RE-EXAMINING THE CHARGEABLE GAINS ON CAPITAL GAINS TAX IN NIGERIA: FINANCE ACT 2021 IN PERSPECTIVE*

Abstract

Tax is a compulsory levy imposed by the government on the incomes of tax payers in order to pay the expenses of governance. Capital gains tax is the taxation levied on capital gains. A capital gain is the excess of the sales proceeds of asset such as building, land, stocks, bonds and qualifying machinery and equipment etc. over the original cost of that asset. Capital gains tax is a gain accruing from increase in the market value of assets to a person who does not habitually offer such item for sale and in whose hands they do not constitute stock in trade. The gain here, may be realized where the assets are sold or disposed of or proper gain where the assets appreciate in value while still in hands of the owner. Capital gains tax is chargeable at the rate of 10%. With the effect from the 1st January, 1998, stocks and shares ceased to be chargeable gains. Subsequently, the Finance Act of 2021, which took effect on 1st January, 2022, amended the Capital Gains Tax Act and reintroduced tax on stocks and shares as chargeable gains. The reintroduction of capital gains tax on share transactions, will affect the pricing conditions and the tax provisions in the sale and purchase agreement. This paper will re-examine the nature of capital gains, the effect of reintroduction of taxation on gains of stocks and shares and also, considers the tax treatment of shares and stocks in some selected jurisdictions. This paper recommends more sensitization on capital gains tax regime in Nigeria and the need to strengthen the administration of CGT to avoid revenue leakages.

Keywords: Capital Gains Tax Act, Chargeable gains, Shares, Assets, Disposal, Finance Act

1. Introduction

In Nigeria, there is a distinct tax on gains arising from disposal of capital assets known as Capital Gains Tax. Though, there has been a tax on income since the early 20th century, capital gains were not chargeable to tax till 1967. In 1967, the Capital Gains Tax Act (CGTA) was first introduced in Nigeria. The tax is on the Exclusive Legislative list of the Nigerian Constitution, hence, on the federal legislature (National Assembly) to validly legislate on it. Nonetheless, both Federal and State government are empowered to collect the said tax, as matters of collection are within the Concurrent Legislative list. While the Federal Inland Revenue Service (agent of tax administration of the federal government) is charged with the collection of the tax from corporate bodies and the State Boards of Internal Revenue (agent of tax administration of the State government) collects solely from individuals and unincorporated bodies. It is on record that the 1967 Capital Gains Tax Act imposed charge on shares and stocks, subsequently, the said Act was amended on 1st January, 1998 and tax liability was removed from gains on shares and stocks. By 2021, section 30 of the CGTA was amended by section 2 of the Finance Act, which reintroduces charge on shares and stocks again. This paper focuses on re-examining of the nature of capital gains tax, chargeable gains, the effect of reintroduction of charge on stocks and shares on foreign direct investment in Nigeria and also, the tax treatment of shares and stocks in some selected jurisdictions.

2. Nature of Capital Gains Tax

The scope of the capital gain tax legislation is for there to be a charge to tax, there must be a corresponding 'disposal' but the sum on which tax is charged is merely arithmetic difference. The sum to which the charge is made, is treated under the Capital Gains Tax Act as consideration. For liability to capital gains tax to arise, there must be a disposal of a type relevant to capital Gains Tax (CGT), it must be of an asset of a type relevant to CGT, again, it must be by a person chargeable to tax and finally, it must be an asset on which a chargeable gain is computed under the Act[1]. The scheme of the legislation is to distinguish a gain from a chargeable gain. It is only the later that is subjected to tax. The legislation does not specify how a gain should be computed. Rather, it specifies what costs can be deducted from the consideration. In the computation of any chargeable gains under the Act, such gains as may be chargeable to tax shall, subject to the provisions of this Act, be the difference between the consideration accruing to any person on a disposal of assets and sum to be excluded from that consideration, and there shall be added to that sum the amount of the value of any expenditure allowable to such person on such disposal by virtue of the Act.

Persons Chargeable to Capital Gains Tax

Under the Capital Gains Tax Act, the categories of persons chargeable to the above tax when they deal with chargeable assets are a). Companies throughout Nigeria, b) Persons to whom the income tax apply. The State

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[1] MT Abdulrazaq, *Revenue Law and Practice in Nigeria,* 3rd edn (Lagos; Malthouse Press Limited, 2015) p.159.

Boards of Internal Revenue assess individuals while the Federal Inland Revenue Service (FIRS) assesses companies[2].

Chargeable Assets

These are all assets not specifically exempted by the provisions of the Act. By virtue of section 3 of the Capital Gains Tax Act (CGTA), chargeable assets are assets whose disposal will result in chargeable gains. They include (a) Options, debts and incorporeal property generally, (b) Any currency other than Nigerian Currency; and (c) Any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired from the foregoing, only the assets mentioned above are subjected to the payment of tax on their disposal. From the foregoing, only the assets mentioned above are subjected to the payment of tax on their disposal.

Chargeable Gains

Chargeable gains are provided under section 6 of the CGTA. The section provides that subject to any exceptions provided by the Act, a disposal of assets occurs where any capital sum derived from a sale, lease, transfer, an assignment, a compulsory acquisition or another disposition of assets notwithstanding that no asset is acquired by the person paying the capital sum. Assets are said to be disposed where any capital sum is derived from a sale, lease, transfer, assignment etc. The disposal is deemed to have taken place even though the person paying such capital sum acquired no asset. Some examples, specifically mentioned is section 6[3] include

a. Capital sum derived by way of compensation or employment
b. Capital sums receive under a policy of insurance for the risk of any kind of damage or injury or the loss or depreciation of assets.
c. Capital sums received is return for future or surrender of rights or for refraining from exercising rights.
d. Capital sum received as consideration for use or exploitation of any assets; and
e. Capital sums received in connections with or arising by virtue of any trade, business, profession or vocation

It should be noted that though section 6 makes chargeable, sums derived from compulsory acquisitions, by section 9, such sums are exempted if the person acquiring the land did not have knowledge of the authority's acquisition of it and had taken steps to dispose of the land to the authority or others.

Exclusion of Losses

By virtue of section 5, CGTA, in computing the chargeable gains, the amount of any loss which accrues to a person on a disposal of any asset shall not be deductible from gains accruing to any persons on disposal of such asset. The provision of section 5, negates the principles of fairness or social justice as between the tax payer and the government[4]. The government should equally share in capital losses just as it share in capital gains. In fairness, capital losses or a part thereof should be allowed as set-off against capital gains or any other taxable income.

Exempted Bodies

Capital gains are not chargeable under section 26 CGTA, if it accrues to any of the following bodies;

a. Ecclesiastical, charitable or educational institutions of a public character
b. Any statutory or registered friendly society,
c. Co-operative societies under the co-operative societies law of any State,
d. Any trade union registered under the trade unions Act provided the gain is not derived from any disposal of any asset acquired in connection with any trade carried on by the institution,
e. Any local government council,
f. A purchasing authority company
g. Corporation established for fostering economic Capital Gains Tax Act development of any part of Nigeria.

From the foregoing, these bodies are exempted from the liability of capital gains tax, so far as their gains are not derived from any disposal of any assets acquired in connection with any trade or business carried on by them and the gains are in turn applied purely for the purpose of the institutions.

[2] JAA Agbonika, *Problems of Personal Income Tax in Nigeria* (Ibadan, Ababa Press Ltd, 2012) p. 143.
[3] Capital Gains Tax Act, CAP C1, LFN 2004.
[4] AK Ibigbami 'An Assessment of Capital Gains Tax in Nigeria' in O Akanle (ed*), Tax Law and Tax Administration in Nigeria, Nigerian Institute of Advanced Legal Studies* (Ibadan, Intec Printers Limited, 1991) p.213.

Exempted Gains

The following gains shall not be chargeable if they accrue,

a. To a person from disposal of investments of super annuation funds, under section 28,
b. To a person from his disposal of investments in statutory provident fund or retirement benefits scheme – section 28.
c. To any person on the disposal of decoration awarded for valour or gallant conduct otherwise than for consideration in money or money's worth –section 29.
d. From a disposal of an interest in life assurance policies or deferred annuity contracts other than disposal by purchases of such policies from the original beneficial owner for value – section 34.

3. Chargeability of Capital Gains Tax on Shares and Stocks Prior to Finance Act of 2021

The tax treatment of profits or gains made from the disposal of shares of any company in Nigeria or government stocks, bonds, or securities are re-examined here. It is pertinent to re-examine the position under the CGTA, 2004. Under the CGTA 2004, section 30, gains accruing to a person from a disposal by him of Nigerian government securities, stocks and shares shall not be chargeable gains under this Act. Similarly, shares of Nigerian companies were not chargeable as CGT under the CGTA 2004. Stocks and shares ceased to be chargeable gains in Nigeria with effect from 1st January, 1998. Thus, prior to the commencement of Finance Act in 2021, shares and stocks were not deemed as chargeable gains under the Act.

4. Chargeability of Capital Gains Tax on Shares and Stocks under the Finance Act of 2021

Section 2 of the Finance Act, 2021 amended section 30 of CGTA by substituting section 30 with a new section, to the effect that disposal of shares in any Nigerian company is now chargeable to CGT. Section 30-(1) Gains accruing to a person from a disposal by it of Nigerian government securities shall not be chargeable gains under this Act. (2) Without prejudice to any other applicable law, the gains accruing to a person on disposal of its shares in any Nigerian company registered under the Companies and Allied Matters Act shall be chargeable gains under this Act.

Capital gains tax at 10% is chargeable on the disposal of shares worth 100 million naira or above in any 12 consecutive months except to the extent that such proceed is reinvested in the shares of the same company or any Nigerian companies. However, GCT will not apply where: such proceeds from disposal are invested within the same tax year, to acquire shares in the same company or other Nigerian companies. CGT will apply proportionally on the portion of sale proceeds not reinvested.

- Aggregate disposal proceeds in any 12 consecutive months are less than 100 million naira, provided the person (s) renders appropriate returns to the Federal Inland Revenue Service
- Shares are transferred between an approved Borrower and Render in a regulated Securities Lending Transaction as defined in the Companies Income Tax Act.
- Also, gains on the disposal of Nigerian Government Securities should not be subject to CGT.

The reintroduction of CGT on disposal of share of a Nigerian company pursuant to the Finance Act 2021 is considered to an extent as a withdrawal of a major tax incentive, which could have direct negative effect on foreign direct investments in Nigeria. Presently, Nigeria has one of the relatively higher corporate income tax rates in the world at 30% (for companies with turnover of over more than 100 million) plus an additional 2.5% education tax, along with an increasing number of ear marked taxes and high cost of doing business. Thus, the recent imposition of CGT on disposal of shares could be dis-incentive to prospective foreign investors. Nonetheless, much as the government is desirous in improving its revenue collection to meet its overwhelming obligations, it is also pertinent to strike a balance between increased revenue in the short term and economic development which is majorly driven by investments.

5. Tax Treatment of Capital Gains on Shares and Stocks in Selected Jurisdictions

The tax treatment of capital gains on shares and stocks in Australia, United States of America and South Africa are examined here. This discussion is pertinent as Nigeria just recently imposed charge on gains accruing from disposal of shares and stocks. It is also pertinent to examine the above mentioned jurisdictions to determine whether they impose charge on gains from disposal of shares and stocks and the parameters for such imposition. These jurisdictions shall be examined *seriatim;*

Australia

Capital gain is the increase in value of a capital asset of any brokerage or other transaction costs[5]. An asset that declines in value is said to have a capital loss. In Australia, just as in most countries that tax capital gains,

[5] L Burmah 'Taxing Capital Gains in Australia: Assessment and Recommendations', available on https://www.urban.org, accessed on 12 August, 2022.

capital gains and losses are only realized for tax purposes when an asset is sold. Losses are deductible against capital gains, but net capital losses (losses in excess of capital gain) are not deductible against other income. Instead, they may be carried over indefinitely and deducted against future capital gains[6]. Unlike Nigeria, there is no consideration for losses in computing capital gains of an asset, as seen under section 5 CGTA. Capital gains tax is chargeable on shares and stocks in Australia, just as in Nigeria. Though, they differ in rates chargeable. The amount of CGT payable on shares here can vary depending on long the investment was held. If the asset was held for less than 12 months, then the CGT is charged at 100% of the capital gain of the tax payer's income tax rate[7]. If the asset was held for longer than 12 months, the rate payable will be at 50% of the capital gain[8]. When an asset that is subject to capital gains tax is disposed, it is regarded as CGT event. The CGT event marks the point in time at which a capital gain is made or loss is incurred[9]. A CGT event may also occur when an investor holds shares in a company and receive a payment from the company other than a dividend to you as a shareholder; and the company is placed under administration or is liquidated and declares that the shares are worthless; and the shares are cancelled because the company is wound up. Similarly, if a tax payer hold shares in a managed fund the fund makes a distribution amount to capital gain that will amount to capital gains tax event. According to Australian Tax Office (ATO), if a person carries out business activities to earn an income from buying and selling shares, then he is considered a share trader.[10] Knowing the difference between selling shares as investor and trading shares as a business will determine the capital gains tax liability of each transaction. If the tax payer is a share investor and sell shares for a profit, for that sale will be considered a CGT event, and that investment income will be considered a capital gain. However, if a tax payer trade in shares as a business, the business will be taxed, and capital gains on shares does not apply[11]. Nonetheless, investor will have to consider the taxes they will have to pay on their shares when making investment decisions, as this could impact could impact on overall returns. Dividend and capital gains taxes are calculated differently and as well as their tax liabilities.

United States of America

Capital gains tax is the tax payable on profits generated on profits from the sale of assets, including stocks, real estate and businesses. The Internal Revenue Service (IRS) generally considers these gains as taxable income. The rates on capital gains vary depending on the income of the tax payer and the length of time the investor has held the asset before selling[12]. Capital gains from assets that was held for longer than one year are considered long-term capital gains and are taxed at a lower rate than short-term gains on assets held less than a year. Capital gains are profits generated by selling assets such as a business, real estate, cars, boats, stocks or bonds. The IRS considers the sale of these types of assets as a taxable event[13]. Any taxable event must be reported to IRS on the tax payer's income form. An asset's cost basis is typically the amount the owner paid for the asset when it when it was purchased. If the owner sells the asset for more than its cost basis, a capital gain is generated. Assets sold for less than their cost produce a capital loss[14].

Capital gains tax is chargeable on shares and stocks here. Any investor that buys and sells stocks, bonds or other assets owes capital gains tax on the profits from investments. However, unlike Property taxes that are paid each year the property is owned, capital gains tax is determined based on several factors, including the duration the asset was owned, the cost of buying and owning the asset, the income tax bracket and marital status.[15] In determining the rate chargeable as CGT on shares, will depend on the duration of the investment. If the shares are held for more than one year, the gain from these investments will be taxed at a long-term capital gains tax rate of 0%, 15% or 20%. On the other hand, if the shares are held for less than one year, the gain from these investments will be treated as normal income and will be taxed according to the tax payer's income bracket[16]. A short-term capital gain results from the sale of asset owned for less than one year and do not benefit from any special tax rates, they are subject to taxation as ordinary income. While long-term capital gains are generally

[6] ibid.
[7] Capital Gains Tax- Australian Tax Office, available on https://www.ato.gov.au>individuals>capital-gains-tax-, accessed on 12 August, 2022.
[8] ibid.
[9] ibid.
[10] ibid.
[11] ibid.
[12] Topic No. 409 Capital Gains and Losses, Internal Revenue Service, available on https://www.irs.gov>taxtopics, accessed on 13 August, 2022.
[13] ibid.
[14] How are Capital Gains Taxed? – Tax Policy Center, available on https://www.taxpolicycenter.org, accessed on 13 August, 2022.
[15] ibid.
[16] Tax Cuts and Jobs Act, (TCJA) 2017.

taxed at a more favorable rate than salary or wages. The tax on a long-term capital is almost always lower than if the asset is sold, since there are taxed at a more favorable rate than short-term capital gains, hence, capital gains tax is minimized by holding the asset for a year or more. Remarkably, under the American capital gains tax regime, there is a consideration for losses in computing chargeable gains as against the Nigerian situation, where such losses are not taken into consideration in computing gains chargeable. Here, any capital losses generated in a given tax year can be used to offset capital gains and reduce the overall burden. Capital losses are first used to offset capital gains of the same type, with short-term losses offsetting short-term gains and long-term losses offsetting long-term gains. The remaining net losses of either type can be used to offset gains of other types[17].

South Africa

Capital gains tax (CGT) is not a separate tax but forms part of income tax. A capital gains arises when an asset is disposed on or after 1st October, 2001 for proceeds that its base cost. The relevant legislation is contained in the Eight Schedule to the Income Tax Act 58 of 1962. Capital gains are taxed at a lower effective rate than ordinary income. Pre 1st October, 2001, CGT, capital gains and losses are not taken into account. Not all assets attract CGT and certain capital gains and losses are disregarded[18]. CGT applies to individuals, trusts and companies. A resident as defined in the Income Tax Act 58 of 1962, is liable for CGT on assets located both in and outside South Africa. A non-resident is liable to CGT only on immovable property in South Africa or assets of a 'Permanent Establishment' in South Africa[19]. Shares can be held on capital account, that is long-term investment or as part of a scheme of profit making, such shares are essentially treated as a tax payer's trading stock. On disposal of shares, the amount received by the taxpayer would be taxed as normal income at the rate applicable to a tax payer's income. In the case of individuals, this is 40%, if the person is taxed at the minimum scale of the tax rates or 28% in the case of a company. The cost incurred by the tax payer to acquire such shares would normally be deductible from this income, similar to the cost of any other trading stock sold[20]. If on the other hand, the shares are held as capital assets, any gain on the disposal of the shares will be subject to capital gains tax. This capital gain is calculated as the amount received (proceeds) less any costs to acquire the shares. Company, this gain is taxed at 66.6% of the company's normal 28% rate[21] . This difference in rates explains why tax payers tend to lean towards the view that the shares were held on capital account, while tax authorities may often be doubtful about this position. In this regard, it is important to note that the burden of proving the nature of the shareholding sold is solely on the tax payer, if the view is held that the shares are held as capital account.

Nature of Shareholding

If a tax payer acquired a share with the intention to make a profit from this share transaction in a manner in which a trader would (that is, holding until the market price increases sufficiently to sell), this share would be utilized in a scheme of profit making and would constitute a trading stock.[22] If however, the tax payer acquired the share to hold as part of his or her income earning structure, the share will be a capital asset. A share can be held as part of the income earning structure, if a tax payer intends to receive dividends from the share, has an interest in the underlying value and business of the share or merely wishes to gain from the long-term appreciation of the share price[23]. The nature of the shareholding in the hands of the tax payer is determined by the tax payer's intention with the shares. This intention is based on subjective intention of the tax payer, but it is well established principle that it must be supported by objective evidence. Here, objective evidence includes the period of time for which the asset is held, as well as surrounding circumstances that could support or cast doubt upon the stated intention of a tax payer. In the case of *CSARS v Capstone556 (Pty) Ltd*[24]*,* here, the tax payer company acquired shares in the JD Group, a group of entities involved in the furniture industry. This acquisition took place on 5 December, 2003, following a period of negotiations and meeting the relevant regulatory requirements such as obtaining permission from the Competition Commission for the transaction. The agreement for acquisition of the shares had a 21 June, 2002 effective date. The tax payer company attempted to secure financing for the acquisition of the JD Group shares for a period of 3 to 5 years, but such funding was not available, and it had to settle for short-term funding. Subsequently, there was a boom in the furniture industry,

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[17] n 13.

[18] Capital Gains Tax in South Africa- South African Revenue Service, available on https://www.sars.gov.za/types-of-tax/capital-gains-tax,accessed on 13 August, 2022.

[19] ibid.

[20] ibid.

[21] ibid.

[22]Tax Implications of Share Transactions-Wall rich, available on https://www. Wallrich.co-za/index.php/8-newsletter-articles/97-tax-implications-of-share-transactions, accessed on 14 August, 2022.

[23] ibid.

[24] [2016] ZASCA 2(*Capital v revenue*).

which led to substantial increase in the price of the JD Group shares. The tax payer company utilizing the opportunity decided to sell the JD Group shares. This sale transaction took place within five months after shares were acquired by Capstone. The South African Revenue Service (SARS) viewed the short period for which the shares were owned by the tax payer as decisive and accordingly taxed the amount received on the disposal as being income. The Tax Court upheld the view of SARS. The high court judgment indicated that if all of the surrounding circumstances are considered, the shares were acquired for strategic reasons with the intention to hold for a relatively long period of time. The sale was merely an advantageous realization of a capital asset when an opportunity arose, which does not change the nature of the assets. Accordingly, it was held that the proceeds received on the sale of shares must be subject to capital gains tax, as opposed to being taxed as income. Subsequently, SARS not satisfied with the decision of the high court, appealed to the Supreme Court of Appeal (SCA). The SCA therefore, found the primary purpose of the acquisition of the shares was to rescue a major business in the retail furniture industry by long-term investment of capital and that it was consistent with an investment of a capital nature that was realized sooner than initially expected because of skilled management and favorable economic circumstances. Tax payers often structure their affairs through companies where they are shareholders. When such arrangement is in place, when their investment is realized, the tax treatment of such disposal will be deemed to be a capital asset.

6. Conclusion and Recommendations

The objective of the CGT is the same as other taxes, which is basically to raise revenue required to fund government's expenditure. Over the years, the government has intensified efforts to improve on non-oil revenue generation by exploring other sectors of the economy. This in turn has resulted in the amendments of various tax laws by Finance Act of 2019, 2020 and 2021 respectively, in a bid to reduce all possible revenue leakages and providing flexible compliance and administration. In Nigeria, Capital Gains Tax no doubt, is yet to yield the desired revenue for the government. Nevertheless, there has been a paradigm shift in the applicable rules for charging capital gains tax on the proceeds of transfer or disposal of shares and stocks in Nigeria. Individual and corporate investors are now at liberty to determine the type of shares to invest and how best to plan their tax affairs for maximizing the proceeds from such investment either in the short or long term. Having examined other jurisdictions, it is observed that they have well-structured tax administration of CGT as opposed to what we have in Nigeria. In other jurisdictions, while computing chargeable gains, there are due considerations given to capital losses and earmarked scheme for offsetting the capital losses, whether it is a long-term or short-term investment. In the jurisdictions x-rayed, they demarcated between long-term or short-term investments for basis of imposition of charge on CGT. Hence, different rates apply to long-term or short-term investments. Though, under Nigerian CGT regime, it did not demarcate between long-term or short-term investments, but the investment in shares of 100 million naira or above, presupposes that the investment will be long-term. Here, only a single rate is applicable to both investments in shares or other capital assets. Nevertheless, reintroduction CGT on shares and stocks will no doubt, provide additional desired revenue to the government. It is therefore recommended that the administration of CGT be strengthened to avoid revenue leakages. Also, the government will adopt the most effective scheme of managing their tax affairs to avoid dis- incentive effect to prospective foreign or local investors. The government can also amend section 5 of CGTA, by giving due consideration to capital losses incurred by tax payer as it is not in every disposal of capital asset, that results in capital gain. In all, the Nigerian Revenue authorities need to observe the tax treatment of CGT in Australia, United States and South Africa in a bid to enhance their own practice.