

FINANCE BILL, 2019 AND ITS IMPACT ON NIGERIAN BUSINESSES

Background

The President of the Federal Republic of Nigeria, President Muhammadu Buhari, recently presented the Nigerian Tax and Fiscal Law (Amendment) Bill, 2019 (the Finance Bill) to the National Assembly for consideration and passage into law. The Finance Bill has been passed by the Senate and is expected to be considered by the House of Representatives, after which it is likely to receive presidential assent. The Finance Bill, by proposing various amendments to the Companies Income Tax Act (CITA), Value Added Tax Act (VAT Act), Petroleum Profit Tax Act (PPT Act), Stamp Duties Act, Personal Income Tax Act (PITA), Capital Gains Tax Act and Customs, Excise Tariff, Etc. (Consolidation) Act, seeks to achieve the following objectives:

- (a) Promote fiscal equity by mitigating instances of regressive taxation;
- (b) Reform domestic tax laws to align with global best practices;
- (c) Introduce tax incentives for investments in infrastructure and capital markets;



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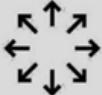
- (d) Support small businesses in line with the ongoing ease of doing business reforms; and
- (e) Raise revenue for government.

This article provides an analysis of key changes introduced by the Finance Bill in the laws highlighted above and the potential impact of the Finance Bill on Nigerian businesses. The article will also provide some recommendations on the next steps particularly with respect to the implementation of the Finance Bill.

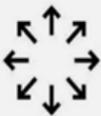
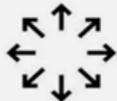
Potential Changes in Law Pursuant to The Provisions of The Finance Bill

COMPANIES INCOME TAX ACT				
 <p>Companies engaged in Digital Services</p> <p>The basis for the taxation of foreign companies is now expanded. Foreign companies providing digital services, technical, management and consultancy services with significant economic presence in Nigerian are now liable to tax in Nigeria.</p>	 <p>Commencement and Cessation Rules Deleted</p> <p>The Commencement and Cessation Rules, which application results in the double taxation of companies commencing business and companies ceasing to do business are to be removed.</p>	 <p>Re-categorisation of Companies</p> <p>Companies will be categorized as Small Companies, Medium Sized Companies and Large Companies for the purpose of computing CIT.</p>	 <p>Tax exemption for Real Estate Investment Companies</p> <p>Real Estate Investment Companies who distribute 75% of dividend and rental income within 12 months of financial year shall be exempt from tax on such dividend and rental income.</p>	 <p>Removal on the Restriction on Carrying Forward Losses.</p> <p>The time restriction of 4 years, which is applicable to unused tax losses to insurance companies and other companies will be removed.</p>

COMPANIES INCOME TAX ACT			
 <p>Small Companies</p> <p>Profits of small companies shall not be taxable under CITA.</p>	 <p>Medium-Sized Companies</p> <p>A lower rate of 20% of gross income will be applicable for Medium-Sized Companies.</p>	 <p>Thin Capitalisation Rules</p> <p>Interest payable by a Nigerian company to a foreign-connected person on money borrowed in excess of 30% EBITDA will no longer qualify as an allowable deduction.</p>	 <p>Exemption of Unit Trusts from deduction of WHT</p> <p>Unit Trust will be exempt from Withholding Tax (WHT) deduction.</p>
 <p>Amendment of minimum Tax Provision</p> <p>The minimum tax payable by a company will be 0.5% of such company's turnover in the relevant year of assessment. Also, Nigerian companies with 25% foreign shareholding now liable to Minimum Tax.</p>	 <p>Deletion of Excessive Dividend Tax provision</p> <p>Companies that do not have a taxable profit but pay dividend from the previous year's reserve will no longer be liable to tax on that dividend.</p>	 <p>Tax Exemption on interests on foreign loan</p> <p>The 100% exemption of tax payable on interest has been deleted such that the highest exemption attributable to interest on foreign loans is 70% in respect of loans above 7 years with at least 2 years moratorium.</p>	

VALUE ADDED TAX ACT			
 <p>Expansion of the scope of "supply of Goods and Services"</p> <p>The meaning of "supply of services" has been widened to include all goods whose benefactor is a taxable person in Nigeria, including goods imported, assembled or installed in Nigeria and supply of services provided to a person in Nigeria irrespective of whether the services are rendered within or outside Nigeria.</p>	 <p>Increase in VAT Rate</p> <p>VAT to be increased from five percent (5%) to seven and half percent (7.5%).</p>	 <p>Registration with the Board</p> <p>Registration with the Board with respect to VAT is now required to be done immediately upon commencement of business.</p>	 <p>Tax Returns by Taxable Persons</p> <p>Only persons who have supplied goods and services over the value of NGN25,000,000 in a given year shall be required to make Tax Returns.</p>
 <p>Default rate and interest for non-remittance of Tax</p> <p>The defaulting taxable person shall pay a default rate of 10% of non-remitted amount per annum plus prevailing interest at CBN rate plus spread.</p>	 <p>Value Added Tax Technical Committee</p> <p>Removal of the VAT Technical Committee.</p>	 <p>Penalty for failure to notify change of address</p> <p>Penalty for failure to notify a change in address is now NGN50,000 in the first month and NGN25,000 every subsequent month.</p>	 <p>Penalty for failure to submit returns</p> <p>Penalty for failure to submit returns is now NGN50,000 in the first month and NGN25,000 every subsequent month.</p>  <p>Connected Persons</p> <p>Business sale or transfer between connected persons will be VAT exempt provided the entities have been so connected for at least 365 days prior to the business reorganisation.</p>

PERSONAL INCOME TAX	
 <p>Electronic service introduced</p> <p>A taxpayer that disputes a tax assessment can now serve its notice of objection to the tax authority electronically.</p>	 <p>Gratuities payable in private sector employment now 100% tax exempt</p> <p>The years requirements an employee is needed to satisfy to qualify for gratuity and the maximum amount payable as gratuity have been removed.</p>

CAPITAL GAINS TAX ACT	PETROLEUM PROFIT TAX ACT	STAMP DUTIES ACT	CUSTOMS, EXCISE TARIFF, ETC. (CONSOLIDATION) ACT
			
CGT Exemption on Sale or Transfer of Business between Connected Persons Business sale or transfer between connected persons will be CGT exempt provided the entities have been so connected for at least 365 days prior to the business reorganisation.	Withholding Tax now applicable to dividends distributed by upstream companies The exemption from withholding tax on dividend paid by upstream companies from profits that had suffered PPT now removed.	Stamp Duty on Bank Transfer Stamp duty on bank transfer to apply only on amounts from N10,000 and above. Transfers between the same owner's accounts in the same bank are exempted.	Expansion of the scope of excise duty Goods liable to excise duty have been expanded to include both goods manufactured in Nigeria and goods exported.

Potential Impact of The Finance Bill on Businesses in Nigeria

(a) Improved Tax Regime for Small and Medium-Sized Companies

The Finance Bill introduces a new categorization of companies under both the VAT Act and CITA: (i) Small Companies, which means companies with gross turnovers of not more than NGN25,000,000.00; (ii) Medium-Sized Companies, which means companies with total turnovers of more than NGN25,000,000.00, but not more than NGN100,000,000.00; and (iii) Large Companies, which means companies with turnovers above NGN100,000,000.00. In addition, the Finance Bill seeks to introduce new tax rates applicable to each category of the companies identified above, such that Small Companies will be exempt from paying CITA and will not be required to make VAT returns with respect to goods and services rendered. Also, Medium Sized Companies will be liable to Companies Income Tax (CIT) at the rate of 20% of gross income. The proposed tax regime and rates appear to be similar to what is obtainable in other jurisdictions such as South Africa where companies pay taxes on a graduated scale, according to the overall taxable income of such companies. It is expected that this will stimulate the emergence and growth of small and medium-sized companies in Nigeria. This will in turn contribute to improving the economic indices in the country. In addition, the Finance Bill provides a relief to small companies from the rigor and cost associated with tax compliance.

Notwithstanding the above, it is important to note that employees of such small and medium-sized companies will still be subject to personal income tax on their earnings.

(b) The Basis of Taxation of Foreign Companies now Expanded

Under the current regulatory regime, we note that a certain degree of physical presence is required for a foreign company to be liable to tax in Nigeria. However, the Finance Bill has expanded the basis for taxation of foreign companies in Nigeria. The Finance Bill seeks to drag foreign companies providing digital services, technical, management, consultancy services into the Nigerian tax net where they are declared to have significant economic presence in Nigeria by the Minister.

(c) No Double Taxation – Excess Dividend Rules

Under the current tax regime, by Section 80(3) of CITA, dividends, when received by a Nigerian company, are deemed to be franked investment income and should not be subject to further tax. However, there has always been the risk that, by Section 19 of CITA, the dividends received by the Nigerian company when redistributed to its shareholders may be subject to CIT at the rate of 30% in the event that the declared dividend exceeds the company's total profit for the year or where the company did not make any profit and goes ahead to declare the dividend to its shareholders. The right of the tax authority to further subject this dividend to tax has been upheld by Nigerian Courts in plethora of cases, some of which are the case of OANDO Plc. Vs. FIRS and UAC of Nigeria Plc v FIRS. The Finance Bill now resolves this controversy such that excess dividend is to apply only to untaxed distributions other than profits specifically exempted from tax and franked investment income.

(d) Recognition of Carrying Forward Losses

One of the problems facing Nigerian companies, particularly insurance companies is the four-year time restriction beyond which such companies are not permitted to carry forward their business losses for the purposes of determining their CIT liabilities. However, CITA was amended in 2007 perhaps with a view to removing this restriction, amongst other amendments but failed to achieve this purpose. More particularly, the provision of section 16(7) of CITA that restricts insurance companies from carrying forward their losses beyond four years is not deleted. On the other hand, two provisions of CITA (which are section 31(2)(a)(ii) and (iii)) restrict other types of companies from carrying forward their losses. However, section 31(2)(a)(iii) was deleted by the CITA amendment of 2007, while section 31(2)(a)(ii) was perhaps inadvertently retained and not deleted. Going by the proposed amendment to CITA in the Finance Bill, all companies will now be entitled to carry forward their losses unrestricted.

Therefore, the proposed amendment will no doubt strengthen foreign investment incentives and encourage the growth of businesses in sectors that are not otherwise immediately profitable but profitable in the long run.

(e) Introduction of Thin Capitalisation Rules

Under the current Nigerian regulatory regime, there are no provisions on thin capitalization rules. However, the Finance Bill now seeks to introduce thin capitalisation rules such that interest on loans advanced by connected foreign companies to their Nigerian affiliates and subsidiaries will only qualify as an “allowable deduction” where such interest does not exceed 30% of earnings before interest, tax, depreciation and amortisation (EBITDA) of the Nigerian companies. The thin capitalisation rule, however, does not apply to Nigerian banks and insurance companies with foreign connected affiliates/subsidiaries. With this introduction by the Finance Bill, the tax planning practice whereby many foreign companies shift away profits from Nigeria by providing loans to their Nigerian subsidiaries (which may have no economic justification) and in return receive interest from these companies, thereby reducing the taxable profits of these Nigerian companies will be put to check or reduced.

(f) Increase in VAT Rate:

The current rate of VAT in Nigeria is 5%. However, the Finance Bill seeks to increase the rate to 7.5%. This increase will no doubt have an adverse impact on the cost of VAT-able goods and services that are consumed in Nigeria.

Recommendations

We applaud the initiative taken by the Executive to introduce the Finance Bill to, among other things, amend the tax laws and make them more responsive to the tax reform policies of the Federal Government and enhance its implementation and effectiveness. However, we advise that notwithstanding that the Executive is keen to push the said tax reforms, it is important that the National Assembly undertakes a wholistic review of all the tax laws that will be affected by the provisions of the Finance Bill. It is imperative that such review is done to ensure that there are no inconsistencies across the federal laws as a result of the amendments and introductions made by the Finance Bill. Such a review would have been easier had the amendments been made via separate amendments to the applicable tax laws e.g. an amendment to CITA, an amendment to the VAT Act, etc. However, a wholistic review is still very feasible irrespective of the format the amendments and introductions have taken, i.e. in the Finance Bill.

From an enforcement perspective, given that this is a major shift from what currently obtains, the Federal Inland Revenue Service (FIRS) will be charged with ensuring compliance by existing business entities and emerging entities particularly with respect to taxation of foreign companies engaged in digital services or technical and consultancy services with significant economic presence in Nigeria. We note that the bulk of company assessment, enforcement and compliance by the FIRS is done via physical inspection and verification of the books of companies. Therefore, given that the companies engaged in digital services or providing technical and consultancy services will not have physical presence, it is important that expertise is developed internally within the FIRS to adequately ensure compliance of the newly included taxable companies.

Furthermore, and as noted above, there may be inconsistencies and grey areas across the extant tax laws if the provisions of the Finance Bill are not thoroughly reviewed in line with all laws that may be affected. One of such grey areas is with respect to the obligations to provide VAT returns by taxable persons. The Finance Bill proposes to amend the VAT Act such that small companies will not be required to make taxable returns. This implies that such small companies may not be required to remit VAT and by implication are not entitled to charge VAT on goods and services supplied. The position of the law remains unclear given that a company or business may only realize that it falls below the threshold for making taxable returns at a later time. This means that such company may have charged VAT in the past but will not be entitled to remit or make returns to the Service in respect of such VAT received from consumers.

As such, it is our recommendation that the FIRS should be ready to issue guidelines and circulars to provide clarity and resolve any conflicts or ambiguity that may arise after the Finance Bill is signed into law.

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At such point, the question that then arises is whether a guideline or circular may in fact be capable of resolving a conflict between provisions in the tax laws or whether an amendment will then be required again. These issues underscore the importance of getting the introductions and amendments right at this stage before the Finance Bill is passed by the House of Representatives and assented to by Mr. President.

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Detail Commercial Solicitors
DCS Place, 8, DCS Street,
Off Remi Olowude Way
Lekki Phase 1, Lagos, Nigeria
+234(0) 12771400-5
www.detailsolicitors.com