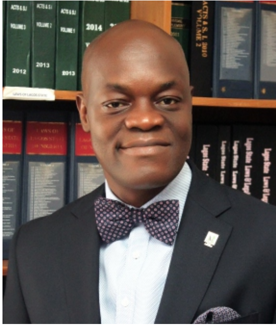
Excess Dividend Tax: The Unfinished Business

'*Taxspectives*' by **Afolabi Elebiju** | Originally published in *ThisDay Lawyer, 26.11.2013, p. 7*



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Introduction

A recent front page item conveyed the intent of Nigerian government to take concerted action, pursuant to the National Tax Policy, against multiplicity of taxes and outsourcing of tax collection by States by leveraging legislation such as the ***Taxes and Levies (Approved List for Collection) Act, Cap. T2 2004*** and administrative instruments, specifically the issuance of Executive Order by the President. See *The Guardian* of 22/10/2013. Whilst this declaration of intent sends the right investment (and very welcome) signals, there would be challenges along the way, including constitutional provisions; but those would be the subject of discussion for another day. Incidentally, Taxspectives' inaugural piece was on outsourced tax collection (ThisDay Lawyer 8/9/2009, p.vi). Editorials like '*To Stop Multiple Taxation*' (The Guardian 11/11/2003) underscore the importance of issues around the recent declaration.

The disciple of competitiveness that I am, I recently mused: *"as a result of slow down of developed economies, and Nigeria's positive demographics (security and other challenges notwithstanding), she has become extremely well positioned within an attractive emerging market (EM), as a destination for investment with high potential returns. Some reform initiatives (with varying degrees of success, e.g. ongoing privatisation of power sector and stalled enactment of the PIB) are supposed to further unlock value of the Nigerian economy. A recent McKinsey study shows that multinationals are developing or refining their EM strategy; it also shows that those that had been implementing EM strategy are outperforming competitors in growing revenues. The Government ... is trying to champion some other reforms to improve Nigeria country competitiveness..."* Whether we are doing enough to take advantage of currently favourable global investment winds (which tends to cyclically shift directions) is another matter. However, the recent announcement that Nigeria will be hosting World Economic Forum (WEF) Africa next May is a welcome development.

Multiplicity of Taxes and Double Taxation

'Multiplicity of taxes' and 'double taxation' are sometimes used interchangeably (and the latter could be an example of the former), but they are not the same. Multiplicity is typified by some States reportedly having "97 different taxes, levies and charges that are imposed on businesses." Apart from the adverse impact on businesses and the economy, this is the stuff that Nigeria's unimpressive showing in the annual *Ease of Paying Taxes* is made of. Imagine that *"for every N100 that businesses have to pay in taxes, they pay about N35 in compliance costs"*!

In ***Global Marine International Drilling Corporation v FIRS (2013) 12 TLRN 1 at 23***, the TAT (S/South Zone) held that: *"double taxation can only happen where the same amount of income is taxed more than once in the hands of the same taxpayer."* Although double taxation offends the canons of taxation, it is the very essence of the excess dividend tax (EDT) provision of Nigerian tax law (*sections 19* and *20(b) CITA*).

EDT as Double Taxation

EDT - apparently an anti-avoidance rule - has been widely criticized, seeking to unravel a journey after safe arrival, albeit the taxpayer faithfully followed 'all the rules of the road' specified by other tax provisions. The destination that these *CITA* provisions frowns at is where no tax is payable or dividends payable by a company is higher than its total profits in a particular year, the dividends shall be deemed, to be the company's "total profits" for that year.

To use criminal law comparison, EDT is tantamount to a strict liability offence that requires no proof of intent: how you arrived at destination (of having no/ lower profits than dividends) is irrelevant: having arrived, you must "suffer the fate" reserved for every traveler, pay EDT! An earlier Taxspectives piece, ***Rethinking Nigeria's Excess Dividends Tax (ThisDay Lawyer, 29/3/2011, p. vii)*** provides some background discussions.

Waiver for Bank Holdcos & Issues

The doubtful utility of EDT was brought into focus recently when the FIRS granted "waiver" of the rule against Bank Holdcos, pursuant to restructuring mandated by the CBN. See ***Paragraph 2.1, FIRS Information Circular No. 2012/01, Explanatory Notes on the Critical Tax Issues for the Operation of Bank Holding Company Structure in Nigeria of 4/4/2012***. Although non-applicability of EDT was (and is) a desirable result, there are valid questions as to FIRS' competence to grant such waiver.

I say this because the premise of FIRS position (that ***section 80(3) CITA*** on treatment of dividends as franked investment income disapplied ***section 19 CITA (EDT)***, is wrong. A review of legislative sequence of the two CITA provisions shows that ***section 19*** (a 1996 amendment) was later in time. In case of conflict, the subsequent provision prevails, moreso as the legislator is presumed not to legislate in vain. In the event, ***section 80(3)*** prevails only over the variant EDT in *section 20(b)*, since both ***(sections 80(3) and 20(b))*** were in existence prior to the 1996 ***section 19*** amendment.

Simply put, it is immaterial that an EDT situation arises pursuant to regulatory induced restructuring. Thus the only way out is either legislative action (repeal) or exercise of Presidential exemption under ***section 23(2) CITA***. However, the drawback of the latter option is that it is unlikely to uniformly apply to all companies and sectors.

The Holdco 'waiver' could signal that EDT provision (although still in the statute book) may fall into disuse. Otherwise, a moral hazard results: will FIRS enforce EDT against companies in other sectors whilst exempting Bank Holdcos?

Can there be a cause of action under *section 42 1999 Constitution* guaranteeing freedom from discrimination? But litigants may be constrained by *locus standi* – given our tax dispute resolution framework (and the 'personal' nature of tax) it may be difficult for a taxpayer to show its being aggrieved by FIRS' preferential treatment of another taxpayer. It is also arguable that section 42 being a "fundamental human right" provision is only for the benefit of "humans", and the direct victim of EDT is the company liable to EDT not its shareholders or directors. This reasoning may prevail, despite a Nigerian company having the powers of a natural person of full capacity pursuant to ***section 38(1) CAMA***.

Why Legislative Action is Required

To make assurance doubly sure that FIRS does not make a future *volte face* even against Bank Holdcos, legislative action is the ultimate solution. Fears about a *volte face* is not farfetched because FIRS' views in the Circular contradicts its EDT arguments in ***Oando v FIRS (2009) 1 TLRN 61*** (a case which FIRS won, and is currently on appeal). Another *volte face* is disclosed in the recharges case of ***Halliburton WA v FIRS (2003) 11 TLRN 84*** where the FHC held that FIRS circulars are no more than FIRS' interpretative opinion and that FIRS cannot be bound by its circulars especially where they conflict with tax provisions.

The EDT rule discourages entrepreneurship. Imagine a company devoting funds to R&D, with potential exposure to the EDT provision. If they decide to forgo the R&D investment because of EDT, the society loses the opportunity to advance. This is an illustration of how the tax law should not 'negatively' influence business decisions.

The EDT provision arguably exemplifies a 'gotcha' approach to tax collection. Does the introduction of the Transfer Pricing (TP) Regulations 2012 not represent a fatal argument against the retention of EDT? Once loopholes are plugged through TP, apparently section 19 is not only an overkill, but seeks to frustrate benefits/incentives given by other Nigerian tax provisions. It is a sore thumb in Nigeria's liberal investment environment.

Also, EDT rule presumes that investment holding structure is inherently bad; definitely, negative impact will attend strict application. However, valid business reasons, including administrative efficiency may commend such structure to an investor. From experience, EDT has been an issue for foreign investors regarding their Nigerian business strategy.

Conclusion

I am not aware of any current legislative initiative to repeal EDT provisions, but the earlier this is done, the better. Repeal should improve Nigeria's tax competitiveness rating, provide clarity as well as obviate needless tax litigation.

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