



APPRAISAL OF THE CHALLENGES FOR TAXATION OF DIGITAL ECONOMY IN NIGERIA***

Abstract

Taxation is a compulsory levy imposed on a subject or upon his property by the government having authority over him. Taxation of digital economy is the imposition of monetary charge by a sovereign state on all economic transactions that occur on the Internet. So many Nigerians engage in digital activities on daily basis, a lot connect to digital sources of news and information on Google, Facebook, Twitter including those who trend online. There are lots of digital non-resident companies that engage in electronic transactions with persons resident in Nigeria like Amazon, Walmart, Alibaba Group Holding Ltd, Apple Inc, e Bay Inc, Starbucks, Macy's, etc. and electronic payments are made through PayPal, Interswitch, Google Pay, Amazon Pay, WePay, Dwolla, Stripe, Braintree etc. There are challenges for taxation of digital economy in Nigeria which are problem of identifying non-resident companies, problem of identifying the income and profits of non-resident companies, problems of identifying the digital activities of these non-resident companies, lack of accurate data, lack of a specialized court, corruption, lack of IT experts, distribution of taxing powers between the source and resident jurisdiction, lack of effective tax enforcement mechanism, and lack of effective tax collection mechanism for viable businesses in online transactions. Nigeria economy is dwindling every day as a result of over dependency on oil as the basic and only reliable source of revenue to the economy of government of Nigeria thereby making it imperative for government to fashion out ways of curbing the challenges of taxation of digital economy so as to achieve a tax-based economy in Nigeria. The aim of this research is to appraise the challenges for the taxation of digital economy in Nigeria. The authors adopted doctrinal research methodology with use of statutes, case law, textbooks, journal articles as well as internet materials. This paper concluded that taxation of digital economy will generate revenue for the Nigerian government and recommended *inter alia* the need for a clear-cut legislation for the provision of a digital services tax and need for a specialized court, need to create a synergy between the Federal Inland Revenue Service (FIRS), Corporate Affairs Commission and the banks and to ensure effective implementation of the proposed digital services tax legislation.

Keywords: Taxation, Finance Act, Digital Economy, E-Commerce, E-payment, Legal Challenges and Nigeria

1. Introduction

Tax is legal civil responsibility imposed by the government to her citizens, either individuals or corporate bodies with a view to raising funds to finance its responsibilities economically, socially and politically.¹ Therefore, to have a complete definition of tax, one must have the following characteristics: It is an imposition by government, it is compulsory, it must have legislative backing and it must be for the support of government² Digital economy is a term for all those economic

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¹ OC Nwachukwu and C J Okongwu, An Expository Review of checking Incidence of Tax Evasion and Tax Avoidance: Nigerian experience', *Chukwuemeka Odumegwu Ojukwu University Law Journal* (COOUU) [2019] 5 (1) 230.

² IU Ibe, 'An Extermination of the Legal Regime for Taxation under the Nigeria Jurisprudence', *Chukwuemeka Odumegwu Ojukwu University, Journal of Private and public law* (COOU JPPL) [2019] 2 (1) 268.



transactions, interactions and activities that are based on digital technologies. As the name suggests, digital economy refers to an economy based on computing and digital technologies, but is often perceived as conducting business through the Internet. It essentially covers all businesses, economic, social and cultural activities that are supported by the web and other digital communication technologies.³ Digital economy is a term for all economic activities that are done through the internet. Taxation of digital economy is the monetary charges imposed by the government on economic digital activities. The global economy has seen rapid growth in digital business transactions, especially in the provision of goods and services through the internet. This rapid growth can be attributed to the fast rate of technological advancement which has changed how business transactions are conducted globally. Many Nigerians engage daily in digital activities with non-resident companies such as Amazon, Facebook, Twitter, Instagram, YouTube, Google, TikTok, WhatsApp, Walmart, PayPal, Interswitch etc. and they make a lot of profits without paying taxes to the government. The Nigerian government depends so much on oil as the only source of revenue, making it imperative for the government to move from an oil-based economy to a tax-based economy through taxing the digital economy. There is no aspect of our lives in Nigeria that is not affected by the wave of online buying and selling of goods and services and digital activities. These online economic activities enjoy some essential government amenities without contributing to the purse of the government by way of taxation. The law prior to the enactment of the Finance Act⁴ made it mandatory for every non-resident companies doing business in Nigeria to have a fixed base in Nigeria. Meaning that these non-resident companies must have a permanent establishment before they can be liable to pay companies income tax and other taxes payable by them in Nigeria. What it means is that non-resident companies carrying on businesses to persons resident in Nigeria through digital platforms were not liable to pay income taxes in Nigeria. However, by the intervention of the Finance Act,⁵ the Act⁶ widened the scope of tax by providing that,⁷ where a non-resident company engage in digital activities that transmits, emits, or receives signals, sounds, messages, images, or data of any kind of cable, radio, electromagnetic system, or any other electronic or wireless apparatus to Nigeria in respect of any activity, including electronic commerce, application store, high frequency trading, electronic data storage, online adverts, such non-resident company has significant economic presence in Nigeria and such profit will be chargeable to tax⁸ in Nigeria. The above provision shows that the issue of significant economic presence for purpose of taxation of income of digital non-resident companies has been settled to a very reasonable extent by the Finance Act⁹.

The Companies Income Tax Act amended by the Finance Act 2021 further expands the scope to include non-resident companies that provides digital services, or technical, management consulting or professional services through digital platforms to have established significant economic presence in Nigeria through the provision of these digital services. This means that these non-resident companies do not need to have a fixed base or a permanent establishment in Nigeria before carrying out digital activities to persons resident in Nigeria.

More so, a company, other than a Nigerian company, shall have a significant economic presence in Nigeria where it derives gross turnover or income of more than #25million Naira or its equivalent in other currencies, from any or combination of the following digital activities like streaming or downloading services of digital contents, including movies, videos, music, applications, games, e-books or any other digital activities.

³ *ibid*

⁴ Finance Act 2019 s. 4 (a)(i) Finance Act 2021 s. 4.

⁵ *Ibid*

⁶ *Ibid*

⁷ *Ibid* s. 4 (a)(i) Finance Act 2021 s. 4.

⁸ Finance Act 2019 s. 4 (a)(ii).

⁹ *Ibid* s. 4 (a) (i) Finance Act 2021 s. 4.



Taxation of digital economy will no doubt move Nigeria from oil-based economy to a tax-based economy. Also, the legal and institutional challenges are inhibiting the prospects inherent in taxation of digital economy in Nigeria. Furthermore, given the exponential growth of the global digital economy and its immense potentials, it becomes imperative for the government and the Nigerian tax authority to explore more creative approaches to ensure effective taxation of the digital economy in Nigeria.

2. Meaning of Digital Economy

Digital Economy is the term for all economic activities that are done through the internet. Digital economy is the worldwide network of economic activities, commercial transactions and professional interactions that are enabled by information and communications technologies (ICT)¹⁰. Digital economy is the economic activity that results from billions of everyday online connections among people, businesses, devices, data, and processes. It is one collective term for all economic transactions that occur on the internet economy. It is also known as the Web Economy or the internet economy. With the advent of technology and the process of globalization, the digital and traditional economies are merging into one. Organization for Economic Co-operation and Development (OECD) refers to the digital economy as an economy that incorporates all economic activity reliant on, or significantly enhanced by the use of digital inputs, including digital technologies, digital infrastructure, digital services and data. It refers to all producers and consumers, including government, that are utilizing these digital inputs in their economic activities¹¹. They are economic business activities that are done through the internet. Simply put, the digital economy is one collective term for all economic transactions that occur on the internet. Hence, it is safe to say that multinational enterprises like Amazon, Twitter, Alibaba, Spotify, Facebook, Google, Netflix, YouTube, etc. are operating in the digital space without necessarily having a physical presence in all the countries where they generate their revenues. Also, the digital economy is taking shape, and undermining conventional transaction notions about how businesses are structured; how firms interact; and how consumers obtain services, information and goods¹².

Taxation of digital economy is the monetary charges imposed by the government on economic digital activities.

3. Challenges for Taxation of Digital Economy in Nigeria

3.1. Lack of Accurate Digital Taxpayer Information

Lack of accurate data of these digital non-resident companies is one of the major challenges facing the Federal Inland Revenue Service in taxation of the digital economy. The Companies and Allied Matters Act (CAMA) 2020 makes it mandatory for every foreign company having the intention of carrying on business in Nigeria shall take all steps necessary to obtain incorporation as a separate entity in Nigeria, but until so incorporated, the foreign company shall not carry on business in Nigeria or exercise any of the powers of a registered company and shall not have a place of business or address for service or documents or processes in Nigeria. If a foreign company fails to comply with the requirements of registration, the company has committed an offence and liable to prosecution.¹³

¹⁰ M K Pratt, Definition of Digital Economy, available at <http://www.techtarget.com> assessed on the 1st of April 2023 at 03:26pm.

¹¹ A Osuji et al, Taxation of Digital Economy and the Introduction of Global Minimum Tax, available at <http://www.mondaq.com> assessed on the 1st of April 2023 at 04:48 pm.

¹² Deloitte, What is Digital Economy, available at <http://www.deloitte.com> assessed on the 1st of April 2023 at 03:38pm

¹³ Companies and Allied Matters Act 2020 s. 79.



Moreso, for purposes of payment of tax, digital non-resident companies are required to register with the Federal Inland Revenue Service (FIRS) for company's income tax. They are also mandated to file its annual returns with its audited account showing the profits of the company and also to obtain a Tax Identification Number (TIN) for purposes of paying tax.

In practice a lot of these digital non-resident companies carrying on digital activities in Nigeria are yet to register with the Federal Inland Revenue Service (FIRS) and many do not file annual returns with the Federal Inland Revenue Service (FIRS). The Act makes it mandatory for these digital non-resident companies to obtain a Tax Identification Number (TIN) but in reality, a lot of this non-resident companies are yet to obtain a Tax Identification Number (TIN) for purpose of payment of tax in Nigeria.

3.2. Identification of Digital Non-Resident Companies and Persons.

The problem of identifying these digital non-resident companies and person is one of the challenges facing the tax authority which is the Federal Inland Revenue Service (FIRS) in taxing the digital economy in Nigeria. This is because business transactions, especially provision and sale of goods and services are now done through the internet. This change can be attributed to the fast rate of technological advancement which has changed how business transactions are conducted globally. With the use of internet these digital non-resident companies are doing their businesses and making digital supplies to persons resident in Nigeria without need to have permanent establishment in Nigeria. This is because digital transactions by its nature does not require having a fixed base in a country where the digital non-resident companies are operating. That is why most of these digital non-resident companies carrying out digital activities to persons resident in Nigeria do not border registering with the Corporate Affairs Commission (CAC) for Identification Purposes and a lot of them do not also border registering with the Federal Inland Revenue (FIRS) for purposes of payment of taxes.

3.3. Lack of Clear-Cut Legal Framework for Taxation of Digital Economy

Prior to the advent of the Finance Act 2019, 2020 and 2021, taxation of digital non-resident companies under the digital economy was captured by the Company's Income Tax Act¹⁴ but it was drafted in line with the traditional basis of taxation, which makes it impossible to effectively monitor or properly tax companies operating in the digital economy or digital space¹⁵ meaning that having a permanent establishment in Nigeria was the basis of taxation for companies operating within the Nigeria Jurisdiction.

However, the advent of the digital economy made it possible for digital non-resident companies to conduct business or carryout digital economic activities in Nigeria without the need for a fixed base or permanent establishment thereby making the traditional basis of taxation grossly ineffective.¹⁶ This prompted the legislature and tax administrators to amend the substantive legislation, and this brought forth the Finance Act 2019, 2020 and 2021 and the Companies Income Tax Act (Significant Economic Presence) Order 2020. The Order 13 provides that a company other than a Nigerian Company, shall have significant economic presence in Nigeria, where its derives gross turnover or income of more than N25million or its equivalent in other currencies from any or combination of the following digital activities like streaming or downloading services of digital contents including movies, videos, music, applications, games and e-books to any person in

¹⁴ Companies Income Tax (Amendment) Act 2007 ss9-13

¹⁵ T. Olowoyo, Taxation of Digital Economy in Nigeria: Gaps and Realities, LPS (2022) (1) (1) <<http://Lawparillion.com> assessed on 20th September 2022.

¹⁶ Companies Income Tax (Significant Economic Presence) Order 2020 s.1(1).



Nigeria.¹⁷ It also includes transmission of data collected about Nigerian users which has been generated from such user's activities on a digital interface including website or mobile applications. Provision of goods or services directly or indirectly through a digital platform to Nigeria or using a Nigerian domain name (.ng) or register a website address in Nigeria. Provision of intermediation services through a digital platform website or other online applications that link suppliers and customers in Nigeria.¹⁸ The Finance Act 2021, also provides that the profits of a company other than a Nigeria Company from a trade or business shall be deemed to be derived from or taxable in Nigeria where it transmits, emits, or receives signals, sounds, messages, images or data of any kind by cable, radio, electromagnetic systems or any other electronic or wireless apparatus to Nigeria in respect of any activity including electronic commerce, application store, high frequency trading, electronic data storage, online advertisement, participative network platform, online payments and so on to the extent that the company has significant economic presence in Nigeria.¹⁹ For purposes of registration and payment of tax, the Finance Act 2020, provides that a non-resident person that makes a taxable supply of goods and services to Nigeria shall register for tax with the Federal Inland Revenue Service and obtain Tax Identification Number (TIN)²⁰. The Finance Act 2021, also provides that the Federal Inland Revenue Service (FIRS) may deploy proprietary or third-party technology, automate the Tax Administration Process including tax assessment and information gathering provided it gives 30 days' notice to the taxpayer²¹. The service may deploy any or third-party payment, processing or other digital platform or application to collect and remit taxes due on international transactions in the supply of digital services to and from a person in Nigeria, in the case of transactions carried out through remote, digital, electronic or other such platform²². Having seen the above provisions of the Act on taxing of digital economy in Nigeria and the digital activities carried out by that non-resident companies and persons that are chargeable to tax in Nigeria. It is clear that this is an improvement on the legal framework on taxation of digital economy in Nigeria. These legal frameworks were amended by the legislature to tackle the global challenges and the effect of Covid-19 Pandemic.

However, despite all these improvements on the legal framework for taxation of digital economy the tax authority is still faced with the challenges as a result of absence of a clear-cut legal framework.

3.4. Problem of Identification of Income and Profits of these Digital Non-Resident Companies and Persons

One of the major challenges facing taxation of digital economy in Nigeria is the problem of identifying the income and profits of these digital non-resident companies and persons. This is because digitalization allows businesses to engage in significant business activities without meeting the requirement of having a permanent establishment in Nigeria. The companies Income Tax (Significant Economic Presence) Order²³ provides that a company other than a Nigerian Company shall have a significant economic presence in Nigeria where it derives gross turn over or income of more than ₦25million Naira or its equivalent in other currencies through online activities. It is clear from the above provision of the law, that where a digital non-resident company derives income which is more than ₦25million Naira or its equivalent in other currencies through these digital activities it

¹⁷ *Ibid* s. 1(1)(i)

¹⁸ *Ibid*.

¹⁹ Finance Act 2021 s.4(c)

²⁰ *Ibid* s.43 (1); Value Added Tax Act 2007.

²¹ *Ibid* s.51 (4); Federal Inland Revenue Service (Establishment) Act s.25.

²² *Ibid* s.51(3)

²³ Companies Income Tax (Significant Economic Presence) Order 2020 s 1.



shall be deemed that the company have a significant economic presence in Nigeria and such income and profits made will be subjected to tax in Nigeria.

It therefore follows the non-resident company do not need to establish a permanent establishment in Nigeria before doing business in Nigeria. These digital economic activities need not be accompanied by a physical presence. This is because these online activities and businesses are done with intangible assets and these intangible assets are easily moved around the world through digital technologies including the satellite. This no doubt makes it increasingly difficult for the tax authority (FIRS) to identify income generated through these intangible assets.

3.5. Identification of the Digital Activities of these Non-Resident Companies and Persons.

Digital economy is an economy that is based on digital technologies, which is carried out through the internet. Under the digital economy, a lot of economic digital activities are carried out such as the electronic commerce platforms, application stores, ride hailing apps, online advertising, online payment services, cloud computing, participative network platform, etc. there are digital economic activities provided by digital service providers such as Netflix which is a streaming service that offers a wide variety of award winning TV shows, movies, documentaries, etc., a company based in California USA. Amazon is a multinational technology company that focuses on e-commerce cloud computing, digital streaming and artificial intelligence. The company is based in Washington United States²⁴. Twitter is an American communications company that operates the microblogging and social networking service²⁵. PayPal is an electronic commerce company that facilitates payments between parties through online transfers and payment. PayPal is an online payment service that allows people and businesses to transfer funds electronically and so on.

The non-resident companies and digital service providers providing digital activities unlike businesses in the traditional economy, companies that are part of the digital economy can generate significant revenue in foreign countries without the need to have a physical presence. This is because these digital activities can be carried out without physical presence or having a permanent establishment in Nigeria. And in the absence of physical presence, it may be difficult for the Federal Inland Revenue Service to fully identify all the digital activities carried out by these non-resident companies to persons resident in Nigeria.

3.6. Lack of Specialized Court

There is no specialized court that entertains tax matters in Nigeria. The Tax Appeal Tribunal established by the Federal Inland Revenue (Establishment) Act 2011²⁶, and the Tax Appeal. Tribunal Procedure Rule 2010²⁷ is a mere administrative tribunal set up to determine the correctness of assessment to tax and entertain tax matters. The Federal Inland Revenue Service (FIRS) can appeal to the tribunal against a non-resident taxpayer for non-payment of tax or for non-compliance with the provisions of the tax laws and a non-resident tax payer can as well appeal to the tribunal on challenging an assessment of tax. However, appeals from the tribunal goes to the Federal High Court. And further appeal from the Federal High Court goes to the Court of Appeal and then the Supreme Court. Tax Appeal Tribunal is not a superior court of record just like the Federal High Court. That is why all appeals from the tribunal goes to the Federal High Court as against when all appeal from the Tribunal moves straight to Court of Appeal. The Tribunal not being a superior court of record will defeat its majority objective which is to minimize the delays and bottlenecks in adjudication of tax matters and to improve the tax payer's confidence in the Nigerian tax system. When these

²⁴ R Hasting, Netflix, NETFLIX (2022) (1)(1) <<http://www.netflix.com>> accessed 25th September 2022.

²⁵ J Dorsey, Twitter, TWITTER (2022) (1) <<http://www.twitter.com>> accessed 25th September 2022.

²⁶ Federal Inland Revenue Service (Establishment) Act 2007 s 59.

²⁷ Tax Appeal Tribunal Procedure Rule 2010.



objectives are not achieved the aim or reason for the creation of the tribunal will be defeated. This is one of the major challenges facing taxation of digital economy in Nigeria. The tax Appeal Tribunal not being a court will delay the adjudication of tax matters but when the tribunal is made a specialized court it will, minimize the delays and aid in Nigeria.

3.7. Inadequate IT Experts

Most of these tax officials with the Federal Inland Revenue Service are mostly accountants and tax experts. These categories of individuals have the requisite skills for managing the present tax issues. Nevertheless, for there to be effective digitalized tax enforcement and to ensure adequate tax compliance by these digital non-resident companies and persons, the tax authority (FIRS) will require data analysts, data scientist, IT experts who have the requisite skills to manage the technology migration. The absence of these employees is one of the reasons for not adopting sufficient and adequate technology.²⁸

3.8. Distribution of Taxing Rights between Source and Resident Jurisdiction.

Most digital businesses are usually subject to their home countries (Resident) and market jurisdictions (Source). Both source and resident countries are entitled to tax the profits. This is one of the major challenges posed by taxing the digital economy. The problem of how taxing rights on income derived from cross-border trade should be allocated amongst participating jurisdictions to address under or over taxation. Given that digital transactions require little or no physical presence of the transacting parties, the income from the transaction may not be captured in the jurisdiction from where it is derived. Consequently, there is currently a mismatch between where profits are currently taxed and where and how value is created.

4. Conclusion

Globalization has seen a rapid growth in digital business transactions, especially in the provision and sale of goods and services through the Internet. These economic digital activities are done by digital resident and non-resident companies and persons with person and companies that are resident in Nigeria and these digital resident and non-resident companies and person makes a lot of profits without remitting the adequate tax due to the government.

There are impediments faced by the government and the tax authorities in taxing the digital economy in Nigeria and there are also a lot prospects in taxing the digital economy in Nigeria such as taxing the digital economy will create more revenue for the government, taxing the digital economy will widen the tax net, It will promote the practice of electronic tax administration, taxing the digital will move Nigeria from an oil based economy to a tax based economy, taxing the digital economy will reduce debt servicing by the government and , taxing the digital economy will reduce the incidence of borrowing by the Nigeria government. Be that as it may, considering the exponential growth of the global digital economy and its immense potential it becomes imperative for the government and the Nigerian tax authorities to explore more creative approach to ensure effective taxation of the digital economy in Nigeria. When this is achieved, it will create more revenue for the government and also boost the economy of Nigeria.

²⁸ A Adegoke & S. Lawal; Nigeria: Technology and Tax Administration by SBIRS in Nigeria: A Wake-Up call; KPMG [2022] (1) (1) <<http://www.mondaw.com> > accessed on 15th September 2022.



5. Recommendations

5.1. Need for a Clear-Cut Legislation for the Provision of a Digital Service Tax

There is need for enactment of a clear-cut legislation for provision of a digital service tax for digital resident and non-resident companies and persons who engage in digital activities with persons resident in Nigeria.

5.2. There is need for Legal Framework for creation of a Synergy between the Federal Inland Revenue Service (FIRS) Corporate Affairs Commission (CAC) and the Banks

There is need for a legal framework for the tax authority which is the Federal Inland Revenue Service (FIRS) to create a synergy between the Corporate Affairs Commission (CAC) and the banks in the sense that when these digital resident and non-resident companies seek for registration and incorporation of their companies the CAC will notify the FIRS. And also making it mandatory that for registration of these companies with CAC, they will be required to obtain a Tax Identification Number (TIN) with the Federal Inland Revenue Service. These legal frameworks will also help the Federal Inland Revenue Service to work with the banks in order to identify resident and non-resident companies and persons and their customers in Nigeria in doing these digital transactions. This will help in taxing these digital taxpayers under the digital economy.

5.3. The Use of Digital Technology Tools to Increase Tax Compliance

There is need for the Federal Inland Revenue Service (FIRS) to make adequate use of technology to increase tax compliance. The revenue authorities should use different ranges of technology tools, data source and analytics to increase tax compliance. This is because economic activities carried out under the digital economy are basically done through the Internet. These digital non-resident companies do not need a physical establishment in Nigeria before carrying out these digital economic activities, for that reason the revenue authority needs an advanced technology tool in order to ensure tax compliance in Nigeria.

5.4. Proper Identification of Digital Non-resident Taxpayer's Income and Resources

There is need to identify the income and resources of these taxable digital non-resident companies and persons in Nigeria. In order to achieve an effective tax administration and enforcement under the digital economy, proper identification of these digital taxpayers' income and resources must be done by the Federal Inland Revenue Service. The Tax Identification Number of these digital non-resident taxpayers should be made to reveal the income and financial status of these digital non-resident taxpayers. This will help in achieving effective taxation of the digital economy in Nigeria.

5.5. Elevation of Tax Appeal Tribunal to a Superior Court of Record

There is need for elevation of Tax Appeal Tribunal to a superior court of record. The Tax Appeal Tribunal is a mere administrative tribunal which do not have the status of a court. Appeals from the tribunal goes to the Federal High Court as a superior court of record. When the status of the tribunal is elevated to that of a superior court of record, its appeal will go straight to the Court of Appeal instead of the Federal High Court. This will no doubt aid in speedy dispensation of Justice in taxation matters.

5.6. Tax Authority Should Leverage on the Automatic Exchange of Information between Jurisdictions

There is need for the tax authority to leverage on the automatic exchange of information between jurisdictions. The Federal Inland Revenue Service should employ innovative technology to secure a proper database of the various online suppliers of goods and services. This will help the Federal Inland Revenue track tax defaulters online.