

Registration for VAT: The Ethiopian Experience

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Abstract

Registration is one of the integral parts of the VAT system. According to article 7(1)(a) of the VAT proclamation registered persons are identified as the first groups of taxpayers. Even though registered person are identified as taxpayers they are not required to pay tax, rather they are only required to collect tax from their customers. The VAT proclamation has introduced two types of registration. Those taxpayers in the first group are duty bound to register and failure to registrar shall result in penalties. On the contrary in case of those taxpayers who fall in the second category they are not by law required to register for VAT but they are given an opportunity to apply for voluntary registration when they satisfy certain requirements.

Registration entails benefits and duties on the taxpayer. One of the main benefits of registration is the benefit of crediting. As provided in article 21 of the tax proclamation registered persons are given the right to claim tax credit for the taxes paid on their purchases. On the other hand registered persons are required to collect VAT from their customers, file a VAT return every month, keep books and accounts and issue VAT invoices to their customers during sale.

Key terms: Ethiopia, Tax, Sales Tax, VAT, Registered person, Voluntary registration, Obligatory registration, VAT invoices, deregistration, divisional registration.

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Registration for VAT

Registration is one the key element in the administration of VAT. Only those persons who are required to register or registered persons are identified as taxpayers or taxable persons as the case may be.¹ In any VAT system registration entails its own benefits and duties for the taxpayer. For instance only registered persons can collect VAT from their customers² in addition registered person are also required to comply with a host of requirements such as using VAT invoices³, the duty to keep books and accounts⁴ and the duty notify change of place of business.⁵ For all these obligations registered persons are rewarded with the benefit of tax crediting.⁶ Registered person for VAT are given the right to setoff their input taxes against the taxes that they collect from their customers.

Kinds of registration

In the design of the VAT system providing the threshold for which registration is required is one of the critical issues to be considered. Setting the threshold either too low or too high will have its own negative consequences.⁷ Having too low registration threshold will invite many taxpayers to register for VAT at the end creating considerable difficulty during administration especially in those tax system where tax compliance is

¹ It must be noted that a registered person even if identified by some legal system for instance ours as a taxpayers, they are not strictly speaking taxpayers as they are not required to pay Vat to government but only collect tax from their customers during supply of goods and rendition of services. In order to avoid confusion in some tax systems the registered person is identified as a taxable person.

² Value Added Tax Proclamation No. 285/2002, art.7(1)(a)

³ See art.22

⁴ See art.37. In addition as provided in article 18 of the income tax proclamation taxpayers with annual turnover more than 500,000 are required to keep books and accounts, since VAT registered person are mainly those person with a turnover more than 500,000, thus in addition to VAT proclamation the income tax laws as well require registered persons to keep books and accounts, See art.18-19 of the income tax regulation 79/2002.

⁵ See art.38

⁶ See art.21

⁷ Ehtisham Ahmad, Abdulrazak Al Faris(ed), Fiscal reforms in the Middle East: VAT in the Gulf Cooperation Council(2010)198

too low and the tax administration is insufficiently developed.⁸ Indeed, in both Ghana and Malta an initially low threshold was one of the primary reasons for the failure of their first VAT. On the other hand, when the registration threshold is too high only very few taxpayers shall be required to register for VAT collecting very low tax for the public treasury, therefore, when the threshold is set for registration it must be considered these two issues. Therefore the threshold must be an amount that can reasonably be managed and at the same time collect enough revenue for the public treasury. The Ethiopian VAT proclamation has provided for two kinds of registration each having its own threshold. In the next section a brief discussion of each kind of registration shall be made.

Obligatory registration

Obligatory registration is the first type of registration. In this type of registration, the trader is duty bound to register and failure to register results in different kinds of penalties.

Traders shall be duty bound to register, if at the end of the year their annual turnover is 500,000 (five hundred thousand) or more.⁹ Alternatively, if at the beginning of the year there are reasonable grounds to expect that the total value of taxable transactions to be made by the person during that period will exceed 500,000 the person is required to register without waiting till the end of the year.¹⁰ For instance, if at the beginning of the year the person imports a good worth 450,000 it is reasonable to assume that at the end of the year the person's transactions would exceed 500,000, therefore, in this situation the person is required to register.

In determining the registration threshold the tax authority in case of related person may add the value of total transactions by each person's when the transactions for both

⁸ The International Tax dialogue , Background Paper Prepared for the International Tax Dialogue Conference on the VAT Rome, March 15–16, 2005 available at www.itdweb.org accessed on January 12, 2012

⁹ See VAT proclamation art.16(1)

¹⁰ Id.

persons is below the threshold and may ask each related person to individually registered for VAT.¹¹ This provision closes the door that can be used by taxpayers in order to evade VAT registrations by splitting their transactions between two or smaller businesses which may at the end of the day serve the same goal.

In addition to those persons provided in article 16 of the proclamation directive 25/2001 has provided list of persons who are obliged to register for VAT, these persons include:¹²

- ✓ Traders engaged in sale of gold
- ✓ Engaged in electronics business sale of refrigerator, TV and the like
- ✓ Importers
- ✓ Engaged in plastic business
- ✓ Shoe factories
- ✓ Contractors from level 1-9
- ✓ Traders engaged in sale of computers and computer accessories
- ✓ Traders engaged in sale and preparation of leather products

Persons who are required to register for VAT are required to collect tax from their customers whenever they provide goods or render services to their customers unless the goods are exempted.¹³ Therefore, when a person who is required to register for VAT fails to register for VAT his actions will result in loss of revenue to the government. As a result the proclamation has provided serious administrative and criminal penalties for persons who ignore the rules regarding registration. Accordingly, a person who fails to register for VAT when there is a duty to do so shall pay administrative penalties.¹⁴ Accordingly, the person shall pay 100% of the tax as a penalty in addition to the payment of the tax.¹⁵

¹¹ Directive in order to govern the registration of VAT , Directive 25/2001, see art. 5.

¹² See art. 4(3) of directive 25/2001

¹³ See,art.7(1)(a) of the VAT proclamation

¹⁴ See art.45 (1) of the proc.

¹⁵Id.

A person required to register shall file an application for registration no later than the last day of the month after the end of the period during which the total taxable transactions value has exceeded 500,000 Birr or the last day of the month of the period in case of persons whose transactions at the beginning of the month is less than the threshold but are reasonable grounds to expect that the total value of taxable transactions to be made by the person will exceed 500,000 Birr.¹⁶

Voluntary registration

The other type of registration is a voluntary registration. A trader who is dealing with taxable transactions may apply for voluntary registration to the authority at his own initiative and when the Ethiopian Customs and revenue authority accepts his application, the taxpayer might be allowed to register.

The main reason for voluntary registration tax credits. As provided in article 21(1) of the proclamation, only registered persons are allowed to get tax credits for those taxes paid during purchase of raw materials or input taxes. Hence, taxpayers by registering voluntarily shall be entitled to get credits. And this is the main reason that would motivate traders to apply for voluntary registration.

There is a danger to the integrity of a tax system in allowing uncontrolled voluntary registration. First, this may allow those who are not in reality engaged in business to register with a view to claiming rebates of input tax when they have no real intention of paying much output tax to the government. In addition, a right to register voluntarily may have the effect of making many more persons than is administratively viable.¹⁷ Cognizant of these facts our law has provided for prerequisites that must be fulfilled in order to register voluntarily.

¹⁶ See art.16(3)

¹⁷ Supra note 8

The first requirement is that the person applying for voluntary registration must supply at least 75% of his goods or render the same percentage of his services to the registered person.¹⁸ Moreover, as provided in article 18(8) of the proclamation the Ethiopian Customs and revenue authority may deny registration if the authority has reasonable grounds to believe that the person will not keep proper records or will not submit regular and reliable tax returns as required under the proclamation. In addition as provided in article 18(8(a)) of the proclamation registration will also will be denied if the person does not have a permanent place of business or abode.

Registration procedure

A person applying to register for VAT is required to do so in such a form as is established by the implementation directives issued by the authority. When a person carrying out taxable transactions files an application to be registered for VAT, the Authority is required to register the person in the VAT register, and to issue a certificate of registration. The certificate to be issued by the authority will incorporate the following details¹⁹:

- the full name and other relevant details of the registered person;
- the date of issuance of the certificate;
- the date from which the registration takes effect; and
- the registered person's taxpayer identification number.

The Authority is required to establish and maintain a VAT register containing details of all persons registered for VAT.²⁰ If a person is required to register for VAT and has not applied to be registered, the Authority may register the person on its own initiative and send to the registered person the certificate.²¹

¹⁸See, art.17.

¹⁹ See, art.18(3)

²⁰ Id.

²¹ See, art.18(6)

Registration for VAT takes effect on the first day of the accounting period following the month in which the obligation to apply for registration arose in case of obligatory registration.²² For instance, if the obligation arose in September then the registration shall have an effect starting from the next accounting month i.e October. In case of persons, applying for voluntary registration the registration shall have an effect on the first day of the accounting period following the month in which the person applied for registration or it shall have an effect on the selected date by the registered person.²³

Divisional Registration

Divisional registration is a situation where a trader is allowed to have more than one VAT registration for businesses under his own name. One of the serious side effects of divisional registration is that at times some persons with sales above the threshold may avoid registration by splitting the business into two or more with sales below the threshold.²⁴

According to Ethiopian VAT laws unity of VAT registration is a mandatory requirement on the part of the taxpayers. As a result, even if a person runs two or more businesses a person can only have one VAT registration certificate. Nonetheless, under exceptional circumstances a person may apply for divisional registration of his business. A person might be allowed to have a separate VAT certificate for his business if the following conditions are fulfilled:²⁵

- The person must prove that single registration entails excessive tax administrative compliance costs.
- Each branch must engage in separate nature of business
- The branch must be located in an area far beyond 100 K from the main head office

²² See art.18(4)

²³ Id.

²⁴ Victor Thuronyi(ed), Tax law design and drafting, Volume 1(1996)176

²⁵ Directive 25/2001, see art.6

- Each branch must have its own independent accounting books and accounts and tax records.
- The nature of business handled by each branch must be different and must be known for their individual and at the same time different nature of business.

When we look at the grounds for allowing divisional registration we can see that divisional registration is allowed only under exceptional circumstances. The requirements are so strict that it would be difficult for businesses owned by a single person to have more than one VAT registration.

Cancellation of Registration

Registration for VAT will make taxpayer part and parcel of the VAT net. Taxpayers who do not want to be in the net for various reasons are given the right to be out of it by fulfilling certain requirements. The process of leaving the VAT net is generally known as cancellation of registration and deregistration.

Traders enter into the VAT system through registration, after registering traders may want to leave the VAT system due to various reasons. A person who wants leave the VAT system may apply for cancellation of his registration.²⁶

A person may request for cancellation of his VAT registration due to various reasons. The first reason for cancellation of registration is cessation of dealing with taxable transactions by the registered person. In this case the person is totally out of the market, thus there is no reason for him to maintain his VAT registration. Moreover registered persons may apply for cancellation of their registration if he shifts his business to exempt transactions. For instance a trader who used to deal with cars may shift to transportation business which is an exempt transaction. In this case the VAT certificate of the person shall be cancelled as he is not dealing with taxable transactions.²⁷

²⁶ Supra note 24 at 182

²⁷ See art. 8 of the VAT proclamation for the list of exempted items and transactions.

On the other hand, when a registered person's taxable transaction is below the statutory minimum the person can apply for cancellation of his registration. However, in order to successfully cancel his registration for three consecutive years the registered person's annual turnover must remain beyond the threshold. The rationale for such a requirement emanates from the very reason that naturally business would show rise and fall.

If a person's registration for VAT is canceled, the authority is required to remove the person's name and all other details from the VAT register and the person is required to return the issued certificate of registration. In addition when the registration of the person is cancelled for any reason goods at hand including his capital goods shall be considered to have been sold. Therefore the trader is required to transfer the same amount that could have been collected from his customers had the goods been sold to third parties. This provision aims at canceling the tax benefit in the form of credited VAT to those persons whose registration is now cancelled.

Main duties of taxpayers registered for VAT

Tax credit is one of the most important benefits of registration. This benefit however, entails some duties on the part of the taxpayer. Specifically registered persons are obliged to perform the following:

Issue tax invoices

One of the duties of persons for VAT is issuance of VAT invoices. Whenever a registered person makes a sale she is required to issue VAT invoices to customers. The proclamation has made it clear that a non-registered person cannot issue VAT invoices. According to the VAT laws the VAT invoice to be issued by the registered person must contain the following information:²⁸

²⁸ The Directive to provide for issuance and keeping of invoices , Directive No.28/2001, art.4, See also art.22 of the VAT proclamation.

- full name of the registered person and the purchaser, and the registered person's trade name, if different from the legal name,
- taxpayer identification number of the registered person and the purchaser,
- number and date of the VAT registration certificate;
- name of the goods shipped or services rendered;
- amount of the taxable transaction;
- amount of the excise on excisable goods;
- sum of the vat due on the given taxable transaction;
- the issue date of the VAT invoice, and
- Serial number of the VAT invoice.

The registered person is required to issue the VAT invoice to the purchaser of goods or services upon the supply or rendering, but not later than 5 days after the transaction.²⁹

Notification of Change

Registered persons are required to notify in writing any kind of change of name to the business, address of the business constitution or nature of the principal business within 21 days of the change occurring.³⁰ A registered person who fails to notify the Ethiopian Customs and revenue authority of the change as required in article 38 will pay the penalties provided in article 52 of the proclamation.

Record Keeping

The other relevant duty is the duty to keep records. The registered person is required to keep record of all the documents provided in article 37(1) of the proclamation at least for 10 years. A registered person or any other person liable for tax is required to maintain

²⁹ See art.38 of the VAT proclamation.

³⁰ Ibid, art.

books and accounts for ten years in Ethiopia. The accounts that must be kept by the taxpayer must include the following documents:³¹

- Original tax invoices received by the person,
- A copy of all tax invoices issued by the person,
- Customs documentation relating to imports and exports by the person,
- Accounting records

Failure to maintain books and records as required by law results in payment of an administrative penalty as provided in 45(d) of the proclamation.

Filing of VAT Return

A registered person for VAT is required to declare his activities for every accounting period. Accounting period for VAT purpose is a one month period.³² Thus registered persons are required to file a VAT return indicating their total output, input tax, goods and services taxed at a zero rate and exempted transactions for that particular month. The declaration has to be made in a form prescribed by the tax authority. The declaration of the activities or filing of the return must be done no later than the last day of the calendar month. Declaration of income must be done though the persons' tax liability for that particular month is nil or zero.

Collection of VAT

By far the most important duty on the part of the taxpayers is the duty to collect taxes from their customers. Accordingly registered persons are required to collect VAT from their customers whenever they provide goods or render services to their customers unless

³¹ See art. 37 of the proclamation. According to Ethiopian income tax laws, traders are classified into three categories based on their annual turnover. Accordingly a person with annual turnover greater than 500,000 is considered as category A taxpayer. According to the same law category A taxpayers are required to keep books and accounts. (Arts 18-20 of Income Tax Regulation 78/2002)

³² See art. 2(1) of the VAT proclamation.

the goods are specifically provided as exempt transaction by the proclamation or the VAT regulation.³³

³³ See art.7 (1) of the VAT proclamation . Goods and services exempted from the VAT payment are provided in article 8(2) of the proclamation and articles 16-30 of the VAT regulation.

Conclusion

Registration is one of the central issues in the administration of VAT. The Ethiopian law has introduced two kinds of registration: obligatory and voluntary. Obligatory registration is mandatory registration and failure to register incurs penalties. On the other hand, voluntary registration gives an option to the trader to be part of the VAT system. However, as VAT requires complex book and account keeping, only those persons who are in a position to keep proper books and accounts are allowed to register. Voluntary registration must be regulated strictly; otherwise, it will create problems to the integrity of the tax system by allowing uncontrolled and unmanageable taxpayers into the system. In addition, the presence of uncontrolled and unregulated voluntary registration will make the presence of a registration threshold redundant. Regarding this matter, the proclamation has made it clear that only a trader with at least 75% of their transactions with registered persons may apply for voluntary registration.