SOW PROFESSIONAL SERVICES LTD

....WE CREATE EDGE FOR BUSINESSES

TAX/AUDIT/MANAGEMENT CONSULTING/ DIGITAL OPTIMISATION/TRAINING

DIGITAL ECONOMY TAXATION

Globally, taxation serves as an important instrument for fiscal stability. In the real sector, governments impose taxes on veritable goods and services to generate revenues for national development. Recent advancements in technology have, however, created more sophisticated ways of deploying technologies to do business. This has given rise to a digital economy that has opened up avenues for rapid economic growth, innovation, enormous employment opportunities and access to a variety of services. Most electronic business transactions are often considered tax-free due to a lack of legal framework or regulatory provisions in some jurisdictions.

The digital economy in its broader perspective refers to any economic activity involving a business model that comprises one or more digital elements such as digital content, digital automation, digital communication, digital distribution, digital payment or other electronic business that is classified as digital economic activity.

Taxation of the digital economy is an emerging issue within the purview of international taxation as there is no universally acceptable practice on the way and manner upon which income derived from digital economic activities should be taxed. Hence, every tax jurisdiction designs and implements its own model.

However, it appears governments are not making the most of the digital boom in generating revenues through appropriate tax policies. (UNCTD, 2019) reports that the digital economy has grown from 4.5% to 15.5% from 2017-2020 of the world's economy. In Nigeria, this value creation did not translate to significant revenues from digital economic activities despite being the second-largest economy in Africa.

In resolving these issues, policy proposals are made that limit the scope of tax avoidance through the enactment of new laws or amendment of existing ones to address the problem of taxation in the digital economy.

Nigeria like many other emerging economies across the globe is losing substantial tax revenues due to its inability to tax digitalized business models simply because of the inadequate regulatory framework. Despite being the most populous nation in Africa with over 200 million populations and over 40 million active users of digitalized business models, Nigeria is still unable to generate meaningful revenues from the digital economic activities in the country.

Digital Economy

The digital economy primarily relies on the non-resident company (NRC) harnessing technology for its customers and clients to interact globally without physical existence but have a significant economic presence (digital presence) or permanent establishment within the host nation. The digitalization of the economy drives innovations and creates employment opportunities which in turn leads to economic growth. The digital economy in its broader perspective refers to any economic activity involving a business model that comprises one or more digital elements such as digital content, digital automation, digital communication, digital distribution, digital payment or other electronic business that is classified as digital economic activity. It has also been defined as a diverse range of economic activities such as the digital elements that used digital content as key factors of production. Through digital content, data is collected, analysed, stored and retrieved via the internet for commercial reasons by foreign entities and their clients, cloud computing, big data, and FINTECH among another technological hub.

Before the advent of the Finance Act of 2019 and 2020, taxation of

NRCs has been captured in sections 9 and 13 of the Company Income Tax Act, but it was modelled or drafted in line with the traditional basis of taxation, which makes it impossible to effectively monitor or properly tax companies operating in the digital space. In essence, this reflects a source or fixed-based taxation, which means taxing NRCs who are operating in Nigeria through an authorized agent, this principle fostered, among others, the requirement of permanent establishment as the basis of taxation for companies operating within any jurisdiction.

However, the advent of the digital economy which has made it possible for NRCs to conduct business in Nigeria without the need for a Permanent Establishment makes the traditional basis of taxation grossly ineffective.

This prompted the legislature and tax administrators to amend the substantive legislature, and this brought forth the Finance Bill of 2019, passed into law in January 2020.

The Finance Act amended section 13(2) of CITA which seeks to tax NRCs by introducing the Significant Economic Presence Rule. This further extends the taxation net which, prior, wouldn't have captured the NRCs. Interestingly, the Finance Act failed to define what Significant Economic Presence means, but going by the provision of CITA, 2004, in sections 13(2)(c) and (e), it draws into the tax net companies drawing 25million (or its equivalent in foreign currency) as annual return.

With Finance Bill of 2019, it has become imperative for organisations operating in the digital space of the country to comply with their tax obligation as stipulated in the Nigerian Tax Laws.

For more information on Digital Taxation kindly contact us at SOW Professional Services Ltd for necessary supports on this

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THANK YOU!