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UNDERSTANDING THE IMPACTS OF GLOBAL TRANSFER PRICING PRINCIPLES AND PRACTICES, BASE EROSION AND PROFIT SHIFTING (BEPS) ON TRANSFER PRICING REGULATION IN NIGERIA

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INTRODUCTION

Transfer pricing, a pivotal element in the arena of international taxation, refers to the pricing of goods, services, and intangibles between related parties across borders. This practice, while legitimate, has been subject to scrutiny due to its potential for tax avoidance by multinational Co-operations (MNCs). The importance of transfer pricing lies in its impact on where and how much tax is paid, significantly affecting countries' tax revenues. In the Nigerian context as a developing economy with a growing presence of MNCs, transfer pricing is not just a tax matter but a critical issue affecting fiscal policy.

The complexity of transfer pricing arises from the subjective nature of the 'arm's length principle,' which is the cornerstone of transfer pricing rules. This principle requires that transactions between related parties be conducted as if they were between independent entities, ensuring that transfer prices are not manipulated for tax advantages . However, the application of this principle is challenging, especially in countries like Nigeria, where market data for comparability may not be readily available or easily ascertained.

In Nigeria, the relevance of transfer pricing and international tax compliance is underscored by the government's efforts to maximize tax revenue in a challenging economic environment. The country has shown

[1]Braithwaite, J. (2020). The Arm's Length Principle and International Transfer Pricing. Journal of International Commerce, Economics and Policy, 11(1), 2050005.

significant proactiveness in updating its transfer pricing regulations, by aligning them with international best practices to curb tax avoidance and ensure fair taxation of MNCs.

THE DEVELOPMENT OF THE BEPS PROJECT

The international tax compliance landscape has been evolving rapidly, especially with the initiatives of organizations like the Organization for Economic Cooperation and Development (OECD) and G20, focusing on Base Erosion and Profit Shifting (BEPS). [2] The BEPS project is one of the key initiatives introduced by the OECD and G20 in 2015, involving a 15-point action plan to combat tax avoidance strategies that exploit gaps and mismatches in tax rules and has significant implications for transfer pricing practices globally. The need to boost government revenues in the light of the recent global financial crisis was key amongst other reasons for this action.

Base Erosion and Profit Shifting (BEPS) refers to tax planning strategies that exploit gaps and mismatches in tax rules across borders to artificially reduce tax base or shift profits to low or no-tax locations where there is little or no economic activity. The OECD estimates that over the years, this has resulted in reduced overall corporate tax paid by Multinationals and an annual loss of tax revenues of between USD 100 to USD 240 billion.

Although initiated by members of the OECD/G20, the BEPS project has been followed very closely by many African tax authorities. The African Tax Administrator's Forum (ATAF) and its members (including Nigeria) were involved in the project through various committees. With the release of the final BEPS recommendations, many African countries, as expected, put efforts on aligning and implementing the recommendations. [3]

These developments proved crucial for countries like Nigeria, which are working to optimize their tax collection from MNCs operating within their jurisdiction while aligning with international standards. [4] Hence, Nigeria's immediate alignment with the OECD recommendations became evident in the policy changes introduced by the Income Tax (Transfer Pricing) Regulations 2018, which reflects a commitment to the United Nation's (UN) Manual on Transfer Pricing, OECD's Transfer Pricing Principles, BEPS project and Documents. [5]

[2] Adediran, S. A., & Alade, M. O. (2019). Transfer Pricing in Emerging Economies: A Case Study of Nigeria. International Tax Review, 31(2), 156-162.
[3] https://pwcnigeria.typepad.com/tax_matters_nigeria/2015/10/the-global-tax-landscape-is-changing-how-will-the-new-oecd-beps-action-plans-affect-you.html
[4] Adegoke, Y. (2021). Transfer Pricing in Nigeria: Policy, Practice, and Procedure. Journal of African Law, 65(1), 145-167.
[5] Chinwuba, O., & Amahalu, N. (2019). Transfer Pricing Regulations and Foreign Direct Investment in Nigeria. Journal of International Business and Law, 18(2), 324-340.

DEVELOPMENT OF TRANSFER PRICING REGULATION AND BEPS RECOGNITION IN NIGERIA.

In the Nigerian context, the development of transfer pricing regulations is relatively recent. Before the establishment of specific regulations, transfer pricing issues were handled under general anti-avoidance rules within the Nigerian tax laws. It was not until 2012 that Nigeria introduced its first comprehensive transfer pricing regulations, signaling a significant shift in its approach to the taxation of multinational enterprises (MNEs).

The 2012 Regulations, primarily focused on providing a framework for the application of the arm's length principle in Nigeria. However, recognizing the need for more robust rules, Nigeria revised these Regulations in 2018, introducing a new era of stricter documentation requirements and penalties for non-compliance principally anchored on the legal frameworks of the **Income Tax (Transfer Pricing) Regulations 2018** and the **Income Tax (Country-By-Country Reporting) Regulations, 2018**. However, we note that in a decision of the Tax Appeal Tribunal (TAT), Lagos Division delivered on 17th August 2023, in the appeal case of Checkpoint Software Technologies B.V. Ltd. v FIRS, the Tribunal ruled that the CbCR Regulation, 2018 is void and unconstitutional because the FIRS board which purportedly made the Regulation as empowered by the law, was not in existence as of the time the Regulation was made, having ceased to exist since 2012 and was not reconstituted until 2020.

As it stands, the current **Income Tax (Transfer Pricing) Regulations, 2018**, having not been voided, serves as the major transfer pricing framework in Nigeria, and Nigeria’s boldest step towards aligning the country's transfer pricing rules with international standards (although the quashing of the CbCR Regulation 2018 questions the credibility of the TP Regulations made at same time too). This revision was a direct response to the challenges encountered in the initial years of implementing the 2012 Regulations and the global shift towards more stringent transfer pricing compliance following the OECD's BEPS project. The Nigerian case also highlights the influence of economic sectors on transfer pricing regulations.[6]

Furthermore, the country's significant reliance on the oil and gas sector, which involves complex international transactions, also necessitated specific considerations in its transfer pricing regime. This sector specific approach is evident in the way Nigeria has tailored its regulations to address the unique challenges posed by the transfer pricing issues arising in transactions within the energy and natural resources sector.

[6] Federal Inland Revenue Service [FIRS]. (2012). Nigeria Transfer Pricing Regulations 2012.

The current Regulations on transfer pricing in Nigeria is anchored on the cardinal principle of ensuring that transactions between related entities reflect the arm's length standard. This standard, widely accepted in international tax and transfer pricing rules, requires that the terms and conditions of transactions between related parties are consistent with those that would have prevailed had the parties been independent entities dealing at arm's length. The application of this principle is crucial for preventing tax base erosion and profit shifting (BEPS) which are common concerns in multinational operations.

Also, accepted methods of transfer pricing in Nigeria are largely in line with OECD guidelines. These methods include the Comparable Uncontrolled Price (CUP) method, the Resale Price Method (RPM), the Cost-Plus Method (CPM), the Transactional Net Margin Method (TNMM), and the Profit Split Method (PSM). Each of these methods has its advantages and limitations, and the choice of method depends on the nature of the transaction and the availability of reliable data for comparability. However, the applicability of these methods in the Nigerian context, particularly in sectors where comparability is scarce, poses significant challenges. [7]

IMPACT OF BEPS AND NIGERIA'S RESPONSE

The BEPS strategy which exploits gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations has impacted adversely on the economy of many nations, Nigeria inclusive. Hence, OECD's BEPS initiative has been a key global response to this challenge posed by BEPS, stemming from the digitization of the economy and globalization. Nigeria, recognizing the importance of this initiative, has been active in implementing several of the BEPS action points. This commitment is reflected in the amendments to its tax laws and the introduction of new regulations aimed at curbing profit shifting and tax avoidance by multinational enterprises.[8]

Furthermore, Nigeria's involvement in international organizations, such as the United Nations (UN) and constant adoption and application of OECD's recommendations on transfer pricing and the BEPS project, highlights its dedication to being a part of the global conversation on tax matters. The bold steps taken by Nigeria in this regard has afforded her the opportunity to contribute to and learn from global best practices in tax policy and administration. [9]

[7]OECD. (2020). Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2020. OECD Publishing.
[8]Ikpefan, O. A., & Achugamonu, U. B. (2019). The Impact of BEPS on Transfer Pricing and Tax Practices: A Nigerian Perspective. European Journal of Accounting, Auditing and Finance Research, 7(4), 1-18.
[9]OECD/G20. (2020). Base Erosion and Profit Shifting Project: Outcomes and Impacts. OECD/G20.

However, aligning with these international standards does not come without its challenges. One of the primary challenges that Nigeria faces is the legal and administrative hurdles involved in implementing these standards. The process of amending existing laws and regulations to conform to BEPS actions and other international norms is complex and often time-consuming. This complexity is compounded by the need to ensure that these changes are compatible with domestic legal frameworks and economic policies. [10]

In addition to legal challenges, Nigeria also grapples with capacity and resource constraints in its quest to adhere to international tax standards. Implementing BEPS actions, for instance, requires a high level of expertise in international taxation, as well as adequate technological and administrative resources.

To this end, the Federal Inland Revenue Service (FIRS) plays a central role in administering, enforcing transfer pricing regulations and implementing BEPS actions in Nigeria. Its responsibilities include conducting transfer pricing audits, ensuring compliance with documentation requirements, and resolving disputes related to transfer pricing adjustments. The FIRS has been actively building its capacity to handle the complexities of transfer pricing and BEPS impacts, though challenges remain in terms of technology, expertise, and other necessary resources.

Moreover, the debate has lingered on the balance between adopting international standards and considering local economic realities. Critics argue that while alignment with global standards is important, it is equally crucial to tailor these standards to fit Nigeria's unique economic and business environment. For instance, some of the BEPS actions may not be directly applicable or may require adaptation to be effective in the Nigerian context.

The potential impact on foreign investment is also a concern. Stricter tax/transfer pricing regulations and compliance requirements, though necessary for fair taxation, could be perceived as a deterrent to foreign investors, especially for a developing economy like Nigeria, which seeks to attract foreign investment for economic growth. [11]

[11]Ikpefan, O. A., & Achugamonu, U. B. (2019). The Impact of BEPS on Transfer Pricing and Tax Practices: A Nigerian Perspective. European Journal of Accounting, Auditing and Finance Research, 7(4), 1-18.

CONCLUSION

In conclusion, the developments in Nigeria's transfer pricing Regulations particularly as it relates to tackling BEPS impacts, demonstrate her commitment to aligning with global tax best practices and the fight against tax avoidance. [12] However, the journey is fraught with challenges, including legal and administrative hurdles, capacity constraints, and the need to balance global norms with local economic realities.

As Nigeria continues to grapple with these challenges, it is hoped that the ongoing development and refinement of Nigeria’s fiscal system will be intentional about achieving balanced domestic and international tax compliance objectives, and an investment friendly economy.

[12] Olarewaju, O. M., & Akintoye, I. R. (2018). Critical Issues in Transfer Pricing and Natural Resources in Nigeria. Journal of Financial Crime, 25(4), 1064-1078.

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