# ENHANCING REVENUE GENERATION THROUGH INDIRECT TAXATION

Presented by

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6. Revised National Tax Policy
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# OBJECTIVES OF SESSION

At the end of this course, participants should be able to:

1. Know the need for increase revenue generation
2. Differentiate between Direct Tax and Indirect Tax
3. Access the reason for shifting to Indirect Tax
4. State the types of Indirect Tax

# 1. CONCEPT OF DIRECT AND INDIRECT TAX

**INTRODUCTION**

Taxation is the means by which the government of a nation generate revenue to finance their expenditure through the imposition of compulsory charges on citizens and corporate entities. The trend for governments to raise more revenues through indirect taxes and direct taxes seems set to continue. However, the International Monetary Fund (IMF), the Organisation of Economic Cooperation and Development (OECD) and the European Commission are all promoting the shift from direct to indirect taxes to help solve the crisis globally, by reducing costs on business and make them more competitive.

In the opening address of the OECD's first Global Forum on Indirect tax, Pascal Saint-Amans (head of the OECD's Centre for Tax Policy and Administration) noted that *"VAT in the OECD countries now accounts for around 20% of total tax revenue, a 70% greater share than in the mid-eighties. With excise duties at 11% and other taxes contributing smaller sums, revenues from taxes on goods and services are now very close to revenues raised from personal income tax (25%), corporate income tax (8%) and other direct taxes such as those on capital gains".*

# 1. CONCEPT OF DIRECT AND INDIRECT TAX CONT'D

Some tax stakeholders are of the thoughts that Direct taxes are regarded to be superior to indirect taxes in effecting a more equitable distribution of income and wealth. But this is not always true. Even indirect taxes can be made progressive by levying them on Luxuries and exempting them on necessaries!. Both direct and indirect taxes are alternative methods of achieving any particular redistribution of income.

The purpose of this presentation is to define methodologies required to enhance the generation of revenue through Indirect taxes but firstly we need to understand the difference between Direct and Indirect tax to pave the way for this subject.

# 1. CONCEPT OF DIRECT AND INDIRECT TAX (Cont'd)

## 1.1. Direct Tax

**Direct tax** are taxes that governments impose directly on individuals and businesses. The payment of direct tax goes straight to agencies such as the Federal Inland Revenue Service or State Internal Revenue Service. One of the major features of Direct taxes is that it cannot be shifted to another entity.

Examples of Direct Taxes are Personal Income Tax, Capital Gain Tax, Property Tax, Companies Income Tax and Tertiary Education Tax.

# 1. CONCEPT OF DIRECT AND INDIRECT TAX (Cont'd)


## 1.2. Indirect Tax

**Indirect Tax** are levied directly on a person who consumes the goods and services and indirectly paid to the government in such a way that the burden of tax can be easily shifted to another person. The tax is progressive in nature. It is levied on every person equally whether rich or poor. The administration of tax is done either by the Federal Government or State Government.

Examples of Indirect Taxes are Value Added Tax, Stamp Duties, Custom Duties (taxes on imported and exported goods), and Excise Duties (taxes on locally manufactured goods). It is pertinent to state that VAT happens to be the principal Indirect tax in Nigeria and globally.

# 1. CONCEPT OF DIRECT AND INDIRECT TAX (Cont'd)

## IN SUMMARY

### Difference between direct and indirect taxes

| Point of difference | DIRECT TAX | INDIRECT TAX |
|---|---|---|
| Incidence & Impact | A tax is said to be direct 'when impact and incidence of a tax are on one and same person. | If impact of tax is on one person and incidence on the another, the tax is called 'indirect' |
| Burden | Direct tax is imposed on the individual organisation and burden of tax cannot be shifted to others. | Indirect tax is imposed on commodities and allows the tax burden to shift. |
| Viability of payment | Direct taxes are lesser burden then indirect taxes to people as direct taxes are based income earning ability of people. | Indirect taxes are borne by the consumers of commodities and services irrespective of financial ability as the MRP includes all taxes. |
| Administrative viability | The administrative cost of collecting direct taxes is more and improper administration may result in tax evasion. | Cost of collecting indirect are taxes is very less as indirect taxes are wrapped up in prices of goods and services and cannot be evaded |

# 2. REASONS FOR SHIFTING TO INDIRECT TAXES

**SHIFTING TO INDIRECT TAX**

- Precision of Indirect Tax
- Administratively, the Cost of Collection is low compared to Indirect Tax
- Digital age: It is one of the most efficient ways of capturing transactions to tax in the digital age.
- Tax Evasion: It is not easy to evade Indirect Tax
- Redistribution of Wealth: It is not easy to evade Indirect Tax since it is transferable to the final consumer

# 3. CONTRIBUTIONS OF INDIRECT TAXES TO THE ECONOMY

The National Bureau of Statistics on Wednesday 21 February 2018 released the sectoral report for Value Added Tax for the 2017 fiscal period, stating that the country generated a total of N972.34bn from VAT (an Indirect tax). Highlighted below are some of the fundamental contributions of Indirect taxes to the economy are as follows:

1. Revenue Generation
2. Redistribution of Income
3. Check against harmful Products

# 4. CHALLENGES OF INDIRECT TAX

Listed below are some of the challenges of Indirect Tax

1. **Public Trust and Confidence in government Institutions:** This is one of the major challenges in generating revenue generally, including Indirect tax. There are certain school of thoughts who are of the view that to encourage voluntary compliance to Indirect tax, government needs to build public trust by investing in public goods and infrastructures for economic growth.

2. **Multiplicity of Taxes:** The efforts to make Indirect taxes more progressive or less regressive result in increasing number of exemptions, multiplicity of rates of taxes in-turn harm the basic simple structure of the tax, making it complex leading to corruption, harassment of the assesses and evasion of taxes.

3. **Increase in Cost to the Ultimate Consumer:** An indirect tax levied at different stages of production and sale results in cascading. This increases the cost of the ultimate product and leads to general price rise in the economy. Cascading encourages vertical integration of the production process

4. **Regulatory Framework:** Indirect taxes in Nigeria such as custom duties and Import duties employ Ad valorem rates (HS Codes). For instances Custom Duties which are taxs payable on goods imported and exported from Nigeria (governed by Consolidation Decree No. 4 of 1999 governs the administration of custome and excise duties in Nigeria. Custom valuations is used to determine the value of goods when they are being entered into various customs procedures e.g Import, export, warehousing and processing into various customs control

# 4. CHALLENGES OF INDIRECT TAX (Cont'd)

5. **Problem of extended litigation in the Nigeria tax system:** This results in delay in recovery of the duty and considerable expenditure on both sides- the "assessee" and the Government. The reason for the set up of the Tax Appeal Tribunal to adjudicate on tax appeals and reduce the burden of superior courts but the effectiveness of the final decision of the TAT relating to Tax matters has most times been appealed.

6. **Transparency:** This is essential in the Nigeria Tax system for administration of Indirect tax to work. Tax payers are entitled to expect a high degree of certainty and predictability in their dealings with laws, regulations. procedures and administrative guidelines and should be made public, be easily accessible and applied in uniform and consistent manner. The basis upon which discretionary powers can be exercised should be clearly defined

7. **Automation:** The government needs to create more awareness in automating its function which will in turn improve efficiency and effectiveness and remove any opportunities for corruption. Inability to automate these processes has increased the level of non-accountability and provided a gap in audit trail for later monitoring and review of administrative decisions.

8. **Recruitment and advancement Process:** No one exist in a vaccum, people are the ones to administer Indirect taxes . Thus, if there are no objectivity in recruitment process and advancement, there is likely to be existence of people that will maintain low standard of professional ethics.

# 5. ABUSE OF INDIRECT TAX THROUGH MULTIPLICITY OF TAXES

*"Multiplicity of taxation began to rear its ugly head in Nigeria in the late 1980's when revenue accruing to states and local government from the Federal Account began to dwindle…"* F. Izendomi, "Eliminating Multiple Taxation in the Capital Market – The Capital Market Perspective". And till date, there are still superfluous introduction of taxes and levies across the States in Nigeria in the quest to boost revenue. Some States Government are introducing new rates and reviewing the rates and fees of an existing fees in the tax laws, ostensibly to reflect the economic realities. In some cases, the rates and fees were skewed too high. The States therefore did not take any serious action to address the concerns of taxpayers.

As part of the responses to curb the menace of multiplicity of taxes, the JTB drew a list of taxes collectible by each tier of government. The list was largely ignored by States who were in dire need of boosting their revenue. The list was eventually given a legal backing vide the Taxes and Levies Approved List for Collection Act.

# 5. ABUSE OF INDIRECT TAX THROUGH MULTIPLICITY OF TAXES (Cont'd)

- Similarly, the Federal High Court in Lagos restrained the Lagos State Government from enforcing the provisions of Hotel Occupancy and Restaurant (Fiscalisation) Regulations 2017 and paragraphs 4, 5, 6, 7, 8, and 11 of the Hotel Occupancy and Restaurant Consumption Law Cap H8, Laws of Lagos State 2015. The law introduced a five percent consumption tax in addition to a five percent Consumption Tax on every purchase or service rendered by hotels, restaurants, fast food outlets, event centers, bars and nightclubs in the State. But in a ruling delivered on March 21, 2018, Justice Rilwan Aikawa restrained the state from further enforcing the law. The judge said the law would remain suspended until the final determination of a suit filed against its implementation by the Registered Trustees of Hotel Owners and Managers Association of Lagos.

- Justice Rilwan Aikawa stopped the state and its agents from visiting the plaintiffs' hotels "for the purpose of installing fiscal electronic device and any other purposes whatsoever in furtherance of the law and the regulations. "Just like VAT, is a tax on sale of goods and services, except for the fact that it is only applicable to specific transactions.

- Other States and Local government even devised an unlawful means of collecting payments without appropriate legal backing through intimidation and harassment of the payers. Collection of it is characterized by the use of stickers, mounting of road blocks, use of revenue Agents/Consultants including motor park touts.

# 5. ABUSE OF INDIRECT TAX THROUGH MULTIPLICITY OF TAXES (Cont'd)

**Ways of curbing the abuse of Indirect Taxes through Multiplicity of Taxes are highlighted as follows:**

1. Institute a law restricting the role of tax consultants in collecting tax;

2. imposing stringent penalties for contravention of the law;

3. Increased allocation to State and Local Government and adequate funding of the Ministries, Agencies and Department;

4. State Government and Local Government should devise a creative approach of generating a revenue. However, should be conducted within the confines of the laws of the Federation;

5. Ensure that the Ministry of Local Government and the House of Assembly play their oversight functions very well on the activities of the Local government.

6. Critical review of the basis of the division of taxing powers in Nigeria under the Constitution.

# 6. REVISED NATIONAL TAX POLICY

The Federal Executive Council (FEC) on Wednesday, 1 February 2017, approved the revised National Tax Policy (NTP). The new policy is one of government's efforts to widen the nation's tax net to shore up the revenue accruing to the country. It is the outcome of the recommendations of the committee set up to review the National Tax Policy, by the Minister of Finance, in August 2016.

The committee was mandated, among other things, to review and update the policy, which was first published in 2012. Its mandate also included the identification of some luxury items for increased tax rates and the recommendation of a workable implementation strategy.

Explaining the highlights of the new policy, the Finance Minister noted that it provides fundamental guidelines for the orderly development of Nigeria's tax system. It is also designed to ensure a competitive and robust macroeconomic environment.

# 6. REVISED NATIONAL TAX POLICY (Cont'd)

**Highlights of the revised NTP include:**

**a) Introduction** – Comprises definition of tax, constitutional provisions, challenges of the Nigerian tax system and objectives of the NTP

**b) Policy Guidelines** – Explains the underlying principles of the Nigerian tax system and ways of using taxation as a tool for economic management and development

**c) Responsibilities of Stakeholders** – The obligation of various stakeholders: government, taxpayers, revenue agencies, etc. is spelt out

**d) Tax Administration** – The NTP provides guidance on tax registration, compliance, administrative efficiency, available technology and dispute resolution

**e) Implementation** – This section sets out implementation measures to be adopted to ensure that the objectives of the NTP are achieved

# 6. REVISED NATIONAL TAX POLICY (Cont'd)

One aspect of the new policy which appears to have overshadowed all others is the increase in **<u>Value Added Tax (VAT) on luxury goods</u>**. These items include : champagne, yachts, private jets, luxury cars based on engine capacity, expensive cosmetics and perfumes, topnotch mobile phones such as iPhone and iPad, designer watches, jewelry and retailer clothing.

However, the Federal Government and the National Assembly will work together to amend the relevant tax laws and then determine the actual VAT rates on these items and the actual date for the implementation of the policy. The revised NTP was issued in recognition of the need to increase tax income and diversify sources of government revenues. Thus its main objective, according to the Minister, is to guide the operations of Nigeria's tax system as well as provide unambiguous implementation and monitoring strategies for stakeholders in the Nigeria tax system.

# 6. REVISED NATIONAL TAX POLICY (Cont'd)

**Merits of the Revised NTP**

The revised NTP, If properly implemented, will

- Guide the operation of our tax system,
- provide the basis for future tax legislation and administration, as well as serve as a point of reference for all stakeholders.
- It would hopefully provide a benchmark on which stakeholders can be held accountable in the tax system., thereby aligning existing and future taxes based on capacity, fairness and simplicity, among other variables.
- Contains measures that will address the problems of multiplicity of taxes and revenue agencies, reduce income tax rates, increase compliance, expand Nigeria's tax base; and
- improve the tax to Gross Domestic Product (GDP) ratio.

# PROFESSIONAL ETHICS,

# STATEMENT OF TAXATION STANDARDS,
# &
# PROFESSIONAL RULES AND PRACTICE GUIDELINES

# 7. PROFESSIONAL ETHICS, STS, PROFESSIONAL RULES AND PRACTICE GUIDELINES (CONT'D)

## 7.1. STATEMENT OF TAXATION STANDARDS (STS 1-8):

Issued by the Chartered Institute of Taxation of Nigeria (CITN). Gazette in June 2013. It sets forth the tax practice standards to be followed in the course of the practice of taxation in Nigeria by members of the CITN.

The subjects contained in the STS are as follows. Each headings with there respective sub-headings

- STS 1: Know your Clients
- STS 2: Tax Returns Position
- STS 3: Procedural Aspects of Filing returns
- STS 4: Previously Agreed Tax Position
- STS 5: Form and Contents of Tax Advice/ Opinion
- STS 6: Knowledge of Error: Administrative Proceedings
- STS 7: Knowledge of Error: Returns Preparation
- STS 8: Use of Estimates

# 7. PROFESSIONAL ETHICS, STS, PROFESSIONAL RULES AND PRACTICE GUIDELINES (CONT'D)

**7.2. STATEMENT OF TAXATION STANDARDS (STS 1-8)**

- **STS 1: Know your Clients:**
  a. A member must exercise *reasonable skill and care* when acting for a client. Failure to exercise such reasonable skill and care may cause a member to be liable for negligence in the discharge of his professional duties.
  b. A member must understands the duties and responsibilities and the risks associated with advising such client.

- **STS 2: Tax Returns Position:** This Statement sets out the applicable standards for members when recommending tax return positions and preparing or signing tax returns (including claims for refund, and information returns) filed with any tax authority.

- **STS 3: Procedural Aspects of Filing returns:** This statement sets out guidance on the applicable standards for members when recommending tax return filing positions and preparing returns.
  a. a position reflected on the tax return as to which the taxpayer has been specifically advised by a member ; or
  b. a position about which a member has knowledge of all material facts and on the basis of those facts, has concluded whether the position is appropriate. For the purposes of this guidance, a taxpayer is a client, a member's employer.

# 7. PROFESSIONAL ETHICS, STS, PROFESSIONAL RULES AND PRACTICE GUIDELINES (CONT'D)

## 7.2. STATEMENT OF TAXATION STANDARDS (STS 1-8)

- **STS 4: Previously Agreed Tax Position:** This sets out the applicable standards for members in recommending a tax return position that departs from the position determined in an "administrative proceeding" or in a court decision with respect to the taxpayer's prior return.
- **STS 5: Form and Contents of Tax Advice/Opinion:** Sets out guidance for members on certain aspects of "providing advice to a client". It also considers the circumstances in which a member has a responsibility to communicate with a client when subsequent developments affect advice previously provided.
- **STS 6: Knowledge of Error: Administrative Proceedings:** sets out guidance on the applicable standards for a member who becomes aware of an error in a return that is the subject of an "administrative proceeding," such as an examination by any tax authority.
- **STS 7: Knowledge of Error: Returns Preparation:** To guide members on how to conduct themselves when error is detected in a taxpayer's previously submitted tax return or a taxpayer's failure to submit a required return. Within this guidance, the term error includes any position, omission, or method of accounting that, at the time the return was submitted, fails to meet the standards set out in STS
- **STS 8: Use of Estimates:** Guidance on the applicable standards for member when using the taxpayer's estimates in the preparation of a self assessment return.

# 7. PROFESSIONAL ETHICS, STS, PROFESSIONAL RULES AND PRACTICE GUIDELINES (CONT'D)

## 7.2. RULES AND PRACTICE GUIDELINES:

This contains Rules and Guidelines for the conduct of Tax practice in Nigeria (Chapter 1 – 14)

**Contents:**

1. Introduction
2. Professional Rules:
3. Practice Governance
4. New Clients
5. Client Service
6. Conflicts of Interest
7. Other client Handling issues
8. Charging for Services
9. Complaints
10. Ceasing to Act

Practice Guidelines: (2-14)

# 7. PROFESSIONAL ETHICS, STS, PROFESSIONAL RULES AND PRACTICE GUIDELINES (CONT'D)

**7.2. RULES AND PRACTICE GUIDELINES: This contains rules and guidelines for Tax practice in Nigeria (Chapter 1 – 14)**

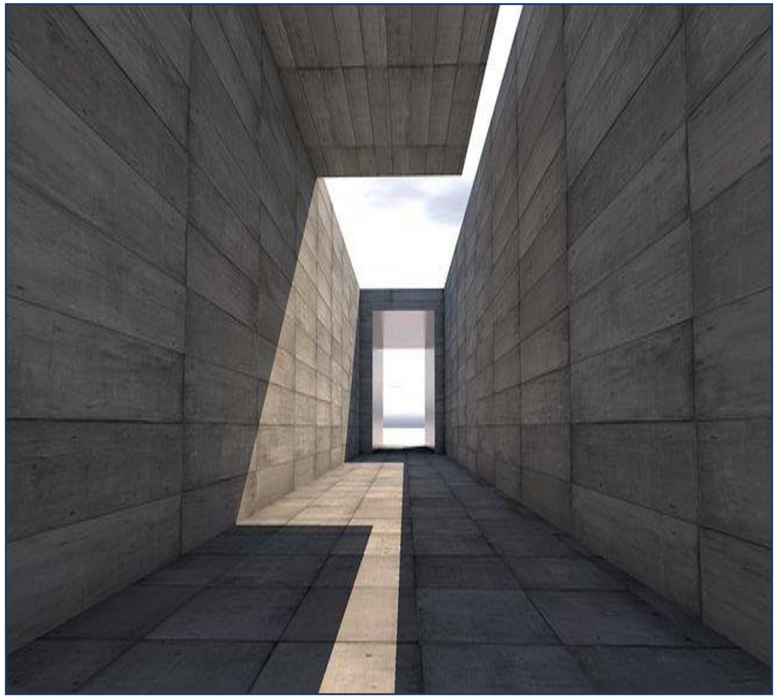
Contents (cont'd):

11. Training and MPTP
12. Members in Employment
13. Legal Matters
14. Advertising, Publicity and Promotion.

Practice Guidelines: (2-14)

# 8. CONCLUSION

Many OECD countries have been shifting their tax base towards consumption tax using the proceeds to lower the taxes and capital income.. Thus in order to enhance a proper shift in tax base- direct to indirect tax, there would be need for adequate planning, for a structured tax system. Implementation of an automated tax system to captured transactions from its source. No doubt that the fast tracking of the implementation of tax policy would go a long way to enhance the tax administration. However, as earlier mentioned the government needs to play its part in building the trust of the citizens as it is not a one way traffic. The government and the tax payers must be on the same page. Thus, beyond Direct tax, State Government must be creative, obtain the advise of tax professionals to advise of the methodologies to generate revenue through indirect taxation while avoiding multiplicity of taxes.



# 9. CASE STUDY I

**Case Study 1:**

Wazobia Nigeria Limited was incorporated on 1 January 2018. In February 2018, it employed the service of Omooyinbo UK LLP, a limited partnership based in London to carry out Transfer Pricing benchmarking analysis based on data provided via email. Omooyinbo completed its services in London and delivered hard copies of its report to a representative of Wazobia in Jayejaye hotel London. Wazobia paid Omooyinbo GBP5,000 for the services. Omooyinbo did not include VAT on its services on its belief that it qualifies as exported services under the UK VAT Act. Wazobia charged the professional fees to its profits and loss accounts but did not account for VAT to the Federal Inland Revenue Service (FIRS). FIRS raised VAT form 07 at the rate of 5% for the collection of VAT referred to as evaded VAT with its belief that reverse charge and destination principle caught up with the transaction. FIRS simultaneously included penalty of 10% and interest 19%. Wazobia raised objection on the ground that the services was not rendered in Nigeria. A tax dispute reconciliation meeting was fixed appointing you as the chairman of the dispute resolution. In your view:

1. Was Wazobia correct not to charge VAT on the ground purported?
2. Was the FIRS right to have imposed VAT on the ground of reverse charge and destination principle?
3. Comment on whether the case qualifies as tax evasion
4. Is application of penalty and interest right or not
5. As the chairman, what is your ruling and who is correct between Wazobia limited and the FIRS?
6. What case is similar to this in practice?

# 9. CASE STUDY 2

**Case Study 2**:

Reconsider scenario 1 above with the modification that Omooyinbo UK LLP Nigeria Limited sent one of its experts to Nigeria to generate the report. The expert used Eko Hotel. On completion, Wazobia collected the reports at Eko Hotel. Omooyinbo did not include VAT believing the transaction to be exported services. Wazobia agreed with omooyinbo and did not charge VAT. As the Chairman of the reconciliation team, what would be your answer to these questions:

1. Was Wazobia correct not to charge VAT on the ground purported?
2. Was the FIRS right to have imposed VAT on the ground of reverse charge and destination principle?
3. Comment on whether the case qualifies as tax evasion
4. Is application of penalty and interest right or not
5. As the chairman, what is your ruling and who is correct between Wazobia limited and the FIRS?
6. What case is similar to this in practice?

# 9. CASE STUDY SOLUTION

**Solution to Case Study 1**:

Yes
No
No
No
Wazobia.
Gazprom vs FIRS

**Solution to Case Study 2**:

No
Yes. But not on ground of reverse charge but services rendered in Nigeria.
No. It is tax controversy.
No
FIRS.
Vodacom vs FIRS

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