THE CHARTERED INSTITUTE OF TAXATION OF NIGERIA

VALUE-ADDED TAX IN NIGERIA

POLICY, LEGAL, ADMINISTRATIVE ISSUES AND OPTIONS FOR REFORM

Lead Editors:
Temitope Ajodun SAMAGBEYI, FCTI
Olatunde Julius OTUSANYA, FCTI

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To be one of the foremost professional associations in Africa and beyond

MISSION
To build an Institute which will be a citadel for the advancement of taxation in all its ramifications

MOTTO
Integrity and Service

CORE VALUES
Service
Teamwork
Excellence
Professionalism

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FOREWORD

The publication of **"Value Added Tax in Nigeria – Policy, Legal, Administrative Issues and Options for Reform"** are crucial to the current and challenging economic condition of Nigeria due to the COVID – 19 pandemic ravaging the world economy inclusive that of Nigeria, and this has led to a decline in economic activities.

Before 2019, the VAT Act needed a lot of amendments due to its significant contribution to the economic growth and development of our nation. Despite the need to increase the revenue generation of government, the VAT rate in Nigeria ranked among the lowest in the World at 5%. The present administration through the 2019 Finance Act increased the VAT rate to 7.5% while certain sections of the Act which had hitherto raised a lot of concerns from stakeholders were amended. The recent developments in the administration of VAT in Nigeria has led to the compilation of this book by seasoned members of our great Institute. The book will serve as a reference material for stakeholders including policymakers, legislators, tax authorities at various levels of government, tax practitioners, taxpayers, the academia and students of taxation at undergraduate, postgraduate and professional levels. The material explains in detail the policy, legal and administrative issues thrown up by the amendments to the Act and recommendations for reforms.

The publication of this material is timely and useful for the general administration and implementation of VAT in Nigeria. The book covers all aspects of VAT including the history and concept of VAT, the historical development of VAT in Nigeria, a review of amendments to the VAT Act from 1993 up to 2020, VAT administration and technology in Nigeria, resolving the conundrum in the application of VAT to real estate transactions, examining the effect of recent tax reforms, the applicability of VAT to professional services in Nigeria, tax appeal – assessment, objection, appeal, issues and options for reform etc.

I believe that this book will provide insight to tax professionals, administrators and the public who wish to fully understand the legal and administrative framework of VAT in Nigeria, therefore, I recommend this book for policymakers, legislators at various levels of government, tax authorities as well as taxpayers.

Mr. Adesina Adedayo, FCTI
15th President/Chairman of Council
Chartered Institute of Taxation of Nigeria
Lagos, July 2021

PREFACE

Indirect taxes are taxes collected from a person by intermediaries (such as retail shops, government agencies (e.g. FIRS), etc) who pays the taxes as included in the purchase price of a product or service. The intermediary or agent is expected to file tax returns and forward the tax proceeds collected to the government with the return. Indirect taxes cover such areas as excise taxes, sales tax, service tax, customs duty, Value-Added Tax (VAT), and Securities Transaction Taxes (STT).

This book is an effort to bring clarity to the reader, most especially practitioners, administrators and students of indirect tax examining bodies in Nigeria, with the clear purpose of disserting the conceptual and application principles that underpin the adoption, implementation and administration of Value-Added Tax in Nigeria.

The book- Value Added Tax in Nigeria – Policy, Legal, Administrative Issues and Options for Reform is part of the Institute's efforts to bridge the knowledge gaps in dealing with administrative issues that surrounds the implementation of VAT tax in Nigeria. The book will serve as a guiding manual to help both the tax practitioners, administrators and students of Values-Added Tax to understand the rudimental of the tax across key segments of the VAT tax legislation in Nigeria.

We hope that this publication will become a handy companion to provide a working guide on dealing with Value-Added Tax issues that confront tax practitioners, tax administrators, corporate organizations and professional examination candidates. Students of tertiary institutions offering courses in taxation will find the simple and everyday language of the textbook an easy tool to passing their courses in this area.

Temitope Ajodun Samagbeyi, FCTI
Dean, Indirect Tax Faculty
The Chartered Institute of Taxation of Nigeria

16th July 2021

ABOUT THE INSTITUTE

The Chartered Institute of Taxation of Nigeria started on February 4, 1982, as an Association of Tax Administrators and Practitioners (ATP). Thereafter, it transformed into Nigeria Institute of Taxation (NIT), which was formally launched on February 21, 1982, and statutorily recognized on May 6, 1987, as a company Limited by Guarantee.

The Institute was chartered by the Federal Government of Nigeria by enabling Act No. 76 of 1992 (now Chartered Institute of Taxation of Nigeria Act, CAP C10, Vol. 2, Laws of the Federation of Nigeria, 2004) and was charged with the responsibility, among others, of regulating and controlling the practice of the tax profession in its entire ramifications and determining what standards of knowledge and skills are to be attained by persons seeking to become professional Tax Practitioners or Administrators.

THE CHARTER OF THE INSTITUTE

The aims and objectives of the Institute as laid down in its charter (Act No. 76 of 1992), among others, are:-

- To determine what standards of knowledge and skills are to be attained by persons seeking to become registered members of the taxation profession;
- To raise, maintain and regulate the standard of taxation practice amongst its members;
- To promote professional ethics and efficiency in tax administration and practice; and
- To encourage, promote and coordinate research for the advancement of taxation practice and administration in Nigeria.

Under the Act, the Institute is the only professional body empowered to regulate tax practice and administration in Nigeria and only its members can practice Taxation. The Act sets out the rules as regards membership composition and officers of Council, etc.

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Prof. Olateju Somorin, FCTI, popularly known as "TEJUTAX" started her academic career in 1955 at the Ijero Baptist School, Apapa Road, Lagos and given her excellent performance at the Common Entrance examinations, had to skip Primary Six class to move to the prestigious Methodist Girls High School, Yaba, Lagos (the oldest secondary school for girls in Nigeria, founded in 1879), where she graduated as the Best Form V Student in 1968 (Arts Class), received prizes and also served as a School Prefect. She joined the then Federal Inland Revenue Department, (FIRD), (now (FIRS) in 1976. She retired in 2010 having worked for 34 years. At FIRS, she took part in major tax reforms, review of tax laws and enforcement activities and was one of those who took an active part in the emergence of both the Value Added Tax and the National Tax Policy document for Nigeria. Professor Teju Somorin has contributed significantly to the growth of the CITN where she had served as Member, Vice-Chairman or Chairman of nearly all the Committees of Council before attaining the position of President of the Institute.

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CHAPTER 1

VALUE ADDED TAX CONCEPT AND HISTORICAL DEVELOPMENT IN NIGERIA

Abstract

The basic philosophy of taxation is embedded in the raising of public funds, which is used by the Government to provide public goods and services for its citizens. The paper traces the historical development of raising public funds through indirect taxation using the Value Added Tax (VAT) method. German businessman, Wilheim von Siemens and American Economist, Adams, first initiated VAT as an indirect tax. However, their idea was crystallized by Maurice Laure' the Joint Director of the French Tax in 1954 and later introduced in several countries of the world that at present, about 140 countries including Nigeria, have introduced VAT into their tax system. Nigeria's introduction of VAT was necessitated by the quest to diversify the revenue base through the reform of the nation's tax system. The reform led to the establishment of two Study Groups in 1991 and consequent upon their recommendations, a Modified VAT (MVAT) Committee was set up to undertake the preliminary work for the VAT and on August 24, 1993, the VAT Decree No. 102 was signed into law and took effect in January, 1994. VAT can be defined as a tax on consumption of goods and services. The chapter argues that the objectives are achievable by eliminating pitfalls such as ineffective administration, low base, low compliance, low remittance of revenues collected, non-judicious use of revenues, lack of infrastructure and low awareness etc. Thus, going forward, VAT in Nigeria has to come stay and will succeed with proper administration and implementation, which promotes compliance and citizen's trust.

1. Introduction

Taxes have been with us for as long as civilization. It is one of the important sources of providing internally generated revenues for government's expenditure. The Value Added Tax (VAT) as a means of taxation was introduced as an indirect tax on the supply of goods and services, which is eventually borne by the final consumer but collected at each stage of the production and distribution chain. It is a general consumption tax on goods and services calculated by adding all the costs involved in making and distributing goods and services minus the amount that business can claim back during the production process for their inputs. VAT is tax on spending and touches on every stage of the production process so that generally, individuals who spend the most on purchases pay the most VAT.[1]

German businessman, Wilheim von Siemens and American Economist, Adams are credited with the development of the idea of a VAT in the 1920s and what was only an idea by them has since been built into a system by Maurice Laure' who was the Joint Director of the French

Tax in 1954. Thereafter, Brazil through the country's fiscal reform introduced the VAT in 1965 to apply to all stages of production and other countries followed up to its introduction in Nigeria in 1993 through the quest to diversify the nation's revenue base.

This quest led to the establishment of a Study Group in January 1991 headed by Professor Edozien and a parallel Study Group on the Indirect Tax System in April 1991 headed by Dr. Sylvester Ugoh.

Against this backdrop, this chapter highlights the nature of VAT, the rationale for its introduction and its development in some climes while focusing on the historical development of VAT in Nigeria. The introduction of VAT by about 140 Countries of the world[2] shows that VAT is a reliable source of tax revenue. VAT has become relevant as countries reflect on the need to raise revenue to deal with the significant increases in public debt caused by economic and finance crises. It helps in making forecast of government incomes possible resulting in possibility of better planning and also guarantees the continuity of the flow of income into government treasury. However, VAT has suffered challenges in its ability to raise maximum revenue and reduce consumption patterns hence, the paper argues that Nigeria must ensure proper administration and efficiency through widening the VAT base, presumptive tax, establishing threshold, proper collection and accountability, judicious application / use of VAT revenue and continuous reform. These will promote compliance, increased revenues, provision of public goods and services, citizen's trust and growth of the economy.

The advocates of VAT contend that it is an efficient method of raising revenue for the government and that it would permit concomitant reductions in income tax. Many ascribe the global spread of VAT to the fact that it is a consumption tax, best suited to the revenue needs of states in an increasingly globalised economy.[3] Even those who recognise the role of key regional and international institutions in promoting VAT often attribute the motives behind the promotion to the merits of the policy instrument itself.[4] As a result, the rise of VAT is credited to virtues, such as the tax being the best method of taxing general consumption, its neutral treatment of exports, and its revenue-raising capacity.[5]

On the other hand, the opponents argue that, as a regressive tax, it puts too much burden on those who are least able to afford it.[6] Additionally, since this is a regressive tax, those with lower income bear the greatest burden.[7] The burden of VAT, like that of other consumption taxes, tends to be passed on to the final consumer.[8] However, to minimise this burden, necessities are often taxed at a lower rate than luxury items.[9]

2. Nature of VAT

VAT can be described in the following ways:

a. Economically, it is the difference between the worth of outputs and inputs
b. Legally, it is the difference between the value of goods and services supplied and value of goods and services bought. The VAT is the kind of multipurpose tax which is

calculated and collected according to percentage of value added to the goods and services produced and supplied in the process of production and distribution cycle.[10]

c. Represents all income from sales, rentals, charges and fees relating to activities enjoyed by customers
d. An *advalorem* tax because it is imposed upon the difference between the cost of an asset to the taxpayer and the present fair market value of such asset. It is a tax based on a percentage of the value of the property subject to taxation as opposed to a specific tax which is a fixed sum applied to all of a certain class of articles
e. Tax on spending hence, the rebuttable presumption that individuals who spend the most on purchases pay the most VAT
f. Tax borne by the final consumer of goods and services because it is added to the price paid
g. Tax on final consumption and eliminates all taxes on businesses throughout the production chain leaving businesses free to organize in the most efficient way it chooses without any tax induced biases or distortions.[11]
h. Touches on every stage of the production process
i. Indirect tax paid to the Government by the seller rather than the person (consumer) who ultimately bears the economic burden of the tax

In all, VAT features, display consumption and multi-stage tax whose incidence is borne by the final consumer and is calculated by adding all of the costs involved in making and distributing goods and services minus the amount that businesses can claim back during production process for their inputs. Indeed, the purchaser sees it as tax on the purchase price while the seller accepts it as tax only on the value added to a product, material or service. Thus, the manufacturer remits to the government the difference between these two amounts and retains the rest to offset the taxes previously paid on the inputs and the Government only receives the difference as tax paid on gross margin of each transaction by each participant in the sales chain.[12]

3. Rationale for VAT

The rationale for VAT varies from country to country. Many countries introduced VAT owing to dissatisfaction with the existing Sales Tax such as Wholesales Tax, Manufacture Tax and Cascading Turnover Tax.[13] This dissatisfaction in most cases was economically motivated by the need to diversify the revenue base of indirect taxes. In Japan, it was introduced in response to the macro-economic problem situation of the post Second World War. Guatemala in the 1980's introduced VAT as part of the reforms required to redeem the country from grave economic regression worsened by political problems. Jamaica was in similarly economic distress when it launched a tax policy that contained VAT in 1986/87. The introduction of VAT by Indonesia and Colombia was precipitated by economic needs borne out of fiscal crises. In Nigeria, the implementation of VAT was recommended owing to studies on how the nation's tax systems could be diversified to raise revenue while for the European Economic Community (EEC) countries, it was critical for membership.[14]

VAT is also justified because it is a:

a. Methodology and way of thinking which shows more social equity without any negative effects on investment and production motiVATion. It is pay as you buy or consume. This way, VAT addresses regressivity
b. Self-control system which reduces collection system cost and shows transportation of transactions
c. Money-spinner that helps countries raise the percentage of indirect tax contribution to gross tax receipts, which is usually dominated by direct tax returns
d. Reliable, consistent and flexible source of income whose implementation results in improvement of technology, taxation system and accounting
e. Revenue source in a neutral and transparent manner and is one of the most effective instruments for generating government revenue, as marginal cost of raising funds for public purposes through VAT is generally lower than it would be if other taxes were employed. VAT's neutrality is its potential for eliminating the tax burden on intermediary businesses and shifting the burden to final consumption only. This way, VAT is capable of complete economic neutrality in terms of business organisations and processes, consumption choices and consequent investment choices
f. Key considerations for the European Union (EU) in the need to replace levies on state enterprises anticipating membership of the EU. Therefore, VAT's neutrality toward international trade makes it a preferred alternative to custom duties in the context of trade liberalization. VAT is neutral to international trade because it is paid at the point of consumption
g. Source of advantage for exports to allow the recovery of the input tax because certain imports by domestic firms are tax deductible so in such areas of import, VAT will not affect the competitiveness of domestic firms
h. Relatively secure source from serious fraud in the domestic market because it relies on staged collections mechanism in which successive taxpayers are entitled to deduct input tax on purchases and have to account for output tax on sales. In the end, the tax collected by tax authorities should equal the tax paid by the final consumer
i. Good money source according to economists, that encourages savings and investments because it is a tax on consumption and not on income or profit
j. Tax that has a cascading effect because it has built-in credit and refund mechanisms
k. Tool of fiscal policy because the rates can be varied or modified to achieve specific economic objective
l. Tax that promotes voluntary compliance because it is based on self-assessment
m. Tax that is easy to compute because it is based on actual selling price of goods and services
n. Tax that encourages record-keeping by businesses

Overall, VAT appears as an efficient tax because revenue is secured while collected throughout the chain of production unlike a retail sales tax which all revenue may be lost if there is evasion at the final stage.[15]

4. Brief Historical Development of VAT in Some Climes

The history of anything tells us that life can be lived forward but can only be understood backwards. The origins of VAT have never been decisively settled.[16] Attribution is variously accredited to the German Businessman, Wilhelm von Siemens in 1918 and the American Economist, Thomas S. Adams from 1910-1921. However, von Siemens's VAT Concept was the addition type in which the tax base would be the sum of wages and capital income. This discouraged cheating and smuggling so was the original concept historically used to counter evasion in a sales tax or excise. The Germans designed it as a technical innovation to solve the financial problems of the German government on the turnover tax.

In Japan, following the economic dislocation of the Second World War, there was need to reform the tax structure to shore up the economy. A team of Tax Experts directed by Professor Shoup in the 1930's to study the tax system and prescribe reforms proposed the introduction of VAT in 1948 in response to the macro-economic problem situation of the post Second World War. When Japan's gridlock to introduce VAT was broken, the law limited the number of exempt supplies and applied a single rate to a comprehensive base of taxable supplies. Informed by this, the United States of America State of Michigan decided to experiment the implementation of what looked like a modified VAT in 1953. Later VAT was introduced in Argentina[17] but implemented first in France by Maurice Laure' in 1954 when France began series of tax reforms which included the introduction of VAT on the consumption of goods. France VAT introduced production tax, which was a type of excise duty that applied only to manufacturers in the first instance and to the production and wholesale stages of the business supply chain after the second step. Later the tax was changed to a consumption type, which gave full credit for tax paid on investment goods. Though France had legislated a full VAT in 1954, it was only in 1968 that VAT became operational and this was also the same time it commenced in Germany.

During this time, most countries of the EEC[18] relied on inefficient cascading multi-stage turnover taxes for indirect taxation on consumption. The turnover tax levied in Belgium, Germany, Italy, Luxembourg and the Netherlands had a cascading effect collected at every stage of production and distribution with no credit for taxes collected and paid to government at earlier stages. The effect was that the tax included in the final prices varied widely even for the same products taxed at the same rate in the same country. Later there was an agreement for a better consumption tax that would tax final consumption which operated on a destination basis and would prevent cascading tax as goods and services moved from country to country. The VAT was seen as an ideal solution to the dilemma.

The adoption of VAT by EEC was made obligatory under the Treaty of Rome signed January 1957 and backed by reports from Neumark and Jansen Committees. The EEC adopted VAT in 1967 and later made its adoption a condition precedent for membership. They were then obligated to agree to accept VAT but to levy different rates for different types of supplies and treating many other supplies as exempt supplies. Thus, multiple rate structures were designed to enable VAT become a tax capable of attracting sufficient support for

implementation across the Community.[19] Few years later, Nicholas Kaldor prescribed the implementation of the expenditure tax in India in 1957. In 1965, Brazil through the country's fiscal reform introduced the VAT to apply to all stages of production. By 1965, VAT expansion was limited to 10 Countries as most general consumption taxes in the Organisation for Economic Cooperation and Development (OECD) were retail sales taxes. The EU on April 11, 1967 adopted the first two VAT Directives, which established a general multistage, but non-cumulative turnover tax to replace all other turnover taxes in member states.

The VAT spread gradually in Europe and beyond. The European Union and its predecessor EEC are given credit for the spread of VAT in Europe.[20] The European countries to operate a full VAT was Columbia January 1965, Denmark in July 1967 and then Asia with South Korea as the first to introduce VAT with the help of the International Monetary Fund (IMF). Later, other countries such as Turkey, Pakistan, Bangladesh and Lebanon introduced VAT. It was adopted in Sweden in 1969, Austria, 1971, Ireland in 1972, Belgium January, 1973, the United Kingdom (UK) in November, 1974, replacing the purchase tax as a consumption tax levied by the National Government and administered by Her Majesty's Revenue and Customs (HMRC) through the VAT Act, 1974. Chile adopted VAT in March 1975 until 1986 when a new model for the VAT now called Modern VAT appeared in New Zealand. In 1986, New Zealand VAT Law closely followed with its substantive rules differing from the traditional European VAT by using a single rate and keeping exemptions to an absolute minimum. They also carefully choose definitions and rules intended to overcome the multitude of technical problems that had become evident in Europe. It quickly became a model for the modern VAT Law spreading across the English-speaking world including Canada, South Africa, Singapore and Australia.

In Iran, the VAT Bill was first presented to the Islamic Consultative Assembly (Parliament) in January 1987 for the reason of stabilizing the prices and by 1989, 48 Countries primarily located in Western Europe and Latin America and some developing countries like former colonies of France, Cote d'Ivoire and Senegal had adopted VAT. By 1991, the Financial Department of IMF proposed the use of VAT Policy as one of the factors for increasing the efficiency of the tax system. After series of suggestions and deliberations by experts and feasibility studies, the Bill was made into law. In Nigeria, VAT was introduced in 1993 via Decree No. 102, which replaced the Sales Tax Decree No. 7 of 1986.

5. Historical Development of VAT in Nigeria

The march towards VAT in Nigeria can be traced to the following factors:[21]

a. International revenue generation was fast dwindling and nearly all the States' Governments had reduced funds. There was therefore the need for increased revenue
b. All the progressive economy of the world had introduced or were introducing VAT
c. The Economic Community of West African States had introduced and harmonized VAT. VAT introduction in Nigeria was necessary for compatibility with the Franco-Phone West African Countries

d. The introduction of VAT will eradicate all other taxes related to goods and services, help to curtail tax evasion as well as replace the Sales Tax Decree No. 7 of 1986[22] introduced in Nigeria by the repealed Sale of Produce (Taxation) Ordinance No. 12 of 1953. The idea of replacing the Sales Tax with VAT was necessary because the base of sales tax was narrow targeting only locally manufactured goods and covering only nine categories of goods plus sales and services in registered hotels, motels and similar establishments
e. VAT is a money-spinner that will help raise the percentage of indirect tax contribution to gross tax receipts because its base is broader and includes professional services and profit generating banking transactions. Therefore, VAT would increase public funds and help in avoiding the taking of loans from international agencies. Also, VAT being on general consumption behavior is neutral and, would produce high yield
f. VAT is equitable because it relates to every purchaser and would bring more stakeholders into the nation's tax system
g. The government's desire for tax reform to create an efficient tax system based on taxes that are politically feasible and administratively practicable to generate more public revenue and at the same time reduce the tendency for economic distortions. According to the National Tax Policy,[23] there was an urgent need to diversify tax revenue by moving from the lopsidedness over dependence on oil taxes hence, the need to introduce indirect taxes and reduce the rates of direct taxes so that the tax system can strike a balance between the cost of doing business in Nigeria and savings, investment and consumption until such a time that equilibrium exist for direct and indirect taxes in the non-oil sectors.

With all these considerations, on 9th January 1991,[24] the Study Group on the Nigerian Tax System and Administration headed by Professor Emmanuel Edozien was established.[25] The Study Group was to review the entire tax system by critically examining the changes made since independence, evaluating the effectiveness of the system and proffering recommendations.[26] Again, on April 20, 1991, a parallel Study Group led by Dr. Sylvester U. Ugoh was set up to assess the Indirect Tax System in Nigeria with the responsibility to study the feasibility of introducing VAT in Nigeria as an improvement of the existing sales tax.

After series of empirical studies and research tours within and outside the country, the Study Groups came out with a major outcome in November 1991 that VAT should be introduced in Nigeria after two years of preparatory work. Following this, the Government adopted the Modified Value Added Tax (MVAT) in principle giving a period of two years within which necessary machinery would be put in place for the introduction of VAT. Thereafter the MVAT Committee was set up on June 1, 1992 led by Ijewere to undertake preliminary work and examine the feasibility of the earlier recommendation to introduce VAT.[27]

Adoption of the VAT went through several arguments and considerations. These included:

a. The Institution to Administer the VAT: There were concerns about the Country's

preparedness and the competence and suitability of the Federal Board of Inland Revenue (FBIR) to administer the tax effectively.[28] By December, 1993, possibilities of administering the tax existed among the Institutions that administer customs and excise duties, internal indirect taxes, income taxes or a Special private Commission to be set up for the implementation of the tax, making the choice of administration of VAT a case between four institutions - the FBIR with its Federal Inland Revenue Service (FIRS), the States Inland Revenue Service, Customs and a separate VAT Commission. At this time, Chief D.A. Olorunke as the Director-General of the Federal Ministry of Finance headed the FBIR. J.K. Naiyeju later took over from him as first Executive Chairman from November 1992 – February 5, 1999 and observations made were that in some countries for example, in the 18 of the 21 OECD countries that had VAT, the same Inland Revenue Department administered it. In Belgium, Luxembourg and the United Kingdom, there was a close cooperation between the direct tax authorities of the Inland Revenue Service and the VAT Customs Administrators. In the United Kingdom, the Board of Customs and Excise administered VAT. Only Indonesia established a separate VAT Commission but there was a move to integrate it with the Direct Taxes of the Inland Revenue Service. In Nigeria, it was discovered that the personnel of Customs and Excise are not trained and experienced in many intricacies of VAT administration such as examination of taxpayers records, auditing, cross checking, information matching etc. Therefore, it was considered that the Institution administering other indirect taxes such as sales tax should handle it. This is why the States were clamouring to administer VAT especially as the MVAT Committee was alleged to advocate a modified value added tax which did not provide built-in credit system to mitigate cascading effects of a multi-stage tax like VAT. The Federal Government argued that Nigeria opted for VAT not a modified VAT. Indeed, VAT is not a replacement for sales tax rather a higher tax that required expertise and that information obtainable from VAT returns is relevant and useful for income tax. Therefore, the Institution administering income tax that is the FBIR should administer VAT so that it does not suffer the set back of sales tax. Another issue was the creation of a new Commission to administer VAT which was even canvassed by the MVAT Committee but this was considered as a duplication of Institution which will also create coordination complexities amongst the Institutions especially realizing that the Ghana's experience of setting up a new Commission was not a success story. In all these, the Federal Government settled for the FBIR

b. There were also arguments by the States that they were the ones entitled to VAT proceeds because VAT only replaced sales tax which they administered. The Federal Government argued that VAT was an improvement on sales tax and not a replacement and that since they are the arm of Government with exclusive Constitutional powers to legislate on tax matters including the taxation of consumption, they will also share from the revenue. This was accepted by the Federal Government so that at inception in 1994, only the States and the Federal Government enjoyed the revenue to the exclusion of the Local Governments

c. Launching a new tax at a time of inflation did not go down well with many fiscal economists, government functionaries and members of the organized private sector. Members of the Federal Executive Council vehemently opposed its introduction because it was perceived as ill-timed and not acceptable considering the economic and austerity measures in place at that time[29] but the Ministry of Finance under Chief Olorunke[30] persisted and it was approved after the FBIR had assured the Federal Government that it had put in place adequate machinery to administer the tax which will be at a 5% rate,[31] and the rate was not likely to be unduly burdensome as to cause disaffection
d. For the multinational companies, they argued that the rate of 5% was low because any rate below 10% - 15% was uneconomic and could not provide surplus revenue. Again, VAT would bring a reform of the Sales Tax therefore, what should be established was a Modified VAT[32] because the Nigerian economy was not sufficiently structured to produce the necessary data and discipline for VAT collection. Accordingly, the classical VAT should not be in operation until such a time that the Nigerian economy had matured for it because even the record keeping of sales in Nigeria was very low and may lead to serious degree of evasion and avoidance in the system
e. For the World Bank Team, a 15%-17% was better than a 5% rate because that would produce paltry revenue. The Federal Government rejected this argument because it preferred to start a new tax under a depressed economy with attendant social problem with a very low penetration rate to avoid public resistance. Indeed, the first year returns later vindicated Government's stand
f. The Trade Union also argued that the introduction of VAT would add to the existing taxes and fuel high rate of inflation in the country especially as a group of assessors had argued that the tax revenue projection of N6b for 1994 which was the experimental year for VAT was unrealistic. This was owing to the fact that the IMF had estimated an amount of N4.5b as the projection for 1994 and even the Sales Tax being replaced by VAT yielded only N1.2b in its nine years of existence.[33]

Despite these challenges, the Federal Government accepted the introduction of VAT and consequently directed the Honourable Minister of Finance to commence the new tax on an experimental scale with a small outfit within the Federal Ministry of Finance. This was made public by the announcement by Dr. Chu S. P. Okongwu, Minister for Budget and Planning of the approval of VAT with a single rate to replace the Sales Tax in its entirety to avoid multiplicity of tax structures. The Government agreed to introduce VAT by the middle of the year, 1993. It was later shifted to September 1st. Later, Prince Oladele Olashore, the Honourable Secretary of Ministry of Finance in the Interim National Government of President Ernest Shonekan saw the need to commence the new tax without further delay and directed the MVAT Committee to liaise with the FBIR, the agency responsible for the administration of income tax in the Ministry of Finance for a smooth handing over of the preliminary work done so far on the assignment of the Committee. The MVAT Committee finally wound up its midwifery activities in June 1993 when FBIR fully took over the

implementation of the new tax but the final commencement of VAT was announced by the then Head of State, General Sanni Abacha in the 1994 Budget Speech.

With the promulgation of Decree No. 102 of 1993, VAT came into existence abrogating the Sales Tax Decree No. 7 of 1986. However, the VAT Decree, which took effect on 1st December 1993, did not commence until January 1, 1994. Alhaji Ibrahim A. Zukogi was appointed the first Director of VAT in 1993 and later became the Director of Human Resources who played the major role of recruiting VAT Officers deployed to various VAT Offices created at that time. He was also the Chairman of the FBIR from February 6 1999 - June 6, 2001. N. K. Naiyeju took over from him until he was appointed Accountant-General of the Federation and handed over to Ballama Manu who became Chairman from September 2001 – April 2004. By May 2004, Ifeuko Omogui-Okauru took over the FIRS as Executive Chairperson until April 12, 2012 when Kabir Mashi was appointed Ag. Executive Chairman of the FIRS. Mr. Samuel Ogungbesan was later appointed Ag Executive Chairman and was replaced in 2015 by Mr. Babatunde Fowler. At the expiration of his tenure on December 9, 2019, Mr. Muhammad M. Nami was appointed and is the present Executive Chairman of FIRS.[34]

Decree No. 102 of 1993, VAT came into existence in Nigeria as an indirect tax imposed on the net sales value of non-exempt, qualifying goods and services. The Decree was arranged into 6 broad parts with 3 Schedules and contained 43 sections. The 6 parts covered imposition of VAT, administration of the tax, returns, remittance, recovery and refund of tax, the establishment of a Technical Committee to advise on the tax from time to time, offences, penalties and other miscellaneous items. The 3 Schedules provided details of taxable goods and rate of tax, taxable services and rate of tax and exempt goods and services. The Decree places administration of VAT on the FBIR to do all such things as it may deem necessary and expedient for the assessment, collection and accounting for the tax.

The operation of the VAT as a consumption tax payable on goods and services consumed by individuals, government agencies or business organisations ensures that at each production level; the entire economy helps in its enforcement. VAT is charged and payable on all income from sales, rentals, charges and fees relating to supply of goods and services enjoyed by customers under the Act other than those goods and services listed in the first Schedule to the Act.[35]

The VAT Act was amended in 2007 by the VAT (Amendment) Act No. 12 of 2007 and mandates all purchasers of chargeable goods and services to pay 5% flat rate of the purchase price as tax. This rate is borne by the final consumer on the value of all taxable goods and services as determined under sections 5 & 6. VAT is collected on behalf of the Federal Government by businesses and organisations recognized as sellers and providers of such goods and services. They must be registered with the Tax Authority to ensure payment and remittance, which is made monthly to the FIRS Integrated Office on or before the 21st day of

the month next following that which the supply was made under a zoning arrangement into the bank zoned to the Local VAT Office[36] and finally paid into the VAT Pool Account rather than the Federation Account as, provided by the 1999 Constitution.

VAT operates on the basis of self-assessment and is structured in a way that a registered person is able to take credit for the VAT paid. This way, the registered person can indemnify itself against any loss. The FIRS has a duty to enlighten and sensitize citizens on the workings of VAT. This includes teachings about forms and circulars on VAT registration, administration and compliance for example, VAT Registration Form (VAT 001),[37] Return Form (VAT 002),[38] Monthly Return on VAT Reconciliation Statement from Area Offices to Zonal Office (VAT 003), Returns of VAT Reconciliation from Zonal Offices to Headquarters (VAT 004), Returns of VAT Collection to a Designated VAT Account in the Federation Account (VAT 005) and Pay-in-Form.[39] In addition, the FIRS produces series of Information Circulars for taxpayer's education such as: Information Circular No. 9304,[40] Information Circular No. 9305 dated November 5, 1993 and devoted exclusively to the operation of VAT on imports, Information Circular No. 9401 dated March 1994 and contains a comprehensive list of exempted goods and services, Information Circular No. 9501 dated January 13, 1994 on VAT refund procedure, Information Circular No. 9502 dated February 20, 1995 on Guidelines on the Collection Procedure for VAT by Ministries and Parastatals, and Information Circular No. 9503 dated December 1, 1995 on VAT operations in Banks and Other Financial Institutions,[41] Information Circular No. 9701 dated March 1, 1994 and updated on January 1, 1997,[42] Information Circular No. 9901 to update changes in the VAT Legislation, Information Circular No. 9902 dated January 1, 1999 on Guidelines on the Collection Procedures for Withholding Tax and VAT by Ministries, Parastatals and Other Government Agencies and Information Circular No. 2005 / 01dated February 2006 on tax invoice and its relevance to VAT operation etc.

There are variants of VAT. The phrase "VAT" refers to the mechanism by which the tax operates not what it ultimately seeks to tax for example, the Japanese call it "Consumption Tax", the English call it "Goods and Services Tax" and Nigeria decided for consumption variant. Also, VAT Systems can also be called Modern or Traditional. European VAT Systems are traditional because they generally have multiple positive rates and high exemptions while the Modern has a single positive rate with fewer and much more tightly targeted exemptions.

Nigeria operated the modern model and the rate as at 2005 was 5% for goods and services and zero-rate for exports.[43] In 2006, the Federal Government attempted to increase the rate from 5% to 10% when the Federal Government lost N570 billion oil revenue due to the activities of militants in the Niger Delta leading to a budget deficit record of about N21billion and also to synchronise it with the ECOWAS Protocol. This was done by the then Minister of Finance, Nenadi Usman exercising the powers of the Minister to vary the rate of VAT in the Schedule to the Act.[44]

Nigerians rejected the increase therefore, as at 2006, Nigeria's VAT rate was worrisome because it could not match the ECOWAS adopted Uniform VAT Protocol due to constant movement of people and goods across the countries in the sub-region. Owing to Nigeria's influence, the ECOWAS advisory rate was reduced to 10% yet Nigeria despite being a signatory to the Protocol was still operating at 5%, which is the lowest rate across the sub-region. With the urgent need to increase and diversify the nations revenue base which is badly needed in the country[45] in order to close the deficit gap in the budgets especially the 2020 budget, the President presented the Finance Bill 2019 alongside the 2020 Appropriation Bill to the joint session of the National Assembly on October 8, 2019.[46] The Finance Bill seeks to amend about 90 provisions in the Companies Income Tax Act, Personal Income Tax Act, Stamp Duties Act, Capital Gains Act, Customs and Excise Tariffs Etc. (Consolidation) Act, Petroleum Profits Tax Act and the Value Added Tax Act. On November 7 and 21, 2019, the Bill passed the second and third reading respectively at the Senate and was passed by the House of Representatives after the third reading on November 28, 2019. On January 13, 2020, President Buhari signed it into law. Nigeria thus has the Finance Act, 2019 which commences on February 1, 2020.[47]

Greater reliance on VAT is necessary to sustain governments revenue base and make up for any potential shortfall especially as VAT have overtime offered a more regular revenue inflow and lower compliance cost with huge prospect for improved tax compliance.[48] The Finance Act made the following amendments to the VAT:

a. VAT rate is now 7.5% with effect from February, 2020[49]
b. Goods and services are defined[50]
c. Modification of "exported goods"[51]
d. Specific requirement for VAT de-registration for discontinuing operations
e. Taxable persons require registering for VAT and file returns. These are those within N25m revenue threshold in a calendar year. Anyone outside the threshold is exempted from registering, collecting, remitting or issuing tax invoice[52]
f. Remittance of VAT now on cash basis
g. Expansion of VAT exemption list[53]
h. Exemption of assets sold in restructuring exercise or transferred to a related company or party in a restricting exercise[54]
I. Introduction of VAT reverse charge on imported services etc.[55]

The Finance Act, 2019 was amended in 2020 to the Finance Act, 2020 which came into force January1, 2021.[56] The amendment to VAT payment are as follows:

a. Taxable supply with respect to goods[57] shall be deemed to take place if the goods are physically present in Nigeria at the time of supply, imported to Nigeria, assembled or installed in Nigeria (that is the goods is situated, registered or exercisable in Nigeria) or the beneficial owner of the right in or over the goods is a taxable person in Nigeria
b. Taxable supply with respect to services are services consumed by a person in Nigeria whether rendered within or outside Nigeria excluding employment
c. In respect of corporeal, it includes exploitation of a right, acquisition or assignment

of rights by a person in Nigeria

d. Incorporeal is connected with tangible or immovable asset located in Nigeria
e. A non-resident person that makes a taxable supply to Nigeria is required to register for tax and obtain Tax Identification Number (TIN), include VAT on the invoice and may appoint a representative in Nigeria for the purpose of its tax obligations
f. Commercial airline tickets and hire or lease of agricultural equipment for agricultural purposes are exempted from VAT payment.

The changes made are capable of boosting the economy by stimulating growth of Micro, Small and Medium-sized (MSMs) Enterprises and also encouraging Foreign Direct Investment (FDI) into Nigeria however; every new law comes with its challenges and opportunities.[58] Increasing the rate of VAT may be challenging leading to higher cost of production and increase in the volume of unsold goods with its attendant result of reduced capacity utilization and ultimate loss of job and high rate of unemployment, exacerbation of poverty, environmental volatility, social unrest and rise in inflation but the opportunities exist. These include compensation with palliatives (such as improvement on VAT administration and correction of anomalies in the VAT in line with global practice as well as provision of options such as threshold to protect low-income earners),[59] increase in VAT revenue yields, judicious use and application of VAT revenues and curtailing consumption patterns.

6. Definition and Basic Features of VAT

In order to facilitate the reader's understanding of this chapter, it is now pertinent to examine the various definitions of VAT proffered by some key authors. VAT has been defined as an indirect tax on the domestic consumption of goods and services, except those that are zero-rated (such as food and essential drugs) or are otherwise exempt (such as exports).[60] It is levied at each stage in the chain of production and distribution from raw materials to the final sale, based on the value (price) added at each stage.[61] It has also been defined as a consumption tax levied at each stage of the consumption chain, and borne by the final consumer of the product or service.[62]

In a similar vein, Soyode and Kajola defined VAT as a consumption tax, charged at 5% on all valuable goods and services.[63] They went further to state the attributes of VAT as "a consumption tax, a multi-stage tax, and the incidence of which is on the final consumer."[64]

Also, VAT has been defined as a consumption tax on the value added to a product.[65] In other words, it represents a tax on the "value added" to the product throughout its production process.[66] The VAT system is invoice-based and each seller in the product chain includes a VAT charge on the buyer's invoice.[67]

In this connection, it is a multi-stage tax levied only on value added at each stage in the production process with the provision of a set-off for the tax paid at earlier stages in the chain, which can be appropriated against the VAT liability on a subsequent sale.[68] The objective of

this tax model is to avoid "cascading", which can have a snowballing effect on prices.[69] The assumption is that, due to cross-checking in a multi-staged tax, tax evasion will be checked, giving rise to increased revenues to the government.[70]

From the foregoing definitions, it is clear that VAT is not a cost to the producer or the distribution chain members and, whereas its full brunt is borne by the end consumer, it avoids the double taxation (tax on tax) of a direct sales tax. VAT gives sellers along the supply chain a direct economic motiVATion to collect the tax; it is more transparent and uniform than other taxation models; it avoids under-valuation at all stages of production and distribution, and is, therefore, less prone to tax evasion.

Basic Features of VAT

It is necessary to examine the key terms underlying the features of VAT, and by so doing, provide a brief and basic outline of some of the more fundamental principles of VAT. These are now discussed below.[71]

Standard Rate

This is the VAT rate applicable to all taxable goods and services, which varies from one country to another. For instance, the VAT rate on the value of all goods and services in Nigeria was 5% [72]until the Finance Act 2019 came into force on Monday 13th January 2020. Under the Finance Act, the applicable rate is 7.5%.

Zero-Rated Supplies

These are supplies of goods that would have a VAT rate of 0 percent. This simply means that VAT will be charged on these classes of goods and services at the rate of 0 percent. The supplies are categorised as zero-rated.[73]

Taxable and Exempt Supplies

A taxable supply is defined as everything which is not an exempt supply, while an exempt supply means a supply of goods and services, where no VAT is charged.[74] It is, therefore, very germane to be very certain about what supplies are taxable and those that are exempt under VAT. For instance, VAT covers manufactured goods and imports, as well as professional and banking services, while it exempts essential goods, such as all medical and pharmaceutical products, basic food, books and educational materials, newspapers and magazines, baby products, fertilizer, agricultural and veterinary medicine, farming and transportation equipment.[75] Furthermore, services exempted include: medical services, services rendered by community banks, people's bank and mortgage institutions as part of learning and all exported services.[76]

It should be noted that an enterprise may be making mixed supplies, that is, both exempt and taxable supplies,[77] but a VAT liability on sales can only arise when a person is making taxable supplies. However, registered businesses cannot claim for VAT paid on their purchases that went into producing those exempt supplies.[78] A person making only exempt supplies is not

carrying on a taxable activity and, therefore, VAT is not chargeable on such supplies and a person making only exempt supplies is not required to register for VAT purposes, and will, therefore, have no VAT filing or reporting obligations.[79]

Goods and Services
The Finance Act 2019 made clarifications to the meaning of Goods and Services. Under the Finance Act, goods have now been defined to include all forms of tangible properties that are movable at the point of supply, any intangible product, asset or property excluding interest in land. Goods are to be deemed supplied in Nigeria and liable to VAT if they are physically present in Nigeria at the time of supply, imported into Nigeria, assembled in Nigeria, installed in Nigeria; or where the beneficial owner of the rights in or over the goods is in Nigeria and the goods or right thereof is situated, registered or exercisable in Nigeria.

Services are defined to include anything other than goods, money, securities and services provided under a contract of employment. Services are to be deemed supplied in Nigeria where the services are rendered in Nigeria by a person physically present in Nigeria at the time of providing the service; or where the services are provided to a person in Nigeria, regardless of whether the services are rendered within or outside Nigeria.

Taxable Person
For VAT purposes, a taxable person is any individual, partnership, company or other entity, which supplies taxable goods and services in the course of business and exploits tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business or a person or agency of Government, who operates in that capacity.[80]

Input Tax
This is the tax paid by a taxable person.[81] The law requires a taxable person to pay to the supplier the tax on taxable goods and services purchased by or supplied to the person.[82] Simply put, it means the VAT a registered business will pay on the value of imports and on the value of goods and services acquired or obtained from other registered businesses.

For a VAT registered enterprise, “Input Tax” is credited against "Output Tax", which is the amount of VAT charged on taxable supplies made by the enterprise.[83] For individuals making mixed supplies (i.e., both exempt and taxable supplies), input tax credits are allowed only for those inputs used to make taxable supplies.[84]

Output Tax
This is the VAT a registered business will charge its customers when they buy goods and services.[85]

Payment Due
This is the amount of VAT a registered business will have to pay over to the Federal Inland Revenue Service (FIRS) at the end of the tax period.[86] It is calculated by deducting the VAT

paid on all the business purchases in the month from the VAT collected on all the business sales of that same month.[87]

Consideration

Consideration, in a VAT context, has a very wide connotation but it essentially means anything that is given to or done for the supplier by the recipient in return for whatever has been supplied.[88] This means the amount paid or payable, whether in cash or in kind for a supply or an importation of goods or services.[89] This is usually money but can sometimes be goods or services supplied in return (i.e., a barter transaction).[90] Income received in this way is squarely within the scope of VAT and will either be taxable income or will be exempt from VAT.[91]

Invoice Credit System

All registered businesses are under an obligation to issue VAT invoices when conducting transactions with other VAT registered businesses.[92] A tax invoice shall be issued on supply, whether or not payment is made at the time of supply.[93] When conducting business with unregistered businesses and the final consumer, an individual is to issue a sales receipt, showing the cost of the item and the amount of VAT paid by the unregistered person. Without a Purchase Invoice from the seller, VAT registered businesses would not be able to claim for VAT paid on their purchases.[94]

7. Distinctions between VAT and Other Related Concepts

In this section of the paper, the author deems it worthwhile to distinguish VAT from such other related concepts, like retail sales tax and turnover tax. Although, the differences between VAT and these taxation models are clear, they do over-lap in some instances.

VAT and Retail Sales Tax

VAT and retail sales tax are two different forms of consumption taxes. Thus, they are different in the methods by which they are levied on consumers. VAT is a form of indirect tax, which is imposed on products or services at different stages of the manufacturing process.[95] Simply put, it is imposed on each stage of the supply chain and ultimately charged in full to the final purchaser and, because it is typically included in the price that the consumer pays, it is often not even visible to the purchaser.[96] The tax is paid to the government directly by the producer. The value added to any product may be calculated as the sales price, minus the cost of supply and the other taxable items.[97] Since the tax is imposed at every level of the production process, it becomes absolutely difficult to evade the tax payment. This system involves much needed transparency and is easy to comprehend; but one of its disadvantages is that it requires comprehensive handling of accounts.[98]

On the contrary, sales tax is levied at the time of the purchase of the products or services; it is easily calculated, charged on the final value of commodity, and the consumer knows how much he has to pay because it is separately stated on the invoice issued to the customer.[99] Therefore, it is a single-point taxation.[100] Thus, the step-by-step gradual accumulation of tax

funds, throughout the transformation from raw materials to finished product, does not occur here, as it does with VAT.[101] The amount of sales tax may be calculated as a percentage of the taxable price of the sale and the tax is collected from the consumer by the seller at the time of purchase.[102] The seller, at a later stage, transfers the tax to the responsible government agency.[103] Since sales taxes have stringent rules to follow, ideally, it should be difficult to avoid, have a high compliance rate, and easy to collect.[104] But the reality is actually different, as sales tax has a very high level of avoidance.[105]

Under Sales Tax, most imports are assessed for tax at the time of importation and no further liability arises as the goods go through wholesalers and retailers to final consumers.[106] Under VAT, however, all imports will be assessed for VAT at the time of importation and the VAT payable on imports will be allowed as a deduction against the output tax charged on sales, made by importers, who are registered for VAT purposes.[107]

Different Types of Sales Tax
When the term "sales tax" is used in a generic sense, it simply refers to the taxes that states impose on retail sales. However, there are different types of sales tax that, together, comprise the state's sales tax, which shall hereunder be examined *seriatim.*

Seller or Vendor Privilege Taxes
These taxes are imposed on retailers for the privilege of making retail sales in the state.[108] Retailers usually have the option of absorbing the tax (that is, paying the tax out of their own pockets) or passing it along to their purchasers.[109]

Consumer Excise Taxes
These taxes are imposed on the persons who make retail purchases in the state. It is usually charged on items that are not considered necessary for survival. For instance, items, like cigarettes, wine, and alcohol, usually have an excise tax tied to them.[110] This automatically raises the price of the items and provides additional revenue for community projects and programmes, while attempting to reduce consumption.[111]

For example, a bottle of wine, that normally costs N1,000 (One Thousand Naira) only, may have an excise tax of N100 (One Hundred Naira) only on it. The end result is that individuals will pay N1,100 (One Thousand, One Hundred Naira) only for that bottle of wine.

It should be noted that, in states that impose this type of tax, sellers serve purely as agents, who must collect the tax on the state's behalf and, because the tax is primarily the purchaser's responsibility, sellers do not have the option of absorbing the tax and usually must separately state the tax on the receipts or invoices they provide to their purchasers.

Retail Transaction Taxes
These taxes are imposed on the retail sale transaction itself, with the primary liability of paying the tax falling upon both the sellers and the purchasers.[112] Sellers are responsible for

collecting and paying the tax, and purchasers are responsible for paying the tax that the sellers must collect and pay.[113] In essence, this type of sales tax is a hybrid of the other two types; however, it bears close resemblance to a consumer excise tax because sellers are not given the option to absorb the tax.[114]

At this juncture, this writer submits that it is of the utmost legal importance for one to know the type of sales tax regime that one is dealing with because it will go a long way in determining who can be liable for the tax, who can sue on the tax, or who can make a claim for a refund of the tax.

VAT and Turnover Tax

A turnover tax, also known as cascade tax, is a tax paid on a good during or after its manufacture, rather than when it is sold, and it is usually calculated as a percentage of the value of a good.[115] It is similar to a VAT, with the difference being that it taxes all sales, including intermediate goods.[116] It is a tax on investment and also on the value of sales, with no credit for tax on inputs.[117] It is an indirect tax, typically on an *ad valorem* basis, applicable to a production process or stage.[118] For example, when manufacturing activity is completed, a turnover tax may be charged on some companies.[119] It is a very simple tax that is calculated on a business's turnover for a single year and normally tax is charged on the profits for that year.[120] This method of paying tax is great for small businesses, where record keeping is costly, since the tax payable can very quickly be determined by simply looking at all the incomes for that year.[121] Turnover tax is also very inexpensive, compared to VAT and other tax structures, as one does not need to hire tax consultants to administer the tax.[122]

In the light of the above differences, it is crystal clear that a VAT is considered an indirect tax, in that the tax is collected from someone, other than the person who actually bears the cost of the tax (namely the seller, rather than the consumer). It is also considered to be a consumption tax, because it is borne ultimately by the final consumer and not really a charge on businesses. Finally, it is collected fractionally through a system of partial payments, whereby taxable persons (i.e., VAT-registered businesses) deduct from the VAT they have collected the amount of tax they have paid to other taxable persons on purchases for their business activities. This mechanism ensures that the tax is neutral, regardless of how many transactions are involved.

8. How has VAT Fared in Nigeria?

VAT has a chequered history in public finance in Nigeria like many Countries of the World. For example, in 1949, it was discountenanced in Japan and in the UK; it did not have an easy entry because critics assessed the introduction in 1974 as an economic set back and a tab on the fiscal sovereignty of the EEC member-nation. Indeed, it took series of enlightenment campaigns, public education and adoption messages to counter the critics. In Nigeria, it was hotly debated and despite generating public fears, resistance and resultant controversies of regressivity, anticipated high administration costs especially the cost of monitoring the tax, apprehension that buoyant tax turnover might lure Government to extravagant expenditure,

compliance cost, effect on prices, incompatibility of VAT with sales tax and fear of inability of FIRS to administer the tax efficiently, VAT has come to stay.

It operates thus: Product moves from raw materials – Manufacturer – Wholesaler – Retailer - Consumer and at every stage of the chain, there is an increase in price which is finally paid by the consumer.[123] In this operation, the question is …has VAT achieved the objectives for its imposition - raise public funds and control consumption pattern of citizens? This will be answered examining the objectives vis-à-vis certain parameters as follows:

a. Revenue generating capacity: VAT has a significant impact on revenue generation in Nigeria. The VAT system, which harmonised the many consumption and production taxes that preceded it, has been effective in generating revenue. Statistics show that VAT proceeds since inception has been great especially in States where commercial activities are high. From a total of N8.6b in 1994 which was adjudged as 36.5% beyond the N6b projections of that year, VAT revenue has snowballed[124] and is a major money-spinner helping Nigeria raise the percentage of indirect tax contribution to gross receipts which was usually dominated by direct tax returns. The Act has witnessed significant changes in the design of its charging clauses which has been expanded to catch more taxpayers through expansion of registered persons, restricting the scope of refund and curbing evasion by making the issuance of invoice mandatory.

b. Efficient Administration: From revenue generation is the question of the fiscal policy ability of the tax system.[125] How has VAT administration fared? These questions arise in the face of certain challenges such as:
   - VAT is consumption tax and not an investment tax. VAT will only assist in investment as expected by government through exemptions in VAT related investment[126]
   - Existence of low registration of service providers because many taxable persons especially those in the rural areas are not registered. The Finance Act 2019 has expanded VAT base. There must be effective monitoring and auditing to get in necessary stakeholders[127]
   - Low and non-remittance of VAT owing to self-assessment will be cured by efficient monitoring and auditing capacity of the administrative authorities
   - Low Domestic compliance. Efficient collection, accountability and judicious use of VAT revenue will increase compliance
   - Low Cross-border compliance. VAT is payable by international taxable persons. The FIRS published a number of information circulars on VAT and this showed that VAT strictly construed is chargeable on international, inter-state and intra-state supplies of goods and services. Administering VAT at these levels especially the international level may pose administrative challenges in terms of the ability and capacity of the FIRS to administer the tax efficiently therefore, the challenge is FIRS' ability to monitor this if the subsidiaries decide to hide the details of such transactions
   - Complexities in granted exemptions. Some of the exemptions are not defined leading to complexities in identification and interpretation. This problem will still

arise for example on tangible goods until the provisions of the Finance Act is tested in the courts

- Lack of transparency. Unclear definitions for example, of exemptions will lead to discretions, loss of transparency and arbitrariness in the application of the Act
- Training of Officers will increase administrative capacity
- Elimination of fear that VAT will be paid on everything will demand training and Enlightenment of tax payers on VAT provisions and operations
- The continual exclusion of VAT revenue from the Federation Account violates section 162 (1) and (10) of the 1999 Constitution
- Increasing complaints especially from the organized private sector about the adverse effect of VAT will lead to rising operational cost and prices of their goods. This will create difficulty of compliance for the real sector which is already grappling which the challenges of multiple taxation and lack of infrastructure
- Companies operating in the oil and gas sector should not be treated on the same platform as government agencies or parastatals. Its yet to be seen if the threshold under the Finance Act 2019 solves this problem
- Agitations for increase of VAT rate to harmonise with ECOWAS States is still not satisfied with the recent increase to 7.5%
- VAT increases no doubt is borne by consumers because suppliers of goods and service providers treat VAT as input costs yet government injects VAT revenue back into the system as consumption expenditures. The resultant effect is disruptions in the economy
- Challenge in tax refund and accounting culture still exists
- The original Act consisted of 43 sections and 3 Schedules. This was amended in 1996 to create the VAT Tribunal to deal with all cases related to the tax. This amendment consolidated in VAT Act Cap. V-1 Laws of the Federation of Nigeria, 2004 consisting of 47 sections with one schedule, which contained the List of Goods and Services Exempt, derogated from the Constitutional powers of the Federal High Court in section 251 (1) (a) because appeals from the Tribunal went to the Court of Appeal. This arrangement contravening the exclusive jurisdiction of the Federal High Court continued because of the Constitution (Suspension and Modification) Decree No. 1 of 1984. Upon return to Democracy, the arrangement was challenged in *Stabillini v. FBIR*[128] and *Cadbury v. FBIR* [128]and with the establishment of the Tax Appeal Tribunal (TAT) in 2007 by the FIRS (Establishment) Act to handle all tax cases, VAT Tribunal and the Body of Appeal Commissioners were by necessary implication repealed. Tax disputes cases now lie to the TAT. However, there is an existing jurisdictional controversy about the status of the TAT with the exclusive jurisdiction of the Federal High Court under section 251 of the 1999 Constitution as amended.[130] We wait the final decision on jurisdiction
- Another issue is VAT revenue distribution: From inception, proceeds from VAT have been distributed according to the prescribed sharing formula at the Monthly Meetings of the Federation Accounts Committee. In 1994, the distribution formula was 20% to the Federal Government and 80% to the States.[131] There was no allocation

for the Local Government. At the end of 1994, the Federal Government increased its share to 50%. By 1995, when the revenue increased again, the distribution formula was again altered and has been so as revenue increased.[132] At present, the distribution of VAT proceeds formula is 15%, 50% and 35% for the Federal, States and Local Governments respectively. States like Lagos State are still clamouring for more funds by passing the Sales Tax (Schedule Amendment) Order) 2000. Does this not offend the VAT (Amendment) Act No. 15 of 2007 and the Doctrine of Covering the Field in Nigeria? In *Lagos State Board of Inland Revenue v. Eko Hotels & Anor,*[133] Sales Tax was held null and void and owing to this, Lagos State went ahead to pass the Hotel Occupancy and Restaurant Consumption Law (popularly called Consumption or Tourism Tax) to impose 5% tax on goods and services purchased from hotels, restaurants and event centres in the State

- Section 21 of the Act establishes the VAT Technical Committee comprising of the Chairman who is the Chairman of FIRS, all Directors of FIRS, Legal Adviser of FIRS, a Director of Nigerian Customs and 3 Representatives of the States Internal Revenue Service. They are to consider all the tax matters that require professional and technical expertise and make recommendations and advise the Federal Board of Internal Revenue on its duties of VAT administration in section 7 of the Act. This provision does not help the due administration of VAT because most of the persons represented are from FIRS making recommendations to themselves, the Federal Board of Inland Revenue which FIRS is a part of

c. Impact of VAT on Consumption: Understanding the peculiar nature of the Nigerian economy, the Act has not been able to control or reduce consumption pattern even with the expanded base because Nigeria is more of consumption than production nation. The existence of exemptions and waivers and their meanings lead to discretions that affects the collection and accounting mechanism especially at the retail level. With the Finance Act, exempt basic food list and definition may reduce the problem of interpretation minimally for example, there are arguments whether shares are VATable[134] or not and it may not also control consumption patterns

9. Conclusion

All over the world, VAT has come to be and this happened in Nigeria with the promulgation of Decree 102 of 1993. The considerations in adopting VAT in Nigeria were necessary to assure the benefits that indirect tax VAT will bring.

Revenue raising poses challenges but yields opportunities, which must be harnessed. Nigeria requires proper administration and efficiency to maximize the objectives for the imposition of VAT. The Finance Act 2019 has made several reforms, which should grow the nations revenue and the economy but while increasing revenue through VAT, the cost of compliance and administration must be low while transparency, judicious application / use and accountability for tax revenue must be promoted to increase compliance.

The VAT System must be sustained with continuous empirical analysis, effective stakeholder consultation and efficient political leadership. It is possible so, lets do it.[135]

10. Recommendations

Dealing with these issues is critical in order to bolster VAT revenues and control consumption patterns. The Finance Act 2019 and 2020 have both broadened the tax base to ensure that businesses are taxed in well-defined cases but there is continuous need to update the database of all service providers and guidelines for international issues affecting VAT for simplification and effective compliance. Businesses should be provided with certainty and clarity in ways of tax administration with corresponding penalties. Also, ways to combat VAT fraud and other abuses from international trade for example, strategies such as prompt and rapid exchange of information between countries for example, the Joint Council for Europe / OECD Convention on Mutual Administrative Assistance in Tax Matters is very good for countries to emulate as it allows for exchange of information on generic tax frauds and avoidance schemes. Citizens must be educated and sensitized on the provisions of the Act and its workings so that they embrace it and help to achieve its objectives.[136]

These concerns show the need to strengthen the benefits of the VAT as a reliable means of public revenue, which is not easily affected by economic crises. VAT provision of increased revenue and reduction of consumption of certain commodities will depend on good management and greater stakeholder compliance hinged on constant reform in the following ways:

a. Rate of VAT: The rate or rates at which VAT is levied is an important consideration in the operation of VAT. There are three rate models – single, double[137] and multiple rates.[138] Most of the countries that adopted VAT earlier implemented multiple rates and also delimited the tax base through exemptions. Over the years, some countries have moved from single to double and back to single for example, the United Kingdom. Multiple VAT rates must be avoided because it will affect the efficiency of the system and create complexity.[139] Nigeria introduced VAT in 1993 with a narrow base, single rate, low registration and number of zero- rates listed in first Schedule to the Act. Single -rate appears good and seems to be largely favoured by even developing countries for example; the 21 African Countries that adopted VAT from 1990 – 2000 have a single rate system.[140] Single rate VAT is also supported by the 2007 Copenhagen Economics Study and the 2008 Draft Chapter of the Mirrlees Review of the UK Taxes[141]
b. Simplification of the Administration of the VAT System. VAT administration must be simple and reduce compliance costs for businesses. It must be possible for businesses to pay VAT anywhere and the tax authorities will remit it to each other within a country or sub-region or any part of the world. There must be concrete measures to improve the level of transparency of tax revenue utilization. This is will be aided by better accountability to improve compliance
c. With the increase of VAT rate to 7.5% payable in Nigeria, it is 0.80% and the lowest compared to Gross Domestic Product (GDP) in many countries[142] therefore, there may be need for constant upward revision of rate. All over the world, rather than reduced rates,

there are exemptions and zero- rates in relation to specified items in different countries hence, the recent increase in Nigeria

d. Increased compliance is necessary to deal with VAT fraud, which reduces expected revenues
e. Broadening collection base is necessary to increase yields. It must be supported by effective and efficient monitoring for efficient performance
f. Open political debate and sufficient representation is very critical in VAT increase and administration. VAT like any tax is an expression of a political consensus. Citizens should be informed and consulted to be a part of any reform. Open public debate not only informs the citizens but also helps to build trust with the government and greater compliance. Therefore, appropriate consultation, communication and management is always necessary as part of a wider tax reform to help minimize the political costs associated with changes to any VAT System.[143]

ENDNOTES

1 Alan A. Trait, *Value Added Tax International Practice and Problems* (Washington D.C: International Monetary Fund, 1988) p. 4
2 The US is the only country in the OECD that has not adopted VAT
3. *Supra,* note 4, p. 5.
4. *Ibid.*
5. See, for example, OECD, Consumption Tax Trends, 23 (2008), quoted in *Supra,* note 8 at p. xi.
6. *Supra*, note 5.
7. Donald W. Parker, "The Value-Added Tax in the European Economic Community" (1988), 11 *Boston College International and Comparative Law Review*, p. 3, available at http://lawdigitalcommons.bc.edu/iclr/vol 11/iss1/10 (last accessed March 02, 2015).
8 *Ibid.*
9. *Ibid.*
10 Alan A. Trait, *Supra*
11 Richard Krever, *VAT in Africa* (South Africa: Pretoria University Law Press (PULP), 2008) p. 10
12 In comparism to Sales Tax, the VAT avoids the cascade effect of Sales Tax by taxing only the value added at each stage of production
13 Alan, *Supra*
14 J. k. Naiyeju, *Value Added Tax The Facts of a Positive Tax in Nigeria* (Lagos: Kupag Public Affairs, 1996) p.15
15 The demerits of VAT especially in Nigeria are the rate of 5% which is considered weak on the ground of being equity-deficient, difficult to predict the tax yield if goods and services are very elastic due to fluctuations and somewhat high administrative cost of monitoring compliance. The rate is now 7.5% under the Finance Act 2019
16 P. U. Oluyede "Prospects of State Sales Taxation" M. A. Ajomo & O. Akanle eds. *Tax Law and Tax Administration in Nigeria*, (Lagos: NIALS, 1991)
17 January, 1975
18 Now EU
19 E. Afe Ogundele, *Value Added Tax (VAT) Theory and Practice* (Lagos: University of Lagos Press, 1986) p. 3
20 The Community moved to rationalize and harmonise the rates and exemptions with the adoption in May 1977 of the Sixth Directive, which set out standards to which all Community VAT Laws were to conform to. These were re-enacted as amendment in 2006 VAT Directive. In January, 2007, another VAT Directive was adopted which consolidated all the existing provisions into one piece legislation and set the minimum rate at 15% allowing member states possible exceptions and derogations. The spread of VAT in Europe was driven by the fact that it is a prerequisite for membership of the EU and at present, it has accelerated spread especially with the support of IMF and is being implemented in about 140 countries of the world, contributing for about one-fifth of the total tax revenue
21 Abdulrazaq Muhammed T, *Introduction of Value Added Tax (VAT) in Nigeria* (Ibadan: Ababa Press, 2011)
22 The Decree became the Sales Tax Act Cap. 399 Laws of the Federation of Nigeria

(LFN) 1990 until the repeal with the introduction of VAT. Commenting on the Fiscal Policy Program, the Secretary of Finance, Prince Oladele Olasore in the Press Briefing on the 1993 Budget and National Rolling Plan announced the repeal in paragraphs 16 & 17 stating that this shifts the tax burden from production to consumption. The idea is to moderate the rate of the cost-push inflationary effects on the cost of production. This will also help rationalize the consumption behavior of the populace. Therefore, the tax favours the low-income segment of the population since VAT does not affect the basic needs of life such as food, shelter and clothing etc. The VAT rate is 5% … and the proceeds will be shared as follows - Federal Government 20% and State Governments 80%. The States are enjoined to abolish all other forms of Sales Tax and Levies while the amount distributable from the States' Revenue Pool will be shared on the following criteria: State of Origin 30%, Consumption / Destination 30% and Equality of States 40% and the VAT will commence operation by July 1, 1993. This commencement date was later shifted to September 1, 1993 and on August 24; VAT Decree was promulgated as Decree No. 102 of 1993. Though the Decree stipulated that VAT became collectible from December 1, 1993, it did not commence until January 1, 1994 when the various recommendations of Edozien, Ugoh And Ijewere-Led Groups were harmonised

23 2011 launched April 7, 2012

24 This was 13 years later after Nigeria inaugurated the Tax Force on Tax Administration headed by Alhaji Shehu Musa (to introduce withholding tax, impose 10% special levy on bank's excess profits and imposition of 2.5% turnover tax on building and construction companies)

25 The Study Group was commissioned on January 9, 1991 by the Hon. Minister of Finance & Economic Development, Alhaji A. Alhaji during the tenure of D. A. Olorunke as Chairman of FBIR

26 Indeed, some of the thrust reform included to review and consider new taxes, establishment of the Federal Inland Revenue Service (FIRS) as an operational arm of the Federal Board of Inland Revenue (FBIR) and setting up of revenue services at the States and Local Governments. The Study Group ion page 19 of its report dentified the need to transform the Sales Tax System into a Value Added Tax in Nigeria

27 Federal Ministry of Budget and Planning Study Group on Indirect Taxation, *Final Report on Modified Value Added Tax Study* (Ile-Ife: UNIFECS Consultancy Services Centre, Obafemi Awolowo University, 1991) The MVAT Committee later worked with the FBIR in 1993 for the later takeover of the administration of the new tax

28 The existing administrative structure at the FBIR had two mandatory and professional Directorates. When VAT was introduced, a new Directorate was established to take charge of VAT administration and the first Director of the VAT Directorate was Alhaji Zukogi

29 Account of Dr. Teju Somorin who was Secretary to the FBIR 1987-2000 & 2001-2003. She was the Secretary of the Study Group in 1991 and recorded the minutes of Group meetings, which was produced in six volumes. She was also the Coordinator of VAT Workshops and Rapporteur-General who took part in editing the draft of the VAT Decree and later served as the first and only Secretary to the VAT Technical Committee

30 Chief David Ajibola Olorunke was appointed pioneer President of the Chartered Institute of Taxation (CITN) and Director-General of the Ministry of Finance

31 The World Bank and IMF who stated that any rate below 10-15% was uneconomic

opposed the rate. Any revenue surplus to be generated from the imposition of VAT required an optimum rate of 10% and 17.2% thus, Ghana followed this advice and imposed a rate of 17.2% in 1996 but this led to widespread riots and consequent abandonment of the tax until its reintroduction later

32 The Committee set up in 1993 by the Federal Government to formulate the proposal for the implementation of VAT was termed the Modified VAT Committee

33 Dickson E. Oriakhi & Rolle R. Ahuru "The Impact of Tax Reform on Federal Revenue Generation in Nigeria"@www.arabianjbmr.com Accessed June 14, 2015

34 With the inauguration of the FIRS Board on January 16, 2020 by the Minister of Finance, Budget and National Planning, Ms Zainab Ahmed, the Chairman of FIRS hopes to reposition FIRS for better service anchored on four cardinal pillars – rebuilding FIRS Institutional Framework, robust collaboration with stakeholders, building a tax payer-centric institution and also, a data-centric institution

35 Teju Somorin, "Enhancing VAT Voluntary Compliance" *Business Day* Wednesday 21 January 2015 p. 39 Also www.businessdayonline.com

36 As at 2001, there were 68 banks designated by the FIRS. This arrangement had its short comings such as late or non-remittance, incomplete documentation and other sharp practices

37 This enrolls a VATable person and confers him with the authority to issue VAT Invoices to third parties. The Form is divided into two parts. Part A gives the details of name, business place, tax identification number, date of incorporation, nature of business/ types of goods and services and date of commencement of business while Part B deals with certification that is, attesting to the correctness of the information given. This must be signed by the principal officer, stamp affixed and dated

38 This form is used to render assessment and monthly returns. On receipt of this, the VAT Officer checks it for accuracy and sends it for filing

39 This is a bank document used for entering the particulars of payment. It shows the name and branch of the designated bank, the type of FIRS account - VAT Account, the date of payment, relevant VAT Office, VATable person, his address and VAT registration number, amount of tax paid etc.

40 This was dated August 20, 1993 and in the 9th Clause described a VATable person as person who trades in VATable goods and services for a consideration. A VATable person includes a sole proprietor, a professional, a partnership or a body of individuals having a recognizable identity. This circular is a follow up on the FIRS published booklet on "What You Should Know about VAT" which defines a VATable person as a person who independently carries out in any place an economic activity as a producer, wholesaler, trader, supplier of services or person exploiting tangible property for the purpose of obtaining income by way of trade or business

41 This lists the financial VATable services, which include commission on turnover, ledger fees, bank charges for cheque books, commission on documentary credit import and credit export etc.

42 To resolve the problems experienced by importers of goods at the ports as well as the urgent need to bring together all the budget pronouncements as they affect VAT

43 Why does Nigeria have a uniform rate rather than a discriminatory rate in relation to volumes of transactions? Originally, zero-rate was in the law but since it will result in refund, the 2007 Act provided for refund to be paid into the Consolidated Fund under the Constitution. Also, the VAT Act did not provide for threshold, which has been

provided by the Finance Act 2019. This aligns to the ECOWAS Protocol. Again the Act does not contain any waiver but in practice some companies were granted waivers by the Ministry of Finance through the then Minister Nenadi Usman. This has changed because the amended law provided for waiver

44 This was wrong because the rate was no longer in the regulation but a provision of a section, which could only be amended through Legislative Process by the National Assembly. This was resisted by the populace and returned to 5%. Economy Watch @ www.economywatch.com Accessed April 8, 2015

45 According to Bretton Woods Institute, there was an urgent need for a comprehensive economic reform to expand Nigeria's non-oil tax revenue

46 The Nigerian Tax and Fiscal Law known, as the Finance Bill is the first bill accompanying an Appropriation Bill since return to democracy in 1999. It seeks to promote fiscal equity, align domestic laws with global best practices, support Micro, Small and Medium-sized (MSMs) Businesses and increase government revenues and stakeholders' investments. It was a major aspect of the initiatives suggested by the Presidential Enabling Business Environment Council (PEBEC) and the National Tax Policy Implementation Committee to cure deficiencies of major tax legislation and originally introduced in 2016 / 2017 by the Finance minister, Mrs. Kemi Adeosun

47 The Finance bill faced challenges in the 8th Assembly owing to conflict between the Executive and the Legislative arms of government in the first tenure of President Muhammadu Buhari and also, owing to the choice of a Communication Tax Act over VAT Act amendment

48 Kabir M. Mashi, *Compendium of Tax and Related Laws* (Abuja: Federal Inland Revenue Service (FIRS), 2012) 717

49 Increase in rate would increase government revenues while also increasing the financial burden on taxpayers. The rate of 7.5% is still the lowest in Africa as South Africa is 15%, Ghana – 12.5%, Kenya – 16%, Egypt – 14%, Rwanda – 18% and Senegal – 18% etc.

50 Goods are all forms of tangible property that are moveable but do not include securities. The question is.. Are shares not tangible properties? The definition also extends to tangible asset or property over which a person has ownership or rights, derives economic benefits or can be transferred. With this extension, it appears shares are subject to VAT payment

51 This is defined as "Service rendered within or outside Nigeria by a person resident in Nigeria to a person outside Nigeria"

52 This exemption reduces tax compliance of small businesses

53 Basic food item include – additives (honey), bread, cereal, cooking oils, culinary herbs, fish, flour and starch, fruits (fresh and dried), live or raw meat / poultry, milk, nuts, roots, salt, vegetables, water, locally manufactured sanitary towels, pads or tampons, tuition relating to nursery, primary, secondary and tertiary education etc.

54 It contains a proviso to ensure that such assets are not sold by the acquiring company within 365 days after the date of restructure

55 Which requires recipients of goods and services supplied in Nigeria to self-account for VAT on goods purchased for non-residents. This extinguishes the controversy as to the application of VAT on services provided by non-resident companies to Nigerian resident companies and upholds the FIRS stand on reverse charge mechanism

56 By section 43 (5), the FIRS may issue guidelines for the purpose of giving effect to the

Finance Act, 2020

57 Goods means all forms of tangible properties, moveable or immovable excluding land, buildings, money and securities while services mean anything other than goods or services provided under a contract of employment etc.

58 Requiring administrative notes, enlightenment and implementation guides. Businesses and investors should seek professional advice and guidance to enable them understand the impact of the Finance Act on their business operations including compliance requirements

59 Registration threshold is a means by which small firms are protected from the problems of VAT. It is a way of simplifying VAT administration in relation to turnover for example, in the UK, a business must register to pay VAT when the value of its taxable supplies exceeds £82, 000 per annum. The threshold is based on the total of everything sold that is VATable. Likewise in Ireland, a trader whose turnover exceeds of €75,000 must be registered. Https://www.gov.uk/VAT-registration/when-to-register Accessed 18/4/15

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61. *Ibid.*

62. S. A. Adereti, *et. al.,* "Value Added Tax and Economic Growth of Nigeria", (2011) *European Journal of Humanities and Social Sciences,* vol. 10,no. 1, p. 4, available at http://www.journalsbank.com/ejhss_10_4.pdf (last accessed March 4, 2015). See also John C. Onwuchekwa, *et. al.,* "Value Added Tax and Economic Growth in Nigeria" (2014),*European Journal of Accounting, Auditing and Finance Research,* vol.2,no.8, pp.62-69 at p. 62, available at http://www.eajournals.org/wp-content/uploads/Value-Added-Tax-and-Economic-Growth-in-Nigeria.pdf (last accessed March 04, 2015).

63. L. Soyode, *et. al., Taxation – Principles and Practice in Nigeria,* (Ibadan: Silicon Publishing Company, 2006), quoted in Angus O. Unegbu, *ibid.*

64. *Ibid.*

65. Financial Dictionary, "Value Added Tax (VAT) Definition and Example", available at http://www.investinganswers.com/financial-dictionary/tax-center/value-added-tax-VAT-2335(last accessed March 05,2015).

66. *Ibid.*

67. *Ibid.*

68. Legal Service India, "Analysis of Value Added Chain Value Added Tax in India", available at http://www.legalserviceindia.com/articles/VAT_VAT.htm (last accessed August 13, 2015).

69. Indian Infoline Limited, "Understand the Basic Concepts of VAT", available at http://www.indiainfoline.com/article/research-articles/understand-the-basic-concepts-of-VAT-45946516_1.html (last accessed March 05, 2015).

70. *Ibid.*

71. See generally "VAT Definitions and Concepts", available at http://www.finance.gov.bw/VAT/definitions&concepts.html and Ministry of Finance and Economic Planning, "VAT Concepts", available at http://www.finance.gov.vc/index.php?option=com_content&view=article&id=74&Itemid=94 (last accessed March 05, 2015).

72. "Value Added Tax Act, vol. 15, Cap VI LFN 2004, s. 4.

73. *Ibid*., Part III of the First Schedule.
74. *Supra,* note 63.
75. *Supra,* note 64*,* Part I of the First Schedule.
76. *Ibid.,* Part II of the First Schedule.
77. *Supra,* note 65.
78. *Ibid.*
79. *Ibid.*
80. Fast Lane International, "What is a Taxable Person?", available at http://www.wedelivertheworld.co.uk/courier-services/faqs/what-is-a-taxable-person (last accessed March 05, 2015).
81. *Supra,* note 64*,* s. 12.
82. *Ibid.*
83. *Supra,* note 63.
84. *Ibid.*
85. *Supra,* note 64*,* s. 11.
86. *Supra,* note 63.
87. *Ibid.*
88. VAT Club, "Funding or Consideration: It Makes a VAT Difference", available at https://www.linkedin.com/grp/post/4415648-110386293 (last accessed March 06, 2015).
89. *Ibid.*
90. *Ibid.*
91. *Ibid.*
92. *Supra,* note 64, s. 13A.
93. *Ibid.* A tax invoice shall contain the following: tax payers identification number; name and address; VAT registration number; the date of supply, name of purchaser or client; gross amount of transaction; tax charged and rate supplied.
94. *Ibid.*
95. Classle, "Difference between VAT and Sales Tax", available at https://www.classle.net/book/difference-between-VAT-and-sales-tax (last accessed March 06, 2015).
96. Thomson Reuters, "Sales Tax Versus Value Added Tax-Calculation and Compliance Differences", available at https://tax.thomsonreuters.com/blog/onesource/VAT-gst-management/sales-tax-vs-value-added-tax-calculation-and-compliance-differences (last accessed August 14, 2015).
97. *Supra,* note 91.
98. *Ibid.*
99. *Supra,* note 92.
100 Divya Gandhi, "Point of Difference between VAT and Sales Tax", available at http://taxpaisa.com/difference-between-VAT-and-sales-tax (last accessed March 06, 2015).
101 Robert Morello, "Difference between VAT and Sales Tax", available at http://smallbusiness.chron.com/difference-between-VAT-sales-tax-56577.html (last accessed March 06, 2015).
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103 *Ibid.*
104. Supra*,* note 91.

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108. Winmark Business Solutions, "Types of Sales Taxes", available at http://www.wbsonline.com/resources/types-of-sales-taxes (last accessed May 12, 2015).
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112. Business Owners Tool Kit, "Understanding Your Sales Tax Obligations", available at http://www.bizfilings.com/toolkit/sbg/tax-info/sales-taxes/understanding-sales-tax-obligations.aspx (last accessed June 26, 2015).
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114. *Ibid.*
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116. Stephen Smith, "The Major Taxes: Economic Issues (3) Value Added Tax (VAT)", p. 4, available at http://www.ucl.ac.uk/~uctpa15/Econ7008_slides4.pdf (last accessed March 09, 2015).
117. *Ibid.*
118. Wikipedia the Free Encyclopedia, "Turnover Tax", available at http://en.wikipedia.org/wiki/Turnover_tax (last accessed March 09, 2015).
119. *Ibid.*
120. Art right, "Turnover Tax", available at http://www.artright.co.za/artbusiness/money-management/tax/turnover-tax (last accessed March 09, 2015).
121. *Ibid.*
122. *Ibid.*
123. Generally, VAT is on the final consumer. However, this is true according to the Economist from the monopolist view but from the retailer view, it may not be on the final consumer
124. In 1995, VAT yield was N21b against the projected N12b. In 1996, it was N32b against the projected N22b, in 1997; it was N35.3b against the projected N35b. In 1998, it was N37.6b against the projected N40b. In 1999, it was N47.7b against the projected N50b. In 2000, it was N58.0b, in 2001, it was N91.7b and in 2002, the projection was N90b while revenue collected was N108.6b. In 2003, it was N136b, 2004, it was N163.4b, 2005, it was N192.7b, 2006, it was N232.7b, 2007, it was N314.5b, 2008, it was N401.7b, 2009, it was N481.4b and 2010, it was N564.9b. 2011, it was N4.628 trillion…by 2018 and 2019, total collection was N992.8b and N542.4b, respectively. As at quarter 4 of 2020, VAT yield is N454.69 billion despite the COVID-19 Pandemic
125. Tamunonimim A. Ngerebo& M. Masa, "Appraisal of the Tax System in Nigeria (A Case study of VAT)"@www.rjopes.emergingresource.org. Accessed April 9, 2015
126. Patrick Ezeagu, "New VAT Regime: Stakeholders Demand Waivers, Exemptions and Infrastructure" Available@www.Punchng.com Accessed January 20, 2020
127. It is possible to adopt the Presumptive Tax Method to distribute the burden of VAT
128. NTLR (2010) p. 22

129. *Supra*
130. *TSKJ 11 ConstrucesInternacionalsSociodadeUnipessoal LDA v FIRS* [2014] TLRN (Vol.13) 1; *NNPC v. TAT* [2014] TLRN (Vol. 13) 39 and *Standard Trust Bank Plc v. Chief Emmanuel Olusola* [2007] CLRN 41
131. Resulting in the Federal Government receiving N234,200,000, FCT N12,160,000 and States N960,640,000
132. In 1995, revenue increased to N21b, N32b in 1996 and N35.3b in 1997 with corresponding formula of 50%, 35%, and 25% respectively and 40% in 1998 to the Federal Government with the States receiving 25%, 40%, 45% and 35% respectively. The share of the Local Governments rose from 0% in 1994 to 25% in 1995 and 35% in 1999
133. (2008) All FWLR (Pt. 398) 235
134. The Supreme Court in the case of *Aberuagba v. AG, Ogun State* (1997) 1 NRLR (Pt. 1) 51 underscored this. Lack of clarity also manifested in the case of *CNOOC v. AG Federation* NRLR 1 [2013] 88 where the argument was whether the 3rd Defendants contract rights in the Production Sharing Contract (PSC) constituted either goods or services owing to ambiguity in the VAT Act. The Court held that it did not constitute goods and services but however, agreed that the Act should be amended to define intangible rights as VATable as was done in the UK VAT Act, 1994. Also, in deciding who is a taxable person, the Court held in *FBIR v. Cadbury Nigeria Plc* NRLR 2 [2013] 184 that overseas company doing business through its subsidiary in Nigeria would pay VAT. The challenge is, when there is lack of clarity in the laws, it leads to discretion which is subjective and may create greater difficulty in making decisions that control consumption patterns
135. Sijbren Cnossen, "Administrative and Compliance Costs of the VAT: A Review of the Evidence" *Tax Notes Int'l,* June 20, 1994 p.1649 TNI 118-9
136. Okoye E. I. & Egbegi D. O. "Effective Value Added Tax: An Imperative for Wealth Creation in Nigeria"@http://globaljournals.org Accessed June 14, 2015
137. This is where a destination based VAT system adopts one tax rate and zero rates. Owing to destination rate, all exports are zero-rated and the system becomes a dual-rate. In view of the refund involved in zero-rating exports, it is expensive to operate
138. The EU favours multiple rates with a minimum rate of 15%, which allows adjustments and derogations. The main reason for the multiple rates was the desire to alleviate the tax on goods and services that forms a larger share of expenditures of the poorest households. Other countries included Algeria 7% & 17%, Belgium with 12.5% & 21%, Bulgaria with 7% & 20%, Croatia with 10% & 23%, France 5.5% & 19.6% and Cote D' Ivoire with 18% & 20%. Nigeria adopted a double rate consisting of 5% & zero-rate for exports. The zero-rated items are non-oil exports, goods and services purchased by Diplomats and goods purchased for use in humanitarian funded projects
139. In New Zealand, the 1986 VAT Reform introduced a broad-based VAT with a low single standard rate, a low registration threshold and few exemptions. South Africa implemented a VAT in 1991 that allows the New Zealand Model however, at inception; it is zero-rated for basic food items. Singapore introduced VAT in 1994 with a broad based single rate and high threshold registration. Australia introduced in 2000 with a wide base and a number of zero- rates for health and medical care, educational supplies and childcare, food and beverages
140. South Africa has 15%, Rwanda 18%, Senegal 18%, Uganda 17%, Cameroun 18.7%,

Chad 18%, Kenya 16%, Gabon 18%, Ghana 12.5%, Mauritius 15%, Morocco 20%, Zambia 17.5% and Lesotho 14%

141. The Draft Chapter chaired by the Nobel Prize Winner Sir James Mirrlees and commissioned by the Institute for Fiscal Studies recommended that moving to a single VAT rate would not only raise revenues but would also cut administration costs. Single rate is also favoured by the fact that it is assumed that the poorest households spend a high proportion of their income on essentials

142. Ghana is 4.60%, Benin – 6.60%, Kenya – 4.20%, South Africa – 7% and ECOWAS average is 6.70% according to the Ministry of Finance, Budget and Planning 2020 Budget Presentation to the National Assembly

143. Ikeji Chibueze C. "Politics of Revenue Allocation in Nigeria: A Consideration of Some Contending Issues" *Sacha Journal of Policy & Strategic Studies* Vol. 1 No. 1 (2011) pp. 121-136

CHAPTER 2

VALUE ADDED TAX: A REVIEW OF VAT THEORIES

Abstract
Value Added Tax (VAT) is among the widely used tax instruments in the world; in particular, it is often resorted to as an efficient means of raising revenue. VAT is a general consumption tax imposed on all commercial activities involved in the process of producing goods or rendering services. In recent years, proposals for the adoption of value added tax have been made with increasing frequency. Existing literature shows that there is no general theory of value added tax. What could be done is that modifications to existing tax structure can be used to model the effect of value added tax in an economy. Therefore, this chapter examines the theoretical foundations of value added tax within the macroeconomic set-up with activities in the demand and supply sides of the economy, making provision for the role of government in regulating economic activities through tax.

1. Introduction

VAT is often associated with a multi-stage tax that is levied on the value added by each business firm at every stage of production and distribution of goods and services. VAT is intended to tax personal consumption comprehensively, neutrally, and efficiently. One of the widely used tax instruments in the world, it is often employed as an efficient means of raising revenue. Indeed, VAT has become an important source of government revenue in Nigeria. VAT is a general consumption tax designed to be imposed on all commercial activities involved in the process of producing goods or rendering services[1]. VAT is a generic name associated with multi-stage tax that is levied on the value added by each business firm at every stage of production and distribution of goods and services.

VAT was introduced in Nigeria, following the report of a study group set up by the federal government during the regime of the military president, General Ibrahim Badamosi Babangida in 1991, to complement the financial resources needed for government development project. The promulgation of the VAT decree became effective from 1st December, 1993 as a replacement for sales tax, which had been criticised for its non-performance. In a nutshell, the introduction of value added tax became necessary because government expenditure was steadily overshooting revenue, resulting in deficit financing.

More specifically, the reasons behind replacing the Sales Tax Decree No.7 of 1986 with the VAT Decree No.102 of 1993 are as follows:

I. *The incidence of tax is on the consumer when the price is high; thus, introducing VAT improves the fairness in tax system to ensure that people pay in line with their ability to purchase goods and services.*

II. *The introduction of the principles of consumption tax in Nigeria is expected to cut across consumable goods and services; hence, the base of VAT has been broadened against the nine categories of goods and services covered by sales tax. This expanded tax base has the capacity to increase government revenue.*

III. *To lower the personal income tax burden of low-income earners without necessarily reducing revenue earned by government but by redistributing income.*

IV. *VAT is easy to administer and difficult to evade.*

V. *Revenue from VAT provides a fairly accurate measure of growth in the economy, since purchasing power increases with economic growth.*

VI. *VAT reduces the dependence on revenue from oil in Nigeria.*

VII. *VAT increases when the earning power of the population rises, which reflects the business well-being of the country.*

Above all, the major reason for the replacement of Sale Tax with VAT is to enhance the income level of government.

2. Systems of Tax – Who Pays What?

In Adam Smith's famous book, *The Wealth of Nations*[2], one of the "Canons of Taxation" states that a tax should be linked to "ability to pay". VAT does not adhere to this because the amount of VAT on a particular commodity is the same for everyone, irrespective of what they earn.

Systems of taxes are based on the two major components of tax - tax rate and tax base. Tax rate is the amount of tax (usually expressed as a percentage) which is levied per unit of base, e.g., 10% of personal income or ₦1000. The tax base is the object that is taxed, i.e., the object upon which a tax is levied. Thus, the total amount of tax is equal to the rate multiply by the base, i.e.,

$$T = R' \ B \text{ Or } B = \frac{T}{R},$$

Where R represents the rate, B represents the base and T represents the amount of tax.

Progressive Taxation

Progressive tax exists when the tax rate (R) increases as the base (B) increases. In other words, a tax is progressive, if the ratio of tax to income increases as income rises, that is, tax takes an increasing proportion of income as income rises. It increases more than proportionately with income. An example of this tax is Pay as You Earn (PAYE). Income taxes are progressive in nature, e.g., if a ₦2,000 income base is taxed at 2 per cent, a ₦20,000 income may be taxed at 4 per cent, a ₦40,000 income at 8 per cent, and so on. We may note that since progressive taxation helps to redistribute income, it is said to be basically

equitable.

The degree of Progressive tax is principally measured in three ways, as follows:

I. The average rate progression (the ratio of change in effective rate to change in income).
II. The liability progression (the ratio of percentage change in liability to percentage change income).
III. The residual income progression (the ratio of percentage change in after-tax income to percentage change in before-tax income).

When applied to discrete income intervals, the corresponding formulae are:

$$\text{a.} \quad \frac{\frac{T_1}{Y_1} - \frac{T_1}{Y_0}}{Y_1 - Y_0}$$

$$\text{b.} \quad \frac{T_1 - T_0}{T_0} \div \frac{Y_0}{Y_1 - Y_0}$$

$$\text{c.} \quad \frac{(Y_1 - T_1) - (Y_0 - T_0)}{(Y_0 - T_0)} \div \frac{Y_0}{Y_1 Y_0},$$

Where Y_0 and Y_1 are the lower and higher levels of income and T_0 and T_1 are the corresponding tax liabilities.

Graphically, progressive taxation can be represented as in Figure 1 below.

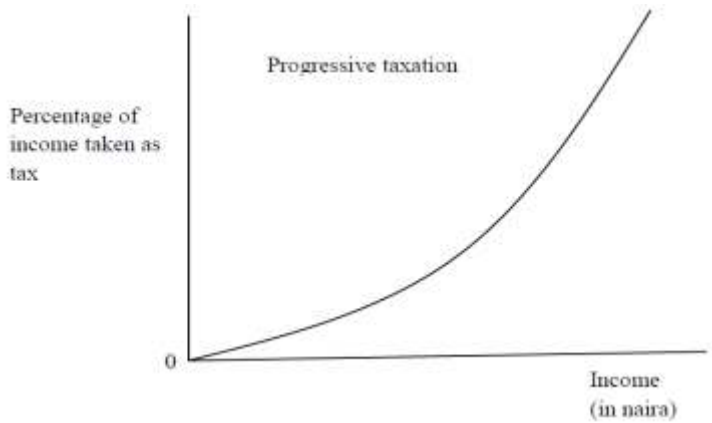

Figure 1: Progressive Taxation

Arguments in Favour of Progressive Taxation

I. It conforms with the ability-to-pay and equal-sacrifice principles.
II. It is a stabiliser in a market economy.
III. It is advocated on the grounds of social justice, as manifested in payment of tax according to the taxpayer's financial capability, i.e., ability to pay.
IV. It is administratively convenient.

V. It is helpful in mitigating the ill effects of social and political unrest, weak health and low productivity of the masses, and misuse of the nation's productive resources.

Proportional Taxation

Proportional tax is a tax where the percentage of income paid in taxation always stays the same. In other words, the average rate of taxation is constant. In term of tax rate and tax base, the tax rate (R) remains constant as the base (B) increases. A tax is proportional, if the ratio of tax to income remains constant when moving up the income scale; that is, it is a tax, which is levied at the same rate at all income levels. Hence, each person pays the same proportion of his income, irrespective of the amount of his/her income. For example, a person on ₦2,000.00 income base per annum pays 10 per cent (₦200.00) and another person on ₦20,000 income base per annum pays 10 per cent (₦2,000.00). This system of taxation is not equitable, since it fails to redistribute income in favour of the poor.

Graphically, proportional taxation can be represented as in Figure 2 below.

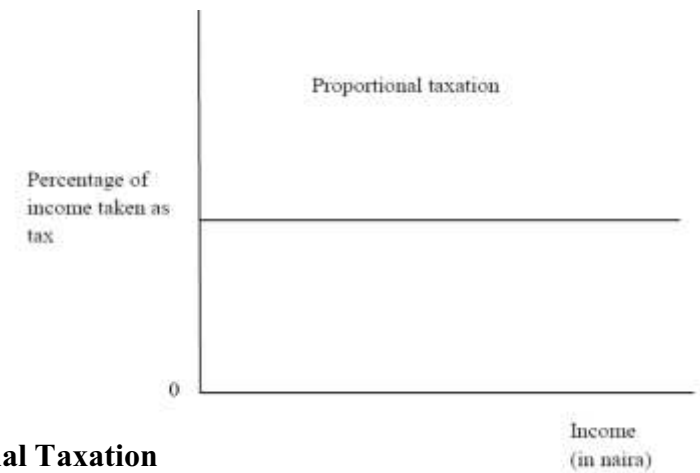

Figure 2: Proportional Taxation

Arguments in Favour of Proportional Taxation

I. Proportional taxation is a solution to our inability to decide upon a precise and appropriate degree of progression.
II. Proportional taxation is easily decided and enforced, especially when a complicated rate schedule and a degree of progression in each tax is not to be worked out.
III. It does not change the relative position of different taxpayers. It is neutral in terms of the allocation of resources of the economy to different uses.

Regressive Taxation

Regressive tax is a tax that represents a smaller proportion of a person's income as income rises. In other words, the average rate of taxation falls. Regressive taxation occurs when the tax rate (R) decreases as the base (B) increases. A tax is regressive, if the ratio of the tax to income declines when moving up the income scale; that is, the proportion of tax decreases as

income rises. Under this system of taxation, a higher amount is taken from the poor than from the rich. The rich pays a lesser proportion of his/her income as tax than the poor. An example is poll tax, where tax payers are required to pay a flat amount, say, ₦15.00. In this sense, an individual on an income base of ₦500.00 pays ₦15.00, or 3 per cent, while another on an income base of ₦2,000.00 pays ₦15.00, or only 0.75 per cent.

Other regressive taxes are property tax and consumption or sales tax. As the term, regressive tax implies, it works against the poor in the society. It can be graphically represented, as shown in Figure 3 below.

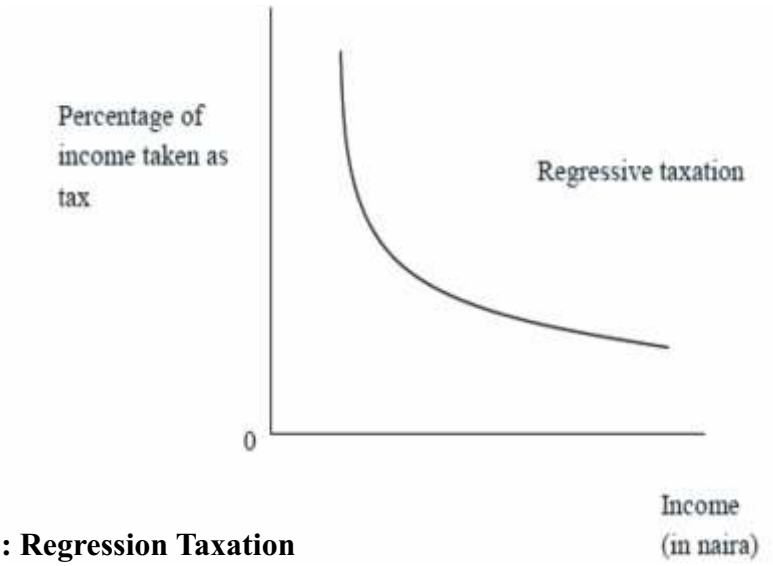

Figure 3: Regression Taxation

Degressive Taxation

A tax is a degressive tax, if the tax rate (R) increases at a decreasing rate, as the base increases, that is, if the acceleration rate becomes constantly less as the base increases. It can be graphically represented as in Figure 4 below.

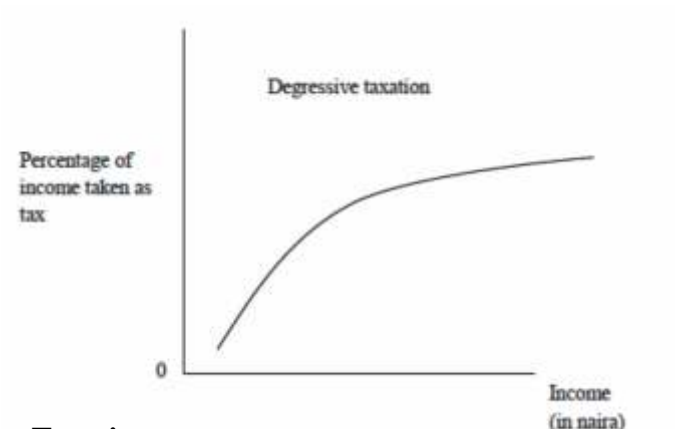

Figure 4: Degressive Taxation

3. Incidence of Taxation (Elastic or Inelastic Demand) – Who Pays How Much?

Incidence of tax refers to how the final burden of a tax is distributed. The incidence of tax can be direct or indirect. Incidence of tax is direct when the burden cannot be shifted, e.g., income tax. The amount of tax paid reduces the income of the taxpayer. In case of indirect tax, the final burden is distributed, and it depends on the elasticity of demand for the particular product. The burden of this tax can be shared between the producer and the consumer, or borne by either of them, e.g., purchase tax.

The burden of an indirect tax is very important and will vary according to the elasticity of demand for the product it is imposed on. If the demand for the good is very elastic (very responsive to price changes), then the price will fall significantly. Figure 5 below shows this.

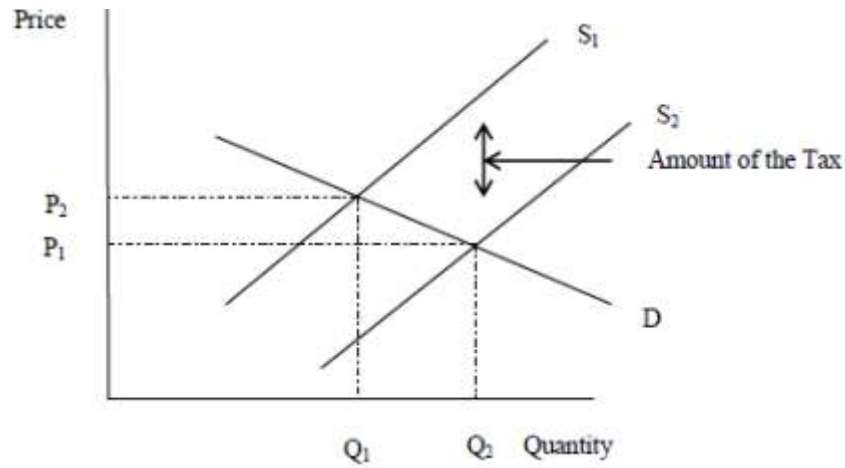

Figure 5 Elastic Demand

From Figure 5, we can see that the price has risen slightly, compared with the amount of the tax. The main burden of the tax has, therefore, fallen on the firm, as it is only compensated by a relatively small increase in price. The consumer has only suffered a fairly small price increase from P_1 and P_2. It is for this reason that indirect taxes are generally not levied on goods with elastic demand, as the tax revenue would be relatively small.

Also, when demand for a product is perfectly elastic, the producer bears the full burden of the imposed tax. This can be shown in Figure 6 below.

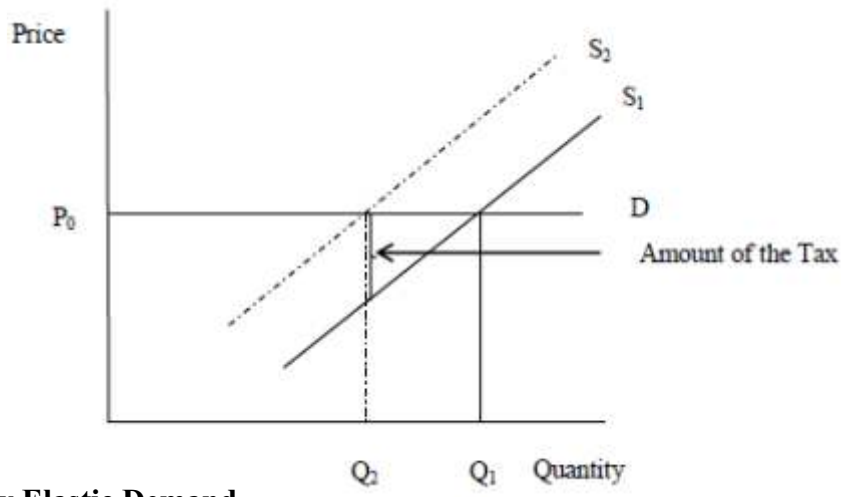

Figure 6 Perfectly Elastic Demand

In this case, we can see that, as a result of the imposed tax, supply shifts from S_1 to S_2, thus the quantity falls from Q_1 to Q_2, but the price remains at P. This is because the consumer will not buy the product at a slight rise in its price. Hence, the producer bears the entire burden of the tax.

In the case of goods with inelastic demand, the picture is very different because consumers are much less sensitive to price changes of these goods; the bulk of the tax can be passed on by the firm, as Figure 7 below shows.

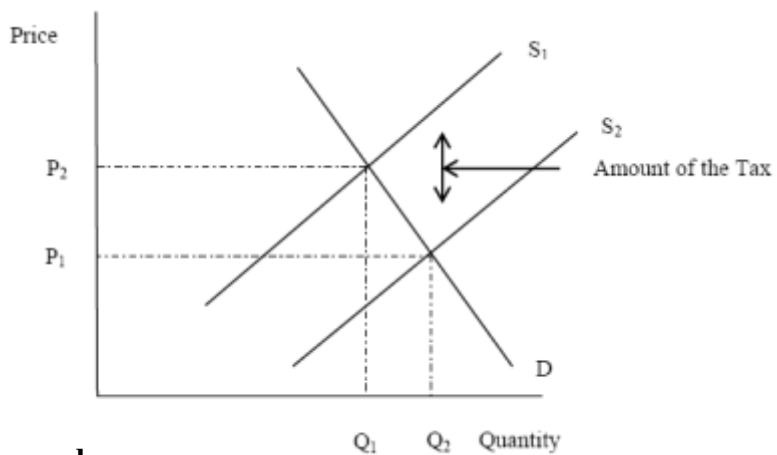

Figure 7 Inelastic Demand

Here, the quantity has only fallen very slightly, and the price has risen almost by the full amount of the tax. In fact, if the demand for the good had been perfectly inelastic, then all the tax could have been passed on as a price increase. Therefore, when the demand for a product is inelastic, the burden of the tax will fall on the consumer.

However, if the demand for a product is perfectly inelastic, the incidence of an imposed tax is borne by the consumer. This can be shown, as in Figure 8.

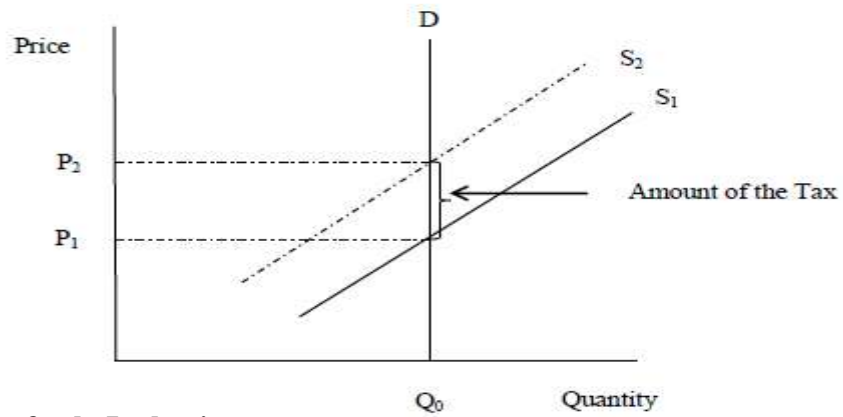

Figure 8 Perfectly Inelastic

Figure 8 shows that, with the imposition of tax, the supply curve shifts backward from S_1 to S_2 and price increases tax from $0P_1$ to $0P_2$. The quantity demanded remains unchanged at $0Q_0$. The full amount of the tax is shifted to the consumer because this rise in price does not affect the quantity demanded.

4. Indirect Tax – What Happens to Market Prices?

Indirect taxes are taxes that are levied upon commodities before they reach the consumers who ultimately pay the taxes as part of the market price of the commodity. There are two major types of indirect tax: per-unit tax and ad-valorem tax. A per-unit tax is one where the amount charged is always the same on each unit. An ad-valorem tax, by contrast, is one where the tax is charged as a percentage of the value of the goods. This is where VAT comes in at its current rate of 7.5 per cent[2] of the value of the goods.

The effect of indirect tax on the market equilibrium will be slightly different for each of these two types of tax. In the case of per-unit tax, this tax will be paid to the government by the firm and will, therefore, shift the firm's supply curve. To be willing to supply the same quantity as before, the firm will now aim to set a price commensurate with the tax imposed. The tax has, therefore, shifted the supply curve vertically upwards by the amount of the tax. The impact of this on the market is shown in Figure 9.

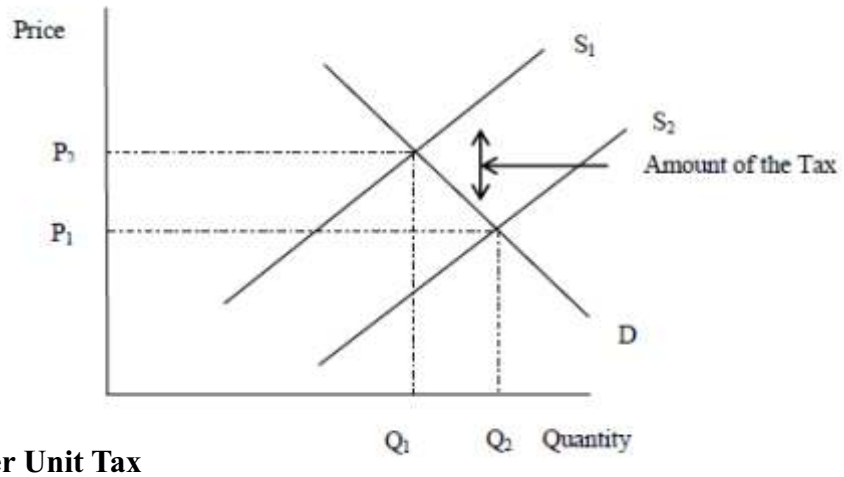

Figure 9 Per Unit Tax

As we can see from the diagram, the equilibrium price has risen, and the equilibrium quantity has fallen. The extent to which this happens depends on the elasticity of demand for the good.

In the case of ad-valorem tax, the principles are the same, but the effects are very slightly different. The tax will still shift the supply curve vertically upwards, as the firm will want a higher price to compensate it to supply the same quantity. However, because the tax is a percentage of the value of the commodity, it will shift by different amounts, according to the price of the good. For example, the VAT on a good costing ₦10 will be ₦0.75, but for a good costing ₦100, it will be ₦7.50. The effect of this is shown in Figure 10.

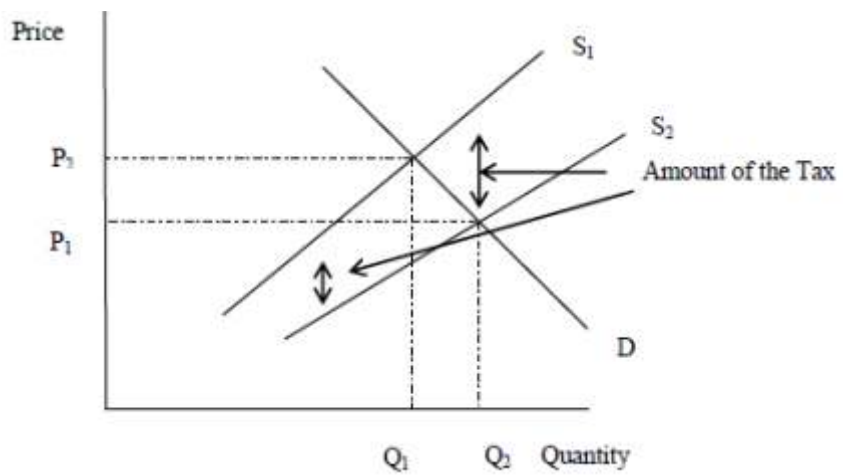

Figure 10 Ad-valorem Tax

The impact on the equilibrium price and quantity, therefore, depends on the amount of the tax.

5. Taxing Externalities – Why Tax?

Externality is the cost and benefit arising from any activity, which does not accrue to the person or organisation carrying on the activity. External costs, or diseconomies, constitute a damage to other people or the environment, for example, by radiation, river or air pollution, or noise, which does not have to be paid for by those carrying on the activity. External benefits or economies are effects of an activity, which are pleasant or profitable for other people, who cannot be charged for them, for example fertilization of fruit trees by bees, or the public's enjoyment of views of private buildings or gardens. The consumption of many goods can also be referred to as external costs, or negative externalities, because they affect people other than those consuming them. The costs to society (the social costs) are, therefore, the private costs and the external costs. These two together are the full cost to society.

The external costs of people's actions are often not taken into account by those people when they consume a product and, so, they will regard the product as cheaper than it really is. Take, for instance, smoking. The private cost of smoking to individuals is the financial cost, i.e., the amount they pay for their cigarettes. Therefore, there are further costs to society. These may include any medical cost because of smoking-related diseases, time (and, therefore, production) lost through illness, the possibility that passive smoking may cause an illness, and so on. Because people do not take these costs into account, they may over-consume the product, because it is seen as cheaper than it really is. This is shown in Figure 11.

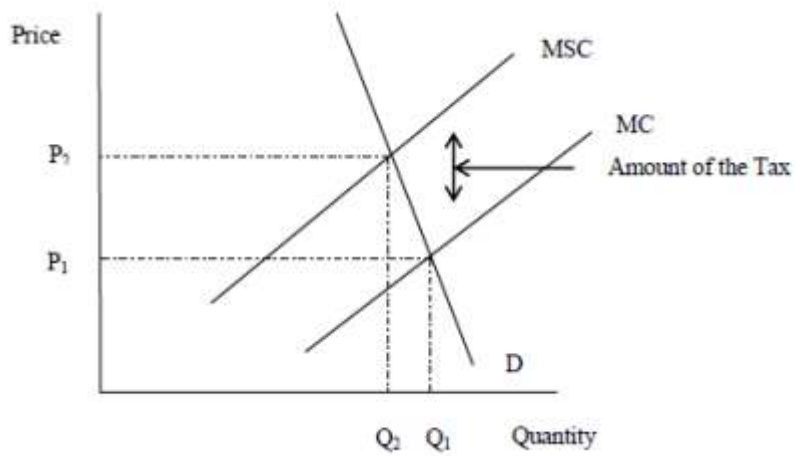

Figure 11 Externality Cost

The private cost of smoking is represented by the MC curve. If people take account of these costs, then they will consume Q_1. However, as discussed above, there are further costs – external costs – and these are shown by the gap between the MC curve and the MSC (Marginal Social Cost) curve. The MSC curve includes all costs. On the basis of all these

costs, people should only consume Q_2, as the presence of external costs will often lead to over-consumption of a good.

To cope with this problem and ensure that the optimum quantity of a commodity is consumed, the government may choose to tax the commodity. This tax can be arranged to be equivalent to the value of the external costs and will then increase the price by the required amount and, hopefully, ensure that the correct quantity is consumed (Q_2 in the diagram above). The main problem for government is how to assess accurately the value of the external costs and, therefore, set the value of the tax appropriately.

6. Conclusion:

Value added tax has been adjured as instruments employed around the world as an efficient means of raising revenue. The chapter has examined the various tax theories to understand the system of tax in establishing who pays what? It demonstrates this by looking at the implications of the various forms of taxation - progressive, proportional, regressive and digressive. It further illustrates the incidence of taxation to determined who pay how much. The effect of market equilibrium was discussed using per unit tax and ad-valorem tax to demonstrates what happens to market price. The chapter also reviews the taxing externalities to illuminate the cost and benefit arising from any activity of the taxpayers in relation to the relationships that exist between price and quantity.

7. Recommendations:

It is observed that theories are usually very useful in determining the effect and incidence of tax on the taxpayer. On this strength the chapter advocates for deep and through analysis of that effects by policy makers in formulation of viable and efficient tax policy.

The chapter further recommends that in formulating the VAT policy the issues relating to externality needs to be considered to ensure that the cost associated with such goods and services.

The tax base of a gross domestic product VAT is goods and services included in gross domestic products, e.g., personal consumption and capital goods (GDP also takes into account government consumption and gross investment, as well as the net of exports over imports). Taxpayers are not allowed an input credit (or other adjustment) for the VAT that they have paid on capital goods used in their business. This has the effect of affecting the extent of determining the value of consumption and investment.

Income-style VAT: The tax base of an income VAT is the tax jurisdiction's net national income. Taxpayers are allowed an input credit(or other adjustment) for the VAT that they have paid on inputs, including capital goods used in connection with their taxable business activity, but they must spread the credit on capital goods over their useful lives through a depreciation-like allowance.

ENDNOTES

1. Section 2 of VAT Act, CAP VI, LFN 2004 as amended, and was further amended pursuant to s. 40 of the Finance Act 2020
2. Smith, A. [1776] (1904). An Inquiry into the Nature and Causes of the Wealth of Nations by Adam Smith, edited with an Introduction, Notes, Marginal Summary and an Enlarged Index by Edwin Cannan, London: Methuen, 2 Vols.

CHAPTER 3

A REVIEW OF AMENDMENTS TO THE VAT ACT: 1993 - 2015

Abstract

Generally, tax laws remain the legal instrument which a tax administrator uses, as the basis of authority, to administer the tax policies of a country. Nigerian tax laws, like those of other countries, do undergo changes, almost on an annual basis. Such amendments are often so numerous that even the tax experts get confused in applying them. All tax laws and their amendments play significant roles in transforming the Nigerian tax system in one way or the other, as they introduce changes each time they are enacted or amended. This chapter seeks to trace all the amendments made to the principal ***Value Added Tax (VAT) Decree No. 102 of 1993 (VAT Act)*** *since its enactment up to date. Indeed, between the enactment of the VAT Act in 1993 and 2015, there have been over forty amendments to it.*[1] *The first six amendments, which took place during the military era, were done by the Finance (Miscellaneous Taxation Provisions) Decrees. Given our 2015 timeframe, the most recent amendment to the VAT law is the* ***Value Added Tax (Exemption of Commissions on Stock Market Transactions) Order, 2014****, released via an Official Gazette, dated 30th July, 2014. The effects of each of the amendments on the shape of the law were also treated in the chapter. Essentially, the VAT law today is a clear departure from its original intention, as many provisions have been altered by way of amendments. This Chapter concludes with a postscript that many of the gaps have been filled by amendments through Finance Acts 2019 and 2020.*

1. ORIGINAL VERSION OF THE VALUE ADDED TAX DECREE, No. 102, 1993

It is trite that the Value Added Tax Decree No. 102 of 1993, introduced VAT into Nigeria.[2] Signed into law by General Babangida,[3] on 24th August 1993, the VAT Decree repealed the then Sales Tax Decree.[4] The VAT Decree took effect from 1st December, 1993, although its administration was delayed until 1st January, 1994 when invoicing for tax purposes began.

The original Decree was in six parts, made up of 43 sections; in addition, there were three schedules. The Decree imposed VAT on certain goods and services, including all goods manufactured and assembled in Nigeria.

Part I of the Decree, made up of six sections, was mainly about the Imposition of the VAT. Other issues covered were Taxable Goods and Services and Rate, Goods and Services Exempt, Computation of tax, values of taxable goods and services, as well as value of imported goods.

The Administration of the law was contained in Part II. It had only three sections, which focussed on Registration, Records and accounts.

Returns, Remittances, Recovery and Refund of Tax were dealt with in Part III. Other issues included payment of tax by taxable persons, collection of tax by taxable persons, effect of failure to render returns and effect of non-remittance of tax.

Part IV, in four sections, was entirely devoted to Value Added Tax Technical Committee, focussing on its establishment and composition, Functions, Proceedings and Staff.

Offences and Penalties were contained in Part V, specifying offences, such as furnishing of false documents, evasion of tax, failure to notify change of address, failure to issue tax invoice, resisting an authorised officer, failure to register, failure to keep proper records and accounts, failure to collect tax, failure to submit returns, etc.

Part VI was on Miscellaneous issues. Sections 34 - 43 dealt with issues, such as Power of Secretary to vary schedules, Distribution of Revenue, Appointment of Agent for manufacturer or importer, Signification, Forms, Regulations, Repeal of Sales Tax Act No. 7 of 1987, Interpretation, Citation and Commencement.

There were three Schedules to the original law. Schedule 1 had 17 Taxable Goods. Schedule 2 listed 24 Taxable Services. The Rate of Tax was specified in each. Schedule 3 was divided into two parts, namely: Part I- Goods Exempt, and Part II - Services Exempt.

A. Amendments to the VAT Decree: 1994 – 1999 & Other Allied Developments

The Decree has undergone several amendments, the first being the three consecutive amendments in 1996. The three were gazetted in the Finance (Miscellaneous Taxation Provisions) Decrees No. 30, 31 and 32 (respectively) of 1996 of 23rd October, 1996.

The Finance (Miscellaneous Taxation Provisions) Decrees were omnibus Decrees, used in Nigeria during the tenure of the military to amend several tax laws simultaneously in a year. Instead of making separate laws for amending each tax law, whenever the need arose, the military rulers adopted the annual practice, whereby a single omnibus Decree was used to amend several tax laws simultaneously.

The six omnibus Decrees, which amended the VAT Decree, were as follows:

1. Finance (Miscellaneous Taxation Provisions) Decree No. 30 of 1996, issued on 23rd October, 1996;[5]
2. Finance (Miscellaneous Taxation Provisions) Decree No. 31 of 1996, issued on 23rd October, 1996;
3. Finance (Miscellaneous Taxation Provisions) Decree No. 32 of 1996, issued on 23rd October, 1996;
4. Part V, Finance (Miscellaneous Taxation Provisions) Decree No. 18 of 10th May 1998;[6]

5. Finance (Miscellaneous Taxation Provisions) (No. 2) Decree No. 18 of 1998; (Decree No. (19);
6. Part V, Finance (Miscellaneous Taxation Provisions) Decree No. 30 of 1999.

Subsequently, the VAT Added Tax Tribunals Notice, No. 25 of 2000, was released. The prior amendments are now discussed in further detail.

(1) Part V, Finance (Miscellaneous Taxation Provisions) Decree No. 30 of 1996.
These provisions made sundry amendments to sections 2, 8, 21, 22, 23, 26, 28 and 42 VAT Decree.

Section 8 was amended by substituting for the words "manufacturer, wholesaler, an importer and supplier of taxable goods or services", the words "a taxable person." In effect, the taxable person has compliance obligations under the VAT Decree. For example, the amended section 8 provided that where a taxable person fails or refuses to register with the Board, within the time specified, he shall be liable to a penalty of ₦10,000 for the first month in which the failure occurs; and ₦5,000, for each subsequent month in which the failure continued.

The phrase, "intent to deceive" were deleted from section 21, while the two words, "knowingly" and "fraudulent", were deleted from section 22. The Decree also deleted, in sections 23 and 28, the words "knowingly or intentionally" from the original provision. For example, the original section 33 was worded as follows: "*A person required to make an attribution, who knowingly or intentionally fails to do so, or having done so, fails to notify the Board, is liable to pay a penalty of ₦5,000."* Similarly, the original section 28 provided that a taxable person, "*who knowingly or intentionally fails to register under this Decree, is guilty of an offence and liable on conviction to a fine of ₦5,000, and if after one month, the person is not registered, the premises where the business is carried on shall be liable to be sealed up."*

(2) Part V, Finance (Miscellaneous Taxation Provisions) (No. 2), Decree No. 31 of 1996[7]
The Finance (Miscellaneous Taxation Provisions) Decree No. 31 signed on 23rd October, 1996, which came into effect retroactively from 1st January, 1995, amended sections 8A, 8B, 10(A), 12(1), 17, 36, 42, Item 8 of Part I of the Schedule and the insertion of Item 4 of the amended Schedule of Part 1V. It provided, amongst others, that:
(a) VAT shall be computed at the rate of 5% on the value of all taxable goods and services (section 4).
(b) Every Government Ministry, statutory body and other agency of Government shall register as agents of the Board for the purpose of collection of tax.(Insertion of new section 8A).
(c) Every contractor transacting business with a Government Ministry, statutory body and other agency of the Federal, State or Local Government shall produce evidence of registration with the Board as a condition for obtaining a contract. (Insertion of new Section 8B).

(d) A non-resident company that carries on business in Nigeria shall register for the tax using the address of the person with whom it has a subsisting contract, as its address for purposes of correspondence relating to the tax.

(e) A non-resident company shall include the tax in its invoice and the person to whom the goods or services are supplied in Nigeria shall remit the tax in the currency of the transaction. (Insertion of section 8A).

(f) Every Ministry, statutory body or other agency of Government shall, at the time of making payment to a contractor remit the tax charged on the contract to the nearest local VAT Office.
The remission shall be accompanied with a schedule showing the name and address of the contractor, invoice number, gross amount of invoice, the amount of tax and month of return**.** (Insertion of section 10A).

(g) Section 12(1) was amended by substituting for the words "14th day of the month", the words "30th day of the month[8].

(h) The Legal Adviser to the FIRS, omitted in the VAT Decree, was included in the membership of the VAT Technical Committee, and thus amended section 17.

(I) The VAT proceeds, as provided in section 36 of the VAT Decree, was amended as follows:
- 40% to the Federal Government (instead of the former 20%)
- 35% to the State Governments and the Federal Capital Territory, Abuja (previously 80%) and
- 25% to the Local Governments (formerly nil %)

(j) Section 42 provided new definitions as follows:
- *"'Agency of Government', includes a Ministry, Department, Statutory body, public authority and an institution of* the Federal, State and Local Government."
- Taxable goods and services mean *"the goods and services not listed in the Schedule to this Decree."*
- The words "*Other than a public authority acting in that capacity"* were deleted from the original definition of "Taxable person"[9].
- Definition of "taxable services"[10] was deleted.

(k) In the amended Schedule of Part I, immediately after item 7, the following new item, that is, "8
All exports", was inserted.

(l) Likewise, in the amended Schedule of Part II, immediately after item 3, the following new item,
that is, "4. *All exported Services*" was inserted.

(3) Part V, Finance (Miscellaneous Taxation Provisions) No. 3 Decree No. 32 of 1996

Decree, No. 32 of 1996, came into effect on 1st January, 1996.[11] The Decree amended sections 2, 10, 16, 16(2) and 16 (3), 36 and Second Schedule, VAT Decree.

By the insertion of new section 16(2) and (3), the VAT Tribunal replaced the Federal High Court as the initial forum for adjudication of all VAT cases. It inserted that a taxable person

who is aggrieved may appeal to the VAT Tribunal and provided for appeals from the VAT Tribunal to the Court of Appeal.

It further amended section 36 by substituting a new distribution formula as follows:
(a) 35% to the Federal Government (instead of former 40%)
(b) 40% to the State Governments (previously 35%)
(c) 25% to the Local Governments and Abuja (previously nil)

The Second Schedule was also amended to empower the Minister to *"establish by Notice in the Federal Gazette five Zonal VAT Tribunals spread geographically throughout the country".* The amendment provided elaborate provisions for the mode of conducting cases before the Tribunal. The modalities are specified in Paragraphs 2-20 of the Schedule.

(4) Part III, Finance (Miscellaneous Taxation Provisions) Decree No. 18 of 1998
The above Decree, No. 18 of 1998, came into effect retrospectively on 1st January, 1997.[12] The Decree inserted section 13A in respect of allowable input tax, also Items 8-12 to the re-numbered First Schedule, and paragraph 12 of the 2nd Schedule. It provided that the input tax, to be allowed as a deduction from output tax, shall be limited to the tax on goods purchased or imported directly for resale and goods, which form the stock-in-trade, used for the direct production of any new product on which the output tax is charged. Therefore, it made a grand error by providing as follows:

(2) Input tax—
(a) on any overhead, service, and general administration of any business which otherwise can be expended through the income statement (profit and loss accounts); and
(b) on any capital item and asset which is to be capitalised along with cost of the capital item and asset, shall not be allowed as a deduction from ***input*** *tax.*

It renumbered the Schedule in the VAT Decree as "First Schedule" and inserted the words "locally produced" after the word "fertilizer".
(b) After item 8, it inserted the following new Items 9, 10, 11 and 12:

"9. *Plant and machinery imported for use in the Export Processing Zone.*
10. Plant, machinery and equipment purchased for utilization of gas in downstream petroleum operations.
11. Tractors, ploughs, agricultural equipment and implements purchased for agricultural purposes; and
12. Water treatment chemicals."

The Second Schedule, which itself was inserted by the Finance (Miscellaneous Taxation Provisions) No. 3 Decree, 1996, was further amended by substituting new Paragraph 12 as follows*:*

(a) 12. "*An award or judgment of the VAT Tribunal shall be enforced as if it were a judgment of the Federal High Court on registration of a copy of the*

award or judgment in the Registry of the Federal High Court by the party seeking to enforce the award or judgment.".

(b) In paragraph 13, by inserting after paragraph (f), the following new paragraph**:**

(g) "an address for service of any notice, precept or other documents to be given to the appellant by the Secretary to the Zonal VAT Tribunal".

(c)by inserting immediately after paragraph 20, the following new paragraphs:

21. *The Minister shall make rules regulating the practice and procedure of the VAT Tribunal and, until such rules are made, the practice and procedure of the Federal High Court shall apply with such modifications (whether by way of addition, alteration of omission) as the circumstances may require.*

22. *Any case or proceeding relating to a matter for which the VAT Tribunal has jurisdiction pending before the Federal High Court on the commencement of this paragraph shall be continued and completed as if this Decree had not been made.*

23. *(1) Following the decision of the VAT Tribunal, notice of the amount of the tax chargeable under the assessment as determined by the VAT Tribunal shall be served by the Board on the company or person in whose name the tax is chargeable.*

(2) Notwithstanding that an appeal is pending, tax shall be paid in accordance with the decision of the VAT Tribunal within one month of notification of the amount of the tax payable in pursuance of subparagraph (1) of this paragraph.

24. *(1) Any party aggrieved by the decision of the VAT Tribunal may appeal against the decision on a point of law to the Court of Appeal on giving notice in writing to the Secretary to the VAT Tribunal within thirty days after the date on which the decision was given setting out the grounds on which the decision is being challenged.*

(2) On receipt of a notice of appeal under subparagraph (1) of this paragraph, the secretary to the VAT Tribunal shall compile the record of proceedings and judgment before the VAT Tribunal and shall cause them to be transmitted to the Chief Registrar of the Court of Appeal together with all the exhibits tendered at the hearing before the VAT Tribunal within thirty days after the date on which the decision was made.

25. *The President of the Court of Appeal may make rules providing for the procedure in respect of appeals made under this Decree and until such rules are made, the Court of Appeal Rules relating to the hearing of appeals shall apply to the hearing and determination of an appeal under this Decree".*

(5) Finance (Miscellaneous Taxation Provisions) (No. 2) Decree No. 18 of 1998

The Decree came into effect on 1st January, 1998 and made yet another amendment to section 36 VAT Decree by altering the sharing formula as follows:

a) 25% to the Federal Government (previously 35%)
b) 45% to the State Governments (previously 40%)
c) 30% to the Local Governments and Abuja (previously 25%)

(6) Part V, Finance (Miscellaneous Taxation Provisions) Decree No. 30, 1999

The Decree was signed into law at Abuja on 10th May, 1999, with a commencement date of 1st

January, 1999;[13] it amended sections 13A and 36, while it deleted three items.
The Decree corrected the mistake made in Decree No. 18 of 1998, whilst inserting a new sub-section 13A(2), where the words "input tax" replaced "output tax."
The Decree made yet another amendment to section 36 VAT Decree in respect of the 1996 distribution formula of VAT among the three tiers of government as follows:

(a) 15% to the Federal Government, instead of 25%.
(b) 50% to the State Governments and the Federal Capital Territory, Abuja, instead of 45%; and
(c) 35% to the Local Governments, instead of 30%.

The First Schedule was amended by a deletion of the following:

- **Item 4** (Newspapers and Magazines),
- **Item 6** (Commercial Vehicles and Commercial Vehicle spare Parts) and
- **Item 12** (Water Treatment Chemicals).

The Second Schedule was also amended by substituting a new first paragraph:

> *"The Minister may by notice in the Federal Gazette, establish a Value Added Tax Tribunal in each Zone of the Federal Inland Revenue Service*."

(7) VAT Tribunal Notice No. 25 of 2000
The VAT Tribunal Notice No. 25 of 11th February, 2000, established the VAT Tribunal in each of the eight Zones of the Federal Inland Revenue Service.

(8) Value Added Tax Decree 102 of 1993 as CAP V1, LFN, 2004
The VAT Act (being the VAT Decree as variously amended which had the status of existing law under the 1999 Constitution) was codified as Cap. V1, LFN, 2004.[14]
[2]

Part V of Cap. V1 specified 13 Offences and penalties in sections 25 to 37, which included Furnishing of false document, Evasion of tax, Failure to make attribution, Failure to notify change of address, Failure to issue tax invoice, Failure to register, Failure to keep proper records and accounts, Failure to collect tax and Failure to submit returns. Section 45 repealed the Sales Tax Act.[15]

(9) Value Added Tax (Amendment) Act, 2007
A major outcome of the 2002-2004 Tax Reform initiative was the set-up of a Presidential Committee on 18th October, 2004, to review the tax laws.[16] On 16th April, 2007, the Value Added Tax (Amendment) Act No. 53 of 2007 was one of the four legislations passed by the National Assembly.

The amendment Act retained the existing 5% VAT rate, but introduced other fifteen changes. The amended sections were 4, 10, 10A, 11A, 12, 13(3), 16(2), 16(4), 16(5), 36, 42, First Schedule, insertion of new Part 111 and provision of 17 Orders in a newly introduced Subsidiary Legislation.

The amendment Act provided for the following:

- In view of the reform that introduced the system of integration of Tax Offices, the words "VAT Office" were substituted with the words "Tax Office" wherever they occurred in the VAT Act.
- *"The tax shall be computed at the rate of 5% on the value of all goods and services, with the exception of goods and services, listed under Part III of the First Schedule, which shall be taxed at zero rate.''*
- *"The Service to determine and direct the companies operating in the Oil and Gas sector to deduct VAT at source and remit same to the Service"*
- Insertion of a new section on Tax Invoice such that a taxable person, who makes a taxable supply, shall, in respect of that supply, furnish the purchaser with a tax invoice, containing certain information.[17]
- *"A Tax Invoice shall be issued on supply whether or not payment is made at the time of supply."*
- Amendment of Section 12 - Time of Filing - by substituting for the figure and word "30th" day, for the figure and word "21st" day, and inserting that any payment made to duly authorized government agents shall be deemed to have been made to the FIRS.
- A taxable person, who is aggrieved by an assessment, made on the person, may file an objection to the FIRS.
- An appeal before the FIRS shall be determined within 30 days.
- Appeal from the decisions of the FIRS shall be made to the Tax Appeal Tribunal (TAT).
- An appeal from the TAT shall be made to the Federal High Court (FHC).
- Another distribution formula, of 15% to the Federal Government, 50% to the State Governments and the Federal Capital Territory, Abuja, and 35% to the Local Governments[18], was prescribed.
- Insertion of interpretation to "exported service"[24], "Imported Service"[25] and "Taxable person".[26]
- Substitution of new paragraph "7" to the First Schedule.[19]
- Insertion of new "Part III" on Zero-rate goods and services.[20]
- Appeals shall be as in the FIRS Act.

(10) Value Added Tax (Exemption of Commissions on Stock Market Transactions) Order, 2014

The Value Added Tax (Exemption of Commissions on Stock Market Transactions) Order, 2014 (the 2014 Order), was released via an Official Gazette, dated 30th July, 2014.[21]

The 2014 Order exempts[22] VAT on certain stock exchange transactions for a period of five years. This exemption is aimed at encouraging the increase in stock exchange transactions by bringing down the average cost of transactions on the stock market.

By this exemption, transaction costs for capital market transactions, normally borne by the investors, will be reduced. Additionally, it may reduce the compliance costs for operators,

such as stockbrokers and the regulators in accounting and remitting Value Added Tax to the Federal Inland Revenue Service.

ISSUES and CHALLENGES

(1) VAT Law and the Constitution

Under the 1979 and 1999 Constitutions, neither the VAT nor the Sales Tax was specifically allocated to either the Federal Government or State Governments. The VAT Act as constituted at present, is deemed as both a State Law and a Federal Law, pursuant to section 315, 1999 Constitution of the Federal Republic of Nigeria as amended.[23]

(2) Court of Appeal on Jurisdiction of the VAT Tribunal

The establishment of the VAT Tribunal under the VAT Act (VATA), equated the VAT Tribunal with the FHC, since appeals from its decision was to lie to the Court of Appeal (COA). Section 251(a) 1999 Constitution vests jurisdiction in revenue matters involving the FG or any of its agencies to the FHC to the exclusion of any other court. This nullifies the existence of VAT Tribunals.

(3) Declaration of VAT Tribunal Unconstitutional

The VAT Tribunal was declared unconstitutional in Stabilini Visinoni Limited v. FBIR[24] by the COA, Lagos Division. The Appellant's claim was that the provisions of section 20 VAT Act, which established the defunct VAT Tribunal, violated the provisions of section 251 of the 1999 Constitution. Therefore, the Appellant prayed the Court to dismiss the suit on the ground that the VAT Tribunal lacked jurisdiction to hear the suit. The prayer was granted, and it was declared that section 20 on the VAT Tribunal was inconsistent with the 1999 Constitution and, therefore, null and void.

Subsequently, the VAT Tribunal was abolished, and the TAT Appeal Tribunal was created by the FIRS (Act to also determine VAT disputes. In Cadbury v. FBIR,[25] about a year later, the same Lagos Division of the COA affirmed the decision in Stabilini Visinoni.

(4) Value Added Tax Pool Account

The VAT Pool Account receives monies realised from the administration of VAT all over the Federation. Its sharing formula is different from the formula of the Federation Account. Section 162 of the 1999 Constitution provides that all monies, collected by the Government of the Federation, must accrue to the Federation Account, whereas VAT is being paid into a different account. Thus, the existence of the VAT Pool Account could be regarded as a contravention of the Constitution.

(5) Sharing Formula

The method, adopted at present in allocating the VAT proceeds, is arguably inequitable; derivation formula should have more weight on the allocation. Furthermore, the percentage, allocated to the Federal Government should be further reduced in favour of States. States should be allocated in the region of 80%, as used to be the case at the inception of VAT.

(6) Is the TAT a Court or Part of the Administrative Mechanism for Settlement of Tax Disputes?

Even the TAT, which replaced the VAT Tribunal, has some flaws, as quite a number of taxpayers had challenged its jurisdiction in certain cases before the TAT, e.g.:

(a) **FIRS v. General Telecom Plc**[26] and

(b) **Esso Exploration and Production, Nigeria (Deep Water) Ltd. & Anor v. FIRS & Anor**[27]

In those cases, taxpayers had raised preliminary objections that the TAT had no jurisdiction to hear and determine their cases on the basis that section 59 FIRS Act was inconsistent with section 251 1999 Constitution.

But the TAT held in those cases that it had jurisdiction to determine them and that its jurisdiction was not inconsistent with that of the FHC, principally on the basis that it was not a court. The position of the TAT was that there was no inconsistency between section 59 FIRS Act and section 251(1) 1999 Constitution, the TAT not being part of the judiciary, but an administrative tribunal, established by the Minister of Finance.

An additional case, to illustrate where taxpayers raised preliminary objections that the TAT had no jurisdiction to hear and determine their cases on the basis that section 59 was inconsistent with section 251 of the 1999 Constitution, is:

c) TSKJ Construction International Sociadade Unipessonal LDA v. FIRS.[28] There, Ademola, J of the FHC, Abuja, upheld the argument of the company that the TAT lacked the jurisdiction to entertain the suit on the ground that section 59(I) FIRS Act which established the Tribunal was null and void for inconsistency with section 251(a) & (b) of the 1999 Constitution.[29] The Respondent's counsel also argued that the TAT, created by the FIRS Act, was an administrative panel, and not a court.

The learned Judge in delivering his judgment on 30th October 2013, found that the jurisdiction of the TAT was in direct conflict with the jurisdiction of the FHC and therefore invalid. He, consequently, upheld the appeal by TSKJ. The judge ordered the Finance Minister to disband the tribunals with immediate effect. The FIRS promptly appealed against the decision.[30]

(7) Notice of Increase in Rate of the VAT

Prior to the amendment of the VAT Act in 2007, an attempt was made on 3rd May 2006, by a former Minister of Finance[31] to increase the VAT rate[32], effective 23rd May, 2007. The Minister announced an increase in the VAT rate from 5% to 10%[33] and issued a Public Notice[34] in various newspapers, notifying the public on the increase and other new tax-related regulations.

The VAT increase was intended to be implemented as a total relief package under the then on-going reform and was to include a reduction or elimination of multiple taxes, reduction in stamp duties rates and improved Personal Income Tax (PIT) rate regime.

The increase in rate to 10% was necessitated by the following developments:

(i) The VAT rate of 5% is the lowest in the African Sub-region and has remained without change since the commencement of VAT in 1993, thereby constituting a source of distortion to trade and discouraging competition within the Region.

(ii) Nigeria, being a strong member of the Economic Community of West African States (ECOWAS), is obliged to review its current VAT rate, in line with the policy directives of the Commission on harmonisation of VAT and Excise Duties within the ECOWAS between then and 2009.

(iii) The ECOWAS Commission has, for this reason, suggested a transition period of two (2) years, terminating in 2009, within which member-States, at present applying low VAT regime, should close the gap to a point within the range of 10 – 20%;

(iv)With the recently promulgated VAT amendments, certain key features of a standard VAT system are now being introduced into Nigeria's VAT system in order to make it attractive for business. The input-output credit adjustment mechanism will eliminate inflationary effects.

Paragraphs (c) to (g) of the Notice, amongst others, defined taxable person and humanitarian donor-funded projects and re-emphasised the goods and services that remained exempt from VAT.

(8) Notice of Reversal on the 10% Increase in VAT Rate

Following the public outcry against the increase, Government announced its suspension and directed that the rate be reversed to 5%, pending further dialogue between Labour and Government representatives, as well as other stakeholders at a future date.

Subsequently, the Ministry issued a statement to confirm that the FG has indeed reversed the rate from 10% back to 5%, with effect from 23rd June, 2007.

(9) Oil Companies

Prior to September 2007, oil companies were not under obligation to deduct VAT at source, except from non-resident companies; but from that date, a new section, 10A(2), imposed responsibility on all companies in the oil and gas sector, whether upstream or downstream, as agent of VAT collection, expected to deduct VAT at source.

This new tax provision is similar to the provisions of sections 9 and 10 VAT Act. The section requires government Ministries, Departments and Agencies (MDAs) that have contract agreements with contractors and companies in Nigeria and which have contract agreements with non-resident companies, to hold back VAT charges, due on contracts awarded by them and remit such deductions directly to the FIRS.

An FIRS Information Circular was subsequently released to explain the amendment. It outlined the new duties and obligations on companies awarding contracts in the oil and gas sector.[35] Also, Contractors providing services to companies in the oil and gas sector are equally charged with some legal obligations.

(10) Tax Appeal Tribunals (Establishment) Order, 2009

In exercise of the powers conferred upon the Minister by section 59 and the Fifth Schedule FIRS Act, Dr. Mansur Muhtar, Minister of Finance, in 2010 constituted[37] the TAT.[38] The TAT thus replaced the defunct Body of Appeal Commissioners (BAC) and the VAT Tribunal. The TAT formally took off, pursuant to the Tax Appeal Tribunals Establishment Order, 2009.

The TAT is an attempt to provide a single appeal tribunal for the adjudication of disputes arising from the administration of taxes administered by the FIRS, instead of the previous arrangement whereby the VAT Tribunal focussed on VAT cases alone, whilst the defunct BAC handled cases that arose from other taxes.

The TAT for the various Zones were inaugurated on 4th February, 2010.[39] Specifically, and in accordance with Section 59(2) of the FIRS Act, TAT has powers to adjudicate and resolve controversies arising from the operations of the tax laws and regulations, as specified in the 1st Schedule to the FIRS Act as follows:

- Companies Income Tax Act (CITA)
- Petroleum Profit Tax Act (PPTA)
- Personal Income Tax Act (PITA)
- Capital Gains Tax Act (CGTA)
- Stamp Duties Act (SDA)
- Value Added Tax Act (VAT Act)
- Taxes and Levies (Approved List for Collection) Act; as well as other laws, regulations, proclamations, government notices or rules related to these Acts.[40]

Paragraph 5 of the Order provided that: *"All pending proceedings before the dissolved Body of Appeal Commissioners and Value Added Tax Tribunals are hereby transferred to the Tax Appeal Tribunals"*. Accordingly, in compliance with the Order, 122 appeals from the defunct BAC and the VAT were transferred to the TAT.

(11)Location of the Tax Appeal Tribunals

For administrative convenience, the TAT is located in eight (8) Zones, namely: Lagos, Abuja, South West (Ibadan), South-South (Benin), South East (Enugu), North Central (Jos), North East (Bauchi) and North West (Kaduna) with a coordinating secretariat to coordinate, render support services and facilitate the operations of the respective Zones.[41] Many of the TAT Commissioners appointed to be in charge of the Zones are not versed in taxation and many might have never handled a single tax case in their lives. Thus, there is need to be mindful of this consideration; it would be optimal to ensure that the TAT is composed of retired Tax Administrators and seasoned Tax Practitioners who are members of the Chartered Institute of Taxation of Nigeria.

(12) Ministries as Government Agencies

Section 10A VAT Act directs that Ministries and government agencies should withhold and remit tax charged on contracts awarded by them to the nearest local VAT office. This contradicts the general rule that the supplier is the taxable person in VAT. It is the supplier who is to file returns of output tax and not the buyer. But under section 10A, it is the government agency (i.e., the buyer) which is obliged to withhold VAT payable and remit to the VAT office. The implementation of this section has further created certain problems, including the fact that suppliers are denied their input tax, thus making VAT have the effect of a turnover tax, and refunds are not paid. This provision is deserving of revision.

(13) FIRS Information Circulars

The Information Circulars are not legal documents, the FIRS merely issues them for guidance and they are not binding; therefore, they cannot create estoppel against the FIRS. Since the Information Circulars do not have the force of law, the FIRS should desist from using such circulars to amend the law. They should merely be used for what they are meant for, which is guidance in understanding the tax laws.

(14) VAT Refund

Refund arises when input tax exceeds output tax; and according to section 13(1)(b) VAT Act, if input tax exceeds output tax, the FIRS is to refund, but this had been difficult to implement until the enactment of the FIRS Act in 2007. For a number of years, the FIRS failed to effectively operate a VAT refund system. However, with the establishment of the FIRS Act, the VAT refund system is now in place. Government should provide adequate fund for the purpose, as absence of an efficient VAT refund mechanism creates an apparent lack of trust and confidence in the tax system.

(15)Failure to Expunge the VAT Technical Committee

Section 21 establishes the VAT Technical Committee as follows:

There is hereby established a committee to be known as the Value Added Tax Technical Committee (in this Act referred to as "the Technical Committee".

The Committee functioned last in 2003; since then, its role has been taken over by the Technical Committee of the FIRS Board (TECOM). Therefore, it is hereby suggested that Part V VAT Act, which established it, be deleted.

(16) Co-existence of Value Added Tax Tribunal and the Tax Appeal Tribunal

Sections 20(1) and (4) of the VAT Act, provides that:

*(1) Any tax, penalty or interest which remains unpaid after the period specified for payment may be recovered by the Board through proceedings in the **Value Added Tax Tribunal**. [1996 No. 32.]*

*(4) Appeal from the decisions of the Federal Inland Revenue Service shall be made to the **Tax Appeal Tribunal.***

This is conflicting. Both the Value Added Tax Tribunal and the Tax Appeal Tribunal cannot co-exist in view of paragraph 5 of the Tax Appeal Tribunals (Establishment) Order, 2009, which stipulate that all pending proceedings *"before the dissolved Body of Appeal Commissioners and Value Added Tax Tribunals are hereby transferred to the Tax Appeal Tribunals"*. Section 20 (1) should be amended since the VAT Tribunal has been abolished.

(I7) Low Rate of the VAT
The current 5% rate of VAT has remained so since 1993, as consumers and taxable entities have opposed an attempt to adjust the rate. It is now imperative that the rate is increased to 10%, as contemplated in 2006.

(18) Limitation of the Claim of lnput Taxes on Capital Items
The current VAT regime limits the claim of input taxes on capital and overhead expenses. It will lead to cost inefficiency and consequently make goods produced in Nigeria less competitive. The non-deductibility of input taxes on capital items and overhead expenses has been criticised, as these are normally to be treated along with profit and loss expenses or be included in the cost of capital.

(19) Activities Carried out by Public Bodies
The current VAT law fails to recognise activities carried out by public bodies in the national interest as "activities outside the scope of VAT". An amendment is required in this area.

(20) Contractors as Final Consumers
Contractors, who rendered Services to Ministries, Departments and Agencies (MDAs), are often treated as final consumers and denied the refund of VAT paid on behalf of contract employers. Since this was not the intention of the law, it requires to be amended to be in tandem with the law.

(21) Registration Requirement of Non-Resident Companies

Non-resident companies are required to register for VAT in the name of the person with whom they have a subsisting contract, who shall then remit the tax in the currency of transaction.

(22) Abolition of Sales Tax Decree No. 4 of 1986, Cap. 192, LFN
In view of the inequity in the VAT sharing formula, some States such as Lagos, exercised their constitutional right to introduce Sales Tax on certain goods and services. The Federal Government erred by not abolishing sales tax throughout the Federation when the VAT Decree was introduced.

(23) VAT Allocation to States
At the onset of the VAT, its distribution to States and Local Governments was based on some parameters, which included recognition of derivation. Indeed, while commenting on the

fiscal policy programme for the 1993 fiscal year, the Secretary of Finance, Prince Oladele Olasore, announced, in Paragraph 17 of his Budget Speech, that t*he proceeds of the VAT will be shared as follows: Federal Government 20%; State Governments 80%.* He added that *the amount distributable from the States' revenue pool will be shared on the basis of the following criteria:*

State of origin 30%, Consumption/Destination 30% and Equality of States 40%.

The alterations to the VAT distribution formula over the years have hardly recognised the original parameters with respect to derivation. The effect of this neglect can be felt in the level of agitation for more revenue and the crave for internally generated revenue, which has led to multiplicity of taxes. The principle of fiscal federalism should be applied such that the States get their fair allocation.

(24) Contractors are required to produce evidence of VAT registration before they could obtain contracts from Government Departments. Whilst this requirement is not backed up by law, its policy underpinning cannot be faulted.

(25) Definition of "Basic Foods"

The scope of what is basic food is not yet clear. There is need to give a clearer definition that would remove the ambiguities. A guide should be provided by the FIRS to aid its interpretation, otherwise the taxpayers will remain confused.

(26) Absence of VAT Threshold

The concern here is about the absence of a VAT threshold, as currently being applied among ECOWAS member countries. It is a well-known fact that the Tax authority does not have sufficient resources to cover all taxable entities in enforcing actual compliance.

(27) VAT Exemption

The omnibus description, that any expense, not specifically exempted, is VATable, should be reconsidered.

(28) Current Status of the VAT Act - Re-Write of the VAT Law: The Project

The International Monetary Fund (IMF) team, under the technical assistance program, visited Nigeria in January 2010, and one of its recommendations was that all the Nigerian Tax Laws be re-drafted in plain English language, while expressing specifically that the VAT law should be re-written. Since then, various efforts, including working group sessions, have been held to achieve this novel feat. The FIRS has held numerous workshops to critically review the draft law as it affects e-commerce, financial services, government services, oil and gas and telecommunications, in order to develop a comprehensive and attractive VAT regime that will be accepted.

Recently, the FIRS received some funding intervention from DFID to be applied solely for the complete review of the current law. This review is on-going and is aimed at improving

understanding and communication, with a view to building the taxpayer's confidence in the system.

What led to the Review?
What informed the policy to review the VAT law was that the VAT law, as it is, is not explicit. It tends to deny the taxpayer of some basic entitlements, like the right to fully utilise all input taxes against output taxes. Input taxes paid, which are not in relation to the goods sold, are disallowed, for example, input taxes on restaurant bills. Capital items are also disallowed, whereas the international best practice is to allow such input taxes as creditable.

Another flaw in the Nigerian VAT is making the agent, the final consumer. The VAT is a consumer-oriented tax and should be paid only by the final consumer. Therefore, agents are not the final consumers, the customer is the final consumer. The VAT law is being rewritten completely in order to align it with the VAT Protocol Agreement, which is being adopted for the ECOWAS sub-region.

Expectations in the Re-write Project
The re-writing of the entire VAT law, with the aim of aligning the tax provisions with the best practices being adopted in the ECOWAS sub-region, would recognise the:

- Adoption of a VAT threshold.
- Retention of a single VAT rate.
- Taxable list and restricted exemption list.
- Deductible input taxes on capital items and overheads expenses and elimination of ambiguous provisions in the new VAT law.
- It is hoped that all the observations, which are being addressed in the proposed VAT re-write project, will significantly transform the Nigerian tax system to an enviable one.

Postscript: many of the gaps identified in this Chapter and the suggestions for reform have been addressed by substantive amendments to the VAT Act by the Finance Acts 2019 and 2020. Given the 'timing focus' of this Chapter, those subsequent amendments and their implications are respectively discussed in greater detail in other Chapters of this book, and readers are invited to refer to them accordingly.

ENDNOTES

1. As at 2015, there have been three versions of the Nigerian VAT law: the original Value Added Tax Decree No. 102; the Value Added Tax Act, Cap. VI, LFN, 2004 (codifying Decree No.102, as an existing law) and the Value Added Tax (Amendment) Act of 2007, which amended Cap. V1, LFN 2004. The Finance Decrees introduced over 25 amendments, while the 2007 VAT (Amendment) Act introduced over 15.
2. The VAT Decree (later became the VAT Act as an existing legislation by virtue of section 315 1999 Constitution) was codified as Cap.V1, LFN 2004.
3. The criticism has been made that the VAT Decree was one of the Decrees hurriedly signed into law by Gen. I.B. Babangida before he handed over the office on 27th August, 1993. (See James Adebisi Ariwodola, Value Added Tax, paper presented at the CITN Workshop in July 2001, p. 4).
4. No. 7 of 1986, Cap. 399, LFN 1990. Section 41 VAT Decree (now section 45 VAT Act) provided that, "subject to section 6 of the Interpretation Act, the Sales Tax Decree 1986 is hereby repealed."
5. The Finance (Miscellaneous Taxation Provisions) Decree No. 30 of 1996, issued on 23rd October, 1996 (Part V: Value Added Tax Decree) took effect retroactively from 1st January, 1994.
6. The Finance (Miscellaneous Taxation Provisions) Decree No. 18 of 1998; Part V.
7. The Decree made sundry amendments to income tax laws to give effect to the fiscal measures, contained in the 1995 Budget.
8. The original version provided that "a taxable person shall render to the Board on or before the 14th day of the month following that in which the purchase or supply was made, a return of all taxable goods purchased or supplied by him during the preceding month in such manner as the Board may, from time to time, determine."
9. Originally, "taxable person" was defined to mean "a person (Other than a public authority acting in that capacity) who independently carries out in any place an economic activity as a producer, wholesaler…….by way of trade or business."
10. "Taxable services" was originally defined to mean the services listed in Schedule 2 to this Decree, which are subject to tax under this Decree.
11. The Decree made sundry amendments to income tax laws to give effect to the fiscal measures, contained in the 1996 Budget. It was made at Abuja on 23rd day of October, 1996, and signed by General Sanni Abacha, the then Head of State, Commander- in-Chief of the Armed Forces, Federal Republic of Nigeria.
12. The Decree was signed into law by General Abdulsalami Alhaji Abubakar, Head of State, Commander-in Chief of the Armed Forces, Federal Republic of Nigeria.
13. The Decree was similarly signed by General Abdulsalami Abubakar, Head of State, Commander-in Chief of the Armed Forces, Federal Republic of Nigeria.
14. In May 2007, the National Assembly enacted the Revised Edition (Laws of the Federation of Nigeria) Act, 2007, to give effect and approval to the Laws of the Federation of Nigeria, compiled and published under the authority of the Attorney-General of the Federation and Minister of Justice. In Cap. V1, the commencement date of 1st December, 1993, and the six parts in the principal Decree are retained with two schedules - the First Schedule and the Second Schedule. Whilst the VAT Decree had 43 sections, Cap. V1 at the point of codification had 47 sections. Whilst the VAT Decree had three schedules; Cap. V1, LFN, 2004 had only two Schedules and does not

list "taxable goods and services", as was done in the VAT Decree.

15. LFN, Cap. 123.
16. This step produced tax bills, which ultimately became the Federal Inland Revenue Service (Establishment) Act, Cap. F36, 2004 LFN (FIRS Act, originally Act No.57 of 2007); Companies Income Tax (Amendment) Act No.11 of 2007; Personal Income Tax (Amendment) Act No. 20 of 2011 and the Value Added Tax (Amendment) Act No.12 of 2007.
17. (a) Tax payer's identification number; (b) Name and address; (c) VAT Registration Number; (d) The date of Supply; (e) Name of Purchaser or Client; (f) Gross Amount of Transaction; and (g) Tax Charged and Rate Applied.
18. Provided that the principle of derivation of not less than 20% shall be reflected in the distribution of the allocation amongst States and Local Governments, as specified in sub-paragraphs "(b) and (c) of this section".
19. 7. Plant, machinery and goods imported for use in an Export Processing Zone or Free Trade Zone: provided that 100% production of such company is for export, otherwise tax shall accrue proportionately on the profits of the company".
20. The zero-rated goods and services: 1. non-oil exports; 2. Goods and services purchased by diplomats; and 3. Goods purchased for use in humanitarian donor-funded projects." "Humanitarian donor-funded project" includes "Projects undertaken by Non-Government Organizations and Religious and Social Clubs or Societies recognized by law whose activity is not for profit and in the public interest".
21. The 2014 Order was issued by the finance minister in exercise of her powers under section 38 of the VAT Act. The commencement date of the Order is 25th July, 2014, to be in force for five years from the date of commencement.
22. The VAT exemption applies to commissions or fees earned on traded shares, Due to the Securities and Exchange Commission (SEC); the Nigerian Stock Exchange (NSE); and the Central Securities Clearing System (CSCS). The exemption covers commissions on bond as well as equity trades.
23. In 2001, the Lagos State Ministry of Finance (Board of Internal Revenue) notified the general public that "the Sales Tax Law Cap. 175, Laws of Lagos State of Nigeria 1994 which was amended by the Sales Tax (Schedule Amendment Order 2000) on selected luxury items is still in force" and listed 11 taxable Goods and Services.
24. [2009] 13 NWLR (Pt. 1157), 200.
25. [2010] 2 NWLR (Pt.1179), 561.
26. (2013) 1 NRLR 44; (2012) 7 TLRN 108.
27. (2012) 8 TLRN 45.
28. (2014) 13 TLRN 1
29. Section 251(1)(a) & (b) confers exclusive jurisdiction on the Federal High Court in respect of Tax matters.
30. See FIRS v. TSKJ Construcoes Internacional Sociadade Unipersonal LDA (2017) 23 TLRN 58. The COA overruled the FHC and posited that the TAT is an administrative tribunal per its enabling statute. The court also stated unequivocally that the jurisdiction of the TAT is not a usurpation of the jurisdiction of the FHC, but a condition precedent to invoking its jurisdiction.
31. The Notice was signed on 21st May, 2007, by Mrs. Nenadi E, Usman, Hon. Minister of Finance.
32. The decision for the 100% increase was informed by the ECOWAS Commission

directives to member-States to harmonise their respective rates, along with certain other key features that will improve VAT Administration.

33. The Minister cited Section 34(a) of the Value Added Tax (VAT), 1993 (as amended), (inserted by Finance (Miscellaneous Taxation Provisions) Decree No. 31 of 1996), which vested the power to amend the rate of tax chargeable under the Act in the Honourable Minister of Finance.
34. Paragraph 1 Value Added Tax Act Rate of Tax Chargeable Order replaced the 5% figure with 10%, thereby amending section 4 VAT Act. The Order had a commencement date of 23rd May 2007.
35. Such companies are to:

- Withhold and remit to the FIRS, the VAT charges, due on all contract awards.
- Prepare and forward to the FIRS, the relevant VAT schedules, as specified.
- Pay VAT on all the contracts being awarded (other than exempted goods and services).
- Separate the returns on normal trading activities from those of its own consumption or contract awards; and demand from the FIRS, relevant receipts, as evidence of VAT paid. Evidence of VAT withheld should be produced to the contractors to facilitate any claims of refund from the FIRS.

36. This Order seeks, among other things, to specify the number of zones, location of each zone in the States, appointment of Chairmen and Commissioners of the Tribunal and other matters for the effective exercise of its jurisdiction, as provided under the Fifth Schedule to the Federal Inland Revenue Service (Establishment) Act, 2007.
37. The 2009 Order was published in the Federal Government Gazette No. 296, Vol. 96 of 2nd December, 2009.
38. The Honourable Minister constituted the Tribunal into the following zones of the Federal Republic of Nigeria: North East Zone Tax Appeal Tribunal, North West, North Central, South West, South East Zone, South South, Abuja Tax Appeal Tribunal and Lagos Tax Appeal Tribunal.
39. The first term of the pioneer members inaugurated expired in February 2013 and they have been re-appointed for a second and final term.
40. It is important to state that the FIRS Act and the Education Tax Act were not specifically mentioned in the list of the tax laws that TAT can adjudicate on. Perhaps because they are not really "tax laws".
41. The locations of the TAT are listed in Gazette No. 77, Vol. 96, dated 2nd December, 2009. All the eight zones of the TAT commenced sitting in the first quarter of 2011. The cases before the TAT included new and old cases that were initially pending before the BAC and the VAT Tribunal.

CHAPTER 4

RECENT DEVELOPMENTS IN VALUE ADDED TAX IN NIGERIA FROM 2013-2020

Abstract

Considering the dynamic nature of taxation, it is important to keep abreast of developments from time to time to determine the current policy and law on a particular issue. The coverage of review in this chapter is limited to 2013 to 2020. One of the major policy issues, relating to VAT, is whether or not the rate would be increased from five percent. There are conflicting pronouncements from the government officials on a possible rate review. On the statutory plane, the last substantive amendment to the Value Added Tax Act (VAT Act) was made in 2007, via the Value Added Tax (Amendment) Act of 2007 which the Finance Act 2019 and 2020 has consolidated. There has, however, been some recent moves by the legislature to consolidate all taxes into a single enactment; this would see all tax laws collapsed into one law, including the VAT Act. In addition, the scope of exemption was slightly widened through a subsidiary legislation; the Value Added Tax Act (Exemption of Commissions on Stock Exchange Transactions) Order 2014, which grants a five-year exemption on certain commissions earned on traded value of the shares and stock-related transactions. Certain developments have also taken place through case laws, as the Tax Appeal Tribunal and law courts pronounced in life disputes between the taxpayers and tax authorities. These include the decision of the Supreme Court, dismissing the case of Lagos State Government, which challenged the constitutionality of the VAT Act on a technical preliminary point. There have also been conflicting decisions of the Federal High Courts, Sokoto and Lagos Divisions, on whether bottled water is subject to VAT; and between the Abuja and Lagos Zones of the Tax Appeal Tribunal on the liability of a non-resident company to VAT in Nigeria. This chapter notes that these developments have introduced a measure of uncertainties in the policy and law on VAT in Nigeria and calls on the Federal Government to harmonise, clearly articulate and streamline the policy and legal frameworks.

1. Introduction

Nigeria is in the aftermath of a huge economic crisis, due to the sharp fall in the price of crude oil, which is the mainstay of government revenue.[1] The deficit in the federal and state budgets is widening. Virtually all the States are still in deep financial crisis, despite federal intervention by way of bail out.[2] In troubled times, such as this, one would expect the government to reinvigorate the tax policy, law and administration in order to give the economy a new lease of life.[3] It is remarkable that nothing much has been done to give us hope that there will be a turnaround on a sustainable basis. The Value Added Tax Act[4] (VAT Act) was last amended in 2007 through the *Value Added Tax (Amendment) Act*[5] of 2007 until the current legislative activism of the National Assembly through the enactment of Finance

Act 2019 and 2020, respectively. Some of the significant changes by that amendment have been discussed in a recent publication by the Chartered Institute of Taxation of Nigeria.[6] The coverage of this chapter will, therefore, be limited to a period from 2013 to2020. The period of coverage is reinforced by the ordinary meaning of the word "recent", which is "that which happened only a short while ago."[7] and the need to avoid or minimise the repetition of what had been sufficiently discussed in other chapters of this book.[8] This chapter, therefore, discusses the major policy, legal and administrative changes to the Value Added Tax (VAT) in Nigeria from 2013 till the date of the publication of this book.

2. Policy Changes

A good tax system is predicated on a sound policy, law and administration in that order. The alternative is to have a sub-optimal tax system. Tax policy is a set of fundamental ideas or plans on how the tax system is established, operated and reformed when the need arises. A policy serves as a useful guide or barometer in determining what legislative and administrative action government may or may not take. Thus, the National Tax Policy[9] declares:

> The National Tax Policy seeks to provide a set of guidelines, rules and modus operandi that would regulate Nigeria's tax system and provide a basis for tax legislation and tax administration in Nigeria.[10]

The Federal Government espoused a set of objectives, which include reduction of the number of taxes, shifting the focus of the tax system from direct to indirect taxes, reduction of internal multiple taxation, streamlining the tax incentives, comprehensive review of tax laws every three years, etc.[11] The Federal Government declares its intention to pursue a consistent tax policy reform thus:

> However, there is now a renewed commitment by the Federal Government to diversify the economy by growing the non-oil tax revenue in order to develop a stable and sustainable revenue source to finance developmental projects. Following from the above, it is evident that the tax system required reform. Although there had been several reforms in the past, these reforms were not pursued under any policy direction and, in some cases, were carried out in an uncoordinated manner. This informed the decision of the Study and Working Groups (referred to above) that there should be a National Tax Policy that would provide a direction for Nigeria's tax system and establish a framework that all stakeholders would subscribe to and to which they would be held accountable. It is in line with this, that the National Tax Policy is set out below.[12]

In so far as the National Tax Document Policy has not been amended, it is fit and proper to regard it as the barometer by which the standpoint of the Federal Government will be measured.

The major policy issue relating to VAT was whether or not the rate will be increased from 5 percent, which is, perhaps, the lowest in the world[13] to current rate of 7.5%. The erstwhile Managing Director of the IMF, Christine Lagarde, sometime advised Nigeria to consider increasing the VAT rate.[14] There is yet no coherent policy statement from the Federal Government. While there was no categorical statement by the President in his 2016 Budget Speech on whether there would be an increase of VAT,[15] an official position was subsequently projected that there would be no increase of the VAT rate or introduction of a new tax. At the end of the National Economic Council (NEC) meeting, presided over by Vice-President Yemi Osinbajo in January, 2016, briefing the media, the Minister of Budget and National Planning, Senator Udoma Udo-Udoma, said there was no plan to increase either the VAT or the corporate tax. According to him:

> We do not intend to increase VAT rate at the moment but increase collection rate from 20 per cent. We will also not raise the corporate tax because we do not want to impose additional burden on Nigerians. Government's position is, however, that those who make money and have not been paying taxes should pay. We expect at least 20 per cent increase in tax collection rate which is conservative in terms of our revenue projection.[16]

The general understanding of the above statement is that, as a strategy to improve tax revenue, government would widen the tax base, rather than increase any tax rate, which is consistent with the National Tax Policy. It appears that the Federal Government may have reconsidered its position, following a subsequent statement by the Vice – President, Prof Yemi Osinbajo, on the imperative of increasing the VAT rate thus:

> The International Monetary Fund had last week reiterated its advice to the Federal Government to increase the VAT rate gradually. The Managing Director of the fund, Christine Lagarde, had in January during her visit to Nigeria, urged the government to increase the VAT rate. "To move the nation forward, we must move beyond oil." The reality is that, while oil accounts for 14.4 per cent of our Gross Domestic Product, it continues to be the source of 90 per cent of official foreign exchange earnings; and prior to this year, up to 76 per cent of government revenues.[17]

Whatever merit may be in the above statement, it is ill timed in the writer's view to increase the VAT rate, considering the rising inflation and the general hardship following the recent deregulation of the price of oil.[18] Unfortunately, this increase proposal was successfully passed into law by the National Assembly, which had consistently in the past refused to pass consent to increase of VAT rate, even when the economy was relatively far better.[19]

3. Legal Changes

The VAT was introduced in Nigeria in 1993.[20] Since then, the Value Added Tax Decree[21] has been amended more than half a dozen times[22], the latest being the *Value Added Tax (Amendment) Act*[23] of 2007. However, no subsidiary legislation has been made since then.

Subsidiary Legislations

Value Added Tax Act (Exemption of Commissions on Stock Exchange Transactions) Order 2014

In response to the clamour by the stakeholders in the Nigerian Capital Market for alleviation of tax burdens, the Minister of Finance made an Executive Order: the *Value Added Tax Act (Exemption of Commissions on Stock Exchange Transactions) Order 2014,* which granted a five-year exemption on four types of commissions, viz: (i) earned on traded value of the shares; (ii)payable to the Securities and Exchange Commission (SEC); (iii) payable to the Nigerian Stock Exchange (NSE); and(iv)payable to the Central Securities Clearing System (CSCS). It should be borne in mind that the Executive Order lapsed in 2019 on effluxion of time, unless it is re-enacted. It is difficult to assess the extent to which these exceptions have alleviated the concerns of the capital market operators and helped to deepen the market. Therefore, in the absence of an empirical study, the assessment of the possible impact of the exemption will be a matter of conjecture.

In the view of this author, the major concerns of the operators in the capital market relate mainly to double income taxation and multiplicity of fees. By double income taxation, they mean that tax is levied on the income of the company in its hands (in its corporate name) and, thereafter, the dividends and other distributions, made to shareholders out of the profits, are again subjected to tax in the shareholders' hands, as their personal income tax.

Technically speaking, the above scenario does not amount to double taxation. This is what happens where the taxation of the income of companies is based on the Classical Theory of taxation. Double taxation is a well-established concept in international taxation. Double taxation, at the intra-national level, occurs where the same income or piece of property is subject to tax twice or more in the hands of the same taxpayer by the same tax authority. Therefore, since a company is a distinct and separate person from its shareholders, the taxation of the income of a company cannot be said to be the same as the taxation of the income of the shareholders. The Classical Theory of taxation of companies views companies' income tax as part of the price paid for the privileges of incorporation. An investor, who desires to avoid paying companies' income tax, has a choice of carrying on business, either as a sole proprietor or partnership.

The Imputation Theory, however, taxes the profits of a company in its hand but allows, on distribution, a portion of the companies' income tax already paid, to be imputed to the income tax liability of the shareholder. In this circumstance, a shareholder will be given credit for the tax already deducted under the companies' income tax. The imputation system is popular in the European Union.[24] White has commended the system in the following glowing terms:

> It attracts investors and broadens the base of capital markets which is at the heart of a good 'communautaire'[25]

In view of the relative advantage of the imputation model, it may be worthwhile for the operators in the capital market to advocate for the imputation model, instead of seeking to directly eliminate, either taxation of company or dividends. But the implications of such a reform, especially, on the earning of the government(s) and inter-government fiscal relations must be carefully examined.

VAT and Transfer Pricing Regulations, 2018

Another recent development, with respect to Value Added Tax, is the insertion of the VAT Act, as one of the tax laws, that is to be given effect to under the new Income Tax (Transfer Pricing) Regulations, No. 35, Volume 105 of 2018. This is a departure from the old Regulation, in which there was no reference to VAT. The implication is that VAT is to be taken into consideration for Transfer Pricing assessments or audits. However, this is suspect. Although the Federal Inland Revenue Service (FIRS), through one of its officials, defended the inclusion of the Value Added Tax Act, as one of the laws, that is to be given effect to or considered under the Transfer Pricing Regulations, the reality is that it is doubtful if this is necessary. First the VATAct does not have trnsfer pricing-related provisions. Unlike the Companies Income Tax Act, the Personal Income Tax Act, the Capital Gains Tax Act and the Petroleum Profits Tax Act, the VATAct does not contain any provision seeking to prevent tax avoidance through artificial transactions. This means that, there is no statutory basis for accusing or holding a taxpayer liable for tax avoidance through artificial transactions under the VATAct. Therefore, it remains to be seen how a taxpayer would be accused of engaging in artificial transactions for VAT purposes. This also means that it is legally, and must add, practically impossible, to manipulate VAT for transfer pricing purposes. VAT is a tax on supply of goods and services and is calculated, based on the declared value of the transferred goods or services. Therefore, if there is to be any manipulation at all, it would be with respect to income or price paid for the transferred goods and services, and not necessarily on the VAT aspect of the transaction.

4. Case Law Developments

There have been some developments in the ways that the Tax Appeal Tribunal (TAT) and the Courts have interpreted some of the provisions of the VAT Act. The important development centred on (i) *VAT and Division of Taxing Power*, (ii) the *definition of basic food item*, and (iii) *the liability of a non-resident company to VAT in Nigeria*. What follows is a discussion of the relevant cases on these developments.

(i) VAT and Division of Taxing Power

Following the commencement of civil rule under the Constitution of the Federal Republic of Nigeria, 1999[26], there emerged a dispute between the Lagos State Government and the Federal Government on which level of government has power to impose VAT. There has been persistent call by Lagos State for fiscal federalism and a revision of who has power to impose VAT between the Federal Government and the States. The discontent of Lagos State arose from the sharing formula for distributing the VAT pool under the VAT Act. Following a series of unsuccessful attempts to resolve the dispute, the Lagos State Government, in 2005,

filed an action at the Supreme Court to determine whether the VAT Act was valid, in view of the constitutional provisions on division of taxing power under section 4 of the Constitution of the Federal Republic of Nigeria, 1999.

The case *Attorney General of Lagos State v Attorney General of the Federation &Ors*[27] was commenced by Lagos State in 2008, while judgment was delivered in 2014. Lagos State invoked the original jurisdiction of the Supreme Court by filing the case at the apex court. It argued that the Lagos State House of Assembly was entitled to enact laws with regard to imposition and collection of tax on supply of all goods and services within Lagos State and that Lagos State or any of its agencies was the body entitled, to the exclusion of any other body, to assess and collect such a tax. The revenue of Lagos State Government has been, and continues to be, affected by the enforcement of the VAT Act. The Plaintiff, therefore, sought an order of the Supreme Court, declaring the VAT Act unconstitutional, and a perpetual injunction, restraining the Federal Government, its servants or any of its agencies, from continuing to give effect to the provisions of the Value Added Tax Act. However, the Federal Government filed a preliminary objection, challenging the action on the ground, among others, that it related to acts of a federal organ and, therefore, could not form the basis of invoking the original jurisdiction of the Supreme Court. The Supreme Court held that the main grouse of Lagos State related to the administration of VAT by the FIRS. Upholding the preliminary objection, the Court held that its original jurisdiction could only be invoked to resolve a dispute involving a State and the Federation, and not a dispute with an agency of the Federal Government.

The bottom-line of this decision is that Lagos State ought to have instituted its case at the Federal High Court and gone through the appeal ladder to the Court of Appeal, up to the Supreme Court. The judgment has been severely criticised by a wide spectrum of writers. According to Chuka:

> Rather curiously, the Court attempted to draw a distinction between *"Federal government and the governments of the states*" on one hand and *"the federation and the various states"* on the other hand. There is nothing to show that both expressions are different in character and meaning and the Court did not offer any guidance in respect thereof. The Court held that since the dispute is between *"Federal government and the governments of the states*" rather than *"the federation and the various states",* it is therefore not within the contemplation of section 232 of the 1999 Constitution.
>
> While it is correct that section 232 of the Constitution speaks of the '*Federation*' and not the '*Federal Government*', for the purposes of the Supreme Court's original jurisdiction, there is no record of such a distinction having ever been drawn. Indeed, the various disputes between the Federal Government and the various State Governments[28] have been heard by the Supreme Court in the exercise of its original jurisdiction without any jurisdictional challenge. The concern is that this decision of the Supreme Court has the potential of excluding every suit between the '*Federal*

> *government and the governments of the states*' from the Supreme Court's original jurisdiction, thereby rendering that jurisdiction redundant. This decision also creates unnecessary debate as to the matters which come within the Supreme Court's original jurisdiction as every time there is a dispute between a State and the Federal Government, there is likely to be a debate as to the court seised with jurisdiction.[29]

While the above analysis is substantially correct,[30] it appears that the Supreme Court, as the final court in Nigeria, chose to save VAT, rather than bury it.[31] This can be inferred from the initial broad approach of the Court to the narrow the confines on which its decision was based. When the Federal Government raised a preliminary objection that the case amounted to an abuse of court process on the ground that Lagos State should have appealed against the decision of the Court of Appeal in *Attorney-General, Lagos State v Eko Hotels*[32], instead of instituting a fresh action, the Supreme Court ruled that both the preliminary objection and the substantive suit should be taken together, which suggested a desire to accelerate the hearing of the case. The subsequent turn of event, however, reveals lack of commitment on the part of the Supreme Court to treat the case with the urgency it deserves. At the instance of the Supreme Court, parties had explored out-of-court settlement option to no avail. Despite the report by the parties, that the case be determined on merit, following the failure of their efforts to resolve the case amicably, the case still suffered undue adjournments on a number of occasions at the instance of either the Supreme Court or the parties. For a case that has dragged for so long, one would have expected the Supreme Court to also decide the case on its merit, having heard the parties on the merit of the case.

In any event, since the decision of the Supreme Court, Lagos State has not filed a fresh action at the Federal Court and has generally played down its criticism of the VAT structure. Notwithstanding the quietness of Lagos State, it is doubtful if the issue can be said to have been satisfactorily resolved, without either a constitutional amendment or a decision of the Supreme Court on merit.

(ii) Definition of Basic Food Item

Section 2 and Item 2 of Part 1 of the First Schedule to the VAT Act exempt "basic food items" from VAT. The meaning and scope of the exempted goods and services are not defined in either the Statute or the FIRS Circulars. For example, the scope of what is meant by "basic food" is not clear. Generally, what is a basic food depends on the status in life of an individual and varies from person to person.[33] The present practice by the FIRS is to limit the meaning of basic food to uncooked and unprocessed food items,[34] while processed food items, such as spaghetti, corn flakes, baked beans and cheese, are taxable..[35]

Remarkably, the FIRS served the defendant, who was trading in stock fish, with a demand notice for VAT in the case of *Federal Inland Revenue Service v Chi Chi & Mark Limited.*[36] The Tax Appeal Tribunal had no difficulty in holding that the Defendant was not liable to VAT, since it was not trading in commodities liable to VAT.

The VAT status of water has, however, been controversial. In *Monamer Khod Ent. Nig. Ltd.&Anor v Federal Inland Revenue Service & Ors,*[37] (*Monamer's case),* the Sokoto Judicial Division of the Federal High Court held that sachet water was subject to VAT on the basis that it had undergone the process of manufacturing and packaging. According to the Court:

> In the instant case the court is not in doubt upon the totality of evidence before the court that the plaintiffs are in the business of manufacturing and packaging of water called GHADIR TABLE WATER in sachets and the law as currently amended section 2 finance MISCELLANEOUS TAXATION PROVISIONS (NO.2) Act 1996 No.31 clearly prescribes that tax shall be charged and payable on the supply of goods and services classified as taxable except on those exempted in the schedule. There is no doubt under the law taxable goods include all goods manufactured in Nigeria including water. Once it has undergone process of manufacturing and packaging whether in bottles or other containers as sachet or by whatever name called. Unless it is shown clearly by evidence that a particular process by which water was produced is exempted under the third schedule to the Act. In the instant case the plaintiffs have not been able to adduce any good reason to support why they decide to flagrantly refuse to comply with the law despite the fact that they were served with exhibits "E & F". In the circumstances of this case the plaintiffs have not adduced any cause to support any of the reliefs claimed couched deliberately to embarrass and to annoy all. The plaintiffs' case ought to fail. It has woefully failed and consequently dismissed for lack of merit.

But in the case of *Warm Spring Waters Nig. Ltd. & Ors v Federal Inland Revenue Service*[38], the Lagos Judicial Division of the Federal High Court held that water was a basic food and, therefore, exempted from VAT. The court reasoned that treatment and packaging of water did not remove water from the scope of basic food items under the VAT Act. According to the court:

> The fact that water is treated and/or bottled does not change or alter its character such as to make it incapable of constituting a basic food item.....the treatment and bottling merely improves the safety of water for consumption and does not in any way reduce its relevance or necessity as a basic food item.

The existence of conflicting decisions of two divisions of the Federal High Court, the Sokoto and Lagos divisions has introduced a measure of confusion in a subject where certainty is most desirable. The FIRS and taxpayers would ordinarily be free to pick and choose where to pitch tents until there is a decision of the Court of Appeal on the matter. The amendment to the VAT Act pursuant to Section 46 of the Finance Act 2019 has however resolved the controversy[39].

The judge in *Monamer*'s case, though, gave a correct decision but adopted a wrong reasoning. Section 2 and Item 2 of Part 1 of the First Schedule to the VAT Act exempts basic food item, not basic food. Emphasis seems to have been placed on "basic food", without considering the possible effect of "item". The word item means "a single article or object."[40] If the intention were to exempt basic food, it would not have been necessary to insert "item" at the end of basic food. The question whether water is liable to VAT will depend on whether water is a basic food item. The view of this author is that water is neither "food" nor "food item". Food and water mean separate things. Food refers to "things that people or animal eat"[41], while water refers to "a liquid without colour, smell or taste, that falls as rain, is in lakes, rivers and seas, and is used for drinking, washing, etc.[42] We eat food, while we drink water. At restaurants, hotels and eateries, food and waters are charged separately. The fact that food is qualified by use of word "basic" shows a clear indication not to exempt all foods, which generally will require a determination of what foods are basic and what foods are not. However, with regards to water, it is not necessary to consider the meaning "basic", for it is after something has qualified as a food that the question whether it is a basic food becomes relevant. Thus, it would have been sufficient for the learned Judge, in *Monamer*'s case, to hold that packaged water was liable to VAT, not being exempted in the Schedule. The fact that they had "undergone the process of manufacturing and packaging" is totally irrelevant, as VAT is triggered by mere supply of goods and services, except those exempted in the Schedule to the VAT Act.

(iii) Liability of a Non-Resident Company to VAT in Nigeria

Sections 2 and 10 of the VAT Act have the audacious objective of subjecting a non-resident company to VAT. The provisions are set below, for ease of reference:

> 2. The tax shall be charged and payable on the supply of all goods and services (in this Act referred to as "the taxable goods and services") other than those goods and services, listed in the First Schedule to this Act.
>
> 10.
>
> (1) For the purpose of this Act, a non-resident company that carries on business in Nigeria shall register for the tax with the Board, using the address of the person with whom it has a subsisting contract, as its address for purposes of correspondence relating to tax.
>
> (2) A non-resident company shall include the tax in its invoice and the person to whom the goods and services are supplied in Nigeria shall remit the tax in the currency of the transaction.

The FIRS has always held the view that the above provisions obligate a non-resident supplier of goods and services to a person, with whom it has a contract in Nigeria, to register for and charge VAT on its invoice(s), which will be accounted for by the latter. Some taxpayers have, however, taken the view that the obligation to register and charge VAT would arise only where the non-resident supplier "carries on business in Nigeria".[43] While many may not agree with the FIRS' position on the scope and effect of sections 2 and 10 VAT Act, it would appear that majority of taxpayers have been "sheepishly" complying. *Gazprom v FIRS*[44]

(Gazprom's Case) presented the first opportunity to test the correctness, or otherwise, of the FIRS' position. The Appellant received advisory and research services from non-resident companies. These services were performed outside Nigeria and the foreign companies never sent any employee or equipment to Nigeria. Sometime in June 2012, the Respondent carried out an audit of the Appellant. During the reconciliation meeting, everything discussed was in relation to Withholding Tax alone, after which the Respondent reduced the assessment, which it had earlier computed. There was no discussion as to liability for VAT. However, by another letter, dated 27th November, 2013, the Respondent, for the first time, accused the Appellant of not rendering VAT in respect of advisory and research services supplied by non-resident companies and raised two additional assessments in the sum of $339,168.87 and Euro 50, 894.96. Following the refusal of the Appellant's objection, the Appellant appealed to the TAT on 11th June, 2014.

On 10th June, 2015, the TAT, Abuja Zone, held, in the Gazprom's case, that section 10 imposes obligation to register only on non-resident companies "carrying on business in Nigeria", and not on all non-resident companies generally. Thus, a non-resident company, that does not carry on business in Nigeria, is not obligated to register for and charge VAT. It is not clear whether the FIRS has appealed against this decision[45]. Like a typical case of different strokes for different people, some practitioners have considered the Gazprom's case a good law, while some others, including the FIRS, have considered it a bad law.[46] Those, who saw it as a good law, expressed the view that it was a vindication of the literal rule and that the case had settled the position on the VAT treatment of supplies by non-resident companies. According to a source:

> This decision puts to rest the question of whether under the VAT legislation, a Nigerian company receiving services from a foreign company outside Nigeria is required to account for or pay any VAT to the FIRS on the fees payable for the services received. The broader implication of this decision is that it emphasizes the age-long principle of interpretation of tax laws. Where the tax law is clear it must always be interpreted literarily and if ambiguous, and imposes a burden, then it should be interpreted strictly against the tax authority.[47]

About eight months after the decision in Gazprom, the TAT, Lagos Zone, was presented with facts, which are similar to those of Gazprom's case in the case of *Vodacom v FIRS*(Vodacom's Case). Vodacom is a company registered in Nigeria and carrying on business in Nigeria. Vodacom had entered into a contract for the supply of bandwidth with New Skies Satellites (NSS), a company based in the Netherlands, with no subsidiary or affiliate in Nigeria. NSS supplied Vodacom with bandwidth, as per the terms of the contract, which Vodacom paid for, without remitting VAT on the transaction. The FIRS assessed Vodacom to VAT on the transaction, which Vodacom subsequently challenged on the grounds that NSS was a non-resident company and did not carry on its business in Nigeria and also that, since the supply was not made in Nigeria, it was a service rendered outside Nigeria that, therefore, could not be assessed VAT. It argued that NSS was not registered with the FIRS for the purpose of

remitting VAT, as provided under the VAT Act, and that, therefore, it could not be assessed to pay VAT. It relied on the decision in GAZPROM v FIRS.

The FIRS, on the other hand, argued that the facts that NSS was not resident in Nigeria did not hold water because it was the transaction, and not the supplier that was taxable. Since the bandwidth capacities were received in Nigeria through earth-based stations set up in Nigeria by the Appellant to receive them, they were effectively imported into Nigeria and subject to VAT, in line with the destination principle. The relevant provision was Section 2 of the Act, and not section 10, which it termed a mere administrative provision.

It was held that a Nigerian company, to whom a non-resident company made a supply, was obligated to account for VAT, irrespective of whether the non-resident company (i) carried on business in Nigeria, (ii) had registered and (iii) invoiced for VAT. The Tribunal held that Section 10 could not be interpreted in isolation of section 2 but must be read together with it. Section 2 VATA, being the charging clause, imposed tax on goods and services but that the provision of section 10 VATA did not, on its own, impose VAT on a non-resident company. The decision in *Gazprom* did not take into consideration the import of section 2 of the VATA and was, therefore, decided *per in curiam*.

The apparent confusion, created by the forgoing decisions of two different zones of the TAT, implies that none of the decisions is superior to each other until a superior court of record, in this case, the Federal High Court[48], rules on the matter, if and when one of the cases comes on appeal. It will be recalled that the TAT itself is a beneficiary of conflicting decisions of the Federal High Court on the constitutionality of the TAT. It would appear, anyway, that the hand of the FIRS seems to be strengthened, as it continues to apply what it has always believed to be the correct position.

The bottom line of Vodacom's case is that supply of services by a non-resident supplier, who does not carry on business in Nigeria, is liable to VAT. The Nigerian customer, to whom the supply is made, is liable to withhold and account for VAT, whether, or not, the foreign supplier has invoiced for VAT. This will, inexorably, increase the cost of importation by 5%. Nigerian businesses, that are importing good and services, should take note of this development and appropriately guide the foreign supplier(s), who may not be aware of the VAT regime.

The TAT, Lagos Zone, is not bound by the decision of the Abuja Zone in *Gazprom*, being a Tribunal of co-ordinate jurisdiction. The TAT, Lagos Zone, did not just depart from *Gazprom* but rightly articulated why it was unable to apply the reasoning. The ratio is that Section 2 of the VAT Act, being the charging clause, is the centre of gravity, on which all other provisions revolve, and that section 10 does not extend the scope of exemption beyond that provided in section 2 and the First Schedule. *Gazprom* would have encouraged capital flight, as more taxpayers may have incentives to import goods, which may, otherwise, be sourced locally. It appears that the focal point of sections 2 and 10 is the Nigerian "consumer" of imported

goods and services, and not the non-resident supplier, who is clearly out of the reach of the tax authority.

The seeming confusion, created by the forgoing decisions of the TAT, has now been put to rest by the Federal High Court in the appeal, filed by the FIRS against the decision of the TAT in the Gazprom matter. At the Federal High Court, it was held, *inter alia,* that, where a non-resident company provides services to a Nigerian company on an agreed consideration or fees payable by the Nigerian company, then the non-resident company is deemed to carry on business in Nigeria. In addition, the court stated that the term "carrying in business in Nigeria" is not limited to the physical presence of the non-resident company.

It seems incorrect to say that the decision of the Tax Appeal Tribunal has resolved any issue with finality, considering that it is an inferior Tribunal. Therefore, any party, who is aggrieved with the decision of the TAT, should leverage on the provisions of Paragraph 17 of the Fifth Schedule to the FIRS Act, which gives "any person dissatisfied with the decision of the Tribunal the right to appeal within 30 days." Further appeal could be made to the Court of Appeal and the Supreme Court. Until the Supreme Court has ruled on a matter, it cannot be said to be final. Where a party is convinced about the correctness of its position, there are few cases where such a party may want to litigate the matter up to the Supreme Court, notwithstanding the cost. Where the taxpayer succeeds, the FIRS may consider allowing the cost of litigation and, ultimately, amend the relevant tax laws to accommodate such a deduction.

5. Conclusion

Since 1993, the Value Added Tax has become a significant source of revenue to all levels of governments in Nigeria. Considering the dynamic nature of taxation, it is important to keep abreast of developments from time to time to determine the current policy and law on a particular issue. The coverage of review in this chapter is limited to 2013 till date. One may easily fall into the error of thinking that there have not been any significant developments in the VAT in Nigeria since the 2007 Amendment of the VAT Act if the focus were to be on the statutory framework.

There have also been conflicting decisions of the Federal High Courts, Sokoto and Lagos Divisions, on whether bottled water is subject to VAT, and between the Abuja and Lagos Zones of the Tax Appeal Tribunal on the liability of a non-resident company to VAT in Nigeria. The chapter notes that these developments have introduced some measure of uncertainties in the policy and law on VAT in Nigeria and calls on the Federal Government to harmonise, clearly articulate and streamline the policy and legal frameworks.

A review of the case laws, however, reveals a pocket of significant developments, which exhibit or affirm the unique features of the Nigerian VAT system. These include the decision of the Supreme Court, dismissing the case of Lagos State Government, which challenged the constitutionality of the VAT Act, on the technical point that Lagos State should not have

instituted the case at the Supreme Court, being on a case "between the State and a Federal Government agency", and not between "the State and the Federation."

6. Recommendations

A review of the *Value Added Tax Act (Exemption of Commissions on Stock Exchange Transactions) Order 2014,* which granted a five-year exemption on four types of commissions relating to shares and stocks, has since expired. This leaves a gap in the policy and legal basis for the exemption of the transactions from VAT unaddressed. It is recommended that the major tax concerns of the operators on the capital market can only be addressed with an amendment of the VAT Act.

Since the National Tax Policy provides for a periodic review of tax law within a period of three years, time may be ripe for a review of the VAT Act, which was last amended in 2007.

ENDNOTES

1. After several years at more than $100 per barrel, the price of oil has cratered, falling to under $35, and few analysts expect the price to rise sharply this year. Though the fall in oil prices is caused mostly by factors beyond Nigeria's control, it has had a major impact on Nigeria's economy, and has sent the government of President Muhammadu Buhari scrambling to respond. "Impact of fall in oil price is, to put it mildly, catastrophic," said Bismarck Rewane, chief executive of Lagos-based advisory firm, Financial DeriVATives Company. See "Budget Woes Hit Nigeria Amid Oil Price Crash." Available online at http://www.voanews.com/content/rocky-year-ahead-for-nigeria-amid-oil-price-crash/3183020.html. Site visited on 7th June, 2016.
2. See Bailout: CBN Injects N338bn in 27 States to Stimulate Economy. Available online at http://www.thisdaylive.com/articles/bailout-cbn-injects-n338bn-in-27-states-to-stimulate-economy/218955/ Site visited on 20th February, 2016.
3. Abiola Sanni, "True Federalism: A Panacea to the Economic Crisis In Nigeria", (Lagos, ASCO Publishers, 2016) a Lecture delivered as a Guest Speaker at the 7th Prince Bola Ajibola Annual Lecture Series, organised by Magna Curia Chambers of the Obafemi Awolowo University on 25th February.
4. Decree No. 104 of 1993 (Now Value Added Tax Act, Cap V1, Laws of Federation, 2004.
5. No. 12 of 2007, which commenced on 27th May, 2007.
6. See generally A Sanni, 'Value Added Tax in Nigeria", Indirect Taxes in Nigeria, ed. A. Sanni& A. Elebiju, Chartered Institute of Taxation of Nigeria, 2014, pp. 64-108.
7. See A.S. Hornby, Oxford Advanced Learner's Dictionary, International Student's Edition, Oxford University Press, 2010, p.1226.
8. ibid
9. See Compendium of Tax and Related Laws, Compiled by Federal Inland Revenue Service, 2012, p.699.
10. See the "Introduction", at p.700.
11. See especially paras 1.4 and 1.7 on Rational for and Purpose of the Policy and Objectives of the Nigerian Tax System, respectively.
12. At p. 702.
13. See section 4 of the VAT Act. The rate is as high as 85 percent on some goods and services in Kenya and Malawi. The rate is 17.5 percent in Ghana and 18 percent in Benin, respectively. See. J.K. Naiyeju, op. cit., p. 18.
14. The Managing Director, IMF, Christine Lagarde, on the third day of her four-day working visit to Nigeria, during an interactive session with members of the Senate at the National Assembly complex in Abuja, urged the Federal Government to broaden the tax base and reduce leakages by improving compliance, enhance collection efficiency, and at the same time, bolster public finances to further meet the huge expenditure needs. She said since the nation had the advantage of a huge population, increasing the VAT rate would enable it to earn more revenue for developmental projects and service its foreign debts. She said, "For example, the current VAT rate is among the lowest in the world and well below the rates in other ECOWAS member states. So, some increase shouldbe considered." See "IMF wants flexible exchange rate, higher VAT for Nigeria". Available online at http://businessnews.com.ng/2016/01/08/imf-wants-flexible-exchange-rate-higher-

VAT-for-nigeria/. Site visited on 6th June, 2016.

15. The only reference to VAT in the 2016 Budget Speech was where the President stated: "In 2016, oil related revenues are expected to contribute N820 billion. Non-oil revenues, comprising Company Income Tax (CIT), Value Added Tax (VAT), Customs and Excise duties, and Federation Account levies, will contribute N1.45 trillion. Finally, by enforcing strict compliance with the Fiscal Responsibility Act, 2007 and public expenditure reforms in all MDAs, we have projected up to N1.51 trillion from independent revenues" See para 8.
16. See "FG: We will NOT increase VAT, other taxes". Available online at https://www.thecable.ng/fg-rules-out-tax-increase-targets. Site visited on 6th June, 2016.
17. See "5% Value Added Tax too low – Osinbajo". Available online at http://www.punchng.com/5-value-added-tax-too-low-osinbajo/. Site visited on 6th June, 2016.
18. On 11th May, 2016, the Federal Government removed subsidy from the sale of Premium Motor Spirit, PMS, also known as petrol, with immediate effect. It, however, added that a benchmark of N145 per litre, as a recommended pump price, at which any trader, irrespective of the source of foreign exchange used to import cargo, is guaranteed adequate profit. This development sparked a strike by a faction of the Nigerian Labour Congress, which lasted about three days. See "Petrol price hike: Labour plans nationwide total strike". Available online at https://www.google.com.ng/#q=strike+over+deregulation+of+fuel+price+in+nigeria. Site visited on 6th June, 2016.
19. The National Assembly, when passing the Value Added Tax (Amendment) Act 2007 into law, rejected the proposed increase from 5% to 10%. An attempt by the Executive to increase the tax rate through a Ministerial Order soon thereafter was not successful. See "Notice of Increase In VAT Rate To 10% And Other New Tax Related Regulations",The Punch Newspaper of Wednesday,23rdMay, 2007, at p.18. By virtue of Section 34 of the Finance Act, 2019 amended Section 4 of the VAT Act and consequently increased the VAT rate from 5% to 7.5%.
20. VAT was introduced on 24th August, 1993.
21. Decree No. 104 of 1993 (Now Value Added Tax Act, Cap V1, Laws of Federation, 2004.
22. See Finance (Miscellaneous Taxation Provisions) Decree No. 21 of 1991; Finance (Miscellaneous Taxation Provisions) Decree No. 63 of 1991;Finance (Miscellaneous Taxation Provisions) Decree No.31 of 1993; Finance (Miscellaneous Taxation Provisions) Decree No. 30 of 1996;Finance (Miscellaneous Taxation Provisions) Decree No. 31 of 1996;Finance (Miscellaneous Taxation Provisions) Decree No. 32 of 1996; Finance (Miscellaneous Taxation Provisions) Decree No. 18 of 1998; Finance (Miscellaneous Taxation Provisions) Decree No. 19 of 1998; Finance (Miscellaneous Taxation Provisions) Decree No. 21 of 1998 Finance (Miscellaneous Taxation Provisions) Decree No. 40 of 1998; andFinance (Miscellaneous Taxation Provisions) Decree No.30 of 1999.
23. No. 12 of 2007, which commenced on 27th May, 2007.
24. See, generally, B.B. Kanyip, "Companies Income Tax",CITN Nigerian Tax Guide, pp. 176-8.
25. Ibid., p.353.

26. Cap C23, LFN 2004.
27. Vol. 9 All NTC, 331.
28. Such as AG AbiaState v. AG Federation [2002] 6 NWLR (Pt. 763) 264, wherein the plaintiff Attorneys General of all the 36 States challenged the constitutionality of certain provisions of the Electoral Act, enacted by the National Assembly in 2001; A.G. Abia State & 35 Ors v. AG Federation [2006] 16 NWLR (Pt. 1005) 265, wherein the plaintiff Attorneys General of Abia, Delta and Lagos States challenged the constitutionality of the Monitoring of Revenue Allocation to Local Governments Act, passed by the National Assembly in 2005; and A.G. Lagos v. A.G. Federation & 35 Ors [2003] 12 NWLR (Pt. 833) 1, wherein the plaintiff Attorney General of Lagos State challenged the constitutionality of the nationwide application of the Nigerian Urban and Regional Planning Decree No. 88 of 1992.
29. Chuka Ikuwasom, "SC/20/2008 – A.G. LAGOS STATE V. A.G. FEDERATION & 35 ORS: Through the Eye of a Needle". Unpublished Position Paper Prepared for the Chartered Institute of Taxation of Nigeria, 2015.
30. I do not share the view that "Federation" and "the Federal Government" mean the same thing. In my view, the Federal Government refers to the entire machinery of government (the three arms) of the government at the centre, while federation refers to the aggregation of the states and the federal government. This can be garnered from the provisions of section 2(2) of the Constitution of the Federal Republic of Nigeria that Nigeria shall be a federation consisting of States and the Federal Government. Also, section 318 of the 1999 Constitution separately defines "federation" to mean the Federal Republic of Nigeria."
31. To parody the statement of Mark Anthony in Julius Caesar: Act 3, Scene 2, page 4: "Friends, Romans, countrymen, lend me your ears. I have come here to bury Caesar, not to praise him…"
32. Supra.
33. Under the law of contract, whether an article e.g. cloth, food, shelter is a necessary or not is a question of mixed law and fact. The preliminary question whether an article is capable of being a necessary is one to be decided by a judge. If the judge decides that the article is capable of being a necessary it is question of fact whether it a necessary in the particular circumstances. This process involves a consideration of the status of the infant in life, whether he already has an adequate supply of the articles and so on. See Chapple v. Cooper (1844) 13 M & W 253, Peters v Flemming (1840) 6 M & W 42.
34. such as garri (a staple cassava food in Nigeria)
35. See A. Sanni, ---- Supra note --, p.???
36. --ALL NTC, p. --???
37. Supra.
38. FHC/L/CS/157/2015.
39. Water i.e. natural water and table water e.g. spring water, rain water, pipe borne water, well water and all natural water of the same kind, all table water other than sparkling water and flavoured water are now clearly exempted in the VAT Act.
40. Supra, note -- at p.798.
41. At p. 580.
42. Oxford Advanced Learner's Dictionary, 8th Edition, p. 1678.
43. These parties maintained these opposing positions in the case considered below.
44.

45. Recently, the Federal High Court, in an appeal by the FIRS, set aside the decision of the TAT on the matter.
46. For instance, the members of the Indirect Tax Faculty of Chartered Institute of Taxation of Nigeria (CITN), comprising about 15 Chartered Tax Practitioners, were sharply divided when Gazpom's and Vodacom's cases were being discussed.
47. See "PwC secures a landmark TAT decision in a VAT case on imported Services." Available online at http://pwcnigeria.typepad.com/tax_matters_nigeria/2015/06/pwc-secures-a-landmark-tat-decision-in-a-VAT-case-on-imported-services.html. Site visited on 6th June, 2016.
48. See note 46.

CHAPTER 5

ACCOUNTING TREATMENT OF VALUE ADDED TAX TRANSACTIONS

Abstract

A key component of any efficient tax administration is the establishment of proper accounting that provides a reasonable assurance that the financial statements have been prepared in accordance with generally accepted accounting principles. The regulation of financial reporting is a major concern to large businesses, government and the revenue authority, and much effort is required to ensure that sound accounting systems are put in place. However, one area that has possibly been overlooked is the compliance with Valued Added Tax (VAT) processing within the financial systems. This chapter, therefore, seeks to stimulate debate on the accounting treatment for VAT transactions in order to facilitate its understanding and proper application through the various levels of the value chain. The chapter provides a theoretical framework for exploring VAT and its relationship with the business enterprise and the tax authority. VAT cases were cited to demonstrate VAT accounting entries and mechanism for VAT operations. The chapter also discusses the significance of tax accounting and its implications for tax revenue sustainability and revenue governance in Nigeria. The chapter suggests reforms in order to minimise the attendant problems created by lack of proper accounting, transparency and accountability in VAT administration in Nigeria.

1. Introduction

The reform of tax system through the introduction of VAT is the major fiscal innovation of the century (see Ola, 2001[1]). VAT is a popular tax worldwide[2], as it is usually easy to compute, collect and generally[3]. In common with other countries in Sub-Sahara Africa, VAT was introduced in Nigeria through Decree No. 104 of 1993[4] (see Sanni, 2014[5]). VAT is a major source of tax revenue, and companies collect this for the state. Technically, VAT is a tax on the consumer, not on the company, in the same way as sales taxes are in the US and other countries. Companies charge VAT on their customers and are themselves charged VAT on their purchases. However, a corporation separates out VAT received from customers and VAT paid to suppliers in its accounting and every month pays the difference between the output VAT and allowable input VAT.

In recent years, there has been a considerable increase in the volume of research and scholarship on the issue of indirect taxes, particularly Value Added Tax[6]. This literature is informed by a variety of theoretical perspectives, which seek to address issues about governance, policy shift, legal and administrative concerns[7]. While there is considerable research on a number of aspects, broader accounts of the accounting process and procedures

of VAT, as impediment to tax compliance and tax revenue sustainability in developing countries, are scarce, despite the fact that accounting techniques give visibility to the objects of taxation and help to regulate them. Thus, there is scant literature on the accounting treatment for VAT transactions because it is too often overlooked in the compliance of VAT processing within financial systems[8]. This chapter, therefore, seeks to stimulate debate on accounting for VAT Transactions in order to promote its understanding and appropriate application through the various levels of the value chain.

The rest of this chapter is divided as follows. Section Two provides the theoretical background, explaining VAT and its relationship with the business enterprise culture. It is argued that the tax policy and proper accounting treatment are key to non-violation of the tax law and the enhancement of efficient and effective tax administration. Section Three focuses on Records and Accounts, while Section Four dwells on the Administration of VAT. Section Five provides extracts from a number of VAT cases to demonstrate VAT accounting entries and the mechanism for VAT operations. Section Six highlights the implication of the adoption of International Financial Reporting Standards in VAT treatment. Section Seven discusses the significance of VAT accounting and its implications for Economic and Tax Revenue Sustainability. The final section, Section Eight, concludes the chapter and suggests reforms in order to minimise the attendant problems created by lack of proper accounting, transparency and accountability.

It might be useful to explain that there are three possible systems of Value Added Tax: the multi-stage, the credit mechanism and the invoice tax systems. These systems, though different, complement one another in conceptualising how the VAT system operates and the treatment of the relationship between the various stakeholders within the production chain.

2. Concept of Value Added Tax

VAT is imposed at every stage of the production chain from the Manufacturer to the Consumer (i.e., it is a multi-stage tax system). In order to eliminate the cascading effect of taxation at every stage of production, a credit mechanism system is installed to allow VAT paid on imports or purchases of raw materials (INPUT TAXES) to be deducted from the VAT charged on sales (OUTPUT TAXES) and, therefore, the tax to be paid by a taxable firm is the difference between output tax and input tax. In this connection, the Federal Inland Revenue Service notes that:

> This credit mechanism acts as a safeguard against the negative impact of the tax so that VAT is made neutral to price determination (VAT is not an element in the price). The credit mechanism also helps VAT to promote export drive in view of its neutral characteristic to international trade. In export trade, the total input taxes incurred on production is refundable.[9]

In other words, Value Added Tax is added to sales by businesses selling goods and services. When businesses purchase goods and services, they have to pay VAT. They must then remit the difference between the VAT they recover from customers and the VAT they pay their

suppliers to the tax authorities. As a transaction, the receipts (from sales) equal the payments (to suppliers and to the tax authorities) and, hence, these are not shown in the Statement of Comprehensive Income, although the unremitted liability to the taxation authorities appears in the Statement of Financial Position as a current liability. Collier notes that, in retail businesses, where VAT is more complex (as some retail transactions are exempt from VAT), the VAT-inclusive and VAT-exclusive turnover may both be shown in the Statement of Comprehensive Income[10]. VAT is essentially a tax on consumers collected by traders and is accounted for in a similar way to pay as you earn (PAYE) income tax, which is a tax on employees collected by employers. According to Statement of Standard Accounting Practice (SSAP) 5, Accounting for Value Added Tax:

> As a general principle, the treatment of VAT in the accounts of a trader should reflect his role as a collector of the tax and VAT should not be included in income or in expenditure whether of a capital or revenue nature. There will, however, be circumstances in which a trader will bear the VAT, and in such cases where the VAT is irrecoverable, it should be included in the cost of the items reported in the financial statements[11].

The concepts underlying VAT is that the tax is paid by the ultimate consumer of the goods and services but that everyone in the supply chain must account for, and settle, the net amount of VAT they have received in the VAT tax period[12]. In other words, it will not be regarded as business expenses, on which relief could be claimed under the personal or corporate income tax. According to Porter (1985), every business is:

> A collection of activities that are performed to design, produce, market, deliver, and support its product … a firm's value chain and the way it performs individual activities are a reflection of its history, its strategy, its approach to implementing its strategy, and the underlying economics of the activities themselves[13].

Therefore, value chain, as a collection of inter-related business processes, is a useful concept to understand businesses that produce either goods or services. Each element of the value chain contributes to the price a customer is willing to pay, but also attracts costs. A VAT could either qualify as input VAT, which can be deducted from output VAT or it could be regarded as sunk cost and no tax relief could be obtained[14]. Revenue excludes amount collected on behalf of third parties, for example, a value added tax or where the entity acts as an agent[15]. IAS 18 (paragraph 8) makes clear that the same principles are followed:

> Revenue includes only the gross inflows of economic benefits received and receivable by the enterprise on its own account. Amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes are not economic benefits which flow to the enterprise and do not result in increase in equity. Therefore, they are excluded from revenue.[16]

In theory, the amount received in stages by the relevant authority[17] will equal the amount of VAT paid by the ultimate consumer in the final stage of the supply chain. The effects of the standard vary, depending on the status of the accounting entity under the tax legislation. As noted in the FIRS Information Circular No, 9304, the input-output tax mechanism in VAT also makes it self-policing:

> In essence, it is the **Output tax less Input Tax** that constitutes the **VAT payable.** It is the equivalent of the VAT paid by the final consumer of the product that will be collected by the government. Although VAT is a multiple stage tax, it has a single effect and does not add more than the specified rate to the consumer price no matter the number of stages at which the tax is paid.[18]

VAT is chargeable at each stage of the distribution chain. The chargeable persons at each state are not the sufferers of VAT, they are mere agents of government. The totality of the VAT is borne by the final consumers of taxable goods and services[19], as demonstrated in Table 1 below:

Table 1. VAT Concept and Collection Procedure

Stage 1			
Raw Material Supplier		VAT[20]	Gross Amount
Selling Price	100,000.00	7,500.00	107,500.00
Cost	(Nil)	(Nil)	(Nil)
Value Added	100,000.00	7,500.00	
VAT Returns			
Output VAT		7,500.00	
Input VAT		(Nil)	
VAT payable		7,500.00	
Stage 2			
Manufacturer		VAT	Gross Amount
Selling Price	200,000.00	15000.00	215,000.00
Cost	100,000.00	7,500.00	107,500.00
Value Added	100,000.00	7,500.00	
VAT Returns			
Output VAT		15,000.00	
Input VAT		(7,500.00)	
VAT payable		7,500.00	
Stage 3			
Wholesaler		VAT	Gross Amount
Selling Price	250,000.00	18,750.00	268,750.00
Cost	200,000.00	15,000.00	215,000.00
Value Added	50,000.00	3,750.00	
VAT Returns			
Output VAT		18,750.00	
Input VAT		(15,000.00)	
VAT payable		3,750.00	
Stage 4			
Retailer		VAT	Gross Amount
Selling Price	375,000.00	28,125.00	403,125.00
Cost	250,000.00	18,750.00	268,750.00
Value Added	125,000.00	9,275.00	
Stage 5			
Consumers		VAT	Gross Amount
Selling Price	375,000.00	28,125.00	403,125.00

VAT History Selling	Value Added	VAT@ 7.5%	Cost	Price
Raw Mat. Supplier	Nil	100,000	100,000	7,500
Manufacturer	100,000	200,000	100,000	7,500
Wholesaler	200,000	250,000	50,000	3,750
Retailer	250,000	375,000	125,000	9,375
			375,000	28,125

Source: Adapted from Ola C. S. (2001), pp. 602-604.

The VATD, 1993 is silent on the word "Final Consumer" or its definition. Generally, VAT is borne by a person who is at the terminal end of the distribution chain. In this case the final consumer pays ₦28,125 VAT on the gross sales value of N375,000.

Registered Traders

Most VAT regimes require registered (taxable) persons to file returns (and remit tax). Registration is part of a self-assessment VAT system that typically is reinforced with civil and criminal penalties for non-compliance[21]. Taxable persons are obliged to keep such records and books of all transactions, operations, imports and other activities relating to taxable goods and services, as are sufficient to determine the correct amount of tax due. Many VAT systems describe a taxable person, subject to the VAT rules, as a person who is registered or is required to register. A taxable person is defined as:

> a person who independently carries out in any place an economic activity as a producer, wholesale trader, supplier of services(including mining and other related activities) or person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business and includes public authority acting in that capacity)[23].

In most other jurisdictions, a firm (taxable person) is required to register, if it makes or expects to make, at least, the statutory minimum level of annual taxable sales in connection with the business or economic activity[24]. Up to the end of 2019, as Hamzaoui notes that:

> The Nigerian law does not specify any revenue threshold for registration purposes. **'A resident person is required to register for VAT not longer than 6 months after starting business'**[25].

In common with other jurisdiction, the new Finance Act, 2019 introduced VAT compliance threshold. The threshold exempt companies with an annual turnover of ₦25,000,000 or less from registering for the VAT, charging the tax (VAT), rendering a monthly return of its sales and purchases and from the penalties prescribed by the Act for non-compliance with the administrative provisions[26]. However, the implication of the above provision is that such businesses will be unable to recover input VAT incurred on their purchases, especially those involved in the supply of VATable products.

The registration requirement generally is imposed on a person or firm that makes a taxable sale. But a non-resident, without a fixed location in the country, may be subject to a different set of rules. VAT is also payable by non-resident individuals and companies in Nigeria, if the individuals and non-resident companies deal in Taxable goods and services[27]. This will, however, be paid by that resident individual or company through whom the non-resident individual or company conducts business in Nigeria. This was further expanded in the new s.10 (2) to (4) of VATA CAP VI as amended[28] that:

> (2) the Service may, by notice, determine and direct the companies operating in the oil and gas sector which shall deduct VAT at source and remit same to the service.
> (3) a non-resident company shall include the tax on its invoice for the supply of taxable services
> (4) the person to whom the services are supplied in Nigeria shall withhold and remit the tax directly to the service in the currency of payment

Therefore, for a registered trader, accounts should only include figures net of VAT. It should be noted that VAT on the sales will be deducted from the invoice amount. The VAT will be payable to the government and the net amount of the sales invoice will appear in the statement of comprehensive income in arriving at the sales turnover figure. According to IAS 18:

> The turnover to be subjected to tax treatment under loyalty program shall be the payments made for both the consumed and deferred portion of the services. Revenue shall be recognized for tax purposes at the point of realization. VAT will be charged on total invoice value, whether consumed or deferred.[29]

The VAT on purchases will be deducted from the purchases invoice. The VAT will then be reclaimed from the government and the net amount of the purchases invoice will appear in the statement of comprehensive income in arriving at the purchases figure. The only exception to the use of amounts, net of VAT, is when the input tax is not recoverable.[30] How VAT appears in the ledger accounts and in the financial statements depends on the following categories businesses fall into:

Non-registered or Exempt Trader

If a sale of a particular good or services is exempt under the credit-invoice VAT or the Japanese CT variant, the sale is not taxed and the seller is denied an input credit for the tax paid on purchases used in the exempt activity.[31] Hence, such businesses are exempted from accounting for VAT. They do not add VAT to the amount at which they sell their products or supply their services, nor do they get a refund of the VAT they themselves paid on goods and services bought by them. For a company that is classified as non-registered or exempt, the VAT that it has to pay on its purchases and expenses is not reclaimable from the government. Because the company cannot recover the VAT, the expense that appears in the statement of comprehensive income must be inclusive of the VAT. It is treated as part of each item of

expenditure and the cost treated accordingly. It will be included, where relevant, with each item of expense (including capital expenditure), rather than being shown as a separate item.[32] Schenk and Oldman further note that the grant of exemption for domestic sales subsequently increases the administrative and compliance costs of a VAT, especially if a business makes both taxable and exempt sales[33].

Partially Exempt Trader

Partial exemption status is accorded to those businesses, which deal in both exempt and taxable (zero-rated[34] and standard) supplies[35]. An entity that is partially exempt can only recover a proportion of input VAT, and the proportion of non-recoverable VAT should be treated as part of the costs on the same lines as with an exempt trader. The VAT rules are complex, but for the purpose of understanding the figures that appear in the published accounts of public companies, treatment as a registered trader would normally apply[36]. Under the credit-invoice VAT, a seller of a zero-rated item does not charge VAT on sale. The sale is classified as a taxable sale, subject to zero rate. As such, the seller is entitled to recover, as an input credit, the tax included in the cost of taxable purchases, attributable to that sale. Under a sales-subtraction VAT, zero rating is accomplished by excluding the
designated sales from gross receipts and allowing the business to deduct taxed purchases attributable to these zero-rated sales[37].

Methods of Calculating Value Added Tax Liability

The special feature of modern value added tax is the mode of collection. This section discusses the widely used European-style, credit-invoice VAT, the Japanese-style credit-subtraction VAT that does not rely on invoices, and the addition-method VAT, not used at the national level. There are three methods of calculating Value Added Tax. These are: the credit method, the subtraction method, and the additional method[38].

a. Credit-Invoice VAT

The most prevalent method of calculating VAT worldwide is the credit-invoice VAT (or invoice VAT) that relies on a tax-against-a-tax methodology. This form of VAT was established after World War II in Western European countries. In this connection, James notes that:

> The consensus within the conventional approach is to levy the VAT through the invoice-credit mechanism. It is the collection mechanism that distinguishes the VAT from other consumption taxes, including its main competitor[39].

Under the ***credit method***, two stages of VAT calculation are done as Output VAT and Input VAT. These are calculated separately, and the Input VAT is subtracted from the Output VAT to get the VAT payable to the Revenue. This is the system that is prevailing in Nigeria and some European countries. This method or mechanism requires each entity to charge VAT on all taxable supplies and provide the purchaser with an invoice, showing the amount of VAT charged. If the purchaser is a registered entity, the VAT, charged or incurred on their

purchases, can be credited/deducted against the VAT charged on their supplies. The registered entities submit tax returns for a tax period (which is monthly in Nigeria). The net tax liability for the tax period will be the difference between the output tax charged on taxable sales and the input tax credit available for the tax paid on inputs/purchases. James further notes that:

> Timing rules are necessary to assign sales and purchases to a relevant 'tax period'. The timing rule and the valuation rules are also necessary to identify the value of consideration of the goods and services supplied[41].

If a registered entity receives more VAT than it pays, then it remits the difference (between the VAT Charged and VAT paid) to the revenue authorities. If the entity pays more VAT than it receives (for example, if an entity is an exporter), then the entity is entitled to a refund.

The Finance Act, 2019 provides clarification that VAT should be accounted for on cash rather than accrual basis[42]. Accounting for VAT on cash basis means that a taxpayer can only recover input VAT that has been "paid" against output VAT that has been "collected". For taxpayers who do not have input VAT to claim, it is only VAT that has been collected that should be remitted to the FIRS. The amendment would help manage taxpayers' cashflows and reduce the risk that a business ultimately bears the VAT burden for its customers, particularly in cases of bad debt. A taxpayer who is entitled to a VAT refund is required to first recover its overpayment as a credit against subsequent VAT collections. Any excess over and above the amount credited against VAT collections would then be refunded. Therefore, the administrative cost to businesses for making refund claims shall reduce significantly.

b. Sales-Subtraction VAT

The ***subtraction method*** calculates net VAT liability by multiplying the tax rate by the base. The base is the difference between total sales, less total taxable purchases from other firms. This, according to Obatola, involves:

> the subtraction of the total value of purchases from the total turnover or sales to arrive at the net sales. The figure obtained is then multiplied by the Value Added Tax rate to get the Value Added Tax payable to the Revenue Service. It is a system that is in use in Japan[43].

The VAT liability for each period is the product of the tax base, multiplied by the VAT rate. Like an additional VAT, the sales-subtraction VAT is a period tax, based on cumulative data for each period, not a tax imposed on individual transactions. The seller must price taxable goods and services, inclusive of VAT. These VAT inclusive data are used to calculate periodic VAT liabilities. This method of calculating tax liability makes it difficult to impose more than one rate of VAT on taxable goods or services[44]. This is the method mostly applicable in Nigeria.

c. Addition-Method VAT

The addition-method VAT requires a taxable firm to calculate tax liability for each tax period

by adding the firm's economic factors of production for the period (wages, rent, interest, expense and profit for VAT purposes) and multiplying the total by the tax rate[45]. Schenk *et al.* note that, like the accounts-based sales subtraction VAT (also a period tax), an addition VAT must be imposed at one rate because 'company accounts' do not usually divide sales by different product categories, coinciding with different sales tax rate, and ….they certainly never divide inputs by differential tax liabilities[46]. As van Brederode notes:

> The addition method cannot accommodate multiple rate because company accounts do not distinguish different product categories within their sales that coincide with different sales tax rate, nor do they divide inputs by different tax liabilities[47].

It is further noted that, if the 'profit' portion of the addition-method VAT base is taken from data prepared for income tax purposes, this method of calculating VAT liability may be expected to be an income-based, not consumption-based tax. Because the tax base includes only the value added, as measured by the economic factors of production employed at each stage, revenue lost at a prior stage is not recovered (as under invoice VAT) at the next stage of production or distribution of goods or rendition of services. The addition method has not been adopted as a national tax, except for Isreal's taxation of financial institutions and insurance companies[48] under a tax measured by the sum of the firm's wages and profits. As a period tax, an addition-method VAT probably will be treated as a cost of production and will be included in the pricing structure of taxable goods and services. "Since the VAT liability is not based on the… sales price [of]…goods, it is unlikely that the exact VAT, no more and no less, will be shifted to consumers."[49]

3. Records and Accounts

It has been argued that record-keeping is a burden of VAT, and it is, indeed, a great constraint to the implementation of VAT in Nigeria[50]. Record-keeping is another core and integral function in tax administration. Lack of, or inadequate, records or accounts by businesses, with which to determine accurately the VAT payable, maintenance of more than one VAT Accounts to evade payment of Value Added Tax, and corruption on the part of tax collectors (as some dishonest ones collude with VAT payers to defraud the government) are some of the problems of Value Added Tax administration in Nigeria[51].

Accounting is the mechanism that provides us with reliable financial information. This financial information is used by managers, employees, shareholders, potential purchasers, customers, suppliers, financial institutions, and the revenue authorities. Accounting is an information system that identifies, collects, describes, records and processes data and then communicates it as financial information. The accounting system will vary from one business to another, depending on its nature and size, the volume of transactions and the demands made by its management, but the system's components and the method of processing the information are essentially the same in all accounting systems. In order to be able to provide such financial information for users, particularly to the tax authority, each business must keep an accurate record of its activities on a day-to-day basis, with a high level of transparency[52].

Every 'VATable person'[53] is expected to keep proper records and books of all transactions, operations, imports and other activities relating to taxable goods and services, as are sufficient enough to calculate the amount of VAT payable[54]. These include the cash book, the sales and purchases day books, ledger accounts and the statement of financial position. Specifically, for VAT purposes, tax invoices are to be issued for all supplies and VAT Accounts are also to be kept[55]. The FIRS Information Circular 9304 notes that:

> The VAT account is the summary of the output and input tax in a normal ledger account form. That is, VAT on purchases, VAT attributable to bad debt relief etc. are debited to the account while VAT charged on sales for the month, VAT charged on service, etc., are credited. Where there is a credit balance, VAT payable is remitted through the designated collecting bank. Conversely, a debit balance calls for refund and would be made promptly by the FIRS after necessary verification[56].

For the purpose for accounting for VAT, every registered person shall keep the following records and accounts:

a. The VAT Account

All registered business must account for VAT on all the taxable supplies they make and all taxable goods and services they receive. This includes standard-rated, reduced rate and zero-rated supplies. They must also keep a summary (called a VAT Account) of the total of input tax and output tax and the amount due or refundable for each VAT period. All these must be kept up to date[57]. The VAT account is the summary of the output and input tax in a normal ledger account form. That is, VAT on purchases, VAT attributable to bad debt relief, etc., are debited to the account, while VAT charged on sales for the month, VAT charged on service, etc., are credited. Where there is a credit balance, VAT payable is remitted through the designated collecting bank. Conversely, a debit balance calls for a refund and would be made promptly by the FIRS after necessary verification. In addition, relevant business and accounting records[58] should be maintained, including sales and purchase journals, cash books, ledgers and other subsidiary books of account. In this regard, Sanni notes that

> 'No particular accounting standard is prescribed. Hence, books and records which a taxable person is expected to keep will depend on the nature and size of its business provided that they are 'sufficient to determine the correct amount due'[59].

Given that the tax is collected by traders and businesses on behalf of the government, invoice totals will include the VAT. However, we must ensure that only the net amount (excluding VAT) is entered into the sales, purchases and returns accounts. Banks and Other Financial Institutions[60] are required to adopt the following simple methods of recording their transactions for VAT purposes:

i. When any service is identified as VATable, internal entries are raised by the Bank for the cost of the service, plus 7.5% VAT.
ii. The Bank is expected to debit the account of the customer accordingly with the cost of

the service, plus the 7.5% VAT charged.

iii. Credit the Income account of the Bank or Institution with the income element of the charge, excluding the VAT

iv. Credit the FIRS VAT Account in the particular Bank or Institution with the 7.5% VAT deducted from (ii), to arrive at (iii).

b. The Tax Invoices

Invoice generally means any document issued as evidence of demand for payments. A Tax Invoice is similar in many respects to a normal sales or purchases invoice, except that it has a provision for TIN and VAT payment at the prescribed rate. Every taxable firm has a duty to issue a tax invoice for every single taxable transaction carried out by the business, details of which must be furnished to the nearest tax office of the FIRS within the period prescribed in the Act for the rendition of VAT returns. The tax invoice can be regarded as a commercial invoice, but a commercial invoice cannot be regarded as a Tax Invoice because the document has to satisfy certain requirements in order to qualify as a 'Tax Invoice'.

The above requirements are very essential because they determine the legality of the Tax Invoice. This implies that a credit can be allowed against output tax, only if the invoice satisfies the requirements which are mandatory and are intended to achieve the following:

> To improve the low level of compliance by taxable persons with respect to observance of accounting principles and maintaining of the records of transactions. To enable the Revenue Authority to monitor every trading transaction conducted by the taxable firms, thereby ensuring that the reported monthly sales returns in the books of the seller are in agreement with the monthly returns made by the purchaser[61].

The VAT Act provides specific obligations on taxable persons. The VAT Act states that each taxable person is obliged to issue a Tax Invoice at the time of delivery of a taxable good or service. This means that only a taxable person is obliged to issue a Tax Invoice. It is, therefore, an offence for a taxable person to fail to obtain a TIN as well as fail to issue a tax invoice when it is already confirmed to be doing business. Stiff penalties have been provided in the VAT Act to check these abuses. Section 32 of the VAT Act, as amended, states that:

> The Tax Invoice should be issued at the time of delivery of the taxable goods or services. This emphasises that the tax is due at the time of delivery, and not at the time of payment[62].

An exception to this rule may exist only where payment is received before the deliveries. Therefore, a tax invoice should include a tax invoice issued and received.

Importance of Invoices and Credit Notes

Tax invoices are to be issued for all supplies and VAT accounts are also to be kept. Copies of these invoices need to be retained by the suppliers and the customers also need tax invoices to support their claims for input taxes. In order for VAT-registered traders to claim VAT on

purchases, they must receive proper VAT invoices from their suppliers. It is vital, therefore, that these invoices are properly drawn up and carefully retained. The checking of invoices and credit notes forms a very important part of the periodic examination, which revenue officers may make of a trader's VAT position. The VAT law contains specific requirements for the issue and retention of invoices, credit notes and related documents. Failure to comply with these requirements leaves a trader liable to penalties[63]. Traders who issue invoices and credit notes, and persons to whom these documents are issued, should ensure that the documents accurately represent the transactions to which they refer. Otherwise, this may undermine accurate determination and accounting for the tax payable. Ola observes that the problem with some taxable persons, such as banks, is that they do not normally issue invoices/receipts on their transactions[64]. In this respect, the FIRS also notes that:

> The mode of operation in the Banks does not permit the issuance of tax invoices to customers. The VAT charges therefore have to be reflected in the customers' statements of accounts in order to enhance disclosure and easy verification by tax officers[65].

VAT calculations are expected to be based only on the charges made for services rendered. It should, however, be noted that the focus of VAT is on the charges levied on customers for the consumption of services rendered by Banks[66]. Bank statements, debit or credit advices are normally used to explain their transactions to the customers. Except these documents are re-designed in conformity with the tax invoice requirements, they cannot be used to advise the customers of their VAT position in a tax period. The only viable alternative is to use a debit advice by the bank, though it may be expensive to operate and may involve a lot of paper work.

4. Other VAT Mechanisms

This section provides the illustration of VAT treatments when transactions also suffer withholding tax and how VAT operates within government establishments where contractor engages in bidding for government contracts and private contracts.

VAT and Withholding Tax

VAT is not a substitute for withholding tax. A VATable service may still be liable to the deduction of withholding tax. VAT is a tax on consumption, while withholding tax is an advance payment of tax, which the taxpayer is entitled to deduct from his/her/its actual tax liability. In the case of VAT, the taxpayer is the consumer of VATable supplies, while withholding tax is suffered by the supplier or manufacturer of goods or the person whose service is being paid for. This can be demonstrated, using the case in Table 2 below:

Busola & Co. raises a bill for the tax advisory services rendered to Pen Nigeria Limited. The detail of the bill is as follows:

Table 2. Bill for Tax Advisory Services

	₦	₦
Fee		10,000
Out of pocket expenses: Air fare		
(tax ₦1000 and VAT inclusive ₦279.07)	4,000	
Photocopy	200	
Hotel accommodation		
(VAT inclusive = ₦697.67)	10,000	
Local transportation	1,000	15,200
		25,200

The consideration is whether VAT should be charged on ₦10,000 or ₦25,000. The airfare and hotel accommodation have already suffered VAT. The expenses are passed at cost to Ayo Nigeria Ltd. If photocopy and local transportation are to suffer VAT, it should have been imposed at source. If VAT is chargeable on ₦25,200, then the VAT of ₦976.74, suffered on air ticket and hotel accommodation, should be regarded as input VAT and the net VAT of ₦913.26 (₦1,890-₦976.74) should be paid to the VAT office. Even then, this treatment has not removed the tax implication on photocopying and local transportation. This problem should definitely call for a tax planning. On the other hand, Ayo Nigeria Limited is entitled to make a claim of ₦1,260 input VAT suffered. The effect of charging VAT only on ₦10,000 means the total VAT suffered by Ayo Nigeria Ltd. on which a claim could be made is:

Table 3: VAT Chargeable

	₦	₦
Fee: ₦10,000 @ 7.5%		750.00
VAT on air ticket	297.07	
Hotel accommodation	697.67	
		976.74
		1,726.74

The treatment has removed VAT implication on photocopying and local transportation, which ordinarily could not have been VATed.

Mechanism of VAT Operation in Government Establishments

(a) Where a contractor engages in bidding for Government contracts only

At the point when payment is to be made to the contractor for services rendered, the government agency is expected to withhold the VAT charge initially imposed on itself and remit it to the VAT office nearest to it. The VAT office will issue a receipt to the Government establishment for the amount paid in the name of the contractor, who may ultimately require the receipt to enable him make necessary adjustment when he/she is rendering returns of his/her VAT transactions to the local VAT office. This can be demonstrated, as shown in Table 4 below.

Table 4: VAT Returns for a Contractor dealing only with Government MDAs

		Adjustment	
	₦	₦	₦
Assume a contract value of ₦100,000		100,000	
VAT payable at 7.5% (to be withheld by Govt. and paid directly to the FIRS)		7,500	7,500
		107,500	
Contract purchases	60,000		
VAT at 7.5% (paid by contractor along with his purchases	4,500		4,500
	64,500		
Less: Adjustment for VAT withheld and paid by government agency to			3,000
FIRS quoting receipt number			(7,500)
Net Refund due to contractor			(4,500)

The above case has resulted in an excess payment of ₦4,500 and this amount must be refunded to the contractor on application. VAT collectible on the transaction is ₦3,000, although a total of ₦7,500 had been collected.

(b) Where a contractor engages in bidding for both government and private contracts

In this case, VAT charges on private contracts will be accounted for by the contractor in the normal way, while the VAT on government contract is to be withheld and remitted directly to the VAT office by the government agency. Receipts issued in both cases will reflect the name of the contractor, who would require them to support his/her VAT returns to the local VAT office. Here is another case, as shown in Table 5, to clarify the position.

Table 5: VAT Returns for a contractor dealing with government and private organizations.

	VAT ₦	₦	*Adjustment* ₦
Value of contract A (from government)		100,000	
7.5% VAT (charged by government agency and paid to FIRS)		7,500	7,500
		107,500	
Value of contract B (private)		150,000	
7.5% VAT (charged by contractor and paid to FIRS)		11,250	11,250
		157,500	18,750
Total output VAT collectible			
Deduct			
Contract Purchases on			
- Job A (Govt.)	40,000		
- Job B (private)	20,000		
	60,000		
7.5% VAT (paid by contractor along with his purchase)	4,500		4,500
	64,500		
Net VAT due			14,250
Less: Adjustment for VAT initially withheld and remitted to the FIRS by government agency			7,500
VAT balance now payable			6,750

In this case, an additional VAT liability of ₦6,750 has resulted; this must be remitted by the contractor to the VAT office in the normal way. Finally, it should be emphasised that an important feature of the VAT system is the establishment of a VAT Refund Account, which must operate efficiently to instill confidence in the minds of the public. The adjustments arising from the two cases will be adequately reflected in the VAT Form 002.

5. VAT Accounting Entries

The double-entry system can be modified for the inclusion of VAT with a few simple amendments. It will also need including in day-book entries before these are posted to the ledger account. Given that the tax is collected by traders and businesses on behalf of the government, invoice totals will include the VAT[67]. However, the preparer must ensure that only the net amount (excluding VAT) is entered into the sales, purchases and returns accounts. VAT-related accounting documents are tax invoices, the cash book and the general ledger (VAT Account). For illustrative purpose, let us assume that the following transaction or figures, and to emphasise VAT journal entries, let us assume no withholding taxes apply.

Company A – Seller (VAT-registered) sold to Company B – buyer (VAT-registered) for ₦2,000,000, exclusive of 7.5% VAT, or a total of ₦2,150,000. Company A – seller's purchases amounted to ₦1,000,000, exclusive of 7.5% VAT or a total of ₦1,075,000.

Sales of goods
In the month VAT returns, sales of goods are classified into regular sales, zero-rate and exempt sales, simple accounting entries are as follows:

Regular sales

Dr.: Cash or Account Receivable	₦2,150,000
Cr.: Sales	₦2,000,000
Cr.: Output VAT	₦150,000

Zero-rated or VAT exempt sales

Dr.: Cash or Account Receivable	₦2,000,000.
Cr.: Sales	₦2,000,000.

Please, note that VAT is shown separately through Output VAT in regular sales, VAT is added, while in zero-rate and exempt sales, no Output VAT is imposed.

Purchases of goods or properties and services
The purchase of goods or properties and services is a reciprocal of sale on the part of the seller. It could be with VAT for VATable or without VAT for VAT-exempt or zero-rated transaction.

Purchases

Dr. Expenses or Purchases or Asset Account	₦1,000,000.
Dr. Input VAT	₦75,000.
Cr. Cash or Account Payable	₦1,075,000.

Credit Purchases
Credit purchases are posted to the ledger accounts as follows:
Dr. Purchases account - with the creditor's account.
Dr. VAT account - with VAT on purchases.
Cr. Creditor's account – with full amount owed.

You will notice that there are two entries for the one credit entry. The total of the two debits – the net purchase (without VAT) and the VAT itself – will equal the credit entry – the credit purchases with VAT included (the gross total), which is credited to the supplier's account.

Credit Sales
Credit sales are treated in the same way – credit sales with VAT
Dr. Debtors account – with gross amount.

Cr. Sales account – with net sale (no VAT).
Cr. VAT account – with VAT on sale.

Returns
The same applies to both returns inward and returns outwards:

Returns inwards with VAT

Dr. Returns inwards - with net amount.
Dr. VAT on returns inwards.
Cr. Debtor's – with gross amount.

Returns outwards with VAT

Dr. Creditor's account – with gross amount,
Cr. Returns outwards with net amount.
Cr. VAT on return outwards.

As stated earlier, the selling price of a good will include VAT, which means that part of the business's overall sales revenue will not contribute to the business's profits. The outstanding balance on the VAT account represents what the business owes to the Federal Inland Revenue Service. It represents the VAT collected, less VAT that has been paid and can be offset against the VAT owing. Until the payment is actually made, the amount for VAT owing would appear as a current liability on the statement of financial position. If the balance brought down had been a debit balance, the business could claim back VAT from the FIRS, as it would have paid more for VAT than the business had collected from VAT on sales.

Other items in the VAT account

Non-current assets
VAT is likely to be included on the non-current assets that the business purchases as well as other expenses related to the running of operations. Such businesses will be able to reclaim the VAT paid on the purchase of non-current assets by offsetting it against VAT payable on sales, in the same way that VAT paid on purchases is used.

Where VAT can be reclaimed on purchases of non-current assets:
Dr. Non-current asset account – with the cost of the asset.
Dr. VAT account – with the amount of VAT on the asset.
Cr. Cash book – with the amount paid, including the VAT.

Where VAT cannot be reclaimed on purchases of non-current assets
Dr. Non-current asset account – with the cost and the VAT paid on the asset.
Cr. Cash book – with the amount paid including the VAT.

We can see that whether the VAT can be reclaimed or not, the total of the two debits equals the credit entry.

Cash sales and cash expenses

Especially for small businesses, there may be small amounts that may be entered into the VAT account. VAT collected on cash sales should be treated in the same way as VAT collected from debtors on credit sales. Likewise, VAT that can be reclaimed on expenses (petty cash payments and others) would be debited to the VAT account in the same way as VAT on purchases is accounted for. One complication that may be encountered is where the VAT has already been added in the amount. The problem here is that simply subtracting 7.5% from the total given will not give the correct amount. If this is thought about, then it is obvious – if an amount is increased by adding 7.5% VAT on top of the original total, the new total is higher, and 7.5% of this new, higher total, will not be the same. The correct procedure, usually applied, is to multiply the total figure as follows: VAT total = 7.5/107.5 * Gross total.

VAT and discounts

The trade discounts do not appear in ledger accounts. However, cash discounts (for prompt payment) will appear and the inclusion of VAT in these invoices with discounts will complicate matters. VAT will always be calculated on the assumption that the cash discount is taken – that is the lowest possible total. Even if the payment arrives too late to qualify for the discount, the VAT will be calculated, assuming the discount is taken. The above can be demonstrated by assuming that a business sells goods worth ₦750,000 but allows a trade discount of 20%. A cash discount is offered for prompt payment at a rate of 5%. The invoice total for this sale will be computed thus:

Stage 1 Deduct the trade discount
₦750,000, less 20% equals ₦600,000 (₦750,000 - ₦150,000)

Stage 2 deduct the cash discount
₦600,000, less 5% equals ₦570,000 (₦30,000 being the cash discount).

Stage 3 compute the VAT
₦570,000 x 7.5% equals ₦42,750,

Stage 4 compute the invoice total (adding the VAT on before the cash discount is deducted), that is:
₦600,000 + ₦42,750 = ₦642,750.

If the cash discount is taken, then the debtor would pay ₦642,750, less the ₦30,000, that is, ₦612,750. The trade discount has no effect, as it is not included in the accounting aspect of the sale. A common mistake is to add the VAT on the amount after the cash discount is deducted. It is important to note that the invoice total will be before the cash discount is taken. All the cases discussed above are aimed at promoting transparency, fiscal responsibility and accountability.

6. VAT and the Adoption of International Financial Reporting Standards

On 28th July, 2010, the Nigerian Federal Executive Council accepted the recommendation of the Committee on the Roadmap to the adoption of International Financial Reporting Standards (IFRS) in Nigeria, that it would be in the interest of the Nigerian economy for reporting entities in Nigeria to adopt globally accepted, high-quality accounting standards, by fully adopting the IFRS. This implies that the VAT returns, to be submitted to the FIRS after the adoption of the standards, must be prepared in compliance with standards issued by the IFRS[68]. In line with the above, the FIRS published the guidelines on tax treatments to be given to each of the Standards, especially where, after the adoption, there are deviations from the Nigerian Generally Accepted Accounting Practice[69]. Specific transactions affected by the IFRS adoption are discussed below.

IAS 2 – Inventories

The FIRS notes that, where allowable input VAT is included in the cost of inventories, it shall be disallowed for income tax purposes and treated separately as deductible from the output VAT, as contained in the VAT Act.

IFRS 16 – Leases

The guidelines on finance lease, as described in the FIRS Information Circular No. 2010/01, dated 12th April, 2012, which relates to VAT and WHT, was applicable prior of the amendment to the VAT Act by the Finance Act 2019. The lessor is also required to include VAT on its invoice for the annual lease rentals, collect same from the lessee and remit to the FIRS. However, The Finance Act seeks to expand the definition of "goods" to include 'any intangible product, asset or property over which a person has ownership or rights, or from which he derives benefits, and which can be transferred from one person to another, excluding interest in land". Consequently, the VATability of incorporeal property, such as rights, patents, trademarks, royalty, etc., that was hitherto controversial has now been legislated in favour of the treasury pursuant to Section 46 Finance Act 2019[70].

IAS 18 - Revenue

In the case of deferred consideration, where imputed interest is embedded in sales revenue, the entire value on the invoice will be subjected to tax. However, where the interest element is clearly shown and separated on the invoice, VAT should not apply to the interest portion. It is further noted that the turnover, to be subjected to tax treatment under loyalty programme, shall be the payments made for both the consumed and deferred portion of the services. Revenue shall be recognised for tax purposes at the point of realisation. VAT will be charged on total invoice value, whether consumed or deferred.

IAS 40 - Investment Property (IP)

Prior to the Finance Act 2019, tax implication where the property is rented out as an IP, VAT is payable, except when it is used for residential purposes, e.g., staff quarters (Benefit-In-Kind would be recognised in the computation of Personal Income Tax). The amendment to s. 2 of VAT Act 2004 as amended defines 'good'. This provision clarifies that VAT is chargeable

on: a. goods which include property (tangible or intangible) such as articles of trade, rights in goods or property (e.g. rights in mineral resources, copyrights, trademarks), assets, motor vehicles, oil wells, rigs, aircrafts, ships, buildings, roads, jetties, or any other type of property[71].

IFRS 2 - Share-Based Payment
The cost of the asset, purchases or expense, is the invoice price, upon which VAT Act provisions shall be applicable.

IFRS 7, IFRS 9, IAS 32 and IAS 39 – Financial Instruments
The FIRS shall disregard the effective interest rate used in calculating both the interest income and expense and use the interest rate stated in the contract. VAT shall be applicable on fees and similar charges incurred. Fees and interest income on Financial Instruments (assets), classified as **Loans and Receivables,** shall be recognised for tax purposes immediately they are earned. VAT and WHT shall be applicable to the fees, while only WHT will be applicable to interest income.

7. VAT Accounting and its Implication for Economic and Tax Sustainability

The drop in oil prices, which has led to dwindling revenues for government in Nigeria, has, once again, brought into a sharp focus the need to diversify the source of government revenue away from oil and more toward taxation. The era of absolute dependency on oil is over and the FIRS is now, more than before, looked upon to generate government's revenue through taxation to fund Government's activities and projects. Transparency in modern financial reporting is considered crucial in helping users to understand and reach their own conclusions about businesses. As Billings and Capie note:

> The volume of information available has reached levels not previously seen and continues to grow as reporting requirements become more extensive and voluntary disclosures are made for a variety of reasons[72].

There is wide acceptance that this long-term trend is appropriate in today's business world with greater emphasis on corporate governance issues, driven by more demanding shareholders and other interested parties. Key challenges are to align practices in accounting practice and VAT administration with reform objectives and to establish an effective accountability architecture. Such reforms, which typically require radical changes to the established culture and values in VAT collection procedures (assessment and rendering of returns) and revenue governance (transparency and accountability).

Revenue Sustainability
Although in a contemporary modern state[73], government revenues (tax or non-tax) are central to development, the availability of this revenue is crucial to any attempt by the state to redistribute wealth, alleviate poverty and provide various public goods to make a difference to the quality of life and survival[74]. To ensure sustainability in tax revenue, particularly that from VAT, there is need for continuous tax verification, monitoring, audit and investigation

and regular tax drive. This requires monitoring, from time to time, the premises of every taxable person by authorised tax officers from the FIRS. Such visits are:

> To ensure compliance with the VAT legislation and registrations in all its ramifications; To ensure that full amount of VAT deducted are promptly accounted for; To examine method of recording transactions and offer suggestions where necessary; To afford the VAT payer the opportunity to ask any questions and seek clarifications as may be necessary; and To educate VAT payers on new developments in the system.

Tax drives are to take place periodically at the instance of the Tax Controllers/State Monitors. Such tax drives are to stimulate the collection of VAT from defaulters and enforce prompt remittance of VAT payable to avoid evasion and avoidance. Although tax revenues are crucial to enable the state to redistribute wealth and to provide public goods, such aspirations are increasingly checked by tax evasion and tax avoidance practices. These practices are encouraged by the intensification of globalisation, poor regulation, unaccountable state institutions and the absence of ethical and moral constraints. As Elliott and Elliott have observed:

> Tax avoidance and tax evasion has been perceived by the public as being unfair and governments have internationally attempted to combat the problem through legislation, case law and encouraging positive consumer reaction to put pressure on companies not appearing to pay fair amount of tax nationally[75].

Tax evasion practice has international connections through the activities of multinational companies (MNCs). There have been a number of studies implicating MNCs in designing and using a variety of tax schemes to reduce taxes which have had a considerable impact on government revenue[76]. This chapter takes the view that tax avoidance and tax evasion are interconnected. Sometimes, a matter may be considered to be avoidance, but, upon legal challenge, is found to be evasion. Although developing countries often lack the financial and political resources to pursue numerous schemes, which may be labelled as 'avoidance', Cobham was of the view that:

> In general, the most striking characteristic of tax evasion and tax avoidance practices from a legal, moral and economic perspective is that they have negative social consequences[77].

Many reports and also accounts in the academic literature have documented tax evasion practices in both developed and developing countries. However, what is interesting is the variety of schemes and tactics used by businesses to evade tax in Nigeria. As a result of these practices, the loss of government revenue constrains investment in education, healthcare, the provision of clean water and the fight against disease. This has therefore created a huge gap in the standard of living in Nigeria compared to other nations with recorded government revenues[78]. Therefore, in order to regulate the behaviour of taxpayers to facilitate

compliance, the tax regulator is expected to institute tax audit and investigation on a regular basis. This involves checking the VAT payers' records to ensure strict compliance with the law and the accountability of the VAT collected.

Transparency and accountability

The definition and nature of accountability have changed over time. Traditionally, in its simplest form, accountability entails a relationship whereby some people are required by others to explain and take responsibility for their actions, that is, giving and demanding reasons for conduct. It focuses on 'who' is to be accountable to 'whom' and 'for what'. But it has changed beyond its core sense of being called to account for one's actions. Accountability has become multi-faceted, involving account-giving, holding to account but also sitting in judgement and applying sanctions, and being responsive to citizens[79]. A number of commentators have identified various aspects or features of accountability in the public sector and particularly in revenue governance. Scholars have identified three elements or stages to account-giving:

> First, an obligation felt by an account-giver to inform by providing various data about performance, outcomes or procedures; second, an account-receiver is prompted by this information to question the account-giver; and third, the account-receiver is able to pass judgement and may impose sanctions, whether formal or informal[80].

Accountability is said to have three aspects: first, compliance, being held to account; second, transparency, giving an account; and third, responsiveness, taking account[81].

Transparency has emerged as a key principle in the global business regulation and revenue governance in the contemporary global economy. It is often suggested that providing stakeholders with more information on companies' activities can enhance transparency and accountability. Within the accounting literature, transparency has been considered an aspect of accountability which informs, empowers and improves resource governance and, more broadly, societal change[82]. Indeed, 'transparency' is centred on the idea of making things visible. As Gray argues:

> 'The development of accountability . . . increases the transparency of organisations. That is, it increases the number of things that are made visible, increases the number of ways in which things are made visible, and, in doing so, encourages a greater openness. The inside of the organisation becomes more visible, that is, transparent'[83].

However, given that the fundamental assumption of transparency, as expressed within the conventional accounting reporting, is to communicate information to various social constituents, what is *revealed or uncovered* is arguably to be as significant as what is *concealed*[84]. Yet, it has been argued that, through inclusion by measurement and disclosure, importance and relevance are assigned to some matters of business, but, through exclusion, some issues have repeatedly been excluded[85].

The Nigerian tax system is expected to contribute to the well-being of all Nigerians and taxes, which are collected by government, and should directly impact on the lives of the citizens. Therefore, tax administration (including VAT) in Nigeria should be seen to be transparent and accountable to all the taxpayers. Taxpayers should be aware of existing taxes or new taxes imposed on them, and the proper utilisation of the tax revenue. One of the primary objectives of the National Tax Policy is to create a tax system, which ensures that Government transparently and judiciously accounts for the revenue it generates from taxation by investing in the provision of public goods and services, demanded by her people. It was noted in the National Tax Policy that where this is in place, Nigerians would have a system that they can fully relate to and provide a vital tool for National Development[86].

Taxpayers are the single most important group of stakeholders in the tax system. They are the primary focus of all tax authorities, due to the significant role which they play in the tax system. As entrenched in the tax law, taxpayers are required to discharge their roles, by ensuring strict compliance with the tax laws, including Value Added Tax Act[87]. Taxpayers are required to ensure voluntary registration with tax authorities and make timely, correct and complete tax returns and payments, as required under the provisions of the VAT Act. In addition, they shall act in an informal supervisory role, as they have the right to demand for transparency and accountability in the collection, allocation, disbursement of VAT revenue proceeds.

Tax professionals and practitioners are also key in the administration of VAT in Nigeria for they are expected to use their skill and expertise to simplify tax compliance process, support the taxpayers on compliance requirements and also provide necessary insight and assistance to tax authorities. It is, therefore, expected that professionals and practitioners shall discharge their duties with a high level of integrity and adherence to their professional code of ethics, aimed at ensuring accountability and transparency in their professional assignments. They should not be party to wilful or negligent non-compliance with relevant provisions of the VAT Act and related tax laws.

At the completion of the tax administration process, it is expected that tax revenue would have been paid by taxpayers and collected by the tax authority. The end of the compliance process is the commencement of another process, whereby the tax authority is required to account for the tax revenue collected. It is, therefore, the responsibility of the tax authority to ensure that proper, timely and complete, account is given of all tax revenues collected, including those from VAT, within the specified periods, in compliance with the established laws. It has been argued that accountability and transparency of tax revenue management is necessary to assure taxpayers that tax revenue collected is accounted for and that there are no leakages on the part of the tax authority and their collecting agents. In addition to ensuring proper accountability for tax revenue collected, there is need to ensure proper utilisation of tax revenues, given that the revenues are generated and utilised by the Government in trust on behalf of its citizens for socio-political and economic growth and development.

8. Conclusion

This chapter has examined the importance of proper accounting in VAT administration to prevent tax revenue leakages (tax evasion, tax avoidance and fiscal corruption) in the assessment and collection of VAT revenues in Nigeria. The review in the chapter suggests that 'anti-revenue' behaviours are common in tax administration, including that of VAT as a result of the lack of proper accounting for VAT transactions and their documentations; the lack of transparency; and the lack of a tradition of voluntary compliance, coupled with inefficiency in the tax administration system. The tax revenues, owed to the Nigerian government, due to lack of proper accounting, are essential for funding the much-needed development of the country. Thus, the size of the revenue base has far-reaching implications for the government's ability to meet its objectives and to ensure a holistic socio-economic growth and development. Unfortunately, however, the reduced revenues available, because of tax revenue leakages, have restricted the development of the Nigerian economy, and, as a result, Nigeria is forced to continue to rely on foreign aid and foreign borrowing.

As a consequence of these tax leakages and tax frauds, the infrastructural development, promised to Nigerian citizens, has not been provided and, even where such amenities have been provided, they are not adequate. The unavailability of these amenities (good roads, electricity, healthcare system and schools) has pushed many Nigerians to cater for their own needs, which has serious implications for the legality of the state and the various taxes imposed on citizens. On the strength of this, taxpayers cheat on their taxes because of the low or non-existent accountability structures in the tax system. Thus, as in any country, where the state does not hold the government accountable for its expenditures, there is likely to be indiscipline, corruption, waste, misplaced priorities and gross inefficiency, which will continue to have a detrimental impact on the development of Nigeria. Yes, it is acknowledged that, in every system, there is bound to be leakages. It is, therefore, the duty of the tax authorities to identify all such avenues for leakages in the Nigerian tax system and minimise or eradicate them.

9. Recommendation

The Nigerian government, by means of its administrative apparatus, has put in place tax regimes and regulations and has promised to make effective use of the tax revenues generated by providing public goods and services, as contained in the National Tax Policy. It is also suggested that, to address the issue of tax leakages in the VAT administration, in particular, and in the Nigerian tax system, in general, there is a need to reform and overhaul the entire administrative machinery in order to prevent billions of Naira from continuing to be lost yearly. The reform should not be half-hearted. Thus, the entire structure of transparency and accountability must be strengthened to include reforming taxation processes, policies, institutions and revenue governance. To encourage citizens and corporations to perform their statutory duties, the Nigerian government should embark on more serious efforts to adopt sound government structures, devoid of bad leadership, corruption, mismanagement and insensitivity to the plight of the poor.

ENDNOTES

1. C. S. Ola, Income Tax Law and Practice in Nigeria, (Ibadan: Heinemann Educational Books, 2001), p. 584.
2. VAT, which is only 44 years old in practice, has been adopted by about 100 countries worldwide, about 75 per cent of which are developing nations (see Supra, note 1).
3. As at the end of year 2004, one hundred and twenty-five countries operate Value Added Tax as a simple source of generating revenue (see O. S. Obatola, The Rudiments of Nigerian Taxation, (Lagos: ASCO Publishers, 2013), p. 317; A. Schenk, V. Thuronyi& W. Cui,Value Added Tax - A Comparative Approach, (New York: Cambridge University Press), pp. 10-11.
4. Now Value Added Tax Act, CAP VI, Laws of Federation of Nigeria, 2004, as amended by Value Added Tax (Amendment) Act of 2007.
5. A. Sanni, Value Added Tax in Nigeria, in Sanni, A. and Elebiju A., Indirect Taxes in Nigeria, Lagos: Chartered Institute of Taxation of Nigeria, 2014).
6. See J. K. Naiyeju, Value Added Tax: The Facts of a Positive Tax in Nigeria, (Lagos: Kupag Public Affairs, 1996); Supra, Ibid., note 1, at pp. 583-606; Supra, note 4, pp. 64-108; E. O. Ogundele, Value Added Tax (VAT), Theory and Practice, (Lagos: Libriserve, 1996); A. Sanni and A. Elebiju, Value Added Tax in Nigeria, (Lagos: Chartered Institute of Taxation of Nigeria, 2014).
7. See A. Sanni and A. Elebiju, Value Added Tax in Nigeria, (Chartered Institute of Taxation of Nigeria, Lagos 2014).
8. See Supra, note 1; See Supra, note 3; See Supra, Ibid., note 5; See Supra, note 8; See Supra, note 9.
9. Federal Inland Revenue Service (FIRS), (Information Circular No. 2005/01,February 2006),p. 2.
10. P. M. Collier, Accounting for Managers: Interpreting Accounting Information for Decision Making, (London: John Wiley, 2012), p. 98.
11. See Statement of Standard Accounting Practice (SSAP) 5.
12. See F. Wook& A. Stangster, Business Accounting1 Ninth Edition, (Essex: Pearson Education, 2002) p. 183.
13. See M. E. Porter, Competitive Advantage: Creating and Sustaining Superior Performance, (New York: Free Press, 1985) p. 36.
14. See Supra, note 1, p. 600.
15. See Supra, note 5, p. X.
16. See IASB, 2001, para. 8; See also B. Elliott & J. Elliott, Financial Accounting and Reporting, (England: Pearson Educational, 2013), p. 419.
17. The collection of the tax on imports and tax on domestic sales typically are administered by different departments of the tax authority – Customs for imports and Inland Revenue (or a comparable department) for tax on domestic (including export) sales. In the case of Nigeria, it is the Nigerian Custom Service and Federal Inland Revenue Service (FIRS), respectively.
18. See Value Added Tax (VAT) Information Circular No. 9304, FIRS Abuja, 20thAugust, 1993) p. 4.
19. See Supra, note 1, p. 590. VAT is borne by a person who is at the terminal end of the distribution chain.
20. The computations of the Value Added Tax in Table 1 above is based on the amendment

of the VAT rate from 5% to 7.5% (s. 4 VATA as amended) See s. 34 of the Finance Act, 2019 and s. 42 of Finance Act, 2020.

21. See s. 8(2) of VATA as amended by Finance Act, 2019 at p. A16.
22. See Supra, note 5, p. 83; See Supra, note 20, p. 7.
23. See s. 46 of the Value Added Tax Act.
24. In most EU and several other European countries with VATs, there are thresholds for distance selling and retail export scheme. See A. Schenk and O. Oldman, Value Added Tax: A comparative Approach (Cambridge: Cambridge University Press, 2007), p. 74.
25. See s. 8(1), Value Added Tax (Amendment) Act of 2007; R. Hamzaoui, Global Corporate Tax Handbook 2013. IBFD Global Tax Series, (The Netherlands: Global Tax Series, 2013), p. 838.
26. See s. 15 of VATA CAP VI as amended by s. 38 of Finance Act 2019
27. See Supra 3, p. 323.
28. See s. 36 of Finance Act, 2019 at p. A16
29. FIRS Information Circular, Tax Implications of the Adoption of the International Financial Reporting Standards (IFRS), FIRS Abuja, March 2013, p. 9.
30. See Supra, note 18, p. 419.
31. See Supra, note 24, p. 52.
32. See Supra, note 18, p. 419.
33. See Supra, note 24, p. 52.
34. Zero rating is the mechanism under a VAT system by which the tax can be completely removed from a particular product or service or from a particular transaction. See Schenk and Oldman, Supra, Ibid., note 23, p. 50. Zero-rated goods include: (a) Non-Oil Exports; (b) Goods and Services purchased by diplomats; and (c) Goods and Services purchased for use in humanitarian donor-funded projects.
35. A. R. Jennings, Financial Accounting (London: DP Publications, 1990), p. 279.
36. See Supra, note 18, p. 419.
37. See Supra note 24, p. 50.
38. C. E.Ruebling, A Value Added Tax and Factors Affecting its Economic Impact (Federal Reserve Bank of St. Louis, September 1973) pp. 15-16.
39. K. James, The Rise of the Value Added Tax (New York: Cambridge University Press, 2015), p. 70.
40. See Supra 3, p. 319; See Supra, note 24, p. 38. For a thorough analysis of the advantages of the invoice VAT over the sales-subtraction VAT, see James, Supra, note 37, pp. 72-73.
41. See Supra, note 37, p. 71.
42. See s. 37 of Finance Act, 2019 at p. A17, provides for Cash basis for accounting for VAT and VAT refunds through amendment to s. 16 of the VATA by substituting a new subsection '1'.
43. Ibid, at p. 320.
44. See Supra 24, at p. 42.
45. See Supra, note 3 at p. 321; See Supra note 24 at p. 42.
46. See A. Schenk, V. Thuronyi, & W. Cui, Value Added Tax: A Comparative Approach (New York: Cambridge University Press, 2015) p. 33.
47. See R. F. van Brederode. Systems of General Sales Taxation: Theory, Policy and Practice (The Netherlands: Kluwer Law International, 2009), p. 21.
48. See Supra, note 43, p. 33; see also note 44, p. 21.

49. See Supra, note 43, p. 33.
50. S. M. Adesola, Tax Laws and Administration in Nigeria (Ile-Ife: Obafemi Awolowo University Press, 1998), p. 258.
51. See Supra 3, p. 329.
52. See Supra, note 14, p. 187.
53. A VATable person is one who trades in VATable goods and services, other than those goods and services listed in the First Schedule to the Act for a consideration [see S. 2 of VAT (Amendment) Act, 2007]; see Supra 3, Ibid., p. 323; see Supra 6, p. 80.
54. See Supra, note 14, p. 187.
55. See S. 11 VAT (Amendment) Act, 2007; see Supra, note 4; See Supra 19, p. 8.
56. See Supra 20, p. 9.
57. See Supra 14, p. 187.
58. Documentation relating to the importation and exportation of goods and services; all debit and credit notes or other documents providing evidence of an increase or decrease in the value of goods and services purchased or sold by him/her; and such other records, as the Revenue may specify.
59. See Supra 5, p. 83.
60. These are legal entities incorporated under the Companies and Allied Matters Act (CAMA) of 1990 and engaged in banking and financial activities, as defined by the Banks and other Financial Institutions Act (BOFIA), 1991. They are companies within the financial sector of the Nigerian economy and are either publicly quoted or private companies. Banks will ordinarily include commercial banks, merchant banks and development banks, while other financial institutions will include finance houses, insurance companies, re-insurance companies, stock-brokerage firms, investment companies and financial consultants.
61. See Supra, note 11, p. 2.
62. Ibid., p. 3; also, see Supra, note 4, Value Added Tax Act, as amended.
63. See s. 29 and s. 31 of the Value Added Tax Act, Cap V1, LFN, 2004 (as amended).
64. See Supra, note 1 p. X.
65. See the FIRS Information Circular No. 9503, 1stDecember, 1995, p. 2.
66. In arriving at what constitutes taxable financial services, a distinction should be made between activities that constitute return on investment and consumption of services rendered by financial institutions. All charges arising from the services of banks and financial institutions will ordinarily attract VAT (See Ibid., p. 2).
67. See IAS 18 (paragraph 8) (IASB, 2001).
68. See s. 55(1) of the Companies Income Tax Act, Cap C21, LFN, 2004, requires a company, filing a return, to submit its audited accounts to the FIRS, while Ss. 8, 52 and 53 of the Financial Reporting Council of Nigeria Act, 2011, gave effect to the adoption of FIRS.
69. See Federal Inland Revenue Service, Tax Implications of Adoption of International Financial Reporting Standards, (FIRS Information Circular March 2013), Abuja.
70. See s. 46 of VAT Act, CAP VI, LFN 2004 as amended.Aa
71. See Finance Act 2019; Nigerian FIRS VAT Circular No. 2020/02, 29th April 2020 available online https://www.firs.gov.ng/wp-content/uploads/2021/01/Nigeria_FIRS_VAT_circular_Apr2020.pdf accessed on 6th June 2021.
72. See M. Billings and F. Capie (2009), Transparency and Financial Reporting in Mid-

20th Century British Banking, Accounting Forum, 33, 38-53, at p. 38.

73. The State is a political conduit for class rule. It is also the means for constituting civil society as an organic unity embracing all segments of the populace. The State's power, therefore, comes from the coercive apparatus as well as the entire complex of theoretical and practical activities used by a ruling class to rationalise its dominance and win the active consent of the masses.
74. See M. O. Bakre (2007), The Unethical Practices of Accountants and Auditors and the Compromising Stance of Professional Bodies in the Corporate World Evidence from Corporate Nigeria, Accounting Forum, 31(3): 277-303. See also P. Sikka (2008) 'Enterprise Culture and Accountancy Firms: The New Master of Universe', Accounting, Auditing and Accountability Journal, 21(2): 268-295.
75. Elliott and Elliott, 2013,note 18, p. 420.
76. See Bakre, 2007, note 69; also, see P. Sikka (2006), 'Can Major Accounting Firms Behave Ethically?' International Accountant, September, 2006: 28-30.
77. A. Cobham (2005), Tax Evasion, Tax Avoidance and Development Finance, QEH Working Paper Series – QEHWPS 129, Online. Available at: http://www3.qeh.ox.ac.uk/pdf/qehwp/qehwps129.pdf (accessed 18th July, 2016).
78. For instance, the late Nigeria dictator, Sani Abacha and members of his inner circle, looted and exported an estimated $2.2 billion (some estimates are even higher). Such diversion is particularly troubling in view of the World Bank's estimates that the entire GDP for Nigeria was approximately $41.1 billion and that 70 per cent of the estimated population of 123.9 million people were living on less than $1 a day (UN Office on Drug and Crime, on-line athttp//www.unodc.org/unodc/en/corruption_projects_nigeria_project2.html, accessed on 12thJanuary, 2016.
79. See Shaoul, J., Stafford, A. and Stapleton, P. (2012). Accountability and Corporate Governance of Public private Partnerships.
80. Ibid at p. 215.
81. See Accountability 2004.
82. See Belal, A. R., Cooper S. M. And Roberts, R. W. (2013). Vulnerable and Exploitable: The Need for Organisational Accountability and Transparency in Emerging and Less Developed Economies. Accounting Forum, 37 (2), 81-91; Welch, T. C. and Rotberg, E. H. (2006). Transparency: Panacea or Pandora's Box. Journal of Managerial Development, 26 (5), 937-941; and Drucker, S. and Gumpert, G. (2007). Through the Looking Glass: Illusions of Transparency and the Cult of Information. Journal of Managerial Development, 26 (5), 493-498.
83. R. Gray, (1992). Accounting and Environmentalism: An Exploration of the Challenge of Gently accounting for accountability, transparency and Sustainability. Accounting, Organisations and Society, 17 (5), 399-425, at p. 621.
84. See J. Roborts, (2009), No One is Perfect: The Limits of Transparency and an Ethic for 'Intelligent' Accountability. Accounting, Organisations and Society, 34, 957-970.
85. See Young, 2003, p. 621.
86. See Federal Ministry of Finance (2012). National Tax Policy. Federal Ministry of Finance, Abuja, 1-43.
87. Particularly the provisions contained in S. 8-18 of VAT (Amendment) Act, 2007.

CHAPTER 6

VAT COLLECTION AND REMITTANCE

Abstract

Value Added Tax (VAT) is an indirect and multi-stage tax, imposed and charged on goods and services, other than those exempted under the statutorily provided list. As a result of its indirect nature as well as its cascading effect, the collection and remission of VAT are major issues to a taxable or VAT-able person. In resolving these issues, there is a need to differentiate between VAT-able person and the targeted payer under the Value Added Tax Act, V1, LFN, 2004 (VATA). This distinction and the recognition of some entities as agents under the VATA have led to the questions: Who is responsible for collecting VAT? And who is a Collecting Agent? This chapter will further consider the core issues, such as collection and computation of VAT, remission and remittance of VAT, including refund, the process for collection of VAT and evidence in proof of collection and remission in the light of the policy and legal framework amidst the administrative mechanisms in Nigeria.

1. Introduction

Value Added Tax (VAT) is an indirect and multi-stage tax, imposed and charged on goods and services, other than those exempted under the statutorily provided list. The target of VAT is consumption of goods and services and, unless an item is specifically exempted by law, the consumer is liable to VAT. Conceptually, VAT is not collected directly from the targeted payer (the end consumer), who ultimately bears the economic benefit of the tax. The responsibility for collection and remittance of the tax is placed on another party, an intermediary. Nevertheless, it has been observed that separate and distinct status of the targeted payer and the intermediary may, in practice, be blurred by the design of VAT. According to David Child:

> VAT is, or should be in concept, a tax on consumption by final consumers. It should not be a cost on businesses. However, VAT designs often maximize exemptions and restrictions on deducting input tax so that businesses become the de facto final consumer and hence the tax falls on business owners, employees and financiers of the firms whose input is being taxed[1].

VATs are designed to deal with the intermediaries and effectively capture the collection and remission of VAT. In different jurisdictions, VATs are tailored and designed to address the issues surrounding the collection and remission of VAT in the relevant clime. In Nigeria, the legal and administrative mechanisms for collection and remission of VAT are contained in

the Value Added Tax Act, V1, LFN, 2004 as amended (VAT Act), the Federal Inland Revenue Services (FIRS) Information Circulars[2] and Public Notices. The Act contains 47 sections and One Schedule. Sections 7 to 20 of the Act directly or indirectly address the collection and remittance of VAT.

2. Definition of Major Terms

Collection

The Act does not define the term "collection". The word "collection" is used in the Act as part of the title for some sections, while the word "collect" is used in expressing some provisions of the Act. For example, section 14 of the Act is titled "*Collection of tax by taxable person*" whereas section 14 (2) states that "*The tax collected by a taxable person under subsection (1) of this section shall be known as output tax*". However, collection has been defined as "*the act of obtaining money that is owed to you*"[3]. The Oxford Advanced Learner's Dictionary also defines collection as "*an act of collecting money to help a charity or during a church service; the money collected'*"[4]. The word "collect" has been defined as "*to ask people to give you money for a particular purpose*"[5]. It can be said that in the context of the VAT Act, "collect" refers to asking people or persons (including individuals and corporate entities) to give you money for the purpose of fulfilling VAT obligations.

Remittance and Remission

Similarly, the Act does not define the terms "remittance". Remittance is, defined as "*a sum of money sent to another as payment for goods or services; the action or process of sending money to another person or place*"[6]. *Oxford Advanced Learner's Dictionary* also defines "remittance" as "*a sum of money that is sent to somebody in order to pay for something; the act of sending money to somebody in order to pay for something; synonym – payment.*"[7] Remittance, in the context of the VAT Act, can, therefore, be referred to as the sending of money for VAT to the FIRS or the payment of VAT into the account of the FIRS.

From the foregoing definition of the major terms, VAT collection and remittance refer to the act, practice and process of asking individuals, professionals and corporate entities for an amount, representing the VAT and sending or paying that amount into the coffers of the Federal Government in the care of the FIRS.

3. Policy Background to Collection and Remittance of VAT

In 1991, Professor Edozien led a Study Group on the Review of the Nigerian Tax System. The Study Group recommended a policy shift from direct taxation to indirect taxation. On that background, a parallel Study Group on Indirect Tax System was set up to study the feasibility of introducing VAT in Nigeria, as an improvement on the Sales Tax that was in operation. Dr. Sylvester Ugoh led the team and in November 1991, the team recommended that Nigeria should introduce VAT after two years of creating and developing the preliminary framework to that effect. In furtherance to that, the Ijewere-led Modified Value Added Tax (MVAT) Committee was constituted in June 1992 to consider the feasibility of the previous

recommendation and undertake preliminary work for the introduction of the VAT[8]. According to J.K. Naiyeju:

> The modified value added tax canvassed by the MVAT Committee is nothing but a glorified sales tax because it has no credit system built into it to mitigate the cascading effects of a multi-stage tax like VAT. Nigeria has opted for VAT and not a glorified sales tax[9].

It is worth noting that collection of VAT regarding the administrative outfit to administer the tax, has been a burning policy issue from inception. The MVAT Committee advocated for an elaborate separate commission to administer the new tax. The Federal Government, however, rejected this position and directed that VAT should be administered by the Federal Inland Revenue Service (FIRS), which was an agency in the Ministry of Finance, responsible for the administration of Income Tax. Commenting on the Decree creating the VAT, J.K. Naiyeju stated:

> The Decree places the administration and management of the tax on the Federal Board of Inland Revenue (FBIR) and empowers the Board to do such things as it may deem necessary and expedient for the assessment, collection and accounting for the tax. It is in the exercise of this power that the Board has appointed other statutory bodies like Nigeria Customs Service (NCS), NITEL, public and private companies and a host of other organisations to act as agents of collection of the tax in their respective areas of operation[10].

This position consequently has been codified in the VAT Act to the effect that FIRS shall have the power to administer the charge, collect and enforce the VAT Act in Nigeria[11].

4. National Tax Policy

The National Tax Policy[12] provides direction for Nigeria's tax system and establishes a framework for tax collection. The NTP 2017 states that tax administration in Nigeria cuts across the three-tiers of Government. This tax policy document establishes clear guidelines on crucial tax administration issues. In the context of the Nigerian Tax Policy, tax authorities at all levels shall administer their mandates in accordance with the following amongst :other things:

> *Efficiency of Administration: Payment Processing and Collection*
> *Collection system shall leverage on modern technology towards advancing ease of payment and prevention of revenue losses.*

To that effect, the Tax Policy anticipates payment and collection of taxes including VAT through modern technology. It is opined that such technology should resolve the following issues:

a. Who collects what?
b. How it is collected.
c. Who controls what is collected?
d. How is what is collected shared?

e. Who is responsible for spending what is collected?
f. Who is ultimately responsible and accountable to the taxpayers for the revenue collected and its expenditure?[13]

5. Legal and Administrative Framework on Collection & Remittance

As earlier noted, the legal and administrative mechanisms for collection and remission of VAT are contained in the VAT Act, FIRS Information Circulars and Public Notices. The FIRS derives its administrative power for collection of VAT from section 7 (2) of the VAT Act, which states thus:

> The Board may do such things as it may deem necessary and expedient for the assessment and collection of the tax and shall account for all amounts so collected in accordance with the provisions of this Act.

It is this writer's view that it is pursuant to the above provision that the FIRS is statutorily empowered to issue circulars and public notices regarding the collection and remittance of VAT. However, in considering whether the administrative mechanisms under the FIRS circulars and public notices are properly synchronised with the VAT Act, some issues have emerged. The salient issues are considered below.

Taxable and Registered Person

The VAT Act defines taxable person to include:

> an individual or body of individuals, family, corporations sole, trustee or executor or a person ***who carries out in a place an economic activity, a person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business or a person or agency of Government acting in that capacity***.[14]

From this definition, it can be seen that the taxable person is not defined in terms of the consumer or the final consumer that bears the economic benefit of the VAT. The definition, *strictosensu*, does not recognise the final consumer as a taxable person. Although VAT is a consumption tax, payable on the goods and services consumed by any person, whether a government agency, a business association or an individual. On the other hand, the taxable person with respect to certain goods or services may be the final consumer of *other items* of goods or services. In other words, the taxable person for a transaction may be the final consumer in another transaction. Taxable person, therefore, covers wide-ranging individuals or body of individuals, such as manufacturers, wholesalers, retailers, companies (small, medium, large and multinational), partnerships, professional firms, government ministries, agencies, parastatals and other suppliers of goods and services.

A taxable person is required to register with the FIRS within six months of the commencement of its business.[15] The VAT Act specifically mandates every Government Ministry, statutory body and other agency of Government to register as agents of the FIRS for the purpose of collecting VAT[16]. The condition precedent to obtaining a contract from the

Government Ministry, statutory body and other agency of Government is for the contractor, who is to transact business with the Government Ministry, statutory body and other agency of Government, to produce evidence of registration with the FIRS[17]. In the same vein, a non-resident company that carries on business in Nigeria is to register with the FIRS for VAT, by using the address of the person with whom it has a subsisting contract as its address for purposes of VAT correspondence[18]. The statutory provisions regarding a non-resident company assume some facts, which we will be considered later in this chapter.

Who is responsible for collecting VAT?

Generally, the person supplying goods and services to his/her accredited distributor, agent, client or consumer, has the responsibility for collecting VAT on those goods or services[19]. This VAT collected is known as Output Tax[20]. The rationale for assigning responsibility for collection on the supplier of goods or services is that the supplier is the one entitled to the money, money's worth or fund. Therefore, at the time of receiving the payments, costs or fees for the goods and services, the supplier has the obligation to collect the VAT, while the purchaser or the recipient of goods or services has the duty to pay the supplier the VAT on the goods and services[21]. When a purchaser makes payment for VAT, it is known as Input Tax.[22] This universal understanding regarding the payment and collection of VAT may blur the appreciation of the collection responsibility imposed on some institutions, agencies and bodies under the Nigerian VAT regime. Some collection responsibilities have nothing to do with whether the taxable person is a supplier or a purchaser: the taxable person is just serving as a channel of collection, or as a Collecting Agent for VAT.

Who is a Collecting Agent?

As earlier stated, every Government Ministry, statutory body or other agency of Government is required to register as taxable persons. At the time of making payment to a contractor, every Ministry, statutory body or other agency of Government shall remit VAT charged on a contract to the nearest local office of FIRS[23]. It appears that there may be a conflict of responsibilities where the contractor is the supplier of goods and the contractor is claiming the collection of Output VAT from the relevant agency of Government. Should the agency of Government go ahead to remit the VAT to FIRS or should the VAT be paid to the contractor as supplier, who will then remit the VAT to FIRS? There is inherent uncertainty in this instance, contrary to the certainty nature of law.

Section 41 of the VAT Act provides thus:

(1) The Board may, by notice in writing, appoint any person to be the agent of any manufacturer or importer and the person so appointed shall be the agent of the manufacturer or importer for the purposes of this Act.

(2) An agent may be required to pay any tax which is or may become payable by the manufacturer or importer from any money which may be held by him for, or due by or to become due by him to the manufacturer or importer, as the case may be, and in default of such payment, the tax shall be recoverable from him.

(3) For the purpose of this section, the Board may require a person to give information as to any money, fund or other assets which may be held by him for,

or of any money due from him to a manufacturer or an importer.

The effect of these provisions is that the FIRS may appoint any person as the agent of any manufacturer or importer. In which case, the agent will be required to pay the VAT, which is, or may become, payable by the manufacturer or importer from any money held by the agent for the manufacturer or importer, or due by the agent to the manufacturer or importer. Considering the wording of these provisions, the VAT Act contemplates that the agent will deduct the VAT at source, which is akin to the operation of the withholding tax system. The deduction of VAT at source has been described as "the reverse charge method of collection of VAT".[24]

In exercise of its power, however, the FIRS appointed the Nigeria Customs Service (NCS) in January 1994 as an agent on its behalf to collect the VAT on imports[25]. It is this writer's view that, considering the language of section 41 of VATA, the FIRS could not have derived the power to appoint NCS from the provisions of section 41 of VATA. The Working Group proposed that the delegated functions, exercised by the NCS in VAT collection on imports, should be codified into law[26].

Collection and Remittance Procedure for VAT

The rate of VAT to be charged at the time or point of collection is 7.5% on the value of all goods and services[27]. The value of taxable goods or services is the money consideration for supply of goods or services, net the VAT, i.e.:

Money consideration = VATable value + VAT; or

VATable value = Money Consideration - VAT. This is VAT, ***inclusive of*** pricing system,

while the value of imported goods is the price of the imported goods, including all taxes, duties and other charges, levied either outside or by reason of importation into Nigeria, and all costs by way of commission, parking, transport and insurance up to the port or place of importation[28], i.e.:

VATable value = Price of the Imported Goods + Taxes + Duties + Charges + Other Costs as defined. This is VAT, ***exclusive*** of pricing system.

In effect, two pricing systems are in use within the Nigeria VAT regime. Whether the VAT, exclusive of pricing system, is also applicable to imported services is not stated or indicated in the VAT Act or any FIRS circular. But, by the canon of interpretation, it is known that, where there are two provisions, one general and another specific, the legislature, in making the special provisions, is considering the particular case and expressing its will in regard to that case[29]. Therefore, it can be safely submitted that the VAT, inclusive of pricing system (that is of general application to taxable goods or services) is applicable to imported services.

VAT Registration Process

The prospective taxable person will obtain and complete VAT Form 001, which will be filed with a letter of application at the nearest FIRS Integrated Tax Office. The application must be

on the organisation's letterhead with the signature of the company's officer[30]. The particulars on the VAT Form 001 are as follows:

1. The full name of the taxpayer.
2. The address of the taxpayer.
3. Date and number of incorporation.
4. Date of commencement of business operations.
5. Business registration certificate number.
6. Nature of business.
7. Tax Office where the registration is done; and
8. Date registered with the VAT office.

The FIRS will issue a permanent registration number, which is the same as the Tax Identification Number (TIN), to also be used for other transactions relating to taxes imposed and collected by the Federal Government.

VAT Invoicing

Invoice generally means any document issued as evidence of demand for payments. A Tax Invoice is similar in many respects to a normal sale or purchase invoice, except that it has provision for VAT registration reference number and VAT payment at the prescribed rate. Every taxable firm or company has a duty to issue a Tax Invoice for every single VAT-able transaction carried out by the business, details of which must be furnished to the nearest Integrated Tax Office of the FIRS within the prescribed period for the rendition of VAT returns.[31]

The tax invoice may be originated from the following sources:

i. Overseas Suppliers - Invoices from this source usually originate from a foreign country to cover goods being imported to Nigeria. It becomes a Tax Invoice at the point when VAT is imposed by the NCS on the CF value of the goods duly reflected on the invoice.
ii. Local Suppliers - Invoices issued locally by one taxable business entity to another in normal business transactions, e.g., manufacturer's invoice to wholesaler or retailer in the business chain.
iii. Local Consumers - Invoices raised by taxable entities to final consumers, who must ultimately bear the burden of the tax paid. Invoice raised by a retailer to a final consumer is not useable for VAT purpose.

The supplier of taxable goods and services shall furnish the purchaser with a VAT invoice, whether, or not, payment is made at the time of supply[32]. In other words, the VAT invoice should be issued at the time of delivery of the taxable goods or services. This emphasises that the tax is due at the time of delivery, and not at the time of payment. The rationales for these regulations are:

- To simplify the calculation of the tax due. Through accrual accounting basis, only records of sales are required; those of payments or accounts receivables will not be

required.
- To safeguard tax revenue in order to ensure that tax revenue is collected early; and that no bad debt is taken into account in calculating the amount of tax due, since the tax revenue is purely based on invoices; and
- To plug loopholes and leakages in the collection system.

An exception to this rule may exist only where payment is received before the delivery. The VAT invoice shall contain the following:
1. Taxpayer's identification number (now the same as TIN).
2. Name and address of supplier.
3. VAT registration number of the supplier (now the same as TIN).
4. The date of supply or delivery.
5. Name of purchaser or client.
6. Gross amount of transaction; and
7. VAT charged and rate supplied.

Records and Returns

A registered taxable person is required to keep such records and books of all transactions, operations, imports and other activities relating to taxable goods and services as are sufficient to determine the correct amount of VAT due[33]. A taxable person is obligated to file returns of the taxes collected and this is done on a monthly basis, on or before the 21st day of the following month, with the aid of VAT Form 002. In practice, VAT returns are to be accompanied with bank statements, detailing the transactions made in the month under review, or, alternatively, where the company has no bank accounts, a letter stating that the company has not commenced business operations and that it is filing NIL returns. The returns[34] are usually done with the following particulars on VAT Form 002:
1. The individual or company's VAT number.
2. The name and address of the VAT-able individual organization.
3. The VAT office where payment is made.
4. The relevant month.
5. Value of total zero-rated supplies.
6. Value of total VATable supplies.
7. Total VAT charged by the taxpayer.
8. Any adjustment made to the individual or organisation's VAT account.
9. Total output tax.
10. VAT on total VATable supplies received, for which invoicing requirements have been met.
11. Total VAT now payable by the taxpayer.
12. VAT on Purchases not wholly used in making VAT-able supplies.
13. Total deductions (Input tax); and
14. Amount to pay/refund due (delete, as applicable).

Exception to Filing Returns

As identified above, failure to file VAT returns as at when due constitutes a reprehensible conduct and any defaulter is liable to pay penalty upon conviction. The derogation however has now been limited to taxable persons whose annual turnover supplies of goods and services either singularly or commulatively are above N25,000,000.00[35]. This constitutes an exception to the general rule for filing monthly returns otherwise known as "threshold filing principle".

Derogation from Collection and Remittance of VAT

Once collections are made, remittances are supposed to be made, with the VAT returns filed. There are two forms of VAT remittances: (i) remittances with Input VAT and (ii) remittances without Input VAT. First, remittances with Input VAT are remittances that attract both remittance and refund systems. It is this form that represents the multi-stage nature of VAT and its cascading effect. The format of Form VAT 002 can be used to compute the remittance payable or refund due. Remittance is payable where the Output VAT exceeds the Input VAT[36], that is, VAT collected, and to be remitted, is more than the VAT paid to the supplier. Refund[37] will, however, be claimed where the Input VAT exceeds the Output VAT, that is, the VAT paid to the supplier is more than the VAT collected and remitted. This first form is limited to the VAT on goods purchased or imported directly for resale and goods which form the stock-in-trade used for the direct production of any new product on which the Output VAT is charged.[38] These goods fall into manufacturing and goods for direct resale.

A taxpayer will be risking serious consequences where he fails to collect VAT and or collect but neglects to remit the amount to FIRS, Specifically, apart from the compulsory payment of the amount collected as VAT, the defaulter shall pay a sum of 10% of the sum not remitted with an interest at the prevailing minimum rediscounted rate by the Central Bank of Nigeria.[39]

Collection and Remittance of VAT by Non-Resident Individual or Company

Before 2019, one of the most uncertain areas of VAT is the application of VAT to non-resident company. T

As earlier stated, the VATA requires a non-resident company to register for VAT. A non-resident company is also mandated to include the VAT in its invoice and the person to whom the goods or services are supplied in Nigeria shall remit the VAT in the currency of the transaction. With respect to this provision, a learned writer has submitted thus:

> As laudable as the provisions may be, they however pose certain administrative challenges in practice. For instance, where a foreign company has business dealing with more than one person, who are located in different places across the country, the foreign company will be required to register with the tax office at different locations where its customers are located which may be administratively burdensome and discouraging. A better approach, in our view, may be to require each local supplier to disclose such transaction and withhold

> the requisite VAT rather than requesting the foreign company to register. This is more so when in practice, the trading activities of such foreign companies usually became known through either a voluntary compliance or during the audit of the local companies with which the foreign company had contracted.[40]

In the recent case of *Gazprom Oil & Gas Nig. Ltd. v. Federal Inland Revenue Service (FIRS)*[41] the issue of whether a non-resident has the obligation to invoice and or remit VAT came up for interpretation, In that case, the Respondent, after the conduct of a Tax Audit, made an allegation of non-rendition of Value Added Tax (VAT) Returns for Non-Resident Companies that had provided services to the Appellant. The Appellant argued stated that the Non-Resident Companies were not carrying on business in Nigeria, and did not register for VAT. It was further contended that they did not charge any VAT. The Appellant consequently approached the VAT Tribunal.

The Tribunal raised the question: Are the Non-Resident Companies, in the facts at hand, carrying on business in Nigeria? The Tribunal responded that:

> it will amount to over stretching the provision of the VAT Act to state once you carry on business with a Nigerian Company one must register with the Board and charge VAT.… the lawmakers had intended and indeed created an obligation on the recipient to remit the Tax in the currency of the transaction once it is invoiced. Of course, remittance on the face value is a function of same having been charged. The mere fact that it is expected that both Non – Resident and Nigerian Company work together creates a duty on the part of the Nigerian Company to ensure collection of the Tax. Section 26 of the Act…the above section however would appear to deal with situation where such allegation which borders on crime is proven. Otherwise the clear interpretation of the Act is that the recipient will only pay when a VAT invoice is issued for the good or service.

The decision in *the Gazprom case* has, however, suffered a deadly blow in the recent case of *Vodacom Business Nig. Ltd. v. Federal Inland Revenue Service (FIRS)*[42]. In that case, New Skies Satellites (NSS), a Netherlands-based company, supplied satellite-network bandwidth capacities to the Appellant for use in Nigeria. The Appellant did not remit VAT on the bandwidth after NSS had issued an invoice to the Appellant for the transaction. The FIRS assessed the transaction to VAT and issued a reassessment notice. The Appellant objected that the transaction was not VAT-able and concluded that a satellite in an orbit cannot constitute a fixed base for NSS, as it forms part of Nigeria under international law. The FIRS, however, argued that, by virtue of sections 2, 3, 46 and the 1st Schedule to the VAT Act, any good or service, supplied in Nigeria, is liable to VAT. The FIRS, however, pointed out that, receiving bandwidth capacities from the Netherlands through earth-based stations in Nigeria, amounted to supply of bandwidth capacities and qualified the transaction as an imported service. The FIRS added that section 10(2) of the VAT Act placed the burden of remitting VAT on the person to whom goods or services were supplied and that the Appellant

owed the duty to remit VAT, not NSS, because the duty was not dependent on NSS's registration with the FIRS or NSS's duty to issue tax invoice.

The Tribunal sitting in Lagos held, *inter alia*, as follows:

> The applicability of the destination principle under the International VAT/GST Guidelines raised by the Respondent also came up for determination in **the Gazprom case**. The Tribunal held that section 10, VAT Act did contemplate the applicability of the destination principle, but it could not be applied to the circumstances of the case before it. While not binding on us, that destination principle is a helpful guide in resolving this case. The destination principle provides that for consumption-tax purposes, internationally traded services and intangibles should be taxed according to the rules of jurisdiction of consumption. VAT is a consumption tax. Bandwidth is intangible. The VAT Act prevails.

As a matter of fact, the Vodacom case went on appeal to the Court of Appeal[43] which settled the lingering issue in the following manner:

> *Now does the fact that the non-resident company did not issue a VAT invoice absolve the appellant as the consumer of the VATable services render from paying the VAT?..... The Appellant contention is that the respondent cannot assess it for VAT in the absence of VAT invoice by a non-resident foreign company.*

The Court of Appeal in its decision further reviewed the provisions of Sections 2 and 10 of the VAT Act held as follows:

> *The parties are agreed on the dual duty imposed by Section10 (2)of the VAT Act, one on the non-residentcompany to include VAT in its invoice and the other on the person to whom the goods and services are supplied in Nigeria to remit the tax. While one ought to follow the other, I am unable to agree with the Appellant that the duties are conjunctive. Where there is a failure to include the VAT in an invoice, it does not bring to an end the liability to remit the VAT which has already kicked in by the stipulations of Section 2 of the VAT Act which mandatorily requires that VAT is to be charged and paid on all goods and services except those listed in the First Schedule to the Act.*

On the whole, the Court of Appeal concluded that by all odds, these afford statutory backing for the assessment issued on the Appellant not withstanding that the non-resident foreign company did not issue a VAT invoice. The duty on the Appellant to remit the tax remained sacrosanct. This issue number two is resolved in favour of the FIRS.

It should be noted that the application of VAT to non-resident individuals or companies may either be by exported goods and services, or by imported goods and services. All exported goods and services are exempted from VAT[44]. The VAT Act defines "exported service" as:

> Service performed by a Nigerian resident or a Nigerian company to **a person**

outside Nigeria.[45]

This means that the recipient or the consumer or the final consumer of goods and services outside the Nigerian borders is not subject to VAT and that the payments due from the exported goods and services are not subject to VAT.

Imported Goods

Section 15(2) of the VAT Act provides that a person, who imports taxable goods into Nigeria, shall render to the FIRS returns on all the taxable goods imported by him/her into Nigeria within the prescribed period. Also, an importer of taxable goods shall, before clearing those goods, pay to the FIRS the VAT on those goods[46]. In that instance, by the amendment of 2007, any payment, made to duly authorised Government agents, shall be deemed to have been made to the FIRS. The subsection 15(3) is a valid enabling provision for appointing NCS as agent of collection on VAT imports. The FIRS Circular[47] has expanded on the payment and returns with respect to the VAT on imports thus:

> An importer does not have to wait for the rendering of returns before paying his VAT – since the VAT must be paid along with customs duties and other charges before the goods can be cleared at the ports. The **NCS's Bill of Entry** is designed to accommodate the column for the assessment of VAT on the import (**see appendix IV).** In other words, the VAT for each imported consignment must be in **bank cheque or draft** at the same time the customs duties are being paid and not later. The bank certified cheque/draft should be drawn on "**Federal Government of Nigeria – F.I.R.S. – VAT Account."**

The Nigeria Customs Service is to render, on a monthly basis, returns of VAT which it has collected and paid to the Central Bank of Nigeria. These returns are to be rendered by each point of entry (as defined in paragraph 7 above) to the nearest local VAT office on or before 21st day of the month following that for which the returns are being submitted.

In making the returns, the Nigeria Customs Service, in each point of entry, must include:

i. the number of the Bill of entry.
ii. the total value on which VAT was charged.
iii. the VAT charged.
iv. the remittances.

The return required by each point of entry (NCS) is to be rendered on Form VAT 006 as contained in ***appendix V.***

It must be noted that section 10(2) of the VAT Act provides that a non-resident company shall include VAT in its invoice and that the person, to whom the goods or services are supplied in Nigeria, shall remit the VAT in the currency of the transaction. Although the provisions of sections 10(2) and 15 appear to be directed to the same taxable object, but they follow different directions; the peculiar circumstance of a non-resident to remit tax and impracticability to recover informs the adoption of the reverse charge rule.

FIRS Electronic Platform

In the past, the FIRS developed different electronic systems for filing and payment of taxes in Nigeria. The electronic systems are administrative platforms, designed for effective and efficient administration of taxes. One of such administrative platforms is the FIRS VAT Collect for sales of tickets by domestic airlines in Nigeria[48], The first and second paragraphs of the Notice are reproduced below:

> The Federal Inland Revenue Service (FIRS) has implemented an auto tracking and remittance platform for Value Added Tax (VAT) from sales of tickets by domestic airlines in Nigeria. The platform is called FIRS VAT-Collect and all domestic airlines in Nigeria have been sensitised on the need to enrol on the FIRS VAT Collect platform. The platform was launched in August 2013 and some airlines have linked up to the system, leaving out four (4) airlines.
>
> 2. The benefit of this collection system is that VAT revenue from domestic ticket sales are remitted promptly by the collecting banks to the VAT pool at the Central Bank without delay. This creates transparency and efficiency in the collection process and facilitates easy reconciliation with FIRS.

However, by the provision of the Finance Act 2020[49], commercial air-ticket and airline transportation tickets are now exempted from value added tax. Consequently, the FIRS electronic platform established for sales of domestic air-tickets by the Circular is rendered useless. In the recent times, the FIRS has now opened an electronic platform for all taxpayers to make remittance within the time required by law.

6. Conclusion

In this chapter, the collection and remittance of VAT has been considered in the context of local and international supplies of goods and services. This reveals that the concept of a taxpayer is confused with collecting agent. Another critical issue is the registration of a non-resident company as it concerns collection and remittance which may lead to multiple registration for VAT. The chapter also discussed invoicing as precursor to collection and remittance as there cannot be collection or remittance without invoicing. The timing for filing returns being the heart of collection and remittance with serious consequences to be meted against any derogation by taxpayers and collecting agents is another fundamental issue which has been addressed by the amendment made to the VAT Act pursuant to Finance Act, 2020. The creation of electronic platform for collection of VAT through the FIRS Circular introduced another dimension to the collection and remittance of VAT which is limited to air tickets in the air transportation services.

7. Recommendation

Based on the foregoing issues and exposition, the following recommendations are made for reforms:

1. There should be a clear distinction between a taxpayer and collection agent for VAT purpose as the definition of taxpayer as presently contained in the VAT Act belied the context.

2. There should be a reform in the area of VAT registration by non-resident companies especially in situation where such non-residen company has contracts with more that one local entity.
3. Considering the fact that in practice, the FIRS has now opened a separate office for registration of non-resident companies, the requirement of using the local address of the person to whom the non-resident company transact with should be deleted in the VAT Act.

ENDNOTES

1. David Child, VAT Administration: Addressing private Sector Concerns in VAT in Africa, edited by Richard Krever (Pretoria: Pretoria University Law Press),p. 130.
2. FIRS Information Circular No. 9304 of 20th August, 1993; FIRS Information Circular No. 9305 of 5th November, 1993; FIRS Information Circular No. 9502 of 20th February, 1995; FIRS Information Circular No. 9503 of 1st December, 1995; FIRS Information Circular No. 2005/01 of February, 2006. In the case of Halliburton v FBIR N.R.L.R. 2 [2013],page 10, at 32-33, it was held that Information Circulars, issued by the FIRS, are neither laws nor regulations, but are merely for the information of the general public and, in particular, all taxpayers' representatives or advisers and the staff of the FIRS. They contain what the makers consider to be their interpretation of the various Nigerian Tax Acts and, thus, constitute their opinion on points of law, with no legally binding effect.
3. Longman Dictionary of Contemporary English. (New 5th Edition) (Pearson Education, 2009; Print, 2012), p. 318.
4. Oxford Advanced Learner's Dictionary. (New 8th Edition) (Oxford: Oxford University Press, 2010; Print, 2015), p. 278.
5. Id.
6. Supra 6, Id.
7. Supra 4,p. 1246.Aaa
8. The VAT was enacted into law on 24th August, 1993, and commenced operation on 1st January, 1994.
9. J.K. Naiyeju, Value-Added Tax: The facts of a positive Tax in Nigeria, KUPAG Public Affairs (1996),p. 39.
10. Ibid.,p. 40.
11. Sections 7 and 8 of the VAT Act (as amended)
12. National Tax Policy, February, 2017, Page 9
13. Supra 13,p. 4.
14. Section 12 of the VAT (Amendment) Act 2007 amended the principal legislation as contained in Section 42 of the Act . Italics and bold are ours for emphasis.
15. Section 35 of the Finance Act which amended Section 8 of the VATAct. Failure or refusal to register within the specified time will attract a penalty of N50,000 in the first month in which the failure occurs and N25,000 for each subsequent month in which the failure continues.
16. Section 9(1) of the VATAct.
17. Section 9(2) of the VATAct.
18. Section 10 of the VATAct.
19. Section 14(1) of the VATAct.
20. Section 14(2) of the VATAct.
21. Section 12(1) of the VATA.
22. Section 12(2) of the VATA.
23. Section 13(1) of the VATA.
24. Olaleye Adebiyi, VAT Amendment Bill: Highpoints and Matters Arising, in Indirect Taxes in Nigeria, edited by Abiola Sanni& Afolabi Elebiju CITN Publications (Lagos: Concept Publications, 2014), p. 107.
25. M. T. Abdulrazaq, Value Added Tax, in CITN Nigerian Tax Guide & Statutes, 2nd

Edition, Volume 2 (Lagos: CIBN Press, 2014).

26. Report of the Working Group on the Review of the Report of the Study Group On the Nigerian Tax Reform, March 2004, p. 18.
27. Section 34 of the Finance Act 2019 amended Section 4 of the VATAct by increasing the rate from 5% to 7.5%.Aaa
28. Section 6 of the VATAct.
29. See Attorney General, Lagos State V. Attorney General, Federation &Ors, SC. 20/2008, delivered on Friday, 11th April, 2014,pp. 38 to 39: "It is an accepted canon of construction that where there are two provisions, one special and the other general, covering the same subject matter, a case falling within the words of the special provision must be governed thereby and not by the terms of the general provision. The reason behind this rule is that the legislature in making the special provisions is considering the particular case and expressing its will in regard to that case; hence the special provision forms an exception importing the negative; in other words, the special case provided for in it is excepted and taken out of the general provision and its ambit; the general provision does not apply."
30. Olugbenga S. Obatola, The Rudiments of Nigerian Taxation(ASCO Publishers, 2014),p. 323.
31. FIRS Information Circular No. 2005/01 of February, 2006.
32. Section 13A of the VATAct.
33. Section 11 of the VATAct.
34. The VATAct does not specify the filing of returns by a taxable person that has not commenced business operations. It is this writer's view, however, that it is a good practice adopted by the FIRS because it makes the administration of the VAT easy; the FIRS does not need to separate the companies that should be filing returns from the ones that should not, and all companies are easier captured in the FIRS database. However, there is a need to provide for this in the VAT legislation.
35. Pursuant to Section 38 of the Finance Act, 2020, the provision of Section 15 of the VAT Act was amended. This however does not obviate the obligation to invoice for VAT-able transactions, collection and remittance of VAT to the FIRS
36. Section 16 (1) of the VATA.
37. .
38. Section 17(1) of the VATA.
39. Section 40 of the Finance Act amended Section 19 of the VAT Act to this effect. Consequently, the consequence of derogating from collection and remittance of VAT is grievous.
40. Abiola Sanni, Current Law and Practice of Value Added Tax in Nigeria, British Journal of Arts and Social Sciences,Vol.5, No.2 (2012),p. 193.
41. Suit No: TAT/ABJ/APP/030/2014, delivered on Wednesday, 10th June, 2015.
42. Suit No: TAT/LZ/VAT/016/2015, dated 12th February, 2016
43. The Court of Appeal sitting in Lagos Division in the Appeal No:- CA/L/556/2018 delivered its judgment on the 24th June, 2019.Aaa
44. Parts I and II of the 1st Schedule to the VATA.
45. Section 46 of the VATA.
46. Section 16(2) of the VATA.
47. FIRS Information Circular No. 9305 of 5th November, 1993.
48. FIRS Public Notice, titled: "NOTICE ON INTENTION BY FEDERAL INLAND

REVENUE SERVICE (FIRS) TAX TO ENFORCE VAT ON DEFAULT DOMESTIC AIRLINES", published in THISDAY NEWSPAPER, dated Monday, August 10, 2015.

49. Section 45 of the Finance Act amended the Schedule to the VAT Act to this effect

CHAPTER 7

APPLICABILITY OF VALUE ADDED TAX TO PROFESSIONAL SERVICES IN NIGERIA

Abstract

The application of the Value Added Tax (VAT) Act to "VATable" and non-exempt goods and services is no more in doubt; there is a perennial discuss and lack exactitude as to whether professional services should be subject to VAT. This chapter carries out a historical review of the VAT jurisprudence and its coverage of professional services. Using a comparative approach, the paper looks at the VAT application to "Exported Services" i.e., professional services which originate from Nigeria and which are provided to Non-Resident companies, and also considers VAT application to "Intra-Company Services" between Sister Companies within the same organization. The chapter also critiques VAT application to Imported Services and the legal issues which guide qualification for Exemption Treatment which are accorded to the supplier of services in Nigeria. In the end, the chapter offers suggestions for reform.

1. Introduction

Sections 1, 2, & 4 of the Value Added Tax Act[1] (VAT Act) jointly impose a 7.5% VAT rate (as amended on January 20, 2020, by Sections 33 and 34 of the Finance Act 2019 (Finance Act 2019)[2] on all taxable goods and services in Nigeria, save for the goods and services exempted from VAT under Parts I, II and III to the First Schedule to the VAT Act. Further, Part II of the First Schedule lists all the services exempted from VAT to include medical, educational and export services, generally. It follows that supplies of most professional services are subject to VAT in Nigeria, unless such is exempted. Nevertheless, there have been certain topical issues that have arisen from the application VAT to professional services to wit:

a. How transactions originating from Nigeria that are provided to foreign non-resident companies are subject to VAT—the issue of "exported services"?;
b. How cross-border intra-company services between sister companies within the same organization are subject to VAT, i.e., whether cross-border supplies between companies within a corporate group are subject to VAT?;
c. How imported professional services are subject to VAT?; and a careful review of services that are exempted from VAT.

By using a comparative approach, this chapter will highlight the state of law and developments in similar common law countries and identify necessary lacunas within the Nigerian laws that will be beneficial to all stakeholders.

Perspective of Professional Services

Professional services support businesses of all sizes and in a wide range of industries. People working in professional services help their clients to manage and improve their business. Accountants, management consultants and lawyers all provide professional services to their clients. Agency services, software, legal services, physician service, forecasting and logistics. As a matter of fact, there are theories around this term. We have knowledge intensive based and semi-knowledge extensive based professional service. This may further be classified as occupational and supportive professional service. It is therefore imperative to conceptualize the term "professional services".

According to Margaret Rouse[3] professional service is an intangible product that a contractor or product vendor sells to help a customer manage a specific part of their business. Interestingly,
professional service is viewed as a product! On the contrary, Merriam-Webster[4] defines professional service as follows:

> Professional service is a service requiring specialized knowledge and skill usually of a mental or intellectual nature and usually requiring a license, certification, or registration.

The Professional Services Higher Apprenticeship currently covers jobs in audit, tax and management consultancy. An interested person working in an accountancy firm or in the finance team of another type of company will be regarded as being engaged in professional services. A job in audit could mean that you will be helping companies with their accounts or analysing financial results for them. Advising businesses on how to be tax efficient or completing their tax returns is certainly professional service and not a product.

2. VAT Application to "Exported Services"—Professional Services Originating from Nigeria and Provided to Non-Resident Companies

In Nigeria, Paragraph 4 of Part II of the First Schedule to the VAT Act previously states that "all exported services" are tax exempt, i.e., VAT is only chargeable on the supply of services, other than those exempted under the VAT Act. Section 2(2)(b)(i)&(ii) of the VAT Act now provides a clear definition of what amounts to "supply of services" from Nigeria:

> (b) In respect of services—
>
> (i) the services are rendered in Nigeria by a person physically present in Nigeria at the time of services provision
>
> (ii) the services are provided to a person in Nigeria, regardless of whether the services are rendered within or outside Nigeria.[5]

Perhaps the most relevant exposition of the "exempted services" is the Kenyan VAT Appeals Tribunal's decision of 26th November 2013 in ***Coca-Cola East and West Africa Ltd vs. Commissioner of Domestic Taxes (Coca-Cola vs CDT).***[6] There, the Kenyan VAT Tribunal delved into an analytical examination on the concept of consumption with regards to the supply of a service and consequently established the applicable) VAT rate chargeable against exported services. Coca-Cola East and West Africa Ltd (Coca-Cola) was a limited company incorporated in Kenya, and its principal activity was the promotion of the Coca-Cola brand, i.e., by providing various marketing and support services to Coca-Cola Export Corporation (CCEC), a company incorporated and domiciled in the United States. The services rendered to CCEC by Coca-Cola were provided at a fee, under which Coca-Cola entered into a contract with CCEC to promote the Coca-Cola brand in Kenya, Eritrea, Somalia, Uganda, Burundi, Reunion, Djibouti, Rwanda, Madagascar, Congo, Seychelles, Mayotte, Democratic Republic of Congo, Malawi, Mozambique, St. Helena, Zambia and Zimbabwe.

In respect of the promotional services, Coca-Cola engaged agents in Kenya for the purposes of advertising the Coca-Cola brand on local Kenyan television and radio stations, in Kenyan local dailies and on billboards in various areas within Kenya. In addition, Coca-Cola organized various functions and promotional activities geared toward the promotion and marketing of the Coca-Cola brand. However, there were several companies in Kenya, independent of Coca-Cola and CCEC, that also bottle Export's products.

Thereafter, the Kenya Revenue Authority (KRA) carried out an audit on Coca-Cola and noted that the company had not charged VAT on the services it had rendered, and so proceeded to issue an assessment on the grounds that these services were "local supplies" for which Coca-Cola should have charged VAT. Coca-Cola appealed on the grounds that the services were consumed by CCEC, which was domiciled in the United States, and therefore the supply amounted to an export that should be zero rated. The now repealed Kenyan VAT Act[7] which was in force at that time defined a "service exported out of Kenya" to mean a service provided for use or consumption outside of Kenya. Such a service was zero rated. The Tribunal sought to answer the following issues with a view to determining the place of consumption and hence determine if VAT was chargeable at the rate of 16%. The issues for determination before the VAT Tribunal were:

- Whether the requisition or payment of services necessarily amounted to consumption of services; and
- Whether the services rendered by Coca-Cola were consumed in Kenya.

The pertinent issue that was in contention was whether the services provided by the Appellant were standard rated (VAT applied at 16%) or zero rated (VAT applied at 0%), and on this issue of whether requisition or payment of services amounted to consumption, the VAT Tribunal held that, just because CCEC requisitioned the services from Coca Cola, it did not mean it was necessarily the consumer of those services. In its reasoning, the tribunal stated that consumption or use of a service is not determined by reference to the location or the payer or person requisitioning the service. What was pertinent, according to the tribunal,

was the location of the consumer of the services. The location of the payer is immaterial, and what was material was whether the supplier of the service had established a business or permanent establishment in Kenya and whether the services are consumed in Kenya.

In addressing the issue of who the consumers of the services were, the tribunal held that households in Kenya were the final consumers of the advertising and promotion services leading to the eventual purchase of the product being advertised. These people, according to the tribunal, heard the advertisements on the radio, saw them on television, read them in the dailies and attended the various functions, and by hearing, seeing and reading these advertisements, these people were physically consuming the advertising services offered by Coca-Cola. The tribunal emphasized that it is immaterial that CCEC earned revenue from the services rendered by Coca-Cola. Rather, what was important was the place of consumption and not the location of the person who earned revenue from the services undertaken. The tribunal therefore held that the services were not exported as they were consumed in Kenya and were therefore subject to VAT.

This is similar to the recent decision of the Tax Appeal Tribunal, Lagos Zone, Nigeria in ***Allan Gray Investment Management Limited v Federal Inland Revenue Services,***[8] which held that:

i. services which flow from service providers in Nigeria to third parties (such as persons resident in Nigeria) on behalf of or for the benefit of persons resident outside Nigeria do not constitute exported service for tax purposes in Nigeria, and
ii. a Nigerian resident through whom a non-resident person carries on economic activity in Nigeria for profit-making purposes, is effectively an agent of the non-resident person in Nigeria for tax purposes; and, accordingly, liable to satisfy the tax obligations of that non-resident person in Nigeria

The lesson for Nigeria is that for a taxpayer to benefit from the exemption accorded to "exported services" under Paragraph 4 of Part II of the First Schedule to the VAT Act, the place of consumption must be outside Nigeria, even if payment is received in Nigeria.

3. VAT Among Affiliated Companies within A Group

Another aspect of VAT is how intra-company transactions between members of a single economic group should be subject to VAT on such transactions.

In Europe, the introduction in 2011 of the VAT European Implementing Regulation (hereinafter the 'Implementing Regulation')[9] changed the understating of fixed establishment by providing various definitions of the concept. The above was the issue addressed in ***Judgment in Skandia America Corporation (C-7/13). (Skandia Case).***[10] In Skandia Case, on September 17, 2014, the Court of Justice of the European Union ("CJEU") ruled that services provided by a head office to a fixed establishment that was part of a VAT group were subject to VAT, and that the VAT due must be paid by the VAT group as purchaser of the services. The facts were that Skandia America Corporation ("Skandia") was established in the United States and had a fixed establishment in Sweden, and the fixed

establishment was part of a Swedish VAT group. In 2007 and 2008, the US head office recharged (with a mark-up) externally acquired IT services to the Swedish fixed establishment, and the Swedish fixed establishment modified the IT and, in turn, recharged the IT costs with a mark-up to the other group companies (both within and outside the VAT group). The Swedish court requested a preliminary ruling from the CJEU on two issues

(a) Whether VAT was payable on the external services purchased by the head office that were allocated to the fixed establishment, given that the fixed establishment was part of a VAT group?; and
(b) If this was the case, whether the VAT reverse charge mechanism applied?

In its ruling, the CJEU held that services performed by the head office of Skandia in the United States for its fixed establishment in Sweden, which was part of a VAT group in Sweden, constituted taxable transactions for VAT purposes, and the services were taxable in Sweden. Further, the VAT group in Sweden was subject to Swedish VAT under the reverse charge mechanism. Reacting to this, according to Meijburg & Co, a group of tax lawyers in the Netherlands, the ruling implied that the services were not deemed to be performed between the US head office and the Swedish fixed establishment of Skandia, and rather, the services were deemed to be performed between the US head office of Skandia and the VAT group in Sweden, with the Swedish fixed establishment of Skandia being part of this VAT group in Sweden and thus services are provided between two separate taxpayers.[11]

From Skandia Case, intra-company services were taxable in Sweden, the country where the purchaser is resident, and for VAT purposes, the Swedish fixed establishment of Skandia was deemed to be part of a VAT group in Sweden, a different taxpayer than the US head office of Skandia, with the latter, as service provider, was therefore not regarded as a taxpayer with an establishment (fixed establishment) in Sweden. For this reason, the Swedish VAT payable was reverse charged to the purchaser, the VAT group in Sweden.

Subsequently, on October 30th, 2015, the Her Majesty Revenue Commissioners (HMRC) updated its Guidance on United Kingdom's Implementation of the Skandia case, by stating that intra-entity and intercompany flows may, from January 1st, 2016, would be subject to UK VAT.[12] Thus, in the
United Kingdom, as from January 1, 2016:

- Services made by overseas VAT-Grouped branches to its UK branch should be treated as supplies for VAT purposes (whether or not the UK branch was itself grouped). Under normal rules, these services would be subject to UK VAT under the so-called 'reverse charge' mechanism.
- Services provided by a UK branch to an overseas VAT-grouped branch would also be treated as supplies for VAT purposes; depending on the nature of those services, the UK branch would be entitled to recover VAT on these services.[13]

4. VAT Application To Imported Services

The current position of the law in Nigeria is that where professional services are imported into Nigeria, the local recipient of the professional services is obligated to pay "reverse charge VAT" to tax authorities irrespective of whether the foreign supplier has issued an invoice or not.[14] This is now stipulated by Section 36 of the Finance Act 2019 which now provides a new Section 10 of VAT Act thus:

Section 10. Registration by non-resident companies.

(1) For the purpose of this Act, a non-resident company that carries on business in Nigeria shall register for the tax with the FIRS, using the address of the person with whom it has a subsisting contract, as its address for purposes of correspondence relating to the tax.
(2) The FIRS may by Notice determine and direct Companies in the oil and gas sector to deduct VAT and remit to the FIRS
(3) a Non-Resident company shall include the VAT tax on its Invoices for the supply of taxable services
(4) The person to whom the services are supplied to in Nigeria shall withhold and the V AT tax to the FIRS in the currency of the transaction.[15]

To determine whether professional services would constitute "imported services," Nigerian courts will use the "destination principle" as the basis for deciding the location of performance/delivery of imported services.[16] In Vodacom Case, Court of Appeal[17] which settled the lingering issue in the following manner:

> Now does the fact that the non-resident company did not issue a VAT invoice absolve the appellant as the consumer of the VATable services render from paying the VAT?..... The Appellant contention is that the respondent cannot assess it for VAT in the absence of VAT invoice by a non-resident foreign company.

The Court of Appeal in its decision further reviewed the provisions of Sections 2 and 10 of the VAT Act held as follows:

> The parties are agreed on the dual duty imposed by Section 10 (2) of the VAT Act, one on the non-resident company to include VAT in its invoice and the other on the person to whom the goods and services are supplied in Nigeria to remit the tax. While one ought to follow the other, I am unable to agree with the Appellant that the duties are conjunctive. Where there is a failure to include the VAT in an invoice it does not bring to an end the liability to remit the VAT which has already kicked in by the stipulations of Section 2 of the VAT Act which mandatorily requires that VAT is to be charged and paid on all goods and services except those listed in the First Schedule to the Act.

On the whole, the Court of Appeal concluded that by all odds, these afford statutory backing for the assessment issued on the Appellant notwithstanding that the non-resident foreign company did not issue a VAT invoice. The duty on the Appellant to remit the tax remained sacrosanct. This issue was resolved in favour of the FIRS.

Unlike "exported services" which is expressly exempted from VAT in Nigeria, "imported services," which is only defined by Section 47 of VAT Act, will continue to attract VAT. Section 10(4) of the VAT Act mandates the Nigerian consumer of imported services to remit the VAT.[18] Similarly, the new Section 14(3) of VAT Act states thus:

> (3) A non-resident company shall include the VAT tax on its invoice and the person to whom the goods and services supplied to within Nigeria shall remit the VAT tax to the FIRS in the currency of the transaction.[19]

As to the meaning of the phrase "supplied in Nigeria" in the context of the VAT Act, Section 46 of VAT which defined "supply of services" to mean "any service provided for a consideration" and 'supply of goods to mean:

> any transaction where the whole property in the goods is transferred or where the agreement expressly contemplates that this will happen and particularly includes the sale and delivery of taxable goods on hire or leasing, and any disposal of taxable goods.

The above definitions of supply of goods and service have a common feature, namely the movement of the goods or services from the supplier to the consumer for use, and the acts of sale and delivery are acts of supply clearly different from production, with sale and delivery taking place when the goods or services are received and paid for by the consumer.

The cardinal principle guiding the application of VAT the world over is encapsulated into two, i.e., "the destination principle" and "the origin principle," and either of these principles is usually incorporated into tax laws. Some jurisdictions apply both principles. Nigeria applies the "destination principle" as embodied under Section 10(4) of the VAT Act:

> Thus, the phrase "supplied in Nigeria" as used in Section 10(2) underscores the applicability of the destination principle in Nigeria, and the destination principle applies in Nigeria along with the application of the rules of the jurisdiction of consumption.[20]

Thus, the Nigerian VAT law jurisprudence expressly shows that Section 10(4) of the VAT Act creates two statutory duties, to wit:

(1) the duty of the non-resident company to include the tax in its invoice, and
(2) the duty of the person to whom the goods or services are supplied in Nigeria to remit the tax.

These duties are separate, distinct and independent of each other. The duty of the supplier of services to issue VAT invoice under Section 10 of the VAT Act has been held to be solely enacted for proper record, accountability and ease of compliance/enforcement, and not conditions precedent for liability to pay VAT. Therefore:

> The very moment the services were received in Nigeria by the Nigerian company, the liability to account for VAT arose even with the failure of

> non-resident company to include VAT in its invoice or did but under assessed it. Simply put, as separate duties, the non-performance of one does not detract from the duty of the other, and the non-registration or non-issuance of invoice for VAT is not fatal to the remittance of VAT by a taxable person because Section 15(1) of the VAT Act compels a taxable person to render account of his transaction.[21]

If Section 10 of the VAT Act were to be interpreted to prevent VAT collection when the foreign supplier of services fails to register for VAT and fails to raise VAT invoice, then a recipe for tax evasion would be brewed as the consumers of services in future cases would only need to ensure that their non-resident suppliers do not comply with Section 10 for them to escape VAT on the services. Section 10 of the VAT Act is revenue oriented and must be construed liberally in favour of revenue.[22] The decision of the Court of Appeal in Vodacom's Case appears to have settled this principle. The above position is supported by Offshore International SA vs FBIR,[23] where it was held that for tax purposes, a company does not even have to be ·registered in Nigeria and does not have to be resident in Nigeria before it can be subjected to tax. The Vodacom FHC court also held that the non-resident supplier was carrying on business by supplying services while using the fluid and flexible modern techniques:

> On the issue of whether NSS carried on business in Nigeria, one of the cardinal features of VAT is flexibility, this means the systems for taxation should be flexible and dynamic to ensure that they keep pace with technological and commercial developments. In a world driven by Information and Communication Technology making e-commerce (virtual business) trendy, quickly dispensing with the actual presence of the parties, a businesses located anywhere in the world can supply services (usually intangible) to everywhere and anywhere on earth. In such transaction, there are no customs controls to impose the VAT at importation. This is usually done without physically being in the place where the supplied services are received by the contracting party. In my considered view "carries on business in Nigeria" in Section 10(1) VAT Act includes a single contract of supply of goods and services into Nigeria. The contract could lead to continuous transactions but not necessarily so. In short, where an entity outside Nigeria contracts to make a supply in Nigeria to a person in Nigeria such entity carried on business in Nigeria for VAT purposes, and qualifies as a non-resident company carrying on business in Nigeria. The Tribunal had held that NSS did not carry on business in Nigeria, this ·is a misdirection arising' from the perception that business can only be carried on in Nigeria if the company is resident in Nigeria. All that is to be considered in finding out whether an entity is carrying on business in Nigeria from outside Nigeria or not for the purpose of VAT is the occurrence of a supply to' a person in Nigeria. Physical presence is not a condition to carrying on business in Nigeria for the purpose of Section 10 of the VAT Act.[24]

5. Value Added Tax Exemption Eligibility Test for Professional Services

Generally speaking, VAT is chargeable on the "supply of goods and services" other than those exempted in the Act.[25] A close perusal of the Schedule to the VAT Act containing the list of exempted goods and services shows that the following professional services are VAT a. exempt.

a. Medical services[26]
b. Educational services[27]
c. Banking services rendered by microfinance bank, people's bank and mortgage institutions[28]

From the content of the VAT Act, one is tempted to say that a professional service will not be VAT-able once it falls within the exemption as there is no express criteria to determine eligibility especially when such service is provided by a non-expert. One finds it irresistible to probe further on the determinant factors. Is it the service itself or the person that renders the service that makes the service qualify as VAT exempt?

The Court of Justice of the European Union (CJEU), in the case of Kugler,[29] has held that the exemption granted to certain classes of professional services is not dependent on the legal form of the taxable person supplying the medical services. Therefore, the exemption can apply where services are supplied through such an entity.

Also, it is not just the status of the person providing the service that determines whether it is exempt from VAT but also the actual service that is being provided and the purpose for which it is being provided. For instance, the full range of medical services carried out for the purposes of protecting, including maintaining or restoring a patient's health, or diagnosing, treating, and if possible, curing diseases and health disorders will qualify for exemption, and the qualifying services will also include the following when provided by a recognised medical professional:

a) Post-offer of employment medical examinations including medical fitness to operate machinery and undertake manual work;
b) Health surveillance services, including sight and hearing tests;
c) Health screening, stop smoking, and stress management programmes;
d) Cosmetic surgery procedures where it is clearly shown that they are required to maintain or restore a patient's health or to treat a patient's disease or illness
e) Vaccination programmes to protect employees where there is a high risk of transmission of infectious diseases.[30]

Thus, in Peter d'Ambrumenil and Dispute Resolution Services Ltd v Commissioners of Customs & Excise[31] the court allowed an exemption claimed on medical tests prescribed by a medical practitioner but carried out by a third-party, such as a laboratory, which allow patients to be observed and examined before it becomes necessary to diagnose care for or heal potential illness. However, in Lu PCase,[32] the CJEU held that the following activities did not qualify for exemption as medical services:

i. Genetic tests carried out by a doctor to establish paternity;[33]
ii. General care and domestic help provided as part of an outpatient service;[34]
iii. Provision of a doctor's report on a person's state of health for the purposes of a war or disability pension claim or of personal injury litigation given that the principal purposes of the service effected is to provide the third party with the necessary element for taking a decision and the main purposes of such service is not the protection of that persons health.[35]

The above decisions of the Court have the effect of denying VAT exemption for services that do not have the effect of protecting a patient's health or diagnosing, treating, or curing health disorders.[36]

There is also the issue of composite supplies, i.e., where there is a mixture services supplied, and where some parts of the supplied services qualify for exemption, with some parts not qualifying. Generally, a composite supply is defined in the VAT Act as a supply made by a taxable person to a customer comprising two or more supplies of goods or services or any combination of these supplied in conjunction with each other, one of which is a principal supply. In the case of a composite supply the tax chargeable on the total consideration which the person is entitled to receive for that composite supply shall be at the rate appropriate to the principal supply but if the principal supply is exempt then tax shall not be chargeable on that composite supply.[37] For instance, where a registered medical practitioner supplies a service that is not recognised under the Nigerian Medical and Dental Act,[38] such as Homeopathy or Acupuncture:

> then that supply will, when supplied separately or when supplied in conjunction with a supply of goods, not qualify for exemption but will be treated as taxable. However in certain circumstances the whole supply, consisting of the exempt medical service and the taxable service, may qualify for exemption if it can be shown that a composite supply, of which the exempt medical service is the principal supply, is involved.[39]

If a qualifying medical professional makes a composite supply for a single consideration of exempt services and taxable services and the exempt services are regarded as the principal supply then the entire supply is treated as exempt:

> An example would be a doctor provides qualifying professional exempt medical services and as part of that service also supplies a taxable homeopathic service. If it can be shown that the homeopathic service is supplied as part of a composite supply of exempt and taxable services and the exempt service is the principal supply then the entire supply can be treated as exempt.[40]

6. Conclusion

After a long interlude in the examination of the scope of VAT law in Nigeria, it appears that the recent repositioning of the Nigerian government to focus on non-oil exports as the source

of federal revenue will bring into fore the central role of VAT as the most reliable and easiest tax instrument in Nigeria. It is also apposite that the wide acceptance and usage of Internet and Computer Technology will now make cross-border supply of services—especially professional services more fluid and transferable.

7. Recommendation

The VAT Act has not expressly stated the reason for exempting medical service and banking services rendered by certain classes of banks. The ultimate objective and direct beneficiary of the services appear to be driven by the concept of public interest. To this end, an amendment of the VAT Act is recommended first to set a standard in determining the eligibility for such an exemption as in the European Union Model.

Secondly, the amendment should be extended to expand the list of exempted professional service to include any service directly related to enforcement of fundamental human right provided in the 1999 Constitution such as legal representation or services to client only for the enforcement of fundamental human rights in courts.

It is therefore high time that Nigerian tax stakeholders reviewed the extant VAT laws and regulations, with particular focus on application of VAT to professional services so as to bring Nigerian VAT laws at par with contemporary VAT laws worldwide.

ENDNOTES

1. Cap. V1, Laws of the Federation of Nigeria, 2004 (as amended by the VAT (Amendment) Act, 2007)
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6. Kenya VAT Appeal Tribunal, Appeal No. 11 of 2013.
7. Value Added Tax Act, Cap 476, Laws of Kenya.
8. Unreported judgment of the Tax Appeal Tribunal (Lagos Zone) delivered on Wednesday, November 13, 2019 in Appeal No. TAT/LZ/VAT/019/2018.
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10. See, the September 17th, 2014 decision of the Court of Justice of the European Union ("CJEU") in ***Judgment in Skandia America Corporation (C-7/13). (Skandia).***
11. Meijburg& Co, "Judgment in Skandia America Corporation (C-7/13)," 22 September 2014. Available at: https://meijburg.com/news/judgment-in-skandia-america-corporation-c-7-13. Last accessed on February 1st, 2018. (Meijburg).
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13. *Ibid.* at 2.
14. Unreported decision of Honourable Justice Babs O. Kuewumi in ***Vodacom Business Nigeria Limited vs Federal Inland Revenue Service (FIRS)*** before the Federal High Court (Lagos Division), Suit No.: FHC/L/4A/2016, dated December 19, 2017. (Vodacom FHC)
15. This reproduction is the author's surmise of Section 10 of VAT Act.
16. ***Vodacom FHC*** expressly adopted the OECD (2017), International VAT/GST Guidelines (OECD Publishing, Paris, April 12, 2017). Available at: http://dx.doi.org/10.1787/9789264271401enInternational. Last accessed February 2nd, 2018. (OECD Guidelines).
17. The Court of Appeal sitting in Lagos Division in the Appeal No:-CA/L/556/2018 delivered its judgment on the 24th June, 2019.
18. Finance Act 2019 (n 2) at Section 36.
19. *Ibid.* per Finance Act, at Section 37.
20. OECD Guidelines (n 29).
21. ***Vodacom FHC*** (n 27).
22. ***Phoenix Motors Ltd vs NPFMB*** (1993) NWLR (Pt 272) at 731.
23. (2011) 4 TLRN 58.

24. ***Vodacom FHC*** (n 27) at 25-26.
25. Section 2 of the VAT Act, 2004 (as amended)
26. Item 1 of Part II of the First Schedule to the VAT Act, 2004 (as amended)
27. Section 47 of the Finance Act 2019 amended paragraph 4 of the Part II of the First Schedule to the VAT Act, 2004 (as amended) and substituted with a new Paragraph 5. The educational services exempted are limited to tuitions relating to nursery, primary
28. Section 47 of Finance Act, 2019 which amended Paragraph 2 of the First Schedule of VAT Act,
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32. C-106/05.
33. ***D Case*** C-384/98
34. ***Kugler Case*** C-141/00
35. ***Unterpertinger***Case C-212/01.
36. ORC (n 39) at 2-4.
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38. Cap M8, Laws of the Federation of Nigeria (2004).
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CHAPTER 8

APPLICATION OF VAT TO REAL ESTATE TRANSACTIONS: EXAMINING THE EFFECT OF RECENT TAX REFORMS

Abstract

The proper application of the Value Added Tax[1] (VAT Act) to real estate transactions in Nigeria has been mired in controversy. The general belief is that real estate properties, and the rights attached to them, constitute land. The inference therefore is that since land is neither good nor service, supply of real estate in terms of building, sale or lease does not constitute supply under the VAT Act. However, the Federal Inland Revenue Service (FIRS) actually issued a circular in 1997[2] (1997 FIRS VAT Circular) subjecting commercial rent[3] to VAT while exempting rent on residential buildings. Basically, two earlier judicial decisions constituted the case law in Nigeria on whether real transactions are liable to VAT. One of the decisions held that rent from lease of a commercial real estate property is subject to VAT, while the second held that sale of serviced land constitute supply so as to render the full value of the land subject to VAT. More recently, there were also two conflicting decisions on VAT treatment of real estate transactions. Subsequently, amendments to the VAT Act vide the Finance Acts 2019 and 2020 has provided much needed clarity. This article examines the nature of the real estate industry in Nigeria with a historic perspective on the VAT treatment of real estate transactions, exemplified by judicial decisions. . A review of the two earlier judicial decisions shows that the two decisions are not correct in the light of clear statutory provisions. The two latter decisions reached divergent conclusions: one affirms that VAT is inapplicable to real estate, whilst the other held to the contrary. The controversy has now been settled by statutory amendments re-defining "goods" and "services" whilst exempting transactions involving transfer of interest in land from VAT.

1. Introduction

The VAT Act whose enforcement commenced in 1993 has been viewed as one of the most successful taxes in Nigeria in terms of administrative ease and revenue yield.[4] According to a learned author, since its introduction, the relative success of VAT in Nigeria has surpassed the expectations of all skeptics, including the International Monetary Fund (IMF) and emerged as a significant source of income for all the levels of government.[5]

However, the application of the tax to transactions in the real estate industry has been fraught with controversies. The conundrum has its foundation on a conglomeration of factors, ranging from hazy statutory drafting to lack of understanding or in-depth review of the provisions of the VAT Act in the course of judicial determination of disputes arising from application of the tax to real estate transactions. Those factors constitute part of the

challenges militating against the proper administration and implementation of the tax. Recently, Nigeria was advised by the IMF to increase its VAT rate on the premises that the current rate of 5% is one of the lowest in the world.[6] The Nigerian government has heeded this advice by carrying out extensive statutory tax reforms,[7] including amendment of section 4 VAT Act which increased the VAT rate from 5% to 7.5%. This does not detract from the view that Nigeria needs to also focus on widening the tax base, as rather than increment of the tax rate.

One of the means of widening the VAT base is proper application of the provisions of the VAT Act to real estate transactions. This Chapter seeks to review the current state of VAT application to real estate transactions as reflected by the decisions in four cases namely **Federal Board of Inland Revenue v. Ibile Holdings**[8] **(Ibile Holdings)**, **Momotato Nigeria Limited v. UAC Property Development Company Plc,**[9] **(Momotato), Ess ay Holdings Nigeria Limited v. FIRS**[10] **(Essay Holdings)** and **Chief J.W Ellah, Sons & Company Limited v. FIRS**[11] **(Ellah Sons**) While **Ibile Holdings** was decided by the defunct VAT Tribunal, Momotato was decided by the Federal High Court (FHC). The two latter decisions in **Ess ay Holdings** and **Ellah Sons**, were delivered by Lagos and Benin Zones of the Tax Appeal Tribunal (TAT). However, of all the cases, **Momotato** case can arguably be referred as the current case law on application of VAT to real estate transactions in Nigeria, as at the date of this article. This is because in the cases of **Stabilini Visinoni v. FBIR**[12] and **Cadbury v. FBIR**,[13] the Court of Appeal (CA) held that the VAT Tribunal was unconstitutional. It is therefore doubtful if the decision of the defunct VAT Tribunal could be held to possess any legal authority. **Momotato** on the other hand was delivered by the FHC, which is superior to the TAT. The view that not having been appealed against, **Momotato** still remains the case law, is moderated by another subsequent FHC decision in **CNOOC E&P Nigeria Limited v Attorney-General of the Federation & 2 Ors**[14] **(CNOOC**) before Finance Acts 2019 and 2020 amendments, crown the definitive tax treatment.

2. Definition of Terms

The VAT Act defines VAT as tax payable on supply of all goods and services other than those goods and services, listed in the First Schedule to the Act.[15] Conundrum simply means, mystery, puzzle or confusion. It best describes the state of statutory provisions on VAT *vis a vis* the judicial decisions on VAT in Nigeria today generally,[16] and particularly with respect to the real estate sector. To put it in the right perspective, most of the cases examined in this article on VAT Act's application to real estate transactions are out of sync with the provisions of the VAT Act. What is urgently needed with respect to VAT in Nigeria is statutory and judicial realignment that will hopefully lead to correct application of the tax and the attendant positive revenue yield. It is indeed time to carry out an informed judicial reconstruction of the VAT system in Nigeria as it applies to real estate industry.

3. An Overview of the Nigerian Real Estate Industry

The Nigerian real estate industry is a large one. According to a report released in 2015:

> The Nigerian Real Estate Sector has recorded steady and consistent growth

> over the last four years becoming one of the greatest contributors to the Nation's rebased GDP from the non-oil sector - having contributed 8.03% and 11% in 2013 and 2014 respectively. The market which is currently valued at approximately ₦6.5 Trillion is estimated to grow at an average of 10% over the next few years. The major growth drivers in the sector have been credited to: an increased inflow of foreign investment (especially from South Africa, MEA and the United States); increased institutional investment from local companies including PFAs and Mutual Funds; the growing population of High Net worth Individuals; and the targeted intervention of the Federal Government in the housing finance sector.[17]

The real estate industry consist of companies and individuals involved in the purchase, ownership, management, leasing, rental and/or sale of real estate for profit. They acquire lands, build on them and then either sell or lease out the developed properties. Some of the companies also offer facilities management with the attendant services. Real estate could take form of commercial, residential or industrial estate. The analysis of the real estate industry for VAT purposes will not be complete without an overview of various transactions involved in the industry. A long time before erection of structures on land, several important steps are usually taken involving appointment of some professionals particularly lawyers, surveyors and architects. The lawyers conduct searches at the land registry office, draft property acquisition agreements and perfect the title of the real estate company over the land. The surveyor will be saddled with the responsibility of mapping out the exact location of the land and preparing the survey plan. The architect on his part will prepare a plan of the intended structure. In the course of developing the building on the land, other professionals including engineers, quantity surveyors and so on will be employed. Another area where professional services would be required is the process of raising fund for the development. Basically, the developer may raise the fund for the real estate development.

The majorly recognised real estate financing methods used across the world are: Joint Venture, Equity and Debt Financing, Sale-lease Back Financing, Advance Payment of key money and Sale of Securities.[18] Any of these methods will usually require hiring professionals with finance background. Upon conclusion of the development, other facility management professionals and agents would be engaged to ensure proper post construction management of the property.

4. The Policy Thrust of VAT on Real Estate in Nigeria

The general policy thrust behind the VAT is to, among other aims, ensure a paradigm shift from direct to indirect taxation for economic growth.[19] The introduction of VAT is one of the means of achieving this aspiration. However, with specific reference to application of VAT to real estate transactions, the policy is not quite clear. According to the 1997 FIRS VAT Circular , rent on residential accommodation or residential real estate is exempted from VAT[20]. The implication therefore is that rent on commercial real estate would be subject to VAT. The grounds for subjecting rent from commercial estate to VAT while exempting residential estate

is not clear, as the VAT Act does not differentiate between rent from residential property and that from commercial real estate. However, it has been held that the Circulars issued by the FIRS have no force of law and are at most advisory.[21] Moreover, clearly the FIRS has no power to exempt anyone from paying tax save as stipulated by the law.

5. International Perspectives on VAT Application To Real Estate

Various countries impose taxes based on the statutory provisions within those countries and VAT is not an exception. In the United Kingdom, VAT application to real estate is not straightforward. VAT is charged on taxable supply of any goods or services in the UK.[22] Taxable supply is a supply of goods or services made in the United Kingdom other than an exempt supply[23]. Supply in the UK Act includes all forms of supply, but not anything done otherwise than for a consideration. Anything that is not a supply of goods but is done for a consideration (including if so done, the granting, assignment or surrender of any rights) is a supply of services.[24] Consequently, the grant, assignment or surrender of a major interest in land is a supply of goods for VAT purposes.[25] However, supplies of land and buildings, such as freehold sales, leasing or renting, are normally exempt from VAT. This means that no VAT is payable, but the person making the supply cannot normally recover any of the VAT incurred on their own expenses, except where he exercises an option to impose VAT.[26] Commercial property owners can opt to charge VAT at the standard rate (currently 20%) when selling or leasing their property. When a vendor or landlord opts to tax a property, they must usually charge VAT on all supplies they make relating to that property. Therefore, they must charge VAT on the sale or rentals.[27] Sale, lease or rent of building for residential or charitable purposes are exempted from VAT.[28]

Similar trend exists in Canada and New Zealand, where the sale and rental of immovable property are taxable in principle, but residential rents (and rental values) are exempt, as is the sale of previously occupied residential property. "This implies that the construction, alteration, and maintenance of all buildings are taxable. So is the rental of business accommodations."[29]

Generally, European Union and Organization for Economic Cooperation and Development (OECD) countries tax real estate as follows:

a. Construction of real estate and building materials are subject to VAT, though with slight variation on rates.
b. All members exempt rent from residential building from VAT except Australia that subjects rents from residential building to VAT at 10%.[30]
c. All the countries exempt the sale of previously occupied residential real estate; and most countries the sale of other real estate, too from VAT. Six countries (Canada, Iceland, Japan, New Zealand, Spain, and Turkey), however, tax the sale of other (non-residential) real estate under their VAT regimes.[31]

It should be noted however, that the practices as obtained in these countries are supported by their statutory provisions on VAT and cannot be applicable to Nigeria where our VAT Act

does not have similar provisions. The need to avoid heavy reliance on foreign definition in describing our tax laws was hinted by the Supreme Court (SC) in **Attorney-General of Ogun State v. Aberuagba**[32] where the SCourt held as follows:

> I think the meaning given to the word by other common law countries would hardly assist in finding the answer to the question because each meaning was decided within the context of the Constitution of the country concerned. Hence there is no universal meaning of the word. Each case must be viewed through the spectacles of its constitutional perspectives.

It therefore important to view the application of VAT to real estate in terms of the law as applicable in Nigeria under the VAT Act. Next is the review of Nigerian case laws on VAT application to real estate transactions.

6. Review of the Nigerian Case Laws on VAT Applications to Real Estate Transactions

FBIR v. Ibile Holdings - VAT on Rents

The first case to be reviewed is **Ibile Holdings** which is a decision on whether rents from lease of real estate property should be subject to VAT in Nigeria. In this case, the Respondent (Ibile Holdings) was a property management company whose business included building, selling and renting of properties. The Appellant carried out routine VAT monitoring/compliance exercise at the premises of the Respondent, following which a VAT Assessment Notice was issued on the Respondent. Upon failure of the Respondent to pay the assessed VAT sum, the Appellant instituted this matter at the VAT Tribunal to recover the money.

In its argument, the Appellant contended that since the Appellant was carrying on the business of property management, it was dealing on 'VATable' goods and service. According to the Appellant, in VAT, consumers are taxed on the value added and the act of building on a land, sale and rental of buildings, constitute value added. The Applicant further contended that VAT is a consumption, multi stage tax, increase in the value of goods and services in the process of their production and is on the amount of value a firm contribute to a good or services by applying its own factors of production. Referring to Section 42 of the Act which defined "supply" and "taxable person",[33] the Appellant argued that the business of the Respondent which is exploitation of land in form of building amounted to supply of goods and services and thus VATable; and that since the type of goods and services of the Respondent were not exempted under the VAT Act, they were engaged in supply of VATable goods and services.

The Respondent on its part argued that it was impossible to apply VAT to rent, since there is no input VAT at the intermediate level with respect to rent and that the absence of multi stage characteristics meant there was no VATable transaction. The Respondent also contended that the relationship between landlords and tenants on the property let out could not be described as goods and merchandise. The Respondent concluded as follows:

a. A rentable property is not a good or merchandise as described by the Appellant.

b. Income from rent whether for private or commercial use is taxable income but not subject to VAT.
c. Only estate agency services and services charged for maintenance of property are VATable and that even in such cases, the cost of input has to be considered.
d. Income from rent already attracted 10% WHT and should not at the same time attract VAT.

The VAT Tribunal in deciding the matter based its judgment on resolution of the following issues, namely: interpretation of "supply of goods" and whether rent on commercial real estate property could safely come under "supply of goods" for the purpose of VAT; whether the features of VAT as defined are applicable in totality to rent within the context of the VAT Act and whether a situation whereby output VAT is charged with no corresponding input tax, can be described as VATable.

In its decision, the Tribunal held as follows:[34]

> We observe that the major business of the company is not buying and selling land but building, selling and renting of properties. We are of the view that these activities constitute the taxable goods of the company which come under the purview of the provisions of section 42 which unequivocally spell out the supply of goods to include sale and delivery of taxable goods used outside the business, the letting out of taxable goods or hire or leasing and any disposal of taxable goods.

The VAT Tribunal further held that there is nowhere in the VAT Act where the goods or services offered by the Respondent were expressly exempted from VAT. It also held that there was no provision in the Schedule exempting rent from residential building from VAT. In conclusion, the Tribunal held as follows:

> We therefore uphold the applicant's submission that VAT is chargeable on commercial rents collected by the company on its commercial properties together with service charges from 1st January 1996 to 31st December 2000.

The effective implication of the Tribunal's decision is that building, selling and renting of properties constitute taxable goods under the VAT Act, thereby rendering rent subject to VAT. Arguably, the description of building, selling and renting of properties as goods for VAT purposes was not correct under the old VAT Act (before amendment by Finance Act 2019). The VAT Act in the same section 42[35] referred to by the VAT Tribunal in its decision, defined supply of goods as:

> "supply of goods" means any transaction where the whole property in the goods is transferred or where the agreement expressly contemplates that this will happen and in particular includes the sale and delivery of taxable goods or services used outside the business, the letting out of taxable goods on hire or leasing, and any disposal of taxable goods;

Unfortunately, as at the time of the decision, the VAT Act did not define goods and none of the parties in the matter sought to define goods or addressed the Tribunal on the meaning of goods for the purposes of VAT Act in that case. Some years after the decision in **Ibile Holdings**, the FHC was faced with determination of "goods" for VAT purposes in **CNOOC** where it held as follows:

> I refer in particular to the definition of "goods" by Black's Law Dictionary, Seventh Edition, as; "Items of merchandise, supplies, raw materials or finished goods. All things (including especially manufactured goods) which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities and things in action." (Underlining provided). I also refer to the Lagos State Sale of Goods Law, 2003 cited by the Learned Senior counsel to the Plaintiff which defines "goods" to include: "All chattels personal, other than things in action and money, and includes emblements, industrial growing crops, and things attached to and forming part of the land which are agreed to be severed before sale or under the contract of sale". This definition is in tandem with the definition of goods under the UK Sales of Goods Act 1979 which by its section 61 (1) defines "goods" to include: "All personal chattels other than things in action and money, and in Scotland all corporeal moveables except money; and in particular "goods" includes emblements, industrial growing crops and things attached to or forming part of the land which are agreed to be severed before sale or under the contract sale ...." And the word "Service" is also defined by Black's Law Dictionary as an intangible commodity in the form of human effort, skill or labour.[36]

Definitely, from the definition given above, building, selling and letting of properties from the highlighted definitions of "goods" and "supply of goods" cannot and do not constitute goods as the Tribunal would have us believe. At best, they can be described as services. Moreover, the holding that "rent is VATable" because building, selling and letting of properties constitute taxable goods reveals a disconnection between the premises and conclusion of the judgment. Rent simply means consideration paid usually periodically for the use of, or occupancy of property.[37] At best, rent is an income derived from letting out a property. Therefore, it is not derived from either building or selling a property. The income derived from building a house may be wages or construction fees, but never rent. On the other hand, the income derived from selling a property is a profit after the expenses have been deducted.

Therefore, at best, the Tribunal should have held that rent is VATable because letting is a taxable good. This is however assuming that the reasoning of the Tribunal was correct. Having linked rent only to letting which was one of the activities of the Respondent in the matter, the next question would be whether letting of properties constitutes supply of goods and services for the purposes of VAT which would then render the rent from letting of the property liable to VAT.

The VAT Act defined supply of goods to include letting of taxable goods. The question then would be whether letting out a real estate property constitutes supply of taxable goods. Specifically, does real estate property constitute taxable goods? This question brings us to the same issue that the Court faced in **CNOOC v. AG of the Federation & 2 Ors.**[38] attached to, or erected on it, excluding anything that may be severed without injury to the land. According to the author,[39] "Land (especially freehold) became real property because only it could be specifically recovered…." He concluded that the definition of land includes buildings when he stated that:

> Generally speaking at common law, land covers the earth surface (i.e the top soil), the subsoil, things attached to the land e.g structures,[40] crops etc, and other incorporeal hereditaments enjoyed on land.

There are also statutory definitions of land. In the **Interpretation Act**,[41] land is defined as including any building and any other things attached to the earth or permanently fastened to anything so attached but does not include minerals. Statutory definitions also make it clear that land includes interests on land (incorporeal hereditaments) such as rent. Thus the Property and Conveyancing Law defines land to include incorporeal rights which has been defined to include profits and rents.[42]

The basic implication of these definitions is that generally, real estate constitutes land under common law and statutes on real estate. Therefore, the letting of real estate does not constitute supply of VATable goods and services, as land is neither good nor service. Consequently, it is arguable that the VAT Tax Tribunal was not correct to have held in **Ibile Holdings** that rent from letting out of real estate property is subject to VAT on the ground that building, letting and selling of real estate property constitute VATable goods and services. However, this position may not be totally correct, as will be revealed later. Latter reviews will show that the decision suffered more than anything else, from lack of proper analysis and applications of the provisions of VAT Act.

Momotato v. UACN Property Development Company Plc -VAT on Supply of Serviced Land

The second decision under review is **Momotato**, which was on whether supply of serviced land should be liable to VAT. In that case, the Plaintiff purchased a piece of serviced land from the Defendant for ₦10 Million. The Plaintiff, however, refused to pay the VAT on the transaction in the sum of ₦0.5 million as demanded by the Defendant, on the ground that land was not goods or services subject to VAT. The Defendant, however, argued that the land in question was a serviced or developed land as the Defendant had provided sand filling, tarred road network, electricity supply, water supply, telecommunication facility and an estate office which all made the sale a supply of service and therefore, liable to VAT. The Plaintiff then instituted this action seeking declaratory and injunctive reliefs to restrain the Defendant from demanding or collecting the demanded VAT from the Plaintiff. The main argument of the Plaintiff was that land being neither good nor service could not be a VATable. The Defendant on the other hand argued that the land sold to the Plaintiff included services such as roads, lighting and other infrastructures and that this factor rendered the transaction between the

parties subject to VAT.

The Court while agreeing that land does not constitute good, held that services and development rendered on land may be subject to VAT. Based on these premises, the Court declared that real estate development qualifies as a service subject to VAT and consequently dismissed the Plaintiff's claims. According to the Court:

> No mention of transaction relating to businesses of real estate development is made in the excluded list. It is common knowledge that there is a lot of economic profit in the type of defendant's business. Applying the legal maxim relied upon by both counsel that *"expressiouniusest exclusion alterius"*, it is my view and indeed I so hold that since the type of business of the defendant which is improvement of land to sell for profit has not been specifically excluded by the VAT Act, it can come under supply of services which is VATable.[43]
>
> In the case of Udoh v. O.H.M.B. (supra) referred to by Mr Oyetibo (SAN), the Supreme Court held inter alia that:
> "it is a well-settled principle of construction of statute that where a section names specific things among other possible alternatives, the intention is that those not so named are not intended to be included". I hold the view that since services provided to develop land such as the defendant did in this case have not been specifically exempted in the Act, it will amount to restrictive interpretation to so imply. I hold that the transaction is subject to VAT.

Therefore, in dismissing the suit of the Plaintiff, the Court held that the sale of a serviced plot would attract VAT on the full value of the serviced land. The grounds for the decision is that the VAT Act did not exclude the business of real estate development or services provided to develop land from being subject to VAT. In other words, the service of real estate development is not contained in the Schedule to the Act as part of the exempted goods and services. While the grounds or reason for the judgment was sound and commendable, the final decision of the court in holding that the full value of the serviced land is subject to VAT was incorrect. There should have been an attempt to distinguish the services, which are subject to VAT from the land itself which is not subject to VAT. This is because there is a difference between services offered with respect to the land in form of provision of infrastructures and other amenities and the land itself. Their values are also distinguishable through keeping of proper records. The services are VATable but the land itself is not. It would therefore be wrong to impose VAT on the value of land and services offered in improving or developing the land itself. This was akin to imposing tax on items or activities outside the contemplation of the VAT Act.

Chief J.W Ellah, Sons & Company Limited v. FIRS -Lease of Commercial Properties is Subject to VAT

The Appellant, which is engaged in leasing and maintaining properties, was served by the

Respondents with tax assessments including assessments for non-remitted VAT. The Appellant instituted the appeal to challenge the VAT assessment among others.

The Appellant argued that the Respondent erroneously assessed the Appellant for VAT on commercial letting or leasing of premises. According to the Appellant, commercial letting of premises constituted transfer of choses in action which is not supply of goods and services, and therefore not subject to VAT. Unfortunately, the TAT in its judgment did not outline the argument of the parties in this appeal. However, in its judgment, the TAT, after reviewing the various provisions of the VAT Act held that commercial letting of properties was subject to VAT. In arriving at its judgment, the Tribunal reviewed the definition of VAT, supplies and supplies of goods and services under VAT Act. The Tribunal also relied on the 1997 FIRS VAT Circular. According to the TAT, the definition of VAT in Section 1 VAT Act shows that VAT is applicable to supplies of goods and services except those that are expressly exempted under the 1st Schedule to the Act. In other words, if a supply of goods or services is not listed as exempted under the 1st Schedule, such supply would be liable to VAT.

Also, after reviewing the definitions of supplies, supply of goods and supply of services, the TAT held that supply of goods includes letting out goods on hire or leases. According to the Tribunal "From the above, it is obvious that commercial building where a charge, fee rent or any other consideration is payable is subject to VAT whereas domestic or residential building in our opinion are not VATable".[44] Despite recognising that FIRS Circulars do not have the force of law, the Tribunal also relied on the provisions of the 1997 FIRS VAT Circular which exempted rental incomes from residential buildings while subjecting rents from commercial building to VAT. Finally, the TAT cited **Ibile Holdings** in which the defunct VAT Tribunal held that "building, selling and renting properties which constitute commercial rents collected from commercial properties are subject to VAT".

The challenge with the Tribunal's judgment is that it limited its reasoning to definitions of supplies and supplies of goods and services under the VAT Act, without seeking to determine whether letting of properties constitutes supply of goods and services. There was no determination of what constituted goods and services under the VAT Act. If the Tribunal had adverted its mind to this important fact, it would have realized that letting out of properties involves only transfer of interest in land. This interest is in form of intangible rights known as choses in action which has been held by the FHC in **CNOOC** to be neither goods nor services.

In **CNOOC**, the Plaintiff sought to challenge the attempt by the FIRS to subject transfer of interests in an Oil Mining Lease (OML) to VAT. The Appellant in its argument asserted that transfer of interest in an OML did not constitute transfer of goods and services so as to be subjected to VAT, since the interest in OML is neither good nor service. The Defendant on the other hand argued that there was no express exemption of transfer of interest in OML in the Schedule to the VAT Act. The FHC in its considered decision recognised that there was no definition of goods and services in the VAT Act. Relying on the definition of goods and services under the Sale of Goods Law of Lagos State, the Court held that from the definition of

goods under the laws, an interest in OML does not qualify as a goods. The Court also considered the definition of services and held that the interest does not constitute services.

It was not clear whether the FHC decision in **CNOOC** was cited to the TAT in **Ellah Sons.** However, there seemed to be an allusion to **CNOOC** at page 80 of the TAT's judgment, where the Tribunal recognised that the Appellant had argued that commercial leases are not VATable, because they are transfer of 'choses in action'.[45] It is therefore strange that the TAT failed to consider the decision of the FHC which is a superior court on a matter before it.

Ess-ay Holdings Limited v. FIRS - Rents from Lease of Properties are not Subject to VAT
The Appellant (Ess-ay Holdings) is a Nigerian company which develops real estate for leasing to tenants for both commercial and residential purposes.
Following a tax audit, the Respondent assessed the Appellant for VAT on incomes derived by the Appellant from the Appellant's commercial tenants. Upon the Respondent's refusal to amend the assessment after the Appellant's objection, the Appellant instituted this appeal to challenge the VAT assessment.

The main issues for determination in the appeal were whether rental incomes are liable to VAT and whether the provision of the 1997 FIRS VAT Circular which seeks to exempt only rents from residential properties from VAT, is valid.

The Appellant argued that rental incomes, whether residential or commercial, are not liable to VAT as the transactions giving rise to them did not constitute supply of goods and services under the VAT Act. It further argued that VAT must be administered in accordance with VAT Act and not pursuant to circulars issued by the FIRS. Thus, the provisions of the 1997 FIRS VAT Circular is null, void and of no legal effect whatsoever.

On the other hand, the FIRS as the Respondent argued that real estate properties are not in the list of exempted items in section 3 and First Schedule VAT Act and as such they are subject to VAT as set out under relevant provisions of the VAT Act. The FIRS also maintained that the 1997 FIRS VAT Circular is valid because section 38 VAT Act empowers the Minister to amend, vary or modify the Schedule to the VAT Act and section 44 VAT Act also enables the Minister to donate this power (including the power to issue the said FIRS Circular), to the FIRS.

The TAT in its judgment while holding that VAT is on transactions and not on the consideration paid for the transaction, noted that there was no definition of goods and services in the VAT Act. Relying on the Black's Law Dictionary, Sale of Goods Act 1893 and the United Kingdom's Sale of Goods Act 1979, the Tribunal held that before a thing can be regarded as goods, it must be moveable and where attached to land, it must be severable from the land. After due consideration, the, the Tribunal decided that 'We find it difficult to agree with the Respondent that the lease in this appeal amounts to a supply of goods'. The Tribunal further held that real estate can be best characterised as property that does not move or that is

attached to the land, and therefore, not severable. Consequently, the Tribunal found that because of these features, real properties cannot be regarded as goods and thus, any transaction relating to real properties cannot be regarded as supply of goods. The TA accordingly found that the Appellant's lease or letting of its real properties does not amount to a supply of goods or services. Based on this finding, the Tribunal held that the lease of real properties does not amount to supply of goods or services and therefore VAT is not chargeable or payable on the transaction.

It is noteworthy that the Tribunal considered **Ibile, Momotato** and **CNOOC** in the course of delivering its judgment. Although it was silent on the implication of the decision in **Momotato**, the Tribunal rejected the decision in **Ibile** while it based its decision on the **CNOOC**.

On the second issue, the Tribunal, relying on ***FBIR v. Halliburton (WA) Limited,***[46] ***Warms Spring Waters v FIRS***[47] and what is more, in ***The Registered*** **Trustees** ***of Hotel Owners*** **and** ***Managers Association Lagos v. A-G Fed & Anor***[48] held that the Information Circular being an opinion of the Respondent cannot be regarded as regulation or law capable of amending the VAT Act by subjecting a particular transaction to VAT. While it may not be the current judicial authority on VAT in Nigeria, the decision of the Tribunal in this appeal can be regarded as the most comprehensive decision on VAT in Nigeria.

The Finance Acts 2019 and 2020 Amendments of the VAT Act and the Effect on Application of VAT to Real Estate

At root the challenges with respect to application of the VAT Act is the absence of the definitions of 'goods' and 'services'. Perhaps, influenced by the conflicting and cacophonous state of the judicial decisions which in turn is fueled by the absence of definition of goods and services in the VAT Act, the Nigerian policy makers carried out extensive amendments on the VAT Act through the recently passed Finance Act 2019 (FA 2019).[49] One of the amendments to the VAT Act through the FA is introduction of the definitions of goods and services for the purposes of the VAT Act. Thus goods for the purpose the VAT Act has been defined as:

a. All forms of tangible properties that are movable at the point of supply but does not include money or securities
b. Any intangible products, assets or properties over which a person has ownership or rights or from which he derives benefits and which can be transferred from one person to another excluding interest in land[50]

With the definition of goods and services, it therefore seems that the lacuna which had dogged the VAT Act and resulting in the conflicting decisions with respect to application of VAT Act to real estate has finally been taken care of. Although choses in action and intangible rights which includes leasehold would have been subject to VAT by virtue of the amendment, the latter part of definition of goods clearly excludes interest in land from definitions of goods. Therefore, transactions involving transfer or supply of interests in real estate such as sales, leases, letting among others are not subject to VAT under VAT Act. The amendment therefore

tallies with the decisions in **CNOOC** and **Ess ay Holdings** while rendering nugatory the decisions in **Momotato** and **Ella Sons** . The implication therefore is that as far as case law is concerned, **CNOOC** is now the case law.

Although transfer of interest in land is currently excluded from VAT, it is arguable that that this does not translate to exclusion of all real estate industry transactions from VAT. The next discussion centers on application of VAT to real estate industry.

7. Towards Proper Application of VAT Act Provisions to the Real Estate Industry

The best place to commence in ensuring proper application of VAT Act to real estate transaction is in first in deciphering the purport of the Act by taking a look at the charging clause. The charging clause of a tax statute is the provision that actually imposes the tax. In the VAT Act, the charging clauses are Sections 1 and 2. The two sections are reproduced below:

> Imposition, etc., of Value Added Tax
> 1. There is hereby imposed and charged a tax to be known as the Value Added Tax (in this Act referred to as "the tax") which shall be administered in accordance with the pro- visions of this Act.
> 2. Taxable goods and services
> The tax shall be charged and payable on the supply of all goods and services (in this Act referred to as "taxable goods and services") other than those goods and services, listed in the First Schedule to this Act.

Section 1 imposes the tax while Section 2 states the tax base. It should be noted that the charging clause of the VAT Act was never considered in the two judgments that have been reviewed. From the charging clause, what triggers VAT liability is the "supply of goods and services in Nigeria" and "Supplies" is defined in section 46 (the definition section) as ***"any transaction whether it is the sale of goods or the performance of a service for a consideration that is for money or money's worth".*** Therefore VAT is a tax on SUPPLY of all goods and services, save those expressly exempted by the Act.

The Act also states the person who is to pay the tax. The person is called the taxable person[51] who is defined under the Act as including an individual or body of individuals, family, corporations sole, trustee or executor or a person who carries out in a place an economic activity, a person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business or a person or agency of Government acting in that capacity. The importance of the taxable person to proper administration of the VAT Act can be seen in the various obligations imposed on him under the Act.

The duties include registration for VAT, payment of the tax to the supplier of goods and services purchased by or supplied to the taxpayer (input tax), collection and remittance of taxes upon making taxable supply of goods and services (output tax). In making remittance, where the output tax exceeds the input tax, he is expected to remit the excess to the FIRS. On

the other hand, where the input tax exceeds the output tax, he will be entitled to refund. The taxable person is also expected to issue invoices for goods supplied by him and render tax returns to the tax authorities. He is also statutorily obliged to keep records of taxable supplies of goods and services made by him.

From the earlier review of real estate industry, taxable activities usually commence even before the development of the intended property. Pre-construction steps include acquisition of land and taking all the necessary steps to perfect title to the land. Another pre-construction stage is financing. Where the developer engages professionals to carry out these steps, he would have to pay fees including input VAT.[52] To commence development of the land, the developer would have to also hire various professionals including surveyors, architects, electricians, contractors, etc who would also charge VAT for their services.

In addition, the developer would also purchase building materials some of (if not all) which would also attract input VAT. Therefore, technically, a real estate property such as a block of serviced flats, office building or even a shopping mall is a bundle of land, goods and services all of which can be distinguishable from one another through proper record keeping. The next is to consider the various relevant provisions of the VAT Act and how they apply to real estate transactions.

The VAT Act provides that a taxable person shall pay to the supplier the tax on taxable goods and services purchased by or supplied to the person.[53] It also states that a taxable person shall on supplying taxable goods or services to his accredited distributor, agent, client or consumer, as the case may be, collect the tax on goods or services at the rate specified in section 2 VAT Act.[54] The definition of taxable person in VAT Act is wide enough to include individuals or corporate bodies operating in the real estate industry.[55] They are therefore liable to the obligations imposed under the Act. Section 11 VAT Act provides that:

> A person who is registered under section 8 of this Act (in this Act referred to as "a registered person") shall keep such records and books of all transactions, operations, imports and other activities relating to taxable goods and services as are sufficient to deter- mine the correct amount of tax due under this Act.

This means that developers and property management companies such in **Essay Holdings, Ellah, Sons**, **Ibile Holdings** are expected to keep records of all the taxable goods and services purchased or supplied by them. They are therefore expected to keep record of the building materials and all services expended by them in the course of developing the properties. The records should also include the input VAT expended by them on the goods and services supplied to them. In addition to this, the developer is also expected to render to the FIRS, returns of all taxable goods and services they have purchased or supplied.

Therefore, where the business of the developer also include property management services, it is expected to keep record of the supply of this service and render necessary returns to the

FIRS. It is actually in the economic interest of the developers to keep proper records of the input tax expended by them, to enable them recoup same from the output tax when they charge rent and service fees.

Although the common law principles state that what is attached to the land forms part of the land and there are statutory definitions that generally define land to include property, it is very possible to separate the cost and value of the two. A developer can conveniently keep proper records of taxable goods and services purchased by it in the course of developing the property. In other words, the value of the property can be properly delineated from the actual cost of the bare land on which the property let out or sold is built.

Moreover, it is trite that statutes have precedence over common law in Nigeria and that a specific statutory provision has precedence over that with a general provision on the same matter. In **God Bless Ezenwata Nigeria Limited v. Sunday Odioku & Ors**[56] it was held that:

> It seems that the law is settled that in circumstances such as this, it is the specific legislation, id est, the Direct Labour Agency Law, as opposed to the general legislation, id est, the Public Officers Protection Law that would apply. Indeed in circumstances that are not entirely dissimilar, this Court per Ogunwunmiju, JCA in INTEGRATED DATA SERVICES LTD vs. ADEWUMI (2013) LPELR (21032) 1 at 14 held as follows: "On the applicable limitation law in the circumstances of this case, I am of the view that a specific law made on an issue overrides general law made on same issue. See NDIC as. Okem Enterprises Ltd. & Anor (2004) 4 SCNJ 244. Thus where there is a specific provision as in this case, it prevails over general provision on 5 the same subject matter.[57]

Thus while the common law and some statutes may seek to define land as including real estate properties, the VAT Act which is a statute specifically on VAT provides that not only should the properties and services expended in developing the property over the land be taxable, but that the developer must keep proper record of the transactions involving the purchases and supplies of these goods and services for VAT purposes. In other words, the VAT Act seeks to separate the value of the building from the value of the land on which it was built. Moreover, a cursory review of the Schedules of the VAT Act reveals that building materials and various services involved in property development including facilities and property management are not exempted from VAT.

It is therefore arguable that when a developer leases or let out a developed property, he is supplying to the tenant a bundle of three things namely: the land, the building materials and the services expended in building the let property. While land is not VATable, the building materials and services will attract VAT. Since the developer (lessor/landlord) is expected to keep proper records, he is expected to charge output VAT on the building materials, property development services and property management services.

On this score, the decision of the Court in Ibile Holdings case can be qualified. Rent from real

estate properties should be subject to VAT to the extent that the tax is paid on taxable goods and service portion of the property in question, excluding the cost of the land on which the property is built. This will also enable the developer-lessor to deduct input VAT it paid on taxable goods and services in the course of developing the property. The VAT Act also specifically provides for issuance of tax invoice. It states in section 13A that:

> A taxable person who makes a taxable supply shall, in respect of that supply, furnish the purchaser with a tax invoice containing, inter alia, the following-
> (a) tax payers identification number;
> (b) name and address;
> (c) VAT registration number;
> (d) the date of supply;
> (e) name of purchaser or client;
> (f) gross amount of transaction; and
> (g) tax charged and rate supplied.
>
> (2) A tax invoice shall be issued on supply whether or not payment is made at the time of supply.[58]

The use of "inter alia" means that the tax invoice can contain some other information in addition to that listed in section 13A. Therefore, the developer should state in the tax invoice, the value of the land and that of taxable goods and services and VAT on the taxable good and services excluding the value of the land itself.

Where also the development company offers maintenance and facilities management services, these also should attract VAT if added to the rent of the building. The success of this procedure largely depends on proper record keeping by the developer or the landlord. It is also on this score that the decision in **Momotato** in imposing VAT on the full value of the developed land was wrong and ought to be overturned. After holding the view that "since services provided to develop land such as the defendant did in this case have not been specifically exempted in the Act", the Court still went ahead to subject the whole transaction of purchasing the developed or serviced land to VAT.

What the Court should have done is to sever the cost of goods and services expended by the defendant in developing the land from the value of the land itself and impose VAT on the former. If the Defendant had failed in keeping proper record as imposed by the VAT Act, it should then be made to shoulder the tax as penalty.
In respect of services, Finance Act 2020 (FA 2020)'s amendments to the VAT Act has provided further clarity to remove doubts. Section 44 VAT Act as amended by section 44 FA 2020 specifically excludes "land and building" from the definition of "goods"; whilst "services means – (a) anything other than goods or services provided under a contract of employment; and (b) includes any intangible or incorporeal (product, asset or property) over which a person has ownership or rights, or form which he derives benefits and which can be transferred tom one person to another, excluding interest in land and building, money or security."

Also, section the new section 2(3)(b)(iii) and 2(3)(c) as introduced by section 40 FA 2020, there is taxable supply of services where " (iii) the service is connected with existing immovable property (including the services of agents, engineers, architects, valuers, etc) where the property is located in Nigeria; and (c) in respect of an incorporeal – (i) the exploitation of the right is made by a person in Nigeria, (ii) the right is registered in Nigeria, assigned to or acquired by, a person in Nigeria, regardless of whether the payment for its exploitation is made within or outside Nigeria, or (iii) the incorporeal is connected with a tangible or immovable asset located in Nigeria"

8. Conclusion

Although the recent amendments have excluded transfer of interest in real estate from VAT, the current provisions of the VAT Act, if properly administered, can be applied to tax real estate property transactions. What is required is proper record keeping on the part of property developer and the need to demarcate the value of the bare land or the interest in such land from that of taxable goods and services with VAT payable on the taxable goods as recognized in the VAT Act. However, with the recent amendments to the VAT Act, in which the definition of goods under the Act has been modified to clearly exclude interests in land, it is clear that government has heeded the advice of the Court in **CNOOC** where it was held that:

> If, in this Country, we need to charge VAT on such incorporeal property like the contractor rights of the Plaintiff in the PSC, we need to borrow a leaf from the U.K. VAT 1994 referred to by the Learned Senior Counsel, by amending our VAT Act, Cap VI Laws of the Federation of Nigeria, 2004 to incorporate the provision of Section 5(2) of the U.K. VAT Act which provides:
> "Anything which is not a supply of goods but is done for consideration (including, if so done, the granting, assignment or surrender of any right is a supply of services." The above provision is clear enough and should be food for thought for the 1st and 2nd Defendant in this case.[59]

It is hoped that the amendments have helped in further making clearer and demarcating real estate transactions subject to VAT from those clearly excluded.

ENDNOTES

1. Cap. V1, Laws of the Federation of Nigeria (LFN) 2004.
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7. In January and December 2020 respectively, Nigeria enacted Finance Acts 2019 and 2020, amending several tax legislation including the VAT Act. Section 34 Finance Act 2019 amended section 4 VAT Act by increasing the VAT rate from 5% to 7.5%.
8. 6 All NTC 1.
9. 6 All NTC 37.
10. Appeal No. TAT/LZ/VAT/029/2019 judgment of 10 September 2020.
11. TAT/SSZ/001/2019 delivered on 9 September 2020.
12. [2009] 13 NWLR (Pt. 1157), 200.
13. [2010] 2 NWLR (Pt. 1179), 561.
14. 7 All NTC 371.
15. See sections 1, 2 and 42 of VAT Act.
16. A review of various recent judicial decisions in Nigeria on VAT will reveal a host of inconsistencies. See the conflicting decisions of the TAT, in **Gazprom v. FIRS** (2015) 19 TLRN 66; Appeal No. TAT/ABJ/APP/030/2013 of 12 February 2016 and **Vodacom v FIRS** on liability of foreign companies for VAT; the decisions in **FBIR v. Cadbury 6 All NTC 11** and **CNOOC** on VAT application to intangibles; the decisions of the Federal High Court in **MonamerKhod v. FIRS 11 All NTC 103** and **Warm Spring Waters Nig. Ltd v. FIRS** (2015) 20 TLRN 49 on the VATability of bottled or packaged water.
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19. See Paragraph 2.2.3 National Tax Policy, 2017, available at: https://www.firs.gov.ng/wp-content/uploads/2021/01/National-Tax-Policy-Revised-

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20. See Para L© at p. 21 of the 1997 FIRS VAT Circular (Other Exempted Goods and Services which by Inference Fall within Categories and (b) above), Item 6 "House rent. (i.e rent on residential accommodation only)".
21. See Halliburton WA Ltd v. FBIR 6 All NTC 4367.
22. See section 1, United Kingdom Value Added Tax Act 1994.
23. Section 4(2) of the United Kingdom Value Added Tax Act 1994.
24. Section 5(2)(a)and(b) of the United Kingdom Value Added Tax Act 1994.
25. Paragraph 1(1), 4th Schedule, UK VAT alue Act 1994.
26. UK VAT Notice 742A.
27. Ibid.
28. See Schedule 8 of the UK VAT Act 1994 and Paragraph 3.1 of the UK Tax Notice 2015.
29. SijbrenCnossen, VAT Treatment of Immovable Property, in Victor Thuronyi ed., Tax Law Design and Drafting (IMD, 1996), Vol.1, Chapter 7), at p.6. ();
30. See section 10(2)(5) Australian General Sales Tax Act.
31. SijbrenCnossen, (supra), p.10.
32. 3 All NTC 17, at 52-53.
33. Now section 46 VAT Act.
34. At p.6.
35. Now section 46. This is the definition section of the VAT Act.
36. Supra, at p. 379.
37. Black's Law Dictionary, p. 1410.
38. Supra.
39. Prof. I.O Smith, Practical Approach to Law of Real Property in Nigeria (2nd ed., Ecowatch, 2007), p. 1.
40. Structures would include buildings.
41. Cap. I23, LFN 2004.
42. I.O Smith (supra), p. 22.
43. At p. 52.
44. At p. 80.
45. This is the ratio in **CNOOC** (supra).
46. (2014) LPELR 24230 CA.
47. Suit No. FHC/L/CS/157/2015 delivered May 11, 2015.
48. Suit No. FHC/L/CS/1082/2019 delivered May 8, 2020.
49. FA 2019 received presidential assent on 13 January 2020.
50. See section 46 FA 2019 which amended section 46 VAT Act.
51. See section 46 VAT Act.
52. The only exception is where the professionals are in the employment of the developer. See also section 17(2) VAT Act where input VAT in form of overhead services and general administration of any business which otherwise can be expended through the income statement (profit and loss account) are not allowed as deduction from output VAT.
53. Section 12 VAT Act.
54. Section 14 VAT Act.
55. See section 46 VAT Act.
56. (2015) LPELR-24438(CA), see also Nigerian Deposit Insurance Corporation (NDIC) v. The Governing Council of the Industrial Training Fund and Anor. (2011)

LPELR-19755(CA).

57. Per Ogakwu, JCA at 16-17E-A.

58

59. See also sections 9-5 Australian GST Act: "You make a taxable supply if: (a) you make the supply for consideration; and (b) the supply is made in the course or furtherance of an enterprise that you carry on; and (c) the supply is connected with the indirect tax zone; and (d) you are registered, or required to be registered. However, the supply is not a *taxable supply to the extent that it is GST-free or input taxed. 9-10 Meaning of supply (1) A supply is any form of supply whatsoever. (2) Without limiting subsection (1), supply includes any of these:…….. (e) a creation, grant, transfer, assignment or surrender of any right; (f) a *financial supply; (g) an entry into, or release from, an obligation: (i) to do anything; or (ii) to refrain from an act; or (iii) to tolerate an act or situation; (h) any combination of any 2 or more of the matters referred to in paragraphs (a) to (g)."

CHAPTER 9

VALUE ADDED TAX IMPLICATIONS OF E-COMMERCE

Abstract

Before the Finance Act, 2019 and 2020, taxation of e-commerce and digitized products posed unique challenges, which the tax laws were not able to adequately capture from a Nigerian perspective. The unique nature of e-commerce and digitized products makes it difficult to determine taxable nexus. The Value Added Tax Act 2004 (as amended) (VAT Act) imposes tax on the supply of "goods" and "services" except goods and services exempted under the Schedule to the Act. Before the Finance Act 2019 and 2020, VAT Act did not define goods and services sufficiently to include digitized products. In addition, the Nigerian Value Added Tax (VAT) law did not properly articulate that VAT will apply in the place of consumption or impose a reverse charge mechanism for cross-border transactions. There were conflicting precedents that did not put the matter to rest, leading to loss of revenue for government. The Finance Act introduced a policy shift to align more closely with the Organisation for Economic Co-operation and Development (OECD)'s best practices in order for Nigeria to obtain value in the form of tax revenue from these transactions.

1. Introduction

Electronic commerce also known as e-commerce is the use of internet for commercial transactions. This includes, but not limited to, buying and selling online, transfer of information such as audio, images and software, as well as advertisements. It can happen within one jurisdiction or several jurisdictions and the parties involved may be anonymous. Generally, e-commerce transactions can be categorised either as business-to-business (B2B) (e.g. a business purchasing materials for its production process), business-to-customer (B2C) (e.g. Amazon) and customer-to-customer (C2C) (e.g. eBay). There are some e-commerce businesses that combine both the B2C and C2C system.

Businesses, whether resident or non-resident, are obligated to pay tax on profits. Just like conventional trade, it is only rational and ethical that e-commerce activities be taxed, but taxation of e-commerce is very controversial and difficult. E-commerce organization have some peculiar characteristics which makes their profits difficult to tax. Some of these are:

A. How will e-commerce affect the definition of permanent establishment (PE) since companies can transact business in many jurisdictions without creating a PE?
B. How will electronic products be categorized under broad headings of goods or services?

C. What will be the tax implication of products ordered and delivered online across borders and without physical presence in the country where the goods are ultimately supplied?
D. How will international deliveries be treated from a tax perspective especially when the supplier has no presence in the customer's jurisdiction?

The Finance Act, 2019 and 2020 has provided some answers to some of these questions. However, some other areas of e-commerce still require international cooperation for the proper assessment and enforcement of the provisions of the VAT Act. This would ensure that there is no double taxation, which is a very important objective, and all companies are treated fairly.

2. Electronic Goods and Services Classification for VAT Purpose

Before the advent of the Finance Act, 2019 and 2020, the Nigerian VAT Act was silent about e-commerce because when it was drafted many years ago, it was almost a non-existent concept. Also, the internet and the worldwide web was not being used for business on a large scale as is being done today. However, e-commerce businesses are expected to comply with VAT like conventional trades.

The VAT Act Section(2) states that *"The tax (VAT) shall be charged and payable on the supply of all goods and services (in this Act referred to as "taxable goods and services") other than those goods and services listed in the First Schedule to this Act"*.

However, there were questions on the distinction between goods and services in e-commerce and the digital economy and how VAT applies to them. Before the year 2020, the Nigerian VAT Act did not define the words "goods" or "services". This created a gap and therefore left the classification of items into goods or services to the subjective interpretation of the taxpayers or the adoption of their ordinary definition in dictionaries. The absence of a definition in the past meant that electronic goods and services from an e-commerce lens may fall out of scope for VAT because goods are physical and their ownership can be transferred while services are distinguished by their intangibility and the requirement for someone to expend effort to provide them.

There was no controversy on the underlying transactions being carried out online, as long as they could be categorized as goods or services. In this regard, the ordering of goods online and its physical delivery regardless of location can be classified as supply of goods such as books, CD, accessories and clothes. Similarly, the ordering of services online such as air transport (through purchase of tickets), or a massage at the spa, can be classified as purchase of services. However, there was an issue in classifying digitized products because they are intangible and are not services.

In the United Kingdom, for example, when the products are digitized (not tangible), it is treated as supply of services, irrespective of whether effort is expended or not. Examples

include supply of electronic services such as website hosting, supply of software and updating it, supply of images, information, games, music, films, educational or entertainment broadcast, etcetera.

The lack of clarity in the Nigerian law led to several disputes with the tax authorities. In a case between *CNOOC Exploration and Production Nigeria Ltd V. Attorney General of the Federation &Ors'*, on the payment of VAT on the transfer of interest in an oil agreement, the Plaintiff (CNOOC) argued that the VAT Act does not define "goods" and "services". Also, the Plaintiff referenced Section 46 of the old VAT Act which stated *"supply of good as any transaction where the whole property in the goods is transferred or where the agreement expressly contemplates that this will happen and in particular includes the sale and delivery of taxable goods or services used outside the business, the letting out of taxable goods on hire or leasing, and any disposal of taxable goods. And supply of services as any service provided for a consideration"*.

Based on section 2 and section 46 of the VAT Act, CNOOC stated that the transfer of an interest in a production sharing contract license is neither a good nor a service and therefore out of scope for Nigerian VAT purposes. The Federal Inland Revenue Service ("FIRS") did not present any counter argument. Hence, the FHC ruled against FIRS stating that such intangible property cannot be categorised as a good or service according to the VAT Act.

Considering this precedent, some transactions fell out of scope of VAT, leading to loss of revenue for government. Transactions which could be arguably out of scope based on this precedent include digital advertising, digital music, digital books and any other form of intangible product.

In order to address this gap, the Finance Act 2019 addressed some of these challenges which were later updated in the Finance Act 2020. Specifically, between January 2020 and 31 December 2020, the VAT Act introduced a definition for goods as *"Any intangible product, asset or property over which a person has ownership or rights, or from which he derives benefits, and which can be transferred from one person to another excluding interest in land"*. This definition captures the product of e-commerce activities and the digital economy as a whole. It also defined services as *"anything other than goods, money or securities which is supplied excluding services under a contract of employment"*.

These definitions were updated by the Finance Act 2020 as follows:

Goods:
All forms of tangible properties, moveable and immoveable but does not include, land and building, money or securities

Services:
Includes any intangible or incorporeal (product, asset or property) over which a person has

ownership rights or from which he derives benefits, and which can be transferred from one person to another, excluding land and building, money or security.

Based on the above, intangible products like audio and video streaming subscription, supply of images, information, films, online advertisement slots, etc. are now under services. Also, any supply that cannot be placed under goods would automatically be treated as services, e.g. software as a service (SaaS), Platform as a service (PaaS) and Infrastructure as a Service (IaaS), etc.

3. Source and Destination Principle

Prior to the January 2020 and the enactment of the Finance Act, 2019 and 2020, the Nigerian VAT Act was ambiguous on whether source or destination principle should apply to cross-border transactions, particularly for services. There have been many recent disputes particularly on in-bound services and in 2019, on exported services.

Imported Services

Whether VAT is imposed based on the location of the recipient of the service is important in the digital economy where services can be provided without physical presence in the target country.

Before the Finance Act 2019 and 2020, according to the section 46 of the Nigerian VAT Act, imported services were *services rendered in Nigeria by a non-resident person to a person inside Nigeria*. Imported service is defined but it does not refer to anything in the VAT Act; hence ,the phrase was redundant.

The only relevant provision of the VAT law, as at that time, on how to tax such in-bound transactions was in Section 10 (2) of the VAT Act which stated that *"A non-resident company carrying on business in Nigeria shall include the tax in its invoice and the person to whom the goods or services are supplied in Nigeria shall remit the tax in the currency of the transaction"*. This has been subsequently updated in the Finance Act 2020 which we will consider later.

In a case between the Federal Inland Revenue Service (FIRS) and Gazprom at the Abuja Tax Appeal Tribunal (TAT), FIRS argued that the term "***supplied in Nigeria"***means the destination principle applies based on the Act. However, the Abuja TAT declared that the Nigeria VAT Act does not articulate or impose VAT on the basis of the destination principle neither is it clear on the source Principle. In actual fact, from reading the law, the phrase "supplied in Nigeria" suggests the location of the person receiving the supply and is not the basis for imposing the obligation on the non-resident to charge VAT or the Nigerian recipient to pay the VAT. However, this decision was overturned at the Federal High Court that held that once it was established that the non-resident had a subsisting contract with a Nigerian customer under Section 10(1) of the VAT Act, Nigerian VAT would be applicable.

Similar conclusions were reached by the Court of Appeal in a case between the FIRS and Vodacom, on the supply of bandwidth services to Vodacom Nigeria from a non-resident company where it was suggested that having a contract with a Nigerian customer can be considered carrying on business in Nigeria and should trigger VAT for the Nigerian customer.

The 2 cases above are under appeal and therefore there is no clear resolution on the matter until a Supreme Court judgment. This ambiguity on how imported services should be treated, and lack of reverse charge mechanism created uncertainty for taxpayers and possible revenue leakage for tax authorities for many years.

Again, the Finance Act, 2019 proffered some solution which were then updated in the Finance Act 2020 with the following amendments:

1. Section 2 of the VAT Act was expanded to cover a wide range of transactions. Specifically, a definition of place of supply of intangible goods was introduced as where the rights are situated and the place of supply for services was defined as the location of the service recipient:

(a) In respect of goods:

(ii) the beneficial owner of the rights in or over the goods is a taxable person in Nigeria and the goods or right is situated, registered or exercisable in Nigeria

(b) In respect of a service:

(ii) the service is provided to and consumed by a person in Nigeria, regardless of whether the services are rendered within or outside Nigeria or whether or not the legal or contractual obligation to render such service rests on person within or outside Nigeria.

2. An introduction of reverse charge under Section 14(4) of the VAT Act

Where a person to whom taxable supplies is made in Nigeria is issued an invoice on which no tax is charged, such a person shall self-account for the tax payable and remit the output tax to the Service within the timeline prescribed under Section 15 of this Act.

These amendments clarify the ambiguity around the VAT implication of imported intangible goods and services by imposing VAT using the destination principle and introducing the reverse charge mechanism. This blocks revenue leakages for government on B2B transactions as it will shift the responsibility of the VAT compliance to the locally registered consumer of the goods or services. However, for B2C transactions, where the recipient of the service is not registered for VAT, there is currently no mechanism for the collection of VAT in such a scenario where the supplier is non-resident..

Exported Services

Exported services is defined as services performed by a Nigerian resident or a Nigerian company to a person outside Nigeria. The first schedule of the VAT Act exempts all exported services from VAT. However, the term "person outside Nigeria" needs to be well conceptualized. Does it mean a person or company registered/ resident in another country or does it mean a person who is physically outside Nigeria when the service was received? In fact, FIRS sometimes took a very adverse view that the services have to be physically provided outside Nigeria to qualify as exported. The Allan Grey vs FIRS decision at the Tax Appeal Tribunal also created more controversy as it suggested that the basis of VAT is "where the service was performed and not the location of the consumer", which is contrary to international best practices on VAT.

The ambiguity on the definition of exported service for e-commerce is that transactions involving Nigerian service providers and foreign customers could be classified as exported service and therefore exempt from VAT, thus leading to loss of revenue to the Nigerian government, even where the services are consumed in Nigeria. For example, in terms of tax avoidance, a Nigerian customer (A) may request for a Nigerian e-commerce service provider (B) to contract with its foreign parent [(C) who is the parent of (A)] even though the service is consumed by A. Such a structure appears to be clearly immoral but opens a debate on whether the transaction is subject to VAT on the basis that the service contract is legally between (B), a Nigerian company and (C), a foreign company.

The Finance Act 2019 provides some clarity from January 2020 that the services can be provided inside or outside Nigeria and would still qualify as exported service as long as it is (i) provided to a non-resident outside Nigeria; and (ii) it is not provided to the PE or a fixed base of a non-resident

4. OECD's Best Practice

From the digital economy perspective, the OECD Base erosion and profit shifting (BEPS)'s Action plan 1 on digital economy states that the "destination principle" should be applied for B2B and B2C supplies of services and intangibles. In the principle, international traded goods or services should be taxed according to the rules in the jurisdiction of consumption.

However, according to the International VAT/GST Guidelines, B2C supplies of services and intangibles, which can either be on-the-spot or otherwise can be taxed where the supply is physically performed or at the usual residence of the customer. "On-the-spot supplies" (e.g. catering services, exhibitions, hairdressing, accommodation, etc.) are taxed at the jurisdiction where the supply is physically performed. The person performing and consuming the service or intangible should be physically present at the same time. These services and intangibles are consumed at the same time and at place where they are physically performed. However, for supply of services and intangibles which do not qualify as "on-the-spot", some which are e-commerce related like telecommunication and broadcasting services, online gaming, online supplies of software and software

maintenance, online supply of movies, music, etc. should be taxed based on the customer's residence (where the customer regularly lives or has established a home).

5. Input and Output VAT

Another contentious issue is whether input VAT can be applied to e-commerce especially with regards to business to customer's ("B2C") transactions.

Section 17(1) of the VAT Act states;

> *"For purposes of section 13(1) of this Act, the input tax to be allowed as a deduction from output tax shall be limited to the tax on goods purchased or imported directly for resale and goods which form the stock-in-trade used for the direct production of any new product on which the output tax is charged".*

Literally, input VAT cannot be claimed on supply of services. Before the Finance Act 2019, there was limited scope to claim input VAT on services that are aggregated and sold in vouchers. For a short period of time, the definition of goods in the Finance Act 2019 allowed for an argument to claim input VAT on items like software, content, etc. that are purchased to produce a final product on the basis that they were defined as goods between January and December 2020. However, the revised definitions in the Finance Act 2020 that excludes intangible assets from the definition of goods, eliminated that opportunity for companies that procure digital assets in order to supply their products.

With the increase in VAT rate from 5% to 7.5%, there may be a need to further expand the scope for claiming input VAT, especially for e-Commerce in order to bring our VAT laws in line with best practices.

It is my view that the scope and potential for e-commerce to generate tax revenue would not justify any proposal to exempt or zero-rate e-commerce transactions from VAT. However, the burden on the final customer should not be escalated due to limitation in the scope of claiming input VAT. The government should therefore consider expanding the scope of claiming input VAT on e-commerce transactions to all direct purchases of goods or services used in the production or sale of the final product to customers.

6. Other issues created by the Finance Act 2020

The Finance Act 2020 presents additional amendment to the VAT Act. One of the major changes is that the Finance Act 2020 introduced a revised Section 10(1) of the VAT Act to state that *"for the purpose of this Act, a non-resident person that makes a taxable supply of goods or services to Nigeria shall register for tax with the Service and obtain Tax Identification Number (TIN)".*

The previous requirement to be carrying on business in Nigeria before having VAT obligations was deleted from Section 10(2).

This introduces a very weird requirement for anybody in the world who has Nigerian customers to register for VAT and file returns in Nigeria, whether they have a physical connection to Nigeria or not.
They are also required to include Nigerian VAT on their invoices, even if they have VAT invoice requirements in the country where they operate from. This brings about an additional administrative burden on such companies that should not necessarily be brought into the tax net, even though the VAT would be self-charged or deducted by their Nigerian customers. The non-resident companies are also at liberty to appoint a representative for the purpose of its tax obligation.

In terms of services and intangible goods transactions between businesses (B2B) between a non-resident and a Nigerian company, the Nigerian recipients are required to account for and pay the applicable VAT under the reverse charge mechanism. However, it appears that the FIRS may want to the foreign digital companies to collect and pay the VAT on all transactions (i.e. both B2B and B2C). The FIRS may want to pursue this approach on the basis of Section 10(3) which states that *"the taxable to whom the supply of taxable goods or services are made in Nigeria* ***or such other person as may be appointed by the service shall withhold*** *and remit the tax to the service in the currency of the transaction".* The FIRS believe that they can appoint the foreign digital companies to collect and remit VAT on B2C transactions on this basis. However, this position is not really supported by the law as the companies would be collecting the VAT and not withholding the VAT as anticipated by the law. The practicality of this approach should be further reviewed and verified that it is in line with international best practice and aligns with the government's objective of improving the ease of doing business.

7. Penalty and offences

The Finance Act 2019 and 2020 has brought about a strict penalty regime which will be also be enforced in the e-commerce space and the digital economy. All businesses including those operating a reverse charge mechanism with their suppliers are required to file their tax returns on or before the 21st of the month following the month of transaction. The following penalties applies for non-compliance:

- Late Filing- NGN50,000 in the month of default and NGN25,000 subsequently
- Failure to register for VAT-NGN50,000 in the first month of default and NGN25,000 subsequently
- Failure to notify the FIRS of change in business and failure to notify the FIRS of cessation of operations- NGN50,000 in the first month of default and NGN25,000 subsequently.

8. Conclusion

VAT is to be borne by the final consumer. However, globalization, and e-commerce businesses has brought a new perspective which our VAT law is adapting to cope with.

9. Recommendations

The following recommendation have been proposed in order to improve the compliance level of VAT on e-commence transactions:

1. Experts in Information Communication and Technology may be required as well as international collaboration to enhance the understanding of e-commence in the country.
2. There is also a need to be consistent with other countries so that Nigeria appropriately tax transactions in similar ways as is done in other countries and grant similar reliefs as is available in other countries. This will ensure relief from double VAT incidence and double non-taxation.
3. The tax administrators must upskill very quickly to cope with e-commerce and the digital economy, based on the various grey areas and complexities highlighted in the VAT Act, as well as understanding the latest technology trends and disruptions.
4. It should be noted that the scope and potential for e-commerce to generate tax revenue would not justify any proposal to exempt or zero-rate e-commerce transactions from VAT. However, the burden on the final customer should not be escalated due to limitation in the scope of claiming input VAT. The government should therefore consider expanding the scope of claiming input VAT on e-commerce transactions to all direct purchases of goods or services used in the production or sale of the final product to customers.

E-commerce transactions has huge potential to improve the economy in terms of creation of jobs and opportunities; therefore, government must be very deliberate in designing the tax policies that would impact on the sector.

ENDNOTES

1. Finance Act 2019, No. 6, Vol. 107, Government Notice No. 11, 14th January, 2020. Lagos, Nigeria. (Finance Act 2019).
2. Finance Act 2020, No. 4, Vol. 108, Government Notice No. 1, 4th January, 2021. Lagos, Nigeria. (Finance Act 2020).
3. VAT Act, Cap. V1, Laws of the Federation of Nigeria (LFN), 2004 as amended.

CHAPTER 10

VALUE ADDED TAX AND THE INFORMAL SECTOR

Abstract

The Nigerian Tax Policy 2017 listed the lack of robust framework for the taxation of the informal sector, thus limiting the revenue base and creating inequality as one of the major challenges of the Nigeria Tax System. Reliable data shows that the Informal sector (consisting of small business expressions), represents 50 - 65% of economic activities in Nigeria but this sector has been grossly punching below its weight in contributing to the nation's gross domestic product (GDP). Being "the shadow economy" their activities are seldom captured by the tax net, including Value Added Tax (VAT). Nonetheless, substantial proportion of the activities and services of the informal sector are supposed to be subject to VAT (VAT Act, Cap. VI, LFN 2004. However, the N25 million minimum turnover VAT compliance threshold introduced by Finance Act 2019, has inevitably further exclude the informal sector from the VAT net. The chapter examines the evolution of the Nigerian VAT regime, the size and features of the informal sector, the economic implication of exclusion of the informal sector from optimal VAT compliance, and proffer suggestions for making the sector a more impactful contributor to the public fisc.

1. Introduction

The introduction of Value Added Tax (VAT) in Nigeria vide the enactment of the VAT Act,[1] (VAT Act) in 1993 was a watershed in the history of Nigerian taxation.[2] Section 45 VAT Act repealed the Sales Tax Act (STA)[3] which applied nationally, the STA having earlier displaced to the extent of inconsistency, Sales Tax Laws (STL) in States that had such legislation,[4] effectively repealing or rendering respective STLs, otiose. [5]Essentially, VAT Act having covered the field on the issue of sales tax, its provisions prevails over those of the Lagos STL. It has been powerfully argued that *"the Federal Government should also come to terms with the fact that an important aspect of VAT on intra State supply of goods and services is essentially within the taxing powers of the State. It is therefore ultra vires the Federal Government to continue to impose and collect VAT on intra state supply of goods and services. Hence, the Federal Government should yield the power to administer VAT on intra-State supplies to the States…"*[6]

The history of the initiatives and policy actions leading to ***VAT Act*** enactment has been well documented elsewhere.[7] The most recent VAT regulatory event is the enactment of ***sections 33 – 47 Finance Act 2019*** which significantly amended the ***VAT Act***.[8] Although Nigeria's 7.5% VAT rate[9] is generally considered low - given average African rates[10] - VAT has generated substantial revenues since its inception in 1993. For example, according to recent Federal Inland Revenue Service (FIRS) data, VAT receipts in 2018 and Q1 to Q3 of 2019 and

2020 was ₦1,108.0 billion, ₦876.0 billion and ₦1,076.5 billion respectively.[11]

The importance of VAT to the Nigerian economy and fiscal governance is underscored by the fact that VAT is split between the three tiers of government – Federal, State and Local.[12] VAT also remains one major avenue for improving Nigeria's tax to GDP ratio,[13] which remains abysmally low at 6%,[14] lagging behind many African countries.[15]

2. 'Overviews': Nigerian VAT Regime

By sections 2 and 3 VAT Act, VAT is "chargeable and payable on the supply of all taxable goods and services in Nigeria other than those listed in the First Schedule to this Act", (the VAT exempt list).[16] Only zero rated goods and services in Part II, Schedule 1 are VATable but at 0% (i.e. zero rated), not at the standard 7.5% rate, (section 4 VAT Act). VAT Act prescribes requisite compliance obligations on "taxable persons"[17] without any formal or informal sector distinctions.[18] However the informal sector is likely to form the bulk of persons below the minimum VAT compliance threshold. Save for new amendments to VAT Act, administrative and enforcement responsibilities of the FIRS also does not allow for the informal sector to be treated differently - albeit practical reality may make such outcome inescapable.[19] The challenge remains to treat taxpayers equally, as equity is one of the fundamental canons of taxation.[20]

Offences and Penalties (Part V VAT Act), also illustrate this point very well: furnishing of false documents, evasion of tax, failure to make attribution, failure to issue tax invoice, etc are all prohibited with sanctions.[21] It is trite that payment of tax is the civic responsibility of every eligible taxpayer;[22] and consequences of VAT Act non-compliance includes imprisonment (sections 36 and 37 VAT Act).

3. 'Definitions': The Informal Sector

The International Labour Organization (ILO) defined informal economy as "*all economic activities by workers and economic units that are in law or in practice not covered or insufficiently covered by formal arrangements. Their activities are not included in the law, which means that they are operating outside the formal reach of the law; or they are not covered in practice, which means that although they are operating within the formal reach of the law, the law is not applied or not enforced; or the law discourages compliance because it is inappropriate, burdensome or imposes excessive costs.*"[23]

Although every economy typically consist of the formal and informal sector, only activities of the formal sector forms the Gross National Product (GNP) and Gross Domestic Product (GDP) of the economy. By its very definition, activities in the formal sector are usually more structured, reflective in greater legal and regulatory compliance. According to an authoritative study under the auspices of the International Monetary Fund (IMF), the informal sector represents between 50% - 65% of Nigeria's economic activities.[24] These authors argued that "The characterization of the informal economy has been debated in both policy and academic circles. There is no standard definition of the informal economy in the

literature, and terms such as shadow economy, black economy and unreported economy have been used to define it. Feige (2005), notes that "the phrase informal economy has been used frequently, and inconsistently; he argues that the informal economy comprises economic activities that circumvent costs and are excluded from the benefits and rights incorporated in laws and administrative rules covering property relationships, commercial licensing, labour contracts, torts, financial credit, and social systems. Measuring informality is important given that workers in informal conditions have little or no social protection or employment benefits; and these conditions undermine inclusiveness in the labour market. Additionally, informal economic activity severely limits tax revenues for developing countries most in need of a stable tax base. This suggests that developing economies have an incentive to understand the scale of informal economic activity and how to shift production from the informal to the formal sector."

The informal sector mostly comprises artisans, small scale farmers, street vendors, road side and petty traders, domestic workers, transporters, professionals or individuals carrying on businesses without registration, regulatory framework and reputedly with little or no attention from the government.

Even without empirical data, it is more than obvious that the informal sector contributes a substantial ratio to employment figures or inversely, significantly helps to curb the swelling tide of unemployment.[25]

4. Challenges: Getting the Informal Sector into the VAT Net

This section is organised under two subheadings: pre and post Finance Act 2019 and 2020 amendments.

A. Pre-Finance Act

The National Tax Policy 2017 (Para 1.4) recognises one of the challenges of the Nigerian Tax System, that "*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 amongst others: lack of robust framework for the taxation of the informal sector and high network individuals, thus limiting the revenue base and creating inequity.*"[26]

The informal sector operates on the fringes of the formal economy: many operators, given their typically low turnover axiomatic of basic or 'subsistence' business operations, undertake cash only transactions, and do not keep proper records, if at all. Many are not even aware of VAT requirements[27] and the possibility of same applying to them. The market woman or trader becomes aware of VAT (or compliance conscious), only when her business has grown enough. For example on becoming a distributor to say an FCMG manufacturer, she may be required to register for VAT as part of on-boarding process, and from then on, begins to see VAT as an item in her purchases. Obviously, small scale informal businesses struggling to stay afloat in a harsh economic environment would be more focused on their

existential issues rather than VAT compliance.[28]

This is more so that the FIRS does not have the wherewithal yet (albeit technology deployment will help in closing gaps) to enforce VAT (and other tax) compliance provisions on every defaulting taxpayer. FIRS (as every Revenue would), thus have to make 'economic' decisions to prioritize enforcement against defaulters that could generate decent or 'worthwhile' tax revenue to its coffers.[29] On such pragmatic reasoning, recovery and enforcement actions against 'bigger' taxpayers represents the low hanging fruits for the FIRS, based on effort and reward considerations.

The informal sector had expectedly taken advantage of the institutional capacity gaps and continue to enjoy the 'benefits' of being outside the tax net. Whilst detailed data on the ratio of informal players who took advantage of the recent tax amnesty initiative, the Voluntary Assets and Income Declaration Scheme (VAIDS) compared to the formal sector has not been made available, presumably some inroad was made, even if below the projected levels.[30]

Illustrations of how regulatory requirements could be unwittingly helping informal sector to sidestep VAT compliance include the fact that most property transactions require only evidence of tax clearance certificate (TCC), which relates to personal or companies' income tax only, and not VAT – there is no provision for any certification of VAT compliance as documentation requirement.[31] Again, whilst corporate vehicles or business names owned/registered by informal players need VAT registration as part of their bank account opening requirements, an individual doing business in his own name does not have such compliance burden to contend with. This could encourage him to assume that he does not have to charge VAT as a line item in his invoices (that is if he issues invoices at all), or to even register for VAT and file VAT returns.

Pre-Finance Act, even though VAT Act did not excuse individuals who are suppliers of VATable goods and services from VAT registration and compliance, *in practice the FIRS does not seem to expect individuals to register for VAT*. This may also be an issue of risk management – individuals could be presumed to be more likely not to remit VAT collected, or in the event of death, unremitted VAT may be difficult to recover from their estate (assuming their estate is solvent enough).[32]

It has also been argued that the relative low level of non-compliance by the informal sector is borne out of the fact that they feel no 'connection' with, or obligation to pay taxes to, the government ostensibly because government has not been there for them: *"why should we pay taxes to the government that does nothing for us"*?[33] Such feelings may be more exacerbated in rural areas where citizens may feel even more distant from government. Given the mandatory (expropriatory) nature of taxation, this is not a legally valid defence or excuse, but it has some moral weight because the government-citizen social contract comprises mutual obligations.[34]

Contrarily, does not the formal sector that tends to be more tax compliant also suffer from the same neglect as the informal sector? Clearly, they both suffer from the inclement macro/operating environment. This would tend to make informal sector's excuses less tenable, even though the formal sector typically has more resources to make alternative arrangements to ensure continuity of operations despite the business landscape infrastructural challenges.

The challenge with the view of *"government has not done anything or enough for me, so I should not pay tax"* - is that it represents a chicken and egg situation. Where will government get enough to do more for the citizenry except through taxation? Why should citizens pay until they have started feeling the impact of government?[35] Continued sensitisation, such as advertisements by the FIRS showing infrastructure projects and stating that these are part of what VAT proceeds pay for, could help engender paradigm shifts in potential informal sector taxpayers. Sensitisation in indigenous languages remain paramount, given the level of illiteracy especially in the rural areas. Technology and diverse mass media platforms can also make the sensitisation more impactful.

Can a *Presumptive Income Tax Assessment* scheme suggested for income taxation of the informal sector, also be used for widening the VAT net?[36] Whilst this has even be rendered moot by Finance Act 2019 amendments, we think not in any event, given the fundamental nature of VAT as consumption tax. But maybe the challenges we face in upping the VAT collection ante provide basis for exploring options along these lines? Given the potentially significant VAT revenue impact, and other related strategic implications for national development, it is not out of place to keep exploring avenues for improving Nigeria's VAT yield by optimising informal sector contributions to same.

It is also noteworthy that the informal sector does not totally escape paying VAT; in other words, the problem may thus not be as bad as we think, even though it remains significant. For example on transactions with the formal sector, informal sector players who consume VATable goods and services sold by the former cannot escape paying VAT. Thus they pay VAT on all bank charges, and on interest income from bank deposits; VAT charge is a component of their electricity and telephone expenditure, hotel and restaurant expenses, (and until recently), airline tickets,[37] etc. On imported goods, VAT is computed together with the customs duty and other charges, and payment of all assessed charges (including VAT) is prerequisite to clearance of goods from the ports. Here, the informal sector importer is not treated differently. If purchasing from a formal sector importer, he is also unlikely to escape payment of VAT.[38]

Another illustration is with oil and gas clients of the informal sector – clients typically deduct VAT on all vendor invoices,[39] including of informal sector vendors, thereby reducing the risk that the VAT may be unremitted by the informal sector player. The same applies to government ministries, agencies and departments (MDAs) that also deducts VAT on vendor invoices,[40] albeit the FIRS/JTB has also lamented the related problem of non-remittance or

much delayed-remittance of VAT and withholding tax (WHT) collected by MDAs to the Revenue.[41] Nonetheless, these MDA VAT deductions contribute their quota in giving effect to VAT compliance.

Mr. Babatunde Fowler, the immediate past Executive Chairman of FIRS announced that VAT would be payable on online transactions effective January 2020. According to him, absent VAT, such transactions not only enjoyed unfair advantage over their brick and mortar peers, but were actually non-compliant.[42] It is also important to note that VAT may not be so relevant for most players at the bottom of the economic pyramid, because the most important of the basic necessities (basic food items, including water) is not VATable.[43] Even housing (rent on residential properties) is also VAT exempt, whilst the erstwhile VAT Amendment Bill 2018 proposed to remove rent on commercial rent from VAT.[44]

B. Post Finance Act Amendment Issues

The most famous amendment of VAT Act vide the Finance Act is the 50% increase in VAT rate from 5% to 7.5%. The next must be the new VAT threshold provision of section 15(1) VAT Act whereby businesses with gross turnover of less than N25 million are exempted from VAT compliance obligations – mostly registering for, invoicing, collecting, remitting VAT; and rendering VAT returns.[45] This is obviously to help small businesses find their feet, the pricing advantage of their products, relative to bigger competitors, should stabilise and enhance prospects of their survival, whilst accelerating their growth. The administrative time that would have otherwise gone into VAT compliance can be focused on the business' core operations thereby solidifying its foundation.[46]

Obviously the Federal Government must have concluded that the benefits of such threshold requirement (improving ease of doing business, avenue for economic stimulation, optimisation of FIRS' administrative energies, etc) outweigh the foregone VAT revenue. What are the implications of this?

- A business is supposed to register for VAT immediately upon commencing business (***section 8(1)***). However, given the threshold exemption, unless its first transaction is at least N25 million, it may not need to immediately register for VAT. Although ***section 8(1)*** is worded to apply generally, the fact that ***section 15(2)*** exempts businesses below the threshold from the penal provisions of ***section 8(2)*** (i.e. for breach of ***section 8(1)***), effectively means that such businesses may not see the need to register immediately upon commencing business. However, a strict construction is that whilst the business registers upon commencing business, all its other VAT compliance obligations (invoicing, remitting VAT and filing returns) are suspended until it falls within the VAT compliance threshold;

- Is it the case that businesses already registered for VAT pursuant to erstwhile requirements (VAT registration within six months of commencing business, irrespective of turnover), but whose turnover is below the new VAT threshold will no longer have

VAT compliance obligations until their turnover reaches N25 million? Does a combined reading of sections 8 and 15 VAT Act mean that the VAT threshold is only in respect of start-ups? Because it would be unreasonable to discriminate in applying the turnover threshold based on start-up status vs longevity of business, we believe the provision should be non-discriminatory. However, such interpretation bring with it, its own challenges some of which are noted below;

- Since there is no express provision for de-registration,[47] can existing businesses below the threshold 'deregister' by default, *viz* by no longer filing VAT returns until they reach the threshold? Is the FIRS to assume that any previously registered business that stops filing VAT returns is now below the threshold?;

- A low threshold business will still continue to pay VAT on invoices from its VAT obligatory vendors – showing that it is only exempted from charging and reporting VAT. Since it cannot register for VAT until it meets the VAT compliance threshold, will it be able to claim refund of its input VAT incurred which it is unable to set off against output VAT?;

- By the new section 14(4) VAT Act provision, where a vendor fails to charge applicable VAT, the customer "*shall self-account for the tax payable and remit the output tax…within the timeline prescribed…"* Meanwhile, section 15(2) does not list section 14(4) amongst the provisions that below threshold businesses would enjoy exemption from. What if the customer is a below VAT threshold business that has no VAT compliance obligation? If the party required to self-account charges itself VAT and remits same in such circumstances, the competitive pricing benefits of the latter's products would be lost;

- VAT that had been billed pre Finance Act, but collected afterwards, should ordinarily still be remitted to the FIRS. If customer pays the VAT after the low turnover business has been 'deregistered' for VAT purposes, will there be any incentive to still remit the VAT collected?;

- In businesses or sectors where "image is everything" and an entrepreneur for example focuses on building his brand, the ability to bill VAT may be seen as a status symbol such that the entrepreneur may flinch from having to deregister for VAT because the gross turnover of the business is still under the VAT threshold. Signalling to clients that 'we are in the VAT picture' may be a 'pragmatic' reputational management issue;

- Is there a possibility that some businesses that dip below the threshold will continue to charge VAT (since they already have TIN) and then not remit? Counterparties (clients) lack ability to confirm VAT threshold status of their vendors.[48] The VAT Act does not seem to contemplate VAT audits of below threshold companies, unlike the CITA that expressly provides that tax exempt status does not relieve small companies from CITA compliance requirements;

- What happens if a business anticipates that it will cross the VAT threshold and bills VAT in anticipation but due to business vagaries fall below same? This can happen for example when there are multiple orders that would bring turnover up to or above the threshold, VAT billing is done accordingly, but some of the orders are cancelled or reviewed downwards;

- Can businesses in order to stay below the threshold incorporate many companies and route transactions through them so that whilst the combined turnover would be above threshold, the individual business will remain outside VAT reporting coverage? This would however be balanced against the start-up and maintenance costs of proliferating entities. Also can the threshold requirements incentivize creative accounting to stay below the VAT radar?;

- Since only companies are required to file their audited financials with the FIRS (pursuant to the CITA and PPTA provisions), how will the FIRS know when the turnover of non-corporates like partnerships and sole proprietorships that are not taxable by it reaches N25 million?;

Some of these issues will receive clarity in the near future as the Minister issues regulations, the FIRS issues circulars and undertakes sensitisation/awareness programmes, whilst the judiciary also weighs in on contentious matters submitted for its determination. Meanwhile, some notable definitional improvements in the VAT Act will obviate continued controversy that had produced substantial litigation under the previous regime.[49] Like everyone, the informal sector will benefit from the clarity that had been introduced by the legislative amendments.

5. 'Optimisations': Getting to Eldorado

Following recent initiatives including the VAIDS, increased collaboration of FIRS/SIRS with MDAs such as the CAC, etc it was recently reported that Nigeria's has increased its tax net from fourteen (14) million taxpayers in May 2017 to nineteen (19) million as at May 2018.[50] It can be safely assumed that a sizeable chunk of that number would be informal operators, since presumably those already in the tax net are already 'formal' or quasi-formal. Leveraging technology to further improve ease of paying taxes in terms of catering to taxpayers' convenience and lightening their compliance burden, would continue to be a significant factor.[51] By the same token integration and harvesting of data from multiple sources – driver's and vehicle license databases, company/business name registrations, tax registrations, immigrations, National Identity Card and voter's card registrations, property registries, service providers (telcos, banks), importers and exporters' data, etc of course *subject to requisite confidentiality and legally valid or 'appropriate' use considerations*. Another suggestion is that maybe access to public social services like health and educational facilities should be on subsidised basis for taxpayers, albeit this would also have hefty downsides – it could be construed as anti-poor and anti-inclusion.

6. Conclusion

The lack of a robust framework for the taxation of the informal sector will continue to leave 'a crack in the tax walls', providing a means of 'escape' for some players in the informal sector. Such enjoys a competitive advantage over their formal counterparts (even though some formal operators may enjoy advantages of scale over the informal sector), as long as the informal sector enjoys 'benefits' of VAT non-compliance.[52] The challenge of FIRS is to progressively whittle down the advantage by gradually enlarging the informal sector VAT net to eventually capture everyone.

Presumably, not all VAT non-complaint informal sector players are unaware of VAT compliance requirements, other contributing factors include burdensome and erstwhile not business friendly/facilitative framework that will 'regularize' the informal sector. This will ensure sector-accurate data collation to expand Nigeria's VAT net and reduce the probability of VAT collection but non-remittance by tax payers. In this regard FIRS initiatives such as collaboration including sharing of data with the SIRS, the CAC, Immigration Services, Customs and other MDAs are noteworthy steps in this direction.[53] As the incidence of non-cash transactions in the informal sector reduces (through mobile money, online transfers, PoS transactions etc), same is likely to help in focusing the informal sector to their VAT compliance responsibilities. Thus, the National Financial Inclusion Strategy (NFIS) Refresh must be vigorously pursued amongst other initiatives.[54]

7. Recommendations

As governments strive for more accountability and prudent management of tax revenues, coupled with consistent sensitisation of the citizenry, further deployment of technology to aid tax administration. It is believed that informal sector will be incrementally drawn into the tax net. The FIRS may seek to measure its performance in this area by setting up near term, medium term and long term targets or benchmarks.[55] The long term objective (say over 10 years or less) would be to get all informal sector players into the tax net. Strict application of enhanced (post amendment) VAT Act penalties and enforcement provisions will also go a long way in 'encouraging' defaulting informal sector players to make the shift to compliance.[56]

The amendment to VAT Act has addressed some of the major shortcomings in the VAT Act by bringing it up to date with current economic realities, for example by increasing the severity of penal sanctions to incentivize compliance, creating VAT exempt status for small businesses and increased the VAT rate to 7.5% in order to generate more revenue for the public fisc. Given the NTP's leaning towards indirect taxes, VAT might yet be the greatest tool to improving Nigeria's tax to GDP ratio, hence all hands must be on deck to ensure that the informal sector contributes its fair share in that direction.[57]

The promised annual enactment of Finance Acts going forward will afford the government opportunity to make changes on an ongoing basis, as it leverages lessons from what is working and what is not, whilst staying in tune with economic realities. It is envisage for

example, that over time, the VAT threshold could be progressively lowered, to N5 million or totally removed.[58] Sensitisation and appropriate messaging (including accountable government actions) whereby the informal sector looks forward to contributing more to public revenues would be a complement in this regard.

ENDNOTES

1. ***Cap. V1, Laws of the Federation of Nigeria (LFN), 2004 as amended.***
2. VAT Act was originally enacted as VAT Decree No. 102 of 1993 by the military administration of General Sani Abacha. Pursuant to the existing law provision of section 315 1999 Constitution, the VAT Decree became VAT Act. VATA's most significant amendment was vide VAT (Amendment) Act No. 12 of 2007. Several subsidiary legislation issued pursuant to VAT Act, have also 'amended' First Schedule VAT Act in 2012 and 2014. In June 2018, the Federal Executive Council (FEC) approved the submission of VAT Amendment Bill 2018 (VATAB) to the National Assembly for their consideration.
3. STA was enacted in 1986 as ***Sales Tax Decree No. 7 of 1986*** and later codified as ***STA,Cap. 399, LFN 1990.*** It imposed Sales Tax (ST) at 5% on taxable services (leisure and hospitality industry) and 5% on eight listed categories of 'luxury' items (goods), with only wine liquor and spirits rated 10%. The State Internal Revenue Services were to administer ST, subject to directions from the Joint Tax Board (JTB) (section 7 STA). The view that tax base of STA was narrow could be seen when its Schedule is contrasted with VAT Act's. Whilst only the listed items in STA were subject to ST, VAT Act adopts the opposite approach: all "goods and services" are subject to 5% VAT, unless listed in Schedule 1 VAT Act.
4. Such as Ogun State's Sales Tax Law, 1982, which albeit predated STA was invalidated by the Supreme Court in ***A-G Ogun State v. Aberuagba (2009) 1 TLRN 82***, on the ground amongst others, that it purported to tax products of inter-State commerce, which is beyond the legislative competence of the Ogun State House of Assembly. Other States with STLs were Oyo, Bendel, Plateau and Kaduna. See Dr. Teju Somorin, 'Evolution of Nigerian Tax Laws', (2015, CITN), p. 26.
5. In ***AG Lagos State v. Eko Hotels Ltd (2018) 36 TLRN 1 at 35,*** the Supreme Court held the ***Sales Tax Law, Cap. 175 Laws of Lagos State*** **1995** (originally enacted as ***STL No. 9 of 1982*****,** subsequently codified as***STL, Cap. S3, Laws of Lagos State 2003)***, to be invalid.
6. See Prof. Abiola Sanni, 'Policy, Legal and Administrative Imperatives in the Quest for Eradicating Multiplicity of Taxes in Lagos State', 1st Annual Lecture of Lagos State Professorial Chair of Tax & Fiscal Matters, 28.11.2017, p. 44.
7. See for example, Ifueko Omoigui-Okauru, 'Federal Inland Revenue Service and Taxation Reform in Democratic Nigeria', (2012, Safari Books), p. 9. See also, Prof. Taofek Abdulrazaq, 'Introduction to VAT in Nigeria' (2nd ed. 2011, Ababa Press), p.1. Per Abdulrazaq (supra, at p. 2).
8. Unless the context otherwise requires, every reference to VAT Act in this article is to VAT Act as amended by the Finance Act 2019 and Finance Act 2020.
9. The VAT rate was recently increased from 5% to 7.5% by section 34 Finance Act 2019 which amended section 4 VAT Act. By ministerial proclamation widely reported in the news media, the effective date for the new VAT rate is 1st February 2020 (See s. 42 of Finance Act 2020).
10. For example, standard VAT rates in some African countries are as follows: Madagascar and Morocco (20%); Algeria and Cameroun (19%); Cote D'Ivoire, Gabon, Tanzania, Chad and Uganda (18%); Kenya (16%); Mauritius, Tunisia, Ghana and South Africa (15%); Egypt (14%); Mozambique (17%); Botswana (12%); etc. For further details,

see http://taxsummaries.pwc.com/ID/Value-added-tax-(VAT)-rates (visited on 17.10.2018). An attempt was made to increase Nigerian VAT rate to 10% in 2007, but same was subsequently reversed and the proposed increase was never implemented. For a high level discussion, see Teju Somorin (*supra*), *at pp. 103 – 105.*

11. NBS, CSL Research (2021), available online at https://nairametrics.com/2020/11/05/VAT-collection-surges-on-increased-VAT-rate/, retrieved 5 June 2021.
12. By ***section 40 VAT Act,*** the three-tier distribution formula is 15%; 50% and 35% to the Federal, State and Local Governments, respectively.
13. It has been observed that: "*Low non-oil revenue mobilization is affecting the government's objectives to expand growth-enhancing expenditure priorities, foster higher growth and employment, and comply with its fiscal rule which limits the federal government deficit to no more than 3 percent of GDP. There is significant revenue potential from structural tax measures. A broad-based and comprehensive tax reform program is needed in the short and medium term to address these objectives and generate sustainable revenue growth by broadening the bases of income and consumption taxes, closing loopholes and leakage created by corporate tax holidays and the widespread use of other associated tax expenditures, as well as creating incentives for the sub-national tiers of government to raise their own source revenues."* See *IMF Country Report No. 18/64,* ***'Nigeria Selected Issues'****, (March 2018), p.*5: https://www.imf.org/en/Publications/CR/Issues/2018/03/07/ Nigeria-Selected-Issues-45700, visited on 17.10.2018.
14. According to the World Bank, Nigeria's tax to GDP ratio in 2013 was a dismal 1.48% (compared to 1.53% in 2003): https://data.worldbank.org/indicator/GC.TAX.TOTL.GD.ZS?locations=NG (visited on 17.10.2018). See also, Tobi Awodipe, ***'Nigeria's Tax: GDP Ratio Remains one of the Poorest in Africa'***, *The Guardian, 24.03.2018:*https://guardian.ng/business-services/nigerias-tax-gdp-ratio-remains-one-of-the-poorest-in-africa/, reporting that *"Financial experts have lamented the country's tax to GDP ratio, describing it as one of the poorest in Africa. The figure ... at just 6 per cent is significantly lower than Ghana and Egypt at 16 percent, Morocco at 22 percent and South Africa at 27 percent."* The article reported proceedings of a tax conference on *'Understanding Tax and its Effect on Nigerian Businesses'*, organized by the Nigerian Association of Chambers of Commerce, Industry, Mines and Agriculture (NACCIMA), FIRS and LIRS in Lagos. Incidentally the administration of President Jonathan in 2013 announced it was working with McKinsey & Co to "progressively increase" Nigeria's tax to GDP ratio to 22% by the end of 2015. See *Talatu Usman,* ***'Nigerian Government Hires Tax Consultants to Increase Revenue Generation',*** *Premium Times, 27.11.2013*: (visited on 17.10.2018).
15. An OECD Study, ***'Revenue Statistics in Africa 2017'*** analysing comparable data on tax and non-tax revenues for 16 participating countries: Cape Verde, Cameroun, Democratic Republic of Congo, Côte d'Ivoire, Ghana, Kenya, Mauritius, Morocco, Niger, Rwanda, Senegal, South Africa, Swaziland, Togo, Tunisia and Uganda, showed that the 2015 average tax-to-GDP ratio in these countries was 19.1%. This was however lower than the average tax-to-GDP ratios for Latin America and the Caribbean (LAC) and the OECD: 22.8% and 34.3% respectively. See OECD news item, ***'Revenue Mobilisation in Africa Continues to Improve, says New Report'***

http://www.oecd.org/tax/revenue-mobilisation-in-africa-continues-to-improve.htm (visited on 17.10.2018).

16. Effectively, *VAT applies to all goods and services except those listed* in ***Schedule 1 as amended pursuant to s. 47 of Finance Act 2019***. This derives from the interpretative rule embodied in the Latin maxim *expressio unis est exclusion alterius:* the express mention of one thing is the exclusion of others not mentioned - ***AG Abia State v AG Federation [2005] ALL FWLR (Pt. 275), 414***. Arguably, ***Schedule 1*** helps to moderate the compliance and interpretative challenges occasioned by the omission of VAT Act to define *"goods and services"* – given the general rule that any doubtful and ambiguous provision of a tax statute is to be resolved in favour of the taxpayers: ***Citibank Nigeria Limited v. FIRS (2017) 30 TLRN 40.*** The counter argument is that VAT Act would not apply to purchases and supplies that are not "goods and services", for example bare land or choses in action. See further, Taxspectives by Afolabi Elebiju, 'Why Are You Charging Us VAT?', THISDAY Lawyer, 24.01.2012, p. 14; also available at:http://www.lelawlegal.com/pdf/*Why-Charge-Us-VAT.pdf.*
17. By virtue of section 15(1) VAT Act introducing VAT compliance threshold, Section 46 VAT Act's definition of "taxable persons" now excludes persons less than N25 million gross turnover.
18. Such compliance obligations include VAT registration of taxable persons upon commencement of business (section 8(1) VAT Act); keeping *"of such proper records and books of all transactions, operations, imports and other activities relating to taxable goods and services as are sufficient to determine the correct amount of tax due*" (section 11 VAT Act); payment of VAT to supplier on taxable goods and services (input VAT) (section 12 VAT Act); furnishing purchasers with tax invoice containing prescribed details, invoice must be issued on supply whether or not payment is made at the time of supply (section 13A VAT Act); collection of tax (output tax) by taxable person on supply of taxable goods (section 14(1) and (2) VAT Act); non-resident companies are to include VAT in their invoice and the recipient of the goods or services in Nigeria shall remit the VAT in the currency of the transaction (section 14(3) VAT Act); a customer who should have been charged VAT but was not shall self-account for the VAT payable and remit same to the FIRS (section 14(4); rendering of returns by the 21st day of the following month of supply or purchases (section 15 VAT Act); payment of excess of output VAT over input VAT, and entitlement to utilise excess input tax as a credit against output tax or to claim tax refund from the FIRS for the excess input VAT subject to producing satisfactory supporting documentation (section 16 VAT Act); however the input VAT to be allowed as deduction over output VAT shall be only in respect of goods purchased for resale or which comprise stock in trade used for production (section 17 VAT Act).
19. VAT Act's penal and enforcement provisions include: section 8(1) – failure to register upon commencement of business (defined per section 46 VAT Act as the date of the business' first transaction) attracts penalty of N50,000 for the first month and N25,000 for every subsequent month; same default and continuing default penalties are also applicable for failure to: (a) notify the FIRS of change of address within 30 days of such change; (b) notify the FIRS of permanent cessation of trade or business within 90 days of such cessation of with intention to de-register the business for tax purposes; and (c) file monthly VAT returns to the FIRS (sections 42 and 44 VAT Act); FIRS ability to assess VAT on best of judgment basis for taxpayer's failure to render returns

(section 18); section 19 – failure to remit VAT within prescribed timeline attracts 10% of the tax not remitted and (default) interest) at the prevailing Central Bank of Nigeria (CBN) minimum re-discount rate and the provisions of VAT Act relating to collection and recovery of unremitted VAT, penalty and interest shall apply.

20. See Ayoluwatunwase Fadeyi, '***Tax Planning: Walking the Thin Line Between Tax Avoidance and Tax Evasion', (BD Legal Business (BusinessDay), 29.03.2018, p. 26;*** **also available at:**http://www.lelawlegal.com/pdf/Tax%20Planning_Payment_Ayo.pdf**. See also**, ChuksOkoriekwe, ***'Taxing the Informal Sector: On Your Marks, Set, Go!', (BD Legal Business (BusinessDay), 06.04.2018, p. 26;*** **also available at:**http://www.lelawlegal.com/pdf/Lelaw%20-%20Taxing%20the%20Informal%20Sector%20Article.pdf**.**

21. See ***sections 25-29 VAT Act***. Furnishing of false documents is an offence which upon conviction attracts a fine of twice the amount under-declared (***section 25***); evasion is punishable with the higher of a fine of N30,000 or twice the amount of the VAT being evaded (***section 26***); failure to issue VAT invoice is sanctionable with a fine of 50% of the goods or services not invoiced (***section 29***), etc. Others include failure to keep proper records and accounts attracts N2,000 fine for every month that the failure continues; failure to collect VAT attracts 150% of the VAT not collected plus 5% interest above CBN's rediscount rate (***section 34)***;.

22. ***Independent Television/Radio v. ESBIR [2015] 12 NWLR (Pt. 1474), 442 at493***. According to the oft quoted obiter of US Supreme Court Justice Oliver Wendell Holmes, Jr in a 1927 dissenting judgment:***Compania General De Tabacos De Filipinas v. Collector of Internal, (275 U.S. 87, 88)****: "Taxes are what we pay for civilized society."*

23. See ILO, 'Informal Economy and Atypical Forms of Employment': http://www.ilo.org/actrav/areas/WCMS_ DOC_ATR_ARE_INF_EN/lang--en/index.htm(visited on 13.10.2018)

24. Leandro Medina *et al,* 'The Informal Economy in Sub-Saharan Africa: Size and Determinants', Working Paper No. 17/156, July 2017, pp 2, 5, 13, 19 and 26: https://www.imf.org/en/Publications/WP/Issues/2017/07/10/The-Informal-Economy-in-Sub-Saharan-Africa-Size-and-Determinants-45017(last visited on 13.10.2018). According to the authors (*at p. 1*),*"*

25. See for example, the National Bureau of Statistics (NBS)' publication, 'Labour Force Statistics Vol. 1: Unemployment and Under Employment Report Q1–Q3 2017' on employment/unemployment data and trends for the period: file:///C:/Users/USER/Downloads/q1-q3_2017_unemployment_report_VOLUME_1%20(4).pdf (visited on 17.10. 2018).

26. Federal Ministry of Finance 'National Tax Policy',*February 2017, p.6:* http://pwcnigeria.typepad.com/*files/ fec-approved-ntp---feb-1-2017.pdf (last accessed on 13.10. 2018).*

27. At a recent jointly organised conference, NACCIMA's President, Alaba Lawson, *"stressed that there was a need to educate the masses now more than ever before. ...she pointed out that several challenges continue to prevent people from complying. 'Some contentious tax related matters which require clarification include ... [VAT], which many of us need to be enlightened about…' "*See Tobi Awodipe (***supra***).

28. Such compliance could implicate costs (book keeping, preparation of, and filing returns) which their business does not have the wherewithal to meet. For example, the

book keeping and VAT returns may require employment of an accountant or outsourcing the service, and these have financial implications. Most informal sector players do not have nor keep proper record for tax purposes, no record of sales, purchases and other forms of transactions, this could be related to: under-staffing entrepreneurs long for stability and success of the business before loading up on overheads as a result of misplaced priorities, lack of skilled manpower (low remuneration may not attract the right skill set), ignorance of keeping proper record, high cost of accounting software and old paradigm mind set, this makes assessment for VAT purposes cumbersome.

29. This was illustrated with the recent FIRS action of purported substitution (pursuant to ***section 31 CITA***), advising banks to place restrictions on corporate accounts (of non-compliant taxpayers with turnover of over N5 billion for the past three (3) years), and directing banks to debit their accounts in favour FIRS with alleged tax indebtedness of such taxpayers. Incidentally, such powers are expected to be exercised after the tax liability of such have been determined judicially or assessments have become final and conclusive. It is emblematic of FIRS push to rake in more taxes, for example it began to assess not compliant property owning companies to tax by treating their property values as turnover as a way to ginger such companies into action. The substitution action attracted some criticism. See: 'Freezing Customers' Bank Accounts over Tax Payment Default, Threat to Economy – LCCI', *Vanguard Newspaper, 16.08.2018:* (visited on 17.10.2018).

30. Out of the N305 billion projected VAIDS revenue, FIRS collected only N30 billion towards the tail end of VAIDS in June 2018. See Ndubuisi Francis, '***Receipts from VAIDS Hit N30bn',*** *ThisDay, 07.06.2018*: https://www.thisdaylive.com/index.php/2018/06/07/receipts-from-vaids-hit-n30bn/, and '***VAIDS: Lessons to Learn from Tax Amnesty'****ThisDay, 18.06.2018*: https://www.thisdaylive.com/index.php/2018/06/18/vaids-lessons-to-learn-from-tax-amnesty/, both visited on 17.10.2018

31. See section ***Section 101(2) CITA*** stipulation of TCC as documentation requirement for most regulatory approvals. Part of JTB resolutions at its 135th meeting in July 2016 was that *"[SIRS] should make presentation of TCC a requirement for processing of drivers' license and number plates."* Others include *that "Nigeria Immigration Service making it mandatory for presentation of Tax Clearance Certificate (TCC) for issuance of immigration facilities"* and *"Federal Road Safety Corps, Vehicles Inspection Officers and other traffic agencies enforcing presentation of Taxpayer Identification Number (TIN) as requirement for the resolution of a road traffic offence."* See Deloitte Tax Alert, (***supra***). More often than not, evidence of VAT registration is also requested for, as part of contractor/ vendor registration with MDAs.

32. .It is common to see an individual engaged as consultant or independent contractor to an employer. If he issues invoice to the employer in his own name, he would typically not include VAT. However, if he subsequently registers a business name or incorporates and issues invoice through those, he would have to add VAT and also account for the VAT collected to the FIRS. Also, individuals are not currently required to furnish their TINs for account opening purposes by banks, thus individuals trading in their own names as sole proprietors (as opposed to those using registered business name), are able to escape VAT compliance requirements in this regard.

33. The converse of this is that citizens may demand less accountability from government

if they do not pay taxes. The government itself feels less accountable, especially if as it happened previously in Nigeria, government can look to other sources of "easy" revenues – proceeds of crude oil exports. At the CITN 2018 Tax Conference, Vice President Osinbajo reportedly stated: tax *"compliance and good governance should exist side by side as the head and tail of a social contract that binds citizens and government. 'But it is also a fact that when people pay taxes, they are more inclined to hold their governments to account.'... 'The moral is a simple one that when citizens pay their full share of taxes they take more than a passing interest in how they are governed and how public funds are utilized and accounted for…' He also said that government had relied more in the past on oil revenues than on taxation adding that a decline in taxation depicted a decline in government's accountability and ability to deal with the needs of the people. He said poor tax management was one of the issues that increased corruption in the system adding that the fact remained that the tax payer was less tolerant of corruption than another who failed to pay. He stated that because what government spent was oil money and taxes of few persons a lot of people saw government's money as belonging to no one. 'We have aggressively expanded the implementation of the TSA and IPPIS both designed to ensure that public funds are transparently managed and spent…"* See Mark Itsibor, ***'Nigeria Now has 19 Million Active Taxpayers – Osinbajo'***, *Leadership Newspaper, 10.05.2018:* https://leadership.ng/2018/05/10/nigeria-now-has-19million-active-taxpayers-osinbajo/ (visited on 17.10.2018).

34. See for example, Juliana Agbo, 'Informal Sector Has Been Alienated, Neglected', *Leadership Newspaper, 21.03.2018*:https://leadership.ng/2018/03/21/informal-sector-has-been-alienated-neglected/ (visited17.10.2018) , where the CEO/ Director-General of the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) at a recent capacity building workshop for the Federation of Informal Workers Organisation of Nigeria (FIWON): *'Transition from the Informal to the Formal Economy.'* reportedly stated that the workshop was organised to correct the monumental neglect of the informal sector, which had contributed to the economic imbalance plaguing the country. *"The government has realised the importance of the sector as a catalyst for the growth, productivity and competitiveness of the economy of the country… Developing the issues in to the main stream of the economy require plan and strategy to enhance their effectiveness and efficiency,"* Other measures to help ensure sectoral effectiveness include: *"the impact of government policies and interventions, the self-propelling dynamism of the sector and the nature of linkages between the informal and the formal sector."*

35. JTB resolutions at its 135th meeting in July 2016 include that *"tax potentials from the informal sector should be explored in order to meet government's goal of growing IGR."* Also, *"automation of tax administration processes should be given priority to cover all aspects of taxation at both federal and state levels"* and *"deduction of [VAT] and [WHT] at source should be implemented at the State and Federal [MDAs], by automating the process to enhance efficiency and boost collection of taxes.*" See Deloitte Tax Alert, 'Joint Tax Board: Communique on Presumptive Tax Regime for Informal Sector':https://www2.deloitte.com/ng/en/ pages/tax/articles/joint-tax-board-communique-on-presumptive-tax-regime-for-informal-sector.html, visited on 17.10.2018.

36. Section 45 of Finance Act 2020, added paragraph 6 to part II of the First Schedule to VAT Act 2004 as amended exempted airline
37. Section 45 of Finance Act 2020, added paragraph 6 to part II of the First Schedule to VAT Act 2004 as amended exempted airline transport tickets issued and sold by commercial airlines registered in Nigeria.
38. The foregoing is further buttressed by VATA provisions: ***section 6*** defines the value of imported goods to include *"all taxes, duties and other charges levied either outside or by reason of importation into Nigeria"* (other than Nigerian VAT) and *"all costs by way of commission, parking, transport, and insurance up to the port or place of importation."* Further, section 15(3) VAT Act provides that *"a person who imports taxable goods into Nigeria shall render to the [FIRS] returns on all the taxable goods imported into Nigeria."*
39. Section 13(2) VAT Act provides an exception to the general VAT billing and collection process that: "The Service may, by notice, determine and direct the companies operating in the oil and gas sector which shall deduct VAT at source and remit same to the Service." The FIRS issued its Information Circular No. 02/2007, 'Notification of Guidelines on the Implementation of VAT Deduction (Reverse Charge) and New Payment Arrangement with Respect to Fees, Levies, and other Charges Payable by Companies in Oil and Gas Industry' to the effect that oil and gas operators withhold the VAT payable by them to their vendors and remit same to the FIRS.
40. These has been helped by the fact that for companies, VAT registration is no longer a separate process, but is part of the registration for taxes with the FIRS, whilst business names (partnerships and sole proprietors) also register for VAT with FIRS. The Tax Identification Number (TIN) granted upon such tax registration is part of the documentation requirements for most vendor registrations and transactions with MDAs.
41. See for example, Kauthar Anumba - Khaleel, 'N115bn: Reps Probe MDAs For Alleged Non-remittance To FIRS', *Leadership Newspaper, 08.11.2017:* https://leadership.ng/2017/11/08/n115bn-reps-probe-mdas-alleged-non-remittance-firs/; Seyi Awojulugbe, 'EXCLUSIVE: Presidency Fails to Remit PAYE, VAT to FIRS', *The Cable, 18.07.2018:* https://www.thecable.ng/exclusive-presidency-fails-to-remit-paye-VAT-to-firs (both visited on 17.10.2018).
42. Recently, a 'VAT-like' N50 charge on POS transactions was disclaimed as illegal by the Federal Competition and Consumer Protection Commission (FCCPC) that it was to be borne by merchants and not consumers.
43. See Part I, Schedule 1 VAT Act.In ***MonamerKhod Enterprise Nig Ltd v. FIRS Suit No: FHC/S/CS/2005*** and ***Warm Spring Waters &Ords v. FIRS [2015] 20 TLRN 49*** the Federal High Court reached different conclusions on VAT exempt status of bottled water. In the former, it was held that bottled water, being packaged product is subject to VAT whereas in the latter, the Court departed from Monamer and decided that it is a basic food item exempt from VAT.
44. For policy reasons, the FIRS in practice treats residential rent as not liable to VAT, albeit same is VATable per VAT Act. Note judicial decisions to the effect that the FIRS cannot whilst purporting to clarify statutory provisions through information circulars, produce outcomes that will amount to amending substantive provisions.
45. *Cf*. with the small company categorisation under the Finance Act 2019 amendments to the Companies Income Tax Act (CITA): profits of companies with less than N25

million is tax exempt, albeit such companies are required to file tax returns and be in good tax compliance status: section 23(1)(o)(I) CITA.

46. Section 15(1) VAT Act provides as follows: *"A taxable person who, in the course of a business, has made taxable supplies or expects to make taxable supplies, the value of which, either singularly or cumulatively in any calendar year is N 25,000,000 or more shall, render to the Service, on or before the 21st day of every month in which this threshold is achieved and on or before the same day in successive months thereafter, a return of the input tax paid and output tax collected by him in the preceding month in such a manner as the Service may prescribe."* By ***section 15(2)***, such businesses are exempted from VAT Act provisions: (a) penalising failure to register with FIRS for VAT (section 8(2)); (b) mandating remission of VAT charged on contracts with the public sector or oil and gas contracts to the FIRS by the relevant agency or private sector oil and gas player respectively (section 13); penalising failure to issue VAT invoice, collect VAT and submit VAT returns (sections 29, 34 and 35) respectively.

47. Assuming there was de-registration as a result of falling below the threshold, at the point of deregistering, will their prior VAT compliance status, be an issue as they should be required to account for VAT previously billed and collected?

48. The current VAT forms only require figures of input and output VAT and the VAT being remitted. There is no requirement for details of individual VAT transactions and counterparties; these would be discoverable at audit.

49. For example, taxable goods and services have been more precisely defined, the issue of whether bottled water is basic food item has been addressed by the new provisions of section 46 VAT Act.

50. See **Mark Itsibor,** *'Nigeria Now has 19 Million Active Taxpayers – Osinbajo'*, *Leadership Newspaper, 10.05.2018:* **https://leadership.ng/2018/05/10/nigeria-now-has-19million-active-taxpayers-osinbajo/**. According to the report, the Vice President, Prof. Yemi Osinbajo, stated in his keynote speech at the 2018 Annual Tax Conference of the Chartered Institute of Taxation of Nigeria (CITN) on 9th May 2018 that: *"Earlier, I noted that as of May 2017, only 14 million economically active Nigerians paid taxes. I am pleased to announce that the number is now in excess of 19 million and still growing. This means that efforts led by the [FIRS] in collaboration with many of the [SIRS] have already added more than five million new tax payers to the tax base. But there is still a lot of work ahead of us; as Nigeria races to catch up with the rest of the world in terms of tax compliance we all have a role to play in this."* That there is still scope for more is borne out by reported views of experts at a recent NACCIMA organised tax conference. One of the presenters, Oluseye Arowolo reportedly said: *"according to the [CAC], there are just 2.5 million tax-registered corporates while there are 30 million on the CAC list… government and taxpayers have several challenges that need to be overcome soonest."* Tobi Awodipe, *op cit.*

51. Part of the major strides attained by FIRS is attributed to *"the use of technology brought about the ease of tax payment, manifested in the introduction of e-some Registration, e-Filing, e-Payment, e-Receipt, e-TCC (Electronic Tax Certificate), e-Stamp Duty, Auto VAT Collect, Integrated Tax Administration System (ITAS) and Government Information Financial Management Information System (GIFMIS), all of which resulted in automation and blocked leakages."* See Julius Asemota, 'FIRS: Triumph of Tax Reforms' *Vanguard Newspaper, 26.08.2018*: https://www.vanguardngr.com/2018/08/firs-triumph-of-tax-reforms/. According to

the article, *"If proof was needed on the effectiveness of the reforms being implemented in the country's tax/ revenue collection and administration system by the [FIRS], it was provided by the Service's 2018 Half Year (HY) Revenue Performance Report, which showed an improvement of about 42 per cent over that of the same period in 2017 and indicated that the Service had already realized 75 per cent of its target for 2018."*

52. 7.5% VAT can make a difference in the purchase price of items leading price-conscious customers to prefer to transact with the informal sector operative whose price is 7.5% less, by virtue of not charging VAT. Alternatively, an informal sector operator that charges VAT but does not remit has effectively increased its revenue by 7.5%; this could enable better cashflow and thereby conferring a competitive advantage over a peer business but which charges and remits VAT collected. There is anecdotal evidence of transactions where the vendor granted a 'discount' by removing the erstwhile 5% VAT from the sale price. The new section 15 VAT Act provision must be interpreted as expression of government support for small businesses, which essentially are more in the informal territory than formal.

53. *According to Mr. Fowler, "FIRS will continue to implement initiatives that will drive compliance and generate revenue by continuous taxpayer enlightenment, implementation of the auto VAT collection in other sectors of the economy, simplification of the tax processes especially for small taxpayers, strengthening collaborations with other agencies such as Corporate Affairs Commission (CAC), States Boards of Internal Revenue, Ministry of Trade and Investment, [and] Nigeria Customs Service."* See Omodele Adigun, 'FIRS 'll Drive Tax Compliance through innovative Ideas, says Executive Chairman, Fowler', *The Sun, 09.10.2018*, http://sunnewsonline.com/firs-drive-tax-compliance-innovative-ideas-fowler/ (visited on 17.10.2018)

54. The NFIS 2012 "set two financial inclusion targets for the year 2020: an overall financial inclusion rate of 80% of the adult population and a formal financial inclusion rate of 70% of the adult population": 'Executive Summary of the Exposure Draft of the NFIS Refresh, July 6 2018';https://www.cbn.gov.ng/Out/2018/CCD/Exposure%20Draft%20of%20the%20National%20Financial%20Inclusion%20Strategy%20Refresh_July%206%202018.pdf (visited on 17.10.2018).

55. In 2013, the President Jonathan administration engaged the services of McKinsey & Co to advise on strategy for raising Nigeria's tax to GDP ratio. See ***'Double Standard',****The Nation (editorial), 09.12.2013:*http://thenationonlineng.net/double-standard/

56. In this regard, the impact of moral suasion and reputational impact of FIRS actions - apart from litigation – may be incentives for informal sector VAT compliance. Recently, the erstwhile FIRS Chairman stated that FIRS will be issuing new certificates of VAT compliance to businesses which they can display in their premises. This can spawn increased desire for compliance as part of their competitive business strategy. See Omodele Adigun (***supra***).

57. Key findings from the OECD study, ***'Revenue Statistics in Africa 2017'*** (**supra**), are that 2015 tax-to-GDP ratios in the sixteen (16) African countries surveyed *"ranged from 10.8% in the Democratic Republic of the Congo to 30.3% in Tunisia, with an average of 19.1% across the 16 countries." Also, "between 2014 and 2015, all featured countries except Kenya, Tunisia and Morocco increased their tax-to-GDP ratios. On average, they increased their tax-to-GDP ratios by 0.4 percentage points, a*

slightly lower increase than for the LAC [Latin American and Caribbean] average (0.6 percentage points) but above the OECD average (less than 0.1 percentage points). All countries in the publication had higher tax-to-GDP ratios in 2015 than in 2000, and all have increased more than the OECD average. Since 2000, the average tax-to-GDP ratio has increased by 5.0 percentage points, a similar increase to the LAC average (4.9 percentage points). In contrast, the OECD average grew by just 0.3 percentage points over this period." In terms of tax structure, *"taxes on goods and services were the principal source of total tax revenues in 2015 (57.2%, on average) and particularly VAT (31.5% on average). The share of revenues from taxes on income and profits amounted to 32.4%, on average. Kenya, South Africa and Swaziland obtained about half of their tax revenues from taxes on income and profits in 2015 whereas among the other 13 countries, this category ranged from 18.6% in Togo to 37.6% in Rwanda. Tunisia and Morocco reported the highest share of social security contributions among the 16 countries in 2015 (29.5% and 17% respectively). The African countries featured in this publication have significantly lower social security contributions than LAC countries. This accounts for most of the difference between their respective average tax-to-GDP ratios."*

58. The reduction could be in N5 million inclements (from N25 million to N20 million, then N15 million, N10 million and finally N5 million) over a five to ten year period.

CHAPTER 11

VALUE ADDED TAX AND POWER SUPPLY IN THE ENERGY SECTOR

Abstract

Globally, there has been controversy amongst scholars and tax practitioners regarding the classification of "electric power" or "electricity" in the energy sector as either "goods" or "service". Considering that what value added tax imposes is a tax on supply of goods and services not exempted by law, the uncertainty of the nature and classification of electricity and power supply either as goods or service requires attention with a view to ascertain its VATability and incident on power generation companies (Gencos), distribution companies (Discos) and end-users under the extant legislation i.e. Value Added Tax Act (VAT Act). It is therefore important to conceptualize the models around the world on the peculiar nature of things produced or consumed in power industry such as electricity, solar, nuclear and wind power and how supply of same is arranged in the power market giving the understanding of business of power generation, transmission, distribution and trading in Nigeria with a view to expanding the VAT net and also mitigating taxpayers' burden under the Electric Power Reform Sector Act, 2005 and VAT Act, 2004.

1. Introduction

Over the years, the energy industry has been dominated by the petroleum companies and perhaps this precipitated the interchangeably use of oil and gas such that when energy is discussed, ones' mind set is restricted to think it only relates to extractive industry, mining, exploration, refining, manufacturing, production and distribution of petroleum products i.e. oil and gas. Consequently, taxation discourse and incidental government actions have been centred on upstream oil and gas[1]. This may largely be due to the fact that power was not privatized. With the recent development of unbundling of National Electric Power Authority that witnessed the privatization of electricity coupled with the recent discovery of renewable energy actiVATes the understanding of the nature and scope of the energy sector in Nigeria[2]. In fact, with the implementation of the government's reform programme in the Nigerian Electricity Supply Industry (NESI) reputed to be one of the most ambitious privatisation exercises in the global power industry, it has contributed a transaction cost of over three billion dollars ($3.0bn) into the Nigerian economy[3].

Energy is a broad term that warehouses several sectors each of which may stand alone as an industry including but not limited to power industry. It comprises the extractive products which are used as source of energy and electricity power, nuclear power, coal power,

renewable energy like solar power, hydroelectric power and wind power. In treating power as an industry, there has also been a misconception of energy and power as both are used contemporaneously as if both mean the same thing, though they are closely related. This calls for summary explanation. Energy is the *capacity* to do work i.e. move an object measured in joules, or even calories. For electrical energy, it is measured in watt-hour. On the other hand, power is the rate of producing or consuming energy. Power is energy per unit of time, and measured in watt[4].

There is no gainsaying the fact that energy sector a set of is utility-driven activities for consideration or money's worth. Therefore, the consideration and analysis of the taxability of the utility so created cannot be over-emphasised in the context of value added tax (VAT). As a matter of law, the system of VAT is multi-layered as it is imposed at every stage of value addition in the chain of utility creation. The valued added tax is a consumption tax imposed on all supply of VATable goods and services in Nigeria. The principal legislation on this specie of indirect tax is known as Value Added Tax Act (VAT Act) and it has been an existing law which remains valid and enforceable throughout Nigeria. Therefore, every supply for consideration other than those exempted by the VAT Act is chargeable. Power supply is a transaction involving series of economic activities supplied for consideration. The stages of economic activities performed in the supply of power include generation, transmission and distribution of power.

The supply of electric power, wind power or solar power is not tangible but substantially creates human needs or utility. In discussing this paper, effort is made to consider whether such power supply qualifies for value added tax giving the extant provision of the VAT Act as against the general argument that the nature of power such as electric power or renewable energy like solar or even hydroelectric power cannot ordinarily be regarded as goods item or services envisaged under the principal legislation. Hence, this paper is divided into four parts. In addition to the introductory part, Part 1 is dedicated to an overview of the business of power supply and identifies the various stages in the chain of utility creation. Part 2 considers the conditions for the application of value added tax to supply of goods and services. Part 3 gives a critical analysis of VATability of electric power / solar power supply under the current legal order and comparison with other jurisdiction like United Kingdom. Part 4 focuses on the proposition for reforms and conclusion.

Scope of this Paper

As earlier indicated in the preceding paragraph, energy sector covers all source of power generation which is not limited to oil and gas. However, the focus of discourse herein is limited to energy supplied through electricity either through hydroelectricity or solar power. The reason largely is based on the fact that energy generated through oil, gas, and coal can actually fit into the description of goods items contemplated under the Value Added Tax Act. The propositions and submissions presented in this paper therefore are directed strictly to cover electricity power supply.

2. Understanding the Business of Power Supply in Nigeria

As earlier stated, supply of power is a hub of activities and it is in stages which also necessitate obtaining license and approvals from the appropriate regulatory authority as provided and envisaged in the Part IV of the principal legislation[5] that guides the power sector. A better understanding of the business of power supply shall be discussed in the light of the economic activities available within the sector namely: power generation[6], power transmission[7], power distribution[8], system operation[9] and trading[10]. In the power supply, the major stakeholders are the transmission company, the Gencos, the Discos and the end users or consumers. Power is generated from the power plant and transmitted through the national grid by the Gencos; the quantity generated is supplied to the discos from the grid to the transmission lines. The Discos takes delivery and distributes to the consumers. From this simply analysis, it can be seen that while there is a supply of right of use by Transmission Company of Nigeria(TCN) to Gencos, power is supplied to Discos through a power sub-station and which is further distributed to the consumers' homes, factories, shops and so on through the alternating current voltage transformers. Note that each of these stages of supply is done for money's worth or consideration.

Figure 1 Inter-Relationship Component Chart in the Energy Sector

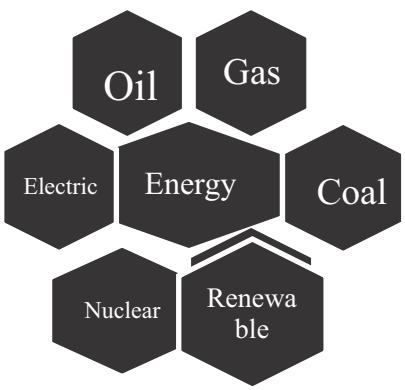

Figure 1 shows the energy relationship with other components. Energy is at the center while other industries as shown in the chart above are attached. It should be noted that all the attached industries can produce power and supply it in commercial quantity.

Power generation

This is the process of generating electric power from sources of primary energy. For electric utilities in the electric power industry, it is the first stage in the delivery of electricity to end users, the other stages being transmission, distribution, energy storage and recovery, using pumped-storage methods. Production is carried out in power plants. Electricity is most often generated at a power station by electro-mechanical generators, primarily driven by heat engines fueled by combustion or nuclear fission but also by other means such as the kinetic energy of flowing water and wind. Other energy sources include solar photovoltaics and geothermal power[11].

Presently, there are thirty-eight (38) GenCos in Nigeria some of which specialized in generating power through oil and gas, water (hydroelectricity), sunlight (solar) and wind[12].

Figure 2: A Generating Plant

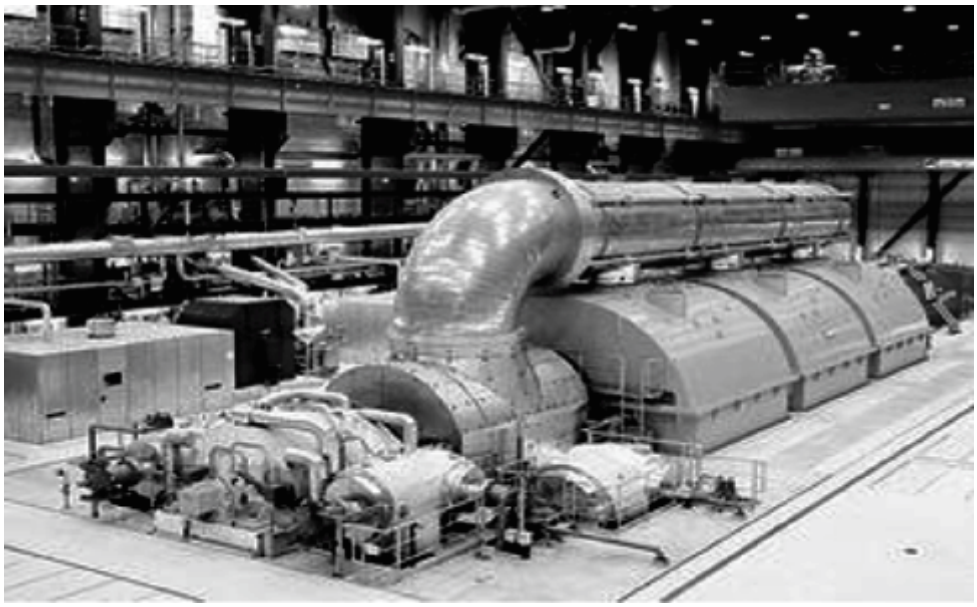

Figure 2 shows a generating plant showing the turbines generator. The power generated herein is transmitted to the grid and ready for supply to the Discos.

Power Transmission

This is the bulk movement of electrical energy from a generating site, such as a power plant, to an electrical substation. The interconnected lines which facilitate this movement are known as a transmission network. This is distinct from the local wiring between high-voltage substations and customers, which is typically referred to as electric power distribution. The combined transmission and distribution network is known as the "national grid" in Nigerian or “power grid” in other countries like United Kingdom, India, North America and Malaysia. In the local parlance, the national grid is otherwise known as power lines. The authority in charge of the transmission of power in Nigeria today is known as Transmission Company of Nigeria (TCN). As today, there are presently twenty-three (23) grid-connected generating plants supplying power in the country.[13] What TCN does is to provide the platform i.e. the network which is the transmission lines on the national grid. The TCN neither supply any power nor distribute anything. Rather it grants the GenCos the right to use the network which is a form of non-tangible item not covered by the valued added tax classification of goods and services.

Figure 3 Sample of Power Sub-Station

Figure 3 shows a sample of sub-station where power is transmitted by the Gencos to the Discos.

Power Distribution

This is the final stage in the delivery of electric power; it carries electricity from the transmission system to individual consumers[14]. Distribution substations connect to the transmission system and lower the transmission voltage to medium voltage ranging between 2 kVand 35 kV with the use of transformers. Primary distribution lines carry this medium voltage power to distribution transformers located near the customer's premises. Distribution transformers again lower the voltage to the utilization voltage used by lighting, industrial equipment or household appliances. Often, several customers are supplied from one transformer through secondary distribution lines. Commercial and residential customers are connected to the secondary distribution lines through service drops.

Figure 4: A Transformer

Fig 4: This represents the usual 33KVA transformers installed on the street to enable the Discos reach the customers[15].

In Nigeria today, there are eleven Discos registered and licensed to distribute power to the Nigerian population[16]. These are: Abuja Disco, Benin Disco, Eko Disco, Enugu Disco, Ibadan Disco, Ikeja Disco, Jos Disco, Kaduna Disco, Kano Disco, Port-Harcourt Disco and Yola Disco.

Figure 5 The Chains of Production of Power Supply

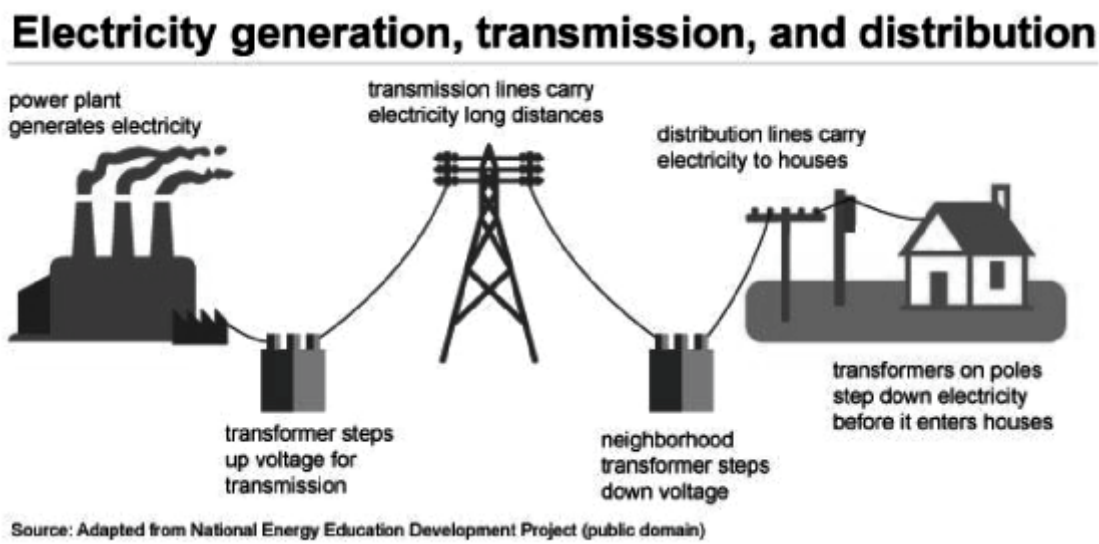

Figure 5: This shows the chains of production of power supply from generation, transmission to distribution to the final consumers[17].

3. Nature, Scope & Basis for Charging of Value Added Tax

As a general principle of taxation, issue of tax, imposition, charging, ascertainment, assessment, payment and enforcement of compliance are matters of statute as may be provided in the enabling law. It cannot be implied[18]. The principal legislation that provides for charging, ascertainment, computation and application of VAT in Nigeria is known as Value Added Tax Act[19].

By virtue of Section 2 of the Act, a tax known as VAT is chargeable on the "supply of goods and services" other than those exempted in the Act. The implication of this provision is that an item is VATable once it is qualified as goods or services, and it is supplied to another person for money's worth and it is not exempted by the Act[20]. For the Act to apply, following factors must be considered:

i. The supply made must be a goods or services
ii. The supply must have been for a money consideration;
iii. The goods or services must not have been exempted by the Act; *and*

iv. The consumer must be a taxable person under Act

In ***FBIR v Ibile Holdings***[21], the VAT Tribunal being the relevant judicial body at the material time succinctly held as follows:

> *We observe that the major business of the company is not buying and selling land and building, selling and renting of properties. We are of the view that these activities constitute the taxable goods of the company which come under the purview of the provisions of Section 42 which unequivocally spell out the supply of good to include sale and delivery of taxable goods used outside the business, the letting out of taxable goods or hire or leasing and any disposal of taxable goods.*

In the light of the above established position of the law, it seems that so long as a particular item be it goods or services is supplied and not expressly exempted under the Act, it will be subject to VAT liability. As sound as this position may seem, authorities abound that suggest a contrary view. For instance, the Federal High Court in the case of ***CNOOC v Attorney General of the Federation & Ors (the CNOOCs case)***[22], held that a transfer of chose in action such as "a contractual right" does not qualify as goods or services that can be taxed under the Act.

In view of the above judicial pronouncement, the basis for charging VAT as presently constituted creates a loophole for intangible articles or items or things which are neither goods nor services such as franchise right, grants, license, and so on. Suffice to conclude that the act of supplying alone is not enough to justify VATability of any article; it is the supply with payment of consideration for the things or articles (tangible or intangible) supplied that characterizes its taxability in VAT.

4. VATability of electric power/solar power supply under the Act

As can be gleaned from Figure 5 provided before now, the channel of power supply is depicted in the power plant, sub-station and distribution lines. They are not ends but a means to an end. These are equipment and not the power energy and power generated by the GenCos and supplied to the Discos which is eventually distributed to the consumers. The power can neither be seen nor touched. The question therefore is whether such power supply is categorized as goods or services contemplated under the Act on one hand let alone taxing the supply; are the GenCos and Discos within the meaning of taxable persons on one hand and the TCN that simply makes its platform (distribution network) as taxable person on the other hand.

Is Electricity Power in the nature of goods or services?

There had been raging controversy over the nature of electricity as either goods or services at the international trade forum. According to the World Trade Organization Services Sectoral Classification List, MTN.GNS/W/120, July 10, 1991 neither the General Agreement on Tariffs and Trade (GATT), which explicitly covers goods, nor the General Agreement on

Trade in Services (GATS), which explicitly covers services, clearly define electricity, nor do they explicitly decide on its inclusion or exclusion. The GATS comes close, as it includes a section entitled "Services Incidental to Energy Distribution"[23].

The subject matter of the value added tax in Nigeria is the goods and services supplied to the consumers. In other jurisdiction like India, Australia and New Zealand, it otherwise referred to as "goods and service tax". It is not in doubt that something is supplied for money consideration but in the power sector and electricity in particular, whether what is supplied is a goods or service has been controversial. The principal legislation on value added tax neither defines the word "goods" nor interprets the meaning of "services" in the context in which the words are used in the Act. This precipitates reliance on external aids in interpreting these cardinal terms. By the nature of electrical power, it is very difficult to classify it as goods or services. However, the critical arguments of the economic philosophers who belong to utilitarian jurisprudential school of thought such as the Jeremy Bentham (1748–1832) and John Stuarts Mill amongst others is that anything that satisfies human needs or creates utility is either a goods or service. The opinion of this school of thought has received judicial approval in United States, Australia, New Zealand and New South Wales.

United States

*In **Otte v Dayton Power & Light Co***[24] the facts are that a consumer suffered injury to his property as a consequence of a malfunction in the electrical supply provided by the defendant. The plaintiff sought to establish strict liability for the tort of selling a product in a defective condition which was unreasonably dangerous to the user or consumer or to his property. The relevant question in the case was "whether the supply of electricity was the selling of a product". The Supreme Court of Ohio described as ``an intellectual disaster'' the plaintiff's attempt to equate the process of creating and delivering electricity to the manufacture and sale of an ordinary consumer product. This was in part because of the special characteristics of the errant voltage in that case. Of greater interest for the purpose of determining the nature of electric power is the following passage in the judgment of the Court:

> *Consumers, moreover, do not pay for individual electrically charged particles. Rather they pay for each kilowatt hour provided. Thus, consumers are charged for the length of time electricity flows through their electrical systems. They are not paying for individual products but for the privilege of using DP & L's service.*

The Court then observed that the electrical charge received by the consumer is substantially different from that which leaves the generator plant where the supposed manufacture takes place, so that this requirement for strict product liability had not been established. The Court then concluded:

> *For this reason, and for the reasons stated above, we find electricity is a service, not a product, in the generally accepted sense of the word under the factual context of this case.*

This represents the current position in the United States until a contrary decision is made.

Australia

Contrary to the United States perspective, the Australian Court considered the supply of electricity power as a thing or product or goods for sale. The Supreme Court of Victoria established this perspective in ***AGL Victoria Pty Ltd v Lockwood***[25]. F&T agreed to buy and AGL agreed to supply electricity on the terms of the agreement. The contract, in annexure 1, fixes the price for this supply at a rate per MWh. There is also a demand charge which is calculated by reference to MVA/year.

> *In normal legal usage, a sale, or for that matter a purchase, involves the transfer to the purchaser of a thing or rights to a thing in exchange for money or other consideration. In the case of the supply agreement, this thing is a type of energy with certain qualities. The measure of the thing sold is in terms of the period of time of its provision. What exactly this energy is was said by Professor Mareels to be uncertain, although it has certain known characteristics. Nevertheless, F&T received this thing which was a benefit to it and it used the thing in its manufacturing process. Whatever it be, it is a thing which AGL was prepared to sell and F&T was prepared to purchase.*

The Court gave an analogical perspective of the circumstances in which a transaction may be classified as goods or service when it held as follows:

> *If the contract uses ``sale'' and ``sell'' in this sense, it becomes very difficult to characterise as services rendered the essential activity of AGL in the performance of its obligation under the supply agreement. I take as an example the case of a customer desirous of acquiring a motor car. The customer goes to a dealer, who does not then own the car, and agrees the sale price. As I have mentioned, where the dealer does nothing more than sell and procure the delivery of the car to the customer, the transaction is characterised as a sale by the dealer to the customer because, on a proper analysis, the owner sells to the dealer and the dealer on-sells to the customer. Where, however, the dealer is merely acting as a broker, whose task it is to find an owner and to negotiate a price for a sale direct from the owner to the customer, the transaction between the dealer and the customer might be characterised as that of rendering services.*

It is worth noting that there are legislative definitions of "services" in both United States and New Zealand which aided the Court in arriving at their decisions. In recent times, the parliament of the Commonwealth of Australia Senate in its New Tax System (Goods and Services Tax) Amendment (Make Electricity GST Free) Bill 2017 makes a supply of electricity GST-free. The argument in support of this bill is that electricity just like water should be considered as an essential service. This would commence from the first day of the quarter following Royal Assent. This proposal supports some scholars' contention that *"VAT is, or should be in concept, a tax on consumption by final consumers. It should not be a cost on businesses."*[26]

United Kingdom

In the UK, the attention is not on the classification as to whether a thing is "goods" or "service". The VAT Act, 1994 is fundamentally concerned with "supply" of things which may either be goods, service or something which can neither be classified as goods nor services. In Section 5(2)(a) of the Act, the word "supply" is defined to include all forms of supply but does not include anything done otherwise than for a consideration. Hence, in ***Customs and Excise Commissioner v Diners Club Ltd***[27], the act of buying a debt owed to another company was held to be a supply of service and subject to value added tax. In that case, the court went further to hold that anything which is not a supply of goods but is done for a consideration (including if so done, the granting of assignment or surrender of any right) is treated as a supply of service. Unlike other jurisdiction, the United Kingdom has express provision covering the VATability of electricity power including gas, fuel, coal, heat and host of other forms of energy. Electricity is subject to value added tax though at a reduced rate of 5% instead of 17.5% on general goods and services[28].

India

There is a 101st Constitution Amendment Act, 2016, through which the Indian Government shares the legislative powers to levy Goods and Services Tax (GST). In its Entry No. 53 of the State List, "taxes on the consumption or sale of electricity" is reserved and constitutes the subject matter for the State Government and no GST is to be levied on alcohol for human consumption, property registration, petrol, diesel and electricity are clearly outside of GST in India.

However, before the amendment, there has been similar controversy on the classification of electricity as being goods or services and the Supreme Court of India had made pronouncement in plethora of cases. In ***CST v. M.P. Electricity Board, Jabalpur (the CST's Case),***[29] the Supreme Court held that electricity is 'goods'. In the case of ***State of Andhra Pradesh v. National Thermal Power Corporation***[30], the Constitution Bench approved the observations made in M.P. Electricity Board ***the CST's Case*** to the extent that electrical energy can be transmitted, transferred, delivered, possessed, etc., but did not agree with the observation that electrical energy can be stored. The Constitution Bench then held that significant characteristic of electrical energy is that its generation or production coincides almost instantaneously with its consumption.

However, in a latter decision as contained in ***Karnataka Power Transmission Corporation v. Ashok Iron Works private Limited***[31], the court considered specifically the issue whether electricity is goods or service under the Consumers Protection Act regarding the deficiency of energy supplied and or purchased. In that case, the Supreme Court though considered its earlier decision in ***the CST's Case*** but held that electricity is not goods but service. The Court reasoned that given the express provision of Section 2(1)(o) of the Consumer Protection Act, 1986 that defines "service" a thus:

> *"Service" means service of any description which is made available to potential users and includes the provision of facilities in connection with*

> *banking, financing, insurance, transport, processing, supply of electrical or other energy, board or lodging or both, entertainment, amusement or the purveying a news or other information, but does not include the rendering of any service free of charge or under a contract of personal service."*

In the light of the above provision, the Court took the view that from the place of generating electricity, the electricity is supplied to the sub-station installed at the units of the consumers through electrical high-tension transformers and from there electricity is supplied to the meter. The Court concluded that electricity is rather a service and not goods[32].

Nigeria

Coming down home, neither the Electric Power Sector Reform Act[33] (EPSR Act) that regulates the business of electricity power supply in Nigeria nor the VAT Act defines "goods" or "services". The provision of Federal Competition and Consumer Protection Act[34] however attempted to define and classify gas and electricity as "goods". Reading the provision of Section 62(1) of EPSR Act, one can say that the identified transactions and or trading activities involved do not suggest whether electricity power is either goods or service. However, the EPSR Act is suggestive of the fact that some dealings in power supply are goods while others are services. For clarity, Section 62(1) of the Act provides thus:

> *62.-(1) No person, except in accordance with a license issued pursuant to this Act or deemed to have been issued under section 98 (2), shall construct, own or operate an undertaking other than an undertaking specified in subsection (2) of this section, or in any way engage in the business of:*

(a) electricity generation, excluding captive generation; for by
(b) electricity transmission;
(c) system operation;
(d) electricity distribution; or
(e) trading in electricity,

The act of generating, transmitting, operating, distributing and trading for all intent and purposes cannot be a product but services rendered by someone[35]. However, to the end-user of the electricity so generated, distributed, traded and supplied which is eventually used cannot be service but a product. Hence, supply of electricity will be a service rendered by the GenCos to the Discos on one hand, it will be a product to the final consumers. This submission finds support from the definition of "market power" in the interpretation section of the EPSR Act.

Suffice to say that the EPSR, Act does not contemplate electricity power supply as goods but service as the consumers pay for the energy used and not the power station, transmission lines, meter board or bulbs. They pay for *each kilowatt hour provided.* This cannot be faulted for the reason that the contract entered into between consumer and supplier requires the supplier to perform obligations or do work which will result in the provision of electricity to a consumer. To this end, the supply of any of the services mentioned in Section 62(1) of the

EPSR Act would be subject to value added tax in so far as none of it is excluded and or exempted by the Act.

For argument sake, this position seems perfect for the generation, distribution and trading companies but certainly not for the services rendered by the transmission company. This is due to the fact that the Transmission Company of Nigeria (TCN) neither generate nor distribute energy. It simply makes its platform / network available for use by the generating companies to ease and facilitate the movement or process of supplying and delivering energy to the distribution companies.

5. Conclusion

By virtue of Section 2 of the VAT Act, Act, value added tax is chargeable on the "supply of goods and services" other than those exempted in the Act[36]. The implication of this provision is that an item is VATable once it is qualified as goods or services, and it is supplied to another person for money's worth and it is not exempted by the Act. A perusal of the items on the First Schedule to the Act does not contain electricity as an exempted item. Consequently, it is presumed to be subject to tax under the Act. This forms the basis of the VAT invoice of 5% which has now been increased to 7.5% on the electricity bills from GenCos in respect of the supply to the Discos and similar invoice to the Discos' customers who are the end-users. No such invoice is noticeable from the TCN to the GenCos despite the fact that the use of the national grid / platform is for a consideration.

It is conceded that TCN does not produce and or generate energy but its platform creates utility to the GenCos. In as much as it could be regarded as service by the proposition above, it should be VATable. However, the decision of the Federal High Court in ***the CNOOC's Case***[37], does not suggest that TCN can validly invoice the GenCos for the grant or use of the national grid or network. In that case, the Court held that a transfer of "chose in action" such as "a contractual right" does not qualify as goods or services that can be taxed under the Value Added Tax Act. Suffice to say that the right or permission granted to use the TCN network for money consideration is neither goods nor services contemplated under the VAT Act. The judicial activism may however be actiVATed to bring such service into the value added tax net.

6. Recommendation

As earlier identified in this paper, there is no express provision categorizing electricity as either goods or service; it is also not an exempted item under the VAT Act. There is a looming legal dispute which may throw the adjudicatory body into legal controversy. It is therefore recommended as follows:

a. Effort should be made to amend the VAT principal legislation and EPSR Act to conceptualize and define the terms "goods / services" in broad terms to include "*anything capable of being made, rendered, purchased, used and or satisfy human needs"*. This will cover those utility created which may neither be explicitly classified as goods and services such as contractual right, brokerage in power supply etc.

b. Just as is being practised in United Kingdom, a "reduced rate" is recommended to the relevant authority for value added tax on supply of electricity power for both domestic and commercial purpose. A reduced rate of 2.5% will not be a bad idea to encourage investment and boost the nation's production economy. Invariably, there would be a drastic fall in the electricity prices to domestic and industrial expenditure while the commodity price index is further reduced. Of course, the government revenue would drop by 5% coming from electricity supply which is not up to 0.5% of the total contribution of value added tax to national gross domestic product of the Government of the federation.

c. In the alternative, the relevant authority may classify electricity as a zero-rated goods/service while the Indian model may also be considered to decentralize the charge, collection and remittance of value added tax to the federating States. The country may also adopt the method whereby VAT on business electricity and gas bills is charged at a rate of 7.5%, but some businesses will be able to pay a reduced rate of 5% provided they use less than 33 kilowatt hours of electricity - or less than 145kw hours of gas per day as it is done in the UK.

Except there is a clear judicial authority on the nature of electricity as either as goods or service, a legal challenge against its subjectivity to value added tax may result into unhealthy relationship in the electricity power market. In the circumstance, as Lord Denning (MR) of blessed memory said in ***Parker v Parker***[38] *"that no case has been found in which it has been done before….. If we never do anything which has not been done before, we shall never get anywhere. The law will stand still while the rest of the world goes on, and that will be bad for both.*

ENDNOTES

1. There is a special legislation on taxation of petroleum oil, special regulations on value added tax for oil and gas companies as contained in Petroleum Profit Tax Act, Cap P13, LFN 2004; Even though there is a principal legislation that regulates the business of power generation, transmission, distribution and trading in power supply and the Companies Income Tax Actgenerally applicable to all companies, no attention is paid to the peculiar nature of the transactions involving power such as electricity, solar, nuclear and wind power and how supply can be subjected to value added tax. This is considered as neglect and or omission compared to what is obtainable in other jurisdiction like the United Kingdom. This paper is also directed at the relevant tax administrators and legislature to see the need to take the power sector seriously.
2. Electric Power Sector Reform Act, 2005, the Transfer Order No 85 Vol. 97 of 20th August, 2010
3. http://www.nercng.org/index.php/home/nesi
4. Power used by a 60-watt light bulb is 60 watts. Now, how much energy the bulb uses depends on how long it is left burning. A 60-watt bulb burning for an hour would consume 60-watt-hours of energy. Ten bulbs burning for ten hours would consume 6,000 watt-hours of energy or 6Kwh. This is graphically explained in Fig: 2. Thus when discussing energy storage for renewables (e.g. solar) and choosing batteries. This is why "how much total energy can the system produce" (In Watt-hours) and how much total energy can the system store" (In Watt) are considered as fundamental clauses in power supply agreement. Therefore, it is one thing to produce enormous energy and another thing is the load the energy can carry or power.
5. Electric Power Sector Reform Act, Cap E7, LFN 2005 (as amended)
6. Section 64 of EPSR Act
7. Section 65 of EPSR Act
8. Section 67 of EPSR Act
9. Section 66 of EPSR Act
10. Section 68 of EPSR Act
11. https://en.wikipedia.org/wiki/Electricity_generation; Nuclear energy comes from splitting atoms of uranium in a reactor to heat water into steam, turn a turbine and generate electricity. https://www.washingtonpost.com/lifestyle/style/explaining-nuclear-energy-for-kids/2011/03/15/ABhFsfl_story.html?noredirect=on&utm_term=.e6cf6c90dcd5 Renewable energy is energy that is collected from renewable resources, which are naturally replenished on a human timescale, such as sunlight, wind, rain, tides, waves, and geothermal heat - Ellabban, Omar; Abu-Rub, Haitham; Blaabjerg, Frede (2014). "Renewable energy resources: Current status, future prospects and their enabling technology". Renewable and Sustainable Energy Reviews"Renewable energy resources: Current status, future prospects and their enabling technology". Renewable and Sustainable Energy Reviews. 39: 748–764 [749]. doi:10.1016/j.rser.2014.07.113.
12. According to Information Guide Nigeria, the 38 GenCos currently operating in Nigeria are kanji Power Station Reservoir; Jebba Hydro Power Station; Shiroro Power Station; Transcorp Ughelli Power Station; Afam I- IV & V Power Station; Geregu I Power Station; Omotosho I Power Station; papalanto (Olorunsogo) Power Station; Kwale Okpai Power Station(IPP); Afam VI Power Station; Ibom Power Station (IPP);

Aes Barge; Omoku Power Station (IPP); Trans-Amadi Power Station (IPP); Rivers Ipp; Aba Power Station (IPP); Geregu II Power Station (IPP); Sapele Power Plant; Alaoji Power Plant; Olorunsogo II Power Station; Omotosho II Power Station; Omoku II Power Station; Ihovbor Power Station; Egbema Power Station; Calabar Power Station; Gbarain Power Station; Mambilla Power Station; Itobe Power Station, Azura Thermal Power Station; Kano Power Station, Qua Iboe Power Plant; Zungeru Power Plant, Kaduna Power Plant; Gurara Power Plant, Dadin Kowa Hydro Power Plant; and Okpai Power Plant (Phase II) See also https://infoguidenigeria.com/power-stations-nigeria/

13. http://www.nercng.org/index.php/home/nesi
14. Short, T.A. (2014). Electric Power Distribution Handbook. Boca Raton, Florida, USA: CRC Press. pp. 1–33. ISBN 978-1-4665-9865-2; See also https://en.wikipedia.org/wiki/Electric_power_distribution
15. https://en.wikipedia.org/wiki/Electric_power_distribution
16. http://www.nercng.org/index.php/contact/discos
17. https://www.eia.gov/energyexplained/index.php?page=electricity_delivery. Last updated on 31st August, 2018
18. Cape Brandy Syndicate vs Commissioner of Inland Revenue 12 Tax Cases 358 at 366
19. Cap V1 LFN, 2004 (as amended). The Value Added Tax Act was formerly enacted as a decree in 1993 which came into force on 1st September, 1993 during the military era at the time in Nigeria. Any reference to this statute in this paper shall be the "Act" except where otherwise expressly stated); and by extension, it includes all the Rules and Regulations which have been made pursuant to the principal legislation.
20. Section 2 of the Act imposes VAT on supply of goods or services to any person which presupposes a supply either within a state, interstates of the federation or outside the country as a whole. It should be noted that by Section 34 of the Finance Act, 2019, Section 4 of the principal legislation which originally fixed the tax rate at 5% was recently reviewed and increased to 7.5% with effect from 1st February, 2020.
21. 2 TLRN 3 (2010) 151; In that case, one of the submissionsandcontentions of the Applicant is that the Respondent's business of property management such as renting, leasing and sale of properties is VATable. The Respondent argued otherwise. The VAT Tribunal resolved the issue in favour of the Board and came to the conclusion that once there is supply of goods and services not exempted by the Act, the service is VATable.
22. (2011) 4 TLRN 185, the Federal High Court, per Bello J (as he then was) reasoned that since the Act did not clearly define the words "goods" or "service" transfer of contractual right or chose in action which does not match the qualities described in the dictionary used as an external aid (going by the counsel submission) for goods or services subject of value added tax.
23. sourced from: https://www.stout.com/insights/article/debate-charges-electricity-good-or-service
24. 523 NE 2d 835 at 839(Ohio 1988); This decision was accepted and applied in the Appellate Division of the Supreme Court of New York in the US cases, Bowen v Niagra Mohawk Power Corporation 590 NY Supp 2d 628 at 631-2 (1992). The Court held that "electricity is the flow of electrically charged particles along a conductor. The utility does not `manufacture' electrically charged particles, `but rather, sets in motion the necessary elements that allow the flow of electricity'. In that context also, the Court concluded that electricity supply is not a product for sale but a service.

25. (2003) VSC 453
26. David Child "VAT Administration: Addressing PriVATe Sector Concerns" in VAT in Africa edited by Richard Krever (Pretoria: Pretoria University Law Press) Page 130
27. (1989) 2 All ER 385
28. See Section 29A(1)(a) of Value Added Tax Act, 1994 and Section 99(1)(4) Finance Act, 2001.
29. (25 STC 188),
30. (2002) 5 SCC 203
31. [2009] 3 SCC 240
32. The same Supreme Court however treated electricity as goods while considering the provision of Sales Tax Law in the case of Southern Petrochemical Industries Co. Ltd. v. Electricity Inspector & ETIO and Others (2007) 5 SCC 447. The Court made following pertinent obserVATions:
    It may be that electricity has been considered to be "goods" but the same has to be considered having regard to the definition of "goods" contained in Clause 12 of the Article 366 of the Constitution of India. When this Court held electricity to be "goods" for the purpose of application of sales tax laws, in our opinion, the same would have nothing to do with the construction of Entry 53 of List II of the Seventh Schedule of the Constitution of India.
33. Cap E7, LFN 2004
34. By Section 167(1) of the FCCP Act, 2018, defines the term "goods" when used with respect to particular goods includes gas and electricity therefore classifying gas and electricity as goods and not service. Considering the various economic activities in the energy sector, it may be difficult to classify the service rendered by Transmission Company of Nigeria as "goods" who merely grants the use of its platform for transmission of energy to the GenCos.
35. In Section 100 of the EPSR Act, all these undertakings are defined as follow which contemplates that electricity is a service. For instance, "Distribution" means the delivery of electricity over a distribution system;
    "Generation" means the production at a generating station of electric power and other generation products such as, but not limited to, reactive power;
    "Trading" means any form of marketing, brokering or intermediation in the sale of electricity, whether or not it entails the purchase of electricity for resale, or whether or not title is taken to the electricity sold;
    "Transmission" means the conveyance of electric power and energy over a transmission system
36. Section 2 of the Act imposes VAT on supply of goods or services to any person which presupposes a supply either within a state, interstates of the federation or outside the country as a whole.
37. (2011) 4 TLRN 185, the Federal High Court per Bello J (as he then was) reasoned that since the Act did not clearly define the words "goods" or "service" transfer of contractual right or chose in action which does not match the qualities described in the dictionary used as an external aid (going by the counsel submission) is not goods or services subject of value added tax.
38. (1953) 2 All ER 127 at 129

CHAPTER 12

VALUE ADDED TAX IN NIGERIA'S OIL AND GAS SECTOR – CHALLENGES AND RECOMMENDATIONS

Abstract

The importance of Value Added Tax (VAT) in Nigeria's fiscal revenue equation cannot be overemphasised. VAT contributed about 31% (₦1.531 trillion) of the tax revenue of ₦4.95 trillion in 2020 as reflected in the Federal Inland Revenue Service (FIRS) 2020 Tax Statistics Report.[1] Peculiarity of the oil and gas industrial service providers, where non-resident companies (NRC) render most of the services, constituted a bane to efficient compliance with VAT remittance requirement, and this made government to lose revenue. Therefore, government changed the collection and remittance aspect of the VAT obligation through a reverse charge and source deduction mechanism by a gazette amending the extant VAT legislation[2] and FIRS Public Notice[3] on 15 June 2007 and 11 December 2007 respectively. The regulatory change which shifted the hitherto VAT collection obligation of the suppliers to the customers (i.e. companies operating in the Nigerian oil and gas sector) addressed the non-remittance of VAT revenue, but it came with attendant challenges. This Chapter reviews the challenges and proffers feasible reform solutions, whilst taking account of recent regulatory developments such as issuance of FIRS public Notice in 2019[4] and amendments to the Value Added Tax Act[5] VAT Act vide the Finance Acts 2019 and 2020.

1. Introduction

Value Added Tax (VAT) is a multistage consumption tax, which is charged and payable on the supply of all goods and services, other than those specifically listed as exempted in the First Schedule to the VAT Act. Since its introduction in 1993, VAT has become an important source of revenue to the government, accounting for about 31% of the total tax revenue generated in the country in 2020 as reported in the FIRS Tax Statistics/Report.

Based on the requirements of the VAT Act, it was the primary responsibility of the supplier of taxable goods and services to charge, collect and remit the tax to the FIRS. However, it was observed that there were numerous cases of non-compliance by suppliers of taxable goods and services. This was particularly alarming for the oil and gas sector of the economy, given the large scale activities in that sector and the contribution of the sector to revenue generation in the country. Consequently, such compliance gaps with respect to VAT was estimated to have been leading to colossal loss of government revenue. This necessitated inquisition into possible ways to address the noticeable gap in VAT compliance and ensure optimum VAT collection in the sector.

As in 2007, the Federal Government enacted the VAT (Amendment) Act that amended the VAT Act.[6] Among the amendments to the VAT Act was the introduction of section 13(2) which provided that *"the Service may, by notice, determine and direct the companies operating in the oil and gas sector which shall deduct VAT at source and remit same to the Service."*

Subsequently, the FIRS on 11 December 2007, through its public notice titled "***Notification of Guidelines on the Implementation of VAT Deduction (Reverse Charge) and New Payment Arrangement with Respect to Fees, Levies, and other Charges Payables by Companies in the Oil and Gas Industry***" (the Notice), directed taxpayers in the oil and gas industry to deduct VAT at source before payments are made to suppliers or vendors on goods and services consumed. This is termed the *"reverse charge principle"*. The reverse charge principle has been more successful in VAT collection than the prior approach where the responsibility was vested in the hands of the suppliers.

Despite the enormous success in VAT collection brought about by the reverse charge principle, so many questions have trailed the implementation. Some of the challenges include:

2. Which companies are covered by the reverse charge principle?

According to section 13(2) VAT Act and the Notice, the VAT reverse charge principle applies to *"companies operating in the oil and gas sector"*. There was no specific definition for companies operating in the oil and gas sector in the VAT Act and the Notice. Thus, the following are the questions arising on the exact scope and coverage of the words *"companies operating in the oil and gas sector":*

- What qualifies a company as *"operating in the oil and gas sector"?*
- Should oil and gas companies be restricted to crude oil exploration and production companies (E&P companies), petroleum products marketing companies and companies that provide exclusive engineering services to E&P companies?
- How about other companies that provide exclusive services to oil and gas companies such as personnel outsourcing companies, catering services, etc.?
- Should this be restricted to services of specialised nature?

In practice, oil and gas companies include exploration and production (E&P companies, or upstream sector), transportation or midstream players, petroleum products marketing companies (downstream sector) and companies that provide exclusive engineering services to E&P companies (oil servicing companies). Companies that provide subsidiary services to oil and gas companies such as personnel outsourcing, catering, etc. are not regarded as operating in the oil and gas sector for the purpose of VAT reverse charge and therefore not required to deduct VAT at source from their suppliers' invoices.

Given the continuous fiscal and tax system reforms in Nigeria, it will certainly be a welcome development for FIRS to issue a circular clarifying the companies that fall under the purview

of *"oil and gas"* companies for the purpose of VAT reverse charge mechanism.

What is the process of recovering input VAT under reverse charge principle?
A taxable person, upon rendering of its VAT returns, is required to recoup input VAT from the output VAT payable and remit the excess to the FIRS or be entitled to a refund of excess input VAT from the Board. Input VAT refers to the tax paid by a taxable person on goods and services purchased while output VAT is the tax received by a taxable person on goods and services sold.

However, Section 17(1) VAT Act restricts recoverable input VAT to "*tax on goods purchased or imported directly for resale and goods which form the stock-in-trade used for the direct production of any new product on which the output tax is charged"*.

Section 17(2) VAT Act further specifies that input VAT on services, general administrative expenses, overheads and capital expenses are not allowable as deductions against output tax. Rather, while the input VAT on operating expenses are written off to the income statements, the input tax on capital expenditure are capitalised alongside the cost of the item.

However, the implementation of VAT reverse charge mechanism creates challenge of input VAT recoverability to companies whose principal business activity is the sale of goods to companies in the oil and gas sector. This is because they are not in control of the output VAT from which input VAT could be recovered due to the reverse charge mechanism. This renders the application of section 16(1) impracticable under the reverse charge mechanism and puts the companies in a precarious cash flow situation.

While companies operating in the oil and gas sector can offset their recoverable net input VAT from VAT deducted from their suppliers' invoices, non-operators in the oil and gas sector will continue to face the challenge of accumulated excess input VAT for services rendered to operators in the oil and gas sector. The only option available for addressing this challenge is to seek a refund from the tax authorities. Considering time value of money, such companies might be in precarious cash flow situation. Hence, there is an urgent need to seek legislative amendment to expand the coverage of the input/output VAT offset system, given the VAT reverse charge principle.

The VAT refund process
Following from the unavailability of output VAT to be offset against input VAT under reverse charge, it may be convenient to argue that there is a provision for tax refund in the VATA. However, it should be noted that the refund process is not automatic but is subject to a special tax audit exercise to be carried out by the FIRS to establish the tax refundable amount, after due consideration to other tax liabilities due from the taxpayer. The tax refund process is onerous and time consuming. The special tax audit may result to less, nil or negative refundable amount. In the event of a negative refundable amount, the taxpayer would be required to pay additional tax liabilities to the FIRS.

Given the length of time it takes to close out an FIRS audit, the tax refund option is not a solution which ameliorates the foregoing concern in the short term. Where the refund is ultimately successful, the Board does not consider interest on the refundable amount to ameliorate the impact loss in the value of money suffered by the taxpayer.

Therefore, it is pertinent that the VAT refund system be simplified. A strategic way out would be the adoption and implementation of an automated taxpayer transaction tracking system, which will provide details of taxpayers' input VAT *vis-a-vis* their output VAT. Other approaches would include the isolation of a VAT refund case arising from an application of the "reverse charge mechanism", from other potential refunds arising from other tax types. This would facilitate the quick refund of recoverable input VAT arising from the implementation of VAT reverse charge and increase the confidence of the taxpayers in VAT administration.

Double VAT payment

Another major concern is that of double VAT payment with respect to companies whose client portfolio consist of companies within and outside the oil and gas sector. During tax audits or VAT verification exercises, FIRS would normally compute applicable output VAT based on the total turnover of the companies without considering portions of turnover on which output VAT had already been withheld at source by its oil and gas customers/ clients.

Over the years, it has been the practice of the tax authorities to demand for 'proof of remittance' of such withheld VAT from the affected companies. Where this 'proof' is not readily available as it is in practice, they are forced through the rigour of prolonged tax audit or settle the applicable VAT deducted at source.

This has posed a mind boggling question: Who has the statutory duty to provide the proof of VAT remittance? The operator in the oil and gas sector which has the statutory duty to deduct and remit VAT or the supplier which had suffered the impact of the reverse VAT charge?[7]

The supplier should not be burdened with the onerous task to provide the proof of VAT remittance. This should be the responsibility of the vendor (operator in the oil and gas sector), who remits the VAT to the FIRS. Furthermore, in line with the Federal Government initiatives on improving Nigeria's ease of doing business, the FIRS should ensure that the administration of the VAT reverse charge does not constitute undue burden to the service providers in the oil and gas sector.

The introduction of FIRS Tax Administration Solution (TaxPro-Max) which encompasses tax registration, filing, payment and automatic credit of withholding tax and other tax credits to the Taxpayer's accounts among other features is a good development.[8] However, there is need to improve the solution to automatically credit the service providers to the oil and gas sector with the payment of VAT deducted on their invoices as soon as such payment are remitted to the FIRS by the operators in the oil and gas sector.

This would consequently ease the reconciliation process during tax audit exercise and mitigate incidence of double VAT charge on companies.

3. Conclusion

In conclusion, FIRS should review and continue to fine-tune the VAT reverse charge mechanism which appears to have come to stay in the oil and gas industry. A welcome development would be to take positive steps towards identifying and straightening the bottlenecks in the tax administration and collection system. A potential benefit would be an improved level of voluntary tax compliance.

ENDNOTES

1. FIRS, 2020 Tax Statistics/Report, available at: https://www.firs.gov.ng/tax-statistics-report/accessed 13 June 2021.
2. Value Added Tax Act Cap. V1, Laws of the Federation of Nigeria (LFN) 2004 (VAT Act).
3. FIRS, Information Circular 02/2007, Notification of Guidelines on the Implementation of VAT Deduction (Reverse Charge) and New Payment Arrangement with Respect to Fees, Levies, and other Charges Payable by Companies in Oil and Gas Industry: https://taxaide.com.ng/files/Guidelines%20on%20Deduction%20of%20VAT%20at%20Source%20and%20New%20Method%20of%20Payment.pdf accessed 13 June 2021.
4. See FIRS Public Notice (the FIRS Notice) of 14th August 2019, in Nigerian newspapers, titled "…Deduction at Source of Withholding Tax (WHT)/Value Added Tax (VAT) on Compensation Paid to Agents, Dealers, Distributors and Retailers by Principal Companies".
5. Cap. V1, LFN 2004 (supra). References to the VAT Act is as amended to date.
6. See the Value Added Tax (Amendment) Act No. 12 of 2007 which received presidential assent on 16th April 2007.
7. By the combined effect of sections 10 and 13 VAT Act as amended, the reverse charge principle also applies to Nigerian counterparties of non-residents, and government ministries, departments and agencies (MDAs) respectively. The FIRS' attempted to extend the boundaries of reverse charge principle through its2019 Public Notice, to the fast moving consumer goods (FMCG) sector without any legislative backing to that effect. However, that effort appears to have been (rightly) discontinued, following the appointment of a new Executive Chairman of the FIRS in December 2019.
8. See the FIRS Public Notice, Introduction of FIRS Tax Administration Solution (TaxPro- Max), available at: https://www.firs.gov.ng/public-notice-introduction-of-firs-tax-administration-solution-taxpro-max/ accessed 13 June 2021.

CHAPTER 13

VALUE ADDED TAX IN THE TELECOMMUNICATIONS INDUSTRY

Abstract

The telecommunication industry (the industry) is a vital element of every economy. In Nigeria, the Industry accounts for about 9% of total rebased gross domestic product (GDP) based on data from the Nigerian Bureau of Statistics. The importance of the Industry in Nigeria cannot be overemphasized as other businesses such as internet services and online businesses, thrive on the industry's platforms. Basically, the introduction of Global System for Mobile Communications (GSM) into the Nigerian market caused a positive disruption in the national economy. This has changed the way people, government and society interact and conduct business. From the advent of the GSM and its attendant services in 2001, the annual growths in terms of subscribers, revenue and market penetration has increased over the years.

In line with Value Added Tax Act, 2004 as amended (VAT Act), businesses operating in the Nigerian telecommunication industry are required to pay value added tax (VAT) on the taxable goods and services consumed. This chapter critically analyse the telecommunication Sector of the Nigeria economy from VAT perspectives.

1. Introduction

The telecommunications industry is one of the most dynamic in Nigeria today. The transformation of the industry took off from the orthodox situation of being just service providers in 2001 to providing a wider array of value added services. Indeed, telecommunication companies (Telcos) have over the years become one of the country's major economic drivers. This is not limited to Nigeria. The world's economic landscape is changing, and this is partly attributable to the evolution of seamless exchange of data and information.

The Industry is an important growth driver of the Nigerian economy. According to the National Bureau of Statistics[1] (NBS), the telecommunications and information services sector accounts for about NGN6.9trillion (US$44.3bn), which is 9% of the rebased gross domestic product (GDP), approximated at NGN80.3trillion (US$510.1bn).

The Industry comprises several segments along the value chain. The major players in the various segments include operators, infrastructure and platform providers, device vendors, retailers and distributors. Different roles are performed at each of the segments of the

Industry, culminating into the variety of services enjoyed by the consumers.

Today, many businesses in Nigeria leverage the output of the telecommunications industry to meet the needs of their customers. For instance, numerous innovative products in the financial services industry, such as internet banking, mobile banking etc., rely heavily on internet access, which is an output of the Industry. Many on-line retail platforms have also emerged as a result of the impact of the Industry.

The development in the telecommunication industry has also come to the attention of the tax authorities who more than before, have subjected transactions by companies within the industry, to intense scrutiny. The objective, as can be reliably assumed, is to ascertain the completeness of revenue declared for tax purposes, and to ensure expenses claimed for tax purposes are valid.

To align the development of the industry with the expectations of the tax authority, tax policy makers have constantly reviewed laws and guidelines to conform to best practices and to ensure loopholes are plugged as far as possible. In doing so, they tend to compare the existing provisions of the law with the practicality of implementation and where necessary, issue guidelines to bridge the gap.

This Chapter focuses on the administration and applicability of VAT in the telecommunication sector. It also highlights the gaps that have been identified and how these have been resolved, or suggested amendments to the law to enhance the robustness of the tax laws in this regard.

2. Basis for imposition of Value Added Tax

VAT in Nigeria is governed by the VAT Act[2], the principal legislation, together with Guidelines and Circulars issued pursuant to the VAT Act. The provisions of the VAT Act is administered by the Federal Inland Revenue Service ('FIRS'). The Act empowers the FIRS to do *"such things as it may deem necessary and expedient for the assessment and collection of the tax"*.

In addition, the VAT Act empowers the Minister of Finance to amend, by order published in the Gazette, the rate at which the tax is chargeable and vary/modify the list set out in the First Schedule of the Act (exempt goods and services).

3. Statutory requirement to keep VAT records and file monthly returns

The VAT Act imposes a duty of full compliance on taxable persons. It requires all taxable persons to register for the tax, issue tax invoices, collect the tax, render returns, keep records and make records available for audit, amongst others.

A taxable person is defined in the VAT Act as "*an individual or body of individuals, family, corporations sole, trustee or executor or a person who carries out in a place an economic*

activity, ***a person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business*** *or a person or agency of Government acting in that capacity*".

Based on the above definition, Telcos fall within the bracket of taxable persons contemplated by the VAT Act. Therefore, they are required to comply with the provisions of VAT Act just like other Companies carrying on businesses in other sectors of the Nigerian economy.

4. Basis for imposition of VAT in Nigeria

Section 2 of the VAT Act imposes VAT on the supply of all goods and services other than those exempted by the same legislation.

The tax is chargeable at a standard rate of 7.5% on the supply of all VATable goods and services. Some specific goods and services are also subject to VAT at a rate of 0%.

5. Applicability of local VAT rules to Telecommunication transactions

A generally acceptable definition of telecommunication is the 'transmission of signs, signals, messages, words, writing, images and sounds or information of any nature by wire, radio, optical or electromagnetic systems'. Also, the Nigerian Communications Act ('NCC Act') defines telecommunication as '*any transmission, emission or reception of signs, signals, writing, images, sounds or intelligence of any nature by wire, radio, visual or electro-magnetic systems*'. Telecommunication is deemed to occur when the exchange of information between communication participants includes the use of technology.

Due to the unique nature of the telecommunication sector and the paucity of specific policies that provide clarification on the VAT implications of all industry transactions, there are some uncertainties in the appropriate VAT treatment of quite a number of Telco transactions. While most of these business arrangements with "unclear" VAT treatments are between resident and non-resident Telcos, others relate to the recoverability of input VAT from output VAT.

Few of these transactions are discussed below:

VAT on transactions between Telcos registered in Nigeria and Non-Resident Companies (NRC)

Action 1 of the Base Erosion and Profit Shifting Project ('BEPS Project') of the Organization for Economic Co-operation and Development ('OECD'), calls for the need to address the tax challenges of the digital economy – both direct and indirect taxes. In particular, the OECD recognizes that digital economy creates challenges for the collection of value added tax, especially where the services and intangibles are provided by non-resident companies ('NRCs').

By design, VAT is structured as a tax on the final consumption of goods and services. However, the tax is collected from the suppliers of such goods and services, rather than

directly from the consumers who ultimately bear the burden of the tax, as part of the market price of the goods purchased or services enjoyed.

The VAT Act in Nigeria provides that any NRC that carries on business in Nigeria should register with the FIRS and may appoint a representative for the purpose of its VAT obligations. The VAT Act also prescribes that such NRC should include VAT on its invoices, and stipulates that the local recipient of the supply of the goods or services or such other person as may be appointed by FIRS should remit the VAT in the currency of the transaction, to the FIRS.

The determination of what constitutes "a supply in Nigeria" was an area of controversy between taxpayers and the FIRS until amendments to VATA by Finance Acts 2019 and 2020 that now elaborate what constitutes taxable supply in Nigeria.

The above notwithstanding, the applicability of the two principles below are still relevant in determining VAT on NRC contracts:

1. Origination Principle; and
2. Destination Principle.

The origination principle stipulates that the supply of service should be subjected to VAT in the jurisdiction where a supplier is resident, whether the beneficiary is a foreign customer, or a local entity.

The destination principle invests VAT taxing rights in the taxing authority of the jurisdiction where the customer is tax resident. Essentially, the focus is on the tax jurisdiction where the customer is resident. Consequently, the supply is free of VAT (exempt or zero-rated) in the jurisdiction of the supplier, and is subjected to VAT in the jurisdiction of the customer. The supplier is therefore required to register (depending also on the local VAT rule) in the customer's jurisdiction, collect and remit the tax there.

Generally, the destination principle is often regarded as the international norm, from both the theoretical and practical standpoints. This is because VAT is levied on consumption, and should be borne by the ultimate consumer.

The destination principle aligns with the provisions of the VAT Act as amended by the Finance Acts.

In Nigeria, when the customer is a VAT-registered business, the VAT is often collected through a "reverse charge" mechanism – a tax mechanism that shifts the liability to pay the tax from the supplier to the customer. That is, the customer withholds the VAT due on the invoice of the supplier, and directly remits the VAT to the FIRS.

On the basis of the foregoing, the expectation is that a NRC in Nigeria should include VAT in its invoice, while the Telco should deduct the VAT and remit same to the FIRS, in the currency of transaction.

Where the non-resident companies make use of satellite to render their services to a Telco in Nigeria

The supply of satellite network bandwidth capacities, regardless of the location of the satellite, will be liable to VAT. This principle was clarified in the court judgment between FIRS v. Vodacom (Appeal No. FHC/L/4A/2016). Further, amendment based on Finance Act 2020 has clarified that services rendered outside Nigeria is liable to VAT provided the service is provided to and consumed by a person in Nigeria.

Deductibility of Input VAT and restrictions

The VAT Act provides that only "allowable input" may be recovered against output VAT. 'Allowable input VAT' is defined in Section 17(1) of the VAT Act, as *'tax on goods purchased or imported directly for resale and goods which form the stock-in-trade used for the direct production of any new product on which the output tax is charged"*. The input VAT paid on services, administrative and overhead costs should be expended through the income statement. In addition, the VAT Act also requires that input VAT on any asset acquired be capitalized together with the cost of the asset.

The wording of the law cannot be separated from the apparently expressed intent of the legislature throughout the VAT Act. Overall, the VAT Act prescribes that VAT should be collected through a multi staged process. Entities within the supply chain are required to charge VAT on the value added element in the process. Consequently, the tax payable to the FIRS should be the difference between the VAT imposed on the final output (output tax) and the VAT incurred on input for the same period (input VAT).

In order to complete a voice call between networks (i.e. interconnect calls which are initiated on one network and terminated on another), operators are required by the NCC Act and the NCC, to co-venture and leverage their respective platforms, and third parties. The revenue accruing to a telco on the sale of pre-paid vouchers (used to complete interconnect calls) accrues proportionately to each operator that performed a role in completing an interconnect call. That is, for an operator to complete a call, it requires the service of another operation (via interconnect) to compete such calls.

Going by the strict wording of the VAT Act, telecommunication companies should not be able to claim input VAT paid on services rendered to them, as a relief on the VAT they pay (output VAT). However, the uniqueness of the telecommunications industry has made it necessary for companies within the industry to leverage the 'input VAT' mechanism in recovering VAT overpayments made by operators to the FIRS in respect of pre-paid vouchers. It is reasonable to conclude that for a call service rendered by a telco (on which output VAT in charged), it requires the input from an interconnect provider, which would

have charged VAT (input VAT). Therefore, a reasonable argument can be made that the input VAT incurred by the Telcos should be an allowable one for the purpose of rending the output VAT. In practice, the FIRS accepts this arrangement. However, it is not strictly supported by law and the FIRS may repudiate its position without notice to the Telcos.

In other tax jurisdictions, a similar position is adopted. A form of synergy is required when completing a call, where the person making the call and the receiver use different operators. The revenue earned from such service provided to the customer is "deemed shared" through an agreed settlement/invoicing arrangement. By extension, the obligation to account for VAT should fall on each operator in proportion to their share of revenue. Nonetheless, the primary operator (i.e. the party that sold the pre-paid voucher) accounts for the VAT on behalf of itself and the co-venturers, and then recovers the 'VAT overpayment' from the tax authority by leveraging the 'input VAT' mechanism i.e. by setting off the VAT paid on interconnect charges against the VAT collected on the sale of pre-paid vouchers. In these jurisdictions, the principle is generally applicable in the telecommunications industry and the tax authorities have accepted the practice.

6. Decision in the case of Vodacom vs FIRS

The taxation of services supplied by NRCs to Nigerian companies has been an issue of great debate in recent times. By its ruling of 24 June 2019, the Court of Appeal held, in the case between Vodacom Business Nigeria Limited (Vodacom) v FIRS that the supply of satellite bandwidth capacities from an NRC to Vodacom (a Nigerian based company) is subject to VAT in Nigeria. Based on the facts of the case, the Court of Appeal in the case was correct to have subjected supply of bandwidth capacities to Vodacom to VAT. However, the rationale used by the Court to then attempt (as it seemed to do), to assert that all imported services are liable to VAT in Nigeria, appears to be at variance with the express provisions of the VAT Act, which requires that imported services be supplied in Nigeria before VAT liability can arise.
In the Vodacom decision, the transaction qualified as a VATable supply under the VAT Act because Vodacom had received the bandwidth capacities with equipment located in Nigeria. Although and sadly so, the Court of Appeal in reaching this decision had jettisoned the distinction between the location of supply of a service and the location of receipt of such service and inadvertently interpreted the supply of a service and the receipt of a service to mean the same thing in determining the VATability of a transaction.

Therefore, following the Court of Appeal's decision, a number of stakeholders have taken a view that the decision has expanded the scope of the VAT liability of Nigerian resident companies to include all forms of services rendered by NRCs whether or not such services are physically supplied in Nigeria (by employees or via some form of equipment located in Nigeria).

The Court of Appeal held that Vodacom was liable to self-assess and remit VAT on the said transaction. In giving its decision, the Court of Appeal recognized the fact that although the satellite network was in the orbit, the bandwith was received in Nigeria through Vodacom's

transponders. Thus, the service was rendered in Nigeria and liable to Nigerian VAT.

7. Challenges facing application of VAT in the telecommunication industry

There are several challenges operators in the telecommunication industry face regarding the application of VAT on their purchases and supplies. Some of the major challenges are as follows:

Non-deductibility of input VAT

The non-recoverability of VAT incurred via the input-output mechanism is a major issue affecting profitability in the telecommunication industry. According to NBS, the service industry, including the telecommunication industry, accounts for over 50% of Nigeria's rebased GDP. Given the strict conditions for offsetting input VAT against output VAT, companies in the service industry are not able to recover the whole input VAT incurred on their purchases. This is regardless of the fact that VAT is incurred on cost of service that forms part of the direct cost of the companies. This impacts the cash-flow of these companies negatively.

Recognition of VAT on interconnect charges

Some operators in the telecommunication industry usually pay interconnect charges to other service providers/operators for using their networks to complete calls that originate from their networks but terminate in such other networks. These charges are usually inclusive of VAT. In practice, the operators prefer to offset the VAT incurred on interconnect charges from output VAT charged to their customers for services provided.

FIRS, in contrast, usually frowns at this practice and demands the full VAT on revenue earned from the customer, while insisting that the VAT incurred on interconnect charges be charged/expensed to/in the statement of comprehensive income.

Accounting for VAT - accrual or cash basis?

In the telecommunication industry, operators such as the mobile service providers, receive cash from prepaid customers before recognising or earning revenue. The unearned portion of the cash receipts is regarded as deferred revenue (or unearned income) and reported as liability in the books of the companies.

Prior to amendment by Finance Act 2019, it may be argued that VAT is due on prepaid revenue/cash receipt since VAT is invoice based. This position is supported by the FIRS due to its preference that companies should account for VAT on cash basis rather than accrual basis preferred by the Industry. However, for infrastructure and platform providers in the telecommunication industry, FIRS prefer such companies to account for VAT on an accrual basis. This is because revenue is usually earned by the companies before cash is collected.

The above notwithstanding, it is worthy of note that the controversy has now been addressed by the Finance Act 2019. Section 15 (1) of the VAT Act clearly states that:

"A taxable person who in the course of a business has made taxable supplies or expects to make taxable supplies, the value of which, either singularly or cumulatively in any calendar year, is ₦25,000,000 or more; shall render to the service, on or before the 21st day of every month in which this threshold is achieved and on or before the same day in successive months thereafter, are turn of the input tax paid and output ***tax collected*** *by him in the preceding month in such a manner as the Service may from time to time prescribe."*

This amendment supports the fact that all taxpayers (including those in telecommunication industry) should account for VAT on cash basis. Therefore, this clarifies the controversy on the accrual vs cash basis method of determining VAT liability.

8. Conclusion

The issues identified above are proofs that there is a wide gap between current business realities and the provisions of VAT Act. While businesses have continued to evolve, the tax laws have not been sufficiently amended to address the new business exigencies and realities despite the amendments introduced by the Finance Acts 2019 and 2020.

9. Recommendations

Considering the peculiarities of the telecommunication industry, the companies operating in it should constantly engage with the FIRS to obtain clarity on areas which the tax laws do not provide adequate clarity on.

There is also the need for our tax laws to recognize the evolving digital economy, and to be amended to reflect current realities. Note that despite a low VAT rate of 7.5%, and year on year amendments since 2019, the VAT system and VAT Act still do not reflect business realities. The VAT Act, in its current form, is unable to capture the evolution in the operations and business models of companies, including operators in the telecommunications industry. Telcos can leverage the now annual Finance Act process to propose amendments to the tax laws that put the telecommunication industry in a disadvantaged position.

Further, one of the principle of a good tax system is fairness and equity. It was on this backdrop, amongst others, that the National Tax Policy was developed and subsequently revised by the Federal Government of Nigeria in 2017. The discriminatory provision in VAT Act as it affects the claim of input VAT in service industries has created a lot of controversies. The service industries must be given the opportunity to claim input VAT in the same manner as companies operating in the trading and manufacturing sectors. Several countries of the world, such as the United Kingdom, South Africa and even Ghana, allows full recoverability of input VAT from output VAT.

Finally, tax officials are encouraged to adequately familiarize themselves with both the strict wording and intention of the law, as well as the uniqueness of various industries.

The telecommunication industry has been and remains one of the symbols of successful policy implementation stories of the Federal Government of Nigeria in the last decade. Therefore, to the extent that the Industry continues to be at the frontier of major economic initiatives of the government at various levels, friendlier tax practices can only help to enhance productivity and investment in the Industry and the Nigerian economy at large.

ENDNOTES

1. Nigerian Gross Domestic – Product Report (Q3 2020)
2. As amended by Finance Act 2019 and Finance Act 2020

CHAPTER 14

VALUE ADDED TAX ON FINANCIAL SERVICES

Abstract

In many of the jurisdictions with a VAT system, most financial services are exempt from VAT due to the difficulty in identifying and measuring for tax purposes, the value added in a financial intermediary's margin on a transaction-by-transaction basis. This approach however, gives rise to significant difficulties. To mitigate the difficulties associated with the exemption method, alternative methods of application of VAT on financial services have been proposed. This chapter examines the legal and regulatory framework for application of VAT on financial services in Nigeria and the treatment adopted in a few other jurisdictions in comparison. It also looks at some of the problems associated with the exemption method and the alternative methods for application of VAT on financial services.

1. Introduction

The basic principle underlying a Value Added Tax (VAT) system is that the tax should apply to any fee paid as a consideration for a supply. However, where financial services are concerned, distinguishing the several components of financial transactions is generally seen as administratively complex and costly as financial transactions incorporate several types of financial flows, which may be difficult to evaluate for VAT purposes.

Added to this is the rapid development in the range of financial services and instruments offered by financial institutions. These instruments, across the financial value chain, take so many different forms that it may be difficult to develop VAT rules to clearly identify the value of the services rendered to each party to an instrument that should be included in the VAT base. Movement of money, internet banking and global business have added to the complexity of international financial services. As a result, many jurisdictions simply exempt financial supplies from VAT while some others apply zero rating on the services due to the problem of lack of recoverability for exempt transactions.

This chapter examines the legal and regulatory framework for application of VAT on financial services in Nigeria and the issues associated with the current treatment. In this regard, the chapter also looks at international practices highlighting the treatment adopted in a few other jurisdictions in comparison and the alternative approaches to the current treatment.

2. Nature of financial services

Financial services include a large variety of services including bank deposits and loans, life and general insurance, financial advisory, agency and brokerage services, asset management to mention a few. On a broad level, financial services can be categorized either by the type of services e.g. banking services, insurance services, brokerage and other agent services, advisory, asset management etc. or by the type of service provider e.g. bank or insurance company.

3. VAT on financial services in Nigeria

Legal Framework

The Value Added Tax Act[1] (as amended)provides the legal framework for application of VAT on taxable goods and services. In addition, the Federal Inland Revenue Service (FIRS) had published a number of Information Circulars on VAT, which to some extent throw light on some of the provisions. It should however be noted that the FIRS Circulars or Information Notices are not legal documents and are merely issued for the guidance of taxpayers. They are neither binding on nor create estoppel against the FIRS.

Meaning of Financial institutions

The VAT Act contains very limited provisions regarding financial services. Specifically, other than the exemption of services rendered by microfinance banks, peoples bank (now defunct) and mortgage institutions from VAT, the Act makes no further mention of financial institutions and their services. However, the FIRS Circular on "Value Added Tax (VAT)on the Services of Financial Institutions" provides some clarification as to which entities that qualify as financial institutions and application of VAT on their services[2].

The Circular states that financial institutions means any bank, individual, body, association or group of persons, whether corporate or unincorporated, licensed under Banks and Other Financial Institutions Act (BOFIA) and any other related Act which carries on the business of a discount house, finance company, money brokerage and those whose principal objects include factoring, project financing, equipment leasing, debt administration, fund management, private ledger services, investment management, local purchases, order financing, export finance, project consultancy, financial consultancy, pension fund management and such other business as the Central Bank of Nigeria, Nigeria Deposit Insurance Corporation, Pension Commission and other regulatory body may, from time to time, designate.

The Circular further clarifies that Financial institutions include but not limited to banks, insurance companies, pension fund administrators, discount houses, brokerage firms etc.

Taxable financial services

Pursuant to section 2 of the VAT Act, VAT is chargeable on the supply of all goods and services (referred to in the Act as "taxable goods and services") other than those goods and

services listed in the First Schedule to the Act. Part 2 of the First Schedule to the Act only exempts services rendered by microfinance banks, peoples bank and mortgage institutions from VAT. Accordingly, all other banking and financial institutions are required to charge VAT on taxable services rendered by them to their customers and account for same to the FIRS.

According to the FIRS Circular, in determining what constitutes VATable financial services, a distinction should be made between activities that constitute return on investment and consumption of services rendered by financial institutions. All charges arising from the services of banks and financial institutions will ordinarily attract VAT and they include among others, the followings:

a. Commissions charged on forex trading or remittance;
b. Commissions on sale of Bank drafts/certified cheques;
c. Commissions paid to brokers, reinsurers, underwriters and other insurance agents by an insurer
d. Commission on asset trading;
e. Account Maintenance Fees, ledger fees etc.;
f. Legal and other fees chargeable on lease arrangements;
g. Fees charged for advisory services e.g. mergers and acquisition, financial strategy counseling etc.;
h. Fees chargeable on public/private issues;
I. Debt conversion fees;
j. Fees on asset trading;
k. Fees earned on fund management;
l. Fees earned on letters of credit/documentary collection to finance import/export;
m. Fees chargeable on stock-brokerage and trust services;
n. Fees charged on electronic banking, POS and ATM charges;
o. Fees charged on electronic bill payments;
p. Mobile money transactions and other like transactions;

In contrast, services of banks and other financial institutions, which constitute return on investment or consideration for risk are not regarded as consumption of services for VAT purposes. Thus, the charges payable on such services do not attract VAT and they include:

a. Interest on loans and advances, including overdraft facilities;
b. Interest on savings accounts;
c. Interest on bank deposits;
d. Interest on interbank placements;
e. Premium on insurance policies;
f. Dividends; and
g. Profit or gain on disposal of securities.

The VAT Act stipulates that where input tax exceeds output tax, the taxpayer will be entitled to refund of the excess tax from the FIRS on production of such documents as the FIRS may, from time-to-time require[5]. However, Section 17 of the Act limits this ability to recover input tax only to input tax incurred on goods purchased or imported directly for resale or goods used for direct production of other goods on which output VAT is chargeable[6]. The Act further stipulates that input tax on any overhead, service, and general administration of any business should be expended through the income statement (profit and loss accounts). To this effect, this input VAT is not allowed as a deduction from output tax. Thus, for taxable financial services, banks and other financial institutions are not allowed to deduct the input VAT incurred on their purchases of goods and services from the output VAT chargeable on the taxable supplies.

The FIRS in the Circular provides that Input tax claimable by financial institutions shall be in accordance with the provision of Section 17 of the VAT Act. In this regard, it clarifies that input VAT incurred on purchases of fixed assets are to be capitalized along with the cost of the assets while input VAT incurred on services are to be expensed in the Statement of Profit or Loss Account.

In line with Section 17 of the VAT Act, the Circular further clarifies that where financial institutions suffer input VAT on goods supplied to customers, such input VATis allowable against the output VAT on those goods.

While the primary obligation to charge and remit the VAT on services falls on the person providing the service, with regard to financial institutions, the Circular outlines certain instances where this obligation may shift as follows:

a. In case of agency or broker arrangements where they act as intermediaries between the service providers and the customers, the obligation to charge and remit VAT shall be that of the agent or broker;
b. Where the agent or broker cannot charge VAT due to being either individuals (including staff of the financial institution), or being a person below the VAT threshold, the financial institution has the obligation to self-account and remit same to the Service; and
c. Where the agent or broker fails to charge VAT, it shall be the obligation of the financial institution to self-account and remit the VAT to the Service.

Where the broker or agent fails to charge and collect or charges and collects but fails to remit the tax, the penalties prescribed in the relevant tax laws shall apply.

4. International practice

The exemption approach

The European Union (EU) and most other countries following a VAT model based on the EU approach, exempt most financial services (banking, insurance and other financial services)

from VAT, in part because of the difficulty fitting intermediation services within a transaction-based, credit-invoice VAT system. There is an extensive body of literature examining the taxation of financial services under a VAT, the rationale for the exemption, issues and challenges with exemption, the deviations from that model in some countries, and proposals for change. This chapter draws on some of the literature[7].

When a financial institution charges explicit fees or commission for its services, the value of those services is the fees or commission charged which fits into the standard credit invoice method of calculating VAT (the most commonly used method) as the fee provides the base for application of the VAT. A Financial institution however, renders the bulk of its services as an intermediary example in bringing together depositors and borrowers for which the compensation is in the form of a financial margin and this is where the problem lies. Other margin-based services provided by financial institutions include foreign exchange transactions, trading in shares, bonds, derivatives and other instruments. This chapter uses banking institutions for illustration purposes.

In rendering financial intermediation services, banks for instance add value in several ways such as pooling of savings from savers to make loans to borrowers, pooling of risks, managing loans and deposits etc. These activities add value by reducing the costs of transactions. Measuring this value added is however not straight forward mainly due to the fact that in many cases, banks do not charge explicit fee for these services but rather earn compensation in the form of a margin or spread. That is, the charges for these services are buried in interest rates and other financial margins

The value of these intermediation services is implicit in the margin between the interest charged on loans (on borrowers) and interest paid for borrowed funds (to depositors), or for instance in the margin between the buying and selling rates for a foreign currency.

In arriving at the margin, the value added is only one out of the several elements taken into consideration. The financial flows that will typically arise among the parties to the transaction i.e. the depositor , the borrower and the intermediary (i.e. the bank) will include transfers of funds (capital) from savers (depositors) to the borrowers, pure (or risk free) interest charge, a risk premium to adjust for losses and the intermediation services of the financial institution. Of the various flows or elements, the financial intermediation is considered to be the only element in the financial margin that gives rise to value added and should be the only element subject to VAT. Other components of the margin, which represent mere transfers or return on investment should not be included in the tax base.

However, the charge for this intermediation is in reality often mingled together with the other flows among the parties. In most cases, it is difficult if not impossible to separately identify the actual margin associated with financial intermediation from the other flows or elements that are included when determining the rate of interest or margin on a transaction-by-transaction basis. In effect, since the value-added services are provided to both savers and

borrowers, allocating the value-added charge to one or the other i.e., on a transaction-by-transaction basis is not straight forward.

Similar issues arise in the taxation of insurance and other types of financial intermediation services example currency exchange and trading in securities.

The inability to find a satisfactory measure of taxation of implicit financial intermediation fees has led most countries with a VAT regime to exempt financial services where fees for the intermediation services are wholly or partially hidden within financial margins or spread.

Issues with the exemption system

The exemption system necessitated by the practical difficulties in measuring the consideration for financial services is not itself without problems. Under the exemption system, no tax is paid on the goods and services exempt from VAT while at the same time, no input credit is allowed for the tax paid on the inputs acquired for use in providing the exempt supplies. Thus, while financial institutions pay input tax on inputs used in rendering financial services, they cannot claim input tax credits on the exempt services.

The blockage of input VAT under the system gives rise to a number of problems including the following[8]:

i. Definition and interpretation complexities

Definition of what constitutes financial services is key for the operation of the exemption system. However, the various provisions in the VAT legislation or rules which outline the VAT treatment of financial services are often subjected to different interpretation and application making it difficult to define the scope of exemption. A contributory factor to this problem is the rapid changes in the financial services sector including significant developments in new finance products, the emergence of new supply structures and rise of the internet as a medium for financial transactions. To this end, it has become increasing difficult to determine whether these new products and new supply structures fall within the scope of the exemption.

Thus, given the variety and complexity of financial transactions and the provision of mixed supplies, the dividing line between exempt and taxable financial supplies is often blurred resulting in difficulties in determining whether or not a service falls within the exemption. This has given rise to litigation in many jurisdictions. For instance, in the EU, this has resulted in a significant amount of litigation both at the level of the Court of Justice of the European Union (CJEU) as well as within the member states. The CJEU has been frequently asked to clarify the correct interpretation[9]. The time and effort spent in determining the scope of the exemption and the correct VAT treatment increases administrative and compliance costs.

ii. Economic distortion

Exemption results in a break in the VAT chain and distorts competition in several ways including the following:

- The under-taxation of the household consumption of exempt financial services compared with the consumption of other goods and services which are subject to VAT.
- Tax cascading arising from the over-taxation of the consumption of financial services by business user of the services. In the case of business to business transactions (B2B transactions), the exempted financial services serve as intermediate input in the production and distribution process. As there is no output VAT on the exempted financial services, the non-deductible input VAT paid by the financial institution, gets embedded in the cost of the supply to the business customer. This cost in turn gets embedded in the price of the product supplied by the business customer to the final consumers.

In essence, where the unrecoverable input tax is passed on to business users of financial services, they too will pass on the hidden VAT in the prices of goods and services sold to their customers. In the case of taxable supplies, the VAT will also be applied on a price which already includes the hidden VAT resulting in tax cascading. The prices of goods and services sold to final consumers would reflect not only the tax applicable at the point of final sale, but also the embedded, non-creditable input taxes. In effect, goods and services which include financial services as inputs are more heavily taxed than other goods and services.

- Bias for self-supply: Creates an incentive for a financial service provider to self-supply services by using in-house services rather than purchase these inputs from external suppliers or obtain tax free services from foreign suppliers in order to avoid some or all of the unrecoverable VAT on purchases from registered domestic suppliers.

- Advantage to offshore suppliers: It creates competitive advantage to offshore financial service providers where they render services to domestic purchasers free of VAT or at a reduced rate. Given the globalization of business today and the ever-increasing ability to provide services from remote locations through telebanking and internet banking, there is growing concern in jurisdictions which exempt financial services from VAT that customers would prefer to obtain services from financial institutions based in countries with no VAT regime or those with a VAT regime which zero rates international supplies of financial services. This will make the domestic suppliers of similar services less competitive as their pricing structure will include VAT.

- Loss of revenue: Exemption may create loss of revenue for government. As the financial services sector is considered to be of high importance in most countries accounting for a significant portion of government revenue from tax, revenue loss could be significant.

iii. Allocation and apportionment of input credits

In situations of mixed supplies, i.e., where the supplies consist of both exempt and taxable or zero-rated activities which would mostly likely be the case for most financial institutions,

allocation and calculation of VAT on the taxable activities is often problematic and costly. There will be compliance costs associated with apportioning VAT between taxable and exempt supplies. In order to carry out the allocations, financial institutions may need to collect information and modify accounting systems that would not otherwise be required. This has given rise to considerable case law in the EU.

iv. Treatment of financial institutions as final consumers

By denying financial institutions the ability to recover VAT on the inputs used in making exempt supplies, they are in effect treated as the final consumers in respect of these activities. The treatment of financial institutions as final consumers is considered to be contrary to the principle of VAT as a tax on consumption and the supply chain neutrality of the tax as the goods and services supplied to these institutions will invariably be used as inputs to the services they supply.

Despite the many problems associated with the exemption system, most of the countries with a VAT regime continue to exempt at least some financial and insurance services under their VAT regimes as it is considered to be too difficult to effectively tax the value of those services on a transaction-by-transaction basis and provide business users of those services an input credit for the tax imposed.

Modified Exemption System

Confronted with the problems associated with the EU exemption method, some countries with newer VAT regimes have adopted modifications to the approach[10]. They include:

Taxation of fee based financial services (Narrower exemption)

Exemption of both explicit fees and margins is the approach adopted under the EU's VAT Directive which has a wide exemption for financial services applying to virtually all banking and insurance services and a wide range of asset management services. However, other VAT systems introduced after the EU system e.g. in Australia, Singapore and New Zealand, are more restrictive and have a structure where intermediary services which are rendered for an explicit consideration are taxable. Also, general insurance services are liable to VAT, while life insurance remains exempt from tax.

Theoretically, taxation of explicit fees and agency services increase the coverage of taxation of financial services and should reduce tax cascading and other distortions. This would be the case where the explicit fees account for a significant portion of total revenues of financial institutions in which case, the quantum of blocked input taxes would be reduced significantly. However, in reality, deposit and lending transactions of banks on which they derive interest margin constitute the bulk of their total revenues and the exemption system remains in place for these revenues. This is the main drawback of this approach as the greater portion of the total revenues earned by financial institutions do not come from explicit fees. Thus, it does not really address the problem of tax cascading and other problems associated with the exemption system.

Option to tax

Option to treat otherwise exempt financial services as taxable provides a mechanism for the removal of tax cascading. The option approach already exists within the EU system although it is not widely used. The EU VAT Directive allows member states to introduce an option to tax for financial services. Under the optional clause, member states are given the discretion to allow financial institutions a right of option for taxation in respect of certain financial transactions[11]**.**The option however excludes insurance transactions.

The use of the option system has however been limited in the EU with only a few member states applying it namely: Austria, Belgium, Estonia, France, Germany, and Lithuania. The reluctance of the member states to apply the option system has been attributed to the lack of guidance and vagueness of the option clause.

Part of the European Commission's (EU's) proposal to reform the EU's VAT regime include an extension of the Option to Tax System to make it compulsory for member states to introduce the option and discretionary for financial institutions to opt for taxation or exemption and extend the coverage to all exempt financial institutions including insurance.

The expectation is that an extended option to tax would address some of the economic distortions arising from the VAT exemption for financial services.

Zero rating business to business (B2B) supplies of some financial services:

Under zero-rating, no tax is charged on the supply of financial services to business customers, but the financial service provider is allowed to recover input tax credits related to the supply. This means that VAT would be applied on transactions between financial institutions and registered businesses and the financial institutions would be able to claim input tax credits on inputs used in providing the financial services to businesses. This will eliminate the irrecoverable input tax on the inputs used in the production of the financial services as well as on the financial services purchased by business customers.

Zero rating B2B financial services is generally regarded as the most effective method of reducing blocked input VAT and the tax cascading that otherwise occurs under the exemption method. There are however some disadvantages which include: compliance costs and administrative burden that will be borne by financial institutions in identifying and distinguishing between supplies to business customers and non-business customers (final consumers). Zero rating B2B transactions does not eliminate the need to allocate input VAT between taxable and exempt transactions. Also, loss of government revenue among others.

Countries that have adopted zero rating include New Zealand, Singapore and Quebec, Canada.

Compensatory taxes

Compensatory taxes are applied to recover revenue lost as a result of the exemption or zero

rating of financial services. These include payroll and profit taxes on financial institutions and insurance premium taxes. The countries that have introduced compensatory taxes include France in the form of a payroll tax, Israel as an addition-Method VAT, and the province of Quebec in Canada as supplementary taxes on labour and capital.

Partial recovery of the blocked input tax.

The major source of distortion under the exemption system is the blockage of input taxes on exempt financial services rendered to businesses. The problem is mitigated somewhat through the taxation of explicit fees and commission. Some jurisdictions have introduced other measures to further reduce the quantum of blocked input taxes including zero-rating of selected or all financial services or reduced taxation of inputs. For instance, under the Australian Goods and Services Tax (GST), introduced in 2000, although financial services are still exempt, the regime provides for a 'reduced input tax credit' system under which financial service providers can claim credit for the GST attributable to exempt supplies. This reduces the incentive to self-supply services and also reduces the competitive distortions between domestic and foreign suppliers of services to banks. Other jurisdictions that have adopted similar measures include Singapore and New Zealand.

5. Some specific country practices

European Approach

Under the EU VAT regime, most financial services are exempt from VAT. The scope of the exemption for financial services in the EU countries is set out in the Council Directive 2006/112/EC on VAT. Under Article 135 (1) of the Directive, most banking services as well as insurance and other financial services are exempt from VAT with no right of input deduction. Under Article 168 of the Directive, VAT paid on input transactions will only be deductible where the goods and services are used in making taxable transactions by a taxable person.

Thus, whereas financial institutions do not charge VAT on most of their output, they cannot deduct the VAT charged on their inputs. This is commonly referred to the “irrecoverable VAT problem”. There is however an exception to the rule where the customer is established outside the Community, or where the financial transactions relate directly to goods to be exported out of the Community, in these cases the taxable person will be entitled to deduct any related input VAT under article 169 of the Directive. This exclusion from the right to deduct input VAT means in practice that financial suppliers will have significant amounts of non-recoverable VAT, resulting in considerable tax costs.

The VAT Directive however permits member countries to allow financial institutions an option to treat financial services as taxable supplies. The option is granted due to the denial of deduction of input taxes to financial institutions in respect of their exempt services which leads to a number of difficulties some of which are highlighted in this chapter.

Review of the exemption approach

The Council of the EU recognizing that the VAT exemption for financial and insurance services under the VAT Directive was out of date, carried out a number of research studies into possible methods of taxing financial services including insurance under a VAT system. Majority of the studies identified the cash flow method and its variants as potential alternative methods which are discussed later in the chapter.

In 2010, the EC published Taxation Papers on Financial Sector Taxation. The Papers considered two potential tax instruments for taxation of the financial sector namely: the Financial Transaction Tax (FTT) and the Financial Activities Tax (FAT). The FTT focuses on the transactions executed in the financial markets such as trading in equity, bonds, derivatives, currencies, etc. while the FAT seeks to target the value added by the financial sector. The FAT is in essence a tax on the sum of profit and remuneration of financial institutions. The tax is seen as having the features of being a good substitute or proxy for VAT. Some countries are already applying some variants of the FAT which are discussed further under "Alternatives to Exemption" in this chapter.

The EC also published a Communication for the Taxation of the Financial Sector in October 2010 which recommended an EU-wide FAT over an EU-wide FTT. Despite the recommendation for an EU-wide FAT in the 2010 Communication, the EC further initiated an impact assessment which analyzed the FTT and FAT and concluded that an FTT was the preferred option. In September 2011, it published its initial proposal for a Council Directive on a common system of Financial Transaction Tax in the 27 Member States of the EU[13]**.**The proposal did not receive the required unanimous support within the Council but a number of Member States expressed a strong willingness to go ahead with the FTT. Under the EU Treaty, enhanced cooperation allows a number of Member States (a minimum of nine) to advance on specific policy issues based on the authorization of the Council of the EU. In 2012, the Commission received requests to establish enhanced cooperation in the area of FTT from a group of 11 Member States (Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia, and the Slovak Republic), based on the scope and objectives of the Commission's initial proposal.

In 2013, the Commission adopted the Proposal for a Council Directive implementing enhanced cooperation in the area of FTT together in the participating Member states **13a.**To date, the EU is yet to reach a consensus on the adoption of the FTT in the member states. The FTT is not discussed further in this chapter since it is not essentially based on value added.

The question of VAT exemption (and of the related tax advantage that the financial sector is deemed to enjoy in comparison with other sectors of the economy) remains a discussion point within the EU.

Singapore

Under the Singapore Goods and Services Tax Act, financial services are exempt from VAT[14]. However, agency services relating to arranging, broking, underwriting or advising on financial activities are excluded from the exemption. Therefore, any consideration earned for any agency service would be liable to VAT in Singapore. This approach in effect narrows the scope of exempt financial services. However, the consideration earned for such agency services may be zero rated when they are provided to overseas customers.

To counter the effects of tax cascading and self-supply bias, Singapore allows financial institutions to claim input tax credits under the "fixed input tax recovery method." Under this method, a financial institution can claim a credit for a fixed percentage of total input taxes. The recovery percentages are differentiated according to the type of financial institutions and reflect the mix of their business and non-business customers. The recovery percentages are generally based on the share of services estimated to be provided to VAT registered customers and overseas customers. The percentages are reviewed on a yearly basis.

New Zealand

New Zealand after exempting many financial services for many years, revised the exemption system effectively from 2005 to allow, on an elective basis, zero rating of supplies to taxable customers. Under the current regime, a New Zealand financial institution, can electto treat exempt financial services as zero rated supplies if the service recipient is registered for GST; and 75% or more of the supplies by the service recipient in a given 12-month period are taxable supplies. If the recipient of the financial services is a member of a group, the level of taxable supplies made by the group must exceed 75% of the group's total supplies in a given 12-month period.

Under a special rule, financial services provided to another financial services company may be zero rated to the extent that the second company supplies financial services that are zero rated[15].Supplies of financial services to consumers and non-qualified businesses, remain exempt. Like the rule in most other countries, New Zealand disallows tax on business inputs used in rendering exempt services.

South Africa

South Africa enacted its VAT in 1991and initially exempted most domestic financial services and zero-rated exported financial services[16]. Starting in 1996, it expanded the scope of taxable financial services to include explicit charges for all fee-based financial services rendered domestically. Financial intermediation services for which there are no specific charges remain exempt from tax. Under the South African VAT legislation, the definition of 'financial service' stipulates that where the consideration is any fee, commission, merchant's discount or similar charge, the activities would not be deemed to be a financial service.

The South African Revenue Service (SARS) worked with the banking industry to agree on the tax status of a list of banking services in 1996[17]. The document updated in 2006,

classifies each of the listed services as taxable, zero-rated, or exempt from VAT[18]. This approach had added a measure of certainty both for SARS and the banks.

Nonetheless, despite the 1996 agreement on the tax status of various banking services, the banks and SARS continued to have disputes over the appropriate allocation of input tax between taxable and exempt supplies. In 2003, SARS, in an effort to reduce the areas of dispute, developed a standardized method of apportioning tax on business inputs between taxable and exempt banking services[19].The South African model has been adopted by some of the neighboring African countries, such as Namibia and Botswana

Ghana

Ghana implemented a new VAT law, Act 870 in 2015 which increased the standard VAT rate from 15% to 17.5% and imposed VAT on some financial services. With the introduction of Act 870, the scope of VAT was extended to cover all financial services rendered by banks for a fee, commission, or a similar charge except where they relate to life insurance and reinsurance. This means that life insurance, and reinsurance financial services do not attract VAT whether or not they are rendered for a fee, commission or similar charge.

Providers of fee based financial services (unless exempt) as a result, are required to register and charge VAT &National Health Insurance Scheme (NHIL) on the qualifying services. Under Act 870, banks are entitled to deduct input VAT & NHIL directly attributable to taxable financial services and other VAT & NHIL registered persons are entitled to deduct the VAT & NHIL charged by the banks on financial services, subject to the general VAT & NHIL deductibility rules.

However, in 2017, the government of Ghana abolished VAT on financial services as part of the relief package announced in the 2017 budget. The Ghana Parliament gave effect to this when it passed the VAT (Amendment) Act 2017 (Act 948) which included supply of financial services as an exempt supply.

Australia

Under the Australian Goods and Services Tax (GST) legislation, financial supplies are "input taxed". This means that suppliers of financial services are not allowed to claim tax credits for the purchased inputs used in making the exempt supplies[24]. The term "input taxation" refers to taxation of input rather than output.

Australia however, has two schemes under which a registered person making exempt financial services can claim credit for some or all of the GST attributable to the exempt services namely: the "Financial Acquisition Threshold" regime and the "Reduced Input Tax Credit" system.

Under the Financial Acquisition Threshold, acquisitions related to making financial supplies remain creditable if the entity does not exceed the financial acquisitions threshold. An entity

exceeds the financial acquisitions threshold if, in the current month and the preceding 11 months, or in the current month and the next 11 months, the GST on acquisitions related to financial supplies exceeds, or will exceed, either the lesser of AUD150,000 or 10% of the total input tax the entity incurs[25]. In calculating the amount of GST on financial acquisitions, financial acquisitions related to borrowings are excluded. Acquisitions related to borrowings that are not used to make input-taxed supplies remain creditable.

Under the Reduced Input Tax Credit (RITC) system, a registered financial service provider is allowed to use a "reduced credit acquisitions" system to claim credit for otherwise disallowed input tax credits. The GST Regulations specify the reduced credit acquisitions that give rise to an entitlement to a RITC. For each kind of reduced credit acquisition, the Regulations also specify a percentage to which the input tax credit is reduced. The maximum percentage a registered financial services provider can claim is currently set at 75% of the input tax.

With these measures, Australia substantially narrowed the definition of financial services, whether the services are rendered in business to business (B2B) or business to consumer (B2C) transactions, so more financial services exempt under other VAT regimes including fee-based financial services are taxable in Australia.

6. Alternative approaches to exemption

As already mentioned in this chapter, exemption of financial services from VAT raises a lot of issues and challenges. Aside from the modified exemption methods, various alternative methods have been proposed for taxation of financial services. The following is an overview of some of the more popular proposals for taxation of financial services.

The cash flow methods

Full taxation of financial services is seen as the best solution to alleviate the economic distortions which arise under the exemption method. One method identified in literature for application of VAT to financial services is the cash flow method discussed in more details below.

The cash-flow method has received considerable attention in literature both as an alternative form of a VAT and as a replacement for the corporate income tax. It was initially proposed in 1978 by the Institute for Fiscal Studies in London in a report, known as the 'Meade Commission Report'[26]mostly from the perspective of serving as a substitute for corporate income tax. Further work was however done on it as a component of a broad-based VAT system applying to both financial services and non-financial goods and services[27].

Basic cash flow method

The basic cash flow method treats cash flows from financial transactions in the same manner as flows from non-financial transactions. Under this method, cash inflows from financial transactions are treated as taxable sales (whether income or capital) on which a financial

institution would remit VAT to the government (e.g., a bank would remit VAT on receipt of a deposit), and cash outflows are treated as purchases of taxable inputs on which a financial institution would be entitled to a refund of VAT from the government (e.g., a bank could claim an input tax credit on withdrawal of a deposit).

An exception to this relates to share transactions in a company's own equity. In this regard, an issue of equity is not considered to give rise to a taxable inflow of funds and dividend payments do not give rise to input tax credits.

Under this approach, transactions with non-residents are zero-rated by applying the zero rate of tax to cash inflows and outflows from and to non-residents. All input tax credits related to commercial activities are now claimable, not just those related to non-financial supplies.

A number of benefits have been ascribed to the cash flow method such as:

- Compatibility with the credit-invoice system for non-financial services,
- Removal of tax cascading on financial services provided to businesses as it provides for claiming of input tax credits on financial transactions;
- It does not require input allocations between financial and non-financial activities.
- Does not require disaggregation of the financial margin into its components in order to identify the value-added.

  However, a number of draw backs have also been associated with the method including:
- Huge administrative and compliance costs, which businesses would have to bear on large volume of cash flows in order to calculate their deductible tax on inputs purchased from the financial institutions. Such costs would be especially burdensome for small and medium-sized enterprises.
- Since the principal amount of a loan would be subject to tax at the time the loan is made (which is not offset until repayment), the method could cause cash flow problems to borrowers as they may have to find financing for the tax in addition to the original loan requirements.
- It can also trigger significant transition problems upon implementation of the system and whenever the tax rate changes example if a deposit is received prior to implementation, no VAT would be remitted while if the deposit is withdrawn after the implementation date, VAT would be refunded even though it was not remitted when the deposit was received. Also, in the case of a tax change, the credit for the cash outflow should be at the same tax rate as that used on the original cash inflow. This will require an adjustment.

As a result of the draw backs, the basic cash flow method is generally deemed to be non-operational despite its many attractions. To alleviate the main difficulties associated with the basic cash flow method, a study initiated by the Commission of the European Communities developed two variants of the cash flow method, the cash-flow method with tax calculation account and the truncated cash-flow with tax calculation account[28]. Both variants are discussed below.

Cash Flow Method with Tax Calculation Account

The tax calculation account (TCA) operates as a tax suspension account under which tax payment by taxpayers and credits by government are suspended in the period cash inflows and outflows of a capital nature occur. Under this system, "tax that would otherwise be payable or creditable is instead debited or credited to the TCA and carried forward to the period during which the capital transaction is reversed example when a loan is repaid or deposit is withdrawn. However, these deferrals of tax are subject to interest charges at the government borrowing rate (referred to as the indexing rate or cost of funds rate). The basic features of this approach are briefly summarized as follows[29]:

- Tax payments on cash inflows related to financial instruments (whether an asset or a liability) are debited to the TCA
- Input tax credits on cash outflows related to a financial instrument are credited to the TCA
- The net balance in the TCA is subject to an indexing adjustment at the government borrowing rate
- A balance in the TCA is payable (or refundable, if negative amount) periodically, after subtracting a notional amount equal to the tax rate times the value of the financial instrument at the end of the period.

The TCA method would only apply to those activities on which a financial institution earns a consideration in the form of a margin. Other activities which attract explicit fee or commission are taxable in the same as non-financial activities.

The advantages of the system relative to the basic cash-flow system include:

- Elimination of cash-flow problems by deferring tax payments and credits on capital transfer;
- The benefit or loss from the deferral of tax or credit is offset by indexing of outstanding TCA balances by the government borrowing rate;
- Transition difficulties are addressed through initial debiting/crediting of the TCA at the commencement of the system and adjustment of the outstanding balance at the time of any change in the tax rate;
- Government is at little risk in respect of tax deferrals as tax payments on capital inflows are expected to be reversed by tax credits on capital outflows

There are however still some problems which include:

- The compliance burden associated with debit and credit entries in the TCA for each bank deposit and withdrawal, and applying the indexing adjustment would be considerable particularly on non-financial, and small and medium businesses.
- The method necessitates the choice of an indexing rate and when this rate falls outside the range of the deposit and lending rates, special rules may be required.
- The tax amount computed on a given transaction would reveal information on margins earned by financial institutions which could affect market competition and could also be misinterpreted

Truncated Cash-Flow Method with a TCA

The truncated cash-flow method with a TCA is a variant of the cash-flow method with TCA, which was developed to simplify compliance requirements for non-financial and small businesses, a major difficulty with the cash flow approach. Under this method, all the cash-flow computations would be carried out by financial institutions, thus relieving smaller businesses from large compliance costs with a periodic statement issued for the net tax credit claimable by business customers, thus truncating the calculations required under the other cash flow methods.

Under the truncated cash-flow method, VAT would be imposed on financial services provided for a fee or commission, on the profit margin on financial instruments acquired by a financial institution for the purpose of resale and on the interest spread on deposits and loans by financial institutions.

The final statements issued to the customer by the financial institution on the basis of TCA calculations operates as a tax invoice and serves the same purpose as a tax invoice for non-financial goods and services. Registered businesses eligible for the input tax credit could claim an input credit, if the services were acquired for use in a taxable activity.

The truncated cash-flow method with TCA was piloted on some selected European financial companies in Europe. Although the results of the study indicated that the TCA method was technically feasible and that it could allow full taxation of financial services, it was not implemented as concerns were raised regarding disclosure of proprietary information, application to complex financial instruments, and cost of implementation.

Portfolio TCA Method (with zero rating)

As a possible solution to some of the issues under the cash flow methods, Huizing a proposed a simplified TCA method which has been described as Portfolio TCA method[30]. Under the portfolio TCA method, transactions with VAT registered customers would be treated as zero rated, i.e., no tax would be charged on services supplied by financial institutions to business customers and no tax credit would be claimable by business customers.

Applying TCA method with zero-rating would solve the issue of disclosure of proprietary information, since no invoices would be sent to business customers. Furthermore, the approach decreases the compliance costs associated with TCA system, since the accounts related to business customers would be excluded from the system. That is, as the more complex financial products are primarily sold to business customers, the portfolio TCA method eliminates the need to calculate VAT on many of those products.

For transactions with non-registered customers, financial institutions would be allowed to make TCA calculations on an aggregated basis for portfolios of similar financial products, rather than on an account-by-account basis. It is however noted that under this method, financial institutions would still be required to separate their transactions with registered

customers from those with the final consumers, which is seen as an unnecessary administrative burden and could lead to confusion among the customers.

It is noteworthy that in spite of the technical feasibility of the cash-flow taxation of the financial services, no country has adopted any of the versions of this method. Considerable compliance costs are thought to be the main reason for that.

Modified Reverse Charge

The modified reverse charge as proposed by Howell Zee, shifts the collection of the VAT on deposit interest from depositors to banks, in conjunction with the establishment of a franking mechanism similar to the one used by corporations to frank dividends[31]. Under the method, tax and credits apply to interest and charges and not on the principal.

The franking mechanism is managed by banks and effectively transfers the VAT collected to borrowers as credits against the VAT on their loan interest on a transaction-by-transaction basis. The mechanism ensures that when borrowers are granted VAT credits, the credits are derived from deposits that have been reverse-charged. The absence of a link between any specific deposit and any specific loan is overcome by a pooling system with regularly updated running balances. The margin for any particular intermediation service is an average of all current deposit and lending transactions in the pool.

The outcome ensures that the net VAT revenue to be remitted to the government by a bank is equal to the VAT rate on the bank's provision of intermediation services, while, at the same time, the VAT burden on such services is borne by final consumers either directly as bank borrowers or indirectly when they consume goods and services in which the intermediation services have been embedded.

One major benefit claimed for this method is that it is fully compatible with the invoice-credit mechanism with VAT being assessed and charged at the point of each interest payment. One of the drawbacks attributed to the method is the uncertainty as to how it will work where intermediation services are provided by non-financial institutions.

Subtraction Method

Under this method, the value-added tax base is determined by subtracting from revenues expenses on taxable goods and services. For financial institutions under this approach the tax base for each VAT reporting period is determined by subtracting from the total revenues for that period (fees and commissions as well as margin income), the total cost of inputs incurred by the institution. The VAT liability is then computed by multiplying the tax base by the VAT rate.

The rationale is that if the value for financial services is included in the VAT base, financial institutions should then be entitled to full input tax deduction

This approach has some notable advantages such as its simplicity, for example: no adjustment is required when the tax is introduced or when the tax rate changes, the margin could be calculated for any given period and is subject to the tax rate applicable for that period, compatibility with the credit-invoice system as no adjustment is required.

The approach however has some difficulties. A major draw-back being that it cannot be easily calculated on a transaction-by-transaction basis and thus requires approximation or adjustments on a formula basis for zero rated exports and for giving input tax credits to registered persons. Approximations can create inequities and also lead to incentives for planning activities which could affect the long-term stability of the tax[32].

The Addition Method (Financial Activities Tax)

In 2010, at the request of the G20 countries, the International Monetary Fund (IMF) published a report titled "A Fair and Substantial Contribution by the Financial Sector" [33]. The Report proposed a Financial Activities Tax (FAT) which would be levied on financial institutions to address the under taxation of financial services. The Report proposes three alternative versions of the FAT namely: the addition method FAT, the rent-taxing FAT and the risk-taxing FAT. Of the three, the addition method FAT has received the most attention. Discussion of the FAT in this chapter will focus on the addition method.

The addition method is based on the assumption that a firm's value added equals the compensation paid or payable to its employees and owners. Under this method, taxes are levied on the total of wages and salaries and profits of the firm. VAT could be extended to financial institutions under the addition method with the tax base defined as the sum of wages and profits.

In practice, some countries are already applying some versions of the FAT as a surcharge on services that are fully or largely exempted from VAT. The addition method FAT is also commonly referred to as the addition method VAT.

Some of the adhoc systems used for applying tax on financial services such as compensatory and supplementary taxes are considered to be variants of the addition method. Examples of this approach include the Israeli and Quebec systems[34]. Under the Israeli system, taxes are levied on the sum of an entity's wages and profits, as an approximation of value added. The tax applies to insurers and deposit-taking institutions. These institutions cannot claim a credit for input VAT. Credits are also not available to registered customers purchasing financial services from financial institutions. It is essentially a separate tax from the invoice-credit VAT that is also applied elsewhere within the Israeli system.

The province of Quebec zero-rates financial services under value-added tax but imposes compensatory taxes on financial institutions in the form of supplementary payroll and profit taxes and a tax on insurance premiums.

A major objective of the addition method compensatory taxes is to raise revenue in respect of activities that are seen as not being subject to full taxation. Conceptually, if non-labor inputs are already taxed under the exemption system, then with supplementary taxation of labour used to supply financial services and the profits from supplying such services, full taxation of the value of financial services is achieved.

Some problems that could arise from the implementation of this approach have been identified such as incompatibility with the credit-invoice VAT system as it is not imposed on a transaction-by-transaction basis and inability to deal with the basic problem of tax cascading that exists in the exemption system where financial services are intermediate steps in the supply chain.

7. Conclusion

Taxation of financial services present a huge challenge from a VAT perspective for policy makers. VAT exemption for financial services, the issues associated with it as well as potential solutions to these issues have been the subject of considerable analysis and commentary for decades now. VAT originated from the EU and the exemption approach under that system is associated with a number of issues and challenges some of which have been discussed in this chapter. Many of the activities of financial institutions are intermediation services generating margin-based income rather than clearly identifiable fees or commission which makes the application of the traditional invoice-credit mechanism difficult.

Other jurisdictions that adopted a VAT system after the EU have modified or designed their VAT systems to mitigate the impact of the issues and challenges associated with EU approach with some degree of success. Alternative methods for application of VAT on financial services have been proposed by authors on the subject. While these approaches have to some extent avoided some of the problems associated with the exemption system, they have raised their own distortions and difficulties.

The Nigerian approach to taxation of financial services adopts a narrow exemption focus which is in line with the more modern approach coming after the EU system. However, whereas in most other VAT regimes, financial institutions are allowed to take credit for the input VAT incurred on making taxable financial services, banks and other financial institutions in Nigeria are not allowed to recover input VAT, even if they use the related inputs for the purposes of rendering taxable financial services.

It is noteworthy that the Nigerian approach is not restricted to financial services but applies to all other services in general. Under the Nigerian system, input VAT incurred on services is not creditable against output VAT whether or not the input VAT relate to services used in making taxable supplies. This is not in line with international practice as most jurisdiction with a VAT regime would allow recovery of input tax incurred in making taxable supplies.
In comparison with other VAT systems, the Nigerian system calls for reforms in order to

accord with international practice. One of the areas that requires review is the lack of credit for input VAT incurred in rendering taxable services.

As it is, the search continues for a fair and equitable method or combination of methods that will address the issues and complexities associated with the existing methods for VAT taxation of financial services. While the search is on-going and based on international experience, narrowing the scope of exemption and minimizing the quantum of blocked input taxes (example via zero rating of B2B margin transactions) could go a long way in mitigating some of the problems associated with the exemption system.

ENDNOTES

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4. Cap B3 LFN 2004
5. Section 16 (b)
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15. Taxation (GST, Trans-Tasman, Imputation and Miscellaneous Provisions) Act 2003 of 25 November 2003; International VAT Monitor September/October 2011, "New Zealand" at 310-315
16. Value-Added Tax Act No. 89 of 1991 (South Africa)
17. Value-Added Tax: Banking Services Provided and Fees Which May be Charged in Connection with Such Services, as prepared by the Council of South African Bankers and approved by the Commissioner for Inland Revenue, effective 1 October, 1996)
18. This document classified services in eight different categories: general banking services, card services, treasury services, credit and lending services, motor and other asset finance, securities services, other services, and international services).
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20. Section 6(1)(a) of the Act read with Part 1 of the Schedule, item 13
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CHAPTER 15

HOTEL OCCUPANCY AND RESTAURANT CONSUMPTION TAX

Abstract

Mobilising domestic resources, in particular through taxation, is key to unlocking the resources required for sustainable finance, public investment in infrastructure, growth and development. Over the years, governments, at all levels in Nigeria, have relied heavily on revenue from oil and neglected tax revenue in the process. As part of the measure to grow the internally generated revenue at the state level, Lagos State introduced the hotel occupancy and restaurant consumption tax on tourism and hospitality business. Therefore, this chapter examines the economics of taxing travel and tourism to kick-start a re-evaluation imposition of hotel occupancy and restaurant consumption tax by some states in Nigeria. The chapter further examines its implementations, and the legal and constitutional challenges its enactment has created in the Nigerian tax system. The decision of the Supreme Court on the matter, as will be read, validates the power of the State House Assembly to legislate on any aspect of tourism, other than tourist traffic, which by the judgment, is reserved exclusively for the National Assembly. The decision of the court further concludes that it is within the residual power of the State House of Assembly to enact the hotel occupancy and restaurant consumption law as one arising from its power to make laws on tourism, other than tourist traffic.

1. Introduction

Taxation is essential to sustainable development. Mobilising domestic resources, in particular through taxation, is key to unlocking the resources required for sustainable finance, public investment in infrastructure, growth and development.[1] Tax[2] is the most important, sustainable and predictable source of public finance for almost all countries. Taxes are a necessary precondition of a functioning state, which itself is essential for economic growth and for the protection of human rights.[3] In recent time, governments in a growing number of developing countries are facing the challenges of raising sufficient revenue, through taxation, to meet their competing needs. As one commentator noted:

> Over the years, governments at all levels in Nigeria have relied heavily on revenue from oil and neglected tax revenue in the process. With the current state of the oil industry, it is now clear that reliance on oil is not sustainable. Taxation is a more reliable and predictable source of revenue, but it comes with its own challenges, especially in a clime where the rate of compliance has been historically very low.[4]

The primary goal of a national tax system is to generate revenue to pay for the expenditure of government at all levels. Therefore, rising fiscal responsibilities,[5] combined with growing reluctance of residents to pay taxes, have induced many state and local governments to enact new taxes or increase rates on existing taxes. A key issue is how state governments can expand their resource base beyond transfers.

Today, in most countries, annual budgets are sufficient to cover cities' operating costs, but not to finance much-needed capital investment, particularly in the tourism sector. A good business environment for tourism is essential to support the industry's central role in many countries' development strategies. Tourism[6] is a major industry globally and a major sector in many economies.[7] As tourism continues to grow in many countries, the infrastructures of these countries are becoming increasingly overburdened. Dwyer, Forsyth and Dwyer (2010) have argued that

> Tourism development is not a free good. Like residents, tourists and their suppliers demand public services which have to be paid through taxes or user charges. Unless efforts are made to fund travel and tourism infrastructures, destinations will not be capable of attracting and retaining global market share.[8]

The influx of tourists imposes an extra cost on the government relating to the provision of items, such as greater security and improved environment. It has been noted that as non-residents, tourists do not pay to finance these extra costs, except for the contributions made by way of such taxation schemes as a Goods and Services Tax (GST).[9] In practice, the tourism sector can be taxed, either by taxing the businesses in the tourism sector or by taxing the tourist directly.[10] Occupancy tax is a tax on the rental of rooms that states or locality may require.[11] As noted above, there has been growing evidence that taxes on travellers and travel companies (tourism and hospitality industry)[12] have been increasing, as governments have viewed the expanding industry as a ready source of revenue. Research has shown that the burden of the hotel room occupancy tax falls largely on room occupants, hence, it is a consumption tax. In common with other federating states in other jurisdictions, Lagos State Government imposes a five per cent (5%) consumption tax on all goods and services consumed in Hotels, Restaurants, and Event Centres within the territory of Lagos State. The Lagos State Consumption Tax has been criticised for infringing the double taxation rule. The Lagos State Government has, however, contended that consumption tax is a residual matter under the Federal Constitution of Nigeria.[13]

In recent years, there has been considerable increase in the volume of research and scholarship on the issue of indirect taxes and, particularly, Value Added Tax.[14] This literature is informed by a variety of theoretical perspectives, which seek to address issues about governance, policy shift,[15] legal and administrative concerns, and national tax policy,[16] aimed at expanding government resource base beyond transfers[17]. While there is considerable research on a number of aspects, broader accounts of the imposition of hotel occupancy and restaurant tax law and procedures of its implementation and tax revenue sustainability in developing countries and Nigeria, in particular, are scarce[18]. This chapter examines the

economics of taxing travel and tourism. It further seeks to stimulate debate on the imposition of hotel occupancy and restaurant tax by some states in Nigeria, its implementations, legal and constitutional challenges that its enactment has created in the Nigerian tax system.

The chapter is divided into five sections, with this section as the first section. The second section examines the Nigerian tax policy, which, among other things, emphasise indirect taxation. The third section provides an overview of the hotel and restaurant industry. It further shows the overlaps that exist between hospitality and tourism. The fourth section examines the hotel occupancy and restaurant law in Nigeria, with particular reference to the Lagos State Hotel Occupancy and Restaurant Consumption Law of 2009. The fifth section analyses the court cases on the constitutionality of the Lagos State Hotel Licensing Law. The last section presents the conclusion and highlights the areas for future reforms.

2. The Nigerian National Tax Policy

Nigerian tax policy up to 2010 was a varied mix of legislation, judicial pronouncements, budget speeches, committee reports and international treaties. The National Tax Policy- an outcome of the 2002 Study Group of the Nigerian tax system- was approved by the Federal Executive Council in 2010. The National Tax Policy[19] provides the objectives to be achieved and the principles to be adhered to at all times in the Nigerian tax system. The National Tax Policy explains the aims or intentions of the government of Nigeria, the basis of which its tax activities are guided towards the achievement of set economic, social, political and other important objectives.

The underlying philosophy of the National Tax Policy (NTP) and the new tax system, envisioned to arise from the implementation of the policy, is the promotion of sustainable development, as well as healthy competition among tax and revenue authorities in Nigeria. The National Tax Policy seeks to uphold the principles of fiscal federalism in revenue generation and expenditure at all levels of government, within the ambits of the Nigerian Constitution. In simple terms:

> It will resolve issues surrounding "who gets what, how it is collected, who controls what is collected and who is ultimately responsible for and accountable to the taxpayers for the revenue collected and its expenditure.[20]

The three tiers of Government have different powers spelt out in the Fourth Schedule of the 1999 Constitution of Nigeria. State Governments of the Federation, through the Houses of Assembly, can exercise the power of imposing fees, levies and rates collectable by them and the Local Governments in the respective States;[21] this is in addition to the personal income tax they are constitutionally charged with collecting.

As stated in the current National Tax Policy, Chapter 2 of the Constitution of the Federal Republic of Nigeria, 1999, contains fundamental objectives and directive principles of state policy, which are relevant to the NTP. Accordingly, appropriate tax laws, administrative processes and procedures should be made to advance the Constitutional provisions.

Therefore, the NTP suggests that tax policies, laws and administration shall promote the attainment of the following:

> The ability of all taxable persons to declare their income honestly to appropriate and lawful agencies and pay their tax promptly; residence rights of Nigerians, free mobility of people, goods and services throughout the federation; promoting fiscal responsibility and accountability that reflects the principle of fiscal federalism; ensuring that the rights of all taxable persons are recognized and protected; eradicating corrupt practices and abuse of authority in the tax system; ensuring that the resources of the nation promote national prosperity and self-reliant economy; securing maximum welfare, justice and equity; ensuring that the resources of the nation are harnessed and distributed to serve the common good; promoting and protecting Nigeria's national interest; promoting African integration, international co-operation and eliminating discrimination; and respecting international law and treaty obligations.[22]

The Nigerian Constitution vested in each of the three tiers of government[23] the power and duty to charge and collect taxes, levies and rates, as allocated to it by the Constitution. The powers of the tax system in Nigeria are mostly given by tax legislations, passed by Acts of the National and State Houses of Assembly and Bye laws by Local Government Authorities. These legislations confer necessary powers on the taxing authorities to impose taxes on the citizens. As noted by Obatola (2013):[24]

> The need for this clear demarcation becomes necessary to avoid a situation whereby one taxpayer would be taxed more than once on the same income or profit by more than one taxing authority as it was the case prior to the promulgation of the law tagged 'Taxes and Levies (Approved List for Collection) Act' in 1998[25].

The Nigerian tax administration is one that is basically statutory in nature, as there is no type or form of tax or levy, either at the Federal level or the State/Local government levels, that is not covered by one enabling law.[26] The interpretation of these laws is left to, either a well constituted Tax Appeal Tribunal or law court, to determine, should there be a dispute between a taxpayer and the taxing authority at any level of government.

The NTP specifically, in section 2, subsection 2, states that the current policy of government should focus on indirect taxation:

> The tax system should focus more on indirect taxes which are easier to collect and administer and more difficult to evade. Tax rates should be progressive and should be designed to promote equality. The tax system should gradually seek a convergence of personal income tax and capital gain tax rates with corporate income tax rates to reduce opportunities for tax avoidance.[27]

In line with the above NTP emphasis on revenue diversification, a number of states in Nigeria have diversified their internally generated revenue base by enacting laws to tax hotel occupancy and restaurant consumption. The next section provides an overview on the hotel and restaurant industry, as bases for our further discussion.

3. An Overview of the Hotel and Restaurant Industry

The tourism industry is a major contributor to the world economy. According to the estimates of the World Tourism Organisation (WTO), international tourism alone generated $1.4 trillion in receipts, contributing 9 per cent of the global GDP, and accounting for one in eleven jobs, worldwide.[28] As tourism serves as the main market for hotel and restaurant services, visitor traffic results in a corresponding boom in the hotel and restaurant industry. The hospitality industry includes enterprises that provide accommodation, meals and drinks in venues outside of the home. These services are provided to both residents and overseas visitors. UNWTO (2015) described the international tourism's sixth straight year growth with a record of 1.2 billion tourists, noting:

> International tourist arrivals grew by 4.4 per cent in 2015 to reach a total of 1,184 million in 2015, marking the sixth consecutive year of above-average growth with international arrivals increasing by 4 per cent or more every year since the post-crisis year of 2010. Some 50 million more tourists (overnight visitors) travelled to international destinations around the world in 2015 than in 2014.[29]

In line with the development in the sector, the Federal Government of Nigeria, in its determined efforts to develop and promote tourism into an economically viable industry, had, in 1991, evolved a tourism policy. The main thrust of the policy was:

> To make Nigeria a prominent tourism destination in Africa, generate foreign exchange, encourage even development, promote tourism-based rural enterprises, generate employment, accelerate rural-urban integration and foster socio-cultural unity among the various regions of the country through the promotion of domestic and international tourism.[30]

Tourism is an activity of increasing social and economic importance, which involves movement of people from one point to the other in search of pleasure, fun, business, adventure, cultural and political exchanges. Pre-colonial Nigeria had her first international tourists in 1472, when Portuguese merchants visited Lagos, apparently in search of trade. There are also historical records of Trans-Saharan and caravan movements. Since then, the tourism industry has continued to show appreciable growth in the country. In 1962, the Government established the Nigerian Tourist Association (NTA) and charged it with the responsibility of promoting domestic and international tourism in the country. In 1976, NTA was dissolved and the Nigerian Tourism Board (NTB) established in its place. The development of the sub-sector was boosted in 1990, when the Ministry of Trade and Industry was created, and the NTB became a Corporation.

The significance of tourism lies in its great potentials for generating foreign exchange. In this regard, Okpoko and Ali (2012) have observed that tourism expenditure does not only create additional (increased) income for the workers (through employment), it is also a source of revenue for the government, since the tourism industry is expected to pay taxes or licence fees to the local or central government.[31] For example, according to the Central Bank of Nigeria (CBN), a total of 328,906 tourists arrived in Nigeria in 1987 and the receipt earned was N1.1 billion. Estimated earnings were expected to reach some N53 billion by the year 2000, and much higher by 2005, particularly given the stabilising democratic dispensation in the country[32]. According to the National Bureau of Statistics (NBS), the Nigerian tourism sector directly contributed N1.56 billion and 1.7 per cent to the GDP in 2014. It was estimated that the hospitality industry would attain 2.4 per cent growth in GDP by mid-2015 and rise by 5.8 per cent per annum in 10 years.[33] Given the enormous size and even bigger potential of the hospitality and tourism industry, it is clear why the desire to regulate the industry has been a major concern to policy makers and stakeholders.

It was observed that Nigerians preferred to travel overseas for their vacation and health care needs to the disadvantage of the very large tourism potential in Nigeria. To address this problem, the Nigerian government enacted the Tourism Law to promote, develop and regulate tourism and hospitality businesses in Nigeria. The Nigerian Tourism Development Corporation Act 1992,[34] established the Nigerian Tourism Development Corporation (NTDC) as the statutory authority empowered to promote, develop and regulate tourism and hospitality businesses in Nigeria. NTDC Act specifically requires the corporation:

> To encourage people living within and outside Nigeria to take their holidays in Nigeria, and to further encouraged the provision and improvement of tourism amenities and facilities in Nigeria. Its responsibility also includes the encouragement of the development of Hotels and their ancillary facilities necessary to promote tourism.[35]

Over time, an increasing number of destinations have opened up and this has led to investment in tourism development, turning modern tourism into a key driver for socio-economic progress. It has, therefore, been argued that, most times, hospitality businesses make use of public utilities, that, hence, such businesses should be taxed to support the growth and development of the state. Tourists encounter a wide variety of indirect taxes when they travel:

> These include excise and sales taxes levied on lodging accommodation, automobile rentals, admissions of visitor attractions, restaurant meal, purchases of gift and souvenirs and so on.[36]

For a long time, the industry has been regulated solely by the Nigerian Tourism Development Corporation (NTDC) in Nigeria. Many states in Nigeria are currently making efforts to diversify and increase internally generated revenue.[37] Measures range from extensive tax policy reforms to administrative measures, like improved remittances and recording. These include the introduction of hotels and events centres occupancy and restaurants consumption

law, thereby introducing consumption tax on the hospitality industry goods and services. As Shosanya (2010) noted:

> One of the thriving activities in Lagos State is hospitality business. It has grown in leaps and bounds and has continued to absolve (sic) unemployed youths in the state. It was further speculated that the increasing number of hospitality businesses in the state will be at geometric rate with the increasing population of people in no distant future.[38]

There are several main arguments for taxing tourism or imposing hotel occupancy and restaurant tax. State and Local Governments levy tourist taxes to diversify and expand their tax base, pay for visitor-induced increases in public services cost, and extract economic rents from tourism tax to benefit residents and correct for market failure.[39] Perhaps, this was what spurred the Lagos State government into introducing Hotel Occupancy and Restaurant Consumption Law.[40] For example, the World Travel and Tourism Council (WTTC) (2009) forecast that:

> Tourism taxes which account for $164,352 billion in 2010 (9.7 per cent of all taxes on travel and tourism), will account for 10.7 per cent of global taxation revenue by 2020.[41]

On the other hand, tourism taxes can impose costs on a destination. They can result in a contraction of economic activities, with adverse effects on Gross Domestic Product, employment and foreign exchange earnings; they can also lead to retaliation by other destinations.[42] Furthermore, poorly conceived and implemented taxation leads to fall in tourism demand, lost output, lost growth, lost jobs and a worsening economy. The consequences of taxes on tourism vary, according to the type of tax and the tax system that are in operation within the destination. Occupancy tax rates and rules vary by city, county, state, and country. They are generally owed on the accommodation price, plus any fees for other items, like cleanings or extra guests.[43]

Overlap between Hospitality and Tourism

While often grouped together as a single industry, the hospitality and tourism industries should be viewed as two different, though overlapping sectors:

> The tourism industry can be defined as 'the activities of persons travelling to and staying in places outside their usual environment for not more than one consecutive year for leisure, business and purposes other than being employed in the place visited'.[44]

As defined earlier, the hospitality industry covers the provision of accommodation, meals and drinks in venues outside of the home. These services are provided to both residents and overseas visitors (non-residents).[45]

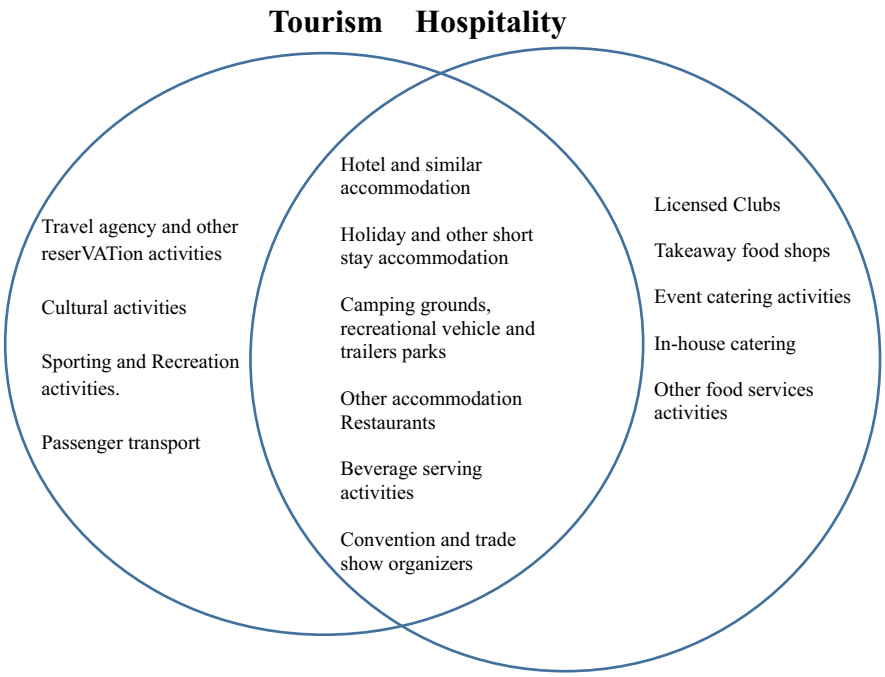

Figure 1 Mapping of tourism and hospitality industries[46]

Figure 1, above, illustrates the overlap and inter-related nature of the relationship between the tourism and hospitality industries. Definitions for both industries cover hotels, accommodation, restaurants and public houses. Activities specific to the hospitality industry include catering activities, licensed clubs and takeaway food shops, while activities specific to the tourism industry include travel agency activities, cultural activities, sporting and recreational activities, and passenger transport services.

4. Hotel Occupancy and Restaurant Consumption Law in Nigeria

The instability of oil revenues as a result of the volatile global oil market is one major source of concern for such dependence of Nigerian state governments on revenues accruing to the federation account[47]. There are issues with the options, capacity and opportunities for some of the federating units (particularly, the states and local governments) to raise internally generated revenues. *Nigeria Governors' Forum (2015)* further observed that:

> A number of the revenue line items assigned to states by the Constitution are yet to be developed enough to yield robust revenues to them.[48]

As part of the measure to grow the internally generated revenue of Lagos State, the Lagos State Government introduced the hotel occupancy and restaurant consumption tax. The introduction of this tax led to a debate on the constitutionality of the hotel occupancy and restaurant consumption law. The former Executive Governor of Lagos State[49] assured the citizens that the legislation was people friendly and had the potentials of growing the state's economy:

> We shall give due priority to the upgrading of infrastructure and security around hotel facilities and tourists sites. We expect that the attendant boost to economic activities in the tourism and leisure industry will also aid support industry to greater profitability, attract even more visitors to Lagos State and generate even more employment opportunities.[50]

While the legislation was favoured by some commentators, a number of mixed reactions were articulated by other stakeholders. To justify the action of the state, the governor further noted that:

> As a people and as a nation, we have decried relative level of our development and we have compared ourselves with the progress made in other jurisdictions and we have not asked ourselves enough what price other jurisdictions have had to pay for the level of their development. This is one of the things that are done in other jurisdictions by whose standards we measure ourselves.[51]

Therefore, the introduction of the hotel occupancy and restaurant consumption tax law by the state government was commended to be a right step in the right direction and was not tantamount to double taxation in the real sense of it.

Legal Framework

Sales Tax Act enacted by the Federal Military Government vested the administration of sales tax within each state in the state government. The revenue from the tax collected by each state forms part of its Consolidated Revenue Fund and utilised for its independent purposes at its discretion.[52] Following the second advent of military rule in 1984 and the consequent suspension of the 1979 Constitution, the Sales Tax Decree, No. 7 of 1986 was promulgated. It empowered state governments to administer and take the benefit of revenue from sales tax. It has been argued that countries introduced Value Added Tax because they are dissatisfied with the existing tax structure.[53] This dissatisfaction was based on the fact that the then sales tax was not satisfactory and that the evolution of the system had not kept pace with the development of the country. In contrast, Olumide (2014) noted that:

> The federally administered VAT and its prospects of increased revenue to the states appear to have shifted the focus of the state governments from their respective sales tax regimes such that Sales Tax Laws of the states such as Lagos and Ogun, although not repealed, were hardly enforced.[54]

It was further argued that the re-introduction of sales tax in Lagos State in 2000 witnessed stiff resistance from the agents for the collection, accounting and remittance of the tax. This resistance invalidated the Lagos State Sales Tax Law. While this was being contested in court, Lagos State enacted the hotel occupancy and restaurant tax law. The Hotel Occupancy and Restaurant Consumption Tax Law[55] imposes a 5 per cent tax on goods and services consumed in hotels, event centres and restaurants within Lagos State.[56] The tax base is the total cost of facilities, consumable or personal services supplied to a consumer in, by or on

behalf of the hotel, restaurant or events centre[57], excluding the value added tax. Hotel restaurants and other businesses, affected by the law, are required to register with Lagos State Internal Revenue Service (LIRS)[58] within thirty days of the commencement of the law or upon commencement of business (whichever is earlier).

Registration

Any hotel, restaurant, departmental store, or other business, affected by this law, shall, within thirty (30) days of the commencement of law or upon commencement of business, whichever is earlier, shall be registered with the service for the purpose of the law. Every collecting agent shall register and collect a certified electronic fiscal device or electronic cash register to be used for the collection and recording of payment. For hotels, hotel facilities or event centres, the rate of tax imposed by this law shall be five percent (5%) of the total bill issued to the consumer, excluding value added tax.

Reporting Requirements

Persons owning, managing or controlling any business or supply goods or services chargeable under the Law (for example, hotel owners and managers) are the collecting agents on behalf of the LIRS and are required to remit amounts collected to the LIRS on or before the 20th day of each calendar month.[59] As Elebiju (2014, p. 151) puts it:

> Section 12 HOCL mandates transferees to withhold amounts due under HOCL from the sale price if affected businesses or facility are to be sold, and requires them to conduct due diligence, for example, by confirming from LSIRS the current HOCL liability status of the target. Failing this, amount due prior to transfer date in respect of the affected business or facility could be recovered from the transferee.

Therefore, the tax filing must be accompanied with a report, stating the total amount of payments made for all chargeable transactions during the preceding period. In addition, the amount of tax collected by the agent, during the reporting period must be disclosed, and any other information, required by LIRS is to be included in the report. Furthermore, every collecting agent is required to keep, maintain and preserve such records, books and accounts in respect of all transactions chargeable under the law. Where a collecting agent fails to make a return or remittance as and when due, the LIRS may make an estimate of the total amount due and such an estimate shall become due, not later than 21 days of the service of such notice.

Exemption from Sales Tax Law

From the commencement of the HORCT Law, the Lagos Sales Tax would not be applicable to any transaction or facility covered by the HORCT Law. The only exemption is only in respect of goods and services consumed in hotels, event centres and restaurants within Lagos State, which are liable to tax under this new law.

Appeals Procedure

Any person aggrieved by the assessments made under the HORCT Law may object thereto within seven days to the LIRS of being notified of such a decision, or other designated officer, requesting the service to review, amend or reverse the assessment. Upon receipt of such a notice, the LIRS may reconsider, affirm or amend its assessment and notify the complainant of its decision. Where the LIRS has served the complainant a notice of refusal to amend, a complainant, who is dissatisfied by the refusal, may institute an action at the Lagos State High Court. Where an aggrieved taxpayer fails to contest the assessment within seven days, the assessment shall be deemed to be final.[60] Elebiju (2014) notes that the time required to respond is not in consonance with other similar legislations:

> The objection period is rather short, compared to thirty days under sections 69(2) and 58(1) of Companies Income Tax Act (CITA) and Personal Income Tax Act (PITA) and twenty one (21) days under Petroleum Profit Tax Act (PPTA), section 38(2) respectively.[61]

The LIRS has the powers to distrain the property of persons, who, after their assessments have become final and conclusive, have not responded to demand notices within the time required for the payment of the tax owed. Section 14 enshrines the jurisdiction of the State High Court over the HORCT Law issues, particularly the actions of the LIRS to enforce the law.

Penalty

Failure to remit the tax collected within the stipulated time would attract interest at the rate of 5 per cent per annum above the prevailing Central Bank of Nigeria (CBN) minimum rediscount rate (MRR), as determined at the time of actual remittance[62]. Where a collecting agent fails to file a report and remit taxes within the stipulated time, in addition to the interest payable, a penalty of 10 per cent of the amount of tax due will become payable. Persons convicted under the law may be liable to imprisonment for up to two years, or a fine of up to two million naira, or both.[63]

5. Constitutionality of Lagos State Hotel Licensing Law

The Hotel Licensing Law 2003[64] and the 2010 amendment[65] established the Lagos State Hotel Licensing Authority (LSHLA) and made other provisions for the licensing of hotels. This law further empowered Lagos State to make laws to regulate, standardise and grade tourism operations, which was previously the exclusive preserve of a federal government agency, the Nigerian Tourism Development Corporation (NTDC). It was in the exercise of its powers to license and regulate hotels that the House of Assembly enacted the HORCT Law.[66]

The imposition of sales tax by some states in Nigeria has been resisted on the grounds, either that a state lacks the power to impose taxes under Nigeria's Constitution, or that a state cannot validly impose sales tax as long as the Value Added Tax Act, a federal law, remains in force, the Value Added Tax Act having 'covered the field'[67]. The key arguments against the hotel

occupancy and consumption law were that:

> It exemplifies double taxation, being a consumption tax that duplicates value added tax; Lagos State Government (LASG) should resolved its VAT issues with the Federal Government rather than making affected businesses bear the brunt of the HOCL; and the HOCL is discriminatory and punitive of the hospitability sector, thereby breaching constitutional provisions against discriminatory treatment.[68]

As a consequence, some stakeholders went to court to challenge the validity of the hotel occupancy and consumption law. Odinkonigbo and Ikeyi (2015) contend that:

> None of these grounds is valid under Nigeria's Constitution: a state government can impose sales tax in exercise of its residual powers; and the doctrine of covering the field is inapplicable in the inquiry.[69]

Nigeria's fiscal operations adhere to the Federal System of Government. The government's fiscal authority is based on a three-tiered tax structure divided between the Federal, State and Local Governments, with the Federal Assembly and the State Houses of Legislature exercising their legislative (exclusive, concurrent and residual) powers to administer the relevant taxes falling under their jurisdictions. The next section presents the cases at the High Court.

The Cases at the High Court

The cases reported here were at both the state and the federal levels. The case at the state level was instituted by Mas Everest Hotels Limited and another against the Attorney General of Lagos Sate and another, challenging the constitutionality of the HORC tax. In addition, two other reported litigations were instituted at the Federal High Court. The Registered Trustees of the Fast Food Confectioners of Nigeria and Prince Court Limited sued the state government at the Federal High Court, challenging the validity of the law.

Lagos State High Court

After the enactment of the Hotel Occupancy and Restaurant Consumption Bill of Lagos State into Law, Mas Everest Hotels Limited and Chariot Hotels Limited also filed a suit against the Attorney-General of Lagos State and the State Internal Revenue Service (LIRS) at the State High Court,[70] contending that the state government could not validly make the consumption law to impose tax on goods and services consumed in hotels, restaurants and event centres, in view of the provision of section 4(2) and (3) of the Constitution of the Federal Republic of Nigeria 1999 and section 1 of the Taxes and Levies (Approved List for Collection) Act. The Claimants, therefore, prayed the court to restrain the government from enforcing the law, arguing that the law was invalid by virtue of the above quoted sections. The Defendant filed a preliminary objection, challenging the *locus standi* of the Claimants to bring the action, since they were not the 'consumers' liable to pay the tax. In a considered ruling, the lower court, presided over by Justice Hakeem Oshodi, held that:

> The consumption tax law was validly passed by the Lagos State House of Assembly, adding that it was separate and distinguishable from the taxes

> exclusively reserved to the federal government. The court also identified that the hotel operators lacked the locus stand to sue because they were agents for collection while the tax was on consumers.[71]

On the issue of validity, the court held that the hotel occupancy and consumption law is valid because it does not purport to apply to specific matters on item 59 of the Exclusive Legislative List (2nd Schedule 1999 Constitution) over which only the National Assembly could legislate (taxation of incomes, profits and capital gains), but rather 'affects the spending power of the consumers'. The presiding Judge further states that:

> The tax is limited, and not general. It is not targeted on income or profit or capital gains, but consumers who pay for the use or possession or for the right to the use or possession of any hotel, hotel facility or events centre, or who purchase consumable goods or services in any restaurant whether or not located within a hotel in Lagos State.[72]

The Court further notes that, since relevant constitutional provisions contain the reserVATion '*except as otherwise provided by this Constitution*'[72], section 4(7) 1999 Constitution empowers the State Houses of Assembly to legislate on both the concurrent and residual lists, and that, since collection of taxes is on the concurrent List, '……the Law is not unconstitutional'. The Court dismissed the claim and ruled that the HORCT Law was within the legislative competence of the Lagos State Government.

Federal High Court

At the Federal High Court, Registered Trustees of Association of Fast Food Confectioners of Nigeria and Others, in 2009, challenged the imposition of the HORC tax by asking the Court to restrain a tax authority from the enforcement of the tax law. The Registered Trustees contended that the law imposed double obligation on them as collecting agents under the law, in addition to a similar obligation performed under the provisions of the Value Added Tax Act. They further argued that the discharge of the obligation, imposed by the new consumption law, would materially impair their business, as they would incur administrative costs in its collection, which would also impair the consumption finances of their customers. In its verdict on the case[73], the Federal High Court, presided over by Justice Okechuckwu Okeke, restrained the Lagos State government from implementing the law. The Court, in granting the interlocutory injunction, stated that:

> While appreciating the 1st defendant's effort to provide infrastructure and service for the populace, there is still the need for the exercise of patience and operation under the rule of law. That is the hallmark of true democracy.[74]

The Court held in favour of the Applicants that, subjecting applicants' customers to circumstances that might amount to double taxation and subjecting the applicants to double obligation, with respect to complying with the Value Added Tax obligation and the obligation under the HORCT Law would impair the business of the applicants and that this would be a ground for granting an injunction against a tax authority. Subsequently, the 1st defendant (Attorney General of Lagos State) filed a preliminary objection, praying the court

to strike out the matter on the ground that:

> The subject matter of the suit was a State law and, therefore, not one of the matters under the jurisdiction of the Federal High Court and that reliefs sought in the matter were against the 1st defendant who was not a State agency.[75]

The Plaintiff, in opposing the preliminary objection, contended that the Federal High Court had jurisdiction, as the new tax imposed an obligation on companies and, thus, affected operations and that the 2nd Defendant was an agency of the Federal Government. The preliminary objection, premised on lack of jurisdiction, was dismissed by the Court and the Court held that:

> The dispute is whether the plaintiffs should continue to pay taxes on goods and services rendered by them under the Value Added Tax Act and Hotel Occupancy and Restaurant Consumption Law 2009 touches on the revenue accruable to the Government of the Federation. It is my humble view that the Federal High Court has jurisdiction to resolve this dispute.[76]

A further case[77] was filed at the Federal High Court, seeking declaratory relief, amongst others, that the HORC Law was inconsistent with the VAT Act and the Taxes and Levies (Approved List for Collection) Act and was unconstitutional, being inconsistent with sections 4(4) and (5) and items 7[78] & 8[79], Part II, Second Schedule, 1999 Constitution.

The Federal High Court, presided over by Justice Ajakaiye, held that the hotel occupancy and consumption Law to be void for inconsistency with constitutional provisions, as well as with the provisions of the VAT Act and the Taxes and Levies (Approved List for Collection) Act. Furthermore, the operators of affected businesses have a *locus standi* to challenge the HORC Law because it imposes similar obligations on them, as collecting agents, as the VAT Act does:

> If the Lagos State Law is upheld, it will amount to the Plaintiff serving two masters and it will be to its prejudice.

This flowed from the Court's decision that no person or authority has the right or power to assess or collect any tax in form or semblance of value added tax other than the Federal Government.

> …I am of the view that the tax imposed [pursuant to hotel occupancy and consumption Law] is same as imposed by virtue of the provisions of the VAT Act…[80]

There was an appeal to the Court of Appeal[81] on the decision of the Federal High Court. One of the issues for determination was whether the learned judge was right when he held that VAT Act had covered the field of sales tax and that the plaintiff/respondent was a taxable or remitting agent to only the Federal Board of Inland Revenue (the 2nd respondent) in respect of tax on sales to its customers and that it would amount to double/taxation to require the 1st

respondent to yield to the demands of both the 2nd respondent and the appellant at the same time.

The core of the decision of the court was that VAT and sales tax were the same, as VAT was ordinarily a national tax on sales of goods and services. With reference to whether the provisions of the VAT Act and the Sales Tax Law create double taxation, the court held in the affirmative that:

> As the actual beast of burden of the VAT/sales tax is the consumer and the tax is charged on similar consumable items as defined in the Schedules of both the VAT Act and the Lagos State Sales Law. It affirmed that with respect to VAT collection and remittance, the 1st respondent is an agent only to the 2nd respondent and as such is obligated to collect and remit VAT to same; and that it is not so obligated with reference to the appellant.

The court further held that in the circumstances, VAT had covered the field of tax on consumption of the services provided by the 1st respondent:[82]

> Value Added Tax is neither on the Exclusive nor Concurrent Legislative Lists contained in the Second Schedule to the 1999 Constitution. This means that VAT is a residual matter.

The import of this decision on the Nigerian tax system is that, whereas the House of Assembly of a State may legislate on the residual field, where the National Assembly has already legislated on such an item, then the law passed by the House of Assembly is null and void because the 'field' in question has already been 'covered'.[83] Therefore, in the case under review, the court gave an order restraining the 1st and 2nd Defendants, either by themselves, their privies, servants, or whosoever, acting on their instruction, from enforcing, in whatever form, the said HORC Law against the Plaintiff.

In 2017, the LIRS issued the Hotel Occupancy and Restaurant Consumption (Fiscalisation) Regulations ("the Regulations") pursuant to its powers under Section 9 of the Law. The Regulations require that:

> All persons who own, manage or control any business or supply any goods or services chargeable under the Law, to use an Electronic Fiscal Device to record all taxable transactions.[84]

The Registered Trustees of Hotel Owners and Managers Association of Lagos ("RTHMAL" or "the Trustees"), being displeased with the provisions of the Regulations, filed an ex-parte motion with the FHC for an Order of Interim Injunction restraining:[85]

> i. The LIRS, its agents, servants, privies, or any other person from enforcing and/ or implementing the provisions of the Act and/or the Regulations.
> ii. The LIRS, its agents, servants, privies, etc. from visiting members of RTHMAL between 1 March – 10 March 2018 or any other period before or thereafter for the

> purpose of installing the Fiscal Electronic Device and/or any other purposes whatsoever in furtherance of the Law and/or the Regulations.

In granting the above prayer, the FHC granted RTHMAL's request by issuing the above Order on 21 March 2018. However, following further representations by the counsels to the first defendant and the plaintiffs, the FHC varied its initial Order on 7 May 2018. The new FHC Order allows:

> The LASG to continue to enforce the Law, but not the Regulations, pending the final determination of the substantive suit.

In essence, the LASG is permitted to continue to enforce the provisions of the Law pending the determination of the suit, but cannot install any Fiscal Electronic Devices or enforce any provisions of the Regulations. The RTHMAL contention in its originating summon was that the VAT Act already covered the field as it relates to taxation of consumption of goods and services in hotels, restaurants and event centres. According to the RTHMAL:

> Based on the doctrine of 'covering the field' the consumption tax imposed by LIRS should remain in abeyance and cannot be enforced at the same time as VAT.

Contrary to the claims conversed by RTHMAL, the A.G., Lagos State in support of their case argued that in view of the fact that the Constitution of the Federal Republic of Nigeria 1999 does not make any provision for the taxation of consumption of goods and services in hotels, restaurants and event centres, the taxation of such matters is a residual matter lying within the exclusive purview of the State House of Assembly. The A. G., noted further that:

> The doctrine of covering the field cannot be invoked in this case because the Constitution does not empower the National Assembly to make legislation for the taxation of consumption.[86]

In addition, the A.G., Lagos State argued that the Taxes and Levies (Approved List for Collection) Act by its subsidiary Amendment Order of 2015[87] overrides the VAT Act. Relying on the Amendment Order of 2015, the A. G., Lagos State, charged the Court that by listing Consumption Tax as one of the taxes to be collected by States, must be deemed to have repealed the VAT Act because the provisions of the two laws cannot be given effect simultaneously.

On 3rd October 2019, the Federal High Court sitting in Lagos[88] declared the provisions of the Value Added Tax Act in relation to goods and services consumed in hotels, restaurants and event centres invalid and unconstitutional in view of the provisions of the Constitution of the Federal Republic of Nigeria and the Taxes and Levies (Approved List for Collection) Act. The Court also granted an order restraining the Federal Inland Revenue Service from enforcing the VAT Act with respect to goods and services consumed in hotels, restaurants and event centres.

The Case at the Supreme Court

The Federal Government (before the Supreme Court) challenged the right of Lagos State to make laws on tourism, specifically where the National Assembly had already legislated on the same issue through the NTDC Act 1992.[89] The issues for determination were:

> Whether matters pertaining to tourism fall under the exclusive legislative list of the Constitution of the Federal Republic of Nigeria 1999; Whether the Lagos State House of Assembly and the Lagos State Government can enact and promulgate laws on matters within the exclusive legislative list; Whether the Lagos State House of Assembly and the Lagos State Government can enact and promulgate laws which directly conflict with the provisions of an existing law of the National Assembly and if it can supersede the National Assembly law.[90]

The respondent, on the other hand, argued that the power of the National Assembly to make laws on tourism is restricted to tourist traffic, which relates to the imposition of administrative restrictions on entrants to Nigeria by way of permitting them to enter the country and limiting their period of stay within the country. The claimants prayed the Court to establish:

> Whether regulation, registration, classification and grading of hotels, guest houses, motels, restaurants, travel and tour agencies and other hospitality and tourism related establishments are matters in the Exclusive and Concurrent Legislative List and outside the legislative power of Lagos State House of Assembly. Whether the relevant laws of the Lagos State are invalid by reason of their inconsistency with the provision of the Nigerian Tourism Development Act.

The key decisions of the Supreme Court border on tourist traffic and the doctrine of covering the field. On tourist traffic, the Supreme Court held that the power of the National Assembly to make laws on tourism was restricted to tourist traffic and did not extend to other aspects of tourism, which the court held to be within the residual power of the States' Houses of Assembly. The Court, in defining the scope of the phrase, tourist traffic,[91] used in the Exclusive List, held as follows:

> The words 'tourist traffic' used in item 60(d) of the second schedule of the Constitution, alludes to ingress and egress of tourist from other countries. These are international visitors or foreigners.[92]

The Court further stated:

> What I can deduce, from the above definitions of 'tourist traffic', is that it applies to anyone who moves from one place to another for sightseeing, relaxation and possibly cultural purposes. It may not necessarily be from another country, but within a country; from one town to another. But within the context of item 60(d) it connotes that a tourist is an international traveller who travels to another country for the purpose of sightseeing, etc., and who

> must thus obtain a visa to visit the said other country, (in this case Nigeria) which calls for the exercise of the function of the immigration department of the Ministry of Internal Affairs, as governed by the Immigration Act Cap 1 2004 of the laws of the Federation of Nigeria. My interpretation of tourist traffic, used in item 60(d) of the Second Schedule of the Constitution supra, is that it alludes to the ingress and egress of tourist from other countries. It is definitely confined to International Visitors, i.e., foreigners.[93]

Based on the above, the Supreme Court held that the contention of the Federal Government on matters pertaining to the regulation, registration, classification, grading, of hotels, motels, guest houses, restaurants, travel and tour agencies, and other hospitality and tourism-related establishment are matters within the Exclusive Legislative List, is incorrect and unsustainable. The Court further held that the Federal Government lacks the constitutional powers to make laws on other aspects of tourism other than tourist traffic which by implication residue matters for the State Assembly. The Supreme Court held as follows:

> The purported exercise by the National Assembly of its legislative power in enacting the National Tourism Development Corporation Act which regulates hospitality facilities is certainly a null and void one. The null and void Act cannot even be saved by virtue of item 68[94] of part 1 of the same 2nd Schedule since the subject matter it dwells upon, regulation and classification of hotels and eateries, is neither incidental nor supplementary to the task the Assembly is empowered to legislate on by virtue of item 60(d) of part 1 of 2nd Schedule of the Constitution.[95]

On the application of the doctrine of covering the field, the Supreme Court held that the doctrine would apply where both the Federal and State legislatures could legislate on a matter under the Concurrent Legislative List. The court held that the doctrine could not be applied to preclude the State House of Assembly from making laws on tourism since tourism was not one of the matters set out in the Concurrent List of the Constitution of the Federal Republic of Nigeria. Thus, the Supreme Court held, as follows:

> The relevant authorities are to the effect that the doctrine is applicable to where concurrent legislative powers are validly exercised on the same subject matters. This point was exhaustively thrashed in the locus classicus on the matter in the case of LAKANMI v. ATTORNEY-GENERAL WESTERN REGION (1970) 6NSCC 143 and re-echoed in the case of ATTORNEY-GENERAL OGUN STATE v. ATTORNEY-GENERAL FEDERATION (1982) 13 NSCC 1 at 35, where it was held that
>
> '… The phrase covering the field' means precisely what it says where a matter legislated upon is in the concurrent list and the Federal Government has enacted a legislation in respect thereof where the legislation enacted by the state is inconsistent with the legislation of the Federal Government, it is void and of no effect for inconsistency.

Explaining further the concept of 'covering the field', the Court referred to *Federalism in Nigeria under the Presidential Constitution* by Prof. Ben Nwabueze, SAN, where he had opined thus:

> The question whether a state law on a concurrent matter can co-exist with Federal Law on the same matter arises where the latter expressly or impliedly evinces an intention to provide a complete statement of the law governing the matter.

In the light of the above, the Court found that the doctrine had no application to the issue before it.[96] The Supreme Court, therefore, dismissed the federal government's suit and delivered its judgment in favour of Lagos State. It was the view of the court that the NTDC Act went beyond its powers, as stated in the Exclusive Legislative List of the Constitution, which is to regulate 'tourist traffic'. This effectively challenged the constitutionality of the NTDC's powers to unilaterally regulate and control hotels and tourism in Nigeria. The court, therefore, validated the respective laws of Lagos State.

The Implications of the Supreme Court Judgment

The HORC Law has been challenged in a number of cases[97], with conflicting decisions on its validity. Henceforth, the judgment given by the Supreme Court cannot be challenged further on the same principle. The key tax issue arising from the judgment of the Supreme Court is whether by holding that the Lagos State House of Assembly has the constitutional power to enact the HORC Law, the Court has validated the right of the state government to make laws on the taxation of consumption of services relating to hotels, motel, guest houses, restaurants, travel and tour. As noted by some commentators:

> The judgment did not address the issue of the imposition of tax and whether or not Lagos State has the constitutional right to impose consumption tax on hotels, restaurants and event centres.[98]

The decision of the Supreme Court is a validation of the power of the State House Assembly on any aspect of tourism, other than tourist traffic, which, by the judgment, has been settled to be reserved exclusively for the National Assembly. Furthermore, by holding that it is within the residual power of the State House of Assembly to enact the HORCLaw, as one arising from its power to make laws on tourism, the Supreme Court has affirmed the power of the State House of Assembly to impose taxes on consumption of services relating to tourism, other than tourist traffic. In this connection, Ipaye has noted:

> I believe that just about that period, the Aberuagba case was litigated and Supreme Court very clearly said that matters of domestic consumption were undoubtedly in the purview of the State to choose when, if and how to tax, that it had nothing with the Federal Government. Ref.?

The judgment can also be construed as setting a limitation on the application of the Value Added Tax Act. By its decision that it is within the residual power of the State House of Assembly to enact the HORC Law, the Supreme Court has also stated indirectly that the

National Assembly does not have constitutional vires to make laws on such a subject-matter. This, therefore, implies that VAT Act will not apply to those subject-matters being an Act of the National Assembly.

Hotels, restaurants, and event centres, liable to the Lagos State consumption tax include:

> …any building used as a guest house, inn, lodge, motel, tavern, night club, restaurant, event centre and any other place for the sale of food and drink within the premises of a hotel and includes fast food outlets and restaurants operating outside the premises of a hotel. [99]

The Licensing Law does not clearly define an event centre or a restaurant. These were defined in the Hotel Occupancy and Restaurant Consumption Law, as follows:

> Event centres includes hall, auditorium, fields and places designated for public use at a fee. Restaurant includes any food sale outlet, bar, tavern, inn or cafe, whether or not located within a hotel.[100]

In the above context, Oyedele (2013)[101] argued that both definitions have a wide scope and are potentially ambiguous.

In AG Federation vs AG Lagos, where the federal government had sought to invalidate Lagos State laws that regulate hotel occupancy and licensing and restaurant operation within Lagos State, the Supreme Court held that the federal government's power to enact laws on Tourists Traffic under Item 60 of the Exclusive List would not oust Lagos State's power to regulate intra-state hotel businesses. In the light of the afore-mentioned court decision, Obayemi (2014) submitted that:

> It is therefore necessary to state that clear judicial pronouncement is still required to resolve the issue as to whether it is legal for the federal government to continue to collect VAT on goods and services relating to hotel licensing and occupancy or other restaurant operations, in view of the fact that the Supreme Court has ruled that such subject-matters are clearly ultra vires of the federal government and are solely reserved for States.[102]

The next section examines the recent development in hotel occupancy and restaurant consumption tax across some states in the country, after the Supreme Court judgement that validates the power of the State House Assembly to legislate on any aspect of tourism, other than tourist traffic, which, by the judgment, is reserved exclusively for the National Assembly.

6. Recent Development in Hotel Occupancy and Restaurant Consumption Tax

A number of other states in the South West, South East, South-South, North West and North Central geopolitical zones of Nigeria, have also followed the footsteps of Lagos State by enacting their versions of the HORC Law. The Edo Hotel Consumption Law also imposes 5 per cent tax on target transactions, but unlike that of Lagos, payment is due on or before the

7th day of the following month. Delayed remittances, as contained in Section 12, attract 2 per cent interest above the CBN'S MRR, as against 5 per cent in Lagos State. Other states, such as Ogun State, Rivers State, Kwara State, Abia State, Delta State, Kano State and Imo State, have also enacted their own Consumption Laws, as contained in Table 1. Therefore, with this trend, and with the current drive for revenue diversification, a number of other states in the federation are likely to enact their consumption laws in no distant future.

Table 1: List of States with Consumption Tax

State	Name o f the Tax Law	Year
Lagos State	Lagos State Hotel Occupancy and Restaurant Consumption Tax	2009
Edo State	Hotel and Event Centres Occupancy and Restaurant Consumption Law	2011
Ogun State	Hotel Occupancy and Restaurant Consumption Law	2015
Rivers State	Hotel Occupancy and Restaurant Consumption Bill	2016
Kwara State	Hotel Occupancy and Restaurant Consumption Bill	2017
Abia State	Hotel Occupancy and Restaurant Consumption Law	2015
Delta State	Hotel Occupancy, Restaurants and Departmental Stores Consumption Tax Bill	2017
Kano State	Consumption Tax Law	2017
Imo State	Hotel Occupancy and Restaurant Consumption Tax Law No. 35.	2019

Source: Extracted from *the States' Consumption Tax Laws.*

As indicated in the above Table, states have now seen that consumption tax is one of the funding options for states to support their development strategies following the revenue shortfalls from the federal allocation. As one commentator noted:

> As any resident or business owner in Lagos State can see, we have several important developmental needs for which our collective efforts and contribution are necessary. Ref.?

Therefore, the governments still need to do a lot to enlighten the people on the necessity for the law and assure the citizens that, as practised in major cities of the world, consumption tax is only on goods and services consumed in restaurants, hotels and event centres.

7. Conclusion

This chapter has sought to stimulate debates about the contemporary role of tourism and hospitality, its regulation and taxation. It has also focussed on the enactment of HORC tax in Lagos State and the legal and judicial debates on the constitutionality of the state licensing law. Consumption tax law came to the centre stage of tax policy because of the extensive expansions required in the states, for which government needs revenue to implement. It was also driven by the recent determination of government to diversify its revenue base and move towards indirect taxation because of its inherent benefits. While consumption tax has revenue potentials for the states, it has recorded a huge resistance from different stakeholders. The debate on its constitutionality was laid to rest by the Supreme Court judgment on Lagos State hotel licensing law (and its amendment) and the hotel occupancy and restaurant consumption law.

Governments all over the world are targeting tourism as a growing source of their revenues. However, tourism taxation can have significant effect on welfare, which should be taken into account when taxes are levied. The usual criteria for good taxation are that it should be efficient, equitable and administratively simple. There are sound economic reasons for taxing tourism beyond simply collecting revenue to provide public service to tourists and their suppliers. However, tourism taxes can impose costs on a destination, resulting in a contraction of the economic activity. Excessive taxation of international tourism or goods and services in the hospitality sector may cause tourism to suffer, relative to other sectors in the global economy.

The National Tax Policy prescribes a number of ways by which disputes can be resolved, taking into cognisance the role and status of the various stakeholders in the whole system. While recognising the extant constitutional provision, which requires disputes between Federal and State Governments to be resolved by the adjudication of the Supreme Court, the National Tax Policy advocates alternative dispute-resolution methods[103] before the parties resort to litigation at the Supreme Court.

Taxpayers are constitutionally empowered to seek judicial remedy to disputes in which they have a stake. Taxpayers are, therefore, entitled to explore the tax appeal process if and when they are dissatisfied with the decisions of any tax authority relating to the taxpayer's status. They may also explore the same option with regard to the interpretation/application of tax laws and other matters, which may affect the rights and status of the taxpayer. Tax authorities are expected to enlighten taxpayers on the tax appeal process and are responsible for informing taxpayers, individual or corporate, of their right to tax appeal. Tax authorities may also engage taxpayers so as to collaborate with them on alternative dispute resolution of such contentious issues.

The net benefit from tourism development depends critically on how a destination designs its public finance/revenue system to tax travel and tourism. Evidence has shown that Nigeria is one of the countries in the world, that are perceived to have some of the highest costs of doing business because of the lack of basic infrastructural facilities and multiple taxation. The co-existence of VAT with the Lagos State Consumption Tax will only exacerbate these perceptions to the further peril of all the economies, State or Federal. The inability to restructure equitably the distribution of VAT proceeds, or to increase its charging rate, while reducing the tax rates for personal and corporate taxes, makes a strong case for the transfer of its administration to each individual State in the Federation of Nigeria for VAT to be charged on goods and services distributed within that State, while the Federal Government administers VAT on goods and services within its direct jurisdiction, i.e., regarding matters on the exclusive legislative list.

8. Recommendations

However, tourism taxation can have significant effect on welfare, which should be taken into account when taxes are levied. The usual criteria for good taxation are that it should be efficient, equitable and administratively simple.

1. Policy makers should be mindful of the experience so far suffered on all sides when formulating taxes affecting the tourism and hospitality industry.

2. Policy makers should have wide consultations with stakeholders who would come to be affected by taxes from different levels of government on related tax bases.

3. Mediation by the Judiciary must be done in a manner that does not impugn on the independence and the impartiality of the Judiciary, especially if it appears likely that such a dispute may finally be resolved through judicial adjudication.

ENDNOTES

1. See: A. Cobham, Tax Evasion, Tax Avoidance and Development Finance, *QEH Working Paper Series – QEHWPS 129*, 2005, available on-line at http://www3.qeh.ox.ac.uk/pdf/qehwp/qehwps129.pdf Accessed on 18th July, 2008; and O. J. Otusanya, 2010 ???- A number of studies have noted that if countries and states are to eradicate poverty and hunger, then they will need to do so by increasing their own public finances – principally through tax revenues.
2. Tax plays a vital role in society. They bind citizens together in a social contract with the governments they pay them to, and who they expect to spend them. Tax should redistribute wealth from corporations and rich individuals, fund public services and tackle poverty.
3. See S. 24 of the 1999 Constitution of the Federal Republic of Nigeria. The Constitution enjoins every citizen to declare to the appropriate and lawful agencies his/her income for tax purposes and ensure that tax once imposed on him/her or his/her property is paid promptly. This is to enable the government to carry out successfully its duties to the public in order to meet the basic primary and secondary needs of the people. Also, see S. 4 of the Constitution.
4. See T. Oyedele, Guess how many Nigerians Pay Tax and how our Government Spends the Money, *Tax-Watch*, June 2016, p. 1.
5. In the past few years, state and local governments have grappled with dire budget cuts and dwindling revenue. To make ends meet, they have turned an eye toward one of the easiest targets in town – travellers, who can pay taxes for hotel rooms.
6. According to the United Nations World Tourism Organisation (UNWTO), over the past six decades, tourism has experienced continued growth and diversification to become one of the largest and fastest growing economic sectors in the world.
7. The World Travel and Tourism Council (WTTC) estimates that tourism contributed 9.2 per cent of global GDP and forecasts that this will continue to grow at over 4 per cent per annum during the next ten years, to account for some 9.4 per cent of Gross Domestic Product (GDP) (WTTC 2010).
8. See L. Dwyer, P. Forsyth and W. Dwyer, *Tourism Economics and Policy* (Bristol: Channel View Publications 2010), p. 23.
9. *Ibid*., at p. 23.
10. The UNWTO (1998) has identified 45 different types of taxes, imposed on the tourist in developed and developing countries. These are divided into five broad areas: taxes on airlines and airports, hotel and other accommodation, road transportation, food and beverages, and providers of tourism services.
11. In New York State, to mention a few, this tax is referred to as Sales Tax on Rent for Hotel Occupancy, while in other states, like Vermont, it is referred to as Meals and Rooms Tax. The law provides for a 9.0 per cent on sales of prepared and restaurant meals, 9.0 per cent on sales of lodging and meeting rooms in hotels and 10.0 per cent on sales of alcoholic beverages, served in restaurants. In some other parts, it is referred to as tourist tax, while in the United States, the most encountered tourist tax is the hotel occupancy tax. In many places, this is known as an occupancy tax, but may also be known as a lodging tax, a room tax, a sales tax, a tourist tax, or a hotel tax. Occupancy tax is generally paid by the guest, but the obligation to remit the taxes to the government usually falls on the host.

12. The hotel room tax is a popular tax because it is perceived to be an efficient way to raise tax revenue from non-residents. It was designed to bolster tax revenue, promote tourism and the hotel industry by channelling money realised into projects that lure visitors to the states.
13. There was a Sales Tax Act enacted by the Federal Military Government, which vested the administration of Sales Tax within each State on the State Government. The revenue, from the tax collected by each State, forms part of its Consolidated Revenue Fund and is utilised for its independent purposes at its discretion. See section 7 of the Sales Tax Act, No. 7, of 1986.
14. See: J. K. Naiyeju, Value Added Tax: The Facts of a Positive Tax in Nigeria, (Lagos: Kupag Public Affairs, 1996); C. S. Ola, *Income Tax Law and Practice in Nigeria*, (Ibadan: Heinemann Educational Books, 2001), pp. 583-606; Value Added Tax Act, CAP VI Laws of Federation of Nigeria, 2004, as amended by Value Added Tax (Amendment) Act of 2007, pp. 64-108; E. O. Ogundele, *Value Added Tax (VAT), Theory and Practice*, (Lagos: Libriserve , 1996); A. Sanni and A. Elebiju, *Value Added Tax in Nigeria*, (Lagos: Chartered Institute of Taxation of Nigeria, 2014).
15. See T. A. Olaiya, Implication of Policy Shift from Direct to Indirect Tax Regime in Nigeria, in Sanni, A. and Elebiju A., *Indirect Taxes in Nigeria*, (Lagos: Chartered Institute of Taxation of Nigeria, 2014), pp. 25-63. See also A. Sanni, Value Added Tax in Nigeria, in Sanni, A. and Elebiju A., *Indirect Taxes in Nigeria*, (Lagos: Chartered Institute of Taxation of Nigeria, 2014), pp. 64-126.
16. See, for example, Federal Republic of Nigeria, *National Tax Policy*, (Federal Ministry of Finance, 2017), p. 4. NTP noted specifically that the tax system should focus more on indirect taxes, which are easier to collect and administer and more difficult to evade.
17. Governments are becoming increasingly dependent on inter-governmental transfers, which have been shrinking over time, in part because of the fiscal pressure, created by the global economic slowdown.
18. See A. Elebiju, The Hotel Occupancy and Restaurant Consumption Law, in A. Sanni and A. Elebiju, *Value Added Tax in Nigeria*, (Lagos: Chartered Institute of Taxation of Nigeria, 2014), pp. 150-165.
19. The National Tax Policy (NTP) was first published in 2012, as part of the efforts to entrench a robust and efficient tax system in Nigeria. A policy has been described as a statement of intention that guides the thinking, actions and behaviour towards the achievement of a well-thought-out and laid-down objectives.
20. See Federal Inland Revenue Service (2012). A Comprehensive Tax History of Nigeria, Ifueko Omoigui Okauru (ed.) Ibadan, Safari Books, p, 313. See also, FIRS (2012) Federal Inland Revenue Service and Taxation Reforms in Democratic Nigeria, Ifueko Omoigui Okauru (ed.), Ibadan, Safari Books Ltd., pp. 76-77.
21. See Taxes and Levies (Approved List for Collection) Act (Amendment) Order, 2015. The Federal Government in 2015, amended the Taxes and Levies (Approved List for Collection) Act, Cap. T2, Laws of the Federation of Nigeria, 2004. The Act was previously referred to as Taxes and Levies (Approved List for Collection) Decree, No. 21 of 1998.
22. See *Supra* note 19, at p. 1.
23. Nigeria is governed by a federal system and operates a federal tax system. Namely, the government fiscal power and policy is based on a three-tier tax structure, shared between the federal, state and local governments, with each having different tax

jurisdictions.

24. See O. S. Obatola, *The Rudiments of Nigerian Taxation*, (Lagos: ASCO Publishers, 2013)
25. This was amended in 2004 and renamed Taxes and Levies (Approved List for Collection) Act, CAP T2, Laws of the Federation of Nigeria, 2004.
26. There are seventeen (17) Nigerian tax laws enacted since 1990. With the Taxes and Levies (Approved List for Collection) Act, (Amendment) Order, 2015 Nigeria now has fifty five taxes and levies (as against forty contained in the 1998 Act) shared among the three tiers of government in ratio nine, twenty five and twenty one for the federal government, state governments and the local governments, and information technology levy, vested in the Federal Inland Revenue Service.
27. See *Supra*, note 19, at p. 4.
28. With more than one billion tourists travelling to an international destination every year, tourism has become a leading economic sector, contributing 10% of global GDP and 6% of the world's total exports. Representing more than just economic strength, these numbers reflect tourism´s vast potential and increasing capacity to address some of the world´s most pressing challenges, including socio-economic growth, inclusive development and environmental preserVATion. See UNWTO Annual Report, 2015, p. 10.
29. See *Supra*, note 17, at p. 15.a\a\A
30. See UHY International Ltd. (2014). Doing Business in Nigeria, p. 9.
31. See P. U. Okpoko and V. E. Ali (2012). National Park System in Tourism Development: Yankari National Park, Nigeria, *Bassey Andah Journal*, Vol. 5, p. 28.
32. Nigeria has numerous tourist attractions located in the various parts of the country, although only a few of them are being exploited at present. When fully developed, the sub-sector has the potential of generating significant amounts of foreign exchange.
33. See also: http://www.realhotelier.ng/blog/posts/the-nigerian-tourism-sector-contributed-n1-56-billion-and-1-7-percent-to-the-gdp-in-2014#sthash.8GKyveuJ.dpuf Accessed on ???
34. See Nigerian Tourism Development Corporation Decree 81, LFN 1992, now an Act of Parliament since Nigeria returned to democracy in 1998.
35. See *Supra*, note 24, at S. 4(1) NTDC Act 1992.
36. See J. Mark (2005), Tourist Taxes, in Cordes, J., Ebel, R. O. and Gravelle, J. G. *The Encyclopedia of Taxation and Tax Policy*, (Washington D. C.: The Urban Institute), p. 441. See also *Supra,* note 8, at p. 539.
37. According to *Nigeria Governors' Forum* (2015):
    The components (sources) of IGR to States include tax revenues, non-tax revenues, and other
    miscellaneous sources. Tax revenues include PAYE, direct assessment, withholding tax, property
    tax, capital gains tax for individuals, sales or consumption tax, pool betting taxes, lottery and
    casino taxes, business premises and registration fees, development levies for taxable individuals,
    fees for right of occupancy on urban land, owned by the State government, market taxes and
    levies. (p. 16).

38. See *Daily Trust*, http://www.dailytrust.com.ng/sunday/index.php/28-sunday-trust-magazine/community-news-oodua/5141-consume-more-pay-more-tax-in-lagos-hotelsrestaurants#XDO32ASjG1zdydlX.99, April 9, 2010.
39. See *Supra*, note 36, at p. 422. See also *Supra,* note 8, pp. 557-560.
40. The law was assented to by the State Governor, Mr. Babatunde Fashola, in June 2009. It imposes tax on goods and services or items, consumed in hotels, event centres and restaurants within the state.
41. See *Supra*, note 8, at p. 540.
42. See *Supra,* note 8, at p. 24.
43. In some other places, hotel occupancy tax is required on a per-person, per-night basis.
44. Author and title of article???
http://www.un.org/esa/sustdev/natlinfo/indicators/methodology_sheets/econ_development/tourism_contribution.p Accessed on ???
45. Oxford Economics, *The Economic Contribution of the UK Hospitality Industry*, a Report prepared by *Oxford Economics* for the British Hospitality Association, September 2015.
46. *Ibid*., at p.5.
47. See *Nigeria Governors' Forum (2005)*:With commodity prices falling below what is required to balance budgets in many countries, the search for alternative and/or complementary sources of revenues is likely to intensify in the years ahead. This is more so for Nigeria and the component States. (p. 4).
48. See *Supra,* Note 32, at p. 8.
49. Mr. Babatunde Raji Fashola, SAN (2007-2015).
50. *Daily Trust*, 9thApril, 2010, p. 1.
51. *Ibid.,* at p. 2.
52. See S. 7 of the Sales Tax Act No. 7 of 1986.
53. See A. Sanni, Current Law and Practice of Value Added Tax in Nigeria, *British Journal of Art and Social Sciences,* 2012, 5(2): 186-210.
54. See B. D. Olumide, Sales Tax in Nigeria, in Sanni, A. and Elebiju A., *Indirect Taxes in Nigeria*. (Lagos: Chartered Institute of Taxation of Nigeria, 2014). p. 127.
55. On 22nd June, 2009, the Executive Governor of Lagos State signed the Hotel Occupancy and Restaurant Consumption Bill into law, following passage by the State House of Assembly.
56. Lagos State government, in its quest to bring development to the door-steps of the people and free some part of the state for further development, introduced some local taxes, which include the hotel occupancy and restaurant consumption Tax Law.
57. The term **hotel** is defined under the Law to include motels, guest houses, and apartments for short-time letting, while **restaurant** is defined to include any food-sale outlet, bar tavern, inn or café, whether or not located within a hotel. **Events centers,** on the other hand, are defined under the Law to include halls, auditoriums, fields, and places designated for public use at a fee.
58. See S. 3 of the Lagos State Hotel Occupancy and Restaurant Consumption Tax Law.
59. See S. 7of the Lagos State Hotel Occupancy and Restaurant Consumption Tax Law.
60. See s. 13 of the Lagos State Hotel Occupancy and Restaurant Consumption Tax Law.
61. See *Supra,* note 19, at p. 151.
62. See S. 11(1) of the Lagos State Hotel Occupancy and Restaurant Consumption Tax Law.

63. See S. 11(2) of the Lagos State Hotel Occupancy and Restaurant Consumption Tax Law.
64. See the Hotel Licensing Law, Cap H.6, Laws of Lagos State of 2003.
65. See the Hotel Licensing (Amendment) Law, No. 23, Vol. 43, Lagos State of Nigeria official Gazette, July 2010.
66. See the Hotel Occupancy and Restaurant Consumption Law, No. 30, Vol. 42, Lagos State of Nigeria official Gazette.
67. See J. J. Odinkonigbo and N. Ikeyi (2015). Is the Power of a State to Impose Sales Tax in Nigeria Fettered by the imposition of Value Added Tax by Federal Government, *Commonwealth Law Bulletin* 41(4):577 – 596.
68. See *Supra,* Note 17, at pp. 153-154.
69. *Ibid*., at p. 557.
70. See Mas Everest Hotels Limited & Anor v. AG of Lagos State & Anor, ID/40M,2009, *ALL NTC*, pp. 93-1105.
71. See [2003] *3 NWLR (Pt. 650)*, 565. The Court relied on 7Up Bottling Company Plc v. LSIRB, where the Court of Appeal held that, although the employer was the statutory agent for collection and remittance of personal income taxes of its employees, pursuant to Pay-As-You-Earn (PAYE) scheme, the employer had no locus to complain, if its employees were wrongly assessed. It is the employee who directly bears the personal income tax burden that could validly challenge the Revenue.
72. See *Supra,* note 69, at p. 100.
73. Registered Trustees of Association of Fast Food Confectioners of Nigeria & 2 Ors v Attorney-General Lagos State & Federal Inland Revenue Service.
74. See Suit No. FHC/L/CS/747/2009, *7 ALL NTC.*
75. See *Ibid.,* at p. 59
76. See *Ibid.,* pp. 12-13.
77. Nay: Princel Court – Princel Court Limited v. Attorney General of Lagos State & 2 Others,*FHC/L/CS/851/2009,* was filed also by originating summons on 8thAugust, 2009.
78. In the exercise of its powers to impose any tax or duty on – (a) capital gains, incomes or profits of persons other than companies, and (b) documents or transactions by way of stamp duties, the National Assembly may, subject to such conditions, as it may prescribe, provide that the collection of any such tax or duty or the administration of the law imposing it, shall be carried out by the Government of a State or other authority of a State.
79. Where an Act of the National Assembly provides for the collection of tax or duty on capital gains, incomes or profit or the administration of any law by an authority of a State, in accordance with paragraph 7 hereof, it shall regulate the liability of persons to such a tax or duty in such manner as to ensure that such a tax or duty is not levied on the same person by more than one State.
80. See the case of Attorney-General Ogun State v. Aberuagba [1985] *1 NWLR (pt. 3)*, 395. See also Attoney-General,Abia State &Ors. v Attoney-General, Federation [2002] *6 NWLR(Pt. 763),* 264.
81. See Lagos State Board of Internal Revenue v Eko Hotel Ltd. & Anor, [2008] *All FWLR (Pt. 398)* 235.
82. See *Ibid*., pp. 222-223.
83. See Section 4(5), Constitution of the Federal Republic of Nigeria.

84. See Section 9 Hotel Occupancy and Restaurant Consumption (Fiscalisation) Regulation (2017)
85. See FHC Order and Ruling with Suit No: FHC/L/CS/360/2018. The RTHMAL further approached the court by an originating summons to challenge the validity of the consumption tax imposed by the Lagos State Internal Revenue Service (LIRS) pursuant to the Hotel Occupancy and Restaurant Consumption Law 2009 and its subsidiary Regulations published in 2017.
86. See Supra note 81.
87. See *Supra* note 21.
88. The Registered Trustees of Hotel Owners and Managers Association v. A.G., Lagos State and the Federal Inland Revenue Service (Suit No.: FHC/L/CS/360/2018)
89. In the case, the Attorney General of the Federation invoked the original jurisdiction of the Supreme Court to declare three laws enacted by the Lagos State House Assembly null and void. The laws sought to be invalidated are: the Hotel Licensing Law, Cap H.6, Laws of Lagos State of 2003; the Hotel Licensing (Amendment) Law, No. 23, Vol. 43, Lagos State of Nigeria official Gazette, July 2010; the Hotel Occupancy and Restaurant Consumption Law, No. 30, Vol. 42, Lagos State of Nigeria official Gazette.
90. See T. Oyedele, *Nigerian Tax Alert*, July 2013, at p.2.
91. See Second Schedule, Legislation Power, *the Constitution of the Federal Republic of Nigeria (Promulgation) 1999,* No. 24, at p. A1059.
92. See Hon. Minister for Justice and Attorney-General of Federation v. Hon. Attorney-General of Lagos State,*12 TLRN*, at p. 92.
93. *Ibid*., at p. 92.
94. Item 68 states, any matter incidental or supplementary to any matter mentioned elsewhere in this list, p. A1060.
95. See *Supra*, note 65, at p. 114.
96. See *Supra,* note 65, at p. 104.
97. See *Supra* note 17.
98. Supra Note 90
99. See Supra note 64.
100. See Supra note 66.
101. See *Supra,* note 70, at p. 3.
102. See O.K. Obayemi (2014). Tax Litigation in Nigeria and a Review of Recent Nigerian Court Decisions on Taxation, *Research Journal of Finance and Accounting,* 5(24), p. 168.
103. The Policy recommends deliberations between the parties under the auspices of different platforms, including the Nigeria Governors' Forum, the National Economic Council, the Federal Executive Council, and the meetings of the Council of States. Where deliberations at any, or all of these fora fail, the Policy recommends mediation by the other State Governments, or Federal Government Agencies, or by other arms of Government, such as the Judiciary.

CHAPTER 16

A CRITICAL REVIEW OF A. G. LAGOS STATE VS. EKO HOTELS LIMITED & ANOR.

Abstract

Nigeria is professed to be a federation which suggests the practice of fiscal federalism amongst the federating units. Therefore, each of the federating units ought to have clearly defined fiscal power within the federal structure. The enactment of the Value Added Tax (VAT) Act by the National Assembly has generated the arguments around fiscal federalism. The challenge to the constitutionality of the VAT Act forms the substance of the suit instituted by the Lagos State Government as contained in this case under review. This chapter therefore makes a critique of the Supreme Court's decision on the validity of the VAT Act as it affects the fiscal legislative power of the States within the federation. This no doubt has thrown up fundamental legal issues including the doctrines of covering the field, the concept of double taxation, the pith and substance principle as well as the assumption of the validity of the constitutionality of a statute form the key issues discussed in this chapter.

1. Introduction

The constitutionality of Nigeria's Value Added Tax ("VAT")[1] Act and the legislative competence of its National Assembly to enact the Act has attracted the attention of both legal and academic stakeholders in recent times. Even when the opportunity presented itself for the country's Supreme Court to pronounce on the issues, the substance of the case was not dealt with as the case was decided on the issue of the jurisdiction of the Supreme Court to hear and determine the case.[2] The discourse has been extended to the critical challenge against the legislative competence of the State House of Assembly in enacting their Sales Tax Laws[3] (and the application of the said law especially from the extractive companies and manufactures of goods and services in Nigeria. Manufacturers, suppliers and some taxpayers have argued[4] that since the National Assembly has enacted the VAT Act, there is no basis for State governments to enact the Sales Tax Law as it would amount to double taxation on consumption. It is within this context that we need to examine the decision of the Supreme Court of Nigeria in ***Attorney General of Lagos State v. Eko Hotel International Plc & Anor.***[5]

Essentially, this paper reviews the Supreme Court's judgment of 8th December, 2017 with a view to understanding the legal issues and the bases for the apex court's conclusions. Ultimately, this author shall state his opinion on the policy implications of the judgment. In

so doing, effort is made at analysing the factual circumstances in the case and the legal doctrine of covering the field and the concept of double taxation.

2. Factual background

Pursuant to an Originating Summons filed by on 5th March, 2004, the 1st Respondent (Eko Hotel suing as the Plaintiff) by way of Interpleader Summons sought a determination by the Federal High Court on which, between the Federal Inland Revenue Service (2nd Respondent sued as the 2nd Defendant) or the Lagos State Government (Appellant sued as 1st Defendant) should monies collected as tax from its consumers be paid to. The question was raised in light of the provisions of section *1, 2, 10, 11, 12, 13, 14 and 16 of the VAT Decree No. 102 of 1993 and sections 1, 2, 3, 4, 5 and 6 of the Sales Tax Law, Cap.175 and Sales Tax (Schedule Amendment) Order 2000 of Lagos State.*

Specifically, Eko Hotel sought the following reliefs:

a. A declaration the plaintiff can only be a "taxable person" or remitting agent in respect of the amount due as tax on its sales to consumers to a single body or agency and not to state and Federal agencies together.
b. An order that the Plaintiff is not entitled to pay or remit tax on its sales to its consumers to the defendants until the rightful body to collect same is determined.
c. An amount directing the Plaintiff to pay the amount due as tax on its sales to its consumers to a dedicated account until the rightful body to collect same is determined.

The Originating Summons was supported by a 16-paragraph Affidavit deposed to by the Company Secretary/Legal Adviser (the Deponent) of Eko Hotel. In the Affidavit, the Deponent clearly portrayed the dilemma which the hotel found itself. Lagos State and FIRS filed Counter-Affidavits in opposition to the Originating Summons. Lagos State also filed a Counterclaim and Preliminary Objection challenging the Court's jurisdiction to hear the suit. Lagos State however withdrew the Counterclaim and the court struck it out accordingly.

The Preliminary Objection was heard alongside the substantive suit. The learned trial judge dismissed the Preliminary Objection and held that the Federal High Court had jurisdiction to entertain the suit. It also held that the 1st Respondent could only be a "taxable person" or remitting agent in respect of the amount due as tax on its sales to its consumers to a single agency, which is FIRS.

Dissatisfied with the decision, Lagos State appealed to the Court of Appeal. In a judgment delivered on 13th July, 2007, the Court of Appeal dismissed the appeal and affirmed the decision of the trial court. Principally, it held that the provisions of VAT Act and Sales Tax Law would amount to double taxation. Additionally, the Court reasoned that since the VAT Act has covered the field legislated upon by the Sales Tax Law, Lagos State law must give way. Further, aggrieved by the decision of the Court of Appeal, Lagos State appealed to the Supreme Court. The Supreme Court affirmed the lower courts' decision and consequently

dismissed the appeal. This decision forms the focus of this review.

3. Key Legal Issues Considered by the Apex Court

From the 5 grounds of appeal filed on 2nd April, 2008, learned counsel for the Appellant, Lagos State Government, distilled 5 issues for determination. The 2 issues[6] relevant to this critique are:

a. Whether the lower court was right when it held that the VAT Act has covered the field of Sales Tax and its (VAT Act) provisions prevail over the Sales Tax Law of Lagos State (the "**Covering the Field Issue**").

b. Whether the Court below was right when it held that imposition of both VAT and Sales Tax will create double taxation (the "**Double Taxation Issue**").

Summary of Parties' Submission on the Covering the Field Issue.

Appellant's Submissions:

Lagos State Government questioned the application of the doctrine of covering the field to the facts and circumstances of the appeal. It relied on the Supreme Court decisions in ***A.G. Abia State vs. A.G Federation***[7] and ***INEC vs. Musa***[8] to contend that the legislative competence of the National Assembly to enact VAT Act must be resolved first in applying the doctrine. The provisions of **Section 4(2), (3), (5), (6) and (7) of the 1999 Constitution** with the particular emphasis on the phrase *"any law **validly** made by the National Assembly"* were cited and reviewed as well as the textbook, ***Federalism in Nigeria Under the Presidential Constitution*** *by Prof. Ben Nwabueze.*

Referring to **section 2 of the VAT Act**, Lagos State argued that what triggers liability under the Act is the "*supply of goods and services*" and that "*supplies*" is defined in *Section 42 of the Act* to mean:

> *"any transaction, whether it is the sale of goods or the performance of a service for a consideration that is for money or money's worth"*

Lagos State Government submitted that VAT has a very broad base compared to other taxes, which exempts certain persons, companies and institutions from liability. It further submitted that, where VAT is concerned, the location of supplier and consumer are immaterial as it applies to international, inter-state and intra state transactions / supplies throughout Nigeria. While Lagos State conceded that the Federal Government has incidental sales taxing power in respect of trade and commerce, it posited that the power is incidental and limited only to the exclusive power of the National Assembly over international and inter-state trade and commerce. Lagos State contended that the National Assembly does not have the competence to make any law on intra-state trade and commerce and therefore cannot impose tax on intra-state transactions / supplies, which the VAT Act appears to have covered. Lagos State argued that by imposing VAT on intra-state transactions supply of

goods and services, the Act has exceeded the powers of the Federal Government under the Constitution to impose VAT. Reference was made to the Supreme Court decision in ***Fawehinmi vs. Babangida***.[9]

Lagos State Government concluded its submission that, the issue of having identical legislations on the same subject matter does not arise and therefore the doctrine of covering the field was not applicable to justify supremacy of the VAT Act over the Sales Tax Law of Lagos State. It questioned the misapplication of the doctrine of covering the field with the legislative competence of the National Assembly to enact the Law with heavy reliance on ***A.G Abia State vs. A.G Federation*** (*supra).* Lagos State submitted that where the National Assembly lacks legislative competence, the State law prevails as that would not violate the inconsistency rule as enshrined in section **3(1) of the 1999 Constitution**.

Respondents' Submissions:
Eko Hotel (1st Respondent) submitted that the constitutionality or validity of VAT was not in issue in the Court below. It further submitted that VAT and Sales tax are the same, as the incidence on both taxes is on the consumer and the tax is charged on consumable items as stated in the schedules to both laws. It contended that the rates and goods upon which the charges are made are the same. It was submitted that the lower court was right to have relied on the case of ***A.G Ogun State vs. Aberuagba*** *(1985) 1NWLR (Pt. 3) 395* in reaching the conclusion that the VAT Act had covered the field on matters dealt with by the Sales Tax Law of Lagos State. It was further argued that the decisions of ***A.G Abia State V A.G. Federation*** *(Supra) and* ***Fawehinmi vs. Babangida*** *(Supra)* relied upon by Lagos State were inapplicable to the facts of the case.

FIRS (the 2nd Respondent) argued that the Value Added Tax Decree which was promulgated into law by the Federal Military Government for the entire nation remained in force with amendments until the coming into effect of the 1999 Constitution and is therefore an existing law deemed an Act of the National Assembly by virtue of ***section 315 (a) & (b) of the said 1999 Constitution***. It was further argued that ***section 4 of the 1999 Constitution*** guarantees the power of the National Assembly to make laws on the items in the Exclusive and Concurrent Legislative List and that by virtue of ***Item 7 Part II*** thereof, the National Assembly is empowered to make laws on collection of taxes. It contended that VAT is a tax payable on goods and services all over Nigeria and that all tiers of government, including Lagos State are beneficiaries of the proceeds. It contended that Lagos State whilst still a beneficiary of the Act, cannot approbate and reprobate by complaining about the same law. It also relied on the provisions of **Section 4(5) of the Constitution** and submitted that since the VAT Act is a "**valid law of the National Assembly**", the Sales Tax Law of Lagos State is void to the extent of its inconsistency therewith. It also relied on the same *Aberuagba's case* and ***Nigerian Soft Drinks Ltd v Lagos State*** *(1987) 2 NWLR (Pt. 57) 444;* ***Lakanmi & Anor v A.G. Western Nigeria*** *(1970) NSCC 143 at 144* and ***A.G Abia State v A.G Federation*** *(supra) at 431, B-E.* In conclusion, it maintained that the VAT Act, as currently administered by the FIRS, has already covered the field sought to be regulated by the Sales Tax Law of

Lagos State.

Summary of Parties' Submission on the Double Taxation Issue

Appellant's Submissions:
Lagos State submitted that double taxation might arise in two instances: the first is the imposition of two taxes on the same property, taxpayer or profit or goods during the same period, by one taxing authority; while the second is the imposition of comparable taxes in two or more States on the same tax payer for the same subject or identical goods. Reference was made to the **Black's Law Dictionary**, 8th edition. It was submitted that neither situation existed in this case. It was further contended that except the VAT Act can validly impose tax on the same subject as the Sales Tax Law, the issue of double taxation would not arise.

Lagos State further argued that the VAT Act is unconstitutional and invalid to the extent of its inconsistency with **Item 7 of Part II** of the concurrent Legislative List. It argued that the tax imposed by VAT is a consumption tax levied on the value added to a product in the course of production and is different from capital gains tax, nor does it qualify as income or profits of persons other than companies. It argued further that it is also not a levy on documents or transactions and that the two legislations are distinct and enacted by separate legislative bodies. It submitted that even if the issue of double taxation was to arise, it was not for the consumer to determine which law to obey without first seeking to invalidate one.

Respondents' Submissions:
Eko Hotel submitted that in so far as the objectives of the two taxes are the same and the incidence of the taxes is on the consumer, the Court below was right to have held that the imposition of both taxes would create double taxation since the VAT Act is still an existing law by virtue of **Section 315(1) of the Constitution** and the absence of any decision invalidating it. It referred to the ***Aberuagba's case*** (supra).

2nd Respondent noted that the Sales Tax Law of Lagos State (Schedule Amendment) Order 2000, having imposed tax on the same goods and services and at the same rate of 5% as VAT, it would amount to double taxation as the actual payer of the taxes in both cases is the same consumer of the goods and services. It contended that the VAT Act was enacted to correct the mischief and defects of the Sales Tax Laws which were prior in existence and to protect tax payers from double taxation. It submitted that VAT sought to compensate the States from the abrogation of the Sales Tax Laws by making provision in **Sections 21 and 22 of the VAT Act** for the involvement of State Governments in the administration of the tax. It also referred to **Section 40 of the VAT Act** which sets the formula for distribution of revenue accruing by virtue of the operation of the Act wherein the State Governments receive 50% and the Local Government 35% of the generated revenue. He also referred to **Section 36 of the VAT (Amendment) Act 2007** and maintained that Lagos State, beneficiary of the VAT Act cannot be heard to complain.

Summary of the Supreme Court's Decision:
In its evaluation of the Covering Field Issue, the Court examined the application of the doctrine of covering the field as it relates to the powers of the National Assembly and State Houses of Assembly to make laws. The Court relied on the words of His Lordship Kayode Eso in **A.G Ogun State V A.G Federation** (1982) NSCC (Vol.13) 1 @ 35 Line, 18-30 thus:

> "*I take the view that when one considers the doctrine, the phrase Covering the field means precisely what it says. When the matter legislated upon is in the concurrent list and the Federal Government has enacted a legislation in respect thereof, where the legislation enacted by the State Government is inconsistent with the legislation enacted by the Federal Government, it is indeed void and of no effect for inconsistency. Where however the legislation enacted by the State Government is the same enacted by the Federal Government where the two legislations are in parimateria, I respectfully take the view that the State legislation is in abeyance and becomes inoperative for the period the Federal Legislation is in force. I will not say it is void. If for any reason the Federal Legislation is repealed, it is my humble view that the State legislation which is in abeyance, is revived and becomes operative until there is another Federal Legislation that covers the field."*

The Court went further to examine **section 4(5) of the 1999 Constitution** (as amended) but stated that the issue in dispute was not the constitutionality of the Sales Tax Law of Lagos State nor the validity of the VAT Act. The Court went further to state that in the absence of any relief challenging the legitimacy of the VAT, the only issue the Court is confronted with on this point was whether as the law stood at the time the cause of action arose, the money already collected by the 1st Respondent under the VAT Act should be remitted to the 2nd Respondent rather than the Appellant, as there is no issue from the Appellant seeking to invalidate the VAT Act.

The Court went on to state that Section 2 of the VAT Act provides that the tax to be charged and payable on goods and services is as set out in Column A of Schedules 1 and 2 of the Act. Section 1 of the Sales Tax Law of Lagos State makes similar provision, and the goods and services charged under the different legislations are the same. It follows that the VAT Act has effectively covered the field in that regard. The Court concluded by stating that even if the Lagos State House of Assembly has the requisite legislative competence to enact the Sales Tax Law, which is not an issue before the Court, once an existing Federal law or Act of the National Assembly has covered the field, the Act of the National Assembly or such existing Federal law must prevail.

On the Double Taxation Issue, the Court addressed the arguments of parties and held that since the VAT Act remains an existing law it has covered the field on Sales tax and therefore prevails over Lagos State Sales tax (Schedule Amendment) Order 2000. The Court agreed with the Respondents and concluded that:

> *Not only do both legislations cover the same goods and services, they are*

> *also targeted at the same consumer. The tax has already been collected by the 1st Respondent pursuant to the VAT Act. When a dispute arose as to which of the two claimants the tax collected should be remitted to, it rightly approached the court for direction. There is no doubt in my mind that it would amount to double taxation for the same tax to be levied on the same goods and services, payable by the same consumers under two different legislations.*[10]

The Supreme Court consequently affirmed the decision of the Court of Appeal which held that the trial court was right in holding that Eko Hotel can only be a remitting agent to a single body and not to both State and Federal Governments at the same time.

Implication of the Judgment

The judgment, as presently constituted is not without its legal and fiscal implications some of which are listed hereunder:

a. It may send a wrong signal to the Federal Legislature that, irrespective of its legislative limit, once it makes a law on a matter that covers the field, the State Legislature cannot legislate on such matter (which is within its competence) and if it is done, the said State law will remain in abeyance;
b. The judgment is also understood to have decided that, in applying the doctrine of covering the field, a party needs to challenge the validity of the Act of the National Assembly in question before the Court can consider it;
c. An entity or taxable person cannot be a remitting agent for more than one tax authority on the same subject matter even when the enabling law of the other tax authority is exercised within its constitutional legislative competence;
d. The hope of a true fiscal federalism whereby the taxing powers are shared between the Federal Government and the Federating States may be unachievable as it will be difficult, if not impossible, for States Governments to exercise control over the transactions or supply of goods and services within their geographical territories (intra-state supplies).[11]
e. Irrespective of the "pith and substance" of a tax law on a particular subject matter, no two tax authorities can impose similar tax on the same subject as doing so would amount to double taxation.

It should be mentioned that there were other issues decided by the Supreme Court, however this Chapter focuses on the Covering the Field Issue and the Double Taxation Issue.

4. Analysis of Legal Issues Arising from the Final Judgment

For the purpose of this analysis, multi-dimensional legal points have been identified to show whether the decision of the apex court on the two issues under consideration are faulty or otherwise. In this analysis, effort is also made to review some procedural steps taken by Counsel representing both parties. The multi-dimensional legal points are:

a. The application of doctrine of covering the field in a federal structure; and

b. The presumption of constitutionality of the VAT Act
c. The concept of double taxation and principle of avoidance of double taxation in construction of taxing statutes
d. The concept of pith and substance of the VAT Act and the Sales Tax Law

Misapplication of the Doctrine of Covering the Field

In arriving at its decision justifying that both the VAT Act and the Sales Tax Law of Lagos State would amount to double taxation, the Supreme Court in the lead judgment delivered by Kekere-Ekun JSC applied the "doctrine of covering the field" to hold that:

> *It follows that VAT Act has effectively covered the field in that regard. Section 7(1) of the Act provides that the tax shall be administered by the 2nd respondent. In the circumstances, I am in complete agreement with the court below, which affirmed the finding of the trial court, that the VAT Act having covered the field on the issue of sales tax, its provisions prevail over the provisions of the Sales Tax Law of Lagos State. Thus, even if Lagos State House of Assembly has the requisite legislative competence to enact the Sales Tax Law, which is not an issue before us, once an existing Federal Law or an Act of the National Assembly has covered the field, the Act of the National Assembly or such existing Federal law must prevail.*[12]

Concurring with the lead judgment, His Lordship, M.D. Muhammad, JSC, complemented the lead judgment in further substantiating the decision, introduced the constitutional point and relied on Section 4(5) of the 1999 Constitution (as amended). The Court held on Page 555 that:

> *The two legislations the Value Added Tax and Sales Tax Law of Lagos State, given their schedules, dwell on the d same subject matter, to wit, tax on consumable items payable by customers. By virtue of Section 4(5) of the 1999 Constitution (as amended) the Value Added Tax Act is deemed to have covered the field and excludes the operation of the sales tax law of Lagos State being State law. Learned Appellant's Counsel simply cannot be right to insist that the State law still operates notwithstanding the clear provision of Section 4(5) of the Constitution which provides to the contrary. The principle is that the Value Added Tax Act that has provided for the very tax the State Sales Tax Law provides "covers the field" putting the latter in abeyance and inoperative.*

Of particular importance to this paper is the contribution of His Lordship, Eko, JSC as he articulated the constitutional origin of the doctrine of covering the field. His Lordship's summarized as follows:

> *The constitutional doctrine of "covering the field" only applies in a federal set up where legislative powers are shared between the central government and the federating units / State Governments.*

The Court went further to quote copiously the provision of Section 4(1 - 7) of the 1999 Constitution clearly showing how powers are shared in the Nigerian federal structure. In presenting this critique, it is fundamental to re-examine the provision of Section 4(2), (5) and (7) of the 1999 Constitution as amended which the Court had cited as the constitutional origin of the doctrine of covering the filed. The section provides:

4(2) The National Assembly shall have power to make laws for the peace, order and good governance of the federation with respect to any matter included in the Exclusive Legislative List shall, save as otherwise provided in this Constitution, be to the exclusion of the House of Assembly of States

*(5) If any law enacted by the House of Assembly of a State is inconsistent with **any law validly made by the National Assembly**, the law made by the National Assembly shall prevail, and that other law shall be to the extent of the inconsistency be void.*

(7) The House of Assembly of a State shall have power to make laws for the peace, order and good governance of the State or any part thereof with respect to the following matters, that is to say:

(a) any matter not included in the Exclusive Legislative List set out in Part I of the second Schedule to this Constitution;

(b) any matter included in the Concurrent Legislative List set out in the first column of Part II of the Second Schedule to this Constitution to the extent prescribed by in the second column opposite thereto; and

(c) any other matter with respect to which it is empowered to make laws in accordance with the provisions of this Constitution.

By Section 2(2) of the 1999 Constitution (as amended), Nigeria as a sovereign state, is a federation comprising of states and federal capital territory. This necessitates the sharing of powers amongst its federating units as provided in Section 4 referred to above. The Courts have always adopted relevant principle of construction to interpret the Constitution and determine the intention of the legislature. One of these principles of construction is literal rule which dictates that the words used in a statute are given its literal meaning where it is clear and unambiguous. The Supreme Court harped this point in ***I.M.B. v. Tinubu,***[13] Court ***per Iguh JSC*** where the relevant guiding approach for interpreting constitutional provisions was reinstated as follows:

> *... it will be necessary to recall the general principle of law governing the interpretation of our Constitution. This is that such interpretation as would serve the interest of the Constitution and best carry out its objective and purpose should be preferred. Its relevant provisions must be read together and not dis-jointly and where the words of any section are clear and unambiguous, they must be given their ordinary meaning unless this would lead to absurdity or be in conflict with other provisions of the Constitution" (emphasis added)*

The Supreme Court had stated that the issue in the appeal under review is neither about constitutionality of the Sales Tax Law nor the validity of the VAT Act but it proposed to apply the doctrine of covering the field as it is sourced from the provision of Section 4 of the Constitution. Though this finding appears to be the position considering the pleadings of the parties to the appeal but as a matter of fact, Lagos State indeed questioned the validity of the Act both at the Court of Appeal and Supreme Court in arguing the inapplicability of the doctrine of covering the field.

Turning to Section 4(5) of the Constitution which the Court had applied, it must be stated that the section qualifies the basis for which the doctrine of covering the field would apply. This can be found in the phrase ***"inconsistency with ANY LAW VALIDLY MADE by the National Assembly***" For the Supreme Court to apply the doctrine of covering the field in the light of the VAT Act and Sales Tax Law of Lagos State, the two-prongs approach prescribed by the Constitution must be observed. The first is the inconsistency approach and the second is the discovery of the validity of the VAT Act. Instead of the Court to observe these two approaches, it applied the doctrine of presumption of validity which deemed the VAT Act as being validly made without basis.

With due respect and sense of humility to their Lordships, a community reading of Section 4(2), (5) and (7) of the 1999 Constitution clearly indicates that both the National Assembly and State House of Assembly have a list of items upon which they have power to legislate exclusively. They also have list of items on the legislative list which both of them share. The exclusive list is reserved for the National Assembly while the concurrent list is shared by both the National Assembly and State House of Assembly. As decided by the Supreme Court in ***A.G. Lagos State v A.G. Federation***[14] per Kalgo JSC, those items not mentioned in either exclusive or concurrent list is exclusively reserved for the State House of Assembly. The Court held:

> *Nigeria is no doubt a federal republic with a federal constitution in which the legislative powers of the federal Government through the national Assembly and the legislative powers of the State Government through the State Assemblies were clearly defined. These consists of the Exclusive Legislative List on which only the National Assembly can legislate; the Concurrent legislate List which is shared between the National Assembly and the State Assemblies and the remaining which is called the residual list not included in the Exclusive or Concurrent List which only the State Assemblies can legislate on.*[15]

For the doctrine of covering the field to be applicable, the Supreme Court ought to have considered the **"validity of the VAT Act".** This is because the provision of **Section 4(5) of the Constitution** that warehouses the doctrine of covering the field makes "**validity**" as the standard threshold for the doctrine to apply. Of course, there may be the argument that a court is not permitted to decide an issue not raised or in dispute between parties. This argument is however weak in the face of the constitutional requirement for inconsistency and validity of

the Act of the National Assembly. It is therefore submitted that the Supreme Court was wrong to have applied the doctrine of covering the field without first ascertaining the validity of the VAT Act. In ascertaining the validity of the VAT Act, the Supreme Court would have considered whether the "sales or supply of goods and services" fall within the Exclusive Legislative List of the National Assembly or the Residual Exclusive List[16] of the State House of Assembly or the Concurrent Legislative List for both Legislature.

One therefore finds it irresistible to submit that if the Supreme Court had considered the validity of the VAT Act, it would have found as a fact one of the following, that:

a. Consumption (sales and supply of goods and services) is neither listed in the Exclusive Legislative List nor contained in the Concurrent Legislative List.
b. Item 62(a) of the Exclusive Legislative List which provides for trade and commerce is only in respect of international and inter-states transaction; and not intra-state transactions.
c. The VAT Act can only be valid to the extent that it provides for international and inter-states sales and supply of goods and services.
d. Sale Tax Law of Lagos State can only be applied to transactions or supplies made within the geographical territory of Lagos State.
e. There can be a situation where a taxable person can actually be a remitting agent for more than one tax authority at the Federal, State and or Local Governments level depending on the pith and substance of the taxes imposed.
f. The pith and substance of VAT Act and Sales Tax Law are not the same as the two legislations cannot amount to double taxation

This position will be in tandem with the recently adopted Prof. Abiola Sanni's Commission Report on the National Tax Policy 2017, by the Federal Government of Nigeria. This tax policy recognizes the powers of the State Government to impose taxes on transactions within their State in view of the fiscal federalism principle.

The Validity of the VAT Act cannot be Presumed

It is settled principle of construction of statute that if certain provisions of the law construed one way would make them consistent with the Constitution and another interpretation would render them unconstitutional, the court would lean in favour of the former construction. Please see ***Compare R (on the application of Rusbridger) v Attorney General***.[17] The basis of the rule is the assumption that the intention of the legislature is not to violate the constitution. The Supreme Court had presumed that the VAT Act was validly made and consequently did not bother to consider its constitutionality or validity on the ground that it was not an issue in dispute between the parties.

The law is settled that where the word "any" is used in a statute, it means that the class of matters specified after the word "any" has no limitation. In ***NURTW. vs. Ogbodo,***[18] *Niki*-Tobi JCA (as he then was) succinctly posited that "*the word "**any**" means one indefinitely, no matter which. In the context, the word covers all actions without exception. The word extends*

and expands all possible actions on the part of a plaintiff".Interestingly, the Supreme Court approved this principle of the law in its earlier decision, ***Texaco Panama Inc vs. Shell Petroleum Development Corporation of Nig Ltd***[19], per Kalgo, JSC, where it was held that:

> *The word "any" is not restrictive or limited in its application. It includes all things to which it relates or of the thing mentioned.*[20]

In the instant case under review, the word "any" is used the before the phrase "law validly made by the National Assembly" in Section 4(5) of the Constitution. It would appear that the Court, in this judgement, did not consider the word "any" as it qualifies the validity of the Act of National Assembly i.e. VAT Act. The Supreme Court had risen to the occasion to condemn editing the clear provision of a rule or statute let alone the Constitution in ***Olley v Tunji***[21] per Ngwuta JSC, where His Lordship had this to say:

> *The Court had no business editing the clear provision of the rules in the pretext of abandoning technicality in preference to substantial justice.*[22]

The Supreme Court obviously omitted to consider the word **"any"** used before the word "law validly made by the National Assembly" thereby edited the requirement for validity test and consequently presumed the validity of the VAT Act without a hearing on the 'validity' question. This again is at variance with the Latin expression ***"ex nihilo, nihil fit"*** (translated, nothing comes from nothing) which in this context would mean that in the absence of the validation of the VAT Act, its validity cannot exist. It is arguable that adherence to the principle that a party has to raise an issue and or join issues against another before the court can adjudicate on it is a mere technicality. It is respectfully submitted that it is arguable that the application of presumption of validity or constitutionality is not open to the Supreme Court in favour of the VAT Act as **Section 4(5) of the Constitution** makes the "validity" as a standard rule.

The Pith and Substance of the VAT Act Ought to Have Been Applied

As a general statutory interpretation principle in any federal structure, the Pith and Substance doctrine" is well entrenched which was evolved by the Privy Council to ascertain the constitutionality of statutes regarding the violations of the rules of the distribution of powers. This was first developed by the Privy Council when considering Canadian and Australian statutes.[23] The Indian government followed this doctrine since 1935. The Pith and Substance Principle simply states that, where there are irreconcilable conflicts on inconsistency, to apply the Supremacy Rule, competing legislative houses would have their legislative competences determined based on the "nature and content of the legislation".

It is arguable that if the validity of the VAT Act had been considered as required by Section 4(5), the Supreme Court in presuming the validity of the VAT Act did avert its mind to the "pith and substance[24]" of the VAT Act. The Court ought to have considered the presumption in the context of the Exclusive Legislative List and Concurrent Legislative List in the Second Schedule of the 1999 Constitution. The function of the Legislative Lists is not only to confer powers but also to demarcate the legislative fields.[25] The entries in the Lists are only legislative heads or fields of legislation, and the power to legislate is given to the appropriate

Legislature by Section 4. In the instant case under review, the Supreme Court simply held that the VAT Act is an existing Act of the National Assembly under Section 315 of the Constitution with wide application throughout Nigeria and having been so, it remains valid. Interestingly, the Supreme Court appears to have presumed the validity of both the VAT Act and Sales Tax Law but closed its eyes to the inconsistency requirement as of Section 4(5) of the Constitution which can only be resolved by a critical consideration of the Pith and Substance Principle. It is arguable that the Supreme Court did not consider the pith and substance of the VAT Act in the circumstance that if it had done, it would have realized that the substance of Item 62(a) in the Exclusive Legislative List of the Second Schedule to the Constitution restricts the National Assembly to international and intestate trade and commerce. The pith and substance do not cover intra-state transactions which the States' Sales Tax Laws covers. The application of the doctrine of "presumption of validity" without any consideration of the Statute's pith and substance would appear to constitute a fundamental error as against the Sales Tax Laws which has to its credit the presumption that its pith and substance is territorial. It has obviously resulted in attributing to the National Assembly that it has power to legislate on sales and supply of goods and service beyond its competence. Please see the case of ***New India Sugar Mills v Commissioner of Sales Tax***[26] on how India dealt with similar issue among its federating units.

As earlier noted, the provision of Section 4(5) which is the source of the doctrine of covering the field does not presumes the constitutionality of an Act of the National Assembly for it to prevail over the law of a State. Such an Act of the National Assembly must have been ascertained to be validly made. The argument that neither of the parties raised the validity of the VAT Act may not avail the Supreme Court. The wordings of Section 4(5) of the Constitution is clear enough to have put the Court on suspicion that even if none of the parties failed to raise it, there is no way it would arrive at a just decision applying the doctrine of covering the field without considering whether the VAT Act was validly made. It is a requirement of the Constitution. It is arguable that the Supreme Court was duty bound to raise the validity question and call parties to address it on it.

It must be stated that, raising an issue *suo motu* by the Supreme Court is not uncommon in our legal system. The Supreme Court has adopted such approach in many cases especially where it involves constitutional provisions. In the case of ***PDP v Okorocha,***[27] the Supreme Court was faced with a factual situation where the judgment of the Court of Appeal in an election was delivered within 60 days prescribed but the reason for the judgment delivered outside the 60 days prescribed by the Constitution. None of the parties to the appeal raised the validity of the judgment in the appeal and briefs. The Supreme Court in its wisdom identified it and raised the question of the validity of the judgment appealed against. Their Lordships then called the parties to address it on the validity of the judgment in line with the provisions of Section 285(7) of the Constitution.

Of course, both parties complied with the directive. On its part, the Appellant amongst other submissions contended that the Supreme Court was incompetent to raise the issue *suo motu*

as no ground of appeal was filed in respect of it and neither of the parties submitted such issue for the Court's adjudication. He urged the Court to hear the appeal on its merit. The Respondents submitted that the issue raised is a constitutional point and that the Rules of Court permitted the Court to raise any issue *suo motu* provided parties are heard on the issue so raised. The Supreme Court disagreed with the Appellant's submission and held per Ngwuta JSC in the lead judgment as follows:

> *The Court hearing a matter, whether as a court of first instance or an appellate court has a duty to ensure that the processes by which a party seeks relief before it comply (sic) with the relevant provisions of the applicable law.* ***It may raise an issue suo motu provided that if the issue so raised is one on which the matter will be disposed of, learned Counsel for the parties must be heard on it before decision is taken.***[28]

In his contributory judgment that complemented and further clarified the lead judgment, His Lordship Muhammad JSC hit the nail on the head when he categorically held:

> *Although, the issue for address raised by this court suo motu has not been captured by any parties, particularly the appellants in their amended notice of appeal, it is beyond dispute that Section 285(7) and (8) are enactments of the Constitution.* ***Each and every one of us over here has sworn to uphold the constitution. Where a party, either by accident or design, neglects to invoke the provision of the Constitution, it is the bounden duty or responsibility of the Supreme Court and indeed any other court established by the same Constitution to bring the issue to light and bring same to the notice of the parties to the action or appeal*** *and then afford each of them an opportunity to be heard on same.*[29]

Conclusively, it is arguable that the failure to consider the question of the validity of the VAT Act before arriving at the conclusion that the Sales Tax Law of Lagos State must remain inoperative may perhaps be incorrect.

5. The Principle of Avoidance of Double Taxation

In its decision under consideration, the Supreme Court had reasoned and held that the imposition of both the VAT Act and Sales Tax Law of Lagos State would create double taxation. The justification by the court in arriving at this decision amongst other can be found on pages 555 – 556 of the NWLR which includes that:

a. both laws provided for collection of tax from the customer on consumable items set out in both laws;
b. the rates in both laws are the same;
c. goods upon which charges are made would lead to "unhealthy competition" between the two laws;
d. the two laws would throw the consumer and collecting agents into confusion.

Although, there is a general principle of construction that permits the Court to adopt an interpretation that avoids double taxation by the same Act whenever its strict interpretation

will result in double taxation of the same income or transaction. His Lordship, Viscount Radcliffe elucidated the principle in ***IRC v F. S. Securities Ltd***[30] thus:

> *Double taxation in itself however is not something which is beyond the power of the legislature to provide for, where construing its tax scheme. It is rather that given that a situation would really involve double taxation, it is so unlikely that there would have been an intention to penalise particular form of income in this way that the approaches the interpretation of complicated structure of the Code with a strong bias against achieving such a result.*

It appears that the Supreme Court's decision in ***A.G. Lagos v Eko Hotels*** *(supra)*under review, applied the principle of avoidance of double taxation in holding that Sales Tax Law of Lagos State amounts to double taxation based on its finding that the VAT Act is an existing law of the National Assembly.

It is arguable that this principle was misapplied in the circumstance that where the legislature creates such double taxation within its legislative competence, the principle will no longer be applicable. In ***Jain Bros v Union of Indian***,[31] the provision of **Section 23(5) of the Indian Income Tax Act, 1922** had provided for the assessment and payment of tax by a registered partnership firm and also for inclusion of the share of income of a partner within the firm in his total income tax. The argument was that the partners carry on their business simply under the registered name and that does not in itself make it taxable. The Supreme Court of Indian dealing with similar situation in *Jain Bro's case* unequivocally made the point when it held:

> *But as the rule of avoidance of double taxation is merely a rule of construction, it ceases to have any application where the legislature expressly enacts a law which results in double taxation of the same income. The law so made cannot be held invalid merely on the ground that it results in double taxation.*

Agreeing with the above ratio, C.P. Singh[32] adopted this view in his book and concluded that there is no general principle which states that there can be no double taxation in the levy of a particular tax but the court may lean in favour of a construction that is against it if that circumstance occurs. It must be noted that India also practices constitutional federalism like Nigeria. In fact, most of the Nigerian constitutional provisions are fashioned in like manner with the Indian Constitution. Certainly, the circumstance of the instant case under review does not permit the Supreme Court to apply this principle of avoidance of double taxation to arrive at the conclusion that Sales Tax Law of Lagos State amounts to double taxation. This is because, Lagos State was presumed to have acted within its legislative competence in passing the Sales tax legislation which is an exception to the general rule.

The VAT Act Cannot be Presumed to be an Existing Act of the National Assembly until its Conformity Test is Applied

The Court had also invoked the provision of **Section 315 of the Constitution** to support its decision that the VAT Act is an existing law in Nigeria. This position, though appears to

represent the correct position of law on what constitutes an existing law, it may however be faulty on the ground that the historical perspective or background of the VAT Act which was formerly a decree ought to have been considered to ensure that it is in conformity with the provisions of the 1999 Constitution (as amended). The Supreme Court had handed down this principle in ***A.G. Lagos State vs. A.G. Federation***[33] when it was considering a similar decree which was later deemed an Act of the National Assembly upon the coming into force of the 1999 Constitution. The dictum of the Court per Kalgo, JSC is very instructive:

> *... at the time the Nigerian Urban and Regional Planning Decree 1992 was promulgated, the Federal Military Government which made it had power to make laws for the whole Federation of Nigeria.* ***With the coming to civilian or democratic regime in 1999, this law must be examined critically to see if it can be applicable to the whole country or any component part of it with or without any amendment. This is what Section 318 of the 1999 Constitution refers to an existing law and can only be effective with such modifications as may be necessary to bring it into conformity with the provisions of the Constitution****.*

The point being made here is that, in arriving at its conclusion that the VAT Act is an existing law of the National Assembly, the Court must have ascertained that the application of its provisions throughout Nigeria on all supply of goods and services irrespective of whether it is international, inter-state or intra-state, is in conformity with the current democratic dispensation envisaged under the 1999 Constitution which exclusively reserved the taxation on intra-State supply of goods and services to the States' Governments. It must be stated that a strong position which Lagos State Government should have canvassed is the fact that the 1st Respondent (Eko Hotel) failed to identify whether the supplies made to its customers was either across boarder, inter-state or intra state in which case, the presumption that the supplies were within the territorial jurisdiction of Lagos State would have been preferred.

Concept of Double Taxation at a Glance

A perusal of the Supreme Court's opinion on the basis for holding that VAT Act and Sales Tax Law would amount to double taxation precipitates an inquiry into what does double taxation mean as the court did not make any categorical definition of the term. According to Angharad Miller & Lynne Oats[34], these scholars attempted to contextualize and referred to it as *being exposed to tax more than once on same profits or income and may take the form of economic or juridical double taxation*. These scholars maintained that economic double taxation covers any situation where an amount of income is taxed twice in a single country while juridical double taxation occurs where more than one country attempts to tax the same income due to jurisdictional conflict in the rules that are applicable to determine the residence and or source of the tax base. In the **West's Encyclopaedia of American Law**, a situation of double taxation is said to occur "*when the same transaction or income source is subject to two or more taxing authorities. This can occur within a single country, when independent governmental units have power to tax a single transaction or source of income*[35]*"*. It is therefore safe to state that double taxation occurs in different ways. It may

arise where the same tax authority imposes two charges on the same subject or transaction for the same reason under the same legislation. It is submitted that there cannot be double taxation where such tax is imposed by different authorities on the same subject. One factor that permeates the above definitions is the imposition of more than one tax on the same subject.

Although the States' Sales Tax Laws and the Federal VAT are both targeted at the supply of goods and services, it is arguable that the subject matters of the two tax legislations are not same. As earlier submitted, VAT is expected to cover international and inter-states supply of goods and services whereas sales tax covers intra-state supply. These two species of supplies are not the same and cannot be any "unhealthy competition" as what each of the legislation targets is on different sphere.

The experience of countries practicing true federalism, such as the USA, Canada, India or Australia evinces that there are instances of Federal, State and Local Government taxes operating side by side and each of these levels of governments impose a form of tax on the same subject matter. This is particularly so in the case of sales tax, consumption tax or VAT. The percentages might vary among Federal, State or local taxes, but one often finds them all sitting on the same invoice. While one should not be construed to be advocating that in Nigeria, it is the norm in a federal structure that the Nigeria professes to be. As a matter of fact, the current fiscal practical arrangement in India has been codified through its 2015 constitutional amendment to foster its fiscal federalism.[36]

It is further submitted that the proper approach should be to make an inquiry as to whether either or both statutes have constitutional basis. If they both do, then both charges remain in effect and must be operating concurrently. For some reasons, Ade Ipaye[37] maintained and which view seems to be correct that the drafters of the Nigerian Constitution specifically reserved some taxes for Federal control, deliberately excluding Sales or Consumption Taxes. That is why VAT or Consumption Tax cannot be found on the Exclusive or Concurrent Legislative Lists.

6. Concluding Remarks and Recommendations:

The review of this case will not be complete without stating the fact that this analysis should not be construed to be suggesting or encouraging multiplicity of taxes in the country which in itself have negative effect on investment and economic development of the country. This chapter seeks to identify the legal implication of the judgment on the political economy of Nigeria, what ought to have been done but which was omitted and the implication of such omission with the view of ensuring such is remedied when the opportunity presents itself in the future.

By the doctrine of *stare decisis*, the judgment of the Supreme Court in ***A.G. Lagos State v Eko Hotel*** discussed in this review will remain the law until set aside by the Supreme Court. The decision is not only an authority on the application of doctrine of covering the field but

also capable of limiting the fiscal legislative competence of State Governments within the federal structure in Nigeria. The decision is not only at variance with the new National Tax Policy recently adopted by the Federal Executive Council in 2017 as a starting point to re-engineer and strengthen Nigeria's fiscal federalism; it is also an authority that seems to suggest that the validity of an Act of the National Assembly would not be considered in applying the doctrine of covering the field so long as none of the parties to the action fail to raise it.

The Supreme Court is called upon to revisit and reinstate its earlier decision in ***Attorney General of Ogun State v Aberuagba& 7 Ors***[38] where their Lordships adopted the principle of "trade and commerce clause" to interpret the validity of the Sales Tax Law of Ogun State in the context of the 1979 Constitution which provisions are *parimateria* with the1999 Constitution thereby ascertaining the limits of the taxing powers of the Federal and States' Governments.

Although, the dispute between the parties involved the validity of the tax law and legislative competence of the Federal and State Legislature in Aberuagba's case, it is suggested that the Supreme Court should invoke its inherent power to raise issue of validity of any law where raising such issue would clarify the dispute or where the validity is required as a standard; even when such has never been done before. According to Lord Denning, MR reasoned in ***Parker v Parker***:[39]

> *That no case has been found in which it has been done before..... If we never do anything which has not been done before, we shall never get anywhere. The law will stand still while the rest of the world goes on, and that will be bad for both.*[40]

Additionally, it is worth noting that in the exercise of its adjudicatory role, the Supreme Court rose to the occasion in ***A.G. Federation v A.G. Lagos State (2013) 16 NWLR (Pt. 1380) 249*** and validated the Hotel Occupancy & Restaurant Consumption Law which is a specie of Consumption Tax just like VAT. The ripple effect of the decision had precipitated other States in the federation to enact similar laws. This in a way has developed the fiscal federalism of the country. This is unlike the case under review.

Tax dispute is *sui generis* and requires expertise in deciding it. Therefore, the tax practitioners in Nigeria under the auspices of the Chartered Institute of Taxation of Nigeria whose responsibility is to train and regulate tax practice in the country should lend assistance to Nigeria Courts in explaining some of the tax issues and concepts when called upon (*amicus curie*) to enable the Court arrive at just decisions.

The Ministry of Justice should also engage registered tax practitioners and consultants especially the legal practitioners that double as tax consultants to advice on the strategy for their cases.

Engaging consultants would avoid taking wrong steps in the course of proceedings such as when Lagos State Government withdrew its Counterclaim filed in the suit at the trial court. Of course, the Counterclaim which challenged the constitutionality of the VAT Act would have presented additional opportunity to the Supreme Court to deal with the issue. This view certainly springs from the benefit of hindsight.

The 2017 National Tax Policy constitutes Nigeria's national ideology and policy direction on taxation. It will serve as an instrument of external aid to the Court in interpreting many of the tax legislations in terms of their pith and substance, constitutionality and validity, considering the peculiarity of the Nigerian federalism.

ENDNOTES

1. Formerly Decree No. 102 of 1993 now Cap V3 LFN, 2004 (as Amended)
2. See the case of ***A.G. Lagos State v. A.G. Federation (2014) NWLR (Pt. 1412). 217*** In that case, the constitutionality and validity of the VAT Act was raised and made an issue in dispute. The Federal Government of Nigeria, the 1st Defendant, filed a preliminary objection to the hearing of the suit on the ground that the Supreme Court lacked original jurisdiction over the acts of the Federal Inland Revenue Service (FIRS), a federal agency, considering the provision of Section 251 of the 1999 Constitution. On its part, the Lagos State Government argued that the dispute is in respect of a claim between the Federal Government and States Government over which the Supreme Court has original jurisdiction. It argued further that the dispute bothers on the constitutionality of VAT and illegality of such collection by the Federal Government's agency. The Supreme Court agreed with the Federal Government's argument and declined jurisdiction to hear the suit on the ground that the dispute is in reality a complaint against the actions of an agency of the Federal Government. The Supreme Court further noted that there is a distinction between the 'Federal Government of Nigeria' and 'Government of the Federation'. Consequently, the case was struck out.
3. Cap 175 Laws of Lagos State 1995
4. Nnaemeka Boniface AMADI "Understanding the Fundamental Issues of Multiple Taxation in Nigeria: The Theoretical and Historical Approach" International Journal of African and Asian Studies ISSN 2409-6938 An International Peer-reviewed Journal Vol.64, 2020, p.38
5. (2018) 7 NWLR (Pt. 1619) 518
6. See generally pages 536 – 543 of the law-report
7. (2002) 6 NWLR (Pt. 763) 264
8. (2003) 3 NWLR (Pt. 806) 72
9. *(2003) 3 NWLR (Pt. 808) 604*
10. See at page 547.
11. Interestingly, Lagos State Government had also enacted the Hotel Occupancy & Restaurant Consumption Law, Cap H8 Laws of Lagos State, 2009 of No. 30 Vol. 42. In ***A.G. Federation v A.G. Lagos State (2013) 16 NWLR (Pt. 1380) 249***, the Supreme Court validated the law which is a specie of a consumption tax on supply of goods and services made in hotels and restaurants within Lagos State. In view of the decision of the Court in *A.G. Lagos State v Eko Hotels* under review, it is respectfully submitted that a judicial situational controversy would arise such that in one breath, the Supreme Court held that validated a consumption tax of a State as valid and operational and in another breath declaring a State consumption tax amounts to double taxation and inoperative.
12. See at page 545
13. (2001) 45 WRN 1 at 19
14. (2003) 12 NWLR (Pt. 833) 1 at 159
15. *Ibid ……. at Page 158. The Supreme Court per Uwaifo, JSC, on page 191 of the law-report, relying on its earlier decision in A.G. Ogun State vs. Aberuagba& Others, in that case declared that "by this Constitutional arrangement which allocates legislative jurisdiction between the National Assembly and the House of Assembly of a State, it is recognized that any matter not mentioned either in the Exclusive or*

Concurrent Legislative List becomes a residual matter exclusively for the State House of Assembly by virtue of Section(7)(a).'' In the decision under review, the Supreme Court did not consider whether the provisions of VAT Decree No. 102 of 1993 which has now become VAT Act, Cap V1 LFN 2004 upon the coming into the civilian democracy from 1999 is in conformity with the legislative lists enumerated and reserved under the 1999 Constitution. It is submitted that until its conformity is ascertained, it cannot be regarded as an existing Act of the National Assembly and effective as prescribed by Section 318 of the Constitution. Its conformity would have been seen only to extent that VAT Act cannot cover supply of goods and services and at best, the "trade and commerce clause" under Item 62(a) may be stretched to reserve inter-state and international supply of goods and services exclusively for the National Assembly.

16. In ***A.G. Federation v A.G. Lagos State (2013) 16 NWLR (Pt. 1380) 249*** at 364, the Supreme Court refusing to apply the doctrine of covering the field to matters exclusively reserved for the State. In that case, Hotel Occupancy & Restaurant Consumption Law of Lagos State 2009 amongst other laws which impose tax on supply of goods and services in hotel and restaurant in Lagos State was challenged against Nigerian Tourism Development Act, Cap 137 LFN 2004 by way of covering the field as prescribed in Section 4(5) of the Constitution. In clear term and correctly too, the Supreme Court sitting as a Full Court of a 7-man panel disagreed with the Plaintiff (A.G. Federation) that the doctrine applies. In his contribution, Ngwuta, JSC contribution nailed it as follows:
"I have said earlier that the doctrine of covering the field is inapplicable in a matter within the exclusive legislative competence of the National Assembly as any law made by a State Assembly will be void for lack of power to make such law. In the same vein, there can be no issue of covering the field in a matter which is neither in the Exclusive List nor in the Concurrent List. In the case of such residual matter, the State Assembly has exclusive power to legislate and the issue of inconsistency of conflict with a Federal Law will not arise. Also the plaintiff cannot rely on Section 4(5) of the Constitution which cannot apply as the federal Law was not validly made by the National Assembly. See A.G. Ondo State vs. A.G. Federation (2002) 9 NWLR (Pt. 772) 222". (Emphasis underlined)
17. (2003) All ER 784
18. (1998) 2 NWLR (Pt. 537) 189 at 199
19. (2002) 5 NWLR (Pt. 759) 209.
20. Please see at page 230.
21. (2013) 10 NWLR (Pt. 1362) 275
22. Please see at 317
23. Vartika Srivastava in "Explained: The Doctrine of Pith and Substance" culled from https://lexforti.com/legal-news/doctrine-of-pith-and-substance/.
24. Sometimes the entries in different lists or the same list may be found to overlap or to be in direct conflict with each other. In that event it is the duty of the court to find out its true intent and purpose and to examine the particular legislation in its 'pith and substance' to determine whether it fits in one or other of the lists as was held in Synthetics and Chemicals Ltd. v. State of U.p.13 (SCC at pp. 150-51, para 67; SCR at p. 673); India Cement Ltd. v. State of T.N. 14 (SCC at p. 22, para 18; SCR at p. 705)].

25. HarakchandRatanchandBanthia v. Union, [1970] 1 S.C.R. 471,489,
26. (1963) AIR SC 1207 at 1213
27. (2012) 16 NWLR (Pt. 1323) 205 at 252
28. Please see at page 240 of the law report
29. Please see at page 252.
30. (1964) 2 All ER 691
31. (1970) SC 778 at 782
32. Principles of Statutory Interpretation, 12th Edition, 2010, LexisNexis, Butterworth's Wadhwa Nagpur, Pages 822 - 823
33. See Page 159 of the law-report
34. Principles of International Taxation, 2006,Tottel Publishing Ltd, Maxwell House, pages 57- 58
35. *West's Encyclopaedia of American Law, edition 2. Copyright 2008 The Gale Group, Inc*
36. By the Constitution (One Hundred and First Amendment) Act, 2016, an amendment which recognized goods and services tax chargeable by each of the arms of government was introduced in India. It came into force from 1 July 2017.
37. Nigerian Tax Law and Administration – A critical review, 2014, ASCO Prime Publishers, Page 323
38. *(1985) 1 NWLR 395*
39. *(1953) 2 All ER 127*
40. Please see *at 129*

ABOUT THE BOOK

"Value Added Tax in Nigeria – Policy, Legal, Administrative issues and Options for Reform" is the combination of various articles written by tax practitioners, administrators and the academia, to provide conceptual and application principles that underpin the adoption, implementation and administration of Value-Added Tax in Nigeria. The book has been compiled and reviewed by the Indirect Taxation Faculty of the Chartered Institute of Taxation of Nigeria.

The book discusses topical issues in the administration of Value Added Tax (VAT) in Nigeria, together with recent amendments to the VAT Act up to 2020 Finance Act amendments. It covers all aspects of Value Added Tax in Nigeria including the history and concept of VAT, the historical development of VAT in Nigeria, a review of amendments to the Value Added Tax Act from 1993 up to 2020, Value Added Tax administration and technology in Nigeria, resolving the conundrum in the application of Value Added Tax to real estate transactions, examining the effect of recent tax reforms, the applicability of VAT to professional services in Nigeria, tax appeal – assessment, objection, appeal, issues and options for reform. This is a handy reference material for tax practitioners, administrators, taxpayers, manufacturers, producers and consumable stores and outlets etc.

The book will assist tax practitioners, administrators, taxpayers, manufacturers and producers and consumable stores and outlets in managing Value Added Tax issues that are encountered in their daily activities.

ABOUT THE INSTITUTE

The Chartered Institute of Taxation of Nigeria was established on February 4, 1982, as the Association of Tax Administrators and Practitioners (ATP). Thereafter, it transformed into Nigeria Institute of Taxation, which was formally launched on February 21, 1982, and statutorily recognized on May 6, 1987, as a company limited by Guarantee.

The Institute became chartered by the Federal Government of Nigeria by the enabling Act No. 76 of 1992 (now CITN Act, CAP C10, Laws of the Federation of Nigeria, 2004) and was charged with the responsibility among others of regulating and determining what standards of knowledge and skills are to be attained by persons seeking to become tax professionals in Nigeria and only it's members can practice taxation in Nigeria.