ABSTRACT

This study examined the impact of the tax incentives on the overall performance of registered small scale industries in Rivers State, Nigeria. Eleven, out of the twenty two registered small scale food and beverages manufacturing industries in Rivers State were selected randomly for the study. Questionnaires were administered to 260 respondents in the selected companies. Frequency distribution and chi-square were used in the analysis of data and hypotheses testing respectively. The findings revealed that there are various tax incentives available to small scale industries and the operators in these industries are very familiar with them. It was also discovered that tax incentives do significantly affect the profitability, staff strength and the growth and development of small scale industries positively. The key recommendation includes that government should periodically review the tax incentives so as to reflect the prevailing economic conditions.

Key words: Tax incentives, Profitability, Economic growth and development
1.0 BACKGROUND TO THE STUDY

The modern day taxation and its use as a fiscal policy could be traced to 1926, which was a year of economic depression in Great Britain. During this period, Britain witnessed an unprecedented decline in her overall economic activities resulting to reduction in total earnings, shortage of fund in the private sector and reduced income per capitol with attendant low standard of living. The effect of this depression was felt not only in Britain but almost the world over. Governments at this time were trying to revive, rehabilitate and mobilize enough capital to provide for economic and social expenses and to raise the standard of living of its populace. In doing this, various fiscal policies were formulated which include taxation.

According to Aguolu (1999: 1); taxation may be defined as a compulsory levy by Government through its agencies on the income, consumption and capital of its subjects. These levies are made on personal income such as salaries, business profits, interests, dividends, discounts and royalties. They are used to provide security, social amenities and create conditions for the economic well being of the society. The main purpose of taxation according to Ola (1998:14) is to raise funds to meet Government’s expenditure and to redistribute wealth and management of the economy.

Historically, Nigeria’s experience of taxation predates the colonial period. The Hausas of Northern Nigeria were paying taxes, though in kind, to the Emir in return for security and common services. However, with the advent of the colonialists, direct taxation was introduced in 1904 by Sir Lord Lugard, the then British appointed Governor. Its implementation started first in the North and later in the Southern and Eastern regions.

According to Ezejelue and Ihendinihu (2006:1) taxation can be defined as the demand made by the government of a country for a compulsory payment of money by the citizens of the country with the objective of raising revenue, satisfy collective wants of the people and regulate economic and social policies.
Aguolu (1999:17) defined tax incentive as an exemption or relief granted to an individual or a company to reduce the effect of taxation and thus encourage savings and investment. These incentives are granted to individuals or companies whose income or profit is accruing in, derived from, brought into or received in Nigeria. They include: (i) Personal Allowance (ii) Investment Allowance (iii) Capital Allowance (iv) Loss Relief (v) Roll over Relief (vi) Pioneer Relief (vii) Exploration incentives

These incentives are however backed by various Government legislations. They are granted to enhance the growth and development of industries as well as empowering individuals and corporate taxpayers economically. This work will therefore focus on tax incentives and their impact on small-scale industries with emphasis on selected small-scale industries in Rivers State.

2.0 STATEMENT OF THE PROBLEM

The objective of granting tax relief and incentives to small and medium scale enterprises is to enhance their growth and development, thus contributing to the overall economic development of the country. But the objective cannot be achieved in a situation where the would-be beneficiaries are not even aware of the existence of such incentives. Moreover, the few who are aware of these incentives do not even bother to apply for them due to the poor and inefficient tax administration. Therefore, there is the need to proffer solutions to these problems to ensure the growth and development of our economy.

3.0 OBJECTIVE OF THE STUDY

The objective of this study is to identify the existing tax incentives in Nigeria relevant to the small-scale enterprises; and to also examine the effect of tax incentives on the after tax profits of small scale enterprises.

Research Questions

The following research questions will be considered in this study:

1) What are the tax incentives available to small scale enterprises in Nigeria?
2) What is the level of taxpayers’ awareness of the existence of these incentives?
3) What effects do tax incentives have on after tax profits of small scale enterprises?

4) Is there any relationship between tax incentives and the growth of small scale enterprises in Nigeria?

**Research Hypotheses**

In order to ascertain the impact of tax incentives on the performance of small-scale enterprises, the following hypotheses have been formulated:

H₀₁: Tax incentives do not have any significant effect on the after tax profits of small-scale industries.

H₀₂: Tax incentives do not enhance the growth of small scale enterprises.

**4.0 REVIEW OF RELATED LITERATURE**

Taxes generally are construed as a compulsory or obligatory payment to the government to enable it function. A tax is a financial charge or other levy imposed on an individual or a legal entity by a state or a functional equivalent of a state. Individuals who enjoy tax incentives in Nigeria are individuals and companies, whose income or profit is accruing in, derived from, brought into or receive in Nigeria, Aguolu (1999:137–140). Kohler (1961:41) defined tax as a charge levied by a government unit against the income or wealth of a person or corporate for the common benefit of all.

Although Douglas (1983:40) views taxes as obstacles to economic success, the definition suggested by Rabiu (1981:10-12) explained the context in which taxes should be viewed for the purpose of this research. He defined taxation as the demand made by the government of a country for a compulsory payment of money by the citizens of the country. He further went on to explain that taxation has some main objectives.

The original purpose of taxation is to raise revenue to finance government expenditures. It is also used to influence the economy, for example in providing incentives for production, investments and savings. In attempting to define tax incentives, Elezue (1984:48) argued that any country that wants to develop has to create
the right kind of investment climate to attract inventible funds into the industry and tax measures form an integral part of the investment climate.

The Companies Income Tax Act

The law regulating the taxation of companies in Nigeria is the Companies Income Tax Act 1979 as amended. The Act is contained in chapter 60, Laws of the Federation of Nigeria (LFN) 1990 and is amended by subsequent decrees (Acts) including the Finance (Miscellaneous Provisions) of 1993 and other subsequent amendments thereto. The administration of CITA rests on the shoulders of the Federal Board of Inland Revenue which has the following powers and duties:

1. It is responsible for the administration of the Companies Income Tax Act and Decree. It assesses and collects the necessary company taxes.
2. It can sue and be sued in its official name
3. It can acquire, hold or dispose any property held as security and account for the proceeds to the Minister of Finance.
4. It may authorize any person within or outside Nigerian to perform or exercise any of its power except those stated under the first schedule to the Act.
5. It may (with the consent of the Finance Minister) appoint the joint Tax Board to perform or exercise any of its duties or powers.

Pioneer Legislations and Pioneer Conditions

One of the investment incentives available to industries in Nigeria is that under the Industrial Development (Income Tax Relief) Act 1971, The Act which is now under Chapter 179 of the Laws of Federation of Nigeria (LFN) 1990 came into force on 1st April, 1971 throughout Nigeria. Where the National Council of Ministers (the Council) is satisfied that:-

(a) Any company is not being carried on in Nigeria on a scale suitable to the economic requirements of Nigeria, or
(b) It is not carried out at all, or
(c) There are favourable prospects of further development in Nigeria of any industry, or
(d) It is expedient in the public interest to encourage the development or establishment of any industry in Nigeria, the council may declare such industries pioneer industries and of their products to be a pioneer products.

Some of the conditions that must be met for a company to be granted a pioneer status include the following: It may apply at any time for the issue of a pioneer certificate in relation to any pioneer industry or product with non-refundable fee of N100. Also a company that wishes to engage in an industry or product which not been designated pioneer may submit an application for the industry to be included in the list. Furthermore, where an application is successful, the company is issued with a pioneer certificate in which the conditions for enjoying the income tax relief will be stated. Finally, for any application for pioneer certificate to be considered, the estimated cost of qualifying capital expenditure to be incurred by the company as or before production day shall not be less than: ^50,000 in respect of indigenous controlled company or ^150,000 in the case of other companies

The Concept of Tax Incentives

Tax incentives have been defined in various ways by different scholars. Nevertheless, the concept is essentially the same. Both Okauru 2009, and Aguolu 1999 described tax incentive as an exemption or relief granted to an individual or a company to reduce the effect of taxation and thus encourage savings and investment. Okauru (2009:2) noted further that the reality of tax incentives in Nigeria is that not many people truly take advantage of the incentives that exist, and even when they do, past trends have suggested an individual corporate approach rather than an industry-wide approach.

Tax Incentives in Nigeria

The government of Nigeria has over the years allowed tax incentives and reliefs such as:
1. Pioneer Companies’ Tax Holiday subject to a maximum of 5 years is granted to companies with pioneer status on the basis of newness and relevance of the products by the companies. This will be fully discussed later in this study.

2. Export free zone exempt profit from tax at a rate of hundred percent (100%). Exemption for profits obtained from export free zone for 3 consecutive assessment years.

3. Solid minerals mining for a new company going into the mining of solid minerals for the first 3 years of its operation.

4. Hotel income exempt from tax: Twenty-five percent (25%) of income is put in a reserved fund to be utilized within 5 years for the building expansion of new hotels, conference centres and new facilities for tourism development.

5. Spare parts fabrication: For a company engaged wholly in the fabrication of spare parts, tools and equipment for local consumption and export; twenty five percent (25%) investment tax credit is allowed on qualifying capital expenditure, S. 28 F 9 (1) of CITA.

6. Locally manufactured plant: A fifteen percent (15%) investment tax credit is allowed for a company which produces totally manufactured plant, machinery or equipment.

7. Replacement of Obsolete plant: A fifteen percent (15%) investment tax credit for a company which has incurred expenditure for replacement of all obsolete plant and machinery.

8. Investment Tax Relief: Relief is granted for 3 years to companies located at least 20km away from essential infrastructure such as electricity, water, tarred roads and telephone services, when expenditures are incurred on such infrastructure.

9. Investment allowance: A ten percent (10%) tax relief for companies in the first year of purchase of plant and machinery used for agricultural and manufacturing companies. This is in addition to the normal initial and annual allowances.

10. Rural investment allowance: This is granted to companies established in rural areas lacking infrastructural facilities.
8 Objectives of Tax Incentives

Tax incentives are meant to encourage and stimulate the economic activities of enterprises and investments, Donald (1980:72). They are fiscal policies designed by the Government to revive, rehabilitate and stabilize individuals and corporate bodies. The tax incentives are also used by the Government to channel some specific economic activities towards the vital sectors of the economy where they are not felt or non-existent. Philips (1969:10) observed that tax incentives will not only generate employment but will motivate the self-employed to incorporate into limited liability companies. Okelle (1995:2) noted that the nation’s economy can be healthy through generous tax incentives to corporate tax payers, to projects, the profitability of which may not likely materialize until about three to five years time.

Otumba (1995) is of the opinion that tax incentives are measures used to stimulate private investment but such measures cannot work effectively if the economy is not resilient and properly solidified to absorb these incentives schemes. According to International Bank for Reconstruction and Development (IBRD) Report (1992:7), some of the structural criteria to which tax incentives devices may be addressed include: Development of the domestic market, Balanced regional development, Reduction in unemployment, Better utilization of existing capital, Diversification of output, Balance of payment consideration, and Re-direction of investment pattern.

5.0 METHODOLOGY AND ANALYSIS

The data used for this study were obtained from eleven out of the twenty-two registered Food and Beverage companies in Rivers State, Nigeria. The eleven companies were randomly selected. Well structured questionnaires were used to collect the required data from the selected companies. Two hundred and sixty (260) questionnaires were administered to the respondents. The data were analyzed using frequency distribution while the hypotheses were tested using the chi-square test.
Table 1: Responses Related to the Awareness of Tax Incentives.

<table>
<thead>
<tr>
<th>Questions</th>
<th>‘Yes’ Responses</th>
<th>%</th>
<th>‘No’ Response</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>246</td>
<td>96.85</td>
<td>8</td>
<td>3.15</td>
</tr>
<tr>
<td>2</td>
<td>246</td>
<td>96.85</td>
<td>8</td>
<td>3.15</td>
</tr>
</tbody>
</table>

Source: Field Survey 2010

The data in table 1 above can be analyzed as follows: To question 1, 246 representing 96.85% of the respondents are aware of tax incentives as it affects small scale industries. Meanwhile 8, representing 3.15% of the respondent are not aware of tax incentives. In response to question 2, 246 representing 96.85% of the respondents asserted that their companies do enjoy tax incentives currently. On the other hand 8 representing 3.15% of the respondents indicated otherwise. From the analysis above, one can conclude that most of the respondents are aware and familiar with tax incentives granted to small scale industries by government.

Table 2: Responses Related to the Effect of Tax Incentives on After Tax Profit of Small Scale Enterprises

<table>
<thead>
<tr>
<th>Questions</th>
<th>‘Yes’ Responses</th>
<th>%</th>
<th>‘No’ Response</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>3</td>
<td>220</td>
<td>86.61</td>
<td>34</td>
<td>13.39</td>
</tr>
<tr>
<td>4</td>
<td>200</td>
<td>78.74</td>
<td>54</td>
<td>21.26</td>
</tr>
</tbody>
</table>

Source: Field Survey 2010

The data in table 2 above can be analyzed as follows: To question 3, 220 representing 86.61% of the respondents agreed that tax incentives affect the after tax profits of small scale enterprises. Meanwhile, 34 representing 13.39% disagreed with this opinion. In response to question 4, 200 representing 78.74% of the respondents are of the opinion that tax incentives do enhance the level of after tax profits of small scale enterprises. On the other hand, 54 representing 21.26% of the respondents are of the opposite view. From the analysis above, one can conclude that tax incentives do enhance the level of after tax profits of small scale enterprises.

Table 3: Responses Related to the Effect of Tax Incentives on the Capital Employed of Small Scale Enterprises
The data in table 3 above can be analyzed as follows: To question 5, 200 representing 78.74% of the respondents are of the opinion that tax incentives do affect the capital employed of small scale industries. Meanwhile, 54 representing 21.26% of the respondents are of the contrary opinion. To question 6, 220 representing 86.61% of the respondents agreed that tax incentives lead to increase in the capital employed of small scale industries. On the other hand, 34 representing 13.39% do not agree with this opinion. From the analysis above, one can conclude that tax incentives do lead to increase in capital employed of small scale industries.

Table 4: Responses Related to the Relationship between Tax Incentives and Growth of Small Scale Enterprises

<table>
<thead>
<tr>
<th>Questions</th>
<th>‘Yes’ Responses</th>
<th>%</th>
<th>‘No’ Response</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>250</td>
<td>98.42</td>
<td>4</td>
<td>1.58</td>
</tr>
<tr>
<td>8</td>
<td>210</td>
<td>82.68</td>
<td>44</td>
<td>17.32</td>
</tr>
</tbody>
</table>

The data in table 4 above can be analyzed as follows: To question 7, 250 represent 98.42% of the respondents affirmed that there is relationship between tax incentives and the growth of small scale industries. Meanwhile 4 representing 1.58% disagreed. In response to question 8, 210 representing 82.68% of the respondents agreed that tax incentives encourage the growth of small scale industries. On the other hand, 44 representing 17.32% of the respondents are of the opposite opinion. Thus, it may be concluded that tax incentives do encourage the growth of small scale industries.
Table 5: Summary of Hypotheses tested

<table>
<thead>
<tr>
<th></th>
<th>Hypothesis 1</th>
<th>Hypothesis 2</th>
<th>Hypothesis 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Critical value</td>
<td>3.8415</td>
<td>3.8415</td>
<td>3.8415</td>
</tr>
<tr>
<td>$X^2$ Computed</td>
<td>5.4978</td>
<td>5.4978</td>
<td>36.8116</td>
</tr>
<tr>
<td>Degree of freedom</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Level of significance</td>
<td>0.05</td>
<td>0.05</td>
<td>0.05</td>
</tr>
</tbody>
</table>

**Discussion of Findings**

Table 5 above summarized the hypotheses tested. In the first hypothesis, the calculated $X^2$ value of 5.4978 is greater than the critical $X^2$ value of 3.8415 at 0.05 level of significance and 1 degree of freedom. Therefore, the calculated value is said to be significant and as such we will reject the null hypothesis of no significant effect of tax incentives on the after tax profits of small scale industries. Thus, the alternative hypothesis is accepted. This means that tax incentives do have significant effect on the after tax profits of small scale industries.

Similarly, in the second hypothesis, the calculated $X^2$ value of 5.4978 is greater than the critical $X^2$ value of 3.8415 at 0.05 levels of significance and 1 degree of freedom. Therefore, the null hypothesis is rejected while the alternative hypothesis is accepted. Thus, tax incentives do have significant effect on the capital employed of small scale industries. Finally, in the third hypothesis, the calculated $X^2$ value of 36.8116 is greater than the critical $X^2$ value of 3.8415 at 0.05 level of significance and 1 degree of freedom. Therefore, the null hypothesis is rejected while the alternative hypothesis is accepted. Thus, Tax incentives do enhance the growth of small scale enterprises.

**6.0 CONCLUSION AND RECOMMENDATIONS**

From the literature review, data analysis and discussion of the findings of this study, the conclusion is that tax incentives do have significant effect on the economic performance of small scale industries. Specifically, tax incentives help in improving the after tax profit and capital employed of small scale industries in Nigeria. Also
the following recommendations are made: First, government should periodically review the tax incentives available to small scale industries so as to reflect prevailing economic realities. Furthermore, the exemption from tax of the dividend of small scale industries for the first 5 years of operations should be extended to ten (10) years. This will further encourage more investments in the small scale industries. Finally, government should also grant five years unconditional tax holidays to small scale industries. This is very important if the government is to attract reasonable investments in the small scale industries.

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