

## THE TAXING POWER OF VALUE ADDED TAX AND FISCAL FEDERALISM IN NIGERIA: THE PATH AHEAD

ANIFOWOSE DAMILOLA JOSEPH\*

### Abstract

*It is a notorious fact that the taxing power of Value Added Tax (VAT) as a consumption tax is a prominent issue that has consistently put Nigeria's federalism on trial. This paper explores the taxing power of the Value Added Tax (VAT) within the context of fiscal federalism in Nigeria. It aims to examine the historical and current state of VAT in Nigeria, analyze its impact on fiscal federalism, and propose a way out. The study delves into the complex VAT tax powers between the central and state governments, its legal challenges and constitutional implications as well as the consequences for revenue generation in relation to fiscal autonomy. The major point of argument is that VAT as a consumption tax by whatever nomenclature it may be enacted should not be put solely in the hands of the Federal Government so as to ensure the states' financial viability. The finding of this paper is that there is a legal basis upon which consumption tax could be enacted by the state government subject to some limitations. The ultimate objective is to provide policymakers with insights and recommendations for fostering a more sustainable fiscal federalism framework in Nigeria.*

**Keywords:** Consumption Tax, Fiscal Federalism, Taxing power, Value Added Tax

### 1. Introduction.

There is Value Added Tax (VAT) frenzy among States and the Federal Government in Nigeria. The main reason for this agitation is not farfetched. It has been contended that some States are taking a lopsided share of the aggregate revenue relative to the amount

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\* LL.B (Hons), LL.M, Legal Practitioner, Email: [damilanifowose@gmail.com](mailto:damilanifowose@gmail.com)

of VAT being collected within their territories.<sup>1</sup> The agitation has been further fanned into flames by the judgment obtained by the Rivers State Government at the Federal High Court, Port Harcourt *Attorney General for Rivers State v Federal Inland Revenue Service (FIRS) & Attorney General of the Federation*.<sup>2</sup> In its judgment, the Court ruled that States, not the Federal Government, have the constitutional authority to levy the consumption tax known as VAT.<sup>3</sup>

Although the agitation is largely brewing in Rivers and Lagos states,<sup>4</sup> it is nevertheless bound to have sweeping implications on fiscal federalism in the country. This is because if Lagos and Rivers States successfully wrestle VAT from the Federal Government, it is bound to profoundly alter the fiscal autonomy of States in Nigeria. Despite its merits, the administration of VAT by sub-national states in a federal economy like Nigeria is fraught with difficulties. In order to provide a possible approach to implementing VAT in Nigeria, this paper explores the historical context of the consumption tax in Nigeria as well as the level of government to legislate VAT. The legal implications of the position of the law are also analyzed. Lastly, the paper proffer some way forward out of the identified legal problem.

## **2.0. Overview of Value Added Tax (VAT)**

VAT is a type of tax that is akin to the Sales Tax, both being indirect taxes that are levied only on the sale and purchase of affected products as opposed to direct taxes like Income, Profit, and Capital Gains taxes.

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According to former Minister of Finance, Mrs. Kemi Adeosun, in August 2017, 55 percent of the revenue generated by the FG was from the VAT collected from Lagos State alone, while the remaining 45 percent was generated from the remaining 35 states and the FCT. Ifeanyi Onuba, '55% of VAT Revenue Generated from Lagos' (*Punch*, 2 August 2017) <<https://punchng.com/55-of-vat-revenue-generated-from-lagos-adeosun/>> Accessed 24 JULY 2023

<sup>2</sup>Suit No. FHC/PH/CS/149/2020.

<sup>3</sup>Unreported judgment of the FHC, delivered by Hon. Justice Stephen Dalyop Pam, on August 9, 2021, in Suit No. FHC/PH/CS/149/2020.

<sup>4</sup>Paul Omorogbe 'FG, Wike put Nigeria's federalism on trial over VAT collection — Experts, lawyers' (*Tribune*, 09 September 2021) <<https://tribuneonlineng.com/fg-wike-puts-nigerias-federalism-on-trial-over-vat-collection-experts-lawyers/>> Accessed 2 August 2023.

Although it must be emphasized that Sales Tax differs from the Value Added Tax, the former has a narrow base, sourced from selected goods and services and levied only on the final consumer. Both are a type of consumption tax.<sup>5</sup>

It is therefore pertinent to state here that the term Value Added Tax commonly referred to as VAT, has no generally acceptable definition and to this end, there have been varying definitions. Value Added Tax has been defined as a consumption tax that is being charged and embraced by many developed and developing countries, which is relatively easy to administer and very difficult to evade.<sup>6</sup>

According to one of the leading tax authors in Nigeria, Value Added Tax was defined as a tax on the consumption of goods and services.<sup>7</sup> While this definition can be regarded as very applicable to the extant statutory VAT Act in Nigeria, it, however, fails to qualify the applicability of the tax, as not all goods and services consumed are under VAT going by the provisions of the law.

### **3.0. History of VAT in Nigeria**

There is no doubt that VAT and Sales Tax are fundamentally the same in terms of their nature and incidence as a consumption tax. The history of VAT as in the nature of consumption tax goes back to 1953 when the Sales of Produce Taxation Act was enacted<sup>8</sup> and the government was empowered to impose a tax on the sale of specified

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<sup>5</sup>A tax on the purchase of a commodity or service is known as a consumption tax. Sales taxes, Value Added taxes, excise taxes, and other taxes on consumed products and services are examples of consumption taxes. A taxing system in which people are charged according to how much they spend rather than how much they contribute to the economy (income tax) is referred to as a consumption tax. KAGAN Julia, 'Consumption Tax' (*Investopedia*, 31 March 2021) <<https://www.investopedia.com/terms/c/consumption-tax.asp>> Accessed 21 JULY 2023

<sup>6</sup>D Adegbe, F. Festus, J. Olajumoke and K.J. Dajuma, 'Assessment of Value Added Tax on the Growth and Development of Nigeria Economy: Imperative for Reform' Available at <<https://papers.ssrn.com>> Accessed 6AUGUST, 2023.

<sup>7</sup>A. Ipaye, *Nigerian Tax Law and Administration* (SCO Prime Publishers, London, 2014).

<sup>8</sup>Ordinance No, 12 of 1953.

commodities made to a Marketing Board or to a licensed buying agent.<sup>9</sup> However, the 1954 Constitution, for the first time, recognized the constituent regions as separate entities and made definite provisions for the imposition of sales tax by them. The regions then abrogated the 1953 enactment and replaced the Act with their own separate and regional Produce Sales Tax Laws.<sup>10</sup>

The Federal Government enacted the Sales of Produce (Taxation) Act, of 1957, to replace the Sales of Produce Taxation Act, of 1953, and provided for a tax in the Federal Territory of Lagos, on sales of produce to the Western Region Marketing Board, or any of the licensed buying agents.<sup>11</sup> The commodities taxed were cocoa, palm kernel, and palm oil only.

The Nigerian Constitution (Amendment) Order, 1959, introduced "taxes on amount paid or payable on the sale or purchase of commodities" as an item on the exclusive legislative list.<sup>12</sup> Some commodities were however exempted: These were agricultural produce, hides and skins, petrol, and diesel oil. These exceptions gave the regions leeway of taxing the exempted commodities. Item 35A of the 1959 Amendment was re-enacted as item 38 of the exclusive list of the Constitution of the Federation of Nigeria, 1960. As the tax on items such as agricultural produce, hides and skins, petrol, and diesel oil was not specifically placed on the concurrent list, it found a place on the residual power in respect of which the regions could legislate.<sup>13</sup> Thus, there was in existence the Sales tax which had been expressly provided for in both the Independence Constitution of 1960 and the Republican Constitution of 1963, which only the National Assembly

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<sup>9</sup>F.R.A. Williams, A submission to the Federal Court of Appeal, Ibadan, in the case of *Alhaji Ayinke' Aberuagbe vs. Ogun State*, FCA\*134/83 (1983).

<sup>10</sup>For example, the Western Region passed the Produce Sales Tax Law (No. 14 of 1957) after abrogating the Act as seen in Cap 99 Laws of Western Region of Nigeria 1959.

<sup>11</sup>Cap, 184, Vo I, VI, Laws of the Federation of Nigeria, 1958.

<sup>12</sup>Introduced as a new item 35A.

<sup>13</sup>Constitution of the Federation, 1963, Exclusive Legislative list, Item 38.

could legislate upon to the exclusion of the Regional Legislative Houses.

The 1979 Constitution,<sup>14</sup> however, omitted item 38 in its entirety as set out in both the 1960 and 1963 Constitutions. Though this omission precluded implicitly the imposition of sales tax as a residual subject, it was interpreted that the States did have the competence under the Constitution to legislate and impose a tax on the supply of goods and services within the States. This removal followed the recommendation of the 1975 Constitution Drafting Committee which reserved all taxes outside those on profits, incomes, capital gains, customs and excises duties, and stamp duties, to the States.

However, despite the fact that the Supreme Court upheld the power of States Governments to impose Sales Tax within the limit of their jurisdiction under the 1979 Constitution,<sup>15</sup> shortly after, there was a military coup that distorted the taxing system and brought sales tax under the jurisdiction of the Federal Government. The new Federal Military Government promulgated the Constitution (Suspension and Modifications) Decree 1984. The effect of the Decree was to give the Federal Government legislative powers over all matters, including state sales taxation. The implication of this is that The Military Governor of a State who is the sole legislator in the State now exercises delegated, authority thus having to seek the consent of the Federal Military Government before making any law even with respect to matters on the concurrent legislative list.

Thereafter, due to a combination of factors such as inefficient administration, the narrowness of its base, and evasion, Sales Tax did not yield the much-desired revenue for the State Governments; hence, their reliance on federal allocation persisted. In a bid to find a solution, the Federal Military Government introduced VAT which was a type of Sales Tax under the umbrella of consumption tax with effect from

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<sup>14</sup>The Constitution of the Federal Republic of Nigeria, 1979.

<sup>15</sup>*Attorney General of Ogun State v Alh. Ayinke Aberuagba*[1985] 3 NWLR 395.

1st January 1994 to replace Sales Tax.<sup>16</sup> Section 41 of the VAT Decree specifically repealed the Sales Tax Decree of 1986.<sup>17</sup>

At the planning stage, some doubts were expressed about the competence and desirability of the Federal Board of Inland Revenue (FBIR), to effectively administer the VAT. The States posited that the administration of VAT should be left to them. The Federal Government however felt the States did not have sufficient expertise to efficiently administer the new tax.<sup>18</sup> Also, the Sales Tax Laws enacted by the various States went beyond the ambit of their power under the constitution and therefore had a number of constitutional and administrative complications.<sup>19</sup>

Therefore, the administration and management of VAT were vested in the FBIR.<sup>20</sup> The revenue from VAT is paid into a special central account and distributed among the three levels of government. The initial policy was that 80 percent of it would be shared among the States and the Federal Capital Territory while Federal Government would retain 20 percent as administrative charges.<sup>21</sup> However, when the prospect of VAT as a cash cow became manifest, the Federal Government modified the distribution formula in its own favor and also extended it to the Local Governments in the ratio of 50, 25, and 25 percent to the Federal, State, and Local Governments respectively.<sup>22</sup> Due to protests by States and Local Governments, the distribution formula has been reviewed on a few occasions in such a

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<sup>16</sup>Decree No.7 of 1986, Cap 399, Laws of Federation, 1990.

<sup>17</sup>VAT Decree 1993, S 41.

<sup>18</sup>AbiolaSanni, 'Lagos State Sales Tax: Matters Arising' [2002] Justice Chambers, Faculty of Law, Obafemi Awolowo University, Nigeria. 2

<sup>19</sup>Ibid

<sup>20</sup>VAT Decree 1993, S 7.

<sup>21</sup>AbiolaSanni, 'Lagos State Sales Tax: Matters Arising.' ... (n18).

<sup>22</sup>A.R. Ipaye 'Legal and Social Framework for VAT in Nigeria', Unpublished Paper Presented at Workshop on Tax Law and Administration Organised by the Nigerian Law Reform Commission, 5.

way that would ensure fair VAT distribution based on the principle of the derivation of its proceed.<sup>23</sup>

It is important to say that the exclusion of VAT or Sales Tax as a consumption tax was also carried into the 1999 Constitution of the Federal Republic of Nigeria.<sup>24</sup> It was an omission that VAT was not mentioned in the 1999 Constitution despite being a major tax already in force. The implication for it post the 1999 Constitution, however, was the effect that there was already a federal consumption tax in effect through the VAT Decree which had no constitutional foundation but was actually in operation through further legislation making it an Act of Parliament despite its exclusion in both the exclusive and concurrent list.

Against these backgrounds, agitations have persisted by many states in a bid to increase internally generated revenue on the consumption tax issue. The Governor of Lagos State reintroduced Sales Tax in his Year 2000 budget speech. The State forged ahead to introduce its independent Sales Tax with effect from 1st January 2001.<sup>25</sup> Since then, litigation and controversy have trailed the issue of consumption tax in Nigeria either as a state tax law or as a federal VAT as constituted in the VAT Act and whether it is within the jurisdiction of a state or that of the Federal Government.

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<sup>23</sup>The existing formula is 50% to the State, 35% to the local government and 15% to the federal government. Ayo Teriba, "Insights on VAT Collection and Distribution in Nigeria" (*Vanguard*, 21 September 2021 <<https://www.vanguardngr.com/2021/09/insights-on-vat-collection-and-distribution-in-nigeria/#:~:text=Distribution%20of%20VAT&text=With%20effect%20from%20January%201999,%25%20and%20derivation%2020%25.%E2%80%9D>> Accessed 6 August 2023

<sup>24</sup>Ade Ipaye, *Nigerian Tax Law Administration* (SCO Prime Publishers 2014) 311-336.

<sup>25</sup>Oladipupo Stephen, 'Nigeria: Legislator Disagrees with Tinubu Over Tax' (*AllAfrica*, 28 December 1999) <<https://allafrica.com/stories/199912280155.html>> Accessed 1 August 2023

#### 4.0.State-Level VAT Administration and Implication on Fiscal Federalism

The failure of states to generate and manage revenue is one of the biggest obstacles to Nigeria's ailing fiscal federalism. Small and unstable revenue bases exist at the sub national levels. Thus, Nigeria's federalism appears to be suffering the most at the sub national level.<sup>26</sup> Sub national administrations in the nation constantly lament having a limited resource base in comparison to their enormous fiscal obligations. Those in favor of individual state administration argue that it will boost the IGR of many states since they will now be in a stronger position to collect VAT, as it is generally believed by some that VAT collection efficiency in Nigeria is low partly because it is centrally collected and thus, will reduce the incidence of non-remittance of VAT collections by companies.<sup>27</sup>

The necessity for a state-driven consumption tax is also predicated on the fact that it would help the state become more personally responsible for the economic growth of the state. This will help to aid more fiscal autonomy for the state. Much concentration has continued to be on sharing available funds rather than on *how to generate income. Individual states are not laying emphasis on production. The main reason for this is because there is no real incentive to boost productive activities in the state which would increase consumption tax in each state since they can always share with other states. If VAT is administered by individual states, there would be more creativity and push to improve production. If production improves, it will be very easy for Nigeria to grow and states will become more financially viable.*

*Also, when VAT is administered at the state level, it has the potential to simplify the collection of VAT and also allow for better monitoring*

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<sup>26</sup>Chukwuma. Agu, 'Fiscal Federalism, Governance and Internally Generated Revenue: Examining Weak Subnational Finances in Nigerian States.' [2010] 1(1) International Journal of Business Management and Economic Research 41-57.

<sup>27</sup>Prof Uche Uwaleke, a former Commissioner for Finance in Imo State and financial expert, (*Daily Trust* 09 March 2021) <<https://dailytrust.com/30-states-risk-bankruptcy-as-lagos-rivers-set-for-new-vat-regime>.> Accessed 2 August 2023.



and management of the tax system.<sup>28</sup> With states taking charge of VAT collection, they can now tailor their strategies and policies to better suit their specific needs, ultimately benefiting the local businesses and economy. The state-level approach would undoubtedly foster a sense of ownership and accountability among the states, leading to a more efficient and effective VAT collection system as the closest to the people especially in a country where tax avoidance and evasion are the norm.<sup>29</sup>

However, VAT in Nigeria is believed to be imposed for the benefit of all levels of government but collected by the Federal Government for onward sharing with States.<sup>30</sup> The justification for collecting VAT on behalf of States government seems dissentious considering that the allocation of a chunk of 50% to the State government appears to be a silencer.<sup>31</sup> But the question is, should it be imposed and collected by the Federal Government at all?

#### 5.0. Constitutional Provisions Related To VAT Taxing Powers

Section 1(1) of the Constitution asserts its supremacy over all authorities and individuals across Nigeria, encompassing not only the Federal Government, the Courts, and the FIRS but also all other entities and persons within the nation.<sup>32</sup> Section 1(3) however provides that any law that is inconsistent with the provisions of the Constitution shall be void to the extent of its inconsistency.<sup>33</sup> In *AG Ondo State v AGF*,<sup>34</sup> the court held that "... once the powers, rights and the

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<sup>28</sup>Gale, William G., and Benjamin H. Harris, "A VAT for the United States: Part of the Solution."

[2011]Tax Analysts 64-82.

<sup>29</sup>Bello, Temitayo. 'Law and Economics of Taxation, Tax Avoidance, and Tax Evasion; A Nigerian Template. (2017) SSRN 12.<[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2970992](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2970992)> Accessed 10August 2023.

<sup>30</sup>Section 40 of the VAT Act allocates 15% to the Federal Government, 50% to the State Governments and 35% to the Local Governments

<sup>31</sup>Ibid.

<sup>32</sup>CFRN 1999, s 1

<sup>33</sup>*AGF v Abubakar* [2007] 8 NWLR 1035 - 117.

<sup>34</sup>[2002] 9 NWLR 772 - 222.

limitations under the Constitution are identified as having been created, their existence cannot be disputed in a court of law".

It is on this basis that the Constitution empowers the National Assembly to legislate on matters contained in the Exclusive Legislative List and certain items under the Concurrent Legislative List.<sup>35</sup> The 2<sup>nd</sup> Schedule to the Constitution,<sup>36</sup> (Concurrent Legislative List) provides that the National Assembly in the exercise of its power to impose tax or duty on persons other than companies, may prescribe that such tax or duty be collected or administered by the state.

Items 58 and 59 within the Exclusive Legislative List of the Constitution pertain to matters related to stamp duties, taxes on incomes, profits, and capital gains. Notably, the Value Added Tax (VAT) is conspicuously absent from these items. Similarly, the Concurrent Legislative List, which grants legislative authority to both the Federal and State governments, does not make any reference to VAT either. This absence of VAT in both the Exclusive and Concurrent Lists implies that VAT does not fall under the jurisdiction of Items 58 and 59 in the Exclusive List or Item 7 in the Concurrent List. Consequently, VAT can be argued to be excluded from Federal Government control, marking it as a residual matter. It squarely falls within the domain of the States, making it a subject that the State Houses of Assembly have the legislative authority over.<sup>37</sup>

#### **6.0. Legal Challenges and Constitutional Implications**

Prior to the implementation of the Value Added Tax (VAT) system in Nigeria, there existed a notable legal ambiguity regarding the authority of State Governments to impose Sales Tax. This issue came to the forefront in the case of the *Attorney General of Ogun State v Alh. Ayinke Aberuagba*.<sup>38</sup>

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<sup>35</sup>CFRN 1999, s 3 and 4.

<sup>36</sup>Ibid, items 7 and 8 of Part II.

<sup>37</sup>*Attorney-General of the Federation v Attorney-General of Lagos State*, [2013] 16 NWLR (Pt 1380) 249(SC).

<sup>38</sup>[1985] 1 NWLR (3) 395.

Under the 1979 Constitution, a distinctive situation emerged compared to the two earlier Constitutions. Unlike its predecessors, the Exclusive Legislative List in the 1979 Constitution did not explicitly include provisions for sales or purchase taxes. Despite this absence, the now-defunct House of Assembly of Ogun State proceeded to pass the Sales Tax Law in 1982. This law mandated the imposition of taxes on specific goods brought into Ogun State and those purchased within the State.

The appellants, who were engaged in wholesale beer purchases within the State, took legal action to challenge the Sales Tax Law. They argued that this law contradicted the provisions of the 1979 Constitution, raising fundamental constitutional questions concerning the taxation powers allocated to both the Federal and State governments. This legal dispute brought to light the intricate interplay between Federal and State taxation authorities during this period of Nigeria's legal history. In its interpretation of Section 4 of the 1979 constitution, the Supreme Court clarified that:

...by residual legislative powers within the context of Section 4, is meant what was left after the matters in the Exclusive and Concurrent Legislative Lists and those matters which the Constitution expressly empowered the Federation and the States to legislate upon had been subtracted from the totality of the inherent and unlimited powers of a sovereign legislature. The Federation had no power to make laws on residual matters<sup>39</sup>

Furthermore, on the issue of whether a State could legislate on the sales tax, the Apex court held that every State in Nigeria may enact legislation imposing a sales tax within its borders as part of the concurrent legislative list, provided that it does not impede trade between other States. Once it does that, it has gone beyond its

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<sup>39</sup>Ibid.

jurisdiction, and the state's sales tax may be declared illegal.<sup>40</sup> The learned Justice who delivered the lead judgment held, inter alia that:

Having regard to the foregoing, I may summarize that the federation has implied exclusive power to make sales tax law on all matters within the exclusive and concurrent lists while states have implied or residuary power to enact sales tax law on all matters outside the said list.<sup>41</sup>

With the legal controversy generated by Sales Tax under the 1979 Constitution, there was an expectation that attention would be given to the issue in the 1999 Constitution. Regrettably, however, neither the Sales Tax nor VAT is specifically allocated to any of the three tiers of government under the Constitution.

The opportunity to settle this deep legal question arose in the 2017 case of *A.G of Lagos State v. Eko Hotels Limited & Anor.*<sup>42</sup> In this case, after receiving multiple demand letters from both the Federal Government and the Lagos State Government regarding the collection of VAT and sales tax, Eko Hotels Limited (EHL) took legal action on March 5, 2004. They filed a lawsuit in the Federal High Court to determine which government entity was legally entitled to collect the tax. The Federal High Court and the Court of Appeal, in this case, ruled that EHL should only remit the tax on its sales to customers to the Federal Government. However, Lagos State was dissatisfied with the decisions of both courts and decided to appeal to the Supreme Court. In their appeal, Lagos State argued that, according to Section 4 of the 1999 Constitution, they had the constitutional authority to collect sales tax.

It must be stated that despite the fact that the decision of the apex court was not as to the validity of the VAT, it still provides illumination on the controversies around VAT under our law. The question posed

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<sup>40</sup>Ibid.

<sup>41</sup>Ibid.

<sup>42</sup>[2017] 12 SC 1-107.

before the Apex court was whether the lower Court was right when it held that the VAT Act covered the field of sales tax and whether its provisions prevailed over the Sales Tax Law of Lagos State. Further, the court held that the VAT Act has covered the field on the subject of Sales Tax and therefore prevails over the Sales Tax Law of Lagos State. However, it must be stated that the issue of the constitutionality or otherwise of VAT being collected by the States was not dealt with.

In another case, *The Registered Trustees of Hotel Owners and Managers Association of Lagos (suing for itself and on behalf of all its members) v. Attorney-General of Lagos State & Federal Inland Revenue Service*,<sup>43</sup> The Lagos State Government argued that sections 1, 2, 4, 5 and 12 of the VAT Act are invalid, unconstitutional, and unenforceable because they are incompatible with the legislative authority granted to the various tiers of government and reserved in sections 4(2), (4), and (7) of the Constitution. The Lagos State Government's contention was upheld and sustained by the Federal High Court after hearing arguments, and as a result, it was decided that the Lagos State House of Assembly has the legislative authority to impose, charge, and collect tax on the supply of goods and services used in hotels, restaurants, and event venues because this power is listed on the residual list in the Schedule to the Constitution.<sup>44</sup>

More recently, the constitutional competence of the National Assembly and the Houses of Assembly of the respective States of the Federation to legislate on taxation matters was put to the test in the 2020 case of *Attorney General for Rivers State v Federal Inland Revenue Service (FIRS) & Attorney General of the Federation*.<sup>45</sup> In the said judgment, the court specifically held that based on *Item 7(a) & (b) of Part II, Second Schedule, 1999 Constitution*, the National Assembly may empower the State Government or authority to collect and

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<sup>43</sup>Unreported judgment delivered by Hon. Justice R. M. Aikawa of the FHC on October 3, 2019 in Suit No: FHC/L/CS/360/2018.

<sup>44</sup>Section 4(7) CFRN, the Taxes and Levies (Approved List for Collection) Act, the Taxes and Levies (Approved List for Collection) Act (Amendment) Order 2015, and the Lagos Consumption Law 2009.

<sup>45</sup>Suit No. FHC/PH/CS/149/2020.

administer the tax laws relating to capital gains tax, income tax on persons other than companies or stamp duty on documents or transactions. The court also determined that if the National Assembly delegates these powers to anyone or any entity other than the State Government or Authority, such delegation is invalid. Furthermore, in addressing this matter, the Court determined that the specifications outlined in Item 7(a) & (b), Part II, Second Schedule of the 1999 Constitution do not grant the National Assembly the authority to create legislation for imposing Sales Tax, VAT, or any other taxes beyond those explicitly mentioned in Item 7(a) & (b).<sup>46</sup>

Despite the fact that FIRS has challenged the ruling by filing an appeal against the Rivers State Attorney General and others,<sup>47</sup> to enable a more fiscally autonomous state government, there needs to be a shift to a dual VAT system where both the Federal and State Governments have the power to impose VAT on the supply of any goods and services within their respective sphere of influence. However, a federal VAT should only be validly imposed on international and inter-State supplies of goods and services while a State VAT or Sales Tax should be restricted to intra-State supplies of goods and services.<sup>48</sup>

#### **7.0. Possible Effects of State-Level VAT Administration**

VAT collection by State may increase its efficiency and responsiveness in Nigeria due to the fact that it will now be locally collected and thus, may reduce the incidence of non-remittance of VAT collections. Also, VAT collection by states would enhance its fiscal autonomy and resource control.<sup>49</sup> It could motivate individual

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<sup>46</sup>Unreported judgment of the FHC, delivered by Hon. Justice Stephen Dalyop Pam, on August 9, 2021, in Suit No. FHC/PH/CS/149/2020.

<sup>47</sup>CA/PH/282/2021. AEjekwonyilo, 'VAT Collection Tussle: Appeal Court orders Rivers, Lagos to halt enforcement' (Premium times, 10 September 2021) <<https://www.premiumtimesng.com/news/headlines/484203-vat-collection-tussle-appeal-court-orders-rivers-lagos-to-halt-enforcement.html>> Accessed 26 July 2023.

<sup>48</sup> *Attorney General of Ogun State v Alh. AyinkeAberuagba ...* (n 15)

<sup>49</sup> Vehorn, Charles L. "Tax Administration." In *Fiscal federalism in theory and practice*.

[1997] International Monetary Fund 116.

states to find ingenious ways to make their state more alluring to investors so as to support an increase in economic activities if they take charge of the proceeds. There are however other inevitable and far-reaching consequences of State administration of VAT in Nigeria.

The fact that a federal VAT would prevent the disparity in tax law and administration from State to State as was observed during the Second Republic under the 1979 Constitution is probably the biggest argument in favor of one.<sup>50</sup> This was the logic that informed the enactment of the Sales Tax Decree by the Federal Military Government in 1986.<sup>51</sup>

Also, the likely implications would be the general increase in prices of VAT-able goods and services.<sup>52</sup> In this respect, a company that sources the raw materials for manufacturing its product from a company in another state has to pay VAT at 7.5% through an initial company (input VAT). In this case, when this particular company's product is eventually sold, the final consumer is charged VAT at 7.5% (output VAT) in the state where it is to be sold. If this becomes the likely outcome, then, there will be an added burden on final consumers as companies factor in this additional tax burden when setting prices

A bottleneck in administration may also develop. In the present VAT collection system, where the FIRS oversees VAT administration, the maximum tax burden placed on the end consumer is set at 7.5%. This scenario could change if the responsibility were shifted to the states, as it would necessitate the calculation of input or output VAT, potentially altering the tax burden for the final consumer. However, if the States become responsible for the VAT administration, the collection

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<sup>50</sup>AbiolaSanni, 'Lagos State Sales Tax: Matters Arising.' 9... (n18)

<sup>51</sup>Tolu-Kolawole Deborah, 'VAT 'War' Fuels Struggle for True Fiscal Federalism as States Seek More Funds' (*Punch*, 13 March 2021) <<https://punchng.com/vat-war-fuels-struggle-for-true-fiscal-federalism-as-states-seek-more-funds/>> Accessed 24 July 2023.

<sup>52</sup>Taiwo Oyedele, 'How to fix Nigeria's broken VAT System' (*PWC Nigeria*, 11 March 2021) <[https://pwc-nigeria.typepad.com/tax\\_matters\\_nigeria/2021/09/how-to-fix-nigerias-broken-vat-system.html](https://pwc-nigeria.typepad.com/tax_matters_nigeria/2021/09/how-to-fix-nigerias-broken-vat-system.html)> Accessed 28 July 2023.

becomes complicated in that each state may be unwilling to permit the offsetting of input VAT against output VAT.<sup>53</sup>

Additionally, another consequence would be reduced VAT revenue for the majority of the states. In a situation where state governments are responsible for the collection of VAT, all the states of the federation, with the exception of Lagos, Rivers, and FCT, going by the 2020 VAT collection data, are likely to be worse off than they are under the present system of VAT collection and distribution.<sup>54</sup>

### 8.0. The Way Forward

Exploring the possibility of a dual VAT administration could be one of the most viable ways forward.<sup>55</sup> Based on a plethora of cases, the current position of the law seems to be that both the Federal and State Governments have the power to impose VAT on the supply of any goods and services within their respective sphere of influence.<sup>56</sup> However, a federal VAT can only be validly imposed on international and inter-State supplies of goods and services while a State VAT or Sales Tax will be restricted to intra-State supplies of goods and services.<sup>57</sup> This approach would involve both the Federal and State

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<sup>53</sup>Ibid.

<sup>54</sup>The data, shows that VAT generated from Lagos represents 65% of the total VAT generated in Nigeria; followed by FCT, which represents 17% of total VAT revenue. HannatuMusawa, 'VAT Administration Beyond Constitutionality: (Covering Nigeria with a Short Sheet)' (*Leadership*, 14 March 2021) <<https://leadership.ng/vat-administration-beyond-constitutionality-covering-nigeria-with-a-short-sheet/>> Accessed 17 MARCH 2023.

<sup>55</sup>Gurumurthi, S. 'Fiscal federalism: Towards an appropriate VAT system for a federal economy.' [1999] *Economic and Political Weekly* 2875-2888.

<sup>56</sup>In *Attorney-General of the Federation v Attorney-General of Lagos State*, [2013] 16 NWLR (Pt 1380) 249 (SC). while considering the inconsistency of laws made by the National Assembly and the State House of Assembly and the concept of federalism, among others, the Supreme Court upheld the constitutionality of the Hotel Licensing Law 1983, Hotel Occupancy and Restaurant Consumption Law 2009, and the Hotel Licensing (Amendment) Law 2010. See also, *Attorney General for Rivers State v Federal Inland Revenue Service (FIRS) & Attorney General of the Federation* Suit No. FHC/PH/CS/149/2020.

<sup>57</sup>*Attorney General of Ogun State v Alh. AyinkeAberuagba...* (n 15)



governments having their own VAT administrative bodies, but with clear guidelines and protocols to ensure smooth coordination between them. This could help address the challenges faced by businesses operating across different states, as well as ensure that VAT regulations are effectively implemented at both the federal and state levels. By adopting this approach, the government can strike a balance between centralized control and regional autonomy, thereby creating a VAT administration system that caters to the unique needs and dynamics of each state.

Also, Constitutional amendments and legislative reforms would also pave the way for more clarity in resolving the nagging questions on the scope of federal and state governments VAT/Sales taxing powers.<sup>58</sup> Thus, revisiting and updating the relevant provisions in the constitution to provide a clear framework for the administration of VAT, ensuring that it aligns with the current economic landscape and best practices in taxation. Additionally, legislative reforms can be undertaken to streamline VAT laws and regulations, making them more comprehensive, transparent, and easily enforceable. By undertaking these constitutional amendments and legislative reforms, the government can lay the foundation for a robust VAT administration system that is adaptable to changing economic realities and capable of addressing emerging challenges.

Furthermore, it is essential for there to be a harmonious collaboration between the Federal and State governments. It is therefore suggested that the States and the Federal Government should work out a realistic timeframe within which all the requisite legal and administrative frameworks would be worked out to ensure a smooth take-off of States' Sales Tax.<sup>59</sup> In order to create a harmonious and efficient system for Value Added Tax (VAT), it is thus crucial for the Federal and State governments to strengthen their collaboration. By working together, they can share resources, insights, and best practices, leading to a more cohesive and streamlined VAT administration process. This

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<sup>58</sup>AbiolaSanni, 'Lagos State Sales Tax: Matters Arising.' 1... (n18)

<sup>59</sup>Ibid

collaboration could also involve regular meetings, sharing of data and information, and joint training programs for government officials involved in VAT administration.

Finally, the role of the judiciary in the interpretation of the statute and resolving any dispute and conflicts related to the constitutional scope of VAT becomes crucial. As there are questions about the constitutionality of the VAT Act and the powers of the Federal Government and state governments in imposing and collecting VAT, the judiciary can play a vital role in giving clarity to the constitutionality of the taxing powers of the government in relation to VAT.<sup>60</sup> Also, in a possible dual VAT administration, there is the possibility of conflicts in the laws and therefore, it is essential for the Judiciary to take a bold and decisive stand in its interpretation in handling VAT-related cases.

#### **9.0. Conclusion**

The independence of the constituent parts, particularly fiscal independence, is one aspect of federalism. The incapacity of states to significantly generate, retain, and manage revenue, however, is one of the most significant obstacles to Nigeria's faltering fiscal federalism. Since VAT and other consumption taxes seem to fall under the residual legislative purview of states, I think one of the options that should be considered is the prospect of state administration.

Despite the potential drawbacks of fragmentation and tax competition which could also come with administrative complexities and coordination challenges if administered by the state government, it's still a necessity. The need for a state-driven consumption tax is predicated on the fact that it would help the state become more personally responsible to the economic growth of their state. This will help to aid more fiscal autonomy for the

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<sup>60</sup>Aladekomo, Anthony. 'Division of Taxing Powers in the Federation of Nigeria.' *SSRN* (2020). 9  
<[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3639090](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3639090)> Accessed 10 August 2023.

state and also aid the increased efficiency and responsiveness of its citizens to its administration.

The major point of argument is that VAT should not be left to the Federal Government alone since States are the primary provider of public goods to the retailers. There is no doubt, the makers of the constitution could not have intended that the Federal Government which controls and taxes all mineral resources would also send its taxmen to local businesses, offices, roadside cafes, and kiosks to demand the payment of taxes. Despite the fact that there is a constitutional argument surrounding the administration of VAT on intra-State supplies of goods and services in support of the states, it is quite clear that Federal Government is unwilling to let it go *amid paucity of funds in states*.

The way forward in the taxing power of the state and federal government lies in exploring the possibility of dual administration, strengthening collaboration, implementing constitutional amendments and legislative reforms, and relying on the judiciary to resolve any disputes. By embracing these viable solutions, the government can pave the way for a VAT model system that strengthens the fiscal viability of the state government.

If the country is really serious about the intention of a fiscally autonomous state, we must come to terms with the reality and necessity of a State consumption tax to enhance fiscal autonomy and financial viability of the state institution.