

Taxation of High Net-Worth Individuals

Is this a chase after shadows?

The current economic landscape has forced several State Governments hitherto dependent on Federal Government allocations to look inwards for revenue. Personal Income Tax (PIT), especially those payable by high net worth individuals (HNWIs) is gradually attracting the attention of State Internal Revenue Services (SIRS). This is based on the reality that PIT derived from individuals within the organized private sector cannot close the large budget deficits created by dwindling oil revenue. Against this backdrop, some SIRS are currently deliberating the tax revenue potentials of HNWIs. But who are HNWIs?

HNWIs are those who hold at least US\$1 million in financial assets excluding collectibles, consumables, consumer durables and primary residences¹. A recent World Wealth Study reveals that the number of HNWIs in Nigeria has risen to over twenty thousand (20,000) individuals, from approximately five thousand (5,000) recorded at the turn of the 21st century.

The report indicates over four hundred percent (400%) increase in the number of HNWIs in Nigeria. It should be expected that such individuals who comprise the 20,000 would be tax literate and competent in taking advantage of the available reliefs within the tax laws to manage the tax incidences of their transactions as well as exposure on their income.

It thus becomes pertinent to inquire what marginal tax revenue a focus on these individuals would bring. This is however not to suggest that tax authorities should not seek to confirm whether or not these individuals meet expectations in terms of their tax compliant status.

Given that one of the reasons for Nigeria's compliance problem in the tax space is the large scale informal sector, the number 20,000 for HNWI is too paltry and adopting a figure as high as \$1million dollars for classification purposes would be counter-productive as a large proportion of potential taxable persons deserving of a SMART² target approach from tax authorities may be unwittingly excluded. A lower

threshold for Nigerian tax purposes would be more reasonable and useful.

In this column, a year and a half ago, we submitted that one major imperative before the tax authorities, notably Federal Inland Revenue Service (FIRS), has been the need to accelerate the expansion of the tax net. "Expanding the tax net has varying dimensions but that which is the focus of this column is increasing the number of taxpayers or potential taxable persons in the tax base by whatever strategy or combination of strategies howsoever developed. Reducing the ranks of defaulting taxable persons must be rigorously and relentlessly pursued. A significant catchment of potential taxable persons that must be brought within the tax net are those operating in the informal sector of the economy."

With respect to HNWI as a critical catchment of the informal sector, it is important to understand why tax collection from HNWIs is low. In other climes, several HNWIs who do not pay PIT or pay very little do so because they have devised ingenious means of avoiding taxes e.g. taking advantage of specific provisions of the law, in which case they structure their business in a certain way such that they legally avoid taxes. In these climes it is abnormal to find a HNWI who does not account for taxes and it is usual to find the tax authorities go after HNWIs for violating tax regulations.

However, in Nigeria this is not entirely the case. There are alleged cases of brazen non-compliance by certain HNWIs. These HNWIs fall into two groups – the known and unknown.

It is believed that several HNWIs who do not pay PIT are known to the tax authorities. They earn vast amounts of income ranging from property to trading income and their businesses are known to many. However, it is understood that they wield a lot of power behind the "throne" or scene and have become largely untouchable. For those who are yet to be discovered, it may simply be because tax authorities have

simply not been rigorous and relentless in their pursuit to track these taxable persons.

The following considerations may improve the approach to resolving HNWIs tax compliance challenge:

Proper classification of HNWI

This is important as there are no set parameters for determining individuals who fall within this bracket. Some state revenue authorities at their discretion have adopted the income rate of N6million as the minimum threshold for HNWI, but this rate in reality varies according to the state of residence of the tax payer. Clearly, adopting a \$1million threshold would not be appropriate. State tax authorities should review this critically and adopt a very realistic threshold for HNWI income in their respective jurisdictions.

Presumptive Income Tax Assessment (PITAS)

While it may be easy to identify HNWIs in the formal sector, there is no accurate statistics of the number of HNWIs in the informal sector of the country's economy. Necessity is therefore laid upon the revenue authorities to bring all such persons into the tax net. This has led to the proposal of PITAS. PITAS is focused on taxable persons who historically failed to comply with the tax laws, due to size and lack of fixed business address; by providing simplified tax assessment procedures.

Harmonization of individual data

Different sectors of the economy have individuals' data for their respective purposes. This includes the Bank Verification Number (BVN) which have streamlined customers' accounts and provides a single link for accessing individual banks' transactions from various banks. The tax authority can leverage these platform to access the HNWI to account for their fair share of tax to the government.

Voluntary Asset and Income Declaration Scheme (VAIDS)

It is perhaps the invisibility of the HNWIs that drove the National Economic Council (NEC) to approve another

tax amnesty scheme, VAIDS. VAIDS which is expected to take effect from 1 May 2017, will leverage the current global movement against tax evasion and illicit financial flows and will encourage voluntary declaration of undisclosed income and assets with consequential payment of applicable tax liabilities over a defined period. It is expected that corporate and individual taxpayers will utilize the limited amnesty to remedy their tax compliance.

State tax authorities must not only innovate and strengthen the tax administration system, they must adopt compliance strategies that speak to the identified attitudes of taxpayers and/or taxable persons as follows:

Those who decide not to comply	Capacity to deploy the full force of the law is welcome here
Those who do not want to comply	Capacity to deter by detection is relevant here
Those who try but don't always succeed to comply	Capacity to help is useful here
Those willing to do the right thing	Capacity to make compliance easy/easier is applicable here

A more effective reward-based approach could be adopted in lieu of the existing sanction based system to compensate taxpayers in a tangible manner with fiscal reliefs for sustained significant high compliance level as a direct taxpayers and in their capacity as tax collection agents for withholding tax and value added tax.

It is important to stress once again that it is the constitutional duty of every citizen to declare his income honestly to the appropriate and lawful agencies and pay his taxes promptly.

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¹Wikipedia
²That is, one which is specific, measurable, achievable, realistic and time-bound