THE EXCESS DIVIDEND TAX CONUNDRUM

Background

In 2013, Actis Africa (Nigeria) Limited ("the Appellant") made profits and retained some of its earnings (after tax had been paid on the profits made). In contrast, no profits were made in the subsequent year, that is, 2014, as a result, no income tax was paid by the Appellant. In spite of this, the Board of Directors of the Appellant recommended that interim dividends of N49,095,020 (Forty-Nine Million, Ninety-Five Thousand and Twenty Naira) be declared to the shareholders of the company payable from the retained earnings of the company for the previous financial year.

The Federal Inland Revenue Service ("the Respondent") however reviewed the Appellant's Income Tax computation for 2015 year of assessment, and asserted that the Appellant did not consider the dividends paid in its tax returns and consequently assessed it to additional tax in the sum of N14,728,506 (Fourteen Million, Seven Hundred and Twenty Eight Thousand, Five Hundred and Six Naira).

The Appellant then filed a Notice of Appeal against the Respondent at the Tax Appeal Tribunal ("the Tribunal") on the grounds that the Respondent erred in law when it assessed the Appellant to tax on profits on which tax had been previously paid and that the Respondent applied the literal rule of interpretation in construing the provisions of Section 19 of the Companies Income Tax Act (CITA).

Judgment

A sole issue for determination was formulated by the Tribunal to be: whether the Appellant's action in declaring and distributing part of its post-tax profit of 2013 financial year as dividends in 2014, when it recorded or made no profit, breached and/or contravened the provisions of Section 19 of CITA, to warrant the issuance of the notice of assessment by the Respondent.

The Tribunal stated that the interpretation of Section 19 of CITA which was the crux of the case had been determined by both the Federal High Court and Court of Appeal in the Oando cases, and thus would decide the instant case within the confines of the earlier decisions in strict compliance with the principle of *stare decisis.*

In Oando v. FIRS, the Federal High Court had decided that Section 19 of CITA considers essentially two things – the year of assessment in which the dividend was paid and the total profits for the year. The effect of this is that the dividend is considered from the year it was paid out and not from the year the profit out of which it was paid originated. Therefore, where a company does not record total/taxable profit for the year, the dividend becomes the company's total/taxable profit which is subject to income tax at 30%, as deemed taxable profit. The Tribunal confirmed that the Respondent observed the conditions precedent before applying Section 19 of CITA to the dividends paid by the Appellant.

It further held that since the instant case was on all fours with the Oando case, a distinction was not required and thus aligned itself with the earlier judgment. Accordingly, the Appeal failed, and the Appellant was ordered to pay the tax which it was assessed to by the Respondent in the sum of N14,728,506 (Fourteen Million, Seven Hundred and Twenty-Eight Thousand, Five Hundred and Six Naira).

Our Comments

Undoubtedly, the dispute in the instant case arose as a result of the interpretation of Section 19 of CITA. The section states that:

"Where a dividend is paid out as profit on which no tax is payable due to –

(a) no total profits; or

(b) total profits which are less than the amount of dividend,

which is paid, whether or not the recipient of the dividend is a Nigerian company,
is paid by a Nigerian company, the company paying the dividend shall be charged to tax at the rate prescribed in subsection (1) of section 40 of this Act as if the dividend is the ***total profits of the company for the year of assessment to which the accounts, out of which the dividend is declared, relates."***

By virtue of the above-quoted section, two alternative conditions must be fulfilled before the section can be applied. The company in question must either have no total profits or it paid out dividends which exceed the total profits made in a particular financial year.
The applicable section, that is, Section 19, points out clearly that the dividend relates to the year of assessment of the account out of which the dividend is paid out. It is therefore a misconception that the law does not concern itself with the origin of profits.

In the instant case, even though the Appellant made no profits in 2014, it is an error to conclude that the dividend declared and paid out to its shareholders in the same year, constitutes deemed taxable income on which tax is payable. Where dividend is paid out of retained earnings on which income tax has been paid based on the profit of the accounting period from which the retained earnings arose, the provisions of Section 19 will only apply by tracing the retained earnings to the year it arose. This will involve reopening the tax computation of the relevant year of assessment, in order to ascertain whether section 19 should apply to the dividend being paid.

However, the higher courts have ruled contrary to this position. Rather, dividends have been considered a profit of the year in which it is declared and not where it originated from.

In respect of the appropriate rule to be applied while interpreting statutes, the Supreme Court held in Our Line Limited v. SCC Nigeria Limited (2009) 17 NWLR (pt. 1170), that where the wordings of a statute are clear and unambiguous, it must be given its clear and literal meaning.

...Section 19, points out clearly that the dividend relates to the year of assessment of the account out of which the dividend is paid out...

Particular reference was made in Halliburton West Africa Limited v. Federal Board of Inland Revenue (2013) 10 N.R.L.R. 2, where the court held that where a taxation statute is involved, the first point of call should be the application of the literal rule of interpretation.

However, in Mobil Oil Nigeria Limited v. Federal Board of Inland Revenue (1977) 1 NCLR 1, the court held that even though the literal rule should first be considered, the courts are charged with the duty of promoting the purpose of and curing the mischief in a legislation where the literal rule is stringent and unreasonable. The same position was held in Shell Petroleum Development Company Limited v. Federal Board of Inland Revenue (1996) 8 NWLR (pt 466) 256, where the court applied equitable considerations in interpreting a tax statute.

An amendment of the law and a more assertive judicial approach may be helpful in determining the purport of Section 19 of CITA and its application.

It is expected that the Appellant would appeal the decision of the Tribunal, and although we do not envisage a dissenting judgment at the Federal High Court, due to precedents of higher courts in this regard, we look forward to finding out the decision in the appeal.

Albert Folorunsho
afolorunsho@pedabo.com

Killian Khanoba
kkhanoba@pedabo.com

Fidelis Chukwu
fchukwu@pedabo.com

Oluwasanmi Ogunsanwo
sogunsanwo@pedabo.com

Lagos Office:
67, Norman Williams Street
South West, Ikoyi
Lagos, Nigeria
Tel: 01-2919041
0808 820 8747
info@pedabo.com
www.pedabo.com

Abuja Office:
4th Floor, Grand Square
Mohammed Buhari Road
Central Business District,
Abuja
Tel: 09-8707692

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