BANWO & IGHODALO

Grey Matter Tax Digest

A specialised newsletter providing strategic alerts and comprehensive analyses on tax matters in Nigeria

SPECIAL ISSUE: SEPTEMBER 2021

DOES THE FEDERAL GOVERNMENT HAVE THE CONSTITUTIONAL POWERS TO LEGISLATE ON VAT?

Background

The Federal High Court ("**FHC**" or "**the Court**"), recently delivered judgment in a case instituted in the Port Harcourt Division of the Court by the Attorney General of Rivers State against the Federal Inland Revenue Service ("**FIRS**") and the Attorney-General of the Federation ("**AGF**"), respectively[1]. In the judgment, the Court reaffirmed, re-delineated and re-compartmentalized the constitutional competence of the National Assembly and the Houses of Assembly of the respective States of the Federation to legislate on taxation matters (the "**Decision**").

The FHC in the said judgment specifically held as follows:

- That the Federal Government of Nigeria ("**FGN**") lacks the power to legislate on taxation matters, other than in respect of stamp duties and the taxation of incomes, profits, and capital gains pursuant to the provisions of Items 58 and 59 of Part I of the Second Schedule to the Constitution of the Federal Republic of Nigeria 1999 (as amended), (the "**Constitution**"), and the residual powers conferred on the State Houses of Assembly to make laws under section 4(7) of the Constitution;

- That the FIRS does not have the power to enforce and administer laws inconsistent with, or which exceed the legislative powers of the National Assembly; and

- That the legislative competence of the National Assembly to impose

[1] (Unreported judgment of the FHC, delivered by Hon. Justice Stephen Dalyop Pam, on August 9, 2021, in Suit No. FHC/PH/CS/149/2020).

taxes and levies, and to delegate the power to collect taxes, does not include the power to levy or impose any form of sales tax, such as Value Added Tax ("**VAT**") or any other similar taxes.

The Court further held that:

- There is no constitutional basis for the FGN's imposition of, demand for, and collection of VAT, Withholding Tax ("**WHT**"), Education Tax, and Technology Levy in Rivers State or any other State of the Federation;

- The legislative competence of the National Assembly in relation to taxation and related matters, is limited to the imposition of stamp duties and the taxation of incomes, profits, and capital gains, which does not include VAT, WHT, Education Tax, Technology Levy, or any other species of sales tax or other levy not specifically mentioned in items 58 and 59 of the Exclusive Legislative List, set out in Part I of the Second Schedule to the Constitution; and

- Only the States of the Federation are competent and empowered to impose taxes enforceable or collectible within their respective territories, such as consumption or sales tax, VAT, Education Tax, and other tax or levies, other than the taxes and levies specifically reserved for the FGN under Items 58 and 59 of the Exclusive Legislative List.

The Court also held and opined, that the *Taxes and Levies (Approved List for Collection) Act*[2] (the "**Approved Taxes Act**") is unconstitutional, null and void. In reaching this decision, the FHC relied on the case of ***Uyo Local Government Council v Akwa Ibom State Government & Anor.***,[3] where the Court of Appeal nullified the Approved Taxes Act for being inconsistent with the provisions of the Constitution, and consequently declared that any tax or levy contained therein is automatically unconstitutional, null and void – except such tax or levy is expressly provided for in the Constitution or any other law validly enacted by a competent legislature.

The FIRS has since appealed the Decision and several events have snowballed since the Decision was handed down by the FHC, notably; the passage of VAT Laws by Rivers and Lagos States. The FIRS, pre-empting the outcome of the case, wrote to the National Assembly to seek an amendment of the Constitution to accommodate the inclusion of VAT

[2] Cap. T2 Laws of the Federation of Nigeria ("LFN") 2004.
[3] (2020) LPELR-49691(CA).

collection in the Exclusive Legislative List. The National Assembly is yet to act on the FIRS request.

On September 10, 2021, following an appeal filed by the FIRS, the Abuja Division of the Court of Appeal handed down a *status quo* order effectively restraining the parties from giving effect to the Decision until the determination of several pending interlocutory applications, including an application filed by the Lagos State Government to join the appeal as an interested party.

A *status quo* order may be issued by a court to prevent any of the parties involved in a dispute from taking any action in relation to the dispute pending the resolution of the underlying dispute. It seeks to prevent harm or preserve the existing conditions, so that a party's position is not prejudiced in the meantime until a resolution of the underlying dispute.

The Rivers State Government has lodged a further appeal to the Supreme Court to challenge the propriety of the *status quo* order on various grounds. As at the date of publication of this commentary, the Supreme Court is yet to hear and/or determine the appeal filed the Rivers State Government.

Even though the Decision covers the powers of the FGN / FIRS regarding imposition and collection of VAT, WHT, Education Tax and Technology Tax, the VAT aspect of the Decision has generated significant controversy and interests amongst members of the public.

This commentary highlights and presents an independent and neutral evaluation and analysis of the constitutional issues, as well as the possible gaps and lacuna, which the Decision throws up with respect to VAT.

Delineation of legislative powers under the Constitution

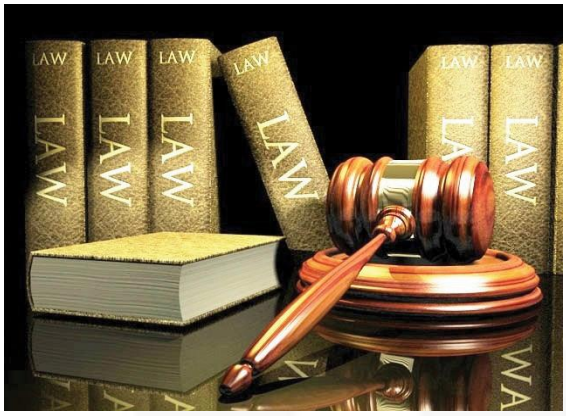
The Constitution clearly delineates legislative powers between the FGN and the State Governments by providing for two legislative lists, namely: (i) the Exclusive Legislative List (**"ELL"**) set out in Part I of the Second Schedule to the Constitution; and (ii) the Concurrent Legislative List (**"CLL"**) set out in Part II of the Second Schedule to the Constitution.

The FGN, through the National Assembly, has exclusive powers to make laws with respect to any matter contained on the ELL.[4] It also has concurrent powers with the State Governments to make laws with respect to any matter contained on the CLL, to the extent provided for in the Constitution.[5] Further, the FGN has powers to make laws on any other matter, as may be prescribed by any specific

[4] See section 4(3) of the Constitution.

[5] See section 4(4)(a) of the Constitution.

substantive provision of the Constitution,[6] and also exercises legislative powers with respect to the Federal Capital Territory, Abuja.[7]



On the other hand, State Governments, through their respective State Houses of Assembly, have powers to legislate on matters contained on the CLL, to the extent prescribed therein. They may also legislate on any matter as may be prescribed by the provisions of the Constitution. State Governments also, have exclusive powers to legislate on matters that are not contained in either the ELL or CLL (i.e., residual matters).

Power to impose and collect VAT

The competence of State Governments to impose consumption tax and the validity of the Value Added Tax Act[8] ("**VAT Act**"), have been the subject of several judicial decisions.

As far back as 1985, in the *locus classicus* case of ***Attorney-General of Ogun State v Aberuagba,***[9] the Supreme Court held that State Governments are only empowered to impose sales tax (a form of consumption tax) on intra-state transactions, without more. The implication of the Supreme Court's decision is that State Governments cannot validly impose sales tax on inter-state or international transactions, both of which are matters exclusively reserved for the FGN on the ELL. Thus, the Supreme Court struck down the Sales Tax Law of Ogun State to the extent that it imposed sales tax on international and inter-state trade and commerce.

In the more recent case of ***Attorney-General of Lagos State v Eko Hotels***,[10] the Supreme Court considered whether a conflict exists between the provisions of the VAT Act and the Sales Tax Law of Lagos State. The 1st Respondent (Eko Hotels Limited) was required, under both legislation, to collect tax at the rate of 5% on the price of the goods and services offered to its customers, and to further remit same to the relevant tax authorities. The 1st Respondent argued that it was difficult to comply with both statutes, as it would amount to double taxation. The Supreme Court noted that both the VAT Act and the Sales Tax Law of Lagos State provide for the collection of consumption tax on certain consumable items and that the rates upon which charges were made under both laws were similar. The Supreme Court ultimately held that the VAT Act had fully covered the field on consumption tax in Nigeria, and to that extent, the Lagos State Sales Tax Law was void. The Supreme Court reasoned that applying both laws simultaneously would amount to double taxation, with the

[6] See sections 4(4)(b) and 4(4) and Part II of the Second Schedule to the Constitution.
[7] See Fasakin Foods (Nig.) Ltd. v Shosanya (2006) 4 KLR (Pt. 216) 1447.
[8] Cap. V1 LFN 2004 (as amended by the Value Added Tax (Amendment) Act 2007, the Finance Act 2019, and the Finance Act 2020).
[9] (1985) 1 NWLR (Pt. 3) 395.
[10] (2017) LPELR-43713(SC).

consumers ultimately bearing the financial burden of both statutes.

In our view, the later decision of the Supreme Court in ***Attorney-General of Lagos State v Eko Hotels*** appears to conflict with the decision in ***Attorney-General of Ogun State v Aberuagba***, in the sense that the Supreme Court did not recognize the dichotomy of legislative powers between the Federal and State Governments as specifically recognized and delineated by the Constitution.

Instructively, section 4(3) of the Constitution and paragraphs 62 and 68 of the ELL vest exclusive powers to legislate on international and inter-state trade and commerce (including matters incidental or supplementary thereto) in the FGN. In contrast, intra-state trade and commerce are residual matters and are within the exclusive legislative remit of State Governments under section 4(7) of the Constitution.

The effect of the foregoing delineation of legislative powers is that, the power to impose consumption tax is effectively shared between the FGN and the State Governments. The FGN's consumption taxation powers are limited to international and inter-state trade and commerce while the consumption taxation powers of the State Governments are limited to intra-state trade and commerce. Accordingly, it is arguable that the VAT Act is invalid to the extent that it imposes consumption tax on intra-state trade and commerce. Similarly, any law enacted by a State Government would arguably be invalid to the extent that such law imposes consumption tax on international and inter-state trade and commerce.

Premised on the foregoing, we reasonably believe that the FHC was correct in holding that State Houses of Assembly are competent to legislate on imposition and collection of VAT on consumption transactions within their geographical territories. However, the FHC's pronouncement that State Governments are the only authority with the powers to impose and collect VAT on all transactions that are subject to VAT within their territories, is problematic to the extent that the FHC did not draw the distinction between inter-state and intra-state transactions as clarified by the Supreme Court in the *Aberuagba's* case and the provisions of the Constitution.

The Decision has again brought to the fore the gaps and lacuna in the Constitution which have led to the controversy around VAT. The view that VAT is a residual matter within the exclusive remit of State Governments may be attributable to the fact that VAT is not specifically mentioned in the ELL. However, this view does not take into consideration the fact that the FGN has powers to impose and collect consumption tax (such as VAT) on transactions pertaining to "*international trade and commerce*", which fall within the ELL. The foregoing is underscored by the fact that the taxation powers of the FGN extend to the imposition and collection of any form of tax that may be

incidental to the matters listed in the ELL, including *international trade and commerce*.[11]

Following the Decision, the FIRS and the Rivers State Internal Revenue Service have issued public statements asserting the right to collect VAT. A similar scenario is playing out in Lagos State and other interested States of the Federation. With this development, individuals and corporate entities liable to charge and remit VAT on consumption transactions may be thrown into confusion as to the appropriate tax authority to deal with, given that before the Decision, all VAT remittances were made to the FIRS. In the face of contending claims, a possible way out is to issue an interpleader summons, in order to avoid paying penalties for default, and the risk of adverse actions from both entities.

Conclusion

Undoubtedly, the Decision has far-reaching political, legal, fiscal and economic significance for all stakeholders in the Nigerian tax space – FGN, State Governments, and taxable corporate entities and individuals. As the general public awaits the pronouncements of relevant appellate courts on the issues in the course of time, taxpayers and tax authorities alike will need to keep a close eye on developments regarding the Decision and appropriately structure their business and administrative operations.

With more States aligning with the Decision and taking a cue from the actions of the State House of Assembly in Rivers and Lagos States (with respect to enacting a VAT Law), a new wave of debates around the restructuring of the Nigerian system; for the proper and effective operation of fiscal federalism has emerged. In one of the resolutions passed in their recent meeting held in Enugu, Governors from the southern region of Nigeria declared that State Governments, rather than the FIRS, should collect VAT[12]. In the circumstances, and without prejudice to the rights of parties to the case before the court to seek legal redress, we believe that finding a political solution to the VAT controversy may be a less hostile, less-cumbersome and more efficient option.

The Grey Matter Concept is an initiative of the law firm, Banwo & Ighodalo.

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- Click here to read Power of the FIRS to access taxpayers' servers and other matters: Examining the contentious issues arising from The Federal High Court (FIRS) Practice Directions, 2021

[11] A combined reading of Section 4(3) and Item 68 of the Exclusive Legislative List shows that the FGN has exclusive powers to legislate on any matter listed in the list, including matters incidental or ancillary thereto. The power to tax a subject matter is naturally ancillary or supplementary to the power to legislate on the subject matter.

[12] https://www.channelstv.com/2021/09/16/southern-governors-back-vat-collection-by-states-zoning-of-2023-presidency-to-south/

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