Quality of tax audit focuses, on the targeted risk, technical correction, procedural correction and correct reference. Tracking of tax violation, non-compliance detection and additional revenue expected from tax audit are measures of tax audit effectiveness (Drogalas, Ioannis, Dimitra & Iohannis, 2015 & OECD, 2006).

Effective audit is truly challenging and examines the fillings of the financial transactions in order to give an opinion on whether taxpayers report an accurate and reasonable view. It is expected to fulfill with necessary auditing and ethical values. In addition, an effective audit activity modified for risks confronting the entity, the business arrangement and the government regulation, auditors should be equipped with theoretically and practically, knowledgeably inquisitive and free from biasness, its approach depending on an awareness of the regulatory environment and it must deliver the right audit opinion, in which investors have confidence (Hobbs, 2013).

The specific obligation of the taxpayers varies from one taxation role to another and from one jurisdiction to the next. The worldwide requirements are likely to exist for almost all taxpayers including, registration in the tax system; timely filing of tax returns; reporting of complete and accurate information in tax returns; and payment of tax obligations on time. These obligations measure the compliance outcome and that its best outcome represents the effectiveness and efficiency that could be expected (OECD, 2010).

In addition to the dependent variable explained above, the following independent variables that affect tax audit effectiveness were carefully selected from earlier researches and used in this study.

3.2. Management Support (MS)

The Tax Authorities audit efficiency and effectiveness activity determined by the nature and scope of powers in the fundamental legislation framework and greatly facilitated by information communication technology. Specifically, in this age of high competition and complex business world, use of information technology and audit software is becoming a necessity (Zabihollah, Ahmad, Rick & Peter, 2018). Now days, every business activity is integrated with IT using Enterprise Resource Planning (ERP), online marketing and online reporting. As a result, properly skilled IT auditors should be trained in order to enhance quality of financial reporting and auditing of business organizations (Barta, 2018). This implies, effective tax audit necessitates the support of higher management and resource allocation, competency of audit staff and quality of audit (OECD, 2006).

H1: Management support has significant positive relation to the tax audit effectiveness.

3.3. Audit Quality (AQ)

The audit quality is multifaceted and it has no worldwide meaning which debates among participants, officials, standard establishers, auditing companies and concerned bodies, and strategy setting. It can be attained when the investigators' judgment on the financial reports will be reliable upon as it was based on adequate and appropriate audit evidence gathered by an appointed audit team which reveals suitable outcome; adequately educated, well-informed and had enough time allocated to implement it. Functional thorough investigation process and quality control procedures provide valuable and timely reports and interacted appropriately with a variety of different stakeholders (International Auditing and Assurance Standards Board (IAASB), 2013).

Audit quality is delivering an appropriate professional opinion supported by necessary evidence and objective judgment. It is said quality audit when its report is independent reliable and supported by sufficient evidence. It also involves appropriate and complete reporting by auditors that enables the concerned body to discharge its responsibility. To this end, evidence should be sufficient in order to produce an objective judgment and complete reporting. Tax auditors should have strong evidence before deciding rejecting financial report prepared by business organizations. In this connection, Antonia and Cristina (2018) argued that income tax computed based on financial statement that is not reliable is by far better than levying tax based on subjective estimation. They further argued that presumptive taxation should be the last resort in tax levy and priority should be given to financial report whatever the quality might be. It can be derived from the philosophy within the audit firm, technical skill and personal quality of audit partner and staff, audit process effectiveness and audit reporting reliability and usefulness. Users of the audit report relay on giving robust and objective opinion in which financial statement indicates a fair and true view, prepared in line with applicable accounting framework and prepared in line with relevant legal requirement (Financial Reporting Council, 2006). In connection to this, Safa, Nadia and Faten (2017) found that quality of audit in Tunisian family businesses has reduced tax avoidance which in turn means achievement of audit effectiveness.

H2: Tax audit quality has a significant positive effect on the tax audit effectiveness.

3.4. Standardized Integrated Government Tax Administration System (SIGTAS)

Automation of the tax system can be used to perform the function of tax administration more rapidly, which enables easy detection of defaulters and reduces corruption by reducing personal contact between tax officials and taxpayers that is necessitated by inefficient manual systems. Automation by itself does not necessarily improve tax administration without the combination of the political willing and effective management system (Kayaga, 2007). According to Drogalas et al. (2015), effectively designed information technology enables tax auditor to track tax violation, which enhance tax audit effectiveness.

H3: Automation of tax system has significant positive effect on the tax audit effectiveness.

3.5. Taxpayers' Awareness (TPA)

According to Mukhtar, Abdi & Elmi (2015), conducting effective taxpayers' awareness, business owners gain more knowledge of tax and it is advantageous for them to comply voluntarily. On the contrary, the failure to create awareness for the taxpayers' result of continues failure of taxpayers to comply voluntarily in payment of taxes its consequence is painful losses with the government. Continues taxpayers' education and awareness about the rights and obligations build good relationships between taxpayers' and tax authority, which creates citizens who have better understanding about tax, which will bring about honest and voluntary compliance. Further, Diana (2016) argued that improving taxpayers attitude enhances the tax compliance behavior and he recommended that future researches should emphasis on mechanisms of enhancing tax payers attitude.

A tax practitioner prepares financial reports, that indicates a tax return or other data for declaration to tax authority, taxpayers are yet accountable for the accuracy of the income filing. The taxpayers might be responsible to administrative penalty and criminal penalty in the 'non- collaboration' group when he or she fails to wholly collaborate with the conduct of an intervention. Awareness of taxpayers' reduces administrative as well as the criminal penalty that faces for taxpayers'. According to Ola (2001), cited in Peter (2013), education about tax is a strategy which performed by a Tax Authority to ensure taxpayers' compliance.

Taxpayers' education is pillar to effective and efficient tax administration function. Susan, Tim and Marty (2017) argued that tax payers should believe that any tax levy by the government is faire and equitable as much as possible. Taxpayers are expected to understand the tax laws, regulation and procedure how computations and assessments will be for the tax they are going to pay. These tax legislatives and rules should be straightforward, clear and understandable in order to improve tax compliance. The awareness creation and education Taxpayers enhance the altitude of voluntary tax compliance and reduce tax avoidance and evasion (Olowookere, 2013).

H4: Awareness of Taxpayers has significant positive relation to the tax audit effectiveness.

3.6. Tax Legislations Complexity (TLC)

Tax laws and procedures should be simple taxpayers to comply with their obligations and access their entitlements; taxpayers may not voluntarily comply if the tax system itself makes it too difficult or too expensive for them to meet their obligations. Antonia and Cristina (2018) found that significant amount of tax evasion in Portuguese as a result of complex tax laws they are having. Tax legislation is expected to be simple for tax officials, so that tax inspectors and experts would not have to devote their time on the interpretation of tax proclamations and regulations. Effectiveness of tax audit will be subjective as a result of complex tax laws; since complicated legislation significantly affects compliance (Drogalas et al. (2015).

Effective tax audit necessitate audit program to be supported by legislative framework, which requires taxpayers' to maintain appropriate books and records; provides the administration with adequate powers to conduct wide ranging inquiries; allows delegation of the powers to staff conducting audits; allows reconstruction of income and reassessments of tax using a range of methods and techniques within a generous timeframe; gives taxpayers a right of appeal, places a burden of proof on the taxpayer; and applies sufficient penalties to deter noncompliance (Forum on Tax Administration's, 2006).

H5: Complexity of tax legislation has significant negative effect on the tax audit effectiveness.

3.7. Tax Accounting and Reporting (TAR)

The presentation of uniform financial reporting framework enhances transparency and responsibility by centralizing financial reporting. It is pillar to support the economy and reduce the risk of economic crisis, business malfunction' and related negative economic impact; it also ensures the provision of financial information meets internationally recognized reporting standards (HPR, 2014).

Except category "C" taxpayer category "A" and "B" are required to maintain books and accounts records by having vouchers authorized by tax authority. The accounting method to determine the income generates and expense rendered in the tax period shall be made in generally accepted accounting principles. The accounting methods in the Ethiopian income tax proclamation specifies taxpayers to compute some transactions in line with accounting principles and income tax legislations, i.e. inventory shall be valued at average method; depreciation expense shall be in the straight line method, bad debt shall be deductible when any lawful act to collect the money owing is undertaken, however, liability is not recoverable, etc. Financial reporting standard enhances shareholders value and benefits investors, lenders; other capital providers as well as reduce cost of compliance facilitate education and training (Pacter, 2011). In connection to this small and medium enterprise in Malaysia who did not keep book of account evade to much tax and the researchers recommended that government should make it an obligation to prepare financial report though it may not be to the standard (Azhar, Mohd & Zarinah, 2016).

H6: Tax accounting and reporting has significant positive relation to the tax audit effectiveness.

4. Research Design And Methodology

This study is designed to identify factors affecting tax audit effectiveness significantly by employing explanatory research design. Purposive sampling technique has been adopted in order to address the tax officials who have direct relation with the tax audit practice. Accordingly, the participants for the study were the tax auditors, tax assessment and collection officials, taxpayers' education officials, including the job process owners and head of the Tax Authorities. However, sample for the study did not include the taxpayers. Out of the 146 questionnaires distributed, 106 questionnaires were returned back from the respondents with the response rate of about 73%. According to the Stevens (1996), cited in Pallant (2005), generalization cannot be repeated for other samples with small sample size. It is scientific to take sample of 15 for each predictor variable, accordingly the number of sample size is greater than fifty plus eight times the number of independent variable in the study. The data collected from 106 respondents with the response rate of 73% is sufficient to generalize about the study, because the numbers of predictor variables in the study are six. To undertake the study primary data were gathered via questionnaire and interview in 2017. Semi-structured interview has been conducted to 6 tax auditors and 2 audit team coordinator of the Tax Authority. The questionnaire was developed considering all variables to be analyzed.

According to Kothari, (2004) the sample should be optimal which satisfies the necessities the efficient, representation and consistency. Whereas determining size of the sample from the population, the investigator should decide the desired accuracy as similarly a tolerable confidence level for approximation. Sample size is the subjective to researcher rather than objective determination based on designing formula for calculation. According to Yamane (1967)), sample size can be computed in the formula,

$$n = \frac{N}{1 + N(e)^2} \quad (1)$$

Where, n is sample size of the study

N is the population of the study

e is level of precision

To this study the sample size computed as: $n = \frac{232}{1 + 232(0.05^2)} = \frac{232}{1 + 232 \cdot 0.0025} = \frac{232}{1.58} = 146$

It is important to set structure of the dependent variable and explanatory variables with their measurements in order to interpret the findings of the study. This analytical framework indicates the reflection of independent variables on the dependent variables via mechanisms and achievement of a tax audit. Based on the literatures defined in the model specification part of the study, the following analytical framework has been developed to show the independent variables and mechanisms to achieve revenue via tax audit.

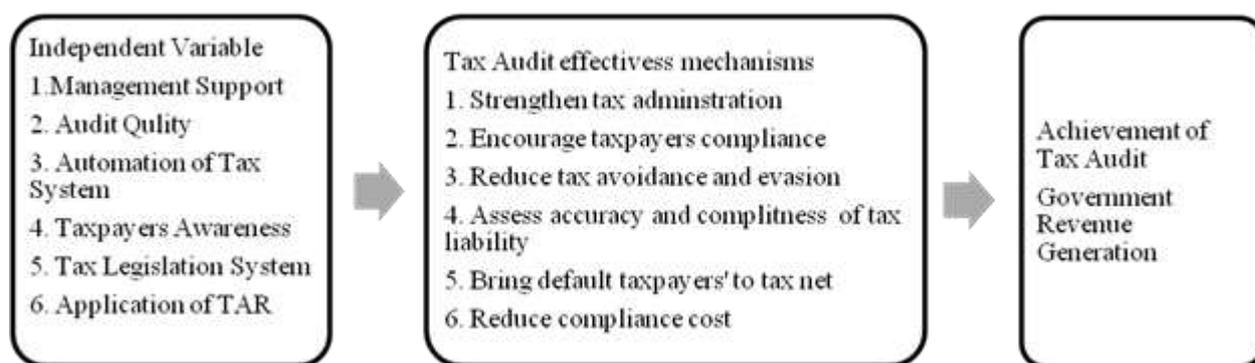


Figure 1: Analytical Framework based on Literature on the Model Specification

4.1. Measures of Dependent and Independent Variables

Tax audit effectiveness is dependent variable. Questionnaires were included to evaluate the tax audit effectiveness in terms of tracking of tax violation, non-compliance detection, additional revenue and other tax audit related issues. Each item of tax audit effectiveness will be measured on a 5-point Likert scale ranging from (1) ‘strongly disagree’ to (5) ‘strongly agree’.

Management support, audit quality, automation of the tax system, awareness of taxpayers’, and tax legislation are investigated as having a direct impact on tracking of tax violation, non-compliance detection and other tax audit related issues. To create a proper measure of independent variables employed in a tax audit, the questionnaires were prepared for each independent variable in the measurement scale of Likert scale ranging from (1) “strongly disagree” to (5) “strongly agree”. Level of agreements will be arranged strongly agree (5), agree (4), neutral (3), disagree (2), and strongly disagree (1).

Data has been analyzed on quantitative basis using Pearson’s correlation, linear regression analysis and descriptive statistics. Moreover, the researcher has undertaken the diagnostic tests for the assumption of the classical linear regression model (CLRM).

Based on the nature of the data collected through questionnaire and semi-structured interview and document review, the descriptive as well as the inferential statistical tools were employed to analysis and presentation of data. Before starting analysis, data has been checked for consistency and completeness and then labeled and entered into a computer, and then it has been processed and analyzed using SPSS Software version 20.

The data obtained about the effectiveness of tax audit have been analyzed via multiple linear regression technique to determine the significance of the independent variables on the dependent variable. Multiple regression analysis has been employed to estimate the magnitude of the effect of the independent variable on dependent variables. Ordinary least squares (OLS) regression model is specified as follows:

$$TAE = \beta_0 + \beta_1 MS + \beta_2 AQ + \beta_3 SIGTAS + \beta_4 TPA + \beta_5 TLC + \beta_6 TAR + \epsilon_i \dots \dots \dots (2)$$

Where: TAE = Tax Audit Effectiveness
 MS = Management Support
 AQ = Audit Quality
 SIGTAS = Standardized Integrated Government Tax Administration System
 TPA = Taxpayers Awareness
 TLC = Tax Legislation Complexity
 TAR = Tax Accounting and Reporting
 = Random Error
 = constant

The coefficients $\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ and β_6 are the parameters of the predictor variables.

5. Result And Discussion

Degree of correspondence between the ordering of two random variables will be measured by correlation. The value of Pearson’s correlation coefficient ranges between -1 and +1, which is an arithmetical measure of the strength of a linear relationship between paired data. The positive sign of correlation designates the increase of a variable increases the other variable and vice-versa, whereas, the negative correlation sign shows the increase of a variable decreases the other variable and vice-versa as well as no correlation means the effect of one variable has no effect on the other variable by either increase or decrease

Table 1: Correlation between Variables

		TAE	MS	AQ	SIGTAS	TPA	TLC	TAR
TAE	Pearson Correlation	1						
MS	Pearson Correlation	.332**	1					
AQ	Pearson Correlation	.518**	.365**	1				
SIGTAS	Pearson Correlation	.341**	.269**	.364**	1			
TPA	Pearson Correlation	.453**	.256**	.454**	.249**	1		
TLC	Pearson Correlation	-.319**	.006	-.078	-.011	-.050	1	
TAR	Pearson Correlation	-.190	.235*	.138	.143	.087	.224*	1

** . Correlation is significant at the 0.01 level (2-tailed). * . Correlation is significant at the 0.05 level (2-tailed).
 Source: Field Survey, 2017

As it has been revealed in the correlation table about the relationship between dependents and independent variables, among the independent variables, TLC and TAR have inverse relation with the TAE. On the contrary, MS, AQ, SIGTAS and TPA have positive relationship with TAE. The correlation between TAR and TAE is -0.190 and the correlation values between TAE and other independent variable are in the range of 0.319 to 0.519. According to Pallant (2005), the correlation between variables ranged in $r = \pm 0.10$ to ± 0.29 are small, $r = \pm 0.30$ to ± 0.49 are medium and $r = \pm 0.50$ to ± 1.0 are large. Except TAR which is found in the small correlation value range, the correlation of other independent variables and TAE were in the range of medium and large. These indicate that TAR was weak negative relationship with the TAE and MS, SIGTAS and TPA were medium and AQ has high positive relationship with TAE. On the other hand, TLC was negative relationship with medium range of correlation with

TAE. There was significant correlation between tax audit effectiveness and predictor variables with ($p < 0.01$) except TAR. TAE significantly correlated with MS ($r = .332$), TAE and TAQ ($r = .518$), TAE and SIGTAS ($r = .341$), TAE and TPA ($r = .453$) and TAE and TLC ($r = -.319$). Also the association between two predictor variables is below 0.454 which is far below the limit of multicollinearity diagnosis value of 0.7.

5.1. Regression Result on the Tax Audit Effectiveness

Effective application and implementation of the tax audit can be enhanced by the scope of powers in the fundamental lawful outline, that provides the appropriate influences for getting evidence and a reasonable regime of penalty to discourage and fine taxpayers' who fail to comply with tax law. Effectively carried out tax audit can reduce tax evasion and avoidance, detect compliance, establish viable and effective tax administration, bring default taxpayers to tax net, verify completeness, correctness and timely filing of returns, teach taxpayers and differentiate the areas of tax laws which necessitate clarification for the concerned party (OECD, 2006).

The following section discusses the model summary, ANOVA and the coefficients of variables.

Table 2: Model Summary^b

R	R Square	Adjusted Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
				R Square Change	F Change	df1	df2	Sig. Change	
.709 ^a	.503	.473	.63194	.503	16.713	6	99	.000	1.664

a. Predictors: (Constant), TAR, TPA, SIGTAS, TLC, TMS, AQ

b. Dependent Variable: TAE

Source: Field Survey, 2017

The model summary box outlines the overall fitness of the model. The model summary shows the amount of variation in the explained variable by the predictor variables. The above model summary table shows that tax audit effectiveness and six explanatory variables were significantly associated with the correlation coefficient $R = .709$. The model summary table also shows the model of tax audit effectiveness with the coefficient of determination $= .503$. The coefficient of determination specified that 50.3% of the deviation in tax audit effectiveness for the 106 responded tax officials explained by variations in practices of management support, audit quality, standardized integrated government tax administration system, taxpayers' awareness, tax legislation complexity and tax accounting and reporting while 49.7% remains unexplained. According to Singh (2007), an adjusted R square of above 75 percent is very good; adjusted R square values in the range of 50–75 percent is good; adjusted R square values in the range of 25–50 percent is fair and adjusted R square value below 25 percent is poor. Therefore, the adjusted R square of this study is 47.3% which is in the range of fair but it approaches to the range of good.

Table 3: ANOVA^a

Model	Sum of Squares	Df	Mean Square	F	Sig.
Regression	40.045	6	6.674	16.713	.000 ^b
Residual	39.535	99	.399		
Total	79.580	105			

a. Dependent Variable: Tax audit Effectiveness

b. Predictors: (Constant), TAR, TPA, SIGTAS, TLC, MS, AQ

Source: Field Survey, 2017

The ANOVA table above reveals that the summary of analysis of deviation and F-statistics, which discloses the value of $F(6, 99) = 16.713$, $p < .0005$ which represents significant at 0.0001. The result for F value is large because F-calculated is greater than table value of $F(6, 99) = 2.29$ it can be concluded that the set of independent variables (MS, AQ, SIGTAS, TPA TLC and TAR) as a whole were contributing to the variance of tax audit effectiveness and consequently, the model shows the real practice of the tax audit for the study.

Table 4: Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	95.0% Confidence Interval for B		Collinearity Statistics	
	B	Std. Error	Beta			Lower Bound	Upper Bound	Tolerance	VIF
(Constant)	1.365	.463		2.951	.004	.447	2.283		
MS	.265	.115	.181	2.298	.024	.036	.493	.808	1.237
AQ	.409	.115	.305	3.548	.001	.180	.637	.680	1.472
SIGTAS	.166	.082	.157	2.026	.045	.003	.329	.836	1.197
TPA	.238	.079	.241	3.008	.003	.081	.396	.778	1.285
TLC	-.231	.076	-.222	-3.039	.003	-.383	-.080	.937	1.067
TAR	-.298	.083	-.269	-3.569	.001	-.463	-.132	.885	1.130

a. Dependent Variable: Tax audit Effectiveness
Source: Field Survey, 2017

Econometric Model from SPSS Result:

$$TAE = 1.365 + .181MS + .305AQ + .157SIGTAS + .241TPA - .222TLC - .269TAR$$

Where, MS= Management Support, AQ=Audit Quality, SIGTAS=Standardized Integrated Government Tax Administration System, TPA=Taxpayers Awareness, TLC=Tax legislation complexity and TAR=Tax Accounting and Reporting.

Multiple regressions were employed to investigate the effect of management support, tax audit quality, standardized integrated government tax administration system, taxpayers' awareness, tax legislation complexity and tax accounting and reporting to predict levels of tax audit effectiveness. Employing multiple regressions necessitate variables to satisfy the assumptions of multicollinearity, autocorrelation, outliers and normality (Wooldridge, 2013).

Introductory analysis was conducted to check violation for assumptions of outliers, normality, multicollinearity, autocorrelation and data reliability. Also, the correlations between the predictor variables included in the study were examined. All independent variables in the study were statistically interrelated with tax audit effectiveness which shows that the data was appropriately associated with the dependent variable for investigation via multiple linear regressions.

In the table 4 above, all predictor variables were statistically significant with $p < .05$, ($.181$, $p = .024$), ($.305$, $p = .001$), ($.157$, $p = .045$), ($.241$, $p = .003$), ($-.222$, $p = .003$) and ($-.269$, $p = .001$). The results were confirmed the expected sign of hypothesis for all predictor variables, except the tax accounting and reporting.

5.2. Hypothesis Testing

It is necessary to test expected hypothesis of the multiple regression result of each predictor variables with the dependent variable.

5.2.1. Management Support (MS)

The political appointment of management as well as the employees of the Tax Authority exposes the revenue body to regular ruling party interfering. Tax legislations are not required to be forced powerfully in the cases of taxpayers with politically by the ruling party. As result, trustworthiness of Tax Authority hurts and worsens the voluntary taxpayers. In addition, political interference creates incredible self-doubt in the Tax Authority. The instability of Tax Authority affects organized remembrance and everyday works. The level of consideration by the governing party to the Tax Authority is vital for the Tax Authority to correctly assess, audit and collection based on the tax legislation. Low consideration to the Tax Authority, particularly in the high profile issues of tax evasion disturbs implementation activities and reflects an incorrect communication to the taxpayer society. Without strong participation of top governmental officials, the bringing the change expected to progress Tax Authority efficiency cannot be achieved (Gill, 2000). Political instability of government in a given country not only affect the financial system but also reduce citizens' trust on government. Trust on stability of the ruling party of a given country negatively affects the compliance of the taxpayers' (Simon James & Clinton Alley, 1999).

As it has been revealed table labelled coefficient, management support has positive relationship to the of effectiveness tax audit with ($\beta = .181, p = .024$), thus, expected hypothesis was strongly supported in the study. The result indicates when other predictors (TAQ, TPA, SIGTAS, TLC and TAR) were constant, for every increase of MS, the TAE increases by 0.181.

5.2.2. Audit Quality (AQ)

Audit is said quality, when its report is independent reliable and supported by sufficient evidence. It also involves appropriate and complete reporting by auditors that enables the concerned body to discharge its responsibility. To this end, evidence should be sufficient in order to produce an objective judgment and complete reporting. Audit quality can be resulting from the philosophy within the audit firm, technical skill and personal quality of audit partner and staff, audit process effectiveness and audit reporting reliability and practicality. Users of the audit report rely on giving robust and objective opinion in which financial statement indicates a fair and true view, prepared in line with applicable accounting framework and prepared in line with relevant legal requirement (Financial Reporting Council , 2006).

The presence of substantial misrepresentation of financial transactions which not distinguished by the investigators can be an indication for the failure audit activity. But, lack of substantial misrepresentations of financial statements is not the only evaluation technique of audit quality since there may have been no substantial misrepresentations to notice. Even the presence of a hidden substantial misrepresentation in the audited economic transactions may not necessarily show a poor quality audit as audits are intended to get relative, not absolute. The difference between complete and rational assurance is particularly applicable when misrepresentation result from frauds that is hidden via fake, collusion and deliberate misstatement (IAASB, 2013).

Coefficient table shows that tax audit quality was positively related to the tax audit effectiveness with ($\beta = .305, p < .001$) thus, expected hypothesis was strongly supported in the study with $p < 0.05$. The result indicates when other predictors (MS, TPA, SIGTAS, TLC and TAR) were constant or controlled the increase for every AQ, increases the TAE by 0.305.

Tax audit done by Tax Authority to examine the compliance of the taxpayers' to the HPR (2002a), Income tax proclamation No 286/2002, HPR (2002c), VAT proclamation 285/2002 and HPR (2002b) TOT Proclamation No 308/2002 Ethiopian tax laws, cross checked by the number of audit cases that submitted by the taxpayers' to the review committee with in ten days from the receiving assessment notice or submitted to appeal committee with in thirty days after the date of receiving decision of review committee and they can forward to the court when they are not satisfied with the decision of the appeal committee. As per the document review result indicates, in Kembata Tembaro Zone, all audited taxpayers submitted to the review committee with in ten days but no case of appeal has been submitted to the appeal committee or court because to provide appeal taxpayer is subject to the payment of half of the sum of tax, penalty and interest which is decided by review committee and to appeal the case to the court he/she is subject to pay all taxes, penalty and interest on the unpaid tax. This has been hindering the taxpayers

submitting the appeal to appeal committee as well as the court. The members of review committee are the tax officials who work in the office which makes the impartiality in question.

5.2.3. Standardized Integrated Government Tax Administration System (SIGTAS)

Information technology provides support for the registration of taxpayers', to issue identification number for taxpayer; authenticating and handling taxpayers returns and receiving tax payments via different networks; taxpayers account creation; identification of delinquent taxpayers; computerizing appeal tracking; and enables an improved service to taxpayers (Guillermo, Niall & Anton, 2013).

In the audit module, risk criteria are used to determine how files are selected for audit. A wide range of options exist. In this way, files are identified for audit, and transmitted to the audit manager for assignment to the audit team. According to Toro (2011) effective information technology reduces compliance costs, facilitate self-assessment and tax administration cost. Effective computer aided or information technology enhances tax auditors to detect violation of tax laws (Drogalas et al. 2015).

In the model, the standardized integrated tax administration system (SIGTAS) was significant at 5% significance level and positively related to the tax audit effectiveness with (.157, $p=.045$). This result shows, the increase of implementation standardized integrated tax administration system increases the effectiveness of tax audit. When other predictor variables controlled, the increase in SIGTAS by one unit increases the TAE by 0.157.

5.2.4. Taxpayers' Awareness (TPA)

According to Islamiah (2015), awareness taxpayers strongly influence the tax compliance. Taxpayers' awareness can be ensured by the early payment of tax, filing of their return, registration as the taxpayers' and reporting trend. Educating tax payer's is input for the effective administration which enhanced by the simple and clear tax legislation. The simplified tax legislation and the taxpayer's awareness about the tax rules and regulations improves the compliance. The degree of awareness about taxation is higher in the business students when compared to non-business students (Hastuti, 2014). Awareness of the taxpayers has positive and significant relationship with taxpayers' compliance (Islamiah, 2015).

As it has been shown in the coefficient table above, taxpayers awareness was positively related to the tax audit effectiveness with the (.241, $p=.003$), this implies the hypothesis is strongly supported with $p<0.05$. This means that the tax audit effectiveness strongly influenced by the taxpayers, the higher the awareness of taxpayers, then the effectiveness of tax audit will increase and vice-versa. On the other hand, for every additional awareness creation of taxpayers' by controlling other predictor variables, the tax effectiveness will be improved by 0.241.

5.2.5. Tax Legislation Complexity (TLC)

The ability of tax administrator to understand tax policy matters and enact tax legislation in a simple, precise language is very vital to the Tax Authority. Lack of clearness or complication in tax laws complicates taxpayers, bases for errors in tax revenues, rises cost of compliance and cost of administration and encourages non-compliance. Vagueness of tax legislation makes to reduce the common understanding between the Tax Authority and taxpayers of the given country, which consume massive organizational resources and interruption tax assessment, audit and tax collections. Moreover, the tendency of representatives to upsurge government revenue collection estimates to finance projects, rises the pressure on the Tax Authority to collect extra taxes revenue (Gill, 2000). According to Toro (2011), tax law simplification and implementation of tax system codes simplify the tax government and compliance with the tax laws. Tax procedure code strengthens administrative powers of audit and debts collection while keeping taxpayers' rights. It cannot be effective when, accompanying actions are absent and unwillingness to implement the rule of law and to levy the strictest of penalties. According to Baer (1997) simplification of tax system enhances effective and efficient tax administrations which encourages the voluntary compliance and reduce compliance cost of the taxpayers. On the contrary, complexity of the tax law increase cost of compliance and tax administration cost (Drogalas et al. 2015).

It is impossible to evaluate the effectiveness or success of tax administration without considering both the level of complication of the tax system and the extent that the tax system remains stable for the long period time. It is

essential to simplify tax payment procedures to taxpayers by removing demands for excess information in tax returns. As mentioned earlier, limiting the number of policy objectives and hence the number of tax expenditures, as well as being willing to accept only basic issues related to taxation that meet the objectives of Tax Authority. When a number of objectives like political, social and economic policy are combined into tax legislation, the result may cause the tax system to be too complex for both taxpayers and Tax Authority for the proper administration of tax. The issue of voluntary compliance will be in doubt when taxpayers find it hard to compute correct figure of their requirements appropriately and withholding, its verification becomes problematic when there are a number of tax exemptions and deductions (Bird, 2015).

In the regression analysis result, tax legislation complexity was negatively related to the tax audit effectiveness with ($-.222, p=.003$), which is strongly supported by stated hypothesis with $p<0.05$. The result supports the previous study which concludes the negative effect of complex tax legislation on the tax audit effectiveness (Drogalas et al., 2015). The result implies that when complexity of tax legislation increases by one more, the tax audit effectiveness will decrease by $.222$ by controlling other predictor variables. On the other hand, which means that the effectiveness tax audit is strongly affected by the complexity of tax legislation itself, the higher the level of complexity of tax legislations, then the level of TAE on the tax office in the Kembata Tembaro Zone will decrease.

5.2.6. Tax Accounting and Reporting (TAR)

The result revealed in the coefficient table, tax accounting and reporting standard was negatively related to the tax audit effectiveness with ($-.269, p=.001$), which did not support the stated hypothesis. The result indicates when taxpayers' use appropriate tax accounting and reporting standards as per the income tax laws, the tax audit effectiveness will be reduced and vice-versa. On the other hand, the one more appropriate use of tax accounting and reporting of taxpayers reduces the tax audit effectiveness by 0.269 , when other predictor variables are controlled or constant.

According to HPR (2002a) Income tax Proclamation No 286/2002, taxpayers required to prepare their financial statements in line with tax law and Generally Accepted Accounting principles. Accordingly, inventory should be computed in average valuation method, depreciation is expected to be valued at straight line method, and taxpayer shall account for tax purposes on a cash or accrual basis.

According to HPR (2002c) VAT Proclamation No 285/2002 (Art 29), HPR (2002b), TOT Proclamation No. 308/2002 (Art 11) and HPR (2002a) Income Tax Proclamation No 286/2002 (Art 69), after reviewing by the Authority, a person has understated his tax obligation, fail to maintain books of accounts and records or for any reason the records and books of accounts are unacceptable to the Tax Authority, or when taxpayer fails to declare his or her return in the time arranged by Proclamations, Tax Authority might assess tax liability by estimation by these Proclamations, the Tax Authority may assess the tax by estimation and shall issue an additional assessment within five years after the end of specified accounting period, but in the case of dishonesty or willful negligence, nevertheless any restriction in any other regulation, the tax assessment will be done at any time.

When taxpayer fails to maintain records and books of account, or for any motive, the books of account and records of taxpayers are not acceptable by the Tax Authority, or when taxpayer fails to proclaim his or her return in the time arranged by Proclamation, as a result Tax Authority might assess tax liability by estimation (2002a), Income Tax Proclamation No 286/2002 and HPR (2002c), VAT proclamation No 285/2002. According to Circular issued by SNNPR Revenue Authority (2006) Reference No 28/77/23/9/06 date 27/9/06 Ethiopian fiscal year. during the estimation of taxpayer who fail to maintain records and books of account auditors should understand about sales condition of taxpayer, sales transaction based on economic condition, number of taxpayer's customers, comparison of other similar taxpayers' transaction, bank transaction of the taxpayer etc. Taxpayers who their books of account and records fail acceptance by taxpayers subjected to pay tax which its computation is based on annual sale. To compute tax sales multiplied by taxable income rate which is for category "C" taxpayers without considering actual administrative cost and cost of purchase of goods or services. According to the circular issued on 03/12/99 reference number ፩፱/፭፱/180/632 and date 25/10/99 EFY (Ethiopian fiscal year) reference number ፳፱3/16/28/509 states category "C" taxpayers assessment to be done by taxable income range of 10% to 30%

according to the nature of business (for example coffee trade 10% of the sale as taxable income, pension 26%, general merchandise 14%, contractor 16%). When the accounting reports prepared by taxpayer fails acceptance by Tax Authority for any reason, category “A” and “B” taxpayers tax assessment subjected to the taxable income rate rather than the modification of the self-assessment of taxpayers (SNNPR Tax Authority, 1999).

Thus, when taxpayers use proper books of accounting and records they become eligible to reduce cost of production or cost of purchase and administrative expense as well as at the same time incurred loss can be off set against taxable income for the coming five tax periods, prior losses being set off before later losses. Net operating loss might be carried forward and subtracted only for two periods of three years, HPR (2002a), Income Tax Proclamation 286/2002 (Art 28) and Council of Minister (2002a), Income Tax Regulation 78/2002 (Art 12). Therefore, when taxpayers prepare financial statements based on knowledge, then reduce government revenue just by trying to find loopholes to avoid tax liability. As per the document review result of the tax audit report, out of audited taxpayers’ there were taxpayers whose self-assessment shows loss, but there were no taxpayers who privileged to the scheme of loss carry forward. The taxpayers’ tax assessment due to audit is based on highest sales of taxpayer by comparing number of alternative sales which found from monthly VAT report, quarterly TOT report, annual financial statement report, withholding, and other third party reports and converting highest purchase to sales based on taxable income rate which was designed for category “C” taxpayers’. Moreover, as it has been reported in the tax audit report Kembata Tembaro, Tax Audit has been carried out by estimation rather than books of account and records with modification. The taxpayers who innocently declared their sales were subject to more tax and unnecessary penalty and interest which do not encourage voluntary compliance.

Since the effectiveness of tax audit can be measured by reduction of tax evasion, reduction of tax avoidance, encouraging voluntary compliance and finally to generate tax revenue to support government expenditure. These can be done through auditing taxpayers with risk based selection criteria by discouraging those evaders and providing information to competent body to the area of tax law that has loophole to avoid tax and assessment of tax and penalty in the evaders. In the tax assessment by estimation scheme the evidences gathered from third party, financial statement of the taxpayer, monthly report of the taxpayer, quarterly report of the taxpayer, withholding report of the taxpayer, information gathered by interviewing taxpayers will be compared with each other and tax will be assessed by using highest sales or service revenue of the taxpayer by applying taxable income rate without considering the cost of purchase and administrative expense of taxpayer. Therefore, those who declared high sales or service revenue innocently have been taxed highly due to audit those who conceal their sales or service revenue subject to low tax liability, penalty and interest on unpaid taxes, which discourage voluntary compliance and make taxpayers to be out of the tax net.

6. Conclusion And Recommendation

Tax audit is one of the activities that helps to achieve the objectives of government revenue. The objective of study is to probe factors that significantly contribute to enhance effectiveness of tax audit. To address the objective of the study, data were gathered from primary sources. Based on the collected data, analysis and the findings of the study, the following conclusion and recommendation have been forwarded.

Expected hypothesis of each predictor variables with the dependent variable has been tested. Accordingly, the management support, audit quality, standardized integrated government tax administration system and taxpayers’ awareness were statistically significant factors that have been affecting the effectiveness of tax audit positively. On the contrary, tax law complexity and tax accounting and reporting were factors that significantly affecting the effectiveness of the tax audit practice negatively. Except tax accounting and reporting, all predictor variables result is the same with the expected hypothesis.

The simplification of tax laws and applicable regulations and directives are important to undertake effective tax administration and tax audit. Automation is essential element for modernizing tax administration in general and tax audit in particular. Tax auditors are not using SIGTAS software from the planning of the tax activity to the production of the audit report due to lack of assessing the financial statement of the taxpayers’ and document creation especially for business income tax and TOT. In principle appropriate tax accounting and reporting is expected to improve the effectiveness of the tax audit practice. But, in Kembata Tembaro Zone Tax Authority taxpayers who declare relatively better return and cost of goods purchase has been subjected to high tax liability,

interest on tax liability and administrative penalty than those who conceal their return and cost of goods purchase in their financial report.

Kembata Tembaro Zone Tax Authority should advance the factors positively affecting the effectiveness of the tax audit, such as management support, audit quality, standardized integrated government tax administration system and taxpayers' awareness in order to improve the effectiveness of tax audit practice and concerned Authority should simplify tax laws and change assessment trend based on taxable income rate of category "C" taxpayers in order to reduce the negative effect of tax law complexity and tax accounting and reporting variables on tax audit effectiveness. To ensure the fair, equitable and reduce subjective assessment of tax among taxpayers' concerned Authority should simplify tax laws and issue workable regulations especially to the TOT proclamation 308/2002, regarding to the administrative and criminal penalty fail to provide sales invoice for service provide and sales made. Since automation is essential element for modernizing of tax administration in general and tax audit in particular. The Tax Authority of Kembata Tembaro Zone should fulfil the computers, provide sufficient training to tax auditors in the SIGTAS software and create document number and make the assessment especially for business income tax and TOT. To levy and collect based on ability to pay principle, tax auditors should encourage those taxpayers' who maintain relatively proper books of account and recording to assess tax based on the return they provide and tax they declare with the modification rather than rejecting the self-assessment of taxpayers' and assessing based on taxable income rate of category "C" taxpayers which discourage voluntary compliance. Tax Authority should follow up the taxpayers' premises periodically and teach taxpayers' in order to improve taxpayers' record keeping nature and to get evidence about business transaction to assess tax based on either objective evidence or taxpayer's books of account/record by replacing the taxable income rate of category "C" taxpayers.

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