



## Suitability of the punishment theory in tax offences: A case for a paradigm shift in Nigeria

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### Abstract

Tax remains the fulcrum to the existence of every nation. Countries have enacted different laws to maximise tax revenue collections. Unfortunately, the laws have been violated in different forms mostly in the nature of tax evasion and tax avoidance. The laws have equally embodied deterrence measures to prevent the commission of tax offences. But, tax evasion continues unabated; and scholarly mind has queried the effectiveness of the penalties prescribed against the commission of the offences: whether tax penalties are effective to dissuading tax offences? This article will investigate the punishment theories of crime, identifying their suitability to tax crime. The paper adopts doctrinal research methodology that focuses on review of different statutes, books and internet materials. The paper would be relevant to policy makers and tax administrator in the review of various tax offences and the commensurate punishment. It would expand the frontier of knowledge in the area of punishment theory that is more suitable and appropriate for tax offences. The paper concludes that if deterrent theory of punishment has not dissuaded the commission of tax offences, there may be need for a paradigm shift to the reformatory theory for the purpose of securing voluntary tax compliance.

**Keywords:** Suitability, tax offences, Nigeria, Nigeria

### Introduction

#### Understanding the nature of tax offences and penalties

The word offence is derived from a Latin word “*offendere*”, which means to strike again and is considered as an evil act<sup>[1]</sup>. The term offence like most law terms has no generally accepted definition. Many jurists have made varied efforts to give definition to the word “offence”. Glanville Williams defines offence as: “A legal wrong that can be followed by civil or criminal proceeding which may result in punishment”<sup>[2]</sup>. Allen Gledhill also asserts that an offence is a human conduct which the state decides to prevent by threat of punishment, liability of which is determined by legal proceedings of a special kind<sup>[3]</sup>. According to Sheila, an offence is synonymous with crime and a crime is an act, default or conduct that is prejudicial to the community, the commission of which by law renders the person responsible liable to punishment by fine or imprisonment in special proceedings normally instituted by officers in the service of the crown<sup>[4]</sup>.

An offence is the violation of any law, regulation or legislation. Anyone who is a party to doing any act which amounts to or results in, or forms part of a series of facts which together amount to or will result in something which is unlawful, is guilty of an offence. An offence may be minor or major in nature. A serious offence attracts severe punishment. According to Black’s Law Dictionary<sup>[5]</sup>, an offence is a violation of law. From all these definitions, an offence can therefore be said to be an act forbidden by the state and which if committed will attract punishment. Tax offence therefore is an offence committed in relation to taxation. Tax offence is simply tax criminality that the law will sanction. Severe tax criminality is an offence against the state which could attract prosecution by the state judicial machineries and which could lead to imprisonment if found guilty. A mild tax criminality on the other hand is a civil aspect of tax offence that attracts only payment of fines in terms of monetary payment.

In Nigeria, tax authorities are empowered to deal with both mild and severe tax offences. The Nigerian tax law empowers tax authority to use both civil as well as criminal sanctions to ensure the prosecution of tax offences.

#### Offence

According to Sheila<sup>[6]</sup> ‘an offence is synonymous to crime’ and a crime is ‘an act, default or conduct prejudicial to the community, the commission of which by law renders the person responsible liable to punishment by fine or imprisonment in special proceedings usually instituted by officers in the service of the crown. Punishment imposed against the commission of the crime is penalty. So failure to pay tax is an offence punishable by law. Chaskda<sup>[7]</sup>, posits on the other hand that ‘penalties’ can be defined as a sanction or punishment imposed upon any tax payer for failure to meet his legal obligation to pay tax. Abdulrazaq<sup>[8]</sup> treated in details tax offences with the attendant penalties. He however focused on the offences by the taxpayer; omitting the possibility that there could be offences against the government for improper utilization of tax fund.

Tax law can be infringed by way of tax evasion, tax avoidance, and tax planning or mitigation which has the potential to cause vast losses to national tax revenues. However, the nature of these activities must be distinguished. Tax evasion concerns the failure to declare, or the under declaration, of income, assets or activities that are taxable under the tax laws of the relevant jurisdiction<sup>[9]</sup>. Broadly, the term may encompass any non-compliance with tax law, regardless of the intention of the taxpayer and without reference to the penalties imposed for non-compliance<sup>[10]</sup>. Tax evasion will always result in a reassessment of the taxpayer’s liabilities and an obligation to pay what is owed<sup>[11]</sup>. However, not all tax evasion is criminal in nature. The tax evader must possess the requisite intention to evade their tax liabilities<sup>[12]</sup>. Some jurisdictions have further attempted to differentiate between the terms “tax evasion” and “tax fraud”, with the latter denoting

criminality<sup>[13]</sup>. In the UK and the US, these terms both reflect criminal conduct<sup>[14]</sup>.

In both countries, offences of fraud extend to dishonest acts and omissions that are intended to evade taxation, yet, if a distinction is made, the term 'tax fraud' is used to represent a calculated attempt to secure an unlawful advantage, as opposed to simply attempting to escape liability<sup>[15]</sup>. In each jurisdiction, a plethora of criminal offences has been enacted to combat tax evasion, yet almost all of these offences require the evader to have possessed the requisite *mensrea* or guilty state of mind.

Thus, to obtain a criminal prosecution of a tax evader in the UK, it must be proved that the defendant acted 'dishonestly<sup>[16]</sup>.' Dishonesty is not defined, but in the US, in contrast, the defendant must have attempted to evade a tax 'willfully,' defined as the 'voluntary, intentional violation of a known legal duty<sup>[17]</sup>.' In both jurisdictions, evidence of the defendant's state of mind, ascertained through their actions or omissions, is an important consideration for authorities in deciding whether to pursue a criminal prosecution or civil penalties.

The term tax avoidance is notoriously hard to define, as the term has no clear meaning and can encompass a wide range of activities<sup>[18]</sup>. However, conventionally, the term tax avoidance comprises all attempts made by a taxpayer to structure his affairs within the boundaries of the law to reduce, eliminate, or defer a liability to tax<sup>[19]</sup>. The legal nature of tax avoidance stems from important judicial decisions, which asserted that a taxpayer had no obligation to pay the revenue more than what was owed, as construed under the relevant taxing statute, even if this may be considered by some to be contrary to Parliament's or Congress' original intention.

Several judicial and academic attempts have been made to differentiate tax avoidance from tax mitigation or tax planning<sup>[20]</sup>. Tax planning involves considering the tax implications of a particular enterprise or activity, ensuring tax is applied as intended by the legislature. Thus, in a crude sense, the distinction may be regarded as follows; 'tax evasion--illegal and criminal; tax avoidance--legal but unacceptable; tax mitigation--legal and acceptable<sup>[21]</sup>.' Nevertheless, some commentators have deplored this further subdivision, as the terms 'tax avoidance' and 'tax planning' essentially refers to non-criminal activities, regardless of the perceived acceptability of the practice<sup>[22]</sup>.

Ultimately, the individual's intention in reducing his liability to tax is pivotal in characterizing the nature and legality of the behavior. Nevertheless, there remains a 'shadowy line' between tax avoidance and tax evasion, as tax evasion has developed a number of 'frayed edges'. For instance, ineffective tax avoidance may be characterized as tax evasion in certain circumstances, specifically, where the arrangements are hidden from the revenue collection authority and there cannot be said to have been a 'respectable technical case' for the failed avoidance scheme. Many commentators in each jurisdiction have examined the judiciary's approach to tax avoidance, specifically, judicial doctrines aiming to counter tax avoidance. In both the UK and US, the doctrine of 'sham' has been applied to tax avoidance transactions, along with other distinctively national approaches, including the "economic substance doctrine" in the US, and the purposive approach to interpreting tax statutes in the UK; all of which have the aim of restricting attempts to avoid taxation. The effectiveness

of these doctrines has been the subject of much debate, and even comparison, with many viewing the US doctrines as broader, and thus, more successful. The perceived limits of the UK doctrines, have led to the introduction of a statutory General Anti-Abuse Rule (GAAR),<sup>[23]</sup> to supplement case law and pre-existing targeted statutory anti-avoidance provisions. The suitability and efficacy of a GAAR generally, (the UK GAAR, and its less expansive US equivalent), have also been the focus of many commentators. Ultimately, the extensive consideration of tax avoidance in legal literature has resulted in comprehensive and contemporary accounts of anti-tax avoidance measures in the UK. The increasingly complex relationship between ineffective tax avoidance and tax evasion has often been examined by the courts in the UK, and some attention has been paid to this issue by commentators. Many have outlined the distinction between the two offences, often with the aim of assisting advisors in ensuring legal tax savings for clients<sup>[24]</sup>, while a few have expressed concern over tax evasion prosecutions for unsuccessful avoidance schemes, including prosecutions of tax advisers<sup>[25]</sup>.

### Tax Compliance, Tax Evasion and Avoidance

Tax compliance is a concept used to describe the voluntary payment of the right amount of tax by a tax payer at the right time and place. It encompasses the taxpayer abiding by the tax laws and rules, for example by declaring the actual income, filing tax returns as at when due and paying the tax timely. Andreoni, *et al*<sup>[26]</sup>, expressed the view that tax payers comply with their tax obligations to avoid legal sanctions because sanctions such as penalties and incarceration may be more costly than compliance. Gwangdi and Garba<sup>[27]</sup> emphasized that low tax compliance is a matter of grave concern in many countries especially developing ones like Nigeria because it limits the capacity of the respective governments to raise revenue for development purposes.

Rotimi, Udu and Abdul-Azeez<sup>[28]</sup> stated that tax evasion denotes an outright defrauding of tax revenues through illegal acts and deliberate suppression or falsification of the facts relating to ones' true tax liability. Soyode and Kajola<sup>[29]</sup> expressed the view that tax evasion is wilful and deliberate practice of not disclosing full taxable income in order to pay less tax. It is a violation of tax laws whereby the tax due by a tax payer is unpaid after the minimum specified period. Nzotta<sup>[30]</sup>, opined that a number of factors are responsible for tax evasion in Nigeria, such as corruption, complexity of tax laws and bye-laws, absence of strong deterrent punishments and unwillingness to prosecute tax offenders, amongst others.

Nzotta<sup>[31]</sup>, posited that tax avoidance refers to arrangement through which a person acting within the letters of law reduces his true tax liability, infringing in the process, both the spirit and intention of the law. Kay<sup>[32]</sup> opined that tax avoidance takes place when facts of the transaction are admitted but they have been arranged or presented in such a way that the resulting tax treatment differs from that intended by the relevant legislation. While tax evasion is illegal, tax avoidance is not illegal under the ambience of the law. According to Agom and Madaki<sup>[33]</sup>, complex payment scheme are designed by companies to avoid the tax master's path, and the bitter struggle for space between the

taxpayer to keep his wealth and the revenue to keep its due is patently obvious.

Ayua <sup>[34]</sup> stated that one of the greatest problems facing Nigeria is the problem of tax avoidance and evasion which is prevalent in the country. According to him, there is general agreement from many quarters that there is tremendous gap between actual and potential tax collections.

### Legal Framework for Tax Offences and Penalties

Since Nigeria tax statutes provides no legislative definition of tax offences and penalties, a working definition of tax offences is given as the action by the taxpayer to evade tax i.e. to get away illegally with his legal obligation to pay tax. Filing incorrect returns by omitting or underestimation of one's income constitutes tax offences and is punishable by either fine or payment of double of the amount which has been undercharged. The punishment or sanction imposed against tax defaulters is referred to as Tax Penalty. The penalty could take the form of civil sanction or criminal sanction <sup>[35]</sup>.

Civil sanctions are those fines that are pecuniary; and include the right of revenue authority to sell the goods of a tax defaulter or chattel, bond and other security in order to realize the amount owed. Criminal sanctions include imprisonment, with or without option of fine, imposed by a competent court upon the conviction of a tax defaulter. Examples of Civil Sanction can be seen under Sections 4 (1), (2) and (3) of Federal Inland Revenue Service (Establishment) Act.

Examples of Criminal Sanctions can be seen in sections 52(7) Personal Income Tax Act; 5(5), 7(5), 71(2)(b), 73(1)(b), 92(1) and 93 Of Company Income Tax Act, Sections 48(2) and 49 of the Petroleum Profit Tax Act.

Recently, tax offences and penalties have played a role within our political system. In the fight against tax evasion and corruption, it has often been thought that taxation would be used to weed out elective office holders or persons who are deficient in their tax payments. Electoral rules have accordingly made payment of tax a precondition for qualification to stand for elective offices. Unfortunately, however, this desired goal has in reality not been realized. A review of judicial authorities have shown that elections are rarely annulled on ground of failure to pay tax as and when due. The only known case within the knowledge of the writer where an election was annulled (and a new one ordered) on the ground of non-payment of tax as and when due is *Alhaji Mohammed NasirIdris (UNCP) v. Alhaji Mohammed Saleh & ors* <sup>[36]</sup>.

Aside from this case, most law reports are replete with cases where the call for such annulment was refused by the courts. In *Mohammed Hassan Rimi v. INEC & anor* <sup>[37]</sup>, for instance, it was held that where failure to pay tax is one of the grounds which make an election to be questionable, the requirements of the law to be fulfilled are as follows –

1. That the person earned a taxable income during the period in question;
2. That there was a proper assessment of the tax covering the period;
3. That notice of assessment was served on the person to pay his tax and he defaulted; and that the person failed to pay tax assessed within two months after the service of notice of assessment. These rigorous conditions outlined by the court make it almost impossible to annul elections on those grounds.

### The Punishment Theories

Punishment is the implication of intended burden upon someone due to his or her wrong doing. It is intended, as it is purposefully planned, and it is a burden as it has a sense of distress within it. Punishment is a form of social control which helps the society to sustain its rules and regulations and guarantee peace in the lives of its inhabitants. For this reason, if the wrong doing is not controlled, then, it will create problem within the society and in the lives of the people. There are mainly three theories of punishment: The deterrent theory which tries to deter crimes by punishing the criminal; the retributive theory which aims to attain retribution by punishing the criminal for his or her wrongdoing and finally the reformatory theory which hopes to reform the character of the criminal by inflicting punishment. Nevertheless, every one of these theories has their own merits and demerits. This research work x-rays the theories and adopts the one that is most appropriate for the purpose of this research.

#### 1. Deterrent Theory of Punishment

According to Mackenzie the aim of the deterrent theory is to deter others from committing similar offence <sup>[38]</sup>. It is also called the preventive theory of punishment or exemplary theory of punishment. Similarly, it is thought that punishment is said to have a deterrent effect when the fear or actual imposition of punishment leads to conformity <sup>[39]</sup>. Specifically, punishments have the greatest potential for deterring misconduct when they are severe, certain, and swift in their application <sup>[40]</sup>." So in general, the aim of punishment is to deter crimes. Punishment is inflicted upon the criminal in order to deter or prevent similar offences. It is done as a preventive measure towards crimes. It is exemplary so that others do not commit similar crimes. It is forward-looking. It is focused on society. The aim of this theory is not towards the individual but towards the society. This is because by exercising punishment, it aims to deter or prevent crimes, and set an example of what would happen if the crime is committed.

Utilitarians or consequentialists are the main advocates of this theory. Utilitarians want a system of punishment designed to make everyone feel a maximum of security <sup>[41]</sup>. This means that the system of criminal justice should prevent people from committing crimes by threatening them with those kinds of punishment that are best suited to the aim of preventing further crime. At the same time, those who do not commit crimes should feel reasonably certain that they will not be punished. This is because it wants to deter crimes in the future by inflicting punishment upon the criminal at the present. According to Bentham, people would be deterred from crime if punishment applies <sup>[42]</sup>.

A major limitation of the deterrence theory is that it promotes the treatment of a person as a means of benefitting others. It can also be criticized for failing to deter crime. Finally, it does not focus on reforming the criminal or retribution but only on the prevention of crimes.

#### 2. Retributive Theory of Punishment

This is another theory of punishment, and the aim of punishment here is to allow a man's deed to return to him and make the offender suffer like his victim. This theory envisages that the criminal has forfeited his or her rights by committing the crime and should be punished accordingly. This is because when a criminal commits a crime, he or she

has done an act that extinguishes their rights. For example, if a person kills another person, then he or she has forfeited his or her rights to be alive. Retributive theory of punishment has the purpose of re-attributing the unjust act, holding that the punishment should be proportionate to the crime. Deontologists are mainly the advocates of this theory. According to deontological ethics, when a person commits a crime, it means that he or she becomes afflicted with guilt, and a guilty person deserves to be punished. Tannsjo describes the system as backward-looking because it tries to do retribution to an already committed crime <sup>[43]</sup>. Judicial punishment should never be used merely as a means to promote some other good for the criminal himself or for civil society, but instead, it must in all cases be imposed on him only on the ground that he has committed a crime.

It is also criticized against forfeiting the rights of the offender. This is because human rights are supreme, inalienable and held as universal for all humans. Because of this, the abolition of rights due to the offender's criminal activity is not acceptable. Furthermore, even if rights are forfeited, the question arises about its length and duration.

### 3. Reformatory Theory of Punishment

According to Lillie, The aim of the reformatory theory is to reform the character of the offender himself <sup>[44]</sup>. In the view of Mackenzie, the aim of the punishment is to educate or reform the offender himself <sup>[45]</sup>. Brooks opines that punishment should teach the offenders a lesson <sup>[46]</sup>. The goal is to restore a convicted offender to a constructive place in society through some combination of treatment, education, and training <sup>[47]</sup>.” Thus it is also called the educational or rehabilitation theory of punishment where it aims to reform or educate or rehabilitate the offender. This theory of punishment reforms the character of the criminal by punishing him or her. It also tries to educate the criminal by inflicting punishment. This theory subscribes to the prevalent norms of contemporary humanism. That is why Lillie says that “the value of this suffering lies in the capacity to make the offender see the evil of his wrongdoing <sup>[48]</sup>.” So by punishment, the character of the criminal is reformed.

The reformatory theory believes that by punishment the criminal will be educated and so he or she will be able to live and contribute to society in a positive way. Its root is thought to be grounded by Plato as he thought that we ought not to repay injustice with injustice or to do harm to any man, no matter what we may have suffered <sup>[49]</sup>.

This position is supported by the criminologist's view that criminals have mental disorders. Thus the crimes they commit are pathological. They are victims of social, political, economic upheavals. So they should have treatment and should be cured as well as educated.

This position is most appropriate to most tax offences in Nigeria. Every tax offender is a victim of social, political and economic vices. The only cure to the offender is the provision of social services which shall serve as incentive to tax payment. The Nigerian tax offences seems more inclined to the deterrent and retributive theories. The law focused heavily on the punishment of tax offenders' rather than reformation of the offenders. Reformatory theory is the most contemporary method of punishment in the global world. This trend has recently crept into Nigerian legal system with the change of the name of 'Nigerian Prison Service' to the 'Nigerian Correctional Service'. Tax offences and punishment thereto are desirous of this shift in trend.

Tax offences and penalties should be reformatory and correctional. Tax offences in Nigeria are mainly caused by lack of tax morale to payment of tax. Lack of tax morale is the lukewarm attitude of taxpayers to payment of tax because of lack of dividends of taxation. People are averse to tax payment because the money supposed to be used to pay tax is personally deployed in the self provision of power, road, water etc which should have been provided by the government. Where, therefore, tax punishment becomes correctional and reformatory, focus should be placed on the causes of tax offences rather than criminalising them. The new tax laws in Nigeria should be legislating on the adequate utilization of tax fund which shall serve as incentive to the taxpayer to pay tax. There should be a social contract punishment theory where a tax payer shall have the *locus* to challenge and enforce punishment against tax authority in the event of the breach of social contract.

### Conclusion

Tax Evasion should be criminally and promptly punished to serve as deterrence to tax defaulters. Defaulters must be adequately prosecuted for tax evasion, or the general public will not take taxation seriously and tax criminality will continue to be on the rise. Monetary penalties and criminal sanctions should be drastically increased in order to serve as deterrent measure to tax evasion. The paltry N200 fine in the omnibus provision of Section 92(1) of Companies Income Tax Act for failure by a company to comply with any of the provisions of the Companies Income Tax Act is a joke. So also is the meager fine and term for failure, without sufficient cause, to attend in answer to notice or summons served on any person under the provisions of the Act, or having attended, fails to answer any question lawfully put to him, which is respectively put at N200 and imprisonment for six months in default of payment of the fine. It is respectfully our considered opinion that these provisions are not deep enough to deter an offender under the deterrence theory of punishment and should be amended to reflect the global new trend.

Nigerian tax policy must urgently consider and apply the reformation of tax offenders to secure their voluntary compliance. The reformation could be in the form of education, training and rehabilitation. More importantly, the mind of a tax offender should be reformed and restored to the tax principles through adequate and efficient utilisation of tax fund to the development of the society.

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