

The withholding tax rate on construction and related activities has been reduced

February 2015

In brief

The Minister of Finance recently issued an official gazette for the Amendment of the Schedule to the Companies Income Tax (Rates etc., of Tax to be Deducted at Source (Withholding Tax)) Amendment Regulations. The amendment reduces the rate of withholding tax on building, construction and related activities (excluding survey, design and deliveries) from the old rate of 5% to 2.5%, effective 1 January 2015.

In detail

Background

The Companies Income Tax (Rates, etc. of tax Deducted at Source (Withholding Tax) Regulations is the regulation guiding the operation of Withholding Tax (WHT) in Nigeria.

Before the amendment, WHT rate on “all aspects of building construction and other related activities” was 5%. This amendment has a commencement date of 1 January 2015.

The Amendment

On 17 December 2014, the Minister of Finance and Coordinating Minister for the Economy signed an amendment to the existing regulation to be cited as “The Companies Income

tax (Rates etc., of Tax Deducted at Source (Withholding Tax)) Amendment Regulations, 2015.

The amendment reduces the rate of WHT on all aspects of building, construction and related activities (excluding survey, design and deliveries) to 2.5%.

The reduction in rate was necessitated by the low margin being earned by many construction companies and the inability of FIRS to pay refund for excess withholding tax credit notes. Apart from the cash flow strain on the affected companies, the lack of effective refund mechanism for excess credit notes meant real additional tax cost.

The excluded services (survey, design and deliveries) are considered as high margin services but it will be necessary for the FIRS to provide

clarification in terms of what constitutes these excluded services especially "Deliveries" which may be open to diverse interpretations.

Other implementation challenges will be in respect of turnkey contracts such as an EPC project (Engineering, Procurement and Construction) where for practical reasons there may be no split of the contract sum into the various components. Where different aspects of a construction project liable to different WHT rates are executed by the same or related contractor(s), FIRS could potentially demand that the split be justified to prevent arbitrary apportionment designed to take advantage of the lower rate.

Also, the retroactive commencement date of the changes may not be practicable to apply where withholding tax has already been deducted by

payers before the regulations were published.

Given that the amendment relate to companies taxable under the Companies Income Tax Act, other entities not taxable under CITA will continue to suffer withholding tax at the rate of 5%. It is not clear if this was intended.

The takeaway

The Amendment explicitly excluded “survey, design and deliveries” from the scope of the

tax reduction. The import of this is that survey and engineering design activities connected to building design and construction cannot be described as “building and construction” activities for tax purposes. These activities are often a significant part of the value of a construction project particularly for certain industries like upstream oil and gas.

It would be useful for government to revisit the entire WHT Regulations to provide greater clarity on the more ambiguous contentious areas

such as “ordinary course of business” which will go a long way to aid compliance amongst taxpayers.

The FIRS commenced a comprehensive review of the WHT Regulations in 2013. We hope that the exercise will be completed sooner rather than later to address the various thorny issues in the administration of WHT in Nigeria.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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