Nigeria's Tax Reforms and the Quest for Economic Stability: A Conceptual Narration

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Abstract

This study explores the relationship between Nigeria's tax reform bill and economic stability, providing a conceptual narration of the potential impacts of tax reform on the nation's economic growth and development. The study examines the current tax regime in Nigeria, highlighting its limitations and challenges, and analyzes the proposed tax reform bill's potential to address these issues. The study investigates how tax reform can influence economic stability through various channels, including increased revenue generation, improved investment climate, and enhanced economic competitiveness. It also discusses the potential challenges and limitations of implementing tax reform in Nigeria, such as resistance from special interest groups and administrative capacity constraints. Using a conceptual framework that integrates tax theory and economic stability, this study provides a nuanced understanding of the complex relationships between tax policy, economic growth, and development. The project contributes to the ongoing debate on tax reform in Nigeria, offering insights into the potential benefits and challenges of reforming the tax system to achieve economic stability. The findings of this study have implications for policymakers, researchers, and stakeholders interested in Nigeria's economic development. The project concludes by highlighting the need for a comprehensive and inclusive tax reform process that addresses the country's unique economic challenges and promotes sustainable economic growth and development. By striking a balance, taxation can support economic stability and promote sustainable development because they are interconnected. Ultimately, this study aims to inform and enrich the discourse on tax reforms and economic stability in Nigeria.

Keywords: Taxation, Tax Reforms, Resource Control, Tax Burden, Economic Stability

Introduction

In the pursuit of economic stability, governments often employ tax adjustments as a crucial policy tool. Tax policies can significantly impact economic activity, influencing factors such as investment, consumption, and employment. The introduction of President Bola Tinubu's Tax Reform Bill has sparked widespread debates across Nigeria. This proposed legislation aims to overhaul the country's tax collection and administration systems, presenting an opportunity to create a more equitable and efficient taxation model.

At the heart of the bill are transformative provisions, such as revisions to the Value Added Tax (VAT) revenue-sharing formula and exemptions for small businesses and the average Nigerians. While these changes could potentially revitalize Nigeria's economy, they also expose critical issues within the country's federal structure, particularly the economic imbalances among regions (States and Local Governments).This narration explores the intricate relationship between tax adjustment and economic stability, highlighting the potential benefits and challenges of using taxation to stabilize the economy.

Relationship between Tax Reform and Economic Stability

The relationship between tax reform and economic stability is complex and multifaceted. Tax reforms can significantly impact economic stability by influencing factors such as revenue generation, investment, consumption, and economic growth (Bird, 2022). Taxation serves as a vital instrument for governments to regulate economic activity and achieve stability. By adjusting tax rates, policymakers can influence the overall level of economic activity, mitigating the effects of economic downturns or overheating.

For instance, during periods of recession, governments can implement tax cuts to stimulate economic growth, increase aggregate demand, and create jobs. Conversely, during periods of high inflation, governments can increase taxes to reduce aggregate demand and curb inflationary pressures.

Benefits of Tax Adjustment for Economic Stability

i. Countercyclical Policy: Tax adjustments can be used to counteract economic fluctuations, helping to stabilize the economy during periods of boom or bust.
ii. Increased Investment: Tax incentives can encourage investment in key sectors, such as infrastructure, research and development, or small businesses, promoting economic growth and stability.
iii. Improved Competitiveness: Tax policies can enhance the competitiveness of domestic industries, attracting foreign investment and promoting economic stability.

Conceptualizing Tax Reform

Tax reform is a fundamental fiscal policy strategy designed to enhance tax administration. Tax reform is a two-way process that necessitates changing the way taxes are collected and managed by government with a view to improving national income and gross domestic product (GDP), and providing economic and social benefits to the citizenry. For example, low tax revenue in most developing countries has been ascribed to inefficient tax administration, which may be a euphemism for corruption and/or distrust in tax administration and inefficient utilisation of tax revenue (Bird, 2022). The upshot is negative perception of taxpayers towards compliance. The suggestion therefore that inefficient tax administration with the resultant low tax revenue can be ameliorated through tax administration reforms underscores the need for this study

The notion of optimal tax structure is a normative concept rather than a positive realism. Virtually all countries experience some commonality of challenges in tax administration. It is doubtful if there is any country, developed or developing, that does not desire to continuously improve their fiscal system. In most countries, the challenges largely owe their origin to perceived inefficient tax administration, usually when a new Administration comes into power, and this includes assessment, collection and creating inclusiveness (breadth and depth) of eligible taxpayers.

Developing countries typically face incremental challenges in evolving efficient tax management due to many factors which, in the main, redound to socioeconomic and demographic historicity. The aim of most tax reforms is to make revenue levels more progressive and sustainable, promote independence from natural resource revenues and foreign 'handouts' (in the case of developing countries), elevate the role of taxation in state-building and create a greater understanding of its impacts on growth and inequality. The foregoing consideration underscores the efficacy of tax reforms in national development and economic stability.

Current national and global economic conditions pose significant challenges for policymakers. Depending on their nature, the critical dimensions of the challenges may need to be isolated to occasion specific macroeconomic reforms. The intention of macroeconomic reforms is to leave the country in a much better and more resilient position to cope with the instability in both the national and the global economy and to continue to steer a course of economic stability. A tax administration reform is an implicit acknowledgement of the failure of extant tax system. The reform is thenceforth necessitated to remediate the defective, deficient and ineffective system. Tax reform is a conceptual fiscal policy strategy designed to enhance tax administration (Nwaorgu et al., 2023).

It is a fiscal structural framework devised to strengthen responsive and accountable public governance. In general, tax reforms are concerned about creating incentives and structures that prospectively address the following concentric issues: (i) introduce focused changes to the country‟s tax system; (ii) unlock tax-revenue collection in pursuit of high levels of macroeconomic growth and development; (iii) enhance tax-administration processes to enforce compliance and increase collections; (iv) improve taxpayer service and communications, and (v) guarantee transparency and accountability of the public sector by providing tools to tackle the challenges of fiscal prudence, fiscal stress, citizen accountability, and public integrity (Pereira, Hoekstra, and Queijo, 2022).

Put differently, a tax reform is the process of reviewing and changing the administration and collection of taxes by government with a view to boosting State revenue on the one hand, and providing greater and better socioeconomic benefits, on the other hand. These reform measures or initiatives have also been echoed by Pereira et al. (2021). Put differently, a tax reform is the process of reviewing and changing the administration and collection of taxes by government with a view to boosting State revenue on the one hand, and providing greater and better socioeconomic benefits, on the other hand.

The review of and changes in the tax administration involve a number of decision variables, including: (a) reducing the level of taxation for all taxable entities; (b) making the tax system more progressive or less progressive; (c) simplifying the tax system and making it more understandable, more friendly and more accountable; (d) plugging all known loopholes to reduce tax evasion and avoidance; and (e) allow for more efficient and fair tax collection mechanism to enhance government's capacity to finance public goods and services. These views have also been echoed by Rao (2021). A successful tax reform involves a number of steps, precisely because it is a major component or process of fiscal consolidation. First, having recognized that there is a problem with and in the country's fiscal system, it is important to dimensionalize the problem. This involves a clinical diagnosis of the problematic of the extant fiscal structure. This is followed by an assessment of the role of taxation as a macroeconomic tool (Islam, 2020).

Economic Stability

No single statistical measure is sufficiently analytic to summarize the complexity of the modern national economy. However, the knowledge of the dimensionality of a particular macroeconomic variable, GDP, has been historically significant. Most economic research and economic policy analyses use GDP as a powerful comprehensive summary of economic activity. In other words, the empirical foundations of economic stability are set in changes in the GDP over time as a unit of analysis. Economic stability refers to economic condition of a country that is devoid of wide fluctuations in key indices of economic performance, such as gross domestic product, unemployment or inflation. This understanding has been facilitated by research attention to the dimensionalities and measures necessary to explain changes in GPD over time and their implications for economic growth, development, employment and inflation.

Stable economies manifest modest growth in GDP and job creation while holding inflation to a minimum. Economic stability implies greater economic prosperity, powered by productivity growth alongside higher levels of employment. The productivity performance of the Nigerian economy has historically been weak and this has created a substantial productivity gap, castrated economic development, and weakened revenue generation. In this economic quagmire, it is more important than ever that reforms are introduced to close both the productivity and revenue gaps. A friendly tax reform is designed to attract more tax payers into the net, incentivize the informal sector to voluntarily enlist into the formal sector, create employment opportunity, and build a stronger economy and fairer society.

Objectives of Economic Stability

The central objective of economic stability is to maximize the rate of sustainable growth and maintain rising prosperity by creating and widening the gamut of economic and employment opportunity. The strategic elements of economic stability are: (i) maintaining macroeconomic stability, (ii) sustaining fiscal stability, (iii) safeguarding financial stability, (iv) addressing the productivity challenge, (v) increasing employment opportunity, (vi) delivering quality public services, and (vii) protecting the environment. For Nigeria, in particular, the ingredients of economic stability reside in macroeconomic policy of government, whose goals are fiscal policy stability and price or monetary stability.

Fiscal stability is concerned with maintaining a balance between government tax revenue and government expenditure such that there is no mismatch or gap between government borrowing and debt service costs. Where government borrowing exceeds a limit that makes future interest payments prohibitively burdensome on government treasury, not only is fiscal instability immediately invoked, but also macroeconomic goals are thrown into serious jeopardy. Over the years, Nigeria has been under the weight of fiscal instability, with government spending outpacing revenue year in, year out. The perennial fiscal deficits are due to the rising gap between government tax revenue and expenditure, and excessive or imprudent government borrowings which have generated growing and unsustainable debt service costs. Financial system stability is critical in sustaining seamless financial intermediation, absorption of system shocks, minimization of systematic risks other risks such as nonperforming loans that can potentially trigger financial crisis and threaten macroeconomic stability.

On the flipside of the economic stability coin is monetary stability, referring to a regime of stable price levels or a low level of inflation. Price stability is a significant objective of monetary policy whose target is to ensure that inflation is contained or that it is not high enough to interfere with the efficient operation of the economy or destabilize fiscal (and trade) policies. Inflation has a pervasive painful effect on the economy such that if allowed to spiral, or if expectations of high inflation are held, it becomes an uphill task to deflate. A prudent strategy of economic stability is aimed at creating a balance between the two policy levers that is, aligning fiscal and monetary policies so as to achieve some equilibrium. Macroeconomic policy objective is to stabilize the economy via a steady growth of GDP and productivity while keeping inflation in check**.**

Tax Reform in Other Countries

Major tax administration reforms have occurred in a number of developed countries, such as Canada, France, Germany, Japan, Spain, United Kingdom and USA, and developing countries, such as the Eastern European countries, Russia, China, and other economies in transition. In 2000, for example, Germany implemented a tax reform program that professionalized the tax administration system which resulted in a dramatic advancement in tax collection (OECD, 2009). Equally, the experience of Spain affirms the hypothesis that a more efficient tax administration leads to more revenue generation. Specifically, enforcement, prosecution and tax auditing in Spain yielded an increase in the number of taxpayers from 1.7 million in 1988 to 2.8 million in 1991 (Hogue, Hassel, Olsson, Sabbe, & Ott, 2000).

Economic reform in Asia, particularly in Southeast Asia, often involves a combination of approaches. Key areas include liberalizing trade and exchange rates, reducing tariffs and non-tariff barriers, and overhauling regulations in areas like business and governance. These reforms aim to boost economic growth and resilience, especially in the face of trade tensions. China for example has implemented significant economic reforms since the 1980s, leading to rapid economic growth and urbanization. Countries like the Philippines, Indonesia, and others have experienced substantial economic growth in recent years, often driven by investment and trade. Studies suggest that well-designed reforms can lead to significant increases in GDP, improve efficiency and productivity across various sectors and also help Asian countries become more competitive in the global marketplace.

The Nigeria' New Tax Reform Bill

Under the new model, 60% of VAT revenue will be allocated to the state where goods and services were consumed, 20% distributed based on population, and the remaining 20% equally shared among all states. This marks a departure from the current system, where revenue is distributed based on where companies remit taxes, often in states with a high concentration of corporate headquarters like Lagos and Rivers. While the new model aims to ensure fairness by emphasizing consumption patterns, it has drawn intense criticism, especially from northern state governors and stakeholders who feel disadvantaged.

The governors' main concern lies in the derivation-based model, which they argue unfairly shifts a larger share of the revenue to southern states. This approach could exacerbate existing economic disparities and disrupt Nigeria's delicate balance of fiscal federalism. However, this resistance also discloses a deeper issue: the over-reliance of certain states on federal allocations instead of actively developing their internal revenue-generating capacities.

The proposed reforms are not without merit. For instance, exempting individuals earning less than ₦800,000 annually from income tax and small businesses with turnovers below ₦50 million from corporate tax offers much needed relief. These measures could strengthen economic activity by reducing the financial burden on vulnerable groups, ease the living status of working-class citizens, and enable small enterprises to reinvest in growth. Moreover, the introduction of taxes on digital assets modernizes Nigeria's tax structure, aligning it with global standards and addressing the rapidly expanding digital economy.

Nonetheless, the reform's success hinges on addressing regional concerns. While northern states grapple with legitimate challenges, including weak industrial bases and security issues, the solution lies in fostering economic self-reliance. States should be allowed to leverage their unique resources, such as agriculture in the North, to develop thriving local economies. The new VAT model offers an opportunity for states to innovate and focus on improving their internally generated revenue (IGR) through investments in infrastructure, education, and business-friendly policies.

The broader implication of the tax reform is the potential to redefine governance in Nigeria. By decentralizing tax administration to empower states and local governments, tax reform could encourage a shift toward more accountable and responsive leadership. While this transition will not be easy, it is a necessary step to reduce the country's over-reliance on oil revenues and promote sustainable economic development.

The outcome of this reform process ultimately depends on transparent implementation and meaningful dialogue among stakeholders, the governors and the president. By encouraging fiscal autonomy, Nigeria can take a significant step to achieve sustainable growth and economic development. President Tinubu's Tax Reform Bill represents a pivotal moment for Nigeria. It offers an opportunity to create a tax system that not only funds essential services but also promotes trust, inclusivity, and collaboration. For this vision to be realized, stakeholders must engage in a transparent dialogue and ensure tax reform is implemented fairly and effectively. The path forward requires determination and cooperation, but the potential rewards will result in a more equitable and prosperous Nigeria.

This reform has four different bills which are The Nigeria Tax Bill 2024, Nigeria Tax Administration Bill, Nigeria Revenue Service Bill, and Joint Revenue Board Establishment Bill. These bills seek to unify all tax laws making it easier for taxpayers to access and understand their duties and how to discharge said duties effectively. This reform takes into cognizance the economic hardship leading to the wind down of small-scale businesses, declaration of bankruptcy and reduced standard of living. Individually, these bills make provision on vital matters that are bound to promote economic growth and stability.

The Nigerian new tax reform bill seeks to repeal certain existing taxation laws, unify the legal framework governing taxation, and establish the Nigerian Tax Act to regulate the taxation of income, transactions, and instruments, along with addressing related matters. The objective of this act is to provide a unified fiscal legislation governing taxation in Nigeria and it applies throughout Nigeria to any person required to comply with any provision of the tax laws whether personally or on behalf of another person. This bill has provision for taxation of income of persons such as residents, non-residents, imposition of income, profits or gains, it discusses rates of tax, development Levy, specialized trade for insurance trade, mining operations, lottery and gaming trade, and the likes. Chapter eight of the bill provides for tax incentives such as income tax exemptions, exemption from stamp duties, and exemption from value added tax.

Nigeria's overdependence on oil revenue makes her a good candidate for tax administration reforms. The urgency of modernizing Nigeria's tax administration (and other fiscal) systems is premised on the realization that the country is rated one of the lowest Tax/GDP ratios in the world. This much was loudly echoed by Nigeria's former Minister of Finance, Kemi Adeosun, at the 2017 Spring Meetings of the IMF-World Bank in Washington DC, USA. Fielding questions on the side-lines of the said meetings, the Minister viewed the situation as unacceptable, stressing that the government was intent on achieving the objective of increasing non-oil revenue by encouraging companies and individuals to pay taxes which will help grow the country's GDP, improve its revenue to debt ratio and enhance its ability to fund budgeted projects and get the economy back on track.

With an unacceptably low level of non-oil revenue, driven chiefly by tax administration failure impelling low collection of tax revenue, the ex-Minister acknowledged that the country must do something fundamental about its revenue improvement. Tax administration reform offers advantages. First, in relation to monolithic or resource-dependent economies, such as Nigeria, tax reform responds to the country's economic diversification strategy, thus widening the government's revenue base. Second, tax reform is fundamental to driving greater competitiveness for businesses through a more efficient capital allocation that results from the diminution or mitigation of fraud, corruption and transactional distortions that hitherto characterized and informed the reform in the first place.

Challenges of the New Tax Reform Bill

The Tinubu new tax reform bill in Nigeria faces several challenges, including:

i. **Resistance from Northern Governors**: The proposed Value Added Tax (VAT) revenue sharing formula has sparked opposition, particularly from the northern states governors who fell disadvantaged by the derivation based model. They argue that this approach could exacerbate existing economic disparities between regions.

ii. **Macroeconomic Instability:** Critics warns that the proposed tax reforms coukd lead to increased inflation, reduced consumer spending, and economic instability. For instance, a 66.7% increase in VAT within 13 months could accelerate demand destruction and perpetuate poverty.

iii. **Implementation Challenge**: Effective implementation will require strong institutional capacity, transparency, and cooperation among stakeholders. Concerns have been raised about the potential for private interests to influence tax administration and the risk of corruption.

iv. **Equity and Fairness:** The tax reform's focus on VAT, a regressive tax, could disproportionately affect low-income earners. Additionally, the blanket exemptions granted for certain goods and services may not necessarily benefit all Nigerians, particularly those in states with limited economic activity.

v. **Fiscal Federalism:** The reform raises questions about Nigeria's fiscal federalism, with some arguing that states should have more control over revenue generation and taxation. This could promote more accountable and responsive leadership.

vi. **Low Tax-to-GDP Ratio:** Nigeria's current tax-to-GDP ratio is relatively low, and the reform aims to increase this ratio. However, some argue that this objective may not be suitable for Nigeria's economic situation.

vii. **Potential Impact on Small Businesses: While** exempting small businesses with turnovers below ₦50 million from corporate tax may provide relief, the overall impact of the reform on small businesses and the informal sector remains uncertain.

Overall, the success of the Tinubu’s Tax Reform Bill depends on addressing these challenges through transparent implementation, meaningful dialogue among stakeholders, and a focus on promoting economic development and fiscal responsibility.

Solution to the Challenges of New Tax Reform

To make President Tinubu's Tax Reform Bill more effective, here are some of the ways forward thus:

i. Engage in meaningful dialogue with stakeholders, particularly northern state governors, to address concerns about the proposed Value-Added Tax (VAT) revenue-sharing formula. This could involve revising the formula to better account for regional economic disparities.
ii. Encourage states to develop their internal revenue-generating capacities by leveraging unique resources, such as agriculture in the North. This can be achieved through investments in infrastructure, education, and business-friendly policies.
iii. Ensure transparent implementation and accountability in tax administration to build trust among stakeholders and promote fiscal responsibility.
iv. Empower states and local governments to take charge of tax collection and administration, promoting accountable and responsive leadership.
v. Regularly assess the impact of the tax reform on the economy, making adjustments as needed to ensure the reform achieves its objectives.
vi. Continue to provide relief to small businesses and low-income earners through exemptions and reduced tax rates, such as exempting individuals earning less than ₦800,000 annually from income tax and small businesses with turnovers below ₦50 million from corporate tax.
vii. Continue to modernize Nigeria's tax structure by introducing taxes on digital assets, aligning with global standards and addressing the rapidly expanding digital economy.By addressing these areas, the Tax Reform Bill can promote sustainable economic development, fiscal responsibility, and a more equitable tax system.

Conclusion

Preident Tinubu's tax reform bills aim to overhaul Nigeria's tax collection and administration systems, promoting a more equitable and efficient taxation model. the Tax Reform Bill 2024 could be the much-needed turning point for Nigeria's struggling tax system. By simplifying and modernizing our outdated laws, this bill offers a chance to create a fairer system that works for everyone from small business owners trying to stay afloat to ordinary Nigerians striving to make ends meet. If carried out with genuine intent and care, it could boost the economy, increase public confidence in the system, and make paying taxes less of a burden and more of a contribution to our collective growth. The key, however, lies in how well it's enforced and whether the government stays true to its promise of making life better for all Nigerians.

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