



**VALUE ADDED TAX AND REVENUE GENERATION IN NIGERIA:
A CONCEPTUAL APPROACH****By****CLEMENT OKO SIMON¹, DR. HARUNA DADDA'U²**^{1,2} *Kaduna State University, Kaduna, Kaduna State, Nigeria,**Corresponding authors' email and mobile: sirclemz45@gmail.com/08036001030¹,**harunadaddau@kasu.edu.ng/08037006042²*

Abstract

The value added tax (VAT) has emerged as a significant means of generating revenue for the Nigerian Government in recent times, however with its attendant problems due to tax evasion and tax avoidance, it has continued to lower revenue. The objective of this study is to examine the contribution of value added tax to government revenue by analysing data from 1994 to 2022. The study employs secondary data sourced from the Federal Inland Revenue Service (FIRS) and the bulletins of the Central Bank of Nigeria (CBN) within the period of review. The study is underpinned by fiscal theory of taxation as well as optimal taxation theory, it primarily utilised descriptive statistical approach to analyse the data. The study concluded that value added tax contribution to revenue generation in Nigeria was extremely low; despite its huge beneficial impact on revenue generation in absolute terms. The study suggested that the Federal Government of Nigeria should persist in enhancing the administration and collection of Value Added Tax (VAT) in order to further augment its contribution to the government revenue.

Keywords: nigeria, revenue generation, taxation, value added tax

1. Introduction

Taxes are a fundamental and indispensable source of revenue for all government of a Country. Nigeria in particular, has two types of taxes: direct and indirect. Its citizens remit direct taxes to the government, notably income tax serving as a perfect illustration of this phenomena. On the other hand, an indirect tax in the category of sales tax or value-added tax is collected through exchange of goods and services on behalf of the government as well as tax collection via consumption of goods and services. The significance of tax revenue in fostering economic development is universally acknowledged, prompting numerous nations to implement value-added tax systems on goods and services. The imposition and collection of taxes are predominantly influenced by a country's economic framework, developmental stage, the expansion of its service sector, degree of industrialization, and employment rates (Qamruz, Okasha, & Muhammad, 2012).

One major source as a component of tax is the value added tax (VAT). Value-added tax functions as a consumption levy, applied at each stage of the consumption process and ultimately borne by the end consumer of the product or service. It has emerged as a significant revenue stream in numerous developing nations across Sub-Saharan Africa, with its implementation witnessed in various countries. In Nigeria, the genesis of VAT can be traced back to the recommendations of a government-appointed committee in 1991, aimed at overhauling the tax system to broaden the financial base for revenue generation and bolster economic growth. The adoption of VAT in Nigeria, under Decree 102 of 1993, marked the transition from the sales tax regime instituted by Decree No. 7 of 1986. Although the Decree came into effect on December 1, 1993, invoicing procedures commenced on January 1, 1994, as per administrative arrangements (Gendron, 2005).



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Onwucheka and Aruwa (2014) opined that several governments implemented value-added taxes on products and services in order to generate revenue; it is also imperative to note that VAT is imposed on the provision of goods and services, with the obligation falling on the vendor to collect VAT from buyers, whether individuals or companies, on behalf of the Federal Inland Revenue Service (FIRS). VAT applies to all goods and services supplied, except those specifically exempted. The Minister of Finance, by order of the Federal Government published in the Gazette, has the authority to adjust the tax rate and revise the list of exempt goods and services. Items exempted are Zero-rated items which include goods and services purchased by diplomats and goods purchased for use in humanitarian donor-funded projects, others are plants and machinery for use in export processing zones (EPZs) or free trade zones (FTZs), basic food items (based on a specific list), medical products and services, pharmaceutical products, books and educational materials, and exported services. On the 1st February 2020, through a technical committee recommendation reviewed the VAT rate upward from 5% to 7.5%; this necessitates the improvement of the revenue generation drive of the Government (Uwaegbute, 2024). However, despite its introduction, many influential figures and interest groups criticized it. There are evident issues associated with VAT.

Since the incorporation VAT into the Nigerian tax framework, it has sparked controversy and ongoing debate among various scholars, such as Naiyeju (2009), who argue that its intended purpose in the Nigerian economy remains unclear. This spark in controversies resulted in the new implementation of the Finance Act 2019 to clear the air on differences in tax rate and implementation. Okpe (2001) also argues that the implementation of VAT in Nigeria was imperative due to the consistent overspending of the government, leading to a substantial fiscal deficit. This deficit is the fallout from the proposition suggests a transition from direct to indirect taxation within the non-oil sector as a strategic measure to invigorate economic growth while maintaining revenue sufficiency. This strategic shift is imperative due to the diminishing sustainability of oil revenues and the pressing need to diversify the revenue base. The proposal advocates for the reduction of direct tax rates, such as Company Income Tax and Personal Income Tax, aiming to mitigate the operational costs for businesses in Nigeria. By enhancing cash flow and disposable income for both corporate entities and individuals, this adjustment seeks to foster a conducive business environment and economic expansion within the non-oil sectors.

The Head of Cooperation of the Delegation of the EU and ECOWAS to Nigeria, Massimo De Luca, while speaking at the 4th session of the Steering Committee of the Support Programme for Fiscal Transition in West Africa held in Abuja, he blamed the low compliance with VAT in Nigeria on corruption and poor implementation. He also noted that while some companies may be willing to pay their taxes, the current taxation system in the country does not allow them to do so (Adaji, 2024). This is viewed as a critical problem that VAT implementation is facing presently in Nigeria. The motivation for this study on value added tax and revenue generation in Nigeria is to provide a conceptual outlook of the study implementation and growth it will bring to the Nation for a period from 1994 to 2022.



2. Literature Review

Conceptual Review

Taxation

Tax is an obligatory levy paid to a government in return for essential services, without necessarily specifying the source of income or directly correlating the services with the funds received (Onwuchekwa & Aruwa, 2014). The fundamental objective of taxation is to generate revenue for the government to cover its expenses and provide social amenities and welfare for the population (Ihenyen & Mieseigha, 2014). Taxation is perceived as an obligation that every person must shoulder in order to support their government, as the government has specific responsibilities to fulfill for the welfare of its constituents (Afubero & Okoye, 2014). Ogbonna and Appah (2012) argue that taxes are imposed to finance state activities and to distribute the tax burden across members of society. This is done to enable the government to obtain revenue for its expenditures. Omes and Nzor (2015) asserted that taxation is a vital source of revenue for every country and that its level of growth is often contingent upon the cash derived from taxes.

Taxation is a method used by the government to produce revenue in order to fulfill the needs of both the government and its citizens. Brautigam (2008) argues that an effectively constructed tax system can assist governments in developing countries in allocating funds, establishing reliable institutions, and enhancing democratic responsibility. According to Musgrave and Musgrave (2004), the decreasing tax revenue generated in developing countries undermines the effectiveness of taxes as a fiscal policy tool for promoting economic growth. Certain countries, like Canada, the United States, the Netherlands, and the United Kingdom, have significantly influenced their economies by generating tax income through Company Income Tax, Value Added Tax, and Personal Income Tax (Oluba, 2008).

Taxation is typically categorized into two primary types: direct and indirect taxes. This paper focuses solely on indirect taxes, particularly delving into the intricacies of value-added tax (VAT). Value-added tax is an indirect levy imposed on all taxable goods and services consumed by individuals and corporate entities (Omes & Nzor, 2015). Functioning as a consumption tax, VAT is imposed at each stage of the consumption process and ultimately borne by the final consumer of the product or service (Qamruz et al., 2012). According to the Value Added Tax Act of 1993 as amended, individuals and businesses are mandated to charge and collect VAT at a standardized rate of 5% on all invoiced amounts, applicable to goods and services not exempted from VAT (Adereti, Sanni, & Adesina, 2011).

Value Added Tax (VAT)

Value Added Tax (VAT) constitutes a levy applied to the provision of taxable goods and services, excluding those delineated in the initial schedule of the VAT Act and as provided in the Finance Act 2020. It operates as a multi-tiered imposition on incremental value at each stage of production or distribution. Within a manufacturing entity, value addition commences with the procurement of raw materials and culminates in the sale to end-users. As the fiscal responsibility ultimately rests upon final consumers, VAT is categorized among indirect taxes; as either taxable transaction or taxable services.

In Nigeria, a taxable transaction involving goods transpires when the said goods are physically within the country or when the beneficial owner is a taxable individual in Nigeria, and the rights to or over the goods are situated therein. Goods, in this context, encompass all tangible assets except for land, buildings, currency, or securities. Regarding taxable services in Nigeria, they occur when a service is



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provided within Nigeria by an individual physically present in the country, the service is delivered to and utilized by an individual within Nigeria, and the service is associated with an immovable property located in Nigeria. Services, in this context, encompass anything other than tangible goods or services provided under an employment agreement. This definition extends to any intangible or non-physical asset for which transferable rights exist, with the exception of interests in land, buildings, currency, or securities.

VAT is a type of tax imposed at a certain stage during the sale of a goods or service. Put simply, it is a type of tax that is placed on customers at every step of consumption cycle, starting from the acquisition of input materials and ending with the purchase of finished items. From the perspective of the customer, VAT is a tax imposed on the purchase price. However, from the perspective of the seller, it is simply a tax levied on the "value added" to a product, material, or service throughout the manufacturing or distribution process (Rehana, 2017). The Nigerian Value Added Tax (VAT) system is distinguished by a fixed rate of 7.5%, which was raised from the previous rate of 5% in 2020, through the Finance Act 2020 (Udo Udoma & Bello-Osagie, 2022). The Value Added Tax (VAT) is managed and administered by the Federal Inland Revenue Service (FIRS) through its VAT Directorate located in Abuja; and is levied on the provision of products and services within the country, as well as on imports. Nigeria's VAT system has undergone multiple revisions to enhance its effectiveness and scope.

The VAT rate in Nigeria is 7.5%, but there are zero-rated and exempt items that do not attract a 7.5% rate. Goods exempt include medical and pharmaceutical products; basic food items of agro and aqua-based staple food; educational books and materials; baby products; fertilizers, locally-produced agricultural chemicals and veterinary medicine; plant, machinery, and equipment purchased for utilization of gas in downstream operations; oil exports; plant, machinery, and goods imported for use in the export processing zone or free trade zone, tractors, ploughs, and agricultural equipment and implements purchased for agricultural purposes; locally manufactured sanitary towels, pads, and tampons; commercial aircraft including its engine and spare parts; petroleum products; renewable energy equipment; raw materials for the production of baby diapers and sanitary towels; raw materials for the production of pharmaceutical products; locally produced animal feeds; military hardware, arms, ammunition, and locally manufactured uniforms used by the Armed forces, para-military, and other security agencies of governments in Nigeria; gas supply by gas-producing companies to Electricity Generating Companies (GENCOs), electricity generated by GENCOs and supplied to National Grid or Nigeria Bulk Electricity Trading Company (NBET), and Electricity transmitted by Transmission Company of Nigeria (TCN) to Electricity Distribution Companies (DISCOs); and agricultural seeds and seedlings; interest in land and building, money, or security; motorcycle (CKD)/Bicycle (SKD – Semi Knocked Down) and parts.

On the other hand, services exempt are medical services; services rendered by Unit Micro-Finance Banks and Mortgage Institutions; plays and performances conducted by educational institutions as part of learning; exported services; commercial airline transportation ticket; lease or rental of a residential accommodation; shared passenger road-transport service; and tuition of a nursery, primary, secondary, and tertiary education. Nevertheless, zero-rated goods and services consist of non-oil export; goods and services purchased by diplomats; and goods purchased for use in humanitarian donor-funded projects



Aside transactions and services exempt from VAT payment; businesses are also exempted from accounting for VAT- Small businesses with an annual turnover of below NGN25 million are exempt from accounting for VAT. A small business can issue an invoice without including the VAT on sales (output VAT). However, the business will pay (input) VAT on the purchase of taxable goods and services (Udo Udoma & Bello-Osagie, 2022). The revenue generated by Value Added Tax (VAT) in Nigeria is allocated among the tiers of government according to an authorized ratio. Presently, the federal government receives 15% of the VAT proceeds, the state government receives 50%, and the local government receives 35% (Oyedokun, 2016). The implementation of VAT as a tax methodology was initially introduced in 1994. Since then, it has greatly increased revenue generation.

Administration and Implementation of Value Added Tax in Nigeria

The administration of Value Added Tax (VAT) in Nigeria is managed by the Federal Inland Revenue Service (FIRS), the governmental agency responsible for the assessment, collection, accounting, and enforcement of taxes owed to the federation and the Federal Government of Nigeria. Historically, the VAT rate was set at 5% when it was introduced in 1998. However, the Finance Act 2019 amended the VAT Act, resulting in an increase to 7.5%, which came into effect in February 2020. All taxable persons must register for tax purposes and obtain a Tax Identification Number (TIN) when they commence business operations. Nonetheless, only businesses that achieve an annual turnover of N25 million (Naira) or more are obligated to collect, pay, and file VAT returns (Udo Udoma & Bello-Osagie, 2022).

VAT returns are to be submitted to the FIRS on a monthly basis, specifically by the 21st day of the month following the month of the transaction. These returns should provide detailed accounts of sales, purchases, output VAT (VAT charged on sales), and input VAT (VAT paid on purchases). Additionally, the payment of any VAT liability must accompany the filed returns within this specified period. Registered businesses must charge VAT on all taxable goods and services and remit the collected VAT to the FIRS. In certain instances, the VAT to be remitted is the difference between output VAT and input VAT. This scenario typically applies to goods purchased for resale or raw materials used in the production of other taxable goods. Failure to comply with the VAT Act results in penalties and interest charges. Therefore, it is crucial for businesses to understand and fulfill their VAT obligations to avoid penalties and legal consequences.

Revenue Generation

Revenue is a key source of income generation. According to Hassan (2012), revenue encompasses tolls, taxes, rates, fees, penalties, rents, forfeitures, dues, and other government receipts from various sources, all of which the legislature has the authority to appropriate, including proceeds from loans. The 1989 Federal Constitution of Section 160 (9) and the 1999 Constitution of Section 5, 162 (10) define revenue as any income or returns received by the government from its property, interest on loans, and dividends from shares or interests held by the government in companies or statutory bodies. Additionally, revenue includes incidental sources related to a specific environment, permissive sources from regular operations, and statutory sources recognized by the Nigerian constitution. Effective revenue generation requires robust revenue control mechanisms to ensure timely collection, accurate receipt of due amounts, and proper deposit of collected revenue into government coffers.

Revenue generation is a crucial element of public finance in Nigeria, since it supplies the essential resources for government spending and the execution of development initiatives;



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the diverse sources of income in Nigeria, encompassing oil revenue and non-oil revenue. Historically, oil revenue has been the primary and most influential source of income in Nigeria, contributing a substantial amount of the country's overall revenue (Adeyemi, 2012). Revenue leakage and illicit money flows pose a substantial obstacle to revenue generation in Nigeria, especially tax evasion and avoidance, corruption, incorrect pricing of products and services, and money laundering (Adeyemi, 2012). There is need for efficient tax administration, robust regulatory frameworks, and global collaboration to combat these unlawful acts and improve revenue generation. To augmenting revenue generation, the strategies to be implemented are: increasing the tax base by improving tax compliance and enforcement, carrying out tax policy reforms, improving revenue administration and management systems, promoting transparency and accountability in revenue collection, and enhancing collaboration between federal, state, and local governments (Umar et al., 2019; Adeyemi, 2012).

Empirical Review

Several studies have examined the effect of value added tax on government revenue generation in different context with diverse approaches. Olaoye (2004) conducted a study on the administration of VAT in Nigeria with the objective of seeking ways of improving government revenue generation base in order to improve the economy. The study recommended that the government should increase citizen's awareness on the existence VAT. Rostami et al, (2012) examined the impact of fiscal policy on economic growth in Iran with emphasis on the role of value added tax. They discovered that value added taxes have significant effect on real output and which conclude that value added taxes as a fiscal policy tool is useful for economic growth. In addition, Adereti et al, (2011) examined value added tax and economic growth in Nigeria, their investigation showed a positive and significant correlation between values added tax and gross domestic product. Wambai and Hanga (2013) on taxation and social development in Nigeria: tackling Kano's hidden economy, they found that taxpayers' attitude towards governance affects their tax compliance behaviour; they recommended a tax system that concentrate on establishing simplicity, predictability, and good governance.

Theoretical Structure

This study will be underpinned by the fiscal theory of taxation and optimal taxation theory. The Fiscal Theory of Taxation examines the role of taxation in the economy, particularly how taxes are used to generate revenue for government expenditures, redistribute income, and influence economic behavior. It is grounded in public finance and economic theory, and focusing on the impact of different tax policies on the economy. The theory was propounded by Adam Smith (1723-1790) and David Ricardo (1772-1823) while Optimal Taxation Theory was propounded by Frank Ramsey (1903-1930), James Mirrlees (1936-2018) as a framework in public economics that seeks to design a tax system that maximizes social welfare while minimizing economic distortions. It considers how different types of taxes affect economic behavior and overall welfare

3. Methodology

This study employed the descriptive research methodology; with a positivist approach. The study examines the relationship between value-added tax and total government earnings using data spanning from 1994 to 2022. The data source which is secondary in nature include of statistics obtained from the bulletins of the Central Bank of Nigeria for different years, as well as the Federal Inland Revenue Service (FIRS). The statistical techniques employed in the investigation were predominantly descriptive.



4. Discussion

Value Added Tax Analysis

Value of Total Revenue and VAT Collected (1994-2022)

Table 1 illustrates the overall revenue performance and the profile of value added tax income from 1994 to 2022. Based on statistical data, the total revenue has consistently risen from the start of the research period. This growth from 1994 to 1999 and a quantum leap from 2000 to 2008 can be attributed primarily to higher oil prices, which have been further supported by improved performance in non-oil revenue. In 2009, there was a decrease in overall revenue, but it quickly rebounded in 2010 and continued to grow till 2013. Until 2015, the decline in global crude oil prices negatively impacted oil revenue.

Nigeria's income has consistently outpaced the continental average, with a growth rate that is 6% higher. However, in 2015, a decline in oil prices resulted in reduced earnings from oil-related industries, namely the Petroleum Profit Tax (PPT), which had a significant impact on overall tax collection (Okwe, 2015). In 2016, there was a rise in revenue recovery, with a higher number of barrels per day compared to previous years. This level has remained relatively stable, despite variations in 2017.

Table 1

Amount of Total Revenue and Value Added Tax (VAT) Collected

Years	Total Revenue (N'B)	VAT(N'B)
1994	49.51	5.03
1995	69.04	6.26
1996	89.53	11.29
1997	96.96	13.91
1998	143.2	16.21
1999	168.99	23.75
2000	359.07	30.64
2001	573.55	44.91
2002	669.82	52.63
2003	855	65.89
2004	1113.94	96.2
2005	1419.64	87.45
2006	1542.77	110.57
2007	2065.41	144.37
2008	2934.84	198.07
2009	2590.67	229.32
2010	3162.54	275.57
2011	3410.1	318
2012	3572.52	347.69
2013	3905.38	389.53
2014	3672.03	388.85



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Years	Total Revenue (N'B)	VAT(N'B)
2015	2859.02	381.27
2016	2467.7	397.06
2017	2992.5	473.77
2018	3753.38	533.74
2019	3636.51	564.45
2020	4204.45	699.37
2021	4867.51	964.11
2022	6239.6	1171.36

Source: CBN Statistical Bulletin on Public Finance (2022)

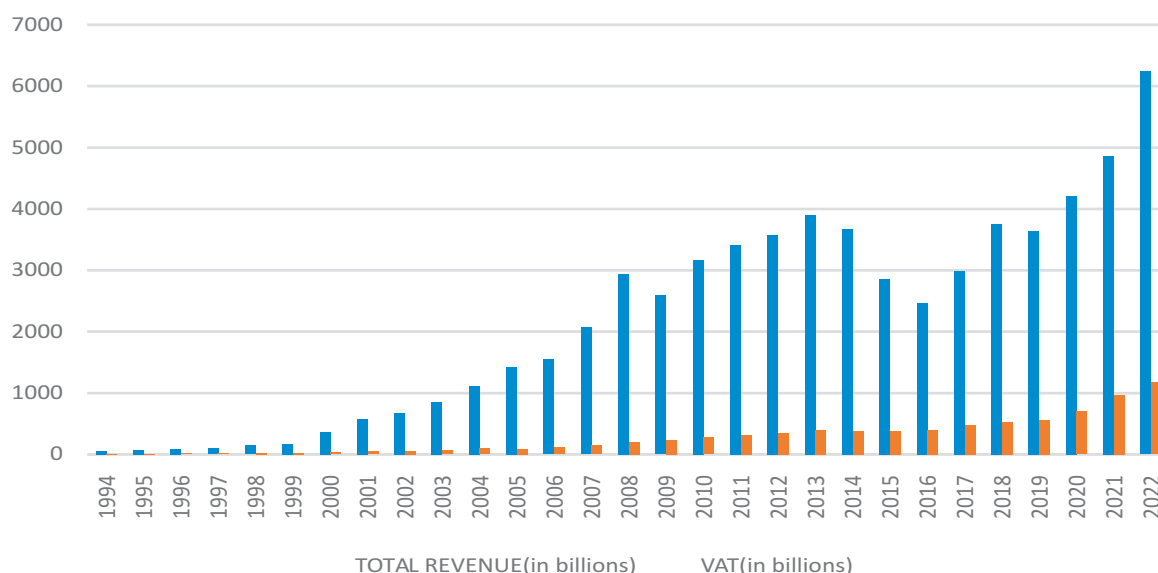


Figure 1: Chart on Total Revenue and Value Added Tax (VAT) Collected

Source: CBN Statistical Bulletin on Public Finance (2022)

Percentage Contribution of VAT to Total Revenue Collected (1994-2022)

Table 2 compares the percentage of value added tax's contribution to the total revenue generated within the period of study. throughout the duration of the study. The percentage contributions of value added tax have been underwhelming. In 1994, the contribution of value added tax to total revenue was 10.16%. This percentage declined to 9.07% in 1995, then had a slight increase to 12.61% in 1996, and further rose to 14.35% in 1997. In 1998, the money generated by VAT accounted for only 11.32%, which increased to 14.05% in 1999. Between 2000 and 2012, the proportion of VAT revenue was extremely low, always below 10%, reaching a peak of 9.7% in 2012. In 2015, there was a slight increase in value added tax, which accounted for 13.34% of the total. In 2016, it rose to 16.09%, but then declined to 15.83% in 2017. In 2018 and 2019, there was a decline in the VAT contribution to total revenue, with percentages of 14.22% and 15.52% respectively. In 2021, the VAT contribution to total revenue was the highest, accounting for 19.81% of the total. However, in 2022, there was a decrease, with the VAT contribution dropping to 18.77%. The abysmal performance of Nigeria's Value Added Tax (VAT) is a detrimental situation for the country, especially considering the unfavorable global attention on the shift from income to consumption taxes, where VAT-type revenue has been emphasized.



Table 2

Percentage Contribution of VAT to Total Revenue Collected

Years	Total Revenue (N'B)	% Contribution of VAT
1994	49.51	10.16
1995	69.64	9.07
1996	89.53	12.61
1997	96.96	14.35
1998	143.2	11.32
1999	168.99	14.05
2000	359.07	8.59
2001	573.55	7.83
2002	669.82	7.86
2003	855	7.71
2004	1113.94	8.66
2005	1419.64	6.2
2006	1543.77	7.16
2007	2065.41	7
2008	2934.84	6.75
2009	2590.69	8.85
2010	3162.54	8.71
2011	3410.1	9.33
2012	3572.52	9.7
2013	3905.38	10
2014	3672.03	10.36
2015	2859.02	13.34
2016	2467.7	16.09
2017	2992.5	15.83
2018	3753.38	14.22
2019	3636.51	15.52
2020	4204.45	16.63
2021	4867.51	19.81
2022	6239.6	18.77

Source: CBN Statistical Bulletin on Public Finance (2022)

VAT Revenue Growth Rate (1994-2022)

Table 3 illustrates the growth in Nigeria's Value Added Tax (VAT) revenue within the period of 1994 to 2022. Accounting for variability in growth is crucial when it comes to tax planning and fiscal policy. Managing budgets and coordinating fiscal activities can provide challenges in situations when tax revenue exhibits significant volatility. While there was significant growth rate from 2011 to 2016, the trend of the value added tax did not exhibit concerning changes on an annual basis throughout the time frame. This is a favorable signal for policymakers as it suggests that VAT revenue would maintain a reasonably consistent level throughout the economic cycle, making it a dependable source for



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forecasting, budgeting, and fiscal coordination. The value-added tax (VAT) exhibits a lower sensitivity to shocks due to its reliance on consumption, as evidenced by empirical research.

Table 3
VAT Revenue Growth Rate

Years	VAT(N'B)	% of VAT Growth
1994	5.03	0
1995	6.26	24.5
1996	11.29	80.4
1997	13.91	23.21
1998	16.21	16.5
1999	23.75	46.5
2000	30.64	29.9
2001	44.91	46.6
2002	52.63	17.2
2003	65.89	25.2
2004	96.2	46
2005	87.45	-9.1
2006	110.57	26.4
2007	144.37	30.6
2008	198.07	37.2
2009	229.32	15.8
2010	275.57	20.2
2011	318	15.4
2012	347.69	9.3
2013	389.53	12
2014	388.85	-0.2
2015	381.27	-1.2
2016	397.06	4.1
2017	473.77	19.3
2018	533.74	12.7
2019	564.45	5.8
2020	699.37	23.9
2021	964.11	37.8
2022	1171.36	21.5

Source: CBN statistical bulletin Public Finance statistic (2022)

5. Conclusion and Recommendation

The paper analyzes the Value-added tax and revenue generation in Nigeria from 1994 to 2022, using secondary data. The analysis reveals that the value-added tax (VAT) accounted for 10.15% of the overall revenue in 1994. Subsequently, it declined to 9.07% in 1995, increased to 12.61% in 1996, and further rose to 14.35% in 1997. The analysis demonstrated that VAT revenue has had a moderate rise



from 13.3% in 2015 to 15.83% in 2017 which signified a stable business cycle that is favourable to policy makers in formulating policies.

The analysis uncovers volatile value-added tax (VAT) growth rates resulting from inadequate monitoring and loopholes in revenue remittance. Policy reforms and the increase of the tax base have the potential to enhance economic growth. However, there are ongoing concerns regarding the decline in growth rates.

The under performance of Nigeria's VAT is concerning, given that other countries are embracing consumption-based tax strategies. Consumption taxes have little distortions on investment, efficient in terms of cost, and are less susceptible to evasion. The study strongly recommended that the government and tax regulators should conduct a comprehensive evaluation of value added tax-based models in order to secure a stable income for the country.

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