

A COMMENTARY ON THE VALUE ADDED TAX DIRECT INITIATIVE BY THE FEDERAL INLAND REVENUE SERVICE

A 2021 report by the International Survey on Revenue Administration reveals that only about 16.7% of the Nigerian economically active population pay tax¹. The informal sector is estimated at 65% of the gross domestic product (GDP)² and according to SMB Intelligence, the reason for the low tax-to-GDP ratio in Nigeria is because of the large size of the country's informal economy.³

The International Labour Organization, has defined the informal sector as a group of production units comprised of unincorporated enterprises owned by households, including informal own-account enterprises and enterprises of informal employers (typically small and non-registered enterprises).⁴ The informal sector in Nigeria comprises businesses that are largely unregistered and operate outside government regulation, they include the commercial bus drivers, artisans, dressmakers, market traders, hawkers, domestic workers amongst others.

Over the years, the efforts by the tax authorities to bring the informal sector under the tax umbrella have suffered major setbacks. Some of the challenges faced by the tax authorities in taxing this sector are: (a) the lack of proper documentation in the sector. Most of the businesses in this sector do not keep proper accounting records which will enable them to produce audited accounts for the purpose of tax computation. (b) lack of trust between the government and taxpayers due to corruption and mismanagement of public funds (c) multiple levies on small businesses by local governments, unions and other non-state actors

which the informal sector views as taxes.

The informal economy comprises activities that have market value and would add to tax revenue and GDP if they were recorded. The gap between the number of registered companies, employed persons and tax compliant companies/persons is massive and to fully maximize tax revenue, this gap needs to be closed. For an economy that is overly dependent on crude oil, the need to find other sources to sustain the government budget has become necessary in the face of fluctuating price of crude oil and the corresponding rise of alternative energy sources, among other economic factors.

Tax has been proffered as immediate solution to address the revenue generation challenge of government. It has been defined as the monetary charge imposed by the government or persons, entities or properties to yield public revenue.⁵ The tax system is an opportunity for the government to assemble extra revenue needed in discharging economic development and creating a conducive business environment for its citizens.

The Value Added Tax (VAT) is an indirect tax levied in Nigeria, it is regulated by the Value Added Tax Act (as amended). VAT is a form of tax that is paid by the final consumer of goods and services as it is included in the price of the goods or services. It is a consumption tax charged on the supply of all goods and services, except for the items listed in the first

¹ Aderemi Ojekunle, '98% of Businesses in Nigeria's Informal Sector Pay Taxes but to Non-State Actors' (*The Cable*, 8th August 2021) <<https://www.thecable.ng/report-98-of-businesses-in-nigerias-informal-sector-pay-taxes-but-to-non-state-actors>> accessed 20th July 2023

² <https://www.businessamlive.com/nigerias-informal-economy-accounts-65-gdp-imf/>

³ Aderemi Ojekunle, '98% of Businesses in Nigeria's Informal Sector Pay Taxes but to Non-State Actors' (*The Cable*, 8th August 2021) <<https://www.thecable.ng/report-98-of-businesses-in-nigerias-informal-sector-pay-taxes-but-to-non-state-actors>> accessed 20th July 2023

⁴ International Labor Organisation, 'Distinguishing the concepts: the informal sector, informal employment and the informal economy' <https://www.ilo.org/global/topics/wages/minimum-wages/beneficiaries/WCMS_436492/lang-en/index.htm#:~:text=The%20informal%20economy%20encompasses%20both,insufficiently%20covered%20by%20formal%20arrangement> accessed 20th July 2023

⁵ BLACK'S LAW DICTIONARY (7th Edition, 1990) Page 1469

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schedule to the VAT Act, which includes medical and pharmaceutical, basic food items, books and educational materials and baby products.

Under the old regime, the VAT rate was 5%, but the Finance Act 2021, amended the VAT rate to 7.5 %⁶. It is pursuant to its powers as the taxing authority, that the Federal Internal Revenue Service has introduced the Value Added Tax Direct Initiative (VDI) aimed at facilitating the collection and remittance of VAT from the informal sector using a purpose-built digital platform.

Through this initiative, the FIRS is partnering with the Market Traders Association of Nigeria (MATAN) to collect & remit VAT from their members using a unified systems technology. The Association has a membership of well over 40 million traders across the country's 774 local governments, and 36 States plus the Federal Capital Territory is the biggest player in Nigeria's market space.⁷ While the modality of how this technology will work has not be made known to the public, it is believed that the adopted technology will simplify VAT payment and remittance for the marketplace and informal sector.

The VDI is not a new tax law, rather, it is the first of its kind program aimed at utilizing technology to foster collaboration between the FIRS and the marketplaces for the collection of tax. The drive for this initiative according to the FIRS is to end multiple taxation and to collect value added tax from the Market Traders Association of Nigeria (MATAN).

It is expected that the Initiative will have a monitoring and evaluation team comprising the FIRS officers and MATAN members to ensure transparency, accountability, prompt VAT remittance, sustained commitment and reporting to build public confidence in the initiative.⁸

According to the FIRS, some of the potential benefits from the success of the initiative are:

- Elimination of multiple taxation in the marketplace: The FIRS has stated that by this initiative, it will partner with the relevant security agencies to improve security in the markets and tackle the activities of touts, miscreants and self-imposed tax collectors.
- It will serve as a source of revenue generation for the government: It is projected that this partnership will lead to more revenue generated and provide the needed resources for infrastructural development and social amenities.
- Expansion of the country's tax net: The VAT direct Initiative will drive an unprecedented entry of people/ businesses within the informal sector into the who were not registered for tax into the tax net.
- Bolster public- private partnership.

Conclusion

While some stakeholders have welcomed this initiative, others believe that in view of the challenges faced by micro businesses that make up the informal sector, the timing of the initiative is wrong. They believe that to show good faith and earn the trust of the people, the government must first address the challenges of the sector before the implementation of the initiative.

Disclaimer

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⁶ Finance Act 2019, s. 34

⁷ Press Release, 'Multiple Taxation: FIRS Partners MATAN for VAT Remittance from Informal Sector' *Premium Times*, 22nd June 2023

<<https://www.premiumtimesng.com/promoted/606097-multiple-taxation-firs-partners-matan-for-vat-remittance-from-informal-sector.html>> accessed 20th July 2023

⁸ Ayodeji Adegboyega, 'FIRS announces plan to collect VAT from traders, informal economy', *Premium Times* (4th July 2023) < FIRS announces plan to collect VAT from traders, informal economy (premiumtimesng.com)> accessed 20th July 2023

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