



## LEGAL AND REGULATORY FRAMEWORK GUIDING TAXATION OF INCOME DERIVED BY FOREIGN COMPANIES IN NIGERIA

### Introduction

It is not novel to find companies expand their reach across borders by incorporating new business entities in foreign countries. There, in fact, exist foreign companies in Nigeria who derive income from Nigeria in one way or another.

This Article seeks to explore the legal framework guiding taxation of income derived by foreign companies in Nigeria.

### Legal and Regulatory Framework Guiding Taxation of Income Derived by Foreign Companies from Nigeria.

There are various laws which regulate the tax liabilities of individuals and companies or entities (foreign or local) who generate income in Nigeria. However, this Article will restrict its examination of the applicable tax laws to the tax liability of foreign companies in Nigeria.

### Companies Income Tax (CIT)

This is regulated by the Companies Income Tax Act ("CITA")<sup>1</sup>: CIT is payable on the profits of a company accruing in, derived from, brought into, or received in Nigeria for trade or

royalties, discounts, charges or annuities, fees, dues and allowances or any other source of income, profits or gains from disposal of short-term government securities, etc. Thus, a Company (whether resident or non-resident) generating income from or receiving income in Nigeria is liable to pay tax on such income and is permitted to make allowable deductions such as interest, rent, repairs and all other expenses wholly, reasonably, exclusively and necessarily incurred for the purpose of such trade or business in deriving its taxable income.<sup>2</sup> Generally, a company is liable to file annual tax returns with the Federal Inland Revenue Service ("FIRS")<sup>3</sup>

### Withholding Tax

Withholding Tax ("WHT") is an advance form of payment of income tax charged on the income of a taxpayer at source. A duty is imposed on a person (body corporate, MDAs or statutory bodies) with the obligation to pay a sum due under a transaction to another person to withhold a certain portion of such money as tax, which is to be remitted to the relevant tax authority and the net amount is paid to the

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<sup>1</sup> Companies Income Tax Act CAP C21 LFN 2004. The relevant provisions are sections 9, 13, 40, and 81.

2018

<sup>2</sup> Section 13 (1 & 2) *ibid*.

<sup>3</sup> Section 55 (1) *ibid*.



beneficiary. WHT must be deducted at source before payment of dividends, rent, interest, Director's fees, technical services, management services, royalties, consultancy and professional services, commissions, all types of contracts other than sale and purchase of goods and services and building construction and related service. Upon remittance of WHT by the withholding party to the relevant tax authority, Credit Notes are issued by the relevant tax authority in favour of the taxpayer and such Credit Notes may be used by the taxpayer to offset subsequent tax liabilities.

WHT deducted at source and remitted to the relevant tax authority in respect of investment income (frank investment) such as dividend, rent, interest and royalty paid (or credited) to a foreign company is treated as final tax due from that company. There will be no further tax liability on such a foreign company in respect of the same income and no obligation to file tax returns.<sup>4</sup>

**Income Tax (Transfer Pricing) Regulations ("the Regulations"):**<sup>5</sup> The provisions of the Regulation aim to ensure the observance of the arm's length principle – fair and market

competitive pricing, as would naturally be the case where both parties are unrelated - in all transactions between related or connected persons. The Regulations stipulate conditions for compliance with the arm's length principle in transactions involving the exploitation of intangible assets to take into consideration the contractual arrangements, the extent it performs functions and assumes risk *relating to the development, enhancement, maintenance, protection and/or exploitation (DEMPE) of the intangible asset in question*<sup>6</sup>. It further provided that *"where there is a transfer of rights in an intangible asset other than complete alienation of the right, tax deductions for any payments for the exploitation of those rights will be capped at 5% of earnings before interest, tax, depreciation and amortization (EBITDA)."*<sup>7</sup>

The Regulations defines **Connected Persons** as:

*"... persons are deemed connected where one person has the ability to control or influence the other person in making financial, commercial or operational decisions, or there is a third person who has the ability to control or influence both*

<sup>4</sup> Section 55 (7) Companies Income Tax Act, CAP C21, LFN 2004 as amended by Section 16 of the Finance Act, 2020

<sup>5</sup> Income Tax (Transfer Pricing) Regulation,

<sup>6</sup> Regulation 7 (1) of the Income Tax (Transfer Pricing) Regulation, 2018

<sup>7</sup> Regulation 7 (5) of the Income Tax (Transfer Pricing) Regulation, 2018



*persons in making financial, commercial, or operational decisions”.*<sup>8</sup>

The Regulations impose an obligation on taxable persons to declare their relationship with all connected persons whether such persons are resident in Nigeria or elsewhere, make updated declaration where there are significant changes in the affairs of the connected persons, to disclose controlled transactions when they occur and to keep records of all connected transactions and provide same to FIRS on demand. There are stringent penalties prescribed for failure to comply with the Regulation.<sup>9</sup>

## CONCLUSION

We have briefly examined the legal and regulatory framework guiding the taxation of income derived by foreign companies from Nigeria. We have noted briefly some of the applicable laws and regulations.

The tax laws treated in this Article are by no means an exhaustive list, but they are the most common and likely tax obligations that a foreign company transacting business in Nigeria will be immediately exposed to.



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<sup>8</sup> Regulation 12 *ibid*.

<sup>9</sup> Regulations 13 (7 & 8); 14 (4 & 5); 15 (3); 16 (5); 17 (5); 20 *ibid*.