

Taxation and Revenue Generation: Challenges and Prospects in Nigeria

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Article History	Abstract
Original Research Article	<p><i>Taxation is an essential mechanism for income creation and economic advancement in Nigeria. It constitutes a primary source of governmental revenue utilised for funding public goods and services, including infrastructure, education, healthcare, and security. Notwithstanding its significance, the Nigerian tax system persists in encountering substantial obstacles that hinder its efficiency and effectiveness. This study analysed taxation and revenue generation in Nigeria, emphasising its significance, difficulties, and potential for enhancement. The research indicated that taxation plays a crucial role in government income but is hindered by various issues, such as tax evasion and avoidance, corruption, ineffective tax administration, double taxing, insufficient tax awareness, and the prevalence of the informal sector. These limitations diminish compliance rates and constrain the government's overall revenue-generating potential. The research indicated that ineffective tax systems and a deficiency of public confidence in governmental spending adversely impact voluntary tax compliance among individuals and enterprises. The report also found other opportunities for enhancing taxation and revenue generation in Nigeria. This encompasses the digitalisation of tax systems, broadening of the revenue base, fortification of tax institutions, execution of successful tax reforms, and enhancement of openness in public financial management. When effectively executed, these approaches can improve tax compliance, diminish revenue losses, and augment government revenue for sustainable national growth. The report suggests that Nigeria encounters substantial taxing issues, however there exist considerable prospects for reform and enhancement. Enhancing the tax system will not only increase income generation but also diminish reliance on oil revenue and foster long-term economic stability and prosperity.</i></p> <p>Keywords: Taxation, Revenue Generation, Tax Evasion, Fiscal Policy, Nigeria, Economic Development.</p>
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Introduction

According to Chugunov et al.'s research from 2020, taxation is a significant fiscal instrument that governments employ in order to produce revenue for the provision of public goods and services, as well as to regulate economic activities and activities inside a country. When it comes to paying government expenditures in Nigeria, such as the development of infrastructure, education, healthcare, security, and other critical social services, taxes play a pivotal role. The tax system in Nigeria has continued to encounter a number of structural and administrative issues,

which restrict its efficiency in attaining optimal revenue collection and sustainable national development. This is despite the fact that the tax system is extremely important.

Taxation in Nigeria may be traced back to both pre-colonial and colonial periods, when traditional rulers and later colonial administrations imposed various sorts of tolls on individuals and groups. This is the origin of taxation in Nigeria. This system eventually developed into a framework for the administration of taxes that was more structured and formalised throughout the course of time.

This was accomplished through the development of tax authorities at the federal, state, and municipal government levels. The Federal Inland Revenue Service (FIRS) and State Internal Revenue Services are two examples of organisations that were established with the purpose of improving tax collection and enforcement, respectively. The ratio of taxes to gross domestic product (GDP) in Nigeria is still very low when compared to that of other developing economies, despite the fact that these institutional frameworks exist. The shortcomings of the administration of taxes, the widespread practice of tax evasion, the existence of a sizable informal sector, and the limited public faith in the institutions of the government are largely responsible for this scenario.

There are a number of chronic challenges that contribute to the problem of taxation and revenue production in Nigeria. These concerns include corruption, ineffective enforcement mechanisms, inadequate tax awareness, and poor compliance among taxpayers (CHUKWUMA & CHARLES-CHUKWU, 2025). As a result of a lack of confidence in the processes by which public funds are administered, a significant number of people and corporations either purposefully avoid paying taxes or underreport their income. As a consequence of this, the government's revenue does not meet the expectations that were set for it, which results in higher borrowing and a growing national debt, which in turn places more pressure on the economy.

The primary objective of this study is to investigate taxation and revenue generation in Nigeria, with a particular emphasis on gaining an understanding of the role that taxation plays in the process of national development, determining the most significant challenges that exist in relation to tax collection, and investigating the potential opportunities for enhancing the effectiveness of the tax system. Research questions that seek to assess the contribution of taxation to government income, the issues that limit effective tax administration, and the opportunities that are available for upgrading the system are the guiding principles for this study.

The significance of this study lies in the fact that it offers insightful recommendations to policymakers, tax officials, researchers, and students regarding the ways in which Nigeria might enhance its tax system in order to achieve greater revenue performance. In addition, it emphasises the significance of taxation as a viable alternative to reliance on oil and as a primary factor in the diversification of the economy and the development of the nation. The focus of the study is restricted to taxation and revenue generation in Nigeria. It will address tax systems that are administered by the federal, state, and local governments, as well as the

accompanying issues and prospects that are present within the setting of Nigeria.

In the context of this discussion, the term "taxation" refers to the imposition of obligatory financial charges by the government on persons and organisations for the purpose of achieving public objectives, whereas the term "revenue generation" refers to the process by which the government collects revenues in order to support public expenditures. The illegal avoidance of tax duties is referred to as tax evasion, and the readiness of taxpayers to adhere to tax rules and regulations is referred to as tax compliance.

Conceptual Framework

Taxation is acknowledged as a mandatory charge levied by the government on individuals, corporations, and other entities under its control to generate cash for public expenditure financing. It is a crucial weapon of fiscal policy employed by governments to affect economic activities, redistribute income, and guarantee the provision of public goods and services (Chugunov & Pasichnyi, 2024). In Nigeria, taxation is a crucial element of government revenue, however its complete potential has not been fully attained due to several structural and administrative inefficiencies. The efficacy of taxes is mostly contingent upon the robustness of the tax system, the degree of compliance, and the efficiency of tax authorities in collection and enforcement.

Revenue generation pertains to the many procedures by which the government acquires income to finance its operations and developmental initiatives. In Nigeria, government revenue is sourced from both oil and non-oil sectors, with taxation being a significant portion of non-oil revenue. Additional sources comprise customs taxes, royalties, penalties, levies, and internally generated income (IGR) at the state and local government tiers. Nonetheless, taxes persists as the most durable and dependable revenue source, particularly with volatile oil prices and rising government expenditure requirements (Audi, 2024). An effective income generation strategy guarantees economic stability, diminishes reliance on external borrowing, and facilitates long-term development planning.

In Nigeria, taxes are primarily categorised into direct and indirect taxes. Direct taxes are levied directly on individuals and entities, determined by their income or wealth. Examples encompass personal income tax, corporate income tax, capital gains tax, and petroleum profit tax. Conversely, indirect taxes are imposed on goods and services rather than on income, and they are frequently incorporated into the product price (Karabulut, 2020). Examples encompass value-added tax (VAT), customs duties, and excise taxes. Both tax categories are crucial for revenue generation; however, indirect taxes are typically

more straightforward to collect owing to their consumption-based characteristics.

The Nigerian tax system is organised into three levels of government: federal, state, and local. At the federal level, agencies like the Federal Inland Revenue Service (FIRS) are tasked with the collection of significant taxes, including corporate income tax, petroleum profit tax, and value-added tax. State governments are tasked with the collection of personal income tax from people, stamp fees, and other levies via their State Internal Revenue Services (Youssef, 2019). Municipal authorities also derive income from market taxes, tenement rates, and various community-based levies. Notwithstanding this framework, coordination difficulties, overlapping tax authorities, and inadequate enforcement tools frequently obstruct efficient tax administration in the nation.

Taxation is essential for national growth as it supplies the financial resources necessary for infrastructure, education, healthcare, security, and social welfare initiatives. It functions as an instrument for economic regulation by shaping consumption patterns, promoting investment, and mitigating income inequality through redistribution. In growing economies such as Nigeria, efficient taxation is crucial for diminishing reliance on oil revenue and fostering economic diversification. An effective tax system improves governmental accountability, as citizens are more inclined to seek openness when they actively contribute to public resources (Gribnau & Jallai, 2018).

Framework

This study is based on Adam Smith's Ability-to-Pay Theory of Taxation (1776), a widely recognised premise in public finance. The theory asserts that individuals and organisations need to be taxed based on their capacity to pay, indicating that those with higher income or larger wealth should contribute more to government revenue than those with lesser income. The fundamental concept of this theory is the justice and equity in the allocation of tax responsibilities within a society. It posits that taxation ought not to impose an identical burden on all taxpayers, but should instead correspond to variations in economic potential.

The Ability-to-Pay Theory is intrinsically associated with vertical equity, which asserts that taxpayers in varying economic circumstances should be treated differently to attain fairness (Bizioli & Reimer, 2020). This idea advocates for progressive taxation, wherein tax rates rise with increasing income. This guarantees that the affluent contribute a greater percentage of their income to public revenue than the impoverished, thus diminishing economic inequality and fostering social fairness. The approach acknowledges that taxation must not drive low-income

individuals into poverty or impose undue burden on vulnerable societal groups.

The Ability-to-Pay Theory is particularly pertinent in Nigeria, given the pronounced income inequality among various social strata. Nigeria possesses a substantial population of low-income earners alongside a comparatively tiny affluent elite, rendering equitable taxation crucial for social and economic stability (Herbert et al., 2018). The practical implementation of this principle in Nigeria is sometimes hindered by ineffective tax administration, inadequate income documentation, and a substantial informal sector where several persons lack verifiable income records. Consequently, tax authorities find it challenging to appropriately evaluate the genuine capacity of people and corporations to fulfil their tax obligations.

Notwithstanding these issues, the Ability-to-Pay Theory continues to serve as a valuable framework for assessing Nigeria's tax system, as it underscores the necessity for fairness, equity, and social responsibility in tax administration (Dasaolu, 2025). It also establishes a foundation for promoting tax reforms that enhance income tracking, bolster enforcement measures, and broaden the tax base to encompass additional actors in the informal sector. If properly executed, the tenets of this theory can assist Nigeria in establishing a more equitable and sustainable revenue generation framework.

Taxation and Revenue Generation in Nigeria

Taxation is a fundamental source of revenue in Nigeria, supplying the government with the necessary revenues to support both recurring and capital expenditures (Craig et al., 2020). In a developing economy such as Nigeria, where developmental requirements are substantial and public resources frequently constrained, taxation functions as a more steady and reliable source of revenue in contrast to fluctuating oil earnings. The Nigerian government generates revenue from both oil and non-oil sources, with taxation serving as the foundation of non-oil revenue and increasingly prioritised for economic diversification.

The primary sources of tax revenue in Nigeria are classified among the three levels of government: federal, state, and local. Taxation at the federal level is predominantly managed by the Federal Inland Revenue Service (FIRS), which oversees the collection of essential taxes like Company Income Tax, Petroleum Profit Tax, Value Added Tax (VAT), and Withholding Tax. These taxes represent a substantial component of the federal government's revenue and are essential for financing national initiatives, including infrastructure development, defence, and debt payment (Cahyadi, 2024). The efficacy of FIRS in tax collection has enhanced over the years due to digital tax systems and regulations designed to mitigate tax evasion.

At the state level, Internal Revenue Services are tasked with the collection of taxes, including Personal Income Tax from citizens, Stamp Duties, and different levies and fees. State governments also derive internally generated revenue (IGR) from sources including motor vehicle registration, land use fees, commercial licenses, and market levies. The effectiveness of revenue collection at the state level in Nigeria exhibits considerable variation, with certain states demonstrating superior performance attributable to robust administrative frameworks and enhanced compliance mechanisms, whereas others contend with inadequate enforcement and minimal tax awareness among the populace.

Local governments additionally facilitate income production via community-based taxes and levies, including tenement rates, market fees, and local company charges. Despite being very little in relation to federal and state resources, these funds are crucial for grassroots development and the delivery of fundamental services, including sanitation, primary healthcare, and local infrastructure. Local government revenue creation is frequently obstructed by political involvement, corruption, and constrained administrative capacity (Oduntan & Abubakar, 2024).

Taxation plays a crucial role in Nigeria's national budget by supplying resources for both recurring expenditures and capital projects. It mitigates excessive reliance on crude oil revenue and fosters economic stability. Nevertheless, the complete potential of taxation in Nigeria remains unfulfilled due to inefficiencies in collection, inadequate compliance, and pervasive tax evasion. Enhancing tax administration at all governmental tiers is crucial for augmenting revenue production and maintaining sustained national growth.

Challenges of Taxation and Revenue Generation in Nigeria

Notwithstanding the significance of taxation as a dependable source of governmental revenue, the Nigerian tax system faces myriad issues that considerably undermine its efficacy. These issues encompass administrative, economic, social, and institutional aspects, thereby impacting the government's overall ability to earn sufficient revenue for developmental objectives (El-Taliawi & Van Der Wal, 2019). Nigeria persists in grappling with inadequate tax compliance, ineffective revenue collection, and excessive reliance on oil revenue.

A major concern is tax evasion and avoidance. Numerous individuals and corporate entities intentionally underreport their income or entirely evade tax obligations due to inadequate enforcement measures and systemic loopholes. The absence of precise financial records, particularly in the

informal sector, which represents a significant segment of Nigeria's economy, further incentivises tax cheating (Olaoye & Adekoya, 2020). This circumstance complicates tax authorities' ability to accurately evaluate and collect taxes from all qualifying taxpayers.

Corruption and mismanagement of public funds provide significant obstacles to income collection in Nigeria. Taxpayers may hesitate to fulfil tax responsibilities due to prevalent beliefs that government finances are mismanaged or appropriated for personal benefit by public officials. The absence of trust in government diminishes voluntary compliance and undermines the broader tax culture in the nation (Gaber & Gruevski, 2018). When citizens perceive a lack of concrete benefits from taxation, their propensity to pay taxes diminishes markedly.

A significant difficulty is the deficient tax administration system. Numerous tax authorities experience insufficient personnel, substandard technical infrastructure, and restricted capability for efficient monitoring and enforcement (Arewa & Davenport, 2022). Despite attempts to establish digital tax systems, their implementation remains varied across various locations. This deficient administrative framework engenders potential for inefficiency, fraud, and revenue losses inside the system.

The prevalence of the informal sector in Nigeria's economy complicates taxation. A significant amount of economic activities transpires outside formal registration, resulting in several enterprises and individuals being excluded from the tax net. This diminishes the overall tax base and constrains government income potential. Moreover, inadequate tax awareness and limited educational attainment among taxpayers lead to non-compliance, as numerous persons lack comprehensive knowledge of their tax responsibilities and the significance of taxation for national progress.

Multiple taxation presents a significant challenge for businesses and individuals in Nigeria. Taxpayers may face diverse taxes and levies imposed by multiple government entities at the federal, state, and municipal levels. This engenders complexity, escalates operational costs, and disincentivises voluntary compliance. Moreover, economic instability, inflation, and unemployment diminish the capacity of individuals and enterprises to fulfil their tax responsibilities, consequently impacting total revenue production.

Prospects of Taxation and Revenue Generation in Nigeria

Notwithstanding the myriad issues confronting the Nigerian tax system, there are certain auspicious potential that might substantially enhance taxation and revenue production if effectively utilised. These prospects are intricately associated with ongoing reforms, technical

innovations, institutional fortification, and heightened understanding of the significance of taxation in national growth. With appropriate policies and implementation tactics, taxation can transform into a more efficient and dependable source of government revenue in Nigeria.

The digitalisation of tax administration is a crucial prospect. The implementation of computerised tax systems, online filing platforms, and automated payment processes by organisations like the Federal Inland Revenue Service (FIRS) has commenced diminishing human intervention and enhancing transparency in tax collection. Digital tax systems also mitigate corruption, diminish tax evasion, and facilitate compliance for taxpayers (Younus et al., 2025). With ongoing technological advancements, Nigeria has significant potential to totally modernise its tax system into a data-driven structure that improves efficiency and accountability.

A significant opportunity lies in the execution of tax reforms and policy enhancements. The Nigerian government has implemented many reforms to streamline tax legislation, minimise multiple taxation, and enhance compliance. Consistent implementation and monitoring of these measures can establish a more favourable tax climate for businesses, promoting investment and enhancing government income (Abbo, 2025). Harmonisation of policies among federal, state, and municipal governments can mitigate tax duplication and enhance cooperation within the tax system.

The broadening of the tax base offers a substantial possibility for enhancing revenue production in Nigeria. A significant segment of the Nigerian economy functions within the informal sector, which is predominantly untaxed. By formulating measures to incorporate informal enterprises into the regular tax framework, the government can substantially augment its income base. This can be accomplished via business registration incentives, streamlined tax processes, and enhanced public awareness initiatives that inform citizens about the advantages of taxation.

Enhancing tax institutions is another significant opportunity. Agencies like the FIRS and State Internal Revenue Services necessitate ongoing capacity development, more money, and upgraded technology infrastructure to operate efficiently. Robust tax institutions enhance compliance enforcement, minimise leakages, and guarantee accountability in revenue collection (Siddiqui & Tariq, 2024). Enhanced training of tax workers and the implementation of contemporary auditing tools can further augment efficiency in tax administration.

Moreover, increased public trust and accountability in governmental expenditure can substantially boost tax

compliance. When citizens are assured that their taxes are allocated for the public benefit, such as infrastructure, healthcare, education, and security, they are more inclined to cheerfully meet their tax commitments. Consequently, transparency in governmental spending and efficient communication of tax advantages are crucial for fostering a favourable tax culture in Nigeria.

Finally, the diversification of revenue streams outside oil and conventional taxes offers a significant opportunity (Adegbe et al., 2023). Integrating developing industries such as agriculture, technology, manufacturing, and services into the tax system can enhance revenue diversification and diminish reliance on crude oil. This diversification would enhance the resilience and stability of the Nigerian economy in the long term.

Conclusion

Taxation is a crucial mechanism for income generation and economic governance in Nigeria. It serves as the financial foundation for governmental functions, encompassing infrastructure development, social services, and economic planning. Nonetheless, despite its significance, the Nigerian tax system has not attained its full potential due to ongoing structural and administrative obstacles. Tax evasion, inadequate enforcement measures, corruption, and a substantial informal sector persistently hinder the effectiveness of tax collection and diminish the nation's overall revenue base.

The research indicates that although Nigeria has endeavoured to enhance its tax system via institutional reforms and the creation of institutions such as the Federal Inland Revenue Service (FIRS), substantial deficiencies persist in implementation and compliance. Inadequate tax administration, difficulties of double taxation, and diminished public trust in government persistently hinder voluntary compliance. These problems underscore the necessity for a more transparent, efficient, and technology-driven tax system that enhances accountability and expands the revenue base.

The outlook for enhancing taxation and revenue generation in Nigeria is optimistic. Nigeria has the ability to substantially augment its revenue generating capacity through continuous digital transformation, tax reforms, broadening of the tax base, and fortification of tax institutions. If successfully executed, these initiatives will enhance government revenue, promote sustainable national growth, and diminish reliance on oil income.

Recommendations

1. The Nigerian government should strengthen tax administration by fully digitizing the tax collection system across federal, state, and local levels. This

will reduce human interference, minimize corruption, improve transparency, and make tax payment more convenient for individuals and businesses.

2. There is a need to expand the tax base by formally integrating more participants in the informal sector into the tax system. This can be achieved by simplifying registration processes, offering incentives for compliance, and conducting sustained public awareness campaigns on the benefits of taxation.
3. Tax laws and policies should be harmonized across different tiers of government to reduce the problem of multiple taxation. Clear coordination between federal, state, and local tax authorities will help create a more organized and business-friendly tax environment.
4. The government should improve accountability and transparency in the use of tax revenue. When citizens can visibly see the impact of their taxes through improved infrastructure, healthcare, education, and security, voluntary tax compliance will increase significantly.
5. Continuous training and capacity building should be provided for tax officials to enhance efficiency in tax collection and enforcement. In addition, stronger anti-corruption measures should be implemented within tax agencies to ensure proper management of public revenue.

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