# PwC secures landmark decision - "sales in the ordinary course of business not subject to WHT"

December 2020

## Legal basis and FIRS practice

The Companies Income Tax (Rates, Etc., of Tax Deducted at source) Regulations 1997 (WHT Regulations) requires that tax is withheld on payment for certain qualifying services. The rates are either 2.5%, 5% or 10% depending on the specific service.

The WHT Regulations provide that *"all types of contracts and agency arrangements other than sales in the ordinary course of business"* are subject to WHT at 5%. This means that sales in the ordinary course of business would not be subject to WHT. However, the WHT Regulations do not define what amounts to "sales in the ordinary course of business" (SITOCOB).

Interestingly, the Federal Inland Revenue Service (FIRS) puts pressure on taxpayers to deduct WHT on all payments whether or not they are in respect of "sales in the ordinary course of business". This imposes a practical burden on low margin businesses (like trade and manufacturing). To avoid assessments and penalties from FIRS, businesses that make such purchases impose WHT on such payments.

## Background to the appeal

The principal activities of Tetra Pak ("the Company") involved importing and sale of packaging equipment and spares, installing equipment and providing after sales repairs.

The Company's customers deducted WHT on its fees for sales provided in the ordinary course of its business. As a result, the Company paid companies income tax (CIT) via WHT in years where it did not make a profit. This impacted the Appellant's cash flows considering that FIRS did not refund the WHT as it is required to do by the Companies Income Tax Act (CITA) and the Federal Inland Revenue Service (Establishment) Act (FIRSEA).

To manage the impact, the Company wrote to FIRS for confirmation that such sales should not be subject to WHT. FIRS ruled otherwise relying on some WHT Information Circulars. The Company appealed to the Tax Appeal Tribunal (TAT) challenging FIRS' position and asking for a refund as well as interest on the WHT.

## The Company's arguments

The Company argued that:

- "SITOCOB" should be given its literal meaning since it was not defined either in CITA or WHT. In addition, FIRS was wrong to attempt to define the phrase via its Information Circulars on WHT in a manner that was inconsistent with the WHT Regulations,
- the rule of interpretation that a specific provision would override the general should be applied distinguishing SITOCOB from "all types of contracts",
- SITOCOB was a question of fact which can be determined from what a business does routinely.
- The Company further relied on a Court of Appeal decision in *Nigerian Breweries v Oyo State Board of Internal Revenue* where the court alluded to the fact that such sales would be exempt from WHT.

## FIRS' arguments

Interestingly, FIRS did not deny that the Company sold packaging equipment or spares routinely. However, it argued that once a sale was completed via a formal contract, it was no longer exempt from the WHT regime but had "forayed into contract" with rights and obligations and therefore subject to WHT. In support, FIRS asked the Tribunal to apply the ejusdem generis rule.

## The TAT's Decision

**Are SITOCOB liable to WHT -** The TAT agreed with the Company that SITOCOB are not liable to WHT. In arriving at its decision the TAT held that although the WHT regime is a collection device, the primary objective is to prevent evasion. Therefore, in this case, there was no occasion for tax evasion as claimed by FIRS, since the taxpayer was not tax anonymous.

The TAT also held that SITOCOB was a question of fact and a tax authority has the responsibility of determining whether a business activity amounted to a SITOCOB. The TAT provided some guidance in determining whether an activity was a SITOCOB –

- whether the activity was contained in the memorandum and articles of association,
- the type of industry the taxpayer operates in,
- the history and antecedents of the taxpayer and
- the frequency of carrying out the activity.

**Refund and payment of interest by FIRS -** The TAT refused to make an order for refund of the excess WHT and interest on the ground that these were not specifically pleaded by the Company.

**Review of WHT rates -** From an administrative perspective, the TAT held that the WHT regime should consider the effective tax rates (ETR) of different industries before imposing WHT to ensure that companies do not suffer more tax than necessary.

## Takeaway

The TAT has finally resolved a long standing, but seemingly straightforward question, of whether SITOCOB should be subject to WHT. The argument by the FIRS that once a contract is established, it would not constitute a SITOCOB is flawed because by saying "…other than sales in the ordinary course of business", the WHT Regulations acknowledge that SITOCOB are contracts but specifically excludes them from WHT. Taxpayers and tax authority can apply the tests provided by the TAT instead of the contradictory position in various FIRS circulars.

With respect to WHT remitted to FIRS before the decision, taxpayers are entitled to refunds per sections 81(7) of CITA and 40 of the FIRSEA which provide that any WHT collected should be refunded to the taxpayer within 90 days. Therefore, the authority has a responsibility to refund such taxes with 90 days.

Though the TAT did not grant the claim for a refund, there is a duty on FIRS to do so within a specific time. Therefore, to give effect to its decision. the TAT could have made a consequential order directing FIRS to refund within the statutory period any WHT wrongly remitted to and collected by the FIRS.

## TCDR Publication – January 2021


The next issue of our Tax Controversy & Dispute Resolution (TCDR) publication will be issued in January 2021. The issue would include articles on the power of the Honourable Minister for Finance to issue Orders to amend existing legislation, VAT on both commercial and residential leases vis a vis recent decisions of the Tax Appeal Tribunal (TAT) and the Finance Act 2019.

## For more information, contact any member of our Tax Controversy & Dispute Resolution (TCDR) team


**Kenneth Erikume**
M:+234 805 609 9622
E: kenneth.y.erikume@pwc.com

**Folajimi Olamide Akinla**
M:+234 802 846 3369
E: folajim.akinla@pwc.com

**Vivian Ezepue**
M:+234 808 934 9840
E: vivian.ezepue@pwc.com