IN THE TAX APPEAL TRIBUNAL
IN THE LAGOS ZONE
HOLDEN AT IKEJA

Consolidated Appeals
TAT/LZ/015/2014 & TAT/LZ/016/2014

Between
Nigeria Agip Oil Company Limited Appellant
And
Federal Inland Revenue Service Respondent

Judgment

Issue for Determination

In determining this appeal, the Tribunal has to address the following question:

> *Under the Petroleum Profits Tax Act (PPTA), can a corporate taxpayer deduct interests it incurred on loans obtained at arm's length from a sister company?*

Introduction

The Appellant Agip obtained loans from Eni Coordination Centre S. A. (Eni) from 2001 to 2011.Agip and Eni belong to the same group of companies. In its Petroleum Profits Tax (PPT) returns from 2006 to 2011, Agip deducted interests on the loans. But when FIRS conducted an audit in 2013, it disallowed the interest deductions. FIRS then issued 2 Notices of Additional Assessment covering 2006 to 2011: one for PPT, and the other for Education Tax.Agip was dissatisfied with FIRS's assessments. It requested FIRS to amend them but FIRS refused. Agip filed the 2 appeals now consolidated.

FIRS argued that it disallowed the tax deductions on the strength of section 13(2) of PPTA. On its face, that provision disallows tax deductions in respect of sums incurred by way of interest where the taxpayer borrows money from a related company.In PPTA's enactment-and-amendments history, section 13(2) was enacted before section 10(1)(g). Agip pointed to section 10(1)(g), which renders interests on inter-company loans tax-deductible if the loan was made under open-market terms.

Facts and Procedural History

Agip obtained loans from Eni. Both companies are part of the same group of companies. When filing its Petroleum Profits Tax Returns from the year 2006 to 2011

(Exhibits OA1/03 to OA1/08), Agip treated the interests on the loans as tax deductible.

In 2013, FIRS conducted an audit of Agip's records. FIRS then assessed Agip to additional petroleum profits tax,as well as education tax, for the years 2006 to 2011. For PPT, FIRS assessed Agip at the rate of 85%; for Education Tax, FIRS assessed Agip at 2%. For both, FIRS disallowed tax deductions. At the chargeable profit of US$22,185,677.45, PPT came to US$18,857,826, and Education Tax US$443,714.

Agip objected to the Notice of Additional Assessment. It argued that section 10(1)(g) of PPTA makes interest on all intercompany loans tax deductible. FIRS rejected Agip's request for amendment, insisting that Agip was not entitled to make any tax deduction.

Agip appealed. FIRS replied. Agip called one witness– Mr Oluwole Samuel Agbede. It also introduced documentary evidence. FIRS neither called any witness nor introduced any evidence, content to rely on issues of law.

Parties' Positions

Agip argues that it is entitled to make tax deductions in its annual returns from 2006 to 2011. It maintained that the loans from Eni,a related company, were obtained on arm's-length terms. According to Agip, the loans were utilized wholly, exclusively, and necessarily for its petroleum operations. It thus submits that the sums incurred by the Appellant as interest on the loans are allowable deductions. Agip has relied on section 10(1)(g) of the Petroleum Profits Tax Act (PPTA) to support its position. The section allows interests on inter-company loans to be deducted.

FIRS contends that based on section 13(2) of the Petroleum Profits Tax Act (PPTA), Agip is not entitled to deduct any sums incurred by way of interest on the obtained loans. FIRS argues that section 13(2) of PPTA operates as an exception to the tax-deductibility provisions of section 10(1)(g).

Analysis

Section 8 of PPTA imposes tax on the profits of each accounting period of any company engaged in petroleum operations. Section 10(1) of the Act provides for certain deductions in the computation of the adjusted profit of such companies. The section lists the nature of outgoings and expenses that qualify for such tax deductions. These outgoings and expenses must be "wholly, exclusively and necessarily

incurred" by the company involved in petroleum operations. For this purpose, the outgoings and expenses that are tax deductible are listed in paragraphs (a) to (m) of section 10(1) of the Act. Section 10(1)(g), on which Agip relies, falls within this ambit. Agip deducted sums incurred by way of interest on inter-company loans obtained under terms prevailing in the open market.

Section 10(1)(g) provides:

> *(1) In computing the adjusted profit of any company of any accounting period from its petroleum operations, there shall be deducted all outgoings and expenses wholly, exclusively and necessarily incurred, whether within or without Nigeria, during that period by such company for the purpose of those operations, including but without otherwise expanding or limiting the generality of the foregoing-*
>
> *(g) All sums incurred by way of interest on any inter-company loans obtained under terms prevailing in the open market, that is the London Inter-Bank Offer Rate, by companies that engage in crude oil production operations in the Nigerian oil industry;*

The above provision would entitle Agip to make deductions since the sums were incurred by way of interest on the loans.

To properly resolve this matter, we must turn to legislative history. We note that the extant Petroleum Profits Tax Act (LFN) 2004 was first enacted as the Petroleum Profit Tax Ordinance No. 15 of 1959. The Petroleum Profits Tax Ordinance was then amended by the Petroleum Profits Tax (Amendment) Decree No.1 of 1967. The 1967 amendment added a new paragraph 10(1)(aa) to the pre-existing section 10(1)(a) and (b). To have a neater legislation, section 10(1)(aa) was replaced in the compilation of the LFN 1990 by section 10(b). The original section 10(b) thus became section 10(1)(c). In 1996 and 1999, new paragraphs were added to section 10(1) of the Act. Section 10 was again amended by Decree 30 of 1999. This amendment introduced section 10(1)(cc), the present section 10(1)(g) of the Act. The new subsection provides that:

> *(cc) all sums incurred by way of interest on any inter-company loans obtained under terms prevailing in the open market, that is*

the London Inter-Bank Offer Rate, by companies that engage in crude oil production operations in the Nigerian oil industry;

Except for the replacement of section 10(1)(b) with subsection (1)(d), section 11(2) of the Act [now section 13(2)] has remained unchanged. This is why section 13(2) of the Act refers to the provisions of section 10(1)(d); but in substance, relates to section 10(1)(g) of the Act. Section 10(1)(d) is clearly on royalties incurred by a company, not 'sums incurred by way of interest…upon any borrowed money… from a second company...' {10(1)(g)}.

By section 10(1)(f) of the Act, the legislative intention is to allow companies deduct tax for sums incurred by way of interest on *any* loan they obtain for their petroleum operations. Section 10(1)(g) of the Act then specifically entitles related companies to the same deductions as provided in section 10(1)(f), but with one important requirement: they must be transacting at arm's length; in the words of the provision, *under terms prevailing in the open market.*

But why has the Legislature subsequently introduced section 10(1)(g), a similar provision to section 10(1)(f)?

Section 10(1)(f) has been part of the Petroleum Profits Tax Act in LFN 1990 [then section 10(1)(c)]. The section allows tax to be deducted upon interest on intercompany loans. Decree 30 of 1999 amended the Act. It did not remove or amend section 10(1)(f). Thus, we must construe this to mean that the legislature intends that section 10(1)(f) and section 10(1)(g) should operate differently.

Section 10(1)(f) of the Act allows tax to be deducted from sums incurred by way of interest upon *any* loan to a company. The interest on such loan was payable on the capital employed in carrying out its petroleum operations. In section 10(1)(g), it is the same transaction but this time it specifically relates to "inter-company loans" obtained at arm's length. Since Agip and Eni are members of the same group of companies, it is under this latter section that the transaction between both companies falls. And contrary to FIRS's argument, section 10(1)(g) does not apply to interests paid on loans between two unrelated companies. Section 10(1)(f) already takes care of that.

This approach is buttressed by the dictum of Tobi JCA (as he then was) in Onagoruwa v. The State (1993) 7 NWLR (Pt. 303) 49 at 102: "It is legitimate to look back at the history of the process which brought the constitution or a particular

provision or section into being. A court of law is not to be oblivious of the history behind the law or section interpreted."

Conclusion

Section 13(2) disallows any tax deductions on sums incurred by a company through any inter-company loan transaction. This appears to contradict the provisions of section 10(1)(g) that allows tax deductions on interests on loans between related companies when they deal at arm's length.

But we must construe the legislative intention behind the introduction of section 10(1)(g) to the Act. Section 10(1)(g) was introduced as a later amendment. The provisions of section 13(2) have always been part of the Act as section 11(2). The legislature intends that for tax purposes, related companies should, from the enactment of section 10(1)(g) begin to enjoy the tax deduction always allowed non-related companies when they transact as though unrelated.

These provisions are not necessarily inconsistent with each other. It is the law that "Seemingly conflicting parts are to be harmonised if possible so that effect can be given to all parts of the constitution" Pa Ogundare JSC of blessed memory in Ishola v. Ajiboye (1994) 6 NWLR (Pt. 352) 506 at 558 – 559. This pronouncement applies with equal to statutory provisions. A community reading of these two provisions state that interest on inter-company loans are not deductible in computing adjusted profit, except as per S. 10(1)(g) where such loans are obtained under terms prevailing in the open market. Thus whether deductions are deductible or not, on interest on inter-company loans, depends on that specific arms-length litmus test.

We allow the consolidated appeals and give judgment for Agip. We set aside FIRS's Petroleum Profits Tax and Education Tax Notice of Assessment (Exhibit OA1/02) PPTBA 91 and PPTBA/ED 83 for 2006, 2007, 2008, 2009, 2010, and 2011 years of assessments. We order FIRS to issue fresh assessment notices which allow deductions of interest on inter-company loans when such transactions are on arms-length terms. In the alternative, FIRS may accept payment in terms of the returns. Such payment will fully discharge Agip of its liabilities for the years assessed.

Legal Representation:-

C. Ikwuazom Esq. with S. Mustafa Esq. H. Abdukareem Esq. And Mrs O. Ogunrinde for the Appellant.

Ms A. Sodipo for the Respondent.

Dated at Ikeja, Lagos this 18th day of September 2014

Kayode Sofola, SAN
Chairman

Catherine A. Ajayi (Mrs)
Commissioner

D. H. Gapsiso Esq.
Commissioner

Mustafa Bulu Ibrahim
Commissioner

Chinua Asuzu Esq.
Commissioner