



Tax Alert

FHC upholds FIRS' application of increased Tertiary Education Tax rate to full accounting period despite mid-year effective date

Background



Shell Exploration and Production Africa Limited (“Shell” or “the Company”) instituted an action at the Federal High Court to contest the Federal Inland Revenue Service’s (“FIRS” or “the Service”)¹ application of the increased Tertiary Education Tax (TET) rate of 3%, introduced by the Finance Act 2023 (FA 23) which was effective from 1 September 2023.

Prior to the Finance Act 2023, section 1(2) of the Tertiary Education Trust Fund (Establishment) Act (TET Act) prescribed a TET rate of 2.5% of assessable profit. The Finance Act amended the rate to 3% effective 1 September 2023. The Company computed TET at 2.5% for income earned from 1 January to 31 August 2023, and 3% for income earned from 1 September to 31 December 2023.

However, during the filing on TaxPro Max, the system applied a flat 3% rate to the entire 2023 accounting period. Shell argued that the Service wrongly applied the 3% rate retrospectively to income earned between 1 January and 31 August, 2023 and sought a court order declaring the additional payment unlawful and requesting a refund or tax credit.

Company's arguments

Shell argued that:

The FIRS' assessment and retroactive application of the increased TET rate of 3% was unlawful and infringed on the Company's vested right to the previously applicable lower rate of 2.5% on income earned before the effective date and was contrary to the provisions of the Finance Act 2023. Shell contended that the TET rate increase should only apply prospectively from its effective date.²

¹ Now known as the Nigeria Revenue Service (NRS)

² Shell Exploration and Production Africa Limited v. Federal Inland Revenue Service (SUIT NO: FHC/L/CS/2341/24)

FIRS' Arguments



The FIRS' arguments were:

- The TET is an annual tax computed on the accounting period of a company, which is defined in the Companies Income Tax Act (CITA) and Petroleum Profits Tax Act (PPTA). The accounting period typically runs from 1 January to 31 December and the rate in force at the end of the accounting period should apply to the entire accounting period without proration.
- FA 2023 amended only the rate of tax and not the statutory framework governing accounting

periods or assessable profits and there is no legal basis in statute or precedent for dividing or prorating the accounting year as Shell had attempted to do. They relied on the established case law of *Unipetrol v. Edo State Board* to emphasise that the accounting period is a legal unit that cannot be fragmented.

- The application of the increased rate to the entire year's profits is lawful and does not constitute retrospective taxation, as the tax is computed annually on the assessable profit for the full year.³

FHC's decision



The Court held that the TET is an annual tax based on a company's entire accounting period and must be computed on a full-year basis, without proration. As such, the tax base cannot be divided into pre and post amendment segments. The Court found no statutory provision in the TET Act, CITA, or PPTA that allows different rates to be applied to portions of the same accounting year. Since the Finance Act 2023 made the 3% rate effective from 1 September 2023 and the Company's accounting year ended on 31 December 2023, the Court determined that the 3% rate applied to the entire 2023 year. Furthermore, the Court emphasised that annual taxes crystallise only at year-end, and therefore, the FIRS'

application of the 3% rate was not retroactive.

The Court rejected the argument that income earned before the new rate took effect created a protected right to the earlier rate. It reasoned that no TET liability arises until the close of the accounting period, and therefore no vested rights were interfered with.

The Court also distinguished this case from **Accugas v. FIRS**, noting that the Accugas case involved the introduction of a new minimum tax regime applied to a completed period, whereas the present case deals with a rate change to an existing annual tax within an ongoing accounting period. As such, the Court found no conflict between the two decisions.

Analysis and Takeaway



The FHC's position that a basis period cannot be fragmented raises concerns around the relevance of effective dates in Nigeria's income tax framework. The judgment implies that tax laws enacted at any point during a financial year could potentially affect the full year's profits, notwithstanding the stated commencement date. The inconsistent application would mean that companies with different accounting year-ends, such as a 30 June year-end, end up with a different result simply because their year closes earlier.

There may be an argument based on Section 29(6) of CITA for the proration of profits. This section allows profits to be split proportionally across different periods unless the FIRS decides otherwise. This provision provides a legal basis for time-based proration in Nigeria's tax system in situations like changes in accounting dates, commencement or cessation of business, or other cases such as where economic activity cuts across different tax periods.

Analysis and Takeaway cont.



Although TET is governed by its own Act, the tax is still assessed using the same accounting period applied for CIT and PPT purposes. One could reasonably expect that where income spans two different statutory rates, as was the case when the Finance Act fixed 1 September 2023 as the date for the rate increase, Section 29(6) could provide interpretive support for proration.

Combining this interpretation with the Accugas ruling where the Courts emphasized that statutes cannot apply retroactively, and that taxpayers are liable only according to the law in force when the income was earned, there may be a basis to argue that

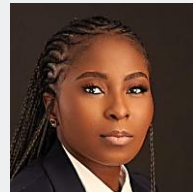
income earned before the effective date of a rate change should not be subjected to the higher rate.

In conclusion, although the Court applied a strict reading of the TET Act which makes things more straightforward for the Service, it also exposes the need for clearer laws on how effective dates should apply to annual taxes, especially in periods of fiscal transition. Taxpayers should pay closer attention to their accounting-year choice, how mid-year rate changes might affect them, and what this judgment could mean for future policy updates, including the application of the Nigeria Tax Act.

For a deeper discussion, please contact



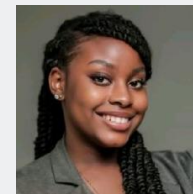
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