

The corporate Withholding Tax (WHT) administration system needs to be overhauled

Background

WHT is an advance payment of income tax, and is deductible at source on payments made for certain transactions. It can be applied as a credit against income tax in many instances.

Section 81 of the Companies Income Tax Act (CITA) provides that WHT should be deducted from payments made to companies on which they will be assessed to income tax. WHT is only applicable on such payments to the extent that the income is subject to income tax. The concept of WHT may have been introduced to reduce tax leakages and gather information of commercial activities being carried out by both resident and non-resident businesses. It is also an effective tool for collecting tax on non-residents' income in Nigeria where cross-border enforcement is impractical.



Some practical issues

The WHT system in Nigeria unfairly discriminates against suppliers from whom WHT has been deducted. Apart from prohibitive rates that eat into margins and cash flows, there are inconsistent practices by tax authorities' and ambiguity from legislation. Many companies carry huge sums of WHT receivables in their accounts without any realistic chance of utilising the WHT or getting a refund. This could discourage voluntary compliance.

The irregularity of the WHT credit system

Let us assume that Company A provides a consultancy service to company B for N100. Company B deducts WHT of N10 and pays company A N90. However, Company B does not remit the WHT to the Federal Inland Revenue Service (FIRS). The FIRS in turn will not provide Company A with the WHT credit notes equivalent to N10 on the basis that it did not receive any remittance from Company B. The FIRS will also deny Company A the benefit of the credit when it files its tax returns.

The FIRS Position

The FIRS take the position that it does not have an obligation to provide a taxpayer with credit notes until the agent who deducted the WHT has remitted it to the FIRS. They argue that WHT is an advance **payment** of tax, and not an advance deduction of tax.

Technically, they have a point for transactions with foreign companies where the WHT is the final tax. In such a case, "the tax, **when paid over to the Board**, shall be the final tax due from a non-resident recipient of the payment" in relation to rent, interest, dividend and royalties. The WHT only becomes final tax in that scenario "when paid over to the board". However, the same argument cannot be made for domestic transactions and any other transaction covered by the WHT Regulations pursuant to Section 81 of CITA.

The law stipulates that upon deduction, the agent is to provide the FIRS with certain particulars of the transaction along with the remittance of the WHT including the name and address of the recipient, the gross amount of the transaction, the amount of the tax, the percentage that has been deducted among others. The FIRS therefore argue that without the agent remitting the WHT and providing this information, the FIRS will not be able to properly process and credit the company with the WHT.

Taxpayers' position

One question that needs to be answered from the viewpoint of the taxpayer is when can it be deemed that WHT has been "paid over to the board"? Is it when the FIRS' agent pays into the FIRS account, or when the amount has been deducted by the FIRS agent?

The best way to answer this question is by considering the relationship between the parties.

The provisions of the Companies Income Tax Act (CITA) and the WHT Regulations mandate companies to deduct WHT on payments made for goods and services received from suppliers. These create an implied 'Principal-Agent' relationship between the FIRS and the company making the deduction respectively.

This agency relationship is mandatory and is so strict that where the agent refuses to deduct or pay WHT as required, the FIRS can assess the agent. This means that the FIRS, as the principal, should be held responsible for the action or inaction of its agent, where the agent deducts and refuses to remit to the principal. Furthermore, the law does not in any way place any obligation on the company providing the service to ensure that the WHT is in fact remitted to the FIRS. Once the WHT has been deducted, the process of remittance is between the FIRS and the agent; and has nothing to do with the supplier.

The above points are supported by the WHT Regulations. The Regulations do not make any provision for the FIRS to issue credit notes. Under Para 3(1) of the WHT Regulations, it is the customer that receives the supply that is required to issue the receipt (not the tax authority issuing a credit note). Para 3(2) also says that the person who suffered the deduction should present the receipt given by the customer to claim the credit. The FIRS practice of issuing credit notes and denying taxpayers the benefit without credit notes is simply illegal.



Arbitrary WHT rate

The FIRS has repeatedly made a judgement call of categorising all general services including security, repairs, logistics, etc as expenses liable to 10% WHT. Whereas, 10% WHT only applies to the extent that those services are considered as technical, consultancy, management or professional. Such services should fall under the generic contracts category (including general services not related to professional/consultancy fees) and should attract 5% WHT. Taxpayers are subject to unnecessary objections and reconciliations during audit with respect to this subject matter.

Furthermore, the recent TAT judgement in the case between Tourist Company of Nigeria and the FIRS dated 17 February 2021 clarified that services like security services are not professional or technical and therefore liable to WHT at the rate of 5%.

Refund of Excess WHT

As earlier mentioned, the practice of indirectly denying Taxpayers their lawful right to recover excess WHT where the amount of tax deducted from their income exceeds their income tax liability discourages voluntary compliance. The process is not only rigorous but almost impossible in practice. This results in the company's potential cash flow being tied down as WHT credits, and ultimately, negatively impacts shareholders value and the company's investment capacity. The refund of excess WHT credits should be automatic in a proper tax administration system, as long as the taxpayer can be easily identified and within the tax net. Otherwise, WHT effectively becomes a punishment for doing business.

Unclearified Grey Areas

Occasionally, the FIRS releases information circulars, which are intended to provide clarity to certain grey areas in tax administration. FIRS circulars are useful so taxpayers are able to get more certainty over their future transactions or anticipate areas where their position may differ from that of the tax authorities. The circulars are not law and only represent the opinion of the FIRS, which could also be contested by taxpayers.

The FIRS has tried to clarify what constitutes a 'sale in the ordinary course of business' because such sales are not subject to WHT. Over the years, the FIRS has given conflicting interpretations of the phrase such as taking the view that it applies only to 'over-the-counter' transactions, cash transactions, or where there is no written contract. The controversy around this was resolved in the landmark case of Tetra Pak V FIRS where the phrase was interpreted to cover sales made by a company in line with its routine business. The FIRS has still not updated its information circulars which has led to some companies still wrongfully deducting WHT even on purchase of goods and assets.

WHT Credit Notes

In Mid-2021, the FIRS rolled out TaxPromax and subsequently commenced a compulsory transfer of physical credit notes to the online portal. Taxpayers have been directed to ensure that all physical credit notes are reconciled with the FIRS, agreed, and subsequently uploaded into Taxpromax. There is a reason for this approach by the FIRS as they are using this opportunity to clean up historic data on WHT. However, the process is time consuming and demanding and shifts internal administrative issues in the FIRS to the taxpayers. In addition, there is no legal basis to deny taxpayers of their right to the credit if it is not uploaded on Taxpromax.

Considering that credit notes were a creation of the FIRS, it would have been ideal for the FIRS to deploy technology towards transferring all unutilised credits to the account of beneficiaries, using their unique Tax ID.

It has also been observed in a few instances that payment of WHT using the TIN of the beneficiary may not necessarily guarantee that the credit is recognised in favour of the beneficiary on Taxpromax. This glitch has been observed in a few cases without any real solution from the perspective of taxpayers.

Conclusion

Where a company deducts WHT from payments to suppliers without remitting the tax to the FIRS, a criminal offence has been committed. The FIRS can prosecute the offending company and take necessary steps to recover the WHT. However, this should not affect or impact the company which has suffered the WHT, as this is an issue purely between the FIRS and its agent.

There is a need to reform the WHT Regulations and processes to align with best practices from other countries. In fact, there are countries that levy less WHT rates than Nigeria or even no WHT at all, but are more efficient in tax administration based on their relative tax to GDP ratio.

With the introduction of the Tax ProMax and the stated intention of the FIRS for all WHT credit balances to be transferred to the TaxProMax, this issue becomes even more important. Companies that are denied the benefit of their WHT either because they do not have the FIRS' issued credit notes or the FIRS has not acknowledged their balance on their portal should consider approaching the courts for fair resolution.

The increasing pressure for the tax authorities to generate more tax revenue, without expanding the tax net, may in fact, be a motivating factor for poor administration of WHT. By denying taxpayers access to refunds or the benefit of their credits, taxpayers are forced to still pay additional CIT. This would encourage evasive tax behaviour compared to countries where they have a robust refund process.

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