"INCREASING NIGERIA'S TAX-TO-GDP RATIO: THE CHALLENGES AND WAY FORWARD"

GODFREY OKOYE UNIVERSITY ENUGU

4th INAUGURAL
Lecture

"INCREASING NIGERIA'S TAX-TO-GDP RATIO: THE CHALLENGES AND WAY FORWARD"

DELIVERED BY

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4th Inaugural Lecture

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Vice Chancellor,
Distinguished Colleagues,
Ladies and Gentlemen

INTRODUCTION

The Vice Chancellor Sir, the choice of the topic for this inaugural lecture was necessitated by the memo from President Muhammadu Buhari to Babatunde Fowler, Executive Chairman of the Federal Inland Revenue Service, on August 18, 2019, asking him to explain the shortfall in tax collected by the agency.

Fowler was asked to justify the obvious differences between the budgeted tax collections and actual collections for the period 2015 to 2018. The letter to Fowler signed by Chief of Staff to the President, Abba Kyari, reads: "Your attached letter (FIRS/EC/CWP/0249/19/027 dated 26 July 2019) on the above subject matter, refers. We perceived significant variances between the budgeted collections and actual collections for the period 2015 to 2018".

"Accordingly, you are kindly invited to present an all-inclusive variance analysis explaining the reasons for the variances between budgeted and actual collections for each main tax item for each of the years 2015 to 2018. In addition, we perceived that the actual collections for the period 2015 to 2017 were drastically worse than what was collected between 2012 and 2014.

"Accordingly, you are kindly to give details for the poor collections. You are invited to respond by 19 August 2019. Please

accept the assurances of my highest regards".

The Chairman of the Federal Inland Revenue Service (FIRS), Mr. Tunde Fowler, has since responded to the query,agreeing that actual tax collection since the inception of President Muhammadu Buhari administration was lower than the 2012 to 2014 period under former President Goodluck Jonathan in general terms. Fowler noted that the FIRS under his watch had performed better concerning particular non-oil tax types such as value added tax (VAT) and corporate income tax (CIT). He associated the overall lower collection since 2015 to the oil market crisis which has seen a fall in commodity prices compared to the period under Jonathan, and recession which slowed down economic activities (Fowler, 2019). Without going into what some people have alleged the political undertones in the query issued to the Executive Chairman of Federal Inland Revenue Services (FIRS), it is fair to say that the President is highly frustrated and rightly so, with the current situation where tax revenue in Nigeria accounts for a paltry 5% of the country's GDP against the West African Regional average of 15%., Asian average of 22% and OECD average of 27% (IMF, 2018).

The query to the Chairman of FIRS is a wake-up call to the apex tax authority that the government cannot afford to provide any meaningful development to the Nigerian people with tax-to-GDP ratio of 5% or for that matter, anything below the regional average of 15%. Perhaps, to situate this lecture in a proper context, it is considered proper to begin from the beginning.

In other words, what really is tax and why does tax matter so much to a country's economic development to the point that the President will issue an open query to the country's chief tax collector to express his frustration with the low tax collections?

This lecture, therefore deals with the nature of tax, the characteristics of a good tax, gross domestic product and taxation, tax evasion and tax avoidance, why people pay tax and the uses of tax revenue, challenges to Nigerian, tax system, conclusion and recommendation"

    A.   Nature of tax

    B.   Characteristics of a Good Tax System

    C.   Gross Domestic Product (GDP) and Taxation

    D.   Tax Evasion and Tax Avoidance

    E.   Why we pay taxes? And what can tax do?

    F.   Tax Revenue-GDP – Ratio

    G.   Challenges to Nigerian tax system

    H.   The way forward

    I.   Conclusion

A.   NATURE OF TAX

Tax has been given varied definitions by individuals, although, there exists some common basic elements in them. *Black's Law Dictionary* (1979) defines tax as a charge by the government on the income of an individual, corporation or trust, as well as, the value of an estate or gift. Similarly, the Webster Business

Dictionary posits that tax is 'a charge or burden, usually pecuniary, laid upon persons or property for public purpose' In his own contribution, Obatola,O.S (2013) defines tax as an obligatory levy imposed by government or any recognized authority of the state on the property, goods, services and people living in an area for revenue generation to offset the expenses incurred by the government or the authority on behalf of the citizens. Furthermore, a tax is an obligatory contribution forced on the citizens by the government in order to provide social services and to ensure the citizens social and economic welfare (Institute of Chartered Accountants of Nigeria [ICAN], 2009).

Tax according to the National Tax Policy for Nigeria is a monetary charge on a person's or entity's income, property or transaction and is usually collected by a defined authority at Federal, State or local level.

Similarly, Cornelius, et al (2016) and Kwaji and Ishaya (2017) simply defined tax as compulsory non penal levy imposed by government on the income, profit and gains of individuals and corporate organizations through government agencies and in compliance with the established law.

Explicit in the above definitions of tax are

1.   Tax is an imposition: this implies that tax is not voluntary but forced on individual; failure to comply attracts penalty. Tax is not optional but an obligation expected of any good citizen to discharge.

2.   Tax is imposed by government: government imposes tax on citizens and uses relevant tax authorities or certified agents to enforce collection and compliance.

3.   Tax is a charge on income of individuals: tax is levied on the income/profit of individuals comprising: persons, families, communities, corporations and trust. This implies that payment of tax reduces the amount of money at the disposal of the individual. Thus it affects consumption and savings potential of those concerned.

4.   Tax is imposed to generate revenue for government: the main objective of government imposition of tax is to raise revenue to oil the wheels of administration. The money so raised helps to off-set the cost of governance and to provide some essential basic amenities to the citizenry.

In view of the above, tax is the legal mandatory extraction of money by government or public authority from the income of individual citizens for the purpose of meeting the needs of government in providing the needs of the people.

B.   **CHARACTERISTICS OF A GOOD TAX SYSTEM**

There have been varied opinions from scholars on what should constitute characteristics of an effective tax system. However, the following should be considered as important:

1.   **Fairness or equity**: A good tax system should be fair or equitable in distribution. Thus individuals in similar financial

condition should pay similar taxes. This is referred to as **Horizontal Equity**. Horizontal equity also demands that individuals with the same income but different allowable expenses pay different amount as tax. Furthermore, persons who are financially advantaged over others should pay at least the same proportion of income in taxes as those who are not well off. This is referred to as **Vertical Equity**. On the vertical equity, taxes could be classified as Regressive, Progressive or Proportional.

A tax is regressive when those with lower incomes pay a larger share of income tax than those with higher income. This is common to tax on necessities such as food items as lower income earners spend much of their income on such items. Also, a tax is proportionate if all payers pay the same share of income in taxes. Corporate Income Tax seems close to proportionate tax as the same rate is applied to most corporate income. In addition to this, a tax is progressive when higher income individuals pay higher share of their income in taxes as typified by Federal Income Tax.

2. Adequacy of a good tax system should be such as to provide adequate revenue to meet the basic needs of the society. Public services are funded from tax, hence as the demand of the public increases, it is expected that the revenue generating activities should grow accordingly to make the tax rate stable or relatively low.

3. Transparency: This connotes that the tax payers and the leaders can easily access information about the tax system and

how the tax revenue has been spent. A transparent tax system readily provides information on who is being taxed, how much is collected and what the money is used for.

4. Simplicity: A tax system should be simple such that payers could understand thus reducing the cost of compliance. It implies that the tax, tax forms and tax filling should be simplified.

5. Administrative Ease: the tax system should not be complicated or costly for tax payer or the collector. The rules should be made known, simple; with forms simplified. The cost of collection should be small relative to the amount collected. Audit should be fairly conducted.

C. GROSS DOMESTIC PRODUCT (GDP) AND TAXATION
GDP is the market value of all final goods and services produced within a country in a given period. It measures the net output or value added as it measures goods and services bought with money. Increase in the annual output of goods and services in a country could be described as economic growth. This could be measured using Gross Domestic Product (GDP) or Gross National Product (GNP). It occurs in a nation when its GNP or GDP becomes larger than what it was. It is the rate of change of real income or real output. GDP measures the total output and sum total income of an economy at a given period respectively (Begg, Fischer & Dornbusch, 2008). GDP is an indicator of a country's economic health, showing how big the economy is and

could be used to compare the earning and spending capabilities of different countries. The increase should be steady and sustained for at least two successive quarters, hence economic growth could be described as a steady increase in the output of final goods and services. In some situations, economists take into consideration the impact of inflation in the measurement of economic growth thus the term Real GDP. It has been argued that by relating the GDP to the population a better picture of the welfare of the citizens are presented resulting in the use of the term GDP Per Capita. In view of the above relationship between economic growth measured by GDP and population, there is the need for increased growth in the economy over the population growth rate to avoid population growth over production that might precipitate starvation. The concept of actual GDP, potential GDP and GDP gap or output gap were described by Lipsey and Chrystal (2011) thus: Actual GDP is what the economy actually produces while potential GDP is what the economy would produce if all the resources, land, labour and productive capacity- were fully employed at their normal level of utilization.

This is also referred to as potential income and is sometimes called full-employment income (high-employment income).GDP gap is the difference between the actual and potential GDP.

Abdulazeez and Dandago (2018) noted that there are numerous studies which examined the correlation between tax revenue

and economic growth of Nigeria. Some of the studies (Adegbite 2015 included oil tax revenue while others (Ezeji & Peter, 2014; Izedonmi & Jonathan, 2014; Lawrence, 2015; Folajmi et al 2016, and Manukaji & Nwadialor, 2016) examined the contribution of specific non-oil taxes on economic growth of Nigeria.

Tax is an agent for economic growth as it is used in funding many potential growth activities and other economic management. Thus, there is the concept of Tax-To-GDP Ratio which is the ratio of a nation's tax revenue to its GDP. The tax-to-GDP ratio is used together with other metrics to measure how much a nation's government controls its economic resources (Investopedia). Since tax is related to economic activities, the ratio should be relatively consistent. This implies that as GDP grows year by year, so should taxation as well. However, in cases of significant shifts in tax law or during serious economic downturns, the ratio can shift sometimes dramatically. Usually, during economic downturn, unemployment rises, consumer spending decreases and fewer property and consumer taxes collected due to less consumption, tax receipts drop pushing tax-to-GDP ratio downwards.

In Nigeria, despite reports by FIRS of increase in tax collection, yet tax GDP ratio has continued to exist unacceptably at 6%. Tax-to -GDP ratio is one of the most widely used tools for measuring the efficiency of a nation's tax system; as a result one can depend on that to describe the level of tax system in Nigeria as poor. This is worrisome, as tax is closely related to economic growth. When

tax grows faster than GDP, tax-to-GDP ratio drops but when at lower rate than GDP, the reverse is the case. The ratio of tax-to-GDP remains consistent as tax is closely related to level of economic activity (Oladipo & Ogochukwu, 2019).

D. TAX EVASION AND TAX AVOIDANCE

Tax evasion is a deliberate or preconceived act or design on the part of a tax payer to decrease tax burden. It is a criminal act which in addition to fines and penalties may lead to imprisonment.

Examples of Tax Evasion

Bassey (2016) lists the following as acts which constitute tax evasion

1. Omitting or understating income liable to tax
2. Overstating expenses so as to reduce taxable income
3. Claiming reliefs and deductions for which the tax payer is not entitled
4. Failure to pay tax due or failure to remit withholding tax and PAYE deducted.
5. Failure to file returns with the relevant authority or submission of false or incorrect return

Examples of Tax Avoidance

Similarly, the following constitute acts of "tax avoidance"

1. Exploiting the loopholes existing in the tax laws

2.   Thin capitalization where the tax payer decides to use more loans than equity to operate

3.   Where there are options, the tax payer can take an option which benefits him/her

E. **WHY DO WE PAY TAX?**

Without trying to cause controversy, I must say that the issue of tax and its payment is as old as mankind. In Genesis Chapter 14 Verse 17-20, Abraham paid some tax (tithe) to Melchizedek King of Salem.

Even in Jesus's time, payment of tax was rife and Jesus approved of its payment by directing Peter to pay for their tax obligation which has fallen due at the time. This event shows that right from creation till now, tax matters so much. The fiscal social contract between citizens and elected leaders implies that citizens should pay tax which the leaders will utilize to execute programmes for their collective good. We also pay tax because it is a legal requirement. As a failure to pay will be punishable by law, thus, there is a biblical injunction, legal requirement, and fiscal social contract requirement making it obligatory for one to pay tax. However, people talk about them, complain about them, and try to dodge them when they can. Businesses also react to taxes, both in how they put together their activities and, perhaps, in where they execute them.

 How persons and businesses react in turn affects the echelon and organization of taxation. We must quickly point out that tax

refers to a compulsory levy by a public authority for which nothing is received directly in return (*absence of quid pro quo*). Tax is therefore, an obligatory contribution, forced by government, and while taxpayers may receive nothing substantial in return for their contribution, they nevertheless have the advantage of living in a relatively educated, healthy and secure society.

In other words, tax is part of the price to be paid in an organized society for the provision of social amenities, redistribution of income and wealth, promotion of social and economic welfare, economic stability and coordination and regulation (James & Nobes, 1992; Nightingale, 2001). Tax is an imposed levy by the government against the income, profits, property, wealth and consumption of individuals and corporate organizations to enable the government obtain the necessary revenue to provide public goods, security and well-being of the citizens.

The first detailed historical information about taxation can be found in Ancient Egypt (Ezzamel 2002). It was said that Pharaohs selected tax collectors (called scribes) and paid them high salaries to reduce the incentives for them to enrich themselves.

Furthermore, scribes working in the field were monitored by a group of special scribes from the Kings Palace (Webber & Wildavsky, 1986). The essence was to eliminate corruption in the collection of tax. Sadly however, corruption of the tax agency is still a problem, especially in developing countries.

OBJECTIVES OF TAXATION

In agreement to the view of Muley (n.d) and ICAN (2009), major objectives of taxation comprise the following:

1)   Revenue Generation: the major objective of taxation is to generate income for the government to finance the general administration and other projects of the government (Public Sector Expenditure). These may not be profit yielding but have indirect link with economic growth and development. The essence of taxation is therefore to raise money needed to satisfy the need of government in the provision of services like defense, law and order, health services and education. Capital projects also benefit from the revenue generated.

Such projects improve social and economic infrastructure such as road, railways, bridges, etc.

2)   Redistribution of Income and Wealth: this could be seen from the doctrine of taxation known as the 'Ability to Pay' which implies that the burden of taxation ought to be heavier on the affluent member of the society than the poor (progressive tax system). This is based on the view that the concentration of nations wealth in hands of few is seen as unjust hence the need to redistribute it. High tax on the income of the rich can have incentive or disincentive effect as tax reduces income and can spur the individual to work harder. Conversely, the impression of government tax as cheat and unnecessary may discourage hard work.

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3) Management of the Economy: Taxation is important in planning of savings and investments by harmonizing it with development strategy and changing economic structure. This may be in the following ways

a. Economic Development: Nations' economic development is largely dependent on capital formation. To overcome scarcity of fund, government of various nations tends to mobilize capital accumulation through taxation. Savings-income ratio which can be raised through taxation policy.

b. Full Employment: The level of employment depends on effective demand. Thus a nation desirous of full employment has to reduce tax rate which would increase money at the disposal of the citizens. In effect, there would be increase in disposable income (money for consumption and savings). The increase in consumption precipitates into effective demand stimulating investment while savings provides for fund for investment.

c. Control of Cyclical Fluctuations: The control of cyclical fluctuations, that is, boom and doom periods. During period of economic depression, tax rates are reduced while during the boom period, tax rates are increased so that the fluctuations are controlled.

d.   Reduction of balance of payment difficulties: In the same vein with customs duties, taxes are also used as instrument of import control on certain goods and as object of reducing balance of payment difficulties thereby encouraging domestic production of import substitutes.

e.   Price stability: One of the short-run objectives of taxation is price stability as taxes are regarded as an effective tool of controlling inflation. Increasing direct tax rate reduces private spending thus curtailing inflation while indirect tax imposed on commodities fuels inflationary tendencies.

f.   Harmonization: Suggestive of harmonization as one of the objectives of modern taxation is the philosophy of single market in Economic Community of West African States (ECOWAS) which is to provide for free movement of goods/services, capital and people between member states.

F.   **TAX REVENUE-GDP RATIO**

The Tax-to-GDP ratio is a ratio of a nation's tax revenue relative to its Gross Domestic Product (GDP), or the market value of goods and services a country produces. Some countries aim to increase the tax-to-GDP ratio to address deficiencies in their budgets. For a country with sound tax system, the higher the value of GDP, the higher the revenue it generate from taxes. The

tables below show the average values of Tax-GDP-Ratio ratio of fifteen lowest and fifteen top rated countries.

|	Low Rated TGR Countries			Top Rated TGP Countries	
S/N	COUNTRY	TGR Rate	S/N	COUNTRY	TGR Rate
1	United Arab Emirates*	1.4	1	Algeria	64.07
2	Kuwait*	1.5	2	Timor-Leste	61.5
3	Equatorial Guinea	1.7	3	Norway	54.8
4	Oman	2	4	Finland	54.2
5	Qatar*	2.2	5	Denmark	50.8
6	Libya	2.7	6	Sweden	49.8
7	Chad	4.2	7	Belgium	47.9
8	Baharin	4.8	8	France	47.9
9	Myanmar	4.9	9	Cuba	44.8
10	Saudi Arabia*	5.3	10	Germany	44.5
11	Republic of Congo	5.9	11	Italy	43.5
12	Iran	6.1	12	Lesotho	42.9
13	Nigeria	6.1	13	Austria	42.7
14	Sudan	6.3	14	Bosnia and Herzegovina	41.2
15	Afghanistan	6.4	15	Iceland	40.4

Source: Heritage Foundation (2016)

Table one shows the Tax-GDP-Ratio of the fifteen countries with low Tax-GDP-Ratio and another set of fifteen with High Tax-GDP-Ratio. The low rated countries are mainly Gulf countries, while the high rated are mostly European countries.
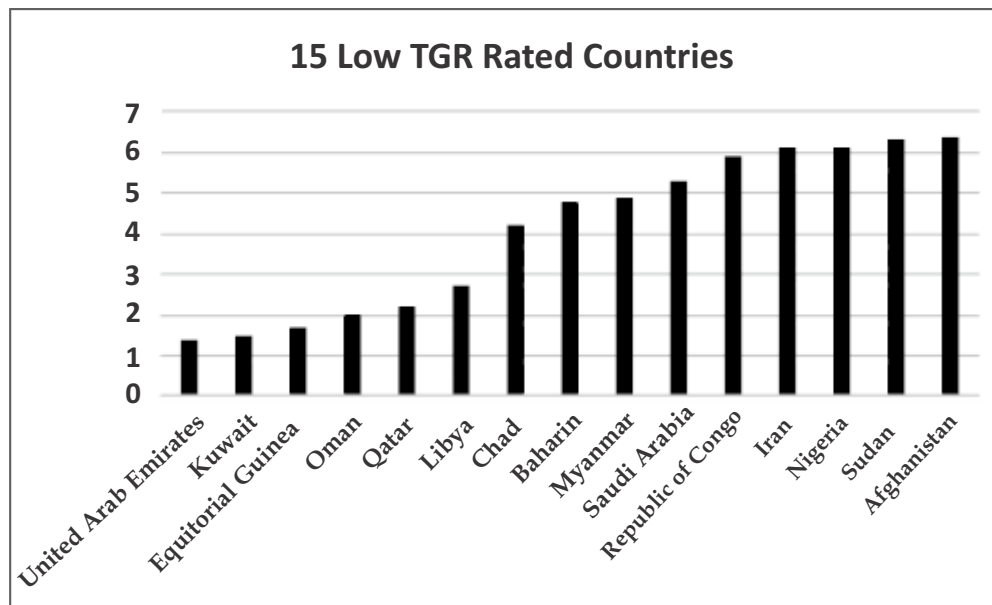
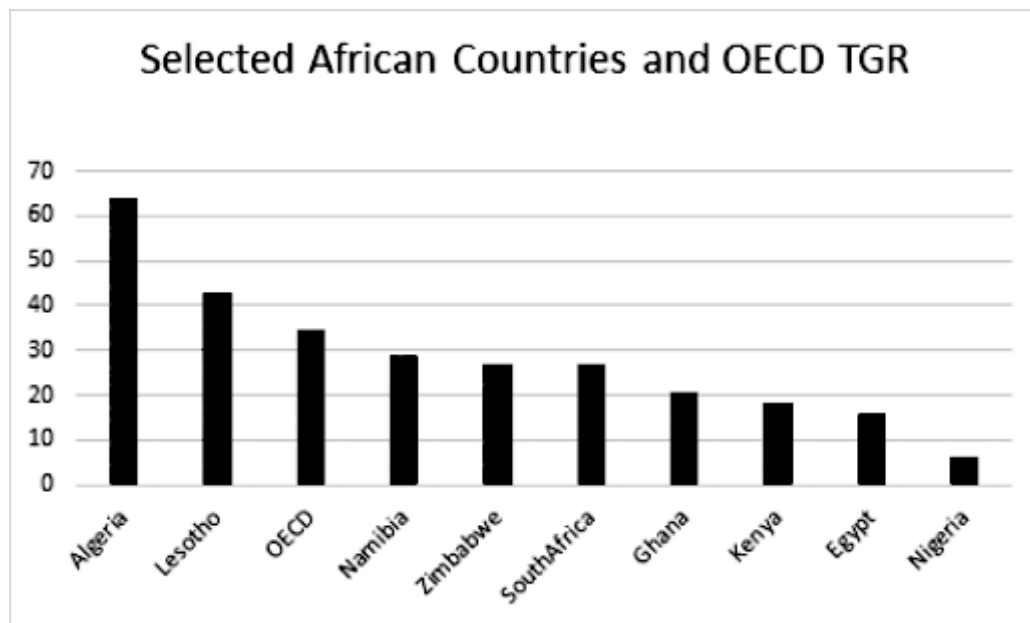**Figure 1** Chart of Tax-GDP-Ratio of 15 low rated countries

Figure 1shows the chart of 15 low tax to GDP rated countries. The rate shows that Nigeria is ranked the 13th lowest amongst countries with low tax to GDP ratio. A look at the countries in the lower ranks shows the Gulf Countries which are usually characterized by low tax rates. These countries are considered rich with manageable population size thus the oil revenue has made them rich and the revenue generated from oil sectors in the Gulf States have been put into infrastructural development and investments. Examples are the United Arab Emirates and Qatar and the Saudi Arabia. These countries do not focus on tax revenue thus having low tax-to-GDP rate. Though Nigeria is also an oil producing state, it has higher population level, poor infrastructure. Although the government understands the importance of tax revenue with a policy aimed at a shift from oil based revenue to tax revenue it has not been able to significantly grow it.
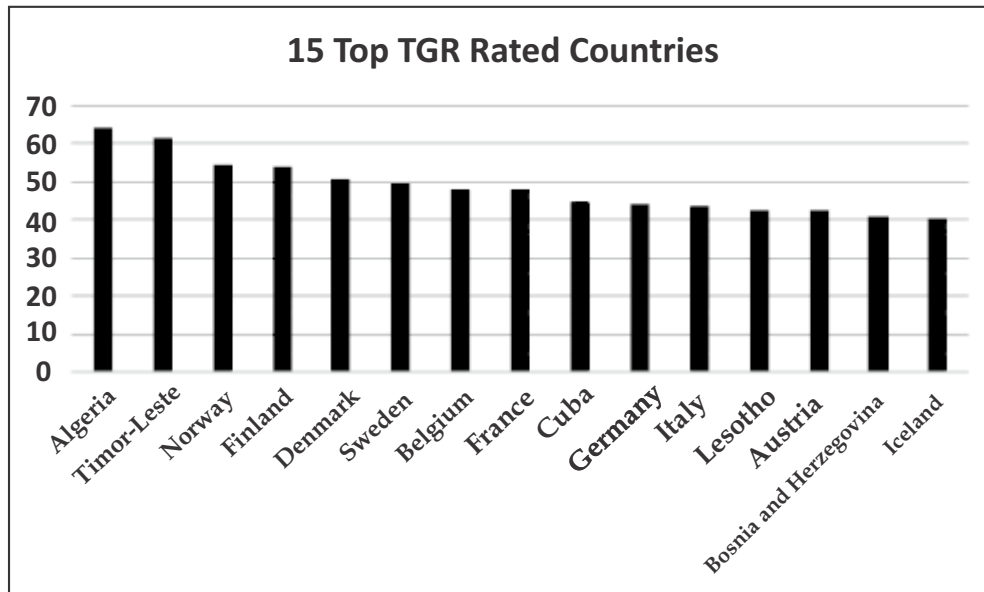
Figure 2: Chart of Tax-GDP-Ratio of 15 top TGR rated countries

Figure 2 shows the chart of the top 15 Countries with high tax rate to GDP ratio. The country with the highest tax-to-GDP ratio considered in this study is Algeria. The country has a high tax to GDP rate of 64% even when the country is also an oil producing state. Most of the countries with this tax rates are developed countries. Over 80% of the countries in this category are European countries. The deduction from this is that the European economy is tax driven and it is mostly non-oil producing state.

Selected African Countries and OECD TGR

Figure 1 Chart of Tax-GDP-Ratio of 15 low rated countries

Figure 3 shows the bar chart of selected African countries and OECD average. Algeria which has world highest average tax-to-GDP rate is from Africa. Amongst the big African Economies, Nigeria ranked the least with respect to tax-to-GDP ratio even when the country has higher GDP value and is considered as the largest economy in Africa. In terms of tax revenue, its performance is very poor as shown by the tax-to-GDP ratio for the respective years. Only three countries in Africa are comparable to OECD tax to GDP rate. The lower tax proportion has affected a sustainable growth in the economy as shocks affecting oil prices which is the major source of revenue to the government throws the economy into crises.

**Table 2:** GDP, Tax Revenue and Tax-GDP-Ratio Statistics of Nigeria

Years	GDP (N'Billion)	Tax Revenue (N'Billion)	Tax-GDP-Ratio
2004	35,020.55	1,194.80	3.41
2005	37,474.95	1,741.80	4.65
2006	39,995.50	1,866.20	4.67
2007	42,922.41	1,846.90	4.30
2008	46,012.52	2,972.20	6.46
2009	49,856.10	2,197.60	4.41
2010	54,612.26	2,839.30	5.20
2011	57,511.04	4,628.50	8.05
2012	59,929.89	5,007.70	8.36
2013	63,218.72	4,805.60	7.60
2014	67,152.79	4,714.60	7.02
2015	69,023.93	3,741.80	5.42
2016	67,931.24	3,307.50	4.87
2017	68,490.98	4,027.94	5.88
2018	69,810.02	5,320.52	7.62
Average	55264.19	3347.531	5.860899
St.Dev	12520.62	1370.218	1.555953

Source: Central Bank of Nigeria (2019)

Table 2 shows the statistics of real GDP, Tax revenue and Tax-to-GDP ratios from 2004 to 2019. The average value of GDP from 2004 to 2018 is 55264.19 billion that of tax revenue is 3347.532 while that of tax revenue-to-GDP is 5.86. This implies that about 94.2% of contribution to GDP within the period was from other sources of revenue like the oil sector. This implies that any factor

affecting the other sources of revenue like oil price fluctuation will significantly impair the level of economic growth of the country. The standard deviations of the variables are also high. This implies lack of stability in growth of GDP and Tax revenue. Without a stable growth, and stable revenue flow the economy will seriously be affected. The volatility value of Tax-to-revenue growth is low which also implies that no serious effort was made towards increasing the rate of Tax revenue-to-GDP since the volatility rate is low.

Table 1 shows the annual GDP values, total tax revenue and the Tax to GDP ratio.
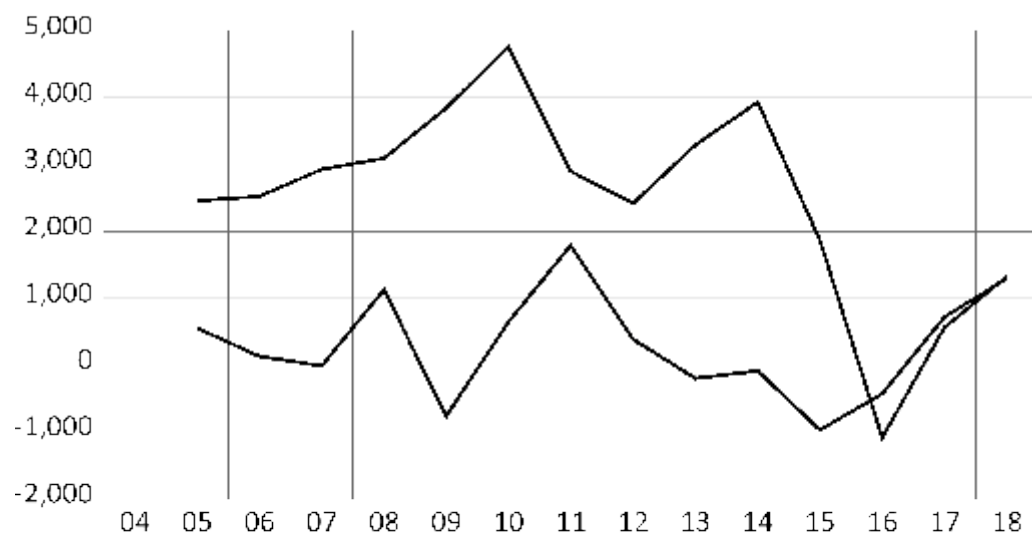
Figure 4 Graph of GDP and Tax Revenue growth of Nigeria

Figure 4 shows the graph of GDP growth and Total Tax revenue growth rate from year 2004 to 2018. The graph depicts that for the majority parts of the years the growth value of GDP and that

of Tax revenue move in the opposite directions. This implies that there is co-movement of the two which is against theoretical expectations. However, a rational explanation of this is that when even there are sufficient revenue flow from other sources such as oil revenue less effort is given to tax revenue. It can be observed that from the year 2014 ending the GDP growth rate decreased to negative growth while the tax revenue grow higher compared to GDP. This is also the period when emphasis was given to tax revenue as a result of decline in oil revenue. However, with increase in oil prices from the middle of 2017 the GDP rate surpassed that of tax revenue growth.

Tax to GDP Ratio

YEARS
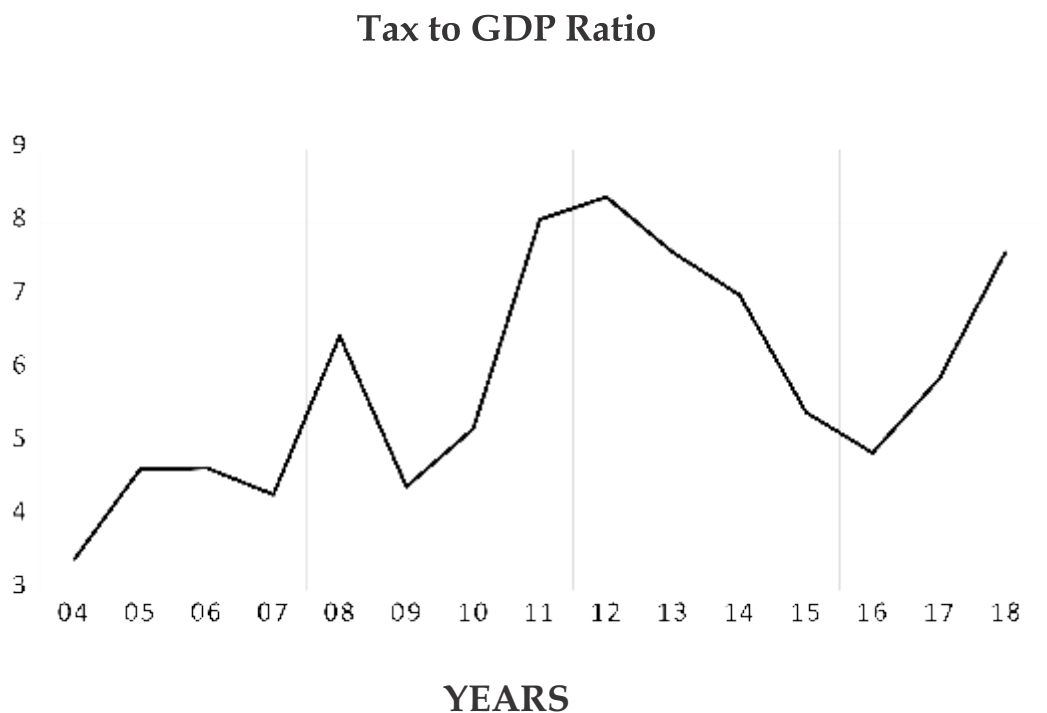
Figure 5: Graph of Tax-GDP ratio growth of Nigeria

Figure 5 shows the movement in the rate of tax revenue to GDP. The movement shows that there is high level of instability in tax performance with respect to GDP. It implies that efforts made to improve tax revenue subsequently reversed back to previous position or even worse. The highest contribution of Tax to GDP was in the year 2012 when it went as high as 8.35%. The rate later declined until the year 2016 when it continued to grow.

G. CHALLENGES TO NIGERIA'S TAX SYSTEM

The following challenges to increasing the tax /GDP ratio are common to all developing African countries, Nigeria inclusive: -

1. Generally, the objectives of a good tax system such as economic efficiency, effectiveness and equitability frequently conflict. In addition, progressive taxes in highly unequal societies including Nigeria are difficult to achieve.

2. Pirtilla (2018) reports that up to 80 % of the workforce in African countries are outside the formal labour force. Even though taxation can be carried out in several ways, one of the most important components of modern tax system is income tax which is deducted from wages and salaries. Income taxation facilitates a broad tax base that is difficult to evade. Unfortunately only about 20% of the workforce in Africa is subjectable to paying income tax.

3. There is hardly any taxation in Africa. Aid appears to be the only external financial inflow to Africa. According to Fjeldstad (2011), African countries are completely

dependent on aid. For instance, in 2007, foreign aid amounted to USD 104 billion (from OECD‑DAC countries) and USD 8 billion (from non‑DAC donor countries). The Foreign direct investments in Africa in 2008 were USD 88 billion. It was mostly shifted to extractive industries and the beneficiaries were Nigeria, Angola, Egypt and South Africa. The remittances from Africans living abroad in 2008 totaled USD 41 billion.

Although there are improvements in their tax systems such as simplification of the tax system, improved tax administrations at the central government level and improved attitudes of tax administrations towards some segments of taxpayers, tax reforms are hardly on the policy agenda in Africa. One of the major factors contributing to low tax revenue and consequently low tax-to-GDP ratio is inefficient tax administration. The problem of tax administration is systemic. One of the major problems is fiscal federalism. Which arm of government collects which tax? Thus tax jurisdiction problem creates room for tax avoidance and evasion as neither the federal nor state government ends up benefiting from the tax revenue. Another fiscal issue is the problem of multiple taxation which subjects same tax base to two or more different multiple taxes. This creates room for the taxpayers to evade or avoid paying taxes. Also another major problem in tax administration is the issue of corruption in the system in the

system. The corruption in tax administration is tripartite. One is corruption by the taxpayers where correct tax amounts are not declared. Thus lower taxes are paid to the relevant tax authorities. The second is the corruption on the part of tax authorities where tax collectors connive with the tax payers to shortchange the government. This usually happen with the taxpayers being issued clean tax clearance where it should not. The third is on the part of the government where the revenue generated from the tax revenue is not utilized to the benefit of the taxpayers as they are stolen from the government purse. This creates apathy with the taxpayers using all available means to minimize tax liabilities, thus a shortage in tax revenue.

4. REVENUE SHOCK ARISING FROM TRADE LIBERALIZATION

Economists have long considered trade liberalization as a central component of growth and development. As increased trade and capital flows spur growth, the loss in trade tax revenues is expected to be easily replaced with the taxes collected from a more dynamic private sector. Consequently, trade liberalization in the developing world was accepted as a necessary step in the path to development success. However, this rosy view notwithstanding, many developing countries have been facing formidable challenges recovering from the revenue shock and substituting their lost trade tax revenues with domestic

taxes (see Rudra & Bastacus, n.d).

The end result is that liberalizing trade has translated into a large and rapid loss of trade tax revenues for governments across the developing world.

A large percentage of citizens (and firms) in poor economies are logistically difficult to tax.

5. There exist weak bureaucracies, staff, and obsolete technologies

6. Difficulty in engaging in tax reform in the liberalizing environment as governments are in a dillema. For instance, they face rising political pressures to keep domestic taxes low so that less-productive firms can survive in the face of international market competition and, at the same time, more-productive exporting firms are demanding even lower tariffs

7. Generally, taxation is low on the domestic political agenda.

8. Most often, the political and economic elite are not part of the tax base. In Nigerian a lot of people do not pay taxes and the ones who pay, pay paltry sum to enable them get Tax Clearance Certificate

9. The tax bases are astronomically narrow: One of the major causes of the low rate of tax revenue to GDP is narrow tax base. Out of estimated 200 million people in Nigeria the World Bank put the economically active population at 65

million, out of this 65 million the Federal Government recently claimed to have increased the taxpayer's population from 10milion to 20 million. This puts the percentage of active tax payers at 31%. This implies lack of efficiency in tax administration in bringing reasonable number of tax payers into the tax bracket. As noted by Oladipo and Ogochukwu (2019) this results to pressure on the active tax payers as government will tax them more in order to meet its revenue demands.

10.   Massive revenues from natural resources are lost

11.   Illicit capital flows which are facilitated by tax havens entrench the inefficient tax systems in Africa.

12.   In Nigeria, a lot of tax revenues are lost as a result of oil pipeline vandalism and illegal crude oil bunkering.

13.   Poor taxation of the Informal Sector: As noted in IMF working paper on informal economy in Sub-Saharan Africa, it is estimated that the informal sector accounts for 50% to 65% of economic activities in Nigeria. The informal sector in Nigeria is estimated at 63%. Business in the informal sector hardly pay taxes or remit other taxes such a value added tax and withholding tax to the relevant authorities. Thus, there is a high level of tax leakages that would have significantly contributed to the revenue derived in the country.

14.   Low Level of Tax Education: Another reason for the low level of tax revenue to GDP ratio is the low level of tax education. The general literacy rate in the country is around 50%. The level of tax education is expected to be lower as tax issues are sometimes very complex. Many tax payers do not know the various taxes they are expected to pay and the businesses as well lack the profession knowledge on tax computation and remittance. There is a high level of non-remittance of withholding tax in our tax system.

15.   Tax Expenditures: One of the factors contributing to the low level of tax revenue is tax expenditure. Tax expenditure comprises of the reliefs and allowances granted to businesses or to taxpayers in a form of social scheme. As defined by the *United States Congressional Budget and Impoundment Control Act of 1974* it is "revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability." Though some of the allowances are given as social benefits, they are supposed to be revenue to the government which the taxpayers enjoy directly without the revenue authorities accounting for them directly as a tax income. This implies that countries which do not entertain for such allowances and reliefs will have higher tax revenue. For example,

companies engaging in manufacturing and agricultural production; mining and solid minerals; and wholly exported and from which trading earnings are less than one million Naira pay only 20% of their accessible profit for the first four years. This could have constituted revenue for the government. Nigeria allows for many deductions and reliefs which contribute to lower tax revenue and consequently, tax-to-GDP ratio.

16.   **Under-Utilized Excise Tax Revenue**

According to International Monetary Fund (2018), excises on alcohol, tobacco, fossil fuels, motoring and environmental degradation (such as littering and pollution) are among the most import pillars of tax revenue systems around the world.

Several considerations underpin the wide use of excise taxation: (a) excises on smoking, abusive drinking, and environmental degradation are imposed to internalize the external costs (physical, financial, psychological) that consumption of such products and activities impose on the society, in this way promoting an efficient allocation of resources; (b) excises on items of luxury goods consumption and airtime may be used to promote progressivity in taxation; (c) excises on motor fuel and motor vehicles can be rationalized as proxies for the cost of government-provided road services and the external costs (pollution, congestion) imposed on other people; and (d) the marginal cost of collecting excise duties is

much lower than that of all other taxes, including the VAT.

In Nigeria, excises yield little revenue and do not fulfill their role in internalizing the negative external costs of use or consumption. At current levels, excises contribute less than 2.3% of total tax revenue or about 0.04 percent of GDP-a situation which contrasts sharply with comparator countries where excise duties contribute on average 12.3% of total tax revenue (more than 5 times higher than Nigeria or 3.2 percent of GDP (Table 3). On a comparative basis, it should be possible therefore to triple or quadruple excise tax collections in Nigeria as per Table 3 Nigeria:

Table 3: Nigeria Excise Collections (2016) and Selected Countries (2014)

Countries	Total Tax, as percentage of GDP	Excise Duty Revenue, as percentage of:	
		GDP	Total Tax
Nigeria (Non-oil)	4.1	0.1	2.3
Comparator Countries			
Ghana	15.3	1.7	11.0
Kenya	19.5	2.9	14.9
South Africa	27.9	3.5	12.2
Commonwealth			
Australia	27.6	3.2	11.4
Canada	31.9	2.9	9.2
United Kingdom	32.5	2.4	7.3
Others			
United States	26.4	2.3	8.7
Turkey	30.0	6.4	22.2

According to International Monetary Fund Report (2018), the excise taxation base in Nigeria is relatively narrow. The Federal Government taxes only tobacco products and alcoholic beverages, independent of alcohol content, at a rate of 20 percent (see Table 4).

Petroleum products are not taxed, while states tax motor vehicles. Other products, such as non-alcoholic beverages, fruit juice, and telephone recharge cards, had been subject to a 5 percent excise before their removal in 2009. Following the British tradition, Nigeria does not levy excise duties on imported excisable goods, but subsumes these in the import duty.

The draft 2019 Budget presented by the authorities to the National Assembly in December 2018 incorporates revenue assumptions from increases in excises (implied on alcohol and tobacco).

Table 4 Nigeria Excisable Goods, Excise and Duty Rates (Percentage)

Duty or Tax	Cigarettes	Beer	Wine	Spirits	Tax Base
Importation					
Import Duty (ID)	20%	Prohibited	20%	20%	CIF Value
Levy	50%	N/A	50%	50%	CIF + ID
Port Development Surcharge	7%	N/A	7%	7%	CIF + ID
Comprehensive Import Supervision Scheme	1%	N/A	1%	1%	CIF + ID
Total effective duty at import	89.6%	N/A	89.6%	89.6%	CIF + ID
VAT	5%	N/A	5%	5%	
Total effective duty and tax on CIF value	94.1%	N/A	94.1%	94.1%	
Domestic					
Excise duty	20%	20%	20%	20%	Unit cost
VAT	5%	5%	5%	5%	Unit cost + Excise
Total effective duty on pre-tax value	26%	26%	26%	26%	

Source: Nigerian Custom Service

According to International Monetary Fund (2018), the following reforms of excise taxation in Nigeria would strengthen its revenue-raising efficiency and externality- correcting properties:

(a). Converting *ad-valorem* excises on alcohol and tobacco to specific (and higher) rates indexed for inflation to reflect the external costs of consumption and production.

In line with international practice, tobacco excises could be more than doubled in real terms, imposed at NGN 100/pack of cigarettes of 20 over a three-year period (with equivalent duty for other tobacco products). Alcohol excises could be linked to alcohol content (beer, wine, and spirits) and increased in value. For example, doubling the excise duty on beer would align it with the current Kenyan excise burden.

(b). Recognizing the function of environmental charges in increasing resource efficiency and revenues. This could be achieved by introducing specific consumer charges on the use of plastic shopping bags, plastic bottles, aluminum cans, and incandescent light bulbs (for example, a waste packaging charge of NGN 5 per plastic bag). To compensate for the cost of global air pollution (carbon dioxide, methane, nitrous oxide) and its contribution to climate change, a low-rate excise charge of NGN 10/liter could be imposed on all fossil fuels (gasoline, diesel and kerosene)

(c). Contributing to the cost recovery of road transport infrastructure. In addition to air pollution, road users create multiple externalities in the form of road damage, particularly by heavy trucks; congestion, which carries an implicit tax on labor; and noise and accident costs. Consumers would make

better decisions regarding their use of the road network if such costs were internalized in the price of fuel—for example, by introducing an additional motoring fuel duty on gasoline and diesel products (NGN 10/liter on leaded gasoline and diesel fuel, NGN 5/liter on unleaded gasoline). Since kerosene is mostly used by poorer households for cooking, heating and lighting, kerosene could be exempted from this additional excise duty on motoring.

(d). Improving tax progressivity by increasing excise duties on luxury goods and air time. This could be achieved by increasing excise duties and motor vehicle license fees on cars (new and imported) and proceed with preparations for introducing a low charge on mobile phone use (airtime) on call minutes and SMS.

(e). Providing a level-playing field for the internalization of external costs by levying excise duties at equal rates on domestically produced and imported goods. A reform of excise taxation would correct the current policy of subsuming excise on foreign goods in the import duty. This would make the protective function of the tax system the exclusive prerogative of the import duty regime, while allowing excise duties to serve as an allocative function irrespective of whether the products originate domestically or from abroad. As elsewhere, VAT should be imposed on the excise (and import) duty-inclusive value of excisable items.

Converting *ad-valorem* excises into a specific rate system is supported by both theoretical and practical considerations.

Economic theory favors the correction of externalities through specific duties over ad-valorem taxation as the external costs on the society of smoking, drinking, motoring, and polluting are independent of the underlying products sales price. In practice, excises provide the authorities with the opportunity to increase revenues without major administrative costs associated with a new ICT system development or the hiring of additional staff. As specific duties require only counting (e.g., cigarettes) or measuring strength (alcoholic beverages) or volume (e.g., of motor fuels), they pose no contentious valuation issues relating to unit cost or unit value at the manufacturing or the import stage. To preserve the real value of excise revenue, specific duties would need to be indexed for inflation through annual adjustments. Gradual excise duty increases at prevailing ECOWAS levels could yield revenues of 2.5% of GDP in the medium term, and of about 4% of GDP in the long run. In the medium term, a comprehensive review should be made of all taxes, duties, levies and charges on road transport, broadly defined. Such a review should have regard not only for revenue-raising efficiency aspects and externality correcting issues, but also for distributional incidence aspects (as discussed on the distributional aspects of fiscal reform). The review should be undertaken in cooperation with the Nigerian States and the Federal Road Authority.

H.   THE WAY FORWARD

1.   In addition to the suggested solution to the challenges identified the government needs to take the following actions:

(a) Improving the existing tax system with a view to reducing inequalities through:

(b) Increasing progressiveness and by raising additional revenue through indirect taxes;

(c) Focusing on tax reforms that would simultaneously facilitate revenue growth, build administrative capacity and build accountability;

2.   Government should also consider taking the following actions:-

(a)   improving her local government taxation;

(b)   levying taxes as consensually and as transparently as possible;

(c)   supporting civil society groups' capacity to engage with the state on tax issues;

(d)   making tax strong on the domestic political agenda

(e)   carrying out tax informality surveys and surveys of taxpayer perceptions, to identify willingness to pay issues around inequality and social injustice,

(f)   establishing better links between taxes paid and service delivery, and

(g)   Intensifying efforts to stop oil theft and illogical oil bunkering

3.   In addition, the Nigerian Government should provide tax reforms that would

    (a)   reduce tax exemptions or eliminate them completely;

    (b)   tackle capital flight aimed at evading taxation;

    (c)   strengthen the administration of natural resources taxation , especially in extractive industries;

    (d)   improve progressivity through income tax and property taxes;

    (e)   seek for more effective ways to tax the informal sector;

    (f)   put in place a simplified tax regime for micro and 'informal' sector ;

    (g)   establish a dedicated tax unit for Small and Medium enterprises in the country;

    (h)   Improve local government taxation (see Fjeldstad, 2011).

4.   Nigeria and other developing nations should urgently strive to replace almost a third of their already low tax revenue base with 'hard to collect' domestic taxes.

5. Effective use of tax clearance certificate for transactions.

I. CONCLUSION

There is no gain in saying the fact that transforming the apparently stagnated tax-to-GDP ratio in Nigeria demands

holistic review of the current tax administrative system and the overhaul of the Nigerian economy. However, without sounding pessimistic, it is doubtful if the government can muster the required political will to change the rhetoric.

It is also unlikely that the tax authorities will adopt the recommended measures for developing the tax system as they may prefer to deploy more immediate and aggressive measures to shore up tax revenue. It is thus essential for taxpayers who are already complying to take extra measures to ensure that their records are properly kept and contact experts to conduct tax health checks where necessary to avoid surprises when the tax authorities attempt to review taxpayer's records to identify additional tax exposures to make up the numbers.

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