

**A STUDY OF THE CHALLENGES AND PROSPECTS OF THE VAT SERVICE IN
GHANA**

(A CASE STUDY OF THE KUMASI METROPOLIS)

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STATEMENT OF AUTHENTICITY

We have read the university regulations relating to plagiarism and certify that this report is all our own work and does not contain any unacknowledged work from any other source. We also declare that we have been under supervision for this report herein submitted.

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I hereby declare that the preparation and presentation of the dissertation were supervised in accordance with the guidelines on supervision laid down by Christian Service University College

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ABSTRACT

Each country has different reasons for adopting VAT but the principal motive is the same: a *properly designed VAT system raises more revenue with less administrative and economic cost than any other more broadly based tax.*

The study sought to unearth the challenges of the Value Added Tax (VAT) administration and highlighted the prospects of VAT as a valuable tool for policy formulation for tax mobilization in Ghana.

The study was conducted using both qualitative and quantitative methods using primary and secondary data. The primary data were the responses from questionnaires received from respondents and also interviews in the form of formal and informal. The secondary data on the other hand were gathered from written materials.

The study revealed that the VAT system in Ghana runs on three key pivots, that is consumers, agents and the VAT services. The finding of this study revealed each of these stakeholders in the VAT system had its own problems. While consumers lacked major education on the entire operations of VAT, the agents, on the hand have no intentions of charging VAT since they want to remain competitive. The VAT service lacked the logistics and manpower to check the infractions on the VAT law.

Although the VAT administration has seen some improvement in the last five years, there is still more room for improvements.

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DEDICATION

To our various families for their constant love and support

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CHAPTER ONE

1.1 BACKGROUND OF THE STUDY

The government or administrative body of a nation or community needs financing in order to execute its roles successfully and carry out its responsibilities. The ability to do this depends on the sources from which the government derives its revenue.

The sources and the adequacy of government revenue will to a large extent determine the quality of service and the specific roles the government can perform. It is for these reasons that every government is concerned with collecting adequate revenue from taxes to enable it perform its roles to the satisfaction of the citizens.

Sources of government revenue refer to the various avenues from which the government gets money to meet its expenditure. For the generation of revenue, governments all over the world derive its revenue from several sources. The major source of government revenue is tax. Total tax revenue in relation to GDP was GH¢4,413.4m equivalent to 17.0% of GDP for the year 2010. (source: 2011 budget, section 69). However, tax is classified into two main types.

These are:

- i. Direct tax
- ii. Indirect tax

Direct taxes

These are taxes based on either the income or wealth of the tax-payer. The following are the main forms of direct taxes:

Income tax is levied on individuals at a standard rate. Income tax is mostly of progressive nature where higher income earners pay more than the lower income earners.

- i) Capital gain tax is imposed on the increase in the value of property between the time of its purchase and its sale.
- ii) Basic rate is a tax imposed on the residents by the various metropolitan assemblies.
- iii) Company tax is paid by companies. It is levied on the profits of companies.

Indirect taxes

These are taxes which are paid indirectly by consumers who purchase goods and services. The following are the main types of indirect taxes which also constitute one of the major sources of revenue for the governments of many countries.

- i. Import duties are taxes imposed on imported goods and services. They are also known as custom duties.
- ii. Export duties are taxes levied on goods leaving the country to other countries.
- iii. Exercise duties relate to manufactured units and the amount of tax, more often than not, is determined by how many units of output.

In addition to the two mentioned above, there are other sources of revenue from which many governments derive revenue to enable them to perform their roles in the socio- economic and political development in their countries. The Ghanaian economy is no exception. The following are some of the non-tax revenue sources.

Grants

These are usually received from international agencies. They are funds or capital items given out freely from other countries especially the developed ones.

Income and fees

These are revenue that accrues to government from some income-generating activities like state owned business enterprises. Sale of property or assets of the state that may not be yielding appreciable returns can also bring some revenue to the government.

Loans

They are financial assistance that are granted to the government by multinational financial organizations such as the World Bank, African Development Bank (ADB) and International Monetary Fund (IMF) which the government has to repay with interest at a specified date.

The Value Added Tax

Before the advent of the Value Added Tax (Act 486) the government of Ghana mobilized its revenue from the sources listed above. The law provided for the imposition of VAT as a

replacement tax for sales tax, entertainment duty, hotels and restaurant tax, betting tax and advertisement tax with effect from 1st March 1995.

However, in less than four months of the introduction of VAT, it was withdrawn. Early in 1996, a reconstituted VAT project was set up on a directive contained in the president's sessional addresses to parliament in January 1996. To start with, the VAT project undertook a thorough evaluation of the outcome of the actual implementation for the two and half months that the tax operated in Ghana.

Apart from the study of the VAT project, the Overseas Development Agency of the British Government that had provided financial assistance and technical support during the implementation in 1995 dispatched a team to Ghana to study what went wrong with the implementation.

In February 1998 the VAT (Act 564) was passed to put Ghana on a firm course to join the ranks of over 100 countries that are currently operating VAT. Indeed, in Africa, countries such as Cote d'Ivoire, Togo, Burkina Faso, Nigeria, Kenya, Uganda, Benin, Zambia, South Africa, Algeria and others had introduced the tax for some time now.

Many people have wondered why the government decided to re-introduce VAT.

The reasons for introducing VAT in Ghana

- i. To expand and diversify the tax base
- ii. To adopt a uniform basis for collecting the general consumption taxes.
- iii. To improve the efficiency and equity of the mechanism for collecting taxes.

It must be noted that VAT is merely a replacement for the sales and service taxes that had operated in the country for over thirty years but not a superimposition on the existing tax structure. VAT was to be charged at 10% from the effective date.

In the year 2000, the VAT was increased to 12 ½%, the increase of 2 ½% was to be paid into an Education Fund called the Ghana Education Trust Fund (GETFund).

1.2 STATEMENT OF THE PROBLEM

Many western countries as well as developing countries in Africa have tried the Value Added Tax (VAT) as an indirect system of taxation. VAT as a system of indirect taxation for revenue mobilization presents a great number of prospects in our bid to develop as a nation. Nonetheless, the golden idea as VAT may be, there are underlying impediment inherent in the administration as well as several social and economic problems that surround its efficient operation.

VAT like other revenue mobilization system relies greatly on proper and effective accounting records kept by operators. This feature if missing may render the operation of the VAT far from success.

The least said about education of the agents the better. Laws enacted by our policy makers regarding VAT are not still understood looking at the current revenue loss through improper filling of VAT returns reported every month (Daily Graphic July,6,7 & 9 August, 2005; Enquirer, Thursday, 14-17 July 2005 ed), the mode of computing VAT seem to be the greatest of all. Most consumers as well as the agents do not understand how the VAT system operates and since the operation of VAT depends a lot on invoice computation, the issue raises a great obstacle to effective operation of VAT system. These and other problems need to be investigated.

In addition to the above, Dr. Nii Moi Thompson in 2006 argued on Metro TV Good evening Ghana that the VAT service is operating far below 25% of its capacity.

What is more, the knowledge of the operations of VAT among consumers and agents is very low and this has resulted to the low generation of income from the VAT system.

1.3 RESEARCH OBJECTIVES

The study investigated the challenges and prospects of the VAT services regarding the Value Added Tax (VAT) in Ghana. The broad aim of the study is to discover the challenges facing VAT administration and to propose appropriate interventions that may be used by the VAT service to enhance and monitor its operation. The research mainly focused on the analysis of the challenges of Value Added Tax administration and prospects in line with the increasing demand on Ghana as a developing economy to mobilize revenue for development.

In order to discover the problems and prospects of the study, it was important to discuss the VAT administration in detail. This study had the following goals:

- i. To analyze the prospects of VAT vis-a-vi the growth of the economy (GDP)
- ii. To analyse the challenges faced by the VAT service in a bid to generate revenue for Ghana as a developing economy.

1.4 SIGNIFICANCE OF THE STUDY

This study will bring out the challenges of the Value Added Tax (VAT) administration and highlight the prospects of VAT as a valuable tool for policy formulation for tax mobilization in Ghana. Assist the Ministry of Finance (MOF), the VAT service, tax consultants, investors and other revenue mobilization bodies to improve upon their revenue mobilization and in their assessment, may employ these findings. The results of the research are important because of the following reasons:

- i. A firm understanding of the problems of VAT administration and its prospects that this thesis hopes to uncover may provide a basis for further research in the area.
- ii. Detailed analysis of the problem of VAT will help unknot the challenges facing these income-generating policies, which are the nerve centre of developing economy in today's global market and find out its prospects for national revenue policy formulation.
- iii. Finding from the study will help contribute to Ghana's revenue generating policies by restructuring the tax administration policies regarding VAT

It was envisaged that the findings from research would to a large extent serve as a basis for further research by economists and the Revenue Agencies Governing Board to advice the government whether to maintain or increase the VAT rate.

It is also to help broaden the knowledge of interested parties, institutions, and companies about the VAT system and the impact it has in the revenue mobilization in Ghana and prevent citizens from evading VAT.

1.5 THE SCOPE OF THE STUDY

The study was limited to the Revenue Agencies (i.e the VAT Office) in Kumasi in the Ashanti Region. Issues of VAT administration in Ghana, implementation, introduction, challenges and prospects in line with tax administration policies in Ghana will be discussed

The study will also look at the measures proposed to ensure the smooth operation of the VAT system having regards to the economic and social impact that the system might generate from 2005 to 2010 fiscal year.

1.6 LIMITATIONS OF THE STUDY

Difficulty in gaining access to relevant information that pertains to the study.

- i. Failure on the part of respondents to complete the questionnaires administered to them because it related to tax.
- ii. Financial constraint was also be a problem to the study since we had to go round the Municipality for information needed to complete the work.
- iii. Illiteracy and ignorance on the part of the respondents was another factor that hindered progress of the study.
- iv. Time constraints were also a limiting factor.
- v. Despite all these limitations the researchers wish to state that the findings remain unbiased.

1.7 METHODOLOGY

The sources of data used for the study were both primary and secondary data. The primary data were the response from questionnaires received from respondents and also interviews in the form of formal and informal interviews used. The primary data has been the convenience sampling procedure. The secondary data on the other hand were gathered from books, journals and public notices from the VAT services.

1.8 ORGANIZATION OF THE STUDY

The study is organized into five chapters.

Chapter one reviews the introduction and the background of the study , statement of problem, purpose of the study, research questions, significance of the study, limitations, methodology and organization of the study.

Chapter two looks at the literature review.

Chapter three is centered on the methods that were used in gathering the data thus the methodology.

Chapter four covers the analysis and findings of the data.

Finally, chapter five provides the summary, conclusions and recommendations

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

This chapter looks at the critical issues involving the implementation and effective monitoring of VAT as a system of taxation. It explores the relevant generic problems levelled against the VAT system as an integral part of the revenue machine of developing economies which have resorted to it.

2.2 TAXING INCOME OR TAXING CONSUMPTION

The difference between consumption VAT and income VAT emerges from the treatment of capital depreciation (Bahitia, 1998). If a firm is allowed to deduct the entire credit when the capital equipment is purchased, the system is termed as consumption VAT. If the firm is allowed to deduct the credit as the equipment depreciates over time, the system is termed as an income VAT. There is a conventional belief that taxing income entails higher welfare (efficiency) cost than taxing consumption (Tanzi, 2001). According to proponents of this idea, the reason for this is that income tax, which contains elements of both a labour tax and a capital tax, reduces the taxpayer's ability to save. The argument is that increasing income taxes should not be considered a viable option on the grounds of both policy (because of their perceived negative impact on investment) and administration (because their revenue yield is less certain and less timely than that from consumption tax). On equity grounds, on the other hand, taxing consumption has traditionally been thought to be inherently more regressive (that is harder on the poor than the rich) than taxing income. Data from industrial and developing countries show that the ratio of income to consumption taxes in industrial countries has consistently remained more than double the ratio in developing countries (that is compared with developing countries, industrial countries derive proportionally twice as much revenue from income tax than from consumption tax).

2.3 THE ORIGIN OR DESTINATION PRINCIPLE

The choice between the origin or destination principle is made in taxing international trade (Riswold, 2003). A VAT is said to use the origin principle when it taxes value that is added domestically to all goods, including goods that are subsequently exported, but does not tax value that has been added abroad and is embodied in goods that are imported and sold domestically (Gills et al, 1990). Under the origin principle, therefore, exports are taxable and

imports are exempt. This regime is compatible with the income VAT. On the other hand a VAT is said to use the destination principle when it taxes all value added, at home and abroad, to all goods that have as their destination in the consuming country (Gills et al, 1990). In this case, therefore, exports are exempt and imports are taxable. While the destination principle is well-suited to the consumption VAT, the origin principle is compatible with income VAT.

The destination principle is used by central governments in most occasions. It is argued that the preference for the destination principle may be due to the general preference for the consumption VAT and a mercantilist inclination to emphasize economic activity (employment) more than consumption (Gills et al 1990). The choice between the destination and origin principles will influence the choice of the method for computing the amount of tax

2.4 THE INVOICE CREDIT METHOD OR SUBTRACTION METHOD

The VAT system has to also choose between two methods of computation for determining VAT liability. These methods of computation are either the invoice credit method or subtraction method (Riswold, 2003). With the invoice credit method, VAT is charged and paid on invoices, thus the producer will remit the difference between VAT received and VAT paid. The subtraction method uses company accounts to determine VAT liability by subtracting taxable receipts less taxable purchases to obtain total value added. In other words, the subtraction method of computing a firm's VAT calls simply for subtraction of total purchase from the sales of the firm in question and the balance, the value added by this firm, is then subject to the VAT rate. The invoice credit method is preferred and is used throughout the Sub Saharan Africa (Riswold, 2003). Further, it is widely accepted that the transactions based on invoice credit method provides several advantages such as the ability to deal with different rates and minimizing tax evasion by providing an audit trail. It is no wonder that this approach is what Ghana uses.

2.5 PRODUCT FIRMS, OR SECTORS TO BE FREE OF VAT

Certain products and services are often freed from the value added tax (Gills et al, 1990). This is because they are to be exported (destination principle) because they are important items in the budgets of low-income families (food), or because they create benefits for society in general (education).

Certain firms are commonly freed from VAT on all their sales because the administrative and compliance costs are large compared with the tax revenue to be obtained (Gills et al 1990).

Compliance costs refer to how much does it cost the taxpayer to comply with the tax law quite aside from the tax itself. For example, all firms whose annual sales are less than a specified amount may be excluded.

Financial firms, especially banks and insurance companies, are commonly free of VAT because the value they add cannot be readily defined and computed (Gills et al, 1990). In certain other service industries, all firms are free of tax for the same reason. Whole sectors of the economy, retailing, for instance, may be left outside the scope of the VAT, chiefly for administrative reasons. The schedule 1 of the VAT act in Ghana enumerated categorically, supplies such as animals and livestock, goods for the disable, educational services, crude oil, transportation, land and building and construction, financial services(details given in the definition of terms) as exempts in supply.

2.6 EXEMPTION AND ZERO RATING

As the name indicates, exemption means no VAT is charged on the supply and no credit can be taken for VAT paid on purchases used to make the supply while zero-rating means the supply is charged with a VAT at zero percent (0%) but credit can be taken for VAT paid on purchases used to make the supply. Exemption of an entire firm on all its sales is allowed usually because the firm is below a certain size and in order to facilitate administration or compliance (Gills et al 1990). The aim of zero-rating, on the other hand, is to lift the entire VAT, including that already collected at earlier stages, from a particular good or service. This is accomplished by allowing full credit for the tax shown on the invoices for purchases of the good in question or of inputs into it. It is argued that exemption should be granted where the lawmaker would rather not free the firm, but feel compelled to do so owing to administrative and compliance difficulties while zero-rating is to be given when the purpose is to lift the VAT completely from a good or service, for social or economic ends (Gills et al 1990).

Zero-rating is often said to be unsuitable for developing countries just because it may require tax refunds (Gills et al, 1990). This is quite a weak argument since tax refunds are important in establishing fairness for tax authorities in these countries. One line of argument against exemption is that it complicates administration, erode the tax base and distort input-choice decisions and hence they have to be kept to a minimum (Gills et al 1990) According to

proponents of this argument where exemptions have been almost entirely eliminated (as in Chile), the VAT has been much easier to administer and therefore quite successful. Exemptions, according to these proponents, require additional record keeping to segregating taxable from exempt sales and in practice the destination between what is exempt and what is taxed is often questionable or subjective. Some items are exempted to improve the distributional impact of the tax-a potentially reasonable tradeoff while others might be exempted for administrative or political reasons. This is exactly why developing countries exempt particular commodities as they are influenced more by distributional objectives than administrative concerns.

Administrative issues are more important under zero-rating (Gills et al 1990). Since zero-rating increases the number of VAT refunds, most developing countries astutely have limited it to exports. In addition, tax administrations in such countries are poorly equipped to handle refunds of any kind, and adding to the number of refunds would divert administrative resources from enforcement of the VAT.

2.7 SINGLE OR MULTIPLE RATES (RATE STRUCTURE)

Many countries employ multiple rates apart from a zero rate in their value added taxes. Multiple rates offer a great opportunity to fit the VAT to various social and political ends (Gills et al, 1990). A low rate, rather than exemption or a zero rate, is sometimes granted to necessities, and luxuries may be subject to a rate higher than the standard. One line of discussion commonly raised in this regard is what should be the standard VAT rate (Gills et al 1990). Some traders and tax administrators claim that standard rates of 18-20 percent are unenforceable in developing countries. According to these persons, high VAT rates provide such strong incentives for evasion that tax enforcement become all but impossible given the scant administrative resources available in developing countries. Other critics support this line of argument also. To say that high rates tend to distort the allocation of resources because they help inefficient enterprises by charging VAT on their sales and not paying the tax to the government that allow failing businesses to continue to operate. Some opponents of high rates even advocate repealing the VAT and returning to a cascade turnover tax which could provide abundant revenues with much lower rates. Some critics oppose this idea of high VAT to be unenforceable in developing countries. Their line of argument is two fold (Gills et al 1990). First, both Brazil and Chile have had considerable success in implementing a VAT with a standard rate of around 18-20 percent. Secondly, in developing countries a substantial

proportion of VAT revenue is collected at the import stage and a large percentage of the rest is collected from relatively few enterprises and hence, in these circumstances, there is little scope for improving compliance and revenue in the short-term through reductions in the standard VAT rate which merely result in an immediate loss of revenue.

There are also critics that say that enforcing of either high or low VAT is unlikely to be so without effective administration (Gills et al, 1990). According to these, scarce administrative resources must be aimed at carefully chosen objectives to ensure an appropriate level of compliance especially when the standard rate is raised to meet short-term revenue needs. This means, the administration has to act quickly and effectively so that the increase in VAT rate can yield the desired revenue. This is because even large enterprises may fail to pay the tax if they are experiencing financial difficulties owing to a general downturn in the economy (Gills et al, 1990).

Experience in both industrial and developing countries suggest that a VAT imposed at low rates may not be worth the administrative and compliance costs involved in the switch to the VAT (Gills et al, 1990). The most comprehensive governmental survey of VAT options for the US also concluded the VAT is not a tax to impose at low rates, because of the additional investment in tax administration that would be required before and during the first few years of operation of the tax.

Many developing countries have adopted two or more VAT rates. Multiple rates are politically attractive because they ostensibly though not necessarily efficiently serve an equity objective, but the administrative price for addressing equity concerns through multiple VAT rates may be higher in developing than in developed countries (Gills et al, 1990). In Ghana the rate has been adjusted to 15% which include NHIL (2.5%) and a portion to the GETFUND for political promise fulfilment since these portions were directed to this areas, it however looked politically magnetic.

2.8 THE NEED FOR VAT

Value added tax is required mainly to prevent cascading, that is, to avoid taxing any ingredient of the final product more than once (Gills et al, 1990). For example, if tax is imposed on a sale by a steel manufacturer to an automobile manufacturer and again on the full value of the automobile when it is sold to a wholesaler or retailer, the steel ingredient is

taxed twice. Alternatively, cascading occurs when a tax on inputs is not refundable and charged again on output.

It is said earlier that one of the requirements for an efficient tax system is the fact that the tax levied should be in proportion to the level of income. VAT fulfils this requirement in that its burden is shared among all residents, each according to his level and type of consumption. Moreover, it has the advantage of reducing the cost of production of industries through its inherent refund system and the fact that it does not burden exports.

The need for VAT also emanates from the very weaknesses of the sales tax that it is intended to replace (Purhoit, 2000). Firstly, sales tax has a cascading effect as a result of the fact that it is levied on the gross value without allowing any credit or set-off for the taxes paid on inputs. As a result, consumer prices will increase by an amount higher than what accrues to the exchequer by way of revenues from it. i. Besides, there is the problem of multiplicity of rates which not only dulls the progressive effects that are anticipated but also generates the need for further calculations by the sellers and increases the cost of compliance with little effect on revenue. Further, it is prevailed by the characteristic of heterogeneity which arises from the fact that apart from general sales tax, most states levy an additional sales tax or a surcharge. Additional tax is based either on their total turnover or on the graduated turnover with different rates for different slabs of turnover. What is more, the existing system of taxes militates against ancillary industries and encourages them to produce more and more of the inputs needed rather than purchase them from ancillary industries. Last but not least, the existing system of commodity taxes is non-neutral thus; it interferes with the producer's choice of inputs as well as with the consumers' choices of consumption, thereby leading to severe economic distortions.

It is argued that VAT would take away all the above problems and would avoid the distorting economic effects (Purhoit, 2000). This means, for example, it would not cause cascading, nor would it cause vertical integration of firms. Also it offers total transparency of the incidence of tax as VAT is a multi-stage sales tax levied as a proportion of the value added. A very important advantage quoted in favor of VAT is that of lesser tax evasion (Bahitia, 1998). This happens because the tax is divided into parts and therefore the incentive to evade tax by any firm is reduced. If a firm understates its output, it will be caught by the disclosures of the firms buying inputs from it. It is also claimed that VAT is conducive to efficiency since a

firm is not exempted from its tax liability even it runs into a loss (Bahitia, 1998). Moreover, as it pays a tax not on its profits but on the value produced, it tries to improve its performance and reduce the cost of production.

2. 9 VAT ADMINISTRATION

The major activities in VAT administration are identifying taxpayers, processing returns, controlling collections, making refunds, auditing taxpayers and levying penalties. On the part of administration, it is a prior task to identify the taxpayers. In this connection, preparation of a single master file, based on unique Tax Identification Number (TIN) is crucial and this ensures that each taxpayer's account contains all the relevant tax and payment data for that taxpayer alone (Grandcolas, 2003). The TIN system is registration mechanism in which a taxpayer is given a single identification number to be used in administering all taxes. The TIN system encompasses personal and business profiles of the taxpayers including full name, address, business information (like annual turnover), banking information (whether he or she has a bank account), and the number of branches, contact address and related information. Different business entities owned by one company or person is categorized under one TIN number. This will avoid duplication and falsification of addresses and information serving as a pretext upon the default. In addition, the TIN has to be feasible for comparison among different taxes such as sales tax and the income tax (including tax on corporate income). The TIN system has the advantages of aiding to draw a comparison of tax statistics with the national accounts, facilitating proper use of the database of various systems and enhancing the financial recording system of the business communities.

On account of the requirements of VAT, the even functioning of VAT would perilously depend upon taxpayers keeping careful and complete records (Purhoit, 2000). To minimize the likely amount of high compliance costs, however, sellers are expected to maintain sufficient details to have information on the following aspects (Purhoit, 2000). These are particulars of invoices giving details of tax on sales and credit on purchases, details of accounts giving information of all purchases and sales and interaction between invoices, purchase and sales accounts with the tax return form.

The other part of VAT administration is assessment on VAT execution. This includes identifying taxpayers and tax evaders as well as the registered and unregistered taxpayers among the business community. It follows that the concerned tax authorities would take legal

measures against people who do not comply with the VAT law, for example, on those who conceal invoices and engage in illicit business transactions. It is not only the authorities who should be responsible in assessment of execution of VAT but the consumers themselves have a key role to play.

The human resource element is essential in VAT administration. Trained personnel are what actually most developing economies lack and this has forced them, for instance, to organize their VAT activities under existing tax administrative structures. Consumers need to make sure that businesses that levy the tax are registered with the VAT administration as evidenced by a registration certificate which is expected to be posted visibly on the establishment's premises, they should receive receipts for the goods and services they purchase and they have to make sure that the receipt clearly indicates the VAT registration number and the taxable items.

Key decisions that must be made before introducing a VAT concern the choice of organization to administer the tax and the organizational changes required. Nearly all developing countries that apply a VAT through the retail stage have assigned its administration to the same organization that administers income taxation, which usually also administered the taxes that the VAT replaced.

2.10 SCOPE OF VAT

The history of taxation reveals that no other tax has swept the world in more than thirty years from theory to practice. The economic and technological changes of the second half of the century have made VAT quite an essential modern tax than ever. It will not be an exaggeration if one were to say that the emergence of the VAT as an important and elastic source of revenue over the last decades is unparalleled in the history of taxation. Nonetheless, VAT as a tax has its general and local scope depending on the laws and countries within which it is adopted. Depending on the laws which establish the VAT, it may cover areas of manufacturing, processing, retailing, wholesaling among others. Some goods and services may be neither taxable nor exempt even though made by taxable person. To illustrate, supplies made outside the country or not in the course of business are outside the scope of VAT. A foreign trade which took place outside the frontiers of Ghana is outside the scope of VAT because it effectively took place outside Ghana.

2. 11 NEED FOR VAT IN GHANA

As pointed out in chapter one, developing countries have been unable to generate sufficient revenue to finance their economy. This emanates from these countries tax system which can be characterized as raising low amounts of tax revenue as a result of low amounts of per capita income, the subsistence nature of their economy (mostly in agriculture), poorly structured tax systems and weak tax administration. VAT is said to be the revenue-raising tool in the developing world. The table below shows total indirect tax revenues (taxes on international trade and taxes on goods and services) both before and after the introduction of the VAT for eight selected economies in Sub Saharan Africa. The actual year of introduction of the VAT was not used in the calculation due to some of the VAT's is being introduced at different times throughout the year. The results depicted in the table are Tax/GDP ratios both before and after the introduction of the VAT and the years in the country column are the times the VAT has first been introduced.

Indirect Tax Revenue with VAT.

Table 1

COUNTRY	3 YRS PRE-VAT AS % OF GDP	3 YRS POST- VAT AS % OF GDP
Benin(1991)	4.8%	7.4%
Burkina Faso(1992)	7.0%	7.2%
Gabon(1995)	7.6%	7.6%
Guinea(1996)	9.6%	8.8%
Kenya(1990)	13.5%	15.0%
Togo(1995)	6.3%	9.3%
Uganda(1996)	14.5%	14.7%
Zambia(1995)	11.7%	12.3%

Source: World Development Indicators 2001

The introduction of VAT has made different impacts on the eight selected countries as can be observed from the Table above. While the effect is neutral for countries like Burkina Faso, Gabon and Uganda, the introduction of VAT has made tremendous impact on the economies of Benin, Kenya and Togo.

The VAT is progressive in its incidence, and the higher revenues brought about by the VAT can provide additional funds for poverty-reducing spending, including primary education (Munoz and Cho, 2003).

The application of the VAT system has been necessitated by the following reasons

- i. Ghana's total revenue from excise tax and sales tax account only for 17% and 14% of the GDP
 - ii. The sales tax did not allow collection of the tax on the added value created wherever sales transaction occurred
 - iii. The value added minimizes the damage that may be caused by attempts to avoid and evade the tax and helps to ascertain the profit obtained by taxpayers
 - iv. Value added taxation enhances savings and investment, as it is a consumption tax
- Replacement of the sales tax by value added tax enhances economic growth and improves the ratio relationship between government revenue and gross domestic product. Same line of argument can be proposed in introducing VAT i.e. the deficiency in sales tax. The sales tax base in Ghana was narrow because it was limited to imports, manufactured goods and a few selected services (Terkper, 1996). Because credit was given only for taxes paid on raw materials, the tax had a cascading effect, distorted efficient resource allocation, and thus impeded economic growth. Hence, in comparison to the sales tax, the VAT taxes services in addition to production, grants zero-rating to exports and gives exemptions to fewer basic products.

2.12 VAT ADMINISTRATION- GHANA'S CASE

According to Section 5 of the Value Added Tax Act, any person who carries on a business activity which makes it remittable as a taxable person can apply for registration. An applicant shall make the application within 30 days of becoming registrable by filling the appropriate VAT Registration Form.

The law on VAT in Ghana, the VAT Act 1998 (Act 546) by its structure, however provides some features that tend to enhance business productivity and thereby encourage investment. The important features are the provisions relating to exemptions, zero rating, relief as well as some special dispensations put in place for the administration of the tax. The VAT Act requires that a person who carries on taxable activity and is not registered is required to file

an application for VAT registration with the VAT Service if at the end of any period of twelve calendar months the person made, during that period, taxable transactions the total value of which the total value is greater or equal to ninety thousand Ghana cedis. When a person carrying out taxable transactions files an application to be registered for VAT, the Commissioner is required to register the person in the VAT register and to issue a certificate of registration within 30 days of the registration. After the application for registration has been made, the VAT Service, will give VAT registration and Tax Identification Number (TIN). The Authority shall issue a VAT registration certificate containing such details as the full name and other relevant details of the registered person; the date of issuance of the certificate the date from which the registration takes effect; and the registered person's taxpayer identification number. This is followed by a certificate of Registration that has to be displayed at the main business premises.

A person registered for VAT that carries out a taxable transaction is required to issue a VAT invoice to the person who receives the goods or services. A VAT invoice is a document executed in the form stipulated by the VAT Service and containing the following information: Full name of the registered person and the purchaser, and the registered person's trade name, if different from the legal name, taxpayer identification number of the registered person and the purchaser, number and date of the VAT registration certificate, name of the goods shipped or services rendered, amount of the tax payable transaction, amount of the excise on excisable goods, sum of the VAT due on the given taxable transaction, the issue date of the VAT invoice and serial number of the VAT invoice.

The products that are exempted from VAT in Ghana are: the sale, transfer or lease of immovable property; the rendering of medical services; the rendering of educational services; the supply of electricity and water; post office operations and the provision of public transport permits and license fees. The design of the VAT includes concessions to small scale business to lessen the administrative burden, such as the relief from the requirement to register to collect VAT. Zero-rated supplies include the supply of export of goods and services. Taxpayers who have the obligation to maintain books of accounts shall have to register with the VAT Service, type and quantity of vouchers they use before having such vouchers printed. Any printing press before printing vouchers of taxpayers shall ensure that the type and quantity of such vouchers is registered with the Tax Authority. The VAT Service shall be empowered to investigate any statements, records and books of account submitted by any

person at any time by sending duly accredited inspectors to check the statements, records and books of account, or any vouchers, stocks or other material items at the person's place of business or practice; requiring the person or any employee who has access to or custody of any information, records or books of account to produce the same and to attend during normal office hours at any reasonable convenience tax office and answer any questions relating thereto; and requiring any person including a municipality, body, financial institution, department or agency of Local government or District Assembly to disclose particulars of any information or transactions.

The VAT in Ghana employs the invoice - credit method as the basis for VAT as only the value added at each stage of the transaction is subject to the tax. The rate introduced was 12.5% and later adjusted to a uniform rate of 15 percent (including 2.5% to NHIL) on most goods and services, with a zero rate on exports and exempted goods and services. The scope of exempted goods and services differs from that under the sales tax.

2.13 IMPLEMENTATION PROBLEMS

Ghana shares developing countries' problems in their effort to establish efficient tax systems in general (Terkper, 1997). Firstly, most workers in these countries are typically employed in agriculture or in small, informal enterprises and this means the possibility of regular or fixed wages is rare as they receive cash payments (i.e., off the books) that further means difficulty to calculate the base for an income tax (Otioku, 1988). Related to this, as most of the workers do not make transactions in large stores, the role played by income taxes and customer taxes is limited and little possibility exists for the government to achieve high tax levels. Secondly, It is difficult to create an efficient tax administration without a well-trained staff, when money is lacking to pay good wages to tax officials and to computerize the operation (or even to provide efficient telephone and mail services), and when taxpayers have limited ability to keep accounts. Thirdly, because of the informal structure of the economy in many developing countries and because of the financial limitations, statistical and tax offices have difficulty in generating reliable statistics. This lack of data prevents policymakers from assessing the potential impact of major changes to the tax system. As a result, marginal changes are often preferred over major structural changes, even when the latter are clearly preferable. This perpetuates inefficient tax structures. Finally, Income tends to be unevenly distributed within developing countries. Although raising high tax revenues in this situation ideally calls for the rich to be taxed more heavily than the poor, the economic and political power of rich

taxpayers often allows them to prevent fiscal reforms that would increase their tax burdens. This explains in part why many developing countries have not fully exploited personal income and property taxes and why their tax systems rarely achieve satisfactory progressivity (in other words where the rich pay proportionately more taxes).

Alternatively, it can be said that the whole tax system in Ghana is faced with such problems as unsatisfactory level of record keeping and administration inefficiency, lack of sufficiently educated/informed taxpayers, there is high cost of tax compliance, extensive evasion, over-zealous and corrupt tax officials (Daily Graphic, July 7, 2005, The Lens, July 6, 2005) and extremely narrow tax base-in many of the countries; twenty to thirty (20-30) large businesses account for two-thirds of the country's tax revenue.

It is obvious that the introduction of any new tax scheme will invariably be met with reservations and mixed reactions from the general public in any country, irrespective of the country's socio-economic status or its level of development. Because VAT is a new and sophisticated tax that differs significantly from the classical tax schemes with which the people were familiar, various misconceptions regarding its impact, its application, and its benefits to the national economy are normal in the initial phase of its application. Several well-meaning but insufficiently informed individuals, or otherwise people with ulterior motives, have misled the public into thinking that its impact is cumulative and claimed that its effect on consumer spending would go far beyond even the 12.5% percent flat rate that the tax imposes which led to many social tensions in Ghana at the initial attempt.

While VAT has been adopted in most developing countries, it frequently suffers from being incomplete in one aspect or another (Riswold, 2003). Many important sectors, most notably services and the wholesale and retail sector have left out of the VAT net, or the credit mechanism is excessively restrictive (that is there are denials or delays in providing proper credits for VAT on inputs), especially when it comes to capital goods.

Munoz and Cho's study on the social impact of tax reform in Ethiopia for example, has indicated that the effective sales tax rates are lower than the effective VAT rates, since many goods and services had lower rates under the sales tax (2003). The replacement of the sales tax in Ghana by the VAT was perceived to have increased the tax payment burden for the average household. The study has further revealed that the sales tax was more progressive

than the VAT (Munoz and Cho, 2003}. In sum, this is true because the VAT has fewer exempt items, and these items are not disproportionately purchased by the year. The VAT is more efficient, but it does shift some of the relative burden of the tax on the poor. The other problem commonly observed is that some of the taxpayers refuse to honor their debt obligations to the VAT service while others submit their VAT returns without payments. There is also deliberate submission of nil returns, non-issuance of VAT invoices and entertainment providers and lotto operators refuse to use the VAT coupons.

The problems of introducing a VAT depend in large measure on whether the country has had previous experience with general sales taxes, the nature of the taxes that the VAT will replace, the effectiveness of the tax administration, the lead in time and the structural features of the VAT (rates, exemptions and treatment of small tax payers).

Administrative considerations have greatly influenced the structure of the VAT in Ghana. Because a single-rate VAT is easier to administer than a multiple rate VAT, the former has been applied. The complexity of administering full exemptions (zero-rating) has led to restrict them to exports. Small taxpayers have been dealt with by exempting those with gross sales below a certain threshold or by taxing them under a simplified system. Because of the difficulty involved in taxing service, the VAT is imposed on selected services only. Insufficiency of resources leads administrators to concentrate their enforcement efforts on large taxpayers, which can encourage non-compliance among other taxpayers.

2.14 PROSPECTS OF VAT IN GHANA

The government has embarked upon major tax reform program after the Economic Recovery Programme that will have a substantial impact on the economy of the country. The introduction of VAT has been a major part of the tax reform program since 1999 to replace a number of non-performing taxes especially the sales tax. VAT after reintroduction has been a major talking issue in recent times by the business community, writers, the government and other members of the society due to the impressive performances it has demonstrated. Many advantages have been attributed to the system. Few among the lot were:

2.14.1 Strengthening the System of Collecting Taxes

In spite of the high cost associated with VAT, administratively it is realized that VAT offers a simpler form of tax collection .VAT by nature aids tax enforcement by providing audit trail

through different stages of production and trade. Under the VAT system the tax paid by registered firms on purchases and expenses (input tax) can be deducted from the tax charged on sales (output tax). However this deduction can only be done if the business is registered and can produce an invoice showing that it paid the VAT hence businesses making regular purchases will insist on getting an invoice to enable them take the input tax credit. Thus, it acts as a self - policing mechanism.

2.14.2 Promotion of Exports

The operation of VAT allows exports from country of origin to be zero rated. By implication VAT on exports are rebuffed whereas VAT is charged on import from other countries. The effect of this is that export commodities from VAT practicing countries are cheaper compared to similar goods from non-practicing countries. VAT particularly improves export competitiveness of local industries due to the 'zero rating' of exports.

On the other hand, VAT is charged on imports from other countries and causes the cost of such products to be higher. This acts as a disincentive for imports from non-VAT practicing countries. As a result, such countries react to the situation by putting in place measures to neutralize the effects which may not auger well for international trade though.

2.14.3 Spreading the Burden of Tax in a Fairer Way

Adam Smith in his book 'Wealth of Nations' propounded that one of the principal canons of taxation is that of equity which seek to treat all tax payers fairly. VAT encompasses a system of implementation of a uniform taxation which is spread over a wider base than what prevails under sales and service tax systems. This means that taxpayers will not be treated differently. Most tax systems (e.g. Personal income tax and import duty) are deliberately designed to make high income earners pay a higher rate of tax. This is not the case with the sales and service tax regimes which excludes most expensive services such as video rental, telecommunication etc from the tax regime making the system rather harsh and inequitable to those paying tax on less expensive goods hence the need for an effective expenditure tax to cover many goods and services to make it fair to all taxpayers.

Previous discussions have clearly indicated that with efficient administration and commitment, there is a bright prospect for effective implementation of VAT in Ghana. In developing nations, the VAT has tended to be something of a money machine. It has been

found out that in Argentina, Chile, Costa Rica, Korea and Indonesia, for example, the ratio of revenue to GDP grew by at least 50 percent within the first three years of the VAT's adoption, compared with revenue from the indirect taxes replaced by the VAT. This is a clear indication that Ghana can implement the tax with minimal risk of revenue loss and with some expectations of fairly strong revenue growth.

The VAT taxes each stage of value added only once, at the stage where it is added. The VAT's neutrality in so far as production efficiency is concerned is that it taxes productive inputs equally and does not promote distortion of production choices. The consumption type of VAT does not distort the choice between consuming now and consuming later, in favor of the former, as does the income tax. This means the VAT does not penalize, as does the income tax, capital accumulation and economic growth.

VAT like other revenue mobilization system relies greatly on proper and effective accounting records kept by operators. This feature if missing may render the operation of the VAT far from success. Seasoned tax and economic experts such as Seth Terkper and Nii Moi Thompson have spoken strongly against the low revenue generation of the VAT service and the potential of the service to generate huge revenues for the state. Records keeping of the stakeholders have been poor and nothing to write home about as it is discussed all over the country. This study sought to investigate all these challenges to prove them or otherwise.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 INTRODUCTION

This chapter examines the research methodologies that will be used for the research work. Thus, research methodology involves the procedures followed in realizing the goals and objectives of the research study. It concentrates on the various methods used in collecting the necessary data for the purpose of the study.

In conducting research, there is the need to gather and collect data by using various tools with the aim of analyzing them into useable information for decision making.

It gives enlightenment into how the data gathering instruments were designed, administered and the various methods employed for the data analysis. This chapter also defines the sample size of the study as well as the variables that are used to analyze the data collected.

3.2 DEFINITION OF VARIABLES.

The variables considered were the challenges and prospects inherent in the operation and administration of VAT in Ghana. This definition is triggered by the fact that VAT has been the bane of many developing economies for that matter Ghana.

It is now one of the necessary fulcrum and prospect to sustain it for development. The VAT service, which is entrusted by law with the mandate of administering, was used as a case study to elicit the efficiency and the effectiveness in their administration of tax in Ghana.

3.3 SOURCES OF DATA

Two sources of data collection used for gathering the necessary information that is needed for effective writing of this research work. These sources were the primary and the secondary data.

3.3.1 Sources of Primary Data.

The primary data was taken from:

- i. Personnel at the local VAT offices (LVOs) - Kumasi
- ii. Consumers
- iii. Agents (Retailers, Wholesalers, Manufactures and Service providers)

3.3.2 Sources of Secondary Data.

The secondary data was taken from various sources such as:

- i. Library materials
- ii. Internet (search engines and websites)
- iii. Brochures on VAT
- iv. The VAT act, 546 of 1998.
- v. Articles and publications on VAT.

3.4 DATA COLLECTION

3.4.1 The Primary Data.

This was collected using self administered questionnaire and interviews to obtain first hand information on how the VAT system is operated in Ghana.

3.4.2 Preparation of Questionnaire

The questionnaire to solicit inputs on the variables examined to gather people's perception on the tax system. The population consisted of two main identifiable groups thus producers of goods and services, consumers and the regional VAT office.

3.4.3 Interview

The management team from the regional office in Kumasi was interviewed to ascertain their views on the administration of VAT. Officials from the VAT service were also interviewed to know the trends regarding VAT administration through a written interview guide.

3.4.4 Data Gathering Instruments and Questionnaire Administration.

The questionnaire was used in gathering data for the study. Three questionnaires were designed to solicit the views of:

- i. The consumers.
- ii. Operators(Retailers, Wholesalers, Manufacturers and Service providers) and

- iii. The regional VAT office in Kumasi on the key issues raised in the questionnaire.

3.4.5 Secondary data

The secondary data was obtained from textbooks, business journal, brochures, internet, and publications newsletters which were relevant to the study.

3.5 SAMPLE POPULATION

A sample size of 150 was selected; convenience sampling method was adopted to select respondents. The research was limited to the Central Business District the Kumasi Metropolis in the Ashanti Region of Ghana; the target population comprises the following:

- i. The VAT Service
- ii. Agents
- iii. Manufacturing
- iv. Distributors and wholesalers
- v. Consumers of all kinds of VAT rated goods and services within the Kumasi Metropolis

3.5.1 Sampling Size

The sample size is 150 to determine the number of respondents to be surveyed. The whole population could not be covered, a sample size comprising of;

- | | |
|----------------------------------|----|
| i. The VAT Service Personnel | 10 |
| ii. Service providers | 25 |
| iii. Manufacturing | 15 |
| iv. Distributors and Wholesalers | 30 |
| v. Consumers | 70 |

3.6 DATA ANALYSIS PROCEDURE

Information obtained from the questionnaire was initially classified according to the various sections for analysis which was subsequently regrouped into definite categories. These categories were then tallied manually and computed into percentages.

The responses from the questionnaires were discussed and comparisons were made to come out with suggestions, illustrations were also applied where the data analyzed involved figures and charts.

CHAPTER FOUR

DATA ANALYSIS, FINDINGS AND DISCUSSIONS

4.1 INTRODUCTION

This chapter focuses on the analyses of data collected from the field by the researchers. The data analyses are based on the research questions administered and interviews conducted. Any tax system can only be properly monitored and controlled if all the parties involved that is consumers, clients, agents and the VAT services play their respective roles effectively to ensure that the aims and objectives for which the VAT service was established could be achieved.

4.2 ANALYSIS OF DATA FROM COMSUMERS/CLIENTS OF VAT.

It is imperative for consumers to understand how the tax system operates and appreciate the reasons why taxes are imposed by government in the first place. This is expected to be achieved through education of the general populace by the VAT service, through the media, VAT seminars, flyers and speeches. This was reflected in the data gathered which shows that majority of the respondents indicated the media as the most effective means through which they acquired knowledge of VAT. Figure 1 shows the various categories of occupation represented within the sample size. The largest number of respondent fall within government institutions while less than 30 people belonging to other areas of employment.

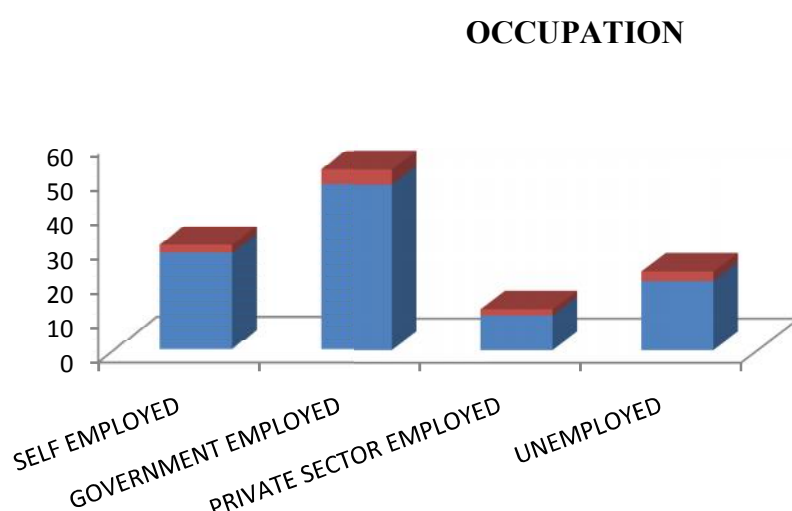


FIG. 1

HOW DID YOU GET TO KNOW VAT?

The researchers asked the respondents how they got to know of the VAT and the operations of the VAT service.

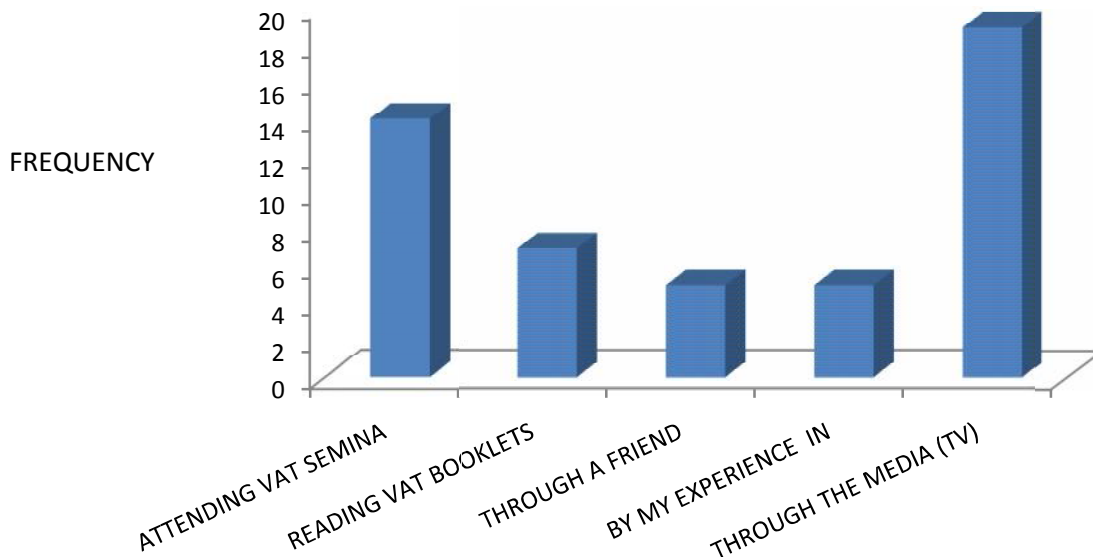


FIG 2

From the diagram, majority of the respondents said they obtained much information about VAT from the media followed by those who attend seminars. Though there seem to be a lot of dissemination of information through the media, there are still some lapses, since the education has not yielded the desired results. This is evident in the fact that most consumers claimed to have heard about VAT yet do not know how it operates.

The researchers asked the respondents whether they believe it is important to insist on seeing a vat registered certificate before vat is charged?

According to the data collected, 78% of the respondents did not know that they had to insist on VAT certificate before they can be charged VAT. Only 22% were educated enough to know that they have insist on VAT registration before they can be charged VAT.

The diagram below is the evidence of the above situation.

DO YOU BELIEVE IT IS IMPORTANT TO INSIST ON SEEING A VAT REGISTERED CERTIFICATE BEFORE VAT IS CHARGED?

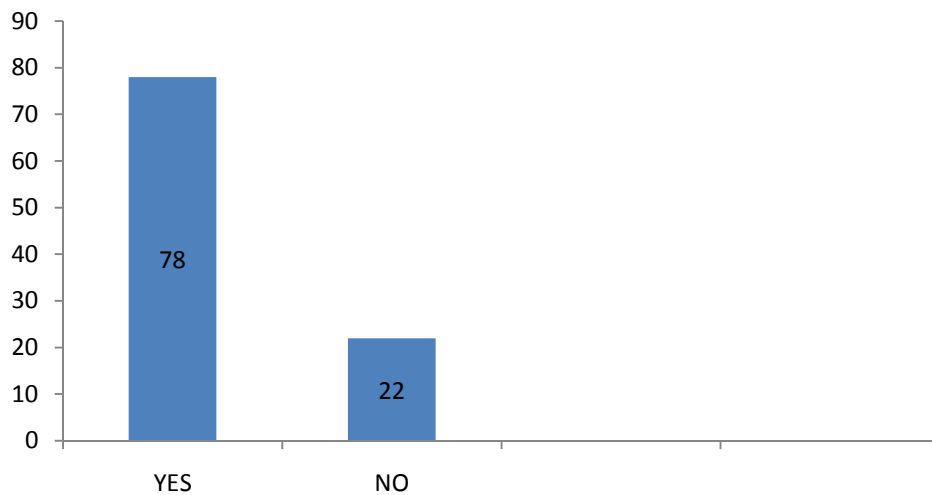


FIG. 3

To ascertain the truth or otherwise of the above situation, the researchers asked further questions on whether the consumers have an idea of how much they were paying for VAT?

The evidence was that 85% of the respondents do not even know the VAT rate that is charged by the VAT service as the chat below depicts.

DO YOU KNOW HOW MUCH TO PAY ON EVERY SERVICE OR PRODUCT UNDER VAT?

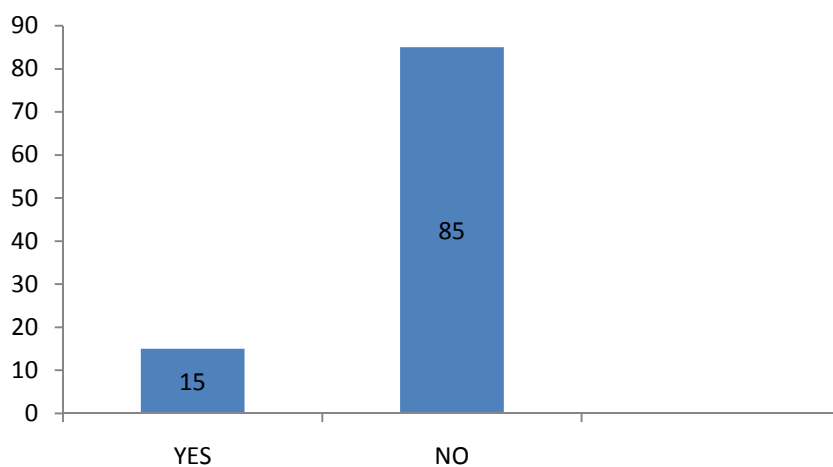


FIG. 4

The survey shows the extent of ignorance on the part of consumers on how the VAT system operates as most do not know how or when VAT is charged. The diagram above shows of how inefficient education on VAT has been since its implementation. This can be attributed to the fact that many consumers are unaware of which supplies attract VAT, who is supposed to charge VAT and do not even know that they have the right to insist on a genuine VAT invoice or receipt when they make a purchase. A further question posed during the interview of some of the consumers indicated clearly that most of the consumers have no idea how the VAT is to be computed.

The challenge this poses to the VAT service are instances where VAT agents charge VAT on exempt or zero rated supplies. The problem is further compounded when the VAT agents do not issue VAT invoices or receipts thereby causing loss of revenue to the state.

Another interview question sought to find out whether VAT should be charged on every item in order to find out the level of education gone to the consumers. Almost all the respondents said they wanted VAT to be charged only on few selected items. This is an indication that most people do not want to pay tax and more so do not know what the money is used for.

4.3 ANALYSIS OF DATA FROM VAT AGENTS

The Kumasi metropolis has seen a diverse range of business sectors over the years. The business environment is basically made up of mainly retail, manufacturing, wholesale and service industries. The majority of the businesses is concentrated at the retailing industry which consists of 45% of the total market whereas manufacturing, wholesaling and service industries only constitute 10%, 13% and 32% respectively of the entire sector. Based on the figure below, our analysis would be mainly focused on the retail industry.

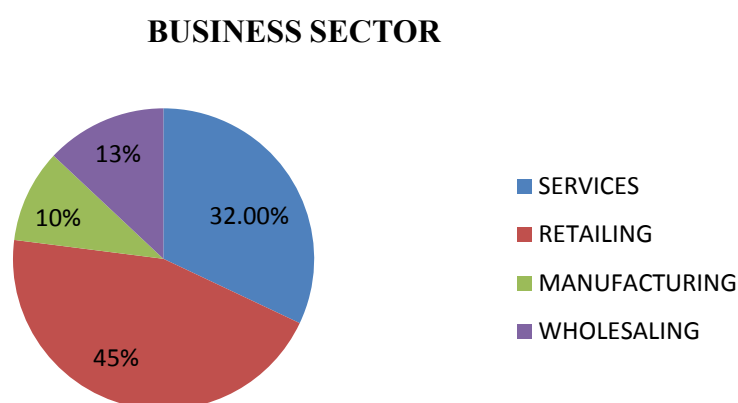


FIG.5

4.3.1 Flat Rate Scheme and the Retailers

The Value Added Tax (Amendment) Act, 2007 (Act) 734) introduced a flat rate scheme that will facilitate VAT collection in the informal retail distribution trader sector. The Act is to the effect that unless otherwise directed by the Commissioner for VAT in writing. This means that a taxable person who is a retailer of goods shall account for the Value Added Tax payable at a flat rate of 3% calculated on the taxable supply.

Thus Vat Flat Rate Scheme operators will charge Value Added Tax and National Health Insurance Levy (VAT/NHIL) on their taxable supplies at a marginal rate of 3% of the value of the supplies. The marginal rate of 3% represents the “effective rate” of tax on supplies that gives rise to net tax payable on application of the input-out mechanism of VAT. This scheme applies to retailers who fall below the threshold of GH¢ 90,000.00 hence all retailers whose annual turnover go above this threshold would have to charge the 12.5% Value Added Tax and 2.5% National Health Insurance Levy.

4.3.2 Vat Registration

The introduction of this flat rate from 2006 has also seen some challenges from the retail industry. Most agents on VAT do not necessarily charge the rate on their supplies either due to their refusal to register for the proposed flat rate scheme or they have simply not registered their business because of fear of paying taxes.

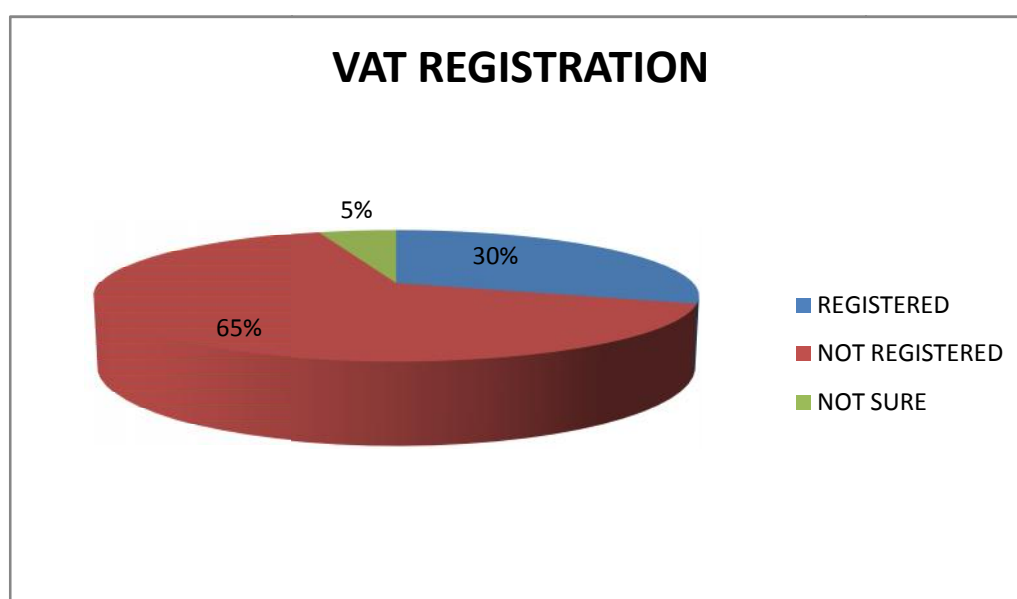


FIG. 6

The survey conducted by the researcher's shows that most retail agents in the Kumasi metropolis have not registered for the VAT certificate. From the diagram above about 65% have not registered for VAT while 30% have registered for and are charging VAT. The remaining 5% have no education on how relevant the registration is to them and the nation. Some businesses are exempted from charging VAT because of the nature of their business for instance being a donor project or charity. The nature of their business does not require that they use their revenue to finance tax lest the government would have to refund it back to the organisation because if they are charged VAT the government would have finance it. Under these circumstances the application of the VAT relief purchase order (VRPO) is used by exempt business in the course of their normal purchase of supplies in order to be relieved of the tax burden.

4.3.3 Record Keeping

The VAT systems operate such that the collection of tax is done by agents. Thus the records kept by these operators should be very accurate and the system must run smoothly and efficiently to enable the VAT service to ascertain the true revenue each agent makes. VAT is based on a system of self assessment under which registered persons make their own declaration of the tax period each month. Control and enforcement of compliance under VAT, therefore depends on records kept by the registered businesses acting as agents of the tax authorities. Every person liable to tax under the Act is required to keep;

- i. Records and accounts of all taxable goods and services received or supplied in the course of the business including zero – rated supplies.
- ii. Records of exempt supplies made or received.
- iii. A summary of the totals of input and out tax for each calendar month.

The absence of these records can negatively affect the generation and collection of revenue. It was observed that the accounting records kept by the registered agents are largely properly kept by most businesses. This aid in revealing exactly how much input or output tax accrues to either the agent or the VAT service. The perception by the Ghanaian populace that proper records are not being properly kept is limited to the small scale retailers. The next chart shows how the agents have fared during the time of the research. (Perhaps, it still shows that there is light at the end of the tunnel since the manufacturing, wholesalers and retailers on the large scale have shown an amazing improvement in record keeping.

WHICH OF THE FOLLOWING BOOKS DO YOU KEEP?

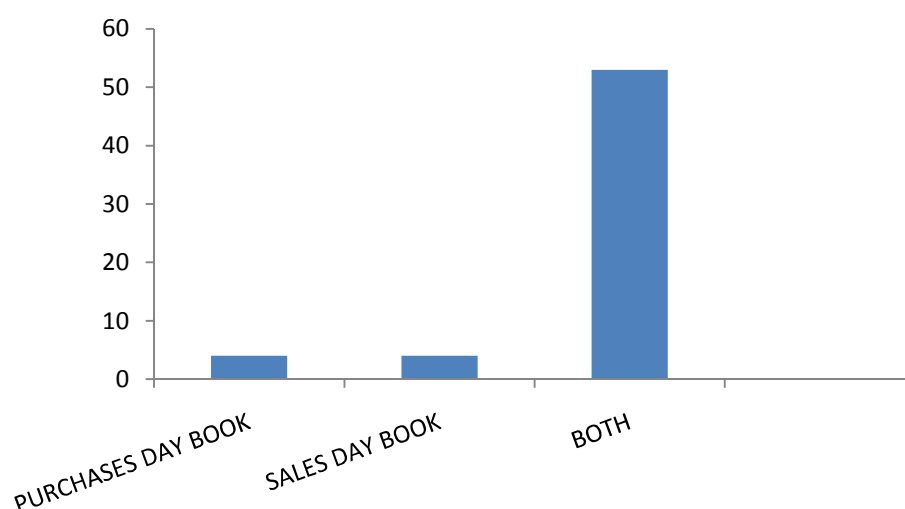


FIG. 7

Although the data above depicts a favourable picture how records are kept by agents, it still shows some grey areas. Most of the retailers confess to keeping accounting records yet do not know what their annual turnover is. When asked about how much their turnover was, most answered they did not know which goes to confirm that these businesses deliberately conceal their turnover for the purposes of not paying the appropriate tax to the state.

Most traders when quizzed on whether they insist on VAT invoices when they make purchases responded in the affirmative, however this assertion was flawed when asked when asked which of the two methods they consider as their cost price on the VAT. A large number of respondents said their cost was on materials and services whereas few claimed that it was on cost, materials and input cost incurred in arriving at the cost of sales. The VAT input tax should not be considered as part of the input in the computation of the VAT. As shown by the graph below most respondents were of the conviction that VAT has increased the cost during business this is why most business feels that VAT affects the prices of their supplies.

HOW DOES VAT AFFECT YOU?

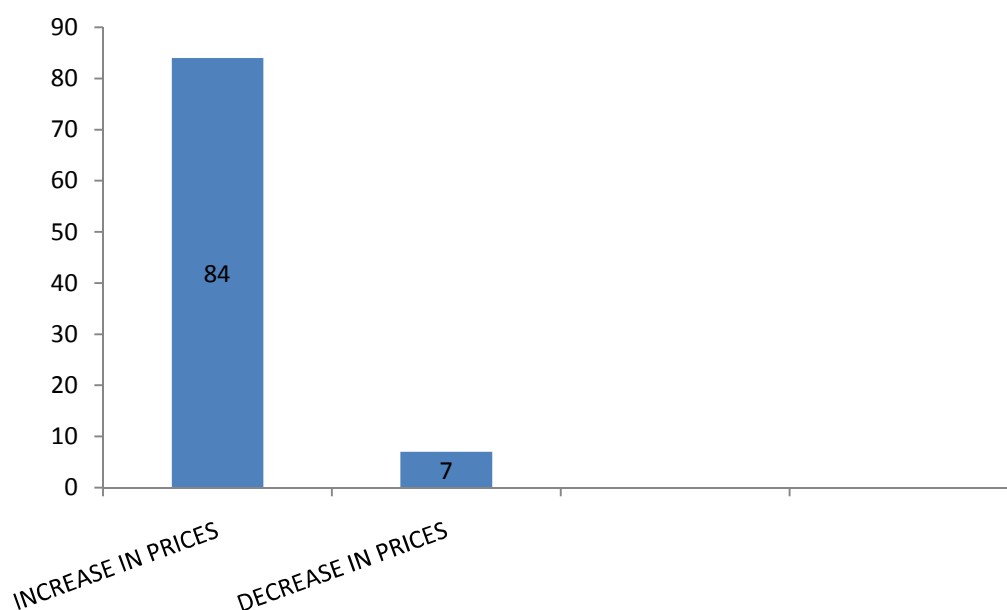


FIG. 8

Due to this mentality, traders who though are not qualified to charge VAT, but have paid VAT on their supplies tend to include VAT in their selling prices, cause an increase in the general prices of commodities and eventually price hikes. This implies that, the VAT registered person charges on the cost of its supplies before adding profit hence making their commodities more expensive than a non-registered agent. This creates an unfavourable competition between businesses of the same industry since the rational consumer would normally purchase goods at lower prices.

4.4 DATA ANALYSIS OF THE VAT SERVICE.

The pivot around which the entire VAT system operates depends solely on the VAT service. This implies that the service has to be “a pillar” on which others (i.e. the agents and consumers) would rely on for support. The research carried out revealed the service is deficient in certain areas of their operation which makes it a thing of concern. Some of the issues that could be addressed are discussed below.

4.4.1 Logistics.

Logistics can be said to mean having the right thing, at the right place, at the right time. The ever present motion by the Ghanaian populace is that most government institutions lack

needed logistics in aiding their duties. This was confirmed through this research that the VAT service is no exception. Though there is a computerised database of all registered business, there is a challenge with incorporating ICT in the collection of revenue. The reason for this is because of the non-availability of computers and intranet networks within the service. In the absence of this, the only solution for this is to manually coordinate revenue collection. With this deficiency, the service personnel were quizzed on how taxes due to the service are monitored. As expected, there are indeed software packages available but limited to just a fraction of the services.

There is a problem of vehicles transportation of VAT officials in the collection of revenue during a normal working day since only one or two vehicles are used for almost all the operation of the service, thus some VAT official are expected to work through their own means. With the large number of agents, it is anybody's guess how many would be visited within the period.

This explains why, the education on VAT to the general public has not been very effective because the necessary resources are simply not available.

4.4.2 Personnel

These are the labour force that ensures that the overall corporate aims and objectives of the VAT service are achieved. From basic economics, labour as part of the factors of production has salary as its reward. The issue with respect to the VAT service is the fact that the employees of the VAT service are not adequately remunerated and subsequently fringe benefits are woefully inadequate.

It is a well known fact that motivation is the force that can enable the staff to put in their best, yet the opposite is the case. This research has identified the reason why labour turnover from 2006 to 2009 in the VAT service is on the increase. Some of the reasons cited through the questionnaire they answered show that their salaries is nothing to write home about and their general welfare has not been addressed. Another reason why some of the employees leave the service is to take on new and challenging roles which can reward better than their present job with the VAT service.

4.4.3 Accounts/Returns

The VAT service may have its personal challenges, but it is also aggravated by the agents with whom they should be working hand in hand. Problems normally arise from some of their agents not having permanent places of business and their level of illiteracy compound the problem. There are sometimes numerous mistakes and omissions in the computations of the taxes due. Others simply would not adhere to the compliance of tax regulations. The service has on some occasion used distress actions, penalties and court orders to sanction some agents who fail to comply with the tax laws.

Records that are kept by the agents pose serious challenges to the VAT services. Most of the respondents who were asked about what problems they encounter in auditing the records of clients indicated that some businesses do not have records at all and there is lack of cooperation on the part of traders. Other VAT officials' recounted instances where some of the records were falsified and some declarations were absolutely wrong. This was also reflected in the data collected from operators when most of them claimed to have kept the requisite books by the standards of VAT but failed to state their turnover levels which presents an absurdity in the information they provided.

It was also observed that traders do not produce the needed records during field operations. They also do not keep the necessary documents and records as required by the VAT act to support the assertions they make. Traders in their bid to conceal wrong doings and take cover as well try all means possible to bribe officers who sometimes find themselves in on very helpless positions.

Even though section 29 of the VAT Act 1998, Act 546 and the VAT Regulation, LI 1546 set out standards on the records to be kept by traders, the calls from legal provisions seem to be consistently breached in their quest to maximize revenue at the expense of the state revenue machines.

The growth of national development depends largely on the how effective the system operates to aid in the collection of revenue to the government. According to CSI Global Education, there are some limitations to fiscal policy's effectiveness. First of all, it takes time to get approval for tax legislation. Secondly, it takes time for the tax policies to affect the economy after they have been implemented.

4.5 EFFECTS OF TAXES ON CONSUMERS

When the government changes its taxation policies, it changes the spending power of individuals. If taxes are increased, prices of goods increase hence consumers tend to spend less. When people decide to spend less, businesses do not make as much profit and start to cut back on their business operations. As individuals see these business cutbacks, they spend even less and the economy starts to decline. However, if the government lowers taxes, prices become relatively lower which encourages them to spend. When individuals start spending, businesses earn more profits and have money to expand. This causes businesses that are not yet registered to get their business registered which would result in an increase in their level of sales that would enhance the economy to grow. With lower prices, people continue to spend and this fuels economic growth.

The Growth of VAT with GDP in Ghana 2006-2010.

Table 2

YEAR/VARIABLES	2006	2007	2008	2009	2010
Domestic VAT	233,284,295 .60	337,019,853 .44	407,574,815 .76	508,043,534 .96	680,592,447. 17
Excise	74,726,695. 58	62,110,072. 29	58,592,828. 30	56,917,607. 51	119,147,071. 81
Comm. Serv. Tax			32,089,333. 75	87,460,414. 96	128,735,974. 75
NHIL	46,764,459. 90	67,333,957. 61	81,548,269. 25	101,608,707 .01	136,118,489. 43
TOTAL VAT	354,775,451 .07	466,463,883 .34	579,805,247 .06	754,030,264 .44	1,064,593,98 3.16

Source: VAT service

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 SUMMARY OF FINDINGS

The Value Added Tax was re-introduced in Ghana as a viable alternative to provide an efficient and effective indirect tax administration in the country. For a tax to be properly administered, it must be equitable. It is for this reason that policy makers in the country introduced the 3% flat rate scheme for retailers not exceeding GHC90, 000.00 and those retailers whose revenue exceed that amount are to charge the 15% rate.

The Value Added Tax is also based on voluntary compliance where agents are to collect the tax, conduct their own assessment make onward payment to the tax office. This is in contrast to the sales tax where much of the assessment was conducted by tax administrators. This also makes the VAT cost effective.

The implementation of VAT requires a highly literate populace, who are aware of what VAT is and how the system operates. This would enable both consumers and sellers provide an effective mechanism for checking fraudulent activities since they all know how the system operates.

It is the obligation of VAT officers to ensure that agents keep the appropriate and adequate records for proper reporting and filling of returns. The Vat officers would need these records to confirm and verify the tax due.

According to the data collected, 78% of the respondents did not know that they had to insist on VAT certificate before they can be charged VAT. Only 22% were educated enough to know that they have insist on VAT registration before they can be charged VAT.

The survey also showed the extent of ignorance on the part of consumers on how the VAT system operates most (85) do not know how or when VAT is charged.

The survey conducted by the researcher's showed that most retail agents in the Kumasi metropolis have not registered for the VAT certificate. From the survey about 65% have not registered for VAT while 30% have registered for and are charging VAT

Moreover, it was discovered that tax officials face many problems in the office. These problems have been stated as:

- i. Lack of logistics or resource.
- ii. Lack of good or conducive environment
- iii. Too many manual work
- iv. Inadequate computerized system

Again tax officials stated the following as problems they face in the field

- i. Inadequate vehicles to move around
- ii. Reluctance of taxpayers to pay their taxes
- iii. Interference from politicians and other influential people in the society
- iv. Evasion of tax
- v. Lack of co-operation from taxpayers
- vi. Disrespect from politicians and
- vii. Lack of awareness or knowledge of tax.

Apart from the problems stated above, tax officials during the study also stated other problems that affect them as:

- i. Low morale
- ii. Lack of motivation
- iii. Lack of sufficient training or refresher course for staff
- iv. Little or no recognition of tax officials' role in the development of the nation
- v. Loopholes in tax laws and
- vi. Lack of enforcement of the tax laws.

According to the study, tax officials face these problems daily and this was made known by all the 100% respondents of the questionnaire to staff.

From the study, tax officials who have been encountering problem associated with collection of tax have made the following suggestions which they believe they would help eliminate or lessen the problems they face. The suggestion included:

- i. Improvement of condition of service of tax officials
- ii. Institution of adequate and frequent training or refresher courses for tax officials
- iii. Frequent, adequate and effective tax education
- iv. Provision of the necessary logistics and resources for tax officials to work with
- v. Institution of measures to stop political interference with the work of tax officials and
- vi. Strict enforcement of the tax laws.

The taxpayers went further to state the problems they encounter, which included the following:

- i. Too many and complex tax procedures
- ii. Little tax education
- iii. Corrupt and distrustful tax officials
- iv. Little or no development from taxes and
- v. High tax assessment.

According to the study, 77% of the taxpayers said these problems influence their decision to pay or not to pay tax. They however believe that the problems could be done away with or reduced if the following suggestions are implemented.

- i. Tax payment should be made simple
- ii. Corrupt and distrustful tax officials should be dealt with very well.
- iii. Tax assessment should not be too high
- iv. Development from taxes should be improved and make known to the public
- v. There should be frequent, adequate and effective tax education.

5.2 CONCLUSION

The general conclusion drawn from the study with particular reference to chapter 2, 4 and the research questionnaire included the following.

It could be concluded that there are actually problems that are associated with collection of tax. Further conclusion could be drawn that VAT service also encounters problems associated with collection of tax.

It is the combination of these that form the problems associated with the collection of VAT in the country.

In addition, it could be concluded that the problems enlisted are similar to problems that have been unearth through research work in other places.

Moreover, it could be concluded that, lack of logistics and resource: lack of motivation, lack of frequent and adequate training for tax officials, political references, lack of strict enforcement of tax laws and lack of adequate and frequent tax education among others are the problems associated with collection of VAT in Ghana and in many other tax agencies in the world as a whole.

Apart from the above, further conclusion could be drawn that measures such as:

Improvement of conditions of service of tax officials; institution of frequent and adequate training for tax officials; frequent, adequate, and effective tax education; provision of necessary logistics and resource; institution of measures to stop political interferences; and enforcement of tax laws would help eliminate or lessen the problems associated with collection of tax.

VAT has achieved some success as compared to the sales and service tax which it replaced.

5.3 RECOMMENDATION

5.3.1 Education

The VAT service should ensure that the general public is aware of how important VAT is to the economy, how much VAT is paid on every item purchased, who should charge VAT and the insistence on seeing a Vat certificate. The education should also include goods and services that are exempted from VAT and the reasons for better understanding of how the system works. Firms and organizations that qualified to register for VAT but have not done so should be given adequate tutorials especially on issues such as VAT not affecting their profit margin and can even serve as short term finance.

5.3.2 Training of Staff

Staff may be qualified for the job alright; further training should be given them so that in pursuance of their duties, only relevant and adequate information would be sort for. Where there are human resource deficiencies, measures should be taken to acquire adequate staffs. The research and monitoring department must also ensure that officers are updated on new ways of verifying accounts and coming out with the total VAT due. Regular training and

retraining of VAT officers would ensure that agents that are conducting their operations in unacceptable ways are corrected. This would also reduce the risk of losing revenue.

5.3.3 Motivation of Agents and Staff

For the service to meet its target there is the need for it to motivate staff in terms of salary, career development, benefits and other conditions of service. Well motivated staff will call for an efficient way of generating revenue for the state.

Itinerant officers who occasionally visit the premises of registered persons to examine and verify their records would also avoid indulging in corrupt practices that would also affect the revenue to be generated. The staff should also be developed to achieve self-esteem, honesty, integrity, transparency, probity and accountability in the performance of their duties as professionals in accordance with the rules and regulations.

Agents should also be motivated by providing incentive packages such as souvenirs, commission reward or award recognition.

5.3.4 Compliance

VAT is based on a system of self assessment under which registered persons make their own declaration of the tax period of one month, but enforcement of compliance by VAT authorities is backed by law and therefore makes a greater impact in the achievement of its objectives. Voluntary compliance to tax laws or system is where agents would willingly keep proper records, file regular returns which are accurate and reliable as far as practicable. Thus if this attitude is cultivated by agents, they would comply with sections of the law that are favourable to them.

5.3.5 Effective Monitoring and Control of the Vat System

It is also recommended that the operations of agents are frequently monitored to ensure that things are done the right way. This would minimize the risk of losing revenue due. The internal control systems in the service should also be strengthened to include better supervision to ensure staffs perform their duties efficiently and effectively.

5.3.6 Effective Communication

The service should intensify communication to traders specifying issues that relate to their right and responsibility under the tax law. This would give them the confidence needed to charge VAT. This would also serve as an intervention to overcome the tendency of corrupt practices.

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APPENDIX

RESEARCH QUESTIONNAIRE FOR CONSUMERS

RESEARCH TOPIC: A STUDY OF THE CHALLENGES AND PROSPECTS OF THE VAT SERVICE IN GHANA (A CASE STUDY OF THE KUMASI METROPOLIS).

PURPOSE: THIS IS AN ACADEMIC WORK IN PARTIAL FULFILMENT OF THE REQUIREMENT FOR THE AWARD OF A DEGREE IN BACHELOR OF BUSINESS ADMINISTRATION.

WE WOULD BE MOST GRATEFUL IF THE REQUIRED INFORMATION WITH REGARD TO THIS QUESTIONNAIRE IS PROVIDED. THANK YOU IN ADVANCE.

Please tick where applicable or necessary.

Q.1 ☐ Sex

☐ Male

☐ Female

Q. 2 Level of education

☐ Below Ordinary Level

☐ Ordinary Level/SSSCE

☐ Advanced Level

☐ Professional Certificate

☐ University Level and above

Q. 3 Age group

☐ 18 - 20

☐

21 - 30

☐ 31 - 50

☐ 51 and above

Q.4 Occupation

☐ Self employed

☐ Government employee

☐ Private Sector employee

☐ Unemployed

Q.5 Have you heard about VAT?

☐ Yes

☐ No

Q.6 If your answer to Q5 is YES. How did you know about the VAT system?

(PLEASE TICK ALL THAT APPLY)

☐ Through VAT Seminars

☐ Through the media (Radio, TV, Newspapers)

☐ Through business associates

☐ Through reading the VAT brochures

☐ Internet

Q.7 Do you know how the VAT system operates?

☐ Yes

☐ No

Q.8 Do you know how much to pay on every service or products under the VAT system?

☐ Yes

☐

No

Q. 9 Do you think VAT could be charged by every trader?

☐ Yes

☐ No

Q.10 Do you believe it is important to insist on seeing a VAT Registered Certificate before VAT is charged?

☐ Yes

☐ No

Q.11 Do you think that VAT should be charged on all supplies?

☐ Yes

☐ No

Q.12 What is the reason(s) for your answer in Q.11 above?

.....

.....

.....

Q.I 3 Do you think it is important to insist on invoice anytime you pay VAT?

☐ Yes

☐ No

Q.I 4(i) If NO, why?

☐ Because Seller does not have invoice/receipt

☐ It makes no difference since price remain the same

☐ Do not want to incur seller's wrath

☐ Other(s)

(ii) If you think other(s), specify.

.....

.....

Q.I 5. How does VAT affect you?

- ☐ It reduces the quantity of supplies that I wish to buy |
- ☐ It increases the prices of the supplies that I buy
- ☐ It does not affect me

Q.I6 Do you think VAT could lead to increase in revenue to the Government?

- ☐ Yes
- ☐ No

Q.17. Do you think VAT should be phased out?

- ☐ Yes
- ☐ No

Q.18. What changes would you like to see in the operation of VAT?

.....

.....

.....

Q.19 Has the education on VAT been effective?

- ☐ Yes

☐ No

RESEARCH QUESTIONNAIRE FOR THE OPERATORS OF VAT
REASERCH TOPIC: A STUDY OF THE CHALLENGES AND PROSPECTS OF
THE VAT SERVICE IN GHANA (A CASE STUDY OF THE KUMASI
METROPOLIS)

PURPOSE: This is an academic work in partial fulfillment of the requirement for the award of a Degree in Bachelor of Business Administration.

We would be most grateful if the required information with regards to this questionnaire is provided. THANK YOU IN ADVANCE.

Q.1. Which business sector are you involved in?

- ☐ Retailing
- ☐ Wholesaling
- ☐ Manufacturing
- ☐ Services

Q.2. Have you registered your business with the registrar generals department?

- ☐ Yes
- ☐ No

Q.3. My Sales turnover for the year is with these ranges.

- ☐ Less than GH¢ 90,000
- ☐ More than GH¢ 90,000
- ☐ Equal to GH¢ 90,000
- ☐ I do not know

Q.4. Do you know about the VAT system?

- ☐ Yes
- ☐ No

Q.4(ii) If yes, how did you know about the VAT system?

(Please tick all that apply)

- ☐ Attending VAT seminars'
- ☐ Reading VAT booklets
- ☐ Through business associates
- ☐ Internet
- ☐ Through the media (TV, Newspapers, Radio)
- Others

Please specify _____

Q.5 (i) have you registered for VAT?

- ☐ Yes
- ☐ No

Q.5 (ii) Give reasons for answer in 5(I) above

.....

.....

Q.6 (i) Do you keep accounting books?

- ☐ Yes
- ☐ No

Q.6 (ii). If no why?

.....

.....

Q.7. If YES, which of the following books do you keep?

☐ Purchases Day Book (Input Tax)

☐ Sales Daybook (Output Tax)

☐ Both

If you keep any other(s), please specify

Q.8 Do you think it is necessary to insist on invoice/receipt when you purchase inputs goods/services?

☐ Yes

☐ No

What is the reason for your answer in Q.8 above?

Q.9. Do you issue invoice/receipts when you sell or render services in all situations?

☐ Yes

☐ No

☐ Sometimes

If no or sometime, why?

Q.10 Do you know how to calculate input / output VAT?

☐ Yes

☐ No

Q.11. Which of the following categories of supply can you classify your goods/ services?

☐ Standard rated (VAT is charged on sales and can claim VAT paid) LJ

☐ Exempt (VAT is charged on sales and cannot claim VAT paid)

☐ Zero rated (VAT is not charged on sales but can claim VAT paid)

☐ Mixed supplies

☐ Do not know

Q. 12. Do you know how to file the VAT Returns?

☐ Yes

☐ No

Q. 13. When do you file your VAT Returns?

☐ Within the statutory period

☐ Sometimes exceed the statutory period

☐ Two months after the statutory period

☐ Other _____

Q.14. Have you ever defaulted in the submission of your VAT returns?

☐ Yes

☐ No

Q.15. Have you ever been fined before for not filing your returns on time?

☐ Yes

☐ No

If yes how many times?

Q.I6. How does VAT affect your business?

- ☐ Increase my profit
- ☐ Decrease my profit.
- ☐ Does not affect me

Q.I7 (i) Does VAT affect the prices of goods/services you offered?

- ☐ Yes
- ☐ No

(ii) If YES, how?

- ☐ Increase in prices
- ☐ Decrease in prices

Q.I 8 Mention some problems you encounter in the compilation of the VAT records

.....

.....

.....

Q.19. Do you receive any assistance from the VAT personnel in the compilation of your records?

- ☐ Yes
- ☐ No

Q.20. Do you think VAT will increase government revenue?

- ☐ Yes
- ☐ No

Q.21. Do you think VAT should be phased out?

☐ Yes

☐ No

Q.22. If NO, what changes do you expect to see in the operation of VAT?

☐ Decreased

☐ Increase the grace period

☐ Reduce the coverage

☐ Increase the rate charged

Q.23. Is the mode of education on VAT effective?

☐ Yes

☐ No

INTERVIEW GUIDE FOR VAT SERVICE

Please, where appropriate provide/attach any available relevant papers, documents or statistical data.

PERSONNEL

1. What are some of the problems that the service faces in recruiting, training and retraining personnel?

.....

.....

.....

2. What are the calibre of staff the service recruit with regards to qualification?

3. What are some of the problems that the service faces when it comes to remuneration and Other benefits?

.....

.....

.....

4. What is the labor turnover rate (from 2005-2010)

.....

.....

5. Do staff provide reasons for leaving? What are some of the reasons they provide?

.....

.....

6. Are there problems with staff discipline (integrity) with respect to field operations? How have these issues been looked at?

.....

.....

.....

CO - OPERATION FROM GOVERNMENT

What has been the co-operation from government(s) so far?

.....

.....

.....

Is it something to write home about? Are there any drawbacks?

.....

.....

OPERATIONS

1. What problems do you encounter in registering operators?
.....
2. Do you have a computerized database on all registered businesses?
.....
3. Have you incorporated ICT in your revenue collection? If YES, how and If NO why?
.....
.....
4. How do you enforce compliance to with revenue collection?
.....
5. What problems do you face when it comes to invoicing?
.....
.....

6. How have they been managed?

.....
.....

7. Do you have packages (software) to monitor VAT due to the service?

.....
.....

8. What problems do you encounter in auditing VAT records of clients

.....
.....

Through which means does the VAT service educate the general public and how effective has it been.

.....
.....

9. Are there standards set for operators in terms of book keeping? What problems crop up in this area?

.....
.....

10. What problems are associated with filing VAT Returns?

.....
.....

11. Do you have operators who owe the VAT service? What has been the trend from 2005-2010

.....
.....

What sanctions are impose on defaulting operators?

.....
.....

FINANCING

1. How do you finance your operations? Are there problems with financing?

.....

.....

2. Are there problems associated with logistics?

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PROSPECTS

1. What does the VAT service envision as a revenue collection body?

.....

.....

2. What are the prospects of VAT in Ghana?

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.....

3. Relative to other African countries, what is the position of Ghana as far as VAT is concerned?

.....

.....

4. What are the critical success factors as far as VAT administration is concerned? How have these been looked at?

.....

.....

THANK YOU