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AN OVERVIEW OF THE MAJOR CHANGES INTRODUCED BY THE FINANCE ACT TO NIGERIA'S TAX REGIME

ARTICLE SERIES

INTRODUCTION

On 13 January 2020, the President of the Federal Republic of Nigeria, His Excellency Muhammadu Buhari, assented to the Finance Bill ("the Finance Act") which made substantial amendments to the Companies Income Tax Act ("CITA"), Value Added Tax (VAT) Act ("VAT Act"), Petroleum Profits Tax Act ("PPTA"), Personal Income Tax Act ("PITA"), Capital Gains Tax Act ("CGTA"), Customs and Excise Tariff Etc. (Consolidation) Act ("CET Act"), and Stamp Duties Act ("Stamp Duties Act").

The projected revenue from the Finance Act signed by the President is expected to partly finance the 2020 budget of the Federal Government of Nigeria.

We examine some of the changes introduced by the Finance Act.

COMMENCEMENT DATE

We note that the Finance Act does not contain a commencement date for the enactments therein to come into force. In the absence of a commencement date, recourse must be had to the provisions of the Interpretation Act. In this regard, section 2(2)(a) of the Interpretation Act stipulates that where no provision is made as to the commencement date of an Act of the National Assembly, it shall come into force on the day the Act is 'passed'. Pursuant to section 2(1) of the Interpretation Act, an Act is passed when the President assents to the bill for the Act.[1]

Based on the foregoing analysis, the Finance Act came into force on 13 January 2020 being the day the President assented to it. However, the Minister of Finance has announced that the increase in the VAT rate will commence on 1 February 2020.[2]

CHANGES TO THE CITA

Digital Permanent Establishments for Foreign Companies

One of the major features of the Finance Act is the introduction of 'digital permanent establishment' for foreign companies. The Finance Act provides that a foreign company which "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 adverts, participative network platform, online payments" and which has a 'significant economic presence' in Nigeria with activities to which profit can be attributable would be subject to companies income tax ("CIT").

The Act empowers the Minister of Finance to determine, by an order, what constitutes the significant economic presence of a foreign company in Nigeria. Nigeria is a member of the Inclusive Framework on BEPS that is working with the OECD to address, amongst others, the tax challenges of the digital economy;

[1] See Omatseye v. FRN (2017) LPELR-42719(CA); and KARUMI v. FRN (2016) LPELR-40473(CA).
[2] https://www.thecable.ng/breaking-7-5-vat-to-be-implemented-from-february-1-says-finance-minister

and we understand that the Minister will adopt the definition that the OECD will accord to significant economic presence when the work on the taxation of the digital economy is finalised.

It is worthy of note that the Finance Act does not make provision for the collection and administration of CIT from foreign companies with digital PEs. We expect the Federal Inland Revenue Service ("FIRS") to publish guidelines on this. In subjecting foreign companies with digital PE to CIT, the FIRS is, however, likely to rely on the 'turnover based taxation' that allows it to tax companies on a 'fair and reasonable' percentage of their turnover. The FIRS currently deems 20% of turnover as being fair and reasonable. When taxed at the standard CIT rate of 30%, this leads to an effective tax of 6% of turnover.

Final 10% Withholding Tax on Payments to Foreign Companies

Payments to foreign companies providing technical, management, consultancy or professional services with a significant economic presence in Nigeria will attract a final withholding tax ("WHT") of 10% under the Finance Act.

Incentives for Small Businesses

Even though not elegantly worded, it appears that small businesses (i.e. with a turnover of N25million or less) are exempt from CIT, whilst medium-sized companies (i.e. with a turnover greater than N25million but less than N100 million) are to be taxed at a reduced rate of 20%.

Due Date for the Payment of CIT

The timeline for payment of CIT has now been aligned with the due date for filing tax returns – 6 or 18 months after the accounting year end for old and new companies, respectively – and CIT may be paid in a lump sum or in instalments, with the approval of the FIRS.

Furthermore, large and medium-sized companies who remit CIT 90 days before the due date will, respectively, be granted 1% and 2% of the CIT paid as a credit against future taxes.

Tax Identification Number

The Finance Act requires each company to display its tax identification number on all documents including business correspondence and correspondence with tax authorities, ministries, and government agencies.

The Finance Act also requires persons engaged in banking to require a tax identification number from companies as a condition for opening a bank account. Existing account holders have 3 months to provide their tax identification in order to continue operating the account.

Carry Forward of Losses

In the 2007 amendment to CITA, only one of the two provisions imposing a four-year limit for carrying losses forward was deleted. However, in practice, the FIRS allows an indefinite carry forward of losses for all companies, except insurance companies because CITA specifically imposed the four-year limit on them.

The Finance Act has now deleted the provisions imposing the four-year limit for all companies including insurance companies. Consequently, all Nigerian companies can now carry losses forward indefinitely.

Introduction of Thin Cap Rules

The Finance Act introduces thin capitalisation rules whereby tax deductibility of an interest expense on a related foreign-party loan is limited to 30% of earnings before interest, tax, depreciation and amortisation in any given tax year. Interest expense that is not fully utilised can only be carried forward for a maximum of 5 years.

Interest on Foreign Loans

The Finance Act has reduced the percentage of withholding tax exemptions on interest on foreign loans. The highest exemption is 70% for loans with a repayment period (including moratorium) of more than 7 years and a grace period not less than 2 years.

Excess Dividend Tax

Section 19 of CITA which imposed CIT on dividends in excess of retained earnings has been amended to eliminate double taxation that occurs where such dividends are paid from retained earnings that have been taxed and to also ensure that tax incentives are not eroded when dividends that are paid out of tax-exempt income suffer the excess dividend tax.

Consequently, CIT will no longer apply to excess dividends- (i) paid out of retained earnings that have suffered tax under CITA, PPTA and CGTA, (ii) paid out of tax-exempt income (iii) paid out of franked investment income; and (iv) paid by a real estate investment company from its rental or dividend incomes.

CIT on Interim Dividends

CIT will no longer be payable upon the declaration of interim dividends as the Finance Act repeals section 43 of CITA which imposed CIT on interim dividends.

Capital Allowance by a Company engaged in Gas Utilisation

As against claiming capital allowance on qualifying capital expenditure post the pioneer period of a company engaged in gas utilisation, the Finance Act now requires the claiming of capital allowance during the pioneer period such that only the tax written down value will be carried forward to the post-pioneer period.

Taxation of Real Estate Investment Company and Securities Lending Transactions

The Finance Act introduces frameworks for the taxation of a real estate investment company and for the taxation of companies engaged in securities lending.

CHANGES TO THE PPTA

Dividends paid out of profits that have been subjected to petroleum profits tax will now suffer withholding tax of 10%. Shareholders that are resident in a country that has signed a double tax treaty with Nigeria will, however, enjoy the reduced rate of 7.5%.

CHANGES TO THE PITA

Tax Identification Number to Open or Maintain a Bank Account

The Finance Act requires persons engaged in banking to require a tax identification number from an individual as a condition for opening or maintaining a bank account.

Deletion of Redundant Reliefs

In light of the consolidation of reliefs in the 2011 amendment to PITA, the Finance Act has deleted references to the reliefs for children and dependants.

Delivery of Notice of Objection

Tax payers can now deliver a notice of objection in response to a notice of assessment via courier or electronic mail.

CHANGES TO THE VAT ACT

VAT Rate Increase

The Finance Act increases the rate of VAT from 5% to 7.5%.

Expansion of the Scope of Taxable Goods and Services

The Finance Act clarifies and expands the scope of taxable goods and services. Goods have now been defined to include all forms of tangible properties that are movable at the point of supply, any intangible product, asset or property excluding interest in land.

Goods are to be deemed supplied in Nigeria and liable to VAT if they are physically present in Nigeria at the time of supply, imported into Nigeria, assembled in Nigeria, installed in Nigeria; or where the beneficial owner of the rights in or over the goods is in Nigeria and the goods or right thereof is situated, registered or exercisable in Nigeria.

Services are defined to include anything other than goods, money, securities and services provided under a contract of employment.

Services are to be deemed supplied in Nigeria where the services are rendered in Nigeria by a person physically present in Nigeria at the time of providing the service; or where the services are provided to a person in Nigeria, regardless of whether the services are rendered within or outside Nigeria.

Exported services

The Finance Act has provided clarity on the meaning ‘exported services’, which are exempt from VAT. An exported service is now defined as a service “rendered within or outside Nigeria by a person resident in Nigeria to a person outside Nigeria”.

Registering For VAT

As opposed to registering for VAT within 6 months from commencing business, the Finance Act now imposes an obligation on a taxable person to register for VAT immediately upon commencement of business.

Failure to register attracts N50, 000 and N25, 000 for the first and subsequent months of default, respectively.

However, the Finance Act exempts companies with less than N25million turnover from registering for VAT.

The Finance Act has re-enacted the section that required foreign companies with a physical presence in Nigeria supplying taxable services to Nigerian resident beneficiaries to register for VAT and the re-enacted section is silent on such a foreign company's VAT registration obligation. In light of this silence and due to the fact that VAT is now payable on services rendered to a resident beneficiary by a foreign company without a physical presence in Nigeria, it can be argued that foreign companies do not have an obligation to register for VAT. This is despite the fact that the obligation to register for VAT is imposed on a 'taxable person' the definition of which does not exclude foreign companies.

The Finance Act requires a taxpayer to notify the FIRS of its intention to deregister for VAT purposes within 90 days of cessation of trade or business.

Self-charging for VAT

The Finance Act provides legislative backing to the decisions of the courts imposing an obligation on a Nigerian resident beneficiary to self-charge VAT upon receiving taxable supplies from a foreign company with or without a physical presence in Nigeria and regardless of whether such foreign company issues a VAT invoice.

Excess Input VAT

As against the option of only claiming refund for excess input VAT, taxpayers can now elect to utilise excess input VAT as a credit against future taxes.

Exemption of Assets sold or Transferred during Business Reorganisation

The Finance Act provides that VAT is not payable upon the sale or transfer of assets during business reorganisation between parties who are related for at least 365 days prior to the business reorganisation, provided that such assets are not sold by the acquiring company within 365 days after the business reorganisation.

CHANGES TO THE CGTA

Exemption of Assets sold or Transferred during Business Reorganisation

The Finance Act provides that capital gains tax is not payable upon the sale or transfer of assets during business reorganisation between parties who are related for at least 365 days prior to the business reorganisation, provided that such assets are not sold by the acquiring company within 365 days after the business reorganisation.

Termination Benefits

The threshold for compensation received for loss of employment that is exempt from capital gains tax has been increased from N10,000 to N10million.

CHANGES TO THE STAMP DUTIES ACT

The definition of receipt liable to stamp duty has been expanded to cover electronic transactions, and stamp duty of ₦50 is payable on every electronic transaction or receipt in excess of N10,000.00, with the exception of own-account transfers.

CHANGES TO THE CET ACT

In a bid to incentivise local production, the Finance Act expands goods liable to excise duties to include imported goods.

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