

## CHAPTER ONE

### INTRODUCTION

#### 1.0 BACKGROUND OF STUDY

For the development and growth of any economy, the provision of basic infrastructure is quite necessary. Among these are the provision of schools, hospitals, construction of roads, bridges, railway lines, airports and seaports. Generally, government is saddled with the responsibility of providing some basic infrastructures for her citizens. In lieu of this, the government of any society seeks sources of fund to maintain the development, and meet the needs of its society. Meeting the needs of the economy call for huge funds which an individual or society can't contribute alone. There are two ways of financing government expenditure in Nigeria; these are, through oil revenue and through non-oil revenue. The Nigerian government sources a large proportion of its total revenue from oil since Nigeria has been seen as a country rich with this natural resources. The petroleum industry generated about 82 per cent income for Federal Government while 18 percent came from non-oil revenue. The Petroleum Industry constitutes a major source of income and occupies a strategic position in the economic development of Nigeria. For the past decades, the industry has been playing vital and dominant role to the economic growth of Nigeria, both in foreign exchange earnings and domestic income generation. One of the sources of petroleum income is the Petroleum Profit Tax, this is just among others, as royalties, rents, oil pipeline and license fees, signature bonuses penalty from gas flared, NNPC earnings from direct sales, proceeds from local sales of crude oil to NNPC, proceeds from export sales of crude oil and gas etc. are sources of petroleum income. But for the purpose of this research, the researcher will be focusing on an aspect of the sources of petroleum income, which is, petroleum profit tax (PPT). Petroleum refers to crude oil and natural gas or simply put, oil and gas. Petroleum, or oil and gas, production and export play a dominant role in the economy of Nigeria and account for about 70 per cent of the nation's GDP and over 90 per cent of her foreign earnings. Nigeria has been seen to be the largest oil producing country in Africa and the eleventh in the world. Petroleum industry is the leading sector in the Nigerian economy. Oil being the mainstay of Nigerian economy plays a vital role in shaping the economic and political destiny of the country. The contributions of the petroleum industry to public expenditure has been phenomenal. Taxation is the system of collecting money by taxes i.e. the system by which taxes are imposed or the process or system of raising income through the levying of various types of taxes. Taxes are levies imposed by government against the income, profit or wealth of an individual,

partnership and corporate organization. From the definitions given it can be said that the main purpose of tax is to provide government with money to provide public services to citizens and it is necessary that all citizens, whether individuals or artificial bodies, pay taxes. The Petroleum Profit Tax Act (PPTA) is the tax law responsible for the governing of the taxation of companies engaged in petroleum operations and, the Act defines petroleum operations as “the winning or obtaining and transportation of petroleum or chargeable oil in Nigeria by or on behalf of a company for its own account by any drilling, mining, extracting or other like operations or process, not including refining at a refinery, in the course of a business carried by the company engaged in such operations, and all operations incidental thereto and sale of or any disposal of chargeable oil by or on behalf of the company”

. The definition is applicable to the upstream sector of the petroleum industry; hence, only companies in the upstream sector are charged with petroleum profit tax (PPT). The importance of taxation on petroleum profits cannot be overemphasized as tax revenue derived from tax in petroleum profits contributes, largely, to the total tax revenue available to the Nigerian government. Petroleum profit tax generates about 42% income for the federal government.

## **1.1 STATEMENT OF RESEARCH PROBLEM**

Reiterating the fact that taxation of petroleum profit is a source of revenue to the Nigerian economy in funding her government expenditure, but in Nigeria today the infrastructures, education, and health care services and other amenities are not showing the effective use of tax contributed by oil companies in the upstream sector. In Nigeria the citizens and companies avoid and evade tax because they do not know how revenue generated through tax is being spent by the government. Nigeria is one of the few countries in the world where it is fashionable to evade tax. The various structures which are required to work together to make tax evasion difficult are not properly coordinated. Tax evasion is one of the major social problems inhibiting development in developing countries and eroding the existing welfare state in developed economies in the world. It has been observed that high profile companies in Nigeria do evade tax. And oil companies are included in this class of high profile companies. This observation says a lot about tax administration system in Nigeria both in its design and in the disposition of some oil companies towards taxation. This presupposes that there are legal frameworks put in place to punish tax evaders it perhaps raises a question on the efficiency and effectiveness of tax laws and tax administration in Nigeria. The Nigerian government in an effort towards solving this problem has even gone to the extent of engaging the services of tax consultants. Despite the effort of government, tax evasion still persists, revenue derived from taxation of

petroleum profits amounts to a great portion of total tax collections of the Nigeria government. The evasion of tax by oil companies could have a drastic effect on the development of the economy of Nigeria.

Oil companies in Nigeria have, over the years, devised means of getting away with every breach of the law. Oil companies justify their actions due to the corrupt nature of the government; they perceive the tax officials and government as a whole embezzle the revenue derived from petroleum profit tax. Tax evasion in Nigeria is becoming uncontrollable; yet, the Nigerian government has failed to pay attention to the analysis of the major causes of tax evasion in its economy, especially the evasion of tax on petroleum profit since this is said to have a significant addition to the total collections of total tax collections. The petroleum profit tax structure, in Nigeria, has been characterized with tax evasion, tax avoidance, corruption and poor tax administration filled with loopholes. Hence, this research work is set out to provide answers and possible solutions to the problems already identified.

## **1.2 AIM AND OBJECTIVES OF THE STUDY**

The following are the aim and objectives, which this study sets to achieve:

1. To identify if a significant relationship exists between petroleum profit tax and the capital expenditure of the Nigerian economy.
2. To identify if there are major differences in the perception of respondent groups on the major causes for avoiding petroleum profit tax.
3. To determine if the tax authorities are effective in the collection of petroleum profit tax (PPT).

## **1.3 RESEARCH QUESTIONS**

Based on the aforementioned problems, the researcher is constrained to ask the following questions:

1. How significant is the relationship between petroleum profit tax (PPT) and the capital expenditure of the Nigerian economy?
2. To what extent are there significant differences in the perceptions of respondent groups on the major causes for avoiding petroleum profit tax?
3. To what extent are the tax authorities of Nigeria effective in the collection of petroleum profit tax (PPT).

## **1.4 RESEARCH HYPOTHESES**

For the purpose of this study, the hypothesis testing shall be stated thus:

Hypothesis 1

HO: There is no significant relationship between petroleum profit tax and the capital expenditure of the Nigerian economy.

H1: There is a significant relationship between petroleum profit tax and the capital expenditure of the Nigerian economy.

Hypothesis 2

H0: There are no significant differences in the perception of respondent groups on the major causes for avoiding petroleum profit tax.

H1: There are significant differences in the perception of respondent groups on the major causes for avoiding petroleum profit tax.

Hypothesis 3

H0: The tax authorities are not effective in the collection of petroleum profit tax

H1: The tax authorities are effective in the collection of petroleum profit tax

## **1.5 SCOPE OF STUDY SAMPLE SIZE**

This study shall cover a selected government agency, which is, Federal Inland Revenue Service (FIRS) in Lagos State, Central Bank of Nigeria (CBN), KPMG accounting firm, Chevron Nigeria Limited.

## **1.6 GEOGRAPHICAL COVERAGE**

The south western part of Nigeria is selected for this research. Primary data necessary for the research work will be gathered from Lagos state. While secondary data necessary for the research work will be gotten from federal inland revenue service (FIRS) and central bank of Nigeria (CBN)

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