27 June 2019

Global Tax Alert

Nigeria's TAT rules on deductibility of voluntary pension contributions and use of Best of Judgment Assessments by tax authorities

NEW! EY Tax News Update: Global Edition

EY's new Tax News Update: Global Edition is a free, personalized email subscription service that allows you to receive EY Global Tax Alerts, newsletters, events, and thought leadership published across all areas of tax. Access more information about the tool and registration here.

Also available is our EY Global Tax Alert Library on ey.com.

Executive summary

Nigeria's Tax Appeal Tribunal (TAT or the Tribunal) sitting in Lagos delivered a judgment in the case of *Nexen Petroleum Nigerian Limited (NPNL) and Lagos State Internal Revenue Service* (LIRS) to the effect that employers have no further obligation to account for subsequent dealings by employees with voluntary pension contributions (VPC), after the employers remit the VPC to the Pension Fund Custodians, specified by the Pension Fund Administrator (PFA).

The TAT, on 18 June 2019, in delivering its judgment, noted the following, among others:

a. NPNL's legal obligation was to deduct and remit the pay-as-you-earn (PAYE) tax of its employees, after deducting all the statutory reliefs in compliance with the relevant provisions, which NPNL has done in this case.

b. That as the statutory agent of the LIRS, NPNL has fulfilled the obligations imposed on them by the relevant laws. Therefore, the responsibility to recover any further tax on the income of the employees that is not in the custody or control of NPNL automatically reverts to the LIRS.

c. The LIRS' refusal to accept NPNL's computed expatriates PAYE tax on actual gross emoluments for the 2014 year of assessment (YOA) and resort to the use of its discretionary powers of Best of Judgment (BOJ) assessment is clearly against the principles of justice, equity and good conscience.

Building a better working world

Based on its ruling, the notices of assessment issued by the LIRS against NPNL, which were the subject of the dispute, were discharged by the TAT.

Detailed discussion

In this case, NPNL, appealed against the Notices of Refusal to Amend (NORA) for the 2013 YOA and 2014 YOA issued to them by the LIRS following a tax audit in respect of its 2013 and 2014 tax records, after which it was subjected to additional tax liabilities.

NPNL in two separate letters dated 21 March 2018 and 18 September 2018 objected to these assessment notices and subsequently filed its notice of appeal before the TAT. Both parties in arguing their positions raised the following issues for determination on whether:

1. The NPNL has fulfilled its statutory obligation of deducting and remitting the correct PAYE for the 2013 YOA and 2014 YOA, hence exculpating itself from any additional tax obligation arising from the voluntary pension contributions made by its employees.
2. An agency relationship exists between the parties, thus making NPNL merely an agent of the LIRS for the PAYE scheme and not a taxpayer for purposes of any future actions of its employees with their earned income or statutory deductions.
3. VPC qualify as tax deductible contributions and remain so in relation to the NPNL as an agent of the LIRS.
4. The LIRS acted judicially and judiciously by rejecting NPNL's computed PAYE on actual gross emoluments for its expatriates without any basis and failure to consider documents submitted before making its BOJ assessment.
5. Under Section 10(4) of the *Pension Reform Act* (PRA), for a VPC made on behalf of employees to be treated as tax exempt, it must be shown that the voluntary contribution was not withdrawn by the employee affected for a period not less than five years.

NPNL in its argument relied on the provisions of Section 81(1) of the *Personal Income Tax Act* and Regulations 2 and 4 of the PAYE Regulations 2002 contending that once it has deducted and remitted the PAYE of its employees, it has fully discharged its statutory obligations to the LIRS. It further contended that the right to use BOJ for the assessment of its expatriates should be based on a discretion that must be exercised judicially. NPNL argued that due consideration should have been given to the representations and justifications made by the company to substantiate the decline in the actual emoluments of the expatriates presented to the LIRS.

The LIRS argued that every employer of labor is under the obligation to deduct and remit taxes due from its employees to the tax authority. It further argued that for NPNL to claim that a portion of the emoluments is tax exempt, the company is expected to provide the evidence for such treatment. It relied on Section 10(4) of the PRA which stipulates that any VPC is subject to tax at the point of withdrawal where the withdrawal is made before the end of five years from the date the VPC was made. It stated that it is not the duty of the various PFAs to deduct and remit tax where withdrawals are made from the RSA before five years and since the VPCs form part of the emolument of the employees, the employer should continue to maintain the obligation to deduct and remit taxes on amount contributed and withdrawn before five years.

The judgment

After considering the arguments of both parties, the Tribunal ruled in favor of the NPNL as follows:

- In compliance with the provisions of Section 11(3) of the PRA, 2014, which asserts that any relief to be granted by the authority must be done based on available and verifiable documentary evidence, NPNL had fulfilled its statutory obligations by providing to the LIRS, its pension schedules detailing the contributions made by the employees, along with copies of corresponding bank tellers evidencing deductions and remittances of the employee's VPC through the appointed custodian and it had no further obligation in this regard.
- NPNL, by virtue of the PAYE Scheme which places the burden of deduction and remittance of the personal income taxes on employers, is an appointed agent of the LIRS. NPNL's legal obligation was to deduct and remit PAYE of its employees after deducting all statutory reliefs and by doing this, it had discharged its responsibility as an agent.
- The LIRS cannot not assess NPNL to any liability for under-remitting PAYE because of tax deductions attributed to the VPC taken by its employees. The responsibility to recover any further tax on the income of the employees that is not in custody or control of the NPNL falls automatically on the LIRS. The TAT noted that VPC is statutorily recognized under the PRA and is not a fictitious scheme invented by employees.

- The provisions of the statutes cited do not mandate an employer to be part of the transactions between the employee and the PFA. The law does not require NPNL to ensure that the provisions of Section 10(4) of the PRA are adhered to. The employer has no right over or access to an employee's Retirement Savings Account based on the statutory obligation of confidentiality maintained on all parties engaged by the PFA or Custodian. Accordingly, NPNL could not have had access to the dealings and transactions of its employees' accounts or that of the PFA or Custodian to insist that the employee complies with the provision of the PRA for not making withdrawals until the expiration of the mandatory gestation period.
- The LIRS' refusal to accept NPNL's computed expatriate PAYE tax on actual gross emoluments for the 2014 YOA and its use of the BOJ basis of assessment was against the principles of justice, equity and good conscience. BOJ assessments should only be resorted to where the taxpayer fails to file grounds or returns or files inadequate returns. The TAT noted that the right to use a BOJ assessment is based on discretion and the TAT concluded that the LIRS by its refusal to accept the documents submitted by NPNL and its use of BOJ assessment, had not exercised its discretionary powers properly.

Implications

With this judgment, it appears that the employers will no longer be held to account for the tax due where employees withdraw their VPC before the expiration of the five years which was prescribed by the PRA. Furthermore, the LIRS may not be able to enforce the recovery of any tax due from the employer for such withdrawals which is the position announced in its public notice issued in the year 2017 where the LIRS emphasized the recovery of any tax due from employers in this regard.

The Tribunal in giving its judgment acknowledged the fact that withdrawal of VPCs before the expiration of five years is a gross violation of the provisions of the PRA and as such, taxes should be recovered for such withdrawals. As the TAT has absolved the employer from any responsibility for the recovery of taxes applicable to such withdrawals, this indicates that the responsibility now falls on the employees who withdraw VPC within five years of making the contribution. It remains to be seen the option the tax authorities may adopt to recover the applicable taxes from individual employees.

Furthermore, the TAT's ruling against the use of discretionary powers to assess expatriates to tax on a BOJ basis of assessment has hopefully put to rest the controversy on the use of deemed income basis of assessment in instances where the employer has provided actual income and supporting documentation. In this regard, the ruling provides a basis for employers with expatriates on their payroll to file income tax returns for such employees based on actual income supported by relevant documentation.

For additional information with respect to this Alert, please contact the following:

Ernst & Young Nigeria, Lagos

- Akinbiyi Abudu akinbiyi.abudu@ng.ey.com
- Temitope Samagbeyi temitope.samagbeyi@ng.ey.com
- Chinyere Ike chinyere.ike@ng.ey.com
- Zion Athora zion.athora@ng.ey.com
- Oluwatumininu Familusi oluwatumininu.familusi@ng.ey.com
- Adefemi Olaore adefemi.olaore@ng.ey.com

Ernst & Young Advisory Services (Pty) Ltd., Africa ITS Leader, Johannesburg

- Marius Leivestad marius.leivestad@za.ey.com

Ernst & Young LLP (United Kingdom), Pan African Tax Desk, London

- Rendani Neluvhalani rendani.mabel.neluvhalani@uk.ey.com
- Byron Thomas bthomas4@uk.ey.com

Ernst & Young LLP (United States), Pan African Tax Desk, New York

- Brigitte Keirby-Smith brigitte.f.keirby-smith1@ey.com
- Dele A. Olaogun dele.olaogun@ey.com

EY | Assurance | Tax | Transactions | Advisory

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

EYG no. 003096-19Gbl

1508-1600216 NY
ED None

ey.com