

**COURSE  
GUIDE**

**ACC 318  
ADVANCED TAXATION**

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<b>CONTENTS</b>	<b>PAGE</b>
Introduction.....	iv
Course Aim.....	iv
Course Objectives.....	iv
Working through this Course.....	iv
Course Materials.....	v
Study Units.....	v
Textbooks and References.....	v
Assessment.....	vi
Tutor- Marked Assignments.....	vi
Final Examination and Grading.....	vii
Course Overview/Presentation.....	vii
How to Get the Most from this Course.....	viii
Facilitators, Tutors and Tutorials.....	ix
Summary.....	x

## INTRODUCTION

ACC 318 is a 300- level second semester course. It introduces you to advanced taxation. This is an adaptation of the **ICAN STUDY PACK**.

## WHAT YOU WILL LEARN IN THIS COURSE

This course guide tells you briefly what to expect from reading this course. The study of financial accounting is to familiarise you with this subject matter which is dealt with herein and of which are expected to know much about after reading through

## COURSE AIMS

The aim of the course is to help the learner become reasonably well-informed about financial accounting. It will also enable you to have the knowledge and skill of analysing, computing and assessing different organisations for taxation purposes.

## COURSE OBJECTIVES

The major objectives of this course, as designed, are to enable the students to know all the relevant enactments and legislations in relation to assessment and taxation in Nigeria. As well, students should be able to:

- discuss in detail the rationale behind imposition of taxation in Nigeria
- explain the term “tax investigation”
- describe the stages of tax investigation
- explain the jurisdiction tax appeal tribunal
- discuss the particulars contained in the notice of appeal against an assessment of a tax payer?
- describe what is meant by right to legal representation by a tax payer
- compare tax avoidance with tax evasion
- distinguish between earned and unearned incomes of individuals
- explain the various incomes that are chargeable or exempted from personal tax
- enumerate the principles of allowable and disallowable expenses or deductions
- identify the reliefs and allowances that are deducted before arriving at the chargeable income for the relevant years of assessment
- differentiate between withholding tax and value added tax
- enumerate the problems of administering withholding tax in Nigeria
- define value added tax
- list the goods and services that have been exempted from value added tax
- enumerate the functions of VAT committee and tribunal
- explain how an agent is appointed
- explain the term capital allowances

- list and explain the types of capital allowances
- define and discuss the concept leasing assets.

## **WORKING THROUGH THIS COURSE**

For you to excel in this course, you are required to carefully read each unit, and understand the contents. You are also required to attempt each unit self-assessment exercises and submit your assignment for assessment purposes. Apart from studying the course material on your own, you also need to attend tutorial sessions for exchange of ideas with your Facilitator.

You are expected to compile the questions that bug you and the grey areas in the course materials and bring these for discussion with fellow learners and the Facilitator. You are expected to carve out specific time each day, every day for your study. Try to form good study habits. Remember that you are a self-learner. In other words, you are on your own. If you study hard every day and do your assignments, you will achieve your goal.

## **COURSE MATERIALS**

You will be provided with the following materials:

- Course Guide
- Course Material containing Study Units
- Assignment File

## **STUDY UNITS**

The 18 study units structured into 3 modules in this course are as follows:

### **MODULE 1**

Unit 1	Taxation, Revenue Authorities and Ethical Issues
Unit 2	Tax Audit and Investigation
Unit 3	Tax Appeal Tribunal and Interpretation of Tax Laws
Unit 4	Tax Planning and Tax Avoidance
Unit 5	Taxation of Incomes: Offences and Penalties
Unit 6	Taxation of Income from Settlement, Trusts and Estates

### **MODULE 2**

Unit 1	Withholding Tax
Unit 2	Value Added Tax
Unit 3	Capital Allowances
Unit 4	Capital Gains Tax
Unit 5	Tax Effects of Privatisation and Commercialisation
Unit 6	Profits, Assessable Profits and Tax Payable

**MODULE 3**

Unit 1	Person Chargeable, Offences and Penalties
Unit 2	Tax on Special Businesses
Unit 3	Petroleum Profit Tax
Unit 4	Stamp Duties
Unit 5	Tax Planning and Tax Administration
Unit 6	Tax on Pioneer Industries

All these units are demanding. They also deal with basic principles and values, which merit your attention and thought. Tackle them in separate study periods. You may require several hours for each.

We suggest that the Modules be studied one after the other, since they are linked by a common theme. You will gain more from them if you have first carried out work on the scope of Family Law generally. You will then have a clearer picture into which to paint these topics. Subsequent courses are written on the assumption that you have completed these units.

Each study units consists of one week's work and includes specific objectives, directions for study, reading materials and self-assessment exercises. Together with tutor-marked assignments, these exercises will assist you in achieving the stated learning objectives of the individual units and of the course.

**ASSESSMENT**

There are two types of assessment for this course: the tutor-marked assignment, and the end of course examination.

In tackling the assignments, you are expected to apply information, knowledge and techniques gathered during the course. The assignments must be submitted to your tutor for formal assessment in accordance with the deadlines stated in the presentation schedule and the assignment file. The work you submitted to your tutor will count for 30% of your total course mark.

At the end of the course, you will need to sit for a final written examination of 'three hours' duration. This examination will also count for 50% of your total course mark.

**TUTOR-MARKED ASSIGNMENTS**

There is a tutor-marked assignment at the end for every unit. You are required to attempt all the assignments. You will be assessed on all of them but the best three performances will be used for assessment. The assignment carries 10% each.

When you have completed each assignment, send it together with a TMA form, to your tutor. Make sure that each assignment reaches your tutor on or before the deadline. If for any reason you cannot complete your work on time,

contact your tutor before the assignment is due to discuss the possibility of an extension. Extensions will not be granted after the due date unless under exceptional circumstances.

## FINAL EXAMINATION AND GRADING

The end of course examination carries 70% of the total score for the course. You will be notified of the time of the examination. You should prepare thoroughly for the examination by studying very hard. You should also submit yourself for the examination.

The table below lays out how the actual course marks are broken down:

ASSESSMENT	MARKS
Assignment 1 – 4 (TMAs) (the best three of all the assignments submitted)	Four assignments. Best three marks of the four count at 30% of course marks
Final Examination	70% of overall course marks
<b>Total</b>	<b>100% of course marks</b>

## COURSE OVERVIEW

This table brings together the units and the number of weeks you should take to complete them and the assignment that follow them.

Unit	Title of work	Weeks activity	Assessment (end of unit)
	<b>Module 1</b>		
1	Taxation, Revenue Authorities and Ethical Issues	1	1
2	Tax Audit and Investigation	1	
3	Tax Appeal Tribunal and Interpretation of Tax Laws	1	2
4	Tax Planning and Tax Avoidance	1	
5	Taxation of Incomes: Offences and Penalties	1	3
6	Taxation of Income from Settlement, Trusts and Estates	1	
	<b>Module 2</b>		
1	Withholding Tax	1	4
2	Value Added Tax	1	
3	Capital Allowances	1	
4	Capital Gains Tax	1	5
5	Tax Effects of Privatisation and Commercialisation	1	
6	Profits, Assessable Profits and Tax Payable	1	6
	<b>Module 3</b>		
1	Person Chargeable, Offences and	1	7

	Penalties		
2	Tax on Special Businesses	1	
3	Petroleum Profit Tax	1	
4	Stamp Duties	1	8
5	Tax Planning and Tax Administration	1	
6	Tax on Pioneer Industries	1	9
	<b>Revision</b>	<b>2</b>	
	<b>Total</b>	<b>20</b>	

## HOW TO GET THE MOST FROM THIS COURSE

In distance learning, the study units are specially developed and designed to replace the university lecturer. Hence, you can work through these materials at your own pace, and at a time and place that suits you best. Visualise it as reading the lecture instead listening to a lecturer.

Each of the study units follows a common format. The first item is an introduction to the subject matter of the unit, and how a particular unit is integrated with the other units and the course as a whole. Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. You should use these objectives to guide your study. When you have finished the unit, you must go back and check whether you have achieved the objectives. If you make a habit of doing this, you will significantly improve your chances of passing the course.

The main body of the unit guides you through the required reading from other sources. This will usually be either from your set books or from a reading section. You will be directed when you need to use a computer and guided through the tasks you must do. The purpose of the computing work is two-fold. First, it will enhance your understanding of the material in the unit. Second, it will give you practical experiences of using programmes which you could well encounter in your work outside your studies. In any event, most of the techniques you will study are applicable on computers in normal working practice, so it is important you encounter them during your studies.

Activities are interspersed throughout the units, and answers are given at the end of the units. Working through these tests will help you to achieve the objectives of the units and prepare you for the assignments and the examinations. You should do each activity as you come to it in the study unit. There are also numerous examples given in the study units, work through these when you come to them, too.

The following is a practical strategy for working through the course. If you run into any trouble, telephone your facilitator or post the questions on your portal. Remember that your facilitator's job is to help you. When you need help, don't hesitate to call and ask your tutor to provide it. In summary,



- Read this course guide.
- Organise a study schedule. Refer to the course overview for more details. Note the time you are expected to spend on each unit and how the assignments relate to the unit. Important information e.g. details of your tutorials, and the date of the first day of the semester is available from the portal. You need to gather together all this information in one place, such as your diary or a wall calendar. Whatever method you choose to use, you should decide on and write in your own dates for working on each unit.
- Once you have created your own study schedule, do everything you can to stick to it. The major reason that students fail is that they get behind with their coursework. If you get into difficulties with your schedule, please let your facilitator know before it is too late for help.
- Turn to unit 1 and read the introduction and the objectives for the unit.
- Assemble the study materials. Information about what you need for a unit is given in the 'Overview' at the beginning of each unit. You will always need both the study unit you are working on and one of your set books, on your desk at the same time.
- Work through the unit. The content of the unit itself has been arranged to provide a sequence for you to follow. As you work through this unit, you will be instructed to read sections from your set books or other articles. Use the unit to guide your reading.
- Up-to-date course information will be continuously posted to your portal.
- Well before the relevant due dates (about 4 weeks before the dates) access the Assignment file on the portal and download your next required assignment. Keep in mind that you will learn a lot by doing the assignments carefully. They have been designed to help you meet the objectives of the course and, therefore, will help you pass the examination. Submit all assignments not later than the due dates.
- Review the objectives for each study unit to confirm that you have achieved them. If you feel unsure about any of the objectives, review the study material or consult your tutor.
- When you are confident that you have achieved a unit's objectives, you can then start on the next unit. Proceed unit by unit through the course and try to pace your study so that you keep yourself on schedule.
- When you have submitted an assignment to your tutor for marking, do not wait for its return before starting on the next unit. Keep to your schedule. When the assignment is returned, pay particular attention to your facilitator's comments. Consult your tutor as soon as possible if you have any questions or problems.
- After completing the last unit, review the course and prepare yourself for the final examination. Check that you have achieved the unit objectives and the course objectives.

## **FACILITATORS, TUTORS AND TUTORIALS**

There are 18 hours of tutorials (10 two-hour sessions) provided in support of this course. You will be notified of the dates, times and location of these

tutorials, together with the names and phone number of your tutor, as soon as you are allocated a tutorial group.

Your tutor will mark and comment on your assignments, keep a close watch on your progress and on any difficulties you might encounter as they would provide assistance to you during the course. You must mail your tutor-marked assignments to your tutor well before the due date (at least two working days are required). They will be marked by your tutor and returned to you as soon as possible. Do not hesitate to contact your tutor by telephone, e-mail, or discussion board if you need help. The following might be circumstances in which you would find help necessary: when:

- you do not understand any part of the study units or the assigned reading
- you have difficulty with the self-tests or exercises
- you have a question or problem with an assignment with your tutor's comment on an assignment or with the grading of an assignment.

You should try your possible best to attend the tutorials. This is the only chance to have face-to-face contact with your tutor and to ask questions which are answered instantly. You can raise any problem encountered in the course of your study. To gain the maximum benefit from course tutorials, prepare a question list before attending them. You will learn a lot from participations in discussions.

## **SUMMARY**

ACC 318 examines the contents of Advanced Taxation. The course is designed and developed for your benefit as an accounting student.

I hope that you will find this course interesting and exciting. The course is a living course. As you go through it, you will develop more insight into family law and the family property.

We hope you will enjoy your experience at the National Open University of Nigeria (NOUN). We wish you success in this course. Success in this course will help you attain your life goals.

Best wishes and regards.

**MAIN  
COURSE**

<b>CONTENTS</b>		<b>PAGE</b>
<b>Module 1</b>	.....	<b>1</b>
Unit 1	Taxation, Revenue Authorities and Ethical Issues.....	1
Unit 2	Tax Audit and Investigation.....	12
Unit 3	Tax Appeal Tribunal and Interpretation of Tax Laws....	24
Unit 4	Tax Planning and Tax Avoidance.....	30
Unit 5	Taxation of Incomes: Offences and Penalties.....	44
Unit 6	Taxation of Income from Settlement, Trusts and Estates.....	59
<b>Module 2</b>	.....	<b>66</b>
Unit 1	Withholding Tax.....	66
Unit 2	Value Added Tax.....	72
Unit 3	Capital Allowances.....	82
Unit 4	Capital Gains Tax.....	393
Unit 5	Tax Effects of Privatisation and Commercialisation....	98
Unit 6	Profits, Assessable Profits and Tax Payable.....	104
<b>Module 3</b>	.....	<b>145</b>
Unit 1	Person Chargeable, Offences and Penalties.....	145
Unit 2	Tax on Special Businesses.....	152
Unit 3	Petroleum Profit Tax.....	161
Unit 4	Stamp Duties.....	190
Unit 5	Tax Planning and Tax Administration.....	198
Unit 6	Tax on Pioneer Industries.....	209

**MODULE 1**

Unit 1	Taxation, Revenue Authorities and Ethical Issues
Unit 2	Tax Audit and Investigation
Unit 3	Tax Appeal Tribunal and Interpretation of Tax Laws
Unit 4	Tax Planning and Tax Avoidance
Unit 5	Taxation of Incomes: Offences and Penalties
Unit 6	Taxation of Income from Settlement, Trusts and Estates

**UNIT 1 TAXATION, REVENUE AUTHORITIES AND ETHICAL ISSUES****CONTENTS**

1.0	Introduction
2.0	Objectives
3.0	Main Content
3.1	Financial Statements
3.2	The International Accounting Standards Board
3.3	Objectives of Financial Statements
3.4	Underlying Assumptions
3.5	Qualitative Characteristics of Financial Statements
3.6	Elements of Financial Statements
4.0	Conclusion
5.0	Summary
6.0	Tutor-Marked Assignment
7.0	References/Further Reading

**1.0 INTRODUCTION**

You are welcome to this course on advanced taxation. In this module, you will be introduced to six units whose titles are: Taxation Revenue Authorities and Ethical Issues, Tax Audit and Investigation, Tax Appeal Tribunal and Interpretation of Tax Laws, Tax Planning and Tax Avoidance, Taxation of Income: Offences and Penalties and Taxation of Income from Settlement Trusts and Estates.

In this unit, you will be introduced to tax revenue authorities and ethical issues. The unit will take you through the study of the rationale for imposing taxation in Nigeria, classification of taxes, principles of an ideal

tax system, distribution of tax burden on taxpayers, and introduction to tax administration.

## **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- Mention the objectives, classification and principles of taxation
- explain the provisions of the Federal Inland Revenue Service (Amendment) Act 2007, the revenue service's composition and functions
- explain the powers conferred on the Federal Inland Revenue Service regarding administration and enforcement of various tax laws
- mention the powers and objectives of the Service's enquiries, know filing, assessment and collection procedures, and know the code of ethics expected of revenue officials.

## **3.0 MAIN CONTENT**

### **3.1 Rationale for Imposition of Taxes**

The rationale for imposing taxes in a market economy such as Nigeria stems from the government responsibilities which include:

#### **(a) Provision of public goods**

A pure public good is one that displays the following characteristics:

- (i) displays zero marginal cost, that is, no extra cost is incurred in supplying the good to more than one person
- (ii) individuals cannot be excluded from consuming the good, even if they have no desire for it
- (iii) all members of society must consume the same amount; it cannot be rejected. For example, law and order.

An example of a pure public good is defence. The provision of national defence protects all members of society from external hostilities at zero marginal cost. No individual can be excluded and it cannot be rejected by those who disagree in principle. For example, pacifists, if left to the market, individuals with no desire for the good would be unwilling to pay the price, yet at the same time, they could not be excluded from benefiting.

Consequently, a free market would be inefficient in the provision of public goods, and they become the responsibility of the state.

**(b) Redistribution of income and wealth**

The mechanism for the redistribution of income and wealth by the use of transfer payments and benefits to those members of society who are less well off promotes social equality. Governments are becoming increasingly socially aware and are seeking to reduce poverty and promote social welfare through income redistribution.

**(c) Promotion of social and economic welfare**

Government often assumes a paternalistic role by providing 'merit' goods. Merit goods, such as health and education, unlike public goods, can be provided privately, but if left completely to market forces, merit goods would be under-consumed, and so there are benefits in the state providing such goods, as everyone benefits from living in a healthy and educated society. There are external benefits in the provision of merit goods as well.

In the same respect, demerit goods such as alcohol and cigarettes are discouraged by government in order to reduce the external costs to society; for example, health risks and pollution.

**(d) Economic stability**

The government is responsible for avoiding high levels of inflation and unemployment in order to promote economic stability and sustainable growth.

**(e) The single Economic Community of West Africa States (ECOWAS) market**

With the introduction of the single market in the 1990's, there is more pressure on the government to be in harmony with other member states.

**(f) Regulation**

Legislation and regulatory controls imposed on producers in order to protect consumers, employees and the general public is the responsibility of any socially aware government.

Given these general responsibilities, taxation can be a powerful tool in the hands of any government as a means of ensuring that the social, political and economic policies of the government in power are brought to fruition.

### **SELF-ASSESSMENT EXERCISE**

- i. State the rationale for imposing taxes in a market economy such as Nigeria.
- ii. List and explain the four core objectives of a modern tax system.

## **3.2 The Classification of Taxes**

A tax is a compulsory contribution imposed by government on her citizens in order to provide public goods and services and ensure their social and economic welfare. Taxes can be classified in the following ways:

### **3.2.1 Tax Base**

Taxes have to be levied on one base or another, and a convenient way of classifying a tax is to do so according to what is being taxed. Three main tax bases are used in the present Nigerian tax system, namely:

- (a) Income
- (b) Capital
- (c) Consumption

### **3.2.2 Differences between Direct Tax and Indirect Tax**

A *direct tax* is one levied directly on the person who is intended to pay the tax. Examples of direct taxes are:

- (a) Income tax
- (b) Company tax
- (c) Capital gains tax

An *indirect tax* is borne by a person other than the one from whom the tax is collected. Examples of indirect taxes are:

- (a) Value added tax
- (b) Custom and excise duties

### 3.3.3 Ad Valorem

An *ad valorem tax* is levied on the value of the tax base, for example; income tax is charged at 10 per cent to 30 per cent, depending on the level and type of income.

### 3.3 Distribution of the Tax Burden

The way in which the burden of tax is distributed among the taxpaying community is another way in which taxes may be classified. The rates of tax can be set in such a way that they are:

- (a) **Progressive:** Progressive taxes take an increasing portion as the value of the tax base rises.
- (b) **Proportional:** A proportional tax takes a constant portion of the value of the tax base and depends on the marginal and average rates of tax being equal.
- (c) **Regressive:** Regressive taxes take a declining portion as the value of the tax base rises and depends on the average rate of tax being greater than the marginal rate of tax.

### SELF-ASSESSMENT EXERCISE

What is the difference between direct taxes and indirect taxes?

### 3.4 The Principles of an 'Ideal' Tax System

In his book, *The Wealth of the Nations* (1776), Adam Smith proposed that a 'good' tax should display the following characteristics, it should:

- (a) reflect a person's ability to pay
- (b) be certain
- (c) be convenient; and
- (d) be administratively efficient and not cause economic distortion.

These principles still hold good today, and in a modern tax system, an 'ideal' tax should conform as far as possible to the following criteria:

1. **Simple, certain and convenient:** The tax should be relatively simple for taxpayers to understand their liability.



2. **Flexible:** The structure and rates of tax should be capable of being altered without too much difficulty.
3. **Administratively efficient:** the costs of administering the tax should not be too high in proportion to the revenue raised.
4. **Neutral:** A tax is said to be neutral if it does not distort economic choices. This distortion of economic choice is known as the excess of burden of taxation, causing substitution effects result in economic inefficiency.
5. **Equitable:** Taxes must not only be fair, they must also be seen to be fair, if the taxpaying public is to find them acceptable.

There are two types of equity to be considered:

- (a) **Horizontal equity** - requires that people in similar situations are treated in a similar way.
- (b) **Vertical equity** - requires that people in unequal situations are treated with the necessary degree of inequality.

### **SELF-ASSESSMENT EXERCISE**

List five principles an 'idea' tax should conform to?

## **3.5 Distribution of Tax Burden among Taxpayers**

### **3.5.1 Traditional Approaches**

There are two traditional approaches to the distribution of tax burden among the taxpaying community. These are:

- benefit theory, and
  - ability to pay.
- (a) **Benefit theory:** This theory holds sway on the idea that taxes should be levied in proportion to the benefit received. On the face of it, this approach would seem to be fair. However, in practice, the benefit is difficult to measure.

- (b) **Ability to pay:** This approach is based on the idea that the burden of taxation should be spread in such a way as to give rise to an equality of sacrifice among the taxpaying community. For example, ₦5, 000 is less of a sacrifice to a person earning ₦150, 000 than to one earning ₦55, 000 all other things being equal.

### 3.6 Introduction to Tax Administration

Presently, there are three tiers of government charged with the administration of tax in Nigeria: the federal, state and the local governments. Each tier of government has its own tax authority, created by federal laws. The authorities include:

#### (1) The federal tax authority

The Federal Inland Revenue Service (Establishment) Act 2007 provides for the Establishment of the Federal Inland Revenue Service (FIRS), its management board and so on. The service shall have a board, known as the Federal Inland Revenue Service Board, which shall have overall supervision of the service as specified under the act. These are:

Executive chairman: (who shall be experienced in taxation), appointed by the President and subject to confirmation of the Senate.

- Six members with relevant qualifications and expertise, who shall be appointed by the President to represent each of the six geopolitical zones.
- A representative of the Attorney-General of the Federation.
- The Governor of the Central Bank of Nigeria or his representative.
- A representative of the Minister of Finance not below the rank of a director.
- Chairman of Revenue Mobilisation, Allocation and Fiscal Commission or his representative who shall be any of the Commissioners representing the 36 States of the Federation.
- The Group Managing Director of the Nigerian National Petroleum Corporation or his representative who shall not be below the rank of Group Executive Director or its equivalent.
- Controller – General of the Nigerian Custom Service or his representative not below the rank of a Deputy Controller-General.
- The Registrar-General of the Corporate Affairs Commission or his representative not below the rank of a Director, and

- The Chief Executive Officer of the National Planning Commission or his representative not below the rank of a Director.

### Note

The members of the Board, other than the Executive Chairman, shall be part-time members.

### (2) The state tax authority

State Internal Revenue Service (SIRS) (Section 85A, B & C of Personal Income Tax Act Cap P8 LFN 2004).

#### *Joint state revenue committee*

According to the act, each state of the federation should have a joint state revenue committee, comprising:

- The Chairman of the State Internal Revenue Service who acts as Chairman of the Committee;
- The Chairman of the local government revenue committee
- A representative of the bureau of local government affairs - (from the rank of director and above)
- A representative of the revenue mobilisation allocation and fiscal commission, as observer
- State sector commander of the FRSC as observer
- Legal adviser of the State Internal Revenue Service; and
- Secretary to the committee - usually a staff of the SIRS.

### (3) The local government tax authority

Refer to Local Government Revenue Committee (Section 85 D & E of Personal Income Tax Act Cap P8 LFN 2004). The Revenue Committee shall comprise:

- the supervisor for finance as chairman
- three local government councilors as members
- two other persons experienced in revenue matters to be nominated by the chairman of the local governments on their personal merits.

The following are constraints to effective tax administration in Nigeria:

- (a) Poor public enlightenment
- (b) Inadequate funding of tax authorities
- (c) Dearth of qualified and/or experienced tax officials at the state and local government tiers of government
- (d) Tax evasion
- (e) Improper use of tax consultants
- (f) Lack of will power on the part of tax authority personnel (administrative ineffectiveness)
- (g) Loopholes in the law; and
- (h) Poor governance.

### **3.6.1 Filing Requirements**

#### **(i) Government assessment system**

Under Section 41 of CITA, CA P C21 LFN 2004, a taxpayer under:

- the government assessment system is expected to submit:
  - i. audited accounts
  - ii. tax computation
  - iii. capital allowances computation
  - iv. a statement of profits from every source; and
  - v. a declaration that the returns reflect a true and correct position of the operations of the company and that the details are true and complete.

#### **(ii) Self-assessment filing**

A company filing self-assessment is required under Section 40B of CITA, to include the following:

- computation of the tax payable for the assessment year; and
- evidence of payment to the designated bank of the tax payable or the relevant installment thereof.

### **3.6.2 Assessments**

#### **(i) Government assessment**

Where the returns filed are accepted by the Revenue Service, they form the basis of the assessment for the year. Where they are rejected, the Revenue Service assesses on “Best-of-Judgment” basis under Section 47(2) of CITA. Where the taxpayer fails to file; the Revenue Service is empowered under Section 47(3) to estimate the assessment.

Where the Revenue Service makes a discovery that a taxpayer has not been assessed or that it has been assessed at less than it ought to have been assessed, the Revenue Service is empowered under Section 48 of CITA to raise additional assessment anytime within six years from the date of the assessment.

Where, under the proviso of Section 48 of CITA the non-assessment or under-assessment is due to any form of fraud, can go back for a longer period than the six years’ limitation.

#### **(ii) Self-Assessment**

The company assesses itself under this system. It also requires full disclosure in respect of the incomes from all the sources.

The returns are not, under internal regulation, to be subjected to the routine process of desk audit but are to undergo field audit to confirm compliance.

### **SELF-ASSESSMENT EXERCISE**

List the constraints to effective tax administration in Nigeria.

### **3.6.3 Final and Conclusion Assessment**

An assessment which has become final and conclusive cannot be reopened without the discovery of new facts. An assessment becomes final and conclusive under the following conditions:

- Where no valid objection is made within the statutory time limit of 30days from the date of the service of the notice of assessment

- Where an appeal against the decision of the revenue service is not made to the Body of Appeal Commissioners within 30 days from the date of the Notice of Refusal to Amend
- Where an appeal is not made of the Federal High Court within 30days from the date of decision of the Body of Appeal Commissioners.

#### **4.0 CONCLUSION**

We stated the objectives, classification and principles of taxation and discussed the provisions of the Federal Inland Revenue Service (Amendment). We also discussed the FIRS Act 2007 enumerating the Revenue Service's composition and functions as well as the established powers conferred on the Federal Inland Revenue Service regarding administration and enforcement of various tax laws. Finally, we listed the powers and objectives of the Service's enquiries, explained how filing, assessment and collection procedures, as well as the code of ethics expected of revenue officials.

#### **5.0 SUMMARY**

This unit deals with tax administration in Nigeria, government assessment and approaches to the distribution of taxation in Nigeria.

In the next unit, we shall examine tax audit and investigation.

#### **6.0 TUTOR-MARKED ASSIGNMENT**

1. Explain in detail the rationale behind imposition of taxation in Nigeria.
2. List and discuss the functions of the three tiers of tax administration in Nigeria.
3. Through what means can tax burdens be distributed in Nigeria?

#### **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 2     TAX AUDIT AND INVESTIGATION**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Audit
  - 3.2 Tax Audits
  - 3.3 The Tax Audit Process
  - 3.4 Types of Audit Exercise
  - 3.5 Audit Programme
  - 3.6 Tax Investigations
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we dealt with tax administration in Nigeria, government assessment and approaches to the distribution of taxation in Nigeria.

In this unit, we shall examine tax audit and investigation.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- state the objectives of tax audit
- discuss how to conduct a tax audit
- explain the basis of the power of the Revenue Service to audit
- enumerate the reasons for tax investigation
- discuss how to conduct a tax investigation.

### **3.0 MAIN CONTENT**

#### **3.1 Audit**

An audit is an examination usually by an independent person, of a set of the accounting books, records, documents, etc, from which a set of financial statements has been prepared.

##### **3.1.1 Objectives of Statutory Audit**

The objectives of an audit are to express an opinion as to whether:

- (a) Proper books have been kept
- (b) The financial statements are in agreement with the books
- (c) The requirements of the applicable legislations, for example, CAMA, 1990 (as amended) have been complied with
- (d) Applicable accounting standards (both local and international) have been adhered to
- (e) The financial statements give a true and fair view of the state of the financial affairs of the enterprise as at its balance sheet date, and
- (f) The financial statements give a true and fair view of the result of the operations of the enterprise for the period under audit.

##### **3.1.2 Specialised Audits**

Specialised audits are normally involved whenever special attention is needed on special issues that are not part of the objectives of statutory audits.

When a specialised audit is carried out, the auditor would cover in his report the particular objectives that were to be achieved as set out in the auditor's terms of reference.

#### **3.2 Tax Audits**

Tax audits are similar to special audits. They are additional to statutory audits and are carried out by tax officials from relevant tax authorities). The approach and scope of work would be slightly different from that to be carried out for audit under CAM A, 1990.



### 3.2.1 Objectives of Tax Audit

The objectives of tax audit are to enable the tax auditors determine whether or not:

- (a) adequate accounting books and records exist for the purpose of determining the taxable profits or loss of the taxpayer and consequently object the tax payable
- (b) the tax computations submitted to the tax authority by the taxpayer agree with the underlying records
- (c) all applicable tax legislations have been complied with
- (d) provision of an avenue to educate taxpayers on various provisions of the tax law
- (e) discourage tax evasion
- (f) detect and correct accounting and/or arithmetical errors in tax returns
- (g) provide feedback to the management on various provisions of the law and recommend possible changes
- (h) identify cases involving tax fraud and recommend them for investigation
- (i) forestall taxable persons' failure to render tax returns
- (j) forestall taxable persons' rendering incomplete or inaccurate returns; and
- (k) encourage voluntary compliance which is one of the strong reasons in support of the self-assessment scheme.

There are two types of tax audit:

- (a) desk audit
- (b) field audit.

#### (a) Desk audit

This ensures the completeness of the items submitted for tax purposes. The inspector carrying out a desk audit will also look for apparent errors or mistakes in the tax computations and/or in the accompanying documents and records.

#### (b) Field audit

A field audit is more elaborate and comprehensive than a desk audit. It is usually carried out outside the inland tax revenue's office i.e. in the taxpayer's business premises. The need to carry it out in the taxpayer's

premises is to enable the tax auditors carry out the examination of applicable documents and also obtain appropriate information directly from the officials of the business.

### 3.3 The Tax Audit Process

This topic will be discussed under the under listed sub-topics.

#### 3.3.1 Pre-Assessment Stage

The tax audit branch carries out audit exercise only on companies that have been referred to it by the management. The ultimate authority for referral of cases for audit lies with the Chairman through the Director of Assessment. The usual channels for recommending cases for audit include:

- (a) **The management:** The technical committees, the chairman and the director could refer cases directly to the bank.
- (b) **Zonal coordinator:** The zonal coordinator may also recommend case for tax audit through the director of assessment.
- (c) **Area tax controllers:** Desk officers recommend cases for tax audit through their area tax controllers (ATC) that passes the recommendation to the director of assessment.
- (d) **Tax audit controllers:** The tax auditor may recommend that ongoing audit be extended to cover related companies.

#### 3.3.2 Assessment Stage

The stages in the audit process are as follows:

- (a) Selection of taxpayer to be audited
- (b) Preliminary review of taxpayer's file
- (c) Notification of taxpayer
- (d) Pre-audit meeting followed immediately by field audit
- (e) Post audit meeting
- (f) Interim audit report
- (g) Post audit review by regional/headquarters audit
- (h) Reconciliation meetings; and
- (i) Final audit report.

**(a) Selection of taxpayers to be audited**

The criteria for the selection for files and audit which are determined by Audit Headquarter are as follows:

- (a) Self-assessment taxpayers - at least two years since the last audit of the taxpayer.
- (b) Taxpayers with refund claims-especially arising from excess withholding tax credits and, or other named reasons.
- (c) Taxpayers with nil returns or continuous loss situation.
- (d) Taxpayers with very low adequacy ratios.
- (e) Based on routine industry checks or sectorial audit (project audit).
- (f) Based on lead information received from intelligence or other FIRS departments or external sources.
- (g) Transfer pricing arrangements.
- (h) Tax planning schemes.
- (i) Claims under Double Taxation Agreement (DTA).
- (j) Secondary files-relationship with another taxpayer by way of holding subsidiary associated or related companies could be criteria for selecting companies for audit.
- (k) Industrial group's compliance evaluation and profitability comparison.
- (l) Verification of poor or extraordinary performance.
- (m) Referrals resulting from desk examinations.
- (n) Information resulting from examination, audit and investigation of other taxpayers.
- (o) Random sampling.
- (p) Firms making unusual requests of taking extraordinary decisions such as centralising as erstwhile decentralised operation.
- (r) Directive from higher government authority.

**(b) Preliminary review of taxpayer's file**

This is aimed at preparing both the audit department and the audit teams that will be involved in the audit exercise for the audit task ahead.

**(c) Preliminary activities**

Before audit executives set out, certain preliminary activities must take place. These are:

- (a) Gathering of the files and grouping them into the number of audit teams to be established.
- (b) Audit teams to acquaint themselves with background information about their cases.
- (c) Prepare audit checklists to be used in respect of each company to ensure that all necessary areas of audit activities are covered.
- (d) Design interview format (if necessary) for each company, depending on the problems, so as to ensure that all grounds are covered;
- (e) Assign specific duties to audit team members.

**(d) Audit checklist**

The checklist is used during the audit exercise to ensure that a thorough job is done.

**(e) Background information**

The following are basic information to be extracted from the taxpayer's file:

- (a) Name of the company
- (b) Registered address
- (c) Business address
- (d) Date of incorporation
- (e) Date of commencement of business
- (f) Tax file number
- (g) Nature of business
- (h) External auditors/tax consultants and their addresses
- (i) Bankers/addresses
- (j) Solicitors and secretaries
- (k) Share capital (authorised and issued)
- (l) Shareholding structure
- (m) Names of directors/number of shares held
- (n) Associated companies/addresses
- (o) Litigation details, if any
- (p) Period covered during the last audit or investigation exercise; and
- (q) Accounting year end.

**(f) Notification of taxpayer**

On completion and approval of the preliminary review by the head of the unit, the taxpayer or his tax consultants will be notified of the field audit,

which will then be carried out in the company's premises. The notification letter will state the following:

- (a) Period (years) that the audit exercise will cover
- (b) List of records/documents to be made available for the audit
- (c) Date and time of commencement of audit exercise
- (d) Names of inland tax revenue officials that will carry out the audit.

**(g) Pre-Audit Meeting followed by Field Audit**

The meeting is aimed at:

- (i) informing the taxpayer of the purpose of the audit
- (ii) confirming background information of the taxpayer earlier obtained in the assessment file
- (iii) getting other relevant information that are not available in the file
- (iv) familiarisation with the company's accounting and operational system
- (v) giving the taxpayers the opportunity to express their views on the audit
- (vi) seeking the cooperation of the taxpayer in terms of providing books and records and explanation where necessary.

**(h) Post audit meeting**

A post audit meeting should be held immediately after the end of the field audit, between the tax auditors and the taxpayers and their representatives at the taxpayer's premises.

**(i) Interim audit reports**

- (1) Preliminary reports:** Sometimes, the schedule officer of a case would come across material issues, in the course of the preliminary review of the assessment file that should be brought to the notice of the management. In such an instance, a preliminary report be prepared and sent to the chairman detailing such issues.
- (2) Interim reports:** After the field audit, but before the conclusion of the audit exercise, progress reports could be called for by management. The team leader should collate the individual reports of all the team members and write the interim Audit Report. The report should highlight details of all the things that may result in

additional tax assessment as well as areas of possible dispute with the taxpayer and suggestions on how to resolve them.

**(j) Post audit review by regional/headquarters audit**

The Regional/Headquarters Audit will review the Interim Audit Report as soon as it is received, by giving clear directives on all reported matters, after due consideration of the technical issues involved based on the prevailing tax laws, as well as the generally accepted accounting principles. This will form the basis for the reconciliation meetings.

**(k) Reconciliation meetings**

This is a meeting between the tax auditors (with representatives of regional/headquarters audit present as appropriate) on the one hand the taxpayers (and their representatives and tax consultants) on the other hand.

**(l) Final audit report**

The audit report is the final stage of the audit. It is very important and should be rendered immediately an audit is completed. It contains all important items about the company and the audit work done.

### **3.4 Types of audit exercise**

There are three types of audit exercises. They are:

- (a) Routine sector audit
- (b) Routine zonal audit
- (c) Special-purpose audit

These are briefly explained below.

**(a) Routine sector audit**

This audit covers companies operating within a specific industry, for example, banking, construction, oil servicing, shipping and so on.

**(b) Routine zonal audit**

The tax audit branch is located within the Lagos zone and thus operates more actively within the zone. However, periodic audit tours of other zones

are carried out. Companies within such zones irrespective of industry are visited and audited.

### **(c) Special purpose audit**

This is when an audit is carried out to achieve a specific purpose by management.

## **SELF-ASSESSMENT EXERCISE**

- i. What are the usual channels for recommending cases for audit?
- ii. List and explain the types of audit exercise.

## **3.5 Audit Programme**

This is a schedule of audit work expected to be performed on each item of the accounts such as income/turnover, expenditures, assets and liabilities.

### **3.5.1 Benefits of the Audit Programme**

The benefits of audit programme are as follows:

- (a) It will provide details of the work, which the team leader requires individual members of the team to perform.
- (b) It will provide information as to how much the audit work has been completed as at a particular date, and how much is outstanding.
- (c) Provides a record of audit responsibility by providing a record of the audit staff members responsible for each part of the completed work.
- (d) Provides an avenue for the team leader to allocate his available staff in the most productive and efficient manner possible.
- (e) It is a time management tool.

## **3.6 Tax Investigations**

Investigations, as distinct from tax audits, are called for when there are problems in, for example, an organisation either affecting the whole or particular segment of the organisation. Such could be required when a large fraud is suspected or when evidence of mismanagement abounds and an interested party requires that the effect on the enterprise be quantified for management decision-making purposes.

### **3.6.1 Stages of Tax Investigation**

The stages of tax investigation are:

- Surveillance or pre-investigation activities
- Evidential audit or investigation
- Case preparation
- Arraignment
- Termination of investigation.

### **3.6.2 Investigation/Intelligence Division**

Some of the roles and responsibilities of the Head of the Division are as follows:

- a. Coordinate the activities of all the units in the division.
- b. Articulate and direct policies and programmes aimed at achieving the objectives of the division.
- c. Define key operating/guiding principles.
- d. Design strategies for deterring violations of tax laws and hence ensuring tax compliance.
- e. Collate and maintain reliable statistics of investigations/intelligence work.
- f. Recommend amendments of tax laws in order to plug all areas of tax leakages and so on.

### **3.6.3 Civil Investigations Unit**

The activities of this unit are highlighted below:

- a. Investigate tax avoidance scheme
- b. Investigate cases for tax refunds
- c. Review cases for mergers and acquisitions
- d. Issue warrants for search and seizure under section 45A
- e. Identify areas for amendments to tax laws in order to plug all areas of tax leakages.



### 3.6.4 Criminal Investigation Unit

The Criminal Investigation Unit is responsible for:

- a. Investigate, penalise and recommend prosecution in cases of tax evasion.
- b. Investigate and liaise with relevant agencies for prosecution.
- c. Carryout search and seizure where such would result in obtaining relevant document for an investigation.
- d. Analyse and evaluate evidences obtained to establish criminal violation, follow up with assessment, penalties and prepare case for prosecution.
- e. Identify the areas for amendments to tax laws in order to plug all tax leakages.
- f. Assist in preparing evidence for prosecution of violators.
- g. Liaise with the National Drug Law Enforcement Agency (NDLEA), Economic and Financial Crime Commission (EFCC), Nigeria Deposit Insurance Corporation (NDIC) and Central Bank of Nigeria (CBN) to investigate violation of tax laws in cases of white-collar crimes such as money laundering.

### SELF-ASSESSMENT EXERCISE

List the responsibilities of the following:

- Investigation/Intelligence Division
- Civil Investigations Unit
- Criminal Investigation Unit.

## 4.0 CONCLUSION

We have defined tax audit and investigations and explained its objectives. We described the two types of tax audit and explained the process of carrying out a tax audit, especially under the pre-self-assessment period and under the current self-assessment regime. However, in the case of tax investigation, an intelligence unit of the authority is involved in sourcing for tax information as regards incomes from all sources received by or paid to a named taxpayer.

## **5.0 SUMMARY**

In this unit, we have stated the objectives of tax audit and discussed how to conduct a tax audit. We explained the basis of the power of the revenue service to audit; enumerated the reasons for tax investigation; and discussed how to conduct a tax investigation.

In the next unit, we shall look into another topic 'tax appeal tribunal and interpretation of tax laws'.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. What do you understand by the term "tax investigation"?
2. State the stages of tax investigation.

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 3      TAX APPEAL TRIBUNAL AND INTERPRETATION OF TAX LAWS**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Establishment of a Tax Appeal Tribunal
  - 3.2 Jurisdiction of the Tribunal
  - 3.3 Criminal Prosecution
  - 3.4 Appeals to the Tribunal
  - 3.5 Appeals to the Federal High Court
  - 3.6 Right to Legal Representation
  - 3.7 Powers and Procedures of the Tribunal
  - 3.8 Further Appeals to the Court of Appeal
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we dealt with tax administration in Nigeria, government assessment and approaches to the distribution of taxation in Nigeria.

In this unit, we shall examine tax audit and investigation.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- interpret tax laws
- state the composition and jurisdiction of Tax Appeal and Tribunal (Tax Appeal Commissioners)
- describe what constitutes an appeal
- enumerate the procedure for raising objections to tax assessments
- list the procedure for the hearing of appeals
- discuss the procedure to be followed for further appeals to the High Court or court of Appeal; and
- list the taxpayers rights in a dispute.

### **3.0 MAIN CONTENT**

#### **3.1 Establishment of a Tax Appeal Tribunal**

If any taxpayer disputes a tax assessment raised on him by the tax authority, he may give notice of objection, and if the objection is turned down, the taxpayer may seek redress with the Tax Appeal Tribunal.

The Tax Appeal Tribunal was established by section 59(1) of the Federal Inland Revenue Service (Establishment) Act 2007, as provided for in the fifth schedule to the act.

##### **3.1.1 Power of the Minister**

According to the act, the minister may by notice in the federal gazette specify the number of zones, matters and places in relation to which the tribunal may exercise jurisdiction.

##### **3.1.2 Composition of the Tribunal**

The tribunal shall consist of five members (hereinafter referred to as “Tax Appeal Commissioners”) to be appointed by the minister.

#### **3.2 Jurisdiction of the Tribunal**

- (a) The tribunal shall have power to adjudicate on disputes, and controversies arising from the following tax laws (hereinafter referred to as “The Tax Laws”).
  - (i) Companies Income Tax Act, CAP 60 LFN 1990
  - (ii) Personal Income Tax Act No. 104, 1993
  - (iii) Petroleum Profits Tax Act CAP 354 LFN 1990
  - (iv) Value Added Tax Act No.102, 1993
  - (v) Capital Gains Tax Act CAP 42 LFN 1990; and
  - (vi) Any other law contained in or specified in the first schedule to the act or other laws made or to be made from time to time by the National Assembly.
  
- (b) The tribunal shall apply such provisions of the tax laws referred to above as may be applicable in the determination or resolution of any dispute or controversy before it.

### **3.3 Criminal Prosecution**

Where in the course of its adjudication, the tribunal discovers evidence of possible criminality; the tribunal shall be obliged to pass such information to the appropriate criminal prosecuting authorities, such as the office of the Attorney-General of the Federation or the Attorney-General of any state of the Federation or any relevant law enforcement agency.

#### **SELF-ASSESSMENT EXERCISE**

State the tax law that established the tax appeal tribunal.

### **3.4 Appeals to the Tribunal**

This topic is discussed under the following sub-topics.

#### **3.4.1 Notice of Appeal**

A notice of appeal against an assessment shall specify the following particulars:

- (a) The official number of the assessment, the date and the year for which it was made
- (b) The amount of total profits on which the tax was charged
- (c) The amount of the tax charged
- (d) The date of service of notice of refusal by the revenue service to amend the assessment
- (e) The precise grounds of appeal against the assessment
- (f) Address for service of any notice, correspondence or other documents to be given to the appellant by the secretary to the Appeal Commissioners.

#### **3.4.2 Notice of Refusal to Amend**

When a notice of refusal to amend has been received by any company, the company, if it desires, can appeal against the assessment upon giving notice (notice of appeal) in writing to the secretary of the tax appeal tribunal, within thirty days from the date of service to the notice of refusal. The date of service is the date on the notice of refusal to amend and not the date of receipt of the notice by the company. A late appeal may be accepted, upon an application being made to the tax appeal tribunal, if there is reasonable excuse for the delay, for example postal delays.

### **3.5 Appeals to the Federal High Court**

- (a) Any person dissatisfied with a decision of the tribunal constituted under this Schedule may appeal against such decision on a point of law to the Federal High Court upon giving notice in writing to the secretary to the tribunal within 30 days after the date on which such decision was given.
- (b) A notice of appeal filed pursuant to subparagraph (a) above shall set out all the grounds of law on which the appellant's case is based.
- (c) If the service is dissatisfied with the decision of the tribunal, it may appeal against such decision to the Federal High Court on points of law by giving notice in writing as specified in (a) to the secretary within 30 days after the date on which such decision was made.
- (d) Upon receipt of a notice of appeal, the secretary to the tribunal shall cause the notice to be given to be given to the Chief Registrar of the Federal High Court along with all the exhibits tendered at the hearing before the tribunal.
- (e) The Chief Judge of the Federal High Court may make rules providing for the procedure in respect of appeals made under this act and until such rules are made, the Federal High Court rules relating to hearing of appeals shall apply to be hearing of an appeal under the act.

#### **SELF-ASSESSMENT EXERCISE**

- i. State the tax law that established the tax appeal tribunal.
- ii. List the particulars that a notice of appeal against an assessment must have.

### **3.6 Right to Legal Representation**

- (a) A complainant or appellant, as the case maybe, may either appear in person or authorise one or more practitioners or any of its officers to represent him or its case before the tribunal.
- (b) Every individual or company in a case before the tribunal shall be entitled to be represented at the hearing of an appeal by a solicitor or chartered accountant or adviser provided that. If the person appointed by the taxpayer to be representative in any matter before the tribunal is unable for good cause to attend hearing thereof, the tribunal may adjourn the hearing for such reasonable time as it deems fit, or admit the appeal to be made by some other person or by way of a written address.

### **3.7 Powers and Procedures of Tribunal**

- (a) The tribunal may make rules regulating its procedures.
- (b) The tribunal shall, for the purpose of discharging its functions under this schedule, have power to:
  - (i) summon and enforce the attendance of any person and examine him on oath
  - (ii) require the discovery and production of documents
  - (iii) receive evidence on affidavits
  - (iv) call for the examination of witnesses or documents
  - (v) review its decisions
  - (vi) dismiss an application for default or deciding matters ex-parte
  - (vii) set aside any order or dismissal of any application for default or any order passed by it ex-parte; and
  - (viii) do anything which in the opinion of the tribunal is incidental or auxiliary to its functions under this schedule.
- (c) Any proceeding before the tribunal shall be deemed to be a judicial proceeding and the tribunal shall be deemed to be a civil court for all purposes.
- (d) The minister may make rules prescribing the procedure to be followed in the conduct of appeals before the tribunal.
- (e) However, each party of an appeal shall bear its own cost.

### **3.8 Further Appeals to Court of Appeal**

An appeal against the decision of the Federal High Court at the instance of either party shall lie to the Court of Appeal.

#### **SELF-ASSESSMENT EXERCISE**

List the powers and procedures of the tribunal.

### **4.0 CONCLUSION**

Under this unit, we have explained a comprehensive procedure for appeals to the tax appeal tribunals (Appeal Commissioners) where the taxpayer and the revenue cannot mutually agree on the tax due. It discusses the composition and matters relating to appeal commissioners and other staff such as appointment, tenure of office and so on.

The right of appeal of the taxpayer and the tax authority to seek further redress from the Federal High Court and Court of Appeal was also discussed.

## **5.0 SUMMARY**

In this unit, we have interpreted tax laws and stated the composition and jurisdiction of Tax Appeal and Tribunal (Tax Appeal Commissioners). We explained what constitutes an appeal and enumerated the procedure for raising objections to tax assessments. We listed the procedure for the hearing of appeals and also discussed the procedure to be followed for further appeals to the High Court or Court of Appeal. Finally, we listed the taxpayers' rights in a dispute.

In the next unit, we shall consider tax planning and tax avoidance.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. What is the jurisdiction tax appeal tribunal? List them.
2. What are the particulars contained in the notice of appeal against an assessment of a taxpayer?
3. Discuss what you understand by right to legal representation by a taxpayer.

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack (2011).



## **UNIT 4 TAX PLANNING AND TAX AVOIDANCE**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Tax Planning – its Definition
  - 3.2 Classification of Taxes
  - 3.3 Tax Planning Checklist
  - 3.4 Tax Avoidance
  - 3.5 Anti Avoidance Legislation
  - 3.6 Company Income Tax Act (CITA) Section 18
  - 3.7 Tax Avoidance and Tax Evasion
  - 3.8 Acceptance of Offer as a Tax Consultant
  - 3.9 Clients’ Documentation and Records
  - 3.10 Communication with Tax Authorities
  - 3.11 VAT Registration
  - 3.12 Communication with other Stakeholders
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we interpreted tax laws; stated the composition and jurisdiction of tax appeal and tribunal (Tax Appeal Commissioners); explained what constitutes an appeal; enumerated the procedure for raising objections to tax assessments; listed the procedure for the hearing of appeals; discussed the procedure to be followed for further appeals to the High Court or Court of Appeal; and listed the taxpayers rights in a dispute.

In this unit, we shall be looking into another aspect of taxation which focuses on tax planning, tax avoidance and the difference between tax avoidance and tax evasion. Also anti-avoidance legislation will be discussed.

## **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- explain the term tax planning.
- discuss the term tax avoidance
- differentiate between tax avoidance and tax evasion
- list clients documents to be kept and maintained by tax practitioners
- explain the nature and information required for registration of the taxpayers with the tax authorities
- discuss suitable replies to tax queries
- explain clients' tax matters.

## **3.0 MAIN CONTENT**

### **3.1 Tax Planning – its Definition**

Tax Planning involves taking conscious efforts to consider the tax that will be payable by a taxpayer at a future date and how such tax can be minimised.

### **3.2 Classification of Taxes**

The main taxes in Nigeria can be classified into direct and indirect taxes as follows:

#### **3.2.1 Direct Taxes**

These are charged on a taxpayer's income, profits or other gains. They are paid by the taxpayer directly to the tax authority. The direct taxes are personal income tax (payable by individuals).

Companies' income tax (payable by companies other than those engaged in petroleum organisations). Petroleum profits tax is payable by companies, whilst capital gains tax is payable by both individuals and corporate bodies.

#### **3.2.2 Indirect Taxes**

Indirect taxes imposed on commodities (goods), professional services and instruments, before they reach the ultimate consumer, client or owner respectively and are paid by them, not as taxes (i.e. not to the tax

authorities), but as part of the selling/legalisation price/cost of the commodity, service or instrument, as the case may be. Examples of indirect taxes include: Value Added Tax Custom Duties, Excise Duties and Stamp Duties.

### 3.3 Tax Planning Checklist

The matters in the under-listed checklist should be considered while planning tax:

- (a) List of approved taxes and levies.
- (b) Timing of fixed assets acquisition.
- (c) Timing of fixed assets disposal in view of balancing adjustments.
- (d) Timing of capital allowances claim and amount to claim.
- (e) Hire of assets as alternative to outright purchase-full hire charge is tax deductible.
- (f) Where to invest?
- (g) Making specific instead of general provisions.
- (h) PAYE properly deducted.
- (i) Withholding tax properly deducted.
- (j) Note critical dates:
  - (i) Filing of tax returns
  - (ii) Filing of notice of objection
  - (iii) PAYE monthly remittances
  - (iv) PAYE year-end returns and final payment
  - (v) Withholding tax remittances to revenue
  - (vi) VAT returns and remittances to revenue
  - (vii) National Social Insurance Trust Fund (NSITF)
  - (viii) National Housing Fund (NHF)
  - (ix) Due dates for income tax payment, to avoid penalty and interest.
- (k) In capital gains tax (TAX), consider roll-over relief.
- (l) CGT Rate is 10% stocks and shares now exempted from CGT. Invest in stocks and shares rather than in buildings.
- (m) Consider current tax incentives:
  - (i) Pioneer companies
  - (ii) Rural investment allowance
  - (iii) Investment tax credits
  - (iv) Export processing zone allowance
  - (v) Export free zone example profit
  - (vi) Exempt profit of solid minerals mining
  - (vii) Hotel income exempt from tax

- (viii) Investment tax credit-spare parts fabrication
- (ix) Investment tax credit-replacement of obsolete plant
- (x) Gas industry incentives.
  
- (n) Consider exempt income and profits (Section 19 CITA).
- (o) Investment options – low or no tax investment opportunities.
- (p) Dividend distribution out of franked investment income.
- (q) Employees remuneration.
- (r) Split to allow for maximum receivable free of tax.
- (s) Consider the effects of benefits in kind on taxable remuneration.

### **3.4 Tax Avoidance**

Tax avoidance arises in a situation where the taxpayer arranges his financial affairs in a form that would make him pay the least possible amount of tax. For example, avoidance of value added tax can be achieved by anyone that does not buy the goods and/or services on which VAT is levied.

### **3.5 Anti-Avoidance Legislation**

The two possible forms of anti-avoidance legislation are:

- (a) Specific legislation to block known tax avoidance devices.
- (b) General anti-avoidance legislation which vests the revenue with power to disregard all transactions entered into that could be proved to have been entered into, solely for tax avoidance purposes.

The following are some advantages and disadvantages of each of these:

#### **(a) Specific anti-avoidance**

##### **Advantages**

- (1) Its provisions make the law imposing tax on a particular transaction clear and certain in its application;
- (2) Ineffective or inadequate legislation can be readily amended.

##### **Disadvantages**

- (1) May make an already complex legislation more complicated and less comprehensible to taxpayers, detracting from the simplicity canon of taxation.

- (2) The taxpayer would seek further loopholes and again exploit such for further tax avoidance which may create an unending need for further legislation.

**(b) General anti-avoidance**

**Advantages**

- (1) The number of anti-avoidance legislations is reduced, consequently minimising the complexity of the tax laws.
- (2) Provisions exist in the tax legislation to discourage all future tax avoidance, that is, schemes that are considered to have violated the spirit of the tax laws.

**Disadvantages**

- (1) Provisions are general, vague and could lack precision.
- (2) Too much reliance is placed on discretion of tax officials for its application. The tax officials could exceed the intention of the legislature in certain respects or fail to carry it out in full in some others.

### **3.6 Company Income Tax Act (CITA) Section 18**

Where the revenue service is of the opinion that any disposition is not in fact given effect to or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, it may disregard any such disposition or direct that such adjustments be made in respect of tax liability as it considers appropriate so as to counteract the reduction of tax liability which would otherwise be affected by the transaction and any company concerned shall be assessed accordingly.

Transactions between persons, one of whom either has control over the other or in the case of individuals, who are related to each other or between persons both of whom are controlled by some other persons, shall be deemed to be artificial or fictitious, if in the opinion of the revenue service, those transactions have not been made on terms which might fairly have been expected to have been made by persons engaged in the same or similar activities dealing with one another at arm's length. A company, in respect of which any direction is made under this section, shall have a right of appeal in like manner as though such direction were an assessment. The whole idea of these provisions is that where any disposition is not in fact

given effect to, the consequence of which is that a tax liability which should normally arise from such disposition did not arise, the revenue service would want to step in. this provision is intended to cover cases where the purported transaction, if recognised as valid, would enable the taxpayer to avoid payment of income tax on that which is truly his taxable income.

The transaction(s) would be considered as artificial, that is not genuine or fictitious.

When these situations are established, the tax authority may disregard such disposition. In the alternative, the authority may direct that such adjustments shall be made in respect of the income of an individual, or an executor, or a trustee, as the authority considers appropriate so as to counteract the reduction of liability to tax effected, or reduction which would otherwise be effected by the transaction.

### **3.7 Tax Avoidance and Tax Evasion**

The key distinction between tax avoidance and tax evasion rests squarely on whether it is illegal or legal.

#### **3.7.1 Tax Avoidance**

This is generally considered as a way of identifying the loop-hole in the tax law and then taking advantage of such loop-hole to reduce the tax payable.

#### **3.7.2 Tax Evasion**

This is considered illegal; it is a deliberate act on the part of the taxpayer not to pay tax due. If the taxpayer is found guilty of this offence, he may be penalised.

Tax avoidance and tax evasion can be compared as follows:

<b>Tax avoidance</b>	<b>Tax Evasion</b>
<b>Legal</b>	<b>Illegal</b>
Achievable through exploiting loopholes in the tax laws	Achievable through deliberate action of fraud and deceit or rendering incorrect returns
Results in taxpayer paying minimum tax possible	Results in taxpayer not paying correct tax or paying

without breaking the law	minimum tax through the breaking of the tax laws
Supported by the courts in decided cases	No support by the courts
No criminal liability	Tax evader could be charged to court for criminal offences with the consequent fines, penalties and, at times, imprisonment
When stretched to the extreme, the scheme could be disregarded (set aside) by the revenue service applying appropriate anti-avoidance legislation	At any level, revenue service will frown at tax evasion
No revenue service investigation as a result of tax avoidance. Prior years assessments will not be reopened	Revenue service investigation will be instituted. Revenue service has the power to open prior assessments beyond the statutory six-year limit.

### **SELF-ASSESSMENT EXERCISE**

What is the difference between tax evasion and tax avoidance?

### **3.8 Acceptance of Offer as Tax Consultant**

The acceptance of offer as tax consultant to a taxpayer is the indication of the readiness of the Tax consultant to render the specific services requested and to provide other special assignments to the client(s) from time to time.

The consultant from inception should understand the nature and scope of the assignment in order to provide adequate services to the client(s). Issues relating to professional fees should be fully discussed at the inception of the contract of service.

### **3.9 Clients' Documentation and Records**

After accepting the offer to act as tax consultant to any taxpayer, necessary documentation and information, should be put in place.

### **3.9.1 Documentation/and Information to be Maintained/Provided by Clients**

The Company's (client's) officers should have maintained the following document/records:

- (a) Certificate of incorporation
- (b) Certified True Copies (CTC) of Memorandum and Articles of Association (MEMAT)
- (c) CTC of Forms of Directors (CAC7), Allotment of shares (CAC2), Appointment of Secretary (CAC2.1) and Notice of Registered office (CAC3)
- (d) Certificate of increase in share capital including Stamp Duties, Registration fees, Board's Resolution, etc.
- (e) Contracts, Rents and other Agreements
- (f) Financial matters:
  - (i) Signed audited financial statements
  - (ii) Books of account, ledger, trial balance (hard & soft copies)
  - (iii) Fixed assets register and title documents
  - (iv) Accounts and procedural manual
  - (v) Payments vouchers, receipts, etc.
  - (vi) Banking & cash transaction documents
  - (vii) Monthly payroll and directors' emolument.
- (g) Correspondence with tax authorities and other third parties
- (h) Minutes of Board of Directors' and Annual General Meeting (AGM)
- (i) Tax and other payment receipts, assessments, forms, tax clearance certificates, etc.
- (j) Other financial and non-financial documents including appointment letters.

The above should be kept intact in a safe place, because they may be required for sighting by the revenue authorities, during registration, filing of assessments and tax examinations.

### **3.9.2 Documentation/Data to be Maintained by the Tax Consultant**

The following documentation/data, among others, will be maintained by the tax consultants in respect of each client. The documents which will either be kept in the permanent file or forwarded to the relevant tax office will include the following:



- (a) CTC of incorporation documents i.e. certificate of incorporation, MEMAT, directors, shareholders, secretary and share capital details, etc.
- (b) Engagement letters
- (c) Company auditors' details if different from that of tax consultant
- (d) Audited financial statements, capital allowances, income tax, education tax and other computations
- (e) Trial balance, detailed analysis and schedules on the financial statements
- (f) Correspondences with the client, tax authorities and third parties
- (g) Registration documents in respect of income tax, value added tax (VAT), PAYE, withholding tax and other levies
- (h) Records of billings outstanding
- (i) Other documents, financials and non-financials.

### **SELF-ASSESSMENT EXERCISE**

- i. List the documents maintained by a tax consultant.
- ii. What are the documents to be provided by clients?

### **3.10 Communication with Tax Authorities**

Communication with tax officials will usually cover the following:

- (a) Registration with tax authorities for income and other taxes using standard questionnaires.
- (b) Filing of tax returns time limits provided by the tax laws.
- (c) Self-assessments and objections to best of judgment (BOJ) assessment.
- (d) Tax queries and replies.

They are fully discussed as follows:

#### **3.10.1 Registration with Tax Authorities**

The FIRS and SIRS have a Standard Questionnaire which is expected to be followed by Taxpayers for the registration under the provisions of CITA, PITA, PPTA and other tax legislations/acts.

The following details together with CTC of Incorporation documents (Originals to be submitted for verification), will be provided in a formal

letter addressed to the Chairman of the relevant tax authority, in respect of every prospective taxpayers:

- (a) Name, registration number and date of incorporation/registration
- (b) The registered or home address (as applicable)
- (c) The business address
- (d) Names and addresses of the directors
- (e) Name and addresses of the shareholders together with their shareholdings.
- (f) Any other directorship held by the directors
- (g) The precise nature of business
- (h) Whether or not the business has any predecessor(s)
- (i) The date of commencement of business
- (j) The accounting year end
- (k) Details of company secretary (where applicable)
- (l) Details of the appointed auditors and tax consultant
- (m) Details of appointed bankers
- (n) Any other information which may help the tax authority in this regard.

### **3.11 VAT Registration**

A VAT able person or VAT agent is required to also file application for VAT registration at the nearest FIRS office. The application will be supported with CTC of the registration documents.

#### **3.11.1 Filing of Tax Returns**

Any company registered in Nigeria must submit relevant information to the tax authority within six months of existence or at commencement of operations (whichever is earlier). An individual must also provide relevant information in the specified format (Form A) at the beginning of every assessment year.

Filing of tax returns for individuals and corporate persons are done using prescribed self-assessment forms, with supporting documents.

The following are usually forwarded to FIRS as tax returns, within 18 months of companies' incorporation or six months after the end of the accounting year end (whichever is earlier):

- (a) Signed audited financial statements together with a covering letter from the tax consultant.
- (b) Capital allowances and income tax computation.
- (c) Self-assessment forms for income and education tax.

### **3.11.2 Self-Assessment for Individuals**

Tax returns for individuals are submitted at the beginning of every assessment year the self-assessment form (Form A) is completed, stating various sources of income and allowances reliefs claimable. The assessment forms must be signed and dated by the taxpayer.

It is relevant to note here that, tax payments to both FIRS and SIRS are now made via e-payment at designated banks. The e-payment has therefore reduced the level of written communication with the tax authorities.

### **3.11.3 Best of Judgment (BOJ) Assessment**

Where the taxpayer fails to file the self-assessment forms and pays the normal tax within the time limit specified under the law, BOJ assessment is raised on the affected taxpayer.

A valid objection must be raised within 30 days of service of such notice, stating valid grounds of objections.

### **3.11.4 Tax Queries and Replies**

#### **(a) Queries**

Tax queries emanate from desk examinations of tax returns by Tax Officials. Returns are examined, asking for supporting documents in order to ascertain whether or not the taxpayer's income has not been understated, reliefs not overstated or that the expenses deducted from the income for the period, were *wholly, exclusively, necessarily and reasonably incurred* in the production of those incomes.

Tax queries may not follow any specific pattern, but tax practitioners must have a better understanding of the taxpayer's operations, and possess adequate technical know-how, with relevant field experience.

The following issues may be raised from related documents, collected or verified by tax officials, in order to eliminate any private or capital

expenditure from the returns and also guide against tax avoidance shares to some reasonable extent:

- (a) Whether there exist, supporting documents for assets, liabilities income and expenditures in the name of the taxpayer.
- (b) Whether private expenses were included in the accounts.
- (c) Whether relevant documents such as certificate of acceptance, input VAT, invoices, supporting invoices, premium claims, invoices on administrative and operating expenses, etc. agreed with amounts stated in the accounts.
- (d) Whether PAYE deducted from salaries and withholding Taxes from supplies or professional fees were promptly remitted.
- (e) Whether capital expenditures in form of cost of increase in capital or incorporation expenses, general bad debts and depreciation have been written back to profit.
- (f) Whether losses and carry forward rules have been adequately observed.

## **(b) Replies**

When replying to tax queries, tax practitioners should endeavour to be more ethical and use subtle language as much as practicable. The consultant should avoid quoting decided cases or tax laws when one is not too sure that circumstances or scenarios are similar

Apart from the above, the consultant should make use of relevant supporting documents from both the client's office and his working papers. Third party documents not relevant to the queries raised should not be forwarded as an attachment.

Finally, the tax consultant should not be seen to be involved in any practices which could be construed to be tax evasion, fraud or outright criminality.

## **3.12 Communication with other Stakeholders**

This is specifically required to gather additional information on the client's business. These stakeholders are classified into the following:

- Communication with former tax consultant and auditors and;
- Communication with others. For example; bankers, pension fund administrators, lawyers and so on.

- (a) Banker – for bank statements is support of bank charges and to vouch certain entries.
- (b) Insurers for premium paid.
- (c) Pension fund administrator – for pension fund certificates, to support exemptions.
- (d) Other professionals, that is, lawyers for legal advice.

### **3.12.1 Third Party Evidence**

The tax consultant must obtain written permission from the client, in support of third parties evidence. One should exercise the duty of reasonable care in making use of any third parties' evidence.

## **4.0 CONCLUSION**

Most companies embark on tax planning in other to reduce their tax liabilities. Tax evasion is considered is considered a fraud and it is subject to criminal prosecution, fines and/or imprisonment. While tax avoidance is a legitimate act, which is all about identifying the loopholes in tax laws in other to take advantage of them.

## **5.0 SUMMARY**

This unit deals with tax planning, tax avoidance as tax schemes that taxpayers could utilise to achieve tax savings, such as tax savings schemes are only allowed if obtained through legitimate exploitation of loopholes in tax laws. We also discussed about communication with clients, relevant tax authorities and related parties. Current issues about tax registration, self-assessment, e-payment, objections and tax queries procedures were equally discussed.

In the next unit, we shall be examining taxation of incomes, offences and penalties.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. How do you compare tax avoidance with tax evasion?
2. Write short notes on the following:
  - (a) Tax queries and replies
  - (b) Third party evidence
  - (c) Best of judgement assessment
  - (d) Self-assessment for individuals
  - (e) Filling of tax returns.

3. Define VAT and state how the registration is undertaken.
4. What is tax avoidance? What are the possible ways by which this could be checkmated?

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 5 TAXATION OF INCOMES, OFFENCES AND PENALTIES**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Developments in Nigerian Taxation
  - 3.2 Chargeable Persons
  - 3.3 Types of Income
  - 3.4 Exempt Incomes
  - 3.5 Offences and Penalties
  - 3.6 Taxation of Income from Partnership
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we defined and explained the terms ‘tax planning’ and ‘tax avoidance’; differentiated between tax avoidance and tax evasion; identified clients documents to be kept and maintained by tax practitioners; discussed the nature and information required for registration of the taxpayers with the tax authorities; gave suitable replies to tax queries; and explained how to communicate effectively with other stakeholders on clients’ tax matters.

In this unit, we shall be examining taxation of incomes, offences and penalties.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- distinguish between earned and unearned incomes of individuals
- list the various incomes that are chargeable or exempted from personal tax
- explain the principles of allowable and disallowable expenses or deductions
- list the various reliefs and allowances to be deducted before arriving at the chargeable income for the relevant years of assessment.

### **3.0 MAIN CONTENT**

Taxation is a common phenomenon all over the world. Most countries cannot do without the imposition of tax, to boost its revenue generation. There are many definitions given to taxation by different authors. However, taxation can be explained as a weapon used by any government to share from the wealth of an individual or corporate body. Hence, it can be concluded that taxation is generally an imposition.

#### **3.1 Developments in Nigerian Taxation**

We shall examine the developments in the evolution of taxation in Nigeria under the following sub-heads:

##### **(a) Income Tax Management Act 1961**

There were various tax systems operating in the Northern, Western and Eastern regions of Nigeria before the Raisman Fiscal Commission of 1958 which recommended that there should be uniform basic principles for taxing incomes throughout Nigeria. It was this recommendation that was embodied in the Nigerian (Constitution) order in council 1960, which resulted eventually in the enactment of the income tax management act 1961 (ITMA 1961), ITMA 1961 was the precursor to CITA 1961, 1979 and 1990 as well as the personal income tax decree (now Act) of 1993.

##### **(b) 1975 Amendments**

In 1975, the Income Tax Management (Uniform Taxation Provisions) Decree No.7 was promulgated. This degree unified reliefs and rates throughout the country with the key advantage of resolving, to some extent, the proliferation of various tax laws in the different states of the federation.

##### **(c) 1985 Amendments**

The Finance Miscellaneous (Taxation Provisions) Decree 1985 introduced some reforms into the tax provisions such as:

- (i) Increases in personal allowances
- (ii) Tax authorities were empowered to request any bank for information about customers (individuals)



- (iii) The basis of computing capital allowances changed from reducing balance to straight-line method
- (iv) Capital allowance claimable was restricted to 75% for manufacturing business and 66<sup>2/3</sup> % for other businesses that with no limit for agricultural businesses
- (v) Interest on loan for agricultural and export purposes were to be treated as exempted from tax
- (vi) Losses carried forward to be limited to four years for businesses other than agricultural business.

**(d) 1987 Amendments**

The amendments to the Nigerian tax laws in 1987 included:

- (i) slight increase in personal allowances
- (ii) review of some capital allowances rate, and
- (iii) treatment of withholding taxes on interest and dividend as final tax payable, in other words, they are treated as Franked Investment Income (FII).

**(e) 1990 Amendments**

The following slight amendments were made:

- (i) Significant improvement in capital allowances rates; and
- (ii) Manufacturing businesses now to enjoy 100% capital allowance claimable.

**(f) 1992 Amendments**

The amendments include:

- (i) increase in personal income tax reliefs and allowances; and
- (ii) amendment in the table of tax rates.

**(g) 1993 Act**

In 1993, the Personal Income Tax Act was promulgated as Decree No.104, which replaced ITMA 1961 as amended up to the point of abrogation. The act provides for the taxation of every individual or corporate sole or body of individuals (e.g. partnership), that are deemed to be resident for that

year, in the relevant state and increase in the table of rates, for the taxation of individual under PITA.

## **3.2 Chargeable Persons**

Every human being or association of human beings resident in the appropriate tax jurisdiction and engaged in trade or business or obtaining taxable remuneration are ordinarily regarded as taxable.

It follows from the above, that if a person has no income or has receipts that are not taxable, he cannot be taxed under the Personal Income Tax Act (PITA).

### **3.2.1 Chargeable Incomes**

Chargeable incomes are the incomes on which chargeable persons are to be assessed to tax under PITA. These incomes include:

- (a) Gains or profits from any trade, businesses, profession or vocation carried on by the chargeable person
- (b) Salaries, wages, fees, allowances or other gains or profit from employment
- (c) Bonuses, premiums or other perquisites granted to an employee
- (d) Gains or profits including any premium arising from a right granted to any other persons for the use of occupation of any property
- (e) Dividends, interest or discounts
- (f) Any other profits, gains or other payments.

The following are, however, excluded from taxation:

- (i) Re-imbusement to an employee for expenses incurred by him which does not constitute a profit or gain
- (ii) Medical or dental expenses incurred by an employee
- (iii) Cost of passage to or from Nigeria incurred by an employee
- (iv) Any sum paid in respect of maintenance education of a child
- (v) Any compensation for loss of employment.

### 3.3 Types of Income

Generally, there are two broad categories of incomes and these are earned and unearned incomes.

#### (a) Earned incomes

In relation to individual, earned incomes, means incomes derived from a trade, business, profession, vocation or employment, carried on or exercised by him. It means incomes that were earned through physical, intellectual or artistic exertion, as opposed to those earned passively through investment. Earned incomes are profits, salaries, wages, commission, bonuses, etc.

#### (b) Unearned incomes

These are incomes derived from sources other than employment, business or reward for services rendered. Mainly, unearned incomes are investment incomes such as rental incomes, dividends, royalties, earnings from trademark, patents, etc. It also includes gifts, inheritance and bequeathals.

### 3.4 Exempt Incomes

Exempted incomes under the Personal Income Tax in Nigeria, include the following, amongst others:

- (a) The official emoluments of the holders of the office of the president, vice-president, the governor of a state, the deputy governor or anybody acting in those capacities.
- (b) All consular fees received on behalf of a foreign state or by a consular officer or employee except where the officer is a Nigerian, working in Nigeria.
- (c) An income in respect of which tax is remitted or exempted under the provisions of the Diplomatic Immunities and Privileges Act.
- (d) The income of a local government or government institution.
- (e) The income of any ecclesiastical, charitable or educational institution of a public character.
- (f) Wound and disability pension granted to members of the armed forces or of any recognised national defense organisation.
- (g) Pension granted to a person under the provisions of the pensions act relating to widows and orphans.

- (h) The income of a trade union, registered under the trade union act.
- (i) Gratuities.
- (j) The income of a cooperative society.
- (k) The income of a statutory or registered friendly society.
- (l) A sum withdrawn or received by an employee from a pension, provident or other retirement or other benefits scheme, fund or society approved by the Joint Tax Revenue Service.
- (m) The income of a person other than a citizen of Nigeria from employment in technical assistance scheme with the government of the federation or a state.
- (n) Interests accruing to a person not resident in Nigeria. These interests are on government loans from international institutions, deposit accounts or transfers made wholly in foreign currencies, loans raised in the United Kingdom.
- (o) Dividends paid to a person by a company incorporated in Nigeria provided:
  - (i) The equity participation of the person in the company paying the dividend is either wholly paid for in foreign currencies or by assets brought into Nigeria between 1<sup>st</sup> January, 1987 and December 31, 1992.
  - (ii) The person to whom the dividends are paid owns not less than 10% of the equity share capital of the company.
  - (iii) The tax free periods for (i and ii) above are limited to 5 years in the case of agricultural and agro-allied companies and 3 years for other beginning from the year of assessment following the year the capital was brought into Nigeria.

### 3.5 Offences and Penalties

There are many offences and prescribed penalties in the Person Income Tax Act in order to: maintain the integrity of the tax system, encourage compliance and minimise the cost of collection.

The offences and penalties include the following:

- (a) **Failure to submit returns:** Where the offence is failure to submit returns, a further sum of ₦40 daily for the period of continued failure shall be payable and in case of default of the payment, the defaulter shall be sentenced to six months imprisonment upon conviction.

- (b) **Non-compliance with notice:** Where a person fails to comply with the requirements of a notice duly served on him, or to attend in answer to a summons served on him, he would be guilty of an offence and be liable on conviction to a penalty of an amount equal to the income tax chargeable on him for the proceeding year of assessment.
- (c) **Incorrect returns:** A person who makes incorrect returns by omitting or understating any income liable to tax is guilty of an offence and liable on conviction to a fine 200 and double the amount of tax, which has been undercharged.
- (d) **False statements and returns:** Anybody who makes a false statement in respect of deduction, set-offs, relief's, etc or abets, aids, assists or counsels, shall be guilty of an offence and liable on conviction to a fine of ₦1,000 or imprisonment for five years or both.

### SELF-ASSESSMENT EXERCISE

- i Payment of fines as a result of failure to submit returns is referred to as .....
- ii. Non-compliance with notice or submission of incorrect returns amounts to .....

### PERSONAL INCOME TAX COMPUTATION FORMAT

	N	N
Earned Income		
Salary		XX
Commission/Bonus	XX	
Pension		XX
Benefits-in-Kind/Perquisites		XX
Fees/Allowances		XX
Trading Income		<u>XX</u>
Total Earned Income		XX
<b>Unearned Income</b>		
Dividend (gross)	XX	
Rent (gross)	XX	
Interest (gross)	XX	
Director's Fees	<u>XX</u>	
Total Unearned Income		<u>XX</u>

Statutory Total Income		xx
<b>Deduct:</b> General Charges		
Mortgage Interest paid	xx	
Approved Subscription	xx	
		(xx)
<b>Net Statutory Total Income</b>		xx
Deduct Personal Reliefs		(xx)
Taxable/Chargeable Income		xx
Tax Due (Using tax table)		<u>xx</u>

### Illustrations 5-1

Mr. Udem has been in employment of a company for ten years and also runs a private business centre on part-time basis.

Mr. Udem income from various sources for the relevant years is stated thus:

2008	₦
Salary and wages	420,000
Christmas bonus	42,000
Overtime	73,000
Benefits in kinds	64,000
Profits from business center operation (2007)	194, 000
Profit from business centre operation (2008)	260,000
Other income in 2008	
Dividend (gross)	14, 000
Rent (gross)	80, 000

Mr. Udem is married with three children; all of them are below 16 years. He also maintains his aged mother up to ₦42, 000 per annum. He pays ₦15, 000 as annual mortgage interest on his personal building and an approved subscription in the sum of ₦12, 000 per annum.

You are required to compute:

- Mr. Udem Chargeable Income for 2008 Assessment Years; and
- Tax Due on him for 2008 using Current Tax Table.

**Suggested Solution 5-1****Mr. Udem****Income Tax Computation for 2008 Assessment Year**

Earned Income:	<b>₦</b>	<b>₦</b>
(a) Salaries & wages		420,000
Christmas bonus		42,000
Overtime		73,000
Benefits in kinds		64,000
Allowances		99,100
		698,100
Trading Profit (PYB)		194,000
Total Earned Income		892,100
Unearned Income:		
Dividend (gross)	14,000	
Rent (gross)	80,000	
Total unearned Income		94,000
Statutory Total Income		986,100
Deduct General Charges:		
Mortgage Interest	15,000	
Subscription	12,000	27,000
Net Statutory total income		959,100
Less: Personal Relief (W1)		(192,920)
Chargeable Income		766,180
Tax Due (W2)		164,145
W1: Calculation of Reliefs:		<b>₦</b>
Personal Allowance		
(N5000+20% of N892,100)		183,420
Children Allowance (N2,500x3)		7,500
Dependant Relative		2,000
		192,920
W2: Calculation of Tax Due:		
1 <sup>st</sup> N30,000 @ 5%		1,500
Next N30,000 @ 10%		3,000
Next N50,000 @ 15%		7,500
Next N50,000 @ 20%		10,000
Next N606,180 @ 25%		151,545
Tax Borne		173,454
Deducted Tax Suffered at Sources:		

Dividend – N14,000 @10%	1,400	
Rent – N80,000 @ 10%	8,000	9,400
Net Tax Payable		164,145

### 3.6 Taxation of Income from Partnership

This topic will be discussed under the following sub-topics.

#### 3.6.1 Introduction

A partnership is defined as “an association of two or more persons agreeing to carry on business with a common view of making profit”.

A partnership can be formed for the purpose of carrying on a trade, profession or vocation, because partnership involves more than one person, it can only operate successfully through agreed conditions, which are usually spelt out in a partnership agreement or deed.

Partnership agreement will spell out the rights and obligations of each partner which will include:

- Name of the partnership
- Capital contribution
- Rate of interest on capital and drawing
- Partners drawings
- Partners salaries and
- Profit/losses sharing ratio.

#### 3.6.2 Fundamental Principles to Partnership Computation

The following fundamental principles are to be noted in dealing with partnership computations:

- (a) Salaries, interest on partners’ capital and leave passage of the partners are allowable expenses in determining the profit of the partnership.
- (b) Salaries, interest on partners’ capital and leave passage costs are taxable in the hands of the individual partners.
- (c) The partner’s share of profits is taxable in his hands along with (b) above.



- (d) Partners are allowed to trade in their own right, subject to the partnership agreement and the incomes from such a trade are to be aggregated with their incomes from the partnership for tax purposes.
- (e) Where a partner trades with his own partnership firm and earns income, such as interest on loan or rental from hired accommodation, such incomes are to be treated as those in (b) above.
- (f) When the income that accrues to a partner under (b) above, is a loss, such a loss shall be set off against the income in (d) above, such that if the loss in (d) is higher, the balance shall be regarded as the loss he has sustained in the trade:
- (g) Where partnership place of business is different from that of one or more of the partners, the tax authority of the place of location of the principal office of the partnership shall be responsible for determining the partnership income or loss and its allocation between the partners and having determined the income/loss accruing to each partners, it is the duty of that tax authority where the partnership is located, to supply the information to the tax authorities where the non-resident partner(s) are located, and
- (h) An appeal against an assessment in relation to (g) above shall be to the tax authority where the partnership is located.

### **3.6.3 Determination of Partners' Income**

Since a partnership is not a legal person, it cannot be assessed to tax as an entity. It is the individual partner's incomes that can be assessed to tax. For the individual partners, the taxable income is made up of the following:

- Partner's salary
- Partner's costs charged into the accounts
- Passages cost charged into the accounts and
- Partner's share of the profits.

The above will be aggregated with all other incomes of the partner from other sources, to arrive at his total income which will be chargeable to tax for the relevant period.

As applicable in the sole proprietorship, it should be emphasised that determining the profit of a partnership, is purely an accounting issue. Also, where no records (or inadequate records) are kept, the incomplete records accounting procedure or the application of capital accretion method by which the increase in the net worth of a business enterprise within the relevant trading period is determined are used to determine the profit of the partnership.

However, in computing the adjusted profit to be shared by the partners, leave passage, interest on capital and partners salaries should not be added back. If they are added back, those portions of the income will be assessed to tax twice, since they will also feature separately as taxable incomes in the hands of the partners who earn them. So , it should be borne in mind that if salaries, interest on capital and private passage costs have been charged to the accounts in arriving at the profits, they are not to be added back in the computations. Where they have not been charged to the accounts they should be deducted from the profits to be shared by the partners to avoid double taxation. This is because like those items (the quantum of which are already agreed in the partnership agreement) the profit to be shared will be charged to tax.

### SELF-ASSESSMENT EXERCISE

- i. .... spells out the rights and obligations of each partner such as: name, capital contribution, salary and/or drawing, interest on capital, share of profit, etc.
- ii. The taxable income of a partner is made up of .....

### Illustration 5-2

Abuja, Lagos and Benin were in partnership in the law firm of Abuja, Lagos, Benin & Co. The company has the following profit and loss account for the year ended 31<sup>st</sup> December, 2008.

	N	N
Gross earnings		2,100,000
Less: Staff salaries	500,000	
Utility bills	35,000	
Office rentals	50,000	
Office expenses	25,000	
Bad debts	55,000	

Interest on loan – Abuja =	10,000		
Lagos =	15,000	25,000	
Interest on Capital – Abuja =	10,000		
Lagos =	7,500		
Benin =	5,000	22,500	
Depreciation		7,500	
Consultancy costs		345,000	(1,065,000)
Net profit for the period			1,035,000

### Note

Capital allowances agreed for the period was ₦7, 500

Off the staff salaries, an equal amount of ₦72, 000 per annum was paid to each of the partners

Benin owned the building that housed the chambers

Only ₦ 30,000 of the bad debts was determined to be bad. The remaining ₦25, 000 is just a provision at 5% of debtors.

The ration of interest on capital paid to the partners reflects their contributions and their share of profits.

### Required:

- Compute the adjusted income of the partnership for the year.
- Calculate the profit shared by each partners.
- Calculate the income of each partner for tax purposes.

### Suggested Solution 5-2

<b>a. Calculation of adjusted income in a partnership</b>			
		<b>₦</b>	<b>₦</b>
	Net profit per account		1,035,000
	Add: Depreciation	7,500	
	Provision for bad debts	25,000	
			32,500
			1,067,500

	Deduct capital allowances					7,500
	Adjusted profit					1,060,000
<b>b</b>	Calculation of the Profits shared by each partner					
	Adjusted profit available for sharing	=				1,060,000
	Adjusted profit actually shared	=				(1,035,000)
	Retained profit					25,000
	Given: the Ratio of interest on capital = the ratio of contribution to capital = the ratio of sharing of profit					
		10,000	to	7,500	to	5,000
		4	to	3	to	2
	As between	Abuja		Lagos		Benin
	Abuja =	4/9	X	1,035,000 1	=	N460,000
	Lagos =	3/9	X	1,035,000 1	=	N345,000
	Benin =	2/9	X	1,035,000 1	=	N230,000
<b>c</b>	Calculation of assessable Income of each partner					
	Abuja		Lagos		Benin	
			<del>N</del>		<del>N</del>	<del>N</del>
	Profit shared		460,000		345,000	230,000
	Interest on capital		10,000		7,500	5,000
	Interest on loan		10,000		15,000	-
	Office rental		-		-	-
	Assessable Incomes		480,000		367,500	285,000

#### 4.0 CONCLUSION

This unit discusses the incomes of individuals and partners chargeable to tax under Personal Income Tax Act (PITA) after allowing for deductions and reliefs. Profit from table, profession or vocation are taxed in the hands of partners in a partnership. Tax tables are usually provided to determine the tax payable. Commencement and cassation rules that apply to individuals also apply to partnerships.

In addition, the unit identified the chargeable person who bears the final tax burden. Finally, the tax computation of beneficiaries is as applicable to that

of individuals under PITA where reliefs are deducted before subjecting the chargeable income to tax.

## **5.0 SUMMARY**

In this unit, we have distinguished between earned and unearned incomes of individuals. We also discussed the various incomes that are chargeable or exempted from personal tax and enumerated the principles of allowable and disallowable expenses or deductions. Finally, we determined various reliefs and allowances to be deducted before arriving at the chargeable income for the relevant years of assessment.

In this next unit, we shall explore the taxation of income from settlement, trusts and estates.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. Distinguished between earned and unearned incomes of individuals.
2. What are the various incomes that are chargeable or exempted from personal tax? Discuss some of them that you know.
3. Enumerated the principles of allowable and disallowable expenses or deductions.
4. What reliefs and allowances are deducted before arriving at the chargeable income for the relevant years of assessment? List and explain these.

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack. (2011).

## **UNIT 6      TAXATION OF INCOME FROM SETTLEMENT, TRUSTS AND ESTATES**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Developments in Nigerian Taxation
  - 3.2 Chargeable Persons
  - 3.3 Types of Income
  - 3.4 Exempt Incomes
  - 3.5 Offences and Penalties
  - 3.6 Taxation of Income from Partnership
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we defined and explained the terms ‘tax planning’ and ‘tax avoidance’; differentiated between tax avoidance and tax evasion; identified clients documents to be kept and maintained by tax practitioners; discussed the nature and information required for registration of the taxpayers with the tax authorities; gave suitable replies to tax queries; and explained how to communicate effectively with other stakeholders on clients’ tax matters.

In this unit, we shall be examining taxation of incomes, offences and penalties.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- workout the tax due from the income of a trustee
- calculate the tax from the income of an executor
- deduce the tax from estates.

### **3.0 MAIN CONTENT**

#### **3.1 Assessment Income of a Trustee, Executor or a Beneficiary**

The assessment income of a trustee, executor or a beneficiary of a settlement or trust for tax year, shall be the income of that person on preceding year basis, derived from business, profession or vocation.

##### **3.1.1 Useful Definitions**

The definition of the following useful concepts would assist you in understanding the working of taxation on the income of a trustee, executor or a beneficiary of a settlement or trust.

###### **(a) Settlement**

A settlement is a means by which enjoyment of an estate or part of it is transferred to another person, either through a disposition, trust, covenant, agreement, arrangement, or transfer of assets by reference to a trust deed for the benefit of persons specified.

###### **(b) Trust**

This is an equitable obligation binding a person called trustee, to deal with a property over which a control is exercised (which is called trust property) for the benefit of person (beneficiaries) of which he himself may be one.

###### **(c) Estate**

It is the aggregate of the properties possessed by person including his goods, money and other type of property.

###### **(d) Executors**

A person appointed by the will of a deceased person to administer his estate after his death.

###### **(e) Administrator**

A person that is appointed by the Court to administer the Estate of an Intestate or o a Testator where an Executor has not be appointed or if appointed does not act.

**(f) Administration period**

It is the period between the date of death and the date in which the Executor is able to set up the Trust or distribute the residue of the estate.

**(g) Annuitant**

This refers to a person receiving an annual payment from the estate which may be charged on the income or capital of specific assets of the estate.

**(h) Life tenant**

It is the right of the person on the income or property held in trust for life.

**(i) Remainder man**

This refers to a person who has a right to the capital of the settlement when the life interest terminates.

**(j) Legatee**

A legatee is the person to whom a legacy is bequeathed

**(k) Settler**

A settler includes a person by which a settlement was made or entered into directly or indirectly and includes a person who has provided funds directly or indirectly for the purpose of the settlement or has made with any other person reciprocal arrangement for that other person to make or enter into the settlement.

**(l) Income of settlement, trust and estates**

This is the income of a settler or the person who created the trust or settlement. It includes all such incomes derived from, received in, or brought into Nigeria.

**SELF-ASSESSMENT EXERCISE**

- i. The transfer of enjoyment of an estate from person to another is called .....
- ii. The person to whom a legacy is bequeathed is referred to as .....
- iii. .... is the right of a person on income or property held in trust for life.



**Illustration 6-1**

The records of Farouke El Nafaty settlement created in favour of ADE, BALA and UFOMA as at 31/12/2008 are as follows:

	N
Rental Income (gross)	24,000
Trade income	10,000
Dividend (gross)	18,000
Sundry income	12,000

The following additional information is available:

Each beneficiary is entitled to 1/5 share of the net distribution income.

Interest on debt repayable by the settlement is N2, 000

Fixed annuity to beneficiary is N3, 000

Trustee remuneration per trust deed:

- i. fixed N 1,000 each (2 Trustee)
- ii. 2% of total income

Administrative and other expenses – N3, 800

Under the terms of the trust deed, the trustee made discretionary payment to Ade, BALA & UFOMA as follows:

		N
ADE	-	3,000
BALA	-	2,800
UFOMA	-	1,500

Capital allowances – N8, 024

The children have no other income.

ADE, BALA and UFOMA are only entitled to personal allowances.

**Required**

Compute aggregate income due to the Estate and Tax Payable by ADE, BALA and UFOMA.

**Suggested Solution 6-1****Farouk El Nafaty Estate:****Computation of Income 2009 Year of Assessment**

	₦	₦				
Rental income		24,000				
Trading income		10,000				
Dividend		18,000				
Sundry income		12,000				
		64,000				
Deduct chargers						
Administrative and other expenses	3,800					
Trustee remuneration – fixed	2,000					
Fixed annuity	3,000					
Interest on debt	2,000					
Trustee remuneration (2/102 x 53.200)	1,043	(11.843)				
		52.157				
Less: Capital Allowances		(8.024)				
Computed income		44.133				
Discretionary payments:	3,000					
Ade						
BALA	2,800					
UFOMA	1,500	(7,300)				
		36.833				
Specific:						
Ade	1/5 x 36,833 -	7,367				
Bala	1/5 x 36,833	7,367				
Ufoma	1/5 x 36,833	7,367				
Trustee net income		14,732				
<b>Aggregate income from the estate</b>						
	ADE	BALA	UFOMA	Annuitant	Trustee	Total
	₦	₦	₦	₦	₦	₦
Annuity	-	-	-	3,000	-	3,000
Discretionary	3,000	2,800	1,500	-	-	7,300
Residue	7.367	7,367	7,367	-	14,732	36,833
<b>Total</b>	10,367	10,167	8,867	3,000	14,732	47.133
<b>Less:</b>						
Personal Relief	97,073)	(7,033)	(6,773)	-	-	

(5,000 + 20% of E.I)						
Chargeable income	3,294	3,134	2,094	3,000	14,732	
<b>Tax Due:</b>						
<b>1st 30,000 @ 5%</b>	164,70	156,70	104,70			

#### 4.0 CONCLUSION

The unit identifies the chargeable person who bears the final tax burden. The tax computation of beneficiaries is as applicable to that of individuals under Personal Income Tax Assessment (PITA) where reliefs are deducted before subjecting the chargeable income to tax.

#### 5.0 SUMMARY

In this unit, we defined some useful concepts applicable to the topic and which would assist students in working out the assessment and tax payable by the trustees and executors of estates.

With this, you have come to the end of the first module in this course.

#### 6.0 TUTOR-MARKED ASSIGNMENT

1. Student is advised to write his hands on the illustrations in the unit and others in similar textbooks to enable him/her have a good grasp of the procedures of assessing the tax payable by the trustees or executors of an estate.
2. Write short notes on the under listed concepts:
  - Settlement
  - Trust
  - Estate
  - Executors
  - Administrator
  - Administration period
  - Annuitant
  - Life tenant
  - Remainder man
  - Legatee

- Settler.

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack. (2011).

## MODULE 2

Unit 1	Withholding Tax
Unit 2	Value Added Tax
Unit 3	Capital Allowances
Unit 4	Capital Gains Tax
Unit 5	Tax Effects of Privatisation and Commercialisation
Unit 6	Profits, Assessable Profits and Tax Payable

### UNIT 1 WITHHOLDING TAX

#### CONTENTS

1.0	Introduction
2.0	Objectives
3.0	Main Content
3.1	Withholding Tax – Definition of Concept
3.2	Merits of Withholding Tax
3.3	Rates of Withholding Tax in Nigeria
3.4	Withholding Tax and VAT on Contracts
3.5	Problems of Administering Withholding Tax
4.0	Conclusion
5.0	Summary
6.0	Tutor-Marked Assignment
7.0	Reference/Further Reading

#### 1.0 INTRODUCTION

Welcome to the second module in this course. This module is made up of six units with the following very useful topics: Withholding Tax, Value Added Tax, Capital Allowances, Capital Gains Tax, Tax effects of Privatisation and Commercialisation as well as Profits, Assessable Profits and Tax Payable.

In this unit, we shall explore withholding tax.

#### 2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define withholding tax
- list the merits of withholding tax

- discuss withholding tax and VAT on contracts
- enumerate the problems of administering withholding tax.

### **3.0 MAIN CONTENT**

#### **3.1 Withholding Tax (WHT) – Definition of Concept**

Withholding Tax (WHT) is an advance payment of tax, which is deducted at source on certain transactions and later applied, where it is not a final tax, as tax credit in the settlement of the income tax liability of the to which the payment that suffered the deduction relates. Arising from this definition are the following peculiarities of the tax:

- Withholding tax is a deduction at source, which gives the taxpayer no option as to whether to pay or not.
- Withholding tax is an advance payment in lieu of the income tax to be paid later. This means that it not a separate tax.
- Withholding tax being an advance payment of income tax cannot be used later as credit for any other tax such as Education Tax or value added tax.
- Some withholding taxes are regarded as final tax. Where this is so, the income from which they have been deducted can no longer be brought into account for tax purposes.
- As withholding tax is to be utilised as credit for the income tax liability of the year to which the income relates, it means that one cannot use it to settle back year or future year tax liabilities, until the account of the year to which the WHT relates has been finalised, and tax fully settled with the withholding or part thereof, still remaining unutilised.
- Withholding tax as a collection device was introduced in a limited form by the CITA and later expanded in terms of coverage.

#### **SELF-ASSESSMENT EXERCISE**

In your own words, how would you define withholding tax?

#### **3.2 Merits of Withholding Tax**

The advantages of withholding tax are numerous and these have made the tax more and more attractive. They include the following:

- (a) It helps to strengthen the tax machinery by engaging numerous officials and collecting agents in tax work, despite the fact that they are not government workers.
- (b) As a result of (a) above, tax collection becomes cheaper.
- (c) Withholding tax helps to bring obscure transactions into the tax net.
- (d) Withholding tax helps to bring unknown taxpayers into the tax net.
- (e) As a result of (c) and (d) above, withholding tax helps broaden the base of the tax and increase the quantum of collection.
- (f) Withholding Tax makes tax payment less cumbersome to the taxpayer who may not bother going to the tax office in order to pay his tax.
- (g) Withholding tax ensures a regular flow of tax revenue to government.
- (h) Withholding tax reduces the incidence of tax evasion.
- (i) Withholding tax helps educate the taxpayer and the tax agent about taxation.
- (j) Withholding tax enhances voluntary compliance.

### 3.3 Rates of Withholding Taxes in Nigeria

Below is a tabular rate of withholding taxes in Nigeria.

Type of Payments	Companies	Individual
	rate (F.I.R.S)	rate (S.I.R.S.)
Royalty	10%	5%
Rents (including hire of equipment)	10%	10%
Dividends	10%	10%
Interests	10%	10%
Commissions	10%	5%
Consultancy & professional services	10%	5%
Technical services	10%	5%
Management services	10%	5%
Director fees	-	10%
Building construction	5%	5%
Contract supplies	5%	5%

*Source: FIRS (2011)*

### SELF-ASSESSMENT EXERCISE

There are some merits in withholding tax. Name six of them that you know.

### 3.4 Withholding Tax and VAT on Contracts

The distinction between deduction of withholding tax from contract sums and collection of VAT from contractors when they are paid is very important. Incidentally, both withholding tax and VAT on contracts now carry the same tax rates of 5%. So, on each contract, two cheques of equal amounts are to be prepared; one for WHT withheld and the other for VAT collected. The WHT is paid to the relevant tax authority depending on whether the taxpayer is a corporate body or an individual. The VAT on the other hand can only go to the FIRS under the Nigerian tax laws.

### 3.5 Problems of Administering Withholding Tax

There are many problems associated with the administration of WHT. These include:

- (a) Non-deduction: Some organisations pay their contractors without deduction of withholding tax. The reason may be either:
  - i. To help them; or
  - ii. Out of ignorance; or
  - iii. As a result of orders from above. This is a very serious offence against the law.
- (b) Non-remittance: Some tax agents deduct and fail to remit but rather prefer to make use of the money in their operations. This is nothing but stealing from both the state who will suffer revenue diminution and the taxpayer who will not be able to take credit for the deductions. When such cases are uncovered, the revenue authority should always endeavour to apply the necessary sanctions.
- (c) Wrong Rates: Wrong rates are often applied either ignorantly or to help the taxpayer. In this regard, it is important to note that the rate to be applied is the rate applicable at the time of payment/deduction and not the rate prevailing when the contract was awarded/executed.
- (d) Credit notes not dispatched: When the taxpayers are not given credit notes, they are not given credit for tax withheld. They insist that they have suffered the tax, while the Revenue Service insists on seeing the credit notes since the deductions may have been diverted or paid to the wrong tax authority.



- (e) Incomplete/incorrect information: Incomplete or incorrect information on the payment schedule may result in the issuance of a defective credit note. This may lead to problems in granting tax credit for tax withheld.
- (f) Payment to wrong tax authorities: There have been cases in which taxes withheld from companies are paid to the SIRS and those collected from individuals are remitted to the FIRS, when these happen the taxpayers cannot take credit since no tax authority will give credit for taxes not collected by it. The answer to this is honesty by the tax authorities. They should have the courage to re-direct such payments.
- (g) Cases of lumping: In some cases, deductions from both individuals and corporate bodies are lumped together in one cheque and paid to either the FIRS or SIRS. In this situation, even the payment schedule attached cannot help since only one composite cheque is attached for money that is for two different tax authorities. Such cheques should be returned to enable the collection agent to issue separate cheques to the appropriate tax authorities.
- (h) Wrong classification of activities: Where the rates of tax deduction are different, wrong classification of activities can result in either overpayment or underpayment. The major problem of misclassification of activities, however, is for example, when contract supplies are classified as across the counter purchases which would lead to total non-payment of tax.
- (i) Dishonoured cheques: Incidents of dishonoured cheques have become the exception rather than the rule: therefore, treasury receipts are not issued until the cheques are cleared. The prevalence of dishonoured cheques was partly responsible for the introduction of direct payment of tax to designated banks.
- (j) Failure to co-operate: Tax officials need to go round from time to time to monitor the extent of co-operation by collection agents. Very often they meet with hostile reception by people who should know better such as permanent secretaries, directors, chairmen of government parastatals, etc. each time there is a withholding tax inspection, it is necessary for the following to be made available for examination:

- Cash book
- Contract file
- Cheque stubs
- Copies of payment schedule
- Payment certificate; and
- Payment vouchers.

#### **4.0 CONCLUSION**

We have defined withholding tax as an advance payment of tax, which is deducted at source on certain transactions and later applied. There were several other definitions made in the unit. The advantages of withholding tax were enumerated while the problems of administering this type of tax were also listed.

#### **5.0 SUMMARY**

In this unit, we have defined withholding tax, listed the merits of withholding tax, discussed withholding tax and VAT on contracts. We also enumerated the problems of administering withholding tax.

In the next unit, we shall discuss value added tax.

#### **6.0 TUTOR-MARKED ASSIGNMENT**

1. Differentiate between withholding tax and value added tax.
2. Enumerate the problems of administering withholding tax in Nigeria.

#### **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 2     VALUE ADDED TAX**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Value Added Tax – Definition of Concept
  - 3.2 Goods Exempted from VAT
  - 3.3 Services Exempted from VAT
  - 3.4 VAT Returns, Remittances, Recovery and Refund
  - 3.5 Administration of VAT, Committee and Tribunal
  - 3.6 Definition of Terms
  - 3.7 Sharing of VAT Proceeds
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 Reference/Further Reading

### **1.0 INTRODUCTION**

In this unit, we defined withholding tax; listed the merits of withholding tax; discussed withholding tax and VAT on contracts; and enumerated the problems of administering withholding tax.

In the next unit, we shall discuss value added tax.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- define value added tax
- list the goods and services exempted from value added tax
- discuss VAT returns, remittances, recovery and refund
- enumerate the functions of VAT committee and tribunal
- specify how VAT proceeds are shared between the three tiers of government in Nigeria.

### **3.0 MAIN CONTENT**

#### **3.1 Value Added Tax (VAT) – Definition of Concept**

Value Added Tax (VAT) is an indirect tax like excise duty, first levied under the Value Added Tax Act (the Decree) No.102 of 1993 (as amended), with effective date of 1 December, 1993. The act repealed the Sales Tax Act, 1986, it is now known as Value Added Tax Act, Cap. VI, LFN 2004.

The tax is charged on the supply of goods and services. The vendor has the responsibility to collect it from the purchaser (persons or companies), on behalf of the Federal Inland Revenue Service. Individuals who are not charged with the responsibility of collecting PAYE are not required under the act to collect VAT. The tax is charged and payable on the supply of all goods and services, other than those exempted.

#### **SELF-ASSESSMENT EXERCISE**

- i ..... is an indirect tax which replaced the sales tax.
- ii ... is charged and payable on the supply of all goods and services, other than those exempted.

#### **3.2 Goods Exempted from VAT**

The following are goods exempted from value added tax:

- All medical and pharmaceutical products
- Basic foods items; processed food items do not seem exempted
- Books and educational materials
- Baby products
- Fertiliser, locally produced agricultural and veterinary medicine, farming machinery and farming transportation equipment
- All exports
- Plant and machinery imported for use in the Export Processing Zone
- Plant, machinery and equipment purchased for utilisation of gas in downstream petroleum operations
- Tractors, ploughs and agricultural equipment and implements purchased for agricultural purposes.

### 3.3 Services Exempted from VAT

We list below the services exempted from value added tax:

- Medical services
- Services rendered by Community Banks (now Micro Finance Banks), Nigerian Agricultural Cooperative Rural Development Bank (NACRDB) and Mortgage Institutions
- Plays and performances conducted by educational institutions as part of learning
- All exported services
- Goods and services purchased for the use of diplomats and donor funded projects.

Rate: The tax is computed at the rate of 5 per cent of the value of all vatable goods and services.

### 3.4 VAT Returns, Remittances, Recovery and Refund

A vatable person shall pay to the supplier the VAT on vatable goods and services purchased by or supplied to him. The VAT so paid by a vatable person is known as input VAT.

A vatable person shall on supplying vatable goods or services to his accredited distributor, agent, client or consumer, as the case may be, collect the VAT on those goods or services at the above mentioned rate. The VAT collected by a vatable person shall be known as an output VAT.

A vatable person shall, on rendering a return:

- a. If the output VAT exceeds the input VAT, remit the excess
- b. If the input VAT exceeds the output VAT, a vatable person will be entitled to a return of the excess VAT from the FIRS on production of such documents as may be required from time to time.

The Nigerian Customs Services shall before releasing vatable goods to its importer, demand the Value Added Tax Compliance Certificate issued by the FIRS on those goods.

### Illustrations 8-1

A pharmaceutical company who deals in drugs also sells gift items in order to attract customer.

Details of sales and purchases for December 2008 were:

	₦
Sales pharmaceutical product	640,000
Sales of gift items and supply of performs	179,920
Total sales for the month	820,820
Vat paid on purchases for December 2008 amounted to	₦6,950
<b>Required:</b> Calculate VAT payable to the tax office	
<b>Suggested Solution 8-1</b>	
<b>CALCULATION OF VAT PAYABLE FOR DECEMBER 2008</b>	
	₦
Total sales	820,820
Less good exempted	640,900
Vatable goods sold (including VAT @ 5%)	179,920
Sales excluding VAT ( $\frac{100}{105} \times \text{N}179,920$ )	(171,352)
Out VAT @ 5%	8,568
Input VAT	6,950
Net VAT payable	1,618

### 3.5 Administration of VAT, Committee and Tribunal

The Federal Inland Revenue Service is responsible for administrating the Value Added Tax.

There is a committee known as the Value Added Tax Technical Committee comprising.

- The Chairman of the Federal Inland Revenue Service (as the Chairman)
- All Directors in the Federal Inland Revenue Service
- The Legal Adviser to the Federal Inland Revenue Service
- A Director in the Nigeria Customs Services; and
- Three representatives of the state government who are members of the Join Tax Revenue Service.

### 3.5.1 Functions

The functions of the VAT Committee and Tribunal are:

- to consider all the tax matters that require professional and technical expertise and make recommendations to the FIRS
- to advise the FIRS on its duties in administering the tax; and
- to attend to such other matters as the FIRS may from time to time refer to it.

### 3.5.2 Appointment of an Agent

The FIRS may, be notice in writing, appoint any person to be the agent of any manufacturer or importer and the person so appointed shall be the agent of the manufacturer or importer. Such agent may be required to pay any tax which is or may become due by him to the manufacturer or importer, as the case may be, and in default of such payment, the tax shall be recoverable from him. The FIRS may require a person to give information as to any money, fund or other assets which may be held by him for or any money due from him to a manufacturer or an importer.

- A vat able person, who fails to submit returns to the FBIR is liable to fine of ₦5,000 for every month in which the failure continues.
- An officer of the FIRS or any other person, who aids and abets the commission of any of the offenses under the VAT act, is guilty of an offence and is liable on conviction to a fine of N50,000 or to imprisonment for a term of five years.
- Where a person's conduct during any specified period has involved the commission or omission by him of any one or more of the foregoing offences, then whether or not the particulars of the offenses are known, he shall be guilty of an offence and liable to pay a fine of ₦10,000 or if greater, four times the amount of any tax that was, or was intended to be evaded by a his conduct, or to imprisonment for a term not exceeding 6 months or to both such fine and imprisonment.
- Where an offence under the VAT act is committed by a body corporate or firm or other association of individuals,

- a. every director, manager, secretary or other similar officer of the body corporate, or
- b. every partner or officer of the firm, or
- c. every person concerned in the management of the affairs of the association, or
- d. every person who was purporting to act in any capacity as aforesaid, is severally guilty of that offence and liable to be proceeded against and punished for the offence in like manner as if he had himself committed the offence, unless he proves that the act or omission constituting the offence took place without his knowledge, consent or connivance.

### 3.6 Definition of Terms

*Agency of government* includes a ministry, department, statutory body, public authority and an institution of the federal, state and local government.

*Authorised officer* means an officer who has been authorised by the service to perform any function under or in pursuance of this act.

*Revenue service*: means the Federal Inland Revenue Service.

*Building*: means any house, including any garage, dwelling apartment, hospital and institutional building, factory, warehouse, theatre, cinema, store, mill building and similar roofed structure affording protection and shelter, radio and television masts, transmission line, tower, vehicle and other similar structure but excludes mobile homes, caravans and trailers.

*Business*: include any trade, commerce or manufacture or any concern in the nature of trade, commerce or manufacture.

*Chairman* means the chairman of the Federal Inland Revenue Service.

*Company*: mean a company as defined under the companies and allied matter act 1990 (as amended), and a corporate body that may be formed under any other written law and includes any association, whether incorporated in or outside Nigeria.

*Entertainment*: includes any exhibition and performance in which admission of person is subject to payment by such persons.



*Import:* means bringing in or carrying to be brought in goods and services from another country or from an export processing zone.

*Importer:* means any person who imports taxable goods.

*Invoice:* means any document issued as an evidence of demand for payment.

*Manufacturer:* means any person who engages in the manufacture of goods and includes a person who has manufactured for him or on his behalf by others, goods made to his specification or design.

*Minister:* means the minister responsible for matters relating to finance.

*Manufacturing:* means the process by which a commodity is finally produced, including assembling, packing, bottling, re-packing, mixing, blending, grinding, cutting, bending, twisting and joining or any other similar activity.

*Motel:* means premises on which accommodation, flats service apartments, beach cottage, holiday cottage, game lodges are provided but excludes the following:

- a. Premises run by a charitable or religious organisation registered under the relevant law for charitable or religious purposes.
- b. Premises operated by a medical institution approved by the secretary for the time being responsible for health for the use of the staff of that institution; and
- c. Premises, whose supply is under a lease or license of not less than one month, unless by prior arrangement, the occupier may without penalty, terminate that lease or license on less than one month's notice.

*Owner:* means in respect of any goods, aircraft, vehicle, plant or any other goods, a person, other than an officer acting officially, who holds out himself to be the owner, manufacturer, agent or the person in possession of or beneficially interested in, or having control of or power of disposition over the goods, aircraft, vessel, vehicle, plant or other goods.

*Registered person:* means any person registered under section 8 of the Act.

*Restaurant:* means any establishment carrying out the business of restaurant services, and includes cafeterias, fast food outlets, snacks bars, food stalls at exhibitions or sport arenas and similar establishment but excludes:

- a. An establishment operated for charitable or religious purposes.
- b. An establishment run by an educational or training institution approved by the Secretary for the use of the staff and students of those institutions, and
- c. Establishments run by a medical institution approved by the secretary for the time-being responsible for the health for the use of the staff and students of the institution.

*Restaurant services:* means the supply of foods or beverages prepared for immediate consumption, whether or not such consumption is on the premises of the restaurant and including outside catering.

*Service:* means the Federal Inland Revenue Service.

*Supplies:* mean any transaction, whether it is the sale of goods or the performance of services for a consideration, i.e., for money or money's worth.

*Supply of goods:* means any transaction where the whole property in the goods is transferred or where the agreement expressly contemplates that this will happen and in particular includes the sale and delivery of taxable goods and services used outside the business, the letting out of taxable goods on hire or leasing, and any disposal of taxable goods.

*Supply of service:* mean any services provided for a consideration.

*VAT:* means value added tax imposed and charged under section 1 of the act.

*Vatable goods and services:* means the goods and services not exempted in the schedule to the act.

*VAT period:* means one calendar month commencing from the beginning of the month to the end of the month.

*Vatable person:* a person who independently carried out in any place, an economic activity as a producer, wholesale trader, supplier of goods, supplier of services including mining and other related activities or a person exploiting tangible or intangible property for the purpose of obtaining income therefrom by way of trade or business; and includes a person and an agency of government acting in that capacity.

*Transaction of arm's length:* means a transaction on normal open market commercial terms.

*Vehicle:* includes for the purpose of the act, every description of conveyance for the transportation by land, of human beings or goods.

*Vessel:* means a mode of transportation or conveyance by water, of human beings or goods.

*Wholesaler:* means a person who obtains his stock predominately from the manufacturers and sells in bulk to the retailer.

### **3.7 Sharing of VAT Proceeds**

The VAT collected by FIRS is shared thus:

- 15 percent to the federal government
- 50 percent to the state government and the Federal Capital Territory, Abuja, and
- 35 percent to the local government.

### **4.0 CONCLUSION**

We noted that Valued Added Tax (VAT) was defined as an indirect tax like excise duty, first levied under the Value Added Tax Act (the Decree) No.102 of 1993 (as amended), with effective date of 1 December, 1993. We also noted from the passage that the VAT act repealed the Sales Tax Act, 1986, and it is now known as Value Added Tax Act, Cap. VI, LFN 2004. Finally, we were told that the tax is charged on the supply of goods and services.

### **5.0 SUMMARY**

In this unit, we defined value added tax, listed the goods and services exempted from value added tax, discussed VAT returns, remittances,

recovery and refund. We also enumerated the functions of VAT committee and tribunal and specified how VAT proceeds are shared between the three tiers of government in Nigeria.

In the next unit, we shall be exploring another interesting topic, capital allowances.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. Define value added tax in your own words.
2. List the goods and services that have been exempted from value added tax.
3. Enumerate the functions of VAT Committee and Tribunal.
4. How is an agent appointed?
5. In what ratio is the proceeds of value added tax divided among the three tiers of government in Nigeria?

## **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## UNIT 3 CAPITAL ALLOWANCES

### CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Capital Allowances
  - 3.2 Treatment of Qualifying Capital Expenditure Acquired Second Hand
  - 3.3 Types of Capital Allowances
  - 3.4 Qualifying Expenditure
  - 3.5 Allowances
  - 3.6 Leasing Assets (Paragraph 18)
  - 3.7 Capital Allowances Rates
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 Reference/Further Reading

### 1.0 INTRODUCTION

In this unit, we defined value added tax; listed the goods and services exempted from value added tax; discussed VAT returns, remittances, recovery and refund; enumerated the functions of VAT committee and tribunal; and specified how VAT proceeds are shared between the three tiers of government in Nigeria.

In the next unit, we shall be exploring another interesting topic, capital allowances.

### 2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define capital allowances
- discuss the treatment of qualifying capital expenditure acquired second hand
- list and explain types of capital allowances
- explain what is meant by qualifying expenditure
- define allowances
- discuss the concept leasing assets
- list the capital allowances rates.

### **3.0 MAIN CONTENT**

#### **3.1 Capital Allowances**

Capital allowance would be claimed on qualifying capital expenditure in use for the purpose of a trade or business. Capital allowance is obtained in replacement for depreciation charge which is treated as an inadmissible expense. For tax purpose, capital allowance is claimed only on the following conditions:

- The qualifying capital expenditures must be owned by the taxpayer making the claim as at the end.
- The taxpayer must be making use of the qualifying capital expenditures for the purpose of its trade or business.
- The qualifying capital expenditures must be “in use” as at the end of the basic period.
- Where the value of the qualifying capital expenditures is not less than N500, 000 (five hundred thousand naira), an acceptance certificate must be obtained from the inspectorate division of the federal ministry of industry. The threshold for the acceptance certificate was just N20, 000 up to the end of 1995-year of assessment.

#### **3.2 Treatment of Qualifying Capital Expenditure Acquired Second Hand**

The treatment to be given to second hand acquisition of qualifying capital expenditures will depend on the class of assets.

##### **a. Buildings**

In respect of buildings acquired second hand:

- No initial allowance will be claimed
- The annual allowance to be claimed must be based on the lower of the original cost of acquisition and the new purchase price.

b. Other assets

There are no clear cut provisions in the tax laws as to the treatment of other assets acquired second hand as the only provision in the law is in respect of buildings. Consequently, where other assets are acquired on second-hand, both initial and annual allowances can be claimed provided they are transaction as arms length. Where the transaction are between two related parties, then:

- No initial allowance can be claimed
- The annual allowance to be claimed must be based only on the unexpired tax life of the asset.

### SELF-ASSESSMENT EXERCISE

- i. .... is claimed on qualifying capital expenditure in use for the purpose of a trade or business.
- ii. Capital allowance is obtained in replacement for ..... which is treated as an inadmissible expense.

### 3.3 Types of Capital Allowance

There are basically four types of capital allowances:

- Initial allowance
- Annual allowance
- Balancing adjustment
- Investment allowance

#### (a) Initial allowance

The allowance is claimed only once in the life of a qualifying capital expenditure. It is a relief granted to a trader or a company whenever a qualifying capital expenditure is incurred. The allowance is granted for the year of assessment in which the asset was first acquired and used.

#### (b) Annual allowance

This allowance is granted every year and it is claimed equally over the estimated tax life of a qualifying capital expenditure.

**(c) Balancing adjustment**

This is divided into two:

Balancing allowance and balancing charge

Balancing allowance: this is obtained when the sales proceeds on disposal of a qualifying capital expenditure exceed the tax written down.

**(d) Investment allowance**

See section 3.5.2 of this unit for explanation.

**SELF-ASSESSMENT EXERCISE**

Capital allowances can be classified into four, namely: ...and .....

**3.4 Qualifying Expenditure**

Qualifying expenditure means capital expenditure incurred in a basis period in connection with:

- Plant, machinery or fixture
- Buildings, structures or works of a permanent nature
- Mines, oil wells or other sources of mineral deposits of a washing nature
- Plantations
- Research and development
- Agricultural plant
- Public transportation motor vehicles and
- Public transportation (inter-city) new mass transit coach.

Any expenditure which is an allowable deduction in computing the profit of the company's trade or business in accordance with the provisions of section 20 of CITA shall not be treated as qualifying expenditure.



## **3.5 Allowances**

### **3.5.1 Initial Allowance**

This is granted in the first year of acquisition on the cost of purchase of the asset whether purchased new or second hand (but see the exception in respect of building as already discussed).

For example, an initial allowance of N25, 000 will be claimed for a qualifying expenditure amounting to N50, 000 on an asset which attracts an initial allowance rate of 50%.

The initial allowance to be granted would be such an amount as the revenue service may determine to be just and reasonable where either the seller has control over the purchaser or the purchaser has control over the seller of the asset. Provided that the aggregate capital allowances granted in respect of any assets shall not exceed 95% of the total cost of the asset. (New section 6(3) inserted in Decree 1966 No.32 effective from 1 January, 1996).

### **3.5.2 Investment Allowance (CITA Section 28)**

In addition to an initial allowance, investment allowance can be claimed in respect of qualifying expenditure incurred on plant and machinery. The rate is 10% of the expenditure. The provisions of CITA relating to initial allowance also apply to investment allowance, except that an investment allowance is not to be deducted from cost of the assets in arriving at the residue of qualifying expenditure.

Investment allowance cannot be claimed, or if already granted, shall be withdrawn if any of the following happened within a period of five years from the date of acquisition of the assets:

- Any sale or transfer of the asset otherwise than to a person acquiring the asset for a chargeable purpose or for scrap.
- Any appropriation of the asset to a purpose other than a chargeable purpose.
- Any sale or transfer or other dealing with the asset being a case where it appears either:
  - a. That the purpose of obtaining tax allowances was the sole or main purpose of the company for incurring the expenditure or for so dealing with the asset, or

- b. That the incurring of the expenditure and the asset being so dealt with, were not bona fide because transactions, or were artificial or fictitious transactions, and were designed for the purpose of obtaining tax allowances.

For the purpose of this section “chargeable purpose” means the purpose of putting the assets to a use such that profits accrue or are intended to accrue there from and will be chargeable to tax.

### 3.5.3 Annual Allowance

This is granted annually and is computed on the balance of cost after the deduction of the amount of initial allowance claim on the asset. In the example of the item shown under initial allowance above, the annual allowance, assuming a rate of 25% shall be N6,250, that is, 25% of N(50,000 – 25, 000). Annual allowance once calculated for particular fixed asset item will be the same amount for each of the years that the assets is in use until the cost of the asset is fully relieved. A nominal sum of N10 per item is retained in the books in the last year of claim of annual allowance. It is retained until the item is disposed of.

Where the basis period for any of assessment is a period of less than one year, the annual allowance for that year of assessment shall be proportionally reduced.

#### Illustration 9-1

New business Nigeria limited commenced a retail trade business on 1 October 2006 and makes up accounts to 30 September of every year. The following qualifying capital expenditure on plant and machinery were incurred.

Date	Amount ₦
1/10/06	520, 000
1/11/06	535, 000
15/4/07	725, 000

#### Required:

Computer capital allowances for the relevant years of assessment.

#### Suggested Solution 9-2

**New Business Nigeria Limited**  
**Computation of capital allowances for the relevant years of assessment**

The annual allowance for the first year of assessment will be as follow:

First year of assessment is 2006 assessment year.

Basis period for capital allowance purposes is the period 1/10/06 to 31/12/06

	₦
Total qualifying expenditure during that period	1,055,000
Less: initial allowance at 50%	<u>527,500</u>
Balance of cost after initial allowance	<u>527,500</u>

Investment allowance is also due, since the item is plant and machinery

	₦
Investment allowance at 10% of N1, 055.00	105,500
Annual allowance:	
For a full year at 25% of ₦527, 500	<u>131,875</u>

But restricted to  $\frac{3}{12} \times \text{₦}131, 875$  in view of number of months in the basis period being less than twelve

Residue of expenditure carried forward to the second year of assessment  
 ₦494, 531.

Whenever in doubt as to whether it is the initial or annual allowance that should be restricted when the basis period is shorter than twelve months, remember that initial allowance is a one-off allowance and is therefore not to be restricted, while annual allowance is on an annual basis and is therefore to be proportionately restricted to the number of months in the basis period, if less than twelve months.

### **3.6 Leasing Assets (Paragraph 18)**

The part of the act that deals with leasing assets is paragraph 18 of the Second Schedule, the substance of which has been reproduced below, it covers the various equipment leasing, including sale and lease back, schemes which are commonly operated by merchant banks and finance houses. With this provision it is the lessor (the owner of the asset under an operating lease) that can claim capital allowances in respect of the cost of the asset. The hire charge payable by the lessee is section 20 deductible, as a trade expense, with regard to a finance lease, it is the hirer or lessee that can claim capital allowances on the qualifying expenditure which is

determined in the same manner as assets acquired under hire-purchase terms.

- a. Where a company owning an asset:
  - has incurred capital expenditure in respect thereof, or
  - leases that assets to any person under an operating lease contract for use wholly, exclusively, necessarily and reasonably for the purpose of a trade or business carried on by such person, the provisions of this schedule shall apply as though such expenditure were incurred for the purpose of a trade or business carried on by the owner or lessor and as though the owner or lessor were using the asset for the purpose of such last-mentioned trade or business in the way in which and for the period or periods during which the asset is in fact in the first mentioned-trade or business.
  
- b. Where, however, an asset is acquired by any hirer or lessee under a finance lease contract, the terms of which provide for the transfer of ownership, risks and rewards to the hirer or lessee, the provisions of this schedule shall apply in the same way as it applies to an asset acquired by any owner or lessor of an asset for the purposes of his trade or business but shall so apply subject to the following modifications, that is to say:
  - The qualifying expenditure within the provisions of this schedule shall, in relation to any asset so acquired under that contract, be limited to the amount of the total lease payments due from the hirer or lessee, during his basis period excluding in the computation of such qualifying expenditure any interest charges payable under the contract.
  - Any reference in this sub-paragraph (2) of this paragraph to any owner or lessor of any asset shall be construed as including a reference to a hirer or lessee under the finance lease contract and as excluding a reference to the person leasing the asset to the hirer or lessee under the contract.
  
- c. Subject to the provisions of this schedule, where a company has incurred capital expenditure on plant and machinery or acquires same by virtue of sub-paragraph (2) of this paragraph, wholly, exclusively, necessarily and reasonably for the purpose of a trade or

business carried on by it, there shall be due to the trade or business an investment of ten per cent of such expenditure.

- d. For the purposes of this schedule, the terms “operating lease” and “finance lease” shall have the meanings ascribed to them by the statement of accounting standards on leases (SAS No.11).

### 3.7 Capital Allowances Rates

The following are the current (2009) capital allowances rates:

<b>Particulars</b>	<b>Initial allowance %</b>	<b>Annual allowance %</b>
Buildings (industrial & non industrial)	15	10
Mining	95	Nil
Plant: Agric Production	95	Nil
Others	50	25
Furniture and fittings	25	20
Motor vehicles: public transportation	95	Nil
Others	50	25
Plantation Equipment	95	Nil
Housing Estate	50	25
Ranching and Plantation	30	50
Research & Development	95	Nil
These rates were effective from the 2006 assessment year		

#### 3.7.1 Claim for Capital Allowances – Options

The following options are available with regard to capital allowance:

- a. Capital allowance must be claimed before it can be granted. This implies that normally it will not be granted when no claim is made by the company. Therefore, a company that does not wish to be granted capital allowances in any particular assessment year can achieve that objective by not making a claim for such, in its tax computations.
- b. Where double taxation relief is applicable, paragraph 23 of the Schedule 2, permits a company to elect that the initial or annual allowance due to it, be calculated at a lesser rate than normally applicable as summarised under capital allowances rate above. When such election is made, the lesser rate desired by the company shall be

the appropriate rate to be used to compute the amount of the capital allowances due to the company for that year of assessment.

### **3.7.2 Basis Period**

The basis period for capital allowances is normally the same as that used in the computation of assessable income. For example, if accounts are made up to 30 September every year, the basis period for the purpose of determining assessable income for 2005 assessment year will be the accounting year ended 30 September 2004 that is period 1 October 2003 to 30 September, 2004.

Capital allowances would be claimed for the 2005 assessment year using the same basis period this:

Initial allowance – on assets purchased during period 1/10/2003 to 30/0/2004

Annual allowance – or residue of expenditure at 30/9/2003 plus the annual allowance amounts calculated on the additions during the year to 30/9/2004. If there are disposals in the year, the residue of such will be eliminated from the residue at 30/9/2003 before the annual allowance is calculated.

This rule will usually be disrupted at commencement and cessation of a business as there will be overlapping and gaps of periods during these occasion.

The provisions of the act are:

- Where two basis periods overlap, the period common to both is treated except for the purpose of annual allowances, as falling to the first basis period only.
- Where two basis periods coincide they shall be treated as overlapping and therefore rule (i) above will be applicable.
- Where there is an interval between the end of the basis period for one year of assessment and the basis period for the next year of assessment, the interval shall be treated as part of the second basis period unless the year of assessment based on the second basis

period is the year of permanent cessation of the trade, when the interval is treated as part of the first basis period.

#### **4.0 CONCLUSION**

This unit covered the second schedule to CITA, which contains the rules of capital allowances as they apply to corporate bodies chargeable to tax under CITA. It was seen that as depreciation of any asset is not an allowable deduction in the computation of adjusted profits of a company, capital allowance is granted instead.

This unit provided all the rules with respect to: classification of qualifying capital expenditure, claim and grant of capital allowances, determination of balancing allowance or balancing charge upon disposal of qualifying assets. The various points to note with respect to capital allowances have also been covered such that proper claim for capital allowances can be filed with the Inland Revenue.

#### **5.0 SUMMARY**

In this unit, we defined capital allowances and discussed the treatment of qualifying capital expenditure acquired second hand. We listed and explained types of capital allowances and explained qualifying expenditure. We also defined allowances and discussed the concept leasing assets. Finally, we listed the capital allowances rates.

In the next unit, we shall examine capital gains tax.

#### **6.0 TUTOR-MARKED ASSIGNMENT**

1. What do you mean by the term capital allowances?
2. List and explain the types of capital allowances you know.
3. What are allowances? List the types of allowances that you know.
4. Define and discuss the concept leasing assets.
5. How do you treat qualifying capital expenditure acquired second hand?

#### **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 4 CAPITAL GAIN TAX**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Capital Gains Tax
  - 3.2 Chargeable Assets
  - 3.3 Allowable and Disallowable Expenditures
  - 3.4 Exemptions from Capital Gains Tax
  - 3.5 Allowances
  - 3.6 Leasing Assets (Paragraph 18)
  - 3.7 Capital Allowances Rates
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In this unit, we shall examine capital gains tax.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- discuss how capital gains act is administered
- explain the nature and objectives of capital gains tax
- list the principles of allowable and disallowable expenditure as applicable to capital gain tax
- state and explain the reliefs available in capital gains tax
- prepare capital gains tax computations in accordance with the provisions of the capital gain tax act, CAP C1 LFN 2004.

### **3.0 MAIN CONTENT**

The Capital Gain Tax Act in 1967 came into effect from the 1967/68 assessment year. In addition to the necessity to charge capital gains to tax, the act could also have been introduced to produce an additional source of revenue to government to finance Nigeria's civil war.



The principal act together with all amendment thereto has been re-enacted as Capital Gains Tax Act CAP C1 of the Laws of the Federation of Nigeria (LFN)

### 3.1 Capital Gains Tax

Under the provisions of the Capital Gains Tax Act, tax liability will arise on actual year basis when a chargeable asset is disposed. The rate of tax is 10%. Capital gains will arise where the sales proceed on the disposal of the chargeable asset is more than the cost of acquisition.

FORMAT	₦	
Sales Proceed		XX
Less: Allowable expenses	<u>(XX)</u>	
Net Sale Proceed	XX	
Deduct: Cost of Acquisition		<u>(XX)</u>
Capital Gains		<u>XX</u>
Capital Gains Tax at 10%	<u>y.y</u>	

#### 3.1.1 Steps to Compute Capital Gains Tax

Step 1: Identify the sales proceed on the disposal of the chargeable asset.

Step 2: Deduct allowable expenses from the sales proceed to obtain the net sales proceed.

Step 3: The cost of acquisition and other capital costs are then deducted from the net sales proceed to obtain the capital gains.

Step 4: Compute the capital gains tax liability by applying the capital gains tax rate of 10% on the capital gains obtained in step 3.

#### SELF-ASSESSMENT EXERCISE

There are ..... steps to compute capital gains tax.

### 3.2 Chargeable Assets

Chargeable assets are assets whose disposal will result in a chargeable gain. Examples of chargeable asset include:

- options, debts and incorporeal properties

- currencies other than the Nigerian naira
- all qualifying capital expenditures.

### **3.3 Allowable and Disallowable Expenditure**

This topic is discussed under the following sub-topics.

#### **3.3.1 Deductions Allowable (Section 14)**

- Cost of acquisition or purchase price, including all costs incidental to the purchase.
- Improvement costs wholly, exclusively and necessarily incurred.
- Cost wholly, exclusively and necessarily incurred in establishing, preserving or defending the owner's title to or a right over the asset.
- Incidental costs of disposal.

These include:

- (a) Fees, commissions or remuneration paid for professional services of surveyor or valuers; auctioneer, accountant; agent and or legal adviser
- (b) Cost of transfer or conveyance (including stamp duties)
- (c) Advertisement cost to find a seller/buyer; and
- (d) Cost reasonably incurred to make any valuation or apportionment required for the purpose of computing the capital gains including expenses in ascertaining market value where required.

#### **3.3.2 Disallowable Expenditure**

Sums allowable as a deduction in computing the profits or gains or losses of a trade for income tax purposes are not allowable deduction under Section 14 above (Section 15).

#### **SELF-ASSESSMENT EXERCISE**

..... is referred to as the sums allowable as a deduction in computing the profits or gains or losses of a trade for income tax purposes.

### 3.4 Exemptions from Capital Gain Tax

The following capital gains are exempted from tax:

- (a) any capital gain arising from the disposal of any government security
- (b) any capital gains arising from the disposal of shares and securities
- (c) any capital gain from the disposal of a medal won for honour and gallantry
- (d) any capital gain on the disposal of life assurance policies and any investment under a super-annuation fund scheme
- (e) any capital gain on the disposal of motor vehicle for private use
- (f) any capital gain on a chattel disposed off for not more than ₦1,000 in any year of assessment
- (g) any capital gain on the disposal of a landed property by a forced acquisition by any government in Nigeria provided:
  - (i) the taxpayer has not taken any previous step to dispose the asset by way of entering into negotiation to sell;
  - (ii) the taxpayer has not shown any previous intention to dispose off the asset e.g. by way of advertisement;
- (h) any capital gain that accrues to any local authority;
- (i) any capital gain accruing to a purchasing authority under any law in Nigeria to acquire any commodity for the purpose of export or to any corporation established for the purpose of fostering.

### 4.0 CONCLUSION

We note from the discussion in the unit that Capital Gain Tax Act in 1967 came into effect from the 1967/68 assessment year. In addition to the necessity to charge capital gains to tax, the act could also have been introduced to product an additional source of revenue to government to finance Nigeria's Civil war. It was also noted that under the provisions of the Capital Gains Tax Act, tax liability will arise on actual year basis when a chargeable asset is disposed. The rate of tax is 10%. Capital gains will arise where the sales proceed on the disposal of the chargeable asset is more than the cost of acquisition. We listed the steps used in computing capital gains tax and discussed chargeable assets while led to differentiation between allowable and disallowable expenditures. We finally enumerated the exemptions to capital gains tax.

## **5.0 SUMMARY**

In this unit, we have discussed how Capital Gains Act is administered and explained the nature and objectives of capital gains tax. We listed the principles of allowable and disallowable expenditure as applicable to capital gain tax, stated and explained the reliefs available in capital gains tax; and treated how to prepare capital gains tax computations in accordance with the provisions of the Capital Gain Tax Act, CAP C1 LFN 2004.

In the next unit, we shall discuss tax effects on privatisation and commercialisation.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. What is capital gains tax?
2. How is capital gains tax administered?
3. Enumerate the principles guiding allowance and disallowable expenditure.
4. Explain how the reliefs available in capital gains tax are treated.

## **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 5 TAX EFFECTS OF PRIVATISATION AND COMMERCIALISATION**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Rationale behind Privatisation and Commercialisation
  - 3.2 Types of Privatisation and Commercialisation
  - 3.3 Phases of Privatisation and Commercialisation in Nigeria
  - 3.4 Parties to Privatisation and Commercialisation Exercise
  - 3.5 Tax Implications in Privatisation and Commercialisation
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we discussed how capital gains act is administered; explained the nature and objectives of capital gains tax; listed the principles of allowable and disallowable expenditure as applicable to capital gain tax; stated and explained the reliefs available in capital gains tax; and treated how to prepare capital gains tax computations in accordance with the provisions of the Capital Gain Tax Act, CAP C1 LFN 2004.

In this unit, we shall discuss tax effects on privatisation and commercialisation.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- explain the rationale behind privatisation and commercialisation
- list the types of privatisation and commercialisation
- enumerate the phases of privatisation and commercialisation in Nigeria
- state and explain the role of the parties to privatisation and commercialisation exercise
- discuss the tax implications in privatisation and commercialisation of an establishment.

### **3.0 MAIN CONTENT**

In the 1960s, 1970s and 1980s, it was fashionable and considered sound economic policy for governments at different tiers in Nigeria, to establish and invest in statutory corporations and state-owned companies. This was the era when socialist, community and welfarist ideologists held sway. Pride and nationalism were promoted at the expense of competitive economic management of national resources. Governments at different levels were thus involved in the acquisition, nationalisation and/or establishment of enterprises covering a broad spectrum of economic activities ranging from banking, insurance, broadcasting, tourism, transportation, steel and petro-chemicals. However, the fall in oil revenues in the past two decades has made it rather difficult for the government to sustain the required funding of these organisations. Many of the organisations experienced stunted developments and were plagued by inefficiencies.

#### **3.1 Rationale behind Privatisation and Commercialisation (P & C)**

The inability of state-owned enterprises and organisations to deliver their mandates made it imperative that necessary reforms should be carried out. Some of the reasons for embarking on P & C were to:

- free government from unproductive financial subventions
- address problems of excessive bureaucratic control and intervention
- integrate the Nigerian economy into the mainstream of world economic order where private and competitive enterprise were taken over from state monopolies
- tackle problems of management ineptitude and gross incompetence
- eliminate operational complacency and crippling corruptions
- redress problems of inappropriate, and sometimes, obsolete technology
- attract foreign direct investment
- generate revenue for government; and
- create more employment opportunities in the long run due to the envisaged multiplier effect of the gains of privations and commercialisation.

### 3.2 Types of Privatisation and Commercialisation (P & C)

Privatisation can be defined as the sale, transfer or removal of ownership and control from public to private entities in respect of state enterprises. Commercialisation involves the adoption of commercial, competitive and profit objectives in the management of public enterprise. It involves the jettisoning of socialist and monopolistic objectives that characterised the operation of public enterprises in the past. Generally, the memorandum and articles of association or enabling legislations setting up these enterprises are either amended or abrogated in order to reflect a new orientation. The changes to the enabling laws are however dependent on the magnitude of changes being effected. P & C are carried out in several variants, amongst which are:

- total or 100% privatisation/commercialisation
- partial privatization
- partial commercialisation
- management contracts (a variant of commercialisation whereby ownership of the affected enterprises is retained by the state while the management is outsourced to an outside and independent entity for purposes of better management)
- general and open privatisation with no restriction to the number of participating buyers
- core investor –based privatisation which requires that a core investor with proven financial, managerial and technical competence is selected to acquire and manage the enterprise.

### 3.3 Phases of Privatisation and Commercialisation in Nigeria

The P & C exercise in Nigeria was scheduled under three phases as follows:

Phase 1: This involved enterprises engaged in commercial and merchant banking, cement plants, petroleum marketing and others already quoted on the Nigerian Stock Exchange. This phase was to be completed by December 1999.

Phase 2: Enterprises of hotels, tourism and motor assembly.

Phase 3: They include the utilities: NEPA, NITEL, and other companies such as Nigerian Airways, NAFCON, ALUMSCO, Petrochemical and Petroleum Refineries.

It is only the first phase that has been successfully completed.

### **3.4 Parties to Privatisation and Commercialisation Exercise**

The following organisations and groups have been identified as parties:

- The national council on privatisation (NCP).
- The bureau of public enterprise (BPE).
- Technical and financial advisers.
- (These are world class investment bankers, legal and other consulting firms to be engaged in undertaking strategic review, restructuring and sale preparation for affected enterprises).
- Floatation advisers.

The important professional advisers in this group include:

- a. Issuing houses
- b. Solicitors to the issues
- c. Reporting accountants and auditors
- d. Stockbrokers to the issues
- e. Asset valuers.

It should be noted that these professionals may either be from within the country or from abroad.

### **3.5 Tax Implication**

In order to discuss the tax implication of Nigeria's privatisation and commercialisation, the applicable provisions in the tax legislation would be considered. What would apply depends on the state of the establishments and the percentage ownership of government before the privatisation or commercialisation.

#### **3.5.1 Government's Partial Ownership**

Where the establishment has been registered as a limited liability company, it would be subject to tax under CITA or under any other relevant act. An example is national oil marketing company plc. This company has been subject to tax under CITA before the privatisation. At privatisation, all that has been done is that government has sold its shareholding in the company. This would not have an effect on the tax status of the company after the



privatisation. This will be the case whether or not government had controlling shares in the establishment.

### **3.5.2 Government's Full Ownership**

Going through section 19 of the companies income tax act, CAP C21 LFN 2004 (as amended), the exemptions relating to government establishment are:

Profits or incomes are exempted from tax, in so far as they are not derived from trade or business being carried on:

The profits of any company or corporation established by the law of a state for the purpose of fostering the economic development of that state.

The privatised company will be liable to pay tax under the provisions of the relevant tax act and it will be easier for the revenue service to enforce as appropriate. With regards to those that have been paying the appropriate tax, privatisation will not have any further tax effect other than they would continue to pay company tax under the appropriate tax act.

Commercialisation would not have any particular implication, since as already indicated; all trading government establishments are liable to pay tax. This would indeed be more pronounced when they are commercialised.

Profits of government establishments that are exempted, even if they are derived from trade or business, relate to local government. Section 19(1) states:

The profits of any company, being a body corporate established by or under any local government or under any local government law or edict in force in any state in Nigeria.

There were no federal government establishments exempted in Section 19 of the act. Thus, all federal government trading establishments were liable to companies even before the privatisation exercise. If they have not been paying tax before, that implies that they have been contravening the nation's laws.

## **SELF-ASSESSMENT EXERCISE**

- i. NCP is the acronym for .....
- ii. BPE is the acronym for .....
- iii. Commercialisation is referred to as .....
- iv. Privatisation is defined as .....

## **4.0 CONCLUSION**

This chapter discusses the tax implications of both the privatisation and commercialisation exercise, depending on the level of divestment of government in the affected establishments. It also explains the types of privatisation and commercialisation and their phases in Nigeria.

## **5.0 SUMMARY**

In this unit, we have explained the rationale behind privatisation and commercialisation. We listed the types of privatisation and commercialisation and enumerated the phases of privatisation and commercialisation in Nigeria. We also stated and explained the role of the parties to privatisation and commercialisation exercise and discussed the tax implications in privatisation and commercialisation of an establishment.

In the next unit, we shall be exploring another topic titled: profits, assessable profits and tax payable.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. What are the rationale behind privatisation and commercialisation of the government businesses?
2. List and discuss the types of privatisation and commercialisation embarked upon by the Federal government of Nigeria.
3. Enumerate the phases involved in the federal government's privatisation and commercialisation programme.
4. What are the parties in Nigeria's privatisation and commercialisation programme and what are their roles?
5. What are the tax implications of privatising and commercialising business enterprises?

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 6 PROFITS, ASSESSABLE PROFITS AND TAX PAYABLE**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Imposition of Tax on Profits
  - 3.2 Authorised Unit Trust Scheme
  - 3.3 Donations
  - 3.4 New Trade or Business
  - 3.5 Changing of Accounting Dates
  - 3.6 Company in Partnership with Another
  - 3.7 Small Business Rate
  - 3.8 Pre-Operation Levy
  - 3.9 Advance Income Tax Payment
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 Reference/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we extensively discussed privatisation and commercialisation and the tax implications in privatisation and commercialisation of an establishment.

In this unit, we shall be exploring another topic titled: profits, assessable profits and tax payable.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- enumerate areas where government can impose tax on profits of companies
- define and explain how tax can be imposed on an authorised unit trust scheme
- specify the bodies to which donations can be made from the profits of companies
- explain how tax can be imposed on a new trade or business

- state the relevance of changing accounting dates in line with government's financial year
- assess the tax on the profits of a company in partnership with another
- determine the tax rate imposed on small businesses and the pre-operation levy
- list the conditions governing payment of advance income tax by companies.

### **3.0 MAIN CONTENT**

Companies income tax is chargeable on the income of all companies operating in the country except those specifically exempted under the act. There is a clear distinction between Nigerian and non-Nigerian companies. A Nigerian company is defined as one incorporated under the Companies and Allied Matters Act, 1990, as amended. The total profits of such companies are assessable to Nigeria tax irrespective of whether or not all the profits have been derived from, brought into or received in Nigeria.

A foreign company (non-Nigerian company) is defined as any company or corporation establishment by or under any law in force in any territory or country outside Nigeria, that is, a company that is not incorporated under the companies and allied matters act.

The profits of a non-Nigerian company shall be subject to Nigerian tax only to the extent to which such profits are attributable to the company's operations in Nigeria, subject to provisions in the respective double taxation agreements, if any, available within the country where the foreign company is registered. Withholding tax of 10% is deductible from dividend, interests or royalties due to non-Nigerian companies arising in Nigeria.

In short, Companies income tax is chargeable on:

- a. The global profits of Nigerian companies irrespective of whether or not they are brought into or received in Nigeria. Dividend income to a Nigerian company is treated as Franked investment income on which no income tax is due.
- b. The portion of the profits of non-Nigerian companies derived from such companies' operations in Nigeria

- c. Dividends, interest or royalties due to non-Nigerian companies, which are assessed at 10% (withholding tax rate) on the gross amount due and only the net is payable to the respective companies.

### **3.1 Imposition of Tax on Profits**

Section 8 of Companies Income Tax Act (CITA) imposes tax at a particular rate (currently 30%) upon the profits of any company accruing in, derived from, brought into, or received in Nigeria in respect of:

- a. Any trade or business
- b. Rent or any premium arising from a right granted to any other person for the use or occupation of any property. The treatment of rental income for companies' income tax purposes is the same as that for personal income tax.
- c. Dividends, interest, royalties, discounts, charges or annuities,
- d. Any sources of annual profits or gains not falling within the preceding categories
- e. Any amount deemed to be income or profit under a provision of the act, or with respect to any benefit arising from a pension or provident fund, of the personal income tax decree.
- f. Fee, dues and allowances (wherever paid) for services rendered. Any company entering into any agreement (whether oral or written) in respect of any service in this regards is required by the act to make full disclosure in writing to the revenue service of the terms of such agreement (Section 10), and
- g. Any amount of profits or gains arising from acquisition and disposal of short-term money instruments like federal government securities, treasury bills, treasury or savings certificates, debenture certificates or treasury bonds.

#### **3.1.1 Identification of a Company**

The incorporation number of a company and the Personal Identification Number (generated by FIRS), to which the provisions of Section 8 apply, shall serve as the identification number of the company and shall be displayed by the company on all business transactions with other companies and individuals and on every document, statement, returns, audited account and correspondence with revenue authorities, including the Department of Customs and Excise, ministries and all government agencies (section 8a), where profits are accrued (CITA Section 11).

The profits of a Nigerian company shall be deemed to accrue in Nigeria wherever they have arisen and irrespective of their being brought into or received in Nigeria.

The profits of a company, other than a Nigerian company from any trade or business shall be deemed to be derived from Nigeria:

- a. If that company has a fixed base of business in Nigeria, to the extent that the profit is attributable to the fixed base.
- b. If it does not have such a fixed base in Nigeria but habitually operates a trade or business through a person in Nigeria authorised to conclude contracts on its behalf or on behalf of some other companies controlled by it or which have controlling interest in it, or habitually maintains a stock of goods or merchandise in Nigeria from which deliveries are regularly made by a person on behalf of the company, to the extent that the profits are attributable to the business or trade or activities carried on through that person.
- c. If that trade or business or activity, involves a single contract for surveys, deliveries, installation or construction, the profit from that contract, and
- d. Where the trade or business or activity is between the company and another person controlled by it or which has controlling interest in it and conditions are made or imposed between the company and such person in their commercial or financial relations, which, in the opinion of the Revenue Service, is deemed to be artificial or fictitious, so much of the profits adjusted by the Revenue Service to reflect arm's length transaction (Subsection 2).

For the purposes of subsection (2) (a) of this section, a fixed base shall not include:

- a. Facilities used solely for storage or display of goods or merchandise;  
and
- b. Facilities used solely for the collection of information.

## **SELF-ASSESSMENT EXERCISE**

The ..... of a company and the ..... (generated by FIRS), to which the provisions of Section 8 apply, shall serve as the identification number of the company.

### **3.1.2 Trade or Business**

Companies are normally formed to carry out particular activities which will be specified in the object clause of their respective memoranda of association. Therefore, in determining what constitutes a trade or business of a company, it is necessary to refer to the objects clause of its memorandum of association, to ascertain the activities that the company was registered to carry out. The carrying on of such activities will definitely constitute trade or business and the income therefrom will be subject to companies' taxation in accordance with the provision of the act.

Thus, a trade or business will include manufacturing and any other activities being carried on in pursuance of the goal for which the company was incorporated. Furthermore, in view of the fact that a company will pursue all possible activities to keep it in business, it is only reasonable to conclude that the income from all such activities constitute chargeable transactions and will therefore be taxed except if they relate to capital items or are specifically exempted by other provisions of the act. Neither the absence of a profit-making motive in particular transactions nor the fact that they are isolated and do not relate to the company's normal business could prevent the income from such transactions from being subjected to companies taxation.

## **SELF-ASSESSMENT EXERCISE**

In determining what constitutes a trade or business of a company, it is necessary to refer to the ..... of its memorandum of association.

### **3.1.3 Dividends**

Tax is imposed on dividend income in Section 8 of CITA. The definition of dividend as given in subsection 3 of section 8 of the act is as follows:

- a. In relation to a company not being in the process of being wound up or liquidated, any profits distributed, whether such profits are of a capital nature or not, including an amount equal to the nominal value

of bonus shares, debentures or securities awarded to the shareholders, and

- b. In relation to a company that is being wound up or liquidated, any profits distributed, whether in money or money's worth or otherwise, other than those of a capital nature earned before or during the winding up or liquidation.

As in the taxation of individuals, the amount to be taken as the income of a company is the gross amount of the dividend and is deemed to arise on the day on which its payment becomes due. The provisions of Section 15 CITA exempt certain dividends from tax. These are dividends:

- a. By a Nigerian company and satisfied by the issue of shares of the company paying the dividend (bonus shares), or
- b. By a Nigerian company, out of any profits exempted from tax by any provisions of the act or by the fact that the company enjoys a pioneer status, or
- c. Out of any profits chargeable to tax under the provisions of the petroleum profits tax act.

Part of the 1985 amendment to the act is to the effect that dividends received from a Nigerian company are to be regarded as Franked Investment Income (FII). The 1987 amendment also exempts from tax, dividend derived by a company from another company incorporated in Nigeria provided that the equity participation on which the dividend is payable is:

- a. Either wholly paid for in foreign currency or by asset brought into or imported into Nigeria.
- b. Brought or imported into Nigeria between 1 January, 1987 and 31 December, 1992.
- c. Not less than 10% of the equity share capital of the company paying the dividend.

For the purpose of this exemption, the tax free period starting from the year following that in which the new capital is brought into Nigeria shall be five years if the company is in the agricultural trade or business, or is engaged in the petrochemicals or liquefied natural gas business. It shall be three years in any other case.



The amount of the withholding tax deducted in connection with any dividend due to a non-resident recipient shall be the final tax on those payments, that is, no further tax is payable by non-resident recipients of any dividends income (section 16(a)).

### **Illustration 12-1**

A company with total profits of ₦10, 000 for an assessment year pays N50, 000 dividends to its shareholders in respect of the account which form the basis for the assessment. The company will pay tax of N15, 000 (30% of N50, 00 assuming its turnover is more than N500, 000) and not N3, 000 (30% of N10, 000) which would have been payable if the company did not declare the dividend.

## **3.2 Authorised Unit Trust Scheme**

The provisions relating to the Unit Trust Schemes are contained in Section 14A. The provision of CITA shall, in respect of the income arising to the trustees of an authorised unit trust, have effect as if:

- a. The trustees were an investment company
- b. The rights of the unit holders were shares in the company; and
- c. Any income accruing to the trustees available to be paid to the unit holders were dividends on such shares.

The profits of an authorised unit trust scheme, on which tax may be imposed shall be the income accruing to the trustees from all sources of the investment of the unity trust and deducing there from sums disbursed as management expenses, including remuneration for the managers. The treatment of tax deducted at source is the same as is applicable to any other company taxable under CITA.

In this section:

Authorised unit trust – is defined as a unit trust scheme that is authorised by the commission under Section 576 of the Companies and Allied Matters Act 1990 as amended to carry on the business of dealing in unit rust scheme.

Unit trust scheme – defined as any arrangement made for the purpose of providing facilities for the participation of the public as beneficiaries under

a trust in profits or income arising from the acquisition, holding, management or disposal of securities or any other property whatsoever.

Unit holder – is defined as any investor, beneficiary or person who acquired units in a unit trust scheme and who is entitled to share of the investments subject to the trust scheme.

A trustee – is defined as the person in whom the property for the time being subject to any trust created in pursuance of the scheme is or may be invested (vested) in accordance with terms of the trust.

### **3.2.1 Exemptions**

Section 19 of CITA contains the list of profits or gains of companies or corporate bodies exempted from company taxation.

- a. Profits or incomes exempted in so far as they are not derived from trade or business being carried on:
  - The profits of any company being a statutory or registered friendly society
  - The profits of any company engaged in ecclesiastical, charitable or educational activities of a public character
  - The profits of any company being a trade union, registered under the Trade Unions Act
  - The profits of any company or corporation established by the law of a state for the purpose of fostering the economic development of that state
  - The profits of any company being a cooperative society, registered under any enactment or law relating to cooperative societies not being profits from any trade or business carried on by that company other than cooperative activities solely carried out with its members or from any share or other interest possessed by that company in a trade or business in Nigeria carried on by some other person or authority; if any income in respect of the foregoing is derived from a trade or business, it is clear from the wordings of Section 19 that such shall become taxable.

- b. The following are also exempted from tax even if they are derived from trade or business being carried on by the bodies concerned.
- i. The profits of any company formed for the purposes of promoting sporting activities where such profits are wholly expendable for such purpose, subject to such conditions as the revenue service may prescribe.
  - ii. Dividend distributed by a unit trust.
  - iii. Dividend derived by a company from another company incorporated in Nigeria, provided that:
    - The equity participation of the recipient of the dividend in the company paying the dividend is either wholly paid for in foreign currency or by assets brought or imported into Nigeria between 1 January, 1987 and 31 December, 1992 and
    - The company receiving the dividends is the beneficial owner of not less than 10% of the equity share capital of the company paying the dividend.

The dividend tax-free period shall commence from the year of assessment following the year in which the new capital is brought into Nigeria for the purpose of the trade or business in Nigeria of the company paying the dividend. If the company paying the dividend is in the agricultural trade or business, or is engaged in the petrochemicals or liquefied natural gas, the tax-free period shall be five years, while in the any other case it is limited to three years.

- i. The profits of any company engaged in petroleum operations within the meaning of Section 2 of the petroleum profits tax act in so far as those profits are derived from such operations and liable to tax under that act. It should be noted that if any part of the profits of such company arises from other operations besides petroleum operations, development and production besides petroleum exploration, development and production and can therefore not be taxed under the petroleum profits tax act, such part is taxable under the companies income tax act.

- ii. The profits of any company being a body corporate established by or under any local government law or edict in force in any state in Nigeria.
- iii. The profits of anybody corporate being a purchasing authority establishment by an enactment and empowered to acquire any commodity, for export from Nigeria as well as from the purchase and sale of that commodity.
- iv. The profits of non-Nigerian companies which but for this paragraph, would be chargeable to tax by reason solely at their being brought into or received in Nigeria.
- v. Dividend, interest, rent or royalty derived by a company from a country outside Nigeria and brought into Nigeria through government approved channels. Government approved channels means the central bank of Nigeria, any bank or other corporate body appointed by the minister as authorised dealer under the second-tier foreign exchange market act or any enactment replacing that act.
- vi. The interest on deposit accounts of a foreign non-resident company, provide that the deposits into the account are transfers wholly of foreign currencies to Nigeria on or after 1 January, 1990, through government approved channels.
- vii. The interest on foreign currency domiciliary account in Nigeria accruing on or after 1 January, 1990.
- viii. Dividend received from small companies in the manufacturing sector, in the first five years of their operation. Small companies are companies, with turnover of N1, 000,000 and below, in an assessment year.
- ix. Dividend received from investments in wholly export-oriented businesses.
- x. The profits of any Nigerian company in respect of goods exported from Nigeria provided that the proceeds from such export are repatriated to Nigeria and are used exclusively for the purchase of raw materials, plants, equipment and spare parts.

- xi. The profits of a company whose supplies are exclusively inputs to the manufacturing of products for export, provided that the exporter shall give a certificate of purchase of the inputs of the exportable goods to the seller of the supplies.

In respect of all the foregoing, appropriate withholding taxes are deductible in accordance with the provisions of section 60, 61, 62 of CITA in spite of the fact of the exemptions of the gains or profits from income tax.

The national council of ministers (federal executive council) may exempt by order:

- a. Any company or class of companies from all or any of the provision of the act; or
- b. All or any profits of any company or class of companies from any source, on any ground which appears to it sufficient.

The national council of ministers may by order amend, add to or repeal any exemption, in so far as it affects a company.

The following notices and order shall continue in force for all purposes of the act:

- a. The Income Exemption (Interests On Nigerian Public Loans), Notice;
- b. The Income Tax Exemption (Nigerian Broadcasting Corporation) order;
- c. The Railway Loan (International Bank) (Exemption of Interest) Notice.

### **3.2.2 Interest on Loans – Agricultural Trade and Others**

Interest payable on any loan granted by a bank on or after 1 January, 1991 for the purposes of an agricultural trade or business shall be exempted from tax, provided that the moratorium is not less than 18 months and the rate of interest on the loan is not more than the base lending rate at the time the loan was obtained (Section 9(7)).

With effect from January 1 1991, the requirements are:

- a. The moratorium is not be less than 18 months and
- b. The rate of interest on the loan is not to be more than the base lending rate at the time the load was obtained.

Base lending rate means the weighted average of the cost of fund to any bank.

Agricultural trade or business is defined in the act as any trade or business connected with:

- a. The establishment or management of plantations for the production of rubber, oil palm, coffee, tea and similar crops
- b. The cultivation or production of cereal crops, tubers, fruits of all kinds, cotton, beans, groundnuts, sheanuts, beniseed, vegetables, pineapples, bananas and plantains.
- c. Animal husbandry, that is to say, poultry, piggery, cattle-rearing, fish farming, and deep sea fish-trawling.

### **Decree 18 of 1998**

Subsection 7 of section 9 of the act has been replaced with a new subsection 7 in Decree 18 of 1998. The new subsection 7 states that: Interest on any loan granted by a bank on or after 1 January 1997 to a company:

- a. Engaged in
  - Agricultural trade or business, or
  - The fabrication of any local plant and machinery, or
- b. As working capital for any cottage industry established by the company under the family economic advancement programme (FEAP), shall be exempted from tax, provided.
  - The moratorium is not less than eighteen months, and
  - The rate of interest on the loan is not more than the base lending rate at the time the loan was granted.

Thus, the provisions relating to the loans granted to agricultural trade or business on or after 1 January 1991 are, with effect from 1 January 1997,

extended to the trade or fabrication of local plant and machinery as well as family economic advancement programme (FEAP) cottage industry.

### 3.2.3 Interest on Loan for Export Business

Interest accruing from loans granted by banks in aid of export activities is exempted from tax in accordance with the Table in Schedule 3 to the act. The Table, which is the table of tax exemption on interest on foreign and other loans, is reproduced below:

**Table 6.1: Tax Exemption on Interest on Foreign and other Loans**

Repayment period including moratorium	Grace period	% Tax exemption allowed
(i) Above 7 years	Not less than 2 years	100%
(ii) 5-7 years	Not less than 18 months	70%
(iii) 204 years	Not less than 12 months	40%
(iv) Below 2 years	Nil	Nil

The exemption is subject to the presentation of a certificate issued by the Nigerian export promotion council stating that not less than 50% of a company's manufactured goods sold in the relevant accounting year were sold outside Nigeria and were not re-exported into Nigeria.

### 3.2.4 Determination of Profits

For tax purposes, use is made of the account produced under the ordinary rules of accountancy, as it will be extremely difficult, if not impossible to prepare new sets of accounting for the purpose only. Besides the difficulties anticipated, there appears to be no justification for the unnecessary duplication of the efforts that would be required in the production of such accounts. It has been established in some decided cases, that in ascertaining the true profits of a trade for tax purposes, regard should be had to be correct principles of accountancy. Thus, in practice, adjustments that are considered necessary in view of the provisions of the tax acts are made to accounting profits, to arrive at the profits for tax purposes. Such adjustments are usually in respect of:

- a. Expenditure charged but not allowable- disallowance expenditure
- b. Items chargeable to tax but not credited in the profit and loss account

- c. Items credited in the profit and loss account but not taxable; and
- d. Expenditure not charged but allowable.

There are adequate provisions in the act which when considered in the light of normal taxation practice, can be applied to determine which items of a company's trading transactions will fall into any of the four categories listed above and for which adjustments will be necessary. The main guiding principles is that of allowable and disallowance expenditure.

### **3.2.5 Allowance Deductions**

All expenses of a company that are wholly, exclusively, necessarily, and reasonably incurred in the production of the profits, are allowable deductions. Thus, any expense that can be proved to meet these conditions will be an allowable deduction in arriving at a company's chargeable profits unless such expenses is specifically prohibited under any other provision of the act.

In addition, the following items are stated in Section 20 of the act, as allowable deductions provided they are incurred for the purpose of acquiring the profits being subjected to tax:

- a. Interest on money borrowed and employed as capital
- b. Rent and premiums in respect of land or buildings occupied for the purpose of acquiring the profits
- c. Repairs and renewal costs relating to the premises, plant, fixtures, etc, used in the business.
- d. Bad and doubtful debts to the extent that they are respectively estimated to the satisfaction of the revenue service to have become bad or doubtful of collection
- e. Contributions to approved pension, provident or other retirement benefits fund, society or science,
- f. In the case of the Nigerian Railway Corporation, such deduction as are allowed under the provisions of the authorised deductions (Nigerian Railway Corporation) Rules, 1959:
- g. Any outlay or expenses incurred during the year in respect of
  - Salaries, wages or other remuneration paid to employees
  - Cost to the company of any benefit or allowance provided for the senior staff and executives which shall not exceed the limit of the amount prescribed by the collective agreement between the company and the employees and approve by the



Federal Ministry of Employment, Labour and Productivity and the Productivity, Prices and Income Revenue Service as the case may be, and

- The expenses proved to the satisfaction of the Revenue Service to have been incurred by the company on research and development for the period including the amount of levy paid by it to the National Science and Technology Fund.
- h. Section 22 allows for the deduction of the amount of reserve made out of profits for research and development subject to a ceiling of 10% of the total profits of the company before any deduction is made under this section and section 21 of the act.
- i. Companies and other organisations engaged in research and development activities for commercialisation shall be allowed 20% investment tax credit on their qualifying expenditure for that purpose.

### **3.2.6 Rental Charges**

Rental charges in respect of residential accommodation occupied by employees of the company are allowed up to a maximum of 100% of the basic salary of employees.

### **3.2.7 Property Holding Companies**

The allowable deductions are limited to:

- a. Expenses attributable to the maintenance of the property concerned and
- b. Directors' remuneration of up to N10, 000 per annum per director payable to a maximum of three directors in any one company.

### **3.2.8 Repairs and Renewals**

The usual items under this heading are those expenses incurred in maintaining the earnings capacity of the assets of the company intact. In view of the fact that the keeping of such assets in good working condition is very essential for the company to acquire profits, cost connected with such exercise must, by reasonable expectation, be allowable deductions.

However, costs incurred in increasing the earning capacity of any fixed assets are capital in nature and therefore will not be allowable deductions.

Repairs expenditure on newly acquired fixed assets might not qualify as an allowable deduction particularly if large amount is involved and the expenditure is incurred to bring the asset into a usable condition after its acquisition. Such cost is to be considered as capital and should be added to the cost of acquisition of the asset. It is important to note that repair costs are incurred for the purpose of maintaining the earning capacity of the asset and this implies that such asset must be in use in the business at the time that the repair work is carried out.

### 3.2.9 Bad and Doubtful Debts

The salient matters to note with regard to the treatment of bad and doubtful debts for tax purposes are as follows:

- i. They must relate to debts incurred in the ordinary course of the trade or business
- ii. They must be identifiable to specific debts. General reserves against bad and doubtful debts are not allowable deductions
- iii. Reserves no longer required are taxable (in the year that they are considered no longer necessary) if previously allowed
- iv. Debts previously written off, allowed in tax computation, and later recovered are taxable as income for the year in which recoveries are made
- v. Necessary evidence must be provided at the request of the revenue service to prove that the debts have become bad or estimated to be doubtful of recovery.

### SELF-ASSESSMENT EXERCISE

Repairs and renewals are known as .....

### Illustration 12-2

The bad and doubtful debts account of a company for a year showed the following:

	₦		₦
Trade debts written off	3,000	Reserves b/f	
Reserves c/f		Specific	10,000
Specific	12,000	General	6,000
General	5,000	Charged to P&L A/C	4,000
	20,000		20,000

In the profit and loss account of this company, the sum of ₦4, 000 will be shown as the charge for bad and doubtful debts for the year. How this sum has been arrived at can be reproduced in a statement from as follows:		
		₦
Trade debts written off	(a)	3,000
Add: increase in specific provision N (12,000 - 10,000)	(b)	2,000
		5,000
Les: reduction in general provision N(6,000 – 5,000)	(c)	1,000
Charged in profit and loss account		4,000

It will be easier from this statement to determine which amount should be adjusted for, in the tax computation in respect of this company's bad and doubtful debts charge, as follows:

- a. This will be an allowable charge as the amount written off is in respect of specific debts
- b. The increase will also be allowable as the amount involved is also in respect of specific debts.
- c. The general provision would have previously been disallowed when created. Any subsequent release of this sort of provision cannot be taxable as it had never been allowed. Thus, the accounting profit will be reduced by the amount of the reduction in the general provision, resulting in lower taxable profit than the accounting profit.

The only adjustment necessary in respect of the foregoing is a deduction of the sum of ₦1, 000 in respect of (c) above from the accounting profit to arrive at the taxable profit of the company. Thus, if a specific reserve for bad debts increases or decreases, no adjustment is necessary to the accounting profit, but in case of general reserve appropriate adjustment will need to be put through.

### SELF-ASSESSMENT EXERCISE

- i. Some of the conditions for treating ..... and ..... debts are that they must relate to debts incurred in the ordinary course of the trade or business and must be identifiable to specific debts.
- ii. One of the allowable deductions for ..... is that expenses attributable to the maintenance of the property concerned.

### 3.3 Donations

Company Income Tax Act (CITA) Section 21 stipulates, among other things, the conditions to be satisfied before any donation can be allowed. These are:

- a. Donations must be made out of the profits of the company (section 21(2)). This, if a company makes a loss, whatever donations paid during that year should not be treated as allowable
- b. Donations should not be expenditure of a capital nature
- c. For any year of assessment, the maximum amount allowable is limited to 10% of the total profits of the company before deducting the donations
- d. The donation must be made to any of the approved bodies.

Following the provisions of the Companies Income Tax (Amendment) act of 16th April 2007, donations (whether of a revenue or capital nature) made in respect of university and other tertiary or research institutions for research or any developmental purpose, or as an endowment out of profits of the period by a company, shall not exceed an amount which is equal to 15% of the total profits or 25% of the tax payable in the year of the donation, whichever is higher.

The Fifth Schedule to CITA which contains the list of the approved bodies, etc. to which donations may be made is reproduced below with necessary grouping to facilitate commitment to memory by readers. Donation to anybody or institution whose name is not included on the list will not be an allowable deduction.

### **3.3.1 Fifth Schedule (Section 21)**

Funds, Bodies and Institution in Nigeria to which donations may be made under Section 21 of the act are:

#### **Youths/Philanthropic Organisations**

- a. The Boys Brigade of Nigeria
- b. The Boys Scouts of Nigeria
- c. The Girls Guides of Nigeria
- d. The Nigerian Red Cross
- e. The National Youth Council of Nigeria
- f. The Nigerian Youth Trust

**Religious**

- a. The Christian Council of Nigeria
- b. Islamic Education Trust

**Medical**

- a. Any hospital owned by the government of the federation or of a state or any university teaching hospital or any hospital which is carried on by a society or association otherwise than for the purpose of profits or gains, to the individual members of that society or association.

**Educational**

- a. Any educational institution affiliated under any law with any university in Nigeria or established under any law in Nigeria and any other educational institution recognised by any government in Nigeria.
- b. The Institute of Medical Laboratory Technology
- c. The National Library
- d. A public fund established and maintained exclusively for providing money for the acquisition, construction, maintenance or equipping a building used or to be used as a school or college by the government of the federation or a state or by a public authority or by a society or association which is carried on otherwise than for the purpose of profit or gain to the individual members of that society or association.
- e. The National Braille Library of Nigeria
- f. Van Leer Nigerian Educational Trust
- g. The Institute of Chartered Accountants of Nigeria Building Fund
- h. Nigerian Accounting Standards Revenue Service
- i. Paterson Zochonis Nigeria Technical Education Trust Fund
- j. Educational corporative society.

**Relief Funds**

- a. National commission for rehabilitation
- b. A public fund established and maintained for providing money for the construction or maintenance of a public memorial relating to the civil war in Nigeria which ended on 15 January, 1970
- c. Southern Africa relief fund

- d. Anya public fund established or approved by the government of the federation or any of the state governments in aid of or for the relief of drought or any other national disaster in any part of the federation.

### **Research**

- a. The Cocoa Research Institute of Nigeria
- b. The National Council for Medical Research
- c. The National Science and Technology Development Agency
- d. The Nigerian Institute for international Affairs
- e. The Nigerian Institute for Oil Palm Research
- f. The Nigerian Institute for Trypanosomiasis Research
- g. National Science and Technology Fund.

### **Welfare**

- a. A public institution or public fund (including the Armed Forces Comfort Fund) established or maintained for the comfort, recreation or welfare of members of the Nigerian Army, Navy or Air Force  
National Sports Commission and its state association  
The Nigerian Society for the Deaf and Dumb
- b. The Society for the Blind
- c. The Nigerian National Advisory Council for the Blind
- d. Association or Societies for the Blind in Nigeria
- e. Training Centres and Residential Schools for the Blind in Nigeria
- f. Rotary International (Polio-plus Programme)
- g. The Musical Society of Nigeria

### **Foundations/Endowment Fund**

- a. Kewalram Chanrai Foundation Limited
- b. Afprint Foundation Limited
- c. University College Hospital Endowment Fund

### **Others**

- a. The Nigerian Museum
- b. Nigerian Conservation Fund

References to donations made by a company do not include any payments made by the company for valuable consideration.

### 3.3.2 Research and Development

The allowability of amounts relating to research and development are in two sections of the act.

Section 20 (g) (iii) allows expenses proved to the satisfaction of the revenue service to have been incurred by the company on research and development for the period including the amount of levy paid by it to the National Science and Technology Fund. Section 22 allows the deduction of amount of reserves made out of the profits of that period by a company for research and development. The deduction to be allowed under this Section for any year of assessment shall not exceed 10% of the total profits of the company for that year as ascertained before any deduction is made under this section and Section 21 (deductible donations) of the act.

The effect of these two sections can be summarised thus:

- a. Actual expenditure on research and development are allowable deductions in accordance with the provisions of Section 20.
- b. Reserve made out of profits for research and development expenditure is allowed as a deduction from profit subject to the ceiling fixed.

One thing to be noted though is that a company cannot make the deduction twice. If the deduction was made when the reserve was made, such cannot be deducted again when the actual expenditure is incurred. In addition, subsection 3 of Section 22 provides for 20% investment tax credits on the qualifying expenditure of companies and other organisations engaged in research and development activities for commercialisation once the expenditure are incurred for that purpose.

### 3.3.3 Disallowable Expenditures

Certain expenditures are disallowed for tax purposes. These are specifically listed in Section 23 of the act and they should be added back to accounting profit even if their charge in the profit and loss account could be justified under ordinary rules of commercial accountancy. These are:

- a. Capital repaid or withdrawn and any expenditure of a capital nature.
- b. Any sum recoverable under an insurance or contract of indemnity.
- c. Taxes on income or profits levied in Nigeria or elsewhere. In case of tax levied outside Nigeria on profits which are also chargeable to tax

- in Nigeria and double taxation relief is not available, such tax will be an allowable deductions.
- d. Payments to unapproved pension, provident, savings or widows and orphans society fund or schemes.
  - e. Depreciation of any asset (capital allowances are granted instead).
  - f. All appropriations for profit; namely, dividends, general provisions for bad and doubtful debts, write off of preliminary and formation expenses and expenses on issue or redemption of shares and other securities, etc. pre-production expenses to the extent to which they are not of capital nature will be allowable deduction as such have been incurred for the purpose of producing the company's profit.
  - g. Any expenses of any description incurred within or outside Nigeria for the purpose of earning management fee unless prior approval of an agreement giving rise to such management fee has been obtained from the minister.
  - h. Any expense whatsoever incurred within or outside Nigeria as management fee under any agreement entered into after the commencement of this section except to the extent as the minister may allow; and
  - i. Any expenses of any description incurred outside Nigeria for and on behalf of any company except of a nature and to the extent as the Revenue Service may consider allowable.

### **3.3.4 Waiver or Refund or Liability or Expense**

Where the liability for an allowed expense is subsequently waived or released or a refund is received for the amount paid, the amount which is so waived, released, or refunded is deemed to be the income of the company in the year in which the waiver, release or a refund is made or given. Similar provision is applicable in personal taxation practice.

It should be noted that where a waiver of a non-revenue item, for example, a loan is in favour of a company, such an amount shall only be subjected to capital gains tax if applicable, not income tax, as the liability had not been previously treated as an allowed expense. If no CGT is due, such a waiver cannot be subject to tax.

### **3.3.5 Basis of Assessment**

As earlier stated, the income tax year which is called an assessment year is the government's financial or fiscal year. It runs from 1 January to 31 December of every year (it was from 1 April to 31 March following, up to



31 March 1980). A company's accounting year will be related to the government's year in which the operating result of such company is to be assessed to tax. An accounting period which is related to any particular assessment year is usually referred to as the "basis period" of that assessment year.

The general rules for determining basis period of assessment are contained in section 25 of CITA. The assessable profits of any company for each year of assessment shall be the profits of the year immediately preceding the assessment year. This is referred to as the preceding year basis of assessment. Assessment profit as defined in CITA is usually the accounting profit of the company as adjusted for tax purposes, that is, the adjusted profit that will be arrived at before reflecting the effect of any loss relief, balancing charge and or capital allowances.

Where a company's accounting year coincides with the government fiscal year (assessment year) it is the accounting year ending within the preceding government fiscal year that is taken as the preceding year. Where the accounting year of a company does not coincide with an assessment year, it is the profit of the accounting year ending on any au in the preceding assessment year that is taken to be the profit of the preceding assessment year.

### Illustration 12-3

Consider the cases of two companies making up their yearly account, one to 31 December and the other to 30 June, respectively. The years of assessment and relevant basis periods will be as follows:

#### Basic periods:

	(A)	(B)
Assessment	Where accounts are made up to 31 December	Where account are made up to 30 June
2001	A/cs. For y/e 31/12/2000	A/cs. For y/e 30/6/2000
2002	A/cs. For y/e 31/12/2001	A/cs. For y/e 30/6/2001
2003	A/cs. For y/e 31/12/2002	A/cs. For y/e 30/6/2002
2004	A/cs. For y/e 31/12/2003	A/cs. For y/e 30/6/2003

Note that in (A) the basis periods coincide with the preceding government fiscal year, since the accounting years of the company coincide with the government accounting years. In (B), the company's accounting years do not coincide with the government accounting years, nevertheless, each of

the company's accounting years ending on a date in each of the preceding government accounting year is used.

This will be the position, for as long as the companies continue to prepare their accounts to cover periods of twelve months, ending on those dates. However, exemptions to this rule are:

1. On commencement of a new trade – first three assessment years.
2. On cessation of trade-last two assessment years.
3. On a permanent change in accounting date-the year of change and the two assessment years following.

The applicable procedures are summarised below.

### **3.4 New Trade or Business**

First assessment year–profit from date of commencement to the 31 December following:

Second assessment year – profit of the first twelve months of operations.

Third assessment year – profit of the preceding assessment year, that is, on the preceding year basis. Remember that if no twelve month accounting has been prepared to end on a date in the preceding assessment year, the second year's assessment is repeated as the assessment for the third year. For the fourth and subsequent years, the preceding year basis rule will apply.

It should also be remembered that election can be made by the taxpayer, that is, the company, to have the assessment for the second and third years based on the actual results for those years. The manner of making this election and applicable time limits are the same for both personal and companies' taxation.

#### **Illustration 12-4**

Mr. Oluwalogbun established Goldmine Fishers Limited in 1991 for the purpose of commercial fish production. The company commenced business on 1 January 1992. Its accounting date is 31 December each year while its adjusted profits for the first ten years are as follows:

Trade periods	Adjusted profits/losses
	₦
Year ended 31/12/92	(100,000)
Year ended 31/12/93	30,000
Year ended 31/12/94	25,000
Year ended 31/12/95	20,000
Year ended 31/12/96	15,000
Year ended 31/12/97	35,000
Year ended 31/12/98	50,000
Year ended 31/12/99	(40,000)
Year ended 31/12/00	35,000
Year ended 31/12/01	30,000

Required: compute the assessable profits for the relevant years [12 marks  
ICAN PE II May 2004 (Question 6)]

#### Suggested Solution 12-4

YOA		Basis period Assessable	Assessable Profits
		₦	₦
1992	01/01/92-31/12/92- actual		
	Loss for year ended 31/12/92	(100,000)	Nil
	Loss c/f to 1993	(100,000)	
1993	1 <sup>st</sup> 12 months – 01/01/92-21/12/92	(100,000)	
	Loss b/f from 1992	(100,000)	
	Loss c/f to 1994 restricted to actual loss sustained	(100,000)	Nil
1994	Preceding year basis-01/01/93-31/12/93		
	Profit for year ended 21/12/93	30,000	
	Loss b/f from 1993	(100,000)	
	Loss c/f to 1995	( 70,000)	Nil
1995	Preceding year basis 01/01/94-31/12/04		
	Profit for year ended 31/12/94	25,000	
	Loss b/f from 1994	(70,000)	
	Loss c/f to 1996	(45,000)	Nil

Penultimate year – the assessment year before the year of cessation is termed the penultimate year. The assessment for this year which would have been based on the preceding year basis would be re-computed on actual year basis. If the amount assessable on actual basis is greater than that on preceding year basis, the Inland Revenue will opt to have the assessment for that year received to actual year basis.

It is to be noted that it is the revenue that has this option at cessation. The taxpayers' option is available at commencement.

Where a company which has permanently ceased to carry on a trade or business subsequently receives or pays any sum which would have been included in or deducted from the profits of that trade or business if it had been received or paid prior to the date of cessation such sum is treated as having been received or paid on the date of cessation.

A company ceasing permanently to carry on a trade shall not deem to derive assessable profits from such trade for the year of assessment following that in which the cessation occurs.

### **3.5 Change of Accounting Date**

When there is a change of accounting date the revenue has power to compute as it deems fit the assessable profits for:

- a. The year of assessment in which the change occurs, and
- b. The two years of assessment following

The assessable profits will be computed on the basis of the old and the new accounting dates for the three relevant years and the revenue will decide on the alternative that produces higher assessable profits. Note that the preceding year rule is strictly observed throughout the computations.

#### **Illustration 12-5**

Format construction Nigeria Ltd, is an incorporated company in Nigeria with affiliate worldwide. It has been operating in Nigeria for many years and prepares its accounts to 31 December of every year. The controlling company for all the affiliates worldwide which has its registered office in Sweden had also been preparing its accounts to 31 December of every year, until 1993, when it decided at its revenue service meeting that all affiliated companies worldwide must submit copies of their 12 months audited

accounts two months before 31 December of every year, beginning from 1993.

There are two alternatives the Revenue Service of Directors of Format Construction Nigeria Ltd, is considering:

To prepare accounts for the year ending within 1994 to end in

- a. June 1994, or
- b. September 1994

As a tax consultant, your advice is sought, so as to ascertain the financial year end that would minimise the assessable profits on which tax is payable for those periods. The following information were provided:

	₦			
Net profit per account for 12 months ended 31 Dec. 1992	200,000			
Net profit per account for 12 months ended 31 Dec. 1993	500,000			
Net profit per account for 12 months ended 31 Dec. 1994	600,000			
Net profit per account for 12 months ended 31 Dec. 1995	700,000			
Other information in respect of the accounts for the year ended 31st December are as follows:				
	1992	1993	1994	1995
	₦	₦	₦	₦
Depreciation charged	20,000	50,000	55,000	70,000
Loss on sales of assets included			(5,000)	
<b>You are required to:</b>				
Advice with supporting computations on the new accounting year end which the Nigerian company should adopt				
<b>Suggested Solution 12-5</b>				
Format construction Nigeria limited				
The profits presented shall be adjusted for tax purposes				
	1992	1993	1994	1995
	₦	₦	₦	₦
Profits per A/cs	200,000	500,000	600,000	700,000
Add back				
Depreciation	20,000	50,000	55,000	70,000
Loss on sale of assets			5,000	
Adjusted profits	220,000	550,000	660,000	770,000

The year of change with the proposal is 1994 assessment year. The Revenue will compute as they think fit the assessments for 1994 (the year of change) and 1995, 1996 (the two years following).					
<b>On the basis of June, as the new accounting date:</b>					
<b>Alternative 1: old Accounting date, 31/12</b>					
					₦
1994		1/1/93 to 31/12/93			550,000
1995		1/1/94 to 31/12/94			660,000
1996		1/1/95 to 31/12/95			770,000
<b>Alternative 2: New accounting date, 30/6</b>					
1994	1/7/92 to 30/6/93	6/12 x N200,000 + 6/12 x N550,000	=		385,000
1995	1/7/94 to 30/6/94	6/12 x N550,000 + 6/12 x N660,000	=		605,000
1996	1/7/94 to 30/6/95	6/12 x N660,000 + 6/12 x N715,000	=		715,000
Revenue compares the two, as follows:					
Assessment year		Old 31/12		New 30/6	
		₦		₦	
1994		550,000		385,000	
1995		660,000		605,000	
1996		770,000		715,000	
Total for the three years		1,980,000		1,705,000	
Revenue chooses the alternative that produces the higher assessable profits, that is, the assessments are:					
		₦			
1994		550,000			
1995		660,000			
1996		770,000			
On the basis of 30 September:					
The alternative on the basis of the old accounting date of 31 December, will be as before:					
1994	1/10/92 to 30/9/93	3/12 x N220,000 + 9/12 x N550,000	=		467,500
1995	1/10/94 to 30/9/94	3/12 x N550,000 + 9/12 x N660,000	=		632,500
1996	1/10/94 to 30/9/95	3/12 x N660,000 + 9/12 x N715,000	=		742,500
Revenue compares to the two, thus					
Assessment year		Old 31/12		New 30/6	

	₦	₦
1994	550,000	467,500
1995	660,000	632,500
1996	770,000	742,500
Total for the three years	1,980,000	1,842,500
Revenue chooses the alternative that provides the higher assessable profits, that is the assessments for the three years are based on the accounting date of 31 December		
	₦	
1994	550,000	
1995	660,000	
1996	770,000	
<b>Explanatory note</b>		
Irrespective of whether the accounting date is June or September, the revenue's option will produce the higher assessable profits and shall be that based on a 31 December accounting date. Thus, whether the company prepares the accounts for the year ending within 1994, to end in June 1994 or September 1994, will have no effect on the assessable profits for the years of assessment involved as it is the Revenue that has the option to make the election.		

### 3.6 Company in Partnership with Another

Where a company is engaged in a trade or business with any other person in Nigeria, that trade or business shall be deemed to constitute a separate source of profits, and the assessable profits of the company from that source shall be determined under the provisions of the Personal Income Tax Decree 1993 in like manner as would be the assessable income of any individual partner in that partnership – CITA Section 25(8).

In effect, the taxation rules for determining the incomes of a partner in a partnership are the same whether the partners therein are individuals or companies.

#### 3.6.1 Total Profits and Sources of Profits

The total profits of any company for any year of assessment shall be the amount of its total assessable profits from all sources for that year together with any additions thereto of the amount of balancing charge that may be applicable less deduction due for loss relief, investment allowance and

capital allowance. This is the substance of the definition of total profits as given in subsection 1 of section 27 of CITA.

The components of this definition which should be noted are: assessable profits from all sources; loss relief; capital allowances including investment allowances and balancing charge. Assessable profit as treated in this chapter is the accounting profit as adjusted for tax purposes but before having regard to any loss relief, capital allowances or balancing charge. Loss relief is considered in the next subparagraph of this chapter while investment and capital allowances as well as balancing charge are discussed elsewhere in this study pack. The reference to “profits from all sources” will not be discussed.

The definition of sources was not given anywhere in CITA. It is therefore uncertain how the business activities of each company are to be grouped for this purpose. The Federal Inland Revenue Service had in 1985 issued a circular in which there was a reference to what “source” could mean. In that circular, examples of sources of profits were given as:

...manufacturing of goods up to disposal of such goods, road construction, building construction, road transport, credit financing, equipment leasing, leasing of immovable property, and investment in stock and shares.

Examples also given in the same circular in the case of an insurance company’s sources of profits are:

...group life, industrial life, ordinary life endowment, all risks, motor vehicle, fire, marine, workmen compensation, investment of funds.

The rationale behind this classification is unknown and it is uncertain whether it will be acceptable to the general business community. Whether or not an acceptable classification is produced the most important thing to note is that each company might be required to produce separate profit and loss account for each separate activity that can be regarded as unrelated to the other ones.

This is with a view to being able to determine whether there are losses from particular sources which should not be aggregated with profits from other sources for the purpose of arriving at the total profits of the company. It is certain that producing such separate profit and loss accounts could be very cumbersome for companies having several lines of business activities, for example, UAC of Nigeria Plc and other conglomerates. Furthermore, the



method of apportionment of joint or overheads of the company to arrive at the profit or loss from each source would need to be specified by the revenue service.

Perhaps CITA might need an amendment to incorporate the definition of the various sources and how the profit or loss from each source is to be determined vis-à-vis the apportionment of joint cost. The enactment of legislation dealing with group relief would also go a large extent in eliminating the practical difficulties inherent in the existing provisions of CITA.

### 3.6.2 Decided Case

The requirement of Section 27(1) is that the assessable profits from all sources are to be aggregated. If a loss has been incurred from any one source, such cannot be aggregated with the profit from other sources to determine total profits. Such loss is to be carried forward for relief against future profits from the same source. Additions and deductions are then made for balancing charge and investment and capital allowances respectively to arrive at total profits. When the total profits have been arrived at, the tax rate (presently 30%) is applied on the total profits to arrive at the tax payable.

#### Illustration 12-6

Consider a hypothetical company with the respective figures and three sources of profits for an assessment year as shown below:				
		Total of assessable profits		Losses carried forward
		₦	₦	
1.	Trade profit	1,000		
	Trade losses brought forward	-		
			1,000	
2	Property income	400		
	Less losses of the same source brought forward	(600)		
	Unrelieved loss		-	(200)
3	Interest income		300	
	Total of assessable profits		1,300	
	Add balancing charge		200	
			1,500	

	Deduct			
	Investment allowance	-		
	Capital allowances		350	350
	Total profits			1,150

It is on these total profits that the tax rate will be applied, to arrive at the amount of tax payable. For example, the tax payable in the illustration above with a tax rate of 30% is N345, that is, 30% of N1, 500. The N200 unrelieved loss from the property income source will be carried forward for relief against future profit from the same source; it cannot be set off against the N1, 150 total profits.

### Order of giving effect to Section 27(1):

The wordings of Section 27(1), regarding total profits of a company for any year of assessment can be interpreted and broken down into stages as follows:

- Stage 1      Aggregate all assessable profits from all sources.
- Stage 2      To the total of the assessable profits from all sources add:  
Any balancing charge.
- Stage 3      Deduct  
Any amount of loss relief due.
- Stage 4      Any also deduct  
Any investment and capital allowance to be granted.

From the illustration above, it is clear that these stages cannot be strictly adhered to as the effect of loss relief (stage 3) had to be shown in stage 1 to ensure that only the net assessable profit from each source are aggregated. Furthermore, the effect of any balancing change as well as investment and capital allowance should also have been shown against the respective source where the relevant fixed assets had been employed. For example, it would appear ridiculous deducting capital allowances from interest income where no qualifying expenditure had been incurred for the purpose of earning such income.

Perhaps the aggregation which is in state 1 should in fact be in stage 4, after the exercise in the other three stages would have been performed for each source of assessable profits wherever applicable and this is the treatment that is recommended. It should be noted that the capital allowances restriction will still be applicable for any capital allowances to be deducted in computing total profit.

### 3.6.3 Losses

In arriving at the chargeable profits of a company, losses, if any, incurred in the preceding year of assessment are to be deducted. Contrary to what obtains in personal taxation, there is no current year loss relief available to companies. It is only the carry forward relief that is available.

Section 27 of the act contains the provisions applicable to losses incurred by companies. Essentially, these are:

- a. The amount of the loss to be allowed should be that which the Revenue Service is satisfied as having been incurred by the company in a trade or a business during a preceding year of assessment (Section 27(2)(1)0. The reference to preceding year in the wordings of that Section of CITA emphasises that current year relief is not available for losses incurred by companies.
- b. In no circumstances shall the amount to be relieved exceed the total amount of the loss;
- c. Relief can only be against profits from the same trade or business in which the loss was incurred.
- d. Losses can be carried forward for a maximum of four year following that in they are incurred, losses incurred by any company engaged in agricultural trade or business can be carried forward with no time limit, and
- e. The loss available for relief should be computed on the same basis as that of assessable profit, for a year to assessment.

### 3.6.4 Terminal Loss Relief

There is no provision in the act for the granting of relief for losses by a company in the year of assessment when its trade or business permanently ceases. Thus, there is no relief for any loss incurred in the last year of trade not for any unrelieved loss accumulated up to the date of cessation.

The computation of the assessable income for the year of cessation will be on actual basis. Since a loss has been incurred for this period, assessment will be nil, for the assessment year concerned. However, there are provisions for the relief of unutilised capital allowances at the time of

permanent cessation of a company's trade. Such capital allowances can be carried back to be relieved against the assessable profits of the preceding years up to the fifth year before the year of cessation (Sch.2 Para. 24(5)).

### 3.6.5 Normal Company Tax Rate

For each year of assessment, tax is payable at the current rate of 30% of the total profits of every company, section 29(1). The current (2008) rate of 30% was introduced from the 1996 assessment year. The rate can be altered at any time upon the passing of the appropriate legislation.

The total profits for any year of assessment have already been discussed.

Education tax will be payable at 2% of assessable profit. The assessable profit of a company must be known, before its education tax liability can be computed.

### 3.6.6 Minimum Tax (Section 28A)

Where in any year of assessment, the ascertainment of total assessable profits from all sources of a company results in:

- a. A loss; or
- b. No tax payable, or
- c. Tax payable which is less than the minimum tax, the tax payable by the company shall be in the minimum tax computed as follows:
  - A. Where turnover is ~~₦~~500, 000 or below and the company has been in business for at least four calendar years.
    - i. 0.5% of gross profits, or
    - ii. 0.5% of gross profits, or
    - iii. 0.25% of paid up capital or
    - iv. 0.25% of the turnover

Whichever is the highest.

- B. Where turnover is higher than ~~₦~~500, 000, whatever is payable as computed in A above plus 0.125% of turnover in excess of ~~₦~~500, 000.

The foregoing provisions do not apply to:

- A company carrying on agricultural trade or business
- A company with at least 25% imported equity capital; and
- Any company for the first four calendar years of its commencement of business.

For any year of assessment when minimum tax is payable, the capital allowances due for that year will still be computed and relieved as much as possible from the assessable profits of the year as if the tax payable is based on the insufficiency of assessable profits can be carried forward to subsequent assessment years. The implication of this provision is that taxpayers will lose the capital allowances that could be relieved against the assessable profits regardless of the fact that the tax is not based on that assessable profits but on turnover, and so on, which will be the case when the minimum tax provisions are being applied. A way out is by not making a claim for capital allowances.

### **3.6.7 Education Tax**

#### **(a) Enabling Law and Imposition of Education Tax**

Education Tax was first introduced in Nigeria in 1993 with the enactment of the education Tax Decree No. 7 of 1993. The act is currently known as Education Tax Act CAP E4 LFN 2004.

Education tax is payable on an annual basis by every registered company in Nigeria that is liable to tax under the Companies Income Tax Act and Petroleum Profits Tax Act, which has an adjusted/assessable loss, will not be liable to Education Tax.

#### **(b) Administration of Education Tax**

The Federal Inland Revenue Service (FIRS) shall assess and collect education tax from Companies. When the FIRS is assessing a company for either income Tax or/and Petroleum Profits Tax, it is required to simultaneously raise the education tax assessment on such company. The tax is payable within 60 days after the Revenue Service has served notice of assessment on a company and the Revenue Service is empowered by the act to device such forms, as it may deem necessary, for the purpose of assessing and collecting the tax. At the moment, a taxpayer is expected to

file self-assessment form for education tax at the time of filling its company tax returns.

### **3.7 Small Business Rate**

Certain companies are referred to as small business with turnover of ₦1,000,000 (one million) and below in the year of assessment shall be charged a lower rate of tax of 20% for four years from the commencement of the business, section 29(6).

The lower rate will be applicable only to companies engaged in the business of:

- a. Manufacturing
- b. Agricultural production
- c. Mining of solid minerals
- d. Wholly export trade.

If it is assumed that a company is a manufacturer of certain goods and that the turnover in respect of the 2008 assessment year is ₦990, 000 with profits of ₦250, 000, the tax payable shall be 20% of ₦250,000 that is ₦50,000. In order to determine the rate of tax that should be applied to any company therefore, the nature of the business being carried on, as well as the turnover of the company in the assessment year, will need to be considered. Furthermore, the ₦1, 000,000 turnover limit, must not be exceeded, if the lower tax rate is to apply.

It should be noted that small business rate was applicable with effect from the assessment years 1988; 1989 and 1990 for companies in operation before 1 January, 1988. The turnover limit then was ₦500, 000. Act No.3 of 1993 provides for an extension of this benefit for an additional two years where the company shows evidence of good records and management and remained in the same line of business.

The turnover limit is now ₦, 000,000 for each assessment year, while the rate can be applied for the first four assessment years provided the annual turnover still qualifies the business.

### **3.8 Pre-Operation Levy**

A company which is yet to commence business after at least 6 months of incorporation shall, for each year it obtains a tax clearance certificate pays a levy of:

- a. ₦25,000 for the first year, and
- b. ₦20,000 for every subsequent year

### **3.9 Advance Income Tax Payment**

When a company wishes to pay dividend out of profit on which no tax has been paid, CITA Section 31(7) provides that tax at standard company tax rate is payable on the amount of the dividend. The provisions of Section 15A and 16(B) of CITA is also to the same effect. If any provisional tax has been paid by the company for the assessment year, this will be taken into account in determining the amount of tax payable under this section.

The tax is payable before the dividend is paid and had nothing to do with withholding tax which will still be deducted normally. The tax so paid will be taken as a deposit against the tax due from the company on the profits out of which the dividends is paid.

Thus, when the company wishes to settle its tax liability, the amount paid as deposit will be deducted from the total amount of the income tax liability of the company for that year.

### **4.0 CONCLUSION**

This unit provides information about profits and sources of profits of corporate bodies that are subject to tax under the companies income tax act, CAP C21 LFN, 2004. Profits or gains of corporate bodies are taxed, while losses are allowed to be relieved against profits of subsequent years. Losses can be carried forward generally for a total of four years but there is no time limit for relief of losses incurred by companies engaged in agricultural business.

The bodies and associations whose income or profits are exempted from tax under the act were listed. Some incomes are exempted on the condition that they were not derived from trade or business being carried on. Others are exempted even if they were derived from trade or business. Readers must have learnt the principle of allowable deductions as applicable to companies chargeable to tax under CITA.

An allowable expenditure has to be that expenditure that is wholly, exclusively, necessarily, and reasonably incurred by the company in the production of the income. It has been shown how the basis period of assessment is to be determined for tax purposes. It has been demonstrated that the preceding year basis rule is applicable generally in the taxation of companies except at commencement or cessation of business.

The global profits of Nigerian companies are taxable irrespective of whether or not they are brought into or received in Nigeria. On the other hand, the profits of non-Nigeria companies are chargeable under CITA subject to applicable exemptions in any available double taxation agreements. Companies' profits chargeable to tax under CITA are assessed to income tax at 30% of total profits and education tax @ 2% of accessible income.

A small business rate of 20% is applicable to companies with turnover of ₦1, 000,000 (One Million Naira Only) and below in each year of assessment for four years from the date of commencement of the business. The lower rate applies to companies that are engaged in the business of manufacturing; agricultural production; mining of solid minerals or wholly export trade.

## **5.0 SUMMARY**

In this unit, we have enumerated areas where government can impose tax on profits of companies and defined and explained how tax can be imposed on an authorised unit trust scheme. We specified the bodies to which donations can be made from the profits of companies and stated how tax can be imposed on a new trade or business stated the relevance of changing accounting dates in line with government's financial year. Furthermore, we assessed the tax on the profits of a company in partnership with another and stated the tax rate imposed on small businesses. We determined the pre-operation levy; and listed the conditions governing payment of advance income tax by companies.

You have now completed the second module of this course.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. What conditions are specified in the Companies Income Tax Act under which donations may be allowed?



2. The Companies Income Tax Act specifies the list of approved bodies to which donations could be made. List some of them which you know.
3. What does Section 31(7) say of companies wishing to pay dividends out of profit on which no tax had been paid?
4. Section 19 of CITA contains the list of profits or gains of companies or corporate bodies exempted from company taxation. List some of these exemptions.
5. Write short notes on the following:
  - Authorised unit trust
  - Unit trust scheme
  - Unit holder
  - A trustee.
6. List the sources on which tax can be imposed on the profits of any company in Nigeria based on Section 8 of the Companies Income Tax Act (CITA).

## **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack. (2011).

**MODULE 3**

Unit 1	Person Chargeable, Offences and Penalties
Unit 2	Tax on Special Businesses
Unit 3	Petroleum Profit Tax
Unit 4	Stamp Duties
Unit 5	Tax Planning and Tax Administration
Unit 6	Tax on Pioneer Industries

**UNIT 1 PERSON CHARGEABLE, OFFENCES AND PENALTIES****CONTENTS**

1.0	Introduction
2.0	Objectives
3.0	Main Content
3.1	Chargeability to Tax
3.2	Persons Answerable
3.3	Directors Appointment of Agent
3.4	Company in Liquidation
3.5	Company's Representative on Tax Matters
3.6	Offences and Penalties
3.7	Duty of Secrecy and Confidentiality
4.0	Conclusion
5.0	Summary
6.0	Tutor-Marked Assignment
7.0	References/Further Reading

**1.0 INTRODUCTION**

You are welcome to the third and final module in this course. In this module, you will be introduced to another six units made up of six different topics, namely: Person Chargeable, Offences and Penalties; Special Businesses; Petroleum Profit Tax; Stamp Duties; Tax Planning and Tax Administration and Tax on Pioneer Industries.

In this unit, we shall be exploring another topic titled: Person Chargeable, Offences and Penalties.

## 2.0 OBJECTIVES

At the end of this unit, you should be able to:

- explain how a company can be chargeability to tax
- state the persons answerable on tax matters on behalf of a company
- explain the powers of the revenue service to appoint directors as agent for tax purposes
- state the conditions under which a company in liquidation shall pay
- list the offences and penalties
- discuss the duty of secrecy and confidentiality.

## 3.0 MAIN CONTENT

Since a company is a separate entity different from its shareholders, it is important that there should be a clear conception of how a company can be charged to tax and who should be answerable for the organisation in that regard. Part VII (Section 36 to 40) of the CITA contains the relevant provision.

### 3.1 Chargeability to Tax

Section 36 of CITA states that “A company shall be chargeable to tax:

- (a) In its own name; or
- (b) In the name of any principal officer, attorney, factor, agent or representative of the company in Nigeria, in like manner and to like amount, as such company would have been chargeable; or
- (c) In the name of a receiver or liquidator or of any attorney, agent or representative thereof in Nigeria, in like manner and to like amount liquidator had been appointed.”

### SELF-ASSESSMENT EXERCISE

A company shall be chargeable to tax in three ways, namely: ....., ..... and .....

### **3.2 Persons Answerable**

Section 37 states: “The principal officer or manager in Nigeria or every company shall be answerable for doing all such acts, matters and things as are required to be done by virtue of the act for the assessment of the company and payment of the tax.” Though there is no reference to this in Section 37, for a company in receivership or in liquidation ‘the principal officer or manager’ is the receiver or liquidator, as appropriate.

The ..... or ..... in Nigeria or every company shall be answerable for doing all such acts, matters and things as required to be done by virtue of Section 37 of the CITA for the assessment of the company and payment of tax.

### **3.3 Directors Appointment of Agent (Section 38)**

The Revenue Service or Directors of a company may appoint any person to be the agent of any company. Any person so declared may be required to pay any tax, which is or will be payable by the company, from any of the company’s money that is, or will be, in the possession of the agent. If the person declare as the agent fails to comply with such request, the tax shall be recoverable directly from the company.

Such a person, however, has a right of objection and appeal for any notice served upon him in accordance with the provisions of Section 38, as if such notice were as assessment on him personally. Section 38 empowers the agents, or any other person answerable for the payment of tax on behalf of a company, to deduct from any of such company’s money coming into his hands so much thereof as shall be sufficient to pay the tax.

### **3.4 Company in Liquidation (Section 40)**

Before any distribution can be made to the shareholders of a company in liquidation, the liquidation must ensure that he has made provision for the payment in full of any tax which may be ascertained payable by the company, including any tax deductions made by the company under any law in force in any part of Nigeria relating to the taxation of individuals.

### **3.5 Company’s Representative on Tax Matters**

Every company shall designate a representative who shall answer every query relating to the company’s tax matters. Such a person should be

knowledgeable in the field of taxation as may be approved from time to time by the Revenue Service (Session 41(6)).

### 3.6 Offences and Penalties

Part XII of CITA contains provisions relating to offences and penalties. The following is a list of what constitute offences under the act, together with the prescribed penalties on conviction:

Offences	Penalties
1. Contravention or failure to comply with any of the provisions of the act or any rule made thereunder: Section 71(1)	A fine of N20,000 and where the offence is the failure to furnish a statement or information or to kept records required, a further sum of N20,000 for each and every day during which such failure continues. In default t of payment then in imprisonment for six months. This penalty is also application for an offence or contravention of any of the provisions of the act for which no other penalty is specifically provided.
2. Failure to comply with the requirements of a notice served on any person under the provisions of the act: Section 71 (2) (a)	As for 1 above
3. Failure, without sufficient cause, to attend or answer to a notice or summons served on any person under the provisions of the act, or having attended, failure to answer any question lawfully put to him: section 71(2) (b)	As for 1 above
4. Making of incorrect returns, without reasonable excuse, by omitting or understating any profits liable to tax under the act: Section 72 (1)(a)	A fine of N200,000 and double the amount of tax which has been undercharged in consequence of such incorrect return or information, or would have been so undercharged if the return or information has been

	accepted as correct.
5. Giving of incorrect information, without reasonable excuse, in relation to any matter of thing affecting the liability of any company to tax: Section 72(1) (b)	As for 4 above
6. Knowingly making false statement or false representation for the purpose of obtaining any deduction, set-off, relief or repayment in respect of any company: Section 73(1)(a)	A fine of ₦200, 000 to an imprisonment for three years or to both such fine and imprisonment.
7. Aiding, abetting, assisting, counseling, inciting or inducing any other person-(i) to make or deliver any false return or statement under the act; or (ii) to keep or prepare false accounts or particulars concerning any profits on which tax is payable under the act; or(iii) unlawfully to refuse or neglect to pay tax: Section 73(1)(b)	As for 6 above
8. (a) Any official of the Revenue Service or any of its employees shall also be guilty of an offence by: (i) Demanding from any company an amount in excess of the authorised assessment of the tax; or (ii) Withholding for his own use or otherwise any portion of the amount of tax collected; or (iii) Rendering a false return, whether orally or in writing, of the amount of tax collected or received by him; or (iv) (a) defrauding any person, embezzling any money or otherwise using his position as to deal wrongfully Revenue Service or (b) collecting or attempting to collect the tax under the Act to do so: Section 74	A fine equivalent to 200 percent of the sum in question or to imprisonment for three years or to both such fine and imprisonment.

### **3.6.1 Other Offences and Penalties**

The offences and penalties listed in Part XII of the act which have been summarised above, are additional to those that are contained in other sections of the act.

### **3.7 Duty of Secrecy and Confidentiality**

Every person having any official duty or being employed in the administration of the act shall regard and deal with all documents, information, returns, assessment lists and copies of such lists relating to the income, chargeable profits or items thereof of any company, as secret and confidential.

Every person who at any time communicates or attempts to communicate such information or anything contained in such documents, returns, list, or copies to any person;

- (a) Other than a person to whom he is authorised by the minister to communicate it; or
- (b) Otherwise than for the purpose of the act or any act or law, relating to a tax upon income, in force in any part of Nigeria; shall be guilty of an offence.

No employee of the revenue service shall be required to produce in any court any return, document or assessment, or to be divulge or communicate to any court any matter or thing coming under his notice in the performance of his duties under the act except as may be necessary for the purpose of carrying into effect the provisions of the act, or in order to institute a prosecution, or in the course of a prosecution for any offence committed in relation to tax.

The obligation as to secrecy shall not prevent the disclosure the disclosure of necessary information to the authorised officers of the government of such other country as might be necessary for double taxation relief purposes.

## **4.0 CONCLUSION**

We have learnt that a company is a separate entity different from its shareholders, and there is therefore a clear conception on how it can be charged to tax and who should be answerable for the organisation in that

regard. The Part VII (Section 36 to 40) of the CITA, we learnt in the discussion, contains the relevant provision. You are expected to browse the website with a view to keeping abreast of the Company Income Tax Act (CITA) as appropriate.

## **5.0 SUMMARY**

In this unit, we have stated how a company can be chargeability to tax and the persons answerable on tax matters on behalf of a company; and discussed the powers of the revenue service to appoint directors as agent for tax purposes. We stated the conditions under which a company in liquidation shall pay its tax and discuss that each company appoints its representative on tax matters and listed the offences and penalties. Lastly, we discussed the duty of secrecy and confidentiality.

In the next unit, you will be introduced to another interesting topic: tax on special businesses.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. How can a company be chargeable to tax according to the CITA?
2. What steps can be taken to ensure that a company in liquidation pays its tax?
3. List what constitutes offences and penalties thereon in the CITA.

## **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack.(2011).



## UNIT 2 TAX ON SPECIAL BUSINESSES

### CONTENTS

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Shipping or Air Transport Business or Non-Nigerian Companies
  - 3.2 Nigerian Companies
  - 3.3 Business of Transmission of Messages
  - 3.4 Insurance Companies (CITA Section 14)
  - 3.5 Non-Nigerian Insurance Companies
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### 1.0 INTRODUCTION

In this unit, we stated how a company can be chargeability to tax; stated the persons answerable on tax matters on behalf of a company; known the powers of the revenue service to appoint directors as agent for tax purposes; stated the conditions under which a company in liquidation shall pay its tax; understood that each company appoints its representative on tax matters; listed the offences and penalties; and discussed the duty of secrecy and confidentiality.

In this unit, you will be introduced to another interesting topic: tax on special businesses.

### 2.0 OBJECTIVES

At the end of this unit, you should be able to:

- enumerate the conditions for charging taxes on the profits of non-Nigerian companies which are engaged in shipping or air transport businesses
- state the conditions governing taxation of the profits of Nigerian companies engaged in shipping or air transport businesses
- list the conditions governing taxation of the profits of companies engaged in the business of transmission of messages
- state the conditions under which Nigerian and non-Nigerian companies engaged in insurance business would be charged tax.

### 3.0 MAIN CONTENT

Company Income Tax Act (CITA) contains special provisions with regards to companies engaged in shipping or air transport business as well as those in insurance business. The provisions which are considered below are additional to the normal rules of allowable and disallowed expenditure in taxation practice.

#### 3.1 Shipping or Air Transport Business or Non-Nigerian Companies

CITA section 12 contains provisions regarding companies, other than Nigerian companies, in shipping or air transport business. The substance of that section is as follows:

- (a) The profit or losses of such company to be deemed to be derived from Nigerian is the full profits or losses arising from the carriage of passengers, mail, livestock, or loaded into an aircraft, in Nigeria. This does not apply to passengers, mails, livestock or goods which are brought into Nigeria solely for transshipment or for transfer from one aircraft to another or in either direction between an aircraft and a ship. Readers are referred to the part of this study packed on double taxation relief for such of these businesses that are exempted from Nigeria tax.

To the sums receivable in respect of passengers, etc. carried in Nigeria as referred to above, there shall be appointed the following:

- (a) The ratio of profits or losses of an accounting period, before depreciation, tot the total sums receivable in respect of the business of the company, and
- (b) The ratio of depreciation to the total sums so receivable as certified by the tax authority of any other country (where the non-Nigeria company is registered) to the satisfaction revenue service.

The amount arrived at shall be the full profits or losses which shall be liable to Nigerian tax. Note that this situation will apply where the revenue service is satisfied that the taxation authority of any other country computes and assesses on a basis not materially different from that prescribed by the act. The profits of a company which operates ships or aircrafts shall be certified to the revenue board by the taxation authority.

- (a) Where the ratios referred to above cannot, for any reason, be satisfactorily applied, the profits to be deemed to be derived from Nigeria may be computed on a fair percentage on the full sum receivable in respect of the carriage of passengers, etc shipped or loaded in Nigeria. When this occurs, the company has within six years to claim that its liability be recomputed on the basis of the rate ratios referred to above; and
- (b) If the company fails to agree with the revenue service, the revenues service shall give notice to the company of refusal to admit the claim and the provisions of CITA with respect to objections and appeals shall apply accordingly with any modifications.

### SELF-ASSESSMENT EXERCISE

..... contains special provisions with regards to companies engaged in shipping or air transport business as well as those in insurance business.

#### Illustration 15-1

Super \Air Limited is a foreign company operating a fleet of passenger and cargo aircrafts between Nigeria and Middle and Far East. The operating results for the four years ended 31 July, 2001, the first year of operation, are as follows:

	₦
Income from cargo freight Nigeria/Hong Kong	315,400
Income from passengers' freight Nigeria/Bombay	425,000
Income from passengers' freight Bahrain to Nigeria	556,600
Income from cargo loaded into aircraft on other routes	350,000
Less: operating expenses:	
Salaries and other expenses	860,000
Depreciation	160,000
Other expenses:	
General provision	40,000
Operational profit	1,060,000
	578,000

The following additional information is provided:

- |   |        |
|---|--------|
| (a) Salaries and other expenses include:  |        |
|   | ₦      |
| (i) Purchases of twin engines   | 65,000 |
| (ii) Use of airport facilities  | 18,000 |
| (iii) Hotel bills for first class passengers  | 21,000 |
| (iv) Accommodation for airlines crew  | 5,000  |
| (v) Gifts to airport staff for gratification  | 6,000  |
| (b) Capital allowances were agreed with the relevant authority at 150% of depreciation charged in the accounts. |        |

You are required to compute

- (i) The total profits of Super Air Limited for the purpose of the Nigerian income tax
- (ii) The liability to income tax in respect of the chargeable income tax and state the relevant year of assessment.

*ICAN past questions adapted*

### **Suggested solution**

#### **Super Air Limited**

#### **INCOME TAX COMPUTATION (YOA 2002)**

Income from cargo/passengers arising from Nigeria:	
Income from cargo freight expenses included;	₦
Income from passengers freight Nigeria/Hong Kong	315,000
Income from passengers' freight Nigeria/Bombay	425,000
	740,000
Allowable deductions:	₦
Salaries and other expenses as given	860,000
Less disallowable expenses included:	
Gifts to airport staff for gratification	(6,000)

	854,000
(Proportion application to Nigeria operation)	
	740,400
1,647,000 x 854,000 =	383,911
Depreciation allowance as agreed with	
Revenue 150% of 160,000	
	240,000
	623,911
Total profits from cargo/passengers arising from Nigeria	
	116,489
Income tax at 30% thereof	34,947

### 3.2 Nigerian Companies

Nigerian companies engaged in shipping or air transport business will be subjected to tax as any other company incorporated in Nigeria. It is their world income that will be subjected to income tax subject to the provisions of any applicable double taxation agreement and or any exemption in other parts of the act CITA.

#### SELF-ASSESSMENT EXERCISE

..... engaged in shipping or air transport business will be subjected to tax as any other company incorporated in Nigeria.

### 3.3 Business of Transmission of Messages

The above also apply to a company other than a Nigerian company carrying on the business of transmission of messages by cable or by any form of wireless apparatus. The provisions shall apply “mutatis mutandis” to the computation its profits, deemed to be derived from Nigeria as though the transmission of messages to places outside Nigeria were equivalent to the shipping or loading of passengers, mails, livestock or goods in Nigeria (CITA section 13).

### 3.4 Insurance Companies (CITA Section 14)

For non-life insurance companies, the profits on which tax may be imposed shall be ascertained thus:

Gross premiums plus interest and other income receivable;	xxx
Less any returned premium and premium paid on	(xx)
Reinsurers:	
Less reserve for unexpired risks at the end of the period:	(xx)
Add Reserve for unexpired risks at the beginning of the period	xx
Less actual losses settled during the period net of settlements	
By reinsurers	(xx)
Less other allowable expenses.	(xx)
Taxable income	

As regards Life Assurance Company, the company, the profits on which tax may be imposed shall be the investment income, less management expenses including commission. Any amount distributed as dividend from the actuarial revaluation of unexpired risks from any other revaluation shall be deemed to be a part of the profits of the company.

Not more than three months after an actuarial revaluation of the unexpired risks or any other revaluation has taken place, then company shall provide to the revenue service full particulars of the revaluation carried.

Careful note should be taken of the basis of computation of the assessable profits of non-life insurance business and that of a life insurance business, while in the former, there is reference to premium and investment incomes, reserves for unexpired risks and claims settlements, in the latter, the relevance is only to investment income, management expenses and commissions.

### Illustrations

Folake Insurance Nig. Plc., a company engaged in non-Life business has the following details of its transactions for the year ended 30 April, 1990.

Premium Received	₦
Dividend received (net)	1,350,000
Profit on sale of fixed assets	12,750
Reinsurance premium	5, 5004
Subscription as member of the Nigerian Insurance Association	345,000

Contribution to state education funds	15,000
Unexpired risk -1/5/89	275,000
- 30/4/90	
Claims	310,000
Amount recovered under reinsurance	120,000
Salary and other administrative expenses	75,000
Capital allowance were:	140,000
Initial allowance	
Annual allowances	40,000
Balancing charge	5,500

You are required to compute the tax payable by the company for 1991 year of assessment. (Assume companies rate of tax as 40%). (10 marks)  
ICAN past question

### **Suggested Solution 15-2**

Refer to the beginning of this paragraph for the provision of section 14 of CITA regarding the computation of chargeable profits of a non-life assurance company.

### **Folake Insurance Nig. Plc.**

#### **Computation Tax for 1991 Assessment Year**

	₦
Premiums Received	1,350,000
Dividend Received (Note i)	
Reinsurance premiums	(345,000)
Net Premium	1,005,000
Unexpired risks 30/4/90	(310,000)
Unexpired risks 1/5/89	275,000
Claims Settled	120,000
Less recovered under insurance	(75,000)
	(45,000)
Less: Allowable expenditure:	
Salaries and other admin Expenses	145,000
Subscription to NIA	5,000
Contributed to state education funds	15,000
	(165,000)

	760,000
Add balancing charge	
	5,500
	765,500
Deduct capital allowances	
Initial	40,000
Annual	78,000
Chargeable profit	(118,000)
	647,500)
Tax payable at 40% thereof	259,000

### Notes

- (i) Dividend income is franked investment income. It is not to be aggregated in arriving at total profits on which income tax will be computed.
- (ii) Contributed to state education funds is an allowable expenditure in accordance with the provision of section 21 CITA.

### 3.5 Non-Nigerian Insurance Companies

The above provisions of CITA section 14 also apply to non-Nigerian insurance companies. With regards to any of such companies having a permanent establishment in Nigeria, the applicable amounts shall be those arising from its Nigerian operations. Agency expenses in Nigeria and a fair proportion of the company's head office expenses are also allowable deductions.

In respect of a life assurance company where the profits accrue in part outside Nigeria, the assessable profits shall be that proportion of the total investment income of the company as the premium receivable in Nigeria bear to the total premiums receivable less the agency expenses in Nigeria and a fair proportion of the head office expenses of the company.

### 4.0 CONCLUSION

This unit discusses the concept of double taxation relief, especially where there is no double taxation agreement between a country and where there is a double taxation agreement in place.

The tax implications of mergers, acquisitions and takeovers, have been discussed. It was noted that the consent of the Inland Revenue service must



be obtained before any merger, take-over, transfer or restructuring of a trade or business carried on by a company, can take place.

Deferred taxation was considered and the need to make adequate provisions for the tax effect of timing difference was emphasised.

Finally, special businesses such as shipping, air transport and insurance were considered. The peculiarities with regards to determination of the sources/nature of the income/taxable profits of each area of business under CITA were also covered.

## **5.0 SUMMARY**

In this unit, we have enumerated the conditions for charging taxes on the profits of non-Nigerian companies which are engaged in shipping or air transport businesses. We stated the conditions governing taxation of the profits of Nigerian companies engaged in shipping or air transport businesses and listed the conditions governing taxation of the profits of companies engaged in the business of transmission of messages. Furthermore, we stated the conditions under which Nigerian and non-Nigerian companies engaged in insurance business would be charged tax.

In the next unit, we shall discuss petroleum profit tax.

## **6.0 TUTOR-MARKED ASSIGNMENT**

The student is expected to try his/her hands on the illustrations contained this unit and in other textbooks on taxation with a view to getting used to the procedures and steps used in computing the taxes for special businesses.

## **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 3     PETROLEUM PROFIT TAX**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Petroleum Operations
  - 3.2 Definitions as given in Petroleum Profits Tact Act (PPTA)
  - 3.3 Administration of Petroleum Profits Tax
  - 3.4 Nature and Classification of Income
  - 3.5 Ascertainment of Adjusted Profits and Imposition of Tax
  - 3.6 Allowable and Non-Allowable Deductions
  - 3.7 Treatment of Losses in Petroleum Profits Tax Computations
  - 3.8 Capital Allowance
  - 3.9 Concepts and Computations of Posted Prices
  - 3.10 Persons Chargeable
  - 3.11 Deduction of Tax at Source
  - 3.12 Double Taxation Arrangement (Section 56)
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we stated how a company can be Chargeability to Tax; stated the Persons Answerable on tax matters on behalf of a company; known the powers of the Revenue Service to appoint Directors as Agent for tax purposes; stated the conditions under which a Company in Liquidation shall pay its tax; understood that each Company appoints its Representative on Tax Matters; listed the Offences and Penalties; and discussed the Duty of Secrecy and Confidentiality.

In this unit, you will be introduced to another interesting topic: tax on special businesses.

## 2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define in the ordinary sense and as found in the petroleum profits tax fact of 'petroleum operations' and define capital allowance
- state how petroleum profits tax is administered
- discuss and classify income on petroleum operations
- determine how to ascertain adjusted profits and impose tax
- differentiate between allowable and non-allowable deductions
- describe the treatment of losses in petroleum profits tax computations
- discuss the concepts and computations of posted prices
- explain the concepts persons chargeable, deduction of tax at source and double taxation arrangement.

## 3.0 MAIN CONTENT

Company Income Tax Act (CITA) contains special provisions with regards to complete engaged in shipping or air transport business as well as those in insurance business. The provisions which are considered below are additional to the normal rules of allowable and disallowed expenditure in taxation practice.

### 3.1 Petroleum Operations

The oil industry has achieved great prominence in the Nigerian economic environment since the early seventies. Influence of oil and gas on the Nigerian economy today, cannot be overemphasised. The oil and gas industry accounts for over 90% of the country's foreign exchange earnings. It also plays a predominant role in the Gross National Product (GNP) index. It is in view of the importance that government attaches to oil exploration and production that the taxation of profits of gains of companies engaging in such operations is taxable under a separate tax law. The applicable law is the Petroleum Profits Tact Act (PPTA), which was first enacted in 1959 with retrospective effective date of 1 January, 1958. This principal act and all amendments thereto have been re-enacted as Chapter P13 of the laws of the Federation of Nigeria (LFN) 2004.

'Petroleum operations' as defined in the act essentially involves petroleum exploration, development, production and sale of crude oil and gas. There is no distinction in the act between associated and non-associated gas. All

activities of petroleum companies that to be taxed under PPTA are referred to as upstream operations. Those that not covered under the definition of “petroleum operations” are referred to as downstream operation. Examples of downstream operations are petroleum refining, petroleum marketing and gas utilisation projects. Companies engaged in downstream operations are subject to tax under the companies income Tax Act cap C21 LFN 2004.

### **SELF-ASSESSMENT EXERCISE**

..... is defined essentially as involving petroleum exploration, development, production and sale of crude oil and gas.

### **3.2 Definitions as given in Petroleum Profits Tact Act (PPTA)**

All terms relate to companies engaged in petroleum operations.

#### **Accounting period**

- (a) This is a period of one commencing on 1<sup>st</sup> January and ending on 31<sup>st</sup> December of the same year; or
- (b) Any shorter period commencing on the day the company first makes a sake or bulk disposal of chargeable oil under a programme of continuous production and sales, domestic, export or both, and ending on 31<sup>st</sup> December of the same year, or
- (c) Any period of less than a year being a period commencing on 1<sup>st</sup> January of any year and ending on the date in the same year, when the company ceases to be engaged in petroleum operations.

#### **Revenue service**

The Federal Inland Revenue Service

#### **Casing head petroleum spirit**

Any liquid hydrocarbons obtained in Nigeria from natural gas by separation or by any chemical or physical process but before the same has been refined or otherwise treated. Casing head petroleum spirit is further subdivided into two namely:

##### **(a) Chargeable natural gas**

Natural gas actually delivered by a company to the Nigerian National Petroleum Corporation under a Gas sales contract but does not include natural gas taken by or on behalf of the government of the Federation.

**(b) Chargeable oil**

Casing head petroleum spirit and crude oil won or obtained by a company from petroleum operations.

**Company**

Anybody corporate incorporated under law in force in Nigeria or elsewhere.

**Crude oil**

Any oil (other than oil extracted by destructive distillation from, coal bitumen sales, or other stratified deposits) won in Nigeria, wither in its natural state or after the extraction of water, sand or other foreign substance therefrom but before any such oil is redefined or other treated.

**Disposal or disposed**

In relation to chargeable oil owned by a company, disposal or disposed of connotes respectively;

- (a) Delivery, without sale, of chargeable oil to; and
- (b) Chargeable oil delivered, without sale to, a refinery or to an adjacent storage tank for refining by the company.

**G-Factor**

Gas projection cost adjustment factor.

**High Court**

The high court in Nigeria within whose jurisdiction is the place:

- (a) In relation to any offence under the PPTA act, where such offence is deemed to have occurred;
- (b) In relation to any suit for tax or appeal against an assessment of tax, where the tax return has been submitted or where the assessment of the tax was made as the case may be;
- (c) In relation to where the Revenue Service directs a company to keep proper books of accounts, in accordance with relevant provisions of the act, from where the direction was issued; and

- (d) In relation to any claim or other matter which is subject to appeal in like manner as an assessment where the claim or other matter was refused by the Revenue Service.

### **Intangible drilling cost**

All expenditure for labour, fuel, repairs, maintenance, hauling and supplies and materials (not being supplies and materials for well cement, casing or other well fixtures) which are for or incidental to drilling cleaning, deepening or completing wells or the preparation thereof incurred in respect of:

- (a) Determination of well locations, geological studies and topographical and geophysical surveys preparatory to drilling;
- (b) Drilling, shooting, testing and cleaning wells;
- (c) Cleaning, draining and leveling land, road-building and the laying of foundations;
- (d) Erection of rigs and tankage assembly and installation of pipelines and other plant and equipment required in the preparation of drilling of wells producing petroleum.

### **Liquefied natural gas**

Natural gas in its liquid state at approximately atmospheric pressure

### **Minister**

Minister charged with responsibility for matters relating to taxes on incomes and profits.

### **MMCF**

One million cubic feet

### **Natural gas**

Gas obtained in Nigeria from bore holes and wells consisting primarily of hydrocarbons.

### **Nigeria**

Includes the submarine areas beneath the territorial waters of Nigeria and the submarines areas beneath any other waters which are or at any time

shall in respect of mines and minerals become subject to the legislative competence of the National Assembly.

### **Non-productive rents**

The amount of any rent for which there is provision for its deduction from the amount of any royalties under oil prospecting license or oil mining lease, to the extent that such rent is not so deducted.

### **Oil mining lease**

A lease granted to a company under the minerals act, for the purpose of winning petroleum, or any assignment of such lease.

### **Oil prospecting license**

A license granted to a company under the minerals act, for the purpose of winning petroleum, or any assignment of such license.

### **Person**

Includes a company and any unincorporated body of persons

### **Petroleum**

Any mineral oil or relative hydrocarbon and natural gas existing in its natural condition in Nigeria, but does not include liquefied natural gas, coal, bitumen sales or other stratified deposits from which oil can be extracted by destructive distillation.

### **Petroleum operations**

The winning or obtaining and transportation of petroleum or chargeable oil in Nigeria by or on behalf of a company for its own account by any drilling, mining, extracting, or other like operations or process, not including refining at a refinery, in the course of a business carried on by the company engaged in such operations, and oil operations incidental thereto and any sale of or any disposal of chargeable oil by or on behalf of the company.

**Resident in Nigeria**

In relation to a company, this means a company, the control and management of the business of which are exercised in Nigeria.

**Royalties**

- a) The amount of any rent for which there is provision for its deduction from the amount of any royalties under an oil prospecting license or oil mining lease to the extent that such rent is so deducted; and
- b) The amount of any royalties' payable under any such licence or lease less any such rent deducted from those royalties.

**Concession**

This includes an oil exploration license, an oil prospecting license, an oil mining lease, any right, title or interest in or to petroleum oil in the ground and any option of acquiring any such right, title or interest.

**Lease**

This includes an agreement for a lease where the term to be covered by the lease has begun, any agreement for the letting or hiring out of asset, but does not include a mortgage, and all cognate expressions including "leasehold interest" shall be construed accordingly.

**3.3 Administration of Petroleum Profits Tax**

The administration of the petroleum profit tax act is under the charge and management of the Federal Inland Revenue Service. The revenue service may do all acts as may be deemed necessary and expedient for the assessment and collection of the tax and shall account for all amounts so collected in a manner to be prescribed to the federal minister of finance through its revenue service.

Whenever the FIRS consider it necessary with respect to any tax, it may acquire, hold and dispose of any property taken as security for or in satisfaction of any tax or of any judgment debt due in respect of any tax and shall account for any such property and the proceeds of sale thereof in a manner to be prescribed by the minister (section 3(b)).



The revenue service may sue and be sued in its official name (section 3(c)).

### **Delegation**

Subject to such conditions as the revenue service may specify, the revenue service may by notice in the federal gazette direct that any information return or documents required to be supplied, forwarded or given to the revenue service may be supplied to such other person whether within or without Nigeria as the revenue service may direct.

The revenue service may by notice in the federal gazette or in writing authorise any person within or without Nigeria to:

- (a) Perform or exercise, on behalf of the revenue service, any power or duty conferred upon the revenue service other than the powers or duties specified in the first schedule. And
- (b) Receive any notice or other document to be given, delivered or served upon the revenue service under or in consequence of the act or any subsidiary legislation made thereunder (section 3 (e)).

The power or duties specified in the first schedule that cannot be delegated by the revenue service is:

- (a) Powers and duties of the FIRS should be as stipulated in the FIRS act, 2007 section 3(b) with respect to any due.
- (b) The revenue service may acquire, hold and dispose of any property taken as security for or in satisfaction of any tax or of any judgement debt due in respect of any tax and shall account for any such property and the proceeds of the sale thereof.
- (c) Section 3(d) the revenue service may by notice in the federal gazette direct that any information, return or documents required to be supplied forwarded or given to the revenue service may be supplied to such other person as the revenue service may direct
- (d) Section 3(2) the revenue service may, from time to time, specify the form of returns, claims statement and notices under act.
- (e) Section 13 the revenue service powers under the artificial transaction provisions.
- (f) Section 29 the revenue service power to call for further information
- (g) Section 35 the revenue service powers to make assessments.

- (h) Section 46 the revenue service power to grant relief for error or mistake.
- (i) Section 49 the revenue service power to levy penalty for making incorrect account.
- (j) Section 50 the revenue power to levy fine in respect of false statements and returns; and
- (k) Section 53 the power of the revenue service to commence prosecution in respect of an offence.

### **Control by the minister**

In the exercise of the power and duties conferred upon it, the revenue service shall be subject to the authority, direction, and control of the federal minister of finance. Any written direction, order or instruction given by the minister after consultation with the chairman of the revenue service shall be carried out by the revenue service.

However, the minister shall not give any such direction etc. in respect of any particular company which would have the effect of requiring the Revenue Service to increase or decrease any assessment made or to be impose or any relief give to or defer the collection any tax, penalty or judgment debt due by such company or which would have the effect of altering the normal course of any preceding, whether civil or criminal relating either to the recovery of any tax or penalty or to an offence relating to the tax. Any act, matter or thing done by or with the authority of the revenue service in pursuance of the provisions of PPTA shall but be subject to challenge on the ground that such was not or was not proved to be in accordance with any direction, order or instruction given by the minister.

### **Significance and Execution of Powers (Section 4)**

- (a) Anything required to be done by the revenue service, in relation to the power or duties specified in the first scheduled to the act, may be signified under the hand of the chairman of the revenue of the revenue service, or of authorised by the revenue service who has been anything done or to be done by the revenue service signify from time to time, anything done or to be done by the revenue service respect of such powers or duties.
- (b) Any authorisation given by the revenue service under or by virtue of the act shall be signified under the hand of the chairman of the

revenue service unless such authority is notified in the federal gazette.

- (c) Subject to subsection (1) of this section, any notice or other document to given under the act shall be valid if:
  - (i) It is signed by the chairman of the revenue service or by any person authorised by him; or
  - (ii) Such notice or document is printed and the official name of the revenue service is duly printed or stamped thereon.
- (d) Every notice. Authorisation or other document purporting to be a notice, authorisation or other document duly given and signified, notified or bearing the official name of the revenue service, in accordance with the provisions of this section, shall be deemed to be so given and signified, notified or otherwise without further proof, until the contrary is shown.

#### **Duty of Confidentiality (Section 5)**

Every person having any official duty or being employed in the administration of the act shall regard and deal with all documents, information, returns, assessment lists and copies of such lists relating to the income, chargeable profits or items thereof of any company, as secret and confidential.

Every person who at any time communicates or attempts to communicate such information or anything contained in such documents, returns, list, or copies to any person;

- (c) Other than a person to whom he is authorised by the minister to communicate it; or
- (d) Otherwise than for the purpose of the act or any act or law, relating to a tax upon income, in force in any part of Nigeria; shall be guilty of an offence.

No employee of the Revenue service shall be required to produce in any court any return, document or assessment, or to be divulge or communicate to any court any matter or thing coming under his notice in the performance of his duties under the act except as may be necessary for the purpose of caring into effect the provisions of the act, or in order to institute a

prosecution, or in the course of a prosecution for any offence committed in relation to tax.

The obligation as to secrecy shall not prevent the disclosure of necessary information to the authorised officers of the government of such other country as might be necessary for double taxation relief purposes.

The Auditor-General of the federation or any other officer authorised by him may not be prevented from having access to such records or documents as may be necessary for the performance of his official duties. The Auditor-General or any such official shall be deemed to be a person employed in carrying out the provisions of the act for the purposes of secrecy.

### **Service of Notice (Section 7)**

Any notice to be served in pursuance of the provisions of the act can be served either personally or by registered post. Where a notice is sent by registered post, it shall be deemed to have been served on the day succeeding the day on which the addressee of the registered letter containing the notice would have been informed in the ordinary course of events that such registered letter is awaiting him at a post office. That a notice shall be deemed to have been served if the addressee proves that no notification informing him of the fact that the registered letter is awaiting him at a post office was left at the address given on such registered letter.

A notice to be served shall be addressed:

- (a) In the case of a company incorporated in Nigeria, to the registered office of the company; and
- (b) In the case of a company incorporated outside Nigeria either to the individual authorisation to accept service of process under the companies and Allied Matters Act at the address filed with the Registrar-General or to the registered office of the company wherever it may be situated.

Where service of any notice has prove impossible, the notice may be served by being left at the appropriate office or address as determined above, unless such address is a registered post office box number.

## SELF-ASSESSMENT EXERCISE

The administration of the petroleum profit tax act is under the charge and management of the .....

### 3.4 Nature and Classification of Income

The oil and gas industry is characterised by certain factors that are peculiar to the industry. One of these is the time lag (could be several years) between the time that an investment is made for exploratory activities and the time that the oil can be produced in commercial quantity and sold to generate income. There is the high risk and uncertainty of the results that will be obtained from exploration activities. The only conclusive evidence of the obtained availability of oil in any location can only be obtained by drilling. The risk is very high of not finding recoverable oil reserves or not finding such in commercial quantity in one out of forty exploratory wells. Other risks that are present in the oil and gas industry are: market risk; sovereign/political risk; partner risk; and taxation risk. All these would impact greatly on the investments and return on investment in the industry.

The very high return in the industry is to compensate for the very high risks. The industry deals in high volume of producing with all the advantages of economics of scale. Financial returns are usually sustained whenever there are large finds. Profitability can also be very high in periods of high oil prices as the situation was in the 3rd quarter of 2008 when oil prices reached an all time high of \$145 per barrel. The main sources of income of a petroleum producing company are:

- (a) Sale of crude oil: export and local (equity share)
- (b) Sale of gas: export and local (equity share)
- (c) Income from lifting and sale of NNPC equity crude

Other items of income, for example, interest income, would be earned from activities that are considered to be incidental to petroleum operations. Incidental income will be subject to petroleum profit tax. Some of the income that could be treated as incidental income is:

- (a) Ululate fees
- (b) Rentals
- (c) Management fees

- (d) Mineral property conveyance
- (e) Interest on fixed deposits.

Balancing charge on disposal of items of qualifying expenditure is also to be treated as incidental income in the computation of petroleum profits tax. (Gains or losses on their disposal are excluded from the petroleum profits tax computations).

Another point worthier of note in the determination of income in the oil and gas industry, is that oil produced is deemed sold when produced. As a result of this the sales value of crude oil produced can be taken to income immediately without waiting until the time of actual sales.

### **Development cost**

Development costs are incurred to obtain access to proved reserves and provide facilities for extracting, gathering, treating and storing the oil and gas. These costs are incurred after a decision has been taken to develop a field or reservoir, and include the following:

- (a) Drilling, equipping and testing development and production wells;
- (b) Production platforms, down hole and wellhead equipment, pipelines, production and initial treatment and storage facilities as well as utility and waste disposal systems; and
- (c) Improved recovery systems and equipment.

### **Production cost**

Production costs are the recurrent costs incurred in oil and gas production activities. Production involves lifting the oil and gas to the surface gathering, treating, field processing and storage. Production costs are usually determined to be all cost incurred from the maintenance of the wells and well heads to the storage facilities when the oil and gas are ready for export or delivery to a refinery.

Production cost are those incurred to operate and maintain a company's wells and related equipment and facilities, including depreciation, depletion and applicable operating costs of support equipment and facilities. Examples of production cost are:

- (a) Cost of personnel engaged in the operation of wells and related equipment and facilities
- (b) Repairs and maintenance of production facilities

- (c) Material, supplies, fuel consumed and services utilised in such operations; and
- (d) Royalties.

### **Support equipment and facilities costs**

Cost incurred on support equipment and facilities in oil and gas production activities, such as vehicles, repair shops, warehouses, supply points, camps, and divisional, district or field offices, aircraft and helicopters, safety and environmental facilities are usually accumulated and reallocated to the classes of cost identified above on some rational basis. For example, use of vehicles may be reallocated on kilometers, use of power house on the basis of wattage reading, and so on.

### **General costs**

Some costs incurred in a company's oil and gas producing activities do not always result in acquisition of an asset and therefore are usually charged to expense. Examples include geological and geophysical costs, the costs of carrying and retaining underdeveloped properties, and the cost of drilling those exploratory wells that do not result in proved reserves.

The cost of a company's well and related equipment and facilities and the costs of the related proved properties are usually amortised as the related oil and gas reserves are produced from the reserve. Depreciation, depletion, and amortisation of capitalised acquisition, exploration, and development cost also become part of the cost of oil and gas produced along with production (lifting) costs identified above.

Oil companies incur substantial cost in providing amenities for the communities where they operate. Such costs which do not have future benefits to the company are usually expensed. Oil companies also incur costs on such matters as corporate affairs, staff training and development.

## **3.5 Ascertainment of Adjusted Profits and Imposition of Tax**

This topic will be discussed under the following subtopics.

### **3.5.1 Imposition**

Section 8 of the PPTA levies tax on the profits of each accounting period of any company engaged in petroleum operations. Particular note should be taken of the fact that the basis period for any assessment year is on current

year basis. For example, assessment for the 1998 assessment year of a company that has been engaged in petroleum operating for several years will be based on the result of the accounting period of the company commencing from 1 January, 1998 and ending on 31 December, 1998. This is a major departure from the preceding year rule that is applicable in the taxation of individuals (under personal Income Tax Act and companies not engaged in petroleum operations (taxable under companies income tax act).

### **3.5.2 The Profit of an Accounting Period**

The profit of a company for an accounting period is computed as the aggregate of the following:

- (a) The proceeds of sale of all chargeable oil solid
- (b) The value of chargeable oil disposed of
- (c) The value of all chargeable natural gas; and
- (d) All income incident to and arising from one or more of its petroleum operations.

In respect of (b) above, the value to be used shall be the aggregate of:

- (i) Value of the chargeable oil as determined for royalty purposes
- (ii) The cost of extraction of that oil deducted in determining its value; and
- (iii) Any cost incurred by the company in transportation and storage of that oil between the field of production and the place of its disposal.

### **3.5.3 Adjusted Profit**

The adjusted profit of an accounting period shall be the profits of that period after the deductions of allowable expenses and any adjustments necessary to exclude the profits or loss attributable to transportation operation which is assessable under companies income tax act (CITA). The transportation operation referred to here, exclude the transportation between the field of production and the place of disposal of oil as referred to in the immediately preceding paragraph.

### **3.5.4 Assessable Profit (Section 14)**

The assessable profit shall be the adjusted profit of the period after adjusting for education tax and the effect of any loss relief available to the company.



### 3.5.5 Chargeable Profits (Section 18)

The chargeable profits shall be the assessable profits, less capital allowances. For this purpose the amount of capital allowances to be deducted is to be restricted to the lower of:

- (a) The amount computed; or
- (b) A sum equal to eighty-five percent of the assessable profits of the accounting period, less one hundred and seventy percent of the total amount of the deductions allowed as investment tax credit or petroleum investment allowance computed under the second schedule for that period. (Investment tax credit if the computation is for a company operating a production sharing contract as provided in the deep offshore and inland basin production sharing contract decree 9 of 1999 and petroleum investment allowance in other cases).

This restriction is in order to ensure that the tax chargeable on the company is not less than fifteen percent of the tax that would have been chargeable had no deduction been made for capital allowance (subsection 3 of section 18).

Capital allowance that cannot be utilised due to this restriction are to be carried less than forward to be aggregated with the capital allowance computed for the following accounting periods and subjected to similar restrictions in each of those accounting periods.

From the foregoing, the relationship between the terms profits, adjusted profit, assessable profit and chargeable profit can be stated as follows:

Profit for the period	xx
Deduct: allowable expenditures (section 10) (After necessary adjustment to eliminate	
Transportation operations expenses included)	(x)
Adjusted profit	x
Less: loss relief (section 14)	(x)
Assessable profit	xx
Deduct: Education tax	xx
Deduct capital allowance (as restricted) (section 15)	(x)
Chargeable profit	xx

### **3.5.6 Artificial Transactions (Section 13)**

- (1) Where the revenue service is of the opinion of:
  - (i) any disposition is not in fact given effect to, or
  - (ii) that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, the revenue service may be regard any such disposition or direct that such adjustment shall be made as respect as respect liability to tax ass it considers appropriate.

The effect of the revenue service's decision will be to counteract the reduction of liability to tax affected, or reduction which would otherwise be effected by the transaction. The company concerned shall be assessable accordingly. In this subsection, the expression "disposition" includes any trust, grant, covenant, agreement or arrangement.

- (2) The following transactions shall be artificial or fictitious; namely:
  - (i) transactions between persons, one of whom has control over the other
  - (ii) or between persons, both of whom are controlled by some other person; which, in the opinion of the revenue service, have not been made on the terms which might fairly have been expected to have been made by independent persons engaged in the same similar activities dealing with one another at arm's length. (Transactions that are not considered to have been carried out at arm's length shall be deemed to be artificial or fictitious).
- (3) A company in respect of which any direction is made under this section shall have a right of appeal in like manner as though such direction were an assessment.

## **3.6 Allowable and Non-Allowable Deductions**

### **3.6.1 Allowable Deductions (Section 10)**

All outgoings and expenses wholly, exclusively and necessarily incurred, whether within or outside or outside Nigeria, for the purpose of petroleum operations shall be deductible in computing the adjusting profit for any accounting period. Any outgoing or expense that falls under this definition

is an allowable deduction irrespective of whether or not such is specifically listed in section 10 of the act.

The following are specifically listed as allowable deductions in section 10 of the act:

- (a) Rents in respect of land or buildings occupied under an oil prospecting licence or an oil mining lease for disturbance of surface rights or for any other similar disturbance:
  - (i) All non-productive rents:
  - (ii) All royalties in respect of natural gas sold and actually delivered to the Nigerian National Petroleum Corporation (NNPC), or sold to any other buyer or customer or disposed of in any other commercial manner.
- (b) All royalties, the liabilities for which were incurred by the company during that period in respect of crude oil or of casing head petroleum spirit won in Nigeria. (Prior to 1995, only royalties in respect of exported crude oil were treated as allowable deductions, while that relating to local sales were tax offsets).
  - (i) All sums by way of customs or exercise duty or other-like charges levied in respect of machinery, equipment and other goods used in the company's petroleum operations.
- (c)
  - (i) Interest on money borrowed where the revenue service is satisfied that the interest was payable on the capital employed in carrying on petroleum operations.
  - (ii) All sums incurred by way of interest on any inter-company loans obtained under terms prevailing in the open market, that is, the London Inter-bank offer Rate.
- (d) Repairs and or renewals of premises, plant, machinery, implements, utensils, fixtures or articles employed for the purpose of carrying on petroleum operations.
- (e) Bad and doubtful debts proved to the satisfaction of the revenue service to have become bad or doubtful during the accounting period. The treatment is the same as in normal taxation practice.

- (f) (i) Any other expenditure, including tangible costs directly incurred in connection with drilling and appraisal of development well, but excluding an expenditure which is a qualifying expenditure for capital allowance purposes and any other provision of this section;
- (ii) Exploration and drilling costs including cost relating to the drilling of the two appraisal wells in a particular field, including expenditure in respect of cement, casing and well fixtures; and
- (iii) Where a deduction may be given under this section in respect of any such expenditure, that expenditure shall not be treated as qualifying drilling expenditure for the purpose of the second schedule.
- (g) Contribution to approval pension, provident, or other society, scheme or fund.
- (h) All sums by way of duty, customs and exercise duties, stamp duties, education tax, (amendment in decree No. 18 of 1998 included education tax with effect from 1/1/96) tax (other than PPT) or any other rate, fee or other like charges.
- (i) Such other deductions as may be prescribed by any rule made under the act.

### **3.6.2 Disallowable Expenditure (Section 11)**

Section 11; subsection 1, of the PPTA states the items that specifically disallowed from being deducted in arriving at the adjusted profit of an accounting period. These are:

- (a) Any disbursements or expenses not wholly and exclusively paid out or expended, or not wholly or exclusively incurred for petroleum operations purposes.
- (b) Any capital withdrawn or any sum employed or intended to be employed as capital.
- (c) Any capital employed in improvements as distinct from repairs.
- (d) Sums recoverable under an insurance or contract of indemnity.
- (e) Rent or cost of repairs to any premises or part of premises not incurred for petroleum operation.
- (f) Amounts incurred as income tax, profits or other similar tax whether charged within Nigeria or elsewhere.

- (g) Depreciation of any kind
- (h) Payment to unapproved provident, savings, widows, and orphans or other society, scheme or fund.
- (i) Any custom duty on goods (including articles or any other thing) imported by the company:
  - i) For resale or for personal consumption of employees of the company, or
  - ii) Where goods of the same quality to those to imported are produced in Nigeria and are available, at the time the imported goods were ordered by the company for sale to the public at prices less or equivalent to the cost to the company of imported goods.

### **3.7 Treatment of Losses in Petroleum Profits Tax Computations**

#### **3.7.1 Loss Relief (Section 14)**

To arrive at the assessable profits, there shall be deducted from the adjusted profits:

- (a) The amount of any loss incurred by the company during the previous accounting period; and
- (b) For a new company, the amount of any loss incurred during its first accounting period in its trade or business.

Losses that cannot be fully deducted in any one period can be carried forward to the next succeeding accounting periods until fully relieved. The four years time limit for the carry forward of trade loss under CITA and PITA is not applicable to losses incurred in petroleum operations as there is no provision in PPTA in that regard. Furthermore, the company has the right to defer the utilisation of any loss relief available to it. This is possible where within five months after the end of the accounting period, the company elects in writing not to deduct the amount of the loss or part thereof from the profit of the accounting period under consideration. The amount so deferred will be deducted from following years accounting profits unless the company makes a similar election in that following year.

## 3.8 Capital Allowance

### 3.8.1 Qualifying Expenditure

Qualifying expenditure means capital incurred in an accounting period, which is:

- (a) Incurred on plant, machinery or fixtures –“qualifying plant expenditure”
- (b) Incurred on pipelines and storage tanks –“qualifying pipelines and storage expenditure”
- (c) Incurred on the construction of buildings, structure or works of a permanent nature –“qualifying building expenditure”
- (d) “qualifying drilling expenditure” –incurred in
  - i) The acquisition of or rights in or over, petroleum deposits.
  - ii) Searching for or discovering and testing petroleum deposits, or winning access thereto, or
  - iii) The construction of any works or buildings which are likely to be of little or no value when the petroleum operations for which they were constructed ceased to be carried on.

Any sum that can be treated as an allowable expense in accordance with the provision of section 10 of the act cannot be treated as qualifying capital expenditure. Qualifying capital expenditure cannot be classified into more than one of the four heading above.

## 3.9 Concepts and Computations of Posted Prices

### 3.9.1 Posted Prices

Posted prices in relation to any crude oil exported from Nigeria by a company means the price free on board (f.o.b.) at the Nigeria port for crude oil of the gravity and quality in question which is from time to time established by the company after agreement with the government of Nigeria as to the procedure to be followed for the purpose as its posted price for Nigeria crude oil of that gravity and quality (section 21(5)).

#### Illustration 15-2

The crude oil exported from Nigeria by Marina Oil Limited in December 2008 was 30° API. The posted price advised by the Nigerian National

Petroleum Corporation (NNPC) is US\$45.50 for the crude stream with a standard API of 35°. What is the posted price for the crude oil exported by Marina Oil Limited?

### Suggested Solution 16-2

		\$
Posted price as advised by NNPC at 35° API		45.50
Standard API	35°	
Gravity of oil exported	(30°)	
Decrease in API from standard	5°	
Reduction in posted price	5° x \$0.03 (0.15)	

Reduction in posted price for the crude oil exported by the company 45.35  
Best of Judgment (BOJ) Assessment

Where for any accounting period of a company, the company has:

- (a) Failed to deliver accounts and particulars provided for in section 28 of the act within the time limited by that section or
- (b) Failed to comply with any notice given under the provisions of section 29 or 30 of the act within the time specified in such notice, or within any extended time provided for in section 32 of the act; and
- (c) The revenue service is of the opinion that such company is liable to pay tax.

The revenue service may estimate the amount of the tax to be paid by such company for that accounting period and make an assessment accordingly (BOJ assessment).

Such assessment shall not affect any liability otherwise incurred by such company by reason of its failure or neglect to deliver such accounts and particulars or to comply with such notices; and nothing in this subsection shall affect the right of the Revenue service to make any additional assessment under the provisions of section 34 of the act (section 33).

### 3.10 Persons Chargeable

Section 22 (1) of the act makes it an offence for any person (other than a company) to engage in petroleum operations with a view to sharing the profits arising from such operations.

It is therefore certain that PPT is payable only by companies.

Where companies are engaged in petroleum operations in partnership or in a joint venture under any scheme or arrangement, the minister may make rules modifying the provisions of the PPTA for the PPTA for the ascertainment of the tax to be charged and assessed upon each of the companies involved. The effect of any such rules shall not be impose a great burden of tax on any company engaged in such partnership or joint venture than the proportion of its share of the benefits there from.

### **3.10.1 Non-Resident Company (Section 23)**

A non-resident company engaged in petroleum operations shall be assessable and chargeable to tax as if it were resident either, directly or in the name of its manager, or in the name of any other person who is resident in Nigeria and employed in the management of the petroleum operations of the company.

The person in whose name a non-resident company is assessable chargeable to tax shall be answerable:

- (a) For all matters required to be done by virtue of the act for the assessment of the tax as might be required to be done by such non-resident company if it were resident in Nigeria, and
- (b) For paying any tax assessed and charged in the name of such person.

### **3.11 Deduction of Tax at Source**

Similar to the provision of section 59C CITA, section 51A has been inserted in PPTA by Decree No. 21 of 1991. The section provides for deduction of withholding tax from payments due to any company, partnership, or person, (whether or not resident in Nigeria) who provides petroleum operations services and related activities to a company carrying on petroleum operations in Nigeria.

The services and activities affected and the applicable rates are:

Nature of service or activity	Rate of withholding tax	
All aspects of building construction and Related activities	5%	5%
All types of contracts other than sale and Purchases of goods and property	5%	5%



Consultancy and professional service	10%	5%
Management services	10%	5%
Technical services	10%	5%
Commissions	10%	5%

Other relevant provisions of the subsidiary legislation are:

- (a) The deductions are not and should not be regarded as additional cost of contracts or services rendered and should therefore not be built into costs. They are deductions in lieu of tax.
- (b) A person who had deducted tax from such payments shall issue a receipt for the amount of tax deducted and a statement showing details prescribed in paragraph 4 below.
- (c) Such person making the remittance of the deduction made shall state the following information writing:
  - (i) Name and address of the person who suffered the tax deduction
  - (ii) Nature of activities or services in respect of which payments were made
  - (iv) Gross amount paid or payable
  - (v) Amount of tax deducted
  - (vi) Amount of tax remitted; and
  - (vii) Date of remittance.
- (d) For the purpose of final assessment, the individual beneficiary of such income that had suffered deduction of tax at source shall present the original receipt issued in respect of the tax deducted at source, to the relevant tax authority for security whenever a claim for tax credit is made.

### **3.12 Double Taxation Arrangement (Section 56)**

- (a) If the minister by order declares that arrangement specified in the order have been made with the government of any territory outside Nigeria with a view to affording relief from double taxation in relation to tax imposed under the provisions of the act and any tax of a similar character imposed by the laws of the territory, and that it is expedient that those arrangements should have effect, the arrangements shall have notwithstanding anything in any enactment.

- (b) The minister may make rules for carrying out the provisions of any arrangements having effect under this section.
- (c) An order made under the provisions of subsection (1) of this section may include provisions for relief from tax for accounting periods commencing or terminating before the making of the order and provisions as to income (which expression includes profits) which is not itself liable to double taxation.
- (d) where, before the publication of the act in the federal gazette upon enactment, any order has been made under the provisions of section 33 of the income tax act and the arrangements specified in that order, with any modifications, are expressed to apply to a tax in a territory outside Nigeria and to income tax in Nigeria and to any other taxes of a substantially similar character either imposed in that territory or Nigeria or imposed by either contracting party to any such arrangements after those arrangements came into force and:
  - (i) Such order was made before 1 January, 1958, then for the purpose of the act, that order shall be deemed to have been shall have effect, in Nigeria, as respects tax for any accounting period; or
  - (ii) Such order was made on a day after the year 1957, then, for the purposes of the act, that order shall be deemed to have been made under this section on that day and the arrangements specified therein shall have effect, in Nigeria, as respects tax for any accounting period beginning on or after the date when those arrangements come into force, and for the unexpired portion of any accounting period current at the date; and where any arrangements, to which this subsection applies, contain a provision for exchange of information with the minister as defined in section 2 of the income tax act, then the order, with respect to those arrangements, as deemed to provide for such exchange with the chairman of the revenue service as respects as respects tax.
- (e) The minister may by order replace or vary any order deemed to have been made under this section for the purpose of the act, without otherwise affecting such last mentioned order the purpose of any other act.

### 3.12.1 Relief for Double Taxation (Section 57)

- (a) The provisions of this section shall have effect where, under arrangements having effect under section 56 of the act, foreign tax payable in respect of any income in the territory with the government tax payable in respect of that income in Nigeria: and in this section the expression “foreign tax” means any tax in that territory which under the arrangements, is to be so allowed, and “income” “means that part of the profit of any accounting period which is liable to both tax and foreign tax before the deduction of any tax, foreign tax, to both tax and foreign tax, before the deduction of any tax, credit therefore or relief granted under subsection (6) of this section.
- (b) The amount of the credit admissible under the terms of any such arrangements shall be set off against the tax chargeable upon that company in respect of the income, and where that tax has been paid the amount of the credit may be repaid to that company or carried forward against the tax chargeable upon that company for any subsequent accounting period.
- (c) The credit for an accounting period shall not exceed whichever is the lower of the following amounts, that is to say:
  - i) The amount of the foreign tax payable on the income, or
  - ii) The amount of the difference between the tax chargeable under the act (before allowance of the credit under arrangements having effect under section 56 of the act) and the tax which would be so chargeable if the income were excluded in computing profits.
- (d) Without prejudice to the provisions of subsection (3) of this section, the total credit to be allowed to a company for any accounting period, if no such credit had been allowed.
- (e) Where the income includes a dividend and under the arrangements foreign tax not chargeable directly or by deduction in respect of the dividend, is to be taken into account in considering is any, and if so what credit is to be given against tax in respect of the dividend. The amount of the income shall be increased by the amount of the foreign tax not so chargeable, which falls to be taken into account in computing the amount of the credit.

- (f) Where the amount of the foreign attributable to the income exceeds the credit therefore computed under subsection (3) of this section, then the amount of the amount that income to be included in computing profits for any purpose of the act other than that of income, increased by the amount of the credit therefore after deduction of the foreign tax.
- (g) Where:
- i) The arrangements provide, in relation to dividends of some classes, but not in relation to dividends of other classes, that foreign tax not chargeable directly or by deduction in respect of dividends, is to be taken into account in considering, if any, and if so, what credit is to be given against tax in respect of the dividend; and
  - ii) A dividend is paid which is not of a class in relation to which the arrangements so provide, then, if the dividend is paid to a company which controls, directly or indirectly, not less than half of the voting power in the company paying the dividend of a class in relation to which the arrangement so provide.
- (h) Any claim for an allowance by way of credit shall be made not later than three years after of the accounting period, and in the event of any dispute as to the amount allowable the revenue service shall give to the claimant notice of refusal to admit the claim which shall be subject to appeal in like manner as an assessment.
- (i) Where the amount of credit given under the arrangement is rendered excessive or insufficient by reason of any adjustment of the amount of any tax payable either in Nigeria or elsewhere, nothing in the act limiting the time for the making of assessment or claims for repayment of tax shall apply to any assessment or claim to which the adjustment give rise, being an assessment or claim made not later than three years from the time when all such assessments, adjustments and other determinations have been made, whether in Nigeria or elsewhere, as are material in determining whether any and if so what, credit falls to be given.
- (j) Where a company is not resident in Nigeria throughout an accounting period, no credit shall be admitted in respect of any income included in profits of that company for that period.

#### **4.0 CONCLUSION**

We note that from the discussion in this unit that the oil industry has achieved great prominence in the Nigerian economic environment since the early seventies. We also noted that the oil and gas industry not only accounts for over 90% of the country's foreign exchange earnings, but also plays a predominant role in the Gross National Product (GNP) index.

It is in view of the importance that government attaches to oil exploration and production that the taxation on profits or gains of companies engaged in such operations are taxable under a separate tax law. This significance in the operations of the oil and gas sector led to the enactment of the Petroleum Profits Tact Act (PPTA), which was first enacted in 1959 with retrospective effective date of 1 January, 1958. This principal act and all amendments thereto have been re-enacted as Chapter P13 of the Laws of the Federation of Nigeria (LFN) 2004.

We have discussed very extensively petroleum operations in Nigeria and how profit or gain is administered, classification of income on petroleum operations, etc.

#### **5.0 SUMMARY**

In this unit, we have defined in the 'petroleum operations' and capital allowance. We stated how petroleum profits tax is administered discussed and classified income on petroleum operations and determined how to ascertain adjusted profits and impose tax. We also differentiated between allowable and non-allowable deductions and described the treatment of losses in petroleum profits tax computations. Moreover, we discussed the concepts and computations of posted prices. Lastly, explained the concepts persons chargeable, deduction of tax at source and double taxation arrangement.

In the next unit, we shall discuss stamp duties.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. What is 'petroleum operations' and define capital allowance?
2. How is petroleum profits tax administered?
3. Discuss briefly and classify income of petroleum operations.
4. Differentiate between allowable and non-allowable deductions.
5. Describe how to treat losses in petroleum profits tax computations?
6. Write short notes on the following:
  - Concepts and computations of posted prices
  - Persons chargeable
  - Deduction of tax at source; and
  - Double taxation arrangement.

## **7.0 REFERENCES/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 4     STAMP DUTIES**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Stamp Duty
  - 3.2 Ad Valorem
  - 3.3 The Administration of Stamp Duty
  - 3.4 Stamping and Collection of Duties on Corporation Instrument
  - 3.5 Mode of Calculating Ad Valorem
  - 3.6 Stamping of Instrument after Execution
  - 3.7 Method of Stamping
  - 3.8 Improper Stamping
  - 3.9 Territorial Limits
  - 3.10 General Provision on Instrument
  - 3.11 Useful Definitions
  - 3.12 Exemption from Stamp Duties
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we defined in the 'Petroleum Operations' and define capital allowance; stated how Petroleum Profits Tax is administered; discussed and classified income on petroleum operations; determined how to ascertain Adjusted Profits and Impose Tax; differentiated between Allowable and Non-Allowable Deductions; described the treatment of Losses in Petroleum Profits Tax Computations; discussed the Concepts and Computations of Posted Prices; explained the concepts Persons Chargeable, Deduction of Tax at Source and Double Taxation Arrangement.

In this unit, we shall discuss stamp duties.

## 2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define stamp duty
- define ad valorem
- briefly discuss the administration of stamp duty
- explain how stamping and collection of duties on corporation instrument is carried out;
- state the mode of calculating ad valorem
- describe the stamping of instrument after execution
- describe the method of stamping
- describe what is meant by improper stamping
- define territorial limits
- list the general provision on instrument
- list the exemption from stamp duties.

## 3.0 MAIN CONTENT

### 3.1 Stamp Duties

Stamp duties basically on instruments (defined to include every written document). The duties are either specific (fixed) or Ad valorem. It is important to stamp instruments, otherwise, such instrument will not, except in criminal proceedings, be given/admitted in evidence, or be available for any purpose whatsoever, in a claim for title or rights. Stamp duties are governed by stamp duties act cap 58, LFN 2004, which provides for the levying of stamp duties on certain documents and matters specified in the act with effective date of 1 April, 1993.

#### Forms of Stamp Duties

##### Specific/Fixed

These are duties that do not vary with the value of the consideration on the document that is subject to the stamp. In other words, the same duty is payable irrespective of the value on the instrument.

Instruments that attract fixed duties include:

- (a) Deeds of assignment
- (b) Mortgages



- (c) Insurance policy (non-life)
- (d) Debenture trust deeds
- (e) Proxy forms
- (f) Bank notes
- (g) Cheque leaves.

### **SELF-ASSESSMENT EXERCISE**

- i. Stamp duty is defined as .....
- ii. Deeds of assignment, mortgages, non-life insurance policies etc. are some of the instruments that attract .....

### **3.2 Ad Valorem**

Ad valorem means “as per value”. There are duties that vary with the value of the consideration on the document that is subject to the stamp. Instruments that attract Ad valorem Duties include:

- (a) Bills of exchange
- (b) Property valuation reports
- (c) Memorandum and articles of association of companies
- (d) Promissory notes
- (e) Lease documents conveyance of sale
- (f) Marketable securities
- (g) Policy of life insurance.

### **SELF-ASSESSMENT EXERCISE**

Ad Valorem means .....

### **3.3 The Administration of Stamp Duty**

Stamp duty is managed by the commissioners for stamp duties. The commissioner for stamp duties determines the appropriate duty by adjudication. As the administrative head of the stamp duties matters as in the act, the commissioner has the following responsibilities:

- (a) Custodian of the stamping instruments, e.g. dies, adhesive stamps, postage stamps, etc.
- (b) Adjudicate/assess the instruments
- (c) Embossing/stamping the instruments with the appropriate die or stamp; and

- (d) Impose penalties where applicable.

An appeal lies from the decision of the commissioners of stamp duties to the high court, with rights of appeal as for ordinary tax cases.

### **3.4 Stamping and Collection of Duties on Corporation Instrument**

Stamping rates vary from both instrument to instrument and the duties are collectable by both the Federal Inland Revenue service and the states internal Revenue services.

The federal government through Federal Inland Revenue Services is the only competent authority to impose, charge and collect duties upon instruments specified in the schedule to the act if such instruments relate to matters executed between a company and individual, group or body of individuals. The state governments through state internal revenue service shall collect duties in respect of instruments executed between persons or individuals at such rate to be imposed or charged as may be agreed with the federal government.

#### **SELF-ASSESSMENT EXERCISE**

FIRS is the only competent authority to impose, charge and collect duties upon .....

### **3.5 Mode of Calculating Ad Valorem Duty**

Where an instrument is charged with ad valorem duty in respect of:

- (a) Any money in any foreign currency, or
- (b) Any stock or marketable security, the duty shall be calculated on the value, on the day of the date of the instrument, of the money in United States dollars, according to the current rate of exchange, or of the stock or security, according to the average price thereof.

Where an instrument contains a statement of current rate of exchange, or average rate exchange, or average price, as the case may require, and is stamped in accordance with that statement, it shall, so far as regards the subject matter of the statement is untrue, and that the instrument is in fact insufficiently stamped.

### **3.6 Stamping of Instruments after Execution**

Any unstamped or insufficiently stamped instrument may be stamped with an impressed stamp at any time within forty (40) days from the first execution thereof, upon payment of the duty or unpaid duty only, but after that time, the said instrument may only be stamped upon payment of the unpaid duty and penalty of twenty naira (N20), and also by way of further penalty, where the unpaid duty exceeds twenty naira, on interest on such duty, at the rate of ten naira per annum, from the day upon which the instrument was first executed up to the time when the amount of interest is equal to the unpaid duty.

### **3.7 Method of Stamping**

Stamps are either impressed (with dies) or adhesive stamps (using gum or glue). Except where express directive is issued to the contrary, all stamp duties must be denoted by impressed/embossed stamp (ordinarily red in colour).

### **3.8 Improper Stamping**

Where an instrument is not stamped, it is nevertheless effective. However, the stamp duties act provides some sanctions for improper stamping or no stamping at all:

- (a) Such instrument is not admissible whether directly or as a collateral, neither is it sufficient as a secondary evidence admissible in any court proceedings;
- (b) Cross examination over an unstamped/improperly stamped document is not allowed in any court proceedings; and
- (c) An instrument which is not duly stamped in accordance with existing law at the time of first execution, shall not except in criminal proceedings, be given in evidence or be available for any purpose whatsoever.

### **3.9 Territorial Limits**

Section 23(4) of the act provides that any unstamped or insufficiently stamped instrument which has been first executed at any place outside Nigeria may be stamped, at any time within thirty days after it has been first received in Nigeria, on payment of the unpaid duty only.

### **3.10 General Provision on Instrument**

The duties to be charged upon the several instruments specified in the schedule to the act are the several duties set out in the said schedule. The duties charged are accounted for in a manner prescribed by the Minister after consultation with the Governors of the state.

### **3.11 Useful Definitions**

Some useful definitions relating to stamp duties are:

“Accountant – General” means the Accountant-General of the Federation;  
“Commissioner” – Means a Commissioner of stamped duties appointed as hereinafter provided.

“Company” includes all legal entity, banks and other financial institution.

“Die” includes may plate, too, or implement whatever used under the direction of Minister of Finance and Economic Development of his counterpart in the state, as the case may be, for expressing or denoting any duty, or rate of duty or the fact that any duty or penalty has been paid, or that an instrument is duly stamped, or is not chargeable with any duty, or for denoting any fee, and also any part of any such plate, type, tool or implement.

“Duty” means any stamp duty for the time being chargeable under this or any other act and also includes any fee chargeable hereunder.

“Executed” and “Execution” with reference to instruments not under seal, mean signed and signature.

“Government” includes the government of the federation or of a state and the department thereof, local government council, and an officer acting in his official capacity on behalf of the government area, and not on behalf of the federation or a state or any department, and not on behalf of a private person.

“Instrument” includes every written document.

“Marketable security” includes a security of such description as to be capable of being sold in any stock market.

“Material” includes very sort of material upon which words or figures can be expressed.

“Money” includes all sums expressed in naira or in any foreign currency.

“Stamp” means as well a stamp impressed by means of a die as an adhesive stamp for denoting any duty or fee.

“Stamped” with reference to instruments and material, applies as well to instruments and material impressed with stamps by means of a die as to instruments and material having adhesive stamps affixed thereto.

“Stock” includes any share in any stock transferable at the Central Bank of Nigeria, promissory notes, and any share in the stocks or funds of any foreign state or government, or in the capital stock or funded debt of any local authority, corporation, company or society in Nigeria or foreign corporation, company, or society.

“Write”, “Written” and “Writing” includes every mode in which words or figures can be expressed upon material.

### **3.12 Exemption from Stamp Duties**

The following are exempted from stamp duties:

- (a) Treaties/agreement – entered into between the federal government and any other foreign governments or foreign private corporations/international organisations
- (b) Liquidation sales/transactions – any property sold by a liquidator
- (c) Company reconstructions and amalgamations – instruments on reconstructions and amalgamations such as conveyance, transfer or sale of property, assigning of debts whether secured or not;
- (d) Receipts issued for the payment of any government taxes, duties or levies; or
- (e) Instrument providing for penal rent in the nature of a penal rent.

## **4.0 CONCLUSION**

Stamp duties under duties Act Cap S8 LFN 2004 is the focus of this unit. It is concerned with the administration, stamping, collection, mode of calculation and various instruments on which duties are payable to either Federal Inland Revenue Services or states Internal Revenue Services.

The unit also mentions the form of stamp duties, such as specific/fixed and ad valorem together with items exempted from stamp duties.

Computer is used to assist in tax planning and management.

## **5.0 SUMMARY**

In this unit, we have defined stamp duty, territorial limits and ad valorem. We briefly discussed the administration of stamp duty and explained how stamping and collection of duties on corporation instrument is carried out. Also, we stated the mode of calculating ad valorem and described the stamping of instrument after execution, method of stamping and what is meant by improper stamping. We listed the general provision on instrument and gave some useful definitions. Finally, we listed the exemption from stamp duties.

In the next unit, we shall look into the topic, tax planning and tax management.

## **6.0 TUTOR-MARKED ASSIGNMENT**

1. How would you differentiate between stamp duty and ad valorem?
2. How is stamp duty administered?
3. What is the mode of calculating ad valorem?
4. Explain the concept 'stamping of instrument after execution'.
5. Define territorial limits. List the exemption from stamp duties.

## **7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 5      TAX PLANNING AND TAX MANAGEMENT**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Tax Planning and Tax Management
  - 3.2 Spreadsheet Application
  - 3.3 Areas of Tax of Planning using Electronics Spreadsheet
  - 3.4 Data Referencing
  - 3.5 Tax Model Computation
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

In the last unit, we defined stamp duty; defined ad valorem; briefly discussed the administration of stamp duty; explained how stamping and collection of duties on corporation instrument is carried out; stated the mode of calculating ad valorem; described the stamping of instrument after execution; described the method of stamping; described what is meant by improper stamping; defined territorial limits; listed the general provision on instrument; understood some useful definitions; and listed the exemption from stamp duties.

In this unit, we shall look into the topic, tax planning and tax management.

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- define spreadsheet application and discuss the step by step ways of imputing data into the spreadsheet
- list areas of tax planning where spreadsheet is used
- define data referencing and the types of data referencing available
- describe the step by step ways of tax model computation.

### **3.0 MAIN CONTENT**

#### **3.1 Tax Planning and Tax Management**

Tax planning and tax management are increasingly becoming a complex activity as businesses grow and organisations expand both in scope of operations and physical size. Given the amount of data that need to be analysed in order to asses and compute tax liabilities, it has become imperative that both tax institutions and companies do deploy computer programs in order to automate tax planning and administration duties. In the light of the above, this unit will explore areas of tax planning and management requiring the application of computers especially the use of spreadsheet to generate tax models.

#### **3.2 Spreadsheet Application**

##### **(a) Electronic spreadsheet – an introduction**

A spreadsheet is a computer simulation program that simulates a paper worksheet; it displays multiple cells that together make up a grid consisting of rows and column, each cell containing either alphanumeric or numeric values. A spreadsheet cell may alternatively contain a formula that defines how the contents of any cell are to be calculated from the contents of any other cell (or combination of cells) each time any cell is update. Spreadsheets are frequently used for financial information modeling because of their ability to re-calculate the entire sheet automatically after a change to a single cell is made.

The related term spreadmart describes the situation that occurs when one or more business analysts develop a system of linked spreadsheets to perform a business analysis, and then grow it to a size and degree of complexity that makes it nearly impossible to maintain. Re-implementing the analysis using datamart architecture often improves both the reliability of the analysis and its maintainability.

Visicaic is usually considered the first electronic spreadsheet (although this has been challenged), and it helped turn the Apple II computer into a success and greatly assisted in their widespread application. Lotus 1-2-3 was the leading spreadsheet when DOS was the dominant operating system. Excel is now considered to have the largest market share on the Window and Macintosh platforms.



**(b) Entering data**

Cells consist of three packages: labels, value and formulas, Labels (alpha character) are the text headings, or titles, that describes what the numbers represents. Values are the numbers that perform calculations on. Platform the calculations by manipulating values to produce a result.

- i) To enter data into a cell, place the cursor on the required cell;
- ii) Type your country (you will be in edit mode)
- iii) Press [Enter] or click Enter on the Formula bar.

**(c) Enter data in a range of cells**

If you do a lot of data entry and do not like navigating to the beginning of the next column or row each time you enter another record of information, there is an easier way.

- i) First, select the range of cells for which you will be entering data
- ii) When you begin typing, your entry will be entered into the active cell.
- iii) To move from cell to cell within the selected range, use the following keys to remain within the selected range.
  - [Tab] to move to the right
  - Shift [Tab] to move left
  - [Enter] to go down a column
  - [Shift] [Enter] to move up

When you come to the end of a long row or column and need to move back to the beginning of the next, just press [Tab] or [Enter], when you reach the end of the range, press [Tab] or [Enter] and you will return to the beginning of the selection.

**Labels**

Labels can be any text that contains at least one alpha character, it can be combined with numbers, as long as at least one letter is included, Excel will consider this entry a label since on calculations can be perfumed on alpha characters.

At times, you may want to use numbers as text label. An example may be you compiling data from the past several years and need to label your

columns, with the year (e.g. '2008'). If you are using Autosum to sum the column, this entry is of the column. To avoid this, change the cell format to a text label instead of a value.

The easy way to do this is to type an apostrophe before the numbers (e.g. '2008'). This will force the format to be text. Do not worry; the apostrophe will be hidden from view in the spreadsheet, although it is visible in the formula Bar.

## **Values**

Excel considers an entry to be a value if it consists of only numbers, no alphanumeric characters, unless formatted otherwise as mentioned above.

## **Formulas**

A formula is an equation that performs operation on values. Formulas can perform mathematical operations, such as addition and multiplication, or they can compare worksheet values or join text formulas can refer to other cells on the same worksheet, cells on other sheets in the same workbook, or cells for Excel to calculate the correct results. Misplaced punctuation and incorrect spelling will result in an incorrect calculation or error message.

A formula in Microsoft Excel always begins with an equal sign (=). The equal sign tells Excel that the succeeding characters constitute a formula. Following the equal sign are the elements to be calculated (the "operand"), which are separated by mathematical operators. Each operand can be a value that does not change (a constant), a cell or range reference, a label, a name, or a worksheet function. Excel calculates the formula from left to right, according to a specific order for each operator in the formula. You can change the order of operations by using parenthesis.

Excel over the years has become a popular brand of electronics spreadsheet for business and home use. This may have been due to the aggressive marketing style of Microsoft, as each office suite of program incorporate the excel program and other related office programs.

### **3.3 Areas of Tax Planning using Electronics Spreadsheet**

This will be discussed under the following subtopics.

### 3.3.1 Personal Income Tax Model

The objectives of this section are to act as our guide in the hands-on exercise on the model used in the computation of personal income Tax (PAYE). However, we shall refresh our understanding of the following functions in the Microsoft Excel which shall be used in the computation.

### 3.3.2 Understanding Excel Function

Before using Excel spreadsheet in tax computations, one has to understand some basic principles and concepts of the software discussed below:

- (a) Referencing
  - (i) Relative
  - (ii) Partial (column or row)
  - (iii) Absolute
- (b) Creating of view
- (c) Use of IF function
- (d) Excel comparison
- (e) Naming function.

### 3.3.4 Defining Names for Columns

You can create names for columns that can be used for natural language formulas. Steps to create a named range are:

- (a) Select the range of cells you want to name, including the row or columns labels.
- (b) Select define option from the Name submenu on the insert menu

The Define Name dialog box is displayed with the name of column in the Names in workbook option (refer below).

- (c) Click on the Add button to add the name
- (d) The range of cells to which the name refers to is displayed in the Refers to field.
- (e) You can select another range of cells by clicking on the collapse button in the 'refers to' field. The collapse button provides a larger view of the worksheet so that you are able to view the complete worksheet while selecting a range of cells.
- (f) Click on the OK button.

### 3.3.5 Hide and Unhide

Let us find out how to hide columns and rows in an Excel worksheet. The steps to hide columns or rows in Excel are:

- i) Select the columns/rows that to hide
- ii) Right click and select the Hide option from the shortcut menu.

All the selected columns and rows are hidden.

- i) Select the columns/rows adjacent to the hidden columns/rows
- ii) Right click and select the Unhide option from the shortcut menu.

The hidden columns/rows are displayed.

### 3.3.6 Need for Views

If you have hidden a number of rows or columns, un-hiding all those columns or rows each time is a time-consuming activity. You can create views to solve this problem. Views will give you faster access to any specific set of rows or columns and their prints settings. It is also possible to have different set of print settings. Let us find out more about views.

### 3.3.7 Create Views

Views are a set of display and print setting that you can name and apply in a workbook. You can create more than one view of the same workbook. Creating a view will help the user to view only those rows and columns that relevant to him.

A user created a view called footwear Daily Report that contains all the rows and columns of the worksheet. Later, he creates a view called, Footwear Weekly Report that contains only the S. no, items, unit price, the user to switch between the daily the daily and weekly reports.

Let us see how to create the views.

The steps to create a view are:

- (a) Click on Customer view option, on the View Menu

The custom views dialog box is displayed.

- (b) Click on the Add button to create a view

The Add view dialog box is displayed (refer to figure 3.4)

- (i) Type the name of the view in the Name field

The “include in view” area, contains two options:

- Print settings –Allows you to save the currently selected printing settings of the worksheet.
- Hidden rows, columns and filter settings –Allows you to save these options of the worksheet. By default, both these options are selected.

- (ii) Click on the OK button

The steps to create a view that contains only specific rows and columns are:

- Hide the specific columns/rows
- Create a view with these settings.

Let us see how you can see a particular view. The steps to see a particular view are:

- (a) Click on the custom views option on the view menu.

The custom views dialog box is displayed

- Select a view from the list of views in the views option
- Click on the show button.

### **3.4 Data Referencing**

#### **(i) Cell referencing**

A referencing is the address of a cell or a range of cells in a worksheet. For example, A1 is the reference to the cell in row 1 and column A. by using cell referencing; you can refer to the data of various cells, in a formula. You can refer to a complete column in a worksheet by referring to it by using the reference to the column. For example, to refer to the column B type

B:B. you can also refer to cells in other worksheets. If you refer to cells in other workbooks, the referencing is called external referencing.

Depending on the task you want to perform, Excel offers three types of cell referencing techniques:

- Relative Referencing
- Absolute Referencing
- 3-D Referencing

Let us find out more about each one of them in detail.

## **(ii) Relative referencing**

Relative referencing is a reference to the cells in a formula based on the position of the cell that contains the formula. By default, Excel uses relative referencing.

## **(iii) Absolute referencing**

By using absolute referencing, you can refer to a particular cell in a formula regardless to the position of the cell that contains the formula. If you want to refer to a cell by using absolute referencing precede the name of the column and row with a dollar (\$) sign. For example, \$H\$5 means an absolute reference to cell H5.

You can also use mixed reference by placing the \$ sign before the column name or the row number. For example, \$5H means that the column has to be absolute and the row is relative and H5\$ means the row is absolute and the column is relative.

## **(iv) 3-D referencing**

You can use 3-D referencing to refer to the same address of a cell or range of cells in multiple worksheets in a workbook. A 3-D reference includes the cell or range reference preceded by a range of worksheet names.

## **(v) Advanced functions**

### **(a) IF**

The IF function is used for testing values and formulas. It takes certain values that are called arguments.

These are:

- Logical test –is an expression that evaluates to either TRUE or False.
- Value if true –us the value that is returned if logical test evaluates to TRUE. It can also be another formula.
- Value if false –is the value that is returned if logical test evaluates to FALSE. It can be another formula.

### **SELF-ASSESSMENT EXERCISE**

- i. Cell referencing is .....
- ii. Relative referencing is .....
- iii. Absolute referencing means .....
- iv. 3-D referencing is defined as .....
- v. What is data referencing?

## **3.5 Tax Model Computation**

### **(a) Step by step a PAYE**

- i) Obtain or create the salary file having all the necessary column; e.g. Basic pay, partially taxable income, and fully taxable income and errors total earned income
- ii) Identify all the partially taxable income and their limit
- iii) Determine the total taxable income
- iv) Determine the total personal relief, Note this is broken down into two;
  - General Relief;
  - Additional for income
- v) Determine your taxable income
- vi) Compute the tax liability
- vii) Compute tax payable i.e. including Min. tax; and
- viii) You may create a view to see specific group of details e.g. gross pay and tax liability, etc.

### **Workings**

#### **(a) Computation of taxable allowance**

- Ascertain what is the maximum allowed
- Use the IF logic function to compare amount earned and maximum allowed to find the tax payables.

## (b) Computation of reliefs

- General –taxable income x 20% + N5,000 + N10,000 + N4,000
- Disable Relief –The lower of N3, 000 & 20% of taxable income using IF function.

## (c) Tax liability

Use the IF function to compare taxable income with the tax rate schedule e.g.

- 1<sup>st</sup> 30,000 @ 5%
- If (Taxable Income > 30,000, 30,000 x 5%, taxable income x 5%)
- Next 30,000 @ 10%
- If (Taxable Income > 60,000, 30,000 x 10%)
- (Taxable Income -1<sup>st</sup> 30,000) x 10%

## (d) Computation of tax payable

Use the IF function to determine if taxable income is less than zero (0). Compute 0.5% of Total Taxable Income, or else our tax liability. See the excel table on page 384 for a demonstration of the above steps.

**4.0 CONCLUSION**

We note from the unit that tax planning and tax management are increasingly becoming a complex activity as businesses grow and organisations expand both in scope of operations and physical size. We also note that given the amount of data that need to be analysed in order to asses and compute tax liabilities, it has become imperative that both tax institutions and companies do deploy computer programs in order to automate tax planning and administration duties.

**5.0 SUMMARY**

In this unit, we defined spreadsheet application and discuss the step by step ways of imputing data into the spreadsheet. We listed areas of tax planning where spreadsheet is used. We defined data referencing and the types of data referencing available and also described the step by step ways of tax model computation.



**6.0 TUTOR-MARKED ASSIGNMENT**

1. What is spreadsheet application? List the step by step ways of imputing data into spreadsheet in tax planning and tax management.
2. List the areas of tax planning where spreadsheet is used to input data.
3. List and briefly explain the types of data referencing that you know.
4. What is tax model computation?

**7.0 REFERENCE/FURTHER READING**

ICAN Study Pack (2011).

## **UNIT 6 PIONEER INDUSTRIES**

### **CONTENTS**

- 1.0 Introduction
- 2.0 Objectives
- 3.0 Main Content
  - 3.1 Pioneer Conditions
  - 3.2 Application for Pioneer Status
  - 3.3 Certification of Qualifying Capital Expenditure
  - 3.4 Cancellation of Pioneer Certificate
  - 3.5 Income Tax Relief and Losses
  - 3.6 Taxable Profits, Exempted Profit and Dividends
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

### **1.0 INTRODUCTION**

A company is an organisation (other than a private company) limited and incorporated and registered in Nigeria and resident in Nigeria. A pioneer company is a company certified by any pioneer certificate to be a pioneer company. The pioneer industry represents any trade or business of the kind included in any list of pioneer industries published in the gazette.

The gazette is the federal gazette and includes the gazette of any state in the federation. One of the investments in countries available to industries in Nigeria is that under the industrial development (income tax relief) act which grants tax holidays to companies in the industries that meet the conditions of being designated pioneer industries.

The tax holiday is usually for an initial period of three years but can be extended for an additional two years maximum

### **2.0 OBJECTIVES**

At the end of this unit, you should be able to:

- define pioneer industry
- state the content of an application of any company requesting for a pioneer certificate

- state the procedure of certifying the amount of qualifying capital expenditure
- state reasons that could necessitate the cancellation of pioneer certificate
- explain income tax relief and losses incurred within the tax relief period
- explain taxable profit, exempted profit and dividend distributed from exempted profits.

### **3.0 MAIN CONTENT**

#### **3.1 Pioneer Conditions**

The national council of ministers (the council) may declare industries as pioneer products where the council is satisfied that:

- any industry is not being carried on in Nigeria on a scale suitable to the economic requirements of Nigeria or at all, or
- there are favorable prospectus of further development in Nigeria of any industry; or
- it is exempted in the public interest to encourage the development or establishment of any industry In Nigeria by declaring the industry to be pioneer industry and any product of the industry to be a pioneer product.

A company that wishes to engage in an industry or manufacture products which have not been designated pioneer may submit an application for the industry to be included in the list of pioneer industries and its products are included in the list of pioneer product. A successful application in either case is issued with a pioneer certificate in which conditions under which the income tax relief can be enjoyed will be stated.

For any application for a pioneer certificate to be considered, the estimated cost of qualifying capital expenditure to be incurred by the company on or before production day shall not be less than:

- a. 150,000 in the case of an indigenous controlled company, or
- b. 150,000 in the case of any other company.

## SELF-ASSESSMENT EXERCISE

What would the national council of ministering consider before issuing a pioneer certificate to a company?

### 3.2 Application for Pioneer Status

Application for pioneer status can be made by a company incorporated in Nigeria or by a group of persons on behalf of a company which is to be incorporated later. The application shall be on a prescribed form. Every such application shall state the grounds upon which the applicant relies and if the application is for the issues of a pioneer certificate to any company, the application shall:

- a. State whether the company is, or the indigenous controlled company.
- b. Give particulars of the assets on which qualifying capital expenditure will be incurred by the company, including their resource and estimated cost.
- c. On or before production day, and
- d. During a period of three years following the production day.
- e. Specify the place in which the assets are to be situated.
- f. State the probable date of production day.
- g. Specify any product and by product (not being a pioneer product to be produced, and give a reasonable estimate of the quantities and value, of such product and by product during a period of one year from production day.
- h. Give particulars of the loan and share capital including the amount and date of each issue and the source from which the capital is to be or has been raised.
- i. In the case of a company already incorporated, give the name, address and nationality of each director and the number of shares held by him.
- j. In the case of a proposed company, give the name, address and nationality of each promoter of the company.

After considering any application made, together with such further information as may be called for, the director shall issue a certificate to the pioneer company certifying the date of its production day, you should note that the period of the tax holiday shall commence from the production day.

## **SELF-ASSESSMENT EXERCISE**

What should be the content of an application requesting for a pioneer certificate to any company?

### **3.3 Certification of Qualifying Capital Expenditure**

A pioneer to the board to certify the amount of the qualifying capital expenditure incurred by the company prior to production day, not later than one month after the production day of a pioneer company has been finally determined and certified by the director or within such extended time as the board may allow.

The proceeds of disposal of any item of capital expenditure disposed of prior to production day shall be deducted from the total amount of capital expenditure incurred to arrive at the amount to be certified. Also, if any of such disposal has not been made in an arm's length transaction, the open market value on the date of the disposal shall be submitted for the disposal proceeds.

After considering the application made for the certification of qualifying capital expenditure as above together with such further information as may be requested, the board shall issue a certificate to the pioneer company certifying the amount of qualifying capital expenditure incurred by the company prior to production date.

## **SELF-ASSESSMENT EXERCISE**

What is the procedure of certifying the amount of qualifying capital expenditure incurred by a company prior to production day?

### **3.4 Cancellation of Pioneer Certificate**

The pioneer certificate issues to any company can be cancelled if:

1. The production day has been certified as on a date which is more than one year later than the estimated there of given in the company's application for a pioneer certificate. However, the council will not cancel the certificate if it is satisfied that the delay is due to causes outside the control of the company or do other good and sufficient cause.

2. The certificate of qualifying capital expenditure as on the production day is to the effect that the amount of qualifying capital expenditure incurred as on that day is less than the prescribed minimum applicable to the company.
3. The pioneer company concerned applies for other provision of the industrial development income act or has failed to fulfill any estimate or proposal made in its application for a pioneer certificate or any of the conditions contained in its pioneer certificate

### **SELF-ASSESSMENT EXERCISE**

What could necessitate the cancellation of a pioneer certificate?

### **3.5 Income Tax Relief and Losses**

A company holding a pioneer certificate shall be on a tax holiday for the period stated on the certificate. The tax relief period is usually for a period of three years at the first instance commencing on the date of the production day of the company unless cancelled or restricted in any manner by the council.

If certain requirements are met, the council may at the end of the three years extend the tax relief period to:

- a. Two period of one year each, or
- b. One period of two years

A pioneer company wishing to obtain such extension shall apply in writing within one month of the expiration of the initial three years tax relief period or of any extension thereof. Such application shall contain details of all capital expenditure incurred by the company by the requisite date. The requisite date is the date of expiry of a pioneer certificate.

Where the board is satisfied that a pioneer company has incurred a loss in any accounting period within the tax relief period, it shall issue a certificate to the company accordingly.

In determining whether such a loss has been made, the board may in its absolute discretion exclude such sum as may be in excess of an amount appearing to the board to be just and reasonable in respect of:

- a. Remuneration to directors of the company.
- b. Interest, service, agency or other similar changes made by a person who is a shareholder of the company or by a person controlled by such shareholder.

A net loss incurred by a pioneer company shall be deemed to have been incurred by the company on the day on which its new trade or business commences that is, on the day following the expiry of the tax relief period.

For each accounting period the board shall issue to the pioneer company a statement showing the amount of the income or loss for that period.

Net loss means the aggregate of losses incurred during the tax relief period after deduction of profit, if any, made at any time during that period.

### **SELF-ASSESSMENT EXERCISE**

- i. What is tax relief period granted to a pioneer company?
- ii. Describe the treatment of a loss incurred by a pioneer company within the tax relief period.

### **3.6 Taxable Profit, Exempted Profit and Dividend**

Any profit earned by a pioneer company from any operations or activities whatsoever other than its pioneer enterprises shall be deemed to be derived from Nigeria and shall be liable to tax under company income tax act (CITA)

Any profit shown on the statement issued by the board in respect of the income of a pioneer company for each of the accounting period of its tax relief period shall not form part of the assessable profit or total profits of the pioneer company for any Year of assessment and shall be exempted from tax under CITA.

Any amount of profit that is exempted from tax as stated above should be credited by the pioneer company to an account to be kept for the purpose of dividend that is declared by the company out of such profit shall be exempted from tax in the hands of the shareholders and shall for the purposes of CITA and PITD be deemed to be paid out of profits on which tax is not paid or payable during a tax relief period, a pioneer company shall not:

- a. Make any distribution to its shareholders, by way of dividend or bonus, in excess of the amount by which the account maintained for the exempted profits is in credit at the date of such distribution
- b. Grant any loan without first obtaining the consent of the minister. The consent of the minister shall only be given if he is satisfied that the pioneer company is obtaining adequate security and a reasonable interest for any such loan.

### **SELF-ASSESSMENT EXERCISE**

Explain the following:

- a. taxable profits
- b. exempted profits
- c. dividends distributed from exempted profits.

### **4.0 CONCLUSION**

In this unit, we discussed pioneer industries. We started by discussing the conditions required to be a pioneer company and proceeded to what should be the content of an application requesting for a pioneer certificate to any company, how is certificate for qualifying capital expenditure obtained, what can result to the cancellation of pioneer certificate, what is income tax relief and losses and finally, what is taxable profits, exempted profit and dividend distributed from exempted profits.

### **5.0 SUMMARY**

You should recall that a pioneer industry is any trade or business of the kind included in any list of pioneer industries published in the federal gazette or state gazette in the federation. A pioneer company is a company certified by any pioneer certificate to be a pioneer company.

A company holding a pioneer statement issued by the board in respect of the income of a pioneer company for each of the accounting period of its tax relief period shall not form part of the assessable profit or total profit of the pioneer company for any year of assessment and shall be exempted from tax under CITA.

### **6.0 TUTOR-MARKED ASSIGNMENT**

1. What should be the content of an application of any company requesting for a pioneer certificate?



2. What could necessitate the cancellation of a pioneer certificate?
3. Explain the following
  - a. Taxable profits
  - b. Exempted profits.
  - c. Dividend distributed from exempted profits.

## **7.0 REFERENCES/FURTHER READING**

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Ariwodola, J. A. (2001). *Personal Taxation in Nigeria*. (4th ed.). Lagos: JAA Nigeria Limited.