Taxation of Petroleum Profit under the Nigeria's Petroleum Profit Tax Act

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ABSTRACT

The aim of this paper is to examine the ownership, the legal framework as well as the basic components of the petroleum profits, which components are revenue, adjusted profits, assessable profit, chargeable profit, assessable tax and chargeable tax. This article focuses on the assessment of the petroleum profit tax under the Petroleum Profit Tax Act, Cap P 13, Laws of Federation of Nigeria, 2004 as well as judicial authorities regarding same. Nigeria's economy is totally dependent on oil. The revenue from oil accounts for over 85% of the entire revenue of Government and about 95% of foreign earnings. Initially, Government's interest in oil was only limited to the collection of royalties and other dues from the oil companies and making rudimentary laws to regulate the activities of the oil companies. However, with the discovery of crude oil in commercial quantities, the role of Government in the sector gradually progressed from mere regulatory to direct involvement in the oil exploration. The oil boom has led to more revenue through tax and royalties. It concludes that when the proposed Petroleum Industry Bill, currently under review at the National Assembly is eventually passed into law, it is believed that it will bring about the much desired development in the sector.

Keywords: *Petroleum Profit Tax Act, petroleum profits, revenue, oil accounts, Nigeria's economy*

INTRODUCTION

Taxation can simply be described as a compulsory sum levied by a sovereign power on the incomes, profits, goods and services or properties of individuals or corporate bodies. In most countries of the world the primary objective of taxation is essentially to generate money for government expenditures on social welfare. The rationale for imposing taxes in a market economy includes provisions of basic amenities for the people, defence, redistribution of incomes, etc. In the past, Nigeria boasts of its resources from export of cocoa, cotton, rubber and groundnut. Before independence in 1960, agriculture was the mainstay of Nigeria economy, providing cash crops as well as food to the

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entire economy[2]. The history of oil production in Nigeria dates back to 1908 when an affiliate of a German Exploration Company, the Nigerian bitumen company came to present day Ondo State to venture for Bitumen (tar sand)[3]. By 1971, a year after the Civil War, oil had started becoming more important to the economy[4]. With the boom in the late seventies of oil, attention shifted completely from the agricultural sector to the oil sector of the economy. The structure of Government's participation, as well as its impacts on the entire sector of the economy, changed from been a mere 'supportive' sector it was in 60s to the predominant source of foreign exchange earnings and development finance as well as a viable access to international development opportunities.

The very vital importance of oil to Nigeria dictates government's involvement in the regulation of the Nigerian oil sector. It is noteworthy that prior to 1971, all of the multinational companies were wholly owned by their foreign parent companies. In that same year, government started acquisition of participating interest in the operation of these companies while citizens also acquired varied shareholding interests in the assets of these companies[5]. To strengthen Government control in the sector, the Nigerian National Petroleum Corporation (NNPC) was established by a decree in 1971[6]. Petroleum is a generic name for combustible hydrocarbon compound found in the earth, and occurring in nature in the gaseous, liquid and solid state[7]. Taxation of petroleum profit started in 1959 with the enactment of the Petroleum Profit Tax Act 1959 which was meant to have a retrospective effective date of 1st January, 1958. This Act serves as a foundation for the present Petroleum Profit Tax Act, 2004; which was further amended in 2007.

The objective of this Act can be gleaned from its preamble which reads:

> *"An Act to impose a tax upon profits from the winning of Petroleum in Nigeria, to provide for the assessment and collection thereof and for purposes connected therewith."*

In line with its objective, the Act in Section 3 thereon establishes a body known as the Board and saddled with the responsibility of assessment and collection of the petroleum profit tax.

1999 CONSTITUTION AND THE OIL AND GAS SECTOR

In Nigeria, like in any other countries, Constitution is the organic law from which all other laws derived their validity. *Njikonye v. MTN Nig. Comm. Ltd[8].; Famfa Oil Ltd. v. A-G Federation & NNPC[9]; Attorney-General, Federation v. A-G Abia State & 35 Ors. (No. 2)[10].* In other words, it is the basis upon which the existence of other laws rest. The Court of Appeal, per Omoleye, JCA, put the position as: "The Constitution of the Federal Republic of Nigeria, 1999, is the organic law from which all other laws flow and derive their validity".[11] In the oil and gas sector of the economy, the 1999 Constitution (as amended) is the supreme law in relation to Nigeria's oil and gas sector. Section 1 (1) of the Constitution provides for its supremacy as follows: "This Constitution is supreme and its provisions shall have binding force on all authorities and persons throughout the Federal Republic of Nigeria." The Constitution further provides that if any other law is inconsistent with the provisions of the constitution, the constitution shall prevail and that other law shall to the extent of its inconsistency be void[12]. Section 44 (3) of the Constitution vests the ownership and control of mineral oil and natural gas in the Federal government of Nigeria. The Constitution provides:

> "*Notwithstanding the foregoing provisions of this section, the entire property in and control of all minerals, mineral oils and natural gas in, under or upon any land in Nigeria or in, under or upon the territorial waters and the Exclusive Economic Zone of Nigeria shall vest in the Government of the federation and shall be managed in such manner as may be prescribed by the National Assembly.*"

In line with these provisions of the Constitution, the National Assembly, through its Standing Committees on Oil and Gas Matter, has as one of its constitutional duties, the responsibility to monitor the activities in the Nigeria's oil and gas sector[13]. This oversight function has helped the Federal Government in saving several billions of naira in the oil and gas sector alone[14].

ADMINISTRATION OF PETROLEUM PROFIT TAX

The administration of petroleum profit tax is vested in the Federal Inland Revenue Service (formerly Federal Board Inland Revenue). The FIRS[15] is statutorily responsible for the assessment and collection of taxes in the oil and gas sector of the economy. Section 3 of the Petroleum Profit Tax Act vests the Board with the following powers, among others;

i. Due administration of the Act;

ii. Acquisition, holding and disposal of any property taking as a security for or in satisfaction of any tax or any judgment debt due in respect of any tax, etc.

iii. The service may by notice in the Federal Gazette direct that any information, returns or documents required to be supplied, forwarded or given to the revenue service be supplied to such other person as the service may direct[16]; Specify from time to time, form of returns, claims, statement and notices under the Act[17], etc.

The scope of FIRS[18] power over tax administration and enforcement covers three types of companies in the oil and gas industry, namely:

a. Crude Oil and natural Gas producing Companies;
b. The Petroleum Marketing Companies; and
c. Servicing Companies[19];

The Act regulates upstream activities as opposed to downstream[20]. Upstream operation involves all activities carried out in the exploration[21], drilling, extraction, development, production, transportation and sale of crude oil. Downstream operations on the other hands involve conversion of crude oil into usable form such as premium motor spirit, diesel, kerosene, gas utilization project etc. In the exercising the duties and power conferred on it by the Act, the Service shall be subject to the authority, direction and control of the Federal Minister of Finance[22]. Consequently, any written direction, order or instruction given by the minister, after consultation with the Chairman of the Service, shall be carried out by the Service.

OIL LICENSES AND FISCAL ARRANGEMENTS

The Petroleum Act provides for three (3) classes of Oil Licenses that can be granted by the Minister to a company[23]. Section 2 of the Act vest the Minister, charged with the responsibility for petroleum, with the power to grant three categories of interest from the absolute ownership of the Federal Government[24]. The law provides that a lease or licence under the Act may be granted only to a company incorporated in Nigeria under the Companies and Allied Matters Act or any corresponding law[25]. The Nigerian Court of Appeal in *Nwadioro & 2 Ors. v. Shell Petroleum Development Company of Nigeria Ltd*[26] held that the Petroleum Decree No. 51 of 1969 (now Petroleum Act) empowers the Minister or government to grant an oil exploration license, oil prospecting license and oil mining license to a citizen of Nigeria or a company incorporated in Nigeria under the Companies Decree, 1968 or any other corresponding law. In any of the three licenses, whatever right is granted to a company, the reversionary right is retained in the grantor, which is the Federal Government of Nigeria. The licenses that can be granted are:

Oil Exploration License (OEL): An oil exploration license is granted to a company to explore for petroleum. An oil exploration license does not confer any exclusive license over the area of the license, and the grant of an oil prospecting license in respect of any area shall not preclude the grant of another oil exploration license or of an oil prospecting license or oil mining lease over the same area or any part thereof[27]. An oil exploration license shall terminate on 31st December next following the date on which it was granted, but the licensee shall have an option to renew the license upon the fulfillment of certain conditions[28].

Oil Prospecting License (OPL)[29]: This license confers exclusive right on the holder of the license to explore, carry away and dispose of petroleum discovered and won in the area of operation[30]. The area covered by an oil prospecting license must be compact but not being an area in excess of 2590km^2 (1000 sq. Miles). The award of oil prospecting license creates a contractual relationship between the parties which is statutory in nature[31]. The duration of an oil prospecting license shall be determined by the Minister, but shall not exceed five years (including any period of renewal)[32]. The holder of an oil prospecting license may carry away and dispose of petroleum won during prospecting operations, subject to the fulfillment of obligations imposed upon him by or under the Act. These obligations include any special conditions imposed under paragraph 34 of the First Schedule to the Petroleum Act or by the Petroleum Profit Tax Act or any other law imposing taxation in respect of petroleum[33]. The oil prospecting license can be converted to an oil mining license[34].

***Oil Mining License (OML)[35]*:** This type of license is issued to a holder of oil prospecting license that has satisfied all the conditions with daily production of not less than 10,000 barrels. This license confers exclusive right on the holder to explore, carry away and dispose of petroleum discovered and won in the area in excess of 1295km^2 (500 sq. miles). The life of an Oil Mining License is usually for a maximum of 20 years but renewable in accordance with the Act, and the leases of the license is expected to apply for a renewal of the license not less than twelve month before the expiration of the lease[36]. A holder of an oil mining license may, with the consent of and on such terms and conditions as may be approved by the President, farm out any marginal field which lies within the leased area. One half of the area granted under an oil mining lease shall be relinquished after a period of ten (10) years.

FISCAL ARRANGEMENTS

***Joint Venture*:** This is an arrangement under which the Federal Government through the Nigerian National Petroleum Corporation (NNPC) enters into a joint operating agreement with multinational companies as joint venture partners. The foreign technical partners are usually designated as "Operators". The operators' duties include the implementation of the work program and budget. Each partner is expected to make contribution to cash calls through exploration, development and production activities, and separately lift and dispose of its share of crude oil based on their equity contribution, usually in the ratio 60:40, and also separately account for petroleum profit tax and royalty. The royalty rate for Joint Venture Operation is as follows:

i. Onshore…………………………………………...........…20%

ii. Offshore less than 100m water depth…………………………….18%
iii. Offshore 100 – 200 water depth………………………….....162/3%

***Product Sharing Contract*:** Under this arrangement, the NNPC, who is the owner of the mineral right (concession) enters in to a contract with a foreign technical partners designated as contractors. The contractors bear all the risks and when oil is discovered in commercial quantity, they recover their cost and share profit on a predetermined ratio with NNPC. The ownership of the concession remains with NNPC. Under this arrangement royalty is payable as follows:

201 – 500 meters water depth ………………………………………….12%
501 – 800 meters water depth …………………………………………….. 8%
801 – 1000 meters water depth ………………………………………… 4%
Beyond 1000 meters water depth …………………………………… 0%
Inland basin water depth …………………………………………… 10%

***Marginal Field Operators*:** Under this arrangement fields discovered by the multinational companies but left unattended to for a period not less than 10 years is compulsorily acquired and reallocated to indigenous concession holders to boost local participation in the oil and gas industry.

***Service Contract*:** Under this scheme, contractors undertake exploration development and production activities for and on behalf of NNPC, the concession owners. The contractors provide the capital and technical expertise and are reimbursed from the fund obtained from the sale of oil produced. However, profit of a company engaged in service contract is not subject to petroleum profit tax, but rather companies income tax.

OWNERSHIP OF PETROLEUM RESOURCES

The entire ownership and control of all petroleum resources in Nigeria is vested in the Federal Government of Nigeria[37]. The Constitution provides that ownership of mineral resources shall be vested in the Federal Government of Nigeria[38].

Section 1 (1) of the Petroleum Act[39] provides as follows:

> *"The entire ownership and control of all petroleum in, under or upon any land to which this section applies shall be vested in the state."*

Although the section provides that ownership is vested in the state, the word 'state' used refers to the Federal Government of Nigeria as opposed to components states. The Supreme Court in the case of *Attorney General, Federation v. Attorney General, Abia State & 35 Ors. (No. 2)*[40] put the position succinctly as follows:

"By virtue of section 315 of the Constitution the four enactments mentioned above are existing laws of the national Assembly and by virtue of Section 4 (2) and (3) of the Constitution, National Assembly has the power to make laws for the peace, order and good government of the Federation of Nigeria or any part thereof with respect to any matter included in the Exclusive Legislative List set out in Part 1 of the Second Schedule to the Constitution. Item 26 of the said Exclusive List is external affairs and each of the aforementioned enactments is concerned with external affairs, one of the items in the Exclusive Legislative List which the State Houses of Assembly are banned from legislating upon.

In the circumstances, the federal Government alone and not the littoral States can lawfully exercise legislative, executive and judicial powers over the maritime belt or territorial waters and sovereign right over the exclusive economic zone subject to universally recognized rights. The validity of the four aforementioned enactments has not been questioned"[41].

The legal implication of this is that no state government, local government or any group or group of persons other than Federal Government can exercise any sovereign right, claim, control or ownership over oil and gas resources within, upon or underlying all lands, sea bed and sub-oil including lands under the territorial waters of Nigeria or that forms part of the Continental shelf or exclusive Economic Zone of Nigeria.[42] The Federal Government, however, permits the involvement of private and public interest in the development, production, marketing and export of discovered associated gas. Although, the Petroleum Profit Tax Act provides a framework for the understanding of the Nigerian petroleum tax regime, there are other various contractual agreements, memorandum of understanding and side letters that provide information on the incentives made available by the Federal Government to the operators in the oil and gas sector. All these are additional provisions of the Act and are usually applied as if they are part of the Act.

ASSESSMENT OF PETROLEUM PROFIT TAX

The Government of Nigeria, like in any other countries of the world, has legislative power to impose on its citizens, any form of tax and at whatever rates it deems appropriate. The taxation of petroleum profit is governed by Petroleum Profit Tax Act[43]. The tax is levied on the profits of a company engaged in petroleum operations during an accounting period. The chargeable persons under the Act are companies engaged in petroleum operations as opposed to individuals who are not permitted to go into petroleum operations[44]. Petroleum, for the purpose of tax, is defined as:

> *"Mineral oil (or related hydrocarbon) and natural gas as it exists in its natural state, and does not include coal or bituminous shales or other stratified deposits from which oil can be extracted by destruction distillation"[45].*

Petroleum Operation is defined as:

> "*The winning or obtaining and transportation of petroleum or chargeable oil in Nigeria by or on behalf of a company for its own account by any drilling, mining, extracting or other like operations or process, not including refining at a refinery, in the course of a business carried on by the company engaged in such operations, and all operations incidental thereto and any sale of or any disposal of chargeable oil or on behalf of the company*."[46]

In the case of *Shell Petroleum Development Company (Nig.) Ltd v. Federal Board of Inland Revenue[47] it* was held by the Supreme Court that petroleum operation for the payment of profit tax by companies engaging in petroleum operations includes not only winning or obtaining petroleum oil by drilling, mining, etc. but all operations that are incidental to such operation. The legal implication of this is that activities such as refining of crude oil, marketing, sold minerals, oil field services, etc., are not subject to petroleum profit tax. These activities are rather subject to companies' income tax under the Companies Income Tax Act. Petroleum profit tax is imposed on the profit derived from petroleum operations. The legal basis for imposition and payment of petroleum profit tax by companies engaged in petroleum operations in Nigeria is contained in section 8 of the Act. The Act provides as follows:

> *"There shall be levied upon the profits of each accounting period of any company engaged in petroleum operation during that period, a tax to be charged, assessed and payable in accordance with the provisions of this Act."*

The above provisions have received judicial blessing in a number of authorities[48]. The Supreme Court in *Shell's*[49] held that by virtue of section 8 of the Petroleum Profit Tax Act, any company engaged petroleum operations is liable to pay profit tax and such tax is to be deemed as debt due to the Federal Government. In order to ascertain the petroleum profit tax payable by a company under the Act, the computation of the following is necessary. The Act provides for the computation of the petroleum profit tax as follows.

Revenue**:** This can simply be described as the proceeds of the company. For the purpose of ascertaining tax payable by a company engaged in petroleum operation, all the revenue accruing to the company during the accounting. The revenue is taken to be the aggregate of:

a. Proceeds of all chargeable oil sold by the company during that period;[50]

b. Value of all chargeable oil disposed by the company during the period[51];

c. Value of chargeable natural gas sold;[52]

d. All income incidental to and arising from one or more petroleum operations, e.g. interest on fixed deposit, rent/hire of equipment, income from services provided to another petroleum company, etc.

The aggregate of what constitute chargeable oil sold for the propose of item "b" is defined in Section 9(2) to include value of oil as determined, cost of extraction of that oil deducted as well as any cost incurred by the company in transportation and storage of that oil between the field of production and the place of its disposal.

***Adjusted Profit*:** The adjusted profit of a company in any accounting year means the profit for that period after the deductions of allowable expenses as contained in section 10(1)[53]. The nature of petroleum operations necessarily require that certain expenses will have to be incurred for the business that could not be tied directly to the income produced. It is clear that such would have been incurred for the petroleum operations but have not produced income/ profits. Consequently, section 10(1) of the Act allows a company engaged in petroleum operations to make some deductions before calculating its profit payable by it. These are regarded as allowable expenses, and they include.

i. Rent incurred by the company;

ii. All non-productive rents, the liability of which was incurred by the company during that period;

iii. All royalties;

iv. Sums incurred by way of interest up money borrowed by the company;

v. Expenses incurred for repair of premises, plant, machinery or fixtures;

vi. Debts directly incurred by the company and proved to the satisfaction of the Board to have become bad or doubtful in the accounting period;[54]

vii. Exploration and drilling costs, including costs relating to the drilling of the first two appraisal wells in a particular field;

viii. All sum incurred by way of interest on any inter-company loans under terms prevailing in the open market;

ix. Any contribution to pension, provident or other society, scheme or fund as may be approved; etc.

Bank charges and scholarships are, ordinarily, not deductible as allowable expenses. However, where the charges arose or were imposed by the Federal Government in the course of the company's operation relating to petroleum operation, such charges will be allowed. In other words, they (charges) will be allowed once they are incidental to petroleum operations. It was held by the Supreme Court in the case of *Shell Petroleum Development Company (Nig.) Ltd V. F.B.I.R*[55] that scholarship expenses incurred by a company will qualify as allowable expenses under section 10(1) of the Act. In that case, one of the issues in contention was whether or not the scholarship expense incurred by the company was deductive as an allowable expense or not.

Uwais, C.J.N that case succinctly put the position as follows:

> *"It seems to me obvious that in computing the adjusted profit of the appellant, bank charges cannot be deducted under the provisions of section 10 subsection (1) (G). This is because the Central Bank of Nigeria, as rightly held by the Court of Appeal (per Awogu, J.C.A) is neither the Federal Government of Nigeria, nor Government of any State no a Local Authority.*
>
> *However, the situation differs with regard to the provisions of section 10 (1) simpliciter. What needs to be determined thereunder is the question whether the payment of bank charges arose in the course of the operations of the appellant as defined under the definition of 'petroleum operations' in section 2 of the Petroleum Profit Tax Act"*[56]

The Court went further:

> *"In my respective opinion, the bank charges qualify for deduction under the general provisions of section 10 subsection (1) of the Petroleum Profit Tax Act"*[57].

This decision was followed by the Nigerian Court of Appeal in the case of *Gulf Oil Company (Nig.) Ltd V. F. B. I. R*[58] The deductions allowed by virtue of the provisions of section 10 (1) are however limited[59]. The following expenses are not allowed for the purpose of calculating adjusted profit;

i. Any disbursement or expenses not been money wholly and exclusively laid out or expended, or any liability not being a liability wholly or exclusively incurred, for the purpose of those operations;
ii. Any capital withdrawn or any sum employed or intended to be employed as capital;
iii. Any capital employed in improvement as distinct from repairs;
iv. Any sum recoverable under an insurance or contract of indemnity
v. Rental of or cost of repairs to any premises or part of premises not incurred for the purpose of those operations; etc.

The Act also allows some adjustments to be made in accordance with the provisions of section 14 of the Act. Section 14 excludes the inclusion of certain profit in the computation of petroleum profit tax.

The section provides thus;

"Where a company engaged in petroleum operation is engaged in the transportation of chargeable oil by ocean going oil-tankers operated by or on behalf of the company from Nigeria to another territory then such adjustments shall be made in computing an adjusted profit or loss as shall have the effect of excluding therefrom any profit or loss attributable to such transportation."

The income derived from the transportation of crude oil by an ocean-going tanker is not an income derived from petroleum operation. Consequently, such income is not chargeable to tax under the provisions of the Petroleum Profit Tax Act. The position of the law is that such income should be subject to tax under the provisions of the companies Income Tax Act. Thus, any expenses incurred to earn the income from the transportation of crude oil shall be treated as a non-allowable expense under the Petroleum profit Tax Act.

It follows then that the profit of the company will be adjusted in such a way as to exclude that portion of the profit relating to transportation of oil outside the shores of the country. The profit so excluded shall be subject to tax under the Companies Income Tax Act. Apart from this, there are other incomes which are regarded as non-taxable incomes, and for which adjustments must be made. These include:

i. Income from refinery operations
ii. Any reversal into income of a previously disallowed expenses
iii. Any profit on the disposal of fixed asset;

There is no provision under the Act, unlike the Companies Income Tax Act, relating to allowable donations. It is therefore correct to say that any donation made by a company engaged in petroleum operations shall be regarded as a non-allowable expense.

It should also be noted that before expenses can be regarded as incidental to petroleum operation such expenses must wholly, exclusively and necessarily be incurred by the company. The Supreme Court held that such must be" *expenses wholly, exclusively and necessarily be incurred for the purpose of petroleum operation*[60], which phrase been interpreted to mean solely or entirely. Where a deduction has been allowed to a company under section 10 in respect of any liability or any part thereof corresponding to such part of the liability, shall, for the purpose of subsection (1) (d) of section 9, be treated as income of the company of the accounting period in which such waiver or release was made or given.

Assessable Profit**:** This refers to adjusted profit less the loss incurred by the company during the previous accounting year in accordance with section 16.[61]

Section 16 (1) provides:

> *"Subject to the provisions of this section, the assessable profit of any company for any accounting period shall be the amount of the adjusted profit of that period after the deduction of –*
>
> *(a) The amount of any loss incurred by that company during any previous accounting period; and*
>
> *(b) In a case to which section 18 of this Act applies, the amount of any loss which under that section is deemed to be a loss incurred by that company in its trade or business during its first accounting period.*

Losses incurred by a company engaged in petroleum operation may be carried forward indefinitely. Thus, for a company subject to tax under the Petroleum profit Tax Act, it is possible for the relief of the loss to be deferred to the succeeding accounting period upon a formal application to the relevant tax authority. This application can only be made not later than five months after the year end.[62]

***Chargeable Profit*:** This is the amount of assessable profit of the accounting period less the sum total of capital allowances provided in the Second Schedule to the Act[63]. In other word, it the amount of assessable profit after deduction of any amount allowed as capital allowance. In calculating the amount to be deducted for the accounting period, it is provided that the limitation imposed by subsection (4) shall apply to ensure that the amount of any tax chargeable on the company for the period shall not be less than fifteen per cent of the tax which would be chargeable on the company. Section 20 (4) provides as follows:

> *"The amount to be allowed as a deduction under subsection (1) in respect of the said allowances shall be –*
>
> *a) the aggregate amount computed under subsection (2) of this section; or*
>
> *b) a sum equal to 85% of the assessable profit of the accounting period less 170% of the total amount of the deduction allowed as petroleum investment allowance computed under the second Schedule to this Act for that period, whichever is the less."*

Capital allowance is granted to a company engaged in petroleum operations in lieu of depreciation. This includes acquisition of right in or over petroleum deposits, searching for and discovery and testing of petroleum deposits and winning access thereto or the construction of any work or buildings which are likely to be of little or no value when the petroleum operations for which they were constructed ceased to be carried on. Capital allowance may be claimed on the following qualifying capital expenditure, which can be classified into four headings:

a. Qualifying Plant Expenditure
b. Qualifying Pipeline and Storage Expenditure
c. Qualifying Building Expenditure
d. Qualifying Drilling Expenditure

Capital allowance on capital expenditure is claimed on a straight-line basis over a period of five years at the following rates:

i. Year 1 …………………………………………..20%
ii. Year 2 …………………………………………..20%
iii. Year 3 …………………………………………..20%
iv. Year 4 …………………………………………..20%
v. Year 5 …………………………………………..19%

The balance of 1% represents the residual value of the qualifying capital expenditure. This must be retained for as long as long as the asset has not been sold. It must also be noted that even where the asset is sold, approval must be obtained from the Minister of Petroleum Resources before the residual can be expunged from the book. Allowances are also granted at varying rates on the cost of the assets. One of such is the Petroleum Investment Allowance. A company is allowed to deduct Petroleum Investment Allowance. The Petroleum Investment Allowance is an allowance granted in the first year a qualifying capital expenditure is incurred for the purpose of the company's operation. The applicable rate depends on the fiscal regime under which the company operates. Petroleum Investment Allowance shall be added to the annual allowance. Where the expenditure is incurred in respect of an asset that has been disposed of by the company before the beginning of its first accounting period, then any loss suffered by the company on the disposal of such asset shall be deemed to be qualifying drilling expenditure incurred by the company on that day, and shall be deemed to have been brought into existence an asset owned by the company in use for the purpose of the petroleum operations carried on by the company.[64]

The petroleum investment allowance is calculated as follows:

Onshore……………………………………………………….. 5%
Offshore up to and including 100 meters above Continental Shelves............10%
Offshore between 100 – 200meters……………...…………..............15%
Offshore above 200 meters…………………………….…………20%

***Assessable Tax*:** This refers to the tax arrived at using the appropriate tax rate on the chargeable profit. In other words, it is the amount of assessable tax less certain tax offset. Up to the end of 1994 year of assessment, the provisions of the PPTA is that tax offset should be used to reduce the assessable profit to obtain chargeable profit. Tax offset items include:

a. Non-productive rent

b. Royalties on local sales
c. Investment tax credit, etc.
d. Customs duty on essential items, etc.

The assessable tax of a company engaged in petroleum operation in any accounting period is the amount equal to 85% of its chargeable profit for that period[65]. Where, however, a company has not yet commenced to make sale or bulk disposal of chargeable oil under a program of continuous production and sale, its assessable tax for any accounting period during which it has not fully amortized all pre-production capitalized expenditure shall be 65.75 per cent of the chargeable profits for that period.

Chargeable Tax**:** This is calculated as the amount of assessable tax less the certain tax offset[66]. Section 22 (3) provides that in computing the tax payable, the Investment Tax Credit shall be applicable in full to petroleum operations in the contracts such that chargeable tax is the amount of assessable tax less the Investment Tax Credit. The investment tax Credit rate for a company operating Product Service Contract with the Nigerian National Petroleum Company (NNPC) is 50% flat rate for the contract area, regardless of the duration of the contract[67]. The Investment Tax Credit allowance shall be offset against the chargeable tax in accordance with the provisions of the production sharing contract.

An oil exploration company files two types of returns under the Petroleum Profit Tax Act; Estimated Petroleum Profit Tax Returns and Annual Petroleum Profit Tax. In respect of the estimated petroleum profit tax, tax for any accounting year is payable in twelve (12) equal installments commencing from March of the accounting year and ending in February of the following accounting year. In other words, the first installment is payable not later than the third month of the accounting period[68]. Subsequent installments will be due and payable not later than the last day of each month[69]. The estimated petroleum profit tax shall be submitted to the Board not later than two (20 months after the commencement of the accounting period[70]. The audited account is expected to be finalized and the actual tax return filed by May of the subsequent year. The annual petroleum tax returns, also known as the 13th instalment, is payable in July of the following accounting year. Where the total amount paid in advance exceeds the tax computed per account, the excess is granted as a tax credit against future installment. If any installment due and payable is not paid within the appropriate time limit, a sum equal to five (5) per cent of the amount due as installment shall be added to amount due[71]. Any company disagreeing with the assessment served on it by the Board has a right of appeal under the Act[72]

CONCLUSION

The article has been able to examine the ownership, the legal framework as well as the basic components of the petroleum profits, which components are revenue, adjusted profits, assessable profit, chargeable profit, assessable tax and chargeable tax. It is also clear from the above that petroleum profit is only payable by companies engaged in the exploration of activities. Where a company is engaged in services such a company will be charged to tax under the Companies Income Tax Act. The only statutory body empowered by law for the collection of petroleum profit tax is the Federal Inland Revenue Services (FIRS). The petroleum profit tax is an indispensable source of revenue to the Nigerian government and offers more prospects if properly annexed. The current rate of the petroleum profit is 50% for operations in the deep offshore and inland basin, while it is 85% for the operations in the onshore and shallow waters. The tax is payable, in advance, in twelve monthly installments plus a final installment[73].

Due to the significance of the sector, coupled with the extent of the revenue accruing to the government from that sector, efforts are being made to revolusionalise the Nigerian petroleum sector. One of such is the proposed Petroleum Industry Bill, currently under review at the National Assembly. Under the proposed Petroleum Industry Bill, there is going to be a total repeal of the petroleum Profit Tax Act, Cap P. 13, 2004. The present petroleum profit tax will be replaced with the Nigerian Hydrocarbon Tax (NHT)[74]. Section 313 of the proposed bill provides that Nigerian Hydrocarbon Tax will be computed on the chargeable profits for the relevant accounting period at 50% for onshore and shallow waters. When this Bill is eventually passed into law, it is believed that it will bring about the much desired development in the sector.

NOTES

[2]Afolabi Khadijat, *Impact of Oil export on Economic Growth in Nigeria from 1970-2006*. from: *http://www.abdulhamidmustapha.wordpress.com/2011/12/29* Retrieved on Saturday 22nd June, 2013

[3]Olanrewaju Fagbohun (2010), *The Law of Oil Pollution and Environmental Restoration: A Comparative Review*, Odade Publishers, Nigeria, p. 153. See also Online Nigeria, *Petroleum Exploration and Production*. Retrieved on Tuesday 6th August, 2013 from : http:onlinenigeria.com

[4]This marked the beginning of the discovery of oil in commercial quantity with the discovery of oil in Oloibiri in 1956 in the present day Rivers State.

[5]Olanrewaju Fagbohun, op. cit. p. 156.

[6]*Performance of Economic Growth in Nigeria (1979-2000): Impact of Oil Industry*. Retrieved on Saturday 22nd June , 2013 from: *http://www.doublegist.com/economic-growth-nigeria-impact-oil-industry*

[7]Williams & Meyers, *Oil and gas Law (2007),* Lexis Nexis, vol.1 p.1.

[8] [2008] All F.W.L.R (Pt. 413) 1343

[9] [2003] 18 N.W.L.R (Pt. 852) 453 SC
[10][2002] F.W.L.R (Pt. 102) 1.
[11]*Njikonye v. MTN Nig.Communication Ltd (*supra*)*
[12]Section 1 (3) of the 1999 Constitution (as amended).
[13] See Section 62, 88 and 89 of the 1999 Constitution (as amended)
[14]Udo Jude Ilo, *Oil Subsidy Report: A Chance for New Democracy in Nigeria*. Retrieved on Tuesday 2nd July, 22013 from: *http://www.opensocietyfoundations.org/voices/oil-subsidy-report-chance-new-democracy-nigeria*
[15] The Service is established by virtue of Section 1 of the Federal Inland Revenue (Establishment) Act, 2007
[16]Section 3 (d) of the Petroleum Profit Tax Act.
[17]Section 6 (2) of the Petroleum Profit Tax Act.
[18] The powers and functions of the Service are also being regulated by Sections 7 and 8 of the Federal Inland Revenue (Establishment) Act, 2007.
[19] Such services include drilling, seismic survey, logging, data interpretation from oil fields, etc.
[20] Downstream operations, which are not subject to petroleum profit tax, include marketing and refining activities.
[21] By oil exploration it means a search for reservoir traps. See Williams & Meyers op. cit. p. 6
[22]Section 3 (1) (f) of the Act.
[23] Section 2(1) of the Petroleum Act
[24] See the case of *Southern Atlantic Petroleum Limited v. Minister of Petroleum Resources NOGC 6[2007-2008] 245 CA.*
[25]Section 2 (2) of the Petroleum Act, Law of Federation of Nigeria 2004.
[26]NOGC 1 [1961-1995] 205 CA.
[27] See paragraph 2 to the First Schedule to the Petroleum Act, 2004
[28] See paragraph 3 to the First Schedule to the Petroleum Act, 2004
[29] Oil Prospecting Licence is defined in section 2 of the petroleum profit tax Act as a lease granted to a company, under Minerals and Mining Act, for the purpose of winning
[30] See paragraph 5 of the First Schedule to the Petroleum Act, 2004
[31] See the Supreme Court decision in the case of *Federal Government of Nigeria v. Zebra Energy Ltd. NOGC 3 (2) [2001-2002] 354 SC.*
[32] See paragraph 6 of the First Schedule to the Petroleum Act, 2004
[33] See paragraph 7 of the First Schedule to the Petroleum Act, 2004
[34]Ayoola-Daniels Niyi (2008), "*Nigerian Laws, Cases and Materials on Oil and Gas*", Petgas Global Consulting Limited, vol. 1, P. 16. See also the Court of Appeal decision in case of *Southern Atlantic Petroleum Limited v. Minister of Petroleum Resources NOGC 6 [2007-2008] 245.*
[35] Oil Mining Licence is defined in section 2 of the petroleum profit tax Act as a lease granted to a company, under Minerals and Mining Act, for the purpose of winning petroleum or any assignments of such lease.
[36]Paragraph 13 of the First Schedule to the Petroleum Act.
[37]Ayoola-Daniel, op. cit. at p. 10.
[38] Section 44 (3) of the 1999 Constitution (as amended)
[39] Cap P10, Laws of Federation of Nigeria, 2004.
[40] (supra)

[41]Per Ogwuegbu, JSC at p. 243, paras. B – E.

[42] Exclusive Economic Zone is defined in Article 55 of the United Nations Conventions on the Law of the Sea, 1982 as an area beyond and adjacent to the territorial sea, subject to the specific legal regime established in this Part, under which the rights and jurisdiction of the coastal state and the rights and freedom of other states are governed by relevant provisions of this Convention. The zone shall not extend beyond 200 nautical miles from the baselines from which the breadth of the territorial sea is measured.

[43] Cap P.13, Laws of Federation of Nigeria, 2004. This Act was amended in 2007. Both the 2004 and the 2007 Acts regulate taxation of petroleum profit in Nigeria.

[44] See section 24 of the Act.

[45] Section 15, Petroleum Act, Cap. P.10, Laws of Federation of Nigeria, 2004.

[46] Section 2 of Petroleum Profit Tax Act

[47]NOGC 2 [1996-2000] 80 SC. Also reported in (1996) 8 N. W. L. R (Pt. 466) 256

[48] See Shell Petroleum Development Company (Nig.) Ltd v. Federal Board of Inland Revenue (supra); Gulf Oil Company (Nig.) Ltd V. F. B. I. R (1997) N. W. L. R (Pt. 514)

[49] supra

[50]It was held by the then Federal Revenue Court in the case of *Shell B.P Petroleum Development Company v. Federal Board of Inland Revenue NOGC 1[1961–1995] 90 FRC* that the word "disposal' in section 10 of the Petroleum Profit Tax Act, 1959 is not the same thing as sale.

[01]In relation to chargeable oil owned by a company, 'disposed of' connotes delivery, without sale, of chargeable oil to a refinery or to an adjacent tank for refining by the company. See Advance Taxation, ICAN Study Park.

[52]Section 9(1) of the Petroleum Profit Tax Act.

[53]Section 9 (3) of the Petroleum Profit Tax Act.

[54] The deduction to be made in respect of a doubtful debt shall not exceed that portion of the debt which is proved to have become doubtful during that accounting period.

[55](supra)

[56]P.104, paragraphs. c – e.

[57]P.105, paragraph H.

[58](supra). Also reported in NOGC 2 [1996-2000] 156 CA.

[59]See Section 13 of the Petroleum Profit Tax Act.

[60]Per Uwais, CJN in *Shell Petroleum Development Company Ltd. v. Federal Board of Internal Revenue (*supra) at p. 109, paragraph f.

[61]Section 9 (4) of the Petroleum Profit Tax Act.

[62]See Section 16 (3) of the Petroleum Profit Tax Act.

[64]Advance Taxation, ICAN Study Park.

[65]Section 21 (1) of the Petroleum Profit Tax Act.

[66]Section 22 of the Petroleum Profit Tax Act.

[67]Section 22 (2) of the Petroleum Profit Tax Act.

[68]Section 45 (2) of the Petroleum Profit Tax Act.

[69]Section 45 (3) of the Petroleum Profit Tax Act.

[70]Section 33 of the Petroleum Profit Tax Act.

[71]Section 46 of the Petroleum Profit Tax Act.

[72]See section 41 of the Petroleum Profit Tax Act.

[73]Section 45 of the Petroleum Profit Tax Act.

[74]See Sections 299-352 of the proposed Petroleum Industry Bill.