

UNIVERSITY OF CAPE COAST

TAX EVASION AND THE GHANAIAAN ECONOMY: EVIDENCE FROM  
GHANA REVENUE AUTHORITY, CAPE COAST METROPOLIS

MARY ESSILFIE-AFFUL

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BY

MARY ESSILFIE-AFFUL

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## DECLARATION

### Candidate's Declaration

I hereby declare that this dissertation is the result of my own original research and that no part of it has been presented for another degree in this University or elsewhere.

Candidate's Signature:..... Date: .....

Name: Mary Essilfie-Afful

### Supervisor's Declaration

I hereby declare that the preparation and presentation of this dissertation were supervised in accordance with the guidelines on supervision of dissertation laid down by the University of Cape Coast.

Supervisor's Signature:..... Date: .....

Name: Mr. Stephen Asante

## ABSTRACT

By far a lot of research has been done but the outcome of this study will strengthen the systems of GRA by way of employing all the necessary strategies probably going beyond what they do to close the loop holes thereby reducing the rate of tax evasion. The main objective of the study was to examine tax evasion and its effects on the Ghanaian economy with evidence from Cape Coast Metropolis. The research was a case study which blended both qualitative and quantitative methods in data collection and analysis in getting to the bottom of issues discussed. The population of the study were all the tax officials of the GRA and businesses in the Metropolis. Convenience sampling method were used to select 120 businesses and five GRA staff. With the help of SPSS version 16, all the results were analyzed using charts and frequency distribution tables. The study revealed that most tax payers lack the fundamental knowledge on the tax payment process. It was again found that even though the level of evasion was high, there were no evidence of sanctions applied to anyone found culpable. It was revealed also that both categories respondents were very much aware that tax evasion reduces government revenue thereby affecting governments' ability to provide the citizenry with the needed infrastructural development. The researcher then recommended that the GRA in the Metropolis should embark on tax education on payment processes, and the importance of tax to the national economy. It again recommended that appropriate reviews of tax processes should be integrated into the entire tax system to encourage taxpayers' compliance. The GRA should in their attempt to profile businesses and individual tax payers, collaborate with Electricity Company of Ghana since ECG has a complete data of all commercial structures, to help them in their search for people liable to pay taxes.

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**DEDICATION**

To my lovely husband, Mr. Simon Essilfie Afful and my adorable children, Joel,  
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## CHAPTER ONE

### INTRODUCTION

#### **Background to the study**

Tax evasion according to Wenzel (2002), is the illegal dodging of taxes by individuals, corporations, and trusts. Tax evasion often entails taxpayers deliberately misrepresenting the true state of their affairs to the tax authorities to reduce their tax liability. It includes dishonest tax reporting such as declaring less income, profits or gains than the amounts actually earned, or overstating deductions. Tax evasion is an activity commonly associated with the informal economy. One measure of the extent of tax evasion (the "tax gap") is the amount of unreported income, which is the difference between the amount of income that should have been reported to the tax authorities and the actual amount reported. In contrast, tax avoidance is the legal use of tax laws to reduce one's tax burden. Both tax evasion and avoidance can be viewed as forms of tax noncompliance, as they describe a range of activities that intend to subvert a state's tax system, although such classification of tax avoidance is not indisputable, given that avoidance is lawful, within self-creating systems (Lymer & Oats 2009).

Tax evasion simply refers to the underreporting of taxable money income with the intention to escape taxes (Gërkhani & Schram, 2001). According to Elffers (2000) "the gloomy picture of massive tax evasion is a phantom". A large share of revenue is collected without fair and democratic system of tax collection. In some economies, the enforcement system is relaxed to explain the high level of tax payments. Experimental result on tax payment does not support the conclusions from neoclassical models when attitudes to risk are controlled.

“Taxes are what we pay for a civilized society. An essential question for policymakers; is the extent to which individuals are willing to pay this price; given that the probability of being audited by the tax administration is rather low” (Torgler, Schaffnera, & Macintyre, 2007.). According to Torgler, Schaffnera and Macintyre (2007), it is important to examine the factors that influence tax compliance beyond the news of the neoclassical researchers. Thus, the tax compliance literature has shown the necessity of going beyond the neoclassical approach when trying to understand why citizens pay taxes (Torgler et al, 2007).

Revenue is much needed by all governments to develop every aspect of their nation. Common to every nation, there are so many sources of government revenue either internally or externally. A few among them are borrowings, grants, service charges from state owned organizations and most commonly, tax. There is no country without a tax system in place. A tax is a legal and compulsory monetary payment or contribution to a nation, which is levied by the central government on the nation’s citizens.

To a very large extent, the development of every nation depends mainly on taxation. A solid revenue base is one of the foundations of every great nation and this includes Ghana. Revenue gained from taxes is very important in developing every economy. According to the World Bank Report on the finances of government of Ghana in 2011, percentage of tax revenue to GDP in Ghana was measured at 14.87%. Also, according to the Bank of Ghana Monetary Policy Report on fiscal developments. Preliminary fiscal data from the Ministry of Finance and Economic Planning showed that for the first quarter of 2012, total

revenue and grants amounted to GHC 3.5billion, representing 5% of GDP (BoG report, 2012). Tax revenue is thus an important issue of concern in Ghana.

Ghana has a corporate income tax rate of 25% compared to 30% or 35% in some other African countries. Value Added Tax (VAT) is chargeable at 15% on all supply of services imported except those goods and services exempted, all imports of goods and all supply of taxable goods and services made within Ghana (Agaliga 2014). Communication service tax (CST) is applicable at 6% on charges for the use of communication services in Ghana. The rate of import duty ranges from nil to 20% depending on classifications in the harmonized code. Excise duties are generally applicable on the ex-factory price of goods and range from 10% to 17.5% depending on the type of goods. Personal Income Tax (PIT) is also relatively low with a marginal tax rate being 25% on incomes earned over GHS 1,350 each month for resident individuals PWC Country Study: Ghana, (2014).

Multinational entities (MNE) contribute significantly to the tax revenue of Ghana in the form of corporate income tax, VAT, personal income taxes and withholding taxes. PWC'S discussions with some GRA officials confirm that multinational entities make up approximately 5% of the total number of registered agents for VAT purposes but contribute 80% of the total revenue collected (PWC Country Study: Ghana, 2014).

It is obvious that the importance of the contributions of MNEs to Ghana's economy cannot be overemphasized. Thus, taxation contributes so much to the revenue of the country and as such taxation issues are top priority issues in the development of the nation. There are two main systems or types of taxation levied by every government including Ghana, which are direct and indirect taxes. (PWC

Country Study: Ghana, 2014) Without discounting the importance of tax to every government, there are several problems surrounding its collection. Bird (2003) opines that even though tax laws propel citizens of a country to contribute to the government's revenue, it is the effectiveness of its tax administration that will determine the revenue amount that flows into the national revenue coffers. Inadequate collections of tax are the result of some weaknesses in the revenue collections.

Kangave (2005) was of the opinion that even though some countries have the problem of driving its citizens and businesses into the taxation process, governments also face such problems as inadequate administration staff who also possess low skills. Other problems faced by the government tax officials are the huge percentage of illiterate tax payers, inadequate working equipment and lack of reliable data. Again, one great challenge in the administration of tax is the inadequate resources to alleviate and aid the operation of tax officials. In this regard, the resources of tax administration can be classified into two main groups: human resources and physical resources. With regards to human resources, the focus is on the number of quality tax officials available. Physical resources can be seen in a wide perspective, ranging from office buildings and equipment to vehicles and communications systems. Tanzi and Zee (2000) suggest that because of financial limits, some tax officials lack the key principles of accounting necessary to analyze business returns which in turn is aggravated by inadequate training facilities and opportunities. One of the other challenges faced by tax officials is high level of illiteracy on the part of taxpayers in the country. According to the Ghana Statistical Service in a survey conducted in 2010, 51.5%



of the adult population in the country are illiterates. This high illiteracy rate shows that most taxpayers are not able to file their returns or even record their sources of income and expenditures, however tax authorities are usually to collect appropriate taxes from such people (Bird, 2003).

In Ghana tax evasion is also a major problem bedeviling the tax system (Aba, 2013). Tax evasion is an illegal practice where a person, organization and corporation intentionally fails to pay a tax liability truly owed. In other words, an unlawful attempt to minimize tax liability through fraudulent techniques to circumvent or frustrate tax laws. In Ghana, it is known that the informal sector accounts for a major source of employment. There is no gainsaying the fact that most informal sector operators are self-employed and they often operate from homes, while some others use any public space available. Thus, with table and a chair one could easily start up his/her own business with family assistance (Farrell et al, 2000). How to tax the informal sector remains a pressing issue. The informal sector is an obvious focus of attention as it forms a significant and growing proportion of the economy in the developing countries, yet pays little in the form of taxes (Anuradha & Ayee, 2002). The Minister of Finance and Economic Planning in 2016 expressed concern that widening the tax net remains one of the main problems that Ghana is facing. The simple fact that a greater percentage of Ghanaians are all engaged in informal private sector businesses makes the generation of revenue a tedious task, (Budget of Ghana, 2016).

Effectiveness and efficiency in tax administration is also very important and it involves simplification wherever feasible, but it sometimes requires more complex procedures in order to secure even enforcement. The aim of this is to

eliminate unnecessary burden on the taxpayer and the tax officials and to secure a more equitable and effective application of the tax laws. Thereby, the morale and cooperation of the taxpayer as well as the tax official will be improved and better revenue structure obtained. An increase in resource devoted to tax administration should also be contemplated. There is a need for the use of presumptive rules in assessing tax on certain hard-to-tax groups in order to generate the needed tax revenue (Oliver & Richard, 2013).

A society's willingness to be taxed will depend on a large extent its belief about what the tax revenue is being used for. Increased tax effort may be difficult when government expenditure patterns do not give rise to substantial acceleration of national income and when tax sacrifices as well as developmental gains are not equitably distributed among the population. It is therefore clear that tax effectiveness and efficiency is an administrative issue. According to Oliver and Richard (2013), tax compliance may also be affected seriously where administrative deficiencies make evasion and avoidance simple to achieve. This is particular in the Cape Coast Metropolis where evasion is common. Similar problem that affects the willingness to be taxed is within the control of the tax function and integrity of the tax collection system.

Satisfaction is what the customer says it is. Satisfaction is a set of momentary emotional responses that are affected by just about everything that can be listed. In the tax division, tax payer satisfaction is paramount to successful tax mobilization, the effective use of the taxpayer's money among other things. It is the gap between the expected and the perceived outcome (Suraman & Zeith, 2015). It involves access or ease with which the service can be obtained. It also

refer to the perceived effective use of the taxes received. The economic and developmental conditions of a place also contribute to the citizenry satisfaction to paying tax. Since taxes are one of the important elements in managing national income and keeping up with national development and economic freedom, it is imperative for the country to lose a chunk of such an important elements of national income.

### **Problem Statement**

The development of the nation depends on the effective and efficient collection of tax revenue. However, the revenue from taxation is not enough to fully support government activities. The level of potential tax revenue is determined by the level of economic activity of an area (James & Alley, 2001). Each year, the Ghana Revenue Authority set targets for the various divisions nationwide in order to ensure that the division maximizes revenue for the government through tax collection. However the division, in many cases is unable to meet the targets set. It has been noticed that most businesses in Ghana are found in the informal sector and are made up of small and medium scale enterprises (SMEs). It is estimated according to same report that with regards to economic activity, the self-employed sector constitutes about 86.3% and these self-employed mostly operate in informal facilities. Out of the total registered informal sector self-employed operators, a little below 30% are duly registered and are assessed to tax. Although tax payment is compulsory, some SMEs are able to evade tax.

This is the situation of various businesses in the Cape Coast Metropolis, in the Central Region. The Cape Coast Metropolis is noted for some of the best second-cycle schools as well as a number of tertiary institutions in the country. However, the metropolis and that matter the Central region is rated among the poor places in the country. The metropolis cannot boast of good roads connecting its towns and villages, good basic schools, a significant proportion of the metropolis do not have access to portable water, youth unemployment is high etc. It is the expectation of the people that the government fill these developmental and economic gaps.

According to GRA end of year report, Cape Coast Metropolis recorded 329 businesses as well as 639 Small and Medium Enterprises as at the year ending 2015. The report further indicated that out of these flourishing figures, less than 60% paid their returns (GRA, End of year report 2016). This implies that close to 40% of expected revenue were lost. The report however did not assign concrete reasons to the percentage loss. In evading tax, the metropolis and the nation lose the revenue it would have earned from them. Tax evasion has a negative impact on both the local and composite economy. The subsequent tax revenue loss due to evasion impedes the proper operation of the public sector, and as such threaten government ability to finance its basic expenses. This hinders developmental progress in the area.

There is also limited research on tax evasion in Ghana, the few studies on tax evasion does not concentrate on the effects of evasion on the economy. It is on this backdrop that this study sought to examine the effects of tax evasion on the Ghanaian economy with evidence from the GRA in the Cape Coast Metropolis.

### **Objectives of the Study**

This study is aimed at investigating and identifying the effects of tax evasion on the Ghanaian economy with evidence from the GRA in the Cape Coast Metropolis. The study specifically seeks to:

1. Investigate why taxes are evaded in the Cape Coast Metropolis.
2. Investigate how individual and businesses taxes are evaded in the Cape Coast Metropolis
3. Examine existing measures in dealing with tax evaders.
4. Examine the effects of tax evasion on the economy.
5. Identify control measures that can help curb tax evasion.

### **Research Questions of the Study**

To arrive at a rational conclusion and constructive suggestion on the effects of tax evasion on the Ghanaian economy, the study will attempt to find answers to the following research questions;

1. Why do individuals and businesses in the Cape Coast Metropolis evade taxes?
2. How are taxes evaded in the Cape Coast Metropolis?
3. What efforts have the GRA put in place to reduce tax evasion?
4. What are the effects of tax evasion on the economy?

5. What control measures can be put in place to help curb tax evasion in the Cape Coast Metropolis?

### **Significance of the Study**

To maximize the collection of the needed tax revenue for the government, it is very important that the GRA are efficient and effective in their duties as they aim at satisfying the public. The level of potential tax revenue is determined by the level of economic activity of an area (James & Alley, 2001). Domestic Tax Revenue Division is a target driven division of the Ghana Revenue Authority. As a result, each year, targets are set for the various offices nationwide in order to ensure that the division maximizes revenue for the government through tax collection.

The study also seeks to recommend better policies and improved administrative practices, good governance and legal equity in terms of tax issues. In the end when the taxpaying attitudes of Ghanaians change from tax non-compliance to voluntary tax compliance, the economic, political and infrastructural developments in the country would also improve. The informal sector will realize the benefits of paying taxes, the reasons why they should not evade tax and how they can contribute to the building of the entire economy when they pay tax.

Results from this study are expected to give important messages to policy makers in tax administration. The findings of the study would also contribute to the limited knowledge. The results of the study may also contribute to the

understanding of theories underpinning the research by providing answers to the research questions raised in the study.

Lastly, given limited studies in the area of tax evasion in the country and that the few studies available are conducted in different countries (Friedland, Maital, and Rutenberg, 2000; Mason R and Calvin, 2001; & Geeroms, and Wilmots, 2003), the findings of this study would add to knowledge on tax evasion by way of reference material.

### **Organization of the Study**

This study is organized into five chapters. Chapter One deals with the introduction of the study, which contains the background to the study, statement of the problem, purpose of the study, research questions the significance of the study and organization of the study. Chapter Two reviews the relevant related literature. The conceptual framework for the study was also discussed.

Chapter Three focuses on the methodology of the study. It describes the study design, the target population, the sampling procedure, sample size, the research instruments that was used, data and sources, data processing and analysis, the ethical issues arising from the research, and the challenges from the fieldwork. Chapter Four concerns itself with the data analysis, the presentation and discussion of results while Chapter Five provides the summary, conclusions and recommendations of the study

## CHAPTER TWO

### LITERATURE REVIEW

#### **Introduction**

This chapter explores the views which various writers and scholars have expressed about the effects of tax evasion. The study seeks to examine tax evasion as well as find out the effects of tax evasion on a nation's economy, and this chapter provides a focus for the study by considering related literature on tax evasion and its effects on the economy.

#### **Overview of Taxation**

A tax is a levy imposed by a government or a legal entity in a country on its citizens (Altus Directory, 2006-2010). Pratt and Kulsrud (2001) see tax as an exaction to support the government, which means that tax provides a way for a government to obtain a greater portion of revenue needed to keep it in operations. It can thus far be seen that tax is not just a source of revenue; though it has become a great instrument that governments use to achieve socio-economic goals. Selma et al (1951) defined taxation as the process by which a government obtains supports from its citizens to maintain the economy. Louis (1991) is of the opinion that governments use taxation to raise money for public spending. It can thus be



understood that government uses taxation to raise revenue to fund development projects in the country. There are two basic different types of tax, namely, direct taxation and indirect taxation.

Direct taxes refer to that form of taxes collected from the individual or organization on which they are apparently imposed. For example, income taxes are taken from the person who earns the income or in the case of paying gift tax. Direct tax is that tax which is levied on organizations and businesses and as such is paid by such organizations. Direct tax includes capital gain tax, corporate tax, gift tax and income tax. In Ghana, the Domestic Tax Revenue Division has the authority to administer this taxation ( ICAG Taxation Study Manual, 2014). Direct tax is very important given that it is a kind of progressive tax and takes more from the people who have more. This decreases the consumption of luxury goods by the rich and facilitates the diversion of resources from luxury goods production to that of capital construction. According to Ali (2001) this ensures a degree of flexibility in the system of tax, increasing the possibility of tax revenues rising as income increases. The progressive ability direct tax makes it ideal for developing countries. For this reason, it promotes distributive justice in developing countries. As Akakpo (2009) said, inequalities are prevalent in developing countries, and with economic development these inequalities tend to become broader.

One can understand that the development of a nation relies on the citizens, though it should be based on each citizen's capability to pay tax. It is easy to determine the incidence and yield in direct tax when one makes a comparison with indirect tax. In direct that, there is that certainty which means each taxpayer

clearly knows what he is expected to pay, and according to (Akakpo, 2009) yield rises automatically as wealth and population rises. Despite these positives, there is huge administration cost and also the “effect on incentive, enterprise and savings in the case of those with large income, may be considerable” (Ali, 2001).

Indirect taxes are opposite of direct taxation. Indirect taxes are collected from someone other than the person responsible for paying the taxes and are collected by an intermediary body. For example retail stores, taxes are collected through sales, during the purchases tax component from the proceeds are collated for returns. The intermediary body later files a tax return and forwards the tax proceeds to government. Simply put, indirect tax is that tax levied on expenditure.

Basically, this is a tax that is imposed on one person with the expectation that the tax will be transferred to another person. In this case the impact and incidence are on different persons (Akakpo, 2009). Examples of these are custom duty, excise duty and value added tax (VAT). Authorities assigned for this tax are the CEPS and VATS (Ali, 2001). It is called indirect because the tax authorities do not directly deal with the consumer as in tax collection but rather do so indirectly through importers, manufacturers or other intermediaries. The transfer of this tax liability is effected by levying the tax element on the selling price of the commodities to the next person in the commercial chain until it is finally borne by the consumer (ICAG Manual: Taxation and Fiscal Policy, 2015).

With indirect tax, the value of the goods determines the rate of duty. Here, the attributes of the commodity determines the tax rate which is also based on a fixed amount. (Akakpo, 2009). Example, the weight of a bag of rice may be taxable at GHS 20.00 per 5kg and drinks may be taxed based on their volume.

There are many advantages of this type of taxation. First and foremost, an increased indirect taxation allows for labor market incentives due to the fact that the government can decrease the whole tax on income and capital. This is especially true as income tax and corporate tax rates have been reduced in Ghana over the years. Most people prefer indirect tax to direct tax because they are able to retain more of their income (Ali, 2001). This explains why returns on working extra hours rise when income tax rates are reduced. However, in the case of income tax, people are able to earn a particular target post-tax income with relatively fewer working hours compared to previous working hours before the tax cut (Ali, 2001). If leisure is regarded as a normal good, employees would choose not to work and in order to enjoy more leisure time and still earn the same income. Secondly, since indirect taxes are only collected from businesses, it is cheaper to administer than direct tax. Government gets more control over its use of fiscal policy with indirect taxation. Also, even without parliamentary approval some indirect taxes can be altered between budgets. A particular example is VAT and excise duty. On the opposite, direct taxes can only be altered in the annual budget.

Despite all these positives, one may argue that an indirect tax is regressive. With indirect taxation, each taxpayer pays the same rate of tax, and considering the different levels of income, it means those who earn low income pay more as compared to those that earn more income. On the part of direct tax, those that earn more income pay more tax as compared to low income earners. That is, as earlier said, direct taxes are progressive.

## **Brief History of Taxes in Ghana**

According to Randolph (2011), taxation was introduced in Ghana in the year 1943. Prior to its introduction in 1943, the colonial government made some attempts to introduce it at earlier date. For example, in April 1852, in order to obtain revenue to fund the increased cost of British Administration, the government introduced what it called the Poll Tax Ordinance. Men, women, and children living in districts under British protection were made to pay one shilling (1/-) per head for a year as poll tax ordinance. Some weaknesses in the system of tax collection made these attempts of direct tax introduction fail, coupled with the fact that the first revenue collected were not used for the purpose for which they were introduced. That was how taxation begun in Ghana and since then, there have been important amendments in the tax laws over the past years. Abdallah (2008) observed that Income Tax Ordinance was introduced in 1943 and was the first income tax law.

Since there was an Income Tax Act already in United Kingdom, the Ghanaian tax our ordinance was modeled on that act. Our ordinance levied the tax primarily on incomes that had their source in Ghana which meant that income from foreign source was not taxable unless it was remitted in Ghana. Our ordinance contained some numerous personal reliefs and deductions and these were important features of the ordinance.

Since its inception, the Income Tax Law has seen diverse changes and modifications. An example is the Income Tax (Amendment) Ordinance 1952. The initial consolidated edition of the Income Tax Ordinance was released in March, 1953. Subsequent to it was the amendment to the consolidated edition Act 68 in

1961. This was preceded by Act 178 and Act 197 in 1963, and Act 312 in 1965. In September 1966, the second consolidated edition, Tax Decree 1966 (No.78) was released. Again, in December 1975, the Income Tax Decree 1975, SMCD 5, the third consolidated edition was released. In the year 2000, the ruling NDC government introduced new tax laws to manage the administration of income tax, capital tax and gift tax in Ghana and thus, made tax administration generally better in Ghana.

### **Evolution of Ghana Revenue Authority**

The Ghana Revenue Authority is the Ghana Government agency responsible for the overall oversight of all the taxation agencies in the country. The authority was established in 2009 as a merger of the Internal Revenue Service (IRS), Customs, Excise and Preventive Service (CEPS), Value Added Tax Service (VATS), and the Revenue Agencies Governing Board (RAGB) Secretariat. Upon its establishment, the GRA issued a statement to the effect that the revenue agencies would therefore, cease to exist and be subsumed into the Ghana Revenue Authority with the passage of GRA Act 2009, (Act 791). This Act established the GRA as a body corporate to replace CEPS, IRS, VATS and RAGB for the administration of domestic tax and customs revenue in Ghana.

In that regard, Mr George Blankson, the Commissioner-General of GRA explained that under the newly established GRA, the operations units of IRS and VATS had been integrated into the Domestic Tax Revenue Division (DTRD), while the operations and preventive units of the CEPS now formed the Customs Division. As such, all the finance, human resource, administration, information

technology and research planning and monitoring, which all constituted the management support functions and were performed by the erstwhile CEPS, IRS, VATS and RAGB, were merged to form a new division called the Support Services Division (SSD). Each of these divisions were then headed by a Commissioner, while the remaining management support functions, including Communication and Public Affairs, Internal Audit, Internal Affairs, Modernization Program Office and Board Secretariat and Legal Affairs were headed by Deputy Commissioners, who reported directly to the Commissioner-General. In accordance with the provisions of the GRA Act, 2009 (Act 791), all dealings and businesses with the former revenue agencies were to be redirected to the Ghana Revenue Authority with immediate effect.

### **The Concept of Tax Avoidance and Tax Evasion**

Considering the problems of tax avoidance and tax evasion and their impact on the Ghanaian economy, it is imperative to understand the concept of taxation and to clarify some misconceptions regarding the distinction between the two concepts. Over the years, a lot of Ghanaians have misunderstood the concept of tax avoidance and tax evasion. Most of them have little or no idea about the fact that tax avoidance is a legal way of reducing tax revenue and tax evasion an illegal way of reducing tax revenues (Quaye, 2014).

The word evade and avoid are generally used interchangeably and they connote same thing. To the professional, there is a sharp and fundamental distinction between the two concepts. The distinction will be clearly emphasized for the purpose of this study, so as to apply the difference appropriately.

Wikipedia describes tax avoidance as 'the legal utilization of the tax regime to one's own advantage, to reduce the amount of tax that is payable by means that are within the law'.

The Legal dictionary describes tax avoidance as 'a process whereby individual plans his or her finances so as to apply all exemptions and deductions provided by tax laws to reduce taxable income'. On the other hand, the International Glossary (1996) describes tax evasion as 'a term used to describe illegal arrangement where liability to tax is hidden or ignored'. For instance, the tax payer pays less than he is legally obliged to pay. According to Abdallah (2008), "Tax evasion is using illegal means to reduce tax". Browning (1979) also describes tax evasion as 'the failure to pay taxes that are legally due.

Tax evasion is the employment of unlawful methods to circumvent the payment of taxes (Legal Dictionary, 2000). The legality distinguishes tax evasion from tax avoidance. Avoidance can be evasion except the act taken to avoid tax are through sincere means and within laid down laws. The tax avoider is anyone who arranges his affairs in such a way that he pays little or no tax at all, and takes advantage of all legal opportunities to minimize his or her state of affairs, while the tax evader, is one who for a number of reasons, refuses to fulfill his civic responsibility under the law, and he is for all intended purpose, a criminal.

There are clear distinction between these two concepts which is important to note. Tax avoidance is an act of winning games without cheating, thereby beating the Internal Revenue Service but tax evasion should be condemn because it is the wrong side of the line. Hoffman, Willis and Phillips, (2002) gave some clear distinction between the two concepts these are listed below:

- a. Tax avoidance is an action within the law while Tax evasion is an illegal act.
- b. Tax avoidance is not criminal, but tax evasion is criminal.
- c. Tax avoidance involves critical study of the tax Acts and taking the best advantage of all reliefs, exemptions and allowance available to the loopholes in tax laws while tax evasion could be due to fraud or willful default in payment.
- d. Under tax avoidance, the tax payer will show up and present all necessary documents to the tax authority and the subsequent assessment will be settled while under tax evasion, the tax payer may not show up at all to the tax authorities.

### **Reasons why People Evade Tax**

Revenue Institutions and a variety of academic disciplines suggest that there are two approaches to explaining the reasons for non-compliance. One is to analyse compliance in terms of economic decisions based on the likely economic incentives and costs of complying or not. The other has been to examine the effects of other factors on compliance decisions, particularly as they relate to tax payer behaviour and sometimes tax agency behaviour. In order to tackle the problem of tax avoidance and tax evasion properly, it is important to understand some of the factors underlying the decision to pay tax or not to pay taxes. (Ablordeppey 2005) is of the opinion that a positive relationship exist between tax evasion and perceived inequality of the tax system.

Spicer (1994) in his dissertation, behavioral model of income evasion



concluded that evasion by an individual was also found to be positively related to the number of his friends or colleagues who they believe are evading taxes. Beattie (1992) is of the opinion that the desire to own more wealth is one of the reasons for evading taxes. This is because ultimate benefit of the sales of a businessman is the amount of money remaining after he has paid all expenses including taxes. His goal is to reduce cost, reduce his price to obtain a bigger share of the market, and thus, increase the cash available to the business at the end of the financial year. Studies have shown that the tax payer attitude and decision to evade tax is based on different reasons. They include excessive corruption on the part of government officials, problems of assessment, collective and enforcement of tax administrators' incompetence on the part of tax authorities, general dishonesty among Ghanaians, political culture, ignorance, unfairness of the tax system, and lack of regard for equity, law and justice, as well as unpatriotic Ghanaian citizens. (Ablordepy, 2006).

It can be deduced from the above, that certain factors have been responsible for increased tax avoidance and tax evasion in Ghana. Basically, ignorance is a major factor because tax payers think that the money is for the tax collectors and government, and they also do not believe they will benefit from the money they pay.

According to Clayton and Brown (2003), "In the first place, people who benefit from government service should be the ones to pay for them and secondly, people should pay according to the benefit they receive". Myles (2005) posits that, "the importance of developing a theoretical understanding of tax evasion can only

be assessed by estimating the actual extent of evasion''. Apart from ignorance, other reasons some Ghanaians avoid and or evade tax include the following:

**Inadequate Tax Incentive by Government:** According to Ablordepy (2006) "the tax incentives offered by government have neither hind up to the expectation or motivating investors into the country nor influencing the location of business''. If the incentives given by government are promising enough, investors and tax payers would be willing to pay the taxes due the government, instead of avoiding and or evading it.

**Poverty or Shortage of Funds:** There is a wide spread of tax avoidance and evasion which can be attributed to high cost of living that has left many individuals in poverty. In view of this, poor individuals who enter into sole proprietorship will always want to evade or avoid tax in order to meet their pressing needs. Also, it is believed that only rich people drive nice cars and live in expensive houses thus, some people avoid and evade tax to enable them get these luxuries and other necessities of life, like food, shelter, and clothing.

**Loose and Weak Tax Law:** Where the tax laws are loose and full of loop holes, it will tempt avoiders and evaders. Punishment for tax evasion is very mild in Ghana, and people may be tempted to evade taxes. The multi-nationals operating within the country may capitalize on these loop holes and also the lack of effective tax legislation to reduce their tax liabilities.

**Inadequate Personnel:** The relevant tax boards and offices are grossly under-staffed. The amount of work exceed manpower and the tendency has always been to rush up work in an attempt to live up to the tasks. This leads to mistake of assessment or complete omission of some tax payers name from the

tax list (Ntim, 2007).

**Inadequate Tax Education:** Where a tax payer who is not criminally minded is aware of massive tax evasion by other tax payers, he may feel that the least he could do is avoid tax by planning in order not to bear more than his fair share of the tax burden (Nightingale, 1979). This is because adequate measures have not been carried out by government to educate citizens on the importance and benefits of taxation to the Ghanaian economy.

**The Decision to Evade:** When one decides to comply with tax laws, it means the person will correctly reveal his tax base and calculate tax liability correctly, file returns on due times, and subsequently pay the tax due. Many decisions to evade tax emanate from these simple points. Those who evade tax first of all may decide not to correctly reveal their tax base, and as such will not give a correct determination of their tax liability. Most evaders too decide not to file their correct returns and thus, subsequently, evade tax. For the problem of tax evasion to be tackled properly, it is imperative to ascertain some factors behind people's decision not to pay tax. In order to come out with methods and instruments to fight tax evasion, it is vital to first of all, establish a broad understanding of the different reasons why people evade taxes. Some causes of tax evasion are specific to some countries, by and large; the various causes of tax evasion are general and can be applied to almost all countries.

Pommerehne et al. (1994) conducted a study to recognize the determinants of tax evasion. They used the presence of grievance in absolute terms in their study. The results indicated that as the sentiments of grievance increased in absolute terms, the level of tax evasion also increased and the level of tax moral

belief decreased”. Orewa (1957), scrutinized the features of tax evasion. His study revealed that because people can move from one district to another easily and continue with their business, there was the chance of saving that legal money. He also found out that some operators do not keep proper or adequate records of their transactions and as such, submit their interim income to tax authorities for tax purposes. Again, it was revealed that people who earn wages or salaries freely dislocate at certain times, in order to prevent tax authorities from locating them and thereafter collecting tax revenue. Some basic reasons why people evade taxes are outlined below.

**The Absence of a “Quid Pro Quo”:** Basically, people do not like the idea of paying taxes. This is because people feel they do not receive anything of value in return for the tax they pay. Most people always argue that “why should they pay tax when those taxes are not used to provide the basic things they need?” Instead of paying, they would rather use that money to provide those amenities to themselves (Kangave, 2005).

**Inequitable Distribution of Amenities:** It is common in most countries and Ghana is not an exception- that people always chastise the government for being partial in the distribution of amenities. Mostly, evaders feel that since a certain part of the country enjoys a greater share of amenities, those working there should be taxable. It is understandable given the fact that one pays tax and still do not have the amenities others enjoy in their part of the nation (Akakpo, 2009).

**Perceived Mismanagement of Tax Revenue by Government:** Everyday there are issues of corruption and misuse of public money on radio stations and televisions. There countless evidences of how people in government have been

carelessly using public funds mostly to their personal benefit. Typical in Ghana is the issue of judgment debts. Various projects, for which government assigned huge sums of money, have reportedly failed and these issues are always discussed by the media. On this grounds, people decide either not to pay the tax at all or pay just a small portion of the real amount, bearing in mind that these mismanagement of public funds will not stop.

**Remoteness of Taxpayers from the Government:** Most people believe that taxes are paid to cater for the well-being of government officials who already belong to that class higher than that of the tax payers. People in government in most cases become enemies to the average Ghanaian, given the way of life, which is wholly apart from the average tax payer. Most tax payers are aware of the various tax reliefs given to these people who already live rich lives. The taxpayer lives quite apart from the government specially, and thus feel no need to pay tax to those government officials living in big cities. Probably, a little education will be able to help taxpayers understand this issue very well.

**Absence of Spirit of Civic Responsibility:** A greater percentage of the adult population in Ghana are illiterates as indicated earlier on. For this reason, most people do not comprehend that they are liable to certain obligations like payment of tax. Regardless, anytime the government tries to educate the public on such negative attitudes, these same public try to suggest that government rather prints enough currencies to alleviate the challenges faced by the country. The absence of this form of patriotism accounts for increased tax evasion in Ghana. Other writers in other countries have also come out with several other causes of tax evasion. For example, Orewa (1957) in Nigeria contended that partial evasion

may occur because of the improper bookkeeping and accounting records maintained by traders and also, the belief by some illiterate taxpayers that only those workers, who earn wages or salaries should be taxable. This belief, however, is a wrong perception. Kiabel (2001) is of the opinion that various entrepreneurs and business operators do not understand the need to pay taxes even though they earn much in their business. It clearly shows signs of unpatriotic citizens. Some people just decide to keep their income to themselves just for that sole reason. Song and Yarbrough (1978) explored both attitudinal and behavioral aspects of tax ethics. Their study revealed that whilst most people feel that the tax laws should be obeyed, they do not regard violations as serious crime meriting a severe punishment. Kaldor (1962) suggests a good link between tax evasion and the perception of inequality in the payment of tax. That is, the higher people's perception of tax inequality, the higher the incidence of tax evasion. Spicer (1976) also opined that, there is a positive relationship between those who evade tax and the rate of tax evasion among such evaders' friends. Dean, Keenan and Kenny (1980) also opined that a majority of the respondents representing 93% thought that "income tax is (much/little) too high" while a substantial proportion of 62% also asserted that the government do not spend taxpayers' money wisely. With this latter point, most people feel that the tax paid is not correctly spent by government. The survey also showed that many respondents felt they were paying too much income tax.

### **Challenges of Tax Evasion on the Ghanaian Economy**

Despite the fact that there are tax laws that compel people to pay tax to enable government embark on developmental projects, the effectiveness of tax laws will determine the tax revenue realized by the tax officials (Ablorh-Quarcoo, 2010). Tax avoidance is very common and persistent such that no matter what legislation is put in place to curb it, some tax payers always find a way around it. Ghana loses millions of United States Dollars in tax revenue every year due to tax avoidance and tax evasion (Senanu, 2005). In effect, the result of tax avoidance and tax evasion reduce revenue to the government through the tax authorities. Multi-national corporations operating in Ghana have been using empirical and exploitative trade liberalization to gain financial advantage, such as taking advantage of tax incentives.

As a result, government has not been able to adequately tax or collect the appropriate taxes from the multi-nationals, local corporations and the elite (Otioku, 1992). The result and effect of this is a serious economic crisis that has led to extreme poverty.

Some of the impact of tax avoidance and tax evasion on the Ghanaian economy are as follows:

**Decrease in Tax Revenue:** The main implication of tax evasion and avoidance is that it reduces the amount that government receives as revenue from taxation therefore, the amount needed by the government to improve the economy is inadequate. A large percentage of revenue for the government comes from taxation. Almost fifty percent (50%) of tax revenue is lost every year as a result of tax evasion (Ablorh-Quarcoo, 2010).

Tax avoidance and its impact is a global phenomenon. Even the world's

developed nations are not spared. For example, in the United States of America, the Senates parliament Sub-committee on Investigation examined the actions taken by Professor Finns, to promote abusive tax shelters were being mass marketed by major accounting firms and as a consequence, the government was losing billions of the U.S dollars (Hoe, 2010).

**Inadequate Supply of Basic Amenities:** Tax avoidance and evasion affect the extent to which the government can provide basic needs of the population. The result and effect is deplorable infrastructure condition (Abler-Quarcoo, 2010), disarrayed educational system and sub-standard health system, water supply, road and power supply. Above all, achievement of the economy “Better Ghana Agenda” is hardly realizable with the low revenue yield.

**Income Inequality:** One of the functions of taxation is to redistribute income, but illegal accumulation of wealth, through tax avoidance and evasion has further widened the gap between the low income earners, and the high income earners (Clayton and Brown, 1983). In the U.S for instance, more than 60% of the largest and profitable U.S companies boasting of pre-tax profit of 1.1 trillion US dollars did not pay any federal taxes from 1996 through 2000 (U.S General Accountability Office, 2004) reports show that because of this tax avoidance, contractors had a great advantage over their domestic competitors thus, there is no possibility of fair competition used.

**Increase in International Tax Planning:** This has also caused a decline in tax revenue. It is greed and the fear of seeing their deep pockets depleted that drives their frenzied attacks against off-shore havens and not a fight against international crime as we are made to believe. It is the increase use of off-shore tax-free



companies by the general populace that constitute a major headache for the government because it reduces their tax revenues (Beattie, 2010).

### **Tax Evasion and Tax Expenditure in Developing Countries**

The provision of public service and infrastructure is the key factor for economic development and growth. Many developing countries fail to raise tax revenue required to finance their public sectors. In 2005, the average tax revenue to GDP ratio in the developed countries was approximately 35%. In the developing countries, it was equal to 15% and in the poorest of these countries, the group of low income countries tax revenue was just 12% of GDP.

Tax avoidance and tax evasion are widely believed to be important factors limiting revenue mobilization. This study reviews existing empirical estimates of tax gaps, that is, tax revenue losses due to tax avoidance and tax evasion in developing countries, the role of tax expenditures, and other determinants of revenue mobilization.

Governments in most developing countries do not consider the principles of economy (Smith, 1978) in collecting tax revenues. This concept means that the cost of collecting tax such as labour cost, machinery, stationery and other tax instruments must be abridged drastically. That is, it should not be anywhere close to the tax revenue. Evidence has proven that most developing countries have high rate of tax expenditure and this reduces tax revenue immensely. The structure for tax collection must be reviewed so that tax expenditure can merely be minimized. Existing empirical studies on tax revenue losses due to tax avoidance and evasion in developing countries distinguish between a domestic component and an

international component. The domestic component includes tax evasion, which occurs due to the domestic shadowed economy. The international component includes profit shifting by corporations and off-shore holdings of financial assets, by private individuals.

The most widely cited study of the domestic component of tax evasion is Cobham (2005), who estimates that developing countries lose \$286 billion USD per year due to tax evasion in the domestic shadow economy. Cobham's calculation of the tax evasion is based on estimates of the size of domestic shadow economy by Schneider (2005). This approach has a number of limitations. Most importantly, the number derived by Cobham (2005) should not be interpreted as an increase in tax revenue, which could possibly be achieved by better tax enforcement or other policy measures.

This is not only due to the fact that it is practically impossible to tax all economic activity in the shadow economy. In addition, the measured size of the shadow economy may be the result of deliberate policy choices made by developing countries like Ghana. This would imply that paradoxically, crowding back the shadow economy may neither increase tax revenue nor be in the interest of national welfare. Secondly, shadow economy activities as quantified in Schneider's estimation include; illegal activities which would be stopped if detected and thus, would not generate tax revenue. Thirdly, measures of the shadow economy as those provided by Schneider have to be interpreted with caution. Due to estimation method used, the change of these measures over time is likely to be more informative than the change the levels of these estimates.

If estimates of level of tax evasion are based on measurement of the size

of the shadow economy, the accuracy of this measure is of key importance. Cobham (2005) relies on shadow economy estimates based on macro indicators. The approach has the advantage that the data is publicly available. We compare to other methods to quantify the (domestic) tax gap. These approaches can be broadly divided into:

- i. Macro approaches: this uses data from national accounts.
- ii. Macro indicators to quantify the tax gap.
- iii. Macro approaches: this uses household or firm level data retrieved from surveys and audits.
- iv. In general macro approaches based on information from tax audits of randomly selected tax payers are most likely to deliver reliable tax gap estimates. In contrast, methods to quantify the domestic tax gap based on macro indicators are less reliable and informative. However, data to implement a micro method is seldom available for developing countries.

#### ***Relevance of Macro and Micro Approaches in Quantifying Tax Gap***

One existing tax gap estimates for developing countries of macro indicator approach, a possible starting point to improve the information on tax gaps in a developing world would be to use macro methods based on the identification of discrepancies in national accounting data. But in the long run, an appropriate quantification of the tax gap in developing countries may be required. Research based on micro approaches, in particular methods, which rely on tax audit information collected by the national tax authorities. Firstly, this would deliver relatively a reliable tax gap estimates. Secondly, it would allow calculation of individual components of the tax group according to tax payers groups (example

is corporations vis-à-vis individuals in different income classes and sectors of activities) and the type of income which is evaded (example is income earned from international and national transactions).

The latter provides important and valuable guidance for reforms of the tax administration and the tax system in a developing country.

### *Other Studies Used To Quantify the International Components of Tax Gap*

Two groups of studies can be distinguished; The first group focuses on shifting of corporate profits out of developing countries. This activity may include both (legal but desirable) tax avoidance and tax evasion (illegal). The most influential studies in this area try to identify profit shifting by analyzing international trade policies (Ali, Cecil, & Knobletti, 2001).

The basic idea is that prices charge for goods exposed to developing countries are distorted upwards, whereas prices of goods imported from developing countries are set artificially at low levels so that income effectively generated in developing countries is shifted to the developed world. According to the studies, trade price distortion may arise with trade between both unrelated parties (where exporters and importers collide) and related parties (within multinational firms) to quantify the tax revenue which developing countries lose due to these price distortions, many studies rely on subjective evidence or non-representative survey data.

More sophisticated work in this area based on macro data for trade transactions finds some evidence on systematic price distortions. These are interpreted as reflecting shift in income from developing countries to industrialize

countries like the US and the United Kingdom. Estimate of revenue losses suffered by developing countries due to the corporate profit shifting range between approximately USD \$35 billion and USD \$160 billion per year (Hines & Rice 2004).

According to Hines and Rice (2004), the methodological weakness of the mispricing approach is that it is unclear to which extent that price differences simply reflect the quantified differences within the product group. The price pattern observed in the data may just reflect differences in the quality structure of goods produced by countries in different stages of economic development. As long as it is not possible to disentangle quality difference and income shifting, the interpretation of numbers generated by the mispricing approach is difficult.

A key short coming of many existing studies based on mispricing is that they only take into consideration overpriced imports into developing countries and underpriced exports of the developed countries. This shifts income into developing countries. Estimate of tax revenue calculations have to take into account income shifting in both directions. If only one direction is considered, the results will be highly misleading thus; tax revenue losses due to mispricing will be overestimated drastically (Prest, 2005)..

Another issue is the way existing studies of profit shifting translate their estimate of mispricing into tax revenue losses by multiplying results for income shifted out of developing countries with statutory corporate tax rate, neglects the existence of investment incentive. For example tax holidays, free enterprise zone and to mention but a few. Investment tax incentives are widely used in developing countries. For this concern, less income shifting would not necessarily increase

corporate tax revenue; part of this income would simply be tax exempt or taxable at very low rate. This aspect implies that existing studies overestimate tax revenue losses due to profit shifting.

In order to better understand the issue of price distortion and corporate income shifting, it is necessary to investigate in greater detail whether prices observed reflect quality difference or income shifting. Clearly, income shifting in both directions has to be taken into account, it takes place either through misplacing or other instruments like debt financing, it is important to investigate why income is shifted out of the developing countries. In order to use this, it would be possible to use micro data for multi-national firms operating in developing countries. Such an approach would allow investigating whether and to what extent taxation, business regulation and institutions like government structures, property rights and to name but a few, contributes to the level of tax a revenue levied from taxing firms.

A second group of international studies (Friedland, Maital, and Rutenberg, 2000; Mason R and Calvin, 2001; & Geeroms, and Wilmots, 2003) focuses on tax evasion by wealthy individuals residing in developing countries that own financial assets abroad and do not report this income in their country of fiscal residence. Estimate of tax revenue losses in developing countries caused by this type of evasion ranges between USD \$15 billion per year (this estimate refers to the 1990s) and for more recent year US \$124 billion. This estimate usually starts with rough estimate of worldwide financial assets held off-shore and then makes some adhoc assumptions on taxable returns, tax rate, and the share of overall assets owned by individuals residing in developing countries. It is difficult to

interpret the results of these calculations. In this area, there is even less data available than for the corporate sectors. So far, the scope for more informative research seems to be limited (Richard, & Oliver, 2005).

### ***Relationship between Tax Avoidance, Tax Evasion and Tax Expenditure***

In addition to tax avoidance and tax evasion, the existence of tax expenditure, in particular tax incentive for investments, is widely seen as a reason for tax revenue losses in developing countries. Unfortunately, internationally recognized similar data for this extent of existing tax expenditure is not available. Existing numbers on the volume of tax expenditure reported by various countries are not comparable because they are based on different measurement concept. While there is some evidence that the use of some of investment incentives has increased in the last decade, little is known about the impact of this expenditure on tax revenue and revenue mobilization (Wenzel, 2002).

As an overall assessment of literature on tax gap estimate for the developing world, it could be conclude that the available knowledge on tax revenue losses in developing countries caused by tax avoidance and tax evasion is very limited.

This is partly due to the lack of data and partly due to methodological shortcomings of existing studies. Some of the existing estimate of tax revenue losses due to tax avoidance and evasion by firms systematically overestimate the losses. Overall, it is fair to conclude that most existing estimate of tax revenue losses in developing countries due to evasion and avoidance are not based on methods of collecting data (Wenzel, 2002).

Moreover, it seems that too much emphasis is put on producing aggregate estimate for tax revenue losses for developing countries. Research on tax avoidance and tax evasion as well as policies to achieve more revenue mobilization should take heterogeneity into account. More research is needed to improve our understanding of tax avoidance and tax evasion and the implication of these activities for revenue mobilization in developing countries.

It is also a fact that the inappropriate use of tax expenditure reduces government revenue. Tax expenditures are widely criticized as policy instrument which lack transparency and which are difficult to control. They are thought to be vulnerable lobbying by special interest groups and even corrupt practices. Therefore strategies to control tax expenditure may be an important element in a broader strategy for improving revenue mobilization in developing countries.

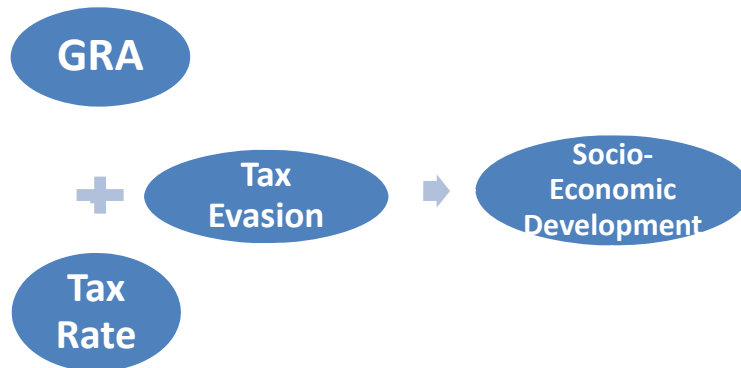
Reports have provided a survey of existing studies on tax avoidance and tax evasion as well as tax expenditures in developing countries. The existing studies are divided into two groups. The first group of studies focuses on tax evasion and tax avoidance related to domestic economic activity. The second group of studies focus on tax evasion and tax avoidance related to international economic activity (Alm & Torgler 2004).

### **Theoretical Framework**

The theoretical framework focuses on the main variable of the studies, the factor of the variable, the gathering of data, how solutions are arrived at and also the presumed relationship between them. In other words, something that explains graphically or in narrative form, the main things to be studied. The main aim of



this part is to reveal the summary of the relevant theories that was employed to conduct this research. It is also to build an appropriate framework to study the effects of tax evasion on the Ghanaian economy. For the purpose of this study, emphasis is laid on the two theories, the Expectancy theory and the Benefit theory.



**Fig. 1. Theoretical framework** (Source: Authors' construct)

Several theories of taxation exist in public economics. Governments at all levels (national, regional and local) need to raise revenue from a variety of sources to finance public-sector expenditures.

### **Expectancy Theory**

The theory proposes that an individual will behave or act in a certain way because they are motivated to select a specific behavior over other behaviors due to what they expect the result of that selected behavior will be. In essence, the motivation of the behavior selection is determined by the desirability of the outcome. However, at the core of the theory is the cognitive process of how an individual processes the different motivational elements. This is done before making the ultimate choice. The outcome is not the sole determining factor in making the decision of how to behave.

According to Montana and Charnov, (2008), expectancy theory is about the mental processes regarding choice, and the effect of the choice. It explains the processes that an individual undergoes to make choices and expected effect of the choice. In the study of National Development, Amann, (1996) used Victor Vroom of the Yale School of Management expectancy theory. "He emphasized that various governments relate infrastructural development to revenues generated.

### **The Benefit Theory**

Adam Smith in *The Wealth of Nations* (1776) wrote: "Such things as defending the country and maintaining the institutions of good government are of general benefit to the public. Thus, it is reasonable that the population as a whole should contribute to the tax costs. It is also reasonable to demand certain other things of a tax system – for example, that the amounts of tax individuals pay should bear some relationship to their abilities to pay. Good taxes meet four major criteria. They are (1) proportionate to incomes or abilities to pay (2) certain rather than arbitrary (3) payable at times and in ways convenient to the taxpayers and (4) cheap to administer and collect."

In modern public-finance literature, there have been two main issues: who can pay and who can benefit (Benefit principle). Influential theories have been the ability theory presented by Arthur Cecil Pigou and the benefit theory developed by Erik Lindahl. There is a later version of the benefit theory known as the "voluntary exchange" theory.

Under the benefit theory, tax levels are automatically determined, because taxpayers pay proportionately for the government benefits they receive. In other

words, the individuals who benefit the most from public services pay the most taxes. Here, two models adopting the benefit approach are discussed: the Lindahl model and the Bowen model.

Lindahl tries to solve three problems:

1. Extent of state activity
2. Allocation of the total expenditure among various goods and services
3. Allocation of tax burden

In the Lindahl model, if SS is the supply curve of state services it is assumed that production of social goods is linear and homogenous. DDa is the demand curve of taxpayer A, and DDb is the demand curve of taxpayer B. The vertical summation of the two demand curves results in the community's total demand schedule for state services. A and B pay different proportions of the cost of the services. When ON is the amount of state services produced, A contributes NE and B contributes NF; the cost of supply is NG. Since the state is non-profit, it increases its supply to OM. At this level, A contributes MJ and B contributes MR (the total cost of supply). Equilibrium is reached at point P on a voluntary-exchange basis.

### **The Ghana Revenue Authority (GRA)**

The Ghana Revenue Authority (GRA) is a modern tax administration established by the Ghana Revenue Authority Act 2009 (Act 791) and charged with the task of assessing, collecting and accounting for tax revenue to the state. The core mandate of the Authority is to ensure maximum compliance with relevant laws in order to ensure a sustainable revenue stream for government as

well as the controlled and safe flow of goods across the county's borders. As part of efforts to improve compliance, the Authority is required to assist taxpayers to understand and meet their tax obligations by providing robust and comprehensive advice.

In the seven years since its inception, GRA has built a solid foundation in the integration of the three erstwhile revenue institutions namely the Customs, Excise and Preventive Service (CEPS), the Internal Revenue Service (IRS), the Value Added Tax Service (VATS) and the Revenue Agencies Governing Board (RAGB).

### **Tax Rate**

The Personal Income Tax Rate in Ghana stands at 25 percent. Personal Income Tax Rate in Ghana averaged 25.00 percent from 2006 until 2016, reaching an all-time high of 25.00 percent in 2007 and a record low of 25.00 percent in 2007. In Ghana, the Tax Rate is a tax collected from businesses and individuals and is imposed on different sources of income like labor, pensions, interest and dividends. The benchmark we use refers to the Top Marginal Tax Rate for individuals. Revenues from the Personal Income Tax Rate are an important source of income for the government of Ghana. This page provides - Ghana Personal Income Tax Rate - actual values, historical data, forecast, chart, statistics, economic calendar and news.

### **Tax Evasion**

Ghana's development is undermined by tax evasion, as colossal millions of Ghana cedis are being invaded by some companies and individuals in the country. These tax evaders take advantages of that loop-holes in the country's revenue mobilization system to steal revenue which could have gone in the provision of basic amenities in the country.

It cannot be denied that there are lapses and leakages in our revenue collection system as well as under invoicing and under declaration at almost all our revenue collection points, e.g. our ports, borders, airport and even our road tolls are not excluded.

#### **a. Tax Evasion and Productivity**

Since independence, many multinational corporations including oil companies (like shell Ghana limited, Benso oil palm plantation limited, star oil company limited, etc) have been in operation in different parts of Ghana where they make huge profit every year. These companies have their head offices in developed countries which are their countries of origin. These companies may be deriving their main revenue from their respective branch offices but the governments of their countries require them to file and pay personal and corporate taxes at the end of every trading period (MaxCorrol, 2009). This leads to double taxation; therefore they try to avoid and evade tax liabilities in Ghana by taking advantage of the tax system. This has a devastating consequence on Ghanaian economy and created unnecessary poverty, hunger, and dispossession among Ghanaian masses.

Researches on tax evasion have shown that domestic, multi-national and

private businesses have reduced government revenue in various ways by avoiding and evading tax.

Some of the common ways are as follows:

- a. Keeping two set of records for business transaction, one records the actual business and the other contain false records.
- b. Barter trade where payments are made in kind instead of money is not accounted for.
- c. Nondisclosure of major sources of income and vital information about their earnings.
- d. Submitting false statements on returns to GRA and other revenue agencies with sole aim of reducing tax liability.

#### **b. Tax Evasion and Performance**

Tax evasion affect the extent to which the government can provide basic needs of the population and the obvious effect is deplorable infrastructure condition (Bakare, 2006). The education sector in Ghana has performed poorly in most rural areas who cannot afford conducive environment for teaching the pupils. According to Viasat News (2011), pupil's of some villages in the Central, Northern and Volta regions attend their classes under trees. There is no adequate educational facility. The health sector also suffers a lot because there is no adequate facility to aid the health sector. This is because the less privileged do not have adequate access to health facilities.

## **CHAPTER THREE**

### **RESEARCH METHODS**

#### **Introduction**

This chapter gives a description of the methods as well as instruments employed in conducting the research. It presents the research design, sources of data, description of the target population, sample and sampling techniques, the

instruments employed in collecting the data, data analysis techniques and the profile of the metropolis under study.

### **Research Design**

Research design deals with the type of research and the procedure for carrying out data collection and analysis. It thus gives a general plan of how research questions will be answered. This study adopted the case study research strategy. Robson (2002: 178) defines case study as a “strategy for doing research which involves an empirical investigation of a particular contemporary phenomenon within its real life context using multiple sources of evidence”. The case study is an examination of tax evasion and its effects on the Ghanaian economy with evidence from the GRA in the Cape Coast Metropolis of Central Region. Out of the various research strategies, the researcher found the case study approach to be the most appropriate for achieving its objectives in that this very approach has a considerable ability to generate answers to the question ‘why’ as well as ‘what?’ and ‘how?’ questions. According to Eisenhardt and Graebner, (2007), a case study strategy is relevant to gain a rich understanding of the context of the research and the processes being enacted.

However, the study blended both the qualitative and the quantitative methods in both data collection and analysis in getting to the bottom of issues. This study used statistics from GRA, interviews and questionnaire in arriving at the collection of data. Case study approach is characterized by data triangulation. According to Saunders et al., (2007), triangulation refers to the use of different data collection techniques within one study in order to ensure that the data are



telling you what you think they are telling you. For example, qualitative data collected using semi-structured interviews may be a valuable way of triangulating quantitative data collected by other means such as questionnaire.

### **Population of the Study**

Just like every research, the study could not be complete without a target population. As such the target population for this study were personnel from the Ghana Revenue Authority, businesses and the individual business persons (self-employed) in the Cape Coast Metropolis basically traders, artisans in the likes of hairdressers/barbers, fashion designers, carpenters, fitters, and masons among others.

### **Sampling Techniques**

According to Saunders et al. (2007), sampling technique enables a researcher to reduce the amount of data he/she needs to collect by considering only data from a subgroup rather than all possible cases or elements. In view of this, the researcher used the Convenience sampling technique, to select the various traders, artisans and the GRA staff who formed the respondents for the study.

The Convenience sampling method used in selecting participants for the study was motivated by the fact that it would have been quite difficult to obtain the list of all traders and artisans since the population of the metropolis was scattered. Even if that was possible, locating all traders and artisans who would be

selected would have been a daunting task to execute. It was on this basis that the Convenience sampling method was used for the study.

### **Sample Size**

For the purpose of this study, the entire population could not have been reached within the time this study was supposed to be completed. There was therefore the need to select a sample. A sample is a finite part of a statistical population whose properties are studied to gain information about the whole. The researcher therefore conveniently selected one hundred and twenty individual business persons (out of 639 total number of businesses registered at the GRA in 2016) and 5 GRA staff, to form the sample size of the study. The researcher also used raw statistical data of of businesses registered at the GRA from 2014 to 2016.

### **Data Collection Instrument**

For the data collection, researcher took a letter of introduction (see Appendix D) from the Department of Accounting, College of Humanities and Legal Studies, University of Cape Coast. With the letter, permission was sought from the Director of Ghana Revenue Authority in the Cape Coast Metropolis to solicit the relevant information and to interview the officials selected to form parts of the sample size. This helped me to get the necessary assistance needed from the official respondents. With the letter of introduction, the researcher was offered all the raw statistical data and the assistance required to complete the study.

The main research instrument used to collect data for the study consisted of raw statistical data from the GRA and questionnaires. A questionnaire includes all methods of data collection in which each person is asked to respond to the same set of questions in a predetermined order (deVaus, 2002).

The self-completed questionnaire, which is usually completed by the respondents was used but then those who could not complete it by themselves due to the level of literacy or any other reason were assisted by the researcher upon request. Under this type the delivery and collection of questionnaires was done by the researcher herself.

### **Ethical Consideration**

The ethical dimensions of every research and how it would be addressed is imperative to talk about. This research took into accounts the issues of informed consent, anonymity and confidentiality. Neuman (2007) posits that researchers must not compel anyone into participating in research. Participation must be voluntary at all times. The researcher made telephone calls and prior visits to management of GRA and made data gathering periods scheduled at convenient hours in that there were no undue interruption of their work. The purpose of the study was explicitly made known to them but respondents who declined participation were not forced or coerced to doing so.

Secondly, the issue of anonymity were not compromised. Anonymity protects privacy by not disclosing a participant's identity after data is gathered. Respondents were assured of their anonymity since names and other personal

details were not associated with specific responses given. For this study, respondents were assured of their confidentiality. The information they provided

### **Profile of the Study Area**

The Cape Coast Metropolitan Assembly is one of the seventeen (17) districts of the Central Region of Ghana. Its capital is Cape Coast, which is also the capital of the Central Region. Cape Coast Metropolitan Assembly is bordered by the Gulf of Guinea to the south, Komenda/Edina /Eguafo/Abirem Municipal Assembly to the west, Abura/Asebu/Kwamankese District to the east and Twifo/Heman/Lower Denkyira District to the north. The Metropolis occupies an Area of approximately 122 square kilometres, with the farthest point at Brabadze, about 17 kilometres from Cape Coast, the capital of the Metropolis, and the Central Region.

The Cape Coast Metropolitan Assembly (CCMA) was established under the Local government (Cape Coast District Assembly) establishment Instrument, 1988 and operates under the Local Government 1993 (Act 462). It is the highest political and administrative authority in the Metropolis. The political and executive head of Assembly is the Metropolitan Chief Executive (MCE). He/she is under Section 20 (2) of Act 462, the chairman of the executive Committee of the assembly. He/she is responsible for the day-to-day performance of the executive and administrative functions of the assembly and responsible for the supervision of the departments of the assembly. He/she is also the chief representative of the Central Government in the Metropolis. The Metropolitan

Coordinating Director (MCD), who is the Head of Civil Service in the Metropolis, assists the MCE in the day-to-day administration of the Assembly.

The population of the Cape Coast Metropolis was 56,123 in 1960 and 69,795 in 1970, giving an inter-censal increase of 29.40%. In 1984 and 2000 the population increased again to 89,477 and 128,106 respectively, indicating a substantial increase of 39.9% for the 14-year period. The population grew at a rate of 2.5% between 1960 and 1970, dropped sharply to 1.9% between 1970 and 1984 and then rose to 2.4% between 1984 and 2000. The population of the Metropolis according to the 2010 population and housing census was estimated to be 148,246.

The major economic activities in the metropolis are fishing, farming and small scale processing of agricultural produce as well as petty trading like hair-dressing, tailoring, carpentry and masonry. The agricultural sector (fishing and farming) employs over 40% of the active population, commerce 20%, manufacturing (industry) 15% and service about 10%. Orange is a major cash crop cultivated in the metropolis. The major food crops cultivated in the metropolis include cassava, maize, yam, cocoyam and vegetables.

### **Data Analysis**

The data was analyzed using simple frequency count for groups of opinions observed. Information about items with similar occurrences was gathered and percentages of the frequencies calculated. The researcher keyed the responses into a data processing device, then through the Statistical Product and

Service Solutions (SPSS) software, a detail analysis enabled the researcher to develop the results and findings of the study.

Codes were assigned to both the open ended and close ended items in the questionnaires and the interview guide after editing. The editing stage gave an opportunity for checking whether respondents had answered all questions. Responses from the research tools, both open- and closed-ended and those from the interview guide, were tallied and counted according to themes. All the results were analyzed using charts and frequency distribution tables.

## CHAPTER FOUR

### RESULTS AND DISCUSSION

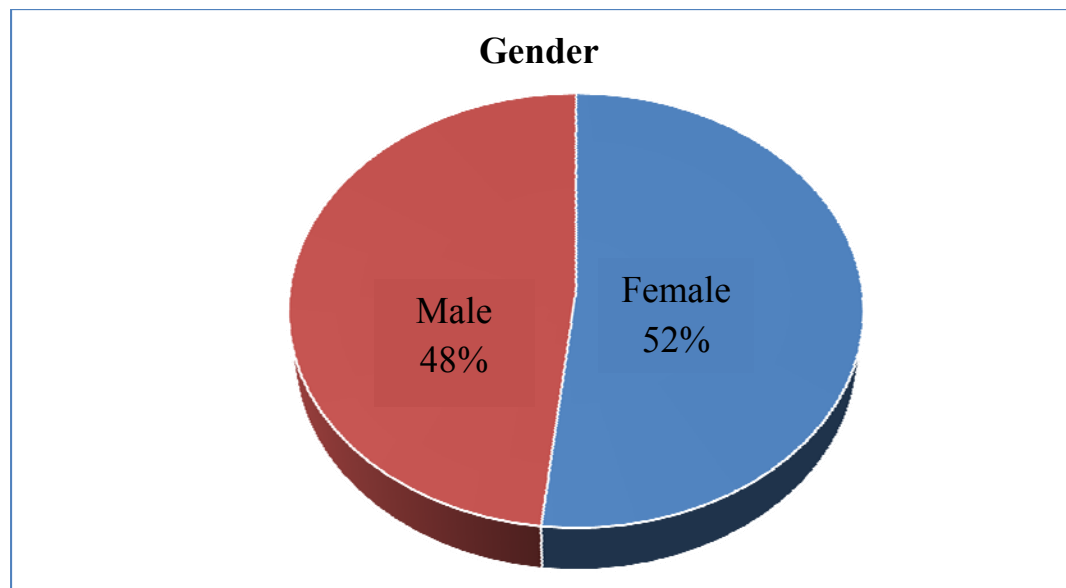
#### Introduction

This chapter is concerned with the data presentation and discussion of the results obtained from the field of study. Charts and tables were used to analyze the data that was obtained from the questionnaire. In all, 120 sets of questionnaire were administered to respondents out of which 95 were returned for analysis.

#### Responses from Tax Payers

##### Gender Distribution of Tax Payers

Figure 2 below shows that 41 (48%) of the tax payer were males and the rest 44(52%) of the tax payers were females.

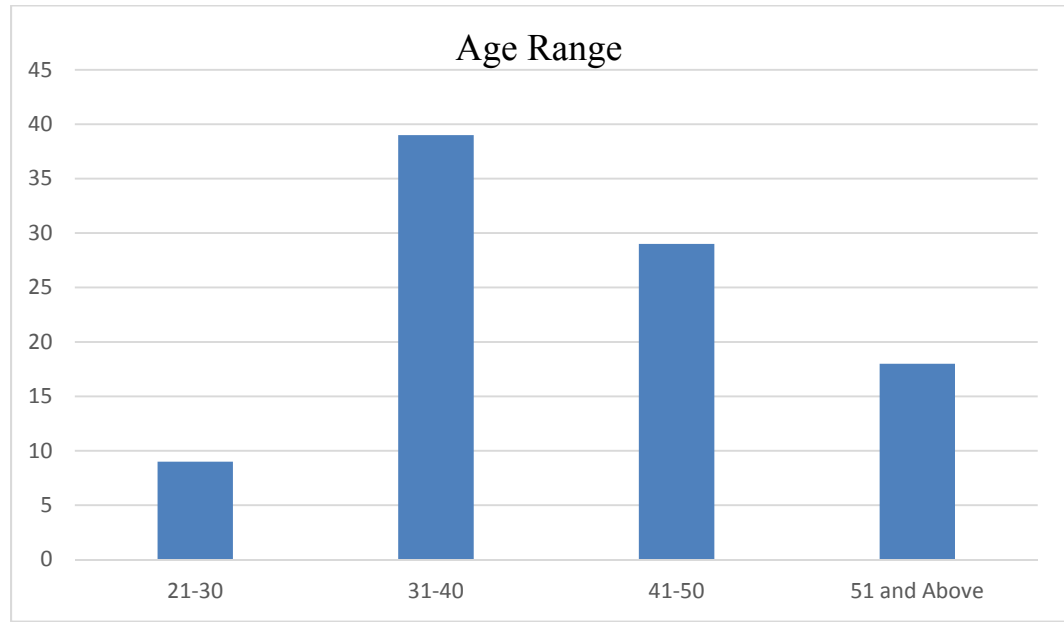


**Figure 2: Gender Distribution of Tax Payers**

Source: Field Survey, Essilfie-Afful (2017)

##### Age Distribution of Tax Payers

Age composition of tax payers was relevant in such a study. It helped in the determination of largest age group. Figure 3 gives the age range of the respondents.



**Figure 3: Age Distribution of Tax Payers**

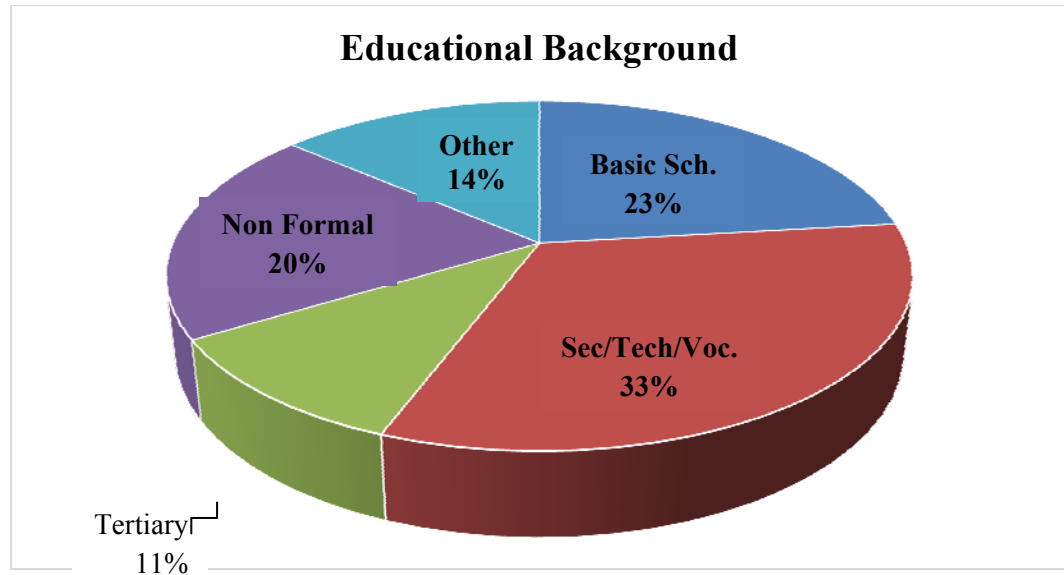
Source: Field Survey, Essilfie-Afful (2017)

The researcher sought to find out the age distribution of the tax payers and the results depict a different age composition of tax payer respondents. Figure 3 of the study revealed that 9 (9.5%) of the tax payers were within the age range of 21-30 years of age. Also, 39 (41%) of the tax payer respondents fall within 31-40 years whiles 29 (30.5%) of the tax payers fall between 41-50 years. However, 18 (19%) of the tax payers were within the category of 51years and above.

From Figure 3, it could be observed that 9.5% of the tax payers fall within the ages of 21 to 30years. This represents the youth who have either completed school and have started businesses on their own or those that have completed



apprenticeship and have started their own business. The majority of the tax payers fall within ages of 31-50 years representing 71.5%. This undoubtedly represents the matured men and women who are entrepreneurs in their own small businesses. Also, 19% of the tax payers who are 51 years and above are possibly the old aged businessmen and women in the Cape Coast Metropolis.



**Figure 4: Educational Background of Tax Payers**

Source: Field Survey, Essilfie-Afful (2017)

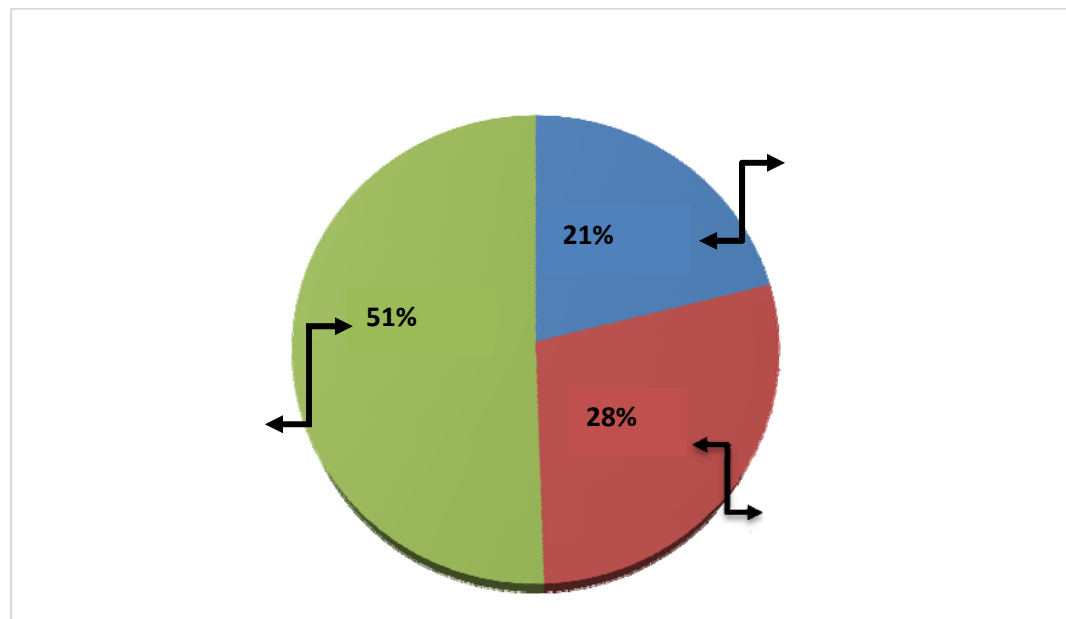
It could be observed that 23 percent of the tax payers indicated they have had basic school education. It was again clear that 33 percent of the tax payers have had SHS, technical and/or vocational training. Significantly, 11 percent of tax payers indicated they have had tertiary education. Also, 20 percent of tax payers indicated they have had no formal education. Then again, 14 percent of the tax payers fell within other level of education specifically, middle school leavers.

This implies that the 11% of the respondents who have had tertiary education and perhaps the 33% who also have received secondary, technical and/or vocational training may have the theoretical knowledge and understanding

in taxation and as such the issue of tax avoidance/evasion. Therefore, almost 56% of the respondents are likely to have little or no knowledge on taxation and tax evasion, aside what they may have heard in the news or from friends and coworkers. This has a greater influence with respect to issue of tax evasion.

### Type of Business Engaged in by Tax Payers

Here the researcher sought to establish the type of businesses engaged in by the respondents. The following results were obtained and presented in figure 5.



**Figure 5: Type of Business Engaged in by Tax Payers**

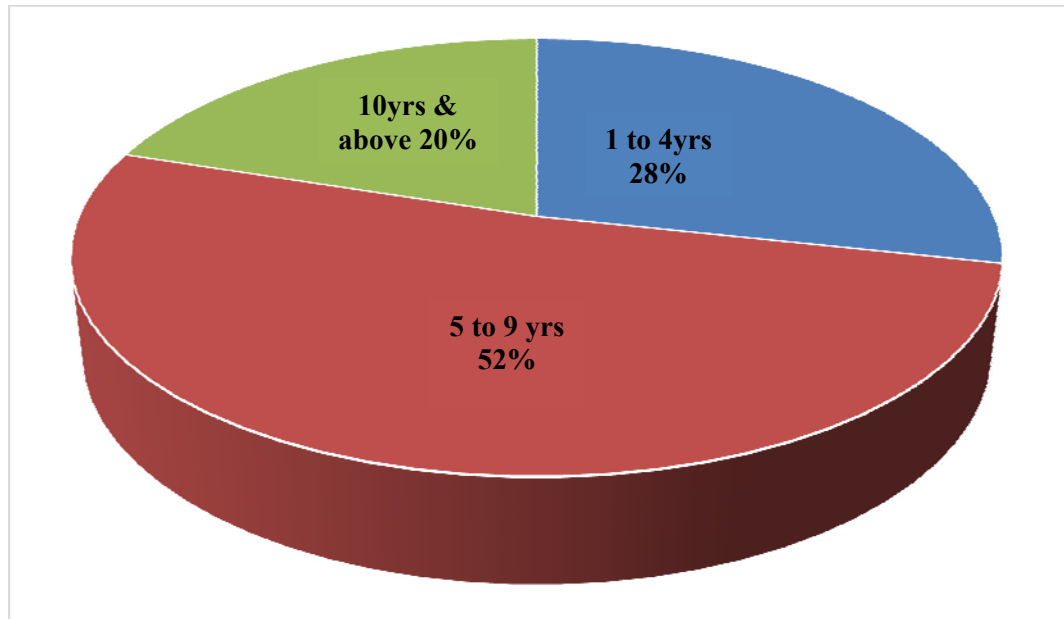
Source: Field Survey, Essilfie-Afful (2017)

From the Figure 5 above, 20 tax payers representing 21% of the total tax payers were engaged in the manufacturing of goods ranging from sachet water, carrier (take away) bags, packaged drink etc, with 27 tax payers representing 28%

involved in service oriented business. Respondents that were involved in distribution and retailing were 48 representing 51% of the tax payers.

### **Period that Tax Payers have operated so far**

The researcher sought to find the length of time the tax payers have been in business in the Metropolis. The responses have been represented in Figure 6



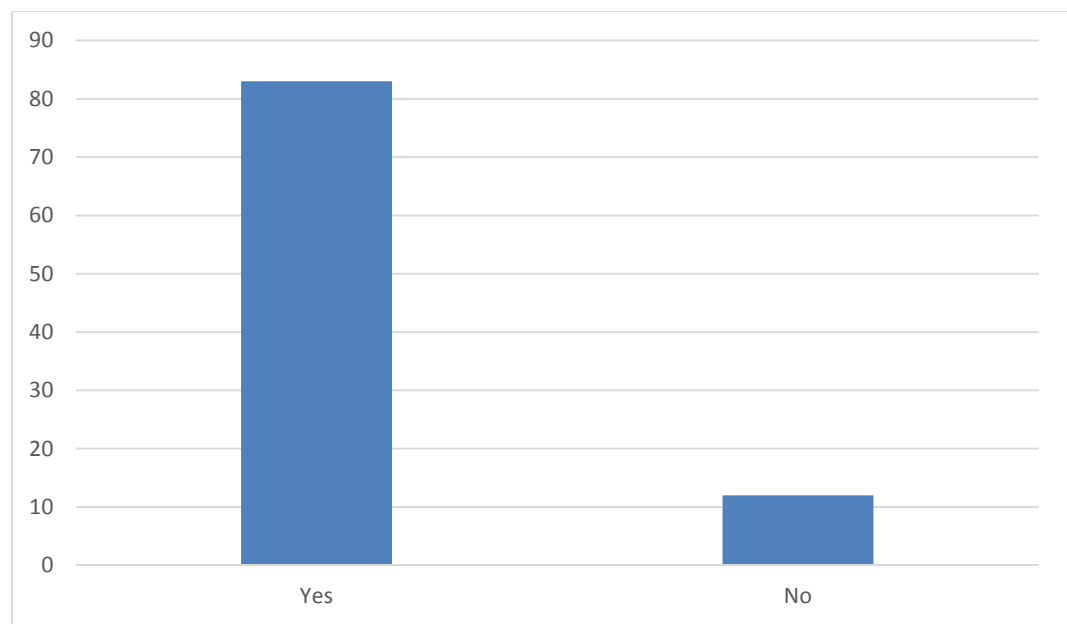
**Figure 6: Period that tax payers have been in business**

Source: Field Survey, Essilfie-Afful (2017)

Figure 6 shows that 27 respondents representing 28% of the total respondents have operated in the Metropolis between 1 to 4 years. 49(52%) respondents have operated in the Metropolis between 5 years to 9years. Also 19 respondents representing 20% of the total number of respondents have been doing business for 10 years and above in the Metropolis. However, none of the participant had operated less than one year.

### Respondents' awareness of the need to declare their interest to GRA

The respondents were then asked about their awareness to the declaration of their income to the Ghana Revenue Authority. Their responses have been presented in the Figure 7 below.



**Figure 7: Awareness of the need to declare their interest to GRA**

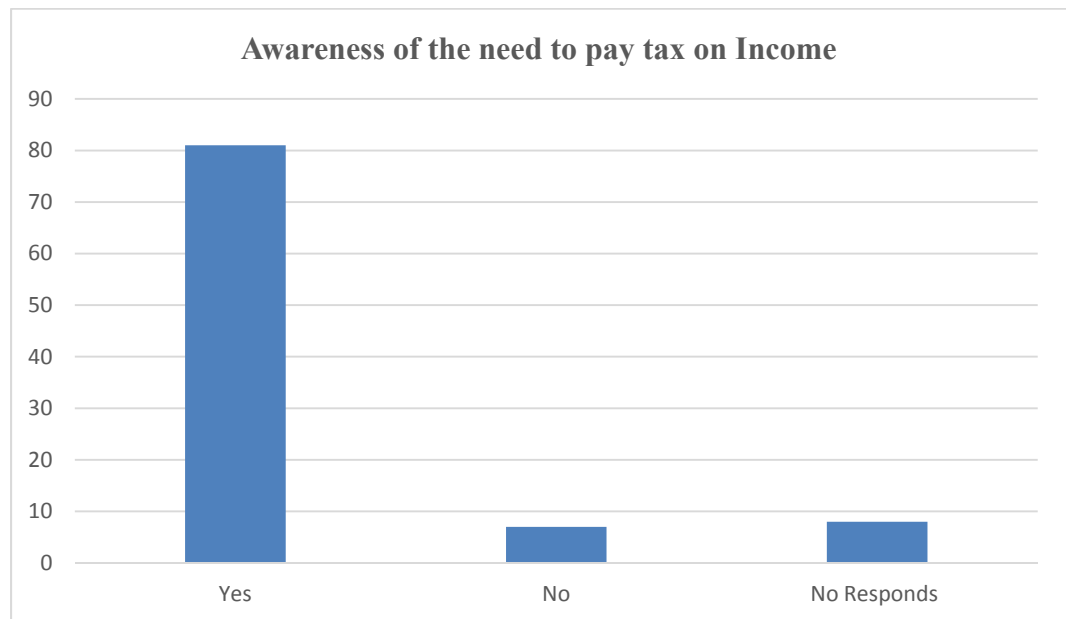
Source: Field Survey, Essilfie-Afful (2017)

From Figure 7, it could be observed that the majority (87%) of the respondents out of the total respondents indicated they are aware that they are to declare their income to the Ghana Revenue Authority while the remaining 12 respondents representing 13% of the total respondents indicated they have no idea as to whether they should declare their income to the Ghana Revenue Authority.

This result goes a long way to influence the tendency of tax evasion/avoidance. This is because those that are aware of the need to declare their income to Ghana Revenue Authority would know about tax payment and its importance.

### **Tax payer awareness of the need to pay tax on Income Generated from Business**

The respondents were asked whether they were aware of the duty to pay tax to the Ghana Revenue Authority. The responses obtained from the questionnaire are represented in the Figure below.



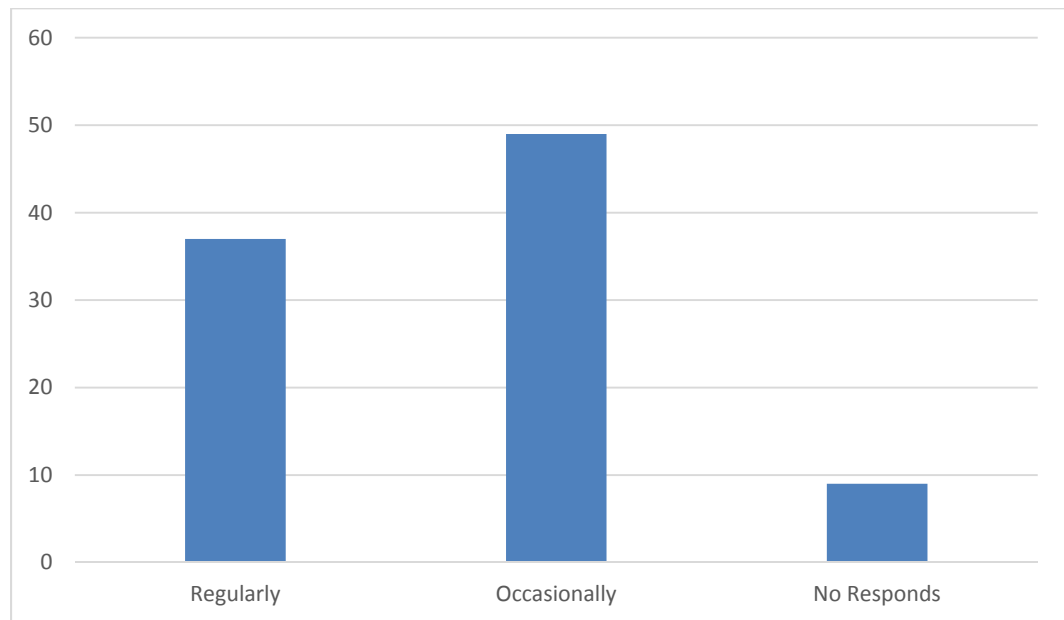
**Figure 8: Tax payer awareness of the need to pay tax on Income Generated from Business**

Source: Field Survey, Essilfie-Afful (2017)

Results in Figure 8 show that 81 respondents representing 85.3% of the total respondents for the study indicated their awareness of the duty to pay tax on the income they generate from their business. However, 7 respondents

representing 7.4 % of the total respondents indicated they do not know that they have to pay tax on the income they generate from their business.

This was unanticipated taking into consideration the fact that a 39% of the respondents were not aware of their obligation to declare their income to the Ghana Revenue Authority but interestingly know of their duty to pay tax. Perhaps this happens because revenue or tax collectors are always seen in markets collecting taxes mostly from the retailers. Again, most tax officials are mostly concerned with only letting these sellers and operators know of their duty to pay tax and not necessarily their obligation to declare their income to GRA.



**Figure 9: Rate of Tax Compliance**

Source: Field Survey, Essilfie-Afful (2017)

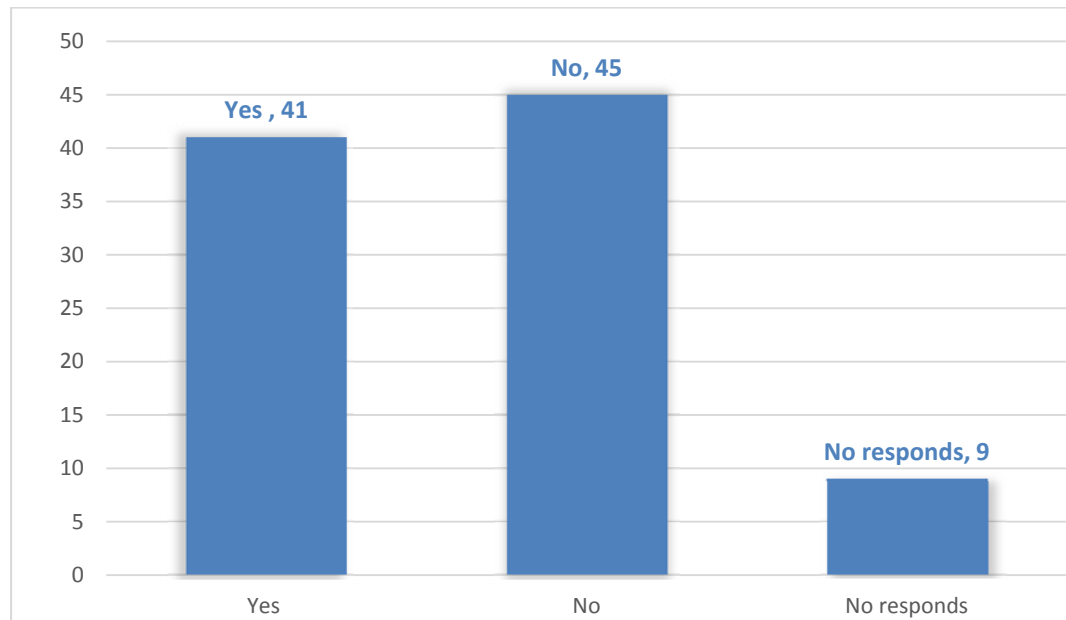
The results from Figure 8 show that respondents numbering 37 representing 38.9% indicated they pay their tax regularly with the remaining 51.6% responding that they pay it occasionally. The respondents who indicated

they pay their tax occasionally made it clear that the tax officials rarely come to collect the taxes and that contributes to their occasional payment of the taxes. According to them, if the tax officials regularly locate them, they would pay their due tax.

The 7 tax payers who responded no to the fact that they do not know that they are obliged to pay tax on what they generate from their business explained that their businesses are small and as such feel they are not taxable.

### Records of Tax Evasion

The researcher sought to inquire from respondents whether they have ever evaded tax. Their responses are presented in the Figure 10



**Figure 10: Records of Tax Evasion**

Source: Field Survey, Essilfie-Afful (2017)

The results from Figure 10 show that 41 respondents representing 43% of the tax payers sampled said they have evaded tax in one way or the other. Again, 45 respondents representing 447% said they have not evaded tax before. While the remaining 9 respondents did not provide responds to this item. Thus, they could not specifically say whether they have evaded tax before or not in that they cannot recall all their contacts with the officials. It can thus be resolved that about half of the total respondents do not regularly pay taxes in the Metropolis. This is obviously a worrisome situation for the Ghana Revenue Authority.

**Table 1: Perception of the current tax rate**

<b>Responds</b>	<b>Frequency</b>	<b>Percentage %</b>
Very High	47	49.5
High	22	23
Very low	9	9.5
Low	17	18
<b>Total</b>	<b>95</b>	<b>100</b>

Source: Field Survey, Essilfie-Afful (2017)

Table 1 clearly indicates that only 9(9.5%) of the respondents perceived the tax rate to be very low. This can convincingly imply that as no one would embrace the idea of paying so much tax to the government’s revenue collecting agencies. Also, 22 respondents representing 23% perceived the tax rate as high. These respondents were of the view that since the country is facing economic challenges, the citizens need to pay taxes to help the government provide the



needs of the people and get the economy on its toes. However, 47 of respondents representing 49.5% perceived the tax rate to be too high. Those that are of the view that the tax rate is high gave such reasons that they do not see accompanying benefits derived from the payment of tax and the rate therefore is high. Others also compared the tax rate in Ghana to other countries in similar economic situations and responded that the rates in Ghana are too high. Most of these respondents would probably evade taxes with the least opportunity available.

### **Respondents Perception on why people evade taxes**

This section presents an analysis on the respondents perception on why people evade/avoid taxes. The results are presented in the table below.

**Table 2: Perception on why people evade taxes**

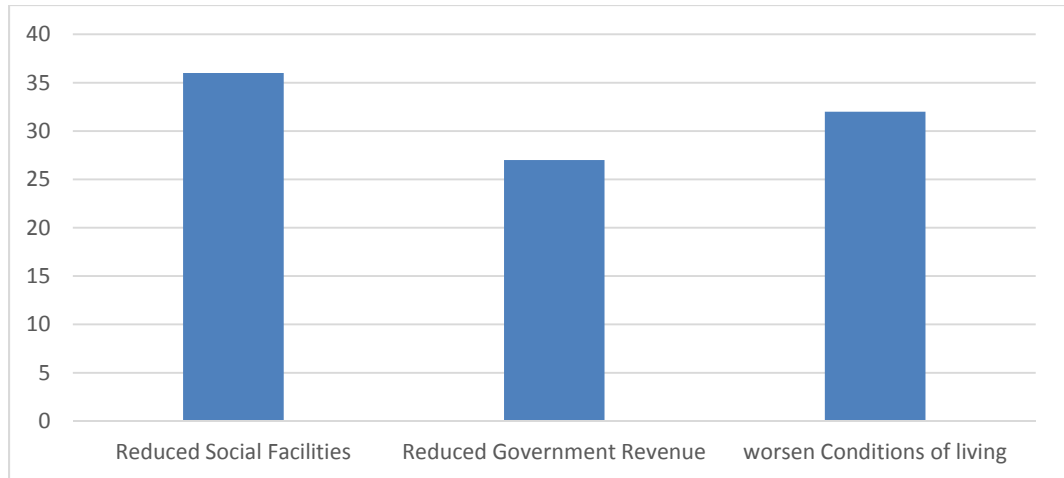
<b>Responds</b>	<b>Frequency</b>	<b>Percentage %</b>
People are not aware they are to pay tax	13	13.7
People intentionally/deliberately evade tax	14	14.7
Other people consider tax too high	27	28.4
People are tempted to evade tax because business not profitable	19	20
Proximity of business location to tax offices makes paying tax difficult	-	-
Lack of trust for the use of income tax by government	22	23.2
<b>Total</b>	<b>95</b>	<b>100</b>

Source: Field Survey, Essilfie-Afful (2017)

Results from Table 2 indicate that 13(13.7%) of the respondents were of the view that people involuntarily evade taxes because they are unaware of their duty to pay tax. This is in line with the earlier responses of some of the respondents that they are not aware of their duty to pay tax. Again, 14 respondents representing 14.7% confirmed that people deliberately/intentionally evade taxes for reasons of greed and the corruption that have engulfed the country. Again, 27 respondents representing 28.4% of the total respondents responded that people evade taxes due to the high tax rate in the country. They were of the view that if the tax rates were to be low and manageable, people would easily comply and pay them. Furthermore, 20% of the total respondents said people evade taxes probably because business is not profitable and as such they see no reason in paying taxes out of that low income. Lastly, 23.2% of total respondents were of the view that people evade taxes for lack of trust for government use of the income tax. This claim cannot be entirely substantiated because there is no concrete grounds that such claims could be established in totality, although respondents made the claim on the basis that they do not enjoy certain basic amenities and their standard of living is very low. They are of the view that government is misusing the tax payers' money.

### **Perception of the effect of Tax Evasion on the economy**

The respondents were asked to give their brief opinion about the effect of tax evasion/avoidance, given their knowledge on the importance of tax payment to the development of the economy. The Figure 11 below represents their responses.



**Figure 11: Respondents Perception of the effect of Tax Evasion on the economy**

Source: Field Survey, Essilfie-Afful (2017)

From Figure 11, 37.9% of the respondents admitted that tax evasion will hinder or reduce the provision of social amenities enjoyed by citizens because the government will not get enough revenue to provide such amenities. Again, 28.4% of the respondents are of the view that tax evasion will reduce government revenue while 33.7% of the respondents also admitted that tax evasion will consequently lead to high cost of living. This means that all the respondents were aware of the damning effects of tax evasion to the development of the nation.

### **Interview with GRA director in the Cape Coast Metropolis**

This section presents the major responses from the managing director of the GRA in the Cape Coast Metropolis who was interviewed, and the documents that were made available for the researcher. The section involves results of the

interview with the GRA boss and the analysis of the raw data retrieved from the GRA Office.

### **Response to Length of stay in the Metropolis**

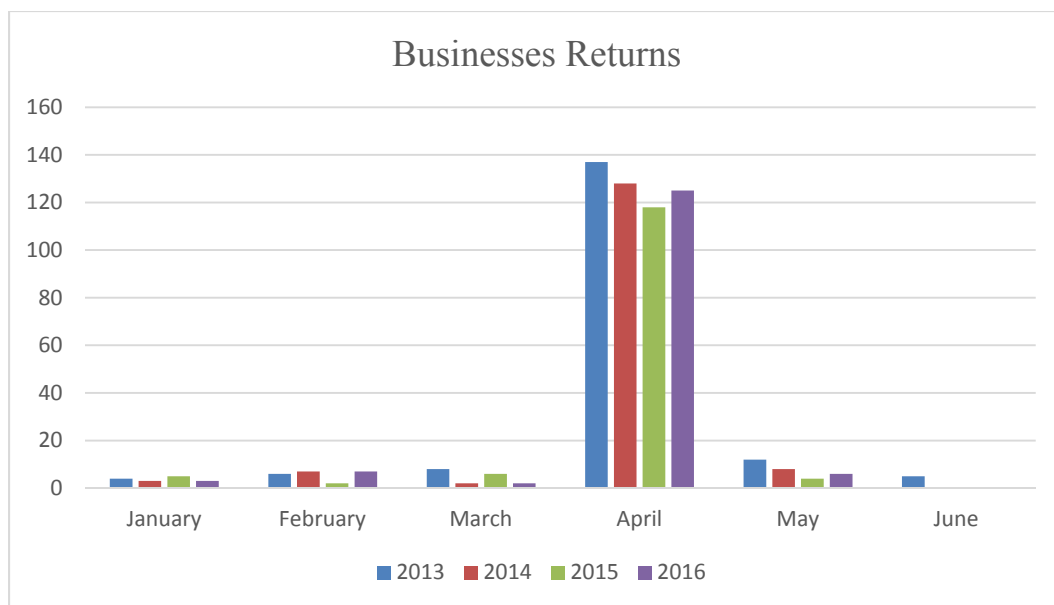
The researcher sought to find out how long the GRA boss has been in the metropolis. He indicated he has been in the metropolis for almost 6 years. His length of stay in the Metropolis is significant enough being the boss, he is perceived to have a fair idea of the compliance level in the Metropolis. He is perceived to have acquired the requisite experience and are knowledgeable enough in the matters of interest to the study.

### **Response to Compliance level in the Cape Coast Metropolis**

When asked whether people evade tax in the metropolis, he indicated that the compliance level in the metropolis was average.

### **Compliance by Businesses**

Statistics of the number of companies and individuals (self-employed) within a four year period was retrieved to determine the compliance level of the period under review (see Appendix D). Below is a graphical representation of compliance by businesses and individuals in the metropolis.



**Figure 12: Business returns for the years ending April 2013 to 2016**

**Source: Statistics from GRA, (End of year report 2016)**

Source: Fieldwork, 2017

**Table 3: Annual Businesses Returns as per the number of Businesses Registered within the period under review**

Filling of returns	Period under review							
	2013	%	2014	%	2015	%	2016	%
No. of Returns	172	32.3	148	35.2	135	37.8	143	43.5

**Source: Statistics from GRA, (End of year report 2016)**

Table 3 present statistics of registered businesses within the period under study and the compliance of their tax obligations by filling of their returns. Table 3 shows that only 172 representing 32.3% filed their returns as at June 2013. Again in 2014, a total of 148 (35.2%) duly filed their returns. The figure reduced

in quantum by May 2015, only 135 had filed their returns. In 2016, however, 143 duely filed their returns.

The results of the statistics clearly show that compliance level in the Metropolis is below average compared to how the tax officials described the situation.

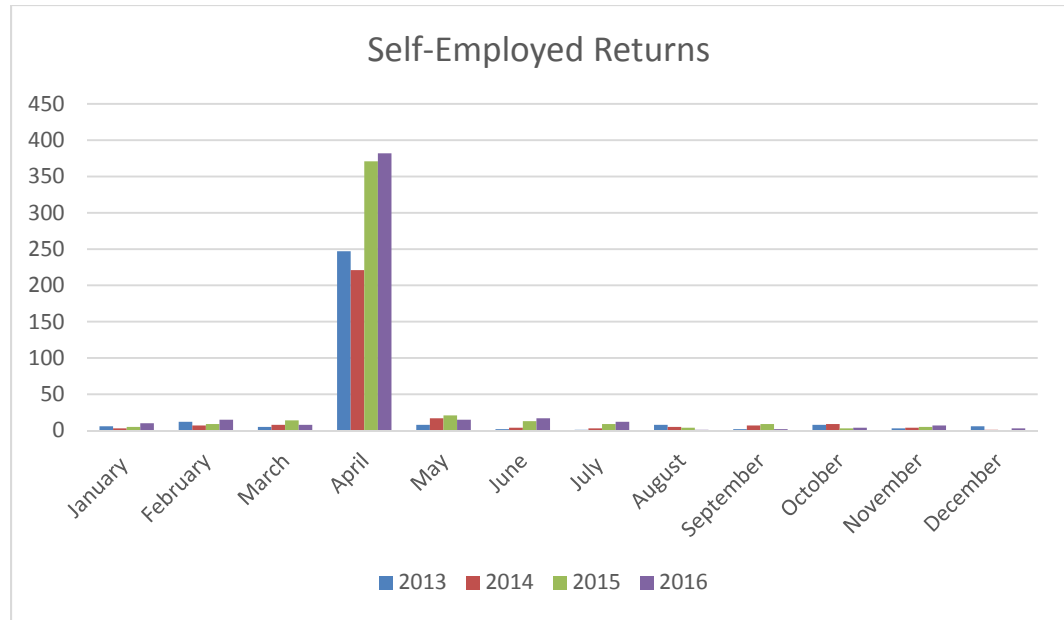
**Table 4: Businesses that Registered but did not file returns within the period under review**

Evaders	Period under review							
	2013	%	2014	%	2015	%	2016	%
No. of Evaders	360	67.7	273	64.8	222	62.2	186	56.5

**Source: Statistics from GRA, (End of year report 2016)**

Table 4 present statistics of businesses that registered but failed to file their returns within the period under study. Table 4 shows that out of the 532 businesses that registered in the year 2013, as high as 67.7% did not file their returns. Again in 2014, 64.8% of the 421 rgistered businesses did not file their returns. In 2015, the businesses that were registered were 357 but 62.2% did not file their returns. In 2016, however, the total number of businesses that evaded tax were 56.5% of the 329 registered businesses.

The results of the statistics clearly show that compliance level in the Metropolis is below average compared to how the tax officials described the situation.



**Figure 13: Individual (Self-Employed) Returns for the years ending April 2013 to 2016**

Source: Statistics from GRA, (End of year report 2016)

**Table 5: Annual Self-Employed Returns as per the number of Self-Employed Individuals Registered within the period under review**

Filing of returns	Period under review							
	2013	%	2014	%	2015	%	2016	%
No. of Returns	308	55.9	289	54.7	463	75	476	74.4

Source: Statistics from GRA, (End of year report 2016)

Similarly, Table 5 present statistics of registered individuals(self-employed) business men and women within the period under review and the compliance of their tax obligations by filling their returns on time. Table 4 shows that a significant number 308 individual business persons filed their returns as at December 2013.

Unlike the businesses, in 2014 the total of 289 individuals(self-employed) business men and women had duly filed their returns. Subsequently the figure increased in quantum in 2015, 463(75%) individuals(self-employed) business men and women had duly filed their returns by December. In 2016, however, the total number of individuals(self-employed) men and women who had duly filed their returns were 476 in December.

Unlike the businesses, the statistics on individuals(self-employed) business men and women compliance is a true reflection on the responses from the tax officials on the compliance level in the metropolis. This is a clear indication that the compliance level in the metropolis is average as suggested by the tax officials. The results again suggest in affirmation that a significant number of companies and individual business men and women in the metropolis evade/avoid taxes.

**Table 6: Annual Self-Employed Individuals who failed to file their returns**

Individual	Period under review							
	2013	%	2014	%	2015	%	2016	%
No. of E vaders	243	44.1	239	45.3	155	25	163	25.6

**Source: Statistics from GRA, (End of year report 2016)**

Table 6 present statistics of individuals(self-employed) business men and women that who failed to file their returns within the period under study. The table shows that 243 individuals(self-employed) business men and women did not file their returns in 2013. Again in 2014, 239 individuals(self-employed) business men and women did not file their returns. In 2015, the individuals(self-employed)



business men and women who did not file their returns were 155. In 2016, however, the total number of individuals(self-employed) business men and women that evaded tax were 163.

The researcher then asked the GRA boss why he think people evade tax and his thought as to what brings about tax evasion. He stressed that some people evade tax deliberately while others evade tax because of their unawareness of their obligation to pay tax. Again, he answered that others evade tax because tax officials are not able to reach them, owing to the fact that the officials are not many and not resourced enough that makes their work very tedious hence their inability to reach all tax payers.

Further responses were that other tax payers also pretend not to be the owners of the various businesses and always claim they are caretakers in order to prevent tax officials from holding them responsible for tax evasion. Besides, most business owners gave excuses that the problems of the current economy and power crisis make it difficult in recording profits and hence virtually unlikely for them to continue paying taxes.

The researcher then asked the GRA boss his professional view on the effects of tax evasion on the Metropolis and the economy as a whole. His responds was that taxes contributes to greater percentage of government revenue used in financing government activities such as payment of salaries, putting up infrastructure (roads, schools, hospitals etc). Therefore if this situation continues, government revenue will reduce which will in turn affect the level of development in the country at large and the Metropolis.

The researcher asked how the menace of tax evasion could be curbed. The GRA boss indicated that, the GRA is in the process of profiling all the companies and individual business men and women. With a database that will provide them with information of businesses, their work will become easy and they will also be able to cover wider range. He also suggested that for their work to be easier, government should consider employing more revenue personnel to help ease their workload thereby reaching out to those within the various suburbs. Some also suggested they have tried out outsourcing some part of tax inspection unit so they are looking forward to its success to see if they can outsource more.

**Table 7: Expected, Received and Unreceived annual Businesses Returns within the period under review**

Filling of returns	Period under review			
	2013	2014	2015	2016
No. of Reg. Companies	532	421	357	329
Expected Returns in GH¢	189,904	204,315	247,620	288,700
Received Returns in GH¢	99,984	112,906	151048.2	228,073
Unreceived returns in GH¢	89,920	91,409	96,571.8	60,627

**Source: Statistics from GRA, (End of year report 2016)**

Table 7 show the expected annual cash returns, the received returns and unreceived returns of the companies registered in the period under review. The table indicates that in all the years under review, the amount received were less than the GRA's expected returns. The table also shows that in almost all the years

under review, the unreceived amount were more than 20% of the GRA's expected returns.

This is a very challenging situation in that, the unreceived returns of the successive years if put together can put up about two (6 Unit classroom block) in the Metropolis. The GRA however also have to address the underlying issues on the unreturned taxes as well as expand the coverage. This implies that the GRA has to apply a significant amount of time and human resources to address these issues, while simultaneously continuing to address its core responsibilities.

### **Discussions**

The responses indicated that the contributing reasons why taxes are evaded in the Cape Coast Metropolis ranged from the deliberate attempts to evade tax, other people consider tax too high, people evade tax because business not profitable and lack of trust for the use of income tax by government. Beattie (1992) is of the opinion that the desire to own more wealth is one of the reasons for evading taxes. This is because ultimate benefit of the sales of a businessman is the amount of money remaining after he has paid all expenses including taxes. His goal is to reduce cost, reduce his price to obtain a bigger share of the market, and thus, increase the cash available to the business at the end of the financial year.

Another finding was that people could not specifically say whether they have evaded tax before or not in that they cannot recall all their contacts with the officials. It can thus be resolved that about half of the total respondents do not regularly pay taxes in the Metropolis. This is obviously a worrisome situation for the Ghana Revenue Authority.

Revenue Institutions and a variety of academic disciplines suggest that there are two approaches to explaining the reasons for non-compliance. One is to analyse compliance in terms of economic decisions based on the likely economic incentives and costs of complying or not. The other has been to examine the effects of other factors on compliance decisions, particularly as they relate to tax payer behaviour and sometimes tax agency behaviour. In order to tackle the problem of tax avoidance and tax evasion properly, it is important to understand some of the factors underlying the decision to pay tax or not to pay taxes. (Ablordeppey 2005) is of the opinion that a positive relationship exist between tax evasion and perceived inequality of the tax system.

Spicer (1994) in his dissertation, behavioral model of income evasion concluded that evasion by an individual was also found to be positively related to the number of his friends or colleagues who they believe are evading taxes. Beattie (1992) is of the opinion that the desire to own more wealth is one of the reasons for evading taxes. This is because ultimate benefit of the sales of a businessman is the amount of money remaining after he has paid all expenses including taxes. His goal is to reduce cost, reduce his price to obtain a bigger share of the market, and thus, increase the cash available to the business at the end of the financial year. Studies have shown that the tax payer attitude and decision to evade tax is based on different reasons. They include excessive corruption on the part of government officials, problems of assessment, collective and enforcement of tax administrators' incompetence on the part of tax authorities, general dishonesty among Ghanaians, political culture, ignorance, unfairness of the tax system, and lack of regard for equity, law and justice, as well as

unpatriotic Ghanaian citizens. (Ablordepy, 2006).

Tax evasion affect the extent to which the government can provide basic needs of the population and the obvious effect is deplorable infrastructure condition (Bakare, 2006). The education sector in Ghana has performed poorly in most rural areas who cannot afford conducive environment for teaching the pupils. According to Viasat News (2011), pupil's of some villages in the Central, Northern and Volta regions attend their classes under trees. There is no adequate educational facility. The health sector also suffers a lot because there is no adequate facility to aid the health sector. This is because the less privileged do not have adequate access to health facilities.

## CHAPTER FIVE

### SUMMARY, CONCLUSION AND RECOMMENDATIONS

In this chapter, the summary, conclusions and recommendations of the study are highlighted. The summary highlights the objectives of the study, some aspects of the methodology and the main findings of the study. The conclusions and recommendations are also presented in this chapter.

#### **Summary of the Study**

The main objective of the study was to examine tax evasion and the effects on the Ghanaian economy with evidence from the GRA in the Cape Coast Metropolis. The study adopted the case study research strategy. However, the study blended both the qualitative and the quantitative methods in data collection and analysis in getting to the bottom of issues discussed. The population of the study consisted of all the tax officials at the GRA office and companies and individual business men and women in the Cape Coast Metropolis. The sample for the study consisted of 120 businesspersons (only 95 participated) and five GRA staff.

Based on the results and discussions of the study, the following is the summary of the findings of the study.

The study revealed that most tax payers in the Cape Coast Metropolis lack the fundamental knowledge on the tax payment process. This implies that the

individuals and businesses in the Cape Coast Metropolis evade taxes because they are ignorant about the taxation process and do not file the required returns.

Tax evasion lessens funds for national infrastructure and skews the burden of taxes towards few categories of persons thus affecting the development of nations.

In direct response to research question two, the study found that even though some respondents admitted that the level of evasion was high in the Metropolis, there were none who mentioned any sanction to anyone found culpable. However, it was established that the GRA was in the process of profiling tax payers. This was anticipated to give the GRA a more expanded data base of tax payers across the Metropolis.

The study revealed that both tax payers and the officials of the GRA were very much aware of the main effects of tax evasion to the economy thus reduced revenue. It was established that taxes contribute to a greater percentage of government revenue used in financing government activities. Therefore the continuous existence of tax evasion will reduce government revenue which will in turn affect the economic fortunes of the country thereby affecting the development of the Metropolis.

### **Conclusions of the Study**

Based on the discussions of the results and the findings of the study, the following conclusions were drawn.

From the records available at the GRA (see Appendix D) and the information gathered from the field it could be concluded that compliance levels were averagely low for businesses and slightly above average for individuals in the Cape Coast Metropolis. This is a recognized fact that historically, one of the biggest problems of the Ghana revenue Authority has been the compliance pattern of the businesses and individuals. A clear indication of some level of tax evasion in the Metropolis.

It could also be concluded that Tax evasion really affect the fundamentals of the national economy since taxes forms a greater part of governments revenue.

### **Recommendations of the study**

In view of the findings of the study, the following recommendations have been made to help in reducing and curbing the rate at which taxes are evaded in the Cape Coast Metropolis.

The study recommends that the Ghana Revenue Authority in the Cape Coast Metropolis should embark on tax education to educate tax payers on the tax system, tax payment processes, and their duty to pay tax and importance of tax to the national economy as a whole.

The study again recommends that another way of ensuring tax compliance and as such reducing tax evasion is the enforcement of punishment to those who are found to commit tax evasion offences. Most times, it is only those who evade huge sums of taxes who are convicted but attention must be given to those in



small scale businesses. This will deter other people from making attempts to evade taxes in the Metropolis.

It is recommended that appropriate reviews and evaluation processes should be integrated into the entire tax system to encourage taxpayers' compliance to taxes. GRA staff in the Cape Coast Metropolis should be motivated to increase their morale in ensuring they stay resolute to insist on the right procedures. In so doing, evasion of taxes will be minimal to ensure the socioeconomic development of Ghana.

It is recommended that a tax census should be conducted in the Metropolis to know about the actual number of taxpayers whether they are individuals or businessmen so that tax evasion incidences would be reduced.

An audit unit should be established and tax clearance certificates should be issued to the taxpayers by the audit unit so that corrupt activities of tax officials could also be removed.

Incentives should be announced to taxpayers on timely payment of tax without adopting any way of tax avoidance and evasion. New policies should not only be developed to remove reasons/causes of tax evasion but also developed to reduce size of shadow economy because shadow economy is that economy in which people do not show their real income and taxable income that they have.

Evading of taxes by the informal sector is very imperative in promoting the socio-economic development in Ghana. The GRA has a role to play in reducing and curbing the rate at which taxes are evaded. Therefore, appropriate systems should be put in place by the GRA to solve or minimize the rate of tax evasion by the informal sector.

Government of Ghana should use media platforms to enlighten citizens on the effects of evasion of taxes on socioeconomic development. Furthermore, tax rates should be reduced to enhance and boost revenue generation which will increase the tax net to capture many individuals and small businesses. Also, the insignificance of penalties and tax authority bearing should also be tackled. Appropriate checks on these two factors will reduce if not eradicate the problem.

The researcher is also of the view that the GRA should in their attempt to profile businesses and individual tax payers consider collaborating with the Electricity Company of Ghana (ECG) since the ECG has a complete data of all commercial structure, it could furnish the GRA with that data, to help them in their search for people liable to pay taxes. This will not eradicate the entire problem of tax evasion but will ensure the collection of taxes which has long eluded the tax officials for so long.

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**APPENDIX A**  
**QUESTIONNAIRE FOR BUSINESSES/INDIVIDUAL BUSINESS MEN**  
**AND WOMEN**

This questionnaire has been put together to gather information about your opinion on tax evasion and its effects on the Ghanaian economy: evidence from available records of GRA office in the Cape Coast Metropolis. You are kindly being requested to take some time of your busy schedule and provide the necessary information and wish to assure you that the answers provided will be used for academic work only and treated confidentially.

Thank you in advance for your time and agreeing to participate in this study

**QUESTIONNAIRE FOR SELECTED CLIENTS OF GRA CCM**

Please tick (√) in the following questions

1. Gender (a) Male [ ] (b) Female [ ]
2. Age (a) Below 20 [ ] (b) 21-30 [ ] (c) 31-40 [ ] (d) 41-50 [ ] (e) 51 and above [ ]
3. Educational background (current) of respondent (a) Basic School [ ] (b) Secondary/Technical/Vocational School [ ] (c) Tertiary [ ] (d) No formal education [ ] (e) Other [ ]
4. Type of Business engaged in (a) Manufacturing [ ] (b) Service Oriented Business [ ] (c) Distribution and retailing [ ] (d) Other [ ]

5. How long have you operated? (a) Less than 1 year  (b) Between 1 - 4 years   
] (c) 5 years and above

6. Do you know you have to declare your total income to the Ghana Revenue Authority (GRA)? (a) Yes  (b) No

7. Are you aware that you owe it a duty to pay tax on what you generate from your business? (a) Yes  (b) No

8. If Yes to question 8 how often do you pay it? (a) Regularly  (b) Occasionally

10. If no, why? If you answered No, skip to question 14

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

9. Have you ever evaded tax? (a) Yes  (b) No  (c) Not sure

10. Do you think all your colleagues pay tax? (a) Yes  (b) No  (c) Not sure

11. To what extent do you think people evade tax in the Metropolis? (a) Very High  (b) High  (c) Low  (d) Very Low  (e) No Idea

12. How do you perceive the current tax rate? (a) Inadequate ( ) (b) Fair ( ) (c) Too High ( ) (d) Don't Know ( )

13. Why do you think people evade tax? a) They are not aware they are supposed to pay  b) It is intentional/deliberate  c) Tax is too huge  d) Business not profitable  e) Distance difficulty in paying tax  f) Unnecessary use of tax income by government

Any other if some of your thoughts could not be found in the above.

.....  
.....  
Thank you for your time

**APPENDIX B**  
**INTERVIEW SCHEDULE FOR GRA STAFF IN THE CAPE COAST**  
**METROPOLIS**

This interview has been put together to gather information about your opinion on tax evasion and its effects on the Ghanaian economy: evidence from available records of GRA office in the Cape Coast Metropolis. You are kindly being requested to take some time of your busy schedule and provide the necessary information and wish to assure you that the answers provided will be used for academic work only and treated confidentially.

Thank you in advance for your time and agreeing to participate in this study.

**INTERVIEW QUESTIONS FOR GHANA REVENUE AUTHORITY**  
**OFFICIALS**

- 1) How long have you worked as a tax official in the Metropolis?.....  
.....
- 2) What is the compliance level in the Cape Coast Metropolis? .....  
.....
- 3) Do people evade tax in this Metropolis? .....  
.....
- 4) What is the extent of tax evasion in the Metropolis? .....

.....  
5) Why do you think people evade tax or what brings about tax evasion? .....

.....  
6) Should tax evasion continue, what will therefore be the resultant effect on the Metropolis and the economy as a whole? .....

.....  
7) What can be done to ensure that people do not evade tax? .....

.....  
8) What are the challenges that you encounter in carrying out your duty? .....

.....  
9) In your opinion, what must be done to do away with these challenges in order to aid your work? .....

.....  
.....  
THANK YOU VERY MUCH

**APPENDIX C**  
**INTRODUCTORY LETTER TO THE GRA OFFICE**

**UNIVERSITY OF CAPE COAST**  
**COLLEGE OF HUMANITIES AND LEGAL STUDIES**  
**SCHOOL OF BUSINESS**  
**DEPARTMENT OF ACCOUNTING**

Telephone: 03321-32440-4, 32480-3 Direct: 03321-37871  
Fax: 233-3321-32847  
Telex: 2552, UCC, GH.  
Telegrams & Cables: University, Cape Coast



UNIVERSITY POST OFFICE  
CAPE COAST, GHANA

Our Ref: SB/DACT/ V.I/R/

Your Ref:

5<sup>th</sup> October, 2016

The Managing Director  
Ghana Revenue Authority  
Cape Coast Branch

Dear Sir,

**INTRODUCTORY LETTER: MS. MARY ESSILFIE AFFUL**

The bearer of this letter, Ms. Mary Essilfie-Afful is a Master of Business Administration (Accounting) student at the Department of Accounting of the School of Business, University of Cape Coast. Ms. Essilfie-Afful is writing her dissertation on the topic "Tax Evasion and its Effects on Ghanaian Economy".

We would be grateful if you could offer her the necessary assistance with regard to the data she might need to enable her work on her dissertation.

Thank you in anticipation of your co-operation.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Zangina M. Isshaq'.

Dr. Zangina M. Isshaq  
**HEAD**

**APPENDIX D**

**DATA FROM THE GRA OFFICE**

	SELF-EMPLOYED RETURNS			
	2013	2014	2015	2016
JANUARY	6	3	5	10
FEBRUARY	12	7	9	15
MARCH	5	8	14	8
APRIL	247	221	371	382
MAY	8	17	21	15
JUNE	2	4	13	17
JULY	1	3	9	12
AUGUST	8	5	4	1
SEPTEMBER	2	7	9	2
OCTOBER	8	9	3	4
NOVEMBER	3	4	5	7
DECEMBER	6	1	0	3
<b>TOTAL</b>	<b>308</b>	<b>289</b>	<b>463</b>	<b>476</b>
<b>NO. OF REGISTERED TAXPAYERS</b>	<b>551</b>	<b>528</b>	<b>618</b>	<b>639</b>

NOTE: THESE RETURNS ARE FILED ANNUAL. THE LAST MONTH IS APRIL FOR THE PRECEDING YEAR RETURNS.

GHANA REVENUE AUTHORITY  
DOMESTIC TAX REVENUE  
CAPE COAST - S.T.O.  
P. O. BOX CT 958  
CAPE COAST

S



	SELF-EMPLOYED RETURNS			
	2013	2014	2015	2016
JANUARY	6	3	5	10
FEBRUARY	12	7	9	15
MARCH	5	8	14	8
APRIL	247	221	371	382
MAY	8	17	21	15
JUNE	2	4	13	17
JULY	1	3	9	12
AUGUST	8	5	4	1
SEPTEMBER	2	7	9	2
OCTOBER	8	9	3	4
NOVEMBER	3	4	5	7
DECEMBER	6	1	0	3
TOTAL	308	289	463	476
NO. OF REGISTERED TAXPAYERS	551	528	618	639

NOTE : THESE RETURNS ARE FILED ANNUAL. THE LAST MONTH IS APRIL FOR THE PRECEDING YEAR RETURNS.

5

GHANA REVENUE AUTHORITY  
 DOMESTIC TAX REVENUE  
 CAPE COAST - S.T.O.  
 P. O. BOX CT 958  
 CAPE COAST



	COMPANIES RETURNS			
	2013	2014	2015	2016
JANUARY	4	3	5	3
FEBRUARY	6	7	2	7
MARCH	8	2	6	2
APRIL	137	128	118	125
MAY	12	8	4	6
JUNE				
JULY	5			
AUGUST				
SEPTEMBER				
OCTOBER				
NOVEMBER				
DECEMBER				
TOTAL	172	148	135	143
NO. OF REGISTERED TAXPAYERS	532	421	357	329

NOTE: THESE RETURNS ARE FILE ANNUAL. THE LAST DAY MONTH IS APRIL FOR THE PRECEDING YEAR RETURNS

GHANA REVENUE AUTHORITY  
DOMESTIC TAX REVENUE  
CAPE COAST - S.T.O.  
P. O. BOX CT 958  
CAPE COAST

	VAT RETURNS				
	2013	2014	2015	2016	
JANUARY	414.00	320.00	346.00	293.00	
FEBRUARY	406.00	324.00	343.00	295.00	
MARCH	428.00	316.00	429.00	315.00	
APRIL	431.00	335.00	364.00	240.00	
MAY	452.00	357.00	367.00	328.00	
JUNE	449.00	351.00	343.00	267.00	
JULY	451.00	307.00	342.00	279.00	
AUGUST	458.00	307.00	323.00	278.00	
SEPTEMBER	450.00	300.00	297.00	281.00	
OCTOBER	447.00	284.00	299.00	298.00	
NOVEMBER	441.00	362.00	306.00	292.00	
DECEMBER	452.00	405.00	315.00	309.00	
<b>TOTAL</b>	<b>5,279.00</b>	<b>3,968.00</b>	<b>4,074.00</b>	<b>3,475.00</b>	
<b>AVERAGE</b>	<b>439.92</b>	<b>330.67</b>	<b>339.50</b>	<b>289.58</b>	
<b>REGISTERED TAXPAYERS</b>	<b>458.00</b>	<b>435.00</b>	<b>478.00</b>	<b>450.00</b>	

NOTE: THESE RETURNS ARE FILED MONTHLY.

GHANA REVENUE AUTHORITY  
DOMESTIC TAX REVENUE  
CAPE COAST - S.T.O.  
P. O. BOX CT 998  
CAPE COAST

	PAYE RETURNS			
	2013	2014	2015	2016
JANUARY	156.00	143.00	144.00	147.00
FEBRUARY	155.00	143.00	144.00	142.00
MARCH	158.00	142.00	148.00	144.00
APRIL	152.00	139.00	147.00	140.00
MAY	154.00	134.00	148.00	125.00
JUNE	154.00	134.00	149.00	137.00
JULY	157.00	142.00	152.00	281.00
AUGUST	158.00	145.00	145.00	125.00
SEPTEMBER	140.00	142.00	149.00	131.00
OCTOBER	138.00	143.00	153.00	133.00
NOVEMBER	157.00	137.00	155.00	135.00
DECEMBER	142.00	140.00	146.00	148.00
<b>TOTAL</b>	<b>1,821.00</b>	<b>1,684.00</b>	<b>1,780.00</b>	<b>1,788.00</b>
<b>AVERAGE</b>	<b>151.75</b>	<b>140.33</b>	<b>148.33</b>	<b>149.00</b>
<b>NO. OF REGISTERED TAXPAYERS</b>	<b>192.00</b>	<b>178.00</b>	<b>181.00</b>	<b>185.00</b>

NOTE: THESE RETURNS ARE FILED MONTHLY.

GHANA REVENUE AUTHORITY  
DOMESTIC TAX REVENUE  
CAPE COAST - S.T.O.  
P. O. BOX CT 958  
CAPE COAST