IN THE TAX APPEAL TRIBUNAL
LAGOS ZONE
HOLDEN AT LAGOS

APPEAL NO: TAT/LZ/012/2014

BETWEEN:

TOTAL EXPLORATION & PRODUCTION NIGERIA LIMITED **APPELLANT**

AND

FEDERAL INLAND REVENUE SERVICE **RESPONDENT**

JUDGMENT

ISSUES FOR DETERMINATION

In determining this appeal, the Tribunal had to consider the following issues:

1. Whether the interest paid on a loan obtained from a related company is tax deductible.
2. Whether dividends from gas income is subject to withholding tax under CITA.
3. Whether balancing charges should be applicable to asset acquired and disposed of in the same year and for which no capital allowance has been claimed.
4. Whether reference to any allowances due in paragraph 9 of the 2nd schedule to the PPTA includes Petroleum Investment Allowance.
5. Whether balancing charge is a profit that is subject to Education Tax.

Issue one

Whether the interest paid on a loan obtained from a related company is tax deductible.

Section 10[1][g] of the PPTA allows deduction of interests on inter-company loans. However, for the interest to be deducted as an expense the loan must have been secured at an arm's length and the interest therein must have been paid.

The Appellant's case is that the loan of US$790,000,000 from TOTAL FINANCE was on terms prevailing in the open market and as such the loan was obtained on arm's length terms. It was submitted that these facts were never disputed by the Respondent and as such need no further proof. The Appellant also contended that the fact that a total sum of US$47,107,664 was paid as interest on the loan was also not disputed.

The Respondent argued that Section 10 [1][g] does not apply in the instant case because the Appellant and TOTAL FINANCE are related entities. The Respondent also submitted that for Section 10 [1][g] to be applicable, the lending company must not be specialized in the business of granting loan and charging interests and urged the tribunal to apply Section 13[2] of the PPTA.

We have had reasons to decide similar issues on whether interests paid on loan between related companies are tax deductible. Our position is that the intention of the lawmakers is to allow companies deduct tax for such sums incurred by way of interest on any loan they obtain for their petroleum operations provided the related companies transacted at arm's length under terms prevailing in the open market.

The legislature intends that for tax purposes, related companies should, from the enactment of Section 10[1][g] begin to enjoy the tax deduction always allowed non-related companies when they transact as though un-related. See *Nigeria Agip Oil Company Ltd v Federal Inland Revenue Service* [consolidated appeals] TAT/LZ/015/2014 & TAT/LZ/016/2014 delivered on 18th September, 2014.

The Appellant obtained the loan from TOTAL FINANCE and paid interest on the loan. There is nothing suggesting that the loan transaction was not at arm's length. The interest payments therefore qualify as deductible expense under Section 10[1][g]of the PPTA. This conclusion is consistent with our earlier decision in *Nigeria Agip Oil Company Ltd v. FIRS* [supra] and *Shell Petroleum Development Company Nigeria Ltd v. FIRS*– TAT/LZ/003/2014 & TAT/LZ/006/2014. We therefore resolve this issue in favour of the Appellant.

Issue two

Whether dividends from gas income is subject to withholding tax under CITA.

The postulation of the Appellant on this issue is that it declared dividends from accounting profits of its combined petroleum operations revenue. It has not made any dichotomy between dividends paid on gas profit and on oil profits. The Appellant argued that it cannot be held to be liable to pay WHT on gas dividends as no dividend was paid out of profit from gas income. The Appellant went further and offered an alternative argument that in the event that the tribunal holds that dividend, or a proportion of it was derived from profits from gas income, the dividend would still not be subject to withholding tax under CITA.

According to the Appellant, the effect of Section 11[2][d] of PPTA is that the company's expenses incurred exclusively in the utilization of associated gas is to be treated as income and profit under CITA and that section 60 PPTA prohibits the Respondent from subjecting the Appellant to tax on a dividend deemed to have been paid from gas profits.

The Respondent on the other hand submitted that the provision of Section 11[2][d]of the PPTA is clear and unambiguous in granting incentive to the Appellant in respect of expenses incurred on the utilization of associated gas. The Appellant's gas income is taxable under CITA and as such the dividend paid from gas income cannot be subject to the protection of Section 60 of the PPTA.

We have reviewed the facts and evidence of the parties against the backdrop of the relevant sections of CITA and PPTA cited by the parties. Section 11[2][d] PPTA provides:

> "The incentives specified under subsection [1] of this section shall be subject to the following conditions, that is:
>
> > [d] expenses identified as incurred exclusively in the utilization of associated gas shall be regarded as gas expenses and be allowable against the gas income and profit to be taxed under the companies income tax act.

The above provision in our view directs that a company must set aside expenses incurred for associated gas utilization and the company's gas income and profit should be taxed under CITA. It puts gas income tax squarely under CITA

including the withholding tax provisions. We have earlier decided in *Shell Petroleum Development Company of Nigeria Ltd v. FIRS* TAT/LZ/004/2014 judgment delivered on 10th February 2015 that a company's gas income is taxable under CITA and that Section 60 of PPTA does not cover taxation of gas incomes. Invariably, the Appellant is not prevented from charging WHT on the dividend paid by it on its gas income.

CITA governs gas income and all taxable gas income derivatives. The Appellant is therefore liable to pay withholding tax on the dividend attributable to profits from gas income. Since the Appellant failed to separate the dividend paid from gas income from that of the oil income and has not disputed that gas income is part of the income from which dividend was paid to its shareholders, it follows therefore that it must succumb to the diligence and fairness mechanism applied by the Respondent to extract the percentage of the aggregate dividend attributable to gas and compute the WHT payable thereon. This issue is therefore resolved against the Appellant.

Issue three

Whether balancing charges should be applicable to assets acquired and disposed of in the same year and for which no capital allowance has been claimed.

A conjunctive reading of paragraphs 7 and 9 of the 2nd Schedule to the PPTA is that a company that has incurred qualifying expenditure for an asset shall be assessed to balancing charge only where the company has enjoyed annual allowance on the assets and the initial allowance on an asset is due only if the company is the owner of the asset at the end of that accounting period. The Appellant contended that the Respondent was wrong in taking into account all assets on which qualifying expenditure was incurred by the Appellant for 2010-2011 accounting periods. It stated that the divestment of its interests in OML4, OML 38 and OML 41 was completed in the 2010 accounting period. The Appellant divested its interest in the assets to a third party in the same 2010 accounting period in which the assets were acquired. This is particularly true in respect of OML 4, OML 38 and OML 41. It further claimed that it did not enjoy any allowance prior to the sale of the assets.

The Respondent has a different view of the commercial activities of the Appellant in respect of these assets and the relevant provisions of the PPTA. According to the Respondent, the purpose of paragraph 9 of the 2nd Schedule of the PPTA is to bring to tax, the total of all the allowances a taxpayer had claimed in respect of the qualifying capital expenditure and that if an amount of expenditure on an asset had been allowed as tax deductible, and the taxpayer later got a refund in the form of an allowance, the refund must be brought to tax upon disposal of the asset. The Respondent viewed the Appellant's tactic of segregating the assets into tangible and intangible and relieving the intangible asset of balancing charge as an avoidance scheme which has no legal basis.

We agree with the Respondent that there is no such dichotomy as tangible and intangible asset for the purpose of qualifying capital expenditure and balancing charge. More so, the assets are sold to a third party without such dichotomy. The question therefore is whether the assets having been sold in the same year of acquisition, are subject to balancing charge.

It is on record that the Appellant claimed allowances for the year 2010-2011 on the asset contrary to the PPTA. This was explained away as an error on the part of the Appellant and that the wrongfully claimed allowances had been reversed in its 2012 tax returns. The Respondent conceded and acknowledged the fact of this reversal but maintained that its assessment is correct.

Upon the true construction of the provisions of Paragraphs 7 and 9 of the 2nd schedule to the PPTA the Appellant is not liable to include the assets it disposed of in the same accounting period it acquired them in the calculation of balancing charge as no capital allowance has been validly claimed in respect of the assets. We therefore resolve this issue in favour of the Appellant.

Issue four

Whether reference to any allowances due in paragraph 9 of the 2nd schedule to the PPTA includes Petroleum Investment Allowance.

The Respondent insisted on a conjunctive reading of the provisions of Paragraphs 9, 10 and 5(2) of the 2nd schedule of the PPTA and submitted that the annual allowance is arrived at by adding to the other allowances the

Petroleum Investment Allowance. The Respondent further argued that the Annual Allowance and Petroleum Investment Allowance are employed for the same purpose in the determination of balancing charge.

The Appellant held a contrary view and submitted that on the authority of *Cape Brandy Syndicate v. Commissioner of Inland Revenue* (1921) 1KB 64, and *FBIR v. Ibile Holdings* 920 TCRN March, 2010 that the tribunal should not read into the statute what is not in the statute. The Appellant further cited the decision of this tribunal in *Shell Petroleum Development Company of Nigeria Ltd v. FIRS* consolidated Appeal Nos TAT/LZ/008/2014 & TAT/LZ/009/2014 which held that Petroleum Investment Allowance is extraneous to the determination of balancing charge.

We are persuaded by the submission of the Appellant and the existing authorities on this issue. We affirm our earlier decision in Shell *Petroleum Development Company of Nigeria Ltd v. FIRS* (*supra*) that Annual Allowance and Petroleum Investment Allowance though subject to the same rule under the PPTA are separate and distinct allowances. Where one is categorically mentioned to the exclusion of the other, that other's inclusion is not intended. We therefore hold that Petroleum Investment Allowance cannot be rightly included in the Annual Allowance for the purpose of determining balancing charge under paragraph 9 of the PPTA. We resolve this issue in favour of the Appellant.

Issue five

Whether balancing charge is a profit that is subject to Education Tax.

The Appellant contended that going by the statutory provisions for the ascertainment of Education Tax under the Tertiary Education Trust Fund [Establishment] Act, 2011, the tax is derivable from the assessable profits of the company. The annual allowances which is the determinant factor in calculating balancing charge has to be deducted at the point of ascertaining the assessable profits of the company and as such the balancing charge is not subject to Education Tax.

The Respondent on the other hand submitted that under Paragraph 9 of the 2nd Schedule to the PPTA, a balancing charge is treated as an income of the

company and is therefore subject to Education Tax. The Tertiary Education Trust Fund [Establishment] Act, 2011 provides at S. 1 [2][3]

> "[2] The tax at the rate of 2 per cent shall be charged on the assessable profits of a company registered in Nigeria.
>
> [3] The assessable profit of a company shall be ascertained in the manner specified in the Companies Income Tax Act or the Petroleum Profits Tax Act as the case may be."

The question is whether a balancing charge will form part of a company's assessable profit in which case it will be subject to Education Tax. The Respondent simply contended that it is treated as income in Paragraph 9 of the 2nd Schedule to the PPTA as such it is subject to Education Tax. The Appellant submits that because balancing charge is not ascertainable until after moving from assessable income to chargeable income at least in accounting practice, it cannot be subject to Education Tax.

There is no dispute that the Appellant has paid its Education Tax on its assessable profit. We hold the view that since Education Tax is payable on assessable profit which is the adjusted profit to which balancing charge is not inclusive, the Appellant is not liable to pay Education Tax in the balancing charge. This issue is therefore resolved in favour of the Appellant.

CONCUSION

In the result the issues are resolved as follow:

1. The loan the Appellant obtained from TOTAL FINANCE and on which interests was paid was at arm's length. The interest payments therefore qualify as deductible expense under Section 10[1][g]of the PPTA.

2. The Appellant is liable to pay withholding tax on the dividend attributable to profits from its gas income. Since the Appellant failed to separate the dividend paid from gas income from that of the oil income and has not disputed that gas income is part of the income from which dividend was paid to its shareholders, it must succumb to the diligence and fairness mechanism applied by the Respondent to extract the percentage of the

aggregate dividend attributable to gas and compute the WHT payable thereon.

3. The Appellant is not liable to include the assets it disposed of in the same accounting period it acquired them in the calculation of balancing charge as no capital allowance has been validly claimed in respect of the assets.

4. Petroleum Investment Allowance cannot be rightly included in the Annual Allowance for the purpose of determining balancing charge under paragraph 9 of the PPTA.

5. The Appellant is not liable to pay Education Tax in the balancing charge.

LEGAL REPRESENTATION

I.Berenibara Esq. with Ms A. Adewusi and J. Dasun Esq. for the Appellant

Jerome Okoro Esq. for the Respondent.

DATED THIS19TH DAY OF MAY, 2016

KAYODE SOFOLA, SAN (Chairman)

CATHERINE A. AJAYI (MRS)
Commissioner

D. HABILA GAPSISO
Commissioner

MUSTAFA BULU IBRAHIM
Commissioner

CHINUA ASUZU
Commissioner

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DATE 18/04/2018