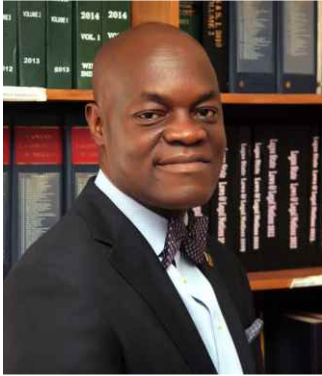
# Why Our Anti-Avoidance Tax Provisions Need Review

*'Taxspectives'* by **Afolabi Elebiju** | Originally published in *ThisDay Lawyer, 7th February 2012, p.12*



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### Introduction

Right from the industrial age, science and technology have been continually deployed to produce artificial products beneficial to mankind. For example, an impressive array of products (over 6,000) is 'artificially' derived from crude oil! However, the taxman bucks the trend by viewing 'artificial' transactions, suspiciously. In tax lingo, such transactions have been crafted without any substantive business object, but to achieve a reduction of the tax payable or to avoid tax liability altogether; accordingly, they must be struck down.

But there are limits to this. As Lord Tomlin famously stated in ***CIR v. DUKE OF WESTMINSTER*** *[1936] A.C. 1*: *"every man is entitled if he can to order his affairs so that the tax attached under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure that result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax."* Justice Learned Hand also stated in ***HELVERING v. GREGORY*** *69 F.2D (2nd Cir. 1934), Aff'd 293 US 465 (S. Ct.)* that: *"there is not even a patriotic duty to increase one's taxes"*, whilst striking down a tax motivated re-organisation as lacking business purpose. Nonetheless, a jocular comment which rings ever true is that *"the difference between tax avoidance and tax evasion is the thickness of a prison wall."*

Should our tax laws not keep pace with the financial markets, given increasing sophistication with structuring of complex transaction? To borrow from Professor Achebe's *Things Fall Apart*, if birds are leaning to fly without perching, shouldn't the taxman also be shooting without missing? This week, I take a ladle into these issues.

### The 'Artificial Transaction' Provisions

*Section 22(1) CITA, Cap. C21 LFN 2004* provides: *"where the Board is of the opinion that any disposition is not in fact given effect to or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, it may disregard any such disposition or direct that such adjustments shall be made as respects liability to tax as it considers appropriate so as to counteract the reduction of liability to tax affected, or reduction which would otherwise be affected, by the transaction and any company concerned shall be assessable accordingly."*

By *section 22(2)(a)*, *"disposition includes any trust, grant, covenant, agreement or arrangement"* whilst *section 22(2)(b)* seeks to catch related party transactions.

*Section 22(2)(c)* stipulates that *"transactions between persons one of whom either has control over the other or, in the case of individuals, who are related to each other or between persons both of whom are controlled by some other person, shall be deemed to be artificial or fictitious if in the opinion of the Board those transactions have not been made by persons engaged in the same or similar activities dealing with one another at arm's length."*

The above provisions of *section 22 CITA* are replicated in parimateria as *section 20 CGTA; section 15 PPTA* and *section 17 PITA.* This shows the pervasiveness of the taxman's intent to deal with 'artificial' transactions. It is pertinent to note that *section 22(d) CITA* (and equivalents) provides for resolution of divergent views between FIRS and the taxpayer through the tax objection and appeal process. This is in recognition of the principle of 'fairness' that the Revenue's opinion that subject transaction is 'artificial', should be subject to challenge or judicial review.

A good example of such contest is whether a merger transaction pursuant to which a post pioneer company (just after the expiry of its tax holiday) acquires a loss making (but strategic) target and amongst other benefits, assumes the losses of the target to reduce the acquirer's taxable profits going forward, could be successfully resisted by the Revenue? Particularly as *section 29(9) CITA* (for example), provides favourable treatment in merger situations where the underlying rationale is better organisation of that trade or business'?

### Case for Nigerian GAAR?

In a January 2007 seminar paper, *Protecting the Public Fisc: A Comparative Review of South Africa (SA)'s Proposed General Anti-Avoidance Rules (GAAR)*, I noted: *"Nigeria does not have a well developed GAAR*

*provision, apparently based on current level of sophistication of its 'emerging' financial market. The major provision is section 22… CITA....It empowers the Revenue to ignore or make adjustments in the case of 'fictitious or artificial' transactions that reduce or would reduce the amount of tax payable especially where there is a disposition and also in related party transaction with a view to imposing the appropriate tax that is otherwise applicable. Pending tax bills before the National Assembly do not contain comprehensive GAAR. SA may well be the only African country with developed GAAR provisions, given the relative sophistication of its economy."*

It would seem that currently, the Nigerian anti-avoidance regime is panoply of disparate provisions. For example, in addition to *section 22, CITA* contains: *section 19* and *20* (excess dividends tax), *section 21 CITA* (deemed dividend distribution), *section 58* (power to call for further returns), and *section 65(3)* (best of judgement assessment). The *CGTA's sections 19, 21* and *22*, deal with bargains comprising two or more transactions, market value, and transactions between connected persons, respectively. Also, *PITA's 2nd Schedule* has provisions to counter farcical trust arrangements (e.g. where settlor has control/ can deal with trust assets).

*Section 19 CGTA* is deserving of illustrative analysis. *19(1)* prescribes a 'single disposal' treatment where although factually there were several transactions, they (in substance) relate to a single bargain. The legislative intent here must be to prevent splitting to obtain advantageous treatment. However, under *section 19(2)*, separate considerations must be treated as one for the purpose of nilling out advantageous treatment, were they to be reckoned separately. The opportunity for the Revenue's intervention is in "apportioning" the consideration between the transactions, presumably guided by arms' length considerations. *Section 19(3)* is interesting: if the application of *section 19(2)* will produce a more favourable result (overall, e.g. because a more apportionment respectively produces nil or low CGT liability), then the Revenue will "accept" the respective agreed considerations!

What makes transactions artificial? It clearly should not be because the transaction is novel, or perceived as complex. Generally, industry trends progressively evolve and develop, leading to growth', which is reflected in transaction structures. *Section 22 CITA* seemingly leans against creativity in proffering more efficient ways of doing transactions. Would rule of the thumb (subjective rather than objective tests), suffice in performing these aspects of the tax regulatory role?

A key issue is that the provisions have been defined at a basic level, and have remained so ever since. For example, *section 22 CITA* is exact reproduction of *section 18 CITA, Cap. 60, LFN 1990*, itself reproduced from *section 18 CIT Decree 1979*. In other climes (Canada, Australia, etc), amendments of anti-avoidance provisions are more periodic, especially as responsive strategy to keep up with aggressive tax avoidance schemes. In the USA, structuring and sale of 'tax shelter' products is a notorious example; response initiatives include the stringent requirements of the *Foreign Account Tax Compliance Act 2010 (FATCA)*. Space constraints detailed consideration of approaches adopted by different countries on GAAR, but tax legislation/amendments is almost an annual ritual in most developed economies.

## Conclusion

Despite this panoply, our anti-avoidance provisions when compared with other jurisdictions seem to be elementary, and may require comprehensive review: Nigeria needs its own 'modernised' GAAR. At the moment, consolation may be found in 'omnibus' provision such as section 19 CITA which deem dividends, where they exceed taxable profits (however arising), as taxable profits for that year. But this may still not be comprehensive enough, for example a company with more than five shareholders (because of *section 21 CITA*) may not declare dividends that year in order to avoid exposure to excess dividend tax!

Pending legislative action, we will continue to count on ingenuity of tax practitioners, the Revenue and the courts to address these issues.

***Postscript:*** After the original publication of this article in February 2012, the Income Tax (Transfer Pricing) Regulations No. 1, 2012 was issued by the FIRS, with a commencement date of 1st August 2012. This author's review, *'TP Regulations: Compliance, "Stay Awake" Issues & Litigation', ThisDay Lawyer, 2nd April 2013, p.12*, is also available here on LeLaw website.

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