

**COMPLEXITY OF NIGERIAN COMPANY INCOME TAX  
ACT (CITA 2007): READABILITY ASSESSMENT**

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**Complexity of Nigerian Company Income Tax ACT (CITA 2007): Readability  
Assessment**

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## **ABSTRACT**

Simplification of tax laws in terms of readability to aid easier and complete compliance by taxpayers is a key issue to achieving the objectives of every country's tax system. The connection between language and compliance is obvious and understanding of the laws is crucial for all stakeholders to be able to carry out their respective responsibilities (Tan & Tower, 1992). In particular, simple tax laws would reduce the burden of compliance costs. Under the self-assessment system (SAS) regime, the simplicity of the tax laws is very important as most responsibilities defined by the laws have been shifted to the taxpayers. Thus, complexity of the tax laws may be an obstacle to both the taxpayer and the SAS.

This study examines the readability of the Nigerian Company Income Tax Act 2007 (CITA 2007) and explores its association with compliance and administrative costs and SAS of taxation. The study employs readability formulae (Flesch Reading Ease Score and Flesch-Kincaid Grade Level), Average Sentence Length (ASL) and Percentage of Passive Voice (PPV) to determine the level of readability of the Act. Furthermore, this study adopts interview approach to triangulate the readability results obtained using the above formulae, and explores the association between the readability of the Act and compliance costs, administrative costs and SAS.

The study found that the CITA 2007 has low level of readability which made the Act very difficult to understand. The low level of readability is also found to be associated with increased compliance costs as well as administrative costs, which subsequently impair the progress of the SAS in Nigeria.

The study recommends that tax simplification policy in Nigeria should include language simplification in order to reduce compliance costs and administrative costs. With this tax simplification effort, it is hoped that tax compliance under the SAS can be improved and more tax revenue can be generated.

**Key Words:** Complexity of tax law, readability, compliance cost, administrative cost and self-assessment system.

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## LIST OF ABBREVIATIONS

ASL	Average Sentence Length
CITA:	Company Income Tax Act
FIRS:	Federal Inland Revenue Service
FRES:	Flesch Reading Ease Score
F-KGL:	Flesch-Kincaid Grade Level
ITA:	Income Tax Act
PPV:	Percentage of Passive Voice
SAS:	Self-Assessment System

## **CHAPTER ONE**

### **INTRODUCTION**

#### **1.1 INTRODUCTION**

This chapter begins with an overview of the background of the study. In the later sections, the problem statement is highlighted, followed by the research questions. Based on the research questions, research objectives are formulated. This is followed by a discussion on the significance of the study. The chapter ends with the description of the scope and limitation of the study and organization of the project paper.

#### **1.2 BACKGROUND OF THE STUDY**

Taxation has a very important role in the development of a country. Taxation is becoming a most fundamental factor for economic development compared to other financing mechanisms, such as trade and aid. Taxation provides a stable flow of revenues to finance developmental priorities (Chipunza, 2010). In order to serve this vital role, a tax system should be efficient and effective. The two criteria of an effective tax system, as highlighted by Gale and Holtzblatt (2000) are: (i) simple to administer; and (ii) simple for taxpayers to comply. On the same note, Salami (2011) asserted that complexities in the tax system may lead to high tax corruption and evasion.

Omuigu (2011) emphasized that simplification of tax laws and tax processes to aid easier and complete compliance by taxpayers, is a key issue to achieving the objectives of Millennium Development Goals (MDGs) and Vision 2020 of Nigeria. It is important to note that these development plans (MDGs and Vision 2020) aim to place Nigeria in the league of developed countries. Therefore, reducing complexity of the tax laws is crucial

to such development plans. Having this in mind, the Nigerian government has significant responsibility to ensure that the tax legislations are simplified. This, in turn will enhance compliance among taxpayers and increase government revenue to enable more development expenditures.

Simple tax laws would reduce the burden of compliance costs. Under the self-assessment system (SAS) regime, the simplicity of the tax laws is very important, as most responsibilities defined by the law have been shifted to the taxpayers. Among the responsibilities shifted to taxpayers are to define (i) the taxable income; (ii) exempted income; and (iii) applicable tax rate. In order to be well-versed on their new responsibilities, taxpayers are expected to learn the laws. However, learning about the tax laws is a cost component to the taxpayers. Thus, complexity of the tax laws may become an obstacle to the taxpayer, as well as the tax authority under the SAS regime.

Gale and Holtzblatt (2000) opined that the level of complexity may be the most common complaint about SAS. They argued that the complexity of the tax system has, to a certain extent, increased compliance costs incurred by the taxpayers. They continued that tax complexity has many dimensions and could plausibly be defined in different ways. Slemrod (1984) defined complexity from the perspectives of compliance costs and administrative costs. Compliance costs include the time taxpayers spend in preparing and filing tax forms, learning about the tax laws, and maintaining record-keeping for tax purposes. The costs also include the amount spent (in time and money) by taxpayers to (i) avoid or evade taxes; (ii) have their taxes prepared by others; (iii) respond to audits; and (iv) pay any costs imposed on any third-party, such as employers. Administrative costs, although incurred by the government, are ultimately borne by the taxpayers. These costs

would include the budget of the tax collection agency, and the tax-related budgets of other agencies that help administer tax programs. Thus, from the perspectives of compliance costs and administrative costs, the system is said to be complex, if these costs are high (Slemrod, 1984).

Saw and Sawyer (2010) and Smith and Richardson (1999), on the other hand, viewed complexity from the dimension of level of readability of tax laws and other tax materials, such as tax instructions, tax schedules, etc. This dimension of tax complexity is concerned with the reading complexity, i.e., how simple are these materials to be read and understood by the taxpayer. In other words, it involves the easiness by which tax laws and the other materials can be read and understood. In addition to this, presentation of the content and style of the tax legislation also plays an important role in reading complexity (Koch & Karlinsky, 1984). Therefore, this project paper focuses on the readability level of tax legislations.

Several indices have been used in the accounting research to measure readability level of financial reports (Clatworthy & Jones, 2001; Li, 2006; Linsley & Lawrence, 2007), as well as tax laws and related materials (Smith & Richardson, 1999; Richardson & Smith, 2002; Saw & Sawyer, 2010 and Urbancic & Hsu, 2007). These indices include Flesch Reading Ease Score (FRES) and Flesch Kincaid Grade Level (F-KGL). According to Cooper (1993), clarity of expression has been one of the important issues identified by tax commentators when they talk about complexity or simplicity of the tax system. Therefore, readability in terms of understanding and fluency, is a crucial factor to be considered when attempting to improve or simplify tax laws.

This study is important as simplicity of the tax laws can reduce both compliance costs and administrative costs, and enhance compliance, especially under the SAS. As noted by Tan and Tower (1992), the connection between language and compliance is obvious, and understanding of the law is crucial for all stakeholders to be able to carry out their respective responsibilities. Tan and Tower (1992) further asserted that simplification of the tax laws in terms of language is always overshadowed by other policies considered to be more important by the government. However, this area has now become of major concern to many taxpayers. The simplification, in this regard, may help Nigeria to achieve the Vision 2020 and MDGs. Also, this effort can help to improve the Nigerian tax system from the current ranking of 138<sup>th</sup> in terms of Ease of Paying Taxes Index,<sup>1</sup> and in turn, increase tax revenue to finance government activities.

While observing every single tax legislation in Nigeria would be useful, this study only focuses on the readability level of the Nigerian CITA 2007. The selection of this tax legislation is consistent with the objectives of Federal Inland Revenue Service (FIRS) to increase non-oil tax collection, as well as compliance via the SAS. It is hoped that the results of this study would assist FIRS towards improving the current CITA 2007 or rewriting the Act, if necessary.

### **1.3 PROBLEM STATEMENT**

Saw and Sawyer (2010) and Smith and Richardson (1999) viewed tax complexity from the dimension of readability of the tax laws. They further argued that readability, with emphasis on comprehension and fluency, is an important factor to consider when

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<sup>1</sup>According to World Bank's Doing Business 2012 Report, Nigeria was ranked 138<sup>th</sup> on the ease of paying taxes out of 183 countries surveyed. Maldives and Venezuela were ranked first and last respectively in the report.

attempting to simplify tax laws. In their conceptual study on the challenges affecting the proper implementation of a good tax system and proper strategies for an efficient tax regime in Nigeria, Micah, Ebere and Umobong (2012) identified tax laws in Nigeria as being complex and difficult for the taxpayer to comprehend, and in some cases problematic, even for literate officials. Consequently, many taxpayers are unaware of the existence of certain taxes. This is an unfortunate scenario, considering that taxpayers should be able to understand all their obligations under the tax laws, especially in the case of the SAS. Consequently, this study attempts to empirically determine the asserted level of the complexity. Prior to that, Tukur (2010) also opined that Nigeria has not achieved the expected voluntary compliance even though the SAS has been in place since 1991. He identified the ambiguity of the tax laws as one of the reasons for the poor performance. Thus, if taxpayers do not understand what their obligations are, any intervention to enforce compliance will be perceived as unfair (Organization for Economic Cooperation and Development, 2004). Therefore, it is important to make taxpayers' obligations clear by making the tax laws and other tax materials easily understandable, simple and non-confusing.

Nigeria was ranked 138<sup>th</sup> in terms of ease of paying taxes, out of the 183 countries surveyed (The World Bank & International Finance Corporation, 2012). The survey further indicated that a medium size company in Nigeria spent, on average, about 26 weeks in a year dealing with its tax affairs. In the same vein, on average, Sub-Saharan Africa and countries in the Organization for Economic Cooperation and Development (OECD) have a tax compliance time of 318 hours and 186 hours respectively. In

comparison, it therefore takes 938 hours for tax compliance in Nigeria (Asabor, 2012).<sup>2</sup> Such a long period consumed may lead to high compliance costs incurred by corporate taxpayers. Undeniably, one possible reason for such a problem is the complexity of the tax laws (Richardson & Smith, 2002). Therefore, the tax laws should be simple and understandable to both taxpayers and the tax authority. If this simplification of the tax system is achieved, the administration and payment of the taxes would be much easier; businesses would be encouraged to register and pay their taxes; which eventually will facilitate the development of the country.

A complex tax system puts unequal pressure on smaller businesses (Lopez, 2012). Small business taxpayers under the regular system of taxation are discriminated, since the compliance requirements and cost of compliance are the same for both small and large enterprises. Reducing the compliance costs would increase the small enterprises' profit margin. This, will in turn, result in an increase in the amount of tax paid to the Government. This is consistent with Vasak's (2008) findings that the simplified tax laws for a micro-enterprise historically have reduced the size of the shadow economy and the number of non-complying registered taxpayers.

Most of the studies on readability of the tax laws were carried out in the developed nations such as Australia, New Zealand and the US (Tan & Tower, 1992, Smith & Richardson, 1999; Richardson & Smith, 2002; Saw & Sawyer, 2010 and Urbancic & Hsu, 2007). Therefore, it is important to carry out such a study in a developing country,

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<sup>2</sup> The report considered ease of paying tax to involve both the cost of taxes that are borne by corporate taxpayers and the tax authorities.

such as Nigeria, in order to determine the readability level of tax legislations in the developing world.

#### **1.4 RESEARCH QUESTIONS**

Based on the literature reviewed, this study aims to answer three questions as follows:

1. What is the level of readability of Company Income Tax Act 2007?
2. How does the level of readability of Company Income Tax Act 2007 associate with tax compliance costs in Nigeria?
3. How does the level of readability of Company Income Tax Act 2007 associate with the self-assessment system?

#### **1.5 RESEARCH OBJECTIVES**

Based on the foregoing research questions, this study is set with the following objectives:

1. To assess the level of readability of CITA 2007.
2. To explore the association between the level of readability of CITA 2007 with tax compliance costs in Nigeria.
3. To explore the association between the level of readability of CITA 2007 with the SAS in Nigeria.

#### **1.6 SIGNIFICANCE OF THE STUDY**

While not all taxpayers would read the primary tax laws, they may form their impressions based on their advisors' reactions to the law. If the taxpayers' perceive that the law is simple, this may reduce their frustration, and possibly increase compliance (Karlinsky & Koch, 1987; Koch & Karlinsky, 1984). In turn, increased comprehensibility could lead to more efficient tax returns preparation and lower cost of compliance. Also, on the side of



the tax authority, this might lower government audit costs or bring about more efficiently allocated resources, because an understandable law could lead to fewer filing errors and disputes (Martindale, Koch, & Karlinsky, 1992).

Therefore, this study sets out to assess the level of readability of CITA 2007 towards enhancing tax compliance and progress of the SAS in Nigeria. By studying readability of tax laws, the result of this study would contribute to the existing literature on tax complexity in particular, and taxation in general. It will also serve as a source of reference for future studies. Additionally, the result of this study would help the tax authority to improve the readability of the current CITA 2007 towards increasing tax compliance, especially under the SAS. In turn, this will help in achieving the objective of the current government to increase non-oil tax revenue.

### **1.7 SCOPE AND LIMITATIONS OF THE STUDY**

Complexity of taxation has been viewed from different dimensions. One of such dimensions is level of readability. Therefore, this study focuses on the level of readability of CITA 2007. The study further explores the association between the level of readability and compliance cost as well as administrative cost, and the SAS in Nigeria. As argued by Richardson and Smith (2002), improving readability is an important way of reducing both compliance cost and administrative costs of taxation.

This study employs four measures of readability, namely: FRES, F-KGL, Average Sentence Length (ASL) and Percentage of Passive Voice (PPV), in order to achieve the first objective of the study. The researcher also conducted interviews with three officers of the Nigerian tax authority (FIRS) from the unit of company income tax and three tax

professionals in Nigeria in order to triangulate the result of the readability indices and achieve the last two objectives of the study.

This study is not without limitations. First, is the use of readability formulae which have been identified with shortcomings, such as simple count of number of words and syllables and not taking into account important factors, such as semantics, presentation of materials, and conceptual difficulty, motivation, and experienced reader characteristics. In order to tackle these shortcomings, interviews were conducted to triangulate the findings. Second, is the use of tax professionals as proxy for taxpayers. While some argue that it is more appropriate to interview taxpayers rather than tax professionals, it is important to note that taxpayers rarely read tax laws and they form their views on tax complexity based on the inputs from tax consultants (Karlinsky & Koch, 1987). In fact, previous studies also used tax professionals (Karlinsky & Koch, 1987) and students (Koch & Karlinsky, 1984) to investigate tax law reading complexity. On the same note, James and Wallschutzky (1997), in criticizing the tax law redrafting projects, argued that taxpayers rarely read the tax legislation, and for that reason, it is not logical to direct redrafting at them. Rather, it should be directed to the professionals, who in turn, can explain the effect of the legislation to the taxpayer (James & Wallschutzky, 1997). Based on this argument, it is considered adequate to include the tax agents as representatives of the taxpayers.<sup>3</sup> Third, is the limited number of interviewees involved which may limit the generalization of the results of this study.

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<sup>3</sup>Given the time constraints and financial commitments, this study finds it impossible to have the responses of the corporate taxpayers. However, most of the required responses have been obtained from the tax agents. In addition, interviewing these tax agents and the tax authority officers are considered appropriate considering that they always deal with the tax laws and the taxpayers.

## **1.8 ORGANIZATION OF THE PROJECT PAPER**

This study is organized into five chapters. In Chapter One, the background, the problem statement, the research questions, the objectives, significance, the scope, and the limitations of the study are discussed. Chapter Two reviews the previous theoretical and empirical studies on tax complexity, giving emphasis to the dimension of readability complexity. The chapter also reviews literature on tax compliance cost and the SAS. The methodology and the source of data used are described in Chapter Three. The results and interpretation of the findings of the quantitative method are discussed in Chapter Four. Chapter Five provides the analysis of the interview responses. Finally, Chapter Six provides the conclusion, policy implication and suggestions for future research.

## CHAPTER TWO

### LITERATURE REVIEW

#### 2.1 INTRODUCTION

This chapter reviews relevant literature in order to develop a good theoretical and conceptual framework. It begins with discussion on background of CITA 2007. The chapter covers literature regarding corporate compliance costs and the SAS of taxation, in relation to tax law complexity. The chapter further reviews literature on tax complexity, giving emphasis to the readability dimension, which is the focus of this study.

#### 2.2 BACKGROUND OF THE NIGERIAN TAX LAWS

Taxation is as old as humans, and has had different shapes since primitive societies. It could have been in the form of tribute payment or compulsory service to the society. In the olden Nigeria (before amalgamation of the four different groups to become Nigeria as it is today), the leaders (Emirs, Obas, Ezes etc.) of various kingdoms, ethnic groups and tribes imposed taxation on their subjects<sup>4</sup>. However, the origin of initial legal backing to taxation in Nigeria dates back to the period of colonialism, when Sir Fredrick Lugard introduced the Native Revenue Proclamation of 1904 in Northern Nigeria, before the amalgamation that formed Nigeria as one country.<sup>5</sup> In 1917 and 1928, the proclamation was implemented in the Western region and Eastern region respectively as Native Revenue Ordinance<sup>6</sup>. One of the major amendments was the incorporation of the Direct Taxation Ordinance No. 4 of 1940<sup>7</sup>. Since then, different governments continued to

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<sup>4</sup> Institute of Chartered Accountants of Nigeria Study Pack, p. 5

<sup>5</sup> Ibid

<sup>6</sup> Ibid.

<sup>7</sup> The Native Revenue Ordinance of 1917, 1918 and 1928 were all incorporated into the Direct Taxation Ordinance No. 4 of 1940 Cap 54

reform the tax laws. Therefore, it is clear that Nigerian tax law is a legacy of the British tax law of 1948. The tax laws were later expanded to reflect current economic conditions. This led to tax laws concerning personal incomes, company incomes, petroleum incomes, etc.

According to Kiabel and Nwokkah (2009) and Abiola and Asiwah (2012), currently, there are eight major tax laws regulating tax collection in Nigeria:

1. Personal Income Tax Act (PITA) CAP P8 Law of Federations of Nigeria (LFN) 2004
2. Company Income Tax ACT (CITA) CAP.60. LFN 1990
3. Petroleum Profit Tax Act (PPTA) 2007
4. Value Added Tax (VAT) Act No 102 LFN 1993
5. Capital Gains Tax Act CAP 42 LFN 1990
6. Stamp Duties Act CAP 411 LFN 1990
7. Education Tax Act No 7 LFN 1993
8. Information Technology Development Act 2007

Of the eight legislations above, this study focuses on CITA 2007 because of the following reasons: (i) CITA 2007 has the highest revenue proportion of non-oil tax revenue compared to other non-oil taxes as shown in Table 2.1. Company income tax contributed the highest proportion of 44.29% compared to other major non-oil sources; (ii) All corporate taxpayers, which include companies under CITA 2007, incur high compliance costs in Nigeria, resulting from the long duration spent on dealing with their

tax affairs (WB & IFC, 2012); and (iii) the SAS is also applicable to company income tax in Nigeria, as with other countries.

**Table 2.1**  
**Non-oil Tax Revenue 2011**

<b>Tax</b>	<b>N' billion</b>	<b>%</b>
<b>Company Income Tax</b>	<b>663.02</b>	<b>44.29</b>
Capital Gains Tax	0.77	0.05
Value-Added Tax	659.15	44.03
Education Tax	130.74	8.73
Personal Income Tax	43.47	2.90
<b>Total</b>		<b>100</b>

Source: CBN Annual Reports 2011

### **2.3 NIGERIAN COMPANY INCOME TAX LAW**

The first company tax law was established in Nigeria when the Companies Income Tax Ordinance was enacted in 1939. This Ordinance was promulgated into Income Tax Ordinance in 1940 to take care of taxation of both companies and individuals. This joint income tax law continued until 1961, when the CITA 2007 was introduced. The Act was re-enacted in 1979 and re-enacted again in 1990. Currently, the Act is codified as the Companies Income Tax Act of 2004 (CITA 2007 CAP C21 2004 LFN), amended in 2007.

CITA 2007 subjects the profit or gain of any company accruing in, derived from, brought into, earned in or received in Nigeria, to be assessable to tax. The company income tax rate for the year 2013 is 30%, and it is applicable on the total profit or chargeable profit

of the company. It is worth noting that Oil Marketing Companies, and Oil Services Companies are also liable to tax under CITA 2007<sup>8</sup>.

Administration of CITA 2007 is the responsibility of the Federal Board of Inland Revenue whose operational arm is FIRS<sup>9</sup>. The FIRS is responsible for the assessment, collection and accounting, for all amounts collected as company income tax<sup>10</sup>. Given the huge contribution of company income tax to economic development, it is imperative to consider reducing the complexity of CITA 2007, which has been criticized for being complex and difficult to understand, even for tax officials (Micah et al., 2012). One way of doing this is by revising the level of readability of the tax legislation, which is the focus of this study.

#### **2.4 COMPLIANCE COSTS OF TAXATION AND TAX COMPLEXITY**

The inherent difficulty in understanding tax legislation led to increased tax compliance costs as well as tax administration costs for the taxpayers and tax administrators, respectively (Richardson & Smith, 2002). Compliance costs involve all expenses incurred by taxpayers to comply with tax regulations, which include the time, and expenses incurred to maintain proper records, undertake tax planning, file necessary reports, and compute the required remittances (Vaillancourt, 1989). In other words, these include, in some cases, the fees paid to tax professionals, such as accountants and lawyers, as well as costs incurred by businesses in collecting, managing, and remitting taxes paid by employees to the government, the costs of paying the businesses own taxes, and in providing tax-related information to the government. In all cases, tax compliance

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<sup>8</sup> See Company Income Tax Act CAP. 60 L.F.N 1990 Act CAP. C 21 L.F.N 2004: Section 9

<sup>9</sup> Ibid: Section 1

<sup>10</sup> Ibid, Section: Section 3

involves commitment of resources from the side of the taxpayer for the purpose of paying tax.

Administrative costs are all costs incurred by the tax authority in collecting taxes and enforcing the tax regulations, which include collecting, administering, and managing the tax collection procedures (Vaillancourt, 1989). In Nigeria, this includes all costs incurred by the FIRS, various State Tax Authorities(SIRS), as well as the various Joint Tax Boards, in administering and managing the tax system in the country.

In order to achieve an optimal tax system, the compliance costs incurred by taxpayers when complying with tax laws and other tax regulations should be kept to minimum levels possible. Similarly, the administrative costs involved by the tax authority should also be minimized. This is particularly important as in the final analysis, both costs are to be borne by the taxpayers. Some authors categorized compliance costs into internal and external compliance costs (Slemrod & Blumenthal, 1992; Slemrod & Blumenthal, 1996 and Chan, Cheung, & Ariff, 1999). The internal compliance costs comprise all staff costs of compliance tasks that are incurred internally and other supplementary costs for tax compliance purposes. External compliance costs comprise costs incurred for hiring the services of tax experts from outside the organization. Compliance cost is an important cost factor in business operations. In fact, compliance cost may be an economic burden that decreases the business size (OECD, 2001), and this could have a negative impact on a business. To this end, Evans (2003) opined that compliance cost should be considered as an important factor when designing tax laws. Looking at the impact on the general economy, compliance cost is an opportunity cost which could have been reinvested by the businesses to support economic growth.



The growing complexity of tax systems, the introduction of Value Added Tax/Goods and Services Tax (VAT/GST) legislative regimes which are associated with high compliance costs, and the increased emphasis placed on self-compliance, has led to increasing interest in tax compliance costs studies.

#### **2.4.1 Determination of Compliance Cost**

Recognition of the importance of compliance cost is an old issue. Adam Smith, in his renowned work, 'Canon of Taxation', emphasized the importance of compliance cost in the tax system (Smith, 1776 as cited in Evans, 2003). More recently, since the renowned study on compliance cost by Sandford (1973) and Slemrod and Sorum (1984) in the UK and the US respectively, several studies have been carried out in different countries on tax compliance costs, most of them in developed countries.

In the early stage of tax compliance cost studies, most of the studies focused on individual taxpayers. Later, research on business/company tax compliance costs were conducted in several countries. For instance, in Canada, Erard (1997) studied the compliance costs of large companies, in operating federal and local income taxes as well as capital taxes, using a survey method. The result of the study reported an average annual compliance cost of \$364,325<sup>11</sup> for the top 500 companies in Canada. This result was comparable with the compliance cost survey on big companies in the US, by Slemrod and Blumenthal (1996). In that study, it was reported that an average annual compliance cost of \$1.57 million was incurred by corporate taxpayers. This indicates

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<sup>11</sup> Converted to USD at the rate of 1.3724 CAD to USD and source of annual exchange rate- Pen World Table (2012)

high compliance cost in the US of more than four times that of Canada<sup>12</sup>. When elicited on the factors contributing towards high compliance costs (the Canadian study had the highest proportion (23%), many of them regarded the complexity of tax laws in the areas of recurrent tax law changes and interest deduction rules, as the main source of high compliance costs. Such complexity made it necessary for taxpayers to hire a tax expert, particularly when it involved answering queries and even litigation. All these mean additional costs for the taxpayers.

In Hong Kong, Chan et al. (1999) investigated the burden of tax compliance costs of listed companies for the 1995-1996 period of assessment. The result of the study showed average overall compliance cost of \$44,798<sup>13</sup>, which consisted of internal and external costs of \$13,427 (30%) and \$31,372 (70%) respectively<sup>14</sup>. It can be deduced from the result of the study that external compliance costs were very high, and computational components constituted the highest proportion of the external costs.

More recently in the US, Slemrod & Venkatesh (2002) studied the compliance costs of large and mid-size businesses, using a sample drawn from a population of 230,945 tax returns. Responses were collected from the taxpayers as well as the tax agents. Analysis from such respondents showed the amount of compliance costs incurred across industries totaled \$719,740, \$272,849, \$582,441, \$382,163, \$249,192 and \$640,353 for Communications, Technology & Media, Financial & Professional Services, Heavy Manufacturing & Transportation, Natural Resources & Construction, and Retail, Food

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<sup>12</sup> The authors claimed that one possible reason for high compliance cost could be due to large number of sample and average company size in the US compared to that of Canada.

<sup>13</sup> Converted to USD at the rate of 1.3724 CAD to USD and source of annual exchange rate- Pen World Table (2012)

<sup>14</sup> Converted to USD at the rate of 7.7343 HKD to USD and source of annual exchange rate- Pen World Table (2012)

&Healthcare, industries respectively. This meant a total compliance cost of \$2,846,738, with an average of \$254,451. In terms of the proportion, the results showed that 58.7% was related to internal costs, another 24.8% was external costs and the remaining 16.5% was incidental cost. Comparing this result with the previous US study by Slemrod and Blumenthal (1996), there was a much lower compliance cost in this study by six times. This may be as a result of some reforms that led to simplification of some aspects of the tax system.

In Australia, McKerchar (2007) studied the effect of tax complexity on taxpayers, tax practitioners and its consequences on the Australian Tax Office (ATO). The study used a mixed method design by selecting a large sample population randomly drawn from the ATO taxpayer database and a case study. The study found that complexity gave rise to unintentional non-compliance and intentional over-compliance. It seemed to be clearly unfair to the taxpayer, as it appeared to be favorable to the tax authority, in terms of revenue collections. The study further found that there was a direct relationship between the effect of complexity and compliance costs, and this in turn had an effect on taxpayers' commitment to compliance. In other words, an increase in complexity made it more difficult for the tax authority to take advantage of the high tax compliance. The result of the study also revealed that taxpayers (respondents) relied heavily on tax agents because they wanted an accurate return of income and they regarded the system as too complex for them to ever understand. Similarly, Lignier and Evans (2012) carried out a survey on the tax compliance costs on small businesses in Australia. The results of the study revealed that the average cost of complying with all taxes in the income tax year 2009/10

was around \$25,684<sup>15</sup>. The study indicated that most of the businesses (in the survey) had a perception that the tax concessions were too complex to understand and not worth the effort. Thus, complexity of the tax law and the structure of the tax system greatly affected the burden of tax compliance experienced by the businesses. Similarly, the survey report of Australian Small Business Deregulation Task Force (1996) indicated that small businesses faced a major problem with the tax system, in terms of complexity, uncertainty and interpretation of the law, among other issues, which increased the compliance burden. These businesses needed simplicity to lessen this burden and have more resources devoted to growing their businesses.

In Portugal, Lopez (2012) carried out a survey on 897 companies to determine the corporate compliance costs in Portugal and its determinants. The findings of the study revealed an average annual cost of \$30,492, consisting of 67% internal and 33% external cost, incurred as costs of tax compliance. Also, company size, complexity of the tax system and the market (local or cross-border) were the major determinants of corporate tax compliance costs in Portugal. Table 2.2 below shows that studying the tax law as a component of compliance costs takes a significant proportion in both total external and internal costs, that account for 12.1% and 8.1% respectively.

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<sup>15</sup> Converted to USD at the rate of 1.090 AUD to USD and source of annual exchange rate- Pen World Table (2012)

**Table 2.2****Portugal Corporate Tax Compliance Costs for the Fiscal Year of 2004 in USD**

<b>Cost Component</b>	<b>Internal</b>		<b>External</b>		<b>Total</b>	
	<b>Cost</b>	<b>%</b>	<b>Cost</b>	<b>%</b>	<b>Cost</b>	<b>%</b>
Appeals & Litigations	267.7	3.3	729.31	4.5	997.01	4.1
Tax Planning	446.17	5.5	1,766.54	10.9	2,212.72	9.1
Advance Payment	624.64	7.7	875.17	5.4	1,499.81	6.17
Preparation of Information	1,492.65	18.4	4,003.09	24.7	5,495.73	22.6
<b>Study of tax law</b>	<b>657.09</b>	<b>8.1</b>	<b>1,961.03</b>	<b>12.1</b>	<b>2,618.11</b>	<b>10.77</b>
Closure of Accounts	1,435.86	17.7	3,581.71	22.1	5,017.57	20.63
Archives Information	1,354.74	16.7	696.89	4.3	2,051.63	8.44
Preparation of Financial Information	1,135.71	14	1,328.96	8.2	2,464.67	10.14
Filing & Sending Tax Forms	697.65	8.6	1,264.13	7.8	1,961.78	8.07
<b>Total</b>	<b>8,112.21</b>	<b>100</b>	<b>16,206.82</b>	<b>100</b>	<b>24,319.04</b>	<b>100</b>

Source: Lopez (2012)

In the developing world as well, several studies were carried out to determine tax compliance costs, for e.g., in India, Croatia, Malaysia, etc. (Gupta, 2003; Blazic, 2004; Sapiei, 2010 respectively)<sup>16</sup>. In India, Gupta (2003) studied income tax compliance costs of Indian companies. The study further investigated the determinants of compliance costs in relation to company characteristics, sources of compliance costs and different compliance activities. The results of the study revealed that legal compliance costs which consisted of internal and external costs was on average 4.12% of profit. Comparing this result with other compliance costs in different countries, various results were obtained as follows: 4.6% to 4.9% in Canada<sup>17</sup>, 6.8% in Australia<sup>18</sup>, 1.5% in Hong Kong<sup>19</sup> and 26.9%

<sup>16</sup> Unlike the developed countries, tax authorities in developing nations are not compelled to show the compliance costs (Ariff & Pope, 2002).

<sup>17</sup> (Plamondon et al., 1998)

to 28% in the US<sup>20</sup>. The projected percentage of compliance costs for all Indian companies was 4.33% to 13.18% of profit. Another important finding in relation to this study was that the main reason for hiring tax experts was ambiguity and complexity of the tax law and regular changes in the law. The study further recommended simplification of tax law by improving tax law drafting and extending the scope of some provisions in the law, as a measure to reduce the complexity in the tax law.

In Croatia, Blazic (2004) also studied the compliance costs of companies' income tax for 2001/2002. The result of the study showed an average tax compliance cost of \$3,444 for the companies in Croatia and an aggregate of \$259 million, which was about 1.2% of GDP. Further, the findings indicated that the compliance costs were proportionally higher on small companies than the larger companies. In comparison to other compliance cost studies, one important difference between the Croatian study and the other studies was the use of interviews to gather relevant information.

In Malaysia, Sapiei (2010) studied the compliance costs and compliance behavior of Malaysian public listed companies (PLCs) based on the perceptions of external tax agents. The study carried out a survey using questionnaire on a sample of 200 external tax professionals drawn from the website of the Inland Revenue Board (IRB). Based on 49 usable questionnaires analyzed, the results showed an overall average external tax compliance cost of RM 28,153 for Malaysian PLCs. Moreover, the respondents were asked to point out areas where most of the PLCs had difficulties concerning tax compliance. Out of the five areas set out by the survey, understanding the income tax law

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<sup>18</sup> As cited in (Gupta 2003)

<sup>19</sup> As cited in(Gupta 2003)

<sup>20</sup> (Slemrod & Venkatesh, 2002)

was ranked 1<sup>st</sup> with 23.2%. In essence, the respondents suggested the need to simplify the tax law and estimation requirements, among other issues, as the measures to reduce the high compliance burden born by the PLCs. The study differed in methodology with most compliance cost studies, in that tried to estimate the compliance costs based on external tax professionals only. However, the study argued that most of the PLCs did not have in-house tax compliance unit; rather they relied on external professionals. It is therefore reasonable to estimate such costs from the perspective of external tax professionals.

By comparing the compliance costs studies in developing countries with those in the developed ones, the results of most of the studies in the developed world showed that most of the public corporations have higher compliance costs than their counterparts in the developing economies. The higher tax compliance costs in the developed world can be explained by the higher tax complexity (Hanefah, Ariff & Kasipillai, 2001). Evans (2003) provided a review of studies on compliance costs all over the world. He identified increased complexity as one of the reasons that triggered studies on compliance costs. He further emphasized that the result of such studies are highly significant, in case of company income tax, personal income tax and VAT/GST, either in absolute or relative terms. Generally, the compliance cost was 2% to 10% of the total tax revenue generated and 2.5% of GDP.

Generally, most of the corporate compliance cost studies found that there was a positive relationship between company size and tax compliance costs. However, the average cost per unit of size was lower for big companies. From the literature, the type of business activity, sector, country, and region can explain the variations in the tax compliance costs. Also, cross-border operations accounted for high tax compliance costs of some

companies in the US and Canada. In the same vein, some of the main conclusions in these studies include: (i) Tax compliance costs of companies are higher compared to tax administration costs; (ii) Tax compliance costs seem to be regressively neglecting the measure of company size used in the study; and (iii) Considering the sources of the tax compliance costs, internal costs take the higher proportion of the total tax compliance costs. For instance, in the US, Slemrod and Blumenthal (1996) showed that for big companies, internal costs account for 85%. Also, most of the studies pointed out that simplification of tax law and reducing tax compliance costs should be treated as a serious issue. Blumenthal and Slemrod (1996) argued for a compromise between simplicity and fairness. In all cases, high tax compliance costs related to tax complexity.

To this end, it is evident that tax compliance costs comprise a large proportion of tax costs and it is significantly high, either in absolute or relative terms to GDP or tax revenue. Therefore, tax compliance costs should receive important consideration in every tax policy for enhancing tax compliance. Although, tax compliance cost is an inevitable cost, it should however not be too high to discourage compliance.

## **2.5 SELF-ASSESSMENT SYSTEM OF TAXATION AND TAX COMPLEXITY**

Reforms and changes of tax legislation can affect the level of complexity of the tax system (Sapiei, 2010). The introduction of the SAS in Nigeria has shifted most of the tax authority's responsibilities (used to handle in the government's assessment system) to the taxpayers. This comes with increased responsibilities, linked to possibility of more tax audits and investigations. In turn, taxpayers may have to look for tax professionals and this will result in additional compliance costs for the taxpayer. As noted by Kasipillai (2007), with the introduction of the SAS, there is anticipation of hiring the services of



external tax experts, especially by the corporate taxpayers. In the same way, the complexity of the tax laws may create additional burden to the taxpayers as they are now responsible for understanding all the legal provisions related to their filing and their tax returns. This can also make it necessary for taxpayers to hire the services of professionals. As pointed out by Simon and Clinton, (2002), there was unintentional tax non-compliance which occurred innocently as a result of taxpayers' inability to meet all their tax obligations due to unawareness or misunderstanding of the provisions of the tax law. Therefore, simplicity of the tax law can help in achieving full compliance. This section discusses the introduction of the SAS, and the complexity issues faced by the corporate taxpayers as a result of the SAS in Nigeria and also in other countries.

### **2.5.1 Introduction of SAS in Nigeria**

SAS in Nigeria has its roots in the constitution of Nigeria. According to Section 24<sup>21</sup>, it is the responsibility upon every taxpayer to truthfully declare his taxable income to the appropriate tax authority and promptly pay his taxes. The SAS was legally introduced in 1991 and started operations one year later. It started with some groups of taxpayers, and in 1998, extended to all taxpayers.

In Nigeria, taxpayers under the SAS (who can be an individual or entity), are required to assess themselves and make the tax payment to the designated bank to receive the e-ticket. After receiving the e-ticket, they are expected to file self-assessment returns on the statutory date to the appropriate tax authority. The tax authority will then accept the returns as it is. Later, the authority would make a random check to ensure the correctness of return forms. Later on, these returns are subjected to risk assessment and audit. Late

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<sup>21</sup> Constitution of the Federal Republic of Nigeria, 1999

returns penalty is imposed for late filing. The tax authority issues administrative assessment when the taxpayers fail to file their returns or intentionally reduce liability. The reduced tax amount is imposed, together with interest for the period when the liability becomes due, based on the information obtained from taxpayers' records and/or a third party. There may be a fine for such failure.

More specifically, companies are required to file returns within six months after the accounting year ends; for newly incorporated companies, either within the six months after the first accounting year ends or within 18 months from the date of incorporation, whichever is earlier. There is a penalty of N25,000 (equivalent to \$158.93<sup>22</sup>) in the first month and N5,000 (equivalent to \$31.79<sup>23</sup>) for subsequent months for failure to file returns within the stipulated date. There is also a penalty of 10% (per annum) of the amount of tax payable and interest for the period when the tax becomes payable until it is paid, both payable with the unpaid amount. In 2011, the FIRS came up with new regulations that would guide the procedures of the SAS in Nigeria on a project-based system. When there is a change in the tax system, such as introduction of the SAS, the procedural issues and the compliance costs are of paramount importance to the taxpayers. Although the SAS was introduced with the objective of increasing voluntary tax compliance, it may come with a complexity that can affect taxpayers' voluntary intentions to pay taxes, and in turn, this can lead to reduced tax compliance.

Many countries introduced the SAS, with the main aims of reducing the administrative costs and maximizing the tax revenue (Muzainah, 2002). Introduction of the SAS in

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<sup>22</sup> Based on monthly average exchange rate of NGN157.30 to USD1 for January, 2013(Central Bank of Nigeria, 2013)

<sup>23</sup> Ibid.

Nigeria, came with new regulations, i.e., keeping more records, spending more time in learning the new tax laws, etc., for the taxpayer. In the same vein, Sapiei and Kasipillai (2013) emphasized the need for obtaining adequate knowledge, since the burden which used to be with the tax authority had now shifted to the corporate taxpayers with the introduction of the SAS. Under the SAS, it is assumed that the taxpayers have the required knowledge and ability to comply with provisions of the tax laws. Thus, taxpayers are indirectly compelled to learn and understand the tax rules and obligations. Sapiei and Kasipillai (2013) further supposed the anticipation of hiring external tax experts under the SAS. Also, external tax experts, given their better position in terms of expertise, may influence their clients' tax compliance behavior. Hanefah (2001) identified *initial irregular cost* as a cost imposed on the taxpayer by the implementation of the SAS. Therefore, there is expectation that the SAS may increase compliance costs for the taxpayer. As pointed out by Sandford (1999), an increase in compliance costs means increase in complexity.

### **2.5.2 Tax Compliance Costs under SAS**

The USA and Canada were among the first countries that introduced the SAS in the 1940s with the aim of reducing administrative costs and increasing compliance. Also, in the late 1940s, Japan, after the World War II, introduced the SAS to help in economic recovery. In the early stages, the system faced a problem of low compliance due to poor administration and lack of tax knowledge from the side of the taxpayers. In 1986, Australia implemented the SAS in order to increase tax compliance. In the UK, after four years of SAS experience, the Association of Certified Chartered Accountants (ACCA) revealed that 36% of its members had difficulty with the SAS and about 9% admitted that

the new system was still problematic (ACCA, 2002, as cited in Lai & Choong, 2009). This confirmed the fact that the system can bring more complexity which even the tax experts complained about. On the side of the taxpayer, this can mean increase in compliance costs by increased hours in the work of the tax agents as a result of the new system.

In the developing world, the SAS was initially introduced in Malaysia in 1998, and its implementation was in stages, starting with corporate taxpayers in 2001, businesses, partnerships and cooperatives in 2003, and salaried individuals in 2004 (Sapiei, 2010). The Malaysian SAS has been identified with problems of high non-compliance amounting to \$93.24 million in 2005. This was a result of non-filing of returns, false returns filings and other false declarations by the taxpayers<sup>24</sup>. Based on this, two questions can be raised, whether higher compliance costs are really associated with the SAS, and whether the increased compliance costs lead to non-compliance.

In response to the above questions, Mansor, Saad and Ibrahim (2004) carried out a study to find out whether the SAS is associated with higher compliance costs. Different cost components were measured to assess the change in compliance costs. From the side of the taxpayers, cost for learning the new tax law and cost of record-keeping showed an average of 10% increase each; cost for discussion with the tax agents and cost of paying taxes showed above 10% increase; and cost of preparing returns and cost of answering queries showed an average increase of less than 10%. For the tax agents, there was an average time increase of 31%, each, for time spent on complying with the new law, the time spent on learning the law and time spent on preparing returns; 30% for time spent on

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<sup>24</sup> Statistics as reported by Lai & Choong, 2009 as in Krishnamoorthy, 2006

discussion with taxpayers; and 10% for answering tax queries. This result confirmed that introduction of the SAS comes with the increment in compliance costs. Time spent in learning the new law and time spent on discussing with tax agents contributed the highest costs. As indicated by the survey results, about 96% of the companies engaged tax professionals for their tax activities. Thus, taxpayers engaged tax professionals because the SAS comes with increased tax audit and enforcement penalties. A similar result was obtained in Australia, where about 72% of the respondents engaged professionals for their tax returns preparation, which was 20% under the old system-authority assessment (Marshall, Smith & Amstrong, 1997). Also, in the US where the SAS has been existing for a long time, the engagement of the professionals was found to be 60% (Newberry et al., 1993 as cited in Muzainah et al., 2004). This is in line with several studies that expected increase of compliance costs as a result of employing more services of external tax experts (Kasipillai, 2007; Kasipillai & Hanefah, 2000; Sandford, 1990). Loh et al. (1997) as cited in Sapiei (2010), reported an average compliance cost of RM 68,836, in which external cost had a proportion of 72% for Malaysian PLCs. This was in the pre-SAS period. On the contrary, empirical results from the study by Sapiei (2010) showed a decrease in the compliance costs of PLCs under the Malaysian SAS estimated at RM 28,153. One can argue that Sapiei's study involved only external costs (without internal) as computational, planning and other cost components were considered to be from the perspective of external tax professionals.

In another study, similar to Muzainah et al. (2004), Lai & Choong, (2009) investigated the compliance complexity encountered by tax practitioners in dealing with their corporate clients. The survey administered 700 questionnaires to the tax practitioners, out of which

280 usable questionnaires were analyzed. Among other findings, the study reported that 69% of the respondents faced problems of interpretation of the laws, as well as public rulings issued by the tax authority. This study also confirmed the fact that the SAS comes with additional complexity in the form of increased compliance costs burden to the taxpayer.

### **2.5.3 SAS and Complexity of the Tax System**

In the SAS, simplicity in terms of understanding the requirements of the tax law is very important to the taxpayers as most responsibilities have been shifted to them. Eriksen and Fallan (1996) emphasized that tax law knowledge plays an important role in the tax compliance behavior. As pointed out by Silvani and Baer (1997), in designing a tax system, the tax authority should make the tax return system simple and easy for the taxpayers and in the taxpayers' perspective. Therefore, the issue of complexity is very important to the corporate taxpayers as they are more likely to hire the services of tax experts when complexity increases. In turn, this will mean more burden on the taxpayer in terms of compliance costs. However, tax authorities in some countries, such as Malaysia, have introduced electronic filings which may be more user-friendly and save costs in terms of printing, postage, transportation and time.

Although big businesses and corporate taxpayers engage tax professionals for their tax issues, they also need to have some basic understanding about the taxable and non-taxable income. The understanding on the basic requirements and obligations under the SAS is very important to enhance their compliance. About 80% of tax professionals (respondents in a survey) complained that they failed to file returns on time because their clients could not provide them with the relevant information needed for tax computations

(Lai & Choong, 2009). Therefore, simplicity of the tax law is important for taxpayers to understand the information they need to furnish their agents. Lai and Choong, pointed out that simplifying the tax laws under the SAS may enhance compliance. This is because the taxpayer will find it easy to understand and interpret the tax law so that he can be able to provide all information required for his returns filing. In turn, this may encourage the taxpayer to make truthful declaration of income and enhance correct computation.

## **2.6 COMPLEXITY OF TAX LAW**

Complexity of tax law is one of the main issues tax commentators discuss. Complexity adds more burden to the taxpayers, as well as the tax authority, in terms of compliance costs and administrative costs, respectively. Excessive complexity in the tax law may have negative effect on taxpayer's voluntary compliance especially in the era of the SAS (James, 2006).

Weaver (1948), in his seminal work on tax law complexity, identified two different types of tax law complexity, i.e., organized and disorganized complexity. Karlinsky and Koch (1983) identified content complexity and reading complexity as two factors that contributed to the tax law complexity. First, content complexity refers to the inherent difficulty in a given concept, for example, the concept of calculus is more difficult to understand than the concept of arithmetic. Second, reading complexity involves presentation of the concept under consideration, for instance, a story in long sentences and many passive voices is more difficult to read and understand than the one in short sentences and less passive voices. Concerning readability, it is generally agreed that from the tax literature, readability problem is among the determinants of tax complexity (Karlinsky & Koch, 1984). In the same vein, Morris and Qios (2011) considered

complicated computations, obscure language, different interpretations for the same term, regular changes, cross-references and unclear terms as the factors contributing to the complexity in the tax law. Complexity in the tax law does not happen on its own; it is a reflection of different phenomena, such as the changing business environment.

According to Cooper (1993), in the discussions of tax simplification, tax commentators refer to at least one of seven factors to indicate tax complexity. The factors are mentioned below:

- i. Predictability: This refers to simplicity, easiness and accuracy in understanding the rules and their scope by the taxpayers as well as their advisers, whenever it is necessary.
- ii. Proportionality: This involves the aim of a tax law in relation to how simple the solution provided by the laws is.
- iii. Consistency: This involves rules on similar issues. In this case, laws should be consistent without arbitrary distinctions.
- iv. Compliance: The tax laws are seen as simple when it is easy for the taxpayer to comply without incurring high compliance costs.
- v. Administration: The tax laws are seen to be simple when it is easy for the tax authority to administer the laws.
- vi. Co-ordination: This involves the consistency of the tax laws with other rules. Thus, the relationship of the tax laws with other rules should be appropriate and not complicated.



Expression: The laws are simple when all rules are clearly expressed.

It can be deduced from the above that complexity of tax laws is a multi-dimensional issue as it refers to different things. However, these can be summarized into three main areas, i.e., tax policy, tax compliance and language. In any case, it should be emphasized that the provisions of the law should be in a simple language for easy understanding to enhance compliance as well as administration of the tax laws. Moreover, these factors involve readability of the tax law, either directly or indirectly. This is because the factors have to do with clarity of the responsibilities of stakeholders as expressed in the laws.

## **2.7 READABILITY**

Readability describes the simplicity by which a text can be read and comprehended. In other words, simplicity in reading may enhance learning and understanding. The term 'readability' is sometimes used interchangeably with understandability. While some argue that readability may be used as a proxy for understandability, it is important to note that there is much more to tax laws being understandable than the extent to which they are readable. Hence, readability is a pre-conditional feature of understandability (Urbanicic & Hsu, 2007). For instance, the understandability needed of the reader may be influenced by his intelligence, education, environment, interest and reason for reading. Having said that, for a document to be readable and understandable, the kind and the number of ideas expressed, the vocabulary, style, format and typography, should be considered. In addition, matching the texts to reader's skills is also very important.

Considering the importance of text readability, numerous studies have been conducted to develop a measure for readability of text materials. At the initial stage, these studies tried to establish a measure that could help in matching students' levels of education to the

textbooks they used in various grades or classes. Over time, readability formulae are now used in various fields such as research, law, health care, journalism, insurance, and industry (DuBay, 2006).

### **2.7.1 Development of Readability Formulae**

According to DuBay (2006), Sherman's work of 1926 is one of the early outstanding studies that set a stage for research in readability. Sherman (1926) made a comparison between the writings in his period and those before him and found that the length of the sentences tend to be shortening over time. He used a statistical method and established that the sentence length reduced from 50 words per sentence to 23 words from pre-Elizabethan period to his period, respectively. The sentence length later fell to 20 words per sentence (DuBay, 2006). Sherman (1926) suggested that shorter sentences are easier to read and understand. Interestingly, he also found that the sentences became less abstract and simpler due to the influence of spoken English over the written one. This is particularly true when syntactic changes occur as a result of technological development (such as computer) and changes in the spoken English (from abstract words to words of real meaning).

In another study, Vogel and Washburne (1928) conducted an empirical study on the structural attributes of text in terms of word difficulty, prepositional phrases, sentence length and kinds of sentences. This study developed *the Winnetka formula* which determines the difficulty of text by grade levels. Although this formula does not provide a perfect match of grade level with the reading ability, it is better than subjective judgments (DuBay, 2006). As in the previous study, this study of Vogel and Washburne (1928) also emphasized sentence length and sentence type, including active and passive voices.

Later, in 1931, Waples and Tyler (1931) carried out a comprehensive study on the adult reading interest. Using the interview approach, the study gathered information on styles of texts that people want to read and the reasons for their refusal. It appeared that suitability and difficulty of the reading materials largely affected reading and their performance. It can be established from the results of the study that making the tax laws simple through language simplification can minimize the likelihood of the taxpayers facing difficulty in reading the material. Hence, this would reduce the dependency on the tax consultants, which in turn, will minimize compliance costs of the taxpayers.

In order to develop more literature in readability, Gray and Leary (1935) carried out a survey to determine the factors that make a text readable for an adult reader. The study focused on the difficulty of text in terms of words structure and sentence length, as these can be measured quantitatively. Based on the 1,690 adult readers surveyed, they found that number of words, prepositional phrases, and number of syllables in a word determined readability. The study also found that many factors affected readability, and these factors were grouped under the following headings: content, style, format, and features of organization of the document (how headings, paragraphs, Sections, chapters, are organized). The formula designed by Gray and Leary was also based on sentence and word length. This study and the previous ones paved the way for the development of the FRES and F-KGL.

### **2.7.2 Flesch Readability Ease Score (FRES)**

Flesch's (1948) study on readability developed a formula that determines the ease or difficulty of a text based on the number of syllables and the number of words in a sentence of a given text. The formula uses a range score of 1 to 100 to determine the

readability of a text. Lower scores indicate ‘difficult to read text’ while higher scores reflect an ‘easy to read text’. For instance, a score of 1 to 30 is considered very difficult while that of 60 and above is easy. Table 2.3 gives the details of the scores and their respective rankings.

**Table 2.3**  
**FRES Scores Description**

<b>Flesch Readability Scores</b>	<b>Description of level of Readability</b>
0.00 to 30.00	Very difficult
30.00 to 50.00	Difficult
50.00 to 60.00	Fairly difficult
60.00 to 70.00	Standard
70.00 to 80.00	Fairly easy
80.00 to 90.00	Easy
90.00 to 100.00	Very easy

Source: (Flesch, 1948)

The scores are calculated using the following formula:

$$\text{FRES} = 206.835 - (1.015 \times asl) - (84.6 \times asw)$$

Where:

- FRES is a point on a scale from zero (0) (most difficult) to hundred (100) (easiest), with 30 as very difficult and 70 as easy.
- *asl*- Average Sentence Length is the number of words divided by the number of sentences.
- *asw*- The average number of syllables per word is the number of syllables divided by the number of words.

FRES has been the most widely accepted readability measure in different fields compared to other readability measurements (Klare, 1997). The potential reason could be due to its flexibility. In addition, FRES is claimed as an easy to use and time saving formula

compared to the previous readability formulae (such as Gray-Leary and Lorge) which require reference to word list (DuBay, 2006).

FRES was first used in accounting in 1952 (Jones, 1997). According to Karlinsky and Koch (1983), the US tax authority used FRES to determine the readability of tax return forms and tax instruction booklets. In the area of academic research, FRES was also used to measure readability of tax instruction booklets (Karlinsky & Koch, 1983). Furthermore, several researchers have used this index to calculate readability of accounting, finance, management, marketing and business communication textbooks. F-KGL is another version of FRES that gives corresponding grade levels as FRES.

### **2.7.3 Flesch Kincaid Grade Level (F-KGL)**

F-KGL is a reformulation of FRES that tries to match a point on FRES scale (0-100) to education level (grade level). This will help in matching the determined readability level of CITA 2007 to the appropriate education level required to understand the Act. Table 2.4 shows the F-KGL scores and corresponding education level based on the Nigerian education system:

**Table 2.4**  
**F-KGL Readability Scores**

F-KGL Score	Equivalent Education Level
17	University graduate
16	Undergraduate level 4
15	Undergraduate level 3
14	Undergraduate level 2
13	Undergraduate level 1
12	Senior Secondary School 3
11	Senior Secondary School 2
10	Senior Secondary School 1
9	Junior Secondary School 3
8	Junior Secondary School 2
7	Junior Secondary School 1
6	Primary school leaver
5	Primary 5

Similar to FRES, F-KGL also calculates the readability of a given text based on the number of syllables per word and the number of words per sentence, as follows:

$$\text{F-KGL} = (0.39 \times \text{number of words/number of sentence}) + (1.8 \times \text{number of syllables/number of words}) - 15.59$$

#### **2.7.4 Average Sentence Length and Percentage of Passive Voice (ASL and PPV)**

In addition to FRES and F-KGL, ASL and PPV in a text are important determinants of complexity of a reading material. Although the length of the sentence is encompassed in FRES and F-KGL, it is important to consider both ASL and PPV separately in readability analysis (Smith & Richardson, 1999). For good readability score in a document, it is a normal practice to keep the number of words per sentence at minimum possible levels and proportion of passive voices. In order to achieve this, excessive use of long sentences and passive voices have to be avoided. Whenever a passive voice can be replaced with an active one, this should be done as long as the intended meaning remains in the text.

Similarly, long sentences should also be replaced with shorter ones as recommended by Strader and Fogliasso (1989), and Tan and Tower (1992), in their studies on complexity of the tax laws. Tan and Tower (1992) found that the use of shorter sentences could reduce the reading complexity of tax laws. Using active voices instead of passive ones makes a sentence clearer by identifying the subject. For instance, the sentence “A taxpayer must file a return.” is simpler and more straightforward than “A return must be filed” (Thuronyi, 1996).

According to Richardson & Smith (2002), a percentage of around 20 for passive voices is considered acceptable in the tax legislation. With regards to ASL, 20 words per sentence would be acceptable (DuBay, 2006). This contention was supported by James (2007), who claimed that short sentences, clear and simple definitions, modern design and appropriate headings, are all needed to help the readers. These can lead to high level of readability which can make tax legislations simple to understand. This simplification of tax laws to solve the problem of complexity in the tax laws, and the SAS in particular, could be done through rewriting the laws in plain English by taking into account the above mentioned criteria. This effort will surely bring improvement to the tax system of the country, as has been experienced in many countries (James & Wallschutzky, 1997).

## **2.8 TAX LAWS RE-WRITE PROJECTS**

While some academicians and professionals support the rewrite program, others may have arguments against it for various reasons. For instance, various commentators in the UK have the opinion that the problems of tax laws complexity need a solution of wider reform and that rewrite project alone cannot solve the problem of complexity. According

to James and Wallschutzky (1997), rewrite is nothing but a reproduction of the existing tax laws. He continued that this is illogical act as no change has been made after accomplishing the re-write. In the UK, the rewrite project has achieved success, but the problem of complexity has not been solved (Gammie, 2008). Other commentators argued that simplification comes at a significant political cost, and that grander plans for simplification would be impractical.

On another note, James and Wallschutzky (1997), argued that it is illogical to direct the tax law rewrite on taxpayers as taxpayers rarely read the tax laws. According to Richardson and Smith (2002), this opinion disagreed with the studies that indicated it is necessary for the tax authority to establish good relationship with taxpayers. Better relationship can be achieved by making the laws easy for compliance and reduced compliance costs. Tax compliance cost is very important in any plan to simplify tax laws, and in particular, the rewrite of tax laws, in order to reduce the compliance burden faced by individuals, as well as corporate taxpayers. This suggests that simplicity, by improving readability of the tax laws, is important as a means of reducing business taxpayers' compliance costs. The tax laws should be precluded from old and abstract words and style. They should be redrafted in ordinary terms, with expressions of common life and short sentences that can be easily understood. Regardless of the debate, some of the countries have successfully undergone the rewrite project such as New Zealand, Australia, and the UK.

### **2.8.1 New-Zealand**

In New-Zealand, the re-write project started in 1990 following the discussion of the rewrite of Income Tax Act (ITA) 1976 and Inland Revenue Department Act (IRDA)



1974 by several reports and papers (Saw & Sawyer, 2010). A committee<sup>25</sup> was set up by the government with the objective of simplification of the tax system. One of the major recommendations of the committee was the need to re-write the tax laws in simple and plain language, which can be easily understood by an ordinary taxpayer (Richardson & Sawyer, 1998 and Saw & Sawyer, 2010). Reading and understanding are considered as aspects of compliance and therefore improving them will enhance tax compliance.

The main drivers of the redraft project were the Organizational Review and Valabh Committee, better known as the Organizational Review of Inland Revenue and Consultative Committee on the Taxation of Income from Capital, respectively. Based on the recommendations of the Valabh Committee, a working party was set up to manage the redrafting project. The working party of the re-write project had the aim of minimizing complexity by re-writing the laws in order to increase readability and understanding of the tax laws (James et al, 2007; and Saw & Sawyer, 2010).

According to Sawyer (2013), the New-Zealand re-write project was divided into four: (i) reorganization into new statutes, namely ITA 1994, Tax Administration Act 1994 (TAA) and Taxation Review Authorities Act 1994 (TRAA). This re-write was done in order to have simple structure in the ITA as provisions dealing with Timing Receipts and Expenditure, each grouped together in separate parts (Prebble, 2000); (ii) the re-writing of the essential provisions; (iii) the re-writing of the major income deductions and timing provisions; and (iv) the final drafting and enacting the ITA 2007. The rewrite of the ITA was accomplished in 2007 and enacted in 2008. After the rewrite project, Saw & Sawyer (2010) investigated the readability of New Zealand ITA and other relevant materials to

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<sup>25</sup> Waugh Committee

assess its success. The study used FRES, F-KGL, ASL and PPV to achieve its objective. The results showed an average FRES of 48.6 with average ASL of 25 words per sentence. This indicated that the laws are now easier to read and understand. For Tax Instruction Booklet (TIB) and Binding Rulings (BR), the FRES index was 36.4 and 32.4, respectively.

Prior to 2010, Tan and Tower (1992) had already conducted an empirical study to test the tax laws in New Zealand. The study used FRES to measure the readability of the ITA 1976, the Goods & Services Tax Act 1985 (GSTA 1985), the Technical Information Bulletins (TIBs) and the Tax Returns Guides (TRG), to determine the readability of such materials. The study used selected samples of Sections from ITA and GSTA before and after the simplification program to enable comparison. The readability of the two Acts was also compared to that of the TIBs and the TRG. The results revealed a Flesch score of less than 30 for both Acts, before and after the simplification. Furthermore, ITA showed an ASL of 141.60 words and 135.22 for the old and the new respectively. Similarly, GSTA showed average words per sentence of 125.69 and 128.11 for the old and new respectively. Also, there was excessive use of passive voice with a range of 35 to 55%. These results indicated that the Acts are still very difficult to read and understand by many taxpayers. Similarly, the TIBs got an average FRES of 40 and ASL of 23.45 words. Finally, the TRG showed an impressive result of Flesch score of 65, ASL of 15 and PPV of 16.29. All the results for the Tax Return Guide were within the acceptable range. Comparing the results obtained by Tan and Tower (1992), and Saw and Sawyer (2010), it is clearly indicated that New Zealand's effort to redraft the tax laws has achieved a reasonable level of success (Sawyer, 2013).

### **2.8.2 Australia**

The Tax Law Improvement Project (TLIP) and Tax Law Improvement (TLI) Team were established in 1993, following the recommendations of the Joint Public Accounts Committee (JPAC), with the main objectives of: (i) simplification of the tax laws; and (ii) reducing tax compliance and administrative costs by rewriting the tax laws into simple and easy to understand tax laws. In line with the objectives of the rewrite project in New Zealand, the TLIP aimed to achieve this objective through the use of plain English, and shorter, clearer sentences (Richardson & Smith, 2002). This became an important issue as compliance cost was estimated to be the highest in the OECD countries- 12% of tax revenue in the country.

The rewrite project aimed at simplifying the tax laws to an understandable level of individuals with ten years of schooling, i.e., a person without university or post-secondary education. In 1996, the first phase of the project, which was the rewritten version of the major provisions covering Assessable Income, Exempted Income, Deductions and Trading Inventory, was tabled in Parliament. The second phase, together with the first one, made up Income Tax Assessment Act (ITAA)1997 and the third one made up the Tax Law Improvement Bill 1998 (Smith & Richardson, 1999).

Following the rewrite project, Smith & Richardson, (1999) conducted an empirical study to investigate the success of the simplification of the ITAA 1936, as amended. The study used readability formulae to measure the readability level of the ITAA 1997 and ITAA 1936 in order to compare and assess the change in readability level after the rewrite project. The study utilized the FRES, F-KGL, ASL and PPV on sampled Sections of ITAA 1936 and the corresponding Sections of the new version- ITAA 1997. In addition,

the study included a sample from other relevant tax materials, such as the recent Taxation Rulings and Taxation Determinations and the Australian Individual Taxation Returns Guide. A sample of 95 Sections from ITAA 1997 and the Sections from ITAA 1936 were analyzed. The study found that based on the samples, ITAA 1997 was more readable than the ITAA 1936. However, the FRES for both laws was found to be below the required readability level benchmark of 60% to 70%. The same results were found for Taxation Rulings and Taxation Determinations. While, for the Tax packs, the result was found to be interesting with high readability level which was within the benchmark score. The results for F-KGL Index for both laws– ITAA 1997 and ITAA 1936, were disappointing. The results indicated that ITAA 1997 is still difficult to understand. The use of passive sentence increased in ITAA 1997 but not to an extreme level. Considering the ASL, there was an improvement with reduction in the words per sentence.

Later, Richardson and Smith (2002) studied the readability of the Australian GST law using an empirical method. The study used large sample of Sections (58.2%, i.e., 205 Sections out of 385) selected from the Australian GSTA . FRES, F-KGL, PPV and ASL were used to assess the readability level of the Act. The results revealed an average FRES of 40.3, which was below the required benchmark of 60 to 70. This means that the ACT is still obscure and complicated. The results also showed that more than 70% of the GSTA required at least university level of education to understand the Act. For the F-KGL, similar results were obtained. An average F-KGL of 11.0 was obtained for the whole sample. This also indicates low level of readability of the Act. For the PPV and sentence length, an average of 20% and 20.9 words per sentence, respectively, were

obtained. To sum up, the Australian GSTA is still difficult for the taxpayers to read and understand.

### **2.8.3 The United Kingdom**

In 1996, the Chancellor of the Exchequer approved the rewrite project of UK tax laws following the report of the Inland Revenue - “The Path to Tax Simplification”- published in the previous year. The report recommended the rewrite of the primary direct tax laws in a simpler and more readable language, with the aim of enhancing voluntary compliance and reducing the compliance costs (Sawyer, 2010). Sawyer further explained the rewrite process as removing difficult words, changing archaic sentences with modern ones, regrouping similar rules, splitting provisions, improving lay out and shortening long sentences.

For that purpose, two committees were set up, i.e., the Steering Committee and the Standing Consultative Committee. The Steering Committee was responsible for ensuring that the project was on the right track by providing strategic advice and taking into account the private sector concerns. The Standing Consultative Committee, on the other hand, was responsible for ensuring regular consultations with the private sector interests.

The rewrite project initially had a target of five years to finish the project, but later realized it was impossible to complete the project in five years. The project accomplished the rewriting of Capital Allowance Act (CCA) 2001; Income Tax Act - Earnings and Pension- (ITEPA) 2003; Income Tax Regulation (Pay as-You-Earn) (ITR) 2003; Income Tax Act (Trading and Other Income)2005 (ITTOIA); Income Tax Act 2007 (ITA) 2007 and Corporation Tax Act (CTA) 2009. Capital Gains Tax, Corporation Tax, Income Tax

and Inheritance Tax which were covered by the Tax Law Rewrite Acts (Amendment) Order 2013 were tabled in Parliament on the 5<sup>th</sup> of March, 2013 (Tax Law Rewrite Acts, 2013).

#### **2.8.4 The United States**

In the US, there has been a debate on simplification of tax laws as the laws have been identified as ambiguous. However, no serious action has been taken to re-write the tax laws. Notwithstanding that, Urbancic and Hsu (2007) studied the readability of tax instruction materials (of income tax) of the Western states in the USA. The study tested the readability of such materials for 16 years (1990 to 2005) to make comparison between the states. The study utilized FRES and Fog Index. The readability levels were determined relative to the level of adult education attainment of the states. The result of the study showed an average FRES of 53 for the states which was a score outside the threshold. Among the eleven states, Illinois had the most favorable Fog index followed by Wisconsin and Michigan with 12.4, 13.4 and 14.1, respectively. Nebraska had the worst result of 17.1.

#### **2.8.5 African Continent**

In 2009, South Africa also announced its intention to re-write income tax laws. However, no progress has been updated so far. Coming down to Nigeria, to the best of the researcher's knowledge, no simplification program has been undertaken. Similarly, there is no empirical study that examined the readability of the Nigerian tax legislations. However, Micah et al., (2012), in their conceptual paper, identified Nigerian tax laws as complex and difficult to understand for both taxpayers and tax officials. Thus, based on the above literature, this study hypothesizes that:

H<sub>1</sub>: Nigerian Company Income Tax Act (CITA 2007) has low-level readability.

## **CHAPTER THREE**

### **METHODOLOGY**

#### **3.1 INTRODUCTION**

This chapter explains the research method used in order to achieve the objectives of the study. The chapter begins with the justification of the adoption of readability measures and the relevant procedures. In the second part, sample selection and the procedure for the interview conducted are discussed.

#### **3.2 ADOPTION OF READABILITY MEASURES**

Referring to the literature, it appears that FRES and F-KGL were developed based on adult reading materials and tested on adult readers. This fact justifies the use of these indices on tax law and other tax materials, as they are based on adult readability. Therefore, this study intends to test the hypothesis based on the four readability measures discussed in Chapter 2, section 2.7. All the readability calculations of this study can be performed using Microsoft Word 2007 computer program. However, using this computer program to calculate readability is associated with large errors as opined by Richardson and Sawyer (1998). After a decade later, Saw and Sawyer (2010) performed the calculations manually and using the computer program. They compared both results and obtained minor differences between the two. As a result, they confirmed that readability result obtained using the computer program is accurate and reliable. Therefore, following Saw and Sawyer (2010), this study utilized the Microsoft Word 2007 computer program to calculate the readability of CITA 2007, comprising 106 Sections in 63 pages (in its original form).



### **3.3 READABILITY DETERMINATION PROCEDURE USING MICROSOFT WORD 2007**

All Sections of the CITA 2007 were subjected to the test excluding fifteen Sections that have less than fifty words. Sentences of less than fifty words were considered inappropriate for this analysis (Smith & Richardson, 1999). Each Section was copied from the Act which is in Portable Document Format (pdf) and pasted on word document, retaining its original format, to test its readability. Then, Microsoft Word 2007 was set up to display readability statistics. This was done by clicking on the Microsoft Office button on the top left of the window of word document. When a dialog box appeared, the “word options” was selected. On the “word options” dialog box, “Proofing” button which was the third option on the left side was selected. On the same dialog box, readability statistics which is under the third section- *when correcting spelling and grammar in Word-* was selected.

After pasting the Section to be tested for readability on the word document, the readability test was carried out based on the following steps: On the menu bar the “Review” button was selected and the standard tool bar appears. On the standard tool bar, “Spelling & Grammar” button was selected. These instructions prompted the Microsoft Word to check spelling and grammar of the text and finally displayed the readability statistics.

### **3.5 INTERVIEW**

This study adopted an interview approach in order to triangulate and compliment the findings of the quantitative analysis, derived from the readability formulae. This

approach is expected to provide more information on the issue at hand. While there are number of interview methods, this study adopted a semi-structured interview.

### **3.5.1 Interview Guide Development**

Questions were developed as a guide for the semi-structured interview before conducting the interviews. The guide consisted of brief explanation of the study and the outlined questions which were sent to the participants. This was to assist the participants to prepare and focus when providing the required information.

### **3.5.2 Sampling Selection**

In a qualitative study, the aim of the sampling is to come up with a sample that is capable of providing rich information for the purpose of the study (Sandelowski, 2000). Therefore, this study interviewed three tax agents and three tax officers of the FIRS, for their views on the complexity of the CITA 2007, in relation to compliance costs and the SAS. For the purposes of this study, this sample is sufficient to provide the required information. There are 82 offices<sup>26</sup> of FIRS (all over the country) that deal with corporate taxpayers. Three officers who deal with corporate taxpayers directly were selected. These officers came from three different branches of the tax authority. There are 1,691<sup>27</sup> accounting firms which offer tax consultation services. In addition, three professional tax agents from three different accounting firms were interviewed. In both cases, convenient sampling was used in selecting the offices as well as the participants. Cavana, Delahaye

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<sup>26</sup> From the FIRS website: <http://www.firs.gov.ng/getdoc/517ba840-941a-4a30-a6fe-28462d93235f/FIRS-Offices.aspx>

<sup>27</sup>This is a total number of accounting firms from Institute of Chartered Accountants of Nigeria (ICAN) web site: <http://www.ican-ngr.org/main.php?section=2&pageid=29>. Members of the institute provide tax consultation services.

and Sekaran (2001) opined that this method guarantees quick access to participants who can provide rich information.

### **3.5.3 Data Collection Procedure**

Semi-structured interview was chosen to compliment the quantitative approach. This is because the study requires information involving participants' personal experience, opinions and perception. Semi-structured interview method allows for questioning the respondents in a sufficient and flexible way to capture relevant information from his or her experience which may not be captured using structured method. In addition, semi-structured method allows for focusing around the required information. In a semi-structured interview method, series of outlined questions can be used to keep the interview in focus and flexible compared to the structured method. Information was collected from the participants and subjected to qualitative data content analysis.

Two chartered accountants and one lawyer representing the accounting firms were interviewed face-to-face. For the FIRS offices, the three participants were interviewed via telephone. In both cases, each of the participants was interviewed for about an hour and the interviews were recorded. In each case, the interview started with a brief explanation of the study in terms of its objective and focus. After that, the interview continued with open questions, which allowed the participants to talk in a broad way and specific questions were then asked to move the conversation to the right direction. In each case, the interview was audio-recorded and transcribed. The written version was sent back to (two of them who gave consent for such request) the participants for more comment and verification, if any. The written versions were subjected to analysis. Responses were categorized into different groups based on their similarities.

## **CHAPTER FOUR**

### **QUANTITATIVE RESULTS AND DISCUSSION**

#### **4.1 INTRODUCTION**

This chapter presents the results of the readability of CITA 2007 which was measured using the readability indices discussed in chapter two. This is followed by discussion of the findings.

#### **4.2 FLESCH READING EASE SCORE (FRES)**

Table 4.1 gives a summary of the CITA 2007 readability test using the FRES index. The Table shows that CITA 2007 has an overall average FRES of 29.76. Given the acceptable threshold score of 60 to 70, this score of 29.76 clearly indicates that the Act is difficult to read and understand.

**Table 4.1**  
**Summary of CITA 2007 Readability Test using FRES Index**

<b>Test</b>	<b>Result</b>
<b>Average Overall Score</b>	<b>29.76</b>
Average Scores by Part:	
Part 1: Administration	36.03
Part 2: Imposition of Tax and Profits	25.60
Part 3: Ascertainment of Profits	32.70
Part 4: Ascertainment of Assessable Profits	39.85
Part 5: Ascertainment of Total Profit	21.30
Part 6: Incentives to Gas Industry	10.90
Part 7: Rates of Tax, Deduction of Tax from Dividends and Relief for Double Taxation	14.52
Part 8: Persons Chargeable, Agents, Liquidators etc.	38.20
Part 9: Returns	29.86
Part 10: Assessments	21.55
Part 11: Appeals	30.60
Part 12: Collection, Recovery and payment of Tax	35.33
Part 13: Offences and Penalties	41.60
Part 14: Miscellaneous	38.63

The Table further reveals that some Parts are more readable than others. For instance, Part 13 (Offences and Penalties) is the most readable Part, followed by Part 4 (Ascertainment of Assessable Profits), with an average FRES of 41.60 and 39.85, respectively. The possible reason for a relatively high readability of Part 13 (compared to the others) is to familiarize the taxpayers about the possible consequences for avoiding or evading tax. This is important to increase awareness of the taxpayers. On the other hand, Part 6 (Incentives to Gas Industry) is the most difficult part followed by Part 7 (Rates of Tax, Deduction of Tax from Dividends and Relief for Double Taxation) with an average FRES of 10.90 and 14.52 respectively. Notwithstanding the fact that Part 6 is the most

difficult, the effect may not be felt by every corporate taxpayers except for those in the Gas Industry. However, it is unfortunate for Part 7 which involves all industries to be the second most difficult to read and understand considering the importance of the Part in computing the tax liability.

Table 4.2 below shows that 56.05% of the Sections have a FRES below 30 which is very difficult to understand. About 25.27% of the Sections are difficult to read and understand and another 10.99% is fairly difficult to understand. Finally, only 6.59% of the Sections fall within the standard score (of 60 to 79) and the remaining 1.10% is easy to understand. This also shows that a substantial part of the Act is difficult to understand.

**Table 4.2**  
**Summary of Flesch Readability Scores**

<b>Flesch Score</b>	<b>CITA 2007</b>		<b>General Reading Ease Score</b>
	No. of Sec.	%	
Below 30	51	56.05%	Very Difficult
30 to 49	23	25.27%	Difficult
50 to 59	10	10.99%	Fairly Difficult
60 to 79	6	6.59%	Standard
80 to 89	1	1.10%	Easy
<b>Total</b>	<b>91</b>	<b>100%</b>	

This is in line with the assertion of Micah et al. (2012) that Nigerian tax laws are complex and difficult for the taxpayers to comprehend, and in some cases are problematic even for the officials of the tax authority. This also indicates that corporate taxpayers have to engage more professionals. As a result of this low level of readability, the tax experts may have to spend longer time working for their clients. Hence, longer time means higher compliance costs to be borne by the corporate taxpayers. In the same vein, the tax

authority has to commit more resources in taxpayer education, tax audit and litigations. Thus, this would increase administrative costs for the tax authority.

Similar results were found in Australian ITA before the re-write process. At that time, the score was 38.44 for the ITA (Smith & Richardson, 1999), indicating a difficult tax Act. After the re-writing process (of some Parts), the Act became more readable with a FRES of 46.42. Although the score of the post re-written ITA 1997 does not meet the required threshold level of 60 to 70, this still indicates an improvement in the readability level of the Act with a percentage increase of 20.86. Thus, if CITA 2007 is redrafted with such a similar increase, the readability level will be 35.97. At this level, the law would be much easier to be understood by those who have undergraduate level of education, under which a large number of the tax consultants may fall.

The results of this study provide a good comparison with the results obtained in New Zealand. The FRES obtained for the New Zealand ITA 1976 was even worse with a score of 1.03 at the early stage of New Zealand tax laws re-write project (Tan & Tower, 1992). Saw and Sawyer (2010) later obtained an improved result of 42.77 for the same legislation after substantial parts of the laws were simplified. This simplification mainly involved the re-writing of the legislation in plain language.

Learning from Australia's and New Zealand's experiences, one can simply conclude that the laws of the developed countries are more readable after the re-write. However, if compared with the results of the pre re-write, they are little bit more readable, with scores of 33.52 (Saw & Sawyer, 2010) and 38.44 (Smith & Richardson, 1999) for New Zealand and Australia respectively.

### **4.3 FLESCH-KINCAID GRADE LEVEL (F-KGL)**

Table 4.3 shows a disappointing results for F-KGL with an average overall F-KGL score of 19.64. Similarly, this score indicates that the Act is not easy to comprehend. It needs education level of a graduate to be able to understand the Act. This supports the assertion of Tukur (2010) that the SAS has not achieved its objective of enhancing voluntary compliance due to the ambiguity in the tax laws. In the same vein, the result supports the Ease of Paying Tax Index that ranked Nigeria 138<sup>th</sup> out of 184 countries (WB & IFC, 2012), as low level of readability is one of the factors that makes tax payment difficult.

Furthermore, Table 4.3 shows that 65.93% of the CITA 2007 can only be understood by those at the university graduate level of education, with a score of 17 and above; while another 17.58% require attainment of undergraduate level 4 of education, with a score of 13 to 16. Only 13.19% is readable by those who have attained senior secondary school 2 level with a score of 7 to 12. The remaining 3.30% requires junior secondary school 1 level of education with a score below 7. To sum up, out of 100%, only 16.49% of the CITA 2007 is within the threshold score of 12 while, all the remaining 83.51% of the Act is below the threshold.



**Table 4.3**  
**F-KGL Summary**

<b>F-KGL Score</b>	<b>No. of Section</b>	<b>%</b>	<b>Education Level</b>
Below 7	3	3.30%	Junior Secondary 1
7 to 12	12	13.19%	Senior Secondary 2
13 to 16	16	17.58%	Undergraduate level 4
17 Above	60	65.93%	University Graduate
<b>Total</b>	<b>91</b>	<b>100.00%</b>	
<b>Overall F-KGL Score of CITA</b>			<b>19.64</b>

Smith and Richardson (1999) and Saw and Sawyer (2010) used F-KGL and obtained scores of 13.38 and 10.76, respectively. When these results are compared with the score 19.64 as obtained in this study, it is apparent that the tax law in Nigeria is more difficult to understand and requires higher level of education.

#### **4.4 AVERAGE SENTENCE LENGTH AND PERCENTAGE OF PASSIVE VOICE**

Table 4.4 shows ASL and PPV of 44.01 and 12.75 respectively. Table 4.4 further shows that 89% of CITA 2007 contains too long sentences that are above the threshold of 20 words per sentence. This together with the ASL indicate the ambiguity of the Act. The PPV gives an interesting result which did not exceed the threshold of 20%. Seventy seven percent (77%) of the Sections are within the threshold. This, in particular, indicates that there is no excessive use of passive sentences in the Act. Yet, this alone does not solve the problem of complexity.

**Table 4.4**  
**Summary of Average Sentence Length and Percentage of Passive Voice**

	<b>ASL</b>	<b>PPV</b>
CITA 2007 Average	44.01	12.75
Sections Within the Threshold (%)	11	77
Sections Outside the Threshold (%)	89	23

In Australia, Smith and Richardson (2002) obtained interesting results for both ASL and PPV for GST 1999 which were 20.9 words per sentence and 20% respectively. Similarly, in New Zealand Saw and Sawyer (2010) obtained 19.98 words per sentence and 13% for ASL and PPV respectively for ITA 2007. All these results were found to be within the threshold. Comparing this result with that of CITA 2007, it is clear that CITA 2007 has longer sentences than tax legislations in both countries. This is further evidence for CITA 2007 being more difficult compared with the Australian and New Zealand legislations. However, in terms of use of passive voices, CITA 2007 appeared to be better with an average difference of 42%. Based on the results from FRES, F-KGL, and ASL, the hypothesis of this study that the readability level of CITA 2007 is low is hereby supported.

Generally, the results show that the CITA 2007 is complex with low readability level. The FRES, F-KGL and ASL results all indicated there is low level of readability which makes the Act difficult to understand. Interestingly, in terms of passive voice usage, the result shows that the Act is not in excessive use of the passive voice. It is also surprising that the Act is also difficult for the trained tax professionals. This can be explained by the fact that most of the professionals are trained accountants, not lawyers, and it is normal, in the case of the SAS, that when a new system is introduced, it takes time before the professionals become familiar with it. A similar situation was observed in the UK. After four years of SAS experience, the ACCA revealed that 36% of its members had difficulty with the SAS and about 9% of them admitted that the new system was still problematic (ACCA, 2002 as cited in Lai & Choong, 2009).

## **CHAPTER FIVE**

### **QUALITATIVE DATA ANALYSIS AND DISCUSSION**

#### **5.1 INTRODUCTION**

After collecting the qualitative information from the participants, this study analyzed the transcribed information collected using content analysis. The data was grouped into different themes and main ideas to answer the research questions in order to achieve the objectives of this study. Content analysis aims at sorting recorded communication which may be transcripts of interviews, observations, etc. (Mayring, 2002). The transcribed information was sorted out under the following themes:

#### **5.2 COMPLEXITY IN THE CITA 2007**

All the participants mentioned that there is language complexity in the CITA 2007 which indicated low level of readability. The participants discussed four major factors as the reasons for this complexity:

##### **5.2.1 Reasons for the Complexity**

When probed on the reasons for complexity of the legislations, the participants came up with four interesting points: (i) The CITA 2007 is difficult to understand because it is drafted in a technical language. Consequently, anybody who is not a professional find it very difficult to understand; (ii) Besides the technical language, other factors, such as long sentences, archaic words and too much information contributed to the language problem; (iii) The Act is still the inherited law from the British colonial masters, has not been changed into Nigerian context and is full of archaic words. Most of the participants noted that, in some cases, even the professionals, such as the lawyers and accountants, find it difficult to understand some provisions of the law. It takes them time to make

conclusions on certain issues due to the low level of readability of the Act; and(iv) the style by which the CITA 2007 is structured has also contributed to complexity. Most of the participants believe that the style of drafting the CITA 2007 is not good in terms of structure and this has added to the problem of low level of readability, thus making the Act very difficult to understand. They further noted that similar items that should be under one Section or Part are dispersed in different Sections and/or Parts. This is in line with the finding of Karlinsky and Koch (1987) that tax laws presentation style has significant impact on understanding the law. For example:

“..... generally, the law is written in a technical language of lawyers. So, it is not easy for somebody who is not a professional to understand the context of the CITA 2007. Sometimes, it takes even the professionals long time to draw conclusions on what the law is talking about...”

(Participant no. 1, Professional Accountant from FIRS)

“.... Talking from my experience as a lawyer, honestly speaking, the CITA 2007 is difficult to understand. ....The law is confusing. Take for example, the issue of assessment. There are different types of assessments - self-assessment, government assessment, best of judgment assessment (amended or revised), additional assessment and the rest. If you look at these assessments, apart from self-assessment, all the rest are government assessments under different circumstances. Also, the language of the law is not plain - is too technical.....”

(Participant no. 2, Barrister from FIRS)

“... internal cross-referencing (on one item) from one Section to another, from one Part to another and from schedule to schedule contributes to the readability problems. I think the law should be straightforward. Similar items should be housed under one Part or Chapter”

(Participant no. 3, Barrister from Accounting Firm)

This response was expected as Micah et al. (2010) identified tax laws in Nigeria as complex and difficult for the taxpayer to comprehend, and in some cases, problematic even for tax officials. This is also in line with the quantitative findings of this study that indicated low level of readability with FRES and F-KGL of 32.44 and 18.71 respectively.

Some of the participants pointed out that content complexity, though different from readability, is another important issue of tax law complexity. This arises as a result of complexity in economic and business systems, which are reflected in the law. Also, in trying to fix the changing business and social environment in the law, the law becomes more complex. For example:

“ ... Although, I observe that content complexity is outside the scope of your work, in my opinion, it adds to the low level of readability.... In the early stage, the law has few Sections but it has expanded and become bulky with so many Sections and long sentences due to expansion and complexity in the business, social and government activities. As such, the content becomes difficult’.

(Participant no. 2, Barrister from FIRS)

### **5.2.2 Impact of the Complexity**

The low level of readability has impacted both taxpayers, as well as the tax authority. The taxpayers make mistakes of under or over-payment of tax because of these complexities. In some cases, this happens unintentionally. This is in line with the assertion of Evans (2012) that complexity increases the chance of both intentional as well as unintentional non-compliance. The participants from the tax authority (FIRS) noted that in most cases, consultants who are professional lawyers and/or accountants represent the corporate taxpayers, but the taxpayers still make such mistakes of under or overpayment. This is because, the taxpayers have to refer to the laws in order to furnish their consultants with some of the information required to file a return. Thus, the taxpayers, as a result of language complexity, make mistakes which may lead to over or under-payment of tax. Some cases of this nature were revealed by tax audit. On the side of the tax authority, it takes them long time to resolve some issues with the tax consultants due to ambiguities in the law. In turn, this makes their work boring and tedious. For instance:

“.. In some cases, the corporate taxpayers (accounting unit) are able to handle the tax issues but due to the perception of complexity in the law, they always rely on the tax consultants”

(Participant no. 1, Professional Accountant from FIRS)

### **5.3 LOW LEVEL OF READABILITY AND COMPLIANCE AND ADMINISTRATIVE COST**

All the participants agree that low level of readability adds to the compliance costs of the taxpayers, especially the corporate taxpayers, who in most cases hire the services of tax

professionals. Basically, low level of readability is one of the factors that makes it necessary for them to depend on the professionals. Most of the participants emphasized that the low level of readability increases the compliance costs by making the work of the tax professionals more difficult. They spend more time that can be saved if the tax law is simple to understand. In turn, this adds to the charges paid to the tax consultants. The comment is as follows:

“ ... So, the taxpayer has to engage our services or other consultants and we don't do it for free. After that, the taxpayer pays the tax according to the law... he is paying twice for something he should have paid only once”

(Participant no. 4, Professional Accountant from Accounting Firm)

On the other hand, as a result of the low level of readability, the tax administration incurs high costs of more employees, workshop for employees, prosecution, and sending notices and reminders to the taxpayers. Most of these costs could have been saved if the law makes everything simple and clear about the responsibilities of all stakeholders.

“... of course, it adds to the administrative costs (referring to low level of readability). If people don't appreciate easily the legislative document, the tax authority has to go the extra mile in order to ensure that people appreciate the content of the law... this adds to the expenses of the workshops, enlightenment programs. A lot of costs may be saved if the tax law is easily comprehensible.”

(Participant no. 2, Barrister from Accounting Firm)

#### **5.4 LOW LEVEL OF READABILITY AND SAS**

The participants from FIRS emphasized that low level of readability is very important issue under the SAS as more responsibilities have now shifted to taxpayers. Indirectly, these responsibilities have actually shifted to tax consultants, because the taxpayers depend on their consultants. Thus, this adds to the compliance costs as the taxpayers have to shift the additional responsibilities to the consultants for a fee. One of the participants, from the tax authority (FIRS), affirmed that they faced more problems in the early stage of the SAS. The SAS comes with the cost of taxpayer education and enlightenment, which could be minimized if the law is simple and clear. The participants from the tax authority also, affirmed that they faced more problems during the early stages of the SAS; even the tax consultants. This is in line with the findings of the ACCA, 2002 as cited in Lai & Choong, 2009, that after four years of the SAS, 36% of its members have difficulty with the SAS and about 9% of them admitted that the new system is still problematic. For example:

“...SAS would have been better if the language of the laws is simplified..... this will help the companies in providing the appropriate information to us and we do our work appropriately. This will also reduce the audit work of the tax authority”

(Participant no. 4, Professional Accountant from Accounting Firm)

#### **5.5 TAX LAW RE-WRITE**

All the participants, with the exemption of one, believe that there is need to re-write Nigerian tax laws in a plain language. However, they noted that this will only mitigate the problem of tax complexity. The re-write will help the taxpayer to easily understand



why, when, where and how much to pay tax. This will enhance voluntary compliance and help in minimizing the non-compliance problem. For example:

“...if countries ( referring to UK, NZ and Australia) with higher level of literacy see reasons in re-writing their laws to be more user friendly, why not Nigeria where the literacy level is lower. So, I’m sure if the law is simple, the level of compliance will be higher”

(Participant no. 4, Professional Accountant from Accounting firm)

Some of the participants have the opinion that the tax law re-write should be directed to the taxpayer. This is because, the taxpayer is the one who pays the tax and tax consultants provide their services to the taxpayer due to the ambiguity in the law. One of the participants suggested writing the tax laws in the three main local languages (Hausa, Yoruba and Igbo) as a measure that can simplify taxation and enhance voluntary tax compliance. For instance:

“ ... in my opinion, tax law rewrite should be directed to the taxpayers as they are the custodians of the information they provide... I think this (referring to re-write) will simplify our job and that of the tax authority.”

(Participant no. 5, Barrister from Accounting firm)

The qualitative findings triangulated the results of the quantitative part of this study. Both supported the hypothesis and answered the research question of whether the CITA 2007 has low level of readability. The qualitative finding further explored the association between the low level of readability and compliance, administrative costs and the SAS.

The responses showed that there is an association between the low level of readability and both costs. The association showed that low level of readability increases both costs. In the same vein, low level of readability impairs the performance of SAS. It also explored the impact of style on readability of CITA 2007. The responses showed that the arrangement of the CITA 2007 does not have a good structure and this makes the Act more ambiguous. Moreover, it should be emphasized that the participants made it clear that even the professionals face the difficulty.

## **CHAPTER SIX**

### **CONCLUSION, IMPLICATION AND FUTURE RESEARCH**

#### **6.1 CONCLUSION**

This study examined the readability of CITA 2007. The study also explored the association between the low level of readability of CITA 2007 and compliance and administrative costs as well as the SAS. The study employed mix method approach to achieve its objectives, via quantitative and qualitative methods. For the quantitative method, the study used the readability formulae - FRES, F-KGL, ASL and PPV. This study found that the CITA 2007 has low level of readability due to long sentences and words. The Act also required attainment of high level of education to be able to understand it because of the low level of readability. Interestingly, in terms of use of PPV, it is found to be within the required threshold. Similarly, the qualitative findings provided more evidences that the CITA 2007 is difficult to understand. The participants suggested that the low level of readability was due to the archaic words, long sentences and the style in which the Act is drafted. Consequently, this issue of low level of readability increases the compliance and administrative costs of taxation, especially under the SAS.

This study used readability indices and found that the CITA 2007 is difficult to understand. It is interesting that the study further used different methodology, through interviews to provide further empirical evidence to support the readability indices results. Moreover, to the best knowledge of the researcher, most of the readability of tax laws studies were carried out in the developed countries. Thus, this study provided evidence on the readability of tax laws in a developing country, specifically Nigeria.

## **6.2 IMPLICATION**

Looking at the results of this study from the policy perspective, the results imply that the CITA 2007 is very difficult to understand, even by the tax professionals. This leads to an increase in compliance costs as well as administrative costs of taxation and also impairs the progress of the SAS. Thus, there is need to re-write tax laws in Nigeria in order to enhance voluntary compliance by reducing both compliance as well as administrative costs of taxation.

This study identified low level of readability as one of the factors that has become an obstacle for tax revenue generation from the non-oil sector. Therefore, there is need for tax policy simplification which should include language simplification. This simplification will also help in making it easy for all businesses, especially small ones, to pay taxes in Nigeria. More importantly, this may encourage foreign businesses to do business in Nigeria.

It can be deduced from the results of previous studies that investigated the success of tax laws re-write projects, that the success achieved is meager. However, it is important to simplify language ambiguity of tax laws to reduce compliance costs by decreasing the amount of assistance needed from tax consultants in completing simple taxation returns and to improve taxpayer compliance (Smith & Richardson, 1999). Consequently, readability of tax law should be treated as a subset of tax policy simplification. Therefore, tax simplification policy that includes readability, together with other important determinants of tax law complexity, should reap better success than one that concentrates on re-writing the tax laws alone. Simplification of tax law has many dimensions; readability is just one out of the many dimensions (Smith & Richardson, 1999).

### **6.3 FUTURE RESEARCH**

Regarding the qualitative results, the study used only a sample of six participants. Future researches should use larger number of samples and different methods, such as cloze<sup>28</sup> analysis to enhance generalizability of the result. More importantly, the sample should include the companies who are the actual taxpayers.

Future research should study tax law complexity from the perspective of other important factors, like tax policy, as complexity of tax law should not be narrowed to readability alone due to the changing requirements of tax policy, which is also a source of such complexity, as noted by James and Wallschuzky (1997).

Finally, complexity of tax laws has been one of the problems tax commentators complained about, while readability of the tax laws is one of the aspects of tax law complexity. Thus, identifying the level of readability is very important in an attempt to increase voluntary tax compliance.

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<sup>28</sup>This is a test used to measure readability of a given text by removing some words and asking the participant to fill in the missing words. This test determines whether the context of the text is understood by the participant.

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