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Capital allowance claim by companies – Should taxpayers complain? (1)

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The crisis of dwindling revenue from crude oil has pushed emphasis on maximizing collection of non-oil revenue from mere lip service to center stage in the financial/revenue planning by the government of Nigeria. The most significant non-oil revenue source is the taxes of individuals, partnerships, companies and other forms of taxpayers.

The structure of Nigeria's tax laws reflects a level of quid pro quo by Government. The provisions, as exacting as they are, show that it is not only about what must accrue to government but also what government is prepared to give up to encourage taxpayers in the certain obligation to pay tax.

Thus, the tax codes allow tax payers to claim certain benefits in relation to their business investments in the country as well as reduce the certain tax burdens which they would have borne, were such provisions not available. One of such provisions is the right of the taxpayer to claim capital allowance[1] on qualifying capital expenditures as provided in the Companies Income Tax Act (CITA), Personal Income Tax Act (PITA) and Petroleum Profits Tax Act.

The Second Schedule to CITA sets the legal basis for the claim of capital allowances by companies. Specifically, Paragraph 24 of the Schedule makes provisions for the manner in which capital allowances and charges can be made. Subparagraph 2 of Paragraph 24, provides for capital allowance to be made to a Company, from the remainder of its assessable profits[2] for the year of assessment for which the allowance is due.

However, over the years, some of the provisions of the Second Schedule have generated controversies between the taxpayers and Federal Inland Revenue Service (FIRS) especially on their interpretation and implementation. These provisions (it would appear) have, in certain

circumstances, defeated the purpose for which capital allowances were introduced. Few of such controversies are highlighted below:

The conditions for granting capital allowance

The Second schedule provides conditions under which a company is qualified to claim capital allowance. Such conditions include:

- the tax payer making such claim must own the fixed asset; and
- the fixed asset must be used for the purpose of a trade or business and must be in use at the end of the period for which the tax is being computed.

However, in practice FIRS also request taxpayers to provide Certificate of Acceptance on Fixed Assets (CAFA) obtained from the Industrial Inspectorate Division (IID) before they can be allowed to claim capital allowances on those assets. Often times the taxpayer would have satisfied the conditions provided in the Second Schedule as noted above yet may not be granted the claim of capital allowance by FIRS. This therefore raises the question of whether FIRS is right to deprive a taxpayer the right to make claim of capital allowance on the basis that the company could not provide the CAFA.

The Industrial Inspectorate Act (IIA) Cap I8, LFN 2007, requires a company who incurs N500,000 and above in the acquisition of fixed assets in each assets category to obtain a CAFA from the IID of the Federal Ministry of Industries. The IIA however does not provide that the CAFA should be used as a basis for the grant of capital allowance by the tax authority. Thus, the basis of insistence by FIRS on the provision of CAFA by taxpayers requires further and better clarification. The fact that FIRS would still request the taxpayer to provide documentary evidence of purchase of the fixed assets in the event of an audit may be tantamount to duplication of efforts and inefficient use of the taxpayers' resources especially if there is no clear justification to impeach the CAFA ex facié.

It would be expedient if the two relevant agencies can adopt a more congruent approach to verify fixed assets acquired by companies in order to ease concerns of taxpayers.

Dividend tax and minimum tax vs claim of capital allowance

The CITA contains anti-avoidance provisions which seek to bring into the tax net, income that have in some way escaped taxation. Two of such provisions include Section 19 on dividend tax and Section 33 on minimum tax. The conditions for the payments of dividend tax and minimum tax are somewhat similar. The minimum tax is payable where it is higher than the tax computed on the taxable / total profit for the tax year while dividend tax is payable in a year where a company declares dividend and the dividend declared is higher than the total profit of the company for the year in which the dividend is declared.

In both cases, before the total / taxable profit of the taxpayer is determined, it is expected that capital allowances would have been deducted from assessable profits. Therefore, where the taxpayer pays minimum tax or dividend tax, after claim of capital allowances, the capital allowance so deducted is lost. This is obvious when one evaluates the impact of the minimum tax/dividend tax on a company's effective tax rate (ETR). Has the government then frustrated its own grant to taxpayers vide a contrary or contradictory provision?

To be continued

Capital allowance is the allowance granted at specified rates (as provided in CITA) on qualifying capital expenditure and on assets in use for the purpose of the business at the end of the relevant basis period

Assessable profit is the profit calculated after making adjustments for deductions such as expenses and other adjustments from the total income, as permitted by the tax laws.