FOREIGN DIRECT INVESTMENTS AND TAX REFORMS: THE NIGERIAN EXPERIENCE (1990 – 2017)

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DEPARTMENT OF BANKING AND FINANCE

FACULTY OF BUSINESS ADMINISTRATION

UNIVERSITY OF NIGERIA

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A DISSERTATION SUBMITTED TO THE DEPARTMENT OF BANKING AND FINANCE, FACULTY OF BUSINESS ADMINISTRATION, UNIVERSITY OF NIGERIA, ENUGU CAMPUS IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTER OF SCIENCE (M.Sc.) IN BANKING AND FINANCE

SUPERVISOR: DR. E. CHUKE NWUDE

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APPROVAL

This Dissertation by ***Ohaegbulam Uche Kennedy***, a postgraduate student in the Department of Banking and Finance, Faculty of Business Administration, University of Nigeria Enugu Campus, with registration number **PG/M.Sc/11/60350** or the award of Master of Science in Banking and Finance, has been approved for the Department of Banking and Finance, Faculty of Business Administration, University of Nigeria, Enugu Campus.

BY

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Dr. E. Chuke Nwude **Date**

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DECLARATION

I, **Ohaegbulam Uche Kennedy**, a postgraduate student in the Department of Banking and Finance, Faculty of Business Administration, University of Nigeria, Enugu Campus with registration number ***PG/M.SC/11/60350*** carried out this research work on “Foreign Direct Investments And Tax Reforms: The Nigerian Experience (1990 – 2017)” in partial fulfillment of the requirements for the award of ***Master of Science in Finance.***

I hereby declare that the work embodied in this dissertation is original and has not been submitted in part or full for any other Diploma or Degree of this or any other University

Ohaegbulam, Uche Kennedy

PG/M.Sc/11/60350

Student

DEDICATION

This work is dedicated to the loving memory of my mother who though intelligent and very passionate never had the opportunity to get even the least of formal education which she so cherished.

Rest on, Mma!

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First and most importantly, I give all the GLORY TO GOD for His enabling Grace that made it possible for me to complete this work despite all odds.

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Finally, I wish to appreciate the management of Federal Inland Revenue Service (FIRS), my valued employer (nay, family), for the official permission granted me to undertake this programme and the great support received too.

ABSTRACT

This study examined the impact of recent tax reforms on Nigeria's foreign direct investment (FDI) net inflow from 1990-2017. Under the right policy environment, FDI encourages the transfer of economic productive technology and know-how between economies through spillover channels and linkages as is the case with China and the Asian Tigers. The drivers of FDI flow include policy factors such as taxation and non-policy factors like availability of natural resources, market openness and size. Nigeria FDI-experience presents a paradox as she has not had a fair share of the world's FDI flow despite her huge non-policy related potentials thus raising critical question on the role policy factors such as taxation may have played over the years especially since the country recently embarked on tax reforms. Despite the reforms, Nigeria Tax System still have complexities which appear to deter the critically needed FDI. There is therefore need to carry out a diagnosis of Nigeria tax system, the impact of the reform and what ought to be done for an impactful and sustainable FDI inflow. The study also derives justification from the apparent dearth of empirical works on the Nigeria FDI-Tax Nexus particularly with the use of Effective Corporate Tax Rate as the tax (independent) variable. The ordinary least square method of multiple regression analysis, at 5% Level of Significance was used to analyze the data and hypotheses proposed. The study employed annual time series secondary data spanning the years (1990-2017) sourced from the Central Bank of Nigeria Statistical Bulletins and the World Bank/PWC Annual Ease of Doing Business Survey Reports in carrying out its statistical analysis. Diagnostic test result showed that the variables were not stationary at same levels hence the use of the Autoregressive Distributed Lag (ARDL) method of Regression Analysis since it accommodates a combination of 1(1) and 1(0) variables. The result of the various analysis tallies with the apriori expectation that Recent (1990 – 2017) Tax Reforms in Nigeria though not effective have impacted positively and significantly on her FDI (Net Inflow). The study also found a marginal FDI-Tax Rate Elasticity of 0.2% indicating that for every one percentage point change in Nigeria's Effective Tax Rate, her FDI (Net Inflow) is affected by 0.2 per cent. This, the study ascertained as the elasticity or responsiveness of FDI to changes in Nigeria's Effective Corporate Tax Rate. This result is consistent with Alli (2015), Okoi and Edame (2013) and similar to Hartman (1984) which found out that tax rate elasticity for retained earnings is significant while for transfers the results are insignificant. The result is also particularly significant for this study which emphasizes the effect of taxation on not just the inflow of FDI but also its retention, hence the use of FDI (Net Inflow) as proxy for FDI variable. Moreso, as affirmed by this study and a recent World Bank Survey reports, investors are now more concerned with the predictability, certainty, simplicity, and the overall integrity of a tax system rather than just the tax rate hence the positive correlation and high coefficient of regression (0.195) between EPTD Index (a measure of investors' perception of tax systems) and FDI. This study strongly recommends that the Government of Nigeria should embark on a more drastic reform of her tax system in order to boost her FDI (Net Inflow). A continuous and concerted effort that yields the optimal balance between a tax regime that is simple, business friendly and one which can leverage enough revenue for public service, is what is urgently needed

Keywords*: Taxation, Foreign Direct Investment, Economic Growth, Tax Reform*

TABLE OF CONTENTS

LIST OF FIGURES

LIST OF TABLES

CHAPTER ONE

INTRODUCTION

1.1 BACKGROUND TO THE STUDY

In the words of Steinmo (1993), "Modern government needs lot of money for development. How they get it and from whom they get it are two of the most difficult political issues faced in any modern political economy". Governments the world over especially developing economies such as Nigeria hardly have sufficient funds to finance their economic growth and developmental needs, hence the need for private sector participation, particularly via foreign direct investment (FDI) what with its enormous benefits to the host economy. Several studies, for instance De Gregorio (2003), Carkovic and Levine (2002), Asiedu (2001); Obwona (2001), Sjoholeu (1999), Bende, Nabende and Ford (1998), Caves (1996), Egbo (2010), etc., as well as several World Bank, IMF, OECD and UNCTAD periodic trade and investment reports affirm that FDI is most preferred of all external financing means. It is now a common knowledge that foreign investment is indispensable for sustainable industrial development in most developing and poor countries of the world. This underscores the importance of a conducive global investment environment, characterized by open, transparent and non-discriminatory investment policies.

Although African countries have witnessed an increase in government revenue since the year 2000, these have been dominated largely by *resource rents* that are quite volatile and influenced heavily by fluctuations in international commodity *prices* (African Development Bank, 2015*)* Most countries of the world see attracting FDI as an important element in their quest and strategy for economic growth and development *OECD (2008).* This is because according to Olusanya (2013), FDI is seen as an amalgamation of capital, technology, marketing, and management – critical factors for meaningful economic development of any modern economy. This is in addition to the equity-based risk-sharing benefit of FDI finance.

Moreso, efforts by several African countries including Nigeria, to improve their business climate stem from the growing desire to attract FDI, *NEPAD (2009).* The importance of FDI to developing economies and Africa in particular is further substantiated by its prime recognition as a critical factor in the New Partnership for Africa's Development (NEPAD) Initiative. It is perceived to be a key resource for the translation of NEPAD's vision of growth and development into reality. This is because Africa like many other developing economic blocs needs a substantial inflow of external resources in order to fill the savings and financing gaps and thus leapfrog itself to substantial growth levels in order to eliminate its current pervasive poverty (NEPAD-OECD, 2009).

Unfortunately, the efforts of most countries in Africa to attract impactful FDI appear to yield little result contrary to the perceived and obvious need for FDI in the continent. The development is disturbing, sending very little hope of economic development and growth for African countries. Further, the pattern of the FDI that does exist is often skewed towards extractive industries, meaning that the differential rate of FDI inflow into sub-Saharan African countries has been adduced to be due to natural resources, although the size of the local market may also be a consideration, (Morisset, (2000); Asiedu (2001).

The high cost of accessing foreign debt financing as well as the stringent and near neocolonial conditions of foreign aids has made foreign direct investment increasingly attractive to developing countries most of whom are facing declining domestic investment and higher cost of foreign borrowing. Moreso, foreign direct investment seems an attractive form of capital inflow because it involves a risk-sharing relationship with the suppliers of this type of foreign fund. This kind of risk sharing does not exist in the formal contractual arrangements for foreign aid and borrowing (OECD, 2014). Furthermore, as the World Bank World Economic Outlook of May 1994 summed it: "Foreign Direct Investment is a large and growing source of finance that may help developing countries close the technology gap with the high-income countries, upgrade managerial and technical skills, and develop their export markets".

Emphasizing the immense importance of inbound FDI in modern economies, (OECD, 2008) Policy Brief that focused on "Tax effects on FDI", submitted as follows: "Given the enormous potential benefit of FDI inflow, policy makers and researches alike, continually re-examine their tax rules (via reforms) to ensure they are attractive to inbound Foreign Direct Investment" and optimal resource mobilization locally. For governments, tax reform is one important instrument to adapt to a changing international environment. In recent years, many countries have implemented tax reforms which reduce the effective tax burden on investment – both foreign and domestic investment with the added benefit of fostering domestic investments. Given that the border crossing mobility of capital and firms increases, it is reasonable to consider a reduction of the tax burden on domestic investment. But lowering the tax burden on investment necessarily implies a cut in public expenditure or a shift of the tax burden to other tax bases like e.g. labor or consumption. Sound tax policy has to carefully weigh the benefits of a corporate tax reduction to the economy as a whole against the cost

There appears to be a consensus in the literature about the main factors affecting foreign investment location decisions, see Dunning (1993); Globerman and Shapiro (2002); (2003); (OECD-MENA, 2010). The most important ones are market size, real income levels skill levels in the host economy, the availability of infrastructure and other resources that facilitate efficient specialization of product, trade policies, taxation and political and macroeconomic stability of the host country. The relative importance of the different factors varies - depending on the type of investment (OECD-MENA, 2007). This study focuses on the role of tax reforms in attracting FDI. Fundamentally, tax policy shapes the environment in which international trade and investment take place, (OECD, 2008). The ability to offer internationally competitive tax system is increasingly seen today as core factor influencing FDI, (OECD, 2003 & 2007). Thus a core challenge for African countries is finding the optimal balance between a tax regime that is business and investment friendly and one which can leverage enough revenue for public service delivery, which also enhances the attractiveness of the economy, (*NEPAD-OECD, 2009*). This is because investors routinely compare tax burdens in different locations, as do policy makers with comparisons typically made across countries that are similar in terms of location and market size (*UNCTAD, 2014).* A widely held view is that taxes are likely to matter more in choosing an investment location as non-tax barriers are removed and as national economies converge, *(OECD, 2008).* The paper further submitted that another factor is how business-friendly the tax administration is perceived to be because Investors look for certainty, predictability, consistency, transparency, simplicity and timeliness in the application of tax rules and in many cases these considerations are as important, if not more important than the statutory tax rate paid, *(OECD,2008).* The desire to tax MNEs and other foreign investors' income while not discouraging investors raises critical questions concerning the sensitivity of FDI to taxation and the appropriate setting of various tax provisions that determine the host country's tax burden and influence on investment and financing behavior, (OECD, 2008). Succinctly put, Tax competition for FDI is a reality in today's globalized world economy!

This study looks at the role of tax reforms on Nigeria Tax System and her potential to attract Foreign Direct Investment, in the light of her recent tax reforms. It focuses on the period 1990 - 2017. A period of time Nigeria tax system and by extension business environment has undergone seeming remarkable and unprecedented reforms as championed by the Federal Inland Revenue Service (FIRS) and successive democratic governments (especially since the return of democracy in 1999). The choice of the topic is particularly against the back drop that most economic reforms by sub-Saharan Africa countries and Nigeria, in particular, hardly have remarkable and sustainable effects, (World Bank, 2010) and the apparent dearth of research work in this area. Hence, effectively and extensively, this study is an attempt at measuring the extent of the on-going tax and general investment climate reforms in Nigeria as it relates to attracting and retaining FDI in her economy**.**

1.2 THE PROBLEM OF THE STUDY

Nigeria tax system despite the recent reforms still has complexities and which appear to deter domestic and foreign investments and offer loopholes for tax evasion, especially by MNEs. Nigeria tax revenue as a percentage of GDP has remained less than 7% compared to Sub-Sahara Africa average of 15%, European Union average of 35.7%, and OECD's 34.8%, *(OECD, 2014;* Bickersteth, 2016). The problem of this study derives from the fact that despite the numerous efforts (especially tax reforms) of the Nigerian government to improve on her business or investment climate as to attract FDI since the advent of democracy in the country in 1999, the gap between her investment need and the FDI response has remained very wide (UNCTAD, 2014; OECD, 2014). These efforts include improvements on her fiscal policy framework, repeal of old and moribund Laws, overhaul of her tax administration machinery, conclusion of bilateral investment and double taxation treaties, etc. Noteworthy, (African Development Bank, 2015); Alli (2015); Mukolu et.al. (2013); Ugwoke (2010); Egbo (2010), Oseghale & Amorchienan (1987); Akinlo (2004), have all confirmed a positive linkage between FDI and economic growth in Nigeria – hence the need to create attractive and motivating economic environment for it.

According to UNCTAD World Investment Report 2011, Nigeria falls below average in Africa and other developing economies when FDI inflows are adjusted to take into account the size of the domestic market and measured in terms of inflows per capita or per 1000 of GDP. It is curious why Nigeria is still largely by-passed by the current world FDI boom in spite of her highly encouraging credentials of being the biggest economy (by GDP) and largest market in the continent of Africa in addition to tax reforms to transform the political, regulatory, business and investment environment of the country

The main research question of the sensitivity of FDI to taxation is an inconclusive empirical issue (OECD, 2012). This is because of the variableness of previous empirical work, Mooij and Ederveen (2003 & 2005), Edozien (1968); Ugwoke (2012), (OECD, 2012 & 2014), Alli (2015) etc. Moreso, extant literature tend to suggest that the influence of tax on FDI is complex and depends on a number of difficult to measure factors, hence additional empirical works are required to better understand the role of taxation amongst key factors influencing FDI attraction or location decisions by investors, (UNCTAD, 2015).

1.3 OBJECTIVES OF THE STUDY

The main objective of this study is to examine the effect of taxation on Foreign Direct Investment inflow to Nigeria during the period (1990 – 2017), a period of time during which the country returned (in 1999) to her present democracy with its attendant conscious efforts to improve on the country's investment climate. It aims also to measure the impact of the ongoing major tax reforms anchored by the Federal Inland Revenue Service (***FIRS)*** – Nigeria's apex tax authority, implementation of which commenced in 2004. Therefore, the specific objectives of the study are to ascertain the:

1. Effect of FDI on the growth of Nigeria economy (1990 -2017)
2. Relationship between taxation and FDI
3. Impact of tax reforms (1990 – 2017) on Nigeria's FDI (Net-Inflow)

1.4 RESEARCH QUESTIONS

1. To what extent does the inflow of foreign direct investment affect economic growth in Nigeria (1990 – 2017)?
2. What is the extent of the relationship between taxation and FDI in Nigeria during the period (1990 - 2017)
3. What is the impact of recent tax reforms on Nigeria's FDI (Net-Inflow)?

1.5 RESEARCH HYPOTHESIS

1. FDI has no significant effect on the growth of Nigerian economy
2. There is negative correlation between taxation and FDI (Net Inflow) in Nigeria.
3. Tax Reforms do not have a significant positive effect on Nigeria's FDI (Net inflow).

1.6 SCOPE OF THE STUDY

The study covers the period 1990 to 2017. The choice of the period is due to the following reasons:

- This is a period that Nigeria economy experienced the most radical tax reforms ever.
- The present democratic dispensation with its attendant political and social stability and economic reforms began in 1999.
- Successive governments have embarked on a number of reforms and specific policies directed at improving the investment climate in the country since 1999.
- The choice of the period will also permit a comparison between FDI inflow in Nigeria pre 2005 (1990 – 2004) and post 2004 (2004 – 2017). This will serve to measure the nominal and real revenue-effects of the ongoing tax and other investment climate reforms on FDI inflow in Nigeria

  Moreso, the study concentrates on the effect of taxation on FDI inflow in Nigeria due to potential difficulty in sourcing reliable data for a panel study.

1.7 SIGNIFICANCE OF THE STUDY

- Nigeria government, tax authorities and other fiscal regulatory, as well as investment promotional agencies (such as NIPC) will benefit from the study as it aims to review Nigeria's present tax regime and the ongoing tax reforms in order to point out its deterrents/loopholes and proffer suggestions on the way forward .
- It will also specifically proffer solution to Nigeria's government on some policy guidelines and checklist for optimal fiscal incentive that will not only optimize tax revenue from MNEs but make our economy very FDI/Investment-Friendly.

- The study will go to contribute to growing body of literature on the Taxation-FDI nexus and particularly as it relates to Nigeria, on which much have not been written.

Again, its attempt to measure the effects so far, of the current major Nigeria tax reforms on FDI is unprecedented. This is particularly important what with the general believe that most sub-Sahara Africa countries (Nigeria inclusive) economic reforms hardly achieve the set economic goals or impact significantly on economic growth, (World Bank 2005 & 2010).

As expected, it is going to be significantly beneficial to policy makers, academia, tax administrators, foreign companies and the Nigeria economy in general.

1.8 LIMITATIONS OF THE STUDY

1. The study has to rely on a number of proxy representations of some of the variables for non-availability or difficulty in deriving or managing the large volume of data that doing otherwise would entail.
2. It is also limited to the use of secondary data by the envisaged difficulty in assessing and collecting primary data. MORESO, Time frame within which to carry out the study, given work and other socio-economic disruptions, was a limiting factor too.

3. As it is typical for this kind of research question, our data are of limited extent and of limited quality. Therefore we have to make some assumptions (using proxies) on which we base our confidence that we can use these limited data to answer our research question.

CHAPTER TWO

LITERATURE REVIEW

2.1 CONCEPTUAL REVIEW

Foreign Direct Investment (FDI) and taxation are critical components of development and their relationship have continued to attract attention. To what extent does Foreign Direct Investment (FDI) respond to international differences in tax regimes? How important are taxation regimes faced by MNEs for their location choices? According to Grubert (2004); and Altshuler and Grubert (2003), over the past decade, interest in these issues has been growing in parallel with the increasing mobility of capital and internationalization of business.

Foreign Direct Investment (FDI) is the net inflows of investment to acquire a lasting management interest control in an enterprise operating in an economy other than that of the investor. It is the sum total of equity capital, reinvested earnings, other long term capital and short term capital as shown in the balance of payments of national economies (IMF, OECD, World Bank Reports, 2012). According to Ugwoke (2010) the many studies that have been carried out on the subject matter ‘Foreign Direct Investment’ especially ‘the determinants of FDI” and “effects of taxation’ are clear indication of its immense importance in the development of economies globally. It is against this backdrop and the fact that a researcher cannot perform significant research without first understanding the literature in the field that we consider it indispensable to do a review of related literatures necessary for this study. De Mooij and Ederveen (2003) further buttressed the importance of literature reviews thus: “literature reviews usually implicitly assign more value to one study over another because quality typically differs among papers”. Hence we shall be concentrating on papers or works that have been adjudged high quality by notable researchers and international development/economic agencies. In this chapter we shall also carry out the conceptual background and theoretical framework of the work as well as an empirical review of earlier works on the Taxation-FDI Nexus.

2.1.1 Concepts of Investment

Investment can be defined in many ways according to different theories and principles. It is a term that can be used in a number of contexts. However, the different meanings of "investment" are more alike than dissimilar. Generally, investment is the application of money for earning more money. Investment is the utilization of resources in order to increase income or production output in the future. Simply put, investment is meant to create and preserve wealth. Although there are general broad definition to the term 'investment', it carries slightly different meanings to different sectors. On the other hand, in "finance", the practice of investment refers to the buying of a financial product such as stocks, bonds, etc or any valued item with anticipation that positive return will be received in the future**.** According to business theories, it is that activity in which a manufacturer buys a physical asset, for example stock production equipment in expectation that this will help the business to prosper in the long run.

John Keynes refers *investment* to as 'real investment', i.e., investment in the production of goods and services. For the purpose of this research work, the term 'investment' is used as commonly understood in business and refers to direct investment in productive assets. It is therefore taken to mean "the deployment, outlay of financial/economic resources in the production of new capital goods, plants and equipment, services, etc, i.e. real investment, (OECD,2009). In order words, Investment is the value of machinery, plants, and facilities that are bought by firms for production purposes. *Simply put, Investment is just new capital accumulation in business,* Piana (2001). It increases employment, production and economic growth of a nation thereby making a direct impact on employment generation, socio-economic enhancement, economic growth and development, etc., (Asiedu,2006). Investment has an immediate impact on GDP. It adds to the stock of capital, and the quality of capital available to an economy is a crucial determinant of its productivity. Investment thus contributes to economic growth and development. *It* also means a new capital accumulation in business and addition to gross domestic product (micro and macro economically speaking), (Libby,2014).

According to Piana (2001), investment plays six major macroeconomic roles:

1. It contributes to current demand of capital goods, thus it increases domestic expenditure;
2. It enlarges the production base (installed capital), increasing production capacity;

3. It modernizes production processes, improving cost effectiveness and efficiency.
4. It reduces the labour needs per unit of output, thus potentially achieving higher productivity and lower employment.
5. It allows for the production of new and improved products, increasing value added in production.
6. It incorporates international world class innovations and quality standards, bridging the gap with more advanced countries and helping exports and an active participation to international trade.

2.1.2 Major Determinants of Investment in an Economy

1. ***Interest Rate:*** Interest rate and investment has an inverse relationship. The higher the prevailing interest rate the lower the level of investment per time in an economy, and vice versa. Investment is inversely related to interest rates, which are the cost of borrowing and the reward to lending. Investment is inversely related to interest rates for two main reasons. Firstly, if interest rate rises, the opportunity cost of investment rises. This means that a rise in interest rates increases the return on funds deposited in an interest-bearing account, or from making a loan, which reduces the attractiveness of investment relative to lending. Hence, investment decisions may be postponed until interest rates return to lower levels. Secondly, if interest rates rise, firms may anticipate that consumers will reduce their spending, and the benefit of investing will be lost. Investing to expand requires that consumers at least maintain their current spending. Therefore, a predicted fall is likely to discourage firms from investing and force them to postpone their investment decisions.
2. ***Expectation***: A change in the capital stock changes future production capacity. Therefore, plans to change the capital stock depend crucially on expectations. As expectations change in a way that increases the expected return from investment, the investment demand curve shifts to the right. Similarly, expectation of reduced profitability shift the investment demand curve to the left. Because investment is a high-risk activity, general expectations about the future will influence a firm’s investment appraisal and eventual decision-making. Any indication of a down turn in the economy, a

possible change of government, war or a rise in oil or other commodity prices may reduce the expected benefit or increase the expected cost of investment.

3. ***The Level of Economic Activity***: Firms need capital to produce goods and services. An increase in the level of production is likely to boost demand for capital and thus lead to greater investment. Therefore, an increase in GDP is likely to shift the investment demand curve to the right.
4. ***The Expected Return on the Investment:*** Investment is a sacrifice, which involves taking risks. This means that businesses, entrepreneurs, and capital owners will require a return on their investment in order to cover this risk, and earn a reward. In terms of the whole economy, the amount of business profits is a good indication of the potential reward for investment.
5. ***Business Confidence:*** Similarly, changes in business confidence can have a considerable influence on investment decisions. Uncertainty about the future can reduce confidence, and means that firms may postpone their investment decisions until confidence returns**.**
6. ***Changes in National Income****:* Changes in national income create an accelerator effect. Economic theory suggests that, at the macro-economic level, small changes in national income can trigger much larger changes in investment levels.
7. ***Corporation Tax:*** Firms pay corporation tax on their profits, so a reduction in tax increases the profits they retain after tax is paid. This acts as an incentive to invest and vice versa.
8. ***The Level of Savings*****:** Household and corporate savings provides a flow of funds into the financial sector, which means that funds are available for investment. Increased savings may reduce interest rates and stimulate corporate borrowing and investment.
9. ***The Stock of Capital****:* The quantity of capital already in use affects the level of investment because most investment replaces capital that has depreciated. A greater capital stock is likely to lead to more investments; there will be more capital to replace.
10. ***Capacity Utilization****:* The capacity utilization rate measures the capital stock in use. If a large percentage of the current capital stock is being utilized, firms are more likely to

increase investment than they would if a large percentage of the capital stock were sitting idle. During recessions, the capacity utilization rate tends to fall and rises during expansion and these lead to decreased investment and increased investment respectively.

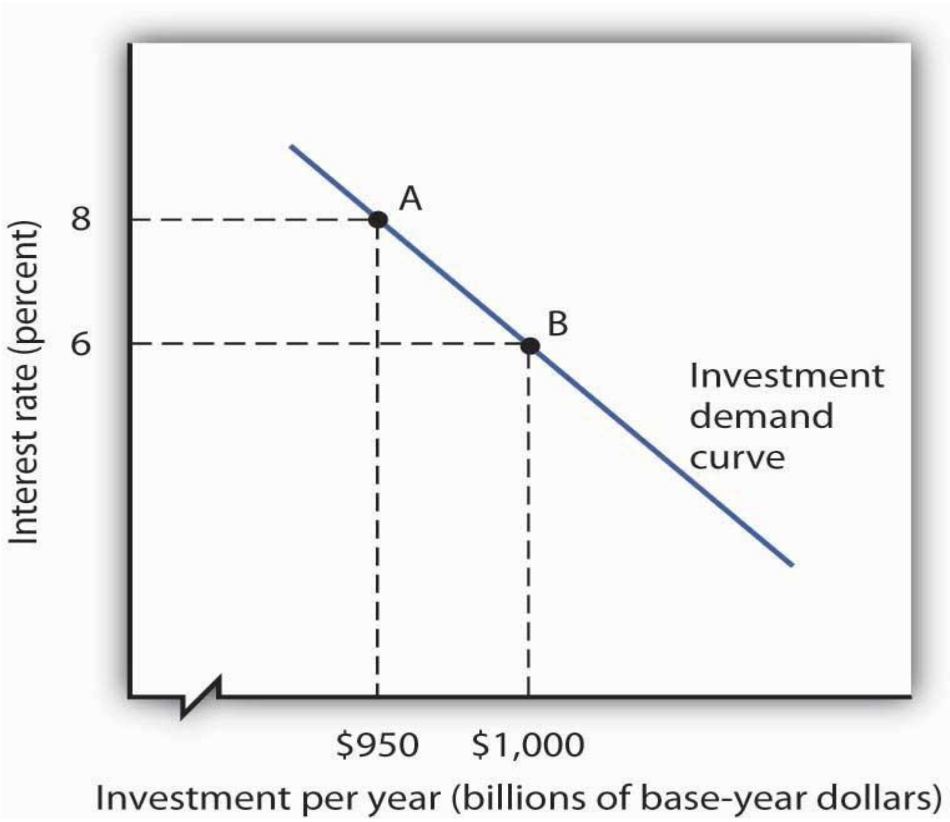
11. ***Cost of Capital Goods****:* If the actual money cost of capital goods, e.g. construction cost of new factories, rises, then the quantity of investment at any interest rate is likely to fall. This shifts the investment demand curve to the left.
12. ***Technological Change***: The implementation of new technology often requires new capital. Changes in technology can thus increase the demand for capital.
13. ***Public Policy*****:** Public policy such as taxation, subsidies, etc. can have significant effects on the demand for capital, Libby (2014).

Investment can be ***categorized*** into several forms and classifications but for the purpose of this study we shall have investment broadly (macro-economically) classified into.

- **Domestic Investment** – This refers to the totality of investments by both the private sector and public sector of an economy rather than those from foreign sources. It could be equity or portfolio in nature.
- **Foreign Investment** simply refers to inflows or investments from outside a nation's economy.

As expected our focus here shall be on foreign investment, especially, Foreign Direct Investment "**The Investment Demand Curve**" shows an investment demand curve for the economy—a curve that shows the quantity of investment demanded at each interest rate, with all other determinants of investment unchanged. At an interest rate of 8%, the level of investment is $950 billion per year at point A. At a lower interest rate of 6%, the investment demand curve shows that the quantity of investment demanded will rise to $1,000 billion per year at point B. A reduction in the interest rate thus causes a movement along the investment demand curve.

Figure 2 .1 The Investment Demand Curve



Source: www.economicsonline.co.uk

The investment demand curve shows the volume of investment spending per year at each interest rate, assuming all other determinants of investment are unchanged. The curve shows that as the interest rate falls, the level of investment per year rises. A reduction in the interest rate from 8% to 6%, for example, would increase investment from $950 billion to $1,000 billion per year, cateris paribus.

2.1.3 Historical and Conceptual Overview of Foreign Direct Investment

Foreign investment played a large role in international economy in the period leading into World War I. Prior to that, during the Victorian era, most of the world's surplus savings flowed from Western Europe to the developing countries of the time, which included some rapidly industrializing ones like the United States. Thus American railroads and canals were financed, at least in part, by European capital, especially United Kingdom's. The UK had accumulated huge savings surpluses from its early industrialization and these were exported around the world. At the same time, European portfolios also included the raw materials and agricultural output of what today is called the Third World. These would be extracted, processed and exported to the European market. Most of the foreign investments were in portfolio form and Great Britain, for instance, had more than 90% of its investment as such. Other major countries with portfolio investments include France and Germany. Exchange rates then were negligible and political situation stable. These international portfolio investments were then governed by interest rate differential. Young and fast growing economies, which offered high returns on capital, naturally attracted money from major leading countries. Most portfolio investors did not have controlling interest in the assets. Even where such investments were substantial, the investors did not muster enough interest in the operations of the organizations to acquire control. UK's dominance of world foreign investment was essentially brought to a dramatic end by a conspiracy amongst the First World War, the Great Depression, the Second World War, Decolonization and Third World Socialism. After 1945, global FDI flows did recover from depression and war, but the geographical pattern of foreign investment was completely transformed. In the postwar economic boom of 1945-80, most of the investment flows took place ***within*** and ***between*** developed countries in a phenomenon which has been labelled the ***Lucas Paradox***. Thus, basically, most — over 90% in 2001 — of the world's foreign investment positions represent rich countries owning one another's productive assets.

According the (OECD, 2002), the late 1980s and early 1990s did see an upswing in FDI flows into the Third World. And that is related to the debt crisis and in part to the insatiation of US investors who were eager to invest abroad due to prevalent portfolio investment interest rate differential then. As a direct outcome of the ***Washington Consensus***, in exchange for a combination of debt relief and financial assistance, the international financial community demanded that the debtor countries restructure their economies in fundamental ways, including privatization of state-owned assets, statutory protection of foreign investment, and the lifting of controls on the mobility of international capital. Thus, started in fitful steps, the return of investment in "emerging markets". However, the pattern of rich countries primarily investing in other rich countries has not gone away. That is still the predominant case, right now (2016). But the absolute level of foreign investment flows has burgeoned in the last 15 years for every country open to them. *We are nowhere near back to 1914 levels in most countries, but 25 years* *of neo-liberal prescriptions have definitely had a conspicuous effect on foreign direct investment in the Third World.* (OECD, 2002)

Uzoma (1998) submits that Foreign Direct Investment takes the form of a foreigner setting up a subsidiary or taking over control of an existing firm in another country thus internationalizing products in order to service markets hitherto served by export. International Monetary Fund (IMF, 2000), refers *Foreign Direct Investment (FDI) to as an investment made to acquire lasting or long term interest in enterprises operating outside of the country of the investor".* It is a long term investment of a "parent" enterprise from "home" economy into a subsidiary, affiliate, or branch enterprise in a foreign "host" economy. The investment is "direct" because the investor, which could be a foreign person, company or group of entities, is seeking to control, manage or have significant influence over the foreign enterprise. FDI flows include assets, property (e.g. parent company technology, branding, skills, etc) and or fresh capital investment (greater than 10% of total shares in a company), reinvested earnings (retained profits in affiliates, or intra company loan/debt transactions (long term borrowing/lending) between firms and affiliate enterprises, (IMF 2002). From the accounting perspective, FDI stocks are the value of capital and reserves (including retained profit) in a company's Balance Sheet attributable to a parent enterprise, Ugwoke (2010).

Furthermore, the third edition of the OECD Benchmark Definition of Foreign Direct Investment defines FDI as a category of int'l investment that reflects the objective of obtaining a lasting interest by an entity resident in one economy (the direct investor) in an another entity resident in an economy other than that of the investor (the direct investment enterprise). The lasting interest implies the existence of a long-term economic relationship between the direct investor and the direct investment enterprise, and a significant degree of influence by the investor on the management of the enterprise. It is also stressed in the OECD guide that direct investment involves both the initial transaction between the two entities and among affiliated enterprises. In both guidelines, ***direct investment ownership is conventionally set at a threshold of 10 percent (IMF 2002).*** In other words, a direct investor acquires 10 percent or more of the ordinary shares or voting power of an enterprise abroad.

According to the above OECD guide, once a direct investment relationship has been established, all subsequent capital transactions between the direct investor and the direct investment enterprises as well as capital transactions among affiliated enterprises residing in different economies are considered to be direct investment. The direct investment relationship is extended to certain other enterprises indirectly owned by the direct investor. Thus, direct investment comprises non-resident subsidiaries, associates and branches either directly or indirectly owned by the direct investor. The inclusion of transactions with and between indirectly owned entities can greatly extend the number of entities involved in the direct investment relationship and adds to complexity of compiling data.

As for the ***direct investor***, it is defined as an incorporated or unincorporated public or private enterprise, a government, a group or related individuals, or a group of related incorporated and/or unincorporated enterprises which has a direct investment enterprise that is, a subsidiary, associate or branch operating in a country or countries of residence of the foreign direct investor or investors.

There are a number of common ***misconceptions about what FDI is***, and hence it is worthy to be clarified as follows:

(i) FDI does not necessarily imply control of the enterprise, as only a 10 percent ownership is required to establish a direct investment relationship;

(ii) FDI does not comprise a group of “unrelated” investors domiciled in the same foreign country - FDI involves only one investor or a “related” group of investors;

(iii) FDI is not based on the nationality of the direct investor, it’s based only on residency; and

(iv) Borrowings from unrelated parties abroad that are guaranteed by direct investors are not FDI, Vong (2010).

2.1.4 Forms of Foreign Direct Investment

Foreign Direct Investment (FDI) has been boosted by increased mobility of factors of production globally, (IMF, 2000). The resultant ownership structure according to Carson (1979), include: **1)** ***Wholly Foreign-Owned Subsidiary***, which takes the form of either a branch or locally incorporated company. In a branch arrangement, the local branch conducts the local activities of its parent company without having a separate legal entity. The second arrangement allows a local incorporation with separate legal entity status from its foreign parent company and shareholders. This results to the formation of a wholly owned subsidiary company;

2) ***Joint Ventures***, which is a form of partnership between foreign investors and the host economy's investors in carrying out a business activity. The association occurs in varying degrees of sharing of control and decision making, risks and profits proportionally to the contribution of each party (unless otherwise stated). Technically, a joint venture can be either of corporate or contractual type. Under a corporate joint venture, sharing ownership through a separate legal entity as the association of both parties is based purely on contract. The rights and obligations will be governed by whatever is agreed upon in the contract, likewise the sharing of profit; risk, ownership of assets; control and decision-making (*provided of course, that the agreed terms are not in conflict with any laws and administrative policies of the host country*). Joint venture is at present an important vehicle for foreign participation in industrial ventures and remains the most common form used in developing countries of Asia, Africa and Latin America;

3) ***Special Contractual Arrangements***, which are similar to contractual joint ventures except that here, a foreign investor's share of benefit is determined by the negotiation of a fair return for his contribution, liability and risk rather than in, strict proportion to his contribution;

4) ***Technology, Management and Marketing Agreement***, whereby the host country's enterprise enters into a contract for the purchase of technology, management or marketing from a foreign enterprise for an agreed price. There is no sharing of control, decision-making, liability, risk and profit although the foreign partner runs the risk of non-payment in case of non-performance of the enterprise. The most prominent types of such business arrangement are *licensing agreements*. Examples include patent agreement, trade mark agreement, and franchise agreement, know-how agreement, other technical services agreement (e.g. engineering services agreements); management and marketing agreement). Usually, the extent of these agreements depend largely upon the specific sector or economic activity, the nature of technology and the level of domestic technological capabilities available;

5) ***Sub-contract, Co-production and Specialization Contract Agreement,*** which as opposed to joint ventures, are based on purely contractual arrangement and like the technology, marketing and management agreements do not involve sharing of control and decision making, liability, risk and profit. They differ from these forms of agreement in that the technology provided by the investor is only meant to supplement a purchase from the local entity or act as a joint effort by the foreign and local entity in production and/or marketing with no ownership or control consideration relating to the subject of joint effort.

2.1.5 Why Do Companies Go Abroad?

The "eclectic paradigm" attributed to Dunning as cited in Agwu (2014) provides a theoretical framework that groups micro and macro level determinants in order to analyze why and where multinational companies (MNCs) invest abroad. It states that firms invest abroad to look for three types of advantages: Ownership (O), Location (L), and Internalization (I) advantages; hence it is called the OLI framework. The *Ownership*-specific advantages of property rights/patents, expertise and other intangible assets) allow a firm to compete with others in the markets it serves regardless of the disadvantages of being foreign because it is able to have access to, and exploit and export natural resources and resource-based products that are available to it. These advantages may arise from the firm's ability to coordinate complementary activities such as manufacturing and distribution, and the ability to exploit differences between countries.

The Location advantages are those that make the chosen foreign country a more attractive site (such as labor advantages, natural resources, trade barriers that restrict imports, gains in trade costs and strategic advantages through intangible assets) for FDI than the others, hence the reason for the FDI is to supply the domestic market of the recipient country through an affiliate (horizontal FDI). The location advantages may arise from differences in coun try natural endowments, government regulations, transport cost, macroeconomic stability, and cultural factors.

Internalization advantages arise from exploiting imperfections in external markets, including reduction of uncertainty and transaction costs in order to generate knowledge more efficiently as well as the reduction of state-generated imperfections such as tariffs, foreign exchange controls, and subsidies (Campos & Kinoshita 2003). In this case, the delocalization of all or a portion of the production process (e.g. production of components/parts and/or different locations) leads to low costs benefits (vertical FDI).

Following on these, Dunning (199different locations) leads to low costs benefits (vertical FDI). Following on these, Dunning (1993) identified four categories of motives for FDI:

a. Resource seeking (to access raw materials, labor force, and physical infrastructure resources). Companies extracting oil (in Nigeria), gold (in Ghana) and diamond (in Botswana) belong to this category.
b. Market seeking (horizontal strategy to access the host-country's domestic markets) which aims to access new markets that are attractive as a result of their size and/or growth.
c. Efficiency seeking (vertical strategy which aims to take advantage of lower labor costs, especially in developing countries), the skills of the labour force, and the quality and efficiency of infrastructure, and
d. Strategic-Asset seeking (to access research and development, innovation, and advanced technology) Campos and Kinoshita (2003).

2.1.6 Benefits of Foreign Direct Investment

(i) ***Foreign Firms Bring In Scientific Technology and Superior Managerial Expertise***. They will provide technological assistance to their local suppliers or customers, and train workers who may subsequently move to local firms. In addition, local firms could learn by watching foreign counterparts. The extent of benefits to host economies depends on how well the technology can spill over to other firms in the local market. However, there appears a consensus in the literature to the effect that direct FDI spillovers depends on the host country's capacity to absorb the foreign technology and the type of investment climate.

(ii) ***Foreign investment steers up healthy competition in the host economy***. The entry of a new firm would tend to increase sectoral output and reduce the domestic price. In addition, the presence of foreign-owned firms may spur domestic firms to operate more efficiently and introduce new technologies earlier.

(iii) ***Foreign investment typically results in increased domestic investment***. Bosivorth and Collins (1999) found out in a panel data study of 58 developing countries (including Nigeria) that half of each dollar of capital inflow translates into an increase in domestic investment. However, when capital inflows take the form of FDI, there is a near one-to-one relationship between FDI and domestic investment.

(iv) ***Foreign investment gives advantages in terms of export market access,*** arising from economies of scale in marketing of foreign firms or from the ability to gain market access abroad.

(v) ***Foreign investment aid in bridging a host country's foreign exchange gap***. Investment often requires imported imparts. If domestic savings are insufficient to support capital accumulation to achieve a target growth, or barriers exist in converting domestic currencies into foreign exchange to acquire imports, foreign inflows can help ensure that foreign exchange will be available to purchase imports for investment.

2.1.7 Determinants of Foreign Direct Investment Flow

As observed in *Vong (2010)*, there are two sets of factors jointly affecting the level of Foreign Direct Investment:

i. **Non-policy** factors, for example, market size and potential, socio-geographical proximity and factor proportions (i.e. relative endowments of different inputs), security and political stability; and

ii. **Policy factors**, including taxation and other fiscal policies, market openness and infrastructure.

Table 2.1

Factors Influencing FDI	
Non-Tax Factors	- Market size - Access to raw materials, e.g. Natural resources, energy supplies - Availability and cost of skilled labour - Access to infrastructure - Transportation costs - Access to output markets, e.g. high consumer demand , low export costs - Political stability - Macro-economic stability - Financing costs
Tax Factors	- Transparency, simplicity, stability and certainty in the application of the tax laws and in tax administration - Tax Rates - Tax Incentives (fiscal, financial and other incentives such market incentives preferences

Source: OECD (2010)

Empirical findings in a recent survey of investors in South East Europe reports that strategic investors consider tax factors as only one of the obstacles to investment with instability and unpredictability of the tax system being perceived the key impediments, (OECD, 2010)

2.1.8 Recent Global FDI Trends

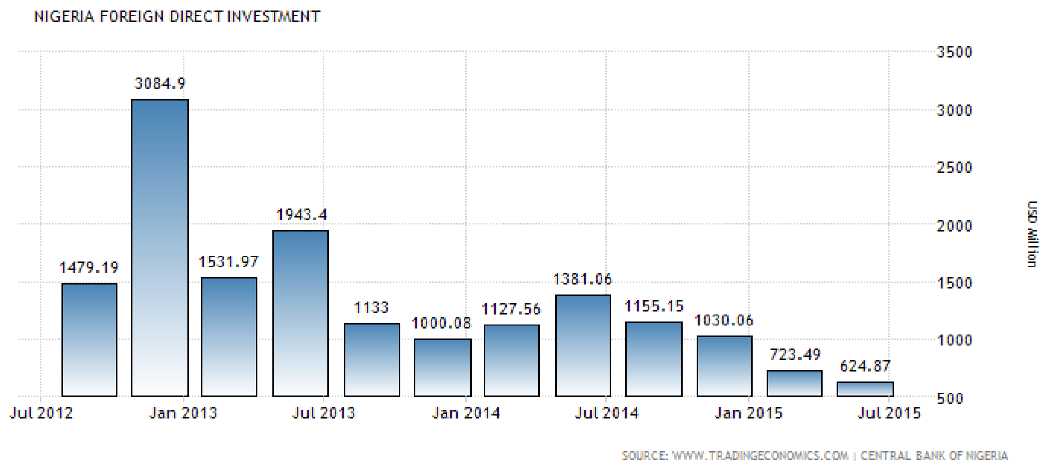
As highlighted in UNCTAD 2018 World Investment Report, global foreign direct investment (FDI) flows fell by 23 per cent to $1.43 trillion. This is in stark contrast to the accelerated growth in GDP and trade. The fall was caused in part by a 22 per cent decrease in the value of cross-border mergers and acquisitions (M&As). But even discounting the large one-off deals and corporate restructurings that inflated FDI numbers in 2016, the 2017 decline remained significant. The value of announced Greenfield investment – an indicator of future trends – also decreased by 14 per cent. FDI flows to developing economies remained stable at $671 billion, seeing no recovery following the 10 per cent drop in 2016. Cross-border investment in developed and transition economies dropped sharply, while growth was near zero in developing economies. With only a very modest recovery predicted for 2018, this negative trend is a long-term concern for policymakers worldwide, especially for developing countries, where international investment is indispensable for sustainable industrial development. This troubling global investment picture underscores the importance of a conducive global investment environment, characterized by open, transparent and non-discriminatory investment policies.

Global flows are forecast to increase marginally, by up to 10 per cent, but remain well below the average over the past 10 years. Higher economic growth projections, trade volumes and commodity prices would normally point to a larger potential increase in global FDI in 2018. However, risks are significant, and policy uncertainty abounds. Escalation and broadening of trade tensions could negatively affect investment in global value chains (GVCs). In addition, tax reforms in the United States and greater tax competition are likely to significantly affect global investment patterns, (UNCTAD, 2018).

After facing its lowest economic growth in over 20 years, Sub-Saharan Africa (SSA) posted a slow recovery in 2017. The International Monetary Fund (IMF) forecasts a modest rise in the region’s GDP growth from 2.8% in 2017 to 3.4% this year. FDI projects into Africa also rebounded from their lowest level in a decade. In 2017, Africa registered 6.2% growth in inward investment projects compared with 2016 and Africa's FDI is more evenly spread than ever before among each of the sub-regional groupings of West, North, South and East Africa, (Ernst and Young, 2018). Foreign investors committed to 718 FDI projects in Africa in 2017, a 6% increase from 2016. This brings us back to 2014 levels of FDI projects, but considerably below the 10 year average. Given the continent's economic recovery during the year, this was in line with expectations of FDI recovering in tandem with higher growth. The increase in FDI was aided by a continuing shift from extractive to sustainable investment. In addition, investors in Africa often take a long term view to investment. They recognize that low growth rates are not permanent. Moreover, given the more positive growth outlook until 2020, investors may be willing to invest more. Another factor that may have played a role in boosting FDI numbers in 2017 was sluggish growth environment by investing while currencies are weak and thus, gaining a cost advantage, (Ernst and Young, 2018).

Overview of Nigeria's FDI Economy and Recent Flows

Nigeria most important source of FDI have traditionally been the have countries of the oil majors. The USA, present in Nigeria's oil sector through Chevron/Texaco and Exxon Mobil, had investment stock of USD 3.4 billion in Nigeria in 2008, the latest figures available. The UK, one of the host countries of shell, is another key FDI partner – UK FDI into Nigeria accounts for about 20% of Nigeria's total foreign investment. As China seeks to expand its trade relationships with Africa, Nigeria is becoming one of China's second largest trading partner in Africa, next to South Africa from USD 3 billion in 2003, China's direct investment in Nigeria is reported to be worth around USD 7 billion in 2017. The oil and gas sector receives 75% of China FDI in Nigeria. Other significant sources of FDI include Italy, Brazil, the Netherlands, France and South Africa. An upsurge in FDI from South Africa is one of the most significant trends of the last decade. Nigeria is South Africa's third-largest trading partner in Africa (after Zimbabwe and Mozambique which benefit from regional trade agreements), and the largest in West Africa (Business in Africa, 2010). More than 20 South African companies are today present in Nigeria, in segments ranging from telecommunications, banking, mega retail outlets (e.g. Shoprite) and entertainment to revenue collection.



From the above, it is evident that Nigeria FDI inflow has been on the decline since 2013 when it rose to an unprecedented high amount of $3,084.9M and even declined further since the inauguration of the current regime of President Muhammadu Buhari. The recent economic recession experienced by Nigeria economy for four (4) consecutive quarters may have stemmed from it, if not vice versa. According to the 2018 UNCTAD World in-vestment report, Foreign Direct In-vestment (FDI) into West Africa declined by 11% to $11.3bn in 2017. The decline was underpinned by a drop in FDI flows into Ghana and Africa's largest economy, Nigeria. FDI into Nigeria declined sharply by 21.3% to $3.5bn, due to the nation's tepid growth recovery. The country's fragile growth weighed on business and investor confidence. Thus, foreign investors were reluctant to invest in the country. On a positive note, Nigeria's economic growth is forecast to continue to grow (2.1%) in 2018. Stronger and broad based economic growth is likely to drive an increase in FDI inflows.

2.1.9 Conceptual Overview of Taxation

Concepts and Essence of Taxation

By way of definition, '***taxation'*** is the inherent power of the state to impose and demand contribution upon persons, properties or rights for the purpose of generating revenue for public purposes. The recently revised National Tax Policy (NTP) 2016 of Nigeria defined ***'tax'*** *as any compulsory payment to government imposed by law without direct benefit or return of value or a service whether it is called a tax or not. It is undoubtedly a veritable instrument for national* *development.* Apart from being a major source of revenue for government to provide goods and services needed by the people, tax policies can stimulate economic growth and job creation through its impact on investment and capital formation in the economy. In this respect, reform of the tax system that ensures effectiveness, equity, and efficiency are necessary conditions for a healthy public finance. OECD see tax as compulsory unrequited payment to gener4al government. According to recently ***IFAC***-adopted ***IPSAS 23***, *'**taxes**' are economic benefits or service potential compulsorily paid or payable to public sector entities, in accordance with laws and or regulations, established to provide revenue to the government. Taxes do not include fines or other penalties imposed for breaches of the law. This we shall adopt as the working definition of 'taxes' in this work.* Though fines and penalties relating to a tax offence are a tax

Roles of Taxation

- Taxation has been an integral part of development policies or nations, interwoven with numerous other areas, from good governance and formalizing the economy, to spurring growth through, for example, promoting small and medium sized enterprises (SMEs) and stimulating export activities *OECD-NEPAD (2009).* Among other things, taxation:
    - Provides governments with the funding required to build the infrastructure on which economic development and growth are based;
    - Creates an environment in which business is conducted and wealth is created;
    - Shapes the way government activities are undertaken; and
    - Plays a central role in domestic resource mobilization.
    - Provide a stable and predictable fiscal environment to promote economic growth and investment;
    - Promote good governance and accountability by strengthening the relationship between government and citizens;
    - Ensure that the costs and benefits of development are fairly shared.

- Taxation provides a predictable and stable flow of revenue to finance development objectives. In fact, the 2002 Monterrey Consensus recognized taxation's key role in domestic resource mobilization, an acknowledgement sentiment echoed at the 2008 United Nations Doha conference on *Financing for Development*.

- Indeed, taxation shapes the environment in which international trade and investment take place. Certainty and consistency of tax treatment, the avoidance of double taxation, and efficient tax administration are all important considerations for business.

- But the role of taxation goes further than promoting economic growth. Tax evasion and the siphoning of funds to tax havens deprive African countries of the fiscal benefits of growth. The development of effective tax responses to counter these challenges is also central to Africa's development agenda, *OECD-NEPAD (2009)*

Tax Categorized

- **Direct Tax** is one levied directly on the person who is intended to pay the tax, e.g. personal income tax and company income tax whereas
- **Indirect Tax** is borne by a person other than the one from whom the tax is collected, e.g. VAT, Excise Duty, Import Duty, etc.

Attributes of a Good Tax System.

These are generally referred to as the ***four (4) Canons of Taxation***. *Adams Smith* in his classic book "*The wealth of Nations, 1776*" outlined the following canons or maxims of taxation.

1. Canon of Equity or Equality
2. Canon of certainty
3. Canon of economy
4. Canon of convenience.

Characteristics (Nature) of Tax

According to Donaven (2010), below are characteristics of tax

- *It's a sacrosanct civic responsibility* – for every citizen (both individuals and corporate) of a state, paying tax should be viewed as a sacrosanct civic obligation, almost akin to paying "tithe", that must be fulfilled!
- *It is an enforced contribution* - its payment is not voluntary nature
- *It is generally payable in cash,* i.e., promissory note or any of form of deferred payment and payment in kind are not allowed
- *It is proportionate in character* - payment of taxes should be based on the ability to pay principle; the higher the income of the taxpayer the bigger amount of the tax paid.
- *It is levied on person or property*.

- *It is levied by the state which has jurisdiction over the person*. As a general rule, only persons, properties, acts, rights or transactions within the jurisdiction of the taxing state are subject to taxation.
- *It is levied by the law making body of the state*. This means a prior law must be enacted first by the legislature before assessment and collection may be implemented.
- *It is levied for public purpose*. Taxes are imposed to support the government for

2.1.10 International Taxation

International Taxation is the determination of tax on income or profit of an individual or enterprise subject to the tax laws of different countries or the international aspects of an individual country's tax laws as the case may be. It is wrong though tempting to think that the term *"International taxation"* denotes the existence of a superior body that determine the interest of states when a transaction is subject to the taxing power of two or more states. The word *"international taxation"* denote taxation beyond domestic or national sphere. The essence of international taxation is the issue of whether and to what extent a country can exercise its taxing power over an individual or company who is subject to two or more national Tax Law. The crux of the matter is the division of the tax revenue among countries for the purpose of avoiding tax avoidance and double taxation. This is the aspect of taxation that concerns FDI.

As a matter of international convention and common practice, governments usually limit the scope of their income taxation in some manner territorially or provide for offsets to taxation relating to extraterritorial income. The manner of limitation generally takes the form of a territorial, residence-based, or exclusionary system. Some governments have attempted to mitigate the differing limitations of each of these three broad systems by enacting a hybrid system with characteristics of two or more. Countries that tax income generally use one of two systems: territorial or residence-based. In the territorial system, only local income – income from a source inside the country – is taxed. In the residence-based system, residents of the country are taxed on their worldwide (local and foreign) income, while nonresidents are taxed only on their local income. In addition, a very small number of countries, notably the United States, also tax their nonresident citizens on worldwide income. Countries with a residence-based system of taxation usually allow deductions or credits for the tax that residents already pay to other countries on their foreign income. Many countries also sign tax treaties with each other to eliminate or reduce double taxation. In the case of corporate income tax, some countries allow an exclusion or deferment of specific items of foreign income from the base of taxation. Jurisdictions that tax income on a residency basis need to define "resident" and characterize the income of nonresidents. Such definitions vary by country and type of taxpayer, but usually involve the location of the person's main home and number of days the person is physically present in the country. On the other hand, Territorial systems usually tax local income regardless of the residence of the taxpayer. The key problem argued for this type of system is the ability to avoid taxation on portable income by moving it outside of the country. This has led governments to enact hybrid systems to recover lost revenue

The world of international tax is constantly changing. Policies change, taxpayers modify their behavior, laws change, new double tax agreements are concluded, existing ones are amended, and administrative practice is improved. With any system of taxation, it is possible to shift or re-characterize income in a manner that reduces taxation. Jurisdictions often impose rules relating to shifting income among commonly controlled parties, often referred to as transfer pricing rules. Residency-based systems are subject to taxpayer attempts to defer recognition of income through use of related parties. A few jurisdictions impose rules limiting such deferral ("anti-deferral" regimes). Deferral is also specifically authorized by some governments for particular social purposes or other grounds. Agreements among governments (treaties) often attempt to determine who should be entitled to tax what. Most tax treaties provide for at least a skeleton mechanism for resolution of disputes between the parties.

Basic Principles of International Taxation and Issues

Below are different principles which are operative under international taxation:

Tax Systems

Taxing systems differ amongst states with their own peculiarities. Every country exercise taxing power and guard this power jealously. Tax systems often come in contact with each other when a person engages in cross border transaction which make such income generated from such transaction liable to tax in two or more countries where the transaction has link with. This gave rise to International Taxation.

Tax Jurisdiction

This deal with who has jurisdiction over the Tax. In dealing this, the question is whether it is *Source base approach* or *Residence base approach* that is adopted. Under a source based approach, the source country is entitled to tax the income of both residents and non-residents which is earned within its territory. Source country is the country in which the income is derived from. However under *Residence based approach*, a country assert jurisdiction to tax the worldwide income of its residents. The question of whether the income is earn within its territory is irrelevant. Nigeria adopt the residence base approach as Nigerian income whether earned in Nigeria or not is subject to paying tax on such income. Only Eritrea and United State of America tax its non-resident citizens on their foreign income.

Multinational Companies (MNCs)

Multinational companies are one of those who in most times are subject to international law issue. Multinational companies controls about 70% of the world economy. They are basically interested in making income for themselves and their shareholders and prefer if possible not to be liable to any tax liability whatsoever. Their allegiance is to their shareholders and not any country in which their business is connected to. They try to reduce their tax liability by using some tax avoidance techniques such as transfer pricing, artificial transaction, transferring their businesses to countries which are regarded as tax haven.

International Double Taxation

International businesses are often faced with issues of double taxation. Income may be taxed in the country where it is earned, and then taxed again when it is repatriated in the business' home country. In some cases, the total tax rate is so high, it makes international business too expensive to pursue. To avoid these issues, countries around the world have signed hundreds of treaties for the avoidance of double taxation, often based on models provided by the Organization for Economic Cooperation and Development (OECD). In these treaties, signatory nations agree to limit their taxation of international business in an effort to augment trade between the two countries and avoid double taxation.

The Use of Treaties

Treaties are bi-lateral agreement between Countries as regards transaction or issues affecting both countries. These treaties provide for how much two countries are prepared to forego taxing rights that would be available under domestic laws, with a view to avoiding double taxation, preventing tax evasion and avoidance, and encouraging investment. Many countries have entered into bilateral treaties with other countries referred to as Double Tax Treaties which aim to define which country a taxpayer will be consider to be a resident for tax purpose and how tax are to be divided between countries having the right to tax. Countries can enter a tax treaty to determine how their tax system would work together so as to ensure that residents of each countries get the double tax relief they are entitled to and prevent hardship on their citizens when their transaction move beyond their own country. Nigeria has a double tax treaties with United Kingdom, China, Germany, amongst others. A treaty can only come into force after it has been ratified by each member state .Each state has its different method for ratifying treaties in their individual domestic Law. In Nigeria, SECTION 12 of the 1999 Constitution of the Federal Republic of Nigeria provide that before a treaty can become binding in Nigeria, it must have been passed as Law by the National Assembly. The position was applied in the case of SANI ABACHA V. CHIEF GANI FAWEHINMI, Where the court held that Nigeria is not bound any international treaty until and unless it has been domesticated and passed as Law by the National Assembly.

The Role of OECD and United Nations:

One of the most active organization in the field of international taxation is the Organization for Economic Co-operation and Development (OECD). One of its aim is to promote trade between its member states. An important facet of its work is to assist in removing barrier to trade posed by taxation issue. Its convention and guideline is not binding on any country but is usually used as a guidelines for bi-lateral treaties. Some has argued that the guideline provided by the OECD favoured the developed countries than the developing or under-developed countries. This lead to United Nations providing its own guidelines for issue of international taxation which had been said to favoured both the developing and under developed states. One major advantage of OECD model is that it provide a valuable tool of interpretation which is of international acceptance. Under the OECD model convention which is the model Nigeria used for its bilateral treaty agreement with other countries, the basis for taxation is "permanent establishment". Article 5 of the OECD model, permanent establishment means a fixed place of business or an established business at a distinct place with a degree of permanence.

Thin Capitalization and Transfer Pricing

An enterprise is considered operating with thin capitalization where the size of paid up capital base is considered "low /small/thin" compare with the size of its operations- (turnover). Most jurisdictions are of the opinion that taxable income may be reduced by amount expended as interest on loans, in a situation where an enterprise finances its subsidiary enterprises through loans rather than capital. ***Transfer Pricing*** refers to the rules and methods for pricing transactions within and between enterprises under common ownership or control. Transfer price is the price at which divisions of a company transact with each other, such as the trade of supplies or labor between departments. Transfer prices are used when individual entities of a larger multi-entity firm are treated and measured as separately run entities.. Nigeria's TP Regulations were released in October 2012 and applicable to basis (accounting) periods commencing after August 2012. For example, a company with an accounting year end date of 31st December 2012 will be required to have its TP documentation in place for the accounting year commencing 1st January 2013 for returns to be filed by June 2014.

Tax Sparing Concept

This is a provision in tax treaties that seeks to protect the tax incentives which the government grants to companies as part of the economic development strategy. The intention of government is that the benefits would accrue to the targeted investor. But without a tax-sparing provision in a bilateral agreement, such benefit would be captured by the tax policy of the investor's country of residence. The income which the government has spared through its incentive legislations may thereby flow, not to the investor directly, but to the government of the country of the investor's residence.

Basis of Taxing Rights in International Taxation

There are two major taxing rights commonly at the disposal of a country;

- **Source Principle of Taxation** : The country may tax the income having its source in that country, regardless of the residence of the taxpayer
- **Residence Principle of Taxation**;

The country has taxing rights over the taxpayer where such tax payer (individual or enterprise) is a resident.

Domestic Tax Laws and Foreign Revenue Law

It should be noted as a general principle, that only the domestic tax laws of a sovereign country are applicable and enforceable within that country. In this regard Article 28 of OECD and United Nations Model Tax Convention titled – *Assistance in the Collection of Taxes* Should not be misconstrued as enforcement of foreign revenue law.

2.1.11 World Bank/PWC Annual Ease of Paying Taxes Index

Now in its 13th edition, *Paying Taxes* continues to be a unique study from PwC and the World Bank Group, which investigates and compares tax regimes across 190 economies worldwide using a medium-sized domestic case study company. Ease of Paying Taxes Index is one of the 10 indices the World Bank uses to access the *Doing Business* or *Investment Climate of over 190* Member Nations of the institution. It has come to be recognized as the highest rating of tax systems worldwide. The ease of doing business ranking compares economies with one another; the distance to frontier score benchmarks economies with respect to regulatory best practice, showing the absolute distance to the best performance on each *Doing Business* indicator.

Paying Taxes Methodology

Doing Business' Ease of Paying Taxes Index records the taxes and mandatory contributions that a medium-size company must pay in a given year as well as measures of the administrative burden of paying taxes and contributions and complying with post-filing procedures. The project was developed and implemented by the WorldBank in cooperation with PwC. Taxes and contributions measured include the profit or corporate income tax, social contributions and labor taxes paid by the employer, property taxes, property transfer taxes, dividend tax, capital gains tax, financial transactions tax, waste collection taxes, vehicle and road taxes, and any other small taxes or fees. *Doing Business* focuses on a case study for a standardized medium- size local company.

The ranking of economies on the ease of paying taxes is determined by sorting their scores for paying taxes. These scores are the simple average of the scores for each of the component indicators *(time, number of payments, and total tax rate)* with a threshold and a nonlinear transformation applied to one of the component indicators, *the total tax rate*. The threshold is defined as the total tax rate at the 15th percentile of the overall distribution for all years included in the analysis up to and including *Doing*. All economies with a total tax and contribution rate below this threshold receive the same score as the economy at the threshold.

The threshold is not based on any economic theory of an "optimal tax rate" that minimizes distortions or maximizes efficiency in an economy's overall tax system. Instead, it is mainly empirical in nature, set at the lower end of the distribution of tax rates levied on medium-size enterprises in the manufacturing sector as observed through the paying taxes indicators. This reduces the bias in the total tax and contribution rate indicator toward economies that do not need to levy significant taxes on companies like the *Doing Business* standardized case study company because they raise public revenue in other ways—for example, through taxes on foreign companies, through taxes on sectors other than manufacturing or from natural resources (all of which are outside the scope of the methodology).

Doing Business measures all taxes and contributions that are government mandated (at any level—federal, state or local) and that apply to the standardized business and have an impact in its financial statements. In doing so, *Doing Business* goes beyond the traditional definition of a tax. As defined for the purposes of government national accounts, taxes include only compulsory, unrequited payments to general government. *Doing Business* departs from this definition because it measures imposed charges that affect business accounts, not government accounts**.** One main difference relates to labor contributions. Value Added Taxes (VAT) are generally excluded (provided that they are not irrecoverable) because they do not affect the accounting profits of the business—that is, they are not reflected in the income statement. They are, however, included for the purpose of the compliance measures (time and payments), as they add to the burden of complying with the tax system.

Doing Business uses a case scenario to measure the taxes and contributions paid by a standardized business and the complexity of an economy's tax compliance system. This case scenario uses a set of financial statements and assumptions about the transactions made over the course of the year. In each economy tax experts from a number of different firms (in many economies including *PwC)* compute the taxes and mandatory contributions due in their jurisdiction based on the standardized case study facts. Information is also compiled on the frequency of filing and payments, the time taken to comply with tax laws in an economy, the time taken to request and process a VAT/Tax refund claim and the time taken to comply with and complete a corporate income tax correction. To make the data comparable across economies, several assumptions about the business and the taxes and contributions are used.

Tax Payments: The tax payments indicator reflects the total number of taxes and contributions paid, the method of payment, the frequency of payment, the frequency of filing and the number of agencies involved for the standardized case study company during the second year of operation. It includes taxes withheld by the company, such as sales tax, VAT and employee-borne labor taxes. These taxes are traditionally collected by the company from the consumer/employee on behalf of the tax agencies. Although they do not affect the income statements of the company, they add to the administrative burden of complying with the tax system and so are included in the tax payments measure.

Time: Time is recorded in hours per year. The indicator measures the time taken to prepare, file and pay three major types of taxes and contributions: the corporate income tax, value added or sales tax, and labor taxes, including payroll taxes and social contributions. Preparation time includes the time to collect all information necessary to compute the tax payable and to calculate the amount payable. If separate accounting books must be kept for tax purposes—or separate calculations made—the time associated with these processes is included. This extra time is included only if the regular accounting work is not enough to fulfill the tax accounting requirements. Filing time includes the time to complete all necessary tax return forms and file the relevant returns at the tax authority. Payment time considers the hours needed to make the payment online or in person. Where taxes and contributions are paid in person, the time includes delays while waiting.

Total Tax and Contribution Rate

The total tax and contribution rate measures the amount of taxes and mandatory contributions borne by the business in the second year of operation, expressed as a share of commercial profit. *Doing Business 2019* reports the total tax and contribution rate for calendar year 2017. The total amount of taxes and contributions borne is the sum of all the different taxes and contributions payable after accounting for allowable deductions and exemptions. The taxes withheld (such as personal income tax) or collected by the company and remitted to the tax authorities (such as

VAT, sales tax or goods and service tax) but not borne by the company are excluded. The total tax and contribution rate is designed to provide a comprehensive measure of the cost of all the taxes a business bears. It differs from the statutory tax rate, which merely provides the factor to be applied to the tax base. In computing the total tax and contribution rate, the actual tax or contribution payable is divided by commercial profit.

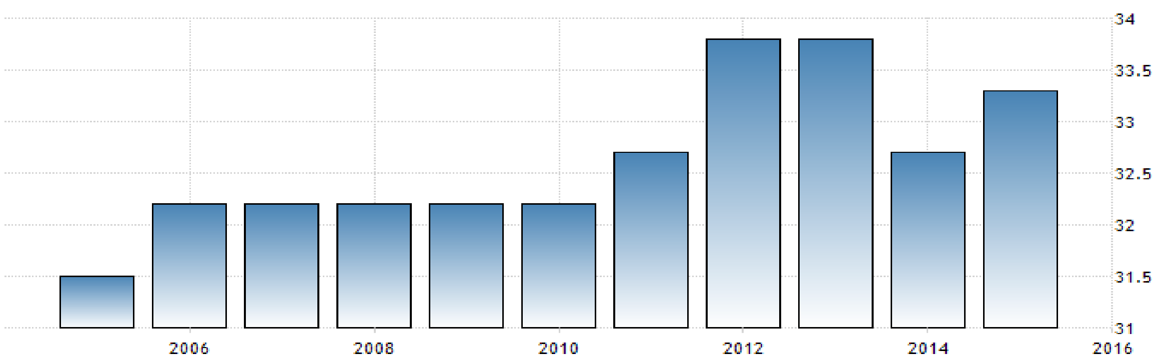
The Distance to Frontier methodology of the Doing Business Index

This measure illustrates the distance of an economy to the "frontier," and the change in the measure over time shows the extent to which the economy has closed this gap. The frontier is a score derived from the most efficient practice or highest score achieved on each of the component indicators (payments, time and Total Tax Rate) by any economy since 2004. Calculating the distance to frontier score for each economy involves two main steps. In the first step individual component indicators are normalized to a common unit where each of the 41 component indicators *y* (except for the total tax rate) is rescaled using the linear transformation *(worst–y)/(worst–frontier)*. In this formulation the frontier represents the best performance on the indicator across all economies since 2005 or the third year in which data for the indicator were collected. For the total tax rate, consistent with the use of a threshold in calculating the rankings on this indicator, the frontier is defined as the total tax rate at the 15th percentile of the overall distribution for all years included in the analysis up to the current year of assessment. For the time to pay taxes the frontier is defined as the lowest time recorded among all economies that levy the three major taxes: profit tax, labor taxes and mandatory contributions, and value added tax (VAT) or sales tax. An economy's distance to frontier score is indicated on a scale from 0 to 100, where 0 represents the worst performance and 100 the frontier.

Table 2.4. NIGERIA'S COMPARATIVE WORLD BANK 'DOING BUSINESS' INDEX

Topics	DB 2016 DTF (% points)	DB 2015 DTF (% points)	Change in DTF (% points)
Starting a Business	78.90	78.63	**0.27**
Dealing with Construction Permits	42.35	42.35	No change
Getting Electricity	30.61	30.48	**0.13**
Registering Property	29.86	21.74	**8.12**
Getting Credit	60.00	60.00	No change
Protecting Minority Investors	68.33	63.33	**5.00**
Paying Taxes	32.17	32.62	**-0.45**
Trading Across Borders	18.05	18.05	No change
Enforcing Contracts	49.34	49.34	No change
Resolving Insolvency	30.68	30.64	**0.04**
Starting a Business	71.20	70.91	**0.29**
Dealing with Construction Permits	73.92	73.74	**0.18**
Getting Electricity	31.91	31.79	**0.12**
Registering Property	36.70	36.69	
Getting Credit	60.00	60.00	No change
Protecting Minority Investors	68.33	63.33	**5.00**
Paying Taxes	32.18	32.63	**-0.45**

Figure 2.4 Nigeria Total Tax Rate (% of Profit)



Source: World Bank Doing Business Data Bank

2.1.12 Conceptual Overview of Tax Reforms

The impact of taxation on macroeconomic variables have been well noted by several studies and books. Apart from revenue generation, taxation is often utilized to create both economic incentive and disincentive effects. It is usually employed to enhance desirable investment and production activities through lower tax rates/burden and discourage socially undesirable activities through high tax rates. High tax rate distort the demand and supply of labour, leading to impairment of productivity. Hence, taxation is a veritable tool that could be used to influence savings behaviour, labor supply, education, investments and productivity. Taxation is dynamic, so reforms are necessary to effect the required changes or adjustments in the tax system. According to *Oriakhi and Rolle (2014)*, the theoretical foundation of tax reforms emanates from the ***'supply-siders'.*** These are sets of Economist who had their hay days between 1970 and early 1980s. The supply-siders believed in the use of economic incentives to encourage production. They opined that higher marginal tax rate will not only create disincentive to work, savings and investment but encourages tax avoidance and evasion that reduces public revenue. The leader of the group Arthur B. Laffer, using what is today known as the *Laffer Curve* showed that there is an optimum tax rate that both encourages savings, investment and labour supply, and at the same time motivate tax payment obligation. Thus, tax rate in excess of the optimum rate will be harmful to economic activities. The recommendations of the supply-siders became a major debate in the Washington Consensus during the 90's. Their recommendations were generously patronized by Ronald Reagan's Administration in USA. Indeed, tax reform became an increasingly important element of adjustment programme in LDCs and massively supported by WorldBank and IMF. The essence of tax reform in both developing and developed countries of the world is the reduction or eradication of fiscal deficits through appropriate restructuring of the tax systems to attract higher revenues or to improve the revenue elasticity or buoyancy of the tax structure.

Tax reform is therefore a deliberate design to increase revenue, improve efficiency, and promote equity (World Bank, 1991) as well as achieve other macroeconomic objective of policy makers in an economy. Tax reform is generally undertaken to improve the efficiency of tax administration and to maximize the economic and social benefits that can be achieved through the tax system, Fjeldstad (2014). Tax reform is an ongoing process which policy makers and tax administrators continually adopt in the tax systems to reflect changing economies, social and political circumstances in the economy. Tax reform can reduce tax evasion and avoidance, and allow for more efficient and fair tax collection that can finance public goods and services and as well attract and sustain foreign investments. It can make revenue levels more sustainable and promote future independence from foreign aid and finite natural resource revenue. Tax reform measures are undertaken to strengthen modern taxes and drastically reduce the complexity and lack of transparency of the system (Oriakhi & Rolle, 2014; Odusola, 2006; Anyanwu, 1997).

Dimensions/Approaches to Tax Reforms:

- ***Institutional Approach*** of tax reforms involve the semi-autonomous revenue authority model, where traditional line departments are separated from the ministry of finance and granted legal status of semi-autonomous revenue authorities. Tax reform involves broad issues of economic policy as well as specific problems of tax structure design and administration (Musgrave, 1987). The establishment of semi-autonomous revenue authorities (ARAs) has been a widely noted tax administrative innovation during the last two decades, Fjeldstad (2014). Currently, there are more than 30 semi-ARAs in the developing world, of which 21 are in Sub-Sahara Africa (as at 2017-End). During the last decade, multilateral institutions and increasing number of bilateral developing agencies have provided technical assistance ad aid to tax administrations in developing countries. And they have been at the fore-front of support for ARAs. The choice of the revenue authority model aims to remove the revenue collection function partly or fully from the direct control of the Ministry of Finance by integrating tax operations that were previously conducted by different departments into a single-purpose agency, and to free the tax administration from the constraints of the civil service system. It is assumed that the revenue authority model will be less vulnerable to political interventions in its operations. This shift to a semi-ARA model has also been attractive to donors and senior politicians because it opens opportunities for more widespread reforms of tax administration. This reform has also brought about shift in the tax administrations' attitudes towards taxpayers. 'Customer service' and 'user-friendliness' have become the norm.

- ***Optimal Tax Reform Approach***.

  Under this theory, it is required that the best way to raise revenue is through taxing goods or factors with inelastic demand or supply, and that taxation relating to distribution and externalities or market failures should concentrate on identifying the source or origin of the problem. Thus for distribution, one should look for the sources of inequality (for example, land endowments or earned in comes) and taxation should be concentrated there. Regarding externalities, an attempt should be made to tax or subsidize directly the good or activity that produces the externality *Stern (1988)*. Employing the optimal tax reform theory, *Newbery and Stern (1987)* applied a normative framework to analyze the tax reform process. The optimal taxation approach according to them emphasizes the need to analyze the impact of tax reform and evaluate both its administrative costs and its effects on social welfare. The major problem of this approach is that it required substantial data which are difficult to source in developing countries. In addition, optimal taxation assume the existence of perfect tax administration, which do not exist in Nigeria and several developing countries.

As highlighted in World Bank (2017), the following approaches in taxation reforms currently trends globally:

- Introduction of the value-added tax;
- Lower personal and corporate income taxes
- Broadening of the tax bases
- Reduction of import duties and simplification of the rate structure;
- Abolition of export taxes, and
- Avoiding excessive reliance on special tax incentives for investors.

2.1.13 Nigerian Tax System

The Nigeria tax system, like any other tax system in the world, is a tripartite structure which comprises of: *Tax Policy, Tax Legislation and Tax Administration.* Tax policy forms the basis for tax laws while tax administration is the implementation of the tax laws. This shows that in a bid to establish an effective and efficient tax system that will make taxation the pivot for national development, appropriate tax policies and legislations should be put in place and adequately implemented. Under current Nigerian law, taxation is enforced by the 3 tiers of government, i.e.

federal, state, and local governments, with each having its sphere clearly spelt out in the Taxes and Levies (approved list for Collection) Decree, 1998. Despite this improvement, there are still a number of contentious issues that require urgent attention and among them is the issue of the appropriate tax authority to administer several taxes.

Guiding Principles of Nigeria Tax System

As highlighted in the recently (2016) revised National Tax Policy of Nigeria, all existing and future taxes are expected to align with the following fundamental features:

Equity and Fairness: Nigeria tax system should be fair and equitable - devoid of discrimination. Taxpayers should be required to pay according to their ability.

Simplicity, Certainty and Clarity: Tax laws and administrative processes should be simple, clear and easy to understand.

Low Compliance Cost: The financial and economic cost of compliance to the taxpayer should be kept to the barest minimum.

Low Cost of Administration: Tax Administration in Nigeria should be efficient and cost-effective in line with international best practices.

Flexibility: Taxation should be flexible and dynamic to respond to changing circumstances in the economy in a manner that does not retard economic activities.

Sustainability: The tax system should promote sustainable revenue, economic growth and development. There should be a synergy between tax policies and other economic policies of government.

Challenges of Nigeria Tax System

Despite the potentials of taxation as a dynamic tool for sustainable national development, Nigeria tax system has been unable to achieve its objectives due to the following challenges, among others as highlighted in the recently revised Nigeria Tax Policy:

- the need to grow internally generated revenue which has led to the arbitrary exercise of taxing powers;
- lack of clarity on taxation powers of each level of government and encroachment on the powers of one level of government by another;

- insufficient information available to taxpayers on tax compliance requirements thus creating uncertainty and non-compliance;
- poor accountability for tax revenue;
- problem of multiple taxes and double taxation
- insufficient capacity which has led to the delegation of powers of revenue officials to third parties, thereby creating complications in the tax system;
- use of aggressive and unorthodox methods for tax collection;
- failure by tax authorities to honor refund obligations to taxpayers;
- the non-regular review of tax legislation, which has led to obsolete laws that do not reflect current economic realities; and
- lack of strict adherence to tax policy direction and procedural guidelines for the operation of the various tax authorities.
- Pervasive corruption among tax officials
- Weak capacity due to a shortage of skilled staff and the lack of modern infrastructure such as IT systems and property registers.
- Nigeria also face taxation challenges due to the large size of her agriculture sector,
- Small tax base and high degree of informality.
- Tax reform is often difficult due to interest groups who benefit from the current system.

Nigeria's National Tax Policy

The National Tax Policy is a document which sets broad parameters for taxation and ancillary matters connected with taxation. It is a clear statement on the principles governing tax administration and revenue collection. It therefore, provides a set of guidelines, rules and modus operandi that would regulate taxation in Nigeria.

Tax Legislation

Tax law is a codified system of order that describes the legal implications of taxation, i.e. government levies on economic transactions.

- Tax laws provide a well-defined legal backing to the administration of each tax type
- States in clear terms the applicable rate,
- Tax laws stipulate what constitutes offence and the appropriate sanctions to each offence.
- They enshrine best practices in terms of ethical and professional conduct.

Major Tax Laws in Force in Nigeria

- Federal Inland Revenue Service (Establishment) Act No. 13 of 2007

- Companies Income Tax Act (CITA) CAP C21 LFN, 2004 (commencement1st Jan, 1958)
- Personal Income Tax Act (PITA) CAP 8 LFN, 2011 (as amended)
- Petroleum Profits Tax Act (PPTA) CAP 13 LFN, 2004 (commencement 1Jan, 1958)
- Deep Offshore and Inland Basin Production Sharing Contracts Act
- Value Added Tax Act (VATA) CAP D1 LFN, 2004 (commencement 1Dec,1993)
- Education Tax Act CAP E4 LFN, 2004 (commencement 1Jan, 1993)
- Capital Gains Tax Act (CGT) CAP C1 LFN, 2004 (commencement1st,April,1967)
- Stamp Duties Act CAP S8 LFN, 2004 (commencement 1April, 1939)
- National Information Technology Development Agency Act (NITDA)
- Industrial Development (Income Tax Relief) Act

Tax Administration in Nigeria

Tax administration is the process of assessing and collecting taxes from taxable individuals and companies by revenue authorities in such a way that correct amount is collected efficiently and effectively with minimum tax avoidance and evasion. It is the whole organizational set-up for the management of the tax system. The tax administrative set-up is a department of government and of course works under regulations prescribed by tax legislation. The broad objective of a tax system is to ensure the long-run fiscal soundness of the policies and programmes of government while the purpose of a tax administration is to fully implement the tax system. (*Odubakin, 2014)*
The administration of taxation in Nigeria is vested in the various tax authorities depending on the type of tax under consideration.

Broadly, there are three categories of tax authorities representing the country's fiscal federalism, namely:

- ***Federal Inland Revenue Service***
- ***State Internal Revenue Service, and***
- ***The Local Government Revenue Committee***

The enabling law in respect of each type of tax will normally contain a provision as to the body charged with the administration of the tax. Each of the above mentioned tax authorities has their distinct composition, powers and functions.

Table 2. 6 List of Nigeria Tax Treaty Partners

S/N	Country	Date/Place of Signing	Date of Entry into Force	Effective Date
1.	Canada	4th August, 1992 in Abuja	16th November, 1999	1st January, 2000
2.	Pakistan	10th October, 1989 in Lagos	7th March, 1990	1st January 1991
3.	Belgium	20th November, 1989 in Brussels	1stJanuary, 1990	1st January, 1991
4.	France	27th February, 1990 in Paris	2nd May 1991	1st January, 1992
5.	Romania	21st July, 1992 in Abuja	18th April, 1993	1st January, 1994
6.	Netherlands	11th December, 1991 in Lagos	9th December, 1992	1st January, 1993
7.	United Kingdom	9th June, 1987 in London	1st January,1988	1st January, 1989
8.	China	15th April, 2005 in Abuja	21st March, 2009	1st January, 2010
9.	South Africa	29th April, 2000 in Cape Town	5th July, 2008	1st January, 2009
10.	Italy	22nd February, 1976 in Lagos	1977	1st January, 1978
11.	Philippines	30th September, 1987 in Manila	18th August 2013	1st January, 2014
12.	Czech Rep.	31st August 1989 in Lagos	2nd December, 1990	1st January, 1991
13.	Slovakia	31st August 1989 in Lagos	2nd December, 1990	1st January, 1991
14.	UAE	19 January, 2016	NA	NA
15.	Kenya	September 6, 2013.	NA	NA
16.	Mauritius	Nigeria and Mauritius signed a DTA on August 10, 2012.	NA	NA
17.	Poland	12 February, 1999	NA	NA
18.	South Korea	6 November 2006	(Legislative Ratification Pending)	NA
19.	Spain	18 November 2004	NA	NA
20.	Sweden	Signed, November 2004.	[Sweden completed ratification procedures in 2005]	December 12, 2012 (Ratified by Nigeria)
21.	Singapore	November 16, 2016.(Approved by Nigeria's Federal Executive Council)	Yet to be approved by the National Assembly	NA
22.	Qatar	February 28, 2016 (Approved by Federal Executive Council)	Yet to be approved by the National Assembly	NA

Source: Federal Inland Revenue Service (FIRS), Nigeria.

2.1.14 Recent Reforms to Nigeria Tax System

Introduction and Historical Overview

According to the Official Report of the 31st Annual CATA Technical Conference – Abuja 2010, taxation has been proven to remain the most reliable means of stimulating economic growth and development. However, the taxation potential of developing nations is rarely fully explored. Not more than one-fifth of what is due is collected, the Conference reported. The reason for this include low capacity of revenue agencies, ineffective and efficient tax policies and laws, the absence of a well-organized and locally controlled market, and very large informal sector where record keeping culture is poor. In the case of Nigeria, there has been overdependence on the finite oil resources as a source of revenue to government for the financing of development. Nigeria's realization of the potentials inherent in an efficient tax system led to recent (2004 – Date) reform of Nigeria's tax policy and system of administration. This total reformation of the entire nation's tax system was dubbed '*Tax Policy and Administration Reforms'*. "It is a new orientation and rebirth of our tax system in order to meet global trend and best practices culminating in entire process of review.*" (FIRS, 2010)*

Tax reform is essential in the administration of developmental economic programme. To this extent, taxation has been defined as the transfer of resources from private sector to the public sector, so that the government can meet its financial responsibilities, *Azubuike (2009).* The study shall adopt *'Tax Reform'* to mean the series of action taken by Nigeria's government to promote the tax system for optimal performance. It is not novel as Nigeria has embarked on series of tax reforms before the recent one. The several tax reforms were designed to broaden the tax base, reduce the tax burden on tax payers, restore the confidence of the tax payer on the tax system, and promote voluntary compliance on the part of the tax payer. On the whole, the ultimate goal of Nigeria's tax reform has over the years remained the enhancement of public revenue generation, until very recently, when the pivotal role of taxation in FDI attraction and overall campaign for improvement in the country's Ease of doing Business was realized. Very little, apart from array of wasteful, inefficient and ineffective incentives, have been done in the area of reforming Nigeria's tax system with FDI in mind. Hence, several studies pertaining to tax reforms in Nigeria concentrated on the effect of tax reforms on economic growth and enhanced revenue generation

The recent reforms process is not the first attempt by the government to address the inefficiencies identified in the tax system over the years. Since the 1970s, a number of attempts have been made at reforming the Nigeria tax system. While the history of modem taxation in Nigeria started with the Stamp Duties Proclamation in 1903 in the then Northern Protectorate — which later became part of amalgamated British Colony of Nigeria — it was the Native Revenue Proclamation of 1906 that systematizes all existing pre-colonial taxes, thus bringing into place a new regime of tax rates. The amalgamation of the Northern and Southern Protectorates to form the colonial federation of Nigeria in 1914 led to the Native Revenue Ordinance, 1917, which was extended from the northern territories to the western and eastern territories in 1918 and 1927, respectively.

Since then, there has been a steady progress in the tax regime with various attempts to modernize, expand, reform and improve the process, procedure, and sanctions inherent in the system of taxation in Nigeria! In 1943, the Nigerian Inland Revenue Department was carved out of the Inland Revenue Department of British West Africa. This Department was later renamed the Federal Board of Inland Revenue under the Income Tax Ordinance, No. 39(1958). This was followed by the Companies and Income Tax Act, No. 22(1961), which established the Federal Board of Inland Revenue, FBIR. The Act also created a Body of Appeal Commissioners to resolve tax-related disputes. In 1993, the Finance (Miscellaneous Taxation Provisions) Act No. 3 and Decree No. 104 established the Federal Inland Revenue Service (FIRS) as the operational arm of the FBIR and reviewed the functions of the Joint Tax Board (JIB), respectively. Since the early 90s, Nigeria has pursued a consistent set of fiscal policy objectives which include which includes: pursuance of deliberate low tax regime aimed at encouraging savings and investment; use of tax incentives to stimulate economic growth and promote the development of certain sectors of the economy; deliberate movement from income to consumption tax; moving from the traditional coercive approach to encouraging voluntary compliance and self-assessment regime; use of due process of the law and mechanism of efficient tax administration to curb tax evasion and avoidance; modernization of tax administration, etc. Even with the above highlighted fiscal policies aimed at reforming the tax system, it was still distortionary, inefficient, ineffective and far below global best practices.

The story of tax administration in Nigeria changed dramatically in 2007 with the granting financial and administrative autonomy to Federal Inland Revenue Service through the passage of the Federal Inland Revenue Service (Establishment) Act 2007. This milestone in the history of taxation and tax administration was a result of the recommendations of the Study and Working Groups on Nigerian tax system. The implementation of the harmonized report of the two groups first began 2004. The implementation of the critical changes in the laws and institutions governing taxation and tax administration fell to the new board and management headed by Ifueko Omoigu-Okauru, who was appointed the Chairman and Chief Executive of the Federal Inland Revenue Service by President Olusegun Obasanjo in May 2004. This marked a new era in the history of both the legal and institutional processes of tax administration in Nigeria, *birthing a scale and gale of modernization and reform practices which, hitherto, had never been attempted in the history of taxation in Nigeria.* The reforms include organizational restructuring of the federal and state authorities. The enactment of a National Tax Policy, reforms in funding, legislation, taxpayer education, dispute resolution mechanism, Taxpayer registration, human capacity building, automation of key processes, refund mechanism and several others.

As highlighted by Oriakhi (2014), reform of Nigeria tax regime became imperative because of the nature of its tax structure, which according to Anyanwu (1997) and IMF (2000) was complex, inelastic, inefficient, inequitable and unfair. Moreover, the country depended on import and export duties, while there were no opportunities to generate revenue through consumption-based tax such as VAT. The dependency of the country on taxes relating to foreign trade activities had made the revenue base of the country to be very unstable. In addition, the Nigeria's tax base was very narrow while the tax rate was very high. The national economy inherited by the President Obasanjo government in 1999 was one that was not only a mono-product economy (preponderantly based on oil revenues), but also one in which taxation was not regarded as a critical means of generating revenue nor a tool in attracting foreign investment. *This was antithetical to the spirit and practice in every modern democracy and international best practice, hence the need for tax reform.*

The main objective behind the tax reform was to create an efficient tax system based on taxes that are politically feasible and administratively practicable, thereby generating more revenue and at the same time reducing the tendency for economic distortions. According to Alli (2009), some of the objectives of tax reforms in Nigeria are:

- To bridge the gap between national development needs and the funding of the needs.
- To accelerate improved service delivery to the public.
- To boosts non-oil revenue by structurally diversifying the economy.
- Make pragmatic efforts at reviewing the tax laws thereby ameliorating the incidence of tax avoidance and evasion.
- To increase the confidence of the public on the tax system, thereby provoking voluntary compliance.
- To improve the system of tax administration thereby making it more responsive, reliable, and tax payer’s friendly.
- To reduce the complexity of the tax system both for the tax administrator and the tax payer.
- To address the issue of multiple taxation which though is still prevalent.

The Macro Environment in Context:

The pre-2004 Nigerian tax system reform agenda was captured within the framework of the National Economic Empowerment and Development Strategy (NEEDS). NEEDS was a medium term plan (2003-2007) crafted by the Federal Government with the buy-in of other tiers of government, the legislature, the organized private sector and the civil society to reduce poverty, create the value system of the Nigerian society. Under the macroeconomic framework, the NEEDS programme focused on four areas for policy intervention, namely: The real sector; the fiscal operations and policy; Balance of payments; and Monetary and Exchange Rates Policies. Within the fiscal operations and policy framework, the tax system reforms identified six keys areas to be addressed in the short to medium term, namely:

- Restructuring the tax system
- Revenue generation consideration
- Efficiency of collection
- Tracking and responding to international standards
- Promoting investment; and
- Coordination of tax administration.

Principles Guiding the Recent Tax Reforms in Nigeria:

The following has been identified as principles upon which the tax reform was based.

- The determination of equity, certainty, convenience and efficiency as the principles that guide the entire tax reform process.
- The creation of a conducive climate for investment and accord recognition to the taxpayer as "King"
- Collapsing the old structure and adopting international best practices in taxation.
- Creation of a one-stop shop operation for all taxes.
- It is also aimed at capacity building and training/exposure to FIRS core staff.
- Regular public enlightenment programmes and taxpayers education.
- Accountability and Transparency in tax administration via regular publication of information circular regarding the revenue accruing to all the government
- Staff re-orientation and value indoctrination.
- Automating the collection and much of the tax administration system in order to ease the process of tax compliance, eliminate leakages and fraud, thereby safe-guarding revenue accruing to all the governments.
- Ensuring minimum visits by tax officials to taxpayers' premises in order to prevent collusion as well as developing a reliable taxpayers' data base.

The Reform Drivers – the interest of stakeholders

1. ***Government*** – needs sufficient revenue for national development
2. ***Donor Agencies*** – want to see positive outcome of their investments in the tax system
3. ***Global Trend*** – conforming with international best practices in tax administration
4. ***Tax Consultants*** – pressurizing the government to take over tax on the promise of better performance
5. ***FIRS: Self Preservation*** – service goal is to continually surpass her revenue target in all taxes and therefore achieve a ratio of non-oil collection to GDP ratio of at least 7% annually; Need to safeguard the job of tax administrators.

Given the inadequacy of the earlier reforms, in August 2002, the Finance Minister Mallam Adamu Ciroma inaugurated another Study Group headed by Professor Dotun Phillips with terms of reference to review all aspects of the Nigerian tax system and recommend improvement therein. In order to make the study easy and detailed, the Study Group was divided into eight subcommittees. The sub-committee were on National Tax Policy, Tax Incentives and Disincentives, Local Government, Oil and Gas Taxation, Taxation and Federalism, Indirect Taxation, Direct Taxation and Tax Administration, The Study Group submitted its report to the Federal Government in July 2003. On 12 January 2004, the new Finance Minister Dr. Ngozi Okonjo-Iweala inaugurated a private sector led Working Group headed by Seyi Bickersteth. The Working Group's terms of reference were to: critically evaluate the recommendations of the Study Group; prioritize the strategies necessary to give effect to the reform of the Nigerian tax system; and segment the strategies into short term, medium term and long term.

At a retreat held between 10 and 11 February 2004, the Working Group prepared its final report and submitted it to the Federal Government. At a Federal Executive Council meeting held on October 18, 2004, the new Executive Chairman of the FIRS outlined the reform agenda necessary to reposition the Nigerian tax system. The reform agenda was distilled mainly from the recommendations both the Study and the Working Groups with inputs from other stakeholders such as the IMF Mission on Tax Administration, the Federal Ministry of Finance, and the Economic Management Team. The unanimous opinion among all stakeholders was that tax reforms should aim at diversifying the Nigerian economy. The highlights of the presentation to the FEC by the Executive Chairman were as follows:

- Tax incentives should be streamlined and exceptions made only for the oil sector, industries located and operating in the rural area and export-oriented industries.
- The tax administration system should be reformed by adopting the following measures:
- Making the Federal Inland Revenue Service autonomous with respect to funding, procurement, recruitment and remuneration;
- Reviewing the organizational structure of the FIRS and ensuring the computerization of its operations;
- Reduction of tax evasion by naming and shaming recalcitrant and defaulting taxpayers;
- The establishment of a tax or revenue division of the Federal High Court to enable specialization by High Court judges as well as quick disposal of disputes;

- The discontinuation of the use of tax consultants for revenue collection by governments at all levels; and
- Harmonizing tax procedure, codes and the creation of a tax friendly environment.
- The informal sector must be encouraged to pay taxes, especially personal income tax, and adequate mechanisms provided for sanctions against infringement of statutory requirements such as the failure to disclose income or gains of a person by a bank and forgery of Tax Clearance Certificate.
- The four year limitation relating to the ability of companies to claim past losses from future profits and carry forward all capital allowances should be expunged from the law. Furthermore, investment tax credit should be replaced with investment allowance and penalties for late filing of returns should be increased.
- The Education Development Fund be renamed the Education Trust Fund which would be funded through yearly votes and several other sources; Value Added Tax should be included in the Exclusive Legislative list of the Nigerian Constitution; and the VAT Act be amended and an administrative appeals procedure for objections to VAT assessments and refunds be instituted.
- A five percent cost of collection should be approved for the Service for its operations; another five percent of collection for tax refunds while a 10 percent cost of collection should be approved for the Nigerian Custom Service. (The Study Group and the Working Group had, respectively, recommended three percent and 10 percent cost of collection for the Service.
- Additional incentives should no longer be given to operators of marginal fields in the area of oil and gas sector.
- The FIRS would work in conjunction with the FCT administration to develop the tax administration structure of the territory.
- The incentives proposed in regard to export processing zones (EPZs) were awaiting the approval of the National Assembly, as well as tax incentives relating to payment of tax on

profit and the exemption of payment of VAT on machinery and goods imported by companies operating in EPZs.

- Of particular importance on the reform agenda was the need to reposition the tax administrative agency of the Federal Government - *FIRS* so as to optimally deliver on its mandate. The primary objectives of the reform initiative with respect to institutional overhaul of FIRS as an organization include:
  - Streamlining the mission, value, goal and organizational structure of the FIRS;
  - Plugging the leakages in service attributable especially to corruption in the system;
  - Securing adequate funding for the Service;
  - Operational autonomy coupled with capacity building and the building of the FIRS institution though adequate staff selection, training and deployment and continuous training;
  - Expansion of the tax net in Nigeria through the introduction of more services;
  - Strengthening the newly created investigation and Enforcement Department; -
  - Invigorating the taxpayer education and services arm of the Service;
  - Automation of the entire collection and general tax administration system; and
  - The stoppage of *(inefficient)* exemptions and waivers.

The FEC largely approved the proposals and objectives of the reforms, particularly the funding of the FIRS through a percentage of revenue collected. It also approved administrative and financial autonomy for the FIRS. The FEC meeting concluded with the constitution of a *Presidential Technical Committee* to fashion the statutory enactments necessary to implement the proposed tax reforms.

Implementation of the Recent Tax Reforms: The implementation of Nigeria's recent tax reform commenced in 2004, which was championed by the then Executive Chairman of Federal Inland Revenue Service (FIRS), Ifueko Omoigu-Okairu marked a milestone improvement in tax administration in Nigeria. The achievements and progress made is one that till date has not been surpassed in the history of tax administration in Nigeria. One important indication of the monumental achievements produced by the reforms since 2004 under the leadership of the Executive Chairman, Federal Inland Revenue Service (FIRS), Ifueko Omoigui Okairu is that, in the fourth year of the reforms alone (that is, in 2008), the actual collection of 2.972 trillion naira (N2,972 trillion) in taxes was over and above the cumulative collection for the eight year period (1996-2003) preceding the reforms – which amounted to only 2.682 trillion naira (N2,682 trillion), (FIRS, 2012).

Nigeria Investment Promotion Commission Act, CAP. Nii7 LFN 2004 – An FDI Booster: An aspect of the implementation of the reform which is specifically targeted at attracting FDI is the enactment of Nigeria Investment Promotion Commission Act, CAP. Nii7 LFN 2004 (NIPCA). By this development, foreigners can now own 100% shares in any company as opposed to the earlier arrangement under the repealed Nigerian Enterprises Promotion Act which limited foreign ownership of business in Nigeria to 40%. Foreign participation is however limited to business enterprises not within the "Negative List" which contains enterprises that foreigners are prohibited from participating in.

The National Tax Policy: A key achievement recorded by the reform is the unprecedented formulation of Nigeria's National Tax Policy. To fulfil their functions, all governments require taxation revenue. However, the level of the tax burden and the design of tax policy, including how it is administered, directly influence business costs and returns on investment. Sound tax policy enables governments to achieve public policy objectives while also supporting a favourable investment environment. Tax policy formulation which is an integral part of the fiscal system usually sets the agenda for any tax system which in turn determines the basis of a tax law and its administration (FIRS, 2010).

On April 7, 2012 the National Tax Policy document was launched by former President Goodluck Jonathan. The main thrust of the Tax Policy is to establish fundamental principles to guide an orderly development of the Nigeria tax system towards meeting its overall objectives. Summarily, some of the salient provisions of the National Tax Policy are:

- The provision of a stable reference point for all stakeholders in the country on which they shall be held accountable;

- Shifting the focus of the tax system from direct to indirect tax that is considered less distortionary;
- Reducing the personal income tax from 25 percent to 17.5 percent, and company income tax from 30 to 20 percent;
- Strategically increasing VAT from 5 to 15 percent,
- Avoiding internal multiple taxation on income, property, imports, production and turnover by the various tiers of government;
- Reducing and streamlining the number of tax incentives in the Nigeria tax System;
- Collection of taxes only by career administrators that are public servants, thereby prohibiting the use of ad-hoc tax administrators,
- vesting of the power to impose, reduce, increase, review or cancel any rate of tax on the National Assembly, especially with respect to taxes from the executive;
- subjecting the Nigeria's tax system to comprehensive reviews every three years pertaining to existing tax legislations.
- an essential component of the national tax policy is the introduction of Taxpayers Identification Number (TIN)**.** TIN was made possible by cooperation between the state and federal government. It is a nation-wide electronic database system for the registration and storage of data of tax payers in Nigeria. Overall, the aim of the national tax policy is to have a nation and people that see taxation as a partnership with the government**.** It is believed that the partnership between the government and tax payers will broaden the tax base by bringing into the tax net both the formal sector and the informal sector that has consistently been elusive to tax administrators.

Interestingly, several years after the formulation of the National Tax Policy, a good number of the prescription of the policy document are yet to be implemented thus leaving some of the challenges of the tax system still unattended to.

Reform of the Nigeria Joint Tax Board

The Board - The Joint Tax Board has over the years continued to contribute to the advancement of the tax administration in Nigeria, especially in the area of harmonization of Personal Income Tax administration throughout Nigeria. The Board is established by section 86 (1) of the

Personal Income Tax Act cap. P8 LFN 2004. Achievements and Contribution of the JTB to Tax reform in Nigeria include:

i. Reduction in the number and proliferation of illegal taxation which have become a major disincentive to investment. In recent years, a few of the states BIR have taken affirmative actions in that regards

ii. Convening of a stakeholder forum on the menace of multiple taxation to understand the issues further

iii. It also called for the enactment of state laws, specifying clearly all approved taxes and levies collectable at state and local government levels

iv. Also advised that the constitution of the Joint State Revenue Committee in line with the provisions of the Personal Income Tax Act.

v. Encouraging joint tax audits, networking and sharing of information of taxpayers amongst revenue authorities, to address the current situation where tax payers take advantage of the existing lack of coordination between federal and state authorities;

vi. The Board has also urged government to encourage investments to their states as these serve to enable job creation, attract residents, boost revenue generated from taxation and ultimately enhance the wealth of the state.

There has been widespread reform at most Nigeria's States Internal Revenue Service ranging from ICT-based automation of collections and overall tax administration, staff training/development, professionalization of staff and tax administration due in part, to the efforts of the Joint Tax Board.

2.2 THEORETICAL FRAMEWORK/ REVIEW

There is no overarching theory relating taxes, or tax policy to FDI, (Coelho, 2015). Hence, the aim of this section is to highlight some key theoretical ideas that help to conceptualize and understand the economic phenomenon called FDI and its relationship with taxation.

i. The Classical Theory of FDI

Basically, the *Classical Theory* marks a shift from earlier doctrinal objections held by many developing countries on the role played by multinational corporations (MNCs) in their economies. Then MNCs were viewed as inimical to the economic development of the developing countries. Based on this assertion, MNCs were either discriminated against or their role in the host economy severely restricted or limited (Seid 2002:15; Markusen and Venables 1999:336; Muchlinski 1995:8; Kennedy 1992:67 in OECD 2010). This assertion also provided a justification for the expropriation of foreign companies or assets. The 1950s, 1960s and 1970s represented a period of uncertainty for foreign investors. Many of their assets or investments were either expropriated or nationalized by host states, Aremu (2005).

According to OECD (2010), the expropriation of MNCs by many developing countries particularly during the early days of their independence symbolized a rejection by these countries of being externally dependent upon "foreigners" (Kennedy 1992:74). As Kobrin (1984) observes: “However, the hostility directed at MNCs in the 1950s and 1970s has largely waned, Rather than strangle the development of FDI on the basis that it is a source of foreign domination and control, many countries have now come to recognize that positive economic gains can be achieved from the presence of FDI (Kobrin 2005:3; Gao 2005:158; Markusen and Venables 1999:336; UNCTAD 1999:4; LaIl1996:44; Muchlinski 1995:9), This change in attitude (*reflected in FDI-friendly tax policies among others*) can be attributed to, inter alia, the slowdown of growth in the world economy in the mid-1970s, change in political leadership and the scarcity of financial capital in the wake of the debt crisis of the early 1980s (UNCTAD 1999:29; Muchlinski 1995: 10). Since the 1990s in an attempt to entice MNCs, developing countries have engaged in various forms of investment liberalization and incentives, (UNCTAD 1991: OECD 1998; Kebonang 2001). These changes in tax policy, wasteful (as they simply confer a windfall on MNCs), demonstrate clearly the importance countries now attach to FDI.

Classical theorists advance the claim that FDI and multinational corporations (MNCs) contribute to the economic development of host countries through a number of channels. These include the transfer of capital, advanced technological equipment and skills (Gao 2005:158: Mody 2004:195; 2004:195; Asheghian 2004; Girma, Kneller and Pisu 2003; Kohpaiboon 2003:55; Hermes and Lensink 2003; Seid 2002:30: Keller 2001: Shihata 1991 :487; Balasubramanyam, Salisu and Sapsford 1996:95; Hymer 1970:443), the improvement in the balance of payments, the expansion of the tax base and foreign exchange earnings, the creation of employment, infrastructural development and the integration of the host economy into international markets (Li and Liu 2005:404; Janeba 2004:367: Amiti and Wakelin 2003:102; Sornarajah 1994:39; Muchlinksi 1995: 91), These claims about FDI have been amplified by the phenomenal economic growth of the newly industrialized countries: Hong Kong, Taiwan, Singapore and South Korea, especially in the late 1980s and early 1990s (Muchlinski 1995:99; Ulmer 1980:458) and more recently by China's impressive economic performance (Cheung and Lin 2004:30: UNCTAD 2003:40; World Bank 2003:151). With its emphasis on the importance of FDI and limited state role, the classical doctrine has been propagated in recent years by international institutions and organizations like the United Nations (UN), the World Bank, the International Monetary Fund (IMF) and the International Labor Organization (ILO) endorsed FDI at its 2002 Monterrey Conference held in Mexico, as a vital complement to national and international development efforts.

According to proponents of the classical theory, the benefits from FDI are derived through positive spillovers and linkage (see, for instance, Cheung and Lin 2004; Girma, Kneller and Pisu 2003; Gorg and Strobl 2002; Lensink and Morrissey 2001. In this matrix, MNCs are an important source of these spillovers. They provide information relating to new technologies, new markets, new customers and management techniques from which domestic firms benefit (Greenaway, Sousa and Wakelin 2001; Sousa, Greenaway and Wakelin 2000). This information spillover from MNCs occurs through imitation, competition, linkages and/or training (Cheung and Lin 2004; Hermes; Gorg and Greenaway 2001; Lensink and Morrissey 2001: Gorg and Strobl 2002: Markusen and Venables 1999). By imitating the more advanced technologies and managerial skills of MNCs, and through the movement of highly skilled staff from MNCs to domestic firms, local firms are forced to catch up and become more productive (Gorg and Strobl 2002; Lensink and Morrissey 2001:3; Aitken and Harrison 1999;605).

ii. The Dependency Theory of FDI

This theory focuses largely on the relationship between the center and periphery. Well-developed and industrialized countries are deemed to constitute the center and the least developed countries the periphery. In this regard, FDI is seen as a conduit through which the center exploits the periphery and perpetuates the latter's state of underdevelopment and dependence. Instead of promoting economic development, the argument goes, foreign investment strangulates such development and perpetuates the domination of the weaker states by keeping them in a position of permanent and constant dependence on the economies of the developed states Sornarajah (1994). MNCs are accused of being "imperialist predators' that exploit developing countries and exacerbate their underdevelopment Alfaro (2003). Bond (2002) and Tandon (2002) among others have either impliedly or expressly questioned the need for FDI. Bond (2001; 2002) sees for instance, multinational corporations as agents of *'global apartheid'* responsible for Africa's worsening economic state, whilst Tandon (2002) argues that what Africa needs is *'self-reliance and not FDI-reliance'*. These views which implicitly suggest that FDI is exploitative, find sympathy in the dependency theory of FDI. They are largely informed by the fact that multinationals have often been involved in the exploitation of natural resources with no corresponding benefits for host economies (UNCT AD 1999). The dependency theory is therefore very much a reaction against this "extractive nature" of FDI.

Drawing from the experience of Latin American countries, proponents of this theory argue that relations of free trade and foreign investment with the industrialized countries are the main causes of underdevelopment and exploitation of developing economies (Wilhelms and Witter 1998:8; Dos Santos 1970). Under the dependency theory, FDI is considered to promote dependence and underdevelopment through its promotion of specialization in production and exports of primary products; increased reliance by least developed countries (LDCs) on foreign products and capital intensive technology; diffusion of western values and elite consumption; acute growth inequality in income distribution and rising unemployment and destruction of indigenous production capacity (Gorg and Strobl 2002; Girma and Wakelin 2000; Markusen and

Venable 1999; Aitken and Harrison 1999; Biersteker 1987; Lall 1975). The crowding-out or displacement of indigenous production necessarily eliminates the development of the national entrepreneurial class and hence "excludes the possibility of self-sustained national development" (Biersteker 1978:7). This dependency is also worsened by the remittance or repatriation of profit, royalties, interest payments, declining reinvestment and lack of local economic spin-off, which taken together lead to a 'decapitalization' of the host economy (Dos Santos 1970: 233; Rojas 2002; Biersteker 1978). These surplus transfers reduce funds available for domestic investment in the less developed countries (Rojas 2002). As a result developing countries are compelled to seek new forms of foreign financing - be it in the form of aid or loans to finance their development or cover existing deficits. In the process they create a perpetual state of dependency (Dos Santos 1970: 233). Accordingly to address this problem, the dependency theorists contend that the solution to underdevelopment requires closing developing countries to international investment and trade (Wilhelm and Witter 1998;8). Because of the perceived exploitative nature of FDI, the dependency and underdevelopment it engenders, proponents of the dependency theory are in unison in calling for the adoption of state policies that are deliberately discriminative of FDI in order to foster the development of local industries and promote self-reliance (see. Tandon 2002; Wilhelms and Witter 1998: 8; Blumenfeld 1991: 63). Only by this means, so they contend, can developing countries or governments acquire the autonomy and freedom to achieve structural changes and economic diversification free from constraints on their development Blumenfeld (1991).

iii. The Intervention/Integration/Middle Path Theory of FDI

The integrative school is a convergence of both the *Classical* and *Dependency Theory. It* attempts to analyze FDI from the perspective of the host country as well as that of the investor. It incorporates arguments from both the classical and dependency theorists. The theory posits that foreign investment must be protected but only to the extent of the benefits it brings the host state and the extent to which foreign investors have behaved as good corporate citizens in promoting the economic and social objectives of the host country (Sornarajah 1994:49). The theory calls for a mixture of intervention (regulation) and openness in dealing with foreign investment and cautions against too much openness and too much regulation or intervention (Seid 2002:23). The theory recognizes that there are instances where the market is better placed to act and other instances where government intervention is necessary. What is needed therefore is a balancing act between those activities that can best be handled by the market and those that can be done by the government.

In many ways, the middle path/integration theory represents a convergence between Adam Smith's case in favor of a laissez-faire approach and Keynes' argument in favor of government intervention in the market. Whilst Adam Smith in his Wealth of the Nations believed that except for intervention in providing public works and institutions, the role of the state in the market must be minimized (Hollander 1972:256; Ginzberg 1934:22; Viner 1928:(38), Keynes, who was greatly influenced by the effects of the US Great Depression of the 1930s, strongly believed that government participation in the market was crucial to stimulate the economy.

The notion that governments and markets are complements and not substitutes stands in stark contrast to earlier views which held the position that the existence of one required the diminution of the other. In the 1950s and 1960s, the state in many developing countries was the primary player in economic matters (Rodrik 1997:412). Following the debt crisis of the 1980s, major reforms were introduced which sought to limit and confine the role of government to the provision of public goods such as securing property rights, maintaining macroeconomic stability and providing education and the necessary infrastructure (Rodrik 1997:412; Whiteley 1986: 175). This idea of a limited government role in the market, often dubbed the *"Washington Consensus"*, was and has been actively promoted by the World Bank and IMF. Although important, the state's role in economic development in this 'market-friendly' approach is to be limited to providing social, legal and economic infrastructure and to creating a suitable climate for private enterprise (Singh 1994:1812). This "market-friendly" approach, which requires a limited government role has been found wanting following South East Asian economic success.

In its 1993 Report, the World Bank acknowledged that the economic success of East Asian countries, particularly Hong Kong, South Korea, Singapore and Taiwan, came not simply because these countries had the basics right (stable macroeconomic policy, high savings rates and investment rates, physical and human capital, economies that were export oriented, and the use of incentives and application of selective import barriers) but because in most of these economies the government intervened systematically and through many channels to foster development and in some cases to develop specific industries (World Bank 1993; Rodrik 1997:413; Singh 1994:1811; Harris and Schmitt 2001 :294; Rueschemeyer and Putterman 1992: 253; Selden 1992: 171). The East Asian miracle has led Haggard and Kaufman (1992:222) to argue that what the Asian success demonstrates is that market institutions and state power are not inversely related: "the expansion of the first does not require a diminution of the second". In more recent studies, Liew (2005: 332) shows that China's rapid economic growth has resulted not from less state control or rapid or "big-bang" liberalization approaches often prescribed by the IMF/World Bank but from intense state intervention and ownership of enterprises. This work

Adapted from Kebonang (2006) - "NEPAD: Drawing Lessons from Theories of Foreign Direct Investment".

2.2.2 Models for Analyzing Tax Effects on FDI

As proposed in (OECD, 2007; 2017), to guide tax policy in relation to FDI, policy analysts may rely on one or more economic models or frameworks to examine possible channels of influence. A selection of these includes is outlined below:

1. **The OECD Model:** As proposed in (OECD, 2005), *The Policy Framework for Investment* targeted at policy makers in developing and transition economies, proposes guidance in ten policy fields including tax, in an effort to identify priorities and help develop effective policies. This policy guides draws largely on survey studies to identify key issues in weighing the pros/cons of corporate tax incentives and alternative tax policies and design options to attract FDI, while also raising revenue from FDI to help finance infrastructure development. In setting the tax burden on inbound investment, policy makers are encouraged to assess whether their host country offers attractive risk/return opportunities, taking into account framework conditions (*e.g.* political/monetary/fiscal stability; legal protection; public governance), market characteristics (market size, availability/cost of labour, energy, state of infrastructure) and the prevalence of location-specific profits. As earlier mentioned,, host country framework conditions and market characteristics depend in part on past and current levels of public expenditures on programs in areas of critical importance to investors (*e.g.* education,

infra-structure development). This link establishes the critical importance of collecting tax where possible on economic profit in order to finance public developmental projects.

2. **The Neo Classical Investment Model:** Perhaps the framework most widely used by public finance economists to analyze tax effects on domestic and cross-border direct investment is the neo-classical investment framework (OECD, 2007). A main attraction is its incorporation of main statutory tax parameters influencing capital costs and establishing the statutory tax burden on investment returns. In particular, parameter-based marginal and average effective tax rates (METRs/AETRs) derived from the neo-classical investment model may be analyzed to determine the percentage change to these tax burden measures resulting from a single or package of corporate tax policy adjustments. When combined with empirical estimates of the sensitivity of FDI to these effective tax rates, the framework lends itself to estimating the long-run effects of corporate tax reform on FDI. The standard neo-classical investment theory predict increased (decreased) inbound FDI following a decrease (increase) in the host country corporate tax burden (if not offset by adjustments to home country foreign tax credits).
3. **The Economic Geography Models:** Theoretical economic geography focuses on building theories arounds spatial arrangement and distribution of economic activities. It deals with economic regionalization as well as local economic development. Central predictions of the neo-classical model as regards tax effects on investment have been challenged in recent years by the new economic geography framework, emphasizing the role of self-reinforcing business concentration (agglomeration) economies. The cruz of the model is that business concentration economies imply that effects of tax rate changes will be non-linear – policy adjustments under certain conditions may have minimal impact on the location of capital, while subsequent adjustments may have dramatic effects, (OECD, 2007).

2.2.3 Taxation of Inbound FDI – Policy Considerations and Perspectives

In recent years, the dynamics of international tax competition have been widely studied and debated, with an eye to assessing tax policy reaction to and potential efficiency effects of competition for a geographically mobile capital tax base. FDI “international competitiveness” concerns and pressures are felt in virtually all countries to somehow accommodate a relatively low host country tax burden. A number of alternative policy approaches in responding to tax competition can be identified in different world economies. While perspectives and positions vary from one country to another, to a large extent they are based on a common broad set of considerations including revenue requirements, efficiency (welfare) considerations, fair domestic competition concerns, and pressures to provide internationally competitive tax treatment. Below is a highlight of major FDI-Tax Policies as highlighted by (OECD, 2007; 2017)

1. **Statutory Tax Rate Adjustment Policy**: Many tax officials underline the attractions of reducing the statutory corporate income tax rate as a means to encourage FDI: a relatively simple tax adjustment to introduce; readily observed; directly relevant to investors who anticipate earning pure economic profits. For EU countries subject to State Aid rules and Code of Conduct rules prohibiting provisions that discriminate in favour of FDI, attention is focused back to the statutory rate as a broad-based mechanism to reduce the host country tax burden. However, such reductions tend to be expensive in terms of revenue foregone, may be observed as unfair, and may create tax arbitrage problems with the personal income tax system.
2. **Base Broadening Policy**: This policy is aimed at cushioning the effect and pressure of aggressive tax planning Multinational Enterprises (MNEs) usually engage in. It is very efficiency improving when combined with statutory tax rate reduction; and reducing tax-planning pressure against the domestic tax base. For inbound FDI, policy interest may arise on account of the potential for a *net* increase in domestic income, shared with government through taxation of wage and salary income and profits of foreign-owned companies, and possibly other taxes on business (*e.g.* property tax). These flows must be additional and not represent displacement effects.
3. **FDI-Specific Tax Incentives Policy**. Where inbound FDI is regarded as particularly mobile and sensitive to host country taxation, governments may be encouraged to target tax relief to FDI to the exclusion of domestic-owned firms (*e.g.* through tax incentives, or through weak or lax enforcement of base protection provisions), or to reduce the tax rate on income from capital more generally. Under a basic tax competition model that ignores labour taxation, increased capital mobility is predicted to result in tax rates on capital income that are set inefficiently low from a public perspective. Other predictions

include large countries competing less for capital through rate cuts, and higher per capita income in smaller countries with lower tax rates and higher capital/labour ratios.

4. **Taxation of Immobile Labour/Waiver of Capital Income Taxation**. Yet another policy strategy is the taxation of immobile labour which has been found to be optimal for a small capital-importing country facing a perfectly elastic supply of foreign capital to waive host country income tax on inbound FDI, with this tax being fully shifted onto labour. Under this situation, it is optimal for the host country to instead tax labour income directly, and avoid production efficiency losses that result from taxing capital income. Subsequent work finds that if economic profit cannot be fully taxed, then some host country taxation of inbound FDI by small capital importing countries is efficient.
5. **Strengthening of Non-Tax Factors Policy:** Inbound FDI has widely been recognized as being attracted by macroeconomic stability; a supportive legal and regulatory framework; skilled labour and labour market flexibility; well-developed infrastructure; and business opportunities tied to market size (with profitability of the domestic market tied to the purchasing power of the population, and foreign markets reached via an extensive network of trade agreements). In other words, a number of non-tax factors are central drivers to FDI decisions. A good number of countries focus on this as a deliberate means of attracting investment while tax fundamentals focused on revenue optimization and other fiscal concerns. Indeed a good number of large OECD countries with relatively high effective tax rates are very successful in attracting FDI. This point to the importance of non-tax factors and other host country attributes in attracting FDI.
6. **Reduction in Effective Tax Rate on Most Mobile Elements of the Tax Base:** Rather than reducing the burden of tax provisions of general application, certain countries prefer to explicitly target tax relief with the aim of encouraging additional FDI at a lower cost in terms of foregone tax revenue. Targeting mobile activities (e.g. shipping, films, export-oriented, head-office) is regarded by some policy makers as an attractive *option.* In considering reductions in the effective tax rate on the most mobile elements of the tax base, the tax treatment of interest and royalty income is increasingly under review, with some countries indicating the dependence of their future policy actions on the actions of

others. Some tax systems target certain activities as a matter of national industry policy, while in others, activities are targeted only where there is believed to be market failure.

7. **Response to Tax Avoidance and Aggressive Tax Planning:** Yet another policy is tightening the noose against the aggressive tax planning of MNCs aimed at paying little or nothing to their host economy. Tax systems focused on adopting this policy usually have tax revenue maximization as their driving principle. This they do using general and specific anti-avoidance provisions including thin-capitalization and transfer pricing rules, robust audit and investigation of the accounts and operations of these MNCs, and other stiff regulatory measures.

In summary, the theoretical underpinning adopted for this work is the Intervention/Middle Path theory which is a convergence of the merits of both the *Classical* and *Dependency Theory.* It incorporates arguments from both the classical and dependency theorists. The theory posits that foreign investment must be protected but only to the extent of the benefits it brings the host state and the extent to which foreign investors have behaved as good corporate citizens in promoting the economic and social objectives of the host country. The theory calls for a mixture of intervention (regulation) and openness in dealing with foreign investment and cautions against too much openness and too much regulation or intervention. This pragmatic FDI theory was the policy approach behind the celebrated phenomenal economic and industrial turnaround of the Asian Tigers and China, World Bank (1993).

Moreso, the approach or basis of analysis of FDI –Tax effect adopted in this work is the Neo-Classical Investment framework. Its main attraction is the incorporation of all statutory or mandatory tax parameters influencing capital costs and establishing the statutory tax burden on investment returns. In particular, parameter-based marginal and average effective tax rates (METRs/AETRs) derived from the neo-classical investment model may be analyzed to determine the percentage change to these tax burden measures resulting from a single or package of corporate tax policy adjustments or reforms. When combined with empirical estimates of the sensitivity of FDI to these effective tax rates, the framework lends itself to estimating the long-run effects of corporate tax reform on FDI.

2.3 EMPIRICAL REVIEW

About the earliest studies on taxation and foreign direct investment was that of *Barlow and Wender (1955).* They studied the influence of taxation of US MNCs investment abroad by US government following numerous suggestions for stimulating foreign investment through tax reduction. They conducted interview with 40 business firms to determine the experience of the executives with respect to foreign investment and their policies in that connection. One remarkable finding at that time was that taxation was not so important a consideration in the minds of executives, in connection with foreign investment as were certain other factors, especially lack of currency convertibility. They however concluded that something can be done from a taxation standpoint to stimulate foreign investment. Modern literature on taxation and FDI started with Hartman (1984). He measured the aggregate inflow of direct investment in the United States as a ratio of GNP(K/Y) between 1965 and 1979 by the rate of return on US investment and taxes, measured as averages on the basis of macro data. The focus of Hartman's paper is on the distinction between FDI financed out of retained earnings and transfer of funds. Hartman claims that retained earnings should be more sensitive to US taxes because mature firms will use retained earnings as the marginal source of finance (which is cheaper than transfer of new funds). Hartman (1984) finds that the aggregate inflow FDI in the United States as a ratio of GNP *(K/Y)* between 1965 – 1979. The finding, even though complex suggest that foreign investment in the U.S. is affected, in the manner predicted, by changes in domestic tax policy – tax reforms. Hartman's results imply that, indeed, the tax rate elasticity for retained earnings is significant while for transfers the results are insignificant.

Young (1988) focused on FDI from Germany and the UK into 11 locations during 1977-1992. He uses a log specification and include lagged FDI in their estimation. Moreover, he stresses the importance of the home country corporate tax for the responsiveness of FDI to host country corporate tax rate. The result reveals negative association between corporate taxation and FDI. Newlon (1987) casts doubts on the studies in the realm of Hartman. First, Newlon shows that these studies have not used the appropriate data for the rate of return on FDI for the period 1965-73.

As noted in De Mooij and Ederveen (2003), these earlier studies all rely on average tax rates based on macro data. Slemrod (1990) was the first to use an alternative measure for the tax rate, namely the marginal effective tax rate derived by Auerbach and Hines (1988). He also criticizes the earlier studies in a number of other ways. Slemrod's criticism of the earlier literature have made researchers reluctant to continue using aggregate time series data along the lines of Hartman. Much later, Billington (1999) and Broekman and van Vliet (2000) have used aggregate FDI flows to estimate the tax elasticity. Billington uses a panel of 7 OECD countries between 1986 and 1993 with aggregate FDI inflows. He regressed the log of FDI to the square of the country statutory tax rates and reports significant but small elasticities. Broekman and Van Vliet focused on aggregate FDI inflows in 15 EU countries using data spanning from 1989 to 1998 and average tax rates based on micro data. Using a simple linear specification, they report elasticities in the order of –2.

More empirically related, in a cross country study using fourteen OECD countries, Cummins, Hasset and Hubbard (1996) employ the GMM approach to examine the impact of tax reform on investment. The study reveals that 12 out of the 14 countries had investments that are significantly responsive to changes in the tax rate. This portends that if the tax reforms in these countries reduces the tax rate, it will stimulate investment in those countries. In the same vein, Rodrigo (2004) empirically examined the relationship between tax reforms and private investment using Chile data. He employs data for the years ranging 1975-2005. The study confirms the findings of Cummins et al. (1996) which found that tax reforms stimulate investment by freeing up investible resources. Grubert and Mutti (2000) exploit micro data of more than 500 US tax returns to construct an aggregate data set on average tax rates and investment in plant and equipment by US multinationals in 60 locations. Using different specifications and different concepts of the average tax rate, Grubert and Mutti report significantly negative elasticities in order to gauge the likely effect of 1999 US Tax Reform. Altshuler *et al.* (2001) have exploit similar data as Grubert and Mutti and used a similar specification. They focus on the distinction in elasticities between 1984 and 1992. For 1984, they find an elasticity that is smaller than for 1992. This suggests that capital has become more responsive to taxes during the *1980s.*

Hines (1996) builds on Slemrod's idea to use information on individual countries' direct investment into the US. He uses data on property, plant and equipment from seven investing countries into 50 different US states and explores the impact of reform to corporate income taxes, measured by the state statutory rates, on the allocation of FDI. Hines reports significantly negative elasticities that are larger than found in most previous studies. The approach of Hines was later used by Gorter and Parikh (2000) who both use a panel of bilateral FDI flows between OECD countries. Both studies use an average tax rate, but Gorter-Parikh's tax rate is based on firm-specific data, whereas Benassy-Quere *et al (2005)* rely on aggregate data. They both report significant tax effects on FDI by exemption countries.

Swenson (2001) takes up the qualifications by Auerbach and Hassett (1993) and distinguishes six different components of FDI: *new plants, plant expansions, mergers and acquisitions, joint ventures, equity increases, and other FDI***.** The data refer to the number of investment projects, rather than the total amount of investment and comprise 46 countries investing in 50 US states, with the statutory corporate tax rates of the states as a proxy for the effective tax rate. The tax elasticity of new plants and plant expansions appear to be significantly negative for most investing countries. However, the effect of mergers and acquisitions is significantly positive in all cases. This suggests that, if mergers and acquisitions take up a larger share of aggregate FDI, it becomes less likely that the tax reforms effect on aggregate FDI will be significantly negative.

More recently, OECD (2016) studies examining cross-border flows suggest that on average, FDI decreases by 3.7% following a 1 percentage point increase in the tax rate on FDI. But there is a wide range of estimates, with most studies finding decreases in the range of 0% to 5%. This variation partly reflects differences between the industries and countries being examined, or the time periods concerned. In yet another study, Mika, Andrew and Shiv (2012) examined the impact of the tax system on small and medium scale enterprises (SMEs) in Shinyanga Municipality, Tanzania. The study utilized the primary data approach, which was analyzed using descriptive statistics, frequencies and percentages. The study reports that majority of the respondents opined that the prevailing tax system is detrimental to the robust performance of small and medium scale enterprises (SMEs). Thus, the study suggested the reforming of the tax policies.

Further on the African context, Newman (1998) examines the impact of tax reform on revenue productivity in Ghana. The study concluded that tax reforms impacts on productivity positively and significantly. More authoritatively, using a panel dataset for sub-Saharan Africa (SSA) countries, Asiedu (2001 & 2006) explores the determinants of FDI and examines why SSA has been relatively unsuccessful in attracting FDI in spite of policy reforms and the determinants of FDI flow in Africa. The results of this study indicate that better infrastructure and a higher return on investment has a positive impact on FDI in non-SSA countries, while there is no significant impact on FDI in SSA countries. The coefficient on openness to trade is conducive to FDI in both SSA and non-SSA countries. However, the marginal benefit from increased openness is lower for SSA countries. The author concludes that factors that determine FDI in the developing world have a different impact on FDI in SSA countries. The results of this study are based on the OLS estimation technique which does not address the problem of endogeneity. Asiedu (2006), reports availability of Natural Resources and large market as the main drivers of FDI in Sub-Sahara Africa.

Very recently, African Development Bank (2018) in a panel study empirically assesses the impact of Company Income Tax (CIT) rate changes on FDI net inflows in Africa using a dynamic spatial Durbin model with fixed effects. The results of the empirical analysis show that cuts in CIT rates increase FDI net inflows in the host country and in the neighboring countries in the short and long run. Furthermore, the study found a strategic complementarity in FDI inflows between the sample countries, suggesting that an increase in FDI inflows in a host country is likely to stimulate FDI inflows of its neighbors. The study further reports that a recent empirical studies on tax incentives, mainly based on developed countries, suggest that competition to attract FDI is likely to lead to a "race to the bottom" among countries (see, e.g., Devereux et al., 2002; Abbas and Klemm 2012).

According ADB (2018), only three studies (Abbas and Klemm, 2013; Cleeve, 2008; Klemm and Van Parys, 2012) have estimated the empirical effects of tax incentives on FDI with samples of developing countries that included African countries. Klemm and Van Parys (2012), using a sample of 40 Latin America, Caribbean and African countries over the period 1985-2004, show that lowering of CIT rate, a form of tax reform, has a significant positive impact on FDI in Latin and Central America but not in Africa. Focusing on 16 sub-Saharan African countries, Cleeve (2008) estimates the impact of fiscal incentives in attracting FDI over the period 1990-2000. He proxied fiscal incentives by a tax holidays variable equal to 0 if no tax holiday is offered in the host country, 1 if the tax holiday is less than five years, and 2 if the tax holiday is greater than five years. Cleeve (2008) shows that tax holidays positively and significantly affect FDI inflows to Sub-Saharan Africa, only when country fixed-effects are not controlled for. Moreover, none of the previous studies discusses the effect of a change in the CIT rate of a host country on FDI inflows in neighboring countries geographically or economically. Abbas and Klemm (2013) find that the Effective Marginal Tax Rate (EMTR) does not significantly affect FDI while only reductions in Effective Average Tax Rate (EATR) applicable to special tax regimes positively affect inward FDI for 50 emerging and developing countries including 13 African countries (*Nigeria, Ghana and South Africa inclusive*) over the period 1996-2007. Notably, these previous studies ignored spillover effects between countries, whereby an increase in FDI in one country can have positive or negative spillover effects on the level of FDI in neighboring countries.

As reported by African Development Bank (2018), beside tax incentives, several determinants of FDI inflows can be found in the literature. These determinants can be classified into two main categories: demand and supply factors on the one hand, and institutional and macroeconomic factors on the other hand. Demand-supply side determinants with positive impact on FDI inflows include domestic market size, typically proxied by population size (Diaw and Guidime, 2013), government spending relative to investments or consumption (Greene and Villanueva, 1991; Serven and Solimano, 1992; Mlambo and Elhiraika, 1997), openness to trade (Asiedu, 2002), and natural resources endowment, particularly in African countries (Asiedu, 2002; Basu and Srinivasan, 2002). FDI determinants in the institutional and macroeconomic category with a negative effect on FDI inflows comprise macroeconomic instability (proxied by inflation rate in the literature) and political risk (Busse and Hefeker, 2007). In contrast, the availability of skilled labor (Noorbakhsh and Paloni, 2001), financial development (Dutta and Roy, 2011; Desbordes and Wei, 2017), and high-quality infrastructure (Asiedu, 2002; Dupasquier and Osakwe, 2006; Diaw and Guidime, 2013) all stimulates FDI inflows through their positive impact on the productivity of investments. Likewise, exchange rate can increase FDI since depreciation makes local assets cheaper to buy while stimulating exports competitiveness (Froot and Stein, 1991).

Within the Nigerian context where you have a handful of studies focusing on the impact of tax reform on investment, Nwokoye and Rolle (2015) remains one of the most current empirical study most related to this work. The study informed by the quest to examine the domestic investment implication of the series of tax reforms in Nigeria, particularly the tax reforms of 2003 and National tax policy of 2012, employs annual time series data spanning the years (1981-2012) to assess the impact. The result of the estimated OLS model shows that tax reform as proxied by VAT and CIT, both positively and significantly stimulate investment in Nigeria. Ekpung and Wilfred, (2014) find that high corporate tax is bad for economic growth and discourages FDI. This is because, it discourages new incentives by distorting FDI decisions and discouraging work effort. Okoi and Edame (2013) find that high corporate tax rate as witnessed in Nigeria has an enormous effect to FDI and GDP. As corporate tax rate rises, it would discourage FDI in the country. High corporate tax rate would reduce the incentives of foreign investors to invest in both physical and human capital. Ali (2015) examines the relationship between corporate taxation and foreign direct investment in Nigeria from 1970-1980 using aggregate data. The independent variable - corporate taxation was measured using the statutory corporate tax rate (CTR) whilst dependent variable foreign direct investment was measured using FDI (% of GDP). The result shows negative significant relationship between CTR and FDI.

In another related study, Ogbonna and Ebimowei (2012) examine the impact of tax reform on Nigeria‘s economic growth and development.. Results reveal that tax reform positively and significantly impact on economic growth, thus enhancing development, and that tax reform granger causes economic development in Nigeria. In a related and apparently the most current study, Ovunda (2018) using primary data and employing multiple regression found that tax reforms have positive and significant relationship with revenue generation and investment. In a similar empirical study of the Nigeria FDI-Tax effect, Ugochukwu et. al. (2015) examine the effect of taxation on investment in Nigeria. It also looked at the direction of causality among Petroleum profit tax (PPT), Value added tax (VAT), Company income tax (CIT), Custom and excise duties (EXCISE), and Investment (INV) employing the method of Johansen co-integration and the Granger causality tests using data spanning the period 1981-2013. The result shows that Value Added Tax and Company income tax have positive impact on Investment in the short run but negative impact in the long run. The result also indicates that petroleum profit tax has positive significant impact on investment both in the short run and in the long run and granger-cause investment. Oriakhi and Ahuru (2014) investigates the impact of tax reforms in Nigeria on federally collected revenue using OLS and concludes that tax reform can result in improved government earnings through reduction in tax avoidance and evasion and scaling down on the burden of taxation stimulate investment, including FDI. An empirical work by Adereti, Sanni and Adesina (2011) using the ordinary least square techniques regressed the GDP, which was a proxy for Economic Growth on Value-Added Tax (VAT). The model estimated has a high explanatory power as the coefficient of determination was put at 0.950544, showing that substantial proportion of the variation in Economic growth proxied by the GDP is accounted for by the variation of VAT revenue earnings. In a closely related approach Ogbonna and Appah (2012) using time series analysis and employing the scope (1981-2007) empirically investigated the impact of tax reform on economic growth in Nigeria. The results showed that changes in all the income taxes have positive coefficient. This implies that tax reform will stimulate economic growth. Peters and Kiabel (2015) examined the influence of tax incentives in the decision of investor to locate FDI in Nigeria using aggregate time series data. Multiple regression result showed that FDI response to tax incentives is negatively significant, that is, increase in tax incentives which form an integral part of most developing countries tax reform, does not bring about a corresponding increase in FDI and so should be reduced and more attention focused on stable and predictable tax system and political climate.

The above studies lend credence to the catalytic role of tax reform to pubic generated revenue and investment as it improves on the business climate of the economy and so conclude that reducing the distortionary effects of the current Nigeria tax structure would permanently increase growth. There is no point in designing a good tax structure that cannot be administered effectively. From the above Nigeria context review, it can be gleaned that much have not been written on the effect of taxation on foreign direct investment in Nigeria. The few available empirical works made use of the statutory tax rate and revenue from various tax types as the independent variable or the tax indicator instead of the more appropriate firm level data on effective tax rate which better captures the actual burden of tax compliance in Nigeria. Again, none of these works considers the necessity of using FDI (Net Inflow) as the FDI data or dependent variable. These gaps and more, this empirical study covers as well as the specific measurement of the impact of recent (2004) and perhaps ongoing tax reforms on Nigeria's FDI (net inflow).

Table 2.5 Summary of Qualitative Studies on FDI Responsiveness to Taxes and Other FDI Determinants

YEAR	REFERENCE		Empirical method	Tax effects on FDI inflows
YEAR	REFERENCE	RESEARCH FOCUS	EMPIRICAL METHOD	TAX EFFECTS ON FDI
1950s	Barlow and Wender (1956)*	Companies' strategy to invest abroad	Interview of 247 U.S. firms	10% of firms listed favourable taxes as an incentive (ranked 4th in list of determinants)
1960s	Robinson (1961)*		Survey of 205 firms	Host governments consider tax incentives determinant while investing firms omit them
	Aharoni (1966)*	How foreign investment decisions are made by U.S. manufacturing firms	Interviews in 38 US corporations	
1970s	Reuber (1973)**	Effect of tax incentives on different investor profiles	Survey of 69 international firms	Impact of tax rates greater in export-oriented companies than in domestic market seekers
1980s	Guisinguer (1985)**	Impact of location incentives on international investment decisions	Survey to 30 international firms with regard to 74 investment decisions in 20 countries	More than 65% of investors report that without an incentive package they had abandoned the project and re-located
1990s	Rolfe (1993)*	Firms' responsiveness to different types of tax incentives	Surveys to U.S. firms' managers	Start-up companies prefer incentives that reduce their initial burden; established firms prefer incentives that target profit
	Wilson (1999)	Firms' responsiveness to different types of tax incentives	Summarize main results of literature on tax competition	Identified several examples of FDI location decisions driven by tax
2000s	Grčić and Babić (2003)	Evaluation of SEEC attractiveness to foreign investors in face of most important previously Confirmed incentives	Analytic Hierarchy Process, assuming institutional development poses the most important factor	Does not consider taxes as a main determinant
	Raudonen (2008)	Review of literature on determinants of FDI with emphasis to taxation in order to prevent negative effects of taxation in Estonia	Analysis of previous studies which found significant impact of taxation on FDI, including surveys and empirical models	Semi-elasticities to tax differentials are significant for both credit and exemption systems (Raudonen, 2008)
	De Mooij and Ederveen (2008)	Summary of the results of previous econometric studies that find taxation as a determinant factor of FDI but are based on different frames	Meta-Analysis	The largest tax based elasticity concerns effect of statutory tax rate in Profit Shifting FDI

Source: Coelho et. al. (2015).

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 PREAMBLE

This chapter highlights the research methodology which is the specific procedures or techniques used to identify, select, process and analyze data about a topic or subject matter of study. It is the basis upon which the overall validity and reliability of the study is being evaluated. It basically includes the process of identifying the variables, method of data collection, measurement and analysis for decision making. Below is an outline of the design adopted in this study.

3.2 RESEARCH DESIGN

Research design is a kind of blue print that guides the researcher in his investigation and analyses. It is usually designed to find answers to the research questions. The study adopts the *ex-post facto* research design. The ex-post factor study is most appropriate for studies involving the use of existing data to establish new knowledge, Gujarati (2009). This is because the study attempts to explore cause and effects relationships where causes already exist and cannot be manipulated, Onwumere (2009). The *ex-post facto* research design is also called a causal comparative research and is used when the researcher intends to determine cause-effect relationship between an independent and dependent variables with a view to establishing a causal link between them. Hence the adoption of ex-post facto research design in this study is considered very appropriate.

3.3 NATURE, SOURCES AND METHOD OF DATA COLLECTION

This research work made use of secondary data and they include the aggregate annual time series for the period 1990 – 2017, extracted mainly from sources such as Statistical Bulletin and Annual Reports of the Central Bank of Nigeria (CBN) and World Bank Doing Business Data Bank. The data is mainly quantitative and time-series by nature. They are denominated in Nigerian Naira (NGN) and expressed in percentages, where necessary. The use of aggregate time series data is appropriate as it’s very useful in establishing long term econometric relationship between variables due to its stationarity features. This implies that the mean and standard deviation do not differ over a period of time, (Gujarati et. al 2012 and Murray and Stephens

2011). The data required for this study, as listed below, are time series in nature and secondary-sourced:

- Nigeria's FDI (Net Inflow), *1990 – 2017*, i.e., *a measure of FDI Inflows net of divestments*
- GDP *(Nominal Value at Current Basic Price)*, *1990 – 2017*, a measure of economic growth
- Nigeria Total (Federal and States) Tax Revenue, *1990 – 2017*
- Indicators for Nigeria's Effective Corporate Tax Rate and Taxation (Nigeria Tax System),
- Data for Control Variables such as *Inflation and GDP Growth Rate, 1990 -2017*

Table 3.1 List of Research Variables and Sources

Variables	**Source of Collection**
Nigeria's Gross Domestic Product (GDP) at Constant Basis Price (Nominal Value)	CBN Statistical Bulletins 2017
Nigeria's GDP Growth Rate	CBN Statistical Bulletins 2017
Nigeria's Ease of Paying Taxes Distance to Frontier Index	WorldBank Doing Business Data Bank
Nigeria Total Tax Rate (% of Profit)	WorldBank Doing Business Data Bank
Nigeria FDI (Net Inflow)	CBN Statistical Bulletins 2017
Nigeria Tax Revenue (Federal and States Govts)	CBN Statistical Bulletins 2017
Nigeria's Annual Inflation Rate	CBN Statistical Bulletins 2017

3.4 MODEL SPECIFICATION AND DESCRIPTION OF VARIABLES

3.4.1 Model Specification

The following models have been specified for the econometric analysis. The models, beyond tax indicators, contain variables that are believed to influence the attraction and retention of FDI. Their description and justification is highlighted below.

Model One

Our First *Model* is specified in line with *Hypothesis One and* tested using Multiple Regression Analysis.

1. H_o: FDI has no significant effect on the growth of Nigeria's economy.

The model is as follows:

$$GDP = F(FDI, INFL,)\ e_t \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (1)$$

This is a linear equation depicting the model and can be econometrically modelled thus:

$$GDP_t = a_o + b_1FDI_t + b_1INF_t + \mu_t \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (2)$$

Where:

b_1GDP_t = Gross Domestic Product at time t

a_o = Constant

FDI_t = Foreign Direct Investment (Net Inflow)

b_1INF_t = Inflation rate at time t

μ_t = the error term

Decision Rule: Level of significance (α) = 0.05

Model Two

Model Two relates to hypothesis two and is tested using the correlation coefficient analysis.

H_o: There is negative correlation between taxation and FDI (net inflow) in Nigeria

The model is *as follows*:

EPTD (FDI) = 0……………………………………………….. (2a)

TTR (FDI) = 0…………………………………………………(2b)

The decision rule for testing the significance of r or rejection/acceptance of hypothesis is as follows:

H_o: $r = 0$ (the two variables are not associated)

H_1: $r \neq 0$ (the two variables are associated)

As a rule, if the calculated value of the t-statistic is more than the table t-value, then we reject the null hypotheses, H_o, otherwise, we accept the null hypotheses, H_1.

Where, EPTD mean "Ease of Paying Taxes Distance to Frontier adopted from World-Bank Doing Business survey for many years. For a particular year of measurement, it represent TTR stands for Total Tax representing the Effective Tax Rate suffered by an average medium-sized local business in Nigeria..

Decision Rule: Level of significance (α) = 0.05

Model Three

Model Three which takes the form of a multiple regression is used for Hypothesis Three.

H_o: Tax Reforms do not have a significant positive effect on Nigeria's FDI (net inflow)

In line with the above research model of Hartman (1984) and Young (1988), Alli (2015) adapted the following regression equation to investigate the elasticity of corporate tax rate to FDI (Net Inflow) in Nigeria.

$$FDI = a_0 + ß1CTR +_{e1}LnGDP +_{e2} EXCR +_{e3}IFL + \mu.$$

Where: FDI = Foreign direct investment net inflow (% of GDP); CTR = Corporate tax rate.
LnGDP = Natural Logarithm of Gross domestic product; EXCR = Exchange rate; and
IFL= Inflation rate. As an adaptation from the above regression model of Alli (2015), we hereby specify the main model for this study as follows:

$$\boldsymbol{LogFDI = \alpha_0 + b_1ETR + c_2EPTD + d_3TGDP + f_5LogGDP + g_6LogTaxRev + \varrho \ldots\ldots\ldots\ldots (3)}$$

Where:
α, is the *intercept;*
ETR, is Effective Corporate Tax Rate time-series data, that is Nigeria's 'Total Effective Corporate Tax Rate' as computed and used by the World Bank/PWC in their *Ease of Paying Taxes Annual Survey Report as Total Tax Rate (TTR).*

EPTD stands for *"Ease of Paying Taxes Distance to Frontier".* This is Nigeria's percentage distance from the annual global best in the WorldBank/PWC Annual Ease of Paying Taxes Survey index. When compared across the years, it reflects how much a tax system has changed over the years due to reform.

TGDP *(Tax-GDP Ratio)* is Nigeria Total (Both Federal and States Govt.'s) Tax Revenue Ratio to GDP for each of the years under study.

LogGDP is natural logarithm of Nigeria's GDP time series data for the period: 1990 – 2017

LogTaxRev is Natural Logarithm of Nigeria's Tax Revenue Times Series data for the period of 1990 – 2015; whereas **ϱ,** is the error margin

Decision Rule: Level of significance (α) = 0.05

3.4.2 Description/Justification of the Variables

Variables in the study comprised of both dependent and independent variables as described below. These include variables that are determinants of FDI inflow and retention. The determinants of FDI flow can be broadly grouped into:

- Demand and Supply Factor ***represented by*** Market Size, usually proxied by GDP
- Institutional Factor ***represented by*** FIRS and States BIRS Tax Revenue Collections
- Macroeconomic Factors ***represented by*** Tax Rate, Tax System Ratings, GDP growth rate and Inflation rate

1. **Foreign Direct Investment (Net Inflow)** is the aggregate inflow of FDI into the country from all other countries of the world and from the various components less aggregate divestments. World Bank (2010) defines FDI (Net Inflow) *as the value of inward direct investment made by non-resident investors in the reporting economy, including reinvested earnings and intra-company loans, net of repatriation of capital and repayment of loans.* This study focuses not just on the impact of taxation on FDI attraction (inflow) but also on the retention of same hence the adoption of this FDI data that reflects both features.

2. **Tax Indicators** – ***TTR*** (Total Tax Rate) and ***EPTD*** (Ease of paying Tax Distance to Frontier). Effective Corporate Tax Rate shall be proxied by *Total Tax Rates (percentage of commercial profit)* as computed and used by the World Bank and PriceWaterhousCoopers in their *Ease of Doing Business/Ease of Paying Taxes Annual Survey Report of several years.* This index is today recognized as the highest global rating for tax systems. Total Tax Rate (TTR) measures the amount of taxes and mandatory contributions payable by businesses after accounting for allowable deductions and exemptions as a share of commercial profits. This aptly captures the actual burden or cost of Tax Compliance in Nigeria hence its adoption this study. It differs from the statutory tax rate, which merely provides the factor to be applied to the tax base. In computing the total tax and contribution rate, the actual tax or contribution payable is divided by commercial profit, (WorldBank/PWC, 2018). The Total Tax Rate model is mathematically stated as follows:

$$TTR = \frac{Tx - D}{CP} \times 100 \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots \quad (4)$$

Where:

***TTR** is Total Tax Rate, **Tx** is Tax payment, **D** is deductions or adjustment for deductions and exemptions, and **CP** is Commercial Profit*

This is adopted from World Bank Ease of Paying Taxes methodology for computation of Total Tax Rate (TTR). Empirically, is in line with *Becker et. al. (2005*) ex-ante or backward-looking effective tax rate. This study believes, as do *De Mooij and Ederveen (2003)*, that the impact of taxation on investment should focus on the tax rate effectively experienced by firms and not just the headline statutory tax rate. Although the statutory tax rate is important for profit shifting by multinational corporations, it does not necessarily influence the allocation of real capital and so can be misleading, hence our decision to use "Effective Corporate Tax Rate" in the empirical analysis of this work as against the more common statutory rate used by previous empirical works reviewed on the Nigeria's FDI-Tax nexus.

3. **Gross Domestic Product (GDP):** In 2014, Nigeria's GDP was rebased using 2010 as the base year to replace 1990 previously used. Thus the data used here is the Post GDP-Rebasing Revisions of GDP at Constant Basic Price (Nominal GDP), 1990 – 2017, which supersedes previous GDP estimates.

3.5 Techniques of Analysis.

Data for the research variables collected will be analyzed in *chapter four* using charts, tables, diagrams and figures, etc. Relevant tables and charts from studies and reports sourced from recognized international organizations' report were also adopted in this study. Measures of central tendency; mean, mode, median and percentages will also be used in analyzing the data. Testing of models specified along hypotheses will be done using descriptive and inferential statistics tools such as correlation, regression techniques and trend analysis. Data diagnostic tools such ADF-Statistics will be used to X-ray the data for non-stationarity *(which violates one of the classical linear assumptions)* and the necessary transformations to derive a set of data having stationarity and non-spurious features carried out.

CHAPTER FOUR

DATA PRESENTATION AND ANALYSIS

INTRODUCTION

This chapter presents the time series data collected and used for statistical/econometric analyses carried out in this work. Each of the variables were subjected to diagnostic test to take care of non-stationarity usually associated with times series data. The study went further to analyze the findings in line with the objectives/hypotheses stated in chapter one. The econometric models specified in chapter three was used to test the hypotheses proposed based on the decision rules, thus, provide answers to the research questions earlier on asked. The policy implication of each findings is also discussed here.

Table 4. 1 DATA PRESENTATION

1 Year	2 FDI (N'M)	3 Tax Rev N'B	4 GDP (N'B)	5 Tax/GDP Ratio (TGDP) %	6 FDI/GDP Ratio (FGDP) %	7 INFLN %	8 TTR (Total Tax Rate) %	9 EPTD* (Ease of Paying Tax Index) %Points
1990	4,686.00	32.66	19,690.41	0.17	1.911	7.4	30.35	33.4
1991	6,916.10	45.58	19,558.81	0.23	2.601	13	30.35	33.4
1992	14.463.10	62.14	19,643.64	3.18	3.06	44.6	30.35	33.4
1993	29,660.30	74.53	20,054.30	0.32	8.521	57.2	30.35	33.4
1994	22,200.20	73.23	20,236.72	0.37	10.83	57	30.35	33.4
1995	75,900.00	102.49	20,174.50	0.51	3.781	72.8	30.35	35.7
1996	111,300.00	125.87	21,181.95	0.60	4.554	29.3	30.35	35.7
1997	110,500.00	158.17	21,775.52	0.73	4.297	8.5	30.35	35.7
1998	80,700.00	128.61	22,366.87	0.58	3.285	10	30.35	35.7
1999	92,800.00	206.01	22,472.94	0.92	2.801	6.6	30.35	35.7
2000	116,000.00	493.09	23,668.07	2.10	2.458	6.9	30.35	35.7
2001	132,400.00	646.02	24,712.08	2.61	2.697	18.9	30.35	39.8
2002	225,200.00	523.51	25,647.35	2.04	3.17	12.9	30.35	40.16
2003	258,400.00	821.85	28,302.92	2.90	2.964	14	30.35	40.16

2004	248,200.00	1329.25	37,851.13	3.51	2.133	15	31.1	40.16
2005	654,193.15	1864.54	39,154.98	4.76	4.439	17.9	31.3	39.8
2006	624,520.73	1991.43	42,369.98	4.70	3.338	8.2	31.3	39.8
2007	759,380.43	2152.61	45,263.17	4.80	3.626	5.4	31.3	39.8
2008	971,543.79	3325.26	48,101.29	6.91	3.939	11.6	31.3	39.8
2009	1,273,815.79	2658.82	51,436.36	5.20	5.048	11.5	31.3	39.8
2010	905,730.77	3259.68	55,469.35	5.88	1.633	13.7	31.8	39.58
2011	1,360,300.00	5118.78	58,180.35	8.80	2.147	10.8	32.2	39.58
2012	1,113,500.00	5588.01	60,670.05	9.21	1.534	12.2	32.4	36.07
2013	875,100.00	5467.69	63,942.85	8.55	1.08	8.5	32.4	32.63
2014	738,200.00	5422.54	67,977.50	7.97	0.818	8.1	33.3	32.17
2015	602,100.00	4424.43	69,780.69	6.34	0.652	9	34.3	32.62
2016	1,330,398.00	4107.92	68,652.43	5.98	1.098	15.7	34.8	32.17
2017	1,258,920.00	4931.53	69,211.63	7.13	0.931	16.5	34.8	28.09

Sources: *columns (2-7), Central Bank of Nigeria 2015 – 2017 Statistical Bulletin; columns (8-9), World Bank Doing Business/Ease of Paying Taxes Data Bank 2004 - 2018*

** Ease of Paying Taxes Distance to Frontier (EPTD) Score: 0%= lowest performance; 100%=Frontier/Best Practice/Highest performance*

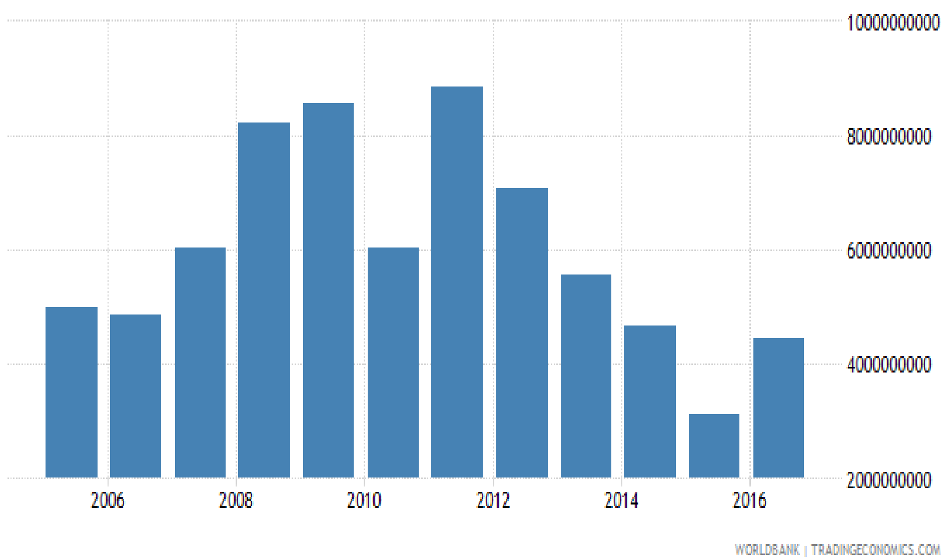
4.2 TREND ANALYSIS OF DATA FOR KEY VARIABLES OF THE STUDY

From the table above, one can easily glean that there was remarkable improvement in Nigeria's federally collected tax revenue due to the effect of arguably the most significant and potent tax reform embarked upon by the government at the return of democracy in 1999. These reforms began in 2004 with the implementation of the harmonized reports and recommendation of both the Study Group and the Working Group. One important indication of the monumental achievements produced by the reforms since 2004 under the leadership of the then Executive Chairman, Federal Inland Revenue Service (FIRS), Ifueko Omoigu-Okairu is that, in the eight year of the reforms alone (that is, in 2012), the actual collection of 5.972 trillion naira (N5,972 trillion) in federally collected taxes was over and above the cumulative collection for the fourteen year period (1990-2003) preceding the reforms – which amounted to only 3.493 trillion naira (N3,493.76 trillion), and nowhere close to the 27.288 trillion naira (N27,288 trillion) collected over the eight years (2004 -2012) following the reforms . However, there was little or no improvement in the overall effectiveness of Nigeria's Tax System as indicated in the increase in Effective Corporate Tax Rate (ETR) – 31.08% average and Ease of Paying Taxes Distance to Frontier (EPTD) that has averagely been less than half (50%) the end-point or best performance (100%) over the years – hovering around average of 31.54 percentage point during the last five years ranking among the worst (two percent) performing economies within the same period – 182 out of 190 economies in 2017.

The Total Tax Rate (effective corporate tax rate) represent the actual burden of taxation borne by average investor in the economy (both local and foreign) and a reflection of the state of the tax system relative to other economies and the impact of reforms over the years. Little wonder the low level of economy's FDI profile relative to GDP which has fluctuated over the years with the highest inflows relative to GDP recorded in far back 1993-1994 which has been on the downward spiral since 2010, perhaps due to the rebasing of the GDP. EPTD (Ease of Paying Taxes Distance to Frontier) has been low (average of 36.3 % point) over the period under consideration. It though picked up (40.16 % point) at the early years of commencement of the recent tax reforms (2001-2004) but slumped again to (39.8 % point) where it stagnated for a period of 7 years (2005 - 2012) after which it nose-dived to 36.07 in 2013 and worse it got for the remaining years (which altogether indicated a deterioration of the tax system notwithstanding the tax reforms and the resultant improved tax revenue collection.

The Distance to Frontier (DTF) score benchmarks economies with respect to regulatory best, showing the absolute distance to the best performance on each Paying Taxes/Doing Business indicator. The distance to frontier score captures the gap between an economy's performance and a measure of best practice. When compared across years, the distance to frontier score shows how much the regulatory environment for local entrepreneurs in an economy has changed over time in absolute terms, while the Ease of Doing Business/Paying Taxes ranking can show only how much the regulatory environment has changed relative to that in other economies, (World Bank, 2016). Nigeria's taxation worsened in both critical indices that influence foreign investors' offshore investment decision. Moreso, Tax compliance rate in Nigeria is still very low hovering around average of 6% of GDP compared to an average of about 15% for Africa (Kenya 19%, Ghana 23%, and South Africa 25%). According to the World Bank Group (WBG), Nigeria ranks 182 out of 190 benchmarked economies on the Paying Taxes sub-index under the Ease of Doing Business Index for 2017. The distance to frontier score is 28.09%, which implies that Nigeria is about 72 percentage points (or 72 places) away from the best performance observed under the Paying Taxes sub-index. The conclusion from these two benchmarks is that Nigeria needs to embark on a significant tax reform to improve its ranking. There are two main areas, based on the 2017 WBG report, which Nigeria needs to address: ***reduction in the number of tax payments and the administrative burden involved in paying taxes in the country***. The import of the result of the above trend analysis is that the effect of the recent reform of Nigeria's tax system still leaves much to be desired as the system is still grossly ineffective both in harnessing the huge revenue potential of Nigeria's economy and in the quantity and quality of her FDI (Net Inflow) which is presently very low at an average value of N438.2Million over the 28 years period of this study

Figure 4.1: Nigeria FDI (Net Inflow), 2005 -2017



Source: WorldBank

4.3 DESCRIPTIVE STATISTICS

Table 4.2

	EPTD	GDPRT	INFL	LogFDI	LogGDP	LogTAXREV	TGDP	TTR
Mean	36.63731	5.650000	18.88462	12.23421	9.278206	6.432471	6.072941	31.08269
Median	35.70000	4.650000	11.90000	12.42199	9.415522	6.591194	6.351286	30.35000
Maximum	40.16000	33.70000	72.80000	14.12322	11.45259	8.628379	8.491931	34.30000
Minimum	32.17000	-0.600000	5.400000	8.452335	6.213968	3.486151	2.802577	30.35000
Std. Dev.	3.017292	6.565440	18.09247	1.606189	1.628062	1.747145	1.702388	1.073121
Skewness	-0.073203	3.111652	1.861164	-0.804133	-0.341508	-0.207848	-0.401490	1.475195
Kurtosis	1.403628	14.04742	5.179250	2.839605	1.957848	1.551962	1.969428	4.501304
Jarque-Bera	2.783991	174.1729	20.15526	2.721093	1.681973	2.458754	1.849094	11.87194
Probability	0.248579	0.000000	0.000042	0.256521	0.431285	0.292475	0.396711	0.002643
Sum	952.5700	146.9000	491.0000	305.8552	241.2333	167.2442	157.8965	808.1500
Sum Sq. Dev.	227.6013	1077.625	8183.434	61.91625	66.26461	76.31286	72.45311	28.78971
Observations	28	28	28	28	28	28	28	28

Source: Authors computation using E-Views version 10

***Key to Abbreviations**:*

EPTD *stands for* *Ease of Paying Taxes Distance to Frontier*
GDPRT " *GDP Annual Growth Rate*
INFL " *Annual Inflation Rate*
LogFDI " *Logarithm of FDI*
LogGDP " *Logarithm of GDP*
LogTAXREV " *Logarithm of Tax Revenue*
TGDP " *Tax-GDP Ratio*
TTR " *Total Tax Rate (Effective Corporate Tax Rate)*

Table 4.2 above contains a summary statistics that quantitatively describes or summarizes the statistical features of the relevant variables used for the study. Unlike an inferential statistics such as regression analysis, it summarizes the statistical features of a sample rather than give information about the population, and by so doing provide a clear and precise understanding of the variables as normal distributions. Table 4.2 therefore shows that on average, FDI (log) inflow to Nigeria for the whole period (1990 – 2017) stand at 12.23 with the highest FDI inflow of 14.2 and the lowest of 8.45. This indicates a standard deviation of 1.60. The result shows a disturbing situation for Nigeria's Tax/GDP Ratio which is about 6% compared to an average of about 15% for Africa and 45% for OECD Countries. This is about the lowest in the world, even in Africa and far below Africa average of about 15%. FDI inflow at a paltry average sum of

N438.2Million calls for an urgent policy action by government to make the country more FDI-friendly which will in turn boost economic recovery and growth.

Figure 4.2 Multiple Bar Chart illustrating Annual Time Series Data for each of the Variables

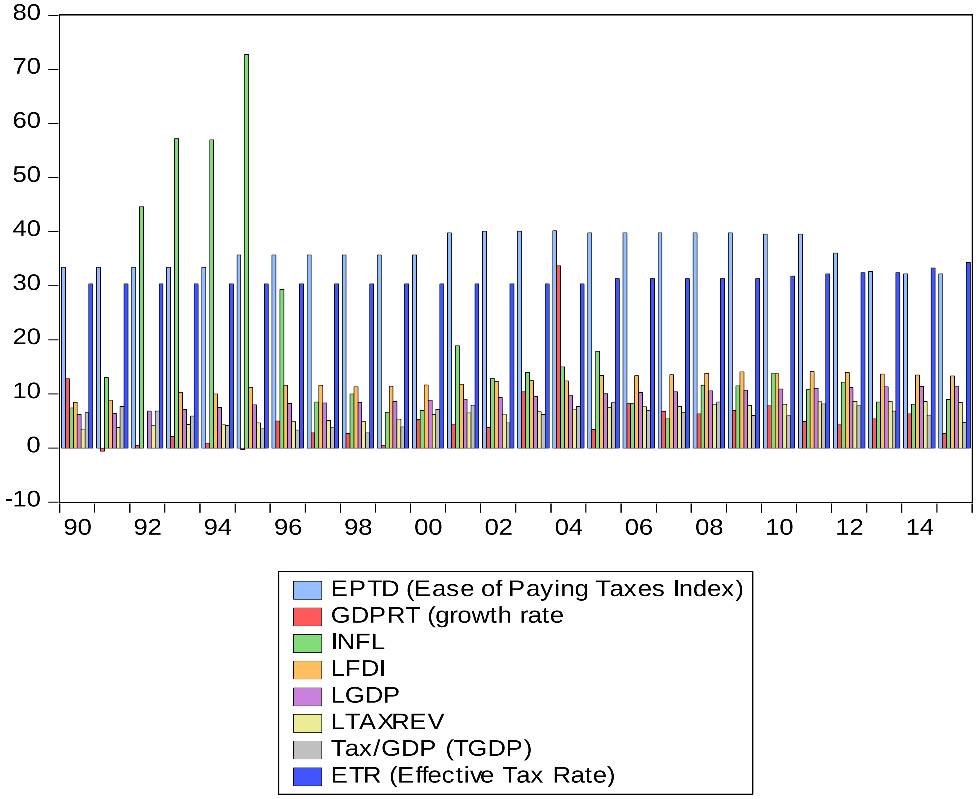


Figure 4.3 Nigeria Total Tax Rate (% of Profit)

Source: World Bank Doing Business Data bank

Figure 4.4 Line Graph depicting the variables on a plane

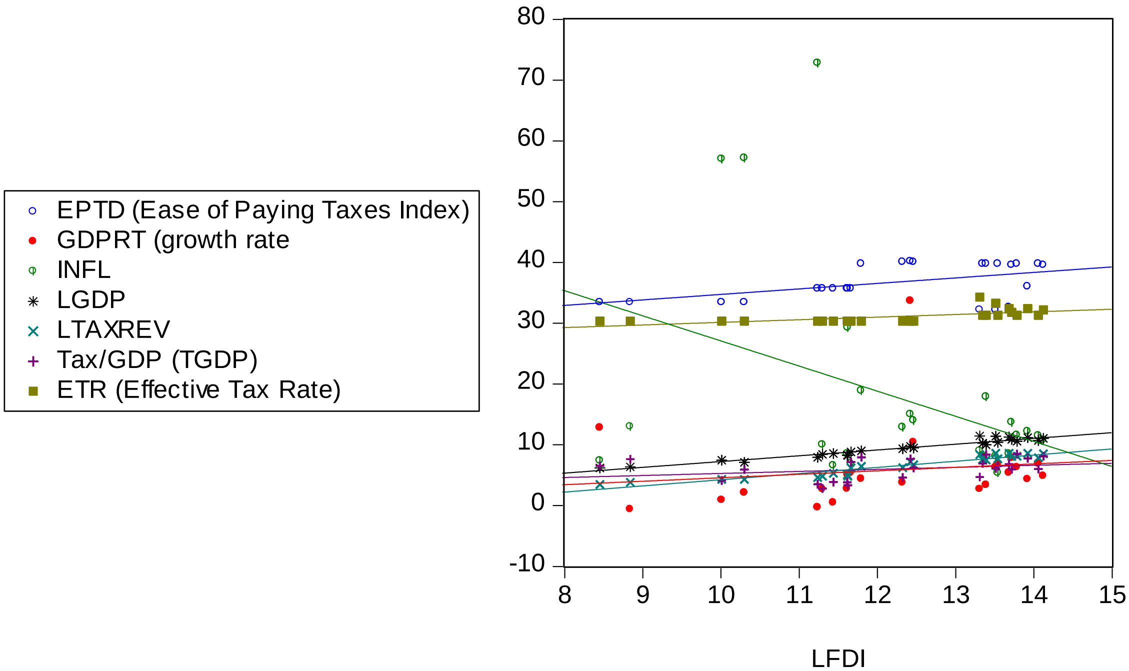


Figure 4.5 Graph depicting Data for each of the Variables between 1990 and 2015

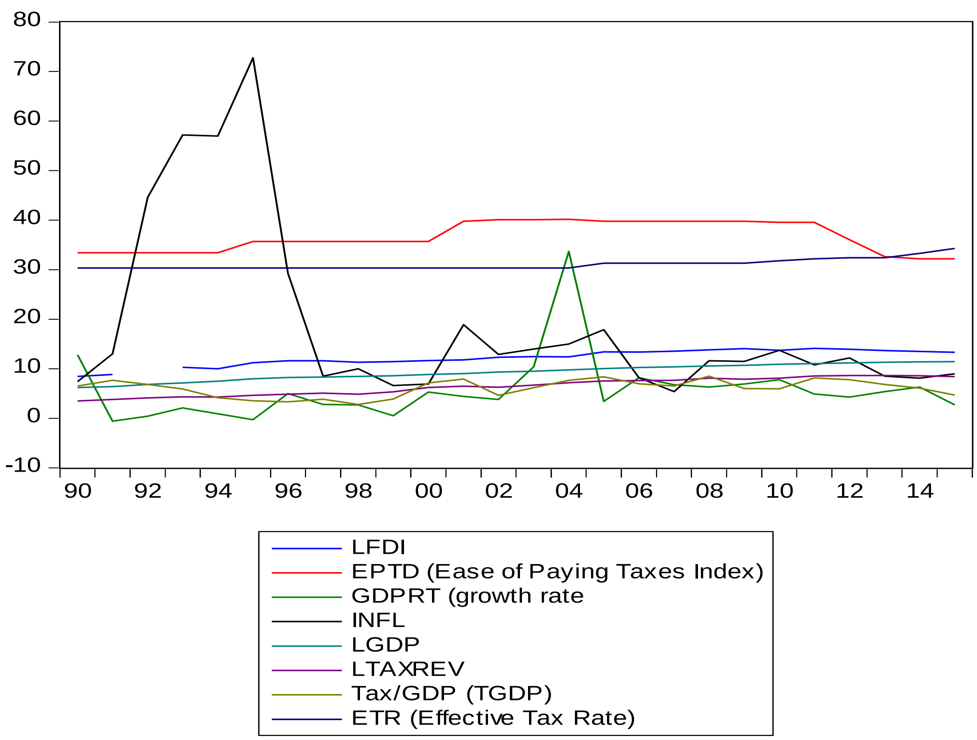


Table 4. 3

Covariance Analysis: Ordinary

Date: 11/12/17 Time: 09:57

Sample: 1990 2015

Included observations: 28

Balanced sample (list wise missing value deletion)

Correlation t-Statistic Probability	EPTD	GDPRT	INFL	LFDI	LGDP	LTAXREV	TGDP	ETR
EPTD	1.000000							
GDPRT	0.360092 1.851119 0.0770	1.000000						
INFL	-0.224390 -1.104297 0.2809	-0.252575 -1.251899 0.2232	1.000000					
LFDI	0.483199 2.646847 0.0144	0.138592 0.671142 0.5088	-0.375581 -1.943506 0.0643	1.000000				
LGDP	0.331255 1.683706 0.1058	0.170884 0.831765 0.4141	-0.442168 -2.364243 0.0269	0.966800 18.14478 0.0000	1.000000			
LTAXREV	0.367669 1.896089 0.0706	0.221603 1.089870 0.2871	-0.470345 -2.556078 0.0177	0.948152 14.30758 0.0000	0.984338 26.77780 0.0000	1.000000		
TGDP	0.360026 1.850728 0.0771	0.333867 1.698637 0.1029	-0.338079 -1.722815 0.0983	0.311025 1.569466 0.0006	0.329541 1.673929 0.1077	0.489036 2.688794 0.0131	1.000000	
ETR	-0.228802 -1.127196 0.2713	-0.070331 -0.338133 0.7383	-0.318602 -1.611963 0.1206	-0.638324 3.976905 0.1302	0.775717 5.894986 0.0000	0.759392 5.597492 0.0000	0.213095 1.045994 0.3064	1.000000

Source: Researcher's computation using E-Views Version 10

As indicated in the result above, FDI and EPTD (index for investors perception of Nigeria's Tax System) are *positively signed (0.4831)* indicating that the better Nigeria's tax system is perceived by investors, the more FDI (Net Inflow) available to the economy. On the other hand, ETR (Effective Corporate Tax Rate) is *negatively signed (-0.6383)* with FDI, implying that as Effective Corporate tax rate decrease, FDI flows into Nigerian economy, vice versa

4.4 ADF UNIT ROOT TEST (Test for Stationarity)

To side step spuriousness in the regression estimates we initially employed the well-known Augmented Dickey-Fuller (ADF) Unit Root Tests. From the above table, the ADF statistics are all more negative than the critical values of 5%, hence the tests reveal that our data satisfies the requirement for stationarity (No Unit Root) and by extension classical linear assumptions.

The unit root (stationarity) test was performed to ascertain the stationarity of the variables under study so as to avoid running a spurious regression and making a non-meaningful conclusion. This test adopted Augmented Dickey-Fuller (ADF) approach and decision was based on 5% level of significance.

Table 4.4 Result of the ADF Unit Root Test

Variable	ADF-Stat	Critical value @5%	p-value	Order of Integration
FDI	-4.99	-3.01**	0.0007	1(1)
ETR	-3.78	-3.61**	0.0360	1(1)
EPTD	-3.82	-2.96**	0.0070	1(1)
TGDPRT	-3.88	-3.61**	0.0291	1(0)
INFL	-4.03	-3.63**	0.0229	1(0)

** Indicates stationarity at 5% level of significance

SOURCE: Researcher's extract from E-views output (See Appendix 1I)

The result above shows that the variables were not stationary at same level. The rejection of the null hypothesis was based on the ADF-stat. being more negative than the critical value at 5% level of significance. This informs the choice of the Autoregressive Distributed Lag (ARDL) because it accommodates a combination of 1(1) and 1(0) variables.

4.5 Analysis of Regression/Correlation Test Result

***HYPOTHESIS ONE*:**

H_{o1}: *Foreign direct investment has no significant effect Nigeria's economic growth*

H_{11}: *Foreign direct Investment has significant effect on the Nigeria' economic growth*

The Ordinary Least Square (OLS) method of regression analysis was used for hypothesis one and the results are shown below:

Dependent Variable: LOG(FDI)
Method: Least Squares
Date: 06/02/18 Time: 09:16
Sample: 1990 2017
Included observations: 28

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOG(GDP)	0.897529	0.258515	3.471870	0.0041
INFL	-0.120151	0.061234	-1.962170	0.0715
C	-1.916114	7.003048	-0.273611	0.7887

R-squared	0.659115	Mean dependent var	19.91817
Adjusted R-squared	0.606671	S.D. dependent var	1.328483
S.E. of regression	0.833170	Akaike info criterion	2.640203
Sum squared resid	9.024239	Schwarz criterion	2.785063
Log likelihood	-18.12162	Hannan-Quinn criter.	2.647621
F-statistic	12.56803	Durbin-Watson stat	1.696987
Prob(F-statistic)	0.000916		

SOURCE: Researcher's extract from the E-Views 10 output

The result of the test as shown above shows a significant positive relationship between FDI and GDP. *The Null hypothesis is therefore rejected*. This implies that for every 1% increase in FDI, Nigeria's GDP (Economic Growth) grows by 0.8975 or 0.9%. The Adjusted R^2 figure of 60.6 indicates that variation in GDP is explained by changes in FDI. The p-value of 0.0041 further shows that the estimates are statistically significant at 0.05 level of significance. The OLS result is further buttressed by the correlation result which shows a high positive correlation of 0.82 between the two variables. This is line with the findings of Egbo (2010), using similar data and econometric analysis, reported that Foreign Direct Investment (FDI) is a major determinant and driver of economic growth in Nigeria. The works of Oyaide (1977), Eke et al. (2003), and Ugochukwu, et al (2013) also found a positive and significant relationship between FDI and economic growth in Nigeria as well as other economies

HYPOTHESIS TWO

H_o: There is negative correlation between taxation and FDI (net inflow) in Nigeria.

H_1: There is positive correlation between taxation and FDI (net inflow) in Nigeria.

Level of significance (α) = 0.05

Table 4.3

Covariance Analysis: Ordinary

Date: 11/12/17 Time: 09:57
Sample: 1990 2015
Included observations: 28
Balanced sample (list wise missing value deletion)

Correlation t-Statistic Probability	EPTD	GDPRT	INFL	LFDI	LGDP	LTAXREV	TGDP	ETR
EPTD	1.000000							
GDPRT	0.360092	1.000000						
	1.851119							
	0.0770							
INFL	-0.224390	-0.252575	1.000000					
	-1.104297	-1.251899						
	0.2809	0.2232						
LFDI	0.483199	0.138592	-0.375581	1.000000				
	2.646847	0.671142	-1.943506					
	0.0144	0.5088	0.0643					
LGDP	0.331255	0.170884	-0.442168	0.966800	1.000000			
	1.683706	0.831765	-2.364243	18.14478				
	0.1058	0.4141	0.0269	0.0000				
LTAXREV	0.367669	0.221603	-0.470345	0.948152	0.984338	1.000000		
	1.896089	1.089870	-2.556078	14.30758	26.77780			
	0.0706	0.2871	0.0177	0.0000	0.0000			
TGDP	0.360026	0.333867	-0.338079	0.311025	0.329541	0.489036	1.000000	
	1.850728	1.698637	-1.722815	1.569466	1.673929	2.688794		
	0.0771	0.1029	0.0983	0.0006	0.1077	0.0131		
ETR	-0.228802	-0.070331	-0.318602	-0.638324	0.775717	0.759392	0.213095	1.000000
	-1.127196	-0.338133	-1.611963	3.976905	5.894986	5.597492	1.045994	
	0.2713	0.7383	0.1206	0.1302	0.0000	0.0000	0.3064	

SOURCE: *Researcher's extract from the E-Views output*

From the above result, *EPTD*, representing impact of tax reform and investors overall perception of Nigeria's Tax system as reported in World Bank/PWC Annual Ease of Paying Taxes Survey is positively correlated with *FDI (Net inflow)*; *LTAXREV*, Nigeria's Federally Collected Taxes is positively correlated with *FDI (Net Inflow); TGDP*, Ratio of Tax Revenue to *GDP* is also positively correlated to *FDI (Net Inflow)* whereas *ETR*, Effective Corporate Tax Rate, being the effective corporate tax rate burden borne by an average Nigeria's medium-sized manufacturing company is negatively correlated with *FDI (Net Inflow).*

HYPOTHESIS THREE

H_o: Taxation does not have a significant positive effect on FDI inflow in Nigeria.

H_1: Taxation has a significant positive effect on FDI inflow in Nigeria.

Dependent Variable: LFDI
Method: ARDL
Date: 11/21/17 Time: 14:36
Sample (adjusted): 1992 2017
Included observations: 26 after adjustments
Maximum dependent lags: 2 (Automatic selection)
Model selection method: Akaike Info Criterion (AIC)
Dynamic regressors (2 lags, automatic): EPTD ETR GDPRT INFL
Fixed regressors: C
Number of models evaluated: 162
Selected Model: ARDL(1, 2, 2, 2, 1)
Note: final equation sample is larger than selection sample

Variable	Coefficient	Std. Error	t-Statistic	Prob.*
LFDI(-1)	-0.173254	0.455413	-0.380433	0.7124
EPTD	0.195006	0.076423	2.551675	0.0311
EPTD(-1)	0.018808	0.094275	0.199500	0.8463
EPTD(-2)	0.128731	0.109986	1.170429	0.2719
ETR	0.341532	0.502712	0.679379	0.5140
ETR(-1)	-0.222354	0.655138	-0.339401	0.0543
ETR(-2)	1.320702	0.689010	1.916811	0.0875
GDPRT	-0.011826	0.012162	-0.972404	0.3563
GDPRT(-1)	0.007614	0.022962	0.331609	0.7478
GDPRT(-2)	0.024386	0.021453	1.136722	0.2850
INFL	-0.016463	0.011805	-1.394567	0.1966
INFL(-1)	0.013031	0.008311	1.567853	0.1514
C	-42.60859	15.99704	-2.663530	0.0259

R-squared	0.970172	Mean dependent var	12.64835
Adjusted R-squared	0.930401	S.D. dependent var	1.166600
S.E. of regression	0.307767	Akaike info criterion	0.769054
Sum squared resid	0.852486	Schwarz criterion	1.413761
Log likelihood	4.540401	Hannan-Quinn criter.	0.920928
F-statistic	24.39415	Durbin-Watson stat	2.112706
Prob(F-statistic)	0.000022		

From the Autoregressive Distributed Lag Regression result shown above, we have that 'Taxation' or Tax Reform as proxied by EPDT has a significant and positive relationship with the inflow of Foreign Direct Investment into Nigerian economy. We therefore *reject* the null hypothesis and *accept* the alternative hypothesis. The result implies that one per cent point change in Nigeria's Annual EPTD index will result in about 0.2% increase in the FDI (Net Inflow) of the economy.

4.6 Discussion of Results and Policy Implication/Usefulness

1. The result of the analysis of hypothesis one which provides answer to our first research question indicate that there is a significant positive relationship between FDI and GDP. This implies that for every 1% increase in FDI, Nigeria's GDP (Economic Growth) grows by 0.8975 or 0.9%. This means that changes in GDP is significantly affected by changes in FDI inflow, implying that FDI is verifiably important to Nigerian economy and should be further encouraged. FDI can contribute to economic growth through capital flows, technology transfer, employment creation, etc. These benefits are not, however, automatic. There is strong evidence pointing to the potential for significant spillover benefits from FDI, but also ample evidence indicating that spillovers do not occur automatically, Nunnenkamp (2004). The benefits derived from FDI depend on the sector in which investment is made and on the level of socio-economic development of the host country. Investment in the primary sector has fewer positive spillovers than investment in the manufacturing sector. For Nigeria, this calls for strategic attraction of investments that will enhance the growth and development of relevant sectors of the economy. This answers the ***first research question*** of this study in the positive – FDI contributes significantly to economic growth in Nigeria.
2. The result of the covariance analysis of hypothesis two shows that taxation is positively correlated with FDI (net inflow) in Nigeria. The first three variables - EPTD, LTAREV, TGDP can all reasonably be associated with tax reform as any improvement on them can easily be attributed to positive effect of tax reforms. On the other hand, ETR – Effective Corporate Tax Rate of Nigeria is negatively but insignificantly correlated with FDI (Net Inflow). Because the first three variables have a more holistic representation of a tax system especially investors' perception of the system and have significant effects with FDI, the null hypothesis was rejected.This, ***in response to the second research question*** of this study, confirms that there is a significant positive relationship between taxation and FDI in Nigeria. Findings of this study is in tandem with recent WorldBank, UNCTAD and IMF reports which confirm that investors are now more interested in the overall economic effect of a country's tax system or burden of tax compliance on their

investment *(which is the focus and taxation conception of this study)* than just the effect of tax rate.

Hence, Nigeria government while attending to her need to shore up tax revenue should also pay reasonable attention to this area of her tax system that will directly impact and improve on investors' perception of her tax system and World Bank Doing Business Rating especially the paying taxes index. According to a recent World Bank (2018) report, the simplicity, transparency and certainty of the tax rules and procedures matter more to an average foreign investor than the headline statutory rate.

3. The analysis of hypothesis three test result indicate that taxation or tax reform as proxied by EPDT (a very objective and internationally recognized reflection of the investment friendliness of an economy's tax system) is positively and significantly related to FDI (net-inflow). This implies that the higher Nigeria ranks on the World Bank Annual Ease Paying Taxes Survey as a result of positive impact of tax reforms, the more FDI is attracted and retained in the economy. The above result is further buttressed by a positive correlation (0.4832) between FDI and EPTD implying that a rise (or improvement) in Nigeria's Ease of Paying Taxes Ranking will certainly lead to an increase in her FDI (Net inflow). Thus, in response to our ***third and main research question,*** tax reforms have significant positive effect on Nigeria's FDI (net inflow).

It is important to highlight that the smallness or infinitesimal size of the elasticity between *ETR and FDI - (Coefficient: -0.2223; P-value: -0.0543) implies that Nigeria's Tax Rates has little or no effect on her FDI (Net Inflows).* The result is particularly significant for this study which emphasizes not just the effect of taxation on the inflow of FDI but sustainable reinvestment of retained earnings and non-divestment, hence the use of FDI (Net Inflow) as the proxy for FDI variable. Since tax reform has a significant positive effect on FDI inflow in Nigeria". The policy implication of this result is that the overall impactful and sustained reform of Nigeria Tax System will avail Nigeria of more FDI (Net Inflows) rather than mere reduction of tax rates or wasteful package of tax incentives. As highlighted above recent (2017) WorldBank Survey, what currently matters to FDI investors is the overall Investment Climate, of which the tax system is an critical part of. FDI responds to the extent to which a tax system is perceived to be business-friendly *because modern Investors look for certainty, predictability, consistency, transparency,* *simplicity and timeliness in the application of tax rules and in many cases these considerations are as important, if not more important than the statutory tax rate paid, OECD (2008).*

Overall, analysis of the econometric test results as well as the trend analysis of the research data, descriptive statistics and graphical representations indicate that though the recent tax reforms appear to have impacted positively and significantly on FDI (net inflow) as the regression analysis suggests, a more careful analysis and synthesis of the results, especially the trend analysis which is a more pragmatic examination of the effect of reforms, show that the reform is still largely ineffective not only in terms of its tax revenue accretion objective but also in the area of enhancing investment and business climate of the economy, hence the continued elusiveness and low contribution index of the critically needed Foreign Direct Investment. Instructively therefore, the reform should be retooled and refocused. A simple tax system with low tax compliance burden will to a great extent enhance the attractiveness of the investment climate of Nigeria's economy!

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 SUMMARY OF FINDINGS

This section highlight the objectives of the study, the methodology adopted and summarizes the various research findings which are derived from the objectives of the study outlined below.

Objectives of the Study

i. assess the impact of FDI on the growth of Nigeria economy;
ii. measure the relationship between taxation and FDI (net-inflow) in Nigeria during the period under review; and
iii. assess the effect of tax reforms on Nigeria's FDI (Net-Inflow).

Methodology

The study adopted the *ex-post facto* design. The ordinary least square method of multiple regression analysis, at 5% Level of Significance and statistical trend analysis were used to analyze the data and hypotheses formulated. The study employed annual time series secondary data spanning the years (1990 -2017) sourced from the Central Bank of Nigeria Statistical Bulletins and The World Bank/PWC Annual Ease of Doing Business Survey Reports in carrying out its statistical and econometric analysis. Diagnostic test result showed that the variables were not stationary at same levels hence the use of the Autoregressive Distributed Lag (ARDL) method of Regression Analysis since it accommodates a combination of 1(1) and 1(0) variables.

Summary of Findings

Below is a summary of the findings as hinged on the objectives of the study:

1. FDI (net inflow) has positive and significant impact on the growth of Nigerian economy (($\beta = 0.087$, $p = 0.0041 < 0.05$),
2. Taxation has a positive and significant correlation/relationship with FDI (net inflow) ($\beta = -0.0246$, $p = -0.0543 < 0.05$)
3. There is a significant positive effect of Tax Reform on FDI (Net Inflow) ($\beta = 0.1950$, $p= 0.031 < 0.05$).

5.2 CONCLUSION

Foreign direct investment contributes to economic growth through capital flows, technology and know-how transfer, employment creation which can result in remarkable poverty reduction and economic development if the *right* flow is sustained. Countries more open to trade and investment tend to be more productive and grow faster (World Bank, 2017). The above finding is in tandem the first objective of the study.

Furthermore, the study found out that *taxation*, which by this study substantially means the overall perception of Nigeria's tax system by investors based on the effective burden of tax compliance is positively correlated with FDI (Net Inflow). Taxation as proxied by World Bank/PWC ease of Paying Taxes Distance to Frontier (EPTD) has a significant and positive relationship with the inflow of Foreign Direct Investment into Nigerian economy. This means that the higher Nigeria tax system reforms improves upon her tax system as evidenced by sustained improvement on distance to frontier (EPTD), the more FDI is attracted and retained in the economy. Dysfunctional tax systems, as the World Ease of Paying Taxes Survey reports annually, impede FDI inflow and encourage capital repatriation.

The findings of the study robustly proffers answers to the main research question of this study which is to know if the recent (1990 – 2017) reform of Nigeria's tax system have impacted significantly on FDI (net-inflow). Based on a thorough analysis of the findings we conclude that Nigeria's tax reforms has over the years impacted positively though marginally as trend analysis of relevant components of our research data reveals. **It has not been effective!** However, since *tax reforms* and *FDI (net-inflow)* are positively related, a more robust and sustained reform of the tax system will likely result in higher FDI (Net Inflow). There are two main areas, based on the 2017 WBG report findings of this study, which Nigeria needs to address: ***reduction in the number of tax payments and the administrative burden involved in paying taxes in the country.***

5.3 MAJOR CONTRIBUTIONS OF THE OUTCOME OF THE STUDY TO KNOWLEDGE

- The effect of Nigeria's recent tax reforms on her FDI (net inflow) was for the first time measured by this study. The findings reveal that the reforms has not been as productive or effective as expected but if retooled and refocused, it can have remarkable positive impact on Nigeria's Investment climate with the attendant improvement on her FDI (Net Inflow)

- The use of World Bank Ease of Paying indices such as Ease of Paying Taxes Distance to Frontier and Total Tax Rate (TTR) computed from firm-level data in the regression model is quite remarkable and unprecedented as no research on the Nigeria Tax-FDI nexus has ever been done using them as taxation and tax rate indicators. The World bank Paying Taxes Index is highly reputable and today recognized as the highest rating of tax systems, worldover.

- This study established a robust correlation between Nigeria tax system (as perceived by investors) and FDI (Net Inflow) in Nigeria. This is unique as estimates by previous findings were based on tax rate and tax revenue which are very poor representation of a tax system especially from the point of view of investment. This is quite remarkable and an unprecedented achievement given the quality of data used.

- This study also generated a coefficient (0.2%) of elasticity between Nigeria's Effective Corporate Tax Rate and FDI (Net-Inflow). This is the responsiveness of FDI (Net-Inflow) to Corporate Effective Tax Rate in Nigeria and unique because of the use of firm level data which captures the actual burden of tax compliance as experienced by medium-sized or average manufacturing firm in Nigeria.

5.4 RECOMMENDATIONS

Based on the foregoing, the following recommendation are hereby proffered:

- **Improvement of General Investment Climate:** The likely response of FDI to host country tax reform very much depends on a wider range of host country conditions, OECD (2002). One should emphasize that tax incentives, financial subsidies and regulatory exemptions directed at attracting foreign investors are not substitute for pursuing the appropriate general policy measures, and focusing in the broader objective of encouraging investment for development regardless of source.

- **Further Reform /Overhaul of Tax System and Machineries**. Tax regimes in developing countries often suffer from weak design, lack of transparency, and cumbersome administration, World Bank (2017). Improving the investment attraction performance of Nigeria apex tax authority, Federal Inland Revenue Service the following:

- ✓ Tax policy documents and laws should be reviewed
- ✓ Better co-operation (via Bilateral Tax Arrangements, Information Exchange, etc) with other Nation's tax administrations to counter tax evasion and aggressive tax planning;
- ✓ Further strengthening of audit and human resource management capability for a more robust, knowledgeable, competent, and professionally engaging tax officers
- ✓ More professional and quality service delivery and taxpayer education;
- ✓ An accelerated expansion of the tax net to increase the number of taxpayers and reduce the ranks of defaulting taxable persons. Expanded tax net will yield more tax revenue and make a more investment-friendly tax regime affordable for Nigeria.
- ✓ Emplacing a more efficient tax system – accelerated debottlenecking of the tax system to ensure a fair, simple and more predictable, administratively efficient and a more tax compliance friendly system for citizens and foreign investors alike.
- ✓ Elimination of multiple taxation - The tax administration processes should be made more transparent, automated and simple

- **Need for a Formal FDI Policy:** There is urgent need for a formal FDI policy in Nigeria. The indices will help policymakers assess the effectiveness of their policy framework and overall FDI contribution too.

- **Building Institutional Capacity:** Relevant public institutions such as courts, FIRS, the Nigeria Investment Promotion Council (NIPC), The Independent Corrupt Practices Commission, Nigeria Customs, the Economic and Financial crimes Commission, etc should be adequately strengthened to monitor and ensure transparency and accountability in the conduct of private and public economic affairs including protection of property rights.

- **Retooling Tax Incentives**

  There is an urgent need to retool Nigeria's. The incentives must be made strategic and FDI-focused. Nigeria must therefore walk a fine line between remaining competitive by offering incentives and ensuring that their benefits outweigh their costs. Reforms to improve the design, transparency, and administration of incentives can help reduce unintended effects and costs, such as economic distortions, red tape, and corruption.

Finally, this study strongly recommends that the Government of Nigeria should embark on a more drastic reform of her tax system in order to boost her FDI (Net Inflow). A continuous and concerted effort that yields the optimal balance between a tax regime that is business friendly and one which can leverage enough revenue for public service is urgently needed. To this extent, the study considers it trite to highlight (OECD, 2006) Policy Guideline Checklist for sound and investment-friendly Tax Policy Framework. The pertinent checklist questions are as follows:

- ***Has*** the government evaluated the level of tax burden that would be consistent with its broader development objectives and its investment attraction strategy? Is this level consistent with the actual tax burden?
- ***What*** is the average tax burden on domestic profits, taking into account statutory provisions, tax-planning opportunities and compliance costs?
- ***Is*** the tax burden on the business enterprises of investors appropriate with reference to the policy goals and objectives of the tax system?

- ***If*** framework conditions and market characteristics for investors are weak, has the government evaluated the limitations of using tax policy alone to influence favourably investment decisions?
- ***Where*** the tax burden on business income differs by firm size, age of the business entity, ownership structure, industrial sector or location, can these differences be justified?
- **Is** the tax system neutral in its treatment of foreign and domestic investors?
- ***Are*** rules for the determination of corporate taxable income formulated with reference to a benchmark income definition (e.g. comprehensive income), and are the main tax provisions generally consistent with international norms?
- ***Have*** targeted tax incentives for investors and others created unintended tax-planning opportunities? Are these opportunities and other problems associated with targeted tax incentives evaluated and taken into account in assessing their cost-effectiveness?
- ***Are*** tax expenditure accounts reported and sunset clauses used to inform and manage the budget process?
- ***Are*** tax policy and tax administration officials working with their counterparts in other countries to expand their tax treaty network and to counter abusive cross-border tax planning strategies

5.5 SUGGESTIONS FOR FURTHER RESEARCH

This central policy and perhaps the main research question of the sensitivity of FDI to taxation is an inconclusive empirical issue. This is because of the variableness of previous empirical work, (Mooij and Ederveen, 2003, Haskana et al 2006; OECD 2012). Hence the following is suggested for further studies.

- The Role of Bilateral Tax Agreements in attraction of FDI in Sub-Sahara African Countries
- The Effect of Taxation on Foreign Direct Investment: a case study of Sub-Sahara African countries
- Transfer Pricing Policy and Practices in Nigeria: Impact on Foreign Direct Investment Inflow.

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Appendix

Null Hypothesis: D(EPTD) has a unit root

Exogenous: Constant, Linear Trend

Lag Length: 0 (Automatic - based on SIC, max lag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-3.883891	0.0291
Test critical values:	1% level	-4.394309	
	5% level	-3.612199	
	10% level	-3.243079	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(EPTD,2)

Method: Least Squares

Date: 11/12/18 Time: 10:08

Sample (adjusted): 1992 2017

Included observations: 26 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(EPTD(-1))	-0.839166	0.216063	-3.883891	0.0009
C	0.934264	0.642948	1.453094	0.1610
@TREND(1990)	-0.072360	0.043528	-1.662369	0.1113

R-squared	0.418049	Mean dependent var	0.000417
Adjusted R-squared	0.362625	S.D. dependent var	1.664889
S.E. of regression	1.329177	Akaike info criterion	3.523466
Sum squared resid	37.10095	Schwarz criterion	3.670723
Log likelihood	-39.28159	Hannan-Quinn criter.	3.562533
F-statistic	7.542752	Durbin-Watson stat	1.934266
Prob(F-statistic)	0.003399		

Null Hypothesis: D(ETR) has a unit root

Exogenous: Constant, Linear Trend

Lag Length: 0 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-3.778695	0.0360
Test critical values:	1% level	-4.394309	
	5% level	-3.612199	
	10% level	-3.243079	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(ETR,2)

Method: Least Squares

Date: 11/12/18 Time: 10:10

Sample (adjusted): 1992 2017

Included observations: 26 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(ETR(-1))	-0.913316	0.241701	-3.778695	0.0011
C	-0.179903	0.131351	-1.369635	0.1853
@TREND(1990)	0.024728	0.009562	2.586062	0.0172

R-squared	0.417681	Mean dependent var	0.041667
Adjusted R-squared	0.362222	S.D. dependent var	0.356513
S.E. of regression	0.284715	Akaike info criterion	0.441811
Sum squared resid	1.702312	Schwarz criterion	0.589067
Log likelihood	-2.301729	Hannan-Quinn criter.	0.480878
F-statistic	7.531357	Durbin-Watson stat	1.836328
Prob(F-statistic)	0.003421		

Null Hypothesis: GDPRT has a unit root

Exogenous: Constant, Linear Trend

Lag Length: 0 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-4.511926	0.0074
Test critical values:	1% level	-4.374307	
	5% level	-3.603202	
	10% level	-3.238054	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(GDPRT)

Method: Least Squares

Date: 11/12/18 Time: 10:10

Sample (adjusted): 1991 2017

Included observations: 27 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
GDPRT(-1)	-0.925249	0.205067	-4.511926	0.0002
C	1.804465	2.753815	0.655260	0.5191
@TREND(1990)	0.240644	0.185920	1.294337	0.2090

R-squared	0.481273	Mean dependent var	-0.404000
Adjusted R-squared	0.434116	S.D. dependent var	8.657727
S.E. of regression	6.512796	Akaike info criterion	6.697581
Sum squared resid	933.1632	Schwarz criterion	6.843846
Log likelihood	-80.71977	Hannan-Quinn criter.	6.738149
F-statistic	10.20577	Durbin-Watson stat	1.871027
Prob(F-statistic)	0.000732		

Null Hypothesis: INFL has a unit root

Exogenous: Constant, Linear Trend

Lag Length: 3 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-4.032233	0.0229
Test critical values:	1% level	-4.440739	
	5% level	-3.632896	
	10% level	-3.254671	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(INFL)

Method: Least Squares

Date: 11/12/18 Time: 10:11

Sample (adjusted): 1994 2017

Included observations: 24 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
INFL(-1)	-0.861571	0.213671	-4.032233	0.0010
D(INFL(-1))	0.380063	0.194366	1.955401	0.0682
D(INFL(-2))	0.313513	0.171022	1.833172	0.0854
D(INFL(-3))	0.464857	0.176225	2.637857	0.0179
C	29.61539	10.53739	2.810505	0.0126
@TREND(1990)	-1.026369	0.469834	-2.184536	0.0441

R-squared	0.529745	Mean dependent var	-2.190909
Adjusted R-squared	0.382790	S.D. dependent var	11.63684
S.E. of regression	9.142217	Akaike info criterion	7.490684
Sum squared resid	1337.282	Schwarz criterion	7.788241
Log likelihood	-76.39752	Hannan-Quinn criter.	7.560779
F-statistic	3.604818	Durbin-Watson stat	2.021277
Prob(F-statistic)	0.022504		

Null Hypothesis: D(LFDI) has a unit root

Exogenous: Constant

Lag Length: 0 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-4.990212	0.0007
Test critical values:	1% level	-3.788030	
	5% level	-3.012363	
	10% level	-2.646119	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(LFDI,2)

Method: Least Squares

Date: 11/12/18 Time: 10:12

Sample (adjusted): 1995 2017

Included observations: 23 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(LFDI(-1))	-1.123750	0.225191	-4.990212	0.0001
C	0.176100	0.095192	1.849939	0.0799

R-squared	0.567220	Mean dependent var	0.004091
Adjusted R-squared	0.544442	S.D. dependent var	0.602450
S.E. of regression	0.406624	Akaike info criterion	1.128536
Sum squared resid	3.141514	Schwarz criterion	1.228014
Log likelihood	-9.849625	Hannan-Quinn criter.	1.150125
F-statistic	24.90221	Durbin-Watson stat	1.342823
Prob(F-statistic)	0.000081		

Null Hypothesis: LGDP has a unit root

Exogenous: Constant

Lag Length: 0 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-3.696371	0.0107
Test critical values:	1% level	-3.724070	
	5% level	-2.986225	
	10% level	-2.632604	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(LGDP)

Method: Least Squares

Date: 11/12/18 Time: 10:12

Sample (adjusted): 1991 2017

Included observations: 27 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LGDP(-1)	-0.041865	0.011326	-3.696371	0.0012
C	0.594332	0.105600	5.628159	0.0000

R-squared	0.372667	Mean dependent var	0.209545
Adjusted R-squared	0.345392	S.D. dependent var	0.109643
S.E. of regression	0.088709	Akaike info criterion	-1.930282
Sum squared resid	0.180996	Schwarz criterion	-1.832772
Log likelihood	26.12852	Hannan-Quinn criter.	-1.903237
F-statistic	13.66316	Durbin-Watson stat	1.625459
Prob(F-statistic)	0.001192		

Null Hypothesis: D(LTAXREV) has a unit root

Exogenous: Constant, Linear Trend

Lag Length: 1 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-5.075946	0.0025
Test critical values:	1% level	-4.416345	
	5% level	-3.622033	
	10% level	-3.248592	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(LTAXREV,2)

Method: Least Squares

Date: 11/12/18 Time: 10:13

Sample (adjusted): 1993 2017

Included observations: 25 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(LTAXREV(-1))	-1.520205	0.299492	-5.075946	0.0001
D(LTAXREV(-1),2)	0.500762	0.208996	2.396032	0.0270
C	0.471740	0.151904	3.105518	0.0058
@TREND(1990)	-0.012197	0.008162	-1.494452	0.1515

R-squared	0.606485	Mean dependent var	-0.022319
Adjusted R-squared	0.544351	S.D. dependent var	0.376126
S.E. of regression	0.253892	Akaike info criterion	0.252954
Sum squared resid	1.224760	Schwarz criterion	0.450431
Log likelihood	1.091029	Hannan-Quinn criter.	0.302619
F-statistic	9.760918	Durbin-Watson stat	1.889054
Prob(F-statistic)	0.000411		

Null Hypothesis: D(TGDP) has a unit root

Exogenous: Constant, Linear Trend

Lag Length: 1 (Automatic - based on SIC, maxlag=5)

		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-4.980529	0.0030
Test critical values:	1% level	-4.416345	
	5% level	-3.622033	
	10% level	-3.248592	

*MacKinnon (1996) one-sided p-values.

Augmented Dickey-Fuller Test Equation

Dependent Variable: D(TGDP,2)

Method: Least Squares

Date: 11/12/18 Time: 10:14

Sample (adjusted): 1993 2017

Included observations: 25 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(TGDP(-1))	-1.506491	0.302476	-4.980529	0.0001
D(TGDP(-1),2)	0.451625	0.206387	2.188238	0.0413
C	-0.113098	0.741674	-0.152490	0.8804
@TREND(1990)	0.001604	0.047851	0.033523	0.9736

R-squared	0.607315	Mean dependent var	-0.024917
Adjusted R-squared	0.545312	S.D. dependent var	2.246338
S.E. of regression	1.514718	Akaike info criterion	3.825106
Sum squared resid	43.59301	Schwarz criterion	4.022583
Log likelihood	-39.98872	Hannan-Quinn criter.	3.874771
F-statistic	9.794958	Durbin-Watson stat	1.883556
Prob(F-statistic)	0.000403		

REGRESSION RESULT FOR HYPOTHESIS I

Dependent Variable: LOG(GDP)

Method: Least Squares

Date: 11/12/18 Time: 09:16

Sample: 1990 - 2017

Included observations: 28

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOG(FDI)	0.897529	0.258515	3.471870	0.0041
INFL	-0.120151	0.061234	-1.962170	0.0715
C	-1.916114	7.003048	-0.273611	0.7887

R-squared	0.659115	Mean dependent var	19.91817
Adjusted R-squared	0.606671	S.D. dependent var	1.328483
S.E. of regression	0.833170	Akaike info criterion	2.640203
Sum squared resid	9.024239	Schwarz criterion	2.785063
Log likelihood	-18.12162	Hannan-Quinn criter.	2.647621
F-statistic	12.56803	Durbin-Watson stat	1.696987
Prob(F-statistic)	0.000916		

Source: E-Views 10

REGRESSION RESULT FOR OTHER HYPOTHESES

Dependent Variable: LFDI

Method: ARDL

Date: 11/21/18 Time: 14:36

Sample (adjusted): 1994 2017

Included observations: 24 after adjustments

Maximum dependent lags: 2 (Automatic selection)

Model selection method: Akaike info criterion (AIC)

Dynamic regressors (2 lags, automatic): EPTD ETR GDPRT INFL

Fixed regressors: C

Number of models evalulated: 162

Selected Model: ARDL(1, 2, 2, 2, 1)

Note: final equation sample is larger than selection sample

Variable	Coefficient	Std. Error	t-Statistic	Prob.*
LFDI(-1)	-0.173254	0.455413	-0.380433	0.7124
EPTD	0.195006	0.076423	2.551675	0.0311
EPTD(-1)	0.018808	0.094275	0.199500	0.8463
EPTD(-2)	0.128731	0.109986	1.170429	0.2719
ETR	0.341532	0.502712	0.679379	0.5140
ETR(-1)	-0.222354	0.655138	-0.339401	0.0543
ETR(-2)	1.320702	0.689010	1.916811	0.0875
GDPRT	-0.011826	0.012162	-0.972404	0.3563
GDPRT(-1)	0.007614	0.022962	0.331609	0.7478
GDPRT(-2)	0.024386	0.021453	1.136722	0.2850
INFL	-0.016463	0.011805	-1.394567	0.1966
INFL(-1)	0.013031	0.008311	1.567853	0.1514
C	-42.60859	15.99704	-2.663530	0.0259

R-squared	0.970172	Mean dependent var	12.64835
Adjusted R-squared	0.930401	S.D. dependent var	1.166600
S.E. of regression	0.307767	Akaike info criterion	0.769054
Sum squared resid	0.852486	Schwarz criterion	1.413761
Log likelihood	4.540401	Hannan-Quinn criter.	0.920928
F-statistic	24.39415	Durbin-Watson stat	2.112706
Prob(F-statistic)	0.000022		

*Note: p-values and any subsequent tests do not account for model selection

Source: E-Views 10