NATIONAL OPEN UNIVERSITY OF NIGERIA

SCHOOL OF MANAGEMENT SCIENCES

COURSE CODE: BHM 417

COURSE TITLE: TAXATION

COURSE DEVELOPMENT

BHM 417

TAXATION

COURSE GUIDE

Course Writer: **Mrs. Ofe I. Inua**
School of Management Sciences
National Open University of Nigeria,
Victoria Island, Lagos.

Course Editor:

Programme Leader: **Dr. Onyemachi J. Onwe**
School of Management Sciences,
National Open University of Nigeria,
Victoria Island, Lagos.

Course Coordinator: Mrs. Caroline Aturu-. Aghedo
School of Management Sciences,
National Open University of Nigeria,
Victoria Island, Lagos.

1.0 INTRODUCTION

BHM 417: Taxation is a first semester two credit and 400 level core course. It will be available for all students offering undergraduate programme in B.Sc. Entrepreneurial and Business Management at the School of Management Sciences.

This course will expose you to the nitty gritty about the operations of taxation in Nigeria. In this course, you will be exposed to the various forms of taxes, how taxes are assessed, penalties for non-payment of taxes etc.

2.0 COURSE GUIDE

The course guide tells you briefly what the course is about, what course materials you will be using and how you can work your way through the study materials. It suggests some general guidelines for the amount of time you are likely to spend on each unit of the course in order to complete it successfully.

It also gives you some guidance on your tutor-marked assignments, which will be made available to you at the Study Centre. There are regular tutorial classes that are linked to the course. You are advised to attend these sessions.

3.0 WHAT YOU WILL LEARN IN THIS COURSE

The course ENT 417 consists of 18 units. Specifically, the course discusses the following:

- Historical and Legal Background of Taxation in Nigeria
- Tax Administration in Nigeria
- Taxation of Income
- Basis for / Period of Assessment
- Taxation of Employees
- Taxation of Self Employed
- Partnership Taxation
- Capital Allowances
- Loss Relief
- Capital Gains Tax
- Double Taxation Reliefs
- Taxation of Settlement, Trust and Estates
- Taxation of Special Business
- Withholding Tax
- Pioneer Industries
- Education Tax
- Petroleum Profit Tax

- Value Added Tax

4.0 COURSE AIMS

The aim of the course can be summarised as follows:

This course aims to give you an understanding of the meaning of tax and taxation, how the theories and concepts can be applied in business and government operations. It also aims to help you develop knowledge and skills that you required as a banker, an entrepreneur, a management practitioner and an accountant in private and public educational institutions to enable you guide against running foul of the law of the land.

5.0 COURSE OBJECTIVES

To achieve the aims set out, the course sets overall objectives. Each unit also has specific objectives. The unit objectives are always specified at the beginning of a unit; you should read them before you start working through the unit. You may want to refer to them during your study of the unit to check your progress.

You should always look at the unit objectives after completing a unit. When you do that, you will ensure that you have followed the instructions in the unit.

Below are the overall objectives of the course. By meeting these objectives, you should have achieved the aims of the course as a whole. On successful completion of the course, you should be able to:

- What are the composition and functions of the State Joint Revenue Committee?
- State five non-taxable income of an employee.
- State the relevant provision in which an income from employment is deemed to be derived in Nigeria.
- Describe the treatment of tax deduction for an employee leaving an employment or branch.
- Describe the income of partners.
- Discuss the relevant tax authority in relation to a partnership.
- State the conditions for granting capital allowances.
- State and describe five qualifying expenditure.
- Explain a carry forward loss relief.
- State the beneficiaries of the income from an estate
- Explain the computed income of a settlement
- In what manner is the computed income of any year apportioned for assessment?
- What is franked investment income?
- Explain withholding tax on interest or royalty.
- Explain withholding tax on rent.
- What should be the content of an application of any company requesting for a pioneer certificate?

- What could necessitate the cancellation of a pioneer certificate?
- Explain the assessment and collection of education tax.
-
- State the reason why sales tax was replaced by value added tax.
- Describe the operation of VAT in Nigeria.

6.0 WORKING THROUGH THIS COURSE

To complete this course, you are required to read the stud y units, read set books and read other materials provided by the National Open University of Nigeria (NOUN). Each unit contains self-assessment exercises, and at a point in this course, you are required to submit assignments for assessment purposes. At the end of the course, there will be a final examination. The course should take you a total of 16 – 17 weeks to complete.

Below, you will find listed all the components of the course. What you have to do and how you should allocate your time to each unit in order to complete the course successfully on time.

The list of all the components of the course is as presented.

7.0 COURSE MATERIALS

Major components of the course are:
- Course Guide
- Study Units
- Textbooks
- Assignment
- Presentation Schedule.

8.0 STUDY UNITS

The study units in this course are as follows:

MODULE 1 TAX ADMINISTRATION IN NIGERIA – AN OVERVIEW

Unit 1 Historical and Legal Background of Taxation in Nigeria
Unit 2 Tax Administration in Nigeria
Unit 3 Taxation of Income
Unit 4: Basis for / Period of Assessment
Unit 5 Taxation of Employees
Unit 6 Taxation of Self Employed

MODULE 2 TAXATION, RELIEFS AND ALLOWANCES

Unit 7 Partnership Taxation
Unit 8 Capital Allowances

Unit 9 Loss Relief
Unit 10 Capital Gains Tax
Unit 11 Double Taxation Reliefs
Unit 12 Taxation of Settlement, Trust and Estates

MODULE 3 TYPES OF TAXES

Unit 13 Taxation of Special Business
Unit 14 Withholding Tax
Unit 15 Pioneer Industries
Unit 16 Education Tax
Unit 17 Petroleum Profit Tax
Unit 18 Value Added Tax

9.0 ASSIGNMENT FILES

A number of self assessment exercises and fifteen assignments have been prepared to help you succeed in this course. The exercises will guide you to have understanding and good grasp of the course.

10.0 PRESENTATION SCHEDULE

The presentation schedule included in your course materials also have important dates of the year for the completion of tutor-marked assignments (TMAs) and your attending to tutorials.

Remember, you are required to submit all your assignments by the due date. You should guard against falling behind in your work.

11.0 ASSESSMENTS

There are two aspects to the assessment of the course: first are self-assessment exercises, second are the tutor-marked assignments; and third, there is also a written examination.

In tackling the assignments, you are expected to apply information, knowledge and techniques gathered during the course. The assignments must be submitted to your tutor for formal assessment in accordance with the deadlines stated in the Presentation Schedule and the ***Assignment File. The work you submitted to your tutor will count for 30% of your total course*** mark.

At the end of the course, you will need to sit for a final written examination of 'three hours' duration. This examination will also count for 70% of your total course mark.

12.0 TUTOR-MARKED ASSIGNMENT (TMAs)

Each of the units in the course material has a tutor-marked assignment (TMAs) in this course. You only need to submit five of the eight assignments. You are to answer all the TMAs and compare your answers with those of your course mates. However, you should ensure that you collect four (4) TMAs from the Study Centre. It is compulsory for you to answer 4 TMAs and submit them for marking at the Study Centre. Each TMA is allocated a total of 10 marks. However, the best three of the four marks shall be used as your continuous assessment score.

You will be able to complete your assignment from the information and materials contained in your reading, references and study units. However, it is desirable in all degree level education to demonstrate that you have read and researched more widely than the required minimum. Using other references will give you a broader viewpoint and may provide a deeper understanding of the subject.

13.0 FINAL EXAMINATION AND GRADING

The final examination for ENT 417 will not be more than three hours' duration and has a value of 70% of the total course grade. The examination will consist of questions, which reflect the types of self-testing, practice exercises and tutor-marked problems you have previously encountered. All areas of the course will be assessed.

Use the time between finishing the last unit and sitting for the examination to revise the entire course. You may find it useful to review your self-tests, tutor-marked assignments and comments on them before the examination. The final examination covers information from all parts of the course.

14.0 COURSE MARKING SCHEME

Total Course Marking Scheme:

Table 1: Course Marking Scheme

ASSESSMENT	MARKS
Assignment 4 (TMAs)	Best three marks of the 4 TMAs @ 10 marks = 30 marks of course = 30%
Final Examination	70% of overall course mar ks
Total	**100% of course marks**

15.0 COURSE OVERVIEW

This table brings together the units and the number of weeks you should spread to complete them and the assignment that follow them are taken into account.

Unit	Title of work	Weeks activity	Assessment (end of unit)
Module I			
1	Historical and Legal Background of Taxation in Nigeria	1	Assignment 1
2	Tax Administration in Nigeria	1	Assignment 2
3	Taxation of Income	1	
4	Taxation of Employees	1	Assignment 3
5	Measurement of Cost Behaviour	1	

6	Taxation of Self Employed	1	
	Module II		
7	Partnership Taxation	1	Assignment 4
8	Capital Allowances	1	
9	Loss Relief	1	
10	Capital Gains Tax	1	Assignment 5
11	Double Taxation Reliefs	1	
12	Taxation of Settlement, Trust and Estates	1	
	Module III		
13	Taxation of Special Business	1	Assignment 6
14	Withholding Tax	1	
15	Pioneer Industries	1	Assignment 7
16	Education Tax	1	Assignment 8
17	Petroleum Profit Tax	1	
18	Value Added Tax	1	Assignment 9
	Revision		
	Total	***18***	

16.0 HOW TO GET THE MOST FROM THIS COURSE

In distance learning, the study units to replace the university lecturer. This is one of the great advantages of distance learning. You can read and work through the specially designed study materials at your own pace, and at a time and place that suits you best. Think of it as you read the lecture and that a lecturer might set you some readings to do. The study unit will tell you when to read your other materials. Just as a lecturer might give you an in-class exercise, you study units also provide exercises for you to do at appropriate points.

Each of the study units follows a common format. The first item is an introduction to the subject matter of the unit, and how a particular unit is related with the other units and the course as a whole.

Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. You should use these objectives to guide your study. When you have finished the unit, you must go back and check whether you have achieved the objectives. If you make a habit of doing this, you will significantly improve your chances of passing the course.

The main body of the unit guides you through the required reading from other sources. This will usually be either from Reading Section or some other sources.

Self-tests are interspersed throughout the end of units. Working through these tests will help you to achieve the objectives of the unit and prepare you for the assignments and the examinations.

You should do each self-test as you come to it in the study unit. There will also be numerous examples given in the study units, work through these when you come to them too.

The following is a practical strategy for working through the course. If you run into any trouble, telephone your tutor. When you need help, don't hesitate to call and ask your tutor to provide it. In summar y,

(1) Read this course guide.

(2) Organise a study schedule. Refer to the course overview for more details. Note the time you are expected to spend on each unit and how the assignments relate to the unit. Important information e.g. details of your tutorials, and the date of the first day of the semester is available. You need to gather together all information in one place, such as your diary or a wall calendar. Whatever method you choose to use, you should decide on and write in your own dates for working on each unit.

(3) Once you have created your own study schedule, do everything you can to stick to it. The major reason that students fail is that they get behind with their coursework. If you get into difficulties with your schedule, please let your facilitator know before it is too late for help.

(4) Turn to unit 1 and read the introduction and the objectives for the unit.

(5) Assemble the study materials. Information about what you need for a unit is given in the 'Overview' at the beginning of each unit. You will always need both the study unit you are working on and one of your set books, on your desk at the same time.

(6) Work through the unit. The content of the unit itself has been arranged to provide a sequence for you to follow. As you work through this unit, you will be instructed to read sections from your set books or other articles. Use the unit to guide your reading.

(7) Well before the relevant due dates (about 4 weeks before the dates) access the Assignment file to download your next required assignment. Keep in mind that you will learn a lot by doing the assignments carefully. They have been designed to help you meet the objectives of the course and, therefore, will help you pass the examination. Submit all assignments not later than the due dates.

(8) Review the objectives for each study unit confirm that you have achieved them. If you feel unsure about any of the objectives, review the study material or consult your tutor.

(9) When you are confident that you have achieved a unit's objectives, you can then start on the next unit. Proceed unit by unit through the course and try to pace your study so that you keep yourself on schedule.

(10) When you have submitted an assignment to your tutor for marking, do not wait for its return before starting on the next unit. Keep to your schedule. When the assignment is

returned, pay particular attention to your facilitator's comments. Consult your tutor soon as possible if you have an y questions or problems.

(11) After completing the last unit, review the course and prepare yourself for the final examination. Check that you have achieved the unit objectives and the course objectives.

17.0 TUTORS AND TUTORIALS

There are eight (8) hours of tutorials provided in support of this course. You will be notified the dates, times and location of these tutorials, together with the names and phone numbe your tutor, as soon as you are allocated a tutorial group.

Your tutor will mark and comment on your assignments, keep a close watch on your pro and on any difficulties you might encounter as they would provide assistance to you durin course. You must mail your tutor-marked assignments to your tutor well before the due date least two working days are required). They will be marked by your tutor and returned to you soon as possible. Do not hesitate to contact your tutor by telephone, e-mail, or discussion boar if you need help. The following might be circumstances in which you would find help necessary.

Contact your tutor if:

- you do not understand any part of the stud y units or the assigned readings.
- you have difficulty with the self-tests or exercises.
- you have a question or problem with an assignment with your tutor's comment on an assignment or with the grading of an assignment.

You should try your possible best to attend the tutorials. This is the only chance to have face-to face contact with your tutor and to ask questions which are answered instantly. You can any problem encountered in the course of your study. To gain the maximum benefit from course tutorials, prepare a question list before attending them. You will learn a lot from participating i discussions actively.

18.0 SUMMARY

As earlier stated, the course ENT 417: Taxation is designed to introduce you to various techniques, guides, principles, practices etc. relating to tax, taxation and their assessment i Nigeria.

We hope you enjoy your acquaintances with the National Open University of Nigeria (NOUI We wish you every success in the future.
s

COURSE DEVELOPMENT

BHM 417

TAXATION IN NIGERIA

MAIN TEXT

Course Writer:	Mrs. O. I. Inua School of Management Sciences National Open University of Nigeria Victoria Island, Lagos.
Course Editor:	
Programme Leader:	Dr. Onyemachi J. Onwe School of Management Sciences, National Open University of Nigeria, Victoria Island, Lagos.
Course Coordinator:	Mrs. Caroline A. Aghedo School of Management Sciences, National Open University of Nigeria, Victoria Island, Lagos.

TABLE OF CONTENT

MODULE 1 TAX ADMINISTRATION IN NIGERIA – AN OVERVIEW

UNIT 1 HISTORICAL AND LEGAL BACKGROUND OF TAXATION IN NIGERIA

CONTENT

1.0 INTRODUCTION

It is the expectation of the public to see that government provides basic infrastructure such as good road, network, bridges, airports, seaports, e.t.c. and other social services like education, electricity supply, pip-borne water, housing and other services that cannot be executed by private hands. These expectations cannot be actualized except there is an enabling financial resource. It is therefore demanded that Government should search for the required substantial amount of funds to meet these obligations.

Government usually raise funds from various source such as issuing of public debt, levying of taxes, fees, fines and specific charges, among the various sources from which Governments can raise finance, taxes are the most important and reliable.

In this unit, we want to discuss the historic and legal background of taxation in Nigeria. We shall also discuss the basic concept of taxation. This would enable you to have a fundamental knowledge, to prepare you for the subsequent discussion on taxation in all the units.

2.0 OBJECTIVES

After studying this unit, you should be able to

1. Discuss the historical background of taxation in Nigeria
2. Explain the Nigeria tax legislation
3. Define tax and taxation
4. State and explain the characteristics of a good tax system
5. Explain direct taxes, indirect taxes, proportional tax, progressive tax and regressive tax.

3.0 MAIN CONTENT

3.1 Historical Background of Tax in Nigeria

Before the advent of the British colony, Nigeria in her separate regions had their elaborate system of taxation. The problem faced by the British when they arrived in Nigeria was how to streamline the multiplicity of tax system into a single general tax of the nature of an income tax payable annually on a single demand.

In 1904, Lord Lugard who was the then High Commissioner of the Northern Protectorate issued the Land Revenue Proclamation, N0. 4 of 1904, to unity the various types of existing taxes. In 1906, another proclamation known as the Native Revenue Proclamation, N0.2 of 1906 replaced the first proclamation of 1904.

In the Western parts of Nigeria, the earliest form of direct taxation was introduced in 1918 following the promulgation of Native Revenue (Southern Province) ordinance N0.29 of 1918. While in the eastern parts of Nigeria, direct taxation was introduced a bit later than in other parts of Nigeria, due to the strong resentment to its imposition. However, by the end of 1930, the system of direct taxation had been firmly introduced throughout Nigeria.

In 1940, the Income Tax Ordinance and the Direct Taxation Ordinance was enacted. It introduced a single income tax system in Nigeria. The Income Tax Ordinance of 1940 and the subsequent Income Tax Ordinance of 1930 provided the basis for the present day legislation on income tax.

Following the recommendations of the Raisman Fiscal commission of 1958, the Federal Government in 1961 enacted the Income Tax Management Acts, 1961, the companies Income Tax Act 1961, and the Personal Income Tax (Lagos) Act, 1961. It was these Tax Acts that laid the foundation for the uniform principles of income tax throughout Nigeria.

The Income Tax Management Act, 1961 was repealed in 1993 by the Personal Income Tax Decree No. 104 of 1993, which thereafter replaced the Income Tax Management Act, 1961.

Self Assessment Exercise 1.1

Explain the historical background of taxation in Nigeria.

3.2 Nigeria Tax Legislation

Tax Legislation enables the imposition of the various types of taxes on the citizenry. The main taxing Acts currently in force in Nigeria are as follows:

1. Personal Income Tax Act (PITA) 1993 – This tax Act or Decree deals with the assessment of the forms of personal income, whether earned or unearned income that is liable to tax for a given fiscal year. The Personal Income Tax Act came into effect on 25th August, 1993, following the promulgation of the Personal Income Tax Decree No. 104 of 1993. Decree No. 104 of 1993 also repealed the previous Income Tax Management Act of 1961. The PITA 1993 assumes jurisdiction over all tax matters relating to individuals residing in the respective states in Nigeria.

2. Companies Income Tax Act (CITA) 1990 – This tax Act deals with the assessment of the profits of limited liability companies incorporated under the Companies and Allied Matters Decree of 1990, or any enactment replaced by that Decree. The present Companies Income Tax Act (CITA) 1990 is a consolidation of the previous Companies Income Tax Act of 1961, which was re-enacted in 1979. It incorporates all subsequent amendments to date and is applicable throughout Nigeria.

3. Petroleum Profit Tax Act (PPTA) 1990 – This tax Act deals with the assessment of the profit of companies engaged in petroleum operations. The original Act in respect of companies engaged in petroleum operations was enacted in 1959. The present PPTA (1990) is a consolidation of the previous Act and the various tax amendments carried out over the years in the oil sector. The Act is applicable throughout Nigeria.

4. Capital Gains Tax Act (CGTA) 1990 – this tax Act deals with the assessment of Capital gains accruing to individuals or corporate bodies on the disposal of capital assets. The original Act was enacted in 1967. The present CGTA (1990) is a consolidation of the previous Act incorporating the various amendments that have occurred over the years. Capital Gains Tax in respect of corporate bodies and residents of Abuja is collected by the Federal Government, while the State Government collect from individuals and other bodies that are outside the tax jurisdiction of the Federal Government.

5. Industrial Development (Income Tax Relief) Act (IDA) 1990 – This Act was introduced to stimulate economic development by both indigenous and foreign companies alike. The Act provides a tax incentive for approved industries in the form of remission of income tax on profits earned during a relief period of three years in the first instance and an addition two years if sought for and granted. It was the earlier Act of 1971 that has now been consolidated into the Industrial Development (Income Tax Relief) Act 1990.

6. Value Added Tax Act (VATA) 1993 – This Act or Decree deals with the assessment of the increase in value of goods as they proceed through various stages of production and distribution and also to services as they are rendered. Value Added Tax is presently imposed at a flat rate of 5% on all goods and services that are taxable under the Act. It is a tax on consumption rather on 1st December, 1993. But it came into effect on 1st January 1994.

7. Education Tax Act (ETA) 1993 – This Act or Decree deals with the assessment and collection of an annual education tax two percent imposed on the assessable profits of companies registered in Nigeria. The Act also established an education into which the tax collected should be paid. The education fund is administered by a Board of Trustees which is responsible for the disbursement of the money in the fund to Federal, State and Local Government education institutions. The Education Decree was promulgated on 1st January, 1993.

Self Assessment Exercise 1.2

Explain the following Nigerian Tax Legislation:

1. Personal Income Tax Act 1993
2. Companies Income Tax Act 1990
3. Petroleum Profits Tax Act 1990
4. Value Added Tax Act 1993
5. Education Tax Act 1993

3.3 The Concept of Taxation

A tax is compulsory levy imposed by a public authority on the income, profit or wealth of an individual, family, community, corporate or unincorporated body etc. for the public use.

Taxes may be distinguished from other types of fees and charges imposed by government by virtue of the fact that they do not bestow on the tax payer the right to claim something equivalent to the tax paid from the government. Thus, the taxpayer is not entitled to any special service or benefit from government that excludes other members of the public on account of the tax he/she paid. Therefore, income generated from taxes is used by government to provide services for the entire citizenry despite the fact that some citizens such as school children and the elderly do not do not pay taxes.

Taxation is the process or system of raising income through the levying of various types of taxes. The extent of which taxation can be used for shaping and directing a nation's socio-political, economic and financial activities will depend on the flexibility, reliability and effectiveness of the various types of taxes introduced and the society's response or reaction to their imposition.

Self Assessment Exercise 1.3

1. Define Tax
2. Define taxation

3.4 Characteristics of a Good Tax System

A well balanced and structured tax system should have certain universally accepted criteria. Let us discuss such criteria below:

1. The Equity Criterion – This criterion implies that the tax burden should be equitable felt by all tax payers, both the rich and the poor. That is, tax should be paid according to one's ability. Hence, taxes should be progressive in nature, where by the larger a person's income, the higher the tax liability.

2. The Convenience Criterion – this criterion implies that the timing of payment and the procedure of payment of tax should be of the least inconvenience of the tax payer.

3. The Economic Criterion – This criterion implies that the tax collection procedure should be highly efficient and effective to ensure that it is carried out at minimum cost. It would be uneconomical for the cost of collection to exceed the revenue generated from the taxes.

4. The Elasticity Criterion – This criterion implies that the tax system should be sufficiently elastic to ensure automatic flexibility in terms of the responsiveness of the tax changes in the gross domestic product (GNP)

5. The Certainty Criterion – This criterion implies that the tax liability should be clear and unambiguous to the tax payer. Thus, the amount of tax due, manner of payment, date of payment and place of payment should be clearly spelt out to the tax payer.

Self Assessment Exercise 1.4

State and explain the attributes of a good tax system.

3.5 Classification of Taxes

Taxes can be classified into direct and indirect taxes.

Direct Taxes

Direct taxes are taxes levied on the income or capital generated by factors of production such as Land, Labour, Capital and Entrepreneurship. These taxes are usually imposed directly on individuals and companies. The burden of tax is not shiftable. The following types of direct taxes are currently in force in Nigeria:

a. Personal Income Tax
b. Companies Income Tax
c. Petroleum Profit Tax
d. Capital Gains Tax
e. Education Tax

Indirect Tax

The indirect taxes are levied on goods and services. They are usually imposed at some point on a good or service. The burden of tax may be shifted to whomsoever it is intended should be the final consumer. Thus, the ultimate incidence of these types of taxes does not occur at the original point of contact. Where an indirect tax is levied as a percentage of the cost of a good, it is known as an Ad Valorem Tax.

The following types of indirect taxes are currently in force in Nigeria:

a. Stamp duties
b. Excise duties
c. Customs duties on imports and exports
d. Mineral royalties
e. Casino tax
f. Value added tax

We can further classify taxes on the basis of the proportion of the total income paid on taxes. In this regard, there are three types of taxes, viz:

1. Proportional tax
2. Progressive tax
3. Regressive tax

Proportional Tax: A tax is proportional when the same tax rate is applicable irrespective of the size of the income. That is, a flat rate is applicable to income whether such income is increasing or decreasing.

Progressive Tax: A tax is progressive when the rate of tax applicable increases as the income increases. That is, higher the income attracts higher tax rates and vice-versa.

Regressive Tax: A tax is regressive when the proportion of the total income paid as tax falls as income rises. Thus, the rate percent of a tax payer income paid as tax decreases as such form of indirect taxes, such as sales tax.

Self Assessment Exercise 1.5

Explain the following terms:

1. Direct tax
2. Indirect tax
3. Proportional tax
4. Progressive tax
5. Regressive tax

4.0 CONCLUSION

In this unit, we looked at the historical background of taxation in Nigeria. We proceeded in discussing the Nigerian tax legislation, the concept of taxation, and the characteristics of a good tax system and finally, the classification of taxes.

5.0 SUMMARY

You should recall that before the advent of the British colonialism, Nigeria in her separate regions had their elaborate system of taxation. By progressive evolvement of tax system in Nigeria, following the recommendation of the Raisman Fiscal commission of 1958, the Federal Government in 1961 enacted tax acts that laid the foundation for the uniform principles of income tax in Nigeria.

A tax is a compulsory levy imposed by a public authority on the income, profit or wealth of an individual, family, community and corporate bodies e.t.c for the public use.
The characteristics of a good tax system are equity, convenience, economic, elasticity and certainly criterion.

Taxes can be classified into direct taxes, indirect taxes, proportional tax, progressive tax and regressive tax.

6.0 TUTOR MARKED ASSIGNMENT

1. Explain the following Nigerian tax legislation

    a. Personal income tax Act 1995
    b. Companies income tax Act 1990
    c. Petroleum profits tax Act 1990
    d. Education tax Act 1995

2. State and explain the characteristics of a good tax system.

3. You are required to explain the following terms

    a. Direct taxes
    b. Indirect taxes
    c. Proportional tax
    d. Progressive tax

7.0 REFERENCES / FURTHER READING

Anyaduba J.O. (1999), Personal income taxation in Nigeria, Benin City United City Press

UNIT 2 TAX ADMINISTRATION IN NIGERIA

CONTENT

1.0 INTRODUCTION

Government all over the world undertakes huge public expenditure on behalf of their citizens. Among the various sources form which governments can raise income, taxes are the most important and the most reliable, contributing much more than any other sources.

It is therefore imperative to ensure that these taxes are properly collected and administered. The reliability and effectiveness of collecting taxes can only be ensured if there are appropriate authorities put in place to act on behalf of the Government.

Government can only access the individuals, communities and corporate bodies via authorised bodies that would ensue that the idea behind taxation is actualized.

That is the essence of this unit, to discuss the various authorised bodies that administer tax in Nigeria.

2.0 OBJECTIVES

After studying this unit, you would be able to:

1. Explain the composition and duties of the Joint Tax Board
2. Describe the composition and functions of the state Board of Internal Revenue.
3. describe the duties and powers of the Inspectors of taxes
4. Describe who is a tax collector
5. Explain the appointment and resignation of an appeal commissioners
6. State the composition and functions of State Joint Revenue Committee

3.0 MAIN CONTENT

3.1 The Joint Tax Board

The Joint tax Board was established to offer advice and co-ordinate various aspects of taxation in Nigeria. The Joint tax Board comprises of:

1. Chairman – This post is held by the Chairman of the Federal Board of Inland Revenue.

2. A member from each state of the Federation experienced in income tax matters. Each member is nominated by the commissioner responsible for income tax in the state.

3. Secretary – The Federal Public Service Commission appoints an officer experienced n income tax matter who maintains records of the Board's proceedings. The secretary ins not a member of the Board.

4. Adviser – The legal adviser of the Federal Inland Revenue Service serves as an adviser to the Joint Tax Board. Although, h is not a member of the Board.

The duties of the Joint Tax Boards are:

1. To exercise the powers or duties conferred on it by any express provision of the PITA (1993).

2. To exercise any other powers and duties arising under the PIT (1993), which may be greed by the Government of each territory!

3. To exercise any powers and duties conferred on it by any enactment of the Federal Government in respect of companies' income tax.

4. To advise the Federal Government n request on double taxation arrangements.

5. To promotes uniformity both in the application of the PITA (1993) and in the incidence of tax on individuals.

6. To advise the Federal Government on request on Capital allowance rates and other taxation matters.

7. To impose its decisions on matters of procedure and interpretation of the PITA (1993) on any state of the Federation for purposes of conforming to such agreed interpretation.

Self Assessment Exercise 2.1

1. What is the composition of the Join Tax Board?
2. State five duties of the Joint Tax Board.

3.2 State Board of Internal Revenue

The administration of the income tax laws in each State of the Federation is vested in the State Board of Internal Revenue. The operational arm of each State Board of Internal Revenue is known as the state Internal Revenue Service.

The State Board of Internal Revenue is composed of:

1. Chairman – He is a person experienced in taxation appointed by the State Government who is the head of the state Internal Revenue Service.

2. Three other persons nominated by the State finance Commissioner on their own personal merit.

3. The Directors and Heads of Departments within the State Internal Revenue Service.

4. A director from the State Ministry of Finance.

5. Legal Adviser – Notwithstanding that the legal adviser is a member of the State Board of Internal Revenue, he may appear for an represent the state Board I his professional capacity in any proceedings in which the state Board is a party.

6. The Secretary of the State service who shall be an ex-officio member.

The functions of the State Board of Internal Revenue are:

1. To ensure the effectiveness and optimum collection of taxes and penalties due to Government under the relevant laws

2. To do all such things as may be deemed necessary and expedient for the assessment and collection of the tax and account for all amounts so collection

3. To make recommendations, where appropriate to the Joint Tax Board on tax policy, tax reform, tax legislation, tax treaties and exemptions as may be required form time to time.

4. To generally control the management of the state Internal \Revenue Service on matters of policy, subject to the provisions of the law setting up the service.

5. To appoint, promote, transfer and impose discipline on employees of the State Internal Revenue Service.

Self Assessment Exercise 2.2

1. What is the Composition of the State Board of Internal Revenue?
2. State the functions of the State Board of Internal Revenue.

3.3 Inspectors of Taxes

The inspectors of taxes are under the control of the Board. They have a variety of duties covering all aspects of taxation. Their main duties and powers are:

1. Receipt and examination of the tax returns and other information from taxpayers and other sources.

2. Make and issue assessment, based on the returns, on which tax is payable.

3. If no return is received or the information therein is suspected to be false, they issue estimated assessments known as best of judgment (BOJ) assessments.

4. Deal with objectives by the taxpayers when revised assessment can be issued as considered necessary. If no body of Appeal Commissioners.

5. Deal with claims for repayment when tax has been overpaid by the taxpayers.

6. They are also connected with the PAYE system by oversight of its administration by employers.

7. Represent the Board at the Leaving of Appeals.

Self Assessment Exercise 2.3

State the duties of Inspectors of taxes

3.4 Collectors of Taxes

These officials of the State Internal Revenue Service are involved in taking steps that would result in the taxpayers settling their tax liabilities. They are concerned with the service of:

1. return of income forms;
2. notice of assessment;
3. summary and affidavits and other supply of information.

They do not handle money or actually collect taxes, but their efforts result in taxpayers paying their taxes section 94(i) of the Decree gives a definition of a Tax Collector as a duly authorised official of the State Service or the Federal Board of Inland Revenue.

A tax collector s empowered by section 95 of the Decree to enter into any house or premises, provided he does so without damage to the house or premises for the purpose of obtaining information in relation to a person who is or may be liable to the tax imposed by the Decree. Section 897 of the Decree states that any person who:

a. having been required to give information under the provisions of the proceeding section willfully obstructs a tax collector in the performance of his duties by neglecting or refusing to give such information or

b. otherwise obstructs or willfully misleads or attempts to mislead a Tax Collector in the performance of his duties under this part of this Decree, is guilty of an offence under this Decree.

Self Assessment Exercise 2.4

Who is a tax Collector?

Body of Appeal Commissioners

The State Commissioner may, by notice in the State Gazette, establish a body of Appeal Commissioners S 59(i). An Appeal Commissioner:

(a) Shall be appointed by notice in the gazette by the State Commissioner form among persons appearing to him to have had experience and shown capacity in the management of a substantial trade or business o the exercise of a profession of law, accountancy or taxation in Nigeria. S 59(2) (a);

(b) Shall hold office for a period of three years from the date of his appointment S 59 (2) (b);

(c) My resign at any time by notice in writing addressed to the State commissioner. On the request of the State Commissioner he my continue to act after the date of his resignation and sit at any further hearing in a case in appeal, until a final decision has been given with respect to that appeal S. 59(2) (c);

(d) Shall cease to be an Appeal Commissioner if the state Commissioner determines that his office be vacant and upon notice of such being published in the state Gazatte or on his acceptance of a political appointment S. 59 (2) (d)

The State Commissioner shall designate a public officer to be the Secretary to the body of Appeal Commissioners and the official address of the Secretary shall be published in the State Gazette s. 59 (3).

The body of Appeal Commissioners shall remain in office until a new body in sworn in S. 59(4).

Self Assessment Exercise 2.5

From the relevant sections, explain the conditions governing the appointment and resignation of an Appeal Commissioner.

State Joint Revenue Committee

The Joint Tax Board was directed in the 1998 Federal Government Budget to incorporate the participation of Local Governments in its activities through the establishment of a State Joint Revenue Committee in each state. The State Joint Revenue Committee is financed by the States and Local Government. The Joint Tax Board approved the following membership and functioned for the Committee.

Membership of the State Joint Revenue Committee

The composition of the Committee shall be as follows:

1. Chairman of the state Internal Revenue service as the chairman.
2. Chairman of the Local Government Revenue Committee Supervisor for Finance
3. A representative of the Bureau on Local Government Affairs not below the rank of director.
4. A representative of the Revenue Mobilisation, Allocation and Fiscal Commission as observer.
5. The State Sector Commander of the Federal Road Safety Commission (FRSC) as observer.
6. The Secretary to the Committee shall be a staff of the State Internal Revenue service s an ex-officio member.

Functions of the Committee

The following functions have been assigned to the State Joint Revenue Committees:

1. Implementation of decisions of the Joint Tax Board
2. Advising the States and Local Governments on effective revenue generation nd collection
3. Briefing and advising the Joint Tax Board, and the states and Local Governments on revenue matters.
4. Harmonization of tax administration in the States
5. Enlightenment f the public generally on state and local government revenue matters and
6. Carrying out any other functions that may be assigned by the Joint Tax Boar From time to time.

Self Assessment Exercise 2.6

1. Enumerate the composition f the state Joint Revenue Committee
2. What are the functions of the State Joint Revenue Committee?

4.0 CONCLUSION

In this unit, we discussed those established authorities put n place to facilitate the collection of taxes. Such authorities discussed were the Joint Tax Board, State Board of Internal Revenue, Inspectors of Taxes, Collectors of taxes, Body of Appeal Commissioners and State Joint Revenue Committee.

5.0 SUMMARY

You should recall that the Joint Tax Board was established to offer advice and co-ordinate various aspects of taxation in Nigeria.

The State Board of Internal Revenue is vested with the power to administer income tax in each state of the Federation.

Other bodies and Committee established to facilitate tax administration are Inspectors of taxes Collectors of taxes, body of Appeal Commissioners and State Joint Revenue Committee.

6.0 TUTOR MARKED ASSIGNMENT

1. Compare the duties and functions of the Joint Tax Board and State Board of Internal Revenue.

2. What are the composition and functions of the State Joint Revenue Committee?

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 3 TAXATION OF INCOME

CONTENT

1.0 INTRODUCTION

Income tax is payable on anything that can be described as an income. There is know where in the Personal Income Tax Decree (1993) where the definition of income has been given through the various sources of income that are chargeable are stated. Generally, tax may be imposed on any form of income derived from whatever source for any given year of assessments.

However, certain factors would determine the imposition or non-imposition of tax on any form of income, such as, the nature of such income, the source from which it was derived, and the circumstances under which it was derived. For instance, the official emoluments of the President and Vice President of the Federal Republic of Nigeria are exempted from tax by Law.

It is in the light of this unit to expose to you those issues and factors that should be considered when dealing with the taxation of the individual tax payer.

2.0 OBJECTIVES

After studying his unit, you should be able to:

1. Explain who a personal taxpayer is
2. explain the term ‘relevant tax authority’
3. Explain how the residence of a taxpayer is determined
4. Explain the rules that guide the determination of residence in Nigeria.
5. Explain artificial transaction in the opinion of a tax authority
6. List some income exempted from tax
7. Calculate the amount o income tax payable using appropriate personal income tax rates.

3.0 MAIN CONTENT

3.1 Personal Tax Payer

The personal tax payer can be broadly classified into:

1. The Person in paid employment
2. The person who is self employed

1. The Person in Paid Employment:

The person in paid employment is an individual who earns employment income. Such a person can be in the employment of a company or Government. Tax matters relating to this class of tax payers are handled under the Pay-as-You-Earn (PAYE) system.

2. The Person Who is Self-employed:

The person who is self-employed is an individual who earns his income form a trade, business, profession or vacation, carried on by him or with others. The person who is self employed includes:

a. Professionals like Accountant, Doctors, Lawyers and Engineers etc who are in private practice

b. A sole proprietor and

c. A Partnership, Trust, executor etc.

Income tax may be imposed on the income of a person for any year of assessment by the relevant tax authority of the territory in which such individual is deemed to be resident.

The relevant tax authority means the tax authority of the territory in which such a person is deemed to be resident for that year. Hence, the State Board of Internal Revenue in the State where the person is resident would be the relevant tax authority. However, there are persons whose relevant tax authority would be the Federal Board of Inland Revenue, irrespective of where they may resident in a given year of assessment. These persons are

1. Persons employed in the Nigerians Armed Forces and the Nigerian Police, other than civilians in such establishments.

2. Officers of the Nigerian Foreign Service

3. Residents of the Federal Capital Territory, Abuja and

4. Non-residents who derive income in Nigeria.

The relevant tax authority will be responsible for raising assessments on the taxpayer, collection of assessments raised and accounting for such collection made.

Self Assessment Exercise 3.1

Who is a personal tax payer?
Explain the term, 'relevant tax authority'

3.2 Determination of Residence

In order to establish the relevant tax authority of a taxpayer for any year of assessment, it is imperative to determine the residence of the taxpayer.

Residence in relation to a personal tax payer, means a place he resides in Nigeria for his domestic use on a relevant day and does not include any hotel, rest house or other place at which he is temporarily lodging unless a more permanent place is in available for his use on that day. Where an individual has to or more places of residence on a relevant day, not both or all of the places of residences are within the same territory. It is required to establish the relevant tax authority which would be the tax authority in care of the territory in which the tax payer has his principal place of residence. The principal place of residence would be determined from the following circumstances:

1. In the case of a person with no source of earned income (income derived from a trade, business, profession, vocation or employment carried on as well as any person from previous employment) other than a pension in Nigeria, that place of those places in which he usually resides.

2. In the case of an individual who has a source of earned income other than a person in Nigeria, that place of those places which is nearest to his usual place of work on the relevant day.

3. In the case of a person whose only source of income is unearned (income derived from an investment that does not relate to any reward for personal services rendered e.g. individual) that place of these places in which he usually resides.

Self Assessment Exercise 3.2

In order to establish the relevant tax authority, it is required to determine the residence of the taxpayer. Explain.

Guide to Determination of Residence in Nigeria

The following guide the determination of residence in Nigeria:

1. Foreign Employment

A person who holds a foreign employment on the first day of January in a year of assessment, or who first becomes liable to income tax in Nigeria for that year by reason of his entering such employment during that year, shall be deemed to be resident for that year in the territory in which the principal office of his employer is situated on that day, or on the day his employment commences as the case may be.

2. Nigerian Employment

A person who holds a Nigerian employment on first day of January in a year of assessment, or who first becomes liable to income tax in Nigeria for that year by reason of his entering such employment during that year, shall be deemed to be resident for that year in the territory in which he has place or principal place of residence on that day or upon the full duties of that employment in Nigeria. And if the person is on leave from a Nigerian employment on the first day of the year of assessment, he shall be deemed to be resident for that year by reference to his place or principal place of residence immediately before his leave began.

However, certain categories of persons are deemed to be resident in the Federal Capital Territory, Abuja, on the first day of any year of assessment irrespective of the actual state in which they may be residing. They are:

1. Persons employed in the Armed Forces and the Police Force, other than civilians in such establishment.

2. Officers of the Nigerian Foreign Service

3. Residence of the Federal Capital Territory, Abuja

4. Non-residents who derive income in Nigeria.

3. Other Employments

The person whose remuneration is subject to income tax in Nigeria for nay year of assessment, but who is not deemed to be engaged in Nigerian employment as in (2) and foreign employment as in (1) above, shall be deemed to be residents in the Federal Capital Territory, Abuja.

4. Pension

a. An individual whose only source of earned income arising in Nigeria on the first day of January in a year of assessment was a pension, shall be deemed to be residnet of that year in the territory in which he has a place or principal place of residence, on that day.

b. An individual whose only source of earned income arising in Nigeria on the first day of January in a year of assessment was a pension and who had no place of residence on that day, shall be deemed to be resident of that year.

i. if the person is a Nigerian pension wholly payable before the Government of one territory, in that territory

ii. if the pension is not a Nigerian pension, in the territory in which the principal office in Nigeria of the pension fund or other person authorising payment of the pension is situated.

c. An individual whose only source of earned income arising in Nigeria on the first day of January in a year of assessment was a Nigerian pension payable by more than one government or if there are two or more pensions arising in different territories to the individual, be subject to the income tax (Armed Forces and other persons) special Provision Act. He shall be deemed t be resident in the Federal Capital Territory, Abuja.

5. ***Earned Income other than from Employment or Pension***

A person who has a source of earned income in Nigeria for a year of assessment, other than an employment or a pension shall be deemed to be resident for that year in the territory in which he has a place or principal place of residence on the first day of January in that year.

However, if the source of such income was first acquired by the person during the year of assessment, and he had no place of residence on the first day of hat year, than he shall be deemed to be resident for that year in the territory where he first establishes a place of residence during that year.

In any other vase, h shall be deemed to be resident for that year in the territory form which part or the whole of his earned income arising in Nigeria is derived. If such income is derived from more than one territory, he shall be deemed to be resident in the Federal Capital Territory, Abuja

6. ***Unearned Income***

A person who has no source of earned income, but has one or more sources of unearned income in Nigeria for a year of assessment shall be deemed to be resident for that year in the territory in which he has a place or principal place of residence on the first day of January in that year. However, if such unearned income for that year arises in one territory, and he has no place of residence on that day, he shall be deemed to be resident for that year in the territory.

If the unearned income for that year arises in more than o ne territory, and he has no place of residence on that day, he shall be deemed to be resident for that year in the Federal Capital Territory, Abuja.

7. ***Corporation Sole or Body of Individuals***

A corporation sole or body of individuals other than a family o community shall be deemed to be resident for a year of assessment in the territory in which its principle office in Nigeria is located on the first day of January in that year. If it has no office in Nigeria on that day, it shall be deemed to be resident in any territory in which any part of the whole of its income liable to tax in Nigeria arises for that year.

Self Assessment Exercise 3.3

Explain the rules that guide the determination of residence in Nigeria under the following condition:

1. Foreign employment
2. Nigerian employment
3. Pension
4. Unearned Income
5. Body of individuals

Artificial Transactions

Where a tax authority is of the opinion that any disposition is not in fact given effect to, or that any transaction which reduces the amount of any tax payable is artificial or fictitious, the tax authority may disregard such disposition or direct that such adjustments shall be made in respect of the income of an individual, or an executor, or a trustee, as the tax authority considers appropriate, so as to counteract the reduction of liability to tax effected, or reduction which would otherwise be affected by the transaction.

A DISPOTION OR TRANSACTION SHALL BE SONDIDERED A ARTIFICIAL or fictitious, if it is made between persons, one of whom wither has control over the other, or is related t the other or between persons both of whom are controlled by some other person, or if in the opinion of a tax authority, the transaction has not been entered into on other terms which might fairly have been expected of independent persons engaged in he same or similar activities, dealing with one another at arms length. A disposition includes any trust, grant, covenant agreement or arrangement.

Self Assessment Exercise 3.4

What is an artificial transaction in the opinion of a tax authority?

Income Exempted from tax

Income earned by certain persons or body of person are exempted from tax as stipulated under the 3rd schedule to Personal Income Tax Decree 1993. Some of such incomes are listed below:

1. The official emoluments of the President, Vice President of the Federation and that of the State Governors and their respective deputies

2. The income of any ecclesiastical, charitable or educational institution of a public character in so far as it is not derived from a trade or business carried on by such institution.

3. The income of any trade union registered under the Trade Union Act, in so far as such income is no derived from a trade or business carried on by such Trade Union.

4. Gratuities payable to a public officer by the government of the federation or of a state in respect of services renewed by him under a contract of service with such government.

5. The income of any statutory or registered friendly society in so far as such income is not derived from a trade or business carried on by such society.

6. The income of nay co-operative society registered under the co-operative societies Act, not being income from any trade or business carried on by the society and with it members.

7. Any such withdrawn or received by an employee form a pension, provident or other retirement benefits fund, society or scheme approved by the Board.

8. The interest accruing to a person on foreign currency domiciliary accounts.

Self Assessment Exercise 3.5

List five kinds of income exempted from tax.

Personal Income Tax Rates

To arrive at the tax payable, the chargeable income of a person as determined will be assessed to tax at graduated rates prescribed in the sixth schedule to the PITD s 37. The following tax rates have been applied over the years.

(From 1st January 1998 to 2000)

	Taxable Income	Rate	Tax Payable
First	N20,000	5%	N1,000
Next	N20,000	10%	N2,000
Next	N40,000	15%	N6,000
Next	₦40,000	20%	₦8,000

For every naira above ₦120,000 at 25%

(From 1st January 2001 to Date)

	Taxable Income	Rate	Tax Payable
First	₦30,000	5%	₦1,500
Next	₦30,000	10%	₦3,000
Next	₦50,000	15%	₦7,500
Next	₦50,000	20%	₦10,000

For every naira above N160,000 at 25%

Example:

Gottage has a chargeable income of N1,200,000 for the 2001 assessment year. Calculate the amount of income tax payable

	Income Chargeable	Rate	Tax Payable
	₦		
First	₦30,000	5%	₦1,500
Next	₦30,000	10%	₦3,000
Next	₦50,000	15%	₦7,500
Next	N50,000	20%	₦10,000
Balance	₦1,040,000	25%	₦260,000
	₦1,200,00		₦282,000

Self Assessment Exercise 3.6

Mr. Osaro has a chargeable income of N800,000 for the 2000 assessment year. Calculate the amount of income tax payable.

4.0 CONCLUSION

In this unit, we discussed the taxation of income. We started by looking at the personal tax payer and proceeded to the determination of residence, guide to determination of residence in Nigeria, artificial transactions, income exempted from tax and finally, the personal income tax rates.

5.0 SUMMARY

You should recall that a personal tax payer can be broadly classified into the person in paid employment and the person who is self employed.

In order to establish the relevant tax authority of a tax payer for any year of assessment, it is imperative to determine the residence of the tax payer. During the course of discussion n this unit, we discussed the rules that guide the determination of residence in Nigeria such as foreign employment, Nigerian employment, others employments, pension, earned income other than from employment or pension, unearned income and corporation sole or body of individuals.

Where a tax authority considers a transaction to be artificial, the tax authority may disregard such transaction or disposition.

To arrive at the tax payable, the chargeable income of a person as determined will be assessed to tax at graduated rates.

6.0 TUTOR MARKED ASSIGNMENT

1. Explain the rules that guides the determination of residence in Nigeria under the following condition:

   a. Foreign employment
   b. Nigerian employment
   c. Pension
   d. Unearned income
   e. Body of individual

2. a. In order to establish the relevant tax authority, it is required to determine the residence of the tax payer. Explain?
   b. Explain the term "relevant tax authority"

3. Mr. Charles has a chargeable income of N700,000.00 for the 2000 year of assessment. Calculate the amount of income tax payable.

Solution

	Taxable Income	Rate	Tax Payable
First	₦20,000	5%	₦1,000
Next	₦20,000	10%	₦2,000
Next	₦40,000	15%	₦6,000
Next	₦40,000	20%	₦8,000
Balance of	₦580,000	25%	₦145,000
	₦700,000		₦162,000

7.0. REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 4 BASIS PERIOD OF ASSESSMENT

CONTENT

1.0 INTRODUCTION

The basis period of assessment is the period in which a tax authority assesses a tax payer. Each tax year is called an assessment year. It runs from 1st January to 31st December every year. The assessable income of any individual is the amount of the income for the year immediately preceding the year of assessment. This is what is referred to as the preceding year basis of assessment. For example, s self-employed trader makes up his accounts regularly to 30th June, every year. The basis period and relevant years of assessments will be as follows:

Year of Assessment	Basis Periods
1995	12 months ended 30/6/94
1996	12 months ended 30/6/95
1997	12 months ended 30/6/96
1998	12 months ended 30/6/97
1999	12 months ended 30/6/98

This is how the tax payer would be assessed as long as prepares his accounts to a period of twelve months to 3oth June every year. However, exemptions to this rule are:

1. On the commencement of a new trade
2. On cessation of a trade
3. On a change in accounting date

These exempted circumstances shall be the focus of this unit. However, you should note that the preceding year rule does not apply to income from employment or pension. That would be treated in a subsequent unit.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Compute assessable profits for the commencement of a business and advice whether the tax payer should take election or to

2. Compute assessable profits for the penultimate and ultimate year of assessment

3. Compute assessable profit for old accounting date an new accounting date an state the one a relevant tax authority will choose.

3.0 MAIN CONTENT

3.1 Commencement of a Trade

A person who carries on a trade, business, profession or vocation will be assessed to tax on the assessable income arising from such activity. For a trade or business already in existence, such assessable income will be ascertained on the preceding year basis. This means that the assessable income for a relevant year of assessment will be that of the preceding year.

However, when the trade or business is now just commencing, the assessable income will be ascertained on a different basis for the first three years of assessment. After which, it maintains the normal preceding year basis. The assessable income of the first three years of assessment of a new trade or business will be determined as follows:

1. First year of assessment in which trade commences. The assessable income shall be the amount of the income from the date of commencement to the following 31st December. For instance, assuming a trader commenced his business 1st October 2007 and makes his account to 31st March every year. He would be assessed for the first year as follows

Year of assessment	Basis Period
2007	1/10/07 to 31/12/07 – 3 months

Second year of assessment

Assessment income shall be the income of the first twelve months of trading. Union the trader above in (1), he would be assessed for the second year as follows:

Year of assessment	Basis Period
2008	1/10/07 to 31/9/08 – 12 months

Third year of assessment

The income assessable shall be the income of the account during year that ended in the preceding year of assessment. That is, the normal preceding year basis. If there is no accounting period of twelve months in length ending in the preceding year, the income of the first twelve months of trading is taken, repeating the second years' assessment. Using the same example, the third year of assessment would be as follows:

Year of assessment	Basis Period
2009	1/10/07 to 31/12/08 – 12 months

The third year of assessment should be on preceding year basis which should cover a twelve-month period. However, form the above example; it is evident that there is o accounting period of twelve months in length ending in the preceding year, therefore, the second year's period was a repeated for the third year of assessment. The next set of assessments will be as follows:

Year of assessment	Basis Period
2010	1/04/08 to 31/03/09 – Preceding year
2011	1/04/09 to 31/03/10 Preceding year

and so on.

Another point that you should note is that the tax payer has a right to elect to have the second and third years of assessment based on actual results for those years. He must apply for both years if election is made and not one without the other. The election will usually be made when it will be more beneficial to the taxpayer. You should note that whether the election is made or not, there would be o effect on the first, fourth and subsequent years.

Example:

Mr. Osaro commenced business on 1st July, 2003 and has the following profits adjusted for tax:

01/07/03 to 31/03/04 ₦65,000
01/04/04 to 31/03/05 ₦70,000
01/04/05 o 31/03/06 ₦60,000

On normal basis the assessment would be

Year of assessment	Basis Period	Assessable Income
		₦
200301/07/03 to 31/12/03	43,333	
	(65,000 x 6/9)	
200401/04/09 to 31/03/10	82,500	
	(₦65,000 + (70,000 x 3/12))	
2005	01/07/03 to 31/08/04	82,500

The 2005 year of assessment should be based on a preceding year. However, because in this case, there is no 12 – month accounting period that ended in the preceding assessment year, the assessment of 2004 year of assessment which is the end year of assessment was repeated.

2006	01/04/04 to 31/03/05	70,000
2007	01/04/05 to 31/03/06	60,000

If election is made, the assessments will be altered to the following:

Year of Assessment	Basis of Period	Assessable Income
2003	01/07/03 to 31/12/03	43,333
	(nothing changed)	

2004	01/01/04 to 31/12/04 ((3/9 x 65,000) + 9/12 x 70,000))	74,167
2005	01/01/05 to 31/12/05 (3/12 X 70,000 + 9/12 x 60,000)	62,500
2006	01/04/04 to 31/03/05 (no change – Preceding year)	70,000
2007	01/04/05 to 31/03/06 (no change – Preceding year)	60,000

The assessments for the second and third years of assessment can be compared in the two circumstances above, namely:

Without Election		With Election	
Year of Assessment	Assessable Income	Year of Assessment	Assessable Income
2004	82,500	2004	74,167
2005	<u>82,500</u>	2005	<u>62,500</u>
	<u>165,000</u>		<u>136,667</u>

Difference = 165,000 – 136,667 = 28,333

To the advantage of the taxpayer, election will be made by the tax payer.

Self Assessment Exercise 4.1

Tunde commenced a trade on 1st April, 2000 and has the following profits adjusted for tax.

01/04/00 to 31/01/10	₦90,000
01/02/01 to 31/01/02	₦100,000
01/02/02 to 31/01/03	₦80,000

You are required to compute the assessable income for the relevant years of assessment if the tax payer was to make an election, would you advise the tax payer to make the election?

3.2 Cessation of a Trade

As you would recall from the introduction of this unit, the second instance when the preceding year basis rule is not followed s when a business ceases permanently. Where a person permanently ceases to carry on a trade, business, profession or vocation in Nigeria, any assessable income accruing to such a trade or business with the last two years of assessment up to the point of cessation shall be determined as follows:

1. The assessable income for the year of assessment preceding that in which the cessation occurs shall be either ;

a. The actual income of the year, or

b. The income of the preceding year
Whichever, is higher. The year of assessment preceding that in which the cessation occurs is known as the per ultimate year.

2. The assessable income for the year of assessment in which the cessation occurs shall be the amount of income of that year. That is, form 1st January of that year to date of cessation. The year of assessment in which the cessation occurs is known as the ultimate year.

   You should note that the power to revise the assessment of the penultimate year is the exclusive right of the relevant tax authority. This is unlike what happens in the case of the commencement of a trade or business, where the option to revise the assessment of the second and third year lies with the tax payer.

Example

Mr. Maxwell who engages in tomatoes selling business had regularly made up his annual accounts to 31st August each year. He permanently ceased his business on 31st December, 2004. His adjusted profits for the last four years were as follows:

Year ended 31/08/02	N300,000
Year ended 31/08/03	N200,000
Year ended 31/08/04	N150,000
Period to 31/1/04	N70,000

You are required to compute the assessable income for the relevant years

Solution

Original Assessment

Year of Assessment	Basis of Period	Assessable Income
2003	01/09/01 to 31/08/02	N300,000
2004	01/09/02 to 31/08/03	N200,000
2005	01/09/03 to 31/08/04	N150,000

Final Assessment

Year of Assessment	Basis of Period	Assessable Income
2003(Per ultimate year	01/07/03 to 31/12/03	N183,333
	(8/12 X 200,000 + 4/12 x 150,000)	
2003	01/09/01 to 31/08/02	N300,000
2004	01/01/04 to 31/01/04	N170,000
	(8/12 x 150,000 + 70,000)	

Remark: The Relevant Tax authority will take the higher of N300,000 and N183,333 for the per ultimate year.

Example:

Cosmix Enterprises is bird feed producing business. It decided to close down permanently on 30th September, 2007 after several years of operation.

The total profits of the enterprises were as follows:

Year ended 31/12/04	N560,000
Year ended 31/12/05	N300,00
Year ended 31/12/06	N270,000
Period to 30/09/07	N140,000

You are required to compute the original and revised assessments and State what option the tax authority may have, if any.

Solution

Cosmix Enterprises

Original Assessment

Year of Assessment	Basis of Period	Assessable Income
2005	01/01/04 to 31/12/04	N560,000
2006	01/01/05 to 31/12/05	N300,000
2007	01/01/06 to 31/12/06	N270,000

Final Assessment

Year of Assessment	Basis of Period	Assessable Income
2006	01/07/03 to 31/12/03	N270,000
	or	
	01/01/05 to 31/12/05	N300,000
2007	01/01/07 to 30/09/07	N140,000

Remark: Since the original assessable income for the ultimate and penultimate years pt together is higher than the revised assessment, the original assessment made by the tax authority will stand.

Self Assessment Exercise 4.2

Mr. Decided to permanently cease his trade. On 1st August 2002 after trading for several years. The total profits of the enterprise were as follows:

Year ended 31/11/99	N400,000
Year ended 31/11/00	N250,000
Year ended 31/11/01	N200,000
Period to 31st August 2002	N120,000

You are required to compute the original and revised assessments and state what option the tax authority may have, if any.

3.3 Change of Accounting Date

An accounting period has to fulfill three conditions before it can be accepted as the basis period for a year of assessment in the normal preceding year basis of assessment, viz:

1. it must be for a period of twelve months

2. it must run from the commencement o the trade or from the end of the accounting period on which he previous assessment was based.

3. it must be the only accounting period ending in the previous year o assessment.

When these requirements are not satisfied, which do happens when there is a change of accounting date, the relevant tax authority has the power to compute the assessable income as they consider appropriate. Such assessable income would be for:

1. the assessment year in which the change occurs and
2. the next two years of assessment following that in which the change occurs.

The normal procedure is that the relevant tax authority will compute the assessable profits for the relevant years' bases on the assumption that the taxpayer still makes up its accounts to the old accounting date. This could be compared with the assessable profits computed on the assumption that accounts are made up to the new accounting date for all relevant years. You should note that the preceding year basis rule would still be applicable in both circumstances. The relevant tax authority will obviously choose the alternative that produces higher assessable profit and therefore higher income to the government.

Example:

Okoro has for several years prepared his accounts u to 30th April. He failed to make up is accounts to 30th April in 2004 in which year the accounts were made up to 31st December?

Available figures of profits are as follows:

Adjusted Profits	N
12 months ended 30/04/03	N80,000
20 months ended 31/12 04	N120,000
12 months ended 31/12/05	N100,000
12 months ended 31/12/06	N140,000

Solution

Alternative one: The relevant tax authority may decide on a basis period ending 30th April. That is, using the former accounting date. This would be calculated for the year. Okoro failed to make up his account to 30th April (i.e. 2004) and the following two years.

Year of Assessment	Basis of Period	Assessable Income
2004	01/05/02 to 31/04/03	N80,000
2005	01/05/03 to 30/04/04	N72,000
	(12/20 x 120,000)	
2006	01/05/03 to 30/04/05	N81,333
	(8/20 x 120,000 + 4/12 x 100,000)	
Total amount for the three years		N233,333

Alternative two: The relevant tax authority may decide on a basis period ending 31st December. That is, using,

Year of Assessment	Basis of Period	Assessable Income
2004	01/01/03 to 31/12/03	N74,667
	(4/12 x 80,000+ 8/20 x 120,000)	
2005	01/01/04 to 31/12/04	N72,000
	(12/20 x 120,000)	
2006	01/01/05 to 31/12/05	N100,000
Total amount for the three years		N246,667

The tax authority will opt for alternative two which produces higher assessable profits of N46,667 than the N233,333 in alternative one for all three years of assessment.

You should note that the preceding year basis rule will still be observed for both alternatives and the whole three years must be taken together in each alternative for the comparison.

Example 2:

Mr. Effiong is a rice distributor based in Calabar. He has been in the rice distribution business since 1995, making up his accounts to 30th June each year. Following 30th June 2006, he decided to change his accounting date to 30th September. The following represents the summary of his adjusted profits.

	₦
12 months ended 30/06/05	N60,000
15 months ended 30/09/06	N80,000
12 months ended 30/09/07	N70,000
12 months ended 30/09/08	N90,000

You are required to show the tax implications of the change in accounting date using the above information.

Solution:

Alternative one: The relevant tax authority decides on a basis period ending 30th June.

Year of Assessment	Basis of Period	Assessable Profits
2006	01/07/04 to 30/06/05	N60,000
2007	01/07/05 to 30/06/06	N64,000
	(12/15 x 80,000)	
2008	01/07/06 to 30/06/07	N68,500
	(3/15 x 80,000 + 9/12 x 70,000)	
Total amount for the three years		N192,500

Alternative two: The relevant tax authority may decide on a basis period ending 30th September.

Year of Assessment	Basis of Period	Assessable Profits
2006	01/10/04 to 30/09/05	N61,000
	(9/12 x 60,000 + 3/15 x 80,000)	
2007	01/10/05 to 30/09/06	N64,000
	(12/15 x 80,000)	
2008	01/10/06 to 30/09/07	N68,500
Total amount for the three years		N195,000

Here, the tax authority will opt for alternative two which produces higher assessable profits of N195,000 than the N192,500 in alternative one for all three years of assessment.

Self Assessment Exercise 4.3

Mr. Felix has for several year prepared his accounts up to 30th September. He failed to make up his accounts to 30th September in 2004 in which year the accounts were made up to 31st December.

Available figure of profits are as follows:

12 months ended 30/09/03	N90,000
15 months ended 31/12/04	N150,000
12 months ended 31/12/04	N80,000
12 months ended 30/09/04	N120,000

You are required to show the tax implications of the change in acconting date using the above information.

4.0 CONCLUSION

In this unit, we discussed the basis period of assessment which is normally on a preceding year basis. The focus was those situations that woud warrant exemption to this rule, which are the commencement of a new trade, cessation of a trade nd change in accounting date.

5.0 SUMMARY

You should recall that when computing for the commencement of business. For the first year of assessment, the assessable profit shall be the amount of profit from the date of commencement to the following 31st December. For the second year of assessment, the assessable profit shall be the amount of profit for the first twelve months of trading. For the third year of assessment, the assessable profit shall be the profit of the accounting year that ended in the preceding year of assessment. In the case of a cessation of business, the assessable profit for the year of assessment preceding that in which the cessation occurs shall be either the actual profit of the year or the income of the preceding year, whichever is higher. While the assessable profit for the year of assessment in which the cessation occurs shall be the amount of profit for that year.

When treating the case of change of accounting date, you should bear in mind that the relevant tax authority would choose the higher assessable profit between accounts made p to the old accounting date and accounts made up to the new accounting dates.

6.0 TUTOR MARKED ASSIGNMENT

1. Mr. Okamafe commenced a business on 1st April, 2003 and has the following profits adjust for tax:

01/04/03 to 28/02/04	N200,000
01/03/04/ to 28/02/05	N250,000
01/03/05 to 28/02/06	N180,000.

You are required to compute the assessable profit for the relevant years of assessment. If the tax payer was to make an election, would you advise the tax payer to make the election?

2. Mr. Okere who engages in cement distribution business had regularly made up his annual accounts to 31 May each year. He permanently ceases his business on 30th September, 2007. His adjusted profits for the last few years were as follows;

Year ended 31/05/05	N450,000
Year ended 31/05/06	N300,000
Year ended 31/05/07	N250,000
Period to 31/09/07	N60,000

You are required to compute the original and revised assessments and state what option the tax authority may have, if any.

3. Mr. Osaeze is a trader. He has been in the trade since 2001, making up his accounts to 30th September each year. Following 30th Sptember, 2008, he decided to change his accounting date to 31st December. The following represents the summary of his adjusted profits.

12 months ended 30/09/07	N80,000
15 months ended 31/12/08	N120,000
12 months ended 31/12/09	N90,000
12 months ended 31/12/10	N110,000

You are required to show the tax implications of the change in accounting date using the above information.

7.0 REFERENCES/FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 5 TAXATION OF EMPLOYEES

CONTENT

1.0 INTRODUCTION

Income tax due on income from employment is collected under the pay-as-you-earn (PAYE) system. Each month, the employer deducts tax at source from each employee's earnings and remits it to the relevant tax authority and pay the net amount to the employees.

Income arising from employment or pension is deemed to have arisen on a daily basis over a given period, and is assessed to tax on actual year basis (AYE).

Where income paid to employees is derived from bonus, commission or allowance payable on one occasion only or at intervals exceeding one month, it shall be deemed to have arisen on the day that I sis actually paid, unless the employment from which it accrued has ceased to exist, in which case it shall be deemed t have arisen on the last day of the employment including any terminal leave, arising therefrom. The implication therefore, is that income from employment derivable from any bonus, commission or allowance shall be assessable to an actual year basis, to the extent that is payable on only one occasion or at intervals exceeding one month. Where that is the case, such income would be assessed to tax on the date that is actually paid, unless the employment has ceased to exist, in which case the last day of such employment, including any terminal leave, shall be the date that such income shall deemed to have been paid.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. State the circumstances under which an employee income is not taxable;

2. Explain according to relevant law the earned income exempted from tax;

3. State the relevant provision in which income from employment is deemed to be derived from Nigeria;

4. Describe the treatment of tax deduction in respect of newly employed employees and employers leaving an employment or a branch.

3.0 MAIN CONTENT

3.1 Employees' Non-taxable Income

The employees' income is not taxable under the following circumstances:

1. Where the income represents reimbursement to the employee of expenses incurred by him in the performance of his duty and form which it is not intended that he should make any profit.

2. The sums paid in respect of medical or dental expenses incurred by the employee.

3. Amount paid in respect of the cost of passage to or from Nigeria incurred by the employee.

4. Amount paid in respect of the maintenance or education of a child if the income tax law of the relevant tax authority provides that any such amount received by the employee during a year of assessment shall be deducted from the personal reliefs to be granted to him in the following year.

5. Any compensation for loss of employment.

6. So much of nay amount of rents the employee is treated as being in receipt of equal to the annual amount deemed to be incurred by the employer under section 5 of the Act.

7. So much of any amount of rent the employee is treated as having received under the provision of section 6 of the Act.

8. Rent allowance paid by the employer to the employee subject to the following restrictions. (with effect from 1992).

   (a) Lagos Area and Federal Capital Territory, Abuja – 28% of the annual basic salary subject to a maximum of N10,000 per annum.

   (b) State Capitals – 28% of annual basic salary subject to a maximum of N6,000 per annum.

   (c) Other places – 28% of annual basic salary subject to a maximum of N4, 000 per annum

   With effect from 1st January 1996, rent allowable for tax purposes in respect of residential accommodation was limited to the actual rent paid subject to a maximum of 100% of the staff basic salary.

In 1998 – 2000, rent allowable was subject t maximum of N100,000 per annum.

With effect from 2001, it was subject to a maximum of N150,000 per annum.

9. Motor vehicle allowance paid to an employee up to a maximum of N2,436 per annum with effect from 1st January 1992.

In 1998 – 2000, it was subject to maximum of N15,000. With effect from 2001, it was N20,000 per annum.

Self Assessment Exercise 5.1

State five non-taxable income of an employee.

3.2 Earned Income Exempted from Tax

The earned incomes of certain categories of workers are exempted from tax by the relevant tax Act.

With effect from 1st January 1993, workers earning N5,000 per annum and below were exempted from tax. In January 1995, the level of workers earned income exempted from tax was increased to N7,500. It was increased further to N10,000 per annum from 1st January, 1996. From 1st January 1998, the level of workers income exempted from tax was increased further to N30,000 per annum.

You should note that a worker's earned income exempted from tax comprises of his basic salary, plus allowances and any other remuneration derived from such employment. Exemption of earned income from tax applies only to persons whose source of income for any year of assessment is from employment what is, applicable only to individuals in paid employed. You should also note that, although workers exempted from tax will not be required to fill any tax return, they are not exempted from payment of minimum tax, which would be 0.5% of their total income. Thus, in the case of the N30,000 ax-free earned income limit introduced on 1st January, 1998, the minimum tax payable will be N150 per annum.

Self Assessment Exercise 5.2

With effect from 1993 to 1998, what is the state of earned income exempted from tax?

3.3 Income from Employment Deemed to be derived from Nigeria

The gains of profits from an employment shall be deemed to be derived from Nigeria if:

1. The duties of the employment are wholly or partly performed in Nigeria, unless;

   i. the duties are performed on behalf of an employer who is in a country other than Nigeria

ii. the employee is not in Nigeria for a period or periods amounting to 183 days or more in an twelve month period commencing in a calendar year and ending either within that same year, or the following year, and

iii. the remuneration of the employee is liable to tax in that other Country.

2. The person s a non-resident who:

i. has a fixed base in Nigeria from where he carried on such trade or business, he should be assessed and charged on such fair and reasonable percentage of the turnover attributable to that fixed base

ii. operates the trade or business through a person in Nigeria authorised to conclude on his behalf or on behalf of some other person related to him or both of whom are controlled by some other person. He should be assessed and charged on such fair and reasonable percentage of the turnover of the business or

iii. habitually maintain a stock of goods in Nigeria from which deliveries are regularly made on his behalf. He should be assessed and charged on such fair and reasonable percentage of the turnover of that contract: or

iv. carries on the trade or business in Nigeria with another person related to him or both of whom are controlled by some other persons and such that conditions are made or imposed between such persons in their commercial or financial relations which in the opinion of the relevant tax authority id seemed to be artificial or fictitious. He should be assessed and changed on a fair and reasonable percentage of the turnover of the trade or business as the relevant tax authority may determine.

Despite the provision of paragraph 2, above, the gains or profits form an employment by a Government in Nigeria shall be deemed to be derived from Nigeria irrespective of where he remuneration is paid if the employee performs the duties of that employment in a country other than Nigeria that exempts the employee from tax a those gains or profits under an agreement or diplomatic usage.

Notwithstanding any of the foregoing provisions, the gains or profits of an individuals from any employment as a seafarer, other than any such employment in the Nigerian Navy or by the Nigerian Ports Authority, shall be deemed to be derived from Nigeria only during any period in which the individual is serving under articles which he has signed in Nigeria or is performing standby duty on board a ship preparatory to his signing articles in Nigeria.

Self Assessment Exercise 5.3

State the relevant provision in which an income from employment is deemed to be derived in Nigeria.

3.4 Tax Deduction in respect of Leaving Employees

If an employee for whom the employer holds a tax deduction card leaves an employment before the end of a tax year, the employer will complete his tax deduction card up to an including the month of leaving and the terminal remuneration paid. The card would be marked "left" with the date of leaving also noted thereon. This will be retained by the employer until the end of the tax year.

A "Leaving Certificate" on form E will be prepared in respect of the leaver with the first copy being forwarded to the relevant tax authority immediately. The second copy will be given to the employee who will be presented to his new employer if any.

Where an employee becomes unemployed any refund due to him after his last pay day will be arranged by the relevant tax authority.

If an employee is transferred from one branch to another in the same employment and within the jurisdiction of the same tax authority, a leaving certificate need not be prepared. If the other branch falls within the territory of another tax authority, a leaving certificate will be prepared unless there is a centralised pay-roll for all the branches of the employer. If an employee dies, form E will be prepared and all copies forwarded to the relevant tax authority.

Self Assessment Exercise 5.4

Describe the treatment of tax deduction for an employee leaving an employment or a branch.

3.5 Tax Deduction in respect of New Employees

When an employee is newly employed, he would be requested to produce the second copy of the leaving certificate prepared by his former employer if any. If he has no previous employment, he will have to apply to the relevant tax authority for a tax deduction card on the basis of which the amount of tax due from him will be computed.

If a leaving certificate is produced, the employer will obtain the second copy from the employee and forward this to the relevant tax authority after completing necessary formalities. Where no leaving certificate is produced, the employer should immediately prepare an emergency card. Tax should then be deducted in accordance with the instructions on the emergency card until a tax deduction card or further directions are received from the relevant tax authority.

Self Assessment Exercise 5.5

Describe the treatment of tax deduction for an employee who is new in an employment.

4.0 CONCLUSION

In this unit, we discussed taxation of employees. We started by looking at employees' non-taxable income and proceeded to earned income exempted from tax, income from employment deemed to be derived from Nigeria, tax deduction in respect of leaving employees and finally, tax deduction in respect of new employees.

5.0 SUMMARY

You should recall that income tax due on income from employment is collected under the pay-as-you-earn (PAYE) system. Some employees' income is not taxable under certain circumstances. The earned incomes of certain categories of workers are exempted from tax by the relevant tax Act.

If an employee for whom the employer holds a tax deduction card leaves an employment before the end of a tax year, the employer will complete his tax deduction card up t an including the month of leaving and the terminal remuneration paid.

When an employee is newly employed, he would be requested to produce the second copy of the leaving certificate prepared by his former employer if any.

6.0 TUTOR MARKED ASSIGNMENT

(1) State five non-taxable income of an employee.

(2) State the relevant provision in which an income from employment is deemed to be derived in Nigeria.

(3) Describe the treatment of tax deduction for an employee leaving an employment or branch.

7.0 REFERENCES/ FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 6 TAXATION OF SELF EMPLOYED

CONTENT

1.0 INTRODUCTION

In the previous unit, we discussed taxation of employees. In this unit, we shall be discussing taxation of the self employed individual. The self employed includes individuals who engages in a trade, business, profession or vocation such as an Accountant, Architects, Engineers, Doctors, Lawyers who are in private practice as well as owners of supermarkets, business centers, fast food/restaurants, bookshop etc.

These self employed individuals make profits from their trade, business, profession or vocation which constitutes taxable income. The taxable income of the self employed is assessed to tax on preceding year basis (PYB). This is because any assessment to tax of a self employed individual can only take place after his financial year has ended.

2.0 OBJECTIVES

After studying this unit, you should be able to:

(1) List some of the allowable and disallowable expenditure.
(2) List some funds, bodies and institutions approved for tax purposes to which donations could be made.
(3) Calculated adjusted profits from a financial statement.

3.0 MAIN CONTENT

3.1 Allowable Expenditure

The self employed taxable income is an outcome of the individual generated revenue which was set against expenses. For an expense incurred by the self employed to be allowed for tax purposes, it must have been incurred wholly exclusively, necessarily and reasonably for the purpose of such trade or business.

The following are specifically allowed under S.20 of PITD.

(i) A sum payable by way of interest on money borrowed and employed as capital in acquiring the income.

(ii) Interest in loans for developing an owner-occupied residential house.

(iii) Rent for that period and premiums the liability for which was incurred during that period, payable in respect of land or buildings occupied for the purpose of acquiring the income.

(iv) Any expense incurred for repair of premises, plant, machinery or fixtures employed in acquiring the income, or for the renewal, repair or alteration of any implement, utensil or article so employed.

(v) Bad debts incurred in any trade, business, profession or vocation, proved to have become bad during the period for which the income is being ascertained, and doubtful debts to the extent that they are respectively estimated to have become doubtful during the said period, notwithstanding that such bad or doubtful debts were due and payable prior to the commencement of the said period.

(vi) A contribution or abatement deducted from the salary or pension of a public officer under the pension Act, or under any approved Scheme within the meaning of the Act, and any contribution, other than a penalty, made under the provisions of any Act establishing a National Provident Fund or other retirement benefits scheme for employers throughout Nigeria.

(vii) A contribution to an approved pension, provident or other retirement benefits fund, society or scheme subject to the provisions of the 4^{th} Schedule to the Decree or Act, and such conditions as the relevant tax authority in its absolute discretion may prescribe.

(viii) The accrual principle shall be observed for the purpose of determining the expenses that are allowable deductions for the purpose of the trade, business, profession or vocation.

(ix) Any expense which is proved to the satisfaction of the relevant tax authority to have been incurred by the individual on research for the period including the amount of levy paid by him to the National Science and Technology Fund.

Self Assessment Exercise 6.1

State five allowable expenses of self employed as stated in Section 20 of PITD.

3.2 Disallowable Expenditure

Section 21 contains a list of expenses specifically prohibited b the Decree. These are:

1. Domestic or private expenses
2. Capital withdrawn from a trade, business, profession or vocation and any expenditure of a capital nature.
3. Any loss or expenses recoverable under insurance or content of indemnity
4. Rent of or cost of repairs to any premises or part of premises not incurred for the purpose of producing the income.
5. Taxes on income or profits levied in Nigeria or elsewhere
6. Payments to pension, provident, savings or widows and orphans society, fund or scheme not approved by the relevant tax authority.
7. Depreciation of nay asset
8. Any sum reserved out of profits except allowable bad and doubtful debts provision.
9. Any expense of any description incurred within or outside Nigeria for the purpose of earning management fee unless prior approval of an agreement giving rise to such management fee has been obtained from the Minister.
10. Any expense whatsoever incurred within or outside Nigeria as management fee under any agreement entered into after the commencement of this paragraph except to the extent that the Minister may allow.

Self Assessment Exercise 6.2

State five disallowable expenses of self employed as stated in section 21 of PITD.

3.3 Further Discussions of Allowable and Disallowable Expenditure

Some expenses incurred in the course of running a business might not be among those stated in section 20 and 21 of PITD 1993. The extent to which such expenses would be allowed or disallowed for tax purposes would depend on factors such as existing income tax practices and decided law cases. Let us examine some of these items of expenditure.

1. Legal expenses – These expenses are usually incurred in respect of a wide range of under-takings. While some may be allowable, other may not be allowable for tax purposes.
2. The following legal expenses are usually allowable:

a. Expenses incurred on debt collection or recovery
b. Expenses incurred in renewing short-term leases (i.e. leases less than fifty years)
c. Expenses incurred in rating valuation appeals
d. Expenses incurred in getting rid of an irresponsible or difficult employee or director.
e. Expenses incurred in defending the title of a business to any of its assets or the maintenance of existing trade rights.
f. Expenses incurred in preparing staff service agreements
g. Expenses incurred in the successful defence of a traffic offence charge

3. The following legal expenses are usually disallowable:

    a. Expenses incurred in challenging income tax assessments, whether or not the taxpayer wins the dispute.
    b. Expenses incurred in respect of the acquisition of a new fixed asset
    c. Expenses incurred in respect of a lease taken out for the first time
    d. Expenses incurred in the renewal of long-term leases
    e. Expenses incurred on issue of share capital

4. Penal Liabilities – Penal Liabilities such as fines for traffic offences or tax penalties on employees are usually disallowable, since they do not constitute trade or business expenses.

5. Entertainment expenses – These are allowable where they are customary, vouched and are wholly, exclusively, necessary and reasonable for purposes of entertaining clients or customers. Expenses incurred in providing entertainment for employees during festive periods such as Christmas are also allowable, provided they are reasonable. What would be regarded as reasonable under the circumstances is usually worked out with the tax authorities.

6. Subscription to trade associations, funds societies etc. Subscription may be allowed or disallowed depending on their nature and the purposes to which they are applied. Subscriptions paid to trade associations and the Armed Forces Comfort Fund are normally allowable expenses. Subscriptions paid to a political party fund and societies such as social clubs, cultural groups and sports such as social clubs, cultural groups and sports club e.t.c. are usually disallowable expenses.

7. Donations – Donations made by a trade or business are usually treated as disallowable expenses, for tax purposes. However, donations made to certain Funds, Bodies or Institutions list under the fifth schedule to the companies Income Tax Act, (CITA), 1990 may be allowed. Certain conditions must be met before donations to such funds, Bodies or Institutions would be allowed. The conditions are as follows:
    a. The donations must be made out of the profits of the company. Thus if the company makes a loss rather than a profit, any donation made by it would be treated as a disallowable expenses for tax purposes.

    b. The donation should not be an expenditure of a capital nature

c. The donation should not exceed 10% of the total profits of the company before any deduction for the donation is made.

Self Assessment Exercise 6.3

1. List four allowable and disallowable legal expenses each.

2. Discuss the position of tax authority in respect of the following expenses

   a. Penal Liabilities
   b. Entertainment Expenses
   c. Subscription
   d. Donation.

3.4 List of Approved Funds, Bodies and Institutions

The list of approved funds, Bodies and Institutions to which donations could be made under the 5^{th} schedule of CITA 1990 is as follows:

1. The Boys Brigade of Nigeria
2. The Boys scouts of Nigeria
3. The Christian council of Nigeria
4. The Cocoa Research Institution of Nigeria
5. Any educational institution affiliated under any other educational institution recognized by any Government in Nigeria.
6. The Girl Guides of Nigeria

7. Any hospital owned by the Government of the Federation or of a state or any University Teaching Hospital or any hospital which is carried on by a society or association otherwise than for the purpose of profits or gains to the individual members of that society or association.

8. The Institute of Medical Laboratory Technology
9. The National Commission for rehabilitation
10. The National Library
11. The Nigerian Council for Medical Research
12. The National Science and Technology Development Agency
13. The Nigerian Institute for International Affairs
14. The Nigerian Institute for Oil Palm Research
15. The Nigerian Institute for Trypanosomiasis Research
16. The Nigerian Museum
17. The Nigerian Red Cross

18. A public fund established and maintained for providing money for the construction or maintenance of a public memorial relating to the civil war in Nigeria which ended on 15^{th} January, 1970.

19. A public institution or public fund (including the Armed forces Comfort Fund) established or maintained for the comfort, recreation or welfare of members of the Nigerian Army, Navy or Air Force.

20. A public fund established and maintained exclusively for providing money for the acquisition, construction, maintenance or equipment of a building used or to be used as a school or college by the Government of the Federation or State or by a public authority or by a society or association which is carried on otherwise than for the purpose of profit or gain to the individual members of that society or association.

21. The National Youth Council of Nigeria
22. The National Sports Commission and its States Associations
23. The Nigerian Society for the Deaf and Dumb
24. The Society for the Blind
25. The Nigerian National Advisory Council for the Blind
26. Associations or Societies for the Blind in Nigeria
27. Training Centers and Residential Schools for the Blind in Nigeria.
28. The National Braille Library of Nigeria
29. The Nigerian Youth Trust
30. Van Leer Nigerian Educational Trust
31. Southern Africa Relief Fund
32. Islamic Education Trust
33. The Institute of Chartered Accountants of Nigeria Building Fund

34. Any public fund established or approved by the Government of the Federation or established by any of the state Government in aid of or for the relief of drought or any other national disaster in any part of the Federation.

Self Assessment Exercise 6.4

List ten bodies, institutions or Funds approved to which donations could be made under CITA 1990.

3.5 Adjusted Profit

What the relevant tax authorities do in order to arrive at taxable profits is to adjust the financial statements submitted to them by the individual taxpayer taking into consideration those revenue and expenditure items that may not be allowed for tax purposes. The profit figure that the tax authorities finally arrived at after making the necessary adjustments is known as adjusted profit. It is this adjusted profit that is finally assessed to tax by the relevant tax authorities. The pro-forma for computation Adjusted profits is as follows;

XYZ Trading Stores
Computation of Adjusted Profit
For Year ended 31 December, 2001

	₦		₦
Net Profit per accounts			XXX
Add: Disallowable items:			
Depreciation	XX		
Loss on sale of fixed assets		XX	
General provision for bad debts	XX		
Other expenses (not allowable)	XX		XX
			XXX
Deduct: Allowable items:			
Interest on Capital employed	XX		
Profit on sale of fixed Assets	XX		
Others	XX		XXX
Adjusted Profit			XXX

Example:
The profit and loss account of Mogudu Business Enterprises for the year ended 31st December, 2004 was as follows:

	₦	₦
Gross profit from trading		680,000
Profit from sale of Motor Vehicle		12,000
		668,000
Salaries and wages	185,000	
Industrial Training Fund	5, 000	
Trade Subscriptions	3,000	
Legal Expenses	7,400	
Depreciation	90,000	
Rent and Rates	30,000	
Medical Expenses	12,000	
Provision for doubtful debts	7,000	
Electricity Bills	58,000	
Telephone charges	20,000	
Repairs and maintenance	80,000	
Postages and Stationery	6,000	503,400
Net profit		164,600

Additional Information

a. Provision for doubtful debts contains N4,000 being a general provision
b. Repairs and maintenance contains an amount of N15, 000 being cost of erecting a new gate to the business premises
c. Legal expenses comprises of:

₦

Acquisition of new leases	1400
General advice for the business	1500
Collection of debt	4500
	7,400

You are required to compute the adjusted profit of Mogudu Business Enterprises for the year ended 31st, December, 2004

Solution

Mogudu Business Enterprises
Computation of Adjusted Profit
For the ended ended 31st December, 2004

		₦	₦
Profit as per account			164,600
Add:	Legal Expenses (acquisition of new leases)	1,400	
	Depreciation	90,000	
	Provision for doubtful debts		
	- General provision	4,000	
	Repairs and maintenance		
	- New gate	15,000	110,400
			275,000
Less : Profit on sale of fixed asset			(12,000)
	Adjusted Profit		263,000

You should note that the sale of Motor Vehicle is not regarded as income in the computation of adjusted profit since capital allowances was claimed. Thus any balancing charge or allowance will be treated as the real income or loss of the business. Capital allowances shall be discussed in subsequent unit. Again, you should recall that legal expenses incurred on new leases are not allowable. However, subsequent expenses incurred in renewing such leases would be allowable.

Example

The Trading Profit and Loss Account of Titi Business Enterprises for the year ended 30th September, 2006.

		₦	₦
Sales			450,000
Cost of Sales:			
Opening Stock	20,000		
Purchases		130,000	
		150,000	
Closing stock		25,000	125,000
Gross profit			325,000
Profit on Sale of Motor Vehicle			30,000
			355,000

Rent	50,000	
Salaries	85,000	
Legal fees	5,000	
Pension fund	8,000	
Loss on sale of generator	7,500	
Repairs and maintenance	6,000	
Depreciation	12,000	
Provision for Bad and doubtful debts	6,500	
Sundry expenses	7,000	
Entertainment	22,000	
Travelling expenses	9,000	
Income tax	8,000	226,000
Net profit		129,000

Additional information:

a. Salaries comprise of:

1.	Drawings by proprietor	N35,000
2.	Other Staff remuneration	N50,000
		N85,000

b. Legal fees were for:

1.	Debt collection	1,500
2.	Purchase of new warehouse	1,500
3.	General advice on business matter	2,000
		5,000

c. Pension funds consist of:

i.	Employer's contribution to NPF (Approved)	4,000
ii.	Proprietor's premium on life assurance policy	4,000
		8,000

d. Repairs and maintenance comprises of:

a.	Cost of making good the defect in a Generator at the time of purchase	2,000
b.	Repainting of business premises	3,000
c.	Maintenance of business vehicle	1,000
		6,000

e. Provision for bad and doubtful debts contains N3,000 being a general provision.

f. Sundry expenses consist of:

i.	cost of police escort from bank to office	N4,000
ii.	payment to the chamber of commerce	N1,600
iii.	Donation to cocoa Research Institute of Nigeria	N1,400
		N7,000

g. Entertainment consists:

i. vacation abroad by proprietor's wife	N15,000
ii. Entertainment of Customer	N 7,000

N22,000

You are required to compute the adjusted profit of Titi Business Enterprises.

Solution

Titi Business Enterprises
Computation of adjusted profit for the
year ended 30th September, 2006

		₦	₦
Net profit per accounts			129,000
Add:	Salaries-drawings	35,000	
	Legal fees – Purchase of new ware house	1,500	
	Pension fund-Premium	4,000	
	Loss on sale of generator	7,500	
	Repairs and maintenance -generator	2,000	
	Provision of Bad and doubtful debt - General provision	3,500	
	Entertainment -proprietor's wife	15,000	
	Income tax	8,000	
	Depreciation	12,000	88,5000
			217,500
	Less: Profit on sale of Motor Vehicle		30,000
	Adjusted Profit		187,500

Self Assessment Exercise 6.5

The following is an extract from the draft annual accounts of freeborn Business Enterprises, based in Lagos.

Freeborn Business Enterprises
Trading, profit and Loss Account for year ended 31st December, 200

		₦		₦
Sales				540,000
Cost of Sales				
Opening Stock	35,000			
Purchases		120,000		
		155,000		
Closing stock		40,000	115,000	
Gross profit				425,000
Profit on sale of generator				5,000
				430,000
Expenses				
Salaries		125,000		
Rent		55,000		

Legal fees	6,000	
Pension fund	7,000	
Loss on sale of generator	13,000	
Repairs and maintenance	8,000	
Depreciation	14,000	
Provision for Bad and doubtful debts	8,000	
Sundry expenses	6,500	
Entertainment	30,000	
Travelling expenses	8,000	
Income tax	5,500	286,000
Net profit		144,000

Additional information:

a. Salaries comprise of:

i.	Drawings by proprietor	N25,000
ii.	Other Staff remuneration	N100,000
		N125,000

b. Legal fees were for:

i.	Purchase of new warehouse	2,000
ii.	Debt collection	2,000
iii.	General advice on business matter	2,000
		6,000

c. Pension funds consist of:

i. Employer's contribution to NPF (Approved)	4,000
ii. Proprietor's premium on life assurance policy	3,000
	7,000

d. Repairs and maintenance comprises of:

i. Cost of making good the defect in a Generator at the time of purchase	3,000
ii. Repainting of business premises	4,000
iii. Maintenance of business vehicle	1,000
	8,000

e. Provision for bad and doubtful debts contains N5,000 being a general provision.

f. Sundry expenses consist of:

i. cost of police escort from bank to office	N2,500
ii. payment to the chamber of commerce	N2,500
iii. Donation to cocoa Research Institute of Nigeria	N1,500
	N6,500

g. Entertainment consists:

i. Vacation abroad by proprietor's wife	N20,000
ii. Entertainment of Customer	N10,000
	22,000

You are required to compute the adjusted profit of Freeborn Business Enterprises.

4.0. CONCLUSION

In this unit, we discussed the taxation of self employed. We started by looking at allowable expenditure and proceeded to disallowable expenditure, further discussion on allowable and disallowable expenditure, list of approved funds, bodies and institutions and finally discussed adjusted profits.

5.0 SUMMARY

You should recall that for expenses incurred by the self employed to be allowed for tax purposes, it must have been incurred wholly, exclusively, necessarily and reasonably for the purpose of such trade or business.

Some expenses incurred in the course of running a business might not be among those stated in section 20 and 21 of PITD 1993. The extent to which such expenses would be allowed or disallowed for tax purposes would depend on factors such as existing income tax practices and decided law cases. What the relevant tax authorities do in order to arrive at taxable profits is to adjust the financial statements submitted to them by the tax payers taking into consideration those revenue and expenditure items that may not be allowed for tax purposes. The profit figure that the tax authorities finally arrive at after making the necessary adjustments is known as adjusted profit.

6.0. TUTOR MARKED ASSIGNMENT

1. State five allowable expenses of self employees as stated in section 20 of PITD

2. List ten Funds, bodies or institutions approved to which donations could be made under CITA 1990.

3. The trading, profit and loss account of Markurdi Business Centre for the year ended 30th September, 2009 are as follows;

Makurdi Business Centre
Trading, Profit and Loss Account for the year ended 30th September, 2009

	₦	₦
Sales		380,000
Cost of sales		
Opening Stock	15,000	
Purchases	85,000	
	100,000	
Closing stock	20,000	80,000
Gross profit		300,000
Expenses		
Salaries and Wages	85,000	

Trade Subscriptions	3,000	
Legal expenses	7,000	
Depreciation	60,000	
Rent	30,000	
Provision for doubtful debts	7,000	
Electricity Bills	15,000	
Telephone Charges	5,000	
Repairs and maintenance	40,000	
Income tax	5,000	
Postages and Stationery	8,000	
Entertainment	15,000	280,400
Net profit		19,600

Additional information:

Salaries and Wages comprise of:

- Drawings by proprietor	N45,000
- Other Staff remuneration	N40,000
	N85,000

Legal expenses comprises of:

Purchase of new warehouse	2,000
Debt collection	3,000
General advice on business matter	2,400
	7,400

Provision for bad and doubtful debts contains N3,000 being a general provision

Repairs and maintenance comprises of:

1.Cost of making good the defect in a Generator at the time of purchase	15,000
2.Repainting of business premises	14,000
3.Maintenance of business vehicle	11,000
	40,000

Entertainment comprises of:

i. vacation abroad by proprietor's wife	N10,000
ii. Entertainment of Customer	N5,000
	15,000

You are required to compute the adjusted profit of Makurdi Business Centre.

Solution

Makurdi Business Centre
Trading, Profit and Loss Account for the
year ended 30th September, 2009

		₦	₦
Net profit per accounts			19,600
Add:	Salaries/wages-drawings	45,000	
	Legal fees – Purchase of new warehouse	2,000	
	Provision of Bad and doubtful debt - General provision	3,000	
	Repairs and maintenance -generator	15,000	
	Entertainment -proprietor's wife	10,000	
	Depreciation	60,000	
	Income tax	5,000	140,000
	Adjusted Profit		159,600

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

MODULE 2 TAXATION, RELIEFS AND ALLOWANCES

UNIT 7 PARTNERSHIP TAXATION

CONTENT

1.0 INTRODUCTION

Partnership refers to a relationship that subsists between two or more persons carrying on a business in common with the intention of making profit. Most partnership are upheld by a formal agreement know as 'Deed of partnership' which contains the following:

1. Contribution of capital by the partners
2. Interest (if any) to be paid on capital contributed
3. Amount which each partner can draw
4. Salaries to be paid to partners
5. Profit and loss sharing ratio

However, where there is no such formal agreement, the partners will share profit and losses equally. And they will not be entitled to interest on capital contributed or to any salaries. A partnership does not have a separate legal status from that of its members, as is the case with limited liability companies. That is, the liabilities of partners in a partnership are usually unlimited.

2.0 OBJECTIVES

After studying this unit, you will be able to

1. Explain partnership income
2. Describe income of a partner
3. State the provision in respect of the commencement and cassation of a partnership
4. Calculate adjusted profits and assessable income of a partner

3.0 MAIN CONTENT

3.1 Partnership Income

Ascertaining the income of the partnership for the assessment year is computed in the same manner as that of any other taxable individual engaged in a trade, business, profession or vocation. The only difference being that expenses such as salaries of partners, interest on capital and leave or recreational passages of partners are allowable business expenses in determining the partnership income. The income so derived is known as the' computed income' of the partnership. However, expenses which would ordinary have been regarded as private or domestic, who is incurred by any of the partners in their individual capacities are not allowable in ascertaining the partnership income.

The partnership income arrived at will be apportioned to each of the partners in accordance with the provision contained in the 'Deed of Partnership' and the assessment on the partner will be as though they were trading individually.

Self Assessment Exercise 7.1

What is partnership income?

3.2 Income of a Partner

The income of any partner shall be the additions of:

1. Remuneration, interest on capital, if any, paid to him and charged in the partnership accounts.

2. Private passage costs to or from Nigeria, if any, charged in the partnership accounts

3. Share of the partnership income as apportioned to him in accordance with the terms of sharing profits/losses as laid down in the partnership agreement.

The total arrived at shall be deemed to represent the partner's ascertained income or loss of that period from a trade, business, profession or vocation carried on by him during that period.

In the event of the 'computed income' from the partnership resulting in a loss, the partner's salary, interest on capital and private passage costs charged in the partnership accounts will be used to offset such loss to the extent that it is possible. Where it cannot be fully offset from the aforementioned items, the partner shall be deemed to have incurred a loss, from the trade or business as the case may be.

The income of a partner as ascertained above is deemed to be his assessable income from the partnership for the period. Each partner is assessed to tax on preceding year basis, and is entitled to make claims for appropriate reliefs and allowances available to the individual tax payer. A net loss sustained by a partner may be carried forward against his share of any future profits for a maximum period of four years. After such statutory limit it will be deemed to have lapsed.

Self Assessment Exercise 7.2

Explain the income of a partner.

3.3 Commencement and Cessation of a Partnership

When a new partner is admitted into an existing partnership, he will partake in the profits with effect from the date of his admission. It will also be assumed that he has commenced a new trade, business or profession as the case may be, from the date of his admission.

When a partner dies or ceases to be a member of a partnership, he will stop partaking in the partnership profits with effect from such date. He will be deemed to have ceased a trade, business or his departure.

However, the commencement and cessation provision shall not apply solely by reason of an individual joining or leaving a partnership, if the nature of the business of the partnership is the same as that carried on by him before or after he became or ceased to be a partner.

Self Assessment Exercise 7.3

State the provision for the commencement and cessation of a partnership.

3.4 Relevant Tax Authority

The relevant tax authority in relation to a partnership is the tax authority resident in the territory where the partnership has its principal office or place of business on the first day of the year of assessment. If any of the partners is resident for a year of assessment in the territory of some other tax authority (that is, if his place of residence differs from the partnership principal office or place of business), then the relevant tax authority will supply the necessary information to the other tax authority.

On demand by the relevant tax authority, to the principal office or place of business of a partnership, a certified copy of the partnership deed shall be submitted. Where there is no such written deed, particulars or any written or oral agreement under which the partnership is currently established is expected to be submitted or communicated.

Where a partnership fails to submit all the necessary particulars as requested by the relevant tax authority, the authority may use its discretion to decide any profits or loss. It may also proceed to assess the partners to tax accordingly.

An appeal by a partner against an assessment in so far as it relate to any partnership income or loss shall be to the body of Appeal Commissioners or court in the territory of the relevant tax authority.

Self Assessment Exercise 7.4

What is relevant tax authority in relation to partnership?

3.5 Adjusting Profits and Assessable Income of Partners

You should recall that the partnership income arrived at will be apportioned to each of the partners in accordance with the provisions contained in the partnership agreement and the assessment on the partners will be as though they were trading individually.

Example:

Festus, Felix and Frank have been in partnership for several years. The firm makes up its annual accounts to 31st December each year. During the ended 31st December, 2005 the firm books of accounts showed the following Net profit after charging items below ₦350, 000

	₦
Depreciation	42, 000
Annual annuity to a retired partner	36, 000
General provision for bad debt	10, 000
Installation of new air conditioner	12, 000
Loss on sale of fixed assets	8,000
Rent paid for business premises	25, 000
Interest on capital	30, 000
Partners salaries	385, 000

Additional information:

1. Festus, Felix and Frank share profits and losses in the ratio of 3:2:1 respectively.
2. Interest on capital
   Festus N10, 000; Felix ₦8, 000; Frank ₦9, 000
3. The partners received salaries as follows
   Frank ₦100, 000 per annum; Felix ₦135, 000 per annum; Frank ₦100, 000 per annum
4. The partnership business premises is owned privately by Frank
5. Capital allowances for the year to 31st December, 2005 were agreed at ₦11, 000

You are required to
   a. Complete the adjusted income of the firm for tax purpose for the year
   b. Complete the assessable income of each partner for 2006 year of assessment.

Solution:

a. Computation of Adjusted Profit

		₦	₦
Net Profit per accounts			350, 000
Add:	Depreciation	42, 000	
	General provision for bad debt	10, 000	
	Installation of air conditioner	12, 000	
	Loss on sale of fixed asset	8, 000	72, 500
			422, 500
Less:	Capital allowance		11, 000
	Adjusted profit		411, 500

b. Computation of Partners' Assessable Income

	Festus	Felix	Frank
	₦	₦	₦
Salaries	150, 000	135, 000	100, 000
Interest on capital	10, 000	8, 000	9, 000
Authority to retired partner	18, 000	12, 000	6, 000
Share of profit (as adjusted)	205, 750	137, 167	68, 583
Income from partnership	383, 750	292, 167	183, 583
Rent received	-	-	25, 000
Assessable income	383, 750	292, 167	208, 583

Self Assessment Exercise 7.5

Merry, Mary and Martha have been in partnership for several years as beauty pageant Consultants in Lagos. The firm makes up its annual accounts to 31st December each year. During the year ended 31st December, 2008 the firm's boos of accounts showed the following:
Net profit after charging items below ₦840, 000

		₦
Depreciation		20, 000
Annual annuity to a retired partner	42, 000	
General provision for bad debt		8, 000
Installation of air conditioner	10, 000	
Loss on sale of fixed assets	8, 000	
Rent paid for business premises		30, 000
Interest on capital		28, 000
Partner salaries		400, 000

Additional Information

1. Merry, Mary and Martha share profits and losses in the ratio of 2:2:2 respectively
2. Interest on capital: Merry ₦12, 000; Mary ₦10, 000; Martha ₦90, 000
3. The partners received salaries as follows
   Merry ₦200, 000, Mary ₦110, 000 Martha ₦90, 000 per annum

4. The partnership business premise is owned by Merry.
5. Capital allowances for the year to 31 December, 2008 were Agree at ₦14,000 you are required to
   a. Compute the adjusted profit
   b. Compute he assessable income of each partners for 2009 year of assessment.

4.0 CONCLUSIONS

In this unit we discussed partnership taxation. We Started by describing what partnership income is and proceeded to income of a partnership, commencement and cessation of a partnership, the relevant tax authority and finally, adjusted profit and assessable income of partners.

5.0 SUMMARY

You should recall that partnership refers to a relationship that subsists between two or more persons carrying on a business in common with the intention of making profit.

Ascertaining the in come of the partnership for the assessment year is computed in the same manner as that of any other taxable individual engaged in a trade, business, profession or vocation.

The income of any partner is admitted into an existing partnership, he will partake in the profit with effect from the date of his admission when a partner dies or ceases to be a member of a partnership, and he will stop partaking in the partnership profit with effect from such date.

The relevant tax authority in relation to partnership is the tax authority resident in territory where the partnership has its principal office or place of business on the first day of then year of assessment.

6.0 TUTOR MARKETED ASSIGNMENT

1. Describe the income of partners.

2. Discuss the relevant tax authority in relation to a partnership.

3. David, Edwin and Fred are inn partnership as architects for several years. The form makes up its annual account to 31st December each year. During the year ended 31st December, 2006, the firm's books of accounts showed the following:

Net profit after changing items below ₦650, 000

	₦
Depreciation	58, 000
Annual annuity to a retired partner	48, 000
General provision for bad debt	14, 000
Installation of air conditioner	20, 000
Loss on sale of generator	6, 000

Rent paid for business premises	40, 000
Partners salaries	600, 000

Additional Information

1. David, Edwin and Fred share profits and losses in the ratio of 3:1:2 respectively
2. Interest on capital: David ₦8, 000; Edwin ₦5, 000; Fred ₦7, 000
3. The partners received salaries as follows: David ₦200, 000 per annum, Edwin ₦200, 000 per annum and Fred ₦200, 000 per annum
4. The partnership business premises is owned privately by Edwin
5. Capital allowances for the year to 31st December, 2006 were agreed at ₦25, 000

You are required to

a. Compute the adjusted income of the firm for tax purposes for the year
b. Compute the assessable income of each partner for 2007 year of assessment.

Solution

A. Computation of Adjusted Profit

	₦	₦
Net profit per accounts		650, 000
Add: Depreciation	58, 000	
General provision for bad debt	14, 000	
Installation of air conditioner	20, 000	
Loss on sale of generator	6, 000	98, 000
		748, 000
Less: Capital allowances		25, 000
Adjusted profit		723, 000

b. Computation of partners' Assessable Income

	David	Edwin	Fred
	₦	₦	₦
Salaries	200, 000	200, 000	200, 000
Interest on capital	8, 000	5, 000	7, 000
Annuity to retired partner	24, 000	8, 000	16, 000
Share of profit	361, 5000	120, 500	241, 000
Income from partnership	593, 500	333, 500	464, 000
Rent receive	-	40, 000	-
Assessable income	593, 000	373, 500	464, 000

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 8 CAPITAL ALLOWANCES

CONTENT

1.0 INTRODUCTION

Capital allowances are a form of tax relief granted in respect of qualifying capital expenditure incurred on depreciable assets employed for the purpose of a trade or business. They are deductible from the business or trade is total profits, thus, reducing its tax liability.

Capital allowances are granted on qualifying capital expenditure incurred during a given basis period. Capital allowance is granted in lieu of depreciation. Depreciation of any asset is not an allowable deduction for the purpose of ascertaining the income of any individual.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. State the condition for granting capital allowances
2. Describe various types of qualifying expenditure
3. Describe initial allowance, investment allowance, annual allowance and nominal residue
4. Describe balancing allowances and charges
5. State the meaning of disposed of`
6. Explain basis period and its complications

3.0 MAIN CONTENT

3.1 Conditions for Granting Capital Allowances

For capital allowances to be granted to the individual tax payer in respect of qualifying capital expenditure, certain condition must be fulfilled, which are:

1. The asset for which the claim is being made must be used for the purpose of the trade, business, profession or vocation.
2. The asset must be owned by the individual claiming the allowance.
3. Qualifying expenditure must be incurred in respect of such asset.
4. The asset must be in use at the end of the basis period.
5. Where capital expenditure is incurred in respect of land and building, it is only the amount that relates to the building that would be claimable as capital allowances are not granted in respect of land.
6. The tax payer is normally expected to make a claim for capital allowances to the relevant tax authority.

Self Assessment Exercise 8.1

State the condition for granting Capital allowances.

3.2 Types of Qualifying Expenditure

Qualifying expenditure refers to the capital expenditure incurred in a given basis period which qualifies for capital allowances. Capital allowances are claimable at varying rates in respect of qualifying expenditure on:

1. Plant, Machinery and Fixtures
2. Building, Structures or works of a permanent nature
3. Mines, Oil wells or other sources of mineral deposits of a wasting nature
4. Plantations
5. Research and Development
6. Agricultural plant
7. Public transportation motor vehicles
8. Public transportation (inter-city) New Mass Transit coach

Plant, Machinery and Fixture: This relates to capital expenditure incurred on plant, Machinery and fixture in a given basis period. Plant, machinery and fixture may include the following:

1. Plant used for storage or processing such as tanks, containers and refrigerator
2. Machinery used in the manufacturing process such as lathes, pumps, drills, shuttles, rollers, sewing machine etc.
3. Fixture and fittings of a permanent and durable nature including furniture.

Building, structure or works of a permanent nature: This relates to capital expenditure incurred on the construction of buildings, structures or works of permanent nature other than expenditure which is included in qualifying plant expenditure or qualifying mining expenditure. Buildings, structures or works of a permanent nature are for purposes of granting capital allowances classified into industrial and non-industrial buildings.

An industrial building is defined as any building or structure in regular use.

i. As a mill, factory, mechanical workshop or other similar building, or as a structure used in connection with any such building.
ii. As a dock, port, wharf, pier, jetty or other similar building or structure.
iii. For the operation of a railway for public use or of a water or electricity undertaking for the supply of water or electricity for public consumption and
iv. For the running of a plantation or for the working of a mine or other source of mineral deposits of a wasting nature.

A non-industrial building, structure or work of a permanent nature that falls outside the definition of an industrial building as stated above is a non-industrial building e.g. an administrative offices or blocks of a manufacturing firm or company.

Mines, Oil well or other Sources of Mineral Deposits of a Wasting Nature: This relates to capital expenditure for, the working of a mine, oil well or the source of mineral deposits of a wasting nature (other than qualifying plant expenditure), on:

i. The acquisition of, rights in or over, the deposits existence and extent of deposits
ii. The searching for, or on discovering and testing deposits or winning access there to or
iii. The construction of works or building that are likely to be little or no value when the source is no longer worked or where the source is worked under a concession that is likely to become valueless when the concession to work the mine comes to an end.

Qualifying Plantation Expenditure: This relates to capital expenditure incurred in connection with a plantation:

i. On the clearing of land for planting and
ii. On planting (other than replanting)

Qualifying Research and Development Expenditure: This means capital expenditure incurred:

i. On equipment and facilities, patents, licenses, secret formula or process or
ii. For information concerning industrial, commercial or scientific process, technical feasibility or products or process and purchase or
iii. On searching for and discovering and testing products or process for future marked or use and such other similar costs which have not brought into existence on asset.

Agricultural Plant: Qualifying agricultural plant expenditure means capital expenditure incurred on plant in use in agricultural trades and business. Agricultural trade and business is defined as any trade or business connected with:

a. The establishment or management of plantations for the production of rubber, oil palm, coffee, tea and similar crops

b. The cultivation or production of cereal crops, tuber, fruits of all kinds, vegetables, pineapples, banana and plantains.

c. Animal husbandry, that is to say, poultry, piggery, cattle rearing and the like and fish farming.

Public Transportation Motor Vehicle: Qualifying public transportation motor vehicle expenditure means capital expenditure incurred on a fleet of buses of not less than three, used for public transportation.

Public Transportation (Inter-city) New Mass Transit Coach: Public Transportation (Inter-city) New Mass Transit Coach expenditure relates to capital expenditure incurred on new mass transit coaches, containing 25 seats and above which are operated by recognized private establishments.

Self Assessment Exercise 8.2

State and describe five qualifying expenditure you know.

3.3 Allowances and Nominal Residue

1. Initial Allowance: This is granted in respect of qualifying expenditure incurred on each asset for the year of assessment, in the basis period in which it was first used. It is granted only once in the life of an asset and is not affected by the length of the basis period in which such asset was first put into use.

2. Investment Allowance: Investment allowance of 10% on capital expenditure incurred with effect from 1st April, 1918, in addition to initial allowance, are given to companies engaged in agricultural production unlike initial allowance, it is not deductible from qualifying expenditure in arriving at the residue of the capital assets. It is also given once like initial allowance and would not be affected by the length of the basis period during which the assets were first put in use. This is to boost agricultural production by the Federal Government.

3. Annual Allowance: This is granted in respect of qualifying expenditure incurred on each asset for the year of assessment, in the basis period in which it was used. It is granted annually over the estimated useful life of the asset. The annual allowance is uniform over the estimated useful life of the asset. Thus, the cost of the asset less any initial allowance granted is written off in equal installments each year. Where the basis period is less than twelve months, the annual allowance for such year is reduced proportionately. In other words, the full amount of the allowance for that year of assessment will not be granted, under the circumstances.

Nominal Residue: A nominal sum of ₦10 per item is retained in the books for tax purposes in the last year an annual allowance will be claimed until the asset is disposed of. This is to ensure that the respective fixed asset items are not forgotten immediately after full allowances have been granted for them and to ensure that balancing adjustments are made on disposal of the items.

Capital Allowances Rates

Qualifying Expenditure In respect of:	1996 to date Initial Allowance %	Annual Allowance %	1993 to 1995 Initial Allowance %	Annual Allowance %
Non industrial buildings	15	10	5	10
Industrial building	15	10	15	10
Mining	95	Nil	20	10
Plant (excluding furniture & fittings)	50	25	20	10
Plant (Manufacturing, Construction)	50	25	25	10
Agricultural Production	95	Nil	25	10
Furniture and Fittings	25	20	15	10
Motor Vehicle	50	25	25	20
Motor Vehicle (Public Transport minimum of 3 buses)	95	Nil	30	20
Plantation equipment	95	Nil	20	33½
Housing estate	50	25	20	10
Ranching and Plantation	30	50	30	15
Researching and Development	95	Nil	25	12½

Self Assessment Exercise 8.3

Describe the following:

1. Initial allowance
2. Investment allowance
3. Annual allowance
4. Nominal residue

3.4 Balancing Allowances and Charges

Balancing adjustment would be made when a fixed asset that has previously been granted capital allowances is disposed of. Where on disposal of the fixed asset, the realizable value the residue of expenditure, a balancing charge exceeds will arise. You should note that a balancing charge should not exceed the aggregate of capital allowances already granted in respect of such asset.

Where on disposal of an asset the residue of expenditure exceeds the realizable value, a balancing allowance will arise.

The balancing allowances and charges ensure that only the cost of the asset to the claimant, less any amount realized on disposal is allowed over the period as a relief from taxation. You should note that capital allowances are not granted for an asset in the year of assessment in which it is disposed of.

Example

Let us show an illustration of the following concept explained above in respect of when balancing allowance or charges arise. Assuming an original cost of ₦55, 000 and a residue value of ₦20, 000 of the asset, Let us assume proceeds of disposal in a case (a) ₦28, 000 (b) ₦15, 000 (c) ₦60, 000.

a.

Sales proceeds	₦28, 000
Residue	₦20, 000
Balancing charge	₦8, 000

b.

Sales proceeds	₦15, 000
Residue	₦20, 000
Balancing allowance	₦5, 000

c.

Sales proceeds	₦60, 000
Residue	₦20, 000
Balancing allowance	₦40, 000

Balancing charges will need be restricted to capital allowances granted which is ₦35, 000 (₦55, 000 – ₦20, 000) and not the ₦40, 000 difference above.

Self Assessment Exercise 8.4

Explain the term balancing allowances and charges.

3.5 Meaning of "disposed of"

A building, structure or work of a permanent nature is disposed of if any of the following events occur:

1. The relevant interest therein is sold or
2. That interest, being an interest depending on the duration of a concession comes to an end on the coming to an end of that concession or
3. That interest, being a leasehold interest, comes to an end otherwise than on the individual entitled there to acquiring the interest which is reversionary thereon or
4. The building, structure or work of a permanent nature are demolished, or cease to be used for the purpose of the trade or business.

In relation to plant, machinery or fixtures when:

1. Sold
2. Discarded or scrapped or

3. They are no longer used for the trade or business.

In relation to mining assets when:

1. They are sold or
2. They are no longer used for the trade either on cessation of trade or on receipt of insurance or compensation monies for them.

Self Assessment Exercise 8.5

What is the meaning of “disposed of”?

3.6 Basis Period and its Complications

The relevant basis period for the purpose of making capital allowance claims is the accounting period proceeding the year of assessment in which the allowances are being claimed.

Basis periods sometimes tend to overlap or coincide, thus resulting in assessments for more than one year being based on the same basis period. Gaps sometimes occur in between basis periods. Basis period complications

1. Overlapping periods

Where two basis period overlap, the period common to both shall be deemed to belong to the earlier period.

Example
A sole proprietor commenced business on 1st June, 1999 making up accounts to 31st May each year.

You are required to show the common periods within the basis period for the first three years.

Solution				**common period**	
1999	01/06/99	to	31/12/99	01/06/99 to 31/12/99 Deemed to belong to 1999	01/06/99 - 31/12/00 Deemed to belong 1999
2000	01/06/99	to	31/05/00	01/06/99 to 31/05/00 deemed to belong to 2000	
2001	01/06/99	to	31/05/00		

2. Coinciding Periods

Where two basis periods coincide, they shall be treated as an overlapping case, and the basis period for the earlier year of assessment shall be treated as ending before the end of the basis period for the later year of assessment.

Example

Omo Enterprises commenced business on 1st January, 2004 and decided to make up its accounts to 31st December each year.

You are required to show the common periods that occur within the basis period for the first three years of assessment.

Solution				**common period**
2004	01/01/04	to	31/12/04	01/01/04 to 31/12/04
2005	01/01/94	to	31/12/04	deemed to belong to 2004
2006	01/01/95	to	31/12/05	

3. Interval or Gap (Rule 1)

Where there is an interval or gap between the end of the basis period of one year of assessment and basis period of the next year of assessment, then unless the second year of assessment is the year in which the business permanently ceases to carry on its activities, the interval shall be deemed to be part of the second basis period.

Example

Freedom Enterprises, an established motor spare parts outfit which previously made up its accounts to 31st March each year decide to change its accounting date 30th June effective from 2003.

You are required to show the basis period for the next 3 years of assessment, starting from 2003 using both the old and new accounting dates.

Solution

	Old Accounting Dates		
2003	01/04/01	to	31/03/02
2004	01/04/02	to	31/03/03
2005	01/04/03	to	31/03/04

	New Accounting Dates		
2003	01/07/01	to	30/06/02
2004	01/07/02	to	30/06/03
2005	01/07/03	to	30/06/04

Where the relevant tax authority chooses the new accounting date, there will be a gap between the last day of the old accounting date and the first day of the new accounting date.

That is,2002 01/04/00 to 31/03/01 01/04/01 to 30/06/01

Deemed to belong to

2003 01/07/01 to 30/06/02 2003

If on the other hand, the relevant tax authority chooses the old accounting date, there will also be a gap between the last day of the old accounting date and the first day of the new accounting date.

That is,	2005	01/04/03 to 31/03/04	01/04/04 to 30/06/04
	2006	01/07/04 to 30/06/0	Deemed to belong to 2006

Rule 2
Where there is an interval or gap between the end of the basis period for the year of assessment preceding that in which the business permanently ceases to be carried on, that is, the penultimate year, and the basis period for the year in which it so ceases, the interval shall be deemed to form part of the first basis period.

Thus, this second rule applies when there is a gap between the end of the basis period of one year and that of the next year, which happens to be the year in which the business permanently ceases.

Example
Efosa trading Enterprises which has been in existence for many years, making up its accounts to 312st December each year, ceased business permanently on 31 December, 2006.

You are required to show the basis period for the last three years of assessment up to the point of cessation.

Solution

2004	01/01/03 to 31/12/03	
2005	Preceding Year 01/01/04 to 31/12/04	
	Actual Year 01/01/05 to 31/12/05	01/01/05 to 31/12/05
		Deemed to belong
2006	01/01/06 to 31/12/06	to 2005

There is a gap between the preceding year of 2005 and the 2006 year of assessment. That is, the gap exists between the basis period 01/01/05 to 31/12/05. The gap, in keeping with rule 2 is deemed to be part of the first basis period that is, it belong to 2005.

You should note that this gap only occurs between the penultimate year and the ultimate year. When the preceding year of the penultimate year rather than the actual year of the penultimate year is being considered.

Self Assessment Exercise 8.6

Describe the three basis period complication.

4.0 CONCLUSION

In this unit, we discussed capital allowances. We started by listing the condition for granting capital allowances, and proceeded to types of qualifying expenditure, allowances and nominal residue, balancing allowances and charges, meaning of " disposed of" and finally, basis period and its complications.

5.0 SUMMARY

You should recall that capital allowances are a form of tax relief granted in respect of qualifying capital expenditure incurred on depreciable assets employed for the purposes of a trade or business.

Qualifying expenditure refers to the capital expenditure incurred in a given basis period which qualifies for capital allowances.

When an asset on which capital allowances have been granted is disposed of, balancing adjustment will need to be made.

The relevant basis period for the purpose of making capital allowance claims is the accounting period preceding the year of assessment in which the allowances are being claimed.

6.0 TUTOR MARKED ASSIGNMENT

1. State the conditions for granting capital allowances

2. State and describe five qualifying expenditure

3. Describe the following term:
   a. Initial allowance
   b. Investment allowance
   c. Annual allowance
   d. Nominal allowance

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 9 LOSS RELIEF

CONTENT

1.0 INTRODUCTION

Trade or businesses are carried out with the aim of making profits which are assessed tax. Sometimes, when generated revenues are matched against the expenses incurred in trade, business or profession, the expenses tend to exceed the generated revenue, thereby resulting in a loss. In such a case, there would not be any taxable profit and the tax assessment for the trade or business for the year of assessment would be nil.

Due to this circumstances, the trade or business may be granted a loss relief to enable it set-off such loss against profits generated from other trading or business activities(if any) carried on by the same individual or from profits that may be generated in future years from the same trade or business that has presently incurred a loss. Where this is to be set-off from future profits it has to be done within a period of four years or the loss will be elapse. Capital allowances are considered first before the capital allowances.

Loss relief may be spread over a number of years. However, the aggregate amount of such relief over such number of years should not exceed the actual amount of the loss incurred.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Explain current year loss relief
2. Explain carry forward loss relief
3. Explain terminal loss
4. Explain the treatment of loss used in aggregation

3.0 MAIN CONTENT

3.1 Current year loss relief

This type of relief is granted in respect of losses incurred by an individual during a year of assessment from any trade or business.

A written claim must be made to the relevant tax authority within twelve months following the year of assessment in which the loss was incurred for current year loss relief to be granted. The loss incurred during the year of assessment is deducted from the total assessable profits derived from different sources during that year as well as from any balancing charges to obtain the current year loss relief.

Any loss that remains unabsorbed in the year in which it was incurred becomes available for carry forward loss relief in subsequent years

Example 1

Mr Mutaya has been in business for several and produces the following results for the year ended 31st August, 2007

	N	N
Sales		300,000
Less cost of sales:		
Opening stocks	80,000	
Purchases	2,520,000	
	2,600,000	
Less closing sales	70,000	2,530,000
Gross profit		470,000
Less expenses		
Wages and salaries	580,000	
Rent and rates	240,000	
Travelling	120,000	
Depreciation	180,000	
Other allowable expenses	120,000	1,240,000
Loss for the year		770,000

His trading profits (adjusted for tax) for the past three years to 31st August, 2006 are N600,000, N800,000 and N500,000 respectively. Ignore capital allowances.

Solution

The accounting loss for the year ended 31st August, 2007 will need to be adjusted for tax purposes. That is, deduct all disallowable expenses and all non- taxable income.

	₦
Net loss per accounts	770,000
Less: depreciation	180,000
Adjusted loss	590,000

The relevant assessments for the four years are:

Financial year ended	years of assessment	Adjusted profit/loss
		~~N~~
31/08/07	2008	(590,000)
31/08/06	2007	500,000
31/08/05	2006	800,000
31/08/04	2005	600,000

Instead of paying the tax due on #500,000 for the 2007 year of assessment, which is in the financial year in which the loss was incurred, Mr Mutaya can apply to have the trading loss incurred in the year ended 31st August,2007 deducted from the profit for the year ended 31st august, 2006. The assessments will then appear as follows:

Year of assessment			N
2005	as before		600,000
2006	as before		800,000
2007	as before		500,000
	Deduct current year loss		(500,000)
	2007 revised assessment		–
2008	loss as before		(590,000)
	Loss relieved in 2007 as above		500,000
	Loss carried forward		(90,000)
	2008 assessment	Nil	

You should note that the balance of the loss (# 90,000) can only be carried forward for relief against future profits of the same trade. Also, that for current year loss relief, the loss can be set against the tax payers income from the other sources during the year in which the loss was incurred.

Self Assessment Exercise 9.1

1. Describe a current year loss relief

2. Mr Felix has been in business from several years and produces the following results for the financial year ended 31st May, 2007

	N	N
Sales		2,500,000
Less cost of sales:		
Opening stocks	50,000	
Purchase	2,000,00	
	2,050,00	
Less closing stock	65,000	1,985,000
Gross profit		515,000
Expenses:		
Wages and salaries	400,000	

Rent and rates	250,000	
Travelling	150,000	
Depreciation	250,000	
Other allowable expenses	120,000	1,170,000
Loss		655,000

His trading profits (adjusted for tax) for the past three years to 31st may,2006 are ₦300,000,₦500,000 and ₦350,000 respectively. You are required to show the assessable profits for the relevant years of assessment. Ignore capital allowances.

3.2 Carry Forward Loss Relief

Carry forward loss relief is only granted against the income from the same trade in which the loss was incurred unlike current year loss relief and for which no current year has been granted. This type of relief is granted in respect of losses incurred by an individual in the preceding year of assessment from any trade, business, profession or vocation which could not be set- off in the year that they were incurred due to the unavailability of assessable profits.

The following should be noted as far as carry forward loss relief is concerned:

1. There is no need for a written claim as it is the case with the current year relief.

2. The loss is brought forward from the preceding assessment year.

3. The amount to be relieved must not have been relieved under the current year loss relief provision. That means there cannot be double relief. In no circumstances shall the aggregate deduction from assessable income in respect of any loss exceed the amount of such loss.

4. Relief is available only against the profit of the same trade in which the loss was incurred.

5. Losses incurred in properly letting can only be relieved under the carry forward provisions. In no circumstance can relief be given against other income of the year of assessment in which then loss was incurred.

6. The relief is granted by deducting the unused loss brought forward as far as possible from the assessable income of the first year of assessment after that in which the loss was incurred. Relief which cannot be so made if the amount of the loss is greater than the assessable profit of that year, is to be made in a similar manner in the next year of assessment, then the next following year of assessment and so on until the total amount of the loss is fully relieved. However, losses can presently be carried forward only for a maximum period of the years.

Example

Mr Osaro commenced a retail business on 18th June, 2006, making up accounts to 31st December each year. His adjusted profit(loss) figures for tax purposes were as follows;

	N
Period to 31st December, 2006	(45,000)

Year ended 31st December 2007 55,000

You are required to compute his assessable profits for the relevant year of assessment.

Solution

Mr Osaro

Computation of Assessable Profits

			Assessment
2006	01/06 /06 to 31/12/06		
	Loss for 7 months	₦45,000	
	Assessment		Nil
2007	01/06/06 to31/05/07		
	Unrelieved loss b/f	₦45,000	
	Profit for 5 months		
	(i.e 01/01/07 to31/05/07)		
	$\frac{5}{12}$* 55,000	₦22,917	
	Unrelieved loss c/f	₦22,083	
	Assessment		Nil
2008	01/01/07 to 31/12/07		
	Unrelieved loss b/f	(₦22,083)	
	Profits for 12 months	55,000	
	Assessment		32,917

Example

Mr Aramude, a general merchant, commenced business on 1st July 2004. He made up his accounts to 31st December each year. His adjusted profits (loss0 were as follows:

Period to 31/12/04	(95,000)
YEAR ENDED 31/12/05	45,000
Year ended 31/12/06	20,000
Year ended 31/12/07	22,000

You are required to compute the assessments for all the relevant years.

Solution

Mr Aramude

Computation of assessable profits

		Assessment
2004	01/07/04 to 31/12/04	(N95,000)
	Assessment	Nil
2005	01/07/04 to 30/06/05	
	Unrelieved loss b/f (6months)	(N95,000)
	Profit (6months)	
	(i.e 01/01/95 to 30/06/95)	

	$\frac{6}{12}$*45,000	N22,500	
	Unrelieved loss c/f	N72,500	
	Assessment		Nil
2006	01/01/05 to 31/12/05		
	Unrelieved loss b/f	(N72,500)	
	Profit for 12 months to 31/12/95	N45,000	
	Unrelieved loss c/f	(N27,500)	
	Assessment		Nil
2007	01/01/06 to 31/12/06		
	Unrelieved loss b/f	(N27,500)	
	Profit for 12 months to 31/12/06	₦20,000	
	Unabsorbed loss (lapses)	7,500	
	Assessment		Nil
2008	01/01/07 to 31/12/07		
	Profit for 12months to 31/12/07	₦22,000	

Self Assessment Exercise 9.2

1. Explain a carry forward loss relief

2. Mr Amadu commenced a retail business on 1st April,2003, making up accounts to 31st December each year. His adjusted profit / (loss) figures for tax purposes were as follows.
   Period to 31st December,2003 (N55,000)
   Year ended 31st December,2004 N65,000

You are required to compute his assessable profits for the relevant years of assessment.

3.3 Terminal loss

Losses incurred in the last year of existence of a trade or business is referred to as terminal losses. This is because there is no provision in the decree for the granting of loss relief in the year of assessment when a trade permanently ceases. There will therefore be no relief for any loss incurred in the last year of trade. Since the computation of the assessable income for the year of cessation will be based on actual, there will be no assessable income in that year as the assessment for the penultimate year on actual, it is not likely that this option will be exercised if it will result in lower assessable income. The taxpayer's claim of current year's loss relief might therefore be frustrated by the tax authority option.

Self Assessment Exercise 9.3

Explain the term 'terminal losses.

3.4 Losses Used in Aggregation

A current year loss relief or a carry forward loss relief can only be granted to the extent that the loss, for which it is being sought, has not already been set-off against profits in computing the total assessable profits for the period. In other words, any part of a loss already used in aggregation should not be relieved against other profits. This implies that loss relief granted for any loss incurred should not be greater ion total than the actual amount of such loss.

Losses incurred for example, in the first years of commencement of trade might cause some difficulties. This is so because they might need to be aggregated with profits to determine the income of a period. The principle that reliefs to be given for any loss shall not in total be greater than the actual amount of the loss incurred must be observed.

Any part of the loss already used in aggregation cannot be relieved against any other profits or income.

Example

Mr Tunde commences trade on 18th May 2005 and makes up his accounts to 28th February every year. His results are:

01/05/05 to 28/02/06 - 10 months less N500,000
01/03/06 to 28/02/07 - 12 months profit N700,000

The assessment is:

2005 - Actual 01/05/05 to 31/12/0
Proportion of loss $= \frac{8}{10} \times$ ₦500,000 (N400,00)
Assessment Nil

2006 –first 12 months of operation

1st to 10 months – trading loss	(N500,000)
Next-2 months-$\frac{2}{12}$ #700,000 profit	116,667
Loss	(383,333)
Assessment	Nil

2007 Preceding year basis
(no 12 months accounts ended in the preceding year, hence, we repeat 2006 assessment)

i.e. 01/05/05 to 30/04/06

1st to 10 months	(N500,000)
Next two months- $\frac{2}{12}$ x 700,000	N116,667
	N383,333
Assessment	Nil

You should note that the amount of loss to be carried forward to future assessment years should be that of the loss which has not been relieved by way of being aggregated with any profit.

Thus in the example above:

₦116,667 of the loss was aggregated with profit during the 2006 assessment year.

Another ₦166,667 was also aggregated for the 2007 assessment year.

A total of ₦233,334 of the loss which has been aggregated will therefore be treated as relieved and only the balance of ₦266,666 (#500,000--₦233,334) is available to be carried forward.

Self Assessment Exercise 9.4

How is losses used in aggregate treated?

4.0 CONCLUSION

In this unit, we discussed loss relief. We started by explaining a current year loss relief, and proceeded to carry forward loss relief, terminal loss and finally losses used in aggregation.

5.0 SUMMARY

You should recall that loss relief is granted to business or trade to enable it set-off losses against profits generated from other trading or business activities (if any) carried on by the same individual or from profits that may be generated in future years from the same trade or business that has presently incurred a loss. However, where the loss is to be set-off from future profits, it has to done within a period of four years.

The current year loss relief is the type of relief granted in respect of losses incurred by an individual during a year of assessment from any trade of business.

The carry forward loss relief is granted in respect of losses incurred by an individual in the preceding year of assessment from any trade or business, which set-off in the year that they were incurred due to the unavailability or sufficiency of assessable profits.

The losses incurred in the last year of existence of a trade or business is referred to as terminal losses.

Any part of a loss already used in aggregation should not be relieved against other profits.

6.0 TUTOR MARKED ASSIGNMENT

1. Explain a carry forward loss relief.

2. Mr. Gregory, a general merchant, commenced trade on 1st June 2003. He made up his accounts to 31st March each year. His adjusted profits (loss) were as follows:

	N
Period to 31/03/04	(87,000)
Year ended 31/03/05	43,000
Year ended 31/03/06	25,000
Year ended 31/03/07	18,000

You are required to compute the assessment for all the relevant years

Solution

Mr Gregory

Computation of Assessable profits

			Assessment
2003	01/06/03 to 31/12/03		
	$\frac{7}{9}$ x 87,000	(N67,667)	
	Assessment		Nil
2004	01/06/03 to31/05/04		
	Unrelieved loss b/f	(N87,000)	
	Profit for 2 months (i.e 01/04/04 to 31/05/04)		
	$\frac{2}{12}$ x 43,000 =	7,167	
	Unrelieved loss c/f	(N79,833)	
	Assessment		Nil
2005	01/06/03 to 31/05/04		
	Unrelieved loss b/f	79,833	
	Profit for 2months		
	2/12* 43,000	7,167	
	Unrelieved loss c/f	72,666	
	Assessment		Nil
2006	01/04/04 to 31/03/05		
	Unrelieved loss b/f	(N72,666)	
	Profit for 12 months	N43,000	
	Unabsorbed loss (lapses)	29,666	
	Assessment		Nil
2007	01/04/05 to 31/03/06		
	Profit for 12 months	N25,000	
2008	01/04/05 to 31/03/07		
	Profits for 12 months	N18,000	

3. How is losses used in aggregation treated?

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 10 CAPITAL GAINS TAX

CONTENT

1.0 INTRODUCTION

Assuming a generator distributor purchased a number of generators with the prime intention or resale. Such generators would constitute his stock-in-trade. Income generated from their sale would constitute income of a revenue nature as against income of a capital nature from which capital gains may arise if on the other hand, the generator distributor bought a number of air-conditioners for use in his enterprise, they would not form part of the enterprise stock-in-trade. Any gains realized on sale of such air-conditioners would constitute capital gains rather than income for tax purposes.

Capital gains are those gains that arise form an increase in the market value of assets that were not purchased with the prime intention of resale. Such assets are usually bought for use and are therefore not regularly offered for sale. On sale or disposal of such assets, an appreciation in its value becomes a realized capital gain.

The administration of the capital gains tax Acts amended is vested in the Federal Board of Inland Revenue (FBIR). Capital gains tax in respect of corporate bodies and residents of Abuja is collected by the Federal Government, while the state Government collect form individuals and other bodies that lie outside the Federal Government tax jurisdiction. The Capital Gains Tax Act of 1967 and the various amendments to the Act have been consolidated and codified under the Capital Gains Tax Act Cap. 42 LFN 1990.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Explain chargeable assets
2. Explain gains chargeable

3. Describe the disposal of assets
4. Describe consideration of asset
5. Explain and calculate cost of asset on partial disposal and determine capital gains tax
6. State some organizations, bodies and circumstances exempted from capital gains tax.

3.0 MAIN CONTENT

3.1 Chargeable Assets

Capital gains tax is a tax imposed on capital gains arising from the disposal of chargeable assets. All forms of property, except where otherwise stated in the Act are chargeable assets. These include:

1. options (i.e. option to purchase shares etc.) debts and incorporeal property generally (i.e. debentures, lease holds etc.)

2. any currency other than Nigerian currency

3. any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired (i.e. artworks created by an artist).

4. stocks and shares of every description included in chargeable assets are assets situated outside Nigeria. Capital gains tax is chargeable on amounts received in a brought accruing from assets disposed of outside Nigeria. Such amounts are treated as chargeable gains when they are received or brought into Nigeria. Disposal of assets situated outside Nigeria occurs under the following circumstances:

    1. Where such disposal is by an individual

        a. Who is in Nigeria for some temporary purpose only and not with any view or intent to establish his residence in Nigeria
        b. If the period or sum of periods for which he is present in Nigeria in that year exceeds 182 days.

    2. Where such disposal is by the trustee of a trust or settlement that is administered outside Nigeria during the whole of the year of assessment

    3. Where such disposal is by a company whose activities are managed and controlled outside Nigerian during the whole of the year of assessment.

Self Assessment Exercise 10.1

What are chargeable assets?

3.2 Gains Chargeable

Gains chargeable to tax shall be the amount of the consideration accruing on the disposal on an assets, after deducting any sums exclude from such consideration and any allowable expenditure. The following expenses are allowable in computing the capital gains accruing to a person on the disposal of an asset:

1. Any expenditure incurred wholly, exclusively and necessarily in acquiring the asset

2. Any expenditure incurred wholly, exclusively and necessarily in establishing, preserving or defending the title to or right over the asset

3. Incidental costs of making the disposal such incidental costs arising on the disposal of an asset include fees, commission or remuneration paid for the professional services of any survey or valuer, auctioneer, accountant, agent or legal adviser and costs of transfer or conveyance (including stamp duties).

Capital gains tax was imposed at the rate of 20% on capital gains arising from the disposal of chargeable assets, up to 31st December, 1995. With effect from 1st January, 1996, the tax rate was reduced to 10%.

In computing chargeable gains, losses incurred on the disposal of assets are not deductible from the gains arising on the disposal of such asset. Thus, a capital loss may not be set against a chargeable gain made in the same year or a later year.

Self Assessment Exercise 10.2

Explain gains chargeable.

3.3 Disposal of Assets

An asset is disposed of when there is either a change of ownership or a transfer of the rights or interest therein. The gain on disposal of an asset must have accrued on or after 1st April, 1967 to attract capital gains tax, irrespective of the date of acquisition of the asset.

Except as specifically exempted by the Act, there is a disposal of assets by a person where any capital sum is derived from a sale, lease, transfer, an assignment, a compulsory acquisition or any other disposition of assts.

You should note that the payee might not actually have acquired any asset in return for the capital sum paid. The Act also listed particular instances in this regard.

1. Where a capital sum is derived by way of compensation of any loss of office or employment

2. Where a capital sum is received under a policy of insurance and the risk of any kind of damage or injury to, or the loss or depreciation of assets.

3. Where a capital sum is received in return for forfeiture or surrender of rights, or for refraining from exercising rights.

4. Where a capital sum is received as consideration for use or exploitation of any asset

5. Without prejudice to paragraph (1) above, where a capital sum is received in connection with a trade, business profession or vocation.

Self Assessment Exercise 10.3

What is disposal of assets?

3.4 Consideration of Asset

Consideration of asset acquired/disposed shall be deemed to be equal to the market value of the asset where any person acquires the asset.

a. Otherwise than by way of a bargain made at arm's length

b. Wholly or partly for a consideration that can not be valued or in connection with his own or another's loss of office in consideration for or recognition of services or past services.

c. As trustee for creditors of the person making the disposal

Where a person disposes by way of a gift for an asset acquired by him by way of a gift or otherwise (not being an acquisition on a devolution on death), the person acquiring the asset on that disposal shall, for all purposes of this Act, so far as relates to the interest taken b y him, be deemed to have acquired the asset:

a. In a case where the amount of the consideration for which the asset was lost disposed of by way a bargain made at arm's length is ascertainable, for a consideration equal to that amount.

b. In any other case, for a consideration equal to the market value of the asset on the date of that disposal; and in this subsection, "gift" does not include a donation mortis causa.

Donations mortis causa is a gift comprising of moveable property given by a donor on his death bed. That is, by a person anticipating death. However, if such death does not eventually occur, the gift becomes void.

Self Assessment Exercise 10.4

What is consideration of asset?

3.5 Cost of Asset Disposed on Partial Disposal

Where there is a part disposal, the cost of that part of asset disposed and that of the indisposed part shall be apportioned. The cost to be apportioned to the part disposed shall be in the proportion that the consideration for the disposal bears to the total value of the whole asset on the date of disposal. The value of the whole asset on that date is the consideration received in respect of the part disposed plus the market value of the part of the asset which remains indisposed.

The proportion or fraction of the original cost of acquisition plus any expenditure incurred in enhancing the value of the asset (which is an allowable deduction in computing the gains arising from the part disposed of) is determined using the following formula:

$$\frac{A}{A + B} \quad x \quad C$$

Where:

A: represents the amount or value of the consideration given for the property disposed of

B: represents the market value of the property undisposed of; and

C: represents the original cost of acquisition and the expenditure incurred in enhancing the value of the asset.

The remaining fraction of the original cost of acquisition and the expenditure incurred in enhancing the value of the asset, attributable to the disposed part which is an allowable deduction, the incidental costs of making such part disposal are also allowed deductions in computing the amount of capital gains arising from such part disposal.

Example

Mr. Tunde sold a piece of land which realized net proceeds of N15,000 on 1st July 2006. The land had been acquired as part of a larger piece of land in 1992 at a total cost of N5,000. The market value of the remaining piece of land held by Mr. Tunde on 1st July, 2006 was N20,000. You are required to compute the capital gains tax payable by Mr. Tunde in 2006 in respect of this transaction.

Solution:

The fraction of the cost attribute to the part disposed of

$$= \frac{A}{A + B} \quad x \quad C \quad = \quad \frac{15{,}000}{15{,}000 + 20{,}000} \quad x \quad 5{,}000$$

$$= \quad \frac{15{,}000}{35{,}000} \quad x \quad 5{,}000$$

Where A = sales proceeds of land

B = market value of remaining land

C = Cost of acquisition

Computation of Capital gains tax

	N
Sales	15,000
Loss proportion of cost attributable to	
Part disposed of	2,143
Chargeable gains	12,857

: Capital gains tax at 10% = 1,286

Example

Intelligence Computer Centre acquired some property in Benin in 1992 at a cost of N600,000. A sum of N100,000 was also spent by the enterprise in enhancing the value of the asset.

On the 1st of May, 2003, the enterprise disposed of substantial part of the property for N750,000. Expenses incurred on the disposal was N46,000. The property retained has a market value of N180,000.

You are required to determine the capital gains tax payable by the enterprise on the property disposed of.

Solution.

The fraction of the cost attributable to the part disposed of = $\frac{A}{A + B} \times C$

$= \frac{750,000}{750,000 + 180,000} \times (600,000 + 100,00)$

$= \frac{750,000}{930,000} \times 700,000$

$= 564,516$

Computing of capital gains tax

Sales proceeds	750,000
Less: disposal expenses	46,000
Net proceeds	704,000
Less: cost of part disposed	564,516
Chargeable gains	139,484

: capital gains tax at 10% = N13,948

Self Assessment Exercise 10.5

Sango business enterprise acquired some property in Lagos in 1985 at a cost of N400,000. A sum of N120,000 was also spent by the enterprise in enhancing the value of the property.

On the 1st of February 1999, the enterprise disposed of a substantial part of the property for N450,000. Enterprise incurred on the disposal was N20,000. The property retained has a market value of N120,000.

You are required to determine the capital gains tax payable by the enterprise on the property disposed of.

3.6 Exemptions and Reliefs

It is important you know that there are certain organizations, bodies and circumstances that would be exempted from capital gains tax when capital gains are made. Some of them are discussed below:

1. Exemption for charities

Gains accruing to the following bodies are exempted from capital gains tax.

(i) Ecclesiastical, charitable or educational institutions of a public character.
(ii) Any statutory or registered friendly society
(iii) Any co-operative society, registered under the co-operative societies Act

(iv) Any trade union registered under the Trade Union Act, provided
  a. The gain or profit is not derived from any assets acquired in connection with any trade or business carried on by the institution or society.
  b. The gain or profit is applied solely for the purpose of the institution or society
  c. If any property held in trust by any of the exempted bodies ceases to be subject to such trust, the trustee shall e treated as if they had disposed of and immediately re-acquired the property for a consideration equal to its market value, any gain on the disposal being treated as if it did not accrue to the institution or society.

2. Statutory Bodies

Gains accruing to any local authority shall be exempted from capital gains tax. However, where such gains are derived from the disposal of any assets acquired by the corporation in connection with any trade or business carried on by it or from the disposal of any share or interest possessed by the corporation in a trade or business carried on by some other person or authority, then they shall not be exempted.

3. Retirement Benefits Schemes

Gains accruing from the disposal of an investment held as part of any approved pension provident or other retirement benefits fund society or scheme are exempted from capital gains tax.

The disposal of a right to, or to a part of a sum payable out of an approved retirement benefit scheme is also exempted from capital gains tax.

4. Decorations

Gains accruing on the disposal of a decoration awarded for velour or gallant conduct which was acquired otherwise than for consideration in money or money's worth are exempted from capital gains tax.

5. Stocks and Shares etc

Gains accruing from the disposal of Nigerian government securities are exempted from capital gains tax. Nigerian government securities include Treasury Bonds, Savings certificates and premium bonds etc.

6. Life Assurance Policies

The disposal of a life assurance policy or of a contract for a deferred annuity does not give rise to chargeable gains, except where the person making the disposal is not the original beneficial owner, and acquired the rights, or interest for a consideration in money or money's worth. Thus, gains arising from the disposal of a life assurance policy are exempted from capital gains tax.

7. Personal Injury.

Compensation or damages received for wrongs or injuries suffered by an individual with the exception of compensation for loss of office in excess of N10,000 for any year of assessment are exempted from capital gains tax. However, with effect from 1^{st} January 1995, payment for compensation for loss of office or employment is exempted from tax.

8. Principal Private Residence

Gains arising from the disposal of an individual only or main residence occupied by him throughout the period of ownership, except for all or any part of the last twelve months of that period, are exempted from capital gains tax.

9. Chattels sold for N1,000 or less in a Year

Gains accruing from the disposal of chattels are exempted from capital gains tax provided the total value of the consideration for such disposal does not exceed N1,000 in a year of assessment. Where the consideration exceed N1,000, capital gains tax payable will be limited to half the difference between the consideration and N1,000. A chattel is a tangible movable property, such as an antique or picture, jewelry etc.

10. Diplomatic Representatives

Gains accruing to a diplomatic representative, foreign envoy, foreign consular officer or an employee of any foreign state, from the disposal of any asset are exempted from capital gains tax.

Self Assessment Exercise 10.6

State six circumstances where capital gains tax would be exempted?

4.0 CONCLUSION

In this unit, we discussed capital gains tax. We started by assessing what chargeable assets are and proceeded to gains chargeable, disposal of assets, consideration of asset, cost of asset disposed on partial disposal and finally, we discussed exemptions and reliefs.

5.0 SUMMARY

You should recall that capital gains are those gains that arise from an increase in the market value of assets that were not purchased with the prime intention of resale. Capital gains tax is a tax imposed on capital gains arising from the disposal of chargeable assets. Chargeable assets are all forms of property, except where otherwise, are stated in the Act. Gains chargeable to tax shall be the amount of the consideration accruing on the disposal of an asset, after deducting any sums excluded from such consideration and any allowable expenditure.

An asset is disposed of when there is either a charge of ownership or a transfer of the rights or interest therein.

Consideration of asset acquired/disposed shall be deemed to be equal to the market value of the asset where any person acquired the asset. Where there is a part disposal, the cost of that part of asset disposed and that of the undisposed part shall be apportioned. The cost to be apportioned to the part disposed shall be in the proportion that the consideration for the disposal bears to the total value of the whole assets on the date of disposal.

And finally, you should recall that certain bodies and circumstances are exempted from capital gains tax.

6.0 TUTOR MARKED ASSIGNMENT

1. Explain the following terms
   a. Chargeable assets
   b. Gains chargeable

2. Cosmix Business Enterprise acquired some property in Ibadan in 1982 at a cost of N560,000. A sum of N60,000 was also spent by the organization in enhancing the value of the asset.

On the 1st of September 2007, the enterprise disposed of a part of the property for N480,000. Expenses incurred on the disposal was N37,000. The property retained had a market value of N420,000.

You are required to determine the capital gains tax payable by Cosmix Business Enterprise on the property disposed of.

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

UNIT 11 DOUBLE TAXATION RELIEFS

CONTENT

1.0 INTRODUCTION

Income chargeable to tax under S. 3(1) of the PITD 1993 includes income from a source inside or outside Nigeria. Income from a source outside Nigeria would normally have been subjected to tax in the foreign country according to that country's tax laws. This income is again subject to tax in Nigeria; obviously it is being taxed twice.

Similarly, income accruing in Nigeria to non-resident would have been subjected to Nigerian tax and could also be taxed in the foreign country whenever received by the tax payer where he resides. Thus, the income is taxed twice. In such cases, the tax burden on the taxpayer could be unduly high and it is only reasonable that he should be given some relief.

When there is a double taxation agreement between the country and Nigeria, the amount of relief to be granted will be computed in accordance with the provisions of the agreement and the relevant provision of s. 38 and S. 39 of the PITD.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. state how double taxation is treated where there is no double taxation agreement
2. state how double taxation is treated where there is double taxation agreement
3. state the procedure for the computation of tax liability of an individual with foreign income.

3.0 MAIN CONTENT

3.1 Where there Is No Double Taxation Agreement

With effect from 1st January 1993, whenever, there is no double taxation agreement between Nigeria and a foreign country, there is no double taxation relief available with regards to income from that country.

Previously, a section of the Income Tax Management Act (ITMA) dealt with situations when there is no double taxation agreement between the foreign country and Nigeria. The computation of the relief due during the period ITMA was in force would be based on the provisions of that section. However, there is no such provision in the Personal Income Tax Decree 1993.

Self Assessment Exercise 11.1

How is double taxation treated in situation where there is no double taxation agreement?

3.2 Where there Is No Double Taxation Agreement

Where there is a double taxation agreement between a country and Nigeria, the amount of relief available will be computed on the basis of the provisions of the agreement and the provisions of S. 38 and S. 39 of the Decree.

The relevant points to be noted are:

1. The arrangement in any double taxation agreement shall have effect to afford relief from double taxation in relation to tax imposed on income chargeable by the 1993 Decree and any tax of a similar character imposed by the laws of another country where the income arises.

2. An order made under the provisions of subsection (1) of section 38 may include provisions for relief form tax for periods commencing or terminating before the making of the order and provisions as to income which is not itself liable to double taxation.

3. For the purpose of affording relief in Nigeria from double taxation, the arrangements specified in the seventh schedule shall be deemed to have been are under the provisions of this section and to apply throughout Nigeria with effect from the year of assessment on the first day of January, 1989 in the case of the United Kingdom and in the case of any other country, on such date as is specified in the agreement with that country.

4. Foreign tax means any tax payable in a country which under the arrangement is to be allowed as a credit against tax payable in respect of that income in Nigeria.

5. The amount of the tax chargeable in respect of the income which is liable to both tax and foreign tax shall be reduced by the amount of the credit admissible under the terms of the arrangement.

6. Credit shall not be allowed against tax for any year of assessment unless the person entitled to the income is resident in Nigeria for that year.

7. The credit shall not exceed the amount which would be produced by computing, in accordance with the provisions of this Decree, the amount of the income which is liable to both tax and foreign tax, and then charging it to tax at a rate ascertained by dividing the tax

chargeable (before the deduction of any relief granted by this part of this Decree) on the total income of the individual entitled to the income by the amount of his total income.

8. Total credit to be allowed for any year of assessment shall not exceed the total tax payable by him for that year of assessment. This in effect means refund cannot be made in Nigeria for foreign income tax paid.

9. It is the gross amount of the foreign income that is included in the various calculations, not the net amount received.

10. A tax payer can elect not to take the benefit of the credit available to him under the agreement

11. Any claim for an allowance by way of credit shall be made not later than two years after the end of the year of assessment

12. In the event of any dispute as to the amount of credit allowable, the claim shall be subject to objection and appeal in like manner as an assessment.

Self Assessment Exercise 11.2

State at least six relevant points to be noted where there is a double taxation agreement between Nigerian and a foreign country.

3.3 Procedure for Computing Tax Liability of An Individual with Foreign Income

The procedure for the computation of tax liability of an individual with foreign income is as follows:

1. Compute the total income including the Naira equivalent of the gross foreign income earned

2. Determine the personal reliefs available if the taxpayer is resident in Nigeria in the year involved.

3. Applying the applicable tax rates to the net of (1) and (2). Calculate the Nigerian tax liability

4. If the amount of Nigerian tax payable as computed is lower than the amount of foreign tax, no further tax is payable in nigeria. The credit that shall be allowed shall not exceed the total Nigerian tax payable by the taxpayer.

5. Deduct the relief from the tax liability computed in (2) above to arrive at the final tax liability.

Self Assessment Exercise 11.3

State the procedure for the computation of tax liability of an individual with foreign income

4.0 CONCLUSION

In this unit, we discussed double taxation relief. We started by discussing situation where there is no double taxation agreement and proceeded to situation where there is double taxation agreement and finally the procedure for computing tax liability of an individual with foreign income.

5.0 SUMMARY

You should recall that where there is no double taxation agreement between Nigeria and a foreign country, there is no double taxation relief available with regards to income from that country.

Where there is a double taxation agreement between a country and Nigeria, the amount of relief available will be computed on the basis of the provisions of the agreement and the provisions of S.38 and S.39 of the Decree.

6.0 TUTOR MARKED ASSIGNMENT

1. State at least six relevant points to be noted where there is a double taxation agreement between Nigeria and a foreign country

2. Certain procedures are followed for the computation of tax liability of an individual with foreign income. State them.

7.0. REFERENCES/FURTHER READINGS

Ariwodola, J. A. (2001), Personal Taxation in Nigeria Lagos, JAA Nigeria Limited 4th edition.

UNIT 12 TAXATION OF SETTLEMENT, TRUST AND ESTATES

CONTENT

1.0 INTRODUCTION

We shall begin our discussion on settlements, trusts and estates by considering some important definitions contained among the relevant provisions of the Personal Income Tax Decree of 1993 and the 2nd Schedule of the Decree that relates to the subject matter.

Settlements
A settlements is an agreement in writing made in form of a will or a deed, whereby money or property is set aside for the use or benefit of another person. The person who benefits from the settlement are known as the beneficiary, while the person who makes the settlement is known as the settler.

Trusts
A trust is the conveying of real or personal property to one or more persons with the understanding that it will be applied for the benefit of others or to some specified purpose. Trusts are usually created by will or deed or in some cases by a court order.

Trustees
A trustee is a person who administers a trust or a settlement. A trustee thus holds and takes care of property for the benefit of those entitled to it whom are known as the beneficiaries. It must be noted however, that a trustee could also be a beneficiary.

Estate
An estate is the aggregate of a person's possessions, which may include property, goods and money.

Executor
An executor is the personal representative of a deceased person appointed to administer his estate after his death. An executor is named by the deceased person in his will to act in such capacity.

Thus, he is shouldered with the responsibility of offsetting necessary funeral expenses, getting the will legal proved, settling debts and legacies and dealing with the residence of the estate as directed by the will.

Administrator
An administrator is the personal representative of a deceased person appointed to administer his estate after his death. However, are administrator unlike an executor is not named by the deceased person in his will to act in such capacity. Thus, the administrator is appointed by the court to carryout such duties in respect of either an intestate (i.e. a person who dies without a will) or a testator for whom no executor was appointed or where appointed did not act accordingly

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. State the beneficiaries of the income from an estate
2. Explain the computed income of a settlement
3. State the manner in which computed income of any year is apportioned for assessment
4. State the provision of the Decree relating to double taxation relief as it affects a settlement, trust or estate.
5. State the treatment of fixed assets transferred to the estate of a deceased individual.

3.0 MAIN CONTENT

3.1 Beneficiaries of the Income from and Estate

The following types of persons may benefit from the income of an estate:

1. Persons who are entitled to specific bequests from an estate. Such persons are known as legatees (That is, persons on whom a legacy has been bequeathed).

2. Persons who are entitled to annual payments for an estate. Such persons are known as annuitants, and the annual payment is known as an annuity.

3. Persons who are entitled to income as well as capital at the expiration of the administration period. Such people are known as residuary legatees or residuary devisees.

4. Persons entitled to income from an estate. Such persons are known as beneficiaries. On the death of a beneficiary or after the expiration of a given period, the beneficiary's capital may pass on to some other person. It is referred to as the remainder.

Self Assessment Exercise 12.1

State the beneficiaries of the income form an estate.

3.2 Computed Income of a Settlement

The computed income of a settlement, trust or estate is the income of a period of twelve months ending on 31st December of each year. The ascertainment of such income involves the same basic principles that would apply to any taxable person on whom income tax is imposed for a given year of assessment by the relevant tax authority of the territory in which such taxable person is deemed to be resident. It may be assessed on actual year basis or preceding basis depending on the nature of the income and its source of derivation. Thus, expenses incurred wholly, exclusively, necessarily and reasonably for the purpose of such trade or business would be allowable in accordance with the relevant provisions of PITD 1993, while those not incurred for such purpose would be disallowable for tax purposes. The following deductions would also be allowable

1. Any expenses of the trustee or executor relative to the settlement, trust or estate which are authorized by the terms of the deed of settlement or trust or of the will as the case may be.

2. Any annuity of fixed annual amount paid out of the income of the settlement, trust or estate in accordance with the provisions of such deed or will.

Self Assessment Exercise 12.2

Explain the computed income of a settlement.

3.3 Capital Allowances/Trade Losses

If the income of a settlement, trust or estate includes any gains or profits form any trade, business, profession or vocation or any rents or premiums, there shall be added or deducted any sums which would have been added or deducted as balancing charge or capital allowances or trade losses for the next following year of assessment if the income from these sources had been assessed on the preceding year basis.

In respect of such fixed assets transferred to the estate of a deceased individual:

1. No balancing allowance or charge shall be given or made to that individual in respect of the asset for the year in which the individual died.

2. The estate is deemed to have incurred qualifying expenditure on the acquisition of each such asset equal in amount to the residue of expenditure of the asset on the day following the date of the death.

3. If any of the asset is later disposed, any balancing charge to be made is computed by reference to the total of the allowances granted both to the individual and the estate.

Self Assessment Exercise 12.3

What is the treatment of fixed assets transferred to the estate of a deceased individual?

3.4 Apportionment of Computed Income

The computed income of any year shall be apportioned for assessment in the following manner:

1. Where the terms of the deed of settlement or trust or of the will provide that the whole income after deduction of any authorized expenses or annuities of fixed amount is to be divided in computed income is apportioned on the beneficiaries on a similar basis.

2. Where a trustee or executor has discretion to make any payment (other than a payment on account) to a beneficiary out of the income of any year, that amount is assessable on that beneficiary in the year of receipt. In such situation, the balance of the income after deduction of the discretionary payment shall be apportioned to the other beneficiaries in their respective proportioned interest. Provided that if such aggregate amount exceeds the computed income, the amount apportioned to each of the beneficiaries shall be proportionately reduced such that the total amount apportioned does not exceed the computed income.

3. Any remainder of the computed income of any year after deducting all amounts apportioned to, or treated as income in the hands of, beneficiaries is assessable on the trustee or executor in his name as trustees of the settlement or trust or as executor of the estate.

Self Assessment Exercise 12.4

What is the manner in which computed income of any year is apportioned for assessment?

3.5 Double Taxation Relief

Where the income of a settlement, trust or estate of any year includes any income which has borne tax in Nigeria or elsewhere, whether by deduction or otherwise, the provisions of the Decree relating to double taxation relief will be applicable to the persons to whom the computed income of the year is apportioned either:

a. In due proportion to their respective shares therein or

b. Where the trustee or executor can make discretionary payment, in proportion to their shares in the remainder of the computed income as specified, and

c. Where there is no computed income, the relief or repayment shall be given or made to the trustee or executor for the account of the settlement, trust or estate

Self Assessment Exercise 12.5

What is the provision of the Decree relating to double taxation relief where the income of a settlement, trust or estate of any year includes income which has borne tax in Nigeria or elsewhere?

4.0 CONCLUSION

In this unit, we discussed taxation of settlement, trust and estates. We started by discussing the beneficiaries from the income of an estate and proceeded to computed income of a settlement, capital allowances/Trade losses, apportionment of computed income and finally double taxation relief.

5.0 SUMMARY

You should recall that a settlement is an agreement in writing made in form of a will or a deed, whereby money or property is set aside for the use or benefit of another person. A trust is the conveying of real or personal property to one or more persons with the understanding that it will be applied for he benefit of other or to some specified purpose.

An estate is the aggregate of a person's possessions which may include property, goods and money. An executor is the personal representative of a deceased person appointed by the deceased person as named in his will to administer his estate after his death. An administrator is the personal representative of a deceased person appointed by the court to administer the estate of the deceased person after his demise.

The computed income of a settlement, trust or estate is the income of a period of twelve months ending on 31st December of each year.

6.0 TUTOR MARKED ASSIGNMENT

1. State the beneficiaries of the income from an estate
2. Explain the computed income of a settlement
3. In what manner is the computed income of any year apportioned for assessment?

7.0 REFERENCES/FURTHER READINGS

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagos, JAA Nigeria Limited, 4th Edition.

MODULE 3 TYPES OF TAXES

UNIT 13 TAXATION OF SPECIAL BUSINESS

CONTENT

1.0 INTRODUCTION

In this unit, we shall be discussing the taxation of special business such as Insurance Companies, Airline and Shipping Companies according to the provision of the Company Income Tax Act. The provisions which shall be discussed are additional to the normal rules of allowance and disallowable expenditure in taxation practice which must applied in all circumstances.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Calculate taxable profit for a non-life insurance companies
2. Compute taxable profit for life assurance companies
3. Compute taxable profit for air line transport companies

3.0 MAIN CONTENT

3.1 Taxation of Insurance Companies (CITAS 14)

The profits on which tax may be imposed for non life insurance companies shall be ascertained thus, gross premiums plus interest and other income receivable less any returned premium and premium paid on reinsurance less reserve unexpired risks at the end of the period. Add reserve for unexpired risks at the beginning of the period less actual losses settled during the period net of settlement by reinsurers less other allowable expenses.

The profits on which tax may be imposed for a life assurance company shall be the investment income less the management expenses including commission. Any amount distribution as divided from the actuarial revaluation of unexpired risks or from any other revaluation shall be deemed to be a part of the total profits of the company.

The company shall provide the Board full particulars of the revaluation carried out, not more than three months after an actuarial revaluation of the unexpired risks or any other revaluation has taken place.

You should note that while in non-life insurance business, there is reference to premium, investment incomes, and reserves for unexpired risks and claims settlements, in a life insurance business the reference is only to investment income, management expenses and commissions.

Example

Safety Insurance Nigeria Plc is a company engages in non-life insurance policies, has the following details of its transactions for the year ended 3oth June, 2006.

			₦
Premium Received			1, 800, 000
Re – Insurance premium			620, 000
Subscription as member of the			
Nigerian Insurance Association (NIA) (allowable)		8, 000	
Contribution to State Education Funds (allowable)		13, 000	
Unexpired risks - 01/07/05			345, 000
- 30/06/06	460, 000		
Claims		170,000	
Amount recovered under reinsurance		90, 000	
Salaries and other administrative expenses		300, 000	
Capital allowances were:			
Initial allowances			60, 000
Annual allowances			70, 000
Balancing charge			10, 000

You are required to compute the tax payable by the company for 2007 year of assessment (Assume companies' rate of tax at 30%)

Solution

Safety Insurance Nigerian Plc

Tax consumption for 2007 year of assessment

	₦	₦
Premium Received		1, 800, 000
Re – insurance premium		(620, 000)
		1, 180, 000
Unexpired risks 30/06/06		(460, 000)

Unexpired risks 01/07/05		345, 000
Claims settled	170, 000	
Less received under reinsurance	(90, 000)	(80, 000)
Less: allowance expenditure:		
Salaries and other admin	300, 000	
Subscription to NIA	8, 000	
Contribution to state education funds	13, 000	(321, 000)
		664, 000
Add balancing charge		10, 000
		674, 000
Less capital allowances		
Initial	60, 000	
Annual	70, 000	(130, 000)
Chargeable profit		544, 000
Tax payable at 39%		₦163, 2000

Example

Life Assurance Limited is a Nigerian Life assurance Company and the following figures were extracted from its trial balance for the year ended 31st December, 2002

		₦
Premiums (Gross) received during the year	870, 000	
Dividends received during the year from		
Nigerian Companies (Gross)	450, 000	
Rental income (Gross)		1, 800, 000
Claims and Commissions (expenses)	650, 000	
Management expenses		820, 000

You are given the following additional information

1. Capital allowances for the year were agreed at ₦25, 000

2. Management expenses include:

Provision for April 2003 staff training course	₦12, 000
Deficit on staff canteen account	₦3, 500
Club subscriptions	₦3, 000
Scholarship to actuarial science students	
At local university	₦2, 500
Donation to Islamic Education Trust	₦7, 000
Depreciation	₦15, 000

3. Agreed trading losses brought forward from 2001 of which the amount of ₦250, 000 relates to 1997 amounted to ₦320, 000

Compute life Assurance Limited's taxable profit or allowance loss for the year, assuming companies rate of tax as 40%.

Solution

Life Assurance Limited

Income tax computation for year of assessment

	₦	₦
Dividend Income (Gross)		450, 000
Rental Income (Gross)		1, 800, 000
		2, 250, 000
Less claims and commissions		650, 000
		1, 600, 000
Management expenses	820, 000	
Less disallowable expenses:		
Provision for training course	(12, 000)	
Club subscriptions	(3, 000)	
Depreciation	(15, 000)	(790, 000)
Assessable profit		810, 000
Losses brought forward	320, 000	
Less amount that has lapsed	250, 000	(70, 000)
		740, 000
Less capital allowances		(25, 000)
Total profits		715, 000
Income tax thereon at 40%		₦286, 000

Self Assessment Exercise 13.1

1. Secured Insurance Nigeria Plc is a company engage in non–life insurance policies, has the following details of its transactions for the year ended 30th April, 2004.

		₦
Premium received		1, 500, 000
Re-insurance premium		410, 000
Subscription as member of the		
Nigerian Insurance Association (NIA) (allowable)		9, 000
Contribution to state Education Funds (allowable)		14, 000
Unexpired risks - 01/05/03		250, 000
- 30/04/04	390, 000	
Claims		120, 000
Amount received under reinsurance		80, 000
Salary and other administrative expenses		250, 000
Capital allowances were:		
Initial allowances		50, 000
Annual allowances		90, 000
Balancing charge		15, 000

You are required to compute the tax payable by the company for 2005 year of assessment assuming companies rate of tax at 35%

2. High Level Assurance Limited is a Nigerian Life Assurance Company and the following figures were extracted from its trial balance for the year ended 31st December, 2007.

	₦
Premium (Gross) received during the year	940, 000
Dividends received during the year	
From Nigerian Companies (Gross)	520, 000
Rental income (Gross)	1, 200, 000
Claims and Commissions	440, 000
Management expenses	620, 000

The following additional information are:

1. Capital allowances for the year were agreed at ₦17, 000

2. Management expenses include:

General provision of	₦14, 000
Club subscription of	₦3, 500
Depreciation of	₦16, 000

3. Agreed trading loss brought forward from 2006 of which the amount of ₦150, 000 relates to 2002 amounted to ₦280, 000

You are required to compute:
High
Level
Assurance Limited's taxable profit or allowable loss for the year assuming companies' rate of tax as 45%

3.2 Taxation of Airline and Shipping Companies

CITA section 12 contains provisions regarding companies, other than Nigerian Companies, in shipping or air transport business.

The content of that section is as follows:

- The profits or loss of such company to be deemed to be derived from Nigeria is the full profits or loss arising from the carriage of passengers, mails, livestock or goods shipped, or loaded into an aircraft in Nigeria. This does not apply to passengers, mails, livestock or goods which are brought into Nigeria solely for transshipment or for transfer from one aircraft to another or in either direction between an aircraft and ship.

- To the sums receivable in respect of passengers etc. carried in Nigeria as referred to above, there shall be applied the following

    a. The ratio of profits or loss of an accounting period, before depreciation, to the total sums receivable in respect of the business of the company.

b. The ratio of depreciation to the total sums receivable as certified by the tax authority of any other country (where the Non-Nigerian company is registered) to the satisfaction of the Board.

The amount arrived at shall be the full profits or loss which shall be liable to Nigeria tax.

- Where the ratio referred to above cannot, for any reason be satisfactorily applied, the profits to be deemed to be derived from Nigeria may be computed on a fair percentage on the full sum receivable in respect of the carriage of passenger etc. shipped of loaded in Nigeria. When this occurs, the company has within six years to claim that its liability be re-computed on the basis of the ratios referred to above.

- If the company fails to agree with the Board, the Board shall give notice to the company of refusal to admit the claims and the provisions of CITA with respect to objections and appeals shall apply accordingly with any necessary modifications.

From the 1988 assessment year sub-section (4) was added to section 12 to the effect that the tax payable for any year of assessment shall not be less that 2% of the full sums receivable in respect of the carriage of passengers, mails, livestock or goods shipped or loaded into an aircraft in Nigeria.

Example
Cross Bridge Airline is an air transport company registered in the United Kingdom. On it's scheduled flight to West Africa the planes land in Lagos to pick passengers whose destination is Paris. Transactions are carried out in Nigeria by this company through an authority agent who sells tickets and meets necessary financial obligations on behalf of Cross Bridge Airline. The agent sold ₦4, 500, 000 tickets on behalf of the company in 1980 and incurred the following local expenses in Nigeria.

	₦
Wages to laborers and security	30, 000
Office expenses	20, 000
Electricity and rates	15, 000
Trade subscription	3, 000
	68, 000

In order to obtain Tax clearance certificate for the purpose of remitting proceeds from air transport business to the home county, the agent consulted you to prepare the tax payable to the Federal Board of Inland Revenue. He informed you that:

a. 20% of total ticket sale proceeds is allowed annually by Federal Inland Revenue to cover depreciation allowance of assets.

b. 30% of the ticket sale proceeds is allowed annually to cover share of Head Office overhead.

c. Local expenses in Nigeria are allowable in full.

You are required to compute the tax payable in Nigeria.

Solution:
Cross Bridge Airline
Nigeria Income Tax Computation

	₦	
Sales proceeds	4, 500, 000	
Less		
Allowed Head of Office expenses (3% 0f 4, 500, 000)		(1, 350, 000)
Depreciation allowance (20% of 4, 500, 000)		(900, 000)
Local expenses		(68, 000)
Chargeable profit		2, 182, 000
Income tax at 45% thereon	₦981, 900	

You should note that the rate is 45% for 1980 assessment year.

Example
British Airline Limited, s a foreign company operating a fleet of passenger and cargo aircrafts between Nigeria and Europe. The operating results for the year ended 31st July, 1991 are as follows:

		₦
Income from cargo fright Nigeria / Swiss		420, 000
Income from passengers' freight Nigeria / Italy		580, 000
Income from passengers' freight Scotland to Nigeria		720, 000
Income from cargo loaded into aircraft on other routes		320, 000
		2, 040, 000
Less: Operating expenses:		
Salaries and other expenses	750, 000	
Depreciation	120, 000	
General provision	40, 000	(910, 000)
Operating profit		1, 130, 000

The following additional information is provided

a. Salaries and other expenses include:

		₦
1.	Purchase of twin engines	120, 000
2.	Use of airport facilities	20, 000
3.	Hotel bills for first class passengers	25, 000
4.	Accommodation for airline crew	5, 000
5.	Gifts to airport staff for gratification	8, 000

b. Capital allowances were agreed with the relevant authority as 140% of depreciation charge in the accounts

You are required to compute:

1. The total profits of British Airline Limited for the purpose of the Nigerian income tax

2. The liability to income tax in respect of the chargeable income and state the relevant year of assessment.

Solution

British Airline Limited
Income Tax Computation
Income from cargo / passengers arising from Nigeria

	₦	
Income from cargo freight Nigeria / Swiss	420, 000	
Income from passengers' freight Nigeria / Italy	580, 000	
	1, 000, 000	
Allowable deductions:		
Salaries and other expenses as given	750, 000	
Less: disallowable expenditure include		
Gifts to airport staff for gratification	8, 000	
	742, 000	
Proportion applicable to Nigeria operations		
$= \frac{742,000}{2,040,000} \times 1,000,000$	= 363, 725	
Depreciation allowance as agreed with		
Tax authority 140% of ₦120, 000	= 168, 000	(531, 725)
Chargeable profits		468, 275
Income tax at 40%		₦187, 310

You should note that the minimum tax payable is 2% of ₦1, 000, 000 i.e. ₦20, 000 according to the provision of subsection 4 of section 12 of CITA since 1988.

However, since the tax computed is greater than this minimum tax, the tax payable is the figure of ₦187, 310 as computed.

The relevant year of assessment is 1992.

Self Assessment Exercise 13.2

Crux Airline Limited is an air transport company registered in the United States of America. On its scheduled flights to West Africa, the planes land in Lagos to pick passengers whose destinations are either Italy or Paris. Transactions are carried out in Nigeria by this company through an authorized agent who sells tickets and needs necessary financial obligations on behalf of Crux Airline. The agent sold ₦7, 000, 000 tickets on behalf of the company in 1980 and incurred the following local expenses in Nigeria.

	₦
Wages to labourers and security me	60, 000
Office expenses	45, 000
Electricity and rates	20, 000
Trade subscription	6, 000
	131, 000

In order to obtain tax clearance certificate for the purpose of remitting proceeds from air transport business to the home country, the agent consulted you to prepare the tax payable to the Federal Board of Inland Revenue. He informed you that:

a. 25% of total tickets sale proceeds are allowed annually by Federal Inland revenue to cover depreciation allowance of assets.

b. 35% of total ticket sale proceeds are allowed annually to cove share of Head Office overhead.

c. Local expenses in Nigeria are allowable in full.

You are required to compute the tax payable in Nigeria.

4.0 CONCLUSION

In this unit, we discussed taxation of special business. We discussed the taxation of Insurance companies and the taxation of Airline and Shipping companies.

5.0 SUMMARY

You should recall that the profits on which tax may be imposed for non-life insurance companies shall be ascertained thus, Gross premiums plus interest and other income receivable less any returned premium and premium paid on re-insurances less reserve for unexpired risks at the end of the period. The profit which tax may be imposed for a life assurance company shall be the investment income less the management expenses including commission.

6.0 TUTOR MARKED ASSIGNMENT

1. Secured Insurance Nigeria Plc is a company engaged in non-life insurance policies, has the following details of its transaction for the year ended 31st December, 2003

	₦
Premium received	2, 200, 000
Re-insurance premium	780, 000
Subscription as member of the Nigeria Insurance Association (allowable)	10, 000
Contribution to State Education Funds (allowable)	15, 000
Unexpired risks - 01/01/03	420, 000
- 31/12/03	580, 000

Claims	280, 000
Amount received under reinsurance	120, 000
Salary and other administrative expenses	450, 000
Capital allowances were:	
Initial allowances	70, 000
Annual allowances	90, 000
Balancing charge	20, 000

You are required to compute the tax payable by the company for 2004 year of assessment using 30% tax rate.

2. Heritage Assurance Limited is a Nigerian life assurance company and the following figures were extracted from its trial balance for the year ended 30th June, 2004.

	₦
Premium (Gross) received during year	920, 000
Dividends received during the year from Nigerian Companies (Gross)	380. 000
Rental income (Gross)	980, 000
Claims and commissions (expenses)	250, 000
Management expenses	420, 000

The following are additional information

a. Capital allowance for the year were agreed at ₦20, 000
b. Management expenses include
   General provision of ₦15, 000
   Club subscription of ₦4, 000
   Depreciation of ₦14, 000
c. Agreed trading loss brought forward from 2003 of which the amount of ₦90, 000 relates to 1999 amounted to ₦160, 000

You are required to compute Heritage Assurance Limited's taxable profit or allowable loss for the year assuming companies rate of tax as 30%.

3. Nobel Airline Limited is a foreign company operating a fleet of passenger and cargo aircrafts between Nigeria and Europe. The operating results for the year ended 31st December, 1991 are as follows

	₦	₦
Income from passengers' freight Italy to Nigeria		620, 000
Income from cargo loaded into aircraft on other routes		520, 000
Income from cargo freight Nigeria to Germany		820, 000
Income from passengers' freight Nigeria to Swiss		480, 000
		2, 440, 000
Less: operating expenses:		
Salaries and other expenses	680, 000	
Depreciation	90, 000	
General provision	30, 000	(800, 000)
Operating profit		1, 640, 000

The following additional information is provided

a. Salaries and other expenses includes:

		₦
1.	Purchase of twin engines	160, 000
2.	Use of aircraft facilities	40, 000
3.	Hotel bills for first class passengers	25, 000
4.	Accommodation for airline crew	60, 000
5.	Gifts to airport staff for gratification	7, 000

b. Capital allowances were agreed with the relevant tax authority as 170% of depreciation charge in the accounts.

You are required to compute:

1. The total profits of Nobel Airline Limited for the purpose of the Nigerian income tax
2. The liability income tax in respect of the chargeable income and state the relevant year of assessment using 40% tax rate.

7.0 REFERENCES / FURTHER READING

Ariwodola J. A. (2000). Companies Taxation in Nigeria, Lagos, JAA Nigeria Limited Third edition

UNIT 14 WITHHOLDING TAX

CONTENT

1.0 INTRODUCTION

The cost and problems of tax collection are quite enormous. One of the ways of achieving optimum result is the aspect of the tax laws which make it mandatory for certain in come to be taxed at source under the applicable laws, the payers of sun due to another person are required to withhold certain amount from such sums as tax and pay the rent amount to the payee. The amount withheld is what is termed withholding tax and is payable to the appropriate tax authority. The payee will be given a certificate evidencing the amount of tax deducted. When the payee is computing his total income, it is the gross amount, not the rent which he actually received, that will be treated as income to him and on which his tax liability will be calculated. The amount of tax withheld will be deducted from the payee's tax liability to arrive at the balance of tax payable.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Explain withholding tax on interest or royalty
2. Explain withholding tax on rent
3. Explain withholding tax on dividend
4. Explain franked investment income
5. Explain the relevant tax authority relating to withholding tax and withholding tax return

3.0 MAIN CONTENT

3.1 Withholding Tax on Interest or Royalty

Where any interest or royalty is due or payable to any person, the payer must at the date when the payment is made or credited (whichever occurs first) deduct tax therefrom at the rate of 10%

of the gross interest and 5% of gross royalty and pay the amount deducted of the stats in which the recipient is demand to be resident in the year of assessment .where the recipient is deemed to be resident in the federal capital territory, Abuja, in the year of assessment the withholding tax will be paid to Federal Board of Inland Revenue, the tax deducted must be paid over to the relevant tax authority within 30 days from the date it was deducted .

Any interest receivable on a savings account deposit of up to ₦50,000 or below is exempted from withholding tax while savings deposit above ₦50,000 are liable to withholding tax also any interest receivable on inter bank deposit is not liable to withholding tax only companies, Government, Ministries and Department Parastatals, statutory bodies and other established organization approved for the operation of payer including any person engaged in banking or charged with administration of federal savings bank that are permitted to deduct withholding tax on interest or royalty due.

Self Assessment Exercise 14.1

Explain withholding tax on interest or royalty.

3.2 Withholding Tax on Rent

Where a rent becomes due or payable to a person the payer of such rent shall ,at the date when the rent is paid or credited whichever risk occurs deduct tax there from at the rate of job of the gross rent and pay over the amount deducted to the relevant tax authority.

The pay of such rent has been defined in the Decree as any company (corporate or unincorporated) including Government, Ministries and Department, Parastatals, Statutory bodies, Institution and other established organization approved for the operation of PAYE whether or not liable itself to tax under any enactment or law relating to taxation of income in Nigeria or elsewhere. Individual paying rent to other person or to companies is not to deduct withholding tax except if such individuals can be described as established organizations approved for the operation of PAYE.

Partnerships or group of individuals or an individual registered under the Registration of Business names Act 1961 and who are approved to operate PAYE scheme are to deduct withholding tax when paying rents.

Self Assessment Exercise 14.2

Explain withholding tax on rent.

3.3 Withholding Tax on Dividend

Where a dividend becomes due from or payable by a Nigerian company to a person, the company making such payment shall, at the date when the amount is paid or credited whichever first occurs, deduct tax therefore at the rate of 10% and pay over the amount deducted to the relevant tax authority, that is, the tax authority of the state in which the recipient is deemed to be resident is deemed to be resident in the year of assessment. Where the recipient is deemed to be resident in the Federal Capital Territory, Abuja, in the year of assessment, then the withholding tax deducted will be paid to the Federal Board of Inland Revenue. The tax deducted must be paid over to the relevant tax authority within 30 days from the date it was deducted.

It should be stressed that only those approved for the operation of PAYE are permitted to deduct withholding tax from dividend due.

Self Assessment Exercise 14.3

Explain withholding tax on dividend.

3.4 Franked Investment Income

Franked investment income is the income derivable from payment of dividend by a company to another company. For instance, where a Nigerian company pays dividends to another Nigerian company, it will deduct withholding tax at source. Such dividends shall not be charged to further tax in the hands of the recipient company as they are deemed to have suffered tax at source. Such income is referred to as franked investment income.

Where the recipient company redistributes such dividend income by paying its own dividends from the income, and tax is to be accounted for on the gross amount of such distribution, it may set-off the withholding tax it suffered on the income against the tax it would be expected to deduct from the dividends payable to its own shareholders.

That is, a holding company would not be charged to tax on dividends received from a subsidiary or associated company. And if it used such dividend income to pay dividends to its own shareholders, it would get a relief for the withholding tax paid on the dividend received from the subsidiary company.

Self Assessment Exercise 14.4

What is Franked Investment Income?

3.5 Relevant Tax Authority and Withholding Tax Return

The relevant tax authority is to be determined be reference to the residence of the recipient of the amount. The relevant tax authority has been defined in the Decree as the Internal Revenue Authority of the state in which the recipient is deemed to be resident in the year of assessment for tax purposes, a person is deemed to be resident in a state where he has his residence on the 1st of January of the year of assessment.

In the case of savings interest, the relevant tax authority shall be that where the bank branch paying the interest is situated. Where any withholding tax is deducted from amounts due to any company or corporation, the relevant tax authority shall be the Federal Inland Revenue Board.

The following information should be submitted to the relevant tax authority when remitting withholding tax.

a. The gross amount of the payment
b. The name and address of the recipient
c. The amount of tax withheld
d. In respect of rent, the address or accurate description of the location of the property and the period which the rent covers.
e. In respect of dividend, the accounting period relating to the profits out of which the dividend is declared to be payable and the date on which payment is due.

Self Assessment Exercise 14.5

Explain the relevant tax authority in respect of withholding tax.

4.0 CONCLUSION

In this unit, we discussed withholding tax. We started by explaining withholding tax on interest or royalty according to the provision of the law. We proceeded to withholding tax on rent, dividend, franked investment income and finally, discussed the relevant tax authority relating to withholding tax and withholding tax return.

5.0 SUMMARY

You should recall that the payers of sum due to another person are required to withhold certain amount from such sums as tax and pay the net amount to the payee. The amount withheld is what is deemed withholding tax and is payable to the relevant tax authority.

Where a Nigerian company pays dividends to another Nigerian company, it will deduct withholding tax at source. Such dividend shall not be charged to further tax in the hand of the recipient company as they are deemed to have suffered tax at source. Such income is referred to as franked investment income.

6.0 TUTOR MARKED ASSIGNMENT

1. What is franked investment income?
2. Explain withholding tax on interest or royalty.
3. Explain withholding tax on rent.

7.0 REFERENCES / FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagod, JAA Nigeria Limited, 4th Edition.

UNIT 15 PIONEER INDUSTRIES

CONTENTS

1.0 INTRODUCTION

A company is an organization (other than a private company) limited and incorporated and registered in Nigeria and resident in Nigeria. A pioneer company is a company certified by any pioneer certificate to be a pioneer company. The pioneer industry represents any trade or business of the kind included in any list of pioneer industries published in the gazette.

The gazette is the federal gazette and includes the gazette of any state in the federation. One of the investments in countries available to industries in Nigeria is that under the industrial Development (income tax relief) Act which grants tax holidays to companies in the industries that meet the conditions of being designated pioneer industries.

The tax holiday is usually for an initial period of three years but can be extended for an additional two years maximum

2.0 OBJECTIVES

After studying this unit, you should be able to pioneer industry:

1. State the content of an application of any company requesting for a pioneer certificate.
2. State the procedure of certifying the amount of qualifying capital expenditure.
3. State reasons that could necessitate the cancellation of pioneer certificate
4. Explain income tax relief and losses incurred within the tax relief period
5. Explain taxable profit, exempted profit and dividend distributed from exempted profits

3.0 MAIN CONTENT

3.1 Pioneer Conditions

The national council of ministers (the council) may declare industries as pioneer products where the council is satisfied that:

- any industry is not being carried on in Nigeria on a scale suitable to the economic requirements of Nigeria or at all, or

- there are favorable prospectus of further development in Nigeria of any industry; or

- it is exempted in the public interest to encourage the development or establishment of any industry In Nigeria by declaring the industry to be pioneer industry and any product of the industry to be a pioneer product.

A company that wishes to engage in an industry or manufacture products which have not been designated pioneer may submit an application for the industry to be included in the list of pioneer industries and its products are included in the list of pioneer product. A successful application in either case is issued with a pioneer certificate in which conditions under which the income tax relief can be enjoyed will be stated.

For any application for a pioneer certificate to be considered, the estimated cost of qualifying capital expenditure to be incurred by the company on or before production day shall not be less than:

a. 150,000 in the case of an indigenous controlled company or
b. 150,000 in the case of any other company.

Self Assessment Exercise 15.1

What would the national council of ministering consider before issuing a pioneer certificate to a company?

3.2 Application for Pioneer Status

Application for pioneer status can be made by a company incorporated in Nigeria or by a group of persons on behalf of a company which is to be incorporated later. The application shall be on a prescribed form. Ever such application shall state the grounds upon which the applicant relies and if the application is for the issues of a pioneer certificate to any company, the application shall:

a. State whether the company is, or the indigenous controlled company

b. Give particulars of the assets on which qualifying capital expenditure will be incurred by the company, including their resource and estimated cast

c. On or before production day and

d. During a period of three years following the production day.

e. Specify the place in which the assets are to be situated.

f. State the probable date of production day

g. Specify any product and by product (not being a pioneer product to be produced, and give a reasonable estimated of the qualities and value, of such product and by product during a period of one year from production day

h. Give particulars of the loan and share capital including the amount and date of each issues and the source from which the capital is to be or has been raised.

i. In the case of a company already incorporated, give the name, address and nationality of each director and the number of shares held by him

j. In the case of a proposed company, give the name, address and nationality of each promoters of the company.

After considering any application made, together with such further information as may be called for, the director shall issue a certificate to the pioneer company certifying the date of its production day, you should note that the period of the tax holiday shall commence from the production day.

Self Assessment Exercise 15.2

What should be the content of an application requesting for a pioneer certificate to any company?

3.3 Certification of Qualifying Capital Expenditure

A pioneer to the board to certify the amount of the qualifying capital expenditure incurred by the company prior to production day, not later than one month after the production day of a pioneer company has been finally determined and certified by the director or within such extended time as the board may allow.

The proceeds of disposal of any item of capital expenditure disposed of prior to production day shall be deducted from the total amount of capital expenditure incurred to arrive at the amount to be certified. Also, if any of such disposal has not been made in an arm‘s length transaction, the open market value on the date of the disposal shall be submitted for the disposal proceeds.

After considering the application made for the certification of qualifying capital expenditure as above together with such further information as may be requested, the board shall issue a certificate to the pioneer company certifying the amount of qualifying capital expenditure incurred by the company prior to production date.

Self Assessment Exercise 15.3

What is the procedure of certifying the amount of qualifying capital expenditure incurred by a company prior to production day?

3.4 Cancellation of Pioneer Certificate

The pioneer certificate issues to any company can be cancelled if:

1. The production day has been certified as on a date which is more than one year later than the estimated there of given in the company's application for a pioneer certificate. How ever, the council will not cancel the certificate if it is satisfied that the delay is due to causes outside the control of the company or do other good and sufficient cause.

2. The certificate of qualifying capital expenditure as on the production day is to the effect that the amount of qualifying capital expenditure incurred as on that day is less than the prescribed minimum applicable to the company.

3. The pioneer company concerned applies for other provision of the industrial development income act or has failed t fulfill any estimate or proposal made in its application for a pioneer certificate or any of the conditions contained in its pioneer certificate

Self Assessment Exercise 15.4

What could necessitate the cancellation of a pioneer certificate?

3.5 Income Tax Relief and Losses

A company holding a pioneer certificate shall be on a tax holiday for the period stated on the certificate. The tax relief period is usually for a period of three years at the first instance commencing on the date of the production day of the company unless cancelled or restricted in any manner by the council.

If certain requirements are met, the council may at the end of the three years extend the tax relief period to:

a. Two period of one year each or
b. One period of two years

A pioneer company wishing to obtain such extension shall apply in writing within one month of the expiration of the initial three years tax relief period or of any extension there of. Such application shall contain details of all capital expenditure incurred by the company by the requisite date. The requisite date is the date of expiry of a pioneer certificate.

Where the board is satisfied that a pioneer company has incurred a loss in any accounting period within the tax relief period, it shall issue a certificate to the company accordingly.

In determining whether such a loss has been made, the board may in its absolute discretion exclude such sum as may be in excess of an amount appearing to the board to be just and reasonable in respect of:

a. Remuneration to directors of the company

b. Interest, service, agency or other similar changes made by a person who is a shareholder of the company or by a person controlled by such shareholder.

A net loss incurred by a pioneer company shall be deemed to have been incurred by the company on the day on which its new trade or business commences that is, on the day following the expiry of the tax relief period.

For each accounting period the board shall issues to the pioneer company a statement showing the amount of the income or loss for that period.

Net loss means the aggregate of losses incurred during the tax relief period after deduction of profit, if any, made at any time during that period.

Self Assessment Exercise 15.5

1. What is tax relief period granted to a pioneer company?

2. Describe the treatment of a loss incurred by a pioneer company within the tax relief period.

3.6 Taxable Profit, Exempted Profit and Dividend

Any profit earned by a pioneer company from any operations or activities whatsoever other than its pioneer enterprises shall be deemed to be derived from Nigeria and shall be liable to tax under company income tax act (CITA)

Any profit shown on the statement issued by the board in respect of the income of a pioneer company for each of the accounting period of its tax relief period shall not form part of the assessable profit or total profits of the pioneer company for any Year of assessment and shall be exempted from tax under CITA.

Any amount of profit that is exempted from tax as stated above should be credited by the pioneer company to an account to be kept for the purpose of dividend that is declared by the company out of such profit shall be exempted from tax in the hands of the shareholders and shall for the purposes of CITA and PITD be deemed to be paid out of profits on which tax is not paid or payable during a tax relief period, a pioneer company shall not:

a. Make any distribution to its shareholders, by way of dividend or bonus, in excess of the amount by which the account maintained for the exempted profits is in credit at the date of such distribution

b. Grant any loan without first obtaining the consent of the minister. The consent of the minister shall only be given if he is satisfied that the pioneer company is obtaining adequate security and a reasonable interest for any such loan.

Self Assessment Exercise 15.6

Explain the following:

a. Taxable profits
b. Exempted profits
c. Dividends distributed from exempted profits

4.0 CONCLUSION

In this unit, we discussed pioneer industries. We started by discussing the conditions required to be a pioneer company and proceeded to what should be the content of an application requesting for a pioneer certificate to any company, how is certificate for qualifying capital expenditure obtained, what can result to the cancellation of pioneer certificate, what is income tax relief and losses and finally, what is taxable profits, exempted profit and dividend distributed from exempted profits.

5.0 SUMMARY

You should recall that a pioneer industry is any trade or business of the kind included in any list of pioneer industries published in the federal gazette or state gazette in the Federation. A pioneer company is a company certified by any pioneer certificate to be a pioneer company.

A company holding a pioneer statement issued by the board in respect of the income of a pioneer company for each of the accounting period of its tax relief period shall not form part of the assessable profit or total profit of the pioneer company for any year of assessment and shall be exempted from tax under CITA.

6.0 TUTOR MARKED ASSIGNMENT

1. What should be the content of an application of any company requesting for a pioneer certificate?

2. What could necessitate the cancellation of a pioneer certificate?

3. Explain the following
   a. Taxable profits
   b. Exempted profits

c. Dividend distributed from exempted profits.

7.0 REFERENCES / FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagod, JAA Nigeria Limited, 4th Edition.

UNIT 16 EDUCATION TAX

CONTENT

1.0 INTRODUCTION

The Education Tax Decree 1993 imposed an education tax on companies registered in Nigeria and establishes an Education Fund into which the tax collected shall be paid.

The Decree also establishes a Board of Trustees to manage and administer the fund for disbursement to Federal, State and Local Government educational institutions including secondary and primary schools, for the restoration, rehabilitation and consolidation of education in Nigeria.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Describe the assessment and collection of education tax.
2. Describe the education tax
3. List offences and penalties.

3.0 MAIN CONTENT

3.1 Assessment and Collection of Education Tax

The assessment and collection of education tax is the responsibility of the Federal Board of Inland Revenue. The assessment is carried out along with the assessment of any company for Companies Income Tax or Petroleum Profit Tax.

The payment of the tax assessed under this Decree is due within 60 days of the service of the notice of assessment on a company. The Federal Board of Inland Revenue shall pay the tax collected to the Education Fund set up under the Decree with necessary details to the Fund's Board of Trustees.

Self Assessment Exercise 16.1

Explain the assessment and collection of education tax.

3.2 The Tax

Education tax is payable by all companies both those companies subject to Companies Income Tax Act and Petroleum Profit Tax Act, from the 1993 assessment year at the rate of 2% of the assessable profits.

The assessable profits to be used would be as defined in the tax legislation. Assessable profit as defined by CITA is usually the tax adjusted profit but before giving effect to loss relief, balancing chare and capital allowances.

Self Assessment Exercise 16.2

Describe the education tax.

3.3 Offences and Penalties

The following constitute offences in tax law and the penalties imposable on such offences:

1. If the tax assessed is not paid within the 60 days time limit, a penalty of 5% flat of the sum assessed shall became payable

2. If the tax and the penalty are not paid within a further period of two months from the date of demand, the company is guilty of an offence under the Decree.

   Section 6, subsection 4 states:

   Where an offence under this decree is committed by a body, corporate or firm or other association of individuals:

   a. Every partner or officer of the firm similar officer of the body corporate
   b. Every partner or officer of the firm
   c. Every person concerned in the management at the affairs of the association or
   d. Every person who was purporting to act in capacity as aforesaid,

   Is severally guilty of that offence and liable to be proceeds against and punished for the offence as if he had committed the offence himself. The defense available to such person is a proof that the act or omission constituting the offence took place without his knowledge, consent or connivance.

   Section 7 of the Decree specifies the penalties as follows:

   A person who is guilty of an offence under this Decree shall on conviction be liable

a. For a first offence, to a fine, of ₦10, 000 or imprisonment for three years

b. For a second and subsequent offence, to a fine of ₦20, 000 or imprisonment for five years, or to both such fine and imprisonment.

Self Assessment Exercise 16.3

Describe the offences and penalties of education tax.

4.0 CONCLUSION

In this unit, we discussed education tax. We started by discussing briefly the assessment and collection of education tax and proceeded to discussing the tax and finally the offences and penalties of education tax.

5.0 SUMMARY

You should recall that education tax is 20% of assessable profit payable by all companies whether these subject to company income tax or those subject to petroleum profit tax.

The assessment and collection of education tax is the responsibility of the Federal Board of Inland Revenue.

6.0 TUTOR MARKED ASSIGNMENT

1. Explain the assessment and collection of education tax.
2. Describe the offences and penalties of education tax.

7.0 REFERENCES / FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagod, JAA Nigeria Limited, 4th Edition.

UNIT 17 PETROLEUM PROFIT TAX

CONTENT

1.0 INTRODUCTION

The oil industries have achieved great prominence in the Nigerian economic environment since early seventies. The Government has attached importance to oil exploration and production such that the taxation of profits of companies engaging in such operations are taxable under a tax law known as Petroleum Profits Tax Act (PPTA), different from the Companies Income Tax Act.

Petroleum operation as defined in the PPTA essentially involves petroleum exploration, development, production and sale of crude oil. Oil companies that only market petroleum products including companies engaged in refining of crude oil such as petrol do not fall into the category of companies engaging in petroleum operations and they are therefore taxable under CITA. Where a company is involved in both petroleum operation and marketing of petroleum product, the trading results from the petroleum operations would be subject to Petroleum Profits Tax while the results from the marketing activities will be taxed under the Companies Income Tax Act. You should not that all reference to companies in this unit relates to companies engaged in petroleum operation except where otherwise stated.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. Describe the administration of PPTA
2. List allowable deductions according to section 10 of PPTA
3. List disallowable expenditure according to section 11 of PPTA
4. Explain qualifying expenditure, petroleum investment allowance, annual allowance, balancing adjustment and residence of qualifying expenditure
5. Explain and calculate various profits resulting in chargeable profits and petroleum profit tax payable.

3.0 MAIN CONTENT

3.1 Administration of Administration of Petroleum Profit Tax Act (PPTA)

The administration of PPTA is under the care and management of the Federal Board of Inland Revenue. The Board may do all acts as may be deemed necessary and expedient for the assessment and collection of the tax and shall account for all amounts so collected in a manner to be prescribed to the Federal Minister of Finance.

Whenever the Board shall consider it necessary with respect to any tax due, it may acquire, hold and dispose of any tax or of any judgment debt due in respect of any tax and shall account for any such property and the proceeds of sale thereof in a manner to be prescribed by the Minister. The Board may sue and send be sued in its official name.

In the exercise of the powers and duties conferred upon it, the Board shall be subject to the authority, direction and control of the Minister of Finance. Any written direction, order or instruction given by the Minister after consultation with the chairman of the Board shall be carried out by the Board.

However, the Minister shall not give any such direction in respect of any particular company which would have the effect of requiring the Board to increase or decrease any assessment made or to be imposed upon or any relief given tax, penalty or judgment debt due by such company or which would have the effect of altering the normal course of any proceeds, whether civil or criminal, relating either to the recovery of any tax or penalty or to any offence relating to the tax. Any Act, matter or thing done by or with the authority of the Board in pursuance of the provisions of PPTA shall not be subject to challenge on the ground that such was not or was not period to be in accordance with any direction, order or instruction given by the Minister

Self Assessment Exercise 17.1

The administration of PPTA is under the care and management of the Federal Board of Inland Revenue. Discuss.

3.2 Allowable Deductions

All outgoings and expenses wholly, exclusively and necessarily incurred, whether within or outside Nigeria, for the purpose of petroleum operations shall be deductible in computing the adjusted profit for any accounting period.

The following are specifically listed as allowable deduction in section 10 of the PPTA Act:

1. Rents in respect of land or buildings occupied under an oil prospecting license or an oil mining lease for disturbance of surface rights or for any other like disturbance.

2. All non-productive rents

3. All royalties in respect of natural gas sold and actually delivered to the Nigerian National Petroleum Corporation (NNPC), or sold to any other buyer or customers or disposed of in any other commercial manner

4. All royalties, the liability for which was incurred by the company during that period in respect of crude oil or of Casinghead Petroleum Spirit won in Nigeria.

5. All sums by way of customs or excise duty or other like charges levied in respect of machineries, equipment and other goods used in the company's petroleum operations.

6. Interest on money borrowed where the Board is satisfied that the interest was payable on capital employed in carrying on petroleum operations

7. All sums incurred by way of interest on any inter-company loans obtained under terms prevailing in the open market, that is, the London Inter-Bank offer rate.

8. Repairs and or renewals of premises, plant, machinery, implements, utensils, fixtures or articles employed for the purpose of carrying on petroleum operations.

9. Bad and doubtful debts proved to the satisfaction of the Board to have become bad or doubtful during the accounting period

10. Any other expenditure, including tangible costs directly incurred in connect with drilling and appraisal of development well, but excluding an expenditure which is qualifying expenditure for capital allowances purposes.

11. Contribution to approved pension, provident, or other social, scheme or fund.

12. All sums by way of duty, customs and excise duties, stump duties, education tax, tax (other than PPT) or any other rate, fee or other like charges.

13. Such other deductions as may be presented by any rule made under the PPTA Act.

Self Assessment Exercise 17.2

List eight allowable deductions according to section 10 of the PPTA.

3.3 Disallowable expenditure

Section 11 of the PPTA states the items that are specifically disallowed from being deducted in arriving at the adjusted profit of an accounting period. They are:

1. Any disbursements or expenses not wholly and exclusively laid out or expended, or not wholly or exclusively incurred for petroleum operation purposes.

2. Any capital withdrawn or any sum employed or intended to be employed as capital.

3. Any capital employed in improvements as distinct from repairs.

4. Sums recoverable under an insurance or contract of indemnity

5. Rent of or cost of repairs to any premises or part of premises not incurred for petroleum operations.

6. Amounts incurred as income tax, profit tax or other similar tax whether charged within Nigeria or elsewhere.

7. Depreciation of any kind

8. Payment to unapproved provident, savings, widows and orphans or other social, scheme or fund.

9. Any custom duty on goods (including articles or any other thing) imported by the company
   a. For resale or for personal consumption of employees of the company or
   b. Where goods of the same quality to those so imported are produced in Nigeria and are available, at the time the imported goods were ordered by the company for sale to the public at less or equivalent to the cost to the company of the imported goods

10. Expenditure for the purchase of information relating to the existence and extent of petroleum deposits.

Self Assessment Exercise 17.3

List six disallowable expenditures according to section 11 of the PPTA.

3.4 Capital Allowances

Qualifying Expenditure:

Qualifying expenditure means capital expenditure incurred in an accounting period which is:

a. Incurred on plant, machinery or fixtures – qualifying plant expenditure

b. Incurred on pipelines and storage tanks – qualifying pipeline and storage expenditure

c. Incurred on the construction of buildings, structure or works of a permanent nature-qualifying building expenditure

d. Incurred I qualifying drilling expenditure such as
   1. The acquisition or rights in or over, petroleum deposit
   2. Searching for or discovering and testing petroleum deposits, or winning access thereto or
   3. The construction of any works or buildings which are likely to be of little or no value when the petroleum operations for which they were constructed ceased to be carried on.

Allowances

The allowances are granted at varying rates on the cost of the assets. Before an allowance can be granted, the following condition must be met.

1. The qualifying expenditure must be wholly, necessarily and exclusively for the purpose of petroleum operations carried on by the company.

2. There must be ownership and usage at the end of the particular accounting period. An asset is deemed to be in use during a period of temporary disuse.

Petroleum Investment Allowance

This is an allowance similar to an initial allowance. It is granted in the accounting period in which the expenditure is incurred. It is granted only once for any particular asset. The amount arrived at is to be added to the annual allowance computed under the PPTA and shall subject to the same rules.

Capital allowances rate in respect of petroleum investment allowance are:

Qualifying expenditure in respect of
- On share operation
  5%
- Operation in territorial waters and continental shelf areas up to and including 100 meters of water depth. 10%
- Operations in territorial waters and continental shelf areas in water depth of between 100 to 200 meters 15%
- Operation in territorial waters and continental shelf areas beyond 200 meter water depth
  20%

Annual Allowance

This is granted annually on cost until the residence of the item is 1% of the original cost. The design is that the amount of any qualifying expenditure is amortized over a period of five years in equal amount except the fifth year when 1% of the amount is retained. The rate is there 20% of the cost per annum for each of the first four years and 19% for the fifth year. The 1% of the cost of the asset must be retained in the books until the disposal of the item.

Any asset in respect of which capital allowances have been granted can only be disposed of on the authority of a certificate of disposal issued by the Minister or any person authorized by him.

Balancing Adjustment

The calculation of balancing allowance or charge follows normal taxation principle. The residence of qualifying expenditure is compared with the disposal proceeds in arriving at the balancing allowance or charge.

However, in PPT, balancing charge is to be treated as other income to form part of the profits of the company. Balancing allowance or charge shall also be made only if immediately prior to the disposal, the asset was in use for the purposes of petroleum operations for which the expenditure was incurred.

Residence of Qualifying Expenditure

The residence of qualifying expenditure, in respect of any asset, at any date, is the total qualifying expenditure incurred less the total of annual allowances granted to that date in respect of the asset.

3.5 Ascertainment of Chargeable Profit

The basis period for any year of assessment is on current year basis. This is a major departure from the preceding year rule that is applicable in taxation of individuals (under PITD) and companies not engaging in petroleum operations (under CITA).

The profits of an accounting period of a company are computed as the aggregate of the following:

a. The proceeds of sale of all chargeable oil sold
b. The value of chargeable oil disposed of
c. The value of all chargeable natural gas
d. All income incidental to and arising from one or more of its petroleum operations.

The adjusted profit of an accounting period shall be the profits of that period after the deductions of allowable expenditure and any adjustments necessary to exclude the profit or loss attributable to transportation operations which is assessable under CITA.

The assessable profit shall be the adjusted profit of the period after adjusting for the effect of any loss relief available to the company.

The chargeable profits shall be the assessable profits less capital allowances. For this purpose the amount of capital allowances to be deducted is to be restricted to the lower of;

a. The amount computed or

b. A sum equal to eight – five percent of the assessable profits of the accounting period less one hundred and seventy percent of the total amount of the deductions allowed as petroleum investment allowance computed under the second schedule for that period.

From the foregoing, the relationship between the terms profits; adjusted profit, assessable profit and chargeable profit can be stated as follows:

Profit for the period
Deduct: allowable expenditure

Adjusted profit
Less loss relief
Assessable profit
Deduct capital allowances
Chargeable profit

Example

Union Petroleum Company Limited has the following particulars to present for the year ended 31st December, 2008.

	₦ '000
Sale of crude oil – export	820, 500
Sale of natural gas	60, 000
Other incidental income	5, 800
The expenses incurred during the period are as follows	
Production	170, 000
Administration	196, 000
Intangible drilling cost	45, 000
Non – productive rentals	14, 500
Royalties on export	4, 500
Royalties on local sales	1, 800
Custom duties on plant and machinery	21, 000

The following additional information is provided:

1. Investment tax credit has been agreed at ₦10, 900, 00
2. Depreciation included in production expenses amounted to ₦25, 000, 000
3. Capital allowances agreed with the Federal Board of Inland Revenue is ₦45, 000, 000
4. Memorandum of understanding (M.O.U) credit is ₦15, 200, 000

You are required to compute the chargeable profit for the relevant accounting period

Solution

Union Petroleum Company Limited
Computation for chargeable profit 2008

	₦ '000	₦ '000
Profit of the accounting period		
Export sale of crude oil		820, 500
Sale of natural gas		60, 000
Other incidental income		5, 000
		886, 300
Less allowable expenditure		
Production	170, 000, 000	
Less depreciation	25, 000,000	145, 000
Administration		196, 000
Intangible drilling cost		45, 000
Non-productive rental		14, 500

Royalties on export	4, 500	
Royalties on local sales	1, 800	
Custom duties on plant and machinery	21, 000	
Education tax (2/102 x 458, 500)	8, 990	436,790
Assessable profit		449, 510
Less Capital allowances		
As agreed with FBIR	45, 000	
Maximum is		
85% of 449, 510, 000	382, 084	
Less 170% 0t 10, 900, 000	18, 532	
	363, 554	
Capital allowances claims		45, 000
Chargeable profit		404, 510

You should note that education tax is 2% of assessable profit. Since education tax is part of allowable expenses, if has to be derived because before assessable profit is gotten, the allowable expenses must have been deducted from the profit of the accounting period.

To get education tax, apply two divided by one hundred and two percent to the difference between profit of the accounting period and the sum of allowable expenses excluding education tax.

i.e. 2/102 x 458, 500, 000

To check whether that is correct

$$\frac{2 \times 449,510,000}{100} = ₦8,990,200$$

You should also note that after getting chargeable profit, you can well determine the chargeable tax and the petroleum profit tax payable. The chargeable tax is derived by taking 85% of the assessable profit less tax off sets (investment tax credit) according to section 20 of PPTA as in the 1999 amendment. The petroleum profit tax payable is derived by (M.O.U) credit from the chargeable tax. The Memorandum of Understanding as it applies to petroleum profits tax computation refers to a tax credit allowed to petroleum producing companies which reduces their petroleum profits tax liability. M.O.U. is to encourage the oil producing companies to invest more in petroleum oil industry.

Therefore, using the example above reaching a chargeable profit of ₦40, 510, 000

	₦
Assessable tax at 85% thereon	343, 833, 5000
Less section 20 Tax offsets	
Investment tax credit	10, 900, 000
Chargeable Tax	332, 933, 500
Less M.O.U credit	15, 200, 000
Petroleum profit tax payable	317, 733, 500

Self Assessment Exercise 17.4

Strafford Petroleum Company Limited has presented the following particulars for the year ended 31st December 2000

	₦ '000
Sale of crude oil – export	620, 000
Sale of natural gas	52, 000
Other incidental income	3, 400
Periods are as follows	
Production	160, 000
Administration	180, 000
Intangible drilling cost	29, 000
Non – productive rentals	12, 100
Royalties on export	4, 200
Royalties on local sales	1, 500
Custom duties on plant	16, 400

The following additional information is provided:

1. Memorandum of Understanding (M.O.U.) credit is ₦14, 300, 000
2. Investment tax credit has been agreed at ₦12, 800, 000
3. Depreciation included in production expenses amounted to ₦15, 400, 00
4. Capital allowances agreed with the Federal Board of Inland Revenue is ₦36, 000, 000

You are required to compute the chargeable profit, chargeable tax and petroleum profit tax payable for the relevant accounting period.

4.0 CONCLUSION

In this unit, we discussed petroleum profit tax. We started by discussing the administration of PPTA and proceeded to those expenses that are allowable and not allowable. We also discussed capital allowances and finally ascertainment of chargeable profit.

5.0 SUMMARY

You should recall that petroleum operation as defined in the PPTA essentially involves petroleum exploration, development, production and sale of crude oil.

The administration of PPTA is under the care and management of the Federal Board of Inland Revenue.

All outgoing and expenses wholly, exclusively and necessarily incurred, whether within or outside Nigeria, for the purpose of petroleum operations shall be deductible in computing the adjusted profit for any accounting period.

The basis period for any year of assessment is on current year basis.

The petroleum profit tax payable is derived by deducting M.O.U. credit from chargeable tax. Chargeable tax is derived by deducting tax offsets from 85% of chargeable profit. Chargeable profit is derived by deduction capital allowances claim from assessable profit. Assessable profit is derived by deduction allowable expenditure from the profit of the accounting period.

6.0 TUTOR MARKED ASSIGNMENT

1. Explain the following terms:
   a. Qualifying expenditure
   b. Petroleum investment allowance
   c. Annual allowance
   d. Balancing adjustment

2. Criscrox Petroleum Company Limited has the following details for the year ended 31st December 2003.

	₦ '000
Sale of crude oil – export	720, 000
Sale of natural gas	45, 000
Other income	6, 000
The expenses incurred during the period are as follows	
Production	182, 000
Administration	152, 000
Intangible drilling cost	36, 000
Non-productive rentals	12, 200
Royalties on export	4, 200
Royalties on local sales	2, 000
Customs duties on plant	20,000,000

The following additional information is provided:

1. Memorandum of Understanding (M.O.U.) credit is ₦14, 000, 000
2. Investment tax credit has been agreed at ₦9, 000, 000
3. Depreciation included in production expenses amounted to ₦16, 800, 000
4. Capital allowance agreed with the Federal Board of Inland Revenue is ₦29,000,000.

You are required to compute the petroleum profit tax payable for the relevant accounting period.

7.0 REFERENCES / FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola J.A. (2000) Companies Taxation In Nigerian, Lagos, J A A Nigeria Limited, 3rd edition.

UNIT 18 VALUE ADDED TAX

CONTENT

1.0 INTRODUCTION

Value added tax is a consumption tax levied on the increase in the in value of goods and services in the course if their production or supply. The incidence of value added tax is on the final consumer of the goods or services.

Value added tax replaced the sales tax which had been in existence since 1986. Value added tax was introduced in Nigeria on 1st December, 1993, its effective take off date however, was 1st January, 1994.The value added tax presently application in Nigeria is at a flat rate of 5% levied on all vat able goods and services.

2.0 OBJECTIVES

After studying this unit, you should be able to:

1. State the reason for the replacement of sales tax with value added tax
2. Describe the administration of VAT
3. Describe the operation of VAT in Nigeria
4. State goods and services exempted from tax

3.0 MAIN CONTENT

3.1 Reason for the replacement of sales tax with value added tax

The following are the main reasons for the replacement of sales tax with value added tax:

1. The sales tax had a very narrow base as it covered only nine categories of goods. It negated the basic principle of consumption tax, which should cut across all consumable goods and services.

2. The sales tax concentrated on locally manufactured goods only, thus placing these locally manufactured goods at a disadvantage in relation to foreign imported goods. The value added tax on the other hand covers both locally manufactured goods as well as foreign goods.

3. The value added tax is based on the general consumption pattern of the populace. Thus, it is expected to yield huge revenue to the government.

Self Assessment Exercise 18.1

State the main reason for the replacement of sales tax with value added tax.

3.2 Administration of Vat

The value added tax scheme is administered by the Federal Inland Service (FIRS) through its VAT Directorate. There is a network of zonal and local VAT office all over the country. The VAT Directorate works in close co operation with the Nigeria Customs Services and the state internal revenue services suppliers of goods and Service under the VAT scheme who may disagree with the assessment of a VAT office may appeal to the local VAT office. If still not Satisfied they can appeal further to the VAT zonal office and from there to the VAT Directorate at Abuja. If still not Satisfied with these administrative review panels, they could still appeal further to the federal high court.

Self Assessment Exercise 18.2

Describe the administration of VAT in Nigeria.

3.3 Operation of VAT in Nigeria

All business organizations that are registered with the Federal Board if Inland Revenue (VAT DIRECTORATE) for VAT purpose are classified as registered persons. Such registration is carried out not later than six months from the date of commencement of the VAT decree whichever is earlier. Each registered person is issued a registration certificate which is displaced in the principal place of business.

The registered person also referred to as a VAT able person will pay 5% VAT on all goods and Services purchased by the business. The tax paid is known as input tax. On selling such goods and services, The registered person will charge 5% VAT , which the registered person includes in the selling prices of such goods and Services is known as output tax where the output tax exceeds the input tax, the difference is known as net VAT payable, which should be paid to the federal board if inland, if the input tax exceed the output tax, the difference will be refunded to the registered person is a claim is put up and it is accepted as valid by the federal board of inland revenue.

Every VATable person is expected to make returns including remittance of net VAT payable to the local VAT office on or before the end of the month next following that in which the supplies were made.

A VATable person must produce a tax invoice before any claim for a credit for input tax would be entertained. Such claim would be subjected to verification by VAT auditors.

If the refund claim is established, the VAT refund could be claim in either through credit, that is, the excess of input tax over the out put tax is set off against any output tax in subsequent month or through cash, that is, the excess of input tax over output is refunded by cash.

Self Assessment Exercise 18.3

Describe the operation of VAT in Nigeria.

3.4 Good and Services Exempted From VAT

The following are goods exempted from VAT:

1. All medical and pharmaceutical products
2. Basic Food items
3. Books and Educational Materials
4. Newspapers and magazines
5. Baby products
6. Commercial Vehicles and their spare parts
7. Agriculture Equipment and products and Veterinary medicine, Farming machinery and Farming Transportation Equipment

The following are Services exempted from VAT:

1. Medical services
2. Services by community banks, people's bank and mortgage institutions
3. Plays and performances conducted by educational institution as part of learning.

Self Assessment Exercise 18.4

List of goods and services exempted from VAT.

4.0 CONCLUSION

In this unit, we discussed value added tax. We Started by listing reasons why value-added tax replaced sales tax and proceeded to the administration of VAT, operation of VAT in Nigeria and Finally listed goods and services that are exempted from VAT.

5.0 SUMMARY

You should recall that value added tax is a consumption tax levied on the increase in value of goods and services in the course of their production or supply. The incidence of VAT is on the final consumer of the goods or services.

The value added tax presently applicable in Nigeria is at a flat rate of 5% levied on all Vatable added and services.

The value added tax scheme is administered by the federal Inland Revenue service FIRS) through its VAT Directorate.

6.0 TUTOR MARKED ASSIGNMENT

1. State the reason why sales tax was replaced by value added tax.
2. Describe the operation of VAT in Nigeria.

7.0 REFERENCES / FURTHER READING

Anyaduba, J. O. (1999) Personal Income Taxation in Nigeria, Benin City, United City Press

Ariwodola, J. A. (2001) Personal Taxation in Nigeria Lagod, JAA Nigeria Limited, 4th Edition.