THE NIGERIAN SME AND THE FINANCE ACT 2023

Practical Implications of the Finance Act 2023 for Small and Medium Enterprises (SMEs) in Nigeria

Due to the peculiar challenges that many Small and medium Businesses (SMBs) or Small and Medium Enterprises (SMEs) encounter, resources are scarcely available for necessary allocation to proper tax / financial planning and for necessary professional advice/ guidance in carefully accessing the potential impacts of tax law updates on various aspects of the SME business operations.

The intention for this write-up is therefore to present the new changes to Nigerian tax laws as brought about by the Finance Act 2023 in simple straightforward language, as they will impact the everyday SME business in Nigeria.

In 2020, for the first time since Nigeria's return to democratic rule in 1999, President Muhammadu Buhari's administration introduced the Finance Act 2019, a fiscal policy tool to complement the 2020 Budget as a means of raising tax revenues to fund the budget. The Administration promised to maintain/ continue the culture of issuing such Finance Acts to accompany Nigeria's annual budgets throughout its tenure. This Finance Act (to be cited as the Finance Act 2023), the fourth of such issues since 2020, was signed into law by Former President Buhari on 28 May 2023, the eve of his handover to a new Administration. According to the Act, its provisions are to take effect from 1 May 2023.

The Federal Inland Revenue Service (FIRS), however, through its Public Notice of 10 June 2023, granted an extension of effective dates of certain provisions of the Act on taxes under its purview (specifically, provisions that are not in favor of or represent disincentive to taxpayers) to 1 July 2023, possibly to ameliorate the tax burden of those new provisions.

Changes in Tax Laws

Here are the Amendments to the Tax Laws by the Finance Act 2023 as they would impact Nigerian SMEs:

01.

Increase in Tertiary Education Tax (TET) Rate to 3%:

Incorporated SMEs (not enterprises/ business names) will now pay 3% of their assessable profits as tertiary education tax obligations, instead of 2.5%. (Note that this is the 2nd increase on this tax rate in 2 consecutive years, from the 2% rate that had applied for years before 2021). According to the FIRS' Public Notice of 10 June 2023, this is to apply only to TET becoming due in respect of accounting period ending on or after 1 July 2023. This means that all tax returns due from now to 31 December 2023 will apply TET at 2.5%.

02.

Excise Duty to Apply on all Services:

Excise duty (at a rate to be specified by the President) will now apply on all services rendered by SMEs. This will apply as a separate tax, in addition to Value Added Tax (VAT).

03.

Capital Gains Tax to Apply on Disposal of Digital Assets:

SMEs making gains from disposal of any digital asset (which by dictionary definition includes cryptocurrencies, digital currency, digital tokens, digital securities, digital data, digital documents, digital collectibles and intellectual property such as eBooks, music, videos, software, patents, trademarks or copyrights) will now pay capital gains tax at 10% on such gains made from disposal of these assets. For SMEs that had been paying Income Taxes at 20% to 30% on any gains from disposal of these assets in the ordinary course of their businesses, this review is a welcome development since the effective tax rate on such gains will now reduce to 10%.

04.

Roll-over Relief to be Granted on Disposal and Immediate Re-acquisition of Stocks and Shares:

SMEs will enjoy roll-over relief (meaning that gains on disposal will not be taxed immediately if they are re-invested in the same class of asset) on disposal of stock and shares provided that the proceeds from such disposals are reinvested within the same tax year in the acquisition of eligible shares in the same or other Nigerian companies.

Please note that SMEs whose business activities consist in chiefly trading in shares and stock may be subjected to tax under companies' or personal income tax act, and consequently such roll-over relief will not apply.

05.

Investment Allowance no Longer to be Granted on New Acquisitions of Plant & Machinery:

Incorporated SMEs will no longer enjoy a one-off tax allowance of 10% on new acquisitions of plant and machinery known as Investment Allowance.
According to the FIRS' Public Notice of 10 June 2023, this stoppage of allowance is to apply only to tax returns becoming due in respect of accounting period ending on or after 1 July 2023. This means that all tax returns due from now to 31 December 2023 will still enjoy this allowance.

06.

VAT Adjustments to Apply on Artificial Transactions with Related Parties:

SME Transactions with related party(ies) that may have VAT implications will be thoroughly reviewed by the tax authority to ensure that such transactions are carried out on arm's length pricing basis. Where it is found that arm's length pricing has not been applied on such transactions, and VAT liabilities are deemed to have been reduced as a result, the Federal Inland Revenue Service may make VAT adjustments/ assessments to recover such VAT short paid or under declared.

07.

Portion of Deferred Annuity Withdrawn Within 5 years of Premium Payment will not Qualify for Personal Income Tax Exemption:

Any amount paid as premium by an individual during the preceding year of assessment in respect of own life or the life of a spouse, or contract for a deferred annuity will be tax deductible provided that any portion of a deferred annuity withdrawn within 5 years of paying the premium will be taxed at the point of withdrawal.

08.

New Rules for Importers:

Importers of goods should note the following -
i. In addition to customs duties, an additional levy of 0.5% will now be imposed on all eligible goods imported into Nigeria from outside of Africa.
ii. Where SMEs purchase goods from an online platform (or foreign website) for import into Nigeria, and they have paid VAT on checkout, they should ensure to collect from the online seller of the goods, proof that the seller has been appointed as agent of the FIRS for the collection of VAT, also collate other necessary purchase documents in order to be exempted from paying VAT again at the point of clearing those goods in Nigeria.

09.

Structures Removable from Land will No Longer Qualify as 'Building' for VAT Exemption Purposes:

SMEs that engage in real estate related transactions should note that VAT will apply on sale of 'building', where such 'building' is substantiated to be a fixture or structure that can easily be removed from the land, such as radio and television masts, transmission lines, cell towers, vehicles, mobile homes, caravans and trailers.
According to the FIRS' Public Notice of 10 June 2023, this provision is to become effective from 1 July 2023.

General Business Implications of the New Changes in Tax Laws for Nigerian SMEs

The tax law changes in Nigeria can have significant implications for small and medium-sized businesses (SMBs). Here are some potential implications:

1. **Increased Tax Compliance Burden**: The changes in tax laws may result in increased tax compliance obligations for SMBs. They may need to adapt their tax processes, update their systems, and ensure accurate calculations and reporting to comply with the amended regulations. This can place an additional administrative burden on SMBs, requiring them to allocate more resources to tax compliance.

2. **Need for Updated Tax Technology:** SMBs that rely on tax technology solutions may need to update their software or systems to incorporate the changes in tax rates, deductions, and reporting requirements. This may involve investing in new tax software, upgrading existing systems, or seeking support from tax technology service providers. The cost of acquiring and implementing tax technology solutions can be a consideration for SMBs with limited budgets.

3. **Impact on Cash Flow:** Changes in tax laws, such as the increase in the Tertiary Education tax rate for companies, can directly affect the cash flow of SMBs. The higher tax rate may reduce the funds available for investment, expansion, or day-to-day operations. SMBs need to carefully assess the impact of the tax law changes on their cash flow and make necessary adjustments to their financial planning.

4. **Accounting and Bookkeeping Adjustments:** SMBs may need to update their accounting and bookkeeping practices to accurately capture and track the changes in tax rates, deductions, and exemptions. This includes ensuring proper record-keeping, reconciling tax accounts, and generating accurate financial statements. Adjustments to accounting processes may require additional training or assistance from accounting professionals.

5. **Potential Competitive Disadvantage:** Depending on the industry, SMBs may face increased competition from larger companies that have the resources and capabilities to adapt quickly to the tax law changes. SMBs should proactively evaluate the impact of the changes on their competitiveness, adjust their strategies accordingly, and explore available tax planning opportunities to maintain their market position.

6. **Tax Planning and Advisory:** SMBs may need to seek professional tax planning and advisory services to navigate the complexities of the amended tax laws. Engaging tax consultants or accountants can help SMBs identify tax optimization strategies, maximize deductions, and ensure compliance with the new regulations. However, the additional costs associated with such services may need to be considered by SMBs with limited financial resources.

7. **Potential for Penalties and Risks:** Failure to comply with the amended tax laws can expose SMBs to penalties, fines, or legal consequences. SMBs need to stay updated on the changes, understand their obligations, and implement effective tax compliance measures to mitigate risks. Proactive tax planning and engaging with qualified tax professionals can help SMBs minimize the risk of non-compliance and associated penalties.

8. **Impact on Pricing and Business Models:** Changes in tax laws, particularly those related to VAT or import levies, can influence the pricing strategies and business models of SMBs. SMBs may need to evaluate their pricing structures to account for the revised tax rates and charges, ensuring they remain competitive while still covering the additional tax costs. Adjustments to pricing strategies may require market research, financial analysis, and potentially renegotiating contracts or agreements with customers or suppliers.

As the tax law amendment has become a yearly occurrence in Nigeria, it is now crucial for SMEs, despite their scarce resources, to proactively continue to assess the implications of the tax law changes, seek professional advice when needed, and allocate reasonable resources to ensure compliance with the amended regulations. Adapting to the changes may require careful financial planning, leveraging tax technology solutions, and considering the potential impacts on various aspects of their business operations.

Click here to view or download the full copy of the Finance Act 2023.

For enquiries about how these changes might affect your business, tax strategies and risk mitigation plans to adopt or the tax technology updates your business may require in order to proactively align with or manage the new changes, do not hesitate to contact us via email – clients@vi-m.com.