

# Capital gains tax in nigeria



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Introduction Discussing capital gain tax without first presenting a general overview of the entire concept of taxation will be tantamount to putting a cart before a horse. It is therefore very important that justice be done by explaining taxation and various types of taxes. Taxation: A General overview Tax and taxation has been variously defined by different authors. Oyegbile (1996) defines tax as a sum of money paid by citizens of a country, state or community to the government for public purpose.

According to him taxation is one of the sources of income for government; such income is used to finance or run public utilities and perform other social responsibilities. This implies that anybody that generates income must compulsorily pay taxes. Sanni (2007) define tax in the following ways: \* Tax is a " compulsory levy imposed on a subject or upon his property by the government having authority over him; \* Tax is a universal contrivance; Tax is the price of social security between the government and the governed; \* Tax is the oxygen of every nation, a pre-condition for its prosperity; and \* Tax is an instrument of social engineering A thorough content analysis of the definitions reveals the following fundamentals about tax: ' Tax is a social obligation; it is a civic responsibility and an important source of finance for the government'. Generally, Taxation is of two types viz: Direct and indirect taxation.

Direct taxation: is the case where the person(s) paying is or are asked to pay for no particular service rendered or goods delivered but for the maintenance of government together with its services. Indirect taxation: is paid when one asks for services or supplies of goods. There are different

forms of taxation. But for the purpose of this work, taxes that will be discussed will be limited to taxes that pertain to property. Property taxation includes the following: The value added tax, withholding tax, betterment tax, stamp duties, probate tax, capital transfer tax, severance tax, capital gains tax and site value rating. Value added tax: Value added tax or VAT as it is widely known can be defined as a government levy on the amount that a business firm adds to the price of a commodity during production and distribution of a good. VAT was introduced in Nigeria by the value added tax decree no. 102 of 1993. VAT affect all goods and services produced or imported to Nigeria with few exceptions. VAT paid by a business on purchases is called input tax. On the company's sale it is called output tax.

If the output is greater than input in any single month, the excess is given to the Federal Board of Inland Revenue but where input is greater than the output, the tax payer should be given the excess from the FBIR though in practice this is not always possible. \* Withholding Tax: This tax was introduced in Nigeria by the Finance (miscellaneous taxation provisions), Decree No. 98 of 1979. It is a tax directed on income earned on land, buildings and other identifiable incomes earned from contractual agreement. This tax is collected at the three tiers of government in Nigeria. Betterment Tax: This tax came into effect via the town and country planning law, Cap 130, section 45, subsection 1-3 of 1963. The tax is levied on all beneficiaries of adventitious value on their landed property as a result of public works, development and planning control activities carried out by government. This tax is computed by first determining the open market value before and after the public works. The tax chargeable is 75% of the difference in value before

and after the public works. \* Stamp duties: This is a tax payable on all documents or instruments executed within a country where the tax is applicable.

The stamp duty act of 1958 requires that all instruments executed in Nigeria like conveyance on sale, assignment of land, leases, mortgage and other documents entered into in contractual agreement should be stamped before they can be registered. Such documents must be stamped before they can be tendered as evidence in a court or presented for registration. \* Probate tax: This is the tax paid on the property or estate of a deceased in order to obtain letters of administration of the estate. The chargeable amount is based on the open market value of the estate, as at the date of death of the deceased. Capital transfer tax: This tax is imposed on the capital value of properties transferred. This tax was introduced in nigeria in 1979 via the federal government official gazette No. 18, vol. 66. The law was enacted to curb embezzlement of public funds by private individuals since the bulk of any money stolen will be subjected to heavy taxation when the estate is to be transferred. \* severance tax: This tax is levied on the extraction of natural resources like agricultural produce, forest resources, petroleum and metallic stones e. t. c. his tax is levied to ensure that the benefits from the natural resources which in real sense are God given free gifts of nature are shared by all. \* Capital gains tax: This tax came about as a result of Decree 44 of 1977. It is a tax on the gains which speculators or other property dealers realize on sale of real estate or landed property. \* Site value rating: This is a tax on unimproved capital value of the site. The tax was introduced to

encourage owners of undeveloped land to put them into immediate profitable use. STRUCTURE OF THE NIGERIAN TAX SYSTEM

Taxation is based on laws which invariably turn to figures and finally ends up in paying money to government's purse as a contribution to the provisions of public utilities. The Nigerian tax is structured to reflect the nature of the business. Depending on the type of business, taxes are levied on businesses on an annual basis. This implies that all businesses, organizations and taxable persons are obligated to make a tax return to the Inland Revenue. Profits arising from transactions of companies constitute taxable income following their assessment to tax.

This also includes personal income tax, which is duly imposed on individuals by the relevant tax authority in the territory where the company has its principal office or the place of business on the first day of the year of assessment or year of commencement of business. The state Board of Internal Revenue is responsible for the administration and collection of the relevant tax in while the Federal Inland Revenue is charged with the responsibility of the company and other related taxes. These structures are governed by the Personal Income Tax Act (PITA, 1993) and Company Income Tax Act (CITA, 1994) respectively.

The Nigerian tax system is prudently organized in order to effectively enhance the collection of taxes and reduce the incidence of tax evasion and the subsequent loss of revenue to the government. The tax laws therefore provides for the collection of taxes at source of the taxpayer's income. This is achieved through the Withholding tax system, which allows taxes to be

deducted at the source of income. This is provided in sections 63 of CITA and 72 of PITA; where the laws recommend that income tax assessable on any company, whether or not an assessment has been made, shall if the Board (the relevant tax authority) so directs, be recoverable from any payments made by any person to such company. The income tax recovered under the provisions of the law by deduction from payments made to a company or person is usually set-off for the purpose of collection against tax charged on the company or individual by an assessment. This is however only to the extent that the total of the deductions does not exceed the amount of the assessment and in case of a company, the deduction is limited to the period in which the payment relates.

The Nigerian tax laws provide that where a dividend or such other distribution becomes due from a taxpayer; person or company, payable by a Nigerian company to any other company or to any person, the company paying such dividend or making such distribution shall on the date when the amount is paid or credited, whichever comes first, deducts tax at the rate specified in the Act and shall forthwith pay over to the relevant tax authority the amount so deducted.

**CONCEPT OF CAPITAL GAINS TAX** Capital gains tax (abbreviated: CGT) is a tax charged on capital gains, the profit realized on the sale of a non-inventory asset that was purchased at a lower price. It is a tax on the gains which speculators or other property dealers realize on sale of real estate or landed property. This is calculated yearly and covers all profits coming to a taxpayer from the sale or lease or other transfer of rights which are subject to a capital gain tax. The most common capital gains are realized from the sale of stocks, bonds, precious metals and property.

In many jurisdictions, including the United States and the United Kingdom, a capital gains tax or CGT is charged on capital gains, that is, the profit realized on the sale of an asset that was previously purchased at a lower price. The most common capital gains are realized from the sale of stocks, bonds, and property. Not all countries implement a capital gains tax and most have different rates of taxation for individuals and corporations. Some of the countries that practice Capital gain tax vis-a-vis their modus operandi are discussed below. Capital Gain Tax in United Kingdom

Capital gains tax was introduced into Britain in 1965 mainly as an anti avoidance measure to discourage taxpayers' devises of turning what was really taxable income into free capital gains. Before then, propertied taxpayers were able to earn tax-free income as capital gains while ordinary taxpayers had their earnings taxed as income. Individuals who are resident or ordinarily resident in the United Kingdom (and trustees of various trusts) are subject to a capital gains tax, with exceptions for, for example, principal private residences, holdings in Individual Savings Account (ISAs) or gilts.

Every individual has an annual capital gains tax allowance: gains below the allowance are exempt from tax, and capital losses can be set against capital gains in other holdings before taxation. Individuals pay capital gains tax at their highest marginal rate of income tax (0%, 10%, 22% or 40% in the tax year 2004/5) but since 6 April 1998 have been able to claim a taper relief which reduces the amount of a gain that is subject to capital gains tax (reducing the effective rate of tax), depending on whether the asset is a "business asset" or a "non-business asset" and the length of the period of ownership.

A taxpayer is exempt from CGT on his/her principal private residence.

Certain other gains are allowed to be rolled over upon re-investment.

Investments in some start up enterprises are also exempt from CGT. The

sale of a family business can be exempt from CGT upon retirement.

Companies are subject to United Kingdom corporation tax on their “chargeable gains” (the amounts of which are calculated along the lines of capital gains tax). Companies cannot claim taper relief, but can claim an indexation allowance to offset the effect of inflation.

A corporate “substantial shareholding exemption” was introduced on 1 April 2002 for holdings of 10% or more of the shares in another company (30% or more for shares held by a life assurance company’s long-term insurance fund). This is effectively a form of UK participation exemption. Almost all of the corporation tax raised on chargeable gains is paid by life assurance companies taxed on the I minus E basis. The rules governing the taxation of capital gains in the United Kingdom for individuals and companies are contained in the Taxation of Chargeable Gains Act 1992.

In the Chancellor’s October 2007 Autumn Statement, draft proposals were announced that would change the applicable rates of CGT as of 6 April 2008. Under these proposals, an individual’s annual exemption will continue but taper relief will cease and a single rate of capital gains tax at 18% will be applied to chargeable gains. This new single rate would replace the individual’s marginal (Income Tax) rate of tax for CGT purposes. The changes were introduced, at least in part, because the UK government felt that private equity firms were making excessive profits by benefiting from overly generous taper relief on business assets. The changes were criticised by a <https://assignbuster.com/capital-gains-tax-in-nigeria/>



number of groups including the Federation of Small Businesses, who claimed that the new rules would increase the CGT liability of small businesses and discourage entrepreneurship in the UK. At the time of the proposals there was concern that the changes would lead to a bulk selling of assets just before the start of the 2008-09 tax year to benefit from existing taper relief.

Individuals paid capital gains tax at their highest marginal rate of income tax (0%, 10%, 20% or 40% in the tax year 2007/8) but from 6 April 1998 were able to claim a taper relief which reduces the amount of a gain that is subject to capital gains tax (reducing the effective rate of tax), depending on whether the asset is a "business asset" or a "non-business asset" and the length of the period of ownership. Taper relief provided up to a 75% reduction (leaving 25% taxable) in taxable gains for business assets, and 40% (leaving 60% taxable), for non-business assets, for an individual.

Taper relief replaces indexation allowance for individuals, which can still be claimed for assets held prior to 6 April 1998 from the date of purchase until that date, but was itself be abolished on 2008-04-05. Capital gains tax in the United States In the United States, individuals and corporations pay income tax on the net total of all their capital gains just as they do on other sorts of income, but the tax rate for individuals is lower on "long-term capital gains," which are gains on assets that had been held for over one year before being sold.

The tax rate on long-term gains was reduced in 2003 to 15%, or to 5% for individuals in the lowest two income tax brackets (See progressive tax). Short-term capital gains are taxed at a higher rate: the ordinary income tax

rate. The reduced 15% tax rate on eligible dividends and capital gains, previously scheduled to expire in 2008, has been extended through 2010 as a result of the Tax Increase Prevention and Reconciliation Act signed into law by President Bush on May 17, 2006 (P. L. 109-222). In 2011 these reduced tax rates will “ sunset,” or revert to the rates in effect before 2003, which were generally 20%.

President Obama’s budget, announced on February 25, 2009, calls for the Capital Gains Tax to be reverted to the 20% rate before the Sunset date of 2011. The IRS allows for individuals to defer capital gains taxes with tax planning strategies such as the Structured sale (Ensured Installment Sale), charitable trust (CRT), installment sale, private annuity trust, and a 1031 exchange. The United States is unlike other countries in that its citizens are subject to U. S. tax on their worldwide income no matter where in the world they reside. U. S. citizens therefore find it difficult to take advantage of personal tax havens.

Although there are some offshore bank accounts that advertise as tax havens, U. S. law requires reporting of income from those accounts and failure to do so constitutes tax evasion. Germany Germany has introduced a very strict capital gains tax for shares, funds, certificates etc. in January 2009 (called as Abgeltungsteuer in German). Capital gains tax will only apply to financial instruments (shares, bonds etc) if they have been bought after 31. 12. 2008. Instruments bought before this date are capital gains tax exempt (assuming that they are held for at least 12 months), even if they are sold in 2065 or later, barring a change of law.

Special treatments of certificates, which only qualify for tax exemption if they have been bought before 15. 03. 2007. Real estate will still be free of capital gains tax if held for more than ten years. The German capital gains tax will be 25% plus Solidaritätszuschlag (add on tax to finance the 5 eastern states of Germany - Mecklenburg-Western Pomerania, Saxony, Saxony-Anhalt, Thuringia and Brandenburg - and the cost of the reunification) plus Kirchensteuer (church tax) effectively coming to about 28%.

No deductions of cost like custodian fees, travelling to and from annual shareholder meetings, legal and tax advice, interest paid on loans to buy shares etc. will be allowed any more from 2009 on. Capital Gain Tax in Canada Currently 50. 00% of realized capital gains are taxed in Canada at an individual's tax rate. (ie \$100 CG with 43% tax rate will attract \$21. 50 of tax. ) Some exceptions apply, such as selling one's primary residence which may be exempt from taxation. For example, if your capital gain (profit) is \$100, you're only taxed on \$50 at your marginal tax rate.

That is, if you were in the top tax bracket you'd be taxed at approx 43%.

Formula for this example using the top tax bracket would be as follows:

$(\text{Capital gain} \times 50.00\%) \times \text{marginal tax rate} = \text{capital gain tax} = (\$100 \times 50.00\%) \times 43\% = \$50 \times 43\% = \$21.50$  In this example your capital gains tax on

\$100 is \$21. 50, leaving you with \$78. 50. The formula is the same for capital losses and these can be carried forward indefinitely to offset future years' capital gains; capital losses not used in the current year can also be carried back to the previous three tax years to offset capital gains tax paid in those years.

Unrealized capital gains are not taxed. Capital Gain Tax in South Africa For legal persons in South Africa, 50% of their net profit will attract CGT and for natural persons 25%. This portion of the net gain will be taxed at their marginal tax rate. As an effective tax rate this means a maximum effective rate of 10% is payable and for corporate taxpayers a maximum of 15%. For example, for natural persons the maximum marginal tax rate is 40%.

Assuming the aggregate capital gain for the year of assessment is R50 000, 25% of R50 000 is R12 500, which is taxed at 40%, therefore R5 000 is payable.

The R5 000 as a percentage of the original profit made is 10%. Capital Gain Tax in Nigeria The Capital Gains Tax was introduced in Nigeria in 1967 at a time when the finance of the Federal Government was under severe pressure due to civil war; hence the revenue objective could have been paramount in the mind of the Federal Government. CGT was introduced in Nigeria through the Capital Gains Tax Act of 1967 and it became effective on 1st April 1967. The provisions of this Act are applicable to transactions effected by companies in the same manner as they apply to transactions effected by individuals.

The highlights of the provisions of the CGT Act are: \* CGT is chargeable at 20% on capital gains arising from disposal of capital assets. Capital gains represent mainly the excess of disposal proceeds over the cost of the particular assets. \* Capital loss on disposal of any asset is not deductible from capital gains on disposal of any other asset even if both are of the same type. \* When the consideration is payable by installments over a period exceeding 18 months, the chargeable gain shall be apportioned to the

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affected assessment years in proportion to the amount of the installments payable in each of the years. Chargeable gains are assessed on current year basis, i. e. preceding year basis is not applicable. Normally, it is the preceding year basis that is applied as companies do not submit CGT computations until the time they submit their respective income tax computations. \* Roll-over relief is available to any company acquiring a new asset to be used for the purposes of the trade in replacement of an old one. This aspect might be of interest to companies as there could be immense benefits accruing to any company claiming the relief

### SCOPE OF CAPITAL GAINS TAX

Capital gains tax has a very wide scope, some of which are discussed under various subheadings in the subsequent paragraphs. Persons liable Any person who is resident in Nigeria shall be liable to the payment of tax on chargeable gains accruing on all disposals of chargeable assets in or out of Nigeria made during that year. The same applies to limited liability companies in respect of the chargeable gains accruing to it for a chargeable period during which the company is resident in the State. Chargeable gains

Chargeable gains accruing to individuals are charged to capital gains tax by the state internal revenue where the person is resident or is deemed to be resident or where the gain is derived. It should be noted that the priority is the residency of the individual. CGT is dealt with by all state offices of the Federal Inland Revenue department. Assessments are made in the year chargeable gain arises that is, on current year basis. The year of assessment as provided by the Act shall be from 1st January to 31st December of each year.

Since the assessments are raised in the year a chargeable gain arises, payment of such is assumed to be on or before 60 days from the date of issuance. Deductions allowable in the computation of CGT include: a. Costs of acquisition or purchase price including all costs incidental to the purchase. b. Improvement costs wholly, exclusively and necessarily incurred. c. Costs wholly, exclusively and necessarily incurred in establishing, preserving or defending the owner's title to or a right over the asset. d. Incidental costs of disposal. This includes: i.

Fees, commissions or remuneration paid for professional services of surveyors or valuer; auctioneer, accountant, agent and or legal adviser. ii. Costs of transfer or conveyance (including stamp duties). iii. Advertisement costs to find a seller/buyer. iv. Costs reasonably incurred in making any valuation or apportionment required for the purpose of computing the capital gains including expenses in ascertaining market value where required. Sums allowable as a deduction in computing the profits or gains or losses of a trade for income tax purposes are not allowable deduction under section 14 of the Act.

Insurance premiums on the asset are not allowable. Computation of gains or losses for chargeable gains tax purposes shall be the " consideration accruing (price paid where transaction is at the market value on date of disposal)" less the cost or value of acquisition together with any allowable expense. There is no one way approach to the presentation of computation of CGT. The presentation varies according to the particular situation. Below are suggested formats for CGT computation in two different approach; the

first approach applies when there is no exemption but have some elements of deductible costs.

The second approach applies where there are some exemptions. APPROACH A

N	N	Disposal proceed	XXX	Less cost and expenses	X	Expenses allowable	X
XX	Chargeable gains	N	YY	Tax payable	YY	at 20%	N 0000

APPROACH B

N	N	Disposal proceed	XXX	Less Exempt	XX	Chargeable gains	N	YY	Tax payable	YY	at 20%	N 0000
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Where there is a part disposal of an asset, the value (costs + expenses) of the asset shall be between the disposed and the undisposed portion. In such a situation, a formula will be applied. Before the formula, an explanation of the figures to be used are is expedient 1.

The amount or value of the consideration (price paid) for the disposal (call that amount or value A), and 2. The market value of the property which remains undisposed of (call that B). 3. The total of cost and expenses of acquisition (call that C) The fraction of the said cost or sums allowable as deduction in computing capital gain accruing on disposal shall be: Amount of consideration for disposal (A) x Cost of whole unit (C) Amount of consideration + Market value of the For disposal (A) undisposed (B) i. e  $\frac{A \times C}{A+B}$  Chargeable events

The major action that gives rise to paying capital gains tax is the disposal of an asset, and disposal here can mean sale, exchange or gift of a chargeable asset. Disposal is said to have taken place where a capital sum is derived from sale, lease, transfer or assignment, compulsory acquisition, e. t. c. Chargeable assets CGT is chargeable on disposal of all forms of property whether situated in or outside Nigeria. All forms of assets are chargeable

except those specifically exempted by CGT Act 1967. Examples of chargeable assets are: 1. land and buildings; 2. shares, options, debts (disposal); 3. disposal of currencies other than Nigerian currency 4. disposal of life assurance policies - since the person disposing of the asset is the beneficial owner 5. Chattels sold for not more than N1, 000 in any tax year. A chattel is defined as tangible movable property, e. g. , personal belongings (clothes, jewelleries). Where sales precedes a specific amount in any tax year, the maximum CGT payable is the lower of normal CGT and half the difference between sales proceeds and specific amount stipulated by the Act.

For the purpose of CGT, disposal means transfer of ownership from one person to another but this definition is extended for the purpose of CGT to include the following situations: i. receipt of capital sum under a policy of insurance; ii. On receipt of capital sum in return for forfeiture or surrender of rights or for refraining from exercising such rights. Market value is used in a situation where the transaction did not take place at arms length, i. e. , transactions involving connected persons. Connected persons include: i. an individual wife or husband; ii. trustee in settlement is deemed connected with the settler as well as any person connected with the settler; iii. partners of a firm are deemed connected with one another as well as with the spouse of each partner; iv. a company is connected with another person if that person has control of it or if that person and persons connected with him together have control of it; v. a company is also connected with another company if the same person has control of both or a person has control of



one, and persons connected with him or her and persons connected with him have control of the other .

The location of the assets is of equal importance. CGT on assets situated outside Nigeria is chargeable on only the amount, if any, received into Nigeria by the owner. The charge is on all persons resident in Nigeria, all Nigerian companies and all others that fall into any of the categories below:

i. An individual in Nigeria for some temporary purpose only and not with any view or intent to establish his residence in Nigeria. ii. If the period or sums of the periods for which the individual is present in Nigeria in that year of assessment exceeds 182 days. iii. A trust or settlement where the seat of the trust is situated outside Nigeria during the whole of that year of assessment. iv. Non indigenous companies whose activities are managed and controlled outside Nigeria but have personal representative are charged during the whole of that year of assessment. EXEMPTIONS AND RELIEFS Section 27 to 40 and section 41 of the capital gains tax act describes the items that are to be exempted from the tax. These include: \* CHARITIES, RELIGIOUS SOCIETIES AND UNIONS. (Section 27) Gains accruing to: i.

An ecclesiastical, charitable or educational institution of a public character ii. Any statutory or registered friendly society iii. Any co-operative society registered under the trade unions act iv. Any trade union registered under the trade union act. The provisions mentioned above are that: a. The gain is not derived from the disposal of any assets acquired in connection with any trade or business carried on by the institution, b. The gain is applied purely for the purpose of the institution or society, where the organisation disposes of its own property. . Where the property held in trusts, ceases to be held,

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the trustees shall be treated as if they have been disposed of and immediately re-acquired the property for a consideration equal to its market value. d. If and so far as any of that property represents, directly or indirectly, the consideration for disposal of assets by the trustees any gain accruing on that disposal shall be treated as not having accrued. \*

**GOVERNMENT ESTABLISHMENTS.** Gains accruing to any local and native authorities are exempted from the provisions of the capital gains tax.

Statutory corporations or any company established by or under any law in Nigeria for procuring goods for export or economic development of any part of Nigeria are exempted from paying capital gains tax. \* **PENSIONS AND PROVIDENT FUNDS** Section 29 provides that the gains accruing to or from any superannuation, pension or provident funds shall be exempted. \*

**DECORATIONS** Section 30 exempts gains accruing from the disposal of a decoration awarded for valour or gallant conduct e. g. an athlete who sells his medal. **GOVERNMENT SECURITIES** Gains from disposal of Nigerian government securities e. g treasury bills are completely exempted from CGT, no matter who owns or sells. Other exemptions not covered above are: i. Gains accruing in connection with the disposal of an interest in or the right under any policy of assurance or contract for a deferred annuity on the life of any person. ii. Sums obtained by way of compensation or damages for any wrong or injury suffered by an individual in his person or in his profession or vocation.

Sums obtained by way of compensation for loss of office shall not be chargeable, except where in any year of assessment the sum received exceeds N 10, 000. iii. Gains accruing on disposal of an individual's only or

main dwelling house throughout the period of ownership up to the time of disposal. iv. A gain accruing on disposal of tangible and moveable assets shall not be chargeable gain if the total value of the consideration does not exceed N 1, 000 in the year of assessment. v.

A motor vehicle for the carriage of passengers is an exempt asset for CGT purposes unless it is of a type not commonly used as private vehicle and is unsuitable to use. vi. Assets acquired by way of gift and disposed of in similar manner. vii. Capital gains accruing to a diplomatic body.

**CONCLUSION** This write-up has provided a comprehensive and concise summary of the concept of capital gain tax with respect to the capital gains tax act of 1967. Besides, it has beamed spotlight on practice of capital gains tax in some of the first world countries from which Nigeria can take cues.