THE CHARTERED INSTITUTE OF TAXATION OF NIGERIA.
2013 INDUCTION TRAINING PROGRAMME

SUBJECT: INTERNATIONAL TAXATION

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International taxation-What is it?

- **International taxation** is the study or determination of tax on INCOME /PROFIT of an individual or enterprise, subject to the tax laws of different countries.
- Any income or profit not taxable under a domestic tax law of a country cannot be taxed in that country under international tax agreement between that country and another country.

Why International Activities ?

- The countries of the world interact with each other and engage in activities across their borders for social, economic, cultural, religious, political, etc reasons, regional integration;
- because no country can live in isolation of others.
- International activity has tax implication

Basis of Taxing Rights

There are two major taxing rules are commonly feature in every tax treaty; namely;

- **Source Rule**, and
- **Resident Rule**

- **Source Rule** : By explanation refers to the Contracting State (country) from where the income generated, hence such Contracting State may be given the opportunity to tax such income
- **Residence Rule** ; This rule confers the taxing rights on the Contracting State where the tax payer (individual or enterprise) is a resident.

Residence Rules :

A resident is a person who has sufficiently close connections to a country whereby he will be liable to tax there on his worldwide income. A Nigerian resident individual is liable to tax on his worldwide income, which may also be liable to tax in another country.

- Under the Nigerian domestic tax laws, an individual is regarded as resident throughout an assessment year if he:
- (i) is domiciled in Nigeria;
- (ii) sojourns in Nigeria for a period or periods in all amounting to 183 days or more in a 12 – month period; or
- serves as a diplomat or diplomatic agent of Nigeria in a country other than Nigeria.
- A taxpayer may be liable to Nigerian taxation, either because he is resident in Nigeria or because the source of his income is located in Nigeria. This implies that, an individual may be deemed resident in more than one country. This creates the problem of "dual residence“

See Article 4 of the Tax Treaty with the title RESIDENT

Tax implications of being resident… Individual

PITA CAP P8 LFN 2004

- Section 2 -Persons on whom tax is to be imposed.
- (1) Tax of an amount to be determined from the set out in the Sixth Schedule (in this Act referred as "income tax") shall be payable for each year of assessment on the total income of -
- (a) every individual other than persons covered under paragraph (b) of this subsection or corporation sole or body of individuals ***deemed to be resident*** for that year in the relevant State under the provisions of this Act

Tax implications of being resident… Individual
PITA CAP P8 LFN 2004

- Section 3 (1) - Income Chargeable

  Subject to the provisions of this Act, tax shall be payable for each year of assessment on the aggregate amounts each of which is the income of every taxable person, for the year, *from a source inside or outside Nigeria..*

Sec 8 Charge of Tax :

"There shall be levied upon the profits of each accounting period of any company engaged in petroleum operations during that period, a tax to be charged, assessed and payable in accordance with the provisions of this Act"

Tax implications of being resident … Enterprises in Non-Oil.. *CITA CAP C21 LFN 2004*

Sec 9(1) *Charge of Tax :*

"Subject to the provision of this Act, the tax shall for each year of assessment, be payable…upon the profits

- *accruing in,*
- *derived from,*
- *brought into or*
- *received in*

Nigeria.

A taxpayer may be liable to Nigerian taxation, either because he is resident in Nigeria or because the source of his/its income is located there.

Domestic tax laws and foreign revenue law

- It should be noted as a general principle, that only the domestic tax laws of a sovereign country are applicable and enforceable within that country
- In this regard Article 28 of OECD and United Nations Model Tax Convention titled –*Assistance in the Collection of Taxes* Should not be misconstrued as enforcement of foreign revenue law

Some Applicable Revenue Law in Nigeria- *Domestic Tax Laws*

The domestic tax laws in the Nigerian context includes;

- Petroleum Profits Tax Act (PPTA)
- Personal Income Tax Act (PITA)
- Companies Income Tax Act (CITA)
- Capital Gains Tax Act (CGTA)
- Education Tax Act (ETA)..
- Value Added Tax (VAT)
- Taxes and Levies (approved list for collection) Act
- etc

Basis of Taxing Rights

There are two major taxing rights commonly at the disposal of a country;

- **<u>Source Principle of Taxation</u>** : The country may tax the income having its source in that country, regardless of the residence of the taxpayer
- **<u>Residence Principle of Taxation</u>**; The country has taxing rights over the taxpayer where such tax payer (individual or enterprise) is a resident.

Provisions for relief against double taxation

- Domestic tax laws
  - Sec 11, 38, 39 PITA as amended by Act 20, 2011) etc and similar provisions in CITA and PPTA
- Tax Treaty provisions:
  - Article 24 – Elimination of Double Taxation
  - This article discusses the methods of elimination of double taxation.
  - In all Nigeria treaties, elimination of double taxation is granted by *Credit Method*.
  - There is also *Exemption Method*.

Chapter V – Methods of Elimination of Double Taxation

- The chapter contains only 1 article:
- Article 24 – Elimination of Double Taxation
- This article discusses the methods of elimination of double taxation.
  - In all Nigeria treaties, elimination of double taxation is granted by *Credit Method*.
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Transfer Pricing - Methodologies

- In determining whether the result of a transaction or series of transactions is consistent with the arm's length principle, one of the following transfer pricing methods shall be applied—
  - (i) the Comparable Uncontrolled Price ('CUP') Method
  - (ii) the Resale Price Method;
  - (iii) the Cost Plus Method;
  - (iv) the Transactional Net Margin Method; or
  - (v) the Transactional Profit Split Method.
  - Advanced Pricing Agreement

Transactions Subject to Transfer Pricing Guidelines

- Transactions between related enterprises within a multinational enterprise group
- Transactions between a Permanent Establishment (PE) and its head office or other related branches. Branches are treated as separate entity.
- Sales & purchase of goods and services
- Sales, Purchase or lease of tangible assets
- Transfer, purchase or use of intangible assets
- Provision of services
- Lending or borrowing of money
- Manufacturing arrangement
- Any transactions which may affect profit or loss of the enterprise involved.

Explanatory Notes on Terms & Concepts-

ARM'S LENGTH PRINCIPLES

- The establishment of transfer prices in transactions between related parties based on the prices charges in similar transactions between unrelated parties. A key concept of most transfer pricing rules is that prices charged between related enterprises should be those which would be charged between unrelated parties dealing at arm's length

THIN CAPITALISATION

- An enterprise is considered operating with thin capitalisation where the size of paid up capital base is considered "low /small /thin" compare with the size of its operations- (turnover)
- Most jurisdictions are of the opinion that taxable income may be reduced by amount expended as interest on loans, in a situation where an enterprise finances its subsidiary enterprises through loans rather than capital.

Explanatory Notes on Terms & Concepts-

CONTRACTING STATES

- The two countries that are parties to a bilateral tax treaty.

INTERNATIONAL TRAFFIC

- The term "international traffic" means any transport by a ship or aircraft operated by an enterprise that has its place of effective management in a Contracting State, except when the ship or aircraft is operated solely between places in the other Contracting State;

COMPETENT AUTHORITY

- The term "competent authority" in all the tax treaties between Nigeria and other countries means the Minister of Finance or his authorised representative.

Explanatory Notes on Terms & Concepts-

DIPLOMATIC CHANNEL

- The Ministry of Foreign Affairs is regarded as "diplomatic channel" through which the Contacting States exchange information.

TREATY SHOPPING

- The use of a tax treaty by a person who is not resident in either of the treaty countries, usually through the use of a conduit entity resident in one of the countries.

TAX SPARING CONCEPT

- This is a provision in tax treaties that seeks to protect the tax incentives which the government grants to companies as part of the economic development strategy. The intention of government is that the benefits would accrue to the targeted investor. But without a tax-sparing provision in a bilateral agreement, such benefit would be captured by the tax policy of the investor's country of residence. The income which the government has spared through its incentive legislations may thereby flow, not to the investor directly, but to the government of the country of the investor's residence.

Double Taxation vs. Multiple Taxation

- The two are NOT the same but interwoven.
- In "Multiple Taxation", one is talking about specific tax legislation, which may be many in number;
- Whereas in "Double Taxation" focus is is on the impact of tax(es) on income/profit

Double taxation

Double taxation may be domestic i.e where taxes are imposed within a country by different taxing authorities (e.g. in Nigeria – Federal, State, Local Govt.) or international i.e. where taxes are imposed by different sovereign states.

Types of Double Taxation

IBFD: Double Taxation is traditionally divided into two kinds;

- Juridical Double Taxation, and
- Economic Double Taxation

- **Juridical double taxation** may be described as the imposition of comparable taxes by two (or more) tax jurisdictions on the same taxpayer in respect of the same taxable income

- **Economic double taxation** may be described as the imposition of comparable taxes by two (or more) tax jurisdictions on different tax payers in respect of.

Tax Treaty-(Avoidance of Double Taxation Agreement)

- Tax treaty is an agreement reached between two countries on a bilateral basis to prevent double taxation (taxes levied twice on the same income, profit, capital gain or other item) or fiscal evasion.

- In some countries they are also known as double taxation agreements, double tax treaties, or *tax information exchange agreements* (TIEA).

Explanatory Notes - **FORCE OF ATTRACTION**

FORCE OF ATTRACTION

- This principle is an anti-avoidance provision to counter the split of profits through the creation of several PEs or Sales Outlets within a jurisdiction.
- Under the principles, the activities in these other sales outlets would be regarded as being attracted to those of the main PE and the profits would be aggregated for tax purposes in as much as the products or activities are the same as, or similar to, those effected through the main PE.
- Article 7 (UN Edition or Nigerian Edition) "The profits of an enterprise may be taxed in the other State but only so much of them as are attributable to:
  - that permanent establishment;
  - sales in that other State of goods or merchandise of the same or similar kind as those sold through that permanent establishment; or
  - other business activities carried on in that other State of the same or similar kind as those effected through that PE"

Objectives or Benefits of Tax Treaty

- Certainty of Taxing Rights between the two Contracting States;
- Avoidance of double taxation;
- Elimination of double taxation;
- Assists investors on investment decisions
  - Certainty of tax treatment
  - Grant of tax treaty relief
  - Lower compliance cost
- Prevention of fiscal evasion;
- Cooperation in tax matters, through:
    - exchange of information
    - non-discrimination- to ensure that non-residents are not unfairly discriminated against
    - mutual agreement procedure – including steps to be taken in time of dispute or conflicts
- Revenue generation – for each Contracting State to get a reasonable share of tax from international business

List of Nigeria Tax Treaty Partners

To date, Nigeria has concluded Agreements with the Following countries:

- United Kingdom and Northern Ireland,
- France,
- Netherlands,
- Canada,
- Belgium,
- Romania,
- Pakistan,
- China
- South Africa.
- Italy (Transportation only)

Treaties duly negotiated which are presently under ratification /domestication are South Korea, Spain, Sweden Russia, Mauritius, Denmark and Algeria