



To cite this article: Yibekal Tadesse Abate, *Value Added Tax Assignment under the FDRE Constitution: Designated or Undesignated?*, *HARAMAYA LAW REVIEW* 8(2019): 41-56

VALUE ADDED TAX ASSIGNMENT UNDER THE FDRE CONSTITUTION: DESIGNATED OR UNDESIGNATED?

*Yibekal Tadesse Abate**

Abstract

Whatever form of tax assignment a federal system of government adopts, an assignment of taxation power for each tier of government shall be determined under the constitution. The FDRE Constitution is detailed in terms of allocating taxation powers between the federal government and the regional States. Despite this, following the late introduction of value-added tax (VAT), there are arguments concerning the taxation power over it. Pieces of legal literatures deem VAT as an undesignated tax while, on the other side, some persons argue that it is a designated one. This leaves the constitutional status of VAT in Ethiopia to remain questionable. Practically, it is the federal government that takes the legislative competences over all sources of VAT in the country. This paper aims at examining the stance of the FDRE Constitution concerning taxation power over VAT and to scrutinize whether VAT is practically levied as per the VAT assignments set under the Constitution. Finally, the paper argues that the FDRE constitution has designated VAT (as a family of sales tax and 'in other forms' too) for both tiers of government within their respective taxation powers. In fact, it is also revealed that there are certain undesignated VAT sources from which the government practically collects a VAT. There, the existing practice where the federal government takes the legislative competence over VAT sources shall be re-visited in light of the constitutional provisions.

Keywords: *Fiscal Federalism, Sales tax, VAT, Constitutional Status, Ethiopia.*

I. INTRODUCTION

“Scholars are undivided in arguing that fiscal federalism may aggravate imbalances and contests if there are ambiguities in the tax assignment of major tax bases.”¹ Hence, the assignment of the power of taxation of each tier of the government in a federal system needs to have constitutional status and guarantee. Like other federal states, Ethiopia has assigned the sources of revenue for the two tiers of the government under the FDRE Constitution. The

* LL.B (Bahir Dar University), LL.M in Business and Corporate Law (Bahir Dar University), Lecturer in Law, Mizan-Tepi University, School of Law. I am grateful to the anonymous reviewers of HLR for the insightful and constructive comments on earlier version of this article. All errors remain mine. The author can be reached at yibekaltadesse@gmail.com.

¹Alefe Abeje Belay, *System of Division of Revenue in Ethiopia*, 2 EUROPEAN SCIENTIFIC JOURNAL, /Special/ 95 (2014).

Constitution allocates the power of taxation in the forms of federal exclusive, state exclusive, concurrent power and undesignated power of taxation.² According to the Constitution, federal exclusive and state exclusive taxation power is not the tax base but the tax source.³

However, due to its late introduction as “new tax”, the constitutional status of VAT turns out to be argumentative. As exemplified below, it is sometimes argued that VAT is an undesignated tax whose assignment to a level of the government needs to pass the requirements of Article 99 of the FDRE Constitution.⁴ Contrarily, it is also stated that VAT is a designated tax under the Constitution as a family of sales tax. By and large, the source of such a dispute is the absence of VAT by name in the Constitution.

Constitutional assignment of power of taxation in a federal system is very difficult as, among others, the two different authorities are arising from the same body of taxpayers. States may apportion the sources of revenues to each tier of the government based on the theories of fiscal federalism and political processes and behavior of political agents.⁵ Many federal states do not, however, assign the power of taxation in accordance with the theories of fiscal federalism.⁶ When it comes to Ethiopia, as indicated above, to which level of the government the country allocates the power over VAT is still argumentative. Literatures written on the tax assignments in Ethiopia have divided standings pertaining to the constitutional status of VAT. In fact, so far, one cannot find a literature devoted to addressing the constitutional status of VAT in Ethiopia as a sole endeavor. Largely, literatures touched the constitutional status of VAT tangentially while discussing the concept of the so-called undesignated power of taxation. For instance, Taddese Lencho argued that, depending on different considerations, VAT can be deemed as designated or undesignated tax. “If we considered the substance, VAT is designated under the Constitution as a family of general sales tax. And “If we take ‘undesignated’ to mean literally ‘unmentioned,’ VAT qualifies as an undesignated tax and thus falls under Article 99 of the Constitution.”⁷ Ghebrehiwet Tesfai has also argued that “the assignment of VAT implicitly respects the assignment of sales tax which has been stipulated in the FDRE Constitution.”⁸

Despite the above, the joint session of the Federal Houses designated the power to levy VAT to the federal government.⁹ Hence, it means that the two Houses had apparently taken VAT as an

² *The Constitution of the Federal Democratic Republic of Ethiopia*, Proclamation No 1/1995, FED. NEGARIT GAZZETA 1st Year No.1, Addis Ababa 21st August 1995. (Hereinafter, FDRE CONSTITUTION).

³ For example, the FDRE Constitution does not assign the whole income tax base to the federal. It assigns this base to both levels of the governments. The same holds for excise tax and sales tax.

⁴ As per Art. 99 of the Constitution, taxes which have not been specifically provided for in the Constitution will be assigned as federal exclusive, state exclusive or concurrent power by the joint session of the Federal Houses.

⁵ See NERINGA SLAVINSKAITE, FISCAL DECENTRALIZATION AND ECONOMIC THEORY 88- 97(2015). available at <https://parc.ipp.pt/index.php/rebules/article/> (Accessed on 10 September 2018)

⁶ See Taddese Lencho, *Income Tax Assignment Under the Ethiopian Constitution: Issues to Worry About*, 4(1) MIZAN LAW REVIEW 31, 36 (2010).

⁷ Taddese Lencho, *The Ethiopian Tax System: Excesses and Gaps*, 20(2) MICHIGAN STATE INTERNATIONAL LAW REVIEW 327, 333 (2013).

⁸ Ghebrehiwet Tesfai Baraki, *The Practice Of Fiscal Federalism In Ethiopia: A Critical Assessment 1991-2012, An Institutional Approach*, (unpublished, Doctoral Thesis, Fribourg University, Switzerland, 2015). at 249. (Hereinafter, Ghebrehiwet Tesfai).

⁹ See the Minutes of the joint session of the House of Peoples’ Representatives and the House of Federation, at 1-6 (1994). (As quoted in Getachew Mengeste, *Intergovernmental Fiscal Transfers In Ethiopia: Challenges And Some*

undesigned tax. Moreover, currently, the federal government defines and determines the tax bases, exemptions and the rate for overall sources of VAT in the country. As a result, VAT is uniform across the country and the states are administrators of the federal Value Added Tax Proclamation No.285/2002.¹⁰

In general, it can be concluded that, though there are pieces of literature on VAT, none of them deeply scrutinize its constitutional assignment in Ethiopia. In addition, literatures that considered VAT as a designated tax (as sale tax) neither critically examine how VAT is a variety of sales taxes nor do they examine the modes used in the FDRE Constitution in the tax assignments. Moreover, there are practical scenarios where VAT in Ethiopia is collected from activities/supplies which are not properly sale transactions.¹¹ The constitutional base of VAT on such non-sale transactions is therefore unclear. Hence, whether the power of taxation over VAT is only anecdotal with the provisions that state about sales tax or VAT can also be inferred in other cases is an important question.

As per the theories of fiscal federalism and theories of tax assignment, any tax base which has a macroeconomic stabilization and income redistribution role should automatically belong to the central government.¹² Among others, personal income tax, corporate income tax and VAT are some of the major revenue sources that have redistribution impact and, hence, they need to be sacred to the center.¹³ With regard to VAT, the theories of fiscal federalism recommend that the tax base determination, tax administration and collection shall be given to the central government while VAT rate determination shall be exercised jointly by the central and regional governments.¹⁴ The rationale of the theories for such allocation is the assumption that VAT is among taxes with the role of wealth/income redistribution.¹⁵

This article aims at shedding light on the overall constitutional status of VAT by examining the nature and notion of VAT, its relation with sales tax, and by making inferences from the tax assignment modes used in the FDRE Constitution. To meet its purpose, the paper analyzes the relevant provisions of the FDRE Constitution and other relevant laws. The constitutions of

Options, A Comparative Study, available at <http://www.aau.edu.et/library/resources/aau-institutional-repositoryelectronic-thesis-and-dissertation/> (Accessed on 10 May 2019)

¹⁰ *Value Added Tax Proclamation*, Proclamation No. 285/2002. FED NEGARIT GAZETA, 18th Year, No. 33, Addis Ababa, 4th July (2002) (Hereinafter, VAT Proclamation).

¹¹ A 'supply' as defined in the VAT proclamation is much broader than a sale transaction. According to Art.2 (17) of the VAT Proclamation, supplies means the sale of goods or the rendition of services or both. More importantly, Art. 4 of the same Proclamation defines both supply of goods and services. Supply of goods means 1) a sale of goods; 2) a grant of the use or right to use goods, whether with or without a driver, pilot, crew or operator, under a rental agreement, credit agreement, freight contract, agreement for charter or any other agreement; 3) a transfer or provision of thermal or electrical energy, gas or water. And a rendition of services means *anything* done which is not a supply of goods or money, including; 1) the granting, assignment, cessation, or surrender of any right; 2) making available a facility or advantage.

¹² Alene Agegnehu and Ayele Behaylu, *Tax Assignment: Theory Nexus Practice in Australia, Canada, Germany, Ethiopia and Switzerland: Review*, 6(7) RESEARCH JOURNAL OF FINANCE AND ACCOUNTING, 123 (2015).

¹³ *Id.*

¹⁴ Taddese, *supra* note 6, at 37.

¹⁵ Alene and Ayele, *supra* note 12, at 123- 124.

selected federal states, books and journals are also consulted to know the approaches used in the assignment of the value added tax.

The rest of this article is divided into five sections. Section II addresses the general conceptual framework of VAT. Under section III, the assignment of taxation power and constitutional status of VAT in federal systems have been discussed. Section IV briefly examines the methods and principles of tax assignment embodied under the FDRE Constitution. Section V is about the constitutional assignment of VAT in Ethiopia. Finally, section concludes and forwards recommendations.

II. VALUE ADDED TAX: CONCEPTUAL FRAMEWORK

Before the emergence of VAT, taxes imposed on transactions were known as sale taxes that consisted of retail, wholesale and manufacturer's sales tax.¹⁶ Countries used different variants of these sales taxes. For example, a Retail Sales Tax was known in Sweden and various states of United States¹⁷ while at the same time other forms of sales taxes have been used by other nations such as Wholesale Sales Tax in Switzerland¹⁸, Two-Stage wholesale-Retail Sales Tax in Finland, Manufacturer's Sales Tax in Canada¹⁹, Value Added Tax in France, Turnover or Cascade Tax in Germany, Italy, Belgium, Netherlands, and Luxembourg.²⁰ If VAT is considered as a variant of a sales tax, its origin run deep though it is generally perceived as a modern fiscal innovation.²¹ The German businessman, Wilhelm Von Siemens, is credited for the idea of VAT in the 1920s.²² However, VAT was first introduced at a national level in France in 1954.²³

Because of the pitfalls or distortionary character of general sales taxes, countries have been moving to different variants of sales taxes, including VAT.²⁴ As of the mid-20th century, most countries of the world have moved to VAT by replacing their general sales tax and its varieties.²⁵ VAT is now the most important form of general sales tax in use.²⁶ Under a general sales tax system, businesses do not have an opportunity to recover sales taxes (input tax) they paid in the previous transactions for intermediate goods and services. Therefore, they would shift the input

¹⁶ Ann F. Friedlaender, *Indirect Taxes and Relative Prices*, 81(1) THE QUARTERLY JOURNAL OF ECONOMICS, 126 (1967).

¹⁷ *Id.* It is a single-stage taxes that may be imposed at one of several stages in the manufacturing and distribution process. In the US, it is a retail sales tax which is enforced even today.

¹⁸ *Id.*

¹⁹ *Id.*, A single-stage tax at the manufacturers' level is designed to limit tax to sales by manufacturers to wholesalers or retailers.

²⁰ *Id.*

²¹ Kathryn James, *The Rise of the value-added tax*, Part of Cambridge Tax Law Series, Cambridge University Press, 978-1-107-04412-8, at 1, (2015), available at <https://www.cambridge.org/core/series/cambridge-tax-law-series/> (Accessed on 17 July 2018).

²² Ebrill et al., *The Modern VAT* (Washington: International Monetary Fund). at 4 (2001); available at <<https://www.elibrary.imf.org/doc/IMF>> (Accessed on 10 June 2019).

²³ *Id.*

²⁴ Dasalegn Mosissa Jalata, *The Value Added Tax and Sales Tax in Ethiopia: A Comparative Overview*, 6(23) EUROPEAN JOURNAL OF BUSINESS AND MANAGEMENT, 246 (2014).

²⁵ GOODE RICHARD, *GOVERNMENT FINANCE IN DEVELOPING COUNTRIES*, 157 (Washington D.C.: Brookings Institution, 1984).

²⁶ WORLD BANK, *THE TAX ASSIGNMENT PROBLEM: CONCEPTUAL AND ADMINISTRATIVE CONSIDERATIONS IN ACHIEVING SUBNATIONAL FISCAL AUTONOMY* 29 (Proceedings. Washington DC: World Bank Group.1999).

taxes to the next chain of transactions by adding to the sale price of the taxed goods or services. Since the sales tax base is going to be the gross receipt (includes the sales value of the goods plus the tax charged accumulatively in previous stages), the imposition of sales tax on business inputs led to cascading tax (tax on tax).²⁷ This in effect will increase the amount of tax to be paid by business persons especially in capital intensive industries, and increased export prices compared to countries operating a VAT.²⁸ General sales tax can, thus, increase the prices across the chains, distort market signals and influence efficient allocations of resources, and ultimately impeded economic growth.²⁹

Unlike general sales tax, which is applied to the full value of a product every time it changes hands in the process of production and distribution, VAT is assessed at each stage only on the value added to the product or service after the last taxable transaction. At the end of the chain, the total amount of tax paid on a given commodity or service is only a function of the rate of tax and of the final price of the commodity independently of the number of stages through which it has passed.³⁰ This is because VAT is levied on each of the entities in the supply chain with the facility of set-off of input tax.³¹ For this reason, in contrast to general sales tax, there is no space in the VAT system for cascading of tax and hence the amount of tax liability will not get higher even if the production chains are longer.³² Indeed, end users of products and services bear the tax burden or the incidence since they cannot recover the tax paid on the consumption of goods and services.

Moreover, the nature of VAT may be explained based on the fact that taxes can commonly be classified as direct and indirect taxes. While direct taxes are those taxes whose official burden (the impact) and economic burden (the incidence) fall on the same person, indirect taxes are those taxes whose impact and incidence fall on different persons. VAT is a typical example of an indirect tax since it is possible to set-off input tax. The incidence of a VAT is identical to that of a final-point sales tax (a consumption or retail sales tax if that final-point sale is to a consumer).³³

In general, sales tax is a *basket of taxes* which comprises different taxes, including VAT. However, VAT falls under the general category of a consumption tax as it is imposed on consumptions and it is to be charged on the value of imports and on value added to goods and services supplied by one business to another person.³⁴ Despite its name, the VAT is not thus generally intended to be a tax on value added as such; rather, it is usually intended as a tax on

²⁷ As sales taxes paid for inputs at earlier stages are not credited (refunded), businesses will shift them to the next chain. In the next chain, the input taxes will constitute part of the base for the tax. This results in tax over tax.

²⁸ South African Revenue Service, *Key Revenue Sources a Brief History of Income Tax and VAT*, available at www.sars.gov.za, (Accessed on 13 May 2019).

²⁹ DASALEGN, *supra* note 24, at 246-247.

³⁰ See "The Value-Added Tax in Developing Countries", Staff Papers- International Monetary Fund, Vol. 20, No. 2 At 318-378(Jul., 1973), available at <http://www.jstor.org/stable/3866322>, (Accessed on 13 April 2019)

³¹ For example, input VAT paid at the stage of the purchase of goods by a trader and on the purchase of raw materials by a manufacturer.

³² DASALEGN, *supra* note 24, at 246-247.

³³ Richard Bird and Sijbren Cnossen, Policy Watch, Value-Added Tax Options for India, Kluwer Academic Publishers, at 115, (1995), available at <http://personal.lse.ac.uk/sternn/077NHS.pdf> (Accessed on 13 May 2019)

³⁴ Dasalegn, *supra* note 24, at 246.

consumption.³⁵ Correspondingly, VAT is practically charged on certain transactions such as the sale of goods, the provision of services, and other types of supplies.³⁶

III. VALUE ADDED TAX UNDER THE CONSTITUTIONS OF SELECTED FEDERAL SYSTEMS

In this section, the author presents experiences of selected countries on the basis of the character of their constitutions and practical situations with regard to assignment of VAT. Accordingly, brief discussion is made on the experience of countries having different constitutional clauses regarding VAT. When we look at constitutional tax assignment, federal constitutions have assigned taxes by specifically mentioning the name of the tax base or merely the name of the 'tax family'. The constitutions that assign by general tax families to either tiers of the government consider that the specific taxes within that tax family are deemed to be assigned together.³⁷ As succinctly depicted below, while there exist constitutions that consider VAT under generic terms like 'sales tax' or 'transaction taxes', there are constitutions that expressly mention VAT by name. Moreover, there are countries with no indication at all for sales taxes or VAT in their constitution. In this case, subsidiary legislations are important to know which level of the government has the power to levy and collect the taxes.

In Switzerland, the federal constitution gives the three levels of the government, federal, cantonal and municipal, the right to levy taxes. The Confederation (Center) relies on consumption (indirect) taxes whereas the cantons and municipalities are largely accredited on direct taxes like income and wealth taxes.³⁸ The cantons have fiscal sovereignty where it is not the domain of the Confederation.³⁹ As the Confederation may only claim exclusive jurisdiction over relatively few types of taxes such as on customs duties, VAT, special expenditure taxes, stamp duties and Swiss withholding tax, the cantons are given broader scope to define their own tax legislation.⁴⁰ Accordingly, each canton has its own tax legislation and taxes as appropriate on the income and assets of individuals, the profits and capital of legal entities, inheritances and donations, property gains, etc. The Confederation may administer only those taxes which the federal constitution expressly authorizes it.⁴¹ As to VAT, the constitution specifically gives the power of taxation to the central government by expressly mentioning the name VAT.⁴²

³⁵ Njogu, L. K. (2015). The effect of value added tax on economic growth in Kenya. *International Academic Journal of Economics and Finance*, 1 (5), 13. available at: http://www.iajournals.org/articles/iajef_v1_i5_10_30.pdf (Accessed on October 23 2019).

³⁶ Bekure Herouy, *The VAT Regime under Ethiopian Law with Special Emphasis on Tax Exemption: The Ethiopian and International Experience*,7(2004); available at <http://www.crdaethiopia.org/>; (Accessed on 18 October, 2019).

³⁷ For example, in India power on VAT is exercised on the basis of the constitutional power on sales taxes. See *Value Added Tax (VAT) at Central and State Level means*, available at <https://howtoexportimport.com/Value-Added-Tax-VAT-at-Central-and-State-level-mea-9453.aspx>, (Accessed on 17 May, 2019).

³⁸ Macos Terak, *The Swiss Taxation System*, at 11. available at [https://www.caminada.com/sites/default/files/See also ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT\(OECD\), FISCAL FEDERALISM AND FINANCIAL EQUALIZATION, at 55 \(2002\).](https://www.caminada.com/sites/default/files/See%20also%20ORGANIZATION%20FOR%20ECONOMIC%20COOPERATION%20AND%20DEVELOPMENT(OECD)%20FISCAL%20FEDERALISM%20AND%20FINANCIAL%20EQUALIZATION%20at%2055%20(2002).)

³⁹ Federal Constitution of the Swiss Confederation of 18 April 1999 (status as of January 2018), Art. 3, available at <http://www.constituteproject.org/>. (Accessed on 27 April, 2019).

⁴⁰ *Id.* Art. 130- 133.

⁴¹ Macos Terak *supra* note 38, at 11.

⁴² Federal Constitution of the Swiss Confederation, *supra* note 39, Art. 130.

Like Switzerland, the Constitution of Nepal of 2015 has clearly assigned the revenue power between three layers of the government. Schedules 5 to 9 of the constitution have provided the exclusive and concurrent revenue assignments of the federal, state, local governments.⁴³ In respect to VAT, the constitution expressly (by name) assigned to the central government.⁴⁴

In Nigeria, section four of the 1999 constitution provides the exclusive federal powers and the concurrent powers. It reserves the residual power of taxation to the states.⁴⁵ The Nigerian constitution empowers the federal government to have exclusive power to collect taxes on incomes, profit, and capital gain.⁴⁶ And the concurrent powers of taxation are over capital gains, incomes or profits of persons other than companies, and documents or transactions by way of stamp duties.⁴⁷ Therefore, other forms of taxes are given to the states based on residuality.⁴⁸ Since VAT or sales taxes is not mentioned by name or substance in the constitution, the power of taxation over VAT is thus assigned to states.⁴⁹ In practice, however, it is the federal government that has a legislative competence over VAT though the federal government has a duty to distribute the proceeds among the three tiers of governments.⁵⁰

In India, the assignment of tax powers is based on the principle of separation (the tax bases are exclusively assigned to the center or states) and the principle of residuality.⁵¹ Most of the broad-based and productive tax bases are to the center. Hence, taxes such as corporation tax and customs duty, taxes on the sale or purchase of newspapers and on advertisements published therein, taxes on the sale or purchase of goods that take place in the course of inter-state commerce are assigned to the center.⁵² On the other hand, states have the power of taxation over, among others, sale or purchase of goods other than newspapers, taxes on the consumption or sale of electricity.⁵³ Besides, the center is given all residual powers.⁵⁴ Though the India constitution is too detailed in specifying power of taxation, it does not mention VAT by name. As a result, the government is assuming power *on the basis of sales taxes* in the constitution which, as shown

⁴³ Nepal's Constitution of 2015 with Amendments through 2016, available at <http://www.constituteproject.org>, (accessed on 20 July, 2019).

⁴⁴ *Id.*, Schedule 5(5).

⁴⁵ Section 4 (7) of the 1999 constitution of Nigeria provides that the House of Assembly of a state shall have power to make laws for the peace, order and good government with respect to any matter not included in the exclusive legislative list and concurrent list in the second schedule to this constitution. It is clear from this that states have residual powers to make laws on any matter that is not on either the exclusive or concurrent legislative list.

⁴⁶ Constitution of the Federal Republic of Nigeria, 1999 Schedule II, parts I, item 59, available at <https://www.wipo.int/edocs/lexdocs/laws/en/ng/ng014en.pdf>, (Accessed on 27 April, 2019).

⁴⁷ *Id.*, schedule II, part II, item 7.

⁴⁸ Ayodele Odusola, *Tax Policy Reforms in Nigeria*, RePEc, at pp 12-13(2006) available at <https://www.researchgate.net/publication/> (Accessed on 17 May, 2019).

⁴⁹ *Id.*, at 49.

⁵⁰ Abiola Sanni, *Current Law and Practice of Value Added Tax in Nigeria*, BRITISH JOURNAL OF ARTS AND SOCIAL SCIENCES, 196. (2012).

⁵¹ The Constitution under art 268, art 269 and under the seventh schedule apportion the tax power of the union and the states (See the Constitution of India (2015), Articles 268 and 269 and Entry in List I of the Seventh Schedule, 92 A. and 97).

⁵² *Id.*, Articles 268 and 269 and Entry in List I of the Seventh Schedule, 92 A.

⁵³ *Id.*, at List II of the Seventh Schedule, Entry No. 52-54.

⁵⁴ *Id.*, Entry in List I of the Seventh Schedule, 97.

here, are allocated to both layers of the government on different subjects.⁵⁵ Hence, the tiers of the government may levy VAT on their respective sales tax competence. Accordingly, India introduced a VAT by replacing federal sales tax and state sales tax.⁵⁶ Now, India has adopted a system of dual VAT: central VAT at the federal level, and state VAT at the state level.⁵⁷ Thus, the constitutional provision of sales tax in India is considered as it includes VAT.

In some other federations, power of administering sales taxes or VAT is allocated through subsidiary legislations since their constitutions are not detailed on the allocation of taxing power on tax bases. For example, the constitutions of Belgium, Australia and Canada do not contain provisions regarding sales taxes in general and VAT in particular. Through their legislations, Australia (as of 2000), and Belgium have assigned VAT only to the center.⁵⁸ Indeed, the countries have chosen an indirect method of VAT decentralization which is VAT revenue sharing arrangements between the center and regions.⁵⁹ In Canada, both federal and provincial governments can levy consumption taxes.⁶⁰ While the federal government levies a VAT (goods and services tax- GST), the provinces levy a retail sales tax (RST).⁶¹ However, Quebec collects the federal VAT along with its own VAT (known as the QST, the Quebec sales tax).⁶²

From the abovementioned discussions, it can be noticed that constitutional assignments can be categorized into three forms. The first category is countries, like Switzerland and Nepal, which specifically assigned VAT by name under the constitution. Secondly, there are countries that assign taxes by the name of the 'sales/transaction tax family'. In this regard, India can be mentioned. Thirdly, there are countries that assign VAT by the principle of residual power. A case in point here is Nigeria.

IV. TAX ASSIGNMENT UNDER THE FDRE CONSTITUTION

The tax assignment between the federal and state governments under the FDRE Constitution is made in the forms of exclusive federal taxes, exclusive state taxes, concurrent taxes, and undesignated power of taxation. The Constitution departs from the assignment formula set for expenditure powers and prescribes a special procedure for assignment of taxes which are neither concurrent nor exclusive to either levels of the government.⁶³ In this sense, the Constitution

⁵⁵ Value Added Tax (VAT) at Central and State level means, *supra* note 37.

⁵⁶ Vishwa Nath Alok, *Assignment Systems in Federations*, Work Session 4, at 107 (2008). available at www.forumfed.org/libdocs/...2/IntConfFed07-Vol2-AS-Alok.pdf (Accessed on 17 May, 2019).

⁵⁷ Mahesh C. Purohit, *Emerging Issues in Fiscal Federalism*, Subtheme Paper Assignment Systems in Federations, p.41 (2008), available at <http://www.forumfed.org/library/theme-paper-emerging-issues-in-fiscal-federalism/> (Accessed on 17 May, 2019). ; See also Dil Bahadur Chhetry, *Tax Assignment in Selected Federations: Lessons for Nepal*, INTERNATIONAL JOURNAL OF SOCIAL SCIENCES, 515 (2017).

⁵⁸ Richard M. Bird and Pierre -Pascal Gendron, *VATs in Federal States: International Experience and Emerging Possibilities*, Working Paper #01 -4, International Studies School of Policy Studies Georgia State University Atlanta Georgia, 7, (2001) available at <https://www.researchgate.net/.../4737794> (Accessed on 18 May, 2019).

⁵⁹ Katarzyna wójtowicz, *Decentralizing VAT – appearance or reality?* Maria Curie, Sklodowska University, at 1294 (2015). available at <https://www.semanticscholar.org/.../> (Accessed on 17 May, 2019).

⁶⁰ Richard M. Bird and Pierre -Pascal Gendron, *supra* note 58, at 8.

⁶¹ *Id.*

⁶² Martin A. Sullivan, *VAT Lessons from Canada*, 285 (2011); available at www.taxhistory.org/www/...nsf/.../SULLIVAN.../SULLIVAN-22.pdf (Accessed on 17 May, 2019).

⁶³ Taddese, *supra* note 6, at 31

comes up with the so called ‘undesigned taxes’ which should pass through the allocation process to be done by the two-thirds majority vote of the two Federal Houses.⁶⁴ Generally, the tax assignment in Ethiopia is not exhaustively made at least for two reasons. First, either of the governments may introduce new taxes from the grand tax bases assigned under the Constitution. This is so because the tax assignment in the Constitution is not based on the tax base. Second, new tax bases and/or sources may be invented by either layers of government since the Constitution does not adopt the concept of residual power.

Global experiences show that tax assignments to different levels of a federal government are done on tax bases.⁶⁵ A certain tax base, say personal income tax or VAT, is assigned exclusively to either levels of the government. Nevertheless, such method of tax assignment is not as such reflected in the FDRE Constitution in which a single tax base is divided between the federal and state governments based on various principles. If we take the income tax assignment as an example, the Constitution divides different income tax sources into smaller pieces and apportions them to both levels of the government. In assigning taxation power to the federal, state and to both concurrently, the FDRE Constitution has relied on various principles such as ownership principle⁶⁶, type of business form⁶⁷, principle of origin⁶⁸, domiciliation principle⁶⁹, inter-State and international trade⁷⁰, and administrative feasibility.⁷¹

On the basis of the aforementioned principles, the FDRE Constitution assigns taxes by name and/or substance.⁷² Taxes mentioned by name are income taxes, monopoly tax, excise tax and customs duty. Unlike other tax families, the income tax assignment under the FDRE constitution is too detailed. The Constitution has divided and assigned income taxes in specific names such as personal income tax, agricultural income tax, income from game of chance, rental income tax and profit income tax. Furthermore, personal income taxes are apportioned into federal exclusive, state exclusive and concurrent powers. Profit income tax is also divided and assigned

⁶⁴ FDRE CONSTITUTION, Art. 99.

⁶⁵ Ghebrehwet Tesfai, *supra* note 8, at 233.

⁶⁶ According to this principle, the owner of a certain public sector or a business activity has taxation power on the resulting tax yield. See Ghebrehwet Tesfai, *supra* note 8 at 233- 238. See also Taddese, *supra* note 7, at 331.

⁶⁷ It has to do with the legal registration of business organization form. If the body has a form of private limited company and share company, it is concurrent power of taxation. On the other hand, revenues generated from sole proprietorship business are under State taxation powers. See Ghebrehwet Tesfai, *supra* note 8, at 233- 238.

⁶⁸ This refers to as the business place from where a particular revenue is generated. For example, Tax on incomes from transport services rendered on waters within State territory is assigned to the States, save for the matters considered as a concurrent power of taxation. See Ghebrehwet Tesfai, *supra* note 8, at 233- 238.

⁶⁹ It refers to the assignment of taxation power to different levels of government which are the permanent residences of the taxpayer. Regardless of the form of business organization, personal income tax on employees of private companies is assigned to the States on domiciliation principle. See Taddese, *supra* note 7, at 331.

⁷⁰ In this regard, we find custom duties and other charges on imports and exports are exclusive taxation powers of the federal government. As it is presumed to be a huge revenue source and the international trade relations are the jurisdiction of the federal government and to redistribute the revenue generated in equitable manner, such taxes shall be assigned to the central government. See Ghebrehwet Tesfai, *supra* note 8, at 233.

⁷¹ The constitution assigns to the central government tax relating to institutions which have more connection with the federal government for administrative conveniences. Such as personal income tax on employees of international organizations, taxes on incomes of air, rail, and sea transport services; taxes on monopolies. See Ghebrehwet Tesfai, *supra* note 8, at 233.

⁷² Taddese, *supra* note 7, at 333.

as federal exclusive, state exclusive and concurrent power of taxation.⁷³ To show how much the Constitution is detailed as to income tax, it may be good to bring some instances. For example, the Constitution does not simply allocate income taxes by declaring that “income taxes on enterprises owned by the federal government to the federal” or it does not stipulate that “regional States shall levy income taxes on individual traders carrying out a business within their territory” either. Rather, it has divided the *grand family income tax* into personal income tax (personal income tax on employees of state owned enterprises, personal income taxes from employees of private enterprises, personal income tax on enterprises they jointly establish, etc.), profit income tax (profit income tax on individual trader, profit income on companies/enterprises, etc.), rental income tax (rental income taxes on income of houses owned by the Federal, rental income taxes on income derived from private houses, etc.), and agricultural income tax (taxes on income of private farmers and farmers incorporated in cooperative associations).

The very intention of the Constitution in getting into such specification is not without reason. It was intended that a tax which is not named and assigned under the Constitution, while its folks (found within the same family) are assigned, will be deemed as unassigned (undesigned) tax and hence shall undergo the procedure set under Article 99 of the Constitution.⁷⁴ Since the Constitution is detailed with regard to such types of tax family, assignment by constitutional interpretation is difficult. Thus, for example, an income tax not specifically named under the Constitution needs to pass through Article 99. This is because the Constitution is very specific as far as income tax family is concerned so that placing new income taxes to one tier of government is very difficult. It is, therefore, in such cases that the role of Article 99 comes into play. For example, income taxes on royalties from the exercise of copyrights and patents, personal income tax of employee of domestic NGOs and income taxes on bank deposit interest are not designated in the Constitution while their folks under the same family are specifically designated. For these mentioned income taxes, either level of the government cannot have power except through Article 99 of the Constitution. That is why, in their joint meeting, the Federal Houses designated the above-mentioned taxes.⁷⁵ In support of the argument, Taddese stated that ‘income tax from royalties, the exercise of copyright and patent, and from interest from bank deposit could not be considered as designated either in name or substance and there would be little debate over the decisions the Federal Houses.’⁷⁶

⁷³ FDRE CONSTITUTION, Arts. 96-98.

⁷⁴ The practice shows such proposition. For example, income from royalties, exercise of copyright and patent, income derived by an entertainer, musician or sportsman/woman from his/her personal activities and income on interest from bank deposit are considered as unassigned as they are unmentioned while their folks are mentioned in the constitution and hence passed through Art 99 of the constitution. Likewise, though the federal houses have appreciated VAT as unassigned tax, the latter decision of the federal government permission to regions to collect and take proceeds of VAT from sources of which they are empowered under the constitution to levy sales taxes, in turn confirms that, Article 99 works for taxes whose tax family is not put in grand and general way.

⁷⁵ Minutes of the 1st Joint Session of the House of Federation and the House of Peoples Representatives (Meskerem 26, 1996 E.C. in Amharic), as quoted in, TADDESE, *supra* note 7, at 334.

⁷⁶ *Id.*, *supra* note 7, at 334.

V. THE VALUE ADDED TAX ASSIGNMENT UNDER THE FDRE CONSTITUTION: DESIGNATED OR UNDESIGNATED?

In the above discussion, it is said that the FDRE Constitution assigns taxes to the two levels of the government by name and/or in substances. It is also added that income taxes are mentioned by their specific names and that power of taxation in relation to a new income tax should be exercised after the decision pursuant to Article 99 of the Constitution. Furthermore, as it can be observed from the Constitution, certain powers of taxation are expressed by mentioning the tax families.⁷⁷ For the tax bases stated in the form of general tax families in the Constitution, the government with the power of taxation over that tax family will have the same power over the specific taxes within the tax family. The Constitution deliberately assigns certain tax families in a beta way. Had it not been the intention of the Constitution to permit a tier of the government to have a power over specific taxes within a tax family, it would have specified the taxes by name like what it does for income taxes.⁷⁸

Having said the above, it is essential to briefly discuss as to what kinds of taxes are provided under the Constitution in the form of tax family or/and by substances. In this regard, it is good to first read Article 96(1) of the Constitution which states that “The federal government shall levy and collect custom duties, *taxes* and other charges on imports and exports.” [Italics added]. Article 96(1) gives the power to the federal government to levy ‘*taxes.....on import and exports*’ without mentioning the specific type of the import and export taxes. In other words, each and every kind of tax the federal government may impose cannot surely be known since the Constitution simply states “*taxes on import and export*”.

Unlike income taxes, the Constitution does not make specification on taxes on import and export in the above provision. In such cases, the federal government can levy specific types of import/export taxes which are not actually named in the Constitution as long as they can fall within the frame of the substances (taxes on import and export). Hence, the federal government does not need to get the blessing of the two houses because such taxes are not regarded as unassigned taxes. It is for this reason that the federal government imposes surtax on imported goods though it is not mentioned under the Constitution by name.⁷⁹

The other tax base which is assigned in the form of tax family in the FDRE Constitution is the *sales taxes*. Unlike income taxes, the Constitution does not make a specification on the ‘*sales tax family*’. With regard to sales taxes, the Constitution has assigned to both levels of the government on ownership principle, domiciliation principle and type of business form/structure, without breaking down the tax family into various slices. The Constitution, for instance, provides that “states shall levy and collect *sales taxes* on enterprises owned by the States”. Unlike income tax family, it does not break down the sales tax family like into retail, wholesale, manufacture’s

⁷⁷ For example, taxes on import and export, sales taxes. See the FDRE CONSTITUTION, Art 96-98.

⁷⁸ Here, given the general nature of constitutions, one cannot surprise himself by the position taken by the FDRE Constitution.

⁷⁹ *Import Sur-Tax Council of Ministers Regulations*, Regulations No. 133/2007, 13th Year No. 23, Addis Ababa, 11th April 2007.

sales tax, turnover tax and VAT. As shown above, this model of assignment of the constitution is similar with the form adopted by Indian constitution.

As a supreme law, the Constitution may not do this simply without taking into consideration the situations that existed at the time of drafting and the social, political and economic factors in the making up of the federation.

It may not be tenable to say that the Constitution does not break down the sales tax into its members because the framers of the Constitution did not know the fact that sales taxes have varieties.⁸⁰ It could be presumed that Ethiopian scholars at the time of drafting the Constitution had knowledge of the varieties. As of 1954, the time Ethiopia introduced the first general sales tax, the country has been introducing different varieties of sales tax.⁸¹ Accordingly, from general sales tax, Ethiopia has introduced manufacturer's sales tax in 1956.⁸² Besides, the country introduced turn over tax upon all sales at all levels in 1963.⁸³ These forms of sales tax were popular forms of sales tax for the Ethiopian government in the 1970s, 80s and early 90s. Thus, the fact that sales tax has different varieties like that of income tax was known in Ethiopia long before the promulgation of the FDRE Constitution in 1995. Even after the FDRE government came to power, manufacturer's sales tax and turn over tax as types of sales tax were administered in Ethiopia although the government eliminated turn over tax from the sales tax regime in the 1993 tax reform.⁸⁴ Hence, it can be fairly argued that the framers of the Constitution knew that sales taxes have various slices.

As it can be inferred from the 1993 sales and excise taxes laws, the transitional government had decided to have a single-stage sales tax regime with application upon imports, goods manufactured locally and a limited number of services at that time.⁸⁵ The consideration that the 1993 sales tax regime was "a single stage sales tax" and the fact that turn over tax was eliminated may tell us that the intention of the transitional government, influential in making the Constitution, was to have a single stage sales tax than the various varieties of sales tax. Based on this, it may be argued that the Constitution refers to the single-stage sales tax recognized in the 1993 Sales and Excise Taxes Proclamation when it talks about 'sales taxes'. It then means that power of taxation over new varieties of sales taxes shall be determined in accordance with Article 99 of the Constitution. This argument could not, however, be accepted at least for three reasons.

First, in stating sales taxes, the Constitution uses '*sales taxes*', not "sales tax" in a singular form.⁸⁶ Hence, the fact that sales taxes contain more than one variety was known to the framers of the Constitution. Second, the Constitution would have put a fencing clause stating that other

⁸⁰ The fact that the family of sales tax has different varieties was known long time ago. Even VAT as a form of sales taxes has been spreading throughout the world since its introduction in 1954.

⁸¹ Taddese, *Towards Legislative History of Modern Taxes in Ethiopia (1941-2008)*, XXV (2) JOURNAL OF ETHIOPIAN LAW, at 138 (2012).

⁸² *Id.*, at 137.

⁸³ *Id.*, at 138.

⁸⁴ The Sales and Excise Tax Proclamation No 68/1993, FED. NEGARIT GAZZETA 52nd Year No.61, Addis Ababa.

⁸⁵ *Id.*

⁸⁶ See FDRE CONSTITUTION, Arts. 96(3), 97(4, 7), 98(1), and 98(2, the Amharic version).

varieties of sales taxes shall not be introduced had it assumed that there is only a single sales tax. Unless the Constitution has fenced it, problems such as the constitutional status of VAT would inevitably arise. Third, as pieces of literature have indicated, the reasons for the late introduction of sales tax, for elimination and addition of sales tax varieties were associated with the tax administration capacity of the country.⁸⁷ Corresponding to this, Taddese stated that subsequent amendments of Ethiopian sales tax laws predictably widened the coverage of sales taxes as the tax administration became more confident in its enforcement capacities.⁸⁸

In conclusion, the framers of the Constitution had recognized the existence of varieties of sales tax and had knowingly put the power of taxation in terms of tax family.⁸⁹ In view of that, it can be understood that the Constitution has assigned all forms of sales tax with the knowledge and after close examination of each form of sales tax. So, for economy of words (especially it matters in constitutions), it has preferred to put in a broad way. Thus, as sales tax is not apportioned into smaller pieces, it means that VAT, as a tax base within sales taxes, is entrusted to the government to which that respective sales tax is allocated for the following reasons. First, the Constitution deliberately puts such kinds of allocation of taxation as discussed above. Second, if, for example, the Constitution had not intended the regions to have power over VAT within the sales tax family, it would have specified like what it has done regarding income taxes.

On the basis of the aforementioned discussion, we can therefore conclude that the Constitutional status of VAT in Ethiopia is a designated tax base as a family of sales taxes. Hence, both levels of government can levy VAT over areas where they are given the power to levy sales taxes.⁹⁰ Accordingly, the federal government has exclusive power to levy VAT on enterprises it has owned.⁹¹ Likewise, states have an exclusive power to levy VAT on individual traders carrying out a business within their territory and enterprises owned by the States.⁹² Moreover, both tiers of governments have also concurrent power over VAT to be collected from enterprises jointly established by the federal and state governments and on companies.⁹³ In respect of VAT, the rationales for bestowing competence over it to regions could be related to the second generation theory of tax assignment that inserts other noneconomic elements such as accountability, administrative feasibility and tax autonomy of regions.⁹⁴

⁸⁷ Taddese, *supra* note 81, at 137- 138.

⁸⁸ *Id.*, at 138.

⁸⁹ Accordingly, it is presumed the framers knew that VAT and turnover tax are forms of sales tax, but they preferred to entrust “a sales tax as a family” to the levels of the government in their respective competence as shared power.

⁹⁰ It is the “separate VATs or dual VAT” concept whereby both levels of the government collect the VAT independently on a separate economic base as per the powers defined in the constitution. In this case, both tiers retain autonomy in fixing tax rates, exemptions and administrative procedures.

⁹¹ FDRE CONSTITUTION, Art. 96(3).

⁹² *Id.*, Art. 97(4,7).

⁹³ *Id.*, Art. 98(1) and art 98(2) of the Amharic version).

⁹⁴ Alene and Ayele, *supra* note 12, at 124 and 126.

Nevertheless, in practice, it is the federal government that takes the legislative competence on all sources of VAT in the country leading to a single national VAT in Ethiopia.⁹⁵ Accordingly, there is a federal VAT law which regulates the exclusive VAT sources of regions and the central government, and the concurrent sources of VAT. Thus, the federal government takes away the powers of states given under the Constitution which makes the federal VAT law unconstitutional. In fact, the federal government has assumed power on the basis of erroneous appreciation and decision of the Federal Houses pertaining to VAT as undesignated and their decision to give the power to the federal government.⁹⁶

Be the above as it may, close examination of the scope of the VAT proclamation may give rise to certain undesignated VAT sources. Currently, as already said, the federal government levies VAT generally on taxable supplies of goods and services.⁹⁷ As per the VAT Proclamation, save for the exempted supplies, VAT is applied on every taxable transaction or activity (of goods and services) so long as the supply is made as a commercial activity.⁹⁸ Nevertheless, every taxable activity is not necessarily a sale,⁹⁹ and it can be observed from the VAT Proclamation that VAT is also collected from supplies which are not sale. By virtue of the law, supply of services rendered as part of commercial activities is subject to VAT.¹⁰⁰ For example, VAT is collected on rental of buildings in Ethiopia. In such cases, the VAT is not collected from sales, but from leasing activities or supplies of services. However, the constitutional base for levying VAT on supplies other than sales would be another question in the Ethiopian VAT system. Arguably, unlike other quarrelsome areas, levying VAT on non-sale activities does not have a constitutional base. As a result, the competency of the federal government in this regard is dubious from the constitutional point of view.

⁹⁵ Practically, the model of VAT assignment in Ethiopia is Federal VAT with Tax Sharing. The VAT is collected at the federal level and shared with the regional governments based on a formula.

⁹⁶ Minutes of the 1st Joint Session of the House of Federation and the House of Peoples Representatives (Meskerem 26, 1996 E.C. in Amharic), *supra* note, 74.

⁹⁷ The Value Added Tax Proclamation, Art 7. As per the VAT proclamation, taxable supply means any supply of goods or services by a person registered for Value Added Tax which is not an exempt supply. Hence, irrespective of the character of sale, supplies are going to be subject to VAT as long as the supply is made as a commercial activity. This can be understood from the cumulative reading of Articles 2(17), 6 and 7 of the VAT proclamation.

⁹⁸ The Value Added Tax Proclamation, Arts. 6 and 7(3).

⁹⁹ For example, a legal dictionary defines that sale is a transaction, contract or an agreement by which one of the contracting parties, called the seller, gives a thing and passes the title to it, in exchange for a certain price in current money, to the other party, who is called the buyer or purchaser, who, on his part, agrees to pay such price. *A Law Dictionary, Adapted to the Constitution and Laws of the United States. By John Bouvier.* (1856), available at <https://legal-dictionary.thefreedictionary.com/sale>, (Accessed on 8 August 2019). Similarly, Merriam-Webster Dictionary defines sale as the act of the transfer of ownership of and title to property from one person to another for a price, available at <https://www.merriam-webster.com/dictionary/>, (Accessed on 8 August 2019). As can be understood from different dictionaries, sale involves the transfer of title from the seller to the buyer. Therefore, while the law says sales tax, it is to mean sale transaction in proper sense of the term. Similarly, in Ethiopia, sale is defined as ‘a contract whereby one of the parties, the seller, undertakes to deliver a thing and transfer its ownership to another party, the buyer, in consideration of a price expressed in money which the buyer undertakes to pay him’; See CIVIL CODE OF THE EMPIRE OF ETHIOPIA, Proclamation No 165/1960, NEGARIT GAZETA, 19th Year No. 2, 5th May 1960, Addis Ababa, Art 2266).

¹⁰⁰ Value Added Tax proclamation, Arts. 6, 7(1) and 7(3), See also *supra* note 11.

VI. CONCLUSION

The FDRE Constitution has assigned power of taxation to the tiers of the government upon different methods and principles. In the assignment of taxes, the Constitution breaks down certain tax families (such as income tax) into pieces and it allocates them to the tiers of the government by specific tax names. In such cases, assigning a new tax of a tax family to the layers of the government by way of interpreting the constitutional provisions would not be easy. The only possibility would be an assignment through Article 99 of the Constitution. On the other hand, the Constitution assigns some taxes in the form of tax families without naming specific varieties within them. An example in this respect is *sales tax* in which the VAT, as a variety, is the major one. Since the FDRE Constitution assigns sales taxes in the form of a tax family, it does not mention VAT by name. Attributed to this, it is identified that there are arguments regarding the constitutional status of VAT.

Despite the arguments, this paper revealed that the Constitution has broadly assigned the grand sales taxes with the knowledge of the varieties within them. This means that the Constitution has assigned VAT in substance like the case of Indian constitution. Moreover, the assignment of VAT in the Constitution can be inferred from cases other than a sales tax form. In this regard, Article 96(1) of the Constitution that empowers the federal government to levy “*taxes on imports*”, without any further qualification, can be mentioned. Accordingly, the FDRE Constitution adopts the dual VAT, where the two levels of government collect VAT independently, and joint VAT system of assignment. Both levels of the government are given the power to administer VAT independently on a separate economic base and jointly from enterprises they jointly establish and on companies.

Furthermore, it is noted in practice that VAT is not levied based solely on the constitutional provisions of sales tax. It is also administered on other non-sale taxable supplies that are not indicated in the Constitution. Based on this, it can be argued that the VAT proclamation is unconstitutional to the extent that it imposes VAT on activities other than sale transactions. The practice also tells us that the federal government takes away the constitutional power of states upon sales taxes or/and VAT though the federal government apportioned VAT proceeds to regions.¹⁰¹ Since the Constitution needs to be respected, states shall be allowed to levy VAT over areas where they have the constitutional power to levy sales taxes. If there can be any justifiable reason to give such power to the federal government alone, it shall only be done through a constitutional amendment. Article 99 of the Constitution should also be triggered in relation to VAT on non-sale activities/supplies because power of taxation needs a clear constitutional support.

* * * * *

¹⁰¹ HoF, 1989 E.C 2nd Regular Meeting minute, at 76-80; (as quoted in Ghebrehiwet, *supra* note 8, at 232.)

