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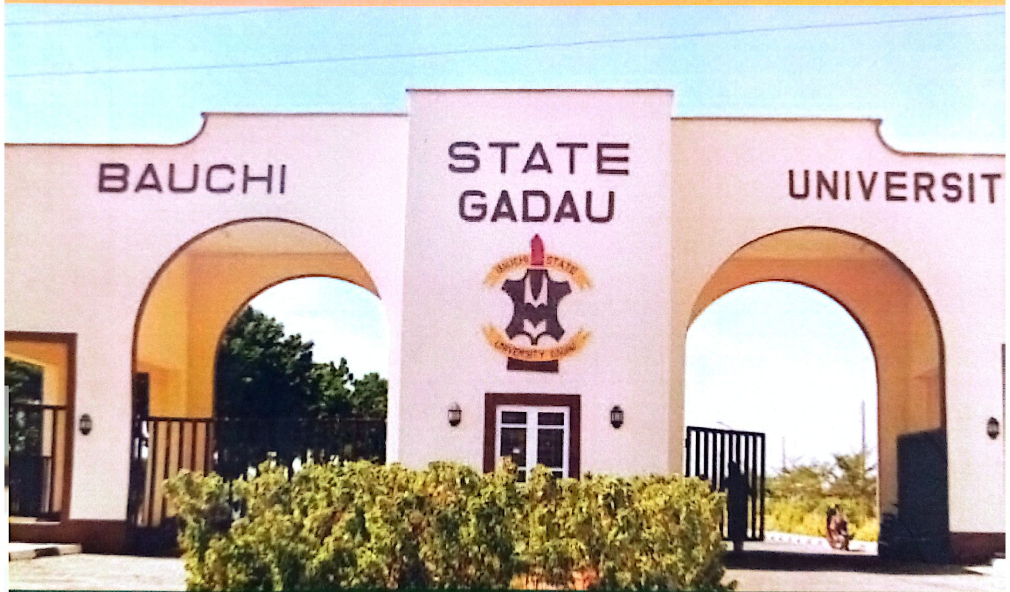

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NIGERIA'S TAX POLICIES AND SMALL FIRM PERFORMANCE: AN EMPIRICAL INVESTIGATION

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Abstract
Small enterprises performance has been hypothesized to depend on tax policies implemented by the government. However, the direction of this dependence has not been sufficiently established in empirical literature. Therefore, the effect of Nigeria tax policies on small firm performance was empirically investigated in the study *Secondary data obtained from relevant institutions were used for the investigation while regression analysis was used for analysis of data and hypothesis testing. Results indicated that company income tax and value added tax affect small enterprise performance negatively. It is recommended that tax authorities show concerns for the viability of small enterprises in the formulation and implementation of tax policies.*

Keywords: Tax policy, small enterprises, performance, Nigeria, empirical investigation

Introduction

The impact of taxation on any nation globally cannot be delineated as unimportant. It is an important means of income generation to the government at all levels enabling

them to achieve their macro-economic objectives (Omodero, 2020). For the Nigerian government to effectively discharge its responsibilities, adequate funding is sine qua non. It serves as impetus to the creation of a civilized, sound and powerful and economy. Tax payment serves as a barometer of such desire, though if not properly administered; it could be misconstrued by tax payers as a way of exploitation by the government (Ocheni & Gemade, 2015; Agu *et al.*, 2019).

It can be said that the health of a firm, regardless of its size, correlates with the nation's tax systems and this goes to say that a nation that has in place a conducive tax system will birth a thriving and financially viable firms which will enhance the economic performance of that nation. This therefore highlights the inter-dependence between In essence; businesses and tax policies greatly rely on each other for survival (Bismark et al., 2015).

Though Nigeria depends majorly on oil, her economy is also characterised by pockets of small enterprises covering the major economic activities within the country. These small enterprises are principally non-public enterprises and therefore face difficulties when dealing with the government and tax authorities and this can be said to be the case in developing countries (Ocheni, 2015).

Though the opinion that tax plays a major role in revenue earning and generation of fund for infrastructural and general economic development; what has not been given ample attention is the nexus between tax policies and firm sustainability and expansion. Small firms perennially face the challenges of high tax rates and multiple taxes which occupy prominent position in the hierarchy of the determinants of the success of small firms (PWC, 2020). these tax- related issues have eroded the meagre profit made by these small firms part of which normally should have been ploughed back into the business for growth and expansion and has resulted in increased cases of small enterprises winding-up in recent times (Ocheni & Gemade, 2015).

Despite this, literature has not contributed much in exploring the Nigeria tax policies and small firm performance (Evans *et al.*, 2016). Additionally, most of the literature on the subject matter have originated from western nations where the operations of small firms differ significantly from that obtainable Nigeria. In essence, questions on how Nigeria tax policies affect the performance of small firms in Nigeria remains largely unanswered. This study thus sought to look at the effect of Nigeria tax policies on small firm performance with focus on company income tax (CIT) and Value Added Tax (VAT) which are very relevant in the context of SMEs' operations in Nigeria (Inim et al., 2020).

Therefore, this research seeks to:

i. Examine the trend between tax policies and small firm growth in Nigeria
ii. Investigate how CIT affects performance of small firms in Nigeria.

iii. Evaluate the impact VAT has on small firm performance in Nigeria.

Two hypotheses were tested in a bid to provide empirical solutions to the problem. These hypotheses are as stated below:
H_{O1}: The performance of small firms in Nigeria is not significantly affected by CIT.
H_{O2}: The performance of small firms in Nigeria is not significantly affected by VAT.

Conceptual Literature Review
Bismark et al. (2015) define tax as 'the compulsory transfer of money from citizens of a country to the government as a source of revenue and cannot be avoided without attracting punishment'. In the same vein, the Institute of Chartered Accountants of Nigeria, (ICAN, 2018) views tax as 'an enforced contribution of money, enacted pursuant to legislative authority and assessed in accordance with some reasonable rule of apportionment on persons or property within tax jurisdiction'. This definition of tax would be adopted as it covers important aspects of the study area.

Ojochogwu & Ojeka (2012) opine that a good tax system should be geared towards wealth and job creation with an underlying objective of arresting wasteful expenditures while helping to shape and direct economic activities, stimulate economic activities and employing the revenue accruing to finance public welfare. Taxation affects business entities and the functioning of the economy and this effect may vary depending on the type of taxes as well as the tax rates applicable to certain entities. Therefore, a favourable tax system should be one that makes the private sector attractive to small entrepreneurs and reduces the incidences of tax avoidance and evasion (Ocheni & Gemade, 2015).

Taxes can be classified from the perspective of the tax subject, the tax base or the distribution of the tax burden (ICAN, 2018). When classifying tax based on tax Subject, there are two basic forms of tax; direct tax and indirect tax and the basis of breaking it into these two broad categories is largely due to the possibility of shifting tax burden from tax payer to some other persons (Abomaye, 2017). Types of direct tax include personal income tax (PIT), company (CIT) income tax, land and property tax and Capital gain tax while types of indirect tax includes Value Added Tax (VAT) import-export tax and excise duties.

PIT is levied on salaried employment, that is, it is based on a pay as you earn system and every taxpayer in Nigeria is liable to pay tax on the aggregate amount of his income whether derived from within or outside Nigeria (Abomaye, 2017). CIT is a tax usually administered by the Federal Inland Revenue Services (FIRS) and is levied on the accessible profit of companies at a minimum rate of 20% (ICAN, 2018). VAT is a consumption tax levied at each stage of the consumption chain and is borne by the final consumer at a flat rate of 7.5% of all invoiced amounts of taxable goods and

services (Finance Act, 2020; ICAN, 2018). It is usually charged on all supplies of goods and services in Nigeria with few exceptions.

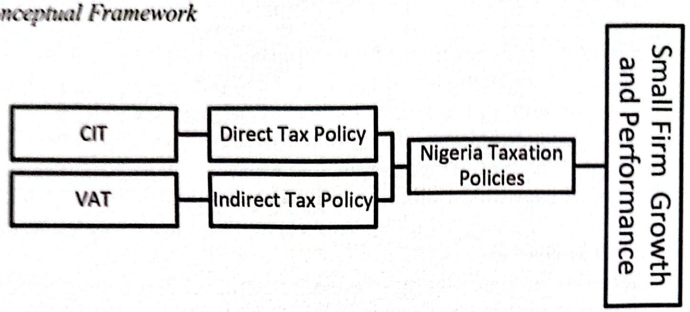
According to PWC (2020), MSMEs find both CIT and VAT difficult to comply with because of the lack of coordination between federal and state tax agencies, multiple of taxes and levies; absence of technology platform(s) to make tax payment easy as well as lack of fully functional tax refunds schemes at the state and federal level. Others included the absence of comprehensive tax payment schedule notification or calendar, and physical harassment/intimidation by local tax collectors.

Small Enterprises in Nigeria
Small scale enterprises are generally regarded as the engine of economic growth and equitable development in developing economies (Gale & Brown, 2013). They are labour intensive, capital saving and capable of helping create most of the one billion new jobs the world will need by the end of the century therefore being very key in ensuring poverty alleviation and employment generation in Nigeria (Mba & Cletus, 2014). Company Income Tax Act (CITA) defines small enterprises for the purpose of taxation as enterprises operating in sectors of the economy such as solid mineral mining, manufacturing, export trade and agriculture with a turnover of 1,000,000 naira and below (CITA, 2004).

Despite the catalytic role of small enterprises in the economic emancipation of countries, some of their major operational challenges in Nigeria Include: financial Problems, management problems, Inadequate Basic Infrastructure, Socio-Cultural Problem, Strategic Planning Problem, Location/Economic Problem, high operation cost, Poor Accounting System, Multiple taxation, lack of transparency, Unstable policy environment (Mba & Cletus, 2014; Bismark et al., 2015; Ocheni & Gemade, 2015; PWC, 2020).

Conceptual Framework for the Study
The conceptual framework of this study is illustrated in Figure 2.1. According to the conceptual framework, we seek to analyse the impact of selected taxation policies on the performance of small enterprises.

Figure 2.1
Conceptual Framework



Source: *Author's Initiative, 2022*

Theoretical Literature Review

The Laffer curve theory (LCT) (Holter et al., 2014; Kazman, 2014) developed by Professor Arthur Laffer and Ibn Khaldun theory of taxation are two prominent theories that have been used to explain the relationship between taxation and business performance. The proponent of LCT opines that the imposition of a high tax rate on businesses leave them with very little investible capital, a situation which often forces business owners to relocate their businesses to a more conducive business environment. The theory argues that low tax rate increases business income since businesses are afforded more money to invest which could result in expansion thus increased tax revenue.

Similarly, Ibn Khaldun Theory of Taxation developed by Ibn Khaldun in the fourteenth century strongly argues that for tax revenue to increase and tax collection to be efficient, government must adopt low tax rate. The theory stresses that though lower tax rates may have a direct relationship with tax revenue generated, it nonetheless relates inversely with business performance (Onakoya & Afintinni, 2016; Kipilimba, 2017).

The current study is underpinned by the LCT because of its success in correctly predicting the relationship between taxation and firm performance which is the subject matter of the study.

Empirical Literature Review

Inim et al. (2020) examined the impact that taxation has on SMEs growth in Nigeria from 2007-2019. Secondary data generated from the CBN's Statistical Bulletin and SMEDAN were used in the study. Co-integration and error correction modelling results show that CIT and VAT have significant inverse effect on SMEs growth.

Another empirical study conducted by Agot & Ugwuoke (2018) with a focus on the relationship between taxation and SMEs growth in Nigeria revealed that the two variables relate inversely with the former exerting a negative impact on the latter with resultant increases in running costs and stunted growth of SMEs. Evans *et al.* (2016) researched the impact taxation has on SMEs performance. The correlation and regression results obtained from the analysis of the primary data used in the study revealed the existence of an indirect effect of taxation on the performance of SMEs. Similarly, Ocheni & Gemade (2015) in their research examined how multiple taxation affect SME performance in Benue State and found SMEs' survival is hampered by multiple taxation. Bismark et al. (2015) in Ghana and Ojochogwu & Ojeka (2012) in their research conducted in Nigeria also affirmed the negative relationship between taxation and the growth of SMEs. However, the studies of Omodero (2020) and Agu et al. (2019) have indicated that the performance of SMEs could be enhanced by taxation as their results showed that the two variables are positively related.

Methodology

Quantitative research design was used in carrying out this research. Secondary data relating to the subject matter were sourced from different sources and authors. Data on CIT and VAT from period of 1993-2020 were obtained from CBN bulletin (CBN, 2017; 2020), FIRS (2018) and relevant literatures. The study made use of two variables namely taxation policies and small enterprise performance with taxation policies being the independent variable and small enterprise performance being the dependent variable. Small enterprise performance was measured in terms of its contribution to GDP from 1993-2020. Taxation policies further broken down to CIT and VAT for the purpose of the study was measured looking at their respective contribution to total tax revenue collected from the period 1993-2020.

For data analysis, the researcher employed the use of descriptive and inferential statistics. The inferential statistics used in this study was multiple regression models which helped in estimating the effect of taxation policies on small enterprise performance in Nigeria. Euler's (1987) model which has also been used by Orogbu et al. (2017) in another study was adopted and this model is expressed as;

$$Y = F(X_1, X_2, X_3, X_4 \ldots\ldots\ldots\ldots X_n) \quad \text{(I)}$$

Substituting the variables of the current study into this equation, we have the following function

$$SEP = f(CIT, VAT) \quad \text{(II)}$$

To estimate equation II, we introduced a stochastic error term was introduced in order to minimize the score variance. Therefore, we can rewrite equation II as;

$$SEP_t = \beta_0 + \beta_1 CIT_t + \beta_2 VATt + e_t \quad \text{(III)}$$

Where; SEP_t= Small Enterprise Performance; β_0= Intercept; β_1, β_2 = Coefficients of independent variables.
E_t = Error Term

Results/Summary/Discussion of Findings
Descriptive Statistics
Table 4.1 below showed the mean, maximum, minimum, skewness, kurtosis, and Jarque-berra statistics and standard deviations of all variables of Companies Income Tax (CIT), Value Added Tax (VAT) and Small Enterprise Performance (SEP).

Table 4.1
Descriptive Analysis Result

	CIT	SEP	VAT
Mean	419756.0	17480807	361018.9
Median	192600.0	7783255.	199850.0
Maximum	1377478.	57071500	1185063.
Minimum	9554.000	113320.0	0.000000
Std. Dev.	441952.4	19939651	351636.4
Skewness	0.727253	0.703867	0.690073
Kurtosis	2.098605	2.006721	2.227573
Jarque-Bera	3.172109	3.215677	2.709902
Probability	0.204732	0.200320	0.257960

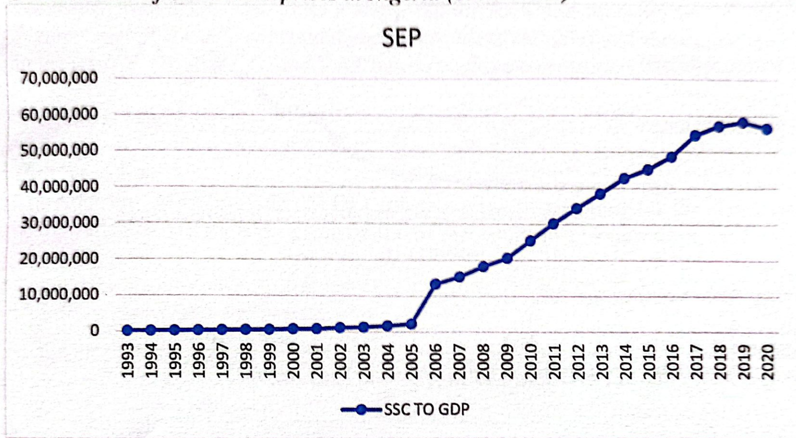
Source: *Author's Computation, 2022*

The table above presents the statistical description of the variables used in the study. Specifically, Company Income Tax (CIT) had a mean value of419,756.000; minimum value of9,554.000and maximum value of 1,377,478.Total CIT obtained in the 26-year period stood at 10,913,657 with 441,952.4 as standard deviation. VAT has a mean value of 361,018.9, minimum value of zero, maximum value of 1,185,063, total VAT obtained in the 26-year period stood at 9,386,491 and a standard deviation value of 351,636.4. Also, Small Enterprise Performance (SEP) measured via contribution to the GDP has a mean, minimum and maximum values of 17,480,807, 113,320 and 57,071,500 respectively, while total contribution to GDP over the period of 26 years stood at 454,500,980 and 19,939,651 standard deviation.

The table also shows that SEP, VAT and CIT values were normally distributed as shown by Jarque-Bera test in the sense that the probability value obtained are greater than the acceptable 0.05. The skewness and kurtosis test for the variables (SEP, VAT, CIT) showed that the data value contained in the three variables are not close that is, they are greater and less than the standard skewness value 0 and kurtosis value 3 respectively for a normal distribution.

Analysis of Trend
The pattern of the trend existed over the years with regards to the variables is depicted by Figure 4.1.

Figure 4.1
Growth Trend of Small Enterprises in Nigeria (1993 -2020)



Source: *Author's computation, 2022*

Figure 4.2
Growth Trend of Value Added Tax in Nigeria (1993-2020

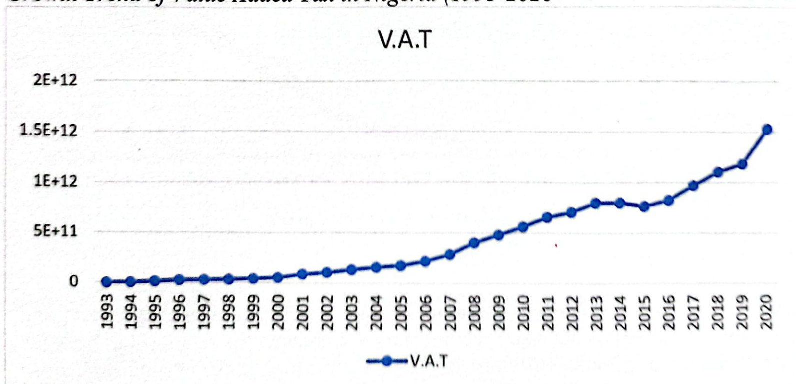
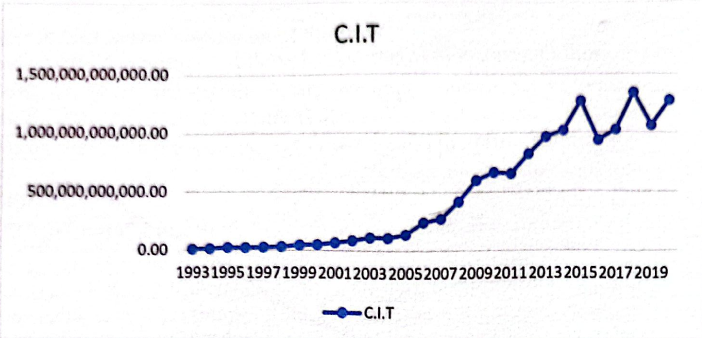


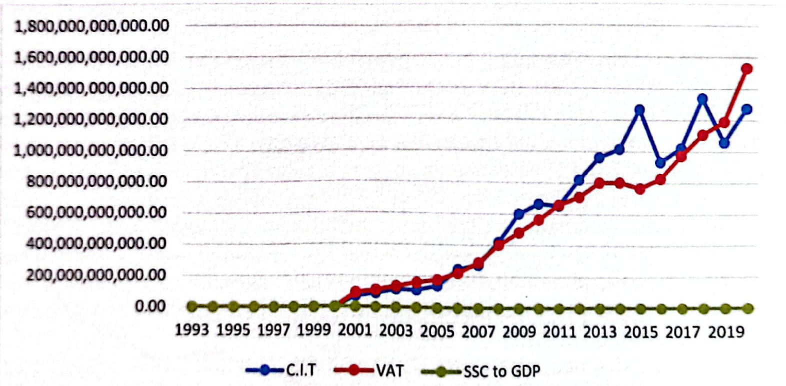
Figure **Source:** *Author's computation, 2022*

Figure 4.3
Growth Trend of Company Income Tax in Nigeria (1993-2020)



Source: *Authors computation, 2022*

Figure 4.4
Growth Trend of SEP, VAT and CIT in Nigeria (1993-2020)



Source: *Authors computation, 2022*

Figure 4.1, 4.2 and 4.3 showed the nature of individual trend of the dependent and independent variables of the study while figure 4.4 showed the relationship between the dependent and independent variable. Figure 4.1 which looks at small enterprise performance showed a consistent yet steady increase in small enterprise contribution to the GDP from the period of 1993-2005. The table however showed a sharp increase in Small enterprise contribution to the GDP in 2006 followed by an upward increase

in their contribution up to 2015. A drop was noticed beginning 2016 followed by increase from 2017-2020 and this could be attributed to the economic recession and recovery which led to the winding up of some small enterprises. Figure 4.2 and 4.3 which looks at CIT and VAT reveal similar trend nature in the sense that a consistent increase was noticed from 1993-2005 followed by a sharp increase though not too consistent from 2006-2014 then a sharp fall in 2016 and recovery in 2017-2018. Figure 4.4 combines the dependent and independent variables and shows that the rise in the growth trends of CIT and VAT has no positive correlation with SEP.

Inferential Statistics

Unit Root Test

The Augmented Dickey-Fuller (ADF) unit root test was used to check the stationarity of the variables. Below is the presentation of the results in a tabular form:

Table 4.2
Unit Root Test Result

Var.	Cri.val. at 5%	t-stat	Prob.	Comment
SEP	-2.991878	-3.406210	0.0209	Stationary at levels
CIT	-2.991878	-4.777771	0.0009	Stationary at levels
VAT	-2.998064	-6.822533	0.0000	Stationary at levels

Source: *Extracted from E-views 7 output (2022)*

The result contained in table 4.2 above shows that the stationary form for all variables were achieved at levels. Hence, the use of regression analysis for model estimation.

Test of Hypothesis

The result of the ordinary linear regression obtained using E-views 7 is as shown below in Table 4.3:

Table 4.3
Regression Result

Var	Coef.	Std. Err.	t-Stat	P-value
CONSTANT	-.737827	.581513	-1.268806	.2178
LCIT	-.601672	.293568	-2.049515	.0000
LVAT	-.481052	.312937	-1.537219	.1385
R^2	.979259		D-W stat	.776080
F-sta	519.3559			.000000

Source: *Extracted from E-views 7 output (2022)*

From Table 4.3 above, the R^2 value of .979 which indicates that the independent variables jointly explained 97.9% of the variation in the independent variable. The F-value of 519.3559 shows a good model fit since the prob. value is less than 0.05.

The independent variables are all negatively signed in conformity with a priori expectation which assumes a negative interaction between tax and small enterprise performance.

Ho1: The performance of small firms in Nigeria is not significantly affected by CIT.
The coefficient value of -0.601672 obtained from the result for CIT as shown in table 4.3, is said to be significant since the prob value is 0.000 at 0.05 level. This reveals that a percentage increase in CIT produces 60% decrease in small firm performance in Nigeria. Thus, the rejection of the null hypothesis in favour of the alternative hypothesis. This conforms with the findings Agot & Ugwuoke (2018) and Inim *et al.* (2020) which explained explained that the more the money collected from a tax payer, the less he has to invest and ultimately grow.

Ho2: The performance of small firms in Nigeria is not significantly affected by VAT.
The result obtained from the OLS demonstrates that VAT has a non-significant negative coefficient of -0.481052. This implies that a decrease of 48% is associated with every 1% increase in VAT on the average in Nigeria for the period under consideration. However, the study failed to reject the null hypothesis since the probability value of 0.1385 is greater than the 0.05 level of significant. This also conforms to the result obtained by Evans *et al.* (2016); Ocheni and Gemade (2015); and Bismark et al. (2015) that explained that VAT could have detrimental effect on small enterprises.

Conclusion and Recommendation
The relationship between Nigeria tax policies and the performance of small firms has been investigated in this study using secondary data covering the period 1993-2018 collected mainly from CBN statistical bulletins. From the findings made, it can be inferred that there has been an upward movement in small firm performance in Nigeria though there are occasional fluctuations. Furthermore, CIT has been found to affect adversely the performance of small firms in Nigeria. The implication of this is that CIT and VAT policies as they are being practiced presently stymie growth of small enterprises and hampers its contribution to economic growth in Nigeria.

In summary, current tax policies in Nigeria do not provide enough incentives for the growth and promotion of small firms. Therefore, to ensure that small firms flourish in Nigeria, tax policies that soothe healthy development of the sector and the long run positive performance of small firms which will invariably have positive effect on the growth of the economy as a whole should be initiated and implemented. It is recommended that policy makers should push for more stable and friendly tax policies in order to promote stability in the small enterprises sector.

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