

EXAMINING THE EFFECTS OF CORPORATE TAX INCENTIVES IN NIGERIA

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Abstract

This paper deals with corporate tax incentives and its effects in Nigeria particularly with how it impacts on investment promotion, tax incentives are those closed and special provisions created by the government that allow for exclusions, credits, preferential tax treatment or even deferral of tax liability. They are preferential tax treatment that are allowed for selected group of tax payers for certain purposes. They can be informed of tax holiday for a specific period, credits, investment allowances and many more. The paper will also review the possible impact of tax incentives on the Nigerian economic growth and to also expose the areas of advantages and disadvantages of the history and trajectory of tax incentives in Nigeria. Tax incentives are given to approve tax payers. It is considered to be centered on correcting market inadequacies, promote industrial infrastructure, subsidized consumption and to encourage investment among other things. This work will review with the aid of statute, case law and available texts as primary and secondary sources with available data in the area as research methodology, this paper sought the explanation surrounding corporate tax incentive in Nigeria and how it promotes investment.

Keywords: Tax, Incentives, Holiday, investment and exemption

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1.0 Introduction

Tax Incentives are those special clauses that allow for preferential treatment of a tax payer for the purpose of encouraging investment or development of a particular sector, it is special treatment of a tax payer, on the hand It should also be noted that the liability to tax a foreign company in Nigeria is determined by whether the home country of the company has a double tax agreement with Nigeria or not. Since the company is not a Nigerian company, its profits are not deemed to accrue in Nigeria. However, the profits of the foreign company would be subject to tax in Nigeria if the profits are deemed to be derived from Nigeria. These profits would be deemed to derive from Nigeria if they meet certain criteria.¹ In order to identify whether a foreign company is liable to tax in respect of its profits some tests have been suggested. In other words, the CITAA precisely set out a number of tests through which the profits of foreign companies would be deemed to be derived from Nigeria and so subject to tax.² Thus the Act provides:

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;³

The first criteria to be observed is to determine whether a company has a fixed base in Nigeria or not. This is because the profits of a foreign company with a fixed clear understanding of the phrase 'fix base'. However there is no statutory definition for it. Consequently recourse must be sought from the interpretation of courts contained in various Nigerian and foreign cases.

¹ Harold J. Benjamin, The Interaction of the law and tax (SCM Press Ltd, London, 1974) p. 23

² BBC Votes Nigeria World Most Populace People who don't pay tax - Daily Independence (Lagos) 27 February, 2024, p.23

³ s 11(2) (a).

In the case of *Shell International Petroleum v FBIR*⁴ a fixed base is taken to be the place from where a foreign company carries on business in Nigeria. There is no time threshold or limit for a place to be classified a fixed base. So, a facility used by a foreign company to carry on business in Nigeria would qualify as a fixed base even if the facility was in place only for a very short time.⁵

The business of the foreign company must be carried on from the fixed base. A facility would not qualify as a fixed base if the business carried on from it is not that of the foreign company. For example, if a dispute arises as to whether the profits of a foreign company invited to Nigeria to execute a specified project is subject to tax, it would not help the FIRS' case to show that the facility alleged to be the foreign company's fixed base is used by a major grain importer to store his grain. It is necessary to establish that the business of the foreign company or a related Nigerian company is carried on from the facility. Furthermore, where a foreign company is awarded a contract and incorporates a Nigerian subsidiary to execute it, the subsidiary could be deemed to be the foreign company's fixed base. A fixed base does not include a facility used solely for storage or display of goods or for the collection of information. In other words, if a foreign company has a showroom in Nigeria where it displays its goods, and subsequently supplies some goods to a customer in Nigeria from a source outside Nigeria, the profits from the transaction would not be liable to tax in Nigeria. However, if it makes the supply from its showroom in Nigeria, the profits made from the transaction will be subject to tax. It seems that only something in nature of a facility would constitute a fixed base. This inference can be gleaned from the nature of things which do not constitute a fixed base and from the fact that the Companies Income Tax Act gives the indication that a foreign company may maintain a stock of merchandise in Nigeria and would still not be deemed to have a fixed base. It can therefore be argued that an

⁴ (2002) 3 NWLR (Pt 859) 61.

⁵ K Amaefule (n.70)

employee of a foreign company who is in Nigeria to repair the airplanes of a client would not constitute a fixed base of the company.

2. Objectives of Tax Incentives

A foreign company may have a fixed base in Nigeria. It may generate profits from various places not only from its fixed base in Nigeria. Consequently the only portion of its profits that would be deemed to be derived from and therefore subject to tax in Nigeria, are those profits which are attributable to the fixed base. Profits which were not generated from the fixed base would not be subject to tax in Nigeria.

Another test which is also used to determine whether a foreign company has to pay tax from its profits is its habitual operation in Nigeria by an authorized person. According to the Act, a foreign company is liable to corporate tax even if it does not have a fixed base in Nigeria but on condition that it habitually operates a trade or business through an authorized person.⁶ This shows that a foreign company may not have a fixed base in Nigeria, but may habitually carry on business or preserve a store of its product for distributions through an authorized agent. The profits generated from such business or deliveries by the foreign company would be deemed to be derived from Nigeria and therefore liable to tax. The authorized person can be a direct representative of the company or acting on behalf of some other companies that are under the care and management of the foreign company. He can also be on behalf of another companies that have interest in the foreign company.⁷ The requirement that the company 'habitually' operates a business creates the impression that profits from a one-off and unrepeatable transaction would not be covered by this provision.⁸ This is the view of the FIRS. However, a court has held that the FIRS is not bound by its views in such circulars and is therefore at liberty

⁶ s 11(2) (b)

⁷ *ibid*

⁸ FIRS *Information Circular* No. 9302 of 22 March, 1993.

to subsequently canvass divergent views.⁹ The word ‘habitually’ implies frequency of customariness. An isolated transaction may therefore not be covered by the provision. But would profits from a transaction on behalf of a foreign company, which used to habitually carry on business through a person but for the past 5 years did not operate any business in Nigeria, be covered? It is not certain what number of transactions is to be carried out on behalf of a foreign company for it to be taken that the company ‘customarily’ operates business through a person.

The issue may be clear-cut in a number of cases, for others, it is not advisable to lay a general principle but to decide each case on its merits.¹⁰ Secondly, the profits of a foreign company would be liable to tax if deliveries are regularly made on its behalf by a person from a store of goods which the company habitually maintains in Nigeria. This provision applies to a foreign company that hands its goods over to an intermediary for the purpose of delivering the goods to its customers in Nigeria. The intermediary is merely the means by which the foreign company transacts with its customers in Nigeria. Equally, any profit made by the company on the sale of the goods by the intermediary would be subject to tax in Nigeria. A foreign company may carry on business through a number of persons none of whom can be said to habitually conduct its business in Nigeria. This arrangement would not shield the company from tax in Nigeria. This is because words which are used in the singular sense in an enactment include the plural form of the words. Therefore, it wouldn’t matter if the foreign company uses one or more persons to operate its business. It doesn’t matter if the authorized person does not act for the foreign company alone but does business with another company. It seems a foreign company would not have a defense if it claims the person does not have its express authority from the fact that the person has conducted and continues to conduct business or make deliveries on behalf of the company.¹¹

⁹ ibid

¹⁰ ibid

¹¹ ibid

Turnkey project is another method which is considered to verify the taxability of a foreign company. Turnkey project is a term used to refer to a single contract split into several components to be executed onshore and offshore respectively. Under the CITAA, a foreign company is to tax in respect of its profits derived from Nigeria even if the trade or business or activities involves a single contract; for surveys, deliveries, installations or construction, the profit from that contract.¹² Accordingly, the profits made by a foreign company from a single contract for surveys, deliveries, installations or construction are subject to tax in Nigeria. It has been suggested however, that the word ‘or’ between installations and construction be replaced with ‘and’. This is because the use of ‘or’ conveys the impression that profits of a foreign company from a contract for survey or a contract for deliveries etc. would be deemed to be derived from Nigeria. The rationale behind the suggested substitution becomes obvious when one considers the objective of this provision. The goal is to cover any loophole that would be used by companies to avoid tax from the profit made by turnkey project.¹³

Usually, the onshore component is executed by a Nigerian company while the offshore component is undertaken by a foreign company. For instance, a foreign company may split a contract to construct a football stadium in Nigeria into several components such as survey, design, fabrication, construction, delivery, and installation and award the first five components to a foreign company while a Nigerian company undertakes installation.¹⁴ This could be done with the aim of minimizing the profits liable to tax in Nigeria and increasing the foreign company’s profits from the contract. Nevertheless, the fragmentation of the contract does not avail in excluding the profit from the tax under the CITAA. This is because the Act has taken such type of project to be a single contract. The profits arising from it is

¹² s 11(2) (c)

¹³ K Amaefule, *Jurisprudence of Tax in Nigeria* 1st Ed (Princeton and Associate Publishing Co Ltd 2019) p. 41

¹⁴ *ibid*

subsequently subject to tax. It must be mentioned that profits from turnkey project are not always deemed to be derived from Nigeria. For example, a contract may involve various components e.g. fabrication, construction and installation. If the fabrication aspect cannot be locally done, the profits attributable to it ought not to be subject to tax in Nigeria. On the other hand, the profits derived from the construction and installation components are subject to tax even if any of them is executed offshore.

Artificial transaction is another test which is used to identify the taxability of a profit made by a foreign company. According to the Act¹⁵, a foreign company is liable to corporate tax in respect of any profit derived from Nigeria in as much as it is made from a transaction which is viewed as artificial by the Federal Inland Revenue Services.¹⁶ But the question here is how to determine whether a particular transaction is artificial or not.

It is relevant to know that a transaction is said to be artificial if it is between two related companies and the terms which govern the transaction are unlike terms which govern transactions between unrelated companies. Related companies often arrange intra-group transactions such that profits are shifted from one company to another which, for some reason, is liable to pay little or no tax. Where a foreign company makes more profits from an intra-group transaction, the FIRS is entitled to make an adjustment by applying open market terms in the intra-group transaction.¹⁷ The effect is that the portion of the company which is artificial would be transferred to the Nigerian company and subject to tax in Nigeria. For example, if a Nigerian subsidiary over-invoiced for a service performed by its foreign parent company, the Nigerian company would end up with less taxable profits in its books. This is because it would claim the over-invoiced amount as a deductible expense in its tax computations. Here, the FIRS is entitled to apply for a reduced rate, which approximates to an open market

¹⁵ s 11 (d)

¹⁶ ibid.

¹⁷ K Amaefule (n.13)

estimate, to the service. This will lead to lesser amount deducted as an expense for the service and therefore more taxable profits in the books of the subsidiary. Usually, the difference between the pre-adjustment taxable profits and the post-adjustment taxable profits would be the artificial component of the profits made by the foreign parent company.¹⁸

3. Corporate Income Chargeable to Tax

In Nigeria and many other countries, income has been taken as the base for the imposition of tax. It is therefore an obvious candidate of corporate taxation. A company can only pay tax out of the income it receives from its trade or business activities and investment. Consequently, ascertainment of income for tax purpose may appear very easy to some extent. However, the precise meaning of the term “income” is part of the most difficult area in taxation.¹⁹

Literally, different words are used as synonymous to the term ‘income’. These *inter alia*, include pay, earnings, wage, salary, profits, proceeds, interest, receipts, revenue and returns.²⁰ Each of these indicates a sum of money that comes in and received by a person. The term is denotatively used to mean the amount of money received by a person as the result of his work or trade and investment.²¹ This confines the meaning of income to cash that only comes from particular sources namely trade investment. However, an online dictionary extends the meaning to include the amount of “money or its equivalent received during a period of time in exchange for labour or services, from the sale of goods or property, or as profit from

¹⁸ *ibid*

¹⁹ A Shipwright, E Keeling, *Text Book on Revenue Law*, (Blackstone Press Limited, London, 1997) MH

²⁰ MH Manser, *Chambers Dictionary of Synonyms and Anonyms* (Chambers Harrap Publishers Ltd, 1997)

²¹ AS Hornby, *Oxford Advance Learners Dictionary* (Oxford University Press, 2010); Longman *Dictionary of Contemporary English*, (Pearson Education Limited, 2011)

financial investments.”²² In the same vein, income is defined in another dictionary as the money or other form of payment that one receives usually periodically, from employment, business, investment, royalties, gifts and the like.²³ These imply that the word has a wider meaning than its synonyms. This is because it covers all sorts of returns irrespective of the time and kind of activity from which it is derived or received for.

Statutorily, Companies Income Tax Act²⁴ did not provide for a specific definition of the word “income”, let alone the phrase “income tax” or “companies income” chargeable to tax. However, according to the Act, income is determined by reference to the sources it originated from. But in the case of *Coltaness Iron Co. v Black*²⁵ income is described as nothing more than whatsoever is assessed for tax purpose in as much as it is of the nature of income regardless of the sources it originated from. But this did not hint at the concept of income for tax purpose let alone its nature that will enable a person to distinguish between things that are of the same nature with it from those that are not. In the case of *Whitney v IRC*²⁶, income was evasively defined as “such income taxable under the Act.”²⁷ But the question that remains is “what is that income which is taxable under the Act?” In the same vein, income tax is defined in the case of *London County Council v Attorney General*,²⁸ as a tax on income. It is not meant to be a tax on anything else. This definition is not clear. The main question of what is income is still on. Thus, in the case of *Secretary of State for India v. Scoble*,²⁹ it is declared that income tax is not and cannot be case upon

²² AS Hornby, Income In: *Free Dictionary* < <http://www.thefreedictionary.com> > accessed 10 August 2022

²³ BA Garner, *Black's Law Dictionary* (West Publishing Co. Texas 2009)

²⁴ 2007, No. 11.

²⁵ (1881) 9 T.C. 286.

²⁶ (1925) 10TC at p.113

²⁷ *ibid.*

²⁸ (1901) AC 26 at p.35

²⁹ *ibid.*

absolutely logical lines.³⁰ Because of this in the Canadian case of *Oxford Motors Ltd v Minister of National Revenue*³¹ Abbot J. stated that in deciding the meaning of income, the courts are faced with practical considerations. Thus, determination of the meaning of income and ascertainment of income for tax purpose must all be based on particular facts of each case.³²

It is generally clear that the word ‘income’ is far from being precise. This is because it is multifaceted that could be perceived from multifarious angles. Any attempt to give the word a conceptual definition that is not all embracing may result in loss of huge amount of revenue that can be used to provide necessary amenities needed to attract investment in the country. However, a person can simply state that income is not capital. Subsequently it is essential to distinguish income from capital. This is because the distinction is on the fundamental basis upon which corporate taxation depends. Corporate tax is a tax imposed on the income of a company not upon its capital. It is therefore necessary to determine whether receipts have the character of capital or income.

The idea behind the companies income tax is that tax should be paid upon the company’s annual income its capital or the means by which income is produced. Thus, it is not a tax on wealth or upon individual transactions. It is a tax upon the regular, recurrent and periodic returns to companies. However, this is with exclusion of its capital receipts and after allowing losses and outgoings incurred in process of deriving the income. It is stated in the case of *Strick v Regend Oil Company Ltd*,³³ that no part of English law of taxation present the insoluble conundrums on determining whether a receipt or outgoing is capital or income for tax purpose. The parliament left the matter to the common sense of tribunals and judges before whom

³⁰ (1903) AC 299.

³¹ ibid

³² ibid

³³ (1965) 3 WLR p.1571.

these matters are brought.³⁴ Consequently, many courts adopted the primordial analogical expression in determining the concept of capital and income which says that the tree is the capital from which the annual income of the fruit crops is derived. This analogy shows the capital represent the stock of resources from which flows the income to capital in order to escape the payment of tax. Consequently, the physical nature of the asset and its functions should be put into consideration in order to identify what is capital and what is income for tax purpose.³⁵

Generally, income is ordinarily used to indicate the amount of money or its equivalent received by a person within a particular period of time. It normally comes from trade or business and investment. However, the CITAA provides for the sources of the companies income chargeable to tax. Therefore, companies' income chargeable to tax can be defined as the amount of money or its equivalent received by a company from trade/business or investment and taxable under the CITAA.

From the dimension of corporate taxation, profits are the income chargeable to tax under the CITAA. It is on this ground that the Act provides that tax shall be payable upon the profits of any company, accruing in, derived from, brought into or received in Nigeria.³⁶

Like the term income, profit has no statutory definition. Consequently, it must be given its ordinary meaning. The Oxford Advanced Learner's Dictionary³⁷ defines profit as 'the money that you make in business or by selling things especially after paying the cost involved'.³⁸ Black's Law Dictionary³⁹ defines it as 'the excess of revenues over expenditures in a

³⁴ *ibid.*

³⁵ I A Ayua (n.36)

³⁶ s 8 (1)

³⁷ A S Hornby (n.21)

³⁸ *ibid.*

³⁹ B A Garner (n.23)

business transaction'.⁴⁰ It is used to mean the excess of receipts over the expenditure necessary for the purpose of earning the receipts.⁴¹ Consequently, profit is an income although it is not any income can fall within the term profit.

The phrases 'accruing in, derived from, brought into, or received in Nigeria' encapsulated in the provision of the CITA are in need of thorough scrutiny. In the case of *Commissioner of Taxation v Kirk*⁴² the words 'derived from' was held to be synonymous with 'accruing in'. Both were meant to refer to 'acquired, obtained, or got'. But in the case of *Toufiq Karan v. Commissioner for Income Tax*,⁴³ Hooper J. looked at the phrases of 'accruing in' and 'received in' import a clear territorial limitation to Nigeria. By implication any profit acquired or obtained in Nigeria is taxable under the CITAA. He also opined that the words 'derived from' is designed to meet among other things cases where profits arises from transaction carried out in Nigeria by nonresident tax payer. Consequently, it is only the profits gained as the result of the business activities carried out in Nigeria by a foreign company that will be subject to tax under the CITAA. On the other hand, the words 'brought into' bring profits from transactions carried on outside Nigeria by a Nigerian company into the tax net on condition that the profits is actually imported into Nigeria.

It is understood from the above that corporate income subject to tax under the CITAA can be either the profits made in Nigeria or the profits made by Nigerian company. Subsequently, all profits of Nigeria or the profits made by Nigerian company. Subsequently, all profits of Nigerian or foreign companies derived from trading activities in Nigeria are subject to tax

⁴⁰ *ibid.*

⁴¹ I O Oni (n.46), (n.64)

⁴² (1935) 19 TC 390.

⁴³ (1948) WACA 25

unless otherwise provided under the Act.⁴⁴ If a company does not earn any profit, or it earns the profit but is not subject to tax or is exempted from tax, then the company is not liable to corporate tax. However, the Act imposed minimum tax on companies which have no taxable profit or taxable profit resulting in lower than the minimum tax.⁴⁵ This means that such companies must pay taxes out of their capital. This will undoubtedly discourage investment and increase the risk of failure for companies in periods of little or no profitability.

The profit of a Nigerian company is subject to tax irrespective of where and how it arises. It is equally subject to tax whether it arises inside or outside the country and whether it is remitted to Nigeria or not. It is also subject to tax in whatever form it is received. Whether it is received in cash or in kind, in local or in foreign currency, it is subject to corporate tax under the CITAA. Thus, the Act provides that the profits of a Nigerian company shall be deemed to accrue in Nigeria wherever they have arisen and whether or not they have been brought into or received in Nigeria⁴⁶. Therefore, if a Nigerian company derived profit from a trade or business carried on in the United Arab Emirates (UAE), such profit is deemed to be accruing in Nigeria and subsequently subject to tax irrespective of whether it is brought into Nigeria or not.⁴⁷ A Nigerian company can only escape from corporate tax if its profits fall within the scope exempted by the Act. Therefore, legislative approach on the issue of how to identify the company's income subject to tax (taxable profits) under the CITAA is based on determining income by reference to the respective source from which such income is derived.⁴⁸ Accordingly, the Act enumerates the types of profit sources

⁴⁴ Offshore International S.A.v FBIR (FRC/36/75, FRC Lagos 1975) Unreported

⁴⁵ s 28A (1) CITAA

⁴⁶ s 11 (1), CITAA.

⁴⁷ I O Oni (n.21)

⁴⁸ D Asada, The Administration of Personal Income Tax in Nigeria: Some Problem Areas <http://www.ujmicrosoft_academy.com> accessed 7 June 2024

deemed to be chargeable to tax from the companies' income in Nigeria. These include:

1. Any trade or business for whatever period of time such trade or business may have been carried on;
2. Rent or any premium arising from a right granted to any person for the use or occupation of any property;
3. Dividend, interest, royalties, discount, charges or annuities;
4. Any source of annual profits or gains not falling within the preceding categories;
5. Any amount deemed to be income or profits under a provision of CITA, or with respect to any benefit arising from a pension or provident fund of the PITA.
6. Fees, dues and allowances (wherever paid) for services rendered;
7. Any amount of profits or gains arising from acquiring or disposing short-term money instruments like Federal Government Securities, Treasury Bill or Saving Certificate, Debenture Certificate and Treasury Bonds.⁴⁹

It should be noted that each source of profits enumerated above is independent of one another. A company can only avoid tax by proving that it has got no profits or gains accruing in derived from Nigeria in any of the sources or categories of income above-mentioned.

4. Conclusion and Recommendations

To this extent, the work has been summarized. The major findings have been identified. Recommendations have therefore been made as follows-

- i. **Corporate Tax Rate Reduction:** The rate of tax statutorily imposed upon the profit of any company in Nigeria is thirty percent (30%). This rate is among the highest in the world. To avoid negative impact on the flow of foreign investment to the country, the amount should be reduced to 20%. This is to

⁴⁹ s 8, CITAA.

harmonize with some African countries such as Libya, Egypt, Mauritania and Madagascar and other Asian and European countries such as Turkey, Thailand, United Kingdom and Russia. The reduction will definitely attract more investors and retain the existing ones.

- ii. **Repeal of Minimum Tax Provision:** Section 22A (1) of the CITAA provides for the payment of corporate tax if the company fails to secure any profit. This is a serious problem that has a negative impact on companies in general and their investment in particular. Consequently, the provision should be amended
- iii. **Elimination of Corporate Multiple Taxation:** To encourage more investors, corporate multiple taxation must be eliminated. Companies' income tax alone is enough.
- iv. **Amendment of CITA Provision for Non-Compliance:** N600, N1,000, N20,000 and N25,000 provided under sections 74, 73(1), 71(1) and 41 (3) of the CITAA respectively as fine for corporate tax avoidance or evasion are not adequate. To ensure compliance and generate more revenue that can be used for investment promotion, the amount must be increased to reflect current realities. The amounts should be raised to N60,000, N100,000, N200,000, and N250,000 respectively. This is in consideration of the huge amount of profits earned by companies nowadays particularly transnational corporations. Consequently, provisos of the said sections of the Act should be amended.
- v. **Good Governance and Judicious Management of Revenue Collected:** Good governance and proper management of tax revenue is one of the most effective ways of investment promotion. Once the revenue collected is properly utilized on actual projects that have a direct impact on the taxpayers it will automatically encourage companies to invest more and positively impact on investment promotion. Once the revenue is not looted or squandered it will have more money for public services and security of life and properties. This will definitely encourage

companies to expand their investments and attract new investors and increase the flow of FDIs to the country

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