

## REVIEW: COMPANIES INCOME TAX (SIGNIFICANT ECONOMIC PRESENCE) ORDER 2020

### 1.0 INTRODUCTION

1.1 The Finance Act 2020 (“the Act”) was enacted to effect measures that would radically revamp the Nigerian economy as well as provide a fiscal means for offsetting the deficit in the 2020 budget. The Act brought several developments to the Nigerian tax regime with the amendment of the various tax legislation in Nigeria. One of the legislations amended is the Company Income Tax Act, Cap C20, LFN 2004 (CITA).

1.2 Sequel to the amendments made in CITA, the Finance Minister (“the Minister”) in collaboration with the Federal Inland Revenue Service (FIRS) released quasi-legislative documents to clarify the amendments made to CITA. One of the clarifications is central to this discourse – the Minister’s Order on Significant Economic Presence.

1.3 Before the Finance Act, taxation of Non- Resident Companies (NRCs) was based on profits accrued to its physical presence within the country. Section 13(2) of the CITA lists the following instances:

- where a company has a fixed base in Nigeria;
- where a company operates a trade or business in Nigeria through an agent;
- where a company is executing a turnkey project in Nigeria;
- where a company fails to price their related party transactions at arm’s length.

1.4 The implication of the above is that profits owing to online transactions of NRCs with persons (natural/artificial) resident in Nigeria are not liable to tax. This outrightly strips Nigeria of a huge chunk of revenue due to it.

1.5 Thankfully, the Finance Act has enlarged the tax web of NRC by the introduction and amendment of Section 13 of CITA.

1.6 Specifically, Section 13 (2c) of CITA (as Amended by the Finance Act 2019), states that:

*“ if it transmits, emits or receives signals, sounds, messages, images or data of any kind by cable, radio, electromagnetic systems or any other electronic or wireless apparatus to Nigeria in respect of any activity including electronic commerce, application store, high-frequency trading, electronic data storage, online adverts, participative network platform, online payments and so on, to the extent that the company has significant economic presence in Nigeria and profit can be attributable to such activity”*

Whilst Section 13 (2e) posits:

*“if the trade or business comprises the furnishing of technical, management, consultancy or professional services outside of Nigeria to a person resident in Nigeria to the extent that the company has significant economic presence in Nigeria”*

1.7 Furthermore, Section 13 (4) empowers the Minister to determine activities that constitute significant economic presence of non-resident companies.

## 2.0 COMPANIES INCOME TAX (SIGNIFICANT ECONOMIC PRESENCE) ORDER, 2020.

2.1 Following the enactment of the Finance Act, the tax space has been thrown into uncertainties due to the non-definition of Significant Economic Presence. The Minister of Finance in a bid to provide a meaning to the phrase issued the Companies Income Tax (Significant Economic Presence) Order 2020 in May 2020.

2.2 Paragraph 1 of the Order provides the criteria to determine the significant economic presence of non-resident companies involved in digital services. These categories of companies provide an outlet for electronic distribution of information across multiple platforms and devices such as cloud services, online search engines, and online marketplaces, etc.<sup>1</sup>

2.3 The qualification for significant economic presence activities of non-resident digital service provider are:

- a. Where it earns a gross turnover or income of more than N25 Million or its equivalent in other currencies are derived from the activities such as:
  - i. Streaming or downloading services of digital contents
  - ii. transmission of data collected about Nigerian users, and
  - iii. provision of goods or intermediation services through digital platforms
- b. Where it uses a Nigerian domain name or registers a website address in Nigeria;
- c. Where it engages in a purposeful and sustainable interaction with persons in Nigeria by customising its digital page or platform to target persons in Nigeria.

2.4 Going by the above provision, companies such as Amazon, Apple (iTunes), Netflix, Zoom, etc. will be subject to company income tax in Nigeria.

2.5 Additionally, Paragraph 2 of the Order postulate that non-resident companies carrying on a trade or business comprising the furnishing of services of technical, professional, management or consultancy in nature shall be deemed to have significant economic presence in Nigeria, where it earns any income or receives any payment from;

- a. any person resident in Nigeria, or
- b. a fixed base or agent of a non-resident company.

2.6 Thus, a non-resident company will be deemed to have significant economic presence in Nigeria, if in an accounting year, it receives payment for any of the expertise listed above, from a person resident in Nigeria, a fixed base of a foreign company or an agent of a foreign company.

2.7 The permitted exemptions to Paragraph 2 of the Order include:

- a. Payments made to contract staff resident in Nigeria
- b. Payments made for educational purposes.
- c. Payments by a foreign fixed base of a Nigerian company.

2.8 Accordingly, non-resident companies that identify with countries that have multilateral agreements or consensus arrangements to address tax challenges arising from the digitalization of their economy to which Nigeria is a party shall be treated in accordance with that agreement or arrangement. This simply translates to lesser tax burdens for non-resident companies whose country of origin have tax treaties with Nigeria.

1. <<https://www.csirtdsp.nl/en/digital-service-providers>>

### 3.0 INSIGHT CORNER

3.1 Nigeria has joined the league of nations who have figured out what approach to adopt in taxing digital corporations such as Zoom, Microsoft, Google, Tik-Tok, Netflix, Facebook, etc. While this might seem to be the right step in the right direction, the country still has several rungs ahead.

3.2 Firstly, the taxation of non-resident entities with virtual presence is more of a global problem than a national one because of the non-uniformity of tax laws and systems involved in taxing entities in different jurisdictions.

3.3 In 2019, the OECD published its Programme of Work otherwise known as **Base Erosion and Profit Shifting (BEPS) 2.0** to address the tax challenges of digitalization. The work plan focuses on how much taxes multinational entities pay and the jurisdiction the tax is paid into. The implementation of the work plan is based on two pillars, namely:

- a. Pillar One: which would allocate higher taxable profits to the countries where the produce consumers and service recipient reside, and
- b. Pillar Two: which would introduce a global minimum tax to prevent the shifting of profits to low-tax jurisdictions. <sup>2</sup>

However, notwithstanding the objective of Pillar One, countries have been taking independent steps towards taxing non-resident companies on the basis of Significant Economic Presence. Some of these countries include; Kenya, Italy, Israel, and India.

3.4 Nigeria joining the league is yet another feat, considering the significant steps the nation has made within its international tax space. For instance, Nigeria has signed the following:

a. *Multilateral Competent Authority Agreement (MCAA) for the exchange of country by country (CbC) reports*: The implementation of this MCAA provides the tax authorities with key information on the global activities of Multinational entities (MNEs) for the purpose of risk assessment.

b. *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (the MLI)*: The MLI is a legal instrument to prevent BEPS by MNEs. This MLI enables Nigeria to transpose results from the BEPS project into its existing network of tax treaties and in a quick and efficient manner.

c. *Multilateral Competent Authority Agreement on the Automatic Exchange of Financial Account Information (CRS MCAA)*: This agreement enables Nigeria exchange Common Reporting Standard (CRS) information with about 105 jurisdictions who are signatories to the MCAA.

d. *Introduction of the Income Tax (Transfer Pricing) Regulations (TP Regulations) 2018*: It ensures Nigeria imposes tax on the appropriate taxable base corresponding to the economic activities deployed by taxable persons.

e. *Introduction of the Income Tax (Country by Country Reporting) Regulations (the CbCR Regulations)*: The Regulations requires Ultimate Parent Entities (UPEs) of MNEs who are tax residents in Nigeria with consolidated revenue of ₦160 billion (or EUR750 million for MNE Groups headquartered outside Nigeria) or above to prepare and file CbCR reports with the FIRS

f. Introduction of Income Tax (Common Reporting Standard) Regulations (the CRS Regulations): The CRS Regulations will enable the FIRS collate and exchange bulk information of taxpayers. This will enable the FIRS have access to information on global income of Nigerians and ascertain if appropriate taxes are being paid.

3.5 Regardless of these significant contributions, the pragmatics of the Order issued must be duly considered. How does the FIRS intend to audit the transactions of non-resident companies online in ascertaining taxes to be paid on the profits?

3.6 We suggest the FIRS may want to consider a holistic approach to implementing this order. The use of blockchain technology may come in handy in this regard. A blockchain is essentially a digital ledger of transactions that is duplicated and distributed across the entire network of computer systems on the blockchain. It is a system of recording information in a way that makes it difficult or impossible to change, hack, or cheat the system.<sup>3</sup> With the use of blockchain technology, the agency may find it easy to monitor the transactions of non-resident companies. Hence, transparency, as afforded by blockchain may help a great deal in determining the amount of assessable profits to be taxed by the agency.

#### 4.0 Going Forward

Notwithstanding the challenges envisaged, non-resident companies are expected to strategize their tax affairs in light of this new Order, by registering/regularizing their tax positions with the Non-Resident Persons' Tax Office ("NRPTO") at the Ikoyi Office. NRPTO commenced operations 1st January 2020 and is solely devoted to the taxations of non-resident entities with economic presence in Nigeria.

3. <https://www.euromoney.com/learning/blockchain-explained/what-is-blockchain>

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