Effect of Goods and Services Tax on Capital Expenditure in Nigeria

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Abstract: *This study is an empirical examination of the effect of goods and services tax on capital expenditure in Nigeria for the period 2005 - 2020. The specific objectives are to ascertain the effect of value added tax (VAT) on capital expenditure (CAPEX) and secondly to determine the effect of Customs and Excise Duties on capital expenditure (CAPEX) in Nigeria. The study is theoretically linked to Benefit Received Theory. The study was an ex-post-facto research which made use of secondary data obtained from the Central Bank Statistical Bulletin. The study employed descriptive statistics and graphical representation using E-Views 10 software to check for the trends, linearity or otherwise of the data. Regression model was applied in determining the extent of the effect exerted on capital expenditure (CAPEX) by value added tax (VAT) and custom and excise duties (CED). The result of the analysis revealed that the duo independent variables which are value added tax and custom duties had a significant and positive effect on capital expenditure. The implication of this finding is that the capital expenditure has been influenced significantly by value added tax and customs duties. The study concluded that a long-run relationship existed among VAT, CED and capital expenditure. It is therefore recommended that revenues generated from VAT and CED should be invested and allocated adequately in major domestic sectors of the economy of Nigeria so as to expand the revenue sources of the nation.*

KEYWORDS: VAT, CED, CAPEX, goods, service, expenditure, tax.

INTRODUCTION

Government all over the globe have deemed it fit to devise appropriate means of generating revenue to finance expenditure which continue to soar as a result of growth in population with its attendance demand for social, economic and infrastructural investment. This has prompted tax to become legally accepted all over the world as one of the most suitable means of generating revenue. Tax is a compulsory payment made by individuals and corporate bodies to the government for financing government expenditure or for general purpose of government aimed at improving the taxpayers welfare and in which both the taxpayer and the public at large benefit (Okwo, 2006).

A tax can also be defined as a means by which Government appropriate part of the public/private sectors income. It is now clear that taxes are now seen as compulsory extractions that involves personal obligations for common public purposes. In consonance with the above mentioned

responsibilities of the government, subjects or citizens has realized the need to contribute towards nations building through fulfilling their compulsory payment of tax. It has been highlighted that to device a means to these responsibility, there is need to impose the value added tax (VAT). A value-added tax (VAT), known in some countries as a goods and services tax (GST), is a type of tax that is assessed incrementally. It is levied on the price of a product or service at each stage of production, distribution, or sale to the end consumer. If the ultimate consumer is a business that collects and pays to the government VAT on its products or services, it can reclaim the tax paid. It is similar to, and is often compared with, a sales tax. VAT is an indirect tax because the person who ultimately bears the burden of the tax is not necessarily the same person as the one who pays the tax to the tax authorities (Onuiri, Faroun, Erhinyeme & Jegede, 2015).

Another means by which government generate revenue to enhance capital expenditure is through the custom and excise duties. This is an indirect tax paid to the government of Nigeria by producers of goods. Excise duty is the opposite of customs duty in that it applies to goods manufactured domestically in the country, while customs is levied on those coming from outside of the country. The customs and excise authorities assess and collect the customs and excise duties levied by the government as an important source of revenue. The customs and excise authorities make sure that the amount of certain imports does not exceed the quota or limit allowed to be imported within a specified period. Tax occupies a unique position because it is an important part of government policies (Osiegbu and Nnamdi, 2009). The ability of a government to generate revenue from this sector affects services offered by such a government. A means of improving internally generated revenue is through value added tax alongside with custom and excise duties.

In developing countries such as ours, citizens' apathy towards taxation is common, due to some factors, which are: lack of transparency and accountability by governments and their agencies, and, the presence of bureaucracy by various tiers of government, especially the revenue-generating agencies. The State as the provider of public goods and services owes the responsibility to impose tax. This obligation to provide these goods and services for the citizens compels government spending, and taxes are sure way to finance these, and a certain way to get citizens participate in their funding. Taxation is therefore seen as an inherent power of the state to secure the funds needed to meet its social obligations (Wilson et al, 2018). Apart from being an essential fiscal policy tool and one of the primary sources of public revenue across the world, Nwaorgu, Herbert, and Onyilo (2016) shows that the interactive effects of taxation play a pivotal role in the economy. There is a general lack of consensus among scholars on the contribution of tax revenue to the economic growth of nations. For instance, whereas Ariyo (1997) in his study on productivity of the Nigerian tax system documented a satisfactory level of productivity of the tax system before the oil boom, Festus and Samuel (2007) established that the role of tax revenue in promoting economic activities and growth is not felt in Nigeria. The two studies reflected that the oil boom has not improved the economic state of the country since before the boom, there was a level satisfactory and after the boom, the growth of economic activities deteriorated. It has not also enhance government expenditure hence the need for value added tax and custom/excise duties. Government expenditure no doubt is an essential instrument for a government to control the economy of a nation. In Nigeria, the federal government's expenditures are broadly divided into

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capital and recurrent expenditure. The recurrent expenditure consists of government expenditure on administration such as wages, salaries, interest on loans, maintenances. Whereas the capital expenditure is on projects like roads, airport, health, education, electricity generation, telecommunication, water etc. Capital expenditures are investments with multiplier effects on the economy in terms of public benefits. In most cases, government intervention has brought stability in income and employment in the economy (Udezo & Onuora, 2021). Therefore, based on this background, this current study is set to examine effect of Goods and Services Tax on Capital Expenditure in Nigeria.

The broad objective of the study is to ascertain the effect of goods and services tax on capital expenditure (CAPEX) in Nigeria. The specific objectives are to;

(i) Ascertain the effect of Value Added Tax (VAT) on capital expenditure (CAPEX) in Nigeria.

(ii) Determine the effect of Customs and Excise Duties on capital expenditure (CAPEX) in Nigeria.

The hypotheses stated in null form are denoted by (H_0):

Ho_1: Value Added Tax (VAT) does not have significant effect on capital expenditure (CAPEX) in Nigeria

Ho_2: Customs and Excise Duties have no significant influence on capital expenditure (CAPEX) in Nigeria.

REVIEW OF RELATED LITERATURE

Conceptual Review

Value Added Tax

Value Added Tax (VAT) is a replacement of the sales tax, which was earlier promulgated into existence through decree No.7 of 1986. The rationale behind replacing sales Tax with VAT was informed by a number of factors and considerations (Ogunbesan, 2015). Notable among these are: The base of the sales tax in Nigeria as operated under Decree No. 7 of 1986 was narrow. It covered only nine (9) categories of goods plus sales and services in registered hotels, motels and similar establishments. The narrow base of the tax negates the fundamental principle of consumption tax which by nature is expected to cut across all consumable goods and services expected. VAT base is broader and includes most professional services and banking transactions which are high profit-generating sectors.

Mbanefoh (2012) states that in the case of VAT it is neutral in this regard. Under VAT, a considerable part of the tax to be realized is from imported goods. This means that under this new indirect tax, locally manufactured goods will not be placed at a disadvantage relative to imports. Another reason was that VAT is a consumption tax and is based on the, general consumption behaviour of people; the expected high yield from it is boosting the revenue collected by governments with minimum resistance from the payers of the tax.

Omoh (2007) states that tax reforms are changes that are made in the Nigerian Tax system to increase the revenue base of the company. No matter the angle from which VAT is viewed, the purpose is to generate more revenue to the government. A critical examination of the current formula: Federal Government 15%; State Governments 50% and Local Government 35%, shows clearly that VAT was designed to favour development at the lower-tier level of government. The introduction of VAT in 1993 and its actual implementation in 1994 recorded a huge success in Nigeria (Eme & Johnson, 2012).

Customs and Excise Duties Tax

Osiegbu and Nnamdi, (2009) posited that custom and excise duty refers to taxes levied on imported or exported goods. The two types of customs duties collected under international trade are import and export duties. The duties are listed in the country's tariff schedule.Duties may be ad valorem or specific. An ad valorem duty is a fixed percentage of the value of the goods that are being imported e.g. 10% of value. A specific duty is a duty of a specific amount of money that does not vary with the price of the goods but with its weight, volume, surface, etc. The specific duty stipulates how many units of currency are to be levied per unit of quantity.

Okafor (2012) is of the view that an excise tax is any duty on manufactured goods which is levied at the moment of manufacture, rather than at sale. Excises are often associated with customs duties which are levied on pre-existing goods when they cross a designated border in a specific direction; customs are levied on goods which come into existence – as taxable items – at the border, while excise is levied on goods which came into existence inland.

Although sometimes referred to as a tax, excise is specifically a duty; tax is technically a levy on an individual or more accurately, the assessment of what that amount might be, while duty is a levy on particular goods (Omoh, 2007). Rohaya, Nur Syazwani and Nor'Azam (2010) state that an excise is considered an indirect tax, meaning that the producer or seller who pays the levy to the government is expected to try to recover their loss by raising the price paid by the eventual buyer of the goods. Madugba, Okpe, and Ogbonnaya (2016) defined indirect tax as tax paid by an individual and commercial entity that is involved in importation and exportation of goods and services. Custom duties are classified into export and import duties. While import duties are taxes levied on goods imported into a country from other countries, export duties are charged on goods sent out to other countries. The value of tax duties is based on Cost, Insurance and Freight (CIF) The Finance Act 2020 also impacts on the Customs and Excise Tariff Act, as section 21 (5th Schedule) of the Customs, Excise Tariff, etc. (Consolidation) Act 1995 was also amended. Under the amendment, goods imported into Nigeria have been added to those that must pay excise duty in the country.

Capital Expenditure

Capital expenditure or spending by government or public sector institutions has been growing steadily, and notwithstanding the expenditure are mainly part of the contributions from tax revenues like the value added tax, custom and excise duties etc. Government expenditure could be current, recurrent, and capital expenditures. Capital government expenditure refers to spending on

fixed assets such as roads, schools, hospitals, building, plant and machinery, the benefits of which are durable and lasting for several years while recurrent government expenditure refers to the expenses that government incurs for its maintenance, for the society and the economy as a whole (Uwaezuoke, Nweke & Ogar, 2018). Government expenditures have far a very high effect on the overall economic activities of any nation. Government expenditure on production depends on three factors; the ability to work, save and invest; the willingness to work, save and invest and the diversion of economic activities between different uses and localities (Musa & Asare, 2013).
Uwaezuoke, Nweke and Ogar (2018) explained further that government expenditure in the form of grants and subsidies to farmers, firms and industries is highly productive as it minimizes the cost of production which leads to a fall in prices. In contrast, expenditures on education and health have a direct welfare effect on society. Expenditure on education and health is seen as an investment in human capital improves skill formation and raises the ability to produce which has the effect of raising disposable income and in turn increases consumption, investment and the economy performance at large.

Theoretical Framework

This study is theoretically linked to "Benefit Received Theory", which was propounded by two economists from the Stockholm School, popularly known as Knut Wicksell (1896) and Erik Lindahl (1919). The benefits received rule argues that those who receive the greatest benefit from the government, either directly or indirectly, should pay the most taxes, in principle of fairness.
It is normally appropriate in appraising fiscal policy and assessing the efficiency of taxes. The benefit principle is a concept in the philosophy of taxation from public finance. It bases taxes to pay for public goods expenditures on a politically revealed willingness to pay for benefits received. The principle is sometimes likened to the function of prices in allocating private goods.

The benefit principle takes a market-oriented approach to taxation. The objective is to accurately determine the optimal amount of revenue that should be spent on public goods. The free-rider problem is the primary criticism given for limiting the scope of the benefit principle. When information about marginal benefits is available only from the individuals themselves, they tend to under report their valuation for a particular good; this gives rise to the preference revelation problem. Each individual can lower his tax cost by under reporting his benefits derived from the public good or service. One solution would be to implement a tax choice. If taxpayers had to pay taxes anyway but could choose where their taxes went (without the possibility of secret rebates or similar), then they would have no incentive to hide their exact preferences.

Empirical Review

Otu and Theophilus (2013) studied the effects of tax revenue on economic growth in Nigeria, applied time series data for the period spanning from 1970 to 2011. It adopted the Ordinary Least Square (OLS) regression technique and established that tax revenue has positive effect on economic growth in Nigeria. The result also showed that domestic investment, labour force, and foreign direct investment have positive and significant effect on economic growth in Nigeria.
Akwe (2014) studied the impact of oil Tax Revenue on Economic Growth from 1993 to 2012 in Nigeria. Secondary data were collected from the 2012 Statistical Bulletin of the Central Bank of

Nigeria (CBN). These data were analyzed using the Ordinary Least Squares Regression. Their result showed that there exists a positive impact of Non-oil Tax Revenue on economic Growth in Nigeria.

Inyiama and Ubesie (2016) examined the effect of value added tax, Custom and excise duties on Nigeria economic growth. They applied simple regression technique for the analysis of their hypotheses, while correlation analysis was used for the assessment of the relationship between the non-oil sources of revenue and Nigeria Domestic Product. The study showed that all the non-oil revenue affects Nigeria Gross Domestic Product. They concluded that revenue sources could be used to predict the value and status of the nation's Gross Domestic Product. Value Added Tax and Custom and Excise Duties are some of the major contributors to Nigeria Gross Domestic Product. Anyanwu (2014) investigated the effects of taxes on Nigeria's economic growth using the Ordinary Least Squares technique and Cochrane - Orcutt, and data set from 1981 to 1996. The study found out that personal income tax negatively and insignificantly affects economic growth. He concludes that both company income tax customs and excise duties have positive and significant relationship with Gross Domestic Product, while petroleum profits tax is positively but insignificantly related to economic growth.

Onaolapo, Aworemi, and Ajala (2013) examined the impact of value added tax on revenue generation in Nigeria. Secondary data was sourced from Central Bank of Nigeria statistical Bulleting (2010), Federal Inland Revenue Service Annual Reports and Chartered Institute of Taxation of Nigeria Journal. Data was analyzed with stepwise regression analysis. Findings showed that Value Added Tax has statistically significant effect on revenue generation in Nigeria. Ebi and Ayodele (2017) carried out a study on tax reforms and tax yield in Nigeria. The study adopted Error Correction Mechanism (ECM) technique in analyzing the data. The results revealed that all the tax components were inelastic, there was a general improvement in post-reformed tax elasticities, and tax reform further confirmed to improve tax revenues by positive and significant coefficients of the dummies.

Olaoye and Ayeni (2018) studied the effects of value added tax and custom duties on revenue generation in Nigeria (2000-2016). Autoregressive Distributed Lag (ARDL) and Granger causality tests were used as the estimation techniques. The study revealed that there was no long run relationship among value-added tax, customs duties and revenue generation. It was equally revealed that there is no causality among the variables. Egbunike, Emudainohwo and Gunardi (2018) carried out a study on tax revenue and economic growth in Nigeria and Ghana. The study adopted multiple regressions as tools of analysis and found out that there is positive impact of tax revenue on the gross domestic product of Nigeria and Ghana.

Nwofor & Gordon (2013) studied tax revenue and government expenditure. They explored how revenue generated from taxation affects Nigeria expenditure. Secondary data used for data collection hypotheses and hypotheses tested using Pearson moments collation coefficient. The study found out that the volume of expenditure incurred by the government can negatively affect total tax revenue, especially those when those expenditures are mainly a recurrent expenditure.

Ofoegbu, Akwu and Oliver, (2016) examined the effect of tax revenue on the economic development of Nigerian, and to ascertain whether there is any difference in using HDI and GDP in establishing the relationship. The approach adopted in this study was that of using annual time series data for the period 2005 - 2014 to estimate a linear model of tax revenue and human development index using ordinary least square (OLS) regression technique. Findings show a positively and significantly relationship between tax revenue and economic development. The result also reveals that measuring the effect of tax revenue on economic development using HDI gives lower relationship than measuring the relationship with GDP thus suggesting that using the gross domestic product (GDP) gives a painted picture of the relationship between tax revenue and economic development in Nigeria

Modebe, Regina, Okafor and Onwumere (2012) examined the impact of recurrent and capital expenditure on Nigerian economic growth by using three variables multiple regression model. The result emanating from this study revealed that while recurrent government expenditure had positive and non-significant impact on economic growth, capital expenditure had negative and non-significant impact on economic growth which emphasized the need for increase and encouragement of private sector investment.

METHODOLOGY

This study adopts an *ex post facto* research design which implies after the fact research. It provides an empirical and systematic solution to research problems, by using data which are already in existence. The study was carried out in Nigeria.
Data series were collected for customs and excise duties, value added tax and Capital Expenditure from the Central Bank Statistical Bulletin for the periods spanning from 2005 to 2020. The model is represented thus:

$CAPEX_t = \beta_0 + \beta_1 VAT_t + \beta_2 CED_t + \mathcal{E}_t$ ……………………...…………….. (1)

Where:
CAPEX = Capital Expenditure
VAT = Value Added Tax
CED= Customs and Excise Duties
β_0 = *Coefficient (constant) to be estimated*
t = *Current Period*
$\mathcal{E}$ = *Stochastic disturbance (error) term*

The effect of goods and services tax on capital expenditure in Nigeria is tested using the multiple regression analysis. The nature and significance for interpretation of the result for test of hypotheses is provided by EViews Statistical software. The decision rule for the test of hypothesis accepts significant coefficient when its p-value is equal or less than 0.05.

DISCUSSION OF FINDINGS

Descriptive Statistics of the Variables and Graphical Representations

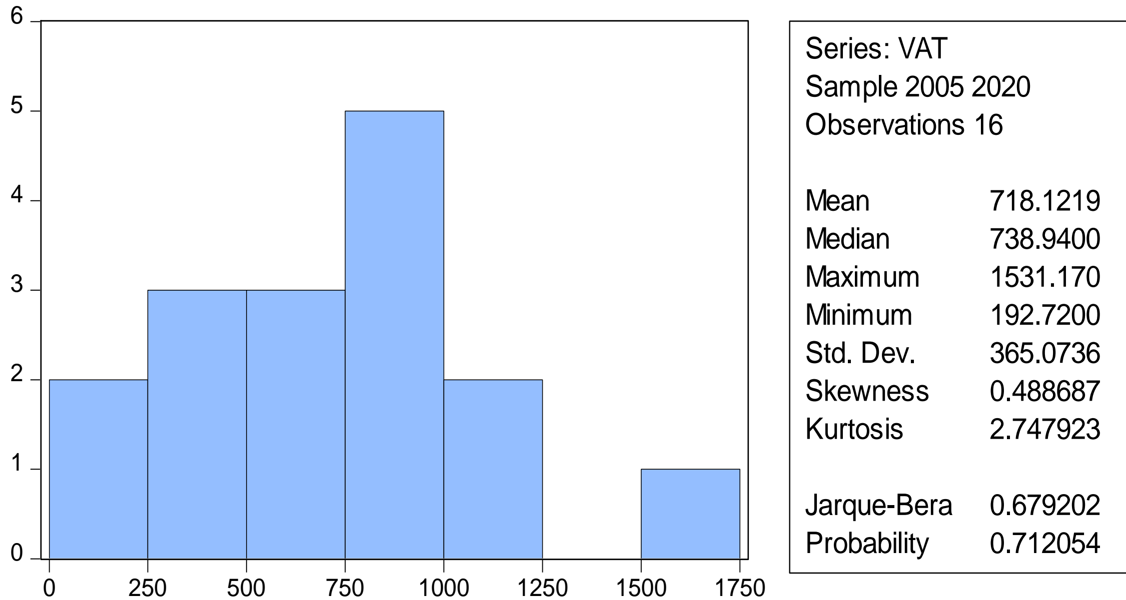

Figure 1: Representation of Value Added Tax
Source: *Eviews 10 Statistical Software*

The mean figure for value added tax is 718.1219 while the median is 728.9400. The standard deviation is 365.0736 while the insignificant Jarque-Bera Statistic of 0.712054 shows a normal distribution of the time series data. The value added tax graph shows some fluctuations resulting from unsteadiness in value added tax revenue indices over the sample period.

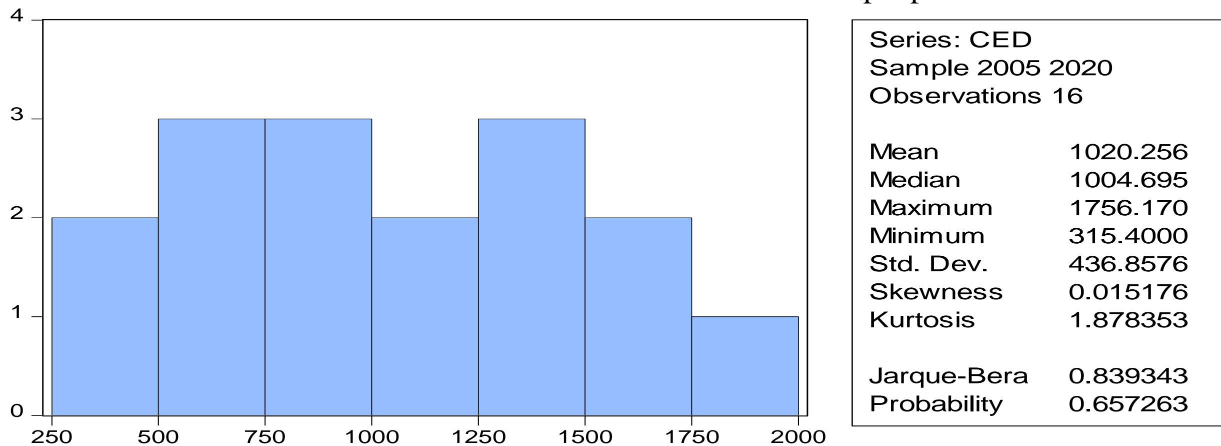

Figure 2: Representation of Customs and Excise Duties
Source: *Eviews 10 Statistical Software*

The mean value for customs and excise duties (CED) is 1020.256, while the median is 1004.695. The standard deviation is 436.8576 while the insignificant Jarque-Bera Statistic of 0.657263 shows a normal distribution of the time series data for CED. The graph above depicts some form of variations in revenue generated from CED which impacts on capital expenditure for the sampled periods.

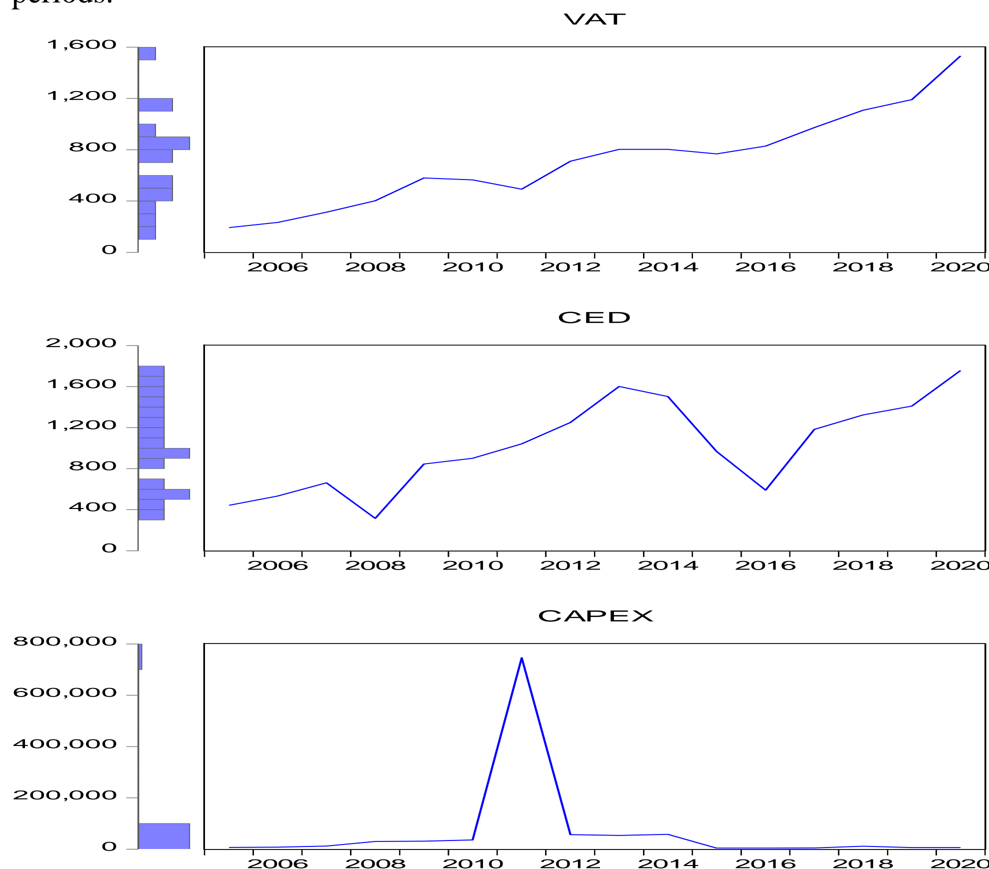

Figure 3: Composite representation of VAT, CED & CAPEX
Source: *Eviews 10 Statistical Software*

The connections between the above variables were elucidated in the analysis below.

Test of Hypothesis 1

Restatement of the Hypothesis in Null and Alternate forms:

Ho_1: Value Added Tax (VAT) does not have significant effect on capital expenditure (CAPEX) in Nigeria

Ha_1: Value Added Tax (VAT) have significant effect on capital expenditure (CAPEX) in Nigeria

Table 1: Regression Analysis Result

Dependent Variable: CAPEX
Method: Least Squares
Date: 08/30/22 Time: 12:50
Sample: 2005 2020
Included observations: 16

Variable	Coefficient	Std. Error	t-Statistic	Prob.
VAT	741.9646	99.46838	7.459301	0.0020
C	0.000356	0.000527	0.674409	0.5110

R-squared	0.8031465	Mean dependent var	718.1219
Adjusted R-squared	0.7037716	S.D. dependent var	365.0736
S.E. of regression	371.8944	Akaike info criterion	14.79157
Sum squared resid	1936276.	Schwarz criterion	14.88814
Log likelihood	116.3325	Hannan-Quinn criter.	14.79651
F-statistic	3.454827	Durbin-Watson stat	0.134372
Prob(F-statistic)	0.011035		

Source: *Eviews 10 Statistical Software*

Table 1 revealed the regression analysis of the effect of goods and services tax on capital expenditure in Nigeria. The table shows that value added tax (VAT) has a positive and significant effect on capital expenditure (CAPEX). The decision rule is that the null hypothesis will always be rejected when the t-statistic is greater than 2. In this case, the t-statistic is 7.459301 which is greater than 2. Hence, the null hypothesis is rejected and the alternate accepted. The adjusted R-Squared is 0.7037716. This means that about 70% of the variations in capital expenditure could be explained by value added tax while about 30% of the variations in CAPEX could be attributable to other factors not considered in this contemporary study. The F-statistic of 3.454827 shows a significant probability value of 0.011035 which means that the effect of goods and services tax on capital expenditure in Nigeria may not have occurred by chance. This shows that the interactions between VAT and CAPEX are sustainable both at the short and long run in Nigeria.

Test of Hypothesis 2

Ho_2: Customs and Excise Duties have no significant influence on capital expenditure (CAPEX) in Nigeria.

Ha_2: Customs and Excise Duties have significant influence on capital expenditure (CAPEX) in Nigeria.

Table 2: Regression Analysis Result

Dependent Variable: CAPEX
Method: Least Squares
Date: 08/30/22 Time: 12:59
Sample: 2005 2020
Included observations: 16

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CED	1.001311	0.001687	593.4288	0.0101
C	3350.817	315.9765	10.60464	0.0000

R-squared	0.899960	Mean dependent var	67060.60
Adjusted R-squared	0.799957	S.D. dependent var	182141.7
S.E. of regression	1188.715	Akaike info criterion	17.11560
Sum squared resid	19782615	Schwarz criterion	17.21218
Log likelihood	134.9248	Hannan-Quinn criter.	17.12055
F-statistic	352157.7	Durbin-Watson stat	0.415371
Prob(F-statistic)	0.002100		

Source: *Eviews 10 Statistical Software*

Table 2 regression analysis portrays that customs and excise duties influences capital expenditure. The extent of the influence shows that customs and excise duties (CED) has positive and significant effect on capital expenditure (CAPEX). The decision rule is that the null hypothesis will always be rejected when the p-value is less that 0.05 level of significance. In this case, the p-value is 0.0101 which is less than 0.05. Hence, the null hypothesis is rejected and the alternate accepted. The adjusted R-Squared is 0.799957. This means that about 80% of the variations in capital expenditure could be explained by customs and excise duties while about 20% of the variations in CAPEX could be attributable to other factors not considered in this article. The F-statistic of 352157.7 shows a significant probability value of 0.002100 which means that the effect of goods and services tax on capital expenditure in Nigeria may not have occurred by chance. This implies that the short run effects will be sustainable in the long run.

Summary

The analysis of data depicts that value added tax has a positive and significant effect on capital expenditure in Nigeria due to the fact that its t-statistics of 7.459301 is greater than 2.0 and its probability value being 0.0020 was less than 0.05. In similar trend, customs and excise duties exerts a positive and significant effect on capital expenditure in Nigeria as the t-statistics of 593.4288 was greater than 2.0 while its probability value of 0.0101 was less than 0.05.

Having examined empirically the effect of goods and services on capital expenditure in Nigeria, it can be concluded, based on the results and discussion of findings that there existed long-run

relationship among VAT, CED and capital expenditure in Nigeria. It is therefore recommended that revenues generated from VAT and CED should be invested and allocated adequately in major domestic sectors of the economy so as to expand the revenue sources of the nation.

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