



KAMPALA INTERNATIONAL UNIVERSITY  
**LAW JOURNAL**

KIULJ Vol.4 Issue 2,2022



**KAMPALA  
INTERNATIONAL  
UNIVERSITY  
LAW JOURNAL**

**(KIULJ)**

*KIULJ. VOL 4, ISSUE 2, 2022*

**KAMPALA INTERNATIONAL UNIVERSITY LAW JOURNAL (KIULJ)**

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Journal of School of Law, Kampala International University, Kampala, Uganda

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**ISSN: 2519-9501(Print)**

**ISSN: 2519-9528(Electronic)**

**Published by:**

School of Law  
Kampala International University  
P.O. Box 20000 Kampala  
Kampala  
Uganda

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**Citation**

This Journal may be cited as *KIULJ Vol 4, Issue 2, 2022*.

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The primary objective of the **KAMPALA INTERNATIONAL UNIVERSITY LAW JOURNAL (KIULJ)** is to provide as platform for a robust intellectual discourse, through the publication of incisive and insightful articles and other contributions from a variety of scholars, jurists and practitioners across jurisdictions. The desire to accomplish this objective guides the choice of the materials being presented to the reading public in every edition. The peer review and editing processes of the papers that are finally selected for publication are equally influenced largely by the pursuit of this goal.

To this end, articles from seasoned scholars and practitioners in each edition address a wide spectrum of issues from different branches of the law, such as, International Criminal Law, Law of International Institutions, Environmental Law, Human Rights Law, Medical Law, Oil and Gas Law, Constitutional Law, Corporate Governance to mention but a few. You will, no doubt, find these scholarly works a worthy contribution to knowledge in their respective fields.

On behalf of the Editorial Board, I wish to appreciate all our reviewers, internal and external, for their constructive criticisms, comments and suggestions. These go a long way to enrich the quality of the papers published in this Journal. The various contributors who painstakingly addressed the observations and suggestions of the reviewers, thus facilitating the achievement of the purpose of the review process also deserve our commendation.

We also, with a grateful heart, acknowledge the interest our teeming readers have continued to show in the succeeding editions of the journal just as we assure them of our readiness to give them the best always. We equally thank our editorial consultants for their useful advice and comments that have contributed to the continuous improvement of the quality of the journal. Legal practitioners and scholars are hereby informed that contributions to our journal are received on a rolling basis. They should feel free to send in their manuscripts and ensure they comply with the submission guidelines as spelt out in the Call for Papers obtainable from the journal's website ([www.kiulj.kiu.ac.ug](http://www.kiulj.kiu.ac.ug)). All contributions should be addressed to the Editor-in-Chief and forwarded to the email addresses supplied in this edition.

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# LEGAL MECHANISMS TO COUNTER TAX AVOIDANCE IN NIGERIA

ISAU OLATUNJI AHMED, Ph.D.\*

## Abstract

*Taxation is one of the major sources from which the Nigerian government generates its revenue which is by levying taxes on individuals, corporate entities, goods and services. However, over the years, the Nigerian government's revenue generation efforts through taxation have been hindered and impeded by the issue of tax avoidance. Tax avoidance, alongside other concepts such as tax evasion and tax planning, has been described as fiscal termites eating away the potential tax revenue of government. Unlike tax evasion and tax planning which are generally considered to be illegal and legal respectively, there is no such clear cut classification for tax avoidance thereby posing a serious threat to the government's revenue generation efforts. The magnitude of potential revenue lost to the menace of tax avoidance necessitated the need for the government to put in place legal mechanisms and measures to prevent tax avoidance. The objective of this article is to examine the concept of tax avoidance and its underlying incentives. The article also examines the impact of tax avoidance and as well as the legal mechanisms to counter it. The article is a library based research that made use of primary and secondary materials such as the constitution, tax legislations, case laws, journal, textbooks, dissertations and theses. The finding of the article revealed that the legal mechanisms to counter tax avoidance in Nigeria are currently inadequate and it recommended that the legal mechanisms be strengthened for them to be effective.*

**Keyword:** Taxation, Tax Avoidance, Revenue loss, legal mechanisms.

## Introduction

Taxation is now generally regarded as an important source of revenue generation for the Nigerian government.<sup>1</sup> This is due to the fact that, through taxation, the government is able to raise a significant amount of revenue to meet its needs and provide basic amenities for its citizens. In Nigeria, the government of the country through its revenue agency, Federal Inland Revenue Service (FIRS) generated about 1.97 trillion Naira (5 billion US dollars) through taxation in the first half of 2015 which represented 98% of the targeted revenue of 2.28 trillion Naira (7 billion US

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<sup>1</sup> Rotimi O. and Udu S. A., 'Revenue Generation and Engagement of Tax Consultants in Lagos State, Nigeria: Continuous Tax Evasion and Irregularities' (2003) 1(10) European Journal of Business and Social Sciences 2.

dollars) for January and June 2015.<sup>2</sup> Likewise, in the year 2018, the government disclosed that it generated 5.320 trillion Naira (13 billion US dollars) from taxation.<sup>3</sup> This was said to be the highest revenue generated from taxation in the history of Nigeria as at 2018.<sup>4</sup>

However, in recent times, the government's revenue generation efforts from taxation have been impeded by certain fiscal resistant such as tax avoidance which has resulted in huge revenue loss to the government. According to the Global Financial Integrity<sup>5</sup>, close to 100 billion US dollars per year is lost in revenue to tax avoidance in developing countries.<sup>6</sup> Another report compiled by Christian Aid estimates that revenue lost to the menace of tax avoidance each year in developing countries could rise 160 billion US dollars.

The magnitude of potential revenue lost to tax avoidance is having a significant negative impact on the government which requires revenue to improve essential services to its citizens.<sup>7</sup> This has made the government to pay closer attention to the issue of tax avoidance which has the potential of the depriving the government of the revenue needed to cater for the citizens.<sup>8</sup>

Apart from tax avoidance, tax planning and tax evasion contribute to loss of revenue to the government. However, unlike tax planning and tax evasion which are generally classified under various tax laws as being legal and illegal respectively, there is no clear cut classification of tax avoidance as being legal or illegally thereby making its regulation difficult for the government. It therefore becomes important to examine the concept of tax avoidance to determine its legality or otherwise.

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<sup>2</sup> Premium Times, 'FIRS realises N1.97trillion revenue', *Premium Times Newspaper* (Lagos 10 August 2015) <<http://www.premiumtimesng.com/business/banking-and-finance/188103-firs-realises-n1-97trillion-revenue.html>> accessed on 15 April 2022.

<sup>3</sup> Oladeinde Olawoyin, 'FIRS generates N5.3 trillion in 2018, highest in Nigeria's history-Official' (Lagos 8 January 2019) <<https://www.premiumtimesng.com/news/headlines/304675-firs-generates-n5-3-trillion-in-2018-highest-in-nigerias-history-official.html>> accessed on 15 May 2022.

<sup>4</sup> Ibid.

<sup>5</sup> Global Financial Integrity (GFI) is a non-profit, Washington, DC-based research and advisory organization, which produces high-caliber analyses of illicit financial flows, advises developing country governments on effective policy solutions, and promotes pragmatic transparency measures in the international financial system as a means to global development and security <<http://www.gfintegrity.org/about/>> accessed on 15 April 2022.

<sup>6</sup> World Finance Magazine, 'The true costs of tax avoidance' <<http://www.worldfinance.com/strategy/the-true-costs-of-tax-avoidance>> accessed on 15 April 2022.

<sup>7</sup> Christian Aid, 'Death and taxes: The true toll of tax dodging' <<http://www.christianaid.org.uk/images/deathandtaxes.pdf>> accessed on 13 March 2022.

<sup>8</sup> Tanzi V., 'Globalization, Technological Developments and the works of Fiscal Termites' International Monetary Fund Working Paper 2000, <<http://www.imf.org/external/.../wp00181.pdf>> accessed on 13 May 2022.

## **The Concept of Tax Avoidance**

There is no fixed legal, legislative or statutory definition/meaning of tax avoidance owing to the difficulty of framing an exhaustive definition to cover the concept which makes a precise definition unlikely.<sup>9</sup> In order to provide an understanding of the concept of tax avoidance, this article will consider definitions provided by various scholars, tax commissions as well as the definitions contained in various judicial pronouncements on the concept.

Garner and Henry<sup>10</sup> define tax avoidance as the ‘act of taking advantage of legally available tax planning opportunities in order to minimize one’s tax liability’. This definition portends that tax avoidance occurs when a person arrange his affairs in such a way as to take advantage and/or exploit the tax law to minimize his tax liability. This definition implies that tax avoidance could be legal in nature.

The ‘Radcliffe Commission’ defined tax avoidance as ‘some acts by which a person so arranges his affairs that he is liable to pay less tax than he would have paid but for the arrangement’.<sup>11</sup> A similar definition is given by Carter Commission which defined tax avoidance as every attempt by legal means to reduce tax liability which would otherwise be incurred by taking advantage of some provisions or lack of provision in the law.<sup>12</sup>

The Organization for Economic Co-operation and Development (OECD) defined tax avoidance as one that is generally used to describe the arrangement of a taxpayer's affairs that is intended to reduce his tax liability and that although the arrangement could be strictly legal it is usually in contradiction with the intent of the law it purports to follow.<sup>13</sup> The Review of Business Taxation defined tax avoidance as a misuse or abuse of the law that is often driven by the exploitation of structural loopholes in the law to achieve tax outcomes that were not intended by Parliament but also includes the manipulation of the law and a focus on form and legal effect rather than substance.<sup>14</sup>

Wheatcroft defines tax avoidance as the art of dodging tax without actually breaking the law, or alternatively, the right of every citizen to structure ones affairs

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<sup>9</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management* (2<sup>nd</sup> ed. Stirling-Horden Pub. Ltd. Ibadan 2013).

<sup>10</sup> Garner B. A. and Henry C. B., *Black’s Law Dictionary* (9<sup>th</sup> ed., St. Paul MN-West, 2009).

<sup>11</sup> The Royal Commission on Taxation of Profits and Income, United Kingdom, 1955 para 1016.

<sup>12</sup> Royal Commission on Taxation (The Carter Commission) 1966 Canada.

<sup>13</sup> The Organization for Economic Co-operation and Development (OECD) Glossary of Tax Terms <<http://www.oecd.org/ctp/glossaryoftaxterms.html>> accessed on 14 April 2022.

<sup>14</sup> Second Reading Speech, Income Tax Laws Amendment Bill (No. 2) 1981, Hansard, House of Representatives, 27 May 1981.

in a manner allowed by law, to pay no more than what is required.<sup>15</sup> Ulph also defined tax avoidance as the use of artificial or contrived methods of adjusting taxpayers' social, economic or organizational affairs to reduce their tax liability in accordance with the law while not affecting the economic substance of the transactions.<sup>16</sup>

The Courts have also had the opportunity to give succinct interpretation to the concept of 'tax avoidance'. This usually arises from cases coming before them on the grounds of contravention of sections in the tax law which are usually referred to as an anti-avoidance provision.<sup>17</sup> However, courts in Nigeria and the United Kingdom have adopted different approaches to the interpretation of tax avoidance and this has resulted in different meaning and definitions of the term.<sup>18</sup> The obvious result of this is that different approaches by the courts in interpreting tax law have resulted in different classification of transaction and as such, inter-country comparisons in this respect have proved fruitless in the search for common meaning of the concept of tax avoidance.<sup>19</sup>

One of the clearest definitions of tax avoidance was provided by Lord Nolan in his judgment in the *Willoughby case*<sup>20</sup>, which also very succinctly seeks to draw a line of distinction between tax avoidance and tax planning where he stated as follows:

*The hall mark of tax avoidance is that the taxpayer reduces his liability to tax without incurring the economic consequences that Parliament intended to be suffered by any taxpayer qualifying for such reduction in his tax liability. The hall mark of tax mitigation, on the other hand, is that the taxpayer takes advantage of a fiscally attractive option afforded to him by the legislation, and genuinely suffers the economic consequences that Parliament intended to be suffered by those taking advantage of the option.*

From the above definition given by Lord Nolan, it is clear that there is a difference between tax avoidance and tax planning. Tax avoidance occurs when a taxpayer reduces his tax liability in a manner not intended by the tax law while tax planning is a reduction of tax liability in manner approved by the tax law

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<sup>15</sup> Wheatcroft G.S.A- 'The attitude of the Legislature and the Courts to tax avoidance', (1955) 18 (3) Modern Law Review 209.

<sup>16</sup> Ulph D., *Managing Tax Risks in Beyond Boundaries: Developing Approaches to Tax Avoidance and Tax Risk Management* (Freedman J. eds) Oxford University Centre for Business Taxation 101-115.

<sup>17</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management*, (2<sup>nd</sup> ed. Stirling-Horden Pub. Ltd. Ibadan 2013) 109.

<sup>18</sup> *Ibid* 109.

<sup>19</sup> *Ibid* 109.

<sup>20</sup> *CIR v Willoughby* [1997] 4 All ER 65 at p.73, See also the case of *CIR v Challenge Corp Ltd* [1986] S.T.C. 548.

Furthermore, Lord Templeman in the *Challenge Corporation case*<sup>21</sup> noted that:

*Income tax is avoided and a tax advantage is derived from an arrangement when the taxpayer reduces his liability to tax without involving him in the loss or expenditure which entitles him to that reduction. The taxpayer engaged in tax avoidance does not reduce his income or suffer a loss or incur expenditure but nevertheless obtains a reduction in his liability to tax as if he had*

Tax Avoidance is further defined by the European Court of Justice as wholly artificial arrangements which are designed to obtain a tax advantage which are aimed at circumventing tax laws.<sup>22</sup> The Nigerian case of *Akinsete Syndicate V. Senior Inspector of Income Tax*<sup>23</sup> provided an insight into the meaning of tax avoidance. The court held that tax avoidance by lawful means is acceptable even though the Court did not state which category of tax avoidance by lawful means is not acceptable.<sup>24</sup>

The above definitions of the concept of tax avoidance are indicative of the fact that is not entirely illegal as it involves the legal exploitation of the tax system to reduce tax liability. Even though this legal exploitation is not fraudulent in nature, the results of such legal exploitation are considered immoral, improper, abusive and against the spirit of the tax law. It can therefore be postulated that tax avoidance is an exploitation of the fiscal legislation in a manner not intended by the legislature.

Accordingly, while a person has the right to arrange his affairs in order to reduce his tax liability, where such person embarks on an artificial arrangement for the purpose of escaping and reducing tax liability otherwise due, such an arrangement may not be socially acceptable.<sup>25</sup> Thus, a manipulative transaction which has the effect of artificially reducing tax liability would be disallowed for being a tax avoidance scheme.<sup>26</sup>

It is important to note however that it is not all the activities of taxpayers towards reducing or minimizing their tax liability that will amount to tax avoidance. While tax avoidance is an example of tax minimization, other examples of tax minimization are tax evasion and tax planning. Although, these labels (tax

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<sup>21</sup> *CIR (NZ) v Challenge Corporation Ltd*, [1987] AC 155.

<sup>22</sup> *Imperial Chemical Industries Plc (ICI) v Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)* (1998) ECR I-4695.

<sup>23</sup> *Akinsete Syndicate V. Senior Inspector of Income Tax* F.S.C 164/66 (Unreported).

<sup>24</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management*, (2<sup>nd</sup> ed. Stirling-Horden Pub. Ltd. Ibadan 2013) 109.

<sup>25</sup> *Ibid.*

<sup>26</sup> *Ibid.*



avoidance, tax planning and tax evasion) are not used universally, they have been accepted internationally by the International Academy of Comparative Law at its 18<sup>th</sup> congress in Washington in 2010.<sup>27</sup>

The distinction among tax avoidance, tax planning and tax evasion can be viewed as a partially overlapping legal spectrum of tax minimizing behaviour.<sup>28</sup> At one end is tax evasion which is illegal and criminal in nature. Tax planning, at the other end of the spectrum, is tax minimization behaviour that the government is aware of and allows to continue.<sup>29</sup> In some instances the government may even encourage it.<sup>30</sup> Tax avoidance on the other hand lies between the two, exploiting the tax law while denying its substance.

### **Features of Tax Avoidance Transactions**

There is no consensus as to what makes a transaction to constitute tax avoidance in nature. However, there are some laid down features that determines whether a transaction constitute tax avoidance. These feature revolve around the notions of ‘form’, ‘purpose’ and ‘policy’<sup>31</sup> These are briefly discussed below:

#### **i. Form**

The first feature to identify tax avoidance is the ‘form’ of the transaction. ‘Form’ generally refers to the legal relationships that gives legal structure to transactions through which taxpayers achieve desired economic results which is the ‘economic substance’ of the transactions.<sup>32</sup> The form approach identifies the economic outcome of a transaction and concludes that tax avoidance occurs when the taxpayer secures an economic outcome that avoids the normative tax treatment intended by Parliament.<sup>33</sup> Thus, where a taxpayer sets up an artificial or contrived transaction or scheme merely for the purpose of minimizing its tax liability, such transaction or scheme will amount to tax avoidance.<sup>34</sup>

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<sup>27</sup> Brown B. K. and Snyder D.V., ‘General Report Regulation of Corporate Tax Avoidance’ <<http://www.link.springer.com/content/pdf/bfm%3A978-94-007-2354-2%2F1.pdf>> accessed on 15 April 2022

<sup>28</sup> Prebble B.C., ‘Should Tax Avoidance be Criminalised? Tax Avoidance and Criminal Law Theory’ (LL.B Dissertation, University of Otago 2011) 20.

<sup>29</sup> Ibid.

<sup>30</sup> Example are some of tax incentives such as Pioneer Status under the Industrial Development (Income Tax Relief) Cap I 7 LFN 2004, The Nigerian Liquefied Natural Gas (NLNG) (Fiscal Incentives, Guarantees and Assurances) Act Cap. N8 7 LFN 2004 and so on.

<sup>31</sup> Cooper G. S., Tax Avoidance and the Rule of Law (IBFD Publications BV, Amsterdam 1997) 28.

<sup>32</sup> Taylor M. D., Tax Policy and Tax Avoidance: The General Anti-Avoidance Rule from a Tax Policy Perspective (LLM Dissertation, University of British Columbia 2006) 37.

<sup>33</sup> Ibid 38.

<sup>34</sup> Ibid 38.

However, it is to be noted that it is not all transactions or schemes aimed at minimizing tax liability that constitute tax avoidance. A transaction or scheme, even if its legal form is artificial and contrived in nature, could be justified for business reasons.<sup>35</sup> In addition, there are situations where tax legislations often encourage taxpayers to use artificial and contrived legal forms as an incentive to achieve particular economic outcomes by suspending the normal tax consequences of those outcomes.<sup>36</sup> Accordingly, taxpayers taking advantage of such incentives cannot be viewed as engaging in tax avoidance merely because they have chosen contrived, tax-preferred legal forms for their economic activities.<sup>37</sup> It can only be said that they are merely engaging in permissible tax planning/mitigation<sup>38</sup>.

## ii. Purpose

The second feature of tax avoidance focuses on the underlying purpose of the transaction. This means that where a taxpayer engages in transactions for the purpose of reducing its tax liability, the transaction will be deemed to constitute tax avoidance.<sup>39</sup> This approach is premised on the view that the underlying purpose of a transaction must have a real economic substance and not a mere artificial transaction whose only purpose is to minimize tax liability without real economic substance.<sup>40</sup>

A distinct advantage of a purpose-oriented approach is that the purpose of taxpayers' transactions are generally much easier to identify based on an objective.<sup>41</sup> It is therefore not surprising that most countries have adopted purpose-oriented approach in determining whether or not a transaction constituted tax avoidance. For example, the purpose-oriented approach was adopted by the United States of America Supreme Court in 1935<sup>42</sup> as a primary anti-avoidance rule<sup>43</sup>.

However, the purpose-oriented approach is not without its weaknesses. One is that, from a tax policy perspective, taxpayers' motives and purposes are sometimes not relevant to the taxation of their transactions.<sup>44</sup> This is because tax result from

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<sup>35</sup> Cooper G. S., *Tax Avoidance and the Rule of Law* (Amsterdam: IBFD Publications BV, 1997) 30.

<sup>36</sup> Arnold B. & Wilson J., 'The General Anti-Avoidance Rule - Part II' (1986) 36(5) *Canada Tax Journal* 1144.

<sup>37</sup> *Peterson v. Commissioners of Inland Revenue* (2005) U.K. P. C. (P.C.) (Peterson).

<sup>38</sup> *CIR v Willoughby* [1997] 4 *All ER* 65 at p.73. See also the case of *CIR v Challenge Corp Ltd* [1986] *S.T.C.* 548.

<sup>39</sup> Taylor M. D., *Tax Policy and Tax Avoidance: The General Anti-Avoidance Rule from a Tax Policy Perspective* (LLM Dissertation, University of British Columbia 2006) 39.

<sup>40</sup> *Ibid* 39.

<sup>41</sup> Arnold B., 'In Praise of the Business Purpose Test', in Report of the Proceedings of the Thirty-Ninth Tax Conference, 1987 Conference Report (Toronto: Canadian Tax Foundation, 1988)

<sup>42</sup> *Gregory v. Helvering*, 293 *U.S.* 465 (1935).

<sup>43</sup> Taylor M. D., *Tax Policy and Tax Avoidance: The General Anti-Avoidance Rule from a Tax Policy Perspective* (LLM Dissertation, University of British Columbia 2006) 41.

<sup>44</sup> Arnold B., 'In Praise of the Business Purpose Test', in Report of the Proceedings of the Thirty-Ninth Tax Conference, 1987 Conference Report (Toronto: Canadian Tax Foundation, 1988).

objective economic circumstances and not from taxpayers' purposes for their transactions. The exception to this is where legislation may make purposes relevant, such as when distinguishing between business and personal expenses.<sup>45</sup>

A more significant problem with the purpose-oriented approach relates to the numerous tax expenditure provisions that encourage certain activities by granting tax reductions and incentives at the expense of tax law's primary purpose of raising revenue.<sup>46</sup> This serves as an incentive to taxpayers to engage in certain transactions in order to obtain those tax incentives even without an underlying non-tax purpose<sup>47</sup>.

### iii. Policy

The third feature of tax avoidance is the policies underlying the tax legislation. Under this approach, tax avoidance occurs when taxpayers obtain tax results not intended by the tax legislation or when transaction defeats the policy underlying the tax legislation.<sup>48</sup> This approach has been articulated in a number of different ways. For example, the UK Tax Law Review Committee (TLRC) described tax avoidance as any action taken to reduce or defer tax liabilities in a way that Parliament plainly did not intend or could not possibly have intended had the matter been put to it.<sup>49</sup>

The policy-based approach is premised on the idea that the underlying policy of a tax legislation should not be defeated by the tax outcome of a transactions. Thus, from a tax policy perspective, the focus is to ensure that a transaction complies with the fiscal and economic policies underlying the tax legislation.<sup>50</sup> This approach also allows for tax mitigation/planning because it acknowledges that some tax-reduction transactions actually accord with the purpose of the legislation.<sup>51</sup>

The disadvantage of this approach is that it can sometimes be extremely difficult to clearly identify a policy underlying tax legislation. This is because determining the

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<sup>45</sup> Ibid 42.

<sup>46</sup> Example of these are the allowances provided under the Second Schedule to the Companies Income Tax Act CAP C.21 LFN 2004, Pioneer Status under the Industrial Development (Income Tax Relief) Cap I 7 LFN 2004, The Nigerian Liquefied Natural Gas (NLNG) (Fiscal Incentives, Guarantees and Assurances) Act Cap. N8 7 LFN 2004 and so on.

<sup>47</sup> See the Canadian case of *Stuart Investments Ltd. v. R.*, 84 D.T.C. 6305 at 6324.

<sup>48</sup> Taylor M. D., Tax Policy and Tax Avoidance: The General Anti-Avoidance Rule from a Tax Policy Perspective (LLM Dissertation, University of British Columbia 2006) 43.

<sup>49</sup> The Institute of Fiscal Studies Tax Law Review Committee <<http://www.ifs.org.uk/comms/comm64.pdf>> accessed on 15 April 2022.

<sup>50</sup> Taylor M. D., Tax Policy and Tax Avoidance: The General Anti-Avoidance Rule from a Tax Policy Perspective (LLM Dissertation, University of British Columbia 2006) 45.

<sup>51</sup> Cooper G. S., Tax Avoidance and the Rule of Law (IBFD Publications BV, Amsterdam 1997) 31.

parliament intention can sometimes be problematic to the courts.<sup>52</sup> Requiring the courts to go behind a legislation to deal with questions of underlying policies of the legislation may sometimes be impractical<sup>53</sup>. From the above, it is postulated that the features of a tax avoidance transaction are where:

- (a) the transactions result in a mismeasurement of taxpayers' economic income so that they pay less tax than they would have paid if they were taxed on their economic income;
- (b) the transactions are engaged in by taxpayers for the sole or primary purpose of obtaining such a tax benefit; and
- (c) the transactions result in an outcome not contemplated by policy underlying tax legislation.<sup>54</sup>

Thus, in identifying tax avoidance, attention should be on the means adopted to implement a particular arrangement, transaction or scheme. This means that the greater the degree of artifice, the more likely it is that the arrangement, transaction or scheme is of a kind which was not intended by the parliament.<sup>55</sup>

### **The Underlying Incentive for Tax Avoidance**

Various and diverge reasons have been attributed as serving as the incentives for taxpayers indulge in tax avoidance. These reasons can be classified into two categories.<sup>56</sup>

The first category comprises of factors that negatively affect taxpayers' compliance with tax legislation. These consist of low willingness to pay taxes (low tax morale), high costs to comply with tax laws, low quality of the service in return for taxes paid, lack of fairness and equity in the tax system, low transparency and accountability of public institutions, high level of corruption and lack of rule of law and weak fiscal jurisdiction.<sup>57</sup> The second category comprises reasons for the low ability of tax administration and fiscal courts to enforce tax liabilities. These factors can be summarized as resulting from insufficiencies in the administration and collection of taxes as well as weak capacity in auditing and monitoring tax payments which limit the possibility to detect and prosecute violators.<sup>58</sup>

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<sup>52</sup> Ibid 45.

<sup>53</sup> Ward D., 'The Business Purpose Test and Abuse of Rights' (1985) 1 British Tax Review 121.

<sup>54</sup> Brooks N., 'The Responsibility of Judges in Interpreting Tax Legislation' in Cooper G. S., *Tax Avoidance and the Rule of Law* (Amsterdam IBFD Publications BV, 1997) 96. See Rosenberg J. D., "Tax Avoidance and Income Measurement" (1988-1989) 87 Michigan Law Review 365.

<sup>55</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management*, (2<sup>nd</sup> ed. Stirling-Horden Pub. Ltd. Ibadan 2013) 113.

<sup>56</sup> The International Tax Compact (ITC), 'Addressing tax evasion and tax avoidance in developing countries' <[http://www.taxcompact.net/.../2011-09-09\\_GT](http://www.taxcompact.net/.../2011-09-09_GT)> accessed on 24 April 2022.

<sup>57</sup> Ibid.

<sup>58</sup> Ibid.

Apart from the above, several studies also indicate that taxpayers, such as corporate entities, make use of tax avoidance strategies as a way to increase their financial accounting earnings in order to boost their reputation and their share price.<sup>59</sup> This is why corporate leaders do not perceive tax avoidance as a problem often resulting from the fact that tax avoidance is not illegal like tax evasion.<sup>60</sup> For example, in defending Google's tax arrangements, which reportedly involved the (legal) transfer of 9.8 billion US dollars of revenues from international subsidiaries into Bermuda in 2011, Google Chairman, Eric Schmidt, reportedly stated, 'I am very proud of the structure that we set up. We did it based on the incentives that the governments offered us to operate'.<sup>61</sup>

Corporate leaders, in some other occasions, have viewed tax avoidance as obligatory and as part of their fiduciary duties to shareholders.<sup>62</sup> For example, in response to criticism of General Electric (GE)'s tax practices, GE's 2010 Citizenship Report emphasized that the company fully complies with the law and there are no exceptions but at the same time acknowledged that it has a responsibility to its shareholders to reduce its tax costs as the law allows.<sup>63</sup>

A study analyzing why a corporate tax executive would refuse to engage in tax avoidance strategies revealed that a majority (69.5%) of executives considered the potential harm to the company's reputation to be an important or very important factor in determining whether or not to adopt a tax avoidance strategy.<sup>64</sup> This means that the risk of harm to a company's reputation is more frequently cited consideration not to engage in tax avoidance than the risk of detection and challenge by the tax authority.<sup>65</sup>

Overall, many factors influence the decisions whether or not to engage in tax avoidance practices. On the whole, tax avoidance involves no more than the selection of a method of transaction which is least costly in tax as it conveniently involves the techniques by which the lawyers and the accountants can so arrange a

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<sup>59</sup> Graham J. R., 'Incentives for Tax Planning and Avoidance: Evidence from the Field 26' (MIT Sloan Research Paper No. 4990-12, 2013) <http://www.ssrn.com/abstract=2148407> m accessed on 22 March 2022.

<sup>60</sup> Fisher J. M., 'Fairer Shores: Tax Havens, Tax Avoidance, And Corporate Social Responsibility' (2014) 94 Boston University Law Review 348.

<sup>61</sup> Ibid 349.

<sup>62</sup> Ibid 349.

<sup>63</sup> General Electric Corporation, GE 2010 Citizenship Report 17 (2010) [http://www.ge.com/lu/en/docs/1315417188571\\_ge\\_2010\\_citizenship\\_report.pdf](http://www.ge.com/lu/en/docs/1315417188571_ge_2010_citizenship_report.pdf) accessed on 22 April 2022

<sup>64</sup> Fisher J. M., 'Fairer Shores: Tax Havens, Tax Avoidance, And Corporate Social Responsibility' (2014) 94 Boston University Law Review 349.

<sup>65</sup> Ibid 349.

client's affairs so as to achieve a reduction in the amount of tax he would otherwise have to pay.<sup>66</sup>

### **The Impact of Tax Avoidance in Nigeria**

Tax avoidance has a damaging effect on the economy as there is always the prospect of losing much needed revenue through it. For example, investigative reports indicated that Nigeria has been losing several billions of dollars in revenue every year due to tax avoidance activities by local and multinational corporations.<sup>67</sup> According to an investigative report by Premium Times, the Nigerian government lost about 23.187 billion Naira (700 million US dollars) to the tax avoidance activities of certain telecommunication operating in the country.<sup>68</sup> Furthermore, the recent announcement by the FIRS that Nigeria lost about 178 billion US dollars to tax avoidance between 2007 and 2017 is a confirmation that tax avoidance is on a continuous rise and it is gradually obliterating the revenue base of the country.<sup>69</sup>

However, it has been suggested that the adverse effect of tax avoidance on developing countries such as Nigeria is more damaging than that of developed countries.<sup>70</sup> According to research, the effects of tax avoidance on developed economies minimal because these countries have strong regulatory framework to checkmate and prevent the menace of tax avoidance.<sup>71</sup> On the other hand, developing countries are more susceptible to tax avoidance.<sup>72</sup> This is due to the lack of strong regulatory framework and administrative resources to tackle the issue of tax avoidance head on.<sup>73</sup> For example, in Nigeria, the lack of clarity on tax jurisdiction and lack of robust database management have prevented the government from tackling the issue of tax avoidance effectively.<sup>74</sup>

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<sup>66</sup> Abdulrazaq M. T. 'Judicial and Legislative Approaches to Tax Evasion and Avoidance in Nigeria' (1985) 29(1), *Journal of African Law* 65.

<sup>67</sup> Bakre O. M., 'Tax Avoidance, Capital Flight and Poverty in Nigeria: The Unpatriotic Collaboration of the Elite, the Multinational Corporations and the Accountants: Some Evidence' (Paper presented at the Tax Workshop, University of Essex, United Kingdom, July 2006).

<sup>68</sup> Emmanuel Mayah 'How MTN ships billions abroad, paying less tax in Nigeria' Premium Times Newspaper (Nigeria 26 October 2015) <<http://www.premiumtimesng.com/investigationspecial-reports/192159-investigation-how-mtn-ships-billions-abroad-paying-less-tax-in-nigeria.html>> accessed on 29 April 2022.

<sup>69</sup> James Emejo, 'FIRS: Nigeria lost ₦5.4tr to tax evasion by Multinationals' Thisday Newspaper (Nigeria 12 January 2021) <<https://www.thisdaylive.com/index.php/2021/01/12/firs-nigeria-lost-n5-4tn-to-tax-evasion-by-multinationals/>> accessed on 29 April 2022.

<sup>70</sup> Rushanara Ali, 'Tax avoidance hurts both Britain and developing countries', *Labour List Magazine* (United Kingdom, 9 February 2013) <<http://labourlist.org/2013/02/tax-avoidance-hurts-both-britain-and-developing-countries/>> accessed on 14 April 2022.

<sup>71</sup> Ibid.

<sup>72</sup> World Finance Magazine, 'The true costs of tax avoidance' <<http://www.worldfinance.com/strategy/the-true-costs-of-tax-avoidance>> accessed on 15 April 2022.

<sup>73</sup> World Finance Magazine, 'The true costs of tax avoidance' <<http://www.worldfinance.com/strategy/the-true-costs-of-tax-avoidance>> accessed on 15 April 2022.

<sup>74</sup> Aliyu A. O. and Kumai N. S., 'A conceptual review of Nigerian Tax Administration in Globalization and profit shifting challenges' <<https://www.scirp.org/journal/paperinformation.aspx?paperid=118746>> accessed on 9 September 2022.

The lack of strong regulatory framework therefore makes the impact of tax avoidance to be more acute in developing countries. This makes tax avoidance to have a direct life or death impact in developing countries bearing in mind that the tax revenue needed by the government to invest in essential services such as healthcare, education, and infrastructure is severely and negatively affected.<sup>75</sup> For some Non-Governmental Organizations like Save the Children,<sup>76</sup> the impact and effect of tax avoidance also constitute a political problem.<sup>77</sup> It is argued that the impact of revenue lost to tax avoidance has a direct impact not only on the quality of development but also on people's lives such as high mortality rate and health risks.<sup>78</sup>

It can therefore be posited that the negative effect of tax avoidance in developing countries is much more than revenue loss. The impact and effect of tax avoidance on the economies of developing countries such as Nigeria was well encapsulated by Baker<sup>79</sup> who described tax avoidance as the ugliest chapter in global economic affairs since slavery and is still one of the worst problems affecting developing economies.<sup>80</sup>

### **Prevention of Tax Avoidance in Nigeria**

Generally, the traditional approach to counter tax avoidance has always been for countries to include anti-tax avoidance provisions in their domestic income tax legislations to prevent taxpayers from exploiting the loopholes in the tax law to reduce or minimize their tax liability.<sup>81</sup> This can be in the form of a Specific Anti-Avoidance Rule (SAAR) or a General Anti-Avoidance Rule (GAAR).<sup>82</sup> Both the SAAR and the GAAR provisions are regarded as the most common domestic legislative measures that are used and relied upon by countries to counter act of tax avoidance schemes.<sup>83</sup>

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<sup>75</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management* (2<sup>nd</sup> ed., Stirling-Horden Pub. Ltd. Ibadan 2013)133

<sup>76</sup> Save the Children also known as the Save the Children Fund International is an international non-governmental organization that promotes children's rights provides relief and support children in developing countries. It was established in the United Kingdom in 1919 in order to improve the lives of children through better education, health care, and economic opportunities, as well as providing emergency aid in natural disasters, war, and other conflicts, <<http://www.savethechildren.net/>>, accessed on 12 March 2022

<sup>77</sup> World Finance Magazine, 'The true costs of tax avoidance' <<http://www.worldfinance.com/strategy/the-true-costs-of-tax-avoidance>> accessed on 15 April 2022

<sup>78</sup> Ibid

<sup>79</sup> The founder and President of the Global Financial Integrity, <<http://www.gfintegrity.org/about/>> accessed on 15 April 2022

<sup>80</sup> Baker R., 'The Ugliest Chapter in Global Economic Affairs Since Slavery' <[http://www.taxjustice.net/cms/upload/pdf/Baker\\_070628\\_Conference\\_speech.pdf](http://www.taxjustice.net/cms/upload/pdf/Baker_070628_Conference_speech.pdf)> accessed on 15 April 2022

<sup>81</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management* (2<sup>nd</sup> ed., Stirling-Horden Pub. Ltd. Ibadan 2013)135

<sup>82</sup> Ibid

<sup>83</sup> Shaa'bani T., 'Anti-tax avoidance measures in OPEC-member countries' (2011) 7(11) Journal of American Science 106

Specific Anti-Avoidance Rule (SAAR) provisions are enacted for the sole purpose of preventing a specific known tax avoidance scheme.<sup>84</sup> This type of anti-tax avoidance provision is normally targeted at a specific avoidance scheme and providing for many consequential adjustments.<sup>85</sup> Example of SAAR in Nigeria is the Income Tax (Transfer Pricing) Regulations 2018 introduced by the FIRS pursuant to its powers under section 61 of the Federal Inland Revenue Service (Establishment) Act No. 13 2007. The Regulation was meant to provide specific transfer pricing regulation in Nigeria.<sup>86</sup>

General Anti-Avoidance Rule (GAAR) provisions are usually a set of rules within a country's income tax legislation designed to prevent or counteract an avoidance of tax.<sup>87</sup> GAAR provisions are normally of general application vesting the tax authority with broad, all-embracing rule and wide-ranging powers to deny the taxpayers of any tax benefits of any transaction or arrangement which is believed not to have any economic or commercial substance or any purpose other than to avoid payment of tax.<sup>88</sup>

The primary policy objective of the GAAR is to deter taxpayers from entering into any arrangements that would lead to avoidance of tax and where taxpayers go ahead with such an arrangement, the GAAR operates as a mechanism to deny any tax benefit which the taxpayer is trying to achieve.<sup>89</sup> In essence, the ultimate purpose of a GAAR provision is to stamp out tax avoidance.

In Nigeria, there are GAAR provisions in various tax legislations in the country to safe guard the tax base of the country from being eroded through various forms/schemes of tax avoidance. The provision of section 22 of Companies Income Tax Act<sup>90</sup> is widely considered as a GAAR provision in this regard. There are corresponding provisions in other tax laws such as the Personal Income Tax Act

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<sup>84</sup> Ibid 126

<sup>85</sup> Ibid 129

<sup>86</sup> Isau A. O., 'Transfer Pricing: The Nigerian Perspective' (2014) 2 (2) International Journal of Accounting and Taxation 26 <<http://aripd.org/journal/index/ijat/vol-2-no-2-june-2014-current-issue-ijat>> accessed on 9 July 2022

<sup>87</sup> Ernst & Young, 'GAAR rising mapping tax enforcement's evolution' <<http://www.ey.com/publication/.../GAAR.pdf>> p. 2 accessed on 20 July 2022

<sup>88</sup> Watters A. and Ferguson S., 'Tax Avoidance in the Modern World' (2013) 6(15) Tax Planning International European Tax Service 7

<sup>89</sup> HMRC, 'HM Revenue and Customs (HMRC) General Anti Abuse Rule (GAAR) guidance' <[https://www.gov.uk/.../2\\_HMRC\\_GAAR](https://www.gov.uk/.../2_HMRC_GAAR)> accessed on 14 July 2022

<sup>90</sup> Companies Income Tax Act CAP. C21 LFN 2004 (as amended)



(PITA),<sup>91</sup> Capital Gains Tax Act (CGTA)<sup>92</sup> and Petroleum Profits Tax Act (PPTA).<sup>93</sup>

The provision of Section 22 of CITA which is similar in content with the provisions of Section 17 of PITA, Section 20 of CGTA and Section 15 of PPTA is reproduced hereunder:

*Where the Board is of opinion that any disposition is not in fact given effect to or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, it may disregard any such disposition or direct that such adjustments shall be made as respects liability to tax as it considers appropriate so as to counteract the reduction of liability to tax affected, or reduction which would otherwise be affected, by the transaction and any company concerned shall be assessable accordingly.*

The above provision qualifies as a GAAR provision as it satisfies all the possible features of a GAAR. First, the provision identified the scheme to include any disposition which in the opinion of the FIRS is not given effect to or any transaction which reduces or would reduce the amount of any tax payable. Second, the provision identified tax reduction as the sole and dominant tax benefit of such transaction. The provision is therefore an omnibus anti-avoidance provision which empowers and invests the FIRS with the powers to disregard any artificial or fictitious dispositions and transaction meant to reduce tax payable and direct any adjustment in that regard.

It is posited that that GAAR provision in section 22 of CITA specifically empowers the FIRS with powers to:

- i. disregard any disposition which in its opinion is not given effect to;
- ii. disregard any artificial or fictitious transaction which reduces tax; and
- iii. direct adjustment in respect of the tax liability of such disposition and transaction as it considers appropriate to counter act the tax reduction.<sup>94</sup>

Due to its broad and general nature, the provision of section 22 of CITA occupies a critical position in the country's anti- tax avoidance armoury as it represents an attempt to make provisions to prevent future manifestations of unacceptable tax avoidance schemes in a situation where the tax avoidance scheme is not covered

<sup>91</sup> Section 17 Personal Income Tax Act CAP P8 LFN 2004

<sup>92</sup> Section 20 Capital Gains Tax Act CAP. PC1 LFN 2004

<sup>93</sup> Section 15 Petroleum Profits Tax Act CAP. P13 LFN 2004

<sup>94</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management* (2<sup>nd</sup> ed., Stirling-Horden Pub. Ltd. Ibadan 2013) 135

under any enactment.<sup>95</sup> It can therefore be seen that the powers conferred on the FIRS in section 22 of CITA is very wide and it is applicable to all possible tax avoidance schemes that may be conceived.<sup>96</sup>

However, using the GAAR provision in section 22 of CITA to deter tax avoidance is not without its own challenges. It has been argued, in this regard, that the language of the GAAR provision is too ambiguous, vague and imprecise in nature. For example, according to Ayua,<sup>97</sup> the language of the GAAR provision places enormous burden on the interpretative skills of tax officials requiring them to examine every transaction which can sometimes be a very difficult task. The author contended that due to the low level of training of the FIRS officials, the tax officials are usually reluctant to apply the GAAR provision to strike down tax avoidance in the country. This has affected the significance and the usefulness of the GAAR provision and accounts for the reason why the FIRS is yet to test the GAAR provision in the court.<sup>98</sup>

The situation is further compounded with the history of Nigerian courts which has consistently and religiously resolved any ambiguity in the tax legislations in favour of the taxpayer.<sup>99</sup> Courts in Nigeria usually confine themselves to the strict letter of taxation statute and consider tax as an imposition depriving citizens of their financial liberty. They are therefore traditionally hostile to statutes seen as encroaching on a citizen's property or liberty and any ambiguity in the tax law is usually resolved against the government and in favour of taxpayers.<sup>100</sup> The implication of this is that due to the ambiguous nature of its language, if tested in court, the GAAR provision is most likely to be resolved against the FIRS and in favour of the taxpayer.

It can therefore be posited that the GAAR provision in section 22(2) (b) of CITA cannot effectively on its own prevent tax avoidance in the country. That is why despite its presence in the CITA, the country continue to lose huge amount of tax

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<sup>95</sup> Obadina D. A., 'Fighting Aggressive Tax Avoidance in Nigeria: An Agenda for Reform' <[https://www.academia.edu/10805766/Tackling\\_Aggressive\\_Tax\\_Avoidance\\_in\\_Nigeria\\_an\\_agenda\\_for\\_reform](https://www.academia.edu/10805766/Tackling_Aggressive_Tax_Avoidance_in_Nigeria_an_agenda_for_reform)> accessed on 22 July 2022.

<sup>96</sup> Ibid.

<sup>97</sup> Ayua, I.A., *The Nigerian Tax Law* (Spectrum Law Publishers, Lagos 1996) 261.

<sup>98</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management* (2<sup>nd</sup> ed., Stirling-Horden Pub. Ltd. Ibadan 2013) 143.

<sup>99</sup> For example, in the case of *Ahmadu v. Gov. Kogi State* (2002) 3 NWLR (PT. 755) 502 at 522 paras B-E, the Court of Appeal held thus: 'In taxing legislations, one has to look merely at what is clearly said. There is no room for intendment. There is no equity about tax. There is no presumption about tax. Nothing is to be read in and nothing is to be implied. One can only look at the language used. But the strictness of the interpretation may not always ensure to the subject's benefit, for if the person sought to be taxed comes within the letter of the law, he must be taxed, however great the hardship may appear to the judicial mind'.

<sup>100</sup> Ibid

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revenue to various tax avoidance schemes which necessitated the need to introduce a regulation on transfer pricing.<sup>101</sup> However, notwithstanding its defects, the GAAR provision in section 22 of CITA provides the country with an extensive means of preventing tax avoidance in the country due to the fact that it can be extended to disallow all forms of conceivable tax avoidance scheme.<sup>102</sup>

### **Conclusion**

The article provided an in-depth understanding of the concept of tax avoidance. The article revealed that tax avoidance involves the legal utilization of the tax regime to reduce the amount of tax that is payable by means that are within the law. The article further revealed that while tax avoidance is not entirely illegal but it is considered to be immoral, improper, abusive and against the spirit of the law.

The article examined feature of tax avoidance transaction from the notions of 'form', 'purpose' and 'policy' and found that any transaction or scheme whose sole purpose to minimize tax liability and defeat the intention of parliament will be regarded to constitute tax avoidance. The article also found that apart from revenue loss, tax avoidance has direct negative impact on the lives of the people living in developing countries such as Nigeria. The finding of the article revealed that tax avoidance is countered through both Specific Anti-Avoidance Rule (SAAR) and a General Anti-Avoidance Rule (GAAR) which are considered inadequate. It is recommended that the Nigerian government and its policy makers should endeavor to strengthen the GAAR provisions in the various tax legislations in the country to overcome its defects in order to be more effective in preventing all forms and scheme of tax avoidance in the country.

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<sup>101</sup> Abdulrazaq M. T., *Principles and Practice of Nigerian Tax Planning & Management* (2<sup>nd</sup> ed., Stirling-Horden Pub. Ltd. Ibadan 2013) 144

<sup>102</sup> *Ibid* 123

KAMPALA INTERNATIONAL UNIVERSITY  
**LAW JOURNAL**

KIULJ Vol.4 Issue 2,2022



**ISSN: 2519-9501**