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TAX UPDATE:

WITHHOLDING TAX RATES ON DIVIDEND, INTEREST AND ROYALTY PAYMENT TO RESIDENTS OF NIGERIA TREATY PARTNERS

Introduction

In 1999 the Federal Government of Nigeria ("FGN"), in its budget statement, indicated that a recipient of interest, dividend and royalty income who is resident in a country with which Nigeria has an effective Double Taxation Agreement ("DTA") will pay withholding tax ("WHT") at the rate of 7.5% where such income is derived from Nigeria. On the basis of the statement, Nigerian resident payers of interest, dividend and royalty to treaty beneficiaries have been implementing a uniform WHT rate of 7.5% on such passive incomes made to such non-resident beneficiaries, whereas the maximum WHT rate specified in the relevant domestic tax laws remains at 10%.

As of 1999, Nigeria had operational DTAs with ten countries, namely the United Kingdom, France, Canada, Belgium, the Netherlands, Pakistan, Czech, Slovakia, Romania, and Italy. The treaty WHT rates in these DTA's are 12.5% for dividends, where the recipient controls at least 10% of the voting power of the Nigerian company paying the dividend, and 15% in all other cases; and 12.5% for interest and royalty payments. Nigeria has since 1999 signed additional DTA's with other countries including China, South Africa, Singapore, Spain, Sweden, the Philippines, all of which are currently in force. Except for China and Singapore, which apply a flat WHT rate of 7.5% to dividend payments, and the Philippines which applies a flat WHT rate of 10% on dividends, the treaty WHT rates for dividends under the post 1999 DTA's is 7.5% for dividends where the recipient controls at least 10% of the voting power of the Nigerian company paying the dividend, and 10% in all other cases. The WHT rate for interest and royalty payments under the post 1999 DTA's is 7.5% except for the Philippines which applies a WHT rate of 10% on interest payments.

In a circular published by the Federal Inland Revenue Service ("**FIRS**") titled "Information Circular on the Claim of Tax Treaties Benefits and Commonwealth Tax Relief in Nigeria" dated 11th May, 2022 (the "**Circular**") and a public notice titled "Public Notice on Application of Withholding Tax on Dividends, Interest and Royalties paid by Residents of Nigeria and Beneficially Owned by Residents of Treaty Partners of Nigeria Under the Double Taxation Agreements Between Nigeria and other Countries" (the "**Notice**"), the FIRS has stated that the Minister of Finance, Budget and National Planning has now approved the discontinuation of (a) the unilateral application of the 7.5% WHT rate and (b) the uniform application of a WHT rate of 7.5% on dividend, interest and royalty payments to treaty beneficiaries. On the basis of this discontinuation, with effect from 1st July, 2022 ("Effective Date"), the relevant WHT rate specified in Nigeria's domestic tax laws will now apply. The Circular and the Notice are to give effect to the ministerial approval. Although the Circular covers other treaty benefits, this update will focus on the application of the Circular and the Notice to WHT rates on interest, dividends and royalties.

The FIRS' justification for the reversal of the existing practice (which is based on the 1999 policy statement) is that the policy statement of the FGN on unilateral reduction of WHT rate to 7.5% was not promulgated into a law and published in the Official Gazette of the FGN. As a result, there was no reduction or any form of amendment to the tax laws on the WHT rates applicable in Nigeria to residents of Nigeria's treaty partners. In addition, the FIRS further stated that protocols were not executed between Nigeria and the treaty partners to effect a reduction in the WHT rates specified in the relevant DTAs to give effect to the policy statement.

Summary of the Circular and Notice regarding WHT on Interest, Dividends and Royalties

The FIRS states in the Notice that, from the Effective Date, the WHT rate of 10% specified in Nigerian domestic tax laws will apply on dividend, interest, or royalty payments to treaty beneficiaries. Where, however, the rate specified in the domestic tax law exceeds the maximum rate specified in the applicable DTA, the maximum rate specified in that DTA will apply. Consequently, from the Effective Date, in line with the provisions of the relevant DTA and those of Nigerian domestic tax laws, the following WHT rates shall apply on dividend, interest and royalty payments by residents of Nigeria to (and beneficially owned by) residents of DTA partners and the current application of a uniform WHT rate of 7.5% will cease to apply.

No.	Country	Dividend		Interest	Royalties	
		Company with voting powers of 10% and above	All others		Payment to Companies	Payment to Individuals
1.	Italy	10%	10%	10%	10%	5%
2	United Kingdom	10%	10%	10%	10%	5%
3	Belgium	10%	10%	10%	10%	5%
4	Pakistan	10%	10%	10%	10%	5%
5	Czech Republic	10%	10%	10%	10%	5%
6	Slovak Republic	10%	10%	10%	10%	5%
7	France	10%	10%	10%	10%	5%
8	Netherlands	10%	10%	10%	10%	5%
9	Romania	10%	10%	10%	10%	5%
10	Canada	10%	10%	10%	10%	5%
11	South Africa	7.5%	10%	7.5%	7.5%	5%
12	China	7.5%	7.5%	7.5%	7.5%	5%
13	Philippines	10%	10%	10%	10%	5%
14	Singapore	7.5%	7.5%	7.5%	7.5%	5%
15	Sweden	7.5%	10%	7.5%	7.5%	5%
16	Spain	7.5%	10%	7.5%	7.5%	5%

The above treaty WHT rate cap is only applicable in Nigeria when payments are made to non-residents and the payments are not connected to a permanent establishment that the non-resident has in Nigeria. The FIRS stated in paragraph 7 of the Notice that it has withdrawn all previous rulings, directions or approval which it had given in relation to the applicable WHT rate with respect to all the DTAs.

From the Effective Date, interest or royalty payments to beneficiaries who are resident in China, South Africa, Singapore, Spain and Sweden will remain at the reduced WHT rate of 7.5%. For dividend payments due to recipients resident in China and Singapore, the applicable WHT rate will also remain 7.5%. On the other hand, the WHT rate on dividend payments to recipients who are resident in South Africa, Spain, and Sweden will generally be 10% but will only reduce to 7.5% if the recipient holds at least 10% of the share capital of the Nigerian company making the payment. The continued application of the reduced WHT rate of 7.5% for residents of these countries is because the relevant DTAs contain a maximum WHT rate which is lower than that specified under Nigerian domestic tax laws.

With respect to residents of countries with a WHT rate that is higher than that specified under Nigerian domestic tax laws, the lower rate of 10% specified in the domestic tax laws will apply.

What would happen from the Effective Date?

From the Effective Date, Nigerian companies that pay dividend, interest or royalty to treaty beneficiaries will have an obligation to implement the changes introduced by the Circular and apply the relevant WHT rate and remit the tax withheld to the FIRS. Failure to do that could cause the FIRS to impose the penalties specified in the domestic tax laws on defaulters.

Conclusion

Based on our reading of the DTAs and the domestic tax laws, the change in the FGN's position is not necessarily an increase in the WHT rate applicable to treaty beneficiaries. Rather, it is a withdrawal and discontinuation of the incentive of 2.5% reduction in the WHT rate for treaty beneficiaries which was not passed into law or implemented by way of a protocol between Nigeria and the relevant countries. Therefore, unless there is a subsequent change in the position of the FGN, it is unlikely that the reversal will be suspended.

The changes introduced by the Circular will apply to all existing transactions (such as lending, investment in debt instruments (excluding those issued by the FGN), equity investments etc), and to future ones. The implementation will bring the tax cost of borrowings by Nigerian residents from treaty lenders (excluding lenders resident in China, South Africa, Singapore, Spain, and Sweden) to that of non-treaty lenders. The reduced rate of 7.5% will continue to apply to interest payments on loans obtained from lenders, and investments in debt instruments by persons, resident in China, South Africa, Singapore, Spain, and Sweden. Lastly, the reversal has no impact on the application of gross up provisions in loan documents as such provisions remain valid and enforceable.

This update is for general information purposes only and does not constitute legal advice. If you have any questions or require any assistance or clarification on how this update could apply to you or your business or require litigation advice on any aspect of the Nigerian laws, please contact taxteam@uubo.org.