

# FIRS Information Circular on the claim of tax treaty benefits in Nigeria



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## Background

The Federal Inland Revenue Service (FIRS) has recently issued an information circular (Circular 2021/05) on the claim of tax treaty benefits in Nigeria. The circular which is dated 3 June 2021, withdraws and replaces the earlier FIRS circular on the same subject issued on 4 December 2019. We present the highlights of the circular below:

## Highlights of the circular

### Definition

A Double taxation agreement (DTA) is an agreement between two or more countries with the objective of ensuring that a resident of one or both contracting countries does not suffer tax more than once on the same income in both jurisdictions, or unduly benefit from not paying appropriate taxes in any of the countries through tax evasion or avoidance.

### Nigeria's DTA with other countries

The FIRS circular highlights that Nigeria has operational DTAs with 16 countries namely: Canada, Pakistan, Belgium, France, Romania, Netherlands, United Kingdom, China, South Africa, Italy (airline and shipping only), Philippines, Czech Republic, Slovakia, Singapore, Sweden and Spain.

### General eligibility for treaty benefits

The FIRS highlights that to be entitled to the benefits under a DTA with Nigeria, a taxpayer must be a resident of Nigeria or the treaty partner or both countries. In addition,

- i. the taxpayer must be liable to tax in the treaty country of which he is a resident.
- ii. the relevant income is not tax exempt in Nigeria.
- iii. the tax for which benefit is being sought, is covered by the DTA.
- iv. the benefit to be claimed is not excluded under the DTA.
- v. the benefit is claimed within the time stipulated by the treaty or domestic laws. The FIRS stated that claims for tax credit can only be made not later than 2 years after the end of the year of assessment (YOA) in which the foreign tax was paid.

### Eligibility for reduced Withholding Tax (WHT) rates on passive income and technical fees

A WHT rate of 7.5% is applicable on dividends, interests and royalties paid from Nigeria to a foreign company resident in a treaty country. This does not apply to taxpayers that are resident in Italy, as the Nigeria-Italy DTA only covers shipping and airline activities.

To be eligible for reduced WHT, in addition to fulfilling the general conditions above, the following additional conditions must be met:

- i. the beneficial owner of the income must be a resident of the other treaty country, even if the income was not paid directly to the recipient;
- ii. the income must not relate to a Permanent Establishment (PE) which the beneficiary has in the paying country. WHT on such income connected to a PE will attract WHT at 10%.

With respect to payments for management, professional, technical or consultancy services, WHT will apply at 10% or 5% on payments to foreign companies and individuals respectively, resident in treaty countries. However, such fees are required to be covered under the Article on Business Profits in the DTA, or connected to a PE or Fixed Base in Nigeria. In the absence of such PE or Fixed Base, WHT will not apply on such fees.

### Treaty tax rates applicable to eligible international transport businesses

A foreign airline or shipping company that is resident in a treaty country will not pay Companies Income Tax (CIT) in Nigeria in a YOA, if a Nigerian airline or shipping company also operates in the home country of that foreign company. Otherwise, CIT will apply at 1% (1.5% for Philippines) on the profits of such foreign company that are generated from Nigeria.

However, CIT will not apply on the Nigeria-generated profits of a foreign airline or shipping company that is resident in the United Kingdom, Italy and China, regardless of whether a Nigerian airline or shipping company also operates in these countries or not.

### Denial of treaty benefits

A taxpayer may not be granted treaty benefits if:

- i. It is discovered that its residency of one of the treaty countries was principally for the purpose of accessing the treaty benefits;
- ii. A principal purpose of the arrangement of a transaction or business is to take advantage of the treaty.

### Relief in respect of foreign taxes

Where a resident of Nigeria has paid foreign tax on an income derived from a treaty partner of Nigeria, such taxpayer can obtain foreign tax credit in Nigeria. However, the income which has been taxed in the foreign treaty country is required to also be included in the global income of the company taxable in Nigeria. Also, the following conditions should be fulfilled:

- i. The income is not exempt from tax in Nigeria
- ii. The tax credit in Nigeria cannot exceed the total tax payable in Nigeria for that YOA on that same income

### Procedures for claiming treaty benefits

The following procedures are to be followed for applying for the treaty benefits:

- i. **Completion of certificate of residence:** This includes the Certificate of Residence for Nigerian residents - to be completed by Nigerian residents seeking tax treaty claims foreign countries, and a Certificate of Residence for non-residents - to be completed by non-residents seeking to access tax treaty benefits in Nigeria;
- ii. **Submission of formal application to the Relevant Tax Authority:** The formal application should be addressed to the Executive Chairman of the FIRS, for the attention of the Director, Tax Policy and Advisory Department. The completed Certificate of residence, evidence of foreign tax paid (for Nigerian residents), or evidence of income on which WHT treaty rate is being sought (for non-residents) must be attached to the application;

iii. **Submission of claim for tax credit:** Once the claim for tax treaty benefits has been approved by the FIRS, the taxpayer is also required to submit:

- a copy of the approval to the appropriate FIRS field office or the State Board of Internal Revenue (SBIR) along with its self-assessment returns, where the application is for a foreign tax credit relief.
- a copy of the approval to the WHT collecting agent, where the application for a WHT treaty rate relief.

## Takeaway

**We have included our comments on some of the paragraphs in the FIRS circular below:**

- **Basis for administrative procedures:** The circular clarifies the administrative procedures recently introduced by the FIRS, to approve the claim of treaty benefits by companies. As these administrative procedures are not included in the treaties themselves, questions may be asked with regards to the legal basis for denying treaty benefits to companies that do not undergo the procedures. However, companies are advised to comply with the required steps in order to forestall avoidable disputes.
- **2-year restriction:** The FIRS circular stated that claims for foreign tax credits can only be made within 2 years after the end of the YOA in which the foreign tax was paid. However, there is no basis for this restriction in the tax laws or in the treaties between Nigeria and its treaty partners. Therefore, this could be challenged even though companies may comply just to be pragmatic. The Companies Income Tax Act already prescribes a 6-year time frame to claim a tax relief and/or refile returns to correct errors or mistakes.
- **Historical application:** Some portions of the Circular and the Certificate of Residence forms suggest that the FIRS wants companies to apply for the treaty relief retrospectively, i.e to obtain tax credit after the tax has been paid. In practice, the FIRS requires the application to be completed annually or at least every 2 years (in line with their timelines), so an advance approval for several years is not possible.
- **Significant Economic Presence (SEP) rules:** The FIRS circular did not specifically clarify the interaction between tax treaties and the recently introduced SEP rules. Based on the SEP rules, foreign companies that remotely provide digital, technical, professional, management or consulting services are now subject to income tax in Nigeria. However, it is expected that where Nigeria has a DTA with the home country of the relevant company, the SEP rules will not apply and such foreign companies will only have Nigerian income tax implications where the conditions for income tax in the relevant treaty are met. This was alluded to in the circular where the FIRS highlighted that WHT will not apply on technical, professional, management or consulting fees paid to foreign companies from treaty countries that do not have a PE or Fixed Base in Nigeria.

In general, the issuance of the information circular provides some clarity on the FIRS' expectation with regards claiming treaty benefits. However, the procedures may be considered a bit burdensome to taxpayers, and may be prone to bureaucratic bottlenecks that may hinder or delay treaty benefit claims. We recommend that the FIRS streamlines the application process, also considering some of the takeaway points highlighted above.

**For a deeper discussion, please contact any member of our Tax Controversy and Dispute Resolution team below:**

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