TAX AUDIT PRACTICE AND ITS SIGNIFICANCE IN INCREASING REVENUE: THE CASE OF BALE ROBE TOWN ADMINISTRATION

By: Eyob Negusie Haile

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Eyob Negusie Haile

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Principal Advisor: Fasil Ejigu (Assistant professor)

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Approved by Board of Examiners

1. **Advisor**

   Name: ------------------------------------ Signature: ----------------------- Date: -----------------

2. **Internal Examiner**

   Name: ------------------------------------- Signature: --------------------- Date: ------------------

3. **External Examiner**

   Name: -------------------------------------- Signature: --------------------- Date: -----------------

Statement of Declaration

I Eyob Negusie, hereby declare that this study entitled, **“Tax Audit Practice and Its Significance in Increasing Revenue: The Case of Bale Robe Town Administration”** is my original work. I have carried out the present study independently with the guidance and support of my research advisor, **Fasil Ejigu(Assistant professor)**. The study has not been submitted for award of any degree or diploma and that all sources of materials used for the study have been appropriately acknowledged.

Eyob Negusie

Signature: ----------------------

Date: ------------------------

Statement of Certification

This is to certify that Ato Eyob Nigussie has carried out his research work on the topic entitled

"Tax Audit Practice and Its Significance in Increasing Revenue: The Case of Bale Robe Town Administration" The work is original and is suitable for submission for the award of Master Degree in Accounting and Finance (M.Sc.).

Advisor: Fasil Ejigu(Assistant professor)

Signature: --------------------------

Date: -------------------------------

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ACRONYMS

AAA	–	*American Accounting Association*
AAA	–	*Amount After Audit*
ABA	–	*Amount Before Audit*
ANOVA	–	*Analysis of Variance*
CAAT	–	*Computer Assisted Audit Tool*
ERCA	–	*Ethiopian Revenue & Customer Authority*
IFAC	–	*International Federation of Accountants*
INTOSAI	–	*The International Congress of International Organization of Supreme Audit Institutions*
LTO	–	*Large Tax Payers Office*
MOFED	–	*Ministry of Finance & Economic Development*
OLS	–	*Ordinary Least Squares*
PITP	–	*Personal Income Tax Proclamation*
RTA	–	*Relevant Tax Authority*
SAI	–	*Supreme Audit Institution*
SPSS	–	*Statistical Package for Social Science*
TSCS	–	*Time Serious Cross Section*
VAR	–	*Vector Auto Regressive*
VAT	–	*Value Added Tax*

Abstract

The purpose of this study was to investigate tax audit practice and its significance in increasing revenue in Ethiopia in case of bale Robe town administration. This research work can give feedback to tax payers and the tax authority regarding the significance, application and practice of tax audit. The study also contributes in evaluating the prevailing tax audit practice and in making some adjustments on the existing tax audit systems. The researcher used a quantitative and qualitative research paradigm or the mixed research approach in integrated way since the primary goal of this research is to gain a better understanding of tax audit practice and its significance in increasing revenue in bale Robe town administration, it is impressive that the results obtained were generalizable to different types of organizations. As a result, the study adopted an explanatory research design which explains the tax audit practice and its significance in increasing revenue in bale Robe town administration. In this study the researcher used stratified random sampling because the technique requires dividing the population in to sub categories or strata before conducting the sample. The study used both primary and secondary data which were collected from Robe town administration. Tax audit should be carried out on a routine basis to ensure that actual revenue collected is what the relevant tax authority remits to the government. Regarding the impact of tax Audit on reduction of Tax Evasion and other fraudulent intensions, the survey indicated that the respondents are in agreement with the impact of tax Audit on reduction of Tax Evasion and other fraudulent intensions are high. Facilitation and Control, Increasing compliance, Bad auditing experience and Fear of Audit are issues which are raised as a result of tax audit which helps to reduce tax evasion.

Key words: Tax Audit Practice, Revenue, Robe Town Administration

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CHAPTER ONE

INTRODUCTION

1.1. Background of the study

According to Adediran *et al* (2013) governments devise suggests that to get generate revenue to undertake their responsibilities. Traditionally, this has been done through the levying of varied kinds of taxes. In pre-modern times, taxation was viewed as an immediate exchange of cut-price within which the onerous authorities on one hand, and also the tax payer or money handler on the opposite hand, every expected to receive equal profit in reference to what it gave out. Taxes were looked upon because of the wages paid to government for its services, the chief among them being security. This idea became called the „bargain theory (Danquah, 2007). The common read was that everyone was to produce all his wants otherwise he paid the government authorities to do that for him.

It has become tighter for governments everywhere the world to plan applicable suggests that of generating adequate revenue to finance their expenditure that still soar as a result of growth in population with its attendant demand for infrastructure and different social and economic investment. It's for this reason that taxation has become wrongfully accepted everywhere on the planet united of the foremost appropriate suggests that of generating revenue (Adediran *et al*., 2013).

According to (Brown et al, 2003) Today tax agencies generally lose some proportion of total revenues because of evasion and different kinds of rebelliousness called the "tax gap" The first goal of a revenue body's compliance activity is to enhance compliance with their tax laws, and within the method instill confidence within the community that the legal tax system and its administration are unit truthful, instance of failure to go with the law area unit inevitable, whether because of carelessness, foolhardiness, recklessness and deliberate evasion, or weaknesses in administration. To the extent that such failures occur, governments, and successively the communities they represent, area unit denied the tax revenues they have to produce services to citizens (Forum on tax administrations compliance, (2006). At a time once evasion techniques have mature additional refined, tax agencies have at the same time been hit with a cascade of monetary fund and staffing restrictions, regularly dynamic tax statutes and additional rigorous needs for privacy. As a result of these pressures, several tax agencies still consider audits of taxpayer's business records and monetary affairs to make sure taxpayers have computed there.

Tax due in accordance with current tax laws and rules and this means the tax revenues growth otherwise, tax agencies will lose vital revenue opportunities. (Brown et al, 2003)

When tax audit is well conducted, taxpayers perceive that their returns were quickly and scientifically analyzed, voluntary compliance rates could raises which might facilitate tax agencies to avoid prices and more improve revenue collections (Brown et al, 2003). Tax audit and compliance system, a comprehensive, integrated resolution designed to enhance tax auditor productivity and increase tax revenues.

In Ethiopia, taxes area unit thought considered about as a supply for growth and development. The tax revenues audit may be a vital issue to many African nations, also for gov't of Ethiopia. Tax revenues and different revenues are unit central to this current economic development agenda. They supply a stable flow of revenue to finance development priorities, like strengthening physical infrastructure, and area units interlocking with various different policy areas, from sensible governance and formalizing the Economy, to urging growth (Pfister, 2009).

A tax audit can modify the gov't of Ethiopia to manage and make sure the taxpayers compliance with tax laws therefore may increase tax income collected from taxpayers. One among the functions of auditing is to notice or detect errors and frauds; ERCA's tax audit and investigation aim at stopping the loss that comes from evasion, fraud and corruption. If there is a dishonorable event by taxpayers, auditing practices can modify ERCA to search out the taxpayers who had avoided paying tax and paying the tax due with penalties and fines (Akinbuli, 2010).

An Expanded domestic revenue base (especially taxation) offers a promise of larger autonomy within the future and a possibility from restrictive aid and loan conditionality's. With this vision, the Ethiopian government over the years has tried to enhance tax systems. For instance, ERCA has evolved from the merging of Ethiopian customs Authority and Ministry of Revenue, to strengthen and alter the distributed collecting system.

In addition to a shot tried increasing the government's domestic revenue, the government introduced tax auditing into the thought of tax administration in July 2008, The core duty of the Tax Audit unit is, to look at monetary statements of tax payer's with the read of creating their dependableness, accuracy and completeness. It's conjointly expected to notice and counter any tax evasion and shunning schemes, optimize the declared tax liabilities, ensure

Compliance with the Tax Laws, educate tax payers and recommendation the ERCA on policy formulation. The unit is presently staffed with One Thousand Two Hundred (1,200) officers with seventy

(70) Members being active field officers. A well-resourced Tax Audit unit will contribute far more Niu (2010).

1.2. Statement of the problem

Taxes are the most revenue for the government and so the involved agency ought to guarantee they're collected the proper means. The system should be monitored to avoid evasion and wrong submissions. Once these are in place and the right tax program is followed, then there's taxpayer mobility and there are unit different sources of revenue aside from tax, the revenue collected can increase. That's once there's no political interference and also the season is correct otherwise the revenue collected can decrease.

Obviously, a properly designed and administered taxation system is incredibly very in generating revenue additionally as increasing the assets base to the government of developed, developing, and shift economies. As Bird (2008) noted, it's unquestionable to make sure that the revenue collected from tax ought to be raised in economical and effective manner though it's troublesome without concern or favor in countries that area unit politically fragile.

However, the tax base of developing countries adversely affected by administration issues as well as poorly planned tax policies and lack of certainty relating to future policy changes. additionally, tax administrations also can produce issues for the tax payers as they impose burdensome (difficult) coverage and record keeping necessities, perform excessive inspections and audits, fail to contend with their corrupt workers, and failure to supply transparency within the operations of tax administration (Baurer, 2005).

In reality, below inadequate tax administration as well as low and ineffective plan, the potential quantity of taxation revenues in developing associate degreed shift countries has not been collected in an economical and equitable or just manner (Edmiston & Bird, 2004).

Further, weak tax administration could build the legal tax system unfair in this honest taxpayers would bear heavier and disproportionate burden. It, in turn, could have impact on the potency of tax operation, and additional could encourage businesses to figure within the smuggled economy.

In Ethiopia, taxation has been used for the aim of raising governments revenue is the maximum amount as potential to fulfill the ever-expanding public expenditure desires of the gov't. It's additionally a mechanism for reduction of inequalities in financial gain distribution, promotion of capital.

Investment's and trade, encouraging and/or discouraging certain industries counting on however appropriate for country's economic development program. However, it's hardly ever the case to gather the potential taxation within the country due to lack of awareness of taxpayers additionally as tiny range of tax agencies. ‟ cooperation with the business community‟‟‟. Tax systems are unit sometimes careful while not correct discussion with the business community. In addition, the business homeowners don't have quick access to clarification on info of the tax laws. Moreover, they lack awareness relates to the tax agencies seldom give advising services. As a result, taxpayers misinterpret tax rules, laws and regulations. Moreover, they lack awareness relating to the tax kind to be obligatory on their activity, purpose and operation of table audit, merchandise goods and services exempted from tax, negative issue of contraband trade, and coverage and filing necessities of the tax law (ECC & EBDSN, 2005).

A successful audit program ought to be enforced that is capable to investigate, detect and prevent loss of taxation. To the best potential extent, tax systems ought to be supported by clear and straight forward laws and procedures that facilitate revenue assortment, develop taxpayer's awareness, and minimize taxpayer's effort and compliance costs. The administration ought to be given acceptable social control tools, including as well as conduct of effective audit. Hence, to form a good and truthful legal system, and , it's very important to deal within the administration issues that have effect on it.

Regarding audit staff, there is no competency assessment model, and less emphasis is given for continuous upgrading the capability and knowledge of staff resources once they have given and control a specific position. Due to this reason, there is staff turnover in the tax authority, tax audit unit in particular. The authority fails to retain experts and well-trained auditors. As a result, ERCA get in to hassle to retain experts and well-trained auditors. If Tax auditors aren't the required level of operational capability to conduct tax audit and skilled capability they get troubled in giving appropriate services to taxpayers. The incapability of tax auditor could be because of absence of using effective pre-audit plan and inadequate audit couching as well

additionally their lack of willingness (Getaneh, 2011).

Currently few researches are drained this space, of that most of them are not primarily based in Ethiopia. Their main concern is to point out, the positive relationship between Tax Audit and to that of Government revenue and Tax compliance. In addition the negative relation between Taxes audit and tax evasion. In their analysis half they indicated that Tax Audit has inflated

Government income by increasing tax compliance and decreasing tax evasion and avoidance as well.

Furthermore, during regard there are not any researches are done on Tax audit follow and its significance in increasing revenue in Ethiopia in case of bale Robe town administration. In addition to the above tax administration issues and also the presence of research gap initiates the research or science fill the gap in this area. Besides the citizens don't perceive the relationship between revenue collection and tax audit and therefore they see it as a waste of time and a trouble to them. So, this study was intended to fill these gaps by establishing Tax audit practice and its significance in increasing revenue in Ethiopia in case of bale Robe town administration. Furthermore, the study additionally showed how Tax Evasion and non-Compliance affects taxation assortment of a government.

1.3. Research Questions

In line with the problems statements, the researcher developed five specific research questions. So, the key research questions were:

- What does tax audit practice look like in bale Robe town administration
- How does tax audit in increasing government's revenue by strengthening tax administration capacity?
- How does tax audit practice minimizes tax evasion in bale Robe town administration?
- What is the significance of tax audit leads to taxpayers‟ compliance with tax laws?
- What does tax audit legal frame work look like in bale Robe town administration?

1.4. Objectives of the Study

1.4.1. General Objective

The general objective of the study is to investigate tax audit practice and its significance in increasing revenue in Ethiopia in case of bale Robe town administration.

1.4.2. Specific Objectives

Specifically, the study attempts:

1. To study tax audit practice in bale Robe town administration
2. To analyze the effect of tax audit in increasing governments revenue by strengthening tax Administration capacity.
3. To assess the tax audit practice in minimizing tax evasion in bale Robe town administration.
4. To show the significance of tax audit leads to taxpayers‟ compliance with tax laws.
5. To study tax audit legal framework in bale Robe town administration

1.5. Hypotheses

This research is related to Tax Audit and Tax Revenues Growth. This focused on:

H1: “Tax audit contribute to tax revenues”.

H0: “Tax audit does not contributes to tax revenues growth”

1.6. Significance of the Study

This research work can give feedback to tax payers and the tax authority regarding the significance, application and practice of tax audit. The study also subsidizes in evaluating the predominant tax audit practice and in making some adjustments on the current tax audit systems. Moreover, it can provide constructive feedback about the efficiency and effectiveness of the existing Tax audit practice and its significance in increasing revenue in Ethiopia in case of bale Robe town administration. For those who are interested to make further study on the related issue it may be used as an indication. In addition, this project work is intended to provide immense benefit to tax administration and auditing in Ethiopia and also seeks among other things to establish the extent to which tax administration and auditing can be improved. Again, knowing the positive extent to which tax administration and auditing has helped and the purpose of which tax auditing has been introduced to help in planning the country’s economy.

1.7. Scope of the study

This research work assesses the Tax audit practice and its significance in increasing revenue in Ethiopia in case of bale Robe town administration. While studying the tax audit practice, this study considerers only the practice and its application in the Robe town administration, thus the scope may be somehow limited. However, since the general guidelines, application procedures and practice are the same throughout the country; it is supposed that this study can fairly reveal the tax audit practice and its effect in increasing the revenue of the town.

1.8. Limitation of the study

The researcher faced various limitations that hinder the proper investigation of the study. The main limitations of the study were lack of openness to provide adequate information to the researcher due to speculation concerning job security. Besides, the major factor was COVID-19 in order to carry out the study properly and to gather sufficient information since people were worrying face to face contacts. In addition, the reluctance to give back questionnaires on time and fail to understand the questions and guess answers may confront the researcher while collecting data and conducting the research.

1.9. Organization of the Study

The study was organized under five chapters. The first chapter consecrates to the background, statement of the problem, basic research questions, objectives of the study, significance of the study, and delimitation of the study. Chapter two is concerned all about the related literature on the research subject and has parts that define some concepts in the research. The third chapter explores the methodology used for the research and the data analyzed in the fourth chapter of the report. Finally, there are summary of the major findings, conclusions and recommendations in the fifth chapter of the report.

CHAPTER TWO

2. REVIEW OF RELATED LITERATURE

2.1 THEOROTICAL CONCEPTS

This section sections scholarly literature on taxation and tax audit practices. It provides an extensive and sufficient guide for the research and to assist other researchers who seek to replicate or delve more deeply into the thesis research topic.

2.1.1 Definition of Taxation

Taxation is usually outlined as, the levying of compulsory contributions by public authorities having tax jurisdiction, to contribute the price of their activities" (Arnold and McIntyre, 2002:6). No specific reward is gained by the tax payer. The money collected is employed for the common good of the grouping – for the assembly of bound services, as said, that are thought of to be additional efficiently provided by the State instead of by individuals e.g. maintenance of law and order or security, water, electricity, transportation, etc. (Eugene,2011)

2.1.2 Purpose of Taxation

The definition of taxation given above underlines the most purpose of taxation, that is, to boost revenue to pay the price of services provided by the State. Different purpose of taxation are to cut-back inequalities arising from the distribution of wealth; to restrain bound sorts of consumption e.g. alcoholic beverages and cigarettes; to safeguard home industries and to manage certain aspects of the country's economy e.g. Balance of payment, employment saving, investment and productivity. (Mesfin, 2008)

2.1.3 Basis for Taxation

Governments have denumerable responsibilities, a number of these embody economic infrastructure (roads, monetary system, enforcement of contracts, etc.), social control of law and public order, and protection of property, infrastructure, social engineering, welfare and public services (including education systems, health care systems, pension for the elderly and public transportation. Energy, water and waste management systems are also common public utilities) and therefore operation of government itself.

A number of revenue sources are on the market to a government to execute these responsibilities. Among the various sources is tax. Taxes comprise one outstanding, prudent and feasible source of revenue for the government. Governments thus tax the individuals in their country as they produce to earn income for themselves. Taxes type a high share amount of revenue to nations. Funds provided by taxation are employed by states and their purposeful equivalents throughout history to carry out many of these functions outlined above. Governments use completely different forms of taxes and vary the tax rates. This is often done to distribute the tax burden among individuals or classes of the population concerned in taxable activities, like businesses, or to spread resources among individuals or classes in the population.

Historically, the nobility were supported by taxes on the poor; fashionable social insurance systems are supposed to support the poor, the disabled, or the retired by taxes on those who are still operating. In addition, taxes are applied to fund foreign and military aid, to influence the macroeconomic enactment of the economy (the government's strategy for doing this is often referred to as its fiscal policy), or to modify patterns of consumption or employment within an economy, by creating some classes of transaction additional or less expensive.

2.1.4- Tax Audit

An audit is that the self-determining examination of financial statements of related economic information of an entity, whether profit concerned with or not, and regardless of its size, or legal type, once such an examination is conducted with observation to expressing an opinion on it. The American Accounting Association (AAA) (2008) has provided a broader definition of audit that refers to a scientific method of objectively gaining and evaluating proof concerning assertions regarding about economic actions and events to establish the degree of correspondence between those assertions and established criteria and interconnecting the results to interested users. In a narrower sense, auditing attestation communication as a result of it presents the auditor's opinion or judgment regarding the degree of correspondence between accounting information and established criteria (Eugene, 2011).

A tax audit is one among the foremost sensitive contacts between the taxpayer and a revenue body. The presence of an auditor during taxpayer's private dwelling or business premises, plus the exploration of private and business problems issues and therefore the gathering of information from taxpayer's‟ books and records, or just the disruption of regular advancement, represents a burden on the taxpayer and will be seen by some as an unwarranted intrusion into their affairs. Though this, tax audits stay the sole effective technique for ascertaining extra facts or confirming provided information. (Eugene, 2011)

The tax audit operate plays an essential role within the administration of tax laws altogether countries. In addition to their primary role of perceiving and deterring disobedience, tax auditors are usually needed to interpret advanced laws, carry out intensive examinations of taxpayer's books and records, whereas through their various interactions with taxpayers operative considerably because the public face of a revenue body. These factors, in addition to the absolute size of the audit operate in most revenues bodies; offer a robust case for all revenue bodies paying nearby attention to the general management of the tax audit purpose. (Eugene, 2011)

Traditionally, the audit function conducted by public accountants has been linked with this activity of verifying to financial statements. Tax audit (probable to be accomplished by public accountants) can be thought of as a delay of this, attest function‟. For tax purpose, one assessor's is liable to file a return to the apprehensive assessing officer with supporting documents sometimes required by tax law for instantaneous obedience with the return. The assessor's is sometimes called upon by the assessing officer under the tax law for producing the same. In this context, the question of tax audit may arise. And „tax audit‟ means to audit an assessor's accounting and other documentary evidences to prepare the correct tax return as well as to prepare the statements showing the detailed computational working for different heads of income or items in tax return and other mandatory evidential statements concerning allowances and disallowance for deductions and all these are to be followed by an audit report giving the auditor's belief about the degree of correspondence between the information content in the tax return and the regulatory necessities of the existing tax laws (AAA, 2008). Thus, tax audit encompasses the behind:

Accounts and other evidences are required to comply with the „tax basis of accounting‟, i.e. as per requirement of tax laws;

preparation of tax return, statement computational working for objects in the return and statements comprising particulars of allowances and disallowance for deduction;

Giving audit report portraying the attest function whether the tax return and statements have been fairly prepared as per the regulatory requirement of tax laws (Mukul)

When we think about who does tax audits, we first think of a public inspector, a civil servant, integrated in a public organization or agency of the government. Nevertheless, in the field of private financial statements audit, the audit must comprise all the economic-financial operations, including the taxes-originated ones, and the auditors opinion must also include whether the taxpayer has correctly assessed tax liability. For instance, according to Kamal Gupta & Ashok Arora, in India, the Income Tax Act, provides for compulsory audit of the accounts of certain income tax assessor's (i.e. persons liable to pay income tax) whose turn over exceed the specified limits. It was also practiced for some years in India but left after the 1997 E.C. election. The objective of such audit is to assist tax authorities in making the correct income tax assessment of the assessor's concerned. The tax auditor has to specifically report on certain transactions which have an impact on the income tax liability of the assessor's concerned and are, thus important to the tax authorities (Ahymed and Stern, 1991).

2.1.5 Scope & Extent of Governments Revenue

In recognition of the significance of an efficient revenue collection system for mobilizing the budgetary resources of the government, the need to establish revenue audit as a specialized and independent domain has been engaging the attention of the highest Audit Institutions for quite some time. The International Congress of International Organization of Supreme Audit Institutions (INTOSAI) held at Rio de Janeiro, Brazil in May, 1959 recommended that: Supreme Audit Institutions (SAI) ought to exercise the broadest possible supervision of revenues. (mesfine,2008)

Supervision should not be limited to the checking of collection of revenues in line with the accounts rendered by the collectors but, wherever possible, a check should be made to see whether or not tax payments were in line with legislation.

SAIs should ascertain whether there has been negligence in the matter of collections or exaggeration in the estimates. The SAIs ought to be equipped to carry out their duties, especially as regards supervision of revenues, with mechanized accounting and statistical services. (Eugene,2011)

The concept of tax audit was a sub-theme in the Third International Seminar of INTOSAI held at Bali, Indonesia in June 1988. The following guidelines were recommended in the area of tax audit.

(a) Audit mandate: SAIs ought to look for clear and specific legal authority for enterprise comprehensive tax audits in conformity with the relevant provisions of the Lima Declarations on Auditing Precepts.

(b) Audit of individual tax assessments: It's necessary that individual tax files remain examined to measure the adequacy of the system and procedures of tax assessment and assortment. For instance the examination of all tax files is neither possible nor necessary, best results could also be obtained whereas concentrating on high worth and risk areas. Selective auditing of business financial gain cases instead of remuneration assessment, investigations of according evasions and use of appropriate applied statistical sampling techniques in the review of files area unit most well-liked practices. Data and evidence on tax payers collected by the tax authority may be verified beside other freelance sources accessible.

(c) Interpretation of tax laws: SAI's ought to scrutinize the foundation rules, regulations and by the notifications issued by the chief agencies underneath the tax statutes.

(d) Scrutiny of choices of tax authorities: Wherever quasi-judicial and discretionary powers are unconditional within the tax officers, any decisions taken within the exercise of such powers ought to be scrutinized in audit.

(e) Audit methodology: Audit ought to be chiefly system primarily based and also the objective ought to be to find loopholes, lacunae and deficiencies not solely in tax administration however conjointly in tax laws. Adequate procedures for characteristic and handling minimization rising from deficiencies in laws might be thought-about so remedial action as well as amendments to the laws might be taken promptly.

(f) Socio-Economic implication of taxation. The social and economic goals projected to be achieved through tax concession and relief ought to be reviewed in audit.

(g) Reporting on the results of tax audit: Having respect to personal privacy concerns, it's imperative that confidentiality be maintained in reporting individual assessments within the audit reports.

(h) Training of tax auditors: Tax audit could be a specialization which needs thorough data of the relevant laws and rules. SAIs ought to give intensive and frequent coaching for tax auditors taking advantage of the training facilities accessible in their native departments coaching establishments as well as those in other SAIs.

2.1.6 Roles of the Taxpayer Audit Program

The tax audit platform of a revenue body performs a variety of the legal necessary roles that effectively disbursed and might create a big contribution to improved administration of the legal tax system. These roles are delineated briefly hereunder: (Mesfine, 2008)

- Promote voluntary compliance: The first role of the audit program is to push voluntary compliance by taxpayers with the tax laws. It seeks to attain this by reminding taxpayers of the risks of noncompliance and by engendering confidence in the broader community that serious abuses of the tax law were detected and suitably penalized.
- Detect non-compliance at the individual taxpayer level: By concentrating on major areas of risk (e.g. unreported cash income) and those people individual taxpayers possibly to be evading their responsibilities, audits could arouse lightweight important understatements of tax liabilities, and extra government tax revenue collections.
- Gather information: on the „health‟ of the tax system (including patterns of taxpayers‟ compliance behavior): The results of traditional audit activity could give provide information on the overall well-being of the legal system. Audits conducted on a random basis will assist overall revenue administration by gathering crucial information needed to make judgments on overall levels of tax compliance, that over time is wont to determine trends in overall structure effectiveness and to collect a lot of precise data which will be wont to inform decision-making on future compliance improvement methods, to refine automatic risk-based case choice processes, and even support changes to tax legislation.
- Gather intelligence**:** Audits could arouse to lightweight information on evasion and rejection schemes involving giant numbers of taxpayers that which will be wont to increase major counter-abuse comes.
- Educate taxpayers**:** Audits will assist clarify the appliance of the law for individual taxpayers and to spot enhancements needed to recordkeeping and therefore could contribute to improved compliance by tax payers within the future. Identify area unit as of the law that require clarification: Audits could arouse to lightweight areas of the tax law that are inflicting confusion and issues to giant numbers of taxpayers and therefore require

Further efforts by the revenue body to clarify the laws‟ necessities and/or to raised educate tax payers on what they need to do follow into the longer term. Given the broad vary of roles to be performed a revenue body's audit program normally entails the most important allocation of a revenue body's total employees resources. From this perspective alone, the audit program represents a sizeable strategic investment that dictates the requirement for sound management policies and practices (Eugene, 2011)

2.1.7 Audit of Revenue of Government.

As mentioned earlier, government revenues are sourced from varied tax and nontax receipts. The country papers bring out the proportions of these two sources that in turn influence the areas of audit priority. These are tax and non-tax revenues. Government revenues are foremost half addicted to taxes legislated through varied tax statutes. However, the unfold of the two sources, viz. tax and non-tax revenues, varies from nation to nation. (Eugene,2011).

The scope of audit activities varies across countries, partially as a result of the system of assessment in place. There are two generally accepted systems of tax assessment applied worldwide (administrative assessment and self-assessment) in around partial countries, body assessment is used to varied degrees among the administration of personal income tax and company profits/income tax. All countries administer VAT below self-assessment principles. (mesfine, 2008).

Assessment systems operate on the principle that each one tax returns have be compelled to be subject to a degree of technical scrutiny before a correct assessment is distributed to the payer. In follow, however, heaps of the scrutiny previously undertaken by technical staff has been replaced in many countries by utilization of automated screening techniques to identify returns requiring scrutiny before a correct assessment is issued. To the extent that there is some level of scrutiny applied by technical officers, it ranges in follow from an extremely casual examination of some tax returns to a more heaps of in-complexity examination where any inquiries additionally created with taxpayers (sometimes by correspondence) before a recognized assessment is issued. Even countries that operate body assessment regimes complement these arrangements with a recognized program of post-assessment audits. However, in follow such programs tend to be conducted on a smaller scale than is that the case in countries only applying self-assessment principles.

In countries where self-assessment principles are applied, returns are typically accepted as filed in the first instance (with the exception of returns containing mathematical errors or clearly erroneous deductions) and, for income tax, a formal assessment/ notice confirming/advising the tax liability is sent to the taxpayer before any inquiry. A sample of returns is selected f o r post-assessment audit, generally applying computer-based risk selection techniques and/or manual screening processes. Large scale matching programs may could to boot mounted on a post – assessment basis for the most categories of monetary gain (i.e. wages, interest, and dividends)(mesfine,2008).

Since regarding all tax returns are accepted as filed whereas not technical scrutiny applying self-assessment principles, it is essential for the system to be supported by a reliable automated audit case alternative system exploitation risk-based screening techniques. Typically, such systems stand developed using risk-based criteria derived from analyses of completed audit cases and are typically updated to want account of the results of audit activities and to replicate important changes among the behavioral patterns of taxpayers. Models of risk identification models and approaches are drawn among the companion note, Audit Case alternative. As systems of body assessment and self-assessment have evolved over time in many countries there is one issue of a fine-line in follow between their choices and relative effectuality. (Eugene, 2011).

According to the Ethiopian Federal Inland Revenue Authority's tax assessment and audit manual (2006), associate in nursing an initial review by tax official of the tax declarations and information provided by tax payer and a verification of the mathematical and technical accuracy of the declared tax liabilities shortly once the submission of the declaration. The initial review put together includes the applying of various risk criteria to visualize possible tax underpayments and thus the later alternative for tax audit.

An audit on the alternative hand is that the conduct by audit staff for acceptable verification of selected tax payers declared tax liabilities. This might embrace a review of tax payer's systems, books of account and different connected knowledge. It's about to put together embrace cross checks of tax payer's records with those of tax payer's suppliers or with different provide source of information just like the custom authorities or different government departments and agencies. (Eugene, 2011)

2.1.8 Key Audit Characteristics

According to (Eugene, 2011), Compliance regimes operate within the intervals the distinctive legal, cultural and administrative background of individual member countries. Yet, there are form of common pre-requisite choices and desires that need to be in place to form certain associate honest level of effectiveness and efficiency from audit activities and to support continuous improvement. They are:

- A comprehensive legal framework, along with associate in nursing acceptable regime of sanctions.

- Well-defined organizational and management processes, along with a comprehensive performance activity framework.

- Well-defined audit techniques and adequate support arrangements; and.
    - Adequate human resource management and development programs.

2.1.9 Demands for Tax Audit

Four conditions tend to form the demand for the freelance performance of the audit or attest perform. They are as follows: (Eugene, 2011)

- ✓ Conflict of interests between those who prepare accounting information reports and people who use them;
- ✓ Consequence of information to users whereas exploitation them in decision-making;
- ✓ Complexity of subject material and audit process; and
- ✓ Remoteness of users from subject material and preparer.

When audit function is extended to tax, the above-mentioned four conditions are also required to be satisfied. Here, the preparer of income tax return and relevant information (the assessors") has the conflicting relationship in terms of financial interest with his counterpart user or evaluator of the return (the assessing officer). Because, manipulated information in the tax return may reduce the tax liability (Eugene, 2011).

Second, use of the tax return, assumed to be correct and complete, may have serious consequence on Government business enterprise estimation and assortment thence. As a result, all the budgetary appropriations could indicate for nothing however unwarranted imagination (Eugene, 2011).

Third, both financial accounting and tax accounting square measure recognized as a way advanced discipline because of technicalities and their distinct characteristics of difficulties.

Finally, between the preparer of the come back and also the information in that (by the assesse) and also the assessing officer, there exists a wall of remoteness though the latter will demand. Any additional information from the previous to be glad with the completeness and correctness of the information provided. But sometimes this may not be possible due to time and cost constraints and some other reasonable causes (Eugene, 2011).

In this case, the tax authority will apply his best judgment, which cannot be the expression of the fact and so the parties, the Government and also the assessors‟ may be affected by under- or over-charging of tax. Therefore, all the conditions making the demand for audit with relation to tax can be found to be glad.

The International Federation of Accountants (IFAC) commission, within the Code of Ethics for Professional Accountants‟ has defined „professional service‟ as any service requiring occupation or connected skills performed by a professional accountant bourgeois as well as accounting, auditing, taxation, management, consulting and money management services‟. Hence, associate in nursing auditor should be competent main in accounting, inevitably in auditing, as well as thenceforth in taxation (Eugene, 2011).

Introduction of tax audit by qualified professional skilled accountants is so the reputable recognition of their specialized competency. the important like obligatory from tax audit, if lawfully enforced, is that the audit can guarantee maintenance of correct books of accounts and other records. The growing accounting habit so developed can modify creation of a transparency of the within the middle of grey area between assumed financial gain and reportable financial gain.

Thus, nonpayment was markedly checked through testing the dishonorable practices regarding colluded accounts. alternative arguments in favor of tax audit include: legal return with additionally credibleness and in the middle of tax audit reports as well as necessary supporting statements will faithfully be given before the authority facilitating tax administration, relieving assessing officers from completing routine verifications, and aiming to a lot of necessary investigation aspects of assessment cases through utilization of the saved time.

2.1.10 Types of Tax Audits

Audits will vary in their scope and therefore the level of intensity to that they’re conducted. For this reason, varied terminologies have evolved to explain different kinds of audit activity (Mugume, 2006):

Full audits–The scope of a full audit is broad. It's usually entails a comprehensive examination of all information relevant to the calculation of a taxpayer's liability for a given period amount. The target is to work out the right tax liability for an income tax return as a full. In some countries full audits are square measure disbursed as part of random audit programs that square measure wont used to gather information on the extent, nature and specific options of tax compliance risks, for compliance analysis research functions and/or the event of processed audit choice formulae. Given their broad scope, full audits square measure usually pricey to undertake a right smart program of

full audits would require considerable resources and scale back the speed rate coverage of taxpayers might well be achieved by a lot of varied mixture of audit varieties.

Limited scope audits – restricted scope audits square measure confined to specific problems on the income tax return and/or a specific tax theme arrangement utilized by the remunerator. The target is to look at key potential risk areas of rebelliousness. These audits consume comparatively fewer resources than full audits and permit for an raised coverage of the taxpayer population.

Single issue audits – Single issue audits are measure confined to at least one item of potential non-compliance which will be apparent from examination of a taxpayer's return. Given their slim scope, single issue audits usually take less time to perform and might be might to be wont to be review massive numbers of taxpayers concerned in similar schemes to hide non-compliance. In follow, the scope and nature of any audit activity undertaken for a specific taxpayer will rely upon the offered proof inform to the probably risks of rebelliousness and a taxpayer's previous history. Intensive audit inquiries can also be even just because a taxpayer's financial and /or business activities square measure remarkably complicated.

Periods beneath examination: Audits will concentrate on specific financial year or accounting period, or be extended to hide multiple fiscal periods. An audit will concentrate on specific elements of the taxpayer's activities (such as sales, goods in stock etc), specific incidents or transactions or activities (such as those disbursed during a branch or subsidiary), or specific tax obligations. An audit will vary in its level of detail. Typically the taxpayer's affairs are examined intimately and in different things, subject to the extent of risk perceived, just superficially (Bukenya,1996).

2.1.11. Resources for the Tax Audit Perform

Revenue bodies typically have at their disposal a finite level of resources to conduct the day to day business of revenue administration. Given the numerous tasks to be performed and therefore inevitable choices that have got to create on priorities, a method is needed to workout however those resources are to be allotted. In some member countries, revenue bodies have comparatively restricted discretion on however workers resources are to be unfolding across the assorted areas of work, whereas in others broad discretion is given to senior management on how resources there to be allotted (Eugene, 2011).

Regardless of however the general budget of resources for audit work is acquired a, a key issue for the audit perform is however those resources were spread over the varied segments of taxpayers. Determining how resources may best be allocated could be a key component of a revenue body’s strategy for compliance improvement and is restricted within the following section one

1. Forum on Tax Administrations Compliance Sub-cluster
2. Tax Administrations in OECD and chosen Non-member countries: Comparative Information Series (2006)

The significance of the roles vie by the taxpayer audit perform, as represented beyond than is proved partly by the comparatively massive proportion of the workers resources dedicated to audit perform. In several member countries, the proportion of the revenue body’s overall workers resources dedicated to audit and different verification activities exceeds over half - hour.

2.1.12 Location of Audits

Tax audits will be conducted in several locations. Typically there’s is a requirement to hold out the audit at a taxpayer’s business premises. In different things, the books and records needed to finish an audit will be collected by, or sent to, the revenue body and therefore the audit work performed within the organization. Tax audits can be classified as „field audits’ or office or desk audits‟ on this basis. (mesfine,2008).

Given that audits can vary in terms of their scope and intensity revenue bodies ought to have a transparent policy on the types (and numbers) of audits to be conducted, and therefore the circumstances in which specific types of audits are to be carried out, so that audit officers (including managers) understand what is expected of them. (mesfine,2008)

2.1.13. Approaches & Standards of Tax Audit

In conducting a tax audit the auditor ought to apply the generally accepted practices of auditing jointly would knock off the case of different audits, e.g. an audit of an organization beneath the businesses act (Kangave, 2004). The generally accepted auditing practices are measure communicated within the varied pronouncements of the individual country. The auditor ought to get the financial statements in addition because the statement of particulars genuine by the assessed before he verifies them. The auditor will apply the technique of selective verification (statistical sampling/test-checking), counting on his analysis of the internal control system prevalent in the entity under audit therefore the materiality of transactions.

In conducting the audit the auditor ought to detain mind that the essential objective behind is to help the authorities in assessing the collect financial income of the assessed. for conducting the tax audit effectively an auditor must develop an approach that could be a synthesis of taxation laws and auditing principles. The character of tax audit is such an auditor needs to place confidence in varied legal pronouncements within the field of taxation. Tax Administration in OECD and Selected Non-member Countries: Proportional Information Series (2006).

2.1.14 The Efficiency and Effectiveness Tax Audit

Audit effectiveness is measured by examining the amount of evidence selected for examination in relevance entire out there available evidence and an optimal level of evidence. Audit efficiency is then defined as audit effectiveness per unit of time by taking the audit effectiveness measure divided by minutes spent on the task (Kangave, 2004). The key findings were that time pressure (manipulated by four levels of a time budget for the task) affected performance only at the extremes, with the highest time pressure group performing more efficiently than the auditors in the lowest time pressure group. Efficiency was also affected by audit program structure, with high structure (more detailed audit procedures listed) being associated with increased efficiency.

Apostolou *et al*. (1993) defined Audit efficiency as the ability to meet the budget and operationalize it as the percentage deviation between actual and budgeted hours. This research examined the effect of leader behavior on audit efficiency. Two leader behaviors; (1) facilitating cooperation and teamwork and (2) administering discipline; resulted in increased audit efficiency. On the other hand, showing consideration contributed to reduced audit efficiency (Apostolou *et al*., 1993).

In addition in an economic sense, the concept of efficiency is rooted in the ideas of minimization of inputs, absence of waste, and least cost production methods Auditing practitioners tend to define efficiency as accomplishing the audit task in less time thereby increasing profitability (McGrath and Hollingshead, 1993). The efficient and effective conduct of audit activities requires that a revenue body's audit and investigation staff have appropriate powers of access to information held by the taxpayer and other parties so that taxpayers liabilities stated in their takings can be properly verified or, in the absence of returns, be truthfully recognized. There should also be an appropriate regime of sanctions to punish and deter non-compliance (Moyi and Muriithi, 2003).

For these causes, revenue bodies necessitate a set of powers and sanctions in the legal framework supporting the conduct of tax administration activities that includes the provision of adequate powers for obtaining information and an appropriate regime of sanctions covering the various offences that may arise (Cheeseman and Griffiths, 2005). In practice, this legal framework may be set out separately in the laws governing each tax administered or, preferably for ease of legislative maintenance, in a single comprehensive law on tax administration that provides a common set of provisions covering all taxes. In the US, an official form titled „Cost Benefit Analysis‟ (Review of Cost Effectiveness of Investigations) is used to measure the cost benefit of continuing an audit. The form is being prepared at a predetermined stopping point in the audit (such as when 60 hours have been expended by the auditor) (Cheeseman and Griffiths, 2005). The form calculates cost benefit by assigning dollar values for the auditor's hourly labor costs and multiplying the cost by the hours projected to complete the audit. The auditor's total labor dollar cost is matched against the Projected revenue anticipated (benefit of continuance). A negative cost benefit analysis may result in the early termination of the audit.

Collectibles is another factor for possible consideration. Some countries use collectability as a pre-contact consideration and other countries reported that it could become a factor during the course of the audit if bankruptcy were imminent (Kangave, 2004). The collectability concept implies that a taxpayer's inability to pay a future proposed tax assessment would be sufficient basis for not conducting the audit. Those administrations that do not use this concept report that collectability is a secondary objective and should not diminish the primary objective of a correct assessment of tax liability. In addition, the limitation of collectability considerations to the current tax period may not provide a complete financial picture for the taxpayer as it excludes consideration of future payment potential (Kangave, 2004).

2.1.15. Importance of Tax Audit in Fighting Corruption

Simply defined, corruption is the abuse of public power for personal gain or for the benefit of a group to which one owes loyalty. It occurs at the intersection of public and private sectors, when public office is abused by an official accepting, soliciting, or obtains by threat a bribe. Klitgaard (1996) has established a simple model to clarify the dynamics of corruption: C (Corruption) = M (Monopoly Power) +D (Discretion) – A (Accountability)

In other words, the degree of exploitation depends on the amount of monopoly power and discretionary power that an official exercises. Monopoly power can be large in highly regulated economies; discretionary power is often large in developing countries and transition economies where administrative rules and regulations are often poorly defined. And at last, accountability may also be weak, entire as a result of poorly defined ethical standards of public service, fragile administrative and financial systems and ineffective watchdog activities. Tax is one of the most exposed issues for corruption since it is carried out by the interaction of the tax payer and the tax auditor. (Eugene, 2011)

2.1.16- Criteria for a Good Tax Audit

For the tax inspector to hold out an honest audit exercise, the subsequent conditions should be consummated.

1. The tax auditor should be familiar with the environment within which he's employed. It is a condition which is extremely essential that the tax inspector should be properly instructed within the political, economic, social, cultural and religious environment of the taxpayer. Sensible information of his environment will affect the decision made by him.
2. The tax officers ought to be intended to hold out tax audit, they must be properly trained and have expertise in that area. The tax inspector should not be anxious by corrupt practices that render the aim of the tax audit useless.
3. The tax audit should be properly supervised by people who are professional skilled and when new tax inspectors are sent to hold out the audit, they should be monitored by older ones therefore on certify that the proper factor is done.
4. Specialization should be inspired. The cases should be sorted. This may permit the tax audit employees to become specialist in an exceedingly specific field.

5. The style within which the audit is being carried out be modified. The usage of computer should replace the manual method as this go protracted manner in facilitating the job and

serving to preserve information for a long time. This may improve the efficiency of the implementation (Ogundele, 1999).

2.1.17- Tax audit and investigation

According to (mesfine,2008), A number of issues are usually mentioned when discussing matters relating to Tax Audit and Investigation. They are so persistent that they cannot simply be unheeded. A modest effort will hereby be created to deal some of these contemporary issues related to Tax Audit and Investigation. Some of these are summarized below:

A. Responsibility for the result of Tax Audits

The result of a tax audit is enforced by holding the employer responsible for any tax liability arising from the tax audit of the employees. In a situation where some affected staff (local and expatriates) might have left the country by the time of the audit there is always a debate as to who should be held responsible. This debate is quite unnecessary as the law is clear on who should be held responsible. Article`90 of the Personal Income Tax Proclamation (PITP) states Penalty for Failure to Withhold Tax can be

1) A withholding agent who fails to withhold tax in accordance with this Proclamation is personally liable to pay to the tax Authority the amount of tax which has not been withheld, the withholding agent is entitled to recover this amount from the payee.

2) The tax withholding liability imposed by this .Proclamation shall be treated as a tax liability for purposes of any Article providing taxpayers with the right to contest the amount of tax due or to recover tax paid. .

3) In addition to any amount for which a withholding agent is liable under Sub-Article (1), an agent who fails to withhold tax in accordance with this Proclamation shall be liable for a penalty of. 1,000 Birr for each instance of failure to withhold the proper amount.

so uncollected tax from Income tax shall be recoverable as a debt due by the employer to the relevant authority. Thus it is the duty of the prearranged collection agent or a firm to fully account for what it had withheld, or ought to have deducted, on behalf of the pertinent tax authority.

B. Definition of Income.

Chargeable Income is defined in Section 10 of Income Tax Proclamation 286/2002 "Income" shall mean each variety of economic profit including nonrecurring gains in cash or in kind, from whatever source derived and in whatever form paid credited or received. 3 (1) of the PITP as the financial gain of a person “from a source inside or outside Ethiopia ” and it includes any gain, profit salary, wages, fee, compensation, bonus, premium and most conceivable allowances however excluding some reimbursable expenses and compensation for loss of office. In some cases, only basic salary is included by the employers while other taxable allowances like bonus, appropriate portions of rent and transport allowances and leave pay are wrongly excluded from taxable income. In the oil industry where the recompense package is robust, exclusion of relevant income and allowance has the tendency of gross understating pays taxes and remittances to the respective state government. The normal audit approach is to re-compute the taxable income and tax there from with a view to recovering possible underpayments, if the collection agents have previously been computing the taxable income as stipulated by the Proclamation, there would have no need like for associate elaborate tax audit.

C. Concentrate on Revenue Generation

It is usually aforementioned that the client is usually right, this is however not the case in the relationship between the tax authority and the payer. This can be therefore as a result of the most important aim of tax audit and investigation is not to manage the taxpayer however attention on generating revenue. (Ojo, 1996).

2.1.18- Impact of tax audit on revenue collection

Tax audit affects revenue assortment therein that it promotes voluntary compliance of taxpayers that will increases revenue. It also determines the accuracy of returns so as to ensure the right taxes are submitted. With tax audit tax liability can be easily declared and matters that need adjustment are identified. It also helps in collecting tax interests and penalties which thereby increase revenue collection. Tax audit also helps to implement changes to eradicate evasion. Thus, tax audit is positively related to tax collection.

2.1.19- Theories on Tax Audit & Revenue Collection

This part explains the theoretical contributions from various authors on tax audit and revenue collection. It also gives contribution of various research studies as carried out by various authors and then concludes on the general view of the various authors.

2.1.19.1- Specific Theories

Awe (2008) defines auditing as an independent examination of the books and accounts of an organization by a duly appointed person to enable that person give an opinion as to whether the accounts give a true and fair view and comply with relevant statutory guidelines. The American Accounting Association (1971) in its Statement of Basic Auditing Concepts in Hayes, Schilder, Daseen and Wallage (1999) described auditing as: a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between these assertions and established criteria and communicating the results to interested users. Akinbuli (2010), Hayes et al (1999) reported that several theories of auditing were made to specify and determine the audit functions. Some of these theories include:

2.1.19.1.1- The Policeman Theory

This theory of auditing was formulated by Awe, (2008) on assumptions that once monitoring is done on the systems at unspecified times then that is like policeman.

2.1.19.1.2- The Moderator of Claimants Theory

This theory is stated by Frey, (2003) that it is important that all vital participants in an organization continue to contribute. In order to continue these contributions, it is important that each group believes it receives a fair share of the organizations income. This is based on the assumption that when one gets a fair share then a fair share were contributed. To the auditing theory then fairness is introduced.

2.1.19.1.3- Agency Theory

This theory is associated with conflicting interests of shareholders and management of organizations, suggesting that the less informed party will have to demand for information that monitors the behavior of better informed manager (Akinbuli, 2010). According to Hayes et al (1999), assumptions are made that agency theory can be used to explain the supply side of the audit market. The contribution of an audit to third parties is basically determined by the probability that the auditor will detect errors in the financial statements and the auditor"s willingness to report these errors. Then independence is emphasized in auditing.

2.1.20- Classical Theory of Tax Compliance

This theory of tax compliance initially formulated by Toggler, (1970) is also called the A-S models based on the deterrence theory. In the theory the taxpayer is assumed to maximize the expected utilities of the tax evasion gamble, balancing the benefits of successful tax cheating against the risky prospect of being caught and punished by tax authorities (Sandmo, 2005).

Alabede et al (2011) asserted that the deterrence theory depends largely on tax audit and penalty. They further stressed that this theory of tax compliance makes taxpayers to pay tax as a result of fear and sanctions.

Trivedi and Shehata (2005) says that the deterrent theories suggest that taxpayers "play the audit lottery", that is they make calculations of the economic consequences of different compliant alternative.

Verboon and Dijke (2007) stated that the essence of the deterrence model of tax compliance is to chiefly examine the interaction between probabilities of detection and sanction severity that should affect non-compliance. Brook (2001) says that classical theory is only based on economic analysis but social and psychological variables are equally important in understanding the issue of noncompliance to tax. Some of the important studies about the effects of deterrence on compliance include Hasseldine (2000), Torgler (2002) and Kirchler (2007).

Elffers (2000) and Braithwaith (2003) argued that if deterrence (that is the probability of detection and sanction severity) would be the most significant variable in explaining compliance, rational individuals in most societies of the world would be non-compliant because the levels of deterrence are low. The theory has contributed to theory the fact that revenue authorities should seek audited statements or perform audits to ascertain compliance.

2.1.21- Theory of Planned Behavior

The theory of planned behavior states that the behavior of individuals within the society are under the influence of definite factors, originate from certain reasons and emerge in a planned way (Erten, 2002). It was assumed that the ability to perform a particular behavior depends on the fact that the individual has a purpose towards that behavior. Therefore, it was asserted that the factors that determine the purpose towards that behavior are attitude towards behavior, subjective norms and perceived behavioral control. Ajzen (2002) says that these factors are under the influence of behavioral beliefs, normative beliefs and control beliefs. It is also asserted that sociological and psychological factors have proved to be important in understanding the high levels of tax compliance. In such analyses, concepts such as trust in authorities perceived fairness of the system moral considerations and norms are added to theory and are used to promote better understanding of tax compliance.

2.2- Empirical Studies

In this part the researcher tried to revise some researches which are done in different global area of tax audit and has summarized as follows.

2.2.1 Global context

Burcu Gediz Oral and Ferhan Sayın, (2015), Aiming to determine the relationship between corruption and tax auditing during the period of 1985-2011 in Turkey, the study determines the relationship between the variables using the Vector Autoregressive (VAR) Analysis. The results from VAR Granger Causality Test indicate that audit rate variable has an impact on the corruption index and also corruption index variable on the share of the tax revenues in the general budget revenues. The Variance Decomposition Analysis results used in order to determine the most effective of the variable on those in the model show that corruption variable acts as an exogenous variable in the short-term. In other words, corruption is not affected by other variables in the short term. Changes in index of corruption are largely due to the corruption itself and audit rate in the long term. However, results of Impulse-Response Analysis to show whether the effective variable could be used as an effective policy instrument indicate that variable likely to be in audit rate could be positively effective for the mid-term while it could decrease in the long run. In other words, the tax audit reduces corruption in the long term.

Niu (2010) in his study found, a positive association between the audit and the voluntary compliance. The finding suggests that the audit productivity may be under estimated in many studies in the literature. It reminds us that when considering the productivity of the audit work. Besides the direct audit collections, we should also take the audit impact on the voluntary compliance into consideration. For this reason, the finding may provide tax professionals and tax authorities with incentives to strengthen the audit power and to better structure their audit organization to generate more revenue for the state. Niu (2010) Historical population data of a New York State economic sector were used in this study instead of experimental data or Randomly selected sample data often used in the literature. the results of both ordinary Least Squares (OLS) and Time Series Cross Section (TSCS) autoregressive modeling methods. The results of both methods suggest that after an audit, a firm would report a higher sales growth rate.

According to, Badara, M.S. (2012) Questionnaire distributed to forty-eight (48) respondents using descriptive statistics. The result shows that the Relevant Tax Authority (RTA) employed tax audit towards achieving target revenue, that tax audit reduce the problems of tax evasion, that tax payers do not usually cooperated with tax audit personnel during the exercise. There are several theoretical and empirical studies on tax audit and tax compliance. These studies provide mix reactions on the relationship between tax audit and tax compliance. J.Alm and McKee, (2006) investigates the application of experimental methods to examine the individual compliance responses to a “certain” probability of audit, and conclude that the compliance rate rises if an individual knows he were audited and the rate falls if he knows he will not be audited.

Slemrod et al, (2001) examines randomly selected taxpayers and inform them that their filling were "closely examined‟ and found evidence of taxpayers‟ behavior changes in response to an increased probability of audit, although the responses are not uniform among different groups of taxpayers.

Mittone (2006) investigates that early experience of audits in taxpayers‟ "tax life" is a more effective way to increase compliance than later audits. Also Kastlunger et al, (2009) study of experimental research also suggests that, although the effectiveness of audits and fines cannot be completely confirmed, early audits in taxpayers‟ "tax life" have a positive impact on compliance.

According to Kleven et al (2010), 40,000 individual tax filers using experimental design and randomization test and SKAT‟s Business object Database with ordinary least square. Their research found that tax evasion rate is small for income subject to third party reporting, but substantial for self-reported income; marginal tax rates have a positive impact on tax evasion, but that this effect is small; prior audits substantially increase self-reported income and threat of audit letters also have a significant effects on self-reported income, and the size of this effect depends positively on audit probability expressed in the letter.

Hyun (2005) Japan & Korea using world value survey dataset and descriptive statistics and multiple regressions for analysis. Japan has the higher level of tax culture than that of Korea; and the legal system is relatively more important factor to determine the level of tax culture which eventually affects the level of compliance. Plumley et al (1996) Data set from 1991-2001 using Ordinary Least Square The result found significant effects attributable to many tax policy and tax administration parameters; including: audits; third party information documents; the issuance of targeted non-filer notices; criminal tax convictions; marginal tax rates.

Adediran S. A., Alade S. O and Oshode,(2013) , examines the impact of tax audit and investigations on revenue generation in Nigeria. The aim is to determine if tax audit and investigations can actually increase the revenue base of the government and if it can also stamp out the incidence of tax evasion. Data were collected through the primary sources from four hundred and ten respondents who are staff of the Federal Inland Revenue Service and Edo State Board of Internal Revenue. Hypotheses formulated were tested with Pearson Correlation Coefficient using SPSS output data. The findings are that Tax audit and investigations can increase the revenue base of the government and can also stamp out the incidents of tax evasion in the country. It was recommended that Tax audit and investigations should be carried out more often and as thorough as possible to accomplish its task of increasing the revenue base and stamping out tax evasion in the country.

Mutarindwa and Rutikanga ,(2014), seeks to explore the role of financial statements audit in promoting tax revenues Growth in Rwanda in the broader perspective. Survey questionnaires as primary data collection Instruments were distributed to all audit officers of Rwanda Revenue Authority equaling to 100 staff and followed both analytical research designs. Secondary data included reports from Rwanda revenue authority from 2006 to 2010. The paper also examines preliminary empirical results on the relationship between financial statements audit and tax growth , it also supports the notion that the practices of audit of final books of accounts for both small and medium enterprises at institutional level are prerequisite for growth of tax revenues in the country. In conclusion, the study found out that taxpayers „attitudes towards tax audit is still negative and results showed that the tax audit greatly influences the tax revenues collected by government.

Kennedy & John Obi, (2014), examines the impact of tax audit and other qualitative attributes on the tax compliance level of companies in Nigeria. Questionnaires were administered to staff of sampled companies in selected states of the five geo-political zones of Nigeria. Ordered Logistic Regression technique was employed to analyses the responses. The result showed that there exists a positive relationship between tax audit and tax compliance. The result also revealed that the probability of being audited, perception on government spending, penalties and enforcement, the joint effect of tax audit and penalties have a tendency significantly influences tax compliance in Nigeria. It also recommend that the relevant authorities should seek more pragmatic and effective means of enhancing the impact of tax audits on corporate tax compliance in Nigeria in order to consolidate on government's revenue.

Onoja & Iwarere , (2015.) examines, The increase in tax evasion and actual tax revenue collected but not fully remitted to the government necessitated this study on tax audit. An average Nigerian has no faith in the government and will not want to entrust their resources to the government as such payment of taxes were ranked among the least obligation they owe to the government at all levels. The study explores the effects of tax audit on revenue generation in Federal Inland Revenue Service and to determine the relationship between the tax audit and revenue generation in Federal Inland Revenue Service. The population of the study consists of the staff of the Federal Inland Revenue Service, Abuja and Taro Yamane sampling technique was used to determine the sample size. The questionnaire was used to generate the data. The hypotheses were tested using Analysis of Variance (ANOVA). Finding revealed that: tax audit has significant effects on revenue generation in Federal Inland Revenue Service and tax audit has a positive relationship with the revenue generation in Federal Inland Revenue Service. The study recommends that there is a need for tax audit department autonomy to be able to carry-out their responsibility effectively as specified in Federal Inland Revenue Service Establishment Act 2007. Also Tax audit should be carried out on a routine basis to prevent tax evasion and extreme tax avoidance by the tax payers. As indicated in the empirical study part above, the variables used are similar to the variables used in this research work. Since, the variables used in the both the empirical studies and this research work are the same, they have the same issues under study.

2.2.2. In Ethiopian context

According to Tadesse & Goitom (2014), like other developing countries, Ethiopia faces vaults in raising revenue to the required level in order to scale up the development endeavors. Ethiopia has experienced a steadfast expenditure surplus over revenue for a long period of time. Therefore effective tax audit program of revenue body performs a number of important roles and can make a significant contribution to improved administration of the tax system.

According to Ketema (2013), Millions (billions) of Birr are lost through tax evasion every year which leads to excess of public expenditure over public revenues resulting deficit. In addition, taxpayer grievances related to tax audit works result in long delays in collecting the government revenue that is expected to be collected because of the judicial appeal processes. Therefore, it is of great importance to identify the factors affecting tax audit effectiveness in order to achieve tax authority's objectives and to facilitate the tax administration aim of getting "the right tax at the right time." This is the issue that motivates the researcher to do so.

According to the Ethiopian Herald interview with Prof. Dr. Fisseha-Tsion Menghistu, "the tax to GDP ratio of Ethiopia is far below the Sub-Saharan average despite many tax reforms since 2002"(Central intelligence agency world fact book and other sources, 2017). This may be as a result of evasion or fraud by the taxpayers which includes; underreporting profits and turnover, underreporting employee wages, failure to register or file tax declarations, dearth of willingness to operate in accordance with tax laws.

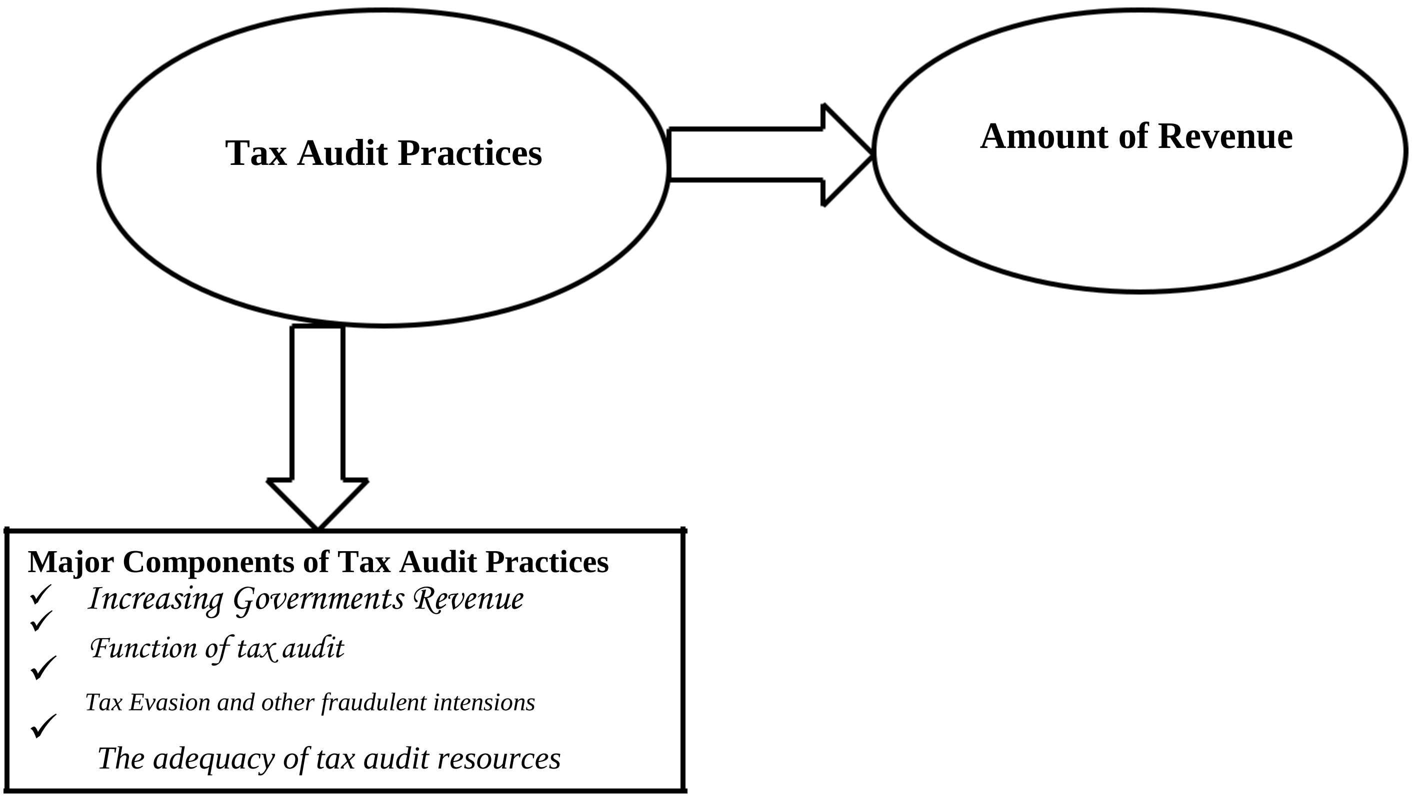
Netsanet (2014) revealed that like many other jurisdictions, Ethiopia's tax system is fraught with evasion. One factor that significantly contributes to tax evasion is lack of intensive audits and absence of predetermined audit criteria.

There are few researches done on tax audit in Ethiopia. For example Mesfin (2008) tries to assess tax audit practice and its significance in increasing revenue in Ethiopia the case of Addis Ababa city administration by adopting quantitative research design. Another study conducted by Getaneh (2011) tries to examine the tax audit practice in Ethiopia: the case of the federal government. Netsanet (2014) conducted a study on assessment of tax audit practice: the case of Hawassa city administration. A study by Elias (2014) tries to investigate the factors affecting tax audit effectiveness on category ‘‘A’’ taxpayers in Bahirdar city administration revenue office considering audit quality, organizational setting, support from top management, auditee attributes, and organizational independence as determinant factors by adopting quantitative research approach; thus further mixed methods studies by incorporating other factors are needed. Another study conducted by Samuel (2016) tries to assess tax audit practice and its challenges-a case study of Ethiopian revenue and customs authority large taxpayers’ office. Recently, Melat (2016) tries to identify factors affecting tax audit effectiveness evidence from large taxpayer’s office of Ethiopian revenue and customs authority on auditors’ perception.

This study is different from previous researches by the type of research design and approach it adopts as well as by consideration of tax audit practice and its significance in increasing revenue. Therefore, the purpose of this study is to investigate tax audit practice and its significance in increasing revenue: the case of bale robe town administration by employing mixed research approach to fill the above gap.

2.3. Conceptual Framework

A conceptual framework is a structure of concepts and theories which are put together as a map for the study and it shows the relationship of research variables (Kothari, 2004). The framework is usually used to explain the relationship between the independent variables and the dependent variables of the study.



Source: Compiled from extensive review of the related literature by researcher

2.4. Literature Summary and Knowledge Gap

Tax audit practice is a current issue for both developing and developed countries. In the theoretical review, to the knowledge of the researcher, there is no standard as to the percentage of audit methodologies to be conducted in a given tax authority. In addition, there is no adequate literature regarding the appropriate audit examination techniques to be used for checking the accuracy of tax returns in line with the level of economy and technological advancement.

The empirical studies that have been reviewed in the preceding section (like study conducted by; J.Alm and McKee, 2006,Badara, M.S. 201; Niu ,2010; Burcu Gediz Oral and Ferhan Sayın, ,2015; Getaneh, 2011; Netsanet, 2014; and Atisbha, 2016) focused on the different audit strategies that affect tax compliance behavior, income tax in particular, and the use of sampling tax audit strategy for improving the tax audit coverage. In addition, most prior studies regarding tax audit issues tried to examine the possible audit strategies including the use of audit information for the purpose of compliance improvement and fraud detection, and the impact of component reporting requirements on taxpayer incentives to misstate the tax liability.

However, as far as the knowledge of the researcher is concerned, it is possible to conclude that although there have been some studies on tax audit related issues both in developed and developing countries, Ethiopia in particular, the studies did not explore challenges in tax audit thoroughly though some has been said about the practices. Most of those studies had made a little effort to address on issues related to practices of tax audit, and major issues that focus on its significance has not been well elaborated.

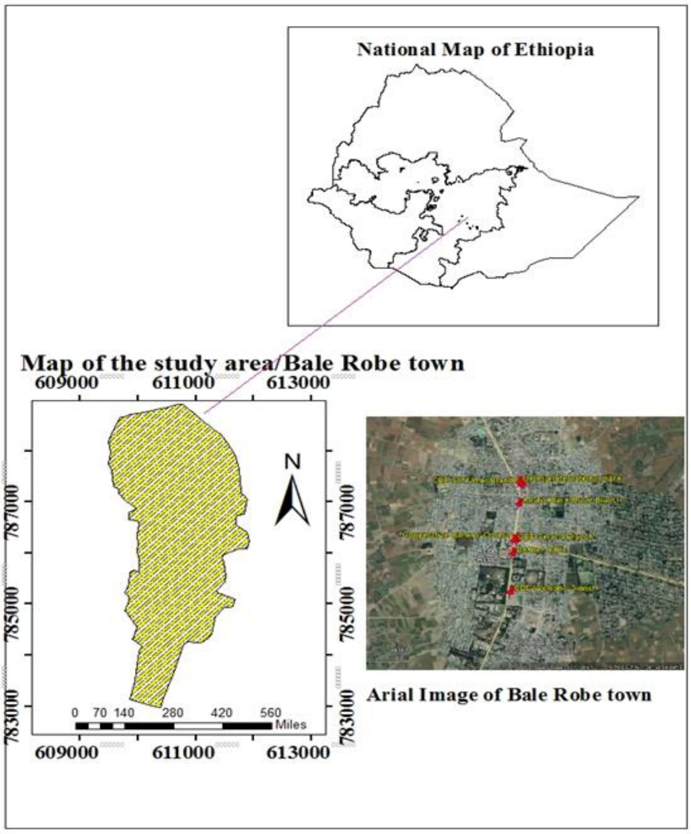
Based on these gaps in the literature together with the problems stated in section one of chapter one, and in order to attain major objective of the study, the following research questions were Addressed; What does tax audit practice look like in bale Robe town administration. How does tax audit in increasing government's revenue by strengthening tax administration capacity? How does tax audit practice minimizes tax evasion in bale Robe town administration? What is the significance of tax audit leads to taxpayers‟ compliance with tax laws? What does tax audit legal frame work look like in bale Robe town administration? Furthermore questions that associated with tax audit significance in bale Robe town administration Revenue Authority were raised.

CHAPTER THREE

RESEARCH DESIGN &METHODOLOGY

3.1. Description of the Study Area

Robe town is found in Oromia region, Bale zone. The total population of the town is estimated up to 92,000 and among this 43,000 are female (Robe town Administration).It is located 430km distance from the capital city, Addis Ababa. The relative location of Robe town from the north Gassera woreda, from the south Goba woreda, from the east Sinana woreda and from the west Dinsho woreda.The climate condition of Robe town 25" hot and 12" cold. According to the document of Robe town administration office most of the society in the town are different ethnic groups mainly Oromo and Amhara. This place has deep rooted value for Oromo people who are the brain child of the culture of the "Gada" system as it has been recurrently indicated by elders and researchers. In addition, the town is occupied with different religion followers such as Orthodox, Muslims and Protestants (Robe town Administration, 2002).



3.2. Research Approach

The quantitative research paradigm subscribes to the philosophy of positivism (Glesne &Peshkin, 2002; Sale, 2002). A positivist researcher believes that reality is objective and independent of the observer. This type of researcher can also measure and predict reality (Orlikowski & Baroudi, 1991; Walliman, 2005; Biggam, 2011). The qualitative research paradigm, on the other hand, does not rely on numerical data because it focuses on explaining events and people as well as issues related to events and people (Fox & Bayat, 2007; Robson, 2011). The researcher used a quantitative and qualitative research paradigm or the mixed research approach in integrated way since the primary goal of this research is to gain a better understanding of tax audit practice and its significance in increasing revenue in bale Robe town administration, it is impressive that the results obtained were generalizable to different types of organizations.

3.3. Research Design

Once the research project is identified and defined clearly, the next step is to design the research method, because the research design provides guidelines for data collection. A research design is a plan for collecting and utilizing data so that desired information can be obtained as defined by Paul et al (2009). Thus, the researcher used an explanatory research design for the study because an explanatory research design intends to explore the relationships existing between the independent and dependent variables of the study. As a result, the study will adopt an explanatory research design which explains the tax audit practice and its significance in increasing revenue in bale Robe town administration

3.4. Population of the Study

Under this study, the population was solely the Robe town administration (Revenue and Audit officers) and some management members. The population under this research comprises 120 Revenue and Audit officers and management members who are from the Large tax payers office. The reason in which this research work based in Large tax payers office is, because this office is the largest tax collection office in Robe town administration which contributes a large annual tax collection and the office is well organized than other branches, this makes the researcher want to focus on this office.

3.5. Sampling technique

In this study the researcher used non probability sampling which is judgmental purposive sampling because sampling procedure which does not afford any basis for estimating the probability that each item in the population has of being included in the sample. This enables the researcher to address all level workers in order to get reliable information. In this case Robe town Revenue administration has got different divisions of work unit as well management stages.

3.6. Sampling size

For this reason, from the total population of 120, the sample size is determined by using the following formula, which is presented by Yamane (1967:886) as used by Israel, (1992).

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

Where, n=sample size

N= total population; which in this case will be 120

e= precision level (sampling error); which is standard and fixed 0.05

$$n = \frac{120}{1 + 120(0.05)^2}$$

$$n = \frac{120}{1.3}$$

.n=92, sample size will be taken

Therefore, the samples were selected deliberately by the researcher. Hence, the researcher believed that judgment sampling was preferable to take the sample size mentioned.

3.7. Data collection instruments

The study used both primary and secondary data which are collected from Robe town administration Tax Audit staffs and summaries of monthly and yearly tax audit and tax collection report. Based on this the main instruments used to collect data are Questionnaires. By referring standardized questionnaire formats the researcher tried to develop the questionnaires. Data's are the basic input to conduct meaningful research. In conducting the research the data that are used are both primary and secondary data. Among the different primary data collection methods questionnaires are the most usually applied in this research paper. The questionnaire contains some open – ended, which need further elaboration and suggestion by the respondent. Whereas, the remaining closed –ended questions about tax audit application and its efficiency and effectiveness.

3.7.1. Questionnaire Design

Questionnaire design for tax audit surveys typically helps to extract information on the characteristics of the Organization, issues of tax evasion, tax compliance, tax related malpractices by tax payers and other related issues like tax audit practices. The respondent's high and medium educational qualification and moderate experience make the responses given more valid and reliable; furthermore most of the respondents were expected to have average work experience. So, experience and educational qualification can matter a lot in the reliability of the response given (Donald H & Theresa I, 2007). Besides, secondary data's are collected in the form of financial data's (Amount of tax collection vs. tax collection during audit) which will help to strengthen the responses given through questionnaires.

3.8. Data analysis

Collected data were analyzed through descriptive statistics then proper tools and a technique has been applied for classification and analysis of data. The main tools that can be applied for classification of data are tables. Excel and SPSS software helped to transform the variables into format suitable for financial data analysis, after which SPSS software has been used for the analysis.

In addition to the above, other statistical tools such as ratios and percentage are used for the analysis (For the Questionnaires).The analysis is also based on the revenue collection performance of the Robe town administration. Assumptions tests to use in T-test are,

- Continuous dependent variables,
- Independent variables have a normal distribution
- The data must be collected from a representative, randomly selected portion of the population.
- Reasonably large sample size

3.9. Validity and Reliability

The most important criterion of research is validity. Validity is concerned with the integrity of the conclusions that are generated from a piece of research. Validity suggests fruitfulness and refers to

the match between a construct, or the way a study conceptualizes the idea in a conceptual definition, and the data. It refers to how well an idea about reality fits in with actual reality.
Actually, quantitative studies are more interested in giving a fair, honest, and balanced account of social life from the viewpoint of someone who lives it every day (Neuman, 2003). In today‟s research most popular reliability statistics is Cornbrash's alpha

3.10.Validity

The researcher will check the validity of questionnaires developed for this study. Before distributing the final questionnaires to the respondents, it were properly checked and commented by few employee of Revenue office and the advisor of the researcher. The final version of the Questionnaires were distributed after incorporating all the comments and feedbacks obtained from them the researcher re designed the questioner.

3.11. Reliability

Cronbach alpha provides a measure of internal consistency of a test or scale. It is expressed as a number between 0 and 1 and the higher the score of cronbach alpha, the more the reliable the generated scale is and the closer the alpha coefficient is to 1.0, the greater the internal consistency and the reverse is true. (Cronbach, 1951). Accordingly the researcher will make pilot test and analyze it by the help Cronbach Alpha in order to insure the reliability of the questionnaire and got the following result.

3.12. Ethical Consideration

The researcher reflects on the ethical issues in every aspect of the activity doing this study. While revising the literature which is done previously by different scholars the researcher try to acknowledge each of the literature sources. Furthermore a letter from Madda Walabu University is written to Revenue office to assure that the study is meant to be used for academic purpose.
Confidentiality and anonymity of the respondent were ensured while carrying out the study.
Participants also not expected to disclose their personal information.

CHAPTER FOUR

4. DATA ANALYSIS AND PRESENTATION

Introduction

This chapter presents results and discussions based on the analysis done on the data collected from the respondents. Then, the results of the study are discussed by using the findings obtained from different source results: questionnaire results, and interview results. The discussion attempts to accomplish the objectives of the study, and answer the research questions.

The Robe Revenues and Customs Authority is the body responsible for collecting revenue from customs duties and domestic taxes. In accumulation to raising revenue, it is accountable to shield the society from adverse special effects of trafficking. It seizes and takes legitimate action on the people and vehicles involved in the act of smuggling while it facilitates the legitimate movement of goods and people across the frame.

4.1. Analysis of Demographic Characteristics of the Respondents

4.1.1. Response Rate

The study sampled 85 respondents from the target population to collect data to the tax audit practice and its significance in increasing revenue.

The returned questionnaire results are shown in Table 4.1.

Table 4.1 Response Rate

Response Rate	No	Percentage
Returned questionnaire	85	92.39
Unreturned questionnaire	7	7.61
Total	**92**	**100**

Source: Own Survey

4.1.2. Analysis of Demographic Characteristics of the Respondents

The information in table 4.2 illustrates 60(70.6%) and 25(29.4%) employees‟ were male, and female respectively.

Table 4.2. Sex of Respondents

Sex			
		Frequency	Valid Percent
Valid	Male	60	70.6
	Female	25	29.4
	Total	85	100.0

Source: Own Survey

4.1.3. Age of the respondents

Age of the respondents was analyzed. The findings revealed that majority of the respondents (29.4%) who participated in the study were between the ages of 35 and 44 years, followed by (23.5%) who were between 25-34 years, (23.5%) of respondents again were from 45-54, (17.6%) were under 20 years and finally (5.9%) of them were above 55 years The summary of the above analysis is clearly indicated in Table 4.3.

Table 4.3 Age of respondents

Age			
		Frequency	Valid Percent
Valid	Under 25 years	15	17.6
	25 – 34 years	20	23.5
	35- 44 years	25	29.4
	45- 54 years	20	23.5
	Above 55 years	5	5.9
	Total	85	100.0

Source: Own Survey

4.1.4. Academic Qualification of the Respondents

Regarding to the academic qualification of respondents majority 40(47.1%) were Diploma holders whereas 35(41.2%) Bachelor degree and 6(7.1) were Master of Degree; whereas, the least number which is 4(4.7%) of them have another qualification.

Table 4.4 Academic Qualification of respondents

Educational Background			
		Frequency	Valid Percent
Valid	Master degree	6	7.1
	Bachelor degree	35	41.2
	Diploma	40	47.1
	Other	4	4.7
	Total	85	100.0

Source: Own Survey

4.1.5 Experience of the respondents

The study included the identification of the worker experience of the respondents. As to the experience majority of employees 38(44.7%) were more than 5 years**,** 22(25.9%) were between 4-5 years of experience, 16(18.8%) were 1-3 years and the rest 9(10.6%) were less than 1 year. Therefore, majority of employees‟ had remarkable working experience.

Table 4.5. Experience

Experience			
		Frequency	Valid Percent
Valid	Less than1 year	9	10.6
	1- 3 years	16	18.8
	4 – 5 years	22	25.9
	More than 5 years	38	44.7
	Total	85	100.0

Source: Own Survey

4.1.6 Position of the respondents

The study indicated that majority of employees 75(88.2%) were Experts and 10(11.8%) were Leaders at different level in the organization.

Table 4.6. Position of the employees

		Frequency	Valid Percent
Valid	Leaders	10	11.8
	Experts	75	88.2
	Total	85	100.0

Source: Own Survey

4.2. Analysis Using Descriptive Statistics

Table 4.7 Descriptive Statistics

No.		N	Mean	Deviation
1	Do you Agree that Tax Audit have a significant impact on increasing Governments	85	1.86	1.025
3	What do you think that the impact of tax Audit on Reduction of Tax Evasion and other Fraudulent intensions?	85	2.13	1.242
5	Do you Agree with the function of tax audit will increase tax payer's compliance with	85	1.65	.909
7	Is there effective sanction on non-compliance With the tax rules and regulation?	85	1.47	.609
8	By whom Audit functions are performed?	85	2.59	.603
9	By whom Audit Files are selected?	85	2.80	1.100
10	What type of audit most usually applied in Robe town Revenue Administration?	85	2.26	1.399
11	Which type of assessment most usually applied in Robe town Revenue Administration?	85	2.35	.767

Question No.1: Do you Agree that Tax Audit have a significant impact on increasing Governments Revenue

Table 4.8. Descriptive Statistics

		Frequency	Valid Percent
Valid	Strongly Agree	42	49.4
	Agree	20	23.5
	Neutral	18	21.2
	Disagree	3	3.5
	Strongly Disagree	2	2.4
	Total	85	100.0

Source: Own Survey

The survey results showed that, out of total samples respondents 49.4% of them stated that they strongly agree that Tax Audit has a significant impact on increasing Governments Revenue, 23.5% of them stated that they agree, the rest 21.2%, 5.9 % them stated that they are Neutral and Disagree and Strongly Disagree .From this we can conclude that 72.9% of the respondents with the mean value of 1.86 and standard deviation of 1.025 are in agreement with tax audit can increase Governments Revenue significantly. Furthermore these responses are collected and summarized from the answers given to question number two of the questionnaire attached in the annex part. As a result, the response indicates that Auditing makes tax payers to fear the tax laws and regulations & this makes them to comply with the tax laws, consequently revenue will increase. Besides, it will reduce collision between employees and tax payers (reduce tax fraud). Hence, it helps tax payers to take due care before declaration of their report this will reduce un-intentional mistakes done by tax payers. However, since some tax payers are not educated and they don’t understand the purpose of paying tax, they are not dedicated to pay tax rather they tried to avoid. So, tax audit will teach such tax payers about the purpose of paying tax and helps to develop their bad taxpaying capability and helps them to be a good tax payer in the future. (Help to apply modern tax collection system through educational process.). In addition, due to fear of criminal and administrative penalty and Interest, tax payers become pushed to pay their taxes on a timely basis.(it reverse the adverse behavior of tax payers by levying penalty and interest,). Moreover, it helps Government to collect further revenue from penalty and interest.

Table 4.9 Tax Evasion and other fraudulent intensions

Question-No.3: What do you think that the impact of tax Audit on Reduction of Tax Evasion and other fraudulent intensions?			
		Frequency	Valid Percent
Valid	Very High	35	41.2
	High	22	25.9
	No Impact	16	18.8
	Low	7	8.2
	Very Low	4	4.7
	Don’t Know	1	1.2
	Total	85	100.0

Source: Own Survey

Regarding the impact of tax Audit on Reduction of Tax Evasion and other fraudulent intensions, 41.2% of the survey respondents and 25.9% of them stated that the impact of tax payers audit in reduction of tax evasion is very high and high, 18.8%, 8.2% and 4.7%% of the respondents stated that there is no impact, low impact and very low impact. In addition, 1.2% of them have no idea about it. From this we can see that 67.1% of the respondents with the mean value of 2.13 and standard deviation of 1.242 are in agreement with the impact of tax Audit on Reduction of Tax Evasion and other fraudulent intensions are high.

Besides, these responses are collected and summarized from the answers given to question number four of the questionnaire attached in the annex part. Hence, most of the corruptions occurred on tax are through the reduction of Sales or Increasing of expense, this can happen by hiding sales receipts and adding fake receipts . This can reduce the revenue or increase the expenses of the auditee, as a result `profit and tax were reduced. So, such fraudulent findings can be caught through the activity of tax Auditing. Additionally, among the objective of Auditing is balancing between Facilitation and Control. Besides, due to tax audit tax payers compliance with the tax laws will increase as a result fraudulent activities can reduce. Furthermore, audit makes tax payers to learn from their past mistakes (fraudulent activities), help them to made corrections also audit makes tax payers to fear & to follow tax rules in case decrease tax evasion.

Table 4.10 Tax payer's compliance

Question-No. 5: Do you Agree with the function of tax audit will increase tax payer's compliance with			
		Frequency	Valid Percent
Valid	Strongly Agree	46	54.1
	Agree	30	35.3
	Neutral	4	4.7
	Disagree	3	3.5
	Strongly Disagree	2	2.4
	Total	85	100.0

Source: Own Survey

The survey respondents further showed that, they agreed with the function of tax audit will increase tax payer's compliance with tax law. As it is clearly indicated on table above, out of the total respondents 54.1% of them stated that they strongly agree that the function of tax audit will increase tax payer's compliance with the tax law, 35.3% of them stated that they agree, the rest 4.7%, 3.5% and 2.4 stated that they are Neutral, Disagree and Strongly Disagree. From this we can conclude that 89.4% of them with the mean value of1.65 and standard deviation of .909 are in agreement with the function of tax audit will increase tax payer's compliance with tax law.

This result is in agreement with the study done by Kennedy & John Obi , (2014), which examines the impact of tax audit on the tax compliance level of companies in Nigeria.

The result showed that there exists a positive relationship between tax audit and tax compliance. The result also revealed that the probability of being audited, perception on government spending, penalties and enforcement, the joint effect of tax audit and penalties have a tendency to significantly influence tax compliance in Robe town. This indicates that the result of this part have similarity with the above study which is done in this area.

Furthermore these responses are collected and summarized from the answers given to question number six of the questionnaire attached in the annex part. Hence, one of the purposes of

Auditing activity is teaching the Auditee or creating positive awareness to the tax payers. Through learning it is possible to avoid bad taxpaying experience and noncompliance with tax laws, which finally helps to increase revenue. Besides**, t**ax audit declares hidden taxes and over passed tax laws by tax payers, as a result penalty and interest will imposed and pushes the tax payers to incur additional costs. So, fear of criminal and administrative penalty and Interest helps tax payers to comply with tax laws.(it reverse the adverse behavior of tax payers by levying penalty and interest,). Moreover, audit will help qualified tax payers to learn from their mistakes from the previous tax audit findings. This can help them to correct their previous year's mistakes and make them ready for future correction, (to be compliant with the law.)

Table 4.11 tax rules and regulation

Question- No. 7: Is there effective sanction on non-compliance With the tax rules and regulation?			
		Frequency	Valid Percent
Valid	Yes	50	58.8
	Neutral	30	35.3
	No	5	5.9
	Total	85	100.0

Source: Own Survey

As it is shown that 58.8% of the respondents state that there is effective sanction on non-compliance, the rest 35.3% and 5.9 % of the respondent's state that they are neutral and there is no effective sanction. From this we can conclude that the mean value of 1.47 and standard deviation of .609 indicates that even if there are sanctions during noncompliance but there are also situations in which these sanctions are not implemented.

Table 4.12 Audit functions

Question-No.8: By whom Audit functions are performed?			
		Frequency	Valid Percent
Valid	Individual Auditor	5	5.9
	Audit Team	25	29.4
	Both	55	64.7
	Total	85	100.0

Source: Own Survey

The survey indicates that 5.9% of the respondents states that Audit Functions are done by a single Auditor, 29.4% of the respondents states that Audit Functions are done by Audit Team and 64.7% of the respondents states that Audit Functions are done by both. Hence, based on the majority of the respondents with the mean value of 2.59and standard deviation of .603 Audit Functions are done by both Individual Auditor and Audit Team.

Table 4.13 Audit Files are selected

Question-No.9: By whom Audit Files are selected?			
		Frequency	Valid Percent
Valid	By an Auditor	15	17.6
	By an Audit Team	16	18.8
	By Audit Manager	25	29.4
	By one of the Above	29	34.1
	Total	85	100.0

Source: Own Survey

The survey indicates that 17.6% of the respondents states that Audit files are selected by a single Auditor, 18.8% of the respondents states that files are selected by Audit Team and 29.4% of the respondents states that Audit files are selected by audit manager and 34.1% of the respondents states that Audit files are selected by one of the Above *This with the mean value of* 2.80 and standard deviation of 1.100 can indicate that there are situations in which tax payers files are selected by individuals, which can result in collision between Auditors and Customers which finally resulted in to a case of corruption.

Table 4.14 Applied in Robe town Revenue Administration

Question No.10: What type of audit most usually applied in Robe town Revenue Administration?			
		Frequency	Valid Percent
Valid	Full audit	44	51.8
	Limited scope audit	5	5.9
	Single issue audit	6	7.1
	Any of the three as appropriate depends on the risk identified	30	35.3
	Total	85	100.0

Source: Own Survey

The survey indicates that 51.8% of the respondents states that there is full audit applied in their organization, 5 . 9 % of the respondents states that there is Limited scope audit applied in their organization, 7.1% of the respondents states that there is Single issue audit applied in their organization and 35.3% of the respondents states that there is any of the three as appropriate depends on the risk identified audit applied in their organization. Hence, with 35.5% based on the majority of the respondents with the mean value of 2.26 and standard deviation of 1.399 can indicate that there are situations in which either of Full audit, Limited scope audit or Single issue audit applied in Robe town Revenue Administration.

Table 4.15 Type of assessment most usually applied

Question No.11: Which type of assessment most usually applied in Robe town Revenue Administration?			
		Frequency	Valid Percent
Valid	Administrative assessment	15	17.6
	Self-assessment	25	29.4
	Both	45	52.9
	Total	85	100.0

Source: Own Survey

The survey indicates that 17.6 % of the respondents states that there is Administrative assessment applied in their organization, 2 9 . 4 % of the respondents states that there is Self-assessment applied in their organization, 52.9% of the respondents states that there is both Administrative assessment and Self-assessment applied in their organization. Hence, with 52.9% based on the majority of the respondents with the mean value of 2.35and standard deviation of 767 can indicate that there is both Administrative assessment and Self-assessment applied in their organization. From the responses given by the respondents, to question twelve and thirteen, respondents indicated that there is a no strong control of tax evasion and avoidance, there is no any reward mechanism of honest tax payers and poor training service for tax auditors. From their response this can negatively affects the tax revenue collection activity of Robe town revenue administration. So, there must be a strong control of tax evasion and avoidance through strong enforcements like penalty and interest.

CHAPTER FIVE

5. CONCLUSION, FINDINGS & RECOMMENDATIONS.

This chapter provides concluding remarks of tax audit practices of Robe town revenue administration. The conclusions are supported by a summary of the results from the analysis on prevailing tax audit practice and tax performance. The chapter also contains a couple of recommendations aimed at improving overall revenue mobilization of Robe town revenue administration.

5.1- Conclusion

The result of the survey indicates that, the majority of respondents are in agreement with the function of tax audit can increase tax payer's compliance with tax law. Awareness Creation, Penalty & Interest and Bad Audit Experience are issues which are raised as results of tax audit which can increase of tax payer's compliance with the law.

Regarding the impact of tax Audit on reduction of Tax Evasion and other fraudulent intensions, the survey indicated that the respondents are in agreement with the impact of tax Audit on reduction of Tax Evasion and other fraudulent intensions are high. Facilitation and Control, Increasing compliance, Bad auditing experience and Fear of Audit are issues which are raised as a result of tax audit which helps to reduce tax evasion.

Furthermore, the results of the survey indicates that , even if there are sanctions during noncompliance but there are also situations in which these sanctions are not implemented. There are also situations in which tax payers files are selected by individual tax auditors, which can be a cause for collision between Auditors and Tax payers can finally resulted in a case of corruption.

Besides, Full (Comprehensive Audit) is the type of audit mostly performed by Robe town revenue administration, tax audit unit than Cut-off Audit, and Limited Scope Audit will also be performed accordingly. This is one of the strengths of Robe town revenue administration, which contribute a lot in more tax revenue collection. Regarding the assessment methods, Even though, self-assessment method can lead to collision between Auditors and tax payers for adjustment to be done, but in the survey it is indicated that Robe town revenue administration performs both Administrative and Self-Assessment methods comparable.

An indication of absence of strong control on tax evasion and avoidance, absence of any reward mechanism to honest tax payers and poor training service for tax auditors are issues raised by the respondents , which needs to be focused by Robe town revenue administration. Furthermore, it is stated that, this issues have their own contribution in the reduction of the tax revenue collection activity of Robe town revenue administration.

From the previous studies done, it is shown that Tax audit actually has an effect on increasing Governments revenue, but as per the results of the secondary data collected from Robe town revenue administration implied that, there is statistically no significance correlation between tax collected before the audit and to that of after the audit. This clearly indicates the effort done in Tax Audit in Robe town revenue administration is not enough, Lack of highly experienced tax auditors, low level of awareness raising activity to tax payers and manual tax auditing system can be raised as a core reason for this result.

5.2- Findings

Even if the major aim of this research is to show the effect of tax audit on Governments Revenue, but there are situations which affect and hinder the Tax collections process and the Tax Audit activity as well. So, the major findings are the following:

Insufficient number of Tax Auditors: Even if Tax Audit has a great impact on increasing Governments Revenue, but this is not the case of Robe town revenue administration one of the reasons for this is, the number of Tax Auditors done do not match with that of the number of Tax payers. Audit coverage per year is a lower audit coverage status. Smaller audit coverage, resulted in lower tax revenue collection from tax audit functions. Manual Tax Audit System: The Tax Audit system is not supported by Computer Assisted Audit software is not supported by technology like Computer Aided Audit Tool (CAAT). Rather the Audit work is done manually.
Uncompetitive salary payment scale: This can force experienced tax auditors to resign and to be substituted by new un experienced auditors. Finally it can lead to poor Tax Audit performance. Poor Awareness Raising and customer relation Activity: The presence of weak Tax Payers

awareness raising activity can lead tax payers to submit lower amount tax unknowingly. This consequently reduces government's revenue.

Tax Payers Complain : High customer complains to pay tax due to system problem and miss-match between the number of tax collection staffs and number of tax payers this takes the tax payers two or three days to pay his tax. Which resulted in customer complain.

Insufficient Training Service*:* In order to cope up with the current dynamic business environment training to auditors is vital, which helps them to upgrade and refresh their knowledge and to give a better reliable service and be competitive. But the trend of Robe town revenue administration, LTOs training service for tax auditors is no sufficient. Trainings are given once or twice a year which is not timely and sufficient in the current ever changing business environment. Therefore the researcher concludes that, the above findings are a base for noncompliance. And tax avoidance, which have a negative impact in decreasing Governments revenue.

5.3 - Recommendations

Tax audit should be disbursed on a routine basis to confirm that actual revenue collected is what the relevant tax authority remits to the government. Supported on the tax administration and within the context of tax audit practice with a special reference to the Robe town revenue administration and based on the findings obtained the subsequent recommendations are made:

Increasing the quantity of Tax Auditors: Since the office of Robe town revenue administration is that the largest tax collection office of Robe town revenue administration, it has to be lean higher attention than different offices. The higher the tax collection the higher, the corruption and risk of miss-statement of financial economic reports. So, as to safeguard such mischievous activities, the contribution of tax audit is higher. In order to have strong tax audit system, there should be qualified auditors with enough range.
Better Training service: In order to cope up with the ever changing dynamic business environment, Robe town revenue administration must update tax auditors through trainings completely. Even though its expensive, , it is very vital important to auditors, which helps them to upgrade their knowledge and to give a better reliable service. So, it is better for Robe town

revenue administration if off Job trainings are given on a quarterly basis, otherwise tax payers will deceive tax auditors easily.

Computer Assisted Audit Tools (CAATs) :- Relevant higher officials and tax auditors and should have full knowledge of modern audit tools like, Computer Aided Audit Tools (CAATs) to reinforce performance and maximum tax revenue generation. The importance of tax revenue to the government cannot be over emphasized especially now that government over dependence on Agricultural products is falling because of global drop in prices. All relevant authority should to encourage tax audit for increase in tax revenue, in order for government to stay up with its obligation to his citizen.

Continuous education : Awareness rising should be provided to the tax payers by the Robe town revenue administration in order to create awareness about their rights and obligations so as to build and develop a better partnership with them and also to create citizens who have better understanding of taxation which will engender honest and voluntary compliance.

Strong Control: To have a successful revenue collection, there is the need to have a strong control not only on the tax evasion but also on tax avoidance by applying effective and efficient tax audit based on reliable evidences and documents.

Strong Reward and Penalty mechanism: The tax collection system should be designed in such a way that not only the tax evasion but also the tax avoidance becomes very expensive for the taxpayer and compliance very rewarding.

Establishing Good Relationship with Tax payers: increased accountability and an open and honest relationship with taxpayers are crucial for maintaining public trust and confidence in the performance of tax administration. Taxpayers must be able to expect a high degree of certainty in their dealings with revenue agencies. This can only be achieved when tax laws, regulations, procedures, and administrative guidelines are made public, easily accessible, and applied in a consistent manner by avoiding unstable tax laws which creates confusion not only for tax payers but also for tax auditors.

Optional Payment Mechanism: Since there are customers who have complains in the area of tax collection due to system failure, Robe town revenue administration has to think about other cash collection mechanisms as an option. i, e, manual tax collection mechanism.

System Designing: Most tax payers of any country generally do not want to pay taxes unless compelled by a situation where they are left with no option other than to pay the taxes. Therefore, for better tax compliance, a system should be designed that automatically extracts taxes rather than leaves the payment of taxes to the voluntary choice and morality of taxpayers. To this end tax audit is one of the most powerful revenue administration tools that can ensure that tax payers pay their tax liability with very little room for evasion. Therefore, the tax audit function should be strengthened to minimize both deliberate and innocence tax evasion made by many tax payers. Again appropriate expertise and the necessary resources should be allocated for this tax administration function.

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Appendix-I

Madda Walabu University

School of Post Graduate Studies

<u>Questionnaire</u>

<u>Dear Respondent:</u>

This questionnaire has been prepared in view of assessing the objectives of research entitled "Tax audit practice and its significance in increasing revenue in bale Robe town administration." The purpose of the study is to analyze the prevailing tax audit practice and its significance in tax revenue generation. The primary objective of the questionnaire is to collect data, information & opinion for the conduct of a Senior Thesis for partial fulfillment of the requirement for award of Master of Science in Accounting and Finance. Participation in this project is completely voluntary. Survey results will be recorded anonymously and strict confidentiality were maintained. Individual responses will not be identified in the Researcher's MSC thesis.

The questionnaire has two parts: Part -I is about your personal information. Part-II is the overall questions about Tax audit practices. Please give your honest response to each item.

Thanking you in advance for your valued time & cooperation, the researcher believes that your genuine response, opinions & views are used only for academic purpose.

Eyob Nigussie

The Researcher,

N.B please give your answer on the space provided & put tick a ✓ mark In the box corresponding to your response.

<u>Personal Information</u>

- Sex Male ☐ Female ☐
- Age ________
- Educational background _______________
- Position of respondent__________________________
- Number of years of experience ______________

Instruction:

Please use a tick (√) mark for your thought and where appropriate give your opinion for the open ended questions.

1. Do you Agree that Tax Audit have a significant impact on increasing Governments Revenue?

   - ☐ Strongly Agree
   - ☐ Agree
   - ☐ Neutral
   - ☐ Disagree
   - ☐ Strongly Disagree

2. If your answer is „Strongly Agree or Agree‟ please explain.

   ____
   ____
   ____
   ____
   ____

3. What do you think that the impact of tax Audit on Reduction of Tax Evasion and other fraudulent intensions?

   - ☐ Very High
   - ☐ High
   - ☐ No Impact
   - ☐ Low
   - ☐ Very Low
   - ☐ Don’t Know

4. If your answer is „Very High or High" please explain.

____

____

____

5. Do you Agree with the function of tax audit will increase tax payer's compliance with tax law?

☐ Strongly Agree

☐ Agree

☐ Neutral

☐ Disagree

☐ Strongly Disagree

6. If your answer is „Strongly Agree or Agree" how? Please explain.

____

____

____

____

7. Is there effective sanction on non-compliance with the tax rules and regulation?

☐ Yes

☐ Neutral

☐ No

8. By whom Audit functions are performed?

☐ Individual Auditor

☐ Audit Team

☐ Both

9. By whom Audit Files are selected?

☐ By an Auditor

☐ By an Audit Team

☐ By Audit Manager

☐ By one of the Above

10. What type of audit most usually applied in Robe town Revenue Administration?

- ☐ Full audit
- ☐ Limited scope audit
- ☐ Single issue audit
- ☐ Any of the three as appropriate depends on the risk identified

11. Which type of assessment most usually applied in Robe town Revenue Administration?

- ☐ Administrative assessment
- ☐ Self-assessment
- ☐ Both

12. What has to be done by Robe town Revenue Administration to reduce noncompliance, Evasion and corruption in order to increase tax revenue?

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____

13. Do you have any ideas, opinions and suggestions that have not been included in the aforementioned questions?

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