VAT on petroleum products: Will the “change” era bring relief?

One polemic that has confronted companies engaged in the marketing and distribution of PMS, AGO, DPK and aviation fuel around VAT is whether or not VAT is/should be chargeable on these petroleum products.

Today’s reality is that despite an installed capacity of 445,000 bpd, Nigeria is struggling to achieve adequate and stable supply of refined products. The nation’s refineries have not at any time aggregated output at full capacity and have over the years fallen into a state of disrepair due to neglect, irregular and/or shabby turn around maintenance regimen. Reliance has been placed on importation to make up the short-falls in daily supply of refined petroleum products domestically.

Eleven (11) years ago, the Federal Government opted for full deregulation in the downstream sector. This agenda was touted to be motivated by three main objectives. First was the need to re-appraise government involvement and participation in the downstream sector. This was reflected in Government’s desire to reduce and/or eliminate subsidies to the sector to enhance the prospects cost reflective prices to emerge. Second was the need to engage private capital in the ownership and operation of assets in the sector. Third was the need to achieve security of supply through free interplay of the forces of demand and supply.

It was then expected that market forces would have free rein in determining the retail prices of petroleum products principally kerosene (DPK), automotive gas oil (AGO/diesel), and premium motor spirit (PMS/petrol) rather than for government to fix their retail prices respectively. Eleven years on the reality is not different. Indeed, the level of subsidies in the sector has horrifically exceeded the 2004 level.

Nevertheless, the activities in the downstream sector are such that the Federal Government should be able to assess and collect both direct and indirect taxes. As at the center of the collectible indirect tax is value added tax (VAT). The VAT Act, Cap V1, Laws of the Federation of Nigeria, 2007 (as amended) provides the legal basis for the imposition of VAT on supply of all goods and services in Nigeria except those specifically exempted.

VAT is a multistage consumption tax, which is charged and payable on the supply of all goods and services, other than those listed in the First Schedule (exempted items) to the Act. Goods exempted include, but are not limited to, basic food items, baby products, all exports, books and educational materials. Since its introduction in 1993, Value-added Tax (VAT) has become an important source of revenue to the Federation which is available for distribution amongst the federating units. VAT accounts for about 20% of the total tax revenue generated in the country.

One polemic that has confronted companies engaged in the marketing and distribution of PMS, AGO, DPK and aviation fuel around VAT is whether or not VAT is/should be chargeable on these petroleum products. Industry practice appears to have relied on a letter of 2005 from the Petroleum Product Pricing Regulatory Agency (PPPRA) not to charge VAT given the regulation of retail pricing and provision of subsidy to reduce the cost burden to citizens in relation to these “essential” products.

Naturally, the imposition of VAT will increase the amount payable by the final consumer and this may contradict the objective of the subsidy. There is need for marketers and distributors of these petroleum products to be able to manage their exposure to penalties, interests and other risks arising from a potential allegation of non-compliance with the provisions of the VAT Act.

In this regard, the following questions beg for response:

- Does the relevant PPPRA letter of 2005 have any status under the VAT Act?
- Is there a need for FIRS and PPPRA to provide clarity on this matter to guide affected taxpayers?
- Is the constructive VAT exemption applicable only to subsidized petroleum products or does this extend to AGO in its post-regulation era?
- No doubt, taxation remains a sustainable source of Government revenue due to “the stability and certainty of the tax system”. Thus, the expectation of the National Tax Policy is to resolve the following issues amongst others:
  - Who collects what?
  - How is it collected?
  - Who controls what is collected?
  - Who is responsible for spending what is collected?
  - Who is ultimately responsible and accountable to taxpayers for the revenue collected and its expenditure?

Taxpayers would only understand and trust the tax system when taxes and related compliance requirements are kept simple, certain and clear.

1  (FIRS Q3 2015 report).
2  National Tax Policy.