

Nigeria Issues Significant Economic Presence Order

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Introduction

The Minister of Finance, Budget and National Planning (the Minister) has issued the Companies Income Tax (Significant Economic Presence) Order, 2020 (SEP Order), to complement the 2019 Finance Act (FA 2019).

The SEP Order sets out the conditions under which non-resident companies (NRCs) that provide digital services; or technical, professional, management, or consultancy services (TPMC); to Nigerian customers, from outside Nigeria will be deemed to have a taxable nexus, and therefore be liable to tax, in Nigeria. You can find the SEP Order [here](#).

Finance Act 2019 and SEP

Prior to the entry into force of FA 2019, NRCs were only deemed to be liable to tax in Nigeria on their business income if they: (i) carried on business through a fixed base in Nigeria; (ii) carried on business through an agent in Nigeria; (iii) executed a turnkey project in Nigeria; or (iv) failed to price their related party transactions at arm's length.

FA 2019 expanded the conditions under which the business income of NRCs would be taxable in Nigeria. Under the new rules, NRCs will be liable to tax in Nigeria if: (i) they supply digital services or goods and profits can be attributable to the activities; or they provide TPMC services; and (ii) they have a significant economic presence (SEP) in Nigeria

Although FA 2019 specified the types of business activities that would be affected by these new rules, it did not define what would constitute a SEP of an NRC.

Who is impacted by the SEP Order

The SEP Order specifies the threshold above which NRCs undertaking the specified activities would be deemed to be taxable in Nigeria.

It also clarifies the specific activities and persons impacted to include:

- a) Digital service providers – that is, NRCs whose activities involve: streaming or downloading services of digital contents (e.g. movies, videos, music, applications, games and e-books); transmission of data collected about Nigerian users generated from users' activities on websites or mobile applications; provision of goods or services through digital platform; or provision of intermediation services through digital platforms, website or other online applications that link suppliers and customers in Nigeria; and

- b) NRCs that provide technical (including advertising services, training, or the provision of personnel), professional, management, or consultancy services to Nigerian customers.

SEP threshold for digital service providers

A non-resident digital service provider will meet the SEP threshold in Nigeria if:

- 1) it derives gross turnover or income in excess of ₦ 25million (about US\$65k) in a given year from any or a combination of the activities listed in the SEP Order. The ₦ 25million threshold will also take into account activities carried on by the NRC's connected persons during the accounting year; or
- 2) it uses a Nigerian domain name (.ng) or registers a website in Nigeria; or
- 3) it has a purposeful and sustained interaction with persons in Nigeria by customising its platform to target persons in Nigeria (e.g. by reflecting prices of products/services in Naira, providing options for billing or payment in Naira etc.).

SEP threshold for NRCs providing technical, professional, management or consultancy services

A NRC that provides technical, professional, management or consulting services will have a SEP in Nigeria if it earns income or receives payment from:

- 1) a person resident in Nigeria; or
- 2) a fixed base or agent of a non-Nigerian company.

For this category, the withholding tax deducted by the recipient of the service is the final tax. The SEP Order also includes categories of payments that are exempt.

The SEP order however appears to expand the meaning of technical services to include advertising and training services as well as the supply of personnel. It is debatable if this is in line with the provisions of FA 2019.

Impact of international agreements

The SEP Order provides that if Nigeria enters into any multilateral agreement or consensus arrangement to address the tax challenges arising from the digitalization of the economy, the provisions of that agreement or arrangement will apply (and effectively override the provisions of the SEP Order) with respect to any NRC that is covered by that agreement or arrangement.

It also follows (based on treaty supremacy) that NRCs that operate from a country that has a Double Tax Treaty (DTT) with Nigeria, will not be affected by the SEP, Order until changes are made to the DTT.

Implications for Tax Compliance and Administration

Some of the affected NRCs will be required to register for income taxes in Nigeria and file annual tax returns even if they do not have a physical presence in Nigeria.

Nigerian resident businesses (as well as the fixed bases of non-resident companies) that have transactions with the affected NRCs will also be required to account for withholding tax on some of the payments made to these NRCs.

The SEP Order however raises a number of practical concerns from a compliance and tax administration perspective.

- 1) Profit attribution - The SEP order does not provide any guidance on how the profits attributable to the Nigerian SEP of affected NRCs will be determined. This will create uncertainties for NRCs who need to comply.
- 2) Enforcement and compliance - The FIRS may struggle to enforce compliance without international consensus, as a number of the companies affected may be outside the territorial reach of the FIRS. This problem will also be exacerbated where the NRCs sell their products and services directly to the final consumers in Nigeria. NRCs that do not have any form of presence in Nigeria may also struggle to comply.

Conclusion

Nigeria has joined other countries that have taken unilateral action to tax the digital economy. The SEP Order makes it clear that a physical presence will no longer be required for certain categories of remote services to be taxable.

Non resident companies must therefore assess how the rules affect them and take steps to comply where necessary. This will also apply to Nigerian resident companies that transact with the affected non-residents.

In order to improve compliance and reduce uncertainty for taxpayers, the FIRS is encouraged to introduce simplified registration and compliance processes for affected NRCs. The FIRS will also need to provide clarity on the basis by which profits will be attributed to the SEPs of the NRCs.

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