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Effects of Tax Audit Attributes on Tax Payers' Compliance in Oyo state

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ABSTRACT

Governments worldwide invest heavily in public spending to ensure their citizens have access to essential services and basic amenities. To achieve this, governments require huge funds to meet its obligations. Among the various sources that government generates revenue, tax is major, because it contributes much more than any other sources. This study considered the effects of tax audit attributes on taxpayers' compliance in Oyo state, Nigeria. The study adopted a descriptive research design with 287 questionnaires administered to the selected staff of the Oyo state board of internal revenue selected through the stratified and purposive sampling technique. The data were analyzed with the aid of statistical package for social sciences SPSS to generate both descriptive and inferential statistics. The result of regression analysis of ANOVA which showed F- Value (1.308) and (P=0.0000) suggests that at least one of the independent variables of fairness and impartiality, penalties, reasonable audit duration, have a highly significant effect on the dependent variable which is taxpayers' compliance. The study concluded that the effectiveness of tax audits, professionalism and competence of tax auditors, penalties attached to noncompliance and duration of audit process all have a significant impact on taxpayers' compliance. It is recommended that the government should establish and implement penalties in order to serve as deterrent to non-compliance and in turn increase taxpayers' compliance.

Keywords: Tax, Tax audit, Taxpayers' compliance.

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Introduction

Governments worldwide invest heavily in public spending to ensure their citizens have access to essential services and basic amenities. To achieve this, governments require huge funds to meet its obligations. Among the various sources that government generates revenue, tax is major, because it contributes much more than any other sources. Taxes are mandatory charges that the government imposes on the income, profits, or wealth of individuals, families, communities, and businesses. These taxes are essential for funding public expenditures, which focus on providing social amenities and infrastructure for citizens. By collecting taxes, the government generates the revenue needed to support these vital services and developments within the State. (Olaoye & Ekundayo, 2019).

Tax compliance is the process whereby taxpayers comply with the stipulated laws and regulation by remitting the expected tax return accurately and truthfully (Olaoye & Ekundayo, 2019; Embele, 2021). Since improving the society is every patriotic citizen's top priority, one would think that tax compliance shouldn't often require any kind of coercion (Enofe et al., 2020). However, the extensive body of literature devoted to this subject over the years indicates that intentional tax non-compliance remains a significant challenge in every society, particularly in Oyo State and, hence, Nigeria as a whole. (Embele, 2021). In this wise, Olaniyi & Ilesanmi, (2019) observed that the increased frequency of tax audits and investigations by the Federal Inland Revenue Service (FIRS) and various State Boards of Internal Revenue (SBIR) in Nigeria is a direct response to the non-compliance of taxpayers, which has resulted in significant revenue losses.

Statement of problem

One of the major problems for government in developing countries is encouraging high levels of tax compliance as observed Mebratu (2016). The observation of Olaoye & Ekundayo, (2019) on the power of tax audit at enforcing compliance require further empirical evidence from the perspectives tax payers in oyo state, Nigeria. This is coupled with the fact that improving tax payer compliance is one of the most important but least studied aspects of fiscal reform in developing economies, there appears considerable potential area for research as observed Mebratu, (2016).

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Hypothesis of the Study

The following hypothesis in the null forms was proposed for the study:

H_{O1}: There is no significant difference in the tax audit attributes among tax payers in Oyo State Nigeria

Literature Review

The development of any nation according to Olaoye and Ekundayo (2019). The amount of revenue generated and allocated by the government for public infrastructure plays a crucial role in benefiting society. No economy can thrive without sufficient resources to develop infrastructure, provide power, and ensure essential public utilities and services. Taxes and the structure of tax systems are key elements in nation-building, especially in developing or transitional countries (McKerchar & Evans, 2009). Omodero et al. (2023) also emphasized that tax revenue is essential for government operations worldwide, as taxes are recognized as a major source of national income.

Tax audit

A tax audit entails an In-depth evaluation to verify whether a taxpayer has accurately reported their tax liabilities and fulfilled all related obligations. This type of audit is typically more thorough and detailed compared to other examination methods such as general desk checks, compliance visits, or document matching programs, as stated by the OECD (2006).

Tax compliance

Hamid (2020) suggested that tax compliance involves taxpayers' ability and willingness to adhere to tax regulations, influenced by ethical considerations, the legal environment, and situational factors in a particular time and place. Similarly, various tax authorities, such as the Internal Revenue Service (IRS) in the United States, the Australian Tax Office (ATO), and the Inland Revenue Board of Malaysia (IRB), define tax compliance as taxpayers' capacity and willingness to adhere to tax laws, accurately file their revenue annually, and pay the appropriate amount of taxes within the designated timeframe (IRSDB, 2009).

Tax gap

Gemmell & Hasseldine (2014) defined the tax gap as the distinction between the actual revenue collected and the hypothetical revenue that would be collected under full compliance, taking into account both tax avoidance and tax evasion. This discrepancy leads to lower overall

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revenue collection. Similarly, the compliance gap, as defined by Khwaja & Iyer, (2014), refers to the difference between the actual tax revenue and the potential tax revenue that could be collected. Tax compliance can be viewed in terms of tax avoidance and tax evasion, with avoidance involving legal backing to reduce tax liability and evasion involving illegal measures.

Audit Scheme

An audit scheme refers to a systematic and structured approach for conducting audits. It outlines the procedures, guidelines, and criteria that auditors follow to measure the accuracy, reliability, and compliance of financial records, processes, systems, or activities within an organization. Audit schemes differ based on the audit nature and the specific requirements of the organization or industry (Kleinman et al., 2019). They are designed to ensure that audits are conducted consistently, objectively, and in accordance with professional standards, ultimately promoting transparency, accountability, and trust in the audited entity's operations (Logie & Maroun, 2021).

Theoretical Review

Deterrence Theory

Deterrence theory suggests that people act based on the anticipated benefits or costs of their actions, rather than the variation in motivational factors. It is a key function of criminal justice systems, environmental contexts, and international relations. In tax compliance, the fear of audits and punishment encourages adherence to tax laws. Deterrence theory is applied to tax audits, as the perceived risk of detection increases the likelihood of compliance. The tax compliance model is based on deterrence theory, emphasizing that individuals seek to maximize their utility while avoiding punishment (Alshrouf, 2019)

Compliance Theory

Compliance cost theory focuses on the economic and administrative burdens faced by taxpayers in meeting their tax obligations. Tax audits can impose both direct and indirect costs on taxpayers, such as time, financial resources, and psychological stress (Birskyte, 2013). Slemrod, Blumenthal & Christian (2001) conducted a Minnesota controlled field experiment to analyze taxpayer response to increased audit probability. They found that low and middle-income taxpayers increased their reported income between 1993 and 1994, with the effect being stronger for those with higher opportunities to evade. The study highlighted the economic and administrative burdens taxpayers face in meeting their tax obligations.

Empirical Review

Wachira (2022) examined income tax compliance among 166 SMEs in Meru Town, Kenya. Despite being 80% taxpayers, they only contribute 5-10% of total tax revenue. The research found that SMEs are knowledgeable about tax filing procedures and understand their obligations. However, tax audits are infrequent and prosecution difficult. The adoption of automated tax systems improved compliance and reduced costs. Taxpayer knowledge was the most significant factor influencing compliance, followed by technology strategies. The study recommends enhanced taxpayer education and the establishment of tax penalty resolution offices to improve compliance.

Pukeliene & Kazemekaityte (2016) identified three main determinants of tax compliance behavior: tax authority, taxpayer, and other taxpayers. They also identified penalty, audit, and income as classical tax behavior determinants. Elly (2015) identified five main factors determining compliance. Kasper & Alm (2020) conducted a laboratory experiment to explore the impact of tax audits on post-audit compliance. They included audit effectiveness, which refers to the extent of undeclared income detected during audits. The study found that effective audits increased post-audit tax compliance, while ineffective audits had the opposite effect.

The study by Olaniyi & Ilesanmi (2019) found a significant positive relationship between tax audit and tax compliance in Kwara State between 2010 and 2016. The study also found a positive linear relationship between government spending and tax compliance. Penalties for default in tax payment also positively affected tax compliance. The findings suggest that routine tax audits and internal mechanisms to monitor tax audit staff are necessary to ensure accountability of tax revenue.

Alm & McKee (2006) found that individuals are more likely to comply with tax regulations if they know they are at risk of being audited. Similarly, Slemrod, Blumenthal & Christian (2001) observed that taxpayers tend to modify their behavior when informed of a "close examination" of their filings, although reactions differed among groups.

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Conceptual Framework

This paper presented a model examining the variables influencing tax audit attributes in the Oyo state board of Nigeria and their impact on taxpayer compliance in the Oyo state internal revenue service. The model is based on the Deterrence theory, which suggests that the perception of detection and punishment acts as a deterrent to potential non-compliance, improving public interest in the state. The model is adapted from Alshrouf (2019) study and is presented in Figure 1

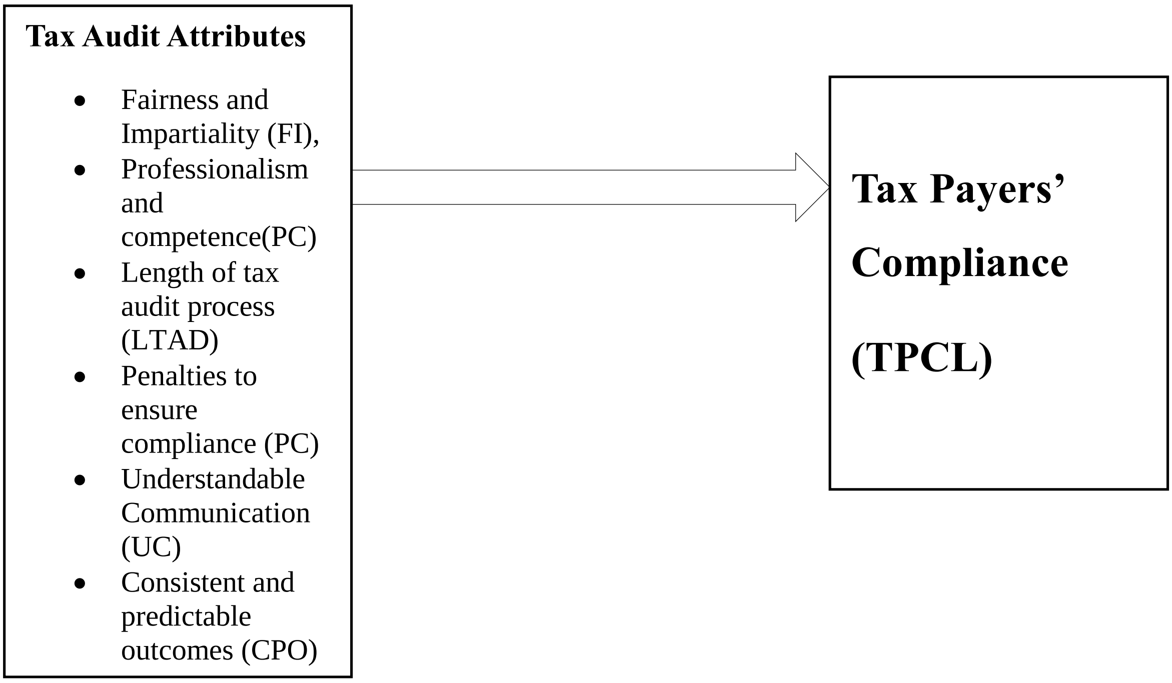

Figure 1: Model on Tax Audit atrributes and tax payers' Compliance of Oyo State.

Source: Adapted from Alshrouf (2019) with some little modification

Methodology

The study, conducted in Oyo State, Nigeria, analyzed data using inferential statistics and SPSS software. The target population included 500 staff members of the Oyo State Board of Internal Revenue and taxpayers, with a sample size of 278 selected through stratified and purposive sampling. The sample included tax auditors, accountants, and inspectors of taxes. Data was collected primarily through a questionnaire and assessed for validity. The study employed Ordinary Least Square (OLS) regression to measure the relationship between tax audit attributes (independent variables) and taxpayer compliance (dependent variables), with taxpayer characteristics as control variables. Multicollinearity, a potential issue when independent variables are linearly related, was assessed using correlation coefficients, tolerance statistics, and Variance Inflation Factor (VIF). The study followed thresholds established by Gujarati (2003) to determine if multicollinearity was significant. In order to arrive at the sample size for this study, stratified and purposive sampling techniques were used. Stratified and purposive sampling technique is one in which larger population is divided into separate subgroups from which sample size is drawn which is believed to be a fair representation of the entire subgroup. Purposive sampling is a non-probability sampling method that is particularly useful when focusing on a specific cultural domain, especially when the study requires input from experts with deep knowledge in that area (Rai & Thapa, 2015). This technique can be applied in both qualitative and quantitative research methodologies. The entire population of this study was segregated into stratum based on their professionalism and their perceived knowledge of tax audit.

Table 1 Division of Oyo State Board of Internal Revenue Base on Stratum

SN	Staff Categorization	No of Staff
1	Tax Auditors	85
2	Accountants	57
3	Station Managers	61
4	Inspector of Taxes	75
	Total	**278**

Source: Authors' compilation

Based on the above table, a sample of size of 278 was selected based on their stratums, which is the departments to which they belong. These are those in the categories of tax auditors, accountants and station managers and inspector of taxes.

Model Specification

OLS regression Model

$$TPLC = f(Audit\ attributes)$$

$$TPLC = f(FI, PC, DTA, PEC, UC, CPO)$$

TPCL = f (Audit attributes) (1)

TPCL= f (FI, PC, DTA, PEC, UC, CPO)

Where,

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TPCL= Tax payer's compliance

F I – Fairness and Impartiality

PC- Professionalism and competence

DTA-Duration of tax audit

PEC-Penalties to ensure compliance

UC-Understandable communication

CPO- Consistent and predictable outcomes

The above equation can be restructured in an explicit functional form after taking into consideration independent variables as:

$$\text{TPCL} = \beta_0 + \beta_1 FI_1 + \beta_2 PC_2 + \beta_3 DTA_3 + \beta_4 PEC_4 + \beta_5 UC_5 + \beta_6 CPO_6 + e \quad (2)$$

Where:

β_0= Constant term

X1 to X5 are Audit attributes

e = error term

$\beta_0 - \beta_6$ to are the parameters to be estimated. The apriori expectation is that the estimated parameters are greater than zero. The dependent variable is Tax payers' Compliance level (CL) which is the aggregate amount of actual tax collected annually in a state as a percentage of expected annual tax volume(in %).

Results and Discussion

Questionnaires were designed and distributed to the sampled population and two hundred and seventy eight (278) copies of questionnaire were administered while 278 (100%) copies of the questionnaire were retrieved and used for the analyses for efficient understanding of the work, the responses were treated expressly in the Table 2.

Respondents	**Questionnaire Distributed**	**Returned**	**Percentage**
	278	278	100%

Source: Author's Computation, 2024

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Demographic Characteristics of the Respondents

Four (4) major socio-economic characteristics were examined for relevance among the responded questionnaire administered. This is with a view towards understanding the socio-economic characteristics of respondents. Finding from the study on the four (4) socio economic characteristics were presented in Table 3

The survey sample, primarily aged 50 and above, has a demographic skew towards older respondents, suggesting potential differences in attitudes and experiences related to tax audit attributes. Additionally, there is a gender imbalance, with males comprising 66.2% and females 33.8%, suggesting different perceptions of tax audit attributes between genders, indicating a need for further analysis. The survey reveals a diverse workforce, with 28.4% having 11-15 years of experience, indicating a relatively experienced workforce. The majority (51.8%) earn between 50,000 to 100,000 monthly, indicating a diverse socioeconomic background, which may influence their financial perspectives and perceptions of tax audit attributes.

Table 3: Distribution of Respondents by demographic Characteristics

S/N	Socio Economic Characteristics	Variables	Frequency	Percentage (%)
1		less than 20 yrs.	1	.4
		21-30 yrs.	19	6.8
	Age	31-40 yrs.	12	4.3
		41-50 yrs.	64	23.0
		50yrs. and above	182	65.5
		Total	**278**	**100.0**
2		Male	184	66.2
	Gender	Female	94	33.8
		Total	**278**	**100**
3		1-5years	43	15.5
		6 -10 years	42	15.1
		11 – 15 years	79	28.4
	Work Experience	16 – 20 years	51	18.3
		20 – 25 years	43	15.5
		Above 25 years	20	7.2
		Total	**278**	**100.0**
4		Less than 50,000	67	24.1
		50,000-100,000	144	51.8
	Monthly income	Above 100,000	67	24.1
		Total	**278**	**100.0**

Source: Researchers computation using SPSS version 22, 2024

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Extent to which tax audit affect taxpayers' compliance

The study reveals that a majority of taxpayers (61.9%) believe the fairness and impartiality of tax audits influence their compliance with tax regulations. However, a significant portion (23.7%) disagrees, suggesting a need for improved transparency and communication. Auditor professionalism and competence also have mixed perceptions, with 53.6% acknowledging their influence and 28.7% disagreeing. Understanding tax penalties encourages compliance, but a significant proportion (34.2%) remains skeptical. A reasonable audit duration positively impacts compliance, but 28.7% expresses dissatisfaction. Consistent and predictable audit outcomes are also important motivators.

Table 4 Extent to which tax audit attributes affect tax compliance among tax payers

S/N	Variables	SA (%)	A (%)	UD (%)	D (%)	SD (%)
1.	The fairness and impartiality of the tax audit process influence willingness to comply with tax regulations.	72(25.9)	55(19.8)	85 (30.6)	34(12.2)	32(11.5)
2.	The professionalism and competence of tax auditors affects compliance with tax laws.	56(20.1)	62(22.3)	59(21.2)	53(19.1)	49(17.6)
3.	Knowing that tax audits are conducted to ensure compliance by attached penalties makes them to be more compliant.	85(37.1)	70(25.2)	28 (10.1)	55(19.8)	40(14.4)
4.	Clear and understandable communication during a tax audit makes tax payer more likely to comply with tax requirements.	83 (29.9)	89(32)	40(14.4)	42(15.1)	24 (8.6)
5.	A reasonable duration for completing tax audits impacts tax compliance positively	83 (29.9)	66(23.7)	49(17.6)	48(17.2)	32(11.5)
6	Consistent and predictable outcomes from tax audits motivate tax payer to comply with tax laws.	103 (30)	70(25.1)	43(15.5)	37(13.3)	25(9.0)

Source: Researches computation using SPSS version 22, 2024

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Test of Hypothesis

The correlation coefficient (R) indicates a strong positive relationship between independent and dependent variables. The R Square (R2) represents the proportion of variance explained by independent variables in a regression model. A value of 0.967 indicates 96.7% of the dependent variable's variability is accounted for by the independent variables. The Adjusted R Square (0.966) adjusts for overfitting and maintains high explanatory power. The Standard Error of the Estimate measures the variability of actual values around predicted values, representing the average distance between observed and predicted values. In this case, the standard error is 0.20470.

The Regression section of the ANOVA in Table 6 assesses whether the overall regression model is statistically significant. The high F-statistic (1.308E3) and very low p-value (.000) indicate that the regression model is statistically significant. This suggests that at least one of the independent variables has a significant effect on the dependent variable.

Table 5 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.983[a]	.967	.966	.20470

a. Predictors: (Constant), Fairness and impartiality, Professionalism and competence, Ensure compliance, Understandable communication, Reasonable duration, Consistent and predictable outcomes

b.

Table 6: Analysis of Variance

Model	Sum of Squares	Df	Mean Square	F	Sig.
1	.983[a]	.967	.966	.20470	
Regression	328.760	6	54.793	1.308E3	.000[a]
Residual	11.355	271	.042		
Total	340.115	277			

a. Predictors: (Constant), Fairness and impartiality, Professionalism and competence, Ensure compliance, Understandable communication, Reasonable duration, Consistent and predictable outcomes
b. Dependent Variable: Tax compliance

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Table 7: Coefficients[a]

		B	Std. Error	Beta	T value	Sig
1	(Constant)	.162	.050		3.253	.001
	Fairness and impartiality	.020	.013	.022	1.516	.131
	Professionalism and competence	.959	.014	.985	67.754	.000
	Penalties Ensure compliance	.286	.050	.294	5.734	.000
	Understandable communication	.059	.043	.069	1.372	.171
	Reasonable duration	-.297	.051	-.312	-5.869	.000
	Consistent and predictable outcomes	-.076	.045	-.084	-1.690	.092

a. Dependent Variable: Tax compliance

Discussion of findings

Findings from the multiple regression analysis in Table 5 showed that the constant (.162) represents the estimated value of the dependent variable (DV) when all independent variables are zero (assuming they are continuous and centered). T value (3.253) and Sig (.001) indicate that the intercept is statistically significant at the 0.05 level, suggesting that even without the independent variables, the dependent variable differs significantly from zero. Beta (.022) suggests a very small positive relationship with the dependent variable. T value (1.516) and Sig (.131) indicate that this variable is not statistically significant at the conventional significance level (0.05).

Therefore, fairness and impartiality, as measured here, may not significantly predict tax compliance. Beta (.985) indicates a strong positive relationship with the dependent variable. T value (67.754) and Sig (.000) indicate that this variable is highly statistically significant ($p < 0.001$), suggesting that higher perceptions of professionalism and competence among tax auditors strongly predict higher tax compliance. Beta (.294) indicated a moderate positive relationship with the dependent variable. T value (5.734) and Sig (.000) indicate that this variable is statistically significant ($p < 0.001$), suggesting that when taxpayers perceive audits as ensuring compliance through established penalties rather than harassment, it positively

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influences tax compliance. Beta (.069) suggests a small positive relationship with the dependent variable. T value (1.372) and Sig (.171) indicate that this variable is not statistically significant at the conventional significance level (0.05).

Thus, clear and understandable communication during audits may not significantly predict tax compliance in this model. Beta (-.312) indicates a moderate negative relationship with the DV. T value (-5.869) and Sig (.000) indicate that this variable is statistically significant ($p < 0.001$), suggesting that longer audit durations negatively impact tax compliance. Beta (-.084) suggests a small negative relationship with the dependent variable. T value (-1.690) and Sig (.092) indicate that this variable is marginally not statistically significant at the conventional significance level (0.05). There is a trend towards significance ($p = 0.092$), suggesting that consistent and predictable outcomes might have a slight negative impact on tax compliance, but it is not strong enough in this sample to be conclusive. This finding is consistent with research by Modugu & Anyaduba (2014), which suggests that tax compliance in Nigeria is significantly influenced by tax audit attributes.

Conclusion and Recommendations

Conclusion

The study concluded that there is a strong positive relationship between perceived professionalism and competence of tax auditors and tax compliance. Taxpayers are more likely to comply when they perceive auditors to be competent and professional. Assurance that penalties associated with tax laws are established to ensure compliance rather than harassment positively influences tax compliance behaviors among taxpayers. Longer audit durations negatively impact tax compliance. Taxpayers are less compliant when audits are perceived to be unnecessarily prolonged.

Recommendations

Based on the findings, it is recommended that;

i. Government should clearly communicate to taxpayers that audits are conducted to ensure compliance and maintain fairness in tax administration, with penalties for non-compliance clearly spelt out. This transparency can mitigate taxpayer resistance and improve voluntary compliance.

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ii. Government should streamline audit processes and ensure reasonable audit durations to minimize taxpayer burden and enhance compliance. Efficient audits are more likely to achieve compliance without unnecessary delays.

iii. Government should simplify complex tax laws and provide clear guidelines to both taxpayers and auditors. Enhance information management systems to facilitate secure and efficient access to taxpayer information, ensuring comprehensive audits.

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