REAPPRAISING THE LEGAL FRAMEWORK FOR TRANSFER PRICING IN NIGERIA*

Abstract

Transfer pricing is a practice whereby companies use transactions between different corporate units to shift income between jurisdictions for the purpose of reducing the company's overall tax burden. Transfer pricing has become a critical and important issue in the Nigerian business environment as a result of the increase in foreign direct investment. The complexities prevalent in cross border transactions between affiliated companies have equally thrown up the need for close scrutiny on related party transactions. Transfer pricing as a valid business practice describes the process of setting the prices at which related companies transfer physical goods, intangible property or services among themselves. It is a growing cause of concern for tax authorities as it could provide avenues for a tax avoidance hence translating into great loss of potential tax revenue. Transfer pricing regulations are meant to ensure that all transactions between related parties are carried out at arm's length. This paper evaluates the legislative framework for transfer pricing in Nigeria, while analyzing the key features of the Income Tax (Transfer Pricing) Regulations 2018 and Organization for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017. This paper advocates among others that a proper implemented transfer pricing regime in Nigeria will enhance certainty in the cost of carrying out business operations in Nigeria, encourage negotiation of more double taxation treaties, thus leading to avoidance of double taxation and this will in turn close all loopholes for tax avoidance.

Keywords: Transfer Pricing, Arm's Length, Connected Persons, OECD, Tax Avoidance

1. Introduction

Transfer pricing has emerged as one of the most important issues in international taxation forming a key component of discourse among tax practitioners, lawyers, economists, organizations etc. Transfer pricing has become of a great concern presently to tax authorities when used as a tax avoidance device. Transfer pricing abuse results in loss of potential tax revenue and forms the bulk of illicit financial outflows especially from developing countries like Nigeria. Recently, there has been an increase in intercompany transactions and number of non-resident multinational enterprises operating with in Nigeria. This increase can be attributed to the rapid growth of foreign direct investment in Nigeria especially in the oil and telecommunications sectors of the economy. This development has earmarked the need for close monitoring of transactions with related parties in a bid to avoid tax. Transfer pricing legislation serves the major purpose of ensuring that transactions between related parties comply with the arm's length principle. In the international sphere, the bulk of transfer pricing legislations are based on the Organization for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines for Multinational Enterprises and United Nation's Transfer Pricing Practical Manual for Developing countries. In Nigeria, the general anti-avoidance provisions embedded in various tax legislations [1] were used previously in the application of the arm's length principle. However, the provisions were broad, subjective and uncertain, thus necessitating the need for clear and objective guidelines. In a bid to strengthen the general anti- avoidance provisions in the relevant tax laws, the Federal Inland Revenue Service (FIRS) introduced the Income Tax(Transfer Pricing Regulations No.1, 2012 which was amended in 2018.This provides guidelines for application of the arm's length principle. The focus of this paper is to attempt an evaluation of the extant legislative framework for Transfer Pricing in Nigeria vis a vis international legislation on the subject for best practices.

2. Transfer Pricing Mechanism

Transfer pricing has emerged as one of the most important issues in international taxation, forming a key component of discourse among economists, lawyers, etc. Transfer pricing serves as a cause of wrong to tax authorities when used for tax avoidance purposes. Reports are illustrative of the fact that transfer pricing abuse results in loss of potential tax revenue[2] and forms the bulk of illicit financial outflows especially from Africa[3]. In recent times, there has been an increase in the volume of intercompany transactions and number of non-resident multinational enterprises operating within Nigeria. This increase can be attributed to the rapid growth of foreign direct investment in Nigeria especially in the oil and telecommunications sectors of the economy. This development has highlighted the need for a close marking of related party transactions particularly amongst multinationals by Nigerian tax authorities.

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[1] Personal Income Tax Act (PITA) Cap P8 (as amended) Laws of Federation,
(LFN) 2004, s.17, Petroleum Profits Tax Act, Cap P13, (LFN) 2004, s 15, Companies Income Tax Act (CITA), Cap C21, LFN 2004, s 22.

[2] 'Death and Taxes: The true Toll of Tax dogging' www.christianaid.org.uk/unages/deathandtaxes.pdf. Accessed 20 November, 2021.

[3] D Kar and D Wright, 'Illicit financial flows from Africa: A Hidden Resource for Development, 'www.gfintegrity.org/content/view/300/75/ accessed 20 November, 2021.

3. Meaning of Transfer Pricing

Transfer pricing is a term used to describe intercompany pricing arrangements relating to transactions between related entities. Basically, it refers to how related parties price goods, services, intangible assets, loans and other transactions between them[4]. Transfer pricing is a term which encompasses the setting, analysis, documentation and adjustment of charges made between related parties for goods, services, or use of property including intangible property[5]. It relates to the system of setting prices for the transfer of goods and services and intangibles between parties under the same entity or between related entities which operate in more than one tax jurisdiction[6]. Transfer pricing is a major concern of Multinational Enterprises (MNEs) which operate in more than one country and by extension, more than one tax jurisdiction. From the foregoing, transfer pricing refers to an arrangement where multinationals take advantage of loopholes in tax legislations of other countries of shift taxable income or profits among their group of companies at a non-arm's length price to countries with a favourable rate taxes. Thus, transfer pricing is the price at which goods or services are transferred between company divisions within one country or between related companies of a multinational organizations across International Tax legislations and regulations differ from one tax jurisdiction to another and there is need for multinational business entities to comply with all these requirements. Compliance may lead to an increase in the tax burdens of the enterprises through double or multiple taxation. Multiple taxation leads to increased costs for companies which conduct businesses in Nigeria and also creates hurdles is the way of transfer of goods and services across borders generally. Much as, tax administrators all over the world have the right and responsibility to impose tax on these multinationals, but it has to be done equitably. Thus, this can only be achieved when each tax administrator actively determines the income and expenses of the multinational enterprise attributable to its own jurisdiction[7].

4. The Organization for Economic Cooperation and Development (OECD)

The Organization for Economic Cooperation and Development (OECD)[8] has made commendable efforts in offering an international standard for the regulation of transfer pricing. This is majorly reflected on 1984 reports of the OECD on transfer pricing and the introduction of the OECD Transfer Pricing Guidelines for MNEs and Tax Administrations (OECD TP Guidelines) in 1995 as subsequently updated in 2017. Additionally, the OECD has a Global Relations Program, which promotes global dialogue on transfer pricing and aims at promoting good practice, building country transfer pricing capacity and feeding non-OECD country views into the OECD's work in this area.

The OECD set up a Global forum on Transfer pricing which met for the first time in 2012. The OECD Guidelines on Transfer Pricing on MNEs and Tax Administrations (OECD TP Guidelines) offers detailed and comprehensive suggestions on the practical application of the 'arm's length' standard by both member and non-member countries. [9]

The key features of the OECD guidelines as contained in the chapters highlighted above are summarized as follows; Chapter I focuses on a detailed discussion of the 'arm's length' principle. The said chapter states that 'arm's length' adjustments must be applied, irrespective of any contractual obligation of the parties and of any intention of the parties to avoid tax. The chapter further provides accordance with the 'arm's length' principle, the tax liabilities of 'associated enterprises' and the tax revenues of the countries concerned will be distorted.[10] It should be noted however that certain factors other than tax considerations can lead to distortions such as conflicting legislation relating to customs valuation, antidumping, exchange and price control[11]. Chapter II of the OECD Guidelines make provision for common methods and practices in the application of the arm's length principle in transfer pricing. In this regard, the OECD Guidelines outline five methods as determinants for the arm's length price as follows; comparable uncontrolled price (CUP) method[12], Resale Price Method (RPM)[13];

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[4] O Sowande 'Transfer pricing in Nigeria' www.mondaq.com accessed 30 November, 2021.

[5] I O Okauru (ed) Federal Inland Revenue Service and Taxation Reforms in Democratic Nigeria. (Ibadan, Safari Books; 2012).

[6] *Ibid.*

[7] *Ibid.*

[8] The OECD, Other member countries are; Australia, Austria, Belgium, Canada, Chile, the Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, the Slovak republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United States of America and the United Kingdom.

[9] This Guidelines are updated regularly so as reflect developments in international trade. There are usually supplemented with additional guidance addressing other aspects of transfer pricing and are reviewed and revised periodically.

[10] Chapter I, OECD TP Guidelines.

[11] R AVI-Yonah, 'The Rise and Fall of Arm's Length: A study in the Evaluation of U.S. International Taxation. www.ssrn.com/abstract=1017524 accessed 29 November, 2021.

[12] This method compares the price charged for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances.

[13] This method begins with the price at which a product that has been purchased from an associated enterprise is resold to an independent enterprise. This price (the resale price) then reduced by an appropriating margin on this price (the 'resale price

Cost Plus Method (CPM)[14], Transactional Net Margin Method (TNMM)[15] and the profit split method (PSM)[16]. The Guidelines, however, do not a formal order of ranking. Chapter III examines comparative analysis, timing issues in comparability and compliance issues. Chapter IV considers administrative approaches to avoiding and resolving transfer pricing disputes, transfer pricing compliance practices, simultaneous tax examinations, safe harbours, advance pricing arrangements and Arbitration. Chapter V focuses on documentation requirements. It is explicitly stated in this chapter that there is no obligation to present supporting documents at the time the transfer is determined or the tax return is filed[17]. Information requirements that should be provided when filing a return should be limited to information which enables the tax administration to select cases for further examination[18]. The Guidelines also stated that it is not reasonable to burden the tax payer with disproportionately highly costs, e.g. in order to obtain documents from foreign related enterprises or in an exhaustive search for comparable, if the tax payer believes that no comparable exist or if obtaining comparable exist or if obtaining comparable would incur disproportionate costs for the tax payer[19]. The tax payer should not be expected to provide more documentation than the minimum required for a reasonable determination by the tax administration that the tax payer has compiled with 'arm's length' principle[20]. Chapter VII of the OECD guidelines discusses special considerations for transfer pricing of intra-group services. Chapter VIII makes provision for cost contribution arrangements for participants,[21] the tax treatment of contributions and payments expected benefits from the cost contribution arrangements and its entry, withdrawal or termination. Chapter IX considers transfer pricing aspects of business restructurings, the arm's length compensation for the restructuring itself and remuneration of post restructuring controlled transactions.

5. Transfer Pricing Regulations

The Federal Inland Revenue Services in exercised of the powers conferred on it by section 61 of the Federal Inland revenue (Establishment) Act makes this regulation; Income Tax (Transfer Pricing) Regulations 2018[22].

Purpose of the Regulations

The main purpose of these regulations is to give effect to the relevant provisions of the:

a) Personal Income Tax Act, Cap P. 8 Laws of the Federation of Nigeria, 2004;
b) Companies Income Tax Act, Cap C 21, Laws of the Federation of Nigeria, 2004 (as amended by the Companies Income Tax (Amendment) Act, 2007;
c) Petroleum Profits Tax Act, Cap. P 13, Laws of the Federation of Nigeria, 2004; and
d) Capital Gains Tax Act, Cap. C 1, Laws of the Federation, 2004; and
e) Value Added Tax Act, Cap. VI, Laws of the Federation of Nigeria, 2004.

Objectives of the Regulations

a) Ensure that Nigeria is able to tax on an appropriate taxable basis corresponding to the economic activities deployed by taxable persons;
b) Provide the Nigerian authorities with the tools to fight tax evasion that may arise through over or under pricing of transactions between related persons;
c) Reduce the risk of economic double taxation;
d) Provide a level playing field for both multinational enterprises and independent enterprises carrying on business in Nigeria; and
e) Provide taxable persons with certainty of transfer pricing treatment in Nigeria[23].

Scope of the FIRS Income Tax (Transfer Pricing) Regulations

The Regulations are to be applied in transactions between connected persons and shall include:

(a) Sale and purchase or lease of goods and services;
(b) Sales, purchase or lease of tangible assets;

margin') representing the amount of which the reseller would seek to cover its selling and other operating expenses and in the light of the functions performed (taking into account assets and risks assumed), make an appropriate profit.

[14]Cost plus method begins with the costs incurred by the supplier of property (or service) in a controlled transaction for property transferred or services provided to an associated purchaser. An appropriate cost plus mark is then added to this cost, to make an appropriate profit in the light of the functions performed and the market conditions.

[15]This method examines the net profit margin relative to an appropriate base (e.g. cost, sales, assets) realized from a controlled transaction.

[16]This method is based on identification and appropriate split of the profit realized by related enterprises from controlled transaction.

[17] Chapter V, OECD Transfer Pricing Guidelines.

[18] *Ibid.*

[19] *Ibid.*

[20] *Ibid.*

[21] *Ibid.*

[22] This regulation repealed the Income Tax (Transfer Pricing) Regulations No. 1 2012 (The first TP Regulation in Nigeria).

[23] FIRS Income Tax (Transfer Pricing regulation 2).

(c) Transfer, purchase, license or use of intangible assets;
(d) Provision of services;
(e) Lending or borrowing of money;
(f) Manufacturing arrangements; and
(g) Any transaction which may affect profit or loss, or any other matter incidental to, connected with or pertaining to the transactions referred to in paragraphs (a) to (f) of this regulation.

6. Meaning of Connected Persons

Generally, persons are deemed connected where one person has the ability to control or influence the other person in making financial, commercial or operational decisions or there is a third person who has the ability to control or influence both persons in making financial commercial or operational decisions[24]. Connected persons may also be broadly referred to as related parties in the context of transfer pricing. The term further includes individuals who are related to each other or between persons both of whom are controlled by some other persons[25] and 'associated enterprises' as stated under the OECD Guidelines[26]. The phrase 'connected persons' reveal that the regulations apply to both natural and artificial persons[27], as well as persons referred to in specified tax legislation[28]. This definition also has the effect of applying to both local and cross border transactions. This wide definition grants the tax authority to probe into transactions conducted by a company with owner managers, shareholders directors and the relatives of each 'connected persons'. A combined reading of the sections[29] would show that 'connected persons' are defined in reference to 'control' and relationship between tax payers is the case of individuals and corporate entities. The sections cover any person directly or indirectly participating is the management, control, or capitalization of an enterprise that is involved in a transaction or, persons who are directly or indirectly controlled, or managed by another person who is involved in the business under review[30]. This shows that the regulations extend to both the person controlled or managed by another and the person who controls or manages him.

The Regulations, however, does not define the term 'control'. This differs from the position in tax laws in other jurisdictions which define control in terms of shareholding, voting power or participation, either directly or indirectly, in management or capital[31].

7. The Arm's Length Principle

In the context of transfer pricing, the arm's length principle simply means that the transfer price should be the same as if the two companies involved were indeed two independent entities, not forming part of the same corporate structure[32]. Under the Value Added tax Act[33], the arm's length principle is defined as transaction on normal open market commercial terms. Further, in defining the arm's length principle in the context of taxation, recourse is also had to the case law; in *Skalbania (Trustee of) V Wedgewood Village Estates Ltd*[34]. The British Colombia Court of Appeal defined an arm's length transaction as:

> a transaction negotiated by unrelated parties, each acting in his or her own self-interest; the basis for a fair market value determination; commonly applied in areas of taxation when there are dealings between related corporations, e.g. parent and subsidiary… The standard under which unrelated parties, each acting in his or her own best interest, would carry out a particular transaction[35].

A transaction is not deemed to be at arm's length where corporations are controlled directly or indirectly by the same person, whether the person is an individual or a corporation[36].

Arm's length is described by OECD model Tax convention[37] as

> When conditions are made or imposed between two associated enterprises in their commercial or financial relations which differ from those which would have been made or

[24] *Ibid*, Regulation 12.
[25] Personal Income Tax Act, S. 17 (3) (b), Companies Income Tax Act, S. 22 (2) (b).
[26] Article of the OECD Model Tax Convention, the OECD TP Guidelines and UN TP Manual.
[27] The phrase includes 'persons, individuals, entities, companies, partnerships, joint ventures, trusts or associations'.
[28] Including 'persons' mentioned in the S. 13 (2) (d), S. 18 (2) (b) and S. 22 (2) (b). Companies Income Tax Act as amended, S. 15 (2) of the Petroleum Profit Tax Act, S. 17 (3) (b) Personal Income Tax Act, Article 9 of the OECD Model Tax Convention.
[29] Income Tax (Transfer Pricing Regulations), Reg. 12, Paragraph 2.
[30] N Ikeyi et. Al., 'Review of Transfer Pricing Regulations', Newsletter No. 2012/02 P. 2.
[31] Such as India and the UK.
[32] J Neighbour, 'Transfer pricing: keeping it at arm's length'. www.oecdobserver.org/news/archivestory.php/aid/670/transferpricing:keepingitatarm'slength.html, accessed 20 December, 2021.
[33] Value Added Tax Act, S. 46.
[34] (1989) 5 WWR 254
[35] *Ibid*.
[36] *Minister of National revenue V. Sheldon's Engineering Ltd* (1955) S.C.R. 637.
[37] Article 9.

> imposed between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprise, but by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and be taxed accordingly[38].

The regulations[39] adopt the internationally recognized standard of the arm's length principle[40]. Reg. 4 (1) requires connected person to ensure that the taxable profits arising from a controlled transaction must be conducted in a manner consistent with arm's length principle.[41] A literal examination of the above regulation would seem to suggest that the FIRs would focus on an examination of the taxable profits of a connected person rather than the full terms of a 'controlled transaction' in determining whether a transaction is conducted in a manner consistent the arm's length principle. A combined reading of Regulations 5 and 9, however, reveals that the test for determining consistency with the arm's length principle is whether or not the conditions under which a controlled transaction was conducted would have been the same if the transaction had been conducted by or amongst independent and unrelated persons in similar circumstances[42]. Further, Regulation 4(3)[43] empowers the FIRs to make adjustments in the event of non-compliance where necessary, to ensure that the taxable profit of a connected taxable person is consistent with the arm's length principle. The Interpretation of Regulation 4(3), may however inflict a form of hardship on the tax payer. The section broadly provides that; 'Where a connected person fails to comply with the provisions of this regulation, the service shall make adjustments, where necessary …'[44] This provision is vague in the sense that it seems to suggest that noncompliance with every provision of the regulations will ignite adjustments by the FIRS. The proper approach would have been to re-draft the provisions of Reg. 4 (3) to the effect that failure to transact at arm's length would lead to adjustments by the service. This proposition would make for clarity in the interpretation of the section.

8. Transfer Pricing Methods

The regulations provide for the use of specified transfer pricing method sin the whether or not the profits arising from a transaction were derived in line with the arm's length principle.

Accordingly, regulation 5 provides as follows;

> In determining whether the result of a transaction or series of transactions are consistent with the arm's length principle, one of the following transfer pricing methods shall be applied-
> i) the comparable uncontrolled price (CUP) method;
> ii) the Resale price method;
> iii) the cost plus method;
> iv) the Transactional Net margin method;
> v) the transactional profit split method;
> or
> vi) any other method which may be prescribed by Regulations made by the service from time to time[45].

From the foregoing, it is seen that these transfer pricing methods are similar to the ones contained in the OECD transfer pricing guidelines[46]. These transfer pricing methods shall be considered *seriatim*;

i) **Comparable Uncontrolled Price (CUP) Method:** means a method in which the price charged for property or services transferred in a controlled transaction are compared with the price charged from property or services transferred in a comparable uncontrolled transaction[47].
ii) **Resale Price Method:** This is the method in which the resale margin that a purchaser of a property in a controlled transaction earns from reselling the property in an uncontrolled transaction is compared with the resale margin that is earned in a comparable uncontrolled purchase and resale transaction[48].
iii) **Cost Plus Method:** By this method, the mark up on the costs directly and incurred in the supply of goods, property or services in a controlled transaction is compared with the mark up on those costs directly or indirectly incurred in the supply of goods, property or services in a comparable uncontrolled transactions[49].
iv) **Transactional Net Margin Method:** This is a method in which the net profit margin relative to the appropriate base, including costs, sales or assets that a person achieves in a controlled transaction is

[38] *Ibid.*
[39] Income Tax (Transfer Pricing) Regulations.
[40] OECD TP Guidelines.
[41] Ikeyi, *Op. Cit*. P. 2.
[42] *Ibid*.
[43] Income Tax (Transfer Pricing) Regulation, 2018.
[44] *Ibid*, Regulation 27.
[45] *Ibid*, Regulation 5 (1).
[46] OECD TP Guidelines, Chapter II.
[47] Income Tax (Transfer Pricing) Regulations, 2018, Regulation 27.
[48] *Ibid*.
[49] *Ibid*.

compared with the net profit margin relative to the same basis achieved in a comparable uncontrolled transaction.

This method of transfer pricing formed part of the issues canvassed for in *Prime Plastichem Nigeria Limited (PPNL) v. Federal Inland Revenue Service (FIRS)*[50]. PPNL is a private limited liability company engaged in trading of imported plastics and petrochemicals in Nigeria. During 2013 and 2014 Financial Years (FYs), PPNL entered into a related party transaction with Vinmar Overseas Limited (VOL) for the supply of Petrochemical Product. PPNL adopted the Comparable Uncontrolled Price (CUP) TP method to test whether the terms of the transaction with VOL for 2013 FY were at arm's length. In 2014, FY, PPNL changed the testing method to Transactional Net Margin Method (TNMM) using Operating Margin (OM) as the profit level indicator. This according to PPNL was due to lack of information required for applying comparable uncontrolled price. While the FIRs agree with the change, it opted for Gross profit level indicator, albeit for the two years. This led to an additional assessment of N1.7 billion.

Hence, the issue whether the respondents (FIRs) action in benchmarking the Appellant's (PPNL) transfer pricing transaction with the transactional net margin method for 2013 and 2014 financial years was valid and is accordance with the Transfer pricing Regulations 2012 and the Organization for Economic Cooperation and Development (OECD)/United Nations Transfer Pricing Guidelines. The Tax Appeal Tribunal (TAT) held that the Appellant did not provide sufficient documentation to satisfactorily explain its use of different transfer pricing methods in 2013 and 2014 financial years. The Appellant had selected the comparable uncontrolled price method in 2013 financial year and the transactional net margin method in 2014 financial year. Essentially, TAT agreed with the position of the FIRs that the appellant had failed to discharge its burden of proof concerning the selection of transfer pricing methods for the relevant years. Furthermore, the TAT held that consistency in the application of methods from year to year is very important and fundamental. Thus, the transactional net margin method with the Gross profit margin as a profit level indicator was held as the most appropriate profit level indicator in this instance based on OECD Guidelines as explained by the Respondent.

From the foregoing, best practices concerning selection of transfer pricing methods involve a process that starts with a consideration of the respective strengths and weaknesses of the various transfer pricing methods by a detailed function, Asset and Risk (FAR) analysis[51]. This FAR analysis enables the tax payer to accurately characterize the related party transaction[52]. Accurate characterization of a controlled transaction will enable the tax payer to select an appropriate transfer pricing method for analyzing the controlled transaction. Finally, the tax payer is expected to consider the availability of information required to apply the method as well as the degree of comparability between the controlled and uncontrolled transactions[53]. Nonetheless, there are instances where more than one transfer pricing method may be considered appropriate in analyzing controlled transaction after following the transfer pricing method selection procedure. In such instances, the OECD Guidelines[54] and UN TP Manual[55] recommend the selection of the Most Appropriate Method (MAM) based on the information obtained from the selected procedure. However, the chosen transfer pricing method is generally expected to be applied consistently by the tax payer.

v) Transactional Profit Split Method

This is a method in which the division of profit and loss that a person achieves in a controlled transaction is compared with the division of profit and loss that would be achieved when participating in a comparable uncontrolled transaction[56].

9. Transfer Pricing Adjustment

An adjustment is made to the taxation of a transaction or transactions of a connected person resident in Nigeria by a competent authority of another country with which Nigeria has an agreement for the avoidance of double taxation and the adjustment results in taxation in that other country of income or profits that are also taxable in Nigeria[57]. The service may, upon request by the connected person, determine whether the adjustment is consistent with the arm's length principle and where it is determined to be consistent; the service may make a corresponding adjustment to the amount of tax charged in Nigeria on the income so as to avoid double taxation[58]. This is buttress

[50] TAT/LZ/CIT/015/2017. This case is the first Nigerian Judgment on transfer pricing and was decided on 19th February, 2020.
[51] Income Tax (Transfer pricing) regulations, 2018, Reg. 5(2).
[52] *Ibid*.
[53] *Ibid*.
[54] OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, 2017.
[55] United Nation Transfer Pricing Manual.
[56] Income Tax (Transfer Pricing) Regulations, 2018, Reg. 27.
[57] *Ibid*, regulation 10(1).
[58] *Ibi*d.

in *Canada V. Glaxosmithkline Co*[59], here, license and supply agreement was made in reference to patent rights of the parent company to its subsidiary (Glaxosmithkline Canada) in respent of a certain drug manufactured by the parent company. The court relying on OECD Transfer Pricing Guidelines held *inter alia* that the arm's length adjustments must be applied, irrespective and any contractual obligation of the parties and of any intention of the parties to avoid tax that the circumstances stated by the parent company for setting the terms of the license agreement with its subsidiary at a non-arm's length price were reasonable because transfer pricing is not an exact science[60]. Similarly, in *ABC (pty) Ltd v. Commissioner for the South African Revenue Service*[61].

In this case, the tax payer was involved in the automotive industry. Specifically, it procured Precious Group Metals (PGM) from a foreign connected person (Swiss Entity), which was then used in manufacturing of catalytic converters for exhaust systems, which were sold to third party customers in South Africa. The tax-payer did not have transfer pricing documentation in place to support the arm's length nature of the PGM purchases during the period under review, and SARs consequently performed its own analysis relying on an external database benchmarking search for the identification of independent comparable companies. SARs selected and applied the Transaction Net Margin Method relying on a Net Cost-Plus as the Profit Level Indicator (Full-Cost approach) and benchmarked the mark-up on total cost achieved by the tax payer against the comparable companies determined in the data base search. Based on this, SARs came to the conclusion that the tax payer's margin was between the minimum and the 25th percentile of the weighted average arm's length range achieved by the comparable companies. SARs therefore imposed a transfer pricing adjustment resulting in the tax payer's Net Cost-plus margin being increased to the median of the weighted average interquartile arm's length range determined.[62] From the foregoing, SARs is correct in applying the TNMM- Transactional Net Margin Method, as the best suitable method based on the information available. Further, the argument presented by the tax payer on the CUP appeared to be incomprehensive. It is also appropriate to place reliance on the OECD Transfer Pricing Guidelines in testing the arm's length nature of a transaction and when effecting a transfer pricing adjustment.

10. Transfer Pricing Declarations, Disclosures and Documentation

A connected person shall declare its relationship with all connected persons whether such persons are resident in Nigeria or elsewhere[63], and this declaration must be done in a manner prescribed by the services[64]. The transfer pricing declaration must be made and submitted to the Service not later than eighteen months after the date of incorporation or within six months after the of the accounting year, whichever is earlier.[65] Subsequently, each year of assessment, a connected person shall without notice or demand, make a disclosure of transactions that are subject to these Regulations[66].This disclosure shall be made and submitted to the Service not later than six months after the end of each accounting year or eighteen months after the date of incorporation, which is earlier.[67] In addition, a connected persons to maintain and furnish to the FIRS upon request, a written or electronic record of information and data to verify that the pricing of controlled transaction is consistent with the arm's length principle.[68] This document retained by a connected person shall be adequate to enable the Service verify that the controlled transaction is consistent with the arm's length principle.[69] Thus, this documentation retained by a taxable person shall be proof that the conditions of the controlled transactions are consistent with the arm's length principle.[70]

11. Legal Effect of Applying UN and OECD Documents

The UN Transfer Pricing Manual and OECD Transfer Pricing Guidelines shall be applied in a manner consistent with the arm's length principle.[71] Notwithstanding the above provision, it is also provided that where there is any inconsistency between the provisions of any applicable law, rules, regulations, the UN and OECD documents, the provisions of the relevant domestic tax laws shall prevail.[72] More so, the provisions of the FIRS (TP) Regulations will also prevail in any event of inconsistency with other regulatory authorities' approvals.[73]

[59] (2012) SCC 52.
[60] *Ibid.*
[61] (2021) (IT 14305) ZATC 1 (7 January, 2021).
[62] *Ibid*.
[63] Income Tax (Transfer Pricing) Regulations, 2018, reg. 13(1).
[64] *Ibid*, reg. 13 (2).
[65] *Ibid*.
[66] *Ibid*, reg. 14 (1).
[67] *Ibid*, reg.14 (3).
[68] *Ibid*, reg.16.
[69] *Ibid,* reg. 16(9).
[70] *Ibid,* reg.16 (10).
[71] *Ibid,* reg.18.
[72] *Ibid*, reg.19.
[73] *Ibid*, reg.19 (2).

12. Provisions of the Relevant Domestic Tax Laws under Consideration
The provisions of the domestic tax laws considered above as Supreme under the Regulations are the general anti –avoidance rules (GAAR) embedded in the various tax legislations. These shall be considered as follows;

Company income Tax Act (CITA)
Companies Income Tax Act is the principal legislation governing taxation of income of companies in Nigeria. The existing framework in relation to transfer pricing under Companies Income Tax Act as amended is found in sections 13(2) (d) and 22 CITA respectively. Section 13(2) (d) CITA illustrates the existence of the right to tax income of a non-resident person where there is an internal trading between associated or related persons and the terms of such trading are in the opinion of the Board to be artificial and fictitious.[74] A close reading of the above subsection shows that in order for a tax authority to make transfer pricing adjustments, the following elements must be present;

> 1. There must be a web of relationships and the element of control is crucial and such control be direct or indirect in nature or exercised through participation.[75] 2. The relationships involve impositions of conditions in relation to the commercial or financial capacity of the persons exercising the control. 3. Such conditions which impact on the profits of the company does not reflect open market prices.[76]

Section 22 (1) CITA further gives the Board the power to disregard dispositions or make appropriate adjustments where it is of opinion that any disposition[77] or transaction made by related parties which reduces or would reduce the amount of any tax payable is artificial or fictitious.[78] This section applies to both residents and non-residents. For the purpose of illustrating when a transaction is deemed to be artificial or fictitious, a combined reading of Sections 22(2) (b) and 13 (2) (d) CITA is pertinent. S.22 (2) (b), CITAS provides as follows: 'Such transactions between persons one of whom either has control over the other or, in the case of individuals who are related to each other or between persons shall be deemed to be artificial or fictitious if in the if in the opinion of the Board, those transactions have not been made on terms which has been expected to have been made by persons engaged in same or similar activities at arm's length'. With a view of assisting the Board in fulfilling its responsibility of determining the arm's length price as envisaged by the above section, two requirements come to mind; a) The tax authority is required to search for similar transactions or activities between independent parties with those transferred by group in question. b) The tax authority must also establish the price at which independent parties would charge for similar activities.[79] This provision places a burden on the tax authorities to search for comparable transactions or situations between independent parties before it can vividly undertake any transfer pricing adjustments prescribed in these sections.[80]

Personal Income Tax Act (PITA)
The Personal Income Tax Act is the principal statute governing the taxation of the income of individuals and other non-corporate entity. The relevant section of PITA in relation to transfer pricing is the general avoidance provision embedded in s. 17 PITA, which provides as follows:

> Where a tax authority is of opinion that any disposition is not in fact not in fact given effect or to that any transaction which reduces or the tax authority may disregard the disposition[81] or direct that such adjustments would reduce the amount of any tax payable is artificial or fictitious, shall be made as respects the income of an individual, executor or the trustee, as the tax authority considers appropriate so as to counteract the reduction of liability to tax effected, or reduction which would otherwise be effected by the transaction.

In effect, this section gives the tax authority powers to disregard or adjust the income of an individual where the transaction deemed to reduce his tax liability is artificial. Transactions between related persons shall be deemed to be artificial or fictitious if those transactions have not been made on terms which might fairly be expected by the Board to have been made by persons engaged in the same or similar activities dealing with one another at arm's length. This section further provides that in exercising the powers in subsection one above, where it appears that the interest of more than one tax authority are affected thereby, the power to make adjustments falls on relevant tax authority alone and any decision or direction of the relevant tax authority under this section shall be binding on tax authorities.[82]

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[74] J Arogundade, *Nigerian Income Tax and Its International Dimensions*,2nd (Ibadan, Spectrum Publishers Ltd, 2010) p471.
[75] *Ibid*, p472.
[76] *Ibid*.
[77] CITA 2007, s.22 (2).
[78] O Orojo, *Company Law and Practice in Nigeria, (*Lagos,Lexis Nexis, 2008) *Lexis p 542.*
[79] Arogundade, *op.cit*., p473.
[80] CITA 2007, s.s 13 (2) (d) and 22 (1).
[81] Disposition here includes any trust, grant, covenant, agreement or arrangement, s 17(3) (a) PITA.
[82] PITA, s.17 (2).

Petroleum Profits Tax Act (PPTA)

The principal Act governing the taxation of profits from petroleum in Nigeria is the Petroleum Profits Tax Act (PPTA) as amended.[83] Section 15 PPTA deals with artificial or fictitious transactions which is the focus of the discourse. The section provides thus:

> Where the Board is of the opinion that any disposition is not in fact given effect to or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, it may disregard any such disposition or direct that such adjustments shall be made as respects liability to tax as it considers appropriate so as to counteract the reduction liability to tax affected, or reduction which would otherwise be affected, by the transaction and any company concerned shall be assessable accordingly.[84]

From the foregoing, section 15 above is similar to section 22 CITA and section 17 PITA discussed earlier and such any explanations made under the examination of CITA and PITA provisions applies accordingly. An examination of s 13(2) (d) CITA, s 17 (3) (b) PITA and s 15 PPTA illustrates the importance of the element of control in relation to transfer pricing. The definitions of 'related or associated entities' in the three sections highlighted above are similar in the sense that they cover situations of direct and indirect control among corporate entities. However, the definition in s.15 (2) PPTA is restricted to corporate control. In examining the provisions, an explanation of the concept of control becomes necessary. Control is usually defined in relation to direct or indirect participation in capital, control and management.[85] In determining the circumstance which give rise to control, the case of *Irving v Tesco Stores*[86] becomes very illustrative. Here, the delegation of the general business of the company to the directors was held to be delegation of control to directors. In *Calcutta Jute Mills Co. v Nicholson*[87], company manufacturing jute in India and holding the board of directors meeting in the UK, was held to be controlled by the UK. An agent of a company resident in Canada was held not be in control of a business owned by a UK resident.[88] The importance of the element of control to transfer pricing is premised on the fact that control is exercised by the board of directors who take certain administrative decisions including authorizing transactions among related parties. The element of control is equally the yardstick for determining the arm's length price of a transaction for the purpose of comparison. A combined reading of s 17, PITA, s 15 PPTA and s 22, CITA explained earlier reveals that there are no specific provisions for transfer pricing methods in making transfer pricing adjustments where the respective internal transfer pricing arrangements of an affected company does not reflect open market prices. These provisions vested on the FIRS with wide and uncertain discretionary powers in relation to transfer pricing adjustments. From the foregoing, it is seen that the existing framework for transfer pricing in Nigeria prior to FIRS Transfer Pricing Regulations was not in line with internationally accepted standards and best practices.

13. Conclusion

Transfer Pricing Regulations by FIRS has the capacity to strengthen the existing anti general anti avoidance (GAAR) provisions in the Nigerian tax regime. This indeed is a positive step in the right direction in accordance with international developments and best practices. As observed in this paper, proper implementation of the regulations has numerous prospects including the likelihood of increasing tax revenue by wide margin in Nigeria. This in turn will increase foreign direct investment in Nigeria. Thus, it is recommended among others that is need to broaden the Nigerian double tax treaty network. For, an effective implementation of the regulations, the Nigeria's double tax treaty network ought to be expanded to accommodate major trading partners and also to take advantage of the corresponding adjustments embedded in the transfer pricing regulations.

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[83] Cap P13, LFN 2004.

[84] PPTA, .s 15 (1).

[85] Art. 9 (2), Organization for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. Retrieved from http://www.oecd.org/tax/treaties/1914467.pdf. Accessed 28 February, 2022.

[86] 1982 STC 881.

[87] 1876 1 TC 83.

[88] *Oglivie v Kitton* 1908 5 TC 338.