

**IN THE TAX APPEAL TRIBUNAL
IN THE LAGOS ZONE
HOLDEN AT LAGOS**

APPEAL NO: TAT/LZ/020/2014
APPEAL NO: TAT/LZ/021/2014
APPEAL NO: TAT/LZ/022/2014
APPEAL NO: TAT/LZ/023/2014

BETWEEN:

**THE SHELL PETROLEUM DEVELOPMENT COMPANY
OF NIGERIA LTD**

.....

APPELLANT

AND

FEDERAL INLAND REVENUE SERVICE

.....

RESPONDENT

JUDGMENT

The Appellant filed Notices of Appeal against 4 Notices of Additional Assessment raised against it for Petroleum Profit Tax (PPT) and Education Tax (EDT) as follows:

1. Appeal No: TAT/LZ/020/2014 against Respondent's PPT Notice of additional assessment No PPBTA 106 for 31st December 2008 to 31st December, 2011 in the sum of \$4, 631,909.
2. Appeal No: TAT/LZ/021/2014 against Respondent's PPT Notice of Additional Assessment No PPBTA 107 for 31st December, 2008 to December 2011 in the sum of \$84, 100,553.
3. Appeal No: TAT/LZ/022/2014 against Respondent's PPT Notice of Additional Assessment No PPBTA 108 for 31st December 2009 to 31st December 2010 in the sum of \$4, 205,027.
4. Appeal No: TAT/LZ/023/2014 against the Respondent's EDT Notice of Additional Assessment No PPBTA/ED 97 for 31st December, 2008 to 31st December, 2011 in the sum of \$108, 986.



The Appellant had made deductions pursuant to 3 Modified Carry Agreements (MCAs) between it and NNPC for tangible and intangible costs allegedly incurred in its petroleum operations. They had not been approved by NNPC. The Respondent rejected the deduction of Petroleum Investment Allowance on the unapproved tangible MCA costs. The 4th appeal concerned the EDT derived for the period.

The Appellant filed 4 notices of appeal which were consolidated pursuant to an order of the Tribunal of 10th July, 2014. The Appellant called a witness and tendered documentary evidence in support of its case. The Respondent also called a witness and tendered documents in support of its case.

BACKGROUND FACTS:

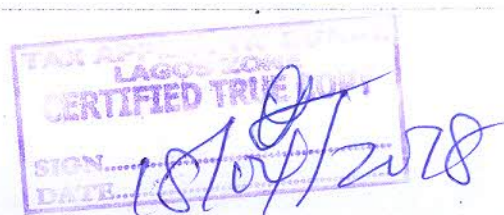
The Appellant had claimed capital allowance in respect of 2008 – 2011 YOAs in respect of Qualifying Capital Expenditure [QCE] in its returns which it claimed it incurred under Section 20 and the Second Schedule of the PPT Act. This arose due to NNPC's inability to meet its cash call obligations and were in accordance, in the view of the Appellant, with the MCAs and are described as "Disproportionate Expenditure" being in excess of the Appellant's participating interest in the JV, claiming they satisfied the "wen" test i.e. were wholly, exclusively and necessarily incurred for petroleum operations.

The Respondent raised additional PPT and EDT on the Appellant's profit in respect of the unapproved tangible/intangible cost for the 2008 – 2011 YOAs.

The Appellant contends that the statutory responsibility to evaluate the expenses and determine whether they satisfied the "wen" test is placed entirely on the Respondent.

The Appellant formulated 3 issues for determination as follows:

1. Issue One: Whether the expenditure incurred by the Appellant pursuant to the Modified Carry Agreements (MCAs) constitutes Qualifying Capital Expenditure incurred in the course of petroleum operations in respect of which the Appellant is entitled to claim Capital Allowance under the PPT Act?
2. Issue Two: Whether the Appellant is entitled to claim Petroleum Investment Allowance (PIA) in respect of the expenditure it incurred pursuant to the Modified Carry Agreements [MCAs]?
3. Issue Three: Whether the Appellant is liable to additional Education Tax?



The Appellant cited some reported cases as well as the decision of this Tribunal in Total Exploration Productions Nigeria Limited & 3 Ors v. FIRS in TAT/LZ/010/2013 delivered on 20th March, 2015, to buttress the point that the Respondent cannot rely on a third party, in this case NNPC, the discharge of its statutory responsibility which requires it to determine if its expenses were compliant with PPT Act with regard to the Education Tax the Appellant contends that it can only arise on a valid additional PPT which is not the case in the instant appeal.

The Respondent contends that the costs in question were “unapproved” tangible and intangible MCA costs and PIA on “unapproved” tangible MCA costs for the following projects:

Gbaran Ubie Gas Project.
Nembe Bundle Oil Project, and
Cawthorne Channel Oil Project:

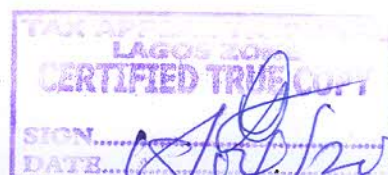
The parties had agreed to carry NNPC share of required capital costs via the Modified Carry Agreements which provided for monthly and annual reconciliation meetings which include the carried capital costs and are jointly signed by the parties. Only the verified costs which are agreed are allowed for recovery, in the submission of the Respondent. An audit of 2008 – 2011 returns showed some unapproved tangible and intangible costs were discovered which led to the FIRS rejecting those deductions and culminated in the additional assessments. Hence these appeals following the refusal of the Respondent to yield to the Appellant’s objections. The Respondent for its part formulated only one issue for determinations.

“Whether or not the Respondent was right to have disallowed the deduction of MCA expenses as deductible expenses by the Appellant in its returns.”

In summary, the Respondent recognises the right of the Appellant to recover 85% of the Carry Capital Costs subject to the verification such expenses at the reconciliation meetings which were also attended by the Respondent. This is not based on the cost estimates but rather the costs incurred, verified and substantiated. But for the MCA these costs were not claimable by the Appellant but rather were claimable by NNPC.

In her oral submission learned counsel for the Respondent submitted that the needed reconciliation meeting had not been held and that the deductibility of the expenses in question was “not ripe for recognition.”

Learned counsel for the Appellant for his part restated the positions that this case was predicated on s. 20 of the PPTA and the Respondent had abdicated its responsibility by not undertaking the verification as stipulated by the statute but sought refuge in the non-recognition by NNPC under the terms of the MCAs.



We have reviewed the submissions of counsel and the evidence adduced by the parties in this appeal. We accept the Respondent's submission that costs estimates differ from costs incurred and verified. The relevant verification is to be carried out by the Respondent which is why the Appellant submitted its returns and produced the papers sought by the Respondent for verification. The substance of the Respondent's case is that the required verification has not been carried out. We have held that the relevant party to verify the returns is the Respondent.

As we held in *Total Exploration and Production Nigeria Limited & 3 Ors. v. FIRS*, appeal no TAT/LZ/011/2013 delivered on 20th February 2015 and several other appeals:

"The Appellants' PPT returns were jettisoned by NNPC. The Respondent relied on the PPT returns prepared and filed by NNPC to assess the Appellants to Education Tax for 2012 year of assessment. The PSC has accorded NNPC the right to attach competent staff to the Contractor (Appellants) to give effect to Clause 13.1. And by virtue of Clauses 12.4 and 13.1, NNPC is deemed to have participated in the preparation of the PPT returns generated by the Appellants. NNPC only has right of participation in the preparation of the PPT returns while still in the domain of the Appellants. The Appellants' PPT returns are the foundation for the determination of their tax affairs by the Respondent. If NNPC has cause to file returns other than the one submitted to it by the contractors of OML 138, it owes the contractors explanation or consultation'. But the Respondent appears to say it does not care whether the figures are wrong or not- it cares only that they were filed by NNPC who has the duty of filing it under the PSC.

Cooperative Compliance is the current global trend at stimulating voluntary compliance and enhancing the integrity of the tax authorities. The Respondent must make conscious efforts at building cooperative relationships with taxpayers. The Respondent must 'view the taxpayer's claims and objection within the overriding objective of its responsibilities for the entire tax regime'. The Respondent can 'direct NNPC to review the areas of the Appellants' objection and confirm the genuineness of their claims'. It could also 'invite all parties to OML [138] Contract Area for round table discussion on the tax affairs where conflicting returns are presented to it"

In the final analysis, the Respondent must itself discharge its statutory responsibility of verification. In the result, we direct that the Respondent should discharge its duty to ascertain which expenses are wholly, exclusively and necessarily incurred for the purpose of petroleum operations in accordance with Section 20 of the PPT Act. This obligation is independent of the view of the NNPC at the Reconciliation meeting.

We direct the Respondent to determine the deductibility of the expenses in question bearing in mind the provision of the PPTA within 60 days from today and issue the appropriate Notices of



Assessment accordingly. The inchoate assessments PPBTA 106, PPBTA.107, PPBTA 108 and PPTBA/ED 97 which had not taken these materials into consideration are hereby discharged.

Legal Representation:

Chukwuka Ikwuazom Esq. with Shehu Mustafa Esq., Mrs Oluwafikayomi Ogunrinde and Tochukwu Anaenugu for the Appellant.

A. A. Iriogbe (Mrs) for the Respondent.

DATED AT LAGOS THIS 27TH DAY OF OCTOBER 2015



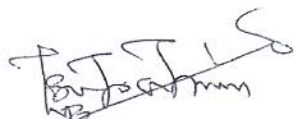
KAYODE SOFOLA, SAN (*Chairman*)



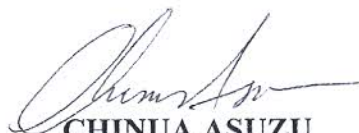
CATHERINE A. AJAYI (MRS)
Commissioner



D. HABILA GAPSISO
Commissioner



MUSTAFA BULU IBRAHIM
Commissioner



CHINUA ASUZU
Commissioner

