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AWARENESS, KNOWLEDGE AND PERCEPTION OF TAX PAYERS TOWARDS VALUE ADDED TAX (VAT) ADMINISTRATION IN YIRGALEM TOWN, SIDAMA ZONE, SNNPR STATE, ETHIOPIA

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ABSTRACT

The study was undertaken with the main objective of assessing the practices and challenges of VAT administration in Yirgalem Town Administration. Both primary and secondary data were deployed for the study purpose. Yirgalem Town Administration was selected purposively as the study area. By adopting simple random basis 83 tax payers selected as sample respondents. Structured questionnaire was prepared to collect primary data from the tax payers. Simple statistical tools such as frequency table and percentages were used for data analysis and interpretation. The findings of the study show that majority of the respondents do not aware about the intricacies of VAT administration and thus having poor knowledge. However, more than 70 percent of the respondents perceived that VAT has helped them to increase sales, turnover, price reduction, revenue to government and ease of accountability. Most of the respondents perceived that there was an improvement in VAT collection and their profession. Nonetheless, majority of the respondents disagreed on the service delivery mechanism of Yirgalem Revenue and Customs Branch Office. As to challenges majority of the respondents perceived that VAT leads to maintain unnecessary documents, increase in operational expenses, involves more paper work, complicated procedure, burden to customers, difficult to administration and poor institutional capacity.

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INTRODUCTION

Taxes are normally classified as direct and indirect. Direct taxes are levied on the income, profit, capital gain and wealth of persons and companies, the most well-known direct tax being person income tax. On the other hand, indirect taxes are levied on transactions, goods and service, not directly imposed on companies and individuals. Value Added Tax (VAT) is one of those indirect taxes. The value added at each stage of production is the difference between the seller's material costs and the selling price.

In essence, VAT is just a general sales tax that is collected at multiple stages. VAT is a key source of government revenue in most of the nations. It was introduced in more developed countries of Europe and Latin America. Ethiopia's tax reform program has introduced VAT at the rate of 15% (fifteen percent) on January 1, 2003 to replace the sales tax proclamation that provides exemption for basic necessities and domestic transportation and zero rating to encourage exports and capital investments. Subsequent to the introduction of VAT, additional exemptions were extended to basic foods,

agricultural fertilizers and to other products. Unlike the sales tax, VAT provides relief of tax on all business inputs, including capital goods and business expenditures and will provide further business incentives by zero rating exports and the international transport of goods and passengers. Since domestically produced goods relieved of VAT, they will be more competitive within international markets. In the Ethiopian context of VAT system, a threshold of half a million Birr is a level above which registration for VAT is legally compulsory. However, the taxpayers below this threshold and engaged small scale businesses such as distributions of goods and domestic trade services are also forcefully categorized as VAT payers contrary to the proclamation (Demirew Getachew, 2004).

Statement of the problem

VAT is a tax on the final consumption of certain goods and services. But it is collected at every stage of production and distribution. VAT is gathered by all entities providing taxable goods and services and imposed on sales to all purchases. A business firm calculates its VAT liability by the VAT rate. The VAT Proclamation No.285/2002 was issued on 4th July 2002 by the Council of People's Representatives to be enforced as of January 2003. The introduction of VAT facilitates substantial improvement in overall tax administration, and indeed adoption of the VAT is often seen as an opportunity for overall tax administration and modernization. The introduction of the VAT, however, has occasionally disrupted the functioning of an existing administration because of inadequate preparation, lack of uniformity in application, lack of awareness by the side of the Taxpayer, application contrary to the law and problems related with institutional capacity. Since the VAT is a tax that is levied on the consumer, it does not constitute a tax on business. In effect, a registered VAT taxpayer is charging and collecting funds that are being held in trust for the government before being remitted to the Ethiopian Revenue and Customs Authority (ERCA). However, ERCA took adequate experiences from other countries before enacting the law and even after due implementation regarding the types of fraudulent activities that have been commonly encountered by many countries where by VAT laws have been introduced. Fraudulent actions deny countries revenue entitlements; create competitive inequalities in the business environment and affect honest business taxpayers. Even though, ERCA has undergone an intensive educational program to improve awareness of tax payers and the general public, there are various problems which restraint the effective implementation of VAT in the country. Further studies assessing the practices and challenges of VAT administration although available few in numbers, such a study is new in the context of the study area (Yirgalem Town) Hence, by the understanding the research gap this study has been undertaken.

Specific Objectives of the Study

The specific objectives of the study are:

- To study the extent of awareness and knowledge of tax payers towards the Value Added Tax.
- To assess the perception of tax payers towards Value Added Tax.
- To identify the challenges of Value Added Tax administration.

MATERIALS AND METHODS

Description of study Area

The study was conducted in Yirgalem Town, Sidama Zone, Southern Nations, Nationalities and Peoples Region (SNNPR) of Ethiopia. It is located at about 45 kilometers of Hawassa which is the capital city of SNNPR and 322 km far from Addis Ababa the national capital. The Town has a latitude and longitude of 6:45'N 38 25'E and an elevation of 1776 meters. Mean annual rainfall varies from 801-1600. It has three agro-ecological Zones, namely *Kolla* (low land and warm), 30.5 per cent; *woina-dega* (moderate), 50 per cent; and *Dega* (cool), 19.5 percent. (BoFED, 2002 E.C.).

Source of data

Both primary and secondary data sources were used for the study with more reliance on the primary sources. Management team, VAT payers, private limited companies were the prime utilized sources of primary data from sample town Administration. Moreover, secondary data was collected from the Yiegalem Town Revenue Customs Authority Branch Office and Regional revenue customs authority bureaus.

Sampling procedure and technique

As far as sampling procedures is concerned, multi-stage sampling technique was used. In the first stage Yirgalem Town in Sidama Zone was selected purposively as the study area by adopting the following criteria such as proximity of the town to conduct the research, presence of larger VAT payers and Topographic divisions of Town in to two sub cities when compared with other Towns in Sidama Zone. In the second stage Yirgalem Town is topographically divided into two sub cities namely: Fil Wuha and Arada Sub City. Each sub city has three Kebeles (Villages) totally six Kebeles. The preliminary investigation indicated that there are 140 VAT payers including six Private Limited Companies (PLCs) in the town of which 74 are in Fil Wuha sub city and 66 are in Arada sub city. Furthermore, in order to decide sample size, simple random sampling technique was applied because its gives equal chance being selection of sample respondents. Minimum population sample for this study was determined by using Yamane's formula (Yamane, 1967) in which the list of each VAT payers was used as a sample frame.

$$n = \frac{N}{1 + N(e)^2} = \frac{140}{1 + 140(0.07)^2} = 83$$

Where:

n= Sample Size,
N= Total number of tax payers,
e = Acceptable Level of Error.

In addition, ten management bodies of the Yirgalem Town Revenue Customs Authority Branch were selected on the basis of purposive sampling technique, because they were few in number and their presence was only at main offices. They were contacted through key informant interview.

Instruments and Methods of data collections

Two data collection instruments were used to gather relevant information for the purpose of this study which includes structured questionnaire and key informant guideline.

Table 1. Sample frame (VAT payers including PLC)

S.No	Kebeles	Sub city	Total VAT payers	Sample VAT payers
1	Aposto	Fil wuha	17	10
2	Awada stadium	Fil wuha	09	05
3	Mahali ketema	Fil wuha	40	25
4	Mesinchomewucha	Arada	35	21
5	Wuha limat	Arada	10	06
6	Kidste mariam	Arada	29	16
	Total		140	83

Source: Yigalem Town Administration, 2017

Questionnaire: The structured questionnaire was prepared which includes close-ended questions. The questionnaire consisted of five parts. Questions relating to demographic profile of the respondents were included in part I, statements and questions relating to awareness and knowledge of the respondents about VAT were included in the part II & III respectively, statements which are to be answered in five point Likert's scaling technique (Strongly Agree, Agree, Undecided, Disagree and Strongly Disagree) pertaining to assess the perception of respondents towards VAT were included in part IV and finally statement relating to Challenges of VAT were asked using Likert's scaling technique to eliciting the required data from the respondents in line with the objectives of the study.

Table 2. Respondents' Awareness about VAT

Items	Yes		No		Total	
	F	%	F	%	F	%
Are you aware that government has implemented VAT?	83	100.0	--	--	83	100.0
Are you aware that the Government of Ethiopia is levying VAT on all kind of products?	27	32.5	56	67.5	83	100.0
Are you aware of the fact that you pay VAT whenever you purchase any product?	23	27.8	60	72.2	83	100.0
Are you aware of that some part of your tax amount is paid by the manufacturer, dealers, and after that they levy the same tax on you?	07	8.4	76	91.6	83	100.0

Source: Field survey, 2017

The structured questionnaires were distributed to the respondents with briefing on how to respond and turn back the filled in questionnaire as soon as possible.

Interview: Unstructured interview guideline was prepared and was administered among the management bodies through personal interview technique. Issues pertaining to the VAT administration by the Yigalem Town Revenue Customs Authority Branch Office were gauged through key informant interview. Further, oral discussions were made with few respondents on certain issues after completion of questionnaire survey.

Methods of Data Analysis and interpretation

After data collected, the data were rechecked, coded and entered in to SPSS version 20 for the purpose of analysis. Both qualitative and quantitative data analyses were used. The first and second objectives were analyzed by using descriptive statistical tools such as frequency table and percentage. Third objective was analyzed by using both qualitative and quantitative analysis method.

RESULTS AND DISCUSSION

Tax payers' awareness about VAT

As depicted in table 2 above, all the respondents under study were aware about implementation of VAT.

However, majority of the respondents 56 (67.5%) had no awareness and only 27 (32.5%) were aware that the government is levying VAT on all kind of products. Continuously, 60 (72.2%) had no awareness and only 23(27.8%) of the respondents aware that they pay VAT whenever they purchase any product. Further, majority of the respondents 76 (91.6%) were not aware and only 7(8.4%) aware that some part of their tax amount paid by the manufacturer, dealers and after that they levy the same tax on them. Thus, it may be stated that majority of the respondents were not fully aware of VAT administration system. Study by Bizualem (2015) and Wollela A (2008) and Habtamu D,et.al (2015) also confirmed the similar finding.

The researchers triangulated the survey findings with interview results which confirmed that "at the beginning of VAT introduction there were announcement made by government through different Medias that taxation of VAT do not include food items or food items are free of VAT" now a days they are asked to pay VAT whenever they purchase any product and sometimes they consider conflict of clients. Therefore, there should be clear rules and regulations on VAT not only for the urban for the rural society at large.

Further the officials of Revenue and Customs Authority stated that most of the VAT registered business owners have fair knowledge on the VAT administration and they hire accountants or business consultants during the taxpaying time. They used to consult with the revenue office and complete all the issues concerning VAT.

Table 3. Sources of awareness about VAT (Multiple replies)

Source	Frequency (N=83)	Percent
VAT seminars	25	30.1
Media	30	36.1
Business associate	18	21.7
RCA officers	67	80.7
Auditors	29	34.9

Source: Field survey, 2017

Perusal of table 3 reveals that as high as 80.7 percent of the respondents aware about the VAT through RCA officers as prime source. VAT seminars (30.1%), Media (36.1%) and Auditors (34.9%) were found to be the second major source of awareness. Simon (2015) found that tax payers had attended training organized by Government on VAT administration. However the result of interview with RCA branch officers confirmed that sincere effort has not been made to provide training on VAT to the tax payers due to the difficulty in getting finance and human power.

Nonetheless, the moment VAT implementation was introduced; tax payers were informed through notice. Moreover, officers used to give brief explanation for the clients whenever they have compliant with their VAT payment process. The researcher found out a gap of communication between the clients and RCA officers because the officers believe that the tax payers can get enough information from each other and the media at large.

Knowledge of respondents about VAT

Table 4: Knowledge about VAT

Responses	Frequency	Percent
Little	32	38.6
Fair	34	41.0
Good	14	16.9
Very much acquainted	03	03.6
Total	83	100.0

Source: Field survey, 2017

A cursory look at the table 4 shows that a simple majority 34 (41%) of the respondents have fair knowledge about VAT administration procedure whereas 32 (38.6%) of the respondents have little knowledge about VAT administration procedure. Respondents have good (16.9%) and well acquainted (3.6%) knowledge was found to be insignificant. This is might be due to the fact that most of the respondents have low level of awareness about VAT administration. As indicated in table 5 above the significant majority of respondents 45(54.2%) do not know how to calculate input

and output VAT whereas 38(45.8%) knows how to calculate input and output VAT. On the same table above 52(62.7%) do not know that VAT is included in retail price and 31(37.3%) knows that VAT is included in retail price. In the table above it was indicated that 42 (50.6%) do not know that earning from VAT is a major source of revenue for any state government. Further, the significant majority of respondents 65(78.3%) knows that the VAT revenue which is collected from commodities use for the state welfare. Nonetheless, 63 (75.9%) have no knowledge that some VAT registered business people collect the tax with illegal invoice.

Perception of respondents towards VAT

Perception of respondents towards improvement of VAT collection and Profession

As mentioned on the above table 5 on perception towards improvement of VAT collection and their profession, the survey result shows that majority 64.9 percent (Total of Strongly Agree and Agree) perceived that there was reduction in tax rates after VAT whereas 14.4 percent of the respondents have disagreed on the statement. Nonetheless, respondents who were undecided were found to be 20 percent to the total. With regard to vigilance and recovery, a simple majority (37.3%) of the respondents perceived that there was strict vigilance and recovery whereas 36.1 percent of the respondents have disagreed on the statement. According to the survey, majority (73.5%) of the respondents opined that they use information technology towards improvement of VAT

Table 5. Knowledge about other aspects of VAT

Item	Yes		No		Total	
	F	%	F	%	F	%
Do you know how to calculate input and output VAT?	38	45.8	45	54.2	83	100.0
Do you know that VAT is included in Retail Price?	31	37.3	52	62.7	83	100.0
Do you know that the earning from VAT is a major source of revenue for any State Government?	40	48.2	42	50.6	83	100.0
Do you know that the VAT revenue which is collected from commodities is use for the State welfare?	65	78.3	18	21.7	83	100.0
Do you know that some VAT registered business people collect the tax with illegal invoice?	20	24.1	63	75.9	83	100.0

Source: Field survey, 2017

Table 6. Payment of VAT on time

No	Statement	SDA		DA		UND		A		SA	
		F	%	F	%	F	%	F	%	F	%
1	I pay my taxes on time	-	-	18	21.6	10	12.0	36	43.4	19	22.9

Source: Field survey, 2017

Table 7. Perception towards service delivery by VAT administration authority

Statements	SDA		DA		UND		A		SA	
	F	%	F	%	F	%	F	%	F	%
The government has not made sufficient efforts on introduction of VAT in creating awareness among taxpayers and the society.	12	14.5	09	10.8	06	7.2	38	45.7	18	21.6
Tax administration office do not give constant information	01	01.6	02	2.6	07	8.4	19	22.9	54	65.1
Rate of VAT is high	05	06.0	06	7.2	07	8.4	40	48.2	29	34.2
No training given for tax payers on the issue of VAT	30	36.1	32	38.5	-	-	16	19.3	05	6.0
Tax payers do not know the tax administration rules and regulations well	18	21.6	05	6.0	05	6.0	38	45.7	17	20.5
Revenue officers does not give respectful services to clients	29	34.9	17	20.5	02	2.4	28	33.7	07	8.4
Overall the service delivery of VAT administration authority is good	30	33.7	19	22.9	03	3.6	20	24.0	11	13.3

Source: Field survey, 2017

Table 8. Perception towards benefits of VAT

Statements	SDA		DA		UND		A		SA	
	F	%	F	%	F	%	F	%	F	%
More sales	02	02.6	10	12.0	07	8.4	25	30.1	39	46.9
More turnovers	07	08.4	03	3.6	10	12.0	49	59.0	14	16.7
Revenue to government	04	4.8	06	07.2	12	14.5	48	57.8	13	15.7
Simplified tax procedure	12	14.5	08	09.6	14	16.7	30	36.1	19	22.9
Relief from additional tax	07	08.4	09	10.8	11	13.3	41	49.4	15	18.1
Reduction in price	05	06.0	04	4.8	02	02.4	55	66.3	17	20.5
Easy to accountability	05	06.0	08	09.6	11	13.3	39	47.0	20	24.1

Source: Field survey, 2017

Table 9. Challenges of VAT administration

Statements	SDA		DA		UND		A		SA	
	F	%	F	%	F	%	F	%	F	%
Unnecessary documents	08	9.6	12	14.5	-	-	38	45.7	31	37.3
Increase in operational expenses	12	14.5	03	03.6	05	6.0	38	45.7	25	30.1
Involves more paper work	09	10.8	08	09.6	02	02.4	40	48.2	24	28.9
Complicated procedure	18	21.6	07	08.4	01	01.6	41	49.3	13	15.6
Burden to customers	08	09.6	06	07.2	03	03.6	28	33.7	38	45.7
Difficult to administration	19	22.9	08	09.6	06	7.2	30	33.7	20	24.0
Decrease in demand	08	09.6	30	36.1	12	14.5	09	10.8	24	28.9
The institutional capacity of Yirgalem RCABO in managing the VAT application is poor.	01	01.6	08	09.6	12	14.5	29	34.9	30	33.7

Source: Field survey, 2017

whereas 25.2 percent of the respondents disagreed on the statement. Informal interview with the PLCs and few MSEs shows that although they have VAT machine, it doesn't work whenever the electric power is off which interrupts the machine regularly. There were some VAT registered general distributors when their clients demands attachment receipt needs to wait till the power come back unless appointed for the next purchase time to collect their receipt which is in doubt. In addition, the majority 68.6 percent of the respondents perceived towards improvement of education and awareness of VAT payers whereas 25.3 percent of the respondents disagreed on the statement. As to more collection effort, majority 77 percent of the respondents perceived that more collection effort is needed to improve the VAT collection and profession.

Perception of respondents towards payment of VAT on time

The survey result as depicted in table 6 shows that majority (66.3%) of the respondents have agreed that they are paying the VAT on time whereas 21.6 percent of the respondents were found that they are not paying the VAT on time. Informal interview with the few respondents show that the respondents reflects the weakness of RCA branch office at the Town and also the VAT amount in accordance with some rules and regulations should need amendments and asked that how the businessman living in Yirgalem Town at Woreda (Village) level be treated equally with businessman living in Addis Ababa?

Perception of respondents towards service delivery of RCA

As far as service delivery is concerned as depicted in table 7, majority of the respondents agreed that the government has not made sincere efforts to create awareness about VAT (67.3%), no constant information about VAT procedures (88.0%), Tax payers' lack of knowledge about rules and regulations (66.2%) and no respectful service for clients (42.1%) as least agreement. As to the overall service delivery, majority 52.9 percent of the respondents showed indifference on the service delivery.

Further, majority 82.4 percent of the respondents agreed that VAT rate is very high. VAT is increasingly being used throughout the world, including many African countries to raise government revenue with less administrative and economic costs. It is believed to be a good means to raise government revenue when relatively poor administered. Keen and Lockwood (2007) also strengthen this idea empirically. They found that in the countries that have adopted VAT, revenue from this source accounted on average 27% of the total tax revenue or 5% of the GDP and about 70% of the world's population now lived in countries with a VAT. This implies that VAT is a key source of most government revenues in the world.

The share of VAT in total tax revenue ranges from 17.4% to 42.4% Keen and Lockwood (2007). This share is higher in Ethiopia compared to other African countries. This is so because, Ethiopia's GDP is lower than other sub Saharan African countries. The VAT to GDP ratio ranges from 2.7% in Egypt to 6.5% in Tunisia with an average 4.6%. Similarly many sub Saharan African countries have also experienced an increase in revenue from VAT. The revenue performance of VAT as measured by the ratio of VAT to GDP in Ethiopia which is 5.7% in much higher than then the African average (4.6%) and stood the fourth among the selected African countries. This implies that VAT in Ethiopia is showing a good revenue performance but this does not mean VAT is collected potentially.

Perception of respondents towards the benefits of VAT

Perusal of table 8 reveals that majority of the tax payers perceived that VAT has benefits in terms of more sales (77.0%), more turnovers (75.7%), revenue to government (73.5%), simplified tax procedure (59.0%), relief from additional tax (67.5%), reduction in price (86.8%) and easy to accountability (71.1%). This shows that although tax payers do not have well awareness and knowledge about VAT, they were highly understood about the benefits of VAT. More than 70 percent of the respondents perceived that VAT has helped

them to increase sales, turnover, price reduction, revenue to government and ease of accountability. Nonetheless study by Radhika (2014) found that VAT is highly beneficial as revenue to government.

Challenges of VAT administration

As illustrated in Table 9 above about respondents' views on Challenges of VAT, majority of respondents (83%) agreed that VAT leads to maintain unnecessary documents, increase in operational expenses (75.8%), involves more paper work (77.1%), complicated procedure (64.9%), burden to customers (79.6%), difficult to administration (57.7%) and Poor institutional capacity (68.6%). Nonetheless, a simple majority (45.7%) disagreed that the VAT did not affect the demand for the product. This finding shows that most of the respondents strongly agreed on the challenges of VAT except decrease in demand. Thus it may be concluded that the institutional capacity of Yirgalem Town RCA branch office is found to be weak and needs due attention in order to establish strong office in collecting the VAT sustainably by convincing VAT registered business community of in the town.

Conclusion

Value Added Tax has also become an indispensable component of tax reform in developing countries. It is the most important tax innovation of the second half of the twentieth century. In line with this perception, an increasing number of developing countries have converted their sales tax to Value Added Tax (VAT). On the basis of findings it may be concluded that most of the tax payers have poor awareness and knowledge about VAT and its different dimensions in Yirgalem Town irrespective of their level of literacy. Although RCA office played crucial role in awareness creation, there is a gap of communication between the clients and RCA officers because the officers believe that the tax payers can get enough information from each other and the medias at large but since the media is not only targeting the study area. No doubt, VAT has its own impact on investment and export according to the study finding. Tax payers do have right perception towards the benefits of VAT. However, majority of the respondents felt that VAT offers many challenges especially increase in operational costs, unnecessary documents maintenance, complicated procedure, etc. Besides, the main areas where there are gaps and problems include registration, record keeping, and issuing VAT receipts.

Recommendation

Based on the findings and conclusion, certain recommendations have been forwarded to overcome the challenges of VAT administration.

- As part of awareness creation, the RCA office need to use community radios with local languages to reach the vicinity clients with adequate information. Short term training programs may be organized by considering the consumers and business people as target participants on VAT Law, Rules, Regulations and Implementation.

- Periodical supervision and inspection need to be undertaken by checking the transactions of the business enterprises.
- As the findings show that even if the numbers of VAT registered business owners were few in relation to the total business owners in the Town, the progress of tax income increases in alarming rate. Hence, budget for promotional and training should be allocated in order to enhance client's perception.
- Institutional capacity of the RCA branch office needs to be strengthened by deploying skilled and experienced human resource to make VAT implementation more effective.
- Tax payers need to be insisted by the concerned body to issue VAT receipt whenever customers makes purchase of goods.
- Absence of well furnished information technology endangers the smooth implementation VAT procedures. Thus, Government need to pave special attention in making the office fully furnished with information technology.

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