IMPLICATION AND IMPLEMENTATION OF VALUE ADDED TAX IN NIGERIA

A Study of Federal Inland Revenue Services Kaduna

By

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CERTIFICATION

This Project Titled "Implications and Implementation of Value Added Tax in Nigeria"

(A Study of Federal Inland Revenue Services Kaduna) By Akinwumi Bamidele Omolere meet the Regulations Governing the Award of the degree of Master of Business Administration (MBA) of Ahmadu Bello University, Zaria and hereby approved for its contribution to Knowledge.

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ABSTRACT

The topic of this research - implications and implementation of Value Added Tax (V.A.T) in Nigeria: A study of Federal Inland Revenue services, Kaduna, assesses taxation as a whole, views the Nigerian economy and gives an insight into circumstances that led to the introduction of a new tax into the Nigerian tax system. The concept of VA.T as regards its operation has also been discussed alongside its working procedure. The relative achievements, impact, problems and prospects of V.A.T have not been left out either, it must, however, be noted that this work may not have touched all things, in as much as it is hinged on areas relevant to the study alone.

The researcher made use of primary and secondary sources of data. The primary source of data consists of information gathered from administered questionnaires and through the structured interview with V.A.T. officers while the secondary data consists of textbooks, encyclopaedia, magazines, periodicals (such as journals and seminar papers as well as circulars) made public from V.A.T I Icadquarters.

As motivation, the researcher was inspired by the fact that a new policy in Nigeria, especially tax which is a citizen's most dreaded policy so to say, is performing tremendously well amidst initial mixed reactions that greeted its advent. To think that VA.T has not only proved successful but has gradually warmed its way into the hearts of many is a marvel.

In addition, the researcher chose the topic for personal enlightenment since a superficial knowledge of anything is not enough to take one very far.

TOPIC: IMPLICATIONS AND IMPLEMENTATIONS OF VALUE ADDED TAX (VAT) IN NIGERIA. A STUDY OF FEDERAL INLAND REVENUE SERVICES, KADUNA.

Dedication: i
Acknowledgement: ii
Table of content: iii

CHAPTER ONE: INTRODUCTION

1.1 Historical Background of the Study 1
1.2 Statement of the Problem 5
1.3 Significance of the Study 6
1.4 Objectives of the Study 6
1.5 Scope of the study 7
1.6 Statement of Hypothesis 7
1.7 Definition of Terms. 8

CHAPTER TWO: LITERATURE REVIEW

2.1.1. Introduction 12
2.2 General Overview of Tax 13
2.2.1 What is Taxation 13
2.2.2 Function or Purpose of Taxation 15
2.2.3 Economic Effects of Taxation 17
2.2.4 Taxable Capacity 18
2.2.5 Preview of the Nigerian Tax System 19
2.2.6 Brief History of VAT in Nigeria 22

CHAPTER THREE: CONCEPTUAL FRAMEWORK

3.1 Introduction 25
3.2 The Conceptualization of Taxation in Nigeria 26
3.3 Taxation as Source of Revenue in Nigeria 34
3.4 The Role of Value Added Tax (VAT) 37
3.5 VAT as a Replacement of Sales Tax 43
3.6 Tax Administration And Policy of VAT in Nigeria 46
3.7 Summary of the Chapter. 51

CHAPTER FOUR: RESEARCH METHODOLOGY

4.1 Introduction 53
4.2 Sources of Data 53
4.3 The Study Area 53
4.4 Methods of Data Collection 54
4.5 Methods of Data Analysis 55

CHAPTER FIVE; DATA PRESENTATION AND ANALYSIS

5.1	INTRODUCTION	57
5.2	Implication of Value Added Tax in Nigeria	58
5.3	Collection of VAT Through Inter-Bank System	58
5.4	Problems of VAT Implementation in Nigeria	58
5.5	Contribution of VAT to Revenue Generation	62
5.5.1.	Effect of VAT on Input and non-Inputs	63
5.6	Prospects of VAT in Nigeria	69

CHAPTER SIX; SUMMARY, CONCLUSIONS & RECOMMENDATIONS

6.1	Summary	74
6.2	Conclusions	76
6.3	Recommendations	77
	Reference/Bibliography	79
	Appendix	

CHAPTER ONE: INTRODUCTION

1.1. HISTORICAL BACKGROUND OF THE STUDY

During the pre-colonial and colonial era, the agricultural sector was playing a dominant role in the Nigeria economy both I terms of revenue generation and physical impact on the economy. Such impact before long started making an impact on the economy, with the oil sector becoming increasingly relevant, other sectors of the economy became secondary in terms of relevance. Other sectors of the economy were neglected in favour of the oil. However, with discovering of oil, which generate an average of 80 per cent of federal collected revenue in Nigeria. These comes from royalties, petrol sales, crude oil etc. Oil therefore becomes the leading product and its sector, the leading sector in terms of Government revenue generation and foreign exchange contribution. The fluctuation in the world oil market price was drastically affecting the Nigerian development plans and economic instability. Fiscal policy is used along with other policy instruments to achieve macro economic objective of price stability, growth, full-employment and balance of payments equilibrium. Fiscal policy is government taxation and expenditure as a means of achieving desired objectives in the economy. Such economic objectives include full employment of productive resources, stable price level, economic growth and balance of payment equilibrium.

There is no intention here to suggest that these objectives are solely the domain of fiscal policy. Indeed, they represent broad statement of the objective of economic policy in general. However, at any point in time, either one or the other may become the primary target of fiscal in policies. This is so because in any given economic situation, two or more of the objection may be in conflict. For instance, government spending to promote economic growth and full employment for her citizens may in some situation be highly inflationary. The principal weapons of fiscal policy are taxes which the source of revenue

generation for government to provide services and run its administration redistribution of income and wealth, management of the economy and to achieve a specific purpose such as discouraging consumption of particular commodity, e.g., alcohol, cigarrette or to encourage production of a particular commodity, e.g. tax free holiday to infant industry (small scale industries).

Taxation is therefore a process of levying and collection by a public authority, with proper jurisdiction, of compulsory contribution from the person or body of persons to defray the cost's incurred by the authority in common interest of all in every country of the world, even in America with government extracts in various proportion some wealth of the citizens for this purpose. It is this sense that taxation connotes a sense of right and responsibility: right owed to the individuals and duties owed by the individuals to the society. As a result of process of taxation some tax payers find themselves with less money to spend and the government finds itself with more money. The transfer of property right from citizen to the government gives rise to obligation on the government to me the right in a way most beneficial to the citizens as a whole.

In Nigeria taxes classification are indirect taxes. Taxes imposed on:

(i) Income, e.g., personal income tax and company tax.

(ii) Capital, e.g., capital gain tax and capital transfer tax.

(iii) Expenditures, e.g., Custom duties and Excise duties, licenses and rate and Value added tax (VAT).

Direct taxes are those taxes levied on changeable person's income or capital and paid directly by the person to the tax authority. Personal Income tax, Company Tax and taxes on capital will fall into the category of direct tax. Conversely, taxes on expenditures are paid indirectly as part of the payment of some goods, services permits to do something. While these taxes may be collected from the person providing the goods or services, their burden is usually borne by ultimate

countries, VAT was introduced as replacement of sales (or some other forms of consumption tax).

In Nigeria, VAT come into being by virtue of Decree 102 of 1993 and is being implemented with effect from January 1, 1994. The Value Added Tax was designed to be progressive and therefore certain essential goods and services were exempted in order to reduce the burden on the average citizen. The taxes which carries a flat rate of 5% was vigorously pursued in 1996. A number of advantages could accrue from the VAT. First, it would diminish the distortions to private savings and investments by shifting the incidence of taxation forward expenditure rather than income. Moreover, it could promote greater flexibility in public sector revenue to allow for the maintenance of development expenditures in light of floatation in oil revenues. On a convenietive bans, the Federal Inland Revenue services has estimated that collection from the VAT for fiscal 1999 will be approximately N10.0 billion.

Value Added Tax is therefore expected to, in addition to being effective, contribute in enhancing the revenue generation base of the government. The system is expected to minimize or at least at best, eliminate the corrupt practices associated with revenue assessment and collection. The importance of revenue in any country and of course in Nigeria, cannot be over-emphasized. Revenue has been the bedrock of government program. The history of revenue in Nigeria dated back to feudal lords or as the case may be, to the Oba's, Kings or Emirs.

Even though, taxes and levies were ensue in cash or kind during the pre-colonial period. It was used to support the sustenance of the colonial administrational dominance. It had been used to mobilized local Farmers into cash crop production mainly for colonial exports through the use of cash taxes. Even after independent taxes have equally played an important role in generating government revenue in Nigeria.

Furthermore, it has also been used to achieve other policies such as the protection of infant industries, income redistribution curtailing the consumption of certain goods, etc. It is therefore very much likely that it will continue to play vital role in the Nigeria economy.

Following the difficulties, irregularities and corruption associated with the assessment and collection of sales tax and other forms of taxes in operation a committee was set up by the Federal Government in 1991 to review the entire tax system in operation. The committee recommended the idea of introducing "Value Added Tax" in the country and another was set up to undertake feasibility studies and make recommendation on it's implementation after which the Federal Government finally approved the introduction of VAT in the Nigerian Tax System with effect from 1st January, 1994. Value Added Tax as the name implies is a tax imposed on the value of goods and services before it is transferred from the supplier to the agents or final consumers.

1.2 STATEMENT OF THE PROBLEM

The research is to find out the position of Value Added Tax revenue generation. The revenue generation by tax system is often one of the most difficult aspects of implementation of government fiscal policy. This research the following statement problem. How does government generate Value Added Tax? How effective is the operation of Value Added Tax system in Nigeria". Is revenue generated from value added tax economic to the government in terms of government revenue generation? And what are the operational problems of generating value added tax? The research also in the effective implementation of government policy on value added tax.

1.3 SIGNIFICANCE OF THE STUDY

The significance of the study is to find how value added tax system has been contributing to the revenue generation and how value added tax system has been useful for government to implement its budget and fiscal policy.

The significance of the study will enlighten tax payers and investors, individual organization companies on how to compute and pay their value added tax and it will also direct the tax payer what is expected from value added tax system both goods and services. The research work will also serve as enlightening purposes for those who are ignorant and unaware of activities of tax authority in operation and implementation of value added tax system.

The significance of the study will enable government on allocation and distribution resources through revenue generation from VAT and it will also guide government on how to implements its government policy, planning and forecasting future Nigeria growth and development. The significance of this research cannot be overemphasized.

1.4 OBJECTIVES OF THE STUDY

One objective of this study is to critically look into the introduction of value added tax as a system of taxation in Nigeria. To look at the relationship between value added tax and the revenue generated through other forms of taxation in Nigeria. It also examines the relationship between value added tax and the entire revenue derived from implementation of value added tax system. It is also to find out the problems associated with the administration and policy of the value added tax (VAT) since its introduction by virtue of Decree 102 of 1993. VAT carries a flat rate of 5% and has pursued up to date.

Another objective is to also examine the collection of VAT through computer and also recommend ways of making VAT to be very effective and responsive to the needs of Nigeria.

1.5 SCOPE OF THE STUDY

The scope of the study is to examine and investigate to what extent implementation of value added tax by government and role of tax authority and modalities of value added tax system. The scope of study is to cover the introduction, implementation, problems and prospects of VAT and its relationship with revenue generation in Nigeria. From this, it is obvious that the topic. "Implications and implementations of value added tax in Nigeria" is well embracing in scope. Therefore it needs to be restricted for any meaningful discussion. It is intended to focus attention in this study on Value Added Tax, implications and implementations in Nigeria.

1.6 STATEMENT OF HYPOTHESIS

The hypothesis of this research is to seek and find solution to the implementation and implication of value added tax system in Nigeria such as:-

(1) Proper of VAT inspection (VAT VISIT) so as to ensure compliance with the VAT legislation and regulation in all its ramifications.
(2) To ensure that full amount of VAT deducted are promptly accounted for.
(3) To examine methods of recording transactions and offer suggestions were necessary.
(4) To afford the VAT payer the opportunity to ask question and seek clarification as may be necessary.
(5) To educate VAT payer on new development in the system.

However, the hypothesis is assumed solution to the research under which it will later contribute to effective and efficient ways of implementation VAT in Nigeria.

1.7 DEFINITION OF TERMS

It is necessary to define some terms for understanding of the operation of VAT.

(1) **INPUT TAX:-** This is the VAT paid by a manufacturer on raw materials purchased by him for his production operation. It does not matter whether such materials are bought locally or imported to Nigeria they will be subjected to VAT so long as they are not included on the list of Vat exempted goods ad services.

(2) **OUTPUT TAX:-** This is VAT collected by manufacturer from buyer of their finished products.

(3) **VAT ON IMPORT:-** This is based on the total value of the imported items. The value of import is taken to include costs, insurance, freight, custom duties and other changes incurred by the importer on the imputed items.

(4) **REGISTERED PERSONS:-** This is any organization that is registered with relevant tax authorities for VAT.

(5) **ZERO RATED GOODS:-** These are goods that ratable at 0%. An example is any goods exported out of the country. Any VAT already paid on goods or security used in producing such goods are refundable to the exporter.

(6) **TIME TABLE:-** The implementation of VAT officially commences on the 1st September, 1993. Home, registered persons were given the

whole September to adjust their accounts, particularly the incorporation of VAT information in their general ledgers, in order to comply with the requirement of the tax. That means all registered persons were to start issuing VAT invoices to their customers as from 1st October, 1993 up to date.

(7) REGISTRATION

(i) All existing manufacturers, distributors, importers and suppliers of goods and services are to register for VAT on or before 30th September, 1993 at the local VAT offices.

(ii) All manufacturers, distributors, importers and supplier of goods and services who commence business after 1st September, 1993 are to register for VAT within three month of such commencement of business.

(iii) The respective VAT payer will obtain and complete VAT form 001 (Appendix 1) and returned it to the nearest local VAT office. A permanent VAT registration number is to be given to each registered payer.

(8) **RATE OF VAT:** The VAT carries a single rate of 5% on all vatable goods and services. Zero rate is assured for export while their goods and services exempted from the tax.

(9) **INSPECTION:** This is a VAT Unit, from time to time, the premises of every vatable persons will be visited by authorized VAT Inspector from local VAT offices; such visits are:-

To ensure compliance with the valued added tax legislation in all its ramifications.

(10) **SUPPLIERS:**

(i) Definition: Supplies means any transaction whether it is the sale of goods or the performance of a service for a consideration, that is for money or money's worth.

(ii) Place of Supply: The supply of goods under Nigeria VAT was to be in Nigeria. Supplies moved outside Nigeria are outside scope of Nigeria VAT.

(a) Goods and services covered by VAT. These are goods and services that are vatable.

(11) GOODS EXEMPTED (NOT VATABLE)

(a) Medical and Pharmaceutical products.
(b) Basic food items.
(c) Books and educational materials.
(d) Newspaper and magazines.
(e) Baby products.
(f) Commercial vehicles and their spare parts, and
(g) Agricultural equipment and products and Veterinary medicine.

(12) **SERVICES EXEMPTED (NOT VATABLE)**

(a) Medical services.

(b) Services by Community Banks, People's Banks and Mortgage institutions, and

(c) Plays and performance conducted by educational institutions as part of learning.

(13) VATABLE PERSON: Vatable person is one who trades in vatable goods and services for a consideration. Every vatable person has an obligation to register for VAT payment. The registration is to cover all the business activities of the vatable persons. The person can be a Sole Proprietor (e.g. a Trader), a professional (e.g. a Lawyer) a partnership (e.g. Ibrahim and Mike & Co) a limited liability company (e.g. E. Afe Consultary Ltd. Club or Asociation, a charity organization.

(14) **VALUE ADDED TAX**

Value Added Tax is a consumption tax that has been embraced by many countries world-wide because it is a consumption tax. It is relatively easy to administer and difficult to evade. The yield from VAT is a fairly accurate measurement of the growth of an economy since purchasing power (which determines yield) increases with economic growth. VAT is a self-assessment tax that is paid when returns are being rendered. In-built in the new tax refund or credit mechanism which in VAT also makes it self-policing.

In essence, it is the Out-put Tax less In-put Tax that constitutes the VAT payable. It is the equivalent of the VAT paid by the final consumer of the product that will be collected by the government.

Although VAT is a multiple stage tax, it has a single effect and does not add more than the specified rate to be consumer price no matter the number of stages at which the tax is paid.

CHAPTER TWO

LITERATURE REVIEW

2.1 INTRODUCTION

Where as taxation is an important factor in economic planning and fiscal policy and also for economic and growth, it is perhaps the least understood and most unappreciated instrument among other government policies by the citizenry, yet they expect government to provide some services, such as provision of roads and infrastructures, (Dams and capital projects), health and cost of running government administrations, etc. This is most probably, owing to the fact that most people, particularly in developing countries like Nigeria, have very little knowledge of how the machinery of government operates.

Thus a tax man is being seen as an average Nigerian, as miniature also ready to prey on its victims or a plague tat most be avoided at all cost.

Benjamin Franklin, a philosopher, observed that "In this world nothing is certain but death and taxes". The certainty of taxes have been established long in Nigeria. Before the arrival of the colonial masters, Nigerians had been paying taxes in kind by giving farm products to their rulers and rendering free services such as clearing the bush, digging pit toilets, well etc. For the benefit of the community as a whole.

Income Tax was first introduced in 1904 by the late Lord Lugard. Various types of taxes therefore came into being through subsequent governments. Despite the facts that there are other sources where government could generate revenue to fashion a society every one can be proud of taxes, still stand very important. Probably because of their dual purpose as source of revenue and as well as fiscal policy tool frequently employed by the government.

Taxation in one form or the other is on e of the oldest institution on earth today. About 3,000 years ago a citizen in Iraq wrote, "you can have a Kind, but the man to fear is the tax collector". However, Lords, Kings and States have continued to levy taxes on persons and these persons have to live with tax collectors.

VAT has gained acceptance in many developing world following its effectiveness and role in the contemporary revenue drive. According to W. O. Ajakaiye, "VAT is becoming a veritable sources of revenue in developing countries. In sub-saharan Africa, for example, VAT has been introduced at least in ten African countries, namely Benin, Cote D'ivore, Kenya, Madagascar, Morroco, Niger, South Africa, Nigeria, Senegal, Kenya. Fragementary evidence suggests that in these countries, VAT has become a major contribution to government tax revenue. For example, according to data presented by Shalizi and Squive (1989), VAT accounted for about 30% of total tax revenue in Cote D'ivore, Kenya and Senegal as at 1982. The oil producing countries are not excluded from the list of countries introducing this tax handle. For example, available data in Tait (1989) shows that VAT has been introduced for 12.53% and 19.71% of total government revenues in these countries respectively. Ajakaiye has submitted that VAT recorded an impressive performance in virtually all countries where it has been introduced. His submission is virtually true and that may have been one of the rationale behind the decision to introduce VAT in Nigeria in September, 1993.

2.2 General Overview of Tax.

2.2.1 What is Taxation?

Taxation is as old as government, the earliest taxes being imposed merely to give the cost of administration and defense. The imposition of taxes has been one of the chief causes of discontent in Nigeria, for instance, a negative attitude has been adopted by the uninformed public towards tradition as they believe

that the money is collected and channeled into the pockets of a few. This group of people is highly opined that government move behind the revenue generation facade and lavishly squander income so generated. This, however, is a rather unfair and disillusioned motion because for one thing there are certain services which individual cannot efficiently provide for themselves as a central authority does such as the provision and maintenance of goods road, rail and other infrastructure.

The concept of taxation include, more than the mere important of compulsory sums of money by government or it agents. It is the sum total of the assessment tax, the imputation of compulsory sums of money by government or its agents, individuals and firms, the collection of and the accurately for the levied amounts and the beeping and auditory of two record.

One can rightly say it (taxation) is an important instrument of economic policy or otherwise a total of economic reformation ream being that tax reform the economically motivation. Its essence is derive from the definition of tax.

A tax is a compulsory sum level by the government or its agency on individuals, firm or on goods and services for the purpose of meeting the cost of its expenditure or for producing economic and social benefits for the public and for the purpose of controlling the economic. In other words, its essence is to raise revenue for meeting part of government expenditure.

Taxation is therefore defined: As the price of the social contract between the governed and the government for the provision of social goods and services by the latter to the former.

At times, government grant them holiday or reducer tax in order to stipulate activity in such area of the economy. Naturally, government expending results on the opposite in private opening. The revenue is also true. Hence taxation

can again be defined as: A method of transferring resources from the private sector to the public sector or effecting a reshuffle with different part of the public and private sectors.

Taxation is the most important, dependable and regular source of government revenue. It necessitates continued government existence. Whenever there is economic reform, a tax reform is apparent because of all potential source of government revenue, it is taxation (and in some cases, return on investment) that can be most being in financing public goods and services.

Taxes are two types:

(i) Direct taxes consists of company income tax, capital gain tax, petroleum profit tax, and capital transfer tax.

(ii) Indirect taxes under which food sales tax, value added tax, custom's excise, license's and miscellaneous.

A good government takes a periodic measure to maim a balance among various forces that makes for a reasonable level of economic activities inflation rate, rate of interest , money supply and foreign exchange management. Consequently, effective management of these end in higher living standards, increase production, low information rate and increase employment.

2.2.2 THE FUNCTIONS OR PURPOSE OF TAXATION.

Reasons for taxation are:

To lessen in equality of incomes. This objective has been achieved chiefly by the imposition of the progressive income tax. This kind of tax is in a pay as you earn

(P.A.Y.E.) basis. The higher a person income, the more the tax he pays and vice-versa.

i). Inequality of income is further reduced by means of subsidy, keeping down the prices of many commodities and giving such grants as children allowance. Although, there are available to both the rich and the poor, they are generally of most beneficial to low-income groups.

ii). To combat inflation: Inflation occurs when the money in circulation far exceed the available goods and services. To remedy inflation, government would increase its expenditure. For instance, an increase in personal income tax would reduce people dispensable incomes. This can, however, only succeed in suppressing and not eliminating inflation.

iii). To check particular production and consumption of commodities, heavy taxes are imposed on commodities which are considered harmful and luxurious. This lead to higher selling prices, the resultant effect being discouraged consumption. Where this happens, less of such goods are likely to be produced. Harmful goods which are usually taxed include alcohol, tobacco and luxurious goods would include brands of cars and clothing material among other things.

iv). Taxation policy can be used to stimulate from a trade depression or to remedy a deflationary trend. During a trade depression, aggregate spending is low, leading to high level of unemployment. What the government does is to decrease direct taxes, as a tax reduction or abolition increase money supply in the private sector and stimulate activities or investments in the affected areas with attendant benefit, such as increased production and employment.

v). It corrects an adverse balance of payments deficit. The importation of

foreign goods (especially non-essential by the use of tariffs. This lowers demand for such goods thereby conserving foreign exchange. Hence, a remedial effect in the balance of payments. On the other hands, less tax is imposed on exports.

vi). Government employs tax to protect infant industries. Young industries at a developing stage cannot compete with foreign firms. To protect them, therefore, high tariff halls are set up against the importation of similar goods produced by the infant industries. This increases the price of imported goods, making them less competitive. Without this function, imported goods could compete against domestic goods and so shifting the income industries at birth.

vii). Revenue generation: Government needs a lot of money for the provision of essential services and the finance of its projects. Money is spent on such things as defense, maintenance of law and order, provision of social amenities and infrastructures as its major sources of revenue, government taxes to meet the cost of providing these, since it is not self-sufficient.

2.2.3 ECONOMIC EFFECTS OF TAXATION

Taxation Policy has quite a number of effects on the economy, such effects could be positive or adverse, depending on the economic conditions, some of these effects are as follows:

(i) Taxation may encourage inflation: This is otherwise called or referred to as effect on the price level. Where, for instance, tax is charged in input of the production sector, prices are likely to go up without an equal match for goods and services demanded. This tends to make the market scenario sure and comfortable.

(ii) A deterrent to work: Hence direct taxation can act as a serious check to production, especially when closely linked with current earnings by encouraging absenteeism, and making men disinclined to work. This will set up a chain of reactions which will increase price of goods, since there is no incentive to those involved in the production such can also lead to a higher level of unemployment as some people would be laid off, and also to under employment of resources – material and human.

(iii) A deterrent to enterprise: Economists condemn taxes on profit as they (taxes) are considered to be a check on enterprise profits are rewards earned by successful enterpreneurs. Enterpreneurs, they argue embark upon risky undertaking.

(iv) A deterrent in saving. Taxation will generally reduce people's ability to save because their disposable in incomes could fall. We must bear in mind however, that this will not always be the case, and will depend on the purpose for which people are saving. Personal income earn discourage consumption and as before mentioned, leads to a low level of productivity as there is no encouragement produce in large quantities.

2.2.4 Taxable Capacity:

it is difficult to determine what the taxable capacity of a nation is, but this is not unconnected with the purposes to which the revenue is put. If the essence of taxation is to enhance the power of state to allocate resources for the citizens, then it may that a symbiotic link exits between fiscal power and tax compliance. The extent to which the tax bares
(a TAX BASE refers to the item or object which is taxed) can bear the burden of taxation without a rupture of the fiscal symbiosis is what is known as TAXABLE CAPACITY.

From the macro – economic stand point this capacity determines the tax Potentials of a nation as well as the compliance tendency of the citizens Especially with regards to per capital income, size of the urbanization Literacy and especially all moral, nation and compliance cost.

The limited of Taxable capacity must be the point beyond this additional Taxation could produce economically harmful result that the gain to the Community from the use of the money raised by taxation.

2.2.5 PREVIEW OF THE NIGERIAN TAX SYSTEM.

The Nigerian tax system is among the systems adopted by the member Countries of the Common wealth Tax Association (C.T.A) unlike most countries of the association, which operates unitary system of government and therefore operates a one tier or unitary tax system, Nigeria operates a federal system of Government to legislate on all income taxes which is an exclusion matter while the administration is two-tier with the federal government collecting taxes principally from the limited liability companies (e.g. Companies Income Tax and petroleum profit tax) and VAT Decree No: 102 of 1993 the state collect taxes from the individuals on the basis of residence, federal collected taxes are paid into the distributable pool account (Federal Account) and shared between the Federal, State and Local Governments.

In addition to income from the above sources, the state and federal governments have jurisdiction on some other taxes which they collect and kept for their own primary use. In the case of the states, they are statutorily obliged to give a determined share of collections from these sources to the local governments. For instance, the federal government collects personal income taxes from the Police, Armed Forces, External

Affairs. Abuja resident individuals, non-resident individual and any other taxes or charges/duties from Abuja, the Federal Capital Territory. The Federal Government uses monies from these sources which are paid into the consolidated account, to run designated and other expenses without sharing the proceeds with the other governments, whether state or local.

For the state government, other sources of income proceeds from personal income tax (such as Pay As You Earn) from workers living in the state and registered for the purpose, and license (stamp duties, vehicle, driving, hacking, rates, etc.). A part from each state being statutorily required to give to its local governments a certain percentage of proceeds from these source each state keeps the balance for funding its activities.

The local governments which are the third-tier of government administration in the national setting, have other sources of extra funds through the operation of some business ventures – transport, housing, markets, rate like motor parks, sanitation, certificates and licenses and other levies. Despite the contribution from the states and from the internal local sources, the bulk of the income of local government is denied from the direct monthly statutory allocations from the federation.

In the Nigerian Tax System, requirement forming the obligations (primary, that is) of the tax payer are therein the tax payer must:

i) register for tax payment,
ii) determine the amount of tax payable,
iii) pay correctly and on time all taxes due or withheld in payments made including tax penalties,
iv) file a return in respect of taxes payable,

v) keep and produce on demand all books of account, records documents and returns necessary for the ascertainment of tax liability,

vi) answer all queries and attend to notices or summons served by the tax authorities,

vii) co-operate with and allow tax officers full access to premises office to search or remove anything required for investigating tax chargeable or bringing up a case in the Law Court,

viii) give information of any other person or company specified in as notice by the tax authorities,

ix) (in the case of banks) supply in within seven days after the end of each month, a list of the names and addresses of all new customers,

x) pay to the tax authorities all part of any amount of money due to a company or person who has defaulted in his tax obligation, if the tax authorities so direct,

xi) have a representative or tax officer designate to answer all questions of tax payment (companies income tax),

xii) do any other thing as may be required by the tax authorities for a month, administration of the tax policy.

The tax structure of the tax system influences in a multiple way, the nature and quality of compliance. Tax structure determines tax payer's response through its capacity or instigate people to handover their private resources to the state in forms of social contribution.

In practice tax system admit when may be called partial compliance. Under company income tax law, for instance a taxpayer may (in spite of the primary obligation that he must pay correctly and on time all taxes due') make part payment of tax. In the Nigerian VAT system, an importer who imports goods

may this imports 'zero-ratio" (that is, non-taxable in spite of the statutory provision that only exports are zero ratio. In any case, in as much on weaknesses are formal here and there, the Federal Inland Revenue Services (FIRS) is not just sitting with its arms folded. On the contrary, they monitor the operation of these taxes, especially the Value Added Tax (VAT) which may study is concerned through the use of private consultants in order to enforce compliance.

2.2.6 BRIEF HISTORY OF VAT IN NIGERIA

T he year 1991 was a major law make in the tax administration of Nigeria. In that year, Professor Edozien – led study group on the review of the Nigerian tax system. Firstly he identify the need to transform the sales tax that was then administered by the state government, within the same year1991, a parallel study group on indirect taxation was led by Dr Sylvester U. Ugoh who given the responsibility to study the feasibility of introducing VAT in Nigeria as an improvement on the existing sales tax.

After a series of studies and research hours to both outside and within the country, the Ugoh group came up with a firm recommendation in November, 1991that VAT should be introduced in Nigeria after two years of preparatory work. As a follow up, by 1992, the Ijewere led MODIFIED VALUE ADDED TAX committee was set up to undertake the preliminary work for the introduction of near tax. The committee was later to in close collaborations with Federal Inland Revenue service in 1993 for the later to take over the administration of tax was about to start.

But on a critical look at what VAT entails, the efficient operation of the tax calls for high level of expertise in auditing similar to that of income tax and very far from the other form of sales tax. Moreover the information obtained from VAT returns is very relevant and useful to enforce income tax. Such information is

only possible if the two taxes administered by the same organization. All these considerations tend to form a united administration under same organization for both income taxes and VAT today including Nigeria.

Rather than engaging in the required preliminary work to put the new tax properly in stream, the MVAT committee started to canvas for an elaborate separates commission. Unfortunately, government did not farn this slaid . The memorandum, which presented this view to the government, was registered in December, 1992 in it entirety while the giver accepted the introduction date of June, 1993 for the new tax. Consequently, government directed Minister of Finance to commence the new tax in an experimental scale with small outfit within the ministry of finance.

By that same 1993, the Honorable Secretary, Minister of Finance in the national Government, Prince Oladele Olashore saw the need to commence the implementation of the new tax without further delay. He therefore directed the MVAT committee to liase with the Federal Inland Revenue services (FIRS) the agency responsible for the administration of Income tax in the ministry of Finance, for a smooth handling over of the preliminary work done so far on the assignment of the committee. The MVAT committee finally would up it midwifery activities in June 199, when (FRS) fully took over the unimplementation of the new tax.

The issue of appropriate VAT rate caught the attention of the visiting World Bank team in 1993 while reviewing the Nigerian VAT proposal. The team advocate for a higher rate of between 15% and 17% as opposed to the propose rate of 5%. Its argument was that the rate of 5% would produce paltry revenue of about 4 to 4.5 billion Naira in the first year. Government was not impressed by that proposal and preferred to start a new tax under a depressed economy with attendant social problems with a very low penetration rate to avoid public resistance. The first year collection of over N18 billion from VAT in 1994 was

vindicated government stand on the matter. The VAT decree was sign into law on the 24th August, 1993 and it was to commence on 1st January 1994.

CHAPTER THREE: CONCEPTUAL FRAMEWORK.

3.1 Introduction.

A decision to whether or not to introduce a VAT for some countries has always been difficult, but incase of Nigeria, the decision to introduce VAT has been made easy by the state of our economy. These was overriding need to broaden the base of government revenue. As it were Nigeria dependence on oil revenue not make for economic stability since it make her future depends almost exclusively on the international price of oil which is not under Nigeria control.

The actual introduction of the tax was made easy for Nigeria since with tax law, rather than being debated in parliament was merely decreed into existence. The decision to introduce VAT would have been harder through tax law since the tax was new to Nigeria.

Introducing VAT in any country, there are many choices to make – these choices are usually difficult to choose from but they have to be considered, some of these choices are:-

(1) What type of VAT to implement:
Whether Consumption tax, Income or Gross product tax.

(2) What department to handle VAT or Income tax, is it customs or a Separate commission.

(3) Whether to go by tax exclusive pricing or the tax inclusive pricing System.

(4) Or even, whether to introduce VAT or be content with one of its less attractive alternatives.

All the above choices and a host of others have to be considered in introducing VAT. In the light of making this decision, the Federal Ministry of Finance, it

appears, ha effectively the VAT goods by professionally and surprisingly making the tax work in Nigeria in spite of potentials odds. The effectiveness of VAT is the teeth of trenchant. Fiscal disequilibrum, social instability and suffocating down ban in the market place ha approved that the tax system is solid and effective.

3.2 THE CONCEPTUALIZATION OF TAXATION IN NIGERIA

Tax has been variously defined by various people. The following are a few of such definitions.

A compulsory contribution of the wealth of persons for the services of the public. Tax can be define as "compulsory contribution to the support of government levied on persons, property, income or commodities, transactions etc. How at fixed rate mostly proportionate to the account on which the contribution is levied" Tax is define as compulsory contribution from person to government to defray the expenses in the common interest of all without references to special benefit conferred.

Taxation is therefore a process of levying and collection by public authority, with proper of compulsory contribution from person or group of persons to defray the cost of its activities. It is one of the economic devices used by the government towards the maintenance of the country in terms of providing some social amenities needed by developing areas. Redistribution of wealth levying tax has objective or function of redistributing wealth. The doctrine that taxation should be based on ability to pay and the diction that the rich should be taxed more, e.g. it is in progressive tax, base credence to this, taxation objective and functions, its also serve as management of the economy. Taxation can be used to alter the aggregate level of demand, and hence control inflation or deflation, other mechanisms such as credit control and the raising of welfare payments are other useful devices which can be used, to stabilize the economy. Finally,

taxation used for achieving a specific purpose such as discouraging consumption of a particular commodity, e.g., alcohol, cigarette or to encourage the production of a particular commodity, e.g. tax free holding.

Nigeria tax system is essentially a derived of historic economy structure and political economy of that country. There are two components of the Nigeria tax system.

1.) The law governing taxation and it's the law that provides the framework for the due administration of tax. The administration of tax law occupies a unique portion in the tax system.

2.) The law determine the liability of the tax payer, the rate and base. It should be noted that while a good tax law is important to a good tax system, good administration is since non to the attainment of the overall good of the system. A country's tax structure is of its economic, political and social circumstances. In Nigeria, tax structure demonstrates the following features:-

(i.) The tax base is too narrow (the base is the basis of taxation, i.e. what is to be taxed). If someone's income is N5,000, what will be his tax base.

(ii.) The types of taxes that are being administered are very few. For example, capital gain, and capital transfer taxes, though have legal provision.

(iii.) There is the general predominance of indirect taxes, particularly in import, but this actually changed with the giving influence of petroleum profit tax.

(iv.) The proportion of tax revenue as proportion of national income is very small. These are many reasons why Nigeria has the type of structure

described above which are:-

(a) Income level is very low because of low level productivity, general low level of education activities, most of which are at subsistent level.

(b) Excise duty cannot be broadly used because manufacturing activities are narrow and restricted to monitor house hold goods and production scale is low that is why excise duty was abolished In 1998 budget report so to reduced the price of domestic manufacturer industries so as to reduce cost of production and reduce the unit prices of the company product.

(c) Company Tax seems to be imposed only few large public companies as most other companies do not render accurate accounts. Moreover, the holidays and generous excursion are being granted to encourage industrialization and investment.

(d) There is the predominance of self employment and lack of suitable accounts which the tax authorities can rely upon.

(e) Marketing of properties is largely under-developed and as such it is difficult to calculate capital gain tax on such properties. The only exemption are the capital gain tax on shares that are traded through the stock exchanges.

(f) There is the lack of technically qualified tax personnel and administrative set up for the efficient functioning of the tax system. Because of poor remuneration in public sector, it has been difficult to attract and retain technically qualified personnel.

(g) Finally, there are high incidence of tax avoidance, tax evasion and tax laws for exerting penalties on these tendencies are not generally involved.

Another way of understanding what taxation is all about is through the classification of taxes into a number of classes. Taxation can be classified based on transaction under the followings:-

(a) Income Tax: This is a tax imposed on the income of individual or institution. Here we have personal income tax, company income tax.

(b) Capital Tax: Tax imposed on the holding or capital of institution or individual, e.g. we have capital gain tax, capital transfer tax.

(c) Expenditure Taxation: These are taxes, imposed on individual disposable income or institutions. This also can be classified based on traceability of burden. Under this we have:-

Direct Taxes: There are taxes on income or receipts and of such taxes fall directly on the payer in that it is not possible for the person who pays the tax to shift the burden to someone else. Examples of direct taxes are personal income tax, capital gain tax and company profit tax. As a fiscal instrument, direct tax can be used to adjust people's disposable income and reduce the area of unnamed income as previously discussed.

Moreover, direct taxes build be used to redistribute income and this bring us in the different firms of direct taxes.

i) Progressive Tax: Under progressive tax system, the higher the tax base, the higher will be the tax rate. The rate of taxation is

graduated progressively as income increases. Most countries adopt progressive tax in their personal income tax because bit reduces in equality of income and increases aggregate demand. Also progressive tax is non-inflationary and could yield more revenue to the government than regressive of neutral taxes. However, progressive tax may lead to disincentive to efforts as people pay exorbitant taxes in addition to their additional incomes after certain level.

(ii) Regressive Tax: This is the exact opposite of progressive tax. The tax rate diminished as income level or tax base increase so that low rate of tax is paid at high level of income. Regressive tax has the main advantage that it creates incentives to efforts but some of its demerits include the tendency to widen angularity of income in the society. Also aggregate demand may become the extra income that accrues to the rich man is saved rather than spent and this will discourage investment in the economy. Regressive tax is handily used in real situation.

(iii) Neutral (or proportional tax): Neutral tax does not take of the economic situation of the tax payer and the tax is proportional to the tax base or income at a constant rate. Neutral tax has the advantages that it is impartial and does not lead to disincentive efforts even though it does not provide incentive either. It can however, be criticized in the sense that it is insensitive to the economic situation and it is also against the spirit of social equity.

INDIRECT TAX

An indirect tax is a tax on expenditure or outlay and it is possible to shift the tax (either partly or wholly) to someone else. Example of this, is import duty. When

an Importer pays tax (import only) on goods imported, the tax will be added to the cost, ultimately pay the tax, i.e. the buyer pays the tax indirectly through the imported goods. Indirect tax can be avoided because it is payable only if one buys a tax invested commodity.

For example, if you do not buy imported commodities, you will not pay any import duty. This distinguishes it from some direct taxes like personal income tax which affect all income earners.

Other indirect taxes include excise duties (taxes paid on home-made goods), purchase tax, value added tax (VAT) etc, custom duty consist of both export and import duties although the later is usually emphasized in countries where import predominates.

Taxes could also be grouped into two types: Hence we have company income tax, capital tax, community tax, etc. Sources of these form have already been discussed in forgone discussion but some are going to be discussed here:-

a) Petroleum Profit Tax (PPT):

This is one of the most important feature in income taxation in Nigeria reasonable revenue generated for the government through PPT. It is levied on profit of all companies that engage in petroleum. Tax is levied by deduction in respect of certain royalties relating to oil extracted. By virtue of the Petroleum Tax Act of 1959, the Federal Board of Inland Revenue is rested with the responsibility for assessing and administration of PPT. The rate of tax on oil companies is assessed by sharing the realized profit on equal brain in such a way that government total annual revenue and it accounted for the bulk of total tax revenue from both direct and indirect sources.

b) **Community Tax**:

This is a source of internal revenue to local government authorities. But according to law, community tax is a state tax with local authority merely acting as collecting agents. The proceeds arising from the payments are usually shared between two parties. This type of income tax was abolished in Kwara State during the political civilian regime between 1979 and 1983. The poll tax was however re-imposed during military regime.

c) **Capital Transfer Tax**:

This tax is levied on properties transferred from a deceased to another person or persons being the inheritors either by virtue of birth or through the deceased will before his death. Before changing the rate allowance is granted in respect of expenses incurred in the sale of the property.

The payment schemes available for personal income tax include:

i) Payment of tax through pay as you earn (PAYE),

ii) Payment through direct assessment.

Tax payment through PAYE system are required to be deducted at source from income such as salaries, dividends, emoluments of employees and pensioners, dividends, and pensioner rent paid etc. Since there is no of value at that time.

From 1954 to date, various tax laws have been made by Resiman Fiscal Commission in 1958 which later became part of 1963 constitution in Nigeria.

The 1979 constitution further classified rather regarding the manner of imposition of income tax. For effective administration of taxation, the joint tax board was set to the general administration of the act in the Federation. At the state levels we have state tax authorities responsible for the operation of personal income tax in their respective territories. The general body of law of taxation in Nigeria is the income tax management act (ITMA) and the company income taxation act (CITA).

Prior to 1954, the taxation of Nigeria was in the hand of the native authorities who tax their subjects differently, that is different from one ration to the other looking at the tax system in Nigeria today. It has achieved some major principles and satisfied the main common underlying taxation:

(i) Economical: The tax system should be so contrived as both to take out and to keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state. In other words, cost of realizing or collection of tax should less than what is actually generated or realized, tax should be inexpensive to administer.

(ii) Equity and justify: The burden of taxation should be spread as fairly as possible having regard to ability to pay. Tax on personal income is under progressive system of taxation by which process the effective rate of tax in income increases as tax of the owner of a large income is made to contribute to large portions of the difference as tax than the common income.

(iii) Certainty: The tax which each individual is bound to pay ought to be certain and non-arbitrary. The form of payment, clear and plain to be contributor and very other persons i.e. tax payer should b certain when payment is made.

(iv) Convenience of Payment: Every tax ought to be levied at the time, or in a manner, mostly likely to be convenient for the contributors to pay it. *Conveniences of payment requires, among other things, that the object* and time of collection of the tax be related to the habit of the people.

3.3 Taxation As Source Of Revenue In Nigeria:

Raising revenue for the government was the original and still remains a significant purpose of taxation. In Nigeria, taxing power and tax administration is shared between the federal, state and local governments. The allocations of taxing power are specified in the constitution as earlier mentioned. Historically, the allocation of this power was arrived at, from the fiscal commission that was set up. The federal government have limited and relatively less productive tax power. The revenue collected by the federal government is shared among the various levels of government through a distributable pool account on the basis of the various fiscal commission and decrees. The term source of revenue is the way by which money is being collected in any given area. The major sources of government revenue is taxation of which VAT is one of them.

The federal government in its 1995 budgets of revenue sought to realize N8.6 billion revenue from VAT between January and December 31st 1994. According to the federal government "Government is now shifting its emphasis from income tax to the tax on consumption (VAT) which is less prone to tax evasion and it is progressive in nature.

About N12.3 billion has been realized from the operation of VAT between January and August in 1995 said Mar J. K. Naiyein who was then the Chairman of the joint tax board (JTB). He describe VAT as "The most

successful economic item in the market because it had not only yielded revenue erosion". Revenue from VAT is shared among the ties of government. In 1998 N57.45 billion was generated from VAT, which is more than the N55 billion that was projected see the below table of VAT generated up till 1998:

YEAR	AMOUNT	TOTAL
1993	N8.6 billion	N8.6 billion
1994	N12.3 billion	N12.3 billion
1995	N30.0 billion	N30.0 billion
1996	N48.20 billion	N48.20 billion
1997	N54.30 billion	N43.30 billion
1998	N67.45 billion	N67.45 billion
1999	N/A	N/A

Source: FIRS/NAT Directorate: Abuja

The objective of Value Added Tax (VAT):

- To elongate the tax bone by bringing in those who ordinarily cannot be reached through direct taxation.
- To reduce consumption of luxuries and
- To curb increase in the consumption of non-essentials.

There, indirect tax on consumption like the Value Added Tax will prevent consumption from moving as fast as income. When the income of the pay rises, their original propensity to consume will also rise as much as the increase in income.

Therefore, the gains of increase in productivity will lead to the increase in income would have been wiped off by the rapid rise in corruption. In order to prevent this situation and free some factors of production for the purpose of investment, a consumption tax is levied to restrain consumption.

Value Added Tax is a neutral tax because it makes no distraction between capital and revenue, goods and services, between exports and imports or between efficient and inefficient businesses, except for products that have been exempted or zero-rated. All goods and services purchased by him qualify for tax credit.

These are four possible ways of levying Value Added Tax (Tait 1988), but the most popular method is the tax in input, normally referred to as the invoice or credit method: The advantage of this method is that it associates. The tax liability with the transaction and provides good audit trail.

Although, technically, tax is changeable in goods and services produced, the object of tax in a value added tax structure is a "Vatable Person". A vatable person can be defined as one who carries on economic activity as a producer, wholesaler, trader or supplier of goods or services. A vatable person does not bear the tax liability himself because whenever he purchases goods or services, the suppliers invoice entitles him to claim credit for tax shown in the invoice. At the end of each accounting period (monthly, quarterly or yearly depending on the country) the vatable person will send to the relevant tax authority vat return showing:

- Total tax on all inputs purchased by him in the normal course of his business.
- Total tax on all the final product i.e. goods and services supplied by him (output), and
- The difference between the two.

If output tax exceed input tax, the difference is sent to the tax authorities with the valuable persons return. On the other hand if input tax exceeds output tax he claims a refund. This self assessment and self enforcement in collection mechanism is unique to value added tax and make the concept very simple from the stand print of return preparation and Government Administration.

3.4 THE ROLE OF VAT IN NIGERIA

The role of VAT cannot be over-emphasized since taxation as the exercise of any governmental power is only a means to an end. An approval of the role of VAT in Nigeria and as it affects the economy, therefore, expected to unravel the extent to which it has assisted the state to pursue its objectives. Before delving into full scale appraisal of the Nigeria VAT, it is perhaps plausible to say there are, so far, no universally accepted yardsticks for measuring the role of any tax. This is because socio-economic situations vary from one economy to another. In assessing the role of a nationwide federal tax (as VAT), therefore, the following points should be borne in mind:

i) The Nigerian tax system is a reflection of the federal political frame work of the country.
ii) The value added tax is an improvement on the states-administered sales tax.
iii) The value added tax was introduced in Nigeria at a time of political instability, rising inflation and general fiscal pessimism.
iv) Many taxes were in operation at federal, state and local government levels when VAT was introduced.
v) The introduction of VAT was to eliminate the multiplicity of taxes at various levels of the government.

Since a tax system cannot be insulated from its social context, hence the role of a tax is beyond that of revenue generation alone, hence we can take the earlier mentioned five points as a yardstick for ganging the assessment on social and micro-economic level.

However, we shall now attempt to examine the role based on the following measures:

a) Budget Objective:

An exclusive appraisal of the tax can only be valid on two grounds. In the first place, it can be relied upon on the basis that government is well informed of micro-economic variables including the potentials of VAT, and is in control of such externalities as the political system, the rate of inflation, and the overall tax system. In the second place, an exclusive appraisal that the degree of under or over-estimation of the tax potentials is not too disproportionate to the tax capacity of the economy or the tax base. The more realistic the tax estimates are vis-à-vis the taxable capacity, the easier it is to assess tax effort. This argument is pinned on the fact that because most developing countries lack reliable economic data, fiscal objectives alone might be insufficient in appraising a tax since economic planners might over or undervalue the policy due to certain (economic or non-economic) reasons. In fact, since economic objectives are to a large extent political objectives should be desegregated for a reliable application of economic parameters in assessing a fiscal policy. Tax scholars rarely over bother themselves within such an exercise.

The post plausible index of the capacity of the VAT to accelerate economic growth is it effectiveness in mobilizing the privately held resources, which automatically should boost public revenue, enhance consumption patterns and general savings. In the pilot year of administering the tax, the Nigerian Government estimated that as much as N6 billion should be the target revenue. This means that the tax was projected to achieve in only 6 months about 150% of what the general sales tax achieved in about four and half years; and to realize in only one year about 30% of the yield of the sales tax in nine years (1986 – 1993).

b). **Comparative Appraisal:**

This trend is to compare the taxes in the same tax territory. This has enabled governments and experts to analyze the fiscal system to identify the most productive, the less productive and the least productive taxes. In as much as one of the operations of the Nigeria VAT is to reduce the inert taxes and insidious tax rate in the system, it is necessary to assess the tax by juxtaposing it with other taxes. The fewer the most effective the role of states in a country, the easier to identify the least productive once and used them out and also the easier its overall administration. For every country including Nigeria, aims at running a tax system in which a few taxes exist and meet government fiscal objectives.

The followings are some of the Federal Taxes being administered by the Federal Inland Revenue as mentioned earlier these are:

i). Petroleum Profit Tax (PPT), Companies Income Tax (CIT), Personal Income Tax, Capital Gains Tax (CGT), Stamp Duties, Value Added Tax (VAT).

Significantly in this regard, VAT has achieved much in harmonizing the tax system and causing the reduction of inert taxes and tax rates within few years in operation. Specifically, as a result of the productiveness of the tax, government was compelled to ban many petty taxes which where administered in the various parts of Nigeria by the mounting of road blocks by council officials. In January, 1995, VAT caused a further reduction of the highest and lowest bands of the rate of personal income tax from 35% and 10% to 30% and 5% respectively. Again, the 1996 budget which was laden with tax incentives continued to reflect the positive role of VAT on the entire tax system, for acceding to the government the reduction in the company revenue tax from 35% to 30% with effect from January 1996 was made as a result of financial receipt from VAT.

c) **Compliance Gap:**

We can also appraise the role of VAT project when we examine the gap between the actual revenue and the potential revenue vis-à-vis how the different tax bases comply with tax laws.

Prior to the commencement of VAT in Nigeria, the government had gathered, processed and digested many data about the feasibility of the tax, it operational demand and dynamics, as well as how these squared with the nation's overall fiscal goals, since Nigeria's Gross Domestic Product stood at N100.98 billion in 1991 and about N103.2 billion in 1995 when VAT revenue estimates were N5 billion and N12 billion respectively. It can be argued that the VAT revenue estimates were not an underestimation of the capacity of the economy to welcome the tax. Of course, the estimated revenue of tax does not necessarily determine its actual revenue. If the revenue estimate may be as low as 70% or even 60% of the N9 billion. The reason is that a tax need not necessarily achieve in a given fiscal year all that might be desirable of the tax. Some tax scholars have explained that, particularly in the case of developing nations taxes, the effective base might be just a fraction of the potential base.

Perhaps this explains why inspite of the large number of business organizations in Nigeria, and inspite of the systematic tax mobilization effort, the active VAT base was rather small at the inception of the tax system. By December, 1999, total registered VAT agent were only 60,681. Most of the agents were city or town based while the largest VAT responsive areas being the commercial and industrial centres of the country. Efforts are continually being made to bridge compliance gaps,

the relative proportion on inland VAT revenue to the total VAT revenue is indicative of the level of success of the tax efforts.

d) **Enforcement Index**:

One of the inherent of VAT was it role of self-assessment. This means that the tax payers have to determine their tax ability, while tax administration retain the enforcement power to compel compliance with the tax laws. So far, the Nigeria VAT has been administered with full cognizance of the ideals of self-assessment in taxation. That is in turn with the FIRS philosophy that, not withstanding the provision of Part 11, Section 7(2), and Part VI, Section 40, of the VAT Decree 102 of 1993, the goals of tax administration should be to encourage voluntary compliance. Hence for VAT the administrators have and are using their enforcement power so much that the amount realizable each month is not lost to litigation time and cost.

e) **Erosion Index:**

By erosion in taxation is meant the nullification of the revenue performance of a tax base through such loopholes as smuggling, corruption, personal exemptions, zero rating, tax holidays, evasion and so forth. The performance of an eroded base equals non-compliance.

The proportion that erosion is a diagnostic test of the role of VAT as a tax system holds true particularly in developing countries when tax bases are usually officially and unofficially wipe off through personal considerations, un-enforced laws and a large unaccounted for underground economy. Even tough, in Nigerian VAT project these have been a lot of exclusion seekers among the large taxable entities. So is a testimony to the commitment of policy makers that, despite the prodding that VAT

administrators have generally kept down the volume of official erosion of the tax base. There is virtually no group of exclusion seekers that has its VAT status altered as a result of lobbying. This of course is a positive role as far as revenue generation is concerned in the Nigerian economy.

f) **The Basis For Success:**

It is not enough to evaluate fiscal policy on specific touch's times. The reason of the success or failure of the policy, seen in the context of the evaluating carrier criteria, deserve a particular analysis. Below are the basic – definitely not all factors that contributed to propelling the introduction of VAT in Nigeria to its logical role. Some of these factors are:

1) **Groundswell Opinion**: i.e. the tax payer's opinion as it reflects in the tax system.

2) **Publicity:** i.e. a consumption – oriented levy such as VAT must necessarily be seen as a commercial product that must be sold to the largest buyers.

3) Management by objectives: i.e. the tax payer that pays his tax does not implicitly buy an (abstract) articles, obligation on the part of the tax–collectors to report to the tax payers how much he collects, as well as the obligation of the government to be payer – conscious in management tax matters in the provision of the desired social goods and services.

4) **Feasibility:** i.e. Vat had been adjusted to tide over socio-economic down-turn forced the temporary exemption of petroleum products from the tax.

5) **Simplicity:** i.e. VAT devices most of its operational impetus from its simplified framework. This even fairly educated Account Clerk do understand application of VAT to transactions.

However, there are still a lot more of the factors as it all depends on what perspective one tends to look at it.

3.5 VAT AS REPLACEMENT OF SALES TAX

Sales tax is an indirect tax levied on luxury goods and services governed by the sales tax edict of 1985 and the Federal Government Sales Decree No 7 of 30th June, 1986, which sought to united and streamline the operation throughout the country. VAT is progressive form of taxation as distinct from sales tax. That is, the more you consume the more you pay. VAT does not make it easy for a person not to pay at one stage or the other. Unlike in sales tax where a person not concerned about the end product of the goods may not necessarily pay sales tax. VAT according to Amadu Awa "is a tax imposed in the value which is added to goods and services as they pass in through the various stages in the business chain by registered persons in the course of their taxable activities up to the final consumption. The net effect is that VAT is paid by the find consumer while the registered person in the course of their taxable activities up to the final consumption. The net effect is that VAT is paid by the final consumer while the registered person's role in the process is to collect the tax for the Federal Board of Inland Revenue (FBIR).

The VAT which took effect from 1st September, 1993 has to replace the then existing sales tax which has been in operation under the Federal Government legislated decree No. 7 of 1986. The rationale behind replacing sales tax with the value added tax is informed by a number of factors and consideration notably:-

(i) The base of sales tax in Nigeria as operated under Decree 7 of 1996 is narrow. It covers only main caliginous of goods and services in registered hotel, motels and similar establishment.
The narrow base of the tax negates the fundamental principles of consumption tax which by nature is expected to cut across all consumable goods and services. VAT base is broader and includes most professional services and banking transactions which are high profit generating sectors.

(ii) Only locally manufactured goods were targeted by the Sales Tax Decree of 1986, although this might not have been the intention of the law. VAT is in this regard, a considerable part of the tax to be realized from imported goods. This means that under the new VAT, locally manufactured goods will not be placed as a disadvantage relative to inputs.

(iii) Since VAT is based in the general consumption behaviour of the people, the expected high yield from it will boost the futures of the State Government with minimum resistance from the payers of the tax.

(iv) VAT is broader, conversing most professional services and banking transactions. Besides locally manufactured goods will not be placed at disadvantage relative to imports.
The nature of VAT is such that it is a consumption tax that has been embraced by many countries world wide, because it is a consumption tax, it is relatively easy to administer and difficult to evade.
The yield from VAT is a fairly accurate measurement of growth of the economy since purchasing power (which determines yield) increase with economic growth. VAT is a self-assessment

tax that is paid when returns are being rendered. In building the new tax is the refund or credit mechanism in VAT also makes it self ""elf-policying"" It constitute the VAT payable.
It is the equivalent of the VAT paid by the final consumers of the product that will be collected by the government.
Every valuable person is to remit to the relevant local VAT office the net VAT payable which is the excess of output tax over the input while filling the VAT returns. Remittance are supposed to be made together with VAST returns file. In other words, the draft for a month in collection is to be submitted along with the returns. The bank certified cheque or draft should be drawn on "Federal Government of Nigeria – VAT ACCOUNT". VAT returns (and payments are normally made monthly to the local VAT office on or before the 14th day of the month next following that in which the supply was made. VAT carries a single rate of 5% on all ratable gross and services. Zero rate is assumed for while these are goods and services exempted from the tax. See the below diagram in figure (1) which shows the collection of multi-stage Vat at 5%.

SALES PRICE
(before VAT)

Supplier's Price **N1000**	**Raw materials Supplier** **Sales Price - N1050** **(inclusive of VAT**	**BY SUPPLIERS** **VAT COLLECTED – N50** **LESS: VAT PAID - N00** **VAT PAYABLE - N50**

Manufacturer's Price N1500	**Manufacturer's Sales Price - N1575 (inclusive of VAT)**	**BY MANUFACTURER VAT COLLECTED - N75 LESS: VAT PAID - N50 VAT PAYABLE - N25 BY MANUFACTURER**
Wholesaler's Price N2000	**Wholesaler's Sales Price - N2100**	**VAT COLLECTED - N75 LESS: VAT PAID - N50 VAT PAYABLE - N25**
Retailer's Price N2500	**Retailer's Sales Price - N2100**	**BY MANUFACTURER VAT COLLECTED- N125 LESS: VAT PAID –N100 VAT PAYABLE - N 25**

CONSUMER PAYMENT TO RETAILER - N2100

TOTAL VAT PAID – N125 (i.e. 5% of N125)

SOURCE: Federal Inland Revenue Service Information Circular Serial No: 9304. Nigeria.

3.6 TAX ADMINISTRATION AND POLICY IN NIGERIA

The VAT system in Nigeria is administered by the Federal Inland Revenue Service (FIRS). The VAT Directorate within FIRS is centrally located at the Head Office in Abuja with a network of Zonal and Local VAT Offices throughout the Federation.

Although VAT is administered centrally by the Federal Government by using the existing tax machinery of the FIRS in close co-operation with the Nigeria Customs Service (NCS) and the State Internal Revenue Services (CIRS), the net proceeds from the new tax is due solely to the State Governments after making an allowance of 20% to cover the cost of administration. In effect, the State Governments will benefit to the tune of 80% of the entire VAT collection.

However, the introduction of VAT brings an innovation to tax system in Nigeria. We have relied for too long on direct assessment for generating revenue from various level of governments. This has limited the growth, vis-à-vis

government's desire to increase local amenities to the generality of the people. It is generally accepted that VAT has a wider base and will result in higher tax yield and its growth will go in line with consumption pattern of vatable goods and services. VAT replaces the sales tax. Sales tax had been managed and administered by the Federal Inland Revenue Service (FIRS) and the relevant revenue accruing from there will be distributed between the Federal Government and State Governments, with the allocation to FIRS to take care of the cost of managing the tax.

The VAT system in Nigeria is administered by the FIRS. The VAT directorate within FIRS is centrally located at Head Office in Abuja with a network of Zonal and Local Office throughout the federation as earlier mentioned. The net proceeds from the new tax accrue solely to cover the cost of administration.

The policy guidelines governing the implementation of VAT in Nigeria are based on the following submission. VAT is a tax on spending. The tax is borne by the final consumer of goods and services because it is included in the price paid. The tax is at flat rate of 5% and the tax is collected on behalf of the government by business and organizations which have registered with the FIRS (FIRS VAT DIRECTORATE) for VAT purposes. A business or organization which has registered for VAT is classified as a registered person; such person will pay 5% VAT on goods and services purchased but can claim credit for this tax called input tax. The registered person has to make regular VAT return and either pays to or to make regular VAT returns and either pay to or service from the FIRS (VAT DIRECTORATE), the difference of the input tax and output tax. VAT returns (and payments are normally made monthly to the local VAT office on or before 14th day of the month next following that in which the supply was made also, to claim a credit for input tax, a registered person must hold a "tax invoice" Records have to be kept.

The FIRS (VAT DIRECTORATE) provides a free information and advising service to help you with VAT. Every vatable person is required to keep proper records and books of all transactions, inputs and activities sufficient enough to calculate the correct amount of VAT payable. These include Cash Book, Sale and Purchases Day Books, Ledger Accounts, Balance Sheet among others. Specifically for VAT purposes, Tax Invoice are to be issued for all supplies and VAT accounts are also to be kept. Whenever, a person supplies vatable goods and services to another person, he must issue a tax invoice in support of the transaction and retain a copy for himself. The customer also needs the tax invoice to support his claim or input tax. All exported goods are zero-rated that is such goods are ratable but at zero point, this means that no VAT is collected from the foreign buyer and at the same time any input tax is refundable. Feature of VAT administration are as follows:-

COLLECTION BY AGENTS:

All those who deal on ratable goods and services are to be registered as collecting agents for the government. Also in order to widen the VAT base, the government required all Government Parastatals, Ministries and Agencies to register as VAT Agents. All Contractors must show evidence of VAT registration certificate and number. They are to deduct VAT at the local VAT offices nearest to it. The payment slip by the Agents must be attached with a schedule showing the name of the Contractor, Invoice number, goods, amount on invoice, amount of VAT, monthly returns and a cheque for the payment.

The non-resident Company shall include VAT in it invoice and shall pay the VAT in the currency for which its goods and services are paid. VAT returns should be made in the same way the resident company does refund claims.

VAT system enables a registered person to make claims for refund if his input tax exceeds the output tax. Refund is also available for VAT paid on zero rated goods and services.

Refunds claims can be by credit method or by direct cash method, under credit method, VAT form 002 is used to calculate the total output tax and input tax as well as deduction to be made. But where output equals to input in means not tax is payable or refundable. Direct method is done where there is perpetual tax balance difference on form to the tax payer that is output always exceeds input. Cash has to be used.

The VAT Auditors usually verify the following documents before refund claims can be made. These are form 002 returned monthly, input tax invoices, sales invoices, notice of import and original proof of tax payment on inputs also export documents, notice of export and proof of realization of export and other relevant documents to back up refund claims.

INSPECTION:

The VAT Inspectors are authorized to visit the premises of very ratable person with the following objective in mind. They are to ensure compliance with the VAT laws and regulation fully.

They are to examine the method of recording transactions and offer suggestions where necessary. They are to allow tax payer to ask for clarity and educate the tax payer in new development in the system.

The Zonal Co-ordinators will periodically carry out VAT tax drive in order to stimulate the collection of VAT from defaulters and inforce from remittance of VAT payable. The Vat Headquarters will on regular basis carry out VAT audit and investigations as to check both the VAT officers and VAT payer's records to

ensure strict compliance with the laws and accountability of the VAT collected offences and penalties.

FBIR officers are trained to carry out their duties in a reasonable manner and are thus more likely to request information politely than to wield the big stick. They do, however have three reserve powers which can be used to encourage co-operation or penalize the lack of it.

Firstly, the FBIR are, to a best of judgement assess where a person has failed to render returns or renders an incomplete or inaccurate returns or verify such returns. Secondly, a person is liable to civil penalties if he fails to comply with a demand for documents or information.

Thirdly, the Commissioners can impersonate under a number of provisions. Tax due from any persons is recoverable as a debt due to the state. The VAT legislation and general law provide the FBIR with a comprehensive commonly with which to recover tax due to them. If a person who deals on ratable goods and services failed to register with the local VAT office, he shall be guilty of an offence and there are various offenses with very stiff penalties under the VAT system.

Some of the offenses are:

i) Failure to register
ii) Failure to furnish required information
iii) Making false claims
iv) Obstructing VAT Inspectors, and
v) Failure to submit returns.

These offenses carry penalties ranging from fines of up to N10,000 to various terms of imprisonment. In some cases the fines or penalties depend on the

amount of evasion involved. The law is even more strict in dealing with officers of the Board. Any officer of the Board who aids or abets the commission of any of the offenses under the VAT law will be liable for a fine of N50,000 and/or imprisonment for five years.

SHARING OF BENEFITS:

Section 36 of the VAT Decree specifies that VAT proceeds shall be shared on the basis of 80% to the State Government and Federal Capital Territory (Abuja) and 20% to the Federal Government at the beginning of the implementation, the Federal Government projected the revenue target of VAT for the year 1994 to the tune of six billion Naira (N6,000,000,000), but at the end of the year, the VAT revenue collected was to the tune of N8.6 billion which was distributed to the State and Federal Capital Territory on the basis of population 50%, 20% equity 30%. The urge to generate more income through an efficient and effective VAT system made the Federal Government to amend Section 36 of VAT Decree to read as follows: 25% Local Government, 25% State Governments and Federal Capital Territory and 50% Federal Government. Thus, there is 150% increase of VAT revenue shared to Federal Government in order to adequately fund and maintain the agencies connected with the collection of VAT revenue. The Federal Government expected to realize N12.3 billion i.e. an excess of N4.3 billion. This is a sign of a ray of hope that all things being equal shall soon be out of the word. In 1998, the revenue was shared in the basis of 35% for the Federal Government, 40% to the states and 25% for local governments including Federal Capital Territory, Abuja.

3.7 SUMMARY OF THE CHAPTER

Reference:

1. Nigeria Taxation Principles and Practice by Edward D. Agyeman
Triumph Publishing Company Nigeria Limited .

2. Companies Income Tax and Petroleum Tax in Nigeria - A. A. Ani 1989.

3. Personal Income Tax in Nigeria by O. T. Odion - 1994.
Department of Accounting, A. B. U., Zaria.

CHAPTER FOUR

RESEARCH METHODOLOGY

4.1 INTRODUCTION

The basic methodology used IN THIS STUDY is sample survey research method. The documentary analysis was first used when the development of a questionnaire as a supplement to the use of a guide interview method. The interview was centered on the VAT as a tax system. While the questionnaire was to take on general overview of the hypothesis, that implication and implementations of Value Added Tax in Nigeria.

4.2 SOURCES OF DATA

In carrying out this study, the research would make use of both primary and secondary sources of data, the primary source of data consists of information gathered from the administered questionnaires and through the structured interview the researcher had with the local vat officers, the collecting agents and the Executive Director of VAT.

The secondary source of data collection in this study research consist of textbooks, encyclopedia, dictionaries, magazines, periodicals (such as journals and seminar papers as well as circulars) made public from VAT headquarters.

4.3 THE STUDY AREA

The main population is the Nigerian economy. Other relevant sectors of the economy that received special tribute were the Federal Board of Inland Revenue

and the Federal Inland Revenue Service. It must however, be noted here that there is no special or accurate records of the other sectors of the economy as far as this new tax system is concerned. Nevertheless, the administering of the questionnaire tend to favour the North-West Zone of the VAT classification, this includes Dutse Local VAT Office, Kaduna Local VAT Office, Hadejia Local VAT Office, Minna Local VAT Office, Sokoto Local VAT Office, Zaria Local VAT Office, Lokoja Local VAT Office, Suleija Local VAT Office and Birnin Kebbi Local VAT Office and some few South-West Zonal Office, Lagos VAT Office, Ibadan VAT Office.

4.4 METHODS OF DATA COLLECTION:

Information used in this project was gathered through the use of documentary analysis, the use of questionnaires which was also supplemented by personal interview.

Documentary Analysis:

An extensive delving of the secondary source of data was carried out for facts and figures so as to allow for in-depth analysis of the gathered data for onward processing into meaningful and unambiguous information as either comparison or application statistics to the gathered data.

Personal Interview:

With this method, the Executive Director of VAT was interviewed, also interviewed were local VAT Officers of some of the North-West Zonal Offices, as well as the Area Tax Controller of VAT. The interview revealed some relevant information especially on the role of VAT to the Nigeria economy and other problems that are associated with VAT. In fact, the interview gave the researcher an insight on how best to go about the research work. Since in some cases, very elaborate explanations were made as much as possible.

Questionnaires:

The research is designed into two set of questionnaires one for the Local VAT Officers (LVO's) and the other for VAST collectors. The questionnaires are both structured and unstructured, so as to enable the respondents give their personal opinion where necessary, as well as to tick appropriate alternatives where provided. (see the end of text for specimen of questopmmaore).

Distribution of Questionnaires:

The administering of the questionnaires began with a brief covering letter to the respondents. It states the aim of the questionnaires, asked for sincere and valid information from them and assured them of the confidentiality of all information and data obtained. Furthermore, the questionnaires were distributed by the researcher to the local VAT officers and the collection agents. The questionnaires were also distributed to the VAT payers.

Collection of Questionnaire: the questionnaire were to be collected after information is provided by the respondents. The questionnaire were sample for data collection.

4.5 METHOD OF DATA ANALYSIS

The data collected would be analyzed manually. The methods to be used or employed to carry out the analysis are:

A. **CODING:**

The researcher adopted both pre-coding and post coding steps.

Pre-coding – In this case the researcher did not assign groups of questionnaires designed as marked group-one and group-two

respectively. The group-one questionnaires was for the local VAT officers to respond to. While the group-two questionnaires was designed for the response from VAT collectors or their equivalent. Pre-Coding – This successful application of this step was to be promised on the responses received from the respondents.

B. **EDITING:**

The responses of the respondents were to be edited to make sure errors in the data collected are identified and eliminated so as to make the data more accurate and presentable.

a) **GRAPHS**:

The researcher would try to illustrate where possible data collected in the form of graphic representation for ease of comparison and understanding.

b) TABULATION:

The data received from various sources as presented in row forms. They also organized in a tabular form, so that they can look more meaningful and easily understandable.

c) PERCENTAGES:

The researcher would base his analysis on percentage. The responses from the administered questionnaires shall be provided with its respective percentage as shall be calculated against each.

CHAPTER FIVE

DATA PRESENTATION AND ANALYSIS

5.1 INTRODUCTION

The aim of this chapter is to show the researcher how to prepare and organize the set of data collected, so that it looks properly presented in a form that would be easily understood by the reader. The first set of data are the ones collected from the documentary analysis and where possible would be presented in a graphic compendious as possible of the first and second hypotheses. Also, the second set of data collected are the responses given by respondents to the interview and also the administered questionnaire as a supplement.

However, in some cases the responses shall be tabulated, summarized and presented in form of tables and percentages assigned in order to make the data clearer.

TABLE 1:

Collecting Agents of Questionnaires Administered	No of Responses	Percentages of Response
100	86	86/100 = 86.6%

While for the local VAT officer, 50 questionnaires were administered and the 50 were responded to respectively; that is of course 100%.

From the Table 1 above the remaining 36% were administered by the Directorate Headquarters, Abuja and some VAT payer in Nigeria.

5.2 IMPLICATION OF VALUE ADDED TAX IN NIGERIA

In discussing the implication of VAT in Nigeria, focus will be placed on its implications ; the banking sector and its indication of entire economy. The approach in the short-run will increase the liquidity and activities of designated banks in addition to providing some commission on their tax turnover. It also will enable the government to use the instrument of taxation to induce a virile banking culture which should ideally, boost commercial and industrial activities which will in turn, enhance the nation's tax base. Technically, the engagement of Merchant Banks in the tax collection business is a significant reform in Nigerian Banking Sector: for it has implicitly

5.3 COLLECTION OF VAT THROUGH INTER-BANK SYSTEM

Presently VAT is remitted to FIRS through the use of primary stage device (diskette) where it is expected that the software program designed by one of the leading banks in run on weekly basis.

The information stored on the diskette from various branches which serves as collection unit are collected by the sole for onward updating. Each branch which serves as a collecting centre has a dedicated computed machine where this programs are run weekly on daily basis a required by FIRS. VAT can be regarded as partially computerized in Nigeria.

5.4 PROBLEMS OF VAT IMPLEMENTATION IN NIGERIA

The effectiveness or otherwise of any tax is a reflection of the quality of the fiscal system, which is a reflection of the domestic economy which in turn, is a mirror of the level of development of the socio-polity. In the case of the Nigeria VAT, a fiscal policy rarely creates its own problems; it merely accentuates or mirrors the weaknesses existing in the society. Owing to problems that are likely

to stall VAT implementation and engineering in developing countries, economists have had to debate that VAT is a lot more suitable for developed nations. A number of fiscal problems have been encountered in the implementation of VAT in Nigeria. Some of these problems are discussed as follows:-

5.4.1 **ADMINISTRATIVE COMPLEXITY**

Just like any operation that encounters problems in its developmental stage, the VAT operation in Nigeria is no exception. Following the tax architecture work of the committee that brought VAT into being, the thugging issue of its administrative network roared up its head. Nigeria tax policy makers were thrown in deep mire as to how it should look. From historical experience of previous government programmes, it did not take too long to discover that VAT needed at least an office in each state, a proposed one (VAT office) in each local government, with such cadres of officers as inspectors, collectors, auditors and so on, to effectively administer the tax to the grass root. These of course, would require series of training and experience. The network grows all the more complex as more offices are being set up.

5.4.2 **ACCOUNTING CULTURE**

Public compliance with VAT regulation in the country does either of two (2) things; it affects tax effort positively or negatively owing to poor business accounting and records keeping. The VAT legislation requires every taxable person to keep such records and books of all transactions, operations, imports and other tax related activities to goods and services as are sufficient to determine the correct amount of tax due. Yet, some difficulties have been encountered in the informal sector as well as in the assumed faintly "organized" sector.

Furthermore, unlike the situation in the developed countries, tax and accounting consultancy services are rarely engaged by Nigerian middle-level organizations except for the purposes of financial auditing or occasionally, tax planning. This makes it fairly difficult for potential VAT payers to discharge their VAT obligations and also hampers effective consumption of tax liability, making tax evasion a more preferable option.

5.4.3 **SMALL ENTERPRISES**

In as much as the Nigerian VAT law does not exempt goods and services of small businesses, tax effort is, at the initial stage, concentrated in the first five (5) years on the organized sectors. Obviously, it is difficult and may be too costly to pursue the taxation of the informed sector where illiteracy is prevalent among the operators and record keeping is low. This problem does not stand alone, as many so-called informed enterprises even deal in multimillion-Naira goods and services hence questioning and undermining the practicality of tax engineering.

5.4.4 **PUBLIC RESISTANCE**

As with any new government policy, VAT administration in Nigeria had to face the hurdle of public resistance. Two (2) factors (underlying) brought about this one, lack of confidence in the capacity of government to judiciously allocate fiscal resources and secondly, the lingering economic stagnation marked by rising inflation, growing unemployment and under-utilization of industrial capacity. Resistance of VAT by public could be measured by the compliance level, the barrage of exemption application and outright attempts at running down the tax. Not even those who acknowledged the need to a reform in the nation's tax revenue collection were in much of a hurry to comply with VAT, at least in the penetration years. By the time VAT operations began in 1994, a monthly collection and auditing of media news reports and published opinion showed an 89% criticism of VAT.

This problem has, however, been effectively arrested by allowing Journalists free access to data that would have been "classified", by a systematic tax payer education programme; and above all, by the financial productivity of tax effort. Generally, however, public acceptance is not effectively reflected in public compliance with VAT law.

5.4.5 VAT AND MULTIPLE TAXES

Behind the VAT façade is the philosophy that the new tax will phase out or replace the myriads of taxes and levies imposed by various governments of the Federation. To achieve this, VAT revenue is partaken of by the three (3) tiers of government at a stipulated formular. In defiance of this, however, there has been a resurgence of various taxes and increased rates imposed by the states and local governments; the existence of which has continually been a major threat to the to the effectiveness of the VAT regime and a source of worry to both tax payers and the Federal Government.

5.4.6 EXTRA-STATUTORY EXEMPTIONS

Vat effectiveness suffered an initial drag at the hands of opportunistic exemption seekers in both private and public sectors. In the case of certain government agencies that had placed orders for foreign goods prior to the commencement of VAT, attempts were made to ensure such imports were untaxed. Now exemptions, be they official or unofficial, constitute a serious drain to the tax base, most especially at the ports, in developing countries.

5.4.7 VAT COLLECTION MACHINERY

The VAT collection machinery experienced a number of problems or difficulties during its crawling age. Such problems include lack of adequate means of

mobility, insufficient funding to meet the day to day requirements for the local VAT offices, and lack of effective support from the stated and local government revenue agencies. There was also the problem of inadequate coverage due to the absence of a VAT office in every local government headquarters. In any case, government has been addressing these and many more problems with a view to removing them. States and Local Governments internal revenue collecting agencies are now involved in VAT collection.

5.5 CONTRIBUTION OF VAT TO REVENUE GENERATION

There are many reasons for government imposing tax on its citizens, but among these numerous reasons, the three (3) most prominent are:-

a. To raise revenue to support public expenditure, such as the provision of basic infrastructure, like education, roads, health services and defense among others.

b. To redirect the consumption pattern of individuals in society especially where the is a deliberate policy to promote the rapid development of local infant industries from being pushed out by multinational corporations.

c. To redistribute income, that is by reducing the income gaps between the rich and the poor in the society.

The above stated facts are among the contending factors upon which VAT gained acceptance in the mind of implementing regime in Nigeria. The introduction of VAT in Nigeria is to among other things as stated in (a) above, stimulate the diversification of revenue base in Nigeria. In a relative submission, the VAT system has significantly contributed in the 1994, 1995, 1996 and 1997 financial years and was expected to contribute most in 1998 and beyond. It is very remarkable to note that the revenue generated through VAT in Nigeria in

1994 stood at N8 billion, in 1995, it was N19 billion. These were far ahead of the estimated targets of N6 billion and N12 billion respectively.

The interesting thing about this development is that the percentage of revenue generated from VAT sources is on the increase. It may also be of interest to note that the percentage of the estimated revenue from VAT over the revenue from both oil and total revenue of the country had increased between 1994 and 1997.

5.5.1 EFFECT OF VAT ON IMPORTS AND NON-IMPORTS

Generally, the Nigerian VAT is based on two (2) levels: Imports and Non-imports. In January 1994, the first month of administering the tax, the import base of the tax yielded N109,314,656.00 while the non-import based realized a total of N12,453,437.00. As a result of massive enlightenment and mobilization efforts, the revenue aggregated by over 400% to N568,927,924 in February, 1994. By the end of the first quarter, the tax yield had surpassed a billion Naira mark by realizing N1,414,476,500.00 instead of the targeted N1.5 billion for the period.

The VAT yield sank by N253,144,823.00 from N800,035,000.00 in August. The low performance of the tax was attributed to political crisis which paralyzed the economy from June to late August, 1994. The factor brought about work stoppages, riots, closure of businesses and non-availability of foreign exchange to importers.

In 1994, VAT realized as much as N1 billion on the monthly basis in September and December. Tax collection figures sources from VAT Directorate, Abuja, revealed that the total yield of tax in the first year of operation was N8,195,154.00. In sum, VAT did not only meet its 1994 budget objective of N6 billion, it overshot by over 30% or N2 billion total yield.

This justified why the Late Head Of State, General Sani Abacha, in his 1995 budget statement said "VAT has proved remarkable success"

Before the original take-off of VAT in Nigeria, there was the contention that this new tax should start with a percentage charge of 15, but the government of the day refused this proposition that it was too high, the proposers of this 15% argued that, if any charge was placed less than 15%, less will generated as the below estimated collection was submitted for the 1994 - 2000.

TABLE 1: ESTIMATED VAT REVENUE FOR 1994 – 2000

YEAR	TOTAL REVENUE N	STATES SHARE (80%)	FED GOVT SHARE (20%)
1994	6,000,000,000	4,800,000,000	1,200,000,000
1995	9,000,000,000	7,200,000,000	1,800,000,000
1996	15,000,000,000	12,000,000,000	3,000,000,000
1997	20,000,000,000	16,000,000,000	4,000,000,000
1998	25,000,000,000	20,000,000,000	5,000,000,000
1999	35,000,000,000	28,000,000,000	7,000,000,000

SOURCE: REVENUE GENERATION IN NIGERIA

Being a text presented to the Committee on Economy, population and Revenue Generation of the Constitutional Conference in August, 1994, by the Chairman, Federal Inland Revenue Service (FIRS).

Beyond all expectation, VAT in its initial year of introduction (1994), culled N8,195,154,145. This figure welled over 400% of the total sales tax collection by the 30 states and the Federal Government at the Federal Capital Territory, Abuja between 1986 and 1992 when it was abolished.

This figure also constituted about 136% of the estimate of N6 billion given by FIRS to the government. Re4lative to other sources of government tax revenue, VAT did exceedingly well in 1994 considering that it was it's year of debut.

VAT revenue of N8,195,154,145 was 12.4% of the total Federal Government tax revenue of N66 billion in 1994. Petroleum Profit Tax (PPT) took the lion share of 68%, while Companies Income Tax (CIT) and other taxes garnered 19.6%.

TABLE 11: PLACE OF VAT IN TOTAL TAX REVENUE FOR 1994

TYPE OF TAX	AMOUNT COLLECTED (N)	% TOTAL
P. P. T.	44,355,302,217	68%
C.I.T. & OTHERS	13,936,153,283	19.6%
V.A.T.	8,195,154,145	12.4%
TOTAL	66,486,610,147	100%

SOURCE: OFFICE OF THE CHAIRMAN, F.I.R.S., ABUJA

In 1995, beyond all expectations, VAT total revenue generated rose to N20,320,580,661, this 27.66% of the Federal Government total revenue for the year, by all standards, it was a very commendable performance. The collection in 1995 was a great improvement on the relative performance of VAT in 1994 which was only 12.4% of total Federal Government tax revenue for that year, this represented a 250.3% of the 1994 VAT collection of N8,195,154,145.

VAT distribution made to the three (3) tiers of government in 1995 were as follows:

Federal Government - N8,014,540,379

State Governments - N6,544,391,521

Local Governments - N5,080,145,165

Federal Capital Territory - N65,443,913m

TABLE 111: PLACE OF VAT IN TOTAL GOVERNMENT TAX REVENUE IN 1995

T A X E S	COLLECTION (N)	% T O T A L
P. P. T.	34,814,214,275	46.71
C.I.T. & OTHERS	19,403,587,844	26.06
V.A.T.	20,320,580,661	27.26

T O T A L	74,583,382,780	100%

SOURCE: PLANNING, RESEARCH AND STATISTICS BRANCH, EBUTE METTA, LAGOS.

In 1996, VAT went further than expected by pooling N31 billion with a total breakdown as follows:-

Federal Government	-	N10,850,000,000
State Government	-	N11,240,420,000
Local Government	-	N 7,750,000,000
Federal Capital Territory	-	N115,958,000m

With Federal Government, State Governments and Local Governments having 35%, 40% and 25% respectively.

TABLE IV: THE PLACE OF VAT IN TOTAL TAX REVENUE FOR 1996

T A X E S	**COLLECTION (N)**	**% T O T A L**
P. P. T.	92 billion	60.5
C.I.T. & OTHERS	26 billion	17.1
V.A.T.	34 billion	22.4
T O T A L	152 billion	100%

SOURCE: NEWSWATCH MAGAZINE, FEBRUARY 23, 1998.

Petroleum Profit Tax (PPT) took the lion's share but at a reduced percentage of the previous years, due to increase in the revenue derived from other sources which over the years will rival PPT with 60.5%.

VAT took its normal position with 22.4% and an increase of 52.30% over the last year (1996). Based on the earlier presentation, the researcher submitted two (2) hypothesis which will be looked at this juncture.

TEST OF HYPOTHESIS ONE:

That VAT has a tendency for price increase especially on vatable goods and services, according to our face to face interviewee, Mr. Linus Agboyi – Administrative Officer, Kaduna Local VAT Office, Alkali Road, Kaduna. He said that VAT goods and services have a charge of 5% attached to the price, which brings about a once and for all increase. It does not necessarily lead to inflation as such. Miss Hauwa Gidado, an Assessment Officer and Rhoda Wada presented a similar opinion.

In a paper, Nigerian Income Policy, Mrs. Ajao traced inflation to VAT starting from 1990 – 1994 as presented below:

TABLE VI: INFLATION RATES AND THEIR ANNUAL INCREMENTS IN NIGERIA BETWEEN 1990 AND 1994

Y E A R	INFLATION RATE	INCREMENT	% INCREASE
1990	7.4	-	-
1991	13.0	5.6	75.68
1992	44.6	31.6	243.07
1993	57.2	12.6	28.25
1994	70.0	12.8	22.37

SOURCE: MRS. AJAO, MINISTRY OF FINANCE, ABUJA.

At 22.37%, it can clearly be seen that the percentage of increase in the inflation rate was even lower in 1994 when VAT was introduced than any other of the years since 1990. The only abnormal increase during the period was in 1992 and this was as a result of a sudden sharp fall in the value of the Naira in that year.

While accepting the fact that it may cause a once and for all general increase in the price level, it does not normally lead to inflation as it is generally feared. Besides, it nearly all countries that have introduced VAT, it has been made to replace an existing tax. This fact is in itself sufficient to make VAT non-inflationary. For example, VAT of 5% in Nigeria was introduced when the rate of Company Income Tax had come down from 45% to 35% and the marginal rate

of personal income was reduced from 65% to 30%. It was also a replacement of sales tax which had a dual rate of 5% and 10%.
This is not to say that VAT does not lead to a price increase of vatable goods and services, but not at an inflationary rate as conceived by many. Government, in its 1998 budget, proved this point that VAT does not have a relationship with inflationary situations, when it gave the percentage inflation rate which has been on the decline since 1995.

In 1995 there was a slight increase from 70.0% in 1994 to 72.8% in 1995, an increase of about 2.8%. In 1996, the percentage fell to 29% and 8.5% in 1997. It could be observed within these years of fall in the inflation rate, that they are the years VAT revenue has been on the increase.

Inflation, both current and VAT driven, cannot be claimed to have worked solely to the advantage of the rax. Two (2) broad reasons may be given for this:

First, inflation as Gustar D. Jud puts it, subjects tax payer to continually rising tax burden.

Secondly, inflation defeats the short run objective of VAT where delinquency lag is prevalent.

Unfortunately, across the world VAT is commonly associated with inflation of which Nigeria is an exception. Inflation reduces VAT revenue especially since revenue is expected to reflect the aggregate demand, the introduction of VAT to an inflationary economy can help government to recover some of the revenue it may have lost through evasion. For by reflecting consumer price index VAT does not suffer much from fiscal drag and by being speedily accounted for and remitted VAT tends to neutralize the effect of inflation on tax revenue.

Hence the proposition by Robin Burgs and Nicholas Stein – that VAT as an ad-valorem tax has provided inflation protection for government in a specific way that specific exercise which it replaced did not.

TEST OF HYPOTHESIS TWO:

The Vat is the best alternative to sales tax in revenue generation due to its scope and willful compliance.

In testing this hypothesis, the researcher intends to use a graphical illustration to make a position about this issue i.e. the revenue derived from VAT since its inception to date. See figure 1 (1994 – 97).

In the words of Afe Ogundele in his book, Value Added Tax Theory and Practice, VAT culled N8,195,154,145.00 in 12 months of implementation in Nigeria. This figure is well over 400% of the total sales tax collection by all states and the Federal Capital Territory. The graph attached on figure 1 elucidates the above contention.

In a capsule, VAT does not lead to a general increase in ordinary price level nor does its sales match VAT in terms of revenue mobilization.

The conclusion without ambiguity therefore is that VAT is a good tool (policy measure) for revenue sourcing (generation) in Nigeria.

5.6 PROPECTS OF VAT IN NIGERIA

In spite of criticisms and the inflationary and unemployment trend, amidst other economic problems, that accompanied the introduction and actual implementation of VAT, the tax has become one of the major sources of revenue to the government. Regardless of the financial ups and down in the economy,

which VAT administration and revenue will reflect from time to time, VAT will continue to play an endless role in business conduct, consumer behaviour and of course, in the mobilization, allocation and redistribution of economic resources, especially for as long as the fiscal system exists. Already visible on the fiscal horizon are certain future VAT developments such as ulterlimination of competing nuisance taxes, higher compliance, lower direct tax rates (like the personal income tax) to a barest minimum and a canopy coverage of the tax. VAT prospects are broadly numbered and discussed below:

5.6.1 PUBLIC COMPLIANCE

In view of the large number of taxable activities in the economy, public compliance with VAT may be seen as being rather low. In any case, the tax has secured a greater public compliance in its first two (2) years of operation than any other fiscal programme ever in Nigeria. For as long as government continues in its bid of effective mobilization and enlightenment of the tax paying public, VAT popularity and compliance with it will likely be enhanced up to a point of spontaneous response to registration, with compliance following an attainment of an optional level.

5.6.2 BROADER VAT BASE

The base of VAT in 1995, was widened to include:

i. All states and Federal Government Ministries, Parastatals and Agencies;

ii. All their contractors are required to show evidence of VAT regulations;

iii. All government departments are now under obligation to deduct Vat from payment due to contractors;

iv. All extra-statutory exemptions granted in 1994 expired the same year. This means that apart from one specifically provided in the Decree, no other non-statutory exemptions is acceptable in 1995; and

v. All non0resident companies transacting business in Nigeria now obliged ti register for VAT using the address of the current employer with whom it has subsisting contract.

The 1996 fiscal year also made provision for a wider VAT base. The above provisions, if properly handled and implemented, have the tendency of doubling revenue from VAT.

5.6.3 MORE VAT OFFICES

There is an increased likelihood of government setting up VAT offices in each local council of the federation in the near future, if government is to effectively spread the VAT gospel round the public and consolidate or rationalize the scope of monitoring the tax. This must however be done systematically, gradually, such that it would b reflective of developments in the national tax administration structure.

Revenue yield must, in addition, definitely justify the spread. Greater involvement of lower tiers of government would be called for as well, after a due and cautious assessment of the fiscal system.

So far, more offices are opened each year as indicated in the yearly budgets. Government intends to open an additional thirty new VAT offices to cover the capitals of the newly created states and headquarters of more local government areas.

5.6.4 NATIONWIDE VAT CENSUS

Presently, not all vatable institutions are registered with the VAT Directorate yet, much revenue is yielded. This shows that its performance has been very impressive as a worthy fiscal innovation. To this effect, government has deemed it reasonable that in order to further enhance the prospect of the tax in years ahead, it (government) shall embark on a nationwide VAT enumeration of all vatable institutions. This, government has said, will create a veritable data base for effective planning, assessment and collection of tax. It is hoped that on completion of this exercise, the future revenue generation of this exercise, the future revenue generation of the tax would be completely overhauled and enhanced.

5.6.4 REVENUE GROWTH

The unmistakable growth of revenue derived from VAT has drawn much attention to it. In its first year of operation, the tax performed above its estimated 6% contribution to the Gross National Product (GNP), recording an average of N175 million proceeds monthly. The second year was no different. VAT achieved about 175% of its budget estimate or N9 billion excess revenue. 1996 was also no exception. Of the N22 billion estimated, about N29 billion was realized. This growth trend will continue and even accelerate if Nigeria's economy stabilizes in the near future.

According to the then Chairman of FIRS, Mr. J. K. Naiyeju, if the 1994/1995 growth rate of about 163% is sustained, VAT may yield an estimated 50% of totally federally – collected taxes in a decade and contribute substantially to shooting up Nigeria's tax ratio. By the year 2000 (this year) he says VAT would have effectively rivalled, if not overtaken, revenue derived from petroleum profit tax and other taxes including customs duties and income taxes. The tax by outshining such taxes as the capital gains tax, companies income tax, stamp

duties and personal income tax, has already enacted a fiscal coup in the tax system.

Year-in-year-out, the VAT contributes huge sums to the Federal Government's purse hence, the nation's GDP with a little more of compliance with the tax, public acceptance and tight control, VAT in Nigeria would surprise the world at large.

CHAPTER SIX

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

6.1 SUMMARY

This work has discussed to a reasonable extent, implications and implementations of Value Added Tax (VAT) in Nigeria. VAT is an ad-valorem tax and a member of the sale tax family, specifically, it is a consumption tax that is chargeable on the value which the producer or supplier of goods or raw material used in the production of the goods as the case may be. Simply, it is a tax on consumption of goods and services that are VATABLE.

Taxation, being the fulcrum of this study is generally overviewed. Reasons for taxation, its effects, types and taxable capacity, together with other things have been brought to light. The essence is to give the reader a deeper understanding of Government's unwavering stand to taxing its citizens.

It has also been necessary to talk on the concept of VAT, its importance, the way in which it is collected, how receipts are disbursed and the various uses to which they are put that is how the VAT proceeds are applied. Focus, here is such that any sour grapes setting people's teeth on edge would be done away with. From the little I have been able to expound, it is hope that Government would be given some credit and breathing space as per VAT.

Of an even greater importance is the need to consider the Nigerian economy as a whole. This has been done because Government, in fact no individual would take an action without a drive.

Chapter Three (3) gives the reader a "faint" idea of the nation's economy, pre and post VAT. The real issue(s) that brought VAT into being is (are) evident here. As a husband and wife would first discuss and then agree on making a baby, so also did Government with the committee that birthed VAT, having weighted its pros and cons, the latter outweighing the former.

The main course of the menu is not in least left out – VAT widespread achievements, impact on the economy, problems and prospects have been carefully outlined and touched on. VAT is a federally administered tax and this has been discussed aggregately. Of course, it may not be as detailed as it ought to be; attempt has, in any case, been made to ensure it is a good representative of all units of the economy taken together.

VAT has among others the following features:

It is directed at consumption, so it is a tax on spending which is borne by the fiscal consumer of goods and services, because it is included in the price paid. It

is based on a flat rate of 5%. It is collected on behalf of the government by business and organizations registered with the Federal Inland Revenue Service (FIRS) for that purpose. It covers both locally manufactured and imported goods and has a zero rate for export. Some goods and services ranging from that of medical and pharmaceutical, food, education, commercial vehicles, and their spare parts, newspaper and magazines, Community Bank services, People's Bank services and so on were exempted.

Consequent upon the profitable outing of 5% consumption on tax, the VAT, in 1994, the scheme has been declared the most successful in Nigeria's fiscal history.

For instance, the uncertainties on Nigeria's political horizon were seen as probable odds against VAT in 1994 so were the prevailing rate of inflation which had radically delimited the consumption behaviour of many Nigerians. It was the singular effective policy in the 1994 budget. It did not take long for the gains of VAT to become visible. Three months after it took off, N2.8 billion was collected. At the end of 1994, the first year of introduction and operation, the target of N6 billion exceeded as N8.6 billion was hauled into the revenue through VAT.

The strength of VAT lies in huge revenue generation as N31 billion revenue generated through it in 1996 exceeded the N22 billion target. It could be seen that more taxable Nigerians have join the effective tax-base, collect and remit VAT more honestly.

This is a clear evidence that VAT like petroleum has become a money spinner and the struggle for its paternity is best seen in the fact that in the sixteen months of its existence, it has had three (3) sharing formula.

Another merit of this tax system is that it is difficult if not impossible to be evaded; especially by the final consumers who bear the collection is made through registered business organization.

The sales tax which VAT replaced has never recorded such a huge success. This success could also be attributed to the perfection of certain areas of VAT operations. Experts have in particular tended to point at the VAT monitoring strategy including desk and field audits which is believed to be subject to continued reappraisal by the FIRS boss.

With the successful introduction of VAT, government is now shifting its emphasis from income tax to the tax on consumption. VAT makes a substantial contribution to government revenue. It is evident that it has come to stay.

Finally, the main course of the menu is not in the least left out – VAT widespread achievements, impact on the economy, problems and prospects have been carefully outlined and touched on. Since it is a federally administered tax, these

were discussed aggregately. Of course, it may not be as detailed as it ought; attempt has, in any case, been made to ensure it is a good representative of all units of the economy taken together.

6.2 CONCLUSION

There are criticisms on VAT. It is said to fuel inflation, at least in the short term, if prices of goods and services rise immediately by the amount of the tax. It is also argued that how income earners spend a greater portion of their income and save less, therefore, have a heavier relative tax burden than higher income earners. Lack of differential VAT rates for luxuries and necessities like Kenya, Belgium etc., further makes the situation worst for the low income earners.

The negative fall-outs of VAT is not only restricted to its administration on goods but also on services. By the scheme, most transactions like insurance, charging VAT on insurance premium amounts to double taxation on the insured, since the insured may have paid VAT on their property at the initial point of purchase and will further pay VAT on premium indirectly through the insurer since service charges will be added to premium payable by the insured.

Even though there are criticisms, VAT have started achieving its goals. It has reactivated the whole tax system of the country and its impact is felt in the whole non-oil revenue generating sector. Despite the huge success recorded by VAT, it is characterized by a lot of loopholes in its implementation.

The FIRS was honest enough to admit that its success had been attended by a number of problems and difficulties.

These problems could be viewed as follows:-

Initial problems
Administrative problems
Non-compliance
Tax evasion.

So many businesses, particularly those that come under the umbrella of the Manufacturer's Association of Nigeria (MAN), the Nigerian Institute of Estate Surveyors and Valuers (NIESV) are also crying foul. They allege double taxation on their goods and services which rub off negatively on the consumers.

According to another group of critics, VAT was successful on other developed countries because those countries have clock work accounting system, a traceable bureaucratic process complimented by co-operative populace already used to a sustained high taxation culture, but in Nigerian economy all these are not obtainable.

Where more consumers joining the high income class, VAT would have a wider base to fatten its revenue but a situation where more people are joining the poverty or low income brackets on daily basis is death blow to any consumption tax.

Reactions were quite obvious since the VAT was introduced. In some quarters, there is fear that the system might not work out well. Others believe it is like an experiment which is subject to changes. In the long run, most, if not all these faults may be corrected.

VAT as a complimentary revenue source has come at a time when it is most needed. At a time where the oil sector is going through a turmoil of sabotage and shortages coupled with administrative and technical problems, we cannot but be thankful for the strength of VAT, especially where the major source of foreign exchange takes a downturn to import fuel.

6.3 RECOMMENDATIONS

One of the essential ingredients in successful tax administration is the ability to sell the product (i.e. tax) to the payers. The public need to realize why the tax is levied on them. The recommendations based on the findings of the study are as follows:-

a. **Effective Communications:** Effective communication should be the hallmark of tax office, this will not only erase distrust and hatred for the tax office but would also improve the relationship and attract tax payers.

b. **Public Enlightenment Campaign:** Public enlightenment campaign should be directed to explain the need to pay tax. The tax laws should be explained and the net effects for not obeying the Tax Laws. Information centres may be set up in appropriate places, such centres would assist in explaining to tax payers doubtful points of law and any portion of the return from that may not be cleared. Workshops and seminars should also be organized to educate Nigerians.

c. **Improving Administrative Machinery:** The mantle of administration should remain with FIRS; no separate administrative commission need be set up because the originator of a system knows best how to handle, maintain and when to change gears on it. However, private tax consultants could be engaged from time to time, when deemed necessary, to monitor compliance on behalf of FIRS.
The administrative machinery needs to be improved upon to enhance more compliance and more yields from the revenue. Like in other developed countries, Nigeria should emulate the, qualified and well trained tax administrators should be placed in the post where they could

be very useful. There should be frequent seminars and workshops organized for tax administrators.

d. **Audit And Inspection:** This is concerned with detecting non-compliance among tax payers whose income is derived from self employment sources.
This is usually done at the tax payers place of business and it involves the examination of books and records of tax payer. More transports should be made available to make the administrators to pay visits to such tax payers. And those found guilty irrespective of their status should be prosecuted and brought to book. The result and stages of their default should be summarized and published in local dailies.
Cordial relationship should be maintained with tax payers. The use of intemperate language should be avoided by VAT authorities so as to instill the FIRS in them. The use of non-euphemistic language should be encouraged by tax officials.
The kind of relationship that subsists between the tax authorities and tax payers is very material in realizing the desired goals of VAT administration. Also, much has to be done to improve the physical structure of tax offices for the comfort of both tax payers and tax officers.

e. **Staff Welfare:** VAT has its oppositions, problems and yet it accounts more than what is estimated for. Does this mean that the VAT administrators are not efficient? No! The VAT administrators have performed very well to enable VAT to produce such yields. Therefore, these staff deserve to be commended delicately. This can be achieved through staff development programs, training, welfare and adequate remuneration. When this is done, those tax administrators who are in the habit of collusive agreement with tax dodgers will stop.

f. **Differential Rates:** Differential "VAT rates" need to be introduced for luxury goods and necessity. This approach could favour progressive tax system necessary to lessen the wide gap between the poor and the rich.

g. **Provision of Adequate Services:** It is very important to let the tax payers see visible and tangible evidence of the end product of the people's money. Services such as food, water, housing, drug and medical facilities ought to be provided adequately or people will loose hope and returns from VAT might fall.

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