

The Excess Dividend Tax Judgments

Could the Courts have applied the wrong Rules of Statutory Interpretation?



...section 19 is an absurdity, an inconvenience to taxpayers and inconsistent with the general intention of CITA (another rule of interpretation is that a statute must be read as a whole).

By Folajimi Olamide Akinla

Understanding or interpreting the provisions of any law can be confusing, challenging and difficult. If you are in doubt ask different people what '*basic food item*' under the Value Added Tax Act means and see if they all arrive at the same conclusion. To interpret the phrase, you will have to define what 'basic' is and bear in mind, 'basic' can be relative. Then you must decide what a 'basic food' means – for example as between cassava and garri, which is basic? Can one be more basic than the other? Does processing deprive a food item from being basic? What level of processing is permissible etc? Whatever interpretation is accepted would have its own consequences.

However, all hope is not lost. There are rules – Rules of Statutory Interpretation – that can be applied to interpret provisions of any law. The outcome of a case can be largely dependent on the rule applied. Let's consider some of these rules and how they could have been applied in a recent decision of the Federal High Court [FHC]¹ to arrive at a different conclusion.

Principles of Implied Repeal and Implied Exception

Generally, repealing or amending a law is a deliberate legislative act. However, there are instances where a new law, not intended to repeal a former one, conflicts with that former, such that both cannot be read in unity. In such instances,

the new law is said to have impliedly repealed the former.

The principle is, however, subject to another rule of statutory interpretation – *generalia specialibus non derogant*. Forget the jargon, it means ‘a general law cannot overrule a specific one’. It is sometimes called Principle of Implied Exception. We’ll come back to this.

Literal rule and its exceptions

Where, in interpreting a statute, the words are plain, clear and unambiguous they must be given their natural and ordinary meaning. However, this rule is also subject to another rule – the Golden Rule – which means that where the natural and ordinary meaning results in an absurdity, inconsistency and inconvenience then the literal meaning should be abandoned for an interpretation that best expresses the intention of the lawmakers. Other exceptions are the Mischief and Purpose rules. We’ll come back to these later.

Facts of the case

The taxpayer paid dividends to shareholders which exceeded its total profits for the years 2005 - 2007. Its case was that the dividends were paid from retained earnings which had suffered tax in prior years. The Federal Inland Revenue Service [FIRS], relying on section 19 of the Companies Income Tax Act [CITA] imposed tax at 30% on the excess dividends as though they were profits. Essentially section 19 imposes tax on dividends, as though they are profits, when the dividends paid exceed a company’s total profits. The section 19 tax is informally referred to as Excess Dividend Tax [EDT].

¹ Dividends received by one company from another which have suffered tax (usually by way of a withholding tax) before paid to the recipient company.

The taxpayer appealed and lost at the Tax Appeal Tribunal [TAT]. On appeal to the FHC, two questions came up for determination:

- a) Whether dividends paid from retained earnings could be subject to EDT and
- b) Whether franked investment income [FII]² which is exempt under section 80 of CITA should be liable to EDT.

Application of the rules

In answering the first question, the FHC, applying the literal rule, held:

It bears repeating that by the unambiguous provision of Section 19, that section does not look at the source of the dividend or whether that source has been taxed in the previous year or not....

In resolving the second question, the FHC, applying the principle of implied repeal held:

This court agrees Section 19 being later in time than Section 80 (3) must prevail over the latter Section by trite rule of statutory interpretation....

The rationale behind this principle is that the provision that is later in time constitutes the new legal order and conforms more with changing times and circumstances and so gains judicial precedence over the old provision...where a conflict can be seen between an old law and a new one...the second repeals the first.... Section 80 (3) is subordinate to section 19.

The decision throws up a couple of questions:

- a) Did the FHC rightly apply the principle of implied repeal or should it have considered the exception to the rule?

- b) Rather than applying the literal rule, did the FHC consider the intention of section 19 or the mischief it sought to cure?
- c) Did the FHC actually apply the principle of implied repeal to repeal section 80 (3) or did it simply conclude that section 80 (3) is subordinate to section 19?

In answering these questions:

Implied Repeal or Implied Exception?

I promised to come back to this. The exception to the principle of Implied Repeal is another rule of interpretation - a general law cannot overrule a specific one. This rule is also referred to as the 'Implied Exception'.

To explain this, there is no implied repeal of an earlier legislation containing specific provisions on a subject by a latter legislation containing general provisions on the same subject. The effect is that the earlier specific legislation is an exception to the more general legislation. Applying the principle of implied exception to sections 19 and 80 (3):

Section 80 (3), is an earlier provision specifically for taxation of FII while section 19, the latter provision, is a general anti-avoidance provision applicable to all dividends on which no tax has been paid. In other words, **section 80 (3), a specific provision would apply to all FII while section 19, the more general provision would apply to profits paid as dividends on which no tax has been paid.**

Therefore, section 80 (3) being an implied exception to section 19 would not be repealed by or be subordinate to section 19.

Literal Rule or the exceptions?

The FHC applied the literal rule by giving section 19 its ordinary meaning. However, applying the literal rule may have resulted in absurdity, inconvenience and inconsistency since CITA does not promote or advocate double taxation. In cases where double taxation is identified, it attempts to provide relief.

Therefore, it is arguable that double taxation occasioned by the literal interpretation of section 19 is an absurdity, an inconvenience to taxpayers and inconsistent with the general intention of CITA (another rule of interpretation is that a statute must be read as a whole).

Perhaps, if the FHC had abandoned the literal rule in construing the provisions of section 19 and tried to discover the intention of the lawmakers (Golden Rule) or the mischief section 19 sought to cure (Mischief Rule) or the purpose for which section 19 was inserted in the law (Purposive Rule), the outcome of the case would be different. Any of these could have been achieved through a review of legislative notes or Hansard at the time of including section 19 into the law etc.

Did the FHC conclude that section 80 (3) has been repealed by section 19?

After relying on decisions³ of appellate courts it appeared the FHC came to a decision that section 80 (3) had been impliedly repealed even though it did not make a specific pronouncement to that effect. Instead it concluded that *Section 80 (3) is subordinate to section 19.*

This conclusion creates some uncertainty as to the fate of section 80 (3). Assuming the section was repealed, FII would no longer enjoy protection from further tax upon re-distribution. This would result in multiple taxation as the same income would be taxed every time there is a re-distribution.

Conclusion

Most tax disputes arise from differences in the interpretation of tax laws. Convincing a Tribunal or Court that one's interpretation is the right one requires an understanding and mastery of the

rules. A Tribunal or Court would need to evaluate all Rules of Statutory Interpretation brought to its attention during a case because whatever decision reached would have consequences. The immediate effect of this decision is a potential tax charge of 60% (as opposed to 30%) on companies. This makes Nigeria less attractive for business, increases capital flight, results in loss of jobs and ultimately less taxes for the government. On the flip side, if the Court had considered the exceptions (assuming they were brought to its attention), the outcome may have resulted in different, but positive, consequences.

Folajimi O. Akinla is a Tax Lawyer in the Tax and Regulatory Services Unit at PwC Nigeria. He specialises in Transfer Pricing and Tax Dispute Resolution.

Visit our tax blog for in-depth analyses, unique insight and superlative perspective on tax matters: **www.pwcnigeria.typepad.com**. *Subscription is free!*

About PwC

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 157 countries with more than 223,000 people who are committed to delivering quality in assurance, advisory and tax services. Find out more and tell us what matters to you by visiting us at www.pwc.com.