



Petroleum Profits Tax in Nigeria

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1. Introduction

There is an old proverb, which states that there is nothing as certain as death and taxes. Taxation is generally recognized as an important and established source of revenue for the Government. There is hardly any country today that does not rely or make pretensions to rely on taxation measures not only to provide the much needed revenue for social-economic development but also to reduce the inequalities of wealth in the society. The tax system is therefore one of the most powerful levers available to any government to stimulate and guide its economic and social development. Taxation therefore looms largely in our lives. Petroleum tax is considered as one of the most important sources of revenue for the government in Nigeria because of the widespread use of petroleum products.

2. Petroleum Profits Tax in Nigeria

The enabling law on Petroleum Tax in Nigeria is the Petroleum Profits Tax Act, 1958. The objective of the Act is to impose a tax upon profits from the winning of petroleum products. The act applies only to the taxation of incomes of companies engaged in petroleum operations. Petroleum taxation in Nigeria is as complex and complicated as the taxation of any other primary products. Many non-tax considerations – political, ethnic, economic, social and other factors weigh higher than taxation and explain the complications. Through the Petroleum Profits Tax Act remains the current principal

Act, it is not the only taxing law. What standard would apply to an operator would invariably be dictated by the type of agreement the operator signed with the Nigeria National Petroleum Corporation (NNPC) or the Petroleum concessionaire, as the case may be. The Petroleum Profits Tax Act still provides the framework for the computation of the Petroleum Profit Tax Act still provides the framework for the computation of the Petroleum Profit Tax but what goes into the computation is dictated by the terms of these agreements which modify the application of the provisions of the Petroleum Profits Tax Act.

The main distinguishing features between Petroleum Profits Tax and the Orthodox income tax on companies are as follows:

- (a) By Section 19 of the Petroleum Profits Tax Act the assessable tax for any accounting period of an oil company is equal to 85% of its chargeable Profits of that period. Deductible from this assessable tax are such liabilities as royalty payments, rates, imports and fees payable to the Federal or State Governments. The effect of this is that the Government bears these outgoings out of its share of the chargeable profits. Subject to the foregoing all “outgoings and expenses wholly and exclusively incurred, whether within or without Nigeria” are deductible from the oil company’s gross profits under section 10 of the Petroleum Profits Tax.

- (b) The above arrangement of, in effect, splitting the chargeable profits between the company and the revenue effects dividend payments payable by the company out of its slice of profits. These are payable without deduction of tax at source and the tax payer is neither entitled to claim any repayment on their grossed up basis nor is he liable to pay income tax on the amount received under section 12 of the Act. Petroleum
- (c) Profits Tax is payable by twelve equal installments.

Like the companies income tax, Petroleum Profits Tax is administered by the Federal Board of Inland Revenue as a federal tax.

Companies involved in prospecting for or extracting and transportation petroleum are taxable under the Petroleum Profits Tax. There are three types of companies in the petroleum industry. These are the crude oil producing companies, which provide services to oil producing companies. These services include seismic survey, drilling, logging and interpretation of data collected from oil fields. Petroleum Profits Tax is the most important sources of revenue for the government. It accounts for about 95 percent of the Federal Government Foreign exchange earnings. It is because of the importance of the Petroleum Profits Tax as fruitful source of revenue to the Government that the Petroleum Act of 1990 vests the entire ownership and control of all petroleum in, under or upon any land or lands in Nigeria in the Federal Government.

The due administration of the Petroleum under the care and management of the Federal Board of Inland Revenue which may do all such acts as may be deemed necessary and expedient for the assessment and collection of the tax from oil producing companies anywhere in Nigeria. The Board is therefore given general administrative powers similar to those under the general Companies Income Tax Act, 1979 for the purposes of administering the Petroleum Profits Tax.

Assessable Tax is levied on the chargeable profits of petroleum companies at the rate of 85

percent in respect of the accounting period of the company.

Petroleum Profits Tax for any accounting period of twelve months is payable in twelve equal monthly installments together with a final installments. The first monthly payment shall be due and payable not less than the third month of the accounting period which shall be in an amount equal to one-twelfth of the amount of the tax estimated to be chargeable for such accounting periods is less than 12 months the installment payment shall be by the number of the months in the accounting period. Further monthly payments shall be due and payable not later than the last day of each subsequent month of the accounting period. The amount of tax to be chargeable for the accounting period less the sum already paid, divided by the number of monthly payments remaining to be made in respect of the accounting period. A final installment of tax is due and payable within 21 days after the service of the notice of assessment which shall be the amount of the tax assessed less the amounts of the monthly payments already made.

The Petroleum Profits Tax is considered as oppressive and disincentive. The present petroleum tax rate of 85 percent in Nigeria could be seen as a clog to the development of Oil industry in the country. It was in recognition of this problem that the Federal Government introduced many concessions on oil products.

In Nigeria, a lot of tax incentives have been provided for to encourage local and foreign investors. These are in the form of various deductible allowances and several fiscal incentives such as tax offsets, credits etc. For any accounting period of a company the current petroleum profits tax rate on chargeable profits is 85 percent.

It has been suggested that the petroleum profits tax would create a large amount of uncertainty for foreign investors who have a continuing and long-term need for investment in the country. That high tax would have an unduly harsh impact on foreign company with low capital base to purchase petroleum products.

In order to reduce the effect of the Petroleum Profits Tax on foreign investors, the Federal Government in June, 1993 announced a 10-point package of incentives to encourage investment

in the downstream sector of the country's petroleum industry. According to Asiodu, "The incentives included 100 percent equity participation by local and foreign investors and the guarantee of investments already made, if effected by Government regulations and policies.

The package includes a five-year tax holiday from the beginning of operations and guaranteed export earnings, which could be kept in approved escrow accounts in the investors' choice of countries. It also includes various other incentives, including capital allowances at 20 percent rate per annum for the first four years. According to Asiodu the investors would also be allowed to feedstock for processing for both export and local markets, enjoying a guarantee of crude oil supply and receive preferential consideration for a duty reduction of up to 50 percent on imported construction materials where considered necessary.

The Federal Government in 1993 also decided to overhaul the system of taxation in the country, to make it more efficient, simple, broad based and cost effective. This move was taken to minimize government over-dependence on oil revenue. The government's desire to strengthen non-oil taxation was to encourage efficient investment growth in the private sector and have the resources to finance public expenditure adequately. According to Olashore, "...in carrying out the overhaul, the government would ensure that the incidence of the new indirect taxes focused on the non-basic consumption items and maintain a progressive approach by taxing luxury items."

In the same vein, the Federal Government in its efforts to encourage and promote the development of the oil producing areas in the country introduced tax concessions to oil companies who are willing to provide basic essentials of life, including water, roads, schools and other facilities, as well as jobs, that could approve the economic well-being of the people in the oil producing area. It was in recognition of this government gesture that Shell Petroleum Development Company in Delta State between 1992-1993 donated furniture for schools in 104 communities, 74 gets new classroom blocks while 60 were provided with portable water, 51 were provided with science equipment. The

company also awarded 30 university and 1,158 post-primary scholarships to students in 17 local governments. The Petroleum Profits Tax provides that where a company engaged in petroleum operations is also engaged in transportation of chargeable oil by ocean going oil-tanker operated by or on behalf of the company from Nigeria to another territory, then any profit or loss attribute to such transportation business shall be excluded from the adjusted profits for the purpose of the petroleum operations.

One major problem of the Petroleum Profits Tax in Nigeria is inadequate penalty. A penalty of N1,000.00 (One Thousand Naira) is certainly inadequate for a multinational company for rendering insufficient and incorrect information in their accounts.

Secondly, for any accounting period of a company, the current Petroleum Profits Tax on chargeable profits is 85 percent. The effect of the tax rate is low in view of several fiscal incentives provided for in the Act.

The present petroleum tax rate of 85 percent for petroleum products and the concessionary tax rate of 65 percent for five years are considered as overbearing and burdensome. Since the nature of the oil business is fraught with a lot of risk and uncertainty, there is need for tax holiday of a longer duration. Retroactive legislation in the area of taxation should be discouraged. The petroleum profits tax act came into operation in 1958; no serious amendment has been made in the area of penalties. For more realistic approach penalties that will ensure effective compliance with the provisions of the act should be imposed, estimated tax should be doubled and imposed.

Under section 4 of the Petroleum Profits Tax Act losses incurred by the petroleum company during any previous accounting period shall be deducted from its assessable profits for any accounting period. Such deduction shall be made so far as possible from the amount, if any, of the adjusted profit of the first accounting period after that in which the loss was incurred and any balance can then be carried forward to the next succeeding accounting period until it is completely wiped out within five months after the end of any accounting period of a petroleum company or within such further time as the Board may permit in writing in any instance, the

company may elect in writing that a deduction of any loss or any part thereof shall be deferred to and be made in the succeeding accounting period until the full amount is wiped out. In other words a petroleum company can elect to carry forward its losses to the next accounting period even though it has sufficient profits in the current accounting period to relieve such losses. One does not see the justification for this to deprive the Government of the revenue needed for social and economic development of the country.

The aspect of enforceability of the Act is another vital area where the government ought to take extra measures. The agency responsible for the enforcement of oil regulations is the Department of Petroleum Inspectorate. To effectively combat crime, the personnel has to be properly trained and equipped but this is far cry from the reality. They are not properly founded. The caliber of staff again matters, checks in the form of constant air and land surveillance on pipelines are not done especially now that the issue of oil bunkering is a re-occurring phenomenon. These administrative lapses should be promptly corrected.

3. Conclusion

In spite of the effect of the Petroleum Profits Tax on foreign investors, many of them made huge profits. For instance Mobil Oil Nigeria in 1992 made after-tax profits of \$8.18million up from \$6million in 1991. According to Owen-Smith "The firm attained a turnover of \$68million, up from \$54.5million

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