THE IMPACT OF VALUE ADDED TAX ON THE NIGERIAN ECONOMIC GROWTH

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Abstract—*There is much literature on the impact of Value Added Tax on the Nigerian Economic growth. However, these literatures suffer from one challenge to the other. These challenges include time range, methodology used and so on which does not reflect the current economic realities. This study explored the impact of VAT on economic growth in Nigeria using empirical studies. The review recommends that further studies should be carried out using current data and appropriate study design so as to gain firm understanding on the impact of Value Added Tax on the Nigerian economic growth.*

Index Terms— Taxation*, Revenue, Value Added Tax and Economic growth*

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1.0   INTRODUCTION

1.1   Background to the Study

The basic philosophy and continuous review of VAT is embedded in the reason for the existence of government. That is, a human being, acting as an individual in society, cannot provide for himself certain crucial services in a community. These include, defense, roads, justice, law etc. Government exists to provide these collective services or public goods. In other words, the public sector has to be financed. Taxation is therefore the price of the social contract between the governed and the government for the provision of social goods and services bythe latter to the former [10].

One of the precedence for the introduction of Value Added Tax (VAT) in Nigeria was based on the fact that taxation as an instrument of fiscal policy is vital in generating revenue to finance the activities of government, redistribute income, stabilize the economy as well as stimulate growth and development [10]. For the past one and half decade of the nation's democracy, the Nigerian economy has been relatively buoyant as a result of oil boom. However due to the increasing cost of governance, drastic drop of oil prices, inflation and the current global economic recession have directed the attention of the government to look inward to the importance and sustainability of taxes, especially Value Added Tax.

The need to direct and re-organize the priorities of the Nigerian economy became urgent. The drastic drop from the international price of crude oil which is Nigeria's biggest source of foreign exchange earner face with the inevitable vulnerability of a mono-economy. According to [9], the administration of tax systems and enthronement of a tax payment culture nationwide has continued to challenge successive government in Nigeria. One of the attempts to expand the tax net with minimum resistance and also to reduce tax evasion so that most of the tax income revenue would get to the government was the introduction of VAT.

This is why [14] stated that in Nigeria; the government fiscal policy is divided into three tiered tax structure: Federal, State and Local governments, each with their different tax jurisdiction. Also, taxes constitute the key sources of revenue to the federation account shared by the three tiers of government. [9]Is with the view that tax system such as VAT should be able to mobilize a nation's internal resource in order to create an environment conducive to promote economic growth.

Despite the contributions and huge revenue generated through VAT, the federal, state and local governments complain of insufficient fund to embark on projects and the citizens have always lamented of poor infrastructural facilities, unemployment, low capita income etc. which have resulted to poor standard of living, high crime rate and other social ills has been on the increase. Nigeria is still listed and regarded as a third world country. A situation of this nature entails asking what is the relationship between VAT and Gross domestic product and total consolidated revenue of the government.

1.2   Statement of the Problem

The government may be happy about high growth of VAT revenues, there are increasing complaints from the organized private sector and the general public about the effect of VAT on their operating costs and the prices of their products especially in this period of economic recession.

Another problem perceived by enterprises or businesses in Nigeria is that of increase in cost of raw materials, finished goods and services caused by VAT. Poor relationship between tax payers and the tax authorities is also a source of concern.

1.3   Objective of the Study

The main objective of this study is to review and assess existing literature on the impact of Value Added Tax on the Nigerian economic growth. This is to enable us have a good understanding on the relationship between Value added tax and the Nigerian economic growth.

1.4   Methodology

This study uses survey of literature from empirical studies on the impact of Value Added tax on the Nigerian economic growth that is based on the critics of literature reviewed.

2.0   REVIEW OF RELATED LITERATURE

In this section we shall look at the theoretical and conceptual frame work of Value Added Tax before looking at other related literature to VAT as a system of taxation.

2.1   Theoretical Framework

2.1.1   Tax Theories

Taxation forms the most important source of revenue to the government. The Value Added Tax is one of such revenue sources today since its inception in 1994. The theory of VAT was first credited by a French Economist Maurice Laure in 1954 and

was first introduced in France on the April 10th, 1954. Maurice Laures theory of VAT was envisioned on sale tax on goods that did not affect the cost of manufacture or distribution but was collected on the final price charged to the consumer [9]. Since VAT is a subset of the entire tax system in Nigeria, it becomes imperative to look at the basic theories surrounding taxation. These theories include among the following;

Convenience theory; this theory was propounded by Adam Smith, the capitalist patriarch. The theory states that tax is a compulsory levy which must be borne by all eligible to bear the burden. The theory however prescribes here that the payer nonetheless should be helped to carry his cross without mush sweat grouse [3].

Expediency theory; this theory was posited that every tax proposal must past the test of practicability. It must be the sole consideration weighing the authorities a tax proposal.

Benefit received theory; this theory is based on the assumption that there is basically an exchange relationship between tax payers and the state. The state provides certain goods and services to the members of the society and they contribute to the cost of these supplies in proportion to the benefits received as stated by [9]

Faculty theory; According to [9] this theory states that one should be taxed according to the ability to pay more so that a citizen should pay taxes just because he can, and his relative share in the tax burden is to be determined by his relative paying capacity. The bottom line of this theory is to maximize the distributive effects of taxes within the country.

Cost of service theory; this theory assert that semi-commercial relationship exist between the state and the tax payer. According to the theorist, the state give up basic protective and welfare functions to cover the cost of the services. This theory is homogenous with benefit received theory [8]

2.1.2   Economic Growth theories

The Harrod-Domar model theory; According to [6] the Harrod-Domar model of economic growth is based on the experiences of advanced economies. They are primarily addressed to advanced capitalist economy and attempt to analyze the requirements of steady growth in such economy. Both of them are interested in discovering the rate of income growth necessary for a smooth and uninterrupted working of the economy. Though their models differ in details, yet they both agree. Harrod and Domar assign a key role to investment in economic growth. But they lay emphasis on the dual character of investment. Firstly, it creates income and secondly, its augments the productive capacity of the economy by increasing its capital stock.

The Salow-Swan theory; The Salow-Swan theory of economic growth postulates a continuous product function linking output to the inputs of capital and labour which lead to the steady state of equilibrium of the economy [5].

The Endogenous Growth theory; the endogenous growth model emphasis technical progress resulting from the rate of investment, the size of the capital stock, and the stock of human capital.

2.2   Conceptual Framework
2.2.1   Concept of Taxation

According to [13] taxation may be defined as the compulsory levy by government through its various agencies on the income, capital, or consumption of its subjects. These levies are made on personal income such as salaries, business profit, interests, dividends, commissions, royalties, rent etc it may also be levied on capital gains and petroleum profits. With effect from 1st April, 1979 until 1st January, 1996 tax was levied in Nigeria on capital gifts and inheritance under capital transfer tax Decree.

[10], the tax which an individual is bound to pay ought to be certain and not arbitrary. The time of payment, the manner of payment, the quantity to be paid ought all to be clear and plain to the contributors and every other person.

Taxation is a compulsory levy imposed on the resident and other legal personalities living in a society by the government otherwise known as the tax authority [3]. The payment of tax once levied is compulsory and its nonpayment usually attracts some penalty. The objective of taxation primarily is to raise revenue for persecuting the business of governance. An attribute of a tax is that payers are not to expect to receive back equal benefit for it. In this context, a tax is said not to be quid pro quo in terms of public goods and services from government.

[12]Asserted that, tax is a compulsory payment made by all concerned to the government of a country from which essential services are rendered, without necessarily offering an explanation on how the money generated was spent or equating the services with the money collected.

2.2.2   Concept of Value Added Tax (VAT)

VAT is a consumption tax levied at each stage of the consumption chain borne by the final consumer of the product or services. Each person is required to charge and collect VAT at a flat rate of 5% on all invoice amounts, on all goods and services not exempted from paying VAT. Value Added Tax with effect from 1st January, 1994, tax is now imposed on a wide range of consumption (purchases) by companies and individuals alike, under the Value added Tax (VAT) Act. This tax is at a standard rate of 55 on most purchase of goods and services with few exemptions such as food, petroleum products, educational books and newspapers, medical services and pharmaceutical products. The Value added though a relatively new concept in Nigeria has become a principal source of revenue to the government. VAT maintain a lead over company income tax (CIT) as a source of revenue from 1996 until 2006 when CIT actually caught up and overtook VAT as a source of revenue to the [13]

Value Added Tax can be defined as the incremental value which a producer using labour contributes to his raw materials of purchases before selling the processed goods or services. Here, the producer can be a manufacturer, distributor or supplier of goods and services [10].VAT is a tax levied on the value added at various stages of sales.

2.2.3   Concept of Economic Growth

[6]Defined economic growth as an increase in the production and consumption of goods and services. It occurs when there is an increase in the product of population and per capital income. Economic growth is often and generally indicated by increasing real gross domestic product (GDP) or gross national product (GNP). In this study, economic growth is measured by GDP.

[14] Define economic growth as the process by which the productive capacity of an economy increase over a period leading to rise in the level of national income. They emphasized that when there is economic growth, it shows in form of an increase in income levels, an expansion in the country volume of trade and consumption. Thus, in general terms, economic growth refers to increase in output quantitatively per unit of input while economic development refers to qualitative changes in economic wants due to the structural and technical arrangement of improved goods and services in the economy. Economic growth

and economic development can be used interchangeably despite the fact that they can mean two different things.

2.3 Empirical Review

There are a lot of research work on Value added Tax. This is as a result of its advantage over other forms of taxes in recent times. Below are some of the reviews of works done under the topic;

[4] Investigated The Roles of Value Added Tax in the Economic Growth of Nigeria.The paper empirically examined the contribution of VAT to the development of the Nigerian economy. Time series data on the Gross Domestic Product (GDP), VAT Revenue, Total Tax Revenue and Total (Federalgovernment) revenue from 1994 to 2010 sourced from Central Bank of Nigeria (CBN) was analyzed, using both simple regression analysis and descriptive statistical method. Findings showed that VAT Revenue accounts and total revenue account for as much as 92% significant variations in GDP in Nigeria. A positive and insignificant correlation exists between VAT Revenue and GDP. The methodology is appropriate however the period of study may not be relevant to the current economic reality.

[8]Carried out a study on investigating the relationship between VAT and GDP in Nigeria. The period of study was from 1994-2008 using a secondary data from CBN statistical bulletin analyse with pearsons' product movement correlation of coefficient. The study reviewed that VAT is not effective as revenue earner and the study recommends maintenance of the status quo. Base on the period of the study above, it would have been more appropriate for the investigation to cover a period of 1994-2015.

[1]Carried out an investigation on Value Added Tax and Economic Growth of Nigeria. The aim was to increase the revenue base of government and make funds available for developmental purposes that will accelerate economic growth. Time series date on GDP, VAT revenue, Total tax revenue and total federal government revenue from 1994-2008 sources from CBN. The data was analyzed using simple regression and descriptive statistic method. Findings show that there is a positive and significant correlation between VAT revenue and GDP. The study recommended that, all identified administrative loopholes should be plugged for VAT revenue to continue to contribute more significantly to economic growth. The authors used appropriate study design, variables for the study but there is a need to extend from 1994-2016 to be able to have a better understanding on the impact of VAT on the Nigerian economic growth.

[8]Carried out a study on the empirical evaluation of the contributions of Value Added Tax to Revenue generation and Gross Domestic Product in Nigeria. The purpose of the study was to examine the impact of VAT on revenue generation and GDP. The study covered a period of 18 years from 1994-2008 using ordinary least square regression for data and the result showed that VAT has a significant impact on GDP.

[11] Investigated Value Added Tax remittance; Observation from developing country. The challenge of the study was to evaluate the performance of VAT as revenue earner in Nigeria and assess revenue generated from VAT since its inception to know if it has been on the increase or decrease. The study covered a period of 7 years from 2005-2011 using a survey research design and the data analysis source from federal Inland Revenue service. The study finds out that VAT revenue has been on the decrease within the period of study and recommends that the Nigerian government should make adequate provision for retrieving the proceeds of VAT from companies and other agents of collection. Even though the right study design however, the study used primary data which is usually subjective and a matter of fact cannot be relied upon completely.

[10] Investigated correlation between Value Added Tax and National revenue in Nigeria. Data spanning from 1994-2012 sourced from CBN statistical bulletin were used, using Error correction model to analyze. The result reveals that VAT is the second long - term source of the federally collected revenue and recommends that all identified loopholes be plugged for VAT revenue to contribute more to total federally collected revenue. This model used by the study is not widely used by most researchers on the topic and might not be accepted as such.

[9]Carried out a study on the Impact of Value Added Tax on Economic Growth in Nigeria from 1994-2012. Data collected from CBN statistical bulletin and FIRS reports using ordinary least square. The result from the model reveals that there is positive significant impact of value VAT on economic growth as proxy by GDP in Nigeria. It recommends that government should put in place measures to effectively utilize generated VAT revenue for infrastructural and economic development. The study is reasonable and recommendable. However there is need to uphold the findings with current studies because of changes in the economy.

[10] Investigated the impact of Value added Tax on Nigerian Economic growth from 1994-2012 employing the Error correction model using time series data from CBN statistical bulletin and FIRS. Findings were that there is a positive and significant correlation between VAT revenue and real GDP are there are some problems inhibiting its potency. The study also recommends that all identified problems and administrative loopholes should be plugged for VAT revenue to contribute significantly to economic growth of the country. This Error correction model is not commonly used as might not be generally accepted and there is also a need to be extended from 1994-2016.

[15]Investigated the Impact of VAT on Nigeria Economic Growth using time series data which were sourced from CBN statistical bulletin for a period of 5 years from 2009-2014. Ordinary least square regression technique was used in the analysis of data. Findings from the study revealed a significant impact of VAT on the economic growth of Nigeria. It was recommended that government should embark on a mass enlightenment campaign to enlighten the public on the importance of paying their tax to minimize incidence of tax resistance. The researcher used the right tool for measurement however, the period covered was not reasonable enough and need to be expanded.

[7]Took a study on the Evaluating the impact of Value Added Tax on the economic growth of Nigeria from 1994-2014. The study uses a secondary data which was analyzed using Johanse (1988) co-integration test. The study found evidence of a significant positive impact of VAT on economic growth. The study therefore recommends that VAT should be sustained hence; all identified administrative loopholes should be covered for VAT to continue to contribute more significantly to the economic growth of the country. The study is considered reasonable for the time period covered however, the instrument adopted may not be generally acceptable in the current time.

[8]Carried out a study on Value Added Tax and Economic Development in Nigeria. The study covered a period of 18 years period between 1994-2012. Multiple regressions was used to analyse the data from CBN statistical bulletin, results showed a negative significant relationship between value added tax revenue

and gross domestic product. The study recommend that federal government should educate the general public more on the essentials of VAT payments and also that machineries should be put in place to ensure that VAT revenue does reduce as this will help foster economic development. The period covered was reasonable enough and the right tool was used but there is need to update it to 2016.

3.0   Conclusion

From the above empirical review from extant literature, it is obvious that Value Added Tax (VAT) has a positive relationship with the Nigerian economic growth though other studies review a negative relationship and most of the findings using different tools of analysis (Multiple regression and Error correlation model) concluded that better methods of closing the loop holes should be adopted in order to increases earnings on VAT revenue and government should create avenues for more awareness on the importance of VAT.

3.1   Recommendation

All the works reviewed were reasonable; however, most of the available studies were from 1994-2012. Therefore, it will be appropriate to update the study up to 2016 to meet with the current economic realities more especially now that there is a total shift from oil driven economy to the non-oil where tax revenue becomes very crucial for the diversification of the economy

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