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

TAT/LZ/VAT/008/2015
TAT/LZ/WHT/009/2015
CONSOLIDATED APPEALS

Between

Brasoil Oil Services Company (Nigeria) Limited **Appellant**

And

Federal Inland Revenue Service (FIRS) **Respondent**

Judgment

Introduction

The Appellant challenges the Respondent's Value Added Tax (VAT) Re-assessment No. LD/OG/US/VAT/14/11 and Withholding Tax (WHT) Demand Notice No. LD/OG/US/WHT/14/19 both datedSeptember 26, 2014.

a. The Appellant disagrees with the Respondent's VAT Re-assessment of US$303,808 –with interest and penalties – for 2006, 2007, 2008, 2010, and 2012 accounting years.

b. The Appellant disagrees with the Respondent's WHT assessment of US$607,616 – with interest and penalties – for 2006, 2007, 2008, 2010, and 2012 accounting years.

Issues for Determination:

The Appellant formulated the following four issues for determination:

1. Is the Appellant liable to pay VAT on reimbursement of expenses incurred by a third party on behalf of the Appellant under the Value Added Tax Act?

2. Is the Appellant liable to deduct WHT on salaries and reimbursement of expenses incurred on its behalf and remit same to the Respondent?

3. Is VAT payable on income earned and WHT applicable to expenses incurred outside Nigeria?

4. Is the Appellant liable to interest and penalties after validly objecting to the Respondent's assessments and subsequently filing appeal at the Tribunal?

The Respondent posed a single issue for determination as thus:

Did the Appellant incur WHT and VAT in the course of the execution of its contract with Petrobras?

Facts of the Matter in Brief:

The Respondent conducted audit of the Appellant's records in November 2013 and found that Petrobras SA provides technical support services to the Appellant. The Respondent found that the Appellant incurred US$4,860,927 for 2006 – 2008, 2010 and 2012 under the Technical Services Agreement (TSA) it signed with Petrobras SA. Based on this figure, the Respondent raised VAT and WHT assessments for the period. The Technical Services Agreement is dated 1st June, 2010 and admitted in evidence as **Exhibit AO1.**However, Petrobras SA provided technical support to the Appellant from year 2006 to 2008 on the basis of service agreement (not in evidence in this case) whose terms are said to be similar to the 2010 service agreement.

Under the TSA Petrobras SA invoices the Appellant for its services at a mark-up of 12% as well as for reimbursable expenses incurred on the Appellant's behalf.

Parties' Arguments:

Issue 1: Is the Appellant liable to pay VAT on reimbursement of expenses incurred by a third party on behalf of the Appellant under the Value Added Tax Act?

The Appellant submits that section **2 of the Value Added Tax Act, Cap V1 Laws of the Federation of Nigeria, 2014** imposes VAT only on the supply of specified taxable goods and services. But the Act does not make VAT applicable to reimbursement of expenses incurred in the course of supplying services to a

Nigerian company such as the Appellant. And that the Respondent is wrong to say that reimbursement expenses incurred by a non-resident company on behalf of the Appellant is caught by section **10(2) of VAT Act.**

The Appellant commends to this Tribunal the decision in **Gasprom Oil & Gas Ltd v FIRS (2015) 19 TLRN 66 at 96-97** where the Abuja Zone of the Tax Appeal Tribunal held that VAT liability pursuant to section 10 of the VAT Act must be premised on seven interrelated conditions.

The Appellant argues that by reason of the fact that there is no VAT liability on the reimbursable expenses, no VAT was charged by Petrobras SA on the invoices it issued the Appellant.

The Appellant has led evidence before the Tribunal, contained in the witness statements of its witness – Akinniyi Odedele (admitted and marked as **Exhibits AO and BAO**) to show that the sums which the Respondent alleges is subject to VAT are reimbursable expenses incurred by Petrobras SA on behalf of the Appellant. The Appellant says **Exhibit AO1** also corroborates this assertion.

The Appellant further states that its witness testified that while there was no written Technical Service Agreement (TSA) between the parties in the period between 2006 and 2008, the services provided were on the same terms as the TSA which was executed between the Appellant and Petrobras SA in 2010. Accordingly the parties' agreement as codified in Clause 3.3 of the 2010 TSA provides that *"Reimbursement of travel costs and expenses (airplane tickets, lodging, ground transport, communication, man hours spent and others) related to the performance of the Services shall be reimbursed ..."*

The Appellant argues that **Exhibits AO and BAO** demonstrate that the amounts in dispute are as follows:

a. 2006 – 2008 years of assessment: reimbursable expenditure (travel costs, accommodation, feeding etc).
b. 2010 year of assessment: reimbursable expenditure and income paid to employees on secondment from Petrobras SA.
c. 2012 year of assessment: income paid to employees on secondment from Petrobras SA.

The Appellant submits that the Respondent did not controvert the testimony of the Appellant's witness nor did it impugn the documentary evidence tendered by the Appellant. Thus, the Appellant urges this Tribunal to give full probative

value to this evidence in line with the decision of the Court of Appeal in the case of **Agomuo v Ogwuegbu**[1999] 4 NWLR (Pt. 599) 405 at 413.

The Appellant also submits that, if at all any VAT is payable on the transactions covered by the expenses, it would have been charged and paid on the original transaction between Petrobras SA and the third party suppliers. The Appellant says the third party vendor is the taxable person with the obligation to deduct and remit the VAT.

But the Respondent argues that the supply of technical support services is not an exempt service under the First Schedule of the VAT Act. That the cost of rendering the technical services plus the mark-up represents the value of VATable service chargeable to VAT. The Respondent says VAT is a multi-stage tax chargeable at each stage of a transaction.

The Respondent submits that the cost of the expatriate salary arose out of the execution of the TSA and hence is VATable. And that the services rendered by Petrobras to the Appellant cannot qualify as an exported service because the Appellant is a resident company and the services were performed in Nigeria. The Respondent adds that under section **10 of the VAT Act**, Petrobras is required to register for VAT using the address of the Appellant with which it has a subsisting contract. The Appellant is then to deduct VAT and remit to FIRS.

The Respondent argues that this Tribunal agreed that **section 2 of the VAT Act** renders VATable all transactions in goods and services backed by consideration. See this Tribunal's decision in **Vodacom Business Nig. Ltd v FIRS TAT/LZ/VAT/016/2015.**Thus, the Respondent maintains that since the services rendered to the Appellant by the foreign company is for a consideration, it isVATable.

Issue 2: Is the Appellant liable to deduct WHT on salaries and reimbursement of expenses incurred on its behalf and remit same to the Respondent?

The Appellant argues that section **13(2)(d) of CITA** provides the basis for imposing tax liability on non-resident company such as Petrobras SA.

The Appellant also submits that **Exhibit AO** demonstrates that the TSA between the Appellant and Petrobras SA complied with the arms-length principle. In particular, **Clause 3.2.1 of the 2010 TSA** imposes 12% mark-up on the compensation schedule agreed by the parties and the Respondent has not challenged the transactions as artificial.

Thus the Appellant is only liable to WHT on the sum representing the 12% mark-up on the compensation schedule agreed by the parties. Accordingly, the Appellant has already deducted and remitted the WHT on the mark-up as per **Exhibit AO8.**

The Appellant argues that CITA does not impose tax liability in respect of salaries paid to expatriate employees seconded to the Appellant for the provision of technical services. The Appellant also says its sole witness gave evidence at paragraph 25.3 of **Exhibit AO** that the reimbursable expenditure did not form part of the compensation to Petrobras SA under the TSA.

The Appellant further submits that in paragraphs 25.4 and 25.5 of **Exhibit AO** its witness testified that it remits Pay-As-You-Earn (PAYE) taxes from the salaries of these workers to the appropriate tax authority. The Appellant also tendered copies of invoices and payments made by the Appellant and Petrobras SA as well as PAYE receipts issued by the Lagos state government for deductions made from seconded personnel – **Exhibit AOX.**

The Respondent submits that the same **section 13(2)(d)** which the Appellant is relying upon empowers the Respondent with discretionary powers to impose taxes where lack of arms-length exist as in this case. The Respondent says that the Appellant computed the value of the contract itself and purportedly based it on the 12% mark-up it determined.

The Respondent avers that the transactions subjected to WHT are in respect of the technical services received from the parent company, Petrobras SA, as per the Appellant's audited financial statements and not for reimbursement of expenses. The Respondent says, the substance of the transaction amongst others is that the Appellant cannot be reimbursing Petrobras their employees' costs. The contentious costs were rather incurred by Petrobras in the performance of the technical service for the Appellant for which Petrobras was paid US$4,860,927. The WHT is not in any way based on income but on payments for specified transactions and the amounts in the Appellant's financial statements representing costs on the technical services. The Respondent insists that it charged WHT only on the fees paid to Petrobras in line with the provisions of CITA. The Respondent also relies on the Companies Income Tax (Rates, etc of Tax Deducted at Source (WHT) Regulations (Schedule to CITA).

The Respondent also argues that giving effect to Clause 3.2 of the TSA requires Petrobras to display the quantum of tax payable on the invoices raised on the Appellant. And failure to do this renders both the Appellant and Petrobras liable.

Issue 3:

The Appellant posits that Nigerian tax statutes do not apply extraterritorially as in **JGC Corporation v FIRS (2015)** (Unreported decision of the FHC Lagos Division [Coram Idris J.] delivered on 18 September 2015 in **Appeal No. FHC/L4A/15)**. Expenditure incurred wholly outside Nigeria is not liable to VAT.

The Appellant argues that the Respondent has stated in its Reply that the WHT assessment is in respect of services rendered by Petrobras to the Appellant and not based on reimbursement of expenses. In this regards, the Appellant submits that a greater percentage of the technical services provided by Petrobras to the Appellant were provided outside Nigeria as demonstrated by **Exhibit AOX.**

The Reassessment and Demand Notices contested by the Appellant, included as taxable, amounts charged to the Appellant by Petrobras SA which were based on expenditure incurred outside Nigeria. Thus the Appellant asserts that these expenditure incurred outside Nigeria are not subject to VAT or WHT.

The Respondent also argues that the technical support service was performed in Nigeria based on the TSA terms. The Respondent opines that the place of performance is not even contentious because the Appellant has said that the tax should be based on mark-up.

The Respondent asserts that under section **13(2)(a) of CITA,** the profit of a non-resident company is deemed to be derived in Nigeria to the extent that it is attributable to a fixed base in Nigeria. That to the extent the staff of Petrobras SA continuously perform this service in the premises of the Appellant – it constitutes a fixed base – and hence the income is subject to tax in Nigeria.

Issue 4:

The Appellant states that even if it is liable to tax, interests and penalties are only applicable where the assessment has become final and conclusive, which in this case is not. The Appellant commends to this Tribunal the decision in **FIRS v Mobitel** (unreported decision of the Tax Appeal Tribunal Lagos Zone in Appeal No. **TAT/LZ/VAT/082/2014)** where the Tribunal held that an assessment must have become final and conclusive for interest to be chargeable. In support of its

position, the Appellant also cites section **32 of the FIRS (Establishment) Act 2007; Paragraph 13(3) of the Fifth Schedule of the FIRS Act; sections 77(2) and 85(1) of CITA; and section 9(1) of the VAT Act.**

The Appellant further argues that a company which has objected or appealed against tax charged by an assessment cannot be said to be in default nor can it be charged liable to penalties for non-payment of a disputed tax liability. In other words the existence of pending objection or appeal puts the timeline in abeyance until there has been a final determination of the objection or appeal. In Appeal No. **TAT/LZ/013/2014, Weatherford Services S.D.E.R.L. v FIRS,** this Tribunal held that "interests and penalties on overdue tax start to run when the tax payer does not object or appeal within 2 months."

The Respondent avers that section **13(1) and (2) of the VAT Act** requires a company to deduct VAT at source. And the due date for remittance is provided in **section 15 of the VAT Act and section 32 and 40 of the FIRS (Establishment) Act 2007.** The FIRS (Establishment) Act provides for penalty and interest where taxes are not remitted on due dates.

Analysis:

We shall treat all the issues together. The Appellant says all the expenses under the TSA are reimbursable except for the 12% mark-up. In paragraph 40 of its written address the Appellant says "... *the Appellant is only liable to deduct and remit WHT to the Respondent in respect of the sum representing the 12% mark-up on the compensation schedule agreed by the parties. The Appellant's position is buttressed by the fact that the 12% mark-up on the compensation schedule amounts to income in the hands of Petrobras SA in respect of which the Appellant is liable to deduct and remit WHT. The Appellant has already tendered before this Tribunal* ***exhibit AO8*** *evidencing the remittance of WHT to the Respondent in respect of the 12% mark-up.*"

We believe this position taken by the Appellant has compromised its argument on **Issue 3** to wit Petrobras SA's transactions are extraterritorial and therefore extraneous to Nigerian tax statutes. In addition the Respondent's target in this contentious assessment, as argued by it and demonstrated in the documents before us, is the tax consequence of the contract agreement between the Appellant and Petrobras SA (a non-resident company), executed in Nigeria. Section **10 of the VAT Act** supports the Respondent's position.

We agree with the Appellant that salaries and reimbursable expenses are not subject to VAT and WHT. But are the Petrobras SA's expenses under the TSA salaries and reimbursable expenses?

Clause 3.2 of the TSA provides that *"Company (Appellant) **shall pay** Contractor (Petrobras SA), upon the issue of an undisputed invoice for the Services to be rendered hereunder, amounts based on the Compensation Schedule in force for the respective year, according to the number of man-hours actually worked in the performance of the Services. Company **shall reimburse** Contractor for travel expenses and other costs that may be incurred related to the performance of the Services in accordance with the principles of **Clause 3.3** below."*

Clause 3.3 states that *"Reimbursement of travel costs and expenses **(airplane tickets, lodging, ground transportation, communication, man hours spent and others)** related to the performance of the Services shall be reimbursed according to Contractor's policies, which Company hereby declares to be fully aware and in agreement, and subject to the following principles:*

i. Contractor shall present the respective receipts of each cost and expense subject to a reimbursement request.
ii. Only expenses directly connected with the Services will be reimbursed.

Clause 3.2.2 says *"**Contractor declares that the Compensation Schedule,** except for the costs and expenses subject to reimbursement as per Clause 3.3 below, **takes into account all costs, taxes, materials, expenses and other legal obligations for the full compliance with the terms of the Agreement throughout the term."***

Clause 3.2 of the TSA has clearly differentiated "Services" under the TSA from "Reimbursable Expenses". The "Services" fall under the "Compensation Schedule" while "Reimbursable Expenses" are those expenses extraneous to the Compensation Schedule but are incidental to the execution of the contract as spelt out more particularly in Clause 3.3.

Clause 3.2.2 provides further clarification on the two components of the expenses under the TSA and states that the Compensation Schedule takes into account all costs including taxes. This position flows from **Clause 3.2.1** which says *"... a mark-up of 12% shall be added to the amounts established in the Compensation Schedule ..."* But the reimbursable expenses are costs that are

exception to those under the Compensation Schedule and also do not qualify for mark-up. And this is exactly why the exception expenses are reimbursable while the expenses under the Compensation Schedule are contractual transaction imbedded with margin of gain – call it mark-up or profit.

The arms-length doctrine is to rid frequent artificiality in related party transactions and inject rationality of commercial transaction between unrelated parties. The Appellant's decision to mark-up the amounts established under the Compensation Schedule is a clear evidence that the contract between the Appellant and Petrobrasis equated to commercial contract between unrelated parties in the ordinary course of business. This is amplified by **Clause 1.2 of the TSA** which says"... *Company agrees to adopt the prices currently operated by the international market for services of same nature and kind of the* ***Service.***"Thus, there is no better evidence to show that the contract value contains profit element at commercial scale. Otherwise why mark-up and arms-length principle? And why benchmark it to international market prices?

The centre piece of the Appellant's argument is aimed at establishing the exact nature of the expenses to characterise them as recorded on occurrence by Petrobras to show that they are either salaries or reimbursable. Thus the weight of the Appellant's evidence was tilted to displaying how Petrobras incurred its expenses under the TSA. But the TSA has categorised the expenses as either falling under the Compensation Schedule or reimbursable – as outlined in Clause 3.3. In this context the "how" of contract execution is irrelevant and we find it to be a mere consequence of invoicing mechanism adopted by Petrobras SA. Rather we are persuaded by the nature and object of the contract which are commercial and service delivery.

The Respondent charged interest and penalties on the disputed tax. The Appellant disagrees with this position and cites our decision in Appeal No. **TAT/LZ/013/2014, Weatherford Services S.D.E.R.L. v FIRS** to wit Interests and penalties on overdue tax start to run when the taxpayer does not object or appeal within 2 months. And in this case the Appellant has objected and appealed. We are not inclined to review our decision.

Decision:

We hold that the Appellant is under obligation to deduct VAT and WHT on the contract sum of the TSA between it and Petrobras SA. But all reimbursable expenses paid by the Appellant in compliance with Clause 3.3 of the TSA are

not subject to VAT and WHT. Interests and penalties were not yet due on the disputed assessment. Accordingly, we direct the Respondent to review its assessment in accordance with this decision.

Legal Representation:

Chukwuka Ikwuazom Esq. with Hamid Abdulkarim Esq. Shehu Mustafa Esq. and Mrs. O. Ogunrinde for the Appellant.

Mrs. A. A. Iriogbe for the Respondent.

DATED AT LAGOS THIS 2ND DAY OF JUNE 2016

KAYODE SOFOLA, SAN (Chairman)

CATHERINE A. AJAYI
Commissioner

D. HABILA GAPSISO
Commissioner

MUSTAFA BULU IBRAHIM
Commissioner

CHINUA ASUZU
Commissioner