THE ASSESSMENT OF THE IMPACT OF CAPITAL GAINS TAX ON ECONOMIC GROWTH IN NIGERIA

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ABSTRACT

The study assessed the impact of Capital Gain Tax on Economic growth in Nigeria. It also evaluated the significant components of Economic growth in Nigeria. Data were gotten from Central bank of Nigeria (CBN) Statistical Bulletin and Federal Inland Revenue service Bulletin from 2006 to 2015. Pearson product moment correlation and multiple regressions were employed to analyze the relationship between the dependent variable (Economic growth) and independent variables (Capital Gain Tax, Exchange rate and Inflation rate). Findings show that there is a positive significant impact of Capital Gains Tax on Economic growth in Nigeria (P>|t = 0.014; $p \le 0.05$) with the adjusted R^2 @ 60.3%. Also, Capital Gain Tax and Exchange rate have positive significant correlation 0.8547*; and 0.7830* respectively with Economic growth in Nigeria. In conclusion, Capital gain tax had positive significant impact on Economic growth but the level of significant is very low in Nigeria. It is now recommended that Government should increase the rate of Capital gain tax in Nigeria so that the revenue generated from this medium will be elevated in order to cater for the well being of the citizen in the country.

Key words: Capital Gains Tax; exchange rate; Inflation rate; GDP; Nigeria

INTRODUCTION

Nigeria is endowed with oil and gas with other mineral resources, but Nigeria depends on oil revenue for the achievement of microeconomic objectives like provision of employment opportunities, economic growth, economic stability, price stability, provision of infrastructural facilities, and optimum allocation of resources and fair distribution of wealth and income. Government is now based on the scavenging of the revenue from all avenues so as to fulfill the fiscal responsibility and to achieve microeconomic objectives of the government. Capital and Recurrent expenditure are now unsustainable to the state and federal government; this is due to the fluctuation in the oil market price which has posted threat, disharmony, harshness, ruggedness and austerity on Nigerian economy. Taxation has been nailed as one of the areas which generate revenue for the government apart from oil. Tax is a compulsory payment levied on all the incomes, goods, services, and properties of individuals, companies, partnerships, trustee and organisation by the government. Taxation is therefore, one among other means of revenue generation of any government to meet the need of the citizens.

According to Public Finance General Directorate (2009) the purpose of taxation as enshrined for the maintenance of public force and administrative expenses. Miller and Oats (2006) uphold that taxation is required to finance public expenditure. A good tax should have the qualities of Equitability, Efficiency, Neutrality, flexibility, and simple. These principles still holds today and even act as a guide for policy formulation (James and Nobes (2009). They noted further that the inability of tax policy to meet up with efficiency and equity criteria against which it is being judged. The central objective of the Nigerian tax system is to contribute to the well being of all Nigerians directly through improved policy formulation and indirectly though appropriate utilization of tax revenue generated for the benefit of the people. In generating revenue to achieve this goal, the tax system is expected to minimise distortion in the economy (Presidential Committee on National tax policy 2008). One of the components of tax which can generate revenues is capital gain tax. Capital gains are taxed only when the gains are realized by sale or exchange of assets, and gains on assets transferred at death are never taxed. Does this component of tax has positive significant impact on economic growth in Nigeria? This study examined effect of capital gain tax on economic growth in Nigeria from 2006 to 2015.

LITERATURE REVIEW

Capital Gain Tax in Nigeria

Capital gains tax (CGT) refers to a tax on capital gains, the profit realized on the sale of a non-inventory asset that was purchased at a cost amount that was lower than the amount realized on the sale (Wikipedia, 2016). The most common capital gains are realized from the sale of stocks, bonds, precious metals and property. According to Thomas (2010), capital gains are taxed as they are realized (that is, when the capital asset is sold or exchanged). Capital assets are property, but there are exceptions such as business inventory, accounts receivable acquired in the ordinary course of business, copyrights, and literary compositions. Capital gains are calculated by subtracting the asset's basis from the sales price. An asset's basis is the original purchase price adjusted for certain additions and deductions; it is not adjusted for inflation. If the basis is greater than the sales price then it is a capital loss. Taxes are charged by the state over the transactions, dividends and capital gains on the stock market. However, these fiscal obligations may vary from jurisdiction to jurisdiction (Wikipedia, 2016).

A capital gains tax is also a tax levied on capital gains incurred by individuals and corporations. Capital gains are the profits that an investor realizes when he or she sells the capital asset for a price that is higher than the purchase price. Capital gains taxes are only triggered when an asset is realized, not while it is held by an investor. An investor can own shares that appreciate every year, but the investor does not incur a capital gains tax on the shares until they are sold (Investopedia 2016). Capital Gains Tax is a tax on the profit obtained from a disposal or exchange of certain kinds of assets. In Nigeria, Capital Gains tax is 10% of the profits from the sale of the qualifying assets. It is recognized in law under the Capital Gains Tax Act while CGT is chargeable at 10 per cent on capital gains from the sale of capital assets (Nairametrics 2013).

Capital Gains Tax Act is under the management of the Board of The Federal Inland Revenue Service (FIRS) and it is administered by the FIRS in respect of corporate bodies and individuals resident in the Federal Capital Territory including members of armed forces, police and foreign serving officers. The tax is also administered by the State Internal Revenue Service in respect of individuals based on the rules of residence. Under the provisions of the Act, tax liability will arise on Actual Year Basis (AYB) when a chargeable asset is disposed. An aggrieved taxpayer or the respective tax authority can appeal against the decision of the tax authority to a conventional court or to the Tax Appeal Tribunal (TAT) as the case may be (Nneka2014)

CGT is chargeable at 10 per cent on capital gains from the sale of capital assets. Capital loss on disposal of any asset is not deductible from capital gains on disposal of any other asset even if both are of the same type. Where consideration is payable by installments over18 months, the chargeable gain shall be apportioned to the affected assessment years in proportion to the amount of the installments payable in each of the years (Nneka2014). Roll-over relief is available to any company acquiring a new asset to be used for the purposes of the trade in replacement of an old one. Gains arising from disposal of shares and stocks are currently exempted from CGT

Assets Exempted From Capital Gains Tax

According to Nairametrics (2013), the following assets are exempted from Capital Gains Tax

1. Gains on Stock, shares, and other government securities such as treasury bonds, premium bonds and savings certificates.
2. Ecclesiastical, charitable or educational institutions of a public character.
3. Any statutory or registered friendly society.
4. Any co-operative society registered under the Co-operative Societies Law of any State in the Federation of Nigeria.
5. Any trade union registered under the Trade Union Act.
6. Gains on a decoration awarded for gallantry conduct.
7. Gains accruing to statutory bodies.
8. Gains arising from acquisitions, mergers, or takeovers provided that no cash payment is made in respect of the shares acquired.
9. Gains on policies of assurance or deferred annuity unless the beneficiary is not the original Owner as in an estate.
10. Compensation for a wrong or injury of libel, slander, enticement, loss of office in a personal or professional capacity.
11. Gains from the main or only private residence of the individual provided that the area does not exceed one acre.
12. Gains on private vehicles.
13. Gains on any asset used for the purpose of a trade or business provided that the gain is used for replacing the old asset sold.
14. Gains from a provident or retirement benefit scheme.
15. Unit holders of a Unit Trust provided the proceeds are not reinvested.
16. Any diplomatic body

Effects of Capital Gains Tax on Economic Growth

Capital Gains may be defined as gains arising from increases in the market value of capital assets to a person or corporate body, who does not habitually offer them for sale and in whose hands they do not constitute stock-in- Trade. Therefore, it is a tax chargeable at the rate of 10 per cent on capital gains arising from the disposal of capital assets. Capital gains mainly represent the excess of disposal proceeds realised over the cost of the particular asset. A change in the capital gains tax rate may alter when a gain is realized without generally changing the total amount taken over time. The revenue estimators at the Treasury, the Joint Tax Committee of the Congress, and researchers at the Congressional Budget Office make some allowance for these short run timing and unlocking effects in their estimates. A permanent change in tax rates may also affect the holding period on assets, and alter the percent of accrued gains that are realized each year. In fact, added saving and investment would be undertaken economy-wide if the tax on capital gains and dividends were lower, rather than higher. A tax on capital income increases the "hurdle rate" of return or "service price" that an asset must earn to be worth investing in. These growth effects or macro-economic effects of cuts in the taxation of capital are not allowed for in the

revenue estimating process. These effects are large and certain, and dwarf the micro-economic effects that the tax estimators are willing to consider. Failure to account for them seriously biases the revenue estimates, and encourages bad tax policy (IRET 2009).

Capital gains taxes may create an additional level of taxation on successful entrepreneurs. Asymmetric taxation of capital gains and losses (in which gains are taxed more heavily than losses) may be an especially important issue for entrepreneurs; the asymmetries in the tax system may discourage entrepreneurs from taking risk (Pınar 2012). Lower and higher capital gains tax rates also affect the financial positions of household and corporations. When capital gains taxes are reduced, the after-tax return on equity rises, stock prices increase, household wealth is higher, some capital gains are realized, consumption increases, output and production rise, capital spending increases, household financial assets tend to rise, liabilities decline, debt service burdens are reduced, and household financial conditions improve(Pınar 2012).

Reducing capital gains taxes also causes realizations to rise as investors and business persons cash-in long-term capital gains. Consumer spending increases as capital gains realizations, after tax, are spent or saved. The rise in asset prices, both in the values of equity and residential real estate, is reflected in a stronger household balance sheet and reductions in debt because of increased income and capital gains realization (Pınar 2012). The amount of revenue raised by the higher tax rates on capital gains is uncertain because it depends on how realizations will respond to the higher tax rates. If realizations of gains fall substantially, little net revenue may be generated; realizations could even fall so far that revenue is lost under the higher rates. The more that a capital gains tax cut raises the return to savers and lowers the cost of capital to businesses, and the more that saving and investment respond to such changes, the more likely it is that such a tax cut will spur saving and investment and raise GNP. Reducing the taxation of capital gains could affect growth in several ways. Lower taxes on capital gains raise the real after-tax rate of return to savers, which may lower the cost of capital to businesses. When capital gains tax rates are raised, taxpayers may decide to defer taking gains or even to hold onto assets for as long as they live, passing the accrued gains to their beneficiaries tax free. A low capital gains tax rate has an important role to play in fostering economic growth and in promoting the entrepreneurial drive on which the Nigeria economy thrives.

Thomas(2010) signified that Capital gains tax reductions increase saving and investment, provide a short-term economic stimulus, and boost long-term economic growth. Capital gains tax rate reductions appear to decrease public saving and may have little or no effect on private saving. Consequently, many analysts note that capital gains tax reductions likely have a negative overall impact on national saving. Furthermore, capital gains tax rate reductions, they observe, are unlikely to have much effect on the long-term level of output or the path to the longrun level of output (i.e., economic growth). A tax reduction on capital gains would mostly benefit very high income taxpayers who are likely to save most of any tax reduction. A temporary capital gains tax reduction possibly could have a negative impact on short-term economic growth. Higher taxes on capital gains and dividends significantly harm the economy and job growth and suggest that the increase in federal tax receipts may not be a worthwhile tradeoff (Pınar 2012).

METHODOLOGY

The data were gotten from Central bank of Nigeria (CBN) Statistical Bulletin and Federal Inland Revenue service Bulletin from 2006 to 2015. This Model evaluated the impact of Capital gains tax on economic growth in Nigeria. Economic growth (proxied by GDP) is the dependent variable while capital gains tax, interest rate, exchange rate and inflation are independent variables. Regression Analysis technique was used to measure the effect of independent variables on dependent variable while Pearson Product Moment Correlation was used to measure the relationship between the dependent variable and independent variables.

MODEL SPECIFICATION

Economic growth (proxied by GDP) is the dependent variable while Capital Gains Tax, Interest rate, Exchange rate and Inflation are independent variables from 2006 to 2015.

$$GDP = f(CGT, INTR, INFL, EXCH, \mu) \quad 1$$

$$GDP = a_0 + a_1CGT + a_2INT + a_3INF + a_4EXCH + \mu \quad 2$$

Transformed to

$$LOGGDP = a_0 + a_1LOGCGT + a_2LOGINT + a_3LOGINF + a_4LOGEXCH + \mu \quad 3$$

$$r = \frac{n\Sigma wc.sf - \Sigma wc\Sigma sf}{\sqrt{(n\Sigma wc^2) - (\Sigma wc)^2} . \sqrt{(n\Sigma sf^2) - (\Sigma sf)^2}} \quad 4$$

Where n = no of observations
r = Coefficient of correlation showing the degree of relationship between the dependent variable and independent variable.

where

$LOGGDP$ - Log of Gross Domestic Product
$LOGCGT$ - Log of Capital Gain Tax
$LOGINT$ - Log of Interest rate
$LOGINF$ - Log of Inflation rate
$LOGEXCH$ - Log of exchange rate
μ - error term

RESULT AND DISCUSSION

The data collected from different reliable source like CBN Statistics Bulletin 2013 were analyzed below:

Table 1 Descriptive Analysis of the Significance of Components of Economic Growth

Variable	Obs	Mean	Std. Dev.	Minimum	Maximum
GDP	10	1.93e+08	2.72e+08	1.86e+07	6.72e+08
CAPTTAX	10	5924415	6961745	110460.8	1.68e+07
INTR	10	10.996	5.295439	5.62	24.4
INFL	10	10.042	2.560615	5.4	13.72
EXCH	10	150.549	23.42363	120.97	199

Source: Researchers' computation (2016) using STATA Version 11

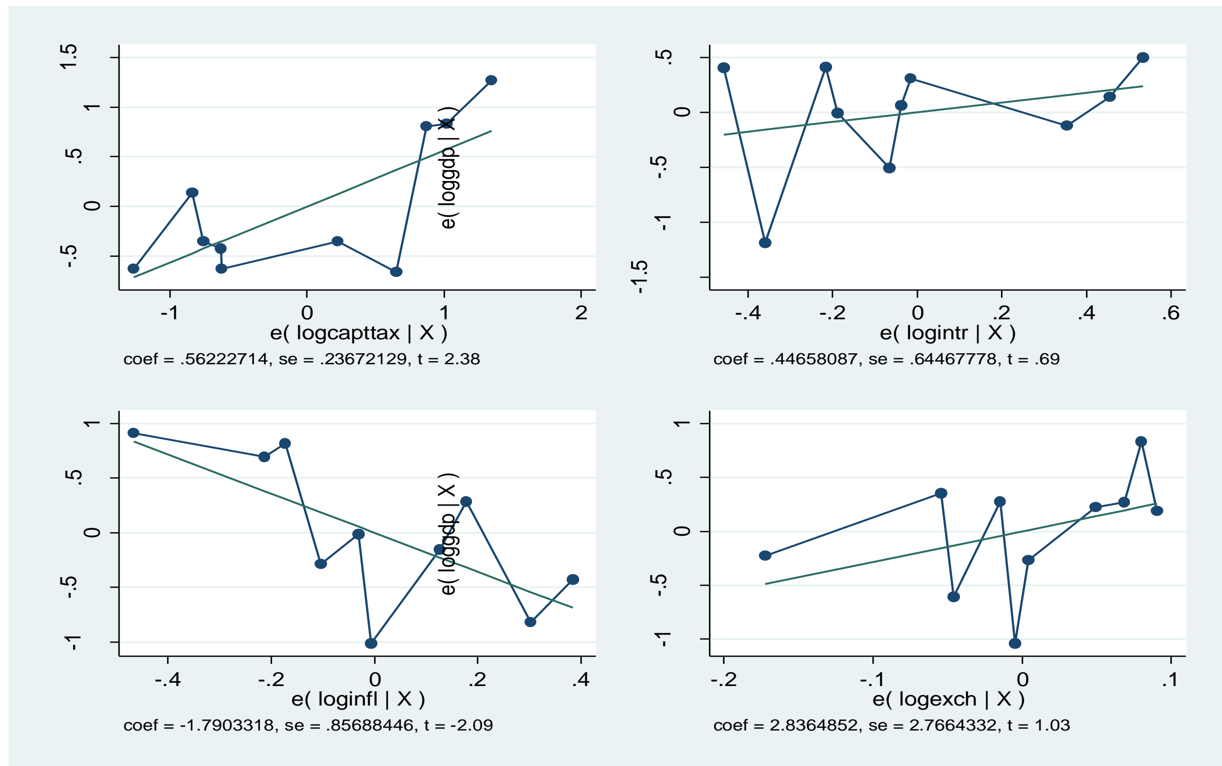
The descriptive statistics of the analysis is presented in Table 1 above shows that Economic growth as the dependent variable which had a mean value of 1.93e+08 with a standard deviation of 2.72e+08, it had a maximum value of 6.72e+08 and a minimum value of 1.86e+07. Capital Gain Tax had a mean of 5924415 and standard deviation of 6961745 with positive maximum and minimum value of 1.68e+07 and 110460.8 respectively, which signifies that for every 1% increase in Capital Gain Tax, Economic growth increases by 5.9%, this implies that there is a positive relationship between Economic growth and Capital Gains Tax. Also, Interest rate, exchange rate and inflation have the mean values of 10.996, 10.042, and 150.549 respectively with standard deviations of 5.295439, 2.560615, and 23.42363 with positive maximum values of 24.4, 13.72 and 199 with positive minimum values of 5.62, 5.4 and 120.97 respectively. This implies that for every 1% increase in Interest rate, exchange rate and inflation there will be an increase in Economic growth in Nigeria. It can be deduced from the analysis that there is a positive relationship between the dependent variables and the independent variables. Therefore, the null hypothesis is rejected and the alternative hypothesis is accepted that is there is a positive significant relationship between Capital Gains Tax and Economic growth in Nigeria.

Table 2: The Effect of Capital Gains Tax on Economic growth in Nigeria

Independent variable	Dependent variables	Coefficient	Standard Error	T	P>|t	[95%Conf. interval]
LOGGDP	LOGCAPTTAX	.5622271	.2367213	3.98	0.014	.0462843 1.170739
	LOGINTR	.4465809	.6446778	0.69	0.519	1.210616 2.103778
	LOGINFL	-1.790332	.8568845	2.99	0.021	3.993023 .4123598
	LOGEXCH	.8364850	2.766433	4.03	0.002	4.274858 9.947828
	constant	-1.353543	10.42698	8.13	0.000	-28.15696 25.44987
R-squared = 0.6909	Adj R-squared = 0.6036	Prob > F = 0.0007 Root MSE = .65818		F(4, 5) = 110.21		

Source: Researchers' computation (2016) using STATA Version 11

Figure 1- The above table is represented by regression plots below:



The table 2 above shows the effect of Capital Gains Tax on Economic growth in Nigeria. 1% increase in the Capital Gain Tax (LOGCAPTTAX) increases Economic growth (LOGGDP) by 0.5%. This suggests a positive effect of Capital Gain Tax on LOGGDP. The result is also significant (**P>|t** = 0.014; P < 0.05). 1% increase in interest rate (LOGINTR) increases LOGGDP by 0.44 %.This means that the relationship between LOGINTR and LOGGDP is positive suggesting that if LOGINTR increases LOGGDP also increases. Conversely, 1% increase in the Inflation rate (LOGINFL) reduces LOGGDP by 0.6%. This suggests a negative effect of LOGINFL on LOGGDP. The result is also significant. Furthermore, 1% increase in Exchange rate (LOGEXCH) increases LOGGDP by 0.8%. This reveals a positive significant effect of LOGEXCH on LOGGDP. This is suggesting that if LOGEXCH in Nigeria increases, LGGDP also increases.

Given R^2 as 0.6909 (69%) with the high value of adjusted R^2 as 60.3%, it signifies that the independent variables incorporated into this model were able to determine effect of capital gains tax on Economic growth by 60%.The F and probability statistics (Prob > F = 0.0007) also confirmed the significance of this model. From the decision rule above, because the p-value for the alternative hypothesis equals 0.0007 which is less than 0.05, therefore the null hypothesis is rejected while the alternative hypothesis is upheld, that is there is significant effect of Capital Gain Tax on Economic growth in Nigeria.

Table 3: The relationship between Capital Gains Tax and Economic Growth in Nigeria

	LOGGDP	LOGCAPTTAX	LOGINTR	LOGINFL	LOGEXCH
LOGGDP	1.0000				
LOGCAPTTAX	0.8547*	1.0000			
LOGINTR	0.5512	0.3787	1.0000		
LOGINFL	-0.1779	0.1746	-0.1718	1.0000	
LOGEXCH	0.7830*	0.8273*	0.4591	0.2454	1.0000

Source: Researchers' computation (2016) using STATA Version 11

The table 3 above shows the relationship between Capital Gains Tax and Economic growth in Nigeria. The result in table 3 shows that Capital Gain Tax (LOGCAPTTAX) has positive relationship with Economic growth (LOGGDP) with the value 0.8547*. Interest rate (LOGINTR) has positive insignificant relationship with Economic growth in Nigeria with the value of 0.5512. This result implies that an increase in Interest rate (LOGINTR) leads to increase in Economic growth in Nigeria. Also, Inflation rate (LOGINFL) has negative correlation with Economic growth in Nigeria. This result implies that an increase in Inflation rate (LOGINFL) reduces Economic growth in Nigeria. More so, Exchange rate (LOGEXCH) has positive significant relationship with Economic growth in Nigeria with the value of 0.7830*. The table also revealed that all the predictor variables have a positive relationship with Economic growth in Nigeria with the exception of Inflation rate.

SUMMARY AND CONCLUSION

This study examined the impact of Capital Gain Tax on Economic growth in Nigeria from 2006 to 2015.This study used multiple regression analysis technique and Pearson product moment correlation to measure the relationship between the dependent variable and independent variables. However, based on the analysis conducted, the result shows that, there is a positive effect of Capital Gain Tax on Economic growth in Nigeria. All other variables have positive effect on Economic growth in Nigeria with the exception of Inflation rate which has negative significant effect on Economic growth in Nigeria. It is also discovered that interest rate and inflation rate have insignificant relationship with economic growth in Nigeria. Capital gain tax and exchange rare have positive and significant correlation with economic growth; that is the more the Capital gain tax and exchange rate, the more will be improvement in the level of Economic growth in Nigeria. Conclusively, Capital gain tax had positive significant impact on Economic growth but the level of significant is very low in Nigeria.

It is now recommended that Government should increase the rate of Capital gain tax in Nigeria so that the revenue generated from this medium will be elevated in order to cater for the well being of the citizen and fulfill government fiscal responsibility in the country. Government should also adopt decisive mechanism in the mode of capital gain tax collection in order to inhibit the leakages so that the capital gain tax generated will not be siphoned to unscrupulous purse. By increasing the capital gains tax rate, tax revenues will also increase which will ultimately has an imperative role to play in fostering economic growth and in promoting the entrepreneurial drive on which the Nigeria economy will flourish.

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