# FIRS Finance Act Circular
# Regulated securities lending transactions

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## Background

The Federal Inland Revenue Services (FIRS) has issued a circular on the tax implications of regulated securities lending (RSL) transactions in Nigeria.

RSL involves various parties including:

- **Lender**: Owner of dividend-bearing securities.
- **Borrower**: Borrows securities from Lender and provides a collateral.
- **Agent**: Facilitates transactions between both parties.

The Borrower obtains securities from Lender through an approved Agent, for an agreed fee and a stipulated period. Borrower provides collateral to Lender usually in the form of cash. Borrower seeks to profit by selling and repurchasing the securities ("short selling").

Lender receives the securities back at the end of the transaction and profits by earning a fee.

Agent profits from commission or brokerage fees.

In the period that ownership is transferred temporarily to Borrower, Borrower pays any dividends on the securities to Lender. Also, Lender pays interest earned on the collateral to the Borrower. These are regarded as "compensating payments" which can be made directly to Borrower or Lender, or through the Agent.

These activities are subject to approval and regulation by the Securities and Exchange Commission (SEC).

## Highlights

The circular clarifies the following:

### Companies Income Tax (CIT)

Rights, bonuses, fees and other benefits accruing to Borrower or Lender constitute taxable income.

Dividends paid by Borrower to Lender are Franked Investment Income exempt from CIT in Lender's hands.

Such dividends paid by Borrower to Lender will not be an allowable deduction for the Borrower.

Interests on collateral paid by Lender to Borrower are taxable in Borrower's hands.

Interests paid by a Lender to earn tax-exempt dividends are not tax-deductible.

Dividends and interests received or paid by the Agent on behalf of other parties are exempt and non-deductible respectively.

### Withholding Tax (WHT)

WHT applies on interests paid by Lender to Borrower. However, if Lender pays through Agent, the responsibility to deduct WHT is on the Agent.

WHT does not apply on dividends paid by Borrower to Lender irrespective of whether the dividends are paid directly to Lender or through the Agent.

The WHT Regulations issued under Section 81 of CITA will not apply to compensating payments made in an RSL.

### Personal Income Tax (PIT)

The amendments relating to RSL only affect entities taxable under the CITA. Therefore, individuals that participate in RSL will continue to be taxed in line with existing provisions of the PIT Act.

### Stamp Duties

RSL instruments such as receipts, shares, stocks or securities and other documents issued by the SEC are exempt from stamp duties.

### Capital gains tax (CGT)

Transfer of securities in RSL transactions are not disposals. Capital gains on the sale of shares are already exempt from CGT under the CGT Act.

## Takeaway

The FIRS circular considers rights and bonus issues as taxable income whereas in the strict sense they are "compensating payments" in respect of capital, and therefore should not be taxed. Rights and bonus issues are adjustments against share capital which do not constitute income for the holders.

The circular regards dividends paid by Borrower to Lender as franked, and exempt from CIT. However, this may not always be the case where such dividends have been exempted from WHT.

Overall, the new tax regime introduced by the Finance Act will facilitate activities in RSL which is expected to have a positive impact on the capital market.

**For a deeper discussion, please contact any member of our Tax team below or your usual contact within PwC Nigeria:**


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