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INFORMATION CIRCULAR

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**Subject: TAXATION OF COMPANIES ENGAGED IN SHIPPING, AIR
TRANSPORT AND CABLE UNDERTAKINGS**

This circular is issued for the information and guidance of the general public, taxpayers and tax practitioners in line with the provisions of the relevant tax laws. The circular replaces FIRS Information Circular No. 2021/14 of 3rd June 2021.

1.0 Introduction

The Companies Income Tax Act (CITA) Cap. C21, LFN 2004 (as amended), makes provisions for the taxation of companies engaged in shipping or air transport in international traffic, as well as cable undertakings. Sections 14 and 15 of CITA specifically provide for taxation of the income of foreign companies operating in these industries. Nigerian companies engaged in the business of cable undertakings or international carriage of passengers, mails, livestock or goods by ship or air are not taxable under the provisions of these sections.

This Circular is issued by the Federal Inland Revenue Service ("the Service") to provide guidance on the taxation of the relevant sectors.

2.0 Tax Rate

Section 9 of (CITA) provides that companies income tax shall, for each year of assessment, be payable at the rate specified in Section 40 of CITA upon the profits of any company accruing in, derived from, brought into, or received in Nigeria.

Section 40(1) (CITA) provides that tax shall be charged at 20% and 30% of Total Profits for **medium companies** (companies having turnover of more than ₦25million but below ₦100million) and **large companies** (companies having more than ₦100million turnover) respectively.

Total Profits are determined as provided by the relevant sections (including S.14) of CITA.

3.0 Basis for Ascertaining Assessable and Total Profits

3.1 Nigerian Companies

Nigerian Companies engaged in Shipping or Air Transport business, or cable or wireless transmission undertakings, are chargeable to tax on their worldwide income in line with Section 13(1) of CITA. As such, interpretations and explanations provided in this circular are not applicable to Nigerian companies.

3.2 Foreign Companies (Non-Resident Companies)

3.2.1 Domestic Tax Law Situation for Foreign Companies Operating Domestic Transport

Profits of a non-resident company from the operation of a business of transport by ships or aircrafts strictly within the borders of Nigeria (departure and arrival is within Nigeria) would have the same treatment as a Nigerian Company engaged in shipping or air transport business.

The profits so derived from Nigeria may fall into two categories; freight income or non-freight income.

- i. Freight income are those earned from the carriage of passengers, mails, livestock or goods shipped or loaded into an aircraft between places in Nigeria.
- ii. Non-Freight income are those earned from other business activities including but not limited to commission, demurrage, container clearing fees, container damage fees, rental of ship or aircraft, stevedoring, etc.

In both cases the income is chargeable to tax in Nigeria without segmenting the accounts along income types.

3.2.2 Domestic Tax Law Situation for Profits from International Transport

Section 14(1) of CITA provides that *"Where a company other than a Nigerian company carries on the business of transport by sea or air, and any ship or aircraft owned or chartered by it calls at any port or airport in Nigeria, its profits or loss to be deemed to be derived from Nigeria shall be the full profits or loss arising from the carriage of passengers, mails, livestock or goods shipped, or loaded into an aircraft, in Nigeria.*

Provided that this subsection shall not apply to passengers, mails, livestock or goods which are brought to Nigeria solely for trans-shipment or for transfer from one aircraft to another or in either direction between an aircraft and a ship".

Section 14 of CITA contain specific rules dealing with the taxation of profits of non-Nigerian companies arising from the operation of business of transport by ships or aircrafts in Nigeria. The summary of the rules are:

- a. Profits of foreign airlines or shipping companies derived from Nigeria are taxable in Nigeria.
- b. The profits so derived from Nigeria may fall into two categories, freight income or non-freight income:
 - i. Freight income are those earned from the carriage of passengers, mails, livestock or goods shipped or loaded into an aircraft in Nigeria.
 - ii. Non-Freight income are those earned from other business activities including but not limited to commission, demurrage, container clearing fees, container damage fees, stevedoring, etc.
- c. Only profits arising from the carriage of passengers, mails, livestock or goods shipped, or loaded into a ship or an aircraft in Nigeria (freight income) is liable to tax under section 14 of CITA.
- d. Profits arising from carriage of passengers, mails, livestock or goods, which are brought to Nigeria solely for trans-shipment are not chargeable to tax in Nigeria.
- e. The tax base for the taxation of freight income of foreign airline or shipping companies is the "**Profits**" computed based on the provisions of Section 14 of CITA.
- f. By the provisions of Section 14(1), the profits chargeable to tax is the full profits arising from the carriage of passengers, mails, livestock or goods shipped or loaded into ship or aircraft in Nigeria. The assessable profits are determined based on the financial statements submitted with respect to Nigerian operations only.
- g. Where a foreign airline or shipping company is a resident of a country which computes and assesses tax on a basis not materially different from that of Nigeria, the taxable profit shall be determined under the provision of section 14(2) as follows:
 - i. "**Total Profits**" shall be ascertained by deducting **depreciation allowance** from the **assessable profits**.
 - ii. "**Assessable Profits**" is computed by applying the "**profit ratio**" obtained from the global account of the company to total income receivable from the carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria.

- iii. **“Depreciation allowance”** is computed by applying the **“depreciation ratio”** obtained from the global account of the company to the total income receivable from the carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria.

Note:

- **“profit ratio”** is the ratio of the profit or loss (before depreciation allowances of the company) of an accounting period to the **total sum receivable globally** by the company in respect of carriage of passengers, mails, livestock or goods.
 - **“depreciation ratio”** is the ratio of the total depreciation of an accounting period to the **total sum receivable globally** by the company in respect of carriage of passengers, mails, livestock or goods.
- h. The provisions of subsection 2 are applicable only where:
- (i) the Service is satisfied that the tax authority of the country (where the foreign company is resident for tax purposes) computes and assesses tax on a basis that is not materially different from that prescribed under CITA; and
 - (ii) the non-resident company produces a certificate from that authority, certifying the ratio of profit or loss and the ratio of allowances (i.e. the **“profit ratio”** and **“depreciation ratio”**)
- i. Where the provisions of Section 14(2) of CITA cannot be satisfactorily applied, profit assessable to tax shall be computed based on provision of section 14(3) of CITA.
- Based on that subsection, the Assessable profit of the foreign shipping or airline company shall be computed as a fair percentage of the total sum receivable from the carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria.
- In line with government policy, the Service has consistently applied **20%** of the total sum receivable as the total profits in such cases.
- j. Notwithstanding whichever of the three approaches discussed in the foregoing paragraphs is used in determining the total profit of a foreign shipping or airline company, the tax payable shall not be less than **2%** of the total sum receivable from the carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria (Section 14(4) of CITA).
- Where the tax computed is less than **2%** of the total revenue receivable from the carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria, the tax payable shall be the minimum tax, which is determined as **2%** of the total revenue receivable from the carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria.

Note: the total sum receivable from the carriage of passengers, mails, livestock's or goods shipped or loaded from Nigeria is the total amount paid in respect of the carriage, irrespective of any breakdown made on the ticket or invoice and no amount is deductible before applying the 2%.

Illustration 1

The global income statement of NAM Airways Ltd., a foreign airline which operates into Nigeria for the year ended 31st December 2017 shows the following:

| | \$'000 | \$'000 |
|--|-----------|--------------------|
| Income from passengers, cargo and mails: | | |
| Outside Nigerian Sales | | 3,100,000 |
| Nigerian sales | | <u>100,000</u> |
| Global Transportation Revenue | | 3,200,000 |
| Transportation Expenses: | | |
| Salaries and other expenses | 2,300,000 | |
| Depreciation | 320,000 | |
| Other disallowable expenses | 180,000 | <u>(2,800,000)</u> |
| Net Transportation Profit | | <u>400,000</u> |
| Other Income: | | |
| Income from Properties (net) | 25,000 | |
| Income from Maintenance (net) | 50,000 | |
| Income from duty-free shops (net) | 50,000 | |
| Income from catering (net) | 75,000 | <u>200,000</u> |
| Net profit | | <u>600,000</u> |

NAM Airways has two ground staff in Nigeria and 5% of the 'other income' is attributable to the operation of the Airline in Nigeria.

Treatment:

A. To determine the Nigerian tax payable on freight income

- i. calculate the profit on the transportation business:

| | |
|--|----------------|
| | \$'000 |
| Net transportation Profit as per account | 400,000 |
| Add Depreciation | 320,000 |
| Other disallowed expenses | <u>180,000</u> |
| Global Transportation Assessable Profits | <u>900,000</u> |

- ii. Compute relevant statutory ratios:

(a) Profit ratio:

$$\frac{900,000}{3,200,000} \times 100\% = 28\%$$

$$(b) \text{ Depreciation ratio: } \frac{320,000}{3,200,000} \times 100\% = 10\%$$

iii Compute the tax payable on the freight income:

| | |
|---|-----------------------|
| Nigerian freight income as above | <u>100,000</u> |
| Total Assessable Profits 28% of \$100,000 | 28,000 |
| Less: Depreciation Allowance 10% of \$100,000 | <u>10,000</u> |
| Total Profit | <u>18,000</u> |
| Tax at 30% | <u>5,400</u> |

iv Minimum tax (2% of the Nigerian sale 100,000 X 2%) 2,000

Therefore, Tax Payable on freight income **\$5,400**

Note: that the depreciation allowance is in lieu of capital allowance granted under the second schedule to CITA.

B. To determine the Nigerian tax payable on non-freight income

| | |
|---|---------------------|
| | \$'000 |
| Total or global non-freight income (net) | 200,000 |
| Amount attributable to Nigeria (5% X 200,000) = | <u>10,000</u> |
| Tax @ 30% (30% X 10,000) = | <u>3,000</u> |

C. To determine the Total Tax Liability in Nigeria:

| | |
|---------------------------------------|---------------------|
| Tax payable on freight income | 5,400 |
| Tax payable on non-freight income | <u>3,000</u> |
| Total Tax Liability in Nigeria | <u>8,400</u> |

3.2.3 Tax Treaty Situation

The Article on Shipping and Air Transport in the Double Taxation Agreements (DTAs) between Nigeria and other countries deals with the sharing of taxing right between Nigeria and the treaty partners. The Article moderates the provision of Section 14 of CITA as regards sum receivable from the international carriage of passengers, mails, livestock or goods shipped or loaded in Nigeria. The scope of the Article covers only **international traffic** (that is, the place of departure is Nigeria while the place of arrival is outside Nigeria). Consequently, the Article does not deal with profits derived by a non-resident company from domestic routes (where place of departure and arrival are in Nigeria). The explanations in this paragraph are applicable regardless of whether the vessel or aircraft is owned, leased or otherwise at the disposal of the Non-resident company.

There are two broad categories of Nigerian DTAs as regards the treatment of companies engaged in shipping or air transport. These are DTAs that grant unconditional tax exemption to shipping or airlines of tax treaty partners and those that provide only conditional (based on reciprocity) exemption.

With respect to tax treaties that grant unconditional tax exemption, the companies engaged in shipping or air transport are exempt from Nigerian income tax if they are residents (as defined by the DTA) of the treaty partner.

Illustration 2:

XYZ Airlines Ltd., a foreign company resident in Utopia a treaty partner of Nigeria, carries passengers from Abuja Nigeria to Utopia with three flights per week.

Treatment:

This trip would be regarded as falling within the definition of international traffic.

Illustration 3:

XYZ Airlines Ltd., a foreign company resident in Utopia, a treaty partner of Nigeria, carries passengers from Abuja Nigeria to Utopia with three flights per week. XYZ Airlines as part of the same voyage to Utopia, first flies between Abuja to Lagos to pick up passengers and then continues to Utopia.

Treatment:

The first and second legs of that trip, Abuja to Lagos and Lagos to Utopia will both be part of a voyage regarded as falling within the definition of international traffic.

Illustration 4:

XYZ Airlines Ltd., a foreign company resident in Utopia a treaty partner of Nigeria, is a new airline starting operations in Nigeria. XYZ Airlines carries passengers from Abuja to Lagos Nigeria only with five flights per week.

Treatment:

This trip would not be regarded as falling within the definition of international traffic.

With respect to DTAs that grant conditional tax exemption, treaty benefits are granted in either of the following ways:

a) Where there is Reciprocity:

Reciprocity clause, in the Article dealing with shipping and air transport, means that ships operated in international traffic by Nigerian companies call at the seaports of a treaty partner and ships operated in international traffic by companies of the treaty partner also call at Nigerian seaports or aircrafts operated in international traffic by Nigerian companies call at the airports of a treaty partner and aircrafts operated in international traffic by companies of the treaty partner also call at Nigerian airports in a given year of assessment.

Therefore, reciprocity applies only where profits as meant in the Article, are derived by companies or other persons of both countries from the operation of ships or aircraft in international traffic to or from each other.

As such, "Reciprocity" in international traffic will occur only where a company of Nigeria derives profits from the operation of ships in international traffic to a treaty partner, and a company of a treaty partner similarly derives profits from the operation of ships or a company of Nigeria derives profits from the operation of aircraft in international traffic to a treaty partner, and a company of a treaty partner similarly derives profits from the operation of aircraft in international traffic to Nigeria.

In such a case, the foreign company will not pay tax in Nigeria and the Nigerian company will not pay tax in the other country. The profits of the companies will only be taxable in their respective home countries.

b) Where there is no Reciprocity:

This is where companies of a Nigeria's tax treaty partner operate ships or aircrafts in international traffic calling at Nigerian ports in a given year of assessment, without any corresponding operation of ships or aircrafts of Nigerian companies in international traffic calling at the ports of that treaty partner.

Any other income accruing to the government of Nigeria or any instrumentality thereof, by way of a commercial or other agreement that does not deal with tax issues, in particular avoidance of double taxation, will not be considered as profits derived from the operation of ships or aircrafts in international traffic.

Consequently, the foreign companies of the treaty partner are assessable to tax in Nigeria in respect of income arising from such operations.

However, Nigerian tax shall be at the rate specified in the respective DTAs.

Note:

- i. The treatment agreed in the DTAs (full exemption of the foreign company from income tax or taxation at treaty rate) is limited to the activities specified in the tax treaty. Profits from all other activities of the foreign company (not listed in the tax treaty) shall fall under the Article on Business Profits in the Agreement and be taxable in Nigeria as provided by the relevant domestic tax law.
- ii. For the purposes of reciprocity, ships and aircrafts are not interchangeable, i.e. ship for ship and aircraft for aircraft.

4.0 Tax Returns

Section 55 of CITA provides that every company (including companies granted exemption from incorporation in Nigeria and those not liable to tax under CITA) shall file self-assessment return.

Based on the provisions of Section 55 of CITA, a non-resident company involved in the carriage of passengers, mails, livestock or goods loaded into ships or aircrafts in Nigeria is required to file annual tax returns with the Service.

4.1 Contents of Tax Returns (Based on Section 55(1A))

By Section 14(1) of CITA, the profits of a non-resident company from the operation of ships or aircrafts calling at Nigerian ports are the full profits arising from the carriage of passengers, mails, livestock or goods shipped, or loaded into an aircraft, in Nigeria. The contents of the tax returns of such a non-resident company as provided in Section 55(1A) of CITA (as amended) are:

- (a) full audited financial statements of the non-resident company and the financial statement of the Nigerian operations, attested by an independent qualified or certified accountant in Nigeria;
- (b) tax computation schedules based on the profits attributable to its Nigerian operations;
- (c) a true and correct statement, in writing, containing the amount of profits from each and every source in Nigeria; and
- (d) duly completed Companies Income Tax Self-Assessment forms

Note:

- i. "Full Audited Financial Statements" implies the global or consolidated account of the foreign entity.
- ii. Financial statement of the Nigerian operations should include necessary details required under the relevant domestic legislation.
- iii. Capital Allowances computation is limited to qualified capital expenditures incurred for Nigerian operations only.
- iv. Information contained in the financial statement of the Nigerian operations will form the basis for computing the assessable profits, capital allowances, total profits and tax due.
- v. Companies Income Tax self-assessment forms are available at <https://www.firs.gov.ng/TaxForms/FIRSTaxForms>.
- vi. The above returns should be accompanied with evidence of payment of the tax due.

4.2 Tax Computation Based on Section 14(2)

Section 14(2) of CITA provides simplification rules for the taxation of non-resident companies (operating ships or aircrafts to Nigeria) whose taxation authorities in their home-countries compute and assess tax on a basis not materially different from that prescribed by CITA. The content of tax computation of a non- resident company should include:

- a. Tax Computation – the tax computation should disclose the following details:
 - i. Global revenue (i.e. total revenue receivable worldwide from the carriage of passengers, mails, livestock or goods).
 - ii. The global net profit from the business of carriage of passengers, mails, livestock or goods.
 - iii. Tax adjustments carried out on the accounting net profit to arrive at the assessable profit of the business of carriage of passengers, mails, livestock or goods.
 - iv. The profit ratio of the business of carriage of passengers, mails, livestock or goods (i.e. the ratio of the assessable profits to global earnings (revenue) for the period).
 - v. The amount of global depreciation (of the business of carriage of passengers, mails, livestock or goods) for the period.

- vi. The depreciation ratio (i.e. the ratio of the annual global depreciation to global earnings (revenue) of the business of carriage of passengers, mails, livestock or goods for the period).
- vii. Earnings (revenue) of the company derived from the carriage of passengers, mails, livestock or goods shipped or loaded into aircrafts in Nigeria during the period.
- Vii Assessable profits of the company derived from Nigeria (i.e. revenue of the company from Nigeria specified in (vii) above multiplied by the adjusted profit ratio)
- viii. Capital allowance deducted (i.e. revenue of the company from Nigeria specified in (vii) above multiplied by depreciation ratio)
- ix. Full profits taxable in Nigeria (i.e. the Assessable profits of the company computed in (viii) above less Capital allowance computed in (ix) above)
- x. Tax Payable in Nigeria, which is the 'full profits' computed in (x) above multiplied by the tax rate as contained in Section 40 of CITA.
- xi. Computation of minimum tax.

b. Capital Allowances Computation – this should contain details of depreciation charged into the global account, the computation of depreciation ratio and capital allowances deductible in Nigeria (computed using the depreciation ratio).

4.3 Section 14(4A) - Contents of Tax Returns by Foreign Shipping and Airline Companies

A foreign company engaged in shipping or air transport business in Nigeria who does not file a separate financial statement for its Nigerian operations in line with paragraph 4.1 above, is required to file with the Service a detailed gross revenue statement of its Nigerian operations, showing the full sums earned during the period.

The detailed gross revenue statement, should be supported with all the invoices issued to the relevant customers and shall be certified by one of the company's directors and its external auditor.

4.4 Section 14 (6) - Roles of Regulatory Agencies in Shipping and Airline Business in Nigeria

Section 14(6) mandates Regulatory Agencies in the shipping and airline business and other related sectors to ensure adherence and compliance to the following, as a pre-requisite for obtaining relevant approvals and permits, to operate or continue business in Nigeria.

- (a) Request companies taxable under the provisions of CITA Section 14(1) to provide evidence of filing of tax returns for the preceding year.
- (b) Request for Tax Clearance certificate (TCC), referencing income tax paid for the three (3) preceding years.

Note: A foreign airline or shipping company that newly commences operations in Nigeria shall register for tax and may approach the Service for the issuance of a TCC to meet the regulatory requirement in paragraph (b) above.

5.0 Advance Payment of Tax

In line with Sections 14(4) and 81 of CITA (as amended), foreign companies that carry on the business of shipping or air transportation in Nigeria are required to remit on a monthly basis, an advance payment of tax, computed as **2%** of the monthly revenue derived from Nigeria.

Note: The 2% remittance is not the final tax. As such, it does not preclude the foreign companies from complying with the provisions of Section 14(1) - (3) of CITA. The payment of the 2% of monthly revenue only enables the companies to fulfil the requirement for repatriation of ticket sales pending the conclusion of the tax matters for the relevant year of assessment.

6.0 Income from Leasing or Charter of Ships and Aircraft

One of the common features of the Shipping and Air Transport business is leasing of vessels, ships or aircraft. The lease may be on "time or voyage basis", or "demise or bare-boat basis" in the case of ships; and dry or wet lease in the case of aircraft.

- a. **A voyage or time charter:** This is an arrangement in which the charterer (or lessee) charters the ship (or part of it) for a particular voyage in which the route and ports have been pre-determined or for an agreed period of time of which they are free to sail to any port and transport any cargo. Voyage or time charter of ships is similar to wet lease or leasing arrangements of aircraft. Depending on the charter arrangement, the charterer or lessee may direct where the ship or aircraft will go but the owner of the ship retains possession of the ship, and maintenance of the vessel still falls under the purview of the

owner. It is the owner of the ship that remains responsible for the employment of the master and crew and responsible for the technical operation of the vessel.

The charterer or lessee pays hire (rental fee) to the owner of the vessel and may sometimes pay for the fuel the vessel consumes, port charges, demurrage, commissions etc. (especially for time charter) but does not retain ownership, while the owner will handle all maintenance-related costs. In a time charter the commercial control of the vessel is not handled by the owner, while in a voyage charter, both the technical and commercial control is retained by the owner. A voyage or time charter of ship or wet lease of aircraft mostly constitutes an operating lease.

- b. **Bareboat or demise charter:** Bareboat or demise charter arrangement has similar features as dry lease or leasing arrangement of an aircraft. In a dry lease or bare-boat or demise charter, the owner gives possession of the ship to the charterer and the charterer hires its own master, crew and ground staff. The charterer or lessee obtains possession and full operational control of the vessel along with the legal and financial responsibility for it. The charterer or lessee pays for all operating expenses, including fuel, crew, port expenses and insurance. A bareboat charter of ship or dry lease of aircraft is in effect a financing arrangement and mostly constitutes a finance lease.

6.1 Treatment of Income from Leasing or Charter of Ships and Aircraft under the Domestic Law

Under CITA, income from the lease or charter of ships or aircraft does not constitute income from shipping and air transport business (freight income) but is treated as non-freight income.

6.2 Treatment of Income from Leasing or Charter of Ships and Aircraft When There is Tax Treaty

6.2.1. Wet Lease, Time or Voyage Charter

The profits of a company, resident in the jurisdiction of a treaty partner with Nigeria, accruing from the charter or leasing of aircrafts or ships on time or voyage basis, or wet lease arrangement shall constitute profits from air and shipping transportation. Such profits will be treated in line with the Article on shipping and air transport, so far as such charter is used solely for international traffic. In this regard, the income of the non-resident company will be subject to tax on the basis of the following instances:

- a. Where the treaty does not allow for source State taxation:** the non-resident company will be taxable only in its home country.
- b. Where the treaty allows for source State taxation but there is reciprocity in international traffic in a year of assessment:** the foreign airline or shipping company will not be subject to tax in Nigeria in that year of assessment. In such a case, each country will tax its own airline or shipping company.
- c. Where the treaty allows for source State taxation and there is no reciprocity in international traffic in a year of assessment:** the tax payable by the non-resident in Nigeria shall be at the rate specified in the respective tax treaty. The applicable rate is contained in paragraph 4.2.1 of FIRS' Information Circular No:2021/05, 3rd June, 2021 on the Claim of Tax Treaties Benefits in Nigeria (which may be accessed on the FIRS website).

However, where the income is derived from only domestic routes within Nigeria, such profits cannot be considered profits derived from international traffic and would be treated as 'business profits' under Article 7 of the treaty. Consequently, the lease or rental income shall be assessed to tax under the relevant provision of the domestic tax law.

6.2.2. Dry Lease or Bareboat Basis

Profits of such companies derived from the charter or leasing an aircraft or ship on bareboat basis or dry lease arrangement shall not constitute income from air and shipping transportation (except the Agreement specifically provides otherwise). The profits are taxed as "business profits" under relevant article of the DTA. Consequently, the lease or rental income shall be assessed to tax under the relevant provision of the domestic tax law, including withholding tax and value added tax.

The lessee in Nigeria may claim capital allowance in respect of the asset.

Illustration 5:

ADK Airways is a foreign company resident in Fantasia that wet leases its aircrafts to Airlines in Nigeria. YBM Airlines, an incorporated company in Nigeria, wants to expand its air transport operations and has taken a wet lease of one aircraft from ADK Airways for a period of 5 years to increase its daily flights between Abuja and Lagos routes. YBM would be required to pay ADK at quarterly intervals based on agreed daily rates for the duration of the lease. YBM is also required to take on the insurance on passengers, baggage, cargo or mail, all operating costs in connection to the aircraft (or reimburse ADK for it if borne by ADK) which includes the fuel and lubricants, landing and parking fees, ground handling, carbon emission charges, passenger and crew in-flight catering etc., and pay a security deposit before the lease starts, by virtue of the terms of the agreement. YBM in addition will ensure that the

Aircraft is free and clear of all liens, charges and encumbrances that have arisen during the Wet Lease Period.

However, ADK will take care of crew expenses and any cost relating to loss or damage to the aircraft including replacement of the aircraft so far as it is not from gross negligence or wilful misconduct by YBM.

Treatment:

Both ADK and YBM are operating domestic air transport in Nigeria and profits derived by each company from their respective activities would be subject to tax in Nigeria. Withholding tax would be applicable on all payments to ADK by YBM in line with section 81 of CITA and the Withholding Tax Regulations S.I.10.

Illustration 6:

Fantasia is a treaty partner of Nigeria and one of its resident companies, ADK flies purely international routes between Nigeria and Fantasia. The treaty between Nigeria and Fantasia allows for source State taxation where there is no reciprocity. In its efforts to expand its operations to international routes between Nigeria and Fantasia, YBM Airlines, a Nigerian company entered into a wet lease agreement with ADK for a period of 5 years. All other facts and conditions stated in Illustration 5 above are assumed to be the same.

Treatment:

Both ADK and YBM derives income from international traffic. As such, the conditions for reciprocity under the tax treaties of Nigeria is met.

Consequently, each country will tax its airlines and the profits of ADK will not be taxable in Nigeria, although the treaty allows for source State taxation.

Illustration 7:

Fantasia is a treaty partner of Nigeria and one of its resident companies, ADK flies purely international routes between Nigeria and Fantasia. The treaty between Nigeria and Fantasia allows for source State taxation where there is no reciprocity. In its efforts to expand its domestic operations include routes between Abuja and Enugu, YBM Airlines, a Nigerian company entered into a wet lease agreement with ADK for a period of 5 years. All other facts and conditions stated in Illustration 5 above are assumed to be the same.

Treatment:

ADK derives income from international traffic while YBM does not. As such, the conditions for reciprocity under the tax treaties of Nigeria has not been met. Consequently, Nigeria will tax the profits of ADK at the rate specified in the relevant tax treaty, if the treaty allows for source State taxation. While YBM will be subject to tax on its income in accordance with paragraph 3.1 above.

7.0 Income from Employment Exercised Aboard a Ship or Aircraft

Income covered under this paragraph includes income from employment exercised aboard a ship or aircraft as part of the crew or in the course of usual operation of the ship or aircraft. Examples of such activities include disc jockeys, expedition leaders, hosts and hostesses, shore excursion managers, water sports instructors, fitness directors, medical staff, bartenders, information technology staff, casino staff, entertainers etc. exercised aboard a cruise ship.

7.1 Tax Treatment of Income from employment under the Domestic Law

7.1.1 Resident Individual

An individual who is a resident of Nigeria, whether master, pilot, crew or ground-staff is liable to tax in Nigeria on all income derived from both inside and outside Nigeria. Employment income, including compensations, bonuses, premiums and benefits, irrespective of where the income is earned or the employment is exercised and whether or not the income is brought into or received in Nigeria will be liable to tax in Nigeria. This is regardless of where the employer is tax resident.

7.1.2 Non-Resident Individual

A non-resident individual, whether master, pilot, or forming part of the crew or ground-staff is liable to tax on employment income derived from Nigeria, whether or not the remuneration is received in Nigeria, where:

- (a) the employment is exercised in Nigeria, the non-resident individual will be liable to tax on the employment income, irrespective of the number of days spent in Nigeria; or
- (b) the employment is not exercised in Nigeria, the non-resident individual will be liable to tax on the employment income, only if:
 - i. the individual has spent 183 days in Nigeria; or
 - ii. the employer is in Nigeria, or has a fixed base in Nigeria which bears the expense; or
 - iii. the employer is one of the Governments in Nigeria regardless of where paid and there no agreement between Nigeria and that other country exempting that income from tax in Nigeria; or
 - iv. the individual is in an employment as a seafarer during any period in which the individual is serving under articles which he had signed in Nigeria or is performing stand-by duty on board a ship preparatory to his signing articles in Nigeria. (This provision does not apply to any person holding such employment in the Nigerian Navy or the Nigerian Ports Authority).

Where the duties of the employment are wholly or partly performed in Nigeria, employment income derived during any period of leave or temporary absence from Nigeria shall be liable to tax in Nigeria. This period will also count for the purpose of determining the 183 days' threshold of the person's residence status in Nigeria.

7.2 Treatment of Income from employment When There is Tax Treaty

7.2.1 Where the Ship or Aircraft Operates in International Traffic

Where an individual exercises their employment aboard a ship or aircraft used for international traffic or serves as a member of the regular complement on that vessel, that income may be subject to tax in Nigeria. Such profits will be treated in line with the Article on dependent personal service or income from employment, so far as such ship or aircraft operates in international traffic. The tax treatment may defer, depending on the treaty provisions. The following are possible treatments:

- i. Shared taxation: allows for source State taxation. Nigeria will tax in accordance with its domestic law.
- ii. Shared taxation: allows for taxation in the state the operator of the ship and aircraft is resident (residence of employer). Nigeria will tax in accordance with its domestic law.
- iii. Exclusive taxation: allows for taxation only in the country of residence of employee. Nigeria will not have a taxing right as this will switch off the domestic law.
- iv. Exclusive taxation: allows for taxation only in the country of residence of employer. Nigeria will tax in accordance with its domestic law.

7.2.2 Where the Ship or Aircraft does not operate in International Traffic

The income from employment will be treated in accordance with the rules stated in 7.1.2 above.

8.0 Taxation of Foreign Ships or Vessels Lifting Crude Oil from Nigerian Territorial Waters

One of the common features of the oil industry in Nigeria is that crude oil is often sold to foreign buyers "Free on Board" origin ("FOB origin"), also sometimes phrased as "FOB shipping" or "FOB shipping point". This means that the foreign or non-resident buyers are responsible for the arrangement and payment for vessels for the transportation of the crude oil from Nigeria. Usually, the shipping companies contracted for the transportation of the crude are non-residents and payments to them are made by the non-resident buyers of the crude oil.

The provisions of Paragraph 3.2 of this Circular will be applicable in such circumstances as the carriage of crude oil from Nigeria falls under the provisions of Section 14(1) of CITA.

Consequently, any vessel that carries crude oil, gas, petroleum products or any other item from Nigeria is liable to tax in Nigeria, irrespective of where or with whom the carriage contract was executed.

9.0 Income from Ancillary Services or Non-Freight Income

9.1 Under the Domestic Law

Section 14 of CITA covers taxation of profits or losses arising from the carriage of passengers, mails, livestock or goods shipped, or loaded into an aircraft, in Nigeria. As indicated in subsection 5, the application of Section 14 of CITA does not cover non-freight income, such as income derived from demurrage & detention, local charges, stevedoring, clearing and forwarding, cargo handling, container leasing, storage, agency, etc. Where a foreign shipping or air transport company engages in any of such activities in Nigeria, profits derived by that company, from such non-freight activities, shall be taxable under Sections 9 and 13(2) of CITA.

These ancillary services are liable to **Value Added Tax (VAT)** in accordance with section 2 of VAT Act. VAT must therefore be charged and remitted to the Service in accordance with the extant tax laws.

9.2 When there is Avoidance of Double Taxation Agreement

Profits of an enterprise engaged in air or shipping transport consist of the profits directly obtained by the enterprise from the transportation of passengers or cargo by ships or aircraft (whether owned, leased or otherwise at the disposal of the enterprise) that it operates in international traffic. However, in some of the Agreements, such profits include profits from other ancillary activities.

Consequently, where a foreign company that engages in air or shipping transport in Nigeria earns income that is not directly derived from the carriage of passengers, mails, livestock or goods by ships or aircraft, such income, except where expressly provided in the ADTA, will not come under the Article on Shipping and Air Transport in the ADTA. The profits attributable to the company's Permanent Establishment in Nigeria is liable to tax in accordance with the Article on Business Profits in the treaty. All other relevant provisions of CITA will be applicable in the computation of assessable profits, total profits and tax payable.

Similarly, where a foreign company engages in providing logistics, agency or other ancillary services to air and shipping transport in Nigeria but does not engage in air or shipping transport, income earned by that company will not come under the Article on Shipping and Air Transport in the Agreement. The

company shall also not be entitled to any concession granted under the Article. The profits attributable to company's Permanent Establishment is liable to tax in Nigeria as provided under the Article on Business Profits in the treaty. All other relevant provisions of CITA will be applicable in the computation of assessable profits, total profits and tax payable.

10.0 Capital Gains Tax

10.1 Under the Domestic Law

10.1.1 Ships or Aircraft Used in International Traffic

Section 24 (f) of the Capital Gains Tax Act Cap. C1 LFN 2004 (as amended) provides that:

*"Ship or aircraft **used in international traffic** is situated in Nigeria if and only if the owner is a resident in Nigeria, and an interest or right in or over a ship or aircraft is situated in Nigeria if and only if the person entitled to the interest or right is resident in Nigeria".*

From the above, a ship or aircraft used in international traffic is situated in Nigeria, irrespective of the location of the ship or aircraft at the time of the disposal, where:

- i. the owner of the ship or aircraft is resident in Nigeria; or
- ii. a resident of Nigeria owns an interest in or right in the ship or aircraft.

As such, gains from the disposal of such ship or aircraft or the right or interest in the ship or aircraft is chargeable to capital gains tax in Nigeria, even where the ship or aircraft is not physically in Nigeria at the time of the disposal. Conversely, the gain will not be taxable in Nigeria where the ship or aircraft is owned by a non-resident or a non-resident owns the right in or interest over it, even where the ship or aircraft is located in Nigeria at the time of disposal.

10.1.2 Ships and Aircraft not used in International Traffic

Where a ship or aircraft which is used for purposes other than international traffic (e.g. a rig, intra-Nigeria transport, lift boat or stationary restaurant, hotel and other uses) is located in Nigeria, such ship or aircraft shall be treated as a tangible moveable property of the owner. The disposal of such ship or aircraft is chargeable to capital gains tax in Nigeria, irrespective of whether or not the owner or alienator is a resident of Nigeria or whether or not the disposal took place in Nigeria.

However, where a ship or aircraft which is used for purposes other than international traffic is located outside Nigeria, the disposal of the ship or aircraft shall be chargeable to capital gains tax in Nigeria only where the ship or aircraft is owned by a resident of Nigeria.

10.3 When there is Double Taxation Agreement

In accordance with the relevant provisions of the DTAs, gains derived by a Nigerian resident from the alienation of a ship or aircraft is chargeable to capital gains tax in Nigeria, irrespective of whether the ship or aircraft is operating in international traffic or not.

In the case of non-residents, gains derived from the alienation of a ship or aircraft:

- i) used in international traffic will not be chargeable to capital gains tax in Nigeria.
- ii) not used in international traffic, will be chargeable to capital gains tax in Nigeria where the ship or aircraft is located in Nigeria and constitutes a permanent establishment of the non-resident. The alienation of a ship or aircraft will also be chargeable to capital gains tax in Nigeria under a DTA where the ship or aircraft is owned by a Nigerian permanent establishment of a non-resident. In both cases, the alienation will be treated in accordance with the provisions on the alienation of business assets of a permanent establishment under the Article on Capital Gains in that DTA.

Note: Where the owner of the ship or aircraft or the person who owns an interest in or right over the ship or aircraft is a resident of both treaty countries, the tie breaker rule under the Agreement shall be applied to determine the jurisdiction of his residence for tax purposes.

11.0 Claim of Tax Treaty Benefits

Relevant information regarding the claim of tax treaty benefits by foreign companies engaged in shipping or air transport in Nigeria may be obtained from FIRS' Information Circular on the Claim of Tax Treaties Benefits in Nigeria, <https://www.firs.gov.ng/TaxResources/TreatyRelatedGuidelinesandCirculars>. Specifically, Paragraph 5 of the Information Circular which provides the procedures for accessing treaty benefits must be complied with.

12.0 Message Transmission Operations

Section 15 of CITA provides that foreign companies engaged in the business of transmission of messages by cable or by any form of wireless apparatus shall be subject to tax as though they were engaged in shipping or air transport business.

Therefore, the guidance provided in this Information Circular equally applies to foreign companies engaged in the business of transmission of messages by cable or by any form of wireless apparatus except where otherwise stated.

13.0 Enquiries

Any request for further information or clarifications on this Information Circular should be directed to the:

Executive Chairman,
Federal Inland Revenue Service
Revenue House,
15, Sokode Crescent, Wuse Zone 5, Abuja.

Or
Director, Tax Policy and Advisory Department,
Federal Inland Revenue Service,
26, Sokode Crescent,
Wuse Zone 5, Abuja.

Or
Email: tpld@firs.gov.ng