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**Comparative Analysis of Government Revenue and Expenditures In the case of the Federal Government of Ethiopia**

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**Abstract:**

Taxation is one of the primary activities of governments in civilized societies, which has been contributing significant share of their revenues. Public expenditure plays important function in economic development process in developing countries like Ethiopia. The general objective of the study was to make a Comparative analysis of government tax revenue and expenditure budget of the federal government of Ethiopia. Both primary and secondary data were used to carry out the study. The primary data were collected from the ministry of finance and economic cooperation and the tax authority using questionnaire and interviews. SPSS 21 versions were used to analyzed the collected data. The findings show that the tax authority has limitations in using technologies to modernize the tax administration, poor the tax collection capacity. The country's Tax to GDP ratio is low as compared to the sub-Saharan countries. There are different factors for the poor tax collection performance; weak enforcement and low tax audit coverage, and lack of strong cooperation with stakeholders. The government has weaknesses in the management public resources. The tax authority should use different Medias to create taxpayers awareness about tax, should strengthen its tax enforcement department to bring non taxpayers to the tax net.

**Key Words:**

*Tax, Enforcement, Tax Audit and Expenditure*

## **1. Introduction**

Taxation is one of the primary activities of governments in civilized societies, which has been contributing significant share of their revenues (James & Nobes, 2012, 2013; Lymer & Oats, 2013, 2014). Tax authorities levy taxes as a compulsory payment on income, expenditure, wealth or people, for which the individual tax payer directly or specifically received nothing in exchange.

Scholars' attentions have been attracted by Government tax revenue performance for decades; On the other hand, there are still numerous arguments on how to assess the tax revenue performance, the potential tax revenue, and how government units make use of the tax revenue potential to generate tax revenue (Bird, et al., 2006). Starting from the mid-20th century econometric techniques have been used by many researchers. Governments are required to collect adequate domestic tax revenue to finance their expenditures to provide goods and services to their respected citizens.

According to Thiru .K. (2013) Public expenditure in developing countries like Ethiopia plays an important role in the process of economic development. Public expenditure helps economic development by expanding economic infrastructure such as roads, power, food, shelter, health, education, employment opportunity, transport and other sectoral development. Further, it raises the standard of living of the people and supports social, economic and human development.

Governments' expenditure budgets are classified as recurrent and capital budgets. The recurrent budgets are expended mainly on routine and day-to-day operations of the government, while capital expenditures are government investment outlays raising the country's wealth (Stephen and Michael 2018).

## **2. Research problems**

The government of Ethiopia has the national vision of becoming a low middle-income country by 2025, to realize this vision the government set broad Growth and Transformation plan with a projected GDP of 11 - 15%. The state lead growth model of Ethiopian has achieved growth rates above the average for sub Saharan countries MOFED (2010). The proposed national growth and transformation plan is to improve the country's economy. The most important function of tax is raising revenue, which serve as the most important means for financing public goods such as public infrastructure and maintenance of law and order (OECD, 2014). To achieve this plan the government carried out many activities and registered remarkable achievements in real GDP growth, however, the performance has still fallen short of the targets set in the Plan. The tax to GDP ratio is low compared to the sub-Saharan countries and the expenditure management has also different shortfalls. Therefore, the purpose of this study was

to investigate the main challenges that hinder the government achieving tax and expenditure management objectives.

### **3. Literature Review**

#### **Definitions taxes, benefits of taxes and public expenditures management**

Taxes are referred as essential contribution to state revenue by individuals, and businesses to cover government costs in providing goods and services to its citizens. Taxpayers do not expect direct and proportionate return from governments for their payment of taxes (OECD, 1996).

Taxes are involuntary payment by individuals and corporate taxpayers to governments to finance their developmental needs and on different social services, political and economic activities however; the benefit received by the taxpayers is not equal to the amount of taxes they have paid.

One of the well-known principles of taxations is imposing least sacrifice on the people as a whole, and more on some people and less on other. The governments services are provided to the society without taking into consideration the taxes paid by the taxpayer. Contemporary governments should try to maximize the welfare and minimize sacrifices of their community.

Taxes are the major sources of country's national revenue for its economic development as Cited in Zahraden (2019) Ahuj (2002) & somaye (2012). To protect and increase the economic and social welfare of citizens' governments incurs huge of amount expenditures. Well-structure revenue system is a necessary condition for a country to have Strong, sustainable and inclusive economic development.

Public expenditures on physical, social and administrative infrastructures are financed by government revenue funds. Stable and accountable government's needs strong revenue system to support strong citizen-state relationship to be effective Michael. C (2015).

According to Thiru .K. (2013) Public expenditure plays a significant role in the process of economic development of developing nations like Ethiopia. Public expenditure helps economic development by expanding economic infrastructure such as roads, power, food, shelter, health, education, employment opportunity, transport and other sectoral development. Further, it raises the standard of living of the people and supports social, economic and human development.

Governments' expenditure budgets are classified as recurrent and capital budgets. The recurrent budgets are expended mainly on routine and day-to-day operations of the government, while capital expenditures are government investment outlays raising the country's wealth (Stephen and Michael 2018).

Public sector budgeting has multiple objectives to address in the public sectors entities in realizing the needs of nations and PEM is an approach to meet these objectives.

In particular, PEM raise the following question. What outcomes do we want to achieve through the budget and what procedures, rules, and processes do we need to put in place in order to achieve these out-comes. PEM promotes three main functions i.e. allocative efficiency, aggregate fiscal discipline and operational efficiency.

#### **4. Objectives**

##### **General objectives**

The general objective of the study is to make a Comparative analysis of government tax revenue and expenditure of the federal government of Ethiopia.

##### **Specific objectives**

1. To evaluate the tax collection performance of the federal government
2. To examine the extent of tax revenue contribute to expenditure budget in Ethiopia
3. To assess the rate of tax revenue and expenditure increments

##### **Research questions**

1. How is the tax collection performance of the federal government
2. What percentage of government expenditure is covered by domestic revenue
3. How is the rate change of revenue and expenditures of the government

#### **5. Methodology**

The research methods used for the study were mixed approaches; this method deals with the problems of the study from different point of view. Primary data collection instruments i.e. questionnaires and interview were used to collect data from the experts and officials of ministry of finance and cooperation and the tax authority and secondary data were collected from internet sources, published journals, magazines and books sources.

#### **6. Results and Discussions**

##### **6.1 pilot study**

Pilot test was carried out to decide the appropriateness and significance of the questions in the instrument. Content validity test was carried out to measure the extent of the instruments coverage, representativeness of the universe, specificity and clarity of the topic under study. The instrument was provided to three academicians and four practitioners who appraised each item thoroughly. The draft was also distributed and piloted on 20 experts of ministry of finance and economic cooperation and tax authority.

##### **6.2 Reliability Test**

The researcher used cronbach's alpha ( $\alpha$ ) to test reliability analysis for the comparative analysis of tax revenue and government expenditure in the Ministry of Finance and Economic

cooperation and tax authority. The most wide and commonly used measure of internal consistency (reliability) is cronbach’s alpha. The cronbach’s alpha ( $\alpha$ ) of the scale used in the research is 0.85 which is far greater than 70 %.the scales with the coefficient alpha above 0.70 is good and acceptable this shows that there is high internal consistency and reliability in the questionnaire. As a result, the level of alpha was considered to be reliable enough to proceed with the data analysis.

### **7. Response Rate**

The field survey result indicates that from 75 questionnaires were distributed to experts in Ministry of Finance and Economic Cooperation and Tax Authority 63 were returned representing 84 percent.

#### **7.1 Demographic information of respondents**

The following table shows information related to respondents age, gender, educational background, and experience of experts in MOFEC and the Tax Authority.

Demographic Characteristics of respondents

Age	Frequency	Percent
<25	18	29
25-35	29	46
>35	16	25
Total	63	100
Experience in Years		
<3	13	20.6
3-6	17	27
6-10	19	30.2
>10	14	22.2
Total	63	100.0
Educational status		
Diploma	-	-
BA	38	60.3
MA& above	25	39.7
Total	63	100

Source compiled from questionnaires (2018)

Out of the 63 respondents 18(29%) are less than 25 years old, 29(46%) respondents’ age range 25-35 years old and the remaining 16(25%) are above 35 years. In summary the majority of the experts’ ages lie between 25 and 35years which is a working age.

The qualifications of the experts sample respondents. Accordingly, out of the respondents, 38(60.3%) of them have B.A Degree, 25(39.7 %) of the respondent has MA or MSC degree in different fields of study. Therefore the all the experts have BA and above educational background which enables to perform their duties and responsibilities.

The experts experience in MOFEC shows that 13(20.6%) have less than 3 years, 17(27%) respondents have 3-6years, 19(30.2%) of the experiences have 6-10 years, and the remaining 14(22.2%) have more than 10 years experience. The majority of the experts have above 3 years works experience which is helpful for the ministry to introduce new technology, system and process without difficulty.

Responses on the government the tax collection potential

No	Items/Statements	Responses										Total	
		SA		A		N		DA		SD		Frequency	Percent
		Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent		
1	The government applies modern technologies in the tax system	9	14	13	21	6	10	24	38	11	17	63	100
2	The tax authority works to bring non tax payers to the tax net to broad tax bases	3	5	19	30	9	14	18	29	14	22	63	100
3	There is smooth relationship and strong cooperation among the tax authority and stakeholders	11	17	15	24	5	8	27	43	5	8	63	100

Source Compiled from Questionnaires (2018).

From the above table for the statement that the government applies modern technologies in the tax system 9(14%) of the respondents strongly agreed, 13(21%) agreed, 6(10%) are neutral 24(38%) disagreed and 11(17%) strongly disagreed. Therefore; significant number 35 (55%) of the respondents disagreed on the statement. The other question raised was whether the tax authority works hard to bring non tax payers to the tax net to broad tax bases; 3(5%) respondents strongly disagree, 19(30%) disagreed, 9(14%) respondents are indifferent, 18(29%) respondents disagreed and 14(22%) respondents strongly disagreed with the statement, almost half of the respondents replied that the government needs to work hard to broaden the tax bases so that it can collect the domestic taxes. To triangulate the question an interview was held with MOFEC senior officials they said that tax reforms were made in the past few years; however,

it was not effective as it was intended to be. They also mentioned that the reasons for the poor tax collection performances were; narrow tax bases, lack of awareness by taxpayers, unable to fully apply/use those new technologies which were introduced for the tax collection purpose and the tax audit coverage was low and was not able to investigate tax evasion and avoidances. The other reason that the interviewee stressed was that there are large number of non taxpayers in the country which adversely affects the government tax revenue. Third questions was the about the relationship and cooperation among the tax authority and stakeholders' their response was 11(18%) of the respondents strongly agreed, 15(24%) agreed and 5(8%) of the respondents have reservation about the statement, 27(43%) respondents disagreed and 5(8%) strongly disagreed with the statement. Therefore more than half 32(51%) of the respondents replied that there is no smooth and strong relationship between the tax authority and stakeholders' which is the most essential prerequisites of the tax collection performance.

#### Percentage of Government Revenue to GDP Ratio

indicators	2011	2012	2013	2014	2015	2016	2017	Average
Total government revenue and foreign aid	16.6	15.5	15.8	14.9	15.4	15.9	15	15.6
Total domestic revenue	13.4	13.8	14.3	13.8	14.4	15	14.3	14.1
Tax revenue	11.5	11.5	12.3	12.5	12.7	12.4	11.6	12.1
Direct taxes	3.8	3.9	4.2	4.4	4.6	4.7	4.5	4.3
Domestic indirect taxes	3.0	3.1	3.7	3.8	4.0	3.6	3.5	3.6
Import taxes	4.6	4.5	4.4	4.3	4.1	4.1	3.7	4.2
Non tax revenue	2.0	2.3	2.0	1.2	1.6	2.7	2.6	2.1
Foreign Aid	3.2	1.7	1.5	1.1	1.0	0.8	0.7	1.4

Source MOFEC 2018

From the above table we can see the sources of domestic taxes and non taxes revenue shows slight increments for the first few years of GTP, however the rate of change is low as compared with plan. The government target was to increase the Tax to GDP ratio by the end of the GTP to be 17 percent however, the actual average Tax to GDP was 12.1.

According to OECD (2019), the average Tax to GDP ratio of sub-Saharan countries is 17.2% and the non tax revenue is less than 5%. Whereas Ethiopia's average tax revenue to GDP and non tax revenue are 12.1% and 2.1% respectively, when we compare these ratios it is by far too low. To investigate the causes of the problems interview questions were raised to the officials of the MOFEC, their response shows that there are different factors which contributes for the

low performance some of these are; there was political instability from 2016 to 2018 which results low GDP and tax collection, lack of commitments and cooperation among stakeholders and senior government officials in implementing the plan, the policies and administrative measures don not encourage taxpayers for the self assessment payment, weak government enforcement measures are some of the reasons for the poor tax collection performance.

Questions related to the extent of tax revenue contribute to expenditure budget

No	Items/Statements	Responses										Total	
		SA		A		N		DA		SD		Frequency	Percent
		Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent	Frequency	Percent		
1	The government expenditure budget is utilized in efficient and effective manner for the intended purpose	6	10	13	21	7	11	26	41	11	17	63	100
2	The government budget deficit is efficiently used for intended purpose	9	14	10	16	2	3	18	29	24	38	63	100
3	Governments officials are held accountable for the wastage of public resources investigated by auditors	5	8	9	14	3	5	29	46	17	27	63	100
4	Government fiscal policies are properly implemented	7	11	16	25	5	8	23	37	12	19	63	100

Source Compiled from Questionnaires (2018).

From the above table for question whether the government expenditure budget is utilized in efficient and effective manner for the intended purpose 6(10%) of the respondents strongly disagree, 13(21%) respondents disagree and 7(11%) respondents are reserved to respond the question whereas 26(41%) respondents disagreed and 11(17%) respondents strongly disagreed with statement. Significant number 37(58%) of the respondents believe that the government budget utilization is not effective and efficient. As cited in HamadA. & Marwan A. (2018), John Maynard Keynes (1936) lay the foundations for the relationship between government spending and economic growth, as he believes that public expenditure stimulates output growth while internal financing can crowd out the private sector. Keynes argues that public spending stimulates economic development through its impact on consumption and investment demands. Question related with whether government deficit financing was properly utilized or not



respondents 9(14%) strongly disagreed 10(16%) respondents disagreed and 2(3%) respondents are neutral and 18(29%) respondents disagreed and 24(38%) respondents strongly agreed. Majority 42(67%) respondents believed that the deficit financing didn't meet its objectives. The other question was whether Government's officials are held accountable for the wastage of public resources investigated by auditors; out of the 63 respondents 5(8%) responds strongly agreed,9(14%) respondents disagreed and 3(5%) respondents are neutral and 26(49%) respondents disagreed and the remaining 17(27%)respondents strongly disagreed with the statement. Majority 43(76%) of the respondents believed that the objective of deficit financing was not met. Responses for the question whether Government fiscal policies are properly implemented or not; 7(11%) respondents strongly agreed, 16(25%) of the respondents disagreed and 5(8%) respondents are neutral and 23(37%) respondents disagreed and the remaining 12(19%) respondents strongly disagreed with the statement. Significant 35(56%) number of respondents believed the government policies are not properly implemented.

Total government revenue and expenditure (in Billions birr)

Descriptions	2011	2012	2013	2014	2015	2016	2017	Average Change
Total expenditure budget	94	124	154	186	225	280.6	329.7 0	23.3
Current budget	40.7	51.4	62.7	78.1	107	136.7	176.6	27.8
Capital budget	53.3	73	91.3	107	118	144.2	153	19.6
Total government resource (TR+FA)	85.6	115.6	137.2	158. 1	199.6	244.8	270.2	21.4
Total revenue (TTR+NTR)	69.1	102.8	124.1	146. 2	186.6	231.8	257.7	25.1
Fiscal deficit	24.9	21.2	29.9	39.8	38.4	48.8	72	-1.8
Total tax revenue	59	85.7	107	133. 1	165.3	190.5	210.2	24.1
Non tax revenue	10.1	17.1	17.1	13.1	21.3	41.3	47.6	36.2
Foreign aid	16.5	12.8	13.1	11.9	13	13	12.5	-4.0

Source compiled from MOFEC reports 2018

From the above table the government total expenditure is increasing on average at rate of a 23.3 whereas the total domestic revenue increases on average at a rate of 25.1 this shows the government tax non tax collection capacity is increasing however there is still in efficiency comparing to the sub Saharan countries. As shown above the government tax revenue was

increased at an average of 24.1 and non tax revenue increases at 36.2 from this it can be concluded the non tax revenue increases at increasing rate as compare to the tax revenue.

When we see the government expenditure budget data the current expenditure budget is increasing at an average of 27.8 while the capital budget increases at 19.6. The government of Ethiopia invests huge amount of capital in economic and social infrastructures like education, health, pure water supply, and road and poverty reduction projects. In the last few years fiscal deficit was increasing because more than 50% of government expenditure budget was allocated for capital/developmental programs MOFEC, (2018). Ethiopia stands 5<sup>th</sup> foreign aid recipients' countries in world and the 1<sup>st</sup> in Africa from Development Assistance Committee members' countries OECD (2019). Foreign aid is an important source of finance for developing countries however; high dependence on foreign aid has short falls especially during political and economic crisis in DAC countries. From the above data Ethiopia's foreign aid is decreasing at average rate of 4 percent from time to time.

## **8. CONCLUSION AND RECOMMENDATION**

### **8.1 Conclusions**

The government invested huge amount money to modernize the tax administration and implemented tax reforms to improve its tax collection capacity in the last few years; nevertheless, it cannot collect adequate domestic tax revenue to finance its developmental needs. The findings show that there are progresses in the tax collection trend as compared to the past trend; however, it is still low when compared to the sub-Saharan countries. The reasons for the poor tax collection performance were weakness in using new technologies to its full capacity in the collection process, lack of awareness by taxpayers; weak enforcement and low tax audit coverage. In addition there is weak cooperation between the tax authority and stakeholders' which adversely affects the government tax revenue. Regarding the government expenditure management system the findings show that there are weaknesses in using government expenditure budget effectively and efficiently for the intended purpose. On the other hand Weakness by the government to held accountable government officials for the wastage of public resources investigated by auditors. Ethiopia receives significant amount of the foreign aid from DAC to cover its expenditure budget. Concerning the fiscal policies the findings show that the country fiscal policy stabilized the macroeconomic and accelerate its growth.

### **8.2 Recommendation**

The government should introduce new modern technologies in the tax administration, and design system to control its proper implementations. The tax authority should provide trainings

to experts on how to use the new technologies. The tax authority should use different Medias to create taxpayers awareness. In addition, the tax authority should strengthen its tax enforcement department to bring non taxpayers to the tax net and increases it tax audit coverage to collect adequate taxes to cover its expenditure budget. On the other hand the tax authority should create smooth relationship and cooperation with stakeholders. The government should improve its expenditure management so that resources can be used for the intended purpose. The other issue which the government should work is to hold accountable public officials for the wastage of resource investigated by auditors. Finally the government should reduce it dependency on foreign aid to cover its expenditure budget.

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