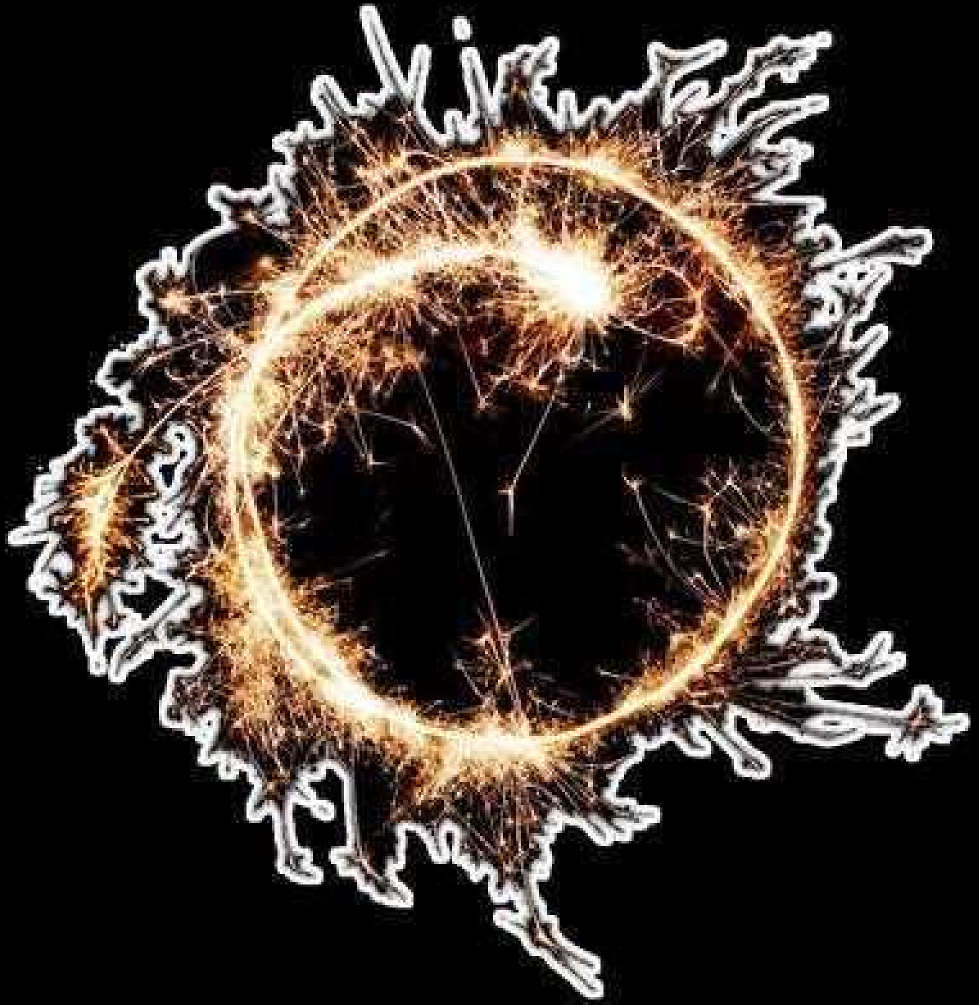

ICAN Gbagada

Agitation for VAT Administration by State Governments: Implication for Businesses

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Fiscal Federalism ….what it entails

Federalism and Fiscal Federalism

- Fiscal Federalism has its roots in Federal System of Government – mixed mode of government that combines a central control with regional control in a single political system
- The control system seeks to share power between the Centre and the Regions
- According to Encyclopaedia Britannicca, Fiscal federalism deals with the division of governmental functions and financial relations among levels of government.
- Fiscal Federalism itself came to light in 1959 through a German-born American economist **Richard Musgrave**

Fiscal Federalism Components – Musgrave's concept

- Just distribution of Income (redistribution) - may be ceded to the Centre. This takes into consideration that income generating power of state is unequal, Federal powers are required for re-allocatino (transfers)
- Allocation of resources – may be left to regions to make it more effective
- These concepts and battle for control especially over revenue distribution and allocation of have generated series of issues(disputes, resolutions and concessions) between the center and regions
  - Resource control – AG Abi & 36 Ors
  - Onshore – Offshore Dichotomy
  - Tourism & Lottery
  - Most recently VAT Administration

Value Added Taxes – More background and Insight

- Value Added Taxes are indirect consumption taxes imposed on supply of goods and services except those specifically exempt.
- VAT is different from Sales Tax. Sales Tax has lower rate and applied at each point of sale
- VAT has input/output set off mechanism

- NASS' power to legislate is derived form Exclusive Legislative List (ELL)
- ELL – prescribes items NASS' can legislation on – (but not the type of legislation)e.g. over 3 income tax laws
- ELL includes "stamp duties, taxation of incomes, profits and capital gains." – *FHC's decision was premised on this*

- VAT is governed by the VAT Act, 1993 (Decree)
- Given Legitimacy by Section 315 Constitution of the Federal Republic of Nigeria, 1999 (as amended) ("the Constitution")
- Premised on the powers of National Assembly (NASS) to legislate

- ELL item 62) also covers "**Trade and Commerce**" – in particular, import, export and inter state trade ***Aberuaagba's case 'in particular' is restrictive***
- Item 67 – "Any other matter with respect to which the National Assembly has powers to make laws in accordance with the provisions of this Constitution."
- Section 68 – "Any matter incidental or supplementary to any matter mentioned elsewhere in this list."

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Situation as it stands ....What Next

- Court of Appeal mandates maintenance of status quo ante –bellum
- *VAT Act stands*
- *Businesses should continue filings & payment shall be to FIRS*

- *Lagos State and Rivers State Laws are in abeyance – inapplicable*
- *FIRS may challenge State Laws for their weaknesses*
  - *Inability to charge VAT on import*
  - *Restriction from legislating on Inter state*

- FIRS issued letters urging filing of VAT returns per branch – wanted to issue VAT Registration no per branch
- FIRS has since stopped the move
- Awaiting Appeal .... final decision could still go to Supreme Court
- Suggested amendment to constitution – State & FIRS

Practical realities

Practical realities – States win

- *Federal continues to claim VAT on import*
- *No Input/output*
- *Federal can claim tax on inter state activities*
- *Complexities of Headquarter and centralized functions e.g. bank approvals/activities*
- *Double taxation – which is against constitution*
- *Administrative chaos – businesses and SIRS*
- *Possibly different rates/returns etc.*
- *Increased difficulty in doing business*
- *Changes to Constitution*

Practical realities – Federal Win

- *Continue administration as we have it - 2022 Budget assumes Federal continues with VAT*
- *Improved derivation principles*
- *Demand for more/better accountability*
- *Better collaboration*
- *Change in law – VATA and Constitution*
- *State Laws become unconstitutional and the doctrine of covering the field applies*
- *Businesses may consider framework for isolating commingle cost for VAT – where easily achievable (changes to ERPs etc.)*

What is the doctrine of covering the field?

The doctrine of covering the field typically operates in a federal system where there are law making bodies at different tiers.

The Nigerian Constitution by its provision for a CLL creates a potential for such conflict.

Under Part II, Section 5 of the Constitution, if any law enacted by a SHA is inconsistent with any law <u>validly</u> made by the NA, the law made by the NA shall prevail and the other law shall to the extent of the inconsistency, be void.

The law by the NA will always prevail provided it is validly made and has sufficiently provided for the matters for which the State law covers

The Exclusive Legislative List ("ELL") enumerates the matters for which only the NA may make laws while the Concurrent Legislative List ("CLL") refers to matters over which both the National and State Houses of Assembly (SHA) enjoy shared competences

Items not listed in the ELL or the CLL are deemed to be left to an imaginary 'residual list' for which the State may legislate on. See Section 4(7) (a)of the Constitution.

However, please note that there is nothing as a residual list under the Constitution

Section 4(7) (a) and (b) empowers the SHA to make laws on matters listed in the CLL as well as on matters not included in the ELL.

Judicial Developments on VAT in Nigeria pre-1999

- The 1979 Constitution just like the 1999 Constitution was silent on consumption/sales/value added taxes, some states had Sales Tax Laws.
- Curiously however, **in AG Ogun State v Aberuagba (1985) –** the Supreme Court held that the **Sales Tax Law of Ogun State was invalid as it encroached on the Exclusive Legislative Powers of the NA**. However, the Court acknowledged that the control of the economy is not within the exclusive powers of the federation and therefore it was wrong to conclude that control over the national economy since trade and commerce was an integral part of the national economy implied exclusive control over every aspects. That trade within a state was within the residual powers of a state.
- **Nigeria Soft Drinks v AG Lagos State –** the Court of Appeal upheld the Lagos State Sales Tax Law on the basis that it did not seek to tax items under the ELL
- In 1993, the VAT Act was promulgated as a Decree No. 102 by the then General Ibrahim Babangida, this by implication, covered the field on VAT or sales taxes
- In 1999, following the return to democracy, States like Lagos reintroduced sales taxes resulting in disputes

Judicial Developments on VAT in Nigeria post-1999

- **AG Lagos State v Eko Hotels Limited** on Sales Tax Law, 1995 (STL) and Sales Tax (Schedule Amendment) Order 2000 (STO). Eko Hotels having received demand notices from both the FIRS and LIRS approached the court for interpretation. The Supreme Court agreed with both the Federal High Court and the Court of Appeal that Eko Hotels remit to the FIRS. It applied the principle of covering the field. The validity of the VAT Act was not considered

- **The Registered Trustees of Hotel Owners and Managers Association of Lagos (the Association) v AG Fed & Anor.** on the Occupancy and Restaurant Consumption Law of Lagos State which imposed 5% consumption tax on the value of goods and services consumed in hotels, restaurants and event centres in Lagos State. The Association approached the Federal High Court (FHC) on the basis that the VAT Act already covered the field. The FHC ruled in favour of the Lagos State on the basis that the SHA have the competence to legislate on consumption taxes

- **Nigeria Employers Consultative Association (NECA) & Anor v AG Fed & 2 Ors** - In 2017, the Kano State Revenue Administration (Amendment) Law imposed 5% consumption tax on consumers of goods and services bought or rendered in any hotel, restaurant, eatery, bakery, takeaway, suya spot, shopping mall, store, event centre and other similar businesses within the state. This was challenged. The Court invalidated the relevant sections 96 and 97 of the Law as the VAT Act had already covered the field. The Court also set aside Section 7(b) item 13 of the Taxes and Levies (Approved List for Collection) Act Amendment Order 2015

- **Emmanuel Ukala v FIRS (2020) –** Similar to the Rivers case, the Plaintiff challenged the powers of the NA to legislate on matters not listed in Items 58 and 59. The VAT Act was declared null and void. The Court based its decision on *expression unius est exclusio alterius*

- In **Uyo Local Government Council v Akwa Ibom State Government & Anor. [2020] LPELR-49691 (CA),** the Court nullified the Taxes and Levies Act for being inconsistent with the Constitution

Thank you