The Transfer Pricing (TP)-specific penalty regime that was introduced via the recently published Income Tax (Transfer Pricing) Regulations 2018 (“new Regulations”) is without a doubt one of the most talked-about aspects of the new Regulations.

The new Regulations take effect from 12 March 2018 and apply to basis periods (i.e. financial years) beginning after this date. The new Regulations revoke the 2012 TP Regulations.

One question that comes up in practically all conversations with affected companies is whether they can suffer penalties under the new Regulations for defaults or transactions relating to periods that preceded the introduction of the new Regulations.

Based on its public notice of 3 October 2018, the FIRS believes it can apply these penalties to prior period defaults; but is this really the case?

**Overview of the penalty regime under the new TP Regulations**

The 2012 Regulations had no specific penalty provisions. The new Regulations however introduce administrative penalties for different offences. These penalties are generally considered to be material.

The minimum penalty for most offences is N10 million. The penalties could also be as high as 1% of the value of the intercompany transaction plus a daily amount of between N10,000 and N25,000 for each day the default continues. The penalties apply to offences such as failure to file TP declarations and TP disclosures, submission of incorrect disclosures, failure to provide TP documentation (or other information) within the time required, etc.

The question we examine is; to what extent any of these penalties can be applied to a taxpayer with prior period defaults; but is this really the case?

**Illustrative case**

To help understand the issues, we will use an illustrative case of a fictitious taxpayer Tough Times Ltd (TTL). Assume these are the facts:

- TTL has a financial year end of 31 December.
- TTL failed to meet all of its TP compliance obligations for the 2016 financial year (FY) as and when due.
- Today is 31 March 2019, and FIRS is reviewing TTL’s TP compliance for the 2016 FY.

- The relevant returns due from TTL are still outstanding.

Based on the above facts, we will consider a number of issues that could arise.

**Can FIRS penalise TTL for failing to submit its 2016 TP declaration and disclosure forms when they were due?**

To answer this question, we will need to examine the relevance of the effective date of the new Regulations as well as the definition of commencement.

The effective date of any law marks the specific date from which the law will apply. The effective date of the new TP Regulations is 12 March 2018. Regulation 27 of the new TP Regulations, however defines the term “commencement” to mean ‘basis periods beginning after the effective date of the new Regulations’. One can therefore conclude that the new Regulations take effect from basis periods subsequent to 12 March 2018. For a company with a 31 December year end, this will mean the 2019 financial year (basis period).

Therefore the FIRS cannot penalise TTL under the new Regulations for failure to file its TP returns which were due on 30 June 2017, i.e. prior to the commencement of the new Regulations. This is supported by the presumption in law that enactments should not apply retrospectively unless specifically stated. Also, Section 4(9) of the Nigerian constitution prohibits the making of laws with a retrospective application (albeit in relation to criminal offences).

**Can FIRS penalise TTL based on the fact that the 2016 TP returns are still outstanding as at 31 March 2019?**

The penalties under the new Regulations will only be effective from the 2019 financial year. As such, even if the 2016 TP returns are still outstanding as at 31 March 2019, the FIRS cannot penalise TTL under the new TP Regulations. This is because section 27 of the new Regulations has specified that the Regulations will commence from basis periods starting after 12 March 2018. The reference to basis periods indicates that the Regulations relate to financial years starting after this date.

In addition, Section 6(1) of the Interpretation Act provides that a penalty or punishment (including a privilege or right) under a repealed enactment subsists even after the enactment is repealed. Therefore, any non-compliance relating to the period in which the 2012 Regulations applied is punishable under the 2012 Regulations.

**If in 2019, FIRS makes a request for TTL’s 2016 TP documentation and the company is unable to provide it within 21 days, can FIRS levy a penalty under the new Regulations?**

This is a grey area. On one hand, the right interpretation of the commencement provision is that all of the provisions of the new Regulations (including penalties) will only affect matters relating to the 2019 financial year and beyond. Based on this, if in 2019, TTL fails to provide the FIRS with its 2016 TP documentation within the time prescribed, FIRS cannot levy TTL as the penalty can only apply for matters relating to FY 2019 and subsequent years.

On the other hand, it can also be argued that the FIRS can penalise TTL (under the new Regulations) for failure to provide its 2016 TP documentation within the time allowed so far as the FIRS’ request is made after the commencement date of the new Regulations i.e. in 2019.

To the extent that a request is made after the effective date and commencement of the new Regulations, any default by the taxpayer can be said to occur under the new Regulations. As such, the FIRS can apply penalties under the new Regulations if TTL does not comply with its request.

**Conclusion**

The FIRS by Public Notice of 3 October 2018 has officially granted taxpayers a grace period up to 31 December 2018 to fulfil all pending compliance obligations. It has further stated that it will administer the penalties under the new Regulations to any outstanding obligations beginning from 1 January 2019.

The public notice shows that the FIRS will attempt to apply the penalties under the new Regulations to defaults relating to periods prior to the introduction of the new Regulations. While we generally do not believe that this is permissible under the law, taxpayers are advised to take steps to avoid a dispute all together by ensuring that they meet all outstanding obligations before the end of the year.