



UDO UDOMA & BELO-OSAGIE

The Nigerian Federal High Court Declares the Tax Appeal Tribunal Unconstitutional; Orders the Minister of Finance to Disband the Tribunal Forthwith and Affirms that Recharges are Deductible from the Turnover of a Foreign Company under the Turnover Basis of Assessment.

The Federal High Court, Abuja Division (“FHC or the Court”) has in a judgment delivered on 30th October 2013 in suit **No.FHC/Abj/TA/11/2012TSKJ Contruces Internationals Sociedade Unipessoal LDA v. the Federal Inland Revenue Service** declared the Tax Appeal Tribunal (“the TAT or the Tribunal”) to be an unconstitutional and illegal body; mandated the Minister of Finance to immediately disband the Tribunal and also affirmed that recharges are deductible expenses from the turnover of a non- resident company under the turnover basis of assesment.

Summary of Facts

TSKJ, a non-resident company, entered into a contract with the Nigeria LNG Limited for the construction of Nigeria Liquefied Natural Gas (LNG) plant. In executing the contract, TSKJ contracted with its Nigerian subsidiary, TSKJ Nigeria (“TSKJ Nigeria”) to provide logistic support services. The arrangement between TSKJ and its Nigerian subsidiary was a ‘cost-plus’ arrangement, in which TSKJ reimbursed TSKJ Nigeria for the actual costs incurred in executing the contract, plus a mark up at an agreed percentage. It is the reimbursement, together with the mark-up, that constitutes what is known as “recharges”.

TSKJ filed self assessment tax returns on the basis of turnover as provided by section 30 (1)(i)(b) of the Companies Income Tax Act. In filing its tax returns, TSKJ deducted from the turnover which it derived from Nigeria the recharges it paid to TSKJ Nigeria. The deduction was disallowed by the Federal Inland Revenue Services (“FIRS”) on the ground that the deduction of recharges was not allowed under the deemed profit basis of assessment. The FIRS, therefore, issued TSKJ with notice of an additional tax assessment for the relevant years. TSKJ objected to the additional assessment and requested the FIRS to reconsider and amend the assessment. The FIRS refused to amend the additional assessment and issued a Notice of Refusal to Amend. Consequently, TSKJ filed an appeal at the Tax Appeal Tribunal (“TAT or the Tribunal”) challenging the additional assessment.

The TAT disallowed the appeal and ordered TSKJ to pay the sum of \$ 12, 924, 947 (twelve million, nine hundred and twenty four thousand and nine Hundred and Forty Seven United States Dollars) as additional tax liabilities based on the add back of recharges for the 1997,1998, 1999, 2000 , 2001 and 2002 years of assessment¹. TSKJ was aggrieved with the decision and lodged an

appeal at the FHC in which it contended, among other grounds, that the TAT misconstrued the provisions of section 30(1)(b)(i) of CITA. Additionally, TSKJ sought and obtained the permission of the FHC to raise and argue that the TAT did not have jurisdiction to entertain the appeal in the first place, because the Constitution of the Federal Republic of Nigeria, 1999 (as amended (“the Constitution”)) confers on the FHC exclusive jurisdiction over all matters relating or pertaining to the revenue of the Federal Government of Nigeria (“FGN”) or the taxation of companies.

Decision on the Issue of Jurisdiction

In its judgment, the FHC held that the TAT did not have the jurisdiction to entertain and decide matters pertaining to the revenues of the FGN. The decision of the Court on this point was anchored on section 251 (1) (a) & (b) of the Constitution which confers exclusive jurisdiction on the FHC in civil cases and matters relating to (a) the revenue of the Government of the Federation in which the said Government or any of its organs is a party and (b) connected with or pertaining to the taxation of companies and other bodies established or carrying on business in Nigeria and all other persons subject to Federal taxation. Based on the Court’s decision on this issue, the Court declared the TAT to be an illegal body and also restrained the TAT from adjudicating on tax matters relating to Federal Government revenues or the taxation of companies and also ordered the Minister of Finance to disband the TAT forthwith. In coming to this conclusion, the Court rejected as “mere semantics, misconceived and untenable in law” the contention of the FIRS that the TAT is not a court per se but a mere administrative panel.

Decision on the Merits of the Case

¹ See TSKJ v. FIRS (2012) 7 TLRN, 48.

After deciding that the TAT lacked the jurisdiction to entertain the matter, the Court, for the sake of completeness, still went ahead to consider the merits of the appeal filed by TSKJ . In this regard, the Court held that the TAT was wrong in law when it refused to follow the earlier decision of the FHC in the Halliburton decision. The Court held, therefore, that the TAT was duty bound to follow the FHC's interpretation of section 30(1)(b)(i) of CITA . The FHC had in the Halliburton case held that²:

“...the Body of Appeal Commissioners³ can, therefore, not be right in its conclusion that Turnover of the Appellant must include all sums received and receivable by the Appellant in the year and that payment which Appellant made to Halliburton Nigeria is not relevant to implementation of the provision of Section 26(1) of CITA. It is not in dispute the fact that both Appellant and Halliburton Nigeria must pay Tax on income that they derive under the contract. The Appellant cannot therefore be taxed for the total amount that it received under the contract inclusive of the money it paid over to Halliburton Nigeria in executing the contract and 4 per cent fee when Halliburton Nigeria would pay Tax on whatever it receives under the contract. To allow that would be double taxation.”

Implication of the Decision

The implications of the decision are two-fold. Firstly, unless the decision is successfully appealed and set aside, all the decisions and judgments of the TAT will be rendered null and void and no legal rights will flow from such decisions. Consequently, any party against whom the TAT had made an adverse judgment now has a valid legal basis to apply to the FHC to set aside such judgment. Similarly, any tax payer that had successfully challenged an assessment at the TAT will

lose the benefit of such judgment because no rights can flow from a judgment that is null and void. Secondly, and as regards the merits of the case, the decision affirms the earlier decision of the FHC to the effect that recharges (i.e. monies paid by a non resident company to its Nigerian subsidiary that participated in the execution of the contract from which the turnover was derived) do not form part of the revenue of the foreign company for purposes of tax assessment under the turnover profit basis of assessment.

General Comments.

Based on the very clear and unambiguous provisions of the Constitution which confers exclusive jurisdiction on the FHC on matters relating to the revenue of the FGN and the taxation of companies, it is our opinion that the decision of the FHC is sound and not likely to be set aside on appeal. By virtue of section 251 (1) (a) and (b) of the Constitution, all matters relating to the revenue of the FGN and/ or taxation of companies ought to be decided by the FHC. Although the TAT was established pursuant to the Federal Inland Revenue Establishment Act (No. 12) of 2007 (the FIRS Act)⁴, its status is tenuous given the obvious conflict between the provisions of the FIRS Establishment Act and section 251 of the Constitution. Under Nigerian law, the provisions of the Constitution are supreme and prevail over any other law that is inconsistent with the Constitution. This being the case, we are of the opinion that the only way to save the TAT is for the Constitution to be amended to include it as a special tribunal in the same manner in which the Constitution (Third Alteration) Act was passed in order to include the National Industrial (NIC) Court, after the Supreme Court had declared the NIC to be an inferior court.

On the issue of recharges, it is our further opinion that the FHC rightly held that the TAT ought to have followed its earlier decision in the Halliburton case, which has not been

² *FHC/L/1A/2005 Halliburton West Africa Limited V. Federal Board of Inland Revenue (Unreported) judgment delivered by Abdullahi Mustapha on 7th June 2006.*

³ The body of Appeal Commissioners was disbanded by the FIRS (Establishment) Act 2007 and replaced with the TAT.

⁴ The TAT was conferred with jurisdiction over matters arising from the following tax statutes: Companies Income Tax Act, Petroleum Profit Tax Act, Personal Income Tax Act, Capital Gains Tax Act, Value Added Tax Act, Stamp Duty Act, Taxes and Levies (Approved List for Collection) Act and any other law for the assessment, collection and accounting or revenue accruable to the Government of the Federation of Nigeria.

successfully appealed by the FIRS. A review of other decisions of the TAT on recharges leaves one with the impression that the TAT was determined to mitigate the effect of the Halliburton judgment by seeking to 'distinguish' cases that would otherwise be on all fours with the Halliburton case. For instance, in its decision in **TAT/SSZ/003: Global Marine International Drilling Corporation v. FIRS** and in the related case of **TAT/SSZ/004: Global Marine Baltic Inc. V. FIRS**⁵ in which our firm represented the Appellants, the TAT distinguished both appeals from the Halliburton case on the ground that the local subsidiary of the Appellants was not a party to the drilling contract between the Appellant and third parties, even though the relevant agreement was not tendered in evidence and the parties did not join issues on that point. This same approach is evident even in the TSKJ case under review where the TAT refused to admit in evidence a circular issued by FIRS but, nonetheless, the TAT relied on that same document to justify its decision that recharges were not an allowable deduction from the turnover of TSKJ.

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⁵ (2013) 12 TLRN, Judgment delivered on 30th July 2013.