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Federal High Court rules against income tax assessment based on the value of a property

KPMG in Nigeria

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The Federal High Court (FHC) sitting in Abuja recently gave a judgement in favour of Theodak Nigeria Limited (TNL or "the Company" or "the plaintiff") in its lawsuit against the Federal Inland Revenue Service (FIRS or "the defendant"). The issue for determination was whether the FIRS had statutory power to deem the value of the Company's property to be its turnover for any year of assessment (and impose income tax thereon) based on the provision of Section 30 of the Companies Income Tax (CIT) Act, Cap. C21, Laws of the Federation of Nigeria (LFN), 2004.

Background

Generally, CIT is payable on the profits of a company "accruing in, derived from, brought into or received in Nigeria[1]" in respect of any trade or business that may have been carried on. The CIT Act requires every company to file its tax returns for every year on a self-assessment basis, containing the amounts of profits from every source, with the FIRS. Section 30 of CIT Act empowers the FIRS to assess a company on a fair and reasonable percentage of the turnover from its trade or business where either the business produces no assessable profits; where the assessable profits are less than might be expected to be, or where the true assessable profits cannot be ascertained.

Facts of the case and issues for determination

The FIRS alleged that the Company did not file its income tax returns for 2015 and thereby failed to pay its income tax liability for that year. Hence, the FIRS invoked the provisions of Section 30(1)(a) of the CIT Act by deeming 20% of the ascertained value of a property admitted to be owned by the Company to be the CIT payable, and issued its assessment notice for the amount.

Dissatisfied with the FIRS' action, TNL filed an appeal at the FHC arguing that:

- Section 30(1)(a) of the CIT Act does not empower the FIRS to assess the value of its property to CIT
- the foregoing CIT Act provision provides for assessments to be based on a fair percentage of the turnover of a trade or business and
- the value of a company's property is not listed as taxable income in Section 9 of the CIT Act.

Thus, the Company urged the FHC to declare that the value of its building was not the same as its turnover, and that the FIRS' action was ultra vires its statutory powers under the CIT Act. The plaintiff also prayed the FHC to set aside the FIRS' assessment and restrain the defendant from enforcing the recovery of the alleged tax liability.

The FIRS, on its part, argued that Section 30(1)(a) of the CIT Act gave it a wide range of power to assess delinquent taxpayers to tax, and therefore had the statutory power to impose its best of judgment assessment on TNL based on the value of the Company's property. This was on the ground that TNL had failed to file its tax returns despite several notices issued by the FIRS. The defendant also argued that the assessment was final and conclusive because the plaintiff failed to object within 30 days as provided by the CIT Act.

The FHC's judgement on the power of the FIRS to assess a company to CIT based on value of its properties has, hopefully, put paid to the controversy attendant on the initiative taken by the FIRS to use properties owned by taxpayers as basis for their assessment to tax.

[1]Section 9 (1) of CIT Act

Decision

After considering the arguments of both parties, the FHC held that:

- The FIRS did not act within the boundaries of Section 30(1) of the CITA in assessing the Company to tax on the basis of the value of its property. Section 30 only empowers the FIRS to assess a company to tax on a fair and reasonable percentage of its turnover, and that turnover refers to the aggregate income that a business receives from its normal business activities for a given period, usually from the sale of goods and services. Hence, the value of the Company's property is not the same as its turnover or income.
- It would be unfair to deem the value of the Company's property as its turnover for the year of assessment, and the FIRS' act of unilaterally assessing the value of the Company's property was oppressive and ultra vires.
- The Company was not under any obligation to object to the FIRS before it could challenge the assessment in court. The use of the word "may" in Section 69(1) of the CIT Act makes it discretionary for the plaintiff to object to the FIRS' assessment, and failing which the Company could not be denied the right of access to court as conferred by the 1999 Constitution of the Federal Republic of Nigeria.

Based on the foregoing, the FHC issued a perpetual injunction restraining the FIRS and or its agents from enforcing any actions against the Company on the basis of the property assessment.

Comments

The FHC's judgement on the power of the FIRS to assess a company to CIT based on value of its properties has, hopefully, put paid to the controversy attendant on the initiative taken by the FIRS to use properties owned by taxpayers as basis for their assessment to tax. The CIT Act is clear on the categories of income chargeable to income tax, which should be respected by the tax authorities. Also, as one of the canons of taxation is equity, taxpayers should be assessed to the right amount of tax in proportion to their income, only.

The FHC judgement that a taxpayer has the discretion to seek redress in the court in the first instance, without first going through the administrative process of objecting to a tax assessment by the FIRS, is quite instructive. The decision essentially invites tax payers to weigh their options and forum shop at two levels. Firstly, in deciding whether to bother objecting to an FIRS tax assessment as provided for in the tax legislation for an initial administrative dispute resolution protocol and, secondly, in deciding whether to refer a tax dispute to the Tax Appeal Tribunal (TAT) at all.

Consequently, this decision may inadvertently lead to a shortening of the tax resolution procedures provided in tax legislation and therefore an early widening of the gates to litigation at the FHC level for cases that may actually not be ripe for adversarial resolution.

As full litigation can be costly and time-consuming, and as judges are also not necessarily as hands on with respect to tax technical issues as the FIRS itself, or the TAT, we are in favour of encouraging taxpayers to explore the less adversarial protocols available under the tax legislation before referring disputes to the FHC for resolution. While a taxpayer cannot be denied the constitutional right of access to the courts, the pursuit of administrative resolution of a tax dispute through objection to a tax assessment by the FIRS should not be totally rejected.

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