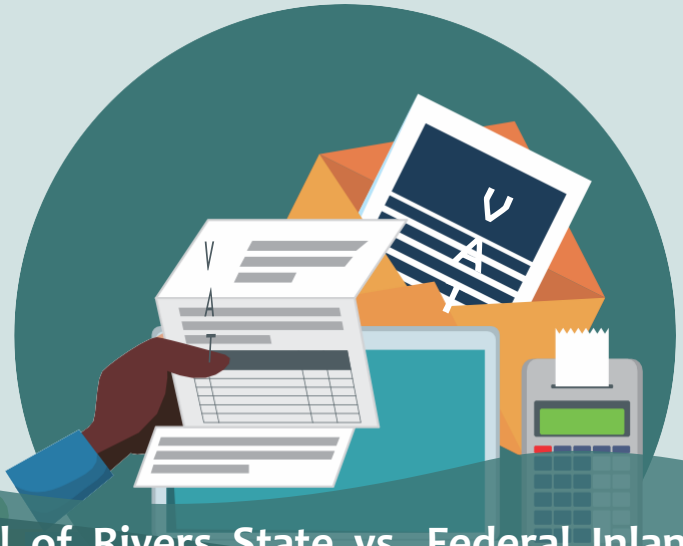

Attorney General of Rivers State vs. Federal Inland Revenue Service: A Review of the Pros and Cons of this Landmark VAT Decision

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Introduction

Recently, in the case of *Attorney General of Rivers State vs. Federal Inland Revenue Service & Attorney General of the Federation*[1], the Federal High Court ("FHC")[2] sitting in Port Harcourt rendered a ground- breaking decision currently agitating the minds of everyone in the country. The decision appears to have revived the lingering debate over fiscal federalism in Nigeria and the unsettled issues of taxing powers of the centre (Federal Government) and the component States within the Federation. Equally, the decision impliedly questions the nature of federalism or rather unitarism that Nigeria practices. Other relevant underbellies of the decision, which our brief analysis considered, are: (1) whether in the light of current judicial pronouncements on the powers of the National Assembly to exclusively legislate on matters contained in Chapter II of the Constitution of the Federal Republic of Nigeria, 1999 (as amended) such have overtaken or rendered useless the "residual powers" traditionally preserved for component States in a true federal arrangement.

In the main, the Pros and Cons of the decision are reviewed to demonstrate the strengths and weaknesses of the FHC's decision; and to point to the direction(s) on how the extant legal impasse could be resolved for a better federal experience in Nigeria.

Overview of FHC's Decision

Prior to the extant decision of the FHC, there was no contentious suit wherein a court in Nigeria barred the Federal Government or any of its agencies – the Federal Inland Revenue Service ("FIRS") in particular – from collecting Value Added Tax "VAT" in the Country; or directed that a State Government has the exclusive power under the Constitution to collect VAT to the exclusion of the Federal Government. The FHC sitting in Port Harcourt became the first court in Nigeria to hold otherwise. Several legal issues relating to the taxing powers of the Federal Government and Rivers State were canvassed and thoroughly argued by the parties. In resolving the issues placed before it, the Court held, among other things, that:

1. It had searched the entire Constitution to find out if the Federal Government is empowered to impose and collect taxes outside the provisions of items 58 and 59 of the Exclusive Legislative List without success. Therefore, the Federal Government's power to impose and collect taxes is limited and/or circumscribed to the specie of taxes listed in items 58 and 59 of the Exclusive Legislative List and no other. In particular, the court held that the Federal Government does not have the power to legislate on VAT, Education Tax and Technology Tax since they are outside its taxing powers[3]

[1]Suit No: FHC/PH/CS/149/2020
[2]Presided by Hon. Justice Stephen Dalyop pam

2. Save corporate income tax, item 7(a)&(b) of the Concurrent Legislative List limits the power of the National Assembly to delegate the power to collect taxes listed in Items 58 and 59 of the Exclusive Legislative List to only State Governments or their agencies thereof. Therefore, any delegation to any other person or entity apart from a State Government or its agency shall be null and void. The implication of this decision is that the National Assembly cannot make law empowering the Federal Government or any of its agents – such as the FIRS – to collect any of the taxes (except companies income tax) listed in items 58 and 59 of the exclusive list.

The above ratios are the main causes of controversy in Nigeria's tax discourse today. The Federal Government and/or FIRS has already appealed against the decision of the FHC.

The Pros of the Decision

Traditionally, federalism is a political device more suited in a heterogenous society for the sharing of powers amongst two – or perhaps more – units of governments with the expectation that each level of government will restrict itself to the legal boundaries drawn for it by the Constitution – considered to be the governing supreme document of the political state. Without delving into the history of the current constitution, it is assumed to be an Act of the people. Many have disputed this because at no time were Nigerians engaged by the departing Military Government of Rtd. General Abdulsalami Abubakar to participate, democratically, in the making of the 1999 Constitution. Therefore, those who oppose the Constitution argue that it is not an Act of the people or an autochthonous living document. Rather, it is seen as a military decree imposed on the people. Regardless, the 1999 Constitution remains the supreme law of the land; and by virtue of section 315 of the Constitution, existing military decrees and edicts or any other law in force before the extant Constitution came into force are preserved. Such existing laws must comply with the conditions stipulated in section 315 and should not violate any provision of the Constitution before it could be accommodated as part of our laws. Indeed, all tax statutes that were in force prior to the coming into force of the present Constitution are deemed to continue to be in operation. Fortunately, the courts have started questioning the propriety or otherwise of some of the existing laws. Last year, the Court of Appeal in *Uyo Local Government Council vs. Akwa Ibom State Government & Anor.*[4] annulled the *Taxes and Levies (Approved List for Collection) Act* for being inconsistent with the Constitution.[2] It is not surprising that Rivers State Government has challenged the authority of the Federal Government, through FIRS, to collect VAT in the State.

Many hail the decision for asserting the principle of fiscal federalism that is currently lacking in Nigeria. The supporters of this decision are against the extant practice where most available resources in the country are in the hands of the Federal Government; while States go cap in hand to Abuja on monthly basis for allocations. This practice has rendered most of the States in Nigeria financially dependent on the Federal Government. Rivers State in this case has challenged the authority of the Federal Government to dominate the country's tax regime – especially the collection of VAT.

The decision of this court appears to have strongly asserted the powers of State Governments to collect taxes. Both Rivers and Lagos State Governments have enacted their State VAT Laws respectively. Many see this decision, if sustained by the appellate courts, as a victory for fiscal federalism that is currently lacking in the country.

The **Cons** of the decision are taken together with the analysis below.

Analysis of the Decision and the Position of the Law

The resolution of the present legal impasse revolves round the taxing powers of the Federal Government of Nigeria and a State Government under the extant Constitution. Thus, it is not in doubt that the Federal Government

[3] Unfortunately, the court added 'Withholding Tax' as a form of taxation that the Federal Government cannot collect.
[4](2020) LPELR-49691 (CA)

(through the National Assembly) has the exclusive power to legislate on matters listed in the Exclusive Legislative List contained in Part 1 of the Second Schedule to the Constitution.[6] A State Government's House of Assembly is forbidden from legislating on matters contained in the Exclusive Legislative List. In addition, both the National Assembly and State Houses of Assembly in Nigeria are empowered to legislate on matters listed in the Concurrent Legislative List contained in Part II of the Second Schedule to the Constitution.[7] Several judicial authorities have held that if in the exercise of their legislative powers, a law made by the National Assembly conflicts with the one made by a State House of Assembly, the law made by the National Assembly will be deemed to have covered the field and leaves nothing for the State.

However, where a subject matter is neither listed in the Exclusive Legislative List nor the Concurrent Legislative List; and also not assigned to any of the legislative bodies (*i.e*, either the National Assembly or State Houses of Assembly) by any part of the Constitution, such subject matter is considered to be a residual matter under section 4(7)(a)&(b) of the Constitution.[8] Residual Matters, according to our courts, fall within the exclusive province of a State Government to legislate on.[9] Thus, the Federal Government, through the National Assembly, are constitutionally prevented from legislating on residual matters.[10] Though the FHC did not discuss the exclusive power of State Houses of Assembly to legislate on residual matters, it focused its attention on interpreting the taxing powers contained in items 58 and 59 of the Exclusive List; and item 7 of the Concurrent List.

As indicated above, the court held that VAT, Education Tax and Technology Tax are not listed species of taxes contained in items 58 and 59 of the Exclusive Legislative List.

Therefore, it is unconstitutional for the Federal Government (through the National Assembly) to make laws imposing or directing the collection of taxes outside the head of taxes contained in items 58 (Stamp duties) and 59 (taxation of incomes, profits and capital gains). The court claimed to have searched the Constitution without seeing any other provision that the National Assembly could rely on to impose taxes outside items 58 and 59 of the Exclusive List. It further maintained that item 7 (a) & (b) limits the entities or bodies that the National Assembly could confer the collecting powers of taxes contained in items 58 and 58 (save Companies Income Tax) to only a State Government or its agency but no other.

Pitfalls of the Judgment:

At a glance, the decision of the FHC on this matter appears sound – especially to the advocates of fiscal federalism; but a critical review of it shows that there are loopholes not properly covered. Some of them are:

(a) Failure to Distinguish Intra-State Transactions from Inter-State and/or International Transactions

In deciding that the National Assembly has no power to impose or collect VAT in Rivers State or any other State for that matter, the FHC failed to draw a line between intra-State transactions on one hand and inter- State or International transactions on the other. On the taxing powers of a State Government over intra- State, inter-State and international transactions, the Supreme Court settled the issue in *Attorney General of Ogun State vs. Aberuagba.*[11] The apex court held, *inter alia,* that a State Government was constitutionally empowered to impose sales tax – a consumption tax – only on intra-State transactions. It clearly held that a State could not impose sales tax on inter-State or international transactions, being matters exclusively reserved for the Federal Government in item 61 ofthe Exclusive Legislative List (i.e, "trade and commerce clause") under the 1979 Constitution – now item 62 of the Exclusive Legislative List, Part 1 of the Second Schedule to the 1999 Constitution. The Supreme Court struck down Ogun State's tax law to the extent that it imposed sales tax on inter-state and international transactions. With this decision, which is still the law, the FHC is wrong to have extended the reach of its decision to inter-State and international transactions – none of which falls within the jurisdiction of a State Government.

[5]The court relied on the ouster clause contained in section 1 of the Decree to nullify the entire statute for being inconsistent with the provisions of the 1999Constitution (as amended)
[6]Section 4(3) of the Constitution of the Federal Republic of Nigeria, 1999 (as amended) ("Constitution").
[7]Sections 4(4)(a) and 4(7)(b) of the Constitution.
[8]Attorney General of Abia State vs Attorney General of the Federation (2006) 16 NWLR (Pt 1005) 265, 38
[9]Ibid
[10]Ibid at 265, 380.
[11](1985) 1 NWLR (Pt 3) 395, 405.

The statutory support for the position taken by the apex court is found in item 62 of the Exclusive List (known as **trade and commerce clause)**. Similar judicial interpretation provided by the Supreme Court in Aberuagba's case was earlier reached by the Supreme Court of Canada in *Dominion Stores Ltd. vs. The Queen*[12] and the US' Supreme Court in *Wardair Canada vs. Florida Department of Revenue*.[13] Therefore, it appears to be a global practice amongst federal states in the interpretation of a trade and commerce clause and the extent of taxing powers of a State or Province to be restricted within the State's or Province's intra-state transactions; and, therefore, does not extend to inter-state or international transactions. This distinction was not drawn by the FHC in prohibiting the Federal Government or the FIRS from collecting VAT in Rivers State.

(b) Failure to Recognise that Withholding Tax is not a Form of Taxation but a Means of Tax Collection

The FHC in this case erroneously treated withholding tax as a form of taxation such that it was considered a separate head of tax different from personal/corporate income taxation and/or other forms of taxation. Of note is that the FHC included **Withholding Tax** as one of the taxes that the Federal Government is excluded from collecting since it is not listed in any of items 58 and 59 of the Exclusive List. This is a display of poor understanding of Nigeria's tax regime. Withholding Tax is not a form of taxation but a means of tax collection in advance. The purpose of withholding tax is to ensure that taxpayers' earnings subject to income tax are captured early to limit the occurrence of tax evasion. Therefore, a purchaser of goods and services subject to withholding tax is authorised to deduct the applicable rate from an invoice of a supplier and then remit the withheld amount to the appropriate tax authority – who in turn will issue a withholding tax credit note through the purchaser for onward transmission to the supplier who in turn will use the credit note to recoup the withheld amount by deducting same from its/his/her income tax liabilities. Having admitted that corporate income tax is not one of the taxes assigned to State Governments to collect, it makes no sense prohibiting Federal Government from collecting advanced corporate income tax through the mechanics of withholding tax.

c) Taxes Listed in items 58 and 59 are not the only Head of Taxes Expressly Listed or Mentioned in the Exclusive List to be within the Exclusive Jurisdiction of the Federal Government to Impose and/or Collect

The FHC held that: "… the Court has searched other parts of the Constitution to see if there is any provision that allows the Federal Government to impose and collect taxes outside the scope of items 58 and 59 of Part 1 of the Second Schedule and the court can find none".[14] This finding is wrong. Without considering items 62 (trade and commerce clause) and 68 (incidental and supplementary clause) because of controversies surrounding their interpretations, the FHC failed woefully to recognise items 16 (customs and excise duties) and 25 (export duties) of the Exclusive List. These are additional taxes that the Federal Government is authorized to exclusively impose and/or collect.

(d) It is Wrong to Hold that the National Assembly is Restricted in the Exercise of its Powers under Items 58 and 59 of the Exclusive List by item 7(a) & (b) of the Concurrent List to Confer the Power to Collect the listed Taxes, thereof, to only State Governments or their Agencies

In interpreting item 7(a)&(b) of the Constitution, the FHC held that the National Assembly in the exercise of its powers under items 58 and 59 of the Exclusive List could only confer the power to collect those taxes on a State Government or its agency. This position is wrong. First, no State Government or its revenue collecting agency is authorised to collect Companies Income Tax. Secondly, the power referred by item 7(a)&(b) is discretionary, which may or may not be exercised. In addition to being discretionary, the provision states that the National Assembly shall prescribe the conditions under which the taxes could be collected. Also, there is no additional new head of tax mentioned in the concurrent list other than the ones listed in items 58 and 59 of the Exclusive List. The exercise of taxing powers listed in the Exclusive List cannot be controlled by the concurrent list which creates no new head of tax. Indeed, it is not surprising that the Personal Income Tax Act under its section 2 allocates the power to collect personal income tax between the Federal and State Governments. The Federal Government is empowered to collect personal income from the members of the Nigerian Police Force, Army, Navy, Air Force, officers of Nigerian foreign service and non-residents of Nigeria who derive income from anywhere in Nigeria.

[12] [1980] 1 SCR 844.
[13] 477 US 1 (1986).
[14] See the last Paragraph of page 41 to the commencement of page 42 of the judgment.

The Slippery Slope

There are certain parts of the Constitution that we consider legal landmines that the appellate courts must be careful in construing to ensure there is no erosion of the residual powers of a State Government. An unrestricted interpretation of these provisions will surely leave nothing for the States except at the mercy of the Federal Government. The provisions are:

(a) Construction of items 62 (trade and commerce clause) and 68 (incidental and supplementary clause) of the Exclusive List

Some may argue that the VAT Act had survived as an existing law under section 315 of the Constitution as a federal enactment with a nation-wide application despite there is no specific head of tax in the Exclusive List where VAT or Sales tax is mentioned. The proponents of this argument could rely on items 62 and 68 of the Exclusive List. These proponents believe that the National Assembly should be taken to have relied on the trade and commerce clause (item 62) or the incidental and supplementary clause (item 68) to have enacted the VAT Act. On the interpretation of the trade and commerce clause, the decision of the Supreme Court in Aberuagba is clear. It does not support the argument that the VAT Act would apply as a federal statute without limitation in its scope or country-wide application – even if it had survived as an existing law under section 315 of the Constitution. As an Act of the National Assembly with a nation-wide application, the VAT Act could only apply and be restricted to inter-State and international transactions.[15] If it survived the section 315 test as a law of State House of Assembly, it can only apply to the Federal Capital Territory (FCT) as a law of a State deemed to have been enacted by the National Assembly under section 299 of the Constitution, which empowers the national legislative body to exercise the powers of a State House of Assembly on behalf of the FCT.

Also, the interpretation of the incidental and supplementary powers of the National Assembly cannot be extended to rely on specific head of tax or subject matter created by any of the items in the Exclusive List. If the legislature had intended to vest on the Federal Government or National Assembly the power to impose VAT, it would have expressly provided for it – just as it did for stamp duties, income tax, capital gains, customs and excise duties. The power to impose tax cannot be implied from the construction of another power granted a legislative house. To argue otherwise would suggest that the express provisions of taxing powers in the exclusive list are merely redundant, superfluous and unnecessary since any head of tax not listed in the exclusive list could be covered on the invocation of items 62 and 68 of the Exclusive List. If this line of reasoning is approved by the court, it means there is no kind of tax imaginable that will not be accommodated under items 62 and 68. Also, the acceptance of this argument would render the principles of residual powers of a State Government and fiscal federalism sterile. We do not think this is the intention of the drafters of the Constitution – for the federal government to usurp all legislative and, perhaps, executive powers of taxation without reserving any for the States.

(b) Construction of item 60(a) of the Exclusive List as a One-Size-Fit-All Clause to Capture all Imaginable Subjects under Chapter II (Fundamental Objectives and Directive Principles of State Policy)

It is also possible that some may argue that the National Assembly may justify the VAT Act as an existing law under item 60(a) and section 16 of the Constitution. Item 60(a) confers exclusive jurisdiction on the National Assembly to make laws relating to the: "The establishment and regulation of authorities for the Federation or any part thereof – (a) to promote and enforce the observance of the Fundamental Objective and Directive Principles contained in this Constitution". Proponents of this view point could argue that item 60(a) has empowered the Federal Government to regulate, control and manage the country's economy under section 16(1)&(2) of the Constitution for the benefit of the citizenry. They are likely to rely on several cases where the courts have held that only the National Assembly could rely on item 60(a) of the Constitution to bring to life any provision of the Chapter II of the Constitution (*i.e*, the Fundamental Objective and Directive Principle of State Policy[16]) considered to have been exclusively assigned to the National Assembly to legislate on.[17]

[15]For detailed analysis on this point, see J.J. Odinkonigbo and N. Ikeyi, "Is the Power of a State to Impose Sales Tax in Nigeria Fettered by the Imposition of Value Added Tax by the Federal Government?" (2015) vol. 41 (4) Commonwealth Law Bulletin 577 – 596. [16]Chapter II of the Constitution is considered unjusticiable by virtue of section 6(6)(c) of the Constitution. They are seen more as the political, economic and social goals that elected officials should pursue for the benefits of the society. Thus, they are viewed as the yardstick to measure the performance of any government in power.
[17]See Attorney General of Lagos State vs. The Attorney General of the Federation & 35 Ors (2003) 12 NWLR (Pt 833) 1; A.G. Ondo vs. A.G. Federation (2002) 6 SC (Pt.1) 1 or (2002) 9 NWLR (Pt.772) 222; HELIOS TOWERS NIG. LTD v. NESREA & ANOR (2014) LPELR-24624(CA)

Normally, this should not be extended to conferring additional powers not expressly provided in the constitution. Taxing powers are expected to be expressly provided so as not to usurp the residual powers of a State Government. Doing otherwise will render the principle of federalism useless. In other federal states, residual powers are jealously guided. For instance, the residual powers in the US are exercised by the States;[18] while in Canada, the Federal Government exercises residual powers[19]. The difference between the two countries is that in Canada, provinces have enumerated powers,[20] while the Federal Government exercises powers over matters expressly conferred on it and others not assigned by the constitution to either of the levels of government. But the common thread is that regardless of which level of government that a residual power is conferred, it must be respected without encroachment from the other.

Nigeria adopted the US' prototype of Federal Constitution in the partition of legislative power, which allocates residual powers to the States. In the US, sales tax or VAT are imposed and collected by State Governments because it does not fall under enumerated federal powers or State powers; and the Federal Government of US has not relied under its trade and commerce clause to wade into the province of sales tax or VAT regime. Therefore, it is expected that in compliance with the principle of true federalism, the powers of the Federal Government under any of the clauses mentioned above or in item 60(a) of the Exclusive List should be restricted in their interpretations to avoid the erosion of the residual powers of a State Government – especially as it concerns taxing powers which are expected to be expressly imposed or authorised by the Constitution.

Recommendations:

From the above, we can see that the issues relating to what level of government is empowered to collect which tax is controversial. Though the FHC sitting in Port Harcourt has decided on this matter, it will not be the last to be heard about this contentious subject. We therefore recommend that:

1. Since this matter borders more on the interpretation of the Constitution, the appellate court could borrow a leaf from the decision of the Supreme Court in Aberuagba's case by holding that State Governments have the exclusive power to legislate on VAT matters relating to intra-State transactions; while the Federal Government exercises the exclusive power to legislate on inter- State and international transactions.

2. The implied legislative powers contained in items 62, 68 and 60(a) to impose VAT, for whatever reason, should be interpreted to restrict the Federal Government powers to only inter-State and international transactions. The exercise of the powers in any of the clauses by the Federal Government must not go beyond the boundaries drawn above; otherwise, it will be clear there is nothing federal in the exercise of taxing powers in Nigeria.

3. We do not support the amendment of the Constitution to take away the powers of State Governments to exercise legislative powers over VAT matters in intra-state transactions. Any amendment of the Constitution in favour of the Federal Government should be restricted to inter- State and international transactions.

Conclusion

The decision of the FHC in *Attorney General of Rivers State vs. Federal Inland Revenue Service & Attorney General of the Federation* (supra) has re-awakened the demand for fiscal federalism in Nigeria. It asserts that the legislative powers of the Federal Government are circumscribed by the Constitution – especially to the extent of express powers conferred on the National Assembly which must not be extended to erode the powers of a State. Regardless, we examined the loopholes left in the decision and discussed correct position(s) of the law. We have also offered brief recommendations on what the Government could do to resolve the current legal impasse and also retains fiscal federalism within the Nigeria's federal arrangement. The bottom line is that the drafters of the Constitution intended to reserve residual powers for State Governments. Since Nigeria follows the US model of federal constitution, we must respect the residual powers of States without usurping them through judicial interpretations or one-sided constitutional amendments that will turn Nigeria into a full-blown unitary State.

[18]See the 10th Amendment to the US' Constitution. This provides that powers not assigned to the United States by the Constitution nor prohibited by it to the States are reserved to the States.
[19]See section 91 of the British North America Act, 1867.
[20]See section 92 of the British North America Act, 1867.