THE REVISED NIGERIAN TRANSFER PRICING REGULATIONS

The Federal Government of Nigeria through the Federal Inland Revenue Service (FIRS) has issued a revised income Tax (Transfer Pricing) Regulations, 2018 effective March 12, 2018, thereby revoking the old Regulations.

Objective Of The New Regulations

The Regulations were issued to ensure alignment with the developments in international tax practice as it relates to Transfer Pricing (TP) particularly the Base Erosion and Profit Shifting (BEPS) project embarked upon by the Organisation for Economic Cooperation and Development (OECD) on the request of the finance ministers of the G20 countries.

The OECD developed thirteen (13) Action Points to mitigate BEPS. Action Point 8 to 10 (Aligning transfer pricing outcomes with value creation) and Action Point 13 (Transfer Pricing Documentation and Country by Country Reporting) focused on intangibles, contractual allocation of risks between Multinational Entities (MNEs), level of returns to funding provided by a capital-rich MNE group members and the requirements for filing “Master and Local files” among other issues.

Highlights of the changes to the old Regulations are as follows:

Custom Duty Value As A Means Of Determining Arms-Length Price

The Service may not accept the value reported for customs duty purposes when considering the income tax implications of non-arm’s length importation.

Intangibles

Where controlled transactions involve exploitation of rights on an intangible, the consideration payable that is allowed for tax purposes is restricted to 5% of the earnings before interest, tax, depreciation and amortisation (EBITDA).

Capital-Rich Low-Function Companies

These are companies capitalised with a relatively high amount of equity (or equity-equivalent) capital, but which have limited capacity to carry out risk-management functions. For tax purposes, such companies shall only be entitled to a risk free return where they fund research and development of another MNE in the group without controlling the financial risks associated with the funding activities.

Advanced Pricing Agreement (APA)

The threshold of N250million that was set for a company to be eligible for APA in the old TP regulations has been removed.

Corresponding Adjustments under a Double Tax Agreement (DTA)

Under the new Regulations, where judicial, administrative, or other legal proceedings, have resulted in a ruling, the FIRS will not make corresponding adjustments where one of the parties involved in the transaction is liable to penalty (after adjustments have been made) as a result of fraud, gross negligence or wilful default.

TP Declarations and Disclosures

The time period within which TP declarations and disclosures should be filed have been aligned with that of CITA, not later than eighteen months of incorporation or six months after accounting year end, whichever is earlier. Updated declaration is also expected to be made in certain situations such as where a company or parent company merges with another company or parent outside the group; or there is an acquisition of up to 20% equity of another entity outside the group; or where there are other changes in structure or arrangement, including retirement or appointment of a Director.

TP Documentation Exemption

Connected persons are expected to maintain contemporaneous documentation. However, connected persons with total value of controlled transactions less than **N300million** may choose not to maintain contemporaneous documentation. But where necessary, the FIRS may demand that the documentation be prepared and submitted not later than 90 days from the date or request.

Safe Harbour

In accordance with international best practice, in order to shed the burden of proving arm's length price, the connected person may adopt prices in accordance with specific guidelines, but such must be as published by the FIRS.

Dispute Resolution

Unlike in the old Regulations, the head of the FIRS TP division now has the responsibility of referring taxpayer's objection to an assessment to the Decision Review Panel (DRP).

Penalties

The penalties regime has been drastically reviewed upwards, leaving taxpayers with no option but to comply with the TP Regulations. The Penalties are summarized below:

1. Failure to file TP declaration: ₦10 million in the first instance and ₦10,000 for every day the failure continues.
2. Failure to file updated TP declaration or provide notification about directors: ₦25,000 for every day in which the default continues.
3. Failure to file TP disclosure: the higher of ₦10 million or 1% of the value of related party transactions not disclosed; and ₦10,000 for every day in which the default continues.
4. Incorrect disclosure of transactions: the higher of ₦10 million or 1% of the value of related party transactions incorrectly disclosed.
5. Failure to file TP documentation upon request: the higher of ₦10 million or 1% of the value of related party transactions not disclosed; and ₦10,000 for every day in which the default continues.
6. Failure to furnish information or documentation upon request: 1% of the value of each related party transaction for which information or document relates; and ₦10,000 for every day in which the default continues.

Our Comments

1. With these changes FIRS has shown that it is keeping pace with the recent changes in the international tax arena, as focus is now more on transparency and disclosures aimed at reducing the incidence of BEPS.
2. Some of the changes, particularly the new penalty regime appears to be beyond what can be effected through a Regulation and may be contested by taxpayers. They also appear not to be in tune with the Federal Government drive for foreign investment and ease of doing business slogan.
3. The threshold of N300 million introduced for taxpayers not required to maintain contemporaneous documentation does not appear to be an exemption, as the FIRS may still request for the documentation at any time and failure to comply attract penalty.

We therefore advise all companies operating in group structures to ensure strict compliance with these regulations to prevent the hammer of FIRS, which it has not used sparingly in recent months.

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