Realization of Economic, Social, and Cultural Rights in Ethiopia: Lifting the Veil of Tax Evasion and Avoidance

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Abstract

Ethiopia is a party to the International Covenant on Economic, Social and Cultural Rights (ICESCR), which obliges the government to ensure the realization of economic, social and cultural (ESC) rights to the maximum of its available resources. Taxation, which is the most predictable source of government revenue, is a critical part of the state's compliance with the Covenant's obligation. Therefore, Member States are required to levy effective types of taxation, while discouraging diversion of resources. Putting in place effective legal frameworks aimed at combating tax avoidance and evasion, is not only an ICESCR compliance step, but also *a sine qua non* of generating sufficient resources that can be used to improve the socio-economic conditions of citizens, particularly the vulnerable groups. This paper examines Ethiopia's tax policies and practices, focusing on their effectiveness in tackling tax avoidance and tax evasion practices, through the prism of human rights principles and standards. The findings reveal that despite having robust legislations to address tax abuse practices, and a consistent nominal increase in tax revenue over the past two decades, Ethiopia is experiencing notable losses in potential tax revenue, and the tax-to-GDP ratio has been gradually declining, particularly for the last seven consecutive fiscal years. The prevalence of both domestic and international tax abuse practices contributes significantly to this situation. Although comprehensive data on the exact extent of these practices is limited, the paper draws on available information, including the State of Tax Justice reports in 2020 and 2021, to highlight how these abusive practices drain funds that could be invested in education, health, poverty reduction, and other critical areas.

Keywords: *taxation, maximum available resources, avoidance, evasion, and socio-economic rights*

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Introduction

Taxation policies have a significant impact on the realization of human rights, as emphasized by Philip Alston, the United Nations (UN) Special Rapporteur on Extreme Poverty and Human Rights, who says that "[*t*]*ax policy is, in many respects, human rights policy* (UN Special Rapporteur (Alston) 2015, para.13)." When taxation policies are effectively designed and implemented, they can serve as a facilitator for the enjoyment of human rights. This relationship between taxes and human rights can be broadly categorized into three principal areas: resource mobilization, redistribution, and accountability (Saiz 2013, 81-87; UN Special Rapporteur (Carmona) 2014, paras.36-53). First, tax is linked with the duty of states to devote the maximum of available resources for the fulfillment of human rights as it supplies the revenue that states need to finance the provision of essential services like education, healthcare, water, sanitation, and electricity (UN Special Rapporteur (Carmona) 2014, paras.42-44). By levying taxes, states can generate the resources needed to invest in and maintain these services. The obligation to mobilize resources, within the human rights law regime, is found in core human rights treaties to which Ethiopia is a party, including ICESCR,[12] the Convention on the Rights of Persons with Disabilities (CRPD),[13] and the Convention on the Rights of the Child (CRC).[14] While the link between taxation and human rights is most clear in ESC rights, it also extends to civil and political rights (Saiz 2013, 78),[15] as the effective realization of all rights necessitates various measures like "legislative, judicial, administrative, and educative," all of which require resources (UN Human Rights Committee (UNHRC) 2004, para.7). There are also soft laws that recognize the vital link between taxation and human rights. For instance, the 2030

12 The International Covenant on Economic, Social and Cultural Rights (ICESCR) Art 2(1).

13 The United Nations Convention on the Rights of Persons with Disabilities (2006) Art 4(2).

14 The United Nations Convention on the Rights of the Child (1989) Art 4.

15 In this regard, Article 2(2) of the International Covenant on Civil and Political Rights (ICCPR) imposes obligations upon member states to "take the necessary steps to give effect to the rights set forth therein."

Agenda for Sustainable Development emphasize the importance of this connection and urge states to enhance their "domestic capacity for tax and revenue collection (Goal 17)," and to address illicit financial flows (Goal 16(4)), including individual and corporate tax abuse (Tax Justice Network (TJN), Public Services International (PSI) and Global Alliance for Tax Justice (GA4TJ) 2021, 20)

The second area where human rights and taxation intersect is in the redistribution of resources caused by taxation (UN Special Rapporteur (Carmona) 2014, paras. 16-17 & 45-50). A progressive taxation scheme allows states in redistributing wealth from the high net-worth individuals and large corporations to the poor, thereby redressing systemic social, economic, and gender inequalities and combating discrimination (Hodgson and Sadiq 2017, 108-118; UN Special Rapporteur (Carmona) 2014, paras. 16-17 & 45-50). This is in line with the right to equality and to non-discrimination, which implicitly urges states to establish a progressive tax system with a redistributive capacity that preserves, and gradually increases, the income of poorer households (UN Special Rapporteur (Carmona) 2014, paras. 51-53).

The third aspect where taxation and human rights intersect is the pivotal role of taxation in ensuring government accountability (Sjursen 2023; Prichard 2015; UN Special Rapporteur (Carmona) 2014, paras. 51-53). Taxation, being a fiscal social contract whereby citizens assent to pay taxes which is used by the government to implement programs for the collective welfare, including the realization of citizens' rights, has a crucial role in cementing the bond of accountability between states and citizens. Research has shown that governments that rely on domestic tax revenues have an incentive to be more responsive to taxpayers (Ross 2004; Saiz 2013, 83). The UN Special Rapporteur on Extreme Poverty and Human Rights (Carmona) also averred that states that have sufficiently tapped their tax bases tend to display higher levels of accountability and participation in public affairs (2014, paras. 51-53).

The aim of this paper is to examine Ethiopia's tax policies and performances through the lens of human rights principles derived from treaties ratified by Ethiopia, with a specific focus on the ICESCR. From its fiscal performance reports, Ethiopia's revenue from taxation has seen a substantial upsurge in nominal values since the end of the socialist era in 1991. The tax revenue recorded a notable surge from Birr 3.08 billion in 1993/94 to Birr 8.19 billion in 2002/03 (Hailu 2004, 3; Kinde and Alem 2018, 69). From 2005 to 2015, the figure increased thirteen-fold, from Birr 12.4 billion to Birr 165.3 billion (UNDP Ethiopia 2016, 1). Furthermore, there was a continuous increase in tax revenue from the fiscal year 2015/16 to 2020/21, reaching 190.5 in 2015/16, 210.2 in 2016/17 (Ministry of Finance Ethiopia 2019, 12), 235.2 in 2017/18, 268.5 in 2018/19, 311.5 in 2019/20, and 388.8 in 2020/21, all measured in billions of birr (Ministry of Finance Ethiopia 2022, 6). Additionally, the country managed to collect 336.7 billion in tax during the 2021/22 fiscal year (Ministry of Revenues of Ethiopia 2022), and 324.3 billion birr in the first nine months of the current fiscal year (2022/23) (Ethiopian Monitor 2023). These figures show an increase in tax collection in nominal terms over the past two decades. However, when examining the tax-to-GDP ratio, which measures a country's tax revenue in relation to its GDP, the figures reveal disappointing results, as discussed in the third section of this paper.

The paper is organized into five sections, including this introduction and the second section that introduces the methodology and the caveats the paper puts forward. The third section illustrates how the ICESCR, particularly the provisions on the obligation to mobilize resources and the principle of equality and non-discrimination, impose constraints on the discretionary power of states in formulating fiscal policies, including taxation. The fourth section delves into the Ethiopian context, analyzing the country's tax policies, tax revenue performance, particularly in terms of tax-to-GDP contribution, and then delving into the issue of tax evasion and avoidance and their impact on the realization of ESC rights. The paper ends with a conclusion.

Methodology and Caveats

Methodology

The paper adopts a qualitative desk-based approach, drawing insights from primary and secondary sources. Primary sources include Ethiopia's domestic laws and relevant human rights treaties ratified by Ethiopia, particularly the ICESCR. Secondary sources comprise scholarly works and reports from civil society organizations working on the human rights and tax issues. The examination of human rights treaties, especially the ICESCR, aims to establish Ethiopia's obligations to combat tax abuse practices to fulfill its human rights commitments. It leverages soft law instruments, such as general comments and concluding observations from the CESCR, to operationalize the principles enshrined in these treaties. The analysis of Ethiopian national legislation and policies on tax issues aims to assess their effectiveness in addressing tax evasion and avoidance practices, considering approaches adopted by other jurisdictions. The paper also draws on Ethiopian government reports from many years over the last two decades on annual budgeted tax revenue and actual tax revenue, which are supplemented by scholarly publications and reports from civil society actors and inter-governmental organizations. This analysis pursues twin aims: assess Ethiopia's tax revenue collection performance via metrics including nominal intake, and tax revenue as a percentage of GDP; and unveil the implications of revenue losses to abusive tax practices in relation to the government's budget for critical social sectors like education, health, justice, and employment programs in the 2022/23 fiscal year.

Caveats

There are two caveats to be noted before moving on to the next section of the paper. Firstly, while there exists a plethora of materials discussing tax abuse practices in Ethiopia, there is no comprehensive figure on the exact amount of revenue lost due to these practices. This constrains a full impact analysis vis-à-vis budgets for critical sectors. The paper thus attempts only to demonstrate, using available information (including the State of Tax Justice reports in 2020 and 2021), how even conservative estimates of revenue leakage stemming from abusive tax practices represent substantial sums of tax revenue lost that could have otherwise expanded budgets to meet Ethiopia's ICESCR obligations. Secondly, the paper does not address the issue of expenditure, which is another critical aspect in the intersection of tax and human rights. It focuses on revenue collection and operates under the assumption that the money lost due to tax-abusive practices could have funded to ensure the realization of socio-economic rights as provided under the ICESCR. However, it is crucial to recognize that the money lost due to abusive tax practices, even if it were collected, is not guaranteed to be allocated to fund socio-economic rights; the government may, for example, allocate it towards strengthening the military. Therefore, considering not only revenue collection, but also expenditure patterns, which are beyond the scope of this paper, is necessary for a complete analysis of the nuances between tax collection and the realization of human rights.

Taxation as a Means to Ensure Implementation of Esc Rights Under the Icescr: tax as a Resource and Tool for Fighting Inequality

Neither the ICESCR nor other human rights treaties prescribe specific fiscal policies for governments. They do, however, limit the discretion of states in formulating fiscal policies, including taxation (UN Special Rapporteur (Carmona) 2014, para. 4). The main limitation of this discretion is rooted in the duty of state parties, under Article 2(1) of the ICESCR, to make full use of all their available resources individually and collectively to progressively achieve the full implementation of the rights in the Covenant. Article 2(1) of the ICESCR commits States parties to:

"take steps, individually and through international assistance and co-operation, especially economic and technical, to the maximum of [their] available resources, with a view to achieving progressively the full realization of the rights recognized in the present Covenant by all appropriate means, including particularly the adoption of legislative measures."

This provision encompasses various sub-obligations, including taking steps, allocating maximum resources, and fulfilling obligations of international assistance and cooperation. The duty to "take steps" stands for the obligation of member states to actively take targeted and specific measures to fulfil ESC rights (UN Committee on Economic, Social and Cultural Rights (CESCR) 1990, paras. 2-12; CESCR 1999, para. 43; CESCR 2000, para. 30; United Nations Committee on the Rights of the Child 2016, para. 18; Limburg Principles on the Implementation of the International Covenant on Economic, Social and Cultural Rights 1986, para. 16).[16] These measures may include adopting legislations, implementing policies, establishing programs, and creating mechanisms that promote and protect the rights outlined in the Covenant. The reference to "resource availability" and "achieving progressively" under the provision reflects a recognition that the implementation of ESC rights can be hindered by a shortage of resources and can only be realized incrementally over time (Office of the United Nations High Commissioner for Human Rights (OHCHR) 2008, 13). In the same vein, the reference to "available resources" shows that a state's compliance with its obligations should be assessed considering the resources, both financial and non-financial, at its disposal (OHCHR 2008, 13). By referring to "available resource," the provision also makes fiscal issues, including mobilization of resources, a human rights issue.

Treaty-monitoring bodies, including the CESCR, interpret the notion of resources broadly and evaluate states' adherence to this obligation not only based on what they can achive with existing resources, but also by mandating them to undertake all necessary measures to mobilize resources. According to the CESCR General Comment 3, "available resources are not limited to those existing resources within a state but include those available from the international community via international cooperation and assistance (1990,

[16] The relevant part of Limburg Principles provides as follows. "All States Parties have an obligation to begin immediately to take steps toward full realization of the rights contained in the Covenant."

para. 13)." It also encompasses resources that a state has a potential to develop but has not yet developed, including what states can gather from taxation (UN Special Rapporteur (Carmona) 2014, para. 27; UN Independent Expert on the Effects of Foreign Debt and Other Related International Financial Obligations of States on the Full Enjoyment of All Human Rights, particularly Economic, Social and Cultural Rights (Bohoslavsky) 2016, paras. 12-13). This implies that resources states do not collect due to tax abuse practices, or bribery, corruption and money laundering, constitute a potentially available resource (UN Special Rapporteur (Carmona) 2014, paras. 27 & 58-62).

The CESCR urges states to mobilize resources, including by enforcing progressive taxation schemes (CESCR 2017, para. 23). The Inter-American Commission on Human Rights also notes that State's actions concerning its taxation policy should comply with the human rights legal framework (Unit on Economic, Social and Cultural Rights 2017, para. 502). The UN Special Rapporteur on Extreme Poverty and Human Rights further highlights taxation policies as a significant factor influencing the enjoyment of human rights (UN Special Rapporteur (Carmona) 2014; UN Special Rapporteur (Alston) 2015). It portrays taxation as a critical tool for addressing inequality by generating the resources required to realize human rights.

Here it is important to note that states are not bound to rely solely on taxation as the primary source of resources to comply with their commitments pursuant to the ICESCR. They can collect the resources they need to meet their obligations from sources other than taxes. However, states cannot argue that they are unable to implement covenant rights due to a lack of resources while allowing potential resources to be squandered through tax evasion and avoidance practices. Such an argument would put them at risk of non-compliance with their obligation to allocate the maximum available resources for implementing the rights outlined in the Covenant (Tuazon and Stenlund 2019, 48; UN Special Rapporteur (Carmona) 2014, para. 60). In other words, they cannot argue that they are not obliged to fulfill their obligations immediately due to a scarcity of resources while allowing tax evasion and avoidance practices to persist within their jurisdiction, as it would mean that not all available resources are being devoted to fulfilling those obligations.

In addition to the obligation to devote the maximum of available resources, human rights treaties including the ICESCR, have human rights principles such as the principles of equality and non-discrimination that are relevant to state resource mobilization. Per this principle, member states must set up a progressive tax system with a redistributive ability, which preserves, and gradually increases, the income of households with lower incomes. In this regard, the CESCR and the Special Rapporteur on Extreme Poverty and Human Rights assert that taxation must be implemented in such a way that it has a redistributive effect on resource mobilization (CESCR 2017, paras. 16-17; CESCR 2016, paras. 41-42; UN Special Rapporteur (Carmona) 2014, paras. 45-50). Accordingly, states must address any action or omission related to tax that perpetuate discrimination and inequality. A state that possesses a very narrow tax base or neglect to tackle abusive tax practices may face difficulties in financing social protection programs or public services, a condition that would most likely generate or entrench inequalities (UN Special Rapporteur (Carmona) 2014, para. 17). Also, if a tax system lacks progressivity, it would transgress the equality principle.

Hence, the responsibility of states under ICESCR to use the maximum of their available resources to finance ESC rights, coupled with the principles of equality and non-discrimination, establishes limits on their discretion in developing and implementing tax policies. Member states facing resource challenges or socioeconomic inequalities like Ethiopia therefore need to undertake specific measures regarding their tax policies. Firstly, states, especially those with the lowest tax-to-GDP ratio, must expand their tax base in human rights-compliant ways to meet their obligation to finance rights and tackle social inequality (Schutter 2017, 6; UN Special

Rapporteur (Carmona) 2014, para.55). The CESCR, in its concluding observations to Guatemala, El Salvador, and Paraguay, urged states to setup a tax system that is adequate, progressive, and socially equitable (2014, para. 8; 2014, para.8; 2015, paras. 10-13). Secondly, it is imperative to ensure sufficient progressivity in tax policies (Schutter 2017, 6; CESCR 2015, para. 14). Thirdly, it is crucial to address tax evasion and tax avoidance practices (Schutter 2017, 6). Both contribute to resource diversion and have a negative impact on the redistributive effect of taxation in all countries, regardless of their level of development (UN Special Rapporteur (Carmona) 2014, para. 5; UN Special Rapporteur (Alston) 2020, para. 47). Tolerance of states to these practices will run afoul of the obligation to devote the maximum of available resources as provided under Article 2(1) of the ICESCR. It was said that "[i]increasing tax levels without also addressing tax evasion would be like pouring water into a leaking bucket (Schutter 2017, 5)." Moreover, tax avoidance and evasion practices hobble the capacity of governments to undertake redistributive policies, thereby undermining the principles of equality and non-discrimination. This is because those engaging in these practices end up paying less than others with similar or even lower capacity to pay. Further still, these abusive practices, although seemingly neutral, disproportionately benefit wealthy individuals and corporations who can afford tax advisors and lawyers, thereby exacerbating the disadvantage of the most vulnerable populations. This can lead to indirect discrimination (UN Special Rapporteur (Carmona) 2014, para. 60). It goes without saying that these abusive practices force governments to resort to regressive taxes, which disproportionately burden low-income earners (UN Special Rapporteur (Carmona) 2014, para. 60). Beyond the economic implications, the prevalence of such practices erodes public confidence in the government, thereby undermining the essential bonds of accountability between states and their citizens.

Alarmed by these practices and their disproportionate impacts on the realization of ESC rights, the CESCR has taken a firm stance. In its General Comment No 24, the Committee urges member states to end tax avoidance, tax abuse, and fraud (2017, paras. 15, 23 & 37).

It was noted further that combating tax evasion not only increases available resources to fulfil the obligations under Article 2(1) of the ICESCR but also puts an end to practices that create significant inequalities (UN Special Rapporteur (Carmona) 2014, para. 60). Along a similar line, the CESCR, in its concluding observations on state parties' reports such as those from the Dominican Republic (2016, paras. 17-18), Honduras (2016, paras.19-20), Kenya (2016, paras.17-18), and the United Kingdom and Northern Ireland (2016, paras.16-17), urges states to undertake measures to address tax abuse practices, by corporations and high net-worth individuals. It also urges Spain to take a string of measures to tackle tax fraud of large inheritances (2018, paras. 15-16).

The next section discusses Ethiopia's fiscal policies, focusing on anti-tax abuse policies, tax-to- GDP performance, and the repercussions of abusive practices on financing ESC rights in the country.

Human Rights and Ethiopia's Tax System

Ethiopian Fiscal Policies on Revenue Mobilization

Ethiopia has undergone multiple rounds of tax policy reforms since the end of the socialist regime in 1991, and over the course of the last two decades, these reforms have intensified significantly (Eshetu 2017, 26-27). The country, for example, abolished its sales tax in 2003 in favor of VAT (and a turnover tax for businesses not eligible for VAT registration), and it adopted tax identification numbers (Eshetu 2017, 26-27). During the implementation of the two Growth and Transformation Plans (GTP I and II) from 2010 to 2020, several tax reform measures were taken, including enacting a separate tax administration proclamation,[17] as well as new excise and income tax laws to boost revenue and increase tax base, among

[17] Federal Tax Administration Proclamation No 983/2016 (TAP). TAP, adopted in 2016, aims to increasing efficiency, effectiveness, and measurement in the tax administration process.

other things.[18] The GTPs were primarily intended to strengthen the enforcement powers of the Ethiopian tax administration to mobilize adequate revenue (GTP I, 27-38 & 96; GTP II, 9-10, 85, 90, 107, 111-114 & 195), but they also addressed other aspects of Ethiopian tax policy, including tax equity (Gemechu 2013, 110-116). In the same vein, Ethiopia's new 10 Year Development Plan, i.e., "A Path to Prosperity" (2021-2030), which replaced the GTPs that were in effect from 2010 to 2020, also includes the tax reform agenda. This Plan identifies inadequate capacity to mobilize domestic resources as one of the past major development challenges, and vows to achieve a healthy balance between revenue and expenditures, including by increasing tax collection and expanding the tax base (Ethiopia's Ten Years Development Plan: A path way to Prosperity 2021-2030, 5&32). The Plan includes an ambitious objective to increase the country's tax-to-GDP ratio to 18.2 percent by 2030 from 9.2 percent in 2019/20 (32).

It is clear from these legislative and policy frameworks that Ethiopia aims to boost its revenue and redistribute resources through taxation. However, it is worth noting that the country's tax legislations do not explicitly address taxation as a human rights issue, nor do they make references to the government's obligation under the ICESCR or other human rights instruments. This decoupling is presumably the result of a tradition of viewing revenue policy as entirely separate from human rights issues, and it carries significant ramifications, including potentially fostering judicial timidity to interpret tax laws in a manner that recognizes this linkage.

Ethiopian Government Legislative Tails in Combating Tax Avoidance and Evasion

The three most common ways in which taxpayers reduce their tax liabilities are through tax avoidance, tax evasion, and tax planning. The right of citizens to limit their tax liabilities through tax planning is acknowledged in democratic societies (Mazur 2012, 551). The right does not apply, however, to tax evasion and avoidance.

[18] Federal Income Tax Proclamation No 979/2016 (ITP) Preamble para 2. The Excise Tax Proclamation No 1186/2020 Preamble Para 3. This Excise Tax Proclamation has now been revised with the Excise Tax (Amendment) Proclamation No 1287/2023.

Tax Avoidance

Tax avoidance refers to the practices of exploiting loopholes or inconsistencies in tax legislations to reduce or avoid owed taxes (Otto, et al. 2015, 4-5). While not an illegal act per se, it entails obtaining tax benefits from a transaction that adheres to the literal reading of tax provisions but circumvent their intended purpose (Mazur 2012, 553). The practice not just erodes government tax revenues, but also undermines the redistribution effect of taxation, resulting in inequality, as the affluent members of society are more likely to take advantage of the legal loophole by, for example, hiring a tax expert to minimize or eliminate their tax liability (UN Special Rapporteur (Carmona) 2014, para. 60). It also unfairly shifts the tax burden. Several countries, recognizing these harmful effects of tax avoidance, have taken a wide range of measures to combat it. These measures are broadly classified as Specific Anti-Avoidance Rules (SAAR) and General Anti-Avoidance Rules (GAAR) (Ostwal and Vijayaraghavan 2010, 63; Waerzeggers and Hillier 2016, 7). Both approaches of tax avoidances are recognized under Ethiopian tax laws.

SAARs, as their name suggests, target specific tax avoidance practices or areas where abuse has been identified (Ostwal and Vijayaraghavan 2010, 63; Waerzeggers and Hillier 2016, 7). The scope of their application is limited to specific "known" arrangements of tax avoidance and they do not give wide discretion to the tax authority. SAARs exist in many jurisdictions although their design and severity vary.[19] Ethiopia's tax law regime also incorporates SAARs to counteract specific avoidance practices such as transfer pricing, thin capitalization, and income splitting (Fenta 2023).[20]

[19] There are specific anti-tax avoidance laws in many countries, including ones targeting income splitting, transfer pricing, and thin capitalization; however, the rules vary in their design and severity.

[20] See for instance Federal Income Tax Proclamation 979/2016 (ITP) Art 78. For more, see Hailemariam Belay Fenta "Ethiopian income tax law tails in combating tax avoidance: A critical analysis from tax policy perspectives" (unpublished paper). I would like to take this opportunity to thank him for sharing his draft article and for his insightful inputs on the early version of this paper.

It should be noted, however, that even though SAARs provide precision and predictability, they cannot be used alone as a tool to effectively address tax avoidance (Mazur 2012, 560). Firstly, it is not feasible for legislators to enact specific rules to target all avoidance practices. Secondly, governments often adopt SAARs reactively, after identifying new avoidance practices, leaving taxpayers to unjustly benefit until the rules are adopted (Department of the Treasury 1999, XIII).[21] Thirdly, SAARs often become ineffective over time as taxpayers' resort to new strategies to circumvent the anti-avoidance rules or to leverage them to their advantage (Mazur 2012, 561). Considering these factors, the SAARs are often regarded as insufficient in combating all avoidance practices, leading countries to adopt GAAR to combat avoidance practices that fall outside the scope of the SAARs. The concept of GAAR is hard to define in a way that everyone agrees on, but it can be summed up as a mechanism of last resort that tax authorities can employ to stamp out tax avoidance practices that would otherwise align with the literal meaning of tax provisions. It empowers a country's revenue authority to deny tax benefits to transactions or arrangements that lack any genuine commercial purpose and only aim to get a tax benefit (Ostwal and Vijayaraghavan 2010, 63; Waerzeggers and Hillier 2016, 7). Many countries, including Australia, Belgium, Canada, UK, China, France, Germany, Italy, Kenya, the Netherlands, Singapore, and South Africa, have implemented statutory GAAR as anti-abuse measures (Waerzeggers and Hillier 2016, 7).

Ethiopia has also incorporated GAAR into its various tax laws, including its VAT Proclamation,[22] Excise Tax Proclamation (ETP)[23] and TAP.[24] The Ethiopian GAAR shares features with the GAARs of other countries and includes many of the attributes

[21] Meaning, the fact that governments typically adopt anti-avoidance rules only after they become aware of a new avoidance practice makes this approach reactive in nature, which permits taxpayers to benefit from a specific scheme until governments recognize and implement measures to address it (Department of the Treasury 1999, XIII).

[22] Value Added Tax Proclamation (VAT) 285 (2002) Art 60.

[23] ETP Art.41.

[24] TAP Arts.2(33) & 110.

common to all GAARs. It defines a tax avoidance arrangement or a “scheme” for the purposes of the GAAR when three conditions are met (Fenta 2023). To begin, a “scheme” must exist; although definitions vary slightly across laws, it is most commonly defined as “any agreement, arrangement, promise, or undertaking, whether expressed or implied, enforceable by legal proceeding or not, or any plan, proposal, course of action, or course of conduct.”[25] The second requirement is that the taxpayer must receive a tax benefit from the scheme.[26] For this purpose, a tax benefit is broadly defined as the reduction or postponement of a person’s tax liability, or any other avoidance of a person’s tax liability.27 Finally, the scheme should have been undertaken solely or primarily for the purpose of obtaining a tax benefit.28 Most importantly, like other modern GAARs, Ethiopia GAAR includes powers of reconstruction that allow the Ethiopian Revenues and Customs Authority to deny in whole or in part the tax benefit where a scheme or arrangement was entered into solely or dominantly for the purpose of avoiding taxes or obtaining tax benefits (Fenta 2023).29 Pursuant to Article 110 of the TAP, tax avoidance practices will also result in a penalty equal to twice the amount of tax that could have been avoided but for the anti-avoidance provision. Considering these attributes, one can assert that the legislative framework in Ethiopia, which aims to address avoidance practices, is praiseworthy. Nevertheless, what remains inadequate is its implementation.

Tax Evasion

Tax evasion refers to intentionally breaking the law to avoid or reduce taxes, which is a crime as it, unlike tax avoidance, violates both the letter and the spirit of the law (Elffers, Weigel and Hessing 1987, 333). There are two main theories that shed light on taxpayers’

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[25] ITP Art.80(4)(a-b). VAT Proclmation Art. 60(1). ETP Art.41(4)(a)).

[26] ITP Art. 80(1)(C). VAT Proclamation Art.60(2)(a). ETP Art.41(1)(b).

[27] ITP Art. 80(4)(b).VAT Proclamation. Art.60 (1) (a-c). ETP Art.41(4)(b). The ETP provides additional indications regarding what tax benefits are. ETP Art 41(5).

[28] ITP Art. 80(1)(c). VAT Proclamation Art.60(2)(b). ETP Art.41(1)(c).

[29] See ITP Art. 80(2); VAT Proclamation Art.60(2); ETP Art.41(1)(c).

compliance or non-compliance with their tax obligations: the deterrence theory (economic deterrence theory) and the behavioral theory (Alem and Tewabe 2022, 273). The deterrence theory of taxation holds that taxpayers prefer not to pay taxes and are deterred from doing so solely by the risk of being audited, detected, and penalized (Allingham and Sandmo 1972). It claims that increasing the likelihood of detection as well as the size of the fine reduces tax evasion (Tajuddin and Muhammad 2019, 318). The behavioral theory of tax compliance argues, however, that taxpayers' decisions on whether to pay taxes cannot be explained solely by expected economic benefits and costs. Their decisions are influenced by different psychological, sociological, and demographic factors (Feld and Frey 2007, 5; Alem and Tewabe 2022, 273). For instance, taxpayers may pay taxes, believing they will get public services in return (Alem and Tewabe 2022, 273). Further, the existence of service and client relations between taxpayers and tax authorities (rather than a cops and robbers' approach) boosts tax compliance by fostering trust (Feld and Frey 2007, 5). Taxpayers may also pay taxes dutifully because of adherence to their personal norm (Doran 2009, 131-132) and perceptions of procedural justice by tax officials (Feld and Frey 2007, 5). Further still, according to proponents of the behavioral theory, incentives also play a key role in enhancing tax compliance behavior (Feld and Frey 2007, 5).

Ethiopia's tax system adopts both theories of tax compliance. To begin, the Ethiopian tax laws, specifically the TAP, include concepts aligned with the behavioral theory.[30] Firstly, the TAP requires tax officers to bear obligations such as treating taxpayers with courtesy and respect, enforcing the tax law honestly and fairly,[31] and avoiding conflict of interest situations while exercising their power and function.[32] These obligations aim to promote good governance and fairness in tax administration, as well as strengthen trust and loyalty between a taxpayer and the government with a view

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[30] TAP Arts 5-8, 21-29, 135 & 49-51

[31] TAP Art 6 (2).

[32] TAP Art 6 (3).

to boosting taxpayer morale (Feld and Frey 2007, 5). Second, the Proclamation requires taxpayers to file a tax declaration and a self-assessment declaration;[33] these actions are intended to foster a bond of trust between the tax authorities and taxpayers, thereby building tax morale in society. Thirdly, the Proclamation offers incentives to taxpayers who consistently fulfill their tax obligations.[34] This approach promotes a positive behavioral norm of tax compliance. Fourth, the Proclamation offers tax relief for taxpayers experiencing severe hardship.[35] This relief scheme is expected to help create a service-client relationship between the government and taxpayers. Furthermore, the Proclamation deals about other issues that help promote a service-client relationship between taxpayers and authorities, such as credit for tax payments,[36] refund of overpaid tax,[37] and confidentiality of tax information.[38]

The Ethiopian tax law regimes also embrace the ideals of deterrence theory, by incorporating administrative, civil, and criminal liabilities against disobedient taxpayers, such as fine, and imprisonment. Regarding criminal liability, the TAP unifies most of the tax offenses that were previously scattered across different tax laws into one single law and provides punishments ranging from fines to the loss of liberty. One of the tax offenses recognized by the Proclamation is tax evasion, which involves activities like concealing income, not filing a tax declaration, or missing the tax deadline, all with the

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33 TAP Arts 21&25.

34 TAP Art.135(1). It is important to note that the TAP does not mandate the publication of lists highlighting taxpayers with exceptional compliance. Instead, it focuses on the publication of criminal tax prosecutions (TAP Art. 133). It was argued that the requirement to publish convictions ignores the negative effects of such publicity on building tax morale (Alem and Tewabe 2022).

35 Art. 51(1)(a)). The relief will be granted when the Ministry of Finance believes payment of the full amount of taxes owed by a taxpayer will cause severe hardships to that taxpayer because of natural causes, supervenient calamities or catastrophes, or personal hardships that are not caused by negligence or any failure on the taxpayer's part. The Proclamation also provides that the ministry of Finance may make concessions if the full payment of the deceased's tax debt would result in serious hardship for his or her dependents.

36 TAP Art 49.

37 TAP Art 50.

38 TAP Art 8.

intention of evading tax responsibilities.[39] Those who violate these prohibitions may face penalties of up to 200,000 Ethiopian Birr and imprisonment for a maximum of five years.[40] The TAP also specifies various civil liabilities that can be imposed on taxpayers individually or in combination with other types of liabilities, including payments intended to recover costs.41 Moreover, the Proclamation provide for the imposition of administrative liabilities against tax not-compliance behavior. The penalties are to be imposed in the form of a "fixed amount penalty" and a "percentage-based penalty."In summary, Ethiopia has laws in place that address tax evasion and avoidance practices. The next two sections analyze their practical implementation.

Unveiling Tax Collection Performance in Ethiopia: Exploring Tax Avoidance and Evasion Scheme, and Their Impact on Financing Esc Rights

Tax-to-GDP Ratio

Ethiopia's revenue from tax has shown nominal progress over time, as discussed in the introductory section. However, the tax-to-GDP ratio remains low and continues to decline. From available data spanning fiscal years between 2001/02 and 2020/21, Ethiopia's tax-to-GDP ratio reached its peak of 12.7 percent in 2013/14 and 2014/15

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[39] TAP Art 125.

[40] TAP Art.125. Also, withholding agents who, with the intent to evade, withhold tax but fail to pay it to the tax authority by the due date may face sentences of three to five years in prison (TAP Art. 125(2)). Besides the principal offender, the TAP proclamation also extends criminal liability to those who aid, abet, counsel, or procure a taxpayer to commit fraud resulting in a tax shortfall or to evade taxation (Art. 128). Also, the Proclamation creates a secondary liability for auditors or accountants when the taxpayer commits fraud or evasion (Art. 48). The TAP and other specific tax legislations have also provisions that sanction different tax related offences including the misuse of a tax identification number, making a false or misleading statement or provides fraudulent documents, obstruction of administration of tax laws and unauthorized tax collection (TAP Arts. 117, 118, 126 & 127). Moreover, the TAP requires the publication of taxpayer names convicted of tax-related crimes as a deterrent mechanism.

[41] TAP Arts. 30(3), 2(39) & 31. Pursuant Art 30(3) of the TAP, taxpayers are required to pay not only the unpaid balance of taxes, but also all charges incurred by the tax administration authority in taking action to recover the unpaid tax

fiscal years, while the lowest ratio of 9.0 percent was recorded in 2020/21 (Harris and Seid 2021, 49).[42]

Table 1: Tax-to-GDP ratios, 2001/02-2020/21[43]

Fiscal year	Tax-to-GDP ratio	year	Tax-to-GDP ratio
2001/02	11.9%	2011/12	11.5
2002/03	11.2%	2012/13	12.4
2003/04	12.6%	2013/14	12.7
2004/05	11.6%	2014/15	12.7
2005/06	10.8%	2015/16	12.1
2006/07	10.1%	2016/17	11.5
2007/08	9.6%	2017/18	10.7%
2008/09	8.6%/	2018/19	10.0
2009/10	11.3	2019/20	9.2
2010/11	11.4	2020/21	9.0

The statistics indicate a consistently low tax-to-GDP ratio trend. In the past two decades, except for four fiscal years, the ratio has been below 12 percent. The highest peak was observed in the fiscal years 2013/14 and 2014/15 when the ratio reached 12.7 percent. However, even this figure fell short of the target of achieving a tax-to-GDP ratio of 15 percent by 2015, as set out in the country's GTP I (33), 17.2 percent by 2020 in the country's GTP II (108), and nowhere near the targeted 18.2 percent under the current 2021-2030 A Path to Prosperity plan (32). Moreover, it was not even possible to sustain the 12.7 percent ratio, as evidenced by the downward trend observed for the last seven fiscal years. Further still, the Country's tax-to-GDP ratio consistently falls below the Africa average. For

[42] In the fiscal year 2020/21, the tax to GDP contribution hit its lowest point in the last two decades, scoring just 9.0 percent.

[43] The paper uses data from IMF on the tax-to-GDP ratio for the fiscal years 2001/02 through 2009/10, which is derived from USAID "EGAT/EG:Leadership in PFM Project" (2013) https://pdf.usaid.gov/pdf_docs/PA00JD81.pdf > (Accessed 23 May 2023). The data for the fiscal years 2010/11 through 2016/17 was derived from the Ministry of Finance's 2012 FY GoE Federal Budget Summary Volume One. <https://www.mofed.gov.et/media/filer_public/7e/b1/7eb14567-ac14-4b52-acf4-424b76817e9b/2012_fy_goe_federal_budget_summary_volume_one_main_document.doc>. The data for the fiscal years 2017/18 and 2018/19 was drived from the Ministry of Finance Ethiopia "የኢትዮጵያ ፌዴራላዊ ዲሞክራሲያዊ ሪፑብሊክ የ2015 በጀት ዓመት የተደገፈ በጀት" (2014) 5-6 (Accessed 9 February 2024).

instance, in the last seven years (2015-2023), the average tax-to-GDP ratio of African countries, calculated using data from 25-30 countries in different years, has been consistently between 15 percent and 17 percent (OECD ATAF, and AUC 2019; 2023). The low ratio in Ethiopia is attributable among other reasons to high prevalence of tax avoidance and evasion (Abdu and Adem 2023, 10; Kibret and Mamuye 2016, 5; Spanjers and Foss 2015, 6).[44]

Ethiopian Tax Avoidance and Evasion Scheme and ESC Rights

There is a considerable disparity between budgeted and collected tax revenues in Ethiopia. The underlying reason for this disparity is attributed to several factors, including non-compliance behavior of taxpayers. This behavior is evident in the widespread prevalence of tax evasion and avoidance practices in the country (Ayele 2019, 54). It is widely held that the level of tax compliance among businesses is exceptionally low, thereby harming the tax-to-GDP ratio (Gemechu 2013, 116). The informal sector's prevalence, low tax morale, weak tax administration, and underdeveloped financial sectors are major contributors to tax evasion (Mengistu, Molla and Mascagni 2019, 7).[45]

The extent of Ethiopia's lost resource due to abusive tax practices is not comprehensively documented, but available figures highlight the alarming nature. It was revealed that the presence of the underground or shadow economy - economic activities that take

[44] The major factors are: the prevalence of tax avoidance and evasion, the presence of informal sectors, the complexity of the tax system and inefficiency of the tax authorities, corruption, political unrest, tax-motivated illicit financial flows (IFFs), substantial tax incentives such as tax holidays and other exemptions, and a low level of tax awareness. For instance, as per the 2016 World Bank's Public Expenditure Review, tax exemptions and incentives have cost as much as 4-5 percent of GDP per annum. And had it not been for the incentives, the revenue ratio-all else equal-near 16-17 percent of the GDP. Accordingly, the existence of a myriad of tax exemptions and incentives would have the potential and result in low effective tax revenue mobilizations.

[45] Taxpayers employ various strategies to avoid or evade taxes, including not declaring and under-reporting income, overstating business expenses and deductions, overstating or understating trading stock, and claiming personal expenses as business expenses to conceal the actual tax liability.

place "off the books," out of the view of tax collectors and government statisticians - contributes to a significant amount of money being lost. The shadow economy allows transactions to take place without taxation, resulting in a decrease in tax revenues. Though estimating the size of the shadow economy is difficult, primarily because people involved in underground economic activities try to avoid detection, the estimated figures in Ethiopia indicate that it is very large. A study conducted by Emerta Asaminew Aragie in 2010 (using currency or money demand approach) revealed that Ethiopia's underground economy accounted for about 35.9 percent of the official economy from 1971 through 2008, reaching the highest levels of 51.8 percent and 51.4 percent in 1979 and 1985, respectively (2010, 16-20). In another study conducted eight years later in 2018, Gebeyehu Dejene estimated that the informal economy had a 43.3 percent share between 1980 and 2016 (Dejene 2018, 45). In his findings, he indicated that the informal economy reached its highest level in 2012, with 54.54 percent, and its lowest point in 2013, with 30.94 percent (Dejene 2018, 45). The World Economics 2021 report has also confirmed the high prevalence of the informal economy, stating that Ethiopia's shadow economy represented 33.7 percent of GDP ($106 billion at GDP PPP levels) (World Economics 2023).

While the size of informal economy cannot accurately reflect the extent of tax evasion arising from underground activities (Sam 2010), as some of the income generated by underground activities is exempt from taxation due to equity and/or political considerations,[46] it is undeniable that the shadow economy relates to tax fraud and avoidance. Using data from Ethiopia, Emerta Asaminew Aragie found that there was a clear inverse relationship between the tax to GDP ratio and the underground economy (2010, 21). According to his estimation, Ethiopia is losing around 10 percent of its GDP in tax evasion (2010, 21). It was also noted that "the shadow economy is also an economy where people hide their actual and taxable

[46] For instance, if a small business fails to properly record its output with the relevant authority and is consequently categorized as part of the informal economy, it may still be exempt from taxation, even if it is registered, provided its annual incomes remain below the tax threshold.

revenue from businesses and other lawful ventures to avoid paying taxes" (Mu, Fentaw and Zhang 2023, 3). The shadow economy thus keeps state revenues lower than what they otherwise would be, and in turn reduces the ability of governments to provide services and goods to their citizens (Schneider and Enste 2002, 11). Tax revenue lost because of unrecorded economic activity would have been used to construct schools, to provide health care services, to provide water, etc.

The shadow economy and tax evasion practices feed off each other as well (Schneider and Enste 2002, 11). If a government does not collect sufficient revenue to finance public services, such as as a result of the existence of a shadow economy, it may be forced to increase tax rates. In turn, this increase will promote a further flight into the shadow economy, worsening the budget constraints facing the public sector (thereby perpetuating the cycle). In Ethiopia, the introduction of several types of tax burdens in the early 2000s was associated with the subsequent growth of the informal sector, which rose from 23.4 percent in 2004 to 33.3 percent during 2007-2008 (Aragie 2010, 17). This illustrates the need for fiscal bodies to focus on improving the efficiency of the tax administration and expanding the tax base rather than imposing high tax rates that discourage taxpayers and force them into the underground economy. The country not only faces a loss of tax revenue in the informal sector but also significant challenges due to tax evasion and avoidance among registered taxpayers. Tax payers employ tactics such as underreporting income, inflating business expenses, and categorizing personal expenses as business-related to reduce their tax obligations. While comprehensive data on the extent of tax revenue lost due to domestic tax abuse by registered taxpayers is unavailable, government reports and research studies acknowledge the existence of this issue. For instance, on May 25, 2023, the Ministry of Revenue announced the recovery of 28.6 billion ETB through audits targeting 6,540 business organizations involved in fraudulent tax filings, tax evasion, and false bankruptcy claims (Demsew 2023). This finding highlights the gravity of the country's tax evasion and avoidance problems. With Addis Ababa alone having over 452,000 taxpayers (Tesfaye 2023), expanding audits to a larger number of taxpayers could potentially expose the severity of these issues. Notably, the recovered amount of 28.6 billion ETB exceeds the budget allocations for key sectors in the country's 2022/23 fiscal year. The budget for health is 19.3 billion ETB, urban development and construction is 18.5 billion ETB, agricultural and rural development is 18.5 billion ETB, justice and security is 17.0 billion ETB, and prevention and rehabilitation is 13.1 billion ETB (Cepheus Research and Analytics 2022, 8). This stark comparison highlights the significant impact of tax evasion and avoidance on the country's finances.

Ethiopia also faces significant losses of resources due to international corporate and private tax abuse. The State of Tax Justice 2020 reports reveal an annual loss of $379,569,403 to international tax abuse in Ethiopia, with $362,658,520 attributed to corporates and $16,910,883 to individuals (Tax Justice Network (TJN), Public Services International (PSI) and Global Alliance for Tax Justice (GA4TJ), 17). This loss of resources could have been utilized to finance the implementation of rights under the ICESCR. It was noted that the lost revenue due to international tax abuse accounts for 56.42 percent of the country's health budget or the equivalent of the annual salaries of 436,648 nurses (TJN, PSI, and GA4TJ 2020, 17). Comparing this loss to the Federal government's budget allocated for the education sector in 2022/23, which amounts to birr 64,763,384,204 (approximately $1.24 billion based on the average USD/birr exchange rate for 2022),[47] it represents approximately 30.48 percent of the education budget. This percentage signifies a huge portion of education funding that could have been allocated towards improving infrastructure, enhancing the quality of education, and investing in the future of the country's youth. This trend persists, as the 2021 report indicates a loss of $148.3 million to international tax abuse, $137.4 million due to corporate tax abuse, and $10.9 million due to individual tax evasion. (TJN, PSI and GA4TJ

[47] On average in 2022, 1 USD was worth 51.9425 ETB. See <https:/www.exchangerates. org. ukUSD-ETB-spot-exchange-rates-history-2022.html > (Accessed 23 May 2023).

2021, 21). According to the report, these lost resources would have been sufficient to fund the vaccination of 8,621,096 individuals (8.31 percent of the population) against COVID-19 (21). Furthermore, when compared to the country's annual health budget, the report shows that this loss stands for 22.26 percent (21). When considering the percentage of the lost amount of $148.3 million in comparison to the Federal budget allocation for food security and job creation in the 2022/23 fiscal year, which amounts to 19.0 billion ETB (United Nations Children's Fund (UNICEF), Ethiopia 2022, 2),[48] it becomes clear that the lost revenue represents around 40.55 percent. This emphasizes the magnitude of the loss and its impact on food security and job creation initiatives.

These abusive tax practices squander the country's available resources, which could otherwise be utilized to finance ESC rights, and have a negative impact on the redistributive role of taxation in curbing vertical and horizontal inequalities.[49]

Conclusion

[48] This amount was equivalent to approximately $365,739,118.61, based on the average USD/Birr exchange rate for 2022. On average in 2022, 1 USD was worth 51.9425 ETB. See <https://www.exchangerates.org.uk/USD-ETB-spot-exchange-rates-history-2022.html > (Accessed 23 May 2023).

[49] These abusive tax practices undermine the principle of equality and non-discrimination. Firstly, they significantly diminish the tax revenue collected by the government, and as a result the government's ability to finance social welfare programs, public services, and infrastructure development will be limited. The money that is siphoned away through these abusive tax practices could have been utilized to improve access to education, healthcare, housing, and other basic needs, reducing poverty and fostering a more equitable society. Tax evasion and avoidance practices also undermine the wealth redistribution role of taxation by increasing burden on honest taxpayers. Tax evasion and avoidance shift the tax burden onto honest taxpayers who cannot or do not engage in such practices. When individuals or businesses successfully evade taxes, it creates an imbalance where a smaller group shoulders a larger share of the tax burden. This can lead to increased economic inequality and hinder the effective redistribution of wealth. Furthermore, these abusive tax practices reinforce existing inequalities. Tax evasion and avoidance tend to benefit wealthier individuals and entities more than those with lower incomes. The ability to employ sophisticated strategies and utilize offshore accounts or tax shelters is typically more accessible to financially wealthy individuals and entities. By evading or avoiding taxes, they can accumulate and retain wealth, exacerbating income inequality and undermining efforts to redistribute resources more equitably. (Taylor 2006, 14; (Zucman 2015, 108).

Taxation policies and human rights are closely intertwined, as taxation generates resource to comply with human rights obligations, promoting equality, and ensuring accountability. While human rights instruments including ICESCR do not prescribe specific tax policies, they incorporate principles that limit the discretion of states in adopting and implementing fiscal policies, including taxation. The duty of member states under the ICESCR to use maximum available resources necessitates measures against tax abuse practices. The principle of equality and non-discrimination also compels states to combat practices that perpetuate discrimination, such as tax evasion and avoidance. Especially, developing countries like Ethiopia, facing resource challenges, are required by the ICESCR to establish and enforce robust laws targeting tax abuses. The paper notes that, when compared to similar laws in other jurisdictions, Ethiopian tax laws exhibit the minimum characteristics of effective anti-tax avoidance and evasion laws, but there is a lack of proper implementation. This inadequate enforcement contributes to Ethiopia's low tax-to-GDP ratio, which is below the African average.

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