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Original Research Article

Tax Revenue and Economic Growth in Nigeria

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Abstract

This paper focus on the impact of tax revenue on economic growth in Nigeria. To achieve this, relevant data for the study were collected from secondary source which include Central Bank of Nigeria Statistical Bulletin; Abstract of Annual Data from the Office of National Bureau of Statistics (NBS) and the tax revenue data for this study were sourced from the Office of the Federal Inland Revenue Service for a time frame of 34 years (1981 to 2014). Ordinary regression method was used to analyse the data. From the analysis, we concluded that all tax variants exert a significant impact on GDP at 5% level and also have the expected positive sign. The result suggests the uniformity of the response of GDP to tax derivatives and thus supports tax-economic growth linkage in line with the endogenous growth theory. Premised on the conclusion, the study recommended that the various sub-components of tax (direct and indirect) should be efficiently collected and utilised to enhance the overall living standard of the people and taxation should be made more dynamic and effective, within the Nigerian context, to promote its role in terms of sustainable economic growth.

Keywords: Tax, tax revenue, economic growth, gross domestic product

JEL Classification Codes: F430, 0470

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1.0. INTRODUCTION

The survival of any nation depends on the amount of resources that are available for the provision of security, basic infrastructure and to meet her recurrent and capital expenditure. There appears to be a consensus that Nigerian economy is overly dependent on revenue from petroleum and petroleum products, with oil accounting for over seventy percent of the total federally collected revenue. Premised on the above assertion, and in the face of the dwindling global price of crude oil, it becomes of necessity for Nigerian government to seek and maintain an alternative and reliable source of revenue. To this end, tax revenue has become a vital alternative source of government revenue. According to Eiya (2012), tax is a compulsory levy imposed on income, profit and capital gains of the individual, companies or other legal entities by the government to raise revenue. Tax is a compulsory transfer or payment from private individuals, institutions or groups to the government (Anyanwu, 1997). The main purpose of tax is to raise revenue to meet government expenditures, to redistribute wealth and the management of a nation's economy (Bhartia, 2009; Ola, 2001). When a taxpayer pays tax with the consciousness of paying tax, it is referred to as direct tax. The primary motive for taxation is to finance government expenditure and to redistribute effectively income and wealth which in turn translates into economic growth and development of a country (Bhartia, 2009; Jhingan, 2004; Ola, 2001; Musgrave & Musgrave, 2004; as cited by Worlu & Emeka, 2012). In the opinion of Romer and Romer (2010), tax policies are implemented to finance a deficit budget, promote long-run growth rate, pay for incurred government expenditures and finally counter other influences in the economy. Whether this revenue is enough to finance the developmental priorities of the State will depend on the needs of the State and how well these resources are efficiently utilised. Under the current Nigerian laws, taxes are collected by the three tiers of government: the Federal, State and Local government with each having its jurisdiction clearly spelt out in the Taxes and Levies (Approved list for collection) Act No 2, 2015. Tax provides a stable flow of revenue to finance economic growth and development priorities, such as strengthening the infrastructures and other numerous policy areas. Grimus (2002) describes economic growth as a long-run process that results from the compounding of economic events over time. Economic growth can also be seen as increase in value of everything without having impact on the living standard of the people.

This paper therefore is anchored on the need to examine the impact of tax revenue on economic growth in Nigeria. Closely following the introduction is the review of literatures thereafter the methodology and finally the conclusion and recommendations.

2.0. REVIEW OF LITERATURE AND HYPOTHESES DEVELOPMENT

The Concept of Taxation

Taxation is a tool for societal development, and also a means by which the rewards of development are redistributed (Oladiran, 2009). The history of both developed and developing countries reveals that taxation is an important tool in the hands of the government, not only to generate revenue but also to achieve fiscal goals such as influencing the direction of societal development. According to the New Internationalist magazine (2008), tax originated from the Latin word '*Taxare*' which means 'to assess'. While Ariwodola (2008) describes taxation as a method by which a nation implements decisions to transfer resources from the private to the public sector. Adejuwon (2009) describes tax as a compulsory levy imposed by the government through its agencies on the income, capital and consumption of its subject to increase the resources of the government and enhance the effective provision of social amenities. Traditionally, taxes are based on income of individuals or profits of an economic entity (Naiyeju, 1996). Ndekwu (1991) also notes that more than ever before, there is now a great demand for the optimisation of revenue from various tax sources in Nigeria. The call for government in the affairs of man is the basis for taxation. This follows the idea that if there is to be a government to superintend human affairs in a given territory, such a government will need resources (human and material) to achieve its objective. The most efficient way of getting such resources is for individuals in the territory concerned to contribute in an agreed manner; such a contribution referred to as tax (Osemeke, 2010).

In the opinion of Anyaduba (2000), tax is a compulsory levy imposed on the income of individual, household and corporate entity by the government or its agent for the purpose of raising revenue. While Ogbonna and Appah (2012) asserts that the main aim of tax is to raise revenue to meet government's expenditure and to redistribute wealth and the management of the nation economy. However, Johansson, Heady, Arnold, Brys, and Vartia (2008) describe a tax system as a system that is primarily aimed at financing public expenditure. They emphasised the importance of tax revenue as a tool for promoting equality and re-addressing issue of social and economic concerns. Tax is a compulsory levy imposed on a subject or upon his property by the government to provide security, social amenities and create conditions for the economic well-being of the society (Appah, 2004, Appah & Oyandonghan, 2011). They further assert that the tax payable by an individual is not a function of

the benefit derivable from the process. The fundamental reason for imposing tax has always been to finance government activities, redistribute income, stimulate economic activities, and influence the level of aggregate demand among others. From the above, tax can be seen as a compulsory or a mandatory levy imposed on the income, profit and gain of individual, household, firms (incorporated and unincorporated) by the government to raise revenue to meet State obligations to her citizens. In differentiating taxation from tax, the latter is a compulsory levy impose on the income, profit and gain of individuals, firms and other entity by the government or its agencies in other to raise revenue for the government while the former is the system or process put in place by government or its agencies in raising the needed revenue.

Economic Growth

According to Dwivedi (2004) as cited in Ogbonna and Appah, (2011) economic growth is a sustained increase in per capita national output or net national product over an extended period. It is also seen as an increase in the capacity of an economy to produce goods and services which are usually associated with technological changes. It implies that the rate of increase in total output must be higher than the rate of population growth. Another quantification of economic growth is that national output should be composed of such goods and services which satisfy the maximum want of the maximum number of people. Economic growth can be determined by four essential determinants namely, human resources, national resources, capital formation and technological development (Ogbonna & Appah, 2011). Economic growth can be measured in nominal terms, which include inflation or in real term which adjust for inflation

Tax Revenue and Economic Growth

Worlu and Emeka (2012) examined the impact of tax revenue on the economic growth in Nigeria. For the purpose of the study, secondary data were collected from the Central Bank of Nigeria (CBN) Statistical Bulletin and the office of Federal Inland Revenue Service (FIRS). The data collected were analysed using the three-stage least square estimation technique. A macro-econometric model approach was adopted. The result of their analysis showed that tax revenue stimulates economic growth through infrastructural development. Masood, Sohaib, and Syed (2010) studied the impact of tax revenue on economic growth in Pakistan. The data used for the investigation were for a 36 year period ranging from 1973 to 2008, gotten from the economics survey of SBP 50 year's statistics of Pakistan. General multivariate VAR model and the Auto Regressive Distributed Lag (ARDL) model were used in the empirical analysis. The results of their analysis showed that all the coefficients are statistically significant, and the coefficient of error correction term showed a low rate of convergence in the long run.

Poulson and Kaplan (2008) examined the impact of tax policy on economic growth in the states within the framework of an endogenous growth model. Regression analysis was used to estimate the impact of taxes on economic growth in the states from 1964 to 2004. Their analysis revealed a significant negative impact on higher marginal tax rates on economic growth. The analysis underscores the importance of controlling for progressivity, convergence, and regional influences in isolating the effect of taxes on economic growth in the states. Mashkoor, Yahya and Ali, (2010) in their study, evaluated the relationship between tax revenue and the rate of economic growth in Pakistan using data from 1973 to 2008. From the study, they concluded that direct tax to GDP ratio and direct tax to total tax ratio caused the real GDP growth

Padda and Akram (2009) in their study from seven Asian countries for 1971 to 2007 concluded that tax policies adopted by developing countries have no evidence that taxes permanently affect economic growth rate but that government policies. Barry and Jules, (2008) examined the impact of tax policy on economic growth in the United States within the framework of an endogenous growth model. Data for the study were gathered for 1964 to 2004 and from the analysis, the study showed that a negative relationship exists between taxes and economic growth in the United States of America. In addition, Karras and Furceri, (2009) examined the impact of changes in taxes on economic growth in 19 European countries and the result from the study showed that a negative and persistent impact of changes in taxes on the gross domestic product. They further stated that increases in social security contribution and taxes on goods and services have larger negative effects on per capita output than increases in income tax

Ayuba (2014) examined the impact of non-oil tax revenue on economic growth from 1993 to 2012 in Nigeria. The study utilised annual time series data from the Central Bank of Nigeria Statistical Bulletin (Real Gross Domestic Product (RGDP)) and the Federal Inland Revenue Service (non-oil tax revenue) for the period of 1993-2012. These data were analysed using the Ordinary Least Squares Regression. The result from the empirical test showed that there exists a positive statistical significant impact of non-oil tax revenue on economic growth in Nigeria. Economic growth was proxied by real gross domestic product while non-oil tax revenue was proxy by taxes such as companies' income tax, personal income tax, capital gains tax, stamp duty,

valued added tax, customs and excise duties, amongst others. In another study, Iyoha and Oriakhi (2010) examined the buoyancy of Nigeria tax system and its effect on GDP. The study concluded that income tax has a positive impact on economic growth in Nigeria.

3.0. RESEARCH METHODS

A longitudinal research design was used for this study while relevant macro-economic data were obtained from the Central Bank of Nigeria (CBN) Statistical Bulletin, Annual Abstract of Statistics from the Office of National Bureau of Statistics while the tax data were obtained from the Office of the Federal Inland Revenue Service for 34 years (1981 to 2014). The ordinary regression method was used in analysing the data gathered. The significant level was set at 0.05. The dependent variable was economic growth, while the independent variables were direct tax, indirect tax and total tax.

Model Specification

In an attempt to determine the impact of tax revenue on economic growth in Nigeria from 1981 to 2014, the model below was adopted for this study:

$$GDP = \eta_0 + \sum_{j=1}^q \eta_2 \Delta TDT_{t-j} + \sum_{j=0}^q \eta_3 \Delta TTR_{t-j} + \sum_{j=0}^q \eta_4 \Delta TIT_{t-j} + \sum_{j=0}^q \eta_5 \Delta OPN_{t-j} + \sum_{j=0}^q \eta_6 \Delta FDI_{t-j} + \sum_{j=0}^q \eta_7 \Delta INF_{t-j} + \sum_{j=0}^q \varphi_1 \Delta ECM_{t-1} + \varepsilon \quad (1)$$

Where;

GDP = real gross domestic product (proxy for economic growth), *TDT* = total direct tax

TTR = total tax revenue, *TIT* = total indirect tax, *OPN* = openness (was used as a control variable), *FDI* =

foreign direct investment (was used as a control variable), *INF* = inflation rate (was used as a control variable),

Δ = the difference operator, u = the stochastic, disturbance or error term, $\eta_1 - \eta_6$ = slope coefficients, q =

chosen lag length, t = time period

apropri expectation: $\eta_1, \eta_2, \eta_3, \eta_4, \eta_5, \eta_6, \eta_7 > 0$

4.0. RESULTS AND DISCUSSION

The data were analysed using (a) unit root test, (b) descriptive analysis (c) error correction model.

Unit root test

Table 1: Augmented Dicky-Fuller (ADF) Unit Root Test Results

Unit root tests at levels			
Variable	ADF-Test Statistic	95% Critical ADF Value	Remark
TDT	1.916	-2.96	Non-stationary
TTR	0.426	-2.96	“
TIT	-1.891	-2.96	“
FDI	-0.285	-2.96	Non-stationary
GDP	-1.105	-2.96	Non-stationary
INF	-3.568	-2.96	Stationary
OPN	-2.070	-2.96	Non-stationary
Unit root test at 1 st difference			
Variable	ADF-Test Statistic	95% Critical ADF Value	Remark
TDT	-6.282	-2.96	Stationary
TTR	-5.696	-2.96	Stationary
TIT	-7.088	-2.96	Stationary
FDI	-4.982	-2.96	Stationary
GDP	-2.991	-2.96	Stationary
INF	-5.880	-2.96	Stationary
OPN	-4.193	-2.96	Stationary

Table 1, presents the result of the ADF test in levels without taking into consideration the trend of the variables. The reason for this is that an explicit test of the trending pattern of the time series has not been carried out. In

the result, the ADF test statistics for the variables is shown in the second column, while the 95% critical ADF value is shown in the third column. The result indicates that all of the variables at levels have ADF values that are less than the 95% critical ADF value of 2.96. Examining the variables at levels, the result is as follows; TDT(ADF=-1.916), TFR (ADF=0.426), TIT (ADF=-1.891), FDI (ADF= 0.285), GDP (ADF= 1.105), INF (ADF=-3.568), OPN (ADF= 2.164). As observed only INF is stationary at level and the other variables are not stationary at levels. Moving forward, we took the first difference of the respective variables and perform the unit root test on each of the resultant time series. The rationale behind this procedure is that according to Box and Jenkins (1976) differencing non-stationary time series will enable it to attain stationarity. Hence, examining the variables at first difference, the result is as follows; TDT (ADF=-5.282), TFR (ADF=-5.696), TIT (ADF=-7.088), FDI (ADF= -4.982), GDP (ADF= -2.991), INF (ADF=-5.880), OPN (ADF=-4.193). The result of the unit root test on these variables in first differencing shows that the ADF values in absolute terms is greater than the 95% critical ADF values. With these result, these variables are adjudged to be stationary. Thus, we accept the hypothesis that the variables possess unit roots. Indeed, the variables are integrated of order one i.e. I(1).

Table 2: Philip Perron Unit root test Results

Unit root tests at levels			
Variable	ADF-Test Statistic	95% Critical ADF Value	Remark
TDT	-1.994	-2.96	Non-stationary
TTR	-0.426	-2.96	Non-stationary
TIT	-1.891	-2.96	Non-stationary
FDI	-5.210	-2.96	Stationary
GDP	-1.080	-2.96	Non-stationary
INF	-2.872	-2.96	Stationary
OPN	-2.141	-2.96	Non-stationary
Unit root test at 1 st difference			
Variable	ADF-Test Statistic	95% Critical ADF Value	Remark
TDT	-7.284	-2.96	stationary
TTR	-6.615	-2.96	Stationary
TIT	-7.088	-2.96	Stationary
FDI	-23.714	-2.96	Stationary
GDP	-5.236	-2.96	Stationary
INF	-9.098	-2.96	Stationary
OPN	-5.509	-2.96	Stationary

Table 2 presents the result of the Phillip-Perron (PP) unit root test at levels and first difference. Phillips-Perron (PP) (1988) test is an extension of the Dickey-Fuller (DF) test, which makes the semi-parametric correction for autocorrelation and is more robust in the case of weakly autocorrelation and heteroscedastic regression residuals. According to Choi (1992), the Phillips-Perron test appears to be more powerful than the ADF test for the aggregate data. Examining the variables at levels, the result is as follows; TDT(ADF=-1.994), TTR (ADF= -0.426), TIT (ADF=-1.891), FDI (ADF= -5.210), GDP (ADF= -1.080), INF (ADF=-2.872), OPN (ADF= -2.141). As observed, only INF is seen to be stationary at levels while all other variables are non-stationary at levels. Moving forward, we take the first difference of the respective variables and perform the unit root test on each of the resultant time series. Examining the variables at first difference, the result is as follows; TDT(ADF=-7.284), TTR (ADF=-6.615), TIT (ADF=-7.088), FDI (ADF= -23.714), GDP (ADF=-5.236), INF (ADF=-9.098), and OPN (ADF= -5.509). The results of the unit root test on these variables in first differencing shows that the PP values in absolute terms are greater than the 95% critical ADF values. With these result, these variables are adjudged to be stationary. Thus, we accept the hypothesis that the variables possess unit roots. Indeed, the variables are integrated of order one i.e. I(1). Consequently, both the Augmented DickeyFuller and the Philip Perron tests for stationary reach a similar conclusion regarding the stationarity status of the variables.

Table 3. Descriptive Statistics

	Mean	Median	Maximum	Minimum	Std. Dev.
TDT	65	68	85	46	12.69537
TTR	2155.604	493.6029	11116.85	10.5087	2981.197
TIT	35	32	54	15	12.69537
FDI	302713.3	86772.95	5028391	264.3	906621.4
GDP	7062381	2705575	30122057	49069.3	9707363
INF	23.08667	15.5	33.1	4.7	18.43776
OPN	85.95867	72.75	111.2	28.5	48.2565

The descriptive statistics is presented for the variables as shown in Table3. As observed, TDT has a mean value of ₦65bn with a standard deviation of 12.695. Maximum and minimum values are ₦85bn and ₦46bn respectively. TTR has a mean value of 2155.604bn with a standard deviation of 2981.197. Maximum and minimum values are ₦11116.85bn and ₦10.5087bn respectively. TIT has a mean value of ₦35bn with a standard deviation of 12.695. Maximum and minimum values are ₦54bn and ₦15bn respectively. GDP has a mean value of 7062381 with a standard deviation of 9707363. Maximum and minimum values are 30122057 and 49069.3 respectively. INF has a mean value of 15.5 with standard deviation of 18.437. The Maximum and minimum values are 33 and 4.7 respectively. OPN has a mean value of 85.958 with a standard deviation of 201.2. The Maximum and minimum values are 111.2 and 28.5 respectively.

Regression analysis

Regression output

Dependent Variable: GDP

Method: Least Squares

Date: 09/13/15 Time: 23:26

Sample(adjusted): 1982 2014

Included observations: 33 after adjusting endpoints

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	4.959017.	19.12279.	2.702944	0.0157
D(TDT)	9.540274.	2.964183.	-3.294146	0.0004
D(TTR)	9.349821	3.610655	2.575647	0.0160
D(TIT)	-9.42669.	2.973189.	-3.264841	0.0003
D(OPN)	2.472311	1.009719	-2.475645	0.0201
D(FDI)	3.207353	1.054280	3.051198	0.0052
GDPRESID01(-1)	-0.468205	1.146774	-0.408280	0.6864
R-squared	0.493224	Mean dependent var		8964066.
Adjusted R-squared	0.350122	S.D. dependent var		11099978
S.E. of regression	8809483.	Akaike info criterion		35.00639
Sum squared resid	2.02E+15	Schwarz criterion		35.32383
Log likelihood	-570.6054	F-statistic		6.162912
Durbin-Watson stat	1.913592	Prob(F-statistic)		0.004797

Estimation showed the effect of tax revenue on economic growth as measured by real GDP. The R^2 of the model is 49.3% with an adjusted R^2 of 35%. The F-stat is 3.466 (p-value = 0.00) and significant at 5% and suggest that the hypothesis of a significant linear relationship between the dependent and independent variables cannot be rejected. The D.W. statistics of 1.9 indicates the absence of stochastic dependence in the model. Commenting on the performance of the structural coefficients, the coefficient and p-values of the three tax variants TDT, TTR and TIT are given as follows; 9.540 {0.004}, 9.349 {0.016} and 9.426 {0.004} respectively. The estimates reveal that all tax variants exert a significant impact on gross domestic product at 5% level. However, only TTR appears to have the expected positive sign.

4.0. RESULTS AND DISCUSSION

Estimations show the effect of tax revenue on economic growth as measured by GDP. Commenting on the performance of the structural coefficients, the coefficient and p-values of the three tax variants TDT, TTR and TIT are given as follows; 9.540 {0.004}, 9.349 {0.016} and 9.426 {0.004} respectively. The estimates reveal

that all tax variants exert a significant impact on GDP at 5% level and also have the expected positive sign. The result suggests the uniformity in the response of GDP to tax derivatives and thus supports tax-economic growth linkage as in line with the endogenous growth theory. Consequently, we fail to accept the hypothesis that tax revenue has no significant positive effect on GDP. The study finding in this regard is in tandem with several studies that have showed a positive relationship (Worlu & Emeka, 2012; Ogbonna & Appah, 2012; Edame & Okoi, 2014; Saibu & Olatunbosun, 2013; Ayuba, 2014; Yakubu & Jibrim, 2013 and Bakare, 2013). In contrast, other studies have also reported a negative relationship (Greenidge & Drakes, 2009; Osundina & Olarewaju, 2013; Ebiringa & Emeh, 2012; Ilaboya & Mgbame, 2012).

5.0. CONCLUSION AND RECOMMENDATIONS

This study examined the impact of tax revenue on economic growth in Nigeria. It complements most of the studies done in this area which focused on tax revenue and economic growth from a disaggregated tax perspective. In this study emphasis was placed on tax revenue from tax variants perspectives which were direct tax; indirect tax and total tax. The paper concludes that all tax variants exert a significant impact on GDP at 5% level and also have the expected positive sign. The result suggests the uniformity of the response of GDP to tax derivatives and thus supports tax-economic growth linkage as in line with the endogenous growth theory. Premised on the conclusion the paper recommended that the various sub-component of tax (direct and indirect) should be efficiently collected and utilised to enhance the overall living standard of the people and taxation should be made more dynamic and effective within the Nigerian context to promote its role in term of sustainable economic growth.

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