

**TAXATION AND INFORMAL SECTOR:
A CASE STUDY OF BOLGATANGA MUNICIPALITY**

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DEDICATION

I dedicate this work to the memory of my late parents, Mad. Mary Obenewah and J. K. Dede.

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ACKNOWLEDGEMENT

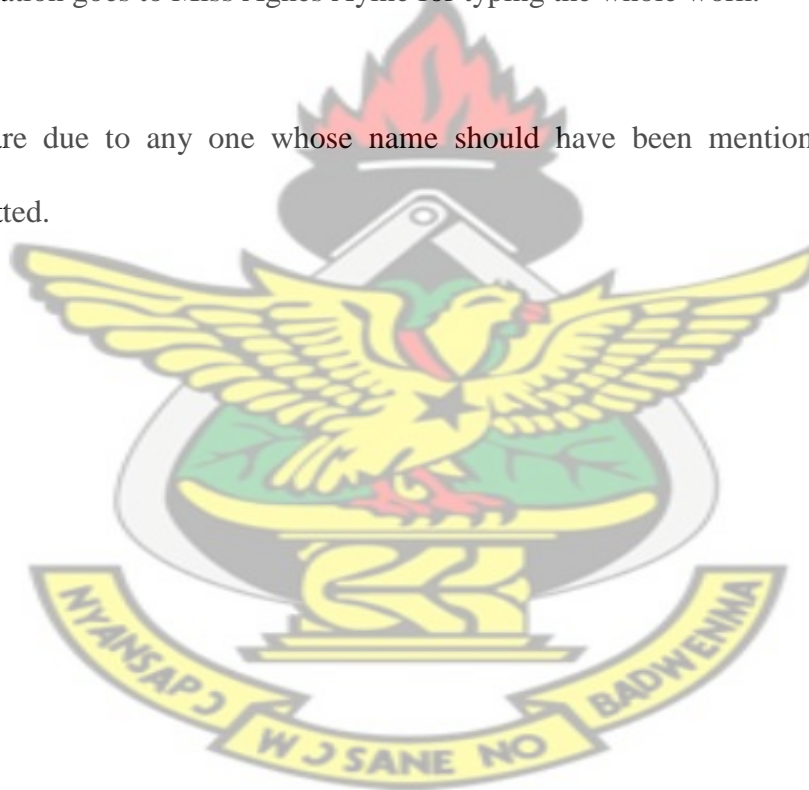
First and foremost, I would like to thank the Almighty God for giving me the knowledge and strength to come out with this work.

Secondly, my deepest appreciation goes to Mr. Gabriel Ahinful, my supervisor, for his tolerance, understanding, constructive criticisms and useful suggestions which helped me in no small way in coming out with this work.

To my wife and children I say thank you for your prayers, support and encouragement.

Also my appreciation goes to Miss Agnes Ayine for typing the whole work.

My apologies are due to any one whose name should have been mentioned but has been unwittingly omitted.



ABSTRACT

Many developing countries including Ghana are faced with the problem of raising the necessary revenues to meet governments' expenditures. Governments' budgeted revenues usually fall short of the expected expenditures. Owing to the lack of liquidity on the international market due to the current financial crisis domestic revenue mobilization is seen as the most reliable source of revenue mobilization. Taxation is therefore seen as the most efficient and effective means of raising revenue domestically for the government. One major sector of developing countries that should have contributed greatly to domestic revenue mobilization through taxation is the informal sector given its employment size and contribution to GNP of low-income countries. But the tax inflow from the informal sector relative to its sheer size is just a drop in the national coffers. Over the past years almost every aspect of dealing with the informal sector has been a problem which has defied all measures aimed at improving the relative share of taxes of the sector. In this regard, the study sought to find out why non compliance with income tax is high in the informal sector and besides, explore further the challenges in taxing the informal sector in Bolgatanga Municipality. In order to achieve the objectives of the study, a sample size of seventy-five (75), comprising seventy (70) tax payers and five tax officials in the Bolgatanga Municipality responded to the administered questionnaire. At the end of the study, it was established that factors such as application of sanctions, regular tax education, anticipation of benefits, high tax rates, among others affect compliance level of the tax payers while capacity constraints, large size of the informal sector, large size of the tax district, improper books of accounts were some of the challenges facing the tax district in the Bolgatanga Municipality. Measures such as intensive and regular monitoring; capacity building; logistical support; regular tax education and advertisement; effective customer relations among others were recommended

as means of raising compliance level of tax payers as well as reducing the challenges in taxing the informal sector in the tax district.

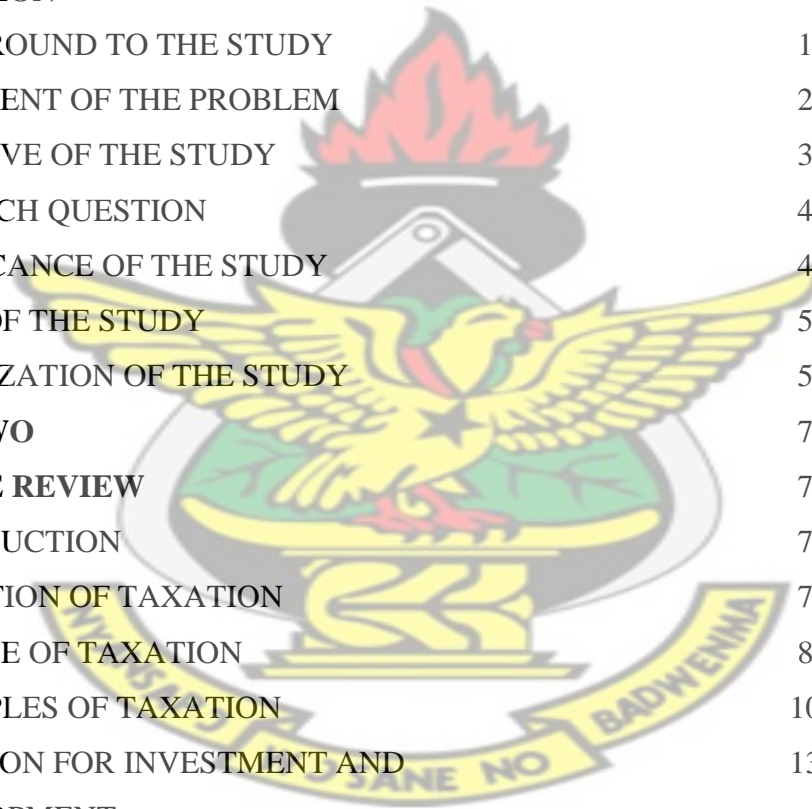
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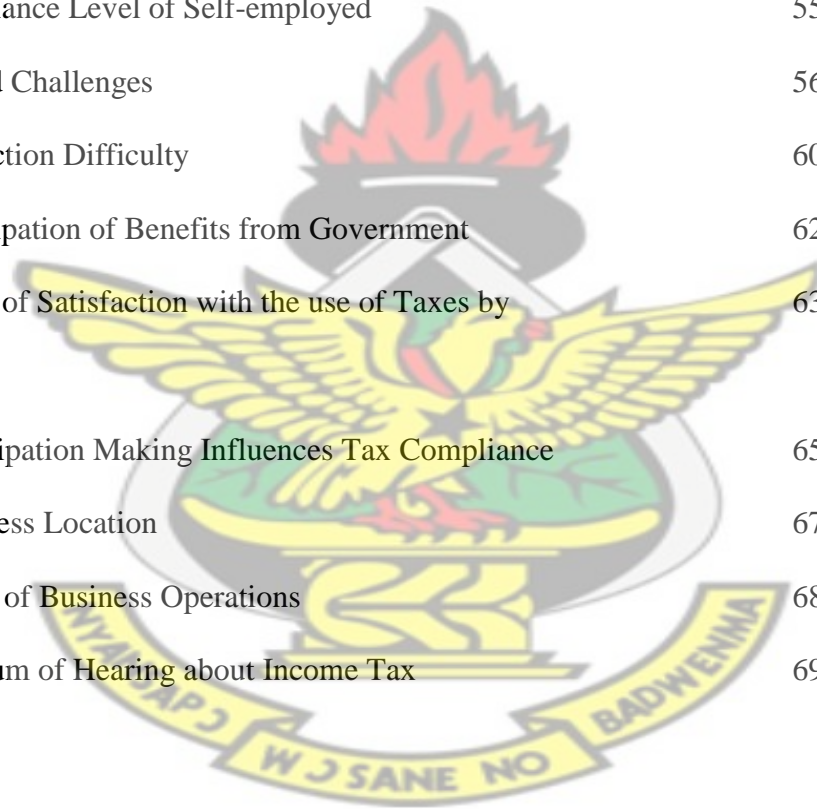
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Figure 1: Respondents Distribution
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CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND TO THE STUDY

Many developing countries including Ghana are faced with the problem of raising the necessary revenues to meet governments' expenditures. Governments' budgeted revenues usually fall short of the expected expenditures. This was acknowledged by the 2007 budget statement of Ghana when the Minister of Finance mentioned that "given the revenues and expenditures outlined above, the 2007 budget is expected to result in an overall budget deficit equivalent to 3.2% of GDP" (Budget of Ghana, 2007). Over the past two decades, the government of Ghana has consistently spent more than it is able to generate as revenue and the gap is often financed with foreign aid which has perpetuated the country's aid dependency (Osei and Quartey, 2005).

The current financial crisis has created financial difficulties for many developing countries that depend mainly on external source for public finance, given the lack of liquidity on the international market, putting into question the robustness of their development (Drine, 2009).

To avoid excessive foreign financing which may in the long run lead to problem of debt sustainability, developing countries need to rely substantially on domestic revenue mobilization (Gupta, 2007). To strengthen domestic resource mobilization developing countries have to rely on taxation and seek to raise additional revenue by expanding the tax base and strengthening revenue administration. Taxation is the most efficient and effective means of raising revenue for the government (Gberegbe, 2007).

The Ghanaian economy is divided into formal and informal sectors. While the formal sector employs about 14% of the labour force, the informal sector (including agricultural sector) is the source of livelihood for the remaining 86% of the working population (GTUC, 2004). According to World Bank estimates, the informal sector accounts for 40% of GNP of low-income countries (Farrell, 2004 cited by Yadav, 2009). Despite the significant contribution of the informal sector to the economies of developing countries, they are the least taxed. According to the Commissioner of Internal Revenue Service (IRS), Major (Rtd) Daniel Ablorh – Quarcoo records at the Registrar General Department of Ghana show that there are 226,760 self-employed registered in the informal sector, but only 53,352 are registered with IRS and are being assessed to tax (GNA, 2009).

Despite the low tax revenue from the informal sector the Government is still determined to expand the tax base to the informal sector to ensure fairness and equity as Baah Wiredu, the former Minister for Finance and Economic Planning, put it “the burden of tax must be shared by all no matter how little one’s contribution is” (GNA, 2006).

1.2 STATEMENT OF THE PROBLEM

One of the major challenges facing the governments of developing countries is how to tax the informal sector. This assertion was recognized by Joshi and Aye (2009), when they did state that “how to tax the informal sector remains a pressing question”. Over the past years almost every aspect of dealing with the informal sector (self-employed) has been a problem which has defied all measures aimed at improving the relative share of taxes of the informal sector (Adom, 2000). The tax inflow of the informal sector relative to its sheer size is just a drop in the national coffers. In spite of the low revenue share of the informal sector, the government is still determined to expand the tax base to the informal sector since ignoring the sector’s activities will lower compliance morale and increase the risk of generalized non compliance (Terkper, 2003). There are many informal sector operators who either intentionally evade tax payment or are not captured by IRS.

The purpose of this study is therefore to find out the causes of tax non compliance behaviour in the informal sector and besides, explore further the challenges in taxing the informal sector in Bolgatanga Municipality.

1.3 OBJECTIVE OF THE STUDY

The study aims at achieving the following:

- (a) To find out why non compliance with income tax is high in the informal sector.
- (b) To identify the challenges that militate against effective revenue mobilization by IRS from the informal sector.
- (c) Making recommendations as to how to incorporate good tax administration principles, procedures and practices in Bolgatanga Municipality IRS.

1.4 RESEARCH QUESTIONS

In order to achieve the set objectives of the study the researcher seeks to find answers to the following questions.

- (a) What factors contribute to the high rate of non compliance among businesses in the informal sector in Bolgatanga?
- (b) What are the challenges that militate against effective revenue mobilization by IRS from the informal sector in Bolgatanga?
- (c) How can IRS improve upon their tax collection in the informal sector by incorporating good tax administration principles, procedures and practices in Bolgatanga Municipality IRS?

1.5 SIGNIFICANCE OF THE STUDY

The study would help policy makers to be able to understand the factors

underlying the individual's decision as to whether to pay taxes or not. Also, it would help the self-employed in the informal sector to know their rights as taxpayers and besides, they would be motivated to appreciate the need to pay taxes regularly and on time.

Again, since the study would unveil some of the problems associated with tax collection in the informal sector in Bolgatanga Municipality and recommend ways of solving them, it would serve as a guide to management for future policies and programmes relating to tax collection in the informal sector.

In addition, it would provide some directions for future research and serve as source of reference for future research into the subject matter.

1.6 SCOPE OF THE STUDY

The study covered businesses in the informal sector such as petty traders, hawkers, hairdressers, dressmakers, artisans and so on in the Bolgatanga Municipality. The decision of the researcher to use the tax district in Bolgatanga Municipality as a case study was based on the fact that the tax district is full of informal sector operators who are purported to be paying taxes to the state.

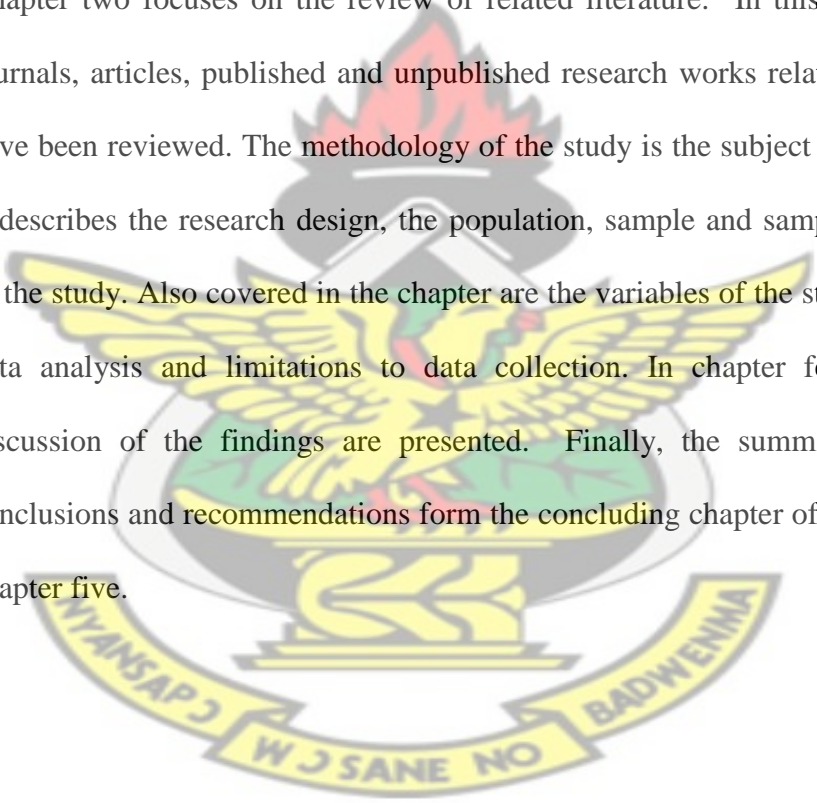
Besides, the tax district lacks the requisite personnel and other resources as compared to other districts of IRS given its area of jurisdiction which covers five District Assemblies in addition to Bolgatanga Municipal Assembly. The selection

of the tax district was also based on the researcher's familiarity with the district.

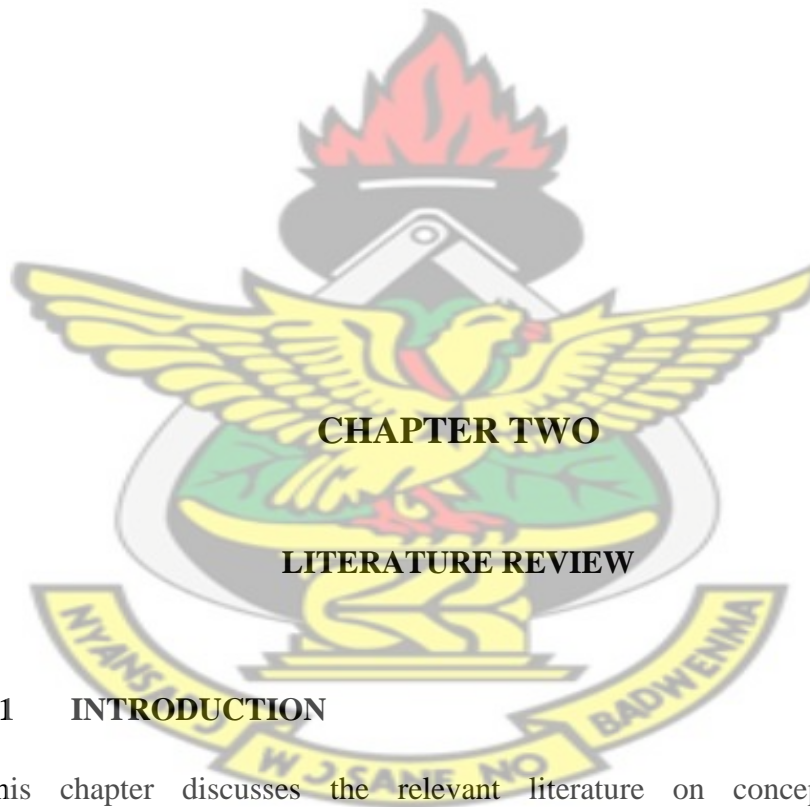
1.7 ORGANISATION OF THE STUDY

The study consists of five chapters. Chapter one deals with the background of the study, the statement of the problem, the objective of the study and research questions. Other aspects of the chapter are significance and scope of the study.

Chapter two focuses on the review of related literature. In this chapter, books, journals, articles, published and unpublished research works relating to the study have been reviewed. The methodology of the study is the subject of chapter three. It describes the research design, the population, sample and sampling procedures of the study. Also covered in the chapter are the variables of the study, methods of data analysis and limitations to data collection. In chapter four, results and discussion of the findings are presented. Finally, the summary of findings, conclusions and recommendations form the concluding chapter of the study that is chapter five.



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CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

This chapter discusses the relevant literature on concepts in taxation, characteristics of informal sector, causes of non compliance behaviour of the informal sector, and challenges in taxing the informal sector.

2.2 DEFINITION OF TAXATION

One of the most flexible ways to raise per capita income and to support increases

in real GDP growth rates is through taxation. Taxation is a sovereign right of the state used to transfer resources from private to public use in order to achieve the economic and political goals of society (Bird, 1992).

According to Bannock et al., (1998) taxation is a compulsory transfer of money (or occasionally of goods and services) from private individuals, institutions or groups to the government.

The US Treasury Department also defined it as a compulsory payment for which no specific benefit is received in return (Slavin, 1999). Tax policy is concerned with the reasoning behind how much revenue the government is collecting, what the revenue is being used for, and whether the government is collecting revenue in the most appropriate way.

Therefore, the above definition by the US Treasury Department is adopted for this study.

2.3 PURPOSE OF TAXATION

The imposition and collection of taxes is simply one of the fundamental policy instruments used to achieve governmental social and economic goals. The objectives of tax policy are similar to those of public policy in developing countries and overlap with the purposes of the tax system or the purpose of most governments.

Edgar and Sandler (2005) revealed that there are five purposes for collecting revenue through taxes: to give government power to allocate resources; to enable

government to provide/support social development; to stabilize the economy; to constitute and define the market place; and to encourage optimal economic growth. Furthermore, three of these are of greatest urgency in developing countries: economic growth; internal and external stability; and ensuring that incomes are distributed appropriately.

2.3.1 ECONOMIC GROWTH

Most developing countries are extremely focused on economic growth in both the private and public sectors. Even in primarily market based economies, governments need to acquire assets for public sector capital formation and development related expenditures (Bird, 1992). There appears to be no limit to the tax gadgetry used in different countries to stimulate economic growth.

Most developing countries encourage foreign direct investment to stimulate economic growth through the use of tax incentives and many developing countries impose higher taxes on retained profits than on distributed profit in order to encourage distribution.

However, the effectiveness of some of the policies especially of incentives remains uncertain because there is still insufficient data to link such policies with growth performance (Shihata, 1991).

2.3.2 STABILIZATION

The use of tax instrument to enhance economic stability is important in developing countries because this enable them to ensure elasticity with respect to changes in the value of money and income levels. If tax yields rise when national income rises, governments have less need to rely on deficit financing to maintain and expand the level of public – sector activity in a growing economy (Bird, 1992).

2.3.3 DISTRIBUTION OF INCOME

The distributional role of taxes in developing countries is another important purpose of tax system. Disparities in income can block development and increase demands for government social spending. The main redistributive tax in most tax systems is personal income tax (Zee, 2005). In practice, the personal income tax in developing countries is far from being progressive due to large disparities in incomes. These disparities are compounded by the influence of the rich, who may end up paying fewer taxes due to numerous exemptions or favours from the government (ibid).

2.4 PRINCIPLES OF TAXATION

A good tax system should possess some principles or qualities. In his book, the Wealth of Nations Adam Smith stated four principles which he called “the canons of taxation” (Hardwick et al., 1994). These include:

2.4.1 EQUITY PRINCIPLE

This principle has been subjected to two interpretations by Modern Economists – the benefit principle and ability-to-pay principle. The benefit principle is based on

the idea that people should be taxed in proportion to benefit they receive from the government (goods and services provided by that tax) (Strafford and LoCascio, 1995). Thus, the amount of tax paid by an individual should be directly related to the benefits, which that individual derives from government expenditure.

The ability-to- pay principle on the other hand, is based on the idea that people who are better able to pay taxes should pay a larger proportion of their income or wealth than people who are less able to pay (Strafford and LoCascio, 1995). This means that taxes should be imposed on people according to what they can afford to pay. Thus, the amount of tax paid should correlate the income available to the taxpayer. In modern day taxation progressive taxation supports this principle.

2.4.2 CERTAINTY PRINCIPLE

This principle means that the payment of taxes should be clear and certain to the taxpayer and the tax collector. Thus, both the taxpayer and the tax collecting agency should be certain about how much, when and where to pay the tax. In this direction, tax laws must be made available to the citizens so that they will know their rights and obligations with regard to tax.

2.4.3 CONVENIENCE PRINCIPLE

This principle means that the method, manner, and time of payment should be convenient to the tax payer. For instance the location of the tax offices must be at

the convenience of the tax payer as well as the forms to be completed must be simple for the tax payer. Thus, taxes should be enforced in a manner that facilitates voluntary compliance to the maximum extent possible

(www.BusinessDictionary.com,2011)

2.4.4 THE PRINCIPLE OF ECONOMY

This principle means that the cost of collection in relation to the tax yield should be minimal. The cost of collecting taxes falls on two parties: the government, which takes on administration costs and the taxpayer who bears the cost of compliance (Wilkinson, 1992). The administration cost includes principally the cost of running the tax authority; the largest being the salaries of all the employees. Compliance costs, on the other hand, include time spent on tax affairs, keeping records, filling in forms, money spent on professional advisers among others by the taxpayer.

2.4.5 OTHER PRINCIPLES OF TAXATION

Nevertheless, www.BusinessDictionary.com (2011) has given additional principles to guide a government in designing and implementing an equitable taxation regime.

These include:-

- Adequacy: taxes should be just-enough to generate revenue required for provision of essential public services.
- Broad Basing: taxes should be spread over as wide as possible section of the

population, or sectors of economy, to minimize the individual tax burden.

- **Compatibility:** taxes should be coordinated to ensure tax neutrality and overall objectives of good governance.
- **Earmarking:** tax revenue from a specific source should be dedicated to a specific purpose only when there is a direct cost-and-benefit link between the tax source and the expenditure, such as use of motor fuel tax for road maintenance.
- **Neutrality:** taxes should not favour any one group or sector over another, and should not be designed to interfere-with or influence individual decisions-making.
- **Restricted exemptions:** tax exemptions must only be for specific purposes (such as to encourage investment) and for a limited period.
- **Simplicity:** tax assessment and determination should be easy to understand by an average taxpayer.

Livingstone et al., (1987) indicated that generally a good tax system may be judged by the following criteria:-

- i. Its effect on the supply and allocation of resources.
- ii. Its effect on the distribution of income and employment.
- iii. Its effect on the stability and growth of aggregate income and employment.
- iv. Administrative efficiency and convenience to the taxpayer.

Unfortunately, a tax which is good in one direction is often poor in another, so that

in practice tax system tend to be a compromise between these economic and social objectives, and incorporate a combination of various forms of taxation (ibid, 1987).

2.5 TAXATION FOR INVESTMENT AND DEVELOPMENT

Taxation is an integral part of countries' development policies, interwoven with numerous other areas, from good governance and formalizing the economy, to spurring growth through, for example, promoting small and medium sized enterprises (SMEs) and stimulating export activities. Among other things, taxation:

- Provides governments with the funding required to build the infrastructure on which economic development and growth are based;
- Creates an environment in which business is conducted and wealth is created;
- Shapes the way government activities are undertaken; and
- Plays a central role in domestic resource mobilization.

Taxation provides a predictable and stable flow of revenue to finance development objectives. In fact, the 2002 Monterrey Consensus recognized taxation's key role in domestic resource mobilization, an acknowledgement sentiment echoed at the 2008 United Nations Doha conference on *Financing for Development*.

While this overview note considers issues of social development in Africa, it also focuses on the tax policy challenges with regards to promoting a business and investment friendly climate on the continent.

It therefore considers the following issues to be addressed to make tax work in favour of investment and development:

- Domestic resource mobilization and broadening the tax base;
- Tax evasion;
- Investment climate and enterprise development; and
- Good Governance.

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Finally, this note will highlight how the Organization for Economic Co-operation and Development (OECD) can support African countries in tackling these challenges.

2.5.1 CURRENT CHALLENGES FOR TAX POLICY IN AFRICA

The African context

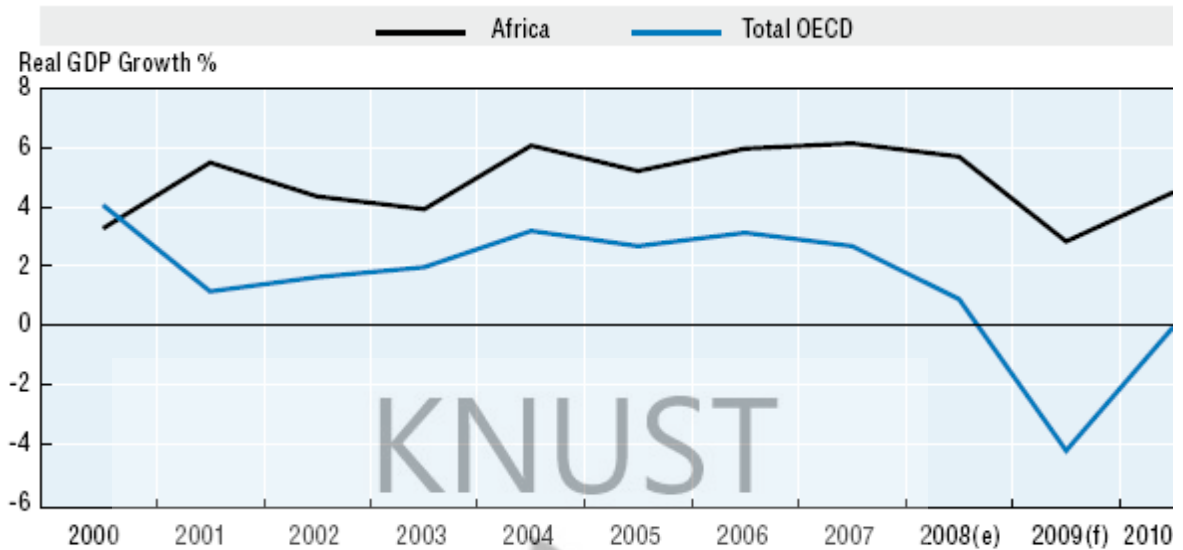
African countries are facing a series of challenges when it comes to optimizing taxation while aiming to reach development targets. Perhaps the most inherently difficult challenge is how to find the optimal balance between a tax regime that is business and investment friendly, while at the same time leveraging enough revenue for public service delivery (which, in turn, makes economies more attractive to investors).

After a period of flat growth between the early 1990s and early 2000s, total government revenue as a share of GDP has steadily increased in most African countries. Domestic revenue — defined as tax and non-tax public revenues

excluding grants — increased by almost four percentage points of GDP between 2002 and 2007, reaching an average of over 25% in 2007 for the whole of sub-Saharan Africa. Excluding Nigeria and South Africa, government revenue as a share of GDP rose even more in the continent, increasing from an average of 18.8% for 1997-2002 to 25.4% in 2007 (OECD, 2008).

However, a significant share of the increase in tax revenue in the region came from natural resource taxes. This included income from production sharing, royalties, and corporate income tax on oil and mining companies. Non-resource related revenue increased by less than 1% of GDP over 25 years (Gupta, 2008). This becomes even more concerning when one considers the impact the crisis has had on the continent, with economic growth in Africa expected to be only 2.8% in 2009, less than half of the 5.7% estimated for 2008 (Figure A), and an important drop of export revenues, as well as a slowdown of investment in oil and mineral production (OECD, 2009). Overall, when compared to the 36% of tax-to-GDP ratio of the OECD countries (2006 un-weighted average) (OECD, 2006), it is evident that African governments suffer from a large revenue gap.

Figure A: Real GDP Growth



Source: OECD Development Centre/World Bank, 2009.

Domestic resource mobilization and broadening the tax base

For tax policy makers, it is essential to strike the right balance between designing an attractive tax regime for investment and growth, and securing the necessary revenues for public spending. Tax policy is central to domestic resource mobilization. When transparently and effectively designed and implemented, it provides an essential financial platform for sustainable development.

As mentioned earlier, the ratio of tax to GDP in poor countries is only about half of what it is in the developed world. Developing countries typically have a narrow tax base, with a relatively small part of the population subject to personal income tax. Tax reform needs to be promoted to widen the tax base and bring a larger part of the population into the formal economy.

Also, effective taxation reduces excessive reliance on aid and mineral rents and

offers a path away from unsustainable revenue streams for many African economies. One of the most pressing challenges facing the continent is to embark on a path to free African countries from an over-dependence on external and volatile capital inflows, such as foreign assistance. In order to do so, African governments need to strengthen their capacities to mobilize domestic resources. Because of its sustainability, domestic revenue should be one of the main sources for fiscal space expansion, thereby reducing dependence on donor assistance (OECD, 2009).

Furthermore, many African countries rely on tariffs for an important share of government revenue. While opening up trade is expected to bolster long-term economic growth, countries participating in trade negotiations, such as the Doha Round and the Economic Partnership Agreements (EPAs), are required to cut their tariffs and are thus likely to collect less revenue. Today, in some African countries, up to 30% of non-resource tax revenue (4% of GDP) is raised through tariffs and trade related taxes. Losing this source as a result of trade liberalization is likely to have significant budgetary consequences (www.africa-pay-more-attention-to-tax-imf.html, 2008).

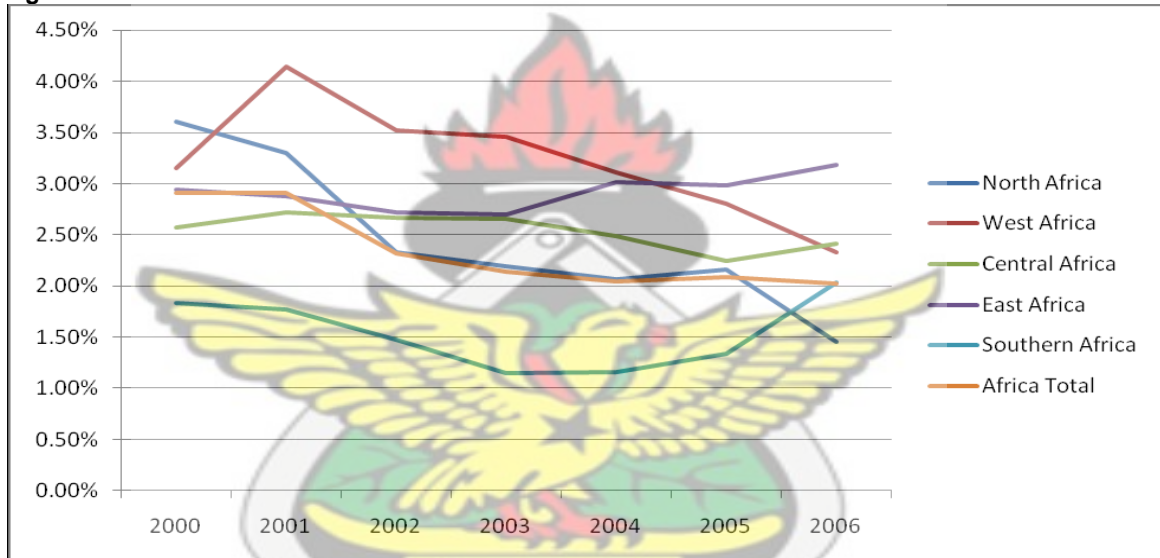
As Figure B below illustrates, recent trends of decreases in revenues from trade taxes could be indicative of such trade liberalization effects. This obviously presents a major challenge to maintaining current revenue bases, let alone increasing them. Alternative revenue sources need to be available before tariffs are

phased out.

This is especially true for Africa in the context of the EPAs with the European Union, as exchanges with the latter traditionally represent roughly two-thirds of African external trade. Cross border trade with neighbouring countries is much less significant, as intra-regional trade only amounts to 10% of Africa's total external trade.

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Figure B: Trade tax in Africa as % of GDP

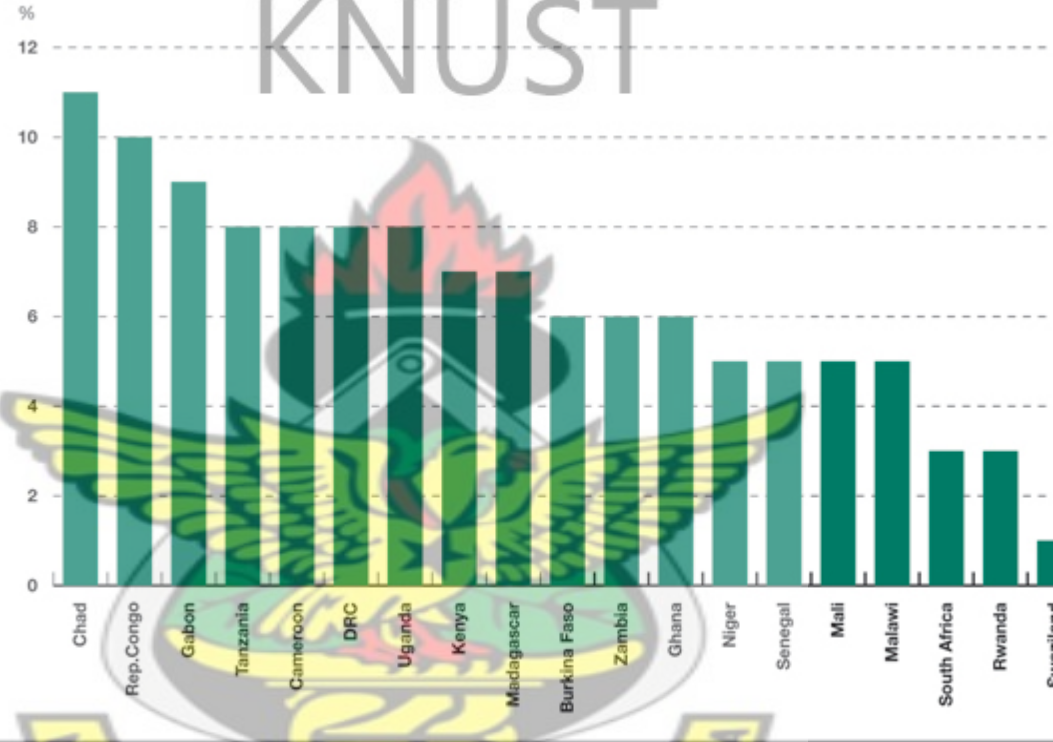


Source: OECD Development Centre

There are avenues for expanding the tax base, which go beyond traditional structural reforms in tax policy. For instance, the growing mobile telephone sector in many African countries presents an opportunity for increasing revenue and broadening the tax base for governments. In fact, a review of 15 countries (Figure C) shows mobile operators contributed more than 8% of government tax revenues in seven of the countries, with Chad providing about 11% (OECD, 2009). The revenue comes from licensing and taxing communication services.

These capital streams can be used to improve basic backbone infrastructure for the ICT industry. The same reasoning applies to other infrastructure sub-sectors as well.

Figure C: Mobile operators' contributions to government tax revenues (in %)



Source: GSM World, 2006, "Taxation and Growth of Mobile Services in Sub-Saharan Africa."

It is clear that expanding the tax base as an avenue for increasing revenue collection, and hence domestic resource mobilization, is a difficult challenge. Issues such as formalizing the economy rely on numerous measures that have to be coordinated and sequenced to ensure that it is actually worthwhile for businesses and individuals to leave the informal sector. Just as important are measures that tackle tax evasion and which can limit capital flight from Africa.

2.6 TAX EVASION AND TAX AVOIDANCE.

Tax evasion may be defined as any action that results in the concealment of all or part of a person's legitimate or illegal economic activities from the tax authorities in order to escape or dodge the payment of tax. It is the willful attempt to circumvent the tax laws through misrepresentation or deceit. In short, it is an intentional and illegal avoidance of paying mandatory taxes to the government (CATA Annual Conference, 2005). Tax evasion takes three forms, namely, non-declaration of income, under-declaration of income and inflation of deductions from income (Aryee, 2007).

In 2008, a US senate subcommittee issued a report highlighting that banks located in tax havens cost US taxpayers some USD 100 billion a year in lost revenue. This leakage occurred despite solid US laws, institutions and other mechanisms to help control tax evasion. If such capital flight is occurring with regulatory frameworks commonly perceived as sound, one can imagine how many more opportunities exist for evasive practices in countries with weak regulatory and legal environments.

Developing countries lose vital revenue through tax evasion and the siphoning of money to tax havens. According to the World Bank, illicit flows of cash from developing countries amount to between USD 500 - 800 billion a year. These are

funds that could otherwise have been used to fund development priorities. Countering the loss of revenue caused by tax havens is a vital element of the G20's and G8's global responses to the current economic crisis. Hundreds of billions of dollars per year have left the African continent between 1991 and 2004. These outflows are estimated at 7.6% of the annual GDP of the region and, in effect, make African countries net creditors of donor countries. They also undermine African countries' tax bases (Pretoria Communiqué).

Tax avoidance, on the other hand, is used to describe tax reductions achieved through artificial but permissible arrangements of personal or business affairs. It refers to the legitimate use of loopholes in the tax laws in order to minimize one's tax burden. In short, tax avoidance is the legal planning to minimize one's tax liability (CATA Annual Conference, 2005). Therefore, there is nothing illegal about it and it is every person's right. Both tax evasion and avoidance result in loss of national revenue and are therefore undesirable to tax administration.

2.7 DEFINITION OF INFORMAL SECTOR

Researchers who are concerned with the informal sector or economy face difficulties in defining it. This is reflected in the variety of names used to identify it – the shadow, hidden, black, underground, gray, clandestine, illegal, unreported, non-cash and parallel economy (Feige, 1990; Thomas, 1992). Several definitions have emerged some of which are as follows:

- (a) All currently unregistered economic activities that contribute to the officially calculated (or observed) Gross National Product (Feige, 1989).

- (b) Market – based production of goods and services, whether legal or illegal, which escapes detection in the official estimates of Gross Domestic Product (Smith, 1994).
- (c) Those economic activities and the income derived from them that circumvent or otherwise escape government regulation, taxation or observation (Schneider, 2005). It is important to note that the informal sector as understood here does not include illegitimate activities such as smuggling, drug dealing or armed robbery; those illegal activities may provide an income to those who engage in them, but add little value to the society and the economy (Fambon, 2006).

The informal sector acquired a proper definition based on production units, both in conceptual and statistical terms only in January, 1993 during the 15th International Conference of Labour Statisticians (ICLS). According to the 15th ICLS informal sector may be broadly characterized as consisting of units engaged in the production of goods or services with the primary objective of generating employment and incomes to the persons concerned. These units typically operate at a low level of organization, with little or no division between labour and capital as factors of production and on a small scale. Labour relations-where they exist-are based mostly on casual employment, kinship or personal and social relations rather than contractual arrangements with formal guarantees (ICLS, 1993). For this study, the researcher adopted Feige’s definition as the working definition.

2.8 CHARACTERISTICS OF THE INFORMAL SECTOR

According to Amin (1989) the informal sector has basically four distinguishing characteristics which have been grouped as follows:-

Enterprise

Characteristics of the activities in the informal sector (Enterprise)

- Unregulated and competitive markets
- Small scale operation with individual or family ownership
- Ease of entry
- Reliance on locally available resources
- Family ownership of enterprise
- Labour intensive and adapted technology
- Absence of access to institutional credits and other similar supports.

Employment

Characteristics of the people engaged in the informal sector (Employment)

- Absence of official protection and recognition
- Non coverage by minimum wage legislation and social security system
- Predominance of own-account and self-employment work
- Absence of trade union organization
- Low income and wages
- Little job security
- No fringe benefits from institutional sources.

Credit

Characteristics of the informal sector credit market (Credit)

- Unregulated and non-stabilized
- Easy accessibility
- Loan availability in very small size and for short terms (periods)
- Low administrative and procedural costs
- Little or no collateral requirements
- Flexible interest rates (from very high to no interest at all)
- Highly flexible transactions and repayments tailored to individual needs

Habitat

Characteristics of the informal sector land and housing (Habitat)

- Unauthorized use of vacant public or private land
- Illegal subdivision and/or rental of land
- Unauthorized construction of structures and buildings
- Reliance on low cost and locally available scrap construction materials
- Absence of restrictive standards and regulations
- Reliance on family labour and artisanal techniques for construction
- Non-availability of mortgage or any other subsidized finance

The characteristics mentioned above are explained as follows:-

2.8.1 CHARACTERISTICS OF ACTIVITIES IN THE INFORMAL SECTOR (ENTERPRISE)

The economic activities taking place in the informal sector exhibit certain unique features. These include:-

2.8.1.1 Small scale operation with individual or family ownership.

The typical informal sector enterprise is individually owned and operated, generally for less than five years duration (Yankson, 1992). Family ownership dominates the ownership of the informal sector businesses because family provides cheap source of labour. Lack of trust on the part of individual does not promote the formation of partnerships and joint ventures. Most often than not, the size of such enterprises are determined by the capital invested and the number of employees. The average number of employees may be four even though this number may vary with the nature of operation- from sole proprietorship to partnerships and family ventures and cooperatives.

2.8.1.2 Ease of entry

Setting a business in the informal sector is very easy since the capital requirement, technology and regulatory requirements are very low and so any body at a point in

time can set up business in the informal sector. Capital intensity in this sector is low- most of the entrepreneurs use labour intensive technology – with the targets units having the most fixed capital per employee (ibid, 1992).

2.8.1.3 Reliance on locally available resources

The informal sector businesses lack the capacity to do off- shore acquisition of resources be it material, financial or human since normally such business are small in size. Hence the informal sector businesses tend to rely more on local resources. These resources are acquired from various sources, some times new, second – hand and or self constructed but rarely imported (Barwa, 1995).

2.8.1.4 Labour intensive and adopted technology

Yankson (1992) postulated that the operators of informal sector businesses mostly lack adequate financial resources to import more advanced technology so the sector heavily relies on labour for its production. The equipments used by the informal sector entrepreneurs are mostly bought locally with subsequent improvements made on those equipments. The level of technology employed in the informal sector in Ghana was low and in poor condition.

2.8.1.5 Unregulated and competitive market

Not even the combine effort of the government and individuals is able to regulate the activities of the informal sector properly. The cost of regulating the informal sector will far exceed the benefits and in fact such an attempt will be a “wild-

goose chase”. More so, the market works on the premise of “survival of the fittest”, due to the presence of many operators in the sector, the informal sectors’ business environment is highly competitive as competitors make all attempts to outdo one another for customers (Farrell et al., 2000).

2.8.2 CHARACTERISTICS OF PEOPLE ENGAGED IN THE INFORMAL SECTOR (EMPLOYMENT)

Persons operating in the informal sector do exhibit certain characteristics which either militate against their progress or favour them. These characteristics are explained below.

2.8.2.1 Little or no job security

Employees in the informal sector can lose their jobs at any time at the will of their employers. Employees cannot take any actions for such unfair dismissals as usually there are no binding contracts. No compensation is usually paid for such dismissals (ibid, 2000).

2.8.2.2 Absence of trade union organizations

The informal sector operators have wide range of activities which makes it extremely difficult for the formation of trade union which is necessary for protecting the interest of individual members. Again, most of informal sector operators presume the formalization of activities of their operators may expose them and eventually attract tax payment hence prefer to operate individually instead of coming together under one umbrella in the name of trade union.

2.8.2.3 Absence of official protection and recognition

The informal sector operators do not enjoy protection from state machinery in the form of legislations against unscrupulous fraudsters who may defraud such entrepreneurs in the course of business dealings. Because the operators in the informal sector do not want to be identified for fear of being taxed avoid being recognized and hence do not enjoy the protection that may be available to them from the state (ibid, 2000).

2.8.2.4 Low income and wages

Entrepreneurs get low return on their investment as a result of keen competition in the sector. The people employed in the informal sector are generally paid low wages due to the existence of excess labour supply and lack of skills that may attract high wages (ibid, 2000).

2.8.2.5 Non coverage by minimum wages legislation and social security

Most employees in the informal sector are often paid below the national minimum wages. The employers also fail to contribute to the social security and pension scheme on behalf of the employees. These employees fail to report their employers for fear of being sacked or out of total ignorance of the law. And as such, these employers escape appropriate sanctions as their illegal activities are hidden from the law enforcement agencies (ibid, 2000).

2.8.2.6 Predominance of self – employment work

Most operators in the informal sector are mostly self employed who either work alone or with the assistance of family members. According to Farrell et al., (2000), there is no gainsaying the fact that operators in the informal sector are self employed operating from their homes most often, with others using any available public space. With a table and a chair one can easily start up own business with family assistance.

2.8.3 CHARACTERISTICS OF THE INFORMAL SECTOR LAND AND HOUSING (HABITAT)

These characteristics have to do with the use of land and housing by the informal sector. These characteristics are considered below.

2.8.3.1 Unauthorized use of vacant public or private land

Informal sector operators usually function from clusters closer to cities, especially those engaged in auto repairs and metal works. Barwa (1995) reiterated that in developing countries kiosks and small containers owned by the informal sector operators litter every conceivable nook and cranny in the cities and towns.

2.8.3.2 Unauthorized construction of structures and building

Informal sector operators tend to put up either kiosk or permanent structures on any piece of land at their disposal either personally owned or rented. Informal

sector operators tend to put up houses on the land from where they operate their businesses. They have no legal title to the land on which they construct such structures. This in some cases has resulted in environmental disaster such as ‘Sodom and Gomorrah’ in Accra (ibid).

2.8.4 CHARACTERISTICS OF THE INFORMAL SECTOR CREDIT

MARKETS (CREDIT)

2.8.4.1 Easy accessibility

Credit is an inevitable practice for success in the informal sector. Some if not most of the informal sector operators thrive on giving credit to their clients.

Usually, informal sector goods are patronized by the low income earners group and credit is an inevitable practice (ibid).

2.8.4.2 Little or no collateral requirement

Mostly it is the low income earners that patronize products in the informal sector hence such individuals lack collateral. Also because credit granted is very small, no collateral is demanded (ibid).

2.8.4.3 Low administrative and procedural cost

Comparatively in the informal sector credit is usually granted to people known to the operators hence no need to assess the individuals being granted credit. This makes administrative or procedural cost of credit low (ibid).

2.9 FACTORS THAT MOTIVATE TAX COMPLIANCE

In the standard economic model of taxpayer behaviour, the perceived quality of government does not influence the level of taxes that are paid. The basic behavioural assumption is that people are free riders: no one will voluntarily contribute to the government unless the threat of punishment makes it sensible (Allingham and Sandmo, 1972). But research has shown that the rate of contribution to a public good is affected by factors such as citizen's trust in others and perceptions of the trustworthiness of the government (Slemrod, 2003).

According to Scholz (1998) without trust there is little basis for social co-operation and voluntary compliance with laws and regulations that could potentially benefit everyone. Thus, without trust coercion provides a reasonable guide for governance. Levi (1998) pointed out that citizens are likely to trust the government only to the extent that they believe that it will act in their interests, that its procedures are fair and reasonable, and that their trust of the state and others is reciprocated. She stresses that government trustworthiness coupled with the perception that others are doing their share, can induce people to become 'contingent consenters' who co-operate even when their short – term interest would make free – riding the individual's best option. Accordingly, citizens' willingness to pay taxes voluntarily rests on the government's capacity to provide services and its demonstrated readiness to secure the compliance of the otherwise non-compliant. From the above analysis it could be seen that the relationship between a taxpayer and the government so far as tax compliance is concerned

involves at least three elements namely:

- (a) Fiscal exchange
- (b) Coercion
- (c) Social Influences

2.9.1 FISCAL EXCHANGE

Compliance can be motivated by the presence of government expenditures. Individuals may pay taxes because they value the goods provided by the government, recognizing that their payments are necessary both to help finance the goods and services and to make others contribute (Alm et al., 1992; Andreoni et al., 1998; Cowell and Gordon, 1988). Hence, a taxpayer may be seen as exchanging purchasing power in the market in return for government services (Levi, 1988). Positive benefits may increase the probability that taxpayers will comply voluntarily without coercion. Without material benefits, willingness to pay becomes less assured. Although most taxpayers can not assess the exact value of what they receive from government in return for taxes paid, they have general impressions and attitudes concerning their own and others' terms of trade with the government (Richupan, 1987). Taxpayers' behaviour is therefore affected by their satisfaction or lack of satisfaction with the terms of trade. If the system is perceived as unjust, tax evasion may be considered as an attempt to adjust the terms of trade with government (Fjeldstad and Semboja, 2001). According to Wintrobe (2001) as long as individuals (and firms) do not believe the government is responsive to their wishes, even if it may be honest, they will attempt to evade

their taxes.

2.9.2 COERCION

According to the classical criminology theorists, crime is an expression of a person's rational decision making process: before committing a crime, a person would weigh the benefits of the crime against the cost of being apprehended. Therefore, if punishments were stringent enough to outweigh the benefits of crime, they would dissuade people from committing the crime in the first place (Gaines and Miller, 2008).

In the same way, the classical tax evasion model assumes that the taxpayer's behaviour is influenced by factors such as the tax rate that determines the benefits of evasion and the probability of detection and penalties for fraud that determine the costs (Allingham and Sandmo, 1972). This implies that, tax evasion like all other crimes, if detection is likely and penalties are severe few people will evade taxes. Therefore to ensure that people pay their taxes voluntarily there should be effective coercion. According to Friedman (2003) we obey the rules when the government does its job and ensure that the systems are in place to force us to comply.

2.9.3 SOCIAL INFLUENCES

Sociologists and social psychologists have long stressed the importance of social interaction in forming tastes and actions (Hessing et al., 1998). It is reasonable to

assume that human behaviour in the area of taxation is influenced by social interactions much in the same way as other forms of behaviour (Snively, 1990). Compliance behaviour and attitudes towards the tax system may therefore be affected by the behaviour of an individual's reference group such as relatives, neighbours, and friends and political associations. Social norms can affect compliance because individuals tend to seek the respect of others (Mc Adams, 1997). One of the most consistent findings in survey research in Western countries about taxpayer attitudes and behaviour is that those who report compliance believe that their peers and friends (and taxpayers in general) comply, whereas those who report cheating believe that others cheat (Yankelovich et al., 1984).

Also, enforcement and the behaviour of others affect taxpayer compliance. Charles Rossotti, a former US Commissioner of IRS, once stated that the slide in audits has raised concern that honesty could suffer as fears of policing declines. If taxpayers begin to believe that others are cheating, the temptations to shave their own tax burdens may become irresistible (Weisman, 2001). Rossotti's comment recognizes that tax enforcement affects social behaviours and that these behaviours can in turn affect taxpayers' compliance decisions. Prior research has shown that individuals who know evading taxpayers are less likely to comply themselves (Vogel 1974, Spicer and Lundstedt, 1976; Grasmick and Scott, 1982; Scott and Grasmick, 1981). Likewise, the probability that a taxpayer will evade increases when the taxpayer suspects that his acquaintances are evading (Westat,

Inc., 1980; Geeroms and Wilmots, 1985). It is against this background that Terkper (2003) pointed out that if informal sector activities are ignored it would lower compliance morale and increase the risk of generalized non-compliance.

Contrary, social relationships may also help to deter non-payment. Individuals can be dissuaded from engaging in evasion out of fear of the social sanctions incurred should their action be discovered and revealed publicly (Grasmick and Green, 1980; Grasmick and Scott, 1982). More so, evidence from behavioural science suggests that the greater the individual participation in decision making process the greater the level of compliance (Lewis et al., 1995; Hessing et al., 1992). This is partly so because participation implies some commitment to the institution and such commitment in turn requires behaviour that is consistent in words and actions. Thus, it is expected that compliance level will be higher when taxpayers feel that they have a voice in the way their taxes will be spent.

Moreover, government trustworthiness tends to legitimize the public sector and therefore impose some social norm to pay taxes. When government is perceived to be trustworthy, citizens are more likely to comply with its demands in general. As long as individuals (and firms) do not trust the government they will be unwilling to pay their taxes (Wintrobe, 2001). Government trust worthiness is linked to citizen's perceptions of the capacity of the government to make credible commitments about the use of their taxes. In the study on citizens views on taxation in local authorities in Tanzania most respondents said that they would be

willing to pay more taxes if public services were improved (Fjeldstad, 2004). Further, Wintrobe (2001) claims that if individuals (and firms) believe that the tax code is fair and is applied fairly, they will be more willing to pay their taxes.

Based on the literature review, one can conclude that indeed fiscal exchange, coercion and social influences motivate people to pay taxes in general and this research is an attempt to establish that the same is true with taxation of the informal sector in Bolgatanga Municipality.

2.10 CHALLENGES IN TAXING THE INFORMAL SECTOR

There has been a growing interest in taxing the informal sector in most developing countries for a number of reasons which include revenue needs; the phenomenal size and growth of informal sector; the impact of tax compliance in the formal sector; state legitimacy; demands from the informal sector and tax-accountability (Aryee, 2007).

As a measure to expand the tax base to the informal sector, the Government of Ghana has introduced several taxes to specifically target the informal sector operators. These include the vehicle Income Tax (VIT) on public transport operators, the Tax Stamp for collecting income tax from small traders and Flat Rate Scheme for expanding the reach of the VAT (Prichard, 2009). This has brought some improvement in the revenue yield but the overall collection from the informal sector has remained small relative to other taxes such as PAYE and Corporate tax. In 2007, out of the total collection of GH¢910.2m by the IRS, self-

employed contributed GH¢45.6m as compared to GH¢372.2m and GH¢418.7m from PAYE and Corporate tax respectively (Revenews, 2008). The self-employed made a record growth in revenue of about 45% against average of 20% over the past four years. This great performance was attributed to effective monitoring of withholding tax which contributed about 35% of the revenue (Revenews, 2009). This means that the direct payments by the taxpayers themselves were nothing to write home about.

Like any developing country, taxing the informal sector in Ghana is a herculean task. This was acknowledged by the 2007 Budget Statement of Ghana when the Minister of Finance and Economic Planning stated that "... one of the major challenges facing Ghana is how to broaden the tax net... the fact that the vast majority of Ghanaians are in the informal private sector makes revenue generation a daunting task" (Budget of Ghana, 2007). To enhance revenue collection and bring a fairer distribution of the tax burden which is currently borne by those employed in the formal sector, the Budget proposes that during 2007 "the government will develop and implement a system to assess and collect income tax using the value of vehicles registered...because a significant percentage of vehicle registrations are from informal sector operators most of whom are not taxpayers" (Budget of Ghana, 2007).

Basically, there are three major reasons why taxation of the informal sector has been almost universally unsuccessful. The first is capacity constraints. Informal sector operators are actively seeking to avoid taxation and even at the best of times

have limited capacity to keep high quality financial records for tax purposes (Prichard, 2009).

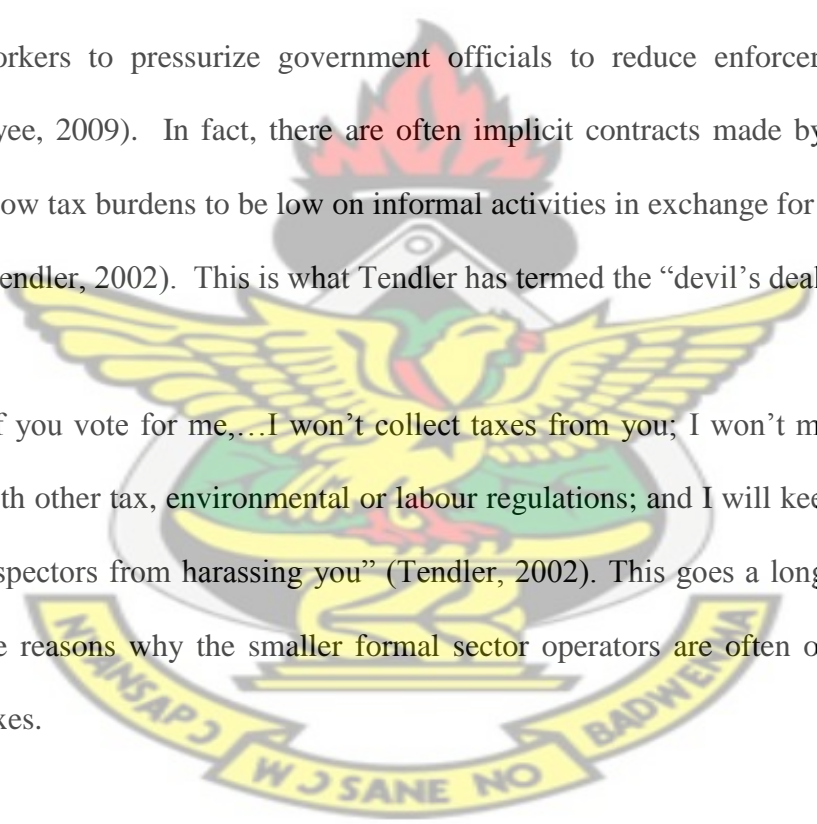
Meanwhile tax administrations of many developing country governments do not have the resources or the personnel capacity to implement, monitor, and enforce tax laws (Stella, 1993; Kiser and Baver, 1994 cited by Joshi and Ayee, 2009). According to Joshi and Ayee, the characteristic of the informal sector exacerbates these problems. The informal economy is characterized by transience and uncertainty. Cash transactions dominate. There is indifference to formal accounting due to high levels of illiteracy and a shortage of affordable accountancy services. In some areas of the informal economy such as transportation or street vending the mobility of the operators makes it difficult to enforce compliance. The large number of people engaged in the sector and the relatively small amounts of tax payable pose an additional logistical problem for collection. Thus, taxation based on formal systems of income calculation, accounts, and payment options are not suited to the informal sector.

The second challenge relates to notions of equity. The vast majority of informal sector operators have very low incomes, and this creates a strong argument for near total exemption from taxation. On the other hand, many informal sector operators have very substantial income and should rightly be asked to pay significant income taxes. In the absence of effective record keeping, the need for equity in the treatment of the low- income group almost certainly makes it more

difficult to target those with higher incomes (Prichard, 2009).

The final challenge is political. Several observers have suggested that taxing the informal sector is politically problematic because the informal sector forms a substantial vote bank for politicians (Cross, 1998 cited by Joshi and Ayee, 2009). State officials and politicians turn a blind eye to activities in the informal sector in order to retain their support base; simultaneously, organised informal sector workers to pressurize government officials to reduce enforcement (Joshi and Ayee, 2009). In fact, there are often implicit contracts made by politicians that allow tax burdens to be low on informal activities in exchange for political support (Tendler, 2002). This is what Tendler has termed the “devil’s deal”.

“If you vote for me,...I won’t collect taxes from you; I won’t make you comply with other tax, environmental or labour regulations; and I will keep the police and inspectors from harassing you” (Tendler, 2002). This goes a long way to explain the reasons why the smaller formal sector operators are often over burden with taxes.



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CHAPTER THREE

METHODOLOGY

3.1 INTRODUCTION

Basically this chapter deals with the research design, the population, sample and sampling techniques, data collection procedure, the procedure for analyzing the data collected and limitations to the data collection .

3.2 RESEARCH DESIGN

The research design includes an outline of what the researcher is writing on including the hypotheses and their operational implications to the final analyses of the data. This research adopted the case study strategy approach. Among the various research designs, case studies are frequently regarded as using both quantitative and qualitative research and a combination of both approaches

(Bryman, 2004). The researcher used both primary and secondary data sources, which were considered to be more appropriate for this study.

3.3 THE POPULATION

The target population of this study was the informal sector as well as the staff of IRS in the tax district of Bolgatanga Municipality. The informal sector operators included hairdressers and beauticians, dressmakers and fashion designers, artisans, food vendors, butchers, contractors and general traders. The total number of businesses in the informal sector registered with the Registrar Generals' Department and had one time or the other filed tax returns in the tax district of Bolgatanga Municipality and the staff strength of IRS at the time of the research, that is, 2010, were six hundred and sixty-nine (669) and twenty seven (27) respectively. Since it was highly impossible to use the whole population, a sample of the above population was used for this study.

3.4 SAMPLE AND SAMPLING TECHNIQUES

Since the taxpayers were scattered all over the tax district and could not be covered in the study, sampling techniques were mainly used to determine the sample size. According to Punch (1998), one cannot study everyone, everywhere, doing everything and so sampling decisions are required not only about which people to interview or which events to observe, but also about settings and processes.

In view of this, randomly selected taxpayers within the Bolgatanga Municipal tax district were used for the study.

A sample size of seventy five (75) respondents was selected for the study. The respondents consisted of seventy (70) taxpayers and five (5) tax officials. The stratified and simple random sampling techniques were used to select the respondents from the informal sector due to the heterogeneous nature of the informal sector.

In the case of the respondents from IRS, purposive sampling technique was used. All the five (5) tax officials were purposively selected from the operations department since they deal directly with taxpayers so far as assessment and collection of taxes are concerned.

The five (5) respondents were made up of three (3) senior and two (2) junior staff members.

A number of both published and unpublished materials on taxpayers and taxation in general from journals and articles as much as possible were used.

3.5 DATA SOURCES

The study made an extensive use of both primary and secondary sources of information from the IRS and the selected taxpayers. The primary sources of data include information that was gathered from the questionnaires that were

administered to the respondents. The advantage of using primary data is that, they are more reliable since they come from the original sources and are collected especially for the purpose of the study. The secondary sources of data included annual reports, brochures and manuals.

3.6 DATA COLLECTION PROCEDURE AND TECHNIQUES

The study was largely based on primary data. Valuable information was collected through questionnaire and direct interview. The questionnaire was structured with open and closed- ended questions.

Most of the questions in the questionnaire were closed–ended questions. The closed ended questions enabled the researcher to obtain the exact information being sought for while the few open – ended questions were used to elicit information on opinions, attitudes and beliefs of the respondents towards taxation in the informal sector. Those who could neither read nor write were assisted to complete the questionnaire. Other information was brought up by the respondents themselves and the researcher took note of them.

3.7 DATA ANALYSIS

The raw data obtained from a study is useless unless it is transformed into information for the purpose of decision making (Emory and Cooper, 1991). The data analysis involves reducing the raw data into a manageable size, developing summaries and applying statistical inferences. Consequently, the following steps

were taken to analyze the data for the study. The data was edited to detect and correct, possible errors and omissions that were likely to occur, to ensure consistency across respondents.

The data was then coded to enable the responses to be grouped into limited number of categories. The Microsoft Excel software was used for this analysis. The data was presented in tabular, graphical and narrative forms. In analyzing the data, descriptive statistical tools such as bar graph, pie charts complemented with mean and mode were used.

3.8 LIMITATIONS TO DATA COLLECTION

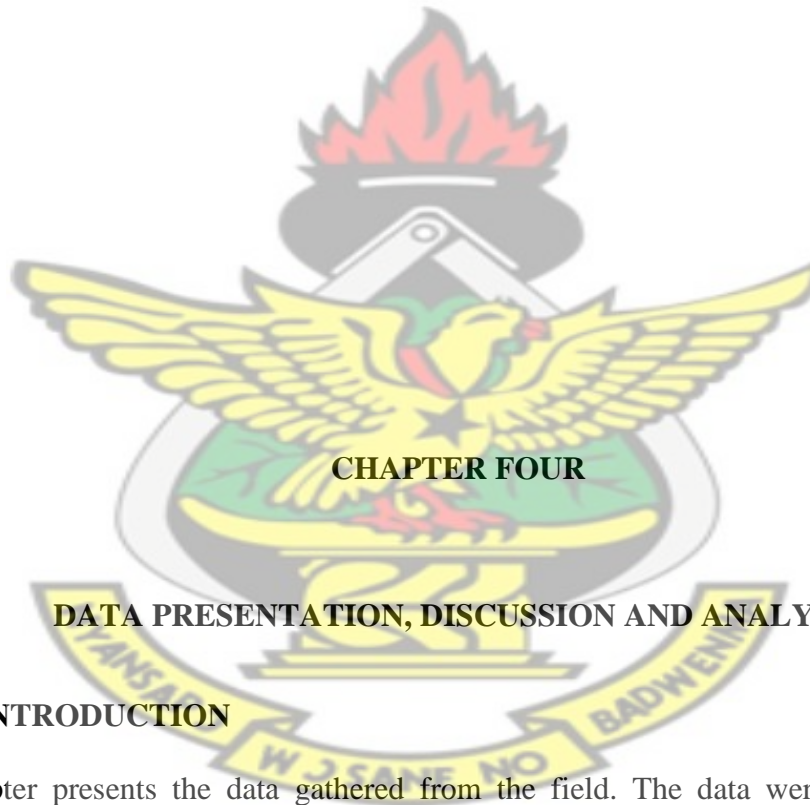
The major limitation of the study was that, due to ignorance and fear of being taxed the respondents were not co-operative initially. However, they were made to understand that the study was just meant for academic purpose and not to collect information for the government for the purpose of increasing their taxes.

Besides, some of the respondents considered the exercise as a waste of time and for that matter were not prepared to spend a few minutes of their precious time to answer the questions. The research was also limited by financial constraints taking cognizance of the extent of the scope of the study and period of investigation.

Another area of limitation to this study came from the inability of respondents to complete and submit questionnaire on time for data to be analyzed. More so, it

must be accepted that the outcome of the study may not be generalized to all self-employed businesses in the country since the outcome of the study might have been influenced by the norms and traditions of the people, economic conditions among others of Bolgatanga Municipality.

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CHAPTER FOUR

DATA PRESENTATION, DISCUSSION AND ANALYSIS

4.1 INTRODUCTION

The chapter presents the data gathered from the field. The data were represented by graphs, charts and tables. Data were also presented in relation to the literature review and compared to the data collected from the field.

4.2 DEMOGRAPHIC CHARACTERISTICS OF RESPONDENTS

4.2.1 Respondents Distribution

Samples were selected based on targeted units using the non-probability sampling method of random sampling, specifically the purposive sampling technique. This method ensured that representative samples of all the known elements of the population were covered in the sample.

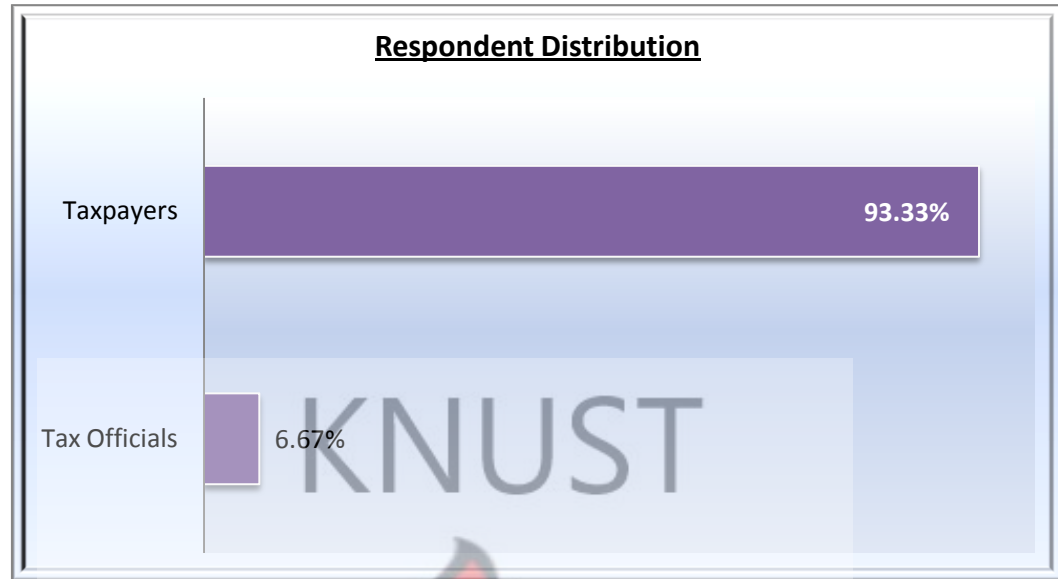
A sample size of seventy-five (75), comprising seventy (70) taxpayers and five (5) tax officials of the target population in the Bolgatanga Municipality responded to the administered questionnaire. The break down in Table 1 shows the distribution of respondents for the study.

Table 1: Respondents Distribution

Respondents Distribution				
	Male	Female	Total	(%)
Tax Officials	4	1	5	6.67%
Taxpayers	30	40	70	93.33%
Total	34	41	75	100.00%
(%)	45.33%	54.67%	100.00%	

Source: Field Survey December, 2010

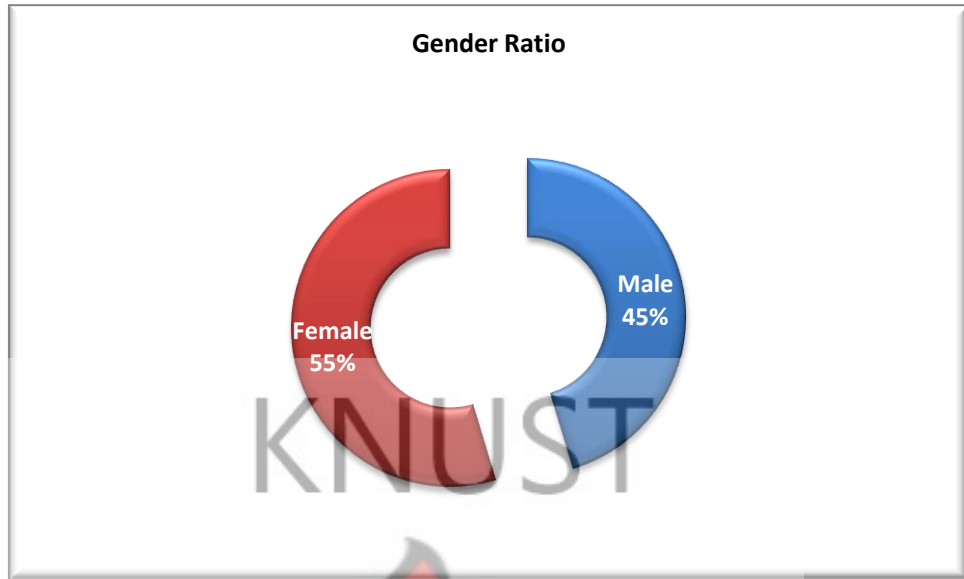
Figure 1: Respondent Distribution



Source: Field Survey December, 2010

As indicated in Table 1 and Figure 1 above, 6.67% of the respondents were tax officials of the Bolgatanga Municipality IRS, while the taxpayers registered the remaining 93.33%. The research further revealed a ratio of 1:1.2 with regard to male and female distribution as illustrated in Figure 2 below. The ratio indicated enough evidence of 55% of slight female dominance, thus, lays credence to the assertion that there is a fair gender balance in the tax industry, with the male population coming up strongly. This emphasizes the point that the informal sector has a much higher female population as compared to the male.

Figure 2: Gender Ratio



Source: Field Survey, December, 2010

4.2.2 The Ages of Respondents

The ages of the respondents were within the range of 16 and 58 years for both staff and taxpayers. The study exhibited the age group 31 – 45 years as the modal class of the respondents with 56% representation (42 in absolute terms); and closely followed by age group 46 – 60 years which attained 41.33% (i.e. 31 respondents); however, tax official representation was bi-modal for 16 – 30 years and 31 – 45 years, with each showing a value of 2 respondents. There were no representations for the age group 60+ years for staff and taxpayers as shown in Table 2 and Figure 3 below.

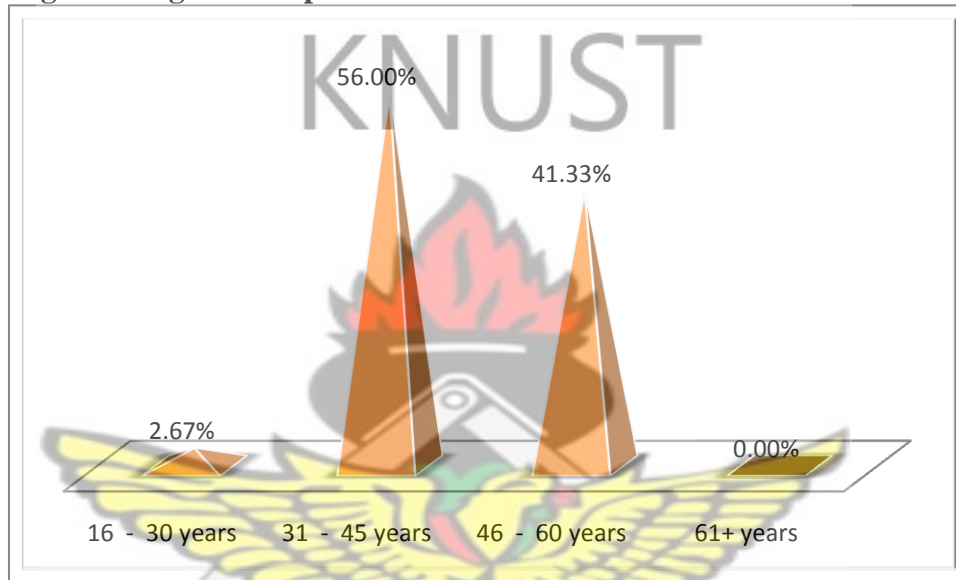
Table 2: Ages of Respondent

Age Group	Frequency			Percentage (%)
	Tax Officials	Taxpayers	Total	
16 - 30 years	2	0	2	2.67%

31 - 45 years	2	40	42	56.00%
46 - 60 years	1	30	31	41.33%
61+ years	0	0	0	0.00%
Total	5	70	75	100.00%

Source: Field Survey December, 2010

Figure 3: Ages of Respondents



Source: Field Survey, December, 2010

In summary, the study illustrated that over 70% strong representations of youthful and energetic respondents with about 30% more belonging to the middle age class.

4.2.3 Number of years with IRS

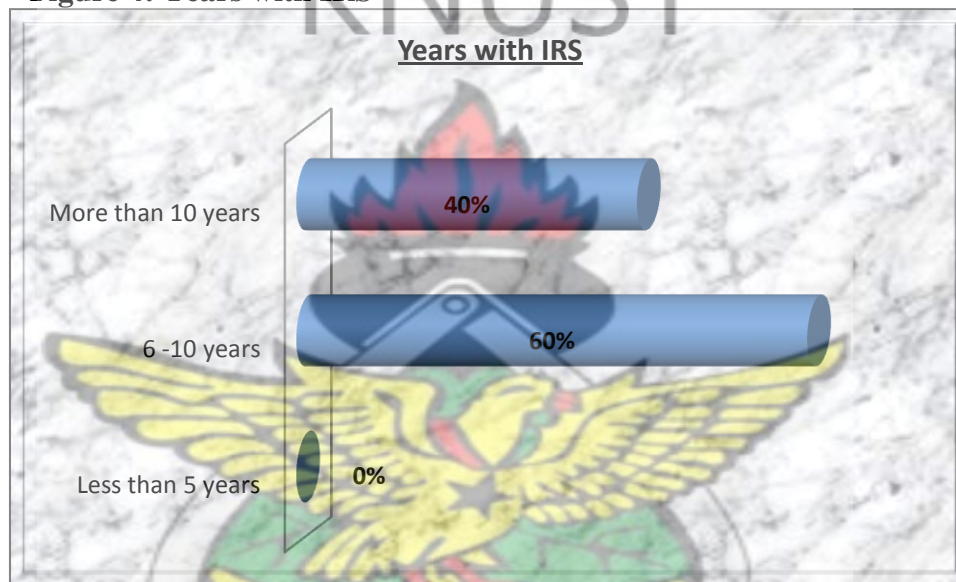
As illustrated in Table 3 and Figure 4 below, 60% of the staff respondents had served the organization (IRS) within a period of 6 and 10 years while 40% had chalked more than ten years of service with IRS. By virtue of the results, it could be easily explained that the Bolgatanga Municipality tax district of the IRS could boast of well experienced and knowledgeable tax officials.

Table 3: Years with IRS

Tax Officials		
Years	Freq.	Percent (%)
Less than 5 years	0	0%
6 -10 years	3	60%
More than 10 years	2	40%
Total	5	100%

Source: Field Survey December, 2010

Figure 4: Years with IRS



Source: Field Survey, December, 2010

4.2.4 Educational Level of Respondents

The research revealed that aggregately, over 33% of the entire respondents had only Basic education, while the university graduates (i.e. both first and second degrees) made up 20%; albeit, this group formed the modal level of education for all tax officials (i.e. 60%). It was again observed that as much as 12% (i.e. 9 persons in absolute terms) has not acquired any form of formal education; and they were basically found within the domain of taxpayers. Professionals on the other hand cumulatively represented 13.33% (and were

only found in taxpayers' domain).

As illustrated in Table 4, the research brought to the fore, over 80% of taxpayers were educated one way or the other; thus, it was assumed that the respondents had a perfect appreciation of the importance of taxation and their respective tax obligations to the state.

Table 4: Level of Education

Level	Tax Officials		Taxpayers		Total	
	Freq.	(%)	Freq.	(%)	Freq.	(%)
Basic	1	20.00	24	34.29	25	33.33
SHS/Commercial	0	0.00	8	11.43	8	10.67
Diploma	0	0.00	7	10.00	7	9.33
First and/or Second Degree	3	60.00	12	17.14	15	20.00
Professional	0	0.00	10	14.29	10	13.33
No formal education	0	0.00	9	12.86	9	12.00
Others ('A' Level)	1	20.00	0	0.00	1	1.33
Total	5	100.00	70	100.00	75	100.00

Source: Field Survey, December, 2010

4.2.5 Types of business

The study classified the respondents into six main types of business in the informal sector within the Bolgatanga Municipality; namely, Hairdressers and Beauticians, Dressmakers and Fashion Designers, Artisans, Contractors, Food Vendors and General Traders . Their representation as per the responses are shown in Table 5 and Figure 5 below.

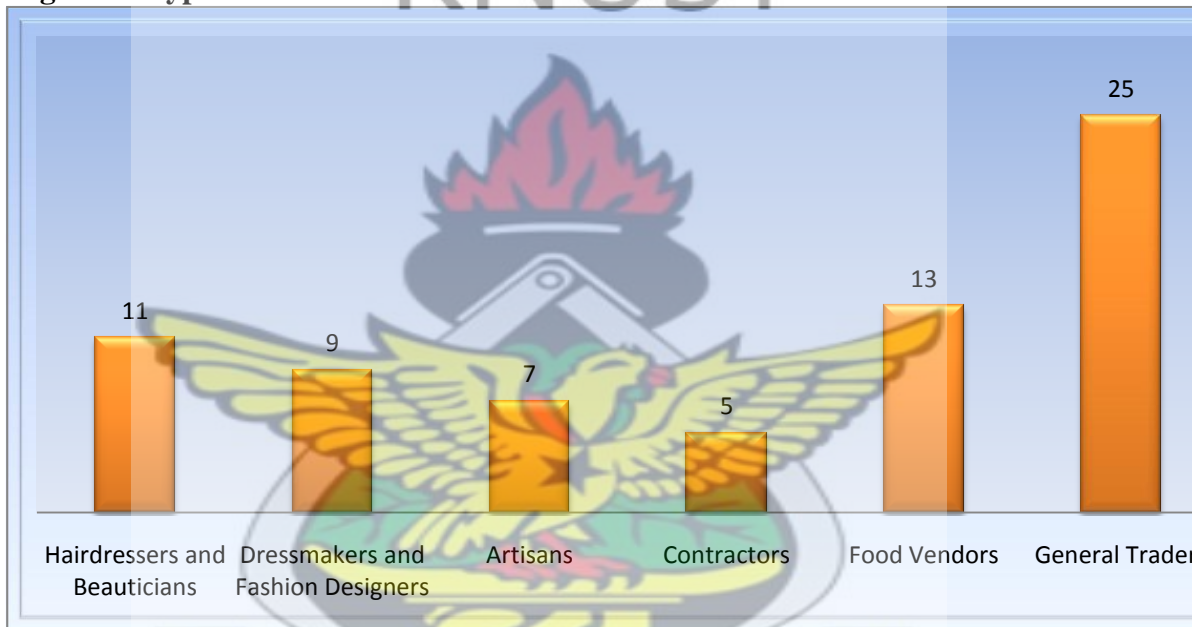
Table 5: Types of Business

Type	Freq.	Percent (%)
Hairdressers and Beauticians	11	15.71%

Dressmakers and Fashion Designers	9	12.86%
Artisans	7	10.00%
Contractors	5	7.14%
Food Vendors	13	18.57%
General Traders	25	35.71%
Total	70	100.00%

Source: Field Survey, December, 2010

Figure 5: Types of Businesses



Source: Field Survey, December, 2010

As indicated in Table 5 and Figure 5 above, General Traders registered 35.71% (i.e. 25 in absolute terms) which apparently represented the modal class of the tax payers; followed by Food Vendors, which chalked 18.57 (13 in absolute terms). The Hairdressers and beauticians class attracted 11 respondents (representing 15.71%); 12.86% (9 persons in absolute terms) was attained by Dressmmakers and fashion designers, while 10% (7persons in absolute terms) was recorded for artisans and the remaining 7.14% (5 respondents) went to contractors.

In view of these findings, IRS could easily target the General traders, most of whom operates on table tops and food venders, many of whom could be located at the permanent locations they ply their trade while other are hawkers who are constantly in mobility. The localised food venders could only be tracked when their wares are still on sale but leaves their premises the moment their produce finishes.

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Apart from the two classes of business mentioned earlier on, ‘Hairdressers and beauticians’ and Dressmakers and ‘Fashion Designers’ are the next class of business dominant in the municipality. The latter, just like the ‘Artisans’ and ‘contractors’ could be targeted by using the Associational strategy.

4.3 RESPONSES FROM TAX OFFICIALS

4.3.1 Factors affecting compliance level

4.3.1.1 Application of sanctions for not honouring tax obligation by tax payers

The study indicated as shown in Table 6 and diagrammatically represented in Figure 6 below that on the issue of applying all the approved sanctions for not honouring tax obligations by tax payers, 40% respondents of the tax officials of IRS responded in the affirmative while as much as 60% dissented.

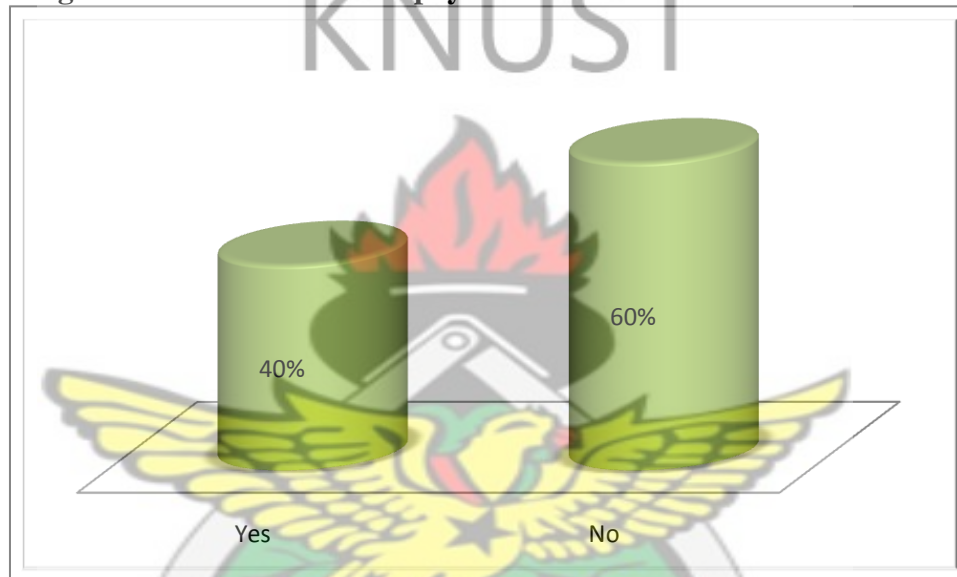
Table 6: Sanctions for non-payment of taxes

	Freq.	Percent (%)

Yes	2	40%
No	3	60%
Total	5	100%

Source: Field Survey, December, 2010

Figure 6: Sanctions for non-payment of taxes



Source: Field Survey, December, 2010

The notable reasons portrayed by the questionnaire for the inertia suffered by officials of IRS to apply the requisite sanctions were lack of the will to apply the sanctions by tax officials and the sanctions involve long and cumbersome procedures.

4.3.1.2 Regular tax education

There was 100% dissent to the issue of IRS in the Bolgatanga Municipality to organize tax education programmes to enlighten tax payers on the need to pay taxes and file returns on time. The reasons for which IRS in the municipality was unable to organize education

programmes were given as ‘capacity constraints’ and ‘lack of resources such as funds and educational materials’.

4.3.1.3 Assessment of existing tax rates

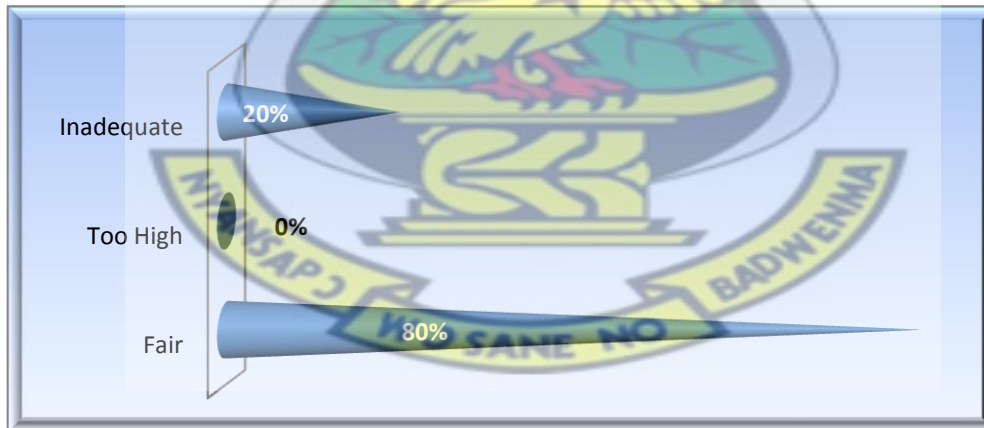
In course of the research it came to light that the respondents believed that the existing tax rates are ‘fair’ by the 80% representation of affirmation, while 20% indicated that they are inadequate and none stood for ‘too high’ as shown in Table 7 and Figure 7 below.

Table 7: Assessment of existing tax rates

	Freq.	Percent. (%)
Fair	4	80%
Too High	0	0%
Inadequate	1	20%
	5	100%

Source: Field Survey, December, 2010

Figure 7: Assessment of existing tax rates



Source: Field Survey, December, 2010

Respondents were of the view that by virtue of the Ghanaian Legal system on taxation which advocates the principle of equity (i.e. benefit principle and ability-to-pay principle), certainty principle (taxes should be clear and certain to the taxpayer and the tax

collector), convenience principle (the method, manner, and time of payment should be convenient to the tax payer) and economy principle (cost of collection in relation to the tax yield should be minimal); the study had only amplified its fairness and further maintained that the rates should not be changed.

4.3.1.4 Compliance level of self-employed

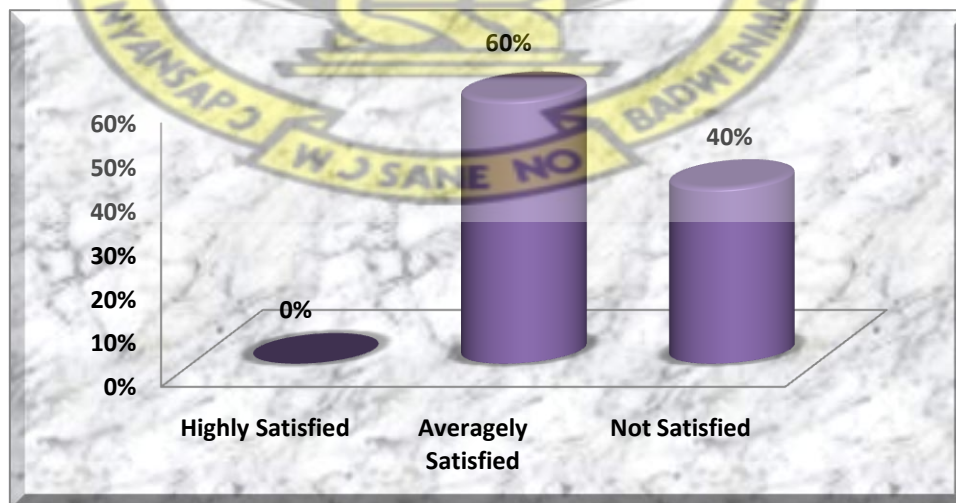
The study revealed that the tax officials are not highly satisfied with the extent of compliance level of self-employed, though, a 60% representation indicated an averagely satisfied staff and 40% not satisfied. Table 8 and Figure 8 below provide the details.

Table 8: Compliance level of self-employed

	Freq.	Percent. (%)
Highly Satisfied	0	0%
Averagely Satisfied	3	60%
Not Satisfied	2	40%
Total	5	100%

Source: Field Survey, December, 2010

Figure 8: Compliance level of self-employed



Source: Field Survey, December, 2010

The study brought to the fore the need to do more work on taxpayers to ensure an increase in their compliance level taking into consideration the statistics of the respondents. If 40% of the staff were not satisfied then it indicates that there are lapses in the tax administration; hence the need to intensify tax awareness programmes and most importantly enforcing the law.

Again, if non of the staff is highly satisfied, an averagely satisfied staff still believes that IRS has not achieve the vision of ensuring that taxpayers level of compliance is highly satisfying.

4.3.2 CHALLENGES IN TAX COLLECTION

4.3.2.1 Challenges faced in the line of duty

It was detected that an overwhelming 100% respondents agreed that there exist challenges starring at IRS in the face. The five major challenges identified, ranked and provided with a value for each coordinate as in First – 5, Second – 4, Third – 3, Fourth – 2 and Fifth – 1. Each of the five tax official respondents’ responses were summed and finally ranked to arrive at Table 9 and Figure 9 below.

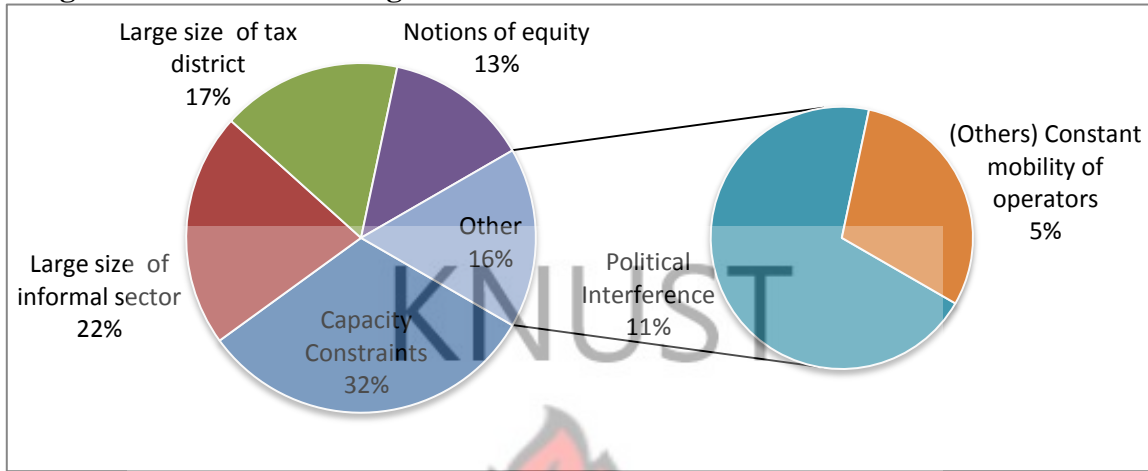
Table 9: Ranked Challenges

Challenge	Marks					Total	Rank
Capacity Constraints	5	5	3	5	1	19	1st
Large size of informal sector	4	4	1	4	0	13	2nd
Large size of tax district	3	3	1	3	0	10	3rd
Notions of equity	2	1	3	2	0	8	4th
Political Interference	1	2	4	0	0	7	5th

(Others) Constant mobility of operators	1	1	1	0	0	3	6th
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Source: Field Survey, December, 2010

Figure 9: Ranked Challenges



Source: Field Survey, December, 2010

As shown in Table 9 and Figure 9 above, tax official considered capacity constraints as the foremost challenge in the collection of taxes in the Bolgatanga Municipality; followed by ‘large size of informal sector’, ‘large size of tax district’, ‘notions of equity’, ‘political interference’ and ‘constant mobility of operators’ in that order as per the ranking.

In view of the fact that the study indicated that ‘Capacity constraints’ was most ranked, with 32% of respondents, the IRS need to take steps to rectify it within the shortest possible time. IRS at the moment is in dire need for effective and efficient tax administration for monitoring and enforcement; but it lacks the requisite capacity to deliver on government set targets. The Human Resource Department and the Training Division of the IRS should develop a comprehensive training programme that would sharpen the technical and managerial competencies of the employees and adopt strategic customer care systems and programmes by ensuring that the right personnel and approaches are used in all its endeavours within the Bolgatanga Municipality involving all

stakeholders.

The study portrayed that 22% of 'large size of informal sector' was the next most challenged factor in the services' operations, followed closely by the 17% 'large size of the tax district'. The IRS could adopt a strategy of segmentation of the district for efficient tax administration. Further prying revealed that IRS has already initiated what they term Associational taxation meant to address some of this problem by using informal sector associations as agents for income tax collection. The associations had intimate knowledge of the activities of their members and could collect taxes without much additional effort. The taxes were collected daily at first, and later weekly to reduce the high costs of printing and monitoring daily receipts, making the payments small and affordable to most members. It is only prudent for IRS to intensify this strategy by encouraging and providing incentives to the associations.

In the area of political interferences, government officials and opposition members alike need to be circumspect with their interferences into the activities of IRS. By virtue of their positions; their interferences may lead to a shortfall in the collection of taxes in the Bolgatanga Municipality.

4.3.2.2 Content with number of tax payers with books of accounts

The research revealed that 100% of the respondents were not content with the number of taxpayers who keep books of accounts; books of accounts help a tax payer in the determination of income for the purpose of tax.

4.3.2.3 Method of tax determinations from tax payers without proper books of accounts or Submit accounts.

The study discovered that the only method used in the assessment of one's tax liability in the absence of books of accounts was Net Worth Method (Living Expenses Method).

4.3.2.4 Tax payers file their returns annually with IRS

It came to light that not all taxpayers file their respective returns with the organization annually. In the same vain tax officials encountered several difficulties with tax payers in the process of filing returns. Notable among them were improper completion of returns; late submission of returns; non submission of returns; tax payers not declaring the right income; and inadequate information from tax payers.

4.3.2.5 Measures to check difficulty of filing returns and non submission of returns

The measures adopted by the tax officials to check the difficulties encountered by the taxpayers in their course of filing returns and non submission of returns as revealed by the research included: assistance from tax officials and auditors in the completion of tax returns; imposition of penalties; and constants education on the need to file returns, the legal implication for failure to file returns as well as the benefits of filing returns.

4.3.2.6 Challenges encountered with tax payers in the payment of taxes

The research revealed an overwhelming affirmation that tax officials encountered on daily basis several challenges in tax collection. Notable among them were tax payers' complains of financial constraints due to poor performance of business and high tax rates.

Other challenges were ignorance of the need to pay taxes; late payment of taxes; high rate of illiteracy and poverty among majority of informal sector operators.

4.3.2.7 Difficulty of tax collection in the informal sector

The research used seven pointers to ascertain the most difficult reasons for tax collections in the Bolgatanga Municipality. The seven points that pose difficulties in tax collections were identified, ranked and provided with a value coordinate as in First – 7, Second – 6, Third – 5, Fourth – 4, Fifth – 3, Sixth – 2, Seven – 1. Each of the five tax official respondents’ responses were summed and finally ranked to arrive at Table 10 and Figure 10 below.

Table 10: Collection Difficulty

Collection Difficulty							
Difficulty	Marks					Total	Rank
Cash Transaction	4	3	3	0	0	10	4 th
Constant mobility of operators	5	5	2	7	0	19	3 rd
Indifference to formal accounting	2	2	5	0	0	9	5 th
Large size of informal sector	7	7	7	6	0	27	1 st
Large size of tax district	6	6	1	7	0	20	2 nd
Political Interference	1	2	4	0	0	7	6 th
Uncertainty	3	1	6	0	0	10	4 th

Source: Field Survey, December, 2010

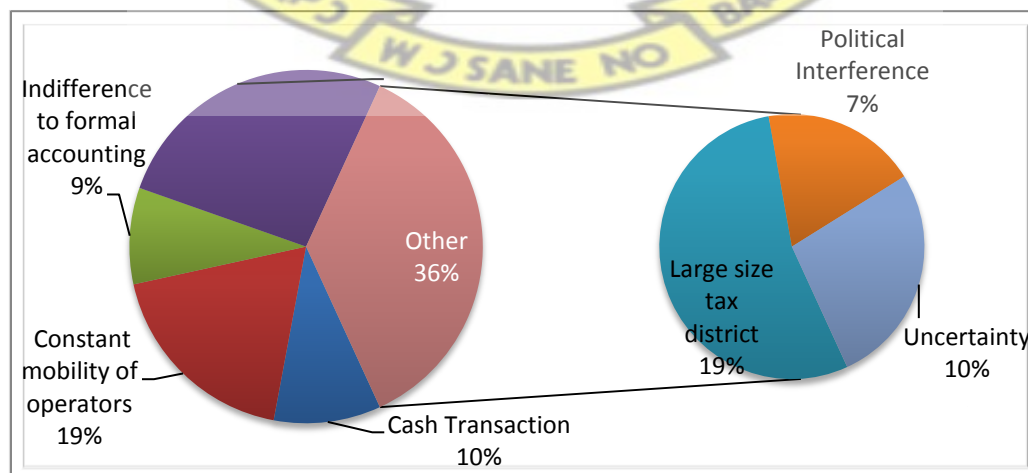


Figure 10: Collection Difficulty

Source: Field Survey, December, 2010

The study showed that the 'large size of the informal sector' and the 'large size of the tax district have been the most difficult tasks to overcome in the collection of taxes in the municipality.

One difficult point that needed consideration was the constant mobility of business operators, thus making it virtually impossible to track them. Issues such as 'cash transactions', 'uncertainty', 'indifference to formal accounts' and 'political interference' all played one role or the other in making it difficult to collect taxes.

The informal sector is noted for not keeping proper books of accounts, thereby causing a lot of difficulty in the assessment of their tax liabilities. Accordingly, in appreciation of the difficulties faced by the informal sector operators in complying with the record keeping requirements of the standards of IRS, easier to operate and more simplified in its record keeping requirements, the agency is currently working feverishly to get the various associations to be trained in the said area. The study exhibited a strong support to Aryee (2007) by reiterating the interference of politicians by stressing that public officials and politicians are willing to turn a blind eye to informal activities in order to retain their support base. The process of bargaining with the informal sector over the payment of tax

is itself a gesture of concession and accommodative, which is fraught with political overtures and undertones.

Again, looking at 'cash transactions as a difficulty in tax collection official of IRS interviewed explained that most business transactions in Ghana and for that matter Bolgatanga are done in cash and even certain reputable organizations are skeptical to accept cheques as mode of payments. The officials further explained that transaction of all businesses in cash is one of the means by which a businessman can conceal taxable income; hence, he is able not only to manipulate his records and turnover figures for tax reduction purposes but he is also able to eliminate all third party information leading to his purchases and sales.

4.4 RESPONSES FROM TAX PAYERS

4.4.1 Factors affecting compliance level

4.4.1.1 Tax Education by IRS

There was an overwhelming response of 98% that IRS does not organize tax education in the Bolgatanga Municipality. Due to the capacity constraints in the area of comprehensive Tax Programme and staff strength of IRS it did not come as a surprise when the respondents emphasized the low outreach programme and enforcement of the law.

4.4.1.2 Anticipation of benefits from government

The research revealed that 79% of tax payers make good their tax obligation with the

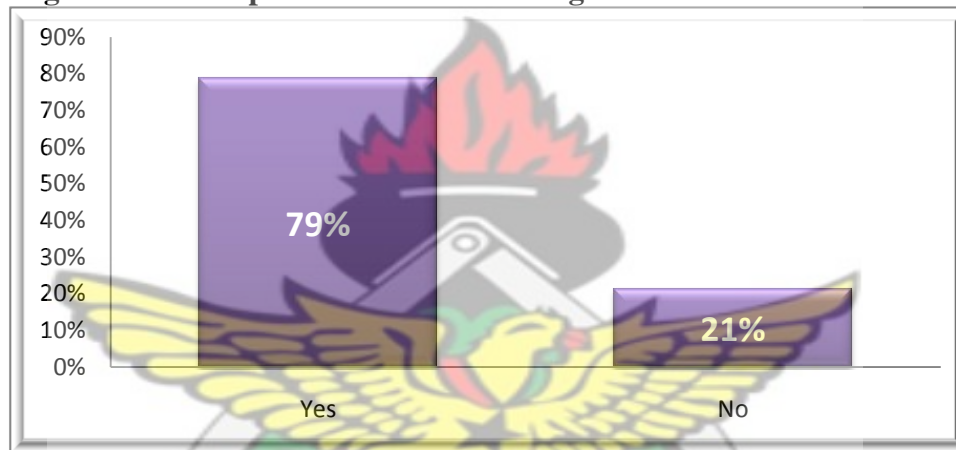
anticipation of benefits (or service) from the government; the remaining 21% expects otherwise. Details are shown in Table 11 and Figure 11 below.

Table 11: Anticipation of benefits from government

	Freq.	Percent (%)
Yes	55	79%
No	15	21%
Total	70	100%

Source: Field Survey, December, 2010

Figure 11: Anticipation of benefits from government



Source: Field Survey, December, 2010

The anticipated benefits of the respondents include provision of infrastructure like roads, schools, hospitals to mention but a few. As good citizens, the respondents expect government to provide goods and services, and their effective provisions enable citizens to pay tax in return for the enjoyment of these goods and services. Also, the respondents believed that paying of tax voluntarily is an act of contributing to government programmes which they support.

4.4.1.3 Level of satisfaction with the use of taxes by government

The research exhibited that 63% of tax payers are 'averagely satisfied' with the judicious

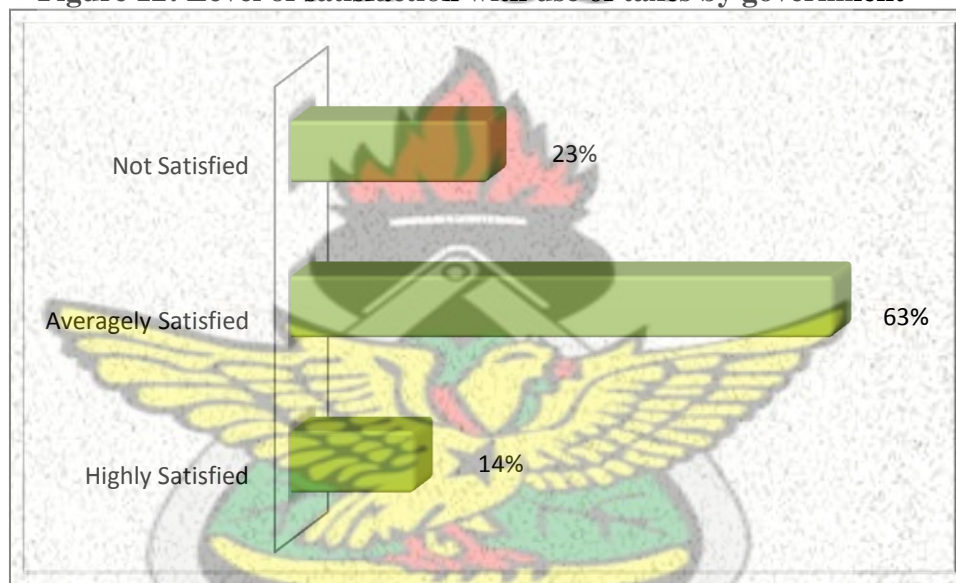
use of taxes paid to government; 14% are 'highly satisfied' and 23% are 'not satisfied' as illustrated in Table 12 and Figure 12 below.

Table 12: Level of satisfaction with use of taxes by government

Level	Freq.	Percent (%)
Highly Satisfied	10	14%
Averagely Satisfied	44	63%
Not Satisfied	16	23%
Total	70	100%

Source: Field Survey, December, 2010

Figure 12: Level of satisfaction with use of taxes by government



Source: Field Survey, December, 2010

The research further exposed that tax payers' assessment of the existing tax rates are 'too high' (i.e.85%) while the remaining 15% had the view that it is 'fair'. It was therefore not surprising that 98% of respondents rooted for a change (i.e. reduction) of the existing rate. Among the reasons provided for the tax rate reduction were 'reduce tax burden so as to encourage voluntary compliance', 'high rates of taxes reduce expected net income' and 'indigenous Ghanaian businesses are already suffering from dumping from China and other stiff competitions from expatriates, and to couple it with high tax rate is simply too

much'. Again, respondents overwhelmingly (99%) affirmed to the fact that severe punitive measures would help stem the tide of tax evasion. Notable among the punitive measures suggested were closure of businesses, seizure of wares of hawkers and more strict terms prosecution.

4.4.1.4 Reasons for tax evasion

The research showed that the four points provided as reasons for tax evasion were very relevant; 41% chose 'too high tax rates', 29% was registered for 'knowing others are not paying', 'unfair application of tax laws' had 16%, and 14% maintained that 'mistrust of government for the use of tax revenue' were strongly affirmed. Also, a respondent provided another reason as, 'the tax net fails to catch all taxable 'insects', while the few complying ones are being pressurized and intimidated'.

Furthermore, 99% of tax payers were of the view that social sanctions can deter people from evading taxes because of public ridicules, and the remaining 1% obviously dissenting.

4.4.1.5 Participation in decision making influences tax compliance

The study indicated by the 81% response that individuals' participation in decision making process in their community serves as a major factor of influencing tax compliance. However, 19% (i.e. 13 in absolute terms) did not share in that view. Table 13 and Figure 13 below illustrate the responses.

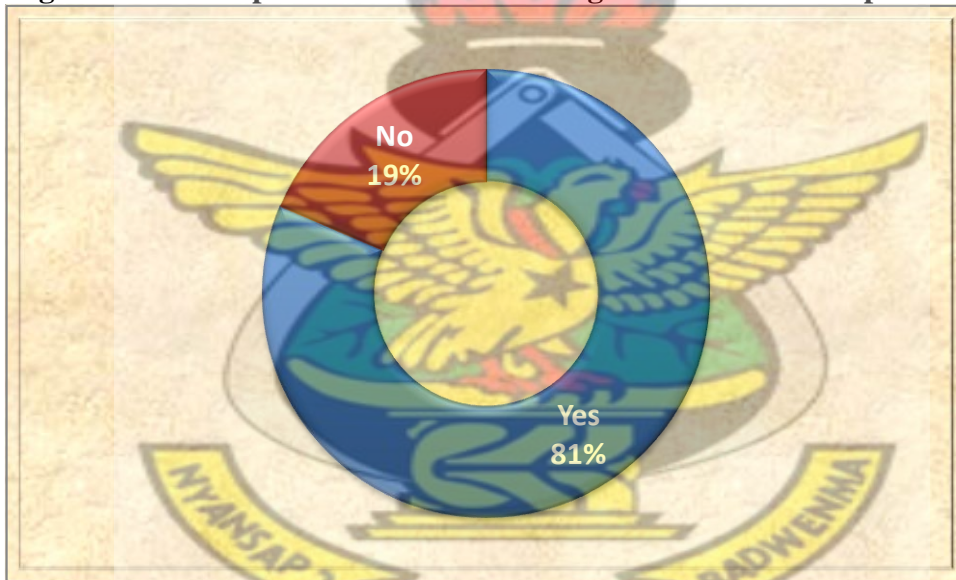
Table 13: Participation in decision making influences tax compliance

	Freq.	Percent (%)
Yes	57	81%
No	13	19%
Total	70	100%

Source: Field, Survey December, 2010

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Figure 13: Participation in decision making influences tax compliance



Source: Field Survey, December, 2010

The respondents that affirmed the notion had reasons among others as ‘commitment to the institution increases’ and ‘proud to be heard and probably implementation of one’s counsel’. The respondent claimed that if they have a voice in the way their taxes are spent they will comply voluntarily. On the other hand, the dissenting voices believed punitive measures should be enforced rather. According to them, if people know that they would

be prosecuted if caught for evading taxes and the punishment involve is severe then they would comply voluntarily.

4.4.2 Challenges in tax collection

4.4.2.1 Business Location

The research revealed that the tax payers from the informal sector operated their businesses from six different locations, as in, store, market stalls, table top, hawking, kiosk and/or container. Majority (40%, 28 in absolute terms) of the respondents were operating from stores, 29% (20 in absolute terms) operated from market stalls, Table Top operators registering 11% (8 in absolute terms) and 20% (14 in absolute terms) from kiosk/containers, albeit, no hawkers are tax payers as shown in Table 14 and Figure 14 below.

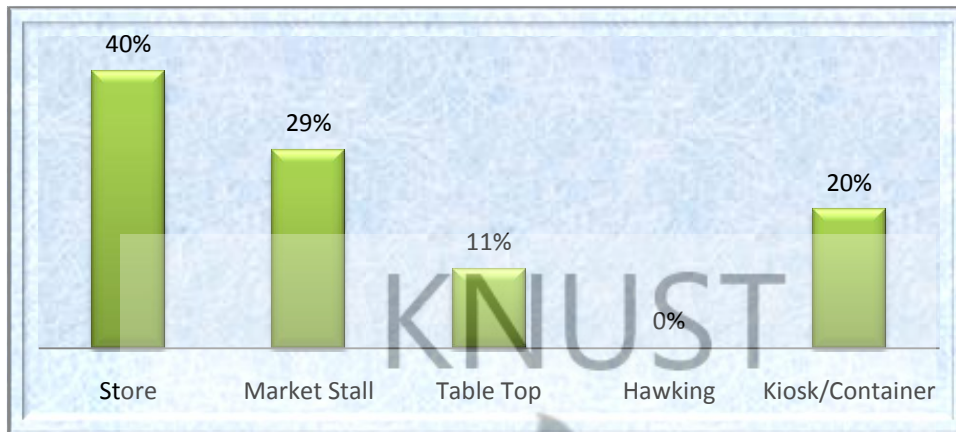
Table 14: Business location

Location	Freq.	Percent (%)
Store	28	40%
Market Stall	20	29%
Table Top	8	11%
Hawking	0	0%
Kiosk/Container	14	20%
Total	70	100%

Source: Field Survey, December, 2010

The reseach findings could be concluded that the hawkers do not pay taxes; and by virtue of the store operators attaining the modal class, it is understandable since all the business types could operate from stores except food vendors who mostly operate from the market stall and table tops. Kiosk/Container operators on the other hand are featuring strongly since that is most dignified location among the poor since the acquisition of stores is quite exhorbitant.

Figure 14: Business Location



Source: Field Survey, December, 2010

4.4.2.2 Years of Business operations

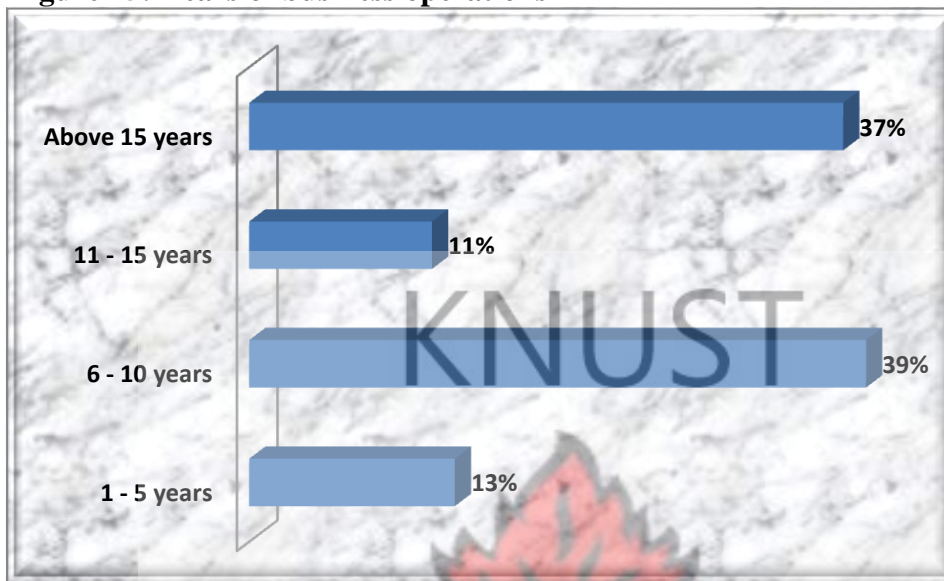
From Table 15 and Figure 15 below, it could be seen that tax payers' years of operating their respective businesses span from one (1) year to eighteen (18) years. The modal class for this distribution was 6 – 10 year, registering 39% (i.e. 27 in absolute terms); closely followed by the Above 15 years class which also chalked 37% (i.e. 26 in absolute terms); and the 1 – 5 years and 11 – 15years classes attaining only 13% and 11% respectively.

Table 15: Years of business operations

Years	Freq.	Percent (%)
1 - 5 years	9	13%
6 - 10 years	27	39%
11 - 15 years	8	11%
Above 15 years	26	37%
Total	70	100%

Source: Field Survey, December, 2010

Figure 15: Years of business operations



Source: Field Survey, December, 2010

The research portrayed that over 80% of respondents have been in operation for over a period of 5 years. This stands to reason that individual business operators have attained a favourable experience curves, taking their excellent competencies and skills into consideration; otherwise they should be out of business by now. The relative high number (34, representing 48%) of business operators who have been in their various businesses for over one decade also reveals that they are people who tax evasion should be made very unattractive, hence the need to be pursued to meet all tax liabilities as they fall due. Again, tax officials need to intensify their education programmes using the associations' strategies.

4.4.2.3 Medium of hearing about income tax

It was detected that tax payers heard about income tax through the 'electronic/print

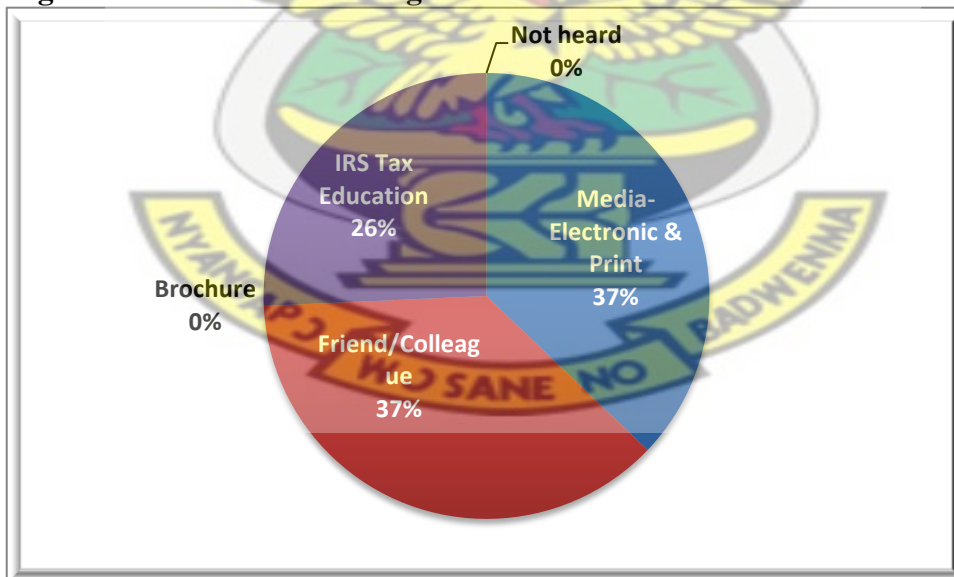
media’, ‘friend/colleague’ and an ‘IRS tax education programme’ with representation of 37%, 37% and 26% respectively; while none of them heard about it either by ‘brochure’ or ‘not heard about it’. Table 16 and Figure 16 below show the details.

Table 16: Medium of hearing about income tax

Medium	Freq.	Percent (%)
Media-Electronic & Print	26	37%
Friend/Colleague	26	37%
Brochure	0	0%
IRS Tax Education	18	26%
Not heard	0	0%
Total	70	100%

Source: Field Survey, December, 2010

Figure 16: Medium of hearing about income tax



Source: Field Survey, December, 2010

The IRS in Bolgatanga needs to double its outreach programmes if the research results is

anything to go by. This is evident by 0% on the effect of brochures as a medium for tax payers to hear about income tax. It is also of much concern if friends/colleagues could register 37% of the distribution; which is even higher than IRS's own tax education which attained only 26%. However, the 37% for both electronic and print media is quite appreciable, indicating the extent to which IRS places premium on the media as a tool of tax education.

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4.4.2.4 Payment for goods and services

The study showed that payments of goods and services are made mostly (60%) by cash while 40% only settles with both cash and cheque. With such a cash dominated economy it clearly shows that IRS cannot depend on the bank statements of tax payers to cross check information presented in their financial statements. This gives the taxpayers the chance to hide valuable information with the intention of reducing their taxable incomes hence taxes.

4.4.2.5 Proper books of accounts

It was detected that 77% (i.e. 54 in absolute terms) of respondents do not keep proper books of accounts; 23% (i.e. 16 in absolute terms) have proper books for accounting purposes. Reasons provided for not keeping proper books of accounts are 'Lack of knowledge in bookkeeping' and 'Inability to engage an accounts officer due to low income earned by business operator'. Besides, respondents' level of knowledge in accounting are either (i.e. 50% each) low/poor or average/medium. None admitted high level of knowledge in accounting. It was further noticed that in spite of the poor

knowledge in proper accounting, 90% of respondents are not engaging the services of an accountant with the reason that they simply could not afford the ‘high service fees’ charged by these professionals.

4.4.2.6 Filing of returns

It was discovered that 64% (45 in absolute terms) of respondents do not regularly file returns at IRS. Reasons provided were ‘Lack of bookkeeping and accounting knowledge’ and ‘Cumbersome procedure of filing (i.e. difficulty in filling/completing forms)’.

4.5 SUGGESTIONS TO IMPROVE TAX ADMINISTRATION

The respondents provided suggestions with the intent of improving tax collection in the informal sector in the tax district of Bolgatanga. Among the suggestions were regular and intensive field operations. Tax officials are expected to seek to increase contact with the Trade and Business Associations especially in the informal sector within the Bolgatanga Municipality through frequent meetings to identify and address policy, operation and other related issues for the improvement of their understanding of tax procedures. Secondly, as an added advantage to the above point, there should be regular and sustained monitoring by tax officials.

Thirdly, more tax officials should be employed to augment the staff strength of Bolgatanga IRS, since the large tax district and the large size of the informal sector have always been the bane of IRS to cover many potential taxpayers. Fourthly, it is important that tax officials are provided with the requisite logistics for efficient and effective

discharge of their duties. Finally, IRS should ensure that tax education programmes are sustainable and cost effective.

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5.1 INTRODUCTION.

This chapter presents the summary of the research findings, conclusion drawn from the study and recommendations.

5.2 SUMMARY OF FINDINGS.

The aim of this research was to find out the causes of tax non compliance behaviour in the informal sector and besides, explore further the challenges in taxing the informal sector in Bolgatanga Municipality; with specific research objectives being: to find out why non compliance of income tax is high in the informal sector; to identify the challenges that militate against effective revenue mobilization by IRS from the informal sector.

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The following summaries are presented based on the findings in chapter four of this study.

Application of sanctions for not honouring tax obligation by tax payers

It was found out that the IRS in Bolgatanga Municipality do not apply all the approved sanctions for not honouring tax obligations by tax payers. This was affirmed by 60% of the respondents from the IRS. The reasons given were lack of the will to apply the sanctions on the part of the tax officials and besides, the sanctions involve long and cumbersome procedures.

Regular tax education

There was 100% affirmations that owing to capacity constraints and lack of resources the IRS in the municipality do not organize tax education programmes regularly to educate the public and for that matter the tax payers on the need to pay taxes and file returns on time. This was also confirmed by the tax payers with 98% responses.

Lack of regular tax education programmes to a large extent contributed to non submission and incomplete filling of returns as well as nonpayment of taxes as indicated by the tax

officials.

Anticipation of benefits and the level of satisfaction with the use of taxes by government.

The research showed that while 79% of the respondents pay their taxes in anticipation of benefits such as provision of infrastructure like schools, hospitals, roads to mention but a few, 21% expects otherwise. Besides, the study showed that 63%, 14% and 23% were averagely satisfied, highly satisfied and not satisfied respectively with the use of tax revenue by the government.

Again, the research revealed that while 15% of the respondents from the informal sector viewed the existing tax rates for the individual tax payers as fair, 85% were of the view that they were not fair and therefore called for a reduction in the current tax rates.

Further, it came to light that 99% of the respondents were of the view that severe punitive measures could dissuade people from evading taxes and suggested punitive measures such as closure of businesses of defaulters, seizure of wares of hawkers and more strict terms prosecution as means of curbing tax evasion in the municipality.

Reasons for tax evasion

The four points provided as reasons for tax evasion were strongly affirmed with the following percentages: 'too high tax rates', 41%; 'knowing others are not paying', 29%; 'unfair application of tax rates', 16%; and 'mistrust of government for the use of tax rates', 14%. Besides, a respondent provided additional reason for tax evasion as, 'the tax net fails

to catch all taxable ‘insects’, while the few complying ones are being pressurized and intimidated’.

Participation in decision making influences tax compliance

The study further revealed by 81% that participation in decision making process serves as a major factor of influencing compliance level with the reasons that it increases ones commitment to the institution and besides, makes one proud to be heard and probably implementing ones counsel.

Challenges in Tax collection

The research showed that there exist challenges starring at IRS in the face; and tax officials considered ‘capacity constraints’ as the most challenged factor in tax collection in the Bolgatanga Municipality; followed by ‘Large size of informal sector’, ‘large size of tax district’, ‘notions of equity’, ‘political interference’ and ‘constant mobility of operators’ in that order as per the ranking.

Tax payers file their returns annually with IRS

The research revealed that not all taxpayers file their respective returns with the organization annually. In the same vain tax officials encountered several difficulties with tax payers in filing returns .These included improper completion or filling of returns, late submission of returns, non submission of returns and ignorance of the benefits of filing returns, tax payers not declaring the right income and inadequate information from tax payers.

Challenges encountered with tax payers in the payment of taxes

The research revealed an overwhelming affirmation that tax officials encountered on daily basis several challenges in tax collection. Notable among them were tax payers complains of financial constraints due to poor performance of business and high tax rates, tax payers ignorance of income tax, high rate of illiteracy and poverty among majority of tax payers in the informal sector and late payment of taxes.

Difficulty of tax collection in the informal sector

The study showed that the ‘large size of the informal sector’ and the ‘large size of the tax district have been the most difficult tasks to overcome in the collection of taxes in the municipality. One other difficult point that needed consideration was the constant mobility of business operators, thus making it virtually impossible to track them. Issues such as ‘cash transactions’, ‘uncertainty’, ‘indifference to formal accounts’ and ‘political interference’ all played one role or the other in making it difficult to collect taxes.

Proper books of accounts

It was detected that 77% (i.e. 54 in absolute terms) of respondents do not keep proper books of accounts; 23% (i.e. 16 in absolute terms) have proper books for accounting purposes. It was further noticed that in spite of the poor knowledge in proper accounting, 90% of the respondents were not engaging the services of accountants with the reason that they simply could not afford the ‘high service fees’ charged by these professionals.

5.3 CONCLUSION

The research revealed that there was lack of tax education in the municipality, majority of the tax payers were either averagely satisfied or not satisfied with the use of tax revenue by the government and the greater percentage of people pay their taxes in anticipation of benefits from government. Also, the IRS were not applying the approved sanctions for failure to pay taxes, the tax net failed to catch all taxable 'insects' and besides, participation in decision making process and social sanctions increase compliance level.

In conclusion, taxing the informal sector depends on a combination of approaches and mechanisms. Tax collection is an important governance challenge that depends on a compliance culture, the values and norms of a society, its history and above all the capacity of the government to deliver. The potential for taxing the informal sector depends upon a) the degree of pressure on governments to increase revenues and b) the existence of collective actors in the informal sector having institutionalized channels for negotiation with the state (Stella 1993 cited by Aryee, (2007)). Above all, there must be a different way of thinking politically about taxation of the informal sector that could lead to a substantial new research agenda. In other words, to make inroads into the difficult problem of taxation of the informal sector we need to think differently about the issue. Maximizing voluntary compliance is therefore a must which must be taken seriously by any reform or new research agenda.

5.4 RECOMMENDATIONS

In view of the findings of the research the following were recommended:

Intensive and Regular Monitoring

Officials of IRS should undertake regular and intensive field operations by ensuring regular monitoring of the operatives within the informal tax net. Secret personnel or spies should be engaged to download verifiable information about all tax evaders for rewards.

Furthermore, tax payers should be encouraged to make use of the cheque system. This will enable IRS to cross check informations provided in the financial statements of taxpayers using their bank statements.

Capacity Building

More tax officials should be employed to augment the staff strength of Bolgatanga IRS. Also, training and re-training of tax official in modern trends of tax assessment is key. Therefore tax official should be well equipped in the area of tax education programmes. Again, as an interim measure to solve the shortage of staff problem the IRS should use the leaders of identifiable groups such as Hairdressers and Beauticians Association, Butchers Association, Dressmakers and Tailers Association and so on to collect taxes from their members.

Logistical Support

Tax officials should be provided with the requisite logistics for efficient and effective discharge of their duties. The tax system should be computerised to bring efficiency in the tax administration and a reduction in the cost of tax collection in the district in terms of time and personnel to be employed.

Regular Tax Education and Advertisement

There should be regular tax education for the general public using both the electronic and print media. Billboards should be mounted at vantage points in the district to educate the public about the importance of taxation. The IRS should organize seminars to teach tax payers basic bookkeeping principles. This will enable them submit accounts for fair assessments.

Effective Customer Relations

Maintenance of very good customer relations is key; thus, tax collectors should apply marketing, human resource strategies and a high sense of diplomacy to convince and encourage tax payers to make good their respective tax liabilities. However, when the need arises the rules and regulations governing tax compliance must be applied. Again, tax net should be widened further so as to capture much more lower income earners. Also, involving the tax payers and the general public in decision making processes so far as taxation is concerned will be of great help since it will ensure commitment.

Prudent utilization of Tax Revenue

Governments should be seen to be using revenue accrued from taxation prudently without misappropriation and misapplication; and governments should be accountable and transparent. By so doing the people will have confidence and trust in the government.

Regular Review of Tax Administration

Research should be conducted on personal developments such as - buildings of complex nature by individuals, types of cars people use and general life-style. A database should be built on taxpayers and potential ones.

Motivation of Tax Officials

The tax officers should be effectively motivated at various levels like – high salary, high end of service benefit, end of year bonus, housing and car loans payable in at least 10 years period.

Reward System

A reward system should be initiated whereby the best small tax payers at the district levels would be awarded annually as in the case of farmers, teachers, health workers among others. This will serve as incentive for tax compliance among the small taxpayers.

Collaborations

The IRS should collaborate with other institutions, for example, the assemblies to get information on potential tax payers since no person can operate business without license from the assemblies.

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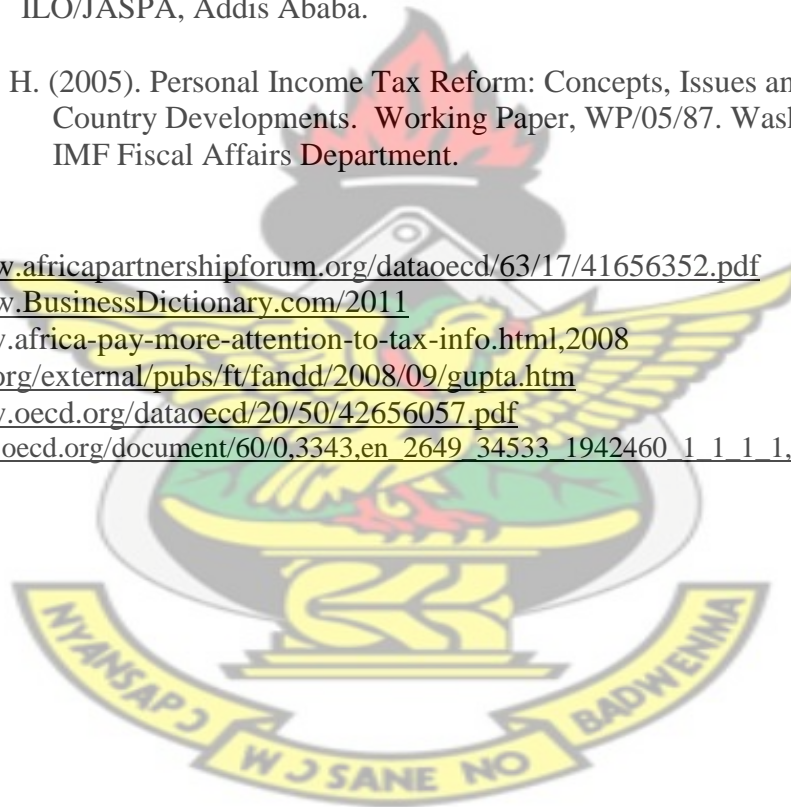
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APPENDIX

QUESTIONNAIRE FOR THE TAX OFFICIALS

KWAME NKRUMAH UNIVERSITY OF SCIENCE AND TECHNOLOGY (KNUST) INSTITUTE OF DISTANCE LEARNING (IDL)

The purpose of this questionnaire is to gather data for a study on Taxation and Informal Sector: A case study of Bolgatanga Municipality. Data collected would be used solely for academic purpose and respondents are assured of the confidentiality of information provided.

A. PERSONAL INFORMATION

1. Gender: Male () Female ()

2. Age Group:
16 – 30 years ()
31 – 45 years ()
46 – 60 years ()
61 years and above ()

3. Level of education
Basic () SHS/ Commercial () Diploma () 1st and/or 2nd Degree
() Professional () Others) ()
Specify.....

4. How long have you been with IRS?
Less than 5 years ()
Between 6 and 9 years ()
10 years and more ()

5. Rank: Junior staff () Senior level () Management Staff ()

B. FACTORS AFFECTING COMPLIANCE LEVEL

6. Do you apply all the sanctions for not honouring taxes by individual tax payers?

A. Yes () B. No ()

7. If no what are the reasons for not applying the sanctions for failing to pay taxes?

.....
.....
.....

KNUST

8. Do you regularly organize tax education programmes to educate tax payers on the need to pay taxes and file returns on time? A. Yes () B. No ()

If no give reasons

.....
.....
.....

9. How do you assess the existing tax rates to individual taxpayers?

Fair () Too High () Inadequate ()

10. Is there the need to change the existing tax rates? A. Yes () B. No () Expatiate your choice of answer.

.....
.....
.....

11. To what extent are you satisfied with the compliance level of the self employed businesses in your tax district?

A. Highly satisfied () B. Averagely Satisfied () C. Not satisfied ()

C. CHALLENGES IN TAX COLLECTION

12. Do you face any challenge while discharging your duties as a tax officer?

- A. Yes () B. No ()

13. If yes, what are some of the challenges? Please tick more than one answer and rank them in order of most prevalent.

Rank

- A. Capacity constraints ()
- B. Notions of equity ()
- C. Political interference ()
- D. Large size of the tax district ()
- E. Large size of the informal sector ()
- F. Please specify if any other.....

14. Are you content with the number of tax payers who keep books of accounts?

- A. Yes () B. No ()

15. How do you determine the taxes of those who do not keep proper books of accounts or submit accounts?

.....
.....
.....

16. Do all taxpayers file their returns with you annually? A. Yes () B. No ()

17. Do you encounter any difficulties with taxpayers in filing their returns?

- A. Yes () B. No ()

If yes, what are the difficulties?

.....
.....
.....

What measures have you put in place to check the difficulties?

.....
.....
.....

18. Have you been encountering any challenge with taxpayers in paying taxes?

- A. Yes () B. No ()

If yes, what are some of the challenges?

.....
.....
.....

19. Why is it difficult to collect taxes in the informal sector? Please rank them in order of most prevalent.

- Rank*
- i. Transience
 - ii. Cash Transaction
 - iii. Uncertainty
 - iv. Large size of the tax district
 - v. Large size of the informal sector
 - vi. Indifference to formal accounting
 - vii. Political Interference

20. What suggestions can you offer to improve upon tax collection in the informal sector in your tax district?

.....
.....
.....

**QUESTIONNAIRE FOR THE INFORMAL SECTOR OPERATORS
(TAXPAYERS)**

**KWAME NKRUMAH UNIVERSITY OF SCIENCE AND TECHNOLOGY
(KNUST) INSTITUTE OF DISTANCE LEARNING (IDL).**

The purpose of this questionnaire is to gather data for a study on Taxation and Informal Sector: A case study of Bolgatanga Municipality. Data collected would be used solely for academic purpose and respondents are assured of confidentiality of information provided.

A. PERSONAL INFORMATION

1. Gender: Male () Female ()

2. Age Group:

 16 – 30 years ()

 31 – 45 years ()

 46 – 60 years ()

 61 years and above ()

3. Marital Status:

 Married () Single () Divorced () Separated () Widow/ Widower ()

4. Level of education

 Basic () SHS/ Commercial () Diploma () 1st and/or 2nd Degree

 () Professional () No formal education () Others () Specify

5. Which of the following informal sector operators do you belong to?

 Hairdresser and Beauticians () Dressmakers and Fashion Designers () Artisans ()

 Contractors () Food Vendors () General Traders ()

Mistrust of government for the use of tax revenue ()

Please, specify if others

.....

.....

.....

12. Do you think social sanctions can deter people from evading the payment of taxes?

A. Yes () B. No ()

13. Do you think individuals' participation in decision making process can influence their level of tax compliance? A. Yes () B. No ()

Explain your answer

.....

.....

.....

C. CHALLENGES IN TAX COLLECTION

14. Where do you operate your business from?

Store () Market stall () Table Top () Hawking () Kiosk/Container
() Others, specify.....

15. How long have you been in your current business?

1 – 5 years () 6 – 10 years () 11 – 15 years () Above 15 years ()

16. Where did you hear about income tax?

Media (Radio, TV & newspaper) ()

Friend/Colleague ()

Brochures ()

Tax education program by IRS ()

Have not heard about income tax ()

17. What is the mode of payment for your goods or services?

Cash () Cheque () Both ()

18. Do you keep proper records or books for accounting purposes?

A. Yes () B. No ()

If No, explain

.....
.....
.....

19. What is your level of knowledge in accounting?

A. Low/Poor ()

B. Average/Medium ()

C. High/Very good ()

20. If low, do you engage the services of an accountant? Yes () No ()

If no, what is the reason? High service fees () Lack of accountants ()

Nneed ()

21. Do you file returns including accounts regularly with IRS?

Yes () No ()

If No, explain

.....
.....
.....

22. What suggestions can you offer to improve upon tax collection

system?.....

.....
.....

KNUST

