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Public Governance Quality and Tax Compliance in Nigeria

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Abstract: The study examined the relationship between public governance quality and tax compliance in Nigeria. Specifically, the studyexamined the relationship between taxpayers' perception about public governance quality and their compliance behaviour in Nigeria; and to ascertain the relationship between financial condition and risk preference individually and jointlyamong taxpayers' perception about public governance quality and their compliance. This study involved a survey of individual taxpayers' opinions, perception and behaviour about public governance quality as well as tax compliance. The major finding revealed that public governance quality has a significant positive relationship with tax compliance behaviour in Nigeria. The study will also indicate that risk preference has a strong negative and moderating effect on the relationship between public governance quality and tax compliance behaviour. Administration of income tax in Nigeria is characterized by low compliance level and therefore, there is no doubt that improvement in public governance quality would contribute significantly to reawakening the culture of tax compliance among individual taxpayers in Nigeria.

INTRODUCTION

Financial resources with which government discharges its numerous responsibilities come in form of tax revenue and non-tax revenue. Alabede (2001) and Olaofe (2008) identified tax as the principal source of revenue to the government in some countries. Eshag (1983) however argued that the amount of tax revenue generated by the government for its expenditure programme depends among other things, on the willingness of the taxpayers to comply with the tax laws of a country. It is well accepted that some people do not like paying taxes and because of this reason, it is difficult for tax authorities to impose and collect taxes anywhere and time (Alm, Martinez-Vazquez & Schneider, 2003). The failure to oblige to tax provisions suggests that a taxpayer may be committing an act of noncompliance, (Kirchler, 2007). Franzoni (2000) stated that tax noncompliance is the most common and critical of all problems of tax administration.

Tax noncompliance is a universal phenomenon present in both developing and developed countries, (Chau& Leung, 2009; Goradichenko, MartinezVanzquez& Peter, 2009; McGee, 2006 and Tanzi&Shome, 1993). In developing countries, tax revenue loss as a result of noncompliance is proportionally greater than the amount in developed countries because of the presence of a large informal economy that is the hard-to-tax sector, (Terkper, 2003). The available statistic put the average tax revenue loss in developing countries too as much as between 35% and 55% of the Gross Domestic Product (GDP) in 2002,

However, over the past few decades, a growing amount of attention has been focused on the issue of tax compliance problems in the world, especially in developed countries. These general concerns have resulted in numerous empirical studies into the phenomenon. Most of the research studies have viewed the problem from the theoretical perspective of economic deterrence models, (RiahiBelkaou, 2004). The classical theory of tax compliance otherwise known as A-S models developed by Allingham and Sandmo in 1972 was based on Becker's (1968) deterrence theory. The theory assumes the taxpayer maximizes the expected utilities of the tax evasion gamble, balancing the benefits of successful cheating against the risky prospect of detection and punishment, (Sandmo, 2005). The general conclusion of this theory is that compliance depends largely on tax audits and penalties. The theory implies that taxpayers will pay taxes only because of the fear of sanction therefore more taxes will be paid with an increase in fine or audit rate.

OBJECTIVES

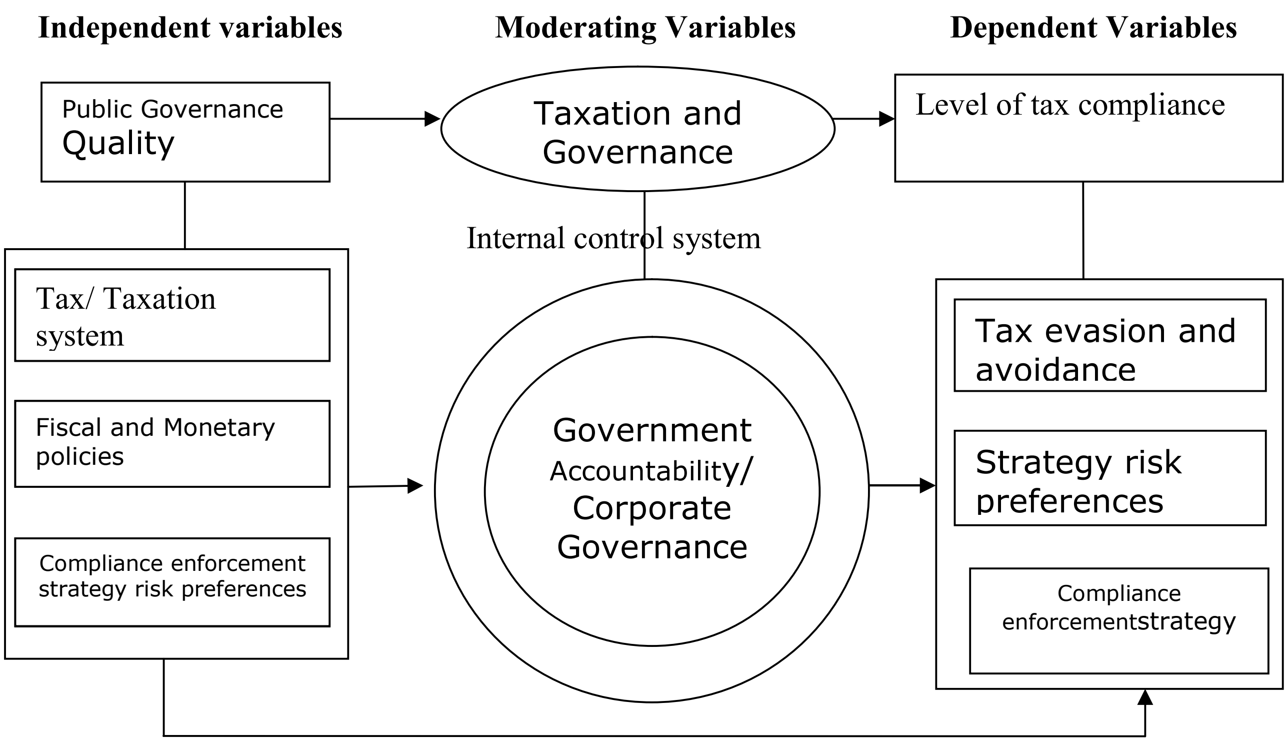
The purpose of this paper is to determine the relationship between public governance quality and the tax compliance behaviour of taxpayers in Nigeria.

Specifically, the study also sought to:

1. Examine the relationship between public governance quality and level of tax compliance.
2. To determine the qualitative strategies of public governance and its efficiencies to the tax compliance level.
3. Evaluate the income tax noncompliance in Nigeria and the moderating effect of public governance quality
4. Determine the relationship between the level of compliance and non-compliance of taxpayers in Nigeria.
5. Determine the relationship between the quality of public governance and the rate of tax evasion and tax avoidance.

The conceptual framework on the Public Governance Quality and Tax Compliance in Nigeria.

Is shown thus:



Source: Research Analysis2019.

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Tax Compliance Behavior in Nigeria.

Today, in Nigeria as the case with some developing countries, the administration of income tax is characterized by low compliance levels. Despite Nigeria's human

and natural endowment as well as economic potentiality, the country has continued to record one of the lowest tax compliance rates in Africa, (CITN, 2010). Even with all efforts through the various tax reforms undertaken by the Nigerian government to increase tax revenue over the years, statistical evidence has proved that the contribution of income taxes to the government's total revenue remained consistently low and is shrinking. However, of all the taxes, personal income tax has remained the most disappointing, nonperforming, unsatisfactory and problematic in the Nigerian tax system, (Asabe, 2005; Kiabel&Nwokah, 2009; Nzotta, 2007; Odusola, 2006; Sani, 2005). The statistical data indicated that contributions of non-oil income tax to total revenue of Government in Nigeria dropped from 19.8% in 1999 to 11.7% in 2008 and the tax ratio in 2009 was 11% the lowest in West Africa and below 15% recommended for low-income countries, (CBN,2008; Cobham,2005; ITN,2010). Specifically, the contribution of individual income tax remained marginal and comparatively low in Nigeria's tax revenue. At the state and local government levels, where the major source of internal revenue is expected to be individual income tax, its contribution to the total revenue of these levels dropped from20.18 and7.7% in 1999 to 12.4 and 1.6% in 2008 respectively (CBN, 2008). Although the low and the shrinking tax compliance level in Nigeria might be caused by a multitude of factors, the relevance of public governance quality cannot be underestimated, (Akpo,2009; Bird, &Zolt, 2005).

Some tax reforms in Nigeria include Structural Adjustment Program in 1986, Shehu's Task Force on Tax, 1978; Dr Sylvester's Study Group on Tax, 1999; Economic Empowering Development Strategies, 2002

Public Governance Quality and Tax Compliance

Public governance quality is an issue of general concernto citizens of nations as it bothers directly on benefits derivable from governance. World Bank (2006) views public governance quality as the process in which authority leaders are selected, monitored and replaced together with the capacity of the government of a country to manage the resources of a country effectively and implement sound policies for the benefit of everyone as well as the respect of the citizens and the government for the institutions that regulate economic and social interaction in the country. Rotberg (2005) also described public governance as the management, supply and delivery of political goods to the citizens of a country. To Besancon (2003) public governance exists to deliver political goods to the citizens and further stated that quality public governance is assumed when a country provides high order of certain political goods.

Taxation and Governance: The Historical Experience Historically, the formation of accountable and affective states has been closely bound up with the emergence of taxation systems (Moore, 2007). Evidence from Western Europe and later in North America show that equally beneficial arrangements between government and taxpayers help to give governments an incentive to promote broad economic prosperity and improve public policies in ways that meet citizens' demands. The OECD (2008) report on "governance, taxation and accountability" indicated that the recognition of the existing fiscal social contract was central to explanations of how representative government and democracy emerged in Western Europe and the United States. Citizens accepted obligations to pay tax in return for rights to be represented in processes of decision-making about how public money was raised and spent.

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Allingham and Sandmo (1972) in their proposition based on the economic perspective of tax compliance which provided a considerable basis for enforcement strategies to ensure compliance had argued that tax rate, penalty and detection probability are the factors influencing taxpayers' behaviour.

In addition, in line with the earlier submission of Alm, McClelland and Schulze (1992), Lassen (2003) said that the political goods mix is also important and declared that if the political goods mix supplied by the government is very different from those the taxpayers prefer or rate of transformation is low due to corruption, taxpayers may feel the attractiveness of the quid pro quo contract diminished and that could lead to lower tax compliance. Arguing in the same vein, Torgler (2003) said that when public governance quality is down, individuals' tax compliance may be crowded out since government fails to honour his honesty. Examining the relationship between public governance quality and compliance further, Everst-Philips and Sandall (2009) noted that there is a linkage between public governance quality and taxation and that quality governance deliver a good tax system and an equally better tax system make it possible to have good governance. Akpo (2009) equally stated that good governance entails the provision of quality public goods to the public and that where government fails to provide public amenities and infrastructure to the citizen in exchange for tax payment, a citizen may become reluctant to pay tax. Alm, *et al* (1992) also submitted that compliance occurs because people appreciate the political goods that their tax payments finance and that if there is an increase in the amount and quality of the political goods going to them from tax payment, their compliance rates may likely increase.

In their contribution, Joshua and Jinjarik (2005) theorized that greater polarization and political instability in a country would reduce the efficiency of tax collection hence lower compliance level. Damania, Fredriksson and Mani (2004) reported that in a politically stable country, there is a high degree of compliance with the regulation.

Compliance;

That taxation is the bedrock for states to fulfil their responsibility and ensure their continuity is an unarguable axiom. As Rakner and Gloppen (2002) notes for most countries taxation goes hand-in-hand with economic growth and taxes have become the lifeblood for governments to deliver essential services and to make long-term investments in public goods. The nexus between government accountability and voluntary tax compliance has emerged as a non-economic approach to modelling voluntary compliance based on the recognition that there exists a relational social contract between the state and the citizens. According to Baskaran and Bigsten (2010), the state's fiscal capacity is influenced by the strength ofthis social contract. The social contract is bounded and strengthened by accountability relations between parties involved.

Both authors argued that through payment of taxes the government is able to meet its obligations to the people. It follows therefore that how the government goes about fulfilling these obligations should matter to the taxpayers because they provide the finance for its sustenance. As a result, governance affairs may have either positive or negative influences on the tax morale of taxpayers. The tax function creates a relational vertical contract between government and taxpayers which Lassen (2003) defined as the expectation of requisite public goods in exchange for taxes paid as the terms of that vertical contract. According to the argument of quid pro quo, complying with tax law provision depends in part, on whether the political goods provided by the government are sufficient in return to the taxes they are paying. Levi (1988) argues that if it is perceived by the taxpayers that the rate of transformation from tax to public goods is low then the taxpayers will feel that the government has not kept its obligation of the contract, as a result, the tax morale will be affected

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negatively which would result in deteriorating voluntary compliance. Taxpayers are sensitive regarding the way the government uses the taxes and as such the tax morale may be represented as a reflection of an input-output relation between what an individual pays with his/her taxes and what comes back from the government. Thus, individuals' tax morale might be influenced by rationalizing the benefits received from the government in form of public goods with taxes paid. Individuals might feel cheated if taxes are not spent adequately which may result in tax morale being crowded out. Akpo (2009) equally stated that good governance entails the provision of quality public goods to the public and that where government fails to provide public amenities and infrastructure to the citizen in exchange for tax payment, a citizen may become reluctant to pay tax. The study of Alm and Gomez (2008) established a significant positive association between the perception of the benefits to be derived from political goods and the willingness of taxpayers to comply with tax laws. Natufe (2006) argued that Nigeria is experiencing a fundamental crisis in public governance. In a similar vein, Abati (2006) notes that the state of decay in Nigeria's public infrastructure and economic activity isa reflection of poor public governance quality and the low tax morale and voluntary compliance may have become the aftermath effect. Moore (1998) in explaining the weakness of tax-accountability relations in African countries, argued that aid and aid dependency has thwarted the development of a reciprocity based fiscal contract and the general governance accountability system. According to this perspective, the more states depend on unearned income the less accountable they will be towards their citizens and the more a state earns its income through the operation of a bureaucratic apparatus for tax collection, the more the state needs to enter into reciprocal arrangements with citizens about provisions of services and representation in exchange for tax contributions (OECD, 2008). In the light of the extant literature, the following hypotheses are stated for the study. H0: Voluntary tax compliance is not influenced by the individual's perception of Government accountability. H1: Voluntary tax compliance is influenced by the individual's perception of Government accountability.

Organizational Effectiveness and performance: This comprises the actual output or results of an organization as measured against its intended outputs (or goals and objectives).According to Richard *et al.* (2009), organizational performance encompasses three specific areas of firm outcomes: (a) financial performance (profits, return on assets, return on investment, etc.); (b) product-market performance (sales, market share, etc.); and (c) shareholder return (total shareholder return, economic value added, etc.)

In recent years, many organizations have attempted to manage organizational performance using the balanced scorecard methodology where performance is tracked and measured in multiple dimensions such as:

- financial performance (e.g. shareholder return)
- customer service
- social responsibility (e.g. corporate citizenship, community outreach)
- employee stewardship
- Organizational performance
- Performance measurement systems
- Performance improvement
- Organizational engineering

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Conclusion

This study expanded the basic tax compliance model to incorporate public governance quality and moderating effects of financial condition and risk preference. These new variables were carefully chosen to meet the environmental, situational and social reality in some developing countries particularly Nigeria. Indeed, the study has proved the suggestions of Alm (1999) and Jackson &Millron (1986) that other factors outside the basic model may influence tax compliance behaviour right. In the first place, the study has provided empirical support for the existence of a strong positive relationship between public governance quality and taxpayers' compliance behaviour and that taxpayers' risk preference also has a significant negative moderating effect on the relationship between public governance quality and tax compliance behaviour. Although the moderating effect of financial condition on the relationship between the two variables is positive as expected but not significant.

In the first place, the findings have proved that environmental, situational, social and cultural factors play important role in influencing tax compliance behaviour not only economic factors as assumed in deterrence theory. Public governance quality plays a vital role in shaping the compliance behaviour of individual taxpayers. Another distinctive contribution from this study is the transformation of the relationship between public governance quality and tax compliance from positive to negative significantly by the interacting effect of risk preference. Moreover, this provides proof to researchers that some other factors may have moderating effects on the relationship between tax compliance and its determinants as suggested in Kirchler et al (2007).

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