

POLICY IMPLICATIONS OF FINANCE ACT 2020: TOWARDS TAX POLICY REFORMS AND ECONOMIC RECOVERY

Dr. (Mrs.) Titilayo Eni-Itan Fowokan B.Ed. (Maths.), FCA,
FCTI, LLM (Int. Bus. Law), Ph.D. (Accounting), FCNA, CFE,
FFAR, ACIS



Content

- Introduction
- Highlights of Key Provisions of FA 2020
- Tax Policy Implications of FA 2020
- Implications of SEP Provisions
- SEP and Digital Economy
- SEP and Free Zone Enterprises
- Conclusion & Recommendations

Introduction

- The Finance Act, 2020 which supports the **2021 Budget of Economic Recovery & Resilience**, came into effect together with the 2021 Appropriation Act, on 1st January 2021.
- Finance Act, 2020 seeks to implement Macroeconomic & Fiscal Policies to:
 - Attract & retain Foreign and Domestic Investment (FDI) in critical sectors;
 - Foster Inclusive, Sustainable & Diversified Economic Recovery & Growth;
 - Create Jobs to create wealth and reduce income inequalities; and
 - Provide immediate fiscal strategies for accelerated Domestic Revenue Mobilization, in response to the COVID-19 Pandemic & global economic downturn.
- The Finance Act, 2020 is structured across five (5) broad Thematic Areas:
 - 1) Institutionalizing ease of doing business (EODB) reforms
 - 2) Enacting counter-cyclical measures & crisis intervention initiatives
 - 3) Reforming fiscal incentive policies for job creation
 - 4) Introducing tax, fiscal responsibility & public procurement reforms
 - 5) Ensuring closer coordination of monetary, trade & fiscal policies

Highlights of Key Provisions of FA 2020 (I)

- 1) Education Tax exemption for micro & small businesses
- 2) Clarification of CGT exemption on compensation for loss of Office
- 3) Exemption of all low-income earners of Minimum Wage from PIT
- 4) Revision of Commencement and cessation rules for Individual
- 5) VAT exemptions - Land, Air ticket by Nigerian registered commercial airlines, Aircraft, Animal feeds, Agric equipment
- 6) Introduction of Significant Economic Presence for NRI
- 7) Reduction of duty – Tractors, Mass Transit (>10persons), Cars
- 8) 50% reduction in MINTAX for 2Years
- 9) Synchronization of filing, payment & penalties deadline

Highlights of Key Provisions of FA 2020 (2)

- 11) Codification of donations for COVID & Subsequent disaster relief fund
- 12) Revision of reporting framework for companies and entities in the FTZs
- 13) Definitions Gross turnover, Nigerian company, Public character, Goods, Services, Exported services, Board, etc.
- 14) Introduction of excise duties on telecommunication services
- 15) Redesignation of the Electronic Money Transfer Levy
- 16) Changes to the framework for the taxation of the Insurance Sector
- 17) Dedicated tax refund account for each tax type
- 18) Revised framework for the taxation of NRCs.

Highlights of Key Provisions of FA 2020 (3)

- 19) Introduction of Unclaimed dividends (Plc.) and Unutilized bank balance Fund
- 20) Establishment of the NGN500bm Crisis Intervention Fund
- 21) Revision to the Contribution to Retirement Benefit Scheme
- 22) Service of notice of assessment and objection can now be done via Email
- 23) Introduction of virtual sitting at the TAT
- 24) Extension of Public Procurement Act (PPA) to - Legislature & Judiciary
Increase in Mobilization Fee thresholds to 30%
- 25) 50% Cost-to-Revenue Ratio introduced for State-Owned & Government-Owned Enterprises Direct deduction from TSA or other accounts SOEs / GOEs may be made

FA 2020 Provisions with Tax Policy Implications

- FA 2020 amendments that has tax policy implications include:
 - **Taxation of the digital economy with the introduction of Significant Economic Presence (SEP) for both non-resident companies (NRCs) and individuals (NRIs).**
 - Automation of tax administration processes
 - Introduction of virtual tax meetings and TAT sitting
 - Acceptance of electronic correspondences for tax purposes
 - Revision of reporting framework for companies and entities in the FTZs
 - Creation of dedicated tax refund accounts for each tax type
 - Codification of donations for COVID & Subsequent disaster relief fund

Implications of SEP Provisions (I)

- Introduction of SEP Provisions in FA 2019 and 2020 is focused on achieving effective tax collection in a digital economy.
- Coverage of SEP includes:
 - digital economy (covering E-commerce, App stores, Online adverts, **Cloud computing, Network participative platforms, High frequency negotiation, Online marketing, Online payment systems)
 - EPC contracts (covering surveys, construction, deliveries, installation, etc.)
 - Technology Transfer (licensing, software maintenance services, etc.)
 - Assignment of intellectual property rights, etc.
 - Cross border professional services by non resident individuals
 - Provision of technical (including advertising services, training, or the provision of personnel), professional, management, or consultancy services to customers in Nigeria.

Implications of SEP Provisions (2)

- A NRC involved in digital transactions will meet the SEP threshold in Nigeria if:
 - 1) it derives gross turnover or income in excess of ₦25 million (about USD65k) in any year, including activities carried on by the NRC's connected persons during the accounting year; or
 - 2) it uses a Nigerian domain name (.ng) or registers a website in Nigeria; or
 - 3) it has a purposeful and sustained interaction with persons in Nigeria by customizing its platform to target persons in Nigeria (e.g. by reflecting prices of products/services in Naira, providing options for billing or payment in Naira etc.).
- A NRC that provides technical, professional, management or consulting services will have a SEP in Nigeria, if it earns income or receives payment from:
 - 1) a person resident in Nigeria; or
 - 2) a fixed base or agent of a non-Nigerian company.
- For this category, the withholding tax deducted by the Nigerian service recipient is the final tax. This does not apply to employment or teaching services.

Implications of SEP Provisions (3)

- Introduction of SEP requires that NRCs carrying on business, or having a fixed base of business, or having a dependent agent, or having significant economic presence in Nigeria are required to prepare full audited financial statements of their Nigerian operations, which must be certified by a Nigerian independent auditors and submitted along with their income tax returns to the Federal Inland Revenue Service.
- Also, NRIs that has SEP, are required to report their income from technical, management and consultancy services provided to a person (natural or legal) resident in Nigeria, and pay the tax liable in Nigeria. Furthermore, they are required to file tax returns in Nigeria, apart from the deduction of 10% withholding tax at source by their Nigerian clients.

Implications of SEP Provisions (3)

- In practical terms, where the NRCs sell their products and services directly to individual consumers in Nigeria, deduction of WHT and application of reverse VAT charge will be an issue.
- Enforcement of compliance by NRCs and NRIs may be a challenge where there are no international consensus on the application of SEP Provisions on NRCs and NRIs.
- Considering that the NRCs and NRIs are not physically present in Nigeria, the burden of the tax will most likely falls on the Nigerian beneficiary of their services which negates the ease of doing business objective of government as the tax costs impact on taxable profits, either as a deduction or as non-allowable deduction (which is arguable).
- The SEP order expands the meaning of technical services to include advertising and training services as well as the supply of personnel but this does not seem to align with the provisions of FA 2019.

SEP and Digital Economy (I)

- Digital economy is characterized by:
 - Complex business models, cross border activities, advanced technology and innovation, and inability to physically attribute taxable presence to jurisdiction of income generation.
- The structure of digital economy pose challenges for effective taxation which includes:
 - Significant profit generation from remote online transactions without a physical presence
 - Difficulty in attributing value to data generated from users through the online platform
 - Challenges with real-time tracking of e-business transactions to determine the tax-point
 - Current VAT collection system is not effective for e-business services and intangibles
 - Difficulty in tracking the relocation of functions, risks and assets related to IP and intangibles from high-tax jurisdiction to low-tax jurisdiction

SEP and Digital Economy (2)

- The implication of the complexities and challenges of digital economy is that its taxation is not as straight forward as imagined. It requires a total change in taxation modalities of the country and understanding of the intricacies of digital services and digitalized businesses with global networks.
- Determination of the taxation point and jurisdiction with the taxing right is critical to the application of taxing rules on such transactions considering that it is usually across borders. Thus, there may be challenges with attribution of the Nigerian SEP of NRCs considering that the SEP Order 2020 does not address this.
- Where an NRC is covered by any multilateral agreement or consensus arrangement to address the tax challenges arising from the digitalization of the economy, to which Nigeria is a party, the provisions of that agreement or arrangement will apply. This effectively means overriding the SEP Order.
-

SEP and Free Zone Enterprises (FZE)

- The amendment to section 53 of CITA affects an FZE as follows:
 - makes it mandatory for companies exempted from tax (including free zone or export processing zone enterprises) to maintain accounting records and prepare certified accounts in English language. Translation of foreign language records to English language is at the cost of the concerned taxpayers.
 - Non-compliance with the above attracts a penalty of N100,000 in the first month in which the failure occurs, and N50,000 for each subsequent month in which the failure continues.
 - The provisions on objection will apply to any disagreement with the FIRS directive on this compliance obligation.
- Can an FZE create SEP by virtue of its transactions with companies outside the Zone? If yes, it is not clear if the above amendment to section 53 of CITA extends to deduction of WHT and application of reverse VAT charge on such transactions. Where this is the case, government's objective for creation of economic zones is jeopardized.

Conclusion & Recommendations

- Government's focus on taxation of digital economy using the SEP Order 2020 is a step in the right direction but there is a lot to be done for effective implementation of the order as intended due to the complexity of the digital services space.
- Considering that SEP applies to NRC providing digital services, there is need to address the potential disparity between NRCs and domestic digital services providers.
- For effective implementation of the SEP Order 2020 and to drive compliance by NRCs and NRIs, government need to leverage on international collaboration towards consensus-based approach to taxation of digital economy.
- The SEP Order 2020 should be reviewed to ensure that provisions related to the basis for attribution of NRC's profits to SEP in Nigeria are included for clarity and easy administration.
- Digitalization of the economy has cross border implications and as such there is need to review the existing tax treaties and bilateral arrangements for alignment with the current realities.