COURSE GUIDE

PUL 433
LAW OF TAXATION I

COURSE TEAM

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INTRODUCTION

Taxation law generally regulates how the income of individuals and companies are being taxed for public use. Our discussion in this semester will focus on the general principle of tax, historical background of taxation in Nigeria, tax administration and computation of income tax. We will equally discuss expenditures, taxation of business and the various forms of taxation.

COURSE LEARNING OUTCOMES

By the end of the study, you will be able to

- discuss the general principles of taxation
- explain the historical background of taxation in Nigeria
- discuss the various forms of taxation in Nigeria
- offer effective analysis of Administration of Tax.

WORKING THROUGH THIS COURSE

To complete this course, you are advised to read the study units, recommended books, relevant cases and other materials provided by NOUN. Each unit contains a Self-Assessment Exercise, and at points in the course you are required to submit assignments for assessment purposes. At the end of the course there is a final examination. The course should take you about 11 weeks to complete. You will find all the components of the course listed below. You need to make out time for each unit in order to complete the course successfully and on time.

COURSE MATERIALS

The major components of the course are.

a) Course guide
b) Study Units
c) Textbooks
d) Self-Assessment Exercises
e) Presentation schedule

MODULES AND STUDY UNITS

The discussion in this course is broken down to 14 (fourteen) study units that are broadly divided into FIVE modules as follows –

Module 1

Unit 1	General Principles of Tax
Unit 2	Historical Background
Unit 3	The Various Forms of Taxation
Unit 4	Tax Base and Income

Module 2

Unit 1	Administration of Tax
Unit 2	Free Inter-State Trade, Commerce and Limitations on Taxing Powers of the Governments
Unit 3	Persons Subject to Tax and the Determination of Residence as a Basis for Taxation.

Module 3

Unit 1	Employment Taxation
Unit 2	Definition and Ascertainment of Income Tax
Unit 3	Computation of Income Tax

Module 4

Unit 1	Deductions Allowances

Module 5

Unit 1	Taxation of Business
Unit 2	Expenditures
Unit 3	Investment

All these Units are demanding. They also deal with basic principles and values, which merit your attention and thought. Tackle them in separate study periods. You may require several hours for each.

We suggest that the Modules be studied one after the other, since they are linked by a common theme. You will gain more from them if you have first carried out work on the law of sea.You will then have a clearer picture into which to paint these topics. Subsequent units are written on the assumption that you have completed previous units.

Each study unit consists of one week's work and includes specific Learning Outcomes, directions for study, reading materials and Self-Assessment Exercises *(SAE)*. Together, these exercises will assist you in achieving the stated Learning Outcomes of the individual units andof the course.

REFERENCES / FURTHER READING

Certain books have been recommended in the course. You should read them where so directed before attempting the exercise.

ASSESSMENT

There are two aspects of the assessment of this course, the Tutor Marked Assignments and a written examination. In doing these assignments you are expected to apply knowledge acquired during the course. The assignments must be submitted to your tutor for formal assessment in accordance with the deadlines stated in the presentation schedule and the Assignment file. The work that you submit to your tutor for assessment will count for 30% of your total score.

SELF-ASSESSMENT EXERCISES

There is a self-assessment exercise at the end for every unit. You are required to attempt all the assignments. You will be assessed on all of them, but the best three performances will be used for assessment. The assignments carry 10% each. Extensions will not be granted after the duedate unless under exceptional circumstances.

FINAL EXAMINATION AND GRADING

The duration of the final examination for this course is three hours and will carry 70% of the total course grade. The examination will consist of questions, which reflect the kinds of self- assessment exercises and the tutor marked problems you have previously encountered. All aspects of the course will be assessed. You should use the time between completing the last unit and taking the examination to revise the entire course. You may find it useful to review yourself assessment exercises and tutor marked assignments before the examination.

HOW TO GET THE MOST FROM THIS COURSE

In distance learning, the study units replace the lecturer. The advantage is that you can read and work through the study materials at your pace, and at a time and place that suits you best. Think of it as reading the lecture instead of listening to a lecturer. Just as a lecturer might give you in-class exercise, you study units provide exercises for you to do at appropriate times. Each of the study units follows the same format. The first item is an introduction to the subject matter of the unit and how a particular unit is integrated with other units and the course as a whole. Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. You should use these objectives to guide your study. When you have finished the unit, you should go back and check whether you have achieved the objectives. If you make a habit of doing this, you will significantly improve yourchances of passing the course.

Self-Assessment Exercises are interspersed throughout the units. Working through these tests will help you to achieve the objectives of the unit and prepare you for the assignments and the examination. You should do each Self-Assessment Exercise as you come to it in the study unit. Examples are given in the study units. Work through these when you have come to them.

ONLINE FACILITATION

There will be about 8 hours of online facilitation provided in support of this course. You will be notified of the dates, times and location of the facilitations, together with the name and phone number of your facilitator, as soon as you are allocated a facilitator who will take you through the course. He will Keep a close watch on your progress and on any difficulties you might encounter. Your facilitator may help and provide assistance to you during the course.

Please do not hesitate to contact your facilitator by telephone or e-mail if:

- You do not understand any part of the study units or the assigned readings.
- You have difficulty with the self-assessment exercises.
- You have a question or a problem with an assignment, with your facilitator's comments onan assignment or with the grading of an assignment.

You should try your best to attend the online facilitation classes. This is the only chance to have face to face contact with your facilitator and ask questions which are answered instantly. You can raise any problem encountered in the course of your study. To gain the maximum benefit from the facilitations, prepare a question list before attending them. You will gain a lot from participating actively.

MAIN COURSE

CONTENTS

MODULE 1

UNIT 1 AN OVERVIEW OF THE GENERAL PRINCIPLES OF TAX

Unit Structure

1.1 Introduction

Tax has existed since the earliest forms of recorded government in human history. It began from ancient Egypt, when the pharaohs levied taxes in the form of shares of agricultural production and labour; to ancient Rome where farmers were required to pay a tenth of their production (decima) to the tax administration (aerarium); and even in Medieval Europe, where a similar taxation system became one source of financing for the Church. In the contemporary world, governments have developed more sophisticated systems and processes for defining who is taxed, what is taxed (the 'tax base'), how much is taxed and which personal conditions of the taxpayers should be taken into account. But what are the principles that should underpin taxation and how do these impact on our daily lives

It is today, a widely and generally accepted knowledge that taxation has a critical role to play in any economy. Taxation is therefore very central and strategic to the growth and sustenance of any economy, whether developed or still developing. There is virtually no State or government of the world today that does not depend on one form of taxation measures or the other, to generate revenue for socio-economic and infrastructural development and for other forms of economic maneuvering. The tax system in essence, is one of the most powerful tools in the hands of the government to stimulate and control its economic and social affairs as far as its developmental goals are concerned. The centrality of the concept of taxation to human wellbeing in any given society was vividly captured in one of the earlier United States Supreme Court cases *(Nicholas v. Ames [1899] 173 US 509*. Here, the Court maintained that taxation is *the one great power upon which the whole national fabric is based. It is as necessary to the existence and prosperity of a natural man. It is not only the power to destroy, it is also the power to keep alive*. With these fascinating comments about the concept of taxation, the question that looms our minds is, what is taxation? It should be noted that for any concept to be meaningfully discussed the students must have a basic idea of what the concept entails; and one of the best ways of understanding the basics of any concept is by knowing its definition. The students also need to appreciate the characteristics of the concept.

In this unit, we shall give the various definitions that have been accorded tax and we shall then move on to examine the characteristics of tax, what are the things that must be present in a tax. We shall also examine the nature of tax as well as the characteristics and criteria used in identifying an ideal tax. Then we shall look at the importance of levying and payment of tax.

1.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- Defining the concept of tax and taxation
- Stating the criteria used to identify a particular payment as tax.
- Differentiating between tax and other types of payments like toll, fare etc.
- Understanding the importance of levying and paying tax in Nigeria.

1.3 General Principles of Tax

1.3.1 The Definition and Nature of Taxation

In a plain language, the *Oxford English Dictionary* (1973) has defined tax as ‘a compulsory contribution to the support of government levied on person’s property, income, commodities, transactions, etc, now at a fixed rate proportionate to the amount on which the contributions are levied’. However, to further simplify this definition, the *Oxford Advanced Learner’s Dictionary* (2006) defined tax as ‘money that you have to pay to the government so that it can pay for public services.’ It further concluded that ‘people pay tax according to their income and businesses pay tax according to their profits. Tax is also often paid on goods and services.'

Another definition supplied by Investwords.com refers to tax as 'a fee charged by a government on a product, income or activity.'

The word tax was further judicially defined in the Australian case of *Mathews v Chicory Marketing Board* (1938) 60 CLR 263 as 'a compulsory exaction of money by a public authority for public purpose or raising money for the purpose of government by means of contributions from individual persons.'

According to *Charles E. McLure, Jr. "Taxation". Britannica, March 2015,* tax can be defined as a compulsory financial charge or some other type of levy imposed on a taxpayer by a governmental organization in order to fund government spending and various public expenditures. Tax is a compulsory contribution made to state revenue, imposed by the government on workers' income and business profits, or added to the cost of some goods, services, and transactions. The word taxation in the other hands is the, imposition of compulsory levies on individuals and or entities by governments. The levying or imposition of tax is what we refer to as taxation. Taxes are imposed in almost every country of the world, primarily to raise revenue for government expenditures, although they serve other purposes as well. Payment of tax is compulsory. Although taxes are regarded as a legal requirement, paying taxes is also considered a civic duty. Where one neglects to pay tax, the institution that oversees taxes in the country (the Federal Inland Revenue Service) will demand that you pay, otherwise, you might face penalties such as large fines or jail term.

Take note that there is no legislative definition for tax. That is, there is no definition of tax in all our laws relating to tax. Thus, we shall only rely on the available definitions.

You should also note that the definition supplied in the Oxford Dictionary has been criticized as inadequate by various writers. According to Chris White H. in his book, *Revenue Law: Principles and Practice,* the definition is inadequate because it has limited its view as to the purpose of tax. He further stated that its description of tax base was irrelevant and it places unnecessary emphasis on proportional taxation as opposed to progressive taxation. Another writer, Abdulrazaq, M. T. (1993), however tried to rectify this anomaly by adding a criterion to the incomplete definition by adding that 'taxes are imposed under the authority of the legislature that they are levied by a public purpose.'

However, despite the various definitions, you should note that a proper tax within the above definitions must be one backed by legislation and must be a deduction that gives to treasury of the authorities concerned with revenue generally. Also, the compulsory nature of tax should also be noted.

Tax should not however be confused with other forms of compulsory contribution which bear semblance with it. The criterion of the compulsory nature of tax becomes clearer when distinguishing a tax from a charge for a government service. Firstly, if a payment is a charge for a government service, some service must be provided directly to the individual. For example, there is difference between paying a bridge toll and paying a tax to be used for the defence of one's country. Secondly, the charge must be related to the service given, and not varied according to the person's ability to pay or to some other criterion such as the value of his property.

I would therefore recommend the definition supplied in *Aiyar's Concise Law Dictionary* (2009) as the most apt and encompassing definition. Tax was defined as 'a compulsory exaction of money by a public authority for public purposes enforceable by law and is not payment for services rendered.' The first known taxation took place in Ancient Egypt around 3000–2800 BC.

Self-Assessment Exercises 1

Attempt the following exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Why do you think the definition of tax supplied in the Oxford Dictionary has a flaw?
2. Discuss equity as one of the attributes of an ideal tax system

It should be pointed out here that, in the economic viewpoint or definition of taxes, transfers to governments are never regard as taxes. For instance, certain transfers to the public sector are regarded as prices. Examples are tuition at public universities and fees for utilities provided by local governments. Governments can also obtain resources by "creating" money and coins (for example, by printing bills and by minting coins), through voluntary gifts (examples include, contributions to public universities and museums), by imposing penalties (such as traffic fines), by borrowing and confiscating criminal proceeds. From the economists' viewpoint, a tax is a non-penal, yet compulsory transfer of resources from the private to the public sector, imposed on a basis of predetermined criteria and without reference to specific benefits received.

In modern taxation systems, governments impose taxes in money. However, in-kind and *corvée* taxation are major features or characteristics of traditional or pre-capitalist States and their functional equivalents. The method of taxation and the government expenditure of taxes raised is usually highly debated in political and economics spheres. While governments impose tax, the collection is performed by their agencies such as the Internal Revenue Service (IRS) in the United States, Her Majesty's Revenue and Customs (HMRC) in the United Kingdom, Federal Inland Revenue Services (FIRS) in Nigeria, the Canada Revenue Agency or the Australian Taxation Office. When taxes are not fully paid, the government may impose civil penalties (such as fines or forfeiture) or criminal penalties (such as incarceration) on the non-paying entity or individual (26 U.S.C. § 7203 in the case of U.S. Federal taxes)

1.3.2 Characteristics/Ingredients of an Ideal Tax System

By an ideal tax, we mean a good tax. Thus, various ingredients that make up a good tax shall be considered under this heading. An ideal or a good tax system should meet some basic conditions including equity/**fairness, adequacy, simplicity, certainty/transparency, and administrative ease/efficiency**, Neutrality, Ability to pay. Although opinions about what makes an ideal or good tax system will vary depending on jurisdiction, there is general consensus that these basic conditions should be maximized to the greatest extent possible. A writer, Adam Smith who, in his book, *The Wealth of Nations*, described the ingredients as ‘cannons of taxation’, and Kath Nightingale (2001) in *Theory and Practice of Taxation* stated that a good tax must possess the following:

1. **Simplicity:** A good tax system must be straightforward, simple and coherent. The concept and principles of the tax must be understood by majority of the citizens and also must be simple to operate. There must also be consistency in administration of the tax among the different strata of government.

2. **Adequacy*: This principle*** means that taxes must provide enough revenue to meet the basic needs of society. A tax system meets the test of this principle if at the end, it provides enough revenue for the government to meet up with its public obligations in terms of the provision of the required public services. Such is the case, if revenue growth each year is enough to fund the growth in cost

of services, and if there is enough economic activity of the type being taxed so rates can be kept relatively low.

3. **Equity or Fairness:** An ideal tax must be administered on the principles of equity. The principle of equity suggests that everybody should pay an equitable and fair share of his taxes. There are two types of equitable principles in the taxing system – horizontal equity and vertical equity. What we mean by **horizontal equity** is that those in equal circumstances should pay an equal amount of tax. And when we say **vertical equity**, it means that those in unequal circumstances should pay different amount of tax. The importance of this criterion is to install confidence in the tax payer who will be more willing to pay their taxes if they believe that the system is fair and equal.

4. **Ability to pay:** By this, we mean that the tax must not be unbearable for the tax payers. It must be within their financial capability. The principle requires that the total tax burden will be distributed among taxpayers according to their capacity to bear it, taking into cognizance all of the relevant personal characteristics. The most suitable taxes from this viewpoint are personal levies (income, net worth, consumption, and inheritance taxes). Historically however, there was common agreement that income is the best indicator of ability to pay. While it is understood that implementation of tax is typically through the coercive power of a public authority, the imposition of tax should not be done arbitrarily. That is why many modern institutions include some restraints on the uncontrolled levying of taxes, with parliament usually having to approve the executive’s proposals. A good example was the 1628 Petition of Rights introduced restrictions on the Crown on non-parliamentary taxation in England). There is need for careful consideration of how the forced acquisition of money affects taxpayers: on the one hand, taxation provides a fundamental source of income for running the government and providing public services; on the other, taxation reduces individual disposable income and business profits and could therefore have a negative impact on decisions about work, consumption and investments. In levying of tax, the financial ability of the taxpayers should be carefully considered.

5. **Administrative Efficiency/Ease:** The administrative costs should not be higher than the revenue yielded. Also, the tax must take into account certain factors such as, the effects on economic incentives, and whether it is compatible with desirable international economic relations. The principle envisions a tax system that is not too complicated or costly for either taxpayers

or tax agents. Rules and laws regulating the tax must be well known and fairly simple; forms are not too complicated; the State can tell if taxes are paid on time and correctly, and the State can easily conduct audits in a fair and efficient manner. The cost of collecting a tax should be very small in relation to the amount collected.

6. **Certainty:** The scope of the tax should be clear. This criterion also means the certainty that the tax can and will be enforced, because a tax that is easily evaded usually causes resentment and often a decline in tax payer morality. Also, the tax which every person is bound to pay ought to be certain and not arbitrary. Under this principle, it is the requirement that tax laws and regulations should be comprehensible enough to the taxpayer. The tax system must be as simple as possible in consideration also, of other goals of tax policy. It must be as well, unambiguous and certain—both to the taxpayer and to the tax administrator. Many every country's tax laws today, are still far from being generally understood by the public. This results not only in a considerable amount of error but also undermines honesty and respect for the law and tends to discriminate against the ignorant and the poor, who cannot take advantage of the various legal tax-saving opportunities that are available to the educated and the affluent

7. ***Transparency:*** *This principle demands that* a tax system should be such that both taxpayers and tax agents can easily find information about the tax system and how tax money generated from tax is being utilized. With a transparent tax system, everybody knows who is being taxed, how much they are paying, and what is being done with the money. people can easily find out who (in broad terms) pays the tax and who benefits from tax exemptions, deductions, and credits.

8. **Flexibility and Stability:** The tax system should be flexible especially in a federal and democratic country such as Nigeria where there are always changes in government. The need for this principle is that, if the tax system is flexible, it can be easily adopted and used by any political party in power to pursue its own socio-economic programmes at a particular political dispensation. To meet up with the requirement of this principle, a tax system must be able to provide enough room for the operation of effective incentives for private enterprise. Not only that, it must provide pace for effective modification of the distribution of income and property ***I. A. Ayua, The Nigerian Tax Law (1999***).

9. **Neutrality:** A tax must be neutral thus it must avoid distortions of the market. For instance, a selective tax, such as the sales tax, is not neutral, because it encourages the consumer to spend his money on another item rather than a taxable one.

It should be noted however, that**,** all these principles are not always followed religiously. Sometimes tax systems hit certain classes of taxpayers or kinds of consumption while leaving others relatively untouched. Sometimes tax systems lack transparency, imposing charges on some goods (eg, fuel excise) without any clear indication on our bills. Also in some cases, taxpayers are burdened with administrative tasks and bottleneck, for example filing yearly tax returns online. Sometimes the tax administration does not, or cannot, apply regulations or adequately prosecute those who evade taxes in a cost-effective manner. In each of such cases, one or two of these principles are offended.

Self-Assessment Exercise 2

Attempt the following exercises to measure what you have learnt so far. This should not take you more than 5 minutes. How important is taxation to our society?

1.3.3 The importance of Taxation

The introduction of tax is a good omen for human society. In egalitarian society, the importance of tax cannot be overemphasized. Therefore, Governments impose charges on their citizens and businesses as a way of raising revenue, which is then used to meet their budgetary and public service demands. This includes financing government and public projects as well as making the business environment in the country conducive for economic growth, provision of defense and maintenance law and order.

Areas where the Importance of Tax are mostly Felt

i. Revenue Generation

Income tax is one of the major sources of revenue for the government, and it must be reckoned with in all the government's budgets. It raises revenue to meet government expenditure. The government expenditure which requires to be met include provision of services which the free market cannot provide such as defense, law and order and parks as well as provision of services which the state feels are better provided by itself such as health services and education – often referred to as public goods. Thus, the taxes collected come back to the tax payers in the form of social amenities. Also, for the business to flourish, there has to be good infrastructure such as roads, telephones, electricity. When governments collect money from taxes it ploughs this money into development this infrastructure and turn promotes economic activity throughout the country. The concept of taxation is also important to business because government can push this money into the economy in form of loans or others funding forms. Taxes contribute in raising the standard of living in a country. The higher the standard of living, the stronger and higher the level of consumption. In addition, when there is a market for their product and services, with a higher standard of living, Business would be assured of a higher domestic consumption as well. Taxes are essential and if the proceed of tax/taxpayers' money are well used, every citizen will definitely reap benefit of these taxes.

ii. Control of Economic Activities

The imposition of tax helps the government to regulate certain types of behavior, to correct market imperfections, and to control the distribution of income or wealth. Fundamentally, however, the main reason for introduction of tax system in the society is to allocate the cost of government in some fair way. In the main, income tax has been used to encourage and discourage some activities in the private sector, though this depends on whether the policy of the government is towards encouraging or discouraging such activities. The tax system may thus be used for discouraging immoral activities such use of alcohol or purchase of cigarettes.

iii. Health and Education Sectors

Without payment of taxes, governments would be unable to meet the demands of their societies. Taxes are crucial because governments collect this money and use it to finance the huge public projects in the areas of health and education. Without taxes, government contributions to the health sector would be impossible. Taxes go to funding health services such as social healthcare, medical research, social security, etc.

Education forms one of the most deserving recipients of tax money in any economy. Governments therefore attach a lot of importance and invest as much in development of human capital which education is central in this development. Money from taxes is channeled to funding, furnishing, and maintaining the public education system.

iv. Governance and Infrastructural Developments

Governance is an essential component in the smooth running of country affairs. Poor or bad governance would have far reached chilling effects on the entire country with a heavy toll on its economic growth. Good governance ensures that the taxpayers' money is utilized in a manner that benefits citizens of the country. This money also goes to pay public servants, police officers, members of parliaments, the postal system, and others. Of a truth, without a proper and functioning form of government, there will be no effective protection of public interest.

In addition to social projects, governments also impose and collected taxes to fund sectors that are crucial for the wellbeing of their citizens including security, scientific research, environmental protection.

Some of the revenue generated from tax are also channeled to fund other numerous projects such as pensions, unemployment benefits and childcare. Without taxes it would be impossible for governments to raise money to sponsor these huge projects.

Additionally, taxes can affect the state of economic growth of a country. this is so because, taxes generally contribute to the gross domestic product (GDP) of a country. Because of this contribution, taxes help spur economic growth which in turn has a ripple effect on the country's economy; raising the standard of living, increasing job creation, etc.

As we identified earlier, taxes are tools in the hands of the government which uses same as a deterrent for undesirable activities such as the consumption of liquor, tobacco smoking, etc. this is achieved through imposition of high excise levies on these products and as a result, raise the cost of these products to discourage people from buying or selling them.

v. Important to Businesses

For a smooth operation of businesses in the country, there has to be good infrastructure such as roads, telephones, electricity, and water system. This infrastructure is developed and maintained by governments or through close partnership and involvement of the government. When governments collect money from taxes, it ploughs this money into development of this infrastructure and in turn create conducive environment which also helps to promote economic activity throughout the country.

The concept of taxation is also important to businesses because governments can fund this money back into the economy in the form of loans or other funding forms.

Taxes help in raising the standard of living in a country. The higher the standard of living, the stronger and higher the level of consumption most likely is. Businesses do well and grow when there is a market for their product and services. With a higher standard of living, businesses would be assured of a higher domestic consumption as well. The reasons for introduction of tax are almost innumerable and that underscores that reason why every citizen stand a good chance of reaping benefits of these taxes. This is why it is important that citizens endeavor to pay taxes and understand that it is meant to be more than just a “money grab” from the government.

Taxation is especially important to businessmen, who enjoy the benefits of water supply, electricity and land allocation. It also reduces the net return on investment and decreases the balance for private savings.

Taxation also has social effects as it affects the lives of nearly everybody. Personal reliefs (aids and assistance), reliefs in respect of children and tuition (scholarships and grants), reliefs on insurance policy premiums, and dependent relatives’ relief (e.g. gratuities of a dead civil servant) affect the social structure of the whole country.

Taxation further assists in the redistribution of wealth in the society. Taxes paid are used to bridge the gap between the rich and the poor. This in turn will reduce inequality among the citizens. Reducing inequality in income is considered by many developing Countries as one of the leading objectives of economic policy. Governments of many countries use income tax as one of the essential tools of income redistribution. The government therefore, often intervened to correct unjust inequality of income among citizens, through the introduction of tax system, among other programmes, which is meant to take more from the rich and less from the poor. (*Olusanya Samuel Olumuyiwa, Peter Medunoye, Oyebo Afees Oluwatosin 2012).*

Income tax also has some effect on population movements and the extent of business carried on. A state with a low-income tax rate will find that more people are moving into that state, while traders will leave states with high income tax rates or engaged in various schemes of tax avoidance and tax evasions.

In describing the importance of tax or taxation to any government, Justice Latham of the United States' Supreme Court in the case of *Nichols v. Ames*, (1989) 173 U.S. 505, 509 maintained that ‘taxation’ “... the one great power upon which the whole national fabric is based. It is as necessary to the existence and prosperity of a nation as the air he breathes to the natural man. It is not only the power to destroy, it is also the power to keep alive".

1.4 Summary

Although there is nowhere in our laws where the word 'tax' is defined, yet we were able to look through some other surrounding materials to bring out a succinct definition for the concept. The definitions supplied in this material ranged from literal to legal and it was concluded that whatever definition is chosen by the learner, he must bear in mind the idea of compulsion in the payment of tax and the fact that the tax must be imposed by legislation.

Before any form of levy or payment can be ideally regarded as a tax, it must show the trait of simplicity, neutrality, administrative efficiency, equity, certainty and transparency.

The levying and payment of tax is so important to mankind that it affects virtually all the strata of man's life. It affects human's life socially by way of various reliefs and population movements from a high tax rate state to a tax friendly state; economically as it assists businessmen in their investment and savings and ultimately being a major source of revenue for the government. In this unit, we examined the various definitions of tax. We also looked at the factors that characterize a good tax and then we discussed the importance of taxation in our society.

1.5 References/Further Readings/Web Resources

Abdulrazaq, M. T. (1993) *Principles and Practice of Nigerian Tax Planning and Management*, Batay Law Publications, Ilorin.

P. Ramanatha Aiyar's *Concise Law Dictionary (2009) 3rd ed,* LexisNexis Butterworths Wadhwa, Nagpur.

1.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. The definition of tax as offered in the Oxford Dictionary has some fundamental flaw and has been criticized as being inadequate in application. In fact, the definition is inadequate as it limited its view as to the purpose of tax and placed unnecessary emphasis on proportional taxation as opposed to progressive and other types of taxation.

2. An ideal tax must be administered on the principles of equity or fairness. The principle of equity suggests that everybody should pay an equitable and fair share of his taxes. We have two types of equitable principles in the taxing system including horizontal equity and vertical equity. H**orizontal equity** suggests that those in equal circumstances should pay an equal amount of tax, while ve**rtical equity**, argues that those in unequal circumstances should pay different amount of tax.

SAE 2

Taxation is important to our society in various respect. First, it serves as a source of revenue generation to the government. It also helps in the control of economic activities, population movement and business management.

UNIT 2 HISTORICAL BACKGROUND OF THE TAX SYSTEM IN NIGERIA

Unit Structure

2.1 Introduction

The word 'tax' first appeared in the English language only during the 14th century. It originates from the Latin word '*taxare'* which means 'to assess'. Prior to that, English used the related word 'task', derived from old French. For some period, 'task' and 'tax' were both in common use, the first requiring labour, while the second demand money. 'Tax' then developed its meaning to imply something wearisome or challenging. Consequently, words like 'duty' were used to suggest a more appealing purpose.

A short and general history of tax is apt here before coming back to Nigerian case. The first recorded form of organized taxation took place in Egypt around 3000 B.C., and is mentioned in numerous historical sources. One of the most valid sources of such historical account is the Holy Bible precisely in. Chapter 47, verse 33 of the Book of Genesis which describes the tax collection practices of the Egyptian kingdom. Here, the Pharaoh would send commissioners to take one- fifth of all grain agricultural harvests as a tax from farmers.

Tax practice of taxation from there, continued and developed as Greek civilization overtook much of Europe, North Africa and the Middle East in the preceding centuries until to the Common Era. The Rosetta Stone, a clay tablet discovered in 1799, was a document of new tax laws as decreed by the Ptolemaic Dynasty in 196 B.C. Named after its leader Ptolemy V, this kingdom was a product of Alexander the Great's legendary conquest of huge swaths of territory, leading to a melding of Ancient Greek and other languages. The text of the Rosetta Stone was therefore written in both Greek and Egyptian hieroglyphic script, and its discovery served as a breakthrough in decoding one of the oldest forms of written language. So, from the Roman age and through medieval European history, new taxes on inheritance, property and consumer goods were imposed/levied, and often played a role in war, either by funding them or provoking them. Other cradles of civilization, such as ancient China, also levied taxes under the authority of a strong centralized government. The Chinese T'ang and Song Dynasties employed a methodical census record to track their populace and impose the proper taxes on them. These funds and materials were then used to support armies and construct canals for transportation and irrigation, among other projects. The Mongol Empire that took control of much of Asia around 1200 instituted tax policy designed to influence large-scale production of certain goods like cotton. (A brief History Taxation-Northeastern University) https://onlinebusiness.northeastern.edu/blog/a-brief-history-of-taxation/

The above count only shows that the concept of tax has been understood and applied by man since time immemorial. This is because the idea of striving towards attaining a better society is not strange to mankind. Not long after the beginning of civilization, people began to pay taxes in support of the things we now take for granted today. These include food, housing, infrastructure, defense, health etc. Taxation is therefore, almost as old as the society and culture themselves.

Nigeria is still a developing country whose economy is not yet stable and efficient and a country's tax system is essentially a derivative of the history, economic structure and political economy of that country. Thus, the advent and evolution of tax levying and payment system in Nigeria has been a chequered history. In view of this, to have a balanced understanding of the legal regime of taxation especially as it operates in Nigeria, you need to know the historical background of the Nigerian tax system. We shall therefore, in this unit, trace those histories from the pre-colonial period till the present-day tax system in Nigeria.

2.2 Intended Intended Learning Outcomes

By the end of this unit, you will be able to:

- give a detailed account of how taxation was levied and paid in Nigeria before the advent of colonialism and English law.
- tell in a graphic form, the history of taxation in Nigeria after the advent of English law.
- Identify the legal structural developments of taxation in Nigeria since the coming of the British into Nigeria till date.

2.3 Historical Background of the Tax System in Nigeria

2.3.1 History of Taxation in Nigeria

History of taxation in Nigeria dates back to the time when even the name 'Nigeria' had not been thought or invented. During this period, the tax administrators then were majorly, the traditional chiefs tax agents and items involved are mostly farm produce and other primary goods. The modern taxing system by the Federal Government of Nigeria under it taxation arm; Federal Board of Inland Revenue (FBIR) with the Federal Inland Revenue Service (FIRS) as its operation arm, could be traced back to the year **1939** when the Companies Income Tax Ordinance was created. According to M. T. Abdulrazaq in his book, *Principles and Practice of Nigerian Tax Planning and Management* (1993), a country's tax system for all intents and purposes emanates from its economic, political and cultural history.

Nigeria is a country with very rich and long cultural histories which still substantially rub on general polity including our tax system. It is known that before the invasion of the Europeans in Africa especially Nigeria, the various communities that existed in the landmass that today constitute the entity known as Nigeria have their respective legal norms and way of lives.

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. The system of taxation is alien to the Nigerian legal system before the advent of British rule. Do you agree?
2. Identify the difference between the Northern and Southern tax systems prior to colonialism

2.3.2 History of Taxation before the advent of British rule in Nigeria

Thus, before the incursion of the British into Nigeria, the idea and system of tax levying and payment was an integral part of the financial system of the Nigerian communities then. It is therefore wrong to assume that in Nigeria, civilization did not begin until colonization was introduced. especially as it relates to the issue of taxation. This reason being that the issue of taxation has been with man since the creation of the world including the communities that existed in the territories that later made-up Nigeria. It should be pointed however that, a country's tax system for all intents and purposes emanates from, and operates in accordance with its economic, political and cultural history. Although at that period, the taxation system was largely operated on an ethnical basis. Therefore, there were few communities where taxes were not levied.

In the northern Nigeria, where there was a well-structured government entrenched on the principles of Islamic law (*Shari'ah*), the emirs as the political and religious leader established various kinds of tax systems. These taxes include the payment of *Zakat* – a tax levied on Muslims for charitable, religious, educational and welfare purposes. It is generally used to cater for the needs of the less privileged and the needy in the society. There was also another kind of tax known as *Jizyah* – a form of tax levied on the non-Muslims who live in the Muslim communities. This was used as a payment for ensuring the safety of their lives and properties while they still lived in the Muslim community. Another tax being levied at the time was *Shukka-Shukka* – a tax paid on all crops that were not liable to *Zakat*. There was also *Jangali* – a tax levied on the heads of livestocks. It was commonly known as Cattle tax. Agricultural tax was also common at the time. It was known as *Kurdin Kasa* and paid by farmers on all their cash crops harvested within the territory of the Emir's province.

However, in the southern Nigeria, not all the communities practiced the taxing system. This is because quite a number of the communities did not have a formalized and organized governance system as the north.

Therefore, in the part of the southern communities where there was an established centralized authority, administrative machinery and judicial institutions (just as it operated in the north), such as the Yoruba land and the Benin Kingdom (both of which fell within the Western and Mid-Western part of Nigeria), there was a system of taxation.

But in other communities which do not have any centralized constituted authority, such as the Ibos, Tivs, Buras, Igbiras and Bachamas, there was little or no form of organized tax system.

You should note that the pre-colonial era taxes were not strictly pecuniary. That is, they were not only paid in money or cash. They were also (largely) paid in kind and through obligatory personal services, which is also known as tribute taxes - for instance the *Ishakole* in the Yoruba land. Although introduction of money did not stop the use of obligatory personal service as a form of tax payment, it rather supplemented it.

2.3.3 History of Taxation after the advent of British rule in Nigeria

After the British came into Nigeria and after having discovered that there was an organized government in the north and upon the introduction of the indirect rule, the British government under Lord Lugard introduced the first Income Tax law in what is today known as Nigeria in 1904 by consolidating all the various traditional taxes under the Land Revenue Proclamation of 1904.

Self-Assessment Exercises 2

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Mention the importance and shortcomings of the 1940 Ordinance to the system of taxation in Nigeria

There was no such tax law in the southern part of Nigeria until 1917 when Lord Luggard made certain changes to the law which culminated in the Native Revenue Ordinance of 1917. The ordinance became operative in the western and mid-western Nigeria in 1918 while it started operating in the eastern Nigeria in 1928. The Native Revenue Ordinance was believed to be discriminatory as it applied to only natives that lived in other parts of Nigeria other than Lagos.

Thus, in 1937, a Native Direct Taxation (Colony) Ordinance No. 41 of 1937 was passed to provide for taxes for natives living within the Lagos colony. Later, the Non-Native (Protectorate) Ordinance of 1939 was also passed to provide for taxation of non-natives.

However, in 1940, the Native Revenue Ordinances of 1917, 1918 and 1928 were all later incorporated into one tax legislation that was more comprehensive – Direct Tax Ordinance No. 4 of 1940.

The Direct Taxation Ordinance 1940 was believed to be the first major tax legislation in Nigeria. It would therefore be proper to describe it as the fore runner of Nigerian tax legislations.

Tax under the Direct Taxation Ordinance 1940 was levied on the community. The community was described in section 2 (1) of the Ordinance as comprising any town, village or settlement, or any locality therein, including a band of nomad herdsmen; and individuals within a community. By section 4 of the Ordinance, the income to be assessed was income from land; rents derived from land; annual profits of the produce from land which were enjoyed by the community or individual;

income from employments and pensions; profits from trade or manufacture; dividends or interest; and the value of all livestock owned by individuals or community. You should note that apart from the introduction of tax over employment and pension, other items upon which tax were levied were those inherited from the earlier traditional tax system.

The importance of the Direct Taxation Ordinance in the history of income tax in Nigeria is that it was the first tax statute that applied throughout the country having consolidated all previous tax ordinances from 1907 to 1939. One shortcoming for the Direct Taxation Ordinance however was its failure to uniformity in the administration of tax in the country. Under the Direct Taxation Ordinance, administrative officers only levied tax on the incomes of Africans throughout the country and the Europeans that lived in Federal Territory of Lagos. Thus, the Europeans living in the former regions were not subject to tax in the regions in which they were resident.

Another shortcoming was that the Ordinance applied to both persons and companies thus lumping together under the same law provisions for the taxation of personal and company incomes.

I also wish to say that at the time we are talking about, the Nigerian tax system has a narrow national tax base and limited tax instruments, thus lacking the revenue elasticity required to meet the usual upward trend in national spending.

The situations described above led to the constitution of the Raisman Fiscal Commission of 1958. The Commission recommended the introduction throughout Nigeria of basic principles for taxing incomes. The recommendation however formed the basis of the Income Tax Management Act of 1961 whose principles we still largely use in Nigeria today though with periodic reviews and amendments. Starting from renovating the revenue agency, the Inland Revenue Department was renamed the Federal Board of Inland Revenue in 1958. This served as a precursor to the present day Federal Inland Revenue Service (FIRS).

After independence in 1960, other legal and institutional reforms were affected in 1961 through the establishment of the Federal Board of Inland Revenue (FBIR) and The Body of Appeal Commissioners as the first contact point should they be any needs for tax disputes resolution. In the same year the Joint Tax Board (JTB) was established with the primary responsibility of ensuring uniformity of standards and application of personal income tax. In 1958 Raisman commission introduced the standardized tax principles. The recommendations from the commission were later adopted by the Nigeria government. Other major reform was the establishment of the chartered institute of Taxation of Nigeria in 1982 and the review of the composition of the FBIR in 1993.

Today's economic realities and commercial complexities as necessitated the need for the various legislations on Tax. As such various legislation have been enacted overtime to deal with raising mattes in taxation. According to the Nigerian Law, there are legal bodies that can levy the taxes in Nigerian; the Federal Internal Revenue Services, the State Board of Internal Revenue and Local Government Revenue Services.

In conclusion, before the advent of the British rule in Nigeria, the idea and system of levying one another for the good of the society has been one of the common norms in certain communities. The taxes levied at the time were based on ethnic factors. Taxes were basically administered in communities that had established centralized and organized administrative governance. Thus, there was no uniform system of taxation.

However, upon the advent of the British colonial rule in Nigeria, the British government through the indirect rule policy introduced the first ever tax legislation in northern Nigeria in 1904. The statute operated only in the northern region until it was extended to other parts of Nigeria in 1918 and 1928.

The inadequacies attendant to the above statute led to the promulgation of the first general legislation on tax in Nigeria, the Direct Taxation Ordinance 1940 and subsequently Income Tax Management Act 1961 which introduced the Basic principles for taxing incomes throughout Nigeria.

2.4 Summary

We have discussed in this unit, the chequered history of taxation in Nigeria. We discussed how taxes are levied in traditional Nigerian communities before the introduction of British law as well as the evolution of the British laws on taxation. We further examined the differences and similarities between the traditional taxation and the taxation introduced under the tax ordinances.

2.5 References/Further Readings/Web Resources

Ola, C. S. (2004) *Income Tax Law and Practice in Nigeria* (3rd ed) Heinemann Educational Books, Ibadan.

2.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. No
2. In the Northern part of Nigeria, even before colonialism, there was a well-organised tax system based on a centralized government. This was not so in many Southern Nigeria before colonialism, due to absence of a centralized authority in many parts of the South.

SAE 2

The Direct Taxation Ordinance 1940 was the first major tax legislation in Nigeria and the first to apply throughout the country. Its shortcomings for are

i. the failure of uniformity in the administration of tax throughout the country
ii. the Ordinance applied to both persons and companies thus lumping together under the same law provisions for the taxation of personal and company incomes.

UNIT 3 VARIOUS FORMS OF TAXATION

Unit Structure

3.1 Introduction

Since the formal introduction tax, the system of taxation has undergone various forms of evolution and transformation. The earliest known form of taxation was on head-to-head basis. And over time, taxation has taken different forms. As a student of law of taxation, it behoves of you to fully understand and be able to identify all the kinds of taxes that operate in our society. In this unit, we will look into the various types of taxation with a view to understanding their respective characteristics and identifying them.

3.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- identify and state the various categories of taxes.

3.3 Forms of Taxation

3.3.1 The Categories/Classifications of Taxes

There are two major categories of taxation depending on the object of the taxation. The different categories of taxes include the following:

1. **Direct/Indirect Taxation**
   Taxes can be classified into either direct or indirect. The distinguishing factor between these two is that whether the taxpayer is aware of the incidence of the particular tax paid.

   a. **Direct Tax**: This is the tax levied directly on the person who is expected to pay the tax. With this type of taxation, the taxpayer will be duly advised through a notification known as 'assessment notice' and he will also be given receipt for the tax paid. Examples of direct taxation include personal income tax, Pay as You Earn (PAYE), capital gain tax, capital transfer tax, company's income tax, etc.

b. **Indirect Tax:** This is a tax demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another. Indirect tax is borne by a person other than the one from whom the tax is collected. Such tax is usually levied on the manufacturer but paid by consumer. The taxpayer of indirect tax s never notified nor have actual knowledge of such levy. Examples of indirect tax include value added tax (VAT), stamp duty, customs duty, excise tax, etc.

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

What is the underlying distinguishing factor between Direct tax and Proportional tax?

2. Proportional, Progressive and Regressive Taxation

This classification is based on the way in which the burden of the tax is distributed among the tax payers.

a. **Proportional Tax:** This is the kind of tax in which the amount paid as tax is directly proportionate (equal) to the amount raised (calculated) as the value of the property taxed (also known as tax base). For this, the percentage of the tax rate remains the same as the tax base increases. It is also referred to as neutral tax.

b. **Progressive Tax:** This is the form of tax in which the percentage of the tax rate increases as the tax base of a person increases. Therefore, a person with higher income would pay a greater percentage of tax than a person who earns a lower income. The progressive tax system preaches fairness and equity by asking the richer to pay more tax than the poor.

c. **Regressive Tax:** This is a tax whose structure is such that the percentage of tax rate paid becomes smaller as the value of the property taxed (tax base) increases. Thus a person earning higher income pays lesser tax than a person earning lower income.

There are other miscellaneous forms of categorizing taxation. Tax may be classified based on the mode of payment of the tax. That is whether par **unit** or ***ad valorem***. UNIT or specific tax is levied on the volume of what is being taxed. Most excise duties for instance are specific in nature, e.g. tobacco tax is charged by weight of the tobacco. AD VALOREM tax is levied on the value if the tax base, e.g. income tax could be charged at 10% to 40% depending on the level and type of income.

In conclusion, the categorization of tax is an unending one. Taxation could be categorized into different categories depending on the variant used. Taxation could be categorized based on the level of awareness of a taxpayer about the incidence of the tax he is expected to pay. It could also be classified based on how the burden of the tax is spread among the inhabitants of the community. It could also be categorized based on the mode of paying such tax.

3.4 Summary

In this unit, we have identified and stated the various categories to which taxation can be divided. Thus, taxation could be classified into direct or indirect, proportionate, progressive and retrogressive as well as unit and *ad valorem*.

3.5 References/Further Readings/Web Resources

Soyode, L and Kajola, S. O. (2006) *Taxation Principles and Practices in Nigeria*, Silicon Publishing Co., Ibadan.

3.6 Possible Answers to Self-Assessment Exercises

SAE 1

The categorization or classification of tax as a direct tax is based on the awareness of the incidence, while the classification of tax as a proportional tax is based on the manner of distribution of the burden of the tax among the tax payers

UNIT 4 TAX BASE AND INCOME

Unit Structure

4.1 Introduction

The term tax base simply refers to the total amount of income, property, assets, consumption, transactions, or other economic activity subject to taxation by a tax authority. We have a narrow tax base which is usually non-neutral and inefficient. There is also a broad tax base reduces tax administration costs and allows more revenue to be raised at lower rates. Tax base can be said to mean, the property or object that gets taxed, while the tax rate is the fraction of the base that is collected by taxation. Thus, the total tax liability is calculated by multiplying the tax rate by the tax base. A taxing authority can tax a narrower base at a higher rate or a broader base at a lower rate in order to achieve the same revenue target.

The federal income tax base includes all types of income such as wages, interest and dividends, and capital gains. However, the federal income tax base is made narrower by various deductions and credits. A more neutral tax base will levy a low rate across a broad tax base with few exceptions. The more exceptions that are carved out of the tax base, the greater the tax burden is shifted upon what remains of the tax base. To calculate the total tax liability, you must multiply the tax base by the tax rate:

4.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the Meaning of Income in Relation to Tax
- explain the Meaning and Types of Consumption as a Tax Base
- distinguish between Income and capital

4.3 Consumption as a Tax Base

A consumption tax refers to a tax levied on consumption spending on goods and services. The tax base of such a tax is the money spent on consumption. Consumption taxes are usually in form of indirect tax, such as a sales tax or a value-added tax. A consumption tax essentially taxes people when they spend money. This is quite unlike the income tax in which you're fundamentally taxed when you earn money or when you get interest, dividends, capital gains, and so on. And a consumption tax that wouldn't happen, you would be taxed essentially when you actually spent the money at the supermarket or store

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Identify any three types of consumption base tax you know
2. What is tax base?

4.3.1 Types of Consumption Base Tax

Various types of consumption tax include:

i. **Value-added tax-** A value-added tax applies to the market value added to a product or material at each stage of its manufacture or distribution. For example, if a retailer buys a shirt for Five Thousand Naira and sells it for Eight Thousand Naira, this tax would apply to the Three Thousand Naira difference between the two amounts.

A simple value-added tax is proportional to consumption but is regressive on income at higher income levels, as consumption tends to fall as a percentage of income as income rises. Savings and investment are tax-deferred until they become consumption. A value-added tax may exclude certain goods to make it less regressive against income. It is common in European Union countries.

Value added tax is a consumption-based tax and is levied each and every time the value of a good gets increased in the process of manufacturing to the point of sale.

ii. **Sales tax-** Sales tax is a consumption tax applicable to sales of goods and services. Sales tax typically applies to the sale of goods, and sometimes includes the sales of services. The tax is applied at the point of sale. The tax amount is usually *ad* *valorem*, that is, it is calculated by applying a percentage rate to the price of a sale. When a tax on goods or services is paid to a governing body directly by a consumer, it is usually called a use tax. Often laws provide for the exemption of certain goods or services from such taxes. Sellers may be at liberty depending on the provisions of the law, to either itemize the tax separately from the price of the goods or services, or to include them in the price.

iii. **Excise tax-** An excise tax is a sales tax that applies to a specific class of goods, typically alcohol, tobacco, gasoline (petrol), or tourism. The tax rate varies according to the type of good and quantity purchased and is typically unaffected by the person who purchases it. Examples are 'Sin taxes' which are a type of excise tax imposed on items that are considered harmful to society, in an effort to decrease their consumption by increasing their prices.

iv **Expenditure tax-** A direct, personal consumption tax may take the form of an expenditure tax, that is, an income tax that deducts savings and investments, such as the *Hall–Rabushka* flat tax. A direct consumption tax may be called an expenditure tax, a cash-flow tax, or a consumed-income tax and can be flat or progressive. Expenditure taxes were briefly implemented in the past in India and Sri Lanka. This form of tax applies to the difference between a person's income and any increase/decrease in savings. Simple personal consumption taxes are regressive with respect to income. However, because this tax applies on an individual basis, it can be made progressive. Just as income tax rates increase with personal income, progressive consumption tax rates increase with personal consumption.

4.4 Income as a Tax Base

A tax base is a total amount of assets or income that can be taxed by a taxing authority, usually by the government. It is used to calculate tax liabilities. This can be in different forms, including income or property. In considering income as a tax base, let's take personal or corporate income as an instance. In this case, the tax base is the minimum amount of yearly income that can be taxed. This is taxable income. Income tax is assessed on both personal income and the net income generated by businesses.

Using the formula above, we can calculate a person's tax liability with some figures using a simple scenario. Say Eze earned $10,000 last year and the minimum amount of income that was subject to tax was $5,000 at a tax rate of 10%. His total tax liability would be $500—calculated using his tax base multiplied by his tax rate:

4.5 Distinguishing Income from Capital

Capital gains are the returns earned when an investment is sold above its purchase price. Investment Income is profit from interest payments, dividends, capital gains, and any other profits made through an investment vehicle. Both capital and income attempt to define the nature of money. While capital is the money invested or available to be invested income refers to flow of money, it could be one’s salary or a firm's earnings. The amount you save from your income, again becomes your capital (which you can use for Investments or expenses).

4.6 Summary

Tax base can be defined as the total amount of assets or revenue on which the government can levy a tax. This is best understood with the help of an example. For instance, in the case of income tax, the tax base is all the income that is earned by the people of the state. Similarly, in the case of property taxes, the tax base is the total value of the property, which changes hands in a given period of time. The tax base is often found to be inversely proportional to the tax rate. When the tax rate is decreased, more corporations start moving their economic activity to the country, and the total tax collected is increased. This inverse relationship continues till a certain point beyond which it ceases to exist. This relationship was explained in detail in a concept called the “Laffer Curve’.

4.7 References/Further Readings/Web Resources

Understanding Tax Terminology: Tax Base https://www.managementstudyguide.com/what-is-tax-base.htm

Julia Kagan, ‘Tax Base’ (2020) https://www.investopedia.com/terms/t/taxbase.asp

4.8 Possible Answers to Self-Assessment Exercises

SAE 1

1. Types of consumption tax base include -Value-added tax, Sales tax, Excise tax and Expenditure tax
2. Tax base simply means the total amount of income, property, assets, consumption, transactions, or other economic activity subject to taxation by a tax authority

MODULE 2

UNIT 1 ADMINISTRATION OF TAX

Unit Structure

1.1 Introduction

After knowing and understanding the general principles of taxation, we now need to know how taxation is being operated (in Nigeria). We also need to look into the framework guiding and espousing the procedural operation of tax. Tax administration is the process of assessing and collecting taxes from individuals and companies by relevant tax authorities; in such a way that correct amount assessed is collected efficiently and effectively with minimum tax avoidance or tax evasion.

In this unit we shall look at the relevant tax authorities responsible for assessing and collecting each category of tax and the process. Add flesh from pg269

1.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the basics of the relevant laws on taxation in Nigeria
- highlight the relevant tax authorities
- have an understanding of the process of collecting tax .

1.3 Administration of Tax

Just like every other country of the world, the main function and responsibility of the Nigerian tax system is to generate revenue for the running of the government at all levels and provide infrastructure and other social amenities to the public. Robust and effective tax drive is achieved through an efficient tax administration and tax system reforms. These elements also create a tax culture, reduced incidences of corruption and tax evasion. There are two components of most tax systems. These are the law and its administration. The law determines the liability of the tax payer, the rate and the base. The law also provides the framework for the due administration of the tax. On the other hand, good administration of the tax law is a *sine qua non* to the attainment of the overall good of the tax system. Meanwhile, it is necessary for you to note that the administration of the tax laws is the function of the tax authorities constituted pursuant to those laws.

However, a proper administration of any tax system requires the establishment of assessable income and assessable entity (that is, the taxpayer) and a relevant and appropriate tax authority. We shall now look at the relevant laws and tax authorities (in Nigeria).

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. List the relevant tax statutes that are applicable to law of taxation in Nigeria.
2. Briefly explain how is a tax statute construed

1.3.1 Relevant Tax Laws

Before we identify the relevant laws that govern tax administration, it should be noted that in order to promote uniformity, the Nigerian constitution vested the legislative power for income tax, whether individuals or corporate, on the federal government. It only delegates the administration of the various taxes to the tiers of government. Thus, the major taxes in terms of revenue, economic and equity significance are enacted under Federal Laws. Such tax laws presently operating include:

a. Personal Income Tax Act, Cap P8, LFN 2004 (as amended).
   Personal income tax is imposed on income of individuals (employees), corporate sole or body of individuals, communities, families or trustees or executors of any settlement as the case may be. The equally covers taxation of sole traders, partnership

assessment, and taxation of estates. This tax is regulated by the Personal Income Tax Act Cap P8 LFN 2004 (as amended). The relevant tax authority responsible under the law to administer this type of tax may vary from the Federal Inland Revenue Service (FIRS) to the various State Boards of Internal Revenue (SBIR).

b. Companies Income Tax Act, Cap C21, LFN 2004.
This type of tax is imposed on profit of companies from all sources. This is majorly under the Federal authority and one of the main taxes administered and collected by the Federal Inland Revenue Service (FIRS). It is a tax paid on the income of incorporated companies. Company's Income taxes are regulated by the Companies Income Tax Act (CITA), Cap. C21, LFN 2004 (as amended). The rate on this tax is 30% of a company of total profit less all expenses for the period which a company reasonably incurred in generating the taxable profit.

c. Value Added Tax Act, Cap V1, LFN 2004.
Value added tax is a tax charged on the sale of specified goods and services usually at a fixed rate, now 7.5%. It is equally known as a consumption tax and it is mostly borne by the final consumer. The FIRS is vested with the power administer and manage of VAT in Nigeria. It is regulated by the VAT Act and the VAT (Amended) Act 2007. Recently, the Federal Government of Nigeria has approved a 50% increase in VAT for supply of goods and services, from 5% to 7.5%. The new rate took effect from 2020.

d. Stamp Duties Act, Cap S8, LFN 2004.
Stamp duties are governed by the Stamp Duties Act, CAP S8 LFN 2004 (as amended) in Nigeria. Stamp duties due from individuals are paid to the respective State Government, while corporate bodies pay to the Federal Government. The stamp duties rates applied by FIRS are in two forms, which are (i) flat rate charges and (ii) ad valorem charges. In line with the Federal Inland Revenue Service (Establishment) Act, FIRS is empowered to administer taxes for stamp duties listed in the first schedule to the Act. It is also administered by the respective States Internal Revenue Services (IRS)

e. Petroleum Profit Tax Act, Cap P13, LFN 2004.
This is a tax levied on income of companies in petroleum operations (Upstream). The tax is regulated by the Petroleum Profits Tax Act, Cap P13 LFN 2004 (as amended). Companies liable to PPT are not liable to Companies Income Tax (CIT) on the same income.

The administration of these laws involves assessment, collection and accounting for revenues accruing to the Government of the Federation.

f. Capital Gains Tax Act, Cap C1, LFN 2004.
Capital gains tax is a tax charged where there is a disposal of assets. This is the case where any capital sum is derived from a sale, lease, transfer, assignment, compulsory acquisition or any disposition of properties classified as chargeable assets. It is regulated by the Capital Gains Tax Act, Laws of the Federation CAP C1 LFN, 2004 (as amended). This tax is usually charged at a flat rate of 10% on chargeable assets. The tax may not be charged from assets which are not in connection with any trade carried on by the organisation. Capital gains tax is also not applicable to charitable or educational institution of public character.

h. Taxes and Levies (Approved List of Collection) Act, Cap T2, LFN 2004.

i. **Education Tax** (EDT):
This tax is regulated by the Education Tax Act, CAP E4, Laws of the Federation of Nigeria, 2004 and administered by the FIRS. The tax is also governed by Tertiary Education Trust Fund (Establishment, Etc.) Act 2011. Education tax is imposed on all companies registered in Nigeria. The rate of the tax is 2% of assessable profit. The amount in the Fund is distributed between Universities, Polytechnics and Colleges of Education in the ratio 2:1:1 respectively.

j. **Withholding Tax** (WHT
Withholding tax is an advance tax payment deduction made on any income or disbursement due to a taxable person or a taxable corporation, for onward remittance to the relevant government authority. When deducted from source the tax is subsequently remitted to the relevant tax authorities. WHT in Nigeria varies and ranges from 2.5 to 10% for companies and 5 to 10% for individuals in accordance with the nature of the transaction involved. *Section 78 of the Companies' Income Tax Act (as amended)* stipulates that where a company makes a payment to another company or to another individual, either as interest (with interbank deposit and royalty included), rent, dividend, etc. such a company shall at the time of making the time of making the payment deduct an advance tax of 10% of the gross amount that is paid and remit such deducted and withheld tax to the FIRS forthwith.

Customs, Excise Tariff, etc. (Consolidation) Act (as amended)

These are taxes levied on on certai imported goods and charged at the Nigeria's Port of Entry. The taxes are usually administered and collected by the Nigerian Customs Service by virtue of the Customs and Excise Management Act. There are two types of taxes charged at the Nigeria Port of Entry; the first is on certain imported goods and secondly, on some exported good. Hence, custom and excise taxes are imposed on goods either for revenue purposes or to discourage consumption of certain products in line with the policy of the government in power. This is why it is a times referred to as consumption tax.

k. Federal Inland Revenue Service Act
The Act establishes the Federal Inland Revenue Service charged with powers of assessment, collection of, and accounting for revenues accruable to the Government of the Federation; and for related matters.

Each of these laws relates to tax administration and form the basis for the regulation of taxes in Nigeria. While some of them deal with individual tax payers, others are concerned with companies and corporate institutions. There are some that deal specifically with the goods and services purchased while few others establish the authorities that are concerned with tax.

1.3.2 Interpretation of Tax Laws

Income tax law is to be interpreted strictly. **A** tax payer has a right to insist on the literal construction of the words used in a taxing statute whatever might be the consequences There is no equity in tax law and no room for intendment. The terms of the law should be applied but not necessarily against the revenue. Where the provisions of the tax law are ambiguous, the law should not be interpreted as to place on the tax payer a burden not previously imposed by any law. Where there is a mistake or an omission in the law or the law has brought an income within the taxing section the revenue board has no right to impose tax but if due to an error or an omission a tax payer’s income is unfairly brought within the charging section, no rules of equity can be pleaded in mitigation of the harshness of the law.

According to ***Rowlatt J. in CAPE BRANDY vs IRC (1921) 2K. B 403,*** in a tax Act, one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax and no room for presumption as to a tax. Nothing is to be read in, nothing is to be implied. One is to look fairly at the language used.

The courts adopted and applied the literal rule of interpretation and in the case of ***IRC v. Vayrshire Employers Mutual Insurance Association Ltd (1946) 1 ALL E.R. 637***. This is a case where a legislation intended to increase the tax net failed to achieve its desired objective, Lord Simmons held that: “It is at least clear what is the gap that it is intended to be filled; hardly less clear is how it is intended to fill the gap. Yet I can come to no other conclusion that the language of the section fails to achieve its apparent purpose and I must decline to insert words or phrase which might succeed where the draftsman failed”.

The literal rule of interpretation is based on the rational that tax statutes are punitive in nature and so should be interpreted strictly in favour of the citizens. In ***S.A. Authority vs Regional Tax Board (1966) NCR 452 and Aderawo Timber Company Limited vs FBIR (1966) NCLR 416 at 422*** *respectively*, Nigerian Courts also adopted the literal rule of interpretation. The view and decision of the court on the rule of interpretation of tax status in the case of ***Mobil Oil Nigeria Ltd Vs Federal Board of Inland Revenue (1977) 1 NCLR 1*** however seem to be different from the general view on the subject matter. The court per Bello JSC (as he then was) held inter alia: *“In considering a statute, regard shall be given to the cause and necessity of the Act and then such construction shall be put upon it as would promote its purpose and arrest the mischief which it is intended to deter”.* The consequence of Bello JSC’s dictum was that a tax statute was treated and interpreted like any other statute where the mischief rule is applicable to discover the intendment of the legislature as against ***Rowlatt J***’s opinion in ***Cape Brandy vs. IRC***, where he stated unequivocally that there is no room for intendment in construing a taxing statute. Also, the decision made it clear that a purposive interpretation is applicable in interpreting a taxing statute rather than a literal rule and its narrow strictures.

The supreme court also toed the same line of reasoning arguing that a purposive approach rather than a literal approach is applicable to tax statutes interpretation. This was the decision of the court in the case of ***Shell Petroleum Development Company Limited vs Federal Board of Inland Revenue (1996) 8 NWLR (Pt 466) 256***, where it applied equitable considerations in interpreting a tax law

Although, pursuant to the doctrine of stare decisis, supreme court’s decisions takes precedent and are binding on all lower courts, the lower courts in open defiance of the rule of hierarchy of courts and without any efforts to distinguishing the facts as reason for non-compliance with the supreme court’s decisions on purposive nature of construing tax statutes continued to apply the literal rule of construction of taxing statutes. Hence, in ***Halliburton West Africa Limited V. Federal Board of Inland Revenue N.R.L.R 2 (2013) 10 at P.34*** Mustapha J (as he then was) stated unequivocally that "*Tax Laws are interpreted strictly; a* tax payer *has a right to stand upon* literal *construction of the words used in a taxing statute whatever might be the consequences".*

On equal note, the Court of Appeal in **7UP Bottling Company Plc V Lagos State Inland Revenue Board N.R.L.R 2 (2013) P.105 at 122-123**) held inter alia:

Taxation provisions are strictly interpreted….If a person sought to be taxed comes within the letter of the law, then such a person must be taxed. On the other hand, if the tax authority seeking to recover tax from a person is unable to bring him within the letter of the law, the person will be free, however apparently within the spirit of the law his case ought otherwise to be.

In the face of the discrepancies, the question is whether the purposive interpretation of tax statute can displace the literal rule. It seems the answer must be in the affirmative bearing in the mind the position of the Supreme Court on the subject matter and particularly, the decision in ***Barclays Mercantile Business Finance Limited vs Mawson (2004) UKHL 51 STC 1*** where Lord Nicholls stated unequivocally that:

As Lord Steyn explained in IRC vs Mc Guckian the modern approach to statutory construction is to have regard to the purpose of a particular provision and interpret its language so far as possible in a way which best gives effect to that purpose" and that "Ramsay case liberated the construction of revenue statutes from being both literal and blinkered.

It should be noted that the reason for the purposive approach is not to entirely discard the literal approach but, so that, where the literal approach could not help; the statute and every word in it can be examined to determine the intendment of the tax statute. On this note, it has been argued that an insistence on a literal interpretation of a taxing statute instead of a wider purposive interpretation may hurt rather than protect the subject of the tax.

Self-Assessment Exercises 2

Attempt this exercise to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Identify the relevant tax authority in Nigeria you know

Interestingly therefore, centuries' old interpretation by literal rule was brilliantly challenged by the supreme court of Nigeria as far back as 1977 in ***Mobil Oil v FBIR*** while the wisdom in a purposive interpretation of tax statute became an international issue for discourse just in 2004, when the House of Lords adopted the same in Barclay's case. Notwithstanding that tax statutes are becoming more elaborate in order to solve the issue of the ever-rising spate of contentious but legal tax avoidance schemes such as tax havens, there are still many cases where only a resort to the purposive rule of interpretation will enable the court give effect to the intendment of the taxing statute

Tunde Esan Shift in interpretation of tax statute (2017) https://www.thecable.ng/shift-in-interpretation-of-tax-statute

1.3.3 Relevant Tax Authorities

After we have known and identified the relevant tax laws, what we need to know now is to identify the relevant tax authorities that are in the position to collect the tax on behalf of government. These are the revenue boards constituted by the government with mandate to assess and collect tax. According to the provision of section 100 of Personal Income Tax Act (PITA) (as amended by the Finance (Miscellaneous Taxation Provisions) Act 1998), 'tax authorities' means Federal Board of Inland Revenue (now Federal Inland Revenue Service), the State Board of Internal Revenue or the Local Government Revenue Committee. For better understanding, some of the relevant tax authorities are discussed hereunder:

1. **Federal Inland Revenue Service (FIRS)**

   The Federal Government collects taxes through the Federal Board of Inland Revenue an agency that administers Revenue laws that deal with taxes paid by the residents of the Federal Capital Territory and those taxes paid by corporate bodies (Limited Liability Companies). They are responsible for accounting for the Federal Government for all taxes collected.

   The FIRS was established by the Federal Inland Revenue (Establishment) Act, 2017 primarily to administer the various Federal taxes as recognized by the relevant laws. This body took over from the erstwhile Federal Board of Inland Revenue (established under section 1 of the Companies Income Tax Act (CITA) 1990), which was dissolved by section 62 of the Act. The FIRS is the federal government's operational agency in charge of assessing and collecting relevant taxes for the Federal Government. This power includes power to assess, collect and account for revenues accruing to the Government of the Federation. Pursuant to **Section (8) (1)(a)(b) and (c) of the Act** the principal functions of the FIRS are;

   (a) assess persons including companies, enterprises chargeable with tax;

(b) assess, collect, account and enforce payment of taxes as maybe due to the Government or any of its agencies;

(c) collect, recover and pay to the designated account any tax under any provision of this Act or any other enactment or law;

More functions of the FIRS as provided in section 8 of the Act, are:

a. to collect, recover and pay to the designated account, any tax recognized bY the Act or any other law or enactment.
b. to assess persons including companies, enterprises and individuals chargeable with tax
c. to assess, collect and enforce payment of taxes as may be due to the government or any of its officials
d. to collaborate with relevant ministries and agencies, for the review of the tax regimes and promote the application of tax revenue for the stimulation of economic activities and development
e. to make, from time to time, a determination of the extent of financial loss and such other losses by government arising from tax evasion and fraud and such other losses (or revenue forgone) arising from tax waivers and other related matters.

The FIRS also has a board, whose power is to provide general policy guidelines relating to the functions of the service, among other related matters (section 7). There is also a Technical Committee of the board which considers all tax matters that require professional expertise and make recommendations to the Board.

2. State Board of Internal Revenue (SBIR)

The State Governments levy and collect taxes through the State Board of Internal Revenue which is the agency that primarily administers the Personal Income Tax Act. Some states of the federation have however, instituted additional revenue statutes, which they administer. They have the responsibility of accounting to the State Government for all revenue collected. The SBIR is the relevant tax authority charged with assessing and collecting taxes that are due to the state government. The SBIR was established under section 85A of the Personal Income Tax Act (PITA) 1993. The SBIR has an operational arm known as State Internal Revenue Services or State Services.

The SBIR is responsible for:

a. ensuring the effectiveness and optimum collection of all taxes and penalties due to the state government under the relevant laws.

b. doing all such things as may be deemed necessary and expedient for the assessment and collection of the tax and shall account for all amounts so collected in a manner to be prescribed by the Commissioner for Finance of the relevant
state.

c. Making recommendations where appropriate to the Joint Tax Board on tax policy, tax reform, tax legislation, tax treaties and exemptions as may be beginning from time to time.

d. generally controlling the management of the State Services on matters of policy subject to the provisions of the law setting up the State Service.

3. Local Government Revenue Committee

The Local Government Revenue Committee was also established under the PITA, section 85D (1). The Local Government imposes and collects taxes through the Local Government Revenue Committee which is responsible for the assessment and collection of all taxes, fines, and rates under its jurisdiction and account for all revenue collected to the chairman of the Local Government. The function of the Revenue Committee includes assessment and collection of all taxes, fines and rates under its jurisdiction and shall account for all amount so collected in a manner to be prescribed by the Chairman of the Local Government.

4. Other tax authorities

Apart from the above mentioned, there are other tax authorities created by the law. These include among others:

a. Joint Tax Board (created under section 85(1) of PITA 1993) Add flesh from pg273

b. The Board of Appeal Commissioners –pg274

c. Joint State Revenue Committee (section 85F PITA 1993 as amended by Finance (Miscellaneous Taxation Provisions) Act 1998).

Tax administration simply means the implementation of the various tax laws in a country (by tax authorities) in order to achieve its objective. In Nigeria, tax administration is carried out by the three tiers of government, including the Federal Government, the thirty-six States of the Federation and the Federal Capital Territory as well as the various

Local Governments, through the machineries established by each of these governments.
The Federal Inland Revenue Service (FIRS) is the body statutorily empowered to administer, manage and enforce the various tax laws in Nigeria at the federal level. The States' Governments administer tax through the various State Boards of Internal Revenue, while the Local Government Revenue Committee of each State administers taxes at the local government areas.

There is also the Joint Tax Board (JTB) which is a creation of Personal Income Tax Act. It is made up of officers of the Federal and State tax authorities. It serves as a big umbrella covering all tax authorities in Nigeria. The official role of the JTB remains purely advisory.

In conclusion, we have seen that a proper tax system would only work through two machineries, good tax laws and responsive tax authorities. With these two in place, the tax system would be properly administered.

1.4 Summary

In this unit, we have been able to identify the machineries that would make a tax system work properly. We identified two of such machineries, the tax laws and the tax authorities. The tax laws are the legislations put in place to provide for the general tax guidelines and stating the punishments for failing to pay tax while the tax authorities are the relevant bodies and/or agencies constituted by the government, either federal, state or local government and charged with the responsibilities of assessing and collecting the relevant taxes on behalf of the government.

1.5 References/Further Readings/Web Sources

Soyode, L and Kajola, S. O. (2006) *Taxation Principles and Practices in Nigeria*, Silicon Publishing Co., Ibadan

1.6 Possible Answers to Self-Assessment Exercises.

SAE 1

1. Relevant tax statutes that are applicable to law of taxation in Nigeria include though not limited to the following:
   - i. Personal Income Tax Act, Cap P8, LFN 2004 (as amended)
   - ii. Companies Income Tax Act, Cap C21, LFN 2004
   - iii. Value Added Tax Act, Cap V1, LFN 2004.
   - iv. Stamp Duties Act, Cap S8, LFN 2004.
   - v. Petroleum Profit Tax Act, Cap P13, LFN 2004
   - vi. Capital Gains Tax Act, Cap C1, LFN 2004

vii. Taxes and Levies (Approved List of Collection) Act, Cap T2, LFN 2004
viii. Education Tax (EDT)
ix. Federal Inland Revenue Service Act

2. Income tax law is to be interpreted strictly. As a result, there is no equity in tax law and no room for intendment **A** tax payer therefore, has a right to insist on the literal construction of the words used in a taxing statute whatever might be the consequences

SAE 2

Relevant tax authorities in Nigeria include but not limited to the following:

i. Federal Inland Revenue Service (FIRS)
ii. State Board of Internal Revenue (SBIR)
iii. Local Government Revenue Committee

UNIT 2 FREE INTER-STATE TRADE, COMMERCE AND LIMITATIONS ON TAXING POWERS OF GOVERNMENTS

Unit Structure

2.1 Introduction

Inter-state trade or commerce means any commercial transactions that cross state boundaries or that involve more than one state. The traditional concept that the free flow of commerce between states should not be impeded has been used to affect a wide range of regulations, both federal and state. Federalism or federal system creates special problems with regard to maintaining free flow of trade and commerce throughout the entire country. In the first place, they may arise, the issue of rivalry between or among the States and such tendency may lead to formulation of policies or taking other measures possible by States to gain advantage over others. The rivalry may ultimately affect the national economy in a bad way. Such lopsided economic tendencies must be put in serious checks to ensure strong federalism. This is also, because, where different constituent units seek to tax or rather, regulate, through the theory of nexus, the same people, commodities and transactions, this will create the problem of multiple burden to be placed on them. In which case, the commercial unity of the federation will in jeopardy. This will be the case, even when the States did not intentionally act to bring such effect or result. Additionally, where each State has the power to enact or legislate on common subject matter, it is most likely that the laws so enacted will be diverse in character for the same subject matter. This will also constitute trade barrier by placing some difficulties in effort to comply with each of the laws enacted by different States.

Free trade is a trade policy that does not restrict imports or exports in a system. It can equally be defined as the free market idea applied to international trade. In government, free trade and commerce is predominantly advocated by political parties that hold economic liberalism as an ideoplogy, while economic nationalist and left-wing political parties generally canvass for protectionism which is the very opposite of liberalism.

1.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- gain understating of the term ‘inter-state commerce and trade
- know how this applies to Nigeria
- effectively discuss the effects of free trade and commerce on tax laws.

2.3 Free Inter-State Trade, Commerce and Limitations on Taxing Powers of Governments

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes. 1. State the major factor that determines the division and allocation of taxing power in a country. 2. Why do you think that many economists are against protectionism?

2.3.1 Issues of Trade and Commerce in Relation to Tax in Nigeria

Trade and Commerce continuous to be an essential aspect of human civilization. For a very long-time tow, it has brought about the free flow and exchange of goods, technology, culture as well as ideas. In some other cases, the emergence of human society has been attributed to activities associated with trade and commerce. This is because in the course of exchange, people associate freely with one another, during which ideas and values are transferred and absorbed. Trade and commerce have played a pivotal role in the development of economy of many nations. Trade and commerce is conducted both to earn profit and satisfaction of human wants, and equally to secure the provision of essential service to the consumers. Trade and commerce is an essential social activity because the society needs uninterrupted supply of goods and services to satisfy the ever increasing and changing but never ending human wants. Thus, trade and commerce is a very important social activity that stimulates human and economic development in the local and international domain. In this unit, we will be discussing trade and commerce and their relation to commerce. Trade (Nwosu Ijeoma G. and Victor Nwokocha, Conceptual Appraisal of Trade and ommerce in Nigeria 2017.

https://www.researchgate.net/publication/316507575_a_conceptual_appraisal_of_trade_and_commerce_in_nigeria

One of the most essential factors that determine the division and allocation of taxing powers in a country is the type of system of government such country operates- a federal or unitary system of government. There is no universal way for the division of taxing powers in a federal system just as there is no one particular universally adopted system of federalism. Arrangements for the division and allocation of taxing powers therefore vary from country to country and from Constitution to Constitution all depending on the prevailing national policies and economic circumstances. Example is the period of military rule in Nigeria when the country was more or less run as a unitary state. So many tax Decrees and Edicts enactment during the military regime are bound to occasion jurisdictional conflicts between the Federal and State Governments in a normal federal system of government and expectedly so, with the coming into effect of the federal constitution in 1999. A good example is the recent declaration by the Lagos State of its intention to re-introduce the collection of “sales tax” as permissible under fiscal federalism" notwithstanding the existence of a Value Added Tax Decree. This raises the question as to whether a State Government can impose its independent sales tax simultaneously with VAT, which is a federal tax applicable throughout the country. and, whether such measure will not amount to double taxation.

Certain techniques are used and usually followed in the division of taxing powers among the tiers of the government. The Nigerian Constitutions for instance, had followed techniques over the years for the same respect:

(a) the division of taxing powers broadly was done in line with the division of legislative powers. Hence, a tier of government can impose taxes only in respect of the subject matters within its competence;

(b) the Constitution may specifically mention certain taxes by name or their bases and reserve same exclusively for a tier of government;

(c) the right or power to legislate with respect to certain elements of a tax may be vested in one tier of government while some other elements are reserved for another tier. Under this method, each tier of government is competent to legislate on the elements within its competence in line with the law;

(d) they can be differences made between tier of governments with respect to implementation. For instance, the power to impose a tax may be vested in one tier of government while the administrative power to collect it may be delegated to another tier of government. This is typical of the distinct feature of the relationship between the State and Local Government Councils in the division of taxing powers under the 1999 Constitution;

(e) A tier of government may be given the power to impose and or collect a tax while the proceeds of the tax is allocated to another tier of government or shared among the different tiers of government concerned.

2.3.2 Effects of Free Trade and Commerce on Tax Laws

Generally, economists are in supportive of free trade. There is a wide consensus among economists that protectionism has a negative effect on economic growth and development while free trade and the reduction of trade barriers has a positive effect on the growth and development of the economy as well as the economic stability. However, in the short run, liberalization of trade can cause significant and unequally distributed losses and the economic dislocation of workers in import-competing sectors.

Murschetz, Paul (2013). State Aid for Newspapers: Theories, Cases, Actions. Springer Science+Business Media. p. 64. ISBN 978-3642356902.

Peláez, Carlos (2008). Globalization and the State: Volume II: Trade Agreements, Inequality, the Environment, Financial Globalization, International Law and Vulnerabilities. United States: Palgrave MacMillan. p. 68.

P.Krugman, «The Narrow and Broad Arguments for Free Trade», American Economic Review, Papers and Proceedings, 83(3), 1993 ; and P.Krugman, Peddling Prosperity: Economic Sense and Nonsense in the Age of Diminished Expectations, New York, W.W. Norton & Company, 1994

Electronic Commerce and Tax Law in Nigeria

For effective and legal taxation of any person or company, there should first of all be a clear provision of the law for that purpose. In every respect, Act of parliament must be read in accordance with the natural construction of its words. Thus, a tax law is to be strictly constructed. In Halliburton West Africa Ltd v FBIR, the court held that it is of public policy that a court of law should interpret the law in a just way and to serve public interest. The Nigerian Supreme Court has however held that the provisions of tax laws can be interpretation not necessarily strictly. VAT is imposed and payable on every international, interstate as well as intra-state supplies of goods and services. As a result, these cover all supplies into Nigeria from outside Nigeria (import), those made within Nigeria (inter-state and intra state) as well as supplies made from Nigeria to outside Nigeria (exports). In any case however, those supplies made from Nigeria to outside Nigeria are expressly exempted on the basis of the territorial nature of tax law.

Value Added Tax (VAT) is usually and generally levied on all goods and services bought and sold for use or consumption within the country. For instance, in *VODACOM Business Nig. Ltd v FIRS (2018) 35 TLRN 1*, the court decided that almost in every jurisdiction like Nigeria, electronic transactions (intangible services) are subject to tax in the place of supply which is the place where the services were supplied or are used and consumed.

By virtue of *section 33* of the Finance Act 2019, those services that are rendered in Nigeria by a person physically present in Nigeria at the time of provision of same and services provided to a person in Nigeria, regardless of whether the services are rendered within or outside Nigeria are subject to taxation. In accordance with section 2 of the VAT Act, 2007, the following transactions were to be taxable by VAT in Nigeria;

(a) The supply of goods and services within Nigeria (including inter-state and intra-state acquisition of goods and services in Nigeria.
(b) The supply of services if the recipient is established to be within Nigeria.
(c) The supply of goods from outside Nigeria.

Part III of the First Schedule to the financial Act however lists services to be exempted from VAT to include medical services, services rendered by Community Banks, People's Bank, Mortgage Institutions, plays and performances conducted by educational institutions which are regarded as part of learning and all export services. In addition, services rendered to diplomats are zero rated, and not subject to VAT. In the above case of *Vodacom Business Nig Ltd v FIRS*, the appellant contracted with a company (the NSS) based in Netherlands for the supply of satellite in Nigeria. The appellants through the transponder located in Nigeria received the service transmitted to it here in Nigeria. In the contract terms, the supplier, (NSS) contracted its VAT liability to the Appellant. The Respondent assessed the Appellants to the assessment and when the Respondent failed to revise the assessment, the Appellant filed the appeal at the Tax Appeal Tribunal against the assessment. The Tax Appeal Tribunal dismissed the appeal. Dissatisfied with the decision and judgment of the Tax Appeal Tribunal, the Appellant appealed to the Federal High Court and on the following grounds:

a. Whether the services (or the transactions arising from the contract) are liable to VAT and alternatively,
b. Whether the requirement of registration is a condition precedent for its VAT liability.

The argument adduced by the Appellant was that the Tribunal's finding was anchored on its reliance on "usage or receipt" of service as a means of determining the Appellant's VAT liability rather than the location of supply of the service as stipulated in the VAT Act. He further maintained that by the Value Added Tax Act, Cap VI Laws of the Federation of Nigeria, 2004, a service supplied by a non-resident person to a person within Nigeria is taxable by VAT only if the service is actually rendered in Nigeria.

The rationale behind this argument seems to be that physical act of rendering the service has to be performed in Nigeria for it to be taxable by VAT. In addition, where the service is rendered from outside Nigeria but only received in Nigeria in such a case, the transaction will certainly not be liable to VAT in Nigeria. This argument seems not to have looked at the impact of section 2 of VAT Act which actually makes every service in Nigeria liable to VAT except those in the list of the services exempt.

It should be noted that the choice of the word "supply" in by section 2 of VAT Act makes the basis of charge of VAT on all goods and services within Nigeria. The same forms the principle incorporated in the charging provision of VAT. Consequently, because tax is territorially enforced, the word supply as it relates to international trade into Nigeria means good and services supplied in Nigeria. This is contrary to opinion formed by some to the effect that e-commerce or transaction is not subject to taxation in Nigeria as a result of the principle of location.

Issue of the Liability of Intangible Services to Pay Value Added Tax (VAT) in Nigeria.

In the determination of the tax liability of an income earned by foreign entities in Nigeria, physical presence or permanent establishment traditionally are major factors. In accordance with provisions of the Companies Income Tax Act CITA 2007, particularly section 13 (2), the profits of a company other than a Nigerian company from trade or business shall be deemed derived from Nigeria if that company has a fixed base of business in Nigeria to the extent that the profit is attributed to the fixed base. However, there is this serious challenge of the best way to determine at what point such non-resident company will be seen or deemed to have conducted business in Nigeria, since it does not require a physical presence in Nigeria to operate its business transaction. This is particularly the case when the customers those complete transactions in the internet platforms may not be aware of the exact location of the digital goods and services they are consuming or enjoying.

Taxation of e-commerce or transaction also faces a major challenge posed by the new world of bits and bytes. For instance, where a company operates online internet transactions, it may maintain and keep all of its records in digital form. In such a case, an external auditor could be presented with a database fraught with computer code, so that, even if the external auditor gains access to the digital records, he may not be able to distinguish the transactional records from other stored digital data which in usual case are encrypted. The only remedy in such situation is when the company cooperates and arranges all of its data for the auditor. *M Riezenman, Beneath the Internet: Explosive Growth Drives Improvements to the infrastructure (United States: IEE Spectrum, 2001,*

In an effort to broaden the tax net, the Nigeria tax authorities have sought to give effect to the interpretation of existing regime to tax digital transactions. In this regard, *Section 9 (1) of the Company Income Tax Act, 2007,* provides specifically that the tax shall for each year of assessment, payable upon the profits of a company accruing in, derived from, brought into or received in Nigeria should be applicable to digital transactions of non-resident companies. Where a taxpayer resident in Nigeria transacts business with a non-resident entity, the taxpayer is required to deduct the VAT at source and remit to FIRS (T. Oyedele 2015). The Nigerian tax authorities have been making efforts to implement the Reversed charge mechanism which mandates such as customer to account for VAT on the transactions. In *VODACOM Business Nig Ltd v FIRS*, the court maintained that:

Reversed charge as a mechanism under which VAT is required to be paid for the goods and services by the recipient rather than the supplier when the supplier is not resident in the country where the supply takes place. When the reverse charge is applied, the recipients of the goods and services make the declaration of both their purchase (Input/VAT) and the supplier's sale (output VAT) in their VAT return.

The implication of the above is that, in international trade, VAT is based on the destination principle, meaning that VAT will not be imposed on exports while imports are taxed on the same basis and at the same rates as local production. The major challenge here is that most of the users of these services are individuals in different areas in Nigeria, thereby making enforcement complicated except if the authorities could develop an ingenious means of tracking such transactions and tax them electronically.

E Eniola, 'Taxation of Business in Nigeria', http;//www.lawyard.ng/taxseris-by-eniola-e-commerce accessed on 20/05/2021.

M Riezenman, Beneath the Internet: Explosive Growth Drives Improvements to the infrastructure (United States: IEE Spectrum, 2001.
T. Oyedele; Insight on Taxation and Fiscal Policy (London: Bloomsburg publication Plc, 2015)

Self-Assessment Exercises 2

Why do you think the doctrine of immunity is important in the economic policies of nations?

2.3.3 Immunities of Governmental Agencies

The essence of the doctrine of immunity is to prevents the federal government and individual state governments from interfering or intruding on one another's sovereignty. Intergovernmental immunity is intended to keep government agencies from restricting the rights of other government agencies. *This* principle was enunciated by the U.S. Supreme Court in ***Mcculloch v. Maryland,*** 17 U.S. at 426 (1819), where Chief Justice ***John Marshall*** and his brother justices unanimously held that states may not regulate property or operations of the federal government. The principle of intergovernmental immunity is often invoked in taxation cases. For instance, in ***Davis v. Michigan Department of Treasury, 489 U.S. 803 (1989)***, the United States' Supreme Court held that the state of Michigan was in violation of federal law by exempting state and local government pensions from taxation but levied taxes on federal government pensions.

The situation with regard to the immunity of state agencies from taxation differs greatly from country to country, and within countries, in respect of different classes of activities and types of taxes, without much indication of any clearly definable systems. As to taxation applicable directly to agencies of foreign States, there seems to be more of a uniform pattern, but still, all the signs do not point in the same direction. Expert are often highly critical about tax immunities, particularly where these has the tendency to restrict the tax base substantially or where they affect commercial activities in competition with private enterprise. In the United States for instance, different principles apply regarding the taxation of federal agencies by the states and vis-a-viz. The federal government, hardly applies taxes to its own activities, however organized, although it still be within its power to do so. In a line of decisions starting from *McCulloch v. Maryland* in 1819 (17 U.S.), the federal courts, in their efforts to protect the national government against interference by the states, established the rule that no state tax could be applied directly to a federal activity. The doctrine was expanded and stretched further to prohibit any state tax in whatever shade, that resulted in any significant economic burden upon the federal government. The implication here is that private contractors on government projects in fact, any private concern or citizen performing services for the Government could be protected by the immunity. The effect of this doctrine was so restrictive on the taxing power of the states which led strong pressure for a change. This prompted the new line of decisions by the Supreme Court, relaxing the doctrine protecting private interests, so that only state taxes whose legal incidence was upon the federal government were prohibited, except greater immunities were authorized by statute. Also, in this line, a series of decisions handed down in 1958 has moved even farther in limiting the immunity of private concerns engaged in government work.

On the other hand, agencies of the state are usually immune from taxes of the state itself. It seems there are no constitutional rule preventing a state from taxing the agencies of another state. The major problem in respect of the immunity of state activities from taxation has arisen from relationships with the federal government. The federal courts have been minded to protect the states on the same grounds, preventing interference of one sovereignty with another that have provided the basis for exemption of federal activities from state taxes, although not to the same extent. The courts have distinguished between the essential governmental activities of a state and its activities that are of a proprietary nature, or of a type normally carried on by private enterprise. Examples are state activities as the sale of alcoholic beverages and mineral water have, which have been as being subject to federal taxation. On this note, Ratchford asserted that the Supreme Court, under prevailing doctrines, does not permit some forms of taxation to either the federal government or the states. These include:

i. taxes directly upon an essential government activity;
ii. property taxes upon property owned by governments or governmental agencies;
iii. property taxes resting directly or indirectly upon government bonds;
iv. excise taxes upon sales directly to governments or governmental agencies;
v. income taxes upon the interest on government bonds.

In Great Britain, as in the Commonwealth nations generally, the traditional principle is that the Crown is not deemed to be bound by any statute, except where there is clear evidence that it was intended to be bound. This doctrine has operated to exempt government agencies from taxation. However, in some of the legislation establishing the entities to operate the nationalized industries, it is specifically provided that they shall be subject to both general and local taxes.

It seems to be the general practice of every government to accord immunity to agents of foreign states regarding taxes the incidence of which would be directly upon such agents. Notwithstanding, in relation to the United States, specific evidence of the tax status of state enterprises carrying on activities in countries other than the United States in competition with private enterprise is not readily available. There appears to be a general tendency toward the development of a rule of international law in support of immunity for movable property owned by a foreign state, and very likely for real property, or at least for real property held for public use. (HYDE,1945). In the United States in particular, the income of foreign governments from any source whatsoever, within the country is exempted from the federal income tax. Such governments, their agencies, and officers have all, in the past, also enjoyed exemption from certain federal excise taxes especially with regards to the case of transactions paid for by the foreign government. However, there have been some inconsistencies in United States practice in relation to this. For instance, in 1922, there was a dispute over the taxation by the United States of a Maine corporation wholly owned by Nicaragua, whose corporate purpose was the operation of railways and steamship lines of Nicaragua. Initially, the position of the United States was that the corporation was a separate legal entity of American nationality and was not entitled to immunity as a part of the government of a foreign state. However, after some years, the decision was taken to refund the taxes collected.

2.4 Summary

2.5 References/Further Readings/Web Sources

Read more: Intergovernmental Immunity Doctrine - Federal, Government, Pensions, and Rights - JRank Articles https://law.jrank.org/pages/7719/Intergovernmental-Immunity-Doctrine.html#ixzz7EYG7Pcy8

Ratchford, Intergovernmental Tax Immunities in the United States, 6 NAT'L TAx J. 305 (1953).

Charles Cheney Hyde, International Law 847 (1945); Bishop, Immunity from Taxation of Foreign State-Owned Property, 46 AM. J. INT'L L. 239, 240, 256 (1952)

1.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. The major factor that determines the division and allocation of taxing powers in a country is the type of system of government such country operates, whether a federal or unitary system of government.

2. **Economists are opposed to** protectionism because of its negative effect on economic growth and development

SAE 2

The doctrine of immunity is important because it prevents the federal government and individual state governments from interfering or intruding on one another's sovereignty

UNIT 3 PERSONS SUBJECT TO TAX AND THE DETERMINATION OF RESIDENCE AS A BASIS FOR TAXATION.

Unit Structure

3.1 Introduction

It is axiomatic that you don’t build something upon nothing. This statement is a truism of the status of tax. Tax is not imposed in vacuum. It must be targeted at an entity that is capable of being taxed. Thus, this unit will identify the persons upon whom are the burden of paying tax. This unit shall also look at the determination of residence as a basis for taxation.

3.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- identify the persons at whom the tax is targeted
- identify the tax authority to whom the taxpayer will pay the tax accruable to and assessed for a particular year of assessment.

3.3 Persons Subject to Tax and the Determination of Residence as a Basis for Taxation

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Identify who are taxable persons in law.
2. How does resident affect the Armed Forces Personnel with respect to payment of tax?

3.3.1 Persons Subject to Tax

Tax is not imposed upon nothing. The entity to be taxed and the source(s) of the income to be taxed must be identifiable. However, it is necessary to state here that the person upon whom tax assessed and from whom tax is collected is known as 'assessable person'. The assessable person is the person whether artificial or real who resides in any part of the country in a particular year of assessment with express exemption of religious, charitable, trade union, labour organizations and government boards, states and corporation. There are personalities relevant to the process of levying and collection of tax. The taxable persons therefore include:

i. Individuals,
ii. Sole proprietors,
iii. Partnerships,
iv. Companies,
v. Communities and families,
vi. Trustees and executors.

The taxes of all of these persons except the company are chargeable under the PITA while the taxes chargeable to a company are assessed under the CITA.

3.3.2 Determination of Residence as a Basis for Taxation

After we have identified the persons liable to pay tax, another issue that is very germane to the proper administration of tax is that of residence of the tax payers. This is because the determination of the residence of the tax payers will resolve the relevant tax authority that will collect the tax. Resolving the issue of residency also affect the scope and type of deductions and relief that may be allowed to a particular tax payer. For example, the amount that would be deducted as PAYE for a person resident in Lagos would be different from the amount to be deducted from the income of a person resident in Dutse.

Generally, residence means living in a particular locality and it may be possible that a person has two places of residence. Residence therefore connotes the idea of remaining and settling in a place for a fairly long period. It is for this reason that residence is used to determine liability to personal income tax.

The Personal Income Tax Act considered the question of where a person is deemed to be resident in a particular year of assessment along the following lines:

a. Individuals in Employment on 1st January of a particular year

A place of residence is defined under paragraph 1 of the First Schedule to the PITA in relation to an individual to mean ‘a place available for his domestic use in Nigeria on a relevant day, and does not include any hotel, rest house or other places at which he is temporarily lodging unless no more permanent place is available for his use on that day.’

However, where an individual has two or more places of residence, his tax would be administered by the tax authority within his principal place of residence. And the phrase ‘principal place of residence’ in relation to an individual with two or more places of residence on a relevant day not being both within a state means:

i. for an individual who is a pensioner, with no other source of income, his principal place of residence is that particular place or those places that he usually resides.
ii. for an individual who earns his income from paid jobs in Nigeria (that is not pensioner), his principal place of residence is that place or those places which on a relevant day is nearest to his usual place of work
iii. for an individual who has a source or sources of unearned income in Nigeria, his principal place of residence is that place or those places in which he usually resides.

b. Individuals taking up Employment within the Year

A person taking up an employment or trade during a particular year of assessment is deemed to be resident for that year in place where he has a place of residence or principal place of residence if he resides in resides in two or more places in an assessment year.

c. Persons on Leave from Employment at 1st January

An individual who is on leave from a Nigerian employment on the first day of January in a year of assessment shall be deemed to be resident for that year by reference to his place or principal place of residence immediately before his Leave begins.

d. An Individual who is in a Foreign Employment on 1st January

An individual who holds a foreign employment on the first day of January of the year of assessment, the duties of which are performed in Nigeria (apart from temporary visits of the employee to Nigeria), is deemed to be resident in that year in the territory in which the main or principal office is situated on that day.

e. Armed Forces Personnel

A member of the Armed Forces (employed in combatant capacity) is deemed to be resident in the Federal Capital Territory for tax purposes in the year of assessment.

f. Trustees

The tax to be paid on the estates managed by trustees on a year of assessment would be payable to the tax authority in charge of the place where the Trustee has a place or place of business (registered office) in the assessment year.

g. Executors

The tax to be paid with respect to the estates managed by an executor would collect by the tax authority in charge of the place where the deceased was last resident.

h. Itinerant Worker

In the case of an itinerant worker, tax may be imposed for any year by any state, in which the itinerant worker is found mostly during the year.

i. Communities

Community income is taxed by the tax authority of the State where the members of the community are usually resident. That is, the State in which the community is found during the year of assessment.

j. Corporation Sole, Partnership or Body of Individuals

A corporation sole, partnership or body of individuals other than a family or community shall be deemed to be resident for a year of assessment in the State in which its principal office in Nigeria is situated on the first day of January in that year. But the corporation sole, partnership or body of individuals has no office in Nigeria on that day, its place of residence shall be the State in which any part or the whole of its income liable to tax in Nigeria arises for that year.

It is important for you to note that any dispute that arises with respect to the determination of place of residence of a person for the purpose of tax in any assessment year shall be referred to the Board for adjudication by the relevant tax authorities involved.

In conclusion, before any tax system can be effective, it must not be imposed in vacuo. Thus, the tax must be targeted at a subject, either an individual who also include businessperson or a corporate body. We have in this unit listed and explained the categories of persons upon whom the onus of paying tax lies.

3.4 Summary

In this unit, we first identified the persons that are subject to the payment of tax. Thereafter, we examined and discussed the factors that determine the jurisdiction of the tax authority. That is, to which particular authority will the taxpayer be required to pay his tax at any year of assessment. To understand this, we looked at how the place of residence of the taxpayer is used to determine that jurisdiction.

3.5 References/Further Readings/Web Resources

Ayua, I. A. (1996). *The Nigerian Tax Law***.** Ibadan: Spectrum Law Publishing.

Ola, C. S. (1999). *Income Tax Law and Practice in Nigeria*. Ibadan: Heineman Educational Books (Nig.) Plc.

3.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. Taxable persons include:
    - i. Individuals
    - ii. Sole proprietors
    - iii. Partnerships
    - iv. Companies
    - v. Communities and families
    - vi. Trustees and executors.

2. A member of the Armed Forces (employed in combatant capacity) is deemed to be resident in the Federal Capital Territory for tax purposes in the year of assessment.

MODULE 3

UNIT 1 EMPLOYMENT TAXATION

Unit Structure

1.1 Introduction

Employment tax or taxation means payroll**,** withholding, social security, workers compensation, unemployment, disability, and other similar charges/taxes including any interest, penalties, additions to tax, or additional amounts with respect thereto imposed by federal, state or local government as the case may be, on any taxpayer or consolidated, combined, or unitary group of taxpayers. It also involves fees charges, duties, levies, imposts, rates, social security contributions including other assessments or obligations, all in the nature of a tax, imposed on, due or asserted to be due from (i) Employees of the federal, state or local government.

Employment tax is also defined as applicable withholdings or deductions for, or on account of, any present or future income taxes, employee national insurance or social security contributions including statutory payments of any nature due in respect of his Basic Net Annual Salary and any other benefits provided to him by the employer, provided such withholdings or deductions are required by and in accordance with the applicable law.

1.2 Intented Learning Outcomes

By the end of this unit, you will be able to:

- explain the term, employment tax
- effectively discuss the term ‘office’, ‘employment’ and ‘emolument’
- list the position of benefits in kinds (BIK) under Nigerian tax law.

1.3 Employment Taxation

1.3.1 Office and Employment

Pursuant to the provision of *section 108* of the Personal Income Tax Act (PITA), ‘Employment’ includes any appointment or office, whether public or otherwise, for which remuneration is payable. For tax purposes, a person in paid employment should be distinguished from another who is self-employed as an independent contractor. As regards employment, a contract of service exists between the employer and the employee whereas the independent contractor is deemed to have a contract for service. In the case of a contract of service, the employer exercises powers and rights of selection and control over the employee while the employee is under strict obligation to act in obedience. However, in the case of a contract for service, an independent contractor is under obligation to deliver the agreed service though he is not obliged to obey orders or do his work in any particular manner.

In determination of employment, the essential factors are that one need to carry out the work wholly or mainly for one business, carry out the work in person, and take orders concerning the way and time to do it, to work where those providing the work tell him to, and to work set hours at an hourly, weekly or monthly rate, and you get paid for overtime, sickness and holidays. In the case of self-employment, the determining factors are that one risk his own capital and bear any losses, control whether, the way, time and place to do the work, provide his own equipment, and is free to employ others to do the work and must be ready to bear the cost of correcting anything that goes wrong. The bottom-line here is that, the Personal Income Tax Act (PITA) makes different regulations for the taxation of such self-employed or independent contractors as the law treats them as it treated individuals carrying on business, trade, profession or vocation.

The definition of employment is hinged on the word’s ‘appointment’ and
‘office’. Thus, in ***Great Western Railway v Bater, Rowlatt J.*** described

employment as "something analogous to an office and which is conveniently amenable to the scheme of taxation which is applied to offices unlike the earning of man who follows a profession or vocation". Although, the PITA is silence on the meaning and definition of 'office', the court per Rowlatt J. in the above case defines same as "an independent, permanent, substantive position which had an existence independent of the person who filled it, which went on and was filled in succession by successive holders". This definition was affirmed by the House of Lords in *Macmillan v. Guest*. Also, in ***Edwards v. Clinch, Lord Lowry*** while describing the nature of an office, maintained that:

"A genuine office does not lapse because the holder dies, retires or completes his assignment. To be in a position of authority is not necessarily to hold an office, and when you appoint somebody to do something you do not thereby appoint him to be something (in other word, to hold an office) unless the Act says so"

Under the PITA therefore, persons who hold office or appointments for remuneration or render services in return for any profits or gains are regarded as persons in employment.

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. What factors will you look out for in determination of employment?
2. Emolument means 'a salary, fee, or profit from employment or office'. Do you agree?

Determination of employees' taxable income

Under the Nigerian tax statute, it is not important distinguishing one type of taxable reward of an employee from another. Pursuant to *section 3(1)(b)* of PITA, chargeable/taxable income includes "any salary, wage, fee, allowance of other gain or profit from employment including compensations, bonuses, premiums, benefits or other perquisites allowed, given or granted by any person to an employee..." *Section 3(2)(b)* goes ahead to provide that income includes any amount deemed to be income under the Act. To qualify as taxable allowance, there is no requirement that a payment must be made directly to or kept by the employee. Under the Act, "Allowance" includes any sum paid or payable in respect of expenses and any sum put by an employer at the disposal of an employee and paid away by the employee.

1.3.2 Meaning of Emolument

Emolument means 'a salary, fee, or profit from employment or office'. It is payment for work in the form of money or something else of value. Emolument include employee's benefits whether in kind or some fringe benefits, perquisites, or perks) including various types of non-wage compensation provided to employees in addition to their normal wages or salaries. Examples are where an employee exchanges (cash) wages for some other form of benefit which is generally referred to as a "salary packaging" or "salary exchange" arrangement. In many countries, most kinds of employee benefits are taxable to at least certain degree. Examples of these benefits include: housing (employer-provided or employer-paid) furnished or not, with or without free utilities; group insurance (health, dental, life etc.); disability income protection; retirement benefits; daycare; tuition reimbursement; sick leave; vacation (paid and unpaid); social security; profit sharing; employer student loan contributions; conveyancing; long service leave; domestic help (servants); and other specialized benefits.

The purpose of employee benefits is to increase the economic security of staff members, and in doing so, improve worker retention across the organization. In the United States for instance, employer-provided benefits are normally tax-deductible to the employer and non-taxable to the employee. There are however, exception to this general rule such as certain executive benefits (e.g. golden handshake and golden parachute plans) or those that exceed federal or state tax-exemption level or standard.

Self-Assessment Exercises 2

What is the position of benefits in kinds (BIK) under the Nigerian taxation law?

1.3.3 Benefits in Kind (BIK) and Nigerian Taxation Law

In the business world today, attraction and retention of talents have become the most singular important success factor especially for competing organizations. These organisations compete against each other as choice employer by offering compensation packages that showcase them as having the best of benefits and perks for employees. For many applicants, the most important factor while considering any job offer is salary. In addition to this, there are other serious factors such as job security, organizational reputation, conducive and/or flexible working conditions.

One of the many ways by which companies and organisations demonstrate their people-centricity value is in the area of benefits and perks they provide to their employees. On this note, they tend to demonstrate that emolument provided to their employees comprises both cash and in-kind benefits. The non-cash benefits usually referred to as in kinds benefits those perks and other benefits, in form of benefits offered to employees outside cash incentives. They include the provision of assets (such as cars and household equipment), accommodation, paid vacation, utilities.

Although, junior staff of an organization can be beneficiaries of the benefits in kinds (BIK) it is the usual case that senior staff are the more common beneficiaries of high-value perks. Junior or lower-level employees often prefer cash (and monetized) benefits, while senior employees enjoy high-value perks in the form of official car, company provided accommodation, company provided furniture, club subscription, free interest loan, and other asset-based employment benefits in addition to cash incentives.

What is interesting to us in this discuss is that such benefits in kinds are also subject to taxation under the Nigerian law of taxation. Pursuant to Section 3(1)(b) of the Personal Income Tax (Amendment) Act 2011 (PITA), chargeable income was defined as "any salary, wage, fee, allowance, or other gain or profit from employment including compensations, bonuses, premiums, benefits, or other perquisites allowed, given or granted by any person to any temporary or permanent employee…". The implication of this provision is that every form of employment benefits, whether cash or non-cash in form of benefits in kinds, are subject to taxation. The fact that benefits in kinds are subject to taxation is also supported by the provisions of Section 33 (2) of PITA which defines gross emolument as, "wages, salaries, allowances (including *benefits in kind*), gratuities, superannuation and other incomes derived solely by reason of employment

Based on the foregoing, any benefits in kinds provided by the employer to the employee is subject to taxation. The question however, is, how are benefits in kinds valued for tax purpose? The fact is that, the value at which benefits in kinds is subject to tax depends on the nature of the benefits and the manner of their provision. The general practice is that, where an employer incurs any expense in the provision of any benefit or perquisite to an employee, the employee is deemed to have enjoyed taxable benefits. Accordingly, where an employee is provided with assets which continue to belong to an employer for his own (employee) benefit, the employee shall be deemed to be in receipt of annual benefits of an amount equal to 5% of the cost of the asset for tax purposes. In the case, where the cost of the asset cannot be ascertained, 5% of the market value at the time of the acquisition as determined by the relevant tax authority will constitute the taxable benefit to the employee. (Yemi, 2014).

The major challenge of this type of taxation normally arises in situations where the assets serve dual purposes – partly for private purposes and partly for official usage. In such case, the value of the benefits is apportioned based on the ratio of usage. The process of apportionment may become so subjective and tax authorities exercise their discretion.

In the case of other benefits such as payment of rent for the employee or hire of assets, the employee is treated as being in receipt of the amount paid to the landlord or the hirer and consequently subject to taxation. However, with regard to living accommodation, the employee shall be deemed as being in receipt of emoluments equal to the annual value of the premises as determined for the purpose of local rates under any law governing assessment of local rates or as determined by the concerned tax authority. The major The challenge with the determination of annual value of premises for company owned houses provided as living accommodation for the employee is the absence of official rates from the government. The discretion given to the relevant tax authority to determine the annual value of the premises may put the taxpayers in precarious positions. It puts taxpayer at the mercies of tax authorities who may likely abuse the discretion on the valuation of benefits.

Where the employer incurs annual expense for providing utilities and other benefits for the employee, the employee would be deemed to be in receipt of the amount of the annual expense. Cases may equally arise where an employer provides its employees with its products or services at zero or discounted price. The question is whether such can be regarded as taxable benefits in kinds or will it be treated as normal business promotional expense?

Another challenge with the provision of benefits in kinds is in the determination of other statutory deductions which are typically based on the cash allowances (even though, some of the benefits in kinds could have been offered in place of certain cash allowances). For instance, where an employee is provided accommodation and official car, how is the pension contribution (which is a function of the basic salary, transport and housing allowances) determined in this situation? (Yemi, 2014).

In conclusion, employment tax involves the fees charges, duties, levies, imposts, rates, social security contributions including other assessments or obligations, all in the nature of a tax, imposed on, due or asserted to be due from the employees of the federal, state or local government. It includes applicable withholdings or deductions for, or on account of, any present or future income taxes, employee national insurance or social security contributions including statutory payments of any nature due in respect of his Basic Net Annual Salary and any other benefits provided to him by the employer, provided such withholdings or deductions are required by and in accordance with the applicable law.

1.4 Summary

In this unit, we conscientiously discussed employment tax and its components. We have looked at 'office' and 'employment', 'emolument', taxable income as well as benefit in kinds (BIK), all in relation to the Nigerian law of taxation.

1.4 References/Further Readings/Web Resources

Yemi Olugbenro, Taxation of Benefits in Kind (Bik) In Nigeria (2014)

Great Western Railway Co v Bater [1920] 3 KB 266

Edwards (Inspector of Taxes) v Clinch | [1981] 3 All ER 543

1.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. In determination of employment, the following factors are important:
   i. the need to carry out the work wholly or mainly for one business,
   ii. carry out the work in person, and take orders concerning the way and time to do it,
   iii. to work where those providing the work tell him to, and to work set hours at an hourly, weekly or monthly rate,
   iv. and get paid for overtime, sickness and holidays
2. Yes

SAE 2

Benefits in kinds (BIK) are also subject to taxation under the Nigerian law of taxation, pursuant to Section 3(1)(b) of the Personal Income Tax (Amendment) Act 2011

UNIT 2 DEFINITION AND ASCERTAINMENT OF INCOME TAX

Unit Structure

2.1 Introduction

Every person or corporate body that earns certain amount of income or gain a measure of profit from its business is subject to payment of tax. Known as income tax, this type of tax is paid after identifying who the payer will be and due assessment of the amount payable has been made. In this unit we shall consider what income tax entails and how it is ascertained.

2.2 Intented Learning Outcomes

By the end of this unit, you will be able to:

- define and ascertaining the income tax
- explain what is used to determine the basis of assessment of period of taxation
- calculate and compute taxes accruable to a given taxpayers and identify the kind of income upon which tax is chargeable.

2.3 Definition and Ascertainment of Income Tax

Self-Assessment Exercise 2

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. How would you define income tax bearing in mind the different types of income tax we have?
2. Only profits and gains form the chargeable incomes. TRUE OR FALSE

2.3.1 Definition and Ascertainment of Income Tax

The ascertainment of income tax payable by an entity in Nigeria depends on the nature of that entity. Thus, the assessment of income tax payable by an **employed individual** is different from an **individual businessman**. The assessment generally for individuals differs from the **company's**.

For individuals (employed and businessman) generally, 'income tax' is the income of the tax payer from all sources, including balancing charge, less allowable deductions for expenses, capital allowances, and losses. It must be the income of the taxpayer. It is however known as the **Statutory Total Income or Total Assessable Income**.

For the company, income tax is payable upon income, accruing in Nigeria, derived from Nigeria, brought into Nigeria and received in Nigeria. Income Tax is payable on income from a source inside or outside Nigeria. It should be noted that examples of the types of income stated above are as follows: income accruing in Nigeria include the income producing assets, income derived from Nigeria include income producing activities; income brought into Nigeria include remittances; while income received in Nigeria include emoluments. See section 8 of the Companies Income Tax Act.

From the foregoing, the sources upon which income tax are payable include but not restricted to the following:

i. profit or gain from a trade
ii. remuneration from an employment, which could be any salary, wage, fee, allowance or gain or profit from employment including compensations, commission, bonuses, premiums, benefits or other prerequisite allowed, given or granted by any person to an employee.

You should further note that there are two types of income (especially in respect of individuals) thus: **earned income** and **unearned income**. Earned income means income derived by a person from a trade, business, profession, vocation or employment carried on or exercised by him and a pension derived by him in respect of any previous employment. It is a reward for effort. Unearned income on the other hand, represents rent, dividends, royalty, discounts, usually received net of withholding tax. These are also known as investment income.

You should however further note that there are two types of income for the purpose of tax namely: personal income and company income.

Personal income tax is charged on income of every taxable person (individuals) from a source inside or outside Nigeria including:

a. the gains or profits from any trade, business, profession or vocation;
b. the salary, wages, fees, allowances or other gains or profits from an employment including gratuities, compensations, bonuses, premiums, benefits or other perquisites allowed, given or granted to an employee
c. the gains or profits including premiums from the grant of rights for the use of occupation of any property
d. dividends, interests or discounts;
e. a pension, charge or annuity; or
f. any profit or gains not mentioned in the above categories
g. balancing charge arising where a business person disposed off an asset used for the purpose of trade or business carried on by it at a profit.

Therefore, the statutory total income or total assessable income for an employed individual is the addition of (a) – (f) above while the statutory total income for individual businessman is the addition of (a) – (g) above.

The following categories of income have been provided for the purposes of measuring the taxable income of companies:

a. gains or profits from a trade or business
b. rents or premiums arising from property
c. dividends, interests, discounts, charges or annuities
d. any source of annual profits or gains not falling within the preceding categories
e. benefits from pension or provident funds treated as income under the Income Tax Management Act
f. fees, dues, and allowances (wherever paid) for services rendered.

You should note that in the case of *Arbico v FBIR (1968) NCLR 150 at pp. 150 -151*, the court had stated that before any particular activity can be said to be a trading transaction which has given rise to profit or gain upon which tax can be levied, the following factors would be considered:

a. nature of assets
b. circumstances of purchase
c. vocation of tax payer
d. number of like transactions
e. the object clause of memorandum and articles of association
f. length of time property was held by the company
g. circumstances of sale

Self-Assessment Exercise 2

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Determine the **tax year** and **basis period** for *J Quarry* company which has just filed 2014 financial statement, having 30th September as its permanent year end. The company has been in operation for over five years.

2.3.2 Basis Period for determination of assessable income (for individuals) or profits (for companies)

It should be noted that for companies, profits are being ascertained on an annual basis. The implication being that every basis period determined on preceding year basis must be **up to 12 months ending on a company's permanent year end**. Pursuant to the provisions of the relevant Tax Laws in Nigeria, companies deriving income from Nigeria meant to pay various forms of taxes. The laws also provide for how the taxes are to be computed on the company's profits and when they should be paid.

Meaning of Basis Period

Basis period is simply means the time within which an assessment is raised or computed on a taxpayer for the purpose of ascertaining and establishing the correct and exact amount of tax liability in a particular period. The term can also be seen as the basis upon which tax liabilities would be computed. Every company running business has its accounting year end (accounting period) as it best suits the company's operations except for few industries in Nigeria where the permanent year end is determined by the relevant authority, such as Banks. In addition, a company's accounting date may not correspond with the government fiscal year; which is 1st January to 31st December. Based on this understanding, it will be correct to state that for the sake of equity; which is one of the major ingredients of the Nigerian tax system, the Nigerian government through the Tax Authorities provides for the basis upon which taxes would be computed on a common ground.

The principle guiding the determination of basis period of assessable income individuals (employed and businessman) and assessable profits for companies is the same. Basis period of assessment is the period, the profit of which is to be assessed in a year of assessment. It is the period of business activity to be taken into account in determining the tax liability of a chargeable person in a particular year of assessment.

Types of Basis Period

Pursuant to the provisions in the Nigerian tax laws including the CITA, PPTA, CGTA, PITA etc., we typically have two (2) types of basis period applicable to every company subject to taxation tax.

These are:

A. Preceding Year Basis Period

According to Section 29 (1) of the Companies Income Tax Act, C21 LFN 2004 (as amended), ... *the profit of any company for each year of assessment from such source of its profits (hereinafter referred to as the "assessable profits") shall be the profits of the year immediately preceding the year of assessment from each such source.*

The provision simply implies that the profit to be subjected to tax in a particular year will not be that earned that current year in question but the profit of the immediate past year. Assessable profits are therefore, computed on the amount of the profits of the year ended on that day in the year preceding the year of assessment.

As earlier stated, it should be noted that for companies, profit is being ascertained on an annual basis. This means that every basis period determined on preceding year basis must be up to 12 months ending on a company's permanent year end.

Under normal circumstance, the basis period is the same as the accounting period. What however differ are the "accounting year" and "tax year"

B. **Actual Year Basis Period**

Actual basis period simply means that the months in the basis period of a year of assessment shall be within the same year. However, unlike preceding year basis period, the year of account will coincide with the year of assessment.

In this case, considering the above exercise or example, the year of assessment will not be 2015 but 2014 and the basis period will be 1/1/2014 – 31/12/2014.

Taxes that are assessed on actual year basis include: Petroleum Income Tax, Capital Gains Tax, Personal Income Tax etc.

Basis Period can also be classified as:

A. Normal Basis Period of assessment

In using a normal basis period of assessment, the tax administrator or collector will use the preceding year to calculate the tax accruing from the taxpayer. Thus, the profit or gain that will be taxed in this year of assessment is the profit of the previous year (i.e. last year). The characteristics of a normal basis period include:

i. It must be of 12 months duration
ii. It must be the only accounting period ending in a preceding fiscal or tax year iii. It must also be commenced from a da immediately after the end of the previous year that is, there is an element of continuity. There must be no gap or coincidence of dates; one basis period must commence the day the end of the previous one.

It is important to note that only a business in continuous operation (say over 3 years) and that has neither changed permanent year end nor cease operations that will have a normal basis period

A. Abnormal Basis period

Abnormal basis period of assessment is used where it is impossible for the administrator to use parameters for the normal basis period to calculate the tax. Thus, any basis period that does not fulfill the conditions stated under the normal basis period is said to be abnormal. The following are examples of situations where a normal basis period will not apply:

i. where a business has just commenced operation
ii. where a business has ceased operation
iii. where there is a change in accounting date

Note that all the above requires special treatments as provided for by Section 29 (3) (a-e) of CITA. It stipulates that:

The assessable profits of any company from any trade or business for the year of assessment in which it commenced to carry on trade or business (or in the case of a company other than a Nigerian Company, for the year of assessment in which it commenced to carry on the trade or business in Nigeria) and for two following years of assessment (which years are in this subsection respectively referred to as **"the first year" "the second year"** *and "the third year" shall be ascertained in accordance with the following provisions:*

A. **First Year**: the assessable profits shall be the profits of that year (i.e. from date of commencement up to the end of the same year)

B. **Second Year**: the amounts of the profits of one year (i.e. 12 months) from the date of commencement of the business.

C. **Third Year**: Shall be computed in accordance with Section 29 (1) as earlier highlighted. This means the basis period will be on a preceding year basis except otherwise provided.

D. For the third year, it may not be possible to obtain a realistic basis period as the period might begin in a month earlier than the month of commencement. This arises where the month of commencement is after the month chosen as the permanent year end. In such situation, the **repetitive rule** will be applied.

In accordance with the provision of the above section, a new business is entitled, on giving notice in writing within two years after the end of the second year to the Board to require that the assessable profits both for the second year and third year (but not for one or other only of those years) shall be the actual profits of the respective years of assessment (i.e. profits of 1st January to 31st December of the second and third years of assessment). This is same as actual year basis we earlier discussed.

This simply means that, the taxpayer reserves the right to be assessed to tax in the second and third year on actual year basis rather than by the rule provided under the commencement of business. Naturally however, the taxpayer will exercise this right only where it may result in payment of lesser amount as tax.

In conclusion, from this unit, you now know the definitions of income tax as it relates to both individuals and companies. You also now know that taxes are not indiscriminately imposed but duly calculated using certain parameters like the period of assessment. In pursuance of this, you have also been taught how the period of assessment is arrived at.

2.4 Summary

In this unit, we discussed the definition of income tax as it concerns the payable tax on the income of an individual and income tax payable by a company. We also explained the meaning of earned and unearned income after which we discussed the categories of income upon which tax will be levied both for individuals and companies. We finally looked at the basis period of assessment of taxable income and its types.

2.5 References/Further Readings/Web Resources

Ayua, I. A. (1996). The Nigerian Tax Law. Ibadan: Spectrum Law Publishing.

Soyode, L and Kajola, S. O. (2006). Taxation: Principles and Practice in Nigeria. Ibadan: Silicon Publishing Company.

2.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. 'Income tax' for individuals means the income of the tax payer from all sources, including balancing charge, less allowable deductions for expenses, capital allowances, and losses.

2. **FALSE**

SAE 2

- Tax Year: 2015
- Basis Period: 1/10/2013 – 30/9/2014

UNIT 3 COMPUTATION OF INCOME TAX

Unit Structure

3.1 Introduction

The computation of the tax is the fulcrum of the study and knowledge of taxation. The aim of this unit is to ensure that the students would not only be grounded in the theoretical concepts of taxation but would also have the ability to explain and if possible, calculate the computation of the tax payable on the income of the various categories of taxpayers in Nigeria.

3.2 Intented Learning Outcomes

By the end of this unit, you will be able to:

- explain and calculate the tax payable on the income of either an individual or a company.

3.3 Computation of Income Tax

3.3.1 Computation of Income Tax

The income tax of taxable persons can be assessed and computed in accordance with the nature of each person. However, the assessment and computation had been undertaken in two major divides – personal income and companies' incomes.

Self-Assessment Exercise

Attempt the following exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. In accordance with the provision of ___ *tax is imposed on the profits of any company accruing, derived from, bought into, or received in Nigeria.*

2. Explain what you understand by the term 'basis of period of assessment' in computation of tax.

3.3.2 Personal Income

Computation of personal income tax accruing to an employed individual is different from an individual business person. Please note that a person is described as an individual or a businessperson. A businessperson is further looked at as a sole proprietor or partnership.
We shall examine them each below.

Assessment and Computation of the Statutory Total Income for employed individual and individual businessperson.
According to section 36 of the Personal Income Tax Act (PITA), the total income of any individual for any year of assessment shall be assessed in accordance with the following steps:

First, the total amount of his total assessable income (statutory total income), earned and unearned, from all sources (listed in unit 1) for that year.

Second, you will add this total assessable income to any balancing charge for the year **Third**, you will deduct the following from the total summation of the above (total assessable income plus balancing charge):

i. any loss relief for that year
ii. any capital allowances for that year
iii. personal relief granted by the Act. For example, personal allowance, life assurance relief, children allowance and dependant relative allowance (e.g. wife etc.)

The *net (total) figure* of the above is called **chargeable income** on which tax is chargeable at progressive rates in force during the particular year of assessment.

However, according to section 37 of the PITA 2005 (as amended) and the *Sixth Schedule* of the Act, the personal income tax shall be computed as follows:

i. the *personal relief allowance* of a flat rate of **40 percent** of the taxpayers' income shall be granted on the income. That is, an amount equivalent to 40 percent shall be deducted from the taxpayers' total assessable income.

ii. After the personal relief allowance has been granted, the balance of income shall be taxed as specified in the following tax table:

Income to be taxed	Percent Rates of Tax
First N30, 000	1 percent
Next N30, 000	5 percent
Next N50, 000	15 percent
Next N50, 000	20 percent
Next N2, 840, 000	25 percent
Above N3, 000, 000	30 percent

3.3.3 Assessment and Computation of the Statutory Total Income for partnerships and companies.

Before the statutory total income of a partnership or a company can be duly taxed, the profits of the enterprise must first be ascertained. And according to sections 19 and 20 of the Companies Income Tax Act, certain expenses and income shall not be included in the profit's computation. Thus, the accounting profits (that is the total calculated profits) will have to be adjusted to obtain the actual profits due for tax. This is called

Adjusted or **Assessable Profits**.
Taxable profit is however arrived at after the treatment of the following:
i. loss relief.
ii. capital allowances and balancing allowances.
iii. balancing charge.

Thus, the adjusted profit of a partnership or company is computed in accordance with the following steps:

First, ascertain the **net profit as per account (**i.e. the accounting profit as explained above**).**

Second, add the available **disallowable expenses** to the accounting net profit

Third, deduct the following from summation of the above (i.e. net profit as per account + disallowable expenses):
i. allowable items not so treated.
ii. income exempted.

After the ascertainment of the taxable profit (adjusted profit) as we have calculated above, then the tax payable for the relevant year of assessment shall be computed as follows:
First, add together the **adjusted profit** and **balancing charge**
Second, then deduct the following from the above summation (i.e. adjusted profit plus balancing charge)
i. capital allowances
ii. loss relief

The result of this calculation is known as **Taxable or chargeable profit**.

Third, after determining the chargeable/taxable profit, the actual tax payable on the profit shall then be determined by *multiplying* the **applicable rate** (as prescribed by the tax authorities from time to time) by the **taxable profit** (e.g. 30% x Taxable Profit).

In conclusion, it is clear from this unit that a student cannot be said to have fully understood this course without actually having an understanding of the taxable and chargeable incomes as well as how taxes are being computed both in respect of individuals and companies.

3.4 Summary

In this unit, we looked at the definition of income tax in order to have a good understanding of the module. We also explained how the income tax is being ascertained and the basis period of assessment, which we said could be normal or abnormal. Finally, we discussed the computation of the income tax.

3.5 References/Further Readings/Web Resources

Soyode, L & Kajola, S. O. (2006). *Taxation: Principles and Practice in Nigeria*. Ibadan: Silicon Publishing Company.

3.6 Possible Answers to Self-Assessment Exercises

SAE
1. section 8 CITA

MODULE 4

UNIT 1 DEDUCTION ALLOWANCE

Unit Structure

1.1 Introduction

Tax concessions or deduction represent perhaps the most widely adopted measure in developed countries to promote economic development. In spite of skepticism of many fiscal experts over the efficacy of tax incentive schemes, virtually all developing countries and developed countries go after inducements to approve enterprises in form of reductions in or exceptional from import duties and income tax for given period of time. The basic question raised by critics is whether the economic benefits of the additional investment attracted outweigh the revenue loss from those who would have invested without special treatment.

We will consider the nature of deductions, the allowable deductions and the ones that are not allowable under this unit. It is also intended to consider waivers, refund and their effect.

(It is suggested that this portion below should be removed to 3.1 below)
Pioneer companies are companies engaged in manufacturing processing, mining, servicing and agricultural industries whose products have been declared pioneer products on satisfying conditions. A pioneer industry or product is regarded as one that is not already carried on in the country, or one not producing enough to meet current or exception requirements. The concept is however, broad enough to include any industry or product for which there is a favourable prospect of development. The policy relating to pioneer industry is dictated by the desire to encourage the development of new or necessary industries that will reduce the country's dependence on imports. The grant of pioneer

status therefore gives a company a preferred position in getting established usually through exemption from income tax. In Nigeria, pioneer industries and products are identified by a list published in the official gazette.

Note that for a company to enjoy the privilege of pioneer status, the company shall forward a written application duly completed form to the federal ministry of industry from where it will be circulated to other ministries and departments, for example, the revenue department for necessary comments. Thereafter a memo will be prepared by the Ministry of Industries to the Council for consideration and approval or otherwise. If the council is satisfied that it is expedient in the public interest to encourage the development or establishment of the industry, the company will be granted a pioneer certificate.

1.2 Intended Learning Outcomes

By the end of this Unit, you will be able to:

- describe the concept of deduction allowance.
- identify deductions allowable and deductions not allowable.
- mention other issues like deductible donations and refunds under Nigerian law.

1.3 Deduction Allowance

1.3.1 Deduction Allowable

Section 20 of the Personal Income Tax Act CAP p.8 LFN, 2004 provides that all outgoings and expenses wholly, exclusively, necessary and reasonably incurred during that period and ultimately borne by a business in the production of the income are deductible in the process of determining the assessable income. The choice of these words in this section presentably intended to have a narrowing effect on the deduction claimed but strictly speaking, it is doubtful whether in practice it has achieved this objective. It would appear that only expenses of a blatantly extravagant nature or expenses incurred which are wantonly unreasonable and are for the private or selfish benefit of directors and their association that it can in practice be readily disallowed. This is because there is no common standard as to what is necessary or reasonable. Moreover, it has been argued that no item of expenditure produces or earns income as expenditure is an outgoing not an incoming item.

Consequently, Section 20 of the CITA Act, 2004 proceeds to provide a list of expenses which are allowable and they include the following.

1. Capital in acquiring the profits

2. Rent and premium in respect of land and buildings occupied for the purpose of a trade or business.
3. Expenses of repairs of premises
4. Any provision for doubtful debt of a specific nature
5. Any bad debt written off
6. Contribution to a pension provident or other retirement
7. Legal expenses that are limited to
    a. general legal advisory services
    b. retainership fees
    c. renewal of a short lease i.e lease whose tenure is not more than 50 years.
    d. any cost of protecting and defending the properties the business.

The objective of deduction allowance includes the following:

- To promote economic development.
- Offers inducements to approval enterprises
- It encourages the development of new industries that will reduce dependence on imports.

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. In computing the profits of a company, only expenses wholly, exclusively, necessarily and reasonably incurred for companies' income tax are deductible. TRUE or FALSE
2. For any donations to be deductible, they must be made to fund, body or instruction in Nigeria. Cite examples.

1.3.2 Deductions Not Allowed

The following items shall not be allowed as deduction for the purpose of ascertaining the income of an individual in respect of:

1. domestic or private expenses.
2. capital withdrawal from a trade, business, protection or vocation and any expenditure of a capital nature
3. any loss or expenses recoverable under an insurance or contract of indemnity.
4. rent or cost of repairs to any premises or part of premises not incurred for the purpose of producing income.
5. taxes on income or profits levied in Nigeria or elsewhere except as provided in section 13 of the act.
6. depreciation of any assets.

7. any sum reserved out of profit except there is in express permission of section
8. 20 of the PITA
9. any provision for doubtful debt of a general nature.
10. any expenses incurred within or outside Nigeria for the purpose of earning management fees unless prior approval of an agreement giving rise to such management fees has been obtained from the minister.
11. legal expenses that include
    a. the cost of defending a traffic offence.
    b. acquisition of new lease-long or short
12. donation
13. fines and penalties.

1.3.3 Deductible Donations

For the purposes of ascertaining the profits or loss of any company for any period, there shall be deducted the amount of any donation made for that period by that company to any fund, body or institution in Nigeria (section 21 of the CITA) which have.

a- The public funds
b- The statutory bodies and institutions
c- The ecclesiastical, charitable, benevolent, educational and scientific institutions established in Nigeria.

These donations can only be made out of the profits of the company and are not expenditure of a capital nature. Such deductions shall not exceed an amount which is equal to 10% of the total profits of that company for that year.

1.3.4 Waiver or Refund of Liability or Expenses

By the provision of section 24 of CITA if a deduction has been allowed to a company under the provisions of the Act in respect of any liability or any expenses which is subsequently waived or released or an expense which is refunded, the amount of the liability or expenses is treated as taxable profits of the company at the date of the waiver, release or refund.
In conclusion, considering the United Kingdom's General Principle for the computation of taxable income, the taxable profits of a company are arrived at in Nigeria by allowing certain expenses to be set off against the company's receipts during the year of assessment as provided for under section 20 of the CITA.

However, it has been provided that where it appears that for any year of assessment, the business of a company produces either no assessable income or assessable income which in the opinion of the Federal Board of Inland Revenue is less than expected to arise from that business, the company may be charged on such fair and reasonable percentage of the turnover of the relevant trade or business and the board may determine.

1.4 Summary

In this unit, we have discussed considered deduction allowable and deduction not allowable, deductible donations and waiver, or refund of liability expenses.

1.5 References/Further Readings/Web Resources

Ola C.S (2004) income tax law and practice in Nigeria, Dalag Prints and Park Ltd, Ibadan.

Aguda A. (1996) the Nigerian tax law, Spectrum Books Ltd, Spectrum House Ring Road, Ibadan, Nigeria.

Soyode L. and Kajola S.O. (2006) taxation principles and practice in Nigeria, Silicon Publishing Company, Lagos- Ibadan Road, Ibadan, Nigeria.

Company Income TAX Act Cap C21 LFN 2004.

1.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. TRUE
2. For a donation to be deductible it must be made to fund, body or institution like:
   i. The public funds
   ii. The statutory bodies and institutions
   iii. The ecclesiastical, charitable, benevolent, educational and scientific institutions established in Nigeria.

MODULE 5

UNIT 1 TAXATION OF BUSINESS

Unit Structure

1.1 Introduction

Taxation of business or business taxation simply refers to the taxes that businesses must pay in accordance with the relevant laws as a normal part of business operations. Whether one operates sole proprietorship, partnership, part of a limited liability company, or a corporation, the business is responsible for adhering to tax regulations and laws.

1.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the term, 'Trading Profits'.
- list the types of business taxes
- identify tax liabilities for business.

Self-Assessment Exercises 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Identify the two perspectives upon which the definition of trading profits may rest
2. What is tax liability?

1.3 Taxation of Business

1.3.1 Trading Profits

Trading profit can be defined in two ways depending on the perspective:

a. Investments: here, the term is seen as *the* earnings achieved by someone who invests particularly in short-term securities. Because of the short (less than one year) holding period of these investments, trading profits are taxed at the higher ordinary income tax rate, rather than the lower long-term capital gains rate that is allowed for investments that someone has held for at least one year. The disparity between these tax rates is substantial, so the trading profit concept is important to a person paying taxes.

b. Operations: Trading profit **is equivalent to earnings from operations**. Thus, it does not include any financing-related income or expenses, nor does it include any gains or losses on the sale of assets. This is a good indicator of the ability of the core operations of a business to generate a profit

Company Income Tax Act particularly in *Section 9(1)(a)* provides that "any trade or business for whatever period of time such trade or business may have been carried on" shall be subject to Companies Income Tax. Pursuant to *Section 23* of the Act, the profits of certain institutions are exempt from tax under CITA, but only in so far as such profits are not derived from 'trade or business'. The implication of this is that the profits of any organization that are derived from 'trade' shall be subject to Companies Income Tax. This raises the question as to what exactly constitutes 'trade'. The word 'trade' was not defined anywhere in Nigerian tax legislation although an attempt was actually made in PITA. The interpretation Section of the Fifth Schedule of the Personal Income Tax Act defines "trade or business" to mean "trade or business or that part of a trade or business the profits of which are assessable under this Act". In any case however, the issue has been deliberated in several legal cases, the rulings of which provide some legal certainty regarding how the courts interpret the word. For instance, in *Arbico Ltd v. FBIR, {1996} 2 All NLR 303*, the plaintiff in the dispute, Arbico, had acquired a plot of land, erected a building, and sold the property at a profit. The company was afterwards assessed for tax on the proceeds of the sale of property. The Company objected to the assessment on the ground that the transaction was a one-off and therefore did not constitute 'trade'. The case eventually got to the Supreme Court. In the ruling the Court propounded two important axioms:

- Firstly, that the word 'trade' should be interpreted in its widest sense, in accordance with its common everyday meaning;

- Secondly, that an isolated one-off transaction can still constitute a "trade". In line with the ruling of the Supreme Court, the following definition seems to capture the common meaning of the word 'trade'. Trade is "the business of buying and selling or barter in goods or services"(taken from Black's Law Dictionary, Eighth Ed. (2004)).

In accordance with these rulings, 'trade' can be regarded as "the business of buying and selling or bartering goods or services". Furthermore, the one-off nature of an activity in no way invalidates that activity as constituting trade. This interpretation accords with the approach in other jurisdictions, including the United Kingdom and United States of America.

1.3.2 Types of Business Taxes

Business taxes are basically classified into five. They are:

i. Gross-receipts tax: This is **a tax applied to a company's gross sales**, without deductions for a firm's business expenses, like costs of goods sold and compensation. A **gross receipts tax** also known as **gross excise tax** is a tax on the total gross revenues of a company, not minding their source. A gross receipts tax is usually compared to a sales tax; although the two differ in the sense that while a gross receipts tax is levied upon the seller of goods or services, a sales tax is nominally levied upon the buyer (although both are usually collected and paid to the government by the seller.

ii. Corporate franchise tax: This is **a tax levied on corporations, LLCs, and partnerships by a state.** This tax is assessed to these companies for the privilege of either doing business in the state or incorporating their business in that state. Like income taxes, typically franchise taxes are assessed annually.

iii. Employment withholding tax: this is a kind of tax arrangement where a **set amount of money is taken out of an employee's paycheck and pays it to the government**. The money taken is a credit against the employee's annual income tax. If too much money is withheld, an employee will receive a tax refund; if not enough is withheld, an employee will have an additional tax bill.

iv. Excise tax: An **excise tax** or simply :excise” is any duty on manufactured goods that is levied at the time of manufacture rather than at sale. Excises are usually associated with customs duties (which are levied on pre-existing goods when they cross a designated border in a specific direction); customs are levied on goods that become taxable items at the *border*, while excise is levied on goods that came into existence *inland*. An excise tax is an indirect tax, which means that the producer or seller who pays the levy to the government is expected to recover their loss by raising the price paid by the eventual buyer of the goods. The buyers will eventually bear the burden although unaware.

v. Value-added tax (VAT): A value-added tax (VAT), is referred to as a goods and services tax (GST) in some jurisdictions. It is a type of tax that is assessed incrementally. It is levied on the price of a product or service at each stage of production, distribution, or sale to the end consumer.

In addition, some industries, such as mining and insurance, companies may need to pay other forms of taxes. While these pay income tax, property tax, and sales tax, these taxes are not specific to business and are thus not generally considered business taxes. In any case, the economic impact of tax payment qualifies all taxes as "people taxes," since they impact people on a personal level.

1.3.3 Tax Liability for Business

As a business owner, especially for small and medium businesses, you need to manage many different expenses, including the business' taxes to make way for the required growth. This is because, several aspects of the company will be subject to taxation, as required by the relevant authorities. The amount of money you owe to federal, state, and local tax authorities through the business you operate is your tax liability. Tax money are in turn used by the government to fund administration and social programmes.

As tax liability is a legally binding debt, failure or refusal to pay tax is an offence and may attract penalties from the relevant authority. Tax liability is a short-term liability, which means that it must pay it within a year. Short-term liabilities, such as tax liability, may be recorded together in your accounting workbook or balance sheet.

Any business transaction that has a tax consequence is referred to as "taxable event". It is important to note that the government has the right and authority to determine which events are taxable. Any time a taxable event takes place in the business, you will need to pay the concerned tax authority. Taxable income, issuing payroll, and making sales are all taxable events. Different taxable events will require different levels and amounts of tax liability, which are calculated as a percentage of the total event. For instance, selling a product is a taxable event for which the government reserves the right to charge you sales tax. However, rather than paying sales tax out of your own pocket, you can include the amount in the total price that you charge customers. After you collect sales tax, you notify and send it to the appropriate government agencies. You can pay sales tax on a regular basis (quarterly or monthly).

1.3.4 Calculation of Business Taxes

The knowledge of tax laws and rules is very crucial to business owners. Further to this, there need to understand taxation processes and know exactly when and how to perform business and personal transactions that would help to reduce your tax obligations. As a business owner you are automatically a taxpayer. There are typically multiple ways to complete a taxable transaction, one of which will result in the reduction of legal tax liability. It should be noted that, it's smart to avoid taxes, but it's illegal and an offence to evade taxes through fraud, concealment or deceit.

If you are engaged in a "trade or business," which means that you are conducting business activities for livelihood or profit, it means that you may be able to deduct business expenses. A trade or business is one in which both a profit motive and economic activity are present. All of taxable income will be calculated according to the tax year. All income received or accrued during a single year is recorded on that year's tax return, along with expenses paid or accrued. It means that once the tax year ends, any tax-saving strategies must have already been applied.

The business must need to report the accounting method to the relevant authority. In many jurisdictions, the two basic methods most applicable to small business owners are "cash" and "accrual." Under some circumstances, however, you might be able to use a hybrid that combines components of both. Moreover, certain kinds of businesses may be allowed to use special accounting methods.

In conclusion, it is already a trite knowledge that both entrepreneurs, corporations, partnerships and their joint owners as well even the people who engage in agriculture and forestry are subject to business taxation. The profits of private business persons and self-employed persons are taxed as entrepreneur's income. The profit of a business partnership is taxed as income of the joint owners in line with the regulations on the taxation of joint owners of business partnerships, while corporations such as limited companies are taxpayers themselves, that pay a corporation tax on their profit. A dividend paid by a corporation is taxed as income of the shareholders.

1.4 Summary

In this unit, we carefully discussed trading profit, examined the types of business taxes, tax liability for businesses and calculation of business taxes

1.5 References/Further Readings/Web Resources

A. Ayua, The Nigerian tax Law (Nigeria, Spectrum Law Publishing:1999)

1.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. Investments and Operations Perspectives
2. Tax liability is the total amount of tax debt owed by an individual, corporation, or other entity to the relevant taxing authority.

UNIT 2 EXPENDITURES

Unit Structure

2.1 Introduction

Expenditure represents payments with either cash or credit to purchase goods or services. Trading companies or businesses must manage trading-related expenses, such as freight, loading charges, storage costs, insurance, customs duty and commission efficiently. It is also important to accurately assess costs, including purchasing costs and all trading charges associated with the trading contract which make up business expenditures.

2.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- explain the term, 'Trading Expenditures'.
- gain useful knowledge on Capital and Revenue Expenditures.

2.3 Expenditures

2.3.1 Trading Expenditure

Trading or business expenses are costs incurred in the ordinary course of running business. These expenses are applicable to small entities or large corporations. Trading expenses are part of the income statement of the business. On the income statement, trading expenses are subtracted from revenue to arrive at a company's taxable net income. There are various types of expenses in the trading environment, all of which are incurred at different times and posted to different accounts, and these are usually not synchronized with the main flow of a trading contract. At the time you are calculating the profit for business, the business owner is entitled to claim a deduction for expenses incurred in setting up or running the business.

The expenses that entitled to claim for are those that are directly related to the running of the business. These include:

i. the purchase of goods for resale
ii. rent and bills for your business premises
iii. employees' pay
iv. running costs for vehicles or machines that you use in your business
v. lease payments for vehicles or machines that you use in your business
vi. interest payments for money you borrowed to finance your business
vii. accountancy fees however, relief for some expenses cannot be claimed for the purposes of taxes. For instance, one cannot claim expenses for any items that are not fully and directly connected to the running of the business. Such expenses are:
    i. clothing (except protective clothing)
    ii. business entertainment expenses
    iii. expenses for personal pay
    iv. expenses for personal food or travel (except those described in the Food and Accommodation Expenses and Travel Expenses manuals).

Also, no claim can be made for a deduction for capital expenditure when calculating the business profit. Capital expenditure is money spent on buying or maintaining land, property or equipment for your business. However, you may claim capital allowances on some of this expenditure.
Some expenses are incurred before even the commencement of the trade. This is referred to as pre-trading commences. In any case, a sole trader may incur costs before setting up their trade. Some of these pre-trading expenses are also allowable for tax purposes subject to being ‘wholly and exclusively’ for the trade or profession. Equally, capital items purchased prior to trading may also qualify for capital allowances.

Self-Assessment Exercise 1

Attempt these exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. Exclusions, deductions, deferrals, credits, and tax rates are examples of _
2. In what ways can you differentiate capital from revenue expenditures?

2.3.2 Capital and Revenue Expenditure

Capital expenditures are basically one-time large purchases of fixed assets that will be used for revenue generation over a longer period. On the other hand, revenue expenditures are those ongoing operating expenses, which are short-term expenses incurred in the course of day to day running of business. Furthermore, while capital expenditures are for fixed assets, that are expected to be productive assets for a long period of time, revenue expenditures are otherwise for costs that are related to specific revenue transactions or operating periods, such as the cost of products sold or repairs and maintenance expense.

The differences between these two types of expenditures are in the following ways:

i. In relation to time, capital expenditures are charged to expense gradually through depreciation, and over a long period of time. Depending on the type of the asset, depreciation charges could extend out for several years even for more than a decade. On the other hand, revenue expenditures are charged to expense in the current period, or shortly thereafter.
ii. in relation to size, capital expenditures usually tend to involve larger monetary amounts than revenue expenditures. The reason for this is because an expenditure is only classified as a capital expenditure if it exceeds a certain threshold value; if not, it is automatically categorized as a revenue expenditure. However, some large expenditures can still be classified as revenue expenditures, in as much as they are directly associated with revenue transactions.

Examples of these capital expenditures are; buildings, computers, furniture and fixtures, machinery, and vehicles, while that of revenue expenditures are; administrative expenses, compensation, research and development, property taxes, travel, and utilities

2.3.3 Disallowed Expenditure

When computing the profit and gains from business or profession, certain expenditures are disallowed. The implication is that the income tax department does not allow the benefit of such expenditures and the assesses are required to pay taxes on such expenditures by adding it back to the net profits.

Tax expenditures are special provisions of the tax procedure such as exclusions, deductions, deferrals, credits, and tax rates that benefit specific activities or groups of taxpayers. Thus, tax expenditures usually are alternatives to direct spending programs or regulations to accomplish the same purpose.

2.4 Summary.

Under this unit, we discussed trading/business expenditure, capital and revenue expenditure and disallowed expenditure.

2.5 References/Further Readings/Web Resources

Ariwodola J.A (2001), Personal Taxation in Nigeria, (4th ed.), Lagos: JAA Nigeria Limited

2.6 Possible Answers to Self-Assessment Exercises

SAE 1

1. Tax Expenditures

UNIT 3 INVESTMENT INCOME

Unit Structure

3.1 Introduction

Investment income refers to the money received in interest payments, dividends, capital gains realized with the sale of stock or other assets, including any other profit realised through an investment vehicle. Interest earned on bank accounts, dividends received from stock owned by mutual fund holdings, and the profits on the sale of goods are all considered investment income. Income from long-term investments usually undergoes different and often preferential tax treatment, which varies from jurisdiction to jurisdiction.

3.2 Intended Learning Outcomes

By the end of this unit, you will be able to:

- gain good knowledge on investment income and the items in it.

3.3 Investment Income

3.3.1 Items in Investment Income

Investment income means the financial gains above the original cost of the investment. This may take different forms, such as interest or dividend payments. The form which it takes is however irrelevant to it being considered investment income in as much as the income is generated from a previous investment. Furthermore, investment income may be received as a lump sum or in regular interest installments paid out over a period of time.

It should be noted that virtually all investment income is subject to preferential tax treatment when the income is realized. The associated tax rate is however based on the form of investment producing the income and other nature of an individual taxpayer's situation.

Self-Assessment Exercise

Attempt the following exercises to measure what you have learnt so far. This should not take you more than 5 minutes.

1. What is dividend?
2. The financial gains above the original cost of the investment is generally referred to as what?

Items in investment income include the followings:

i. Dividends:

This refers to a reward, whether cash or otherwise, that a company gives to its shareholders. Dividends can be issued in various forms, including cash payment, stocks among other forms. Dividend is usually a part of the profit that the company shares with its shareholders. Dividends received by a Nigerian resident company from another Nigerian resident company are taxable at source and after that, not subject to further tax.

On the other hand, dividends received from non-resident companies are taxable except if repatriated into Nigeria through government-approved channels that is, any financial institution authorised by the Central Bank of Nigeria to deal in foreign currency transactions.

Dividends received from small manufacturing companies are exempt for tax purposes during the first five years of operation. Dividends from investments in wholly export-oriented businesses are also exempt.

ii. Discount:

A discount is the amount a price is reduced. To calculate a tax, you can convert the percentage to a decimal, then multiply it by the price. In order to ascertain the total cost, including the tax, you can multiply the original price by one plus the decimal.

iii. Interest

The interest accrued on a basic savings account is treated as investment income. The interest is earned on top of the original investments, which are the deposits placed into the account. That makes the account a source of income.

iv. Annuity

An annuity refers to a contract between you and an insurance company in which you make a lump-sum payment or series of payments and, in return, receive regular disbursements, beginning either immediately or after a period of time. It refers to a series of payments made at equal intervals. Regular deposits to a savings account, monthly home mortgage payments, monthly insurance payments and pension payments are good examples of annuities.

In conclusion, it should be noted that of the fundamental questions concerning the taxation of investment income such as gains, allowable deductions, calculation and remittance systems for tax collection, and tax accounting rules, are also important to such income derived by individuals and to that derived through partnerships, companies, and other entities or relationships.

3.4 Summary

In this unit, we discussed mainly investment income and its items.

3.5 References/Further Readings/Web Resources

Kellison, Stephen G. (1970). *The Theory of Interest*. Homewood, Illinois: Richard D. Irwin, Inc. p. 45

3.6 Possible Answers to Self-Assessment Exercises

SAE

1. Dividends refer to a reward, whether cash or otherwise, that a company gives to its shareholders.
2. Investment income.