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The Incidence and Efficiency of Value Added Tax and its Legal Implication in Nigeria

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Abstract:

The imposition of tax towards revenue generation for the development of a nation takes place globally, but the concern is about who the burden of payment falls on. In spite of the high burden of Value Added Tax (VAT) on consumer, if properly administered in the nation, its contribution will tremendously help to increase revenue generated that will be use to improve the performance of the economy. This study examined the legal and administrative framework, the incidence, and the efficiency of Value Added Tax in Nigeria. The study relied on secondary sources of data and employed qualitative approach for the analysis. The study revealed that Nigeria has been able to achieve its purpose by greatly increasing its revenue from Value added tax. The findings also revealed that incidence of value added tax fall on the final consumer who pay the price of goods and services consumed. However, the findings revealed that the tax has not helped the country to achieve its purpose of efficiency in supporting the realisation of sustainable development. The study therefore recommended how the impact of Value Added Tax can be manifested to encourage the people especially through increase of government expenditure on health care and infrastructural facilities.

Keywords: Efficiency, Incidence, Revenue, Value Added Tax

1.0 INTRODUCTION

The growing need to generate sustainable revenue from local resources has remained a great challenge to developing economies including Nigeria. For those nations that depend on the production and exportation of petroleum as the major source of their revenue, this pressing need is affected by incessant decline and fluctuations in the prices of crude oil in the international market (Siyaka,2024). In the recent times, most countries of the world, including developed and developing nations are targeting at reducing their rising budget deficit via internally generated revenue. However, in spite of the gains from the use of broad-based Value Added Tax globally, its adoption by developed countries including Australia, Canada and United States has been rather sluggish (John, 2017). The argument of the critics of value-added tax is that VAT is a regressive tax which, apart from increasing burdens on businesses, places an increased economic burden on the lower-income taxpayers who are already paying personal income tax (Kumar, 2020). According to Obi and Akpan (2023), VAT provides a major source of revenue for the government as evidence from literature showed that many developing countries that have implemented VAT generate huge revenue from it. Ironically, the governments of these countries continue to complain of inadequate fund to carry out their statutory responsibilities to their citizens. Poor infrastructural facilities, high unemployment rate, poverty, poor standards of livings are the common features in these countries, combined with sophisticated crimes and other social vices.

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In spite of the burden of taxation and its challenges, the importance of taxation in national development cannot be overemphasised. Beside serving as a means of generating revenue to the government for the purpose of development projects, it is also used by the government to achieve both fiscal and macroeconomic objectives of promoting price stability and economic growth particularly in countries like Nigeria. However, poor attitude of Nigerians towards taxation indicated that many people would choose to avoid tax whenever they have the opportunity because they could not felt the impact of tax payment compared to people of other countries. Due to these tax evasion and avoidance habit among Nigerians, the economy keeps losing large revenue from tax evasion. This loss of revenue negatively affects the funding for infrastructures and other developmental projects in Nigeria (Azzimonti et al.2009; Adeniran, 2020).

However, taxation as a source of generating revenue has both positive and negative effects on the performance of an economy as taxes affects both individuals and businesses. Thus, increased taxes help the government to generate revenue to fund infrastructures that stimulate economic productivity. On the other side, increased taxes discourage business activities and, consequently lowers the rate of economic performance. The persistent debate among scholars in taxation and economics as well as the general public is the concern about the value added tax (VAT) being inflationary and who the incidence or burden of payments eventually fall on.

Therefore, the aim of this study is to examine the effectiveness of legal framework governing the imposition of value added tax, the incidence and efficiency of value added tax in Nigeria.

This section provides the introduction of the study. Section two presents the review of related study in the literature; section three explains the method used for this study. Section four contains the discussion of findings, while section five provides the conclusion and recommendations.

2.0 LITERATURE REVIEW

This section provides the conceptual, theoretical and empirical review of related studies.

Value Added Tax is new in the world. It was adopted in United Kingdom in 1973 and was introduced to Nigeria through the Value Added Tax Act in 1993. It is explained to be an amount of value that an organization contributes to goods or services whereby it adds its factors of production. This is addition of land labour capital and entrepreneurial skill.

Characteristics

1. It is consumption or expenditure tax;
2. It is an indirect tax since the consumer paying does not know that it is paying and it is paid with the price for the goods or service
3. The tax is multi- stage
4. The incidence of the tax goes to the consumer who is in the final stage

Objectives of VAT

Its objectives include the following:

- (i) It is targeted towards reduction of Nigeria's extreme dependence on oil income
 - (ii) For direction of tax towards consumption other than income
 - (iii) Provision of incentive for export promotion
 - (iv) For an approach that is progressive whereby luxury goods are targeted and essential goods and services mostly consumed by low income earners are spared
 - (v) For administrative feasibility
- (Agbonika, 2012)



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Legal Framework

The law governing operation of Value Added Tax in Nigeria is the Nigeria Income Tax Act, 2025, Cap 2 Laws of Federal Republic of Nigeria. The law repealed the Value Added Tax Act Cap VI Laws of Federal Republic of Nigeria

The Tax Act was signed into law on June 26 2025. It has provided new provisions into Nigeria legal system. The reform created new enactments by the National Assembly:

- (1) The Nigeria Tax Act;
- (2) The Nigeria Tax Administration Act;
- (3) The Nigeria Revenue Service (establishment) Act (NRSA); and
- (4) The Joint Revenue Board (Establishment) Act.

The reform introduced by the new Act repealed more than 12 old laws on Nigeria Tax regime.

Section 148 of the Value added Tax provides that 7.5% which is old rate shall be paid by the payers as VAT. The Nigeria Tax Act provides that sections 144 to 157 shall govern the management, registration and reporting the rules of VAT. Section 144 provides authority on what VAT should be imposed in Nigeria. It provides that it is applicable to all supply of goods and services except what is expressly exempted. This enlarges what is taxable through the value added Tax and extends it to digital economy. Section 151(1) of the Act provides that A non-resident supplying goods and services to Nigeria is to register and deduct Vat on its supply and reflects same in its invoice. This has been rated as most important aspect of the newly introduced provisions. It includes Companies such as Amazon and Netflix. It also includes cloud devices such as social media platforms that are advertising such as Instagram, Facebook, etc.

Cryptocurrency and digital Assets are also included. Digital assets shall be taxed when being disposed. Likewise, Banking and Fintech fees are to be paid services such as fees charged by banks. They are to pay for bill payment and other transactions. (Eko Solicitors, 2026) Banks are to pay

Goods Rated to Pay 0% VAT

Section 187 made reference to paragraph 2 of the Thirteenth schedule of the Act and provides that 0% are charged on supply of some items: They are:

- (i) Food items that are of basic needs
- (ii) Pharmaceutical products and products for medication. Herbal products are included in this category;
- (iii) Books and educational products and materials;
- (iv) Fertilizers;
- (v) Agricultural Chemicals that are locally produced
- (vi) Veterinary medicine that are locally produced;
- (vii) Feeds meant for animals that are locally produced
- (viii) Live cattle, sheep, goats and poultry products
- (ix) Seeds and seedlings for agriculture
- (x) Electricity generated by companies in charge of it

The 1999 Constitution as amended

The constitution in Section (1)(3) empowers the National Assembly on matters in the Exclusive legislative in Part I of the second schedule. Value added Tax was not expressly listed on what was stated in the second schedule which was challenged in *Attorney General of River State v Federal Inland Revenue Service & Attorney General of the Federation* that the Federal Government cannot



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enact VAT law and collect it. The execution of the decision needs interpretation of the Supreme Court.

Conceptual Review

According to Adekambi et al. (2022), a tax is the statutory payment made to the government by individuals and private organisations. It is a statutory payment which the government usually levies on the earnings, income, assets and profits of private individuals, organisations, and businesses. Taxation is used to promote income redistribution, economic stability and resource allocation. It also provides the major source of revenue of the government to fund expenditure and infrastructure for enhancing economic performance.

The Concept of Value Added Tax (VAT)

The concepts of Value Added in the field of taxation describes output of individuals' effort utilised in the processing inputs or economic resources into the production of goods and services in the economy. Therefore, value added tax is the statutory payment levied on the value added of a given input in the process of producing a particular good or service.

Value Added Tax (VAT) is a tax indirectly levied on goods and services purchased, it is usually charged at each stage of production at the rate of the value added by the producer (Obi & Akpan, 2023).

In Nigeria, VAT is a component of fiscal policy that applies to goods and services consumed which is designed to be paid by the final consumer (FGN, 2017).

The tax rate of VAT (Value-Added Tax) charged on the goods and services are usually set by a country's tax legislation. For instance, in Nigeria, the VAT rate is currently charges at 7.5% across specified consumer goods (Federal Inland Revenue Service, 2021). The recent increase in the VAT rate from 5% to 7.5% is to significantly increase government generated revenue to fund infrastructure and the provision of essential public services. The production of any good or services passes through several stages to meet the utility of the final consumer. In the process of production, value is added by an agent through an effort and the individual adding the value required a reward and the consumer is expected to pay for the reward of the value added at each stage. Tax is therefore imposed on the value added at each stage of production at a specified rate to serve as the consumers' contribution to fund public infrastructure (Obeng & Jong, 2018). The tax imposed at a given stage (input VAT) in the process of production or distribution is non-transferable or constitute part of the cost of production to be incurred in another stage of production.

Theoretical Review

Benefit Received Theory

This Benefits Received Theory (BRT) asserts that the government should levy tax on individuals on the basis of the benefits individuals receive from public goods and services provided by the government (Musgrave, 1959). The theory argued that there should be a positive relationship between the taxes paid by the individuals and the benefits gained from the public infrastructure and essential public services including healthcare, and security. It presumes that those individuals who received higher benefit from the public services should pay more and bear a larger portion of the tax burden and that the amount of tax to be paid should reflect the monetary value of the benefits enjoyed by individuals to ensure a fair tax system.

The theory proceed with the assumption that there should be a basic exchange relationship between the government and tax-payers. The government provides certain essential goods and services to the tax-payers in the society and in turn the tax-payers contribute to the cost of the goods and services in accordance to the benefits they received from the use of public goods (Agboola, 2016).



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The basis of this argument is that taxes should be levied on the basis of benefits received from government provided goods and services.

On the other hand, the Neoclassical and Keynesian theories of taxation posit an indirect relationship between taxation and economic activities. According to Keynes, government must reduce tax on individuals to raise aggregate demand which in turn increase overall economic activities. He argued that decreasing the tax rate will transfer greater purchasing power to the individuals, allowing for increased consumers' spending on goods and services, savings and investment opportunities.

Moreover, the Ricardian theory argued that decrease in tax will increase government borrowing to finance balanced budget in the short-run. These points of view therefore, suggested that tax policy is not revenue neutral. Fiscal variables like taxation and government expenditure affect the output in the short-run but not the long-run economic growth

Incidence of Value Added Tax (VAT)

Tax incidence is usually about the effect of taxation on the prices of goods and services paid by consumers and the amount of profits. The incidence of VAT usually falls on the final consumer. It is part of the consumers' income paid on goods and not a part of the profit of the business enterprise. A study conducted by Gaarder (2016) on the economy of Norway analyse the direct implication of the tax policy changes on the prices of food items as well as the cross-price effects on other goods and found that the type of taxes levied on food are completely shifted to the price paid by the consumer, whereas the price of other goods is not significantly affected. In another Study on the economy of France, Gaarder (2016) analyses two different VAT reforms which decreases the tax rates on new car sales and on the repair of housing services and the results suggested that a greater proportion of the tax burden is paid by consumers, especially in a competitively market for housing repair services. VAT is design to ensure production efficiency, reduce or remove existing tax considered to be ineffective in generation revenue for the state. Business transactions on factor inputs or intermediate goods are not the target of VAT but the final consumer. The desired production efficiency proves to be effective (Crawford, 2010). It provides an important reason for the introduction of the VAT to replace taxes that directly impact intermediate goods (Crawford, 2010). VAT is a chain of production tax and input credit which are usually unbroken, such that no net revenue is received from the taxation on intermediate goods sales so that the fundamental base of the tax is final consumer.

Value Added Tax and Inflation

There is argument that Value Added Tax (VAT) is inflationary in nature meaning that it will cause rise in prices in the distribution chain by affecting the cost of production and distribution. The immediate impact of VAT is that it increases the cost of production at each stage of production in the process of production. Mukhopadhyay (2005) posited that if the inflationary impact of VAT means a sustained increase in the inflation rate then the ultimate concern of VAT would be conceptually misunderstood. The introduction of tax including VAT can never, by itself, lead to a sustained increase in the price level. The increase in inflation rate can only be the result of expansionary monetary policy at all time. Mukhopadhyay (2005) relied on the data from International Monetary Fund on VAT introduction in some countries for the analysis. From the study VAT is never introduce to influence price directly, and therefore, it is difficult to empirically evaluate the effect of VAT on prices.



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3.0 METHODOLOGY

The study employed qualitative approach using systematic review of what other authors have written on Value Added Tax. The data were obtained from secondary sources including journals, text books, internets, reports from National Bureau of Statistics (NBS).

Value Added Tax and Government Revenue

The report from the National Bureau of Statistics revealed that, on the aggregate, Value Added Tax (VAT) for the first Quarter of 2024 was recorded at N1.43 trillion, revealing a significant growth rate of 19.21% on a quarter-on-quarter basis from N1.20 trillion in the last Quarter of 2023. The domestic payments of VAT recorded were N663.18 billion, while the Foreign VAT Payments recorded were N435.73 billion. The VAT on import was recorded at N332.01 billion in the first Quarter of 2024. On a quarter-on-quarter basis, accommodation and food service activities recorded the highest growth rate of VAT payment with 59.15%, followed by the activities of administrative and support with 47.79%. On the other hand, Activities of extraterritorial organizations and bodies had the lowest growth rate with –57.01%, followed by Human health and social work activities with –27.73%.

In terms of sectoral contributions, the top three largest shares in the first Quarter of 2024 were Manufacturing with 26.72%; Information and Communication with 17.42%; and Mining & Quarrying activities with 15.42%. Nevertheless, activities of households as employers, undifferentiated goods- and services producing activities of households for own use recorded the least share with 0.01%, followed by activities of extraterritorial organizations and bodies with 0.03% and water supply, sewerage, waste management, and remediation activities with 0.05%. However, on the annual basis, VAT collections in the first Quarter of 2024 increased by 101.65% from the first Quarter of 2023 (NBS, 2025).

Arguments for and Against VAT

According to Agboola et al. (2026) VAT has recorded positive trend in terms of revenue generation. The implementation of Value added tax have attained a meaningful achievement in Nigeria going by the positive trends of revenues generated since its establishment. There is no doubt that value added tax, the most innovation revenue source of the country and its introduction in Nigeria has been long over-due especially now that Nigeria is very verse to the payment of direct Tax. However, the bulk burden of value added tax is burn by the final consumer.

Value added tax represent a shift in taxation toward expenditure rather than income and thereby minimize the problem of tax evasion since it is a consumption tax. One pays only when he consumed. VAT remains a sustainable source of Nigeria revenue which help in sustaining determined economic development whether the income from oil dwindles as a result of decrease in the global price of oil. VAT is also collected on imported goods; thus, it does not place imported items at an advantage over locally manufactured goods.

4.0 CONCLUSION AND RECOMMENDATIONS

In spite of the major burden associated with VAT implementation bear by the consumers, it is evident that valve added tax remains the sustainable source of government revenue going by the positive trends of revenues generated since the recent reform. There is no doubt that value added tax, the most innovation revenue source of the country is on course especially now that Nigeria is struggling to recover from its debt crisis and place the economy on the path of sustainable development. However, in spite of the substantial amount generated from value added tax, its



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impact has not reflected on the economy as the country is facing infrastructural deficit. On this note, the study made the following recommendations:

- i. The Federal Government should come up with law for the establishment for infrastructural trust fund where a given percentage of income generated from VAT will be use to fix infrastructural deficit in Nigeria.
- ii. The government should also establish healthcare trust fund where a given percentage of income generated from VAT will be use to fund healthcare and make healthcare free to all Nigerians.
- iii. Since the Value Added Tax is paid by every consumer including payers of Personal Income Tax and the scope of collection has been expanded, the rate paid as Personal Income Tax especially by government workers should be reviewed downward.

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