



IS THE UNTAXED INFORMAL SECTOR NIGERIA'S UNEXPLORED ELDORADO?



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In August, the Federal High Court sitting in Rivers State, declared that the Rivers State Government and not the Federal Government of Nigeria is entitled to legislate on and collect Value Added Tax(VAT) within the state. Whilst this judgement may not necessarily speak to the conversation around the overall width of Nigeria's tax net/bracket, it invariably draws attention to the specific width of the Federal Government's earnings via taxation.

However, the focus of this disquisition is not the on goings around the current court dispute as it is beyond that. This article seeks to draw attention to the reality of the small tax net (further threatened by the Federal High Court decision) of not just the Federal Government but indeed, governments across all levels in Nigeria. In doing so, it draws attention to the dire need for a paradigm shift from the current status quo into the unexplored waters of other tax avenues as a critical source of generating revenue for the Nigerian state and her people.

The Informal Sector

Perhaps a convenient point to start from is to first adopt a working understanding of what is meant by the term "informal sector". In its basic



sense, the informal sector refers to the unregulated and unstructured businesses that form part of a nation's economy.

According to the OECD, the informal sector is composed of businesses which are characterised by a number of traits, including: a desire to generate employment or income for the persons concerned; little or no distinction between labour and capital; casual employment; and kinship or personal and social relations rather than formally contracted employees.¹

Although the small and medium-scale enterprises that form the bulk of the informal sector are largely unregulated and therefore untaxed, they remain significant contributors to the GDP of several nations, providing sources of employment and means of livelihood.

In a 2018 report by the International Labour Organisation, the informal sector is reported to account for 85.8% of employment in Africa². In Nigeria, the informal sector is recorded as contributing as much as 41.3% of the nation's GDP. Another report by the International Monetary Fund places Nigeria as having the highest contribution to GDP via the informal sector in Sub-Saharan Africa, also noting that Sub-Saharan figures are the highest globally, only behind Latin America.³

In light of the above statistics and figures, a natural ensuing expectation would be that, beyond providing a means of employment and livelihood for Nigeria's huge unemployed population, the Nigerian state should enjoy the benefits of huge tax revenues from this gargantuan sector.

However, the sour reality remains that as far as tax revenues from the informal sector are concerned, Nigeria's earnings from the sector are extremely low, as Nigeria's tax to GDP ratio is placed at a lowly level 6.1%⁴ when compared to the global OECD average of 33.8%.

The important question that now naturally arises is: what is responsible for this low-level tax earning from the informal sector?

¹ OECD, 'Glossary of Statistical Terms' <<https://stats.oecd.org/glossary/detail.asp?ID=1350>> Accessed 30 September, 2021.

² International Labour Organisation, 'More than 60 Percent of the World's Employed Population are in The Informal Economy' <https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_627189/lang-en/index.htm> Accessed 20 October, 2021.

³ Business A.M, 'Nigeria's Informal Economy Accounts For 65% Of GDP – IMF' <<https://www.businessamlive.com/nigerias-informal-economy-accounts-65-gdp-imf/>> Accessed 20 October, 2021.

⁴ Olunfunso Ola-Ojo and Oladejo Adeyemi, 'Effective Taxation of the Nigerian Informal Sector' <<https://ng.andersen.com/effective-taxation-of-the-nigerian-informal-sector/>> Accessed 23 October, 2021.



Factors Responsible for Low Tax Earnings from the Informal Sector in Nigeria

It is noteworthy that a number of scholarly works have been written discussing the factors responsible for low tax earnings from the informal sector. Drawing from a broad-based perspective of academia, the following factors have been commonly identified⁵:

- a. On the part of the citizenry – a sheer lack of understanding of tax laws and how they are applicable;
- b. A popular culture of unwillingness to pay taxes evidenced by tax avoidance and tax evasion tactics;
- c. The problem of multiple taxation which encourages tax evasion;
- d. Shortage of skilled personnel, equipment and logistics to ensure effective tax assessment and monitoring of compliance levels;
- e. The perceived lack of evidence of the usages of collected tax for the public good; and
- f. Poor accounting records on the part of business persons which does not allow for comprehensive tax assessments etc.

However, beyond the aforementioned factors that have been identified as being largely responsible for low tax earnings, a further view, which runs seemingly parallel to the traditional reasons for low tax earnings from the informal sector, is the fact that the informal sector is taxed but only a negligible percentage of such taxes reaches official government coffers.

In its report titled "Under the Hood: A Look into Taxation in Nigeria's Informal Sector", SBM Intelligence, an African-based R and D organization, found that a major bottleneck to informal taxation earnings arises from the uncertainty shrouding the process, which is characterised by multiple taxation and non-remittance to legitimate government coffers.

On multiple taxation, the report reveals that business people in the informal sector, composed of drivers, commercial motorcyclists, and artisans, etc., typically experience four levels of taxation by the state government, local governments, market organisations, and unions, and that the taxes paid in

⁵ Ibid. See also Adekoya ,A.,Olaoye, A., and Lawal, B., ' Informal Sector and Tax Compliance in Nigeria- Challenges and Opportunities' > Accessed 21 October, 2021.
<https://www.researchgate.net/publication/342451989_Informal_Sector_and_Tax_Compliance_in_Nigeria-Challenges_and_Opportunities?enrichId=rgreq-fd1fea805d2de60a53e121b203520231-XXX&enrichSource=Y292ZXJQYWdlOzM0MjQ1MTk4OTtBUzo5MDYzNjcwMTU1OTYwMzhAMTU5MzEwNjE0NDU4Mg%3D%3D&el=1_x_3&_esc=publicationCoverPdf> Accessed 24 October, 2021.



the grand scheme of things are quite significant. So, using the example of commercial bus driving, a common business across all states in the country, the report found that 67% of drivers in Lagos state paid an average of N3,000 per day in taxes; 89% in Delta state paid between 2100 and 3000 per day; 92% in Kano state paid between N50 and N200; and 77% in Oyo paid between 210 and 500 per day.

Seeing that most Nigerians have boarded one form of public transportation or the other, it is not just a fact but the truth that the collection of levies from drivers and motorcyclists is an occurrence witnessed by the average Nigerian. This is also true for other artisans doing business as they remit one form of payment or the other in the course of their work. One clear fact is that the collecting agents for both the government, trade unions, and other actors are typically aggressive people or even touts/thugs simpliciter. Their mode of enforcement typically involves the use of violence and the seizure of wares or other implements of trade. As a result, regardless of the multiplicity of taxation from the various identified groups, there is almost always compliance from the taxed persons.

As earlier stated, Nigeria's tax revenue contribution to the overall GDP ratio stands at a meagre 6%. This meagre figure is put into more perspective when one considers an IMF report that, as at 2018, Nigeria had only 56,329 corporate entities paying taxes (of the millions of registered businesses in Nigeria) and only 16.7% of Nigeria's active economic population paid individual-based taxes, whereas 80% of this active population is comprised of the informal sector. Indeed, what is clear without a doubt is that, beyond the factors highlighted above as being responsible for low tax returns, as they are contributory nonetheless, the view is expressed here that the major problem is the shadiness around taxing the informal sector, which does not ensure that all roads lead to legitimate government coffers.⁶

The Way Forward

The first thing Nigeria must do is to increase the transparency of the taxation process in the informal sector by ensuring that only authorised government personnel or agents are empowered to collect taxes. This not only solves the problem of multiple taxation and the activities of non-state actors in the collection process, it also, most importantly, ensures that all funds obtained

⁶ William Ukpe '98% of Nigerians Operating in the Informal Economy Pay taxes – Report' <<https://nairametrics.com/2021/08/11/98-of-nigerians-operating-in-the-informal-economy-pay-taxes-report/>> Accessed 24 October, 2021.



are remitted into government coffers. With this mechanism, the government can easily ensure accountability in remittances, set targets for its officials and ultimately nib any form of corruption in the bud.

In order to effectively expand its tax net, the Nigerian government must embark on proper sensitization campaigns on the benefits of taxation. This would achieve both objectives. First, it will help educate the public on how to pay taxes and the importance of taxation, as well as the many amenities the government can effectively fund when taxes are paid. Secondly, it will help counter the concerns that earned tax revenues will only be misappropriated for selfish gains.

The need for the government to honour the social contract is closely related to the point on sensitization taxation. With citizens being forced to pay taxes in order for the government to meet their needs, the government must ensure that it does not abdicate its responsibilities in ensuring social welfare. Leveraging technology is also an opportunity the government cannot afford to ignore. With proper technology deployment, the government can ensure that tax compliance is achieved by linking access to critical services such as telecommunications and banking to a tax payer's identity. So, for example, registered businesses could have tax sanctions imposed on their bank accounts by linking such accounts to a tax payer's identity.

Conclusion

Nigeria's 2021 budget of 13.6 trillion naira was recently passed by the National Assembly. The country's Finance Minister stated in October that 50% of the budget would be sourced from external and internal borrowing. Indeed, what is clear is that for as long as the country's earnings are low, the Nigerian state debt profile of 33.1 trillion naira will only continue to grow.

Now, more than ever, is the time for the country to explore its untapped oasis of tax earnings by taxing the informal sector properly and in the actual sense as captured above. This new stream of revenue will ultimately cushion the harsh economic realities the country currently faces.

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