



# ‘Pioneer Status’ Tax Incentive in Nigeria:

## A Commentary on Recent Developments and Implications for Businesses

Regulatory Alert | by Chuks Okoriekwe (Originally published by *ThisDay Lawyer* 12<sup>th</sup> September, 2017, p.7)

### Introduction

On 2 August 2017, Nigeria’s Federal Executive Council (FEC) reviewed the list of “pioneer industries and pioneer products” (Pioneer List), drastically affecting the potential tax treatment of subject sectors and products. This culminated in the issuance of the **Application Guidelines for Pioneer Status Incentive (AGPSI), 2017** by the Ministry of Industry, Trade and Investment (MITI). A pleasant surprise was the inclusion of the creative industry (film and music) amongst the 27 new additions to the Pioneer List, in line with government’s promise to further encourage a sector that was created out of resilience of practitioners; Nollywood’s giant strides is symbolic of how the industry has put Nigeria in global reckoning. With more support, it would definitely be more impactful.

Pioneer status was introduced retrospectively (to 1970) in 1971 vide the **Industrial Development (Income Tax Relief) Act (IDITRA), Cap. 17 LFN, 2004. Section 1** IDITRA grants the President the power to declare as “pioneer industries and pioneer products” any “industry which is not being carried on ... on a scale suitable to the economic requirement of Nigeria or at all, or there are favourable prospects of further development ... of any industry; or it is expedient in the public interest to encourage the development or establishment of any industry ... by declaring the industry to be a pioneer industry and any product of the industry to be a pioneer product.” The resulting Pioneer List may be varied from time to time, especially pursuant to application for inclusion (**section 1(2) IDITRA**)).

Inclusion of industries or products in the Pioneer List confers eligibility on applicants for Pioneer Status Incentive (PSI); applications being through the Nigerian Investment Promotion Commission (NIPC) the investment promotion/facilitation agency of government. However, the previous administration was widely regarded as abusing the PSI regime, for

example by granting PSI to upstream companies subject to **Petroleum Profits Tax Act (PPTA)** whilst IDITRA (e.g. sections 13-16, 19,20) contemplates applicability to only companies governed by **Companies Income Tax Act (CITA)**. Indeed, IDITRA defines CITA as the principal Act (**section 25**). Another example of abuse was the single grant of five year PSI, instead of three years in the first instance, and subject to meeting stated conditions, either a two year renewal or two one year renewals totalling maximum five years in either case (**section 10 IDITRA**). Consequently, the Buhari administration suspended PSI processes in September 2015 with a view to fine tuning them to align with FG's strategic intents.

The August 2017 resumption of PSI is a facet of the Federal Government (FG)'s Economic Recovery and Growth Plan (ERGP) which amongst other things, emphasizes diversifying revenues. Would this initiative be a springboard to help reflate the economy by attracting investments? In this regulatory alert, we look at the implication of the review on companies willing to take advantage of the new PSI regime and grey areas in the application process/requirements.

### Pioneer Status Incentive (PSI) in Nigeria

Under CITA, companies are liable to pay income tax at 30% on profits accruing in,





derived from, brought into or received in Nigeria. However, to stimulate investment in, and growth of target industries and products, promote transfer of technology and develop local production, the President through MITI can grant PSI, (being essentially tax holidays) to companies in sectors represented on the Pioneer List (**section 10 IDITRA**).

In addition to the IDITRA, PSI is also governed by **NIPC Act, Cap. N117 LFN, 2004, Pioneer Status Incentive Regulations (PSIR), 2014** and **Application Guidelines** issued by the Minister/NIPC from time to time. Successful applications for PSI results in the Pioneer Company (PC) being issued a Pioneer Certificate (PCert) which would reflect terms of the PSI; the details are also publishable in the Gazette (**sections 1,3, 9 IDITRA**).

IDITRA prescribes tax free dividends to shareholders of PCs (**section 17**); the tax relief period commences on the “production day” of the PC (production date, equivalent to commencement of the pioneer enterprise's commercial operations, must be certified by regulator); special commencement and cessation rules apply and any other trade or business apart from the pioneer enterprise shall be reported separately

and taxable in the regular manner under CITA; capital expenditure on assets acquired during the tax holiday shall for the purposes of capital allowances be deemed to have been incurred on the day after end of the holiday; same treatment is applicable to losses during the holiday (**sections 10,11, 14 IDITRA**).

PCs are subject to restrictions. For example, they cannot grant loans without prior ministerial consent (to ensure adequate security and reasonability of interest), and must comply with dividend accounting/distribution requirements (**section 18 IDITRA**). **Section 7 IDITRA** stipulates that a PC in default of these provisions may be liable to cancellation of its PCert or restriction of its tax relief period by the President pursuant to ministerial recommendation. Upon cancellation, the PC would be liable to pay income tax on all its profits as prescribed under CITA.

### **PSI: Path to Economic Recovery and Growth?**

Given the need to fund FG's deficit budget, could the MITI's move to enlarge the Pioneer List and potentially issue more PSIs as a double-edged sword? A preliminary point is that the newly issued (sixteen page) **AGPSI** provides a lot of clarity on PSI procedural

requirements and also contains easy to follow graphical representation (pages 7 and 8), in addition to outlining the roles of various agencies/authorities during the process. In this regard, the **AGPSI** is a major improvement over the **PSIR** (issued in 2014), which sought to “provide policy clarification, consistency and transparency in applying for” PSI. Whilst the **PSIR** was gazetted, the **AGPSI** appears to be ungazetted as at date, albeit that should not affect its effectiveness.

Whilst the clarity objective of these procedural requirements are commendable, there seeming conflicts with some provisions of **IDITRA** (especially **section 2 IDITRA** on “mode of application for pioneer certificate, etc., and fee payable”), even if the former tries to bring discipline and alignment to the PSI regime.<sup>1</sup> The question of supremacy between legislative provision and subsidiary legislation arises (**AGPSI** and **PSIR** were made pursuant to **NIPC Act** and **IDITRA** respectively). Another issue is that there are a few 'internal inconsistencies' between **AGPSI** and **PSIR**; which conflicting provision should prevail?

One key consideration for grant/subsequent renewal of PSI is that: “an applicant must demonstrate the tangible impact its activity (project) will have on Nigeria's economic diversity and growth, industrial and sectoral development, employment, skills and technology transfer, export development and import substitution” (**Guideline 3.1.5, AGPSI 2017**). By **Guideline 3.18 AGPSI**, a PC has an obligation to submit a performance report to NIPC annually for monitoring and evaluation. On its own, **Regulation 11 PSIR**, requires NIPC to carry out periodic impact assessment and evaluate the utilization of the savings accruing from the incentives. The **PSIR** placed the obligation on NIPC whilst **AGPSI** shifts the obligation to PCs.<sup>2</sup> This is not necessarily contradictory, but means that both the PC and regulator are to be mindful of the cost-benefit analysis of PSI from slightly different perspectives.

### **Race for PSI: 100 Meter Dash or 100 Meter Hurdles?**

Obviously PSI is not for all comers. Apart from sectoral or product eligibility, there is also “age” or obsolescence

<sup>1</sup>Whilst **section 2(4) IDITRA** provides for N100 application fee (obviously this no longer reflects current realities and should be repealed), the new PSI regime provides for application and due diligence fees as well as service charges (service charge being a percentage of tax savings to be enjoyed by the PC). **Section 2(1) IDITRA** empowers the Minister to specify the form of application for PSI, and could be regarded as the basis for **AGPSI**, which may also be seen as an upfront application of **section 2(5) IDITRA** empowering him to require applicants furnish further particulars as he may consider necessary, to enable the President consider their application. **AGPSI** may therefore be regarded as an attempt to drive efficiency in PSI application process, by providing detailed guidance to obviate queries or requests for further information/documents. For example, there is a presentation template which elicits information necessary for considering the application; these could have a streamlining effect ultimately and guide against deluge of applications/help focus regulatory consideration on only meritorious applications. These may be considered beneficial, because they amplify the stipulations in **section 2(a) - (g) IDITRA**.

<sup>2</sup>Per **Guideline 4.1.3 AGPSI**, PC's default of its reporting obligation after two reminders by NIPC shall result in the cancellation of the PCert, delisting from PSI beneficiaries on NIPC's website and notification to Federal Inland Revenue Service (FIRS) for the purpose of collection of tax for the unexpired period including the period of non-compliance.

<sup>3</sup>See also **Guideline 3.1.1 AGPSI** which provides along the same lines: “An applicant must make a new application in the first year of production/service and must apply for an extension no later than one month after the expiration of the initial tax relief period of three years or an extension of one year.” Also, **Regulation 3(4) PSIR** that applications for PSI be submitted within first year of commercial production.

considerations – it is geared towards start-ups, hence “production day” provisions in *IDITRA*.<sup>3</sup>

Capital threshold requirements for applicants also raise questions. Whilst *PSIR (Regulation 3(1)(b))*, stipulates that *PSI* applicants must have incurred capital expenditure of more than N10 million, *AGPSI’s Guideline 3.1.3* prescribes non-current tangible asset of over N100 million. If *AGPSI* requirements were to prevail (being later in time), it means a narrower pool of eligible applicants;<sup>4</sup> and there are sound policy reasons for doing so. Another issue of potential conflict is the applicable *PSI* regulatory fees (application and processing fees, service charge).<sup>5</sup> Even if divergence on quantum is an issue, service charge is a welcome attempt to make the administration of *PSI* pay for itself.

As noted earlier, *PSIR* was made by the *NIPC*, pursuant to **section 30 *NIPC Act*** whilst *AGPSI* was issued by the Minister pursuant to **section 2 *IDITRA***. This raises the issue of supremacy and validity; *MITI* supervises *NIPC* and *NIPC’s* actions are presumed to have the blessing of the supervising Minister. The Minister and *NIPC* - both being donees of delegated legislation by substantive Acts, must *NIPC’s* Regulations necessarily be deemed inferior to the Minister’s? The matter is further complicated by the fact that *NIPC Act* was enacted in 1995, whilst *IDITRA* (enabling provision for *AGPSI* issued by the Minister) was enacted in 1971.

A compromise would be to argue that non-conflicting *PSIR* provisions, remains valid. The *MITI/NIPC* may need to further review the application requirements and make clarifications for proper direction of potential applicants. We also note the practical impossibility of *AGPSI* expressly

repealing/amending *PSIR* because of the difference of donees of delegated legislation (Minister/*NIPC*) and of enabling legislation (*NIPC Act/IDITRA*), respectively.

In our experience (and despite credible basis for reservations as discussed above), it would be prescient for applicants to proceed on the basis of the *AGPSI*, which by the way stipulates application process for *PSI* and renewals would take 25 and 15 weeks, respectively. This is a welcome departure from previous practice and is in tandem with *FG’s* move to improve public sector service delivery as a factor to enhancing ease of doing business in Nigeria.<sup>6</sup>

### Conclusion

*FG’s* expansion of the Pioneer List is a welcome development, given the drive to widen the tax net and implement its *ERGP*. The transformation of Nigeria’s telecommunications and cement industries is axiomatic that tax incentives *can contribute* to sectoral growth with significant positive effects for the economy. It could not however be overstressed that ultimately, the greatest attraction for investment is an enabling business environment, and it is heart-warming that *MITI* has accepted the challenge to champion improvements in Nigeria’s ease of doing business.

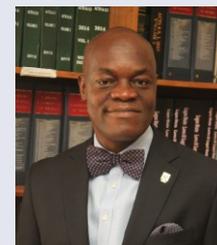
*MITI/NIPC’s* antecedents and dynamism so far exhibited, portends a positive outlook regarding administration of the new *PSI* regime. A noteworthy innovation is the commitment to publish revised Pioneer List biennially (***Guideline 2.4 AGPSI***). Hopefully, the grey areas of conflict with the *PSIR* would be addressed by the *MITI* for seamless application process.

### About LeLaw

We are a niche commercial law firm and are passionate about Nigeria. We help clients – Nigerian and multinationals – succeed in their markets and make positive, enduring impact in their communities. Leveraging our deep Nigerian regulatory and multifaceted sectoral expertise, we assist foreign clients optimise their Nigerian strategy throughout the investment cycle – entry, growth and exit.

For further details, visit our website: [www.lerlawlegal.com](http://www.lerlawlegal.com).

You may also visit the *Thought Leadership* page of our website for interesting and insightful commercial law and Nigerian regulatory articles.



[a.elebiju@lerlawlegal.com](mailto:a.elebiju@lerlawlegal.com)



[c.okoriekwe@lerlawlegal.com](mailto:c.okoriekwe@lerlawlegal.com)

<sup>3</sup>This portends exclusion of small companies - defined by **section 351 *Companies and Allied Matters Act (CAMA), Cap. C20 LFN, 2004*** as having not more than N1 million net asset.

<sup>4</sup>**Regulation 5 *PSIR*** provides for 2% service charge, whilst the flow chart in **Guideline 3.2.6 *AGPSI*** references payment of 'service charge deposit' within a week of applicant being notified of *NIPC’s* decision after *NIPC’s* due diligence. **Guideline 4.2.1 *AGPSI*** provides that “the applicable *NIPC* service fee schedule shall be made available on the websites of *FMITI* and *NIPC*.” It appears that (as at 25<sup>th</sup> August 2017), the list is yet to be uploaded. Under the *PSIR*, an approval letter shall be issued to an applicant upon presentation of evidence of payment of 2% service charge, **Regulation 8 *PSIR***. The service charge payable is to be calculated from the applicant’s estimated tax savings from *PSI*.

<sup>6</sup>The Acting President signed an Executive Order (EO) to concretise these steps in May 2017. It prescribes a default approval regime in terms of its Paragraph 3: “where the relevant agency or official fails to communicate approval or rejection of an application within the time stipulated in the published list, all applications for business registrations, certification, waivers, licenses or permits not concluded within the stipulated timeline shall be deemed approved and granted.”