



Pioneer status incentive scheme in Nigeria: Wider coverage with weightier conditions – any grey areas?

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The Federal Government of Nigeria approved the eligibility of 27 additional industries for possible grant of tax holiday under the pioneer status incentive at the Federal Executive Council meeting held on Wednesday, 2 August 2017. Following FEC’s approval, the Minister of Industry, Trade and Investment announced on Monday, 7 August 2017, the lifting of administrative suspension on approval of pioneer status incentive (PSI) application.

Companies granted pioneer incentive enjoy tax holiday for an initial period of three years, extendable by additional two, subject to meeting the required conditions.

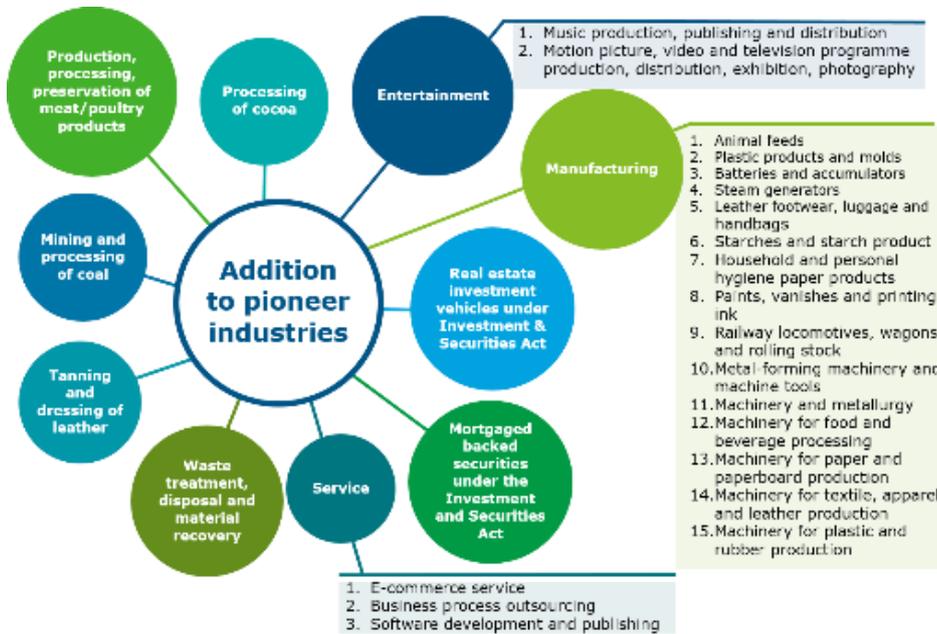
The Federal Government had suspended the grant of PSI in September 2015 to enable a comprehensive review of the incentive scheme due to perceived abuse. Subsequent to this, the National Assembly also, in May 2017, set up an ad-hoc committee to investigate perceived abuses of

PSI by companies operating in Nigeria.

The reformed PSI framework has culminated in additional 27 eligible industries and products as well as release of new guidelines for PSI application. This newsletter examines these developments.

1. Review of new industries and products for PSI

Some of the key industries covered in the new list as announced by the Minister include manufacturing and processing, e-commerce, software development and business process outsourcing. Other notable industries include entertainment (covering music, motion picture, photography, video and television production, etc), mining, as well as real estate investment vehicle and mortgage-backed securities. See diagram below, for a cross-section of all newly added industries/products.



of metal forming machinery” and “manufacture of machinery for metallurgy” are listed as two separate activities. However, both activities are of similar nature and could have been listed as a single activity. Moreso, some of the activities covered under the new list appear to already exist in the erstwhile list of 44 pioneer industries.

Activities involving the production and processing of leather, tanning of leather and leather products are listed separately on the list. Tanning is the process of making leather; it could conveniently be under

exemptions under the provisions of Companies Income Tax Act and the Nigerian Minerals and Mining Act (NMMA) which are similar to the reliefs granted under PSI.

Thus, the inclusion of “mining and processing of coal” as a pioneer activity appears superfluous. Understandably, there are other reliefs under the PSI that may not be covered by these other laws.

The major concern is the potential regulatory overlap that may arise from uncertainty as to the intentions of Government. Presently, the incentives on mining (include tax holiday) are granted in two different pieces of legislation. Tax payers could be tempted (and rightly so) to try to claim reliefs under the two separate but similar schemes incentives (provided they meet underlying criteria).

Other potential possibilities here are that the inclusion of mining on the list may be deemed to be complementary to the tax relief provided for under the NMMA or a reinforcement of the provisions of the NMMA and not as a separate incentive. In this regard, would tax payers be entitled to claim the two incentive regimes – e.g. must the tax relief period run concurrently or would a consecutive arrangement be allowed?

The expansion of the list is a welcome development and it demonstrates the Federal Government’s attunement to some of the plights of business owners and commitment to the development of certain industries. This brings the total list of eligible industries to 71.

A cursory review of the 27 additional pioneer industries raises some concerns as follows:

Repetition of activities and products: There appears to be repetition of certain eligible industries and products on the list. For instance, “manufacture

processing and manufacture of leather.

In view of this, there may be need to revisit and streamline the list (as well as the existing list of 44 approved industries and products) to avoid unnecessary repetitions. This would ensure that each industry/activity on the list is unique and differentiated from others.

Inclusion of seemingly superfluous items: Companies involved in mining activities already have

2. Review of the new application guidelines for PSI

To facilitate the process of granting pioneer status, the Minister also confirmed new application guidelines for PSI. Major highlights of the new guidelines are reviewed below.

Period of application: New applications must be made **within the first year of production of the eligible product**. Also, investors wishing to extend their pioneer status must do so within one month upon expiration of the initial tax relief period of three years or an extension of one year.

This may suggest that investors in approved pioneer industries already well beyond their first year of production are not within the contemplation of the PSI based on the new guidelines. This raises certain questions as set out below:

- **Approbation and reprobation:** This restriction, if interpreted strictly, excludes entities whose industries were just included on the list but had been in operation for a period exceeding one year from benefiting from the incentive. For example, it is arguable that a real estate investment vehicle that has been in operation for 2 years will be unable to benefit from the PSI. It thus appears that government has given a grant with one hand and taken it with another for such businesses.
- **Ambiguity on expansion:** This also comes with uncertainty surrounding existing companies in production who expand their lines of business - for example, setting up a new manufacturing plant. Question here is whether first year of production will be determined with reference to the company as

a whole or with reference to the expansion. If reference is made to the company, the application of the PSI to expansion projects becomes mute as the restriction could then take away some or all of the potential benefits.

- **Ambiguity with new company - old business:** In the event of a merger or re-organization resulting in a new company taking over an old business which qualifies for pioneer, it is unclear whether this restriction would be enforced

Revision of the asset base requirement: Investment requirement for applicants in respect of tangible non-current asset has been increased from ₦10million to ₦100million under the new guidelines. This requirement has been lauded by various stakeholders as it significantly increases the required investment for grant of the incentive and is in line with the current growth and industrialization objectives of Federal Government.

However, an apparent implication of this is that micro, small and medium scale enterprises (MSMEs) may not be able to benefit from the incentive as most would struggle to meet this requirement. This appears contrary to the Economic Recovery and Growth Plan (ERGP) which seeks to promote MSMEs in Nigeria. This is more so as MSMEs do not currently have sufficient incentives.

Similarly, businesses engaged in some of the newly added pioneer industries/products e.g. "Mortgaged backed securities under the Investment and Securities Act" may typically not have investments of up to **₦100million** in tangible non-current assets. Also, e-commerce, software programming and ICT related companies typically invest more

in intangible non-current assets due to the nature of their business. Therefore, if this minimum requirement for investment in **tangible non-current asset** is applied as a rule of the thumb, some listed pioneer industries may be naturally disenfranchised.

Certification of qualifying assets now a prerequisite for PSI applications: Assets of companies engaged in approved activities must be certified by the Federal Inland Revenue Service (FIRS) before applying for an extension of PSI. Under the new guidelines, such certification must be done within a month before the expiration of the initial tax relief period.

Bearing in mind that the application for extension is expected to be completed within one month of expiration of the initial incentive, there may be a period of overlap between both activities as the certification process by FIRS may sometimes stretch beyond the available two month window allowed.

We note that there is an Executive Order directing applicants to deem applications as approved, where government agencies do not approve or reject their applications within specified timelines. In the same vein, we are not aware that FIRS presently have published guidelines for this certification (including timelines). We expect the regulatory agencies to collaborate to ensure efforts of taxpayers in this regard are not frustrated.

Requirement to submit annual performance reports: Beneficiaries of PSI are required, under the new guidelines, to submit annual performance reports to the Nigerian Investment Promotion Council (NIPC) no later than 30

June of the following calendar year.

The performance report is expected to include audited financial statements, production and financial performance, evidence of infrastructure developed, utilization of tax savings, evidence of payment of fees, amongst other things. Failure of a beneficiary to satisfy this requirement may result in revocation of the PSI certificate, deletion of the company's name from the list of beneficiaries and notification to FIRS to collect tax for the unexpired period as well as period for which the report was not submitted.

Addition and deletion to the pioneer list: The new guidelines provide for biennial review of the list of pioneer industries and immediate implementation of to the list. On the other hand, there is a three-year window for products and/or industries impacted by deletion during which they will continue to enjoy pioneer status incentive.

The biennial review is a step in the right direction as it is an indication of Federal Government's commitment to evaluating the economic impact of PSI to each industry.

Zero tolerance for corruption: The new guidelines underpins the current administration's non tolerance for corrupt practices as any proven act of corruption, inducement or gratification in the process of application is frowned upon. Companies that engage in any of these acts, in addition to being investigated by the relevant government agencies, may also face prosecution.

Furthermore, the new guidelines provides a 12-step application process for fresh applications

and is expected to take approximately 25 weeks to complete. For investors seeking to extend their pioneer status, a 7-step application process should be completed in approximately 15 weeks. There may be some concerns around the new timelines, especially as fresh applications would take approximately six months to be completed. However, given that under current practices, some applications take over a year to be completed, the new six month timeline may be seen as a vast improvement.

While the new application process is not significantly different from the current practice, the inclusion of timelines for each stage of the process is a new development and may be an indication of Government's move to hold regulatory bodies responsible under the recent drive of Government to improve the ease of doing business in Nigeria. This is in light of the recent Executive Order signed by the Acting President, requiring Ministries, Departments and Agencies (MDAs) of government to approve or reject applications within specified timelines as applications would be deemed granted where such MDAs fail to do this within the requisite timelines. The question this poses is whether all concerned government regulatory agencies are ready for this eventuality.

3. Seeming deletion of industries from the original list of pioneer industries and products

We understand from the press release issued by the Federal Ministry of Industry, Trade and Investment that the Federal Executive Council also approved the deletion of two industries from the existing list of pioneer industries/products.

These industries/products are however not documented in any formal document (PSI Guidelines or additional list).

Where the deletion has in fact taken place, FMITI should clarify this and lay the ambiguity on deletion to rest. It is also necessary, however, that these deleted industries be made known to be public immediately for planning purposes.

Overall, the inclusion of new industries and products into the approved list for pioneer purposes, and the introduction of new guidelines for application for PSI are laudable developments. They are an indication of the government's drive to achieve industrialization and encourage investment in these sectors, in line with the ERGP. It also corroborates the recent drive for responsibility of regulators (as documented in several Executive Orders) in relation to timeline for bringing applications/grant process to closure. We encourage investors to apprise themselves of these changes to the PSI scheme in order to evaluate possible eligibility for the incentive.

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If you require further clarification or seek to understand how this new scheme may benefit your current or proposed business interest, please reach out to us.

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