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Realizable Price Under the 2000 MOU is the Basis for PPT – Tax Appeal Tribunal

Tax Alert

Introduction

The Tax Appeal Tribunal ("TAT") has allowed the appeal brought before it by Total E & P Nigeria Limited ("**Appellant**") against the Federal Inland Revenue Service (the "**Respondent**" or "**FIRS**") challenging the use of Official Selling Price ("**OSP**") in determining oil pricing for the purpose of calculating Petroleum Profits Tax ("**PPT"**), rather than the Realizable Price ("**RP**") as agreed with the Federal Government in 2000 Memorandum of Understanding ("**MOU**") for determining same. The TAT held that RP was the proper pricing methodology applicable to Petroleum Profits Tax ("PPT") returns for 2006 and 2007 and discharged all additional assessments imposed by the FIRS.

2. Highlights of the Judgment

2.1 The Conflict

The Appellant had filed its PPT returns for 2006 and 2007 with FIRS using RP, following which the Appellant was served with additional assessments. The Respondents had calculated the Appellant's PPT liability using OSP which yielded a higher tax burden for the Appellants. The Appellant argued that by MOU signed with the FG in 2000, the parties agreed to adopt RP as the basis for computing PPT. The Appellant stated that the MOU sprang from sections 9 (2) (a) and 23(5) of Petroleum Profit Tax Act ("PPTA") 2004 and that by the provisions of the MOU, the mode of computation of Royalty and PPT was not OSP as used by the Respondents but RP.

Conversely, the Respondents disagreed and argued that there is no agreement between FGN, NNPC, and the Appellant on the pricing methodology for computing PPT for 2006 and 2007. The Respondents stated that the MOU had long been terminated before the tax period in dispute. They also argued that PPTA overrides any agreement between parties even if any existed. The Respondents argued that OSP is the relevant mode of pricing for the purposes of PPT liability provided in the PPTA which was the mode they adopted to arrive at the Appellant's PPT assessment.

2.2 The Laws

The relevant provisions of the law canvassed by the parties include:
Section 9(2) (a) & (1) (b) of Petroleum Profits Tax Act 2004 (PPTA) *which provides thus:*

> *"For the purposes of **subsection (1) (b)** of this section, the value of any chargeable oil so disposed of shall be taken to be the aggregate of-*
> *(a) the value of that oil as determined, for the purpose of royalty, in accordance with the provisions of any enactment applicable thereto <u>and any financial agreement or arrangement</u> between the Federal Government of Nigeria and the company;"*
> ***"Section (1)** Subject to any express provisions of this Act,*

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> *in relation to any accounting period, the profits of that period of a company shall be taken to be the aggregate of-*
> ***(b)*** *the value of all chargeable oil disposed of by the company in that period;…"*

It allows the price of chargeable oil to be determined by either the provision of any applicable law or any financial agreement or arrangement between the FGN and the oil company.

> Section 23(5) of Petroleum Profit Tax Act 1958 *as amended*
> *In this section,* ***"posted price",*** *in relation to any crude oil exported from Nigeria by a company, means the price F.O.B. at the Nigerian port of export for crude oil of the gravity and quality in question which is from time to time established by the company, after agreement with the Government of Nigeria as to the procedure to be followed for the purpose, as its posted price for Nigerian crude oil of that gravity and quality.*

It defined "posted price" as the price F.O.B. which is from time to time established by the company after agreement with the Government of Nigeria.

2.3 Analysis of the Conflict

In making its submission as to whether the MOU was binding on the parties during 2006 and 2007. The Respondent relied on the decision in *Mobil Producing (Nig.) Unlimited v. FIRS (FHC/C/10A/13)* which held that the PPTA is the regime for computing PPT as against agreement of parties. The Respondent further stated that the MOU had become defunct by effluxion of time, which was before the 2006 and 2007 periods in dispute.

The Appellant disagreed citing a clause in the MOU which provided that where the government fails to provide a new fiscal regime after the termination of the MOU, the MOU will continue to apply notwithstanding the termination until the government comes up with a new regime in which case the MOU will immediately cease to apply. In the instant case, preceding 2006 and 2007 the government had not effectively abrogated the existing regime; hence they argued that the provisions of the MOU continued to apply during the period. The court agreed with the Appellant that prior to 2006 and 2007 the FGN had not officially published a new regime and this meant tacit agreement and connotes that the MOU applied during 2006 and 2007.

Another issue which the TAT had to resolve was whether the MOU can override the clear provisions of the law. While the Tribunal agreed with the respondent on a decision of the Supreme Court to the effect that no matter how strong and well worked out an MOU is, it cannot be used to override clear provisions of the law, it however rejected the position of the Respondent that by the provisions of PPTA, OSP was the method for computing PPT and that it was the adopted standard practice. The Tribunal stated that Section 9 (2) (a) of PPTA allows the FGN and the Oil Company to deviate from the Act by a mutual agreement, as in this case (the MOU). The court stated that the MOU continued to apply until the FGN issued a letter dated 17th January, 2008 which brought to an end the old regime and announced the new regime.

3. Comments

The dispute resolved by the TAT is as a result of improper assessment of the Appellant on the basis of OSP as against RP which the court agreed is the proper basis which should have been adopted by the FIRS in arriving at the PPT payable by the Appellant during the relevant periods.

3.1 Tacit Agreement

The issue of tacit or implied agreement came up in this case. The MOU elapsed by effluxion of time in

2003. However, Clause 7.3 of the MOU stated that notwithstanding, the MOU shall continue to apply until the FG adopts a new regime. After the MOU terminated, the FG remained silent but continued to deal with Oil Companies on the basis of the old regime.

The Tribunal's position was that the period the Federal Government remained silent after the MOU terminated was deemed a tacit agreement and the termination can only take effect as from 2008 when the MOU was officially brought to an end.

3.2 Effect of the Judgment

The TAT is a Tribunal set up by law to mediate and resolve tax disputes in Nigeria and a resort for aggrieved tax payers and stakeholders. The judgment given by the TAT is without doubt commendable and worth taking a cue from. While we are not unaware that tax is a major source of income for governments at all levels, it is our view that the Tribunal must continue to handle each case brought before it with all the sensitivity it requires.

Pursuant to this judgment, the FIRS will have to cancel the additional assessment served on the Appellant. In effect, FIRS will now have to adopt RP for the tax periods during which the MOU between the government and the oil companies concerned remained valid.

Conclusion

Although the judgment may mean reduction in revenue derived for those periods from PPT, that notwithstanding, portends goodwill for the judiciary and tax administration in Nigeria.

The FIRS or the Respondent has the right to appeal to the Federal High Court. Meanwhile, we are not aware that any appeal has been lodged as at the time of this tax alert.

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