

ASSESSMENT OF THE EFFECT OF VALUE ADDED TAX ON CONSUMPTION BEHAVIOR: THE CASE OF NEKEMTE TOWN, WOLLEGA**Adamu TERFA***Wollega University, Ethiopia
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alexandrun@seap.usv.ro***Abstract**

This study has been conducted having the objective of assessing the effect of Value Added Tax on consumption behavior of Nekemte Town households. Descriptive research design has been implemented to undertake this study. The two most commonly used data collecting mechanisms (questionnaire and interview) have been used for this study by taking a sample size of 384, out of 20,870 households using stratified random sampling and three higher officials of Ethiopian Revenue and Custom Authority Nekemte branch from twelve total staff members using purposive sampling. To collect and measure the study, Liker Scale question were used and the collected data were edited for minor error. Relevant statistical methods of analysis like mean, standard deviation correlation and regression were use using the statistical package. The study revealed that the implementation of VAT to go down well with Consumers, the scheme has to come with some compensatory measures such as the reduction of income taxes to put more money in the pockets of households and to boost their purchasing power. And to ensure that the low-income and poor consumers – who may not enjoy the benefits of lower income taxes as most likely they are already exempted from such payment in the first place - are not worse off with VAT, zero-rating some basic essential products and providing other targeted assistance programmes are necessary measures to help them.

Keywords: *value-added taxation, consumption patter and Indirect Tax*

JEL Classification: *F38,H25, H71*

I. INTRODUCTION

Taxes are very important part of the daily functioning of a government. The general idea behind the imposition of taxes by the government is generally to balance the economy in terms of the redistribution of funds and income from the rich to the poor (Mesfin and Sisay, 2009). Taxation is as old as government and in ancient times, practical considerations such as ease of collection and administration took precedence over the more abstract aims that dominate contemporary tax debates. Adams (1982) reports that the Egyptians imposed general sales taxes at major markets, while in the early Roman Republic Caligula was exalted for abolishing the general sales tax in AD 40. Excises and tariffs were the mainstay of tax systems during mercantilist times and it was not until the early 20th century that governments imposed more coherent and comprehensive sales and income taxes to fund their rapidly expanding activities.

Nowadays there is a global shift in paradigm, whereby the focus point is moving from a direct taxation policy towards an indirect taxation policy. This action led to the implementation of the Value-Added Tax (VAT). The VAT was undeniably the most accidental improvement of the last half-century with regard to taxation policy. No other taxes, not even the income tax, have made an impact so quickly and rapidly to such extent that the VAT now exists in over 150 countries around the world, including Ethiopia and other African countries. This is so because the VAT is considered as an important source of government revenue and evidence has shown that the VAT is not only the least distorting tax, but can also be easily administered in most countries. Every country now makes use of the VAT and each year sees a new continent adopting it.(Ebrill et al, 2001).

According to Keen and Lockwood (2007), the idea of value added tax is introduced to the world in 1960s by German and spreads over the world. The value added tax (VAT) is now found in more than 150 countries and raise around 20 percent of the world's tax revenue. Because VAT contributes to the revenue of any country significantly, developing countries that are searching for additional revenue have enacted value added taxes by replacing it with sales tax (Schenk and Old man, 2001). Widely adopted in sub-Saharan Africa, it has been the centerpiece of tax reform in many developing countries. Besides, the IMF played a significant role in the spread of the VAT (Keen and Lockwood, 2007). The rise of the VAT has been the most significant development in tax policy and administration of recent decades. The VAT is simply a multistage sales tax that exempts the purchase of intermediate goods and services from the tax base. The advantage of a VAT over retail sales taxes is that VAT allows business to recoup tax on their inputs (business purchase) so that tax on retail sales does not impose a tax-on-a-tax. Value added is the difference between sales proceeds and purchases of intermediate goods and services over a certain period (Ebrill et al. 2001; Keen and Smith 2007; Webley et al. 2002)

The word consumption is inherent in the concept of VAT. As Plunkett (2008) affirmed, VAT generally applies to goods bought for consumption within a given country. In fact, as termed by Ghatak (2003), VAT is regarded as consumption-based taxes. Similarly, the European Commission (2000,) defines this tax as 'a general consumption tax, which is directly proportional to the price of goods and services. And it is through the prices of goods and services that VAT is a burden for the end consumer as Sopkova and Spisiakova (2007) noted. Abed further advance that the tax burden of VAT falls mainly on consumption.

The "value added tax" has been criticized as the burden of it falls on personal end-consumers of products. Some critics consider it to be a regressive tax, meaning that the poor pay more, as a percentage of their income, than the rich do. Defenders argue that relating taxation levels to income is an arbitrary standard, and that the value added tax is in fact a proportional tax in that people with higher income pay more in that they consume more. The effective progressiveness or repressiveness of a VAT system can also be affected when different classes of goods are taxed at different rates. To maintain the progressive nature of total taxes on individuals, countries implementing VAT have reduced income tax on lower income-earners as well as instituted direct transfer payments to lower-income groups, resulting in lower tax burdens on the poor (Paulo dos Santos et al. 1996).

According to Ghatak (2003), In developed countries there is evidence of an increase in the tax burden of the lower and lower- middle income groups and a reduction in the tax burden of the highest income groups In both developing and developed countries, there is also concern that there has been an increase in the relative tax shares paid by individuals through the personal income tax compared to those paid by businesses through corporate income taxes. Finally, in both developing and developed countries, reductions in overall tax revenues have resulted in a "fiscal squeeze" which can mean the reduction of needed public services with adverse effects in the short-term on the poor and low- income and in the long-term on overall social and economic development (Webley et al. 2002).

Using a sample of fifteen EU countries over the period 1961-2005 (Alm, James and Asmaa El-Ganainy, 2012), found that the effective VAT tax rate is negatively correlated with the level of aggregate consumption. More precisely, a one-percentage point increase in the VAT rate leads to about a one percent reduction in the level of per capita aggregate consumption. This result is consistent across various estimators, alternative time periods, and additional explanatory variables. To the best of my knowledge, these estimation results are the first attempt to include explicitly and to estimate directly the effects of the VAT on consumption behavior. The value-added tax rate varies according to countries. While in the European states it ranges from 12.5 percent to 25 percent, in African countries, including the Southern African Development Community (SADC), it varies between 5 percent and 20 percent. Ethiopia has a standard VAT rate of 15 percent. VAT has become important source of revenue to the States in Ethiopia. But, beyond the effectiveness of VAT in generating revenues for government is also important to carry out a research to assess the effect and significance level of VAT on consumption pattern of the town households depend on the arguments of both classical and modern economists who are criticizing as well as supporting the two ideas, i.e. the repressiveness, neutrality and progressiveness. The research questions of this study is, i. What effect does VAT had on the aggregate consumption of households?; ii. Is there any change in consumption behavior after VAT implementation?, iii. To what extent VAT affects the consumption behavior of households?

II. OBJECTIVES OF THE STUDY

GENERAL OBJECTIVE

The general objective of the study was to assess the effect of Value Added Tax (VAT) on consumption pattern of Nekemte Town households.

SPECIFIC OBJECTIVES

This study is aimed to, to assess the effect of VAT on consumption behavior of goods and services; to assess if there is change in consumption pattern after implementation of VAT; to measure the significance level of the effect of VAT on consumption pattern of Nekemte town households and to evaluate VAT encouraging saving scheme.

IMPORTANT OF THE STUDY

The study focuses on assessing the effect of value added tax on consumption and saving pattern of Nekemte town so the study contributes some useful insights to policy makers, other researchers who have the interest to investigate further on this area and also to the existing literature as a reference.

SCOPE OF THE STUDY

The study centers only on assessing and identifying the effect of VAT on consumption pattern of the Nekemte town house holds. The study delimited to the town, because VAT is the recent addition to Ethiopian tax and the town has experiencing the implementation of it very recently as well as the woredas around this town are not much susceptible to VAT that is why they are excluded from the study.

III. RESEARCH METHODOLOGY

RESEARCH DESIGN

The study applied A descriptive research design that involves gathering hard numbers, often via surveys, to describe or measure a phenomenon so as to answer the questions of who, what, where, when, and how. Involves gathering hard numbers, often via surveys, to describe or measure a phenomenon (Tanner and Raymond, 2010). For this study, a survey was been conducted in the scope to assess, describe, Interpret and analyze effect of VAT on consumptions behavior and saving pattern of Nekemte town households. Moreover the study was used both quantitative and qualitative data's.

SOURCE OF DATA

For this study, both primary and secondary data were been used. Data was gathered mainly from primary sources using questionnaires from the town's household of different sub cities and interview for officials and management team of FERA Nekemte branch office. Some data were collected from secondary sources including books, scholarly articles, government agencies (Ministry of Finance, MRA, CSO) online databases (World Bank, IMF), research reports, theses etc.

POPULATION OF THE STUDY

The target population for this study concerns house hold consumers of the town and the FIRS Nekemte branch office higher Officials. The total number of the households in the town according to population and housing census report, 2010 is about 20,870. Since the population is large, it is difficult to attempt to survey all of its members. As such, a sample can be used to represent the population.

Table 1 - Total Population of the Households in the Town

Sl. No.	Name of sub city	Number of households
1	Cheleleki	3,695
2	Burka Jato	3,887
3	Kasso	2,779
4	Bake Jama	2,241
5	Darge	3,997
6	BekenisaKesse	4,271
Total		20,870

Source : Population and Housing Census Report, August, 2010.

SAMPLE SIZE

Martin and Bateson (1986) indicate that to a point, the more data collected the better, since statistical power is improved by increasing the sample size. According to Gay and Diehl (1992), generally the number of respondents acceptable for a study depends upon the type of research involved. In case of this study descriptive research is going to be implemented. Thus According to Cochran (1997) to determine the desired sampling size, standard statistical approach equation will be used.

Therefore, $n = Z^2pq/d^2$

Where: - n = desired sampling size when population is greater than 10,000

Z = the standard number variable at a required level of confidence

P= the proportion of the target population estimated to have Characteristic being measured

q = 1-p

d = the level of statistical significance test (0.05)

Since the estimated population is greater than 10,000 the above formula will be applied

According to the formula, $n = (Z^2pq/d^2)$; $n = \{(1.96)^2(0.5)(0.5)\}/(0.05)^2$; n = 384

SAMPLING PROCEDURE

The sampling method used in this study was both probabilistic and non probabilistic sampling technique. The probabilistic sampling technique used in this study was Stratified Random Sampling – where the population is divided into six strata’s/ sub cities. The sample size is going to be taken from each sub cities; in proportion to the number of household they hold, using simple random sampling. Whereas, from twelve employees of the Inland Revenue office Nekemte branch three employees of the Inland Revenue office higher officials were purposively selected depend on their position and knowledge of VAT.

To share the total sample size among the strata’s/sub cities the following formula is applicable.

i.e. $n_i = p_i * n / N$

Where n_i =sample size of the sub cities; P_i =population of each strata’s/ sub cities; n= sample size of total population i.e.384; N= total population

Table 2 Sample of the Households from Total Population for the Study

Sl. No.	Name of sub city	Number of households	Sample ($n_i = \frac{p_i * n}{N}$)
1	Cheleleki	3,695	68
2	Burka Jato	3,887	72
3	Kasso	2,779	51
4	Bake Jama	2,241	41
5	Darge	3,997	73
6	BekenisaKesse	4,271	79
	Total	20,870	384

METHODS OF DATA COLLECTION

The two primary data collection methods used for this study were questionnaire and interviews.

A face to face interview was conducted to collect survey data. This technique is preferred over other forms because it allows respondents to clarify questions and it enables to pick up nonverbal cues from the respondent. However, one of the drawbacks is that there are costs involved in the form of transport, time and energy. So it is planned to interview purposively three FIRA Nekemte branch higher officials.

Surveying people is one of the most commonly used techniques to collect quantitative data. The main instrument used to collect empirical data was the questionnaire. It requires numerical data to be collected about how many people hold similar views on the subject matter. To quantify these characteristics, a standardized questionnaires was been designed. The questionnaire design was based on the research objectives and the literature review. It begins with a covering letter that describes the purpose of the study is for. It was written in English but had to be translated for some respondents to Afan Oromo. Effort was made to make it simple and understandable, yet, some technical words had to be used, but these are explained in the ‘general notes’. The questionnaire was been filled by the selected households of Nekemte town.

The questionnaire was divided into 3 sections: (personal information of households, buyer VAT related knowledge and attitude of respondents and relevance of VAT with consumption and saving patterns). Questions

ranged from unstructured (open-ended) to structured (dichotomous) response formats. The five Likert scale type questions (like strongly agree, undecided, agree, disagree, strongly disagree) are also included. Finally, responses was been coded using nominal scaling (assigning a number to each response), ordinal (in order of rank) and interval (likert scale).

METHOD OF DATA ANALYSIS

After gathering data, the collected data was been edited for minor errors, coded and classified to have similar characteristics to make the information ready for analysis. The completed and edited data's were inserted into statistical software SPSS version 20 for calculation and processing. Results were been displayed in the form of charts and tabulations to aid the reader in understanding the data distribution. The descriptive analysis like tables; frequency and percentage were used for analysis. In this phase respondent's remark about the effect of VAT on consumption pattern had carefully assessed. Relevant statistical methods of analysis like mean, standard deviation, correlation and regression was used in order to come up with the result. Results from the survey were used to illustrate the main findings of the research project and interpret the information gathered and write a final project.

RESEARCH ETHICS

Here the researcher pertain to the ethical principles in research while designing, taking sample from population. In addition it followed the scientific research approach. Hence the researcher duly acknowledges all the authors, further the researcher gave due respect for the culture and values of respondents and non personal predisposition while collecting, analyzing and interpreting the data

IV. DATA ANALYSIS AND PRESENTATION

The analysis, description and interpretation of the data collected from the respondents. The response rate was so well-organized that 384 questionnaires were distributed and 376(97.92%) returned. The analysis, description and interpretation of each of the response were done one after the other under the given subtitle. Lastly, the research project conducted to assess the effect of Value Added Tax on consumption pattern in Nekemte town was brought with the following results.

RESPONDENTS PERSONAL PROFILE

Table 3 - Demographic Characteristics of Respondents

No.	Items	Range	Frequency	Percent	Cumulative Percent
1.	Age Group	20-30	13	3.5	3.5
		31-40	92	24.5	27.9
		Valid 41-50	112	29.8	57.7
		more than 50	159	42.3	100.0
		Total	376	100.0	
2.	Sex of respondents	male	334	88.8	88.8
		Valid female	42	11.2	100.0
		Total	376	100.0	
3.	Educational background of Respondents	Grade 12 and less	57	15.2	15.2
		certificate	86	22.9	38.0
		Valid Diploma	129	34.3	72.3
		Degree and Above	104	27.7	100.0
		Total	376	100.0	

Source: own survey, 2014

AGE OF RESPONDENTS

As indicated in table 3, about 3.5% of the total respondents were between age 20-30, 24.5% of the total respondents were between age 30-40, 29.8% of total respondents were between age 40-50 and the rest 42.3% of the total respondents were above age 50. The age spans of 42.3% of respondents lied above age 50 as indicated

in the table. This means majority of the respondents were people with high tax paying experience. They can be considered as matured enough of having awareness about tax and taxation principles.

SEX

The above table has been observed that that 88.8% of the total respondents were male and the rest 11.2% were females. The data obtained showed that majority of the respondents were male households.

EDUCATIONAL LEVEL OF RESPONDENTS

From the table 3, it has been revealed that 27.7% of the total respondents were degree holders and above, 34.3% of them achieved college diploma, and 22.9% of them trained at certificate level while the rest 15.2% were with illiterate with basic education, primary and high school completed. Based on the above description, It is safe to interpreted they were able to understand the objective of taxation and specifically VAT, since they were educated enough having certificate and above education rank.

DESCRIPTIVE STATISTICS/ANALYSIS

MONTHLY INCOME OF HOUSEHOLDS

Table 4 - Monthly Income of Respondents

Description	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Less than Or equal to 2,000.00	152	40.4	40.4	40.4	1.82	.772
Valid 2,001.00-5,000.00	140	37.2	37.2	77.7		
Greater than 5,000.00	84	22.3	22.3	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

As the observation was made from the table 4 above, 40.4% of the respondents were getting income of less than 2,000 Birr whereas 37.2% of the respondents have a monthly income between 2,000-5,000 Birr and the rest 22.3% of them were getting more than 5,000 Birr. Thus, majority of the respondents 40.4% were lower income households following 37.2% with medium income households.

FAMILIARITY WITH ETHIOPIAN VAT LAW AND PROCLAMATION

Table 5 - Familiarization of Ethiopian VAT law Among Households

Are you Familiar with VAT concept?	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Valid Yes	212	56.4	56.4	56.4	1.44	.497
No	164	43.6	43.6	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

Table 5 revealed that about 56.4% of the total respondents were familiar with the Ethiopian VAT law and proclamation and 43.6% of them were not familiar with it. Those who were not familiar with VAT had no information about VAT because the concept of VAT was the most recent development resulted from Ethiopian tax reform of 2003. This revealed that the knowledge and understanding of Value Added Tax is still new to a particular section of the public.

CLARIFICATION MADE BY THE AUTHORITY (ERCA) TO THE PUBLIC ABOUT VAT

Table 6 - Clarification Made by the Authority to the Public about VAT

Do you think ERCA has made sufficient clarification for you?	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Yes	107	28.5	28.5	28.5	2.02	.767
No	155	41.2	41.2	69.7		
No idea	114	30.3	30.3	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

As it has been observed from table 6, about 41.2% of the total respondents said that the authority has not made sufficient clarification to the public about VAT, 30.3% of total respondents have no idea whether the authority has made sufficient clarification about VAT to the public or not and 28.5% responded that there is sufficient clarification made by the authority about VAT to the public. In addition to the information obtained from close ended above, open ended questionnaire and interview also revealed that majority of the public lack sufficient knowledge and concept of tax in general and VAT in particular. This is because of the fact that the taxation system of Ethiopia was revised very recently. In addition, households of Nekemte town were perceived VAT as complicated to understand; there is lack of knowledge and awareness about taxation generally and VAT tax particularly.

CONSUMERS WILLINGNESS NOT TO PURCHASE GOODS AND SERVICES WITH VAT

Table 7 - Consumers Willingness of Buying Goods and Services with VAT

Are you not willing to purchase Goods & Services with VAT?	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Yes	182	48.4	48.4	48.4	1.75	.813
No	105	27.9	27.9	76.3		
No Idea	89	23.7	23.7	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

In addition, the household respondents were asked whether they are not willing to purchase goods and services with VAT. Out of the 376 respondents, 182(48.4%) replied that **yes** they are not willing to purchase VAT inclusive goods and services, 105(27.9%) replied that they are willing to purchase goods and services with VAT and 89(23.7%) replied that they know nothing about. The majority of the respondents, 182(48.4%), agree with the idea that they are not willing to pay for the goods and services they have purchased with VAT. And the respondents put the reasons why these customers are not willing to purchase goods and services that include VAT rate in to its prices. The main reasons are related to the purchasing powers and awareness of the society regarding VAT. The currently increasing level of inflation affects the purchasing power of the society and manifests the customer’s need of searching goods that doesn’t incorporate VAT value in its prices. On the other hand there are also consumers that purchase goods and services that exclude the VAT value in its prices intentionally made by the sellers providing falsified invoices.

Brown (2006) identifies three basic categories of factors that influence the consumer’s purchase decisions; namely personal, psychological and social factors. According to him, psychological factors include motivation, perception, skills and knowledge, positions, personality; while personal factors are referred the ones unique for each consumer. Horská and Sparke (2007) categorize personal factors into age, sex, place of domicile, occupational and economic conditions, personality and self consciousness. Vysekalová (2004) classify situational factors as being the physical environment of the purchase place and time influences

THE EFFECT OF VAT ON CONSUMPTION PATTERN

Table 8 - The effect of VAT on Consumption Pattern

Description	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Positive	33	8.8	8.8	8.8	2.27	.758
Negative	248	66.0	66.0	74.7		
Valid Neutral	57	15.2	15.2	89.9		
No Idea	38	10.1	10.1	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

From table 8, about 8.8% of respondents replied that VAT had positive effect on consumption and 66.0% of the total respondents replied that it had Negative effect on consumption while, 15.2% of the total respondents replied that the effect of VAT on consumption is neutral and 10.10% of the respondents replied that they have no idea on the effect of VAT on consumption pattern. This means majority of respondents concluded that the effect of VAT on consumption is negative. Furthermore, open ended questionnaire and interview shows that, VAT increases price thus the purchasing power decrease. I.e. only small goods and commodities will available in the basket of consumers.

VAT AND CONSUMPTION

Table 9 - Decreases of Consumption due to VAT

VAT decreases your general consumption of Goods & Services.	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Strongly Agree	194	51.6	51.6	51.6	1.78	1.010
Agree	109	29.0	29.0	80.6		
Valid Neutral	45	12.0	12.0	92.6		
Disagree	18	4.8	4.8	97.3		
Strongly Disagree	10	2.7	2.7	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

As depicted on table 9 about 51.6%, 28.99%, and 12.0% of the respondents were strongly agree, agree and neutral on whether VAT decreases general consumption of goods and services respectively. Moreover, 4.8% and 2.7% of the respondents were disagreeing and strongly disagree on whether Value Added Tax decreases consumption of goods and services of households respectively. In addition to this open ended questionnaire and interview responses also described that since VAT increases prices of goods and services; they prefer to reduce their consumption because they have fixed income to consume.

As Plunkett (2008) affirmed, VAT generally applies to goods bought for consumption within a given country. In fact, as termed by Ghatak (2003), VAT is regarded as consumption-based taxes. Similarly, the European Commission (2000,) defines this tax as ‘a general consumption tax, which is directly proportional to the price of goods and services. And it is through the prices of goods and services that VAT is a burden for the end consumer as Sompokova and Spisiakova (2007) noted.

VAT AND PERSONAL SAVINGS

Table 10 – Savings Encouragement due to VAT

VAT encourages you to save part your income.	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Strongly Agree	41	10.9	10.9	10.9	3.89	1.338
Agree	30	8.0	8.0	18.9		
Neutral	22	5.9	5.9	24.7		
Disagree	118	31.4	31.4	56.1		
Strongly Disagree	165	43.9	43.9	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

According to table 10 above, 10.9%, 8.0%, and 5.9% of the respondents were strongly agree, agree and neutral on whether VAT encourage individuals to save part of their income respectively. Moreover, 31.4% and 43.9% of the respondents were disagree and strongly disagree on whether Value Added Tax encourage individuals to save part of their income respectively. In addition to this open ended questionnaire and interview responses also illustrated that since income of every household are fixed and because of VAT individual’s volume of purchase of goods and services with this fixed income reduced. So, there is no probability of saving part of an income for future use. In addition respondents also depicted that having fixed income, they prefer to consume than saving in addition to the inflation in the country in general and Nekemte town in particular. Based on the above, although literature on VAT seems rare, one can derive that the VAT has a major influence on investment decisions, national welfare and mainly on consumer behavior. (Soyode L, Kajola SO 2006)

CHANGE IN CONSUMPTION AFTER IMPLEMENTATION OF VAT

Table 11 - Changes of Consumption after Implementation of VAT

Your Consumption decreases due to implementation of VAT.	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Strongly Agree	112	29.8	29.8	29.8	2.43	1.308
Agree	120	31.9	31.9	61.7		
Neutral	51	13.6	13.6	75.3		
Disagree	58	15.4	15.4	90.7		
Strongly Disagree	35	9.3	9.3	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

From the table 11 above, 29.8%, 31.9%, and 13.6% of the respondents were strongly agree, agree and neutral on whether there is change in consumption after implementation of Value Added Tax respectively. Moreover, 15.4% and 9.3% of the respondents were disagree and strongly disagree on whether there is change in consumption after implementation of VAT respectively. In addition to this open ended questionnaire and interview responses also illustrated that since VAT discourages consumption by raising price of goods and services; it is visible that there is a slight change in consumption currently. Where as in the future there is a probability more change in consumption if things will not change around the subject matter. Modern economists believe that taxation system influences main economic activities like consumption, production and distribution by influencing aggregate demand and supply. They concluded that “taxes have a significant effect on consumption. Because of taxation, purchasing power of the tax payer goes down. There are two reasons for it (a) direct taxes lead to fall in disposable income because these are paid out of income, (b) indirect taxes result in rise in prices. Tax-payer can purchase fewer amounts of goods with the same income on account of rise in prices.” (Jain and Khanna, 2009)

VAT TARGET REVENUE GENERATION AND IS DETRIMENTAL TO CONSUMPTION AND SAVING

Table 12 - Targets of VAT only Revenue Generation and is Detrimental to Consumption and Savings.

VAT targets Revenue generation and is detrimental to consumption and savings.	Frequency	Percent	Valid Percent	Cumulative Percent	Mean	Std. Deviation
Strongly Agree	112	29.8	29.8	29.8	2.53	1.354
Agree	100	26.6	26.6	56.4		
Neutral	51	13.6	13.6	69.9		
Disagree	77	20.5	20.5	90.4		
Strongly Disagree	36	9.6	9.6	100.0		
Total	376	100.0	100.0			

Source: own survey, 2014

It is revealed from the table 12 Above 29.8%, 26.6%, and 13.6% of the respondents were strongly agree, agree and neutral on the idea that says that VAT targets revenue generation and is detrimental to consumption and saving respectively. Moreover, 20.5% and 9.6% of the respondents were disagree and strongly disagree on the idea that says VAT targets revenue generation and are detrimental to consumption and saving respectively. In addition to the open ended questionnaire and interview responses also illustrated that the main reason for the revision of Taxation system of the country in general and VAT in particular is generation of revenue for the state to compensate the economic distortion incurred before a couple of years.

Various authors have identified general relationships between factors such as income, social class, and etc with respect to consumption. For instance, there is a direct relationship between consumption and disposable income, i.e. as disposable income increases, so does consumption (McEachern, 2009). Similarly, social class is another determining factor that influence consumption as it is the consumers in the poor and the middle classes who are expected to reduce consumption. Other authors have also identified the relationship between the commodities in the basket with personal factors. For instance, for the category food & non alcoholic beverages, Harris and Blisard found that elderly groups (65-74 and 75 and older) spent almost ten percent of average weekly income on food.

REGRESSION ANALYSIS

Table 13 - Regression Analysis of Consumption and VAT

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1.	.527 ^a	.278	.276	2.02524

Source Own Survey, 2014

a. Predictors: (Constant) VAT

As it has been observed from the above table the degree of association between consumption and Value Added tax are 0.527 and the degree of influence of VAT is shown by R square is 0.278 meaning among many factors affecting Consumption VAT has 27.8% influence on Consumption behavior of households, while 72.2% of the deviation resulted from other variables which are not included in this study like for example personal factors, psychological factors and Inflation as depicted by Brown (2006) identifies three basic categories of factors that influence the consumer's purchase decisions; namely personal, psychological and social factors. According to him, psychological factors include motivation, perception, skills and knowledge, positions, personality; while personal factors are referred the ones unique for each consumer. Horská and Sparke (2007) categorize personal factors into age, sex, place of domicile, occupational and economic conditions, personality and self consciousness. Vysekalová (2004) classify situational factors as being the physical environment of the purchase place and time influences.

CORRELATIONS ANALYSIS

Table 14 - Correlation Analysis of Variables

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	-1.181	.778		-1.518	.130
vat	1.156	.096	.527	11.998	.000

Source: Own Survey, 2014

a. Dependent Variable: consumption

From the above table, it is observed that there is negative relationship between Value Added Tax and Consumption behavior which is shown on the above table by t-1.518 of the town households. That mean when the rate of value added tax is applied to Goods and Services the consumption pattern of households is going to decrease due to the fact that the rate of VAT will increase the price of these Goods and services. As Boex et al (2006) claimed, “VAT does of course raise the price of consumer goods”. VAT would raise prices by the amount of the tax (Lindholm, 1971) but as portrayed by the VAT Consultancy (2010), as the price of a good rises, a higher proportion of the price will be paid over in VAT. In this way, VAT impacts on consumption as Davies [no date] explains that a 20% rise in price results in a 10% reduction in consumption this means that there is lower quantity of goods available in the consumer’s basket of goods.

Table 15 - Coefficients of Variables

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.13	.000		.000	1.000
Monthly Income of Respondents	1.013	.000	.000	.000	1.000
Familiarity of Respondents with VAT law	1.000	.000	.457	0.255	.000
If ERCA has made sufficient clarification for the peoples	1.000	.000	.707	0.403	.000
Are there consumers not willing to purchase with VAT?	-1.313	.000	.000	.000	1.000
1 The effect of VAT on consumption behavior	1.000	.000	.698	0.048	.000
VAT Decrease general consumption of goods and services	1.000	.000	.930	0.029	.000
VAT encourage individuals to save part of their income	-0.013	.000	.000	.000	1.000
there is change in consumption after implementation of VAT	-3.482	.000	.000	.000	1.000
VAT target revenue generation and is detrimental to consumption and saving	.200	.000	.249	0.211	.000

Own Survey, 2014

a. Dependent Variable (VAT Source) :

In another way the significance level indicates that even though there is a negative relationship between VAT and consumption, the effect is not significant currently. This is because of the fact that there is no full implementation of VAT in the town, there are still unregistered organizations fulfilling the requirement of registration. So, the consumers have an option of purchasing from unregistered business organizations. Ruther the consumers are worrying the effect when it is fully implemented. But, economic distortion is created due to the existence of this unregistered business

V. CONCLUSION

It has been concluded that for the implementation of VAT to go down well with Consumers, the scheme has to come with some compensatory measures such as the reduction of income taxes to put more money in the pockets of households and to boost their purchasing power. And to ensure that the low-income and poor consumers – who may not enjoy the benefits of lower income taxes as most likely they are already exempted from such payment in the first place - are not worse off with VAT, zero-rating some basic essential products and providing other targeted assistance programmes are necessary measures to help them.

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