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The Effect of Contraband on Government Revenue: Case of Segen Area People's Zone

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Abstract- The main objective of this study was to assess the effect of contraband on government revenue of Segen Area People Zone. The study was descriptive used only primary data from revenue authority employees and contraband business operators through structured questionnaires. The targeted respondents were selected using simple random sampling and judgmental sampling technique. The collected data were analyzed statistically with statistical software. The result of the study shows that the motivating factors were lack of formal income, lack of job and the demand and supply gap in formal operation. The finding also reveals that contraband undermines the government revenue, increases the tax burden on formal business operators and may remove them from official system in to informal nontax paying system. Moreover; it kills the need of the investments and innovations in the country, wipes out foreign currency that a country may earn from legal import export and creates unfair competition in the market. The process of controlling contraband faces a great challenge like a bribe, insufficient skilled and competent manpower, lack of ongoing training, low salary of the workers, corruption, inadequate enforcement and penalties and ineffective respond to tax evasion in the area. Accordingly; to mitigate contraband, the government should raise domestic innovations, manufacturing and human resource capacity development, strengthen strong enforcement of the rules and punishments, and even create a conducive environment for effective coordination and communication among controlling unit and the general public.

Keywords: *contraband, government revenue, illicit business, smuggling.*

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THEEFFECTOFCONTRABANDONGOVERNMENTREVENUECASEOFSEGENAREAPEOPLESZONE

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1. Introduction

1.1 Background of the Study

Globalization is an engine for economic growth and significantly enhances trading activities. It also boosts opportunities for informal business operators in informal economies creating a multi-dimensional challenge for the administration. Informal economy comprises those economic activities that circumvent costs and excluded from the benefits and rights incorporated in administrative rules and regulations. It is part of an economy that is not taxed, monitored by any form of government or included in any gross national product (GNP).

Illicit trading activities across a border such as contraband are invasive socio-economic perils deep-rooted in the global trading system. Their syndicates are drawn by huge profits while benefiting from weak legislation. Enforcement agencies face the formidable task of facilitating the flow of legal trade while dismantling organizations involved in smuggling operations. Smugglings dampen the economy in multidimensional ways. It destabilizes the legal industry, restrains innovation and investments, reduces government revenues, fuels transnational organized crime and hampers the health and safety of consumers (FICCI, 2016).

Ethiopia is a landlocked country and experienced strong, broad-based growth averaging 10.5% a year from 2005/06 to 2015/16, compared to a regional average of 5.4% (World Bank, 2017). This growth brought with it positive trends in poverty reduction in both urban and rural areas. Despite this marvelous change; the tax revenue collection performance of the country is lowest compared to an average tax collection performance of sub-Saharan African countries, (Alemayehu, 2015) and even below its neighboring countries (Tilahun, 2014 cited in Workineh, 2016). This low performance is an indication of illicit trade activities outside the formal business activities who evade and avoid tax revenue from government. The products on such illicit trading activities are smuggled goods which have no official entry point in the country, do not have customs document or prior approval to enter into or depart from the country. The agents involved in these activities violate the law that govern the import and export procedure and thus avoid the payment of all applicable taxes for the importation or exportation of goods.

1.2 Statement of the Problem

Products crossing a border in to or out of the country illegally are informal transactions. They remain a great challenge for countries in generating tax revenue for long periods of time. They expand the evader's potential of evading tax revenue from government treasury and disappoint those who operate in legal economy forcing them to shift their activities to illegal markets. Moreover; they kill micro small and medium business enterprises growth shutting their market by providing forbidden and quality products produced with advanced technologies at a low price. By removing revenue from government and demolishing the growth of micro small and medium enterprises, the contrabandist puts the economy of the country at risk.

These contraband activity most of the time typifies developing and underdeveloped nations which are characterized by high manpower, lower per capital

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income and the biggest portion of the economy leading the life by cultivation. These nations have no well-established infrastructures; agriculture covering the largest percentage of GDP and industries that produce products with poor qualities. They are also subject to foreign cultures invasion and dominance of the youngest people losing their identity. Consequently; the individuals in these countries are forced to participate in illegal activities as an agent or direct for themselves.

In Ethiopia, contraband is not a recent phenomenon but existed long periods ago. Since then smugglers did not hesitate to smuggle goods into and out of Ethiopia, and they are still doing it in spite of all laws and regulations[1]. They smuggled products like electronics and electrical goods, garments of various kinds, perfumes, cosmetics, habit-forming drugs, armaments, and others. The products are smuggled from countries like Sudan, Eritrea, Kenya, and Djibouti (Zemzem and Teklu, 2017). These neighboring countries knowingly allow their border for such products to cross Ethiopia to raise illegal activities in the country that will jeopardize the economy of the country at any time.

Thus, it is against the problems stated above that this study tries to investigate the effect that products crossing the border and entering the country unlawfully through Moyale have on the revenue of the Segen area peoples zone tax authority.

In line with the above-stated research problem, the study will answer the following research questions:

- Why do individuals involve themselves in contraband activities?
- What are the effects of these activities on government revenue?
- What are the measures taken or planned to be taken against activities?

1.3 Objectives of the Study

1.3.1 General Objective

The general objective of this study is to investigate the effect of contraband on government tax revenue of Segen Area Peoples' Zone.

1.3.2 Specific Objectives

- To assess the reasons why individuals engage themselves in contraband activities.
- To assess the effect of this activity on government revenue of the area and
- To examine the measures taken and planned to be taken against the activity.

1.4 Scope and Limitation

Segen area people zone consists of five Woredas namely Konso, Dirashe, Burjy, Amaharo and Ali. These Woredas are near one another and located in southern region of the country bordering the region with Oromia region. However, the contraband or smuggled products largely enter the area from Oromia region Moyal to Konso and then distributed to the rest of Zone Woredas and other parts of the region and country at large. Thus this study concentrates on Segen Area People's Zone because of the time and cost that it takes to cover the entire country. The targeted business operators also exist outside the formal system, so the owners may refuse to participate and fill the questionnaires appropriately.

1.5 The Significance of the Study

This study focuses on the effect of contraband which is an illegal activity undertaken against government revenue and the economy at large. So this will have the following benefits:

- It can help tax authority to establish ways that will help them to eradicate if possible or reduce contraband and enhance its tax revenue potential.
- It can also help the government to establish a policy that will reduce the level of informal economy in the country.
- It can also act as a stepping stone for other research on the same area.

1.6 Organization of the Paper

This study is concerned with contraband in Segen Area Peoples' Zone and will have five parts. The first part is about the introduction and incorporates background, statement of the problem, objectives, scope and limitation, significance and organization of the paper. The second section was about the literature review related to the study followed by methods used to collect data, select sample and analysis of the collected data. The fourth section presents data analysis and discussion and the fifth section of the study then concludes the study.

2. Review of Literature

2.1 Contraband and its Meaning

Products produced in or outside a country cross a border to abroad or into the country from outside in two ways. In the first case legally by those who have legal license to do it and pays tax for the government on the income generated from such transactions. They deal with products that are allowed to be imported or exported by rules and regulation of the country and support the economy of that country. On the other hand, there are people who engage themselves in activities that contradict the legal system of the country. They had no state-issued permits, license or registration and did not pay tax on the products. Moreover; the products being imported or exported may be forbidden legally because of the effect that they may have on the socioeconomic and political system of the country. In general word, the products entering or leaving the country in such a way are named as contrabands.

[1] www.erca.gov.et/index.php/customs/org

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The word contraband refers to property that is illegal to possess or transport and may be goods that are illegal to import or export and are attempted to be smuggled into a country. Contraband goods are usually subject to seizure by government officials (https://definitions.uslegal.com/c/contraband). The products have no official entry point, do not have customs document or prior approval to enter into or depart from a country so, they violate the law that governs the import /export procedure and thus avoid the payment of all applicable taxes for the importation or exportation of goods (www.erca.gov.et/index.php/customs/org) and has harmful effect on the socioeconomic development of a country.

In Ethiopia, this contraband enters the country in different directions from neighboring countries namely Kenya, Sudan, Eritrea, Djibouti, and Somalia. The operator brings the products on foot, pack animals, Motor Vehicle and Cars that gives transport service to the public. Moreover, the public office cars that are provided by the government to officials for office purposes like ambulances and those cars that carry oils and gas from the center to different areas of the country also participate in supporting in such evil activities. Some are trafficked hidden within areas such as automobile tires, doors, fenders, bumpers, fuel tanks, and in other secret compartments of trucks, and trains.

Even more; some contraband goods are occasionally smuggled into and out of the country stuck in containers with other legal shipments allowed to be imported or exported after fulfilling customs formality. Drivers of trucks which transport legal shipments stop their vehicle en route and load illegal goods in to the container of legal products. Smugglers are also assisted by some dishonest customs officers at check points and local security forces. Smugglers bribe them and enter or take their goods into or out of the country illegally.

To convey their goods, smugglers cross the land borders of the country and use routes that are not under the control of the federal police. The large part of the Ethiopian border encompasses extensive lowland areas[2] which are difficult to fully control by the federal police. As a result, smugglers can easily cross the border with their substantial smuggled goods. The smugglers, experienced in running contraband goods and adept at traversing the country's border, are canny in looking for other devious routes when their way was blocked by federal policemen. They are also violent enough to intimidate or kill anyone standing in their way. As a result, many elements of the Ethiopian law enforcement community have lost their priceless lives in the fight against smugglers. Using the above mentioned devious devices/methods, smugglers deliver contraband goods to their secret stores and make them available for selling and distribution.

[2] www.erca.gov.et/index.php/customs/o

2.2 *Determinants of Contraband*

Some of illicit transactions may be carried out across a border between countries by illegal traders or by licensed business owners whose aim was to escape government tax. This was the problem for all countries across a globe for an extensive period of times and still exists regardless of the measures developed and taken by governments. However; what remained an answered by academicians, government and even international organizations was, why do people engage themselves in such illegal activities given its existence outside government control?

People participate in contraband activities directly by themselves or assign agents that will act on behalf of them for commission base. They are motivated by various factors may be to avoid taxes and to secure illegal competitive advantage, to avoid customs checkpoints where goods and their documents are examined, to make a living and to escape from the unemployment prevailed in the country (www.erca.gov.et/index.php/customs/org). Others involved in the contraband trade as acts of political defiance. Irresponsible and anti-peace elements may smuggle guns and hand grenades into the country to commit a crime, to damage public infrastructure and to create political instability in the country or to cause an atmosphere of social unrest. Moreover; consumer's willingness to buy goods on the black market is the other factor that drives smugglers (www.erca.gov.et/index.php/customs/org). Smuggled goods are sold at a low price and this has made thousands of poor people prefer to buy smuggled products than legally imported goods. External factors like political instability, social unrest and economic crisis in the neighboring countries may also contribute to the expansion of contraband trade in a given country.

In many parts of the world, the import and export policies usually consider the effect that the products may have on the economy of the country. Accordingly, there are products which are allowed by the import/export policy of the country and also prohibited even if the demand for the products exists in that country taking in to account their effects. In such cases, prohibitions effectively prevent trading in forbidden products on the legal market, but these products continue to be desired, wanted and insisted by consumers. So the absence of legal supply leaves plenty of opportunities for contraband supply to substitute for it. Lack of legal supply to meet this demand for prohibited products (demand gap) may force individuals to engage themselves in illicit activities.

The level of tax burden also plays great role in the economy in expanding the market of contrabandists. Business peoples may join refusing the level tax they are being charged by the government. A well-established tax system considers the ability to pay for the people and also have a pivotal role in inspiring micro small and

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medium business enterprises in the economy. However; many countries mainly developing countries charges their peoples without ability consideration to meet the level of tax they have aimed to collect in that fiscal year. They may do this by increasing tax rate or forcefully incorporate the business into tax net. Thus, this moves the business peoples to smuggling creating higher tax evasion in that country. Several studies by Bhagwati, (1964); Fisman and Wei, (2004); Mishra, (2008) and Buehn and Farzanegan (2011), pointed out that tax rate is vital to push factors for smuggling.

Moreover; effective law enforcement in the nation is a fundamental element in keeping the people in that tax system and reduce illegal acts. A country that has fine law enforcement experiences less illicit activities. A significant measure for lack of a successful enforcement mechanism is the number of policemen per a population and level of investment in technology and training that support surveillance, which enables proactive and effective enforcement actions possible. The costs of smuggling depend on the probability of being caught and punished by the authorities, so intensifying enforcement increases the costs of smuggling in the form of punishment, confiscation, and detection (Martin and Panagariya, 1984). The study shows a significant negative correlation between effective enforcement and smuggling (Buehn and Farzanegan, 2011). Low risk of the law enforcement with profitability from tax evasion from smuggling enhances the motivation for the illegal act of smuggling.

Countries with low innovations and lower level of technology of the domestic industries to produce new products that contend smuggled products in quality and price may experience a higher number of peoples involved in contraband activities. The imported products illegally satisfy the needs of the consumers with emerging technologies, new products with better quality and performance (Bakhtiyari & Salarzaei, 2016). Smuggling of imported goods expands due to enhanced public demand. Ambition value of imported goods with the perceived better quality compared to domestic commodities, coupled with enhances purchasing power tends to provide impetus to smuggling. Findings of the subsequent section on the extent of smuggling show that weakness of domestic industry in producing quality machinery and electronic goods could be one of the causes for smuggling of imported goods.

2.3 *Effect of Contraband*

Regardless of different approaches to definitions of contraband, its effects are numerous and economically significant. It is a serious problem and its impact is far-reaching, affecting various stakeholders including Government, domestic industries and citizens of the country. Most customs, border and law enforcement officials, policymakers, and academicians agree that illegal trans-border trading results in major financial and social costs to economy, and society (FICCI, 2016).

2.3.1 *A Loss of Government Revenues*

The smuggling of goods or products can be considered as one of the tax violations that attack a country's tax system. It dampens legal imports and drastically decreases the volume of revenues collected from various duties and levies by state agencies. Customs duty forms a significant part of the Central Government revenues, which shows a decreasing trend over the past few years (FICCI, 2016).

Illegal trade in contraband products deprives government tax revenue because the product crosses the border illegally without payment of tax. When goods are conveyed secretly or illicitly into or out of the country without the payment of customs duty and taxes, the government loses much revenue (www.erca.gov.et/index.php/customs/org). The eventual outcome of the revenue lost is that it hampers development programs. Therefore to make the development programs feasible and to finance them, the government may be forced to increase taxes or adjust other sources of income. The burden of covering these shortages falls on honest taxpayers who in turn lead to higher prices of commodities which in turn can contribute for the growth of black-markets or as the tax increase drive up the price of domestically produced and imported goods, many consumers seek lower-priced products through a variety of alternative venues and channels, many of which are illegal. (www.erca.gov.et/index.php/customs/org).

The main objective of taxation is to reduce the income inequality among the people usually using progressive tax system. Through this tax system, high-income earners pay accordingly and the poor as well. However, contraband business violates this and amplifies income disparity or the earnings gap between the rich and poor. They are the main parts of the group who are recognized legally in evading government revenue. The products entering or parting the country by these illicit traders are hidden from the view of government and are sold surreptitiously. They use the poor on a little compensation to carry the smuggled products on foot or other means from the border to their store. They accumulate the wealth while the living standards for many stagnate because they are not paying as formal business peoples.

2.3.2 *Impact on Domestic Industries and Innovations*

The flow of contraband products into a country weakens local industries by distorting the prices of the products. These illegal, illicit traders well know by the act of providing the products at chipper prices which will disappoint and may also remove local producers from the market. Their intension was evading and avoiding tax and regulation, so their chip price may result in the breakdown of domestic industries or force domestic producers into bankruptcies.

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Micro Small and Medium enterprises are the principal employment generators and exert a strong influence on the economies of all countries. They are the fertile sectors regarding of innovations and quick remedy for unemployment and also increases tax revenue for the government. Moreover; they are the backbone of every economy in raising the economy through the enhancement of import and export of the country. However; contraband operators remained the main hindrance for these entrepreneurs by providing quality products produced by advanced technologies at lower prices. By doing this, they downsize domestic entrepreneurs development and expansions.

Innovation in the form of the conception of new ideas for the development of new products or processes and experimentation[3] has been recognized widely as an imperative driver of economic growth. Innovators protect their thoughts through patents, copyrights, design rights and trademarks. Without adequate protection of these intellectual property rights, the incentive to develop new ideas and goods is reduced, thereby weakening the innovation process. In industries where product development requires significant investment and innovation, smuggling of counterfeit product impairs investments and innovation by undermining the efforts of innovators and discouraging them from further research and development, which ultimately hampers overall growth of the economy.

2.3.3 Threat to Society

Smugglers involved in clandestine activities also pose a serious threat to society. It affects the internal structure of a society by creating powerful illegal institutions (Dominguez, 1975). It expands the black market and increases convergence between organized crime, terrorist groups and other threat networks available at (http://www.state.gov/documents/organization/250513.pdf). Smugglers and their system outwit the national borders imposing security threat and earnings from this illegal activity may be used finance insecurity that increases the policing costs (Burke, 2013).

Antisocial behavior is conduct that disrupts society or displays disdain or hostility to it. For instance, committing a crime is antisocial manners. Such kind of behavior can be intensified in society by the body of persons who used smuggled in weapons for violence activities calculated to cause death, robbery, burglary, rape and other crimes. Therefore smuggling armaments into the country weakens the struggle to maintain peace and order in the society available at (www.erca.gov.et/indexphp/ customs/ others/101contraband).

2.3.4 A Negative Effect on the Economy

Monetary costs arise from smuggling due to evasion of taxes and tariffs. Smugglers are extra burden for government budget by evading legal duties and taxes/tariffs. A developing country relies more on indirect taxes as compared to direct taxes and low indirect tax collections may have harmful consequences for the government's ability to provide public goods. The provision of public goods increases the productivity of economy (Loayza, 1996), and thus not creating such public products has a harmful effect on productivity, development, and economic growth (Norton, 1988).

Smuggling may have a negative effect on official indicators such as growth and income distribution. It involves bribery and other forms of corruption and tends to promote criminal behavior in the economy (www.ficci.in/spdocument/20807/final). Smuggling may result in mass fall-down in domestic companies who are unable to counter cheap imports, leading to surging in unemployment in the country.

2.3.5 Health and Safety Risks

A contraband operator also carries products that are risky for society. They deal with prohibited goods like narcotics and illicit tobacco which are the serious threat to the life of many citizens of the country (WEF, 2012). And pornography materials which display genitals and show sex acts in an offensive way, thereby eroding the moral values of the society. Even although the legal system of the countries prohibit the importation such products, they are entering the border increasingly with the increasing number of users.

Habit–forming dangerous drugs debase/ demoralize the moral senses of the youth and others who take illegal drugs for pleasure or because of addiction and it also cause them a wave of sickness when they are unable to continue captivating it. The poor quality smuggled goods can produce health problem in the society. In their attempt to control drug trafficking, federal policemen catch people and travelers who bring illegal drugs into the country (www.erca.gov.et/index.php/ customs/org).

2.4 Measures Against Contraband

Cross-border trade below the radar of government oversight is both a boon, and a curse for many African economies (www.ictsd.org/bridges-news/bridges). However; in many countries particularly Africa the cost of contraband or informal cross-border trade outweighs the benefit because of this governments are standing against this activities. They frame some of measures that they think will reduce or eradicate contraband and other illegal cross border trades and in turn enhance domestic production.

Informal cross-border trade touches everybody in the community. So the prevention of contraband needs a wide range of actors including government, both regional and local administrators, and the society at large. The government by itself cannot stop informal trades, so should work together with the community where the contrabandist were located and conceal their

[3] www.ficci.in/spdocument/20807/final.

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products after crossing the border. The Ethiopian government has established a new strategy against contraband and based on this strategy the government has disbanded customs police, the former agent responsible to prevent contraband, and replaced it by the federal police as of July 2008. In addition to this, the government has amended customs and tax laws. This amendment has helped to streamline taxation procedure and to empower the federal police for prevent contraband (www.erca.gov.et/index.php/customs/o). However; federal police only can't carry the burden of averting contraband alone, so they need to work with regional and local administrators, and the community. As a result of the active participation of them in fighting against contraband, the volume of smuggled goods that enter for example into Diredawa via Shinile Zone has decreased (Paper on strategy to prevent contraband, 2009).

Information and knowledge gap usually are bases of failing for many individuals, entrepreneurs, and companies. Having awareness and information about the advantage and disadvantages of something gives a clue to accept or reject it. Enlightening the general public and creating awareness about the effects of contraband on the economy of a given country plays a vast role in challenging the increasing informal cross-border trade activities. Contrabandists usually use the harsh economic and financial condition of the public and use them to carry illegal products from the border through challenging ways using motorbikes, animals and human back particularly females or hide the contraband from government officials. They are doing this because of poor understanding about contraband and abet for contrabandists even and abuse the government officials assuming that officials are blocking the business of the people. Therefore, providing education is necessary to infuse into the hearts and minds of citizens the necessity for proper respect traditional law and to let them stand against contraband. Educating the society about the proclamations, regulations, directives and operational systems of customs using various media and customs website awakens the people to stand up for their country.

Also; to reduce the size of smuggling in the country it is necessary to strengthen the deterrence mechanism for committing the crime. In Ethiopia, sub article 1 of article 92 stipulated in proclamation no.622/2009 any person who, in contravention of this proclamation or the other laws enforced by ERCA, including regulations and directives issued there under, imports or exports prohibited or restricted goods or without customs clearance or illegally imports dully exported goods, without prejudice to the forfeiture of the goods and equipments used in the commission of the offence and the proceeds thereof, be punishable with fine equivalent to the amount of the customs duties and taxes payable on the goods and with rigorous imprisonment from 7 to 15 years (Customs Proclamations No.622/2009)[4]. According to sub article 2 of the same article, any person who transports, stores, offers for sale or buys goods referred to in sub article 1 of this article while being or ought to have been aware of the illegality of their acquisition shall without prejudice to the forfeiture of the goods and equipments used in the commission of the offence and the proceeds thereof without affecting the right of third parties who transacted in good faith, be punishable with a fine equivalent to the amount of the customs duties and taxes payable on the goods and with rigorous imprisonment from 7 to 15 years. According to sub-article 3 of article 92 stipulated in proclamation 622/2009, where the offense is committed by the use of force or by an organized group with the offender of the punishment shall be, without prejudice to the forfeiture of the goods seized and fine from 15 to 20 years, rigorous imprisonment.

The other approach connected with the strategy to prevent contraband is allowing border trade. By making border trade with the neighboring countries: Somalia, Sudan, Kenya and Djibouti, the government has tried to collect taxes. The border trade has been carried out by the directives issued in 2000 and 2001 by the Ministry of Trade and Industries. The objectives of the border trade are to let the residents in the border area fulfill their demand for consumption goods, to let them use border trade as a means of securing the necessities of life, to decrease the activities of contraband and to promote legal trade. By opening the door to border trade, the government anticipates some smugglers will abandon their vicious practice and turn into productive citizens of the country. Export items for border trade are typically consisted of a pulse, livestock such as goats, sheep, camel, and others. Import items are mainly food items, clothing that are usually dressed by the residents of the border area.

Moreover; the simplification of the procedures and creation of a system which allows fewer contacts between the staff and the traders was implemented by some countries, while others upgraded information technology system and even introduced custom software to improve service delivery, increase transparency and shorten customs clearance time. In their reforms, Countries like Uganda and Peru on the other hand employed measures such as cooperation with other authorities, private entities and police, expanded audits and preventative inspections to increase enforcement. Though these efforts may have reduced the clearance time, increased seizures (especially in Mozambique) and a decline in smuggling, corruption is still high (especially in developing countries), which compromises these efforts.

The World Bank findings show that political support for customs reforms is essential, together with

[4] Proclamations No.622/2009, Customs Proclamation.

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stable leadership. Financial support is also a very important ingredient in ensuring successful restructuring. Also, the cooperation of customs staff, taxpayers, and coordination with other tax agencies is critical for effective customs reform (World Bank, 2005).

The literature furthermore points several initiatives that may help to combat illicit trade, including:

- Exchange and joint analysis of statistics of general trends of the risks and seizure of illegal and undeclared goods.
- Enhance cooperation between Customs and different players in the economy, including other law enforcement agencies, to help to better infiltrate and identify production and distribution networks for illegal and illicit trade.
- Exchange of knowledge and experience by customs officials regionally and internationally.
- Establish and designate as appropriate national coordination agencies or bodies and institutional infrastructure responsible for policy guidance, research and monitoring of efforts to prevent, combat and eradicate illicit trade.
- Introduce modernized systems, improved risk management practices, and implement audits of the custodians of regulatory controls.

One measure has been the establishment of simplified trade regimes, which simplify the rules and procedures for small traders and provide tax incentives for trading within the formal sector. Some countries cater expressly for the needs of small-scale traders at their borders, by providing information officers to assist with the correct procedures. Equally, these economic communities promote engagement with informal cross-border trade representatives, to ensure their needs are considered when policies and legislation are developed[5].

3. Research Methodology

3.1 Research Design

The study was descriptive, describing the effect of contraband on government revenue of Segen Area People's Zone. This is because it depicts the participants in accurately and allows insight into life experiences due to its unique approach.

3.2 Data Source and Collection Methods

The core objective of this study was to investigate the effect of contraband on government revenue of Segen Area people's zone. Contraband is informal business operating outside the formal rule and regulation and has no legal records, so it is difficult to measure the amount of revenue loosed by the government through contraband. An estimate made by different experts is used to know the extent of the contraband effect.

This study used only primary data obtained from revenue authority employees and contraband business operators. The study used only primary data because of the illegal nature of the area of investigation, lack of formal records about the revenues of the operators and actual revenue loss of government because of this informal business (contraband).

Primary data were collected through structured questionnaires that contain both open and closed-ended questions distributed to the employees and business operators. Also; Lickert scale was used to generate the perception of various study respondents on the magnitude of contraband. Secondary data were collected through reviewing written documents, articles and journals.

3.3 Sampling Design

The target population of this study was tax authority employees and formal business operators as well as those illicit traders. Segen Area Peoples Zone was composed of five Woredas (Konso, Dirashe, Amharo, Burji, and Ali). Accordingly, the study utilized all data obtained from the employees of the revenue authority and contraband business operators. The tax authority offices were located in Zone city and Zone center in addition to five Woredas.

Collecting enough data from the targeted population is essential for the realization of the research objectives and to arrive at the needed conclusion. The area of investigation lacks formal records about revenue and expense, operates outside the official system of operation and mysterious in number to select the representative sample for the study. Also; they may perceive divulging them for the government for punishment at the time the researcher met them and might refuse to give the data hence their business was informal by nature. Therefore; the researcher picked 50 contraband business operators using judgmental sampling technique considering the ability to fill the questionnaire properly, uniformity of their business and their objectives of preferring illegal business than formal business.

The total numbers of employees in revenue authority are known so; the researcher used simple random sampling. Currently, there are about 178 numbers of employees in the zone tax authority (35 in Konso, 31 in Amharo, 25 in Gidole, 15 in Ali, 22 in Burji, 16 in Segen city and 34 in Zone center). Using simple random sampling technique, the researcher took 75 numbers of employees (15 from Konso, Amharo and Zone city, 10 from Burji and Gidole. The remaining ten were from Ali and Segen city).

3.4 Data Analysis

After collecting all necessary data from respondents; they were examined for detection of

[5] https://www.trademarkea.com/news/east-africa-has-a-lesson-for-sadc-in-formalising-cross-border-trade/

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errors and omissions through careful scrutiny of the completed questionnaires and put into a limited number of categories. The data collected through questionnaire were quantifiable, so were organized systematically and analyzed statistically with statistical software (SPSS 20.0).

4. Data Analysis and Presentation

4.1 Demographic characteristics of the respondents

Table 1: Demographic Characteristics of Employees

		Frequency	Percent	Valid Percent	Cumulative Percent
Gender	Male	48	64	64	64
	Female	27	36	36	100
	Total	75	100	100	
Educational Level	Certificate	13	17.3	17.3	17.3
	Diploma	29	38.7	38.7	56
	BA	30	40	40	96
	Masters	3	4	4	100
	Total	75	100	100	
Field of Study	Accounting	31	41.3	41.3	41.3
	Management	27	36	36	77.3
	Economics	14	18.7	18.7	96
	Other	3	4	4	100
	Total	75	100	100	
Work Experience	less than 2 years	10	13.3	13.3	13.3
	2-5 years	34	45.3	45.3	58.7
	5-10 years	24	32	32	90.7
	Above 10 years	7	9.3	9.3	100
	Total	75	100	100	

Source: Survey (2018)

Table 1 above presents the demographic characteristics of the revenue authority employees used to collect data for the study. As was seen from the table, the majority of the participants were male and also diploma and first-degree holders. This has its own effect on contraband controlling process. Holding the high number of employees that have a lower educational level or completed their education through distance process will affect the revenue of the zone negatively. Not only can this but from the table one can also conclude that the majority of the selected employees were accountant and management field of study. More over; the table reveals that the selected employees have a work experience of between two to ten years.

4.2 Factors Motivating Peoples to Engage in Contraband

Contraband activities are illegal business activities violating the law of the country or performed against the rules and regulations that govern the export and import activities of the countries. Different methods are being designed to cut this illegal business, but instead of dimensioning it is raising and even attracting many young generations including those which are in formal business sectors. Individuals may be involved for the suck of their benefit or serve other on commission bases. The motivating factors are various among the participants like personal financial problems, increasing family responsibility or even lack of a formal job as a source of income and other. The following table presents the factors that motivate peoples to engage themselves in illegal business activities. Moreover; other joins it as a response to overly cumbersome, rigid, time-consuming and inefficient bureaucratic export/import procedures and regulations.

Table 2: Why are you Engaged in Contraband

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Lack of job	16	32.0	32.0	32.0
	Lack of capital to start up my own business	3	6.0	6.0	38.0
	Lack of formal source of income to meet my family responsibilities	21	42.0	42.0	80.0
	Demand-supply gap in formal system	10	20.0	20.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

As shown in Table 2 above, people are being forced by lack of formal income to meet their family responsibilities (42%). Rise in family number and expenses for consumption from time to time with

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decreasing or zero income pushes the family member into activities that will help them to get income for their families expenses particularly contraband. From the table, 32% stated that they are being motivated by lack of the job that will serve as a source of income. We are in situations where young generations stop their schools early because of family support or graduates wait for the hands of government all raising the level of the unemployment rate of the country. So this group has a high probability of participating in contraband activities. Moreover; the demand and supply gap in formal sectors also pushed individuals (20%) into informal sector (contraband). If the formal system cannot meet the demand of the people in the formal system, it is clear that that gap will be filled by informal sectors through products smuggled illegally into the country.

The respondents were also asked who has led them into contraband activities as shown in Table 3. The table reveals that the majority of the contrabandists were directed by their situations (64%) which may be lack of income, job or increasing family responsibility, and other personal problems. On the other hand friend initiation also plays a big role in moving individuals into contraband as was shown in the table (30%). By looking and comparing the revenue that the friend in illegal business sector is generating with the revenue that he/she is obtaining in formal business sector discourage them to leave that formal sector and join informal business sectors or friend pushes to form informal partnership business or advise them about the benefits that they and other are getting by involving themselves in contraband business.

Table 3: Who lead you in to contraband business

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	My own personal situations	32	64.0	64.0	64.0
	My families push	3	6.0	6.0	70.0
	My friend's initiation	15	30.0	30.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

4.3 Knowledge of the Respondents about Contraband

The awareness or knowledge that one has about any activity that he/she wants to do has effect on its outcome. Business peoples usually conduct SWOT analysis before direct starting the business. On the other hand, there are people who engage themselves in a business or other transactions unknowingly or without the idea about the cost and benefit of that activity. There are also other who start a trade activities by looking at the success of other people or do it because other have done it before and became successful in it. The same is true in case of contraband.

Contrabandists run their business violating the law of the country may be by knowing of about the existence of the business outside the government regulation or unknowingly. They merely run it by looking their benefit, but they did not analysis the effect that it has on the society and the economy of the country at large. Accordingly, the response of the respondents about their knowledge regarding the illegality of their business is presented in Table 4:

Table 4: Do you know that the business you are involved in is illegal

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	17	34.0	34.0	34.0
	No	33	66.0	66.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

From the above table the response, the majority of the contraband operators indicates lack of knowledge about the existence of their business outside the rule and regulation of the country. They are running it as a normal business like formal operators, but they did not have awareness about the illegality of their business and its effect on formal business operators and other locally produced products and even innovations.

4.4 Benefits and Effects of Contraband

Although contraband exists outside formal system, it benefits the economy of a country in various ways. For instance, it enables people to meet the education, housing, and other basic needs, employs people in their home countries and in the countries where they source their goods and it is also a supplementary source of family income to people who are under-employed. It also benefits consumers through lower prices of the informally imported products. Table 5 and 6 below show the results of the contrabandist regarding the benefits of their informal business.

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Table 5: Do you think that contraband activities are important for the economy of a country

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	41	82.0	82.0	82.0
	No	9	18.0	18.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

According to the result of the table, their business has a contribution or benefits the economy of the country (82%). In line with the above response, they were also asked in what way illegal activity can benefit the economy of the country.

Table 6: If your answer to question No 17 above was yes, then in what way can it benefit the economy of the country?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	It enables small entrepreneurs to escape poverty	18	36.0	36.0	36.0
	It allows us to meet the education, housing and other basic needs	15	30.0	30.0	66.0
	It acts as a supplementary source of family income	10	20.0	20.0	86.0
	It act as a source of employment to some people who were retrenched	5	10.0	10.0	96.0
		2	4.0	4.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

The benefit of the contraband business according to the operators, through giving ability for the operators and small entrepreneurs to escape poverty (36%), also allows others who have no formal source of income to meet the education, housing and other basic needs for their families (30%) and even acts as a supplementary source of family income to people who are paid low salary (20%).

The illicit transactions that is being conducted in the country outside the formal system or government regulation has harmful effects as well starting from the expansion of crimes to going down in government revenue to distortion of the formal economy of the country. It even promotes anti-social behavior and violation of the rules and norms in the formal economy and also regarded as the cause of low GDP growth. Such illicit activities also have benefits to society in the form of employment, a source of income, and as a means to escape poverty.

Table 7: Effect of Contraband

	Employee Perception					Mean	SD
Statement	SA	A	N	D	SD		
Undermines government tax revenues	88%	12%	0%	0%	0%	1.12	.327
Increases tax burden on formal business operators	48%	29%	21%	2%	0%	1.76	0.836
Discourage formal operators	39%	40%	8%	8%	5%	2.01	1.133
Distorts competition in the market	18%	42%	21%	10%	9%	2.53	1.178
Foster the development of additional criminal activities	10%	12%	64%	8%	6%	2.85	0.911
Undermines investment, innovation and distribution	37%	42%	21%	0%	0%	1.84	0.754
Foreign currency loose	53%	22%	10%	9%	6%	1.89	1.203
Creates unfair competition for official traders	40%	37%	14%	6%	3%	1.93	1.004

Source: Survey (2018)

Table 7 above presents the effect of contraband and as was seen contraband undermines the government revenue the highest response (100%) with a mean of 1.12 and standard deviation of 0.327 because the operators are outside formal system and also are difficult to be taxed. By allowing products illegally to enter the country and sold informally causes the government revenue to fall. It also increase tax burden on formal business operators as was shown on the table (77%) with a mean and standard deviation of 1.76 and 0.836 in such a way that two of them (contrabandist and formal business operators) are selling the products in the same country for similar customers, but one is paying tax on the returns, but the other one didn't pay tax. This expansion of nontax paying business lowers revenue of the government, and in need of revenue to

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cover its expenditures, government tries to raise it through growth of tax bases or raising tax rate which will fall only on formal operators. This, also, may remove official business operators from legal system to join informal nontax paying system (79%) with a mean of 2.01 and standard deviation of 1.133.

Moreover; hence contrabandists bring products at a lower price with higher quality causes the local producers. The country in need of raising its economy takes many measures to attract foreign investors and also local investors to invest capital in different projects. As an investment made in developing country, the products face big challenges in the market if there are quality products imported informally from the developed nation. This kills the need for the investments and innovations in the country as shown in the table (79%) with a mean and standard deviation of 1.84 and 0.754. Such illegal business also wipes out foreign currency that a country may earn from formal import-export activities (77%) with a mean and standard deviation of 1.89 and 1.203 and also can create unfair competition in the market (79%).

4.5 *Contraband Controlling and Challenges Faced in the Controlling Process*

Contraband goods have no official entry point in Ethiopia, do not have customs document or prior approval to enter into or depart from the country according to ERCA report. The smuggler's traffic goods of various kinds into and out of the country illegally without having state-issued permits, license or registration. They violate the law that governs the import /export procedure and thus avoid the payment of all applicable taxes for the importation or exportation of goods.

Because of the negative effect that it has on the economy of the country, revenue authority is framing different means to stop it as much as possible. The prevention strategy involves a wide range of actors-government, regional and local administrators, and the society at large. The government has disbanded customs police and replaced them by federal police who will work with regional and local administrators and the community and even mended customs and tax laws. According to the report, as a result of the active participation of them in fighting against contraband, the volume of contraband goods that enters has decreased.

The government starts to take serious measures by removing the existing government regulatory bodies assigned to control contraband and even amend the rules that govern that activity. The government takes such actions because that illicit activity was growing from time to time negatively affecting the tax revenue of the country. Accordingly, the controlling process to some extent was effective in decreasing the volume of the contraband products entering the country. The response of the contrabandist was presented in Table 8 whether they have ever caught by the government or not.

Table 8: Have you ever caught by government bodies who are assigned to control contraband

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	23	46.0	46.0	46.0
	No	27	54.0	54.0	100.0
	Total	50	100.0	100.0	

Source: (2018)

The result of the contrabandist for this study shows that 54% have never been caught by the controlling units where as 46% were trapped by the controlling unit. From this one can conclude that the controlling process was to some extent not effective.

The contrabandist operators who have been caught by controlling unit were asked about what happens if they were trapped by the government units which are assigned for that illegal activity. The result shows that their products were confiscated by the controlling units 44%. In addition, 48% stated that nothing was happened to them (see Table 9). This group may be caught by government unit, but they may have methods that they are using to escape confiscation or penalty.

Table 9: What was happening to you after being caught by government bodies

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	My products were confiscated	22	50.0	50.0	50.0
	I have been penalized	4	28.0	28.0	78.0
	Nothing was happen to me	24	22.0	22.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

The contraband operators have many ways that they can use to escape confiscation or penalties. They are expert in bribing government bodies who use public power for personal gains and can support the contrabandist. The majority of the respondents stated that they had escaped confiscation or penalty (62%) shown table 10 below.

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Table 10: Have you ever escaped confiscation or penalty after being caught by government bodies

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	31	62.0	62.0	62.0
	No	19	38.0	38.0	100.0
	Total	50	100.0	100.0	

Source: Survey (2018)

The groups from the respondents that escape confiscation as well as penalty were asked how they are dodging and their answers were presented in table 11.

Table 11: How Did You Escape

	Frequency	Percent	Valid Percent	Cumulative Percent
I bribe controlling units	25	50.0	50.0	50.0
I give them the most expensive products that they want from the contraband	18	36.0	36.0	86.0
I promised them to bring the products that they want from abroad	7	14.0	14.0	100.0
Total	50	100.0	100.0	

Source: Survey (2018)

As was revealed in the table, the majority of the respondents (50%) stated that their main means of escaping confiscation and penalty is bribery. They are running a large amount of capital so instead of losing that hug amount of money they prefer paying a bribe for the controlling units informally. They have the ability to pay and also how to pay, so after paying the area, they carry the products publicly without any fear. In addition to this, they offer them the most expensive products that they lacked the ability to buying on the legal market. By giving them those products that the controlling units need, they can escape controlling point easily.

In addition to the above problem in controlling contraband process i.e. bribe and provision of expensive products, the tax authority employees were also asked about the challenges that the tax authority is facing in dealing with contraband. The existence of the business outside the government regulation by its nature was hard to control for the controlling authority. They have no formal license for that business, inter the border illegally, and sold illegally without government permission. This and other problems associated with that illicit business makes the controlling process difficult. Table 12 provides responds to the tax authority employees regarding the challenges associated with controlling contraband.

4.6 Challenges in controlling contraband

Table 12: Challenges in dealing with contraband

Statement	Employee Perception					Mean	SD
	SA	A	N	D	SD		
Insufficient enforcement and penalties	26%	68%	6%	0%	0%	1.77	.535
Lack of ongoing training on how to control contraband	56%	32%	8%	4%	0%	1.60	.805
Weak institutional capacity	12%	38%	22%	16%	12%	2.79	1.21
Lack of competent and skilled man power in control unit	65%	26%	4%	5%	0%	1.47	.759
Insufficient checkpoints to control all cross border activities	20%	12%	54%	14%	0%	2.65	.966
Lack of adequate modern technological instruments and infrastructure	16%	24%	33%	20%	7%	2.77	1.16
Poor working conditions	8%	20%	28%	42%	2%	3.11	1.02
Poor salary for controlling units	68%	30%	2%	0%	0%	1.33	.502
Extensive informal sector in the economy	11%	10%	46%	23%	10%	3.16	1.10
Ineffective respond to tax evasion	27%	43%	28%	2%	9%	2.07	.811
Large and poor border	11%	20%	48%	11%	10%	2.91	1.08
Complex geographical transportation	12%	22%	43%	21%	0%	2.72	.952
Poor coordination within the authority	40%	12%	34%	13%	1%	2.23	1.16
Corruption and coalition	62%	24%	12%	2%	0%	1.53	.811

Source: Survey (2018)

Hence the issue that was being tried to control was the challenging one so need a well trained skilled and committed employees that work in collaboration with the general public. Opposite to this however, the obstacle in controlling process was insufficient human resource that have skill and competent (91%) with a

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mean of 1.47 and standard deviation of 0.759. The products are entering the border illegally with no fixed ways. The contrabandist changes the ways every time so needs ongoing training about how to mitigate that illegal activity. Reverse to this, there was no ongoing training (94%) with mean and standard deviation of 1.77 and 0.535.

4.7 Measures to Reduce Contraband

Contraband business in a given country has different socio-economic, political and cultural effects. It was explored by policy developers as well as academicians at many periods, but the issue was continued to grow instead of diminishing. To protect their country from negative outcomes of that activity and even to secure their tax revenue continuously, it is necessary for governments to reduce the effect. Ethiopia like other African countries is affected by contraband trade, so the government has taken many measures like banning the existing government units assigned on that area, create awareness for the general public, amending tax and customs laws, enhancing public education and enlightenment, allowing border trade and other.

Table 13: Measures to wipe out or reduce contraband

Statement	Employee Perception					Mean	SD
	SA	A	N	D	SD		
Create conducive environment for effective coordination and communication among controlling unit and the general public	50%	34%	8%	8%	0%	1.8	0.959
Human resource capacity development	58%	40%	2%	0%	0%	1.43	0.524
Strong enforcement of the rules and punishments	42%	48%	6%	4%	0%	1.69	0.716
Strengthen domestic innovations and manufacturing to fill demand supply gap	55%	36%	9%	0%	0%	1.55	0.664
Introduce and enhance information technology infrastructure	12%	21%	55%	8%	4%	2.69	0.90

Source: Survey (2018)

Contraband business is to some extent the result of the demand and supply gap in the formal system. The official business operators in a country like Ethiopia provide products with low quality. This supply gap pushes not only those who are not participating in authorized business, but also those that have business to fill that gap. It is so essential for a government to raise domestic innovations and manufacturing as was seen in the above table (91%) and human resource capacity development (98%) with a mean of 1.55 and standard deviation of 0.55. In addition to this, according to the response of the official's poor enforcements and implementation of the existing rules and regulations expand illegal activities, so it is better for the tax authority to strengthen strong enforcement of the rules and punishments (88%). Even more; the tax authority with federal police officers cannot mitigate that illegal activity unless they collaboratively work with the general public. They must create a conducive environment for effective coordination and communication among controlling unit and the general public (84%).

5. Conclusion

The objective of this paper was to assess the effect that contraband business has on government revenue of the Segen Area People Zone. Contraband incorporates those transactions from which the operators generate huge amount of returns but pay no tax for the government. Some of factors push or motivates peoples to engage in such illegal activity according to the result of the study like lack of formal income to meet their family responsibilities (42%), lack of job (32%) and the demand and supply gap in the formal sectors (20%). According to the result, the selected contrabandists were led into such activity by their situations (64%) and friend initiation (30%).

The majority of the contraband operators have no knowledge about the existence of their business outside government regulation. They are running it as a normal business like legal operators, but they did not have awareness about the illegality of their business and its effect on formal operators and other locally produced products and even innovations. Accordingly, their business will support the economy through giving the ability for the operators and small entrepreneurs to escape poverty, allows other who have no formal source of income to meet the education, housing and other basic needs for their families and even acts as a supplementary source of family income to people who are under employed. It directly undermines the government revenue, increase the tax burden on official business operators and may remove formal business operators from formal system to join the informal nontax paying system. Moreover; kills the need for the investments and innovations in the country, wipes out foreign currency that a country may earn from formal import-export and also create unfair competition in the market.

The process of controlling contraband faces a great challenge like the bribe, insufficient skilled, and competent human resource, lack of ongoing trainings, low salary of the workers, corruption, and coalition, inadequate enforcement and penalties and ineffective respond to tax evasion in the area. According to the

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result of the study, it is so better for a government to raise domestic innovations and manufacturing and human resource capacity development. In addition to this, it should also strengthen strong enforcement of the rules and punishments and even create the conducive environment for effective coordination and communication among controlling unit and the general public.

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