CORPORATE TAX AUDIT AND TAX COMPLIANCE LEVEL IN NIGERIA

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Abstract
Tax audit is the independent examination of the returns submitted by taxpayers to the relevant tax authorities to ascertain the level of tax compliance by taxpayers. The objective of this paper is to examine the effect of corporate tax audit on the tax compliance level in Nigeria. To achieve this objective, data was collected from primary and secondary sources. The secondary sources was from scholarly published and unpublished studies and the primary source from a well structured questionnaire two hundred and fifty (250) questionnaire were sent and two hundred and twenty (220) respondents retrieved. The empirical analysis provided a significant relationship between tax audit penalty on tax compliance level in Nigeria. On the basis of the empirical result, the paper concludes that tax audit is one of the compliance strategies that can be used to achieve tax compliance in Nigeria because the average Nigerian is known for tax evasion and avoidance using all the available means of not paying the relevant tax to government. Therefore, the paper recommends amongst others that government should show some degree of accountability and transparency on the revenue collected to make citizens understand the connection between tax revenue and expenditure; the government should implement the relevant tax laws faithfully, equitably and fairly irrespective of the persons status and organization concerned; the relevant tax authorities at all levels should improve on the standard of tax audit employed for effectiveness and efficiency in tax administration to reduce the high level of non-compliance on those that are self-employed.

Keywords: *tax audit, Tax compliance, taxation, audit.*

INTRODUCTION:

One very important strategy that can be applied to increase the revenue base of both federal and state governments in Nigeria is the application of effective and efficient tax administration. This can only be achieved through well implemented tax compliance strategy for the citizens of Nigeria. However, non-compliance is a problem affecting the growth and development of tax as one of the major sources of revenue. Ola (2001) argues that non-compliance is a great disservice and a betrayal of the tax administration and revenue system. It should be seen by citizens of Nigeria as an unacceptable behavior and an act of economic sabotage. Therefore, in order to safeguard tax administration and sustain the confidence of taxpayers, tax audit program have been installed to monitor and detect the non-compliance traits in Nigeria (Ola, 2001; Appah, 2004; Kiabel and Nwikpasi, 2009; Appah, 2010). Azubike (2009) noted that a tax system is an opportunity for the government to collect additional revenue needed in discharging its present obligations.

Taxes and tax system are essential in nation building. They are required for state capacity building for meaningful economic development. The fundamental goal of any revenue authority is to collect taxes and duties payable according to the law. However, taxpayers are not always willing and ready to comply when it comes to the obligations imposed on them by law. Tax compliance is the ability and willingness of taxpayers to comply with tax laws, declare the correct incomes in each year and pay the right amount of taxes on time. Tax compliance is the taxpayer's willingness to obey tax laws in other to attain economic development and goals. From a wider perspective, tax compliance requires a degree of honesty. A key component of any tax system is the manner in which it is administered. No tax is better than its administration, so tax administration matters a lot. An essential objective of tax administration is to ensure the maximum possible compliance by taxpayers of all types with their tax obligations. Unfortunately, in many developing countries, tax administration is usually weak and characterized by extensive evasion, corruption and coercion. In many cases, overall tax compliance levels are low and large proportion of the informal sector of the economy escape tax. Tax compliance is a major problem for many tax authorities. It is not an easy task to persuade taxpayers to comply with tax requirements even as the tax laws are not always precise in some respects. Taxpayers are inherently disposed to reducing their tax liability either through tax evasion or tax avoidance. This may give rise to incorrect filling of their tax returns and loss of revenue to the government.

According to OECD (2006), a tax audit is an examination of whether a taxpayer has correctly assessed and reported their tax liability and fulfilled other obligations. Prior to 1998, tax payers in Nigeria (persons and corporations) were assessed to tax by the relevant tax authorities; a system otherwise known as government assessment. With the introduction of self-assessment scheme into the Nigerian tax system in 1998, tax payers are now required to file in their tax returns independently. This practice informed the need for tax audit, to ensure tax payers file in accurate information regarding their income and expenses. Tax payers inherently disposed to reducing their tax liability either through tax evasion or tax avoidance. In an effort by the FIRS to increase government revenue through taxation, reforms have been put in place by creating the following departments: Process Operations Department (POD), which had five units, including, (i) Information Communication and Technology Unit; (ii) Bank Collection Services Unit; (iii) The Return and Payment Processing Unit; (iv) Tax Refund Processing Unit; and, (v) procurement and Due Process Unit. However, these new processes and units faced serious challenges in the light of the existence of fraud syndicates and the absence of a secured electronic system. Yet another department was established. This was the Audit Department, because the new leadership realized that tax audit and investigation were core operational priorities of a modern system of administration. The existing units and processes in the pre-reform era lacked the requisite funding, training, independence and spread to function optimally. The investigation and intelligence division was created at the same time. It was later merged with the Audit Department in February 2006 to take over the operations of the Special Investigation Branch and the Intelligence Branch.

Statement of the Problem

One major problem inhibiting effective tax administration in emerging economics is tax evasion, i.e. deliberate refusal to pay tax. To combat this ugly phenomenon, various countries of the world have introduced tax audit into their tax system. Prior to 1998, tax payers in Nigeria (persons and corporations) were assessed to tax by the relevant tax authorities; a system otherwise known as government assessment. With the introduction of self-assessment scheme into the Nigerian tax system in 1998, tax payers are now required to file in their tax returns independently (Anyaduba and Modugu2014). This practice informed the need for tax audit, to ensure tax payers file in accurate information regarding their income and expenses. Tax payers are inherently disposed to reducing their tax liability either through tax evasion or tax avoidance. This may give rise to incorrect filling of their tax returns and a loss of revenue to the government. The objective of this study is to examine the corporate tax audit and tax compliance level of companies in Nigeria.

Research Questions

i. What are the effects of Corporate Tax Audit education on tax compliance in Nigeria?
ii. What are the significant of corporate tax audit penalties on tax compliance level in Nigeria?

Objectives of the Study

The main objectives of this study is to examine corporate tax audit and tax compliance level in Nigeria. The followings are the specific objectives, to:

i. Determine the effect of corporate tax audit education on the level of tax compliance in Nigeria.
ii. Determine the significant of corporate tax audit penalties on the level of tax compliance level in Nigeria.

In order to guide the study the following hypotheses were formulated:

Ho1: Corporate Tax audit education does not have significant effect on tax compliance level in Nigeria.

Ho2: Corporate Tax audit penalty has no significant influence on tax compliance level in Nigeria.

LITERATURE REVIEW AND THEORETICAL FRAMEWORK

THEORY OF COMPLIANCE

Any strategy to prevent tax evasion should begin with the theory of why people cheat on their taxes. Naturally, much of it is unconvincing and ambiguous. Nevertheless, to give an indication of the full range of variables that social scientists have studied in an attempt to answer this questions. The forum on tax administration (2004) "identified some of the basic theories of tax compliance" (According to Badara2012).

Sociological Theories: Sociologists tend to see the cause of variation in human behavior in the structure of the social system. Thus they explain people's actions by examining the forces that impinge on the position that they occupy within the system. Among other things, this means that they extend the basic economic model of crime control by making the point that law is not the only source of punishment and rewards. Tax payers life and work in society. They have families, friends and co-workers who are sources of reward or punishment. These social forces shape behavior just as effectively as the reward and punishment administered by the state. Given their basic assumptions about human behavior, sociologists are also likely to look to attitudes towards government views relating to the enforcement of tax laws, views about the fairness of the tax system, contact with the tax department and demographic characteristics as independent variables (Slemrod, 2000). Beron (2002) is of the view that Social Scientists from almost every discipline have turned their attention to tax evasion as social phenomena. What have we learned from their efforts? In a perfect world, by now we would have a theory about why people comply with the tax laws from which an interested tax administration department could deduce a comprehensive compliance strategy. However, compliance with the tax law typically means: True reporting of the tax base, Timely filling of the tax return, and Timely payment of the amount due (Slemrod, 2000).

Economic Theories: Economists approaching the question of why people fail to comply with the law began by constructing a theory based upon the assumption about human behavior that underlies all economics; namely that individuals generally act rationally in evaluating the cost and benefit of any chosen activity. Consequently, in modeling the choice confronting individuals who are deciding whether to engage in tax evasion, their basic model assumes that people would commit evasion when the expected utility of their criminal act exceeds its expected disutility (Slemrod, 2000).

Theory of Planned Behaviour: The theory of planned behavior states that the behavior of individuals within the society are under the influence of definite factors, originate from certain reasons and emerge in a planned way (Erten, 2002). Benket (2011) stated that the ability to perform a particular behavior depends on the fact that the individual has a purpose towards that behavior. Therefore, the factors that determine the purpose towards that behavior are attitude towards behavior, subjective norms and perceived behavioral control (Armitage and Conner, 2001). Ajzen (2002) stated that these factors are under the influence of behavioral beliefs, normative beliefs and control beliefs. Wenzel (2004) states that independent examination of the books and accounts of an organization by a duly appointed person to enable that person give an opinion as to whether the accounts give a true and fair view and comply with relevant statutory guidelines will show the beliefs of that organization. The American Accounting Association (1971) in its Statement of Basic Auditing Concepts in Hayes, Schilder, Daseen and Wallage (1999) described auditing as: a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic and events to ascertain the degree of correspondence between these assertions and established criteria and communicating the results to interested users.

Akinbuli(2010), Hayes et al (1999) reported that several theories of auditing were made to specify and determine the audit functions. Some of these theories include:

The Policeman Theory: This theory of auditing was purely on the arithmetical accuracy and on the prevention and detection of fraud. This theory makes the auditor to detect and prevent errors and fraud in organizations.

The Lending Credibility Theory: This theory of auditing regards the primary function of auditing to be the addition of credibility to the financial statements. Akinbuli (2010) states that audited financial statements can enhance stakeholders' faith in management's stewardship.

Theory of Inspired Confidence: This theory states that the stakeholders demand accountability from the management in return for their contribution to the organization.

The Moderator of Claimants Theory: This theory states that it is important that all vital participants in an organization continue to contribute. In order to continue these contributions, it is important that each group believes it receives a fair share of the organizations income.

Agency Theory: This theory is associated with conflicting interest of shareholders and management of organizations, suggesting, that the less informed party will have to demand for information that monitors that behavior of better informed manager (Akinbuli, 2010). According to Hayes et al (1999), agency theory can be used to explain the supply side of the audit market. The contribution of an audit to third parties is basically determined by the probability that the auditor will detect errors in the financial statements and the auditor's willingness to report these errors(Appah&Eze2013).

NATURE AND SCOPE OF TAX COMPLIANCE

Dijike (2007) stated that tax compliance is the willingness of individuals to comply with relevant tax authorities by paying their taxes. Tax compliance can be defined as an ability of a tax liable body to submit accurate, complete and satisfactory returns in conformity with tax laws and regulations of the state to the authority for the purpose of tax assessment (Badara, 2012). Sarker (2003) also reported that tax compliance is the degree to which a taxpayer complies (or fails to comply) with the tax rules of his country. Brown and Mazur (2005) noted tax compliance as a multi-faceted measure and theoretically, it can be defined by considering three distinct types of compliance such as Payment compliance (timely payment of all obligations). Filling compliance (the timely filling of any required return), and Reporting compliance (the accurate reporting of income and of tax liability). The organization for economic cooperation and development (2001) divided compliance into administrative compliance and technical compliance.

Administrative Compliance refers to complying with administrative rules of lodging and paying. This compliance can also be called reporting compliance or regulatory compliance. Technical Compliancerefers to complying with technical requirements of tax laws. Tax compliance can be achieved through the application of public relations, tax education, tax consultation and guidance and examination.

Tax Public Relations: The purpose of public relations is to build a tax conscious environment not only among taxpayers but also among the public including latent taxpayers, and can be categorized as the need to enhance tax compliance; diffuse and enhance public knowledge of taxation; improve mutual understanding and trust between taxpayers and tax authorities and obtain the understanding and cooperation from mass-media for tax administration (Sarker, 2003; Appah & Eze 2013).

Awareness of Offences and Penalties and Tax Compliance

According to Palil and Mustapha (2011), a theoretical economic model introduced by (Allingham&Sandmo1972) has clearly indicated that penalties as well as audit probability have an impact on tax compliance, the higher penalty and the potential audit probability the greater the discouragement for potential tax evasion. However, the more complex models like principal agent theory and game theory suggest that penalties and audit probability are difficult to portray in compliance models as the results are determined endogenously with tax cheating (Andreoni1998). Andreoni, suggested that to overcome the endogenous tax cheating, it is necessary to control the enforcement environment artificially by using laboratory experiment methods. This has been evidenced by Beck, Davis and Jung (1991) and Becker, Buchner and Sleeking (1987) through their experiments in which they found that penalty rates affect tax compliance in accordance with the theory. However, an experimental approach does limit the environment to a narrow perspective compared to the real world. Bryman and Bell (2003) suggested that an experimental approach is only suitable for a study that can be addressed with a high degree of experimental arrangement and control. Nevertheless, an experimental approach for a tax compliance study might show a smaller effect or influence than for direct observation (Alm, Jackson & Mckee, 1992). In addition, Marrelli (1984), Wang and Conant (1988), Gordon (1990), Marrelli and Martina (1989) indicated results in the other way around, in which penalty rates had a positive association with evasion, meaning that higher rates did indeed encourage people to cheat.

Since previous studies indicate that penalty rates impact upon tax compliance behavior, the awareness of offences was presumed to have a significant influence as well. If the taxpayers are aware of the offences they are committing when evading tax and the consequences of being non compliant tax payers, they might reduce their tendency to evade tax. On the other hand, if they are not aware of the implications of being dishonest in terms of the offence they are likely to be charged with, if caught, they might be more inclined to cheat because they presume that they will not be detected and could save money. Thus, educating taxpayers and keeping them well informed with the sentences of being an evader may be important, as a prevention measure is better than cure (imposition of a penalty). As stated by Anyadudu and Modugu (2014).

MATERIALS AND METHODS

The research design adopted in this study is survey design. The primary source of data employed is the administration of questionnaires. The questionnaire consists of two parts. The part A of the questionnaire is on the demographic characteristics of the respondents while part B of the questionnaire is on the research questions on the research variables namely, tax compliance, tax knowledge and tax penalty. Five-point Likert-style rating scale method of questionnaire was employed in this study ranging from strongly agree of 5-point to strongly disagree of 1-point. The likert-style rating method of questionnaire design enables numerical value to be assigned to cases for easy quantitative analysis. To test for the content validity of the instrument used for data collection in this study, the questionnaire was given to three experts in the Departments of Accounting Business Administration and Sociology of Bayelsa State polytechnic for review. To ensure the reliability of the instrument, the questionnaire was pre-tested using fifty two (52) respondents. Using Statistical Package for Social Sciences (SPSS) to test the reliability, the Cronbach alpha coefficient of 0.82 was obtained. This compares favourably with a stipulated standard of above 0.07 for reliability test. The reliability ratio for this work (0.82) showed that all the research questions in the questionnaire have internal consistency.

The small and medium enterprises in Yenagoa, Bayelsa State, Nigeria constitute the population of the study. A total of two hundred and fifty respondents were randomly sampled from small and medium enterprises in Yenagoa City Bayelsa State, Nigeria. Out of the two hundred and fifty (250) questionnaires administered to SME operators, two hundred and twenty (220) were retrieved and analyzed. The data obtained were analyzed using Statistical Package for Social Sciences (SPSS) to obtain the frequency distributions of the demographic characteristics of the respondents. The descriptive statistics of the variables as well as the ordinary least square (OLS) multiple regression analysis was carried out to assess the relative predictive power of the independent variables (i.e. tax knowledge and tax penalty) on the dependent variable (i.e. tax compliance). The ordinary least square was adopted for the purpose of hypothesis testing. The ordinary least square was guided by the following linear model:

Yi = f (a1, a2) ……………………………………………………1
TCL = f(CTAED, CTAP)……………………………………..2
$TCL = B_1 + B_1CTAED + B_2CTAP + C$ ……………..…3

That is $B_1-B_2 > 0$
TCL = Tax compliance level; CTAED = Corporate Tax Audit Education; CTAP = Corporate Tax Audit Penalties; B_1-B_2 are the coefficients of the regression, while E is the error term capturing other explanatory variables not explicitly included in the model. However, the model was tested using the diagnostic tests of heteroskedasticity, serial correlation, normality and misspecification (Gujarati and Porter, 2009; Asterious and Hall, 2007). Augmented Dickey-Fuller was also used in the study for stationarity of data.

DATA ANALYSIS

Table 1: Summary of Regression Results showing the Effect of Corporate Tax Audit Education on Tax Compliance Level.

Variables	Coef	t-cal	t-tab (0.005,219)	Sig.T	R	R^2	F-cal	F-tab (0.05,1,218)	Sig f
Constants	1.555	9.191		0.000			148.78		
CTAED	0.563	12.198	1.971	0.000	0.637	0.406	3	3.884	0.000

Dependent Variable: Tax Compliance Level
Source: SPSS 20.0 Output (based on 2017 field survey data)

TCL = f(CTAED)………………………la
$TCL = a_0 + a_1CTAED + E$ ………1b
TCL = 1.555 + 0.563CTAED
t-values in bracket (9.191)(12.198)

Table 1 revealed the Pearson's correlation coefficient of 0.637, this correlation coefficient is high indicating that a strong relationship exist between Corporate Tax Audit Education and Tax Compliance Level. The coefficient of determination (R^2) = 0.406. this implies that a variation of 40.6% of Tax Compliance Level is explained by the change in Corporate Tax Audit Education. The remaining 56.4% is explained by other variables not included in this model. The F-calculated of 3.884 had a significant F-valued 0.000, also, conventionally F-cal = 148.783> F-tab (0.05,1,218) = 3.884. Accordingly the researchers upheld a good model utility.

TEST OF HYPOTHESIS 1

$H0_1$: Corporate Tax Audit Education does not have significant effect on Tax Compliance Level in Nigeria.
The table revealed that Corporate Tax Audit Education had a t-cal of (12.198)> t-tab (0.05, 219) = 1.971, and a corresponding significant/probability value (pv) = 0.000 < 0.05 level of significance, thus the researchers reject the null hypothesis and conclude the Corporate Tax Audit Education significantly affect Tax Compliance Level in Nigeria.
Table 2: Summary of Regression Results showing the Effect of Corporate Tax Audit Penalty on Tax Compliance Level

Variables	Coef	t-cal	t-tab (0.05,219)	Sig.T	R	R^2	F-cal	F-tab (0.05,1,218)	Sig f
Constants	1.462	8.420		0.000			154.11		
CTAED	0.563	12.440	1.971	0.000	0.644	0.414	9	3.884	0.000

Dependent Variable: Tax Compliance Level
Source: SPSS 20.0 Output (Based on 2017 field survey data)
TCL = f(CTAED)………………………2a
TCL = b_0+ b_1CTAED + $_E$ ………2b
TCL = 1.462 + 0.586CTAED
t-values in bracket (8.420)(12.440)

Table 1 revealed the Pearson's correlation coefficient of 0.644, this correlation coefficient is high indicating that a strong relationship exist between Corporate Tax Audit Penalty and Tax Compliance Level. The coefficient of determination (R^2) = 0.414. this implies that a variation of 41.4% of Tax Compliance Level is explained by the change in Corporate Tax Audit Penalty. The remaining 50.6% is explained by other variables not included in this model. The F-calculated of 3.884 had a significant F-value 0.000, also, conventionally F-cal = 154.119> F-tab (0.05,1,2010) – 3.884. Accordingly the researchers upheld a good model utility.

TEST OF HYPOTHESIS 2

$H0_2$: Corporate Tax Audit Penalty does not have significant effect on Tax Compliance Level in Nigeria. The table revealed that corporate Tax Audit Penalty had a t-cal of (12.440) >t-tab (0.05,219)= 1.971, and a corresponding significant/probability value (pv) = 0.000 < 0.05 level of significance, thus the researchers reject the null hypothesis and conclude that Corporate Tax Audit Penalty significantly affect Tax Compliance Level in Nigeria.

Table 3: Summary of Results showing the Effect of Corporate Tax Audit Education and Corporate Tax Audit Penalty on Tax Compliance Level.

Variables	Coef	t-cal	t-tab (0.05,219)	Sig.T	R	R^2	F-cal	F-tab (0.05,2,217)	Sig f
Constants	1.467	8.233		0.000					
CTAED	0.252	2.723	1.971	0.042	0.652	0.425	80.289	3.037	0.000
CTAP	0.345	2.723		0.007					

Dependent Variable: Tax Compliance Level
Source: SPSS 20.0 Output (Based on 2017 field survey data)
TCL = f(CTAED)………………………2a
TCL = b_0+ b_1CTAED + $_E$ ………2b
TCL = 1.427 + 0.252CTAED + 0.345CTAP
t-values in bracket (8.233)(2.049)(2.723)

Table 3 revealed the Pearson's correlation coefficient of 0.652, this correlation coefficient is high indicating that a strong relationship exist between Corporate Tax Audit Penalty and Tax Compliance Level. The coefficient of determination (R^2) = 0.425. this implies that a variation of 42.5% of Tax Compliance Level is explained by the change in Corporate Tax Audit Penalty. The remaining 57.5% is explained by other variables not included in this model. The F-calculated of 3.037 had a significant F-value 0.000, also, conventionally F-cal = 80.289> F-tab (0.05,2,217) – 3.037. Accordingly the researchers upheld a good model utility.

TEST OF HYPOTHESIS 2

Corporate Tax Audit Education had a t-cal of (2.049) >t-tab (0.05,219) = 1.971, and a corresponding significant/probability value (pv) = 0.042<0.05 level of significance, thus Corporate Tax Audit Education significantly affect Tax Compliance Level.

CONCLUSION AND RECOMMENDATIONS

This paper examined the corporate tax audit on tax compliance in Nigeria. The paper reviewed relevant literatures that provide strong evidence of the effectiveness of tax audit on voluntary tax compliance. This research empirically substantiated the results of prior studies of the relationship between tax audit and tax compliance. The study highlights the various variables in the tax compliance model developed.

The empirical analysis provided a strong association between the various types of audit conducted by tax and revenue officials and the various elements in the tax compliance model. On the basis of the empirical result, the paper concludes that tax audit is one of the compliance strategies that should be taken seriously to achieve tax compliance in Nigeria because the average Nigerian is known for tax evasion and avoidance using all the available means of not paying the relevant tax to government. Therefore, the following recommendations are provided to achieve an effective and efficient tax audit and compliance in Nigeria:

1. The government should show some degree of tax accountability on the revenue collected to make citizens understand the connection between tax revenue and expenditure.
2. The government should implement the relevant tax laws faithfully, equitably and fairly irrespective of the persons status and organization concerned.
3. The relevant tax authorities at all levels should improve on the standard of tax audit employed for effectiveness and efficiency in tax administration to reduce the high level of tax evasion on those that are self employed.
4. Tax audit should aim at reducing the problems of tax evasion, tax avoidance and other tax irregularities for standardization to improve the level of filing, payment and reporting compliance in Nigeria.
5. The scope of tax audit and investigation should be increased in Nigeria to ensure proper submission of accurate and current returns for proper documentation and computation.
6. The relevant tax authorities should improve the public awareness of the importance of tax payment and the effect of non-tax payment, so that the level of compliance can be improved and non-compliance will be minimized.

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