PwC secures a landmark TAT decision in a VAT case on imported services

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In brief

On 10 June 2015, the Tax Appeal Tribunal (TAT) sitting in Abuja held that foreign companies providing services outside Nigeria to Nigerian companies are not carrying on business in Nigeria for the purposes of the Nigerian Value Added Tax (VAT). As they are not carrying on business in Nigeria, they are not required to register for, or charge Nigerian VAT. A Nigerian company that has not received a VAT invoice from the foreign company is not required to account for or remit VAT to the FIRS.

This decision provides some clarity on the often disputed position of the FIRS that a Nigerian company should self-charge VAT on services received from a foreign entity even when such provider is not carrying on business in Nigeria.

In detail

Background

Section 10 of the VAT Act provides that a foreign company carrying on business in Nigeria shall register with the FIRS using the address of its Nigerian counter-party.

The section further provides that such foreign companies should include the relevant VAT on its invoice which the Nigerian counter-party must deduct and remit to the FIRS in the currency of transaction.

In effect, when a foreign company provides a service to a Nigerian company while carrying on business in Nigeria, the foreign company is required to register for, and charge, Nigerian VAT on any invoice issued to the Nigerian company. The above conditions must be applicable for a Nigerian company to then withhold the VAT and remit to the FIRS.

The FIRS Practice

The FIRS has always taken the view that when a foreign company enters into a contract with a Nigerian company, it becomes compulsory for the foreign company to register for, and charge Nigerian VAT.

If the foreign company did not register or charge Nigerian VAT, the FIRS takes the view that the Nigerian entity is under the obligation to self-charge the VAT and remit it to the FIRS. This is generally referred to as "reverse charge mechanism".

Facts of the case

In Gazprom Oil & Gas Nig Ltd v. FIRS, the Appellant received consultancy and logistic services from foreign companies. These services were performed outside Nigeria and the foreign companies never sent any employee or equipment to Nigeria.

Relying on section 10 of the VAT Act and the reverse charge mechanism contained in FIRS Circular, the FIRS issued two VAT re-assessment notices on the Appellant.

The Appellant appealed to the TAT after the FIRS refused to amend the notices despite the

objections submitted by the Appellant.

In refusing to amend the notices, the FIRS contended that even though the foreign companies did not send any employee to Nigeria, the Appellant enjoyed the benefit of the services in Nigeria.

The FIRS argued that based on the destination principle, the services were provided where they were enjoyed. Since they were enjoyed in Nigeria, it was the view of the FIRS that the foreign companies were carrying on business in Nigeria and therefore should register and charge Nigerian VAT; and even if they did not, the Appellant was required to charge and remit the tax to FIRS.

Destination Principle vs. Origin Principle

In more developed economies, VAT is usually applied based on either of the Destination or Origin Principles. Under the Destination Principle, VAT is imposed by the country where the goods or services are consumed or enjoyed while under the Origin Principle, VAT is imposed by the country where the transaction originated.

Appellant's position

The Appellant argued that:

- the Act does not articulate or impose VAT based on the destination principle,
- a supplier with no physical presence in Nigeria cannot be said to be carrying on business in Nigeria,
- the foreign companies were not carrying on business in Nigeria and therefore not liable to register for or charge VAT in Nigeria,
- the Appellant had no obligation to account for or remit any tax since it did not receive any VAT invoice from the foreign company.

FIRS' position

FIRS' arguments can be summed up as follows:

- The use of the phrase 'supplied in Nigeria' in S.10 imposes VAT based on the destination principle,
- 'carrying on business' in S.10 does not require a place of physical residence,
- the existence of a contract with a long duration implied the foreign companies were carrying on business in Nigeria,
- tax statutes should be interpreted liberally in favour of the FIRS,
- the obligation imposed on Nigerian companies to remit VAT is not dependent on receipt of a VAT invoice, and
- since the recipient of the services was a Nigerian company, the transactions ought to be subject to VAT.

The decision

The decision revolved around the interpretation of S.10 of the Act. In arriving at its decision, the Tribunal raised three questions for determination.

- Whether the provisions of the VAT Act impose tax on the basis of the Destination Principle?
- Whether carrying on business in Nigeria imposes a duty to register and charge VAT by a Non-Resident Company?
- Whether receipt of VAT invoice is a pre-condition for the remittance of VAT charged by a Non-Resident Company?

In resolving question 1, the Tribunal interpreted S.10 of the Act to mean that:

i. the foreign company must be carrying on business in Nigeria,

ii. the foreign company must register with the FIRS,

iii. to carry on business in Nigeria a foreign company must have a subsisting contract with a party in Nigeria,

iv. for the purpose of correspondence, the address of the Nigerian counter-party would be the foreign company's address,

v. the foreign company then has to issue a VAT invoice to Nigerian counter-party,

vi. the Nigerian counter-party remits the VAT in the currency of the transaction.

The Tribunal held that before VAT will be payable on the transactions by the Appellant, all the conditions listed above must be present.

The Tribunal also held that carrying on business in Nigeria means 'conducting, prosecuting or to continue a particular vocation or business as a continuous operation or occupation' within Nigeria.

However, since there was uncontroverted evidence that the foreign companies did not carry out any activity in Nigeria, the Tribunal took the view that they were not carrying on business in Nigeria and there was no requirement to register for or charge VAT.

On question 2, the Tribunal held that once a company carries on business in Nigeria then it had a duty to register with the FIRS and charge VAT on its invoice.

On question 3, the Tribunal held that a recipient of a service from a foreign company has a duty to remit VAT only when it has been issued a VAT invoice. In the instant appeal since the Appellant was not issued a VAT invoice it was not required to account for or pay VAT to the FIRS.

The Tribunal discharged the re-assessment notices and granted all the reliefs sought by the Appellant.

The takeaway

This decision puts to rest the question of whether under the VAT legislation, a Nigerian company receiving services from a foreign company outside Nigeria is required to account for or pay any VAT to the FIRS on the fees payable for the services received.

The broader implication of this decision is that it emphasises the age-long principle of interpretation of tax laws. Where the tax law is clear it must always be interpreted literarily and if ambiguous, and imposes a burden, then it should be interpreted strictly against the tax authority.

The fact that the FIRS seem convinced about a particular interpretation of the law and has applied the interpretation to a large number of taxpayers in the past does not mean the interpretation is correct.

Taxpayers must, when convinced about an interpretation, be willing to challenge the FIRS to establish a precedent and provide clarity in the application of the tax legislation.

The impact of this decision on the VAT collections may prompt the FIRS to restart the process of amending the VAT Act to align the law with the best practice of applying VAT on cross border services based on the destination principle. The process had been started and stalled in the past.

Finally, while it is not clear whether the FIRS will appeal this decision to the Federal High Court, the precedent set by the TAT will remain the position of the law in similar situations until it is overturned by a superior court.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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