

# *TP regulations in Nigeria*

## Frequently Asked Questions

**1) Q: What is Transfer Pricing?**

**A:** Simply put, the term Transfer Pricing (usually referred to as TP) is how related parties price goods, services, intangible assets, loans and other transactions between them. TP rules or regulations are established in various countries to ensure that related party prices are reasonable and fair.

**2) Q: The FIRS has been asking companies to submit their TP policies. What does this mean?**

**A:** A policy is a framework, a statement of intent, a set of principles and procedures to guide decision making in order to achieve desired results or rational outcomes in a consistent manner. Therefore, for TP purposes, there should be a policy to address dealings among group members and other related parties including key shareholders, technical partners and directors. The TP policy generally provides guidelines on how prices are or will be set for related party transactions such as management and technical services, secondment of staff, shared costs, intercompany loans and guarantees, royalty, sale of goods or transfer of assets and so on.

**3) Q: We are a multinational organisation and already have a group policy in place. Would this suffice for the Nigerian TP rules?**

**A:** NO. Your starting point will be the global policy but this must be adapted to suit the specific local TP requirements. There should be more in-depth analysis of the local economic conditions and specific transactions. As much as possible, the approach, principles and methods should be consistent with the global group policy with appropriate justifications for any deviations.

**4) Q: How do I know if my transaction is expected to comply with the TP Regulations?**

**A:** Well, you need to consider whether you have related parties (corporate or individuals) or any person or entity that

you can influence or is capable of influencing you. The next issue is whether you have any commercial dealings with such related parties. If your response in both cases is yes, then you are required to comply with the TP rules whether your related party is domestic or foreign.

In general if the TP rules do not specify a threshold, this means all related party transactions should be documented. However, the extent of analysis required in the documentation will depend on the materiality of the transaction.

**5) Q: Why is it necessary to apply the TP regulations to related parties who are both resident in Nigeria?**

**A:** Generally TP regulations are designed to address cross border related parties transactions. However, there are instances where it will be necessary for local entities to apply the rules e.g. where one entity is under pioneer status, or a loss making entity within a profitable group, or related parties subject to tax at different rates and so on. As a result, there is merit in bringing local groups under the purview of the TP regulations.

**6) Q: When is the first period or effective date that we are required to comply with the TP rules?**

**A:** The Regulations are effective for all tax years beginning on or after August 2, 2012. As such, calendar year taxpayers will be impacted by the new rules starting January 1, 2013. Taxpayers should be aware that although the Regulations will not apply retroactively, because the arm's length principle has always existed in the tax statutes, the FIRS may challenge a taxpayer to demonstrate that transactions undertaken before the issuance of the Regulations were conducted at arm's length. Generally, the FIRS can audit a taxpayer as far back as six years.

**7) Q: Do we wait for the FIRS to request for our TP documentation before carrying out a TP study?**

**A:** NO. You should proceed with TP policies and documentation in line with the

OECD guidelines if you have not already started. Once the FIRS makes a request you must submit the documentation within 21 days which is not sufficient to prepare the documentation. It is therefore advisable to have it ready before submitting your tax returns. Make no mistakes; the documentation is not just about having a written agreement in place – it is about being able to justify to yourself and the FIRS that the price (or fee) being paid is not arbitrary, and has not been manipulated to confer on you or your related party an undue advantage to the detriment of the tax authority.

**8) Q: How do I set the price for my related party transactions and be able to convince the FIRS that it is fair and reasonable rather than arbitrary?**

**A:** A number of methods are stated in the TP regulations from which taxpayers are expected to select the most appropriate for each of their related party transaction. Generally, the most appropriate method to determine is that which reflect prices between independent parties under the given circumstances. The simple question to answer is “how much would I be willing pay or receive if I was dealing with a third party?”

**9) Q: How easily can we obtain information about comparable transactions or companies in order to justify our TP with related parties?**

**A:** Obtaining information about third parties comparables will be quite tasking in Nigeria given the lack of Nigeria specific databases for such information especially where traditional methods such as the Comparable Uncontrolled Price is to be used. In reality, there may be no robust database in Africa. It might be necessary to search for internal comparables or rely on other foreign databases and make country specific adjustments.

The ultimate objective should be that the taxpayer can demonstrate that it has applied its best efforts in carrying out the analysis. Where traditional methods do not work, reliance can be placed on other methods such as the profit based methods.

**10) Q: Okay. So once we prepare the documentation, what do we do if there are new transactions or a change in circumstance of existing ones?**

**A:** A TP document will usually be prepared for several years. It is a document which states the basis for pricing transactions and not necessarily the price. However, the TP documentation should be reviewed and updated when there are new transactions or where there is a significant change in the conditions used in the comparability analysis. Generally, it is recommended that companies carry out a check on their TP documentation ever two years at most.

**11) Q: Can the FIRS raise assessments for past years on the basis of TP adjustments?**

**A:** The TP rules are not to be applied retroactively so any TP adjustments will be assessed going forward. However, given that the requirement to apply the arm's length principle has always existed in the tax laws, the FIRS may reopen past years as part of their normal audit and investigation.

**12) Q: Would we still need to obtain NOTAP approval for management fees, technical services, royalty etc if we already have TP documentation in place?**

**A:** Yes. NOTAP approval will continue to apply as a matter of compliance with an existing law and also for exchange control purposes. However, the basis for tax deduction will no longer be NOTAP but TP analysis.

**13) Q: What happens in the case of disparities between Customs import values and TP documentation?**

**A:** This has been a lingering and prevalent issue particularly in developing countries and where custom duties are handled by separate tax authorities. However, there are instances where reliance has been placed by the courts on customs valuations. In our experience Customs are unlikely to give refunds for a TP adjustment done by the FIRS. It is important for

taxpayers to enter into pre-importation arrangements with the customs and tax authorities where possible to ensure they do not lose out both ways.

**14)Q: Will a TP policy be useful in defending allocation of profits to a Permanent establishment (PE) and taxation on actual rather than deemed profit basis?**

**A:** Currently the FIRS taxes the PE of non residents on a deemed profit basis which assumes that the profit of their Nigeria derived income is 20%. It should be possible to use a TP policy to defend the allocation of profits within an entity to an identifiable PE in Nigeria to support tax on actual profit rather than deemed profit basis.

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