THE FINANCE ACT 2019: SIGNIFICANT CHANGES TO NIGERIA'S TAX LANDSCAPE
On Monday, January 13, 2020, President Muhammadu Buhari assented to the Finance Bill 2019 (the "Finance Act") thereby giving the erstwhile bill the effect of law.

According to President Buhari through a tweet on his Twitter account, “We introduced the bill alongside the 2020 budget, to reform Nigeria’s tax laws to align with global best practices, support MSMEs in line with our Ease of Doing Business Reforms, incentivize investments in infrastructure and capital markets and raise government revenues.”

The Finance Act which was submitted to the National Assembly alongside the Appropriation Act 2020 (the “2020 Budget”) on 8 October 2019, is significant to the implementation of the 2020 Budget as the Executive hopes to increase tax revenue through various sources including: the increase in the VAT rate from 5% to 7.5%; taxation of dividends paid to shareholders of petroleum companies; widening of the tax net and strengthening of tax compliance.
KEY AMENDMENTS INTRODUCED BY THE FINANCE ACT INCLUDE

1. The increase of the VAT rate from 5% to 7.5%.

2. The removal of the exemption applicable to dividends received by shareholders of upstream oil and gas companies.

3. The exemption of small companies (companies with annual gross turnover of 25 million Naira or less) from payment of companies’ income tax.

4. The amendment of the CITA to capture non-resident companies that provide digital services within the Nigerian digital space.

5. The requirement for Tax Identification Number as a pre-condition for opening a company or business bank account or continuing operation of a company or business bank account in Nigeria.

6. The expansion of the list of VAT-exempt items to include a number of staple foods, food additives, water (including mineral water) etc.

The five strategic objectives of the Act are:

I. promote fiscal equity by mitigating instances of regressive taxation;

II. reform domestic tax laws to align with global best practices;

III. introduce tax incentives for investments in infrastructure and capital markets;

IV. support small businesses in line with the ongoing Ease of Doing Business Reforms; and

V. raise revenue for the government by various fiscal measures. This newsletter summarises the key changes introduced by the Finance Act and the potential impacts of the changes on taxpayers.

The five strategic objectives are contained in the letter from the President to the President of the Senate dated 14 October 2019 forwarding the Finance Bill to the Senate.

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KEY CHANGES INTRODUCED BY THE FINANCE ACT

SECTION A - Companies Income Tax Act

1. Expansion of Income Chargeable to Tax

Securities Lending Transactions
The Act expands the definition of interests and dividends to include payments received by a borrower or lender in a regulated Securities Lending Transaction. The Act also introduces a proviso to exclude a regulated Securities Lending Transaction from the scope of “disposal” of money market instruments.

Digital and Electronic Services
The Act expands the tax net to capture any foreign company that ‘transmits, emits or receives signals, sounds, messages, images or data of any kind In; 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...’ to the extent that the company has ‘significant economic presence in Nigeria’ (not defined in the Act) and profit can be attributable to that activity.

This is likely to create a taxable presence for companies streamlining digital content into Nigeria, companies providing technology, management, consultancy, financial or other services online to Nigerian residents etc.

2. Tax Identification Number required to open/operate a Bank Account

The Act imposes a requirement on banks to collect tax identification number (TIN) as a precondition for opening a bank account and for existing companies, as a condition for continued operation of such bank accounts.

Prior to the passage of the Finance Act, in practice, banks requested for TINs prior to the opening of corporate bank accounts. The introduction of this requirement in the Finance Act is meant to formalize the practice and make it mandatory rather than discretionary. This will ensure that business transactions are easily linked to a taxable person and it is also expected that this would assist the Federal Inland Service in its bid to widen the tax net.
3. Insurance Companies

Section 16 (5) (b) (ii) restricts the investment income which is to be reckoned in tax computation to shareholders' funds. The Act also removes the four-year limit for carrying losses forward.

The Act substitutes the old provisions which limited tax deduction from premium for unexpired risks to 45% of the total premium for general insurance and 25% for marine cargo insurance with a provision allowing tax deductions to be computed on a time apportionment basis.

Section 16 (8) (b) substitutes the old provisions which limited tax deduction for outstanding claims and outgoings to 25% of the total premium with a provision allowing tax deductions to be computed on the total estimated amount of all outstanding claims and outgoings with a further 10% for unreported claims for the year under review. Provided that any unutilised amounts will be added back to profits in the following year.

Section 16 (9) (c) is amended to remove restriction on allowable business outgoings in computation of deductions allowed from the income generated from life insurance business.

4. Tax on Payment of Dividend in Excess of Profits

The previous provision had led to concerns and complaints of unauthorised double taxation and was seen as penalising companies which distribute dividends in a year subsequent to the year that the profit is earned. In one case (Oando v. FIRS) where the dividend declared exceeded the profits because of post-tax earnings retained from previous years, the Court held that in the absence of an express exemption of such earnings, they were subject to tax under section 19 notwithstanding that the same income was being taxed a second time in the hands of the same taxpayer.

The new subsection 2 resolves all the controversies arising from this provision by specifically excluding the following from the provision of section 19 (1):

(i) Dividends paid out of retained earnings previously taxed under CITA, PPTA, or CGTA;
(ii) Dividends paid out of income that is tax exempt under CITA, PPTA, or CGTA;
(iii) Profits or income regarded as franked investment income under CITA; and
(iv) Distributions made by a Real Estate Investment Trust.

The similar provision with respect to foreign companies in section 20 (b) (c) has now been deleted.
5. Expansion of the list of Tax-Exempt Profits

The Act expands the scope of tax-exemption in Section 23 of the CITA through the following amendments:

Profits of companies with annual turnover of N25 million or less exempt from tax

Section 23 (1) (o) exempts profits of small companies (companies with annual turnover of N25 million or less) from tax, as well as the dividends received from a small company engaged in manufacturing within the first 5 years of operation. This seeks to encourage small and medium enterprises by excluding these companies from the income tax net.

Tax exempt profits restricted to proportion of export proceeds used in purchasing assets

The Act substitutes the current provision with a new provision which restricts the tax exempt profits to that proportion of export proceeds actually utilised in purchasing raw materials, plant, equipment and spare parts.

Exemption of dividends and rental income received by a Real Estate Investment Company

Section 23 (1) (t) exempts the dividend and rental income received by a Real Estate Investment Company on behalf of its shareholders provided that at least 75% of the dividend or income is distributed within 12 months of the financial year in which the dividend or income was received.

Exemption of compensating payments received in a Regulated Securities Lending Transaction

Section 23 (1) (u) exempts the compensating payments received by a Lender from an approved agent or Borrower under a Regulated Securities Lending Transaction which qualify as dividends under section 9 (c) of CITA. Section 23 (1) (v) also exempts the compensating payments received by an approved agent from a Lender or Borrower under a Regulated Securities Lending Transaction which qualify as dividends under section 9 (c) of CITA.
6. Deductions Allowed

The WENR Test

In Section 24 of the CITA, the words “chargeable to tax” are added after the wholly, exclusively, necessarily and reasonably (“WENR”) test. The new provision will now read as:

Save where the provisions of subsection (2) or (3) of section 14 or 16 of this Act apply, for the purpose of ascertaining the profits or loss of any company of any period from any source chargeable with tax under this Act, there shall be deducted all expenses for that period by that company wholly, exclusively, necessarily and reasonably incurred in the production of those profits chargeable to tax.

The stated objective of this amendment (as can be gleaned from the side note in the Act) is to avoid shifting operating costs to the part of the business that produces the taxable profits and thereby artificially reduce taxable profits. It is not clear that the amendment can attain the stated objective.

Deductibility of Interest Income

The Act introduces a provision which provides that the deductibility of interest income is subject to the provisions of the Seventh Schedule (the new Schedule on thin capitalisation Rules) of CITA.

Distributions made by a Real Estate Investment Company

The Act introduces a new Section 24 (k) which allows the deductibility of dividends or mandatory distributions made by a Real Estate Investment Company to its shareholders as approved by the Securities and Exchange Commission.

Compensating payments made under a Securities Lending Transaction

The Act introduces a new Section 24 (l) which allows the deductibility of compensating payments made by a Lender to its approved agent or Borrower under a Regulated Securities Lending Transaction which qualify as interest under section 9 (c) of CITA.
7. Deductions not Allowed

Expenses Incurred between Related Parties

Section 27 (g) disallows the deductibility of expenses incurred in or outside Nigeria between related parties which are inconsistent with the Transfer Pricing Regulations.

Expenses Incurred in generating Tax-Exempt Income etc.

Section 27 (h) disallows the deductibility of expenses incurred in generating tax-exempt income, capital losses or expenses deductible under the CGTA.

Compensating payments made by a Borrower under a Securities Lending Transaction

Section 27 (i) disallows the deductibility of any compensating payments made by a Borrower to its approved agent or Lender under a Regulated Securities Lending Transaction which qualify as dividend under section 9 (c) of CITA.

Compensating payments made by an Agent under a Securities Lending Transaction

The Act introduces a new provision which disallows the deductibility of any compensating payments made by an approved agent to a Borrower or Lender under a Regulated Security Lending Transaction which qualify as interest or dividend under section 9 (c) of CITA.

Penalty in any Act of the National Assembly

The Act introduces a new provision which disallows the deductibility of any expense incurred as penalty prescribed by/in any Act of the National Assembly for violation of any statute. This amendment brings much desired clarity as there has been some controversy as to the deductibility of such expenses which arguably satisfy the WENR test.

Taxes or Penalty borne on behalf of another person

The Act introduces a new provision which disallows the deductibility of any tax or penalty borne by a taxpayer on behalf another person.

8. Duration of Control in determining tax on transfer/reorganisation

Section 29 (9) has been amended to introduce a new requirement which provides that in order for a company to qualify as a controlling company and to be able to take advantage of the subsections 3 and 4 of section 29, the controlling entity must have been in control for at least 365 days preceding the reorganisation of the business. Similarly, where a purchaser of a business sells the business within 365 days of the purchase, it will lose any concessions enjoyed under the purchase transaction.
9. Duration of carrying of losses

Four Year restriction removed

Section 31 (2) (a) (ii) has been amended to remove the four-years restriction on carrying forward losses.

10. Payment of minimum tax

Simplified Minimum Tax rate

The Act introduces a simplified rate of minimum tax set at 0.5% of gross turnover.

Exemption of Small Companies from Minimum Tax

Section 33 (3) (b) has been amended to exempt small companies (companies that earn gross turnover of less than 25 million naira in a year of assessment) from payment of minimum tax.

11. Revised Tax Rates

Small Companies exempt from Income Tax

The Act exempts small companies (companies with an annual gross turnover of 25 million naira or less) from income tax.

Tax Rate for Medium Companies

The Act prescribes a tax rate of 20% for medium companies (companies with gross turnover of more than 25 million naira and less than 100 million naira).

30% Tax Rate now applicable to only Large Companies

The 30% tax rate now applies to only large companies (a company that is neither a small company nor a medium company).

12. Increase of Penalty for delay in filling returns

The provisions of section 55 (3) (a) and (b) have been amended to increase the penalty for delay in filing tax returns from N25,000 for the first month of default to N50,000 and from N5,000 for every subsequent month of default to N25,000. It is expected that these higher penalties will foster voluntary compliance with filing obligations.

13. Deduction of WHT at Source

The provisions of section 78 and 80 have been amended to confirm that the payments made under a Regulated Securities Lending Transaction and distributions made by a Real Estate Investment Trust Company respectively will not be subject to WHT.
14. Reduction of the rate of tax exemption on interest on Foreign Loans

The provisions of the Third Schedule have been amended to reduce the rate of exemptions on interest on foreign loans. The Third Schedule previously provided as follows:

<table>
<thead>
<tr>
<th>Repayment Period including Moratorium Allowed</th>
<th>Grace Period</th>
<th>Tax Exemption Allowed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Above 7 years</td>
<td>Not less than 2 years</td>
<td>100%</td>
</tr>
<tr>
<td>5-7 years</td>
<td>Not less than 18 months</td>
<td>70%</td>
</tr>
<tr>
<td>2-4 years</td>
<td>Not less than 12 months</td>
<td>40%</td>
</tr>
<tr>
<td>Below 2 years</td>
<td>NIL</td>
<td>NIL</td>
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The revised schedule is as follows:

<table>
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<td>40%</td>
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<tr>
<td>2-4 years</td>
<td>Not less than 12 months</td>
<td>10%</td>
</tr>
<tr>
<td>Below 2 years</td>
<td>NIL</td>
<td>NIL</td>
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</tbody>
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15. Thin Capitalisation Rules

The Act introduces a new schedule which contains provisions disallowing ‘excess interest’ (more than 30% of EBITDA of the Nigerian company) payable on a foreign loan with a connected person (other than a company engaged in banking or insurance business). The interest expense shall not be carried forward for a period exceeding 5 years from the year the excess interest was first incurred. A violation of the provisions of the Schedule shall be punishable by 10% penalty and interest at the CBN monetary policy rate and a spread to be determined by the Minister of Finance computed on any adjustment made by the FIRS on the excess interest.
SECTION B - Petroleum Profits Tax Act

Deductibility of WHT on dividends payable by a PPT company

The provision of section 60 which excludes ‘income or dividends paid out of any profits which are taken into account’ under the PPTA from any other tax under any other statute has been repealed.

This provision was the cause of some controversy and litigation over whether WHT was deductible on dividends paid out of the dividends payable by a PPT company. This amendment will avert such controversy from occurring in future.

SECTION C – Personal Income Tax Act

1. Updated References to the Federal Inland Revenue Service

The Act amends various references to the Federal Board of Internal Revenue or the Board to refer to the Federal Inland Revenue Service and the Service. This amendment will bring the Act up to date and in accordance with the practical realities.

2. Provision Requiring Permission of the Federal Inland Revenue Service for Pension Schemes Deleted

The provision of section 20 (1) (g) which required the approval of the Board (the FIRS) for pension schemes has been deleted.

3. Deduction of allowances for family members

The provisions of section 33 (4) (5) and (6) which provided for allowances for family members have now been deducted to avoid the controversy arising from the retention of these provisions following the enactment of the Consolidated Relief Allowance in 2011 amendments to PITA.

4. Obligations on banks to Require Tax Identification Number for business accounts

The Act introduces an amendment to section 49 by the introduction of a new subsection (1) which imposes an obligation on banks to require the tax identification number for the opening of any business account. This amendment will facilitate the data collection for sole proprietorship businesses which will aid the expansion of the tax net.

5. Delivery of Notices of Objection

The Act introduces an amendment to section 58 to permit notices of objection to be delivered by courier service and electronic mail. This amendment will bring the taxpayers at par with the tax authorities who are already permitted to serve notices of assessment by courier and electronic mail under section 57.
SECTION D – Value Added Tax Act

1. Expanded Scope of Supply

Section 2 is amended to expand the scope of when a supply will be deemed to have been made in Nigeria. In respect of services, a supply will be deemed to be made in Nigeria where the recipient is a person in Nigeria irrespective of whether the services are rendered inside or out of Nigeria. This amendment will avert controversies arising from the current provisions which are silent on supplies made outside Nigeria to a Nigerian resident.

2. VAT rate Increased

Section 4 has been amended to increase the VAT rate from 5% to 7.5%.

3. Registration Period for New Businesses Reduced

The Act introduces an amendment to section 8 reducing the registration period for a new business from the current six months to ‘upon commencement’ which suggests that the obligation to register for VAT is immediate upon commencement of business. The penalty for delay in registration has been increased from N10,000 for the first month of default to N50,000 and from N5,000 for every subsequent month of default to N25,000.

In view of the increased penalty, it is recommended that a specific duration e.g. 2 weeks be imposed for a new business to register for VAT as such a specification will accord with the objective of fairness and clarity in tax statutes.

4. Non-Resident Suppliers to include VAT in Invoices

The Act mandates a non-resident supplier to include VAT in its invoices, but the Nigerian purchaser is to withhold and remit the VAT amount directly to the FIRS. Where the non-resident supplier fails to issue a VAT invoice, the Nigerian purchaser is to self-assess and remit the VAT amount to the FIRS. This will avert controversies as to whether the issuance of an invoice is a condition precedent to VAT liability which has been the cause of litigation.

5. Remittance of VAT by a Nigerian Supplier

The Act introduces an amendment to Section 15 to the effect that the trigger for remittance of VAT by a Nigerian supplier would be a cumulative supply of N25,000,000 in a calendar year. It is not clear if the trigger will mean that all subsequent supplies in that year will be liable to VAT or once the trigger is met then even prior supplies within the calendar year become subject to VAT.
6. Penalty rate for non-remittance or delay increased

The Act increases the penalty rate for non-remittance/delay in remittance of VAT from 5% to 10%.

7. Change in Penalties

The provisions of sections 28 and 35 have been amended to respectively: (a) increase the penalty for default in notifying the FIRS of a change in address; and (b) failure to submit returns from a flat rate of N5,000 to a rate of N50,000 for the first month of default and N25,000 for every subsequent month of default. It is expected that this will boost compliance.

8. Transfer of assets between Related Companies

Section 42 is a new provision introduced to expressly exclude transfer of assets between related companies for reorganisation from VAT. However, to enjoy the exemption, the related companies must have been so related for at least 365 days preceding the date of the transaction. Where the acquiring company further transfers the assets within a period less than 365 days from the date of the transfer, the exemption shall be rescinded and VAT payable as if there was no exemption.

9. Definition of Goods to include intangibles

The Act amends Section 46 particularly the definition of goods to include any intangibles assets or property over which a person can exercise ownership, or from which a benefit can be derived which can be transferred from one person to another other than interests in land. The amendment addresses the issue that was considered by the Court in cases like CNOOC v. AGF & Others [2013] NTLR 88 where the question of VAT over the disposal of an interest in an oil mining lease was disputed.

10. Definition of Exported services

The Act defines exported services as a service rendered within or outside Nigeria to any person resident in Nigeria to a person resident outside Nigeria. Provided that a service provided to the fixed base or permanent establishment of a non-resident in Nigeria shall not qualify as an exported service.

11. Definition of ‘basic food items’ expanded

The Act expands the definition of ‘basic food items’ to include a long list of staple foods, food additives, water including mineral water etc. This amendment will avert a controversy over the scope of the VAT exemption on food items which had even led to litigation such as the decision in Monamer Khod Enterprises Nig. Ltd. & Anor v. FIRS & 2 Ors. Suit No. FHC/CS/1/2004 where it was held that VAT is chargeable on bottled water.
An amendment is made to the provisions of the 5th Schedule to include “goods imported” into Nigeria in order to incentivise local production.

SECTION F – Capital Gains Tax Act

1. Exemption on Takeovers and Business Combinations amended

The Act substitutes the provisions of Section 32 which previously exempted the gains arising from the acquisition of the shares of a company through a takeover or merger (as a result of which the acquired company loses its identity as a limited company) provided that no cash payment is made in respect of the acquired shares.

In place of the old Section 32, the Act introduces a new provision which excludes the transfer of assets between related companies for reorganisation from Capital Gains Tax. However, to enjoy the exemption, the related companies must have been so related for at least 365 days preceding the date of the transaction. Where the acquiring company further transfers the assets within a period less than 365 days from the date of the transfer, the exemption shall be rescinded and CGT payable as if there was no exemption.

2. Compensation for Loss of Office

The Act increases the limit of the exempted amount from the current N10,000 to N10,000,000. This provision is a fair allowance to taxpayers and a recognition of the value of the Naira.

3. Updated language on the Federal Inland Revenue Service

Section 46 (1) is amended so that all references to the Board are amended to refer to the Federal Inland Revenue Service and the Service. This amendment will bring the Act up to date and in accordance with the practical realities.
SECTION G – Stamp Duties Act

1. Definitions extended to include electronic documents

The Act amends the definition provisions in section 2 to the effect that the definition of ‘stamp’ and ‘stamped’ will include an electronic acknowledgement for denoting any duty or fee. The definition of ‘instrument’ includes electronic documents.

2. Receipts

The provision of section 89 has been deleted and replaced by a new provision which provides in section 89 (1) that a receipt will include any ‘electronic inscription whereby any money, or any...’ is acknowledged as received, paid, satisfied or discharged. This amendment will bring the provisions of the Stamp Duties Act in line with modern realities of electronic commerce and business practices. The new section 89 (2) provides that a receipt may be by a ‘digital tag with electronic stamp...’

The new section 89 (3) provides that notwithstanding any other provisions of the SDA, electronic receipt for money deposited with any bank (to a 3rd party account) in the sum of N10,000 and upwards will be chargeable with a singular one-off duty of N50.

The new section 89 (4) provides that any duty charged under subsection (1) to (3) shall be a credit against duty payable by way of adhesive stamp.

The schedule to the SDA has also been amended to include an exemption for receipts issued in Regulated Securities Lending Transactions.

Save where the provisions of subsection (2) or (3) of section 14 or 16 of this Act apply, for the purpose of ascertaining the profits or loss of any company of any period from any source chargeable with tax under this Act, there shall be deducted all expenses for that period by that company wholly, exclusively, necessarily and reasonably incurred in the production of those profits chargeable to tax.
The provisions in the Finance Act 2019 reflect many of the above strategic objectives and will go a long way in resolving many of the controversies and challenges arising from various provisions in the Companies Income Tax Act, Value Added Tax Act, Personal Income Tax Act, Capital Gains Tax Act, Stamp Duties Act, Petroleum Profits Tax Act and the Customs, Excise and Tariffs (Consolidation) Act. The proposed amendments will also promote fairness, facilitate ease of compliance and cost of data collection.
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